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If you have sold or otherwise transferred all of your holding of HSBC Ordinary Shares, please pass this document, together with the accompanying form of proxy/attendance card, as soon as possible to the purchaser or transferee or to the stockbroker, bank or other agent through whom the sale or transfer was effected for transmission to the purchaser or transferee. The distribution of this document in jurisdictions other than the United Kingdom and Hong Kong may be restricted by law and therefore persons into whose possession this document comes should inform themselves about and observe any such restrictions. Any failure to comply with these restrictions may constitute a violation of the securities laws of any such jurisdiction. This document includes particulars given in compliance with the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited for the purpose of giving information with regard to HSBC Holdings. The Directors collectively and individually accept full responsibility for the accuracy of the information contained in this document and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief there are no other facts the omission of which would make any statement herein misleading.

Applications have been or will be made to the UK Listing Authority and to the London Stock Exchange for the New HSBC Ordinary Shares to be admitted to the Official List and to trading on the London Stock Exchange's market for listed securities respectively, to the Hong Kong Stock Exchange for listing of, and permission to deal in, the New HSBC Ordinary Shares, and to the New York Stock Exchange and Euronext Paris for listing of the New HSBC Ordinary Shares. Application has been or will be made for HSBC ADSs representing New HSBC Ordinary Shares to be listed on the New York Stock Exchange. Dealings in New HSBC Ordinary Shares are expected to commence on the London Stock Exchange at 8.00 a.m. (UK time) on 1 April 2003 and on the Hong Kong Stock Exchange at 9.30 a.m. (Hong Kong time) on 2 April 2003.



HSBC Holdings plc

(Incorporated and registered in England and Wales with registered number 617987)

DISCLOSEABLE TRANSACTION CIRCULAR

relating to the acquisition of

Household International, Inc.

by a wholly owned subsidiary of

HSBC Holdings plc

and incorporating a

Notice of Extraordinary General Meeting

Notice of an Extraordinary General Meeting of HSBC Holdings to be held at Cabot Hall, Cabot Place West, Canary Wharf, London E14 5AB, United Kingdom at 11.00 a.m. (UK time) on 28 March 2003 is set out at the end of this document. A form of proxy for use at the Extraordinary General Meeting is enclosed. To be valid, the form of proxy should be completed and returned, in accordance with the instructions set out on it, to the Company's Registrars, Computershare Investor Services PLC, PO Box 451, Owen House, 8 Bankhead Crossway North, Edinburgh EH11 0NU, United Kingdom, or to the offices of Computershare Hong Kong Investor Services Limited, Rooms 1901-1905, Hopewell Centre, 183 Queen's Road East, Hong Kong as soon as possible but in any event so as to arrive no later than 11.00 a.m. (UK time) on 26 March 2003 or 7.00 p.m. (Hong Kong time) on 26 March 2003. Completion of a form of proxy will not preclude you from attending and voting at the Extraordinary General Meeting should you choose to do so.

Morgan Stanley & Co. Limited, Rohatyn Associates LLC and HSBC Bank plc are acting for HSBC Holdings and no one else in connection with the Acquisition and will not be responsible to anyone other than HSBC Holdings for providing the protections afforded to clients of Morgan Stanley & Co. Limited, Rohatyn Associates LLC and HSBC Bank plc respectively or for providing advice in relation to the Acquisition.

Cazenove & Co. Ltd. is acting for HSBC Holdings as sponsor in connection with the applications for the New HSBC Ordinary Shares to be admitted to the Official List and to trading on the London Stock Exchange's market for listed securities and will not be responsible to anyone other than HSBC Holdings for providing the protections offered to clients of Cazenove & Co. Ltd. or for providing advice in relation to the applications.

A Chinese translation of this document and the Notice of Extraordinary General Meeting is available on request from Computershare Hong Kong Investor Services Limited, Rooms 1901-1905, Hopewell Centre, 183 Queen's Road East, Hong Kong.

如欲取得本文件及股東特別大會通告之中譯本，可於香港皇后大道東183號合和中心1901-1905室向香港中央證券登記有限公司索取。

Access to the Meeting

Cabot Hall is wheelchair accessible. To help us ensure the Extraordinary General Meeting is fully accessible to all HSBC shareholders, please contact Stuart Calder (telephone: (0)20 7992 1390, fax: (0)20 7992 4631, email: stuartcalder@hsbc.com) if you have any particular access needs.

This document is available on the HSBC Group's website, www.hsbc.com.

The Extraordinary General Meeting can be viewed live on the internet at www.hsbc.com by selecting the 'EGM webcast' link on the right hand side of the home page. A recording of the Extraordinary General Meeting will be available after the conclusion of the meeting until the Effective Date.

Expected Timetable

Latest time and date for receipt of forms of proxy for the Extraordinary General Meeting	11.00 a.m. on 26 March 2003
Extraordinary General Meeting of HSBC Shareholders	11.00 a.m. on 28 March 2003
Special Meeting of Household Shareholders	10.00 a.m. (Central Standard Time) on 28 March 2003
Effective Date (assuming receipt of various regulatory approvals/consents)	1 April 2003
Admission of New HSBC Ordinary Shares to the Official List and commencement of dealings on the London Stock Exchange	8.00 a.m. on 1 April 2003
Commencement of dealings on the Hong Kong Stock Exchange	9.30 a.m. (Hong Kong time) on 2 April 2003

All references to time in this document are to UK time unless otherwise stated.

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Directors, company secretary and advisers

Directors	Sir John Bond	<i>(Group Chairman, Executive Director)</i>
	The Baroness Dunn, DBE	<i>(Deputy Chairman and senior Non-executive Director)</i>
	Sir Brian Moffat, OBE	<i>(Deputy Chairman and senior independent Non-executive Director)*</i>
	Sir Keith Whitson	<i>(Group Chief Executive, Executive Director)</i>
	The Lord Butler, GCB, CVO	<i>(Non-executive Director)*</i>
	R.K.F. Ch'ien, CBE	<i>(Non-executive Director)*</i>
	C.F.W. de Croisset	<i>(Executive Director)</i>
	W.R.P. Dalton	<i>(Executive Director)</i>
	D.G. Eldon	<i>(Executive Director)</i>
	D.J. Flint	<i>(Group Finance Director, Executive Director)</i>
	W.K.L. Fung, OBE	<i>(Non-executive Director)*</i>
	S.K. Green	<i>(Executive Director)</i>
	S. Hintze	<i>(Non-executive Director)*</i>
	A.W. Jebson	<i>(Executive Director)</i>
	Sir John Kemp-Welch	<i>(Non-executive Director)*</i>
	The Lord Marshall	<i>(Non-executive Director)</i>
	Sir Mark Moody-Stuart, KCMG	<i>(Non-executive Director)*</i>
	S.W. Newton	<i>(Non-executive Director)*</i>
	H. Sohmen, OBE	<i>(Non-executive Director)</i>
	C.S. Taylor	<i>(Non-executive Director)*</i>
	Sir Brian Williamson, CBE	<i>(Non-executive Director)*</i>

all of 8 Canada Square, London E14 5HQ, United Kingdom

** Denotes independent Non-executive Director*

Group Company Secretary	R.G. Barber
Registered Office of Company	8 Canada Square London E14 5HQ United Kingdom
Financial Advisers	Morgan Stanley & Co. Limited 25 Cabot Square Canary Wharf London E14 4QA United Kingdom Rohatyn Associates LLC 30 Rockefeller Place Suite 5000 New York NY 10020 USA HSBC Bank plc 8 Canada Square London E14 5HQ United Kingdom

Sponsor	Cazenove & Co. Ltd. 12 Tokenhouse Yard London EC2R 7AN United Kingdom
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Auditor and Reporting Accountants	KPMG Audit Plc 8 Salisbury Square London EC4Y 8BB United Kingdom
Legal counsel to HSBC Holdings as to English law	Norton Rose Kempson House Camomile Street London EC3A 7AN United Kingdom
Legal counsel to HSBC Holdings as to US law	Cleary, Gottlieb, Steen & Hamilton One Liberty Plaza New York NY 10006 USA Milbank, Tweed, Hadley & McCloy 1825 Eye Street, N.W., Suite 1100 Washington D.C. 20006 USA
Legal counsel to HSBC Holdings as to Hong Kong law	Norton Rose 38/F Jardine House 1 Connaught Place Central Hong Kong
Legal counsel to HSBC Holdings as to French law	Cleary, Gottlieb, Steen & Hamilton 41, Avenue de Friedland 75008 Paris France
Registrar – Principal Register	Computershare Investor Services PLC PO Box 435 Owen House 8 Bankhead Crossway North Edinburgh EH11 4BR United Kingdom
Registrar – Hong Kong Overseas Branch Register	Computershare Hong Kong Investor Services Limited Rooms 1901-1905 Hopewell Centre 183 Queen’s Road East Hong Kong
ADR Depositary	The Bank of New York 101 Barclay Street, 22 West New York NY 10286 USA
Exchange Agent	Computershare Investor Services LLC Wall Street Plaza 88 Pine Street – 19th Floor New York NY 10005 USA

Part I: Letter from the Chairman of HSBC Holdings



26 February 2003

Dear Shareholder

Proposed Acquisition of Household International, Inc.

On 14 November 2002, we announced that HSBC Holdings had reached agreement to acquire Household International, Inc., one of the largest independent consumer finance companies in the USA.

The Acquisition will be effected in accordance with the terms of a Merger Agreement entered into on 14 November 2002 between HSBC Holdings, H2 (a wholly owned subsidiary of HSBC Holdings) and Household, which provides for Household to be merged with and into H2. Following the Acquisition, H2 will continue to be a wholly owned subsidiary of HSBC Holdings but will be renamed "Household International, Inc."

The Acquisition is subject to a number of conditions, including the approval of the shareholders of HSBC Holdings and Household, and regulatory and other consents and approvals in the USA, the UK, Canada and other relevant jurisdictions. Subject to obtaining such consents and approvals, the Acquisition is expected to be completed at the end of the first quarter of 2003.

The purpose of this document is to provide you with details of and reasons for the Acquisition. At the end of this document, you will find a Notice convening the Extraordinary General Meeting to be held on 28 March 2003, at which your approval of the Acquisition will be sought. The Acquisition constitutes for HSBC Holdings a Class 1 transaction for the purposes of the Listing Rules and a discloseable transaction for the purposes of the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange.

Under the terms of the Merger Agreement, Household Common Shareholders will be entitled to receive for each Household Common Share, at their election, 2.675 HSBC Ordinary Shares or 0.535 HSBC ADSs (each HSBC ADS representing 5 HSBC Ordinary Shares).

The HSBC Ordinary Shares to be issued in exchange for Household Common Shares will result in an increase in the issued ordinary share capital of HSBC Holdings of approximately 13.52 per cent (based on the issued ordinary share capital of HSBC Holdings as at 21 February 2003 and the number of Household Common Shares expected to be in issue on the Effective Date).

In addition:

- All the outstanding Household Non-voting Preferred Stock will be converted in the Acquisition into the right to receive from HSBC Holdings cash in an aggregate amount of approximately US\$1,100 million (together with approximately US\$20.9 million in respect of accrued but unpaid dividends up to but excluding the Effective Date, assuming the Effective Date is 1 April 2003).
- All the outstanding Household Voting Preferred Stock will be designated for redemption by Household pursuant to its terms immediately prior to the Effective Date. It is estimated that Household will apply an aggregate amount of approximately US\$114.8 million (together with approximately US\$2.2 million in respect of accrued and unpaid dividends up to but excluding the Effective Date, assuming the Effective Date is 1 April 2003) in redeeming the Household Voting Preferred Stock.

HSBC Holdings plc

Incorporated in England with limited liability. Registered in England: number 617987

Registered Office and Group Head Office:

8 Canada Square, London E14 5HQ, United Kingdom

- Pursuant to their terms, the outstanding Household Equity Units will remain outstanding following completion of the Acquisition, with the purchase contracts that form a portion of such Household Equity Units becoming contracts to purchase HSBC Ordinary Shares in lieu of Household Common Shares, adjusted to reflect the Exchange Ratio.
- Pursuant to their terms, the rights to acquire Household Common Shares under the Household Zero-coupon Debt Securities will be converted, as a consequence of the Acquisition, into rights to acquire HSBC Ordinary Shares adjusted to reflect the Exchange Ratio.
- Options over Household Common Shares outstanding on the Effective Date will be converted into options over HSBC Ordinary Shares, adjusted to reflect the Exchange Ratio. Other rights to receive Household Common Shares outstanding on the Effective Date will be converted into rights to receive HSBC Ordinary Shares, adjusted to reflect the Exchange Ratio.

The Merger Agreement anticipated that the Household Common Shareholders would be entitled to receive the HSBC Holdings second interim dividend in respect of 2002 which is expected to be paid in May 2003 to those HSBC Ordinary Shareholders on the register of members on 21 March 2003. As the Acquisition will not have been completed before the record date for this dividend it is expected that, as provided for in the Merger Agreement, Household will instead declare a cash dividend for Household Common Shareholders on the register of members immediately prior to the Effective Time in respect of each Household Common Share equal to 2.675 times the HSBC Holdings second interim dividend per HSBC Ordinary Share. Such dividend will be paid on 6 May 2003 (the date on which the HSBC Holdings second interim dividend will be paid) or if the Acquisition is completed after 6 May 2003, promptly after the Effective Date. The HSBC Holdings second interim dividend will be announced at the same time as HSBC Holdings publishes its audited accounts for the financial year ended 31 December 2002, which is expected to be on 3 March 2003.

Household has agreed to pay HSBC Holdings a termination fee of US\$550 million under certain circumstances if the Acquisition is not completed.

The Acquisition does not involve any connected person of HSBC Holdings (as defined in the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange).

The consideration is valued at approximately US\$28.92 per Household Common Share (approximately £18.23 or HK\$225.55), based on the closing middle market price for an HSBC Ordinary Share of 681.5p, as derived from the Daily Official List on 21 February 2003 (being the latest practicable date prior to the publication of this document). On this basis, the total aggregate consideration for the number of Household Common Shares expected to be in issue on the Effective Date (not including any Household Common Shares that may be issued on the exercise of options or rights other than those which would lapse if not exercised on or before the Effective Date) is approximately US\$13,860 million (approximately £8,737 million or HK\$108,094 million). The consideration was arrived at after arm's length negotiations between the parties and the Directors of HSBC consider it to be fair and reasonable.

Further details of the terms of the Merger Agreement and of the conditions to the implementation of the Acquisition are set out in Part IV of this document. A copy of the Merger Agreement was filed with the SEC in the United States on 20 December 2002 as an annexure to the Proxy Statement/Prospectus, and is available on the HSBC Group's website at www.hsbc.com and for inspection as referred to in paragraph 13 of Part V.

Household's Business

Household is the holding company of a group of companies offering a variety of consumer lending products primarily to middle-market consumers. Household currently has over 50 million active consumer accounts across the United States, the UK and Canada. Household is listed on the New York Stock Exchange.

Household is one of the largest independent consumer finance companies in the United States. It is also the country's second largest third-party issuer of private label credit cards, the eighth largest issuer of MasterCard and Visa credit cards and the fourth largest provider of credit insurance.

In the UK and Republic of Ireland, Household operates under the HFC and Beneficial brand names and has over 200 branches. In Canada, Household has 110 branches in 10 provinces offering a range of consumer financial services.

The following table sets out selected consolidated financial information of Household, prepared in accordance with US GAAP (in US\$ millions), which has been extracted from its filings with the SEC:

	Year ended 31 December 2002 ¹	Six months ended 30 June 2002 ¹	Year ended 31 December 2001 ²	Year ended 31 December 2000 ²
	US\$m	US\$m	US\$m	US\$m
Total common shareholders' equity	9,223 ³	8,661	7,843	7,667
Income before income taxes	2,253 ⁴	1,502	2,819	2,500
Net income	1,558	998	1,848	1,631

¹ Unaudited

² Audited

³ A full consolidated balance sheet at 31 December 2002 has not yet been published. Total common shareholders' equity at that date has been extracted from Household's unaudited earnings release for the year ended 31 December 2002 dated 15 January 2003.

⁴ Included within income before income taxes for the year ended 31 December 2002 are deductions representing the following:

(a) US\$525 million relating to Household's Multi-State Settlement Agreement

(b) US\$378 million in respect of the disposal of substantially all of the remaining assets and deposits of Household Bank, f.s.b.

Further information on Household is set out in Part II of this document.

Reasons for, and Benefits of, the Acquisition

The Acquisition brings together one of the world's most successful deposit gatherers with one of the world's largest generators of assets, and creates significant opportunities to strengthen HSBC Holdings' business in a way that benefits its shareholders and is consistent with its strategic objectives.

The Acquisition improves the geographic balance of the HSBC Group's earnings, significantly increasing the contribution from the North American business. On the basis of reported performance in the first six months of 2002, adjusted in the case of Household to UK GAAP, each of the North American, Asian and European segments would have contributed approximately 30 per cent to the enlarged group's pre-tax profit on a cash basis. Household offers the HSBC Group national coverage in the United States for consumer lending, credit cards and credit insurance through varied distribution channels including about 1,400 offices in 46 states, over 10,500 franchised auto dealerships, 140 retail merchant relationships, over 250 correspondent mortgage broker relationships and multiple websites. Nevertheless, this improved geographic balance might not prove beneficial to the HSBC Group if the US economy is weaker than generally anticipated over the medium and long term.

As at 30 June 2002, the HSBC Group had approximately US\$101 billion in loans and advances to banks and approximately US\$173 billion in debt securities. As a result of diminished corporate credit demand, the HSBC Group faces potential challenges in deploying other capital without increasing concentration risk. By expanding its US consumer finance operations through the Acquisition, the HSBC Group seeks to add an asset class that further diversifies its portfolio to offset its potential exposure to increased concentration risk. HSBC Holdings is aware, however, that some customers and investors could react negatively to the HSBC Group being associated with sub-prime lending and that pending litigation and negative publicity associated with allegations of improper lending practices by companies in this sector, including Household, could reduce the benefits of the Acquisition to the HSBC Group.

In terms of customer focus, the Acquisition meets HSBC Holdings' stated objective of growing consumer assets, adding over 50 million consumer accounts worldwide and total assets of US\$122 billion on a UK GAAP basis as at 30 June 2002. The current subdued outlook for world economies, interest rates, inflation and corporate profitability increases the attractiveness of being able to access consumers directly at the moment when they are contemplating entering into a financial transaction or reviewing their financial affairs. In this regard HSBC Holdings believes that Household's technology platforms and practices, in particular, in the areas of marketing, database management and credit scoring capability are at the forefront of global practice, and that the Acquisition will allow for the leveraging of these platforms and practices throughout the enlarged group.

The combination of the HSBC Group with Household creates a top 10 credit card issuer globally, and presents a significant opportunity to achieve cost benefits for the enlarged group by consolidating the HSBC Group's North American card processing business, presently outsourced, with that of Household. HSBC Holdings expects that the significant scalability in volume of Household's credit card platforms will allow for low cost expansion across wider geographic markets.

The Acquisition offers significant opportunities to extend Household's business model into countries and territories currently served by the HSBC Group and broadens the product range available to the enlarged customer base. HSBC Holdings believes that the Acquisition will allow the enlarged group to capture valuable

customer business that currently falls outside the enlarged group's franchise. It expects that the Acquisition will permit the enlarged group to market "prime" products through Household's origination channels in the United States and "non-prime" products to the HSBC Group's deposit customers who are not eligible for the HSBC Group's traditional loan products. It also expects that the Acquisition will allow customers who might otherwise have ceased to be Household customers as their financial circumstances improve, to migrate from Household to the HSBC Group thereby remaining customers of the enlarged group. HSBC Holdings also intends to link Household's Hispanic customer base with its Mexican banking network for remittance services and to link the HSBC Group's Mexican banking network, including the recently acquired Grupo Financiero Bital S.A. de C.V. ("GF Bital"), with Household's consumer finance capabilities to serve qualifying emigrants. However, it is possible that some of those opportunities will not be realised.

The HSBC Group and Household currently utilise compatible systems architectures which will allow for cost savings through consolidation and common purchasing. The combination of businesses is also expected to produce cost savings in administrative support and through consolidating card processing. HSBC Holdings also expects that funding costs for the Household business will be lower in the future as a result of the financial strength and funding diversity of the HSBC Group. However, some or all of these anticipated cost savings and reduced funding costs may not be realised. In addition, the Acquisition is expected to be accretive to earnings per share for 2003 on a UK GAAP basis.

Your attention is drawn to the risk factors set out in paragraph 9 of Part V of this document.

Current Trading and Prospects

The benefits derived from the breadth and capital generating strength of the HSBC Group's core domestic franchises continue to support resilient operating performance, including into the current year to date.

In retail markets, continuing weak demand for equity products has been more than offset by strong growth in personal lending and mortgage banking as consumers in some markets respond to sustained low interest rates. Deposit flows remain strong and sales of insurance protection products and capital protected investment products continue to grow.

Lending to the corporate sector remains subdued and as a consequence of successive interest rate reductions over the past 24 months, treasury income is declining as maturing investments are redeployed in lower yielding assets.

Mitigating the impact of lower interest rates on the deployment of the HSBC Group's liquid resources, the continuing low interest rate environment is favourable in maintaining bad debt charges within recent experience.

The HSBC Group remains cautious about the economic outlook for the remainder of the current year, with political factors and external events weighing heavily on economic forecasting. This having been said, the HSBC Group remains strong in capital and earning power and is well positioned to seek growth opportunities globally with few geographic or product constraints.

Recent Developments

Since the announcement on 5 August 2002 of HSBC Holdings' interim results for the six month period ended 30 June 2002, there have been a number of developments across the HSBC Group. On 8 October 2002, HSBC Holdings announced that it had reached an agreement to invest US\$600 million in Ping An Insurance Company of China, Limited ("Ping An"). This investment has now been made and HSBC Holdings has acquired an interest of 10 per cent of the issued share capital of Ping An. With the establishment of this strategic partnership, HSBC Holdings looks forward to working with Ping An to take advantage of opportunities available in China's rapidly growing insurance and wealth management industries.

HSBC Holdings' most recent significant acquisition was completed on 25 November 2002 when it acquired GF Bital in Mexico by way of a cash tender offer. It received 99.59 per cent acceptance of the offer, which resulted in HSBC Holdings paying a total consideration of approximately US\$1.135 billion. All the necessary regulatory approvals needed for the transaction were received and HSBC Holdings has begun the process of integrating GF Bital into the HSBC Group.

In addition, in September 2002 HSBC Holdings announced three new non-executive director appointments when Stewart Newton, Carole Taylor and Sir Brian Williamson agreed to join the HSBC Board.

Directors and Management of HSBC Holdings Following the Acquisition

In seeking to realise the potential benefits of the Acquisition, HSBC Holdings considered that it was important to retain key senior management of Household. Accordingly, it has been agreed that nine senior officers of Household (including, as mentioned below, its Chairman and Chief Executive) will have new employment agreements with Household for terms of three years which will become effective on completion of the Acquisition.

Assuming the Acquisition is completed, William F. Aldinger, III, who is currently Chairman and Chief Executive Officer of Household, will become a member of the HSBC Board.

Following completion of the Acquisition, Mr. Aldinger will serve as Chairman and Chief Executive Officer of Household until 1 January 2004 and thereafter as Chairman and Chief Executive Officer of Household and HSBC North America, Inc.

Mr. Aldinger has entered into a new employment agreement with Household for a term of three years which will become effective on completion of the Acquisition, details of which are set out in Part V of this document.

Save as described above, the composition of the HSBC Board is not expected to change as a result of the Acquisition.

Financial Information and Accounting Treatment

Unless otherwise stated, all financial information in this letter is extracted from the financial information set out in Parts II and III of this document. You should read the whole document and not just rely on key or summarised information.

Except where otherwise stated, amounts quoted in US dollars in this document have been converted into equivalent sterling amounts and Hong Kong dollar amounts, for illustrative purposes only, at the Noon Buying Rates of £0.6304: US\$1 and HK\$7.7991: US\$1 prevailing on 21 February 2003, the latest practicable date prior to the publication of this document.

HSBC Holdings' audited accounts for the financial year ended 31 December 2002 are expected to be published on 3 March 2003 and will be made available on the HSBC Group's website: www.hsbc.com. These accounts will also be filed at the SEC as part of HSBC Holdings' Form 20-F filing. Supplementary listing particulars including extracts from the audited accounts will also be delivered to the Registrar of Companies in England and Wales for registration as required by section 83 of FSMA and will be made available on the HSBC Group's website and for inspection as referred to in paragraph 11.3 of Part V.

HSBC Holdings intends to account for the Acquisition using acquisition accounting under UK GAAP. Under this method of accounting, the assets and liabilities of Household will be recorded at their respective fair values as at the Acquisition completion date and added to those of HSBC Holdings. Financial statements and results of operations of HSBC Holdings reported after completion of the Acquisition will reflect these values, but prior financial statements of HSBC Holdings will not be restated to reflect the historical financial position or results of operations of Household.

The unaudited pro forma financial information contained in this document has been prepared using the acquisition method to account for the Acquisition. Under UK GAAP, the final determination of the purchase price is based on the price of HSBC Ordinary Shares on the date the Acquisition is completed. In addition, the final allocation of the purchase price will be determined after completion of a thorough analysis to determine the fair values of Household's assets and liabilities as at the Effective Date. Accordingly, the final acquisition accounting adjustments and goodwill may be materially different from those reflected in the unaudited pro forma financial information set out in this document.

Extraordinary General Meeting

In view of the size of the transaction, the Listing Rules require HSBC Holdings to obtain HSBC Shareholders' approval of the Acquisition. For this purpose, the HSBC Board has convened an Extraordinary General Meeting for 11.00 a.m. on 28 March 2003. At the EGM, an ordinary resolution will be proposed: (a) to approve the Acquisition (including the arrangements to be put in place in relation to outstanding options over, and rights to receive, Household Common Shares) and to authorise the Directors (or any duly authorised committee thereof) to take the necessary steps to implement it, subject to such non-material modifications as the Directors think fit; and (b) to authorise the Directors for the purposes of section 80 of the Act to allot in connection with the Acquisition

New HSBC Ordinary Shares up to an aggregate nominal amount of US\$702,863,189. This amount is equal to the nominal amount of the approximate maximum number of New HSBC Ordinary Shares which may be issued as a consequence of the Acquisition and represents 14.83 per cent of the total issued ordinary share capital of HSBC Holdings on 21 February 2003, the latest practicable date prior to the publication of this document. The authority will lapse at the conclusion of the annual general meeting of the Company to be held in 2004. The Directors intend to exercise the authority in connection with the allotment of New HSBC Ordinary Shares in connection with the Acquisition. The authority is in addition to the existing authority granted to the Directors at the Annual General Meeting of the Company held on 31 May 2002, which will remain in full force and effect until its expiry at the Annual General Meeting of the Company to be held in 2003, when a new resolution will be proposed, in the usual way, granting authority to the Directors to allot shares.

The Acquisition is conditional on the approval of the Resolution and the Merger Agreement becoming unconditional. The Resolution is being proposed as an ordinary resolution which requires the approval of a majority of the votes cast in person or on a poll at the EGM. A Notice of the EGM is contained at the end of this document.

New HSBC Ordinary Shares

Based on the 473,664,080 Household Common Shares in issue as at 21 February 2003 and the further 5,577,856 Household Common Shares expected to be issued prior to the Effective Date (not including any Household Common Shares that may be issued on the exercise of options or rights other than those which would lapse if not exercised on or before the Effective Date), the Directors expect to allot following the Effective Date up to 1,281,972,179 HSBC Ordinary Shares as Consideration Shares to Household Common Shareholders on the surrender of certificates in respect of their Household Common Shares to the Exchange Agent (as further described in paragraph 5 of Section A of Part IV). The Consideration Shares will be credited as fully paid and will rank *pari passu* in all respects with the existing HSBC Ordinary Shares, save that they will only have the right to receive any dividends or other distributions declared, made or paid in respect thereof with a record date on or after the Effective Date.

Following the Acquisition becoming effective, Additional HSBC Ordinary Shares may be issued. These Additional HSBC Ordinary Shares will rank *pari passu* in all respects with the then existing HSBC Ordinary Shares, save that they will only have the right to receive any dividends or other distributions declared, made or paid in respect thereof with a record date on or after the date of issue.

Applications have been or will be made to the UK Listing Authority and to the London Stock Exchange for the New HSBC Ordinary Shares to be admitted to the Official List and to trading on the London Stock Exchange's market for listed securities respectively, to the Hong Kong Stock Exchange for listing of, and permission to deal in, the New HSBC Ordinary Shares, and to the New York Stock Exchange and Euronext Paris for listing of the New HSBC Ordinary Shares. Application has been or will be made for HSBC ADSs representing New HSBC Ordinary Shares to be listed on the New York Stock Exchange. It is a condition of the Acquisition becoming effective that such applications shall have been approved. Assuming the satisfaction of all conditions under the Merger Agreement and the completion of the Acquisition on 1 April 2003, dealings in New HSBC Ordinary Shares are expected to commence on the London Stock Exchange at 8.00 a.m. (UK time) on 1 April 2003 and on the Hong Kong Stock Exchange at 9.30 a.m. (Hong Kong time) on 2 April 2003.

Further details relating to the New HSBC Ordinary Shares and the procedure for their allotment are set out in paragraph 2 of Part V of this document.

Action to be Taken

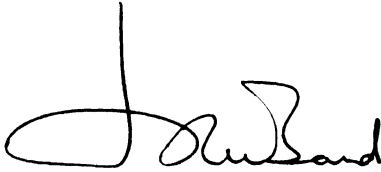
It is important that HSBC Shareholders complete the enclosed form of proxy, in accordance with the instructions printed thereon. The form of proxy must be received no later than 11.00 a.m. (UK time) on 26 March 2003 or 7.00 p.m. (Hong Kong time) on 26 March 2003. Completion and return of a form of proxy will not preclude you from attending and voting at the Extraordinary General Meeting should you so wish.

Recommendation

The board of directors of Household has unanimously recommended that Household Shareholders vote in favour of the resolution to approve the Acquisition and the adoption of the Merger Agreement, which will be proposed at the Special Meeting of Household Shareholders.

The HSBC Board, which has been advised by Morgan Stanley, Rohatyn Associates and HSBC Bank, considers the financial terms of the Acquisition to be fair and reasonable to HSBC Holdings. In giving their advice, Morgan Stanley, Rohatyn Associates and HSBC Bank have relied upon the HSBC Board's commercial assessment of the Acquisition. The HSBC Board considers the Acquisition and the other matters to which the Resolution relates to be in the best interests of HSBC Shareholders taken as a whole. The HSBC Board unanimously recommends that HSBC Shareholders vote in favour of the Resolution to be proposed at the EGM as the Directors intend to do in respect of their respective beneficial holdings amounting to 4,134,637 HSBC Ordinary Shares (0.04 per cent of the issued share capital as at 21 February 2003).

Yours sincerely

A handwritten signature in black ink, appearing to read 'John Bond', with a large, stylized initial 'J'.

Sir John Bond
Group Chairman

Part II: Information Relating to the Household Group

1 Description of Household

Household was created in 1981 as a result of a shareholder-approved restructuring of Household Finance Corporation, which was established in 1878. Household is principally a non-operating holding company. Household's subsidiaries primarily provide middle-market consumers with several types of loan products in the United States, Canada and the United Kingdom. Household, through its subsidiaries (including Beneficial Corporation, which was acquired in 1998), offers real estate secured loans, auto finance loans, MasterCard and VISA credit cards, private label credit cards, tax refund anticipation loans, retail instalment sales financing loans and other types of unsecured loans, as well as credit and speciality insurance products. As at 30 September 2002, Household had approximately 32,000 employees and over 50 million active consumer accounts. Household's principal executive office is located at 2700 Sanders Road, Prospect Heights, Illinois 60070, United States of America.

Based on Household's earnings release on 15 January 2003, at 31 December 2002 Household had US\$107.5 billion in managed receivables and US\$82.6 billion in owned receivables. For the year ended 31 December 2002, Household's income before income taxes was US\$2.3 billion on net revenues of US\$10.8 billion.

2 Financial Information for Household

The financial information on Household reproduced in section A of this Part II of this document was extracted without material adjustment from the audited restated consolidated income statements for the years ended 31 December 2001, 2000 and 1999 and the audited restated consolidated balance sheets as at 31 December 2001 and 2000, included in Household's annual report on Form 10-K/A for the year ended 31 December 2001, as audited by KPMG LLP. The following notes in respect of balance sheet analyses as at 31 December 2000 were extracted without material adjustment from the financial statements included in Household's annual report on Form 10-K for the year ended 31 December 2000, as audited by Household's former auditors, Arthur Andersen LLP. These notes were not affected by the restatement:

- the maturity analyses shown in notes 3, 4, 7, 9, 10 and 15;
- the sensitivity analyses shown in notes 5 and 17;
- the credit and market risk analysis in note 10;
- the concentration of credit risk analysis in note 10;
- the analysis of preferred securities and junior subordinated notes in note 11;
- the number of Household preferred stock authorised for issue in note 12; and
- the analysis of stock options outstanding in note 16.

The financial information in respect of the balance sheet as at 31 December 1999, reproduced in section A of this Part II, was extracted without material adjustment from the financial statements included in Household's annual report on Form 10-K for the year ended 31 December 1999, as audited by Household's former auditors, Arthur Andersen LLP.

The financial information on Household reproduced in section B of this Part II was extracted without material adjustment from the unaudited financial information included in Household's quarterly report filed on Form 10-Q for the period ended 30 June 2002 and from Household's earnings release for the financial year ended 31 December 2002 which was published on 15 January 2003 and was filed as an exhibit to the current report on Form 8-K with the SEC on 16 January 2003.

Household's audited accounts for the financial year ended 31 December 2002 are expected to be published in early March 2003 and will be made available on Household's website: www.household.com. These accounts will also be filed at the SEC on Form 10-K. Supplementary listing particulars including extracts from these audited accounts will also be delivered to the Registrar of Companies in England and Wales for registration as required by Section 83 of FSMA, and will be made available for inspection as referred to in paragraph 13 of Part V of this document.

Household International, Inc.

A. Audited consolidated financial information for the years ended 31 December 2001, 2000 and 1999

The financial information has been prepared in accordance with US GAAP. US GAAP differs from UK GAAP in certain material respects. A summary of these differences is set out in section C of this Part II.

Consolidated statement of income

	Year ended 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Finance and other interest income.....	9,961	8,651	6,554
Interest expense	(4,174)	(3,929)	(2,777)
Net interest margin	5,787	4,722	3,777
Provision for credit losses on owned receivables.....	(2,913)	(2,117)	(1,716)
Net interest margin after provision for credit losses	2,874	2,605	2,061
Securitisation revenue.....	1,763	1,459	1,366
Insurance revenue	662	561	534
Investment income.....	168	174	169
Fee income.....	904	760	546
Other income.....	323	230	224
Total other revenues	3,820	3,184	2,839
Salaries and fringe benefits.....	(1,597)	(1,312)	(1,049)
Sales incentives.....	(273)	(204)	(146)
Occupancy and equipment expense.....	(337)	(307)	(271)
Other marketing expenses.....	(490)	(443)	(347)
Other servicing and administrative expenses.....	(717)	(595)	(550)
Amortisation of acquired intangibles and goodwill.....	(158)	(166)	(150)
Policyholders' benefits.....	(303)	(262)	(258)
Total costs and expenses	(3,875)	(3,289)	(2,771)
Income before income taxes	2,819	2,500	2,129
Income taxes	(971)	(869)	(701)
Net income	1,848	1,631	1,428
Earnings Per Common Share			
Net income.....	1,848	1,631	1,428
Preferred dividends	(16)	(9)	(9)
Earnings available to common shareholders	1,832	1,622	1,419
Average number of common shares	462	472	477
Average number of common and common equivalent shares.....	468	476	482
	US\$	US\$	US\$
Basic earnings per common share	3.97	3.44	2.98
Diluted earnings per common share	3.91	3.40	2.95

The accompanying notes are an integral part of these consolidated financial statements.

Household International, Inc.

Consolidated balance sheet

	At 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Assets			
Cash	544	490	270
Investment securities	3,581	3,259	3,128
Receivables, net	79,263	67,162	52,158
Acquired intangibles and goodwill, net	1,563	1,720	1,611
Properties and equipment, net	531	517	476
Real estate owned	399	337	273
Other assets	3,030	2,824	2,536
Total assets	88,911	76,309	60,452
Liabilities and shareholders' equity			
Debt:			
Deposits	6,562	8,677	4,980
Commercial paper, bank and other borrowings	12,024	10,788	10,778
Senior and senior subordinated debt (with original maturities over one year)	56,824	45,053	34,887
Total debt	75,410	64,518	50,645
Insurance policy and claim reserves	1,095	1,107	1,309
Other liabilities	3,132	2,178	1,722
Total liabilities	79,637	67,803	53,676
Company obligated mandatorily redeemable preferred securities of subsidiary trusts*	975	675	375
Preferred stock	456	164	164
Common shareholders' equity:			
Common stock, \$1.00 par value, 750,000,000 shares authorised; 551,684,740, 551,100,165 and 550,431,057 shares issued at 31 December 2001, 2000 and 1999 respectively	552	551	550
Additional paid-in capital	2,030	1,926	1,781
Retained earnings	8,837	7,397	6,125
Accumulated other comprehensive income	(732)	(215)	(257)
Less common stock in treasury, 94,560,437, 80,080,506 and 82,519,612 shares at 31 December 2001, 2000 and 1999 respectively, at cost	(2,844)	(1,992)	(1,962)
Total common shareholders' equity	7,843	7,667	6,237
Total liabilities and shareholders' equity	88,911	76,309	60,452

* The sole assets of the trusts are junior subordinated deferrable interest notes issued by Household in November 2001, January 2001, June 2000, March 1998 and June 1995, bearing interest at 7.50 per cent, 8.25 per cent, 10.00 per cent, 7.25 per cent and 8.25 per cent, respectively, with principal balances of US\$206 million, US\$206 million, US\$309 million, US\$206 million and US\$77 million, respectively, and due 15 November 2031, 30 January 2031, 30 June 2030, 31 December, 2037, and 30 June 2025, respectively. The US\$103 million junior subordinated deferrable interest notes issued in June 1996 were redeemed in December 2001.

The accompanying notes are an integral part of these consolidated financial statements.

Household International, Inc.

Consolidated statement of cash flows

	Year ended 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Cash provided by operations			
Net income	1,848	1,631	1,428
Adjustments to reconcile net income to net cash provided by operations:			
Provision for credit losses on owned receivables	2,913	2,117	1,716
Insurance policy and claim reserves	204	37	76
Depreciation and amortisation	315	308	299
Deferred income tax provision	(6)	46	(1)
Interest-only strip receivables, net change	(101)	(59)	(34)
Other, net	345	108	(230)
Cash provided by operations	5,518	4,188	3,254
Investments in operations			
Investment securities:			
Purchased	(1,744)	(804)	(1,432)
Matured	482	452	792
Sold	686	238	733
Short-term investment securities, net change	256	(48)	(111)
Receivables:			
Originations, net	(46,325)	(39,930)	(32,888)
Purchases and related premiums	(1,577)	(4,163)	(2,572)
Sold	32,294	26,919	25,250
Acquisition of business operations	—	(87)	(43)
Properties and equipment purchased	(175)	(174)	(140)
Properties and equipment sold	20	16	29
Cash decrease from investments in operations	(16,083)	(17,581)	(10,382)
Financing and capital transactions			
Short-term debt and demand deposits, net change	1,301	182	839
Time certificates, net change	(2,119)	3,220	2,962
Senior and senior subordinated debt issued	21,172	21,608	11,281
Senior and senior subordinated debt retired	(9,107)	(11,152)	(6,871)
Policyholders' benefits paid	(86)	(117)	(127)
Cash received from policyholders	61	60	63
Shareholders' dividends	(407)	(359)	(332)
Issue of company obligated mandatorily redeemable preferred securities of subsidiary trusts	400	300	—
Redemption of company obligated mandatorily redeemable preferred securities of subsidiary trusts	(100)	—	—
Issue of preferred stock	291	—	—
Purchase of treasury stock	(916)	(209)	(916)
Issue of common stock	122	64	45
Cash increase from financing and capital transactions	10,612	13,597	6,944
Effect of exchange rate changes on cash	7	16	(3)
Increase/(decrease) in cash	54	220	(187)
Cash at 1 January	490	270	457
Cash at 31 December	544	490	270
Supplemental cash flow information:			
Interest paid	4,511	3,921	2,758
Income taxes paid	980	690	338
Supplemental non cash investing and financing activities:			
Common stock issued for acquisition	—	209	15

The accompanying notes are an integral part of these consolidated financial statements.

Household International, Inc.

Consolidated statement of changes in preferred stock and common shareholders' equity

	Common shareholders' equity						Total common shareholders' equity US\$m
	Preferred stock US\$m	Common stock US\$m	Additional paid-in capital US\$m	Retained earnings US\$m	Accumulated other comprehensive income ¹ US\$m	Common stock in treasury US\$m	
Balance at 1 January 1999	164	544	1,653	5,029	(145)	(1,015)	6,066
Net income				1,428			1,428
Other comprehensive income, net of tax:							
Unrealised losses on investments and interest-only strip receivables, net of reclassification adjustment					(94)		(94)
Foreign currency translation adjustments					(18)		(18)
Total comprehensive income							1,316
Cash dividends:							
Preferred at stated rates				(9)			(9)
Common, US\$0.68 per share				(323)			(323)
Exercise of stock options		6	103			(51)	58
Issue of common stock			25			20	45
Purchase of treasury stock						(916)	(916)
Balance at 31 December 1999	164	550	1,781	6,125	(257)	(1,962)	6,237
Net income				1,631			1,631
Other comprehensive income, net of tax:							
Unrealised gains on investments and interest-only strip receivables, net of reclassification adjustment					95		95
Foreign currency translation adjustments					(53)		(53)
Total comprehensive income							1,673
Cash dividends:							
Preferred at stated rates				(9)			(9)
Common, US\$0.74 per share				(350)			(350)
Exercise of stock options		1	21			30	52
Issue of common stock			124			149	273
Purchase of treasury stock						(209)	(209)
Balance at 31 December 2000	164	551	1,926	7,397	(215)	(1,992)	7,667
Net income				1,848			1,848
Other comprehensive income, net of tax:							
Cumulative effect of change in accounting principle (FAS No. 133)					(241)		(241)
Unrealised losses on cash flow hedging instruments, net of reclassification adjustment					(458)		(458)
Unrealised gains on investments and interest-only strip receivables, net of reclassification adjustment					200		200
Foreign currency translation adjustments					(18)		(18)
Total comprehensive income							1,331
Cash dividends:							
Preferred at stated rates				(16)			(16)
Common, US\$0.85 per share				(392)			(392)
Issue of preferred stock	292						—
Exercise of stock options		1	31			15	47
Issue of common stock			73			49	122
Purchase of treasury stock						(916)	(916)
Balance at 31 December 2001	456	552	2,030	8,837	(732)	(2,844)	7,843

¹ Accumulated other comprehensive income includes the following:

	Year ended 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Unrealised losses on cash flow hedging instruments	(699)	—	—
Unrealised gains/(losses) on investments and interest-only strip receivables:			
Gross unrealised gains/(losses)	352	42	(110)
Income tax expense (benefit)	128	18	(39)
Net unrealised gains/(losses)	224	24	(71)
Cumulative adjustments for foreign currency translation adjustments	(257)	(239)	(186)
Total	(732)	(215)	(257)

The accompanying notes are an integral part of these consolidated financial statements.

Household International, Inc.

Consolidated statement of changes in preferred stock and common shareholders' equity

	Preferred stock	Common stock		
		Issued	In treasury	Net outstanding
Shares outstanding				
Balance at 1 January 1999	1,398,279	544,124,170	(60,986,431)	483,137,739
Exercise of common stock options		6,083,549	(791,681)	5,291,868
Issue of common stock		223,338	1,055,566	1,278,904
Purchase of treasury stock			(21,797,066)	(21,797,066)
Balance at 31 December 1999	1,398,279	550,431,057	(82,519,612)	467,911,445
Exercise of common stock options		516,823	1,531,458	2,048,281
Issue of common stock		152,285	6,321,263	6,473,548
Purchase of treasury stock			(5,413,615)	(5,413,615)
Balance at 31 December 2000	1,398,279	551,100,165	(80,080,506)	471,019,659
Issue of preferred stock	300,000			
Exercise of common stock options		548,744	1,466,979	2,015,723
Issue of common stock		35,831	1,450,484	1,486,315
Purchase of treasury stock			(17,397,394)	(17,397,394)
Balance at 31 December 2001	1,698,279	551,684,740	(94,560,437)	457,124,303

The accompanying notes are an integral part of these consolidated financial statements.

Household International, Inc.

Comprehensive income

Household adopted FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," on 1 January 2001. The adoption was accounted for as a cumulative effect of a change in an accounting principle. The table below discloses reclassification adjustments and the related tax effects allocated to each component of other comprehensive income (expense) including the adoption of FAS No. 133 and unrealised gains (losses) on cash flow hedging instruments in 2001, unrealised gains (losses) on investments and interest-only strip receivables and foreign currency translation adjustments.

	Before-tax US\$m	Tax (expense) benefit US\$m	Net-of-tax US\$m
Year ended 31 December 1999			
Unrealised gains/(losses) on investments and interest-only strip receivables:			
Net unrealised holding losses arising during the period.....	(135)	47	(88)
Less: Reclassification adjustment for gains realised in net income	(9)	3	(6)
Net unrealised losses on investments and interest-only strip receivables	(144)	50	(94)
Foreign currency translation adjustments	(23)	5	(18)
Other comprehensive expense	(167)	55	(112)
Year ended 31 December 2000			
Unrealised gains/(losses) on investments and interest-only strip receivables:			
Net unrealised holding gains arising during the period.....	152	(57)	95
Less: Reclassification adjustment for gains realised in net income	(1)	1	—
Net unrealised gains on investments and interest-only strip receivables.....	151	(56)	95
Foreign currency translation adjustments	(75)	22	(53)
Other comprehensive income	76	(34)	42
Year ended 31 December 2001			
Unrealised gains/(losses) on cash flow hedging instruments:			
Cumulative effect of change in accounting principle (FAS No. 133).....	(377)	136	(241)
Net losses arising during the period.....	(1,137)	408	(729)
Less: Reclassification adjustment for losses realised in net income.....	423	(152)	271
Net losses on cash flow hedging instruments	(1,091)	392	(699)
Unrealised gains/(losses) on investments and interest-only strip receivables:			
Net unrealised holding gains arising during the period.....	321	(115)	206
Less: Reclassification adjustment for gains realised in net income	(11)	4	(7)
Net unrealised gains on investments and interest-only strip receivables.....	310	(111)	199
Foreign currency translation adjustments	(28)	10	(18)
Other comprehensive expense	(809)	291	(518)

The accompanying notes are an integral part of these consolidated financial statements.

Household International, Inc.

Notes to consolidated financial statements

1 Summary of significant accounting policies

Principles of consolidation

The consolidated financial statements include the accounts of Household International, Inc. and all subsidiaries. Unaffiliated trusts to which Household has transferred securitised receivables which are qualifying special purpose entities as defined by FAS No. 140 "Accounting for Transfers and Servicing of Financial Assets and the Extinguishment of Liabilities, a Replacement of FASB Statement No. 125," are not consolidated. All significant intercompany accounts and transactions have been eliminated.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Certain prior year amounts have been reclassified to conform with the current year's presentation.

Investment securities

Household maintains investment portfolios (comprised primarily of debt securities) in both Household's non-insurance and insurance operations. The entire investment securities portfolio was classified as available-for-sale at 31 December 2001, 2000 and 1999. Available-for-sale investments are intended to be invested for an indefinite period but may be sold in response to events Household expects to occur in the foreseeable future. These investments are carried at fair value. Unrealised holding gains and losses on available-for-sale investments are recorded as adjustments to common shareholders' equity in accumulated other comprehensive income, net of income taxes. Any decline in the fair value of investments which is deemed to be other than temporary is charged against current earnings.

The cost of investment securities sold is determined using the specific identification method. Interest income earned on the non-insurance investment portfolio is classified in the statements of income in net interest margin. Realised gains and losses from the investment portfolio and investment income from the insurance portfolio are recorded in investment income. Accrued investment income is classified with investment securities.

Receivables

Receivables are carried at amortised cost. Finance income is recognised using the effective yield method. Premiums and discounts on purchased receivables are recognised as adjustments to the yield of the related receivables. Origination fees are deferred and amortised to finance income over the estimated life of the related receivables, except to the extent they offset directly related lending costs. MasterCard and Visa annual fees are netted with direct lending costs, deferred, and amortised on a straight-line basis over one year. Net deferred annual fees related to these receivables totalled US\$90 million at 31 December 2001, US\$63 million at 31 December 2000 and US\$29 million at 31 December 1999.

Insurance reserves and unearned premiums applicable to credit risks on consumer receivables are treated as a reduction of receivables in the balance sheet, since payments on such policies generally are used to reduce outstanding receivables.

Provision and credit loss reserves

Provision for credit losses on owned receivables is made in an amount sufficient to maintain credit loss reserves at a level considered adequate to cover probable losses of principal, interest and fees, including late, over limit and annual fees, in the existing owned portfolio. Probable losses are estimated for consumer receivables based on contractual delinquency status and historical loss experience. For commercial loans, probable losses are calculated using estimates of amounts and timing of future cash flows expected to be received on loans. In addition, loss reserves on consumer receivables are maintained to reflect Household's judgment of portfolio risk factors which may not be fully reflected in the statistical calculation which uses roll rates and migration analysis. These risk factors include economic conditions, bankruptcy trends, product mix, geographic concentrations and other similar items. Charge-off and customer account management policies are also considered when establishing loss reserve requirements to ensure appropriate allowances exist for products with longer charge-off periods and for customers benefiting from account management decisions. Loss reserve estimates are reviewed periodically

and adjustments are reported in earnings when they become known. As these estimates are influenced by factors outside Household's control, such as consumer payment patterns and economic conditions, there is uncertainty inherent in these estimates, making it reasonably possible that they could change.

Household's charge-off policy for consumer receivables varies by product. Unsecured receivables are written off at the following stages of contractual delinquency: MasterCard and Visa 6 months; private label 9 months; and personal non-credit card 9 months and no payment received in 6 months, but in no event to exceed 12 months. For real estate secured receivables, carrying values in excess of net realisable value are charged off at the time of foreclosure or when settlement is reached with the borrower. For loans secured by automobiles, carrying values in excess of net realisable value are charged off at the earlier of repossession and sale of the collateral, the collateral being in Household's possession for more than 90 days, or the loan becoming 150 days contractually delinquent. Charge-offs may occur sooner for certain consumer receivables involving a bankruptcy. Household's policies for consumer loans permit reset of the contractual delinquency status of an account to current, subject to certain limits, if a predetermined number of consecutive payments has been received and there is evidence that the reason for the delinquency has been cured. Such re-aging policies vary by product and are designed to manage customer relationships and ensure maximum collections. Commercial receivables are written off when it becomes apparent that an account is uncollectible.

Non-accrual loans

Non-accrual loans are loans on which accrual of interest has been suspended. Interest income is suspended on real estate secured, personal non-credit card and commercial loans when principal or interest payments are more than three months contractually past due. For MasterCard and Visa and private label credit card receivables, interest continues to accrue until the receivable is charged off. For auto finance receivables, accrual of interest income is discontinued when payments are more than two months contractually past due. Accrual of income on non-accrual real estate secured and personal homeowner loans ("PHL's") is resumed if the receivable becomes less than three months contractually delinquent and on auto finance loans when the loan becomes less than two months contractually delinquent. Interest on non-accrual personal non-credit card receivables other than PHL's is recorded as collected. Accrual of income on non-accrual commercial loans is resumed if the loan becomes contractually current. Cash payments received on non-accrual commercial loans are either applied against principal or reported as interest income, according to Household's judgment as to the collectibility of principal.

Receivables sold and serviced with limited recourse and securitisation revenue

Certain real estate secured, auto finance, MasterCard and Visa, private label and personal non-credit card receivables have been securitised and sold to investors with limited recourse. Household has retained the servicing rights to these receivables. Recourse is limited to Household's rights to future cash flow and any subordinated interest that Household may retain. Upon sale, the receivables are removed from the balance sheet and a gain on sale is recognised for the difference between the carrying value of the receivables and the adjusted sales proceeds. The adjusted sales proceeds include cash received and the present value estimate of future cash flows to be received over the lives of the sold receivables. Future cash flows are based on estimates of prepayments, the impact of interest rate movements on yields of receivables and securities issued, delinquency of receivables sold, servicing fees and other factors. The resulting gain is also adjusted by a provision for estimated probable losses under the recourse provisions based on historical experience and estimates of expected future performance. Gains on sale net of recourse provisions, servicing income and excess spread relating to securitised receivables are reported in the accompanying consolidated statements of income as securitisation revenue.

In connection with these transactions, Household records interest-only strip receivables, representing its contractual right to receive interest and other cash flows from its securitisation trusts. The interest-only strip receivables are reported at fair value using discounted cash flow estimates as a separate component of receivables net of Household's estimate of probable losses under the recourse provisions. Cash flow estimates include estimates of prepayments, the impact of interest rate movements on yields of receivables and securities issued, delinquency of receivables sold, servicing fees and estimated probable losses under the recourse provisions. Unrealised gains and losses are recorded as adjustments to common shareholders' equity in accumulated other comprehensive income, net of income taxes. The interest-only strip receivables are reviewed for impairment quarterly or earlier if events indicate that the carrying value may not be recovered. Any decline in the fair value of the interest-only strip receivables which is deemed to be other than temporary is charged against current earnings.

Household has also, in certain cases, retained other subordinated interests in these securitisations. Neither the interest-only strip receivables nor the other subordinated interests are in the form of securities.

In September 2000, the FASB issued FAS No. 140, which revised the standards for accounting for securitisations and required certain disclosures. Household adopted the non-disclosure related provisions of FAS No. 140 as required on 1 April 2001. The adoption did not have a significant effect on Household's operations.

Properties and equipment, net

Properties and equipment are recorded at cost, net of accumulated depreciation and amortisation. For financial reporting purposes, depreciation is provided on a straight-line basis over the estimated useful lives of the assets which generally range from 3 to 40 years. Leasehold improvements are amortised over the lesser of the economic useful life of the improvement or the term of the lease. Maintenance and repairs are expensed as incurred.

Reposessed collateral

Real estate owned is valued at the lower of cost or fair value less estimated costs to sell. These values are periodically reviewed and reduced, if necessary. Costs of holding real estate, and related gains and losses on disposal, are credited or charged to operations as incurred as a component of operating expense. Repossessed vehicles, net of loss reserves when applicable, are recorded at the lower of the estimated fair market value or the outstanding receivable balance.

Insurance

Insurance revenues on revolving credit insurance policies are recognised when billed. Insurance revenues on the remaining insurance contracts are recorded as unearned premiums and recognised into income based on the nature and terms of the underlying contracts. Liabilities for credit insurance policies are based upon estimated settlement amounts for both reported and incurred but not yet reported losses. Liabilities for future benefits on annuity contracts and specialty and corporate owned life insurance products are based on actuarial assumptions of investment yields, mortality and withdrawals.

Acquired intangibles and goodwill

Acquired intangibles consist of acquired credit card relationships which are amortised on a straight-line basis over their estimated useful lives. These lives vary by portfolio and initially ranged from 4 to 15 years. Goodwill represents the purchase price over the fair value of identifiable assets acquired less liabilities assumed from business combinations and up to 31 December 2001 was amortised on a straight-line basis over periods not exceeding 25 years. Acquired intangibles are reviewed for impairment using discounted cash flows and goodwill using undiscounted cash flows whenever events indicate that the carrying amounts may not be recoverable. Household considers significant and long-term changes in industry and economic conditions to be its primary indicators of potential impairment. Impairment charges, when required, are calculated using discounted cash flows.

In July 2001, the FASB issued FAS No. 141, "Business Combinations" and FAS No. 142, "Goodwill and Other Intangible Assets". FAS No. 141 eliminated the pooling of interests method of accounting and required that the purchase method of accounting be used for all business combinations initiated after 30 June 2001. Household had no acquisitions during 2001 which were affected by FAS No. 141. FAS No. 142 changed the accounting for goodwill from an amortisation method to an impairment-only approach. Amortisation of goodwill recorded in past business combinations ceased upon adoption of the statement on 1 January 2002. Amortisation of goodwill reduced net income by US\$46 million in 2001, US\$45 million in 2000 and US\$31 million in 1999, representing a reduction in diluted earnings per share of US\$0.10 in 2001, US\$0.09 in 2000 and US\$0.06 in 1999. Adoption of the statement is expected to increase net income by approximately US\$0.10 per share annually.

Treasury stock

Household accounts for repurchases of common stock using the cost method with common stock in treasury classified in the balance sheet as a reduction of common shareholders' equity. Treasury stock is reissued at average cost.

Derivative financial instruments

2001

With effect from 1 January 2001, Household adopted FAS No. 133, “Accounting for Derivative Instruments and Hedging Activities”, as amended. Under FAS No. 133, all derivatives are recognised on the balance sheet at their fair value. On the date the derivative contract is entered into, Household designates the derivative as a fair value hedge, a cash flow hedge, a hedge of a net investment in a foreign operation, or a non-hedging derivative. Fair value hedges include hedges of the fair value of a recognised asset or liability and certain foreign currency hedges. Cash flow hedges include hedges of the variability of cash flows to be received or paid related to a recognised asset or liability and certain foreign currency hedges. Changes in the fair value of derivatives designated as fair value hedges, along with the change in fair value on the hedged asset or liability that is attributable to the hedged risk, are recorded in current period earnings. Changes in the fair value of derivatives designated as cash flow hedges, to the extent effective as a hedge, are recorded in accumulated other comprehensive income and reclassified into earnings in the period during which the hedged item affects earnings. Changes in the fair value of derivatives used to hedge Household’s net investment in foreign subsidiaries, to the extent effective as a hedge, are recorded in common shareholders’ equity as a component of the cumulative translation adjustment account within accumulated other comprehensive income. Changes in the fair value of derivative instruments not designated as hedging instruments and ineffective portions of changes in the fair value of hedging instruments are recognised in other income in the current period.

Household formally documents all relationships between hedging instruments and hedged items. This documentation includes Household’s risk management objective and strategy for undertaking various hedge transactions, as well as how hedge effectiveness and ineffectiveness are measured. This process includes linking derivatives to specific assets and liabilities on the balance sheet. Household also formally assess, both at the hedge’s inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. When it is determined that a derivative is not highly effective as a hedge or that it has ceased to be a highly effective hedge, Household discontinues hedge accounting prospectively.

When hedge accounting is discontinued because it is determined that the derivative no longer qualifies as an effective hedge, the derivative will continue to be carried on the balance sheet at its fair value, with changes in its fair value recognised in current period earnings. For fair value hedges, the formerly hedged asset or liability will no longer be adjusted for changes in fair value and any previously recorded adjustments to the carrying value of the hedged asset or liability will be amortised in the same manner that the hedged item affects income. For cash flow hedges, amounts previously recorded in accumulated other comprehensive income will be reclassified into income as earnings are impacted by the variability in the cash flows of the hedged item.

If the hedging instrument is terminated early, the derivative is removed from the balance sheet. Accounting for the adjustments to the hedged asset or liability or adjustments to accumulated other comprehensive income are the same as described above when a derivative no longer qualifies as an effective hedge.

If the hedged asset or liability is sold or extinguished, the derivative will continue to be carried on the balance sheet at its fair value, with changes in its fair value recognised in current period earnings. The hedged item, including previously recorded mark-to-market adjustments, is derecognised immediately as a component of the gain or loss upon disposal.

The adoption of FAS No. 133 on 1 January 2001 was accounted for as a cumulative effect of a change in accounting principle. The impact of the adoption was not material to earnings and reduced common shareholders’ equity by US\$241 million. The adjustment to common shareholders’ equity was recorded as a component of accumulated other comprehensive income and was made to recognise at fair value all derivatives that were designated as cash flow hedging instruments. During 2001, approximately US\$119 million in derivative losses associated with the transition adjustment were reclassified into earnings. These losses were offset by decreased interest expense associated with the variable cash flows of the hedged items and resulted in no economic impact on Household’s earnings. Derivative gains associated with the transition adjustment reclassified into earnings during 2001 were not material.

2000 and 1999

Interest rate swaps are the principal vehicle used to manage interest rate risk. Household also utilises interest rate futures, options, caps and floors, and forward contracts. Household has also entered into currency swaps to

convert both principal and interest payments on debt issued in one currency to the appropriate functional currency. Household's interest rate contracts are designated as an effective hedge/synthetic alteration of the specific underlying assets or liabilities (or specific groups of assets or liabilities). The net amount to be paid or received is accrued and included in net interest margin in the statements of income. The correlation between all interest rate contracts and the underlying asset, liability or off-balance sheet item is direct because Household uses interest rate contracts which mirror the underlying item being hedged/synthetically altered. If the correlation between the hedged/synthetically altered item and related interest rate contract ceases to exist, the interest rate contract is recorded at fair value and the associated unrealised gain or loss is included in net interest margin, with any future realised and unrealised gains or losses recorded in other income. Interest rate contracts are recorded in the balance sheet at amortised cost. If interest rate contracts are terminated early, the realised gains and losses are deferred and amortised over the life of the underlying hedged/synthetically altered item as an adjustment to net interest margin. These deferred gains and losses are recorded on the accompanying consolidated balance sheet as adjustments to the carrying value of the hedged/synthetically altered items. In circumstances where the underlying assets or liabilities are sold, any remaining carrying value adjustments or cumulative change in value of any open positions are recognised immediately as a component of the gain or loss upon disposal. Any remaining interest rate contracts previously designated to the sold hedged/synthetically altered item are recorded at fair value with realised and unrealised gains and losses included in other income.

Foreign currency translation

Household has foreign subsidiaries located in the United Kingdom and Canada. The functional currency for each foreign subsidiary is its local currency. Assets and liabilities of these subsidiaries are translated at the rates of exchange in effect on the balance sheet date; income and expenses are translated at the average rates of exchange prevailing during the year. The resulting translation adjustments are accumulated in common shareholders' equity as a component of accumulated other comprehensive income.

Household periodically enters into forward exchange contracts to hedge its investment in foreign subsidiaries. After-tax gains and losses on contracts to hedge foreign currency fluctuations are accumulated in common shareholders' equity as a component of accumulated other comprehensive income. The effects of foreign currency translation in the statements of cash flows are offset against the cumulative foreign currency adjustment, except for the impact on cash. Foreign currency transaction gains and losses are included in income as they occur.

Stock-based compensation

Household accounts for stock option and stock purchase plans in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). In accordance with APB 25, no compensation expense is recognised for stock options issued.

Income taxes

Federal income taxes are accounted for utilising the liability method. Deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. Investment tax credits generated by leveraged leases are accounted for using the deferral method.

2 Business combinations, acquisitions and divestitures

On 7 February 2000, Household purchased all of the outstanding capital stock of Renaissance Holdings, Inc. ("Renaissance"), a privately held issuer of secured and unsecured credit cards to sub-prime customers, for approximately US\$300 million in common stock and cash. The acquisition provided Household with an established platform for growing the sub-prime credit card business and expanding Household's product offerings to customers and prospects in Household's other businesses. The acquisition was accounted for as a purchase and, accordingly, Renaissance's operations have been included in Household's results of operations since 7 February 2000.

In August 1999, Household acquired all of the outstanding capital stock of Decision One Mortgage Company LLC ("Decision One") for approximately US\$60 million in common stock and cash. Decision One originates loans through a 30-state broker network and packages them for sale to investors. The acquisition was accounted for as a purchase and, accordingly, earnings from Decision One have been included in Household's results of operations subsequent to the acquisition date.

3 Investment securities

	At 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Available-for-sale investments			
Corporate debt securities.....	2,054	1,874	1,692
Money market funds.....	342	436	—
Certificates of deposit.....	260	319	—
U.S. government and federal agency debt securities.....	218	174	237
Marketable equity securities.....	21	25	34
Other.....	639	390	1,127
Subtotal.....	3,534	3,218	3,090
Accrued investment income.....	47	41	38
Total investment securities.....	3,581	3,259	3,128

Proceeds from the sale of available-for-sale investments totalled approximately US\$0.7 billion in 2001, US\$0.2 billion in 2000 and US\$0.8 billion in 1999. Gross gains of US\$13 million in 2001, US\$2 million in 2000 and US\$12 million in 1999 and gross losses of US\$2 million in 2001, US\$1 million in 2000 and US\$3 million in 1999 were realised on those sales.

The gross unrealised gains/(losses) on available-for-sale investment securities were as follows:

	Amortised cost US\$m	Gross unrealised gains US\$m	Gross unrealised losses US\$m	Fair value US\$m
At 31 December 2001				
Corporate debt securities.....	2,090	31	(67)	2,054
Money market funds.....	342	—	—	342
Certificates of deposit.....	246	14	—	260
U.S. government and federal agency debt securities.....	217	2	(1)	218
Marketable equity securities.....	24	—	(3)	21
Other.....	612	29	(2)	639
Total available-for-sale investments.....	3,531	76	(73)	3,534
At 31 December 2000				
Corporate debt securities.....	1,949	17	(92)	1,874
Money market funds.....	436	—	—	436
Certificates of deposit.....	319	—	—	319
U.S. government and federal agency debt securities.....	174	2	(2)	174
Marketable equity securities.....	26	—	(1)	25
Other.....	390	1	(1)	390
Total available-for-sale investments.....	3,294	20	(96)	3,218
At 31 December 1999				
Corporate debt securities.....	1,790	4	(102)	1,692
U.S. government and federal agency debt securities.....	249	1	(13)	237
Marketable equity securities.....	33	1	—	34
Other.....	1,128	—	(1)	1,127
Total available-for-sale investments.....	3,200	6	(116)	3,090

See Note 14, “fair value of financial instruments,” for further discussion of the relationship between the fair value of Household’s assets, liabilities and off-balance sheet financial instruments.

Contractual maturities of and yields on investments in debt securities were as follows:

	Corporate debt securities			U.S. Government and federal agency debt securities		
	Amortised cost US\$m	Fair value US\$m	Yield ¹ %	Amortised cost US\$m	Fair value US\$m	Yield ¹ %
At 31 December 2001						
Due within 1 year.....	50	51	5.1	44	45	7.6
After 1 but within 5 years.....	807	817	5.7	85	85	5.7
After 5 but within 10 years.....	393	394	6.5	65	65	5.1
After 10 years	840	792	7.0	23	23	6.0
Total	2,090	2,054	6.4	217	218	5.9
At 31 December 2000						
Due within 1 year.....	199	198	6.97	47	47	5.99
After 1 but within 5 years.....	553	551	6.91	18	19	6.58
After 5 but within 10 years.....	340	333	6.74	37	36	5.59
After 10 years	857	792	7.20	72	72	6.60
Total	1,949	1,874	7.01	174	174	6.22
At 31 December 1999						
Due within 1 year.....	142	142	6.63	30	30	8.43
After 1 but within 5 years.....	389	383	6.46	69	59	6.74
After 5 but within 10 years.....	427	410	6.68	37	47	6.17
After 10 years	832	757	7.24	113	101	6.03
Total	1,790	1,692	6.89	249	237	6.54

¹ Computed by dividing annualised interest by the amortised cost of respective investment securities.

4 Receivables

	At 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Real estate secured	43,857	35,180	24,662
Auto finance.....	2,369	1,850	1,233
MasterCard/Visa.....	8,141	8,054	6,314
Private label.....	11,664	10,347	10,120
Personal non-credit card	13,337	11,328	9,152
Commercial and other	507	599	808
Total owned receivables	79,875	67,358	52,289
Accrued finance charges	1,560	1,303	879
Credit loss reserve for owned receivables	(2,663)	(2,112)	(1,757)
Unearned credit insurance premiums and claims reserves	(896)	(725)	(569)
Interest-only strip receivables	968	636	2,226
Amounts due and deferred from receivable sales	419	702	(910)
Total owned receivables, net.....	79,263	67,162	52,158
Receivables serviced with limited recourse	20,948	20,249	19,439
Total managed receivables, net	100,211	87,411	71,597

Foreign receivables included in owned receivables were as follows:

	At 31 December					
	United Kingdom			Canada		
	2001 US\$m	2000 US\$m	1999 US\$m	2001 US\$m	2000 US\$m	1999 US\$m
Real estate secured.....	925	857	751	458	403	339
MasterCard/Visa	1,174	2,207	2,168	—	—	—
Private label	1,285	1,235	1,145	526	441	427
Personal non-credit card.....	1,218	1,000	1,311	383	377	371
Commercial and other.....	—	1	1	1	2	3
Total	4,602	5,300	5,376	1,368	1,223	1,140

Foreign managed receivables represented 7 per cent, 9 per cent and 11 per cent of total managed receivables at 31 December 2001, 2000 and 1999, respectively.

The outstanding balance of receivables serviced with limited recourse consisted of the following:

	At 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Real estate secured	862	1,458	2,274
Auto finance	4,026	2,713	1,806
MasterCard/Visa	9,254	9,529	9,479
Private label	2,150	1,650	1,150
Personal non-credit card	4,656	4,899	4,730
Total	20,948	20,249	19,439

The combination of receivables owned and receivables serviced with limited recourse, which Household considers its managed portfolio, is shown below:

	At 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Real estate secured	44,719	36,638	26,936
Auto finance	6,395	4,563	3,039
MasterCard/Visa	17,395	17,583	15,793
Private label	13,814	11,997	11,270
Personal non-credit card	17,993	16,227	13,882
Commercial and other	507	599	808
Total	100,823	87,607	71,728

Household maintains facilities with third parties which provide for the securitisation of receivables on a revolving basis totalling US\$12.9 billion, of which US\$10.6 billion were utilised at 31 December 2001. The amounts available under these facilities vary according to the timing and volume of public securitisation transactions.

Contractual maturities of owned receivables were as follows:

	2002 US\$m	2003 US\$m	2004 US\$m	2005 US\$m	2006 US\$m	Thereafter US\$m	Total US\$m
At 31 December 2001							
Real estate secured	11,952	8,589	6,261	4,530	3,377	9,148	43,857
Auto finance	38	75	233	559	1,040	424	2,369
MasterCard/Visa	940	830	702	639	544	4,486	8,141
Private label	5,782	2,280	701	415	276	2,210	11,664
Personal non-credit card	3,336	2,393	1,931	1,507	1,179	2,991	13,337
Commercial and other	44	45	58	40	35	285	507
Total	22,092	14,212	9,886	7,690	6,451	19,544	79,875
	2001 US\$m	2002 US\$m	2003 US\$m	2004 US\$m	2005 US\$m	Thereafter US\$m	Total US\$m
At 31 December 2000							
Real estate secured	8,650	6,352	4,822	3,650	2,803	8,903	35,180
Auto finance	12	29	143	391	809	466	1,850
MasterCard/Visa	983	811	623	571	485	4,581	8,054
Private label	5,666	1,666	518	352	235	1,910	10,347
Other unsecured	4,401	2,450	1,485	944	621	1,427	11,328
Commercial and other	77	37	45	59	42	339	599
Total	19,789	11,345	7,636	5,967	4,995	17,626	67,358
	2000 US\$m	2001 US\$m	2002 US\$m	2003 US\$m	2004 US\$m	Thereafter US\$m	Total US\$m
At 31 December 1999							
Home equity	5,803	4,326	2,980	2,253	1,701	7,599	24,662
Auto finance	7	29	107	238	502	350	1,233
MasterCard/Visa	1,104	828	614	492	404	2,872	6,314
Private label	2,627	1,503	1,365	1,387	304	2,934	10,120
Other unsecured	3,781	1,983	1,153	707	452	1,076	9,152
Commercial	219	43	29	38	52	427	808
Total	13,541	8,712	6,248	5,115	3,415	15,258	52,289

A substantial portion of consumer receivables, based on Household's experience, will be renewed or repaid prior to contractual maturity. The above maturity schedule should not be regarded as a forecast of future cash collections. The ratio of annual cash collections of principal to average principal balances, excluding credit card receivables, approximated 55 per cent in 2001, 53 per cent in 2000 and 62 per cent in 1999.

The following table summarises contractual maturities of owned receivables due after one year by re-pricing characteristic:

	Over 1 but within 5 years US\$m	Over 5 years US\$m
At 31 December 2001		
Receivables at predetermined interest rates.....	27,242	9,986
Receivables at floating or adjusting rates.....	10,997	9,558
Total.....	38,239	19,544
At 31 December 2000		
Receivables at predetermined interest rates.....	21,051	10,580
Receivables at floating or adjusting rates.....	8,892	7,046
Total.....	29,943	17,626
At 31 December 1999		
Receivables at predetermined interest rates.....	14,000	9,294
Receivables at floating or adjusting rates.....	9,491	5,963
Total.....	23,491	15,257

Non-accrual owned consumer receivables totalled US\$2.1 billion, US\$1.6 billion and US\$1.4 billion at 31 December 2001, 2000 and 1999, respectively, including US\$215 million, US\$226 million and US\$237 million, respectively, relating to foreign operations. Interest income that would have been recorded in 2001, 2000 and 1999 if such non-accrual receivables had been current and in accordance with contractual terms was approximately US\$316 million, US\$260 million and US\$240 million, respectively, including US\$35 million, US\$38 million and US\$42 million, respectively, relating to foreign operations.

Interest income that was included in net income for 2001, 2000 and 1999, prior to these loans being placed on non-accrual status, was approximately US\$173 million, US\$144 million and US\$132 million, respectively, including US\$16 million, US\$20 million and US\$23 million, respectively, relating to foreign operations.

Interest-only strip receivables are reported net of Household's estimate of probable losses under the recourse provisions for receivables serviced with limited recourse. Household's estimate of the recourse obligation totalled US\$1.1 billion at 31 December 2001 and US\$1.1 billion at 31 December 2000. Interest-only strip receivables also included fair value mark-to-market adjustments of US\$349 million at year-end 2001 and US\$117 million at year-end 2000.

Amounts due and deferred from receivable sales include certain assets established under the recourse provisions for certain receivable sales, including funds deposited in spread accounts, offset by net customer payments owed to the securitisation trustee. Net customer payments owed to the securitisation trustee totalled US\$27 million at 31 December 2001 and US\$61 million at 31 December 2000.

5 Asset securitisations

Household sells auto finance, MasterCard and Visa, private label and personal non-credit card receivables in various securitisation transactions. Household continues to service and receive servicing fees on the outstanding balance of securitised receivables. Household also retains rights to future cash flows arising from the receivables after the investors receive their contractual return. Household has also, in certain cases, retained other subordinated interests in these securitisations. These transactions typically result in the recording of an interest-only strip receivable which represents the value of the future residual cash flows from securitised receivables. The investors and the securitisation trusts have only limited recourse to Household's assets for failure of debtors to pay. That recourse is limited to Household's rights to future cash flow and any subordinated interest Household retains. Servicing assets and liabilities are not recognised in conjunction with Household's securitisations since Household receives adequate compensation relative to current market rates to service the receivables sold. See Note 1, "Summary of significant accounting policies," for further discussion on Household's accounting for interest-only strip receivables.

Securitisation revenue includes income associated with the current and prior period securitisation and sale of receivables with limited recourse. Such income includes gains on sales, net of Household's estimate of probable credit losses under the recourse provisions, servicing income and excess spread relating to those receivables.

Net initial gains, which represent gross initial gains net of Household's estimate of probable credit losses under the recourse provisions, and the key economic assumptions used in measuring the net initial gains from securitisations completed during the years ended 31 December 2001 and 2000 were as follows:

	MasterCard/ Visa US\$m	Personal non-credit card US\$m	Private label US\$m	Auto finance US\$m	Total US\$m
Year ended 31 December 2001					
Net initial gains.....	7	36	13	110	166
Key economic assumptions: ¹					
Weighted-average life (in years)	0.38	1.23	0.85	2.20	
	%	%	%	%	
Payment speed	93.59	52.33	67.06	34.20	
Expected credit losses (annual rate).....	5.08	7.34	5.49	4.79	
Discount rate on cash flows.....	9.00	11.00	10.00	10.00	
Cost of funds.....	6.15	4.24	5.73	4.54	
	US\$m	US\$m	US\$m	US\$m	US\$m
Year ended 31 December 2000					
Net initial gains.....	44	38	8	80	170
Key economic assumptions: ¹					
Weighted-average life (in years)	0.41	1.28	0.93	2.06	
	%	%	%	%	
Payment speed	92.62	52.01	63.97	35.98	
Expected credit losses (annual rate).....	5.48	6.87	6.60	5.38	
Discount rate on cash flows.....	9.00	11.00	10.00	10.00	
Cost of funds.....	5.88	6.67	6.36	7.12	

¹ Weighted-average annual rates for securitisations entered into during the period for securitisations of loans with similar characteristics.

Certain securitisation trusts, such as credit cards, are established at fixed levels and require frequent sales of new receivables into the trust to replace receivable run-off. These replenishments totalled US\$24.7 billion in 2001 and US\$21.0 billion in 2000. Net gains (gross gains less estimated credit losses under the recourse provisions) related to these replenishments were calculated using weighted-average assumptions consistent with those used for calculating gains on initial securitisations and totalled US\$407 million in 2001 and US\$328 million in 2000.

Cash flows received from securitisation trusts were as follows:

	MasterCard/ Visa US\$m	Personal non-credit card US\$m	Private label US\$m	Auto finance US\$m	Real estate secured US\$m	Total US\$m
Year ended 31 December 2001						
Proceeds from initial securitisations....	261	2,124	500	2,574	—	5,459
Servicing fees received	183	90	35	85	12	405
Other cash flow received on retained interests ¹	789	181	158	112	67	1,307
Year ended 31 December 2000						
Proceeds from initial securitisations....	1,925	2,637	500	1,913	—	6,975
Servicing fees received	180	91	24	61	18	374
Other cash flow received on retained interests ¹	646	177	57	80	82	1,042

¹ Other cash flows include all cash flows from interest-only strip receivables, excluding servicing fees.

Household's interest-only strip receivables are reported at fair value using discounted cash flow estimates.

The sensitivity of the current fair value of the interest-only strip receivables to immediate 10 per cent and 20 per cent unfavourable changes in assumptions is presented in the table below. These sensitivities are based on assumptions used to value Household's interest-only strip receivables at 31 December 2001 and 2000.

	MasterCard/ Visa	Personal non-credit card	Private label	Auto finance	Real estate secured
At 31 December 2001					
Carrying value (fair value) of interest-only strip receivables (US\$m).....	267	335	55	286	25
Weighted-average life (in years)	0.57	1.19	0.79	1.87	1.53
Payment speed assumption (annual rate).....	83.82%	45.62%	69.66%	38.90%	25.95%
Impact on fair value of 10% adverse change (US\$m) ..	(22)	(23)	(5)	(26)	(1)
Impact on fair value of 20% adverse change (US\$m) ..	(42)	(46)	(9)	(60)	(3)
Expected credit losses (annual rate)	5.21%	7.41%	5.49%	6.83%	1.55%
Impact on fair value of 10% adverse change (US\$m) ..	(23)	(36)	(8)	(25)	(1)
Impact on fair value of 20% adverse change (US\$m) ..	(46)	(73)	(17)	(50)	(3)
Discount rate on residual cash flows (annual rate)	9.00%	11.00%	10.00%	10.00%	13.00%
Impact on fair value of 10% adverse change (US\$m) ..	(3)	(3)	—	(7)	(1)
Impact on fair value of 20% adverse change (US\$m) ..	(6)	(6)	(1)	(14)	(1)
Variable returns to investors (annual rate)	5.09%	3.53%	4.62%	5.42%	3.58%
Impact on fair value of 10% adverse change (US\$m) ..	(23)	(19)	(7)	—	(3)
Impact on fair value of 20% adverse change (US\$m) ..	(47)	(38)	(15)	—	(6)
At 31 December 2000					
Carrying value (fair value) of interest-only strip receivables (US\$m).....	218	294	19	100	5
Weighted-average life (in years)	0.61	1.33	0.94	1.87	1.70
Payment speed assumption (annual rate).....	82.75%	45.69%	63.52%	37.57%	27.96%
Impact on fair value of 10% adverse change (US\$m) ..	(19)	(24)	(2)	(3)	(2)
Impact on fair value of 20% adverse change (US\$m) ..	(35)	(48)	(3)	(6)	(4)
Expected credit losses (annual rate)	4.95%	6.35%	6.50%	5.74%	1.67%
Impact on fair value of 10% adverse change (US\$m) ..	(22)	(35)	(9)	(27)	(3)
Impact on fair value of 20% adverse change (US\$m) ..	(45)	(71)	(18)	(54)	(5)
Discount rate on residual cash flows (annual rate)	9.00%	11.00%	10.00%	10.00%	13.00%
Impact on fair value of 10% adverse change (US\$m) ..	(3)	(3)	—	(8)	(1)
Impact on fair value of 20% adverse change (US\$m) ..	(5)	(6)	—	(15)	(1)
Variable returns to investors (annual rate)	6.46%	6.80%	6.70%	7.00%	6.81%
Impact on fair value of 10% adverse change (US\$m) ..	(31)	(39)	(10)	(7)	(5)
Impact on fair value of 20% adverse change (US\$m) ..	(62)	(78)	(19)	(15)	(5)

These sensitivities are hypothetical and should not be considered to be predictive of future performance. As the figures indicate, the change in fair value based on a 10 per cent variation in assumptions cannot necessarily be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the fair value of the residual cash flow is calculated independently from any change in another assumption. In reality, changes in one factor may contribute to changes in another (for example, increases in market interest rates may result in lower prepayments) which might magnify or counteract the sensitivities. Furthermore, the estimated fair values as disclosed should not be considered indicative of future earnings on these assets.

Static pool credit losses are calculated by summing actual and projected future credit losses and dividing them by the original balance of each pool of asset. Due to the short term revolving nature of MasterCard and Visa, personal non-credit card and private label receivables, the weighted-average percentage of static pool credit losses is not considered to be materially different from the weighted-average charge-off assumptions used in determining the fair value of Household's interest-only strip receivables in the table above. At 31 December 2001, static pool credit losses for auto finance loans securitised in 2001 were estimated to be 10.0 per cent and for auto finance loans securitised in 2000 were estimated to be 11.0 per cent.

Receivables information by product including delinquency and net charge-offs for Household's managed portfolios and portfolios serviced with limited recourse were as follows:

At 31 December				
	2001		2000	
	Receivables outstanding US\$m	Delinquent receivables %	Receivables outstanding US\$m	Delinquent receivables %
Managed receivables:				
Real estate secured	44,719	2.68	36,638	2.63
Autofinance	6,395	3.16	4,563	2.55
MasterCard/Visa	17,395	4.10	17,583	3.49
Private label	13,814	5.48	11,997	5.48
Personal non-credit card	17,993	8.87	16,227	7.97
Total consumer	100,316	4.46	87,008	4.20
Commercial and other	507	1.58	599	2.10
Total managed receivables	100,823	4.44	87,607	4.18
Receivables serviced with limited recourse:				
Real estate secured	(862)	5.00	(1,458)	4.01
Autofinance	(4,026)	3.29	(2,713)	2.61
MasterCard/Visa	(9,254)	2.73	(9,529)	2.30
Private label	(2,150)	2.69	(1,650)	4.72
Personal non-credit card	(4,656)	8.36	(4,899)	7.90
Total receivables serviced with limited recourse	(20,948)	4.18	(20,249)	4.02
Owned consumer receivables	79,875	4.53	67,358	4.26

At 31 December				
	2001		2000	
	Average receivables US\$m	Net charge offs %	Average receivables US\$m	Net charge offs %
Managed receivables:				
Real estate secured	40,050	0.53	32,530	0.45
Auto finance	5,323	5.31	3,843	4.80
MasterCard/Visa	17,283	6.63	16,111	5.58
Private label	12,260	5.18	11,194	5.35
Personal non-credit card	17,014	6.79	14,761	6.97
Total consumer	91,930	3.73	78,439	3.64
Commercial and other	555	2.10	693	2.69
Total managed receivables	92,485	3.72	79,132	3.63
Receivables serviced with limited recourse:				
Real estate secured	(1,199)	0.70	(1,848)	0.90
Auto finance	(3,004)	6.32	(2,023)	6.16
MasterCard/Visa	(9,145)	5.27	(8,985)	4.81
Private label	(1,744)	2.72	(1,212)	5.42
Personal non-credit card	(4,528)	6.74	(4,566)	6.86
Total receivables serviced with limited recourse	(19,620)	5.26	(18,634)	5.11
Owned consumer receivables	72,865	3.32	60,498	3.18

Household issued securities backed by dedicated home equity loan receivables of US\$1.6 billion in 2001 and US\$0.5 billion in 1999. For accounting purposes, these transactions were structured as secured financings, therefore, the receivables and the related debt remain on Household's balance sheet. Real estate receivables included closed-end real estate secured receivables totalling US\$1.7 billion at 31 December 2001 and US\$0.4 billion at 31 December 2000 which secured the outstanding debt related to these transactions.

6 Properties and equipment, net

	At 31 December		Depreciable life
	2001 US\$m	2000 US\$m	
Land	8	8	—
Buildings and improvements	575	520	10-40 years
Furniture and equipment	878	844	3-10
Total	1,461	1,372	
Accumulated depreciation and amortisation	930	855	
Properties and equipment, net	531	517	

Depreciation and amortisation expense totalled US\$140 million in 2001, US\$136 million in 2000 and US\$130 million in 1999.

7 Deposits

	At 31 December					
	2001		2000		1999	
	Amount US\$m	Weighted average rate %	Amount US\$m	Weighted average rate %	Amount US\$m	Weighted average rate %
Domestic						
Time certificates	6,001	6.8	6,925	6.7	3,766	6.3
Savings accounts	34	2.1	25	2.9	9	1.9
Demand accounts	36	0.4	15	2.1	1	—
Total domestic deposits	6,071	6.7	6,965	6.7	3,776	6.3
Foreign						
Time certificates	316	5.7	1,530	6.1	1,054	5.6
Savings accounts	54	3.1	56	3.2	69	5.5
Demand accounts	121	3.9	126	5.1	81	2.3
Total foreign deposits	491	5.0	1,712	5.9	1,204	5.3
Total deposits	6,562	6.6	8,677	6.5	4,980	6.0

At 31 December 2001, domestic time certificates included carrying value adjustments totalling US\$25 million relating to derivative financial instruments.

Average deposits and related weighted-average interest rates were as follows:

	At 31 December					
	2001		2000		1999	
	Average deposits US\$m	Weighted average rate %	Average deposits US\$m	Weighted average rate %	Average deposits US\$m	Weighted average rate %
Domestic						
Time certificates	6,468	6.5	6,278	6.7	1,857	6.1
Savings and demand accounts ...	120	0.6	53	1.5	12	1.4
Total domestic deposits	6,588	6.4	6,331	6.6	1,869	6.1
Foreign						
Time certificates	1,173	5.7	1,244	4.5	968	4.8
Savings and demand accounts ...	192	4.5	182	4.5	200	4.4
Total foreign deposits	1,365	5.5	1,426	4.5	1,168	4.7
Total deposits	7,953	6.3	7,757	6.2	3,037	5.5

Interest expense on total deposits was US\$499 million in 2001, US\$484 million in 2000 and US\$168 million in 1999. Interest expense on domestic deposits was US\$424 million in 2001, US\$420 million in 2000 and US\$113 million in 1999.

Maturities of time certificates in amounts of US\$100,000 or more were:

	Domestic US\$m	Foreign US\$m	Total US\$m
At 31 December 2001			
3 months or less	29	211	240
Over 3 months through 6 months	18	30	48
Over 6 months through 12 months	42	39	81
Over 12 months	143	36	179
Total	232	316	548
At 31 December 2000			
3 months or less	28	1,269	1,297
Over 3 months through 6 months	9	125	134
Over 6 months through 12 months	44	109	153
Over 12 months	225	26	251
Total	306	1,529	1,835
At 31 December 1999			
3 months or less	1	556	557
Over 3 months through 6 months	—	160	160
Over 6 months through 12 months	—	94	94
Over 12 months	—	242	242
Total	1	1,052	1,053

Contractual maturities of time certificates within each interest rate range were as follows:

	2002 US\$m	2003 US\$m	2004 US\$m	2005 US\$m	2006 US\$m	Thereafter US\$m	Total US\$m
At 31 December 2001							
Interest rates:							
< 4.00%	72	29	—	—	—	—	101
4.00%-5.99%	428	187	123	17	19	47	821
6.00%-7.99%	1,526	1,091	1,405	821	189	363	5,395
Total	2,026	1,307	1,528	838	208	410	6,317
At 31 December 2000							
Interest rates:							
4.00%-5.99%	301	757	136	138	41	9	1,382
6.00%-7.99%	704	2,431	1,156	1,382	856	543	7,072
8.00% – 9.99%	—	—	—	—	—	1	1
Total	1,005	3,188	1,292	1,520	897	553	8,455
At 31 December 1999							
Interest rates:							
< 4.00%	9	—	—	—	—	—	9
4.00% – 5.99%	766	463	122	165	92	—	1,608
6.00% – 7.99%	233	730	747	424	769	200	3,103
8.00% – 9.99%	57	—	—	—	—	—	57
Total	1,065	1,193	869	589	861	200	4,777

8 Commercial paper, bank and other borrowings

	Commercial paper US\$m	Bank and other borrowings US\$m	Total US\$m
At 31 December 2001			
Balance	9,141	2,883	12,024
Highest aggregate month-end balance			13,926
Average borrowings	9,221	2,240	11,461
Weighted-average interest rate:	%	%	%
At year-end	2.0	2.6	2.2
Paid during year	4.1	3.9	4.0
At 31 December 2000			
Balance	US\$m	US\$m	US\$m
	9,372	1,416	10,788
Highest aggregate month-end balance			12,582
Average borrowings	9,829	2,100	11,929
Weighted-average interest rate:	%	%	%
At year-end	6.6	6.6	6.6
Paid during year	6.3	5.5	6.2
At 31 December 1999			
Balance	US\$m	US\$m	US\$m
	8,822	1,956	10,778
Highest aggregate month-end balance			11,455
Average borrowings	8,620	1,427	10,047
Weighted-average interest rate:	%	%	%
At year-end	5.6	5.6	5.6
Paid during year	5.2	5.0	5.2

Outstanding balances at 31 December 2001, 2000 and 1999 included commercial paper obligations of foreign subsidiaries of US\$375 million, US\$361 million and US\$359 million, respectively, and bank and other borrowings of US\$714 million, US\$722 million and US\$903 million, respectively.

Interest expense for commercial paper, bank and other borrowings totalled US\$463 million, US\$738 million and US\$522 million for 2001, 2000 and 1999 respectively.

Household maintains various bank credit agreements primarily to support commercial paper borrowings. At 31 December 2001, 2000 and 1999, Household had committed back-up lines and other bank lines of US\$13.6 billion, US\$13.0 billion and US\$12.6 billion, respectively, of which US\$12.8 billion, US\$12.3 billion and US\$11.4 billion, respectively, were unused. Formal credit lines are reviewed annually and expire at various dates from 2002 to 2006 (2000: 2001 to 2005) (1999: 2000 to 2004). Borrowings under these lines generally are available at a surcharge over LIBOR. None of these lines contain material adverse change clauses which could restrict availability. Annual commitment fee requirements to support availability of these lines at 31 December 2001 totalled US\$11 million, at 31 December 2000 totalled US\$9 million and at 31 December 1999 totalled US\$11 million.

9 Senior and senior subordinated debt (with original maturities over one year)

	At 31 December					
	2001		2000		1999	
	US\$m	Due 2002 to:	US\$m	Due 2001 to:	US\$m	Due 2000 to:
Senior debt						
Zero-coupon convertible debt securities: due 2021	1,004	—	—	—	—	—
3.50% to 4.99%	1,680	2009	12	2004	413	2004
5.00% to 6.49%	13,224	2013	10,169	2013	10,267	2013
6.50% to 6.99%	8,368	2013	4,204	2013	5,293	2013
7.00% to 7.49%	4,680	2023	4,959	2023	3,099	2023
7.50% to 7.99%	4,695	2019	4,174	2019	661	2012
8.00% to 8.99%	3,712	2010	3,892	2010	679	2008
9.00% and greater; due 2001	—	—	253	2001	429	2001
Variable interest rate debt; 1.89% to 3.53%	19,383	2034	—	—	—	—
Variable interest rate debt; 3.55% to 7.52%	—	—	17,244	2025	13,576	2019
Senior subordinated debt						
6.50% to 8.45%	179	2003	—	—	—	—
6.50% to 9.63%	—	—	260	2003	495	2003
Unamortised discount	(101)	—	(114)	—	(25)	—
Total senior and senior subordinated debt	56,824	—	45,053	—	34,887	—

Senior and senior subordinated debt included US\$1.5 billion of debt secured by US\$1.7 billion of real estate secured receivables at 31 December 2001. At 31 December 2000, senior and senior subordinated debt included US\$0.4 billion of debt secured by US\$0.4 billion of real estate secured receivables.

At 31 December 2001, senior and senior subordinated debt also included carrying value adjustments totalling US\$391 million relating to derivative financial instruments and a foreign currency translation adjustment of US\$(357) million relating to Household's foreign denominated debt.

Weighted-average interest rates were 5.1 per cent, 6.9 per cent and 6.4 per cent at 31 December 2001, 2000 and 1999 respectively. Interest expense for senior and senior subordinated debt was US\$3.2 billion, US\$2.7 billion and US\$2.1 billion for 2001, 2000 and 1999 respectively. The most restrictive financial covenant contained in the terms of Household's debt agreements are the maintenance of a minimum shareholders' equity of US\$2.0 billion for Household, and the maintenance of a minimum shareholder's equity of US\$3.6 billion (1999: US\$3.0 billion) for Household Finance Corporation ("HFC"), a wholly-owned subsidiary of Household. Debt denominated in a foreign currency is included in the applicable rate category based on the effective US dollar equivalent rate as summarised in Note 10.

In August 2001, the parent company issued zero-coupon convertible debt securities. The convertible debt securities are due 2021, have a 1 per cent yield to maturity and have a principal amount at maturity of approximately US\$1.2 billion. Household must pay contingent interest on the securities beginning in 2006 if Household's common stock price reaches certain levels. The possibility of contingent interest payments becoming payable does not begin until August 2006, and then only if Household's stock price reaches approximately US\$114.50 per share. The price level Household's common stock must reach for contingent interest to be paid will increase every year thereafter based on the accreted value of each debenture. The holders of the securities have the right to require Household to repurchase the securities on various dates beginning in August 2002 and ending in August 2016 or if certain "fundamental changes" as described in the prospectus supplement occur. Fundamental changes include, among other things, an exchange offer, liquidation, merger and re-capitalisation. The holders of the securities may convert each US\$1,000 of securities, subject to adjustment, into 9.022 shares of Household common stock if Household's stock price reaches US\$99.87 for 20 trading days in a consecutive 30 trading day period. Household may redeem the securities, in whole or in part, at any time after 1 August 2006.

Maturities of senior and senior subordinated debt were:

	At 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
2000			6,571
2001		8,278	6,044
2002	10,493	8,273	4,291
2003	9,980	6,576	4,125
2004	5,801	3,496	3,255
2005	5,970	5,342	—
2006	6,652	—	—
Thereafter	17,928	13,088	10,601
Total	56,824	45,053	34,887

10 Derivative financial instruments and concentrations of credit risk

In the normal course of business and in connection with Household's asset/liability management programme, Household enters into various transactions involving derivative financial instruments. These instruments primarily are used to manage Household's exposure to fluctuations in interest rates and currency exchange rates. Household does not serve as a financial intermediary to make markets in any derivative financial instruments. Household has a comprehensive programme to address potential financial risks such as liquidity, interest rate, currency and credit risk. The finance committee of the board of directors sets acceptable limits for each of these risks annually and reviews the limits semi-annually.

Objectives for holding derivative financial instruments. Household generally funds its assets with liabilities that have similar interest rate features. Over time, however, customer demand for Household's receivable products shifts between fixed rate and floating rate products, based on market conditions and preferences. These shifts result in different funding strategies and produce different interest rate risk exposures. Household maintains an overall risk management strategy that uses a variety of interest rate and currency derivative financial

instruments to mitigate Household's exposure to fluctuations caused by changes in interest rates and currency exchange rates. Household manages its exposure to interest rate risk primarily through the use of interest rate swaps, but also uses forwards, futures, options, and other risk management instruments. Household manages its exposure to currency risk primarily through the use of currency swaps. Household does not speculate on interest rate or foreign currency market exposure and Household does not use exotic or leveraged derivative financial instruments.

Interest rate swaps are contractual agreements between two counter-parties for the exchange of periodic interest payments generally based on a notional principal amount and agreed-upon fixed or floating rates. The majority of Household's interest rate swaps are used to manage Household's exposure to changes in interest rates by converting floating rate assets or debt to fixed rate or by converting fixed rate assets or debt to floating rate. Household has also entered into currency swaps to convert both principal and interest payments on debt issued from one currency to the appropriate functional currency.

Forwards and futures are agreements between two parties, committing one to sell and the other to buy a specific quantity of an instrument on some future date. The parties agree to buy or sell at a specified price in the future, and their profit or loss is determined by the difference between the arranged price and the level of the spot price when the contract is settled. Household has both interest rate and foreign exchange rate forward contracts and interest rate futures contracts. Household uses foreign exchange rate forward contracts to reduce its exposure to foreign currency exchange risk. Interest rate forward and futures contracts are used to hedge resets of interest rates on Household's floating rate assets and liabilities. Cash requirements for forward contracts include the receipt or payment of cash upon the sale or purchase of the instrument.

Purchased options grant the purchaser the right, but not the obligation, to either purchase or sell a financial instrument at a specified price within a specified period. The seller of the option has written a contract which creates an obligation to either sell or purchase the financial instrument at the agreed-upon price if, and when, the purchaser exercises the option. Household uses caps to limit the risk associated with an increase in rates and floors to limit the risk associated with a decrease in rates.

Market and credit risk. By utilising derivative financial instruments, Household is exposed to varying degrees of credit and market risk.

Market risk is the possibility that a change in interest rates or foreign exchange rates will cause a financial instrument to decrease in value or become more costly to settle. Household mitigates this risk by establishing limits for positions and other controls.

Credit risk is the possibility that a loss may occur because the counter-party to a transaction fails to perform according to the terms of the contract. Household controls the credit (or repayment) risk in derivative instruments through established credit approvals, risk control limits and ongoing monitoring procedures. Household's exposure to credit risk for futures is limited as these contracts are traded on organised exchanges. Each day, changes in futures contract values are settled in cash. In contrast, swap agreements and forward contracts have credit risk relating to the performance of the counterparty. Additionally, certain swap agreements require that payments be made to, or received from, the counterparty when the fair value of the agreement reaches a certain level. Derivative financial instruments are generally expressed in terms of notional principal or contract amounts which are much larger than the amounts potentially at risk for non-payment by counterparties. Household has never suffered a loss due to counterparty failure.

Fair value and cash flow hedges. To manage its exposure to changes in interest rates, Household enters into interest rate swap agreements and currency swaps which have been designated as fair value or cash flow hedges under FAS No. 133. The critical terms of interest rate swaps are designed to match those of the hedged items, enabling the application of the shortcut method of accounting as defined by FAS No. 133 for 92 per cent of the notional amounts of such interest rate swaps at 31 December 2001. To the extent that the critical terms of the hedged item and the derivative are not identical, hedge ineffectiveness is reported in earnings during the current period as a component of other income. Although the critical terms of currency swaps are designed to match those of the hedged items, FAS No. 133 does not allow shortcut method accounting for this type of hedge. Therefore, there may be minimal ineffectiveness which is reported in current period earnings.

Fair value hedges include interest rate swaps which convert Household's fixed rate debt or assets to variable rate debt or assets and currency swaps which convert debt issued from one currency into pay variable debt of the appropriate functional currency. Hedge ineffectiveness associated with fair value hedges was a gain of

US\$0.1 million, net of tax, in 2001 and was recorded as other income. During 2001, all Household's fair value hedges were associated with debt. At 31 December 2001, Household had recorded fair value adjustments for open fair value hedges which decreased the carrying value of its debt by US\$86 million.

Cash flow hedges include interest rate swaps which convert Household's variable rate debt or assets to fixed rate debt or assets and currency swaps which convert debt issued from one currency into pay fixed debt of the appropriate functional currency. At 31 December 2001, Household had US\$699 million of losses on derivative instruments designated as cash flow hedges, net of taxes, in accumulated other comprehensive income. Household expects US\$392 million of currently unrealised net losses, after taxes, will be reclassified to earnings within one year, however, these unrealised losses will be offset by decreased interest expense associated with the variable cash flows of the hedged items and will result in no net economic impact to Household's earnings. Hedge ineffectiveness associated with cash flow hedges reported in 2001 in the other income line was immaterial.

At 31 December 2001, US\$97 million of derivative instruments, at fair value, were recorded in other assets and US\$1,615 million in other liabilities.

Deferred gains resulting from termination of derivatives were US\$552 million and \$44 million and deferred losses from termination of derivatives were US\$72 million and US\$63 million at 31 December 2001 and 2000, respectively. Amortisation of net deferred gains totalled US\$44 million in 2001 and US\$15 million in 2000. The weighted-average amortisation period associated with the deferred gains was 6.2 years and 2.9 years at 31 December 2001 and 2000, respectively. The weighted-average amortisation period for the deferred losses was 5.3 years and 5.8 years at 31 December 2001 and 2000, respectively. At 31 December 2001, net deferred gains and losses increased the carrying value of Household's deposits and senior and senior subordinated debt by US\$25 million and US\$477 million, respectively, and decreased accumulated other comprehensive income by US\$22 million.

Hedges of net investments in foreign operations. Household uses forward foreign exchange contracts to hedge its net investments in foreign operations. The purpose of these hedges is to protect against adverse movements in exchange rates. For the year ended 31 December 2001, US\$9 million of net gains, net of tax, related to these derivatives were included in accumulated other comprehensive income.

Non-qualifying hedging activities. Household uses forward rate agreements, interest rate caps, exchange traded futures, and some interest rate swaps which were not designated as hedges under FAS No. 133. These financial instruments are economic hedges that are not linked to specific assets and liabilities that appear on Household's balance sheet and do not qualify for hedge accounting. The primary purpose of these derivatives is to minimise Household's exposure to changes in interest rates. During 2001, Household recognised US\$0.2 million, net of tax, in net fair value losses on derivatives which were not designated as hedges. These losses were reported as other income.

Derivative financial instruments

The following table summarises derivative financial instrument activity in 2001, 2000 and 1999:

	Exchange traded				Non-exchange traded						
	Interest rate futures contracts		Options		Interest rate swaps	Currency swaps	Foreign exchange rate contracts		Interest rate forward contracts		Caps and floors
	Purchased US\$m	Sold US\$m	Purchased US\$m	Written US\$m			Purchased US\$m	Sold US\$m	Purchased US\$m	Sold US\$m	
At 31 December 2001											
Notional amount, 2000	—	—	—	—	25,708	7,298	9	(245)	448	—	2,676
New contracts	36,675	(22,706)	4,750	—	22,259	2,482	9,347	(10,325)	2,074	—	3,482
Matured or expired contracts	(21,850)	300	—	—	(7,651)	(920)	(51)	173	(1,991)	—	(2,298)
Terminated contracts	—	—	(2,750)	—	(9,833)	(166)	—	—	(31)	—	(847)
In-substance maturities ¹	(13,406)	13,406	—	—	—	—	(9,196)	9,196	—	—	—
Notional amount, 2001 ...	1,419	(9,000)	2,000	—	30,483	8,694	109	(1,201)	500	—	3,013
Fair value, 2001 ² :											
Fair value hedges	—	—	—	—	(153)	67	—	—	—	—	—
Cash flow hedges	—	—	—	—	(348)	(1,085)	2	2	—	—	—
Non-hedging derivatives ...	1	(3)	1	—	3	—	—	(3)	(2)	—	—
Total	1	(3)	1	—	(498)	(1,018)	2	(1)	(2)	—	—
At 31 December 2000											
Notional amount, 1999	100	—	703	—	27,759	5,673	118	(698)	3,242	(69)	3,454
New contracts	21,715	(20,321)	1,300	(300)	15,451	3,047	1,829	(1,798)	4,158	(163)	2,551
Matured or expired contracts	(1,494)	—	(1,403)	—	(13,733)	(767)	(86)	399	(6,819)	232	(3,020)
Terminated contracts	—	—	(600)	300	(3,769)	(655)	—	—	(133)	—	(309)
In-substance maturities ¹	(20,321)	20,321	—	—	—	—	(1,852)	1,852	—	—	—
Notional amount, 2000 ...	—	—	—	—	25,708	7,298	9	(245)	448	—	2,676
Fair value, 2000 ²	—	—	—	—	259	(533)	—	(3)	—	—	(3)
At 31 December 1999											
Notional amount, 1998	70	—	544	—	13,716	4,406	10	(1,250)	2,262	(87)	3,038
New contracts	5,743	(4,725)	1,158	(50)	18,734	2,071	2,090	(1,479)	6,947	(1,242)	2,089
Matured or expired contracts	(1,013)	25	(949)	—	(2,895)	(724)	(117)	171	(5,759)	667	(442)
Terminated contracts	—	—	—	—	(1,796)	(80)	(19)	14	(208)	593	(1,231)
In-substance maturities ¹	(4,700)	4,700	(50)	50	—	—	(1,846)	1,846	—	—	—
Notional amount, 1999 ...	100	—	703	—	27,759	5,673	118	(698)	3,242	(69)	3,454
Fair value, 1999 ²	—	—	—	—	(125)	(319)	—	5	6	—	5

¹ Represent contracts terminated as the market execution technique of closing the transaction either (a) just prior to maturity to avoid delivery of the underlying instrument or (b) at the maturity of the underlying items being hedged.

² (Bracketed)/unbracketed amounts represent amounts to be (paid)/received by Household had these positions been closed out at the respective balance sheet date. Bracketed amounts do not necessarily represent risk of loss as the fair value of the derivative financial instrument and the items being hedged must be evaluated together. See Note 14, "Fair Value of Financial Instruments," for further discussion of the relationship between the fair value of Household's assets and liabilities.

Household operates in three functional currencies, the US dollar, the pound sterling and the Canadian dollar. The US dollar is the functional currency for exchange-traded interest rate futures contracts and options. Non-exchange traded instruments are restated in US dollars by country as follows:

			Foreign exchange rate contracts		Interest rate forward contracts		Other risk management instructions US\$m
	Interest rate swaps US\$m	Currency swaps US\$m	Purchased US\$m	Sold US\$m	Purchased US\$m	Sold US\$m	
At 31 December 2001							
United States	28,405	7,260	109	(1,199)	—	—	2,990
Canada	287	—	—	(2)	500	—	—
United Kingdom	1,791	1,434	—	—	—	—	23
	30,483	8,694	109	(1,201)	500	—	3,013
At 31 December 2000							
United States	23,734	5,752	7	(245)	—	—	2,353
Canada	275	121	2	—	314	—	—
United Kingdom	1,699	1,425	—	—	134	—	323
	25,708	7,298	9	(245)	448	—	2,676
At 31 December 1999							
United States	25,917	4,258	113	(698)	—	—	2,702
Canada	374	223	5	—	246	(67)	—
United Kingdom	1,468	1,192	—	—	2,996	(2)	752
	27,759	5,673	118	(698)	3,242	(69)	3,454

The table below reflects the items hedged using derivative financial instruments which qualify for hedge accounting at 31 December 2001. The critical terms of the interest rate swap have been designed to match those of the related asset or liability.

	Interest rate swaps US\$m	Currency swaps US\$m	Foreign exchange rate contracts US\$m	Total US\$m
At 31 December 2001				
Investment securities	17	—	—	17
Commercial paper, bank and other borrowings	618	—	—	618
Senior and senior subordinated debt	29,848	8,694	—	38,542
Investment in foreign operations	—	—	(605)	(605)
Total items hedged using derivative financial instruments	30,483	8,694	(605)	38,572

Interest rate swaps are contractual agreements between two counterparties for the exchange of periodic interest payments generally based on a notional principal amount and agreed-upon fixed or floating rates. Household primarily enters into interest rate swap transactions to synthetically alter balance sheet items. These transactions are specifically designated to a particular asset/liability, off-balance sheet item or anticipated transaction of a similar characteristic. Specific assets or liabilities may consist of homogeneous groups of individually small dollar assets or liabilities of similar economic characteristics. Credit and market risk exists with respect to these instruments. The following table reflects the items so altered.

	At 31 December	
	2000 US\$m	1999 US\$m
Investment securities	30	37
Receivables: Home equity	—	4,290
Private label	—	12
Other unsecured	—	16
Total owned receivables	—	4,318
Commercial paper, bank and other borrowings	3,502	1,234
Senior and senior subordinated debt	22,176	10,925
Receivables serviced with limited recourse	—	11,245
Total items synthetically altered with interest rate swaps	25,708	27,759

In all instances, the notional amount is not greater than the carrying value of the related asset/liability or off-balance sheet item.

Household manages its exposure to interest rate risk primarily through the use of interest rate swaps. These swaps synthetically alter the interest rate risk inherent in balance sheet assets, liabilities or off-balance sheet items. The majority of Household's interest rate swaps are used to convert floating rate assets to fixed rate, fixed rate debt to floating rate, floating rate assets or debt from one floating rate index to another, fixed rate assets to a floating rate,

or floating rate debt to fixed rate. Interest rate swaps also are used to synthetically alter interest rate characteristics on certain receivables that are sold and serviced with limited recourse. These off-balance sheet items expose Household to the same interest rate risk as on-balance sheet items. Interest rate swaps are used to synthetically alter the interest rate provisions of the securitisation transactions whereby the underlying receivables pay a fixed (floating) rate and the pass-through rate to the investor is floating (fixed). Household has also entered into currency swaps to convert both principal and interest payments on issued debt from one currency to the appropriate functional currency.

The following table summarises the maturities and related weighted-average receive/pay rates of interest rate swaps outstanding:

At 31 December 2001	2002	2003	2004	2005	2006	2007	Thereafter	Total
Pay a fixed rate/receive a floating rate:								
Notional value (US\$m)	9,956	8,229	763	1,040	—	—	—	19,988
Weighted-average receive rate	2.18%	2.44%	2.91%	3.62%	—	—	—	2.39%
Weighted-average pay rate	5.47%	4.99%	5.20%	6.02%	—	—	—	5.29%
Pay a floating rate/receive a fixed rate:								
Notional value (US\$m)	96	—	10	248	140	1,479	8,522	10,495
Weighted-average receive rate	6.69%	—	4.96%	5.91%	5.88%	7.45%	6.67%	6.75%
Weighted-average pay rate	2.09%	—	2.04%	2.60%	2.18%	3.92%	3.32%	3.36%
Total notional value (US\$m)	10,052	8,229	773	1,288	140	1,479	8,522	30,483
Total weighted-average rates on swaps:								
Receive rate	2.23%	2.44%	2.93%	4.06%	5.88%	7.45%	6.67%	3.89%
Pay rate	5.44%	4.99%	5.15%	5.37%	2.18%	3.92%	3.32%	4.63%
At 31 December 2000	2001	2002	2003	2004	2005	2006	Thereafter	Total
Pay a fixed rate/receive a floating rate:								
Notional value (US\$m)	6,638	6,379	2,075	261	709	45	—	16,107
Weighted-average receive rate	6.69%	6.78%	6.67%	6.06%	6.07%	6.07%	—	6.68%
Weighted-average pay rate	6.47%	6.87%	6.65%	6.88%	6.60%	6.60%	—	6.67%
Pay a floating rate/receive a fixed rate:								
Notional value (US\$m)	140	102	158	907	124	1,418	6,252	9,101
Weighted-average receive rate	6.21%	6.66%	6.32%	6.23%	6.71%	7.10%	6.97%	6.89%
Weighted-average pay rate	6.73%	6.76%	6.52%	7.01%	6.58%	7.04%	6.95%	6.95%
Pay a floating rate/receive a different floating rate:								
Notional value (US\$m)	500	—	—	—	—	—	—	500
Weighted-average receive rate	6.47%	—	—	—	—	—	—	6.47%
Weighted-average pay rate	6.79%	—	—	—	—	—	—	6.79%
Total notional value (US\$m)	7,278	6,481	2,233	1,168	833	1,463	6,252	25,708
Total weighted-average rates on swaps:								
Receive rate	6.66%	6.78%	6.65%	6.19%	6.16%	7.07%	6.97%	6.75%
Pay rate	6.50%	6.87%	6.64%	6.98%	6.60%	7.02%	6.95%	6.77%
At 31 December 1999	2000	2001	2002	2003	2004	2005	Thereafter	Total
Pay a fixed rate/receive a floating rate:								
Notional value (US\$m)	1,844	4,855	1,296	1,324	226	178	—	9,723
Weighted-average receive rate	6.24%	6.28%	6.19%	6.34%	6.28%	6.28%	—	6.27%
Weighted-average pay rate	6.31%	6.04%	6.27%	6.02%	6.87%	7.17%	—	6.16%
Pay a floating rate/receive a fixed rate:								
Notional value (US\$m)	199	224	260	100	1,214	100	4,597	6,694
Weighted-average receive rate	6.78%	6.52%	6.15%	6.50%	5.91%	6.86%	6.44%	6.35%
Weighted-average pay rate	5.94%	6.12%	5.53%	5.60%	6.10%	6.11%	6.10%	6.06%
Pay a floating rate/receive a different floating rate:								
Notional value (US\$m)	8,337	500	2,505	—	—	—	—	11,342
Weighted-average receive rate	6.36%	6.11%	6.00%	—	—	—	—	6.27%
Weighted-average pay rate	5.73%	5.63%	5.88%	—	—	—	—	5.76%
Total notional value (US\$m)	10,380	5,579	4,061	1,424	1,440	278	4,597	27,759
Total weighted-average rates on swaps:								
Receive rate	6.35%	6.27%	6.07%	6.35%	5.97%	6.49%	6.44%	6.29%
Pay rate	5.83%	6.00%	5.98%	5.99%	6.22%	6.79%	6.10%	5.97%

The floating rates that Household pays or receives are based on spot rates from independent market sources for the index contained in each interest rate swap contract, which generally are based on either 1-month, 3-month or 6-month LIBOR. These current floating rates are different to the floating rates in effect when the contracts were initiated. Changes in spot rates impact the variable rate information disclosed above. However, these changes in spot rates also impact the interest rates on the underlying assets or liabilities. Household uses derivative financial instruments to hedge the interest rates inherent in balance sheet assets and liabilities, which manages the volatility of net interest margin resulting from changes in interest rates on the underlying hedged items. Had Household not

utilised these instruments, owned net interest margin would have increased by 13 basis points in 2001, decreased by 5 basis points in 2000 and increased by 1 basis point in 1999.

Forwards and futures are agreements between two parties, committing one to sell and the other to buy a specific quantity of an instrument on some future date. The parties agree to buy or sell at a specified price in the future, and their profit or loss is determined by the difference between the arranged price and the level of the spot price when the contract is settled. Household has both interest rate and foreign exchange rate forward contracts and interest rate futures contracts. Household uses foreign exchange contracts to reduce its exposure to foreign currency exchange risk. Interest rate forward and futures contracts are used to hedge resets of interest rates on its floating rate assets and liabilities. Household's exposures to credit risk for futures is limited, as these contracts are traded on organised exchanges. Each day, changes in contract values are settled in cash. In contrast, forward contracts have credit risk relating to the performance of the counterparty. These instruments also are subject to market risk. Cash requirements for forward contracts include the receipt or payment of cash upon the sale or purchase of the instrument. Purchased options grant the purchaser the right, but not the obligation, to either purchase or sell a financial instrument at a specified price within a specified period. The seller of the option has written a contract which creates an obligation to either sell or purchase the financial instrument at the agreed-upon price if, and when, the purchaser exercises the option. Other risk management instruments consist of caps and floors. Written caps and floors expose Household to market risk but not to credit risk. Market risk associated with purchased caps and floors is limited to the premium paid which is recorded on the balance sheet in other assets.

Deferred gains of US\$44 million and US\$51 million and deferred losses of US\$63 million and US\$2 million from hedging/synthetic alteration instruments were recorded on the balance sheet at 31 December 2000 and 1999, respectively. The weighted-average amortisation period associated with the deferred gains was 2.9 years and 4.0 years at 31 December 2000 and 1999, respectively. The weighted-average amortisation period for the deferred losses was 5.8 years and 1.2 years at 31 December 2000 and 1999, respectively.

At 31 December, 2000 and 1999, the accrued interest, unamortised premium and other assets recorded for agreements which would be written off should all related counterparties fail to meet the terms of their contracts were US\$84 million and US\$49 million, respectively.

Concentrations of credit risk. A concentration of credit risk is defined as a significant credit exposure with an individual or group engaged in similar activities or affected similarly by economic conditions.

Because Household primarily lends to consumers, Household does not have receivables from any industry group that equal or exceed 10 per cent of total managed receivables at 31 December 2001, 2000 or 1999. Household lends nationwide, with the following geographic areas comprising more than 10 per cent of total managed domestic receivables.

- 31 December 2001: California – 15 per cent; Southwest – 11 per cent; Midwest – 22 per cent; Middle Atlantic – 14 per cent; Northeast – 11 per cent; and Southeast – 18 per cent.
- 31 December 2000: California – 16 per cent; Southwest – 11 per cent; Midwest – 22 per cent; Middle Atlantic – 14 per cent; Northeast – 11 per cent; and Southeast – 18 per cent.
- 31 December 1999: California – 17 per cent; Southwest – 10 per cent; Midwest – 21 per cent; Middle Atlantic – 15 per cent; Northeast – 12 per cent; and Southeast – 16 per cent.

11 Company obligated mandatorily redeemable preferred securities of subsidiary trusts

The following table summarises Household's company obligated mandatorily redeemable preferred securities of subsidiary trusts ("preferred securities") and the related junior subordinated notes:

	Household Capital Trust VII ("HCT VII")	Household Capital Trust VI ("HCT VI")	Household Capital Trust V ("HCT V")	Household Capital Trust IV ("HCT IV")	Household Capital Trust I ("HCT I")
At 31 December 2001					
Preferred securities:					
Interest rate	7.50%	8.25%	10.00%	7.25%	8.25%
Face value (US\$m)	200	200	300	200	75
Issue date	November 2001	January 2001	June 2000	March 1998	June 1995
Junior subordinated notes:					
Principal balance (US\$m)	206	206	309	206	77
Redeemable by issuer	8 November 2006	30 January 2006	8 June 2005	19 March 2003	30 June 2000
Stated maturity	15 November 2031	30 January 2031	30 June 2030	31 December 2037	30 June 2025
		Household Capital Trust V ("HCT V")	Household Capital Trust IV ("HCT IV")	Household Capital Trust II ("HCT II")	Household Capital Trust I ("HCT I")
At 31 December 2000					
Preferred securities:					
Interest rate		10.00%	7.25%	8.70%	8.25%
Face value (US\$m)		300	200	100	75
Issue date		June 2000	March 1998	June 1996	June 1995
Junior subordinated notes:					
Principal balance (US\$m)		309	206	103	77
Redeemable by issuer		8 June 2005	19 March 2003	30 June 2001	30 June 2000
Stated maturity		30 June 2030	31 December 2037	30 June 2036	30 June 2025
			Household Capital Trust IV ("HCT IV")	Household Capital Trust II ("HCT II")	Household Capital Trust I ("HCT I")
At 31 December 1999					
Preferred securities:					
Interest rate			7.25%	8.70%	8.25%
Face value (US\$m)			200	100	75
Issue date			March 1998	June 1996	June 1995
Junior subordinated notes:					
Principal balance (US\$m)			206	103	77
Redeemable by issuer			19 March 2003	30 June 2001	30 June 2000
Stated maturity			31 December 2037	30 June 2036	30 June 2025

The preferred securities are classified in Household's balance sheet as company obligated mandatorily redeemable preferred securities of subsidiary trusts (representing the minority interests in the trusts) at their face and redemption amounts of US\$975 million at 31 December 2001, US\$675 million at 31 December 2000 and US\$375 million at 31 December 1999. Household Capital Trust II was redeemed for US\$100 million in December 2001.

The preferred securities must be redeemed when the junior subordinated notes are paid. The junior subordinated notes have a stated maturity date, but are redeemable by Household, in whole or in part, beginning on the dates indicated above at which time the preferred securities are callable at par (US\$25 per preferred security) plus accrued and unpaid dividends. Dividends on the preferred securities are cumulative, payable quarterly in arrears, and are deferrable at Household's option for up to five years. Household cannot pay dividends on its preferred and common stocks during such deferments. The preferred securities have a liquidation value of US\$25 per preferred security.

HCT I, HCT IV, HCT V, HCT VI and HCT VII (collectively, "the Trusts") are wholly owned subsidiaries of Household. Household's obligations with respect to the junior subordinated notes, when considered together with certain undertakings of Household with respect to the Trusts, constitute full and unconditional guarantees by Household of the Trusts' obligations under the respective preferred securities.

12 Preferred stock

	At 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
7.50 % Preferred stock, 12,000,000 depositary shares ¹	292	—	—
US\$4.30 Preferred stock, 836,585 shares	84	84	84
US\$4.50 Preferred stock, 103,976 shares	10	10	10
5.00 % Preferred stock, 407,718 shares	20	20	20
8.25% Preferred stock, Series 1992-A, 2,000,000 depositary shares ¹	50	50	50
Total preferred stock	456	164	164

¹ Depositary share represents 1/40 share of preferred stock.

Dividends on the 7.50 per cent Household preferred stock are cumulative and payable quarterly. Household may, at its option, redeem in whole or in part the 7.50 per cent preferred stock on any date after 26 September 2006, for US\$25 per depositary share plus accrued and unpaid dividends. This stock has a liquidation value of US\$25 per depositary share.

Dividends on the US\$4.30 Household preferred stock are cumulative and payable semi-annually. Household may, at its option, redeem in whole or in part the US\$4.30 preferred stock for US\$100 per share plus accrued and unpaid dividends. This stock has a liquidation value of US\$100 per share plus accrued and unpaid dividends in the event of an involuntary liquidation or US\$100 in the event of a voluntary liquidation.

Dividends on the US\$4.50 Household preferred stock are cumulative and payable semi-annually. Household may, at its option, redeem in whole or in part the US\$4.50 preferred stock for US\$103 per share plus accrued and unpaid dividends. This stock has a liquidation value of US\$100 per share.

Dividends on the 5.00 per cent Household preferred stock are cumulative and payable semi-annually. Household may, at its option, redeem in whole or in part the 5.00 per cent preferred stock for US\$50 per share plus accrued and unpaid dividends. This stock has a liquidation value of US\$50 per share.

Dividends on the 8.25 per cent Household preferred stock, Series 1992-A, are cumulative and payable quarterly. Household may, at its option, redeem in whole or in part the 8.25 per cent preferred stock, Series 1992-A, on any date after 15 October 2002, for US\$25 per depositary share plus accrued and unpaid dividends. This stock has a liquidation value of US\$25 per depositary share.

Holders of all issues of Household preferred stock are entitled to payment before any capital distribution is made to common shareholders. The holders of the US\$4.30, US\$4.50 and 5.00 per cent Household preferred stocks will be entitled to vote with the holders of Household's common stock on all matters. Each issue of Household preferred stock is also entitled to vote, as a class separate from Household's common stock, to elect two directors if dividends for a specified period shall be in arrears, until the dividends in arrears are paid in full.

Household's board of directors has adopted a resolution creating an offering committee of the board with the power to authorise the issue and sale of one or more series of Household preferred stock. The offering committee has the authority to determine the particular designations, powers, preferences and relative, participating, optional or other special rights (other than voting rights which shall be fixed by the board of directors) and qualifications, limitations or restrictions of such issue.

At 31 December 2001, up to 8.2 million shares of Household preferred stock were authorised for issue. At 31 December 2000 and 1999, up to 8.2 million and 2.6 million of shares of Household preferred stock were authorised for issue respectively.

13 Forward purchase agreements and junior preferred share purchase rights

At 31 December 2001, Household had agreements to purchase, on a forward basis, approximately 6.5 million shares of its common stock at a weighted-average forward price of US\$59.14 per share. The agreements have terms of up to one year. These agreements may be settled either physically or on a net basis in shares of Household's common stock, at Household's option. Household accounts for these agreements in accordance with EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled In, a Company's Own Stock". As a result, Household initially measures these forward contracts at fair value and reports them as permanent equity. Subsequent changes in their fair value are not recognised.

In 1996, Household issued one preferred share purchase right (a “Right”) for each outstanding share of Household common stock. Under certain conditions, each Right may be exercised to purchase one three thousandth of a share of a new series of junior participating Household preferred stock at an exercise price of US\$100 per one three-thousandth of a share, subject to further adjustment. The Rights may be exercised only after the earlier of: (a) a public announcement that a party or an associated group acquired 15 per cent or more of Household’s common stock; and (b) ten business days (or later date as determined by the board of directors of Household) after a party or an associated group initiates or announces its intention to make an offer to acquire 15 per cent or more of Household’s common stock. The Rights, which cannot vote or receive dividends, expire on 31 July 2006, and may be redeemed by Household at a price of US\$.0033 per Right at any time prior to expiration or acquisition of 15 per cent of Household’s common stock.

14 Fair value of financial instruments

Household has estimated the fair value of its financial instruments in accordance with FAS No. 107, “Disclosures About Fair Value of Financial Instruments”. Fair value estimates, methods and assumptions set forth below for Household’s financial instruments are made solely to comply with the requirements of FAS No. 107 and should be read in conjunction with the financial statements and notes in this annual report.

A significant portion of Household’s financial instruments do not have a quoted market price. For these items, fair values were estimated by discounting estimated future cash flows at estimated current market discount rates. Assumptions used to estimate future cash flows are consistent with management’s assessments regarding ultimate collectibility of assets and related interest and with estimates of product lives and re-pricing characteristics used in Household’s asset/liability management process. All assumptions are based on historical experience adjusted for future expectations. Assumptions used to determine fair values for financial instruments for which no active market exists are inherently judgmental and changes in these assumptions could significantly affect fair value calculations.

As required under US GAAP, a number of other assets recorded on the balance sheet (such as acquired credit card relationships) and other intangible assets not recorded on the balance sheet (such as the value of consumer lending relationships for originated receivables and the franchise values of Household’s business units) are not considered financial instruments and, accordingly, are not valued for purposes of this disclosure. Household believes there is substantial value associated with these assets based on current market conditions and historical experience. Accordingly, the estimated fair value of financial instruments, as disclosed, does not fully represent Household’s entire value, nor the changes in Household’s entire value.

The following is a summary of the carrying value and estimated fair value of Household’s financial instruments:

	At 31 December								
	2001			2000			1999		
	Carrying value US\$m	Estimated fair value US\$m	Difference US\$m	Carrying value US\$m	Estimated fair value US\$m	Difference US\$m	Carrying value US\$m	Estimated fair value US\$m	Difference US\$m
Assets:									
Cash	544	544	—	490	490	—	270	270	—
Investment securities	3,581	3,581	—	3,259	3,259	—	3,128	3,128	—
Receivables	79,263	81,219	1,956	67,162	67,673	511	52,158	52,460	302
Total	83,388	85,344	1,956	70,911	71,422	511	55,556	55,858	302
Liabilities:									
Deposits	(6,562)	(6,839)	(277)	(8,677)	(8,692)	(15)	(4,980)	(4,906)	74
Commercial paper, bank and other borrowings	(12,024)	(12,024)	—	(10,788)	(10,788)	—	(10,778)	(10,778)	—
Senior and senior subordinated debt	(56,824)	(58,327)	(1,503)	(45,053)	(44,638)	415	(34,887)	(34,107)	780
Insurance reserves	(1,095)	(1,346)	(251)	(1,107)	(1,337)	(230)	(1,309)	(1,472)	(163)
Total	(76,505)	(78,536)	(2,031)	(65,625)	(65,455)	170	(51,954)	(51,263)	691
Other:									
Derivative financial instruments ..	(1,518)	(1,518)	—	80	(280)	(360)	41	(428)	(469)
Commitments to extend credit and guarantees	—	51	51	—	49	49	—	49	49
Total	(1,518)	(1,467)	51	80	(231)	(311)	41	(379)	(420)
Total	5,365	5,341	(24)	5,366	5,736	370	3,643	4,216	573

Cash. Carrying value approximates fair value due to the liquid nature of cash.

Investment securities. Investment securities are classified as available-for-sale and are carried at fair value on the balance sheet. Fair values are based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Receivables. The fair value of variable rate receivables approximates carrying value because interest rates on these receivables vary with changing market interest rates. The fair value of fixed rate consumer receivables was estimated by discounting future expected cash flows at interest rates which approximate the rates that would achieve a similar return on assets with comparable risk characteristics.

Receivables also include Household's interest-only strip receivables. The interest-only strip receivables are carried at fair value on Household's balance sheet. Fair value is based on an estimate of the present value of future cash flows associated with securitisations of certain real estate secured, auto finance, MasterCard and Visa, private label and personal non-credit card receivables.

Deposits. The fair value of Household's savings and demand accounts equaled the carrying amount as stipulated in FAS No. 107. The fair value of gross fixed-rate time certificates was estimated by discounting future expected cash flows at interest rates that Household offer on such products at the respective valuation dates.

Commercial paper, bank and other borrowings. The fair value of these instruments approximates their existing carrying value because interest rates on these instruments adjust with changes in market interest rates due to their short-term maturity or re-pricing characteristics.

Senior and senior subordinated debt. The estimated fair value of Household's gross fixed-rate debt instruments was determined either by using quoted market prices or by discounting future expected cash flows at interest rates offered for similar types of debt instruments. Carrying value is typically used to estimate the fair value of floating rate debt.

Insurance reserves. The fair value of insurance reserves for periodic payment annuities was estimated by discounting future expected cash flows at estimated market interest rates at 31 December 2001, 2000 and 1999. The fair value of other insurance reserves is not required to be determined in accordance with FAS No. 107.

Derivative financial instruments. From 1 January 2001, all derivative financial instruments are carried at fair value on the balance sheet. Where practical, quoted market prices were used to determine the fair value of these instruments. For non-exchange traded contracts, fair value was determined using accepted and established valuation methods (including input from independent third parties) which consider the terms of the contracts and market expectations on the valuation date for forward interest rates (for interest rate contracts) or forward foreign currency exchange rates (for foreign exchange contracts). Household enters into foreign exchange contracts to hedge its exposure to currency risk on foreign denominated debt. Household also enters into interest rate contracts to hedge its exposure to interest rate risk on assets and liabilities, including debt. As a result, decreases/increases in the fair value of derivative financial instruments which have been designated as effective hedges are offset by a corresponding increase/decrease in the fair value of the individual asset or liability being hedged. See Note 10, "Derivative financial instruments and concentrations of credit risk," for additional discussion of the nature of these items.

Commitments to extend credit and guarantees. These commitments were valued by considering Household's relationship with the counterparty, the creditworthiness of the counterparty and the difference between committed and current interest rates.

15 Leases

Household leases certain offices, buildings and equipment for periods of up to 25 years. The leases expire at various dates to 2019 and have various renewal options. The office space leases generally require Household to pay certain operating expenses. Net rental expense under operating leases was US\$125 million in 2001, US\$108 million in 2000 and US\$89 million in 1999.

Future net minimum lease commitments under non-cancellable operating lease arrangements were:

	Minimum rental payments US\$m	Minimum sublease income US\$m	Net US\$m
At 31 December 2001			
Net minimum lease commitments for 2002	151	21	130
Net minimum lease commitments for 2003	129	22	107
Net minimum lease commitments for 2004	111	22	89
Net minimum lease commitments for 2005	92	22	70
Net minimum lease commitments for 2006	82	22	60
Net minimum lease commitments thereafter	330	78	252
Net minimum lease commitments	895	187	708
At 31 December 2000			
Net minimum lease commitments for 2001	139	23	116
Net minimum lease commitments for 2002	126	24	102
Net minimum lease commitments for 2003	112	23	89
Net minimum lease commitments for 2004	93	23	70
Net minimum lease commitments for 2005	78	22	56
Net minimum lease commitments thereafter	342	99	243
Net minimum lease commitments	890	214	676
At 31 December 1999			
Net minimum lease commitments for 2000	118	23	95
Net minimum lease commitments for 2001	107	23	84
Net minimum lease commitments for 2002	94	23	71
Net minimum lease commitments for 2003	84	23	61
Net minimum lease commitments for 2004	81	22	59
Net minimum lease commitments thereafter	338	120	218
Net minimum lease commitments	822	234	588

Household has a lease obligation on a facility located in Peapack, New Jersey, United States, expiring in 2010, arising from its 1998 merger with Beneficial. At 31 December 2001 this facility was subleased to the end of the lease period with the sublessor assuming Household's future rental obligations.

16 Incentive compensation and stock option plans

Household's executive compensation plans provide for issuance of non-qualified stock options and restricted stock rights ("RSRs"). Stock options permit the holder to purchase, under certain limitations, Household's common stock at the market value of the stock on the date the option is granted. Employee stock options generally vest equally over four years and expire 10 years from the date of grant. RSRs entitle an employee to receive a stated number of shares of Household's common stock if the employee satisfies the conditions set by the compensation committee for the award. A total of 4.3 million, 4.0 million and 2.0 million RSRs were outstanding at 31 December 2001, 2000 and 1999, respectively. Total compensation cost recognised for RSRs was US\$45 million, US\$24 million and US\$12 million in 2001, 2000 and 1999, respectively. Shares of Household's common stock reserved for stock plans were 34.9 million at 31 December 2001 and 38.9 million at 31 December 2000.

Non-employee directors annually receive options to purchase shares of Household's common stock at the stock's fair market value on the day the option is granted. Director options have a term of ten years and one day, fully vest six months from the date granted, and once vested are exercisable at any time during the option term.

Common stock data for the stock option plans is summarised as follows:

	At 31 December					
	2001		2000		1999	
	Shares	Weighted average price per share US\$	Shares	Weighted average price per share US\$	Shares	Weighted average price per share US\$
Outstanding at beginning of year	16,687,142	31.09	16,068,326	26.30	21,600,569	21.14
Granted	3,080,400	57.16	2,812,469	48.80	2,311,500	44.78
Exercised	(2,015,723)	17.26	(2,056,064)	12.89	(7,805,549)	17.48
Expired or cancelled	(1,535)	28.22	(137,589)	36.84	(38,194)	31.45
Outstanding at end of year	17,750,284	37.19	16,687,142	31.09	16,068,326	26.30
Exercisable at end of year	11,502,384	29.44	11,134,642	24.10	11,023,619	19.64
Weighted average fair value of options granted		18.25		19.65		19.65

The following table summarises information about stock options outstanding:

	Options outstanding			Options exercisable	
	Number outstanding	Weighted average remaining life	Weighted average exercise price US\$	Number outstanding	Weighted average exercise price US\$
Range of Exercise Prices					
At 31 December 2001					
US\$6.65-US\$10.00	303,089	.54 years	8.25	303,089	8.25
US\$10.01-US\$20.00	4,000,974	2.85 years	14.28	4,000,225	14.27
US\$20.01-US\$30.00	491,185	5.46 years	24.02	489,959	24.01
US\$30.01-US\$40.00	4,887,188	6.13 years	36.12	4,367,938	36.07
US\$40.01-US\$50.00	4,957,448	8.28 years	47.33	2,318,673	46.83
US\$50.01-US\$57.16	3,110,400	9.84 years	57.10	22,500	51.38
At 31 December 2000					
US\$6.65-US\$25.90	6,407,604	3.8 years	14.52	6,407,163	14.52
US\$28.22-US\$51.38	10,279,538	8.1 years	41.42	4,727,479	37.09
At 31 December 1999					
US\$6.65-US\$25.90	8,163,682	4.6 years	14.18	8,155,434	14.18
US\$28.22-US\$51.38	7,904,644	8.5 years	38.81	2,868,185	35.17

Household maintains an Employee Stock Purchase Plan (the “ESPP”). The ESPP provides a means for employees to purchase shares of Household’s common stock at 85 per cent of the lesser of its market price at the beginning or end of a one-year subscription period.

Household accounts for options and shares issued under the ESPP in accordance with APB 25, pursuant to which no compensation cost has been recognised. Had compensation cost been determined consistent with FAS No. 123, “Accounting for stock-based compensation,” Household’s net income and earnings per share, on a pro-forma basis, would have been as follows:

	Year ended 31 December					
	2001		2000		1999	
	Diluted US\$m	Basic US\$m	Diluted US\$m	Basic US\$m	Diluted US\$m	Basic US\$m
Earnings available to common shareholders:						
As reported	1,832	1,832	1,621	1,621	1,419	1,419
Pro-forma	1,804	1,804	1,600	1,600	1,403	1,403
Earnings per share:	US\$	US\$	US\$	US\$	US\$	US\$
As reported	3.91	3.97	3.40	3.44	2.95	2.98
Pro-forma	3.85	3.91	3.36	3.39	2.91	2.94

The pro-forma compensation expense included in the table above may not be representative of the actual effects on net income for future years.

The fair value of each option granted was estimated as at the date of grant using the Black-Scholes option pricing model and the following weighted-average assumptions:

	Year ended 31 December		
	2001	2000	1999
Risk-free interest rate	3.62%	5.74%	5.84%
Expected dividend yield	1.44	1.49	1.65
Expected volatility	34.3%	42.8%	46.9%
Expected life	5 years	5 years	5 years

The Black-Scholes model uses different assumptions that can significantly affect the fair value of the options. As a result, the derived fair value estimates cannot be substantiated by comparison to independent markets.

17 Employee benefit plans

Household sponsors several defined benefit pension plans covering substantially all of its US and non-US employees. At 31 December 2001, plan assets included an investment in 1,112,546 shares of Household's common stock with a fair value of US\$65 million. At 31 December 2000 and 1999 the plan assets included investments in 2,480,910 shares and 3,542,155 shares of Household's common stock respectively with fair values of US\$137 million and US\$132 million respectively.

Pension income for defined benefit plans, primarily due to the over funded status of the domestic plan, included the following components:

	Year ended 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Service cost benefits earned during the year	(27)	(23)	(29)
Interest cost on projected benefit obligation	(37)	(33)	(31)
Expected return on assets	101	88	81
Amortisation of transition asset	1	1	1
Recognised gains	—	—	4
Pension income	38	33	26

The assumptions used in determining the benefit obligation and pension income of the domestic defined benefit plans at 31 December were as follows:

	Year ended 31 December		
	2001 %	2000 %	1999 %
Discount rate	7.5	8.25	8.0
Salary increase assumption	4.0	4.0	4.0
Expected long-term rate of return on plan assets	10.0	10.0	10.0

A reconciliation of beginning and ending balances of the projected benefit obligation of the defined benefit pension plans is as follows:

	Year ended 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Benefit obligation at beginning of year	555	548	567
Service cost	27	23	29
Interest cost	38	33	31
Actuarial losses	112	15	1
Foreign currency exchange rate changes	(3)	(5)	2
Plan amendments	9	—	(2)
Benefits paid	(60)	(59)	(80)
Benefit obligation at end of year	678	555	548

A reconciliation of beginning and ending balances of the fair value of plan assets associated with the defined benefit pension plans is as follows:

	Year ended 31 December		
	2001	2000	1999
	US\$m	US\$m	US\$m
Fair value of plan assets at beginning of year	1,059	927	822
Actual return on plan assets.....	(137)	195	181
Foreign currency exchange rate changes.....	(3)	(5)	2
Employer contributions	1	1	1
Benefits paid	(60)	(59)	(80)
Fair value of plan assets at end of year.....	860	1,059	926

The funded status of defined benefit pension plans was as follows:

	At 31 December		
	2001	2000	1999
	US\$m	US\$m	US\$m
Funded status.....	182	504	378
Unrecognised net actuarial loss/(gain)	257	(98)	(3)
Unamortised prior service cost	4	(6)	(7)
Prepaid pension cost.....	443	400	368

Household also sponsors a non-qualified supplemental retirement plan. This plan, which is unfunded, provides eligible employees defined pension benefits outside the qualified retirement plan based on average earnings, years of service and age at retirement. At 31 December 2001 and 2000, the projected benefit obligation was US\$41 million and US\$29 million, respectively. Pension expense related to the supplemental retirement plan was US\$10 million, US\$5 million and US\$7 million in 2001, 2000 and 1999, respectively.

Household also sponsors various 401(k) savings plans and profit sharing plans for employees meeting certain eligibility requirements. Under these plans, each participant's contribution is matched by the company in Household common stock up to a maximum of 6 per cent of the participant's compensation. For 2001, 2000 and 1999, total expense for these plans was US\$57 million, US\$47 million and US\$39 million, respectively.

Household has several plans which provide medical, dental and life insurance benefits to retirees and eligible dependents. These plans cover substantially all employees who meet certain age and vested service requirements. Household has instituted dollar limits on its payments under the plans to control the cost of future medical benefits.

The net post-retirement benefit cost included the following:

	Year ended 31 December		
	2001	2000	1999
	US\$m	US\$m	US\$m
Service cost-benefits earned during the period	(3)	(3)	(4)
Interest cost on accumulated post-retirement benefit obligation.....	(11)	(10)	(10)
Amortisation of transition obligation	(7)	(7)	(6)
Amortisation of prior service cost	2	1	2
Recognised actuarial gain	3	3	1
Net periodic post-retirement benefit cost.....	(16)	(16)	(17)

A reconciliation of the beginning and ending balances of the accumulated post-retirement benefit obligation is as follows:

	Year ended 31 December		
	2001	2000	1999
	US\$m	US\$m	US\$m
Benefit obligation at beginning of year	160	160	181
Service cost	3	3	4
Interest cost	11	10	9
Actuarial losses/(gains)	29	(9)	(27)
Plan amendments	—	5	—
Benefits paid	(7)	(9)	(7)
Benefit obligation at end of year	196	160	160

Household's post-retirement benefit plans are funded on a pay-as-you-go basis. A reconciliation of the components of the accrued post-retirement benefit obligation is as follows:

	Year ended 31 December		
	2001	2000	1999
	US\$m	US\$m	US\$m
Funded status.....	197	161	161
Unamortised prior service cost.....	17	18	23
Unrecognised net actuarial gain.....	31	72	54
Unamortised transition obligation.....	(75)	(81)	(82)
Accrued post-retirement benefit obligation.....	170	170	156

The assumptions used in determining the benefit obligation and cost of such plans at 31 December were as follows:

	2001	2000	1999
	%	%	%
Discount rate.....	7.5	8.25	8.0
Salary increase assumption.....	4.0	4.0	4.0

In 2001, a 9.8 per cent annual rate of increase in the gross cost of covered health care benefits was assumed for 2002. This rate of increase was assumed to decline gradually to 5.35 per cent in 2008.

In 2000, a 7.5 per cent annual rate of increase in the gross cost of covered health care benefits was assumed for 2001. At that time this rate of increase was assumed to decline gradually to 5 per cent in 2007.

In 1999, an 8.0 per cent annual rate of increase in the gross cost of covered health care benefits was assumed for 2000. At that time this rate of increase was assumed to decline gradually to 5.0 per cent in 2006.

Assumed health care cost trend rates have an effect on the amounts reported for health care plans. A one-percentage point change in assumed health care cost trend rates would increase/(decrease) service and interest costs and the post-retirement benefit obligation as follows:

	One per cent increase	One per cent decrease
	US\$m	US\$m
At 31 December 2001		
Effect on total of service and interest cost components.....	1	(1)
Effect on post-retirement benefit obligation.....	8	(8)
At 31 December 2000		
Effect on total of service and interest cost components.....	(1)	1
Effect on post-retirement benefit obligation.....	8	(7)
At 31 December 1999		
Effect on total of service and interest cost components.....	(1)	1
Effect on post-retirement benefit obligation.....	8	(7)

18 Income taxes

Total income taxes were:

	Year ended 31 December		
	2001	2000	1999
	US\$m	US\$m	US\$m
Provision for income taxes related to operations.....	971	869	701
Income taxes related to adjustments included in common shareholders' equity:			
Unrealised gain/(loss) on investments, net.....	111	56	(50)
Unrealised losses on cash flow hedging instruments.....	(392)	—	—
Foreign currency translation adjustments.....	(10)	(22)	(6)
Exercise of stock based compensation.....	(36)	(24)	(89)
Total.....	644	879	556

Provisions for income taxes related to operations were:

	Year ended 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Current			
United States	907	711	634
Foreign	70	112	67
Total current	977	823	701
Deferred			
United States	(4)	52	(1)
Foreign	(2)	(6)	1
Total deferred	(6)	46	—
Total income taxes	971	869	701

The significant components of deferred income tax provisions attributable to income from operations were:

	Year ended 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Deferred income tax provision	(11)	48	(16)
Adjustment of valuation allowance	(12)	(8)	21
Change in operating loss carry-forwards	17	6	(5)
Deferred income tax provision	(6)	46	0

Income before income taxes was:

	Year ended 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
United States	2,541	2,163	1,839
Foreign	278	337	290
Total income before income taxes	2,819	2,500	2,129

Effective tax rates are analysed as follows:

	Year ended 31 December		
	2001 %	2000 %	1999 %
Statutory federal income tax rate	35.0	35.0	35.0
Increase/(decrease) in rate resulting from:			
State and local taxes, net of federal benefit	2.8	2.7	2.4
Tax credits	(2.7)	(1.5)	(0.9)
Other	(0.7)	(1.4)	(3.6)
Effective tax rate	34.4	34.8	32.9

Provision for US income taxes had not been made at 31 December 2001, 2000 and 1999 on US\$268 million, US\$301 million and US\$328 million, respectively, of undistributed earnings of foreign subsidiaries. Determination of the amount of unrecognised deferred tax liability related to investments in foreign subsidiaries is not practicable.

In addition, provision for US income taxes had not been made at 31 December 2001, 2000 and 1999 on US\$80 million of undistributed earnings of life insurance subsidiaries accumulated as policyholders' surplus under tax laws in effect prior to 1984. If this amount were distributed, the additional income tax payable would be approximately US\$28 million.

Household's US savings and loan subsidiary had credit loss reserves for tax purposes that arose in years beginning before December 1987 in the amount of US\$55 million for 31 December 2001, 2000 and 1999. The amount of deferred tax liability on the aforementioned credit loss reserves not recognised totalled US\$21 million at 31 December 2001, 2000 and 1999. As these amounts would become taxable only in the event of certain circumstances which Household does not expect to occur within the foreseeable future, no deferred tax liability has been established for these items.

At 31 December 2001, Household had net operating loss carry-forwards for tax purposes of US\$11 million, of which US\$2 million expire in 2004; US\$2 million expire in 2005; US\$2 million expire in 2006; and US\$5 million expire in 2019. Household also had foreign tax credit carry-forwards of US\$1 million which expire in 2004.

At 31 December, 2000, Household had net operating loss carry-forwards for tax purposes of US\$21 million, of which US\$5 million expire in 2003; US\$11 million expire in 2004; US\$3 million expire in 2005; and US\$2 million expire in 2006. Household also had foreign tax credit carry-forwards of US\$12 million, of which US\$8 million expire in 2003 and US\$4 million expire in 2004.

At 31 December, 1999 Household had net operating loss carry-forwards for tax purposes of US\$37 million, of which US\$0.3 million expire in 2001; US\$5 million expire in 2002; US\$6 million expire in 2003; US\$12 million expire in 2004; US\$7 million expire in 2005, and US\$7 million expire in 2006. Household also had foreign tax credit carry-forwards of US\$21 million, of which US\$8 million expire in 2003 and US\$13 million expire in 2004.

Temporary differences which gave rise to a significant portion of deferred tax assets and liabilities were as follows:

	Year ended 31 December		
	2001 US\$m	2000 US\$m	1999 US\$m
Deferred tax liabilities			
Receivables sold.....	838	822	749
Leveraged lease transactions, net.....	394	385	298
Deferred loan origination costs.....	103	36	—
Pension plan assets.....	154	143	136
Fee income.....	147	78	—
Other.....	215	214	361
Total deferred tax liabilities.....	1,851	1,678	1,544
Deferred tax assets			
Credit loss reserves.....	1,209	1,128	937
Market value adjustments.....	277	—	—
Other.....	522	421	462
Total deferred tax assets.....	2,008	1,549	1,399
Valuation allowance.....	—	(12)	(21)
Total deferred tax assets net of valuation allowance.....	2,008	1,537	1,378
Net deferred tax asset/(liability).....	157	(141)	(166)

The deferred tax asset valuation allowance relates entirely to foreign tax credit carry-forwards. Due to the limited carry forward period and limitations under US tax laws with respect to foreign tax credit utilisation, management believes it is more likely than not that the deferred tax asset will not be realised. The current period net change in the valuation allowance reflects the current utilisation of prior carry-forwards. A 100 per cent valuation allowance has been established relating to the remaining carry-forwards available.

19 Earnings per common share

	Year ended 31 December					
	2001		2000		1999	
	Diluted US\$m	Basic US\$m	Diluted US\$m	Basic US\$m	Diluted US\$m	Basic US\$m
Earnings						
Net income.....	1,848	1,848	1,631	1,631	1,428	1,428
Preferred dividends.....	(16)	(16)	(9)	(9)	(9)	(9)
Earnings available to common shareholders.....	1,832	1,832	1,622	1,622	1,419	1,419
Average shares						
Common.....	462	462	472	472	477	477
Common equivalents.....	6	—	4	—	5	—
Total.....	468	462	476	472	482	477
Earnings per common share.....	US\$ 3.91	US\$ 3.97	US\$ 3.40	US\$ 3.44	US\$ 2.95	US\$ 2.98

20 Commitments and contingent liabilities

In the ordinary course of business there are various legal proceedings pending against Household. Household management believe the aggregate liability, if any, resulting from such actions would not have a material adverse effect on Household's consolidated financial position, results of operations or cash flows. However, as the ultimate resolution of these proceedings is influenced by factors that are outside Household's control, it is reasonably possible that Household's estimated liability under these proceedings may change.

At 31 December 2001, Household's mortgage services business had commitments with numerous correspondents to purchase up to US\$1.1 billion of real estate secured receivables at fair market value, subject to availability based on underwriting guidelines specified by Household's mortgage services business. These commitments have terms of up to one year and can be renewed upon mutual agreement.

See Note 15 for discussion of lease commitments.

21 Segment reporting

Household has three reportable segments: consumer, credit card services, and international. Household's segments are managed separately and are characterised by different middle-market consumer lending products, origination processes, and locations. The consumer segment consists of Household's consumer lending, mortgage services, retail services, and auto finance businesses. The credit card services segment consists of Household's domestic MasterCard and Visa credit card business. The international segment consists of Household's foreign operations in the United Kingdom and Canada. The consumer segment provides real estate secured, automobile secured and personal non-credit card loans. Loans are originated with both revolving and closed-end terms and with fixed or variable interest rates. Loans are offered through branch locations, correspondents, mortgage brokers, direct mail, telemarketing, independent merchants or automobile dealers. The credit card services segment offers MasterCard and Visa credit cards throughout the United States primarily via strategic affinity and co-branding relationships, direct mail and Household's branch network, to sub-prime customers. The international segment offers secured and unsecured lines of credit and secured and unsecured closed-end loans primarily in the United Kingdom and Canada. In addition, the United Kingdom operation offers MasterCard and Visa credit cards and credit insurance in connection with all loan products. Household also cross sells its credit cards to existing real estate secured, private label and tax services customers. All segments offer products and service customers through the internet. The "all other" caption includes Household's insurance and tax services and commercial businesses, as well as its corporate and treasury activities, each of which falls below the quantitative threshold tests under FAS No. 131 for determining reportable segments.

The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies. For segment reporting purposes, intersegment transactions have not been eliminated. Household generally accounts for transactions between segments as if they were with third parties. Household evaluates performance and allocates resources based on income from operations after income taxes and returns on equity and managed assets.

Managed basis	Consumer US\$m	Credit card services US\$m	International US\$m	All other US\$m	Total US\$m	Adjustments/ reconciling items US\$m	Managed basis consolidated totals US\$m	Securitisation adjustments US\$m	Owned basis consolidated totals US\$m
Year ended 31 December 2001									
Net interest margin	5,829	1,497	592	(37)	7,881	—	7,881	(2,094) ⁶	5,787
Fee income	369	1,107	60	7	1,543	—	1,543	(639) ⁶	904
Other revenues ¹	358	99	209	554	1,220	(234) ²	986	1,627 ⁶	2,613
Intersegment revenues	191	38	8	(3)	234	(234) ²	—	—	—
Provision for credit losses	2,550	1,167	227	72	4,016	2 ³	4,018	(1,105) ⁶	2,913
Depreciation and amortisation	65	117	24	109	315	—	315	—	315
Income tax expense/(benefit)	841	188	65	(37)	1,057	(86) ⁴	971	—	971
Segment net income/(loss)	1,327	292	204	174	1,997	(149)	1,848	—	1,848
Receivables	75,641	17,178	7,158	846	100,823	—	100,823	(20,948) ⁸	79,875
Total segment assets	78,699	18,370	8,375	14,117	119,561	(9,702) ⁵	109,859	(20,948) ⁸	88,911
Expenditures for long-lived assets ⁷	17	4	28	126	175	—	175	—	175
Year ended 31 December 2000									
Net interest margin	4,852	1,179	594	(178)	6,447	—	6,447	(1,725) ⁶	4,722
Fee income	348	972	61	6	1,387	—	1,387	(627) ⁶	760
Other revenues ¹	402	114	244	415	1,175	(230) ²	945	1,217 ⁶	2,162
Intersegment revenues	192	33	5	—	230	(230) ²	—	—	—
Provision for credit losses	1,978	1,066	234	(27)	3,251	2 ³	3,253	(1,136) ⁶	2,117
Depreciation and amortisation	78	130	20	80	308	—	308	—	308
Income tax expense/(benefit)	796	102	99	(43)	954	(85) ⁴	869	—	869
Segment net income/(loss)	1,271	145	230	131	1,777	(146)	1,631	—	1,631
Receivables	63,067	15,997	7,847	696	87,607	—	87,607	(20,249) ⁸	67,358
Total segment assets	65,822	17,317	9,018	14,164	106,321	(9,763) ⁵	96,558	(20,249) ⁸	76,309
Expenditures for long-lived assets ⁷	29	283	38	100	450	—	450	—	450
Year ended 31 December 1999									
Net interest margin	4,043	991	614	(138)	5,510	—	5,510	(1,733) ⁶	3,777
Fee income	351	720	54	3	1,128	—	1,128	(582) ⁶	546
Other revenues ¹	207	64	184	475	930	(145) ²	785	1,250 ⁶	2,035
Intersegment revenues	124	17	4	—	145	(145) ²	—	—	—
Provision for credit losses	1,599	912	248	(1)	2,758	24 ³	2,782	(1,066) ⁶	1,716
Depreciation and amortisation	81	114	17	68	280	—	280	—	280
Income tax expense/(benefit)	626	67	59	11	763	(62) ⁴	701	—	701
Segment net income/(loss)	991	95	219	230	1,535	(107)	1,428	—	1,428
Receivables	49,399	13,855	7,619	855	71,728	—	71,728	(19,439) ⁸	52,289
Total segment assets	51,840	15,192	8,846	14,001	89,879	(9,988) ⁵	79,891	(19,439) ⁸	60,452
Expenditures for long-lived assets ⁷	79	6	46	64	195	—	195	—	195

¹ Net of policyholder benefits and excluding fees.

² Eliminates intersegment revenues.

³ Eliminates bad debt recovery sales between operating segments.

⁴ Tax benefit associated with items comprising adjustments/reconciling items.

⁵ Eliminates investments in subsidiaries and intercompany borrowings.

⁶ Reclassifies net interest margin, fee income and loss provisions relating to securitised receivables to other revenues.

⁷ Includes goodwill associated with purchase business combinations and capital expenditures.

⁸ Represents receivables serviced with limited recourse.

22 Restatement

Household restated its consolidated income statements for the years ended 31 December 2001, 2000 and 1999 and its consolidated balance sheets as at 31 December 2001 and 2000 included in its annual report on Form 10-K/A for the year ended 31 December 2001. The Form 10-K/A including these restated financial statements, audited by KPMG LLP, was filed with the SEC on 27 August 2002 and supersedes Household's annual report on Form 10-K audited by Arthur Andersen LLP and filed with the SEC on 13 March 2002.

Household did not restate its consolidated balance sheet as at 31 December 1999 in its revised filing with the SEC completed on 27 August 2002 and as such was not subject to audit by KPMG LLP. The only audited balance sheet as at 31 December 1999 is that included in the financial statements audited by Household's former auditors, Arthur Andersen LLP, and contained in Household's filing with the SEC on Form 10-K for the year ended 31 December 1999.

However, in order to conform with other financial information shown in this Part II the 1999 balance sheet presented herein has been adjusted to reflect the impact of restatement. These adjustments are not material and are summarised below:

At 31 December 1999			
	As originally reported US\$m	Restated US\$m	Adjustment US\$m
Acquired intangibles and goodwill, net	1,590	1,611	21
Other assets	2,854	2,536	(318)
Other liabilities	1,805	1,722	83
Retained earnings	6,339	6,125	214

Household International, Inc.

B. Unaudited consolidated financial information for the year ended 31 December 2002 and for the half-year to 30 June 2002

Extraction of financial information

The financial information on Household set out below has been extracted without material adjustment from the unaudited financial information included in Household's quarterly report on Form 10-Q for the period ended 30 June 2002 and from Household's earnings release for the financial year ended 31 December 2002 which was published on 15 January 2003 and was filed as an exhibit to the current report on Form 8-K with the SEC on 16 January 2003.

The financial information is summary only and has been prepared in accordance with US GAAP. US GAAP differs from UK GAAP in certain material respects. A summary of these differences is set out in section C of this Part II.

Unaudited consolidated statement of income

	Year ended 31 December 2002 US\$m	Half-year to 30 June 2002 US\$m
Finance and other interest income	10,526	5,145
Interest expense	(3,871)	(1,920)
Net interest margin	6,655	3,225
Provision for credit losses on owned receivables	(3,732)	(1,774)
Net interest margin after provision for credit losses	2,923	1,451
Securitisation revenue	2,134	1,042
Insurance revenue	716	348
Investment income	182	90
Fee income	949	407
Other income	543	283
Loss on disposal of Thrift assets and deposits	(378)	—
Total other revenues	4,146	2,170
Salaries and fringe benefits	(1,817)	(898)
Sales incentives	(256)	(122)
Occupancy and equipment expense	(371)	(186)
Other marketing expenses	(531)	(274)
Other servicing and administrative expenses	(889)	(436)
Amortisation of acquired intangibles and goodwill	(58)	(32)
Policyholders' benefits	(369)	(171)
Settlement charge and related expenses	(525)	—
Total costs and expenses	(4,816)	(2,119)
Income before income taxes	2,253	1,502
Income taxes	(695)	(504)
Net income	1,558	998
Earnings per common share		
Net income	1,558	998
Preferred dividends	(63)	(24)
Earnings available to common shareholders	1,495	974
Average common shares		457
Average common and common equivalent shares		462
Basic earnings per common share	US\$ 3.26	US\$ 2.13
Diluted earnings per common share	3.22	2.11
Dividends declared per common share	0.97	0.47

Household International, Inc.

Unaudited consolidated balance sheet

No consolidated balance sheet at 31 December 2002 has yet been published.

	At 30 June 2002 US\$m
Assets	
Cash	347
Investment securities	8,230
Receivables, net	82,133
Acquired intangibles, net	418
Goodwill	1,122
Properties and equipment, net	550
Real estate owned	457
Other assets	3,549
Total assets	96,806
Liabilities and shareholders' equity	
Debt:	
Deposits	5,612
Commercial paper, bank and other borrowings	3,599
Senior and senior subordinated debt (with original maturities over one year)	73,269
Total debt	82,480
Insurance policy and claim reserves	1,037
Other liabilities	2,810
Total liabilities	86,327
Company obligated mandatorily redeemable preferred securities of subsidiary trusts*	975
Preferred stock	843
Common shareholders' equity:	
Common stock, US\$1.00 par value, 750,000,000 shares authorised, 551,779,393 shares issued	552
Additional paid-in capital	2,058
Retained earnings	9,597
Accumulated other comprehensive income (loss)	(605)
Less common stock in treasury, 95,154,527 shares	(2,941)
Total common shareholders' equity	8,661
Total liabilities and shareholders' equity	96,806

* As described in note 8 to the consolidated financial statements, the sole assets of the trusts are junior subordinated deferrable interest notes issued by Household in November 2001, January 2001, June 2000, March 1998 and June 1995, bearing interest at 7.50 per cent, 8.25 per cent, 10.00 per cent, 7.25 per cent and 8.25 per cent, respectively, with principal balances of US\$206 million, US\$206 million, US\$309 million, US\$206 million and US\$77 million, respectively, and due November 2031, January 2031, June 2030, December 2037 and June 2025, respectively.

Household International, Inc.

Unaudited consolidated statement of cash flows

No consolidated statement of cash flows for the year ended 31 December 2002 has yet been published.

	Half-year to 30 June 2002 US\$m
Cash provided by operations	
Net income.....	998
Adjustments to reconcile net income to cash provided by operations:	
Provision for credit losses on owned receivables.....	1,774
Insurance policy and claim reserves.....	87
Depreciation and amortisation.....	117
Interest-only strip receivables, net change.....	(59)
Other assets, excluding FAS No. 133.....	(61)
Other liabilities, excluding FAS No. 133.....	738
Other, net.....	82
Cash provided by operations.....	3,676
Investments in operations	
Investment securities:	
Purchased.....	(2,817)
Matured.....	622
Sold.....	232
Short-term investment securities, net change.....	(2,585)
Receivables:	
Originations, net.....	(22,698)
Purchases and related premiums.....	(407)
Sold.....	18,603
Properties and equipment purchased.....	(84)
Properties and equipment sold.....	3
Cash decrease from investments in operations.....	(9,131)
Financing and capital transactions	
Short-term debt and demand deposits, net change.....	(7,709)
Time certificates, net change.....	(952)
Senior and senior subordinated debt issued.....	19,812
Senior and senior subordinated debt retired.....	(5,747)
Policyholders' benefits paid.....	(214)
Cash received from policyholders.....	35
Shareholders' dividends.....	(238)
Purchase of treasury stock.....	(160)
Issue of common stock.....	86
Issue of preferred stock.....	387
Issue of company obligated mandatorily redeemable preferred securities of subsidiary trusts.....	—
Cash increase from financing and capital transactions.....	5,300
Effect of exchange rate changes on cash.....	(42)
Decrease in cash.....	(197)
Cash at 1 January.....	544
Cash at 30 June.....	347
Supplemental cash flow information	
Interest paid.....	1,892
Income taxes paid.....	469

Household International, Inc.

Notes to unaudited consolidated financial information for the half-year to 30 June 2002

1 Basis of presentation

The accompanying unaudited consolidated financial information of Household and its subsidiaries for the half-year to 30 June 2002 was prepared in accordance with US GAAP for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, it does not include all of the information and footnotes required by US GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included.

This unaudited consolidated financial information should be read in conjunction with the consolidated financial statements and footnotes included in Household's restated annual report on Form 10-K/A for the year ended 31 December 2001 (which was filed with the SEC on 27 August 2002.)

2 Investment securities

Investment securities consisted of the following available-for-sale investments:

	At 30 June 2002	
	Amortised cost US\$m	Fair value US\$m
Corporate debt securities	2,034	2,017
Money market funds	2,312	2,312
Certificates of deposit	202	207
U.S. government and federal agency debt securities	2,313	2,315
Marketable equity securities	31	25
Other	1,274	1,283
Subtotal	8,166	8,159
Accrued investment income	71	71
Total available-for-sale investments	8,237	8,230

3 Receivables

Receivables consisted of the following:

	At 30 June 2002	
	US\$m	
Real estate secured	48,312	
Auto finance	2,363	
MasterCard*/Visa*	6,881	
Private label	10,827	
Personal non-credit card	14,272	
Commercial and other	483	
Total owned receivables	83,138	
Accrued finance charges	1,551	
Credit loss reserve for owned receivables	(2,983)	
Unearned credit insurance premiums and claims reserves	(878)	
Interest-only strip receivables	1,012	
Amounts due and deferred from receivable sales	293	
Total owned receivables, net	82,133	
Receivables serviced with limited recourse	22,323	
Total managed receivables, net	104,456	

* MasterCard is a registered trademark of MasterCard International, Incorporated and Visa is a registered trademark of Visa USA, Inc.

Interest-only strip receivables are reported net of Household's estimate of probable losses under the recourse provisions for receivables serviced with limited recourse. Household's estimate of the recourse obligation totalled US\$1,386 million at 30 June 2002. Interest-only strip receivables also included fair value mark-to-market adjustments which increased the balance by US\$334 million at 30 June 2002.

Receivables serviced with limited recourse consisted of the following:

	At 30 June 2002 US\$m
Real estate secured	576
Auto finance	4,518
MasterCard/Visa	9,906
Private label	2,650
Personal non-credit card	4,673
Total receivables serviced with limited recourse	22,323

The combination of owned receivables and receivables serviced with limited recourse, which Household considers as its managed portfolio, consisted of the following:

	At 30 June 2002 US\$m
Real estate secured	48,888
Auto finance	6,881
MasterCard/Visa	16,787
Private label	13,477
Personal non-credit card	18,945
Commercial and other	483
Total managed receivables	105,461

4 Credit loss reserves

An analysis of credit loss reserves for the half-year to 30 June 2002 is as follows:

	Half-year to 30 June 2002 US\$m
Credit loss reserves for owned receivables:	
Credit loss reserves at beginning of period	2,663
Provision for credit losses	1,774
Charge-offs	(1,609)
Recoveries	125
Other, net	30
Credit loss reserves for owned receivables	2,983
Credit loss reserves for receivables serviced with limited recourse:	
Credit loss reserves at beginning of period	1,148
Provision for credit losses	867
Charge-offs	(689)
Recoveries	49
Other, net	11
Credit loss reserves for receivables serviced with limited recourse	1,386
Total credit loss reserves for managed receivables	4,369

Household maintains credit loss reserves to cover probable losses of principal, interest and fees, including late, over limit and annual fees. Credit loss reserves are based on a range of estimates and intended to be adequate but not excessive. Household statistically estimates losses for consumer receivables based on delinquency and re-age status and past loss experience. In addition, Household provides loss reserves on consumer receivables to reflect Household's assessment of portfolio risk factors which may not be fully reflected in the statistical calculation (which uses roll rates and migration analysis). These risk factors include bankruptcy trends, recent growth, product mix, economic conditions and current levels of charge-offs and delinquencies.

5 Acquired intangibles and goodwill

With effect from 1 January 2002, Household adopted FAS No. 142, "Goodwill and Other Intangible Assets". FAS No. 142 changed the accounting for goodwill from an amortisation method to an impairment-only approach. Amortisation of goodwill recorded in past business combinations ceased upon adoption of the statement on 1 January 2002. Household completed the transitional goodwill impairment test required by FAS No. 142 and concluded that none of its goodwill was impaired.

Household did not hold any intangible assets which were not subject to amortisation. Amortised acquired intangibles consisted of the following:

	At 30 June 2002 US\$m
Purchased credit card relationships	1,039
Other intangibles	26
Accumulated amortisation – purchased credit card relationships	(640)
Accumulated amortisation – other intangibles	(7)
	<hr/>
Acquired intangibles, net	418
	<hr/>

Acquired intangible amortisation expense totalled US\$32 million for the half-year to 30 June 2002.

Estimated amortisation expense associated with Household's acquired intangibles for each of the following years was as follows:

Year ending 31 December	At 30 June 2002 US\$m
2002	58
2003	50
2004	48
2005	43
2006	41

There were no significant changes to Household's recorded amount of goodwill, either in total or by segment, during the half-year to 30 June 2002.

6 Income taxes

Household's effective tax rate was 33.6 per cent for the half-year to 30 June 2002. The effective tax rate differs from the statutory federal income tax rate in all periods because of the effects of state and local income taxes and tax credits.

7 Earnings per common share

The computation of earnings per common share for the half-year to 30 June 2002 was as follows:

	Half-year to 30 June 2002	
	Diluted US\$m	Basic US\$m
Earnings:		
Net income.....	998	998
Preferred dividends.....	(24)	(24)
Earnings available to common shareholders.....	974	974
Average number of shares outstanding:		
Common.....	457	457
Common equivalents.....	5	—
Average number of shares outstanding assuming dilution.....	462	457
Earnings per common share.....	US\$ 2.11	US\$ 2.13

8 Company obligated mandatorily redeemable preferred securities of subsidiary trusts

Household has formed special purpose trusts for the purpose of issuing trust preferred securities. The sole assets of these trusts are junior subordinated deferrable interest notes (“junior subordinated notes”) issued by Household. The following table summarises Household’s company obligated mandatorily redeemable preferred securities of subsidiary trusts (“preferred securities”) and the related junior subordinated notes:

	Household Capital Trust VII ("HCT VII")	Household Capital Trust VI ("HCT VI")	Household Capital Trust V ("HCT V")	Household Capital Trust IV ("HCT IV")	Household Capital Trust I ("HCT I")
Preferred securities:					
Interest rate.....	7.50%	8.25%	10.00%	7.25%	8.25%
Face value (US\$m).....	200	200	300	200	75
Issue date.....	November 2001	January 2001	June 2000	March 1998	June 1995
Junior subordinated notes:					
Principal balance (US\$m).....	206	206	309	206	77
Redeemable by issuer.....	November 2006	January 2006	June 2005	March 2003	June 2000
Stated maturity.....	November 2031	January 2031	June 2030	December 2037	June 2025

The preferred securities must be redeemed when the junior subordinated notes are paid. The junior subordinated notes each have a stated maturity date, but are redeemable by Household, in whole or in part, beginning on the dates indicated above at which time the preferred securities are callable at par (US\$25 per preferred security) plus accrued and unpaid dividends. Dividends on the preferred securities are cumulative, payable quarterly in arrears, and are deferrable at Household’s option for up to five years. Household cannot pay dividends on its preferred and common stocks during such deferrals. The preferred securities have a liquidation value of US\$25 per preferred security. HCT I may elect to extend the maturity of its preferred securities to June 2044. Dividends on the preferred securities have been classified as interest expense in Household’s statements of income.

HCT I, HCT IV, HCT V, HCT VI and HCT VII (collectively “the Trusts”) are wholly-owned subsidiaries of Household. Household’s obligations with respect to the junior subordinated notes, when considered together with certain undertakings of Household with respect to the Trusts, constitute full and unconditional guarantees by Household of the Trusts’ obligations under the respective preferred securities. The preferred securities are classified in Household’s balance sheet as company obligated mandatorily redeemable preferred securities of subsidiary trusts (representing the minority interests in the Trusts) at their face and redemption amount of US\$975 million at 30 June 2002.

9 Forward purchase agreements

At 30 June 2002, Household had agreements to purchase, on a forward basis, approximately 6.1 million of its shares with a weighted-average forward price of US\$55.63 per share. The agreements expire at various dates to June 2003. These agreements may be settled physically or on a net basis either in Household’s common shares or in cash, depending on the terms of the various agreements, at Household’s option, and consequently are accounted for as permanent equity. During the quarter ended 30 June 2002, Household received 966,000 shares at an average cost of US\$62.11 per share as a result of settlements under these forward contracts.

Under a net share settlement, if the price of Household's common shares falls below the forward price, Household would be required to deliver common shares to the counterparty based upon the difference between the forward price and the then current share price. Conversely, if the price of Household's common shares rises above the forward price, the counterparty would be required to deliver to Household Household's common shares based on the price difference. Based upon the closing price of Household's common shares of US\$49.70 per share at 30 June 2002, Household would have been required to deliver approximately 731,800 of its common shares to net share settle these contracts at 30 June 2002. If Household's common share price had been lower by US\$1 per share at 30 June 2002, Household would have been required to deliver an additional 141,000 common shares to net share settle these contracts. If Household's common share price had been higher by US\$1 per share at 30 June 2002, Household would have been required to deliver a total of 596,400 of its common shares to net share settle the contracts. These agreements, however, contain limits on the number of shares to be delivered under a net share settlement, regardless of the price of Household's common shares. At 30 June 2002, the maximum number of common shares Household would be required to deliver to net share settle the 6.1 million shares then outstanding was 31.5 million shares.

10 Comprehensive income

Comprehensive income was US\$1.1 billion for the half-year to 30 June 2002.

The components of accumulated other comprehensive income were as follows:

	Half-year to 30 June 2002 US\$m
Unrealised losses on cash flow hedging instruments	(568)
Unrealised gains on investments and interest-only strip receivables	208
Foreign currency translation adjustments	(245)
Accumulated other comprehensive loss	(605)

11 New accounting pronouncements and changes in accounting policies

With effect from 1 January 2002, Household adopted FAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". The adoption of FAS No. 144 did not have a significant impact on Household's operations.

Household adopted the fair value method of accounting for Household's stock option and employee stock purchase plans in 2002. Under the guidance of FAS No. 123, "Accounting for Stock-Based Compensation", companies may either recognise stock-based compensation expense associated with these plans currently in income or disclose the pro forma impact of the expense. Pursuant to the requirements of FAS No. 123, options granted prior to 1 January 2002 continue to be accounted for under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," under which expenses for stock options are generally not recognised. The impact of adopting the expense recognition provisions of FAS No. 123 is not expected to have a significant impact on Household's future results of operations.

12 Segment reporting

Household has three reportable segments: consumer, credit card services, and international. The consumer segment consists of Household's consumer lending, mortgage services, retail services, and auto finance businesses. The credit card services segment consists of Household's domestic MasterCard and Visa credit card business. The international segment consists of Household's foreign operations in the United Kingdom and Canada. There was no change in the basis of segmentation or in the measurement of segment profit compared to the presentation in Household's Annual Report on Form 10-K for the year ended December 31, 2001.

Household allocates resources and provides information to management for decision making on a managed basis. Therefore, an adjustment is required to reconcile the managed financial information to the reported financial information in the consolidated financial statements. This adjustment reclassifies net interest margin, fee income and loss provision into securitisation revenue.

Managed basis	Consumer US\$m	Credit card services US\$m	International US\$m	All other US\$m	Total US\$m	Adjustments/ reconciling items US\$m	Managed basis consolidated totals US\$m	Securitisation adjustments US\$m	Owned basis consolidated totals US\$m
Half-year to 30 June 2002									
Net interest margin.....	3,377	841	307	8	4,533	—	4,533	(1,308) ⁴	3,225
Fee income	173	527	23	4	727	—	727	(320) ⁴	407
Other revenues ¹	306	108	137	380	931	(101) ²	830	762 ²	1,592
Intersegment revenues.....	79	18	5	(1)	101	(101) ²	—	—	—
Provision for credit losses	1,762	717	151	34	2,664	(23) ³	2,641	(867) ⁴	1,774
Segment net income/(loss)	671	143	82	151	1,047	(49)	998	—	998

¹ Net of policyholder benefits and excluding fees.

² Eliminates intersegment revenues.

³ Eliminates bad debt recovery sales between operating segments.

⁴ Reclassifies net interest margin, fee income and loss provisions relating to securitised receivables to other revenues.

Household International, Inc.

C. Unaudited restatement of Household financial information

Household's income statements and balance sheets as published under US GAAP have been restated in this section to conform to HSBC's UK GAAP basis of presentation. The information in this section has not been audited.

Unaudited consolidated income statements for the years ended 31 December 2001, 2000 and 1999

	Notes	Year ended 31 December 2001			Year ended 31 December 2000			Year ended 31 December 1999		
		US GAAP US\$m	Adjustments US\$m	UK GAAP US\$m	US GAAP US\$m	Adjustments US\$m	UK GAAP US\$m	US GAAP US\$m	Adjustments US\$m	UK GAAP US\$m
Interest receivable										
– interest receivable and similar income arising from debt securities.....		64	—	64	52	—	52	28	—	28
– other interest receivable and similar income.....	(a,c,i)	9,935	3,317	13,252	8,617	3,155	11,772	6,521	2,888	9,409
Interest payable.....	(c)	(4,174)	(1,039)	(5,213)	(3,929)	(1,283)	(5,212)	(2,777)	(1,060)	(3,837)
Net interest income		5,825	2,278	8,103	4,740	1,872	6,612	3,772	1,828	5,600
Dividend income.....		—	—	—	8	—	8	21	—	21
Fees and commissions receivable.....	(c)	2,116	(551)	1,565	1,741	(334)	1,407	1,554	(418)	1,136
Other operating income.....	(b,c)	1,363	(574)	789	1,155	(499)	656	1,011	(365)	646
Operating income		9,304	1,153	10,457	7,644	1,039	8,683	6,358	1,045	7,403
Administrative expenses.....	(a,h,j)	(3,250)	(315)	(3,565)	(2,749)	(244)	(2,993)	(2,291)	(154)	(2,445)
Depreciation and amortisation.....		(140)	—	(140)	(136)	—	(136)	(130)	—	(130)
– tangible fixed assets.....	(f,g)	(59)	(300)	(359)	(57)	(300)	(357)	(42)	(300)	(342)
– goodwill.....										
Operating profit before provisions		5,855	538	6,393	4,702	495	5,197	3,895	591	4,486
Provisions.....		(3,036)	(1,162)	(4,198)	(2,202)	(953)	(3,155)	(1,766)	(1,028)	(2,794)
– provisions for bad and doubtful debts.....	(c,i)									
Operating profit and profit on ordinary activities before tax		2,819	(624)	2,195	2,500	(458)	2,042	2,129	(437)	1,692
Tax on profit on ordinary activities.....	(k)	(971)	143	(828)	(869)	70	(799)	(701)	128	(573)
Profit on ordinary activities after tax		1,848	(481)	1,367	1,631	(388)	1,243	1,428	(309)	1,119
Profit attributable to shareholders		1,848	(481)	1,367	1,631	(388)	1,243	1,428	(309)	1,119
Per ordinary share.....		US\$		US\$	US\$		US\$	US\$		US\$
– basic earnings.....		3.97		2.94	3.44		2.64	2.98		2.33
– diluted earnings.....		3.91		2.91	3.40		2.62	2.95		2.30

The accompanying notes form an integral part of this financial information.

Household International, Inc.

Set out below are the unaudited consolidated balance sheets of Household as at 31 December 2001, 2000 and 1999 restated to conform to HSBC's UK GAAP basis of presentation.

Unaudited consolidated balance sheets as at 31 December 2001, 2000 and 1999

	At 31 December 2001			At 31 December 2000			At 31 December 1999		
Notes	US GAAP US\$m	Adjustments US\$m	UK GAAP US\$m	US GAAP US\$m	Adjustments US\$m	UK GAAP US\$m	US GAAP US\$m	Adjustments US\$m	UK GAAP US\$m
ASSETS									
Items in the course of collection from other banks.....	963	—	963	1,192	—	1,192	1,127	—	1,127
Loans and advances to banks.....	58	—	58	88	—	88	97	—	97
Loans and advances to customers.....	78,609	17,944	96,553	66,245	17,686	83,931	51,269	17,383	68,652
Debt securities.....	935	(9)	926	658	—	658	557	(1)	556
Equity shares.....	63	—	63	141	—	141	164	—	164
Intangible fixed assets.....	1,563	4,814	6,377	1,720	5,114	6,834	1,611	5,414	7,025
Tangible fixed assets.....	531	(16)	515	517	(9)	508	476	(7)	469
Other assets.....	5,515	556	6,071	5,163	858	6,021	4,837	790	5,627
(b,c,e,k)									
Prepayments and accrued income.....	1,570	(128)	1,442	1,310	(110)	1,200	883	(95)	788
(i)									
Total assets.....	89,807	23,161	112,968	77,034	23,539	100,573	61,021	23,484	84,505
LIABILITIES									
Deposits by banks.....	1,985	—	1,985	1,417	—	1,417	1,956	—	1,956
Customer accounts.....	6,562	(24)	6,538	8,677	—	8,677	4,980	—	4,980
Debt securities in issue.....	66,863	20,408	87,271	54,424	19,141	73,565	43,709	18,580	62,289
Other liabilities.....	3,132	(1,222)	1,910	2,178	300	2,478	1,722	—	1,722
(a,b,c,d,e,f,h,i,k)									
Provisions for liabilities and charges									
— deferred taxation.....	—	—	—	—	—	—	—	—	—
— other provisions for liabilities and charges.....	1,991	—	1,991	1,832	—	1,832	1,878	—	1,878
Subordinated liabilities									
— dated loan capital.....	975	—	975	675	—	675	375	—	375
(d)									
Called up share capital.....	457	(6)	451	471	(7)	464	468	—	468
Preference share capital.....	456	—	456	164	—	164	164	—	164
Other reserves.....	(1,451)	7,157	5,706	(201)	6,777	6,576	(356)	7,188	6,832
Profit and loss account.....	8,837	(3,152)	5,685	7,397	(2,672)	4,725	6,125	(2,284)	3,841
Shareholders' funds.....	8,299	3,999	12,298	7,831	4,098	11,929	6,401	4,904	11,305
Total liabilities.....	89,807	23,161	112,968	77,034	23,539	100,573	61,021	23,484	84,505

The accompanying notes form an integral part of this financial information.

Household International, Inc.

Set out below are the unaudited consolidated income statements of Household for the year ended 31 December 2002 and for the half-year to 30 June 2002 restated to conform to HSBC's UK GAAP basis of presentation.

Unaudited consolidated income statements for the year ended 31 December 2002 and for the half-year to 30 June 2002

	Notes	Year ended 31 December 2002			Half-year to 30 June 2002		
		US GAAP US\$m	Adjustments US\$m	UK GAAP US\$m	US GAAP US\$m	Adjustments US\$m	UK GAAP US\$m
Interest receivable							
– interest receivable and similar income arising from debt securities		102	—	102	35	—	35
– other interest receivable and similar income	(a,c,i)	10,426	3,540	13,966	5,120	1,754	6,874
Interest payable	(c)	(3,871)	(674)	(4,545)	(1,920)	(342)	(2,262)
Net interest income		6,657	2,866	9,523	3,235	1,412	4,647
Dividend income		45	—	45	15	—	15
Fees and commissions receivable	(c)	2,267	(620)	1,647	1,066	(322)	744
Other operating income	(b,c)	1,841	(848)	993	908	(396)	512
Operating income		10,810	1,398	12,208	5,224	694	5,918
Administrative expenses	(a,h,j)	(3,606)	(352)	(3,958)	(1,791)	(167)	(1,958)
Depreciation and amortisation – tangible fixed assets		(139)	—	(139)	(67)	—	(67)
– goodwill	(f,g)	—	(359)	(359)	—	(180)	(180)
Operating profit before provisions		7,065	687	7,752	3,366	347	3,713
Provisions – provisions for bad and doubtful debts	(c,i)	(3,909)	(1,546)	(5,455)	(1,864)	(734)	(2,598)
– provisions for contingent liabilities and commitments ...		(525)	—	(525)	—	—	—
Operating profit		2,631	(859)	1,772	1,502	(387)	1,115
Loss on disposal of – investments		(378)	—	(378)	—	—	—
Profit on ordinary activities before tax		2,253	(859)	1,394	1,502	(387)	1,115
Tax on profit on ordinary activities	(k)	(695)	195	(500)	(504)	83	(421)
Profit on ordinary activities after tax		1,558	(664)	894	998	(304)	694
Profit attributable to shareholders		1,558	(664)	894	998	(304)	694
Per ordinary share		US\$		US\$	US\$		US\$
– basic earnings		3.26		1.83	2.13		1.49
– diluted earnings		3.22		1.82	2.11		1.47

The accompanying notes form an integral part of this financial information.

Household International, Inc.

Set out below is the unaudited consolidated balance sheet of Household as at 30 June 2002 restated to conform to HSBC's UK GAAP basis of presentation.

Unaudited consolidated balance sheet as at 30 June 2002

At 30 June 2002			
Notes	US GAAP US\$m	Adjustments US\$m	UK GAAP US\$m
Assets			
Items in the course of collection from other banks	639	—	639
Loans and advances to banks	244	—	244
Loans and advances to customers	(a,c,i) 81,641	19,239	100,880
Debt securities	(e) 3,877	—	3,877
Equity shares	1,763	—	1,763
Intangible fixed assets	(f,g) 1,541	4,634	6,175
Tangible fixed assets	(h) 550	(33)	517
Other assets	(b,c,e,k) 5,840	286	6,126
Prepayments and accrued income	(i) 1,589	(135)	1,454
Total assets	97,684	23,991	121,675
Liabilities			
Deposits by banks	684	—	684
Customer accounts	(b) 5,612	(20)	5,592
Debt securities in issue	(b,c) 76,184	20,494	96,678
Other liabilities	(a,b,c,d,e,f,h,i,k) 2,810	(97)	2,713
Provisions for liabilities and charges			
— deferred taxation	—	—	—
— other provisions for liabilities and charges	1,915	—	1,915
Subordinated liabilities			
— dated loan capital	975	—	975
Called up share capital	(d) 457	(7)	450
Preference share capital	843	—	843
Other reserves	(1,393)	7,077	5,684
Profit and loss account	9,597	(3,456)	6,141
Shareholders' funds	9,504	3,614	13,118
Total liabilities	97,684	23,991	121,675

The accompanying notes form an integral part of this financial information.

UK GAAP adjustments to historical Household statements of income and balance sheets

Household prepares its consolidated financial statements in accordance with US GAAP. In preparing the unaudited UK GAAP financial information, Household's historical consolidated financial statements have been adjusted to conform to HSBC's accounting policies under UK GAAP by making the adjustments described below.

a. Deferred origination expenses

Under US GAAP, certain direct loan origination costs are deferred and recognised over the life of the related loans as a reduction in the loans' yield. Under UK GAAP, HSBC applies a more restricted definition of the directly incurred origination expenses which are deferred and subsequently amortised over the life of the loans and classified as operating expenses. The impact of aligning with HSBC's accounting policies is to reduce the amount of origination costs deferred on the balance sheet, to reduce correspondingly the amortisation cost from deferred origination costs, and to increase operating expenses.

b. Derivative financial instruments

Under US GAAP, all derivatives are recognised on the balance sheet at their fair value. Derivatives are designated either as a fair value hedge, a cash flow hedge, a hedge of a net investment in a foreign operation or a non-hedging derivative. Changes in the fair value of derivatives designated as fair value hedges, along with the change in fair value of the hedged asset or liability that is attributable to the hedged risk, are recorded in current period earnings. Changes in the fair value of derivatives designated as cash flow hedges, to the extent effective as a hedge, are recorded in accumulated other comprehensive income and reclassified into earnings in the period during which the hedged item effects earnings. Changes in the fair value of derivatives used to hedge net investment in foreign operations, to the extent effective as a hedge, are recorded in common shareholders' equity as a component of the cumulative translation adjustment account within accumulated other comprehensive income. Changes in the fair value of derivative instruments not designated as hedging instruments and ineffective portions of changes in the fair value of hedging instruments are recognised in earnings in the period of change in fair value.

Under UK GAAP, non-trading derivatives, including qualifying interest rate swaps, are accounted for on an equivalent basis to the underlying assets, liabilities or net positions. Any profit or loss arising is recognised on the same basis as that arising from the related assets, liabilities or positions.

For purposes of the presentation of Household's UK GAAP financial information, all adjustments to measure non-trading derivatives at fair value have been reversed.

c. Securitisations

Certain loans to customers have been securitised and sold to investors with limited recourse with servicing rights retained by Household. Under US GAAP, the customer loans are removed from the balance sheet and a gain on sale is recognised for the difference between the carrying value of the customer loans and the sales proceeds. The resulting gain is adjusted by a provision for estimated probable losses under the recourse provisions based on historical experience and estimates of expected future performance.

In connection with these transactions, an interest-only strip receivable, representing the contractual right to receive interest and other cash flows from Household's securitisation trusts, is recorded. The interest-only strip receivables are reported at fair value with unrealised gains and losses recorded as adjustments to common shareholders' funds in accumulated other comprehensive income, net of income taxes.

Under UK GAAP, the Household securitisation transactions are treated as financing transactions. The securitised customer loans are treated as owned by Household and consequently are included on Household's balance sheet. Any gains recorded under US GAAP on these transactions and fair value adjustments to the interest-only strip receivables are reversed. For certain securitisation transactions, the receivables and associated debt are reported under UK GAAP under a "linked presentation" format where the debt is non-recourse and is repayable only from benefits generated by the assets being financed or by transfer of the assets themselves. In a linked presentation, the non-recourse debt is shown deducted from the related gross receivables on the face of the balance sheet.

d. Forward purchase agreements

Under US GAAP, the agreements Household has entered into to purchase, on a forward basis, shares of its common stock have been treated as equity instruments. Under UK GAAP, the fair value of such agreements has been recorded as a liability and deducted from shareholders' funds.

e. Investment securities

Under US GAAP, available-for-sale securities are measured at fair value with unrealised gains and losses excluded from earnings and reported net of applicable taxes within accumulated other comprehensive income.

Under UK GAAP, debt securities and equity shares intended to be held on a continuing basis are disclosed as investment securities and are included in the balance sheet at cost less provision for any permanent diminution in value.

All of Household's available-for-sale securities are classified under UK GAAP as investment securities. Accordingly, in the UK GAAP presentation, all such securities have been recorded at cost and the equity adjustment for unrealised gains and losses has been reversed.

f. Goodwill

Under US GAAP, amortisation of goodwill recorded in past business combinations ceased on 1 January 2002. Prior to that time, goodwill was amortised over its estimated useful life. Under UK GAAP, for acquisitions prior to 1998, goodwill was charged against reserves in the year of acquisition. For acquisitions made since 1 January 1998, goodwill is included in the balance sheet and amortised over its useful economic life on a straight-line basis.

In the UK GAAP presentation, for acquisitions prior to 1998, goodwill arising has been eliminated in other reserves and related goodwill amortisation prior to 2002 has been reversed. For post-1998 acquisitions, amortisation has been included in the income statements for all periods.

g. Household's merger with Beneficial Corporation

On 30 June 1998, Household acquired Beneficial Corporation ("Beneficial"), a consumer finance company headquartered in Wilmington, Delaware. Each outstanding share of Beneficial common stock was converted into 3.066 shares of Household's common stock, resulting in approximately 168.4 million shares of Household common stock being issued to the former Beneficial stockholders. In addition, each share of Beneficial convertible preferred stock was converted into Household common stock and each share of Beneficial other preferred stock was converted into newly created Household preferred stock with terms substantially similar to those of the previously existing Beneficial preferred stock.

Under US GAAP, the transaction was accounted for as a pooling of interests which is similar in treatment to UK GAAP merger accounting, and, as such, the published consolidated financial statements of Household include the financial position, results of operations and changes in cash flows of Beneficial for all periods presented.

Under UK GAAP, the merger of Household and Beneficial has been accounted for using acquisition accounting and, as such, the assets and liabilities of Beneficial at 30 June 1998 would have been recorded at their respective fair values and added to the assets and liabilities of Household. Such fair value adjustments would not have been significant. The excess of the purchase price over the net tangible assets of Beneficial has been recorded as goodwill and reflected in the Household UK GAAP balance sheet at 30 June 2002. The amortisation of this goodwill over a 20-year estimated life has been reflected in the Household UK GAAP income statements.

h. Costs of software for internal use

Under US GAAP, costs incurred in the application development stage of the development of software are capitalised and amortised over the estimated useful life of the software. Under UK GAAP, HSBC generally expenses costs of software developed for internal use. In the UK GAAP presentation, any software costs capitalised under US GAAP have been expensed in the period incurred and the resulting amortisation has been eliminated.

i. Suspended interest

Household and HSBC suspend interest income on real estate secured, personal non-credit card and commercial loans when principal or interest payments are more than three months contractually overdue. However, HSBC

also reverses any interest income previously recognised in the period. In the UK GAAP presentation, all accrued interest on the above products more than three months contractually overdue has been reversed together with any loss reserves allocated to that accrued interest.

j. Share-based compensation

Under US GAAP, Household accounts for its share option and employee share purchase plans at their fair values at the date of grant. These values are amortised over the vesting period, in Household's case four years, and the cost of amortisation is charged to compensation costs. This accounting policy was adopted by Household during the second half of 2002.

Under UK GAAP, compensation costs are only recognised if the exercise price differs from the market price on the day options are granted. In the UK GAAP presentation amortisation charged to compensation costs by Household in the second half of 2002 has been reversed.

k. Taxation

Where appropriate, the adjustments from US GAAP to UK GAAP on the statements of income of Household have been adjusted for taxation assuming an effective tax rate of 36.5 per cent.

Under US GAAP tax relief obtained on share based compensation expense is not recorded in arriving at net income, but instead is recorded as part of shareholders' equity. Under UK GAAP such relief forms part of the profit for the year. Upon adoption of FAS No. 123 in 2002, Household began recording the tax relief as part of net income.

Under US GAAP, tax assets and tax liabilities are shown as a net asset or a net liability on the balance sheet. Deferred tax assets have been shown separately to current tax liabilities to comply with UK GAAP.

Adjustments made to conform Household's US GAAP consolidated income statements to HSBC's accounting policies under UK GAAP are set out below under each of the items described in the notes above:

	Year ended 31 December 2002	Half-year to 30 June 2002	Year ended 31 December 2001	Year ended 31 December 2000	Year ended 31 December 1999
	US\$m	US\$m	US\$m	US\$m	US\$m
Other interest receivable and similar income					
(a) Deferred origination expenses . . .	217	111	203	161	121
(c) Receivables sold and serviced with limited recourse and securitisation revenue	3,357	1,650	3,133	3,008	2,792
(i) Interest suspension	(34)	(7)	(19)	(14)	(25)
	3,540	1,754	3,317	3,155	2,888
Interest payable					
(c) Receivables sold and serviced with limited recourse and securitisation revenue	(674)	(342)	(1,039)	(1,283)	(1,060)
	(674)	(342)	(1,039)	(1,283)	(1,060)
Fees and commissions receivable					
(c) Receivables sold and serviced with limited recourse and securitisation revenue	(620)	(322)	(551)	(334)	(418)
	(620)	(322)	(551)	(334)	(418)
Other operating income					
(b) Derivative financial instruments . .	(3)	3	(1)	—	—
(c) Receivables sold and serviced with limited recourse and securitisation revenue	(845)	(399)	(573)	(499)	(365)
	(848)	(396)	(574)	(499)	(365)
Administrative expenses					
(a) Deferred origination expenses . . .	(317)	(151)	(308)	(241)	(152)
(h) Costs of software for internal use	(40)	(16)	(7)	(3)	(2)
(j) Share-based compensation	5	—	—	—	—
	(352)	(167)	(315)	(244)	(154)
Depreciation and amortisation – goodwill					
(f) Goodwill	(19)	(10)	40	40	40
(g) Household's merger with Beneficial	(340)	(170)	(340)	(340)	(340)
	(359)	(180)	(300)	(300)	(300)
Provisions – for bad and doubtful debts					
(c) Receivables sold and serviced with limited recourse and securitisation revenue	(1,550)	(739)	(1,174)	(962)	(1,045)
(i) Interest suspension	4	5	12	9	17
	(1,546)	(734)	(1,162)	(953)	(1,028)
Tax on profit on ordinary activities					
(k) Tax effect of adjustments	184	76	107	46	39
(k) Tax credit on share compensation expense	11	7	36	24	89
	195	83	143	70	128
Total adjustments	(664)	(304)	(481)	(388)	(309)

Adjustments made to the balance sheet under each item described above to conform Household's US GAAP consolidated financial statements to HSBC's accounting policies under UK GAAP are as follows:

	At 30 June 2002	At 31 December 2001	At 31 December 2000	At 31 December 1999
	US\$m	US\$m	US\$m	US\$m
Loans and advances to customers				
(a) Deferred origination expenses	(386)	(347)	(242)	(162)
(c) Receivables sold and serviced with limited recourse and securitisation revenue ..	19,537	18,208	17,857	17,483
(i) Interest suspension	88	83	71	62
	19,239	17,944	17,686	17,383
Debt securities				
(e) Investment securities	—	(9)	—	(1)
	—	(9)	—	(1)
Intangible fixed assets				
(f) Goodwill	(809)	(799)	(839)	(879)
(g) Household's merger with Beneficial	5,443	5,613	5,953	6,293
	4,634	4,814	5,114	5,414
Tangible fixed assets				
(h) Costs of software for internal use	(33)	(16)	(9)	(7)
	(33)	(16)	(9)	(7)
Other assets				
(b) Derivative financial instruments	(535)	(97)	—	—
(c) Receivables sold and serviced with limited recourse and securitisation revenue ..	44	38	—	—
(e) Investment securities	8	7	76	110
(k) Income taxes	769	608	782	680
	286	556	858	790
Prepayments and accrued income				
(i) Interest suspension	(135)	(128)	(110)	(95)
	(135)	(128)	(110)	(95)
Customer accounts				
(b) Derivative financial instruments	(20)	(24)	—	—
	(20)	(24)	—	—
Debt securities in issue				
(b) Derivative financial instruments	(945)	442	—	—
(c) Receivables sold and serviced with limited recourse and securitisation revenue ..	21,439	19,966	19,141	18,580
	20,494	20,408	19,141	18,580
Other liabilities				
(k) Tax effect of adjustments to:				
Deferred origination expenses	(141)	(127)	(88)	(59)
Derivative financial instruments	299	390	—	—
Receivables sold and serviced with limited recourse and securitisation revenue ..	(678)	(627)	(469)	(400)
Investment securities	3	(1)	25	38
Goodwill	(222)	(221)	(232)	(244)
Costs of software for internal use	(12)	(6)	(4)	(3)
Interest suspension	(18)	(16)	(14)	(12)
(b) Derivative financial instruments	(438)	(1,603)	—	—
(d) Forward purchase agreements	341	381	300	—
(k) Income taxes	769	608	782	680
	(97)	(1,222)	300	—
Total adjustments to shareholders' funds	3,614	3,999	4,098	4,904
Ordinary share capital				
(d) Forward purchase agreements	(7)	(6)	(7)	—
Reserves				
(a) Deferred origination expenses	(245)	(220)	(154)	(103)
(b) Derivative financial instruments	569	698	—	—
(c) Receivables sold and serviced with limited recourse and securitisation revenue ..	(1,180)	(1,093)	(815)	(697)
(d) Forward purchase agreements recorded as a liability under UK GAAP	(334)	(375)	(293)	—
(e) Investment securities	5	(1)	51	71
(f) Goodwill	(587)	(578)	(607)	(635)
(g) Beneficial merger using acquisition accounting	5,443	5,613	5,953	6,293
(h) Costs of software for internal use	(21)	(10)	(5)	(4)
(i) Interest suspension	(29)	(29)	(25)	(21)
	3,621	4,005	4,105	4,904
Total adjustments to shareholders' funds	3,614	3,999	4,098	4,904

The following is a copy of a letter received from KPMG Audit Plc:



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The Directors
HSBC Holdings plc
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E14 5HQ

The Directors
Cazenove & Co. Ltd.
12 Tokenhouse Yard
London
EC2R 7AN

26 February 2003

Dear Sirs

HSBC Holdings plc's proposed acquisition of Household International, Inc.

We refer to the statement of significant adjustments which would be required to the consolidated profit and loss statement for each of the years in the three-year period ended 31 December 2001, and to the consolidated balance sheet as at 31 December 2001, 2000 and 1999 reported in the financial statements of Household International, Inc., prepared under United States Generally Accepted Accounting Principles, to restate the information in accordance with the accounting policies of HSBC Holdings plc (the "reconciliations"). The Directors of HSBC Holdings plc are solely responsible for the preparation of the reconciliations in accordance with paragraph 12.11 of the Listing Rules of the UK Listing Authority.

The reconciliations, which have been prepared for illustrative purposes only, are set out in Section C of Part II of the Circular dated 26 February 2003 issued by HSBC Holdings plc.

The reconciliations are based on:

- the audited balance sheets as at 31 December 2001 and 2000 and income statements for each of the years in the three-year period ended 31 December 2001 of Household International, Inc. which were audited by KPMG LLP (USA);
- the audited balance sheet of Household International, Inc. as at 31 December 1999 which was audited by Arthur Andersen LLP;
- the unaudited interim results of Household International, Inc. for the financial period ended 30 June 2002; and
- the unaudited earnings release of Household International, Inc. for the financial year ended 31 December 2002.



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registered to carry on audit
work by the Institute of
Chartered Accountants in

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Registered in England
No 3110745

Registered office
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We express no opinion on these financial statements, interim results or earnings release.

We have reviewed the calculations and basis of preparation for the reconciliations. We conducted our work in accordance with Statements of Investment Circular Reporting Standards issued by the Auditing Practices Board of the United Kingdom.

Our work has not been carried out in accordance with auditing or other standards generally accepted in the United States of America and accordingly should not be relied upon as if it had been carried out in accordance with those standards.

In our opinion the reconciliations have been properly compiled on the basis set out therein. Further, in our opinion the adjustments are appropriate for the purpose of presenting the financial information (as adjusted) on a basis consistent in all material respects with the accounting policies of HSBC Holdings plc.

Yours faithfully

KPMG Audit Plc

Part III: Unaudited Pro Forma Financial Information

HSBC and Household unaudited pro forma condensed combined financial information

The following unaudited pro forma condensed combined financial information and explanatory notes (“the pro forma financial information”) illustrate the impact of the Acquisition on the companies’ historical financial positions and results of operations under the acquisition method of accounting.

The pro forma financial information is presented for illustrative purposes only and, because of its nature, it may not give a true picture of what the operating results or the financial position of the enlarged group would have been had the Acquisition occurred on the respective dates assumed. Also, because of its nature, it may not give a true picture of future operating results or the financial position of the enlarged group.

The final determination of the purchase price will be based on the price of HSBC Ordinary Shares as at the Effective Date. In addition, the final allocation of the purchase price will be determined after completion of a thorough analysis to determine the fair values of Household’s assets and liabilities as at the Effective Date. Accordingly, the final acquisition accounting adjustments and goodwill may be materially different from those reflected in the pro forma financial information presented in this document.

HSBC and Household unaudited pro forma condensed combined statement of income for the half-year to 30 June 2002

	HSBC US\$m (Note 1)	Household US\$m (Note 1)	Acquisition accounting adjustments US\$m (Notes 3,4)	Pro forma enlarged HSBC group US\$m
Interest income	14,229	6,909	(254)	20,884
Interest expense	(6,636)	(2,262)	251	(8,647)
Net interest income	7,593	4,647	(3)	12,237
Other operating income	5,510	1,271	6	6,787
Operating income	13,103	5,918	3	19,024
Operating expenses excluding goodwill	(7,146)	(2,025)	32	(9,139)
Goodwill amortisation	(396)	(180)	(33)	(609)
Operating profit before provisions	5,561	3,713	2	9,276
Provisions for bad and doubtful debts and contingencies	(718)	(2,598)	—	(3,316)
Loss from foreign currency redenomination in Argentina	(45)	—	—	(45)
Amounts written off fixed asset investments	(139)	—	—	(139)
Operating profit	4,659	1,115	2	5,776
Share of operating profits less losses of associates and joint ventures	48	—	—	48
Gains on disposal of investments and fixed assets	350	—	—	350
Profit on ordinary activities before tax	5,057	1,115	2	6,174
Tax on profit on ordinary activities	(1,315)	(421)	(8)	(1,744)
Profit on ordinary activities after tax	3,742	694	(6)	4,430
Minority interests	(462)	—	—	(462)
Profit attributable to shareholders	3,280	694	(6)	3,968
Per ordinary share	US\$	US\$		US\$
— Basic earnings	0.35	1.49		0.38
— Diluted earnings	0.35	1.47		0.37
Average number of ordinary shares in issue (in millions)	9,298	450		10,564
Average number of ordinary shares in issue assuming dilution (in millions)	9,404	455		10,691

The notes to the unaudited pro forma condensed combined financial information are an integral part of this statement.

HSBC and Household unaudited pro forma condensed combined statement of income for the year ended 31 December 2001

	HSBC US\$m (Note 1)	Household US\$m (Note 1)	Acquisition accounting adjustments US\$m (Notes 3,4)	Pro forma enlarged HSBC group US\$m
Interest income	35,261	13,316	(861)	47,716
Interest expense	(20,536)	(5,213)	710	(25,039)
Net interest income	14,725	8,103	(151)	22,677
Other operating income	11,163	2,354	11	13,528
Operating income	25,888	10,457	(140)	36,205
Operating expenses excluding goodwill	(14,605)	(3,705)	99	(18,211)
Goodwill amortisation	(799)	(359)	(66)	(1,224)
Operating profit before provisions	10,484	6,393	(107)	16,770
Provisions for bad and doubtful debts and contingencies	(2,686)	(4,198)	—	(6,884)
Loss from foreign currency redenomination in Argentina	(520)	—	—	(520)
Amounts written off fixed asset investments	(125)	—	—	(125)
Operating profit	7,153	2,195	(107)	9,241
Share of operating profits less losses of associates and joint ventures	73	—	—	73
Gains on disposal of investments and fixed assets	774	—	—	774
Profit on ordinary activities before tax	8,000	2,195	(107)	10,088
Tax on profit on ordinary activities	(1,988)	(828)	(21)	(2,837)
Profit on ordinary activities after tax	6,012	1,367	(128)	7,251
Minority interests	(1,020)	—	—	(1,020)
Profit attributable to shareholders	4,992	1,367	(128)	6,231
Per ordinary share	US\$	US\$		US\$
— Basic earnings	0.54	2.94		0.59
— Diluted earnings	0.53	2.91		0.59
Average number of ordinary shares in issue (in millions)	9,237	459		10,503
Average number of ordinary shares in issue assuming dilution (in millions)	9,336	465		10,625

The notes to the unaudited pro forma condensed combined financial information are an integral part of this statement.

HSBC and Household unaudited pro forma condensed combined balance sheet as at 30 June 2002

	HSBC US\$m (Note 1)	Household US\$m (Note 1)	Adjustments		Pro forma enlarged HSBC group US\$m
			Subsequent adjustments US\$m (Note 2)	Acquisition accounting adjustments US\$m (Notes 3,4)	
ASSETS					
Cash and short-term assets	30,710	639	(114)	(1,440)	29,795
Hong Kong SAR Government certificates of indebtedness	8,986	—	—	—	8,986
Loans and advances to banks	100,965	244	—	—	101,209
Loans and advances to customers	342,057	100,880	—	2,060	444,997
Debt securities and equity shares	181,502	5,640	—	—	187,142
Interests in joint ventures, associates and participating interests	1,233	—	—	—	1,233
Intangible fixed assets	15,111	6,175	—	2,332	23,618
Tangible fixed assets	13,988	517	—	—	14,505
Other assets	51,783	7,580	—	141	59,504
Total assets	746,335	121,675	(114)	3,093	870,989
LIABILITIES					
Hong Kong SAR currency notes in circulation	8,986	—	—	—	8,986
Deposits by banks	61,455	684	—	—	62,139
Customer accounts	470,778	5,592	—	300	476,670
Debt securities in issue	28,683	96,678	(781)	1,420	126,000
Other liabilities	102,934	4,628	—	718	108,280
Subordinated liabilities	15,716	975	—	30	16,721
Minority interests	6,605	—	—	—	6,605
Ordinary share capital	4,725	450	23	160	5,358
Preference share capital	—	843	236	(1,079)	—
Reserves	46,453	11,825	408	1,544	60,230
Shareholders' funds	51,178	13,118	667	625	65,588
Total liabilities	746,335	121,675	(114)	3,093	870,989

The notes to the unaudited pro forma condensed combined financial information are an integral part of this statement.

HSBC and Household notes to unaudited pro forma condensed combined financial information

Note 1 – Basis of presentation

The pro forma financial information for the year ended 31 December 2001 and for the half-year to 30 June 2002 is presented on a UK GAAP basis and combines the following:

- HSBC's historical financial information for the year ended 31 December 2001 (as restated following implementation of FRS 19 "Deferred Tax") and HSBC's unaudited interim report for the half-year to 30 June 2002.
- Household's historical financial information on a US GAAP basis for the year ended 31 December 2001 and for the half-year to 30 June 2002, adjusted to conform with HSBC's accounting policies under UK GAAP as described in section C of Part II.
- Adjustments to give effect to share capital transactions in Household subsequent to 30 June 2002 as described in Note 2.
- Pro forma adjustments related to acquisition accounting utilising the fair values of Household's assets and liabilities as at 30 June 2002 as described in Notes 3 and 4.

The unaudited pro forma condensed combined balance sheet as at 30 June 2002 assumes the Acquisition was completed on that date. The unaudited pro forma condensed combined statements of income for the half-year to 30 June 2002 and for the year ended 31 December 2001 give effect to the Acquisition as if the Acquisition had been completed on 1 January 2001, the first day of the earliest financial period presented.

The pro forma financial information includes estimated costs and adjustments to record certain assets and liabilities of Household at their respective fair values. The pro forma costs and adjustments represent HSBC management's best estimate based on available information at this time. They are subject to updates as variables change, additional information becomes available and additional analyses are performed. For the purpose of the pro forma financial information, the purchase price has been based on the closing mid-market price of an HSBC Ordinary Share on the London Stock Exchange on 13 November 2002, the last day prior to the public announcement of the signing of the Merger Agreement. The final determination of the purchase price is based upon the price of HSBC Ordinary Shares as at the Effective Date. In addition, the final allocation of the purchase price will be determined after completion of a thorough analysis to determine the fair values of Household's assets and liabilities as at the Effective Date. Accordingly, the final acquisition accounting adjustments and goodwill may be materially different from those reflected in the pro forma financial information presented herein.

Additionally, changes to Household's shareholders' funds including retained net income from 1 July 2002 to the date the Acquisition is completed will also affect the amount of goodwill recorded as the pro forma financial information does not include net income for any period subsequent to 30 June 2002 nor does it reflect two significant items announced subsequent to 30 June 2002. These items comprise:

- (i) the US\$525 million pre-tax charge recorded by Household in the third quarter of 2002 related to Household's agreement in principle with a multi-state working group of US state attorneys general and regulatory agencies to effect a nationwide resolution of alleged violations of US federal and state consumer protection, consumer finance and banking laws and regulations related to real estate secured lending from its retail branch consumer lending operations as operated under the HFC and Beneficial brand names; and
- (ii) the impact of Household's announcement on 11 October 2002 that it had determined that the continued operation of Household Bank, f.s.b. ("Household Bank") was not in its long-term strategic interest. During the fourth quarter of 2002, Household completed the sale of substantially all of the remaining assets and deposits of Household Bank. A loss of US\$240 million (after tax) was recorded on the disposal of these assets and deposits. However, the fair value of Household Bank's assets and liabilities as at 30 June 2002 is reflected in the acquisition accounting adjustments in the unaudited pro forma condensed combined balance sheet as at 30 June 2002.

HSBC and Household entered into the Merger Agreement with the expectation that the Acquisition would result in significant funding benefits, cost and revenue synergies and cost savings in the areas of information technology, administrative support and consolidating of card processing. The pro forma financial information

does not include any impact of the expected benefits and synergies and there can be no assurance that the enlarged group will realise these anticipated benefits in full or at all.

The pro forma financial information is presented for illustrative purposes only and is not necessarily indicative of the operating results that would have occurred or the financial position of the enlarged group if the Acquisition had been completed during the period or as at the date for which the pro forma financial information is presented, nor is it necessarily indicative of future operating results or the financial position of the enlarged group.

Note 2 – Subsequent adjustments

The pro forma financial information includes adjustments for Household share capital transactions occurring subsequent to 30 June 2002 that impact the purchase price. The following table reconciles common stock outstanding and shareholders' funds derived from Household's unaudited historical financial statements to the amounts included in the pro forma financial information prior to the acquisition accounting adjustments.

	Common stock outstanding	Total shareholders' funds US\$m
Household on a U.K. GAAP basis – 30 June 2002 (see section IIc)	450,491,376	13,118
Subsequent share capital movements:		
September 2002 preferred stock offering	—	350
October 2002 common stock offering	18,700,000	400
October 2002 Household Equity Units offering (21,663,000 units of which US\$1.45 per unit was allocated to shareholders' funds)	—	31
	<hr/> 469,191,376	<hr/> 13,899
Acquisition related transactions:		
Restricted stock rights which fully vest upon completion of the Acquisition	4,077,074	—
Preferred stock to be redeemed by Household prior to the Acquisition (5%, US\$4.30 and US\$4.50 cumulative issuances)	—	(114)
	<hr/> 473,268,450	<hr/> 13,785
Household shareholders' funds (see note 4)		13,785
Of which preferred stock to be purchased by HSBC		1,079

Note 3 – Acquisition accounting adjustments

The unaudited pro forma balance sheet as at 30 June 2002 includes pro forma acquisition adjustments related to the computation of the purchase price and allocation of the purchase price to the tangible assets and liabilities of Household as described in Note 1.

The unaudited pro forma income statements for the half-year to 30 June 2002 and for the year ended 31 December 2001 include amortisation of the goodwill and fair value adjustments determined as at 30 June 2002. HSBC proposes to amortise the goodwill arising on the Acquisition over a period of 20 years. The fair value adjustments to tangible assets and liabilities are amortised over the remaining lives of the relevant assets and liabilities.

In addition, the unaudited pro forma condensed combined income statements for the half-year to 30 June 2002 and for the year ended 31 December 2001 are adjusted to:

- exclude the amortisation of Household's existing goodwill and intangible assets under UK GAAP; and
- exclude the dividends payable on the preferred stock of Household which is redeemable on completion of the Acquisition and reduce pro forma interest income on the cash consideration payable by Household and HSBC on such redemption.

Acquisition accounting adjustments are summarised as follows:

		Half-year to 30 June 2002 US\$m	Year ended 31 December 2001 US\$m
Interest income			
Amortisation of fair value adjustment to receivables		(244)	(813)
Reduction of interest receivable from debt securities		(10)	(48)
		(254)	(861)
Interest expense			
Amortisation of fair value adjustments relating to:			
Derivatives		30	190
Deposits		52	142
Senior debt		168	377
Subordinated liabilities		1	1
		251	710
Other operating income			
Amortisation of fair value adjustments to insurance reserve and investment securities		6	11
Operating expenses excluding goodwill			
Reversal of current year amortisation of intangibles		32	99
Goodwill amortisation			
Amortisation of goodwill		(33)	(66)
Tax on profit on ordinary activities			
Tax effect of reversing amortisation of fair value adjustments		(8)	(21)
		(6)	(128)
			At 30 June 2002
	Note	US\$m	US\$m
Cash and short-term assets			
Redemption cost of preference shares	4A(iv)	(1,100)	
Acquisition expenses	4A(v), 4D	(295)	
Employment agreements	4C(i)	(45)	
			(1,440)
Loans and advances to customers			
Fair value adjustment (including provision of US\$200 million)	4B(ii), 4C(ii)		2,060
Intangible fixed assets			
Goodwill on acquisition	4D	8,507	
Pre-acquisition goodwill and existing intangible fixed assets	4B(i)	(6,175)	
			2,332
Other assets			
Fair value adjustment to derivatives receivable	4B(ii)	535	
Fair value adjustment to pensions	4B(ii)	(387)	
Fair value adjustment to insurance investments	4B(ii)	(7)	
			141
Customer accounts			
Fair value adjustment	4B(ii)		(300)
Debt securities in issue			
Fair value adjustment	4B(ii)		(1,420)
Other liabilities			
Fair value adjustment to derivatives liability	4B(ii)	(455)	
Fair value adjustment to other liabilities	4B(ii)	(175)	
Fair value adjustment to periodic payment annuity	4B(ii)	(270)	
Taxation on fair value adjustments	4B(iii)	207	
Acquisition expenses	4A(v), 4D	(25)	
			(718)
Subordinated liabilities			
Fair value adjustment	4D		(30)
Total adjustment to shareholders' funds			625

Note 4 – Purchase price computation and allocation

A The computation of the purchase price on a UK GAAP basis included in the unaudited pro forma financial information is based on the following:

- (i) the value of HSBC Ordinary Shares to be issued in exchange for 473,268,450 Household Common Shares (as explained in Note 2) based on the closing mid-market price of an HSBC Ordinary Share on the London Stock Exchange on 13 November 2002, the last day prior to the public announcement of the signing of the Merger Agreement, and the Exchange Ratio of 2.675 HSBC Ordinary Shares for each Household Common Share;
- (ii) the fair value as at 30 June 2002 of options outstanding at that date to purchase Household Common Shares granted to Household employees and directors under Household's option plans. When HSBC and Household complete the Acquisition, all Household options will vest (except for options granted after 14 November 2002) and will be assumed by HSBC and become options to purchase HSBC Ordinary Shares. The number of HSBC Ordinary Shares subject to these options and the exercise price of the options will be adjusted to reflect the Exchange Ratio;
- (iii) the fair value of the conversion obligations of the 8.875% Household Equity Units issued in October 2002. When HSBC and Household complete the Acquisition, the obligation of the holders of Household Equity Units to purchase Household Common Shares will become obligations to purchase HSBC Ordinary Shares. The number of HSBC Ordinary Shares subject to these obligations and price at which they are to be issued will be adjusted to reflect the Exchange Ratio;
- (iv) the cash consideration to be paid by HSBC to the holders of Household Non-voting Preferred Stock; and
- (v) the acquisition costs to be paid by HSBC estimated at US\$265 million. Of this amount, US\$213 million relates to UK stamp duty or stamp duty reserve tax, the calculation of which assumes all Household Common Shareholders elect to receive HSBC ADSs rather than HSBC Ordinary Shares.

No account has been taken in the determination of the purchase price for the purpose of the pro forma financial information of the value of the HSBC 2002 second interim dividend to which economic benefit the Household Common Shareholders are entitled under the Merger Agreement. HSBC expects to declare the amount of the 2002 second interim dividend in March 2003 and pay it in May 2003.

B In allocating the purchase price to the tangible assets and liabilities of Household, adjustments have been made to:

- (i) eliminate Household's existing goodwill and intangibles under UK GAAP as at 30 June 2002, which relate primarily to the acquisition of Beneficial in 1998;
- (ii) reflect the respective fair values of the tangible assets and liabilities of Household as at 30 June 2002; and
- (iii) reflect the taxation effect on (ii) above.

C The fair value adjustments relate primarily to the valuation of Household's financial assets and liabilities (including derivatives) considering market rates as at 30 June 2002. The fair value adjustments also include amounts relating to change in control payments and the provision for bad and doubtful debts as follows:

- (i) of the amount payable under 10 employment agreements which will come into effect on the completion of the Acquisition, HSBC has estimated that an amount of approximately US\$45 million would have been payable under employment arrangements existing prior to 13 November 2002 and this amount has been included as a fair value adjustment. HSBC intends to record a charge, in addition, of US\$55 million in connection with such agreements immediately after completion of the Acquisition; and

- (ii) HSBC's policies on loan loss provisioning on consumer assets are in principle the same as those of Household, seeking to maintain, on a prudent and consistent basis, amounts sufficient to cover probable losses of principal, interest and fees based on analyses of trends in contractual delinquency and historical loss experience. HSBC intends, following the Acquisition and subject to receipt of regulatory and other approvals, to hold Household's private label credit card receivables within HSBC's US banking subsidiary. As a result, HSBC anticipates that regulatory accounting charge-off guidelines issued by the Federal Financial Institutions Examination Council ("FFIEC"), will need to be applied to these receivables following completion of the Acquisition. Implementation of these guidelines will result in private label credit card receivables being charged-off at 6 months contractually delinquent compared with the current Household practice of charging-off at 9 months contractually delinquent. HSBC's plans for ultimate collection on certain of these receivables will therefore be demonstrably different from those of Household due to the shorter charge-off period. As a result, the fair value adjustments include an adjustment to the provision for bad and doubtful debts for these private label credit card receivables of approximately US\$200 million to reflect the expected impact of the implementation of the FFIEC guidelines.

D The initial computation of the purchase price, the allocation of the purchase price to the net tangible assets of Household based on fair values estimated at 30 June 2002, and the resulting amount of goodwill under UK GAAP are presented below.

	US\$m	US\$m
Purchase price:		
Value of HSBC ordinary shares to be issued		14,217
Fair value of outstanding Household stock options		140
Fair value of equity portion of Household Equity Units		53
Cash consideration to be paid by HSBC for cumulative preferred stock		1,100
Acquisition costs payable by HSBC		265
		<hr/>
Total purchase price		15,775
Less:		
Tangible net assets acquired:		
Household shareholders' funds (see note 2)	13,785	
Less: Household existing intangibles including goodwill	(6,175)	
	<hr/>	
Book value of tangible net assets acquired	7,610	
Fair value adjustments	(287)	
	<hr/>	
Fair value of tangible net assets acquired		(7,323)
Acquisition costs payable by Household		55
		<hr/>
Goodwill		8,507
		<hr/>

The following is a copy of a letter received from KPMG Audit Plc:



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The Directors
HSBC Holdings plc
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E14 5HQ

The Directors
Cazenove & Co. Ltd.
12 Tokenhouse Yard
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EC2R 7AN

26 February 2003

Dear Sirs

HSBC Holdings plc's proposed acquisition of Household International, Inc.

We report on the pro forma financial information set out in Part III of the Circular dated 26 February 2003 issued by HSBC Holdings plc, which has been prepared, for illustrative purposes only, to provide information about how the proposed acquisition of Household International, Inc., might have affected the financial information presented.

Responsibilities

It is the responsibility solely of the Directors of HSBC Holdings plc to prepare the pro forma financial information in accordance with paragraph 12.29 of the Listing Rules of the UK Listing Authority.

It is our responsibility to form an opinion, as required by the Listing Rules of the UK Listing Authority, on the pro forma financial information and to report our opinion to you. We do not accept any responsibility for any reports previously given by us on any financial information used in the compilation of the pro forma financial information beyond that owed to those to whom those reports were addressed by us at the dates of their issue.

Basis of opinion

We conducted our work in accordance with the Statements of Investment Circular Reporting Standards and Bulletin 1998/8 "Reporting on pro forma financial information pursuant to the Listing Rules" issued by the Auditing Practices Board of the United Kingdom. Our work, which involved no independent examination of any of the underlying financial information, consisted primarily of comparing the unadjusted financial information with the source documents, considering the evidence supporting the adjustments and discussing the pro forma financial information with the Directors of HSBC Holdings plc.



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registered to carry on audit
work by the Institute of
Chartered Accountants in

England and Wales
Registered in England
No 3110745

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Our work has not been carried out in accordance with auditing or other standards generally accepted in the United States of America and accordingly should not be relied upon as if it had been carried out in accordance with those standards.

Opinion

In our opinion:

- the pro forma consolidated financial information has been properly compiled on the basis stated;
- such basis is consistent with the accounting policies of HSBC Holdings plc; and
- the adjustments are appropriate for the purposes of the pro forma financial information as disclosed pursuant to paragraph 12.29 of the Listing Rules of the UK Listing Authority.

The above opinion is provided solely on the basis of and in accordance with standards and practice established in the United Kingdom. In the United States, reporting standards and practice are different and the role of the reporting accountant does not provide for the expression of an opinion in the manner referred to above. Accordingly, this opinion should not be relied upon as if it had been provided in accordance with United States standards.

Yours faithfully

KPMG Audit Plc

Part IV: Description of the Acquisition

A. Summary of the Terms of the Acquisition

A summary of the principal terms of the Acquisition is set out below. A copy of the Merger Agreement was filed with the SEC on 20 December 2002 as an annexure to the Proxy Statement/Prospectus and is available on the HSBC Group's website at www.hsbc.com. It is also available for inspection as stated in paragraph 13 of Part V of this document.

1 Nature of the Acquisition

- 1.1 If all conditions to the Acquisition are waived or satisfied in accordance with the Merger Agreement, the Acquisition will be effected by a statutory merger under the laws of the state of Delaware whereby Household will be merged with and into H2 (a wholly owned subsidiary of HSBC Holdings) and Household will cease to exist as a separate corporate entity. H2 shall be the surviving corporation in the merger. All the rights, privileges, immunities, powers and franchises of Household shall vest in H2 and all debts, liabilities and duties of Household shall become the debts, liabilities and duties of the surviving corporation. Following the Acquisition, H2 will continue to be a wholly owned subsidiary of HSBC Holdings but will be renamed "Household International, Inc."
- 1.2 On the Effective Date, the consideration will be issued for the benefit of the Household Shareholders as set out in paragraphs 2 and 3 below. The Household Common Shares, the Household Non-voting Preferred Stock and existing shares of H2 will be cancelled and H2 will issue 50 new shares of common stock to HSBC Holdings.

2 Consideration to be Delivered in the Acquisition

- 2.1 Under the terms of the Acquisition, Household Common Shareholders (other than HSBC Holdings or any subsidiary of HSBC Holdings or Household unless holding for the account or benefit of any customer, client or other person, or Household in respect of Household Common Shares held in treasury) will be entitled to receive on completion of the Acquisition, at their election:

for each Household Common Share held at the Effective Date	either 2.675 HSBC Ordinary Shares or 0.535 HSBC ADSs (each HSBC ADS representing five HSBC Ordinary Shares) (the "Exchange Ratio").
--	---

- 2.2 Household Common Shareholders who would otherwise have been entitled to receive a fractional interest in an HSBC Ordinary Share or an HSBC ADS will receive, in lieu thereof, a cash payment calculated by one of two possible methods (at HSBC Holdings' election, to be made prior to the Effective Date). Either:
- 2.2.1 the Exchange Agent will aggregate and sell from time to time on the London Stock Exchange the fractional interests in New HSBC Ordinary Shares (including New HSBC Ordinary Shares underlying fractional interests in HSBC ADSs) that would otherwise be issued. For each fractional interest in HSBC Ordinary Shares or HSBC ADSs that otherwise would have been issued to them, Household Common Shareholders will receive a proportionate interest in the net proceeds (after commissions, transfer taxes and other out-of-pocket transactions costs, including customary expenses of the Exchange Agent) of these sales. As fractional interests will be aggregated and sold from time to time after completion of the Acquisition as Household Common Shares are surrendered for exchange, the market value of an HSBC Ordinary Share upon which this cash amount is based will vary and different cash amounts will be received with respect to fractional interests, depending on when Household Common Shares are surrendered for exchange. Household Common Shareholders will have no recourse against HSBC Holdings, Household, the Exchange Agent, the Depositary or any other person as a result of the difference; or
- 2.2.2 HSBC Holdings will pay each Household Common Shareholder an amount equal to the amount of the fractional share interest to which such shareholder would otherwise be entitled multiplied by either: (a) the closing mid-market price of an HSBC Ordinary Share (disregarding extended hours) on the Effective Date (as reported in the Daily Official List) if such shareholder elects to receive HSBC Ordinary Shares; or (b) the closing price (disregarding extended hours) on the Effective Date of an HSBC ADS (as reported in the Wall Street Journal (US National Edition)) if such shareholder elects to receive HSBC ADSs.

- 2.3 Household Common Shareholders who receive HSBC Ordinary Shares or HSBC ADSs will be entitled to receive or participate in all dividends and distributions payable on such HSBC Ordinary Shares or on the HSBC Ordinary Shares represented by such HSBC ADSs that have a record date on or after the Effective Date.
- 2.4 On the Effective Date, each issued and outstanding share of the Household Non-voting Preferred Stock will be cancelled and holders of such stock will be entitled to receive a cash payment of US\$1,000 per share (US\$25 per depository share, each depository share representing 0.025 of a share of Household Non-voting Preferred Stock), plus all accrued and unpaid dividends (without interest) up to but excluding the Effective Date. Holders of the Household Non-voting Preferred Stock are entitled to assert dissenters' appraisal rights under Delaware law instead of receiving this consideration.
- 2.5 Immediately prior to the completion of the Acquisition, Household will deposit the redemption price of the Household Voting Preferred Stock in trust for the holders of such shares and take all steps required to redeem the Household Voting Preferred Stock in accordance with their terms. Under their terms, these shares will no longer be deemed to be outstanding upon the deposit in trust of the redemption price. The aggregate amount of the redemption price of the Household Voting Preferred Stock is approximately US\$114 million, plus accrued and unpaid dividends up to but excluding the Effective Date.
- 2.6 Pursuant to their terms, the Household Equity Units will remain outstanding, with the purchase contracts that form a portion of such Household Equity Units becoming contracts to purchase HSBC Ordinary Shares in lieu of Household Common Shares.
- 2.7 Pursuant to their terms, the rights to acquire Household Common Shares under the Household Zero-coupon Debt Securities will be converted, as a consequence of the Acquisition, into rights to acquire HSBC Ordinary Shares.

3 Share Options and Other Employee Benefits

- 3.1 On the Effective Date, each outstanding and unexercised option to acquire Household Common Shares held by any current or former employee or director of Household will be assumed by HSBC Holdings and converted into a right to acquire such number of HSBC Ordinary Shares as is equal to the number of Household Common Shares subject to the option multiplied by the Exchange Ratio. The exercise price of such options will also be adjusted to reflect the Exchange Ratio.
- 3.2 On the Effective Date, each right to receive Household Common Shares, including Household restricted stock rights, or benefits measured based on the value of Household Common Shares, will cease to represent the right to receive Household Common Shares or benefits measured thereby, and will be converted into a right to receive such number of HSBC Ordinary Shares or benefits measured thereby equal to the number of Household Common Shares subject to such right multiplied by the Exchange Ratio.
- 3.3 The options referred to in paragraph 3.1 above granted prior to 14 November 2002 will become exercisable immediately following the Effective Time. Restricted stock rights in respect of Household Common Shares granted prior to 14 November 2002 will vest immediately prior to the Effective Time and will be converted, pursuant to the Merger Agreement, into HSBC Ordinary Shares or HSBC ADSs, at the holder's election. Options and restricted stock rights granted after 14 November 2002 will not vest on the Effective Date as a consequence of the Acquisition. All converted options and rights referred to in paragraphs 3.1 and 3.2 above (whenever granted) will continue to be subject to the same terms and conditions as were applicable to them immediately prior to the Effective Time. At or prior to the time that the holder of such an option or right is entitled to receive HSBC Ordinary Shares pursuant to such option or right, the holder will be able to choose between receiving HSBC Ordinary Shares and HSBC ADSs.
- 3.4 Each outstanding purchase right under the Household Employee Stock Purchase Plan shall be exercised at least three Business Days prior to the Effective Date and no further purchase period shall commence under the Household Employee Stock Purchase Plan after that date (assuming the Acquisition becomes effective). At least three Business Days prior to the Effective Date, all purchases of Household Common Shares under the Household Dividend Reinvestment and Common Stock Purchase Plan shall cease (assuming the Acquisition becomes effective). Holders of Household Common Shares received under the

Household Stock Purchase Plans shall be entitled to receive the consideration described in paragraph 2 above. On the Acquisition becoming effective, the Household Stock Purchase Plans will be terminated.

4 Shareholder Approvals and Other Conditions

- 4.1 HSBC Holdings and Household will not complete the Acquisition pursuant to the Merger Agreement unless certain conditions are satisfied or waived by them. These include:
 - 4.1.1 the registration statement on Form F-4 of HSBC Holdings (the “F-4 Registration Statement”) having become effective under the US Securities Act of 1933, as amended, no stop order suspending the effectiveness of the F-4 Registration Statement having been issued and no stop order proceedings having been initiated or threatened by the SEC;
 - 4.1.2 approval for admission to listing or trading (as the case may be) having been granted on the Official List of the UK Listing Authority, the London Stock Exchange, the Hong Kong Stock Exchange and Euronext Paris and authorisation for listing of the HSBC Ordinary Shares and HSBC ADSs on the New York Stock Exchange having been granted, subject to official notice of issuance;
 - 4.1.3 approval of the Acquisition and the other transactions contemplated by the Merger Agreement by Household Shareholders and by HSBC Shareholders having been obtained;
 - 4.1.4 approvals of the Acquisition and the other transactions contemplated by the Merger Agreement by applicable governmental and regulatory agencies having been received;
 - 4.1.5 the absence of any statute, order, injunction or similar legal obstacle prohibiting the completion of the Acquisition; and
 - 4.1.6 the Household Voting Preferred Stock being deemed not outstanding by reason of Household’s deposit of the redemption price.
- 4.2 The obligation of HSBC Holdings to complete the Acquisition is subject to the satisfaction or waiver by HSBC Holdings, prior to the Effective Date, of the following conditions:
 - 4.2.1 the representations and warranties of Household set out in the Merger Agreement being true and correct as at the date of the Merger Agreement and (except to the extent any such representation and warranty speaks as of an earlier date) as at the Effective Date, provided such representations and warranties generally will only be deemed to be untrue or incorrect as a consequence of the existence or absence of any fact, circumstance or event which has had or would be reasonably likely to have a Material Adverse Effect;
 - 4.2.2 Household having performed in all material respects all obligations required to be performed by it under the Merger Agreement and HSBC Holdings having received a certificate to that effect;
 - 4.2.3 HSBC Holdings having received a tax opinion from its US counsel, to the effect that the Acquisition will qualify as a reorganisation within the meaning of the US Tax Code and that each transfer of property to HSBC Holdings by a stockholder of Household pursuant to the Acquisition will not be subject to section 367(a)(1) of the US Tax Code;
 - 4.2.4 no governmental or regulatory consent required to be obtained as a condition to the Acquisition being conditional on the imposition of a Burdensome Condition (as defined in the Merger Agreement); and
 - 4.2.5 the absence of any pending or threatened suits, actions or proceedings by a governmental or regulatory agency seeking to restrain or prohibit the completion of the Acquisition or any other transaction contemplated by the Merger Agreement, seeking to impose any Burdensome Condition or which otherwise would reasonably be expected to have a Material Adverse Effect on HSBC Holdings or Household.
- 4.3 The obligation of Household to complete the Acquisition is subject to the satisfaction or waiver by Household, prior to the Effective Date, of additional conditions substantially similar to the conditions described in paragraphs 4.2.1 and 4.2.2 above, except that references to HSBC Holdings are replaced with

references to Household and references to Household are replaced with references to HSBC Holdings. In addition, Household's obligation to complete the Acquisition is subject to it having received from its US counsel a similar tax opinion as described in paragraph 4.2.3 above.

- 4.4 Neither HSBC Holdings nor Household intends to waive the condition that it has received a favourable tax opinion from its US counsel.

5 Share Exchange Procedures

- 5.1 HSBC Holdings has appointed the Exchange Agent for the purpose of exchanging certificates formerly representing Household Common Shares and shares of Household Non-voting Preferred Stock for HSBC Ordinary Shares or HSBC ADSs or cash, as the case may be. The Exchange Agent will send to each holder of record as at the Effective Time of Household Common Shares or Household Non-voting Preferred Stock a letter of transmittal for use in effecting delivery of certificates representing such shares or stock to the Exchange Agent. The letter of transmittal will require each Household Common Shareholder to make an election to receive either HSBC Ordinary Shares or HSBC ADSs. If a Household Common Shareholder does not make an election, the Exchange Agent will return the letter of transmittal to the holder for completion. If a Household Common Shareholder elects to receive HSBC Ordinary Shares, the holder will receive the HSBC Ordinary Shares in certificated form unless the holder elects in the letter of transmittal to receive them in uncertificated form through CREST.
- 5.2 On surrendering a certificate representing Household Common Shares for cancellation to the Exchange Agent together with a duly executed letter of transmittal, the holder will be entitled to receive in exchange:
- 5.2.1 the whole number of HSBC Ordinary Shares or HSBC ADSs that the Household Common Shareholder has the right to receive pursuant to the Merger Agreement;
- 5.2.2 the amount of any cash in lieu of fractional HSBC Ordinary Shares or HSBC ADSs as described in paragraph 2.2 above; and
- 5.2.3 any dividends or other distributions on the HSBC Ordinary Shares or HSBC ADSs, as the case may be, that have a record date after the Effective Date and shall have been declared and paid prior to the exchange (in the event that a dividend or other distribution has a record date after the Effective Date and has been declared but not yet paid prior to the exchange, the holder will be entitled to be paid such dividend or other distribution at the same time as all other holders of HSBC Ordinary Shares and/or HSBC ADSs).
- 5.3 On surrendering a certificate representing Household Non-voting Preferred Stock for cancellation to the Exchange Agent together with a duly executed letter of transmittal, the holder will be entitled to receive in exchange:
- 5.3.1 cash in the amount of US\$25 per depositary share; and
- 5.3.2 all accumulated and unpaid dividends up to but excluding the Effective Date, without interest.
- 5.4 With respect to both Household Common Shares and Household Non-voting Preferred Stock, taxes will be withheld as required.
- 5.5 Household certificates that are surrendered will be cancelled. No holder of unsurrendered certificates will receive any dividends or other distributions in respect of HSBC Ordinary Shares or HSBC ADSs to which the holder is entitled under the Merger Agreement, or be entitled to vote such HSBC Ordinary Shares, until the Household certificate registered to the holder is surrendered to the Exchange Agent. No interest will be paid or accrued on any amount payable on surrender of certificates.

6 Conduct of Business Pending the Acquisition

- 6.1 Subject to certain exceptions, Household has agreed that, except with the prior written consent of HSBC Holdings, Household will conduct its business in the ordinary course consistent with past practice and will use reasonable best efforts to preserve its present business organisations, to keep available the services of current officers and key employees and preserve existing relationships and goodwill with persons with whom it does business until the Effective Date. Household has also agreed that, prior to the Effective

Date, it will not, among other things, do any of the following except with HSBC Holdings' prior written consent or as disclosed to HSBC Holdings prior to the execution of the Merger Agreement:

- 6.1.1 declare or pay dividends other than the regular cash dividends in respect of the Household Voting Preferred Stock, the Household Non-voting Preferred Stock and the regular Household fourth quarter cash dividend in respect of Household Common Shares, save that in the event that the Acquisition will not be completed until after the record date for HSBC's second interim dividend in lieu of final dividend for 2002, the Household board of directors is entitled in its discretion to declare and pay additional cash dividends on the Household Common Shares, and otherwise to take appropriate steps, so that Household Common Shareholders receive, prior to the Effective Date, further dividends per Household Common Share up to, in total, 2.675 times the HSBC Holdings second interim dividend per HSBC Ordinary Share, unless HSBC Holdings has taken alternative steps, reasonably acceptable to Household, to provide the same economic benefit of such dividend to Household Common Shareholders;
- 6.1.2 split, combine or reclassify any capital stock of Household or its subsidiaries;
- 6.1.3 amend the terms of any option, warrant or right to acquire any securities of Household or its subsidiaries;
- 6.1.4 settle, pay or discharge any suit arising out of a shareholder's equity interest in Household;
- 6.1.5 purchase, redeem, or modify the terms of any indebtedness of Household or its subsidiaries;
- 6.1.6 (other than the issue of Household Common Shares pursuant to the Household Option Plans or the Household Stock-based Awards) issue, sell, pledge, dispose of or encumber, any shares of capital stock of any class or options or other ownership interest in Household or its subsidiaries;
- 6.1.7 amend any charter documents of Household or its subsidiaries;
- 6.1.8 acquire or agree to acquire any business other than acquisitions of consumer finance receivables in the ordinary course of business in accordance with past practices for cash consideration;
- 6.1.9 (except for borrowings under existing credit facilities or refinancing existing indebtedness) incur any indebtedness for borrowed money or issue debt securities or assume, guarantee or take responsibility for the obligations of any person other than one of its wholly owned subsidiaries, except in the ordinary course of business;
- 6.1.10 sell, encumber or subject to any lien any material properties or assets other than in the ordinary course of business;
- 6.1.11 change its accounting methods, except as required by changes in applicable law;
- 6.1.12 restructure or materially change its investment securities portfolio or its gap position;
- 6.1.13 pay or settle any litigation, claims or obligations in excess of US\$1 million, other than in the ordinary course of business consistent with past practice or liabilities incurred in the ordinary course of business since 30 September 2002 or contemplated by Household's financial statements included in its filings with the SEC made before 1 November 2002;
- 6.1.14 amend, except in the ordinary course of business, or knowingly violate in any material respect the terms of any material contracts, or create, renew or amend any agreement or contract containing any restriction on its ability to conduct its business as it is currently conducted or to engage in any type of activity or business; or
- 6.1.15 agree or consent to any material agreements or material modifications of any agreement with any governmental entity in respect of the operations of its business (except: (a) consent decrees contemplated by the Multi-State Settlement Agreement; (b) as required by law, to renew company permits or agreements in accordance with ordinary practice; or (c) to effect the transactions contemplated by the Merger Agreement).

- 6.2 Subject to certain exceptions, HSBC Holdings has agreed that, prior to the Effective Date, it will not, among other things, do any of the following:
- 6.2.1 declare or pay dividends, other than the second interim dividend in lieu of final dividend for 2002 in respect of HSBC Ordinary Shares;
 - 6.2.2 split, combine or reclassify any share capital of HSBC Holdings;
 - 6.2.3 acquire or agree to acquire any other corporation or other business organisation, unless such action would not reasonably be expected to delay or impede the Acquisition; or
 - 6.2.4 amend any constitutional documents of HSBC Holdings or its subsidiaries in a manner that would materially delay or impede the Acquisition or be adverse to HSBC Shareholders.

7 No Solicitation

- 7.1 In addition to its obligations set out in paragraph 6 above, Household has agreed that it and its representatives will not:
- 7.1.1 solicit, initiate or encourage (including by way of furnishing information), or take any other action designed to facilitate any inquiries or proposals regarding any merger, share exchange, consolidation, sale of assets, sale of shares of capital stock (including, without limitation, by way of a tender offer) or any similar transactions involving Household or its subsidiaries that, if completed, would constitute an Alternative Transaction (as defined below) (any such inquiry or proposal being an "Acquisition Proposal");
 - 7.1.2 participate in any discussions or negotiations regarding an Alternative Transaction; or
 - 7.1.3 enter into any agreement regarding any Alternative Transaction.

An "Alternative Transaction" means:

- (a) any transaction through which any person other than HSBC Holdings or its affiliates, directly or indirectly, acquires or would acquire more than 25 per cent of the outstanding Household Common Shares or voting power or of any new class or series of preferred stock that would be entitled to a class or a series vote with respect to the Acquisition whether from Household or pursuant to a tender offer or otherwise;
 - (b) any merger or other business combination involving Household (other than the Acquisition);
 - (c) any transaction through which any person other than HSBC Holdings or its affiliates acquires or would acquire control of assets (including for this purpose, equity securities of Household and equity securities of the entity surviving any merger or business combination including any of Household's subsidiaries) of Household or any of its subsidiaries representing more than 25 per cent of the fair market value of all the assets, net revenues or net income of Household and its subsidiaries; or
 - (d) any other consolidation, business combination, recapitalisation or similar transaction other than those contemplated by the Merger Agreement as a result of which the Household Common Shareholders immediately prior to such transaction do not, in the aggregate, own at least 75 per cent of each of the outstanding common stock and the voting power of the surviving or resulting entity in substantially the same proportion as those holders held the Household Common Shares immediately prior to the transaction.
- 7.2 However, Household and its board are not prohibited from considering and participating in discussions and negotiations with respect to a bona fide Acquisition Proposal received by Household if Household's board:
- 7.2.1 concludes in good faith that the Acquisition Proposal would, if accepted, be reasonably capable of being completed and would, if completed, constitute a Superior Proposal (as defined below) not solicited in violation of the Merger Agreement; and

- 7.2.2 determines in good faith (after consultation with outside legal counsel) that failure to do so would be inconsistent with the directors' fiduciary duties.

If Household does not limit the duration of these discussions and negotiations to 20 days, HSBC Holdings has the right to terminate the Merger Agreement and would be entitled to a termination fee of US\$550 million if Household agrees to an Alternative Transaction, or if an Alternative Transaction is completed, within 12 months after HSBC Holdings terminates the Merger Agreement.

A "Superior Proposal" means an Acquisition Proposal made by a third party which the Household board reasonably believes (after consultation with its financial adviser and outside legal counsel) to be reasonably capable of completion and, if completed, is more favourable from a financial point of view to its shareholders than the Acquisition and the transactions contemplated by the Merger Agreement, taking into account at the time of determination any changes to the financial terms of the Merger Agreement proposed by HSBC Holdings.

- 7.3 Household has agreed to: (a) notify HSBC Holdings promptly (but in any event within 24 hours) in certain situations, including if it receives an Acquisition Proposal or enters into negotiations or discussions regarding an Acquisition Proposal; and (b) cease existing negotiations or discussions with persons other than HSBC Holdings and use reasonable best efforts to procure that persons (other than HSBC Holdings) who have been furnished confidential information in connection with an Acquisition Proposal return or destroy such information.

8 Certain Representations and Warranties

- 8.1 The Merger Agreement contains certain customary representations and warranties by HSBC Holdings and Household with respect to themselves and their respective subsidiaries, regarding, among other things: corporate matters, including due organisation and qualification; capitalisation; authority to enter into the Merger Agreement and the transactions contemplated therein; absence of conflicts with organisational documents; required governmental filings and consents; SEC filings and financial statements; accuracy of information supplied; absence of undisclosed liabilities; absence of material adverse changes; litigation matters; compliance with applicable laws and regulations; brokers; and tax matters.

- 8.2 Household also represented:

8.2.1 that the Multi-State Settlement Agreement will have become effective (which has occurred); and

8.2.2 that the estimated related financial impact of the Multi-State Settlement Agreement on Household will not be materially more adverse than a pre-tax charge of US\$525 million recorded by Household in the third quarter of 2002 and a projected after tax earnings impact on Household of US\$50 million in 2003, US\$100 million in 2004 and US\$150 million in 2005 (as previously publicly disclosed by Household).

- 8.3 In addition, Household made representations and warranties about itself to HSBC Holdings regarding, among other things: material contracts and regulatory agreements with various governmental/regulatory authorities; title to all owned real property and assets, and validity of leases relating to leased real property and assets; outstanding secured or unsecured loans, advances, credit card lines and credit card receivables originated by Household; servicing agreements and securitisation matters; employee benefits and labour matters; intellectual property; environmental liabilities; company insurance policies; actions of Household with respect to the Rights Agreement, dated 9 July 1996, between Household and Harris Trust and Savings Bank; risk management and derivatives; inapplicability of state takeover statutes to the Acquisition; and the receipt of fairness opinions from Household's financial advisers.

- 8.4 The representations and warranties contained in the Merger Agreement do not survive the Effective Date.

9 Indemnification and Insurance

HSBC Holdings has agreed to indemnify (through H2) each present and former director and officer of Household and its subsidiaries in their capacities as such against all losses, expenses, claims, damages or liability arising out of acts or omissions occurring on or prior to the Effective Date, to the fullest extent permitted under Delaware law and other applicable laws. H2 shall, for a period of six years from the Effective Date and subject to specified cost limitations, maintain in effect Household's current directors'

and officers' liability insurance in respect of those persons currently covered by such insurance on terms no less favourable than those of such policy in effect on the date of the Merger Agreement.

10 Termination of the Merger Agreement

- 10.1 The Merger Agreement may be terminated at any time prior to the Effective Date by the mutual written consent of Household and HSBC Holdings, or by either Household or HSBC Holdings if:
 - 10.1.1 the Acquisition is not completed by 30 June 2003 (other than as a result of a breach of the Merger Agreement caused by the party seeking termination);
 - 10.1.2 Household Shareholders do not approve the Merger Agreement at the Household Shareholders' special meeting or any adjournment thereof;
 - 10.1.3 HSBC Shareholders do not pass the resolution approving the Acquisition at the EGM or any adjournment thereof;
 - 10.1.4 a court of competent jurisdiction or other governmental, regulatory or administrative entity issues an order which is final and not or no longer appealable, permanently restraining the Acquisition; or
 - 10.1.5 a governmental or regulatory entity which must grant a regulatory approval as a condition to the Acquisition denies approval of the Acquisition (or, in the case HSBC Holdings, if such approval is subject to a Burdensome Condition) and such action has become final and not or no longer appealable.
- 10.2 The Merger Agreement may also be terminated at any time prior to the Effective Date by HSBC Holdings if:
 - 10.2.1 there has been a breach of any of Household's representations, warranties, covenants or agreements set out in the Merger Agreement, the breach has not been cured within 30 days following written notice of the breach or cannot by its nature be cured within 30 days and the breach, if occurring on the closing date, would constitute the failure of a condition to closing;
 - 10.2.2 Household has wilfully and materially breached its "no solicitation" obligations, or Household's board of directors has failed to recommend in the Proxy Statement/Prospectus the adoption of the Merger Agreement, changed its recommendation to Household Shareholders, recommended an Alternative Proposal or failed to call a meeting of Household Shareholders; or
 - 10.2.3 Household or any of its representatives has engaged in discussions with any person in connection with an Acquisition Proposal and has not ceased all discussions within 20 days of the first date of any such discussions.
- 10.3 The Merger Agreement may also be terminated at any time prior to the Effective Date by Household if:
 - 10.3.1 there has been a breach of any of HSBC Holdings' representations, warranties, covenants or agreements set out in the Merger Agreement, the breach has not been cured within 30 days following written notice of the breach or cannot by its nature be cured within 30 days and the breach, if occurring on the closing date, would constitute the failure of a condition to closing; or
 - 10.3.2 the Board has failed to recommend the Acquisition to HSBC Shareholders or failed to call the EGM.
- 10.4 In the event the Merger Agreement is terminated as described above, the Merger Agreement will become void and neither HSBC Holdings nor Household will have any liability pursuant to the Merger Agreement, except that:
 - 10.4.1 both HSBC Holdings and Household will remain liable for any wilful breach of, or wilful misrepresentation in, the Merger Agreement; and
 - 10.4.2 Household may be required to pay HSBC Holdings a termination fee under the circumstances described in paragraph 11 below.

11 Termination Payments and Expenses

- 11.1 Household has agreed to pay to HSBC Holdings a termination fee of US\$550,000,000 if any of the following occurs:
- 11.1.1 either party terminates the Merger Agreement because the Acquisition was not completed by 30 June 2003 without the Household Shareholders' special meeting or vote on the Acquisition having occurred, if:
- (a) an Acquisition Proposal was made known to Household or its shareholders prior to, and such proposal was not withdrawn at least 15 Business Days prior to, 30 June 2003; and
 - (b) any Alternative Transaction is completed or an agreement with respect to any Alternative Transaction is entered into within 12 months after the date of termination;
- 11.1.2 either party terminates the Merger Agreement because Household Shareholders failed to approve the Merger Agreement at the Household Shareholders' special meeting or any adjournment thereof, if:
- (a) an Acquisition Proposal was made known to Household or its shareholders prior to the taking of the vote at the special meeting; and
 - (b) any Alternative Transaction is completed or an agreement with respect to any Alternative Transaction is entered into within 12 months after the date of termination;
- 11.1.3 HSBC Holdings terminates the Merger Agreement as a result of a breach by Household of any of its representations, warranties, covenants or agreements under the Merger Agreement in such a manner that HSBC Holdings would not be able to complete the Acquisition, if:
- (a) an Acquisition Proposal was made known to Household or its shareholders prior to the occurrence of the breach; and
 - (b) any Alternative Transaction is completed or an agreement with respect to any Alternative Transaction is entered into within 12 months after the date of termination;
- 11.1.4 HSBC Holdings terminates the Merger Agreement on the grounds of paragraph 10.2.2 above; or
- 11.1.5 HSBC Holdings terminates the Merger Agreement on the grounds of paragraph 10.2.3 above, and Household completes or enters into an agreement with respect to any Alternative Transaction within 12 months after the date of termination.
- 11.2 In any situation described above, where more than one event is a condition to the payment of the termination fee (e.g. the termination of the Merger Agreement and completing or entering into an agreement relating to an Alternative Transaction) the fee is not payable until the later of the events has occurred. Save as described above, each party shall pay its own fees or expenses in connection with the Acquisition, whether or not it is completed.

B. Regulatory Matters

HSBC Holdings and Household have agreed to use their reasonable best efforts to obtain all regulatory approvals required to complete the Acquisition. While HSBC Holdings and Household believe that they will be able to obtain these regulatory approvals, HSBC Holdings and Household cannot predict whether the required regulatory approvals will be obtained within the timeframe contemplated by the Merger Agreement or on conditions that would not be detrimental to HSBC Holdings or Household, or whether these approvals will be obtained at all. The Merger Agreement provides that, in connection with obtaining these approvals HSBC Holdings is not required to agree to, or to permit Household to agree to, any limitation, divestiture or condition that would materially and adversely impact HSBC Holdings or Household. HSBC Holdings and Household are not aware of any other material governmental approvals or actions that are required prior to completion of the Acquisition other than those described below.

1 United States

1.1 US Antitrust

Transactions like the Acquisition are reviewed by the Antitrust Division of the United States Department of Justice (the “Antitrust Division”) or the United States Federal Trade Commission (the “FTC”) to determine whether they comply with applicable antitrust law. Under the provisions of the HSR Act and related rules, the Acquisition cannot be completed until both HSBC Holdings and Household furnish information and materials to the Antitrust Division and the FTC and a required waiting period has ended. On 27 November 2002, HSBC Holdings and Household filed their pre-acquisition notification and report forms with the Antitrust Division. Early termination of the waiting period was granted with effect from 16 December 2002.

Even after the termination of the waiting period, at any time before or after the Acquisition is completed, the Antitrust Division, the FTC or any US state could take action under antitrust laws as it deems necessary or desirable in the public interest, including seeking to prohibit the Acquisition or seeking divestiture of substantial assets of HSBC Holdings or Household or their subsidiaries. Private parties may also seek to take legal action under antitrust laws under some circumstances. Based on an examination of information relating to the businesses in which the parties are engaged, HSBC Holdings and Household believe that completion of the Acquisition will not violate US antitrust laws. However, HSBC Holdings and Household can give no assurance that a challenge to the Acquisition on antitrust grounds will not be made or, if a challenge is made, of the result.

1.2 Other Regulatory Matters

Applications or notifications are also required to be filed with various US state banking departments in connection with the change in control of Household’s subsidiaries which act as mortgage bankers, sales finance companies or licensed lenders or which engage in other consumer finance activities. These authorities may determine not to approve the Acquisition based upon the criteria set out in applicable laws and regulations. Applications were submitted by HSBC Holdings on 27 November 2002 to the New York State Banking Department for approval of the change in control of those of Household’s subsidiaries that are licensed to engage in consumer finance activities in the State of New York. The Superintendent of Banks of the State of New York is required to give a decision in respect of such applications within 90 days after acceptance of the applications, unless that deadline is otherwise extended. Applications or appropriate notifications have also been filed in all the other states which require such filings, including Tennessee, Illinois, Maryland, Wisconsin, Oklahoma and Delaware.

The change in control of Household’s subsidiaries that act as insurance underwriters or agencies is also subject to the receipt of necessary approvals from various US state insurance regulatory authorities. The insurance laws and regulations of most states generally require that, to proceed with the acquisition of control of an insurance company domiciled in a state through the acquisition of or merger with the parent company of the insurance company, the acquirer must obtain the prior approval of the insurance regulatory authority of that state. In this regard, completion of the Acquisition is subject to the prior approval of the insurance regulatory authorities of Arizona, Delaware, Michigan, New York and Ohio and applications are being made to the insurance departments of these states. In addition, notices have been sent to insurance regulators in other, non-domiciliary states notifying them of the Acquisition. No prior approval by insurance regulators in these states is required.

In order to complete the Acquisition, HSBC Holdings must also obtain the approval of the Office of the Comptroller of the Currency (the “OCC”) under the Change in Bank Control Act for the change in control of Household Bank (SB), N.A., a limited purpose credit card bank and a subsidiary of Household. HSBC Holdings filed a notice under such Act with the OCC on 27 November 2002. A decision by the OCC is expected to be received within 60 days of the date on which the notice is deemed complete, unless the review period is extended.

2 United Kingdom

2.1 Notification to the OFT

In the UK, the Acquisition is conditional on confirmation having been received by HSBC Holdings from the OFT, in terms reasonably satisfactory to HSBC Holdings, that the UK’s Secretary of State for Trade and Industry does not intend to refer the transactions contemplated by the Merger Agreement, or any matters arising therefrom, to the UK’s Competition Commission.

HSBC Holdings and Household notified the OFT of the Acquisition on 29 November 2002 by way of a prescribed statutory merger notice, under the merger control provisions of the Fair Trading Act 1973. The Secretary of State announced on 17 January 2003 that she had decided not to refer the Acquisition to the UK’s Competition Commission.

2.2 Approval by the FSA

The Acquisition is conditional on, among other things, the approval by the FSA.

Section 178 of FSMA obliges HSBC Holdings to notify the FSA of the Acquisition as it would result in HSBC Holdings acquiring “control” over HFC Bank plc, Hamilton Insurance Company Limited and Hamilton Life Assurance Company Limited, each a wholly owned subsidiary of Household and a UK authorised person under FSMA. A person acquires “control” when he holds 10 per cent or more of the shares in a parent undertaking of a UK authorised person. Applications were filed with the FSA on 6 December 2002.

The FSA has a maximum period of three months from the date it receives the written notice from HSBC Holdings to determine whether to approve the change of control or whether to impose such conditions as it considers appropriate.

3 Canada

HSBC Holdings is required to file an application with the Canadian Office of the Superintendent of Financial Institutions for prior approval of the indirect acquisition of control of Household’s Canadian subsidiaries which was made on 15 January 2003.

HSBC Holdings and Household filed a pre-notification as required under the Canadian Competition Act in connection with the change in control of Household’s Canadian subsidiaries. The 14 day waiting period applicable to this filing expired on 31 January 2003. It is anticipated that the Competition Bureau will complete its review by 28 February 2003.

4 European Union

Notification to the European Commission is not required to be made under the European Union’s Merger Regulation.

5 Other International Regulatory Matters

In addition to the required US, UK and Canadian filings, an application for change of control of Household’s subsidiaries in the Republic of Ireland has been filed and approval has been granted. An antitrust filing has been made in the Federal Republic of Germany, and the German Federal Cartel Office has determined that the Acquisition does not have any effect on the German domestic market and so no further consideration is required. An antitrust filing has also been made in the Republic of Ireland and confirmation received that no order is to be made under relevant legislation. In addition, HSBC Holdings and Household conduct operations in a number of other jurisdictions and other filings or approvals are required or may be desirable in connection with the completion of the Acquisition.

Part V: Additional Information

1 Responsibility

The Directors, whose names are set out in paragraph 3 below, accept responsibility for the information contained in this document. To the best of the knowledge and belief of the Directors (who have taken all reasonable care to ensure that such is the case), the information contained in this document is in accordance with the facts and does not omit anything likely to affect the import of such information.

This document includes particulars given in compliance with the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange for the purpose of giving information with regard to HSBC Holdings. The Directors collectively and individually accept full responsibility for the accuracy of the information contained in this document and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief there are no other facts the omission of which would make any statement herein misleading.

2 Share Capital

- 2.1 The share capital of HSBC Holdings as at the close of business on 21 February 2003 (the latest practicable date prior to the publication of this document), and immediately after the Acquisition becomes effective (assuming: (a) approval of the Resolution; (b) the issue of 1,281,972,179 Consideration Shares (on the basis set out in paragraph 2.3 below); and (c) no further issues of HSBC Ordinary Shares after 21 February 2003 and prior to the Effective Date) is and will be as follows:

	Authorised		Issued and Fully Paid	
	Number	Nominal value	Number	Nominal value
Before the Acquisition				
HSBC Ordinary Shares of US\$0.50 each	15,000,000,000	US\$7,500,000,000	9,481,378,744	US\$4,740,689,372.00
Sterling Preference Shares of £0.01 each	10,000,000	£100,000	—	—
Dollar Preference Shares of US\$0.01 each	10,000,000	US\$100,000	—	—
Euro Preference Shares of €0.01 each	10,000,000	€100,000	—	—
Non-voting Deferred Shares of £1 each	301,500	£301,500	301,500	£301,500
After the Acquisition				
HSBC Ordinary Shares of US\$0.50 each	15,000,000,000	US\$7,500,000,000	10,763,350,923	US\$5,381,675,461.50
Sterling Preference Shares of £0.01 each	10,000,000	£100,000	—	—
Dollar Preference Shares of US\$0.01 each	10,000,000	US\$100,000	—	—
Euro Preference Shares of €0.01 each	10,000,000	€100,000	—	—
Non-voting Deferred Shares of £1 each	301,500	£301,500	301,500	£301,500

- 2.2 At the Extraordinary General Meeting, the Resolution will be proposed, *inter alia*:

- to approve the Acquisition (including the arrangements to be put in place in relation to outstanding options over, and rights to receive, Household Common Shares); and
- to authorise the Directors for the purposes of Section 80 of the Act to allot additional relevant securities (as defined in that section) up to an aggregate nominal amount of US\$702,863,189.

In total up to approximately 1,405,726,378 New HSBC Ordinary Shares may be issued in consequence of the Acquisition (including approximately 123,754,199 New HSBC Ordinary Shares, being the expected maximum number of Additional HSBC Ordinary Shares which may fall to be issued). The aggregate nominal value of those New HSBC Ordinary Shares is equal to the nominal amount of relevant securities for which authority to allot is sought in the Resolution.

- 2.3 Based on the 473,664,080 Household Common Shares in issue as at 21 February 2003 and the further 5,577,856 Household Common Shares expected to be issued prior to the Effective Date (not including any Household Common Shares that may be issued on the exercise of options or rights other than those which would lapse if not exercised on or before the Effective Date), the Directors expect to allot following the Effective Date up to 1,281,972,179 HSBC Ordinary Shares as Consideration Shares, with an aggregate nominal value of US\$640,986,089.50, to Household Common Shareholders on the surrender of certificates in respect of their Household Common Shares to the Exchange Agent. The Consideration Shares will be credited as fully paid and will rank *pari passu* in all respects with the existing HSBC Ordinary Shares, save that they will only have the right to receive any dividends or other distributions declared, made or paid in respect thereof with a record date on or after the Effective Date.

Following the Acquisition becoming effective, Additional HSBC Ordinary Shares may be issued, which will also rank *pari passu* in all respects with the then existing HSBC Ordinary Shares, save that they will only have the right to receive any dividends or other distributions declared, made or paid in respect thereof with a record date on or after their respective dates of issue.

Details of the arrangements to be put in place in respect of the Household Preferred Stock and the outstanding options over, and rights to subscribe for, Household Common Shares are set out in Section A of Part IV of this document.

- 2.4 No temporary documents of title will be issued pursuant to the Acquisition.
- 2.5 The New HSBC Ordinary Shares are not being marketed or made available to the public in whole or in part in conjunction with the applications for listing of those shares other than in connection with the Acquisition.
- 2.6 The New HSBC Ordinary Shares will, when issued, be in registered form and will be capable of being held in certificated form or in uncertificated form through CREST. HSBC ADSs will, when issued, be capable of being held in certificated form or book-entry form.
- 2.7 The HSBC Ordinary Shares are listed and traded on the London Stock Exchange's market for listed securities, the Main Board of the Hong Kong Stock Exchange and Euronext Paris. The HSBC Ordinary Shares are listed, and the HSBC ADSs are listed and traded, on the New York Stock Exchange.

3 HSBC Holdings Directors

The full names and functions of the Directors are as follows:

Sir John Reginald Hartnell Bond	Group Chairman and Executive Director
Baroness Lydia Selina Dunn, DBE	Deputy Chairman and senior Non-executive Director
Sir Brian Scott Moffat, OBE	Deputy Chairman and senior independent Non-executive Director*
Sir Keith Roderick Whitson	Group Chief Executive and Executive Director
Charles Francis Wiener de Croisset	Chairman and Chief Executive Officer, CCF and Executive Director
William Robert Patrick Dalton	Chief Executive, HSBC Bank plc and Executive Director
David Gordon Eldon	Chairman, The Hongkong and Shanghai Banking Corporation Limited and Executive Director
Douglas Jardine Flint	Group Finance Director and Executive Director
Stephen Keith Green	Executive Director, Corporate, Investment Banking and Markets
Alan Wayne Jebson	Group IT Director and Executive Director
Lord Frederick Edward Robin Butler of Brockwell, GCB, CVO	Non-executive Director*
Raymond Kuo Fung Ch'ien, CBE	Non-executive Director*
William Kwok Lun Fung, OBE	Non-executive Director*
Sharon Hintze	Non-executive Director*
Sir John Kemp-Welch	Non-executive Director*
Lord Colin Marsh Marshall of Knightsbridge	Non-executive Director
Sir Mark Moody-Stuart, KCMG	Non-executive Director*
Stewart Worth Newton	Non-executive Director*
Helmut Sohmen, OBE	Non-executive Director
Carole Sandra Taylor	Non-executive Director*
Sir Robert Brian Williamson, CBE	Non-executive Director*

* Denotes independent non-executive Director

The business address of each of the Directors is 8 Canada Square, London E14 5HQ, United Kingdom. The Group Company Secretary of HSBC Holdings is Ralph Gordon Barber, FCIS.

4 Directors' and Other Interests

4.1 As at 21 February 2003 (the latest practicable date prior to the publication of this document):

- (i) the interests (all of which are beneficial unless otherwise stated) of the Directors (and persons connected with them within the meaning of Section 346 of the Act) in the share capital of HSBC Holdings which: (a) have been notified to HSBC Holdings pursuant to section 324 or section 328 of the Act; or (b) are required to be entered in the register maintained pursuant to section 325 of the Act; or (c) are interests of a person connected with a Director (within the meaning of section 346 of the Act) which would, if the connected person were a Director, be required to be disclosed under (a) or (b) above and the existence of which is known to or could with reasonable diligence be ascertained by that Director; and
- (ii) the interests (all of which are beneficial unless otherwise stated) of the Directors in the share capital of HSBC Holdings or its associated corporations (within the meaning of the SDI Ordinance) required to be notified to HSBC Holdings and the Hong Kong Stock Exchange pursuant to section 28 of the SDI Ordinance (including interests which the Directors were taken or deemed to have under section 31 or Part I of the Schedule to the SDI Ordinance) or required, pursuant to section 29 of the SDI Ordinance, to be entered in the register referred to therein or required to be notified pursuant to the Hong Kong Stock Exchange's Model Code for Securities Transactions by Directors of Listed Companies,

were as follows:

	Personal	Family	Corporate	Other	Total
HSBC Ordinary Shares					
Sir John Bond ¹	271,079	3,309	—	—	274,388
R K F Ch'ien	24,273	—	—	—	24,273
C F W de Croisset ¹	35,664	—	—	—	35,664
W R P Dalton ¹	22,643	—	—	—	22,643
Baroness Dunn	112,172	—	—	24,000 ²	136,172
D G Eldon ¹	12,816	863	—	—	13,679
D J Flint ¹	35,609	1,790	—	—	37,399
W K L Fung	328,000	—	—	—	328,000
S K Green ¹	159,290	14,337	—	—	173,627
A W Jebson ¹	45,254	—	—	—	45,254
Sir John Kemp-Welch	25,000	—	—	381,800 ²	406,800
Lord Marshall	7,578	—	—	—	7,578
Sir Brian Moffat	5,640	—	—	—	5,640
Sir Mark Moody-Stuart	5,000	840	—	—	5,840
H Sohmen	—	382,138	2,504,636 ³	—	2,886,774
C S Taylor	500	—	—	—	500
Sir Keith Whitson ¹	101,706	20,000	—	—	121,706
Sir Brian Williamson	14,500	—	—	—	14,500

¹ Details of additional interests in HSBC Ordinary Shares under the share option plans and Restricted Share Plan are set out below.

² Non-beneficial.

³ Interests held by private investment companies.

Sir John Bond has a personal interest in £290,000 of HSBC Capital Funding (Sterling 1) L.P. 8.208 per cent Non-cumulative Step-up Perpetual Preferred Securities.

D. G. Eldon has a personal interest in 300 Hang Seng Bank Limited ordinary shares of HK\$5.00 each.

S. K. Green has a personal interest in €75,000 of HSBC Holdings plc 5½ per cent Subordinated Notes 2009 and in £100,000 of HSBC Bank plc 9 per cent Subordinated Notes 2005.

H. Sohmen has a corporate interest in £1,200,000 of HSBC Bank plc 9 per cent Subordinated Notes 2005, in US\$3,000,000 of HSBC Bank plc Senior Subordinated Floating Rate Notes 2009, in US\$3,000,000 of HSBC Capital Funding (Dollar 1) L.P. 9.547 per cent Non-cumulative Step-up Perpetual Preferred Securities, Series 1 and in US\$2,900,000 of HSBC Finance Nederland BV 7.40 per cent Securities 2003.

As Directors of CCF, C.F.W. de Croisset, W.R.P. Dalton and S.K. Green, each has a personal interest in one share of €5 each in that company. The Directors have waived their rights to receive dividends on these shares and undertaken on cessation of their directorship to transfer these shares to HSBC Holdings.

4.2 As at 21 February 2003 (the latest practicable date prior to the publication of this document), the following Directors have been granted, and have outstanding, options over HSBC Ordinary Shares. The options were awarded for nil consideration at exercise prices equivalent to the market value at the date of award, except that options awarded under the HSBC Holdings Savings-Related Share Option Plan since 2001 are exercisable at a 20 per cent discount to the market value at the date of award and those awarded

before 2001 at a 15 per cent discount. There are no remaining performance criteria conditional upon which the outstanding options are exercisable.

HSBC Holdings Savings-Related Share Option Plan

	Number of HSBC Ordinary Shares under option	Exercise price per share £	Date of award	Exercisable from ¹	Exercisable until ²
Sir John Bond	2,798	6.0299	10 Apr 2000	1 Aug 2005	31 Jan 2006
W R P Dalton	2,798	6.0299	10 Apr 2000	1 Aug 2005	31 Jan 2006
D J Flint	2,617	6.3224	2 May 2002	1 Aug 2007	31 Jan 2008
S K Green	2,498	6.7536	11 Apr 2001	1 Aug 2006	31 Jan 2007
A W Jebson	1,434	6.7536	11 Apr 2001	1 Aug 2004	31 Jan 2005
Sir Keith Whitson	2,798	6.0299	10 Apr 2000	1 Aug 2005	31 Jan 2006

¹ May be advanced to an earlier date in certain circumstances, e.g. retirement.

² May be extended to a later date in certain circumstances, e.g. on death of a participant, the executors may exercise the option up to six months beyond the normal exercise period.

HSBC Holdings Executive Share Option Scheme

	Number of HSBC Ordinary Shares under option	Exercise price per share £	Date of award	Exercisable from ¹	Exercisable until ²
Sir John Bond	75,000 ³	3.3334	1 Apr 1996	1 Apr 1999	1 Apr 2006
W R P Dalton	22,704	2.4062	12 Oct 1993	12 Oct 1996	12 Oct 2003
	30,273	2.8376	8 Mar 1994	8 Mar 1997	8 Mar 2004
	36,000	2.1727	7 Mar 1995	7 Mar 1998	7 Mar 2005
	36,000 ³	3.3334	1 Apr 1996	1 Apr 1999	1 Apr 2006
D G Eldon	36,000	2.1727	7 Mar 1995	7 Mar 1998	7 Mar 2005
	40,500 ³	3.3334	1 Apr 1996	1 Apr 1999	1 Apr 2006
D J Flint	27,000 ³	3.3334	1 Apr 1996	1 Apr 1999	1 Apr 2006
Sir Keith Whitson	60,000 ³	3.3334	1 Apr 1996	1 Apr 1999	1 Apr 2006

¹ May be advanced to an earlier date in certain circumstances, e.g. retirement.

² May be extended to a later date in certain circumstances, e.g. on death of a participant, the executors may exercise the option up to twelve months beyond the normal exercise period.

³ The exercise of these options was conditional upon the growth in earnings per share over a three-year period being equal to or greater than a composite rate of inflation (comprising 50 per cent of the Hong Kong Composite Consumer Price Index, 35 per cent of the UK Retail Price Index and 15 per cent of the USA All Urban Consumer Price Index) plus 2 per cent per annum. This condition has been satisfied.

HSBC Holdings Group Share Option Plan

	Number of HSBC Ordinary Shares under option	Exercise price per share £	Date of award	Exercisable from	Exercisable until ¹
C F W de Croisset	206,000	8.7120	23 Apr 2001	23 Apr 2004	23 Apr 2011
	206,000	8.4050	7 May 2002	7 May 2005	7 May 2012

¹ May be extended to a later date in certain circumstances, e.g. on death of a participant, the executors may exercise the option up to twelve months beyond the normal exercise period.

Following the acquisition of CCF in 2000, HSBC Ordinary Shares were purchased by the HSBC Holdings General Employee Benefit Trust. These shares may be exchanged for CCF shares following the exercise of CCF employee share options in the same ratio as the exchange offer for CCF (13 HSBC Ordinary Shares for each CCF share). As a potential beneficiary of the Trust, C. F. W. de Croisset has a technical interest in all of the shares held by the Trust. As at 21 February 2003, the Trust held 35,745,555 HSBC Ordinary Shares.

As at 21 February 2003, C. F. W. de Croisset held the following options to acquire CCF shares of €5 each. Following the exercise of these options each CCF share will be exchanged for 13 HSBC Ordinary Shares. The options were granted by CCF for nil consideration at a 5 per cent discount to the market value at the date of award. There are no performance criteria conditional upon which the outstanding options are exercisable.

CCF shares of €5 each

Exercise price per share €	Number of shares under option	Equivalent number of HSBC Ordinary Shares	Date of award	Exercisable from	Exercisable until
32.78	10,000	130,000	23 Jun 1994	23 Jun 1996	23 Jun 2004
34.00	30,000	390,000	22 Jun 1995	22 Jun 1997	22 Jun 2005
35.52	30,000	390,000	9 May 1996	9 May 1998	9 May 2006
37.05	30,000	390,000	7 May 1997	7 Jun 2000	7 May 2007
73.50	30,000	390,000	29 Apr 1998	7 Jun 2000	29 Apr 2008
81.71	28,000	364,000	7 Apr 1999	7 Jun 2000	7 Apr 2009
142.50	28,000 ¹	364,000	12 Apr 2000	1 Jan 2002	12 Apr 2010

¹ The exercise of this option was conditional upon continued employment with CCF until 1 January 2002 which has now been satisfied.

HSBC Holdings Restricted Share Plan 2000

	Number of HSBC Ordinary Shares subject to awards ¹	Date of award	Year in which awards may vest
Sir John Bond	29,746	2 Mar 1998	2003
	67,996	4 Mar 1999	2004
	85,365	10 Mar 2000	2005
	80,001	12 Mar 2001	2006
	119,795	8 Mar 2002	2007
W R P Dalton	19,833	2 Mar 1998	2003
	39,665	4 Mar 1999	2004
	38,803	10 Mar 2000	2005
	45,715	12 Mar 2001	2006
	75,660	8 Mar 2002	2007
D G Eldon	23,796	2 Mar 1998	2003
	39,665	4 Mar 1999	2004
	38,803	10 Mar 2000	2005
	7,388	3 Apr 2000	2003
	45,715	12 Mar 2001	2006
	6,736	30 Apr 2001	2004
	50,440	8 Mar 2002	2007
	9,340	15 May 2002	2005
D J Flint	19,833	2 Mar 1998	2003
	39,665	4 Mar 1999	2004
	34,922	10 Mar 2000	2005
	57,144	12 Mar 2001	2006
	75,660	8 Mar 2002	2007
S K Green	23,796	2 Mar 1998	2003
	39,665	4 Mar 1999	2004
	38,803	10 Mar 2000	2005
	80,001	12 Mar 2001	2006
	94,575	8 Mar 2002	2007
A W Jebson	9,917	2 Mar 1998	2003
	33,998	4 Mar 1999	2004
	31,041	10 Mar 2000	2005
	68,572	12 Mar 2001	2006
	88,270	8 Mar 2002	2007
Sir Keith Whitson	23,796	2 Mar 1998	2003
	56,663	4 Mar 1999	2004
	54,323	10 Mar 2000	2005
	62,858	12 Mar 2001	2006
	94,575	8 Mar 2002	2007

¹ Includes additional shares arising from scrip dividends

- 4.3 There will be no changes to the Directors' interests as a result of the Acquisition becoming effective.
- 4.4 No Director has or has had any interest in any transaction which is or was unusual in its nature or conditions or significant in relation to the business of the HSBC Group and which was effected during the current or immediately preceding financial year or which was effected during any earlier financial year and which remains in any respect outstanding or unperformed.

- 4.5 As at 21 February 2003 (the latest practicable date prior to the publication of this document), and immediately after the Effective Date (assuming: (a) approval of the Resolution; (b) the issue of 1,281,972,179 Consideration Shares (on the basis set out in paragraph 2.3 of this Part V); (c) no further issues of HSBC Ordinary Shares after 21 February 2003 and prior to the Effective Date; and (d) no changes to the interests notified), the Directors are aware of the following persons other than a Director who, directly or indirectly, are and will be interested in three per cent or more of the issued share capital of HSBC Holdings:

Shareholder	Number of HSBC Ordinary Shares held as at the date of notification and after the Acquisition	Percentage of issued ordinary share capital in HSBC Holdings before the Acquisition	Percentage of issued ordinary share capital in HSBC Holdings as enlarged by the Acquisition
Legal & General Investment Management Limited	284,604,788	3.00	2.64

- 4.6 Save as set out below, as at 21 February 2003 (the latest practicable date prior to the publication of this document), so far as is known to the Directors, no person (excluding any member of the HSBC Group) has any interest, direct or indirect, in ten per cent or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of HSBC Holdings or its subsidiaries (as defined by section 2 of the Companies Ordinance) (including options in respect of such capital):

Shareholder	HSBC Group company	Percentage interest in share capital of HSBC Group company
Alfred McAlpine Project Investments Limited	Enterprise Civic Buildings (Holding) Limited	10
Ballast Wiltshier Investments Limited	Sussex Custodial Services (Holdings) Limited	15
Banco de Inversion y Serv. Financieros	Cirflex S.A. (in liquidation)	16.56
Berkeley Advisors Incorporated	Hermitage Capital Management Limited	25
BNP Paribas	Gie Carpati Bail	25
Byhome Limited	AGP Holdings (1) Limited	19.50
CAE International Holdings Limited	CVS Leasing Limited	13.39
Chanel	SNC Gaz Finance	25
CIC	SNC Gaz Finance	15
Clifap	Gie Ethylene Est	25
Dah Chong Hong Limited	Way Chong Finance Limited	50
Eurofactor	Elysees Factor	34
Friesenbruch Meyer	HSBC Insurance Services (Bermuda) Limited	10
Hambros	M H Shipping Company	20
Harmondsworth Investments Limited	Falkirk Schools Partnership Limited	20
Iberfomento, S.A.	Cirflex S.A. (in liquidation)	13.74
Indivision Jo Vallet	Banque Eurofin	11.31
International Finance Corporation	Tower Investment Management	10
Interserve Investments plc	ICB Holdings Limited	20
I Vezanis	HSBC (Hellas) AEDAK	27
L-Bank	HSBC Trinkaus & Burkhardt KGaA	20
Munder UK LLC	Framlington Holdings Limited	49
New York International	HSBC – New York Life Seguros de Retiro (Argentina) S.A.	50.63 ¹
New York International	HSBC – New York Life Seguros de Vida (Argentina) S.A.	50.63 ¹
New York International	HSBC Chacabuco Inversiones S.A. AFJP.	40
Paisner & Co.	Paicolex Trust Management AG	49
Paisner & Co.	Roparo Trust Management AG	24
Prévoyance et Epargne Salarial	Elysées Fonds	47.87
Prime Land Services LLC	HSBC Land Title Agency (USA) LLC	45
P.T. Bongamulia Nagadi	PT HSBC Securities Indonesia	15
Quayle Munro Holdings plc	Falkirk Schools Partnership Limited	10.70
Reliance Sussex pfi Limited	Sussex Custodial Services (Holdings) Limited	15
R.W. Fellowes	HSBC Insurance Services (Bermuda) Limited	15
R.W. Fellowes	HSBC Insurance Solutions (Bermuda) Limited	15
Shepherd Securities Limited	ICB Holdings Limited	19.99
Société Cristolienne de Participations	SNC Olivier d'Antibes	40
Sodexho Investment Services Limited	Enterprise Civic Buildings (Holding) Limited	10
Soges Fiducem S.A.	Soges Dewaay SA	50
The Government of Dubai	HSBC Middle East Finance Company Limited	20
WyWy Worldwide Limited	HSBC WyWy Investments Limited (in liquidation)	23.8

¹ Part or all of these interests include voting rights exercisable by New York International in respect of shares held by HSBC Chacabuco Inversiones S.A.

5 Directors' and Proposed Director's Service Contracts

5.1 The main terms on which each of the Executive Directors named below is employed by the HSBC Group are set out below:

	Name of employing company and date of contract	Notice period	Current salary (£'000 unless otherwise stated)	Annual Performance Bonus 2002 ¹ £'000	Total aggregate remuneration and benefits in kind 2002 ² £'000
Sir John Bond	HSBC Holdings 1 January 1993	Rolling contract which requires 12 months' notice to be given by either party	970 ³	923	1,885
C.F.W. de Croisset	CCF 7 January 1980	see Note 4	€541,660 ³	235	609
W.R.P. Dalton	HSBC Bank Canada 5 January 1998	Rolling contract which requires 12 months' notice to be given by either party	496.5 ³	— ⁵	627
D.G. Eldon	The Hongkong and Shanghai Banking Corporation Limited 1 January 1968	Rolling contract which requires 3 months' notice to be given by either party	US\$286,752 ⁶	212	1,226
D.J. Flint	HSBC Holdings 29 September 1995	Rolling contract which requires 12 months' notice to be given by HSBC Holdings and 9 months' notice to be given by Mr Flint	440.5 ³	350	960
S.K. Green	HSBC Holdings 9 March 1998	Rolling contract which requires 12 months' notice to be given by either party	470.5 ³	461	965
A.W. Jebson	HSBC Holdings 14 January 2000	Rolling contract which requires 12 months' notice to be given by either party	440 ³	175 ⁷	823
Sir Keith Whitson	HSBC Holdings 1 August 1992	Rolling contract which requires 12 months' notice to be given by either party	790 ³	1,400	2,170

None of the Executive Directors' service contracts contains provisions for pre-determined compensation on termination which exceeds one year's salary and benefits in kind, save as referred to in Note 4 below.

¹ The annual performance bonus relating to 2002 which will be paid in 2003.

² Comprises salary and benefits in kind which were paid in 2002 and the annual performance bonus relating to 2002 which will be paid in 2003. With effect from April 2003.

⁴ Mr. de Croisset has a contract of employment dated 7 January 1980 that was in force before he joined the Board of CCF. The contract has no set term but provides for three months' notice to be given by either party. Under the terms of the contract Mr. de Croisset would be entitled to receive one month's salary for each year of service with CCF on termination of his employment with CCF. However, in accordance with French legal requirements and practice, this contract is suspended while Mr. de Croisset serves as an executive director of CCF.

⁵ In return for the prior waiver of bonus, the employer contribution into the pension scheme for Mr. Dalton has been increased by the amount (£400,000) which would otherwise have been paid.

⁶ Mr. Eldon's base salary, as an International Manager, is calculated on a net basis including expatriate allowances and will be subject to a separate review in April 2003.

⁷ In return for the prior waiver of bonus, the employer contribution into the pension scheme for Mr. Jebson has been increased by the amount (£175,000) which would otherwise have been paid.

The remuneration of the Executive Directors comprises four key components: salary; annual cash bonus; the long term incentive plan; and pension arrangements. Only basic salary is pensionable.

Cash bonuses for Executive Directors are based on two key factors: individual performance taking into account, as appropriate, results against plan of the business unit or performance of the support function for which the individual has responsibility and Group performance measured by operating profit before tax against plan.

Executive Directors are eligible to receive conditional awards of performance shares under the Restricted Share Plan 2000 and full details of awards held are set out in paragraph 4.2 of this Part V.

Pension arrangements

Sir John Bond, S.K. Green, A.W. Jebson and Sir Keith Whitson are members of the HSBC Bank (UK) Pension Scheme. Their pensions accrue at a rate of one-thirtieth of pensionable salary per year of pensionable service in the UK. In addition, Sir Keith Whitson had a deferred pension entitlement under the HSBC International Staff Retirement Benefits Scheme in respect of his Group service up to 1992, prior to his transfer to the UK. This deferred pension entitlement was increased in accordance with the Rules of the Scheme during the deferred period, which produced a pension of £84,678 per annum as at 31 October 2002. With the agreement of the trustee, Sir Keith Whitson exercised his option under the Rules of the Scheme, to commute fully this accrued pension for a lump sum payment of £1,100,390, which was paid in November 2002.

C.F.W. de Croisset is eligible for pension benefits which are supplementary to those accrued under the French State and Compulsory arrangements. The amount of this supplementary pension, payable from age 60, accrues at a rate of €6,098 per annum for each year of service (up to a maximum of 18 years) as an executive director of CCF.

The pension arrangements for W.R.P. Dalton to contractual retirement age of 60 are provided on a defined benefit basis under the HSBC Canada Pension Plan A, at an accrual rate of one-thirtieth of pensionable salary per year of pensionable service until his transfer to the UK. On taking up his appointment in the UK in 1998, he has also joined the HSBC Holdings Overseas (No 1) Pension Plan on a defined contribution basis, with an employer contribution during 2002, including a bonus waiver of £400,000 (2001: £300,000), of £529,000 (2001: £429,000).

The pension arrangements for D.J. Flint to contractual retirement age of 60 are provided through an executive allowance paid to fund personal pension arrangements set at 30 per cent of basic salary. This is supplemented through the HSBC Holdings plc Funded Unapproved Retirements Benefits Scheme on a defined contribution basis with an employer contribution during 2002 of £80,092 (2001: £78,150). The intention of these arrangements is to provide benefits broadly comparable to an accrual rate of one-thirtieth of pensionable salary for each year of pensionable service.

The pension arrangements for D.G. Eldon are provided under the HSBC International Staff Retirements Benefits Scheme. Pension accrues at a rate of one twenty-seventh of pensionable salary per year of pensionable service.

- 5.2 The emoluments receivable by the Directors will not vary as a result of the Acquisition becoming effective.
- 5.3 William F. Aldinger's New Employment Agreement with Household
 - 5.3.1 William F. Aldinger, III entered into a new employment agreement for a term of three years with Household on 14 November 2002, such term to commence on the Effective Date. Mr. Aldinger will serve as Chairman and Chief Executive Officer of Household until 1 January 2004 and thereafter, as Chairman and Chief Executive Officer of Household and HSBC North America, Inc. Mr. Aldinger will also serve as a member of the HSBC Board. During the term of the agreement, Mr. Aldinger will be paid an annual base salary equal to his annual base salary as at the date of the Merger Agreement (US\$1 million), and an annual bonus in an amount at least equal to the annual average of Mr. Aldinger's bonuses earned with respect to the three-year period ended 2001 (pro rated for any partial year) (US\$4 million). Pursuant to the terms of Mr. Aldinger's new employment agreement, a termination of employment is generally effective immediately upon receipt of notice by either party, except that a termination due to Mr. Aldinger's disability requires 30 days advance notice following his absence from employment on a full-time basis for 180 consecutive business days.
 - 5.3.2 Within 30 days of the Effective Date, subject to the approval of the trustee of The HSBC Holdings Restricted Share Plan 2000 ("Restricted Share Plan 2000"), Mr. Aldinger will receive a one-time special retention grant of HSBC Ordinary Shares with a value equal to US\$10 million (the "Special Restricted Shares"), based on the closing mid-market price of HSBC Ordinary Shares on the date of grant. The Special Restricted Shares will vest in three equal instalments on each of the first three anniversaries of the Effective Date, as long as Mr. Aldinger remains employed on each applicable vesting date, subject to accelerated vesting upon a termination of employment by

Household without “cause”, by Mr. Aldinger for “good reason” or due to his death or disability. After each of the first and second anniversaries of the Effective Date, subject to the approval of the trustee of the Restricted Share Plan 2000, Mr. Aldinger will receive an additional grant of HSBC Ordinary Shares with a value equal to at least US\$5.5 million (“Additional Restricted Shares”), based on the closing mid-market price of HSBC Ordinary Shares on the applicable date of grant. The Additional Restricted Shares will generally be subject to the same terms and conditions as the Special Restricted Shares. To the extent all or a portion of any of the above grants of Restricted Shares cannot be made under the Restricted Share Plan 2000, Mr. Aldinger will receive a cash bonus equal to the amount of the grant of Restricted Shares that he was not able to receive, subject to the same general terms and conditions as such grant.

- 5.3.3 During the term, except with respect to benefits under qualified and non-qualified excess and supplemental defined benefit retirement plans, Mr. Aldinger will receive employee benefits and benefits in kind that are no less favourable than those provided to him immediately prior to the date of the Merger Agreement. In respect of the financial year ended 31 December 2002, Mr. Aldinger’s participation in Household’s qualified and non-qualified defined contribution plans entitled him to a company matching contribution and he received taxable benefits in kind for financial planning services, a car allowance, excess liability and life insurance premium payments and personal travel expenses, which contributions and taxable benefits in kind equal approximately US\$518,000 in the aggregate.
- 5.3.4 As at the Effective Date, Mr. Aldinger’s benefits under Household’s qualified and non-qualified excess and supplemental defined benefit retirement plans will be frozen, and Mr. Aldinger will be entitled to receive the retirement benefits provided under his existing employment agreement. The pension benefits for Mr. Aldinger are provided on a defined benefit basis under the Household qualified and non-qualified pension plans and a supplemental executive retirement plan adopted in 1997 for Mr. Aldinger (the “SERP”). The annual pension benefit under these arrangements generally equals a percentage of his Final Average Salary (as defined below) not in excess of Covered Compensation (as defined below), plus a percentage of his Final Average Salary that exceeds Covered Compensation. “Final Average Salary” equals the average of salary plus bonus for the 48 successive highest paid months out of the employee’s last ten years of service. “Covered Compensation” is the average of the US Social Security taxable wage base over the 35-year period ending in the year of retirement or earlier termination of employment. The SERP provides Mr. Aldinger with a benefit based on the pension plan formula but with twenty years of benefit service added and with an offset for benefits payable under not only the Household qualified and non-qualified plans but also for the pension benefits payable to Mr. Aldinger under the defined benefit pension plans of Wells Fargo and Citibank.
- 5.3.5 Mr. Aldinger’s new agreement provides that if his employment is terminated during the term by him for “good reason”, or by Household for reasons other than “cause” or disability, he will be entitled to:
- (a) a pro rata target annual bonus for the financial year of the date of termination;
 - (b) a payment equal to his annual base salary plus the average of his annual bonuses with respect to the three-year period ended 2001, times the number of full and partial months from the date of termination until the third anniversary of the Effective Date, divided by twelve;
 - (c) the immediate vesting and exercisability of each Household stock option, restricted stock award and other equity-based award or performance award (or cash equivalent) that is outstanding as at the date of termination and treatment as retirement eligible for purposes of exercising any such award;
 - (d) for the remainder of his life and that of his current spouse, continued medical and dental benefits at Household’s cost; and
 - (e) his retirement benefits (as described in paragraph 5.3.4 above) in a lump sum.

- 5.3.6 If any payments or benefits that Mr. Aldinger receives are subject to the excise tax imposed under Section 4999 of the US Tax Code, his agreement provides for an additional payment to restore him to the after-tax position that he would have been in had the excise tax not been imposed.
- 5.3.7 The new employment agreement also provides that, during his employment with Household, and for a period of one year after the termination of his employment for any reason, other than a termination of employment by Household without “cause” or a resignation by Mr. Aldinger for “good reason”, Mr. Aldinger may not become associated with certain competitive entities that are actively engaged in the consumer lending business (including mortgage and credit card lending) and may not solicit the business of any entity that was a significant commercial customer or client of Household and its subsidiaries during the six-month period prior to his termination date. The new employment agreement also contains a confidentiality provision and a non-solicitation of Household employees restriction following certain terminations of employment.
- 5.3.8 Upon the Effective Date, Mr. Aldinger’s new employment agreement will supersede his existing employment agreement with Household, which will be deemed to have been terminated due to a “qualifying termination”, entitling him to the cash payments and other benefits under that agreement as follows:
- (a) a pro rata annual bonus to the date of termination, based on the highest of the annual bonuses payable to Mr. Aldinger during the three years preceding the year in which the termination occurs;
 - (b) a payment equal to three times the sum of Mr. Aldinger’s base salary and highest annual bonus; and
 - (c) a payment equal to the value of three years of additional employer contributions under Household’s tax-qualified and supplemental defined contribution plans.

Following completion of the Acquisition, Mr. Aldinger will be eligible to receive approximately US\$20.3 million in satisfaction of the cash severance obligations described in (a), (b) and (c) above under his existing employment agreement with Household.

In addition, upon a qualifying termination following a change of control, Mr. Aldinger will be entitled to continued welfare benefit coverage for three years after the date of termination, three years of additional age and service credit under Household’s tax-qualified and supplemental defined benefit retirement plans, and outplacement services. If any amounts or benefits received under the employment agreement or otherwise are subject to the excise tax imposed under section 4999 of the US Tax Code, an additional payment will be made to restore Mr. Aldinger to the after-tax position in which he would have been if the excise tax had not been imposed.

6 Material Contracts

- 6.1 Other than the following contracts, there are no contracts (not being contracts entered into in the ordinary course of business) which: (a) are or may be material and which have been entered into by any member of the HSBC Group during the two years immediately preceding the date of this document; or (b) contain any provision under which any member of the HSBC Group has any obligation or entitlement which is material to the HSBC Group as at the date of this document:
- 6.1.1 the Merger Agreement, particulars of which are summarised in Section A of Part IV of this document; and
 - 6.1.2 an agreement dated 20 August 2002 between the Company (1), GF Bital (2), Banco Internacional, S.A. (3), Banco Internacional, S.A. (as trustee) (4), and certain trust beneficiaries (5), pursuant to which the Company agreed by way of a cash tender offer to acquire all the outstanding shares in GF Bital. At the close of the tender offer on 22 November 2002, the Company had acquired 99.59 per cent of the total capital stock of GF Bital for a total cash consideration of approximately US\$1.135 billion. The trustee and the trust beneficiaries have given limited representations and warranties to HSBC Holdings under the agreement which survive for a period of two years after completion of the acquisition. The maximum liability for a breach of any such representations or

warranty is limited to the gross proceeds received by such person under the terms of the tender offer.

- 6.2 Other than the contract referred to in paragraph 6.1.1 above and the Multi-State Settlement Agreement described in paragraph 8.2.2 below, there are no contracts (not being contracts entered into in the ordinary course of business) which: (a) are or may be material and which have been entered into by any member of the Household Group during the two years immediately preceding the date of this document; or (b) contain any provision under which any member of the Household Group has any obligation or entitlement which is material to the Household Group as at the date of this document.

7 Significant Changes

- 7.1 Save as disclosed in the paragraphs headed “Current Trading and Prospects” and “Recent Developments” in Part I of this document, there has been no significant change in the financial or trading position of the HSBC Group since 30 June 2002, being the date to which its most recent interim financial statements have been published.
- 7.2 There has been no significant change in the financial or trading position of the Household Group since 31 December 2002, being the date to which its most recent earnings release statement has been published.

8 Litigation

- 8.1 No member of the HSBC Group is or has been involved in any legal or arbitration proceedings or any claim of material importance nor, so far as the Directors are aware, are any such proceedings or claims pending or threatened which may have, or have had during the 12 months preceding the date of this document, a significant effect on the HSBC Group’s financial position.
- 8.2 Save as disclosed below, no member of the Household Group is or has been involved in any legal or arbitration proceedings or any claim of material importance nor, so far as the directors of Household are aware, are any such proceedings or claims pending or threatened which may have, or have had during the 12 months preceding the date of this document, a significant effect on the Household Group’s financial position.
- 8.2.1 Several lawsuits have been filed alleging violations of law with respect to the Acquisition. These lawsuits are described below. The lawsuits are in their preliminary stages; Household believes that the claims against it lack merit and intends to defend the lawsuits vigorously.

Two of the lawsuits are pending in the Circuit Court of Cook County, Illinois, Chancery Division. One, *McLaughlin v. Aldinger et al.*, No. 02 CH 20683 (filed on 15 November 2002), asserts claims on behalf of a purported class of Household Common Shareholders against Household and certain of its officers and directors for breach of fiduciary duty in connection with the Acquisition on the grounds that the defendants allegedly failed to take appropriate steps to maximise the value of a merger transaction for Household Common Shareholders. The *McLaughlin* complaint contends that plaintiffs will suffer irreparable harm unless the Acquisition is prohibited, but seeks only unspecified damages. The other, *Pace v. Aldinger et al.*, No. 02 CH 19270 (filed on 24 October 2002 and amended on 15 November 2002), is both a derivative lawsuit on behalf of Household and a purported class action on behalf of Household Common Shareholders. This lawsuit was filed prior to the announcement of the Acquisition and originally asserted claims relating to Household’s pre-Acquisition accounting practices. It has since been amended to allege that Household and certain of its officers and directors breached their fiduciary duties in connection with the Acquisition. The complaint seeks to prohibit the Acquisition as well as unspecified damages (including punitive damages) allegedly stemming from both the Acquisition and pre-Acquisition activity.

A third lawsuit relating to the Acquisition, *Williamson v. Aldinger et al.*, No. 03 C00331 (filed on 15 January 2003), is pending in the United States District Court for the Northern District of Illinois. This derivative lawsuit on behalf of Household claims that certain of Household’s officers and directors breached their fiduciary duties and committed corporate waste by agreeing to the Acquisition and allegedly failing to take appropriate steps to maximise the value of a merger transaction. The complaint seeks to prohibit the Acquisition as well as unspecified damages (including punitive damages).

8.2.2 The Multi-State Settlement Agreement

On 11 October 2002, Household reached a preliminary agreement with a multi-state working group of US state attorneys general and regulatory agencies to effect a US nationwide resolution of alleged violations of US federal and/or state consumer protection, consumer financing and banking laws and regulations with respect to secured real estate lending from Household's retail branch consumer lending operations. This preliminary agreement, and related consent decrees entered into with each of the 50 US states and the District of Columbia, are referred to collectively as the "Multi-State Settlement Agreement". The Multi-State Settlement Agreement requires Household to establish a settlement fund and to pay certain expenses of investigation and administration. Household will also provide greater disclosures and alternatives for customers in connection with "non-prime" mortgage lending originated by its retail branch network. No fines, penalties or punitive damages are being assessed by the US states pursuant to the Multi-State Settlement Agreement. In addition, Household will unilaterally amend all branch originated real estate secured loans to provide that no pre-payment penalty is payable later than 24 months after origination. As described in more detail below, the Multi-State Settlement Agreement became effective as at 16 December 2002.

Under the terms of the Multi-State Settlement Agreement, Household will establish a fund of US\$484 million to be divided among all participating states (including the District of Columbia), with each state receiving a proportionate share of the funds based upon the volume of the retail branch originated real estate secured loans made by Household in that state during the period between 1 January 1999 and 30 September 2002. Household agreed to deposit these monies into the fund in three equal instalments. Household made the first two deposits on 15 January and 14 February 2003. It will make the remaining deposit on 17 March 2003.

Household has also paid US\$10.2 million to the states as reimbursement for the expenses of their investigation and will pay US\$9.8 million of the fees and expenses of an independent administrator. At its expense, Household will also retain an independent monitor to report on Household's compliance with the Multi-State Settlement Agreement over the next five years.

Each borrower that receives a payment under the Multi-State Settlement Agreement will be required to release all civil claims against Household relating to its consumer lending practices. Each state has agreed that the settlement resolves all current civil investigations and proceedings by participating attorneys general and state lending regulators relating to the lending practices at issue.

Household recorded a pre-tax charge in the third quarter of the financial year 2002 of US\$525 million reflecting the costs of the Multi-State Settlement Agreement and related matters.

The Multi-State Agreement first became effective as at 16 December 2002 with the filing of related consent decrees in 41 states and the District of Columbia. Consent decrees or similar documentation have now been entered into with all 50 states and the District of Columbia.

Household has also been named in purported class actions by individuals and consumer groups in the United States (such as the AARP and the Association of Community Organisations for Reform Now) claiming that Household's loan products or its lending policies and practices are unfair or misleading to consumers. Before any claim can proceed on behalf of the purported class, judicial certification of the class is required. To date, none of the class claims have been certified. Although the Multi-State Settlement Agreement does not cause the immediate dismissal of these purported class actions Household believes it substantially reduces the risk to it of any material liability that may result since every consumer who receives payments as a result of the Multi-State Settlement Agreement must release Household from any liability for such claims. Household intends to seek resolution of these related legal actions provided it is financially prudent to do so. Otherwise, Household intends to vigorously dispute the allegations. Regardless of the approach taken by Household with respect to these purported class actions, and based on a review of the allegations set out in the complaints and of their status, Household believes that any liability that may result will not have a material financial impact on Household.

8.2.3 As reported in Household's annual report on Form 10-K/A for the year ended 31 December 2001, which was filed with the SEC on 27 August 2002, Household restated its previously reported consolidated financial statements. The restatement relates to certain MasterCard and Visa co-branding and affinity credit card relationships and a third party marketing agreement, which were entered into between 1992 and 1999. All were part of Household's credit card services segment. In consultation with Household's prior auditors, Arthur Andersen LLP, Household treated payments made in connection with these agreements as pre-paid assets and amortised them in accordance with the underlying economics of the agreements. Household's current auditors, KPMG LLP, advised Household that, in their view, these payments should have either been charged against earnings at the time they were made or amortised over a shorter period of time. There was no significant change as a result of these adjustments on the prior periods net earnings trends previously reported. The restatement resulted in a US\$359.9 million, after-tax, retroactive reduction to retained earnings at 31 December 2001. As a result of the restatement, Household and its directors, certain officers and former auditors have been involved in various legal proceedings, some of which purport to be class actions, alleging violations of US federal securities law. These actions, which were filed between August and October 2002, seek to recover damages in respect of allegedly false and misleading statements about Household's stock. To date, none of the class claims have been certified. These legal actions have been consolidated into a single action (with the Lawrence E. Jaffe Pension Plan as the lead plaintiff); a consolidated and amended complaint is to be filed by 7 March 2003. Since the complaint has not yet been filed, it is not possible to state what damages are sought. Household believes that it has not, and its officers and directors have not, committed any wrongdoing and in each instance there will be no finding of improper activities that may result in a material liability to Household or any of its officers or directors.

8.3 Household is subject to ongoing regulation by the SEC, the OCC and various other US (federal and state) and foreign regulatory agencies, which agencies have broad oversight, supervisory and enforcement powers. Within the scope of these powers, requests have been made, to which Household has responded, for factual materials surrounding the matters covered under paragraphs 8.2.2 and 8.2.3 above. Household believes that it has not, and its officers and directors have not, committed any wrongdoing and there will be no finding of improper activities that may result in a material liability to Household or any of its officers or directors.

9 Risk Factors

9.1 HSBC Holdings has not quantified the significant cost synergies and revenue enhancements expected to result from, and may fail to realise the benefits of, the Acquisition

HSBC Holdings and Household entered into the Merger Agreement with the expectation that the Acquisition would result in significant cost synergies and revenue enhancements from additional business opportunities; however, HSBC Holdings has not attempted to quantify these expected cost synergies and revenue enhancements. HSBC Holdings and Household believe that the Acquisition will result in a lower cost of funding for Household and increased cost savings in the areas of administrative support and information technology and through consolidating card processing. In addition, the Acquisition offers significant opportunities to capture new customer business for both companies, to market products to each other's customers, to migrate customers from Household to the HSBC Group as their financial circumstances improve and to link Household's Hispanic customer base with the HSBC Group's Mexican banking network, and the HSBC Group's Mexican banking network, including the recently acquired GF Bital, with Household's consumer finance capabilities for qualifying emigrants.

HSBC Holdings may fail to realise some or all of the benefits of these cost savings as a result of, among other things, Household's failure to benefit from the HSBC Group's lower funding costs, the failure to consolidate successfully the HSBC Group's North American card processing business with Household's, or to expand Household's credit card platforms across wider geographical markets, or the continued duplication of administrative functions. HSBC Holdings also may fail to realise some or all of the benefits of new business opportunities because, among other reasons, it is unable to take advantage fully of cross-selling opportunities, its marketing efforts are unsuccessful or it fails to provide an effective infrastructure for linking customers to networks or retaining customers. Despite Household's experience in forecasting credit risks and costs, HSBC Holdings may also fail to realise some of the benefits of the Acquisition if the US economy and consumer credit levels significantly deteriorate.

9.2 Regulatory requirements or conditions may reduce the anticipated benefits of the Acquisition

As a result of the Acquisition, Household's subsidiaries will become subject to examination by and the supervision of the FRB. They will also become subject to the requirements of the Bank Holding Company Act of 1956, as amended (the "BHCA"), which generally limit the activities in which a financial holding company such as HSBC Holdings may directly or indirectly engage in the United States to those that are "financial in nature". While none of these businesses is material to Household or the enlarged group, as at the second anniversary of the Acquisition, any Household subsidiary engaged in any activity that has not been determined by the FRB to be financial in nature will have to divest such activity unless it otherwise qualifies for an exemption under the BHCA. For example, Household currently owns companies or assets on which it previously foreclosed that are engaged in or involve activities that are not financial in nature. As at the second anniversary of the Acquisition, any such activities may need to be divested. In addition, one or more of the various banking, consumer finance, insurance and other regulatory agencies whose approvals are required in connection with the Acquisition may impose conditions on such approvals. Such requirements or conditions could have an adverse effect on HSBC Holdings or reduce the potential benefits of the Acquisition.

9.3 Household's business, including the business of lending to non-prime consumers, involves special legal, regulatory and reputational considerations

Household is considered to be a lender to the non-prime consumer market as these consumers account for approximately 37 per cent of receivables on a managed basis. Non-prime consumers are individuals who have limited credit histories, modest income, high debt-to-income ratios or have experienced credit problems caused by occasional delinquencies, prior charge-offs or other credit related actions. These consumers generally have higher delinquency and credit loss probabilities and are charged a higher interest rate to compensate for the additional risk and for where the loan is not adequately collateralized to mitigate the risk of loss. The major participants in the business of lending to non-prime consumers, including Household and its principal competitors, have been subject to litigation, adverse publicity and regulatory scrutiny involving allegations of improper practices, including alleged violations of US federal and state consumer protection, consumer finance and banking laws and regulations. Also, Household has been named in purported class actions by individuals and consumer groups (such as AARP and the Association of Community Organisations for Reform Now ("ACORN")) claiming that its loan products or its lending policies and practices are unfair or misleading to consumers.

On 11 October 2002, Household announced that it had reached preliminary agreement in respect of the Multi-State Settlement Agreement, which became effective as at 16 December 2002. Consent decrees or similar documentation have now been entered into with all 50 US states and the District of Columbia. Under the Multi-State Settlement Agreement, Household has committed to make changes to some of its lending practices, including providing greater disclosures and alternatives for customers in connection with non-prime mortgage lending originated by its retail branch network and amending all branch-originated real estate secured loans to provide that no prepayment penalty is payable later than 24 months after origination. The Multi-State Settlement Agreement required Household to establish a fund of US\$484 million to be divided among all participating US states (including the District of Columbia), with each state receiving a proportionate share based upon the volume of the retail branch originated real estate secured loans made by Household in that state during the period between 1 January 1999 and 30 September 2002. Household agreed to deposit these monies into the fund in three equal instalments. On 15 January 2003 and 14 February 2003, Household made the first two deposits and will make the remaining deposit on 17 March 2003. Household has also paid US\$10.2 million to the states as reimbursement for the expenses of their investigation and will pay US\$9.8 million of the fees and expenses of an independent administrator. At its expense, Household will also retain an independent monitor to report on Household's compliance with the settlement over the next five years.

Although each consumer that receives a payment under the Multi-State Settlement Agreement must release Household from all civil claims relating to its consumer lending practices, the Multi-State Settlement Agreement itself does not cause the immediate dismissal of purported class actions seeking redress for the claims covered by the Multi-State Settlement Agreement and there can be no assurance that all plaintiffs and potential plaintiffs will participate in the Multi-State Settlement Agreement. Also, Household expects that various consumer groups, including those that have brought purported class actions against Household in the past, will continue to target Household in the media and with legal actions in an effort to effect additional changes to the non-prime mortgage lending industry.

9.4 Legal actions relating to the Acquisition and Household's prior financial disclosures

Several derivative and/or purported class action lawsuits have been filed against Household and various of its directors and officers alleging violations of fiduciary duty and corporate waste with respect to the Acquisition. Some of these lawsuits seek to prohibit the Acquisition. While these lawsuits are in their preliminary stages and Household intends to defend them vigorously, there can be no assurance that the outcome of these lawsuits will be favourable to Household.

In connection with Household's restatement of its prior period financial results in August 2002 and other disclosure matters, Household, its directors, certain officers and former auditors have been subjected to various legal actions and proceedings, including several purported class action lawsuits, alleging violations of US federal securities laws. Although Household believes that its officers and directors have not committed any wrongdoing and that there will be no resulting material liability to Household or any of its officers and directors, there can be no assurance as to the ultimate outcome of these actions and proceedings.

9.5 Forward-looking statements

This document contains certain forward-looking statements with respect to the financial condition, results of operations and business of HSBC Holdings, Household and the enlarged group.

Statements that are not historical facts, including statements about HSBC Holdings' or Household's beliefs and expectations, are forward-looking statements. Words such as "expects", "anticipates", "intends", "plans", "believes", "seeks", "estimates", "potential", "opportunity", "reasonably possible" and variations of these words and similar expressions are intended to identify forward-looking statements. These statements are based on current plans, estimates and projections, and therefore undue reliance should not be placed on them. Forward-looking statements speak only as of the date they are made, and it should not be assumed that they have been revised or updated in the light of new information or future events.

Forward-looking statements involve inherent risks and uncertainties.

10 Consents

- 10.1 Each of Cazenove & Co. Ltd., Morgan Stanley, Rohatyn Associates and HSBC Bank has given and not withdrawn its written consent to the inclusion herein of the references to its name in the form and context in which it is included.
- 10.2 KPMG Audit Plc has given and not withdrawn its written consent to the inclusion of its reports in Parts II and III of this document and references to its name and such reports in the form and context in which they are included.

11 General

- 11.1 The Company is incorporated in England and Wales with registered number 617987. The Company's registered office is at 8 Canada Square, London E14 5HQ, United Kingdom.
- 11.2 In accordance with FSMA and the Listing Rules, Listing Particulars have been published by HSBC Holdings in connection with the issue of the New HSBC Ordinary Shares and delivered to the Registrar of Companies in England and Wales for registration as required by section 83 of FSMA. Summary Particulars are being sent to Household Shareholders. Copies of the Listing Particulars may be obtained free of charge by calling the following Listing Particulars Request Lines until the Effective Date: in the United Kingdom, on freephone 0800 073 3918; in Hong Kong on 2862 8666; and elsewhere on +44 870 703 0137. You may inspect the Listing Particulars at the offices of Norton Rose at Kempson House, Camomile Street, London EC3A 7AN, United Kingdom and at the offices of The Hongkong and Shanghai Banking Corporation Limited at Level 37, 1 Queen's Road Central, Hong Kong. The Listing Particulars and the Circular will also be available for inspection free of charge at the document viewing facility located at the FSA, 25 The North Colonnade, Canary Wharf, London E14 5HS, United Kingdom.
- 11.3 It is expected that supplementary listing particulars, containing extracts from HSBC Holdings' audited accounts for the financial year ended 31 December 2002 will be published on or around 3 March. Supplementary listing particulars containing extracts from Household's audited accounts for the financial

year ended 31 December 2002 are expected to be published in early March 2003. The supplementary listing particulars will be made available on HSBC Group's website at www.hsbc.com on the date of their publication. Copies of the supplementary listing particulars may be obtained free of charge by calling the Listing Particulars Request Lines set out in paragraph 11.2 above. The supplementary listing particulars will be available for inspection at the offices of Norton Rose at Kempson House, Camomile Street, London EC3A 7AN, United Kingdom and at the offices of The Hongkong and Shanghai Banking Corporation Limited at Level 37, 1 Queen's Road Central, Hong Kong during usual business hours on any weekday (Saturdays and public holidays excepted) until the Effective Date and at the Extraordinary General Meeting. The supplementary listing particulars may also be inspected free of charge at the document viewing facility located at the FSA, 25 The North Colonnade, Canary Wharf, London E14 5HS, United Kingdom.

- 11.4 Certain financial projections (including in relation to estimated synergy benefits of the Acquisition) for Household are comprised in the Proxy Statement/Prospectus filed with the SEC and have been disclosed in calls between the management of Household and analysts or investors including, but without limitation, analysts' calls on 11 October 2002 and 14 November 2002 and an investor call on 6 November 2002. In addition certain financial projections for the enlarged group are contained in the Proxy Statement/Prospectus. Certain of the financial projections for Household and the enlarged group comprised in the Proxy Statement/Prospectus were included by Goldman, Sachs & Co., financial adviser to Household, in connection with their opinion delivered to the Household board and are based on information provided by Household's management and publicly available estimates. The other financial projections for Household contained in the Proxy Statement/Prospectus or disclosed in the calls mentioned above were prepared by Household's management.

These projections were neither seen nor commented upon by HSBC Holdings or its advisers in advance of their preparation and no reliance should be placed on them. The financial projections do not necessarily reflect the Directors' view of Household's prospects and financial performance nor the prospects and financial performance of the enlarged group. The financial projections should not be regarded as a reliable indicator of Household's future operating results nor the operating results of the enlarged group and they should not be relied upon as such.

These projections were prepared prior to the announcement of the Acquisition. Not all of the estimates and assumptions upon which they were based are stated and the facts supporting the estimates and assumptions upon which they were stated to have been based may have since changed. In addition, the base data underlying them may now be out of date.

None of HSBC Holdings or its financial advisers or any other party accepts responsibility for the accuracy, reasonableness, validity or completeness of the financial projections or the estimates and assumptions that underlie them.

None of the financial projections was intended for publication by HSBC Holdings and should not be regarded as a forecast of profits by HSBC Holdings, Household or any of their respective directors and accordingly have not been prepared or reviewed to a standard to which published projections would be prepared and reviewed. Shareholders should not rely upon any of the financial projections in making any decision about investment in HSBC Holdings or Household or in deciding whether or not to approve the Acquisition.

12 Bases and Sources of Financial and Other Information

- 12.1 The financial information contained in this document in relation to HSBC Holdings does not constitute statutory accounts within the meaning of section 240 of the Act, but constitutes non-statutory accounts within the meaning of such section. The auditors of HSBC Holdings are KPMG Audit Plc, 8 Salisbury Square, London EC4Y 8BB, United Kingdom who have audited HSBC Holdings' consolidated accounts for the three financial years ended 31 December 2001 in accordance with UK auditing standards and have made reports under section 235 of the Act in respect of each set of statutory accounts and each such report was unqualified and did not contain a statement under section 237(2) or (3) of the Act.
- 12.2 The financial information set out in Part II of this document has been extracted without material adjustment from the audited restated consolidated income statements of Household for the years ended 31 December 1999, 2000 and 2001 and the audited restated consolidated balance sheets as at 31 December

2000 and 2001, as reported on Form 10-K/A. The financial information in respect of the balance sheet as at 31 December 1999 set out in Part II of this document has been extracted from the financial statements included in Household's filing with the SEC on Form 10-K for the year ended 31 December 1999, as audited by Household's former auditors, Arthur Andersen, LLP.

- 12.3 The qualification of the expert, who has given its opinion on 26 February 2003 for incorporation in this document (and not withdrawn such opinion), is as follows:

Name	Country	Qualification
KPMG Audit Plc	United Kingdom	Chartered accountants

KPMG Audit Plc does not have any shareholding in HSBC Holdings or its subsidiaries (as defined by section 2 of the Companies Ordinance) or any right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in HSBC Holdings or its subsidiaries.

13 Documents Available for Inspection

Copies of the following documents may be inspected at the offices of Norton Rose at Kempson House, Camomile Street, London EC3A 7AN, United Kingdom or at the offices of The Hongkong and Shanghai Banking Corporation Limited at Level 37, 1 Queen's Road Central, Hong Kong during usual business hours on any weekday (Saturdays and public holidays excepted) until the Effective Date and at the EGM:

- 13.1 the Memorandum and Articles of Association of HSBC Holdings;
- 13.2 the audited consolidated accounts of the HSBC Group for each of the two financial years ended 31 December 2001 and 2000 and the interim results for the six month period ended 30 June 2002;
- 13.3 the audited consolidated accounts of the Household Group for each of the two financial years ended 31 December 2001 and 2000, the Forms 10-Q and 10-Q/A filed with the SEC for each of the three month periods ended 31 March 2002, 30 June 2002 and 30 September 2002 and the earnings release statement for the financial year ended 31 December 2002;
- 13.4 the report from KPMG Audit Plc regarding the reconciliations of the financial information on Household to UK GAAP set out in Part II of this document;
- 13.5 the report from KPMG Audit Plc on the pro forma financial information set out in Part III of this document;
- 13.6 the Proxy Statement/Prospectus;
- 13.7 the Listing Particulars;
- 13.8 the service contracts of the Directors and the Proposed Director of HSBC Holdings referred to in paragraph 5 of this Part V;
- 13.9 the material contracts referred to in paragraph 6 of this Part V;
- 13.10 the letters of consent referred to in paragraph 10 of this Part V; and
- 13.11 this document.

Dated 26 February 2003

Definitions

The following definitions apply throughout this document, unless the context requires otherwise:

“Acquisition”	the proposed acquisition by way of merger of Household by a wholly owned subsidiary of HSBC Holdings, details of which are set out in this document
“Act”	the Companies Act 1985, as amended
“Additional HSBC Ordinary Shares”	HSBC Ordinary Shares which may be issued following the Effective Date: <ul style="list-style-type: none">(i) as provided for or contemplated by the Merger Agreement on the exercise of outstanding options over, or rights to acquire, Household Common Shares under the Household Option Plans or the Household Stock-based Awards; or(ii) pursuant to the terms of the future purchase contracts underlying the Household Equity Units or pursuant to the terms of the Household Zero-coupon Debt Securities
“Business Day”	a day on which banks are generally open for business in London, UK or New York, United States (excluding Saturdays, Sundays and public holidays)
“CCF”	CCF S.A.
“certificated” or “in certificated form”	a share or other security which is not in uncertificated form
“common stock”	the US equivalent of ordinary shares in a UK company
“Companies Ordinance”	Companies Ordinance Chapter 32 of the Laws of Hong Kong
“Consideration Shares”	HSBC Ordinary Shares to be issued to the holders of Household Common Shares (other than the Excluded Shares) as at the Effective Time in consideration for the cancellation of such Household Common Shares pursuant to the Merger Agreement
“CREST”	a relevant system (as defined in the Regulations) in respect of which CRESTCo Limited is the Operator (as defined in the Regulations) being a paperless system enabling the settlement of trades in listed securities
“Daily Official List”	the Daily Official List of the London Stock Exchange
“Directors”	the directors of HSBC Holdings, whose names are set out on page 93 of this document
“Effective Date”	the date on which the Effective Time occurs and the Acquisition becomes effective
“Effective Time”	the time at which HSBC Holdings and Household file a certificate of merger with the Secretary of State of the State of Delaware or such later date and time as is specified in the certificate of merger
“enlarged group”	the HSBC Group as enlarged by the Acquisition
“Euronext Paris”	Euronext Paris S.A.

“Exchange Agent”	Computershare Investor Services LLC in its capacity as exchange agent, or failing them, another agent acceptable to Household
“Exchange Ratio”	as set out in paragraph 2.1 of Section A of Part IV of this document
“Excluded Shares”	Household Common Shares held, as at the Effective Time, by: (a) HSBC Holdings or any of its subsidiaries or by any subsidiary of Household unless held for the account or benefit of any third party; or (b) by Household in treasury
“Executive Directors”	the Directors who are described as Executive Directors on page 93 of this document
“Extraordinary General Meeting” or “EGM”	the extraordinary general meeting of HSBC Holdings convened for 11.00 a.m. on 28 March 2003, notice of which is set out at the end of this document, for the purpose, inter alia, of giving approval to the Acquisition
“FAS”	Statement of Financial Accounting Standards issued by the FASB
“FASB”	The Financial Accounting Standards Board of the United States
“FRB”	the Board of Governors of the United States Federal Reserve System
“FRS”	Financial Reporting Standard issued by the Accounting Standards Board
“FSA”	The Financial Services Authority
“FSMA”	The Financial Services and Markets Act 2000, as amended
“H2”	H2 Acquisition Corporation, a wholly owned subsidiary of HSBC Holdings incorporated in Delaware
“Hong Kong”	The Hong Kong Special Administrative Region of the People’s Republic of China
“Hong Kong dollars” or “HK\$”	the lawful currency of Hong Kong
“Hong Kong Stock Exchange”	The Stock Exchange of Hong Kong Limited
“Household”	Household International, Inc.
“Household Common Shareholders”	holders of issued and outstanding Household Common Shares
“Household Common Shares”	shares of Household common stock with par value of US\$1.00 per share
“Household Equity Units”	the 8.875 per cent Adjustable Conversion-Rate Equity Security Units of Household (of which 21,662,962 were outstanding as at 31 January 2003), each unit having a stated amount of US\$25 and consisting of initially (a) a contract pursuant to which the holder agrees to purchase, for US\$25, Household Common Shares on 15 February 2006 (a maximum of 25,306,672 Household Common Shares being issuable under the outstanding units) and (b) a senior note of Household Finance Corporation, a subsidiary of Household, with a principal amount of US\$25
“Household Group”	Household and its subsidiary undertakings and where the context requires, its interests in joint ventures and associated undertakings

“Household Non-voting Preferred Stock”	Household’s: (a) 7% per cent Cumulative Preferred Stock, Series 2002-B; (b) 7.50 per cent Cumulative Preferred Stock, Series 2001-A; (c) 7.60 per cent Cumulative Preferred Stock, Series 2002-A; and (d) 8¼ per cent Cumulative Preferred Stock, Series 1992-A
“Household Option Plans”	Household’s: (a) 1996 Long Term Executive Incentive Compensation Plan; (b) Long Term Executive Incentive Compensation Plan and Beneficial Corporation 1990 Non-Qualified Stock Option Plan; (c) Beneficial Corporation Benshares Equity Participation Plan; and (d) Renaissance Amended and Restated 1997 Incentive Plan, each as amended
“Household Preferred Stock”	the Household Voting Preferred Stock and the Household Non-voting Preferred Stock
“Household Shareholders”	holders of Household Shares
“Household Shares”	the Household Common Shares and the Household Voting Preferred Stock
“Household Stock-based Awards”	any right to receive Household Common Shares or benefits measured by the value of a number of Household Common Shares, or any award consisting of Household Common Shares, granted under any Household benefit plan (including restricted stock, restricted stock units, deferred stock units and dividend equivalents) other than options over Household Common Shares granted under the Household Option Plans or otherwise
“Household Stock Purchase Plans”	the Household Employee Stock Purchase Plan and the Household Dividend Reinvestment and Common Stock Purchase Plan
“Household Voting Preferred Stock”	Household’s: (a) 5 per cent Cumulative Preferred Stock (b) US\$4.50 Cumulative Preferred Stock; and (c) US\$4.30 Cumulative Preferred Stock
“Household Zero-coupon Debt Securities”	Household’s 30 outstanding zero-coupon convertible debt securities (each with a principal amount of US\$1,000) which may be converted in certain circumstances into a total of 270 Household Common Shares
“HSBC ADS”	an American depositary share representing five HSBC Ordinary Shares
“HSBC Bank”	HSBC Bank plc, a wholly owned subsidiary of HSBC Holdings
“HSBC Board”	the board of Directors of HSBC Holdings
“HSBC Group”	HSBC Holdings and its subsidiary undertakings and, where the context requires, its interests in joint ventures and associated undertakings
“HSBC Holdings”	HSBC Holdings plc
“HSBC Ordinary Shareholders”	holders of HSBC Ordinary Shares
“HSBC Ordinary Shares”	the ordinary shares of US\$0.50 each in the capital of the Company from time to time
“HSR Act”	the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (as amended) of the United States

“Listing Particulars”	the listing particulars published by HSBC Holdings in connection with its applications to the UK Listing Authority and the London Stock Exchange for the New HSBC Ordinary Shares to be admitted to the Official List and to trading on the London Stock Exchange’s market for listed securities
“Listing Rules”	the listing rules made by the UK Listing Authority under section 74 of FSMA, as amended from time to time
“London Stock Exchange”	London Stock Exchange plc
“Material Adverse Effect”	with respect to HSBC Holdings or Household, as the case may be, a material adverse effect on: <ul style="list-style-type: none"> (a) the business, assets, liabilities, results of operations or financial condition of such party and its subsidiaries taken as a whole, other than any such effect arising as a result of: (i) the impact of the public disclosure of the transactions contemplated under the Merger Agreement; (ii) changes in laws, rules or regulations of general applicability or interpretations thereof by courts or governmental or regulatory entities after the date of the Merger Agreement; (iii) changes, after the date of the Merger Agreement, in applicable generally accepted accounting principles or regulatory accounting requirements generally applicable to comparable companies; (iv) actions or omissions of a party to the Merger Agreement taken with the prior written consent of the other parties to that Agreement; and (v) changes, after the date of the Merger Agreement, in general economic and market conditions except, in the case of (ii), (iii) and (v), to the extent that such changes have a disproportionately adverse effect on the relevant party and its subsidiaries relative to comparable businesses; or (b) the ability of such party to perform its material obligations under the Merger Agreement and to consummate the transactions contemplated therein
“Merger Agreement”	the agreement and plan of merger dated 14 November 2002 between HSBC Holdings, Household and H2
“Merger Regulation”	Council Regulation (EEC) No. 4064/89, as amended
“Morgan Stanley”	Morgan Stanley & Co. Limited
“Multi-State Settlement Agreement”	the agreement described in paragraph 8.2.2 of Part V of this document
“New HSBC Ordinary Shares”	the Consideration Shares and/or the Additional HSBC Ordinary Shares
“New York Stock Exchange”	The New York Stock Exchange, Inc.
“Noon Buying Rate”	the noon buying rate in New York City for cable transfers in the relevant foreign currency as certified for customs purposes by the Federal Reserve Bank of New York
“Official List”	the Official List of the UK Listing Authority
“OFT”	the Office of Fair Trading
“Proposed Director”	Mr. William Frederick Aldinger, III

“Proxy Statement/Prospectus”	the proxy statement/prospectus distributed to Household Shareholders in connection with their approval of the Acquisition
“Regulations”	the Uncertificated Securities Regulations 2001 (SI 2001/3755), as amended from time to time
“Resolution”	the ordinary resolution set out in the Notice of EGM at the end of this document
“Rohatyn Associates”	Rohatyn Associates LLC
“SDI Ordinance”	Securities (Disclosure of Interests) Ordinance Chapter 396 of the Laws of Hong Kong
“SEC”	US Securities and Exchange Commission
“SSAP”	Statement of Standard Accounting Practice issued by the Accounting Standards Board
“sterling”, “£” and “p”	the lawful currency of the UK
“UK GAAP”	generally accepted accounting principles in the UK
“UK Listing Authority” or “UKLA”	the FSA, acting in its capacity as the competent authority for the purposes of Part VI of FSMA
“uncertificated” or “in uncertificated form”	a share recorded in the HSBC Holdings’ register of HSBC Ordinary Shareholders as being held in uncertificated form, title to which, by virtue of the Regulations, may be transferred by means of an instruction issued in accordance with the rules of CREST
“United Kingdom” or “UK”	the United Kingdom of Great Britain and Northern Ireland
“United States”, “US” or “USA”	the United States of America, its territories and possessions, any state of the United States of America and the District of Columbia and all other areas subject to its jurisdiction
“US dollars” or “US\$”	the lawful currency of the United States
“US GAAP”	generally accepted accounting principles in the United States
“US Tax Code”	the United States Internal Revenue Code of 1986, as amended

For the purposes of the above definitions, **“subsidiary undertaking”**, **“associated undertaking”** and **“undertaking”** have the meanings given by the Act (but for these purposes ignoring paragraph 20(1)(b) of Schedule 4A of the Act), and **“subsidiary”** has the meaning given thereto by sections 736 and 736A of the Act.

HSBC Holdings plc

Notice of Extraordinary General Meeting

Notice is hereby given that an Extraordinary General Meeting of HSBC Holdings plc (the “**Company**”) will be held at Cabot Hall, Cabot Place West, Canary Wharf, London E14 5AB, United Kingdom on 28 March 2003 at 11.00 am to consider and, if thought fit, pass the following resolution:

ORDINARY RESOLUTION

THAT:

- (a) the acquisition by way of merger (the “**Acquisition**”) of Household International, Inc. (“**Household**”) on the terms and subject to the conditions of the agreement dated 14 November 2002 between (1) the Company, (2) Household and (3) H2 Acquisition Corporation (a copy of which, signed by the chairman of the Meeting for the purposes of identification, was produced to the Meeting) (the “**Merger Agreement**”) (including the arrangements to be put in place regarding: (i) the outstanding options to acquire common stock of Household granted by Household to any current or former employee or director of Household or any of its subsidiaries; (ii) any right of any kind, contingent or accrued, to receive common stock of Household; and (iii) any award of any kind consisting of common stock of Household granted under any Household benefit plan (including restricted stock, restricted stock units, deferred stock units and dividend equivalents) (together “**Assumed Options**”)), as described in the circular to shareholders of the Company of which this notice forms part, be and is hereby approved and the Directors (or a duly authorised committee thereof) be and are hereby authorised to take all such steps to implement the same and to execute all documents and deeds as may be necessary or appropriate in relation thereto, subject to such non-material modifications, amendments, waivers, variations or extensions of such terms and conditions as they think fit; and
- (b) conditional upon and with effect from the Acquisition becoming effective pursuant to the Merger Agreement, the Directors be and they are hereby generally and unconditionally authorised pursuant to and for the purposes of section 80 of the Companies Act 1985 to exercise all the powers of the Company to allot relevant securities (within the meaning of that section) up to an aggregate nominal amount of US\$702,863,189 (in the form of ordinary shares of US\$0.50 each) in satisfaction of the Company’s obligations arising in relation to the Acquisition to issue ordinary shares, including shares to be issued as a result of the exercise of the Assumed Options and shares to be issued pursuant to the terms of the purchase contracts underlying the Household 8.875 per cent Adjustable Conversion-Rate Equity Security Units and shares to be issued pursuant to the Household zero-coupon convertible debt securities, such authority to be in addition to, and without prejudice to, that granted to the Directors at the annual general meeting of the Company held on 31 May 2002 (which shall remain in full force and effect until its expiry as stated therein), provided that this authority shall expire at the conclusion of the Company’s annual general meeting to be held in 2004, unless such authority is renewed, varied, or revoked by the Company in general meeting, save that the Company may at any time before such expiry make an offer or agreement which would or might require relevant securities to be allotted after such expiry and the Directors may allot relevant securities in pursuance of any such offer or agreement as if the authority hereby conferred had not expired.

By Order of the Board

R G Barber
Group Company Secretary

HSBC Holdings plc
Incorporated in England with limited liability.
Registered in England: number 617987
Registered Office and Group Head Office: 8 Canada Square, London E14 5HQ, United Kingdom

26 February 2003

Notes:

- (1) A member entitled to attend and vote at the Meeting is entitled to appoint one or more proxies to attend and, on a poll, vote instead of the member. A proxy need not be a member. Completion and submission of an instrument appointing a proxy will not preclude a member from attending and voting in person at the Meeting.
- (2) In order to be valid, the instrument appointing a proxy and the power of attorney or other authority (if any) under which it is signed, or a copy of such authority certified notarially or in some other way approved by the Board, must be deposited at the offices of Computershare Investor Services PLC, PO Box 451, Owen House, 8 Bankhead Crossway North, Edinburgh EH11 0NU, United Kingdom, or at the offices of Computershare Hong Kong Investor Services Limited, Rooms 1901-1905, Hopewell Centre, 183 Queen's Road East, Hong Kong, not less than 48 hours before the time of the holding of the Meeting (or any adjourned meeting). In the case of an appointment of a proxy submitted in electronic form, such appointment must be received not less than 48 hours before the time of the holding of the Meeting (or any adjourned meeting). However, you should note that any power of attorney or other authority relating to an appointment cannot be submitted electronically and must be deposited as referred to above for the appointment to be valid.
- (3) Pursuant to the Uncertificated Securities Regulations 2001, changes to entries on the principal register of members of the Company maintained in England (the "Principal Register") after midnight (London time) on the day prior to the day immediately before the Meeting or any adjourned meeting (as the case may be) shall be disregarded in determining the rights of a member to attend or vote at the Meeting or any adjourned meeting (as the case may be). Accordingly, a member entered on the Principal Register at midnight on the day prior to the day immediately before the Meeting or any adjourned meeting (as the case may be) shall be entitled to attend and vote at the Meeting or any adjourned meeting (as the case may be) in respect of the number of such shares entered against the member's name at the time.
- (4) In the case of joint registered holders of any share, the vote of the senior who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders. For this purpose seniority shall be determined by the order in which the names of the holders stand in the Principal Register or the Hong Kong Overseas Branch Register of the Company, as appropriate.
- (5) For safety reasons, security checks will be carried out on entry to the Meeting. Shareholders are reminded that briefcases, cameras and tape-recorders will not be allowed in the Meeting and that all mobile telephones must be switched off.
- (6) The purpose of the resolution is: (a) to approve the Acquisition (including the arrangements to be put in place in relation to certain outstanding options over, and rights to acquire, Household shares, in respect of which New HSBC Ordinary Shares may be issued); and (b) to authorise the Directors for the purposes of section 80 of the Companies Act 1985 to allot Ordinary Shares to existing holders of Household shares, and to holders of such options or rights, as provided for or contemplated by the Merger Agreement or pursuant to the terms of the purchase contracts underlying the Household 8.875 per cent Adjustable Conversion-Rate Equity Security Units or pursuant to the terms of the Household zero-coupon convertible debt securities.
- (7) In the case of a conflict between any translation and the English text hereof, the English text will prevail.
- (8) CREST members who wish to appoint a proxy or proxies by utilising the CREST electronic proxy appointment service may do so for the extraordinary general meeting and any adjournment(s) thereof by utilising the procedures described in the CREST manual. CREST Personal Members or other CREST sponsored members, and those CREST members who have appointed a voting service provider, should refer to their CREST sponsor or voting service provider, who will be able to take the appropriate action on their behalf.

In order for a proxy appointment made by means of CREST to be valid, the appropriate CREST message (a "CREST Proxy Instruction") must be properly authenticated in accordance with CRESTCo's specifications and must contain the information required for such instructions, as described in the CREST Manual. The message must be transmitted so as to be received by the issuer's agent (ID 3RA50) by the latest time for receipt of proxy appointments specified in the notice of meeting. For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by the CREST Applications Host) from which the issuer's agent is able to retrieve the message by enquiry to CREST in the manner prescribed by CREST.

CREST members and, where applicable, their CREST sponsors or voting service providers should note that CRESTCo does not make available special procedures in CREST for any particular messages. Normal system timings and limitations will therefore apply in relation to the input of CREST Proxy Instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member is a CREST personal member or sponsored member or has appointed a voting service provider, to procure that his CREST sponsor or voting service provider takes) such action as shall be necessary to ensure that a message is transmitted by means of the CREST system by any particular time. In this connection, CREST members and, where applicable, their CREST sponsors or voting service providers are referred, in particular, to those sections of the CREST Manual concerning practical limitations of the CREST system and timings.

The Company may treat as invalid a CREST Proxy Instruction in the circumstances set out in Regulation 35(5)(a) of the Uncertificated Securities Regulations 2001.

