S&P Global
Market Intelligence

HSBC Holdings plc LSE:HSBA

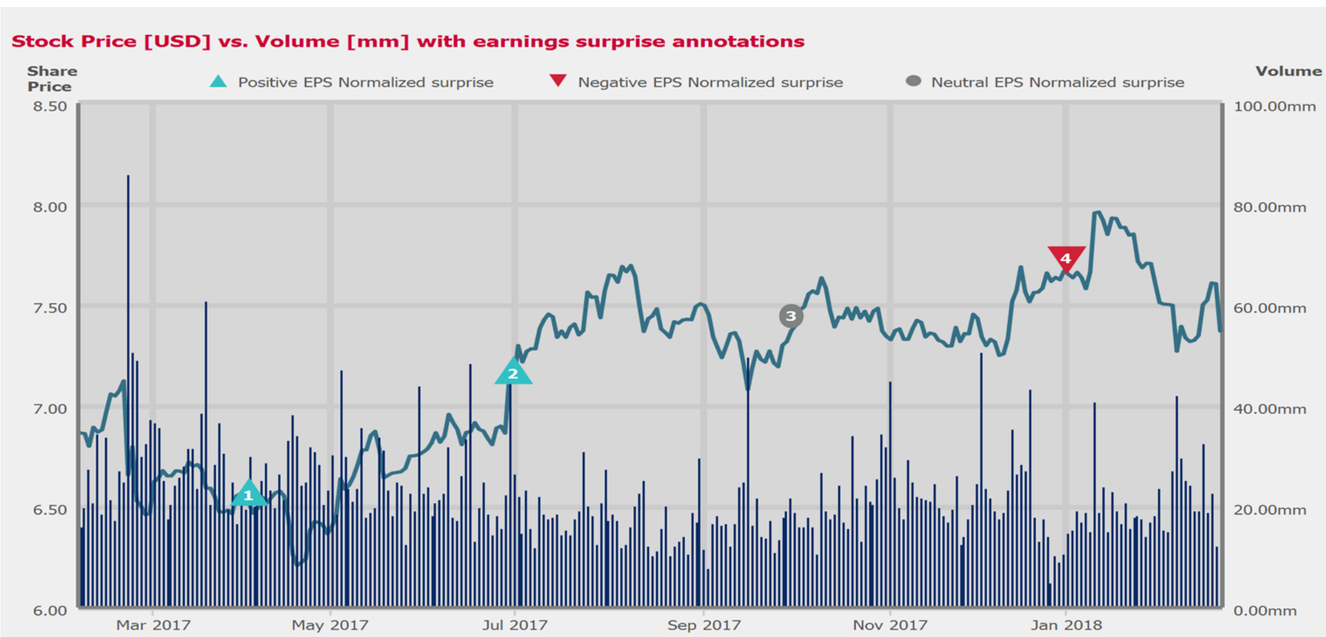
FY 2017 Earnings Call Transcripts

Tuesday, February 20, 2018 7:30 AM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2017-			-FQ1 2018-		-FY 2017-			-FY 2018-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	SURPRISE	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS
EPS Normalized	0.13	0.10	▼(23.08 %)	0.21	▼(4.76 %)	0.70	0.70	●0.00	0.69
Revenue (mm)	12785.48	12440.00	▼(2.70 %)	13902.86	▼(0.55 %)	51404.13	51524.00	▲0.23	54250.86

Currency: USD
Consensus as of Feb-20-2018 7:20 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FY 2017	0.70	0.70	0.00 %

Table of Contents

Call Participants

EXECUTIVES

Iain James Mackay
Former Group Finance Director & Executive Director

John Michael Flint
Group Chief Executive, Member of Management Board & Executive Director

Stuart Thomson Gulliver
Former Group Chief Executive, Chairman of Management Board & Executive Director

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Presentation

Stuart Thomson Gulliver
Former Group Chief Executive, Chairman of Management Board & Executive Director

So good afternoon from Hong Kong. Good morning in London, and welcome to the 2017 HSBC Annual Results Call.

With me today, Iain Mackay; and John Flint, who takes over tomorrow as Group Chief Executive. I'll look at the main points before Iain takes a detailed look at the numbers. I'll then talk about our performance against our strategic actions before handing over to John to talk about 2018.

Now 2017 was a good year for HSBC. Reported profit before tax of $17.2 billion was $10.1 billion higher than 2016 due mainly to the nonrecurrence of a number of large significant items. Adjusted profit before tax of $21 billion was up $2.1 billion or 11%, with increases in all 4 global businesses and 4 out of the 5 regions. A strong revenue performance helped us achieve positive adjusted jaws of 1% in 2017, more than covering increased business investment and higher performance-related costs.

Retail Banking and Wealth Management had an excellent year. Strong deposit growth started to benefit the bottom line as interest rates began to rise. We continued to grow lending in our target markets, especially Hong Kong and the U.K.

Commercial Banking adjusted revenue grew well on the back of an outstanding performance in Global Liquidity and Cash Management. Global Trade and Receivables Finance revenues stabilized after a difficult 2016. And we increased our market share in key geographies.

Global Banking and Markets grew adjusted revenue for the year due mainly to the strength of our transaction banking businesses. Growth in the first 3 quarters of the year in markets and banking enabled both to withstand the effects of subdued market activity in the fourth quarter.

Global Private Banking adjusted revenue continued to reflect the impact of historical repositioning but was broadly stable over the course of 2017 and grew by 10% in our target markets.

Adjusted loan impairment charges were significantly lower than 2016 due mainly to improved conditions in the oil and gas industry in North America.

Our strong equity Tier 1 ratio of 14.5% included the effect of recent changes in U.S. tax legislation, which reduced our capital position by 9 basis points. There was also a net of buybacks throughout the year which totaled USD 3 billion in 2017. Our policy is to consider buybacks where appropriate, subject to the execution of targeted capital actions and regulatory approval. And we plan to issue between $5 billion and $7 billion of additional Tier 1 capital in the first half of 2018. Now the program of strategic actions announced at our investor update in June 2015 concluded at the end of 2017. We completed 8 out of 10 actions on time and on or above target. We also completed the exit of household due to the run-off of our CML portfolio.

Iain will now talk you through the numbers.

Iain James Mackay
Former Group Finance Director & Executive Director

Thanks, Stuart.

Looking quickly at some key metrics for 2017. The reported return on average ordinary shareholders' equity was 5.9%, up from 0.8% in 2016. The reported return on average tangible equity was 6.8%, up from 2.6%. On an adjusted basis, we had a positive jaws of 1%; and with a tangible net asset value per ordinary share of $7.26, up $0.34 on 2016.

Slide 3 provides detailed items that take us from reported to adjusted for both the fourth quarter and the full year. You'll find more details of these adjustments in the appendix, and the remainder of the presentation focuses on adjusted numbers.

Slide 4 breaks down adjusted profit for 2017 by global business and geography. Adjusted profit before tax was up by $2.1 billion or 11% due to higher revenue and lower loan impairment charges. All 4 global businesses grew profit before tax. Retail Banking and Wealth Management had a particularly good year with a 24% increase on 2016. Commercial Banking also registered a strong performance with profit before tax growth of 15%.

Slide 5 looks at fourth quarter profit before tax, which was $807 million higher than the fourth quarter of 2016. This was driven by a 10% increase in revenue, and 4 out of 5 regions delivered higher profits in the quarter. The reduction in Europe was driven by a weaker Global Banking and Markets performance, which included lower revenues in FICC and 2 large impairment charges.

Slide 6 looks at revenue. Fourth quarter revenue from our global businesses was $400 million or 3% higher than last year's fourth quarter. I'll go through each business in more detail in the next few slides.

As Slide 7 shows, Retail Banking and Wealth Management revenue grew by 8% in the fourth quarter compared with the same period last year. Wider spreads and higher balances in Hong Kong helped grow revenue from current account, savings and deposits by $370 million. Income from investment distribution increased by $98 million from higher sales, particularly in Hong Kong. We grew customer lending and customer deposits by 7% and 5%, most notably in Hong Kong and the United Kingdom. Lending revenue was $117 million lower due to margin compression. For the full year, revenue was up by 9%, with strong performances across the business.

Commercial Banking revenue was 11% higher than last year's fourth quarter. Global Liquidity and Cash Management had another excellent quarter, growing revenue by 16% due to higher spreads and balance sheet growth in Asia. Credits and lending grew by 5% due mainly to balance sheet growth in Hong Kong and the U.K. Global Trade and Receivables Finance revenue was broadly stable, as strong asset growth in Asia compensated for the impact of repositioning activity in the Middle East. Full year revenue was 5% up on 2016, mainly driven by Global Liquidity and Cash Management in Hong Kong.

In Global Banking and Markets, the diversity of our product range helped us withstand the impact of subdued trading conditions in the fourth quarter. Revenue was down against a strong fourth quarter performance in 2016. Also, our transaction banking products continued to generate increased revenue from higher balances. In particular, Global Liquidity and Cash Management revenue grew by 18%, and Securities Services grew by 15%. Lower trading volumes and reduced volatility affected FICC revenues, especially in rates. Global Banking and Markets' fourth quarter return on risk-weighted assets was 20 basis points higher than the same period last year, and the business delivered a return on tangible equity of 10.6% in 2017. Revenue for the full year was up 3% on 2016, mainly in Global Liquidity and Cash Management and Securities Services. All of our Global Banking and Markets businesses grew revenue in 2017.

Global Private Banking revenue grew by 2% compared with last year's fourth quarter. We grew client assets in Global Private Banking for the fifth consecutive quarter and saw positive inflows of $15 billion in our target markets in 2017. Revenue grew by 8% in our target markets in the fourth quarter, particularly Hong Kong, and by 10% over the full year.

Corporate Centre revenue grew by $695 million compared with the fourth quarter of 2016. This was principally due to nonrecurrence of a net negative $684 million income reduction in valuation differences and long-term debt and associated swaps in 4Q '16. Balance Sheet Management revenue fell by $167 million. This was due to nonrecurrence of a gain in last year's fourth quarter and repositioning activities carried out earlier in 2017. We have now completed the run-off of our subprime U.S. CML portfolio, the principal legacy of the 2003 household acquisition. As a consequence, associated revenue is $129 million lower than last year's fourth quarter. We will complete the wind-up of the household legal entities in the coming quarters.

Slide 12 shows net interest margin, which was broadly stable. Net interest income of $7.4 billion was $260 million higher than the third quarter. Our net interest margin for 2017 was 1.63%, 7 basis points lower than 2016, excluding Brazil. Net interest margin fell by 3 basis points from the impact of the CML run-off and margin compression in Europe and Asia, 3 basis points from higher costs of debt and 3 basis points from foreign currency translation. This was partly balanced by a 4 basis point increase from higher deposit margins, particularly in Asia and in Global Liquidity and Cash Management. There's a detailed slide on net interest margin and more information on net interest income sensitivity analysis in the appendix.

Slide 13 looks at loan impairment charges. Loan impairment charges were $658 million in the fourth quarter or 27 basis points as an annualized percentage of gross loans and advances. This was $218 million higher than the third quarter due largely to 2 corporate exposures.

Slide 14 looks at costs. Our operating expenses excluding the bank levy were $296 million higher than last year's fourth quarter, reflecting additional investment to grow the business and ongoing investment in digital and IT security. We achieved around $600 million of cost savings in the fourth quarter, which helped support growth and absorb the cost of inflation and investments in regulatory and compliance programs. We invested a further $322 million in business growth in the fourth quarter, mainly in Retail Banking and Wealth Management. Our total expenditure on regulatory programs and compliance was $3 billion, around $200 million more than the prior year. We expect regulatory and compliance spending to remain broadly stable.

Turning to capital on Slide 15. The group's common equity Tier 1 ratio was 14.5% on 31st September compared with 14.6% on 30th of September. Common equity Tier 1 capital reduced by $3.7 billion in the fourth quarter due mainly to the fourth quarter dividend and a reduction in the value of our deferred assets as a result of changes in U.S. tax legislation. Implementation of IFRS 9, including benefits from classification and measurement changes, will result in a favorable impact on our common equity Tier 1 ratio applying the European Union's capital transitional arrangements. The fully loaded day 1 impact is expected to be negligible.

Slide 16 looks at our group return metrics. The return on average ordinary shareholders' equity was 5.9%, up from 0.8% in 2016. And the return on tangible shareholders' equity was 6.8%, up from 2.6%. Our return on tangible equity excluding significant items and the bank levy was 9.3%. If we also exclude the impact of U.S. tax legislation, our return on tangible equity was 10.2%. We're now disclosing our return on tangible equity by global business. The numbers for 2016 and 2017 are on the slide, and there are more details in the appendix. All 4 global businesses improved the return on tangible equity in 2017, with double-digit returns in our 3 main businesses.

I'll now hand back to Stuart.

Stuart Thomson Gulliver
Former Group Chief Executive, Chairman of Management Board & Executive Director

So for the remaining slides, I'm going to summarize the outcome of our 2.5-year strategic action program which concluded at the end of 2017. And then I'm going to hand over to John to talk about the year ahead.

Slide 18 provides the final report card in relation to our 2015 targets. By the end of 2017, we had achieved 8 of the 10 actions we set out at our 2015 investor update. This included actions to reduce group risk-weighted assets, deliver cost savings, accelerate our pivot to Asia and implement Global Standards. Our U.S. bank profitability and RMB internationalization revenue targets remain outstanding, although we have made significant progress towards completing both.

Slide 19 shows how we've increased both capital efficiency and capital strength. We exceeded our group risk-weighted asset reduction target by more than 20% and our Global Banking and Markets target by 31%. We've increased returns at the same time, growing our return on risk-weighted assets from 1.5% in 2014 to 2% in 2017. The reduction in risk-weighted assets has helped us build one of the strongest common equity Tier 1 ratios in the industry while maintaining a strong dividend and returning $5.5 billion to investors in the form of share buyback.

Slide 20 looks at NAFTA profitability. While the low interest rate environment has held back the U.S. business, we've more or less doubled its adjusted profit before tax since 2014. We also achieved nonobjection to our U.S. capital plans as part of the CCAR process in both of the last 2 years. And in 2017, the U.S. business paid the first dividend to the group in more than a decade. A large part of our international business emanates from U.S. customers, so it's of huge importance to the group even if that's not reflected in the U.S. legal entity's numbers. We increased the international client revenue actually booked in the U.S. by 10% in 2017.

Our Mexico business is significantly improved, delivering higher revenue, higher lending, higher market share and higher profit. It has grown market share in both mortgages and personal loans and achieved double-digit revenue growth in international subsidiary banking and with multinationals. 2000 profit before tax -- 2017, sorry, profit before tax of $440 million represents real progress, with revenue up 34% and lending up 38% since 2014. The growth opportunity for our Mexico business remains significant.

Slide 21 shows that we have delivered on our commitment to an -- achieve an exit run rate for 2017 equivalent to our 2014 cost base. We've delivered run rate savings of $6.1 billion since 2015, more than $1 billion above the top end of our Investor Day target range. This has enabled us to absorb the $2.5 billion that we've invested in growth and business improvements, the $2.4 billion of inflation and the $1.3 billion of investments in regulatory programs and compliance over the same period. We've invested a total of $7 billion in costs to achieve between 2014 and 2017. As well as removing costs from the business, this has vastly improved both our systems and the service we offer our customers. It has positioned the business to capture market share and grow revenue whilst also improving life for our employees. You can find examples of how these programs have made us a better bank on Slide 35 in the appendix.

Slide 22 shows how our improved international connectivity helped strengthened our market positions. This is proof of the benefits of our global universal banking business model, which is tailored around the needs of large corporates that operate across our network. We've invested in our network to better deliver the kind of cross-border service that our clients want, while many of our competitors have exited the market at the same time. We've also simplified the business to improve control while retaining the benefits of scale. As a consequence, we've increased the proportion of client revenue that comes from international clients from 50% in 2015 to 53% in 2017. We've also grown our market share in key trade finance markets, increased balances and captured market share in Global Liquidity and Cash Management and maintained our leadership at the corporate foreign exchange market. We've also increased transaction banking revenue by 5% since 2015, whilst 30% of group revenue now comes directly from transaction banking, up from 29% 2 years ago.

Slide 23 shows how we've refocused the business back towards the bank's heartland in Asia. We've grown our lending and insurance income in Hong Kong since 2014. We've rapidly grown lending in the Pearl River Delta; launched new products; and established new businesses, including the first security joint venture in Mainland China to being majority owned by an international bank. We've grown assets under management in Asia by 49% and increased annualized new business insurance premiums in Asia by 32% since 2014. And we've strengthened our position as the world's #1 bank for international renminbi business and established HSBC as the best overall international bank for the Belt and Road initiative, according to both Asiamoney and FinanceAsia.

To conclude. HSBC is simpler, stronger and more secure as a consequence of our strategic actions. We have strong revenue growth and a robust capital ratio. Our international network is better at connecting customers to opportunities in the world's fastest-growing regions. Our investments in Global Standards in risk and compliance helped pave the way for our exit since 2012's deferred prosecution agreement with the U.S. Department of Justice, although financial crime prevention and strong compliance remain a daily focus for us. Our business is now more capital efficient and capable of producing stronger returns for investors.

With that, I will hand over to John.

John Michael Flint
Group Chief Executive, Member of Management Board & Executive Director

Thank you, Stuart.

So these results and the achievements over the last couple of years clearly give us a great platform to build on. With that in mind, there are 5 things to take away about the year ahead. First, we're doing a lot of work to refresh our strategy and accelerate delivery. The strategy we have is working. We need to keep evolving it and to deliver it at pace. We haven't yet achieved our return on equity target, but we remain intent on doing so. That target therefore remains in place, as do our other targets. Second, in an environment where we're generating more revenue, we're going to be better able to invest in growing the business, subject to achieving positive jaws.

Third, we're going to focus keenly on improving customer satisfaction in every business across the group. We've been investing to speed up approval times, simplify processes and significantly reduce bureaucracy, but as our environmental, social and governance reports from last year show, we've got more to do to raise customer satisfaction levels. We'll be disclosing more on customer satisfaction in our 2018 ESG report in April, and we aim to improve in all areas.

Fourth, capital discipline and positive jaws remain essential to achieving our return on equity targets. We're going to run the business more efficiently, absorbing inflation and as much of the cost of investment as we reasonably can. We're also going to keep investing in risk and compliance. We have a clear aim to be the industry leader for risk and compliance and believe this can be a powerful competitive advantage. And finally, the fundamentals of HSBC will remain the same as they always have: strong funding and liquidity, strong capital and a conservative approach to credit.

I will update you further either at or before our half year results in August.

Stuart Thomson Gulliver
Former Group Chief Executive, Chairman of Management Board & Executive Director

Thanks very much.
So we're very happy to take questions. The operator will now explain the procedure and introduce the first question. Operator?

Question and Answer

Operator

[Operator Instructions] We will now take our first question today from Mr. Joseph Dickerson from Jefferies, please.

Joseph Dickerson
Jefferies LLC, Research Division

Just a couple of questions. So firstly, we've obviously had a few rate hikes. And the NIM was flat quarter-on-quarter in Q4, but if I look at the trend in NII, it's actually annualizing in Q4 up about 15% year-on-year. So I'm just wondering, like, what should we see as the trajectory of the NIM now that we've had the drag from the CML eliminated. And it seems like there's some reasonable momentum, particularly in Hong Kong, on the NIM, so any color there about how to think about this over the next year would be very helpful, obviously market impacts notwithstanding. And then secondly, just on the U.S., how many costs are associated with the legacy household entities that you plan to wind up? And then secondly, can you remind us how many costs were associated with the DPA? I know the monitor is probably still in place, but what are the net costs from those 2 aspects that will come out of the U.S. business? That would be very helpful.

Iain James Mackay
Former Group Finance Director & Executive Director

Okay, net interest margin. I think, as the slide title suggests, we certainly feel, based on what we've seen since 2017, that we're reasonably well to benefit as rates move higher. The key drivers for 2017 are set out in the slide quite clearly. We have, as you point out, Joe, the sort of residue of the dilutive impact of running-down the CML portfolio, which completed in the fourth quarter. That accounted for about 3 bps of adverse movement to NIM. Slightly higher costs of MREL, TLAC by another name, and that reflects the higher issuance during 2017. And that program continues in 2018 to ensure we meet the regulatory guidance over the medium term. And then a little bit of impact from currency translation. That's the less-favorable news. The more favorable news is that -- is in that last point, where we saw higher spreads coming through liabilities, our deposit base and surplus liquidity principally over the course of the year. And that was most notable within the U.S. and then to a slightly lesser extent within Hong Kong as well. In addition, one of the things that we experienced in 2017 were tighter margins on the liability side and the U.K. balance sheet on the move down in the bank rates in the middle of 2016. Seeing that adjusted upwards again in the fourth quarter of 2017, again we'd expect to see some benefit of that coming through in 2018. So I think, in terms of our balance sheet disposition; and we look at some of the pricing dynamics on the asset side of the balance sheet and the positioning on the liability side, we'd certainly expect to see some benefit flow through from higher rates. So if the Fed follows through on a market expectation of higher rates in 2018, we should certainly expect to see the benefits of that come through. The headwinds in that regard, some have been eliminated, as you point out. We will continue to issue MREL into the marketplace, which will slightly increase the overall net interest expense that we incur in that space, but overall we think we've got reasonably positive trajectory. We provided more guidance on this, in net interest margin, in the investor deck and in the appendix to the investor deck as well as on Page 110 and 111 of the annual report and accounts, so more detail there, hopefully, for you to help on sensitivity analysis, Joe.

Joseph Dickerson
Jefferies LLC, Research Division

Not there yet in on Page 110, so sorry...

Iain James Mackay
Former Group Finance Director & Executive Director

You'd be a fast reader if you are, Joe, better man than me. On household, the wind-down really is the number of entities. Now this is an organization that operates in a state-by-state basis across the U.S. both in terms of subprime lending as well as some of its insurance businesses. So there are quite a few entities to be wound down, but I think in the round, the cost of winding down some 50 entities is literally in the rounding from an HSBC perspective. As it relates to the DPA, you'll recall that the penalty that was assessed in us in 2012 was $1.9 billion. The annual cost of the monitorship which started in the middle of 2013 and will conclude in the middle of this year has run in the range of $120 million to $140 million per annum in the round. So we will continue to see some expense coming through in 2018 in that regard.

Operator

Our next question today comes from Alastair Ryan from Bank of America.

Alastair William Ryan
BofA Merrill Lynch, Research Division

I feel a little bad asking this question, but the buyback guidance is some of the least useful that we've had in quite some time. So you're coming off a streak of significant buybacks. I appreciate there's this technicality around the AT1 issuance in the very short term, but it's tempting to read a significant shift into this with the new management and...

Stuart Thomson Gulliver
Former Group Chief Executive, Chairman of Management Board & Executive Director

[indiscernible]. No. So no, that's not what you should read it. So literally, and John will just interject here in a moment, this is about the fact that there are technical rules around having AT1s in the market and not being able to buy back shares at the same time. So there's nothing cute about it at all. There's no change in the policy. It absolutely isn't the case that John Flint and Mark Tucker are abandoning what we've had in place for the last 2 or 3 years. And once that technicality has passed, once the market has replaced the $7-odd billion of AT1s that we want to do, then you'd expect to see some form of buyback come along at that point in time. So do not over-interpret into it. And I'll just ask John to sort of join in since he's sitting next to me here.

John Michael Flint
Group Chief Executive, Member of Management Board & Executive Director

Sure, Stuart. Thanks. And Alastair, Stuart is exactly right. You shouldn't read any change in attitude towards our approach to capital management and the role of buybacks within that, but there is a technical reason why we want to get these -- well, we're going to get the AT1s done, and therefore there's a technical reason why we can't announce a buyback at this point.

Alastair William Ryan
BofA Merrill Lynch, Research Division

Clear. Could I just follow up? And this might be a bit thick for me, but you wrote 180 basis points of AT1 out there. $7 billion is a lot to do. It would take you well above the current sort of allowable amount. And your CET1 is already so high that you've effectively filled your Tier 1 requirements with common equity, so it feels like there's an awful lot of capital kicking around in the business. Is -- do we get any back -- how do we scale that, that you're going to end up with very high capital ratios with all this new issuance? And you've already about $13 billion of surplus CET1, so is AT1 substituting to CET1 down the road? Or are you just getting stuff done now ahead of 2023 or whatever it is?

Iain James Mackay
Former Group Finance Director & Executive Director

Part of it is just getting to those regulatory guidance in the medium to longer term, Alastair. And part of it is just normal financing and refinancing activities within the liability stack of the firm as a whole. And you obviously will recall we did a buyback in the second half of last year, and that precluded some [additions] activity which we may otherwise have wanted to do. So that sort of goes to the timing around this, but it is really just in the general round of financing and refinancing activity as well as with an eye to longer-term requirements around AT1.

Operator

Our next question today comes from Robert Noble from Royal Bank of Canada.

Robert Noble
RBC Capital Markets, LLC, Research Division

Just on the extension of the DPA, is there any risk that this affects your ability to withdraw capital from the U.S.? Or is that not an issue? And just in the commercial bank, the loan balance was flat. I was just wondering if there's anything, any specific reason, [well, that's sort of] relating to balances. But even without that it's flat. And you pulled out a comment that said there was spread compression in Asia and the corporate, but -- and I was wondering. Has that improved on the asset side, the spread compression in Asia?

Iain James Mackay
Former Group Finance Director & Executive Director

So last question, first. It's been fairly consistent both within mortgages and Hong Kong as well as corporate credit and lending in Asia over the course of 2017. There is a lot of liquidity [doing the rounds] not only in this part of the world but globally, and the pressure has been consistent. We haven't seen it intensify or slacken in that regard over the course of 2017. I think those competitive pressures remain fairly consistent going into 2018, based on evidence so far. On your first point, to be clear: The deferred prosecution agreement that we entered into in 2012, with respect to AML, the charges in that regard were dropped in December of 2017. And that DPA has now come to an end on the back of a significant investment and work that was done in terms of improving the overall firm's ability with respect to financial crime risk management. The -- as we discussed in previous quarters, our ability to extricate surplus capital from the U.S. was very much informed by CCAR and having nonobjections to the results for stress tests and capital plans associated with those stress tests in previous years. And I think, as Stuart mentioned earlier on, we did get our first dividends from the U.S. in 2017 since -- I think it was 2006 or 2007 was the last time that a dividend had been paid. So it is the first time there was a dividend in 10 years. And we were successful in pulling a quite significant amount of surplus capital from the U.S., in line with those capital plans to which the Federal Reserve raised no objection in 2017. So I think that covers that. With the third point...

Stuart Thomson Gulliver
Former Group Chief Executive, Chairman of Management Board & Executive Director

Yes. It was loan and advances growth in Commercial Banking. Actually, it's up 7%. It was up USD 22 billion net.

Iain James Mackay
Former Group Finance Director & Executive Director

Yes. So in the round. And that's largely informed by growth in the United Kingdom. And we saw some growth in Asia as well, but that was largely informed by a reasonably robust environment in the United Kingdom for Commercial Banking outstanding credit and lending perspective.

Operator

Our next question today comes from Raul Sinha from JPMorgan.

Raul Sinha
JP Morgan Chase & Co, Research Division

Can I have two, please? Just the first one is on staying on loan growth. I mean, if I look at the underlying loan growth in Q4 across the group, year-on-year I think you grew at 7%, which is, let's say, at the top end of your mid-single-digit indication for '18, if I'm generous. And within that, obviously you've got 12%

growth in mortgage balances in Hong Kong, 7% growth in the U.K. Well, how should we think about the composition of growth? Do you think that any of these individual areas that is growing is going to see material pickup or slowdown in 2018 relative to where you are today? Or is it just a continuation of the trends that we've seen so far? So just interested in how you square the [federal] and the mid-single-digit sort of guidance. And the second one is [indiscernible], if you want that as well, is just on thoughts on U.K. asset quality. And I was wondering if you have any thoughts on some of the pressures that we are seeing, especially in the business services sector and construction. Do you think that, at this point, it is sort of isolated incidents? Or do you think that there might actually be more pressures building up from an asset quality perspective in the U.K.?

Iain James Mackay
Former Group Finance Director & Executive Director

So on U.K. asset quality specifically, excepting the 2 large exposures for which we made provision in the fourth quarter, we see a very stable credit environment. And there one see slightly benign, more so than perhaps one would expect. And that has been consistent, again with the 2 notable exceptions, across global banking and markets, Commercial Banking and retail bank Wealth Management. I think overall we've seen a very stable picture across the business in the Americas. We've seen a slight uptick in retail bank Wealth Management in Mexico, but that was expected on the back of the nature of business that we're growing there, particularly within retail banking Wealth Management, with a slightly higher proportion of unsecured personal credit in that particular marketplace. In Asia, very, very stable; and a slight pickup in the Commercial Banking space in Hong Kong; but again not characterized by anything in particular that would be worth bringing out. So I think overall, other than the notable items that we mentioned in the fourth quarter, it's a pretty stable picture. I think it would be entirely accurate to say that, learning from that experience in the fourth quarter, we are, as our credit teams always do, taking a good look at secondary-order impacts that may emanate from particularly one of those names, but at this point in time a reasonably stable picture. Going back to credit and lending growth: I think one of the things which does not necessarily show up by an examination of the fourth quarter balance sheet was how strong credit and lending in Global Banking and Markets and particularly in Asia had been last year. In the fourth quarter, we saw a number of areas of paydown of credits in that Global Banking and Markets scenario, but the pipeline in Asia remains very strong in the Global Banking and Markets space and remains encouraging in Commercial Banking across the piece. And in retail bank Wealth Management, and John can certainly go into more detail on this, we continue to see an opportunity to grow market share in the U.K. mortgage space. We continue to hold a very prudent position with respect to underwriting. LTVs for the portfolio overall are just around about 40%. New issuance tends to -- new underwriting tends to be done at about 60% LTV. And overall experience in that book has been very, very stable. And as we continue to expand the broker channel, I think we now have 23 brokers that give us line of sight to the marketplace, we are seeing more of the market obviously and are quite keen to continue to grow share in that space. Overall stock in the market is still slightly below 7% market share.

John Michael Flint
Group Chief Executive, Member of Management Board & Executive Director

Yes. Iain, thanks. So just maybe just to supplement that. So on the RBWM side, mortgages in the U.K., you should expect us to continue to compete aggressively there and to continue to take market share as we leverage back into the intermediary space, an area that we've been absent from for a while. We retain all of our underwriting -- or we retain control of underwriting, and we're not compromising our credit risk standards or our credit risk appetite. We're just getting more distribution through this new channel. And as we approach the advent of the ring-fenced bank, if anything, the opportunity increases because the surplus funding of the ring-fenced bank is now looking for a home which has looked to be a reasonable place for it. I mean in Hong Kong the market remains extremely competitive, but we will defend our market share there. And our third biggest retail business, Mexico, there is still room for us to grow into our footprint. So across the retail space you should expect to see continued asset growth.

Raul Sinha
JP Morgan Chase & Co, Research Division

I mean that sounds very constructive, but I guess what I'm struggling to square with is your current pace of growth looks like it's running at 7% and yet you're talking about mid-single digit, let's say, an aspiration for 2018. Is that just conservatism baked into that sort of forecast? Or is there something that I'm missing where you might actually be more cautious on?

John Michael Flint
Group Chief Executive, Member of Management Board & Executive Director

7% sounds about mid-single digit to me. Doesn't it [square off, no]?

Operator

Our next question today comes from Chris Manners from Barclays.

Christopher Robert Manners
Barclays Bank PLC, Research Division

It's Chris Manners from Barclays here. Just 2 questions, if I may. The first one was on target capital levels. And when I look at your slide deck, it looks like your MDA at the 1st of Jan next year is going to be 11.6%. You're indicating you're at $25 billion surplus to that. I know, in the past, you've been sort of talking about a sort of 12% to 13% target range. And then you might run a little bit higher than that and for a while. Just maybe a few thoughts on how much capital do you think you need to run with longer term and how that flows back into the buyback. And the second one is I had a couple of questions on the ring-fenced bank. When I look at the ring-fenced bank's sort of illustrative balance sheet, you do look like you have a lot of liquidity there. So 25% of the balance sheet is liquid assets. And also just -- yes. So how can you sort of shift that out of the ring-fenced bank? Or how can you make that more productive? And how much capital do you think that ring-fenced bank is going to need? And so it's got around GBP 82 billion of RWAs. Is it going to just run at the group's CET1 ratio? Or are you going to run that a little bit higher?

Iain James Mackay
Former Group Finance Director & Executive Director

Okay, on the last couple of points, Chris, the guidance on regulatory requirement for common equity Tier 1 in the ring-fenced bank is in the range of 12.5% to 13%, 13.5%. That go around the houses. I don't think you'll find a ring-fenced bank in the U.K. with different guidance in that regard. And as John pointed out, we do have a very strong liquidity position within the ring-fenced bank. And part of the challenge will be profitably deploying that liquidity, as the opportunity to move it further afield in the group is part of ring fencing; and namely to prevent us moving that liquidity further afield in the group, both liquidity and capital resources. So absolutely that will be part of the challenge to continue to look at how we optimize the ring-fenced bank balance sheet and put to good use the resources that we have in it, but it would be fair to say we have a very safe balance sheet going into the start of trading with that bank in the 1st of July this year. On the group's common equity Tier 1 ratio, I think, certainly over the course of the last 12 months, we've tried to encourage you to think about the top end of our 12% to 13% range from a common equity Tier 1 perspective. And certainly, if we reflect on the output of regulatory buffers on the back of stress tests, then the tendency has been to move the Pillar 2 requirements a little bit higher on the back of those stress tests. And I think that's broadly what we would expect to experience again as we work through 2018. So I think we are nudging the common equity Tier 1 requirements for the group probably somewhat above 13% at this stage. And how much above 13%, we'll get better indication when we get some guidance from our principal regulators around how they intend to interpret and apply the learnings from the stress tests of 2017. We'll, hopefully, get some guidance on that over the course -- the coming months, but I think it would be fair to say that we would expect to see that common equity Tier 1 ratio for the group nudge somewhat above 13% now.

Christopher Robert Manners
Barclays Bank PLC, Research Division

Okay, so maybe it [comes towards] sort of 14-ish for the moment. Is that fair?

Iain James Mackay

Former Group Finance Director & Executive Director

You keep trying to put words in my mouth, Chris. I don't think I said that. Did I...

Christopher Robert Manners
Barclays Bank PLC, Research Division

So it's above 13%. It seems to be the next tests, it's next place.

Iain James Mackay
Former Group Finance Director & Executive Director

You don't like anything between 13% and 14%? Never mind. Broadly speaking, I think what we said earlier, around the fact that we don't really see that impacting our overall policy with respect to capital management and the propensity for buybacks.

Operator

Our next question today comes from Magdalena Stoklosa from Morgan Stanley.

Magdalena Lucja Stoklosa
Morgan Stanley, Research Division

I've got 2 questions. One is about the investment growth, and another about kind of year-to-date trading. So the first one, when you look forward and kind of talk about the investments for growth in 2018 and '19, kind of could you give us more detail about the kind of extent and the nature of your key spend items; and maybe a little bit more color, more detail around your digitalization policy? So that's question one. And question two, I mean, how do you see the beginning of the year in trading activity? In particular, we have seen the resurge in volatility but still against kind of very strong underlying economic activity, so how have you started? And when you -- and how do you see particularly trading across 2018?

John Michael Flint
Group Chief Executive, Member of Management Board & Executive Director

Magdalena, It's John. I'll start with the first question, so our investment spend. What I won't do today is kind of talk about the -- anything that relates to the development of the strategy. So that's something that we'll work with the executive and the board on over the next few months and then update everybody at or before the half year results. But what we have been doing over the last couple of years is investing in new technology, bringing technology into the bank to make it easier for customers the bank with us and to automate processes either to reduce headcount or to make it easier for staff to get on and do their jobs. Last year, we spent around about $5.3 billion on technology. As a function, we've invested over $2.3 billion in digital across our 3 biggest businesses over the period 2015 to 2017. Some examples of what we've been spending our money on and where we've got a bit more work to do: We are the biggest financial services user of biometrics, so that's touch, voice recognition and face ID. 40% of our retail customer log-ins are now passed with us. We've got the largest deployment of mobile pay solutions of any retail bank in the world. In Hong Kong, where we're hosting this call from, we have a new peer-to-peer mobile application, PayMe, that allows customers to send money to their family and friends et cetera. So those are some investments that have been rolled out. We have similar work in train. All of that investment, of course, will be subject to the positive jaws constraint. If the revenue environment remains constructive, we should be able to continue to bring new technology and to make the bank better. We'll maintain the positive jaws discipline. And when we get to the strategy update, if there's any change in the priorities of what we're investing in, we'll let you know then.

Magdalena Lucja Stoklosa
Morgan Stanley, Research Division

But John, can I follow up very quickly? It looks like the investment over the last 2 years has been very much about kind of safety, security and the front end, i.e. the customer satisfaction you've talked about kind of earlier in the conversation. How about the back end? How about the kind of middle- and the back-office spend, which kind of tends to -- or kind of -- which tends to be following the -- I think, the front-office investments? Is that something that is also kind of happening in the background to the same degree?

John Michael Flint
Group Chief Executive, Member of Management Board & Executive Director

Yes, it is very much so. So the things that are visible to you and to our customers, the things you can see are part of it, but an awful lot of the investment has gone into the middle- and the back-end processes either to improve the technology platforms that support the business and/or to automate processes that are currently very manual. So there's an awful lot of that going on...

Iain James Mackay
Former Group Finance Director & Executive Director

And there is a very significant amount of investment in the area of meeting regulatory compliance requirements simply with respect to the amount of reporting that we now do for our regulators around the world, whether it's with respect to capital, risk-weighted assets, liquidity, overall exposure from a credit perspective. So improving the speed, reducing cycle times, enhancing data quality. And being able to provide multiple, different cuts of data, which of course has benefit as well to the business in terms of helping inform decision-making at product and segment levels, is an area where there's been considerable investment over the course of the last couple of years.

Stuart Thomson Gulliver
Former Group Chief Executive, Chairman of Management Board & Executive Director

There's quite a bit of detail on Slide 35 in the appendix which gives you a bit of a sort of touches to some -- where some of the middle- and back-office expenditure has been. And then you also asked how we're trading so far this year, which Iain will give you a completely inscrutable answer.

Iain James Mackay
Former Group Finance Director & Executive Director

With those instruction -- no. I think the first 6 weeks of the year have been fairly constructive. It's -- as you say, it's the volatility has contributed to higher volumes that we've seen come through. So I think overall, certainly when you reflect on the daily runs that are coming through Global Banking and Markets, it's a reasonably encouraging picture over the first 6 weeks of the year.

Operator

Your next question comes from Fahed Kunwar from Redburn.

Fahed Irshad Kunwar
Redburn (Europe) Limited, Research Division

I just had a couple of questions. The first is just following up on the margins. Obviously you've got good, higher yields on the surplus liquidity in the year, but Hibor since the beginning of the year has fallen quite sharply, it's off about 50 bps in the beginning of the year. I'm just wondering. That deposit margin and particularly in the Hong Kong exit deposits, is that the -- does that fall going forward? And how does that play into the margins guidance you gave earlier overall? And the second point was just around jaws, obviously very positive. And the investment spend will be kind of under the constraint of positive jaws, but at the moment, consensus close to 3% kind of positive jaws for the next 2 to 3 years. I think you talked about on the call last time jaws of more like 1% to 1.5%, from memory. Is that 3% reasonable? Or do you think that's just still a little bit elevated?

Iain James Mackay
Former Group Finance Director & Executive Director

Fahed, I think your memory is quite good actually. I like that guidance quite a lot. And then from a NIM perspective, there obviously is some variability in terms of how the deposit betas impact the overall flow-through to our income statement. And clearly we're responsive to market pressures in that regard in Hong

Kong just as everywhere else in the world, but broadly speaking, the guidance that we offered is conscious of some of the dynamics that we've seen over the last 4 or 5 weeks.

Stuart Thomson Gulliver
Former Group Chief Executive, Chairman of Management Board & Executive Director

And if I can, on Hibor. So Hibor was kind of trading 50s, averaging about 54 basis points in the first quarter '17, 40 basis points in the second, around 44 in the third, got up to about 84 in the fourth quarter, spiked to around 100 and is back at 80. So the 100 was the outlier, so no, that doesn't require us to change the guidance.

Fahed Irshad Kunwar
Redburn (Europe) Limited, Research Division

Okay. Okay, so the fourth quarter was the outlier. That's very helpful.

Stuart Thomson Gulliver
Former Group Chief Executive, Chairman of Management Board & Executive Director

Yes, it was.

Operator

The next question today comes from Tom Rayner from Exane.

Thomas Andrew John Rayner
Exane BNP Paribas, Research Division

Can I have the -- 2 questions and -- please? Just firstly, to go back to share buyback and the capital guidance. I mean I noticed that you have repeated what has been your dividend guidance for some time, that you're going to hold it flat for the foreseeable future. Obviously, though, that suggests a sort of continuing capital build. And one aspect I don't think you're asked about with regards the share buyback was the fact you haven't been able to finalize or tell us what the final Basel IV outcome is going to be. I just wondered. Is there any issue about the uncertainty around the potential Basel IV impact that may be making you a little bit more cautious on sort of committing to the share buyback? That's my first question. And I have a second one, on costs. I don't know if you want it now or after.

Iain James Mackay
Former Group Finance Director & Executive Director

Fire away, Tom.

Unknown Executive

[indiscernible].

Thomas Andrew John Rayner
Exane BNP Paribas, Research Division

Yes. I just wanted to try and get you to update. I know you're still targeting positive jaws, but just the sort of potential sort of size of those jaws. Because obviously, having taken out more than 6 billion per annum of costs already, I guess it gets increasingly difficult to find those new sort of gross cost savings. You're talking about, so -- or John, I think you were talking about wanting to invest more as revenue improves. So my sense is that, if we're talking positive jaws, we might be more 1% than 3%, but I'm just trying to get a feel for what you're -- you think the potential is there, please.

Iain James Mackay
Former Group Finance Director & Executive Director

Yes, Tom, I think 1% to 1.5%, 2% is pretty good guidance around the jaws number, per the previous questions. So I think your read of it is pretty much spot on in that regard. To go much wider than 1.5% or so is probably beyond what we are thinking about. In terms of Basel, whatever they call it now, 3.5

or 4, I don't think per se that's necessarily what's coloring our thoughts around the buyback. In fact, it's definitively not. The reason we've given you for the buyback is the fact that we've got AT1s that we'd like get into market. The first half year, in our experience, has always been more conducive to getting both good demand and good pricing on those products. And there are listing authority regulations which simply preclude us from doing a buyback at the same time as AT1s, or vice versa for that matter. I think, as far as Basel IV goes, as you probably know as well, if not better than I, there are over 60 areas of national discretion now available within the guidance that was published back in December. And for an organization that operates across 67 markets with some 40 regulators, the opportunity to apply national discretions across a broad range of dimensions within Basel IV creates some uncertainty for us. And I think, when you look at how other people, other institutions that have published their results already on this that have given guidance, it's been pretty much along the same lines that there's pretty broad discretions that can be exercised. And therefore, the outcomes can be uncertain. For those that have provided guidance, I think what characterizes them is they tend to operate in a relatively small number of markets and may have benefited from the fact of some guidance from the regulators already. I think certainly our principal regulators around the world are still very much in the stage of working through their own policy application in this regard. So yes, there is some uncertainty in terms of the impact. And as we get greater guidance, we'll be sure to provide you with some guidance when it becomes meaningful to do, but that's not what's influenced our decision with respect to buybacks at first -- at the end of the year.

Operator

Our next question today comes from Michael Helsby from Bank of America.

Michael Francis Helsby
BofA Merrill Lynch, Research Division

I've got 2 questions, if I can. Thanks for Slide 33, you've given us the future sensitivity in the outer-years to the future move in the yield curve, but clearly, 2017, we saw rates moving already, which does imply that you're, for want of a better word, already pregnant with a higher net interest income in the outer-years. So I was wondering if you could actually quantify that NII benefit for us in '18, '19, '20 like you've done in that slide. And then secondly, I think, ex the $105 million of customer [dress] that's in NII in the fourth quarter, you're annualizing at $29.9 billion. I think, for all the reasons that you've talked about, NIM now looks like it's going up. I think, Iain, you talked about mid-single digit broadly being in line with 7% loan growth. And obviously you've got an FX tailwind in the U.K. next year. It does imply that consensus NII of $30.6 billion looks extremely mean. I was just wondering if you thought that was a fair observation.

Iain James Mackay
Former Group Finance Director & Executive Director

Not necessarily, Michael. I don't think we'll necessarily recut the sensitivity table for you right here and now, but when we give you the first quarter numbers, we'll be sure to really look at that sensitivity table that we provide you on Page 33 and update it for any developments that will have occurred or may have occurred between now and the first week of May, when we get those results into your hands. I think overall, going back to the -- what we talked about at the NIM at the beginning of this call, we come out of 2017 with a reasonably constructive position and a reasonably optimistic outlook for Fed policy movement in this regard. But as you can see, we've got a clear basis of assumptions included on Page 33, and I think that gives you the propensity to take that and then doodle with it in your spreadsheet if you're so inclined.

Michael Francis Helsby
BofA Merrill Lynch, Research Division

Okay, so you don't think that consensus NII in 2018 looks too low.

Iain James Mackay
Former Group Finance Director & Executive Director

Not necessarily at this point in time.

Michael Francis Helsby

BofA Merrill Lynch, Research Division

Interesting.

Operator

Our next question comes from Ronit Ghose from Citigroup.

Ronit Ghose
Citigroup Inc, Research Division

I just wanted to follow up. So if consensus NII doesn't look too mean, consensus costs definitely look too low, right, Iain?

Iain James Mackay
Former Group Finance Director & Executive Director

No, don't think so.

Ronit Ghose
Citigroup Inc, Research Division

Okay. 2 more questions...

Iain James Mackay
Former Group Finance Director & Executive Director

Now remember there's an FX impact when it comes -- remember there is FX impact that is going to come through this, okay? So it is important to reflect. And I think we provided on page, the cost page, within the deck, I think it's Page 14, the impact of applying the FX rates, particularly in the sterling-dollar block, that it would have if we apply the exchange rate on the 14th of February. So that's something that we'd always point out just on the basis that we provide you with adjusted data on a constant currency basis. Just continue to reflect that within your models. And as I say, as we work through the first quarter and have a few months of trading activity behind us and a better sense as to how the year is playing out, we'll continue to update you as we get to that point in time.

Ronit Ghose
Citigroup Inc, Research Division

Sure, sure. And I get that, but I'm just looking at where -- I'm just going back to your comment on jaws, which you've repeated a couple of times. Consensus jaws are clearly quite a bit broader than your guidance, so I'm guessing that the consensus costs number, rather than the consensus revenue number, is where the difference is versus your expectations. But you don't have to comment on that. The question I had was specifically one on MREL please, Iain. Before, you guided to the lower end of the $60 billion to $80 billion range, I think, is that still intact? Or we're going to get more MREL issuance. And I have a second, more broader question, and maybe that's more for your incoming CEO, about open banking in the U.K. HSBC seems to be the only big bank that have done much on this front. And I'm -- just would love any kind of color or anecdotes on how you guys see that playing out, open banking, PSD2, for you in the U.K. this year. So MREL, $60 billion.

Iain James Mackay
Former Group Finance Director & Executive Director

So MREL range, $60 billion to $80 billion. I think that range still holds true. At this point, we have one of our principal regulators that has provided some reasonably firm guidance on this on MREL and the positioning of MREL across the group, and that's the potential regulation authority in the U.K. We -- there is a consultation document out there from the HKMA, which will get firmed up as we move through the year and probably very much towards the end of the year actually, which again would be helpful, as well as an expectation of improved guidance from the U.S. But I think the $60 billion to $80 billion range remains an appropriate range to work on. I'm not sure I would guide you necessarily to the lower end of that range, but certainly within that range is where we see it right now. I think -- in terms of cost guidance, I think we've sort of given you the tools here. We had the exit run rate that we talked about, so excluding the incremental investment that was largely focused within retail bank Wealth Management and certain digital tools in the fourth quarter, we exited 2017 in line with the 2014 expense base, around about 7.5 to 7.6 quarterly run rate. And if you think about that continued investments in the growth of the business to be bound by 1% to 1.5% to 2% positive jaws, then don't multiply 7.6 times 4. Think about revenue growth and the propensity for us to continue to invest into that growth whilst maintaining a positive jaws of 1% or so. And I think, with that, it gives you the ability to model out what this may look like with a reasonable degree of accuracy as the results flow through.

John Michael Flint
Group Chief Executive, Member of Management Board & Executive Director

And I'll pick up on the -- so with respect to the question on open banking: It's open banking is here. It's the regulatory direction of travel on this one is clear. The potential disruption that this could cause, we think, is quite significant, so it's therefore important for us to be in early, testing and learning and experimenting with this. So we've currently got 3 aggregation platforms trialing. We got one in the U.K. called HSBC Beta, which we launched in September last year, which allows customers to see all of their accounts on one screen and, let's say, who they bank with. And from our perspective, it's important that our customers aggregate through us. This is all ultimately about control of the customer relationship. So we've gone out early. I'm very proud of that. We just need to test and learn and see where we take -- where we can take that. We have something in France called personal economy that we're doing in partnership with a fintech. And our first direct brand in the U.K. is also trialing a proposition that's currently in the FCA sandbox. So our attitude towards this is we need to test and learn and be reasonably agile in our thinking. We'll keep you updated as we learn.

Operator

We will take our last question today from Martin Leitgeb from Goldman Sachs.

Martin Leitgeb
Goldman Sachs Group Inc., Research Division

Also 2 questions from my side, please. And the first one is just to go back to your U.K. proposition in light of upcoming ring fencing access and deposit base within the ring fence and your strategy on mortgages. And I just wondered if you could shed a little bit of light on the launch of new -- of the new intermediary mortgage platform, which I think has successfully launched in 4Q. And I was just wondering if you could give us an indication on what you think your market share could get to in terms of mortgage lending because, as far as I'm aware, I think in direct lending you have a kind of a market share of roughly 20% at the moment in mortgages in the U.K. In terms of indirect origination, we have broadcast it's around 1% to 2%. And I was just wondering. The new platform you have launched, where could that potentially get your market share in terms of intermediary lending in mortgages in the U.K.? And the second question is just a follow-up on Slide 33 and the incremental disclosure on NII sensitivity over time, and I was just wondering if I read this correctly. So for any potential rate hikes, you would get the benefit -- around 50% to 60% of the benefit coming through in year 1, with the remainder then over the next coming years. And I was just wondering if that is an indication that you have fairly limited amount of structural hedging in place. Because I would have typically expected that the feed-through could be potentially slower with structural hedging in place.

John Michael Flint
Group Chief Executive, Member of Management Board & Executive Director

Martin, okay, it's John. I'll take the mortgage platform first. So I'd -- I'm not going to give you a number as to where we think we can take market share to. I think we -- well, the figures show that we took our market share of approvals from 8% in '16 up to 9% during the quarters '17, so we're up roughly 1% on the year. We've got -- we still have funding and capital to allow us to continue to grow in the U.K., so we'll just continue to see that trend, but I don't want to signal a number or an end date for that. With respect to the new platform, the platform was launched probably 12, 15 months ago. And it's recently been upgraded, yes, and too early to give you any kind of indication as to what that's going to do to production, but any upgrade clearly is going to help.

Iain James Mackay
Former Group Finance Director & Executive Director

Martin, on the structural hedges, we do have a number of market structural hedges and most notably in the U.K. We do not have structural hedges within the Hong Kong marketplace. So that may inform your question to some degree. We have time for one more question.

Operator

Your next question comes from David Lock from Deutsche Bank.

David John Lock
Deutsche Bank AG, Research Division

So had two, really, on the U.S. The first one was just on HSBC U.S.A. The core Tier 1 looks like it fell from 15.3 to 14.2 quarter-on-quarter. I just wondered if you could clarify what was the driver of that change. Is it an upstream to the group? Or is it a reflection of the U.S. tax change? And the second one was on the U.S. tax change. I just wondered if you -- if it was too early; or if you maybe had any initial thoughts on what you thought the impact could be for your long-term tax rate; and if there's any beat implications, particularly given you obviously fund a lot of the group out of the holding company.

Iain James Mackay
Former Group Finance Director & Executive Director

So the answer to your first question was upstreaming of surplus capital was the driver of the reduction in the capital ratios within the U.S. And then on the tax change, we've got $1.2 billion, $1.3 billion impairment on the deferred tax assets in the U.S. Obviously, in the longer term, as we continue to improve the profitability of the U.S. business, a lower corporate tax rate ought to be beneficial. One of the things that we are working through with a number of our peer group is to understand detailed guidance, which is yet to be received from the IRS, around the application of VAT and how various thresholds apply within that calculation. As I'm sure you know, it's a fairly complex setup and piece of legislation that's been put in place with respect to VAT. So we are still working through whether or not it bites for HSBC. And if it doesn't, then obviously we clearly benefit from a lower corporate tax rate going forward, but we do need to have a clearer read on the guidance from the IRS before we make that final determination.

David John Lock
Deutsche Bank AG, Research Division

And just a couple of follow-ups. So could you just confirm the dollar amount that was upstreamed? And on the beat, I just wondered. I mean obviously, if this works out, then actually it is negative for you because of the funding, the way the funding will be transferred from the holdings into the U.S.A. business. Would you consider issuing locally in order to effectively optimize that? Or is that just not simply something that would work from a regulatory perspective?

Iain James Mackay
Former Group Finance Director & Executive Director

It -- certainly the U.S. regulation with respect to TLAC would conceivably allow us to do that. We do have a SEC-registered entity in the U.S. that has in the past issued senior notes into the marketplace. So it is not beyond the bounds of possibility, but we certainly would make, take no action in that respect until we've got a clearer understanding of exactly how VAT would apply. And there are a number of areas of ongoing consultation and clarification that have been sought from the IRS in terms of how it's going to be applied in that regard. In terms of the total amount of capital upstreamed from the U.S., in 2017, it was USD 4 billion.

Stuart Thomson Gulliver
Former Group Chief Executive, Chairman of Management Board & Executive Director

Okay, that brings the call to an end. Thanks very much. Thank you, operator.