# Full Year 2023 Financial Results Announcement

Virgin Money UK PLC
Registered number 09595911 (England and Wales)
ARBN 609 948 281 (Australia)

2023

## BASIS OF PRESENTATION

Virgin Money UK PLC ('Virgin Money', 'VMUK' or 'the Company'), together with its subsidiary undertakings (which together comprise 'the Group'), operate under the Clydesdale Bank, Yorkshire Bank and Virgin Money brands. This results announcement covers the results of the Group for the year ended 30 September 2023.

**Statutory basis**

Statutory information is set out on page 17 and within the financial statements.

**Underlying basis**

Management exclude certain items from the Group's statutory position to arrive at an underlying performance basis. A reconciliation from the underlying results to the statutory basis is shown on page 17 and rationale for the adjustments is shown on page 133.

**Alternative performance measures (APMs)**

The KPIs and performance metrics used in monitoring the Group's performance and reflected throughout this results announcement are determined on a combination of bases (including statutory, regulatory and alternative performance measures), as detailed at 'Measuring the Group's performance' on pages 122 to 132. APMs are closely scrutinised to ensure that they provide genuine insights into the Group's progress; however statutory measures are the key determinant of dividend paying capability.

Certain figures contained in this document, including financial information, may have been subject to rounding adjustments and foreign exchange conversions. Accordingly, in certain instances, the sum or percentage change of the numbers contained in this document may not conform exactly to the total figure given.

The information contained within this announcement is deemed by the Group to constitute inside information as stipulated under the Market Abuse Regulation No 596/2014. Upon the publication of this announcement via Regulatory Information Service, this inside information is now considered to be in the public domain.

## FORWARD-LOOKING STATEMENTS

This document and any other written or oral material discussed or distributed in connection with the results (the 'Information') may include forward-looking statements, which are based on assumptions, expectations, valuations, targets, estimates, forecasts and projections about future events. These can be identified by the use of words such as 'expects', 'aims', 'targets', 'seeks', 'anticipates', 'plans', 'intends', 'prospects', 'outlooks', 'projects', 'forecasts', 'believes', 'estimates', 'potential', 'possible', and similar words or phrases. These forward-looking statements are subject to risks, uncertainties and assumptions about the Group and its securities, investments and the environment in which it operates, including, among other things, the development of its business and strategy, any acquisitions, combinations, disposals or other corporate activity undertaken by the Group, trends in its operating industry, changes to customer behaviours and covenant, macroeconomic and/or geo-political factors, the repercussions of the outbreak of coronaviruses (including, but not limited to, the COVID-19 outbreak), changes to its Board and/or employee composition, exposures to terrorist activity, IT system failures, cybercrime, fraud and pension scheme liabilities, risks relating to environmental matters such as climate change including the Group's ability along with the government and other stakeholders to measure, manage and mitigate the impacts of climate change effectively, changes to law and/or the policies and practices of the Bank of England (BoE), the Financial Conduct Authority (FCA) and/or other regulatory and governmental bodies, inflation, deflation, interest rates, exchange rates, tax and national insurance rates, changes in the liquidity, capital, funding and/or asset position and/or credit ratings of the Group, future capital expenditures and acquisitions, the repercussions of Russia's invasion of Ukraine, the repercussions of the UK's exit from the European Union (EU) (including any change to the UK's currency and the terms of any trade agreements (or lack thereof) between the UK and the EU), Eurozone instability, any referendum on Scottish independence, and any UK or global cost of living crisis or recession.

In light of these risks, uncertainties and assumptions, the events in the forward-looking statements may not occur. Forward-looking statements involve inherent risks and uncertainties and should be viewed as hypothetical. Other events not taken into account may occur and may significantly affect the analysis of the forward-looking statements. No member of the Group or their respective directors, officers, employees, agents, advisers or affiliates (each a 'VMUK Party') gives any representation, warranty or assurance that any such projections or estimates will be realised or that actual returns or other results will not be materially lower than those set out in the Information. All forward-looking statements should be viewed as hypothetical. No representation or warranty is made that any forward-looking statement will come to pass. While every effort has been made to ensure the accuracy of the Information, no VMUK Party takes any responsibility for the Information or to update or revise it. They will not be liable for any loss or damages incurred through the reliance on or use of it. The Information is subject to change. No representation or warranty, express or implied, as to the truth, fullness, fairness, merchantability, accuracy, sufficiency or completeness of the Information is given.

Certain industry, market and competitive position data contained in the Information comes from official or third-party sources. There is no guarantee of the accuracy or completeness of such data. While the Group reasonably believes that each of these publications, studies and surveys has been prepared by a reputable source, no member of the Group or their respective directors, officers, employees, agents, advisers or affiliates have independently verified the data.

In addition, certain industry, market and competitive position data contained in the Information comes from the Group's own internal research and estimates based on the knowledge and experience of the Group's management in the markets in which the Group operates. While the Group reasonably believes that such research and estimates are reasonable and reliable, they, and their underlying methodology and assumptions, have not been verified by any independent source for accuracy or completeness, and are subject to change. Accordingly, undue reliance should not be placed on any of the industry, market or competitive position data contained in the Information.

The Information does not constitute or form part of, and should not be construed as, any public offer under any applicable legislation or an offer to sell or solicitation of any offer to buy any securities or financial instruments or any advice or recommendation with respect to such securities or other financial instruments. The distribution of the Information in certain jurisdictions may be restricted by law. Recipients are required to inform themselves about and to observe any such restrictions. No liability to any person is accepted in relation to the distribution or possession of the Information in any jurisdiction.

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# Virgin Money UK PLC Full Year Results 2023

## David Duffy, Chief Executive Officer:

"We made good progress executing our strategy in 2023, growing both our relationship customer base and target lending segments. With the momentum we carry into 2024, we are confident in the outlook for our business and we expect to deliver around £800m in distributions to our investors by the end of the three-year period ending in 2024.

"Under the Virgin brand, our ambition is to create the UK's best digital bank. To help achieve this goal, we are stepping up investment in our technological capability to future proof our business and protect our customers from the growing risk of fraud strategies driven by advances in AI."

## Summary financials

| | 2023 £m | 2022 £m | Change % |
|---|---|---|---|
| Underlying net interest income (NII) | **1,716** | 1,592 | 8 |
| Underlying non-interest income(1) | **157** | 150 | 5 |
| **Total underlying operating income** | **1,873** | **1,742** | 8 |
| Underlying operating and administrative expenses | **(971)** | (914) | 6 |
| **Underlying operating profit before impairment losses** | **902** | **828** | 9 |
| Impairment losses on credit exposures | **(309)** | (52) | n.m. |
| **Underlying profit on ordinary activities before tax** | **593** | **776** | (24) |
| Adjusting items(1) | **(248)** | (181) | 37 |
| **Statutory profit on ordinary activities before tax** | **345** | **595** | (42) |
| **Key performance indicators(2)** | | | |
| Total customer lending | **72,754** | **72,565** | 0.3% |
| Net interest margin (NIM) | **1.91%** | **1.85%** | 0.06%pts |
| Underlying cost: income ratio (CIR) | **51.9%** | **52.5%** | (0.6)%pts |
| Statutory return on tangible equity (RoTE) | **3.9%** | **10.3%** | (6.4)%pts |
| Dividends and share buybacks announced | **272** | **267** | 2% |
| Common equity tier 1 (CET1) ratio (IFRS 9 transitional) | **14.7%** | **15.0%** | (0.3)%pts |

(1) Hedge ineffectiveness is now presented as an adjustment to underlying earnings as detailed on page 133. The comparative periods have been adjusted accordingly.
(2) For definitions of the KPIs, refer to 'Measuring the Group's performance' from page 122.

### Delivered strong financial performance and attractive shareholder distributions

- NIM expanded to 1.91% (2022: 1.85%), supported by early management of deposit migration, hedge re-investment & lending mix
- Total income up 8%, reflecting 8% growth in NII and positive fair value movements benefitting non-interest income
- CIR stable at 51.9% in line with guidance; underlying costs of £971m 6% higher as gross savings offset by inflation and investment
- Underlying operating profit before impairments of £902m up 9% on FY22, reflecting positive jaws
- Credit impairment charge of £309m (42bps cost of risk) reflecting prudent macroeconomics and provision build from higher modelled ECL; credit quality remains robust with low arrears; provision coverage of 84bps significantly above pre-pandemic levels
- Adjusting items £67m higher YoY, primarily reflecting higher restructuring charges as anticipated, including 30% reduction in the store network, and an intangible asset write-down, given deferred implementation and redesign of the new mortgage platform
- Statutory profit decreased 42% YoY, reflecting higher impairments and adjusting items; statutory RoTE of 3.9% (2022: 10.3%)
- CET1 ratio remains strong at 14.7% (2022: 15.0%); announced further £150m buyback, above prior guidance, taking FY23 buybacks to £200m; 5.3p full-year dividend means total shareholder distributions of £272m for FY23, c.2% higher than FY22

### Driving continued growth in target lending segments and relationship deposits

- 5% growth in active relationship customer accounts during FY23 to 3.8m accounts
- Relationship deposits 2% higher in FY23 at £35.4bn, remaining 53% of total deposits; total deposits also increased 2% to £66.6bn
- Strong growth in target segments; Unsecured +5.8%, driven by growth in cards; Business lending +6.0% as growth in BAU balances offset a reduction in Government scheme lending; resilient performance in Mortgages (1.1)% leaving overall lending stable

### Strong strategic delivery for customers

- Re-launched Virgin Money Investments, including pensions; launched Digital Wallet to Virgin Atlantic customers with good take-up
- 18% YoY growth in business current account (BCA) sales; net growth in BCA accounts for 22 consecutive months
- Call waiting times down c.65% from peak following additional resource costs to support customer service
- Embedded Consumer Duty requirements; supporting customers through Mortgage Charter and our Cost of Living hub

### FY24 and medium-term outlook

- NIM of 190-195bps in FY24, supported by structural hedge re-investment, deposit mix & ongoing growth in target segments
- Continued loan growth in Unsecured & BAU Business, while maintaining mortgage market share in the medium term; volume growth and improving margin to drive income growth in medium term
- Underlying cost:income ratio(3) expected to remain broadly stable in FY24; continue to target less than 50% in medium term
- Expect cost of risk for FY24 to be in the range of 30-35bps, following strengthened provision coverage in FY23
- Now expect higher annualised gross cost savings of £200m (previously £175m); anticipate majority of remaining c.£60m restructuring charges in FY24
- Anticipate c.£40m investment in financial crime prevention in FY24 with c.£130m FY24-26 (excluded from underlying performance)
- CET1 to be in target 13-13.5% range in FY24 with total shareholder distributions in FY24 to be around FY23 nominal level(4); total shareholder distributions between FY22-24 now expected to be around £800m(4)
- Expect to deliver Underlying RoTE of c.10% in FY24(5) reflecting good business momentum with statutory RoTE of c.8%
- Committed to generating sustainable double-digit statutory returns in the medium term

(3) Excluding financial crime prevention programme from FY24 (4) Buybacks subject to Board and regulatory approval (5) Excluding financial crime prevention programme from FY24 and cash flow hedge reserve.

# Contact details

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Virgin Money UK PLC will today be hosting a presentation for analysts and investors covering the 2023 full year financial results starting at 08:30 GMT (19:30 AEDT) and this will be webcast live and is available at:

https://webcast.openbriefing.com/vmuk-fy23/

A recording of the webcast and conference call will be made available on our website shortly after the meeting at:

https://www.virginmoneyukplc.com/investor-relations/results-and-reporting/financial-results/

A call for fixed income investors will be held today at 14:00 GMT (01:00 AEDT on Friday 24th November 2023): Dial-in details: UK 0800 358 1035; Australia +61 1800 512 331; All other locations: +44 20 4587 0498; Access code: 944297

Announcement authorised for release by Lorna McMillian, Group Company Secretary.

LEI number: 213800ZK9VGCYYR6O495

# Delivering against our strategy

We made good progress executing our Purpose-led strategy in 2023 and are entering 2024 with good momentum in our key target segments across the business.

**David Duffy**
Chief Executive Officer

## We are delivering positive financial performance and strong capital distributions despite a challenging backdrop

**Dear stakeholder**

During the second year of our current strategic cycle, the Group has continued to execute well against our Purpose-led ambition to become the UK’s best digital bank.

2023 has been another year of significant change in the operating environment and I am pleased that we have continued to deliver against this backdrop. The combination of the higher rate environment and our strategy is increasingly translating into growth in relationship customer accounts and income. We’ve made good progress on our journey to digitise the Bank, and I would like to thank our colleagues for a significant year of execution.

There remains more to do as we enter the final year of our current 3-year plan, but we have good momentum across key areas of the business, a robust balance sheet, and a continued focus on ensuring we support and reward our customers’ ongoing loyalty. We will remain vigilant in safeguarding against new and emerging threats, and adapting accordingly, we are increasingly well placed to generate strong, sustainable returns. These will support shareholder distributions, investment in the business and our long-term growth ambitions.

**Strategic delivery in 2023**

Throughout the year, I have been pleased with our commercial momentum across the business. Our balance sheet strength helped us withstand the broader turbulence in the sector earlier in the year as we retained resilient liquidity, funding and capital positions.

Our refreshed digital products are delivering growth in balances across our target segments of Business, Unsecured and relationship deposits. Business, in particular, demonstrated good momentum across both sides of the balance sheet, with a second year of robust current account sales, and lending growth despite a weaker market backdrop. Within Unsecured, our cards business continued to drive good growth, increasing our market share steadily, while also focusing on long-term profitability against the higher rate backdrop. Relationship deposits grew in line with the overall deposit base at a time when many banks have seen significant deposit migration and attrition. Our early management of the trend for customers to seek higher yields, offering attractive products such as our linked savers, demonstrated how we can offer good value to customers while also delivering a more resilient margin outlook.

Earlier in the year the Group took action to invest in improving our service position, and we are seeing an improvement in the key customer satisfaction metrics, albeit we have more to do. As we reaccelerated our digitisation work in the second half of the year, we continued to deliver the gross savings outlined at FY21, mitigating the backdrop of inflationary pressure.

Continuing to build an efficient and sustainable platform to support long-term returns remains a key ambition. However, we must recognise the need to adapt to changes in the environment, including emerging threats and new technology. We have therefore decided to invest c.£130m over 3 years, as we deliver our response to the emerging risks and technologies, including AI, in the evolving financial and cybercrime space. Additional savings have been identified to offset this however, taking the original c.£175m target for cost savings to c.£200m, with no additional cost to achieve.

# Chief Executive Officer's introduction

The improving rate environment, combined with our commercial momentum, saw continued strong underlying capital generation to support the Group's ambitions. Our CET1 ratio remained robust throughout the period and we saw another strong set of results through our second BoE stress testing process.

The Board and I remain committed to continuing to deliver capital distributions for shareholders. We are recommending a 5.3p ordinary dividend for 2023, supplemented by our announcement today of a higher than guided £150m share buyback in respect of FY23, to be executed during H1 2024. This takes total shareholder returns announced for the year to £272m, in line with 2022 (£267m).

## Robust financial performance in 2023

The significantly higher rate environment, combined with our strategic execution in the year, resulted in underlying operating profit before impairment charges 9% higher than a year ago. However, statutory profit before tax of £345m was lower than 2022 (£595m), firstly given higher impairments relative to last year's low charge, which primarily reflected higher modelled provisions, and secondly, higher adjusting items due to ongoing restructuring activity and intangible asset writedowns (see CFO review for full details). Altogether, this resulted in a lower Statutory RoTE of 3.9% (2022: 10.3%), with a Statutory cost:income ratio of 64% (2022: 62%).

Underlying income increased 8% in the year, primarily driven by stronger net interest income (NII). NIM expanded again to 1.91% (2022: 1.85%), supported by a higher yield on our structural hedge, early management of deposit migration trends and growth in higher yielding lending. These developments have helped offset a continued competitive market for mortgages and an increasingly competitive market for deposits.

Underlying operating costs of £971m increased 6% on the prior year. We have continued to deliver against our cost reduction programme, with gross savings broadly offsetting additional costs from inflation and balance sheet growth. However, the additional costs to resolve service challenges and higher levels of investment drove the increase in total costs.

While our overall credit quality remains resilient, we saw a higher credit impairment charge this year, equivalent to a cost of risk of 42bps (2022: 7bps), as we incorporated a more conservative economic outlook and updated credit bureau data. This is reflected in our increased expected credit loss (ECL) provision, and coverage of 84bps, which is significantly higher compared to 62bps at FY22. The key driver of the increased credit provision is credit cards, reflecting a higher modelled view of future losses, given updated assumptions. This leaves the Bank well placed against any future credit deterioration.

Overall lending balances were stable at £72.8bn, despite a muted market backdrop. We achieved 9% growth across our target segments of Unsecured and business-as-usual (BAU) Business lending, while the mortgage book reduced 1%, as market demand slowed against the higher rate backdrop. Pleasingly given the competitive backdrop, deposit balances grew 2% to £66.6bn, with relationship deposits also 2% higher.

Our ongoing profitability supports a robust capital position, reflected in a CET1 ratio of 14.7% (2022: 15.0%) supporting further capital distributions. The liquidity coverage ratio (LCR) of 146% and loan to deposit ratio (LDR) of 109% also highlight the strength of our funding position and the robustness of our balance sheet.

## Responding to evolving technology

As the backdrop continues to evolve and new technologies emerge, the Group remains focused on safeguarding the Bank and our customers. We remain vigilant to the emerging expectations, threats and challenges we face, as well as rising stakeholder expectations.

The rapidly increasing prevalence of online channels and social media are driving higher instances of fraud and financial crime in the UK. Increasingly, this will become an area where banks bear the full extent of fraud losses and associated penalties. Cybercrime represents another area of significant development, with new technologies including AI increasing the sophistication and risk of attacks. Underpinning the defence against such attacks and broader reporting is strong data management, including adoption of the Basel Committee on Banking Supervision (BCBS) 239 data standard, and this will be an area of increased focus for us in the years ahead.

To maintain our vigilance against all forms of fraud and financial crime, we have decided to increase our digital investment in this area from FY24. We will implement new and improved technology and increase the sophistication of our processes, with the goal of providing our customers with upgraded protection against criminal actors.

As a result, we are announcing a c.£130m investment programme over the next three years, of which c.£40m will be spent in FY24. This investment will significantly upgrade our financial crime prevention and cyber defence capabilities, while also delivering increasingly rich data and analytical capabilities, including AI models, to underpin our risk data aggregation and internal risk reporting practices, in line with regulatory requirements.

This is the right thing to do for customers and the Bank in the long term, safeguarding and protecting both as the environment evolves, and will support sustainable shareholder returns over time. While the investment will impact on returns in the short term, we believe it mitigates against the risk of greater impact on the Bank and our customers in the future.

We will also seek to offset the higher costs incurred through additional cost saving initiatives. We are increasing the scope of our existing cost savings programme and are now targeting c.£200m of gross cost savings, up from c.£175m previously. These will be delivered primarily by further strategic rationalisation of our real estate portfolio, outsourcing and systems simplification. This will be delivered within the existing c.£275m restructuring budget set at FY21.

## Delivering against our strategic priorities

We continue to progress our strategic shift towards digital banking, as set out at FY21. This outlined a three-year programme of change and investment towards achieving our strategic ambition of becoming the UK's best digital bank. A summary of our progress against our four key strategic priorities during 2023 is below.

### Delighted Customers and Colleagues

We have made significant improvements in addressing the challenges faced earlier in the year around service. Call waiting times are on average 65% lower compared to their October 2022 peak, and after investing more in the first half, we have been able to reduce the numbers of third-party resources and additional colleagues employed to address the backlog of complaints. Having addressed these issues, over the second half of the year we have re-accelerated efforts to digitise and automate the business as planned.

As a result of these actions, the Group's Smile scores improved for the first time in three years, increasing to 49%. Complaints per 1,000 have reduced to 4.0, as we addressed complaint backlogs and improved processes.

While this investment drove a higher cost out-turn for 2023 than was initially expected, it was right we invested for both our customers and the long-term health of the business. However, we want to do more and remain focused on continuing to improve service levels.

Over the course of the year, we have fully implemented new regulatory requirements including Consumer Duty and the Mortgage Charter as well as supporting additional regulatory focus on the savings market. These new requirements are well aligned to our Purpose and how we conduct our business, meaning we were well placed to deliver them.

Given the current environment, we are also fully committed to supporting customers as they deal with higher living costs, including via our online cost of living hub.

We have made good progress in the development of our digital wallet and this has now been launched to our closed user group made up of Virgin Atlantic credit card users. This work will form the foundation of our all-encompassing integrated app for Virgin Money in 2024 and we are well placed to launch the first iteration of this through the next year.

For colleagues, our A Life More Virgin flexible working proposition continues to garner strong support, with colleague engagement scores rising to 80% (2022: 79%), validating our differentiated strategy. We are also advancing our Diversity, Equity and Inclusion work, seeing some improvement in our key metrics and launching our BRAVER initiative.

**Pioneering Growth**
We have made good progress in 2023 in our target segments, with total active relationship customer accounts increasing by 5% to 3.8m, driven mainly by credit card sales and new Business Current Account (BCA) customers.

I was particularly pleased with our 6% growth in business lending, despite the ongoing reduction in government lending scheme balances. Our Business bank has benefited from our sector specialisms at a time when the market has been muted and we remain well placed to continue to grow profitably.

We delivered 6% growth in unsecured lending, primarily driven by growth in credit cards including a strong performance in our VAA co-branded card. Taken together, we saw 9% growth across our target lending segments of BAU business and unsecured (2022: 7%).

In mortgages, our aim is to maintain our market share over time at around 3.5%. During the year, we traded well against lower market activity levels and strong competition. Given the tougher backdrop, we traded tactically and focused on maintaining margins, as balances reduced by 1%.

Our deposit performance throughout the year has been robust. Maintaining our relationship deposits as a share of deposit mix at 53% (2022: 53%) remains an important strategic focus. We attracted c.110k new Personal Current Account (PCA) sales in 2023 (2022: 131k) by leveraging our attractive linked savings propositions and reward offerings, rather than competing on up-front cash incentives. Our cashback offering also continues to see good utilisation with over 860k customers now enrolled (2022: c.650k).

In the Business bank, our award-winning BCA proposition and improved digital journeys have now driven 22 months of consecutive net customer account growth, via c.39k new BCA sales in 2023 (2022: c.33k).

During 2023, we also completed the build-out of our full product proposition with the launch of Virgin Money Investments. Since launch this has attracted new customers as we offer a Purpose-led, simple approach to investing.

**Super Straightforward Efficiency**
Since we announced our strategy at FY21, inflation has been higher and more enduring than expected, resulting in key costs across salaries, suppliers and change delivery moving significantly higher and providing a major cost headwind. In addition, the technological environment continues to evolve at pace, with new opportunities, threats and regulatory requirements, which we have needed to consider in our investment portfolio.

Digital primacy, which measures the proportion of active PCA and Card customers who are digital only in their engagement with the Bank, improved to 61% (2022: 56%). From a property perspective, the Group announced in H2 that it will be closing an additional 39 stores, as it adapts to changing customer demand, reducing our store network by 30% to 91 stores. The Group's property footprint is now at c.440k sq ft, against a target of c.300k sq ft by FY24, from our c.900k sq ft start point; a 51% reduction.

Having paused some restructuring activity to focus on supporting customer service during the first half of the year, we picked up the pace in the second half, and have now incurred £213m of the anticipated total c.£275m investment programme. We have made good progress, delivering £130m of annualised run rate savings and helping to offset cost pressures from inflation, growth and investment. These savings have been driven by ongoing digitisation, property and organisational changes, and sourcing benefits. Our work in H2 included digitising key customer journeys, which remains central to our strategy, and we have now fully automated 50% of key journeys (2022: 43%).

During the year, we also deployed our latest chatbot Redi across credit cards. This has been well received by customers, attracting favourable Smile scores and supporting a reduction in call volumes.

Following an assessment of the progress of the project to upgrade the mortgage platform and challenges identified during testing, we now anticipate a significant deferral and redesign as we implement the upgraded capability. We remain committed to launching improved capability for our mortgage customers and brokers over time, and there remains no impact on day-to-day trading.

Looking ahead, we believe that delivering greater efficiency will support sustainable value creation for shareholders, a lower cost:income ratio and will enhance our ability to compete effectively in a rapidly changing digital marketplace.

**Discipline and Sustainability**
Our focus has always been on ensuring that our Bank is delivering consistent, sustainable positive outcomes for our customers, investors and other stakeholders. Aligned to that, in 2023 we have been particularly focused on ensuring our resilience against the challenging external backdrop.

The Group has remained well positioned given our strong capital, high-quality customer base and robust asset quality. We maintained our disciplined approach to credit, achieving modest, profitable lending growth in our target areas, while ensuring the resilience of our funding and deposits. Our liquidity metrics remain well above regulatory minimums, and we have maintained good access to wholesale funding markets, all of which demonstrate our prudent approach and market confidence in our business model. We have also now repaid £1.0bn of TFSME funding, ahead of its contractual maturity.

The Group's resilient performance in the BoE's Annual Cyclical Scenario (ACS), remaining significantly in excess of its reference rates on both a transitional and non-transitional basis, demonstrates the sustainability of our franchise against even a severe macro downturn.

We've also made good progress on ESG metrics, maintaining our 'low risk' status from Sustainalytics and AA 'Leader' status from MSCI, evidencing the Group's enhanced disclosure and commitment to continual improvement of our sustainability agenda.

In 2023, the Group has further developed its Commercial net zero targets and road maps, as well as setting targets in relation to its own operations for the first time.

**Leadership changes**
I have further strengthened the Group's Executive Leadership Team this year, ensuring we have the required digital leadership capabilities to deliver now and in the future, against the higher expectations of a tier 1 bank.

As announced last year, Sarah Wilkinson joined the Group as Chief Operating Officer in early 2023, bringing together the Group's Customer Experience and Digital & Innovation functions under new, focused leadership. In late 2023 we appointed Allegra Patrizi as Managing Director, Business and Commercial. Allegra has worked in the financial services sector for over 20 years having started her career at McKinsey & Company where she rose to Partner, before being Chief Product Officer at F&C Asset Management, Group Risk Director at Prudential plc and most recently CEO of Aegon in the Netherlands. Hugh Chater will remain with us as a senior adviser until the end of 2024, and I thank him for all his hard work and leadership over the last seven years.

**Outlook**
The Group's underlying momentum is strong. NIM has continued to expand in FY23, and we expect a NIM of 190-195bps in FY24. This will be supported by re-investment of the structural hedge at higher rates and further growth in higher margin lending, where we expect to grow our business and unsecured segments between 5% and 10%.

We will continue to invest in strengthening our business for all stakeholders, including the digital investment in financial crime prevention and as we focus on improving legacy components of our infrastructure. We will improve digital customer experience further, deliver the second phase of Consumer Duty and launch new digital propositions, while delivering against our expanded, £200m gross cost saving programme. We now anticipate that the underlying cost:income ratio in FY24 will be broadly stable on this financial year, excluding our investment in financial crime prevention.

Having updated our economic outlook under the IFRS 9 methodology, we feel well provided, and expect our cost of risk for the year to be in the range of 30-35bps, subject to the macroeconomic outlook remaining consistent.

The Group remains strongly capital generative and I'm pleased to confirm that, as previously announced, we plan further buybacks through 2024, subject to Board and regulatory approval, following on from £150m today, as we return to operating within our target CET1 range of 13% – 13.5% by FY24. We expect nominal shareholder distributions in FY24 to be in line with FY23; delivering this would mean we have returned around £800m of capital distributions to shareholders over the three years of our strategy.

As a result of the increased level of investment in the financial crime prevention programme, we do now expect to take longer to achieve our double digit statutory return ambition. We expect to generate an underlying RoTE of c.10% in FY24, excluding the financial crime prevention programme and cash flow hedge reserve, with a statutory RoTE of c.8%. We are committed to generating double digit returns in the medium-term and I look forward to communicating more details about the next phase of our strategy at a Capital Markets Day next year.

In the meantime I would like to thank all our colleagues for their hard work, and our customers for their loyalty and support as we continue to execute our strategy and deliver on our Purpose of Making you happier about money. I look forward to updating the market on our further progress during 2024.

**David Duffy**
Chief Executive Officer
22 November 2023

# Resilient performance despite a challenging operating environment

We’ve delivered a strong operating performance in FY23 and enter FY24 with good business momentum. We’re investing to safeguard the bank and customers, supporting sustainable returns over time.

**Clifford Abrahams**
Chief Financial Officer

## 2023 was an important year as we demonstrated momentum in strategic delivery and profitable growth, while maintaining a robust balance sheet, funding and capital position

### Review of the year

The Group performed resiliently this year, with solid financial momentum and further strategic delivery. During the year, the Group made further improvements to customer propositions, supporting a 5% growth in total active relationship customer accounts to 3.8m customers. Operating profit improved relative to 2022, supported by the combination of the higher rate environment and growth in targeted lending and deposits. Alongside this, an increased credit impairment charge and higher adjusting items relative to last year resulted in lower statutory profit and a statutory RoTE of 3.9%, down from 10.3% in FY22. Capital remained strong during the period, with CET1 at 14.7% (2022: 15.0%), supporting total returns to shareholders of £272m, including a full year dividend of 5.3p and the announcement of a total of £200m of share buybacks for FY23.

We were pleased to deliver lending growth in our target areas during the year, while overall customer lending was stable at £72.8bn. Mortgage balances reduced 1.1% during the period to £57.5bn, as the higher rate environment and wider cost of living pressures tempered purchase activity. Business lending increased 6% overall, as growth in BAU balances offset ongoing reductions in government-backed lending. Unsecured balances continued to perform strongly, growing 6% during the year to £6.5bn. This year, we reduced the pace of growth in Unsecured lending relative to 2022, reflecting a disciplined approach to profitability. We continued to attract new deposits during the year, despite a competitive backdrop, supporting overall deposit growth of 1.9%.

The Group maintained a conservative balance sheet position, including strengthened provision coverage and robust funding and liquidity. Credit provisions of £617m (2022: £457m) are equivalent to a coverage ratio of 0.84% (2022: 0.62%). Funding and liquidity remain strong, with the 12-month average LCR ratio increasing to 146% (2022: 140%) and 12-month average NSFR stable at 136% (2022: 134%).

Underlying profit before tax in 2023 was £593m, a reduction compared to last year (2022: £776m), as higher operating income was more than offset by a higher level of impairments compared to last year’s low charge. NIM of 1.91% (2022: 1.85%) improved year-on-year, given the higher rate environment and strategic execution, supporting growth in underlying income of 8% relative to 2022. Underlying costs were 6% higher compared to 2022 as gross cost savings from the restructuring programme helped to mitigate inflation, but with higher investment and temporary customer service related costs. Taken together, this resulted in a stable underlying cost:income ratio of 52% (2022: 52%). Credit impairments of £309m (2022: £52m) were significantly higher year-on-year, mainly reflecting higher modelled expected credit loss (ECL) given updated macroeconomic assumptions and bureau data, in anticipation of a continued increase in arrears, resulting in an increased level of provision coverage overall.

## Financial highlights

| Statutory profit before tax | Underlying profit before tax | Statutory RoTE |
|---|---|---|
| £345m | £593m | 3.9% |
| 2022: £595m | 2022 (restated)[(1)]: £776m | 2022: 10.3% |
| **NIM** | **Underlying cost: income ratio** | **Cost of risk** |
| 1.91% | 51.9% | 42bps |
| 2022: 1.85% | 2022: 52.5% | 2022: 7bps |
| **CET1 ratio** | **Capital distributions announced** | **Dividend per share** |
| 14.7% | £272m | 5.3p |
| 2022: 15.0% | 2022: £267m | 2022: 10p |
| **LCR (12-month average)** | **NSFR (12-month average)** | **Relationship deposit growth** |
| 146% | 136% | +2% |
| 2022: 140% | 2022: 134% | 2022: +13% |

(1) Hedge ineffectiveness is now presented as an adjustment to underlying earnings as detailed on page 133. The comparative period has been adjusted accordingly. This restatement does not impact the statutory results of the Group.

The Group continues to expect to return to its target CET1 range of 13 – 13.5% in FY24, as capital generation through profitable growth supports ongoing shareholder distributions, growth and investment back into the business. The £150m share buyback announced at FY23, which adds to the £50m share buyback announced in August, will be deducted from CET1 in Q1 2024.

Looking ahead, we will be undertaking a new three year investment programme, expected to cost c.£130m. This investment will improve our financial crime prevention capabilities, as well as supporting the enhanced data quality work required of tier 1 banks. While this delays delivery of our previously announced FY24 targets, it is critical we adapt to the fast-evolving environment in order to safeguard the Bank and our customers further.

I am confident that the Group is well positioned to navigate the current economic backdrop with good financial momentum, including a strong margin, targeted growth, and a robust balance sheet. We remain focused on investing to digitise the Bank in the near term, which will drive further cost efficiency and improved customer experience, while also investing to improve our overall resilience across the medium term. The combination of these factors will support improved shareholder returns over the coming periods and delivery of our commitment to distribute surplus capital in line with our capital framework.

## Underlying income

| | 2023 £m | Restated 2022 £m | Change |
|---|---|---|---|
| Underlying net interest income | **1,716** | 1,592 | 8% |
| Underlying non-interest income[1] | **157** | 150 | 5% |
| **Total underlying operating income** | **1,873** | 1,742 | 8% |
| NIM | **1.91%** | 1.85% | 6bps |
| Average interest-earning assets | **89,810** | 86,275 | 4% |

(1) Hedge ineffectiveness is now presented as an adjustment to underlying non-interest income as detailed on page 133. The comparative period has been adjusted accordingly. This restatement does not impact the statutory results of the Group.

### NII and NIM

Net interest income (NII) increased by £124m or 8% relative to 2022, driven by an expansion of the Group's NIM as it continued to benefit from higher rates, including from the reinvestment of the structural hedge.

Asset yields increased 171bps compared to 2022, reflecting the rising interest rate environment throughout the year. Average mortgage lending was broadly stable during the period, reflecting weaker market demand in light of higher rates and lower new purchase activity. Customer rates for new and retained mortgages increased as a function of the base rate environment, though spreads remained tighter reflecting continued strong competition. Taken together, the average mortgage yield increased by 46bps, supporting higher mortgage interest income. In Business, interest income increased by £251m in the year, driven by higher average balances, while the yield of the book also improved, given the rate environment and a reduced proportion of lower-yielding government-backed lending. In Unsecured, interest income increased by £67m in the year, driven by growth in average balances, owing mainly to growth in the credit card book. Elsewhere, the average yield on the Group's liquid assets increased 321bps reflecting the higher rate environment across the financial year.

The balance of the Group's structural hedge reduced in the second half of the year from c.£32.0bn to c.£29.5bn, reflecting the impact of deposit migration from behaviourally stable deposits. During the year, the Group generated £401m of total gross interest income from the structural hedge, including the legacy hedge contribution, benefiting from ongoing hedge reinvestment at higher prevailing rates.

Liability rates on average interest bearing liabilities increased 185bps relative to 2022. During the year, the Group continued with its strategy to grow relationship deposits, and these balances grew by 2%. This was despite the impact of the higher rate environment, which drove increased levels of deposit migration from current accounts across the industry. The Group also participated in the market for term funding during the year, offsetting migration from non-linked variable savings balances. Wholesale funding costs increased in the year, driven by higher average balances, change in mix following issuance throughout the year, and higher rates corresponding to the rate environment.

### Non-interest income

Non-interest income of £157m was 5% higher when compared with 2022 and 7% lower when excluding fair value movements. Mortgage fee income was broadly stable during the period, while Unsecured fee income was modestly lower in the second half of the year, reflecting changes to packaged accounts and reduced associated fees, aligned with Consumer Duty regulations. Business fee income was lower relative to 2022, following the strategic decision by the Group to change its payments partner and expand its relationship with Global Payments, resulting in an initial reduction of merchant services income.

| Average balance sheet | 2023 Average balance £m | 2023 Interest income/ (expense) £m | 2023 Average yield/(rate) % | 2022 Average balance £m | 2022 Interest income/ (expense) £m | 2022 Average yield/(rate) % |
|---|---|---|---|---|---|---|
| **Interest earning assets** | | | | | | |
| Mortgages | **57,980** | **1,537** | **2.65** | 57,996 | 1,272 | 2.19 |
| Unsecured lending | **6,547** | **474** | **7.24** | 6,100 | 407 | 6.67 |
| Business lending[1] | **8,496** | **582** | **6.85** | 8,263 | 331 | 4.00 |
| Liquid assets | **16,000** | **657** | **4.11** | 13,059 | 117 | 0.90 |
| Due from other banks | **782** | **13** | **1.67** | 853 | 2 | 0.22 |
| Swap income/other | **–** | **600** | **n/a** | – | 104 | n/a |
| Other interest earning assets | **5** | **–** | **n/a** | 4 | – | n/a |
| **Total average interest earning assets** | **89,810** | **3,863** | **4.30** | 86,275 | 2,233 | 2.59 |
| **Total average non-interest earning assets** | **2,378** | | | 3,229 | | |
| **Total average assets** | **92,188** | | | 89,504 | | |
| **Interest bearing liabilities** | | | | | | |
| Current accounts | **15,739** | **(203)** | **(1.29)** | 15,829 | (46) | (0.29) |
| Savings accounts | **26,005** | **(433)** | **(1.67)** | 30,895 | (147) | (0.48) |
| Term deposits | **19,603** | **(597)** | **(3.05)** | 12,894 | (149) | (1.16) |
| Wholesale funding | **18,321** | **(909)** | **(4.96)** | 16,169 | (296) | (1.83) |
| Other interest bearing liabilities | **170** | **(5)** | **n/a** | 145 | (3) | n/a |
| **Total average interest bearing liabilities** | **79,838** | **(2,147)** | **(2.69)** | 75,932 | (641) | (0.84) |
| **Total average non-interest bearing liabilities** | **6,531** | | | 7,903 | | |
| **Total average liabilities** | **86,369** | | | 83,835 | | |
| **Total average equity** | **5,819** | | | 5,669 | | |
| **Total average liabilities and average equity** | **92,188** | | | 89,504 | | |
| **Net interest income** | | **1,716** | **1.91** | | 1,592 | 1.85 |

(1) Includes loans designated at fair value through profit or loss (FVTPL).

## Underlying costs

| For the year ended 30 September | 2023 £m | 2022 £m | Change |
|---|---|---|---|
| Staff costs | **367** | 375 | (2)% |
| Property and infrastructure | **40** | 42 | (5)% |
| Technology and communications | **126** | 116 | 9% |
| Corporate and professional services | **173** | 114 | 51% |
| Depreciation, amortisation and impairment | **95** | 116 | (18)% |
| Other expenses | **170** | 151 | 12% |
| **Total underlying operating and administrative expenses** | **971** | 914 | 6% |
| Underlying cost: income ratio | **51.9%** | 52.5% | (0.6)%pts |

Underlying operating expenses increased 6% year-on-year to £971m, while the cost:income ratio remained stable at 52%. During the year, the Group's restructuring activity delivered further cost-efficiencies, taking the total annualised gross savings since FY21 to £130m. Relative to last year, the Group also benefited from a c.£25m higher net pension benefit, and a lower depreciation charge following past changes to depreciation and amortisation practices. These benefits were offset, mainly by higher staff costs (net of the pension benefit), given wage inflation and higher corporate and professional services fees, mainly reflecting additional resource to support the improvement of customer service levels, and additional regulatory related investment.

## Impairments

| As at 30 September 2023 | Credit provisions £m | Gross lending £bn | Coverage ratio bps | Net cost of risk bps | % of loans in Stage 2 | % of loans in Stage 3 |
|---|---|---|---|---|---|---|
| Mortgages | **57** | **57.8** | **10** | **-** | **4.7** | **1.0** |
| Unsecured: | **429** | **6.8** | **665** | **430** | **24.1** | **1.7** |
| of which credit cards | **392** | **6.1** | **688** | **483** | **21.7** | **1.8** |
| of which personal loans and overdrafts | **37** | **0.7** | **488** | **86** | **44.3** | **0.9** |
| Business | **131** | **8.7** | **160**(1) | **44** | **22.8** | **4.7** |
| **Total** | **617** | **73.3** | **84** | **42** | **8.6** | **1.5** |
| of which Stage 2 | **400** | **6.3** | **633** | | | |
| of which Stage 3 | **128** | **1.1** | **1,393** | | | |

(1) Government-guaranteed element of loan balances excluded for the purpose of calculating the Business and total coverage ratio.

| As at 30 September 2022 | Credit provisions £m | Gross lending £bn | Coverage ratio bps | Net cost of risk bps | % of loans in Stage 2 | % of loans in Stage 3 |
|---|---|---|---|---|---|---|
| Mortgages | 56 | 58.5 | 9 | (5) | 5.3 | 1.0 |
| Unsecured: | 284 | 6.5 | 466 | 322 | 17.3 | 1.2 |
| of which credit cards | 246 | 5.5 | 481 | 347 | 13.9 | 1.3 |
| of which personal loans and overdrafts | 38 | 1.0 | 388 | 161 | 34.9 | 0.9 |
| Business | 117 | 8.1 | 159(1) | (112) | 18.7 | 4.6 |
| Total | 457 | 73.1 | 62 | 7 | 7.8 | 1.4 |
| of which Stage 2 | 268 | 5.7 | 472 | | | |
| of which Stage 3 | 104 | 1.0 | 1,124 | | | |

(1) Government-guaranteed element of loan balances excluded for the purpose of calculating the Business and total coverage ratio.

ECL provisions increased to £617m at FY23 (2022: £457m), resulting in higher aggregate provision coverage of 84bps (2022: 62bps). This was mainly due to higher modelled ECL, particularly in credit cards, in anticipation of a continued increase in arrears and reflecting revised macroeconomic assumptions and credit bureau data. The updated economic outlook forecasts a slower recovery in the outer years compared to September 2022, whilst updated credit bureau data was also weaker.

Accordingly, the modelled and individually assessed (IA) ECL increased by £168m to £540m (2022: £372m), while Management Adjustments (MAs) reduced to £76m (2022: £85m). The combination of these factors resulted in a £309m impairment charge during the period (2022: £52m), equivalent to a cost of risk of 42bps (2022: 7bps).

The key macroeconomic assumptions used in the Group's IFRS 9 modelling were updated based on scenarios provided by our third party provider Oxford Economics. The weightings applied to the scenarios were unchanged from FY22 and included 10% to the Upside scenario, 55% to the Base scenario and 35% to the Downside scenario. The weighted macroeconomic scenario includes a 0.6% contraction in GDP in 2024, peak unemployment of 5.1% in 2025 and a decline in the House Price Index (HPI) across 2023-2025.

To supplement the modelled ECL provision, the Group applied expert credit risk judgement through MAs, designed to account for factors that the models do not incorporate. Through this process, the Group applied MAs of £76m (2022: £85m). These include cost of living MAs of £15m (2022: £57m), which were lower in the year given these impacts are now better reflected in the modelled ECL outcome. During the period, the new Loss Given Default (LGD) model in Business lending was fully implemented, resulting in the removal of a negative MA (£(15)m) that was held at 2022, given it is now reflected in the modelled output. There was also an increase in Unsecured MAs, relating to a revised debt sale agreement.

During the year, loans classified as Stage 2 increased from 8% of the portfolio at FY22 to 9%. 96% of stage 2 balances remain <30 days past due (DPD). Stage 3 assets as a percentage of Group lending remained broadly stable at 1.5% (2022: 1.4%). The Group's credit provisioning assumes that arrears continue to increase over the next financial year.

Across all portfolios, the Group has provision coverage that remains above pre-pandemic levels. In Mortgages, the coverage ratio of 10bps is considered appropriate. The portfolio continues to evidence good underlying credit performance, with no significant deterioration in asset quality, despite a marginal increase in late-stage arrears.

Unsecured lending book coverage ratio of 665bps encompasses both the 688bps of coverage for our credit card portfolio, and 488bps of coverage for our smaller personal loans and overdrafts book. In addition to the impact of current macroeconomics, the modelled provision increased due to a weakening of credit bureau data, and higher early-stage arrears compared with prior years. Overall arrears levels remain modest across the portfolio with 97% of balances not past due (2022: 98%).

In Business, the coverage ratio of 160bps is stable relative to FY22. There has been a limited change in underlying asset quality performance and, as yet, no significant increase in specific provision recognition. The lending book continues to be biased away from sectors likely to experience more disruption from higher inflation such as hospitality and retail, towards sectors expected to be resilient, such as agriculture, health and social care.

### Adjusting items and statutory profit

| | 2023 £m | Restated 2022 £m |
|---|---|---|
| **Underlying profit on ordinary activities before tax** | **593** | 776 |
| Adjusting items | | |
| – Restructuring charges | **(131)** | (82) |
| – Acquisition accounting unwinds | **(29)** | (35) |
| – Legacy conduct costs | **(12)** | (8) |
| – Hedge ineffectiveness(1) | **(16)** | 13 |
| – Other items | **(60)** | (69) |
| **Statutory profit on ordinary activities before tax** | **345** | 595 |
| Tax expense | **(99)** | (58) |
| **Statutory profit for the year** | **246** | 537 |
| Underlying RoTE | **7.6%** | 13.3% |
| Statutory RoTE | **3.9%** | 10.3% |
| TNAV per share | **359.8p** | 383.0p |

(1) Hedge ineffectiveness is now presented as an adjustment to underlying as detailed on page 133. The comparative period has been adjusted accordingly. This restatement does not impact the statutory results of the Group.

**Overview**
The Group made a statutory profit before tax of £345m (2022: £595m) after deducting £248m of adjusting items (2022: £181m).

TNAV per share reduced 23.2p in 2023 to 359.8p. The key drivers of the reduction were -14.4p of negative cash flow hedge reserve movements in the year, given rate changes and -25.2p from a lower pension surplus, offsetting +9.8p from retained earnings and +8.4p from share buybacks during the year.

**Restructuring charges**
Restructuring charges totalled £131m in the year, driven by charges related to the Group's digital investment. This included c.£58m for the delivery of IT changes and c.£73m for the closure of stores, changes to the operating model and lower property footprint. The Group continues to expect to incur a total of c.£275m of restructuring costs to implement its digital strategy across FY22-24; after spending £213m to date, the majority of the remaining costs are expected to be incurred in FY24.

**Acquisition accounting unwinds**
The Group recognised fair value accounting adjustments at the time of the Virgin Money acquisition that unwind through the income statement over the remaining life of the related assets and liabilities. The £29m charge during the year included an £8m accelerated charge related to mortgage balances which were in their promotional period on the date of acquisition but have now expired. There are now c.£15m of IFRS 3 balances remaining, which are expected to materially unwind in 2024.

**Legacy conduct**
Charges of £12m were incurred relating to legal proceedings and legacy claims arising in the ordinary course of the Group's business.

**Hedge ineffectiveness**
Hedge ineffectiveness largely represents timing differences that will reverse out over the lives of derivatives that are used in economic hedges but can result in volatility between reporting periods. Charges of £16m were incurred in respect of hedge ineffectiveness and rate volatility in the period.

**Other items**
Other items includes a c.£45m intangible write-off recognised in the year in relation to the Group's mortgage digitisation programme. This follows challenges identified during testing, resulting in a significant deferral and redesign as we implement the upgraded capability.

**Taxation**
There was a £99m tax charge in respect of £345m of statutory profit before tax, reflecting an effective tax rate of 29%.

## Balance sheet

| As at 30 September | 2023 | 2022 | Change |
|---|---|---|---|
| Mortgages | **57,497** | 58,155 | (1.1)% |
| Unsecured | **6,519** | 6,163 | 5.8% |
| Business[(1)] | **8,738** | 8,247 | 6.0% |
| **Total customer lending** | **72,754** | 72,565 | 0.3% |
| | | | |
| Relationship deposits[(2)] | **35,394** | 34,649 | 2.2% |
| Non-linked savings | **9,741** | 17,048 | (42.9)% |
| Term deposits | **21,474** | 13,663 | 57.2% |
| **Total customer deposits** | **66,609** | 65,360 | 1.9% |
| | | | |
| Wholesale funding | **16,658** | 17,012 | (2.1)% |
| of which TFSME | **6,200** | 7,200 | (13.9)% |
| Loan to deposit ratio (LDR) | **109%** | 111% | (2)%pts |
| Liquidity coverage ratio (LCR) (12-month average) | **146%** | 140% | 6%pts |

(1) Of which, £625m government lending (2022: £963m).
(2) Current account and linked savings balances.

**Customer lending and deposits**
At an aggregate level, Group lending was broadly stable at £72.8bn, as growth in Business and Unsecured lending offset a reduction in Mortgages. Total customer deposits increased by 1.9% to £66.6bn.

Mortgage balances reduced 1.1% to £57.5bn, with reduced demand reflecting slower market activity and demand, owing to the higher rate environment, affordability pressures and wider cost of living considerations. Against this subdued market backdrop, the Group traded to preserve profitability, although competition remained intense resulting in completion spreads remaining below book spreads during the financial year.

Business lending increased overall by 6.0% during the year to £8.7bn, driven by growth in non-government scheme lending, which increased by 11.4% to £8.1bn. This performance was supported by the strength of our franchise and sector specialisms in our target market segments. Government-scheme balances declined 35.1% to £0.6bn as expected, as borrowers made contractual repayments.

Unsecured lending increased 5.8% in the year, driven mainly by credit card growth. This performance was supported by resilient demand from existing customers and ongoing new credit card sales as the Group maintained its c.8% market share of balances. During the year, the Group observed customer behavioural activity outperforming assumptions, resulting in the card EIR asset performing better than expected. Personal loans and overdraft balances reduced £0.2bn during the year to £0.7bn, in line with expectations.

Customer deposits increased by £1.2bn or 1.9% during the financial year to £66.6bn. The Group continued to execute against its strategy and optimise its mix of deposits during the period, as relationship deposits grew by £0.7bn, supported by strong customer propositions and competitive rates. The Group actively increased its participation in the term deposit market early in the year to offset deposit migration. Term deposits increased by £7.8bn and were acquired at attractive spreads, locking in term funding at pricing below swaps. Non-linked saving balances reduced by £7.3bn during the period, given higher attrition and churn from the back book and as the Group prioritised the good value opportunities initially available in the term deposit market.

**Wholesale funding and liquidity**
During the period, the Group's LDR reduced to 109% (2022: 111%). The Group has a stable funding base with customer deposits representing c.80% of total funding. The Group's customer deposits are weighted towards retail customers (75%), with the balance being from business customers, predominantly small and medium sized enterprises. Of the total customer deposit book, 72% is insured via the Financial Services Compensation Scheme. Of balances that are uninsured, a proportion are fixed term and/or would incur a charge if customers wanted to withdraw their money.

The Group has a number of well-established wholesale funding programmes and proven markets access. During the year, the Group successfully issued €500m and £300m of MREL senior notes and c.£1.8bn of RMBS and covered bonds, while at the same time repaying £1.0bn of its TFSME drawings (£6.2bn outstanding as at 30 September 2023). On an overall basis, wholesale funding reduced from £17.0bn at FY22 to £16.7bn as at FY23. Of our total debt securities in issue, only 19% (£1.9bn) has less than one year to effective maturity, reflecting term issuance roll-downs (the Group has negligible short-term wholesale funding). The Group has £0.3bn of TFSME maturing in FY24, £2.5bn maturing in FY25, and £2.5bn maturing in FY26, with the remaining £0.9bn subject to term extension beyond FY26. The Group plans to continue to repay TFSME well ahead of contractual maturity to reduce the refinancing risk further.

The stability of the Group’s funding sources is highlighted in its NSFR ratio, which remained stable on a 12-month average basis at 136%. The Group’s 12-month average LCR increased 6% points to 146% (2022: 140%), continuing to comfortably exceed both regulatory requirements and the Group’s more prudent internal risk appetite metrics. The Group’s c.£14bn prime liquid asset portfolio is primarily comprised of cash at the BoE (c.65%), UK Government securities (Gilts) (c.10%) and AAA rated listed securities (e.g. bonds issued by supra-nationals and corporate covered bonds) (c.25%). The liquid asset portfolio is fully hedged from an interest rate, inflation and FX risk perspective and any movements in fair value are recognised in CET1 via the Income Statement or FVOCI reserve.

The Group also has unencumbered pre-positioned collateral at the BoE representing c.£6.9bn of secondary liquidity drawing capacity via the Bank’s Sterling Monetary Framework, which does not form part of the liquid asset portfolio for LCR or internal stressed outflow purposes. This has increased from c.£4.3bn at FY19 and over time, the stock of unencumbered pre-positioned collateral will increase as remaining TFSME drawings are repaid. In addition, the Group has a further c.£18.4bn of unencumbered assets eligible and readily available but not currently pre-positioned at the BoE.

## Capital

| | 2023 | 2022 | Change |
|---|---|---|---|
| CET1 ratio (IFRS 9 transitional) | **14.7%** | 15.0% | (0.3)%pts |
| CET1 ratio (IFRS 9 fully loaded) | **14.3%** | 14.6% | (0.3)%pts |
| Total capital ratio | **21.2%** | 22.0% | (0.8)%pts |
| MREL ratio | **31.9%** | 32.1% | (0.2)%pts |
| UK leverage ratio[(1)] | **5.0%** | 5.0% | –%pts |
| RWAs (£m) | **25,176** | 24,148 | 4.3% |
| of which Mortgages (£m) | **9,072** | 9,155 | (0.9)% |
| of which Unsecured (£m) | **4,819** | 4,817 | –% |
| of which Business (£m) | **6,990** | 6,196 | 12.8% |

Unless where stated, data in the table shows the capital position on a Capital Requirements Directive (CRD) IV ‘fully loaded’ basis with International Financial Reporting Standard (IFRS) 9 transitional adjustments applied.

(1) The prior year leverage ratio has been restated from 5.1% following an adjustment to exclude encumbered note cover and payments system collateral balances.

### Overview

The Group maintained a robust capital position with a CET1 ratio of 14.7% and a total capital ratio of 21.2% (IFRS 9 transitional basis). The Group’s CET1 ratio on an IFRS 9 fully loaded basis was 14.3%. The Group’s latest Pillar 2A requirement has a CET1 element of 1.7%. Overall, the Group continues to maintain a significant surplus above its CRD IV CET1 capital requirement, inclusive of the combined capital buffer (or MDA threshold) of 10.7%.

### CET1 capital

The Group’s transitional CET1 ratio reduced by 30bps over the year. Total underlying capital generation of 145bps was driven by 199bps of underlying profit, offset by 38bps from higher RWAs (including the anticipated impact of implementing mortgage hybrid models) and 16bps of AT1 distributions and related costs. Adjusting items consumed c.60bps while there was 29bps of accrual for expected dividends and 41bps from £100m of share buybacks executed during the period. Dividends of c.£72m relating to FY23 resulted in a payout level of 37%. This is higher than the Group’s 30% payout level in its dividend policy, reflecting a one-off adjustment in FY23 for certain non-cash adjusting items. The announcement of an additional £150m share buyback will reduce CET1 resources in Q1 2024

### RWAs

Overall, RWAs increased by c.4% during 2023 to £25.2bn. In Mortgages, RWAs reduced by £0.1bn as the impact of lower exposures and stronger HPI more than offset a c.£0.4bn post model adjustment for the expected impact of implementing mortgage hybrid models. In Business, RWAs increased by £0.8bn mainly as a result of higher customer balances, excluding government-backed balances that carry a 0% risk weight. Unsecured RWAs were broadly stable in the period, despite the increase in customer lending during the financial year, due to higher provisions reducing the EAD for the cards portfolio. Non-credit RWAs were £3.3bn, c.£0.2bn higher than 2022, driven by higher operational risk RWAs.

### MREL

The Group’s transitional MREL ratio remained broadly stable during the period at 9.3% (2022: 9.0%) of Leverage Exposures, or 31.9% when expressed as a percentage of RWAs (2022: 32.1%). This provides prudent headroom of £1.3bn or 1.5% above the binding loss-absorbing capacity (LAC) requirement of 7.8% of Leverage Exposures, or 5.3% above the binding LAC requirement of 26.6% when expressed as a percentage of RWAs.

| CET1 capital movements[1] | 2023 |
|---|---|
| **Opening CET1 ratio** | **15.0%** |
| Capital generated (bps) | **199** |
| RWA growth (bps) | **(38)** |
| AT1 distributions (bps) | **(16)** |
| **Underlying capital generated (bps)** | **145** |
| Restructuring charges (bps) | **(40)** |
| Acquisition accounting unwind (bps) | **(9)** |
| Conduct (bps) | **(4)** |
| Hedge ineffectiveness (bps) | **(5)** |
| Hybrid mortgage impact (bps) | **(28)** |
| Foreseeable ordinary dividends (bps) | **(29)** |
| Share buyback (bps) | **(41)** |
| Other (bps) | **(19)** |
| Net capital absorbed (bps) | **(30)** |
| **Closing CET1 ratio** | **14.7%** |

(1) This table shows the capital position on a CRD IV 'fully loaded' basis with IFRS 9 transitional adjustments applied.

### FY24 outlook

In FY24, we anticipate full year NIM of 190-195bps, reflecting the benefit of structural hedge reinvestment and a higher yielding asset mix, offset by ongoing competitive pricing pressures in mortgages and deposits.

The Group continues to expect to incur restructuring charges reflecting its ongoing digitisation programme, with the majority of the remaining c.£60m expected to be incurred in FY24. We now expect our strategy to digitise the Bank to deliver around £200m (previously c.£175m) of annualised gross cost savings, generating headroom to absorb inflation and reinvestment, as we focus on improving legacy components of our infrastructure. The Group will also invest c.£130m across FY24-26 in its financial crime prevention programme, of which c.£40m is expected to be incurred in FY24.

The Group now expects to deliver a broadly stable underlying cost: income ratio in FY24. This excludes the additional costs associated with the financial crime prevention programme in FY24, which will be excluded from underlying performance and reported separately as a notable item. The Group expects its cost of risk for FY24 to normalise around its through the cycle average of c.30-35bps.

Consistent with our strategy to diversify the balance sheet, we anticipate 5-10% growth in target lending segments of Unsecured and Business relative to FY23 and to trade tactically in the mortgage market to maintain market share across the medium term.

The Group expects to issue £1.5bn-2.0bn of secured issuance in FY24 subject to deposit flows and relative cost. Capital and MREL issuance is expected to be broadly limited to maintaining the current surplus to regulatory requirements.

By FY24, the Group expects to be operating in its target CET1 range of 13-13.5%. The Group anticipates nominal shareholder distributions in FY24 around the same level as FY23, comprising a target 30% full year dividend payout level, supplemented with buybacks, which will be subject to Board and regulatory approval, reflecting an ongoing assessment of surplus capital, regulatory developments, market conditions and the macroeconomic outlook.

Overall, the Group now expects to deliver a c.10% underlying RoTE in FY24, excluding costs associated with the financial crime prevention programme and the cash flow hedge reserve. The Group expects to deliver a c.8% statutory RoTE in FY24.

### Medium-term outlook

In the medium term the Group's digital acceleration will support the delivery of valuable and differentiated propositions to drive profitable growth. The Group will continue to target diversification on both sides of the balance sheet, delivering growth in Unsecured and Business lending, while maintaining our mortgage market share.

The Group continues to target an underlying cost:income ratio of <50%, while we are committed to delivering sustainable double-digit statutory returns in the medium-term, with further detail to be provided at a Capital Markets Day during FY24.

**Clifford Abrahams**
Chief Financial Officer
22 November 2023

## Guidance

| FY24 outlook | Medium-term outlook |
|---|---|
| **NIM**<br>FY24 NIM of 190-195bps | **Income**<br>Volume growth and improving margin to drive expansion |
| **Underlying costs**<br>Cost:income to remain broadly stable in FY24[(1)] | **Underlying costs**<br>Cost:income ratio to reduce below 50% |
| **Cost of risk**<br>Cost of risk to be in the range of 30-35bps | **Growth**<br>Targeting lending growth in Unsecured and Business; maintaining mortgage market share over medium term |
| **Investment**<br>c.£275m across FY22-24; majority of remaining c.£60m to be incurred in FY24<br>Expect to spend c.£40m in financial crime prevention programme in FY24 | **Investment**<br>Expect to spend c.£130m in financial crime prevention programme between FY24-26 |
| **CET 1**<br>CET1 in target range of 13–13.5% | **CET 1**<br>Remain in target CET1 range |
| **Capital distribution**<br>FY24 distributions around FY23 nominal level; dividends (30% payout); buybacks subject to Board and regulatory approval | **RoTE**<br>Committed to generating sustainable double-digit statutory returns |
| **RoTE**<br>Underlying RoTE of c.10%[(2)]<br>Statutory RoTE of c.8% | |

(1) Excluding financial crime prevention programme from FY24.

(2) Excluding financial crime prevention programme from FY24 and cash flow hedge reserve.

### Summary income statement – statutory basis

| For the year ended 30 September | 2023 £m | 2022 £m |
|---|---|---|
| Net interest income | **1,687** | 1,576 |
| Non-interest income | **140** | 140 |
| **Total operating income** | **1,827** | 1,716 |
| Operating and administrative expenses | **(1,173)** | (1,069) |
| **Operating profit before impairment losses** | **654** | 647 |
| Impairment losses on credit exposures | **(309)** | (52) |
| **Statutory profit on ordinary activities before tax** | **345** | 595 |
| Tax expense | **(99)** | (58) |
| **Statutory profit after tax** | **246** | 537 |

The Group has recognised a statutory profit before tax of £345m (2022: £595m). The reduction in statutory profit is primarily driven by higher credit impairment losses, following the low charge last year and higher adjusting items, primarily reflecting restructuring costs in the year. From FY24, the Group will no longer report on both an underlying and a statutory basis; the income statement will be reported on a statutory basis, with notable items separated out to enable the reporting of Adjusted Income and Expenditure.

### Performance measures[1]

| | 2023 | 2022 | Change |
|---|---|---|---|
| **Profitability** | | | |
| RoTE | **3.9%** | 10.3% | (6.4)%pts |
| Cost: income ratio | **64%** | 62% | 2%pts |
| Return on assets | **0.27%** | 0.60% | (0.33)%pts |
| Basic earnings per share (EPS) | **14.0p** | 32.4p | (18.4)p |

(1) For a definition of each of the performance measures, refer to 'Measuring the Group's performance' on pages 122 to 132.

### Reconciliation of statutory to underlying results

The statutory basis presented within this section reflects the Group's results as reported in the financial statements. The underlying basis reflects the Group's financial performance as presented to the CEO, Executive Leadership Team and Board and excludes certain items that are part of the statutory results. The table below reconciles the statutory results to the underlying results, and full details on the adjusted items to the underlying results are included on page 133.

| 2023 income statement | Statutory results £m | Restructuring charges £m | Acquisition accounting unwinds £m | Legacy conduct £m | Hedge ineffectiveness[1] £m | Other £m | Underlying results £m |
|---|---|---|---|---|---|---|---|
| Net interest income | **1,687** | **–** | **29** | **–** | **–** | **–** | **1,716** |
| Non-interest income | **140** | **–** | **–** | **–** | **16** | **1** | **157** |
| **Total operating income** | **1,827** | **–** | **29** | **–** | **16** | **1** | **1,873** |
| Total operating and administrative expenses before impairment losses | **(1,173)** | **131** | **–** | **12** | **–** | **59** | **(971)** |
| **Operating profit before impairment losses** | **654** | **131** | **29** | **12** | **16** | **60** | **902** |
| Impairment losses on credit exposures | **(309)** | **–** | **–** | **–** | **–** | **–** | **(309)** |
| **Profit on ordinary activities before tax** | **345** | **131** | **29** | **12** | **16** | **60** | **593** |
| **Financial performance measures** | | | | | | | |
| RoTE | **3.9%** | **2.0%** | **0.4%** | **0.2%** | **0.2%** | **0.9%** | **7.6%** |
| Cost: income ratio | **64.2%** | **(6.5)%** | **(1.5)%** | **(0.6)%** | **(0.7)%** | **(3.0)%** | **51.9%** |
| Basic EPS | **14.0p** | **7.1p** | **1.6p** | **0.6p** | **0.9p** | **3.2p** | **27.4p** |

| 2022 income statement | Statutory results £m | Restructuring charges £m | Acquisition accounting unwinds £m | Legacy conduct £m | Hedge ineffectiveness[1] £m | Other £m | Restated Underlying results £m |
|---|---|---|---|---|---|---|---|
| Net interest income | 1,576 | – | 16 | – | – | – | 1,592 |
| Non-interest income | 140 | – | 16 | – | (13) | 7 | 150 |
| **Total operating income** | 1,716 | – | 32 | – | (13) | 7 | 1,742 |
| Total operating and administrative expenses before impairment losses | (1,069) | 82 | 3 | 8 | – | 62 | (914) |
| **Operating profit before impairment losses** | 647 | 82 | 35 | 8 | (13) | 69 | 828 |
| Impairment losses on credit exposures | (52) | – | – | – | | – | (52) |
| **Profit on ordinary activities before tax** | 595 | 82 | 35 | 8 | (13) | 69 | 776 |
| **Financial performance measures** | | | | | | | |
| RoTE | 10.3% | 1.4% | 0.6% | 0.1% | (0.2)% | 1.1% | 13.3% |
| Cost: income ratio | 62.3% | (4.5)% | (1.9)% | (0.4)% | 0.7% | (3.7)% | 52.5% |
| Basic EPS | 32.4p | 4.3p | 1.8p | 0.4p | (0.7)p | 3.6p | 41.8p |

(1) Hedge ineffectiveness is now presented as an adjustment to underlying non-interest income as detailed on page 133. The comparative period has been adjusted accordingly. This restatement does not impact the statutory results of the Group.

# At a time of ongoing challenge for the UK economy, our lending portfolios remain well positioned.

**A disciplined approach to credit risk management supports the Group's operations and has underpinned its resilience in recently challenging times.**

Credit risk is the risk that a retail or business borrower or counterparty fails to pay the interest or capital due on a loan, or other financial instrument. Credit risk needs to be managed through the life cycle of each loan from origination to repayment, redemption, write off or sale. Credit risk manifests itself in the financial instruments and products that the Group offers, and in which it invests, and can arise in respect of both on- and off-balance sheet exposures.

Close monitoring, clear policies and a disciplined approach to credit risk management support the Group's operations, and have underpinned its resilience in recently challenging times. The emergence of the significant inflationary headwinds and cost of living pressures have the potential to affect customer resilience and debt affordability. The Group has taken a number of steps to support customers through this period of heightened affordability pressure, and ensure that its credit risk framework and associated policies and credit strategies remain effective and appropriate.

## Managing credit risk within our asset portfolios

### Risk appetite

The Group controls its levels of credit risk by placing limits on the amount of risk it is willing to take in order to achieve its strategic objectives. This approach involves a defined set of quantitative limits in relation to its credit risk concentrations to one borrower, or group of borrowers, and to geographical, product and industry segments. The management of credit risk within the Group is achieved through timely changes to application scorecards and credit strategies, ongoing approval and monitoring of individual transactions, regular asset quality reviews and the independent oversight of credit decisions and portfolios.

The Group maintained a controlled approach to portfolio management and appetite for new lending origination in an increasing inflationary environment, with updates to underwriting lending assessment to reflect the uncertain economic environment and interest rate pressures. The FY24 RAS continues to consider the impact of higher interest rates combined with inflationary headwinds and cost of living pressures, and is focused on supporting customers through this challenging period. Climate risk is an increasingly important component of the broader RMF and we have recognised this through the inclusion of climate risk as a principal risk. The framework has been updated to embed climate risk considerations across various aspects of customer lending and credit risk management practices.

### Measurement

The Group uses a range of statistical models, supported by both internal and external data, to assess credit risk exposures. These models underpin the IRB capital calculation for the Mortgage and Business portfolios, and account management activity for all portfolios. Further information on the measurement and calculation of ECL and the Group's approach to the impairment of financial assets can be found on page 21.

Political and economic risk is an emerging risk for the Group and includes the future impact on macroeconomic variables, which are used in the calculation of the Group's modelled ECL output. Further detail on the Group's use of macroeconomic variables in the year can be found on pages 40 to 47.

### Mitigation

The Group maintains a dynamic approach to credit management and takes appropriate steps if individual issues are identified, or if credit performance has, or is expected to, deteriorate due to borrower, economic or sector-specific weaknesses.

The mitigation of credit risk within the Group is achieved through approval and monitoring of automated credit strategies, individual transactions, asset quality, analysis of the performance of the various credit portfolios, and oversight of credit portfolios across the Group. Portfolio monitoring techniques include customer, product, industry, geographic concentrations, and delinquency trends, as well as considering layered risks where customers may have more than one higher risk characteristic.

The Group has taken additional steps to update affordability assessments in response to the inflationary and cost of living pressures facing customers. Credit risk mitigation is also supported, in part, by obtaining collateral, and corporate and personal guarantees where appropriate.

The key mitigating measures are described below.

### Credit assessment and mitigation

Credit risk is managed in accordance with lending policies, the Group's risk appetite and the RMF. Lending policies and performance against risk appetite are reviewed regularly.

The Group uses a variety of lending criteria when assessing applications for Mortgage and Unsecured customers. The approval process uses credit scorecards, credit strategies and affordability assessments, and involves a review of an applicant's previous credit history using information held by credit reference agencies as well as internal information. Manual underwriting assessments are also used as and when required. The Group also utilises quantitative thresholds, for example debt to income ratios, as well as the ratio of borrowing to collateral. Some of these limits relate to internal approval levels and others are hard limits above which the Group will reject the application.

For residential mortgages, the Group's policy is to accept only within the maximum percentage loan to value (LTV) limit that may be offered subject to loan size and customer income. Product availability may be altered depending on market conditions and outlook. Product types such as BTL and residential interest-only mortgages are controlled by transactional limits covering both LTV and value.

For business customers, credit risk is further mitigated by focusing on business sectors where the Group has specific expertise, and through limiting exposures on higher value loans and to certain sectors. When making credit decisions for business customers the Group will routinely assess the primary source of repayment, most typically the cash generated by the customer through its normal trading cycle. Secondary sources of repayment are also considered and while not the focus of the lending decision, collateral will be taken when appropriate. The Group seeks to obtain security cover and, where relevant, guarantees from borrowers.

**Specialist expertise**
Credit quality is managed and monitored by skilled teams including, where required, specialists that provide dedicated support for vulnerable customers experiencing financial or other types of difficulties. These specialists act within agreed delegated authority levels set in accordance with experience and capabilities.

**Credit strategy and policy**
Credit risks associated with lending are managed through the application of detailed lending policies and standards that outline the approach to lending, underwriting criteria, credit mandates, concentration limits and product terms.

For complex credit products and services, the Chief Credit Officer and Credit Risk Committee provide a policy framework that identifies, quantifies and mitigates credit risk. These policies and frameworks are delegated to, and disseminated under, the guidance and control of the Board and senior management, with appropriate oversight through governance committees.

Specialist credit teams provide oversight of credit portfolio performance as well as adherence to credit risk policies and standards. Activities include targeted risk-based reviews, providing an assessment of the effectiveness of internal controls and risk management practices. Bespoke assignments are also undertaken in response to emerging risks and regulatory requirements. Independent assurance reviews are regularly undertaken by Internal Audit.

**Portfolio oversight**
The Group's credit portfolios, and the key benchmarks, behaviours and characteristics that are used to manage portfolios, are regularly monitored, with portfolio monitoring packs provided for review by senior management.

**Controls over rating systems**
The Group has a Model Risk Management team that sets common minimum standards for risk models and associated rating systems to ensure these are developed and monitored consistently, and are of sufficient quality to support business decisions and meet regulatory requirements. The Group performs an annual self-assessment of its rating systems to ensure ongoing CRR compliance.

The Group also utilises other instruments and techniques across its wider balance sheet. These are summarised below:

**Derivatives**
The Group maintains control limits on net open derivative positions. At any one time, the amount subject to credit risk is limited to the current fair value of instruments that are favourable to the Group (i.e. assets where the fair value is positive) and in relation to derivatives, may only be a small fraction of the contract, or notional values associated with instruments outstanding. This credit risk is managed as part of the customer's overall exposure together with potential exposures from market movements.

**Master netting agreements**
The Group further restricts its exposure to credit losses by entering master netting arrangements with counterparties with whom it undertakes a significant volume of transactions. Master netting arrangements do not generally result in an offset of balance sheet assets and liabilities, as transactions are usually settled on a gross basis. However, credit risk associated with the favourable contracts is reduced by a master netting arrangement to the extent that, if any counterparty failed to meet its obligations in accordance with the agreed terms, all amounts with the counterparty are terminated and settled on a net basis. Derivative financial instrument contracts are typically subject to the International Swaps and Derivatives Association (ISDA) master netting agreements, as well as Credit Support Annexes, where relevant, around collateral arrangements attached to those ISDA agreements. Derivative exchange or clearing counterparty agreements exist where contracts are settled via an exchange or clearing house.

**Collateral**
The Group evaluates each customer's creditworthiness on a case by case basis. The amount of collateral obtained, if deemed necessary by the Group upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held as security, and other credit enhancements include the following:

**Residential mortgages**
Residential property is the Group's main source of collateral on mortgage lending and means of mitigating loss in the event of the default risk inherent in its residential mortgage portfolios. All lending activities are supported by an appropriate form of valuation. This valuation is applied using either a physical valuation, or another method that is not reliant on a physical inspection, but utilises data and modelled information, such as desktop, automated valuation model or indexed valuations (subject to policy rules and requirements).

It is the Group's policy to dispose of repossessed properties, with the proceeds used to reduce or repay the outstanding balance. The Group does not occupy repossessed properties for its own business use.

**Commercial property**
Commercial property is a source of collateral on business lending and means of mitigating loss in the event of default. For commercial loans, collateral comprises first legal charges over freehold, or long leasehold property (including formal Companies House registration where appropriate). All commercial property collateral is subject to an independent, professional valuation when taken and thereafter subject to periodic review in accordance with policy requirements.

**Non-property related collateral**
In addition to residential and commercial property-based security, the Group also takes other forms of collateral when lending. This collateral can involve obtaining security against the underlying loan through the use of cash collateral and/or netting agreements, both of which reduce the original exposure by the amount of collateral held, subject to volatility and maturity adjustments where applicable. It can also include specific or interlocking guarantees, and loan agreements, which include affirmative and negative covenants and, in some instances, guarantees of counterparty obligations.

The Group also provides asset-backed lending in the form of asset and invoice finance. Security for these exposures is held in the form of direct recourse to the underlying asset financed.

Generally, the Group does not take possession of collateral it holds as security, or call on other credit enhancements, that would result in recognition of an asset on its balance sheet.

**Monitoring**
Credit policies and procedures, which are subject to ongoing review, are documented and disseminated in a form that supports the credit operations of the Group.

- Credit Risk Committee: has oversight of the quality, composition and concentrations of the credit risk portfolio. It also determines and approves strategies to adjust the portfolio for changes in market conditions.
- RAS measures: Measures are reported monthly to ensure adherence to appetite. A formal annual review is carried out to ensure that the measures accurately reflect the Group’s risk appetite, strategy and concerns relative to the wider macro environment. All measures are subject to extensive engagement with the Executive Leadership Team and the Board, and are subject to endorsement from executive governance committees prior to Board approval. Regulatory engagement is also scheduled as appropriate.
- Risk concentration: Concentration of risk is managed by counterparty, product, geographical region and industry sector. In addition, single name exposure limits exist to control exposures to a single counterparty. Concentrations are also considered through the RAS process, focusing particularly on the external environment, outlook and comparison against market benchmarks, as well as considering layered risks where customers may have more than one higher risk characteristic.
- Single large exposure excesses: Excesses on exposures under the delegated commitment authority of the Transactional Credit Committee are reported to the committee when above defined limits. All excess reports include a proposed route to remediation. Exposures are also managed in accordance with the large exposure reporting requirements of the Capital Requirements Regulation (CRR).
- Portfolio monitoring: Continuous monitoring of the portfolio composition and performance is undertaken through monthly reviews.

**Forbearance**
Forbearance is considered to exist where customers are experiencing, or about to experience, financial difficulty and the Group grants a concession on a non-commercial basis. The Group’s forbearance policies and definitions comply with the guidance established by the EBA for financial reporting. Forbearance concessions include the granting of more favourable terms and conditions than those provided at drawdown of the facility, or conditions that would not ordinarily be available to other customers with a similar risk profile. Forbearance parameters are regularly reviewed and refined as necessary to ensure they are consistent with the latest industry guidance and prevailing practice, as well as ensuring that any assessment adequately captures and reflects the most recent customer behaviours and market conditions.

## Measuring credit risk within asset portfolios
At each reporting date, the Group assesses financial assets measured at amortised cost, as well as loan commitments and financial guarantees, for impairment. The impairment loss allowance is calculated using an ECL methodology and reflects: (i) an unbiased and probability weighted amount; (ii) the time value of money, which discounts the impairment loss; and (iii) reasonable and supportable information that is available without undue cost or effort about past events, current conditions and forecasts of future economic conditions.

The Group adopts two approaches in the measurement of credit risk: (i) collectively assessed – where the Group uses a combination of strategies and statistical models that utilise internal and external data to measure the exposure to credit risk within the portfolios (supplemented by management adjustments (MAs) where necessary); and (ii) individually assessed – where a charge is taken to the income statement when an individually assessed provision (IA) has been recognised, or a direct write-off has been applied to an asset balance.

**ECL methodology**
ECL methodology is based upon the combination of probability of default (PD), loss given default (LGD) and exposure at default (EAD) estimates that consider a range of factors that impact on credit risk and the level of impairment loss provisioning. The Group uses reasonable and supportable forecasts of future economic conditions in estimating the ECL allowance. The methodology and assumptions used in the ECL calculation are reviewed regularly and updated as necessary.

The calculated model ECL is determined using the following classifications:

| Stage | ECL calculation period | Description |
|---|---|---|
| **1** | 12-month | An exposure that is not credit-impaired on initial recognition and has not experienced a significant increase in credit risk (SICR) since initial recognition. |
| **2** | Lifetime | An exposure that has experienced a SICR since initial recognition but is not yet deemed to be credit impaired. |
| **3** | Lifetime | An exposure that is credit impaired. |

A Stage 2 ECL is required where a SICR has been identified, such as a deterioration in the PD since origination. Absent any specific SICR factors, the Group operates a 30 DPD backstop for classification as Stage 2, and 90 DPD for Stage 3. Forborne exposures can be classed as either Stage 2 or Stage 3 depending on the type of forbearance programme that has been applied to the customer. IA provisions are classed as Stage 3. When a loan is deemed uncollectable, and all necessary internal procedures have been completed, it is written off against the related impairment loss. Subsequent recoveries of amounts previously written off reduce the expense in the income statement.

Purchased or originated credit-impaired (POCI) financial assets are those that are assessed as being credit-impaired upon initial recognition, and once classified as POCI, remain in Stage 3 until derecognition irrespective of any change in credit quality. The Group regards the date of acquisition as the origination date for purchased portfolios.

SICR criteria and triggers are parameters subject to the same governance pathway as the Group's IFRS 9 models; with changes to triggers initially submitted to and endorsed by the Credit Model Technical Forum and formal approval provided by the MGC.

The Credit Risk Committee provides oversight on the adequacy of ECL provisioning with reviews and robust challenge of the calculation and management judgement recommendations. This includes the rationale behind the inclusion of MAs. The Boards' Audit Committee provides oversight to the ECL calculation and measurement, with reviews and robust challenge of all calculated outcomes and management judgements.

Further detail on the accounting policy applied to ECLs can be found in note 3.1.1 to the financial statements.

**Accounting and regulatory credit loss frameworks**
The approach to calculating credit losses differs between the accounting and regulatory frameworks applicable to the Group, with the most significant difference being that the concept of SICR, which moves exposures from a 12-month to a lifetime ECL calculation in the accounting framework, does not exist under the regulatory framework. The approach to staging under IFRS 9 is also not applicable under regulatory credit loss reporting.

Both frameworks calculate credit losses under a PD x LGD x EAD approach, with the regulatory IRB approach assessing these in the next 12 months, whereas the accounting framework under IFRS 9 requires these losses to be assessed on a forward-looking view, with a lifetime loss calculated where appropriate. Credit losses are supplemented by MAs, where required, under the accounting framework.

Both the accounting and regulatory definitions of default are materially aligned, with default being triggered at 90 DPD, with the exception of the heritage Virgin Money mortgage models, that apply a 180 DPD regulatory default trigger under existing approved permissions. The definition of default will be fully aligned to 90 DPD when the regulatory models are updated in line with the hybrid model adoption, which is anticipated in FY24.

**Cure periods**
The Group aligns the regulatory cure periods for forborne exposures in its IFRS 9 staging criteria (as Stage 2 or 3) at a minimum period of either 24, or 36 months, depending on the forbearance programme utilised. Where exposures are classified as Stage 2 or 3 as a result of not being in a forbearance programme, these can cure and transfer to the appropriate stage when the relevant staging trigger is no longer applicable (i.e., there is no identifiable SICR or the exposure is no longer considered credit-impaired).

### Group credit risk exposures

The Group is exposed to credit risk across all of its financial asset classes, however, its principal exposure to credit risk arises on customer lending balances. Given the relative significance of customer lending exposures to the Group's overall credit risk position, the disclosures that follow are focused principally on customer lending.

The Group is also exposed to credit risk on its other banking and treasury-related activities, and holds £11.3bn (2022: £12.2bn) of cash and balances with central banks and £0.7bn (2022: £0.7bn) due from other banks at amortised cost, with a further £6.2bn (2022: £5.1bn) of financial assets at fair value through other comprehensive income (FVOCI). Cash and balances with central banks includes £10.2bn of cash held with the BoE (2022: £11.0bn). Balances with other banks and financial assets at FVOCI are primarily held with senior investment grade counterparties. All other banking and treasury-related financial assets are classed as Stage 1 with no material ECL provision held.

**Maximum exposure to credit risk on financial assets, contingent liabilities and credit-related commitments**

The following tables show the levels of concentration of the Group's financial assets and credit-related commitments:

| | 2023 | | | 2022 | | |
|---|---|---|---|---|---|---|
| | Gross loans and advances to customers £m | Credit-related commitments £m | Total £m | Gross loans and advances to customers £m | Credit-related commitments £m | Total £m |
| Mortgages | **57,797** | **2,685** | **60,482** | 58,464 | 4,200 | 62,664 |
| Unsecured | **6,814** | **11,242** | **18,056** | 6,513 | 11,057 | 17,570 |
| Business | **8,684** | **4,073** | **12,757** | 8,169 | 4,102 | 12,271 |
| **Total** | **73,295** | **18,000** | **91,295** | 73,146 | 19,359 | 92,505 |
| Impairment provisions on credit exposures(1) | **(612)** | **(5)** | **(617)** | (454) | (3) | (457) |
| Fair value hedge adjustment | **(492)** | **–** | **(492)** | (941) | – | (941) |
| Maximum credit risk exposure on lending assets | **72,191** | **17,995** | **90,186** | 71,751 | 19,356 | 91,107 |
| Cash and balances with central banks | | | **11,282** | | | 12,221 |
| Financial instruments at FVOCI | | | **6,184** | | | 5,064 |
| Due from other banks | | | **667** | | | 656 |
| Other financial assets at fair value | | | **61** | | | 78 |
| Derivative financial assets | | | **135** | | | 342 |
| Maximum credit risk exposure on all financial assets(2) | | | **108,515** | | | 109,468 |

(1) The total ECL provision covers both on and off-balance sheet exposures, which are reflected in notes 3.1.1.1 and 3.7 respectively. All tables and ratios that follow are calculated using the combined on- and off-balance sheet ECL, which is consistent for all periods reported.

(2) Unless otherwise noted, the amount that best represents the maximum credit exposure at the reporting date is the carrying value of the financial asset.

In addition to the balance sheet position above, key metrics of relevance are as follows:

| Key credit metrics | 2023 £m | 2022 £m |
|---|---|---|
| **Impairment charge on credit exposures** | | |
| Mortgage lending | **2** | (30) |
| Unsecured lending | **269** | 178 |
| Business lending | **38** | (96) |
| **Total Group impairment charge** | **309** | 52 |
| Underlying impairment charge(1) to average customer loans (cost of risk) | **0.42%** | 0.07% |
| **Key asset quality ratios** | | |
| Loans in Stage 2 | **8.63%** | 7.76% |
| Loans in Stage 3 | **1.47%** | 1.41% |
| Total book coverage(2) | **0.84%** | 0.62% |
| Stage 2 coverage(2) | **6.33%** | 4.72% |
| Stage 3 coverage(2) | **13.93%** | 11.24% |

(1) Inclusive of gains/losses on assets held at fair value and elements of fraud loss.

(2) Excludes the guaranteed element of government-backed loan schemes.

# Credit risk

The total gross lending to customers has remained broadly stable overall with £73.3bn at 30 September 2023 (2022: £73.1bn). The total lending in the Mortgage portfolio reduced to £57.8bn at September 2023 (2022: £58.5bn) with the demand for new lending slightly reduced due to the higher rate environment, stressed affordability pressure and wider cost of living considerations. The underlying Business lending portfolio (excluding the repayments of the government backed loan schemes) has grown to £7.9bn at 30 September 2023 (2022: £7.1bn) with broad based growth across the sector specialisms in our target market segments. The Unsecured lending book has grown to £6.8bn at 30 September 2023 (2022: £6.5bn), mainly driven by credit card growth.

The performance of the portfolio and overall asset quality remains robust, and whilst there are signs of deterioration in some metrics, the proportion of the Stage 2 portfolio not past due, remains high at 94% at September 2023 (2022: 93%). The Group remains focused on reaching good customer outcomes and deploys a range of customer support measures combined with the Group's risk appetite and continued focus on responsible lending.

The impact of significant external economic and geopolitical factors continues to have the potential to impact the short to medium-term performance of the portfolio, with the most significant of these being the cost of living pressures.

The selection of appropriate MAs is a major component in determining the Group's ECL; a detailed analysis is shown on page 45.

The Group has recorded a total impairment provision of £617m at 30 September 2023, reflecting a 35% increase from £457m at 30 September 2022, and a corresponding increase in coverage from 62bps to 84bps. Within this, the modelled and IA provision has increased to £541m (2022: £372m) driven by the updated macroeconomic inputs, model calibrations and growth in the Business and Unsecured lending portfolios. MAs have reduced in the period to £76m (2022: £85m). The increase in provision coupled with the individually assessed impairment charge of £142m in the year (2022: £107m) results in a net charge to the income statement of £309m (2022: £52m) and an associated cost of risk of 42bps (2022: 7bps).

**Gross loans and advances(1) ECL and coverage**

| | | | Unsecured | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Mortgages | | Cards | | Loans and Overdrafts | | Combined | | Business(2) | | Total | |
| **2023** | £m | % | £m | % | £m | % | £m | % | £m | % | £m | % |
| Stage 1 | **54,540** | **94.3%** | **4,658** | **76.5%** | **398** | **54.8%** | **5,056** | **74.2%** | **6,293** | **72.5%** | **65,889** | **89.9%** |
| Stage 2 – total | **2,704** | **4.7%** | **1,321** | **21.7%** | **321** | **44.3%** | **1,642** | **24.1%** | **1,980** | **22.8%** | **6,326** | **8.6%** |
| Stage 2: 0 DPD | **2,405** | **4.2%** | **1,250** | **20.5%** | **316** | **43.6%** | **1,566** | **23.0%** | **1,951** | **22.4%** | **5,922** | **8.1%** |
| Stage 2: < 30 DPD | **98** | **0.2%** | **37** | **0.6%** | **2** | **0.3%** | **39** | **0.6%** | **14** | **0.2%** | **151** | **0.2%** |
| Stage 2: > 30 DPD | **201** | **0.3%** | **34** | **0.6%** | **3** | **0.4%** | **37** | **0.5%** | **15** | **0.2%** | **253** | **0.3%** |
| Stage 3(3) | **553** | **1.0%** | **109** | **1.8%** | **7** | **0.9%** | **116** | **1.7%** | **411** | **4.7%** | **1,080** | **1.5%** |
| | **57,797** | **100%** | **6,088** | **100%** | **726** | **100%** | **6,814** | **100%** | **8,684** | **100%** | **73,295** | **100%** |
| **ECLs(4)** | | | | | | | | | | | | |
| Stage 1 | **13** | **22.6%** | **42** | **10.8%** | **4** | **12.1%** | **46** | **10.9%** | **30** | **22.6%** | **89** | **14.5%** |
| Stage 2 – total | **27** | **47.9%** | **294** | **74.9%** | **28** | **73.5%** | **322** | **74.8%** | **51** | **39.4%** | **400** | **64.7%** |
| Stage 2: 0 DPD | **23** | **42.0%** | **256** | **65.3%** | **25** | **67.1%** | **281** | **65.5%** | **51** | **39.2%** | **355** | **57.6%** |
| Stage 2: < 30 DPD | **1** | **1.3%** | **17** | **4.3%** | **1** | **1.9%** | **18** | **4.1%** | **–** | **0.2%** | **19** | **3.0%** |
| Stage 2: > 30 DPD | **3** | **4.6%** | **21** | **5.3%** | **2** | **4.5%** | **23** | **5.2%** | **–** | **–** | **26** | **4.1%** |
| Stage 3(3) | **17** | **29.5%** | **56** | **14.3%** | **5** | **14.4%** | **61** | **14.3%** | **50** | **38.0%** | **128** | **20.8%** |
| | **57** | **100%** | **392** | **100%** | **37** | **100%** | **429** | **100%** | **131** | **100%** | **617** | **100%** |
| **Coverage** | | | | | | | | | | | | |
| Stage 1 | | **0.02%** | | **0.98%** | | **1.07%** | | **0.99%** | | **0.49%** | | **0.13%** |
| Stage 2 – total | | **0.99%** | | **23.16%** | | **8.16%** | | **20.07%** | | **2.66%** | | **6.33%** |
| Stage 2: 0 DPD | | **0.98%** | | **21.31%** | | **7.56%** | | **18.38%** | | **2.67%** | | **6.02%** |
| Stage 2: < 30 DPD | | **0.74%** | | **48.66%** | | **35.30%** | | **47.94%** | | **1.56%** | | **12.19%** |
| Stage 2: > 30 DPD | | **1.28%** | | **64.90%** | | **56.02%** | | **64.16%** | | **0.95%** | | **10.38%** |
| Stage 3(3) | | **3.03%** | | **54.15%** | | **77.16%** | | **55.57%** | | **19.76%** | | **13.93%** |
| | | **0.10%** | | **6.88%** | | **4.88%** | | **6.65%** | | **1.60%** | | **0.84%** |
| **Undrawn exposures** | | | | | | | | | | | | |
| Stage 1 | **2,560** | **95.4%** | **10,493** | **96.2%** | **280** | **82.1%** | **10,773** | **95.8%** | **3,453** | **84.7%** | **16,786** | **93.3%** |
| Stage 2 | **114** | **4.2%** | **387** | **3.6%** | **60** | **17.6%** | **447** | **4.0%** | **597** | **14.7%** | **1,158** | **6.4%** |
| Stage 3(3) | **11** | **0.4%** | **21** | **0.2%** | **1** | **0.3%** | **22** | **0.2%** | **23** | **0.6%** | **56** | **0.3%** |
| | **2,685** | **100.0%** | **10,901** | **100.0%** | **341** | **100.0%** | **11,242** | **100.0%** | **4,073** | **100.0%** | **18,000** | **100.0%** |

# Credit risk

| | | | Unsecured | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Mortgages | | Cards | | Loans and Overdrafts | | Combined | | Business[2] | | Total | |
| **2022** | £m | % | £m | % | £m | % | £m | % | £m | % | £m | % |
| Stage 1 | 54,791 | 93.7% | 4,712 | 84.8% | 612 | 64.1% | 5,324 | 81.8% | 6,270 | 76.7% | 66,385 | 90.8% |
| Stage 2 – total | 3,090 | 5.3% | 774 | 13.9% | 335 | 35.1% | 1,109 | 17.0% | 1,526 | 18.7% | 5,725 | 7.8% |
| Stage 2: 0 DPD | 2,763 | 4.7% | 723 | 13.0% | 327 | 34.3% | 1,050 | 16.1% | 1,499 | 18.4% | 5,312 | 7.2% |
| Stage 2: < 30 DPD | 158 | 0.3% | 27 | 0.5% | 3 | 0.3% | 30 | 0.5% | 9 | 0.1% | 197 | 0.3% |
| Stage 2: > 30 DPD | 169 | 0.3% | 24 | 0.4% | 5 | 0.5% | 29 | 0.4% | 18 | 0.2% | 216 | 0.3% |
| Stage 3[3] | 583 | 1.0% | 72 | 1.3% | 8 | 0.8% | 80 | 1.2% | 373 | 4.6% | 1,036 | 1.4% |
| | 58,464 | 100.0% | 5,558 | 100.0% | 955 | 100.0% | 6,513 | 100.0% | 8,169 | 100.0% | 73,146 | 100.0% |
| **ECLs[4]** | | | | | | | | | | | | |
| Stage 1 | 10 | 17.9% | 57 | 23.2% | 6 | 15.8% | 63 | 22.2% | 12 | 10.3% | 85 | 18.6% |
| Stage 2 – total | 32 | 57.1% | 156 | 63.4% | 25 | 65.8% | 181 | 63.7% | 55 | 47.0% | 268 | 58.6% |
| Stage 2: 0 DPD | 28 | 49.9% | 129 | 52.4% | 22 | 57.9% | 151 | 53.1% | 55 | 47.0% | 234 | 51.2% |
| Stage 2: < 30 DPD | 2 | 3.6% | 14 | 5.7% | 1 | 2.6% | 15 | 5.3% | – | – | 17 | 3.7% |
| Stage 2: > 30 DPD | 2 | 3.6% | 13 | 5.3% | 2 | 5.3% | 15 | 5.3% | – | – | 17 | 3.7% |
| Stage 3[3] | 14 | 25.0% | 33 | 13.4% | 7 | 18.4% | 40 | 14.1% | 50 | 42.7% | 104 | 22.8% |
| | 56 | 100.0% | 246 | 100.0% | 38 | 100.0% | 284 | 100.0% | 117 | 100.0% | 457 | 100.0% |
| **Coverage** | | | | | | | | | | | | |
| Stage 1 | | 0.02% | | 1.29% | | 1.06% | | 1.26% | | 0.22% | | 0.13% |
| Stage 2 – total | | 1.02% | | 21.94% | | 7.29% | | 17.22% | | 3.75% | | 4.72% |
| Stage 2: 0 DPD | | 1.02% | | 19.41% | | 6.41% | | 15.09% | | 3.76% | | 4.43% |
| Stage 2: < 30 DPD | | 0.81% | | 57.37% | | 33.67% | | 54.48% | | 3.57% | | 8.53% |
| Stage 2: > 30 DPD | | 1.25% | | 59.03% | | 52.92% | | 58.01% | | 1.47% | | 8.57% |
| Stage 3[3] | | 2.28% | | 50.96% | | 73.14% | | 53.51% | | 19.96% | | 11.24% |
| | | 0.09% | | 4.81% | | 3.88% | | 4.66% | | 1.59% | | 0.62% |
| **Undrawn exposures** | | | | | | | | | | | | |
| Stage 1 | 4,060 | 96.7% | 10,494 | 97.8% | 288 | 89.5% | 10,782 | 97.5% | 3,612 | 88.1% | 18,454 | 95.3% |
| Stage 2 | 132 | 3.1% | 236 | 2.2% | 33 | 10.2% | 269 | 2.4% | 464 | 11.3% | 865 | 4.5% |
| Stage 3[3] | 8 | 0.2% | 5 | 0.0% | 1 | 0.3% | 6 | 0.1% | 26 | 0.6% | 40 | 0.2% |
| | 4,200 | 100.0% | 10,735 | 100.0% | 322 | 100.0% | 11,057 | 100.0% | 4,102 | 100.0% | 19,359 | 100.0% |

(1) Excludes loans designated at fair value through profit or loss (FVTPL), balances due from customers on acceptances, accrued interest and deferred and unamortised fee income.

(2) Business and total coverage ratio excludes the guaranteed element of government-backed loans.

(3) Stage 3 includes POCI for gross loans and advances of £48m for Mortgages and £1m for Unsecured (2022: £56m and £1m respectively); and ECL of (£1m) for Mortgages and (£1m) for Unsecured (2022: (£1m) and (£2m) respectively).

(4) Includes £5m ECL held for the undrawn exposures shown (2022: £3m), of which £1m (2022:1m) is held under Stage 1 and £4m (2022: £2m) under Stage 2.

**Stage 2 balances**

There can be a number of reasons that require a financial asset to be subject to a Stage 2 lifetime ECL calculation other than reaching the 30 DPD backstop. The following table highlights the relevant trigger point leading to a financial asset being classed as Stage 2:

| | | | Personal | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Mortgages | | Cards | | Loans and Overdrafts | | Combined | | Business | | Total | |
| **2023** | £m | % | £m | % | £m | % | £m | % | £m | % | £m | % |
| PD deterioration | **1,739** | **65%** | **777** | **59%** | **317** | **99%** | **1,094** | **67%** | **1,229** | **62%** | **4,062** | **64%** |
| Forbearance | **81** | **3%** | **16** | **1%** | **1** | **–** | **17** | **1%** | **281** | **14%** | **379** | **6%** |
| AFD or Watch List(1) | **1** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **455** | **23%** | **456** | **7%** |
| > 30 DPD | **201** | **7%** | **34** | **3%** | **3** | **1%** | **37** | **2%** | **15** | **1%** | **253** | **4%** |
| Other(2) | **682** | **25%** | **494** | **37%** | **–** | **–** | **494** | **30%** | **–** | **–** | **1,176** | **19%** |
| | **2,704** | **100%** | **1,321** | **100%** | **321** | **100%** | **1,642** | **100%** | **1,980** | **100%** | **6,326** | **100%** |
| **ECLs** | | | | | | | | | | | | |
| PD deterioration | **18** | **67%** | **143** | **49%** | **26** | **93%** | **169** | **52%** | **23** | **45%** | **210** | **52%** |
| Forbearance | **3** | **11%** | **5** | **2%** | **–** | **–** | **5** | **2%** | **14** | **28%** | **22** | **6%** |
| AFD or Watch List(1) | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **14** | **27%** | **14** | **4%** |
| > 30 DPD | **3** | **11%** | **21** | **7%** | **2** | **7%** | **23** | **7%** | **–** | **–** | **26** | **7%** |
| Other(2) | **3** | **11%** | **125** | **42%** | **–** | **–** | **125** | **39%** | **–** | **–** | **128** | **31%** |
| | **27** | **100%** | **294** | **100%** | **28** | **100%** | **322** | **100%** | **51** | **100%** | **400** | **100%** |

| | | | Personal | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Mortgages | | Cards | | Loans and Overdrafts | | Combined | | Business | | Total | |
| **2022** | £m | % | £m | % | £m | % | £m | % | £m | % | £m | % |
| PD deterioration | 2,084 | 69% | 401 | 52% | 329 | 99% | 730 | 66% | 826 | 55% | 3,640 | 64% |
| Forbearance | 106 | 3% | 9 | 1% | 1 | – | 10 | 1% | 235 | 15% | 351 | 6% |
| AFD or Watch List(1) | 6 | – | – | – | – | – | – | – | 447 | 29% | 453 | 8% |
| > 30 DPD | 169 | 5% | 24 | 3% | 5 | 1% | 29 | 3% | 18 | 1% | 216 | 4% |
| Other(2) | 725 | 23% | 340 | 44% | – | – | 340 | 30% | – | – | 1,065 | 18% |
| | 3,090 | 100% | 774 | 100% | 335 | 100% | 1,109 | 100% | 1,526 | 100% | 5,725 | 100% |
| **ECLs** | | | | | | | | | | | | |
| PD deterioration | 18 | 55% | 73 | 47% | 23 | 92% | 96 | 53% | 26 | 47% | 140 | 53% |
| Forbearance | 5 | 16% | 3 | 2% | – | – | 3 | 2% | 12 | 22% | 20 | 7% |
| AFD or Watch List(1) | – | – | – | – | – | – | – | – | 17 | 31% | 17 | 6% |
| > 30 DPD | 2 | 6% | 13 | 8% | 2 | 8% | 15 | 8% | – | – | 17 | 6% |
| Other(2) | 7 | 23% | 67 | 43% | – | – | 67 | 37% | – | – | 74 | 28% |
| | 32 | 100% | 156 | 100% | 25 | 100% | 181 | 100% | 55 | 100% | 268 | 100% |

(1) Approaching Financial Difficulty (AFD) and Watch markers are early warning indicators of Business customers who may be approaching financial difficulties. If these indicators are not reversed, they may lead to a requirement for more proactive management by the Group.

(2) Other refers primarily to rules using additional credit reference agency data as well a number of smaller value drivers.

**Credit risk exposure and ECL, by internal PD rating, by IFRS 9 stage allocation**
The distribution of the Group's credit exposures and ECL by internal PD rating is analysed below:

| | | Stage 1 | | Stage 2 | | Stage 3[(1)] | | Total | |
|---|---|---|---|---|---|---|---|---|---|
| **2023** | | Lending £m | ECL £m | Lending £m | ECL £m | Lending £m | ECL £m | Lending £m | ECL £m |
| **Mortgages** | **PD range** | | | | | | | | |
| Strong | 0 – 0.74 | **52,612** | **8** | **1,355** | **2** | **–** | **–** | **53,967** | **10** |
| Good | 0.75 – 2.49 | **1,540** | **2** | **553** | **3** | **–** | **–** | **2,093** | **5** |
| Satisfactory | 2.50 – 99.99 | **388** | **3** | **796** | **22** | **–** | **–** | **1,184** | **25** |
| Default | 100 | **–** | **–** | **–** | **–** | **553** | **17** | **553** | **17** |
| **Total** | | **54,540** | **13** | **2,704** | **27** | **553** | **17** | **57,797** | **57** |
| **Unsecured** | | | | | | | | | |
| Strong | 0 – 2.49 | **4,443** | **29** | **123** | **12** | **–** | **–** | **4,566** | **41** |
| Good | 2.50 – 9.99 | **607** | **16** | **1,063** | **148** | **–** | **–** | **1,670** | **164** |
| Satisfactory | 10.00 – 99.99 | **6** | **1** | **456** | **162** | **–** | **–** | **462** | **163** |
| Default | 100 | **–** | **–** | **–** | **–** | **116** | **61** | **116** | **61** |
| **Total** | | **5,056** | **46** | **1,642** | **322** | **116** | **61** | **6,814** | **429** |
| **Business** | | | | | | | | | |
| Strong | 0 – 0.74 | **1,860** | **2** | **158** | **–** | **–** | **–** | **2,018** | **2** |
| Good | 0.75 – 9.99 | **4,360** | **27** | **1,441** | **30** | **–** | **–** | **5,801** | **57** |
| Satisfactory | 10.00 – 99.99 | **73** | **1** | **381** | **21** | **–** | **–** | **454** | **22** |
| Default | 100 | **–** | **–** | **–** | **–** | **411** | **50** | **411** | **50** |
| **Total** | | **6,293** | **30** | **1,980** | **51** | **411** | **50** | **8,684** | **131** |

(1) Stage 3 includes POCI for gross loans and advances of £48m for Mortgages and £1m for Unsecured (2022: £56m and £1m respectively); and ECL of (£1m) for Mortgages and (£1m) for Unsecured (2022: (£1m) and (£2m) respectively).

| | | Stage 1 | | Stage 2 | | Stage 3[(1)] | | Total | |
|---|---|---|---|---|---|---|---|---|---|
| **2022** | | Lending £m | ECL £m | Lending £m | ECL £m | Lending £m | ECL £m | Lending £m | ECL £m |
| **Mortgages** | **PD range** | | | | | | | | |
| Strong | 0 – 0.74 | 52,184 | 6 | 1,864 | 10 | – | – | 54,048 | 16 |
| Good | 0.75 – 2.49 | 2,302 | 2 | 641 | 5 | – | – | 2,943 | 7 |
| Satisfactory | 2.50 – 99.99 | 305 | 2 | 585 | 17 | – | – | 890 | 19 |
| Default | 100 | – | – | – | – | 583 | 14 | 583 | 14 |
| **Total** | | 54,791 | 10 | 3,090 | 32 | 583 | 14 | 58,464 | 56 |
| **Unsecured** | | | | | | | | | |
| Strong | 0 – 2.49 | 4,795 | 42 | 413 | 26 | – | – | 5,208 | 68 |
| Good | 2.50 – 9.99 | 524 | 20 | 459 | 72 | – | – | 983 | 92 |
| Satisfactory | 10.00 – 99.99 | 5 | 1 | 237 | 83 | – | – | 242 | 84 |
| Default | 100 | – | – | – | – | 80 | 40 | 80 | 40 |
| **Total** | | 5,324 | 63 | 1,109 | 181 | 80 | 40 | 6,513 | 284 |
| **Business** | | | | | | | | | |
| Strong | 0 – 0.74 | 4,808 | 5 | 719 | 17 | – | – | 5,527 | 22 |
| Good | 0.75 – 9.99 | 1,455 | 7 | 751 | 31 | – | – | 2,206 | 38 |
| Satisfactory | 10.00 – 99.99 | 7 | – | 56 | 7 | – | – | 63 | 7 |
| Default | 100 | – | – | – | – | 373 | 50 | 373 | 50 |
| **Total** | | 6,270 | 12 | 1,526 | 55 | 373 | 50 | 8,169 | 117 |

(1) Stage 3 includes POCI for gross loans and advances of £48m for Mortgages and £1m for Unsecured (2022: £56m and £1m respectively); and ECL of (£1m) for Mortgages and (£1m) for Unsecured (2022: (£1m) and (£2m) respectively).

In terms of the credit quality of the loan commitments and financial guarantee contracts, at least 90% classified as either 'Good' or 'Strong' under the Group's internal PD rating scale with the overall portfolio at 96% (2022: 97%) and the level of default remaining low.

The migration of business lending from the Strong to the Good PD grouping has been predominately driven by the updates to model economic scenarios (MES) received during the year, rather than an observed deterioration in the customer portfolio.

**IFRS 9 staging**

The following table shows the changes in the loss allowance and gross carrying value of the portfolios. Values are calculated using the individual customer account balances, and the stage allocation is taken as at the end of each month. The monthly position of each account is aggregated to report a net closing position for the period, thereby incorporating all movements an account has made during the year.

| | Stage 1 | | Stage 2 | | Stage 3(1) | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **2023** | Gross loans £m | ECL £m | Gross loans £m | ECL £m | Gross loans £m | ECL £m | Total gross loans £m | Total provisions £m | Income statement £m |
| **Opening balance at 1 October 2022** | **66,385** | **85** | **5,725** | **268** | **1,036** | **104** | **73,146** | **457** | |
| Transfers from Stage 1 to Stage 2 | **(8,561)** | **(46)** | **8,535** | **414** | **–** | **–** | **(26)** | **368** | **368** |
| Transfers from Stage 2 to Stage 1 | **6,077** | **16** | **(6,125)** | **(129)** | **–** | **–** | **(48)** | **(113)** | **(113)** |
| Transfers to Stage 3 | **(96)** | **–** | **(586)** | **(109)** | **686** | **138** | **4** | **29** | **29** |
| Transfers from Stage 3 | **121** | **–** | **134** | **8** | **(266)** | **(10)** | **(11)** | **(2)** | **(2)** |
| Net movement | **(2,459)** | **(30)** | **1,958** | **184** | **420** | **128** | **(81)** | **282** | **282** |
| Changes to model methodology | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** |
| New assets originated or purchased(2) | **20,489** | **57** | **629** | **44** | **161** | **34** | **21,279** | **135** | **135** |
| Repayments and other movements(3) | **(2,990)** | **12** | **(558)** | **(22)** | **140** | **(4)** | **(3,408)** | **(14)** | **(14)** |
| Repaid or derecognised(3) | **(15,536)** | **(35)** | **(1,428)** | **(74)** | **(490)** | **(127)** | **(17,454)** | **(236)** | **(236)** |
| Write-offs | **–** | **–** | **–** | **–** | **(187)** | **(187)** | **(187)** | **(187)** | **–** |
| Cash recoveries | **–** | **–** | **–** | **–** | **–** | **38** | **–** | **38** | **–** |
| Individually assessed impairment charge | **–** | **–** | **–** | **–** | **–** | **142** | **–** | **142** | **142** |
| **Closing balance at 30 September 2023** | **65,889** | **89** | **6,326** | **400** | **1,080** | **128** | **73,295** | **617** | **309** |

| | Stage 1 | | Stage 2 | | Stage 3(1) | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **2022** | Gross loans £m | ECL £m | Gross loans £m | ECL £m | Gross loans £m | ECL £m | Total gross loans £m | Total provisions £m | Income statement £m |
| **Opening balance at 1 October 2021** | 61,416 | 111 | 10,178 | 302 | 957 | 91 | 72,551 | 504 | |
| Transfers from Stage 1 to Stage 2 | (8,287) | (45) | 8,227 | 294 | – | – | (60) | 249 | 249 |
| Transfers from Stage 2 to Stage 1 | 10,218 | 27 | (10,282) | (145) | – | – | (64) | (118) | (118) |
| Transfers to Stage 3 | (91) | – | (562) | (84) | 650 | 101 | (3) | 17 | 17 |
| Transfers from Stage 3 | 42 | – | 137 | 8 | (187) | (12) | (8) | (4) | (4) |
| Net movement | 1,882 | (18) | (2,480) | 73 | 463 | 89 | (135) | 144 | 144 |
| Changes to model methodology | 443 | 1 | (442) | (8) | – | – | 1 | (7) | (7) |
| New assets originated or purchased(2) | 22,162 | 187 | 2,055 | 159 | 187 | 32 | 24,404 | 378 | 378 |
| Repayments and other movements(3) | (3,434) | (42) | (155) | (65) | 56 | (15) | (3,533) | (122) | (122) |
| Repaid or derecognised(3) | (16,084) | (154) | (3,431) | (193) | (498) | (101) | (20,013) | (448) | (448) |
| Write-offs | – | – | – | – | (129) | (129) | (129) | (129) | |
| Cash recoveries | – | – | – | – | – | 30 | – | 30 | |
| Individually assessed impairment charge | – | – | – | – | – | 107 | – | 107 | 107 |
| **Closing balance at 30 September 2022** | 66,385 | 85 | 5,725 | 268 | 1,036 | 104 | 73,146 | 457 | 52 |

(1) Stage 3 includes POCI for gross loans and advances of £48m for Mortgages and £1m for Unsecured (2022: £56m and £1m respectively), and ECL of (£1m) for Mortgages and (£1m) for Unsecured (2022: (£1m) and (£2m) respectively). Nil for Business in both periods.

(2) Includes assets where the term has ended, and a new facility has been provided.

(3) 'Repayments' comprises payments made on customer lending which are not yet fully paid at the reporting date and the customer arrangement remains live at that date. 'Repaid' refers to payments made on customer lending which is either fully repaid or derecognised by the reporting date and the customer arrangement is therefore closed at that date.

The IFRS 9 staging movements are driven by a variety of factors at individual product portfolio levels, with further detail provided in the following portfolio performance pages. Overall portfolio activity remains in line with expectations, with the net movements across staging slightly higher than prior year with gross flows in and out of Stage 2 the predominant movement. The increase in write offs has been primarily driven from the credit card portfolio in addition to a small number of individually significant business write offs. The levels of default across the portfolio remain low.

The contractual amount outstanding on loans and advances that were written off during the reporting period or are still subject to enforcement activity was £5.1m (2022: £4.3m). The Group has not purchased any lending assets in the year (2022: none). Further information on staging profile is provided at a portfolio level in the respective portfolio performance section on the following pages.

### Mortgage credit performance

The table below presents key information on the asset quality of the Group's Mortgage portfolio and should be read in conjunction with the supplementary data presented in the following pages of this section.

**Breakdown of Mortgage portfolio**

| 2023 | Gross lending £m | Modelled & IA ECL £m | MA £m | Total ECL £m | Net lending £m | Coverage % | Average LTV % |
|---|---|---|---|---|---|---|---|
| Residential – capital repayment | **35,085** | **10** | **5** | **15** | **35,070** | **0.04%** | **54.2%** |
| Residential – interest only | **7,503** | **8** | **1** | **9** | **7,494** | **0.12%** | **47.0%** |
| BTL | **15,209** | **7** | **26** | **33** | **15,176** | **0.21%** | **52.8%** |
| **Total Mortgage portfolio** | **57,797** | **25** | **32** | **57** | **57,740** | **0.10%** | **52.9%** |
| **2022** | | | | | | | |
| Residential – capital repayment | 36,417 | 13 | 5 | 18 | 36,399 | 0.05% | 54.2% |
| Residential – interest only | 7,041 | 3 | 1 | 4 | 7,037 | 0.05% | 45.4% |
| BTL | 15,006 | 6 | 28 | 34 | 14,972 | 0.22% | 52.4% |
| **Total Mortgage portfolio** | 58,464 | 22 | 34 | 56 | 58,408 | 0.09% | 52.7% |

Mortgage lending has reduced on a net basis to £57.8bn (2022: £58.5bn) with a reduced demand for new lending owing to the higher rate environment, stressed affordability pressure and wider cost of living considerations, being outpaced by repayments and redemptions.

The portfolio continues to evidence solid underlying credit performance, with the majority (98%) of lending not yet past due at the balance sheet date (2022: 98%), and 94% of loans held in Stage 1 (2022: 94%). A significant proportion of the portfolio is rated Strong or Good at the balance sheet date under the Group's internal PD rating scale (97%, consistent with 30 September 2022), and the volume and value of loans in forbearance has reduced to 3,801/£498m from 4,636/£640m, primarily due to customers successfully completing the forbearance reporting probation period and returning to fully performing status.

Stage 3 balances have remained low at 1.0% (2022: 1.0%) and 91% of the portfolio has an LTV of less than 75% (2022: 93%), with the weighted average LTV relatively stable through the year at 52.9% (2022: 52.7%). Further detail on LTV bandings and forbearance measures is provided on the following pages.

The selection of appropriate MAs is a major component in determining the Group's ECL, a detailed analysis of which is shown on page 45. Asset quality metrics for the BTL mortgage book remain robust, but the Group continues to hold a prudent level of provisioning for this customer cohort, with the related MA held stable at £25m (2022: £25m). A £5m MA for economic uncertainty was introduced during the year to reflect the economic circumstances and cost of living pressures such as rising interest rates and inflation which may impact customers. Other small MAs totalling £2m (2022: £4m) have been retained, taking total MAs held to £32m, down from £34m at 30 September 2022.

This has resulted in an impairment charge of £2m in the income statement (2022: credit of £30m) and associated cost of risk of nil bps (2022: (4)bps). The total book coverage has increased in the year to 10bps and is appropriate in the current environment where increased arrears and deterioration are expected to emerge in this portfolio.

**Mortgage Portfolio – interest rate profile**

| | 2023 | | 2022 | |
|---|---|---|---|---|
| | £m | % | £m | % |
| Fixed rate | **52,841** | **91.5%** | 53,387 | 91.3% |
| Variable rate | **3,081** | **5.3%** | 2,106 | 3.6% |
| Standard variable rate | **1,875** | **3.2%** | 2,971 | 5.1% |
| **Total** | **57,797** | **100.0%** | 58,464 | 100.0% |

The Group is a signatory to the government mortgage charter announced by the chancellor of the exchequer on 23 June 2023, to support regulated residential mortgage borrowers impacted by higher mortgage interest rates, in particular borrowers whose existing fixed rate deal is due to end in the immediate future.

During FY23 there has been a shift and increase in the volume of customers opening tracker mortgages as customers monitor the interest rate movements. The increase in interest rates has also driven a reduction in the volume of customers on the standard variable rate.

**Collateral**
The quality of the Group's Mortgage portfolio can be considered in terms of the average LTV of the portfolio and the staging of the portfolio, as set out in the following tables:

**Average LTV of Mortgage portfolio by staging**

| **2023** | Stage 1 | | | Stage 2 | | | Stage 3(2) | | | Total | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **LTV(1)** | Loans £m | % | ECL £m | Loans £m | % | ECL £m | Loans £m | % | ECL £m | Loans £m | % | ECL £m |
| Less than 50% | **22,680** | **42%** | **4** | **1,551** | **58%** | **5** | **282** | **50%** | **2** | **24,513** | **42%** | **11** |
| 50% to 75% | **26,913** | **49%** | **6** | **1,009** | **37%** | **14** | **203** | **37%** | **4** | **28,125** | **49%** | **24** |
| 76% to 80% | **2,270** | **4%** | **1** | **81** | **3%** | **2** | **22** | **4%** | **1** | **2,373** | **4%** | **4** |
| 81% to 85% | **1,408** | **3%** | **1** | **33** | **1%** | **1** | **13** | **2%** | **1** | **1,454** | **3%** | **3** |
| 86% to 90% | **992** | **2%** | **–** | **23** | **1%** | **–** | **9** | **2%** | **1** | **1,024** | **2%** | **1** |
| 91% to 95% | **236** | **–** | **–** | **3** | **–** | **–** | **11** | **2%** | **1** | **250** | **–** | **1** |
| 96% to 100% | **8** | **–** | **–** | **2** | **–** | **1** | **3** | **1%** | **–** | **13** | **–** | **1** |
| Greater than 100% | **33** | **–** | **1** | **2** | **–** | **4** | **10** | **2%** | **7** | **45** | **–** | **12** |
| | **54,540** | **100%** | **13** | **2,704** | **100%** | **27** | **553** | **100%** | **17** | **57,797** | **100%** | **57** |

| 2022 | Stage 1 | | | Stage 2 | | | Stage 3(2) | | | Total | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **LTV(1)** | Loans £m | % | ECL £m | Loans £m | % | ECL £m | Loans £m | % | ECL £m | Loans £m | % | ECL £m |
| Less than 50% | 23,069 | 43% | 2 | 1,659 | 54% | 3 | 288 | 49% | 2 | 25,016 | 43% | 7 |
| 50% to 75% | 27,452 | 50% | 5 | 1,270 | 41% | 19 | 242 | 42% | 2 | 28,964 | 50% | 26 |
| 76% to 80% | 2,412 | 4% | 1 | 103 | 3% | 3 | 17 | 3% | 1 | 2,532 | 4% | 5 |
| 81% to 85% | 1,108 | 2% | 1 | 26 | 1% | 1 | 11 | 2% | 1 | 1,145 | 2% | 3 |
| 86% to 90% | 547 | 1% | 1 | 25 | 1% | 1 | 6 | 1% | – | 578 | 1% | 2 |
| 91% to 95% | 154 | – | – | 4 | – | 1 | 8 | 1% | 1 | 166 | – | 2 |
| 96% to 100% | 16 | – | – | – | – | – | 3 | 1% | – | 19 | – | – |
| Greater than 100% | 33 | – | – | 3 | – | 4 | 8 | 1% | 7 | 44 | – | 11 |
| | 54,791 | 100% | 10 | 3,090 | 100% | 32 | 583 | 100% | 14 | 58,464 | 100% | 56 |

(1) LTV of the Mortgage portfolio is defined as Mortgage portfolio weighted by balance. The portfolio is indexed using the MIAC Acadametrics indices at a given date.
(2) Stage 3 includes £48m (2022: £56m) of POCI gross loans and advances and (£1m) ECL (2022: (£1m)).

The Mortgage portfolio remains highly secured with 91.1% of mortgages, by loan value, having an indexed LTV of less than 75% (2022: 92.3%), and an average portfolio LTV of 52.9% (2022: 52.7%). The total portfolio has reduced by 1.1% with the highest reduction in proportion and value in Stage 2.

### Forbearance

A key indicator of underlying Mortgage portfolio health is the level of loans subject to forbearance measures. Forbearance can occur when a customer experiences financial difficulty. In such circumstances, the Group considers the customer's individual circumstances, uses judgement in assessing whether there has been a SICR, or if an impairment or default event has occurred, and then applies tailored forbearance measures in order to support the customer in a route to stability. Customers may potentially be subject to more than one forbearance strategy at any one time where this is considered to be the most appropriate course of action.

The table below summarises the level of forbearance in respect of the Group's Mortgage portfolio at each balance sheet date. All balances subject to forbearance are classed as either Stage 2 or Stage 3 for ECL purposes.

| | Total loans and advances subject to forbearance measures | | | Impairment allowance on loans and advances subject to forbearance measures | |
|---|---|---|---|---|---|
| **2023** | Number of loans | Gross carrying amount £m | % of total portfolio | Impairment allowance £m | Coverage % |
| Formal arrangements | **1,027** | **134** | **0.24%** | **5.0** | **3.77%** |
| Temporary arrangements | **566** | **93** | **0.16%** | **4.5** | **4.82%** |
| Payment arrangement | **1,194** | **130** | **0.23%** | **1.4** | **1.09%** |
| Payment holiday | **362** | **45** | **0.08%** | **0.2** | **0.35%** |
| Interest only conversion | **460** | **76** | **0.13%** | **0.5** | **0.66%** |
| Term extension | **40** | **3** | **–** | **–** | **0.47%** |
| Other | **55** | **7** | **0.01%** | **0.3** | **3.69%** |
| Legal | **97** | **10** | **0.02%** | **0.3** | **2.83%** |
| **Total mortgage forbearance** | **3,801** | **498** | **0.87%** | **12.2** | **2.44%** |
| **2022** | | | | | |
| Formal arrangements | 1,145 | 137 | 0.23% | 8.6 | 6.23% |
| Temporary arrangements | 518 | 82 | 0.14% | 4.4 | 5.38% |
| Payment arrangement | 1,211 | 133 | 0.23% | 0.6 | 0.49% |
| Payment holiday | 381 | 47 | 0.08% | 0.1 | 0.27% |
| Interest only conversion | 1,193 | 225 | 0.39% | 0.8 | 0.35% |
| Term extension | 66 | 5 | 0.01% | – | 0.45% |
| Other | 14 | 1 | – | – | 0.92% |
| Legal | 108 | 10 | 0.02% | 0.3 | 2.42% |
| **Total mortgage forbearance** | 4,636 | 640 | 1.10% | 14.8 | 2.31% |

As at 30 September 2023, forbearance totalled £498m (3,801 loans), a decrease from the 30 September 2022 position of £640m (4,636 loans). This level represents 0.87% of total mortgage balances (2022: 1.10%), with the decrease primarily driven by customers successfully completing the forbearance reporting probation period and returning to fully performing status.

When all other avenues of resolution, including forbearance, have been explored, the Group will take steps to repossess and sell underlying collateral. In 2023, there were 55 repossessions of which 4 were voluntary (2022: 73 including 7 voluntary). The Group remains committed to supporting the customer and places good outcomes for them at the centre of this strategy.

**IFRS 9 staging**

The Group closely monitors the staging profile of the Mortgage portfolio over time, which can be indicative of general trends in book health. Movements in the staging profile of the portfolio are presented in the tables below.

| | Stage 1 | | Stage 2 | | Stage 3[1] | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **2023** | Gross loans £m | ECL £m | Gross loans £m | ECL £m | Gross loans £m | ECL £m | Total gross loans £m | Total provisions £m | Income statement £m |
| **Opening balance at 1 October 2022** | **54,791** | **10** | **3,090** | **32** | **583** | **14** | **58,464** | **56** | |
| Transfers from Stage 1 to Stage 2 | **(5,237)** | **(3)** | **5,203** | **63** | **–** | **–** | **(34)** | **60** | **60** |
| Transfers from Stage 2 to Stage 1 | **4,827** | **1** | **(4,852)** | **(49)** | **–** | **–** | **(25)** | **(48)** | **(48)** |
| Transfers to Stage 3 | **(58)** | **–** | **(273)** | **(5)** | **328** | **7** | **(3)** | **2** | **2** |
| Transfers from Stage 3 | **112** | **–** | **104** | **7** | **(222)** | **(3)** | **(6)** | **4** | **4** |
| Net movement | **(356)** | **(2)** | **182** | **16** | **106** | **4** | **(68)** | **18** | **18** |
| Changes to model methodology | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** |
| New assets originated or purchased[2] | **8,372** | **2** | **–** | **–** | **–** | **–** | **8,372** | **2** | **2** |
| Repayments and other movements[3] | **(2,366)** | **4** | **(99)** | **(15)** | **(9)** | **3** | **(2,474)** | **(8)** | **(8)** |
| Repaid or derecognised[3] | **(5,901)** | **(1)** | **(469)** | **(6)** | **(126)** | **(3)** | **(6,496)** | **(10)** | **(10)** |
| Write-offs | **–** | **–** | **–** | **–** | **(1)** | **(1)** | **(1)** | **(1)** | **–** |
| Cash recoveries | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** |
| Individually assessed impairment charge | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** |
| **Closing balance at 30 September 2023** | **54,540** | **13** | **2,704** | **27** | **553** | **17** | **57,797** | **57** | **2** |
| *of which:* | | | | | | | | | |
| *Residential – capital repayment* | **33,328** | **3** | **1,489** | **6** | **268** | **6** | **35,085** | **15** | |
| *Residential – interest only* | **6,651** | **1** | **657** | **2** | **195** | **6** | **7,503** | **9** | |
| *BTL* | **14,561** | **9** | **558** | **19** | **90** | **5** | **15,209** | **33** | |

| 2022 | Stage 1 Gross loans £m | Stage 1 ECL £m | Stage 2 Gross loans £m | Stage 2 ECL £m | Stage 3[(1)] Gross loans £m | Stage 3[(1)] ECL £m | Total gross loans £m | Total provisions £m | Income statement £m |
|---|---|---|---|---|---|---|---|---|---|
| **Opening balance at 1 October 2021** | 50,596 | 4 | 7,192 | 64 | 653 | 19 | 58,441 | 87 | |
| Transfers from Stage 1 to Stage 2 | (5,854) | (1) | 5,821 | 55 | – | – | (33) | 54 | 54 |
| Transfers from Stage 2 to Stage 1 | 8,820 | 3 | (8,851) | (55) | – | – | (31) | (52) | (52) |
| Transfers to Stage 3 | (49) | – | (191) | (5) | 238 | 4 | (2) | (1) | (1) |
| Transfers from Stage 3 | 29 | – | 108 | 5 | (140) | (3) | (3) | 2 | 2 |
| Net movement | 2,946 | 2 | (3,113) | – | 98 | 1 | (69) | 3 | 3 |
| Changes to model methodology | – | – | – | – | – | – | – | – | – |
| New assets originated or purchased[(2)] | 9,971 | 1 | 7 | – | 1 | – | 9,979 | 1 | 1 |
| Repayments and other movements[(3)] | (2,484) | (4) | (154) | (23) | (26) | (3) | (2,664) | (22) | (22) |
| Repaid or derecognised[(3)] | (6,238) | (1) | (842) | (9) | (142) | (2) | (7,222) | (12) | (12) |
| Write-offs | – | – | – | – | (1) | (1) | (1) | (1) | |
| Cash recoveries | – | – | – | – | – | – | – | – | – |
| Individually assessed impairment charge | – | – | – | – | – | – | – | – | – |
| **Closing balance at 30 September 2022** | 54,791 | 10 | 3,090 | 32 | 583 | 14 | 58,464 | 56 | (30) |
| *of which:* | | | | | | | | | |
| *Residential – capital repayment* | 34,396 | 7 | 1,650 | 4 | 371 | 7 | 36,417 | 18 | |
| *Residential – interest only* | 6,063 | 2 | 838 | 1 | 140 | 1 | 7,041 | 4 | |
| *BTL* | 14,332 | 1 | 602 | 27 | 72 | 6 | 15,006 | 34 | |

(1) Stage 3 includes POCI for gross loans and advances of £48m (2022: £56m) and ECL of (£1m) (2022: (£1m)).

(2) Includes assets where the term has ended, and a new facility has been provided.

(3) ‘Repayments’ comprises payments made on customer lending that are not yet fully paid at the reporting date and the customer arrangement remains live at that date. ‘Repaid’ refers to payments made on customer lending, which is either fully repaid or derecognised by the reporting date and the customer arrangement is therefore closed at that date.

The Mortgage portfolio continues to evidence strong performance with levels of delinquency and impairment remaining relatively low.

The level of mortgage lending classed as Stage 1 increased from 93.7% in 2022 to 94.3%, with a decrease of assets in Stage 2 from 5.3% to 4.7%. Within the Stage 2 category, 89% of balances are not yet past due at the balance sheet date (2022: 89%). The proportion of mortgages classified as Stage 3 remains modest at 1.0% (2022: 1.0%). The net movements across the stages show reductions, primarily in the Stage 2 and 3 portfolios, driven by a wide variety of factors, but broadly they are all successful outcomes in either restoring customers to fully performing or resuming satisfactory repayment schedules, as the Group is committed to the delivery of good customer outcomes.

Mortgage lending classed as ‘Strong’ has increased modestly to 93.4% from 92.4% at 30 September 2022, with over 97% (2022: 97%) of the Mortgage portfolio classed as ‘Good’ or ‘Strong.’ The sustained quality in the internal PD ratings and high quality of collateral underpinning the book are key factors supporting the provision coverage of 10bps (2022: 7bps).

## Unsecured credit performance

The table below presents key information important for understanding the asset quality of the Group’s Unsecured lending portfolio and should be read in conjunction with the supplementary data presented in the following pages of this section.

### Breakdown of Unsecured credit portfolio

| 2023 | Gross lending £m | Modelled ECL £m | MA £m | Total ECL £m | Net lending £m | Coverage % |
|---|---|---|---|---|---|---|
| Credit cards | **6,088** | **364** | **28** | **392** | **5,696** | **6.88%** |
| Personal loans | **699** | **32** | **1** | **33** | **666** | **4.59%** |
| Overdrafts | **27** | **4** | **–** | **4** | **23** | **11.62%** |
| **Total Unsecured lending portfolio** | **6,814** | **400** | **29** | **429** | **6,385** | **6.65%** |
| **2022** | | | | | | |
| Credit cards | 5,558 | 216 | 30 | 246 | 5,312 | 4.81% |
| Personal loans | 925 | 32 | 2 | 34 | 891 | 3.57% |
| Overdrafts | 30 | 4 | – | 4 | 26 | 12.57% |
| **Total Unsecured lending portfolio** | 6,513 | 252 | 32 | 284 | 6,229 | 4.66% |

Unsecured gross lending balances have increased to £6.8bn (2022: £6.5bn) with underlying growth in the credit card portfolio the primary driver, slightly offset by the personal loan portfolio which continues to contract in line with expectations.

Credit card lending increased circa 10% in the year reflecting resilient demand from existing customers and ongoing new credit card sales as the Group market share steadily grew to circa 8.5% of balances. During the period, in line with the downturn in the broader UK economy, we have seen a migration of customers from Stage 1 to Stage 2 with the value of lending in Stage 2 increasing to £1,321m (2022: £774m). However the proportion of lending in Stage 1 and Stage 2 not past due remains high at 97.2% (2022: 97.5%).

The level of forbearance concessions agreed in the unsecured portfolio, particularly in credit cards, has increased in line with portfolio arrears, driven by continued portfolio maturation, VMs diversification strategy and the wider economic environment.

The impact of the current macroeconomic scenarios together with a weakening of credit bureau data and early-stage arrears compared to prior year has led to an increase in modelled ECL. This increase in ECL resulted in book coverage increasing to 688bps (2022: 481bps). The value of credit cards written off, net of recoveries, increased to £116m (2022: £79m).

The personal loan portfolio continues to reduce on a managed basis.

The selection of appropriate MAs is a major component in determining the Group's ECL, a detailed analysis of key factors on them is shown on page 45.

Taking the modelled ECL and MA together, the total ECL provision held as at 30 September 2023 is £429m (30 September 2022: £284m), which, in addition to a net write off impairment charge of £124m, results in a total impairment charge of £269m (30 September 2022: £178m).

Total book coverage of 665bps has increased from 466bps as at 30 September 2022. The increased coverage is appropriate in the current environment where increased arrears and deterioration are expected to emerge in this portfolio.

**Forbearance**

The table below summarises the level of forbearance in respect of the Group's Unsecured lending portfolios at each balance sheet date. All balances subject to forbearance are classed as either Stage 2 or Stage 3 for ECL purposes.

| | Total loans and advances subject to forbearance measures | | | Impairment allowance on loans and advances subject to forbearance measures | |
|---|---|---|---|---|---|
| **2023** | Number of loans | Gross carrying amount £m | % of total portfolio | Impairment allowance £m | Coverage % |
| Credit cards arrangements | **22,206** | **90** | **1.56%** | **41.7** | **46.13%** |
| Loans arrangements | **467** | **2** | **0.51%** | **0.8** | **40.30%** |
| Overdraft arrangement | **24** | **–** | **0.02%** | **–** | **11.98%** |
| **Total Unsecured lending forbearance** | **22,697** | **92** | **1.42%** | **42.5** | **46.00%** |
| **2022** | | | | | |
| Credit cards arrangements | 15,872 | 62 | 1.19% | 24.3 | 39.47% |
| Loans arrangements | 638 | 3 | 0.56% | 1.4 | 40.33% |
| Overdraft arrangement | 56 | – | 0.04% | – | 30.76% |
| **Total Unsecured lending forbearance** | 16,566 | 65 | 1.12% | 25.7 | 39.51% |

The volume and value of forbearance has increased, notably on the credit card portfolio, where the Group looks to agree concessions and payment arrangements which are in the best interest of the customers in order to maximise their ability to repay the lending and return to fully performing status.

Forbearance on the Loan and Overdraft portfolios remain modest and in line with the reducing size of the portfolios. The level of impairment coverage on the Unsecured portfolio has increased to 46.0% (2022: 39.5%) primarily as a result of the updated PD and other MES model inputs.

### IFRS 9 staging

The Group closely monitors the staging profile of its Unsecured lending portfolio over time, which can be indicative of general trends in book health. Movements in the staging profile of the portfolio are presented in the tables below.

| 2023 | Stage 1 Gross loans £m | Stage 1 ECL £m | Stage 2 Gross loans £m | Stage 2 ECL £m | Stage 3(1) Gross loans £m | Stage 3(1) ECL £m | Total gross loans £m | Total provisions £m | Income statement £m |
|---|---|---|---|---|---|---|---|---|---|
| **Opening balance at 1 October 2022** | **5,324** | **63** | **1,109** | **181** | **80** | **40** | **6,513** | **284** | |
| Transfers from Stage 1 to Stage 2 | **(1,621)** | **(39)** | **1,642** | **320** | **–** | **–** | **21** | **281** | **281** |
| Transfers from Stage 2 to Stage 1 | **590** | **13** | **(608)** | **(69)** | **–** | **–** | **(18)** | **(56)** | **(56)** |
| Transfers to Stage 3 | **(15)** | **–** | **(179)** | **(100)** | **200** | **121** | **6** | **21** | **21** |
| Transfers from Stage 3 | **–** | **–** | **1** | **–** | **(5)** | **(5)** | **(4)** | **(5)** | **(5)** |
| Net movement | **(1,046)** | **(26)** | **856** | **151** | **195** | **116** | **5** | **241** | **241** |
| Changes to model methodology | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** |
| New assets originated or purchased(2) | **1,101** | **12** | **1** | **–** | **2** | **2** | **1,104** | **14** | **14** |
| Repayments and other movements(3) | **(97)** | **–** | **(282)** | **2** | **152** | **(6)** | **(227)** | **(4)** | **(4)** |
| Repaid or derecognised(3) | **(226)** | **(3)** | **(42)** | **(12)** | **(152)** | **(91)** | **(420)** | **(106)** | **(106)** |
| Write-offs | **–** | **–** | **–** | **–** | **(161)** | **(161)** | **(161)** | **(161)** | **–** |
| Cash recoveries | **–** | **–** | **–** | **–** | **–** | **37** | **–** | **37** | **–** |
| Individually assessed impairment charge | **–** | **–** | **–** | **–** | **–** | **124** | **–** | **124** | **124** |
| **Closing balance at 30 September 2023** | **5,056** | **46** | **1,642** | **322** | **116** | **61** | **6,814** | **429** | **269** |

| 2022 | Stage 1 Gross loans £m | Stage 1 ECL £m | Stage 2 Gross loans £m | Stage 2 ECL £m | Stage 3(1) Gross loans £m | Stage 3(1) ECL £m | Total gross loans £m | Total provisions £m | Income statement £m |
|---|---|---|---|---|---|---|---|---|---|
| **Opening balance at 1 October 2021** | 5,148 | 41 | 553 | 118 | 69 | 35 | 5,770 | 194 | |
| Transfers from Stage 1 to Stage 2 | (1,051) | (31) | 1,059 | 210 | – | – | 8 | 179 | 179 |
| Transfers from Stage 2 to Stage 1 | 504 | 16 | (523) | (62) | – | – | (19) | (46) | (46) |
| Transfers to Stage 3 | (19) | – | (116) | (69) | 139 | 83 | 4 | 14 | 14 |
| Transfers from Stage 3 | 1 | – | 2 | 1 | (8) | (7) | (5) | (6) | (6) |
| Net movement | (565) | (15) | 422 | 80 | 131 | 76 | (12) | 141 | 141 |
| Changes to model methodology | – | – | – | – | – | – | – | – | – |
| New assets originated or purchased(2) | 1,708 | 20 | 11 | 4 | 7 | 5 | 1,726 | 29 | 29 |
| Repayments and other movements(3) | (508) | 26 | 166 | (8) | 104 | (4) | (238) | 14 | 14 |
| Repaid or derecognised(3) | (459) | (9) | (43) | (13) | (117) | (72) | (619) | (94) | (94) |
| Write-offs | – | – | – | – | (114) | (114) | (114) | (114) | |
| Cash recoveries | – | – | – | – | – | 26 | – | 26 | |
| Individually assessed impairment charge | – | – | – | – | – | 88 | – | 88 | 88 |
| **Closing balance at 30 September 2022** | 5,324 | 63 | 1,109 | 181 | 80 | 40 | 6,513 | 284 | 178 |

(1) Stage 3 includes POCI for gross loans and advances of £1m (2022: £1m) and ECL of (£2m) (2022: (£2m)).

(2) Includes assets where the term has ended, and a new facility has been provided.

(3) 'Repayments' comprises payments made on customer lending, which are not yet fully paid at the reporting date and the customer arrangement remains live at that date. 'Repaid' refers to payments made on customer lending, which is either fully repaid or derecognised by the reporting date and the customer arrangement is therefore closed at that date.

The individually assessed impairment charge increase from last year is within expectations as the underlying portfolio has deteriorated, in line with the backdrop of a downturn in the broader UK economy. The level of post write off recoveries has increased proportionately and remains robust.

The total ECL held on balance sheet has increased from £284m to £429m with an increase in the modelled ECL being the primary driver. Modelled provision coverage alone is now 589bps (2022: 413bps).

The credit card portfolio is the primary driver of the decrease in the balance of Unsecured lending classed as Stage 1 to 74.2% (2022: 81.8%), with a corresponding increase in assets in Stage 2 from 17.0% to 24.1%. Within the Stage 2 category, 95.4% is not yet past due (2022: 94.7%) but falls into this classification due predominantly to PD deterioration rather than actual delinquency. The proportion classified as Stage 3 increased to 1.7% (2022: 1.2%). The total provision coverage has therefore increased to 665bps (2022: 466bps).

### Business credit performance

The table below presents key information on the asset quality of the Group's Business lending portfolio and should be read in conjunction with the supplementary data presented in the following pages of this section.

**Breakdown of Business credit portfolio**

| 2023 | Gross lending £m | Government(1) £m | Total gross £m | Modelled & IA ECL £m | MA £m | Total ECL £m | Net lending £m | Coverage(2) % |
|---|---|---|---|---|---|---|---|---|
| Agriculture | **1,315** | **46** | **1,361** | **4** | **1** | **5** | **1,356** | **0.35%** |
| Business services | **1,153** | **212** | **1,365** | **38** | **3** | **41** | **1,324** | **3.45%** |
| Commercial Real Estate | **715** | **4** | **719** | **5** | **1** | **6** | **713** | **0.72%** |
| Government, health and education | **1,200** | **38** | **1,238** | **9** | **2** | **11** | **1,227** | **0.85%** |
| Hospitality | **779** | **60** | **839** | **3** | **1** | **4** | **835** | **0.50%** |
| Manufacturing | **669** | **77** | **746** | **17** | **3** | **20** | **726** | **2.87%** |
| Resources | **160** | **5** | **165** | **2** | **–** | **2** | **163** | **1.65%** |
| Retail and wholesale trade | **758** | **145** | **903** | **19** | **2** | **21** | **882** | **2.72%** |
| Transport and storage | **290** | **32** | **322** | **4** | **–** | **4** | **318** | **1.47%** |
| Other | **877** | **149** | **1,026** | **15** | **2** | **17** | **1,009** | **1.87%** |
| **Total Business portfolio** | **7,916** | **768** | **8,684** | **116** | **15** | **131** | **8,553** | **1.60%** |
| **2022** | | | | | | | | |
| Agriculture | 1,392 | 66 | 1,458 | 5 | 1 | 6 | 1,452 | 0.45% |
| Business services | 980 | 286 | 1,266 | 22 | 3 | 25 | 1,241 | 2.53% |
| Commercial Real Estate | 597 | 10 | 607 | 3 | – | 3 | 604 | 0.54% |
| Government, health and education | 1,008 | 54 | 1,062 | 8 | 2 | 10 | 1,052 | 0.95% |
| Hospitality | 652 | 78 | 730 | 4 | 1 | 5 | 725 | 0.80% |
| Manufacturing | 640 | 109 | 749 | 23 | 3 | 26 | 723 | 3.96% |
| Resources | 133 | 8 | 141 | 3 | 1 | 4 | 137 | 2.37% |
| Retail and wholesale trade | 696 | 198 | 894 | 15 | 3 | 18 | 876 | 2.38% |
| Transport and storage | 291 | 56 | 347 | 4 | 1 | 5 | 342 | 1.44% |
| Other | 723 | 192 | 915 | 12 | 3 | 15 | 900 | 2.03% |
| **Total Business portfolio** | 7,112 | 1,057 | 8,169 | 99 | 18 | 117 | 8,052 | 1.59% |

(1) Government includes all lending provided to business customers under UK Government schemes including Bounce back loan scheme (BBLS), Coronavirus business interruption loan scheme (CBILS), Coronavirus large business interruption loan scheme (CLBILS) and Recovery loan scheme (RLS). This excludes £143m (2022: £66m) of guarantee claim funds received from British Business Bank (BBB).

(2) Coverage ratio excludes the guaranteed element of government-backed loan schemes

Gross Business lending increased to £8.7bn (2022: £8.2bn). The government-guaranteed lending portfolio continues to reduce as borrowers repay balances. Growth remains targeted to sectors and sub sectors where we have well established expertise. The sector mix remained stable with lending to the agriculture, business services and government, health and education sectors continuing to account for almost half of the total book, at 46% (2022: 46%)

Whilst there is some weakening in the pre and early delinquency metrics being monitored, there has been no significant deterioration in asset quality metrics across the portfolio and, as yet, no significant increase in specific provision recognition. Coverage for certain sectors has reduced in the period as previously held provisions have been utilised. A range of external risks have remained prevalent throughout the period including general inflationary pressures, interest rate rises, ongoing supply chain distribution and labour market disruption, as well as wider geopolitical risks.

The proportion of loans in Stage 1 has reduced to 72.5% (2022: 76.7%) with a corresponding increase in the proportion of loans in Stage 2 at 22.8% (2022: 18.7%). Within the Stage 2 category, 98.5% is not past due (2022: 98.2%) and 90% remain rated as 'Strong' or 'Good' (2022: 95%) under the Group's internal PD rating scale. Stage 3 loans remain modest at 4.7% (2022: 4.6%).

The updated MES is the primary driver of a net £17m increase in modelled provisions to £116m. Whilst there have been no material signs of stress across the portfolio, there has been an uptick in corporate insolvencies across the UK market, therefore an economic resilience MA of £15m has been retained. A new Business LGD model was brought into use in the Business ECL calculation during the year. The impact of this had been estimated during development, resulting in a negative MA of £15m being held last year, this has now been fully released. The MA composition is covered in more detail on the page 45. The specific provisions held on balance sheet have reduced to £25m (2022: £31m) primarily due to provision utilisation. This results in an overall provision of £131m (2022: £117m) and an impairment charge of £38m (2022: credit of £96m).

Overall, portfolio coverage remains prudent at 160bps (2022: 159bps), reflecting the quality of the portfolio and little evidence of deterioration in asset quality to date.

**Forbearance**
Forbearance is considered to exist where customers are experiencing, or are about to experience financial difficulty, and the Group grants a concession on a non-commercial basis. The Group reports business forbearance at a customer level and at a value which incorporates all facilities and the related impairment allowance, irrespective of whether each individual facility is subject to forbearance. Authority to grant forbearance measures for business customers is held by the Group's Strategic Business Services unit and is exercised, where appropriate, based on detailed consideration of the customer's financial position and prospects.

Where a customer is part of a larger group, forbearance is exercised and reported across the Group at the individual entity level. Where modification of the terms and conditions of an exposure meeting the criteria for classification as forbearance results in derecognition of loans and advances from the balance sheet and the recognition of a new exposure, the new exposure will be treated as forborne.

The tables below summarise the total number of arrangements in place and the loan balances and impairment provisions associated with those arrangements. All balances subject to forbearance are classed as either Stage 2 or Stage 3 for ECL purposes.

| | Total loans and advances subject to forbearance measures | | | Impairment allowance on loans and advances subject to forbearance measures | |
|---|---|---|---|---|---|
| **2023** | Number of loans | Gross carrying amount £m | % of total portfolio | Impairment allowance £m | Coverage % |
| Term extension | **150** | **112** | **1.22%** | **7.9** | **7.08%** |
| Payment holiday | **88** | **204** | **2.21%** | **30.3** | **14.91%** |
| Reduction in contracted interest rate | **1** | **–** | **–** | **–** | **–** |
| Alternative forms of payment | **–** | **–** | **–** | **–** | **–** |
| Debt forgiveness | **4** | **1** | **0.01%** | **0.4** | **47.66%** |
| Refinancing | **8** | **2** | **0.02%** | **0.0** | **1.85%** |
| Covenant breach/reset/waiver | **40** | **174** | **1.89%** | **6.4** | **3.65%** |
| **Total Business forbearance** | **291** | **493** | **5.35%** | **45.0** | **9.14%** |

| | Total loans and advances subject to forbearance measures | | | Impairment allowance on loans and advances subject to forbearance measures | |
|---|---|---|---|---|---|
| **2022** | Number of loans | Gross carrying amount £m | % of total portfolio | Impairment allowance £m | Coverage % |
| Term extension | 154 | 118 | 1.36% | 4.9 | 4.18% |
| Payment holiday | 81 | 193 | 2.23% | 32.6 | 16.86% |
| Reduction in contracted interest rate | 2 | 1 | 0.01% | – | 1.33% |
| Alternative forms of payment | – | – | – | – | – |
| Debt forgiveness | 2 | 1 | 0.01% | 0.5 | 97.05% |
| Refinancing | 9 | 2 | 0.02% | 0.1 | 5.14% |
| Covenant breach/reset/waiver | 41 | 133 | 1.53% | 5.4 | 4.03% |
| **Total Business forbearance** | 289 | 448 | 5.16% | 43.5 | 9.71% |

The number of Business customers reported in receipt of forbearance concessions has remained relatively stable at 291 (2022: 289) with the total customer lending increasing to £493m (2022: £448m). Whilst the forbearance concession may only be applied to one account in the customer's portfolio, in the disclosure above the customer's full lending portfolio is included. Forbearance remains a key support measure for customers in, or about to, experience financial difficulty, and the ability to agree a temporary concession on a non-commercial basis can often be the critical breathing room required to support a return to fully performing status. 13% of forborne customers met exit criteria and returned to performing status in the financial year. Therefore, most forbearance arrangements relate to term extensions allowing customers a longer term to repay obligations in full than initially contracted. As a percentage of the Business portfolio, forborne balances have increased to 5.35% (2022: 5.16%) with impairment coverage slightly reducing 9.14% (2022: 9.71%).

Customers within the forbearance portfolio have £29m of COVID-19 related support loans: £14m CBIL, £4m BBL and £11m RLS.

The table includes a portfolio of financial assets at fair value. The gross value of fair value loans subject to forbearance is £0.5m (2022: £4.7m), representing 0.01% of the total business portfolio (2022: 0.05%). The credit risk adjustment on these amounts is now immaterial. (2022: £0.1m).

### IFRS 9 staging

The Group closely monitors the staging profile of its Business lending portfolio over time, which can be indicative of general trends in book health. Movements in the staging profile of the portfolio in the current and prior year are presented in the tables below.

| | Stage 1 | | Stage 2 | | Stage 3(3) | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **2023** | Gross loans £m | ECL £m | Gross loans £m | ECL £m | Gross loans £m | ECL £m | Total gross loans £m | Total provisions £m | Income statement £m |
| **Opening balance at 1 October 2022** | 6,270 | 12 | 1,526 | 55 | 373 | 50 | 8,169 | 117 | |
| Transfers from Stage 1 to Stage 2 | (1,703) | (4) | 1,689 | 31 | – | – | (14) | 27 | 27 |
| Transfers from Stage 2 to Stage 1 | 659 | 1 | (666) | (11) | – | – | (7) | (10) | (10) |
| Transfers to Stage 3 | (23) | – | (134) | (4) | 158 | 10 | 1 | 6 | 6 |
| Transfers from Stage 3 | 8 | – | 30 | – | (40) | (2) | (2) | (2) | (2) |
| Net movement | (1,059) | (3) | 919 | 16 | 118 | 8 | (22) | 21 | 21 |
| Changes to model methodology | – | – | – | – | – | – | – | – | – |
| New assets originated or purchased(1) | 11,017 | 43 | 627 | 44 | 159 | 32 | 11,803 | 119 | 119 |
| Repayments and other movements(2) | (526) | 8 | (174) | (8) | (1) | (1) | (701) | (1) | (1) |
| Repaid or derecognised(2) | (9,409) | (30) | (918) | (56) | (213) | (33) | (10,540) | (119) | (119) |
| Write-offs | – | – | – | – | (25) | (25) | (25) | (25) | – |
| Cash recoveries | – | – | – | – | – | 1 | – | 1 | – |
| Individually assessed impairment charge | – | – | – | – | – | 18 | – | 18 | 18 |
| **Closing balance at 30 September 2023** | 6,293 | 30 | 1,980 | 51 | 411 | 50 | 8,684 | 131 | 38 |

| | Stage 1 | | Stage 2 | | Stage 3(3) | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **2022** | Gross loans £m | ECL £m | Gross loans £m | ECL £m | Gross loans £m | ECL £m | Total gross loans £m | Total provisions(4) £m | Income statement £m |
| **Opening balance at 1 October 2021** | 5,672 | 66 | 2,433 | 120 | 235 | 37 | 8,340 | 223 | |
| Transfers from Stage 1 to Stage 2 | (1,382) | (13) | 1,347 | 29 | – | – | (35) | 16 | 16 |
| Transfers from Stage 2 to Stage 1 | 894 | 8 | (908) | (28) | – | – | (14) | (20) | (20) |
| Transfers to Stage 3 | (23) | – | (255) | (10) | 273 | 14 | (5) | 4 | 4 |
| Transfers from Stage 3 | 12 | – | 28 | 2 | (39) | (2) | 1 | – | – |
| Net movement | (499) | (5) | 212 | (7) | 234 | 12 | (53) | – | – |
| Changes to model methodology | 443 | 1 | (443) | (8) | – | – | – | (7) | – |
| New assets originated or purchased(1) | 10,483 | 166 | 2,037 | 155 | 179 | 27 | 12,699 | 348 | 348 |
| Repayments and other movements(2) | (442) | (72) | (167) | (34) | (22) | (8) | (631) | (114) | (114) |
| Repaid or derecognised(2) | (9,387) | (144) | (2,546) | (171) | (239) | (27) | (12,172) | (342) | (342) |
| Write-offs | – | – | – | – | (14) | (14) | (14) | (14) | |
| Cash recoveries | – | – | – | – | – | 4 | – | 4 | |
| Individually assessed impairment charge | – | – | – | – | – | 19 | – | 19 | 19 |
| **Closing balance at 30 September 2022** | 6,270 | 12 | 1,526 | 55 | 373 | 50 | 8,169 | 117 | (89) |

(1) Includes assets where the term has ended, and a new facility has been provided.

(2) 'Repayments' comprises payments made on customer lending which are not yet fully paid at the reporting date and the customer arrangement remains live at that date. 'Repaid' refers to payments made on customer lending which is either fully repaid or derecognised by the reporting date and the customer arrangement is therefore closed at that date.

(3) This excludes £143m (2022: £66m) of guarantee claim funds received from British Business Bank.

The level of Business lending classed as Stage 1 has decreased to 72.5% (2022: 76.8%), with a corresponding increase in Stage 2 to 22.8% (2022: 18.7%), primarily driven by the revised MES inputs.

The majority (98.5%) of the portfolio in Stage 2 is not past due and is primarily in this category due to the updated MES inputs and PD deterioration in addition to proactive management measures such as early intervention, heightened monitoring, and forbearance concessions. Stage 3 loans have remained relatively stable at 4.7% (2022: 4.6%) and are predominantly Bounce Back Loans.

The proportion of assets classed as 'Strong' has decreased to 23% (2022: 68%) primarily due to the MES and PD changes although the proportion classed as 'Strong' or 'Good' remains robust at 90% (2022: 95%).

**Business collateral**
The following table shows collateral held at 30 September 2023. The exposure amount shown is net of credit provisions that have some form of associated collateral and is not the total exposure for each asset class as this is disclosed elsewhere in the credit risk report.

A change was made this year where all collateral values captured have now been capped at the exposure value, which impacts the previously uncapped Other Physical Collateral & Receivables columns.

We have also included Immovable Property collateral this year, as an enhancement to last year's table content.

| 2023 | Property £m | Cash £m | Guarantee £m | Netting £m | Debt securities £m | Other physical collateral £m | Receivables £m | Total £m | Exposure £m |
|---|---|---|---|---|---|---|---|---|---|
| Financial assets at amortised cost | | | | | | | | | |
| Loans and advances to customers | **5,072** | **11** | **760** | **169** | **–** | **567** | **334** | **6,913** | **7,514** |
| *Of which: Default* | **61** | **–** | **182** | **–** | **–** | **–** | **17** | **260** | **267** |

| 2022 | Property £m | Cash £m | Guarantee £m | Netting £m | Debt securities £m | Other physical collateral £m | Receivables £m | Total £m | Exposure £m |
|---|---|---|---|---|---|---|---|---|---|
| Financial assets at amortised cost | | | | | | | | | |
| Loans and advances to customers | 4,843 | 7 | 970 | 237 | – | 432 | 379 | 6,868 | 7,399 |
| *Of which: Default* | 65 | – | 127 | – | – | 1 | 7 | 200 | 211 |

Lending backed by government guarantees in response to COVID-19 are included within the Guarantee column.

## Other credit risks

### Offsetting of financial assets and liabilities

The table below presents information on recognised financial assets and financial liabilities that are offset on the balance sheet under IAS 32, as well as those that are subject to master netting or similar arrangements, irrespective of whether they are offset.

The Group reduces exposure to credit risk through central clearing for eligible derivatives, and daily posting of cash collateral on such transactions as detailed in note 3.1.3.2 to the financial statements. The amounts offset on the balance sheet, as shown below, mainly represent derivatives and variation margin collateral with central clearing houses, which meet the criteria for offsetting under IAS 32.

The Group enters into derivatives and repurchase agreements with various counterparties, which are governed by industry-standard master netting agreements. The Group holds and provides collateral in respect of transactions covered by these agreements. The right to offset balances under these master netting agreements only arises in the event of non-payment or default and, as a result, these arrangements do not qualify for offsetting under IAS 32.

Collateral amounts included in the table below are limited to the net balance sheet exposure in order to exclude any over collateralisation. The table excludes financial instruments not subject to offset and that are formally subject to collateral arrangements (e.g. loans and advances). The net amounts presented in the table are not intended to represent the Group's exposure to credit risk, as the Group will use a wide range of strategies to mitigate credit risk in addition to netting and collateral.

| | | | | Net amounts not offset on balance sheet | | |
|---|---|---|---|---|---|---|
| **2023** | Gross amounts before offset £m | Gross amounts offset on balance sheet £m | Net amounts presented on balance sheet £m | Subject to master netting agreements £m | Cash collateral Pledged/ received[2] £m | Net amount £m |
| Derivative assets | **2,606** | **(2,471)** | **135** | **(26)** | **(81)** | **28** |
| Derivative liabilities | **(1,643)** | **1,353** | **(290)** | **26** | **62** | **(202)** |
| Net position[1] | **963** | **(1,118)** | **(155)** | **–** | **(19)** | **(174)** |
| Repurchase agreements | **(552)** | **–** | **(552)** | **552** | **–** | **–** |
| **2022** | | | | | | |
| Derivative assets | 3,340 | (2,998) | 342 | (46) | (182) | 114 |
| Derivative liabilities | (1,797) | 1,469 | (328) | 46 | 32 | (250) |
| Net position[1] | 1,543 | (1,529) | 14 | – | (150) | (136) |
| Repurchase agreements | (703) | – | (703) | 703 | – | – |

(1) The net position is offset against variation margin cash collateral with central clearing houses included within other assets or other liabilities.

(2) Cash collateral amounts not offset under IAS 32 in respect of derivatives with other banks are included within due from and due to other banks. Variation margin cash collateral amounts not offset under IAS 32 in respect of derivatives with central clearing houses are included within other assets and other liabilities.

## Macroeconomic assumptions, scenarios, and weightings

The Group's ECL allowance at 30 September 2023 was £617m (2022: £457m).

### Macroeconomic assumptions

The Group engages Oxford Economics to provide a wide range of future macroeconomic assumptions, which are used in the scenarios over the five-year forecast period, reflecting the best estimate of future conditions under each scenario outcome. The macroeconomic assumptions were provided by Oxford Economics on 1 September 2023 and changes in macroeconomic assumptions between 1 September 2023 and 30 September 2023 have been considered as part of the MAs. The Group has identified the following key macroeconomic drivers as the most significant inputs for IFRS 9 modelling purposes: UK GDP growth, inflation, house prices, base rates, and unemployment rates. The external data provided is assessed and reviewed on a quarterly basis to ensure appropriateness and relevance to the ECL calculation, with more frequent updates provided as and when the circumstances require them. Further adjustments supplement the modelled output when it is considered that not all the risks identified in a product segment have been accurately reflected within the models, or for other situations where it is not possible to provide a modelled outcome.

With UK core inflation remaining stubbornly high and wage inflation causing concern in the Monetary Policy Committee, the Bank of England base rate has been raised to its highest level since before the Global Financial Crisis. Although it is expected that the base rate has now peaked, the impact of the rapid rise in interest rates will not be fully felt until mortgage customers on fixed rate products, that predate the rate rises, remortgage. This will extend the ongoing cost of living crisis for some time to come.

Against this backdrop the Group has continued to assess the possible IFRS 9 economic scenarios to select appropriate forecasts and weightings. The selection of scenarios and the appropriate weighting to use in the IFRS 9 models are considered, debated and decided by ALCO and the Audit Committee. The three scenarios selected, together with the weightings applied, have been updated to reflect the current economic environment and are:

| **Scenario** | 2023 (%) | 2022 (%) |
|---|---|---|
| Upside | **10** | 10 |
| Base | **55** | 55 |
| Downside | **35** | 35 |

The Group continue to select three scenarios, with the largest weighting applied to the base scenario. The weightings mirror those applied in 2022, while there is a shift in the downside scenario to a less severe option. This is a reflection of the view that, while there is continuing economic upheaval from the cumulative effects of Brexit, the COVID-19 pandemic and Russia's invasion of Ukraine, the peak of inflation is in the past and the Bank of England base rate is unlikely to climb much higher as inflation begins the long journey back to the Bank of England's target rate of 2%, leaving the path forward somewhat clearer.

The key macroeconomic assumptions used in the scenarios:

| | Base (55%) | Upside (10%) | Downside (35%) |
|---|---|---|---|
| **GDP** | • Growth limited to sub 1% in all quarters until Q2 2025, but recession is avoided<br>• Overall year-on-year growth in 2024 forecast at 0.4% with a modest recovery in 2025 of 1.5%<br>• GDP increases to 2.3% in 2026 before falling back to 1.5% in 2027 | • Growth of 2.9% in Q1 2024 contributes to year-on-year growth of 3.0% in 2024<br>• Overall year-on-year growth in 2025 is forecast to fall slightly to 2.6% before climbing back to 3.0% in 2026<br>• GDP falls back to 1.6% in 2027, moving towards the long run average forecast | • Negative GDP for six consecutive quarters, from Q4 2023, (1.6%), until Q1 2025, (0.5%) resulting in total contraction of 4.1%<br>• Growth remains sluggish over the remaining forecast period, only recovering to pre-contraction levels in Q3 2027, with annual growth of 1.6% |
| **Inflation** | • Having peaked at 10.8% in Q4 2022, inflation falls back to 4.6% by Q4 2023<br>• Remains persistently above the BoE's 2% target throughout 2024 at 3.2%<br>• In Q2 2025 inflation falls below the 2% target and remains so for the remainder of the forecast | • Having peaked at 10.8% in Q4 2022, inflation falls to 4.9% in Q4 2023<br>• Reverts back to sub 2.0% levels from Q3 2025 for the remainder of the forecast period, going as low as 0.9% in Q2 2026 rising to 1.8% by Q4 2027 | • Having peaked at 10.8% in Q4 2022 before declining to 4.1% in Q4 2023<br>• Inflation continues to fall rapidly, dropping below 2% in Q2 2024 to a low of 0% in Q3 2025<br>• From Q4 2025 inflation rises steadily each quarter reaching 1.7% in Q3 2027 |
| **Base rate** | • BoE base rate hits 5.5% in Q4 2023 and remains at that level until Q3 2024<br>• From then on the rate falls steadily at around 0.25% per quarter over the forecast period to 2.1% by Q4 2027 | • BoE base rate continues to rise, peaking at 6.5% in Q2 2024<br>• The rate begins to fall in Q1 2025 and falls steadily by 0.25% per quarter thereafter to 3.6% by Q4 2027 | • BoE base rate peaks at 5.2% in Q3 2023 before falling back in Q4 2023<br>• The rate falls steadily at 0.25% per quarter from Q2 2024 to Q3 2027, tapering to 1.25% in Q4 2027 |
| **HPI** | • Shows steady decline, reaching a low point in Q3 2025 before rebounding slowly in each quarter after this until the end of the forecast period<br>• Overall Q4 v Q4 year-on-year negative growth of 2.7% in 2023, 7.2% in 2024 and 2.9% in 2025<br>• Growth in the outer years recovers the value lost since Q3 2023 by the end of 2027 | • With the exception of Q4 2023, HPI falls in each quarter until Q2 2025 before reversing and rising in each subsequent quarter<br>• Overall, HPI sees Q4 v Q4 negative growth of 1.3% in 2023, 4.8% in 2024 and 0.9% in 2025<br>• Returns to positive growth of 6.6% in 2026 and 7.0% in 2027 | • Falls steadily and deeply from Q1 2023 to Q2 2026 followed by modest increases in each quarter until the end of the forecast period<br>• Overall, HPI sees a Q4 v Q4 negative growth of 4.7% in 2023, 12.7% in 2024 and 7.6% in 2025<br>• Modest growth in 2026 of 1.0% followed by 7.5% in 2027 leaves house prices well below the levels seen at the start of the forecast |
| **Unemployment** | • Peaks at 4.6% in Q3 2024 and remains there through Q4 2024<br>• From then, the rate falls back to 3.9% in Q2 2026 where it remains through the remainder of the forecast period | • Peaks in Q3 2023, at 4.3%, before falling back in the following quarter<br>• From then, the rate slowly falls back to 3.7% by Q2 2026, where it remains | • Peaks at 7.0% in Q1 2026 and remains there throughout 2026<br>• From Q1 2027 the unemployment rate begins to fall slowly, closing the year at 6.7% |

**Base case – 2023 v 2022(1)**

The following table shows how the Group's base case assumptions in the current year have changed from those used at 30 September 2022:

| Year | Assumption | 2022 % | 2023 % | 2024 % | 2025 % | 2026 % | 2027 % |
|---|---|---|---|---|---|---|---|
| 30 September 2023 | Base rate | | 4.7 | 5.4 | 4.5 | 3.5 | 2.5 |
| | Unemployment | | 4.2 | 4.5 | 4.3 | 3.9 | 3.9 |
| | GDP | | 0.5 | 0.4 | 1.5 | 2.3 | 1.5 |
| | Inflation | | 7.6 | 3.2 | 1.5 | 1.0 | 1.7 |
| | HPI | | (2.7) | (7.2) | (2.9) | 4.6 | 7.1 |
| 30 September 2022 | Base rate | 1.4 | 2.2 | 1.8 | 1.8 | 1.7 | |
| | Unemployment | 3.9 | 4.6 | 4.4 | 3.8 | 3.8 | |
| | GDP | 3.6 | 0.3 | 2.1 | 2.7 | 2.1 | |
| | Inflation | 9.4 | 7.5 | 0.6 | 0.7 | 1.5 | |
| | HPI | 6.8 | (4.6) | (3.0) | 4.4 | 6.7 | |

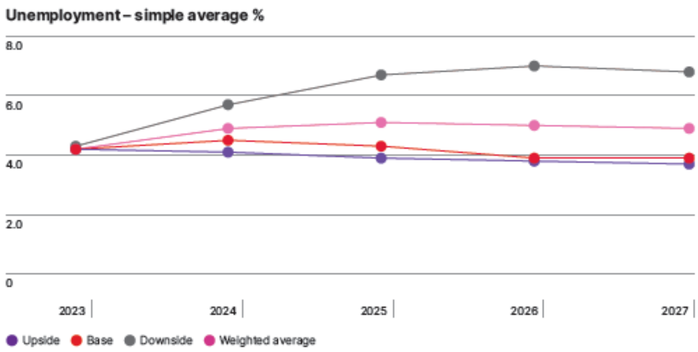
(1) Macroeconomic assumptions provided by Oxford Economics on 1 September 2023 and reported on a calendar year basis unless otherwise stated. The changes in macroeconomic assumptions between 1 September 2023 and 30 September 2023 have been considered as part of the MAs.

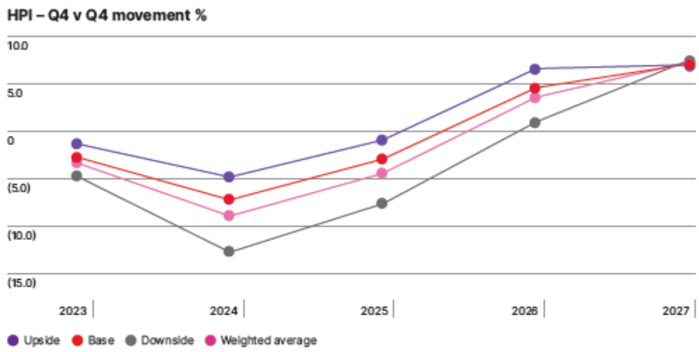
The base case macroeconomic estimates and assumptions used at 30 September 2022 reflected the forward-looking view at that time, which recognised the impact of the ongoing war in Ukraine on global fuel costs, which had triggered a spike in UK inflation of over 10% for the first time in decades. The effect was exacerbated by the autumn budget, and the wider impact of the war on global food prices in 2023. Core inflation has remained stubbornly high, compared to the previous forecast, forcing interest rates higher for longer as the Bank of England look to bring inflation back to their long-term target, prolonging the cost of living crisis.

**Five-year simple averages for the most sensitive inputs of unemployment, GDP and HPI**

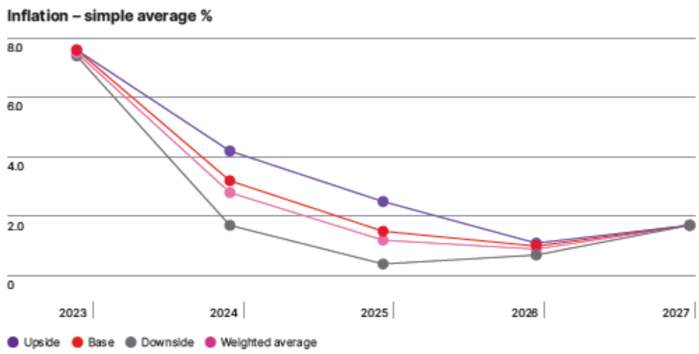
| 2023 | Unemployment % | GDP % | HPI % |
|---|---|---|---|
| Upside | **3.9** | **2.2** | **1.3** |
| Base | **4.2** | **1.2** | **(0.2)** |
| Downside | **6.1** | **0.2** | **(3.3)** |
| **2022** | | | |
| Upside | 3.9 | 3.1 | 3.3 |
| Base | 4.1 | 2.1 | 2.0 |
| Downside | 6.3 | 0.4 | (3.4) |

**Graphical illustrations of the above key inputs over the five-year forecast period are:**








The full range of the key macroeconomic assumptions is included in the table on page 46.

## The use of estimates, judgements and sensitivity analysis

The following are the main areas where estimates and judgements are applied to the ECL calculation:

### The use of estimates

**Asset lifetimes**

The calculation of the ECL allowance is dependent on the expected life of the Group's portfolios. The Group assumes the remaining contract term as the maximum period to consider credit losses wherever possible. For the Group's credit card and overdraft portfolios, behavioural factors such as observed retention rates and other portfolio level assumptions are taken into consideration in determining the estimated asset life.

**Economic scenarios**

The calculation of the Group's impairment provision is sensitive to changes in the chosen weightings as highlighted above. The effect on the closing modelled provision of each portfolio as a result of applying a 100% weighting to each of the selected scenarios is shown below:

| **2023** | Probability Weighted[(1)] £m | Upside £m | Base £m | Downside £m |
|---|---|---|---|---|
| Mortgages | **20** | **17** | **18** | **24** |
| Unsecured of which: | **399** | **382** | **382** | **433** |
| *Cards* | **364** | **352[(3)]** | **350** | **391** |
| *Personal loans and overdrafts[(2)]* | **35** | **30** | **32** | **42** |
| Business[(2)] | **91** | **81** | **86** | **107** |
| **Total** | **510** | **480** | **486** | **564** |

| **2022** | Probability Weighted £m | Upside £m | Base £m | Downside £m |
|---|---|---|---|---|
| Mortgages | 15 | 12 | 13 | 23 |
| Unsecured of which: | 251 | 236 | 237 | 279 |
| *Cards* | 216 | 209[(3)] | 208 | 233 |
| *Personal loans and overdrafts[(2)]* | 35 | 27 | 29 | 46 |
| Business[(2)] | 53 | 39 | 43 | 97 |
| **Total** | 319 | 287 | 293 | 399 |

(1) In addition to the probability weighted modelled provision shown in the table, the Group holds £76m relative to MAs (2022: £85m) and £30m of individually assessed provision (2022: £38m).

(2) Salary Finance contributes more that 50% of the combined Personal Loans and overdrafts ECL.

(3) Due to a minor model interaction effect, the 100% ECL for Upside is marginally higher than the Base case.

One of the criteria for moving exposures between stages is the lifetime PD which incorporates macroeconomic factors. As a result, the stage allocation will be different in each scenario and so the probability weighted ECL cannot be recalculated using the scenario ECL provided and the scenario weightings.

Certain asset classes are less sensitive to specific macroeconomic factors, showing lower relative levels of sensitivity. To ensure appropriate levels of ECL, the relative lack of sensitivity is compensated for through the application of MAs, further detail of which can be found on page 45.

Within each portfolio, the following are the macroeconomic inputs that are more sensitive, and therefore more likely to drive the move from Stage 1 to Stage 2 under a stress scenario:

- Mortgages: Unemployment and HPI
- Unsecured: Unemployment
- Business: Unemployment and HPI

In addition to assessing the ECL impact of applying a 100% weighting to each of the three chosen scenarios, the Group has also considered the effect changes to key economic inputs would make to the modelled ECL output.

The Group considers the unemployment rate and HPI as the inputs that would have the most significant impact on ECL and has assessed how these metrics would change ECL across the relevant portfolios, with the reported output assessed against the base case. All changes have been implemented as immediate effects within the first year of the base case scenario, persisting throughout the scenario.

The following table discloses the ECL impact of a 10% increase and decrease in HPI on the Group's Mortgage and Business lending:

| | 2023 £m | 2022 £m |
|---|---|---|
| Mortgages +10% | **(2)** | (1) |
| Business +10% | **(1)** | (1) |
| Mortgages -10% | **2** | 2 |
| Business -10% | **2** | 2 |

Unemployment is a key input that affects all of the Group's lending categories and the following table highlights the ECL impact of a one percent change in the unemployment rate:

| | 2023 £m | 2022 £m |
|---|---|---|
| Mortgages +1% | **1** | 1 |
| Unsecured +1% | **21** | 15 |
| Business +1% | **4** | 4 |
| Mortgages -1% | **(1)** | (1) |
| Unsecured -1% | **(21)** | (15) |
| Business -1% | **(3)** | (3) |

While the above sensitivities provide a view of how the ECL would be impacted based on these single changes, such changes would not ordinarily occur in isolation and the economic inputs used are linked within each chosen scenario.

**The use of judgement**
**SICR**
Judgement is required in determining the point at which a SICR has occurred, as it is the point at which a 12-month ECL is replaced by a lifetime ECL. The Group has developed a series of triggers that indicate where a SICR has occurred when assessing exposures for the risk of default occurring at each reporting date compared to the risk at origination. There is no single factor that influences this decision, rather a combination of different criteria that enables the Group to make an assessment based on the quantitative and qualitative information available. This assessment includes the impact of forward-looking macroeconomic factors but excludes the existence of any collateral implications.

Indicators of a SICR include deterioration of the residual lifetime PD by set thresholds that are unique to each product portfolio, non-default forbearance programmes, and watch list status. The Group adopts the backstop position that a SICR will have taken place when the financial asset reaches 30 DPD.

The Group does not have a set absolute threshold by which the PD would have to increase by, in establishing that a SICR has occurred, and has implemented an approach with the required SICR threshold trigger varying on a portfolio and product basis according to the origination PD.

The table below illustrates this approach with reference to the Group's Mortgage, Unsecured (credit cards) and Business portfolios. In each case the illustration is of the PD threshold based on a five year full lifetime PD (not the annualised equivalent). The business example reflects the thresholds appropriate for term lending.

| | | Origination PD | SICR Trigger |
|---|---|---|---|
| Mortgages | Low origination lifetime PD | 2.00% | 5.69% |
| | High origination lifetime PD | 10.00% | 17.69% |
| Credit cards | Low origination lifetime PD | 2.00% | 22.34% |
| | High origination lifetime PD | 10.00% | 25.52% |
| Business | Low origination lifetime PD | 2.00% | 6.03% |
| | High origination lifetime PD | 10.00% | 16.70% |

Changes to the overall SICR thresholds can also impact staging, driving accounts into higher stages with the resultant impact on the ECL allowance:

| | 2023 £m | 2022 £m |
|---|---|---|
| A 10% movement in the mortgage portfolio from Stage 1 to Stage 2 | **+13** | +9 |
| A 10% movement in the credit card portfolio from Stage 1 to Stage 2 | **+89** | +87 |
| A 10% movement in the business portfolio from Stage 1 to Stage 2 | **+10** | +18 |
| A PD stress which increases PDs upwards by 20% for all portfolios | **+131** | +106 |

**Definition of default**
The PD of a credit exposure is a key input to the measurement of the ECL allowance. Default under Stage 3 occurs when there is evidence that a customer is experiencing significant financial difficulty, which is likely to affect the ability to repay amounts due.

**MAs**
At 30 September 2023, £76m of MAs (30 September 2022: £85m) are included within the total ECL provision of £617m (30 September 2022: £457m).

These are management judgements which impact the ECL provision by increasing (or decreasing) the collectively assessed modelled output where not all of the known risks identified in a particular product segment have been reflected within the models. This also takes into account any time lag between the date the macroeconomic assumptions were received and the reporting date.

The impact of these judgemental adjustments and how they impact the Group's total reported ECL allowance and coverage ratio for each portfolio is:

| **2023**[(1)] | Mortgages £m | Unsecured £m | Business £m | Total £m |
|---|---|---|---|---|
| ECL before judgemental adjustments (A) | **25.2** | **400.2** | **115.5** | **540.9** |
| Judgemental adjustments: | | | | |
| *To address the cost-of-living crisis* | **—** | **—** | **—** | **—** |
| *To address economic resilience* | **5.0** | **—** | **15.0** | **20.0** |
| *Impact of new LGD model* | **—** | **—** | **—** | **—** |
| *Additional buy-to-let impact* | **25.1** | **—** | **—** | **25.1** |
| *Other credit card adjustments* | **—** | **27.5** | **—** | **27.5** |
| *Other judgemental adjustments* | **1.7** | **1.3** | **0.5** | **3.5** |
| Total judgemental adjustments (B) | **31.8** | **28.8** | **15.5** | **76.1** |
| Total reported ECL (A + B) | **57.0** | **429.0** | **131.0** | **617.0** |
| *% of total ECL (B / total reported ECL)* | **56%** | **7%** | **12%** | **12%** |
| *Coverage – total* | **0.10%** | **6.65%** | **1.60%** | **0.84%** |
| *Coverage – total ex MAs* | **0.04%** | **5.87%** | **1.33%** | **0.74%** |

| 2022[(1)] | Mortgages £m | Unsecured £m | Business £m | Total £m |
|---|---|---|---|---|
| ECL before judgemental adjustments (A) | 21.6 | 251.5 | 99.0 | 372.1 |
| Judgemental adjustments: | | | | |
| *To address the cost-of-living crisis* | 6.3 | 20.2 | — | 26.5 |
| *To address economic resilience* | — | — | 30.0 | 30.0 |
| *Impact of new LGD model* | — | — | (15.4) | (15.4) |
| *Additional buy-to-let impact* | 25.1 | — | — | 25.1 |
| *Other credit card adjustments* | — | 10.5 | — | 10.5 |
| *Other judgemental adjustments* | 2.8 | 1.8 | 3.3 | 7.9 |
| Total judgemental adjustments (B) | 34.2 | 32.5 | 17.9 | 84.6 |
| Total reported ECL (A + B) | 55.8 | 284.0 | 116.9 | 456.7 |
| *% of total ECL (B / total reported ECL)* | 61% | 11% | 15% | 19% |
| *Coverage – total* | 0.09% | 4.66% | 1.59% | 0.62% |
| *Coverage – total ex MAs* | 0.02% | 4.13% | 0.93% | 0.45% |

(1) The impact of rounding means that the combination of the probability weighted total and individually assessed provision may not fully align to the portfolio sections.

The Group assesses and reviews the need for and quantification of MAs on a quarterly basis, with the CFO recommending the level of MAs to the Boards Audit Committee twice a year at each external reporting period.

In the absence of significant events that might impact ECLs going forward, the Group expects the current level of MAs to materially reduce over the next 18-24 months.

**Macroeconomic assumptions**
Annual macroeconomic assumptions used over the five-year forecast period in the scenarios and their weighted averages are as follows:[(1)]

**2023**

| Scenario | VMUK weighting | Economic measure[(2)] | 2023 % | 2024 % | 2025 % | 2026 % | 2027 % |
|---|---|---|---|---|---|---|---|
| Upside | 10% | Base rate | **4.8** | **6.5** | **6.0** | **5.0** | **4.0** |
| | | Unemployment | **4.2** | **4.1** | **3.9** | **3.8** | **3.7** |
| | | GDP | **0.8** | **3.0** | **2.6** | **3.0** | **1.6** |
| | | Inflation | **7.6** | **4.2** | **2.5** | **1.1** | **1.7** |
| | | HPI | **(1.3)** | **(4.8)** | **(0.9)** | **6.6** | **7.0** |
| Base | 55% | Base rate | **4.7** | **5.4** | **4.5** | **3.5** | **2.5** |
| | | Unemployment | **4.2** | **4.5** | **4.3** | **3.9** | **3.9** |
| | | GDP | **0.5** | **0.4** | **1.5** | **2.3** | **1.5** |
| | | Inflation | **7.6** | **3.2** | **1.5** | **1.0** | **1.7** |
| | | HPI | **(2.7)** | **(7.2)** | **(2.9)** | **4.6** | **7.1** |
| Downside | 35% | Base rate | **4.6** | **4.5** | **3.5** | **2.5** | **1.6** |
| | | Unemployment | **4.3** | **5.7** | **6.7** | **7.0** | **6.8** |
| | | GDP | **(0.1)** | **(3.3)** | **0.7** | **1.9** | **1.6** |
| | | Inflation | **7.4** | **1.7** | **0.4** | **0.7** | **1.7** |
| | | HPI | **(4.7)** | **(12.7)** | **(7.6)** | **1.0** | **7.5** |
| Weighted average | | Base rate | **4.7** | **5.2** | **4.3** | **3.3** | **2.3** |
| | | Unemployment | **4.2** | **4.9** | **5.1** | **5.0** | **4.9** |
| | | GDP | **0.3** | **(0.6)** | **1.3** | **2.2** | **1.6** |
| | | Inflation | **7.5** | **2.8** | **1.2** | **0.9** | **1.7** |
| | | HPI | **(3.3)** | **(8.9)** | **(4.4)** | **3.6** | **7.3** |

(1) Macroeconomic assumptions provided by Oxford Economics on 1 September 2023 and reported on a calendar year basis unless otherwise stated. The changes in macroeconomic assumptions between 1 September 2023 and 30 September 2023 have been considered as part of the MAs.

(2) The percentages shown for base rate, unemployment and inflation are averages. GDP is the year-on-year movement, with HPI the Q4 v Q4 movement.

**2022**

| Scenario | VMUK weighting | Economic measure[2] | 2022 % | 2023 % | 2024 % | 2025 % | 2026 % |
|---|---|---|---|---|---|---|---|
| Upside | 10% | Base rate | 1.4 | 3.0 | 2.5 | 2.3 | 2.3 |
| | | Unemployment | 3.8 | 4.2 | 4.0 | 3.7 | 3.6 |
| | | GDP | 3.9 | 2.8 | 3.2 | 3.4 | 2.1 |
| | | Inflation | 9.5 | 8.5 | 1.8 | 0.7 | 1.3 |
| | | HPI | 8.3 | (2.3) | (1.8) | 5.7 | 6.5 |
| Base | 55% | Base rate | 1.4 | 2.2 | 1.8 | 1.8 | 1.7 |
| | | Unemployment | 3.9 | 4.6 | 4.4 | 3.8 | 3.8 |
| | | GDP | 3.6 | 0.3 | 2.1 | 2.7 | 2.1 |
| | | Inflation | 9.4 | 7.5 | 0.6 | 0.7 | 1.5 |
| | | HPI | 6.8 | (4.6) | (3.0) | 4.4 | 6.7 |
| Downside | 35% | Base rate | 1.3 | 1.7 | 0.6 | 0.5 | 0.5 |
| | | Unemployment | 4.0 | 6.0 | 7.1 | 7.3 | 7.1 |
| | | GDP | 2.6 | (5.6) | 0.8 | 2.1 | 2.1 |
| | | Inflation | 9.3 | 5.0 | (1.0) | 0.7 | 1.5 |
| | | HPI | 3.5 | (13.3) | (11.6) | (2.7) | 7.4 |
| Weighted average | | Base rate | 1.4 | 2.1 | 1.4 | 1.4 | 1.4 |
| | | Unemployment | 3.9 | 5.0 | 5.3 | 5.0 | 4.9 |
| | | GDP | 3.3 | (1.5) | 1.7 | 2.5 | 2.1 |
| | | Inflation | 9.4 | 6.7 | 0.2 | 0.7 | 1.5 |
| | | HPI | 5.8 | (7.4) | (5.9) | 2.0 | 6.9 |

(2) The percentages shown for base rate, unemployment and inflation are averages. GDP is the year-on-year movement, with HPI the Q4 v Q4 movement.

## Strong foundations supporting resilience and growth.

**The financial risk framework underpins the Group's robust balance sheet, ensuring strategy is resilient and responsive to external pressures and changing regulatory obligations.**

Financial risk covers several categories of risk which impact the way in which the Group can support its customers in a safe and sound manner. They include capital risk, funding risk, liquidity risk, market risk and pension risk.

### Risk appetite

The primary objective for the management of financial risks is to control the risk profile within approved risk limits to maintain the confidence of the Group's customers and other stakeholders. Financial risks are also managed to protect current and future earnings from the impact of market volatility. The Group applies a prudent approach to financial risks in order to safeguard the ongoing strength and resilience of the balance sheet. These activities are undertaken in a manner consistent with the Group's obligations under ring-fencing legislation and prudential rules.

Financial risk appetite is approved by the Board, with authority delegated to ALCO for subsequent implementation and monitoring. The Board has established a range of capital risk appetite measures including CET1, leverage and MREL. Measures for funding and liquidity risks consider the structure of the balance sheet, the Group's overall funding profile and compliance with the regulatory LCR and net stable funding ratio (NSFR) requirements. Board-approved risk appetite covers both regulatory and internal liquidity requirements and the need to maintain access to liquidity resources sufficient to accommodate outflows of funds in a range of stress scenarios and time periods.

The Group participates in wholesale markets and uses financial instruments to fund its banking activities and manage the liquidity and market risks arising from these activities. The Group establishes an appetite for these risks based on an overriding principle that the Group will not engage in proprietary risk taking.

The Group's pension risk appetite is a component of the Group-wide RAS framework for the management of balance sheet risks and is considered in the context of potential capital impacts as a result of volatility in the Scheme's valuations and future contributions.

### Capital risk

Capital is held by the Group to cover inherent risks in a normal and stressed operating environment, to protect unsecured creditors and investors and to support the Group's strategy of sustainable growth. Capital risk is the risk that the Group has or forecasts insufficient capital and other loss-absorbing debt instruments to operate effectively. This includes meeting minimum regulatory requirements, operating within Board approved risk appetite and supporting its strategic goals.

#### Mitigation

The Group's capital risk policy provides the framework for the management of capital within the Group. The objectives of the policy are to efficiently and sustainably manage the capital base to optimise shareholder returns while maintaining capital adequacy and ensuring that excessive leverage is not taken, so meeting regulatory requirements and managing the rating agencies' assessments of the Group.

The Group is able to accumulate additional capital through retention of profit over time, which may be increased by: income growth and cost cutting; raising new equity, for example via a rights issue; reducing or cancelling distributions on capital instruments; and raising AT1 and Tier 2 capital. The availability and cost of additional capital is dependent upon market conditions and perceptions at the time. The Group is also able to manage the demands for capital through management actions including adjusting its lending strategy.

Capital optimisation remains a key strategic priority, ensuring the Group manages the quantity and quality of resources efficiently while meeting internal targets, stress testing requirements and maintaining regulatory compliance.

#### Measurement

The Group manages capital in accordance with prudential rules issued by the PRA and the FCA. Pillar 1 capital requirements are calculated in respect of credit risk, operational risk, market risk, counterparty credit risk and credit valuation adjustments. The capital requirements for credit risk are calculated using the following approaches:

- Retail mortgages: IRB.
- Business lending: FIRB.
- Specialised lending: IRB slotting.
- All other portfolios: Standardised approach, via either sequential IRB implementation or Permanent Partial Use.

A rigorous approach is taken to assessing risks that are not adequately covered by Pillar 1. The Group also undertakes analysis of a range of stress scenarios to test the impact on capital arising from severe yet plausible scenarios. These approaches to capital are documented in the Group's ICAAP which is subject to review, challenge and approval by the Board. The outputs from the ICAAP and regulatory stress testing are used to inform minimum capital targets and risk appetite, ensuring survivability above peak-to-trough stress movements.

The Group IRB framework looks at the customer PD along with loss severity (EAD and LGD). The outputs are used in the calculation of RWA, expected loss and IFRS 9 ECL. The IRB parameters and rating assessments are actively embedded in the following day-to-day processes:

- Credit approval – IRB models and parameters are used to assess the customer risk and outputs are used to inform cut-off models that drive the lending decisions.
- Pricing – Outputs and estimates are used in the assessment of new products and portfolio pricing reviews.
- Risk appetite – Parameters are included in the assessment of models and are analysed to inform the Group's risk capacity and appetite.
- Asset quality – Parameters are monitored to understand the product and segment performance of the Group's portfolios.

**Monitoring**

The Board approves the capital risk appetite annually, defining minimum levels of capital across a range of capital ratios and measurements. The internal appetite ensures the Group operates above minimum regulatory requirements with reporting conducted through ALCO, Board and Executive Risk Committee. The capital plan, which assesses capital adequacy on a forward-looking basis, is also approved by the Board annually. The annual planning process is supported by rolling forecasting which is reported to ALCO monthly. This ensures that performance trends are reviewed and that there is transparency of the impact on capital ratios, risk appetite and the outlook. As part of the monthly forecasting process, ALCO reviews scenario analysis, considering adverse impacts to economic conditions and modelling sensitivities, including changes to regulation. These processes all support the Group's management of capital and informs the CET1 target operating range of 13.0%-13.5%.

In recent years, the PRA has also taken a thematic interest in the quality of regulatory reporting across the industry, specifically focusing on the completeness, accuracy and timing of regulatory reports. This has resulted in a number of s166 Skilled Person Reviews being commissioned over the governance, controls and processes supporting the regulatory reporting framework. The Group has been subject to such a review and, although no material issues were highlighted, is working on improvements to aspects of its governance and control framework.

**Regulatory capital developments**

The regulatory landscape for capital is subject to a number of changes, some of which can lead to uncertainty on eventual outcomes. In order to mitigate this risk, the Group actively monitors emerging regulatory change, assesses the impact and puts plans in place to respond.

**Designation as an O-SII**

On 29 November 2022 the PRA formally designated the Group as an Other Systemically Important Institution (O-SII). This is not expected to have a material impact on the Group's capital framework and is not currently required to hold a related capital buffer. As part of the O-SII designation the Group will need to comply with BCBS 239 over a three-year period.

**IRB model changes**

Following the BoE's announcements in 2020 regarding supervisory and prudential policy measures to address the challenges of COVID-19, the requirements relating to compliance with updates to definition of default and mortgage IRB models were extended. The Group will apply the relevant models after PRA approval and we currently expect models to be implemented in 2024.

Ahead of the Group's implementation of mortgage IRB models (including hybrid PD), a model adjustment has been applied to increase RWAs and expected losses in advance of formal approval of models (see RWA movement commentary on page 52). There has been little movement in this adjustment since the Interim Financial Report was published.

**Basel 3.1**

Following the publication of final reforms to the Basel III framework in December 2017, the PRA published CP16/22 at the end of November 2022, covering its consultation on the UK implementation of these reforms. There are a number of key amendments to the standardised approaches to credit and operational risks together with the introduction of a new standardised RWA output floor, the latter of which will be introduced gradually over a transition period. There are also amendments to IRB approaches, Credit Valuation Adjustments (CVAs), Credit Risk Mitigation rules and associated reporting and disclosure requirements. Estimates of the impact of these reforms on the Group indicate they will have no material day one impact on the capital position, with no constraint from the output floor expected until late in the transition period. Since the publication of CP16/22, the PRA has stated the intention to issue 'near final' rules and policy on Operational Risk, Counterparty Credit Risk (CCR), CVA Risk and Market Risk in Quarter 4 of 2023 with the remaining elements of Credit Risk, Output Floor and Reporting and Disclosure requirements to be published in Q2 2024. Further, the PRA has advised the implementation date of the final Basel 3.1 policies will be pushed back by six months to 1 July 2025, however the transitional period will be reduced to four and a half years to ensure full implementation is achieved by 1 January 2030.

**Pillar 2A**

As part of its Basel 3.1 proposals, the PRA announced its intention to review its Pillar 2A methodologies more fully by 2024. This review could have an impact on the Group which will be assessed when the proposals are published.

**Contingent leverage**

The PRA published PS 5/23 - Risks from Contingent Leverage in May 2023. The Group is not considered to carry material contingent leverage risk however we have reviewed and updated our policies and processes where relevant. Activity is also ongoing to support new reporting requirements in 2024.

**Solvency Stress Test and Annual Cyclical Scenarios**

The Group completed the 2022 ACS exercise in Q2 FY23. The scenario tested the resilience of the UK Banking system to deep simultaneous recessions in the UK and global economies, real income shocks, large falls in asset prices and higher global interest rates, as well as a separate stress of conduct costs. The BoE published results in July 2023, with the Group remaining significantly in excess of its reference rates on both a transitional and non-transitional basis. In October 2023 the BoE confirmed their intention to run a desk-based stress test exercise, rather than an ACS, in 2024; the Group will participate in this exercise as required.

**Resolvability Assessment Framework**

The BoE has introduced a Resolvability Assessment Framework to ensure major UK banks can be safely resolved. The Group is required to submit an assessment of its resolvability to the BoE biennially; the first assessment was submitted in October 2021 with disclosures published in June 2022. The BoE concluded that, upon their first assessment as resolution authority of the eight major banks, a major UK bank could enter resolution safely, remaining open and continuing to provide vital banking services to the economy. The Group submitted its recent self assessment to the BoE on 6 October 2023 which included enhancements relating to feedback received from the BoE as part of the first cycle. A further disclosure from the BoE will occur in June 2024.

### Capital resources

The Group's capital resources position as at 30 September 2023 is summarised below:

| Regulatory capital[1] | 2023 £m | 2022 £m |
|---|---|---|
| **Statutory total equity** | **5,607** | 6,340 |
| | | |
| **CET1 capital: regulatory adjustments[2]** | | |
| Other equity instruments | **(594)** | (666) |
| Defined benefit pension fund assets | **(333)** | (650) |
| Prudent valuation adjustment | **(5)** | (5) |
| Intangible assets | **(162)** | (256) |
| Goodwill | **(11)** | (11) |
| Deferred tax asset relying on future profitability | **(261)** | (302) |
| Cash flow hedge reserve | **(496)** | (699) |
| AT1 coupon accrual | **(12)** | (13) |
| Foreseeable dividend on ordinary shares | **(27)** | (106) |
| Excess expected loss | **(103)** | (100) |
| Share buyback | **–** | (13) |
| IFRS 9 transitional adjustments | **112** | 114 |
| Unconsolidated losses arising from joint venture | **(4)** | – |
| **Total regulatory adjustments to CET1** | **(1,896)** | (2,707) |
| **Total CET1 capital** | **3,711** | 3,633 |
| | | |
| **AT1 capital** | | |
| AT1 capital instruments | **594** | 666 |
| **Total AT1 capital** | **594** | 666 |
| | | |
| **Total Tier 1 capital** | **4,305** | 4,299 |
| | | |
| **Tier 2 capital** | | |
| Subordinated debt | **1,022** | 1,020 |
| **Total Tier 2 capital** | **1,022** | 1,020 |
| | | |
| **Total regulatory capital** | **5,327** | 5,319 |

(1) Data in the table is reported under CRD IV on a fully loaded basis with IFRS 9 transitional arrangements applied.

(2) A number of regulatory adjustments to CET1 capital are required under CRD IV regulatory capital rules.

| Regulatory capital flow of funds[1] | 2023 £m | 2022 £m |
|---|---|---|
| **CET1 capital[2]** | | |
| CET1 capital at 1 October | **3,633** | 3,616 |
| Share issuance | **2** | 2 |
| Share buyback | **(99)** | (76) |
| Retained earnings and other reserves (including special purpose entities) | **(242)** | 502 |
| Amendment to software asset deduction rules[3] | **–** | (151) |
| Intangible assets | **94** | 103 |
| Deferred tax asset relying on future profitability | **41** | (44) |
| Defined benefit pension fund assets | **317** | (99) |
| Movement in AT1 foreseeable distribution | **1** | 6 |
| Foreseeable dividend on ordinary shares | **(27)** | (106) |
| Excess expected losses | **(3)** | (100) |
| IFRS 9 transitional adjustments | **(2)** | (20) |
| Unconsolidated losses arising from joint venture | **(4)** | – |
| **Total CET1 capital at 30 September** | **3,711** | 3,633 |
| | | |
| **AT1 capital** | | |
| AT1 capital at 1 October | **666** | 697 |
| AT1 instrument issued net of costs | – | 346 |
| AT1 instrument repurchased | **(72)** | (377) |
| **Total AT1 capital at 30 September** | **594** | 666 |
| **Total Tier 1 capital at 30 September** | **4,305** | 4,299 |
| | | |
| **Tier 2 capital** | | |
| Tier 2 capital at 1 October | **1,020** | 1,019 |
| Amortisation of issue costs | **2** | 1 |
| **Tier 2 capital at 30 September** | **1,022** | 1,020 |
| **Total capital at 30 September** | **5,327** | 5,319 |

(1) Data in the table is reported under CRD IV on a fully loaded basis with IFRS 9 transitional arrangements applied.

(2) CET1 capital is comprised of shares issued and related share premium, retained earnings and other reserves less specified regulatory adjustments.

(3) The full deduction treatment for software assets was reinstated by the PRA in January 2022.

The Group's CET1 capital showed an increase of £78m during the year. The Group reported a profit after tax of £246m in the year, which together with reductions in intangible assets and deferred tax asset deductions of £135m, and after absorbing other movements, mostly in other reserves, of £80m, led to a net increase in CET1 of £301m. This net capital surplus was used to fund two share buyback programmes during the year totalling £100m, interim dividend payments of £45m, AT1 distributions of £54m, and a foreseeable ordinary dividend of £27m.

In December 2022, the Group redeemed £72m of AT1 securities (note 4.1.2).

Subsequent to the year end, the Group announced its intention to redeem £250m 7.875% Fixed Rate Reset Callable Notes due 2028 on 14 December 2023.

**Risk-weighted assets**

| Minimum capital requirements | 2023 Exposure £m | 2023 RWA £m | 2023 Minimum capital requirements £m | 2022 Exposure £m | 2022 RWA £m | 2022 Minimum capital requirements £m |
|---|---|---|---|---|---|---|
| Retail mortgages | **60,354** | **9,072** | **726** | 62,545 | 9,155 | 732 |
| Business lending | **12,635** | **6,990** | **559** | 11,959 | 6,196 | 497 |
| Other retail lending | **17,586** | **4,819** | **385** | 17,408 | 4,817 | 385 |
| Other lending | **18,328** | **364** | **29** | 18,165 | 277 | 22 |
| Other[1] | **592** | **674** | **54** | 584 | 637 | 51 |
| **Total credit risk** | **109,495** | **21,919** | **1,753** | 110,661 | 21,082 | 1,687 |
| Credit valuation adjustment | | **278** | **22** | | 258 | 21 |
| Operational risk | | **2,833** | **227** | | 2,623 | 210 |
| Counterparty credit risk | | **146** | **12** | | 185 | 15 |
| **Total** | **109,495** | **25,176** | **2,014** | 110,661 | 24,148 | 1,933 |

(1) The items included in the Other exposure class that attract a capital charge include items in the course of collection, fixed assets, prepayments, other debtors and deferred tax assets that are not deducted.

| RWA movements | 12 months to 30 September 2023 IRB RWA £m | STD RWA £m | Non-credit risk RWA[2] £m | Total £m | Minimum capital requirements £m | 12 months to 30 September 2022 IRB RWA £m | STD RWA £m | Non-credit risk RWA[2] £m | Total £m | Minimum capital requirements £m |
|---|---|---|---|---|---|---|---|---|---|---|
| Opening RWA | **14,943** | **6,139** | **3,066** | **24,148** | **1,933** | 15,699 | 5,844 | 2,689 | 24,232 | 1,938 |
| Asset size | **58** | **127** | **–** | **185** | **15** | 267 | 575 | – | 842 | 68 |
| Asset quality | **(1,011)** | **121** | **–** | **(890)** | **(71)** | (959) | 4 | – | (955) | (75) |
| Model updates[1] | **1,486** | **–** | **–** | **1,486** | **118** | (64) | – | – | (64) | (5) |
| Methodology and policy | **–** | **5** | **–** | **5** | **–** | – | (160) | – | (160) | (13) |
| Other | **–** | **51** | **191** | **242** | **19** | – | (124) | 377 | 253 | 20 |
| **Closing RWA** | **15,476** | **6,443** | **3,257** | **25,176** | **2,014** | 14,943 | 6,139 | 3,066 | 24,148 | 1,933 |

(1) Model updates include MAs.

(2) Other RWA includes operational risk, credit valuation adjustment and counterparty credit risk.

RWA increased c.£1bn to £25.2bn primarily due to the impact of higher lending, the new hybrid model related MAs and increased other non-credit RWAs.

There are a number of offsetting movements between asset quality and model updates. Asset quality movements predominantly reflect the impact from the introduction of new customer data on the incumbent rating system (£0.9bn reduction in RWA), however this is fully offset within model updates where this impact is temporary pending the implementation of the new hybrid models. Model updates also include the hybrid model MA of £0.4bn. In addition to model changes, asset quality includes a £0.2bn reduction in RWA from HPI movements although there is a similar increase relating to risk weights associated with new Business lending.

Other RWA movements of £242m are mainly due to an operational risk RWA uplift of £210m due to a higher three-year average income position in commercial and retail banking compared to the FY22 three-year average. The remainder is predominantly a combination of movements within credit valuation adjustment and counterparty credit risk.

### IFRS 9 transitional arrangements

The table below shows a comparison of capital resources, requirements and ratios with and without the application of transitional arrangements for IFRS 9.

| | 2023 | |
|---|---|---|
| **Available capital (amounts)** | IFRS 9 Transitional basis £m | IFRS 9 Fully loaded basis £m |
| CET1 capital | **3,711** | **3,599** |
| Tier 1 capital | **4,305** | **4,193** |
| Total capital | **5,327** | **5,215** |
| **RWA (amounts)** | | |
| Total RWA | **25,176** | **25,087** |
| **Capital ratios** | | |
| CET1 (as a percentage of RWA) | **14.7%** | **14.3%** |
| Tier 1 (as a percentage of RWA) | **17.1%** | **16.7%** |
| Total capital (as a percentage of RWA) | **21.2%** | **20.8%** |
| **Leverage ratio** | | |
| Leverage ratio total exposure measure | **86,554** | **86,442** |
| UK leverage ratio | **5.0%** | **4.9%** |

Transitional arrangements in CRR mean the regulatory capital impact of ECL is being phased in over time. Following the CRR Quick Fix amendments package, which applied from 27 June 2020, relevant provisions raised from 1 January 2020 through to 2024 have a CET1 add-back percentage of 50% in 2023, reducing to 25% in 2024.

At 30 September 2023, £112m of IFRS 9 transitional adjustments (2022: £114m) have been applied to the Group's capital position in accordance with CRR: £3m of static and £109m of dynamic adjustments (2022: £7m static and £107m dynamic).

### Capital requirements

The Group measures the amount of capital it is required to hold by applying CRD IV as implemented in the UK by the PRA. The table below summarises the amount of capital in relation to RWA the Group is currently required to hold, excluding any PRA buffer.

| | 2023 | |
|---|---|---|
| **Minimum requirements** | CET1 | Total capital |
| Pillar 1[(1)] | **4.5%** | **8.0%** |
| Pillar 2A | **1.7%** | **3.0%** |
| **Total capital requirement** | **6.2%** | **11.0%** |
| | | |
| Capital conservation buffer | **2.5%** | **2.5%** |
| UK countercyclical capital buffer | **2.0%** | **2.0%** |
| **Total (excluding PRA buffer)**[(2)] | **10.7%** | **15.5%** |

(1) The minimum amount of total capital under Pillar 1 of the regulatory framework is determined as 8% of RWA, of which at least 4.5% of RWA is required to be covered by CET1 capital.

(2) The Group may be subject to a PRA buffer as set by the PRA but is not permitted to disclose the level of any buffer.

The Group continues to maintain a significant surplus above its capital requirements. At September the Group maintained CET1 capital in excess of its requirements equal to 4.1% of RWAs (equivalent to £1,025m).

The PRA sets a Group specific Pillar 2A requirement for risks which are not captured within the Pillar 1 requirement. Together Pillar 1 and Pillar 2A represent the Group's Total Capital Requirement or TCR, which is the minimum requirement which must be met at all times.

In October 2022 the PRA communicated an update to the Group's Pillar 2A requirement setting it as 2.97% of RWAs, of which 1.67% must be met with CET1 capital (30 September 2022: £744m, of which £419m had to be met with CET1 capital). In line with previous guidance this requirement has been set as a percentage of RWAs, rather than the fixed nominal Pillar 2A requirements set during 2020 and 2021 in response to COVID-19. Applying this updated requirement in September 2023 resulted in a modest increase in total capital requirements of £4m and CET1 requirements of £2m. At 30 September 2023 this resulted in a TCR of 10.97% of RWAs (equivalent to £2,762m) of which 6.2% must be met with CET1 capital (equivalent to £1,554m).

The regulatory capital buffer framework is intended to ensure firms maintain a sufficient amount of capital above their regulatory minimum in order to withstand periods of stress and mitigate against firm specific and systemic risks. The UK has implemented the provisions on capital buffers outlined in CRD IV which introduced a combined capital buffer. This includes a Capital Conservation Buffer, a Countercyclical Capital Buffer (CCyB) and where applicable a Global Systemically Important Institution (G-SII) Buffer or an Other Systemically Important Institutions (O-SII) Buffer.

The Group's CCyB reflects an exposure weighted average of the CCyB rates applicable in the geographies the Group operates in. Currently this reflects only the UK. As had been previously announced, the CCyB rate increased in the year to 1% in December 2022, rising to 2% in July 2023 to align with its guidance for the CCyB rate under standard risk conditions. The FPC has noted the considerable uncertainties in relation to the economic outlook and will continue to monitor the situation and stands ready to vary the UK CCyB rate – in either direction – in line with the evolution of economic conditions, underlying vulnerabilities and the overall risk environment.

The Group has been designated as an O-SII, but is not required to hold a related capital buffer.

### MREL

| **MREL position** | 2023 £m | 2022 £m |
|---|---|---|
| Total capital resources[1] [2] | **5,327** | 5,319 |
| Eligible senior unsecured securities issued by Virgin Money UK PLC[2] | **2,707** | 2,423 |
| Total MREL resources | **8,034** | 7,742 |
| Risk-weighted assets | **25,176** | 24,148 |
| **Total MREL resources available as a percentage of risk-weighted assets** | **31.9%** | 32.1% |
| UK leverage exposure measure[3] | **86,554** | 85,934 |
| **Total MREL resources available as a percentage of UK leverage exposure measure[3]** | **9.3%** | 9.0% |

(1) The capital position reflects the application of the transitional arrangements for IFRS 9.

(2) Includes MREL instrument maturity adjustments, the add-back of regulatory amortisation and the deduction of instruments with less than one year to maturity.

(3) The comparative figures include a restatement to qualifying central bank claims which have been adjusted to exclude encumbered note cover and payments system collateral balances.

The BoE as the UK Resolution Authority has published its framework for setting a minimum requirement for own funds and eligible liabilities (MREL). This requires the Group to hold capital resources and eligible debt instruments equal to the greater of two times the Total Capital Requirement (TCR) or two times the UK leverage ratio requirement. In addition to MREL the Group must also hold any applicable capital buffers, which together with MREL represent the Group's loss-absorbing capacity (LAC) requirement.

As at 30 September 2023, the Group's leverage based LAC requirement of 7.8% of leverage exposures (or 26.6% when expressed as a percentage of RWAs) was greater than the RWA based LAC requirement of 26.4% of RWAs, meaning the leverage measure is the binding requirement.

MREL resources were £8.0bn (2022: £7.7bn), equivalent to 9.3% of leverage exposures (2022: 9.0%) or 31.9% when expressed as a percentage of RWAs (2022: 32.1%). This provides prudent headroom of £1.3bn or 1.5% above the binding LAC requirement of 7.8% of leverage exposures, or 5.3% above the binding LAC requirement of 26.6% when expressed as a percentage of RWAs.

### Dividend

Distributable reserves are determined as required by the Companies Act 2006 by reference to a company's individual financial statements. At 30 September 2023, the Company had accumulated distributable reserves of £1,044m (2022: £1,056m).

The Board has recommended a final dividend for the financial year ended 30 September 2023 of 2.0p per share.

### Share buyback

On 30 June 2022 the Company announced an inaugural share buyback programme, with an initial repurchase of up to £75m in aggregate between its ordinary shares of £0.10 each listed on the LSE and CDIs, each representing one share, listed on the ASX. The Company repurchased shares and CDIs in approximately equal proportions; the buyback commenced on 30 June 2022 and ended on 9 December 2022.

On 21 November 2022 the Company announced an extension to the share buyback programme with an intent to repurchase a further £50m in aggregate of ordinary shares and CDIs. The Company again repurchased shares and CDIs in approximately equal proportions; the buyback extension commenced on 21 November 2022 and ended on 7 March 2023.

On 2 August 2023 the Company announced a new share buyback to repurchase £50m in aggregate of ordinary shares and CDIs and subsequently repurchased shares and CDIs in approximately equal proportions; the buyback commenced on 2 August 2023 and ended on 22 November 2023.

On 23 November 2023 the Company announced a further share buyback with an intent to repurchase another £150m in aggregate of shares and CDIs, ending no later than 16 May 2024.

### Leverage

| Leverage ratio | 2023 £m | 2022 £m |
|---|---|---|
| **Total Tier 1 capital for the leverage ratio** | | |
| Total CET1 capital | **3,711** | 3,633 |
| AT1 capital | **594** | 666 |
| **Total Tier 1 capital** | **4,305** | 4,299 |
| **Exposures for the leverage ratio** | | |
| Total assets | **91,786** | 91,907 |
| Adjustment for off-balance sheet items | **2,999** | 3,204 |
| Adjustment for derivative financial instruments(1) | **706** | 522 |
| Adjustment for securities financing transactions | **2,261** | 2,974 |
| Adjustment for qualifying central bank claims(2) | **(9,052)** | (9,792) |
| Regulatory deductions and other adjustments(1) | **(2,146)** | (2,881) |
| **UK leverage ratio exposure(3)** | **86,554** | 85,934 |
| **UK leverage ratio(3)** | **5.0%** | 5.0% |
| **Average UK leverage ratio exposure(4)** | **85,910** | 86,144 |
| **Average UK leverage ratio(4)** | **4.9%** | 4.9% |

(1) The comparative figures include a reclassification between adjustment for derivative financial instruments and regulatory deductions and other adjustments in relation to the cash variation margin.

(2) The comparative figures include a restatement to qualifying central bank claims which have been adjusted to exclude encumbered note cover and payments system collateral balances.

(3) The UK leverage ratio and exposure measure are calculated after applying the IFRS 9 transitional arrangements of the CRR.

(4) The average leverage exposure measure is based on the daily average of on-balance sheet items and month-end average of off-balance sheet and capital items over the quarter (1 July 2023 to 30 September 2023).

The UK leverage ratio framework is relevant to PRA regulated banks and building societies with consolidated retail deposits equal to or greater than £50bn. The Group exceeds this threshold and accordingly the average UK leverage ratio exposure and average UK leverage ratio are disclosed.

The PRA simplified the leverage framework from 1 January 2022 with UK banks now subject to a single UK leverage ratio exposure measure. The CRD IV leverage ratio is no longer applicable to UK banks.

The leverage ratio is monitored monthly against a Board-approved RAS, with the responsibility for managing the ratio delegated to ALCO.

The leverage ratio is the ratio of Tier 1 capital to total exposures, defined as:

- Capital: Tier 1 capital defined on an IFRS 9 transitional basis.
- Exposures: total on- and off-balance sheet exposures (subject to credit conversion factors) as defined in the delegated act amending CRR article 429 (Calculation of the Leverage Ratio), which includes deductions applied to Tier 1 capital.

Other regulatory adjustments consist of adjustments that are required under PRA regulations to be deducted from Tier 1 capital. The removal of these from the exposure measure ensures consistency is maintained between the capital and exposure components of the ratio.

The Group's UK leverage ratio of 5.0% (2022: 5.0%) exceeds the UK minimum ratio of 3.25%.

**Funding and liquidity risk**

Funding risk occurs when the Group is unable to raise or maintain funds of sufficient quantity and quality to support the delivery of the business plan or sustain lending commitments. Prudent funding risk management reduces the likelihood of liquidity risks occurring, increases the stability of funding sources, minimises concentration risks and ensures future balance sheet growth is sustainable.

Liquidity risk occurs when the Group is unable to meet its current and future financial obligations as they fall due or at acceptable cost, or when the Group reduces liquidity resources below internal or regulatory stress requirements.

**Exposures**
The Group is predominantly funded by Personal and Business customers. Customer funding is supported by the Group's ongoing wholesale funding programmes, medium-term secured funding issuance (e.g. the Group's securitisation programmes), Regulated Covered Bonds and unsecured medium-term notes. The Group has also drawn against the BoE TFSME, which was introduced to support the UK through COVID-19.

Funding risk exposures arises from an unsustainable or undiversified funding base, for example, a reliance on short-term wholesale deposits. The risk may result in deviation from funding strategy, negatively impact market or customer perception, increase the acquisition cost of new funds or reduce lending capacity, thereby adversely impacting financial performance and stability.

The Group's primary liquidity risk exposure arises through the redemption of retail deposits where customers have the ability to withdraw funds with limited or no notice. Exposure also arises from the refinancing of customer and wholesale funding at maturity and the requirement to fund new and existing committed lending obligations including mortgage pipeline and credit card facilities.

**Measurement**
Funding and liquidity risks are subject to a range of measures contained within the Group's RAS which reflect both regulatory requirements, as a minimum, and the Group's own view on risk sensitivities. The Group RAS is supported by a series of limits agreed by ALCO. These measures provide a short- and long-term view of risks under both normal and stressed conditions. The measures focus on: cash outflows and inflows under stress; concentration risks; refinancing risks; asset encumbrance; and the quantum, diversity and operational capability of mitigating actions.

The Group's funding plan establishes an acceptable level of funding risk which is approved by the Board and is consistent with risk appetite and the Group's strategic objectives. The development of the Group's funding plan is informed by the requirements of the Group's financial risk policies. A series of metrics are used across the Group to measure risk exposures, including funding ratios, limits to concentration risk and maximum levels of encumbrance.

Liquidity is managed in accordance with the ILAAP, which is approved by the Board. Liquidity risk exposures are subject to assessment under both regulatory and internal requirements. The volume and quality of the Group's liquid asset portfolio is defined through a series of stress tests across a range of time horizons and stress conditions. The High-Quality Liquid Asset (HQLA) requirement is quantified as the outflow of funds under a series of stress scenarios less the impact of inflows from assets. Stress cash outflow assumptions have been established for individual liquidity risk drivers across idiosyncratic and market-wide stresses.

The Treasury function is responsible for the development and execution of strategy subject to oversight from the Risk function and review at ALCO. The Group continues to maintain its strong funding and liquidity position and seeks to achieve an appropriate balance between profitability, liquidity risk and balance sheet optimisation.

**Monitoring**
Liquidity is monitored and measured daily by the Group, with reporting conducted through ALCO and the Executive Risk Committee. In a stress situation or in adverse conditions, the level of monitoring and reporting is increased commensurate with the nature of the stress event.

Monitoring and control processes are in place against internal and regulatory liquidity requirements. The Group monitors a range of market and internal early warning indicators on a routine basis for early signs of liquidity risk in the market or specific to the Group. These indicators cover a mixture of quantitative and qualitative measures including daily variation of customer balances, measurement against stress requirements and monitoring of the macroeconomic environment.

**Mitigation**
The Group holds a portfolio of HQLA that can be utilised to raise funding in times of stress. The size of the HQLA portfolio is calibrated based on a view of potential outflows under both systemic and idiosyncratic stress events. The Group has several sources of funding which are well-diversified in terms of the type of instrument and product, counterparty, term structure and market. Wholesale funding is used to support balance sheet growth, lengthen the contractual tenor of funding and diversify funding sources. These funding programmes are a source of strength for the Group and leverage the Group's high-quality mortgage book as collateral for secured funding. In addition, the Group can use the repo market for managing cash flows and bilateral relationships to generate funds and can also participate in BoE operations through the Sterling Monetary Framework (SMF).

As a participant in the BoE SMF, the Group had access to funding via TFSME. TFSME was launched in April 2020 to provide cost-effective funds to banks to support additional lending to the real economy and incentivise lending to SMEs during a period of economic disruption caused by COVID-19.

The funding plan includes an assessment of the Group's capacity for raising funds across a wide range of primary funding sources, thereby mitigating funding risk. Refinancing risks are carefully managed and are subject to controls overseen by ALCO. The Group's funding plan includes TFSME repayment profiles designed to manage refinancing risk within a suitably prudent time frame.

The Group recovery plan has been established for management of an escalated liquidity requirement, if the Group experiences either restricted access to wholesale funding or a significant increase in the withdrawal of funds. The plan identifies triggers for escalation, assesses capacity, details the actions required, allocates the key tasks to individuals, provides a time frame and defines the governance framework to manage the action plan and return the balance sheet structure within appetite.

The Group operates a Funds Transfer Pricing system, a key purpose of which is to ensure that liquidity risk and funding costs are factors in the pricing of loans and deposits.

**Sources of funding**
The table below provides an overview of the Group's sources of funding as at 30 September 2023:

| | 2023 £m | 2022 £m |
|---|---|---|
| Total assets | **91,786** | 91,907 |
| Less: other liabilities[(1)] | **(2,694)** | (3,122) |
| Funding requirement | **89,092** | 88,785 |
| **Funded by:** | | |
| Customer deposits | **66,827** | 65,434 |
| Debt securities in issue | **9,719** | 8,509 |
| Due to other banks | **6,939** | 8,502 |
| *of which:* | | |
| *Secured loans* | **6,291** | 7,230 |
| *Securities sold under agreements to repurchase* | **552** | 1,205 |
| *Transaction balances with other banks* | **19** | 17 |
| *Deposits with other banks* | **77** | 50 |
| Equity | **5,607** | 6,340 |
| **Total funding** | **89,092** | 88,785 |

(1) Other liabilities include derivatives, deferred tax liabilities, provisions for liabilities and charges, and other liabilities as per the balance sheet line item.

The Group's funding objective is to prudently manage the sources and tenor of funds in order to provide a sound base from which to support sustainable lending. At 30 September 2023, the Group had a funding requirement of £89,092m (2022: £88,785m) with the majority being used to support loans and advances to customers.

**Customer deposits**
The majority of the Group's funding requirement was met by customer deposits of £66,827m (2022: £65,434m). Customer deposits comprise interest-bearing deposits, term deposits and non-interest-bearing demand deposits from a range of sources including Personal and Business customers.

**Debt securities in issue**
Growth in customer deposits has been supported by an increase in debt securities to £9,719m (2022: £8,509m). The wholesale funding has been primarily driven by issuance from our covered bond and medium-term note programmes.

**Equity**
Equity of £5,607m (2022: £6,340m) was also used to meet the Group's funding requirement. Equity comprises ordinary share capital, retained earnings, other equity investments and a number of other reserves. For full details on equity refer to note 4.1 within the consolidated financial statements.

**Liquid assets**
The quantity and quality of the Group's liquid assets are calibrated to the Board's view of liquidity risk appetite and remain at a prudent level above regulatory requirements.

The LCR (based on a monthly rolling average over the previous 12 months) increased from 140% to 146% during the year and remains comfortably above regulatory and internal risk appetite.

| **LCR** | 2023 £m | 2022 £m |
|---|---|---|
| Eligible liquidity buffer | **13,798** | 11,503 |
| Net stress outflows | **9,424** | 8,222 |
| **Surplus** | **4,374** | 3,281 |
| LCR | **146%** | 140% |

The liquid asset portfolio provides a buffer against sudden and potentially sharp outflows of funds. Liquid assets must therefore be high-quality so they can be realised for cash and cannot be encumbered for any other purpose (e.g. to provide collateral for payments systems). The liquid asset portfolio is primarily comprised of cash at the BoE, UK Government securities (Gilts) and listed securities (e.g. bonds issued by supra-nationals and AAA-rated covered bonds).

The volume and quality of the Group's liquid asset portfolio is defined through a series of internal stress tests across a range of time horizons and stress conditions. The key risk driver assumptions applied to the scenarios are:

| Liquidity Risk Driver | Internal Stress Assumption |
|---|---|
| **Retail funding** | Severe unexpected withdrawal of retail deposits by customers arising from redemption or refinancing risk.<br>No additional deposit inflows are assumed. |
| **Wholesale funding** | Limited opportunity to refinance wholesale contractual maturities. Full outflow of secured and unsecured funding during the refinancing period, with no reinvestment of funding. |
| **Off-balance sheet** | Cash outflows during the period of stress as a result of off-balance sheet commitments such as mortgage pipeline, undrawn credit card facilities and collateral commitments. Lending outflows, over and above contractual obligations, are honoured as the Group preserves ongoing viability. |
| **Intra-day** | Other participants in the payment system withhold or delay payments or customers increase transactions resulting in reduced liquidity. |
| **Liquid assets** | The liquidity portfolio value is reduced, reflecting stressed market conditions. |

The Group monitors the movements in its credit ratings and the related requirement to post collateral for payment systems and clearing houses. These figures are not considered material compared to the volume of unencumbered liquid assets.

As at 30 September 2023, the Group held eligible liquid assets well in excess of 100% of net stress outflows and Pillar 2 liquidity requirements, as defined through internal risk appetite.

| **Liquid asset portfolio**(1) | 2023 £m | 2022 £m | Change % | Average 2023 £m | Average 2022 £m |
|---|---|---|---|---|---|
| **Level 1** | | | | | |
| Cash and balances with central banks | **8,940** | 9,795 | (8.7) | **9,604** | 7,632 |
| UK Government treasury bills and gilts | **1,655** | 512 | 223.2 | **1,182** | 905 |
| Other debt securities | **3,153** | 2,827 | 11.5 | **2,782** | 2,993 |
| **Total level 1** | **13,748** | 13,134 | 4.7 | **13,568** | 11,530 |
| **Level 2**(2) | **471** | 117 | 302.8 | **327** | 32 |
| **Total LCR eligible assets** | **14,219** | 13,251 | 7.3 | **13,895** | 11,562 |

(1) Excludes encumbered assets.

(2) Includes Level 2A and Level 2B.

The liquid asset portfolio is marked to market and fully hedged from an interest, inflation and foreign exchange risk perspective. All fair value movements are therefore recognised in CET1 via the income statement (market risk) or FVOCI reserve (credit risk). The IRRBB stress testing framework includes limits to manage the stressed credit spread risk arising from hedging the fixed rate securities in the Group's liquid asset portfolio. This ensures the composition of the total portfolio is controlled and the exposure will not exceed internal appetite or the amount of capital allocated.

The NSFR was implemented by the PRA on 1 January 2022 based on Basel standards. During the year, the Group has been comfortably in excess of regulatory and internal requirements. The 12-month average NSFR as at 30 September 2023 is 136% (2022: 134%).

### Encumbered assets

The Group manages the level of asset encumbrance to ensure appropriate volumes of assets are maintained to support future planned and potential stressed funding requirements. The Group RAS includes an internal limit for levels of encumbrance. Reasons for asset encumbrance include, among others, supporting the Group's secured funding programmes to provide stable term funding to the Group, the posting of assets in respect of drawings under the TFSME scheme, use of assets as collateral for payments systems in order to support customer transactional activity and providing security for the Group's issuance of Scottish bank notes.

### Encumbered assets by asset category

| | Assets encumbered with non-central bank counterparties | | | | Other assets | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | Assets not positioned at the central bank | | | | |
| 2023 | Covered Bonds £m | Securitisations £m | Other £m | Total £m | Positioned at the central bank (including encumbered) £m | Readily available for encumbrance £m | Other assets capable of being encumbered £m | Cannot be encumbered £m | Total £m | Total £m |
| Loans and advances to customers | **5,944** | **3,807** | **–** | **9,751** | **17,770** | **24,995** | **17,458** | **2,276** | **62,499** | **72,250** |
| Cash and balances with central banks | **–** | **–** | **–** | **–** | **2,797** | **8,485** | **–** | **–** | **11,282** | **11,282** |
| Due from other banks | **97** | **262** | **296** | **655** | **–** | **–** | **12** | **–** | **12** | **667** |
| Derivative | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **135** | **135** | **135** |
| Financial instruments at FVOCI | **–** | **–** | **1,404** | **1,404** | **–** | **4,780** | **–** | **–** | **4,780** | **6,184** |
| Other assets | **–** | **–** | **14** | **14** | **–** | **–** | **186** | **1,068** | **1,254** | **1,268** |
| **Total assets** | **6,041** | **4,069** | **1,714** | **11,824** | **20,567** | **38,260** | **17,656** | **3,479** | **79,962** | **91,786** |

| | Assets encumbered with non-central bank counterparties | | | | Other assets | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | Assets not positioned at the central bank | | | | |
| 2022 | Covered Bonds £m | Securitisations £m | Other £m | Total £m | Positioned at the central bank (including encumbered) £m | Readily available for encumbrance £m | Other assets capable of being encumbered £m | Cannot be encumbered £m | Total £m | Total £m |
| Loans and advances to customers | 4,268 | 4,620 | – | 8,888 | 14,879 | 28,647 | 17,054 | 2,353 | 62,933 | 71,821 |
| Cash and balances with central banks | – | – | – | – | 2,879 | 9,342 | – | – | 12,221 | 12,221 |
| Due from other banks | 67 | 305 | 269 | 641 | – | – | 15 | – | 15 | 656 |
| Derivatives | – | – | – | – | – | – | – | 342 | 342 | 342 |
| Financial instruments at FVOCI | – | – | 1,535 | 1,535 | – | 3,529 | – | – | 3,529 | 5,064 |
| Other assets | – | – | 40 | 40 | – | – | 218 | 1,545 | 1,763 | 1,803 |
| **Total assets** | 4,335 | 4,925 | 1,844 | 11,104 | 17,758 | 41,518 | 17,287 | 4,240 | 80,803 | 91,907 |

The Group's total non-central bank asset encumbrance increased by £720m to £11,284m as at 30 September 2023. This was primarily due to an increase in encumbered mortgages, supporting Covered Bond funding.

Cash and balances with central banks of £11,282m, as per note 3.1.1.2, include: £1,971m of assets that are encumbered to support the issuance of Scottish bank notes (excluding notes not in circulation) and to support payments systems; £275m of mandatory central bank deposits; and £84m excluded from LCR to cover operating expenses.

Financial assets at FVOCI of £6,184m, as per note 3.1.2, include: £1,404m of encumbered UK Government treasury bills and gilts, £197m of which is encumbered to support Operational Continuity in Resolution.

**Assets and liabilities by maturity**

The following tables represent a breakdown of the Group's balance sheet, according to the contractual maturity of the assets and liabilities. Many of the longer-term monetary assets are variable rate products, with behavioural maturities shorter than the contractual terms. The majority of customer deposits are repayable on demand or at short notice on a contractual basis, with behavioural maturities typically longer than their contractual maturity. Accordingly, this information is not relied upon by the Group in its management of interest rate risk. The Group has disclosed certain term facilities within loans and advances to customers with a revolving element at the maturity of the facility as this best reflects their contractual maturity.

| 2023 | Call £m | 3 months or less £m | 3 to 12 months £m | 1 to 5 years £m | Over 5 years £m | No specified maturity(1) £m | Total £m |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| *Financial instruments* | | | | | | | |
| *At amortised cost* | | | | | | | |
| Loans and advances to customers | 748 | 2,766 | 945 | 6,448 | 55,608 | 5,676 | 72,191 |
| Cash and balances with central banks | 10,193 | – | – | – | – | 1,089 | 11,282 |
| Due from other banks | 510 | 157 | – | – | – | – | 667 |
| *At FVOCI* | – | 506 | 712 | 2,196 | 2,770 | – | 6,184 |
| *At FVTPL* | | | | | | | |
| Loans and advances to customers | – | 1 | – | 16 | 42 | – | 59 |
| Derivatives | 3 | 92 | 10 | 25 | 5 | – | 135 |
| Other | – | – | – | – | – | 2 | 2 |
| Other assets | – | 4 | 149 | 1 | 1 | 1,111 | 1,266 |
| **Total assets** | 11,454 | 3,526 | 1,816 | 8,686 | 58,426 | 7,878 | 91,786 |
| **Liabilities** | | | | | | | |
| *Financial instruments* | | | | | | | |
| *At amortised cost* | | | | | | | |
| Customer deposits | 40,567 | 4,368 | 15,195 | 6,697 | – | – | 66,827 |
| Debt securities in issue | – | 441 | 1,441 | 7,837 | – | – | 9,719 |
| Due to other banks | 96 | 393 | 550 | 5,900 | – | – | 6,939 |
| *At FVTPL* | | | | | | | |
| Derivatives | 2 | 22 | 45 | 196 | 25 | – | 290 |
| Other liabilities | 1,675 | 66 | 119 | 49 | 114 | 381 | 2,404 |
| **Total liabilities** | 42,340 | 5,290 | 17,350 | 20,679 | 139 | 381 | 86,179 |
| | | | | | | | |
| **Off-balance sheet items** | | | | | | | |
| Financial guarantees | – | 12 | 18 | 9 | 40 | – | 79 |
| Other credit commitments | 17,921 | – | – | – | – | – | 17,921 |
| **Total off-balance sheet items** | 17,921 | 12 | 18 | 9 | 40 | – | 18,000 |

(1) The no specified maturity balance within loans and advances to customers relates to credit cards.

| 2022 | Call £m | 3 months or less £m | 3 to 12 months £m | 1 to 5 years £m | Over 5 years £m | No specified maturity[1] £m | Total £m |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| *Financial instruments* | | | | | | | |
| *At amortised cost* | | | | | | | |
| Loans and advances to customers | 764 | 2,378 | 1,019 | 7,241 | 55,053 | 5,296 | 71,751 |
| Cash and balances with central banks | 11,015 | – | – | – | – | 1,206 | 12,221 |
| Due from other banks | 575 | 81 | – | – | – | – | 656 |
| At FVOCI | – | 620 | 602 | 1,917 | 1,925 | – | 5,064 |
| *At FVTPL* | | | | | | | |
| Loans and advances to customers | – | 2 | 1 | 21 | 46 | – | 70 |
| Derivatives | 2 | 46 | 71 | 190 | 33 | – | 342 |
| Other | – | – | – | – | – | 8 | 8 |
| Other assets | – | 7 | 152 | 1 | 1 | 1,634 | 1,795 |
| **Total assets** | 12,356 | 3,134 | 1,845 | 9,370 | 57,058 | 8,144 | 91,907 |
| **Liabilities** | | | | | | | |
| *Financial instruments* | | | | | | | |
| *At amortised cost* | | | | | | | |
| Customer deposits | 48,750 | 3,786 | 10,209 | 2,689 | – | – | 65,434 |
| Debt securities in issue | – | 485 | 1,047 | 6,669 | 308 | – | 8,509 |
| Due to other banks | 67 | 285 | 250 | 7,900 | – | – | 8,502 |
| *At FVTPL* | | | | | | | |
| Derivatives | 3 | 9 | 29 | 253 | 33 | – | 327 |
| Other liabilities | 1,822 | 135 | 134 | 54 | 59 | 591 | 2,795 |
| **Total liabilities** | 50,642 | 4,700 | 11,669 | 17,565 | 400 | 591 | 85,567 |
| | | | | | | | |
| **Off-balance sheet items** | | | | | | | |
| Financial guarantees | – | 33 | 23 | 12 | 44 | – | 112 |
| Other credit commitments | 19,247 | – | – | – | – | – | 19,247 |
| **Total off-balance sheet items** | 19,247 | 33 | 23 | 12 | 44 | – | 19,359 |

(1) The no specified maturity balance within loans and advances to customers relates to credit cards.

**Cash flows payable under financial liabilities by contractual maturity**

| **2023** | Call £m | 3 months or less £m | 3 to 12 months £m | 1 to 5 years £m | Over 5 years £m | No specified maturity £m | Total £m |
|---|---|---|---|---|---|---|---|
| **Liabilities** | | | | | | | |
| *Financial instruments* | | | | | | | |
| *At amortised cost* | | | | | | | |
| Customer deposits | **40,567** | **4,384** | **15,647** | **6,874** | **–** | **–** | **67,472** |
| Debt securities in issue | **–** | **510** | **1,744** | **9,036** | **–** | **–** | **11,290** |
| Due to other banks | **96** | **399** | **837** | **6,304** | **–** | **–** | **7,636** |
| *At FVTPL* | | | | | | | |
| Trading derivatives | **–** | **16** | **29** | **37** | **8** | **–** | **90** |
| *Hedging derivatives* | | | | | | | |
| Contractual amounts payable | **–** | **65** | **556** | **1,668** | **–** | **–** | **2,289** |
| Contractual amounts receivable | **–** | **(21)** | **(463)** | **(1,500)** | **–** | **–** | **(1,984)** |
| Other liabilities | **1,675** | **66** | **119** | **49** | **114** | **381** | **2,404** |
| **Total liabilities** | **42,338** | **5,419** | **18,469** | **22,468** | **122** | **381** | **89,197** |

| **2022** | Call £m | 3 months or less £m | 3 to 12 months £m | 1 to 5 years £m | Over 5 years £m | No specified maturity £m | Total £m |
|---|---|---|---|---|---|---|---|
| **Liabilities** | | | | | | | |
| *Financial instruments* | | | | | | | |
| *At amortised cost* | | | | | | | |
| Customer deposits | 48,750 | 3,801 | 10,291 | 2,732 | – | – | 65,574 |
| Debt securities in issue | – | 521 | 1,294 | 7,863 | 315 | – | 9,993 |
| Due to other banks | 67 | 289 | 492 | 8,793 | – | – | 9,641 |
| *At FVTPL* | | | | | | | |
| Trading derivatives | – | 12 | 40 | 63 | 14 | – | 129 |
| *Hedging derivatives* | | | | | | | |
| Contractual amounts payable | – | 21 | 557 | 1,720 | – | – | 2,298 |
| Contractual amounts receivable | – | (6) | (459) | (1,477) | – | – | (1,942) |
| Other liabilities | 1,822 | 135 | 134 | 54 | 59 | 591 | 2,795 |
| **Total liabilities** | 50,639 | 4,773 | 12,349 | 19,748 | 388 | 591 | 88,488 |

The balances in the cash flow table above do not agree directly to the balances in the balance sheet or the assets and liabilities by maturity table presented above, as the table incorporates all cash flows, on an undiscounted basis, related to both principal and future coupon payments.

**Analysis of debt securities in issue by residual maturity**
The table below shows the residual maturity of the Group's debt securities in issue:

| | 3 months or less £m | 3 to 12 months £m | 1 to 5 years £m | Over 5 years £m | Total 2023 £m | Total 2022 £m |
|---|---|---|---|---|---|---|
| Covered bonds | **8** | **614** | **3,793** | **–** | **4,415** | 3,467 |
| Securitisation | **165** | **89** | **1,486** | **–** | **1,740** | 1,880 |
| Medium-term notes | **6** | **737** | **1,869** | **–** | **2,612** | 2,249 |
| Subordinated debt | **262** | **1** | **689** | **–** | **952** | 913 |
| **Total debt securities in issue** | **441** | **1,441** | **7,837** | **–** | **9,719** | 8,509 |
| Of which issued by Virgin Money UK PLC | **268** | **738** | **2,558** | **–** | **3,564** | 3,162 |

**External credit ratings**
The Group's long-term credit ratings are summarised below:

| | Outlook as at | As at | |
|---|---|---|---|
| | 30 Sept 2023[1] | 30 Sept 2023 | 30 Sept 2022 |
| **Virgin Money UK PLC** | | | |
| Moody's | Stable | Baa1 | Baa1 |
| Fitch | Positive | BBB+ | BBB+ |
| Standard & Poor's | Stable | BBB- | BBB- |
| **Clydesdale Bank PLC** | | | |
| Moody's[2] | Stable | A3 | A3 |
| Fitch | Positive | A- | A- |
| Standard & Poor's | Stable | A- | A- |

(1) For detailed background on the latest credit opinion by Standard & Poor's, Fitch and Moody's, please refer to the respective rating agency website.
(2) Long-term deposit rating.

In June 2023, Fitch revised the outlook on the Group's Long-Term Issuer Default Rating to Positive from Stable reflecting Fitch's expectation of a structural improvement in profitability due to higher interest rates, contained credit impairment charges and further cost efficiency improvements. It also reflects the Group's improving risk profile, notwithstanding the tougher operating environment.

As at 22 November 2023, there have been no other changes to the Group's long-term credit ratings or outlooks since the report date.

**Market risk**
Market risk is the risk of loss associated with adverse changes in the value of assets and liabilities held by the Group as a result of movements in market factors such as foreign exchange risk, interest rates (duration risk), customer behaviour (optionality risk), and the movement in rate spreads across types of assets or liabilities (basis risk and credit spread risk). The Group's balance sheet is predominantly UK-based and is denominated in GBP, therefore foreign exchange is not a material risk for the Group. Any non-GBP denominated funding issuances and any foreign currency securities purchased are cross-currency swapped to sterling for the term of the instrument.

**Exposures**
The Group does not have a trading book and therefore is only exposed to non-traded market risk. Market risk principally arises through Interest Rate Risk in the Banking Book (IRRBB), small foreign exchange exposure and the management of assets to support our liquidity requirements, including Credit Spread Risk in the Banking Book (CSRBB). It comprises the sensitivity of the Group's current and future NII and economic value to movements in market interest rates. The major contributors to interest rate risk are:

- the mismatch, or duration, between repricing dates of interest-bearing assets and liabilities;
- basis risk or assets and liabilities repricing to different reference rates, for example, customer asset and liability products repricing against BoE base rate and Sterling Overnight Index Average (SONIA); and
- customer optionality, for example, the right to repay borrowing in advance of contractual maturity dates.

The focus of the Group's activity is to provide high-quality banking services to its customers. These services include the provision of foreign exchange, interest rate and commodity derivative products to enable customers to manage risks within their businesses. As a result of these activities, the Group may be exposed to forms of market risk that would arise from movements in the price on these products. These risks are monitored daily and are not a material component of the Group's risk profile. Controls and mitigation include the hedging of these products and the use of natural offsets, in line with Group policies.

**Measurement**
IRRBB is measured, monitored, and managed from both an internal risk appetite and an external regulatory perspective. The RMF incorporates both market valuation and earnings-based approaches. In accordance with the Group IRRBB policy, risk measurement techniques include: basis point sensitivity, NII sensitivity, value at risk (VaR), changes in the economic value of equity (EVE), interest rate risk stress testing, and scenario analysis.

The key features of the market risk management measurement approach are:

- Basis point sensitivity analysis is performed daily and compares the potential impact of a one basis point (0.01%) change on the present value of all future cash flows.
- NII sensitivity assesses changes to earnings over a 12-month time horizon as a result of interest rate movements and changes to customer behaviour.
- VaR is measured on a statistical basis using a 99% confidence level based on daily rate movements over a ten-year history set with a one-year holding period.
- EVE is measured in line with PRA Rulebook with all six interest rate shock scenarios assessed on a quarterly basis, including customer optionality stresses. Reporting is performed including and excluding equity.
- Static balance sheet (i.e. any new business is assumed to be matched, hedged or subject to immediate repricing).
- Dynamic balance sheet (i.e. a balance sheet incorporating future business expectations, adjusted for the relevant scenario in a consistent manner).
- Run-off balance sheet (i.e. existing assets and liabilities not replaced as they mature, except to the extent necessary to fund the remaining balance sheet).
- Investment term for capital is modelled with a benchmark term agreed by ALCO.
- Investment term for core non-interest-bearing assets and liabilities is modelled on a behavioural basis with a benchmark term agreed by ALCO.
- Assumptions covering the behavioural life of products and customer behaviour for optionality are reviewed and approved by ALCO.
- Structural hedging, used to reduce earnings volatility, is based on analysis approved by ALCO and Board.
- CSRBB is assessed through VaR applied to the Group's liquid asset buffer portfolio. CSRBB is measured at a 99% confidence level based on daily spread movements over a ten-year history set with a three-month holding period.
- Foreign exchange risk is assessed based on the absolute exposure to each currency.
- IRRBB is fully integrated in the Group's ICAAP.

**Mitigation**
Market risks are overseen by ALCO with delegation for day-to-day management given to Treasury. Treasury uses a number of techniques and products to manage market risks including interest rate swaps, cash flow netting and foreign exchange derivatives.

The Group uses derivative financial instruments to manage its exposures within approved limits and not for speculative purposes. The Group elects to apply hedge accounting for the majority of its risk management activity that uses derivatives. Certain derivatives are designated as either fair value hedge or cash flow hedge:

*Fair value hedges* – the Group hedges part of its existing interest rate risk, resulting from potential movements in the fair value of fixed rate assets and liabilities. The fair value of these swaps is disclosed within note 3.1.3.2 to the Group's consolidated financial statements. There were no transactions for which fair value hedge accounting had to be discontinued in the year.

*Cash flow hedges* – the Group hedges a portion of the variability in future cash flows attributable to interest rate risk. The interest risk arises from variable interest rate assets and liabilities which are hedged using interest rate swaps. There were no transactions for which cash flow hedge accounting had to be discontinued in the year as a result of the highly probable cash flows no longer being expected to occur. The fair value of derivatives is disclosed within note 3.1.3.2 to the Group's consolidated financial statements.

**Monitoring**
Parameters and assumptions of models that are used in market risk monitoring are reviewed and updated on at least an annual basis. Material changes require the approval of ALCO. Oversight of market risk is conducted by the Group's Financial Risk team which is independent of the Treasury function. The Board and Executive Risk Committee, through ALCO's oversight, monitor risk to ensure it remains within approved policy limits and Board requirements.

| | Duration risk | | Credit spread | |
|---|---|---|---|---|
| **Value at Risk** | 2023 £m | 2022 £m | 2023 £m | 2022 £m |
| As at 30 September | **27** | 17 | **62** | 41 |
| Average value during the year | **16** | 19 | **55** | 48 |
| Minimum value during the year | **4** | 14 | **44** | 41 |
| Maximum value during the year | **28** | 27 | **62** | 52 |

### Net interest income

Earnings sensitivity measures calculate the change in NII over a 12-month period resulting from an instantaneous and parallel change in interest rates. +/-25 basis point shocks and +/-100 basis point shocks represent the primary NII sensitivities assessed internally, though a range of scenarios are assessed on a monthly basis.

| 12 months NII sensitivity | 2023 £m | 2022 £m |
|---|---|---|
| + 25 basis point parallel shift | **11** | 18 |
| +100 basis point parallel shift | **42** | 66 |
| - 25 basis point parallel shift | **(11)** | 5 |
| -100 basis point parallel shift | **(45)** | (35) |

Sensitivities disclosed reflect the expected mechanical response to a movement in rates and represent a prudent outcome. The sensitivities are indicative only and should not be viewed as a forecast.

The key assumptions and limitations are outlined below:

- The sensitivities are calculated based on a static balance sheet and it is assumed there is no change to margins on reinvestment of maturing fixed rate products.
- There are no changes to basis spreads with the rate change passed on in full to all interest rate bases.
- Administered rate products receive a rate pass on in line with internal scenario specific pass on assumptions. Any rate reduction in a rate fall scenario is subject to product floors with the assumption customer rates would not go negative.
- Additional commercial pricing responses and management actions are not included.
- While in practice hedging strategy would be reviewed in light of changing market conditions, the sensitivities assume no changes over the 12-month period.

### Market risk linkage to the balance sheet

The following table shows the Group's principal market risks, linked to the balance sheet assets and liabilities.

| | 2023 £m | 2022 £m | Interest rate duration | Optionality | Basis | Credit spread | Foreign exchange |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Financial instruments | | | | | | | |
| *At amortised cost* | | | | | | | |
| Loans and advances to customers | **72,191** | 71,751 | • | • | • | | • |
| Cash and balances with central banks | **11,282** | 12,221 | • | | • | | |
| Due from other banks | **667** | 656 | • | | • | | • |
| At FVOCI | **6,184** | 5,064 | • | | • | • | • |
| *At FVTPL* | | | | | | | |
| Loans and advances to customers | **59** | 70 | • | • | • | | • |
| Derivatives | **135** | 342 | • | | • | | • |
| Other | **2** | 8 | • | | | | • |
| Other assets | **1,266** | 1,795 | • | | | | • |
| **Total assets** | **91,786** | 91,907 | | | | | |
| **Liabilities** | | | | | | | |
| Financial instruments | | | | | | | |
| *At amortised cost* | | | | | | | |
| Customer deposits | **66,827** | 65,434 | • | • | • | | • |
| Debt securities in issue | **9,719** | 8,509 | • | | • | | • |
| Due to other banks | **6,939** | 8,502 | • | | • | | • |
| *At FVTPL* | | | | | | | |
| Derivatives | **290** | 327 | • | | • | | • |
| Other liabilities | **2,404** | 2,795 | • | | | | • |
| **Total liabilities** | **86,179** | 85,567 | | | | | |

**Repricing periods of assets and liabilities by asset/liability category**
The following table shows the repricing periods of the Group's assets and liabilities as assessed by the Group. This repricing takes account of behavioural assumptions where material and the Group's policy to hedge capital in accordance with a benchmark term agreed by ALCO.

| 2023 | Overnight £m | 3 months or less £m | 3 to 12 months £m | 1 to 5 years £m | Over 5 years £m | Non-interest bearing £m | Total £m |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| *Financial instruments* | | | | | | | |
| *At amortised cost* | | | | | | | |
| Loans and advances to customers | **7,745** | **8,132** | **12,381** | **43,151** | **1,321** | **(539)** | **72,191** |
| Cash and balances with central banks | **9,903** | **35** | **105** | **140** | **–** | **1,099** | **11,282** |
| Due from other banks | **626** | **–** | **–** | **–** | **–** | **41** | **667** |
| At FVOCI | **1,635** | **475** | **568** | **881** | **2,440** | **185** | **6,184** |
| *At FVTPL* | | | | | | | |
| Loans and advances to customers | **–** | **2** | **5** | **23** | **29** | **–** | **59** |
| Derivatives | **–** | **–** | **–** | **–** | **–** | **135** | **135** |
| Other assets | **14** | **20** | **59** | **314** | **157** | **704** | **1,268** |
| **Total assets** | **19,923** | **8,664** | **13,118** | **44,509** | **3,947** | **1,625** | **91,786** |
| **Liabilities** | | | | | | | |
| *Financial instruments* | | | | | | | |
| *At amortised cost* | | | | | | | |
| Customer deposits | **7,935** | **16,096** | **18,254** | **23,085** | **1,229** | **228** | **66,827** |
| Debt securities in issue | **4,184** | **250** | **748** | **4,861** | **–** | **(324)** | **9,719** |
| Due to other banks | **6,783** | **10** | **33** | **–** | **–** | **113** | **6,939** |
| *At FVTPL* | | | | | | | |
| Derivatives | **–** | **–** | **–** | **–** | **–** | **290** | **290** |
| Other liabilities | **1,249** | **85** | **255** | **340** | **–** | **475** | **2,404** |
| Equity | **–** | **166** | **748** | **3,007** | **1,329** | **357** | **5,607** |
| **Total liabilities and equity** | **20,151** | **16,607** | **20,038** | **31,293** | **2,558** | **1,139** | **91,786** |
| Notional value of derivatives managing interest rate sensitivity | **5,417** | **1,655** | **8,595** | **(14,136)** | **(1,531)** | **–** | **–** |
| **Total interest rate gap** | **5,189** | **(6,288)** | **1,675** | **(920)** | **(142)** | **486** | **–** |
| **Cumulative interest rate gap** | **5,189** | **(1,099)** | **575** | **(344)** | **(486)** | **–** | **–** |

| 2022 | Overnight £m | 3 months or less £m | 3 to 12 months £m | 1 to 5 years £m | Over 5 years £m | Non-interest bearing £m | Total £m |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| *Financial instruments* | | | | | | | |
| *At amortised cost* | | | | | | | |
| Loans and advances to customers | 7,293 | 8,796 | 13,234 | 41,514 | 1,699 | (785) | 71,751 |
| Cash and balances with central banks | 10,765 | 12 | 37 | 196 | – | 1,211 | 12,221 |
| Due from other banks | 656 | – | – | – | – | – | 656 |
| At FVOCI | 1,265 | 525 | 320 | 1,159 | 1,733 | 62 | 5,064 |
| *At FVTPL* | | | | | | | |
| Loans and advances to customers | – | 30 | 4 | 16 | 20 | – | 70 |
| Derivatives | – | – | – | – | – | 342 | 342 |
| Other assets | 40 | 38 | 113 | 604 | – | 1,008 | 1,803 |
| **Total assets** | 20,019 | 9,401 | 13,708 | 43,489 | 3,452 | 1,838 | 91,907 |
| **Liabilities** | | | | | | | |
| *Financial instruments* | | | | | | | |
| *At amortised cost* | | | | | | | |
| Customer deposits | 7,026 | 18,725 | 13,449 | 26,077 | – | 157 | 65,434 |
| Debt securities in issue | 3,606 | 191 | 432 | 4,686 | – | (406) | 8,509 |
| Due to other banks | 8,438 | 12 | – | – | – | 52 | 8,502 |
| *At FVTPL* | | | | | | | |
| Derivatives | – | – | – | – | – | 327 | 327 |
| Other liabilities | 1,717 | – | – | – | – | 1,078 | 2,795 |
| Equity | – | 264 | 573 | 3,306 | 350 | 1,847 | 6,340 |
| **Total liabilities and equity** | 20,787 | 19,192 | 14,454 | 34,069 | 350 | 3,055 | 91,907 |
| Notional value of derivatives managing interest rate sensitivity | 16,448 | (359) | (239) | (12,146) | (3,704) | – | – |
| **Total interest rate gap** | 15,680 | (10,150) | (985) | (2,726) | (602) | (1,217) | – |
| **Cumulative interest rate gap** | 15,680 | 5,530 | 4,545 | 1,819 | 1,217 | – | – |

**LIBOR replacement**

All regulatory milestones in relation to LIBOR cessation have been met and there are no conduct issues to note.

Loans with an aggregate value of c.£0.9m with a small number of customers remain on three-month GBP synthetic LIBOR. This temporary reference rate is due to cease at the end of March 2024.

There are no remaining USD LIBOR exposures. Post 31 March 2024, there will be no LIBOR exposure (in any currency) on the Group's balance sheet.

Financial instruments linked to IBOR benchmark rates are summarised below:

**Amounts referencing IBOR rates**

| 2023 | Non derivative financial assets – carrying value(1) £m | Non derivative financial liabilities – carrying value £m | Derivatives – nominal amount(2) £m |
|---|---|---|---|
| GBP LIBOR | 1 | – | – |
| Other(3) | 179 | – | – |
| **Total** | **180** | – | – |

| 2022 | Non derivative financial assets – carrying value(1) £m | Non derivative financial liabilities – carrying value £m | Derivatives – nominal amount(2) £m |
|---|---|---|---|
| GBP LIBOR | 94 | – | 67 |
| Other(3) | 164 | – | – |
| **Total** | 258 | – | 67 |

(1) Gross carrying amount excluding allowances for ECLs.

(2) The IBOR exposures for derivative nominal amounts include undrawn loan commitments shown as GBP LIBOR. This is materially the case although some facilities allow drawdowns in a number of different currencies.

(3) Comprises financial instruments referencing EURIBOR, which is not subject to benchmark reform (2022: £127m).

## Pension risk

The Group operates a defined benefit pension scheme, the Yorkshire and Clydesdale Bank Pension Scheme (the Scheme). The Bank is the Scheme's principal employer and there are no other participating employers. The Scheme was closed to future accrual on 1 August 2017 for most members. A small number of members remain on a defined benefit accruals basis subject to certain conditions.

Under a defined benefit pension scheme, the economic benefit an employee receives in retirement is determined by factors such as salary and length of service but is not tied to the employee's or the employer's contributions, or the performance of the scheme's assets. A defined benefit pension scheme is exposed to market risk drivers such as interest rate risk, inflation risk, equity risk, as well as risks pertaining to the life expectancy of scheme members (longevity risk) and to changes in the legislation and regulatory requirements.

Pension risk is the risk that, at any point in time, the value of the Scheme's assets is not enough to meet the Scheme's estimated liabilities. This risk will continue to exist until the Scheme is formally wound up, either if all the liabilities are transferred to a third party (for example an insurer) or once all individual member benefits have been honoured. Pension risk can negatively impact the Group's capital position.

The Group also supports a defined contribution scheme. Defined contribution schemes do not give rise to pension risk, as the employer has no legal or constructive obligation to make further contributions if the defined contribution scheme's assets are insufficient to pay all member benefits. Risks, including market, investment performance and longevity risks are borne by the employee rather than the Group.

### Risk appetite

The Group's pension risk appetite is a component of the Group-wide framework for the management of balance sheet risks.

Pension risk may adversely impact the Group's capital position. The Group is required to hold capital against it and may be required to make further contributions. Consequently, pension risk is considered in the context of potential capital impacts to the Group, due to changes in the valuations of the Scheme's liabilities and assets.

# Financial risk

**Liabilities**
The defined benefit obligation is a series of future cash flows, with relatively long duration. It is estimated by independent actuaries using the projected unit credit method. The actual cost of the Scheme can only be known after the Scheme is formally wound up.

On an IAS 19 basis, the defined benefit obligation present value is calculated by discounting the series of future cash flow estimates using a discount rate linked to yields of high-quality corporate bonds, of a duration aligned to that of the Scheme's liabilities. The cash flows and valuation are primarily sensitive to changes in corporate bond credit spreads, long-term inflation rates and the life expectancy of members. There is a risk that the value of the Scheme's liabilities is higher than that of its assets. In particular:

- an increase in the discount rate corresponds to a decrease in liabilities;
- an increase in long-term expected inflation corresponds to an increase in liabilities; and
- an increase in life expectancy corresponds to an increase in liabilities.

The impact of these actuarial assumptions on valuations will also depend on investment and de-risking decisions (including interest rate, inflation rate and longevity hedging) made by the Trustee, as well as by the inflationary caps within the terms of the Scheme. Nevertheless, material changes to the key actuarial assumptions or changes to the methodology by which they are derived may lead to volatility in the Group's IAS 19 position. In line with pensions legislation, a formal actuarial valuation (Triennial Valuation) of the Scheme's assets and liabilities takes place at least every three years by independent actuaries.

More information on the Scheme's defined benefit obligations is shown within note 3.3 of the Group's consolidated financial statements. The present value of the liabilities was £2,284m as at 30 September 2023 (2022: £2,216m).

**Assets**
The Scheme's assets are held separately from the Group's assets and are administered by a board of trustees (the Trustee). The Trustee has fiduciary responsibilities to the Scheme's members and governs investments according to a Statement of Investment Principles (SIP). The SIP is reviewed and agreed by the Trustee on a regular basis, with the Group consulted on any proposed changes. The SIP sets out the Scheme objectives and the path to meet these objectives and is drafted in accordance with the requirements of Section 35 of the Pensions Act 1995 (as amended by the Pensions Act 2004 and regulations made under it). This results in the Scheme holding an appropriate mix of assets to better match future pension obligations.

There is a risk that the value of the Scheme's assets is lower than the present value of its liabilities. In particular, asset total returns lower than the discount rate used in the calculation of the present value of the defined benefit obligations may have an adverse impact on the Group's IAS 19 position.

The split of Scheme assets is shown within note 3.3 of the Group's consolidated financial statements. The fair value of the assets was £2,796m as at 30 September 2023 (2022: £3,216m).

Within the Scheme's matching assets there is a Liability Driven Investment (LDI) portfolio, which consists of both physical assets and derivatives. The Scheme uses a bespoke, segregated strategy which reflects, as far as possible, the specifics of the Scheme's liabilities in terms of exposure to movements in interest rates and inflation. As at 30 September 2023, the LDI portfolio was valued at £1,038m (2022: £968m).

LDI portfolios are commonly used by defined benefit pension schemes to better match their assets to their liabilities, while retaining their allocations to return-seeking assets. For example, falling interest rates or rising inflation would typically increase the value of a scheme's liabilities but the value of the LDI portfolio would also increase commensurably, hence reducing the scheme's funding level volatility. LDI utilises financial instruments, including derivatives, which require the scheme to provide collateral to counterparties. This generates additional liquidity risks and requirements as these collateral demands can change over periods when rates change. The general trend since LDI strategies were first introduced has been long-term interest rates falling. However, when interest rates rise instead of fall, more collateral is required to be posted for the same level of interest rate and inflation protection to be maintained. Therefore, the scheme needs to ensure that it has sufficient liquidity to meet any such obligation.

As at 30 September 2023, the Scheme is still estimated to have substantial collateral headroom to meet further rises in interest rates of more than 10% (2022: 3%).

During the period, the Group and Trustee to the Scheme agreed to cease their previous contingent security arrangement. Subsequently, the Group has granted a £75m uncommitted facility to the Scheme as an additional contingency against future short-term liquidity challenges resulting from unexpected market turbulence. As at 30 September 2023 the amount drawn under the facility was £Nil.

**Exposure**
The Group's defined benefit pension scheme affects its regulatory capital in two ways:

- CET1 capital – an IAS 19 surplus increases the Group's balance sheet assets and reserves. However, any such amount is not recognised for the purposes of determining CET1 capital. An IAS 19 deficit on the other hand, which increases balance sheet liabilities and reduces reserves, is recognised for regulatory capital purposes, and so will decrease CET1 capital.
- Pillar 2A capital – the Group is also required to determine the level of capital required to be held under Pillar 2A for pension obligation risk as part of the annual ICAAP process. This requirement forms part of the Group's regulatory Total Capital Requirement.

**Mitigation**
The Trustee and Group have a common view of the Scheme's long-term strategic aims, encapsulated by an agreed de-risking journey plan. Within the journey plan, several core principles have been established, including a long-term self-sufficiency funding target (i.e. the point in time when the Scheme would no longer need to call on the Bank for additional funding) with assumptions as to how this target is expected to be managed, monitored and met. Potential actions to address deviations in the actual funding level relative to the journey plan have also been considered.

In addition to the Scheme being closed to new members and essentially closed to future accrual, additional measures have been implemented by the Group and Trustee with the specific aim of reducing risks. This includes hedging against interest rate and inflation risk. Moreover, on 6 April 2023, the Scheme executed a longevity swap transaction to manage longevity risk in relation to c.£1,600m of pensioner liabilities. Cost-effective options to further reduce risk within the Scheme will continue to be assessed.

**Monitoring**
Information on the Scheme's current valuations, asset holdings and discount and inflation rate assumptions are presented to ALCO. This also includes monitoring of the performance of the LDI portfolio as well as of the collateral headroom. The impact of the Scheme on the Group is also subject to risk oversight from the Risk function. In addition, semi-annual pension risk updates are provided to the Board Risk Committee.

Performance of the Scheme's asset portfolio against the various risk metrics is monitored by the Scheme investment adviser, and reported to the Investment Sub Committee, which includes Group representation, and Trustee Board on a quarterly basis.

The Scheme's de-risking plan has delivered resilience to stress-testing and continued improvements in Group and Trustee valuations. The IAS 19 position continues to be assessed in the Group's ICAAP and regulatory stress testing processes.

The Triennial Valuation with effective date 30 September 2022 has concluded and showed a funding surplus. Consequently, no further contributions from the Group will be required and there is no capital impact. The effective date of the Scheme's next Triennial Valuation is 30 September 2025.

# Directors' responsibility statement in respect of the Annual Report and Accounts

The responsibility statement below has been prepared in connection with the Company's full Annual Report and Accounts for the year ended 30 September 2023. Certain parts thereof are not included within this announcement.

The Directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the Group and the undertakings included in the consolidation taken as a whole; and
- the Strategic report includes a fair review of the development and performance of the business and the position of the Company and the Group, together with a description of the principal risks and uncertainties that they face.

The Directors consider the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's and Group's position and performance, business model and strategy.

**David Duffy**
Chief Executive Officer
22 November 2023

# Consolidated income statement

| For the year ended 30 September | Note | 2023 £m | 2022 £m |
|---|---|---|---|
| Interest income | | **3,830** | 2,215 |
| Other similar interest | | **3** | 2 |
| Interest expense and similar charges | | **(2,146)** | (641) |
| **Net interest income** | 2.1 | **1,687** | 1,576 |
| Gains less losses on financial instruments at fair value | | **(12)** | (17) |
| Other operating income | | **152** | 157 |
| **Non-interest income** | 2.2 | **140** | 140 |
| **Total operating income** | | **1,827** | 1,716 |
| Operating and administrative expenses before impairment losses | 2.3 | **(1,173)** | (1,069) |
| **Operating profit before impairment losses** | | **654** | 647 |
| Impairment losses on credit exposures | 3.1.1.1 | **(309)** | (52) |
| **Profit on ordinary activities before tax** | | **345** | 595 |
| Tax expense | 2.4 | **(99)** | (58) |
| **Profit for the year** | | **246** | 537 |
| | | | |
| **Attributable to:** | | | |
| Ordinary shareholders | | **192** | 467 |
| Other equity holders | | **54** | 70 |
| **Profit for the year** | | **246** | 537 |
| Basic earnings per share (pence) | 2.5 | **14.0** | 32.4 |
| Diluted earnings per share (pence) | 2.5 | **13.9** | 32.3 |

All items dealt with in arriving at the profit before tax for each year relate to continuing activities.

The notes on pages 78 to 121 form an integral part of these financial statements.

# Consolidated statement of comprehensive income

| For the year ended 30 September | Note | 2023 £m | 2022 £m |
|---|---|---|---|
| **Profit for the year** | | **246** | 537 |
| | | | |
| **Items that may be reclassified to the income statement** | | | |
| *Change in cash flow hedge reserve* | | | |
| (Losses)/gains during the year | | **(268)** | 962 |
| Transfers to the income statement | | **(12)** | (13) |
| Taxation thereon – deferred tax credit/(charge) | | **77** | (260) |
| | 4.1.5 | **(203)** | 689 |
| *Change in FVOCI reserve* | | | |
| (Losses)/gains during the year | | **(49)** | 15 |
| Transfers to the income statement | | **(1)** | (4) |
| Taxation thereon – deferred tax credit/(charge) | | **14** | (1) |
| | | **(36)** | 10 |
| **Total items that may be reclassified to the income statement** | | **(239)** | 699 |
| | | | |
| **Items that will not be reclassified to the income statement** | | | |
| *Change in defined benefit pension plan* | 3.3 | **(544)** | 122 |
| Taxation thereon – deferred tax credit/(charge) | | **188** | (50) |
| Taxation thereon – current tax credit | | **1** | 6 |
| **Total items that will not be reclassified to the income statement** | | **(355)** | 78 |
| | | | |
| **Other comprehensive (losses)/income, net of tax** | | **(594)** | 777 |
| **Total comprehensive (losses)/income for the year, net of tax** | | **(348)** | 1,314 |
| | | | |
| **Attributable to:** | | | |
| Ordinary shareholders | | **(402)** | 1,244 |
| Other equity holders | | **54** | 70 |
| **Total comprehensive (losses)/income for the year, net of tax** | | **(348)** | 1,314 |

The notes on pages 78 to 121 form an integral part of these financial statements.

# Consolidated balance sheet

| As at 30 September | Note | 2023 £m | 2022 £m |
|---|---|---|---|
| **Assets** | | | |
| *Financial instruments* | 3.1 | | |
| *At amortised cost* | 3.1.1 | | |
| Loans and advances to customers | 3.1.1.1 | **72,191** | 71,751 |
| Cash and balances with central banks | 3.1.1.2 | **11,282** | 12,221 |
| Due from other banks | | **667** | 656 |
| At FVOCI | 3.1.2 | **6,184** | 5,064 |
| *At FVTPL* | 3.1.3 | | |
| Loans and advances to customers | 3.1.3.1 | **59** | 70 |
| Derivatives | 3.1.3.2 | **135** | 342 |
| Other | 3.1.3.3 | **2** | 8 |
| Intangible assets and goodwill | 3.2 | **173** | 267 |
| Deferred tax | 2.4 | **193** | 146 |
| Defined benefit pension assets | 3.3 | **512** | 1,000 |
| Other assets | 1.7, 3.4 | **388** | 382 |
| **Total assets** | | **91,786** | 91,907 |
| **Liabilities** | | | |
| *Financial instruments* | 3.1 | | |
| *At amortised cost* | 3.1.1 | | |
| Customer deposits | 3.1.1.3 | **66,827** | 65,434 |
| Debt securities in issue | 3.1.1.4 | **9,719** | 8,509 |
| Due to other banks | 3.1.1.5 | **6,939** | 8,502 |
| *At FVTPL* | 3.1.3 | | |
| Derivatives | 3.1.3.2 | **290** | 327 |
| Deferred tax | 2.4 | **179** | 350 |
| Provisions for liabilities and charges | 3.7 | **69** | 50 |
| Other liabilities | 1.7, 3.5 | **2,156** | 2,395 |
| **Total liabilities** | | **86,179** | 85,567 |
| **Equity** | | | |
| Share capital and share premium | 4.1.1 | **143** | 148 |
| Other equity instruments | 4.1.2 | **594** | 666 |
| Capital reorganisation reserve | 4.1.3 | **(839)** | (839) |
| Merger reserve | 4.1.4 | **2,128** | 2,128 |
| Other reserves | 4.1.5 | **528** | 766 |
| Retained earnings | | **3,053** | 3,471 |
| **Total equity** | | **5,607** | 6,340 |
| **Total liabilities and equity** | | **91,786** | 91,907 |

The notes on pages 78 to 121 form an integral part of these financial statements.

These financial statements were approved by the Board of Directors on 22 November 2023 and were signed on its behalf by:

**David Duffy**
Chief Executive Officer

**Clifford Abrahams**
Chief Financial Officer

Virgin Money UK PLC, Registered number: 09595911

# Consolidated statement of changes in equity

| | Note | Share capital and share premium £m 4.1.1 | Other equity instruments £m 4.1.2 | Capital reorg' reserve £m 4.1.3 | Merger reserve £m 4.1.4 | Other reserves: Own shares held £m 4.1.5 | Other reserves: Capital redemption reserve £m 4.1.5 | Other reserves: Deferred shares reserve £m 4.1.5 | Other reserves: Equity based comp' reserve £m 4.1.5 | Other reserves: FVOCI reserve £m 4.1.5 | Other reserves: Cash flow hedge reserve £m 4.1.5 | Retained earnings £m | Total equity £m |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **As at 1 October 2021** | | 149 | 915 | (839) | 2,128 | – | – | 14 | 14 | 33 | 10 | 3,049 | 5,473 |
| Profit for the year | | – | – | – | – | – | – | – | – | – | – | 537 | 537 |
| Other comprehensive income, net of tax | | – | – | – | – | – | – | – | – | 10 | 689 | 78 | 777 |
| Total comprehensive income for the year | | – | – | – | – | – | – | – | – | 10 | 689 | 615 | 1,314 |
| AT1 distributions paid | | – | – | – | – | – | – | – | – | – | – | (70) | (70) |
| Dividends paid to ordinary shareholders | | – | – | – | – | – | – | – | – | – | – | (50) | (50) |
| Ordinary shares issued | | 2 | – | – | – | – | – | – | – | – | – | – | 2 |
| Share buyback | | (3) | – | – | – | – | 3 | – | – | – | – | (63) | (63) |
| Transfer from equity based compensation reserve | | – | – | – | – | – | – | – | (9) | – | – | 9 | – |
| Equity based compensation expensed | | – | – | – | – | – | – | – | 5 | – | – | – | 5 |
| Settlement of Virgin Money Holdings (UK) Limited share awards | | – | – | – | – | – | – | (3) | – | – | – | 1 | (2) |
| AT1 issuance | | – | 346 | – | – | – | – | – | – | – | – | – | 346 |
| AT1 redemption | | – | (595) | – | – | – | – | – | – | – | – | (20) | (615) |
| **As at 30 September 2022** | | 148 | 666 | (839) | 2,128 | – | 3 | 11 | 10 | 43 | 699 | 3,471 | 6,340 |
| Profit for the year | | – | – | – | – | – | – | – | – | – | – | 246 | 246 |
| Other comprehensive losses, net of tax | | – | – | – | – | – | – | – | – | (36) | (203) | (355) | (594) |
| Total comprehensive losses for the year | | – | – | – | – | – | – | – | – | (36) | (203) | (109) | (348) |
| AT1 distributions paid | | – | – | – | – | – | – | – | – | – | – | (54) | (54) |
| Dividends paid to ordinary shareholders | | – | – | – | – | – | – | – | – | – | – | (148) | (148) |
| Ordinary shares issued | | 2 | – | – | – | – | – | – | – | – | – | – | 2 |
| Share buyback | | (7) | – | – | – | – | 7 | – | – | – | – | (112) | (112) |
| Purchase of own shares | | – | – | – | – | (2) | – | – | – | – | – | – | (2) |
| Transfer from equity based compensation reserve | | – | – | – | – | – | – | – | (4) | – | – | 4 | – |
| Equity based compensation expensed | | – | – | – | – | – | – | – | 5 | – | – | – | 5 |
| Settlement of Virgin Money Holdings (UK) Limited share awards | | – | – | – | – | – | – | (5) | – | – | – | 1 | (4) |
| AT1 redemption | | – | (72) | – | – | – | – | – | – | – | – | – | (72) |
| **As at 30 September 2023** | | **143** | **594** | **(839)** | **2,128** | **(2)** | **10** | **6** | **11** | **7** | **496** | **3,053** | **5,607** |

The notes on pages 78 to 121 form an integral part of these financial statements.

# Consolidated statement of cash flows

| For the year ended 30 September | Note | 2023 £m | 2022 £m |
|---|---|---|---|
| **Operating activities** | | | |
| Profit on ordinary activities before tax | | **345** | 595 |
| *Adjustments for:* | | | |
| Non-cash or non-operating items included in profit before tax | 5.4 | **(1,207)** | (1,326) |
| Changes in operating assets | 5.4 | **(544)** | 1,212 |
| Changes in operating liabilities | 5.4 | **284** | (238) |
| Payments for short-term and low value leases | 3.6 | **(3)** | (2) |
| Interest received | | **3,300** | 2,112 |
| Interest paid | | **(1,173)** | (378) |
| Tax paid | | **(48)** | (59) |
| **Net cash provided by operating activities** | | **954** | 1,916 |
| **Cash flows from investing activities** | | | |
| Interest received | | **232** | 47 |
| Proceeds from sale and maturity of financial assets at FVOCI | | **1,868** | 673 |
| Purchase of financial assets at FVOCI | | **(2,950)** | (2,019) |
| Purchase of shares issued by UTM | | **–** | (4) |
| Proceeds from sale of property, plant and equipment | | **1** | 1 |
| Purchase of property, plant and equipment | | **(9)** | (13) |
| Purchase and development of intangible assets | 3.2 | **(11)** | (53) |
| **Net cash used in investing activities** | | **(869)** | (1,368) |
| **Cash flows from financing activities** | | | |
| Interest paid | | **(742)** | (246) |
| Repayment of principal portions of lease liabilities | 3.6 | **(24)** | (26) |
| Redemption and principal repayment on RMBS and covered bonds | 3.1.1.4 | **(1,012)** | (1,264) |
| Redemption and principal repayment on medium-term notes/subordinated debt | 3.1.1.4 | **(432)** | – |
| Redemption of AT1 securities | | **(72)** | (614) |
| Proceeds from issuance of AT1 securities | | **–** | 347 |
| Issuance of RMBS and covered bonds | 3.1.1.4 | **1,826** | 2,480 |
| Issuance of medium-term notes/subordinated debt | 3.1.1.4 | **747** | – |
| Amounts drawn down under the TFSME | | **–** | 2,550 |
| Amounts repaid under the TFSME | | **(1,000)** | – |
| Amounts repaid under the TFS | | **–** | (1,244) |
| Share buybacks and purchase of own shares | | **(112)** | (53) |
| AT1 distributions | 4.1.2 | **(54)** | (70) |
| Ordinary dividends paid | | **(148)** | (50) |
| **Net cash (used in)/provided by financing activities** | | **(1,023)** | 1,810 |
| **Net (decrease)/increase in cash and cash equivalents** | | **(938)** | 2,358 |
| Cash and cash equivalents at the beginning of the year | | **12,611** | 10,253 |
| **Cash and cash equivalents at the end of the year** | 5.4 | **11,673** | 12,611 |

# Consolidated statement of cash flows

### Movements in liabilities arising from financing activities

| | Note | Term funding schemes[1] £m 3.1.1.5 | Debt securities in issue £m 3.1.1.4 | Lease liabilities £m 3.6 | Total £m |
|---|---|---|---|---|---|
| **At 1 October 2021** | | 5,896 | 7,678 | 154 | 13,728 |
| **Cash flows:** | | | | | |
| Issuances | | – | 2,480 | – | 2,480 |
| Drawdowns | | 2,550 | – | – | 2,550 |
| Redemptions | | – | (1,264) | – | (1,264) |
| Repayment | | (1,244) | – | (26) | (1,270) |
| **Non-cash flows:** | | | | | |
| Fair value and other associated adjustments | | – | (400) | – | (400) |
| Additions to right-of-use asset in exchange for increased lease liabilities | | – | – | 4 | 4 |
| Remeasurement | | – | – | (4) | (4) |
| Movement in accrued interest | | 28 | 8 | 4 | 40 |
| Unrealised foreign exchange movements | | – | 5 | – | 5 |
| Unamortised costs | | – | 2 | – | 2 |
| **At 30 September 2022** | | 7,230 | 8,509 | 132 | 15,871 |
| **Cash flows:** | | | | | |
| Issuances | | – | 2,573 | – | 2,573 |
| Redemptions | | – | (1,444) | – | (1,444) |
| Repayment | | (1,000) | – | (24) | (1,024) |
| Tax paid | | – | – | (1) | (1) |
| **Non-cash flows:** | | | | | |
| Fair value and other associated adjustments | | – | 59 | – | 59 |
| Additions to right-of-use asset in exchange for increased lease liabilities | | – | – | 76 | 76 |
| Remeasurement | | – | – | (6) | (6) |
| Movement in accrued interest | | 61 | 27 | 3 | 91 |
| Unamortised costs | | – | (5) | – | (5) |
| **At 30 September 2023** | | **6,291** | **9,719** | **180** | **16,190** |

(1) This includes amounts drawn under the TFS and TFSME.

The notes on pages 78 to 121 form an integral part of these financial statements.

# Notes to the consolidated financial statements

## Section 1: Basis of preparation

**Overview**

This section sets out the Group's accounting policies that relate to the consolidated financial statements as a whole. Where an accounting policy is specific to one note, the policy is described in the note to which it relates. This section also highlights newly adopted accounting standards, amendments and interpretations which are relevant to the Group. Where relevant, we explain how these changes are expected to impact the financial position and performance of the Group.

The Group has adopted the UK Finance Code for Financial Reporting Disclosure and has prepared the 2023 Annual Report and Accounts in compliance with the Code.

### 1.1 General information

The Company is a public company limited by shares, incorporated in the United Kingdom under the Companies Act and registered in England and Wales.

The consolidated financial statements comprise those of the Company and its controlled entities, together the 'Group'

### 1.2 Basis of accounting

The consolidated financial statements, have been prepared in accordance with UK adopted IASs.

The financial information has been prepared under the historical cost convention, as modified by the revaluation of certain financial assets and liabilities at fair value through profit or loss and other comprehensive income. Fair value is defined in note 3.1.4.

### 1.3 Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position, are set out in the Strategic report contained in the Group's Annual Report and Accounts. In addition, the full Risk report contained in the Group's Annual Report and Accounts includes the Group's risk management objectives and the objectives, policies and processes for managing its capital.

In assessing the Group's going concern position as at 30 September 2023, the Directors have considered a number of factors, including the current balance sheet position (which reflected the Group's consideration of the potential impact of climate-related risks), the Group's strategic and financial plan, taking account of possible changes in trading performance and funding retention, and stress testing and scenario analysis. The assessment concluded that the Group has sufficient capital and liquidity for at least the next 12 months. The Group's capital ratios and its total capital resources are comfortably in excess of PRA requirements and internal stress testing indicates the Group can withstand severe economic and competitive stresses.

As a result of the assessment, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future and that the Group is well placed to manage its business risks successfully. Accordingly, they continue to adopt the going concern basis in preparing the consolidated financial statements.

The Directors' report contained in the Group's Annual Report and Accounts provides further detail on the Group's going concern and viability assessment.

### 1.4 Basis of consolidation

Controlled entities are all entities (including structured entities) to which the Company is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. An assessment of control is performed if there are indicators that control may have changed.

Controlled entities are consolidated from the date on which control is established by the Group until the date that control ceases. The acquisition method of accounting is used to account for business combinations other than those under common control. A non-controlling interest is recognised by the Group in respect of any portion of the total assets less total liabilities of an acquired entity or entities that is not owned by the Group. Balances and transactions between entities within the Group and any unrealised gains and losses arising from those transactions are eliminated in full upon consolidation.

The consolidated financial statements have been prepared using uniform accounting policies.

### 1.5 Critical accounting estimates and judgements

The preparation of financial statements requires the use of certain critical accounting estimates and judgements that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosed amount of contingent liabilities. Actual results may differ from those on which management's estimates are based. Estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable.

# Section 1: Basis of preparation

The Group considers the most significant use of accounting estimates and judgements relate to the following areas:

| Area | Estimates | Judgements | Further detail |
|---|---|---|---|
| Impairment provisions on credit exposures | Asset lifetimes<br>Economic scenarios | SICR<br>Definition of default<br>PMAs | Credit risk section of Risk management and note 3.1.1.1 |
| EIR | Product life<br>Post promotion attrition and yield | Standard variable rate<br>Macroeconomic factors<br>Model risk reserve (MRR) | Note 2.1 |
| Deferred tax | | Period for the recoverability of deferred tax assets | Note 2.4 |
| Retirement benefit obligations | Discount rate<br>Inflation assumptions<br>Mortality assumptions | | Note 3.3 |

**Critical accounting estimates and judgements related to climate-related risks**
In addition, management has also considered and reflected on the potential impact of climate-related risks on the Group's financial position and performance.

This involved undertaking an assessment over the Group's assets (both financial and non-financial) and evaluating whether the observable effects of physical and transition risk of climate change would have a material impact on the Group's financial position and performance in the current year. It is widely accepted that the effects of climate change in the UK will not be significant in the short term and that the inherent risks and uncertainties in quantifying the effect of climate change in the financial statements are considerable and more likely to impact in the medium to longer term.

The Group's customer lending is the most significant financial asset class exposed to the potential impact of climate-related risks, primarily through ECL implications, the ability of the customer to meet their contractual payments and the potential for a fall in collateral values. Given the challenges associated with modelling specific climate projections, the Group's IFRS 9 scenarios do not make explicit and objective assumptions about climate change impacts for which the associated probability can be derived within the existing methodology. Instead, the Group's base forecast, and therefore the scenarios, incorporate the short to medium-term (five-year horizon) impact of the domestic and global economy on demand for fossil fuel and thus emissions. Consequently we consider that as a UK-based bank with no significant lending outside of the UK, the potential for material ECLs to emerge as a result of climate change in the short term is negligible.

Other non-financial assets that may be impacted include the Group's deferred tax asset and the pension assets held by the Group's defined benefit pension scheme. The Group assesses the recoverability of deferred tax assets over a six-year corporate planning time horizon which incorporates all aspects of the Group's future performance and expectations. The Trustee of the defined benefit pension scheme is responsible for all investment decisions, and these are made in accordance with a SIP which incorporates climate change considerations. In addition, by necessity, the investment decisions made by the Trustees are normally medium to long term in nature to match the related pension obligations. The majority of the scheme assets held at 30 September 2023 are in lower risk government and corporate bonds, with the remaining investments in secure income alternatives, property and renewables. As its funding position has improved it has disinvested from some of the asset classes that were more exposed to climate risks (such as public equity), but the Scheme is increasingly holding a larger proportion of longer dated assets to better match its liabilities. The Trustee is therefore very focused on the sustainability of these assets.

Overall, while the effects of climate change represent a source of significant uncertainty, the Group does not consider there to be a material impact on its estimates and judgements from physical and transition risks of climate change in these financial statements.

## 1.6 New accounting standards and interpretations

The Group adopted the following International Accounting Standards Board (IASB) pronouncements in the current financial year, which have been endorsed for use in the UK by the UK Endorsement Board (UKEB), and are not considered to have a material impact for the Group:

- Amendments to IAS 16 'Property, plant and equipment': proceeds before intended use. This was issued in May 2020 (applicable for accounting periods beginning on or after 1 January 2022) and received endorsement for use in the UK in April 2022. The amendments prohibit a company from deducting from the cost of property, plant and equipment amounts received from selling items produced while the company is preparing the asset for its intended use. Instead, a company will recognise such sales proceeds and related cost in profit or loss.
- Amendments to IAS 37 'Provisions, contingent liabilities and contingent assets': onerous contracts – cost of fulfilling a contract. This was issued in May 2020 (applicable for accounting periods beginning on or after 1 January 2022) and received endorsement for use in the UK in April 2022. The amendments clarify that for the purpose of assessing whether a contract is onerous, the cost of fulfilling the contract includes both the incremental costs of fulfilling that contract and an allocation of other costs that relate directly to fulfilling contracts.
- Amendments to IFRS 3 'Business combinations'. This was issued in May 2020 and received endorsement for use in the UK in April 2022. The amendments update IFRS 3 to refer to the 2018 Conceptual Framework for Financial Reporting, in order to determine what constitutes an asset or a liability in a business combination and applies to those business combinations for which the acquisition date is on or after the start of the first annual reporting period beginning on or after 1 January 2022.

- Annual improvements 2018-2020. This was issued in May 2020 (applicable for accounting periods beginning on or after 1 January 2022) and received endorsement for use in the UK in April 2022. The annual improvements package includes the following minor amendments to: (i) IFRS 1 'First-time adoption of IFRS' – Subsidiary as a first-time adopter; (ii) IFRS 9 'Financial instruments' – Fees in the '10%' test for derecognition of financial liabilities; (iii) IFRS 16 'Leases' – Lease incentives; and (iv) IAS 41 'Agriculture' – Taxation in fair value measurements.
- International tax reform – Pillar Two model rules: Amendments to IAS 12. This was issued in May 2023 (additional disclosure requirements are applicable for accounting periods beginning on or after 1 January 2023, although some paragraphs were for immediate application) and received endorsement for use in the UK in July 2023. The amendments introduce a mandatory temporary exception to the accounting for deferred taxes arising from the implementation of the OECD Pillar Two model rules, together with targeted disclosure requirements for affected entities. As mandated, the Group applied the temporary exemption on adoption and has neither recognised nor disclosed information about deferred tax assets and liabilities related to Pillar Two income taxes.

During the year, the Group also early adopted Amendments to IAS 1 'Presentation of financial statements' and IFRS Practice Statement 2 'Making materiality judgements' which was issued by the IASB in February 2021 (applicable for accounting periods beginning on or after 1 January 2023 with early adoption permitted) and endorsed for use in the UK by the UKEB in November 2022.

The amendments require entities to disclose their material accounting policy information rather than their significant accounting policies. As part of this, the IASB has amended IFRS Practice Statement 2 'Making materiality judgements' by adding guidance and examples of circumstances to help entities determine when accounting policy information is material and, therefore, needs to be disclosed.

The Group has assessed the requirements of the amendments and concluded that the disclosure of certain accounting policies included within the 2022 Annual Report and Accounts would no longer be necessary. Consequently, while the Group continues to apply these policies, the following accounting policy wording has been omitted by early adopting the amendments:

- Basis of consolidation: joint ventures (JVs).
- Foreign exchange: functional and presentation currency/transactions and balances.
- Property, plant and equipment.
- Operating and administrative expenses before impairment losses.
- Taxation: income tax/current tax.
- Intangibles and goodwill: capitalised software/goodwill/impairment.
- Retirement benefits: defined contribution scheme.
- Provisions.
- Other liabilities: deferred grants.
- Leases: as lessee/as sub-lessor.
- Equity: equity/dividends.
- Equity based compensation.
- Contingent liabilities.
- Investment in controlled entities (this policy relates to the Company financial statements).

**New accounting standards and interpretations not yet adopted**
The IASB has issued a number of other minor amendments to IFRSs that are not mandatory for the current reporting year and have not been early adopted by the Group. These amendments are not expected to have a material impact for the Group.

### 1.7 Other accounting policy and presentational changes
The following changes took place during the year:

**Investment property**
IAS 40 'Investment property' allows an entity to select either the fair value model or the cost model for subsequent measurement of investment property. The Group has a historic policy of fair value measurement for investment property but has not held any on its balance sheet for several years prior to the current year.

During the year, the Group has classified £43m of lease right-of-use assets as investment property on initial recognition where there is surplus space which will be sub-let under an operating lease. The Group has also transferred freehold land and buildings with a value of £9m to investment property where there was a change in use. Investment property balances are included within other assets on the balance sheet (note 3.4).

From 1 October 2022 investment property has been recognised at cost, less accumulated depreciation and impairment. The holding of investment property is not a central element of the Group's overarching business model or strategy; it is an incidental consequence of surplus estate arising from changes in operational requirements. Considering the relative materiality and nature of investment property balances, the Group has determined that changing the accounting policy for investment property to align to the measurement basis, which is applied to the Group's other property related assets under IFRS 16 'Leases' and IAS 16 'Property, plant and equipment', will provide greater relevance and consistency to users of the financial statements. This policy change has no impact on prior years.

**Expected credit losses**
During the year, a new Business LGD model was brought into use in the Group's ECL calculation. The development of this model was at an advanced stage in the prior year, to the extent that a negative management adjustment of £15m was incorporated into the ECL figure. The introduction of the new model allowed this negative management adjustment to be removed in the current year. Further detail can be found in the credit risk section within Risk management, pages 36 and 45.

# Section 1: Basis of preparation

**Presentational change**

Other assets and other liabilities have been restated in the prior year in line with the current year presentation. The balance sheet line items for property, plant and equipment and current tax have been removed and the balances assumed into the other assets and other liabilities line items respectively. This is a presentational change to align with peers and is not considered to be a material change in disclosure. The table below reflects the impact of these changes on the balances at 30 September 2022:

| | Other assets £m | Other liabilities £m |
|---|---|---|
| Original balance | 171 | 2,394 |
| Property, plant and equipment | 211 | – |
| Current tax | – | 1 |
| Restated balance | 382 | 2,395 |

# Section 2: Results for the year

## 2.1 Net interest income

**Accounting policy**
Interest income is recognised using the effective interest method which discounts the estimated future cash payments or receipts, at the effective interest rate, over the expected life of the financial instrument to the gross carrying amount of the non-credit impaired financial asset. Interest expense is recognised using the same effective interest method on the amortised cost of the financial liability.

When calculating the EIR, cash flows are estimated considering all contractual terms of the financial instrument (e.g. prepayment, call and similar options) excluding future credit losses. The calculation includes all amounts paid or received that are an integral part of the EIR such as transaction costs and all other premiums or discounts. Where it is not possible to reliably estimate the cash flows or the expected life of a financial instrument (or group of financial instruments), the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments) are used.

Loan origination and commitment fees are recognised within the EIR calculation. Fees in relation to the non-utilisation of a commitment are recognised as revenue upon expiry of the agreed commitment period.

Interest income on financial assets in Stages 1 and 2 is recognised on the gross carrying value of the financial asset using the original EIR. Once a financial asset or group of similar financial assets has been categorised as credit-impaired (Stage 3), interest income is recognised on the net carrying value (which is after deducting the ECL allowance from the gross lending) using the asset's original EIR. Interest income for POCI financial assets is calculated using the credit-adjusted EIR applied to the amortised cost of the financial asset from initial recognition. The Group recognises and presents the reversal of ECLs following the curing of a credit impaired financial asset as a reversal of impairment losses. The Group's policy on ECLs can be found in note 3.1.1.

Interest income includes finance lease income, which is recognised at a constant periodic rate of return on the net investment.

Interest income and interest expense on hedged assets and liabilities and financial assets and liabilities designated as FVTPL are also recognised as part of NII.

Interest income and interest expense on derivatives economically hedging interest bearing financial assets or liabilities (but not designated as hedging instruments) and other financial assets and liabilities held at FVTPL (either mandatory or by election) are presented as other similar interest within NII.

**Critical accounting estimates and judgements**
***EIR***
The EIR is determined at initial recognition based upon the Group's best estimate of the future cash flows of the financial instrument over its expected life. Where these estimates are subsequently revised, a present value adjustment to the carrying value of the asset is recognised in profit or loss. Such adjustments can introduce income statement volatility and consequently the EIR method is a source of estimation uncertainty.

The Group considers that significant judgement is exercised over the mortgage and credit card portfolios. Due to the inherent judgement and estimation uncertainty that exists in determining the EIR adjustment, an MRR is held to mitigate this uncertainty.

The Group assesses the quantification of the EIR adjustment, including the MRR, on a quarterly basis with the CFO making recommendations to the Board Audit Committee twice a year at each external reporting period.

***Mortgages***
For mortgage products the main accounting estimates and judgements when assessing the cash flows are the product life (including assumptions based on observed historic customer behaviour when in a standard variable rate (SVR) period) and the applicable SVR. As at 30 September 2023, a total EIR adjustment of £209m (2022: £201m) has been recognised for mortgages. This represented 0.4% (2022: 0.3%) of the balance sheet carrying value of gross loans and advances to customers for mortgage lending. The net impact of the mortgage EIR adjustments on the income statement in the year represented 0.5% of gross customer interest income for mortgages (2022: (0.7)%).

*Product life*
This primarily involves assumptions of customer behaviour when a fixed rate product comes to an end and reverts to the Group's SVR. The current assumptions indicate that 89% (2022: 85%) of customers will have fully repaid or switched to a new product within two months of reverting to SVR.

*SVR*
Changes to the BoE base rate have an impact on the SVR charged to customers and consequently on the Group's interest income. The Group historically passes base rate changes through to the SVR in full but, on occasion, may choose not to do so.

The significant accounting estimates above are monitored on an ongoing basis to ensure they remain appropriate based on recent, observable customer behaviour, market data (such as market derived base rate forecasts) and take account of the competitive environment in which the Group operates. The Group also considers potential changes to future customer behaviour as a result of macroeconomic factors. There continues to be increased uncertainty in purchase and switching activity as a result of actual and anticipated base rate rises. The Group has taken this into account when determining the EIR modelling assumptions.

### 2.1 Net interest income continued

*Sensitivity analysis*
As noted above, the calculation of the Group's EIR adjustment is sensitive to changes in product life and SVR assumptions. There are inter-dependencies between the assumptions which add to the complexity of the judgements the Group has to make. This means that no single factor is likely to move independently of others, however, the sensitivities disclosed below assume all other assumptions remain unchanged.

| Sensitivity impact on the mortgage EIR adjustment | 2023 £m | 2022 £m |
|---|---|---|
| +/- 1 month change to the timing of customer repayments, redemptions and product transfers | **21/(18)** | 16/(13) |
| 50bps increase to the BoE base rate not passed through to the Group's SVR | **(42)** | (46) |

***Credit cards***
An EIR adjustment arises on credit card products that have a low introductory rate, followed by a higher reversionary rate in future years when the promotional period expires. However, receipt of such interest income depends on the customer staying with the Group beyond promotional expiry and therefore significant judgement is involved in forecasting customer behaviour and estimating the future cash flows. Key behavioural assumptions include an estimation of the utilisation of available credit, transaction and repayment activity and the retention of the customer balance after the end of a promotional period. As at 30 September 2023, a total EIR adjustment of £259m (2022: £285m) has been recognised for credit cards. This represented 4.5% (2022: 5.5%) of the balance sheet carrying value of gross loans and advances to customers for credit cards. The impact of the net credit card EIR adjustments on the income statement was a charge in the year representing (6.2)% of gross customer interest income for credit cards (2022: a credit representing 3.3% of gross customer interest income for credit cards).

Expected cash flows are estimated based on historical experience of similar products and are consistent with those used in product pricing models. The Group reviews and adjusts assumptions where necessary on an ongoing basis, using the most recent observable customer behaviour and market data. The Group also considers potential future changes to customer behaviour as a result of macroeconomic factors.

*Post-promotional yield*
The yield on a credit card following the post-promotional period is a significant estimate within the EIR assumptions. Yield is a function of the Interest Bearing Balance (IBB) and the APR charged to customers. IBB is impacted by customer behaviour and while there is evidence to support the expected IBB following the post-promotional period, there is inherent risk that this data may differ in the future. If the IBB differs to the Group's estimate it can have a material impact on the revised future cash flows. Based on recent experience, the Group has applied an average IBB of 55% (2022: 55%) following the end of the promotional period.

*Post-promotional attrition*
The level of repayment in the post-promotional period is a key sensitivity within the EIR assumptions. There is evidence to support the expected behaviour of customers after the end of promotional periods, however there is inherent risk that this data may not be indicative of actual future behaviour. If the proportion of customers who repay their balance post-promotion differs to the Group's estimate it can have a material impact on the revised future cash flows. Based on recent experience, the Group has applied a long run average attrition rate of 1.5% per month (2022: 1.5% per month) following the end of the promotional period.

*Macroeconomic factors*
When determining assumptions, the Group has considered the impact to customers of inflationary pressures including high energy and utility costs and the recent base rate rises. As a result, temporary adjustments have been made to assumptions. Post-promotional IBB has been decreased to 50% for 18 months and balance attrition has been increased to reflect customer reaction to the high-rate environment for 18 months. If, however, the stress period was to increase to 30 months, the Group estimates it would result in a negative present value adjustment of approximately £19m, which would be recognised in the income statement.

*Sensitivity analysis*
As noted above, the calculation of the Group's EIR adjustment for credit cards is sensitive to changes in post-promotional yield and post-promotional attrition. There are inter-dependencies between the key assumptions which add to the complexity of the judgements the Group has to make. This means that no single factor is likely to move independently of others, however, the sensitivities disclosed below assume all other assumptions remain unchanged.

| Sensitivity impact on the credit card EIR adjustment | 2023 £m | 2022 £m |
|---|---|---|
| +/- 5 ppts change to post-promotional IBB assumption(1) (9.1% relative increase/decrease) | **25/(26)** | 34/(28) |
| +/- 0.5 ppts change to post-promotional monthly balance attrition rate (33% relative increase/decrease) | **(7)/7** | (20)/23 |

(1) Where the IBB assumption is already equal to or less than 50% IBB, no further adjustment has been made on the basis this already represents a downside economic stress.

## Section 2: Results for the year

### 2.1 Net interest income continued

| | 2023 £m | 2022 £m |
|---|---|---|
| **Interest income** | | |
| Loans and advances to customers | **3,150** | 2,095 |
| Loans and advances to other banks | **435** | 70 |
| Financial assets at FVOCI | **245** | 50 |
| **Total interest income** | **3,830** | 2,215 |
| | | |
| **Other similar interest** | | |
| Financial assets at FVTPL | **3** | 5 |
| Derivatives economically hedging interest bearing assets | **–** | (3) |
| **Total other similar interest** | **3** | 2 |
| | | |
| **Less: interest expense and similar charges** | | |
| Customer deposits | **(1,233)** | (342) |
| Debt securities in issue | **(537)** | (227) |
| Due to other banks | **(372)** | (70) |
| Other interest expense | **(4)** | (2) |
| **Total interest expense and similar charges** | **(2,146)** | (641) |
| **Net interest income** | **1,687** | 1,576 |

Net interest income includes a charge of £29m (2022: £16m) in relation to acquisition accounting unwinds as shown in the reconciliation of statutory to underlying results table on page 17.

### 2.2 Non-interest income

**Accounting policy**
***Gains less losses on financial instruments at fair value***
This includes fair value gains and losses from three distinct activities:

- Derivatives classified as held for trading – the full change in fair value of trading derivatives is recognised inclusive of interest income and interest expense arising on those derivatives except when economically hedging other assets and liabilities at fair value as outlined in note 2.1.
- Other financial assets designated at FVTPL – these relate principally to the Group's fixed interest rate loan portfolio (note 3.1.3.1), which were designated at inception as FVTPL. The fair value of these loans is derived from the future loan cash flows using appropriate discount rates and includes adjustments for credit risk and credit losses.
- Hedged assets, liabilities and derivatives designated in hedge relationships – fair value movements are recognised on both the hedged item and hedging derivative in a fair value hedge relationship, the net of which represents hedge ineffectiveness, and hedge ineffectiveness on cash flow hedge relationships (note 3.1.3.2).

***Fees and commissions***
Fees and commissions receivable which are not an integral part of the EIR are recognised as income as the Group fulfils its performance obligations. The Group's principal performance obligations arising from contracts with customers are in respect of current accounts, debit cards and credit cards. The Group provides the service and consequently generates the fee and commission income monthly, with amounts recognised in income on this basis. Costs incurred to generate this income are charged to fees and commissions expense as they are incurred.

# Section 2: Results for the year

## 2.2 Non-interest income continued

| | 2023 £m | 2022 £m |
|---|---|---|
| **Gains less losses on financial instruments at fair value** | | |
| Held for trading derivatives | **1** | 6 |
| Financial assets at fair value[1] | **2** | (19) |
| Ineffectiveness arising from fair value hedges (note 3.1.3.2) | **33** | 46 |
| Amounts recycled to profit and loss from cash flow hedges[2] (note 3.1.3.2) | **2** | (4) |
| Ineffectiveness arising from cash flow hedges (note 3.1.3.2) | **(50)** | (46) |
| | **(12)** | (17) |
| **Other operating income** | | |
| Net fee and commission income | **128** | 134 |
| Margin on foreign exchange derivative brokerage | **19** | 19 |
| Gains on sale of financial assets at FVOCI | **1** | 4 |
| Share of JV loss after tax | **–** | (4) |
| Other income | **4** | 4 |
| | **152** | 157 |
| **Total non-interest income** | **140** | 140 |

(1) Included within financial assets at fair value is a credit risk gain on loans and advances at fair value of £Nil (2022: £1m gain), and a fair value gain on equity investments of £2m (2022: £2m gain).
(2) In respect of terminated hedges.

The Group's unrecognised share of losses of JVs for the year was £6m (2022: £8m). For loss-making entities, subsequent profits earned are not recognised until previously unrecognised losses are extinguished. On a cumulative basis, the Group's unrecognised share of losses net of unrecognised profits of JVs is £15m (2022: £9m).

Non-interest income includes the following fee and commission income disaggregated by income type:

| | 2023 £m | 2022 £m |
|---|---|---|
| Current account and debit card fees | **100** | 102 |
| Credit cards | **63** | 52 |
| Insurance, protection and investments | **7** | 8 |
| Other fees[1] | **16** | 26 |
| Total fee and commission income | **186** | 188 |
| Total fee and commission expense | **(58)** | (54) |
| **Net fee and commission income** | **128** | 134 |

(1) Other fees include mortgages, invoice and asset finance and ATM fees.

## 2.3 Operating expenses

| | 2023 £m | 2022 £m |
|---|---|---|
| Staff costs | **432** | 435 |
| Property and infrastructure | **74** | 38 |
| Technology and communications | **130** | 119 |
| Corporate and professional services | **240** | 135 |
| Depreciation, amortisation and impairment | **116** | 179 |
| Other expenses | **181** | 163 |
| **Total operating and administrative expenses** | **1,173** | 1,069 |

# Section 2: Results for the year

## 2.3 Operating expenses continued

Staff costs comprise the following items:

| | 2023 £m | 2022 £m |
|---|---|---|
| Salaries and wages | **275** | 254 |
| Social security costs | **32** | 30 |
| Defined contribution pension expense | **56** | 50 |
| Defined benefit pension credit (note 3.3) | **(50)** | (24) |
| **Compensation costs** | **313** | 310 |
| Equity based compensation(1) | **6** | 4 |
| Bonus awards | **22** | 27 |
| **Performance costs** | **28** | 31 |
| Redundancy and restructuring | **7** | 3 |
| Temporary staff costs | **24** | 13 |
| Other(2) | **60** | 78 |
| **Other staff costs** | **91** | 94 |
| **Total staff costs** | **432** | 435 |

(1) Includes National Insurance on equity based compensation.

(2) Includes a one-off cost of living allowance of £Nil (2022: £7m).

Phase 2 of the ongoing Pension Increase Exchange (PIE) exercise completed in FY22, and the third and final phase is due to complete in the final quarter of calendar year 2023. The defined benefit pension credit in the current year therefore includes no impact (2022: £10m credit) arising from the PIE exercise. A PIE gives members the option to exchange future increases on their pensions for a one-off uplift to their current pension.

The average number of FTE employees of the Group during the year was made up as follows:

| | 2023 Number | 2022 Number |
|---|---|---|
| Managers(1) | **3,436** | 2,574 |
| Clerical staff | **3,730** | 4,292 |
| | **7,166** | 6,866 |

(1) Includes a combination of managers with and without staff responsibilities.

The average monthly number of employees was 8,110 (2022: 7,829). All staff are contracted employees of the Group and its subsidiary undertakings. The average figures above do not include contractors.

Auditor’s remuneration included within other operating and administrative expenses:

| | 2023 £'000 | 2022 £'000 |
|---|---|---|
| Fees payable to the Company’s auditor for the audit of the Company’s financial statements | **25** | 24 |
| Fees payable to the Company’s auditor for the audit of the Company’s subsidiaries(1) | **4,787** | 4,564 |
| Total audit fees | **4,812** | 4,588 |
| Audit related assurance services | **562** | 262 |
| Other assurance services | **276** | 1,877 |
| Total non-audit fees | **838** | 2,139 |
| Fees payable to the Company’s auditor in respect of associated pension schemes | **126** | 107 |
| Total fees payable to the Company’s auditor | **5,776** | 6,834 |

(1) Includes the audit of the Group’s structured entities.

Non-audit fees of £1m (2022: £2m) were paid to the auditor during the year for services including UN PRB and the second Payment Services Directive assurance, the review of the Interim Financial Report, PRA Written Auditor Reporting, comfort letters for the global medium-term note and covered bond programmes, client money reviews and profit attestations.

Out of pocket expenses of £26k (2022: £13k) were borne by the Group during the year.

### 2.4 Taxation

**Accounting policy**
Deferred tax assets and liabilities are recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax is determined using tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised, or the deferred tax liability is settled.

A deferred tax asset is recognised for unused tax losses and unused tax credits only if it is probable that future taxable amounts will arise against which those temporary differences and losses may be utilised.

***Critical accounting estimates and judgements***
In arriving at the Group's deferred tax asset balance of £193m (2022: £146m), significant judgement is exercised on the component of deferred tax assets that relate to tax losses carried forward of £267m (2022: £302m).

Consistent with prior years, deferred tax assets are recognised to the extent that they are expected to be utilised over six years from the balance sheet date. Gross losses of £83m are not forecast to reverse within this period and have been derecognised (2022: £Nil). If instead of six years the period were five years or seven years, the recognised deferred tax asset would decrease to £148m or increase to £213m respectively, with the latter being full recognition of all losses. If Group profit forecasts were 10% lower than anticipated, the deferred tax asset would be £168m. If Group profit forecasts were 10% higher than anticipated, the deferred tax asset would be £213m. All tax assets arising will be used within the UK.

| | 2023 £m | 2022 £m |
|---|---|---|
| **Current tax** | | |
| Current year | **36** | 81 |
| Adjustment in respect of prior years | **2** | 4 |
| | **38** | 85 |
| **Deferred tax** | | |
| Current year | **65** | (21) |
| Adjustment in respect of prior years | **(4)** | (6) |
| | **61** | (27) |
| **Tax expense for the year** | **99** | 58 |

The tax assessed for the year differs from that arising from applying the standard rate of corporation tax in the UK of 22% (2022: 19%). 22% is the average standard rate for the full financial year, comprising 19% to 1 April 2023 then 25% to 30 September 2023. A reconciliation from the expense implied by the standard rate to the actual tax expense is as follows:

| | 2023 £m | 2022 £m |
|---|---|---|
| Profit on ordinary activities before tax | **345** | 595 |
| Tax expense based on the standard rate of corporation tax in the UK of 22% (2022: 19%) | **76** | 113 |
| *Effects of:* | | |
| Disallowable expenses | **5** | 4 |
| Conduct indemnity adjustment | **(1)** | (12) |
| Deferred tax assets derecognised/(recognised) | **19** | (83) |
| Impact of rate changes | **9** | 23 |
| AT1 distribution | **(12)** | (13) |
| Banking surcharge | **5** | 28 |
| Adjustments in respect of prior years | **(2)** | (2) |
| **Tax expense for the year** | **99** | 58 |

In February 2022 legislation was enacted to reduce the banking surcharge from 8% to 3%, and to increase the threshold below which it is not chargeable to £100m (previously £25m). The impact on deferred tax was reflected in the large rate change charge for the year ended 30 September 2022. The changes are effective for current tax from 1 April 2023 resulting in an average tax rate for the year of 22% (comprising 19% for the six months to 1 April 2023 then 25% to 30 September 2023).

# Section 2: Results for the year

## 2.4 Taxation continued

The Group's effective tax rate is 28.7% (2022: 9.7%). The primary driver of this is the derecognition of losses following a reduction in forecast profits over the corporate planning horizon, and a fall in the cash flow hedge reserve due to market conditions. The current period rate change charge of £9m arises mainly in relation to the defined benefit pension scheme, where current period amounts that are recognised in the income statement are reflected at 22%, while the deferred tax liability on the ultimate accounting surplus is measured at 35%. The Group has recognised deferred tax in relation to the following items in the balance sheet, income statement, and statement of other comprehensive income:

**Movement in deferred tax asset/(liability)**

| | Acquisition accounting adjustments £m | Cash flow hedge reserve £m | Gains on financial instruments at FVOCI £m | Tax losses carried forward £m | Capital allowances £m | Pension spreading £m | Other temporary differences £m | Total deferred tax assets £m | Defined benefit pension scheme surplus £m | Total deferred tax liabilities £m |
|---|---|---|---|---|---|---|---|---|---|---|
| At 1 October 2021 | (10) | (9) | (15) | 255 | 124 | 5 | 27 | 377 | (296) | (296) |
| Income statement credit/(charge) | 2 | 2 | – | 47 | (13) | – | (2) | 36 | (9) | (9) |
| Other comprehensive income charge | – | (260) | (1) | – | – | (5) | (1) | (267) | (45) | (45) |
| At 30 September 2022 | (8) | (267) | (16) | 302 | 111 | – | 24 | 146 | (350) | (350) |
| Income statement credit/(charge) | 2 | 1 | – | (35) | (8) | – | (4) | (44) | (17) | (17) |
| Other comprehensive income credit | – | 77 | 14 | – | – | – | – | 91 | 188 | (188) |
| **At 30 September 2023** | **(6)** | **(189)** | **(2)** | **267** | **103** | **–** | **20** | **193** | **(179)** | **(179)** |

Other temporary differences include the IFRS 9 transitional adjustment of £9m and equity based compensation of £5m (2022: £11m and £6m respectively). The deferred tax assets and liabilities detailed above arise primarily in Clydesdale Bank PLC which has a right to offset current tax assets against current tax liabilities and is party to a Group Payment Arrangement for payments of tax to HMRC. Therefore, in accordance with IAS 12, deferred tax assets and deferred tax liabilities have also been offset in this year where they relate to payments of income tax to this tax authority.

The Group has unrecognised deferred tax assets of £21m (2022: £Nil) (£83m gross loss valued at the mainstream rate of 25%) representing tax losses whose use is not forecast within the foreseeable future.

On 22 November 2023 the Chancellor announced that the authorised surplus payments charge will be reduced from 35% to 25% from 6 April 2024. If this measure had been enacted on the balance sheet date the deferred tax liability in respect of the defined benefit pension surplus would have reduced from £179m to £128m.

## 2.5 Earnings per share

### Accounting policy

***Basic EPS***

Basic EPS is calculated by taking the profit attributable to ordinary shareholders of the parent company and then dividing this by the weighted average number of ordinary shares outstanding during the year after deducting the weighted average of the Group's holdings of its own shares.

***Diluted EPS***

This requires the weighted-average number of ordinary shares in issue to be adjusted to assume conversion of all dilutive potential ordinary shares. These arise from awards made under equity based compensation schemes. Share awards with performance conditions attaching to them are not considered to be dilutive unless these conditions have been met at the reporting date.

| | 2023 £m | 2022 £m |
|---|---|---|
| Profit attributable to ordinary equity holders for the purposes of basic and diluted EPS | **192** | 467 |

| | 2023 | 2022 |
|---|---|---|
| Weighted-average number of ordinary shares in issue (millions) | | |
| – Basic | **1,375** | 1,441 |
| Adjustment for share awards made under equity based compensation schemes | **4** | 3 |
| – Diluted | **1,379** | 1,444 |
| Basic earnings per share (pence) | **14.0** | 32.4 |
| Diluted earnings per share (pence) | **13.9** | 32.3 |

Basic earnings per share has been calculated after deducting 0.2m (2022: 0.3m) ordinary shares representing the weighted-average of the Group's holdings of its own shares.

Note 4.1 provides details of the share buyback programme including buybacks intended for beyond 30 September 2023.

# Section 3: Assets and liabilities

## 3.1 Financial instruments

**Accounting policy**

***Recognition and derecognition***

Financial instruments are recognised when the Group becomes party to the contractual provisions of the instrument. Purchases and sales of financial assets classified within FVTPL or FVOCI are recognised on trade date.

The Group derecognises a financial asset when the contractual cash flows from the asset expire or it transfers the right to receive contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership are transferred. Financial liabilities are derecognised when the Group has discharged its obligation to the contract, or the contract is cancelled or expires.

Note 3.1.4 contains information on the valuation techniques and methodologies applied to financial instruments and their classification within the fair value hierarchy.

***Classification and measurement***

The Group measures a financial asset or liability on initial recognition at its fair value, plus or minus transaction costs that are directly attributable to the acquisition or issue of the financial asset or the financial liability (with the exception of financial assets or liabilities at FVTPL, where transaction costs are recognised directly in the income statement as they are incurred).

Subsequent accounting for a financial asset is determined by the classification of the asset depending on the underlying business model and contractual cash flow characteristics. This results in classification within one of the following categories: (i) amortised cost (note 3.1.1); (ii) FVOCI (note 3.1.2); or (iii) FVTPL (note 3.1.3).

***Repurchase agreements***

Securities sold subject to sale and repurchase agreements ('repo') are retained in their respective balance sheet categories. The associated liabilities are included in amounts due to other banks based upon the counterparties to the transactions. The difference between the sale and repurchase price of repos is treated as interest and accrued over the life of the agreements using the effective interest method.

***Offsetting***

This can only occur, and the net amount be presented on the balance sheet, when the Group currently has a legally enforceable right to offset the recognised amounts and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

***Presentation of risk, offsetting and maturity disclosures***

Certain disclosures required under IFRS 7 'Financial instruments: disclosures' and IAS 1 'Presentation of financial statements' have been included within the Risk management section of this results announcement.

### 3.1.1 Financial instruments at amortised cost

**Accounting policy**

A financial asset is measured at amortised cost when: (1) the asset is held within a business model whose objective is achieved by collecting contractual cash flows; and (2) the contractual terms give rise to cash flows on specified dates which are solely payments of principal and interest on the principal amount outstanding.

All financial liabilities are measured at amortised cost, except for financial liabilities at FVTPL. Such liabilities include derivative contracts, other than those which are financial guarantee contracts or designated and effective hedging instruments.

Financial assets classified at amortised cost are subject to expected credit loss (ECL) impairment requirements.

At each reporting date, the Group assesses financial assets measured at amortised cost, as well as loan commitments and financial guarantees not measured at FVTPL, for impairment. The impairment loss allowance is calculated using an ECL methodology and reflects: (i) an unbiased and probability weighted amount; (ii) the time value of money which discounts the impairment loss; and (iii) reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

ECL methodology is based upon the combination of PD, LGD and EAD estimates that consider a range of factors that impact on credit risk and consequently the level of impairment loss provisioning. The Group uses reasonable and supportable forecasts of future economic conditions in estimating the ECL allowance. The methodology and assumptions used in the ECL calculation are reviewed regularly and updated as necessary. ECLs are assessed either collectively or individually.

The Group's impairment policy for debt instruments at FVOCI is included in note 3.1.2. The impact of the ECL methodology on amounts due from other banks balances held at amortised cost is immaterial. ECLs relating to loan commitments and financial guarantees can be found in note 3.7.

***SICR assessment and staging***

The ECL is calculated as either 12-month (Stage 1) or lifetime depending on whether the financial asset has suffered a SICR since origination (Stage 2) or has otherwise become credit impaired (Stage 3) as at the reporting date. The Group uses a PD threshold curve (distinct for each portfolio) to assess for a SICR in addition to the 30 DPD and 90 DPD backstops for recognising Stage 2 and Stage 3 ECLs respectively.

### 3.1.1 Financial instruments at amortised cost continued

Financial assets can move between stages when the relevant staging criteria are no longer satisfied subject to certain restrictions for forborne assets. If the level of impairment loss reduces in a subsequent year, the previously recognised impairment loss allowance is reversed and recognised in the income statement.

POCI financial assets are those which are credit impaired upon initial recognition (being the point at which the asset was either purchased or originated). Once a financial asset is classified as POCI, it remains as such until derecognition irrespective of its credit quality at each reporting date. POCI financial assets are disclosed separately from those financial assets in Stage 3. The Group regards the date of acquisition as the origination date for purchased portfolios.

The Group has not made use of the low credit risk option under IFRS 9 for loans and advances at amortised cost.

Regardless of the calculation basis, the Group generates a modelled ECL allowance at the individual financial instrument level. The modelled ECL output can be supplemented by management adjustments (MAs) where appropriate.

***Write-offs and recoveries***
When there is no reasonable expectation of recovery for a loan, it is written off against the related provision. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the impairment charge in the income statement.

***Critical accounting estimates and judgements***
ECL methodology requires the Group to apply estimates and exercise judgement when calculating an impairment allowance for credit exposures.

Further information on the chosen scenarios, macroeconomic assumptions, and scenario weightings used in the ECL calculation, including the use of MAs together with sensitivity analysis, is contained in the credit risk section of Risk management on pages 40 to 47.

#### 3.1.1.1 Loans and advances to customers

**Accounting policy**
Loans and advances to customers arise when the Group provides money directly to a customer and includes mortgages, term lending, overdrafts, credit card lending, lease finance and invoice financing. They are recognised initially at fair value and are subsequently measured at amortised cost, using the effective interest method and adjusted for ECLs. They are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership.

Leases entered into by the Group as lessor, where the Group transfers substantially all the risks and rewards of ownership to the lessee, are classified as finance leases. The leased asset is not held on the Group balance sheet; instead, a finance lease is recognised representing the minimum lease payments receivable under the terms of the lease, discounted at the rate of interest implicit in the lease. Interest income is recognised in interest receivable, allocated to accounting years to reflect a constant periodic rate of return.

| | 2023<br>£m | 2022<br>£m |
|---|---|---|
| Gross loans and advances to customers | **73,295** | 73,146 |
| Impairment provisions on credit exposures(1) | **(612)** | (454) |
| Fair value hedge adjustment | **(492)** | (941) |
| | **72,191** | 71,751 |

(1) ECLs on off-balance sheet exposures of £5m (2022: £3m) are presented as part of the provisions for liabilities and charges balance (note 3.7).

The Group has a portfolio of fair valued business loans of £59m (2022: £70m) which are classified separately as financial assets at FVTPL (note 3.1.3.1). Combined with the above, this is equivalent to total loans and advances to customers of £72,250m (2022: £71,821m).

The fair value hedge adjustment represents an offset to the fair value movement on hedging derivatives transacted to manage the interest rate risk inherent in the Group's fixed rate mortgage portfolio.

The Group has transferred a proportion of mortgages to the securitisation and covered bond programmes (note 3.1.5).

**Lease finance**
The Group leases a variety of assets to third parties under finance lease arrangements, including vehicles and general plant and machinery. The cost of assets acquired by the Group during the year for the purpose of letting under finance leases and hire purchase contracts amounted to £71m (2022: £46m) and £557m (2022: £405m) respectively.

Finance lease receivables are presented in the statement of financial position within loans and advances to customers. The maturity analysis of lease receivables, including the undiscounted lease payments to be received, is as follows:

### 3.1.1.1 Loans and advances to customers continued

**Gross investment in finance lease and hire purchase receivables**

| | 2023 £m | 2022 £m |
|---|---|---|
| Less than 1 year | **373** | 269 |
| 1-2 years | **223** | 170 |
| 2-3 years | **158** | 117 |
| 3-4 years | **95** | 66 |
| 4-5 years | **59** | 46 |
| More than 5 years | **31** | 24 |
| | **939** | 692 |
| Unearned finance income | **(83)** | (45) |
| Net investment in finance lease and hire purchase receivables | **856** | 647 |

Finance income recognised on the net investment in the lease was £38m (2022: £21m) and is included in interest income (note 2.1).

**Impairment provisions on credit exposures**

| | 2023 £m | 2022 £m |
|---|---|---|
| Opening balance | **454** | 496 |
| ECL charge for the year(1) | **307** | 57 |
| Amounts written off | **(187)** | (129) |
| Recoveries of amounts written off in previous years | **38** | 30 |
| **Closing balance** | **612** | 454 |

(1) The £309m charge (2022: £52m) for impairment losses on credit exposures shown in the income statement also includes a £2m charge (2022: £5m credit) in respect of off-balance sheet ECLs which are presented as part of the provisions for liabilities and charges balance (note 3.7).

### 3.1.1.2 Cash and balances with central banks

**Accounting policy**
Cash and balances with central banks are measured at amortised cost, using the effective interest method, and are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership. These balances form part of the Group's treasury-related activities and are mostly short term in nature and repayable on demand or within a short timescale, generally three months.

The impact of the ECL impairment requirements (note 3.1.1) on the Group's cash and balances with central banks is immaterial.

| | 2022 £m | 2021 £m |
|---|---|---|
| Cash assets | **1,089** | 1,206 |
| Balances with central banks (including EU payment systems) | **10,193** | 11,015 |
| | **11,282** | 12,221 |
| Less mandatory deposits with central banks(1) | **(275)** | (266) |
| Included in cash and cash equivalents (note 5.4) | **11,007** | 11,955 |

(1) Mandatory deposits are not available for use in the Group's day-to-day business and are non-interest bearing.

### 3.1.1.3 Customer deposits

| | 2023 £m | 2022 £m |
|---|---|---|
| Interest bearing demand deposits | **39,292** | 46,457 |
| Term deposits | **22,775** | 13,951 |
| Non-interest bearing demand deposits | **4,542** | 4,952 |
| | **66,609** | 65,360 |
| Accrued interest | **218** | 74 |
| | **66,827** | 65,434 |

### 3.1.1.4 Debt securities in issue

**Accounting policy**
Debt securities comprise short and long-term debt issued by the Group including, medium-term notes, subordinated debt, covered bonds and RMBS notes.

Debt securities are initially recognised at fair value, being the issue proceeds, net of transaction costs incurred. These instruments are subsequently measured at amortised cost using the effective interest method resulting in premiums, discounts and associated issuance costs being recognised in the income statement over the life of the instrument.

Where relevant, fair value hedge adjustments have been applied.

| | Medium-term notes £m | Subordinated debt £m | Securitisation £m | Covered bonds £m | Total £m |
|---|---|---|---|---|---|
| **2023** | | | | | |
| Debt securities | **2,584** | **938** | **1,729** | **4,392** | **9,643** |
| Accrued interest | **28** | **14** | **11** | **23** | **76** |
| | **2,612** | **952** | **1,740** | **4,415** | **9,719** |
| **2022** | | | | | |
| Debt securities | 2,236 | 899 | 1,875 | 3,450 | 8,460 |
| Accrued interest | 13 | 14 | 5 | 17 | 49 |
| | 2,249 | 913 | 1,880 | 3,467 | 8,509 |

Key movements in the year are shown in the table below(1). Full details of all notes in issue can be found at https://www.virginmoneyukplc.com/investor-relations/debt-investors/

| | 2023 | | | | 2022 | | | |
|---|---|---|---|---|---|---|---|---|
| | Issuances | | Redemptions | | Issuances | | Redemptions | |
| | Denomination | £m | Denomination | £m | Denomination | £m | Denomination | £m |
| Medium-term notes | **EUR, GBP** | **747** | **EUR** | **432** | – | – | – | – |
| Securitisation | **GBP** | **900** | **USD, GBP** | **1,012** | GBP | 700 | USD, GBP | 1,264 |
| Covered bonds | **EUR, GBP** | **926** | **–** | **–** | EUR, GBP | 1,780 | – | – |
| | | **2,573** | | **1,444** | | 2,480 | | 1,264 |

(1) Other movements relate to foreign exchange, hedging adjustments and the capitalisation and amortisation of issuance costs.

The following tables provide a breakdown of the medium-term notes and subordinated debt by instrument as at 30 September (excluding accrued interest):

**Medium-term notes**

| | 2023 £m | 2022 £m |
|---|---|---|
| VM UK 3.125% fixed-to-floating rate callable senior notes due 2025 | **300** | 299 |
| VM UK 4% fixed rate reset callable senior notes due 2026 | **463** | 444 |
| VM UK 3.375% fixed rate reset callable senior notes due 2026 | **330** | 317 |
| VM UK 4% fixed rate reset callable senior notes due 2027 | **350** | 331 |
| VM UK 2.875% fixed rate reset callable senior notes due 2025 | **418** | 413 |
| VM UK 0.375% fixed rate reset callable senior notes due 2024 | **–** | 432 |
| VM UK 4.625% fixed rate reset callable senior notes due 2028 | **421** | – |
| VM UK 7.625% fixed rate reset callable senior notes due 2029 | **302** | – |
| | **2,584** | 2,236 |

## Section 3: Assets and liabilities

### 3.1.1.4 Debt securities in issue continued

**Subordinated debt**

| | 2023 £m | 2022 £m |
|---|---|---|
| VM UK 7.875% fixed rate reset callable subordinated notes due 2028 | **250** | 249 |
| VM UK 5.125% fixed rate reset callable subordinated notes due 2030 | **424** | 400 |
| VM UK 2.625% fixed rate reset callable subordinated notes due 2031 | **264** | 250 |
| | **938** | 899 |

Details of securitisation and covered bond issuances are included in note 3.1.5.

### 3.1.1.5 Due to other banks

| | 2023 £m | 2022 £m |
|---|---|---|
| Secured loans | **6,291** | 7,230 |
| Securities sold under agreements to repurchase(1) | **552** | 1,205 |
| Transaction balances with other banks | **19** | 17 |
| Deposits from other banks | **77** | 50 |
| | **6,939** | 8,502 |

(1) The underlying securities sold under agreements to repurchase have a carrying value of £1,047m (2022: £1,873m) and relate to internally held debt securities, backed by mortgage assets, issued from the Group's securitisation programmes (note 3.1.5).

Secured loans comprise amounts drawn under the TFSME scheme (including accrued interest).

### 3.1.2 Financial assets at fair value through other comprehensive income

**Accounting policy**

A financial asset is measured at FVOCI when: (i) the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and (ii) the contractual terms give rise to cash flows on specified dates which are solely payments of principal and interest on the principal amount outstanding unless the financial asset is designated at FVTPL on initial recognition. An option for equity investments that are not held for trading can be taken to classify them at FVOCI where an irrevocable election is made at initial recognition. This is available for each separate investment, and the Group has not exercised this option for any equity investments.

Interest income and impairment gains and losses on FVOCI assets are measured in the same manner as for assets measured at amortised cost and recognised in the income statement, with all other gains or losses recognised in other comprehensive income as a separate component of equity in the year in which they arise. Gains and losses arising from changes in fair value are included as a separate component of equity until sale, when the cumulative gain or loss is transferred to the income statement. For all FVOCI assets, the gain or loss is calculated with reference to the gross carrying amount.

Debt instruments at FVOCI are subject to the same impairment criteria as amortised cost financial assets (note 3.1.1), with the ECL element recognised directly in the income statement. As the financial asset is fair valued through other comprehensive income, the change in its value includes the ECL element, with the remaining fair value change recognised in other comprehensive income. Any reversal of the ECL is recorded in the income statement up to the value recognised previously.

A low credit risk option is available which allows entities not to assess whether there has been a significant increase in credit risk since initial recognition where the financial asset is deemed as being of low credit risk at the reporting date. The result of exercising the low credit risk exemption is that the financial assets are classed under Stage 1 with a 12-month ECL calculation applied.

The Group exercises the low credit risk option for debt instruments classified as FVOCI, recognising the high credit quality of the instruments. Consequently, no material ECL provision is held for these financial assets.

Financial assets at FVOCI consists of £6,184m of listed securities (2022: £5,064m).

Note 3.1.4 contains further information on the valuation methodology applied to financial instruments at FVOCI at 30 September 2023 and their classification within the fair value hierarchy. Details of the credit quality of financial assets is provided in the Risk management section.

# Section 3: Assets and liabilities

### 3.1.3 Financial assets at fair value through profit or loss

**Accounting policy**
A financial asset is measured at FVTPL if it: (i) does not fall into one of the business models for amortised cost (note 3.1.1) or FVOCI (note 3.1.2); (ii) is specifically designated as FVTPL on initial recognition in order to eliminate or significantly reduce a measurement mismatch; or (iii) is classified as held for trading.

A financial instrument is classified as held for trading if it is acquired principally for the purpose of selling in the near term, forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative not in a qualifying hedge relationship.

Associated gains and losses are recognised in the income statement as they arise (note 2.2).

***Derivatives***
The Group uses derivative financial instruments to manage exposure to interest rate, contractually specified inflation and foreign currency risk. Interest rate risk arises primarily due to the mismatch, or duration, between repricing dates of interest-bearing assets and liabilities, or basis risk from assets and liabilities repricing to different reference rates. Contractually specified inflation risk arises from financial instruments whose cash flows are linked to an inflation index. Currency risk arises when assets and liabilities are not denominated in the functional currency of the entity. Derivatives are recognised on the balance sheet at fair value on trade date and are measured at fair value throughout the life of the contract. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative. The notional amount of a derivative contract is not recorded on the balance sheet but is disclosed as part of this note.

***Netting***
Derivative assets and liabilities are offset against collateral received and paid respectively, and the net amount reported in the balance sheet only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to settle on a net basis. Amounts offset on the balance sheet represent the Group's centrally cleared derivative financial instruments and collateral paid to/from central clearing houses, which meet the criteria for offsetting under IAS 32.

***Hedge accounting***
The Group elects to apply hedge accounting for the majority of its risk management activity that uses derivatives. This results in greater alignment in the timing of recognition of gains and losses on hedged items and hedging instruments and therefore reduces income statement volatility. The Group does not have a trading book, however derivatives that do not meet the hedging criteria, or for which hedge accounting is not applied, are classified as held for trading.

The Group has elected, as a policy choice permitted under IFRS 9, to continue to apply hedge accounting in accordance with IAS 39. The method of recognising the fair value gain or loss on a derivative depends on whether it is designated as a hedging instrument and the nature of the item being hedged. Certain derivatives are designated as either hedges of highly probable future cash flows attributable to a recognised asset or liability, or a highly probable forecast transaction (a cash flow hedge); or hedges of the fair value of recognised assets or liabilities or firm commitments (a fair value hedge).

***Cash flow hedge***
The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in equity. Specifically, the separate component of equity (note 4.1) is adjusted to the lesser of the cumulative gain or loss on the hedging instrument and the cumulative change in fair value of the expected future cash flows on the hedged item from the inception of the hedge. Any remaining gain or loss on the hedging instrument is recognised in the income statement. The carrying value of the hedged item is not adjusted. Amounts accumulated in equity are transferred to the income statement in the period in which the hedged item affects profit or loss.

When a hedging instrument expires or is sold, or when a hedge is discontinued or no longer meets the criteria for hedge accounting, any cumulative gain or loss remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

***Fair value hedge***
Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. This movement in the fair value of the hedged item is made as an adjustment to the carrying value of the hedged asset or liability.

Where the hedged item is derecognised from the balance sheet, the adjustment to the carrying amount of the asset or liability is immediately transferred to the income statement. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item is amortised to the income statement over the remaining life of the asset or liability.

***Derivatives held for trading***
Changes in value of held for trading derivatives are immediately recognised in the income statement (note 2.2).

#### 3.1.3.1 Loans and advances to customers

Included in financial assets at FVTPL is a historical portfolio of loans. Interest rate risk associated with these loans is managed using interest rate derivative contracts and the loans are recorded at fair value to avoid an accounting mismatch. The maximum credit exposure of the loans is £59m (2022: £70m). The cumulative loss in the fair value of the loans attributable to changes in credit risk amounts to £1m (2022: £1m); the change for the current year is £Nil (2022: decrease of £1m), of which £Nil (2022: £1m) has been recognised in the income statement.

#### 3.1.3.2 Derivatives

The tables below analyse derivatives between those designated as hedging instruments and those classified as held for trading:

| | 2023<br>£m | 2022<br>£m |
|---|---|---|
| **Fair value of derivative financial assets** | | |
| Designated as hedging instruments | **96** | 277 |
| Designated as held for trading | **39** | 65 |
| | **135** | 342 |
| **Fair value of derivative financial liabilities** | | |
| Designated as hedging instruments | **204** | 201 |
| Designated as held for trading | **86** | 126 |
| | **290** | 327 |

Cash collateral totalling £267m (2022: £241m) has been pledged and £33m has been received (2022: £38m) in respect of derivatives with other banks. These amounts are included within due from and due to other banks respectively. Net collateral received from clearing houses, which did not meet offsetting criteria, totalled £116m (2022: £149m) and is included within other assets and other liabilities.

The derivative financial instruments held by the Group are further analysed below. The notional contract amount is the amount from which the cash flows are derived and does not represent the principal amounts at risk relating to these contracts.

### 3.1.3.2 Derivatives continued

**Total derivative contracts**

| | 2023 | | | 2022 | | |
|---|---|---|---|---|---|---|
| | Notional contract amount £m | Fair value of assets £m | Fair value of liabilities £m | Notional contract amount £m | Fair value of assets £m | Fair value of liabilities £m |
| **Derivatives designated as hedging instruments** | | | | | | |
| *Cash flow hedges* | | | | | | |
| Interest rate swaps (gross) | **51,185** | **1,295** | **545** | 35,753 | 1,988 | 930 |
| Less: net settled interest rate swaps(1) | **(49,888)** | **(1,222)** | **(531)** | (33,188) | (1,803) | (900) |
| Interest rate swaps (net)(2) | **1,297** | **73** | **14** | 2,565 | 185 | 30 |
| *Fair value hedges* | | | | | | |
| Interest rate swaps (gross)(3) | **19,203** | **1,219** | **862** | 16,600 | 1,201 | 636 |
| Less: net settled interest rate swaps(1) | **(18,113)** | **(1,206)** | **(820)** | (14,611) | (1,144) | (570) |
| Interest rate swaps (net)(2) | **1,090** | **13** | **42** | 1,989 | 57 | 66 |
| Cross currency swaps(2) | **2,350** | **10** | **148** | 2,113 | 35 | 105 |
| | **3,440** | **23** | **190** | 4,102 | 92 | 171 |
| **Total derivatives designated as hedging instruments** | **4,737** | **96** | **204** | 6,667 | 277 | 201 |
| **Derivatives designated as held for trading** | | | | | | |
| *Foreign exchange rate related contracts* | | | | | | |
| Spot and forward foreign exchange(2) | **654** | **7** | **9** | 599 | 26 | 20 |
| Options(2) | **–** | **–** | **–** | 1 | – | – |
| | **654** | **7** | **9** | 600 | 26 | 20 |
| *Interest rate related contracts* | | | | | | |
| Interest rate swaps (gross) | **1,910** | **47** | **50** | 1,411 | 52 | 66 |
| Less: net settled interest rate swaps(1) | **(753)** | **(43)** | **(1)** | (665) | (50) | – |
| Interest rate swaps (net)(2) | **1,157** | **4** | **49** | 746 | 2 | 66 |
| Swaptions(2) | **10** | **–** | **1** | 10 | – | 2 |
| Options(2) | **1,067** | **16** | **16** | 501 | 16 | 17 |
| | **2,234** | **20** | **66** | 1,257 | 18 | 85 |
| *Commodity related contracts* | **167** | **12** | **11** | 199 | 21 | 21 |
| **Total derivatives designated as held for trading** | **3,055** | **39** | **86** | 2,056 | 65 | 126 |

(1) Presented within other assets and other liabilities.
(2) Presented within derivative financial instruments.
(3) Includes inflation and interest rate risk related swaps detailed in the summary of hedging instruments in designated hedge relationships table on page 98.

**Hedge accounting**

The hedging strategy of the Group is divided into micro hedges, where the hedged item is a distinctly identifiable asset or liability, and portfolio hedges, where the hedged item is a homogeneous portfolio of assets or liabilities.

In some hedge accounting relationships, the Group designates risk components of hedged items as follows:

- Benchmark interest rate risk as a component of interest rate risk, such as the SONIA component.
- Exchange rate risk for foreign currency financial assets and financial liabilities.
- Inflation risk where it is a contractually specified component of a debt instrument.
- Components of cash flows of hedged items, for example cash flows linked to benchmark rates such as SONIA.

Other risks such as credit risk and liquidity risk are managed by the Group but are not included in the hedge accounting relationship. Changes in the designated risk component usually account for the largest portion of the overall change in fair value or cash flows of the hedged item.

#### 3.1.3.2 Derivatives continued

**Portfolio cash flow hedges**
The Group applies macro cash flow hedge accounting to a portion of its floating rate financial assets and liabilities. The hedged cash flows are a group of forecast transactions that result in cash flow variability from resetting of interest rates, reinvestment of financial assets, or refinancing and rollovers of financial liabilities. This cash flow variability can arise on recognised assets or liabilities or highly probable forecast transactions. The hedged items are designated as the gross asset or liability positions allocated to time buckets based on projected repricing and interest profiles. The Group aims to maintain a position where the principal amount of the hedged items is greater than or equal to the notional amount of the corresponding interest rate swaps used as the hedging instruments. The hedge accounting relationship is reassessed on a monthly basis with the composition of hedging instruments and hedged items changing frequently in line with the underlying risk exposures. If necessary, the hedge relationships are de-designated and redesignated based on the effectiveness test results.

**Portfolio fair value hedges**
The Group applies macro fair value hedging to a portion of its fixed rate mortgages. The Group determines hedged items by identifying portfolios of homogeneous loans based on their contractual maturity and other risk characteristics. Loans within the identified portfolios are allocated to repricing time buckets based on expected, rather than contractual, repricing dates. The hedging instruments are designated to those repricing time buckets. Hedge effectiveness is measured on a monthly basis, by comparing fair value movements of the designated proportion of the bucketed loans due to the hedged risk against the fair value movements of the derivatives.

The aggregated fair value changes in the hedged loans are recognised on the Group's balance sheet as an asset. At the end of every month, in order to minimise the ineffectiveness from early repayments and accommodate new exposures, the Group voluntarily de-designates the hedge relationships and redesignates them as new hedges. Fair value hedging of fixed rate deposits was discontinued in 2020, and the hedge adjustment recognised on the Group's balance sheet is amortised to profit and loss over the life of the hedged item.

**Micro fair value hedges**
The Group uses this hedging strategy on GBP, inflation or foreign currency denominated fixed rate assets held at FVOCI and GBP and foreign currency denominated fixed rate debt issuances by the Group. Where assets and liabilities are exposed to multiple risk components, for example interest rate and foreign currency risk, these components are simultaneously designated as hedged risks within the same hedge relationship.

**Hedge ineffectiveness**
Hedge ineffectiveness can arise from:

- mismatches between the contractual terms of the hedged item and hedging instrument, including basis differences;
- differences in timing of cash flows of hedged items and hedging instruments;
- changes in expected timings and amounts of forecast future cash flows; and
- derivatives used as hedging instruments having a non-zero fair value at the time of designation.

Additionally, for portfolio fair value hedges of the Group's fixed rate mortgage portfolio, ineffectiveness also arises from the difference between forecast and actual repayments (i.e. prepayment risk).

The Group has no remaining hedge relationships exposed to LIBOR and as no uncertainty remains regarding interest rate benchmark reform, the Group no longer applies the reliefs provided by 'Interest Rate Benchmark Reform – Phase 1 and Phase 2 amendments' to hedge accounting. Further detail on the Group's approach to managing the risk of LIBOR replacement, including derivatives designated as held for trading that have not yet transitioned, is provided on page 67.

### 3.1.3.2 Derivatives continued

**Summary of hedging instruments in designated hedge relationships**
In the table below, the Group sets out the accumulated adjustments arising from the corresponding continuing hedge relationships, irrespective of whether or not there has been a change in hedge designation during the year:

| | 2023 | | | | 2022 | | | |
|---|---|---|---|---|---|---|---|---|
| | | Carrying amount | | | | Carrying amount | | |
| | Notional contract amount £m | Assets £m | Liabilities £m | Change in fair value of hedging instrument in the year used for ineffectiveness measurement[(2)] £m | Notional contract amount £m | Assets £m | Liabilities £m | Change in fair value of hedging instrument in the year used for ineffectiveness measurement[(2)] £m |
| **Cash flow hedges** | | | | | | | | |
| *Interest rate risk* | | | | | | | | |
| Interest rate swaps[(1)] | **51,185** | **1,295** | **545** | **(318)** | 35,753 | 1,988 | 930 | 916 |
| **Total derivatives designated as cash flow hedges** | **51,185** | **1,295** | **545** | **(318)** | 35,753 | 1,988 | 930 | 916 |
| **Fair value hedges** | | | | | | | | |
| *Interest rate risk* | | | | | | | | |
| Interest rate swaps[(1)] | **17,683** | **983** | **257** | **(368)** | 16,150 | 1,059 | 361 | 1,052 |
| *Inflation and interest rate risk* | | | | | | | | |
| Inflation linked interest rate swaps[(1)] | **1,520** | **236** | **606** | **43** | 450 | 142 | 275 | 96 |
| *Foreign exchange and interest rate risk* | | | | | | | | |
| Cross currency swaps | **2,350** | **10** | **148** | **(58)** | 2,113 | 35 | 105 | 6 |
| **Total derivatives designated as fair value hedges** | **21,553** | **1,229** | **1,011** | **(383)** | 18,713 | 1,236 | 741 | 1,154 |

(1) As shown in the total derivatives contracts table on page 96, for centrally cleared derivatives, where the IAS 32 'Financial instruments: presentation' netting criteria is met, the derivative balances are offset within other assets. For all other derivatives, the derivative balances are presented within derivative financial instruments.
(2) Changes in fair value of cash flow hedging instruments are recognised in other comprehensive income. Changes in fair value of fair value hedging instruments are recognised in the income statement in non-interest income.

**Summary of hedged items in designated hedge relationships**
In the table below, the Group sets out the accumulated adjustments arising from the corresponding continuing hedge relationships, irrespective of whether or not there has been a change in hedge designation during the year.

| | 2023 | | | 2022 | | |
|---|---|---|---|---|---|---|
| | | Cash flow hedge reserve | | | Cash flow hedge reserve | |
| | Change in fair value of hedged item in the year used for ineffectiveness measurement £m | Continuing hedges £m | Discontinued hedges £m | Change in fair value of hedged item in the year used for ineffectiveness measurement £m | Continuing hedges £m | Discontinued hedges £m |
| **Cash flow hedges** | | | | | | |
| *Interest rate risk* | | | | | | |
| Gross floating rate assets and gross floating rate liabilities[(1)] | **268** | **625** | **59** | (962) | 979 | (14) |
| **Total** | **268** | **625** | **59** | (962) | 979 | (14) |

### 3.1.3.2 Derivatives continued

| | 2023 | | | | 2022 | | | |
|---|---|---|---|---|---|---|---|---|
| | Carrying amount of hedged items | | Accumulated hedge adjustment on the hedged item | Change in fair value of hedged items in the year used for ineffectiveness measurement | Carrying amount of hedged items | | Accumulated hedge adjustment on the hedged item | Change in fair value of hedged items in the year used for ineffectiveness measurement |
| | Assets £m | Liabilities £m | £m | £m | Assets £m | Liabilities £m | £m | £m |
| **Fair value hedges** | | | | | | | | |
| *Interest rate risk* | | | | | | | | |
| Fixed rate mortgages[3] | **10,864** | **–** | **(492)** | **426** | 9,520 | – | (941) | (779) |
| Fixed rate customer deposits[4] | **–** | **–** | **–** | **–** | – | – | (2) | – |
| Fixed rate FVOCI debt instruments[5] | **2,692** | **–** | **(568)** | **92** | 2,443 | – | (613) | (629) |
| Fixed rate issuances[2] | **–** | **(2,810)** | **234** | **(116)** | – | (2,392) | 350 | 388 |
| *Inflation and interest rate risk* | | | | | | | | |
| Fixed rate FVOCI debt instruments[5] | **1,116** | **–** | **(92)** | **(43)** | 589 | – | (105) | (96) |
| *Foreign exchange and interest rate risk* | | | | | | | | |
| Fixed rate currency FVOCI debt instruments[5] | **64** | **–** | **(2)** | **1** | 76 | – | (3) | (3) |
| Fixed rate currency issuances[2] | **–** | **(2,156)** | **140** | **56** | – | (1,954) | 83 | 11 |
| **Total** | **14,736** | **(4,966)** | **(780)** | **416** | 12,628 | (4,346) | (1,231) | (1,108) |

(1) Highly probable future cash flows arising from loans and advances to customers, due to customers and debt securities in issue.
(2) Hedged item is recorded in debt securities in issue.
(3) Hedged item and the cumulative fair value changes are recorded in loans and advances to customers.
(4) Hedge relationship was discontinued in 2020. The fair value adjustment taken will be amortised over the remaining life of the hedged items, and is recorded in customer deposits.
(5) Hedged item is recorded in financial assets at FVOCI.

| | 2023 | | | | 2022 | | | |
|---|---|---|---|---|---|---|---|---|
| | Hedge ineffectiveness recognised in income statement[1] | Effective portion recognised in other comprehensive income | Reclassified into income statement as | | Hedge ineffectiveness recognised in income statement[1] | Effective portion recognised in other comprehensive income | Reclassified into income statement as | |
| | | | Net interest income | Non-interest income | | | Net interest income | Non-interest income |
| | £m | £m | £m | £m | £m | £m | £m | £m |
| **Cash flow hedges** | | | | | | | | |
| *Interest rate risk* | | | | | | | | |
| Gross floating rate assets and gross floating rate liabilities | **(50)** | **(268)** | **10** | **2** | (46) | 962 | 17 | (4) |
| **Total (losses)/gains on cash flow hedges** | **(50)** | **(268)** | **10** | **2** | (46) | 962 | 17 | (4) |

| | Hedge ineffectiveness recognised in income | |
|---|---|---|
| | 2023 £m | 2022 £m |
| **Fair value hedges** | | |
| *Interest rate risk* | | |
| Fixed rate mortgages | **31** | 33 |
| Fixed rate FVOCI debt instruments | **3** | (2) |
| Fixed rate issuances | **–** | 1 |
| *Inflation and interest rate risk* | | |
| Fixed rate FVOCI debt instruments | **–** | – |
| *Foreign exchange and interest rate risk* | | |
| Fixed rate currency FVOCI debt instruments | **–** | (1) |
| Fixed rate currency issuances | **(1)** | 15 |
| **Total losses on fair value hedges[1]** | **33** | 46 |

(1) Recognised in gains less losses on financial assets at fair value.

#### 3.1.3.3 Other

Included in other financial assets is £1m (2022: £7m) of unlisted securities and £1m (2022: £1m) of debt instruments.

### 3.1.4 Fair value of financial instruments

**Accounting policy**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the valuation date.

When available, the Group measures the fair value of a financial instrument using quoted prices in an active market for that instrument. Where no such active market exists for the particular asset or liability, the Group uses a valuation technique to arrive at the fair value, including the use of transaction prices obtained in recent arm's length transactions where possible, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. In doing so, fair value is estimated using a valuation technique that makes maximum possible use of market inputs and that places minimal possible reliance upon entity-specific inputs.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, which represents the fair value of the consideration paid or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Group recognises profits or losses on the transaction date.

In certain limited circumstances, the Group applies the fair value measurement option to financial assets including loans and advances where the inherent market risks (principally interest rate and option risk) are individually hedged using appropriate interest rate derivatives. The loan is designated as being carried at FVTPL to offset the movements in the fair value of the derivative within the income statement and therefore avoid an accounting mismatch. When a loan is held at fair value, a statistical-based calculation is used to estimate credit losses attributable to adverse movements in credit risk on the assets held. This adjustment to the credit quality of the asset is then applied to the carrying amount of the loan to arrive at fair value and recognised in the income statement.

Analysis of the fair value disclosures uses a hierarchy that reflects the significance of inputs used in measuring fair value. The level in the fair value hierarchy within which a fair value measurement is categorised is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. The fair value measurement hierarchy is as follows:

- Level 1 – quoted prices (unadjusted) in active markets for an identical financial asset or liability.
- Level 2 – inputs other than quoted prices within Level 1 that are observable for the financial asset or liability, either directly (as prices) or indirectly (derived from prices).
- Level 3 – inputs for the financial asset or liability that are not based on observable market data (unobservable inputs).

For the purpose of reporting movements between levels of the fair value hierarchy, transfers are recognised at the beginning of the reporting year in which they occur.

**(a) Fair value of financial instruments recognised at amortised cost**

The tables show a comparison of the carrying amounts of financial assets and liabilities measured at amortised cost, as reported on the balance sheet, and their fair values where these are not approximately equal.

There are various limitations inherent in this fair value disclosure, particularly where prices are derived from unobservable inputs due to some financial instruments not being traded in an active market. The methodologies and assumptions used in the fair value estimates are therefore described in the notes to the tables. The difference between carrying value and fair value is relevant in a trading environment but is not relevant to assets such as loans and advances.

| | 2023 | | 2022 | |
|---|---|---|---|---|
| | Carrying value £m | Fair value £m | Carrying value £m | Fair value £m |
| Financial assets | | | | |
| Loans and advances to customers(1) | **72,191** | **71,611** | 71,751 | 69,277 |
| Financial liabilities | | | | |
| Customer deposits(2) | **66,827** | **66,625** | 65,434 | 65,069 |
| Debt securities in issue(3) | **9,719** | **9,788** | 8,509 | 8,515 |
| Due to other banks(2) | **6,939** | **6,959** | 8,502 | 8,485 |

(1) Loans and advances to customers are categorised as Level 3 in the fair value hierarchy with the exception of £1,085m (2022: £1,098m) of overdrafts which are categorised as Level 2.
(2) Categorised as Level 2 in the fair value hierarchy.
(3) Categorised as Level 2 in the fair value hierarchy with the exception of £3,597m of listed debt (2022: £3,156m) which is categorised as Level 1.

# Section 3: Assets and liabilities

**3.1.4 Fair value of financial instruments continued**

The Group's fair values disclosed for financial instruments at amortised cost are based on the following methodologies and assumptions:

(a) *Loans and advances to customers* – determined by firstly segregating them into portfolios which have similar characteristics. Contractual cash flows are then adjusted for ECLs and expectations of customer behaviour based on observed historic data. The cash flows are then discounted at a weighted average cost of capital (appropriate to the portfolio) to arrive at an estimate of their fair value.

(b) *Customer deposits* – determined using a replacement cost method which assumes alternative funding is raised in the most advantageous market. The contractual cash flows have been discounted using a funding curve with credit spreads reflecting the tenor of each deposit.

(c) *Debt securities in issue* – taken directly from quoted market prices where available or determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity.

(d) *Due to other banks* – determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity.

**(b) Fair value of financial instruments recognised on the balance sheet at fair value**

The following tables provide an analysis of financial instruments that are measured subsequent to initial recognition at fair value, using the fair value hierarchy described above:

| | 2023 | | | | 2022 | | | |
|---|---|---|---|---|---|---|---|---|
| | Level 1 £m | Level 2 £m | Level 3 £m | Total £m | Level 1 £m | Level 2 £m | Level 3 £m | Total £m |
| **Financial assets** | | | | | | | | |
| Held at FVOCI | **6,184** | **–** | **–** | **6,184** | 5,064 | – | – | 5,064 |
| Loans and advances to customers | **–** | **59** | **–** | **59** | – | 70 | – | 70 |
| Other | **–** | **–** | **2** | **2** | – | 4 | 4 | 8 |
| Derivatives | **–** | **135** | **–** | **135** | – | 342 | – | 342 |
| **Total financial assets at fair value** | **6,184** | **194** | **2** | **6,380** | 5,064 | 416 | 4 | 5,484 |
| **Financial liabilities** | | | | | | | | |
| Derivatives | **–** | **290** | **–** | **290** | – | 327 | – | 327 |
| **Total financial liabilities at fair value** | **–** | **290** | **–** | **290** | – | 327 | – | 327 |

There were no transfers between Level 1 and 2 in the current or prior year.

The Group's valuations for financial instruments that are measured subsequent to initial recognition at fair value are based on the following methodologies and assumptions:

(a) *Held at FVOCI* – based on quoted closing market prices.

(b) *Loans and advances to customers* – derived from data or valuation techniques based upon observable market data and non-observable inputs as appropriate to the nature and type of the underlying instrument.

(c) *Other (Level 2)* – represents £Nil (2022: £4m) of Visa Inc. Series A preferred stock received following a conversion event in July 2022. This is calculated by taking the year end New York Stock Exchange share price for Visa inc. The preferred stock was sold in full during the year.

(d) *Other (Level 3)* – represents unlisted equity investments for which the transaction price is considered the best representation of the exit price and is the Group's best estimate of fair value. The Visa Inc. Series B preferred stock received as partial consideration for the sale of the Group's share in Visa Europe, was sold in full during the year.

(e) *Derivative financial assets and liabilities* – includes foreign exchange contracts, interest rate swaps, interest rate and currency option contracts, and currency swaps, and are obtained from discounted cash flow models or option pricing models as appropriate.

### 3.1.4 Fair value of financial instruments continued

**Level 3 movement analysis:**

| | 2023 | | 2022 | |
|---|---|---|---|---|
| | Financial assets at FVTPL £m | Derivative financial assets £m | Financial assets at FVTPL £m | Derivative financial assets £m |
| Balance at the beginning of the year | **4** | **–** | 6 | 1 |
| Fair value gains recognised[1] | | | | |
| In profit or loss – unrealised | **–** | **–** | – | (1) |
| Sales | **(2)** | **–** | – | – |
| Settlements | **–** | – | (2) | – |
| **Balance at the end of the year** | **2** | – | 4 | – |

(1) Net gains or losses were recorded in non-interest income.

**Sensitivity of Level 3 fair value measurements to reasonably possible alternative assumptions**
The Group has limited exposure to Level 3 fair value measurements. If all risks inherent in the valuations were to crystallise in their entirety, total assets would reduce by £2m which would be recognised directly in the income statement.

### 3.1.5 Securitisation and covered bond programmes

**Accounting policy**
The Group sponsors the formation of structured entities, primarily for the purpose of facilitation of asset securitisation and covered bond transactions, the full details of which can be found in note 6.2 to the Company financial statements. The Group has no shareholding in these entities, but is exposed, or has rights, to variable returns and has the ability to affect those returns. The entities are consolidated in the Group's financial statements in accordance with note 1.4.

***Securitisation***
The Group has securitised a portion of its retail mortgage loan portfolio under master trust securitisation programmes. The securitised mortgage loans have been assigned at principal value to bankruptcy remote structured entities. The securitised debt holders have no recourse to the Group other than the principal and interest (including fees) generated from the securitised mortgage loan portfolio.

The externally held securitised notes in issue are included within debt securities in issue (note 3.1.1.4). There are a number of notes held internally by the Group which are used as collateral for repurchases and similar transactions or for credit enhancement purposes.

***Covered bond***
A subset of the Group's retail mortgage loan portfolio has been ring-fenced and assigned to a bankruptcy remote limited liability partnership, Eagle Place Covered Bonds LLP, to provide a guarantee for the obligations payable on the covered bonds issued by the Group.

The covered bond partnership is consolidated with the mortgage loans retained on the Group balance sheet and the covered bonds issued included within debt securities in issue (note 3.1.1.4). The covered bond holders have dual recourse: firstly, to the bond issuer on an unsecured basis; and secondly, to the LLP under the Covered Bond Guarantee secured against the mortgage loans.

Under both the securitisation and covered bond programmes, the mortgage loans do not qualify for derecognition because the Group remains exposed to the majority of the risks and rewards of the mortgage loan portfolio, principally the associated credit risk. The Group continues to service the mortgage loans in return for an administration fee and is also entitled to any residual income after all payment obligations due under the terms of the programmes and senior programme expenses have been met. A deemed loan liability is recognised in the programme sponsor for the proceeds of the funding transaction.

***Significant restrictions***
Where the Group uses its financial assets to raise finance through securitisation and the sale of securities subject to repurchase agreements, the assets become encumbered and are not available for transfer around the Group.

### 3.1.5 Securitisation and covered bond programmes continued

The assets and liabilities in relation to securitisation and covered bonds in issue at 30 September are as follows (excluding accrued interest):

| | 2023 | | 2022 | |
|---|---|---|---|---|
| | Loans and advances securitised £m | Notes in issue £m | Loans and advances securitised £m | Notes in issue £m |
| **Securitisation programmes** | | | | |
| Lanark | **3,743** | **2,967** | 3,776 | 2,768 |
| Lannraig | **1,620** | **1,090** | 768 | 622 |
| Gosforth 2018-1 | **–** | **–** | 872 | 745 |
| | **5,363** | **4,057** | 5,416 | 4,135 |
| Less held by the Group | | **(2,328)** | | (2,260) |
| | | **1,729** | | 1,875 |
| **Covered bond programmes** | | | | |
| Clydesdale Bank PLC (formerly Virgin Money PLC) | **7,575** | **4,392** | 6,739 | 3,450 |

The fair values of financial assets and associated liabilities relating to the securitisation programmes were £5,311m and £1,749m respectively (2022: £5,235m and £1,878m) where the counterparty to the liabilities has recourse only to the financial assets.

There were no events during the year that resulted in any Group transferred financial assets being derecognised.

The Group has contractual and non-contractual arrangements which may require it to provide financial support as follows:

**Securitisation programmes**

The Group provides credit support to the structured entities via reserve funds, which are partly funded through subordinated debt arrangements and by holding junior notes. Exposures are shown in the table below:

| | 2023 £m | 2022 £m |
|---|---|---|
| Beneficial interest held | **1,137** | 1,239 |
| Subordinated loans | **75** | 42 |
| Junior notes held | **853** | 978 |
| | **2,065** | 2,259 |

Looking forward through future reporting years there are a number of date-based options on the notes issued by the structured entities which could be actioned by them as issuer. These could require the Group, as sponsor, to provide additional liquidity support.

**Covered bond programmes**

The nominal level of over-collateralisation was £2,670m (2022: £3,127m) in the Clydesdale Bank PLC (formerly Virgin Money PLC) programme. From time to time the obligations of the Group to provide over-collateralisation may increase due to the formal requirements of the programme.

Under all programmes, the Group has an obligation to repurchase mortgage exposures if certain mortgage loans no longer meet the programme criteria.

# Section 3: Assets and liabilities

## 3.2 Intangible assets and goodwill

| | Capitalised software £m | Goodwill £m | Core deposit intangible £m | Total £m |
|---|---|---|---|---|
| **Cost** | | | | |
| At 1 October 2021 | 1,043 | 11 | 6 | 1,060 |
| Additions | 53 | – | – | 53 |
| Write-off | (28) | – | – | (28) |
| Disposal | (8) | – | – | (8) |
| At 30 September 2022 | 1,060 | 11 | 6 | 1,077 |
| Additions | 11 | – | – | 11 |
| Write-off | (45) | – | – | (45) |
| Disposal | (714) | – | – | (714) |
| **At 30 September 2023** | **312** | **11** | **6** | **329** |
| **Accumulated amortisation and impairment** | | | | |
| At 1 October 2021 | 684 | – | 3 | 687 |
| Charge for the year | 81 | – | 3 | 84 |
| Impairment | 47 | – | – | 47 |
| Disposal | (8) | – | – | (8) |
| At 30 September 2022 | 804 | – | 6 | 810 |
| Charge for the year | 60 | – | – | 60 |
| Disposal | (714) | – | – | (714) |
| **At 30 September 2023** | **150** | **–** | **6** | **156** |
| **Net book value** | | | | |
| **At 30 September 2023** | **162** | **11** | **–** | **173** |
| At 30 September 2022 | 256 | 11 | – | 267 |

In both FY22 and FY23 all software additions form part of internally generated software projects.

A write-off charge of £45m (2022: £28m) was recognised in relation to the Group's mortgage digitisation programme. Following an assessment of the progress of the project to upgrade the mortgage platform and challenges identified during testing, we now anticipate a significant deferral and redesign as we implement the upgraded capability.

£714m of fully amortised assets were disposed of during the year following a data cleanse exercise conducted on the Group's intangible asset registers ahead of a migration to a single asset register in FY24.

## 3.3 Retirement benefit obligations

**Accounting policy**

***Defined benefit pension scheme***

A liability or asset is recognised on the balance sheet in respect of the defined benefit scheme and is measured as the difference between the present value of the defined benefit obligation less the fair value of the defined benefit scheme assets at the reporting date. The present value of the defined benefit obligation for the scheme is discounted by high-quality corporate bond rates that have maturity dates approximating to the terms of the defined benefit obligation. Surpluses are only recognised to the extent that they are recoverable through reduced contributions in the future or through refunds from the scheme. In assessing whether a surplus is recoverable, the Group considers its current right to obtain a refund or a reduction in future contributions and does not anticipate any future acts by other parties that could change the amount of the surplus that may ultimately be recovered.

Pension expense attributable to the Group's defined benefit scheme comprises current service cost, past service cost resulting from a scheme amendment or curtailment, net interest on the net defined benefit obligation/asset, gains or losses on settlement and administrative costs incurred. Where actuarial remeasurements arise, the Group recognises such amounts directly in equity through the statement of comprehensive income in the year in which they occur. Actuarial remeasurements arise from experience adjustments (the effects of differences between previous actuarial assumptions and what has actually occurred) and changes in actuarial assumptions.

### 3.3 Retirement benefit obligations continued

The Group's principal trading subsidiary, Clydesdale Bank PLC, is the sponsoring employer of the Yorkshire and Clydesdale Bank Pension Scheme, a defined benefit pension scheme, which was closed to future benefit accrual for the majority of current employees on 1 August 2017.

The following table summarises the present value of the defined benefit obligation and fair value of plan assets for the Scheme as at 30 September:

| | 2023<br>£m | 2022<br>£m |
|---|---|---|
| Active members' defined benefit obligation | **(4)** | (9) |
| Deferred members' defined benefit obligation | **(988)** | (987) |
| Pensioner and dependant members' defined benefit obligations | **(1,292)** | (1,220) |
| Total defined benefit obligation | **(2,284)** | (2,216) |
| Fair value of Scheme assets | **2,796** | 3,216 |
| Net defined benefit pension asset | **512** | 1,000 |
| Post-retirement medical benefits obligations[(1)] | **(2)** | (2) |

(1) Post-retirement medical benefits obligations are included within other liabilities (note 3.5).

**The Group's pension arrangements**

The current version of the Scheme was established under trust on 30 September 2009 with the assets held in a Trustee administered fund. The Trustee is responsible for the operation and governance of the Scheme, including making decisions regarding the Scheme's funding and investment strategy.

The Scheme is subject to the funding legislation outlined in the Pensions Act 2004 which came into force on 30 December 2005. This, together with documents issued by the Pensions Regulator, sets out the framework for funding defined benefit occupational pension plans in the UK.

The Group has implemented several reforms to the Scheme to manage the obligation. It closed the Scheme to new members in 2004 and since April 2006 has provided benefits accruing on a career average revalued earnings basis. On 1 August 2017, the Scheme was closed to future benefit accrual for the majority of current employees, with both affected and new employees' future pension benefits being provided through the Group's existing defined contribution scheme, 'My Retirement'. The income statement charge for this is separately disclosed in note 2.3.

The Group also provides post-retirement healthcare under a defined benefit scheme for some pensioners and their dependant relatives for which provision has been made on a basis consistent with the methodology applied to the defined benefit pension scheme. This is a closed scheme and the provision will be utilised over the life of the remaining scheme members. The obligation in respect of this scheme was £2m at 30 September 2023 (2022: £2m) and is included within other liabilities in note 3.5.

**Scheme valuations**

There are a number of means of measuring liabilities in the defined benefit schemes, with the ultimate aim of the Trustee being that the Scheme is 100% funded on an agreed self-sufficiency basis (which is where the Scheme is essentially self-funded and does not need to call on the Group for any additional funding). The two bases used by the Group to value its obligations are: (i) an IAS 19 accounting basis; and (ii) a Trustee's Technical Provision basis.

**(i) IAS 19 accounting basis**

The valuations of the Scheme assets and obligations are calculated on an accounting basis in accordance with the applicable accounting standard IAS 19 which provides the basis for the accounting framework and methodology for entries in the income statement, balance sheet and capital reporting. The principal purpose of this valuation is to allow comparison of pension obligations between companies. The obligation under an accounting valuation can be higher or lower than those under a Trustee's Technical Provision valuation.

The rate used to discount the obligation on an IAS 19 basis is a key driver of any potential volatility and is based on yields on AA rated high-quality corporate bonds, regardless of how the Trustee of the Scheme invests the assets. The accounting valuation under IAS 19 can therefore move adversely because of low rates and narrowing credit spreads which are not fully matched by the Scheme assets. Inflation is another key source of volatility and arises as a result of member benefits having an element of index linking, which causes the obligation to increase in line with rises in long-term inflation assumptions. In practice however, over the long term, the relationship between interest and inflation rates tends to be negatively correlated resulting in a degree of risk offset.

**(ii) Trustee's Technical Provision basis**

This valuation basis reflects how much money the Trustee considers is required now in order to provide for the promised benefits as they come up for payment in the future. The Trustee is responsible for ensuring that the calculation is conducted prudently on an actuarial basis, considering factors including the Scheme's investment strategy and the relative financial strength of the sponsoring employer.

A key aspect of this valuation is the investment strategy the Trustee proposes to follow as part of the policy for meeting the Scheme's obligations. Because there are no guarantees about investment returns over long periods, legislation requires the Trustee to consider carefully how much of their expected future investment returns it would be prudent for them to account for in advance.

### 3.3 Retirement benefit obligations continued

On 6 April 2023, the Scheme entered into a longevity swap transaction with Pacific Life Re International Limited and Zurich Assurance Ltd to manage longevity risk in relation to c.£1.6bn of pensioner liabilities. The arrangement provides long term protection to the Scheme against costs resulting from pensioners or their dependants living longer than currently expected, enhancing security for Scheme members and reducing risk for the Group. The fair value of the hedge instrument at 30 September 2023 was £Nil.

During 2023 the Trustee concluded the latest triennial valuation for the Scheme, which was conducted in accordance with Scheme data and market conditions as at 30 September 2022. The valuation resulted in an improvement in the Scheme's funding position, with a reported surplus of £256m (previously a surplus of £144m based on Scheme data and market conditions as at 30 September 2019) and a technical provisions funding level of 109% (previously 103%). As the 2022 valuation outcome was a funding surplus, a deficit recovery plan is not required and the Group is not required to make any additional contributions to the Scheme other than the ongoing funding of the Scheme's administrative expenses.

The next triennial valuation will be conducted in the year ending 30 September 2026 based on Scheme data and market conditions as at 30 September 2025.

Scheme assets are not subject to the same valuation differences as Scheme obligations and are consistently valued at current market value.

**IAS 19 position**

The Scheme movements in the year are as follows:

| | 2023 | | | | 2022 | | | |
|---|---|---|---|---|---|---|---|---|
| | Present value of obligation £m | Fair value of plan assets £m | Total £m | Cumulative impact in other comprehensive income £m | Present value of obligation £m | Fair value of plan assets £m | Total £m | Cumulative impact in other comprehensive income £m |
| **Balance sheet surplus at 1 October** | **(2,216)** | **3,216** | **1,000** | | (3,789) | 4,636 | 847 | |
| | | | | **(126)** | | | | (248) |
| **(Charges)/credits** | | | | | | | | |
| Past service credit | **–** | **–** | **–** | | 9 | – | 9 | |
| Interest (expense)/income | **(117)** | **172** | **55** | | (84) | 104 | 20 | |
| Administrative costs | **–** | **(5)** | **(5)** | | – | (5) | (5) | |
| **Total (charge)/credit recognised in the consolidated income statement (note 2.3)** | **(117)** | **167** | **50** | | (75) | 99 | 24 | |
| **Remeasurements** | | | | | | | | |
| Return on Scheme assets greater than discount rate | **–** | **(470)** | **(470)** | **(470)** | – | (1,393) | (1,393) | (1,393) |
| *Actuarial:* | | | | | | | | |
| Loss – experience adjustments | **(151)** | **–** | **(151)** | **(151)** | (16) | – | (16) | (16) |
| (Loss)/gain – demographic assumptions | **(27)** | **–** | **(27)** | **(27)** | 36 | – | 36 | 36 |
| Gain – financial assumptions | **104** | **–** | **104** | **104** | 1,495 | – | 1,495 | 1,495 |
| **Remeasurement (losses)/gains recognised in other comprehensive income** | **(74)** | **(470)** | **(544)** | **(544)** | 1,515 | (1,393) | 122 | 122 |
| **Contributions and payments** | | | | | | | | |
| Employer contributions | **–** | **6** | **6** | | – | 7 | 7 | |
| Disbursements | **123** | **(123)** | **–** | | 133 | (133) | – | |
| | **123** | **(117)** | **6** | | 133 | (126) | 7 | |
| **Balance sheet surplus at 30 September** | **(2,284)** | **2,796** | **512** | | (2,216) | 3,216 | 1,000 | |
| | | | | **(670)** | | | | (126) |

**3.3 Retirement benefit obligations continued**

In July 2021, the Trustees communicated a Pension Increase Exchange (PIE) exercise to members. A PIE gives members the option to exchange future increases on their pensions for a one-off uplift to their current pension. The exercise is being undertaken in three phases and is due to complete later in calendar year 2023. The defined benefit pension credit in the current year therefore includes no impact (2022: £10m credit) arising from the PIE exercise; any past service credit arising is not expected to be material and will be recognised when the exercise concludes in FY24.

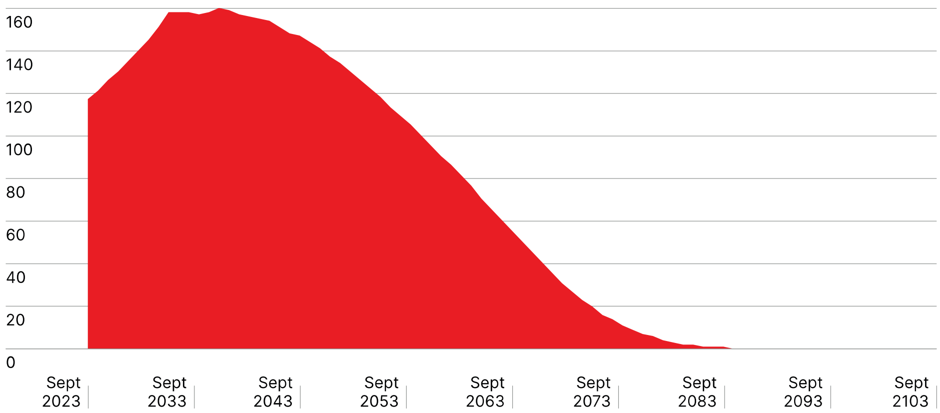
The expected contributions and benefit payments for the year ending 30 September 2024 are £6m (2023: £10m) and £115m (2023: £118m) respectively.

During the year, the Group and Trustee to the Scheme ceased their previous contingent security arrangement, subsequently the Group has granted a £75m uncommitted liquidity facility to the Scheme as an additional contingency against future short-term liquidity challenges resulting from unexpected market turbulence. As at 30 September 2023 the amount drawn under the facility was £Nil.

**Maturity of Scheme liabilities**

The estimated maturity period of Scheme obligations on an IAS 19 accounting basis is as follows:

**Annual Pension Scheme liability cash flows (£m)**




The discounted mean term of the defined benefit obligation at 30 September 2023 is 13 years (2022: 14 years).

**Scheme assets**

In order to meet the obligations of the Scheme, the Trustee invests in a diverse portfolio of assets, with the level and volatility of asset returns being a key factor in the overall investment strategy. The investment portfolio is subject also to a range of risks typical of the types of assets held, such as: equity risk; credit risk on bonds; currency risk; interest rate and inflation risk; and exposure to the property market. The Trustee's investment strategy (including physical assets and derivatives) seeks to reduce the Scheme's exposure to these risks. In managing interest rate and inflation risks, the investment strategy seeks to hold portfolios of matching assets (including derivatives) that enable the Scheme's assets to better match movements in the value of liabilities due to changes in interest rates and inflation.

As at 30 September 2023, the interest rate and inflation rate hedge ratios were 90% and 90% respectively (2022: 97% and 95%) of the obligation when measured on a self-sufficiency basis. This strategy reflects the Scheme's obligation profile and the Trustee's and the Group's attitude to risk. The Trustee monitors the investment objectives and asset allocation policy on a regular basis.

The Trustee's investment strategy involves two main categories of investments:

- Matching assets – a range of investments that provide a match to changes in obligation values.
- Return seeking assets – a range of investments designed to provide specific, planned and consistent returns.

### 3.3 Retirement benefit obligations continued

The major categories of plan assets for the Scheme, stated at fair value, are as follows:

| | 2023 | | | | 2022 | | | |
|---|---|---|---|---|---|---|---|---|
| | Quoted £m | Unquoted £m | Total £m | % | Quoted £m | Unquoted £m | Total £m | % |
| **Bonds** | | | | | | | | |
| Fixed government | **558** | **–** | **558** | | 350 | – | 350 | |
| Index-linked government | **824** | **–** | **824** | | 1,314 | – | 1,314 | |
| Global sovereign | **84** | **–** | **84** | | 90 | 2 | 92 | |
| Corporate and other | **924** | **–** | **924** | | 781 | 37 | 818 | |
| | **2,390** | **–** | **2,390** | **85%** | 2,535 | 39 | 2,574 | 80% |
| **Equities[1]** | | | | | | | | |
| Global equities | **–** | **–** | **–** | | – | 137 | 137 | |
| Emerging market equities | **–** | **–** | **–** | | – | 14 | 14 | |
| UK equities | **–** | **–** | **–** | | – | 7 | 7 | |
| | **–** | **–** | **–** | **–%** | – | 158 | 158 | 5% |
| **Other** | | | | | | | | |
| Alternative credit investments[2] | **–** | **352** | **352** | | – | 874 | 874 | |
| Derivatives[3] | **–** | **30** | **30** | | – | (83) | (83) | |
| Repurchase agreements | **–** | **(383)** | **(383)** | | – | (803) | (803) | |
| Property | **–** | **47** | **47** | | – | 59 | 59 | |
| Renewables | **–** | **238** | **238** | | – | 194 | 194 | |
| Cash | **–** | **122** | **122** | | – | 243 | 243 | |
| | **–** | **406** | **406** | **15%** | – | 484 | 484 | 15% |
| **Total Scheme assets** | **2,390** | **406** | **2,796** | **100%** | 2,535 | 681 | 3,216 | 100% |

(1) Equity investments are classified as unquoted, reflecting the nature of the funds in which the Scheme invests directly. The underlying investments within those funds are, however, mostly quoted.
(2) Alternative credit investments includes both secured income alternatives and alternative credit which were presented separately in the prior year.
(3) Derivative financial instruments are used to modify the profile of the assets of the Scheme to better match the Scheme liabilities. Derivative holdings may lead to increased or decreased exposures to the physical asset categories disclosed above.

The nature of the Scheme assets held has remained broadly consistent year on year, with the exception of equities and certain alternative credit assets (principally hedge equity and hedge multi strategy assets) which the Trustee made a conscious decision to sell out of as part of its de-risking strategy and to raise further liquidity for collateral purposes.

At 30 September 2023, the Scheme had employer-related investments within the meaning of Section 40 (2) of the Pensions Act 1995 totalling £1m (2022: £2m).

### Actuarial assumptions

The following assumptions were used in arriving at the IAS 19 defined benefit obligation:

| | 2023 % p.a. | 2022 % p.a. |
|---|---|---|
| **Financial assumptions** | | |
| Discount rate | **5.65** | 5.45 |
| Inflation (RPI) | **3.30** | 3.58 |
| Inflation (CPI) | **2.70** | 2.94 |
| Career average revalued earnings revaluations: | | |
| Pre 31 March 2012 benefits (RPI) | **3.30** | 3.58 |
| Post 31 March 2012 benefits (CPI capped at 5% per annum) | **2.66** | 2.90 |
| Pension increases (capped at 2.5% per annum) | **2.14** | 2.21 |
| Pension increases (capped at 5% per annum) | **3.15** | 3.37 |
| Rate of increase for pensions in deferment | **2.66** | 2.91 |

### 3.3 Retirement benefit obligations continued

**Demographic assumptions**

| | 2023 Years | 2022 Years |
|---|---|---|
| **Post-retirement mortality:** | | |
| Current pensioners at 60 – male | **27.2** | 27.0 |
| Current pensioners at 60 – female | **29.4** | 29.3 |
| Future pensioners at 60 – male | **28.3** | 28.0 |
| Future pensioners at 60 – female | **30.4** | 30.4 |

**Critical accounting estimates and judgements**

The value of the Group's defined benefit pension scheme requires management to make several assumptions. The key areas of estimation uncertainty in these assumptions are:

*discount rate*: this is set with reference to market yields at the end of the reporting year on high-quality corporate bonds in the currency and with a term consistent with the Scheme's obligations. The average duration of the Scheme's obligations is approximately 13 years. The market for bonds with a similar duration is illiquid and, as a result, significant management judgement is required to determine an appropriate yield curve on which to base the discount rate;

*inflation*: this is set with reference to market expectations of the RPI measure of inflation for a term consistent with the Scheme's obligations, based on data published by the BoE. Other measures of inflation (such as CPI, or inflation measures subject to an annual cap) are derived from this assumption; and

*mortality*: the cost of the benefits payable by the Scheme will also depend upon the life expectancy of the members. The assumptions for mortality rates are based on standard mortality tables (as adjusted to reflect the characteristics of Scheme members) which allow for future improvements in life expectancies.

The table below sets out the sensitivity and impact on the balance sheet surplus position of the Scheme, the defined benefit obligation and pension cost to changes in the key actuarial assumptions:

| Assumption Change | | Balance sheet surplus £m | Obligation £m | Pension cost £m |
|---|---|---|---|---|
| **Discount rate** | +0.25% | (18) | (70) | – |
| | −0.25% | 17 | 74 | – |
| **Inflation** | +0.25% | 9 | 42 | – |
| | −0.25% | (6) | (43) | – |
| **Life expectancy** | +1 year | (22) | 50 | (1) |
| | −1 year | 22 | (50) | 1 |

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, changes in some of the assumptions may be correlated.

# Section 3: Assets and liabilities

### 3.4 Other assets

| | 2023 £m | 2022 £m |
|---|---|---|
| Property, plant and equipment | **184** | 211 |
| Investment properties | **40** | – |
| Finance sub-leases | **2** | 3 |
| Investment in associates | **10** | 10 |
| Prepayments | **59** | 66 |
| Other receivables | **66** | 87 |
| Current tax | **21** | – |
| Other | **6** | 5 |
| | **388** | 382 |

The prior year balance of £382m has been restated from the original £171m by the addition of the property, plant and equipment balance of £211m (note 1.7). This includes right-of-use assets of £115m (2022: £113m) (note 3.6).

The Group classified £43m of lease right-of-use assets as investment property on initial recognition this year as there is surplus space which will be sub-let under an operating lease. Also in the year, freehold land and buildings with a carrying value of £9m were transferred from property, plant and equipment to investment properties following a change in use (note 1.7). Subsequently, an impairment of £6m was recognised in respect of these freehold land and buildings based on the fair value confirmed by an independent professional valuation by Royal Institution of Chartered Surveyors registered valuers. The Group estimated the fair value of the leased right-of-use investment property assets at 30 September 2023 using income based fair value techniques and available market data, an independent valuation was not obtained. The estimated fair value approximates the carrying value.

No material rental income from investment property was received in the year, with the majority of assets currently being marketed for rental.

### 3.5 Other liabilities

| | 2023 £m | 2022 £m |
|---|---|---|
| Notes in circulation | **1,675** | 1,822 |
| Accruals and deferred income | **67** | 74 |
| Current tax | **–** | 1 |
| Other | **414** | 498 |
| | **2,156** | 2,395 |

The prior year balance of £2,395m has been restated from the original £2,394m by the addition of the current tax balance of £1m (note 1.7).

### 3.6 Lessee accounting

**a) Amounts recognised in the income statement**
The income statement includes the following amounts related to leases:

| | 2023 £m | 2022 £m |
|---|---|---|
| **Interest expense and similar charges** | | |
| Interest expense | **(4)** | (2) |
| **Other operating income** | | |
| Income from operating sub-leases where the Group is a lessor | **1** | 1 |
| **Operating and administrative expenses** | | |
| Depreciation and impairment of right-of-use assets | **(26)** | (26) |
| Expense relating to short-term leases | **(2)** | (1) |
| Expense relating to leases of low-value assets that are not short-term leases | **(1)** | (1) |
| **Amounts recognised in the income statement** | **(32)** | (29) |

Total leasing cash outflow in the year was £27m (2022: £28m).

# Section 3: Assets and liabilities

### 3.6 Lessee accounting continued

**b) Amounts recognised on the balance sheet**
**Right-of-use assets**

| | 2023 £m | 2022 £m |
|---|---|---|
| **As at 1 October** | **113** | 135 |
| Additions | **76** | 4 |
| Remeasurements | **(4)** | 1 |
| Disposals | **(1)** | (1) |
| Depreciation and impairment | **(31)** | (26) |
| **As at 30 September** | **153** | 113 |
| **Of which:** | | |
| Property, plant and equipment (note 3.4) | **115** | 113 |
| Investment property (note 3.4) | **38** | – |

In February 2023, the Group announced plans for the closure of six leased office properties. Following the announcement, the associated right-of-use assets were assessed for impairment. An impairment charge of £3m has been recognised within operating and administrative expenses.

In July 2023, the Group announced plans for the closure of 39 stores, of which 34 were leasehold properties. Following the announcement, the associated right-of-use assets were assessed for impairment. Where it is expected that the Group can sub-lease the property, the recoverable amount was determined based on expected sub-lease income. Where the Group does not expect to be able to generate any cash inflows beyond the closure date, the value-in-use was determined to be £Nil. An impairment charge of £7m has been recognised within operating and administrative expenses. In addition to the impairment charge relating to the right-of-use assets, a provision has been recognised for other costs associated with the closures (note 3.7).

In the prior year, 19 surplus properties were impaired following a reduction in estimated value-in-use, resulting in an impairment charge of £4m. In addition, an impairment of £5m was recognised in relation to right-of-use assets for office estate where no further economic benefit was expected following exit.

**Sub-leases**
Future undiscounted minimum payments receivable in respect of sub-leased assets at 30 September were as follows:

| | 2023 £m | 2022 £m |
|---|---|---|
| Operating leases | **3** | 1 |
| Finance leases | **2** | 3 |
| | **5** | 4 |

**Lease liabilities**

| | 2023 £m | 2022 £m |
|---|---|---|
| Lease liabilities(1) | **180** | 132 |

(1) Lease liabilities are presented within other liabilities (note 3.5) on the balance sheet.

Future undiscounted minimum payments under lease liabilities at 30 September are as follows:

| Amounts falling due | 2023 £m | 2022 £m |
|---|---|---|
| Within 1 year | **22** | 22 |
| Between 1 and 5 years | **63** | 60 |
| Over 5 years | **142** | 66 |
| | **227** | 148 |

### 3.6 Lessee accounting continued

#### c) Lease commitments not recognised on the balance sheet

In addition to the lease liabilities recognised on the balance sheet, the Group also has lease commitments relating to leases which have not yet commenced at the balance sheet date.

Future undiscounted minimum payments on leases which are yet to commence were as follows:

| Amounts falling due | 2023 £m | 2022 £m |
|---|---|---|
| Within 1 year | **–** | 4 |
| Between 1 and 5 years | **1** | 22 |
| Over 5 years | **5** | 99 |
| | **6** | 125 |

#### d) Leased investment property

Right-of-use asset additions shown in 3.6(b) above include £43m of assets classified as investment property (2022: £Nil). Depreciation charges of £1m were recognised in the year (2022: £Nil) and a £4m impairment charge was also recognised (2022: £Nil) relating to leased investment property floors. The leased investment property balance at 30 September 2023 was £38m (2022: £Nil).

### 3.7 Provisions for liabilities and charges

| | Employee related costs provision £m | Customer related provision £m | Property provision £m | Off-balance sheet ECL provisions[1] £m | Total |
|---|---|---|---|---|---|
| **As at 1 October 2021** | 22 | 19 | 55 | 8 | 104 |
| Charge/(credit) to the income statement | 2 | 8 | – | (5) | 5 |
| Utilised | (17) | (14) | (28) | – | (59) |
| **As at 30 September 2022** | 7 | 13 | 27 | 3 | 50 |
| Charge to the income statement | 7 | – | 24 | 2 | 33 |
| Utilised | (6) | (3) | (5) | – | (14) |
| **As at 30 September 2023** | **8** | **10** | **46** | **5** | **69** |

(1) The Group's ECL accounting policy can be found in note 3.1.1.1.

#### Employee related costs provision

This includes provision for staff redundancies and for NIC on equity based compensation. During the year, provisions of £7m (2022: £2m) were raised relating to staff redundancy costs.

#### Customer related provision

This relates to customer matters, legal proceedings, and claims arising in the ordinary course of the Group's business. A number of these matters are now reaching a conclusion and the risk that the final amount required to settle the Group's potential liabilities in these matters being materially more than the remaining provision is now considered to be low.

#### Property provision

This includes costs for stores and office closures. During the year, provisions of £24m (2022: £Nil) were raised.

# Section 4: Capital

## 4.1 Equity

### 4.1.1 Share capital and share premium

| | 2023 £m | 2022 £m |
|---|---|---|
| Share capital | **134** | 141 |
| Share premium | **9** | 7 |
| **Share capital and share premium** | **143** | 148 |

| | 2023 Number of shares | 2022 Number of shares | 2023 £m | 2022 £m |
|---|---|---|---|---|
| **Ordinary shares of £0.10 each – authorised, allotted, called up and fully paid** | | | | |
| Opening ordinary share capital | **1,408,530,988** | 1,439,993,431 | **141** | 144 |
| Issued under employee share schemes | **3,947,282** | 2,982,745 | **–** | – |
| Share buyback programme | **(67,837,302)** | (34,445,188) | **(7)** | (3) |
| **Closing ordinary share capital** | **1,344,640,968** | 1,408,530,988 | **134** | 141 |

The holders of ordinary shares are entitled to dividends as declared from time to time and are entitled to one vote per share at meetings of the shareholders of the Company. All shares in issue at 30 September 2023 rank equally with regard to the Company's residual assets.

The following dividends were declared in the current and prior periods:

- A final dividend in respect of the year ended 30 September 2021 of 1p per ordinary share in the Company, amounting to £14m, was paid in March 2022.
- An interim dividend in respect of the year ended 30 September 2022 of 2.5p per ordinary share in the Company, amounting to £36m, was paid in June 2022.
- A final dividend in respect of the year ended 30 September 2022 of 7.5p per ordinary share in the Company, amounting to £103m, was paid in March 2023.
- An interim dividend in respect of the year ended 30 September 2023 of 3.3p per ordinary share in the Company, amounting to £45m, was paid in June 2023.

The Directors have recommended a final dividend in respect of the year ended 30 September 2023 of 2.0p per ordinary share in the Company, to be paid in March 2024. The payment of the final dividend is subject to approval of the shareholders at the 2024 AGM. These financial statements do not reflect the recommended dividend.

The following share buybacks have been announced in the current and prior periods:

- On 30 June 2022, the Company announced an initial repurchase of up to £75m. The buyback commenced on 30 June 2022 and ended on 9 December 2022.
- On 21 November 2022, the Company announced an extension to the share buyback programme with an intent to repurchase a further £50m. The buyback extension commenced on 21 November 2022 and ended on 7 March 2023.
- On 2 August 2023, the Company announced a new share buyback programme to repurchase £50m. The buyback commenced on 2 August 2023 and ended on 22 November 2023.

68m ordinary shares (2022: 34m), with a nominal value of £7m (2022: £3m), were repurchased in the year for a total consideration of £112m (2022: £50m).

Each buyback is completed in aggregate between the Company's ordinary shares of £0.10 each listed on the LSE and CDIs, each representing one share, listed on the ASX. The Company repurchased shares and CDIs in approximately equal proportions. All shares repurchased were cancelled and the nominal value of the share cancellation transferred to the capital redemption reserve with the premium paid deducted from retained earnings.

On 23 November 2023, the Company announced a further share buyback with an intent to repurchase another £150m, ending no later than 16 May 2024.

Share premium represents the aggregate of all amounts that have ever been paid above par value to the Company when it has issued ordinary shares.

A description of the other equity categories included within the consolidated statement of changes in equity, and significant movements during the year, is provided below:

#### 4.1.2 Other equity instruments
Other equity instruments comprises AT1 capital which consists of the following Perpetual Contingent Convertible Notes:

| | 2023 | | 2022 | |
|---|---|---|---|---|
| | Carrying value £m | Nominal value £m | Carrying value £m | Nominal value £m |
| Perpetual securities (fixed 8% up to the first reset date) issued on 8 February 2016 with an optional redemption on 8 December 2022. | **–** | **–** | 72 | 73 |
| Perpetual securities (fixed 9.25% up to the first reset date) issued on 13 March 2019 with an optional redemption on 8 June 2024. | **247** | **250** | 247 | 250 |
| Perpetual securities (fixed 8.25% up to the first reset date) issued on 17 June 2022 with an optional redemption on 17 June 2027. | **347** | **350** | 347 | 350 |
| | **594** | **600** | 666 | 673 |

On 8 December 2022, perpetual securities (fixed 8% up to the first reset date) issued on 8 February 2016 totalling £72m were redeemed.

The issuances are treated as equity instruments in accordance with IAS 32 'Financial instruments: presentation' with the proceeds included in equity, net of transaction costs, which is the difference between the nominal and carrying values. AT1 distributions of £54m were paid in the year (2022: £70m).

#### 4.1.3 Capital reorganisation reserve
The capital reorganisation reserve of £839m was recognised on the issuance of the Company's ordinary shares in February 2016 in exchange for the acquisition of the entire share capital of the Group's previous parent company, CYB Investments Limited (CYBI). The reserve reflects the difference between the consideration for the issuance of the Company's shares and CYBI's share capital and share premium.

#### 4.1.4 Merger reserve
A merger reserve of £633m was recognised on the issuance of the Company's ordinary shares in February 2016 in exchange for the acquisition of the entire share capital of CYBI. An additional £1,495m was recognised on the issuance of the Company's ordinary shares in October 2018 in exchange for the acquisition of the entire share capital of Virgin Money Holdings (UK) Limited. The merger reserve reflects the difference between the consideration for the issuance of the Company's shares and the nominal value of the shares issued.

#### 4.1.5 Other reserves
**Own shares held**
Virgin Money Holdings (UK) Limited established an EBT (the 'VMH EBT') in 2011 in connection with the operation of its share plans. On the date of acquisition by the Company, the shares held in the VMH EBT were converted to the Company's shares at a ratio of 1.2125 Company shares for each Virgin Money Holdings (UK) Limited share. The investment in own shares as at 30 September 2023 is £0.3m (2022: £0.6m). The market value of the shares held in the VMH EBT at 30 September 2023 was £0.2m (2022: £0.4m).

During the current year, Virgin Money UK PLC also established an EBT (the 'VMUK EBT') in connection with the operation of its share plans. The investment in own shares as at 30 September 2023 was £2.0m (2022: £Nil). The market value of the shares held in the VMUK EBT at 30 September 2023 was £1.9m (2022: £Nil).

The total investment in own shares as at 30 September 2023 was £2.3m (2022: £0.6m). The total market value of the shares held in both EBTs at 30 September 2023 was £2.1m (2022: £0.4m).

As part of the buyback programme, the Company has entered a non-discretionary arrangement with Citigroup Global Markets Limited to purchase shares as riskless principal and to make trading decisions independently of the Company. Any purchase of shares pursuant to this engagement will be carried out on the LSE or other recognised investment exchange. This arrangement results in the recognition of a liability (included within due to other banks) and a deduction from retained earnings of £14m at 30 September 2023 (2022: £11m). The liability will reduce as shares are repurchased and cancelled with the impact on share capital and capital redemption reserve as described elsewhere within this note.

**Capital redemption reserve**
Under UK companies legislation, when shares are redeemed or purchased wholly or partly out of the company's profits, the amount by which the company's issued share capital is diminished must be transferred to the capital redemption reserve. The capital maintenance provisions of UK companies legislation apply to the capital redemption reserve as if it were part of the company's paid up share capital. The nominal value of the shares repurchased and cancelled under the buyback programmes has been transferred to the capital redemption reserve.

**Deferred shares reserve**
The deferred shares reserve comprises shares to be issued in the future relating to employee share plans in regard to the settlement of outstanding Virgin Money Holdings (UK) Limited share awards, which will be settled through the issuance of the Company's shares at a future date in line with the vesting profile of the underlying plans.

**Equity based compensation reserve**
The Group's equity based compensation reserve records the value of equity settled share based payment benefits provided to the Group's employees as part of their remuneration that has been charged through the income statement and adjusted for deferred tax.

**FVOCI reserve**
The FVOCI reserve records the unrealised gains and losses arising from changes in the fair value of financial assets at FVOCI. The movements in this reserve are detailed in the consolidated statement of comprehensive income.

# Section 4: Capital

### 4.1.5 Other reserves continued

**Cash flow hedge reserve**

The cash flow hedge reserve represents the effective portion of cumulative post-tax gains and losses on derivatives designated as cash flow hedging instruments that will be recycled to the income statement when the hedged items affect profit or loss.

| | 2023 £m | 2022 £m |
|---|---|---|
| At 1 October | **699** | 10 |
| **Amounts recognised in other comprehensive income:** | | |
| **Cash flow hedge – interest rate risk** | | |
| Effective portion of changes in fair value of interest rate swaps | **(268)** | 962 |
| Amounts transferred to the income statement | **(12)** | (13) |
| Taxation | **77** | (260) |
| **Cash flow hedge – foreign exchange risk** | | |
| Effective portion of changes in fair value of cross currency swaps | **–** | – |
| Amounts transferred to the income statement | **–** | – |
| **At 30 September** | **496** | 699 |

## 4.2 Pillar 3 disclosures

**UK Capital Requirements Regulation**

Pillar 3 disclosure requirements are set out within the Disclosure (CRR) part of the PRA rulebook. The disclosures required under the PRA framework are substantially equivalent to those required by Part Eight of the EU CRR. The consolidated disclosures of the Group, for the 2023 financial year, will be issued concurrently with the Annual Report and Accounts and can be found at www.virginmoneyukplc.com/investor-relations/results-and-reporting/annual-reports/

# Section 5: Other notes

## 5.1 Contingent liabilities and commitments

**Accounting policy**
***Financial guarantees***
The Group provides guarantees in the normal course of business on behalf of its customers. Guarantees written are conditional commitments issued by the Group to guarantee the performance of a customer to a third party and are primarily issued to support direct financial obligations such as commercial bills or other debt instruments issued by a counterparty. The rating of the Group as a guarantee provider enhances the marketability of the paper issued by the counterparty in these circumstances.

The ECL requirements as described in note 3.1.1 apply to loan commitments and financial guarantee contracts, with the ECL allowance held as part of the provisions for liabilities and charges balance (note 3.7).

The table below sets out the amounts of financial guarantees and commitments which are not recorded on the balance sheet. Financial guarantees and commitments are credit-related instruments which include acceptances, letters of credit, guarantees and commitments to extend credit. The amounts do not represent the amounts at risk at the balance sheet date but the amounts that would be at risk should the contracts be fully drawn upon and the customer default. Since a significant portion of guarantees and commitments is expected to expire without being drawn upon, the total of the contract amounts is not representative of future liquidity requirements.

| | 2023<br>£m | 2022<br>£m |
|---|---|---|
| Guarantees and assets pledged as collateral security: | | |
| Due in less than 3 months | **12** | 33 |
| Due between 3 months and 1 year | **18** | 23 |
| Due between 1 year and 3 years | **8** | 9 |
| Due between 3 years and 5 years | **1** | 3 |
| Due after 5 years | **40** | 44 |
| | **79** | 112 |
| **Other credit commitments** | | |
| Undrawn formal standby facilities, credit lines and other commitments to lend at call | **17,921** | 19,247 |

**Capital commitments**
The Group had future capital expenditure which had been contracted for, but not provided for, at 30 September 2023 of £0.1m (2022: £0.4m).

**Other contingent liabilities**
**Conduct risk related matters and legal claims**
There continues to be uncertainty with judgement required in determining the quantum of conduct risk related liabilities, with note 3.7 reflecting the Group's current position where a provision can be reliably estimated. Until all matters are resolved the final amount required to settle the Group's potential liabilities for conduct related matters remains uncertain.

The Group will continue to reassess the adequacy of provisions for these matters and the assumptions underlying the calculations at each reporting date based upon experience and other relevant factors at that time.

The Group's subsidiary, Clydesdale Bank PLC, along with its former parent company, National Australia Bank Limited, is a defendant in nine separate claims (comprising 904 individual claimants) co-ordinated by the claims management company, RGL Management Limited, in connection with (i) the payment of break costs and (ii) the composition of fixed interest rates, both, in respect of historic tailored business loans. The cases involving four individual claimants (being the first and fourth claims) are currently being heard before His Majesty's High Court of Justice, with the hearing scheduled to conclude on 20 December 2023. The remaining claims are currently stayed by agreement and court order. Clydesdale Bank PLC is robustly defending all such claims. No provision has been made in these financial statements in respect of the current claims, nor any other claims of a similar nature which may be brought by other claimants.

The Group is named in and is defending a number of other legal claims arising in the ordinary course of business. No material adverse impact on the financial position of the Group is expected to arise from the ultimate resolution of these legal actions.

### 5.2 Equity based compensation

The equity settled share based payment charge for the year is £5m (2022: £5m).

**Virgin Money UK PLC awards**
The Group issues awards to employees under the following share plans:

| Plan | Eligible employees | Nature of award | Vesting conditions(1) | Grant dates(2) |
|---|---|---|---|---|
| DEP(3) | Selected employees | Conditional rights to shares | Continuing employment or leaving in certain limited circumstances | 2017, 2018, 2019, 2020, 2021 and 2022 |
| LTIP | Selected senior employees | Conditional rights to shares | Continuing employment or leaving in certain limited circumstances and achievement of delivery of the Group's strategic goals and growth in shareholder value | 2017, 2018, 2019, 2020, 2021 and 2022 |

(1) All awards are subject to vesting conditions and therefore may or may not vest.
(2) The year in which grants have been made under the relevant plan.
(3) Grants made under the DEP are made the year following the financial year to which they relate.

Further detail on each plan is provided below:

**DEP**
Under the plan, employees are awarded conditional rights to Virgin Money UK PLC shares. The shares are subject to forfeiture conditions including forfeiture as a result of resignation, termination by the Group or failure to meet compliance requirements. Awards include:

- the upfront and deferred elements of bonus awards where required to comply with the PRA Remuneration Code or the Group's deferral policy; and
- buyout of equity from previous employment.

**LTIP**
Under the plan, employees are awarded conditional rights to Virgin Money UK PLC shares. The shares are subject to forfeiture conditions including forfeiture as a result of resignation, termination by the Group or failure to meet compliance requirements. The performance conditions of the plan must be met over a three-year performance period. The measures reflect a balanced approach between financial and non-financial performance and are aligned to the Group's strategic goals. Measures, relative weightings and the quantum for assessing performance are outlined in the Directors' remuneration report contained in the Group's Annual Report and Accounts.

**Awards/rights made during the year**

| Plan | Number outstanding at 1 October 2022 | Number awarded | Number forfeited | Number released | Number outstanding at 30 September 2023 | Average fair value of awards at grant pence |
|---|---|---|---|---|---|---|
| **DEP** | | | | | | |
| 2016 Commencement | 1,310 | – | – | (1,310) | **–** | 266.03p |
| 2017 Bonus | 2,120 | – | – | (2,120) | **–** | 313.20p |
| 2018 Bonus | 136,520 | – | – | (34,129) | **102,391** | 192.35p |
| 2019 Bonus | 79,160 | – | – | (18,388) | **60,772** | 174.50p |
| 2019 Commencement | 8,046 | – | – | (5,195) | **2,851** | 174.50p |
| 2020 Commencement | 9,600 | – | – | (5,908) | **3,692** | 135.40p |
| 2021 Commencement | 107,747 | – | – | (64,315) | **43,432** | 142.70p |
| 2022 Bonus | – | 1,289,482 | – | (1,109,992) | **179,490** | 176.75p |
| 2023 Commencement | – | 567,651 | – | (110,384) | **457,267** | 158.95p |
| **LTIP** | | | | | | |
| 2017 LTIP | 269,629 | – | – | (125,918) | **143,711** | 313.20p |
| 2018 LTIP | 2,000,311 | – | – | (620,091) | **1,380,220** | 190.47p |
| 2019 LTIP | 6,941,307 | – | (4,721,502) | (694,962) | **1,524,843** | 174.50p |
| 2020 LTIP | 8,359,759 | – | (274,998) | – | **8,084,761** | 135.40p |
| 2021 LTIP | 6,487,823 | – | (531,566) | – | **5,956,257** | 172.65p |
| 2022 LTIP | – | 7,265,385 | (365,233) | – | **6,900,152** | 176.75p |

# Section 5: Other notes

### 5.2 Equity based compensation continued

**Determination of grant date fair values**
Where awards are subject to only non-market performance conditions the grant date fair value of the awards has been taken as the middle market share price value on the day immediately preceding the grant. An estimate is made of the number of awards expected to vest in order to determine the overall share based payment charge to be recognised over the vesting period. Where awards contain market performance conditions, these are incorporated into the calculation of grant date fair value using Monte Carlo simulation pricing models. During the year, awards were granted under the LTIP on 9 December 2022 and under the DEP on 9 December 2022 and 20 June 2023, based on the middle market share price on the day immediately preceding the grant.

### 5.3 Related party transactions

The Group undertakes activity with the following entities which are considered to be related party transactions:

**Yorkshire and Clydesdale Bank Pension Scheme ('the Scheme')**
The Group provides banking services to the Scheme, with customer deposits of £7m (2022: £12m). Pension contributions of £7m were made to the Scheme in the year (2022: £7m).

During the year, the Group and Trustee to the Scheme ceased their previous contingent security arrangement, subsequently the Group has granted a £75m uncommitted liquidity facility to the Scheme as an additional contingency against future short-term liquidity challenges resulting from unexpected market turbulence. As at 30 September 2023, the amount drawn under the facility was £Nil. There is also a £7m BACS facility held for the Scheme in relation to payments to the Scheme's members (2022: £7m). As at 30 September 2023, the amount drawn on the facility was £Nil (2022: £Nil).

**JVs and associates**
The Group holds investments in JVs of £10m (2022: £10m). The total share of profit for the year was £Nil (2022: loss of £4m). In addition, the Group had the following transactions with JV entities during the year:

- Salary Finance – the Group provides Salary Finance with a revolving credit facility funding line, of which the current gross lending balance was £290m (2022: £318m) and the undrawn facility was £60m (2022: £32m). The facility is held under Stage 2 for credit risk purposes (2022: Stage 2), with an ECL allowance of £22m (2022: £19m) held against the lending. An impairment charge of £3m (2022: £19m) was recognised in the year. The lending made via Salary Finance continues to be held as part of the Group's Unsecured lending portfolio and consists of personal lending to Salary Finance customers. During the year, the number of customers not maintaining scheduled loan repayments has reduced slightly with no material change to the ECL allowance held from that at September 2022. Additionally, the Group received £16m (2022: £10m) of interest income from Salary Finance in the year and holds deposits of £10m (2022: £10m). Board approval is in place for this facility up until December 2025 with £350m being the approved limit; and
- UTM – the Group provides banking services to UTM which has resulted in amounts due of £3m (2022: £4m). Additionally, the Group received £9m of recharge income in the year (2022: £7m) from UTM in accordance with a Service Level Agreement in respect of resourcing, infrastructure and marketing. During the year, the Group provided no additional funding to UTM (2022: £4m). The Group has also paid consortium relief to UTM of £1m (2022: £Nil) for losses surrendered from UTM in respect of FY21 and FY22. During the year, the Group provided UTM with a 30 day notice account with customer deposits of £17m (2022: £Nil) which resulted in interest of £0.5m being paid to UTM (2022: £Nil). The Group also provided UTM with five term deposit accounts during the year. £16m was originally held in deposit, however these matured in September 2023 (2022: £Nil).

**Other related party transactions with Virgin Group**
The Group has related party transactions with other Virgin Group companies(1):

- Licence fees due to Virgin Enterprises Limited for the use of the Virgin Money brand trademark resulted in an amount payable of £5m (2022: £5m), with expenses incurred in the year of £17m (2022: £15m).
- The Group incurs credit card commissions and air mile charges with Virgin Atlantic Airways Limited (VAA) in respect of an agreement between the two parties. Amounts payable to VAA totalled £2m (2022: £1m) and expenses of £17m were incurred in the year (2022: £16m).
- The Group incurs charges and receives commissions concerning the cashback incentive scheme with Virgin Red Limited in relation to the credit card and PCA portfolio. Amounts receivable totalled £0.2m (2022: £0.1m), amounts payable totalled £0.1m (2022: £1m) and during the year this resulted in expenses of £0.5m (2022: £3m) along with income of £0.4m (2022: £0.5m).
- The Group has an arrangement with Virgin Start Up Limited to host a series of events, podcasts and videos and other digital content. During the year this resulted in amounts payable of £0.1m (2022: £Nil) and expenses of £0.4m (2022: £0.5m).
- The Group paid £20m (2022: £7m) of ordinary dividends to Virgin Group Holdings Limited.

(1) All companies are incorporated in England and Wales with the exception of Virgin Group Holdings Limited, which is incorporated in the British Virgin Islands.

**Charities**
The Group provides banking services to The Virgin Money Foundation ('the Foundation') which has resulted in customer deposits of £1m (2022: £1m). The Group has made donations of £1m in the year (2022: £1m) to the Foundation to enable it to pursue its charitable objectives. The Group has also provided a number of support services to the Foundation on a pro bono basis, including use of facilities and employee time. The estimated gift in kind for support services provided during the year was £0.5m (2022: £0.4m).

# Section 5: Other notes

## 5.3 Related party transactions continued

**Compensation of key management personnel (KMP)**
KMP comprises Directors of the Company and members of the Executive Leadership Team.

| | 2023 £m | 2022 £m |
|---|---|---|
| Salaries and short-term benefits | **9** | 9 |
| Equity based compensation[(1)] | **3** | 3 |
| | **12** | 12 |

(1) The expense recognised in the year is in accordance with IFRS 2 'Equity based compensations', including associated employers' NIC.

The following information regarding Directors' remuneration is presented in accordance with the Companies Act 2006.

| | 2023 £m | 2022 £m |
|---|---|---|
| Aggregate remuneration[(1)] | **5** | 5 |

(1) Aggregate remuneration includes amounts paid for the 2023 financial year and amounts paid under the LTIPs in relation to the 2018 and 2019 LTIP awards. LTIP figures in the single figure table for Executive Directors' 2023 remuneration in the Remuneration report contained in the Group's Annual Report and Accounts relate to the 2019 LTIP award in respect of the 2020–2022 LTIP performance period cycle.

None of the Directors were members of the Group's defined contribution or defined benefit pension schemes during 2023 (2022: none).

None of the Directors hold share options and none were exercised during the year (2022: none).

**Transactions with KMP**
KMP, their close family members, and any entities controlled or significantly influenced by the KMP have undertaken the following transactions with the Group in the normal course of business. The transactions were made on the same terms and conditions as applicable to other Group employees, or on normal commercial terms:

| | 2023 £m | 2022 £m |
|---|---|---|
| Loans and advances | **1** | 1 |
| Deposits | **1** | 1 |

No provisions have been recognised in respect of loans provided to KMP (2022: £Nil). There were no debts written off or forgiven during the year to 30 September 2023 (2022: £Nil). Included in the above are five (2022: five) loans totalling £0.6m (2022: £0.3m) made to Directors. In addition to the above, there are guarantees of £Nil (2022: £Nil) made to Directors and their related parties.

# Section 5: Other notes

## 5.4 Notes to the statement of cash flows

| | 2023 £m | 2023 £m |
|---|---|---|
| **Adjustments included in the profit before tax** | | |
| Interest receivable | **(3,833)** | (2,217) |
| Interest payable | **2,146** | 641 |
| Depreciation, amortisation and impairment (note 2.3) | **116** | 179 |
| Derivative financial instruments fair value movements | **12** | 17 |
| Impairment losses on credit exposures (note 3.1.1.1) | **309** | 52 |
| Net charge in respect of provisions for liabilities and charges | **31** | – |
| Equity based compensation (note 5.2) | **5** | 4 |
| Gain on disposal of FVOCI assets (note 2.2) | **(1)** | (4) |
| Other non-cash movements[1] | **8** | 2 |
| | **(1,207)** | (1,326) |
| **Changes in operating assets** | | |
| Net (increase)/decrease in: | | |
| Balances with supervisory central banks | **–** | (3) |
| Derivative financial instruments | **(269)** | 1,847 |
| Financial assets at FVTPL | **18** | 57 |
| Loans and advances to customers | **(303)** | (713) |
| Defined benefit pension assets | **(7)** | (7) |
| Other assets | **17** | 31 |
| | **(544)** | 1,212 |
| **Changes in operating liabilities** | | |
| Net increase/(decrease) in: | | |
| Due to other banks | **(627)** | 1,235 |
| Derivative financial instruments | **(37)** | 119 |
| Customer deposits | **1,249** | (1,510) |
| Provisions for liabilities and charges | **(14)** | (50) |
| Other liabilities | **(287)** | (32) |
| | **284** | (238) |

(1) Included within other non-cash movements is a net credit in respect of defined benefit pension schemes of £49m (2022: £24m) (note 2.3) and the share of post-tax losses of associates and joint ventures of £Nil (2022: £4m).

For the purposes of the statement of cash flows, cash and cash equivalents comprise the following balances with less than three months' maturity from the date of acquisition. This includes cash and liquid assets and amounts due from other banks (to the extent less than 90 days).

| | 2023 £m | 2022 £m |
|---|---|---|
| Cash and balances with central banks (less mandatory deposits) | **11,007** | 11,955 |
| Due from other banks (less than three months) | **666** | 656 |
| | **11,673** | 12,611 |

# Section 5: Other notes

### 5.5 Segment information

The Group's operating segments are operating units engaged in providing different products or services and whose operating results and overall performance are regularly reviewed by the Group's Chief Operating Decision Maker, the Executive Leadership Team.

The Group operates under four commercial lines: Mortgages, Unsecured, Business, and Deposits, which are reported through the Chief Commercial Officer. At this point in time, the business continues to be reported to the Group's Chief Operating Decision Maker as a single segment and decisions made on the performance of the Group on that basis. Segmental information will therefore continue to be presented on this single segment basis.

**Summary income statement**

| | 2023 £m | 2022 £m |
|---|---|---|
| Net interest income | **1,687** | 1,576 |
| Non-interest income | **140** | 140 |
| Total operating income | **1,827** | 1,716 |
| Operating and administrative expenses | **(1,173)** | (1,069) |
| Impairment losses on credit exposures | **(309)** | (52) |
| Segment profit before tax | **345** | 595 |
| | | |
| Average interest earning assets | **89,810** | 86,275 |

The Group has no operations outside the UK and therefore no secondary geographical area information is presented. The Group is not reliant on a single customer. Liabilities are managed on a centralised basis.

### 5.6 Post-balance sheet events

On 23 November 2023, the Company announced a further share buyback with an intent to repurchase another £150m in aggregate of shares and CDIs, ending no later than 16 May 2024.

# Measuring the Group’s performance

As highlighted within the Strategic report, Financial results, Directors’ remuneration report, and Risk report, all contained in the Group's Annual Report and Accounts, a range of metrics are considered that measure and track the Group’s performance. Some of these metrics will be the Group’s KPIs, which are a set of quantifiable measurements used to gauge the Group’s overall long-term performance. Others are not referred to as KPIs, but are still useful metrics for the Group to reflect on and are disclosed to aid comparisons with peers.

These metrics fall into two main categories:

- Financial – which are further split into:
  - IFRS based – meaning the basis of the calculation is derived from a measure that can be found and is directly required under generally accepted accounting principles (GAAP); and
  - Non-IFRS based – these are also referred to as APMs and can be derived from non-GAAP measures.
- Non-Financial – being those that are not directly linked to the Group’s financial performance, but more in relation to other external factors.

Non-IFRS based financial performance metrics can be calculated on either a statutory or an ‘underlying’ basis; further detail on how the underlying measure is arrived at, along with management’s reasoning for excluding the impact of certain items from the Group’s current underlying performance rationale, can be found on page 133, directly following this section.

## Financial performance metrics

**Profitability**:

<table>
<tr><th>Metric</th><th>KPI</th><th>LTIP</th><th>LTIP Year</th><th>Basis</th><th>Definition/formula</th><th>Why it matters</th></tr>
<tr><td>Gross annualised cost savings</td><td>Yes</td><td>No</td><td>N/a</td><td>Non-IFRS</td><td>Annualised gross cost savings benefits driven from the Group’s efficiency programmes.</td><td>It provides an annualised progress indicator for the Group’s accelerated digital strategy and stated target of delivering approximately £175m of additional cost savings by FY24, enabled by £275m of restructuring investment.</td></tr>
<tr><td>Statutory return on tangible equity (RoTE)</td><td>Yes</td><td>Yes</td><td>2023<br>2022<br>2021<br>2020<br>2019</td><td>Non-IFRS</td><td>Statutory profit after tax attributable to ordinary equity holders as a percentage of average tangible equity (average total equity less intangible assets and AT1) for a given year.
<table>
<tr><th></th><th>2023</th><th>2022</th><th>2021</th><th>2020</th></tr>
<tr><td>Statutory profit after tax attributable to ordinary equity holders (a)</td><td>£192m</td><td>£467m</td><td>£395m</td><td>£(220)m</td></tr>
<tr><td>Average tangible equity (b)</td><td>£4,971m</td><td>£4,539m</td><td>£3,875m</td><td>£3,554m</td></tr>
<tr><td>Statutory RoTE (a)/(b)</td><td>3.9%</td><td>10.3%</td><td>10.2%</td><td>(6.2)%</td></tr>
</table></td><td>It’s an indicator of the Group’s profitability and gives the return generated for shareholders as a percentage of the Group’s tangible equity.</td></tr>
<tr><td>Underlying cost: income ratio</td><td>Yes</td><td>Yes</td><td>2021<br>2020<br>2019</td><td>Non-IFRS</td><td>Underlying operating and administrative expenses as a percentage of underlying total operating income for a given year.
<table>
<tr><th></th><th>2023</th><th>Restated[1] 2022</th><th>Restated[1] 2021</th><th>Restated[1] 2020</th></tr>
<tr><td>Underlying operating and administrative expenses (a)</td><td>£971m</td><td>£914m</td><td>£902m</td><td>£917m</td></tr>
<tr><td>Underlying total operating income (b)</td><td>£1,873m</td><td>£1,742m</td><td>£1,564m</td><td>£1,558m</td></tr>
<tr><td>Underlying cost: income ratio (a)/(b)</td><td>51.9%</td><td>52.5%</td><td>57.7%</td><td>58.9%</td></tr>
</table></td><td>It’s a measure of efficiency in terms of how total operating expenses compare to total operating income on an underlying basis.</td></tr>
</table>

(1) Hedge ineffectiveness (2022: income of £13m, 2021: income of £8m, 2020: expense of £16m) is now presented as an adjustment to underlying earnings. The comparative periods have been adjusted accordingly. This restatement does not impact the statutory results of the Group.

**Financial performance metrics continued**
**Profitability continued:**

| Metric | KPI | LTIP | LTIP Year | Basis | Definition/formula | Why it matters |
|---|---|---|---|---|---|---|
| Net interest margin **(NIM)** | No | No | N/a | Non-IFRS | Underlying NII as a percentage of average interest earning assets (which is adjusted to exclude short-term repos used for liquidity management purposes) for a given year. | It's an indicator of the Group's profitability by showing the difference between how much the Group is earning in interest on its loans compared to how much it is paying out in interest on deposits. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Underlying NII (a) | **£1,716m** | £1,592m | £1,412m | £1,351m |
| Average interest earning assets (b) | **£89,810m** | £86,275m | £86,947m | £86,826m |
| Short-term repos used for liquidity management (c) | **£-m** | £12m | £16m | £16m |
| NIM (a)/((b)-(c)) | **1.91%** | 1.85% | 1.62% | 1.56% |

| Metric | KPI | LTIP | LTIP Year | Basis | Definition/formula | Why it matters |
|---|---|---|---|---|---|---|
| Statutory basic earnings per share **(EPS)** | No | No | N/a | IFRS | Statutory profit after tax attributable to ordinary equity shareholders, divided by the weighted average number of ordinary shares in issue for a given year (which includes deferred shares and excludes own shares held or contingently returnable shares). | It's an indicator of the Group's profitability on a statutory basis. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Statutory profit/(loss) after tax attributable to ordinary equity shareholders (a) | **£192m** | £467m | £395m | £(220)m |
| Weighted average number of ordinary shares in issue (b) | **1,375m** | 1,441m | 1,442m | 1,440m |
| Statutory basic earnings/(loss) per share (a)/(b) | **14.0p** | 32.4p | 27.3p | (15.3)p |

| Metric | KPI | LTIP | LTIP Year | Basis | Definition/formula | Why it matters |
|---|---|---|---|---|---|---|
| Statutory cost: income ratio | No | No | N/a | Non-IFRS | Statutory operating and administrative expenses as a percentage of statutory total operating income for a given year. | It's a measure of efficiency in terms of how total operating expenses compare to total operating income on a statutory basis. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Statutory operating and administrative expenses (a) | **£1,173m** | £1,069m | £1,203m | £1,104m |
| Statutory total operating income (b) | **£1,827m** | £1,716m | £1,489m | £1,443m |
| Statutory cost: income ratio (a)/(b) | **64.2%** | 62.3% | 80.8% | 76.5% |

| Metric | KPI | LTIP | LTIP Year | Basis | Definition/formula | Why it matters |
|---|---|---|---|---|---|---|
| Statutory return on assets | No | No | N/a | Non-IFRS | Statutory profit after tax as a percentage of average total assets for a given year. | It's an indicator of the Group's profitability on a statutory basis. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Statutory profit/(loss) after tax (a) | **£246m** | £537m | £474m | £(141)m |
| Average total assets (b) | **£92,188m** | £89,504m | £90,537m | £90,522m |
| Statutory return on assets (a)/(b) | **0.27%** | 0.60% | 0.52% | (0.16)% |

**Financial performance metrics continued**
**Profitability continued:**

| Metric | KPI | LTIP | LTIP Year | Basis | Definition/formula | Why it matters |
|---|---|---|---|---|---|---|
| Underlying basic EPS | No | No | N/a | Non-IFRS | Underlying profit after tax attributable to ordinary equity shareholders, divided by the weighted average number of ordinary shares in issue for a given year (which includes deferred shares and excludes own shares held or contingently returnable shares). | It's an indicator of the Group's profitability on an underlying basis. |

| | 2023 | Restated(1) 2022 | Restated(1) 2021 | Restated(1) 2020 |
|---|---|---|---|---|
| Underlying profit after tax attributable to ordinary equity shareholders (a) | **£376m** | £602m | £685m | £33m |
| Weighted average number of ordinary shares in issue (b) | **1,375m** | 1,441m | 1,442m | 1,440m |
| Underlying basic earnings per share (a)/(b) | **27.4p** | 41.8p | 47.5p | 2.3p |

| Metric | KPI | LTIP | LTIP Year | Basis | Definition/formula | Why it matters |
|---|---|---|---|---|---|---|
| Underlying profit before tax | No | No | N/a | Non-IFRS | Statutory profit before tax plus total underlying adjustments to the statutory view of performance. | It's an indicator of the Group's profitability on an underlying basis. |

| | 2023 | Restated(1) 2022 | Restated(1) 2021 | Restated(1) 2020 |
|---|---|---|---|---|
| Statutory profit/(loss) before tax (a) | **£345m** | £595m | £417m | £(168)m |
| Restructuring charges (b) | **£131m** | £82m | £146m | £139m |
| Acquisition accounting unwinds (c) | **£29m** | £35m | £88m | £113m |
| Legacy conduct (d) | **£12m** | £8m | £76m | £26m |
| Hedge ineffectiveness (e) | **£16m** | £(13)m | £(8)m | £16m |
| Other (f) | **£60m** | £69m | £74m | £14m |
| Underlying profit before tax (a) + (b) + (c) + (d) + (e) + (f) | **£593m** | £776m | £793m | £140m |

| Metric | KPI | LTIP | LTIP Year | Basis | Definition/formula | Why it matters |
|---|---|---|---|---|---|---|
| Underlying profit after tax attributable to ordinary equity shareholders | No | No | N/a | Non-IFRS | Underlying profit before tax less underlying tax charge, less AT1 distributions. The underlying tax charge (or credit) is the difference between the statutory tax charge (or credit) and the tax attributable to exceptional items. | It's an indicator of the Group's profitability on an underlying basis. |

| | 2023 | Restated(1) 2022 | Restated(1) 2021 | Restated(1) 2020 |
|---|---|---|---|---|
| Underlying profit before tax (a) | **£593m** | £776m | £793m | £140m |
| Underlying tax charge (b) | **£163m** | £104m | £29m | £28m |
| AT1 distributions (c) | **£54m** | £70m | £79m | £79m |
| Underlying profit after tax attributable to ordinary equity shareholders (a) - (b) - (c) | **£376m** | £602m | £685m | £33m |

(1) Hedge ineffectiveness (2022: income of £13m, 2021: income of £8m, 2020: expense of £16m) is now presented as an adjustment to underlying earnings. The comparative periods have been adjusted accordingly. This restatement does not impact the statutory results of the Group.

**Financial performance metrics continued**

**Profitability continued:**

| Metric | KPI | LTIP | LTIP Year | Basis | Definition/formula | Why it matters |
|---|---|---|---|---|---|---|
| Underlying RoTE | No | No | N/a | Non-IFRS | Underlying profit after tax attributable to ordinary equity holders as a percentage of average tangible equity (average total equity less intangible assets and AT1) for a given year. | It's an indicator of the Group's profitability on an underlying basis and gives the return generated for shareholders as a percentage of the Group's tangible equity. |

| | 2023 | Restated[1] 2022 | Restated[1] 2021 | Restated[1] 2020 |
|---|---|---|---|---|
| Underlying profit after tax attributable to ordinary equity holders (a) | **£376m** | £602m | £685m | £33m |
| Average tangible equity (b) | **£4,971m** | £4,539m | £3,875m | £3,554m |
| Underlying RoTE (a)/(b) | **7.6%** | 13.3% | 17.7% | 0.9% |

(1) Hedge ineffectiveness (2022: income of £13m, 2021: income of £8m, 2020: expense of £16m) is now presented as an adjustment to underlying earnings. The comparative periods have been adjusted accordingly. This restatement does not impact the statutory results of the Group.

**Financial performance metrics continued**

**Lending (Basis – non-IFRS):**

<table>
<tr><th>Metric</th><th>KPI</th><th>LTIP</th><th>LTIP Year</th><th>Definition and formula (where applicable)</th><th>Why it matters</th></tr>
<tr><td>Target lending segment asset growth</td><td>Yes</td><td>No</td><td>N/a</td><td>Target lending segment asset growth over the year. Target lending is defined as Unsecured and BAU Business lending (excluding Government lending schemes noting these are closed and in run off).
<table>
<tr><th></th><th>2023</th><th>2022</th><th>2021</th><th>2020</th></tr>
<tr><td>Total lending – current year (a)</td><td>£14,632m</td><td>£13,448m</td><td>£12,573m</td><td>£13,006m</td></tr>
<tr><td>Total lending – prior year (b)</td><td>£13,448m</td><td>£12,573m</td><td>£13,006m</td><td>£12,900m</td></tr>
<tr><td>Target lending growth ((a)-(b))/(b)</td><td>8.8%</td><td>7.0%</td><td>(3.3)%</td><td>0.8%</td></tr>
</table></td><td>It's an indicator of how well the Group is performing against its 'pioneering growth' strategic priority.</td></tr>
<tr><td>Relationship deposits growth</td><td>No</td><td>Yes</td><td>2021<br>2020</td><td>Relationship deposit growth over the year.
<table>
<tr><th></th><th>2023</th><th>2022</th><th>2021</th><th>2020</th></tr>
<tr><td>Total relationship deposits – current year (a)</td><td>£35,394m</td><td>£34,649m</td><td>£30,596m</td><td>£25,675m</td></tr>
<tr><td>Total relationship deposits – prior year (b)</td><td>£34,649m</td><td>£30,596m</td><td>£25,675m</td><td>£21,347m</td></tr>
<tr><td>Relationship deposit growth ((a)-(b))/(b)</td><td>2.2%</td><td>13.2%</td><td>19.2%</td><td>20.3%</td></tr>
</table></td><td>It's an indicator of how well the Group is performing against its 'pioneering growth' strategic priority.</td></tr>
</table>

**Financial performance metrics continued**

**Asset quality (Basis – non-IFRS):**

| Metric | KPI | LTIP | LTIP Year | Definition/formula | Why it matters |
|---|---|---|---|---|---|
| Impairment charge to average customer loans **(cost of risk)** | No | No | N/a | Impairment losses on credit exposures as a percentage of average customer loans (defined as loans and advances to customers, other financial assets at fair value and due from customers on acceptances). | It's an indicator of the asset quality of the Group's lending portfolio. |
| % of loans in Stage 2 | No | No | N/a | Stage 2 loans as a percentage of gross loans and advances. | It allows period-on-period comparison of Stage 2 loans as a percentage of overall gross loans and advances and therefore provides insight into the asset quality of the Group's lending portfolio over time. |
| % of loans in Stage 3 | No | No | N/a | Stage 3 loans as a percentage of gross loans and advances. | It allows period-on-period comparison of Stage 3 loans as a percentage of overall gross loans and advances and therefore provides insight into the asset quality of the Group's lending portfolio over time. |
| Total book coverage | No | No | N/a | Total impairment provisions on credit exposures as a percentage of total customer loans. | It provides a measure of the level of provision the Group holds for the total lending portfolio. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Impairment charge/(credit) (a) | **£309m** | £52m | £(131)m | £501m |
| Average customer loans (b) | **£72,770m** | £71,989m | £72,447m | £73,403m |
| Cost of risk (a)/(b) | **0.42%** | 0.07% | (0.18)% | 0.68% |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Stage 2 loans (a) | **£6,326m** | £5,736m | £10,178m | £12,844m |
| Gross loans and advances (b) | **£73,295m** | £73,146m | £72,551m | £72,925m |
| % of loans in stage 2 (a)/(b) | **8.6%** | 7.8% | 14.1% | 17.7% |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Stage 3 loans (a) | **£1,080m** | £1,038m | £957m | £862m |
| Gross loans and advances (b) | **£73,295m** | £73,146m | £72,551m | £72,925m |
| % of loans in Stage 3 (a)/(b) | **1.5%** | 1.4% | 1.3% | 1.2% |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Impairment provisions on credit exposures (a) | **£617m** | £457m | £504m | £735m |
| Gross loans and advances (b) | **£73,295m** | £73,146m | £72,551m | £72,925m |
| Total book coverage (a)/(b) | **0.84%** | 0.62% | 0.70% | 1.03% |

**Financial performance metrics continued**

**Asset quality (Basis – non-IFRS):**

| Metric | KPI | LTIP | LTIP Year | Definition/formula | Why it matters |
|---|---|---|---|---|---|
| Stage 2 coverage | No | No | N/a | Stage 2 impairment provisions as a percentage of Stage 2 gross loans and advances (excluding government backed loans). | It provides a measure of the level of provision the Group holds for the lifetime of the Stage 2 lending portfolio. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Stage 2 impairment provisions on credit exposures (a) | **£400m** | £268m | £302m | £465m |
| Stage 2 gross loans and advances (b) | **£6,305m** | £5,736m | £10,178m | £12,844m |
| Total stage 2 book coverage (a)/(b) | **6.33%** | 4.72% | 3.02% | 3.66% |

| Metric | KPI | LTIP | LTIP Year | Definition/formula | Why it matters |
|---|---|---|---|---|---|
| Stage 3 coverage | No | No | N/a | Stage 3 impairment provisions as a percentage of Stage 3 gross loans and advances (excluding government backed loans). | It provides a measure of the level of provision the Group holds for the lifetime of the Stage 3 lending portfolio. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Stage 3 impairment provisions on credit exposures (a) | **£128m** | £104m | £91m | £134m |
| Stage 3 gross loans and advances (b) | **£920m** | £1,038m | £957m | £862m |
| Total Stage 3 book coverage (a)/(b) | **13.93%** | 11.24% | 9.59% | 15.73% |

**Financial performance metrics continued**

**Capital (Basis – non-IFRS):**

| Metric | KPI | LTIP | LTIP Year | Definition/formula | Why it matters |
|---|---|---|---|---|---|
| Announced shareholder distributions | Yes | No | N/a | Dividends announced for the year plus buybacks as a percentage of statutory profit after tax attributable to ordinary shareholders. | It shows how much of our profits after tax and distributions we are paying out to our shareholders. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Interim dividend (a) | **£45m** | £36m | n/a | n/a |
| Final dividend (b) | **£27m** | £106m | £14m | n/a |
| Buybacks (c) | **£200m** | £125m | n/a | n/a |
| Statutory profit after tax attributable to ordinary equity holders (d) | **£192m** | £467m | £395m | £(220)m |
| Announced shareholder distributions ((a)+(b)+(c))/(d) | **142%** | 57% | 4% | n/a |

| Metric | KPI | LTIP | LTIP Year | Definition/formula | Why it matters |
|---|---|---|---|---|---|
| Common Equity Tier 1 **(CET1)** ratio (IFRS 9 transitional) | No | No | N/a | CET1 capital as a percentage of RWAs, on an IFRS 9 transitional basis. | It's an indicator of bank solvency that gauges the strength of the Group's CET1 capital relative to RWA. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| CET1 capital (IFRS 9 transitional) (a) | **£3,711m** | £3,633m | £3,616m | £3,271m |
| RWA (IFRS 9 transitional) (b) | **£25,176m** | £24,148m | £24,232m | £24,399m |
| CET1 ratio (IFRS 9 transitional) (a)/(b) | **14.7%** | 15.0% | 14.9% | 13.4% |

| Metric | KPI | LTIP | LTIP Year | Definition/formula | Why it matters |
|---|---|---|---|---|---|
| CET1 ratio (IFRS 9 fully loaded) | No | No | N/a | CET1 capital as a percentage of RWAs, on an IFRS 9 fully loaded basis. | It's an indicator of bank solvency that gauges the strength of the Group's CET1 capital without adjusting for temporary IFRS 9 relief. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| CET1 capital (IFRS 9 fully loaded) (a) | **£3,599m** | £3,519m | £3,482m | £2,961m |
| RWA (IFRS 9 fully loaded) (b) | **£25,087m** | £24,056m | £24,156m | £24,246m |
| CET1 ratio (IFRS 9 fully loaded) (a)/(b) | **14.3%** | 14.6% | 14.4% | 12.2% |

| Metric | KPI | LTIP | LTIP Year | Definition/formula | Why it matters |
|---|---|---|---|---|---|
| Tier 1 ratio | No | No | N/a | Tier 1 capital as a percentage of RWAs. | It's an indicator of bank solvency that gauges the strength of the Group's Tier 1 capital relative to RWA. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Tier 1 capital (a) | **£4,305m** | £4,299m | £4,313m | £4,186m |
| RWA (b) | **£25,176m** | £24,148m | £24,232m | £24,399m |
| Tier 1 ratio (a)/(b) | **17.1%** | 17.8% | 17.8% | 17.2% |

**Financial performance metrics continued**
**Capital (Basis – non-IFRS):**

| Metric | KPI | LTIP | LTIP Year | Definition/formula | Why it matters |
|---|---|---|---|---|---|
| Total capital ratio | No | No | N/a | Total capital resources as a percentage of RWAs. | It's an indicator of bank solvency that gauges the strength of the Group's total capital relative to RWA. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Total capital (a) | **£5,327m** | £5,319m | £5,332m | £4,935m |
| RWA (b) | **£25,176m** | £24,148m | £24,232m | £24,399m |
| Total capital ratio (a)/(b) | **21.2%** | 22.0% | 22.0% | 20.2% |

| Metric | KPI | LTIP | LTIP Year | Definition/formula | Why it matters |
|---|---|---|---|---|---|
| Tangible net asset value **(TNAV)** per share | No | No | N/a | Tangible equity (total equity less intangible assets and AT1) divided by the number of ordinary shares in issue at the year end (which includes deferred shares and excludes own shares held). | It represents the value per share of the Group based on the Group's tangible net assets and can be used as a comparison against the current market share price. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Tangible equity (a) | **£4,840m** | £5,407m | £4,185m | £3,526m |
| Number of ordinary shares in issue (b) | **1,345m** | 1,409m | 1,440m | 1,439m |
| Deferred shares (c) | **2m** | 3m | 5m | 6m |
| Own shares held (d) | **1.3m** | 0.3m | 0.1m | 0.2m |
| Tangible net asset value per share (a)/((b)+(c)-(d)) | **359.8p** | 383.0p | 289.8p | 244.2p |

| Metric | KPI | LTIP | LTIP Year | Definition/formula | Why it matters |
|---|---|---|---|---|---|
| Total shareholder return **(TSR)** | No | Yes | 2023<br>2022 | Share price at the end of the financial period, less the share price at the start of the financial period including dividends received over the period, divided by the share price at the start of the financial period. | The use of total shareholder return enables us to target a measure that is directly linked to an investor's total return on a share, incorporating both share price movement and dividends paid. |

| | 2023 | 2022 | 2021 | 2020 |
|---|---|---|---|---|
| Share price at the end of the financial period (a) | **168.4p** | 124.3p | 204.4p | 73.0p |
| Share price at the start of the financial period (b) | **124.3p** | 204.4p | 73.0p | 114.9p |
| Dividends (assuming reinvestment) (c) | **12.6p** | 3.2p | n/a | n/a |
| Total shareholder return ((a)-(b)+(c))/(b) | **45.5%** | (37.6)% | 180.1% | (36.5)% |

# Measuring the Group's performance

**Non-financial performance metrics:**

| Metric | KPI | LTIP | LTIP Year | Definition/formula (where applicable) | Why it matters |
|---|---|---|---|---|---|
| Colleague engagement | Yes | No | N/a | Outcomes from the colleague engagement survey preceding the end of the financial year | Measures our understanding of employee sentiment noting our Purpose of Making you happier about money extends to our colleagues and ensures our customers will be supported by delighted colleagues working in a healthy, flexible, digitally-led environment. |
| Customer complaints per 1,000 accounts | Yes | No | N/a | In line with FCA regulations, number of complaints per thousand accounts calculated as:<br><br>$\frac{\text{Total number of complaints received in six-month period to reporting date}}{\text{Total number of accounts as at reporting date}} \times 1{,}000$<br><br>Currently excludes complaints relating to Insurance and Pure Protection FCA reporting group given historically skewed influence of legacy payment protection insurance. | Provides a measure to benchmark against peers and drives accountability within the Group to improve customer service and ensure we are making our customers happier about money. |
| Digital primacy | Yes | No | N/a | It measures the proportion of active PCA and Card customers who are digital-only in their engagement with Virgin Money. To qualify, each customer must:<br><br>1. be digitally adopted and active (successfully logged in to the mobile app in the past 90 days);<br><br>2. be signed up to our paperless proposition;<br><br>3. have not transacted in stores within the last 90 days; and<br><br>4. have not completed an authenticated call with contact centres in the past 90 days. | Measures the level of digitisation across our customer journeys while demonstrating the realisation of our ambition 'to be the UK's best digital bank'. |
| Group diversity indicators | Yes | Yes | 2023 | Percentage of colleagues who identify as female within our 0-3 leadership population and percentage of colleagues from under-represented cultural heritage backgrounds within our 0-3 leadership population and overall Virgin Money colleague base. | Having a diverse and representative workforce at all levels of our organisation enables us to better reflect, understand and support our customers. It also creates the conditions for rapid innovation, balanced perspective on risk and improved problem solving organisationally |
| Group Smile score | Yes | No | N/a | % of interactions scored as a 'Smile'. A 'Smile' is determined by our customers and only counted as a 'Smile' if they score the following three aspects at the highest ranking:<br><br>• Whether the customer got what they wanted on an interaction.<br>• How easy the interaction was.<br>• How the interaction made them feel. | It's a score that is used to supplement NPS, however we use the Smile scores as our key customer experience metric given its ability to capture the role of emotion in customer advocacy. |
| Total active relationship customer accounts | Yes | No | N/a | Active PCA, BCA and Card customer accounts where active is defined as > £0 balance for Cards; transaction in the last 12 months for PCA and BCA customer accounts. | It's an indicator of how well the Group is performing against its 'pioneering growth' strategic priority. |

# Measuring the Group's performance

**Non-financial performance metrics:**

| Metric | KPI | LTIP | LTIP Year | Definition/formula (where applicable) | Why it matters |
|---|---|---|---|---|---|
| ESG scorecard | No | Yes | 2023<br>2022 | Demonstrating progress against the Group's short, medium and long-term targets for:<br>1. senior colleague gender representation(1);<br>2. senior colleague ethnic minority representation(1);<br>3. Group-wide ethnic minority representation(1);<br>4. carbon emissions, Scope 1 and 2;<br>5. net zero plan delivery (financed emissions reduction); and<br>6. colleague engagement.<br>(1) As a percentage of the population declared. | Our ESG scorecard tracks our progress in creating a sustainable future and the inclusion of an ESG scorecard within our LTIP ensures that Executive Director remuneration is aligned with the Group's aspiration to drive positive social and environmental impact through everything we do. |
| Risk scorecard | No | Yes | 2023<br>2022 | Demonstrating progress against the Group's targets for customer complaints, operational risk losses, cost of risk, Group risk profile and Group risk appetite. | Our Risk scorecard demonstrates our commitment to, and monitoring of, prudent risk management within the business, and its inclusion within our LTIP ensures Executive Director remuneration is aligned with the Group's aspirations to deliver exceptional customer experience and ensure operations and processes drive resilience and positive customer outcomes. |

# Underlying adjustments to the statutory view of performance

Management exclude certain items from the Group's statutory position to arrive at an underlying performance basis. Management's approach to underlying adjustments is aligned to the European Securities and Markets Authority (ESMA) guidelines on APMs and recommendations are subject to review and agreement by the Board Audit Committee. Additional detail on these items is provided below to help understand their exclusion from underlying performance.

| Item | 2023 £m | Restated 2022 £m | Reason for exclusion from the Group's current underlying performance |
|---|---|---|---|
| **Restructuring charges** | **(131)** | (82) | These costs relate to the Group's Digital-First strategy. The Group expects to incur c.£275m of restructuring charges across FY22-24. |
| **Acquisition accounting unwinds** | **(29)** | (35) | This consists of the unwind of the IFRS 3 fair value adjustments created on the acquisition of Virgin Money Holdings (UK) PLC in October 2018. These represent either one-off adjustments or are the scheduled reversals of the accounting adjustments that arose following the fair value exercise required by IFRS 3. These will continue to be underlying adjustments until the remaining amounts have been fully reversed. |
| **Legacy conduct** | **(12)** | (8) | These costs are historical in nature and are not indicative of the Group's current practices. |
| **Hedge ineffectiveness**[(1)] | **(16)** | 13 | The result of hedge accounting and fair value movements on derivatives in economic hedges to the extent they either do not meet the criteria for hedge accounting or give rise to hedge ineffectiveness. These items are often volatile, driven by accounting requirements and not generally considered as a component of the core financial result. |
| **Other:** | | | |
| UTM transition costs | **(2)** | (9) | These costs relate to UTM's transformation costs, principally for the build of a new platform for administration and servicing. |
| VISA shares | **1** | 2 | A one-off gain on conversion of Visa B Preference shares to Series A preference shares. |
| Internally developed software adjustments | **(47)** | (62) | These costs relate to the write-off of WIP and intangible asset balances held on the balance sheet as a result of a reassessment of the Group's practices on capitalisation against the backdrop of the move to an Agile project delivery in FY22, and in FY23 the write-off charge is in relation to the Group's mortgage digitisation programme. Following an assessment of the progress of the project to upgrade the mortgage platform and challenges identified during testing, we now anticipate a significant deferral and redesign as we implement the upgraded capability. |
| Property, plant and equipment, and investment property adjustments | **(12)** | – | £6m of these costs relate to a data cleanse exercise conducted on the Group's fixed asset registers ahead of a migration to a single fixed asset register in FY24 and a £6m reduction in the valuation of an investment property due to changes in market conditions. |
| **Total other** | **(60)** | (69) | |
| **Total underlying adjustments** | **(248)** | (181) | |

(1) Hedge ineffectiveness is now presented as an adjustment to underlying earnings due to the increase in volatility caused by the recent significant changes in interest rates. The comparative period has been adjusted accordingly.

# Glossary

| Term | Definition |
|---|---|
| Additional Tier 1 (AT1) | Securities that are considered AT1 capital in the context of CRD IV. |
| Agile | Agile working is about bringing people, processes, connectivity and technology, time and place together to find the most appropriate and effective way of working. |
| arrears | A customer is in arrears (or in a state of delinquency) when they fail to adhere to their contractual payment obligations resulting in an outstanding loan that is unpaid or overdue. When a customer is in arrears, the total outstanding loans on which payments are overdue are said to be delinquent. |
| average assets | Represents the average of assets over the year adjusted for any disposed operations. |
| Bank | Clydesdale Bank PLC. |
| Basel II | The capital adequacy framework issued by the Basel Committee on Banking Supervision (BCBS) in June 2004. |
| Basel III | Reforms issued by the BCBS in December 2017 with subsequent revisions. |
| Basel 3.1 | An updated version of the Basel III reforms of the regulatory framework issued by the BCBS in December 2017. These are being implemented in the UK by the PRA from 1 July 2025. |
| basis points **(bps)** | One hundredth of a percent (0.01%); meaning that 100 basis points is equal to 1%. This term is commonly used in describing interest rate movements. |
| BAU Business lending | Business lending excluding government lending scheme balances. |
| Board | Refers to the Virgin Money UK PLC Board or the Clydesdale Bank PLC Board as appropriate. |
| Bounce back loan scheme | A scheme implemented by the UK Government to provide financial support to businesses across the UK that were losing revenue, and seeing their cash flow disrupted as a result of COVID-19, enabling them to benefit from £50,000 or less in finance. |
| Business lending | Lending to non-retail customers, including overdrafts, asset and lease financing, term lending, bill acceptances, foreign currency loans, international and trade finance, securitisation and specialised finance. |
| carbon related assets | Assets tied to the energy and utilities sectors under the Global Industry Classification Standard (mapped to internal industry classifications), excluding water utilities and independent power and renewable electricity producer industries. |
| carrying value (also referred to as carrying amount) | The value of an asset or a liability in the balance sheet based on either amortised cost or fair value principles. |
| cash and cash equivalents | For the purposes of the statement of cash flows, cash and cash equivalents comprise cash and non-mandatory deposits with central banks and amounts due from other banks with a maturity of less than three months. |
| Code | The 2018 UK Corporate Governance Code. |
| collateral | The assets of a borrower that are used as security against a loan facility. |
| Common Equity Tier 1 capital **(CET1)** | The highest quality form of regulatory capital that comprises total shareholders' equity, less goodwill and intangible assets and certain other regulatory adjustments. |
| Company | Virgin Money UK PLC. |
| Coronavirus business interruption loan scheme | A scheme implemented by the UK Government to provide financial support to smaller businesses across the UK that were losing revenue, and seeing their cash flow disrupted, as a result of COVID-19. |
| Coronavirus large business interruption loan scheme | A scheme implemented by the UK Government to provide financial support to mid-sized and larger businesses across the UK that were suffering disruption to their cash flow due to lost or deferred revenues as a result of COVID-19. |
| counterparty | The other party that participates in a financial transaction, with every transaction requiring a counterparty in order for the transaction to complete. |
| Coverage ratio | Impairment allowance as at the year end shown as a percentage of gross loans and advances as at the year end. |
| covered bonds | A corporate bond with primary recourse to the institution and secondary recourse to a pool of assets that act as security for the bonds on issuer default. Covered bonds remain on the issuer's balance sheet and are a source of term funding for the Group. |
| CRD IV | Capital Requirements Directive (EU) 2013/36 revised by Directive (EU) 2019/878, as implemented in the UK by PRA Policy Statement 22/21 and incorporated into the PRA Rulebook from 1 January 2022. |
| credit conversion factor **(CCF)** | CCFs are used in determining the EAD in relation to a credit risk exposure. The CCF is an estimate of the proportion of undrawn and off-balance sheet commitments expected to be drawn down at the point of default. |
| Credit impaired financial asset | A financial asset that is in default or has an individually assessed provision. This is also referred to as a 'Stage 3' impairment loss and subject to a lifetime ECL calculation. The Group considers 90 DPD as a backstop in determining whether a financial asset is credit impaired. |
| Credit risk mitigation | Techniques to reduce the potential loss in the event that a customer (borrower or counterparty) becomes unable to meet its obligations. This may include the taking of financial or physical security, the assignment of receivables or the use of credit derivatives, guarantees, credit insurance, set-off or netting. |
| CRR | Capital Requirements Regulation (EU) 575/2013 revised by Regulation (EU) 2019/876, as implemented in the UK by PRA Policy Statement 22/21 and incorporated into the PRA Rulebook from 1 January 2022 |
| customer deposits | Money deposited by individuals or corporate entities that are not credit institutions, and can be either interest bearing, non-interest bearing or term deposits. |
| days past due **(DPD)** | The number of days a facility has borrowing in excess of an agreed or expired limit or, where facilities are subject to a regular repayment schedule, contractual payments are not fully up to date. |

# Glossary

| Term | Definition |
|---|---|
| default | A customer is in default when either they are more than 90 DPD on a credit obligation to the Group, or are considered unlikely to pay their credit obligations in full without recourse to actions such as realisation of security (if held). |
| delinquency | See 'arrears'. |
| Demerger | The demerger of the Group from NAB which took effect on 8 February 2016 pursuant to which all of the issued share capital of CYB Investments Limited was transferred to the Company (formerly CYBG PLC) by NAB in consideration for the issue and transfer of the Company (formerly CYBG PLC) shares to NAB in part for the benefit of NAB (which NAB subsequently sold pursuant to the Company's IPO) and in part for the benefit of NAB shareholders under a scheme of arrangement under part 5.1 of the Australian Corporations Act. |
| derivative | A financial instrument that is a contract or agreement whose value is related to the value of an underlying instrument, reference rate or index. |
| effective interest rate **(EIR)** | The rate used to calculate interest income or expense under the effective interest method. |
| emissions intensity | Emission rate of a given pollutant per unit of economic output or activity. |
| encumbered assets | Assets that have been pledged as security, collateral or legally 'ring-fenced' in some other way which prevents those assets being transferred, pledged, sold or otherwise disposed. |
| exposure | A claim, contingent claim or position which carries a risk of financial loss. |
| exposure at default **(EAD)** | The estimate of the amount that the customer will owe at the time of default. |
| fair value | The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions. |
| Flood Re | A joint initiative between the UK Government and home insurers to provide widely available and affordable insurance for homes in high-risk flood areas. |
| forbearance | The term generally applied to the facilities provided or changes to facilities provided to assist borrowers, who are experiencing, or are about to experience, a period of financial stress. |
| full time equivalent **(FTE)** | The standardised method of measurement that represents the number of hours worked by all Virgin Money employees, both full time and part time (excluding contractors or long-term absences). |
| Group | Virgin Money UK PLC and its controlled entities. |
| hedge ineffectiveness | Represents the extent to which the income statement is impacted by changes in fair value or cash flows of hedging instruments not being fully offset by changes in fair value or cash flows of hedged items. |
| IFRS 9 | The financial instrument accounting standard which was adopted by the Group with effect from 1 October 2018. |
| IFRS 9 transitional adjustments – dynamic | That part of the transitional adjustments on regulatory capital arising from the increase in impairment provisions (on non-credit impaired exposures) from the date of initial adoption of IFRS 9 to the reporting date. |
| IFRS 9 transitional adjustments – static | That part of the transitional adjustments on regulatory capital arising from the increase in impairment provisions on initial adoption of IFRS 9 from those calculated under IAS 39. |
| impairment allowances | An ECL provision held on the balance sheet for financial assets calculated in accordance with IFRS 9. The impairment allowance is calculated as either a 12-month or a lifetime ECL. |
| impairment losses | The ECL calculated in accordance with IFRS 9 and recognised in the income statement with the carrying value of the financial asset reduced by creating an impairment allowance. Impairment losses are calculated as either a 12-month or lifetime ECL. |
| Internal Capital Adequacy Assessment Process **(ICAAP)** | The Group's assessment of the levels of capital that it needs to hold through an examination of its risk profile from regulatory and economic capital viewpoints. |
| Internal Liquidity Adequacy Assessment Process **(ILAAP)** | The Group's assessment and management of balance sheet risks relating to funding and liquidity. |
| Internal Ratings-Based approach **(IRB)** | A method of calculating credit risk capital requirements using internal, rather than supervisory, estimates of risk parameters. |
| investment grade | The highest possible range of credit ratings, from 'AAA' to 'BBB', as measured by external credit rating agencies. |
| Level 1 fair value measurements | Financial instruments whose fair value is derived from unadjusted quoted prices for identical instruments in active markets. |
| Level 2 fair value measurements | Financial instruments whose fair value is derived from quoted prices for similar instruments in active markets and financial instruments valued using models where all significant inputs are observable. |
| Level 3 fair value measurements | Financial instruments whose fair value is derived from valuation techniques where one or more significant inputs are unobservable. |
| lifetime ECL | The ECL calculation performed on financial assets where a SICR since origination has been identified. This can be either a 'Stage 2' or 'Stage 3' impairment loss depending on whether the financial asset is credit impaired. |
| Listing Rules | Regulations applicable to any company listed on a UK stock exchange, subject to the oversight of the UK Listing Authority (UKLA). The Listing Rules set out mandatory standards for any company wishing to list its shares or securities for sale to the public. |
| loan to value ratio **(LTV)** | A ratio that expresses the amount of a loan as a percentage of the value of the property on which it is secured. |
| location-based emissions | Calculated using the average emissions intensity of the grids on which energy consumption occurs, using mostly grid-average emission factor data. |
| loss-absorbing capacity **(LAC)** requirement | The required level of MREL resources that the Group is required to hold to meet its MREL requirement and applicable capital buffers set by the BoE. |

# Glossary

| Term | Definition |
|---|---|
| loss given default **(LGD)** | The estimate of the loss that the Group will suffer if the customer defaults (incorporating the effect of any collateral held). |
| Low-carbon economy | An economy based on energy sources that produce low levels of greenhouse gas emissions. |
| market-based emissions | Calculated as the electricity that companies have purposefully chosen to purchase. It derives emission factors from contractual instruments, which include any type of contract between two parties for the sale and purchase of energy bundled with attributes about the energy generation, or for unbundled attribute claims. |
| medium-term notes | Debt instruments issued by corporates, including financial institutions, across a range of maturities. |
| Minimum Requirement for Own Funds and Eligible Liabilities **(MREL)** | A minimum requirement for institutions to maintain equity and eligible debt liabilities, to help ensure that if an institution fails the resolution authority can use these financial resources to absorb losses and recapitalise the continuing business. |
| National Databank | The National Databank provides free mobile data, texts and calls to people in need via Good Things Foundation's network of local community partners. |
| net interest income **(NII)** | The amount of interest received or receivable on assets, net of interest paid or payable on liabilities. |
| Net Promoter Score **(NPS)** | This is an externally collated customer loyalty metric that measures loyalty between a provider, who in this context is the Group, and a consumer. |
| Net zero | Negating the amount of greenhouse gases produced by human activity. |
| Paris Climate Agreement | Legally binding international treaty to limit global warming to below 2 degrees Celsius, and preferably to 1.5 degrees Celsius above pre-industrial levels. |
| Personal lending | Lending to individuals rather than institutions excluding mortgage lending which is reported separately. |
| probability of default **(PD)** | The probability that a customer will default over either the next 12 months or lifetime of the account. |
| Recovery loan scheme **(RLS)** | A scheme implemented by the UK Government to provide financial support to small and medium-sized businesses across the UK to promote growth and investment following the disruption caused by COVID-19. |
| regulatory capital | The capital which the Group holds, determined in accordance with rules established by the PRA. |
| relationship deposits | Current account and linked savings balances. |
| residential mortgage-backed securities **(RMBS)** | Securities that represent interests in groups or pools of underlying mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and principal). |
| ring-fencing | A regime of rules which require banks to change the way that they are structured by separating retail banking services from investment and international banking. This is to ensure the economy and taxpayers are protected in the event of any future financial crises. |
| risk appetite | The level and types of risk the Group is willing to assume within the boundaries of its risk capacity to achieve its strategic objectives. |
| risk-weighted asset **(RWA)** | On and off-balance sheet assets of the Group are allocated a risk weighting based on the amount of capital required to support the asset. |
| sale and repurchase agreement **(repo)** | A short-term funding agreement that allows a borrower to create a collateralised loan by selling a financial asset to a lender. As part of the agreement, the borrower commits to repurchase the security at a date in the future repaying the proceeds of the loan. For the counterparty (buying the security and agreeing to sell in the future) it is a reverse repurchase agreement or a reverse repo. |
| Scheme | The Group's defined benefit pension scheme, the Yorkshire and Clydesdale Bank Pension Scheme. |
| Science based targets | Science based targets provide a clearly defined pathway for companies and financial institutions to reduce GHG emissions, helping prevent the worst impacts of climate change and future-proof business growth.<br>Targets are considered 'science based' if they are in line with what the latest climate science deems necessary to meet the goals of the Paris Agreement – limiting global warming to 1.5°C above pre-industrial levels. |
| Scope 1/2/3 emissions | Scope 1, 2, and 3 emissions are a way of categorising business emissions, accounting for both direct and indirect emitted GHGs. Scope 1 emissions are GHGs released directly from a business. Scope 2 emissions are indirect GHGs released from the energy purchased by an organisation. Scope 3 emissions are also indirect GHG emissions, accounting for upstream and downstream emissions of a product or service, and emissions across a business's value chain. |
| secured lending | Lending in which the borrower pledges some asset (e.g. property) as collateral for the lending. |
| securitisation | The practice of pooling similar types of contractual debt and packaging the cash flows from the financial asset into securities that can be sold to institutional investors in debt capital markets. It provides the Group with a source of secured funding that can achieve a reduction in funding costs by offering typically 'AAA' rated securities secured by the underlying financial asset. |
| Segment | Generally refers to customer, product or commercial lines unless used within the financial statements where the results are disclosed on a single segment basis in line with that reported to the Group's Chief Operating Decision Maker. |
| significant increase in credit risk **(SICR)** | The assessment performed on financial assets at the reporting date to determine whether a 12-month or lifetime ECL calculation is required. Qualitative and quantitative triggers are assessed in determining whether there has been a SICR since origination. The Group considers 30 DPD as a backstop in determining whether a SICR since origination has occurred. |
| standardised approach | In relation to credit risk, a method for calculating credit risk capital requirements using External Credit Assessment Institutions ratings and supervisory risk weights. In relation to operational risk, a method of calculating the operational capital requirement by the application of a supervisory defined percentage charge to the gross income of eight specified business lines. |
| stress testing | The term used to describe techniques where plausible events are considered as vulnerabilities to ascertain how this will impact the own funds or liquidity which a bank holds. |

# Glossary

| Term | Definition |
|---|---|
| structured entity | An entity created to accomplish a narrow well-defined objective (e.g. securitisation of financial assets). An SE may take the form of a corporation, trust, partnership or unincorporated entity. SEs are often created with legal arrangements that impose strict limits on the activities of the SE. May also be referred to as an SPV. |
| subordinated debt | Liabilities which rank after the claims of other creditors of the issuer in the event of insolvency or liquidation. |
| Term Funding Scheme **(TFS)** | A scheme launched in 2016 by the BoE to allow banks and building societies to borrow from the BoE at rates close to base rate. This is designed to increase lending to businesses by lowering interest rates and increasing access to credit. |
| Tier 1 capital | A measure of a bank's financial strength defined by CRD IV. It captures CET1 capital plus other Tier 1 securities (as defined by CRD IV) in issue, subject to deductions. |
| Tier 2 capital | A component of regulatory capital, including qualifying subordinated debt, eligible collective impairment allowances and other Tier 2 securities as defined by CRD IV. |
| unsecured lending | Lending in which the borrower pledges no assets as collateral for the lending (such as credit cards and current account overdrafts). |
| value at risk **(VaR)** | A measure of the loss that could occur on risk positions as a result of adverse movements in market risk factors (e.g. rates, prices, volatilities) over a specified time horizon and to a given level of confidence. |

# Abbreviations

| | |
|---|---|
| **ACS** | Annual cyclical scenario |
| **AFD** | Approaching financial difficulty |
| **AGM** | Annual General Meeting |
| **AI** | Artificial intelligence |
| **ALCO** | Asset and Liability Committee |
| **ALMV** | A Life More Virgin |
| **APM** | Alternative Performance Measure |
| **ASX** | Australian Securities Exchange |
| **AT1** | Additional Tier 1 |
| **ATM** | Automated teller machine |
| **AUM** | Assets under management |
| **BAU** | Business as usual |
| **BCA** | Business current account |
| **BCBS** | Basel Committee on Banking Supervision |
| **BoE** | Bank of England |
| **bps** | Basis points |
| **BTL** | Buy-to-let |
| **CBES** | Climate Biennial Exploratory Scenario |
| **CBI** | Confederation of British Industry |
| **CCC** | Climate Change Committee |
| **CCF** | Credit conversion factor |
| **CCyB** | Countercyclical Capital Buffer |
| **CDI** | CHESS Depositary Interest |
| **CDP** | Carbon Disclosure Project |
| **CER** | Certified Emissions Reduction |
| **CET1** | Common Equity Tier 1 Capital |
| **CIPD** | Chartered Institute of Personnel and Development |
| **CMA** | Competition and Markets Authority |
| **CPI** | Consumer Price Index |
| **CRD** | Capital Requirements Directive |
| **CRE** | Commercial Real Estate |
| **CRR** | Capital Requirements Regulation |
| **CSRBB** | Credit spread risk in the banking book |
| **CYBI** | CYB Investments Limited |
| **DE&I** | Diversity, equity and inclusion |
| **DEP** | Deferred Equity Plan |
| **DPD** | Days past due |
| **DTR** | Disclosure Guidance and Transparency Rules |
| **EAD** | Exposure at default |
| **EBA** | European Banking Authority |
| **EBT** | Employee benefit trust |
| **ECL** | Expected credit loss |
| **EIR** | Effective interest rate |
| **EPC** | Energy performance certificate |
| **EPS** | Earnings per share |
| **ESG** | Environmental, social and governance |
| **EY** | Ernst & Young LLP |
| **FCA** | Financial Conduct Authority |
| **FIRB** | Foundation internal ratings-based |
| **FPC** | Financial Policy Committee |
| **FRC** | Financial Reporting Council |
| **FTE** | Full time equivalent |
| **FVOCI** | Fair value through other comprehensive income |
| **FVTPL** | Fair value through profit or loss |
| **GAAP** | Generally Accepted Accounting Principles |
| **GDIA** | Group Director Internal Audit |
| **GDP** | Gross Domestic Product |
| **GDPR** | General Data Protection Regulation |
| **GFC** | Global financial crisis |
| **GHFA** | Green Homes Finance Accelerator |
| **GHG** | Greenhouse gases |
| **G-SII** | Global Systemically Important Institution |
| **HaRi** | Human resources meets artificial intelligence |
| **HMRC** | His Majesty's Revenue and Customs |
| **HPI** | House Price Index |
| **HQLA** | High Quality Liquid Asset |
| **IAS** | International Accounting Standard |
| **IASB** | International Accounting Standards Board |
| **IBOR** | Interbank Offered Rate |
| **ICAAP** | Internal Capital Adequacy Assessment Process |
| **IFRS** | International Financial Reporting Standard |
| **ILAAP** | Internal Liquidity Adequacy Assessment Process |
| **IPO** | Initial Public Offering |
| **IRB** | Internal ratings-based |
| **IRRBB** | Interest rate risk in the banking book |
| **ISA** | International Standards on Auditing |
| **ISAE** | International Standard on Assurance Engagements |
| **ISDA** | International Swaps and Derivatives Association |
| **ISSB** | International Sustainability Standards Board |
| **JV** | Joint venture |
| **KMP** | Key management personnel |
| **KPI** | Key Performance Indicator |
| **LAC** | Loss-absorbing capacity |
| **LCR** | Liquidity coverage ratio |
| **LDR** | Loan to deposit ratio |
| **LGBTQ+** | Lesbian, gay, bisexual, transgender, queer (or questioning) plus |
| **LGD** | Loss Given Default |
| **LIBOR** | London Interbank Offered Rate |
| **LSE** | London Stock Exchange |
| **LTIP** | Long-term incentive plan |
| **LTV** | Loan to value |
| **MGC** | Model Governance Committee |
| **MREL** | Minimum Requirement for Own Funds and Eligible Liabilities |

# Abbreviations

| | |
|---|---|
| **MRT** | Material Risk Takers |
| **NAB** | National Australia Bank Limited |
| **NII** | Net interest income |
| **NIM** | Net interest margin |
| **NPS** | Net promoter score |
| **NSFR** | Net stable funding ratio |
| **NZBA** | Net-Zero Banking Alliance |
| **O-SII** | Other Systemically Important Institution |
| **PBT** | Profit before tax |
| **PCA** | Personal current accounts |
| **PCAF** | Partnership for Carbon Accounting Financials |
| **PD** | Probability of Default |
| **PIE** | Pension Increase Exchange |
| **POCI** | Purchased or originated credit impaired |
| **PRA** | Prudential Regulation Authority |
| **RACE** | Risk Analytics Centre of Excellence |
| **RAF** | Risk Appetite Framework |
| **RAS** | Risk Appetite Statement |
| **RLS** | Recovery Loan Scheme |
| **RMBS** | Residential mortgage-backed securities |
| **RMF** | Risk Management Framework |
| **RoTE** | Return on Tangible Equity |
| **RPI** | Retail Price Index |
| **RWA** | Risk-weighted asset |
| **SASB** | Sustainability Accounting Standards Board |
| **SBC** | Sustainable Business Coach |
| **SBTi** | Science-based targets initiative |
| **SDG** | Sustainable Development Goal |
| **SICR** | Significant increase in credit risk |
| **SIP** | Statement of Investment Principles |
| **SMCR** | Senior Managers and Certification Regime |
| **SME** | Small or medium-sized enterprise |
| **SMF** | Sterling Monetary Framework |
| **SONIA** | Sterling Overnight Index Average |
| **SST** | Solvency Stress Test |
| **STIP** | Short-term Incentive Plan |
| **TCFD** | Task Force on Climate-related Financial Disclosures |
| **TFS** | Term Funding Scheme |
| **TFSME** | Term Funding Scheme with additional incentives for SMEs |
| **TNAV** | Tangible net asset value |
| **TNFD** | Taskforce on Nature-related Financial Disclosures |
| **TPT** | Transition Plan Taskforce |
| **UK SDS** | Sustainability Disclosure Standards |
| **UN PRB** | United Nations' Principles for Responsible Banking |
| **UNEPFI** | United Nations Environment Programme Finance Initiative |
| **UTM** | Virgin Money Unit Trust Managers Limited |
| **VAA** | Virgin Atlantic Airways Limited |
| **VaR** | Value at risk |
| **VIU** | Value-in-use |
| **WIP** | Work-in-progress |
| **YoY** | Year-on-year |

# Country by country reporting

The Capital Requirements (Country by Country Reporting) Regulations 2013 came into effect on 1 January 2014 and place certain reporting obligations on financial institutions that are within the scope of the European Union's CRD IV. The purpose of the Regulations is to provide clarity on the source of the Group's income and the locations of its operations.

The vast majority of entities that are consolidated within the Group's financial statements are UK registered entities. The activities of the Group are described in the Strategic report contained in the Group's Annual Report and Accounts.

| | 2023 UK |
|---|---|
| Average FTE employees (number) | **7,166** |
| Total operating income (£m) | **1,827** |
| Profit before tax (£m) | **345** |
| Corporation tax paid (£m) | **45** |
| Public subsidies received (£m) | **–** |

The only other non-UK registered entity of the Group is a Trustee company that is part of the Group's securitisation vehicles (Lanark and Lannraig). Lannraig Trustees Limited is registered in Jersey. This entity plays a part in the overall securitisation process by having the beneficial interest in certain mortgage assets assigned to it. This entity has no assets or liabilities recognised in its financial statements with the securitisation activity taking place in other UK registered entities of the structures. This entity does not undertake any external economic activity and has no employees. The results of this entity as well as those of the entire Lanark and Lannraig securitisation structures are consolidated in the financial statements of the Group.

# Other information

The financial information included in this results announcement does not constitute statutory accounts within the meaning of section 434 of the Companies Act 2006. Statutory accounts for the year ended 30 September 2023 were approved by the directors on 22 November 2023 and will be delivered to the Registrar of Companies following publication in December 2023. The auditor's report on those accounts was unqualified and did not include a statement under sections 498(2) (accounting records or returns inadequate or accounts not agreeing with records and returns) or 498(3) (failure to obtain necessary information and explanations) of the Companies Act 2006.