Near Risk-Free Rate Risk Disclosure

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The following is provided for general information only. You should conduct your own assessment of the risks involved and seek guidance from professional advisors (such as legal, tax and/or accountancy advisors) on the possible implications of the changes outlined in this Disclosure. The information below is not exhaustive and HSBC is not in a position to express a view on the likelihood of any particular event occurring. HSBC does not, through this Disclosure, provide any advice or recommendation of product offering, nor does it assume any responsibility to provide advice.

The Interbank Offered Rates ("IBORs") are the subject of national and international regulatory guidance and reform. Important interest rate changes are happening in 2021.

Why are we sending this to you?

The market and industry conventions for near Risk-Free Rates ("RFRs") are continuing to evolve and are new in the context of many products. Therefore, we wanted to make you aware of the potential impact these changes and the use of RFRs may have. This information may help you decide whether products using RFRs are appropriate for you.

Differences between IBORs and RFRs

RFRs differ from IBORs in a number of material respects. IBORs and RFRs are not economically equivalent. RFRs are calculated differently and may result in changes to the amount payable under a financial security, credit facility, derivative or other financial instrument (a "Product").

IBORs are "term rates" which means they are published over different periods of time (e.g. 3 or 6 months) and are "forward-looking" which means they are published at the beginning of the interest period. IBORs are measures of unsecured interbank lending rates, and include the additional risks involved in lending over a future term. These risks include a credit risk element that the borrower may not be able to repay as well as a term liquidity risk of committing funds over a longer period.

Most RFRs are currently "backward-looking" overnight rates based on short-term actual historic secured (e.g. the Secured Overnight Financing Rate (USD SOFR), the Swiss Average Rate Overnight (CHF SARON)), or unsecured (e.g. the Euro Short Term Rate (EUR €STR), the Tokyo Overnight Average Rate (JPY TONAR), the Sterling Overnight Index Average Rate (GBP SONIA)) transactions in the wholesale market. RFRs do not incorporate any term risk or credit risk and are therefore typically lower than their IBOR equivalents.

The following outlines a number of potential key risks of entering into a Product which references an RFR directly or indirectly.

Potential impact

- RFRs are not free of risk, hence they are considered "near risk-free". RFRs can rise or fall as a result of changing economic conditions and central bank policy decisions.
- The interest rate for a Product based on an RFR may be calculated based on a series of overnight rates compounded over the relevant interest period. Therefore, the interest payable under such a Product may only be known at or near the end of that interest period and it may be difficult for you to estimate reliably the amount of interest which will be payable.
- Different methodologies may exist for the calculation of interest for RFR-based products. This could mean that amounts payable or receivable could be lower or higher depending on the calculation methodology used.
- Daily changes in the RFR may be more volatile than daily changes in comparable benchmark or market rates and, as such, the return or payments on a Product linked to an RFR may fluctuate more than in the case of a Product that is linked to a less volatile rate.
- An adjustment spread may be added to the RFR to compensate for the difference to IBORs. The level of the adjustment spread may vary depending on a number of factors, e.g. the currency, the calculation methodology used and the interest period selection made.
- The method of adoption or application of RFRs may differ in each of the capital markets, derivatives and loan markets. Therefore, you should carefully consider how any potential mismatch between the adoption of RFRs across these markets may impact any hedging or other financial arrangements which you may have in place in connection with any acquisition, holding or disposal of a Product referencing an RFR.
- Future changes to market practice or conventions relating to the use of RFRs may result in HSBC aligning with another future prevailing market standard, for example the adoption of forward-looking term RFRs which are currently being developed. Future changes could potentially have adverse impacts for you, require you to make changes to the documentation you have executed with us or require other administrative and operational changes. These further changes could result in you incurring additional costs.
- The number of financial instruments referencing RFRs such as OTC derivatives is limited and so there may be limited liquidity in the market. Some market participants may be considering alternative reference rates other than RFRs for certain Products. The adoption of a variety of replacement rates for IBORs instead of the emergence of a single successor rate could impact the pricing and limit the liquidity of a Product referencing an RFR.

Where can I find further information?

- If you have any questions, please speak to your Relationship Manager. However, please note we are unable to provide specific advice or recommendations to you on this issue. Given the current level of uncertainty and the complexity of this issue, we strongly recommend you seek guidance from professional advisors if you have any questions.

Further information is available on our website: www.hsbcprivatebank.com (see Financial Regulation section)

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