

HSBC MEXICO, S. A.
Institución de Banca Múltiple, Grupo Financiero HSBC
AND SUBSIDIARIES

Consolidated Financial Statements

December 31, 2013 and 2012

(With Independent Auditors' Report Thereon)

(Translation from Spanish Language Original)



Independent Auditors' Report

(Translation from Spanish language original)

The Board of Directors and Stockholders
HSBC México, S. A., Institución de Banca Múltiple,
Grupo Financiero HSBC and Subsidiaries:

(Millions of pesos)

We have audited the accompanying consolidated financial statements of HSBC México, S. A., Institución de Banca Múltiple, Grupo Financiero HSBC and Subsidiaries (the Bank), which comprise the consolidated balance sheets as at December 31, 2013 and 2012 and the consolidated statements of income, changes in stockholders' equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and presentation of these consolidated financial statements in accordance with the accounting criteria for credit institutions in México, established by the National Banking and Securities Commission (the Banking Commission), and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Bank's preparation and presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

(Continued)

Opinion

In our opinion, the consolidated financial statements of HSBC México, S. A., Institución de Banca Múltiple, Grupo Financiero HSBC and subsidiaries for the years ended December 31, 2013 and 2012 have been prepared, in all material respects, in accordance with the accounting criteria for credit institutions in Mexico issued by the Banking Commission.

Emphasis of Matter

Without qualifying our opinion, we draw attention to the following:

As discussed in note 4 to the accompanying consolidated financial statements, during the year ended December 31, 2013, the Banking Commission issued modifications to the general provisions applicable to credit institutions in Mexico (the Provisions), which amend the methodology for the determination of preventive commercial loan loss reserves. The Bank applied these changes from June 2013 and in accordance with the Provisions, recognized a debit to "Retained earnings" of \$799 (\$559 net of deferred taxes).

KPMG CARDENAS DOSAL, S. C.

SIGNATURE

Hermes Castañón Guzmán

February 12, 2014.

HSBC MEXICO, S. A.
Institución de Banca Múltiple, Grupo Financiero HSBC
AND SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2013 and 2012

(Millions of pesos)

Assets	2013	2012	Liabilities and Stockholders' Equity	2013	2012
Cash and cash equivalents (note 6)	\$ 55,407	55,846	Deposit funding (note 18):		
Margin accounts (note 7)	-	53	Demand deposits	\$ 178,358	187,271
Investment securities (note 8):			Time deposits:		
Trading	51,121	36,338	General public (note 18)	103,414	104,358
Available-for-sale	96,081	97,184	Bank bonds (note 19)	6,036	4,244
Held-to-maturity	6,253	6,481		<u>287,808</u>	<u>295,873</u>
	<u>153,455</u>	<u>140,003</u>	Due to banks and other institutions		
Debtors under agreements to resell (note 9)	500	7,706	(notes 12c and 20):		
Derivatives (note 11):			On demand	2,900	1,980
Trading	49,601	43,312	Short-term	15,466	19,140
Hedging	168	37	Long-term	2,144	1,607
	<u>49,769</u>	<u>43,349</u>		<u>20,510</u>	<u>22,727</u>
Current loan portfolio (note 12):			Creditors under agreements to repurchase (note 9)	34,765	20,729
Commercial loans:					
Commercial activity	108,207	109,164	Collateral sold or pledged as guarantee:		
Financial institutions	4,339	4,823	Securities lending (note 10)	9,076	3,888
Government entities	18,133	28,107	Derivatives (note 11):		
Consumer loans	37,675	33,585	Trading	46,853	39,818
Residential mortgages	24,480	19,287	Hedging	790	1,103
Total current loan portfolio	<u>192,834</u>	<u>194,966</u>		<u>47,643</u>	<u>40,921</u>
Past due loan portfolio (note 12):			Other accounts payable:		
Commercial loans:			Income tax and employee statutory		
Commercial activity	9,617	2,072	profit sharing (note 24)	916	746
Financial institutions	3	3	Settlement transactions (note 13)	37,519	29,556
Government institutions	45	-	Sundry creditors and other accounts		
Consumer loans	1,788	1,302	payable (note 21)	14,966	17,511
Residential mortgages	703	636		<u>53,401</u>	<u>47,813</u>
Total past due loan portfolio	<u>12,156</u>	<u>4,013</u>	Subordinated debt issued (note 23)	9,463	10,196
Total loan portfolio	<u>204,990</u>	<u>198,979</u>	Deferred credits	601	526
Less:				<u>10,064</u>	<u>10,722</u>
Allowance for loan losses (note 12c)	12,223	9,381	Total liabilities	463,267	442,673
Loan portfolio, net	192,767	189,598	Stockholders' equity (note 25):		
Benefits receivable on securitization			Paid-in capital:		
transactions (note 12c)	182	155	Capital stock	5,680	5,261
Other accounts receivable, net (note 13)	40,293	31,972	Additional paid-in capital	27,088	22,357
Foreclosed assets, net (note 14)	159	218		<u>32,768</u>	<u>27,618</u>
Property, furniture and equipment, net			Earned capital:		
(note 15)	6,927	7,207	Statutory reserves	10,773	10,373
Permanent investments in shares			Retained earnings (deficit)	1,436	(202)
(note 16)	148	139	Unrealized gain from valuation of		
Deferred taxes (note 24)	7,624	6,138	available-for-sale securities	290	902
Long-term assets available for sale	5	-	Mark to market from cashflow hedges	(9)	(103)
Other assets, deferred charges and intangible			Subsidiary dilution effect	200	200
assets (notes 17 and 21)	3,637	3,076	Net income	2,146	3,997
	<u>510,873</u>	<u>485,460</u>		<u>14,836</u>	<u>15,167</u>
Total assets	\$ 510,873	485,460	Non-controlling interest	2	2
			Total stockholders' equity	47,606	42,787
			Commitments and contingent liabilities (note 29)		
			Total liabilities and stockholders' equity	\$ 510,873	485,460

(Continued)

HSBC MEXICO, S. A.
 Institución de Banca Múltiple, Grupo Financiero HSBC
AND SUBSIDIARIES

Consolidated Balance Sheets, continued

December 31, 2013 and 2012

(Millions of pesos)

Memorandum accounts

	<u>2013</u>	<u>2012</u>
Guarantees issued (notes 12 and 27a)	\$ -	4
Irrevocable lines of credit (notes 12 and 27a)	25,561	25,222
Assets in trust or under mandate (note 27b)	439,469	402,770
Assets in custody or under management (note 27d)	378,679	365,995
Collaterals received by the entity (note 8)	17,291	48,967
Collaterals received by the entity and sold or pledged in guarantee (note 8)	16,583	43,200
Investment banking transactions on behalf of customers, net (note 27c)	50,353	49,446
Uncollected interest accrued in respect of overdue credit portfolio (note 12b)	221	113
Amounts under derivative instruments	2,771,506	3,060,163
Loan portfolio rated (note 12)	230,551	224,205
Other memorandum accounts	316,563	322,039

See accompanying notes to the consolidated financial statements.

At December 31, 2013, capitalization index for credit and total risks (unaudited) amount to 22.26% and 14.81%, respectively (22.36% and 14.51%, respectively, at December 31, 2012).

"These consolidated balance sheets were prepared in accordance with the accounting criteria for credit institutions issued by the National Banking and Securities Commission pursuant on Articles 99, 101 and 102 of the Law for Credit Institutions, which are of general and mandatory nature. Accordingly, these reflect the transactions carried out by HSBC through the dates noted above. Furthermore, these transactions were carried out and valued in accordance with sound banking practices and the applicable legal and administrative provisions."

"These consolidated balance sheets were approved by the Board of Directors under the responsibility of the undersigned officers."

SIGNATURE

 Luis Peña Kegel
 Chief Executive Officer

SIGNATURE

 Gustavo Ignacio Méndez Narváez
 Chief Financial Officer

SIGNATURE

 Ngar Yee Louie
 Director of Internal Audit

SIGNATURE

 Juan José Cadena Orozco
 Chief Accountant

HSBC MEXICO, S. A.
 Institución de Banca Múltiple, Grupo Financiero HSBC
AND SUBSIDIARIES

Consolidated Statements of Income

Years ended December 31, 2013 and 2012

(Millions of pesos)

	<u>2013</u>	<u>2012</u>
Interest income (note 28a)	\$ 28,993	31,347
Interest expense (note 28a)	<u>(8,255)</u>	<u>(11,117)</u>
Financial margin	20,738	20,230
Allowance for loan losses (note 12d)	<u>(8,086)</u>	<u>(5,534)</u>
Financial margin net of allowance for loan losses	12,652	14,696
Commission and fee income (note 12c)	8,358	8,014
Commission and fee expense	(1,810)	(1,794)
Financial intermediation income (note 28b)	2,273	2,686
Other operating income, net (note 28c)	2,808	4,116
Administrative and promotional expenses	<u>(21,573)</u>	<u>(22,343)</u>
Net operating income	2,708	5,375
Equity in the results of associated and affiliated companies, net (note 16)	<u>43</u>	<u>35</u>
Income before income taxes	2,751	5,410
Current income taxes (note 24)	(1,677)	(1,324)
Deferred income tax (note 24)	<u>1,073</u>	<u>(89)</u>
Income before non-controlling interest	2,147	3,997
Non-controlling interest	<u>(1)</u>	<u>-</u>
Net income	<u>\$ 2,146</u>	<u>3,997</u>

See accompanying notes to the consolidated financial statements.

"These consolidated statements of income have been prepared in accordance with the accounting criteria for credit institutions issued by the National Banking and Securities Commission pursuant to Articles 99, 101 and 102 of the Law for Credit Institutions, which are of general and mandatory nature. Accordingly, these reflect all revenues and expenses derived from HSBC's operations during the periods noted above. Furthermore, these transactions were carried out and valued in accordance with sound banking practices and the applicable legal and administrative provisions."

"These consolidated statements of income were approved by the Board of Directors under the responsibility of the undersigned officers".

SIGNATURE

 Luis Peña Kegel
 Chief Executive Officer

SIGNATURE

 Gustavo Ignacio Méndez Narváez
 Chief Financial Officer

SIGNATURE

 Ngar Yee Louie
 Director of Internal Audit

SIGNATURE

 Juan José Cadena Orozco
 Chief Accountant

HSBC MEXICO, S. A.
 Institución de Banca Múltiple, Grupo Financiero HSBC
AND SUBSIDIARIES
 Consolidated Statements of changes in Stockholders' Equity
 Years ended December 31, 2013 and 2012
 (Millions of pesos)

	Paid-in capital		Earned capital						Non-controlling interest	Total stockholders' equity
	Capital stock	Additional paid-in capital	Capital reserves	Accumulated losses	Unrealized gain (loss) from valuation of available-for-sale securities	Mark to market from cashflow hedges	Subsidiary dilution effect	Net income		
Balances at December 31, 2011	\$ 5,261	22,357	11,057	(202)	547	(243)	-	716	3	39,496
Changes resulting from stockholder resolutions (note 25a):										
Appropriation of prior year's net income	-	-	-	716	-	-	-	(716)	-	-
Resolution at the Ordinary General Stockholders' Meeting on April 27, 2012 - Reserve constitution	-	-	716	(716)	-	-	-	-	-	-
Resolution at the Board of Director's Meeting on October 20, 2011 - Dividends paid from the resolution made on March 15, 2012	-	-	(1,400)	-	-	-	-	-	-	(1,400)
Total items related to stockholders' resolutions	-	-	(684)	-	-	-	-	(716)	-	(1,400)
Changes related to the recognition of comprehensive income (note 25b):										
Net income	-	-	-	-	-	-	-	3,997	-	3,997
Valuation effect of available-for-sale securities and hedging of cashflow (notes 8 and 11)	-	-	-	-	355	140	-	-	-	495
Subsidiary dilution effect	-	-	-	-	-	-	200	-	-	200
Non-controlling interest	-	-	-	-	-	-	-	-	(1)	(1)
Total comprehensive income	-	-	-	-	355	140	200	3,997	(1)	4,691
Balances at December 31, 2012	5,261	22,357	10,373	(202)	902	(103)	200	3,997	2	42,787
Changes resulting from stockholder resolutions (note 25a):										
Appropriation of prior year's net income	-	-	-	3,997	-	-	-	(3,997)	-	-
Resolution at the Ordinary General Stockholders' Meeting on January 24, 2013 - Increase in Capital stock and additional paid-in capital	419	4,731	-	-	-	-	-	-	-	5,150
Resolution at the Ordinary General Stockholders' Meeting on April 26, 2013 - Reserve constitution	-	-	400	(400)	-	-	-	-	-	-
Resolution at the Board of Director's Meeting on March 21, 2013 - Dividends paid from the resolution made on March 26, 2013	-	-	-	(1,400)	-	-	-	-	-	(1,400)
Total items related to stockholders' resolutions	419	4,731	400	2,197	-	-	-	(3,997)	-	3,750
Changes related to the recognition of comprehensive income (note 25b):										
Net income	-	-	-	-	-	-	-	2,146	-	2,146
Valuation effect of available-for-sale securities and hedging of cashflow	-	-	-	-	(612)	94	-	-	-	(518)
Recognition of the effect derived from the application of the new methodology for determining the preventive commercial loan loss reserves, recognized in retained earnings (note 4a)	-	-	-	(559)	-	-	-	-	-	(559)
Total comprehensive income	-	-	-	(559)	(612)	94	-	2,146	-	1,069
Balances at December 31, 2013	\$ 5,680	27,088	10,773	1,436	290	(9)	200	2,146	2	47,606

See accompanying notes to the consolidated financial statements.

"These consolidated statements of changes in stockholders' equity were prepared in accordance with the accounting criteria for credit institutions issued by the National Banking and Securities Commission pursuant to Articles 99, 101 and 102 of the Law for Credit Institutions, which are of general and mandatory nature. Accordingly, these reflect all the stockholders' equity account entries relating to the transactions carried out by HSBC during the periods noted above. Furthermore, these transactions were carried out and valued in accordance with sound banking practices and the applicable legal and administrative provisions."

"These consolidated statements of changes in stockholders' equity were approved by the Board of Directors under the responsibility of the undersigned officers".

SIGNATURE
 Luis Peña Keigel
 Chief Executive Officer

SIGNATURE
 Gustavo Ignacio Méndez Narváez
 Chief Financial Officer

SIGNATURE
 Ngai Yee Louie
 Director of Internal Audit

SIGNATURE
 Juan José Cadena Orozco
 Chief Accountant

HSBC MEXICO, S. A.
 Institución de Banca Múltiple, Grupo Financiero HSBC
AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended December 31, 2013 and 2012

(Millions of pesos)

	<u>2013</u>	<u>2012</u>
Net income	\$ 2,146	3,997
Adjustments for non cash items:		
Cancellation of intangible assets under development	-	110
Depreciation of property, furniture and equipment	1,274	1,286
Amortization of intangible assets	389	340
Provisions	2,589	1,903
Current and deferred income taxes	1,099	1,413
Equity in the results of associated and affiliated companies	(43)	(35)
Non-controlling interest	<u>1</u>	<u>(1)</u>
	7,455	9,013
Operating activities:		
Change in margin accounts	53	(26)
Change in investment securities	(14,360)	21,838
Change in debtors under agreements to resell	7,206	(1,957)
Change in derivatives (assets)	(6,287)	(254)
Change in loan portfolio	(3,968)	(12,860)
Change in foreclosed assets	59	(15)
Change in other operating assets	(8,352)	(1,578)
Change in deposit funding	(8,065)	(2,246)
Change in loans from banks and other institutions	(2,217)	(9,809)
Change in creditors under agreements to repurchase	14,036	5,356
Change in securities lending (liability)	-	(4)
Change in collateral sold or pledged as guarantee	5,188	(7,770)
Change in derivatives (liability)	6,722	(2,375)
Change in subordinated debt issued	(733)	(292)
Change in other operating liabilities	2,678	11,393
Income taxes paid	<u>(1,694)</u>	<u>(1,405)</u>
Net cashflows from operating activities	<u>(2,279)</u>	<u>7,009</u>
Investing activities:		
Proceeds from sale of property, furniture and equipment	3	110
Purchase of property, furniture and equipment	(997)	(689)
Purchase of intangible assets	(950)	(408)
Proceeds from dividends in cash	<u>34</u>	<u>-</u>
Net cashflows from investing activities	<u>(1,910)</u>	<u>(987)</u>
Financing activities:		
Increase in capital stock and additional paid-in capital	5,150	-
Payment of dividends	<u>(1,400)</u>	<u>(1,400)</u>
Net cash flows from financing activities	<u>3,750</u>	<u>(1,400)</u>
Net (decrease) increase in cash and cash equivalents	(439)	4,622
Cash and cash equivalents at the beginning of year	<u>55,846</u>	<u>51,224</u>
Cash and cash equivalents at end of year	<u>\$ 55,407</u>	<u>55,846</u>

See accompanying notes to the consolidated financial statements.

"These consolidated statements of cash flows, were prepared in accordance with the accounting criteria for credit institutions issued by the National Banking and Securities Commission pursuant to Articles 99, 101 and 102 of the Law for Credit Institutions, which are of general and mandatory nature. Accordingly this reflects all cash provided and used derived from HSBC's operations during the periods noted above. Furthermore, these transactions were carried out and valued in accordance with sound banking practices and the applicable legal and administrative provisions."

"These consolidated statements of cash flows were approved by the Board of Directors under the responsibility of the undersigned officers".

SIGNATURE

 Luis Peña Kegel
 Chief Executive Officer

SIGNATURE

 Gustavo Ignacio Méndez Narváez
 Chief Financial Officer

SIGNATURE

 Ngar Yee Louie
 Director of Internal Audit

SIGNATURE

 Juan José Cadena Orozco
 Chief Accountant

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

For the years ended December 31, 2013 and 2012

(Millions of pesos)

These consolidated financial statements have been translated from the Spanish language original solely for the convenience of foreign/English-speaking readers.

(1) Description of business and significant transactions-

Description of business-

HSBC México, S. A. Institución de Banca Múltiple, Grupo Financiero HSBC (the Bank or HSBC) is a subsidiary of Grupo Financiero HSBC, S. A. de C. V. (the Group), who owns 99.99% of its capital stock. HSBC Latin America Holdings (UK) Limited (HSBC LAH) currently owns 99.99% of the Group's capital stock. In accordance with the Law of Credit Institutions (LCI), the Bank is authorized to provide multiple service banking operations, consisting of receiving deposits, accepting loans, granting loans, trading securities and derivative transactions and entering into trust agreements, among others.

Significant transactions and other issues-

2013

On December 9, 2013, the Bank placed two issuances of Bonds (CEBURES); the first issuance aggregating \$2,300 with a 5-year term, bearing monthly interest at the TIIE rate plus 30 basis points and the second issuance for \$2,700, with a 10-year term, bearing half-yearly interest at the rate of 8.08% (note 19).

On January 31, 2013, the Bank issued preferred subordinated debentures, subject to mandatory conversion into common shares representing capital stock, provided that any of the following conditions is met: (i) where the result from dividing the Tier 1 Basic Capital by the Bank's total weighted assets subject to risk is 4.5% or less; or (ii) where the National Banking and Securities Commission (the Banking Commission) notifies the Bank that it has not complied with the minimum remedial action in case of not having the minimum capitalization level required or when non complying with the minimum capitalization index required by the LCI and the Bank does not rectify such situation. Such issuance totaled US\$110 million and bears interest at the 30-day LIBOR rate plus 365 basis points (note 23).

2012

The Banking Commission fined the Bank for \$379 on November 4, 2011, due to a breach of various prudential dispositions identified by that authority for the years 2007 and 2008. On July 25, 2012 the Bank settled the fine, recognizing a debit in the consolidated statement of income under "Other operating income, net".

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(2) Authorization and basis of presentation-

On February 12, 2014, Luis Peña Kegel (Chief Executive Officer), Gustavo Ignacio Méndez Narváez (Chief Financial Officer), Ngar Yee Louie (Director of Internal Audit) and Juan José Cadena Orozco (Chief Accountant) authorized the issuance of the accompanying consolidated financial statements and related notes thereto.

In accordance with the General Corporations Law and the Bank's bylaws, the stockholders are empowered to modify the consolidated financial statements after issuance. The unconsolidated financial statements issued on the same date, will be submitted for approval at the next Stockholders' Meeting.

Basis of preparation-**a) Statement of compliance**

The consolidated financial statements have been prepared in conformity with the accounting criteria for credit institutions in Mexico issued by the Banking Commission (the Accounting Criteria), which were in effect at the consolidated balance sheet date. The Banking Commission is responsible for the inspection and supervision of credit institutions and for reviewing their financial information.

The Accounting Criteria states that if there is a lack of specific accounting criterion from the Banking Commission for credit institutions, or in a broader context of Mexican Financial Reporting Standards (FRS), the supplementary basis under FRS A-8 should be applied, and only if the International Financial Reporting Standards (IFRS for its acronym in English) as referred to in the FRS A-8, do not provide solutions to the accounting recognition, a supplementary norm could be applied, only if it complies with all requirements mentioned in the aforementioned FRS, and under the following order: the accounting principles generally accepted in the United States of America (US GAAP) and any accounting criterion that forms part of a formal and recognized accounting criteria.

b) Use of estimates and judgments

The preparation of consolidated financial statements requires management to make a number of estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying value of investment securities and derivatives, repos, securities lending, allowance for loan losses, foreclosed assets, employee retirement benefits and deferred income taxes. Actual results may differ from these estimates and assumptions.

c) Functional and reporting currency

The aforementioned consolidated financial statements are presented in Mexican pesos (reporting currency), which is the same as the local and the functional currency.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

For purpose of disclosure in the notes to the consolidated financial statements, when reference is made to pesos or “\$”, it means Mexican pesos, and when referring to USD\$ or dollars, means dollars of the United States of America.

The consolidated financial statements of the Bank recognize assets and liabilities related to purchase and sale of foreign currencies, investment securities, repurchase agreements and derivative financial instruments at the date when transactions are made, regardless of the settlement date.

(3) Summary of significant accounting policies-

The significant accounting policies applied in the preparation of the consolidated financial statements are as follows:

a) Recognition of the effects of inflation-

The accompanying consolidated financial statements include the recognition of the effects of inflation on the financial information until December 31, 2007, the date on which according to the FRS B-10 “Effects of Inflation” the economy changed from an inflationary to a non inflationary environment (Cumulative inflation in the last three years less than 26%), using for this purpose the Investment Unit Value (UDI for its acronym in Spanish). The UDI is a unit of measurement whose value is determined by the “Banco de México” (Central Bank) based on inflation. Annual inflation percentages of the three preceding years and the UDI values at the end of indicated years are as follows:

<u>December 31</u>		<u>Inflation</u>		
		<u>UDI</u>	<u>Annual</u>	<u>Accumulated</u>
2013	\$	5.0587	3.77%	11.76%
2012		4.8746	3.90%	12.31%
2011		4.6913	3.64%	12.11%
		=====	=====	=====

b) Basis of consolidation

The accompanying consolidated financial statements include those of the Bank and those of its subsidiaries, including the special purpose entities (SPE) that qualify to be consolidated in accordance with the accounting criteria issued by the Banking Commission. Significant intercompany transactions and balances have been eliminated in consolidation. The consolidation was made based on the financial statements of the subsidiaries and SPE as of and for the years ended December 31, 2013 and 2012, except for the financial statements of the Irrevocable Management Trust 1052 (Su Casita or Trust 1052), which have been prepared as of and for the twelve-month periods ended November 30, 2013 and 2012, without any relevant transactions in the non-coinciding period. In the following two pages are detailed the subsidiaries, SPE, and the percentage of the shareholding of the Bank as at December 31, 2013 and 2012.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

<u>Activity and subsidiary</u>	<u>Shareholding in 2013</u>	<u>Shareholding in 2012</u>
<u>Real estate</u>		
Inmobiliaria Bisa, S. A. de C. V.	99.99%	99.99%
Inmobiliaria Grufin, S. A de C. V.	99.99%	100.00%
Inmobiliaria Guatusi, S. A. de C. V.	100.00%	100.00%
Inmobiliaria el Nuevo París, S. A. de C. V. ¹	-	100.00%
Edificaciones Prime, S. A. de C. V. ¹	-	100.00%
HSBC Inmobiliaria México, S. A. de C. V.	99.96%	99.96%
Inmobiliaria GBM Atlántico, S. A. de C. V. ¹	-	99.99%
Inmobiliaria Banga, S. A. de C. V. ¹	-	99.99%
Inmobiliaria Bamó, S. A. de C. V. ¹	-	99.90%
<u>Financial services</u>		
HSBC Servicios Financieros, S. A. de C. V.	100.00%	100.00%
<u>Not in operation, but the legal process of dissolution or liquidation has not started:</u>		
Mexicana de Fomento, S. A. de C. V.	71.41%	71.41%
Almacenadora Banpacífico, S. A. de C. V.	99.99%	99.99%

The controlling interest includes the direct and indirect interest of the Bank in its subsidiaries.

¹ On December 16, 2013 these entities were merged, whereby Inmobiliaria Grufin, S. A. de C. V. is the merging concern.

Special Purpose Entities (SPE)

As of December 31, 2013 and 2012, the Bank has incorporated the following SPE, which have been consolidated given that the Bank has the control and they were created to achieve a specific purpose.

- Irrevocable administrative trust 1052 created in April 2011 upon the execution of the acknowledgment of debt and payment between the Bank and Hipotecaria Su Casita, S.A. de C.V., SOFOM ENR, arising from a loan granted by the Bank. As a result of the aforementioned, the Bank is the owner of "patrimonio A" which consists of: a) individual loans with mortgage guarantee ("capital loans"); b) cash furniture and real estate properties reserved as part of the trust management and credit collection; and, c) collection rights arising from capital loans. As of December 31, 2013 and 2012, "patrimonio A" amounts to \$336 and \$364, respectively, which is included under the "Residential Mortgages loans" item in the consolidated balance sheet.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

- Joint venture created between Credit Suisse Capital Partners (Luxembourg) S.à.r.l., the Bank, and Credit Suisse Alzette Holdings S.à.r.l. (Tula), incorporated in June 2011, where the Bank had an interest of 99.3% of the risks and benefits of the assets and liabilities, which purpose was the investment in high credit rating debt denominated in pesos. On March 22, 2013, the operations of this SPE were early terminated; consequently, the effects and transactions in force at that date were incorporated in the Bank's own operations. At December 31, 2012, the amount of the investment in debt through this SPE amounted to \$5,371 which were included as part of investments in securities, classified as available-for-sale.

c) *Cash and cash equivalents-*

Cash and cash equivalents consist of cash, precious metals (coins), bank account balances, 24 and 48-hour foreign currency purchase and sale transactions, bank loans with original maturities of up to three days ("Call Money") and deposits with the Central Bank.

Offsetting entries for 24 and 48-hour foreign currency purchase and sale transactions represent rights or obligations, which are recorded in "Other accounts receivable, net" and "Settlement transactions", respectively.

This category includes deposits related to monetary regulation, as required by the Law of the Central Bank, whose purpose is regulating the liquidity of the money market and are recognized as a restricted asset.

At the date of the consolidated financial statements, interest income and profit or losses on valuation are included in the income statement as incurred as part of the interest income or interest expense. Moreover, results from valuation and sale of precious metal coins and currency are grouped in the consolidated statement of income under the caption "Financial intermediation income".

d) *Margin accounts-*

This account is comprised of the total collateral held in cash, securities or other highly liquid instruments in respect of derivative transactions on recognized stock market exchanges.

e) *Investment securities-*

Investment securities consist of equities, government securities and bank notes, listed and unlisted, classified into the next categories, depending on management's investment intentions.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Trading securities-

Trading securities are bought and held mainly to be sold in the near term. Debt securities and equities are initially and subsequently marked to market at a price provided by an independent price vendor. Valuation effects are recognized in results of operations within "Financial intermediation income". If the amount of trading securities is short for settling the amount of securities deliverable in value date transactions in relation to purchase-and-sale of securities, the credit balance is shown as a liability under "Delayed delivery securities".

Available-for-sale securities-

Securities not classified as trading or held-to-maturity are classified as available-for-sale securities. Available-for-sale securities are recorded in the same way as trading securities; however, the mark-to-market adjustment is reported in stockholders' equity under the caption "Unrealized gain from valuation of available-for-sale securities". Unrealized gains are cancelled when the respective securities are sold, reporting the difference between net realizable value and acquisition cost within the results of operations.

It is necessary to evaluate whether at the consolidated balance sheet date there exists objective evidence of impairment, considering the difference between the initial carrying value of the security net of any principal payment or amortization and the fair value of the security. Any difference identified as impairment should be recognised in the income statement for the period.

Held-to-maturity securities-

Held-to-maturity securities are those securities that the Bank has the ability and intent to hold until maturity, and that have defined payments. Held-to-maturity securities are initially recorded at fair value and subsequently at amortized cost. Interest is recognized in income as earned. When securities mature, the difference between the actual amount received and the net book value is recognized in the consolidated statement of income within "Financial intermediation income".

If objective evidence of impairment exists in respect of held to maturity securities, the value of the security should be reduced and the impairment amount should be recognised in the current year income consolidated statement.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Transfers between categories-

The sale of securities to be held to maturity must be reported to the Banking Commission. Likewise, securities may be reclassified from the categories "trading securities" and "available-for-sale securities" to the category "held to maturity securities" or from "trading securities" to "available-for-sale securities", as long as the Banking Commission grants its authorization. Also, they can be reclassified from the category "held to maturity securities" to "available-for-sale securities", provided that there is no intention or the capacity to keep them to maturity.

During 2013 and 2012, there were no transfers between categories.

For operations where no settlement is agreed upon immediate or same day value date, on the date of the agreement the right and / or the obligation should be recorded in the clearing accounts until the liquidation is settled. In cases where the receivable is not settled within 90 calendar days from the date on which it was registered in clearing accounts, it will be reclassified as past due debt and estimation should be registered for the total amount.

f) Securities under repurchase/resell agreements-

Repurchase agreements that do not comply with the terms set out in criterion C-1 "Recognition and derecognition of financial assets", have been treated as collateralized financing transactions, reflecting the economic substance of such transactions and regardless of whether they are "cash based" or "securities based".

The Bank when recording these transactions as financing transactions recognizes the receipt of cash or an account receivable, as well as an account payable for the agreed price, which represents the obligation to repay that money, and reclassifies the financial asset as restricted collateral. When the Bank is acting as the provider of finance, it recognizes the payment of cash or an account payable and also registers an account receivable in respect of the agreed price, which represents the right to recover the cash provided and recognizes the collateral received in a memorandum account. Over the life of the repo, the account payable or receivable are presented in the consolidated balance sheet as debtors or creditors as appropriate, and are valued at amortized cost, recognizing interest in the results for the year as it accrues, according to the effective interest method. The accrual of interest arising from the repo operation will be presented under the heading of "Interest income" or "Interest expense", as appropriate.

In relation to the financial assets that have been sold or pledged as buyer of securities, there is recognition of an account payable for the obligation to restore the collateral to the seller, which is valued at fair value in the event of a sale and at the amortized cost if the assets were pledged in a repurchase transaction.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The differential, if any, that is generated by the sale of or using the security as collateral will be presented under the heading of “Financial intermediation income”.

In accordance with the dispositions of the Central Bank, any repurchase transaction, with a maturity period over three days must include an obligation to guarantee such transaction, when the fluctuations in the value of the securities under the repurchase agreement represents a net exposure which exceeds the maximum amount agreed by the parts.

The collaterals granted (without transfer of ownership) are recorded in the securities portfolio as securities for trading or in collateral, and if it corresponds to cash deposits, are registered under the cash and cash equivalents account as a restricted asset.

Securities under repurchase/resell agreements that cannot be renegotiated with a third party are reported as secured borrowing or lending transactions. Premiums are recognized in income as they accrued, on a straight-line basis, throughout the term of the transaction.

g) *Securities lending-*

In operations where the Bank transfers securities to a borrower and receives other financial assets as collateral, it recognizes the fair value of the securities lent as restricted, while financial assets received as collateral (including cash managed in trusts), are recognized in memorandum accounts. When the Bank receives securities in a securities lending transaction, it records the value of the securities in memorandum accounts while the financial assets provided as collateral are recognized as restricted (including cash managed in trusts). In both cases the financial assets received or delivered as collateral are recorded following the rules of valuation, presentation and disclosure in accordance with applicable accounting standard, while the values recorded in memorandum accounts are valued according to custody operation rules. The premium earned is recognized in the income statement, through the effective interest method over the life of the operation, against a receivable or payable as appropriate. The account payable which represents the obligation to repay the transaction value is reported in the consolidated balance sheet under the heading of “Collateral sold or pledged as guarantee”.

h) *Derivative transactions-*

Transactions with derivative financial instruments comprise those carried out for trading or hedging purposes. These instruments are recognized at fair value, regardless of their classification. The accounting treatment is described below:

Futures and forward contracts – The consolidated balance sheet shows the net fluctuation in the market value of the contracts’ price. These effects are recognized in income, except in the case of hedging transactions where the related gains or losses are recorded as deferred credits or debits and amortized using the straight-line method during the term of the underlying instruments and shown together with the primary hedged position.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Swaps – Rights or obligations established in the contract arising from the exchange of cash flows or asset yields (swaps) are recorded as assets or liabilities. The assets and liabilities derived from swaps are marked to market, reporting the net value of the swap on the consolidated balance sheet while the related gains or losses are recognized in income, except in the case of transactions designated as hedges where gains or losses are recorded as deferred credits or debits and amortized using the straight-line method during the term of the underlying instruments and shown together with the primary position they cover.

Options – Put and call option obligations (premiums collected) or rights (premiums paid) are recorded at contract value and subsequently valued at fair value, recording all gains or losses in the consolidated statement of income. Premiums collected or paid are recognized in “Financial intermediation income, net” when the option expires.

i) Offsetting of clearing accounts-

Amounts receivable or payable arising from investment securities, securities under repurchase/resell agreements, securities lending and/or derivative financial instruments which have expired but have not been settled at the consolidated balance sheet date as well as amounts receivable or payable resulting from the purchase or sale of foreign currencies which are not for immediate settlement or those with a same day value date, are recorded in clearing accounts included within “Other accounts receivable, net” and “Settlement transactions”.

The debit and credit balances of clearing accounts are offset as long as they have the contractual right to offset the amounts recorded at the same time, there is an intention to settle on a net basis or to realize the asset and settle the liability simultaneously.

j) Past due loans and interest-

Outstanding loan and interest balances are classified as past due according to the following criteria:

Commercial loans with principal and interest payable upon maturity – 30 days after due date.

Commercial loans with principal payable upon maturity and periodic interest payments – When interest or principal have not been collected 90 or 30 days after their due date, respectively.

Commercial loans with principal and interest repayments – when principal and interest have a period of 90 days past due.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Revolving credits, credit cards and others – when unpaid for two past due billing cycles or when the billing period is not monthly, at the equivalent of 60 days or more of past due.

Mortgage loans - when the outstanding balance of a loan has unpaid instalments for 90 or more days overdue.

Overdrafts from checking accounts without lines of credit – when the overdraft arises.

In addition, a loan is classified as past due when the debtor files for bankruptcy protection.

Non-current loans for which fully settled outstanding balances is made (including interest) and restructured or renewed loans showing sustained payment of credit, are reclassified as current. When those loans are reclassified to current portfolio, interest recorded in memorandum accounts, are recognized in consolidated statement of income at the moment of reclassification.

k) *Restructured loans*–

The Bank has eligibility for credit restructuring, which generally consider that the terms of such restructuring are based on the repayment capacity of borrowers depending on each of the different types of credit.

Non-performing loans that are restructured or renewed remain within nonperforming loans, while there is no evidence of sustained payment.

Loans with a single payment of principal to maturity and periodic interest payments and credits with a single payment of principal and interest at maturity that are restructured during the term of the loan or renewed at any moment shall be considered as non-performing loans until there is evidence of sustained payment.

Those categorized as revolving credit, which are restructured or renewed at any time shall be deemed performing only when the borrower liquidated all of the accrued interest, the credit is not in arrears, and counts with elements indicating the ability to pay of the debtor.

Performing, loans other than those mentioned in the two preceding paragraphs, which are restructured or renewed shall be deemed to remain performing only if they meet the following:

- The life of the loan is below 80% of the original term of the loan, when the borrower has:
 - i) Covered all of the accrued interest, and
 - ii) Covered the principal of original loan amount, which at the time of the renewal or restructuring should have been covered.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

- If the loan is restructured or renewed during the course of the final 20% of the original term of the loan, when the borrower has:
 - i) Paid all accrued interest
 - ii) Covered the entire original loan amount that at the date of the renewal or restructuring should have been covered
 - iii) Also covered 60% of the original loan amount.

Should not all the conditions described above meet, then they are considered to be past due from the moment they are restructured or renewed, and until there is evidence of sustained payment.

l) Allowance for loan losses-

The allowance for loan losses, according to the administration, is sufficient to cover any losses that may arise from loans in its portfolio of loans and credit risk guarantees and irrevocable loan commitments. The allowance for loan losses is determined as follows:

Rated loans - The loan portfolio is classified according to the rules issued by the Ministry of Finance and Public Credit (SHCP for its acronym in spanish) based on the "General provisions applicable to credit institutions" (the "Regulations") issued by the Banking Commission, using the standard methodology for commercial loans, consumer and mortgage. The methodology distinguishes credit risk ratings and based on this determines the reserve.

On June 24, 2013, the Banking Commission published in the Federal Official Gazette a resolution whereby the Provisions are amended for the creation of preventive reserves for commercial loans other of States, Municipalities and Investment Projects with own source of payment to adopt an expected loss, considering the probability of default, the loss given default and the exposure at default. In addition, the commercial loan portfolio is classified in two groups: the first group includes those with annual sales fewer than 14 million UDIS, where quantitative factors are assessed and the second group includes borrowers with annual sales equal to or greater than 14 million UDIS, which are also assessed for qualitative factors.

The resolution came into force on the following day of its publication and it was resolved that the application of the new criteria concerning the commercial loan portfolio would occur by December 31, 2013, allowing early application and the recognition of the financial effects from the application of the new methodology in stockholders' equity of the institutions in cases where, being impractical, it is not possible to apply the effect retrospectively. On June 30, 2013, and in accordance with the provisions of transitory article two, the Bank early adopted the new methodology (refer to note 4). In the case of the creation of preventive reserves for loans granted to financial entities, the new methodology will be applied from January 2014 while the financial impact for the creation of additional reserves should be recognized by June 30, 2014.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The current methodology published in the Federal Official Gazette on October 5, 2011 that is based on concepts such as: expected loss, probability of default, exposure at default and loss given default by loan and borrower applies for States, Municipalities and Investment Projects; considering mainly the ratings provided by rating agencies.

The allowance for loan losses is determined depending on the risk level as follows:

Risk level	Consumer loans		Residential	Commercial
	Non revolving	Revolving	Mortgage	
A - 1	0.00 - 2.00	0.00 - 3.00	0.00 - 0.50	0.00 - 0.90
A - 2	2.01 - 3.00	3.01 - 5.00	0.501 - 0.75	0.901 - 1.50
B - 1	3.01 - 4.00	5.01 - 6.50	0.751 - 1.00	1.501 - 2.00
B - 2	4.01 - 5.00	6.51 - 8.00	1.001 - 1.50	2.001 - 2.50
B - 3	5.01 - 6.00	8.01 - 10.00	1.501 - 2.00	2.501 - 5.00
C - 1	6.01 - 8.00	10.01 - 15.00	2.001 - 5.00	5.001 - 10.00
C - 2	8.01 - 15.00	15.01 - 35.00	5.001 - 10.00	10.001 - 15.50
D	15.01 - 35.00	35.01 - 75.00	10.001 - 40.00	15.501 - 45.00
E	35.01 - 100.00	75.01 - 100.00	40.001 - 100.00	45.001 - 100.00

As of December 31, 2012, the allowance is established considering the risk levels in accordance with the following table:

Risk level	Range of allowance percentages
A - Minimum	0.50 - 0.99
B - Low	1.00 - 19.99
C - Medium	20.00 - 59.99
D - High	60.00 - 89.99
E - Irrecoverable	90.00 - 100.0

The Dispositions establish rules for the creation of allowances that recognize potential losses in the loan portfolio and of foreclosed assets or received in lieu of payment over time.

General reserves – In accordance with the Dispositions risk grade A and B-1 from the revolving consumer portfolio are considered general reserves.

Specific reserves – Those reserves resulting from loans with risk grade B, C, D and E, but not including those which result from risk grade B-1 from the revolving consumer portfolio.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Exempt portfolio – consists mainly of loans to the Bank Savings Protection Institute (IPAB for its acronym in Spanish), which are not rated.

Impaired loans – Commercial loans which are not likely to be fully recovered. Both, current and past due portfolios may be identified as impaired loans. For consolidated financial statement disclosure purposes, “impaired loans” are those commercial loans classified by the Bank as having the risk levels “D” and “E”.

Additional reserves – Are those that are created for hedging risks that are not provided by the various methodologies for rating the loan portfolio. Also included are estimates for items such as uncollected ordinary interest accrued and other ancillary charges, as well as reserves required by the Banking Commission.

Loans considered irrecoverable are written off against the allowance when their collection is determined to be impractical. Recoveries derived from loans written off are recognized in income of the year.

As a result of the rating process, increases or decreases in the preventive loan loss reserve are recorded in the year’s income (loss), adjusting the financial margin.

When the balance of the preventive loan loss reserve exceeds the amount required in accordance with the rating methodologies, the difference is cancelled on the date on which the next rating occurs depending on the type of loan (commercial, consumer or housing) versus the year’s income (loss) and affecting the preventive loan loss reserve. In cases where the amount to be cancelled exceeds the recorded balance of such allowance in the year’s income (loss), the excess is recognized in “Other operating income, net”:

Claim reductions, debt cancellations, rebates and discounts are recorded as charges to the preventive loan loss reserve. If the amount of the latter exceeds the balance of the reserve associated with the loan, reserves for up to the amount of the difference are created in advance.

m) Other accounts receivable-

Loans to officers and employees, collection rights, and other receivables from identified debtors, whose agreed-upon maturity does not exceed 90 calendar days, are assessed by management to determine their estimated recovery value and, where applicable, a loan loss reserve is created. Amounts receivable from other accounts receivable, that are not recovered within 90 days subsequent to their initial recording (60 days if balances are unidentified) are totally reserved, except for those related to recoverable tax balances, value added tax, and clearing accounts. This caption also includes debtors on settlement of 24 and 48-hour foreign currency sales transactions.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

n) *Foreclosed assets-*

Foreclosed assets are recorded at the lesser of: (a) cost, (b) its fair value deducted from the strictly necessary costs and expenses that are incurred in the adjudication and (c) the value of the asset or amortizations due or overdue that led to the adjudication, net of its estimates.

When the book value exceeds the value of the foreclosed asset, the difference will be recognized in the consolidated statement of income of the year as part of "Other operating income". In the case of a promise of sale-and-repurchase agreements including ownership reserves, these transactions do not comply with the requirements of accounting criteria C-1 "Recognition and derecognition of financial assets". In this case the asset should be recognized and classified as restricted, depending on the relevant type of asset, at the book value on the date of the agreement, even if the agreed sale price is higher than the book value.

Payments received in advance in relation to the aforementioned assets are recorded as a liability. The gains or losses arising from these transactions are recorded in "Other operating income" on the date that the conditions to consider that the ownership has been transferred in accordance with accounting criteria C-1 are met.

The Bank creates additional reserves on a quarterly basis to recognize potential losses for the impairments in asset value due to the passing of time. These reserves are created in accordance with the Dispositions which are determined as follows:

<u>Elapsed months since the date of foreclosure or lieu of payment</u>	<u>Percentage of the allowance</u>	
	<u>Real Estate</u>	<u>Other assets</u>
More than: 6	0	10
12	10	20
18	10	45
24	15	60
30	25	100
36	30	100
42	35	100
48	40	100
54	50	100
60	100	100

o) *Property, furniture and equipment-*

Property, furniture and equipment are initially recorded at acquisition cost and through to December 31, 2007, for being the last year considered as inflationary economic environment under FRS "B-10" were adjusted for inflation by using factors derived from the UDI.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Depreciation and amortization are calculated using the straight – line – method over the estimated useful life of the assets. The useful life of the principal assets classes are show on note 15.

p) *Permanent investments in shares-*

Investments in affiliated and associated companies are valued using the equity method, which recognizes changes in income (loss) of the year. It is also included under this caption other permanent investments in which there is no significant influence, which are recorded at their acquisition cost.

q) *Other assets, deferred charges and intangibles-*

Other assets include recoverable balances of taxes pending to be offset or recovered. Deferred charges include the prepayment of labour obligations and other expenses pending amortization arising from services and commissions paid in advance, whose amortization is made on straight line over the term of the related transaction.

“Intangible Assets” includes costs directly related to the installation and commissioning of computer equipment software and the cost of the necessary licenses to operate such equipment. According to the internal policies of the Bank, only projects that comply with the following characteristics are subject to be capitalized: (i) the assets are identifiable, (ii) the Bank has control over the assets and (iii) that there will be anticipated future economic benefits from them. The average life of these assets which are amortized on a straight line basis is 3 to 5 years, based on its characteristics.

r) *Income tax (IT) and flat rate business tax (IETU)-*

IT and IETU payable for the year are determined in conformity with tax regulations in force at December 31, 2013 and 2012.

Deferred IT or IETU is accounted for under the asset and liability method which compares accounting and tax values. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the consolidated financial statement carrying amounts of existing assets and liabilities and their respective tax bases, as well as for unamortized tax losses carry forward and unused tax credits. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in results of operations for the period the change is enacted.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

s) *Deposit funding-*

This caption includes demand and term deposits made by the general public including negotiable instruments issued. Interest is recognized in operations on the accrual basis. Regarding those instruments placed at a price other than par value, difference between the instrument par value and the cash amount received for it, is recognized as a deferred charge for issue expenses, under the caption "Other assets, deferred or intangible charges", or a deferred credit in the liability that gave rise to it and is amortized under the straight-line method against income during the term of the instrument that generated it.

t) *Due to banks and other institutions-*

Bank and other loans comprises short and long-term bank loans, loans obtained through credit auctions with Central Bank and development fund financing. In addition, this category includes loans rediscounted with agencies specializing in financing economic, productive or development activities. Interest is recognized on accrual basis. In the case of interbank loans received within less or equal to 3 days are presented as part of the category of immediate enforceability.

u) *Employee benefits-*

Termination benefits other than restructuring and retirement to which employees are entitled are recorded in the consolidated statement of income, based on actuarial computations using the projected unit credit method, considering the projected salaries. At December 31, 2013 and for purposes of recognizing benefits upon retirements, the remaining average service life of employees entitled to pension and seniority premium plan, are approximately 16 years and 13 years for post-retirement benefits (for 2012, 18 years and 14 years respectively).

Actuarial gains or losses are recognized in the consolidated statement of income as accrued considering the remaining service life of the employees expected to receive plan benefits and are amortized based on life expectations of the group of retirees. In the case of pension plan of defined contribution and other defined contribution benefits are recognized in the statement of operations as accrued.

v) *Share-based payment-*

The Bank offers different payment program based on shares of its ultimate holding Company's equity for certain employees, recognizing an operating expense in the consolidated statement of income and a liability, during the vesting period, at the estimated fair value of the equity securities when settling the liability. The vesting period of the grant of such programs varies between one and three years in average.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

w) *Revenue recognition-*

Interest on loans granted is recorded in income as earned. Interest on past due loans is not recognized in income until collected.

Fees and interest collected in advance are recorded as deferred income under "Deferred credits", and recognized in results of operations as earned.

The annuity and renewal fees for credit cards are deferred over a period of twelve months.

Fees charged for initially granting loans (personal, residential mortgages, and commercial loans) are recorded as a deferred credit, which is amortized against income of the year as interest income, pursuant to the straight-line method during the life of the loan. All other fees are recognized at the time they are generated in the line item of fees, and rates charged in the consolidated statement of income. Costs and expenses associated with credit loans are recognized as deferred charge and amortized over the same period in which revenue is recognized by fees charged for granting of such credits.

The interest from repurchase transactions are recognized as earned. Fees earned in connection with fiduciary operations and those arising from asset custody and management services are recognized in income as earned.

x) *Foreign currency transactions-*

The accounting records are maintained in both pesos and foreign currencies, which for presentation of the consolidated financial statement purposes, in the case of currencies other than the dollar are translated from the respective currency into dollars as established by the Banking Commission and the dollar equivalence with Mexican currency is translated at the exchange rate established by the Central Bank. Foreign exchange gains and losses are recognized in the consolidated statement of income during the year.

y) *Contributions to the Institute for the Protection of Bank Savings (IPAB for its acronym in Spanish)-*

Among other provisions, the Bank Savings Protection Law provides for the creation of the IPAB, which intends to act as a system for protecting the bank savings of depositors and regulates the financial support granted to the commercial banking institutions to achieve this objective. The IPAB guarantees a maximum of 400,000 UDIS (\$2 at December 31, 2013) by saver and by institution. The Bank recognizes in results of operations the mandatory contributions to the IPAB.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

z) Contingencies-

Liabilities for loss contingencies are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated. When a reasonable estimation cannot be made, qualitative disclosure is provided in the notes to the consolidated financial statements. Contingent revenues, earnings and assets are not recognized until their realization is virtually assured.

aa) Impairment of recovery from long term assets-

The Bank evaluates periodically the long term assets to determine whether there is an indication of potential impairment. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net revenues expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated net revenues, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the consolidated balance sheets and reported at the lower of the carrying amount or realizable value.

(4) Accounting changes and reclassifications-**Accounting changes-**

- a) On June 24, 2013, certain amendments to the Provisions, relating to the methodology for rating the commercial loan portfolio granted to financial entities, were published in the Federal Official Gazette (DOF); individuals with business activities and legal entities other than: projects with own source of financing, as well as credit schemes commonly known as “structured”. The Bank applied the new methodology for rating the commercial loan portfolio from June 2013, recognizing a charge to stockholders’ equity of \$799 (\$559 net of deferred taxes), in accordance with the transitory articles of such Provisions.

The Bank has not determined the retrospective financial effect from the application of this new methodology as of the end of December 2012. While management has made all the reasonable efforts, it has not been able to obtain the historical data required by the new methodology. Consequently, these consolidated financial statements do not include information set out by paragraph 11 of FRS B-1, “Accounting changes and error corrections”, as required by the Banking Commission under transitory article four about the amendments to the provisions published on June 24, 2013.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

- b) The Mexican Board of Financial Reporting Standards (*Consejo Mexicano de Normas de Información Financiera, A. C.* or CINIF) issued the following FRS and improvements to FRS that had no significant effects on the Bank's consolidated financial statements:
- **FRS B-8 “Consolidated or combined financial statements”**- FRS B-8 is effective for years beginning on or after January 1, 2013, with retrospective effects. This change supersedes FRS B-8 “Consolidated or combined financial statements”- Main changes include the definition of control; the inclusion of the concepts of “protective rights” and “structured entity” as well as the figures of “principal” and “agent”.
 - **FRS C-5 “Prepayments”, Bulletin C-9 “Liabilities, provisions, contingent assets and liabilities, and commitments” and Bulletin C-12 “Financial instruments with characteristics of liability, equity, or both”**- This FRS provides that expenses on the issue of debentures be presented as a reduction of the respective liability and charged to income based on the effective interest method.
 - **FRS D-4 “Income Taxes”**- FRS D-4 provides that current and deferred income tax be recognized and included in profit or loss for the period, except to the extent that tax arises from a transaction or event that is recognized in a different period, outside profit or loss, either in other comprehensive income or directly in equity.

The improvements discussed above became effective for years beginning on or after January 1, 2013 and their recognition is prospective in respect of changes in valuation and retrospective when it comes to presentation changes.

c) **Reclassifications-**

Certain captions of the consolidated financial statements for the year ended December 31, 2012 have been reclassified to conform to the classifications used in the 2013 financial statements.

(5) **Foreign currency exposure-**

Central Bank regulations require that banks maintain balanced positions in foreign currencies within certain limits. The short or long position permitted by the Central Bank is equal to a maximum of 15% of the basic capital. In accordance to the basic capital of the Bank, as published by the Central Bank as of September 30, 2013 and 2012, the maximum exposure permitted as of December 31, 2013 and 2012, amounts to USD\$491 and USD\$431, respectively.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The foreign currency position as of December 31, 2013 and 2012 is analyzed as follows:

	<u>(Millions of dollars)</u>	
	<u>2013</u>	<u>2012</u>
Assets	38,029	29,056
Liabilities	<u>(37,904)</u>	<u>(29,349)</u>
Net assets (liabilities)	125	(293)
	=====	=====

The exchange rate of the peso to the dollar as of December 31, 2013 and 2012 was \$13.0843 and \$12.9658, respectively. The exchange rate on February 12, 2014, the date of issuance of the consolidated financial statements was \$13.3056 pesos per dollar.

(6) Cash and cash equivalents-

At December 31, 2013 and 2012, cash and cash equivalents are analyzed as follows:

	<u>2013</u>	<u>2012</u>
Cash	\$ 12,251	12,630
Deposits with domestic and foreign banks	6,965	5,310
Other cash equivalents	1	11
Restricted cash and cash equivalents:		
Central Bank deposits	32,599	32,542
Bank loans with maturity up to three days	2,988	-
24 and 48-hour foreign currency purchases	40,729	22,487
24 and 48-hour foreign currency sales	<u>(40,126)</u>	<u>(17,134)</u>
	\$ 55,407	55,846
	=====	=====

At December 31, 2013 and 2012, cash balances valued in Mexican pesos by currency included in the cash and equivalents caption is as follows:

<u>Currency</u>	<u>Exchange rate</u>		<u>2013</u>	<u>2012</u>
	<u>2013</u>	<u>2012</u>		
Mexican peso	\$ -	-	\$ 12,104	12,430
Dollar	13.0843	12.9658	146	198
Euro	18.0302	17.1382	<u>1</u>	<u>2</u>
			\$ 12,251	12,630
			=====	=====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

At December 31, 2013 and 2012, the Bank did have deposits in dollars with the Central Bank for \$6 and \$32, respectively.

At December 31, 2013 and 2012, the deposits with the Central Bank in local currency relates to monetary regulation deposits with no specific term and bear interest at the average rate of deposit fundings.

At December 31, 2013, the Bank has call money loans with 3-day maturities (did not have call money at December 31, 2012), as follows:

	<u>Term</u>	<u>Rate</u>	<u>Amount</u>
Nacional Financiera, S. N. C.	2 days	3.50%	\$ 1,600
Banco Mercantil del Norte, S. A.	2 days	3.45%	650
Banco Nacional de México, S. A.	2 days	3.40%	<u>738</u>
			\$ 2,988
			=====

At December 31, 2013 and 2012 currencies receivable and deliverable on purchases and sales to be settled in 24 and 48 hours, translated into pesos, are analyzed as follows:

<u>Currency</u>	<u>2013</u>		<u>2012</u>	
	<u>Purchased</u>	<u>Sold</u>	<u>Purchased</u>	<u>Sold</u>
Dollar	\$ 30,061	(29,544)	21,105	(16,684)
Sterling	-	(49)	15	(15)
Euro	117	(3)	664	(423)
Brazilian real	10,368	(10,452)	703	-
Other currencies	<u>183</u>	<u>(78)</u>	<u>-</u>	<u>(12)</u>
	\$ 40,729	(40,126)	22,487	(17,134)
	=====	=====	=====	=====

(7) Margin accounts -

On December 31, 2012, the margin accounts relates to deposits at the MexDer, Mercado Mexicano de Derivados, S. A. de C. V. amounting to \$53.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(8) Investment securities-

At December 31, 2013 and 2012 the Bank's investments in securities are analysed as follows:

	2013		2012	
<u>Trading</u> *:				
Government securities	\$ 45,730		27,669	
Banking promissory notes	2,019		1,847	
Bonds	1,301		1,298	
Equities	<u>2,071</u>	51,121	<u>5,524</u>	36,338
<u>Available-for-sale</u> *:				
Government securities	92,117		93,140	
Bank securities	508		1,840	
Corporate securities	<u>3,456</u>	96,081	<u>2,204</u>	97,184
<u>Held-to-maturity</u> *:				
Special CETES of the UDIS Trusts:				
Mortgages	4,323		4,161	
States and municipalities	627		603	
Corporate securities	<u>1,303</u>	<u>6,253</u>	<u>1,717</u>	<u>6,481</u>
Total investment securities	\$	153,455		140,003

* The total of trading securities and available-for-sale securities include restricted securities which have been pledged as collateral, as explained later in the collateral section.

During 2013 and 2012, the Bank did not record any transfers between categories of investment securities.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Collaterals

At December 31, 2013 and 2012 securities pledged and received as collateral, including collateral sold or pledged as a guarantee were as follows:

	<u>2013</u>	<u>2012</u>
<i><u>Pledged (Restricted securities) (note 9):</u></i>		
Trading securities	\$ 28,292	16,033
Securities available for sale	<u>16,922</u>	<u>5,804</u>
	\$ 45,214	21,837
	=====	=====
<i><u>Received (in memorandum accounts) (notes 9 and 10):</u></i>		
In respect of repo transactions	\$ 8,008	45,064
In respect of securities loan:		
Fixed income	<u>9,283</u>	<u>3,903</u>
	\$ 17,291	48,967
	=====	=====
<i><u>Collateral sold or pledged as guarantee:</u></i>		
In respect of repo transactions (note 9)	\$ 7,507	35,306
In respect of securities loan:		
Fixed income	<u>9,076</u>	<u>7,894</u>
	\$ 16,583	43,200
	=====	=====

Collateral pledged, received or sold and given as a guarantee, originates primarily from repo transactions and stock borrowing and lending transactions. Collaterals received are recorded in memorandum accounts whilst the collaterals sold or pledged as guarantees are recorded in the account "Collateral sold or given as guarantee" whose balance in the case of repo transactions is presented net of the collaterals received in the consolidated financial statements.

At December 31, 2013 and 2012, the Bank had the right to pledge as a guarantee, the collateral received in sale and repurchase transactions or the right to sell or pledge the collateral received in stock borrowing transactions.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

At December 31, 2013 and 2012 the Bank maintains, investments (other than government securities), from the same issuer exceeding 5% of the Bank's net capital (as of September 30, 2013 and 2012 of \$2,649 and \$2,365, respectively), for a total value of \$15,153 and \$5,535, respectively, as follows:

<u>Issuer</u>	<u>Symbol</u>	<u>Series</u>	<u>Amount</u>	<u>Rate</u>
<u>2013</u>				
Brazilian government	BNTN071	140101	\$ 4,200	4.83%
Brazilian government	BLTN6M6	140101	6,254	9.49%
Brazilian government	BLTN6Z8	140101	<u>4,699</u>	10.36%
			\$15,153	
			=====	
<u>2012</u>				
Brazilian government	BNTN071	140101	\$ 4,918	9.76%
Brazilian government	BRAZX87	130617	<u>617</u>	10.25%
			\$ 5,535	
			=====	

Classification of investment securities-

At December 31, 2013 and 2012, the classification of investment securities in accordance to their nominal term of the securities portfolio in short and long term, is as follows:

<u>Securities</u>	<u>2013</u>		<u>2012</u>	
	<u>Short term</u>	<u>Long term</u>	<u>Short term</u>	<u>Long term</u>
Trading	\$ 32,731	18,390	29,210	7,128
Available-for-sale	11,248	84,833	22,673	74,511
Held-to-maturity	<u>-</u>	<u>6,253</u>	<u>340</u>	<u>6,141</u>
	\$ <u>43,979</u>	<u>109,476</u>	<u>52,223</u>	<u>87,780</u>
	\$ 153,455		140,003	
	=====		=====	

The weighted averages of maturity terms in years (unaudited), of investments in securities classified by categories at December 31, 2013 and 2012 is shown below:

<u>Securities</u>	<u>2013</u>	<u>2012</u>
Trading	1.57	1.38
Available-for-sale	2.79	4.12
Held-to-maturity	7.58	8.48

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The weighted average rates (unaudited) and interest income from securities at December 31, 2013 and 2012 (refer to note 28), is shown below:

Securities	2013		2012	
	Interest	Rate	Interest	Rate
Trading	\$ 1,162	3.03%	\$ 1,275	3.38%
Available-for-sale	4,467	4.97%	5,130	5.01%
Held-to-maturity	<u>295</u>	4.75%	<u>332</u>	4.83%
	\$ 5,924		\$ 6,737	
	=====		=====	

During the years ended December 31, 2013 and 2012, the net losses and gains in respect of available for sale securities were \$43 and \$16, respectively, which are recognized in the "Financial intermediation income" caption in the consolidated statement of income.

During the years ended December 31, 2013 and 2012, the Bank did not record any losses caused by impairment in available for sale or held to maturity securities.

The gain derived from the valuation of available for sale securities recognised in the stockholders' equity at December 31, 2013 and 2012 were \$23 and \$1,737, respectively, and the Bank reclassified to the statement of income \$883 and \$1,230, respectively, on the sale of various available for sale securities. Due to the above the net effect on the consolidated statements of changes was for \$874 (\$612, net of deferred tax) and \$507 (\$355, net of deferred tax), respectively.

(9) Securities under repurchase/resell agreements -

The debtor and creditor balances in respect of sale and purchase of repo transactions at December 31, 2013 and 2012, are analyzed as follows:

	Purchaser		Seller	
	2013	2012	2013	2012
Repo operations	\$ 8,001	43,012	34,765	20,729
Collaterals sold or pledged	(7,501)	(35,306)	-	-
	\$ 500	7,706	34,765	20,729
	=====	=====	=====	=====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Below is shown the type and total amount by type of asset of the collateral delivered as part of repo transactions and recorded as restricted securities as well as the securities received in repo transactions and the average terms of those open operations at December 31, 2013 and 2012:

	2013				2012			
	Reporting (restricted)	Reported (memorandum account)	Average term		Reporting (restricted)	Reported (memorandum account)	Average term	
			Sell	Purchase			Sell	Purchase
<u>Government securities</u>								
BONDES D	\$ 12,682	6,570	66	2	\$ 12,019	10,602	38	9
CETES	4	-	7	-	3,541	30,727	4	2
UMS	2,717	-	2,221	-	3,233	-	1,134	-
BPAT	-	-	-	-	-	707	-	2
BPAG91	-	1,436	-	2	-	-	-	-
BONDES M	18,308	-	277	-	2,618	3,028	1,055	2
BONDES182	-	2	-	66	-	-	-	-
<u>Bank notes</u>								
IBANOBRA	<u>2,011</u>	<u>-</u>	2		<u>426</u>	<u>-</u>	15	-
	\$ 35,722	8,008			\$ 21,837	45,064		
	=====	=====			=====	=====		

During the year ended December 31, 2013, interest income and expense from repo agreements, recognised in the consolidated income statement amounted to \$565 and \$1,889 respectively (\$2,063 and \$2,898, respectively in 2012) (note 28).

(10) Collaterals sold or pledged as a guarantee-

At December 31, 2013 and 2012, the collateral received in stock borrowing transactions and sold or pledged as a guarantee is shown as follows:

	2013			2012		
	Securities	Amount	Average term	Securities	Amount	Average term
Cetes	401,961,572	3,928	2	101,953,570	\$ 1,012	2
Bonds	47,185,452	4,957	2	25,892,639	2,705	2
Udibonos	343,464	<u>191</u>	14	315,302	<u>171</u>	2
		9,076			\$ 3,888	
		=====			=====	

Securities lending transactions outstanding at December 31, 2012, earned premium payable of \$22, which are recognised in the "Securities lending" account in the consolidated balance sheet.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

During the years ended December 31, 2013 and 2012, interest expense arising from securities lending transactions recognised in the consolidated statement of income, amounted to \$22 and \$16, respectively (note 28).

(11) Derivative transactions -

The Bank's main objectives in executing derivative transactions are neutralizing market, credit and liquidity risks that may affect the entity's future results. These instruments are also offered to certain of our customers with the same intention. The execution of these transactions is in agreement with the policies established by HSBC Holding plc and with the authorization of the Central Bank. Valuation models are duly authorized and are proper for recognition of the risks involved.

Interest rate and foreign currency swaps represents that the Bank and its customers interchange currencies and/or rates in the future. Options grant the right to receive or pay an interest rate or foreign currency at a determined price. Futures are a standard and mandatory agreement to buy or sell a predetermined amount of a specific tangible good (commodity) on a future day or date, pursuant to a standardized contract. The terms and conditions of derivative transactions of the Bank are in accordance with market standards.

The Bank uses derivatives for hedging purposes (cash flows) to convert variable flows to fixed flows. This allows two risk types of hedged:

Interest rate risk - If the underlying instrument is an asset with variable interest rate, such interest is converted into fixed interest rate through an interest rate swap, by receiving a fixed flow and paying a variable flow. If the underlying instrument is a liability, it is converted into fixed interest rate through an interest rate swap, by receiving a variable flow and paying a fixed flow. The hedged risk is the risk attributable to changes in interest rates of the underlying instrument.

Foreign currency risk - Whether the underlying instrument is an asset or a liability, fixed interest denominated in another currency is translated into pesos by entering into a foreign currency swap. The hedged risk is the risk of changes in the functional currency equivalent to cash flows for a recognized foreign currency and measured by the spot exchange rate.

There is always a one-to-one ratio between the hedged underlying instrument and the hedging instrument.

At December 31, 2013 and 2012, the Bank had derivative-related financial assets, which amounted to \$49,769 and \$43,349, respectively. Such assets had the credit quality shown on the following page.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

<u>Risk level</u>	<u>2013</u>	<u>2012</u>
Low	\$ 42,145	34,935
Satisfactory	7,487	7,954
Significant	137	65
High	-	<u>395</u>
Total	\$ 49,769	43,349
	=====	=====

The prospective effectiveness of the inception will be evaluated by comparing the critical terms of the hedged asset/liability, in connection with the hedging instruments. With this reconciliation and on this basis, the hedge is expected to be highly effective upon inception and over the life of the hedge.

Present effectiveness and prospective effectiveness of the life of the hedge will be evaluated at each month-end, by calculating the changes in cash flows of the derivative in all applicable periods in which the instrument has been designated as a hedge. These will be compared with changes in cash flows of the hedged item in the same period to which it applies.

The value of exposure to market risk of transactions with derivative financial instruments is included in the Value at Risk of HSBC's Global Market, which is explained in note 30.

If the primary position had not been hedged with the derivative financial transactions mentioned earlier, there would have been an adverse impact in the results of operations for 2013 of \$27 and an adverse impact for \$54 in 2012.

Fair value hedges

In respect of fair value hedges, at December 31, 2013, hedging instrument losses and gains in respect of the hedged position were \$456 and \$416, respectively and (\$241 and \$259, respectively in 2012).

Cash flow hedges

At December 31, 2013, the periods in which cashflows in respect of cashflow hedges are expected to occur are as follows:

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>2019</u>
Interest rate swaps	\$ (890)	(856)	(437)	-	-	-
Currency swaps	11	13	16	18	158	147
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
	\$ (879)	(843)	(421)	18	158	147
	====	====	====	==	====	====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The total amount recognised in comprehensive income during 2013 in respect to fair value changes in effective cash flow hedges was a profit of \$134 (profit of \$263 in 2012).

The amount reclassified from comprehensive income to the income statement for the years ended on December 31, 2013 and 2012 in respect of the unamortized fair value of re-designated hedges and in respect of the sale of the hedged positions (bonds) was an income of \$44 and \$90, respectively, which was registered in "Financial intermediation income".

During 2013 and 2012 the amount reclassified from comprehensive income to the income statement for the respective years in respect of the amortization of the fair value of swaps re-designated from cash flow swaps to net interest income was a loss of \$50 and \$27, respectively.

Compensation and net exposure to credit risk in derivatives

The Bank has the right to compensate derivative transactions at the time of settlement under the ISDA (International Swaps and Derivatives Association) and CSA (Credit Support Annex) which have jointly agreed with its customers. The effect that this right of reimbursement had over the credit risk exposure at December 31, 2013 and 2012 was \$21,502 and \$27,828, respectively.

Notional amounts

Notional amounts of contracts represent the derivatives volume outstanding and not the potential gain or loss associated with the market risk or credit risk of such instruments. The notional amounts represent the amount to which a rate or price is applied for determining the amount of cash flows to be exchanged.

At December 31, 2013 and 2012, the Bank did not provide non cash collateral in respect of derivative liabilities. Equally the Bank did not receive any non cash collateral from derivative counterparties.

At December 31, 2013 and 2012, the credit risk (including collaterals) in respect of derivative financial instruments, amounted to \$11,030 and \$6,428, respectively.

During the year ended December 31, 2013, the Bank's counterparties had defaults originating from derivative transactions that amounted to \$473. During the year ended December 31, 2012 there were no defaults resulting from derivative transaction contracts. At December 31, 2013 and 2012, the balance in sundry debtors resulting from defaults in this type of amounted to \$1,513 and \$945 respectively, of which \$1,425 as of December 31 2013 were reserved (\$945 in 2012).

At December 31, 2013 and 2012, the memorandum account "Amounts under derivative instruments", and fair value valuation are analyzed as shown in the following page.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

December 31, 2013

	Notionals								Fair Value								
	FX		Interest rate		Shares		Total		FX		Interest rate		Shares		Total		Net
	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	
Trading																	
Forwards	\$ 328,123	326,720	20,000	16,500	301	301	348,424	343,521	3,505	2,407	36	32	45	45	3,586	2,484	1,102
Options	11,473	10,247	14,255	17,724	-	-	25,728	27,971	83	83	128	92	-	-	211	175	36
Swaps	185,873	169,287	1,145,009	1,178,378	-	-	1,330,882	1,347,665	18,896	16,965	26,908	27,229	-	-	45,804	44,194	1,610
	525,469	506,254	1,179,264	1,212,602	301	301	1,705,034	1,719,157	22,484	19,455	27,072	27,353	45	45	49,601	46,853	2,748
Hedge																	
Swaps	-	282	17,120	16,352	-	-	17,120	16,634	-	27	168	763	-	-	168	790	(622)
	\$ 525,469	506,536	1,196,384	1,228,954	301	301	1,722,154	1,735,791	22,484	19,482	27,240	28,116	45	45	49,769	47,643	2,126

December 31, 2012

	Notionals								Fair Value								
	FX		Interest rate		Shares		Total		FX		Interest rate		Shares		Total		Net
	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	
Trading																	
Futures	\$ 868	-	65	-	-	-	933	-	-	-	-	-	-	-	-	-	-
Forwards	190,278	188,193	300,950	330,000	1,299	6,816	492,527	525,009	3,057	1,344	64	175	3	1	3,124	1,520	1,604
Options	19,212	19,157	31,913	-	-	-	51,125	19,157	-	-	106	54	-	-	106	54	52
Swaps	182,809	159,266	1,039,775	955,723	-	-	1,222,584	1,114,989	19,098	17,456	20,984	20,788	-	-	40,082	38,244	1,838
	393,167	366,616	1,372,703	1,285,723	1,299	6,816	1,767,169	1,659,155	22,155	18,800	21,154	21,017	3	1	43,312	39,818	3,494
Hedge																	
Swaps	-	1,533	12,325	9,402	-	-	12,325	10,935	-	121	37	982	-	-	37	1,103	(1,066)
	\$ 393,167	368,149	1,385,028	1,295,125	1,299	6,816	1,779,494	1,670,090	22,155	18,921	21,191	21,999	3	1	43,349	40,921	2,428

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(12) Loan portfolio-

At December 31, 2013 and 2012 the loan portfolio and the credit commitments are analyzed as follows:

	<u>2013</u>	<u>2012</u>
Total loan portfolio, shown in the consolidated balance sheet	\$ 204,990	198,979
Recorded in memorandum accounts (note 27a):		
Guarantees	-	4
Lending commitments	<u>25,561</u>	<u>25,222</u>
	\$ 230,551	224,205
	=====	=====

(a) Classification of current and past due loan portfolio by currency, rated portfolio, economic sector and by aging of past due loans-

At December 31, 2013 and 2012, the classification of current and past due loan portfolios by currency, which includes economic sector, rated portfolio and ageing of past due loans is shown in the following page.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2013 and 2012

(Millions of pesos)

Portfolio	Commercial activity		Financial institutions		Government entities		Consumer		Residential mortgages		Total	
	2013	2012	2013	2012	2013	2012	2013	2012	2013	2012	2013	2012
Current:												
Pesos	\$ 83,048	84,157	4,219	4,593	18,068	27,458	37,675	33,585	23,468	18,063	166,478	167,856
Foreign currency	25,159	25,007	120	230	65	649	-	-	-	-	25,344	25,886
UDIS	-	-	-	-	-	-	-	-	1,012	1,224	1,012	1,224
Total	108,207	109,164	4,339	4,823	18,133	28,107	37,675	33,585	24,480	19,287	192,834	194,966
Past due:												
Pesos	8,919	1,236	3	3	45	-	1,788	1,302	631	554	11,386	3,095
Foreign currency	698	836	-	-	-	-	-	-	-	-	698	836
UDIS	-	-	-	-	-	-	-	-	72	82	72	82
Total	9,617	2,072	3	3	45	-	1,788	1,302	703	636	12,156	4,013
Total:												
Pesos	91,937	85,393	4,222	4,596	18,113	27,458	39,463	34,887	24,099	18,617	177,834	170,951
Foreign currency	25,887	25,843	120	230	65	649	-	-	-	-	26,072	26,722
UDIS	-	-	-	-	-	-	-	-	1,084	1,306	1,084	1,306
Total	\$ 117,824	111,236	4,342	4,826	18,178	28,107	39,463	34,887	25,183	19,923	204,990	198,979
Classification by activity												
Manufacturing	\$ 63,109	61,349	-	-	-	-	-	-	-	-	63,109	61,349
Agriculture, forestry and fishing	10,596	9,469	-	-	-	-	-	-	-	-	10,596	9,469
Trade and tourism	21,249	21,893	-	-	-	-	-	-	-	-	21,249	21,893
Services	22,870	18,525	-	-	-	-	-	-	-	-	22,870	18,525
Financial services	-	-	2,074	1,546	-	-	-	-	-	-	2,074	1,546
Credit Unions	-	-	1,046	932	-	-	-	-	-	-	1,046	932
Municipalities	-	-	-	-	1,085	1,280	-	-	-	-	1,085	1,280
States	-	-	-	-	7,636	8,716	-	-	-	-	7,636	8,716
Credit to the Federal Government (support programs)	-	-	-	-	386	582	-	-	-	-	386	582
Other government entities (see note 12a)	-	-	-	-	9,071	17,529	-	-	-	-	9,071	17,529
Others to financial organizations	-	-	1,222	2,348	-	-	-	-	-	-	1,222	2,348
Automobile credit	-	-	-	-	-	-	2,479	2,669	-	-	2,479	2,669
Credit Card	-	-	-	-	-	-	19,115	17,374	-	-	19,115	17,374
Multicredit	-	-	-	-	-	-	15,808	13,504	-	-	15,808	13,504
Fixed payment	-	-	-	-	-	-	2,061	1,340	-	-	2,061	1,340
Construction and housing	-	-	-	-	-	-	-	-	25,183	19,923	25,183	19,923
Total	\$ 117,824	111,236	4,342	4,826	18,178	28,107	39,463	34,887	25,183	19,923	204,990	198,979
Past due loans by aging												
From 1 to 180 days	\$ 2,448	689	-	3	45	-	1,778	1,286	518	540	4,789	2,518
From 181 to 365 days	5,927	133	3	-	-	-	10	15	106	96	6,046	244
From 1 to 2 years	74	495	-	-	-	-	-	1	51	-	125	496
More than 2 years	1,168	755	-	-	-	-	-	-	28	-	1,196	755
Total	\$ 9,617	2,072	3	3	45	-	1,788	1,302	703	636	12,156	4,013

NOTE: The amounts above are for cumulative amounts of principal (for 2013 \$203,890 and 2012 \$198,065) and interest (for 2013 \$1,100 and 2012 \$914) which are classified in the consolidated balance sheets of the Bank as assets under the caption of current and past due loans.

Loan portfolio rated	2013	2012	2013	2012	2013	2012	2013	2012	2013	2012	2013	2012
Portfolio rating risk												
A-1 and A-2 (A-Minimum in 2012)	110,258	102,942	2,677	3,543	10,542	11,362	2,721	7,563	22,244	17,337	148,442	142,747
B-1, B-2 and B-3 (B-Low in 2012)	18,801	28,932	1,665	1,283	4,191	8,124	32,226	24,077	2,526	2,135	59,409	64,551
C-1 and C-2 (C-Medium in 2012)	3,888	3,428	-	-	2,833	15	2,644	1,907	401	448	9,766	5,798
D-High	8,942	297	-	-	228	-	1,816	1,302	12	3	10,998	1,602
E-Irrecoverable	1,496	863	-	-	-	8	56	38	-	-	1,552	909
Total portfolio rated	143,385	136,462	4,342	4,826	17,794	19,509	39,463	34,887	25,183	19,923	230,167	215,607
Exempt portfolio	-	-	-	-	384	8,598	-	-	-	-	384	8,598
Total portfolio	\$ 143,385	136,462	4,342	4,826	18,178	28,107	39,463	34,887	25,183	19,923	230,551	224,205
Allowance and percentage												
A-1 and A-2 (A-Minimum in 2012)	\$ 600	571	15	21	59	58	25	44	65	45	764	739
B-1, B-2 and B-3 (B-Low in 2012)	423	1,287	79	65	125	385	2,327	2,362	154	115	3,108	4,214
C-1 and C-2 (C-Medium in 2012)	316	1,238	-	-	207	3	984	725	172	150	1,679	2,116
D-High	4,108	227	-	-	67	-	1,365	893	8	2	5,548	1,122
E-Irrecoverable	803	863	-	-	-	8	56	38	-	-	859	909
Total	6,250	4,186	94	86	458	454	4,757	4,062	399	312	11,958	9,100
Additional reserves	121	19	-	-	-	-	129	200	15	62	265	281
Total	\$ 6,371	4,205	94	86	458	454	4,886	4,262	414	374	12,223	9,381
General and specific allowances												
General	\$ 600	571	15	21	59	58	25	45	71	58	770	753
Specific	5,771	3,634	79	65	399	396	4,861	4,217	343	316	11,453	8,628
Total	\$ 6,371	4,205	94	86	458	454	4,886	4,262	414	374	12,223	9,381

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Unsecured loans to IPAB:

On September 27, 2002, the Bank granted a \$47,357 (nominal) loan to IPAB. The loan was documented by a promissory note that may only be endorsed to the Central Bank as a guarantee for the note amount. In addition, on May 12, 2005, the Bank granted to IPAB an unsecured loan for a total nominal amount of \$5,000. Finally on May 31, 2007, the Bank and IPAB signed a new agreement to document the consolidated principal outstanding balance as of that date amounting to of \$29,058. In accordance to the aforementioned agreement, the total balance was split into four tranches of \$7,265 each, which mature between May and December 2013, payments in advance are permitted. Each tranche bears interest at an annual rate equal to the annual yield rates of 28-day CETES plus 56 basis points. At December 31, 2013 the four loan tranches have been settled in accordance with the maturity dates set forth in the debt recognition agreement. At December 31, 2012 the outstanding balance of this loan amounted to \$8,016 and was included in the loan portfolio within "Loans to government entities".

Federal Government support programs:

As a result of the economic crisis in 1995, the Federal Government and the Mexican Bankers' Association established loan support programs and agreements with debtors of credit institutions named Additional Benefits to Housing Loan Debtors (BADCV, for its acronym in Spanish).

The financial support programs and agreements consist of discounts granted to debtors, which are generally absorbed proportionately by the Federal Government and the Bank, in accordance with the terms of each program. These discounts were applied in each payment of the loans subject to the program. On July 15, 2010, the Bank signed an agreement with the Federal Government for an early termination of the support programs for housing loans. This early termination scheme (ETA, for its acronym in Spanish) consisted that the qualified loans received on or before December 31, 2010 the benefit of the discount on the unpaid balance of the loan. The discount absorbed by the Federal Government will be paid to the Bank in five equal installments, the first in December 2011 and the rest in the months of June of the years 2012-2015, to which they will add a financial cost, based on the 91 days treasury certificates rate. The payment of each installment is subject to the delivery of a series of reports to the Banking Commission. As of December 31, 2013 and 2012, the amount receivable from the Federal Government in connection with discounts granted and the costs related to the Bank and the ETA are analyzed as follows:

	<u>2013</u>		<u>2012</u>	
	<u>Portfolio</u>	<u>Cost</u>	<u>Portfolio</u>	<u>Cost</u>
ETA/BADCV	\$ 386	3	582	10
	===	=	===	==

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The discounts related to the early termination agreement are shown as follows:

	<u>In charge to</u>	
	<u>Bank</u>	<u>Federal Government</u>
Discounts granted	\$ 457	973
Additional discount granted by the Bank	<u>93</u>	<u>-</u>
Discount granted at December 31, 2010	550	973
Discounts to unallowed credits ^(a)	(2)	(3)
Discounts of credits that did not demonstrated compliance with payment ^(b)	(12)	(26)
Restructured loans under the agreement formalized up to the cut-off date	<u>(1)</u>	<u>-</u>
Total discounts granted at December 31, 2011	535	944
Total additional discounts granted by the Bank that did not belong to ETA	<u>(93)</u>	<u>-</u>
Total additional discounts granted by the Bank that belong to ETA	\$ 442	944
	===	===

^(a) Through communications issued in April 2011, the Banking Commission requested the replacement of the exhibits for the year ended on December 31, 2010, and subsequently, during the issuance of the report on the correct application (ETA report) on September 29, 2011, where the portfolio balances and the related discounts decreased for, with 28 credits defined as not subject to the ETA, 24 of which were benefited from the Discount Program.

^(b) This corresponds to the credit discounts that as of March 31, 2011 did not demonstrate a compliance with the payment and that would had been chargeable to the Federal Government, in the event of complying with such condition.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

As of December 31, 2010, the discount related to the Federal Government was reclassified to be presented as part of the accounts receivable from the Federal Government which are part of the current loans portfolio with government entities; the corresponding amount of discount related to the Bank was cancelled against the allowance for loan losses, in accordance with the special accounting criteria issued by the Banking Commission.

A reconciliation of movements in the allowance for loan losses related to the conditioned discount covered by the Bank is shown below:

Opening balance as of December 31, 2010	\$	70
Debt forgiveness, discounts and/or rebates		(2)
Conditioned discount assigned to the Bank		(550)
Allowance charged to the consolidated statement of operations		<u>496</u>
Final balance	\$	14
		===

Determination of obligations of the Federal Government:

The final base amount determined through the ETA Report is \$944, divided in five installments of \$189 each. The first installment was received on December 31, 2013 and the remaining installments will be payable on the first banking day of June, from 2014 to 2015. Accordingly, the balance receivable as of December 31, 2013 and 2012 by ETA amounts to \$378 and \$566, respectively, of principal, plus \$8 and \$15 corresponding to the accrued not collected financial cost.

The discounts granted due from the Government in Mexican pesos or UDIS related to those credits that should have shown sustained payment by March 31, 2011, according to the agreement, amounts to \$167 at December 31, 2010.

There were no discount in charge to the Government related to credits in UDIS for which they received prior discounts over the outstanding balance before they were incorporated in to the "Discount program", as referred at the numeral 3.1.2 of the Circular 1430 issued by the Banking Commission.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

At December 31, 2010 there were some clients that did not meet the requirements to be incorporated into to ETA. However, in accordance with the actual rules it is still possible that they will subsequently be incorporated in to the program; in such case the Bank must have to absorb 100% of the discount granted. The maximum amount of discount that the Bank would absorb for these credits at December 31, 2013 and 2012, amount to \$7 and \$20, respectively.

The numbers of securities related to BADCV that are held by the Bank at December 31, 2013 and 2012 are shown as follows:

	<u>Trust Program</u>	<u>number</u>	<u>Term</u>	<u>Special Due date</u>	<u>Special “C” CETES</u>
Programs to support Debtors of mortgage credits	421-5	20 Years	13/07/2017	12,549,378	766,145
	422-9	25 Years	07/07/2022	5,772,652	184,517
	423-2	30 Years	01/07/2027	30,074,223	-
Program to support the construction of houses in the stage of individualize credits		25 Years - from 230 to 330 thousand Udis	11/08/2022	74,389	50,693

(b) Program for the support of people affected by tropical storm Manuel and hurricane Ingrid:

Due to the natural disasters caused by the hydro-meteorological events “Ingrid” and “Manuel” that affected several Mexico locations and with a view to supporting borrowers who were affected by such natural phenomena while trying to promote the stability of credit institutions, through official document P065/2013 dated October 18, 2013, the Banking Commission authorized the country’s credit institutions certain special accounting criteria applicable to loans of customers with domiciles or source of payment of their loans in locations in the Mexican Republic that were declared in emergency or natural disaster by the Ministry of the Interior through publication in the DOF during the months of September and October 2013. The authorized accounting criteria refer to not considering as past due or restructured portfolio in accordance with criterion B-6 of the Provisions, the loans to which the benefit referred to in the following paragraph is applied, provided the following is complied: 1) the loan was recognized as performing at the date such events hit; 2) the restructuring or renovation procedures end by 120 natural days after the date such events hit; and 3) the new maturity of is not greater than three months after the date on which the loans became due and payable.

The benefit offered by the Bank to its customers who so request consists of the total deferral of their payments for up to three months. The program applies for mortgage-backed housing loans, automobile loans, personal loans, payroll loans, credit cards and PYME loans.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

At December 31, 2013, the amount that would have been recorded and presented on the consolidated balance sheet and in the consolidated statement of income, had the special accounting criteria authorized by the Banking Commission not been applied, which relates to interest, was immaterial.

Since the benefit applied by the Bank consisted only of the deferral of the payment of principal and interest thereon for up to 3 months, it was not necessary to make any entries in the accounting associated with the application of this disaster relief program.

*(c) Additional loan portfolio information -**Commission by type of loan:*

For the years ended at December 31, 2013 and 2012, commissions by type of loan included in commissions and fees collected within the consolidated statements of income, are presented in as follows:

	Amount	
	<u>2013</u>	<u>2012</u>
Commercial	\$ 293	383
Consumer	2,380	2,009
Mortgage	<u>31</u>	<u>40</u>
Total	\$ 2,704	2,432
	=====	=====

Below shows the increases in deferred credits account for the initial granting of credits for the years ended at December 31, 2013 and 2012.

	Amount	
	Commissions	
	<u>2013</u>	<u>2012</u>
Consumer	\$ 15	16
Commercial	162	269
Mortgage	<u>69</u>	<u>23</u>
Total	\$ 246	308
	====	====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

During the years ended at December 31, 2013 and 2012, \$210 and \$212, respectively, were recorded corresponding to the accrued commissions by the initial granting of credits of the period, using the straight line method, which were registered in the line "Interest Income" in the consolidated statement of income. The average weighted period (in months) for such commissions and fees are as follows:

Commercial	31
Consumer	35
Credit cards	12
Mortgages	201
	===

The initial costs and expenses for the issuance of credits related to the years ended December 31, 2013 and 2012 amounts to \$157 and \$141, respectively. These amounts relate to payment of commissions and underwriting credits.

Annual weighted lending rates:

During 2013 and 2012, the annual weighted lending rates (unaudited information) were as shown in the following page.

	<u>2013</u>	<u>2012</u>
Commercial loans	7.80%	10.04%
Financial entities	5.12%	5.87%
Personal loans	26.85%	26.41%
Mortgages loans	9.91%	10.16%
Government entities	5.96%	6.07%

Loans discounted with recourse:

Mexican Government has established certain funds to promote the development of specific areas of agriculture, cattle ranching, industrial and tourism sectors, which are managed mainly by the Central Bank, Nacional Financiera SNC (a national development bank, NAFIN), the National Foreign Trade Bank, and the Guarantee Fund for Agricultural Development by discounting loans with recourse.

At December 31, 2013 and 2012, the amount of loans granted under these programmes amounted to \$10,062 and \$10,662, respectively, and the related liability is included in "Due to banks and other institutions" (note 20).

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Restructured and renewed loans:

At December 31, 2013 and 2012, restructured and renewed loans are analyzed as follows:

	2013			
	Renewed and restructured portfolio			Modified not considered as restructured ⁽⁴⁾
	Past due restructured ⁽¹⁾	Transfer to past due ⁽²⁾	Stayed current ⁽³⁾	
Commercial loans	\$ 1,143	624	3,338	6,181
Government entities	-	-	1,325	-
Consumer loans	19	-	55	-
Credit card	106	-	314	-
Mortgage loans	<u>143</u>	<u>-</u>	<u>669</u>	<u>-</u>
	\$ 1,411	624	5,701	6,181
	=====	====	=====	=====
	2012			
	Renewed and restructured portfolio			Modified not considered as restructured ⁽⁴⁾
	Past due restructured ⁽¹⁾	Transfer to past due ⁽²⁾	Stayed current ⁽³⁾	
Commercial loans	\$ 673	694	3,776	6,540
Government entities	-	-	9,369	-
Consumer loans	16	-	32	-
Credit card	103	-	255	-
Mortgage loans	<u>92</u>	<u>-</u>	<u>652</u>	<u>-</u>
	\$ 884	694	14,084	6,540
	====	====	=====	=====

(1) Nonperforming loans that was restructured or renewed.

(2) Restructuring or renewals of loans with a single payment of principal at maturity and periodic interest payments and credits with a single payment of principal and interest at maturity, which were transferred to past due loans for been restructured or renewed.

(3) Restructured or renewed loans that remained in current portfolio under paragraphs 57 to 61 of Criteria B-6 "loan portfolio" of Annex 33 of the Provisions.

(4) Modified loans that were not considered as restructured according to paragraph 62 of Criteria B-6 "loan portfolio" of Annex 33 of the Provisions.

For the years ended December 31, 2013 and 2012, the amount of interest income recognised due to the restructuring of overdue loans was \$1 each year. In respect of loans to small and medium enterprises in the commercial portfolio, with the aim of reducing the level of the Bank's credit risk, there is an agreement with NAFIN to promote this type of credits, where NAFIN supports up to 50%, 90% or 100% of the loan granted depending on the applicable program. For the years ended December 31, 2013 and 2012, NAFIN supported \$3,874 and \$3,685, respectively.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Restructuring processes entail the granting of a reduction in interest rates, a waiting period for complying with the payment obligations, the cancellation of any portion of capital, default interest and commissions. At December 31, 2013 and 2012, debts cancelled totaled \$27 and \$28, respectively. Sometimes, in the restructuring process additional guarantees such as mortgage guarantees are obtained. At December 31, 2013, the value of such additional guarantees aggregates \$137 (\$125 in 2012).

Past due loan portfolio

Nominal interest that would have accrued in 2013 from the past due loan portfolio amounted to \$221 (\$113 in 2012).

An analysis of the annual movement of past due loans for the years ended December 31, 2013 and 2012, is shown as follows:

	<u>2013</u>	<u>2012</u>
Balance at beginning of year	\$ 4,013	5,082
Transfers from current to past due loan portfolio	23,922	12,297
Transfers to current loan portfolio by restructures and renewals	(335)	(492)
Credits collected:		
Cash collections	(4,287)	(2,738)
Collection in kind	(15)	(193)
Write offs	(5,356)	(5,817)
Transfer to current loan portfolio	(5,800)	(4,063)
Foreign exchange	<u>14</u>	<u>(63)</u>
Balance at end of year	\$ 12,156	4,013
	=====	=====

During 2013 and 2012, there were no write-offs of loans granted to related parties.

For the year ended at December 31, 2013, the amount of recoveries for those loans that were previously written-off amounted \$760 (\$705 in 2012).

Impaired loans:

At December 31, 2013 and 2012, the balance of impaired commercial loans is \$10,665 and \$1,168 respectively, of which \$1,096 and \$189 are recorded as current loans and \$9,569 and \$979 as past due loans, respectively.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Risk concentration:

As of December 31, 2013 and 2012, the Bank maintains three loans that exceeded the 10% limit of its basic capital at September 30, 2013 of \$4,313 (\$3,695 at September 30, 2012). These loans represent the three main debtors of the Bank amounting to \$12,067 (\$16,722 in 2012) that represents the 27.98% (43.58% in 2012) of the basic capital.

Securitisation of mortgage portfolio:

Outstanding securitisation transactions as of December 31, 2013 and 2012, relate to transactions undertaken in 2008 and 2007, by means of transferring of all of the Bank's risks and rewards of such mortgage portfolio without reserves or limitations in favour of three Trusts (used as a securitization vehicle). The Trusts issued certificates that were acquired by the public and a subordinated trust acknowledgment, which gives the Bank the right to receive any remaining funds of the Trust. The Trust note is recorded on the available-for-sale investment portfolio on the consolidated balance sheet.

The amounts of the portfolio that was sold in the market, as well as the conditions of the certificates issued by the stockmarket certificate issued by the Invex Trusts are as follows:

<u>Invex</u>	<u>Date of issuance</u>	<u>Nominal portfolio sold</u>	<u>Cash received</u>	<u>Acknowledgment</u>	<u>Maturity date</u>	<u>Stockmarket certificates interest rate</u>			
						<u>Series "A"</u>	<u>Series "B"</u>	<u>Series "A1"</u>	<u>Series "B1"</u>
I	22-mar-07	\$ 2,525	2,474	25	1 to 30 years	8.24%	9.58%	-	-
II	2-oct-07	3,538	3,457	36	2025	8.80%	10.11%	-	-
III	4-sep-08	1,663	1,483	163	2028	-	-	9.99%	10.16%
		=====	=====	====		=====	=====	=====	=====

The Bank acquired the subordinated trust acknowledgments, which grant the right to any remainder of the mortgage portfolio upon payment of the amounts due under the certificates.

As of December 31, 2013 and 2012, the book value of the subordinated trust acknowledgments is recognized in "Benefits receivable on securitization transactions" and is analyzed as follows:

		<u>2013</u>	<u>2012</u>
Original amount of the certificates	\$	224	224
Recoveries of the values of trust acknowledgments		(2)	-
Valuation		(40)	(69)
Trust certificates	\$	182	155
		====	====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The result of trust acknowledgment valuations is determined considering the fair value of the notes issued by the trustee, which is obtained through a price vendor.

In the event that the total amount due of the certificates is less than 10% of the par value of the total amount of the certificates on the date of the offering, the Bank shall have the option to repurchase the remaining portfolio of the trust and with such proceeds the outstanding certificates would be repaid.

The Bank executed a service provision agreement, through which the Bank provides the administration and collection of the mortgage portfolio sold in the market, in exchange for a commercial commission.

(d) Allowance for loan losses -

As explained in notes 3(1) and 30, an allowance is established to provide for credit risks associated with the collection of the Bank's loan portfolio.

At December 31, 2013 and 2012 the allowance for loan losses, analyzed in section (a) of this note is shown below:

		<u>2013</u>	<u>2012</u>
Rated loan estimate	\$	11,958	9,100
Additional reserves, including past due interest		<u>265</u>	<u>281</u>
Total allowance for loan losses	\$	12,223 =====	9,381 =====

The classification by risk grade of the commercial portfolio, financial entities and government entities credit reserves at December 31, 2013 and 2012, is as follows:

		<u>2013</u>	<u>2012</u>
A-1	\$	447	393
A-2		227	269
B-1		211	706
B-2		132	558
B-3		284	475
C-1		423	932
C-2		100	313
D		4,283	214
E		<u>816</u>	<u>885</u>
	\$	6,923 =====	4,745 =====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The following is an analysis of the movements of the allowance for the years ended December, 31, 2013 and 2012:

		<u>2013</u>	<u>2012</u>
Balance at beginning of year	\$	9,381	10,900
Increase charged to income		8,083	5,534
Exchange rate valuation effects		3	(145)
Effect on stockholders equity by the change in the methodology of commercial loans (note 4)		799	-
Reverse of excess in allowance for loan losses		(6)	(857)
Applications:			
Write-offs		(5,765)	(5,506)
Debt forgiveness		<u>(272)</u>	<u>(545)</u>
Balance at end of year	\$	12,223	9,381
		=====	=====

At December 31, 2013 and 2012, reverse of excess in allowance for loan losses of commercial loans in the amount of \$6 and \$857, respectively, were recorded in the caption "Other operating income, net" (refer to note 28c).

(e) Sale of written-off portfolio -

During 2013 and 2012 the Bank did not sale previously written off portfolio.

The Bank's credit policies are disclosed in note 31.

(13) Other accounts receivable -

At December 31, 2013 and 2012, other accounts receivable are analyzed as follows:

		<u>2013</u>	<u>2012</u>
Debtors on settlement transactions	\$	28,808	19,752
Due from employees		3,103	3,075
Granted collaterals in cash		6,167	6,598
Other debtors		3,685	3,716
Preventive estimations		<u>(1,470)</u>	<u>(1,169)</u>
	\$	40,293	31,972
		=====	=====

The balance of settlement accounts recorded under other accounts payable at December 31, 2013 and 2012 was \$37,519 and \$29,556, respectively, and recognized in the accounting item of "Settlement transactions".

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(14) Foreclosed assets -

As of December 31, 2013 and 2012, foreclosed assets or assets received in lieu of payment are analyzed as follows:

	<u>2013</u>		<u>2012</u>	
	<u>Amount</u>	<u>Reserve</u>	<u>Amount</u>	<u>Reserve</u>
Securities	\$ -	-	<u>31</u>	<u>(31)</u>
Property:				
Land	10	(6)	9	(6)
Buildings	<u>216</u>	<u>(61)</u>	<u>269</u>	<u>(54)</u>
	<u>226</u>	<u>(67)</u>	<u>278</u>	<u>(60)</u>
	<u>226</u>	<u>(67)</u>	<u>309</u>	<u>(91)</u>
Foreclosed assets, net	\$ 159		218	
	===		===	

The charge to the income is related to the valuation reserve of foreclosed assets in 2013 amounted to \$27 (\$34 in 2012).

The total foreclosed property includes constructions recorded as restricted assets due to the sale executed via reservation of title agreement, which amounts to \$9, with a reserve for \$5 generated at December 31, 2013 (\$40 and \$14, respectively in 2012).

(15) Property, furniture and equipment-

Property, furniture and equipment at December 31, 2013 and 2012 are shown in the following page.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

		<u>2013</u>	<u>2012</u>	<u>Annual depreciation and amortization rate</u>	<u>Useful life in years</u>
Property	\$	2,214	2,378	2% to 5%	20-50
Office furniture and equipment		1,474	1,586	10%	10
Computer equipment		4,006	4,951	Various	3 to 7
Transportation equipment		6	6	25%	4
Installation expenses		5,031	4,582	5% and 10%	10 to 20
Other equipment		<u>2,475</u>	<u>2,274</u>	Various	
		15,206	15,777		
Accumulated depreciation and amortization		<u>(8,768)</u>	<u>(9,060)</u>		
		6,438	6,717		
Land		<u>489</u>	<u>490</u>		
	\$	<u>6,927</u>	<u>7,207</u>		
		=====	=====		

Depreciation and amortization charged to the consolidated statement of income in 2013 and 2012 amounted to \$1,274 and \$1,286, respectively.

In 2012, as a result of the evaluation to the useful life of certain property owned by subsidiaries of the Bank it was decided to extend the depreciation of these from 20 to 50 years, derived of this change the annual depreciation expense decreased in \$65.

As a result of the conduction of a physical inventory of Bank owned assets, a negative adjustment was recorded in their net book value of \$86, which was recognized in the year's income under "Other operating income, net".

During the years ended at December 31, 2013 and 2012 several properties were sold with a book value of \$5 and \$42, respectively, generating a profit of \$1 and \$50, respectively, which were recorded as "Other operating income, net" (refer to note 28c).

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(16) Permanent investments in shares-*Investments in associates and other permanent investments*

At December 31, 2013 and 2012, permanent investments in shares classified by activity, are analyzed as follows:

	<u>2013</u>	<u>2012</u>
Associated and affiliated companies:		
Supplementary banking services	\$ 122	113
Mutual funds	9	8
Security and protection	<u>5</u>	<u>4</u>
	136	125
Others	<u>12</u>	<u>14</u>
	\$ 148	139
	====	=====

The recognition of the equity in the results of associated and affiliated companies represented a profit of \$43 in 2013 (\$35 in 2012).

(17) Other assets, deferred charges and intangibles assets-

At December 31, 2013 and 2012 other assets deferred charges and intangibles assets include:

	<u>2013</u>	<u>2012</u>
Recoverable taxes	\$ 727	42
Pre-paid labour obligations (note 21)	1,078	894
Pre-paid services and commissions	801	1,334
Software, net	1,025	790
Other intangibles assets, net	<u>6</u>	<u>16</u>
	\$ 3,637	3,076
	====	=====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The movement for the years ended at December 31, 2013 and 2012 of other assets, deferred charges and intangible assets are analyzed as follows:

		<u>2013</u>	<u>2012</u>
Balance at beginning of year	\$	3,076	3,506
Movements for the year from:			
Taxes		685	(242)
Software (*)		438	408
Software impairment		(47)	(110)
Amortization for the year		(128)	(340)
Prepaid expenses		(466)	(37)
Others		<u>79</u>	<u>(109)</u>
Balance at end of year	\$	3,637	3,076
		=====	=====

(*) Software developed internally, which is amortized over a five-year period.

As a result of a corporate restructuring carried out during 2012, the use of the systems has been evaluated, as well as the probable impairment in the useful life of them, resulting in the cancellation of a number of projects and, as a consequence, of the related software as shown below:

		<u>Acquisition Cost</u>	<u>Accrued amortization</u>	<u>Impairment</u>	<u>Book Value</u>	<u>Annual amortization rate</u>
<u>2012</u>						
Software	\$	2,964	(910)	(1,264)	790	20%
		=====	=====	=====	=====	=====

At December 31, 2013 and 2012 impairment losses of \$47 and \$110, respectively were recorded in the consolidated statement of income within the "Other operating income" caption.

Intangible assets that are shown in the consolidated balance sheet do not include any restriction, are not considered as debt guaranty; there are no contractual commitments, related to the acquisition thereof.

(18) Deposits funding-

The weighted average deposit rates (unaudited) for the years ended December 31, 2013 and 2012 are analyzed as follows:

	<u>2013</u>			<u>2012</u>		
	<u>Pesos</u>	<u>Dollars</u>	<u>UDIS</u>	<u>Pesos</u>	<u>Dollars</u>	<u>UDIS</u>
Demand deposits	0.92	0.05	-	1.30	0.05	-
Time deposits	3.41	0.19	0.16	3.91	0.11	0.22
	=====	=====	=====	=====	=====	=====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(19) Bank bonds-

At December 31, 2013 and 2012, the Bank has made the following issuances under the bank bonds program:

Issuance Day	Reference Rate	Maturity Day		<u>2013</u>	<u>2012</u>
May 10, 2006 ⁽¹⁾	TIEE – 0.01%	May 1, 2013	\$	-	2,000
June 29, 2006 ⁽¹⁾	TIEE – 0.01%	May 1, 2013		-	1,220
May 10, 2006 ⁽²⁾	9.08%	April 27, 2016		1,000	1,000
December 9, 2013 ⁽¹⁾	TIEE –30 bp	December 3, 2018		2,300	-
December 9, 2013 ⁽²⁾	8.08%	November 27, 2023		<u>2,700</u>	-
				6,000	4,220
Accrued Interest				<u>36</u>	<u>24</u>
Total of Bank bonds			\$	<u>6,036</u>	<u>4,244</u>
				=====	=====

⁽¹⁾ Interest payments on a monthly basis

⁽²⁾ Interest payments on a semi-annual basis

bp - basis points

(20) Due to banks and other institutions-

At December 31, 2013 and 2012, due to banks and other institutions are analyzed as follows:

	<u>2013</u>		<u>2012</u>	
	<u>Term</u>		<u>Term</u>	
	<u>Short</u>	<u>Long</u>	<u>Short</u>	<u>Long</u>
Pesos:				
Multiple bank (on demand)	\$ 2,900	-	1,980	37
Development bank ⁽¹⁾	3,309	-	4,675	-
Promotion funds ⁽¹⁾	<u>4,187</u>	<u>1,703</u>	<u>3,176</u>	<u>1,553</u>
	<u>10,396</u>	<u>1,703</u>	<u>9,831</u>	<u>1,590</u>
Foreign currencies translated into pesos:				
Commercial bank ⁽²⁾	7,548	-	10,416	-
Development bank ⁽¹⁾	15	7	36	10
Promotion funds ⁽¹⁾	<u>407</u>	<u>434</u>	<u>837</u>	<u>7</u>
	<u>7,970</u>	<u>441</u>	<u>11,289</u>	<u>17</u>
Total by term	<u>18,366</u>	<u>2,144</u>	<u>21,120</u>	<u>1,607</u>
Total due to Banks and other institutions	\$ 20,510		22,727	
	=====		=====	

⁽¹⁾ Funds granted under the development fund program (refer to note 12c).

⁽²⁾ Resources from related parties.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions pesos)

At December 31, 2013 and 2012, the annual average rates (unaudited) are analyzed as follows:

	<u>Pesos</u>		<u>Foreing currency</u>	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
Development bank	5.46%	6.00%	3.11%	3.35%
Promotion funds	3.83%	4.06%	1.21%	1.05%
	=====	=====	=====	=====

(21) Employee benefits-

The Bank maintains a defined pension plan that covers all employees who reach 60 years old with 5 years of service or 55 years old with 35 years of service. The benefits are based on years of service and the employee's compensation. The Bank paid annual contributions to the plan equal to the maximum amount that can be deducted for income tax purposes based on the projected unit credit method.

In addition to the defined benefit pension plan, the Bank sponsors other postretirement benefits through pantry vouchers, life insurance and major medical plan that provide postretirement medical benefits to employees who have rendered their services to the Bank until their retirement date and for their wife, parents and child under 21 years.

Moreover, the Bank grants short-term benefits such as paid vacations, vacation premiums, savings fund, year-end bonus, etc.

Effective April 2004, the defined contribution component was included in the pension plan and starting 2007, in the postretirement medical benefits plan. At present, only unionized workers and those workers who expressed their intention to continue under the defined contribution component participate in the defined pension plan and in the postretirement benefits. The remaining employees elected to move to the defined contribution pension plan and the defined contribution postretirement medical benefits plan.

In addition to the defined benefit pension plan, the post-retirement benefit pension plan and the defined contribution pension plan, the Bank pays the benefits provided by the Federal Labor Law in relation to the legal severance payment for reasons other than restructuring, as well as seniority premium. The latter is paid in the event of death, invalidity, resignation after fifteen years of service and severance payment for reasons other than restructuring and retirement.

The amounts for short-term benefits payable at December 31, 2013 amounted to \$1,282 (\$1,421 in 2012), and are recorded under the caption "Sundry creditors and other accounts payable" in the consolidated balance sheet.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Cash flows -

Contributions and benefits paid were as follows:

	Funds contributions		Paid benefits	
	2013	2012	2013	2012
Termination	\$ 26	22	26	31
Retirement	315	204	167	160
Other post retirement benefits	<u>236</u>	<u>260</u>	<u>217</u>	<u>189</u>
	\$ <u>577</u>	<u>486</u>	<u>410</u>	<u>380</u>
	===	===	===	===

The cost, obligations and other pension plans, seniority premiums and fees at the end of the employment relationship other than restructuring, referred to in note 3(u) were determined based on estimates prepared by independent actuaries at December 31, 2013 and 2012. The components of net cost of the years ended December 31, 2013 and 2012 are shown as follows:

	Benefits					
	2013			2012		
	Termination	Retirement	Total	Termination	Retirement	Total
Net periodic cost:						
Service cost	\$ 69	63	132	66	30	96
Interest cost	28	152	180	35	158	193
Return on plan assets	(2)	(90)	(92)	(3)	(94)	(97)
Net actuarial gain or loss	(83)	59	(24)	(25)	31	6
Labour cost of past services:						
Amortization of prior services and plan amendments	-	15	15	-	16	16
Amortization of liability in transition	-	-	-	38	8	46
Effect from early settlement prior to early extinction	<u>-</u>	<u>(16)</u>	<u>(16)</u>	<u>(8)</u>	<u>(35)</u>	<u>(43)</u>
Net period cost	\$ <u>12</u>	<u>183</u>	<u>195</u>	<u>103</u>	<u>114</u>	<u>217</u>
	===	===	===	===	===	===

	Other Post-retirement benefits	
	2013	2012
Net periodic cost:		
Service cost	\$ 51	185
Interest cost	202	202
Return of plan assets	(177)	(186)
Net actuarial gain or loss	108	72
Amortization of liability in transition	-	19
Effect from early settlement prior to early extinction	<u>(3)</u>	<u>(57)</u>
Net periodic cost	\$ <u>181</u>	<u>235</u>
	===	===

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Below is the determination of liabilities for benefit plans at December 31, 2013 and 2012.

2013

	<u>Retirement benefits</u>		<u>Other</u>	
	<u>Seniority</u>	<u>Pension</u>	<u>Post-</u>	
	<u>Premium</u>	<u>Plan</u>	<u>retirement</u>	<u>Total</u>
			<u>Benefits</u>	
Defined benefit obligation:				
Defined benefit obligation at beginning of the year	\$ 52	2,617	3,533	6,202
Service cost	4	59	51	114
Interest cost	3	149	201	353
Actuarial gain or loss	(9)	(55)	(417)	(481)
Paid benefits	(3)	(164)	(217)	(384)
Reduction/liquidation effect	-	<u>(105)</u>	<u>(69)</u>	<u>(174)</u>
Defined benefit obligation at end of the year	\$ 47	2,501	3,082	5,630
	==	=====	=====	=====

2012

	<u>Retirement benefits</u>		<u>Other</u>	
	<u>Seniority</u>	<u>Pension</u>	<u>Post-</u>	
	<u>Premium</u>	<u>Plan</u>	<u>retirement</u>	<u>Total</u>
			<u>Benefits</u>	
Defined benefit obligation:				
Defined benefit obligation at beginning of the year	\$ 38	2,052	2,654	4,744
Service cost	3	27	45	75
Interest cost	3	154	202	359
Actuarial gain or loss	16	661	844	1,521
Paid benefits	(3)	(158)	(188)	(349)
Past service cost	-	-	141	141
Reduction/liquidation effect	(5)	<u>(119)</u>	<u>(165)</u>	<u>(289)</u>
Defined benefit obligation at end of the year	\$ 52	2,617	3,533	6,202
	==	=====	=====	=====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Below is the determination of plan benefits assets at December 31, 2013 and 2012:

	<u>Retirement benefit</u>		<u>Other Post- retirement benefits</u>	<u>Total</u>
	<u>Seniority premium</u>	<u>Pension Plan</u>		
<u>2013</u>				
Plan assets:				
Plan assets at the beginning of the year	\$ (38)	(1,209)	(2,465)	(3,712)
Expected performance	(3)	(87)	(177)	(267)
Actuarial gain or loss	2	67	146	215
Company contributions	(8)	(307)	(236)	(551)
Paid benefits	3	164	217	384
Anticipated liquidations	-	<u>27</u>	<u>29</u>	<u>56</u>
Plan assets at the end of year	\$ (44)	(1,345)	(2,486)	(3,875)
	==	====	====	====
<u>2012</u>				
Plan assets:				
Plan assets at the beginning of the year	\$ (32)	(1,041)	(2,105)	(3,178)
Expected performance	(3)	(91)	(186)	(280)
Actuarial gain or loss	(1)	(57)	(123)	(181)
Company contributions	(5)	(200)	(260)	(465)
Paid benefits	3	158	188	349
Anticipated liquidations	-	<u>22</u>	<u>21</u>	<u>43</u>
Plan assets at the end of year	\$ (38)	(1,209)	(2,465)	(3,712)
	==	====	====	====

The Bank estimates that during 2014 they will make contributions to defined benefit plans amounting to \$221 (includes termination seniority premium).

Below are the categories of plan assets at December 31, 2013 and 2012:

	<u>Retirement benefit</u>		<u>Other Post- retirement benefits</u>
	<u>Seniority premium</u>	<u>Pension plan</u>	
<u>2013</u>			
<u>Fair value of the plan assets:</u>			
Local equity instruments	20%	20%	21%
Global equity instruments	9%	10%	10%
Debt instruments (nominal rate)	31%	32%	33%
Debt instrument (real rate)	33%	31%	35%
Short term debt instruments	<u>7%</u>	<u>7%</u>	<u>1%</u>
Total	100%	100%	100%
	====	====	====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

<u>2012</u>	<u>Retirement benefit</u>		<u>Other Post- retirement benefits</u>
	<u>Seniority premium</u>	<u>Pension plan</u>	
Fair value of the plan assets:			
Local equity instruments	20%	20%	20%
Global equity instruments	10%	10%	10%
Debt instruments (nominal rate)	28%	28%	28%
Debt instruments (real rate)	28%	28%	28%
Short term debt instruments	<u>14%</u>	<u>14%</u>	<u>14%</u>
Total	100%	100%	100%
	=====	=====	=====

The expected long-term return rate of the assets depends on the mix of the investment fund, while the information on the investment policy and the expected and current return depend on the portfolio assets.

According to the current Bank investment policy, the expected return of the assets is obtained as follows:

	<u>Asset distribution(1)</u>	<u>Expected return (2)</u>	<u>Total (1) x (2)</u>
Local equity instruments	20.0%	11.50%	2.30%
Global equity instruments	10.0%	8.30%	0.83%
Debt instruments (nominal rate)	<u>70.0%</u>	5.90%	<u>4.13%</u>
Total	100.0%		7.26%
	=====		=====

Below are the amounts of the last four preceding annual periods of the defined benefit obligation, fair value of plan assets, the status of the plan and the experience adjustments arising from the liabilities and assets of the plan.

	<u>Seniority premium</u>				
	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>
Defined benefit liabilities	\$ 47	52	39	37	29
Plan assets	(44)	(38)	(32)	(24)	(19)
Plan situation	3	14	7	13	10
Actuarial gain (loss):					
Plan liabilities	(9)	16	2	5	7
Plan assets	2	(2)	(3)	(1)	(2)
	==	==	==	==	==
	<u>Pension plan</u>				
	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>
Defined benefit liabilities	\$ 2,501	2,617	2,052	2,209	1,746
Plan assets	(1,345)	(1,209)	(1,041)	(1,044)	(947)
Plan situation	1,156	1,408	1,011	1,165	799
Actuarial gain (loss):					
Plan liabilities	(55)	662	40	218	352
Plan assets	67	(58)	40	(58)	(48)
	===	===	===	===	===

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

	Other post-retirement benefits				
	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>
Defined benefit liabilities	\$ 3,082	3,533	2,654	2,433	1,935
Plan assets	(2,486)	(2,465)	(2,105)	(2,036)	(1,857)
Plan situation	596	1,068	549	397	78
Experience adjustments:					
Plan liabilities	(417)	844	311	469	47
Plan assets	(146)	(123)	37	(77)	(105)
	=====	=====	=====	=====	=====

At December 31, 2013 and 2012 the present value of the liabilities for the benefits of the plans are as follows:

		Benefits				Other post-retirement benefits	
		<u>Termination</u>		<u>Retirement</u>		<u>2013</u>	<u>2012</u>
		<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>		
Acquired rights and obligations	\$	501	514	1,744	1,811	2,997	2,753
Amount		===	===	=====	=====	=====	=====

		Benefits				Other post-retirement benefits	
		<u>Termination</u>		<u>Retirement</u>		<u>2013</u>	<u>2012</u>
		<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>		
Defined benefit liabilities amount	\$	520	534	2,548	2,669	3,082	3,533
Fair value plan assets		(33)	(32)	(1,389)	(1,247)	(2,486)	(2,465)
Funds financial situation		487	502	1,159	1,422	596	1,068
Unrecognized past services:							
(Liabilities) / assets in transition		-	-	-	-	-	-
Plan modifications		-	-	(187)	(210)	-	-
Actuarial gain (loss)		-	-	(1,191)	(1,298)	(1,468)	(1,884)
Projected Liabilities / (Assets)	\$	487	502	(219)	(86)	(872)	(816)
		===	===	=====	=====	=====	=====

	<u>Termination and retirement benefits</u>		<u>Other post-retirement benefits</u>	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
Nominal discount rate used to show the present value of obligations	7.25%	5.90%	7.25%	5.90%
Nominal rate of increase in the levels of future salaries	4.75%	4.75%	4.75%	4.75%
Nominal rate of return expected in the plan assets	7.25%	7.25%	7.25%	7.25%
Medical inflation rate	-	-	6.75%	6.75%
Average remaining work life of employees (applicable to retirement benefits)	16.06	17.56	12.62	14.12

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

At December 31, 2013 and 2012, the amortization periods in years of the remaining items are shown as follows:

	<u>Retirement benefits</u>		<u>Other post-retirement benefits</u>
	<u>Seniority Premium</u>	<u>Pension plan</u>	
<u>2013</u>			
Plan modifications	-	13 years	-
Actuarial (loss) / gain	17 years	16 years	13 years
<u>2012</u>			
Plan modifications	-	14 years	-
Actuarial (loss) / gain	18 years	18 years	14 years

The effect of the increase or decrease of one percentage point in the increase rate of medical expenses used in the actuarial projections is shown below:

	<u>Increase in 1%</u>	<u>Decrease in 1%</u>
Labour cost plus financial cost	\$ 33	(29)
Defined benefit obligations	441	(395)
	=====	=====

For the years ended at December 31, 2013 and 2012, the Bank recognized expenses for defined contribution plans, which amount to \$187 and \$112, respectively.

(22) Share based payments-

At December 31, 2013 and 2012, the amount of outstanding share based payment awards amounted to \$241 and \$309, respectively, and were registered in the caption "Sundry creditors and other accounts payable". The cost of these programmes for the years ended December 31, 2013 and 2012 of \$132 and \$429 respectively, was included within "Administrative and promotional expenses" in the consolidated income statement. Payments made during the years 2013 and 2012 were \$200 and \$231, respectively.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(23) Subordinated debt issued -

At December 31, 2013 and 2012, the Bank had issued subordinated debentures, which are not convertible into shares of its capital stock. The debentures and accrued interest thereon are analyzed as follows:

	<u>2013</u>	<u>2012</u>
<u>Debentures issued:</u>		
In 2003, maturing in 2013 ⁽¹⁾	\$ -	2,200
In 2008, maturing in 2018 ⁽²⁾	4,090	4,090
In 2009, maturing in 2019 ⁽³⁾	3,924	3,890
In 2013, maturing in 2022 ⁽⁴⁾	1,439	-
Accrued interest	<u>10</u>	<u>16</u>
Total subordinated debentures	\$ 9,463	10,196
	=====	=====

- (1) The subordinated obligations issued in 2003 through a private offering, bear interest at a rate equivalent to the 28-day Inter-bank Interest Rate (TIIE). These debentures were paid off in December 2013.
- (2) During October and December 2008, the Bank made two public offerings of subordinated debt obligations, non convertible to HSBC shares for a total amount of \$1,818 and \$2,300, respectively. Of the second issuance, as of December 31, 2013, \$28, had not been placed. The subordinated obligations have a maturity of 10 years and bear interest at a rate equivalent to the 28-day TIIE plus 60 and 200 basis points, respectively.
- (3) As part of a programme of subordinated non convertible debt issuance (both preference and non preference securities), authorised by the Banking Commission, the Bank undertook a foreign currency issuance on 26 June 2009. This issuance was for a total of US\$300 million, of which US\$196.7 million was placed on the date of issue and the remaining US\$103.3 million was placed at a later date. The term of this issuance is 10 years and it pays a variable rate of interest at Libor plus 350 basis points.
- (4) On January 31, 2013, the Bank issued foreign currency preferred subordinated debentures subject to mandatory conversion into common shares representing capital stock, provided that any of the following conditions is met: (i) where the result from dividing the Tier 1 Basic Capital (note 25d) by the Bank's total weighted assets subject to risk is 4.5% or less; or (ii) where the Banking Commission notifies the Bank that it has not complied with the minimum remedial action in case of not having the minimum capitalization level required or when non complying with the minimum capitalization index required by the LIC and the Bank does not rectify such situation. Such issue totaled US\$110 million, was totally subscribed, has a 10 year maturity and bears interest at the 30-day LIBOR rate plus 365 basis points. Such issuance was recorded as a liability, considering the aforementioned conversion conditions, the Bank's capitalization index and financial condition at the date of issuance of the financial statements.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

At December 31, 2013 and 2012, the balance of subordinated obligations count as supplementary capital for the determination of the capitalization ratio, which is calculated based on the applicable rules as of those dates, issued by the Central Bank.

(24) Tax on earning (Income Tax (IT) and Flat Rate Business Tax (IETU)) and employee statutory profit sharing (ESPS) -

On December 11, 2013, a decree was published in the Official Gazette whereby several tax provisions were amended, supplemented, and repealed. This decree became effective as of January 1, 2014. Such decree repeals the IETU Law, the Cash Deposits (IDE) Law and the IT Law in effect through December 31, 2013 and a new IT Law is issued.

a) Tax on earning

Under the current tax legislation in effect in 2013, companies must pay the greater of their IT or IETU. If IETU is payable, the payment will be considered final not subject to recovery in subsequent years.

According to the IT Law in effect as of December 31, 2013, the IT rate for fiscal years 2013 and 2012 was 30%; for 2014, the rate would be 29%, and for 2015 and thereafter, 28%. The new IT law imposes an IT rate of 30% for 2014 and thereafter. The IETU rate for 2013 and 2012 was 17.5%.

At December 31, 2013 and 2012, the IT and IETU expense shown in the consolidated statement of income is analyzed as follows:

		<u>Tax on earning</u>	
		<u>2013</u>	<u>2012</u>
IT expense from the Bank at the rate 30%	\$	1,666	1,295
IT of subsidiaries		-	8
IETU of subsidiaries		<u>11</u>	<u>21</u>
Tax on earning in the consolidated statement of income	\$	<u>1,677</u>	<u>1,324</u>
		=====	=====

Deferred IT:

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Deferred IT changes for the years ended December 31, 2013 and 2012, are analyzed as follows:

		<u>2013</u>	<u>2012</u>
Balance at beginning of year	\$	6,138	6,409
Charged to results:			
IT (expenses) benefit		1,073	(89)
Reported in capital:			
Valuation effects of available for sale and derivatives		255	(205)
Effect in capital for the change in the consumer loan methodology		240	-
Others		<u>(82)</u>	<u>23</u>
	\$	<u>7,624</u>	<u>6,138</u>
		=====	=====

The items that give rise to significant portions of the deferred tax assets and liabilities at December 31, 2013 and 2012, are shown as follows:

		<u>2013</u>	<u>2012</u>
Deferred tax assets:			
Allowances:			
Allowance for loan losses	\$	6,705	5,342
Allowance for foreclosed assets		277	237
Other provisions		1,093	1,141
Property, furniture and equipment		641	595
ESPS provision		121	103
Valuation of financial instruments		258	244
Commissions received in advance		354	189
Other		<u>30</u>	<u>35</u>
		<u>9,479</u>	<u>7,886</u>
Deferred tax liabilities:			
Interest from Special CETES UDIS			
Central Bank		(990)	(872)
Valuation of financial instruments		(233)	(614)
Deductions in advance		(632)	(262)
		<u>(1,855)</u>	<u>(1,748)</u>
Net deferred tax asset	\$	<u>7,624</u>	<u>6,138</u>
		=====	=====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Reconciliation of the statutory income tax rate and the effective income tax rate is as follows:

	<u>2013</u>		<u>2012</u>	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
Income before income taxes	\$ 2,751	100%	5,410	100%
Expected tax expense	825	30%	1,623	30%
(Reduction) increase resulting from:				
Inflation effect	(380)	(14%)	(490)	(9%)
Non-deductible expenses	331	12%	908	17%
Tax income on derivatives	-	-	(52)	(1%)
Non-taxable interests	(295)	(11%)	(880)	(16%)
Subsidiaries' IETU	11	-	21	-
Tax SPE	221	8%	380	7%
Changed in rates	(307)	(11%)	(62)	1%
Others	<u>198</u>	<u>8%</u>	<u>(35)</u>	<u>-</u>
IT expense	\$ 604	22%	1,413	27%
	====	====	=====	====

Other considerations:

In accordance with Mexican tax law, the tax authorities are entitled to examine transactions carried out during the five years prior to the most recent income tax return filed.

In accordance with the Income Tax Law, companies carrying out transactions with related parties are subject to certain requirements as to the determination of prices, since such prices must be similar to those that would be used in arm's-length transactions.

At December 31, 2013, the balances of the Capital Contributions and after-taxes earnings accounts amount to \$38,149 and \$20,338, respectively (\$31,545 and \$17,613 respectively in 2012).

The Bank computes ESPS considering the one month's salary limit set forth in article 127, section III of the Federal Labor Law. During the year ended December 31, 2013, the ESPS payable amounts to \$398 (\$343 in 2012) and is recorded in the consolidated statement of income captioned "Administrative and promotion expenses".

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(25) Stockholders' equity-

The main features of the accounts comprising stockholders' equity are the following:

(a) Structure of capital stock -Movements in 2013

On April 26, 2013, the General Ordinary Stockholders' Meeting agreed to apply the net income for the year 2012 of \$3,997 as follows: \$400 to capital reserves and \$3,597 to retained earnings, which shall be made available to the stockholders when the Board of Directors shall so decide.

On March 21, 2013, the General Ordinary Stockholders' Meeting authorized the distribution of a dividend, which was paid on March 26, 2013 at the rate of \$0.7216 pesos per share for each of the 1,940,009,665 outstanding shares, for a total payment of \$1,400, which was charged to retained earnings and paid out of the previously taxed earnings account.

On January 24, 2013, the General Extraordinary Stockholders' Meeting agreed to increase the contributed capital in \$5,150 by issuing 209'689,909 shares with a par value of two pesos each, corresponding 195,178,687 to Series "F" and 14,511,222 to Series "B", which were paid at a price of \$24.5601 pesos per share; therefore, the difference with respect to the par value was recorded as additional paid-in capital. At this same Meeting it was approved to cancel 86,956,567 shares that had been deposited in the Bank's Treasury, which were neither subscribed nor paid up.

Consequently, at December 31, 2013, capital stock is represented by 1,940,009,665 subscribed and paid up shares, of which 1,805,754,708 shares are represented by Series "F" shares and 134,254,957 Series "B" shares, with a par value of two pesos each.

Movements in 2012

On April 27, 2012, the General Ordinary Shareholders' Meeting agreed to transfer the net income for year 2011 of \$716, affecting \$72 to the legal reserve and \$644 recorded in the other reserves account; such amount shall be made available for the stockholders until the Board of Directors agrees to do so.

At the Board of Directors meeting on October 20, 2011, the Board of Director authorized a maximum dividend of \$500 million, therefore on March 15, 2012 were declared dividends of \$1,400, equivalent to a price per share of \$0.8091 pesos for each one of the 1,730,319,756 shares outstanding without coupon, with charge to the net tax profit account. This dividend was paid on March 29, 2012.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The share capital at December 31, 2012 is integrated by 1,817,276,323 shares (1,730,319,756 subscribed and paid, of which 1,610,576,021 shares represented by shares of Series "F" and 119,743,735 shares of Series "B") with nominal value of two pesos each.

(b) Comprehensive income-

The comprehensive income reported in the consolidated statement of changes in stockholders' equity represents the results of the Bank's activities during the year and includes the net income, the gain or loss from mark to market of investments in "Available-for-sale" securities and for cash flow hedges, and additionally in 2013 for the constitution of allowance for loan losses derived of a change in the calculation methodology (note 4).

(c) Restrictions on stockholders' equity-

The Credit Institutions Law requires that the Bank segregate 10% of its net income for the year to the statutory reserves up to the amount of its paid-in capital stock.

Stockholder contributions may be reimbursed to the stockholders tax-free, to the extent that the tax basis of such contributions equal or exceed stockholders' equity. Retained earnings on which no income taxes have been paid, are subject to income taxes in the event of distribution to stockholders.

The un-appropriated retained earnings of subsidiaries may not be distributed to the Bank's stockholders until these are received by way of dividends. Also, gains from marking to market investment securities and derivative transactions may not be distributed until realized.

(d) Capitalization (unaudited)-

In accordance with the Law of Credit Institutions, credit institutions are required to maintain a net capital in relation to their exposure to market risk, credit risk and other risks which are incurred during the course of their operations. Net capital cannot be lower than the total of adding up the capital requirement for each type of risk. In accordance with the Capitalization Rules, credit institutions must comply with the capital requirement for operational risk.

Information in relation to the Bank's net capital, risk based assets and capital requirements as of December 31, 2013 and 2012, is shown below. The amounts for 2013 and 2012 correspond to those Published by the Central Bank at the date of issuance of the consolidated financial statements.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

	<u>2013</u>	<u>2012</u>
<u>Basic, supplementary and net capital</u>		
Stockholders' equity	\$ 47,555	42,781
Reduced by:		
Intangible assets	(5,575)	(4,117)
Investments in shares of financial entities	(17)	(32)
Investments in shares of other companies	-	(91)
Investment in subordinated debt	(92)	(91)
Investment in financial instruments related to securitizations	<u>-</u>	<u>(77)</u>
Basic capital (Tier 1)	<u>41,871</u>	<u>38,373</u>
Add:		
Not convertible subordinated debt	7,182	7,980
Subordinated debt eligible for conversion	1,439	-
General allowance for loan losses	1,287	1,753
Investment in financial instruments related to securitizations	<u>-</u>	<u>(78)</u>
Supplementary capital (Tier 2)	<u>9,908</u>	<u>9,655</u>
Net capital (Tier 1+ Tier 2)	\$ 51,779	48,028
	=====	=====

On November 28, 2012 was a published in the DOF "resolution amending the general Dispositions applicable to credit institutions" (Resolution). This resolution is intended to strengthen the composition of the net capital of credit institutions consistent with the most recent international consensus in this field in accordance with the guidelines established by the Capital Agreement issued by the Committee of Banking Supervision (Basel III). The resolution entries into force on January 1, 2013, except as provided in articles transient thereof, which stipulate the entry into force of certain provisions at a later date.

Intangibles assets.- Consider excess deferred taxes on the 10% capacity as the Basic Capital deduction required by \$3,048 and \$1,657 to December 31, 2013 and 2012, respectively.

Subordinated debentures not convertible into shares – For computing supplementary capital at December 31, 2013 in accordance with the Provisions, the amount to be considered shall be determined as 90% of the subordinated debentures not convertible into shares at December 31, 2012 as well as the January 31, 2013 issues that meets with the requirements for the 100% computation in accordance with the aforementioned Provisions. Since the maturity of the 2003 issue is less than one year, it shall no longer be considered for computing the supplementary capital.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Exhibit 1-O - Disclosure of capitalization related information

Below we provide details of each of the captions comprising exhibit 1-O considering information corresponding to the Bank but not the consolidation effects with its subsidiaries, based on the calculation and presentation bases issued by the Banking Commission for filling the respective template:

Table I.1 Composition of net capital

Reference	Tier 1 capital (CET1): instruments and reserves	Amount
1	Common stock that qualifies as tier 1 capital plus the corresponding premium	\$ 32,769
2	Retained earnings	1,376
3	Other comprehensive income items (and other reserves)	13,411
4	Capital subject to gradual elimination from tier 1 capital (applies only to companies not linked to stock)	Not applicable
5	Common stock issued by subsidiaries held by third parties (amount allowed in tier 1 capital)	Not applicable
6	Tier 1 capital before regulatory adjustments	47,555

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

	Tier 1 capital: regulatory adjustments	
7	Prudential valuation adjustments	Not applicable
8	Goodwill, net of deferred tax asset	
9	Other intangibles other than mortgage servicing rights (net of the corresponding deferred income tax liabilities)	980
10 (conservative)	Deferred income tax assets that are dependent on future income, excluding those arising from temporary differences (net of deferred income tax liabilities)	
11	Mark to market from cash flow hedges	
12	Pending reserves	
13	Benefits on remnant in securitization transactions	
14	Losses and gains due to changes in own credit rating on liabilities carried at fair value	Not applicable
15	Defined benefit pension plan	

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

16 (conservative)	Permanent investment in shares	
17 (conservative)	Reciprocal investments in common equity	
18 (conservador)	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, and where the Bank does not own more than 10% of the issued share capital of the entity (amount in excess of the 10% threshold)	8
19 (conservative)	Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, and where the Bank owns more than 10% of the issued share capital of the entity (amount in excess of the 10% threshold)	
20 (conservative)	Mortgage servicing rights (amount in excess of the 10% threshold)	
21	Deferred income tax assets arising from temporary differences amount in excess of the 10% threshold, net of deferred tax liabilities)	3,048
22	Amount in excess of the 15% threshold	Not applicable
23	of which: Significant investments where the Institution owns more than 10% of the common stock of financial institutions	Not applicable
24	of which: Mortgage servicing rights	Not applicable
25	of which: Deferred income tax assets arising from temporary differences	Not applicable

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

26	Local regulatory adjustments	1,648
A	of which: Other comprehensive income (other reserves)	
B	of which: Investment in subordinated debt	92
C	of which: Gain or increase in the value of assets due to acquisition of securitization positions (Originating Institutions)	
D	of which: Investments in multilateral organizations	
E	of which: Investment in related parties	
F	of which: Investments in venture capital	
G	of which: Investment in investment funds	9
H	of which: Financing for the acquisition of own shares	
I	of which: Transactions that contravene the provisions	
J	of which: Deferred charges and prepayments	1,548
K	of which: Positions in First Loss Schemes	

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

L	of which: Deferred employee statutory profit sharing	
M	of which: Relevant related persons	
N	of which: Defined benefits pension plan	
O	of which: Adjustments for recognition of capital	
27	Regulatory adjustments that apply to tier 1 capital due to the inadequacy of additional tier 1 capital and tier 2 capital to cover deductions	
28	Total regulatory adjustments to tier 1 capital	5,685
29	Tier 1 capital (CET1)	41,871
	Additional tier 1 capital: instruments	
30	Directly issued instruments that qualify as additional tier 1 capital, plus their premium	
31	of which: Classified as capital under the applicable accounting criteria	
32	of which: Classified as liabilities under the applicable accounting criteria	Not applicable
33	Capital instruments issued directly and subject to gradual elimination of additional tier 1 capital	

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

34	Additional tier 1 capital instruments issued and Tier 1 capital instruments not included in line item 5 that were issued by subsidiaries, held by third parties (amount allowed in additional tier 1)	Not applicable
35	of which: Instruments issued by subsidiaries subject to gradual elimination	Not applicable
36	Additional tier 1 capital before regulatory adjustments	
	Additional tier 1 capital: regulatory adjustments	
37 (conservative)	Investments in own additional tier 1 capital	Not applicable
38 (conservative)	Reciprocal investments in additional tier 1 capital instruments	Not applicable
39 (conservative)	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, and where the Bank does not own more than 10% of the issued share capital of the entity (amount in excess of the 10% threshold)	Not applicable
40 (conservative)	Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, and where the Bank owns more than 10% of the issued share capital of the entity	Not applicable
41	Local regulatory adjustments	

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

42	Regulatory adjustments that apply to tier 1 capital due to the inadequacy of additional tier 1 capital and tier 2 capital to cover deductions	Not applicable
43	Total regulatory adjustments to tier 1 capital	-
44	Additional tier 1 Capital (AT1)	-
45	Tier 1 capital (T1 = CET1 + AT1)	41,871
	Tier 2 capital: instruments and reserves	
46	Instruments issued directly that qualify as tier 2 capital, plus their premium	1,439
47	Capital instruments issued directly and subject to gradual elimination from tier 2 capital	7,182
48	Tier 2 capital instruments, tier 1 capital instruments and additional tier 1 capital that have not been included in line items 5 or 34, which were issued by subsidiaries, held by third parties (amount allowed in supplementary tier 2 capital)	Not applicable
49	of which: Instruments issued by subsidiaries and subject to gradual elimination	Not applicable
50	Reserves	1,287

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

51	Tier 2 capital: before regulatory adjustments	9,908
	Tier 2 capital regulatory adjustments	
52 (conservative)	Investments in own additional tier 2 capital	Not applicable
53 (conservative)	Reciprocal investments in additional tier 2 capital instruments	Not applicable
54 (conservative)	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, and where the Bank does not own more than 10% of the issued share capital of the entity (amount in excess of the 10% threshold)	Not applicable
55 (conservative)	Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, and where the Bank owns more than 10% of the issued share capital of the entity.	Not applicable
56	Local regulatory adjustments	
57	Total regulatory adjustments to tier 2 capital	-
58	Tier 2 capital (T2)	9,908
59	Total capital (TC = T1 + T2)	51,779
60	Total risk-weighted assets	349,581

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

	Capital ratios and supplements	
61	Common equity tier 1 (as a percentage of total risk-weighted assets)	11.98%
62	Tier 1 capital (as a percentage of total risk-weighted assets)	11.98%
63	Total capital (as a percentage of total risk-weighted assets)	14.81%
64	Specific institutional supplement (should at least consist of the Common equity tier 1 requirement plus the capital conservation buffer, the counter-cyclical buffer and the G-SIB buffer; expressed as a percentage of total risk-weighted assets)	7%
65	of which: Capital conservation supplement	2.5%
66	of which: Specific banking counter-cyclical buffer	Not applicable
67	of which: Supplement of global systemically important banks (G-SIB)	Not applicable
68	Common equity tier 1 available for covering supplements (as a percentage of total risk-weighted assets)	4.98%

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

	Local minimums (if different from Basel III)	
69	Minimum national CET1 ratio (if different from minimum required by Basel 3)	Not applicable
70	Minimum national T1 ratio (if different from minimum required by Basel 3)	Not applicable
71	Minimum national TC ratio (if different from minimum required by Basel 3)	Not applicable
	Amounts under thresholds for deduction (before risk weighting)	
72	Non-significant investments in the capital of other financial institutions	Not applicable
73	Significant investments in the common capital of financial institutions	Not applicable
74	Mortgage servicing rights (net of deferred income tax liabilities)	Not applicable
75	Deferred income tax assets arising from temporary differences (net of deferred income tax liabilities)	4,492
	Limits applicable to the inclusion of reserves in tier 2 capital	
76	Reserves that are eligible for inclusion in tier 2 capital with respect to exposures subject to the standardized methodology (prior to applying the limit)	-
77	Limit for the inclusion of provisions in tier 2 capital under the standardized methodology	1,287

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

78	Reserves that are eligible for inclusion in tier 2 capital with respect to exposures subject to the internal ratings methodology (prior to applying the limit)	
79	Limit for the inclusion of provisions in tier 2 capital under the internal ratings methodology	
Capital instruments subject to gradual elimination (applies only between January 1, 2018 and January 1, 2022)		
80	Current limit of CET1 instruments subject to gradual elimination	Not applicable
81	Amount excluded from the CET1 due to the limit (excess over the limit after amortizations and maturities)	Not applicable
82	Current limit of AT1 instruments subject to gradual elimination	
83	Amount excluded from the AT1 due to the limit (excess over the limit after amortizations and maturities)	
84	Current limit of T2 instruments subject to gradual elimination	7,980
85	Amount excluded from the T2 due to the limit (excess over the limit after amortizations and maturities)	798

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Table II.1 Capital recognition adjustment

Description	Without capital recognition adjustment	% APSRT	Capital recognition adjustment	With capital recognition adjustment	% APSRT
Basic Capital 1	41,871	11.98	-	41,871	11.98
Basic Capital 2	-	-	-	-	-
Basic Capital	41,871	11.98	-	41,871	11.98
Supplementary Capital	9,908	2.83	-	9,908	2.83
Net Capital	51,779	14.81	-	51,779	14.81
Total risk-weighted assets (APSRT)	349,581	Not applicable	Not applicable	349,581	Not applicable
Capitalization index	14.81	Not applicable	Not applicable	14.81	Not applicable

Table III.1 Net capital ratio in balance sheet

Reference to the balance sheet caption	Balance sheet captions	Amount
	Assets	510,799

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

BG1	Cash and cash equivalents	55,406
BG2	Margin accounts	-
BG3	Investment securities	151,347
BG4	Debtors under agreements to resell	500
BG5	Securities lending	-
BG6	Derivatives	49,770
BG7	Valuation adjustments from hedging of financial assets	-
BG8	Loan portfolio, net	192,485
BG9	Benefits receivable on securitization transactions	182
BG10	Other accounts receivable, net	40,236

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

BG11	Foreclosed assets, net	151
BG12	Property, furniture and equipment, net	5,027
BG13	Permanent investments in shares	4,530
BG14	Long-term assets available for sale	5
BG15	Deferred taxes, net	7,540
BG16	Others assets	3,620
	Liabilities	463,243
BG17	Deposit funding	287,808
BG18	Due to banks and other institutions	20,510
BG19	Creditors under agreements to repurchase	34,765

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

BG20	Securities lending	-
BG21	Collateral sold or pledged as guarantee	9,076
BG22	Derivatives	47,643
BG23	Valuation adjustments from hedging of financial liabilities	-
BG24	Obligations in securitization transactions	-
BG25	Other accounts payable	53,382
BG26	Subordinated debt issued	9,463
BG27	Deferred taxes, net	-
BG28	Deferred credits	596

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

	Stockholders' equity	47,556
BG29	Paid-in capital	32,769
BG30	Earned capital	14,787
	Memorandum accounts	4,246,440
BG31	Guarantees issued	-
BG32	Contingent assets and liabilities	-
BG33	Irrevocable lines of credit	25,561
BG34	Assets in trust or under mandate	439,469
BG35	Financial agent of federal government	-
BG36	Assets in custody or under management	378,679

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

BG37	Collaterals received by the entity	17,291
BG38	Collaterals received by the entity and sold or pledged in guarantee	16,583
BG39	Investment banking transactions on behalf of customers, net	50,354
BG40	Uncollected interest accrued in respect of overdue credit portfolio	221
BG41	Other memorandum accounts	3,318,282

Table III.2 Regulatory concepts considered in calculating the components of Net Capital

ID	Regulatory concepts considered in calculating the components of Net Capital	Disclosure form reference of the composition of capital of section I hereof	Amount in accordance with notes to the table "Regulatory concepts considered in calculating the components of Net Capital"	Reference(s) of the balance sheet caption and amount related to the regulatory concepts considered in calculating Net Capital taken from the aforesaid reference
	Assets			
1	Goodwill	8	0.0	

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

2	Other intangibles	9	980	BG16 3620
3	Deferred income tax (assets) arising from losses and tax credits	10	-	
4	Benefits on remnant in securitization transactions	13	-	
5	Investments of the defined benefits pension plan without unrestricted and unlimited access	15	-	
6	Investments in the institution's own shares	16	-	
7	Reciprocal investments in ordinary capital	17	-	
8	Direct investments in the capital of financial entities where the institutions owns no more than 10% of the issued share capital	18	-	
9	Indirect investments in the capital of financial entities where the Institutions owns no more than 10% of the issued share capital	18	8	BG13 4530
10	Direct investments in the capital of financial entities where the institutions owns more than 10% of the issued share capital	19	-	
11	Indirect investments in the capital of financial entities where the Institutions owns more than 10% of the issued share capital	19	-	
12	Deferred income taxes (assets) arising from temporary differences	21	3,048	BG15 7540
13	Reserves recognized as supplementary capital	50	1,287	BG8 192485

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

14	Investments in subordinated debt	26 - B	92	BG8 192485
15	Investments in multilateral organizations	26 - D	-	
16	Investments in related parties	26 - E	-	
17	Investments in venture capital	26 - F	-	
18	Investments in investment funds	26 - G	9	BG13 4530
19	Financing for the acquisition of own shares	26 - H	-	
20	Deferred charges and prepayments	26 - J	1,548	BG16 3620
21	Employee statutory profit sharing, net	26 - L	-	
22	Investments in defined benefits pension plan	26 - N	-	
23	Investments in clearing houses	26 - P	-	
	Liabilities			
24	Deferred tax assets related to goodwill	8	-	
25	Deferred tax asset related to other intangibles	9	-	
26	Defined benefits pension plan liabilities without unrestricted and unlimited access	15	-	
27	Deferred tax asset related to defined benefits pension plan	15	-	

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

28	Deferred tax asset related to others	21	3,048	BG15 7540
29	Subordinated debentures, amount that complies with Exhibit 1-R	31	-	
30	Subordinated debentures subject to transience that are computed as basic capital 2	33	-	
31	Subordinated debentures, amount that complies with Exhibit 1-S	46	1,439	BG26 9463
32	Subordinated debentures subject to transience that are computed as supplementary capital	47	7,182	BG26 9463
33	Deferred tax assets related to deferred charges and prepayments	26 - J	-	
	Stockholders' equity			
34	Contributed capital that complies with Exhibit 1-Q	1	32,769	BG29 32769
35	Retained earnings	2	1,376	BG30 14787
36	Mark-to-market from cash flow hedges	3	13,411	BG30 14787
37	Other elements of earned capital that are different from the foregoing	3	-	
38	Contributed capital that complies with Exhibit 1-R	31	-	
39	Contributed capital that complies with Exhibit 1-S	46	-	

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

40	Gain (loss) from valuation of cash flow hedge instruments for items not recorded at fair value	3, 11	-	
41	Cumulative translation effect	3, 26 - A	-	
42	Equity adjustment for non-monetary assets	3, 26 - A	-	
	Memorandum Accounts			
43	Positions in First Loss Schemes	26 - K	-	
	Regulatory concepts not considered in the balance sheet			
44	Reserves pending to be created	12	-	
45	Gain or increase in the value of assets due to acquisition of securitization positions (Originating Institutions)	26 - C	-	
46	Transactions that contravene the provisions	26 - I	-	
47	Transactions with relevant related persons	26 - M	-	
48	Capital recognition adjustment	26 - O, 41, 56	-	

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Risk-based assets and capital requirements

	Equivalent risk weighted assets		Capital requirement	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
<i>Market risk:</i>				
Transactions or positions:				
In pesos at nominal rates	\$ 66,526	64,512	5,322	5,161
In pesos at interest rate over nominal rate	910	1,291	73	103
In pesos at interest rates discounted from inflation or denominated in UDIS	1,222	1,760	98	141
In foreign currency at nominal rates	6,503	8,502	520	680
In UDIS or with yields linked to the Consumer Price Index	9	14	1	1
Foreign currency positions or with Exchange rate indexed yields	679	789	54	63
Share transactions or transaction based on shares	<u>33</u>	<u>-</u>	<u>3</u>	<u>-</u>
Total market risk	<u>75,882</u>	<u>76,868</u>	<u>6,071</u>	<u>6,149</u>
<i>Credit risk:</i>				
Group II (weighted at 20%)	6	6	-	-
Group II (weighted at 50%)	7,713	3,340	617	267
Group III (weighted at 10%)	36	529	3	42
Group III (weighted at 11.5%)	401	509	32	41
Group III (weighted at 20%)	3,960	5,833	317	467
Group III (weighted at 23%)	129	-	10	-
Group III (weighted at 100%)	464	-	37	-
Group IV (weighted at 20%)	3,239	2,437	259	195
Group V (weighted at 20%)	499	809	40	65
Group V (weighted at 50%)	1,680	804	134	64
Group V (weighted at 115%)	-	404	-	32
Group V (weighted at 150%)	5,694	7,058	456	565
Group VI (weighted at 50%)	5,203	4,032	416	323
Group VI (weighted at 75%)	<u>3,446</u>	<u>2,174</u>	<u>276</u>	<u>174</u>
Credit risk to the following page	<u>32,470</u>	<u>27,935</u>	<u>2,597</u>	<u>2,235</u>

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

	Equivalent risk weighted assets		Capital requirement	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
Credit risk from previous page	<u>32,470</u>	<u>27,935</u>	<u>2,597</u>	<u>2,235</u>
Group VI (weighted at 100%)	43,798	39,381	3,503	3,150
Group VII (weighted at 10%)	432	-	35	-
Group VII (weighted at 20%)	5,180	4,047	414	324
Group VII (weighted at 23%)	6,481	4,834	519	387
Group VII (weighted at 50%)	673	268	54	21
Group VII (weighted at 100%)	106,939	107,286	8,556	8,583
Group VII (weighted at 115%)	267	4,870	21	390
Group VII (weighted at 150%)	646	565	52	45
Group VIII (weighted at 125%)	8,488	1,846	679	147
Group X (weighted at 1250%)	998	-	80	-
Others assets (weighted at 100%)	23,429	23,724	1,874	1,898
Securitizations (weighted at 20%)	151	-	12	-
Securitizations (weighted at 50%)	10	-	1	-
Securitizations (weighted at 1250%)	370	-	30	-
Resecuritizations (weighted at 1250%)	<u>2,270</u>	<u>-</u>	<u>182</u>	<u>-</u>
Total credit risk	232,602	214,756	18,609	17,180
Total Operational risk	<u>41,097</u>	<u>39,478</u>	<u>3,287</u>	<u>3,159</u>
Total market credit and operational risk	<u>349,581</u>	<u>331,102</u>	<u>27,967</u>	<u>26,488</u>

Capitalization ratios:

	<u>2013</u>	<u>2012</u>
Capital to credit risk assets:		
Basic capital (Tier 1)	18.00%	17.87%
Supplementary capital (Tier 2)	4.26%	4.49%
Net capital (Tier 1 + Tier 2)	22.26%	22.36%
	=====	=====
Capital to market, credit and Operational risks assets:		
Basic capital (Tier 1)	11.98%	11.59%
Supplementary capital (Tier 2)	2.83%	2.92%
Net capital (Tier 1 + Tier 2)	14.81%	14.51%
	=====	=====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Table V.1 Principal characteristics of securities making up the Net Capital

Ref.	Characteristic	EQUITY	LIABILITY	LIABILITY	LIABILITY	LIABILITY
1	Issuer	HSBC México, S.A., Institución de Banca Múltiple, Grupo Financiero HSBC	HSBC México, S.A., Institución de Banca Múltiple, Grupo Financiero HSBC	HSBC México, S.A., Institución de Banca Múltiple, Grupo Financiero HSBC	HSBC México, S.A., Institución de Banca Múltiple, Grupo Financiero HSBC	HSBC México, S.A., Institución de Banca Múltiple, Grupo Financiero HSBC
2	ISIN, CUSIP or Bloomberg identifier	INTENAL	HSBC 08	HSBC 08-2	HSBC 13-1D	HSBC 09-D
3	Legal Framework	L.I.C.; C.U.B., L.G.S.M.;	L.I.C.; LGTOC., L.M.V, CUB	L.I.C.; LGTOC; L.M.V: CUB	L.I.C.; LGTOC; L.M.V: CUB	L.I.C.; LGTOC; L.M.V: CUB
	Regulatory treatment					
4	Level of capital considering transitional arrangements	N.A.	Supplementary	Supplementary	Supplementary	Supplementary
5	Level of capital without considering transitional arrangements	Basic 1	Not Applicable	Not Applicable	Supplementary	Not Applicable
6	Level of instrument	Credit institution that does not consolidate subsidiaries	Credit institution that does not consolidate subsidiaries	Credit institution that does not consolidate subsidiaries	Credit institution that does not consolidate subsidiaries	Credit institution that does not consolidate subsidiaries
7	Type of instrument	Series "F" and "B" shares	Subordinated debenture	Subordinated debenture	Subordinated debenture	Subordinated debenture

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Ref.	Characteristic	EQUITY	LIABILITY	LIABILITY	LIABILITY	LIABILITY
8	Amount recognized in regulatory capital	Series "F" shares 1,805,754,708; Series "B" shares 134,254,957, which represents \$3,880 of nominal capital at \$2.00, plus share Premium and restatement for 28,888,503,834	1,636	2,045	1,439	3,501
9	Par value of instrument	32,768	1,817	2,272	1,439	3,925
9A	Currency of instrument	Mexican pesos	Mexican pesos	Mexican pesos	USD	USD
10	Accounting classification	Equity	Liability	Liability	Liability	Liability
11	Date of issue	31/12/2007; 31/08/2009; 31/10/2009; 31/12/2009; 31/12/2011; 29/01/2013	02/10/2008	22/12/2008	31/01/2013	30/06/2009
12	Term of instrument	Perpetuity	Maturity	Maturity	Maturity	Maturity
13	Maturity date	None	09/20/2018	12/10/2018	12/10/2022	06/28/2019
14	Prepayment clause	No	Yes	Yes	Yes	Yes
15	First prepayment date	N.A.	09/26/2013	12/16/2013	01/05/2018	06/28/2014
15A	Regulatory or fiscal events	No	No	No	Yes	No

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Ref.	Characteristic	EQUITY	LIABILITY	LIABILITY	LIABILITY	LIABILITY
15B	Settlement price in prepayment clause	Not applicable	Equal to Par Value plus interest accrued up to the early repayment date, provided that (i) the Issuer, through the Common Representative, notifies in writing his/her decision to exercise its right to early repay to the Debenture-holders, the Banking Commission, the Indeval and the BMV, through the means as shall the latter determine, with at least 10 (ten) Business Days in advance of the date on which the Issuer intends to early redeem the totality of the Subordinated Debentures; and (ii) the early repayment takes place in the payment form and place referred to in Clause Eleven of the Debenture Indenture.	Equal to Par Value plus interest accrued up to the early repayment date, provided that (i) the Issuer, through the Common Representative, notifies in writing his/her decision to exercise its right to early repay to the Debenture-holders, the Banking Commission, the Indeval and the BMV, through the means as shall the latter determine, with at least 10 (ten) Business Days in advance of the date on which the Issuer intends to early redeem the totality of the Subordinated Debentures; and (ii) the early repayment takes place in the payment form and place referred to in Clause Eleven of the Debenture Indenture.	Equal to Par Value plus interest accrued up to the early repayment date, subject to authorization by the Central Bank in terms of paragraph five, article 64 of the LIC, in any Interest Payment Date: (i) since the fifth year after the Date of Issue; or (ii) in cases where Subordinated Debentures are no longer computed as supplementary capital of the Issuer as a result of amendments to or reforms of laws, regulations and other applicable provisions, provided the Issuer, notifies in writing his/her decision to exercise its right to early repay to the Debenture-holders, with at least 10 (ten) Business Days in advance of the date on which the Issuer intends to early redeem the totality of the Subordinated Debentures; and (ii) the early repayment takes place in the payment form and place referred to in section 11 hereof.	Equal to Par Value plus interest accrued up to the early repayment date, provided that (i) the Issuer, through the Common Representative, notifies in writing his/her decision to exercise its right to early repay to the Debenture-holders, the Banking Commission, the Indeval and the BMV, through the means as shall the latter determine, with at least 10 (ten) Business Days in advance of the date on which the Issuer intends to early redeem the totality of the Subordinated Debentures; and (ii) the early repayment takes place in the payment form and place referred to in Clause Eleven of the Debenture Indenture.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Ref.	Characteristic	EQUITY	LIABILITY	LIABILITY	LIABILITY	LIABILITY
16	Subsequent prepayment dates	Not applicable	01/16/2014; Payment should be made on any of the dates noted for the payment of interest, to be informed 10 business days in advance of the authorized payment date.	01/13/2014; Payment should be made on any of the dates noted for the payment of interest, to be informed 10 business days in advance of the authorized payment date.	02/04/2018 payment date to be informed 10 business days in advance of the authorized payment date.	07/28/2014 payment date to be informed 10 business days in advance of the authorized payment date.
	<i>Yield / dividends</i>					
17	Type of yield/dividend	Variable	Variable	Variable	Variable	Variable
18	Interest/dividend rate	The last rate known was from March 2013: 0.7216 per share	TIEE 28 + 0.60 pp	TIEE 28 + 2.0 pp	1-month Libor + 3.65 pp	1-month Libor + 3.50 pp
19	Dividend cancellation clause	No	No	No	No	No
20	Discretion in payment	Mandatory	Mandatory	Mandatory	Partially discretionary	Mandatory
21	Interest increase clause	No	No	No	No	No
22	Yield/dividends	Non-accruable	Non-accruable	Non-accruable	Non-accruable	Non-accruable
23	Instrument convertibility	Not convertible	Not convertible	Not convertible	Convertibles	Not convertible

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Ref.	Characteristic	EQUITY	LIABILITY	LIABILITY	LIABILITY	LIABILITY
24	Convertibility conditions	Not applicable	Not applicable	Not applicable	Subordinated Debentures shall be of compulsory conversion into common stock representing the Issuer's capital stock, without this event being considered an event of default, and which shall take place when any of the following conditions is met: 1. When the result of dividing Common Equity Tier 1 by the Issuer's total risk-weighted assets is 4.5% or less. For purposes of the provisions of this section, the Issuer should proceed with the conversion on the Business Day following the publication of the capitalization index referred to by Article 221 of the Capitalization Provisions. 2. When the Banking Commission notifies the Issuer, in accordance with the provisions of Article 29 Bis of the LIC, that it has incurred in any of the grounds referred to by sections IV or V of Article 28 of the LIC and in the period of time provided for by said Article 29 Bis, the Issuer does not rectify the events or in dealing with the grounds for revocation referred to in section V the Issuer does not request to opt for the conditioned operations regime or does not refund the capital. For purposes of that provided for in this section, the Issuer should proceed with the conversion on the Business Day following that on which the deadline referred to in the aforementioned Article 29 Bis of the LIC has expired. In any event, the conversion into shares referred to in this section shall be final; therefore, no clauses may be included that foresee the restitution or grant any compensation to the debenture holders.	Not applicable

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Ref.	Characteristic	EQUITY	LIABILITY	LIABILITY	LIABILITY	LIABILITY
25	Degree of convertibility	Not applicable	Not applicable	Not applicable	The conversion shall be made at least for the lesser of: (i) the totality of the Securities; and (ii) the necessary amount in order that the result from dividing the Issuer's Common equity tier 1 the Issuer's total risk-weighted assets is 7.0% (seven percent). The conversion into common stock shall once again proceed in the same terms every time the aforementioned assumptions change. The conversion should be made observing at all times the shareholding limits by person or group of persons provided for by the applicable laws. For purposes of the foregoing, from the time of the Issue, the Issuer shall ensure and verify that such limits are complied, that the notices are filed and/or that the corresponding authorizations are obtained.	Not applicable

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Ref.	Characteristic	EQUITY	LIABILITY	LIABILITY	LIABILITY	LIABILITY
26	Conversion rate	Not applicable	Not applicable	Not applicable	The conversion as well as the remission or cancellation foreseen herein shall be prorated with regard to all the securities of the same nature that are computed in the Issuer's supplementary capital. The conversion of the Subordinated Debentures shall be made by surrendering 59.80678909 (fifty nine point eight zero six seven eight nine zero nine) common shares representing the Issuer's capital stock for each Subordinated Debenture.	Not applicable
27	Type of instrument convertibility	Not applicable	Not applicable	Not applicable	Mandatory	Not applicable
28	Type of financial instrument of convertibility	Not applicable	Not applicable	Not applicable	Common shares	Not applicable

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Ref.	Characteristic	EQUITY	LIABILITY	LIABILITY	LIABILITY	LIABILITY
29	Instrument issuer	Not applicable	Not applicable	Not applicable	HSBC México, S.A., Institución de Banca Múltiple, Grupo Financiero HSBC	Not applicable
30	Write-down clause	No	No	No	No	No
31	Write-down conditions	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable
32	Write-down degree	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable
33	Write-down temporality	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable
34	Temporary write-down mechanism	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable
35	Subordination level in the event of liquidation	Not applicable	Non-preferred	Non-preferred	Non-preferred	Non-preferred
36	Default characteristics	No	Yes	Yes	No	Yes
37	Description of default characteristics	Not applicable	Not applicable	Not applicable	No	Not applicable

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Table VI Capital Management

As for capital management, the Bank conducts half-yearly internal assessments of the adequacy of its capital, where it identifies and measures exposure to the various types of risks facing the entity. The resulting document is called Internal Capital Adequacy Assessment Process (ICAAP). Such document has as purpose to ensure that under a prospective analysis, the Bank's capital is adequate and supported by a strong risk management framework. This report is generated for complying with the requirements of HGHQ (London based group) in compliance with Pillar II of the Basel Accord.

Moreover, the Bank has an internal framework of minimum levels of total and basic capital index beyond the early warnings defined by the Banking Commission. Such levels are approved annually at the Asset and Liability Management Committee (ALCO).

On the other hand, the expected impacts on the capital index are computed on a quarterly basis, considering the sensitivity to the exchange rate, interest rate and credit spread variables, where the following is assessed:

1 - Exchange rate sensitivity: sensitivity is assessed by monitoring the impact on the basic capital index and the capitalization index, where a 10% shock is applied to a 20% increase/decrease in the exchange rate of each of the significant currencies.

2 - Interest rate sensitivity: the impact is measured of a change in the interest rate on the basic capital index and in the capitalization index. This year, the impact is calculated on instruments classified as available-for-sale and cash flow hedges that directly affect capital reserves. The shock considered for this calculation is an increase/decrease in the market interest rate of 200 basis points.

3 - Credit spread sensitivity: sensitivity is assessed in the basic capital index and in the capitalization index to a change of 300 basis points in the country risk, calculated also on instruments classified as available-for-sale. The shock considered is an increase/decrease of 300 basis points.

The findings are set out in the ALCO.

Last, the Bank generates monthly liquidity stress reports that allow for conducting an analysis of the adequacy of financial Resources under certain stress scenarios. For further details, we refer to note 30 to the financial statements.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

As discussed in note 4, since June 2013 the Bank opted for calculating preventive reserves by considering the expected loss methodology issued by the authority pursuant to the Provisions, which had an effect on the Credit Risk and the Supplementary Capital. For Supplementary Capital computed at December 31, 2013, the difference is considered between the total Reserves created for Investment Projects, Financial Entities and Other additional reserves and the reserves for expected losses and additional reserves not considered Supplementary Capital. Only the General Reserves were considered through December 31, 2012.

The Bank reports on a monthly basis the trend of the capitalization indices, detailing basic capital and net capital to the Risk Committee and the Assets and Liabilities Committee. In addition, significant variances in the risk-weighted assets by credit and market risk, and variances in stockholders' equity, are explained and reported.

In addition, prior to undertaking any material commercial banking or treasury transactions, an assessment is made to determine their effect on the capital requirement. Based on this, the above mentioned Committees may authorize the proposed transactions. For these operations the Bank considers as a basis the minimum capitalization index, which is higher than the required by the Banking Commission in the Early Warnings.

(26) Related party transactions and balances-

During the normal course of business, the Bank carries out transactions with related parties. According to the Bank's policies, the Board of Directors authorizes all credit transactions with related parties, which are granted at market rates with guarantees and terms in accordance with sound banking practices. At December 31, 2013, the Bank had granted loans to related parties totalling \$318 and (\$4,489 in 2012).

During the years in 2013 and 2012, the Bank maintained derivative liability positions with related parties, which amounted to \$2,875 and \$3,016, respectively.

The main transactions carried out with related parties during the years ended December 31, 2013 and 2012, are shown as follows:

	<u>2013</u>	<u>2012</u>
<u>Transactions:</u>		
Income:		
Administrative services	\$ 1,793	2,105
Interest and commissions, received	519	440
	=====	=====
Expenses:		
Insurance premiums	\$ 208	205
Premiums on securities repurchase/resell agreements	-	176
Interest and commissions, paid	52	43
Administrative expenses	1,203	1,145
	=====	=====

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Balances receivable from and payable to related parties as of December 31, 2013 and 2012, were as shown as follows:

	<u>2013</u>		<u>2012</u>	
	<u>Receivable</u>	<u>Payable</u>	<u>Receivable</u>	<u>Payable</u>
<u>Holding</u>				
Grupo Financiero HSBC, S. A. de C. V.	\$ <u>7</u>	<u>15</u>	<u>-</u>	<u>15</u>
<u>Other related parties</u>				
HSBC Seguros, S. A. de C. V.	89	1	91	1
HSBC Vida, S. A. de C. V.	25	2	18	-
HSBC Casa de Bolsa, S. A. de C. V.	140	337	22	573
HSBC Fianzas, S. A.(*)	-	-	1	25
HSBC Pensiones, S. A.	4	2	3	3
HSBC Global Asset Management, S. A. de C. V.	46	-	67	-
HSBC Servicios, S. A. de C. V.	83	12	1	15
HSBC Bank Brasil, S. A. Banco Multiplo	239	162	116	125
HSBC Holdings Plc.	54	123	28	250
HSBC Banco Salvadoreño, S. A.(*)	-	-	17	-
HSBC Bank Panamá, S. A.(*)	-	-	86	-
HSBC Colombia, S. A.	15	-	39	1
Banco HSBC Honduras, S. A.(*)	-	-	3	-
HSBC Bank USA National Association	-	8	-	1
HSBC Software Development (Guandong)	-	3	-	-
HSBC Bank Argentina S. A.	44	20	15	14
HSBC Argentina Holding, S. A.	6	2	1	-
HSBC New York Life Seguros de Vida (Argentina), S. A.	8	-	5	-
HSBC Private Bank (SUISSE) S. A.	1	10	2	1
HSBC La Buenos Aires Seguros, S. A	-	-	3	-
HSBC Bank plc.	11	67	11	78
The Hong Kong and Shanghai Banking Corporation Limited.	-	30	-	75
HSBC Latin America Holdings (UK) Limited	266	-	56	-
HSBC Software Development (India) Private Ltd.	-	26	2	36
HSBC Software Development (Brazil)	-	1	-	31
HSBC Technologies and Services (USA) Inc.	-	13	-	31
HSBC Technologies, Inc.	-	-	-	18
HSBC Bank Perú, S. A.(*)	<u>-</u>	<u>-</u>	<u>68</u>	<u>-</u>
Subtotal other related parties to the following page	\$ <u>1,031</u>	<u>819</u>	<u>655</u>	<u>1,278</u>

(*) As of December 31, 2013, these entities are not larger considered as related parties.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

	<u>2013</u>		<u>2012</u>	
	<u>Receivable</u>	<u>Payable</u>	<u>Receivable</u>	<u>Payable</u>
<u>Other related parties</u>				
Subtotal other related parties to the following page	\$ <u>1,031</u>	<u>819</u>	<u>655</u>	<u>1,278</u>
HSBC Bank (Paraguay), S. A.(*)	-	-	48	-
HSBC Bank (Uruguay), S. A.	3	-	20	-
HSBC Bank Canada	-	3	-	18
HSBC Bank (Chile), S. A.	5	-	5	-
HSBC France	-	3	-	8
HSBC Insurance Holdings Limited	-	-	-	5
HSBC Securities (USA) Inc	-	3	-	2
HSBC Finance Transformation (UK) Limited	-	-	-	47
HSBC Global Asset Management (USA) Inc	-	-	-	4
HSBC Bank Middle East Limited	-	1	-	-
HSBC Global Operations Company Limited (antes HSBC Global Resourcing (UK) Limited)	-	42	-	2
HSBC PB Service (SUSSIE) S.A.	<u>-</u>	<u>5</u>	<u>-</u>	<u>-</u>
Total other related parties	<u>1,039</u>	<u>876</u>	<u>728</u>	<u>1,364</u>
Total holding and other related parties	\$ <u>1,046</u>	891	728	1,379
	=====	====	====	=====

(*) See note in previous page

Accounts receivable and payable from with to related parties do not generate interest and do not have defined maturity.

(27) Memorandum accounts-**(a) Irrevocable lines of credit and guarantees-**

At December 31, 2013, the Bank had irrevocable commitments arising from issuance of letters of credit, where, through loans, the Bank ensured paying customers to third parties irrevocable commitments amounted to \$25,561 (\$25,222 in 2012).

On December 31, 2012, the Bank acted as an intermediary between a subsidiary of HSBC in Tokyo, and a Mexican government enterprise, thus providing a guarantee which was \$4.

The amount of the provisions recorded at December 21, 2013, for letters of credit and guarantee receivables, amounts to \$29 and is included in the allowance for loan losses (\$157 in 2012).

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

At December 31, 2013 and 2012, the Bank had no losses caused by the guarantee and letters of credit.

(b) Assets in trust or under mandate -

At December 31, 2013 and 2012, the Bank's trust activity, which is recorded in memorandum accounts, is summarized as follows:

	<u>2013</u>	<u>2012</u>
Type of trust:		
Administrative	\$ 298,141	273,996
Guarantee	56,296	43,403
Investment	52,811	53,155
Other	<u>31,285</u>	<u>31,561</u>
	<u>438,533</u>	<u>402,115</u>
Mandates to:		
Administrative	840	611
Guarantee	93	42
Investment	<u>3</u>	<u>2</u>
	<u>936</u>	<u>655</u>
	\$ 439,469	402,770
	=====	=====

Trust activities revenue for the years ended December 31, 2013 and 2012 amounted to \$180, each year.

(c) Investments on behalf of customers-

At December 31, 2013 and 2012 the Bank received funds from the public and invested them in various instruments of the Mexican financial system on behalf of its customers, which are recorded in memorandum accounts as follows:

	<u>2013</u>	<u>2012</u>
Funds of investment companies:		
Managed by HSBC	\$ 3,091	3,397
Other	19,980	22,314
Government securities	22,924	18,540
Equities and other	<u>4,358</u>	<u>5,195</u>
	\$ 50,353	49,446
	=====	=====

In case that the funds are invested in the Bank's own instruments, the amounts of such funds are included in the consolidated balance sheet.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(d) Assets in custody -

The Bank records in this account the assets and securities of third parties it receives in custody or for management purposes. At December 31, 2013 and 2012, this account comprises:

	<u>2013</u>	<u>2012</u>
Custody	\$ 326,472	310,367
Administration	49,894	53,183
Guarantee	1,294	1,237
Collection	<u>1,019</u>	<u>1,208</u>
	\$ 378,679	365,995
	=====	=====

For custody operations, types of goods handled are: stocks and shares in custody, government paper, bankers' acceptances, corporate bonds and shares. Amounts related to securities issued by the institution itself amount to \$2,885 (\$1,506 in 2012) and are classified as follows:

	<u>2013</u>	<u>2012</u>
Bank paper	\$ 2,773	1,382
In private debt	<u>112</u>	<u>124</u>
	\$ 2,885	1,506
	=====	=====

For management operations, types of goods, including goods and foreign values that are received for administration are: bank stocks, private or government.

At December 31, 2013 and 2012, income from activity of assets under custody and administration operations amount to \$35 and \$36, respectively.

(28) Additional information on results of operation and segments-**(a) Condensed statement of operations by segment-**

The condensed consolidated statement of operations by segment includes Retail Banking and Wealth Management (RBWM), Commercial Banking (CMB), Global Banking and Markets (GBM) and other Corporate Activities (OAC). A brief description of the Bank's business segments follows:

Retail Banking and Wealth Management – Focused primarily on individuals that comprise mainly consumer products, which include credit cards, personal and car loans as well as mortgage loans and traditional deposits.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Commercial Banking – Focused primarily on corporations, offering financing in Mexican pesos and other currencies, lines of credit for working capital, term loans, and the financing of exports, in addition to financial services relating to checking and investment accounts and cash management.

Global Banking & Markets – Focused primarily on corporations, which comprise: trust, treasury and custody services, corporate finance advisory, as well as risk management and cash flow services. This segment comprises products such as letters of credit, factoring, discounted documents and investments in the money and capital markets.

The allocation of income to each segment is determined in accordance with the profile of the client. For the allocation of expenses to each segment a cost management system is used which utilizes an Activity Based Costing (ABC) approach, although directly identifiable segment costs are not subject to this methodology. Within HSBC a catalogue of transactions and their relevant costs exists, and in this way each time that a transaction is completed for a client, the cost of this transaction is registered in the segment to which that client belongs.

In the following page is presented the condensed statement of operations by segment for the years ended December 31, 2013 and 2012.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

Condensed statements of operations by segment

Years ended December 31, 2013 and 2012

(Millions of pesos)

	RBWM		CMB		GBM		Total	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
Financial margin	\$ 13,304	12,311	5,850	6,182	1,584	1,737	20,738	20,230
Allowance for loan losses	<u>(5,963)</u>	<u>(5,668)</u>	<u>(1,525)</u>	<u>(60)</u>	<u>(598)</u>	<u>194</u>	<u>(8,086)</u>	<u>(5,534)</u>
Adjusted financial margin	7,341	6,643	4,325	6,122	986	1,931	12,652	14,696
Commissions and fees, net	4,568	3,902	1,475	1,621	505	697	6,548	6,220
Financial intermediation income	101	86	173	179	1,999	2,421	2,273	2,686
Other operating income	2,156	2,485	428	1,202	224	429	2,808	4,116
Administrative and promotion expenses	<u>(13,490)</u>	<u>(13,618)</u>	<u>(5,491)</u>	<u>(6,069)</u>	<u>(2,592)</u>	<u>(2,656)</u>	<u>(21,573)</u>	<u>(22,343)</u>
Total operating income	676	(502)	910	3,055	1,122	2,822	2,708	5,375
Equity in the results of non consolidated subsidiaries, associated and affiliated companies	<u>26</u>	<u>22</u>	<u>13</u>	<u>11</u>	<u>4</u>	<u>2</u>	<u>43</u>	<u>35</u>
Income before income tax	<u><u>702</u></u>	<u><u>(480)</u></u>	<u><u>923</u></u>	<u><u>3,066</u></u>	<u><u>1,126</u></u>	<u><u>2,824</u></u>	<u><u>2,751</u></u>	<u><u>5,410</u></u>

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The condensed statement of cash flows by segment for the years ended December 31, 2013 is presented as follows:

	2013		
	<u>RBWM</u>	<u>CMB</u>	<u>GBM</u>
Net income	\$ 548	720	878
Adjustments for non cash items	2,975	1,419	915
Operating activities	(6,998)	(4,199)	1,463
Investments activities	(968)	(495)	(447)
Financing activities	1,370	1,010	1,370
Net (decrease) increase of cash and cash equivalents	(3,073)	(1,545)	4,179
Cash and cash equivalents			
At the beginning of the year	<u>34,588</u>	<u>21,657</u>	<u>(399)</u>
At end of year	\$ <u>31,515</u>	<u>20,112</u>	<u>3,780</u>
	=====	=====	=====

The assets and liabilities identifiable by the different segments at December 31, 2013 and 2012 are analyzed as follows:

	2013			2012		
	<u>RBWM</u>	<u>CMB</u>	<u>GBM</u>	<u>RBWM</u>	<u>CMB</u>	<u>GBM</u>
Assets	\$ 62,821	81,329	48,618	56,686	91,093	53,019
Liabilities	162,347	94,754	30,707	160,975	99,372	32,831
	=====	=====	=====	=====	=====	=====

Financial Margin

The financial margin for the years ended December 31, 2013 and 2012 is analyzed as follows:

	<u>2013</u>	<u>2012</u>
Interest income:		
Cash	\$ 1,395	1,567
Investment securities	5,924	6,737
Interest and premium on securities Purchased under agreements to resell	<u>565</u>	<u>2,063</u>
Subtotal interest income to the following page	\$ <u>7,884</u>	<u>10,367</u>

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

	<u>2013</u>	<u>2012</u>
Subtotal interest income from previous page	\$ 7,884	10,367
Loan portfolio:		
Commercial loans	7,142	8,173
Financial institutions	266	359
Consumer loans	10,154	8,705
Residential mortgages	2,157	1,946
Government entities	1,347	1,601
Initial fees for loan granting	210	212
Others	<u>(167)</u>	<u>(16)</u>
	<u>28,993</u>	<u>31,347</u>
Interest expense:		
Deposit funding	(1,668)	(2,310)
Time deposit	(3,416)	(4,398)
Due to banks and other institutions	(420)	(588)
Bank bonds	(162)	(249)
Interest and premiums on securities purchased under agreements to resell	(1,911)	(2,914)
Interest by subordinated debt issued	(521)	(516)
Others	<u>(157)</u>	<u>(142)</u>
	<u>(8,255)</u>	<u>(11,117)</u>
Financial margin	\$ 20,738	20,230
	=====	=====

(b) Financial intermediation income-

For the years ended December 31, 2013 and 2012, the financial intermediation income is analyzed as follows:

	<u>2013</u>	<u>2012</u>
<i>Valuation gain (loss):</i>		
Investment securities	\$ (514)	396
Trading derivatives	483	1,267
Foreign currency exchange and precious metals	<u>178</u>	<u>232</u>
Total valuation gain (loss) to the following page	\$ <u>147</u>	<u>1,895</u>

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

	<u>2013</u>	<u>2012</u>
Total valuation gain (loss) from previous page	\$ <u>147</u>	<u>1,895</u>
<i>Purchase/sale gain (loss):</i>		
Investment securities	286	1,057
Securities repurchase/resell agreements and trading derivatives	1,038	(385)
Foreign currency exchange and precious metals	<u>802</u>	<u>119</u>
	<u>2,126</u>	<u>791</u>
Total financial intermediation income	\$ <u>2,273</u>	<u>2,686</u>
	=====	=====

(c) Other operating income, net-

For the years ended December 31, 2013 and 2012, "Other operating income, net" is analyzed as follows:

<u>Income</u>	<u>2013</u>	<u>2012</u>
Recoveries and reimbursements	\$ 714	1,345
Payments received in relation to the use of infrastructure from subsidiaries	1,833	2,138
Gain on sale of properties	1	50
Gain on sale of foreclosed assets	121	76
Loan to employees	137	137
Cancellation of excess of allowance for loan losses (note 12d)	6	857
Others	<u>1,056</u>	<u>279</u>
	<u>3,868</u>	<u>4,882</u>
 <u>Expenses</u>		
Write offs	(315)	(591)
Foreclose assets reserve	(27)	(34)
Loss on sale of properties	(214)	(141)
Others	<u>(504)</u>	<u>-</u>
	<u>(1,060)</u>	<u>(766)</u>
Other operating income, net	\$ <u>2,808</u>	<u>4,116</u>
	=====	=====

(*) Within the expenses there are fraud losses of \$134 (\$451 in 2012).

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(d) Financial Ratios-

The principal ratios as of and for the years ended December 31, 2013 and 2012 are analyzed below:

	<u>2013</u>	<u>2012</u>
Non-performing loans to total loans	5.93%	2.02%
Allowance for loan losses to past-due loan portfolio	100.55%	233.75%
Operating efficiency (<i>administrative and promotional expenses to average total assets</i>)	4.33%	4.73%
ROE (<i>net income to average stockholders' equity</i>)	4.75%	9.71%
ROA (<i>net income to average total assets</i>)	0.43%	0.82%
Liquidity (<i>liquid assets/liquid liabilities</i>)*	102.99%	90.97%
Financial margin after provision for loan losses /average interest earning assets	2.86%	3.56%
Capital index to credit risk assets	22.26%	22.36%
Capital index to market and credit risk	14.81%	14.51%
	=====	=====

* *Liquid assets* – Cash and cash equivalents, trading and available-for-sale securities.

* *Liquid liabilities* – Demand deposits, demand and short-term bank and other loans.

(29) Commitments and contingent liabilities-**(a) Leases-**

Certain premises and equipment are leased. Lease agreements provide for regular adjustments to rent amounts based on changing economic factors. Total lease expense amounted \$1,482 in 2013 and \$1,601 in 2012.

(b) The Bank has executed a distribution agreement with Principal Afore, S. A. de C.V., Principal Grupo Financiero, in which there is a commitment to distribute on an exclusive basis its products through the Bank branches over a five-year period, ending in 2016.

(c) On March 7, 2012, the Bank signed a distribution agreement with AXA Seguros, S. A. de C. V., whereby the Bank agrees to the exclusive distribution of general insurance products in exchange for an agreed-upon commission. The term of the agreement is 10 years from April 2013.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

(c) *Lawsuits and litigation -*

The Bank is involved in a number of lawsuits and claims arising in the normal course of business. It is not expected that the final outcome of these matters will have a significant adverse effect on the Bank's financial position and results of operations.

In accordance with FRS C-9 liabilities, provisions, contingent assets and liabilities and commitments, the Bank classifies its legal obligations in:

Probable: When the possibility of future event occurs is high (probability of loss greater than 50%);

Possible: The possibility that the future events occurring is more than remote but less than likely (probability of loss greater than 5% and less than 50%);

Remote: The possibility that the future events occurring is low (probability of loss greater than 5%).

At December 31, 2013 and 2012, the Bank presented in the consolidated financial statements the recognition of liabilities for this purpose for an amount of \$266 and \$264 respectively, which correspond to cases in which it was considered that the possibility of loss would likely be probable. The Bank at December 31, 2013 and 2012 had outstanding cases with a possible loss contingency in the amount of \$59,348 and \$59,428, respectively.

The Bank has contingent liabilities in disputes with third parties, which have not been disclosed pursuant the related financial reporting standards given that the administrative procedure is at an initial stage and no resolution has been issued yet.

(30) Risk management (unaudited)-

Within the Financial Group of HSBC in Mexico the comprehensive risk management involves both compliance with Prudential Provisions on the Subject of Comprehensive Risk Management included in the "Circular Unica" issued by the Banking Commission and the worldwide Group regulations established by HSBC Holding PLC (HGHQ), whose ultimate purpose is generating shareholder value, whilst maintaining a conservative profile in respect of exposing the organization to risk.

The recognition of fundamental concepts is essential for efficient and effective comprehensive management of risks, both quantifiable and discretionary (credit, market and liquidity) and non-discretionary: operational (technology and legal) and under the premise that basic identification, measurement, monitoring, limitation, control and divulging processes are fulfilled.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

As in its principal affiliates, the Bank's risk management function begins with the Board of Directors, who has primary responsibility for approving the related objectives, guidelines and policies and for determining the risk exposure limits, which is supported by the Assets and Liabilities Committee (ALC) and the Risk Management Committee (RMC).

Assets and Liabilities Committee (ALC)

This Committee meets on a monthly basis and is chaired by the Bank's Executive President and General Director. Committee members include senior bank executives from areas such as: Corporate, Business and Commercial and support areas such as: Treasury, Finance, Risks, Treasury Operations, Balance Sheet Management, Planning and Economic Capital. Similar structures are maintained at other affiliates.

The ALC is the prime vehicle for attaining the objectives of an adequate management of assets and liabilities. Its principal purposes concerning risks are as follows:

- Providing strategic management and ensuring tactical follow-up by creating a balance sheet structure that integrates objective compliance within the pre-established risk parameters.
- Identifying, monitoring and controlling all relevant risks, including the information generated by the RMC.
- Distributing the necessary information for proper decision making.
- Conducting overall reviews of sources and destination of funds.
- Determining the most likely environment for the Bank's assets and liabilities in planning and considering contingency scenarios.
- Evaluating alternatives for: rates, prices and portfolio mixes.
- Reviewing and becoming accountable for: distribution and maturity of assets and liabilities, position and size of interest margins, liquidity levels and economic utility.

For reinforcing decision making, the local ALCs as is the case of Mexico's report directly to the Group's Central Finance Direction of HGHQ.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Risk Management Committee (RMC)

The Risk Committee is responsible to the Board of Directors. The Committee may meet with the frequency with which it is deemed necessary. It is expected that the Committee sessions on a monthly basis, and is usually held the third week of the month.

In response to the regulatory Dispositions and in order to have independent opinions to the Bank's management, the Risk Committee is composed of three external counsellors, and senior managers of the Bank, including the CEO, Deputy CEO of Risk, Deputy CEO of Audit, Deputy CEO of Consumer Banking, Deputy CEO of Commercial Banking, Deputy CEO for Global Banking, Deputy Corporate CEO and CTSO, Deputy CEO of Finance, Head of Legal, Head of Global Markets, Chief Risk in Latin America and Secretary. The Committee is chaired by an external Counsellor.

The major Committee objectives, which are shared with Bank affiliates, are as follows:

- Monitoring of current and potential risks that could impact the operation of the Bank, its realization and evaluate the potential impact they might have, either reputational, financial or operationally. You must also develop a focused and integrated approach to identifying them.
- Propose solutions to improve early risk profile and review strategies for risk mitigation.
- Develop a clear profile and trends in credit, market, liquidity, insurance, operational, reputational and internal controls that could impact or cause changes in business strategy.
- Establish a process focused on risk management of relevant risks, contingencies and mitigating and consolidate reporting risks ALCO review.
- Approve and propose to the Board changes in rules and policies on Risk Management, in accordance with the regulation that sets the Banking Commission.
- Authorize the maximum tolerance to market risk, credit risk and other risks considered acceptable in terms of treasury operations (derivatives).
- Review and approve the goals, operations and control procedures, and the level of risk tolerance, based on market conditions.
- Authorize the terms of reference of committees depend on it, including the authorization of its members and provide them with guidance and supervision in their activities.
- Approve the methodologies for measurement and identification of all risks.
- Oversee the approval of new products as well as subsequent revisions and amendments.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

- Approve changes to the methodology for calculating reserves and the economic factor and emergency periods.
- Develop and modify the objectives, guidelines and policies origination and credit administration.
- Review important topics that are open, which will be included in the certification of the Director General (depending on time of certification), likewise, should monitor the resolution of these issues.
- Monitor the current risks that might have an impact on the legal entities comprising the Group, at the frequency defined for each entity.

Market Risk**Qualitative information****a) Description of qualitative issues related to the Comprehensive Risk Management process.**

The objective of the Bank's market risk management function is to identify, measure, monitor, limit, control, inform and disclose the various risks to which the institution is exposed.

The Board of Directors establishes the RMC, whose objective is to manage the risks to which the institution is exposed, and to oversee that transactions adhere to the risk management purposes, policies and procedures and the global and specific risk exposure limits previously approved by the Board of Directors.

Market risk, as defined by the institution, is the "risk that market prices and rates on which the Bank has taken positions – interest rates, foreign exchange rates, stock prices, etc. – move adversely relative to positions taken, thus causing losses to the Bank; that is, the potential loss arising from changes in risk factors relating to the valuation or expected results of assets, liabilities or contingent liability transactions, such as interest rates, foreign exchange rates, price indexes, among others.

The main market risks to which the Bank is exposed, can be generally classified in accordance with the exposure of its portfolios to variances of the different risk factors, as follows:

- Currency or exchange risk.- This risk arises in open positions of currencies other than the local currency, which lead to exposure to potential losses due to variances in the exchange rates involved.
- Interest rate risk.- This risk results from having to maintain assets and liabilities (real, nominal or notional) with various maturity or depreciation dates. Thus, exposure to changes in the interest rate levels is created.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

- **Stock risk.**- This risk emerges from maintaining open positions (purchase or sale) with stock or stock-based instruments. Thus, exposure to changes in the market price of stock or stock-based instruments is created.
- **Volatility risk.**- The volatility risk is related to financial instruments with options so that their price depends, among other factors, on volatility perceived in the option's underlying asset (interest rate, stock, exchange rate, etc.)
- **Base or margin risk.**- This risk arises when an instrument is used as hedge of another one and each is valued using different rate curves (for instance, a government bond hedged by an interbank rate derivative) so that the market value may differ leading to hedge imperfections.
- **Credit Risk Margin** it is the risk of incurring losses in the price of corporate bonds, bank or sovereign in foreign currency for credit changes in the credit perception of the issuer.

b) Principal elements of market risk management methodologies.

The Bank measures elected to identify and quantify the Market Risk exposure are Value at Risk (VaR) and "Present Value of a Basis Point" (PVBP) calculations, which measure the sensitivity to interest rates. Both risk measures are monitored on a daily basis compared to market risk exposure limits duly approved by Management. Additionally, stress testing is performed. Furthermore, it is important to mention that to calculate VaR and PVBP, all of the Bank's positions are marked to market.

Value at Risk (VaR)

The VaR is the statistical measure of a portfolio's maximum potential loss arising from changes in market risk factors of the financial instruments for a given holding period. Therefore, the VaR calculation is based on specific levels of confidence and holding periods. Since January 2006, the VaR is obtained by Historical Simulation with total valuation, considering 500 historic changes in the market risk factors. The Board of Directors, at the Risk Committee's proposal, has set a confidence level of 99% with a 1-day holding period; accordingly, the VaR level represents the maximum loss that that the Bank could possible experience in one day with a 99% probability.

Present Value of a Basis Point (PVBP) and Forward PVBP (F-PVBP)

The PVBP is a technique to measure the market risk exposure resulting from changes in interest rates. This measure shows the potential loss that results from a one basis point change in interest rates used to determine the price of financial assets and liabilities, marking to market all of the positions in financial instruments sensitive to interest rates.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The purpose of the Forward PVBP (F-PVBP) is to measure the effect of interest rate changes on financial instruments subject to interest rates. In this sense, the F-PVBP is based on the assumption of a scenario in which the forward rates implied in the curve increase by one basis point.

Surcharge risk

By surcharge risk we understand the potential adverse fluctuation in the value of positions of financial instruments with surcharge (floating government bonds) due to market fluctuations in such risk factor.

Base risk

Base risk is the term used for describing the risk that exists for the movement of a market (due to internal factors) with respect to others. The base risk increases when an instrument is used for hedging another one and the instrument prices are set by two different interest rate curves.

These differences are caused by the various existing characteristics between markets, which are:

- Regulation
- Individual market restrictions
- Calendars
- Conventions (basis in rates)
- Others

Credit Spread (CS01)

The Credit Spread Risk or CS01 is used to control the risk of keeping the bonds issued by the private sector, the value of which may vary due to changes in the credit rating of the issuers.

Such credit rating is reflected in the profit differential with respect to sovereign bonds. HSBC employs market risk limits to control the sensitivity that value may experience in these positions due to changes in the credit rating of issuers.

Vega or Volatility Risk

The Bank takes positions in instruments that are sensitive to changes in implicit market volatility, such as interest rate options and foreign exchange. Vega limits are used to control the risks associated with such market volatilities.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Stress testing

This is a technique that takes into consideration extreme values occurring isolatedly but which are unlikely based on the distribution of probabilities assumed for the market risk factors, but in case it happens this could generate from moderate to severe impacts. The generation of stress testing scenarios for analyzing the sensitivity of the Bank's positions and the interest rate risk exposure is performed on the basis of hypothetical scenarios. Both positive and negative changes are considered to measure the impact on the portfolios of the Bank.

At the same time, the base PVBP forward is linearly extrapolated to the hypothetical scenarios (assuming that the portfolio is perfectly linear) so as to compare both calculations and obtain the implied convexity. In addition stress tests are performed in relation to exchange rates and share prices.

Methods for Validation and Calibration of Market Risk models

In order to detect in a timely manner any decrease in the prediction quality of the model, automatic data loading systems are in place, thus preventing manual data inputting. Furthermore, for the purpose of measuring the efficiency of the VaR estimation model, back-testing is performed. This type of test allows verification that the maximum estimated losses, on average, do not exceed the reliability level established, comparing the profits/losses that would have been generated had the portfolio been held during the VaR holding period. Back-testing is reinforced by performing hypothesis testing procedures.

As for the PVBP, it has been compared with the sensitivity of the portfolios to market quotations. The results of these tests confirm the accuracy of the models. In order to reinforce the validation and verification of the various risk factors, a set of matrices has been designed that show the behaviour of different risk factors selected in order to check their reasonableness in relation to the values prevailing in the financial markets and verify the current value and the value on the preceding business day for consistency.

Portfolios subject to VaR and PVBP calculation

For a detailed and precise portfolio management, and adhering to the international (IAS) and local (Local GAAP) standards or effective market risk management, the Market Risk management of HSBC Mexico has perfect control of the portfolio structure. Such specific classification should at all times be comprehensible from an accounting viewpoint. This allows for calculating the risk measures (sensitivity, potential loss and stress measures) for any sub-portfolio aligned with the accounting.

The market risk area calculates the VaR and PVBP for the Bank's total portfolio and specific Accrual and Total Trading portfolios so as to monitor the Bank's own and trading positions.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Global VaR is estimated for each portfolio. Additionally, VaR is broken down by risk factors (Interest Rates and Foreign Exchange Rates and Interest rate, FX and Shares volatilities).

PVBP is presented by segment of the forward curve (Buckets), for both peso and dollar interest rates (Accrual and Trading Intent).

Stress testing is performed for the Bank's portfolio and the "Total Trading" and "Accrual" portfolios, furthermore, a special stress test is performed for Available for Sale (AFS) and Hedging Securities (CSH and FVH).

Quantitative information

As follows it is going to be presented, the Bank's VaR and PVBP and the Total Trading and Accrual portfolio sub-division of "Trading Intent" and "Accrual" for the 4Q of 2012 (in million of dollars).

The VaR & PVBP limits shown correspond to the latest updating of Market Risk Limits approved by the Group's Board of Directors and the Risk Committee.

Value at Risk (VaR) (All risk factors being considered)

	<u>Bank</u>		<u>Total Trading</u>		<u>Accrual</u>	
	Average		Average		Average	
	Q4 2013	Limits*	Q4 2013	Limits*	Q4 2013	Limits*
Total	17.51	38	3.29	11.5	15.55	35
Rates	14.08	40	2.82	6.5	13.00	38
Credit margin	4.24	22	0.51	4	3.76	22
Exchange rates	0.77	5	0.78	5	N/A	N/A
Interest rates volatility	0.04	4.5	0.04	2	-	2.5
FX rates volatility	-	2	-	2	N/A	N/A
Equities	0.00	2.5	0.00	2.5	N/A	N/A
	====	====	====	====	====	====

* Absolute value, N/A = Not applicable

* Global Market Value at Risk (VaR) (Compared to last quarter)

Global Market Value at Risk (VaR) (Compared to last quarter)

	<u>September 30, 2013</u>	<u>December 31, 2013</u>	<u>Limits *</u>	<u>Q3 2013 average</u>	<u>Q4 2013 average</u>
Bank	19.81	16.78	38	19.72	17.51
Accrual	20.07	13.30	35	18.47	15.55
Total trading	1.83	4.11	11.5	2.35	3.29
	====	====	====	====	====

* Absolute value, N/A = Not Applicable

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The Bank's VaR at the end of the fourth quarter of 2013 decrease - 15.30% in respect of the 3Q 2013. During the period, VaR levels remained below the limits set by management.

The Bank's average VaR for the fourth quarter of 2013 decrease - 11.21% in respect of the average VaR for the 3Q 2013.

Comparison of Market risk VaR to Net Capital

Below a comparative VaR average against Net Capital table as of September 30 and December 31, 2013; in millions of dollars:

	September 30, 2013	December 31, 2013
Total VaR *	19.72	17.51
Net Capital **	4,020.91	3,957.35
VaR / Net Capital	0.49%	0.44%
	=====	=====

* Quarterly Average VaR of the Bank (absolute value)

** Net Capital of the Bank at the end of quarter

Average market VaR represented 0.44% of net capital in fourth quarter of 2013.

Present Value of a Basis Point (PVBP) for Peso Interest Rate

	Sep 30, 2013	Dec 31, 2013	Limits *	Average Q3 2013	Average Q4 2013
Bank	(1.195)	(1.279)	1.90	(0.963)	(1.196)
Accrual	(1.167)	(1.101)	1.45	(0.895)	(1.074)
Trading desk	(0.028)	(0.178)	0.30	(0.068)	(0.122)
	=====	=====	=====	=====	=====

* Absolute value N/A - Not Applicable

The Bank's PVBP in peso rates for the close of the fourth quarter of 2013 varied 7.03% with respect to the PVBP for the close of the previous quarter. The Bank's average PVBP corresponding to the fourth quarter of 2013 varied 24.20% with respect to the PVBP for the close of the previous quarter.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Present Value of a Basis Point (PVBP) for Dollar Interest Rates

	<u>Sep 30, 2013</u>	<u>Dec 31, 2013</u>	<u>Limits*</u>	<u>Q3 average 2013</u>	<u>Q4 average 2013</u>
Bank	0.080	0.034	0.430	0.026	0.043
Accrual	0.043	(0.008)	0.300	(0.010)	0.006
Trading desk	0.036	0.042	0.130	0.036	0.037
	=====	=====	=====	=====	=====

* Absolute value N/A - Not applicable

The Bank's PVBP in US dollars interest rate at the end of Q4 2013 changed by (57.50%) as compared to the PVBP at the end of Q3 2013. The Bank's average PVBP for Q4 2013 changed by (65.38%) as compared to the average PVBP for Q3 2013.

Present Value of a Basis Point (PVBP) for UDIS interest rates

	<u>Sep 30, 2013</u>	<u>Dec 31, 2013</u>	<u>Limits*</u>	<u>Average Q3 2013</u>	<u>Average Q4 2013</u>
Bank	(0.047)	(0.057)	0.150	(0.049)	(0.047)
Accrual	(0.035)	(0.031)	0.050	(0.038)	(0.033)
Trading desk	(0.012)	(0.026)	0.100	(0.011)	(0.013)
	=====	=====	=====	=====	=====

* Absolute value N/A - Not applicable

The Bank's PVBP in UDIS interest rate at the end of Q4 2013 changed by 21.28% as compared to the PVBP at the end of Q3 2013. The Bank's average PVBP for Q4 2013 changed by (4.08%) as compared to the average PVBP for Q3 2013.

Liquidity risk**Qualitative information**

Liquidity risk arises primarily from gaps between the maturities of the Institution's assets and liabilities. Customer demand and time deposits mature on dates which differ from those of loans placed and investment securities.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

HSBC has implemented liquidity ratio limits both in pesos and dollars. These liquidity ratios are calculated daily and compared to the limits authorized by the Assets and Liabilities Committee and confirmed by the HSBC Group. In addition, the Institution performs a daily review of cash commitments and evaluates the requirements of the principal customers for diversifying the sources of funding.

In addition, HSBC has implemented a methodology for measuring liquidity risk based on different period cash flow projections and the formulation of liquidity scenarios.

Since 2003, HSBC implemented a liquidity contingency plan, which defines the potential liquidity-related contingencies and establishes plan responsible individuals, action plan and alternative sources of funding available to the Institution should a contingency arise. During the year, the Assets and Liabilities Committee ratified the plan.

Quantitative information

At the end of Q4 2013, HSBC liquidity ratios were USD\$4,210 million in term up to 7 days, USD\$2,363 million in a term of a month, USD\$1,169 million in a term of 3 months; every scenario resulted in a positive cumulated cash flow. This is a reflection of the Entity's adequate cash flow position for the subsequent twelve months.

During the quarter, average levels were USD\$3,085 million in 7 days, USD\$1,589 million for 1 month, of USD\$1,180 million for 3 months. With respect to last quarter's liquidity position was affected by transactions changes made, money market operations and long-term investment.

Credit risk-**Qualitative information**

For managing the credit risk at HSBC, in addition to following up on the behaviour of the loan portfolio on a regular basis, risk assessment tools are developed, implemented and monitored. The primary objective of managing the credit risk is knowing the quality of the portfolio and taking timely action for reducing potential losses associated with credit risks, complying at the same time with the Group's and Basel II policies and standards as well as Banking Commission's regulations.

Credit risk is defined as the risk of financial loss if a customer or counterparty fails to meet an obligation under a contract with a Group member or members, that is, the potential loss on lack of payment by a borrower or counterparty. For the proper measurement of the credit risk HSBC has credit risk quantification methodologies as well as advanced information systems.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

In general, the methodologies separate client risk (probability that a client defaults its payment obligations: Probability of Default) from credit or transaction risks (risk inherent to the structuring of the loan, which mainly includes the value and type of security).

In addition, HSBC has developed policies and procedures that comprise the various loan process stages: assessment, granting, control, follow-up and recovery.

a) Model and systems used for the quantification and management of credits risk:

Commercial portfolio

1. Allowance for loan losses

Since June 2013, the Bank adopted the new rules for estimating preventive reserves established by the CNBV in the Provisions, which set forth an expected loss methodology.

Administrative models

The Bank has various models for internal risk management, developed to encompass the three key parameters of credit risk:

1. Probability of default
2. Loss given default
3. Exposure at default

These models are evaluated and monitored on a quarterly basis to assess their performance and their proper application, so that the follow-ups are carried out in a timely manner.

Regarding the models of Probability of Default (PD), monitoring is aimed at testing the differentiation between customers that comply with their obligations to the Bank and those which do not, and will order them by the appropriate risk levels. Moreover, it validates the quantification model and compared with observed default rates to meet its accuracy.

On the other hand, for models of Exposure at Default and Loss Severity, it is validated the estimates on the loss that may be incurred by the institution in case that the client fail, are accurate with sufficient conservatism.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

It is important to note that each version of the models is reviewed and approved according to standards set by the Group.

a) Probability of default model (PD)

The Bank developed eight models for risk rating customers of the business portfolio with annual sales of up to \$7,000, which was implemented in October 2010 (These models are derived from statistical analysis of the various economic activities that resulted in four large segments which are subdivided by the level of sales, higher and less than \$100).

It is important to note that these models were reviewed and approved by experts in model developing of HGHQ.

In addition to the above models, the Bank has implemented the following global models that were developed by HGHQ.

- A model to evaluate the global clients (GLCS), applicable to mayor corporate offices with sales equal to or greater than USD \$7,000.
- A model for banking financial entities (RAfBanks).
- Eleven models for non-banking financial entities (NBFIDST).

The implementation of the models mentioned in the previous paragraphs was accompanied by a new level of customer risk rating known as Customer Risk Rating (CRR), which consists of 23 levels, of which two are for customers in default.

This scale has a direct correspondence to Probabilities of Default and allows sufficient granular measurement of the creditworthiness of customers.

The default probability models included in the internal rating system are monitored quarterly with the aim of checking its proper performance, and if the results of this monitoring are not the expected according to Bank standards action plans are established to meet the established guidelines.

In the results of the last monitoring for commercial portfolio models developed locally (for corporate head offices with annual sales of up to \$7,000), we noticed a good overall statistical performance with an Accuracy Ratio of 0.57, which is over the Group-established threshold; however, the overrides rates have been increasing during 2013 above the level desired for these models. It is worth noting that these 8 models are currently in the process of being improved.

The rest of the global models, GLCS, RAf Banks and NBFIDST are low default models so it is currently not possible to measure their performance; however, override rates are being monitored, which are within the tolerances set out by the Group.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

b) Model of estimation of Loss Given Default (LGD)

Regarding the estimation of Loss Given Default (LGD), which represents the economic loss as a percentage of exposure to default that will face the Bank at the time that a customer defaults, the Bank developed a local model for business and corporate clients. Similarly, for banking financial institutions, the Bank has implemented a model developed by HGHQ.

The most recent monitoring of the LGD model shows a relatively low correlation (17.89%) between the observed and the estimated Severity; therefore, the model is currently in the process of being redeveloped.

c) Model of exposure at default (EAD)

For estimating the Exposure at Default (EAD), the Bank also developed a model for local business and corporate customers. It is also estimated the exposure at default of banking financial institutions based on the guidelines established by HGHQ.

In order to have a more accurate measurement of risk, the Exposure at Default model was modified in 2012, and is currently being evaluated under the standards that HGHQ has determined to subsequently be upgraded in computing systems.

The most recent quarterly performance monitoring for this model showed a satisfactory (over 50%) correlation between the values of the observed and the estimated EAD.

2. Risk assessment system

In order to establish a better infrastructure, management and measurement of credit risk for commercial loans, the Bank uses the assessment tool Moody's Risk Analyst (RA), which allows an assessment of the credit quality of the customers based on their financial and qualitative information.

Furthermore, HSBC has a system worldwide for managing, controlling and better following up on the commercial loan approval process in Commercial Banking known as *Credit Application and Risk Management* (CARM), used for approving most loan applications. This system allows for finding out the status of the loan application during and process stage. Additionally, only in a few cases, applications are approved via *Workflow Authorization* (SIPAC). This system will be replaced by CARM at the end of 2014.

Additionally, and in order to improve the administration of the guarantees of commercial loans, since 2006 the Bank has been using the system called Fair II. Finally, it is important to note that it also has a system that controls and limits the use of credit lines from approval Lines III.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Quantitative information

The expected loss of the portfolio of commercial loans at December 31, 2013 is \$12,228, showing a decrease of \$1,870 (18%) over the previous quarter. The average balance of commercial loans at December 31, 2013 is \$162,922 with an increase of \$5,155 (3%) compared to that reported in the previous quarter.

Below are average balances and the expected loss of the commercial portfolio by business line:

Line of Business	Average Balances for the 3-month period		VAR		Balances		VAR		Expected Loss		VAR	
	3T2013	4T2013	(\$)	(%)	Sep-13	Dic-13	(\$)	(%)	Sep-13	Dic-13	(\$)	(%)
CMB	\$93,777	\$95,086	\$1,309	1%	\$93,144	\$97,038	\$3,894	4%	\$8,647	\$10,586	\$1,939	22%
GBM	\$63,865	\$67,610	\$3,745	6%	\$66,815	\$68,819	\$2,005	3%	\$1,711	\$1,642	-\$69	-4%
GBP	\$125	\$226	\$100.99	81%	\$130	\$275	\$145.39	112%	\$0.11	\$0.01	-\$0.10	-88%
Total	\$157,767	\$162,922	\$5,155	3%	\$156,322	\$160,088	\$3,766	2%	\$10,358	\$12,228	\$1,870	18%

Portfolio of consumer credit and mortgage

Qualitative information

An efficiency assessment of consumer and mortgage loan originating models is performed on a quarterly basis, for verifying that the population being assessed by the model is similar to the population used for constructing the model, that the model continues to have the ability to distinguish delinquent customers from those who are not and that the model continues to award high ratings to customers with lesser risk. The model is recalibrated or replaced when an efficiency deviation is detected.

As part of the management of the consumer and mortgage loan portfolios monthly reports are issued for measuring creditworthiness. Reports are segmented by product and include general portfolio statistics, measures of distribution by level of default, default measures by date of opening, transition reports by level of default, etc. Also, the portfolio expected loss is determined monthly. The expected loss model currently being used considers a two-dimensional approach where each loan is assigned a Likelihood of Default and a percentage of Severity of Loss. The model is calibrated for estimating losses expected over an annual horizon and was prepared using the previous portfolio experience.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Quantitative information

The expected loss for the commercial portfolio of consumer credit and mortgage at December 31, 2013 is \$5,094, which represents 8% of the total balance, a decrease of \$90 (1.8%) with respect to previous balance in Q3 2013.

Operational risk**Qualitative information**

Operational risk is the risk of loss arising from internal processes, people and systems failure or external events including technological and legal risks.

The corporate governance structure which underpins the function is complemented by the Operational Risk and Internal Control Committee and by the Operational Risk Management Group which operate as sub-committees of the Risk Management Committee and which are responsible for compliance with the relevant applicable standards and regulations as well as knowing and understanding the risk profile of the company, establishing the risk management priorities, evaluating the strategies and plans for risk mitigation and to monitor risk exposure and mitigation measures on an ongoing basis.

The scheme HGHQ operational controls is based on "three lines of defence", in order to ensure that risks and controls are properly managed global business areas, support areas and the area of global technology services (HTS) continuously. The model establishes administrative responsibilities based on risk management and control environment. The model of the three lines of defence should be applied with common sense, considering the business structures and HGHQ support.

First line of defence

The first line of defence comprises predominantly managing global business areas and HTS, which are responsible for their activities, processes and controls should be checked daily and to identify, mitigate and monitor key risks in all its activities and operations by a control environment commensurate with risk appetite. Management is responsible for creating its own control equipment, as necessary, to delegate these responsibilities.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Second line of defence

The second line of defence comprises mainly global support areas whose function is to verify compliance with the statement of risk appetite HGHQ. Your responsibilities are:

- Ensure, monitor and exceed the effectiveness of risk and control activities carried out by the first line;
- Develop frameworks to identify and measure the risks assumed by the parties respective business area;
- Monitor the performance of key risks through key indicators and monitoring programs / safety in relation to risk appetite and tolerance levels defined.

Furthermore, global support areas must maintain and monitor controls which are directly responsible.

Third the line defence

The third line of defence is to provide independent assurance by Internal Audit regarding the effectiveness of the design, implementation and integration of risk management frameworks and management of risks and controls by the first line and monitoring control by the second line.

Proof of use of these lines of defence, is the ongoing verification to gather evidence of compliance with the ORIC management framework within the decision making process of the business. It is also a formal practice referred to gathering evidence that the following facts are carried out continuously:

- The Department is aware and is involved in the management of operational risk.
- Operational risk processes and management information used to inform decision-making.
- The quality of operational risk management information is inadequate to make business decisions.

By identifying and assessing risk and operational controls as part of its decision-making process, senior management must inform thereof ORIC and these should be reflected in the reports of the entity.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

The heads of the areas (senior management), to monitor the operational risk management and internal control environment, should-for-control section:

- Establish an appropriate organizational structure with BRCMs Equipment (Business Risk and Control Managers for its acronym in English) in order to ensure effective coverage of all business and operations under their span of control, ensuring that staff complies BRCMs Team are individuals with experience and skills suitable for the performance of its functions:
 - Identify and assess operational risk and controls as part of the decision making process (Test Use).
 - Identify and report incidents.

BRCM teams are responsible, within their respective areas, the following:

- Define key operational risks and set minimum standards of control and indicators / meters suitable;
- Conduct supervision to verify the adequacy of the monitoring of administrative control (functional). When these teams carry out supervision, ORIC can strengthen this work fulfilling its oversight responsibilities to avoid duplication of effort, providing you follow the rules strictly and properly;
- Review and report indicators / meters and take the appropriate action when an area is operating or risk of operating outside the established risk appetite;

ORIC team is responsible for ensuring that they comply with the minimum standards set.

Each year, for the tenth consecutive year has been conducted identifying and evaluating all operational risks throughout all Bank entities worldwide reassessment period is in December 2013. The methodology used for this exercise was reinforced by new guidance based Framework Operational Risk Management Group specifies that all areas of the Group should conduct a Risk Assessment and Control (RCA) or guest reviews Operational Risk at least once a year. The Risk Assessment Methodology and Approach Control has replaced ABCD identification and operational risk self-assessment (RSA) and is applicable to all entities of the Bank worldwide.

The Operational Risk and Internal Control Management are responsible for coordinating and guiding the RCA practices at the Bank. During the execution of the RCA annual year 2012-2013 relevant risks were denominated, described and classified into fourteen categories: Compliance, Fiduciary, Legal, Accounting Information, Tax, Internal Fraud, External Fraud, Persons, Political, Physical, Business Continuity, Systems, Operations and Project.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Quantitative information (including Technology Risk and Legal Risk)

The assessment of operational risks resulting from the 10th evaluation exercise carried out during the period 2012-2013, with the changes and updates made during the 4th quarter of 2013 shows a total of 1,511 relevant risks identified and evaluated, distributed as follows: 7.47% (113) of type A, 14.09% (213) of the type B, 27.92% (422) of the type C and 50.49% (763) of type D.

The evaluation of the operational risks identified from the 10th evaluation realized between 2012-2013, considering the changes and updates made during the 4th trimester of 2013 amounts a total of 1,511 relevant risks identified and evaluated, distributed as follows: 7.47% (113) Type A, 14.09% (213) Type B, 27.92% (422) Type C and 50.49% (763) Type D.

In response to a new regulatory requirement, since the third quarter of 2013 the Loss Events due to Operational Risks are being reported on a quarterly basis to the local regulator using reports R2811 and R2813, which purpose is to collect information on losses over \$1 sustained by the entities, arising from: i) internal control failure or deficiencies; ii) errors in the transaction processing and storage or in the transmission of information; iii) adverse administrative and judicial resolutions; and iv) fraud or theft, all grouped by lines of business, processes and products.

The appetite for operational risk statement for the Bank is US\$34.42 million for operational losses, considering US\$9.12 million for Credit Related Operational Losses (CROLs), is monitored monthly through the BSC, which is presented to the Risk Management Committee.

The cumulative operating loss at December 31, 2013 amounts to a total of USD\$32.13 million.

Both the risks and loss incidents are reported in the corporate platform designed specifically for the management of operational risk and operational record of occurrences.

Technology risk-

The area of information technology (IT) maintains an adequate control technology risk through the guidelines of the Group related to methodologies and standards: FIMs (Functional Instruction Manual), RBPM (risk-based project management), and BIM (procedures general and local work instructions HTS).

In conjunction with the operation structure, the HTS is also in line with the guidelines of other manuals and procedures, among others, the Operations FIM; the foregoing is due to the fact that it is the service and technology solution provider entity for the different channels and business lines of the Bank.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

As part of its governance structure, the Bank follows up the topics and requirements of the local authority through its compliance area, where one of its main functions is the constant assessment of the risk and the monitoring of the compliance with local law.

The principal methodologies used in the technological risk valuation are:

- I. Through a streamlined governance structure, safe and reliable: designed to maintain proper control of technological risks and response capabilities for all banking services provided at the various distribution channels. The risk is managed in the high-level committees: HTS Steering Committee, Risk Management Committee (RMC), Operational Risk & Internal Control Committee (ORICC) and Group Operational Risk Management (GGRO).
- II. The above is carried out with the updating and testing of different scenarios for the Business Continuity Plans (BCP) and its corresponding disaster recovery plan (DRP) for events that required the positioning of its operation in alternative sites.
- III. Risk and Control Assessment (RCA).
- IV. Information technology project management through the standard tool of the group (Risk-Based Project Management - RBPM).
- V. Risk management with active participation of the specialized Business Risk and Control Management area (BRCM's), including operation risk management, Sarbanes Oxley (SOX), internal, external and regulatory audits coordination.
- VI. This is carried out with a measurement tool and control scorecard that enables the measurements of the main objectives defined in its strategic planning, which in general refers to the system availability, the project and budget compliance in terms of time and quality and that are presented in different forums and committees for decision-making purposes.

Legal risk

Legal risks which could give rise to financial loss, sanctions or reputational damage, have been defined as follows:

- Contractual: This is the risk that the rights or obligations in a contractual relationship are inadequate, including: misrepresentations, documentation, unintended consequences, unintended breaches, enforceability and external factors;
- Litigation: It consists of the risks to which one is subject to when an actual or potential litigation situation occurs, and includes both the exposure and the litigation handling;

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

- Legislative: It is the risk of noncompliance with the laws of the different jurisdictions and includes: the compliance with such regulation and its amendments;

On the other hand, policies, controls and procedures are designed to enable the identification, measurement and control of the legal risk in order to avoid potential financial losses and operation errors. The specific risks that are intended to be mitigated are as follows:

- Non contractual rights: It is the risk that assets are not duly appropriated, that other parties breach the rights related to such assets or that the rights of the other party are breached, including infringement, ownership interest and legal liability.

All contracts entered into by any member of the institution that contains restrictions that affect the business must have the authorization of the legal representative with appropriate authority levels. Additionally, there are procedures for the regular review of standard contracts to ensure that they remain properly in the light of any legal change.

- Contractual Risk Control; They have procedures to ensure that any document that creates a contractual relationship can be signed on behalf of the institution, unless it is received legal advice internal and / or external, either in relation to the form of the documentation or specifically on the transaction and in most cases, are standardized contracts.
- Litigation: Litigation Risk Control: Procedures are established to ensure appropriate action in response to the claims against, defend efficiently and effectively, be able to take action with the ability to protect and preserve the rights of the institution and inform the responsible Legal issues on trial.

Practices or procedures are properly documented and in place to ensure that liability is not admitted involuntarily in situations of dispute, and it can not be inferred from any internal correspondence or third parties.

They have procedures and regulations for the Legal area is immediately reported if there is threat of litigation or whether to proceed against the institution, managing demand subsequent actions.

- Legislative Risk Control: There are documented procedures and practices implemented to monitor any new law or regulation proposal and any court case resulting in the need to change existing procedures or documentation in their respective jurisdiction and any other jurisdiction which they are responsible. From this, and with the area of Compliance (Compliance), implemented the necessary changes so that operations continue to be made in accordance with current legislation.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

- Risk Management for Failure no contractual rights: There are procedures in place to ensure that the legal care at all times the correct use of the Group's brands, local brands, advertisements and copyright.

For a third party to make use of the Group's brands or local brands must be previously validated and approved by the Legal Department.

There is a procedure to verify the legal area when required use of trademarks or proprietary third party advertisements, is duly authorized by the holder.

The legal department cares at all times that all the artistic or literary works that are generated either by his charge to employees or outside vendors or by subsequent acquisition of proprietary rights, are properly documented.

The Legal department is involved in any social media activity and campaign that is initiated by its business area within its jurisdiction. The approval of the Central Legal Offices is required for all social media activities.

The Legal Operational Controls is based on the three defense lines scheme mentioned in the Operational Risk section of this document, to guarantee that the risks and controls are duly managed throughout the year the exercise of the function of the first and second defense lines.

Also been met institutional policies, procedures have been established about Operational Risk and Internal Control, there have been statutory audit has been carried out the estimation of potential losses arising from adverse judgments and established a base historical data on judicial decisions, its causes and costs.

U.S. regulatory and law enforcement investigations:

In October 2010, HSBC Bank USA subscribed a cease and desist order with the Office of the Comptroller of Currency ("OCC"); and the indirect holding of such company, HSBC North America Holdings ("HNAH") subscribed a cease and desist order issued by the U.S. Federal Reserve Board (the "Orders"). Such orders provide for improvements to establish an effective compliance program in handling risk in the activities of HSBC in the U.S.A., including several topics relating to the U.S. Banking Secrecy Act ("BSA") and compliance of money laundering prevention ("MLP"). Action continues to comply with the Order requirements to ensure their compliance and to maintain effective policies and procedures.

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HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

In addition to the foregoing, in December 2012, HSBC Holdings, HNAH and HSBC Bank USA subscribed agreements with government agencies of the U.S. and U.K. as to deficiencies in the past in complying with LSB, PLD and sanctions acts. Among these agreements, HSBC Holdings and HSBC Bank USA subscribed a 5-year deferred prosecution agreement with the US Department of Justice (“DJ”), with the U.S. Attorney’s Office for the Eastern District of New York and with the U.S. Attorney’s Office for the Northern District of West Virginia (“DPA of USA”), HSBC Holdings subscribed a two-year deferred prosecution agreement with the New York County District Attorney (“FDCNY”) (“DPA of FDCN”) and HSBC Holdings subscribed a cease and desist order; HSBC Holdings and HNAH subscribed the consent of a monetary sanction of the Federal Reserve Board (“FRB”). In addition to the foregoing, HSBC Bank USA subscribed the consent of a monetary sanction of the Department of Treasury’s Financial Crimes Enforcement Network) (“FinCEN”) and a diverse monetary sanction of OCC. HSBC Holdings also subscribed an agreement with the Office of Foreign Assets Control (“OFAC”) in regard the historical transactions that involve parties subject to OFAC sanctions and an Undertaking with the UK Financial Services Authority (currently the Financial Conduct Authority Direction (“FCA”)for complying with certain obligations in relation to the PLD in the future and with obligations relating to sanctions.

In accordance with these agreements, HSBC Holdings and HSBC Bank USA made payments for a total of US\$1,921m to the US authorities and continue complying with the outstanding obligations. On July 1, 2013, the United States District Court for the Eastern District of New York approved the DPA of USA and retained jurisdiction for supervising its implementation. In conformity with these agreements with the DJ, the FCA and the FRB, a independent corporate compliance monitor has been appointed (which, for FCA purposes is an “expert” according to section 166 of the US Financial Services and Markets Act), who shall continually assess and examine the effectiveness of PLD compliance and HSBC sanctions as well as progress in implementing obligations in accordance with the relevant agreements. The monitor’s activities, which started on July 22, 2013, are being conducted as planned and are consistent with the terms and requirements set out in the relevant agreements.

Where HSBC Holdings and HSBC Bank USA meet the requirements imposed by the DPA of USA, the charges imposed by the DJ against these entities shall be dismissed after the five-year term relating to the agreement has expired. In like manner, if HSBC Holdings meets the requirements imposed by the DPA of the FDCN, the charges imposed by FDCNY against it shall be dismissed after the two-year term relating to this agreement has expired. Both DJ and FDCNY may initiate actions against HSBC Holdings or HSBC Bank USA in cases where any of these entities violates the terms and conditions of their respective agreements.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

HSBC Bank USA also subscribed a separate consent order with the OCC, whereby the former is required to correct the circumstances and conditions observed by the OCC in its last supervision report; furthermore, certain restrictions are imposed on HSBC Bank USA with regard to any acquisition of direct or indirect control of, or investment in any new financial subsidiary or for initiating a new activity in its existing financial subsidiaries, unless it receives prior authorization from the OCC. HSBC Bank USA also subscribed a separate consent order with the OCC that compels it to adopt a global institutional compliance program.

The agreements with US and UK authorities do not exclude the possibility of litigation with regard, among other things, to HSBC's compliance with PLD and LSB laws and sanctions or other regulatory or law enforcement actions relating to PLD, LSB or sanctions not foreseen by the agreements.

(31) Credit policies-

Management constantly reviews the consistency between the objectives, guidelines and policies, supporting infrastructure (processes, appropriate personnel and computer systems) and functions of credit origination and management within the Bank, ensuring at all times, irrespective in carrying out their activities to avoid conflicts of interest, in addition those activities performed by the Comprehensive Risk Management process.

Credit promoting-

Promotion of retail credit (individuals) and commercial (individuals with small business and companies) is performed through a branch, internet and / or other means, according to business areas.

Credit evaluation-

Qualitative and quantitative evaluations to approve and grant the different types of financing is done through individual or parametric methods, using models or opinion of highly qualified personnel that meet the standards of the Basel II and the Banking Commission established independently by the area of credit risk.

Credit approval-

Only the highest level by the Board of Directors are empowered to approve individual commercial loans, who in such case, may be delegated to other local officials experienced, considering the level of risk of potential borrowers and their operations.

Credit approval by parametric methods, is performed using automated systems to analyze customer information, based on minimum required information which is standardized data and information, which shed weight for a favourable outcome has been previously defined by the risk area.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

Instrumentation-

The legal department is responsible for the implementation of all credit transactions, including processing of all credit contracts, promissory notes and the issuance of the opinion of the legal capacity of their applicants.

Restructuring-

Restructuring may only be made viable projects, avoiding incurred in renewing the operation not to affect the Bank Guarantees, working to improve the position. Policy not current Securities shall be released and in case of the possibility of replacing them, they should be the same or better.

As an exception to this policy can restructure clients not showing viability of payment, when by this means improve the Bank's position (with partial payments, higher guarantees, correcting problems documentaries).

A restructuring operation is one which is derived from any of the following situations:

- a) Extension of Credit Guarantees of the concerned, or;
- b) Changes to the original terms of the loan or payment schedule, among which are:
 - Changing the stated interest rate for the remaining term of the loan;
 - Currency exchange or unit of account, or
 - Provision of a waiting period for compliance with the obligations to pay under the original terms of the loan, unless the award is granted after the deadline originally agreed, in which case it will be a renewal.

Restructuring is not permitted to hide losses.

Monitoring, control and recovery-

The rating of the loan portfolio is made according to the methodology and procedures to comply with the Group standards, Basel II and the Banking Commission, determined by the area of credit risk.

Credit records are concentrated in specialized facilities and are administered by accredited, while parametric loans are integrated by credit.

Monitoring, administrative or judicial recovery, including the assignment of loan portfolio, involves fair treatment of customers and considering best practices, according to criteria established by the business areas, collections, legal and/or credit risk, as appropriate, as well as the areas and people who perform the role of comprehensive risk management.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

To ensure a risk-based approach, that is consistent with the problematic exposure and minimizes potential losses, management requirements and criteria that must be met are established, which responsibility is of the area of analysis and credit approval.

Officials of the segments are responsible for detecting early warnings of broken profiles of their credit portfolios, as well as gather the necessary information for analysis and monitoring, within the management process.

The control and monitoring of credit activity is complemented by the internal audit function, independent of the business and administrative areas.

(32) Recently issued accounting standards -

The Consejo Mexicano de Normas de Información Financiera, A. C. (CINIF) has issued the FRS and Improvements listed below:

FRS B-12 “*Offsetting financial assets and financial liabilities*”- FRS B-12 is effective for years beginning on or after January 1, 2014; however, earlier adoption is permitted as of January 1, 2013. Among its principal features, we cite the following:

- Principles are established in relation to the rights of offset that should be considered for presenting, on a net basis, a financial asset and a financial liability in the statement of financial position.
- FRS B-12 establishes the requirements to be met by an offsetting intention, based on the principle that a financial asset and a financial liability should be presented by the offset amount, provided the future cash flow from its collection or settlement is net.
- FRS B-12 establishes other subjects relating to the offsetting of financial assets and liabilities such as the intention of realizing the asset and settling the liability simultaneously for its net presentation in the statement of financial position, the bilateral and multilateral offsetting agreements and the treatment of collateral.

FRS C-3 “*Accounts Receivable*”- FRS C-3 is effective for years beginning January 1, 2016, and is applicable retrospectively; however, early adoption is permitted. Some of the primary changes resulting from the adoption of this FRS are as follows:

- FRS C-3 provides that accounts receivable based on a contract are deemed financial instruments. On the other hand, some other accounts receivable, resulting from legal or tax provisions, may include certain characteristics of a financial instrument, such as bearing interest, though these are not deemed financial instruments.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIAS

Notes to the Consolidated Financial Statements

(Millions of pesos)

- FRS C-3 sets out that the allowance for doubtful trade receivables shall be recognized as revenue is earned. Thus, the allowance shall be recorded as expenses in the statement of comprehensive income.
- FRS C-3 provides that, from the initial recognition, the money value in time shall be considered. Therefore, should the effect of the present value of the account receivable be significant in view of its term, an adjustment must be made taking into consideration such present value.
- A reconciliation between the initial and final balances of the allowance for doubtful accounts is required for each period presented.

FRS C-11 “Stockholders’ equity”- FRS C-11 is effective for years beginning January 1, 2014, and is applicable retrospectively. FRS C-11 supersedes Bulletin C-11 “Stockholders’ equity” and Circular 38 “Temporary acquisition of treasury stock” and Circular 40 “Accounting treatment of stock issuance and placement costs”. Some of the main aspects resulting from the adoption of this FRS are as follows:

- FRS C-11 requires that in order to capitalize the advances for future capital stock increases, at the stockholders’ or partners’ meeting it shall be agreed that such advances be applied for future capital stock increases and also, the price per share to be issued pursuant to such contributions shall be fixed. Furthermore, it shall be agreed that these contributions shall not be refunded before being capitalized.
- FRS C-11 broadly identifies financial instruments with characteristics of equity which would otherwise, be regarded as liabilities. However, the specific standard that classifies financial instruments as either equity or liabilities, within the same compound financial instrument, is FRS C-12 “Financial instruments with characteristics of liabilities and equity”.

FRS C-12 “Financial instruments with characteristics of liabilities and equity”- FRS C-12 is effective for years beginning January 1, 2014, and is applicable retrospectively. FRS C-12 supersedes Bulletin C-12 “Financial instruments with characteristics of liabilities, equity or both”, and the provisions regarding these instruments under Bulletin C-2 “Financial instruments”. Some of the main aspects resulting from the adoption of this FRS are as follows:

- This FRS sets forth that the primary characteristic to be met for a financial instrument to be classified as an equity instrument, is that its holder be exposed to the entity’s risk and rewards rather than the right to charge the entity a fixed amount.
- By exception, if certain conditions apply and, provided there is no other obligation virtually assured to require payment to the holder, a redeemable instrument is classified as equity.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

- The subordination concept is included.
- An instrument may be classified as equity if there is an option to issue a fixed number of shares at a price fixed in a currency other than the issuer's functional currency, provided that all existing owners of the same class of equity instruments have that option, on a pro rata basis.

FRS C-14 “*Transfer and retirement of financial assets*”- FRS C-14 is effective for years beginning on or after January 1, 2014, with retrospective effects and is issued for amending the absence of accounting standards with regard to the transfer and retirement of financial assets. The main aspects covered by this FRS include the following:

- Based on the principle of assigning the risks and benefits of ownership of a financial asset as primary condition for its retirement.
- For a transfer to signify that the transferor may retire a financial asset from its statement of financial position, it is required that it may no longer have a future benefit or loss with regard to such financial asset.

FRS C-20 “*Receivable financing instruments*”- FRS C-20 shall be effective for years beginning January 1, 2016, and is applicable retrospectively. Early application is not permitted and FRS C-20 supersedes the provisions set forth in Bulletin C-3 in this regard. Some of the main aspects resulting from the adoption of this FRS are as follows:

- Classification of financial instruments under assets. To determine such classification, the concept that defines the intention to acquire and hold financial instruments has been ruled out. Instead, the concept of management business model is adopted, either for obtaining a contractual yield, generating a contractual yield and selling in order to achieve certain strategic objectives, or generating earnings from the purchase and sale thereof, in order to classify them in accordance with the respective model.
- The valuation effect of investments in financial instruments is also focused on the business model.
- The reclassification of financial instruments is not permitted among receivables, strategic investments, and negotiable instruments, unless the entity changes its business model.
- The embedded derivative that modifies the cash flows of principal and interest is not separated from its host receivable financial instrument. The entire receivable financial instrument shall be measured at fair value, as if it were a negotiable financial instrument.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

2014 FRS Improvements

In December 2013, CINIF issued the document referred to as “2014 FRS Improvements”, which contains precise modifications to some FRS. The modifications that bring about accounting changes are listed below:

FRS C-5 “Prepayments”- FRS C-5 provides that amounts paid in foreign currency be recognized at the exchange rate in force as of the transaction date, and shall not be modified as a result of foreign exchange fluctuations between the functional currency and the foreign currency in which the prices of goods and services regarding such prepayments are denominated. Additionally, it provides that impairment losses arising from prepayments, as well as the reversal of such losses, shall be reported as part of the net income or loss for the period. These improvements are effective for years beginning January 1, 2014, and the resulting accounting changes shall be recognized retrospectively.

Bulletin C-15 “Impairment or disposal of long-lived assets”-

Bulletin C-15 provides that the impairment loss for a long-lived asset in use, as well as the reversal thereof, and the impairment loss of long-lived, available-for-sale assets, including increases or decreases, shall be reported in the results of operations for the period, under the line items of costs and expenses, where depreciation and amortization is recognized. The impairment loss and reversal thereof, for indefinite-lived intangible assets, including goodwill, shall be presented in the results of operations for the period, under the line item for depreciation and amortization expenses on assets of the cash generating unit to which such tangible assets relate. Under no circumstances shall impairment losses be presented as part of the expenses that have been capitalized in the value of a certain asset.

Likewise, it sets out that in order to report the impairment losses of associates, joint ventures and other permanent investments, and the goodwill thereof, the provisions of FRS C-7 shall be complied with. FRS C-7 provides that impairment losses be recognized under the line item equity in the net income or loss of other entities.

Additionally, Bulletin C-15 sets out that assets and liabilities identified with discontinued operations shall be presented in the statement of financial position, grouped in a single line item of assets and a single line item of liabilities, classified as short-term, and shall not be offset between them. Furthermore, such items shall be reported as long-term in the event of sale agreements that are essentially purchase options and sale - leaseback agreements. It also provides that the entity shall not restate previously issued statements of financial position as a result of such reclassification.

These improvements are effective for years beginning January 1, 2014, and any resulting presentation changes shall be recognized retrospectively.

(Continued)

HSBC MEXICO, S. A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(Millions of pesos)

FRS B-3 “Statement of comprehensive income”, FRS B-16 “Financial statements of non-profitable entities”, FRS C-6 “Property, plant and equipment”, FRS C-8 “Intangible assets”, Bulletin C-9 “Liabilities, provisions, contingent assets and liabilities and commitments” and FRS D-3 “Employee benefits”- The improvements of these standards are aimed at performing the modifications related to the presentation of certain transactions that were previously recognized under the line item of other income and expenses, as the presentation of such line item ceased to be required after the new FRS B-3 became effective. These improvements are effective for years beginning January 1, 2014 and the resulting presentation changes shall be recognized retrospectively.

Management estimates that the new FRS and the improvements to FRS will be immaterial.

Financial Reform-

On January 10, 2014 amendments to various financial laws and decrees, known as the “Financial Reforms” were published in the Federal Official Gazette. These amendments purport, among other things, to: i) boost development banks; ii) increase the legal certainty of the activities of private financial institutions and promote the increase of the credit supply at more competitive costs; iii) encourage competition between financial institutions; and iv) strengthen the regulatory framework. Such Financial Reform considers greater surveillance attributes to the National Commission for the Protection and Defense of Financial Services Users (“CONDUSEF”) for overseeing and regulating financial products. The Bank is currently in the process of assessing the impacts that this Financial Reform may have on its operations and financial performance taking into account that amendments to subsidiary laws and specific rules to be issued by the Banking Commission, the Central Bank and other related bodies are still in the process of being developed.