

## HSBC BANK CANADA SECOND QUARTER 2003 REPORT TO SHAREHOLDERS

- Net income<sup>‡</sup> was C\$146 million for the half-year ended 30 June 2003, an increase of 24.8 per cent over the same period in 2002.
- Net income was C\$73 million for the quarter ended 30 June 2003, an increase of 78.0 per cent over the second quarter of 2002.
- Return on average common equity was 19.1 per cent for the six months ended 30 June 2003 and for the quarter ended 30 June 2003 compared with 14.8 per cent and 10.1 per cent, respectively, for the same periods in 2002.
- The cost:income ratio was 56.3 per cent for the half-year ended 30 June 2003 and 57.1 per cent for the quarter ended 30 June 2003.
- Total assets of C\$36.1 billion at 30 June 2003 compared with C\$35.1 billion at 30 June 2002.
- Total assets under administration were C\$15.8 billion at 30 June 2003, of which C\$12.4 billion were funds under management and C\$3.4 billion were custody and administration accounts.

<sup>‡</sup> HSBC Bank Canada acquired Merrill Lynch HSBC Canada Inc. ('MLHSBC') on 31 October 2002. For financial reporting, the income and expenses of MLHSBC were accounted for effective 1 July 2002, the date the HSBC Group acquired full ownership of MLHSBC, and were recorded in the results for the fourth quarter of 2002.

## Financial Commentary

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HSBC Bank Canada recorded net income of C\$146 million for the six months ended 30 June 2003, an increase of C\$29 million, or 24.8 per cent, from C\$117 million for the comparable period in 2002. Net income for the quarter ended 30 June 2003 was C\$73 million compared with C\$41 million for the second quarter of 2002, an increase of 78.0 per cent. Excluding a C\$28 million restructuring charge in the second quarter of 2002, the increase would have been 8.5 per cent and 23.9 per cent, respectively, for the six months and quarter ended 30 June 2003 compared with the same periods in 2002. The improvement in net income resulted from higher net interest income and lower levels of provisions for credit losses.

Martin Glynn, President and Chief Executive Officer, said: "Results were satisfactory given the mixed economic conditions we have experienced. While there was an improvement in the equity markets during the second quarter, the uncertain outlook continues to have an adverse impact on capital markets and mutual fund revenues. However, record low interest rates and high consumer confidence continued to fuel an active housing market in Canada. Growth in residential mortgages and consumer loans benefited net interest income. Credit losses for the six months and quarter ended 30 June 2003 were lower than in the same periods in 2002 as provisions in the prior periods covered an exposure in the telecommunications sector.

"The current strength of the Canadian dollar relative to the US dollar and the ongoing uncertainty of the economy in the United States is expected to dampen the future demand for Canadian goods and services. In addition, near-term domestic activity, primarily in the travel and hospitality sectors, has been weakened by SARS. We are continually monitoring direct exposures to the affected business sectors to mitigate the impact, if any, that these economic factors may have on the bank.

"We are continuing to align our services for customers in Canada with those of our colleagues in the United States, including Household International, and GF Bitel in Mexico, to create a seamless North American service proposition. By establishing a broader range of services and products to offer our retail and commercial clients in Canada, we should be better positioned to gain market share and benefit when economic conditions improve."

### Net interest income

Net interest income for the six months ended 30 June 2003 was C\$440 million, an increase of C\$16 million, or 3.8 per cent, compared with C\$424 million for the same period in 2002. For the quarter ended 30 June 2003, net interest income was C\$222 million, an increase of C\$9 million, or 4.2 per cent, over the comparative period in 2002. Net interest income continued to benefit as the impact of higher volumes of residential mortgages and consumer loans in the active housing market more than offset the increase in funding costs.

The net interest margin, as a percentage of average interest earning assets, was 2.77 per cent for the six months ended 30 June 2003 compared with 2.86 per cent for the six months ended 30 June 2002. For the quarter, the net interest margin, as a percentage of average interest earning assets, was 2.76 per cent compared with 2.82 per cent for the same period in 2002. For the six months and quarter ended 30 June 2003, the net interest margins were impacted by competitive pricing on residential mortgages and an increase in funding costs as competitive pricing on consumer deposits resulted in a change in funding mix towards higher costing non-consumer deposits.

## Financial Commentary *(continued)*

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### Other income

Other income for the six months ended 30 June 2003 was C\$216 million compared with C\$213 million for the same period in 2002. For the quarter ended 30 June 2003, other income was C\$111 million compared with C\$103 million for the same period in 2002. Increased activity during the first half of 2003 in Personal Financial Services and Commercial Banking resulted in higher credit fees and deposit and payment service charges. The increased volatility of foreign exchange rates helped boost income from foreign exchange transactions in 2003 compared with 2002. Income from securitisations was lower for the six months ended 30 June 2003 due to a C\$9 million gain recognised in the first quarter of 2002 on the sale of personal loans.

Capital market fees were higher for the six months ended 30 June 2003 compared with the same period in 2002. This was aided by an improvement in equity markets in the second quarter of 2003 and income from MLHSBC of C\$9 million and C\$6 million, respectively, for the six months and the quarter ended 30 June 2003. The restructuring of the institutional equity business in the second quarter of 2002 also impacted comparability of capital market fees between 2003 and 2002. The uncertainty of the global equity markets continued to dampen retail investor activity. As a result, mutual fund and administration fees were lower for the six months ended 30 June 2003 compared with the same period in 2002.

### Non-interest expenses

Non-interest expenses were C\$369 million for the six months ended 30 June 2003 compared with C\$374 million for the same period in 2002. For the quarter ended 30 June 2003, non-interest expenses were C\$190 million compared with C\$205 million for the same period of 2002. The second quarter of 2002 included a C\$28 million restructuring charge related to the withdrawal from institutional equity trading, sales and research activities. Non-interest expenses for the six months and the quarter ended 30 June 2003 included C\$12 million and C\$7 million, respectively, from MLHSBC.

Salaries and employee benefits were higher in the six months and quarter ended 30 June 2003 compared with the same periods in 2002. Variable compensation costs were higher, due in part to increased capital markets and foreign exchange revenue, and employee medical costs increased, reflecting the higher portion of these costs borne by the private sector. Included in salary costs were MLHSBC expenses amounting to C\$3 million and C\$2 million, respectively, for the six months and quarter ended 30 June 2003. Other non-interest expenses were higher for the six months and quarter ended 30 June 2003 compared with the same periods in 2002 largely from MLHSBC related costs of C\$6 million and C\$4 million, respectively. These increases were offset by lower operating losses for the six months ended 30 June 2003 compared with the same period in 2002.

### Provision for income taxes

The effective tax rate for the six months ended 30 June 2003 was 39.2 per cent compared with 37.4 per cent for the same period in 2002. For the quarter ended 30 June 2003, the effective tax rate was 39.2 per cent compared with 35.9 per cent for the second quarter of 2002. The higher effective tax rate in 2003 reflected lower levels of tax-exempt investment income compared with 2002.

## **Financial Commentary** *(continued)*

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### **Credit quality and provision for credit losses**

The provision for credit losses was C\$39 million for the six months ended 30 June 2003 compared with C\$68 million in the same period of 2002. For the quarter ended 30 June 2003, the provision for credit losses was C\$19 million compared with C\$43 million for the same period in 2002. The higher provision level in 2002 related to an exposure in the telecommunications sector. While the ongoing performance of our loan portfolios is satisfactory, the outlook remains uncertain in light of the slow economic recovery, particularly in the United States.

Total impaired loans decreased by C\$101 million, or 29.1 per cent, to C\$246 million at 30 June 2003 compared with C\$347 million at 30 June 2002. The allowance for credit losses was in excess of impaired loans by C\$92 million compared with C\$12 million at the same time last year. As at 30 June 2003, the loan portfolio consisted of a higher proportion of lower risk residential mortgages. The allowance for credit losses, as a percentage of loans outstanding, was 1.36 per cent compared with 1.53 per cent at the same time last year.

### **Balance sheet**

Total assets at 30 June 2003 were C\$36.1 billion, up C\$1.0 billion from 31 December 2002. Consumer confidence and historical low interest rates continue to benefit business volumes as residential mortgages, net of securitisations, and consumer loans were C\$0.6 billion higher at 30 June 2003 compared with 31 December 2002. Commercial volumes also increased as bankers' acceptances grew by C\$530 million in 2003.

Total deposits were flat from 31 December 2002 to 30 June 2003. Personal deposits were C\$0.5 billion lower while commercial deposits increased by C\$0.5 billion over the same period. The majority of the decrease in personal deposits was due to the stronger Canadian dollar at 30 June 2003 relative to 31 December 2002. While US dollar based deposits increased slightly during the period, the Canadian dollar equivalent of these deposits was lower upon conversion to Canadian dollars for reporting purposes.

### **Total assets under administration**

Funds under management were C\$12.4 billion at 30 June 2003 compared with C\$11.5 billion at 31 March 2003 and C\$11.7 billion at 30 June 2002 (after including MLHSBC funds of C\$1.9 billion). The net increase in the second quarter of 2003 was aided by the strengthening of the equity markets over the same period. However, these increases were offset by the continued strengthening of the Canadian dollar relative to the US dollar.

### **Capital ratios**

The tier 1 capital ratio was 8.0 per cent and the total capital ratio was 10.9 per cent at 30 June 2003. This compares with 8.1 per cent and 11.1 per cent, respectively, at 30 June 2002 and 7.9 per cent and 10.8 per cent at 31 March 2003.

### **Dividends**

A regular dividend of 39.0625 cents per share (totalling C\$2 million) has been declared on the Class 1 Preferred Shares – Series A. The dividend will be payable in cash on 30 September 2003 to shareholders of record on 15 September 2003.

## Review of Business Line Results

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### Personal Financial Services

Income, before taxes and non-controlling interest in income of trust, for the three months ended 30 June 2003 was C\$34 million, compared with C\$25 million for the same period in 2002 and C\$40 million for the first quarter of 2003. For the six months ended 30 June 2003, income, before taxes and non-controlling interest in income of trust, was C\$74 million compared with C\$64 million for the half-year ended 30 June 2002.

Record low interest rates and high consumer confidence continued to fuel an active housing market in Canada and benefit net interest income through growth in residential mortgages and consumer loans. However, margins were negatively impacted by lower spreads in residential mortgages due to competitive pricing and an increase in funding costs as competitive pricing on consumer deposits resulted in a change in funding mix towards higher costing non-consumer deposits. Provision for credit losses were lower due to fewer problem loans. Other income for the quarter and six months ended 30 June 2003 was higher than the same periods in 2002 due to increased capital market fees, primarily from MLHSBC, increased revenue from foreign exchange transactions and increased deposit and payment service charges. These increases were offset by lower securitisation income. Non-interest expenses for the quarter and six months ended 30 June 2003 were higher than the same periods in 2002 due largely to MLHSBC and higher variable compensation costs. The increases were offset by lower operating losses in 2003.

### Commercial Banking

Income, before taxes and non-controlling interest in income of trust, for the three months ended 30 June 2003 was C\$55 million, compared with C\$65 million for the same period in 2002 and C\$55 million for the first quarter of 2003. For the six months ended 30 June 2003, income, before taxes and non-controlling interest in income of trust, was C\$110 million compared with C\$127 million for the half-year ended 30 June 2002.

Net interest income was slightly lower for the six months ended 30 June 2003 compared with the same period in 2002 due to lower term lending as clients opted for shorter-term financing from acceptances. Other income for the quarter and six months ended 30 June 2003 was in line with the comparative periods. The continued uncertain equity markets impacted market sensitive revenues but were largely offset by higher fees generated in the banking operation due to increased volumes in bankers' acceptances and higher revenue from foreign exchange transactions. Non-interest expenses for the quarter and six months ended 30 June 2003 were higher than the same periods in 2002 due to higher variable compensation costs and higher operating losses.

### Corporate, Investment Banking and Markets

Income, before taxes and non-controlling interest in income of trust, for the three months ended 30 June 2003 was C\$48 million, compared with a loss of C\$10 million for the same period in 2002 and income of C\$43 million for the first quarter of 2003. For the six months ended 30 June 2003, income, before taxes and non-controlling interest in income of trust, was C\$91 million compared with C\$28 million for the half-year ended 30 June 2002.

Net interest income was higher for the quarter and six months ended 30 June 2003 than the same periods in 2002 due to repositioning of the balance sheet over the latter part of 2002 to hedge the balance sheet for increasing interest rates. Provision for credit losses in the second quarter of 2002 was higher due to an exposure in the telecommunications sector. Other income for the six months ended 30 June 2003 was lower than the same period last year due to lower capital market fees and trading revenue as a result of the continued uncertain equity markets and the impact of the restructuring of the institutional business in the second quarter of 2002. Non-interest expenses were higher in the second quarter of 2002 due to restructuring charges.

## Summary

<i>Figures in C\$ millions (except per share amounts)</i>	<i>Quarter ended</i>			<i>Half-year ended</i>	
	<i>30 June 2003</i>	<i>31 March 2003</i>	<i>30 June 2002</i>	<i>30 June 2003</i>	<i>30 June 2002</i>
<b>Earnings</b>					
Net income	<b>73</b>	73	41	<b>146</b>	117
Basic earnings per share	<b>0.15</b>	0.15	0.09	<b>0.30</b>	0.25
<b>Performance ratios (%)</b>					
Return on average common equity	<b>19.1</b>	19.0	10.1	<b>19.1</b>	14.8
Return on average assets	<b>0.79</b>	0.81	0.45	<b>0.80</b>	0.67
Net interest margin	<b>2.76</b>	2.79	2.82	<b>2.77</b>	2.86
Cost:income ratio	<b>57.1</b>	55.4	64.9	<b>56.3</b>	58.7
Other income:total income ratio	<b>33.3</b>	32.5	32.6	<b>32.9</b>	33.4
<b>Credit information</b>					
Impaired loans	<b>246</b>	243	347		
Allowance for credit losses					
- Balance at end of period	<b>338</b>	326	359		
- As a percentage of impaired loans	<b>137 %</b>	134 %	103 %		
- As a percentage of loans outstanding	<b>1.36 %</b>	1.33 %	1.53 %		
<b>Average balances</b>					
Assets	<b>36,275</b>	35,587	34,598	<b>35,933</b>	34,172
Loans	<b>24,322</b>	23,960	22,885	<b>24,142</b>	22,468
Deposits	<b>28,732</b>	28,464	27,738	<b>28,599</b>	27,228
Common equity	<b>1,505</b>	1,510	1,563	<b>1,507</b>	1,547
<b>Capital ratios (%)</b>					
Tier 1	<b>8.0</b>	7.9	8.1		
Total capital	<b>10.9</b>	10.8	11.1		
<b>Total assets under administration <sup>‡*</sup></b>					
Funds under management	<b>12,447</b>	11,528	9,844		
Custody and administration accounts	<b>3,388</b>	3,285	5,077		
Total assets under administration	<b>15,835</b>	14,813	14,921		

<sup>‡</sup> Custody and administration accounts as at 30 June 2002 included C\$1,894 million of assets administered on behalf of MLHSBC. As a result of the MLHSBC acquisition, these balances were reflected in funds under management effective 1 July 2002.

\* Balances as at 30 June 2002 are restated to eliminate inter-company holdings of assets.

**Consolidated Statement of Income (Unaudited)**

<i>Figures in C\$ millions (except per share amounts)</i>	<i>Quarter ended</i>			<i>Half-year ended</i>	
	<i>30 June 2003</i>	<i>31 March 2003</i>	<i>30 June 2002</i>	<i>30 June 2003</i>	<i>30 June 2002</i>
<b>Interest and dividend income</b>					
Loans	352	333	318	685	617
Securities	30	28	28	58	55
Deposits with regulated financial institutions	14	13	14	27	32
Total interest income	396	374	360	770	704
<b>Interest expense</b>					
Deposits	165	147	139	312	264
Debentures	9	9	8	18	16
Total interest expense	174	156	147	330	280
<b>Net interest income</b>	222	218	213	440	424
Provision for credit losses	19	20	43	39	68
<b>Net interest income after provision for credit losses</b>	203	198	170	401	356
<b>Other income</b>					
Deposit and payment service charges	20	20	18	40	35
Credit fees	17	16	16	33	31
Capital market fees	22	16	15	38	35
Mutual fund and administration fees	13	13	15	26	30
Foreign exchange	15	14	13	29	25
Trade finance	7	6	7	13	13
Trading revenue	2	3	5	5	7
Securitisation income	3	5	2	8	14
Other	12	12	12	24	23
Total other income	111	105	103	216	213
<b>Net interest and other income</b>	314	303	273	617	569
<b>Non-interest expenses</b>					
Salaries and employee benefits	95	87	83	182	168
Premises and equipment	28	29	27	57	55
Other	67	63	67	130	123
Restructuring costs	-	-	28	-	28
<b>Total non-interest expenses</b>	190	179	205	369	374
<b>Income before taxes and non-controlling interest in income of trust</b>	124	124	68	248	195
Provision for income taxes	47	47	23	94	70
Non-controlling interest in income of trust	4	4	4	8	8
<b>Net income</b>	73	73	41	146	117
Preferred share dividends	2	2	2	4	4
<b>Net income attributable to common shares</b>	71	71	39	142	113
Average common shares outstanding (000)	471,168	471,168	456,168	471,168	456,168
Basic earnings per share	0.15	0.15	0.09	0.30	0.25

See notes to consolidated financial statements

**Condensed Consolidated Balance Sheet (Unaudited)**

<i>Figures in C\$ millions</i>	<i>At 30 June 2003</i>	<i>At 31 December 2002</i>	<i>At 30 June 2002</i>
<b>Assets</b>			
Cash and deposits with Bank of Canada	371	417	406
Deposits with regulated financial institutions	<u>3,713</u>	<u>3,317</u>	<u>3,869</u>
	<u>4,084</u>	<u>3,734</u>	<u>4,275</u>
Investment securities	2,491	2,875	2,211
Trading securities	<u>596</u>	<u>870</u>	<u>1,087</u>
	<u>3,087</u>	<u>3,745</u>	<u>3,298</u>
Assets purchased under reverse repurchase agreements	<u>596</u>	<u>416</u>	<u>822</u>
<b>Loans</b>			
Businesses and government	11,992	11,949	11,957
Residential mortgage	10,248	9,809	9,250
Consumer	2,573	2,422	2,236
Allowance for credit losses	<u>(338)</u>	<u>(311)</u>	<u>(359)</u>
	<u>24,475</u>	<u>23,869</u>	<u>23,084</u>
Customers' liability under acceptances	2,904	2,374	2,424
Land, buildings and equipment	105	111	109
Other assets	<u>888</u>	<u>940</u>	<u>1,046</u>
	<u>3,897</u>	<u>3,425</u>	<u>3,579</u>
Total assets	<u><u>36,139</u></u>	<u><u>35,189</u></u>	<u><u>35,058</u></u>
<b>Liabilities and shareholders' equity</b>			
<b>Deposits</b>			
Regulated financial institutions	710	758	2,064
Individuals	13,914	14,432	13,595
Businesses and governments	<u>13,641</u>	<u>13,182</u>	<u>12,437</u>
	<u>28,265</u>	<u>28,372</u>	<u>28,096</u>
Subordinated debentures	<u>509</u>	<u>528</u>	<u>541</u>
Acceptances	2,904	2,374	2,424
Assets sold under repurchase agreements	25	28	289
Other liabilities	2,541	1,984	1,890
Non-controlling interest in trust and subsidiary	<u>230</u>	<u>230</u>	<u>230</u>
	<u>5,700</u>	<u>4,616</u>	<u>4,833</u>
<b>Shareholders' equity</b>			
Preferred shares	125	125	125
Common shares	950	950	935
Contributed surplus	165	165	165
Retained earnings	<u>425</u>	<u>433</u>	<u>363</u>
	<u>1,665</u>	<u>1,673</u>	<u>1,588</u>
Total liabilities and shareholders' equity	<u><u>36,139</u></u>	<u><u>35,189</u></u>	<u><u>35,058</u></u>

*See notes to consolidated financial statements*

## Condensed Consolidated Statement of Changes in Shareholders' Equity (Unaudited)

<i>Figures in C\$ millions</i>	<i>Half-year ended</i>	
	<i>30 June 2003</i>	<i>30 June 2002</i>
<b>Preferred shares</b>		
Balance at beginning and end of period	<u>125</u>	<u>125</u>
<b>Common shares</b>		
Balance at beginning and end of period	<u>950</u>	<u>935</u>
<b>Contributed surplus</b>		
Balance at beginning and end of period	<u>165</u>	<u>165</u>
<b>Retained earnings</b>		
Balance at beginning of period	433	400
Net income for the period	146	117
Preferred share dividends	(4)	(4)
Common share dividends	<u>(150)</u>	<u>(150)</u>
Balance at end of period	<u>425</u>	<u>363</u>
<b>Total shareholders' equity</b>	<u>1,665</u>	<u>1,588</u>

*See notes to consolidated financial statements*

## Condensed Consolidated Statement of Cash Flows (Unaudited)

<i>Figures in C\$ millions</i>	<i>At and quarter ended</i>			<i>Half-year ended</i>	
	<i>30 June</i>	<i>31 March</i>	<i>30 June</i>	<i>30 June</i>	<i>30 June</i>
	<i>2003</i>	<i>2003</i>	<i>2002</i>	<i>2003</i>	<i>2002</i>
<b>Cash flows provided by/(used in) operating activities</b>					
Net income	73	73	41	146	117
Trading securities	46	228	(56)	274	66
Other, net	568	74	261	642	158
	<u>687</u>	<u>375</u>	<u>246</u>	<u>1,062</u>	<u>341</u>
<b>Cash flows (used in)/provided by financing activities</b>					
Deposits	(111)	4	1,135	(107)	1,389
Securities sold under repurchase agreements	(55)	52	243	(3)	282
Proceeds from subordinated debentures issued	-	-	100	-	100
Dividends paid	(2)	(152)	(152)	(154)	(154)
	<u>(168)</u>	<u>(96)</u>	<u>1,326</u>	<u>(264)</u>	<u>1,617</u>
<b>Cash flows (used in)/provided by investing activities</b>					
Loans, excluding securitisations	(387)	(430)	(640)	(817)	(1,656)
Proceeds from loans securitised	97	75	89	172	375
Investment securities	116	268	164	384	263
Securities purchased under reverse repurchase agreements	(19)	(161)	(471)	(180)	(394)
Non-operating deposits with regulated financial institutions	(390)	(64)	389	(454)	15
Land, buildings and equipment	-	(7)	3	(7)	2
	<u>(583)</u>	<u>(319)</u>	<u>(466)</u>	<u>(902)</u>	<u>(1,395)</u>
<b>Net (decrease)/increase in cash and cash equivalents</b>	<b>(64)</b>	<b>(40)</b>	<b>1,106</b>	<b>(104)</b>	<b>563</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>3,597</b>	<b>3,637</b>	<b>2,595</b>	<b>3,637</b>	<b>3,138</b>
<b>Cash and cash equivalents, end of period</b>	<b>3,533</b>	<b>3,597</b>	<b>3,701</b>	<b>3,533</b>	<b>3,701</b>
Represented by:					
Cash resources per balance sheet	4,084	3,758	4,275		
less non-operating deposits <sup>†</sup>	(551)	(161)	(574)		
Cash and cash equivalents, end of period	<u>3,533</u>	<u>3,597</u>	<u>3,701</u>		

<sup>†</sup> Non-operating deposits are comprised primarily of cash which reprices after 90 days and cash restricted for recourse on securitisation transactions.

See notes to consolidated financial statements

## Notes to Consolidated Financial Statements (Unaudited)

(all tabular amounts are in C\$ millions)

### 1. Accounting policies

The policies adopted in preparing these interim consolidated financial statements are consistent with those described in the Consolidated Financial Statements for the year ended 31 December 2002. Certain additional disclosures are described in note 6.

Certain comparative amounts have been reclassified to conform with the current period presentation.

### 2. Restructuring costs

As at 30 June 2003, the total unutilized balance of restructuring costs of C\$8 million shown below was included in other liabilities in the consolidated balance sheet.

	Salaries and employee benefits	Premises and equipment	Total
Balance at beginning of quarter	7	4	11
Amount utilized during the quarter	2	1	3
Balance at end of quarter	5	3	8

### 3. Issued and outstanding shares

	<i>At 30 June 2003</i>		<i>At 31 December 2002</i>		<i>At 30 June 2002</i>	
	<i>Number</i>	<i>Amount</i>	<i>Number</i>	<i>Amount</i>	<i>Number</i>	<i>Amount</i>
Class 1 Preferred Shares - Series A	5,000,000	125	5,000,000	125	5,000,000	125
Common shares	471,168,000	950	471,168,000	950	456,168,000	935

### 4. Stock-based compensation

When stock-based compensation awards are granted to employees no compensation cost is recognized. Had compensation cost for certain of the bank's employee stock-based compensation arrangements been determined based upon the fair value method, the net income and earnings per share would not have been materially impacted in the current or comparative periods.

## Notes to Consolidated Financial Statements (Unaudited) *(continued)*

### 5. Lines of business

The bank reports and manages its operations according to the lines of business definitions used by the HSBC Group. The bank has, therefore, combined "Wholesale Banking" and "Treasury and Markets" into one line of business, "Corporate, Investment Banking and Markets". For 2003, the results of this combined line of business will be tracked separately. The comparative information reflects this new structure. Also consistent with the HSBC Group's lines of business, "Commercial Financial Services" has been renamed "Commercial Banking".

Effective 1 January 2003, the bank implemented a funds transfer pricing system which shifts structural interest rate risk from the business units to the Treasury department. Refinements to the bank's funding and cost allocations have also been implemented. All of these enhancements have been applied to the comparative results of the lines of business.

	<i>Quarter ended</i>			<i>Half-year ended</i>	
	<i>30 June</i>	<i>31 March</i>	<i>30 June</i>	<i>30 June</i>	<i>30 June</i>
	<i>2003</i>	<i>2003</i>	<i>2002</i>	<i>2003</i>	<i>2002</i>
<b>Personal Financial Services</b>					
Net interest income	<b>82</b>	83	82	<b>165</b>	158
Provision for credit losses	<b>(1)</b>	(5)	(5)	<b>(6)</b>	(11)
Other income	<b>56</b>	55	47	<b>111</b>	101
Non-interest expenses	<b>(103)</b>	(93)	(99)	<b>(196)</b>	(184)
Income before taxes and non-controlling					
interest in income of trust	<b>34</b>	40	25	<b>74</b>	64
Provision for income taxes	<b>(13)</b>	(15)	(9)	<b>(28)</b>	(23)
Non-controlling interest in					
income of trust	<b>(1)</b>	(2)	(1)	<b>(3)</b>	(2)
Net income	<b>20</b>	23	15	<b>43</b>	39
Average assets	<b>13,245</b>	13,041	11,437	<b>13,144</b>	11,188
<b>Commercial Banking</b>					
Net interest income	<b>102</b>	99	102	<b>201</b>	205
Provision for credit losses	<b>(17)</b>	(13)	(16)	<b>(30)</b>	(34)
Other income	<b>32</b>	31	33	<b>63</b>	63
Non-interest expenses	<b>(62)</b>	(62)	(54)	<b>(124)</b>	(107)
Income before taxes and non-controlling					
interest in income of trust	<b>55</b>	55	65	<b>110</b>	127
Provision for income taxes	<b>(21)</b>	(21)	(24)	<b>(42)</b>	(46)
Non-controlling interest in					
income of trust	<b>(2)</b>	(2)	(2)	<b>(4)</b>	(4)
Net income	<b>32</b>	32	39	<b>64</b>	77
Average assets	<b>12,692</b>	12,657	13,253	<b>12,675</b>	13,026

## Notes to Consolidated Financial Statements (Unaudited) *(continued)*

### 5. Lines of business *(continued)*

	<i>Quarter ended</i>			<i>Half-year ended</i>	
	<i>30 June</i>	<i>31 March</i>	<i>30 June</i>	<i>30 June</i>	<i>30 June</i>
	<i>2003</i>	<i>2003</i>	<i>2002</i>	<i>2003</i>	<i>2002</i>
<b>Corporate, Investment Banking and Markets</b>					
Net interest income	<b>38</b>	36	29	<b>74</b>	61
Provision for credit losses	<b>(1)</b>	(2)	(22)	<b>(3)</b>	(23)
Other income	<b>23</b>	19	23	<b>42</b>	49
Non-interest expenses	<b>(12)</b>	(10)	(40)	<b>(22)</b>	(59)
Income/(loss) before taxes and non-controlling interest in income of trust	<b>48</b>	43	(10)	<b>91</b>	28
Provision for income taxes	<b>(18)</b>	(17)	4	<b>(35)</b>	(10)
Non-controlling interest in income of trust	<b>(1)</b>	-	(1)	<b>(1)</b>	(2)
Net income	<b>29</b>	26	(7)	<b>55</b>	16
Average assets	<b>10,338</b>	9,889	9,908	<b>10,114</b>	9,958
<b>Other</b>					
Non-interest expenses	<b>(13)</b>	(14)	(12)	<b>(27)</b>	(24)
Income before income taxes	<b>(13)</b>	(14)	(12)	<b>(27)</b>	(24)
Provision for income taxes	<b>5</b>	6	6	<b>11</b>	9
Net income	<b>(8)</b>	(8)	(6)	<b>(16)</b>	(15)

The impact of the transfer pricing implementation on each business line's results for the comparative periods was as follows:

	<i>Quarter ended</i>	<i>Half-year ended</i>
	<i>30 June</i>	<i>30 June</i>
	<i>2002</i>	<i>2002</i>
Increase/(decrease)		
<b>Personal Financial Services</b>		
Net interest income	(26)	(47)
Net income	(17)	(30)
<b>Commercial Banking</b>		
Net interest income	14	21
Net income	8	13
<b>Corporate, Investment Banking and Markets</b>		
Net interest income	12	26
Net income	9	17

## Notes to Consolidated Financial Statements (Unaudited) *(continued)*

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### 6. Guarantees

Effective 1 January 2003, the bank adopted the new CICA Handbook Accounting Guideline AcG-14 “Disclosure of guarantees”. The guideline clarifies disclosure requirements of certain guarantees.

The Bank issues guarantees and standby letters of credit to meet credit requirements of certain customers. The contract amounts are not included in the consolidated balance sheets and are as follows:

	<u>At 30 June 2003</u>	<u>At 31 December 2002</u>	<u>At 30 June 2002</u>
Guarantees and financial standby letters of credit	920	916	984
Performance standby letters of credit	316	328	392
Total guarantees and standby letters of credit	<u>1,236</u>	<u>1,244</u>	<u>1,376</u>

Guarantees and financial standby letters of credit represent the bank’s obligation to make payments to third parties on behalf of certain customers if these customers are unable to make required payments. Performance standby letters of credit represent the bank’s obligation to make payments to third parties on behalf of certain customers if these customers are unable to meet certain contractual requirements.

The contractual amount represents the maximum undiscounted potential amount the bank could be required to make under the guarantee before any amounts that could possibly be recovered under recourse or collateralization provisions. A large majority of these commitments expire without being drawn upon. In the event of a call on the above commitments, the bank has recourse against those customers who have requested the credit facilities.

The bank is also subject to limited recourse for potential credit losses and potential shortfall of yield on certain of the securitized assets. At 30 June 2003, total recourse against the bank under securitization transactions was C\$15 million (31 December 2002 - C\$14 million, 30 June 2002 – C\$21 million).

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Toronto Stock Exchange

HSBC Bank Canada  
Class 1 Preferred Shares Series A  
(HSB.PR.A-TSX)

HSBC Canada Asset Trust  
Securities – Series 2010 (HSBC HaTS™)  
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