Company Registered Number: 65046

THE ROYAL BANK OF SCOTLAND INTERNATIONAL (HOLDINGS) LIMITED
and
THE ROYAL BANK OF SCOTLAND INTERNATIONAL LIMITED

ANNUAL REPORT AND ACCOUNTS

31 December 2021

Contents

Board of directors and secretary

Chairman

John Philip Ward Brewster

Executive directors

Andrew Martin McLaughlin
Chief Executive Officer

Lynn Ann Cleary
Chief Financial Officer

Non-executive directors

Bruce Mark Cannon

Gregory John Branch

Christine Hilary Ashton

Stuart Porteous (resigned 4 Nov 2021)

Company Secretary

Rachael Emma Pocklington (appointed 6 October 2021)

Ralph Antoine Ricks (resigned 6 October 2021)

Ralph Antoine Ricks (appointed 22 April 2021)

Andrew Nicholson (resigned 22 April 2021)

Auditor

Ernst & Young LLP
Castle Street
St Helier
Jersey
JE1 1EY

Registered office and Head office

Royal Bank House
71 Bath Street
St Helier
Jersey
JE2 4SU

The Board information covers the following companies:

The Royal Bank of Scotland International (Holdings) Limited
Registered in Jersey, Channel Islands No. 65046

The Royal Bank of Scotland International Limited
Registered in Jersey, Channel Islands No. 2304

Report of the directors

Presentation of information

The directors of The Royal Bank of Scotland International Limited (the "Company"/"RBS International"/"RBSI"/the "Bank") present their Annual Report, together with audited consolidated financial statements of The Royal Bank of Scotland International (Holdings) Limited (the "RBSIH"/"RBS International Holdings") and its subsidiaries (together "the RBSI Group") for the year ended 31 December 2021.

The audited financial statements of The Royal Bank of Scotland International Limited and The Royal Bank of Scotland International (Holdings) Limited are clearly and separately identifiable throughout this document.

The financial statements are prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IASB). The Bank publishes its financial statements in the functional currency, pounds sterling ('£' or 'sterling') and all values are rounded to the nearest million pound, except when otherwise indicated. The abbreviations '£m' and '£bn' represent millions and thousands of millions of pounds sterling, respectively.

Activities and Business review

Principal activities

The Royal Bank of Scotland International Holdings is a holding company owning the entire issued share capital of RBS International, as well as the other key companies forming the Group, including NatWest Trustee and Depositary Services Limited (NWTDS) and RBS International Depository Services SA (RBSI DS).

The RBS International is one of the largest banks operating in the Channel Islands, Isle of Man and Gibraltar with wholesale branches in Luxembourg and the United Kingdom (UK). It provides a comprehensive range of financial services through its International Retail & Commercial Banking (IRCB) and Institutional Banking (IB) customer segments. IRCB provides loan and deposit products and services to personal, private, business and commercial customers. IB provides services to European fund asset managers, fund administrators and corporate service providers.

NWTDS provides corporate trustee and depositary services to UK domiciled Authorized Fund Managers in respect of the Collective Investment Schemes they operate. RBSI DS operates Depositary Services for regulated Alternative Investment Funds (AIFs) that are mainly established and regulated in Luxembourg invested in non-custodial assets.

The directors do not anticipate any material change in the type or activities of the Bank or RBSI Group.

In January 2022 NatWest Group announced the creation of the new Commercial and Institutional franchise, bringing together Commercial, RBS International and NatWest Markets to form a single franchise effective in April 2022. A closer coordination across our product capabilities, points of presence and channels will allow us to support and deliver across our customers' lifecycle more completely and effectively. The new franchise, Commercial and Institutional will be run by Andrew McLaughlin, current CEO of RBSIH, and Paul Thwaite, current Chief Executive Officer, Commercial Banking at NatWest Group, who will lead the non-ring fenced and ring fenced parts respectively. Olly Holbourn, current Director of Strategy and Ventures at NatWest Group, will take on the role of CEO for RBSIH during 2022.

The ultimate holding company of RBSIH is NatWest Group plc ('NWG') which provides support and access to all central resources. The RBSI Group will leverage this relationship to NWG and other subsidiaries to continue to improve on the quality and efficiency of the services and products provided.

Copies of the annual report of NWG can be obtained from Corporate Governance and Regulatory Affairs, NatWest Gogarburn, Edinburgh EH12 1HQ, the Registrar of Companies or through the NWG website, www.natwestgroup.com.

Business review

The RBSI Group's purpose, which is aligned with NWG, is to champion potential, helping people, families and businesses to thrive.

We will continue to become much simpler as a bank and much simpler to deal with for our clients, through a focus on great client service and technology and improving client journeys.

Supporting customers at every stage of their lives

- We provided 8,729 financial health checks, of which over 21% were virtual.
- We've introduced 95% mortgages to help more young people onto the property ladder and overall we have supported customers with £366 million of gross new mortgage lending in 2021.
- We have helped customers to grow their deposits with over 500 customers now saving ≥ £100 who have previously never saved with us or have previously had <£100 saved with us.
- We furnished an Isle of Man (IOM) based charity's new office by donating desks, cabinets and a reception desk.

Powered by partnerships and innovation

- We launched Cora, our personal Artificial Intelligence (AI) assistant. 63% of interactions with Cora have been completed without the need for human intervention.
- RBSI's Social Enterprise Mentoring Scheme is now well established. We've partnered with a social enterprise in each retail banking jurisdiction to share our knowledge and expertise. We have also shared our wellbeing material, which received the Wellbeing in the Workplace Star Award for our work with Gibraltar Samaritans.
- Partnering with four local banks, RBSI will contribute £90,000 over three years to help secure the future of Jersey's Community Savings Limited, a registered charity working to promote financial inclusion.
- We are engaging with local governments, initially Guernsey and Jersey, to promote Energy Performance Certificates (EPC) for properties and explore options to embed government grants into our mortgage customer journeys.

Sharpened capital allocation

- We returned to paying dividends during the year, reflecting the strength of our capital position and profitability. Resultant capital ratios remain above management target with capacity to continue supporting targeted growth.

Simple to deal with

- In responding to changing customer demands we introduced cheque deposits in our mobile app amongst other new features (including ability to freeze debit cards, biometric approval and confirmation of payee) across our personal digital channels. These have contributed to a 23% increase in users this year.
- Overall 82% of our local banking customers are now registered with digital banking, which is a 14% increase compared with 2020.
- IB customers have increased convenience with viewing their accounts and authorise payments through our new eQ Mobile app.
- We have worked closely with NatWest Markets across our IB business to create a holistic offering for our customers across products and geographies.

Performance key metrics and ratios	Group 2021	Group 2020	Bank 2021	Bank 2020
Total Income	£549m	£495m	£508m	£461m
Operating profit before tax	£350m	£94m	£335m	£82m
Loans and advances to customers	£15.5bn	£13.3bn	£15.5bn	£13.3bn
Customer deposits	£37.5bn	£31.3bn	£37.5bn	£31.3bn
Loan to deposit ratio	41%	42%	41%	42%
Depositary assets & assets held in a fiduciary capacity	£482bn	£430bn	£2.8bn	£3.1bn
RBSI regulatory metrics				
Liquidity portfolio			£23.1bn	£18.9bn
Risk weighted assets (RWAs)			£7.4bn	£7.3bn
CET1 capital ratio			20.9%	18.6%
T1 capital ratio			25.0%	22.7%
Leverage ratio(1)			4.15%	4.4%
Liquidity coverage ratio (LCR)			136%	137%

(1) Leverage ratio is Tier 1 capital as a percentage of on and off balance sheet exposures in line with Jersey Financial Services Commission (JFSC) guidance. The primary driver of the ratio is short term deposit balances, which RBSI typically holds in high quality liquid assets. Excluding unencumbered central bank balances would result in a ratio of 6.8%.

Strong operating performance with business growth

The RBSI Group's operating profit before tax was £350 million compared with an operating profit before tax of £94 million in 2020, reflecting resilient growth, cost reduction and a significant impairment release.

The Bank's operating profit before tax was £335 million compared with an operating profit before tax of £82 million in 2020.

The RBSI Group and Bank's financial performance are presented in the Income Statement on page 17. These results demonstrate the resilience of our underlying business and the strength of our balance sheet whilst also investing for growth as we support our customers and drive sustainable returns to our shareholder.

Income

RBSI Group income increased by 11% to £549 million with IB customer lending volume growth and higher depositary income.

Operating expenses

RBSI Group operating expenses decreased by 15% to £251 million. Headcount has decreased by 140 to 1,398 permanent employees and related people costs have decreased by £9 million.

Impairments

Whilst we continue to navigate a high degree of uncertainty in the wider economic environment, a net impairment release of £52 million reflects an improved economic outlook. We have assessed the downside risk posed by COVID-19 to be diminishing over the course of 2021. The expected credit losses (ECL) coverage ratio has decreased from 0.93% in 2020 to 0.33%. Whilst we are comfortable with the strong performance of our book, we continue to hold economic uncertainty post model adjustments (PMA) of £20 million, or 36% of total impairment provisions.

Loans and advances to customers

Loans and advances to customers have increased by £2.2 billion during the year to £15.5 billion with growth mainly in IB clients.

Customer deposits

Customer deposits at £37.5 billion have increased £6.2 billion and represent the RBSI Group's primary funding source.

Capital and liquidity management

The RBSI Group's capital and liquidity positions remained robust during 2021. As RBSIH is not a regulated entity, the capital and liquidity metrics of the Royal Bank of Scotland International Limited are discussed.

As at 31 December 2021 the CET1 ratio was 20.9% (2020: 18.6%) and the Liquidity Coverage Ratio was 136% (2020: 137%).

The increase in CET1 reflects an increase in CET1 equity with some audited profits not distributed.

RWAs have increased £0.1 billion to £7.4 billion driven by increased lending commitments with a reduction of £0.1 billion of impaired assets now treated as a capital deduction.

The RBSI Group's loan to deposit ratio stands at 41% at 31 December 2021 (2020: 42%). To support diversification of funding sources the RBSI Group continues to issue Euro Commercial Paper with volumes of £0.5 billion at December 2021.

The RBSI Group's securities holdings of £5.9 billion are highly liquid and comprised primarily of UK Gilts, German Bund and US Treasuries.

Depositary assets & assets held in a fiduciary capacity

The RBSI Group holds assets under management which are not included in its financial statements. This includes trustee and depositary services to Collective Investment Schemes (CIS), including Alternative Investment Funds (AIFs) and Undertakings for Collective Investment in Transferable Securities Directive (UCITS). Depositary assets are favourably impacted by new monies into funds and a strong performance by some fund managers.

Credit ratings

The Bank has the following Credit Ratings at 31 December 2021:

S&P	A- / A-2 (Stable)
Moody's	A3 / P-2 (Stable)
Fitch	A / F1 (Stable)

During the year Moody's upgraded our long-term credit rating to A3 and moved our rating outlook to stable (from positive) and affirmed the short-term credit rating at P-2. The agency noted this reflected the resilience of the business throughout the pandemic, our continued profitability and strong balance sheet position.

Accounting policies

The reported results of the RBSI Group are sensitive to the accounting policies, assumptions and estimates that underline the preparation of its financial statements. Details of the RBSI Group's accounting policies and key sources of estimation uncertainty are included within the accounting policies on pages 22 to 27.

Risk management

The prevailing market and economic conditions pose risks for the RBSI Group. These include the level of defaults from customers on outstanding advances as well as the degree of uncertainty in the valuation of other financial assets and liabilities.

The financial position of the RBSI Group, its cash flows, liquidity position and borrowing facilities are set out in the financial statements. Notes 8 and 18 to the financial statements include the RBSI Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

Governance

The Board

The Board is collectively responsible for the long-term success of the RBSI Group; approving the strategic priorities and delivering sustainable value to its shareholder. It monitors and maintains the consistency of the RBSI Group's activities within the strategic direction of NWG. It reviews and approves risk appetite for strategic and material risks in accordance with NWG Risk Appetite Framework and it monitors performance against risk appetite for the RBSI Group.

It approves the RBSI Group's key financial objectives and keeps the capital and liquidity positions of the RBSI Group under review. The Board is also responsible for purpose and culture, which underpins all of the RBSI Group's activities and its long-term sustainability.

The Board's terms of reference include key aspects of the RBSI Group's affairs reserved for the Board's decision and are reviewed at least annually.

In order to provide effective oversight and leadership the Board has established three Board Committees with particular responsibilities:

The Audit Committee assists the Board in discharging its responsibilities for monitoring the quality of the financial statements. It reviews the accounting policies, financial reporting and relevant compliance practices of the RBSI Group. It also reviews its systems and standards of internal controls and monitors the RBSI Group's processes for internal and external audit.

The Board Risk Committee provides oversight and advice on current and potential risk exposures and on future risk strategy. It reviews compliance with approved risk appetite and oversees the operation within the RBSI Group of its Risk Policy Framework.

The Remuneration Committee is responsible for overseeing the implementation of the RBSI Group's Remuneration Policy. The Remuneration Committee also reviews performance and remuneration arrangements for senior executives of the RBSI Group.

There are a number of areas where the Board has delegated specific authority to management, including the Chief Executive Officer (CEO) and Chief Financial Officer (CFO). These include responsibility for the operational management of the RBSI Group's businesses as well as reviewing high-level strategic issues and considering risk appetite, risk policies and risk management strategies in advance of these being considered by the Board and/or its Committees. The CEO is supported by various management level committees including the ExCo which assists the CEO in managing strategic, financial, capital and operational issues related to the running of the business.

The roles of Chairman and CEO are distinct and separate, with a clear division of responsibilities. The Chairman leads the Board and ensures the effective engagement and contribution of all executive, non-executive and independent non-executive directors. The CEO has responsibility for all RBSI Group businesses and acts in accordance with authority delegated by the Board. The independent non-executive directors combine broad business and commercial experience with independent and objective judgment, and they provide independent challenge to the executive directors and leadership team.

The Bank has a separate board structure to provide effective oversight and leadership.

Directors and Secretary

The present directors and secretary of both the RBSI Group and the Bank, are listed on page 3.

Colleagues

Colleague engagement

As government advice relaxes around workplace, public transport, social distancing, self-isolation rules and the success of the vaccination roll out, the RBSI Group introduced a new way of working with a hybrid approach to office and home working, appropriate to the needs of the role to enable us to continue to deliver for customers. Our office spaces now support a more flexible and dynamic working environment when we do spend time in the office.

The RBSI Group values the input of its colleagues and actively seeks opportunities to engage with them to contribute to on-going dialogue and activities to make the RBSI Group a better bank for our customers and colleagues. The bi-annual colleague listening survey, known as 'Our View', provides valuable data to decision makers across the RBSI Group in support of improving employee engagement and satisfaction. 76% of colleagues completed the latest survey in September 2021. Results are reflective of a challenging couple of years and scores have declined against 2020 but remain above the global industry level in the majority of areas. RBSI ExCo is reviewing actions to be taken as part of the 2022 strategy to improve areas where scores have dropped significantly or remain consistently low.

Diversity, Equity and Inclusion

The RBSI Group has a Diversity, Equity and Inclusion Policy and values and promotes diversity in all areas of recruitment and employment. We work to avoid limiting potential through bias, prejudice or discrimination. The RBSI Group recognises the beneficial contribution of a diverse mix of uniquely talented individuals for the delivery of great service to our diverse customer base.

The key principles of our Diversity Equity and Inclusion Policy are to attract, motivate and retain the best talent. We base the employment relationship on the principles of fairness, respect and inclusion. We comply with local laws on equality and Our Code, which sets out the RBSI Group's expected behaviours and standards of conduct, to build and develop an inclusive workforce in order to understand and respond to our diverse customer base. A series of initiatives were launched this year to support our Diversity, Equity and Inclusion goals:

- To support our commitment to keep our recruitment process free from all forms of bias, we launched a Recruitment Yes Check across all hiring, regardless of level along with inclusion focused training for hiring and line managers.
- Our Employee Led Networks, supported by 52 inclusion champions continue to influence how the RBSI Group is becoming more inclusive and accessible by promoting and advocating colleague awareness on all elements of diversity and inclusion including training and knowledge sharing activities.

- Gender and Ethnicity pay gap data now forms part of NatWest Group's reporting: these are determined by the legal entity employer.
- We report quarterly against our Gender and Ethnicity targets and have seen positive trends in ethnicity through 2021 however gender remains challenging in a relatively small population. Both targets remain a top priority on the people agenda as we build a fully inclusive organisation.

2022 will see the launch of an NWG-wide Diversity, Equity and Inclusion Action Committee which will drive a focused, action orientated and impactful One Bank approach to Diversity, Equity and Inclusion.

Safety, health and wellbeing

We believe that the wellbeing of colleagues forms a large part of making the RBSI Group a great place to work. As an employer we want to make sure our colleagues have the right support to be healthy and happy and feel able to bring their whole selves to work. The RBSI Group's Wellbeing strategy is delivered against four pillars; Physical, Mental, Social and Financial. Within the RBSI Group we have a network of Wellbeing Ambassadors who are available for colleagues to reach out to and can provide practical support and advice. The RBSI Group has a programme of events throughout the year that focuses on physical, mental and financial wellbeing with a host of resources and tool kits available to colleagues. In the RBSI Group we have ensured these resources and toolkits are tailored to our jurisdictions where necessary to ensure all colleagues across the organisation are able to access support where it is needed.

Speak Up

Colleagues can report concerns relating to wrong-doing or misconduct through Speak Up, our whistleblowing service. The service facilitates confidential and anonymous reporting. The 2021 colleague listening survey showed an above financial services industry score when asking colleagues if they feel safe to speak up, as well as understanding the process of how they do that.

Building a healthy culture

The Board views building a high performing and healthy culture as essential to the RBSI Group's long-term success. The RBSI Group's culture plan focuses on becoming a purpose led organisation, helping people, families and businesses to thrive.

Our Values guide the way we serve our clients, how we work together and manage and mitigate risk. They help us to focus on the long term rather than the short term.

The RBSI Group also maintains a risk culture plan, aligned to NWG's target of achieving a generative risk culture whereby "risk is simply part of the way people work and think."

Championing the potential of our colleagues

We are committed to developing knowledge, skills and behaviours in a number of key critical capability areas that support our ambition and purpose. By encouraging a culture of continuous learning, knowledge sharing and reflective practice, we are ensuring that colleagues stay relevant and employable – and that we can adapt to the changing needs of our customers, communities and context.

The RBSI Group offers a wide range of learning opportunities including technical knowledge and skills. To keep the RBSI Group safe and secure, all colleagues must complete mandatory learning on our key policies, including anti-bribery and corruption, health and safety, and inclusion. Some colleagues also complete additional mandatory learning that's related to where they work or the job they do.

In 2021, as part of NWG, we launched Talent Academy which champions the potential of our top talent across all levels of the organisation and seeks to encourage development and mobility for our future leaders. In addition to this we are targeting jurisdictional talent where location may pose more of a barrier to mobility and progression for our colleagues.

Our approach to performance management provides clarity for our colleagues about how their contribution links to our ambition. Individual performance objectives are clearly linked to our vision and strategy.

Rewarding our colleagues

We have a balanced approach to reward which recognises both what the individual has achieved and how they have achieved it. We recognise contributions that support our values and holds individuals to account for behaviour and performance that do not.

Climate

NWG joined the Net Zero Banking Alliance, working with other financial organisations to help deliver the Paris Agreement.

We are taking an active role in the transition to a low-carbon economy. Since 2020, RBSI IB business has lent £1.5 billion in Climate and Sustainable Funding and Financing to drive real-world outcomes with energy transition fund focusing on clean energy production, energy efficiency enhancements and clean energy utilisation. We also continue to work with customers to shape their sustainable performance targets and incentivise performance through Sustainability-Linked Loans. In October 2021, NWG announced a new target to provide an additional £100 billion of Climate and Sustainable Funding and Financing between 1 July 2021 and the end of 2025, which RBSIH will support.

We continue to review our product suite to identify where we can support individuals and local businesses to make climate-focused choices. We launched our first Green Mortgage product for UK properties, rewarding customers for purchasing energy efficient properties. The Green Mortgage product offer a lower interest rate for customers purchasing, porting or remortgaging a property with an EPC rating of A or B, rewarding them for helping drive the UK transition towards a low carbon economy.

We have launched 'Climate Zone' across NatWest International and Isle of Man Bank websites to engage with our customers and highlight the importance of individual action as we support our local communities.

We also ran a series of podcasts 'A Just Transition' throughout 2021 looking at a different topic around ESG.

As part of NWG, we are currently net zero carbon across our own operations through a combination of emissions reductions and, largely, carbon offsetting through the purchase of internationally recognised TIST Carbon Credits.
We continue to embed climate change into how we run our business in addition to fostering a culture of personal climate action. This means reviewing the carbon footprint of our offices (the energy, water use and waste from our buildings), and our supply chain (the environmental impact of the goods and services we use). We also support our employees to review their carbon footprint (through Giki Zero which is currently in pilot). Education amongst all colleagues continues to be a focus for the RBSI Group including a weekly ESG brief shared with all colleagues and climate related risk training for relationship managers.

We supported the applications of Jersey Finance and Guernsey Finance to the UN-Convened Finance Centres for Sustainability (FC4S) by completing the required questionnaires.

Outlook

The rollout of COVID-19 vaccines in 2021 has contributed towards an improved economic outlook. The outlook remains subject to significant uncertainty and we will continue to refine our internal forecast as the economic position evolves.

We support global initiatives aimed at making the global tax system more effective, for example the introduction of the OECD Inclusive Framework proposals published in December 2021.

Scenarios identified as having a potentially material negative impact on the RBSI Group include; persistent or more intense weakness in global economic growth; shifts in the international tax policy environment; an extended period of low inflation and low (or negative) interest rates; market volatility or fluctuations in the value of the pound sterling, new or extended economic sanctions; volatility in commodity prices or concerns regarding sovereign debt; and political and geopolitical instability.

This may be compounded by the ageing demographics of the populations in the markets that the RBSI Group serves, or rapid change to the economic environment due to the adoption of technology and artificial intelligence. Any of the above developments could adversely impact the RBSI Group directly (for example, as a result of credit losses) or indirectly (for example, by impacting global economic growth and financial markets and the RBSI Group's clients and their banking needs).

The directors, noting the continued and forecast challenging economic outlook and cognisant of the macroeconomic and political risks, consider that the RBSI Group's continued focus on accelerating digital transformation, simplifying its business model, maintaining strength, sustainability and supporting growth will assist in the delivery of the NWG's purpose to champion potential, helping people, families and businesses to thrive.

Auditor

The auditor, Ernst & Young LLP, has expressed its willingness to continue as auditor and will continue in office.

Economic and political landscape

The RBSI Group continues to deal with a range of significant risks and uncertainties in the external economic, political and regulatory environment.

Scenarios identified as having a potentially negative impact on the RBSI Group include;

- Decreases in interest rates and/or continued sustained low or negative interest rates could put pressure on the RBSI Group's interest margins and adversely affect the RBSI Group's profitability.
- Changes in currency rates, particularly in the sterling-US dollar and euro-sterling rates, can adversely affect the value of assets, liabilities, income, RWAs and expenses.
- Shifts in the international tax policy environment and imposition of levies and taxes can affect the distributable profits of the RBSI Group, as the RBSI Group is subject to the tax laws and practice in the jurisdictions in which it has operations.
- Political and geopolitical instability could result in subdued confidence and impact on credit ratings.
- Changes to IRB regulation from the Prudential Regulatory Authority (PRA) and the Jersey Financial Services Commission (JFSC).
- Environment, social and governance (ESG) risks relate to climate change, diversity, cybersecurity risk, reputational risk and compliance to the relevant laws.
- Challenges adjusting to the UK's new trading relationship with the EU and supply chain labour and material shortages caused by a range of factors including Covid-related, Brexit-related and specific industry issues.
- The introduction of Basel 3 amendments may result in additional supervisory and prudential expectations, including an increase in risk weighted assets. The details of Basel 3 amendments remain subject to regulatory uncertainty on both quantum and timing.

Going concern

The directors are satisfied with the financial position of the RBSI Group and the Bank and believe that they are appropriately placed to manage their business risks successfully.

Having reviewed the RBSI Group and Bank forecasts, projections and other relevant evidence, the directors have a reasonable expectation that the RBSI Group and the Bank will continue in operational existence for the foreseeable future. Foreseeable future is defined as 12 months from the date of signing of this Report and Accounts, being 16th February 2023. Accordingly, the financial statements of the RBSI Group and the Bank have been prepared on a going concern basis.

Dividends

The Bank's directors declared an ordinary dividend of £54 million (2020: £nil) to RBSIH. No interim dividend was paid during the year. A preference dividend of £20 million (2020: £20 million) was paid to NWG. RBSIH directors declared an ordinary dividend of £76 million (2020: £nil) to NWG.

Post balance sheet events

Post balance sheet events are described in note 22 to the financial statements.

Andrew Martin McLaughlin
Chief Executive Officer

Lynn Ann Cleary
Chief Financial Officer

Date: 17 February 2022

Statement of directors’ responsibilities

The directors of The Royal Bank of Scotland International Limited and the directors of The Royal Bank of Scotland International (Holdings) Limited are responsible for preparing the financial statements in accordance with applicable law and regulation.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards (IFRS) as issued by the IASB. The financial statements are required by law to give a true and fair view of the state of affairs of the Group and Bank and of the profit or loss of the Group and Bank for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and Bank will continue in business.

The directors of The Royal Bank of Scotland International (Holdings) Limited are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the financial statements comply with the Companies (Jersey) Law 1991.

The directors of The Royal Bank of Scotland International Limited are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Bank and enable them to ensure that the Annual Report and Accounts complies with the Companies (Jersey) Law 1991, the Banking Business (Jersey) Law 1991, the Financial Services (General Insurance Mediation Business (Accounts, Audits, Reports and Solvency)) (Jersey) Order 2005, the Financial Services (Trust Company and Investment Business (Accounts, Audits and Reports)) (Jersey) Order 2007 and the Financial Services (Fund Services Business (Accounts, Audits and Reports)) (Jersey) Order 2007, the Financial Services (Jersey) Law 1998 and their Codes of Practice.

The directors of The Royal Bank of Scotland International (Holdings) Limited and the directors of The Royal Bank of Scotland International Limited are responsible for safeguarding the assets of the Group and Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities. The directors confirm they have discharged those responsibilities.

By order of the Boards of The Royal Bank of Scotland International Limited and The Royal Bank of Scotland International (Holdings) Limited:

Andrew Martin McLaughlin
Chief Executive Officer

Date: 17 February 2022

Lynn Ann Cleary
Chief Financial Officer

Date: 17 February 2022

Building a better working world

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF
THE ROYAL BANK OF SCOTLAND INTERNATIONAL (HOLDINGS) LIMITED

Opinion

We have audited the financial statements of The Royal Bank of Scotland International (Holdings) Limited (the "Company") and its subsidiaries (the "Group") for the year ended 31 December 2021 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated Balance Sheet, the Consolidated Statement of Changes in Equity, the Consolidated Cash Flow Statement and the related notes 1 to 22, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards as issued by the IASB.

In our opinion, the financial statements:

- give a true and fair view of the state of the Group's affairs as at 31 December 2021 and of its profit for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards as issued by the IASB; and
- have been properly prepared in accordance with the requirements of the Companies (Jersey) Law 1991.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the financial statements, including the UK FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Group's ability to continue as a going concern for a period up to 17 February 2023 being not less than twelve months from when the financial statements are authorised for issue.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's ability to continue as a going concern.

Other information

The other information comprises the information included in the Annual Report other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained within the Annual Report.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters in relation to which the Companies (Jersey) Law 1991 requires us to report to you if, in our opinion:

- proper accounting records have not been kept by the Company, or proper returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the Company's accounting records and returns; or
- we have not received all the information and explanations we require for our audit.

Responsibilities of directors

As explained more fully in the Statement of directors' responsibilities set out on page 10, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the Group and management.

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Group and determined that the most significant are those that relate to the reporting framework, namely;
    - the Companies (Jersey) Law 1991
- We understood how the Group is complying with those frameworks by making enquiries of management, internal audit and those responsible for legal and compliance matters and corroborated this by reviewing

supporting documentation. We also reviewed minutes of the Board and gained an understanding of the Group's governance framework;

- We assessed the susceptibility of the Group's financial statements to material misstatement, including how fraud might occur by considering the controls established to address risks identified to prevent or detect fraud. We identified the risk of management override associated to impairment provisions and the risk associated with the revenue recognition of manual and partly manual revenue streams to be a fraud risk. When performing our fraud procedures, we identified other areas that we considered, such as cybersecurity, the impact of remote working and the appropriateness of sources used when performing confirmation testing on accounts such as cash, loans and securities; and

- Based on this understanding we designed our audit procedures to identify noncompliance with such laws and regulations. Our procedures involved reading Board minutes, complaints register, compliance reports, and inquiries of internal legal counsel, those charged with governance, executive management, compliance and internal audit, and the performance of journal entry testing meeting our defined risk criteria and our understanding of the business.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at https://www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Use of our report

This report is made solely to the Company's members, as a body, in accordance with Article 113A of the Companies (Jersey) Law 1991. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Steven Robb
for and on behalf of Ernst & Young LLP
Jersey, Channel Islands
17 February 2022

Notes:

1. The maintenance and integrity of the Company's web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.

2. Legislation in the Jersey governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Building a better working world

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF THE ROYAL BANK OF SCOTLAND INTERNATIONAL LIMITED

Opinion

We have audited the financial statements of The Royal Bank of Scotland International Limited (the "Company") for the year ended 31 December 2021 which comprise the Income Statement, the Statement of Comprehensive Income, the Balance Sheet, the Statement of Changes in Equity, the Cash Flow Statement and the related notes 1 to 22, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards as issued by the IASB.

In our opinion, the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2021 and of its profit for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards as issued by IASB
- have been properly prepared in accordance with the requirements of the Companies (Jersey) Law 1991;
- have been prepared in accordance with the requirements of the Banking Business (Jersey) Law 1991;
- have been prepared in accordance with the Financial Services (Trust Company and Investment Business (Accounts Audits and Reports)) (Jersey) Order 2007;
- have been prepared in accordance with the Financial Services (Fund Services Business (Accounts, Audits and Reports)) (Jersey) Order 2007; and
- have been prepared in accordance with the requirements of the Financial Services (General Insurance Mediation Business (Accounts, Audits, Reports and Solvency)) (Jersey) Order 2005.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements, including the UK FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Group's ability to continue as a going concern for a period up to 17 February 2023 being not less than twelve months from when the financial statements are authorised for issue.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Company's ability to continue as a going concern.

Other information

The other information comprises the information included in the Annual Report other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained within the Annual Report.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF
THE ROYAL BANK OF SCOTLAND INTERNATIONAL LIMITED

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters in relation to which the Companies (Jersey) Law 1991 requires us to report to you if, in our opinion:

- proper accounting records have not been kept by the Company, or proper returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the Company's accounting records and returns; or
- we have not received all the information and explanations we require for our audit.

Responsibilities of directors

As explained more fully in the Statement of directors' responsibilities set out on page 10, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the Company and management.

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Company and determined that the most significant are those that relate to the financial reporting framework, namely:
    - the Companies (Jersey) Law 1991;
    - the Banking Business (Jersey) Law 1991; and

- the Financial Services (Jersey) Law 1998

- We understood how the Company is complying with those frameworks by making enquiries of management, internal audit and those responsible for legal and compliance matters, and corroborated this by reviewing supporting documentation. We also read correspondence between the Company and the Jersey Financial Services Commission, read minutes of the Board, and gained an understanding of the Company's governance framework;
- We assessed the susceptibility of the Company's financial statements to material misstatement, including how fraud might occur, by considering the controls established to address risks identified to prevent or detect fraud. We identified the risk of management override associated to impairment provisions and the risk associated with the revenue recognition of manual and partly manual revenue streams to be a fraud risk. When performing our fraud procedures, we identified other areas that we considered, such as cybersecurity, the impact of remote working and the appropriateness of sources used when performing confirmation testing on accounts such as cash, loans and securities;
- Based on this understanding we designed our audit procedures to identify noncompliance with such laws and regulations. Our procedures involved reading Board minutes, complaints register, compliance reports, and inquiries of internal legal counsel, those charged with governance, executive management, compliance and internal audit, and the performance of journal entry testing meeting our defined risk criteria and our understanding of the business; and
- The Company operates in the banking industry which is a highly regulated environment. As such the Audit Partner considered the experience and expertise of engagement team to ensure that the team had the appropriate competence and capabilities, which included use of specialists where appropriate.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at https://www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Use of our report

This report is made solely to the Company's members, as a body, in accordance with Article 113A of the Companies (Jersey) Law 1991. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Steven Robb
for and on behalf of Ernst & Young LLP
Jersey, Channel Islands
17 February 2022

Notes:

1. The maintenance and integrity of the Company's web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.

2. Legislation in the Jersey governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Consolidated income statement for the year ended 31 December 2021

		Group		Bank	
		2021	2020	2021	2020
	Note	£m	£m	£m	£m
Interest receivable		438	439	438	439
Interest payable		(54)	(66)	(54)	(66)
Net interest income	1	384	373	384	373
Fees and commissions receivable[1]		125	95	85	61
Fees and commissions payable		(1)	(1)	(1)	(1)
Other operating income[1]		41	28	40	28
Non-interest income	2	165	122	124	88
Total income		549	495	508	461
Staff costs		(117)	(139)	(103)	(126)
Premises and equipment		(24)	(33)	(22)	(32)
Other administrative expenses		(96)	(103)	(87)	(95)
Depreciation, impairment and amortisation		(14)	(19)	(14)	(19)
Operating expenses	3	(251)	(294)	(226)	(272)
Operating profit before impairment gains		298	201	282	189
Impairment releases/(losses)	8	52	(107)	53	(107)
Operating profit before tax		350	94	335	82
Tax charge	5	(54)	(26)	(52)	(24)
Profit for the year		296	68	283	58

(1) Fees and commissions receivable for 2020 has been re-presented, previously the balance included trading income. In the current year, trading income has been reclassified to other operating income.

The accompanying notes on pages 28 to 96 and the accounting policies on pages 22 to 27 form an integral part of these financial statements.

Consolidated statement of comprehensive income for the year ended 31 December 2021

	Note	Group 2021 £m	Group 2020 £m	Bank 2021 £m	Bank 2020 £m
Profit for the year		**296**	68	**283**	58
Items that do not qualify for reclassification					
Remeasurement of retirement benefit schemes	4	**34**	23	**34**	23
Tax	5	**(3)**	(2)	**(3)**	(2)
		31	21	**31**	21
Items that do qualify for reclassification					
FVOCI financial assets		**8**	6	**8**	6
Cash flow hedges		**(41)**	1	**(41)**	1
Tax	5	**3**	(1)	**3**	(1)
		(30)	6	**(30)**	6
Other comprehensive gain for the year after tax		**1**	27	**1**	27
Total comprehensive income for the year		**297**	95	**284**	85

The accompanying notes on pages 28 to 96 and the accounting policies on pages 22 to 27 form an integral part of these financial statements.

Consolidated balance sheet as at 31 December 2021

		Group		Bank	
	Note	2021 £m	2020 £m	2021 £m	2020 £m
Assets					
Cash and balances at central banks	7	17,220	13,531	17,220	13,531
Derivatives	6,7	158	41	158	41
Loans to banks - amortised cost	7	1,305	1,231	1,278	1,204
Loans to customers - amortised cost	7	15,463	13,262	15,463	13,262
Amounts due from holding companies and fellow subsidiaries	7	579	637	586	646
Other financial assets	7,9	5,923	5,363	5,923	5,363
Intangible assets	7,12	28	14	14	8
Other assets	7,13	330	284	319	278
Total assets		41,006	34,363	40,961	34,333
Liabilities					
Bank deposits	7	266	5	266	5
Customer deposits	7	37,539	31,280	37,539	31,280
Derivatives	6,7	117	126	117	126
Other financial liabilities	7,14	476	542	476	542
Amounts due to holding companies and fellow subsidiaries	7	242	236	308	322
Other liabilities	7,15	149	158	143	155
Total liabilities		38,789	32,347	38,849	32,430
Owners' equity		2,217	2,016	2,112	1,903
Total liabilities and equity		41,006	34,363	40,961	34,333
Memorandum items					
Contingent liabilities and commitments	19	9,613	9,642	9,613	9,642

The accompanying notes on pages 28 to 96 and the accounting policies on pages 22 to 27 form an integral part of these financial statements.

The accounts were approved by the Board of directors on 17 February 2022 and signed on its behalf by:

Andrew Martin McLaughlin
Chief Executive Officer

Lynn Ann Cleary
Chief Financial Officer

Consolidated statement of changes in equity for the year ended 31 December 2021

		Group		Bank	
		2021	2020	2021	2020
	Note	£m	£m	£m	£m
Called up share capital - at 1 January and 31 December	16	311	311	97	97
Paid-in equity - at 1 January and 31 December	16	300	300	300	300
Share premium - at 1 January and 31 December		499	499	5	5
FVOCI reserve - at 1 January		5	—	5	—
Unrealised gains		6	6	5	6
Realised losses		2	—	2	
Tax		(1)	(1)	(1)	(1)
At 31 December		12	5	11	5
Cash flow hedging reserve - at 1 January		1	—	1	—
Amount recognised in equity (1)		(40)	1	(40)	1
Amount transferred from equity to earnings		(1)	—	(1)	—
Tax		4	—	4	—
At 31 December		(36)	1	(36)	1
Retained earnings - at 1 January		900	831	1,495	1,436
Remeasurement of retirement benefit schemes	4	34	23	34	23
Tax on remeasurement of retirement benefit schemes		(3)	(2)	(3)	(2)
Ordinary dividends paid		(76)	—	(54)	—
Paid-in equity dividends paid		(20)	(20)	(20)	(20)
Profit attributable to ordinary shareholders and other equity owners		296	68	283	58
At 31 December		1,131	900	1,735	1,495
		—			
Owners' equity at 31 December		2,217	2,016	2,112	1,903

(1) In 2021, the amount taken to the cash flow hedging reserve comprised £(40) million (2020: £1 million) in relation to interest rate hedges.

The accompanying notes on pages 28 to 96 and the accounting policies on pages 22 to 27 form an integral part of these financial statements.

Consolidated cash flow statement for the year ended 31 December 2021

	Note	Group 2021 £m	Group 2020 £m	Bank 2021 £m	Bank 2020 £m
Cash flows from Operating activities					
Operating profit before tax		350	94	335	82
Impairment (releases)/losses		(52)	107	(53)	107
Impairment of financial assets		13	—	13	
Defined benefit pension schemes		7	(3)	7	(3)
Depreciation and amortisation		14	19	14	19
Change in fair value taken to profit or loss of other financial assets		96	—	96	—
Elimination of foreign exchange differences		(11)	(204)	(10)	(205)
Charges and release on provisions		4	25	4	25
Loss on sale of other financial assets		2	—	2	—
Profit on sale of net assets/liabilities		(1)	—	(1)	—
Interest receivable on other financial assets		(38)	(45)	(38)	(45)
Other non-cash items		(3)	1	(4)	1
Net cash flows from trading activities		381	(6)	365	(19)
Decrease in net loans to banks		1	—	1	—
(Increase)/decrease in net loans to customers		(2,185)	746	(2,185)	746
Decrease/(increase) in amounts due from holding companies and fellow subsidiaries		10	(12)	3	23
Increase in derivative assets		(157)	(5)	(157)	(5)
Increase in other assets		(24)	(2)	(20)	(2)
(Decrease)/increase in derivative liabilities		(9)	70	(9)	70
Increase/(decrease) in banks deposits		262	(9)	262	(9)
Increase in customer deposits		6,259	1,143	6,259	1,143
(Decrease)/increase in other financial liabilities		(68)	542	(68)	542
Increase/(decrease) in amounts due to holding companies and fellow subsidiaries		6	46	(14)	43
Decrease in other liabilities		(23)	(11)	(26)	(10)
Changes in operating assets and liabilities		4,072	2,508	4,046	2,541
Income taxes paid		(41)	(62)	(38)	(59)
Net cash flows from operating activities (1)		4,412	2,440	4,373	2,463
Cash flows from investing activities					
Sale and maturity of other financial assets		1,570	1,811	1,570	1,811
Purchase of other financial assets		(2,234)	(2,099)	(2,234)	(2,099)
Interest received on other financial assets		38	45	38	45
Sale of property, plant and equipment		5	5	5	5
Purchase of property, plant and equipment		(12)	(14)	(12)	(14)
Net asset/liabilities sold		35	—	35	—
Cash expenditure on intangible assets		(15)	(7)	(7)	(2)
Net cash flows from investing activities		(613)	(259)	(605)	(254)
Cash flows from financing activities					
Dividends paid		(96)	(20)	(74)	(20)
Net cash flows from financing activities		(96)	(20)	(74)	(20)
Effects of foreign exchange on cash & cash equivalents		12	204	12	205
Net increase in cash and cash equivalents		3,715	2,365	3,706	2,394
Cash and cash equivalents at 1 January	20	15,299	12,934	15,281	12,887
Cash and cash equivalents at 31 December	20	19,014	15,299	18,987	15,281

(1) Includes interest received of £434 million (2020: £386 million) and interest paid of £56 million (2020: £17 million). Cash flows from operating activities also include interest and repayment of lease liabilities of £4 million (2020: £6 million).

The accompanying notes on pages 28 to 96 and the accounting policies on pages 22 to 27 form an integral part of these financial statements.

Accounting policies

1. Presentation of accounts

The accounts, set out on pages 17 to 96 including these accounting policies on pages 22 to 27, and Risk management sections on pages 57 to 93, are prepared on a going concern basis (refer to the Report of the directors, page 10) in accordance with IFRS as issued by the IASB. The significant accounting policies and related judgments are set out below. The policies apply to both the Group and the Bank.

RBSIH and RBSI are registered in Jersey, Channel Islands. The registered and head office is Royal Bank House, 71 Bath Street, St Helier, Jersey, JE2 4SU.

The accounts are presented in the functional currency, pounds sterling.

With the exception of certain financial instruments as described in Accounting policies on pages 22 to 27, the accounts are presented on a historical cost basis.

Accounting policies are generally considered on an overall basis within RBSI Group such that common accounting policies, assumptions and estimates apply across RBSI Group. Therefore, for the most part, the accounting policies, assumptions, and estimates reflect those in RBSI Group as relevant for the businesses and operations in the Bank and reference to RBSI Group in the notes refers to Bank unless otherwise stated.

Accounting policy changes effective 1 January 2021

The IASB amended IFRS 16 Leases through “COVID-19 amendments on lease modifications – Amendments to IFRS 16 – Leases (IFRS 16)”. The effect of the amendment on NatWest Group’s accounts is immaterial.

2. Basis of consolidation

The consolidated accounts incorporate the financial statements of the Group and entities that give access to variable returns and that are controlled by the Group. Control is assessed by reference to our ability to enforce our will on the other entity, typically through voting rights.

All intergroup balances, transactions, income and expenses are eliminated on consolidation. The consolidated accounts are prepared under uniform accounting policies.

3. Revenue recognition

Interest income or expense relates to financial instruments measured at amortised cost and debt instruments classified as fair value through OCI using the effective interest rate method, the effective part of any related accounting hedging instruments, and finance lease income recognised at a constant periodic rate of return before tax on the net investment. Negative effective interest accruing to financial assets is presented in interest payable and negative interest on financial liabilities is presented in interest receivable. Other interest relating to financial instruments measured at fair value is recognised as part of the movement in fair value.

Fees in respect of services are recognised as the right to consideration accrues through the performance of each distinct service obligation to the customer. The arrangements are generally contractual and the cost of providing the service is incurred as the service is rendered. The pricing base is usually known and always determinable.

4. Employee benefits

Short-term employee benefits, such as salaries, paid absences, and other benefits are accounted for on an accrual basis over the period in which the employees provide the related services. Employees may receive variable compensation satisfied by cash, by debt instruments issued by the NWG or by NWG plc shares. The Group operates a number of share-based compensation schemes under which it awards NWG plc shares and share options to its employees. Such awards are generally subject to vesting conditions.

Variable compensation that is settled in cash or debt instruments is charged to profit or loss on a straight-line basis over the vesting period, taking account of forfeiture and clawback criteria.

Contributions to defined contribution pension schemes are recognised in profit or loss as employee service costs accrue.

For defined benefit pension schemes, the net of the recognisable scheme assets and obligations is reported in the balance sheet. The defined benefit obligation is measured on an actuarial basis. The charge to profit or loss for pension costs (mainly the service cost and the net interest on the net defined benefit asset or liability) is recognised in operating expenses.

Actuarial gains and losses (i.e. gains and/or losses on re-measuring the net defined benefit asset or liability) are recognised in other comprehensive income in full in the period in which they arise. The difference between scheme assets and scheme liabilities, the net defined benefit asset or liability, is recognised in the balance sheet subject to the asset ceiling test which requires the net defined benefit surplus to be limited to the present value of any economic benefits available to the Group in the form of refunds from the plan or reduced contributions to it.

The charge to profit or loss for pension costs (mainly the service cost and the net interest on the net defined benefit asset or liability) is recognised in operating expenses.

5. Property, plant and equipment

Items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for separately.

Depreciation is charged to the income statement on a straight-line basis so as to write off the depreciable amount of property, plant and equipment (including assets owned and let on operating leases) over their estimated useful lives. The depreciable amount is the cost of an asset less its residual value. Freehold land is not depreciated.

The estimated useful lives are as follows:

Freehold and long leasehold buildings	50 years
Short leaseholds	unexpired period of the lease
Computer equipment	up to 5 years
Property adaptation costs	10 years
Other equipment	5 to 15 years

The residual value and useful life of property, plant and equipment are reviewed at each balance sheet date and updated for any changes to previous estimates.

6. Intangible assets and goodwill

Intangible assets acquired by the Group are stated at cost less accumulated amortisation and impairment losses. Amortisation is charged to profit or loss over the assets estimated useful economic lives using methods that best reflect the pattern of economic benefits and is included in depreciation and amortisation. These estimated useful economic lives are:

Computer software	3 to 12 years
Other acquired intangibles	5 to 10 years

Expenditure on internally generated goodwill and brands is written-off as incurred. Direct costs relating to the development of internal-use computer software are capitalised once technical feasibility and economic viability have been established. These costs include payroll, the costs of materials and services, and directly attributable overheads.

Capitalisation of costs ceases when the software is capable of operating as intended. During and after development, accumulated costs are reviewed for impairment against the benefits that the software is expected to generate. Costs incurred prior to the establishment of technical feasibility and economic viability are expensed as incurred as are all training costs and general overheads. The costs of licences to use computer software that are expected to generate economic benefits beyond one year are also capitalised.

Goodwill on the acquisition of a subsidiary is the excess of the fair value of the consideration transferred, the fair value of any existing interest in the subsidiary and the amount of any non-controlling interest measured either at fair value or at its share of the subsidiary's net assets over the net fair value of the subsidiary's identifiable assets, liabilities and contingent liabilities.

Goodwill is measured at initial cost less any subsequent impairment losses. The gain or loss on the disposal of a subsidiary includes the carrying value of any related goodwill.

7. Impairment of non-financial assets

At each balance sheet date, the Group assesses whether there is any indication that its intangible assets, right of use assets or property, plant and equipment are impaired. If any such indication exists, the Group estimates the recoverable amount of the asset and the impairment loss if any. Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired.

The recoverable amount of an asset that does not generate cash flows that are independent from those of other assets or groups of assets, is determined as part of the cash-generating unit to which the asset belongs. A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. For the purposes of impairment testing, goodwill acquired in a business combination is allocated to each of the Group's cash-generating units or groups of cash-generating units expected to benefit from the combination. The recoverable amount of an asset or cash-generating unit is the higher of its fair value less cost to sell or its value in use. Value in use is the present value of future cash flows from the asset or cash-generating unit discounted at a rate that reflects market interest rates adjusted for risks specific to the asset or cash-generating unit that have not been taken into account in estimating future cash flows.

An impairment loss is recognised if the recoverable amount of an intangible or tangible asset is less than its carrying value. The carrying value of the asset is reduced by the amount of the loss and a charge recognised in profit or loss. A reversal of an impairment loss on intangible assets (excluding goodwill) or property, plant and equipment can be recognised when an increase in service potential arises provided the increased carrying value is not greater than it would have been had no impairment loss been recognised. Impairment losses on goodwill are not reversed.

8. Foreign currencies

Transactions in foreign currencies are recorded in the functional currency at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the relevant functional currency at the foreign exchange rates ruling at the balance sheet date. Foreign exchange differences arising on the settlement of foreign currency transactions and from the translation of monetary assets and liabilities are reported in income from trading activities except for differences arising on cash flow hedges (see accounting policy 18).

Non-monetary items denominated in foreign currencies that are stated at fair value are translated into the relevant functional currency at the foreign exchange rates ruling at the dates the values are determined. Translation differences arising on non-monetary items measured at fair value are recognised in profit or loss except for differences arising on nonmonetary financial assets classified as fair value through other comprehensive income (OCI), for example equity shares, which are recognised in other comprehensive income unless the asset is the hedged item in a fair value hedge.

Assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated into Sterling at foreign exchange rates ruling at the balance sheet date. Income and expenses of foreign operations are translated into Sterling at average exchange rates unless these do not approximate to the foreign exchange rates ruling at the dates of the transactions. Foreign exchange differences arising on translation of foreign operations are recognised in other comprehensive income. The amount accumulated in equity is reclassified from equity to profit or loss on disposal of a foreign operation.

9. Leases

As lessor

Finance lease contracts are those which transfer substantially all the risks and rewards of ownership of an asset to a customer. All other contracts with customers to lease assets are classified as operating leases.

Loans to customers include finance lease receivables measured at the net investment in the lease, comprising the minimum lease payments and any unguaranteed residual value discounted at the interest rate implicit in the lease.

Interest receivable includes finance lease income recognised at a constant periodic rate of return before tax on the net investment. Unguaranteed residual values are subject to regular review; if there is a reduction in their value, income allocation is revised and any reduction in respect of amounts accrued is recognised immediately.

Rental income from operating leases is recognised in other operating income on a straight-line basis over the lease term unless another systematic basis better represents the time pattern of the asset's use.

Operating lease assets are included within Property, plant and equipment and depreciated over their useful lives.

As lessee

On entering into a new lease contract, the Group recognises a right of use asset and a lease liability to pay future rentals. The liability is measured at the present value of future lease payments discounted at the applicable incremental borrowing rate. The right of use asset is depreciated over the shorter of the term of the lease and the useful economic life, subject to review for impairment.

Short term and low value leased assets are expensed on a systematic basis.

10. Provisions and contingent liabilities

The Group recognises a provision for a present obligation resulting from a past event when it is more likely than not that it will be required to transfer economic benefits to settle the obligation and the amount of the obligation can be estimated reliably.

Provision is made for restructuring costs, including the costs of redundancy, when the Group has a constructive obligation to restructure. An obligation exists when the Group has a detailed formal plan for the restructuring and has raised a valid expectation in those affected by starting to implement the plan or by announcing its main features.

The Group recognises any onerous cost of the present obligation under a contract as a provision. An onerous cost is the unavoidable cost of meeting the Group's contractual obligations that exceed the expected economic benefits. When the Group vacates a leasehold property, the right of use asset would be tested for impairment and a provision may be recognised for the ancillary occupancy costs, such as rates.

Contingent liabilities are possible obligations arising from past events, whose existence will be confirmed only by uncertain future events, or present obligations arising from past events that are not recognised because either an outflow of economic benefits is not probable or the amount of the obligation cannot be reliably measured. Contingent liabilities are not recognised if not probable but information about them is disclosed unless the possibility of any outflow of economic benefits in settlement is remote.

11. Tax

Income tax expense or income, comprising current tax and deferred tax, is recorded in the income statement except income tax on items recognised outside profit or loss which is credited or charged to other comprehensive income or to equity as appropriate. The tax consequences of servicing equity instruments are recognised in income statement.

Current tax is income tax payable or recoverable in respect of the taxable profit or loss for the year arising in profit or loss, other comprehensive income or equity. Provision is made for current tax at rates enacted or substantively enacted at the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable in respect of temporary differences between the carrying amount of an asset or liability for accounting purposes and its carrying amount for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent their recovery is probable.

Deferred tax is not recognised on temporary differences that arise from initial recognition of an asset or a liability in a transaction (other than a business combination) that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax is calculated using tax rates expected to apply in the periods when the assets will be realised or the liabilities settled, based on tax rates and laws enacted, or substantively enacted, at the balance sheet date.

Deferred tax assets and liabilities are offset where the Group has a legally enforceable right to offset and where they relate to income taxes levied by the same taxation authority either on an individual Group company or on Group companies in the same tax group that intend, in future periods, to settle current tax liabilities and assets on a net basis or on a gross basis simultaneously.
Accounting for taxes is judgmental and carries a degree of uncertainty because tax law is subject to interpretation, which might be questioned by the relevant tax authority. The Group recognises the most likely current and deferred tax liability or asset, assessed for uncertainty using consistent judgments and estimates. Current and deferred tax assets are only recognised where their recovery is deemed probable and current and deferred tax liabilities are recognised at the amount that represents the best estimate of the probable outcome having regard to their acceptance by the tax authorities.

12. Financial instruments

Financial instruments are measured at fair value on initial recognition on the balance sheet.

Monetary financial assets are classified into one of the following subsequent measurement categories (subject to business model assessment and review of contractual cash flow for the purposes of sole payments of principal and interest where applicable):

- amortised cost measured under the effective interest rate method;
- fair value through other comprehensive income (FVOCI) measured at fair value, interest on effective interest rate method and change in fair value through other comprehensive income;
- mandatory fair value through profit or loss measured at fair value through profit or loss; or
- designated at fair value through profit or loss measured at fair value through profit or loss.

Classification by business model reflects how NatWest Group manages its financial assets to generate cash flows. A business model assessment helps determine the measurement approach depending on whether cash flows result from holding financial assets to collect the contractual cash flows, from selling those financial assets, or both.

Business model assessment of assets is made at portfolio level, being the level at which they are managed to achieve a predefined business objective. This is expected to result in the most consistent classification of assets because it aligns with the stated objectives of the portfolio, its risk management, manager's remuneration and the ability to monitor sales of assets from a portfolio.

The contractual terms of a financial asset; any leverage features; prepayment and extension terms; and triggers that might reset the effective rate of interest; are considered in determining whether cash flows comprise solely payments of principal and interest.

Certain financial assets may be designated at fair value through profit or loss (DFV) upon initial recognition if such designation eliminates, or significantly reduces, accounting mismatch.

Equity shares are measured at fair value through profit or loss unless specifically elected as at fair value through other comprehensive income (FVOCI).

Upon disposal, the cumulative gains or losses in fair value through other comprehensive income reserve are recycled to the income statement for monetary assets and non-monetary assets the cumulative gains or losses are transferred directly to retained earnings.

Regular way purchases of financial assets classified as amortised cost are recognised on the settlement date; all other regular way transactions in financial assets are recognised on the trade date.

Financial liabilities are classified into one of following measurement categories:

- amortised cost measured under the effective interest rate method;
- held for trading measured at fair value through profit or loss; or
- designated at fair value through profit or loss measured at fair value through profit or loss with the changes in fair value attributable to the credit risk component recognised in other comprehensive income. These are not subject to recycling to profit or loss.

13. Impairment: expected credit losses (ECL)

At each balance sheet date each financial asset or portfolio of loans measured at amortised cost or at fair value through other comprehensive income, issued financial guarantee and loan commitment is assessed for impairment and presented as impairments in the income statement. Loss allowances are forward looking, based on 12 month expected credit losses where there has not been a significant increase in credit risk (SICR) rating (refer Note 18 for details), otherwise allowances are based on lifetime expected losses.

Expected credit losses are a probability-weighted estimate of credit losses. The probability is determined by the risk of default which is applied to the cash flow estimates. In the absence of a change in credit rating, allowances are recognised when there is reduction in the net present value of expected cash flows. On a significant increase in credit risk, ECL are adjusted from 12 months to lifetime. This will lead to a higher impairment charge.

Judgment is exercised as follows:

- Models – in certain low default portfolios, Basel parameter estimates are also applied for IFRS 9.
- Non-modelled portfolios, RBSI Retail remains Basel standardised for Risk Weighted Assets, therefore modelled Probability of Default (PDs) and Loss Given Default (LGDs) are not available for calculating stage 1 and stage 2 ECLs. Instead this is undertaken by sourcing the equivalent product PD & LGD from within NatWest UK, which was identified as the closest comparable portfolio to RBSI Retail. The PD and LGD benchmarks are then used, along with the known exposure, to calculate an account level ECL.
- Multiple economic scenarios (MES) – the central, or base, scenario is most critical to the ECL calculation, independent of the method used to generate a range of alternative outcomes and their probabilities.
- Significant increase in credit risk - IFRS 9 requires that at each reporting date, an entity shall assess whether the credit risk on an account has increased significantly since initial recognition. Part of this assessment requires a comparison to be made between the current lifetime PD (i.e. the current probability of default over the remaining lifetime) with the equivalent lifetime PD as determined at the date of initial recognition.

On restructuring a financial asset without causing derecognition of the original asset the revised cash flows are used in re-estimating the credit loss. Where restructuring causes derecognition of the original financial asset, the fair value of the replacement asset is used as the closing cash flow of the original asset.

Impaired loans are written off and therefore derecognised from the balance sheet when the Group concludes that there is no longer any realistic prospect of recovery of part, or all, of the loan. For loans that are individually assessed for impairment, the timing of the write off is determined on a case by case basis. Such loans are reviewed regularly and write off will be prompted by bankruptcy, insolvency, renegotiation and similar events.

The typical time frames from initial impairment to write off for Group's collectively-assessed portfolios are:

- Retail mortgages: write off usually occurs within five years, or when an account is closed if earlier.
- Overdrafts and other unsecured loans: write off occurs within six years.
- Commercial loans: write offs are determined in the light of individual circumstances; the period does not typically exceed five years.
- Business loans are generally written off within five years.

14. Derecognition

A financial asset is derecognised when the contractual right to receive cash flows from the asset has expired or when it has been transferred and the transfer qualifies for derecognition. Conversely, an asset is not derecognised by a contract under which the Group retains substantially all the risks and rewards of ownership. If substantially all the risks and rewards have been neither retained nor transferred, the Group does not derecognise an asset over which it has retained control but limits its recognition to the extent of its continuing involvement.

A financial liability is removed from the balance sheet when the obligation is discharged, or cancelled, or expires.

15. Sale and repurchase transactions

Securities subject to sale and repurchase agreement under which substantially all the risks and rewards of ownership are retained by the Group continue to be shown on the balance sheet and the sale proceeds recorded as a financial liability. Securities acquired in a reverse sale and repurchase transaction under which the Group is not exposed to substantially all the risks and rewards of ownership are not recognised on the balance sheet and the consideration paid is recorded as a financial asset. Where Collateral supporting the transaction is received in the form of cash, deposit is recorded. Sale and repurchase transactions that are not accounted for at fair value through profit or loss are measured at amortised cost. The difference between the consideration paid or received and the repurchase or resale price is treated as interest and recognised in interest income or interest expense over the life of the transaction.

16. Netting

Financial assets and financial liabilities are offset and the net amounts presented in the balance sheet when, and only when, the Group has a legally enforceable right to set off the recognised amounts and it intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously. The Group is party to a number of arrangements, including master netting agreements, that give it the right to offset financial assets and financial liabilities but where it does not intend to settle the amounts net or simultaneously the assets and liabilities concerned are presented gross.

17. Capital instruments

The Group classifies a financial instrument that it issues as a liability if it is a contractual obligation to deliver cash or another financial asset, or to exchange financial assets or financial liabilities on potentially unfavourable terms and as equity if it evidences a residual interest in the assets of the Group after the deduction of liabilities.

18. Derivatives and hedging

Derivative financial instruments are initially recognised, and subsequently measured, at fair value. The Group's approach to determining the fair value of financial instruments is set out in the Critical accounting policies and key sources of estimation uncertainty entitled Fair value - financial instruments; further details are given in Note 7 on the accounts.

A derivative embedded in a financial liability contract is accounted for as a stand-alone derivative if its economic characteristics are not closely related to the economic characteristics of the host contract; unless the entire contract is measured at fair value with changes in fair value recognised in profit or loss.

Gains and losses arising from changes in the fair value of derivatives that are not the hedging instrument in a qualifying hedge are recognised as they arise in profit or loss. Gains and losses are recorded in Income from trading activities except for gains and losses on those derivatives that are managed together with financial instruments designated at fair value; these gains and losses are included in Other operating income. The Group enters into three types of hedge relationship: hedges of changes in the fair value of a recognised asset or liability or unrecognised firm commitment (fair value hedges); hedges of the variability in cash flows from a recognised asset or liability or a highly probable forecast transaction (cash flow hedges); and hedges of the net investment in a foreign operation (net investment hedges).

Hedge relationships are formally designated and documented at inception in line with the requirements of IAS 39 *Financial instruments – Recognition and measurement*. The documentation identifies the hedged item, the hedging instrument and details the risk that is being hedged and the way in which effectiveness will be assessed at inception and during the period of the hedge. If the hedge is not highly effective in offsetting changes in fair values or cash flows attributable to the hedged risk, consistent with the documented risk management strategy, hedge accounting is discontinued. Hedge accounting is also discontinued if RBSI Group revokes the designation of a hedge relationship.

Fair value hedge - in a fair value hedge, the gain or loss on the hedging instrument is recognised in profit or loss. The gain or loss on the hedged item attributable to the hedged risk is recognised in profit or loss and, where the hedged item is measured at amortised cost, adjusts the carrying amount of the hedged item. Hedge accounting is discontinued if the hedge no longer meets the criteria for hedge accounting; or if the hedging instrument expires or is sold, terminated or exercised; or if hedge designation is revoked. If the hedged item is one for which the effective interest rate method is used, any cumulative adjustment is amortised to profit or loss over the life of the hedged item using a recalculated effective interest rate.

Cash flow hedge - in a cash flow hedge, the effective portion of the gain or loss on the hedging instrument is recognised in other comprehensive income and the ineffective portion in profit or loss. When the forecast transaction results in the recognition of a financial asset or financial liability, the cumulative gain or loss is reclassified from equity to profit or loss in the same periods in which the hedged forecast cash flows affect profit or loss. Otherwise the cumulative gain or loss is removed from equity and recognised in profit or loss at the same time as the hedged transaction. Hedge accounting is discontinued if the hedge no longer meets the criteria for hedge accounting; if the hedging instrument expires or is sold, terminated or exercised; if the forecast transaction is no longer expected to occur; or if hedge designation is revoked. On the discontinuation of hedge accounting (except where a forecast transaction is no longer expected to occur), the cumulative unrealised gain or loss is reclassified from equity to profit or loss when the hedged cash flows occur or, if the forecast transaction results in the recognition of a financial asset or financial liability, when the hedged forecast cash flows affect profit or loss. Where a forecast transaction is no longer expected to occur, the cumulative unrealised gain or loss is reclassified from equity to profit or loss immediately.

Hedge of net investment in a foreign operation - in the hedge of a net investment in a foreign operation, the portion of foreign exchange differences arising on the hedging instrument determined to be an effective hedge is recognised in other comprehensive income. Any ineffective portion is recognised in profit or loss. Non-derivative financial liabilities as well as derivatives may be the hedging instrument in a net investment hedge. On disposal or partial disposal of a foreign operation, the amount accumulated in equity is reclassified from equity to profit or loss.

19. Cash and cash equivalents

In the cash flow statement, cash and cash equivalents comprises cash and deposits with banks with an original maturity of less than three months together with short-term highly liquid investments that are readily convertible to known amounts of cash and subject to insignificant risk of change in value.

20. Depositary assets

Assets and liabilities held in a fiduciary capacity are not included in these financial statements.

Critical accounting policies and key sources of estimation uncertainty

The reported results of the Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its accounts. IFRS require the directors, in preparing the Group's financial statements, to select suitable accounting policies, apply them consistently and make judgments and estimates that are reasonable and prudent. In the absence of an applicable standard or interpretation, IAS 8 'Accounting Policies, Changes in Accounting Estimates and Errors' requires management to develop and apply an accounting policy that results in relevant and reliable information in the light of the requirements and guidance in IFRS dealing with similar and related issues and the IASB's 'Conceptual Framework for Financial Reporting'.

The judgments and assumptions involved in the Group's accounting policies that are considered by the Board to be the most important to the portrayal of its financial condition are discussed below.

Consideration of this source of estimation uncertainty has been set out in the notes below:

Critical accounting policy	Note
Amortisation of fees	1
Pensions	4
Fair value - financial instruments	7
Loan impairment provisions	8
Provisions for liabilities and charges	15

Future Accounting developments

International Financial Reporting Standards

Effective 1 January 2022

- Onerous Contracts – Cost of Fulfilling a Contract (Amendments to IAS 37)
- Property, Plant and Equipment: Proceeds before Intended Use (Amendments to IAS 16)
- Reference to Conceptual Framework (Amendments to IFRS 3)
- Fees in the "10 per cent" test for Derecognition of Financial Liabilities (Amendments to IFRS 9)

Other new standards and amendments that are effective for annual periods beginning after 1 January 2023, with earlier application permitted, are set out below.

Effective 1 January 2023

- IFRS 17 Insurance Contracts (Amendments to IFRS 17 Insurance Contracts)
- Classification of Liabilities as Current or Non-current (Amendments to IAS 1)
- Deferred Tax related to Assets and Liabilities arising from a Single Transaction (Amendments to IAS 12)
- Disclosure of Accounting Policies (Amendments to IAS 1 and IFRS Practice Statement 2)

NatWest Group is assessing the effect of adopting these standards and amendments on its financial statements but do not expect the effect to be material.

Notes to the accounts

1. Net interest income

	Group and Bank	
	2021 £m	2020 £m
Interest receivable on assets:		
Loans to banks - amortised cost [1]	14	25
Loans to customers - amortised cost	338	330
Amounts due from holding company and fellow subsidiaries	2	5
Other financial assets- Debt Securities	38	45
Interest receivable on liabilities:		
Customer deposits	44	34
Other financial liabilities- Debt Securities	2	—
Interest receivable [2]	438	439
Interest payable on liabilities:		
Balances with banks	(1)	(2)
Customer deposits: demand	(1)	(4)
Customer deposits: savings	(9)	(1)
Customer deposits: other time	(6)	(30)
Lease liabilities	—	(1)
Amounts due to holding company and fellow subsidiaries	(5)	(6)
Interest payable on assets:		
Loans to banks - amortised cost	(31)	(22)
Amounts due to holding company and fellow subsidiaries	(1)	—
Interest payable [2]	(54)	(66)
Net interest income	384	373

(1) Includes interest received on cash balances at Central Bank.
(2) Negative interest on loans to banks is classed as interest payable and on customer deposits and debt securities is classed as interest receivable.

Interest income on financial instruments measured at amortised cost and debt instruments classified as FVOCI is measured using the effective interest rate which allocates the interest income or interest expense over the expected life of the asset or liability at the rate that exactly discounts all estimated future cash flows to equal the instrument's initial carrying amount. Calculation of the effective interest rate takes into account fees payable or receivable that are an integral part of the instrument's yield, premiums or discounts on acquisition or issue, early redemption fees and transaction costs. All contractual terms of a financial instrument are considered when estimating future cash flows. Finance lease income included in interest receivable was £3.7 million (2020: £4.7 million).

Critical accounting policies: Amortisation of fees

Until mid 2021, the RBSI Group amortises the loan arrangement fees over the contractual life of the loan for the fees above £50k and based on the behavioural life of each portfolio of loans for the arrangement fees below £50k. From mid 2021, all new arrangement fees received are amortised over the contractual life of the facility, irrespective of fee size.
The RBSI Group continues using the behavioural life approach for all fees less than 50K received pre mid 2021. The average behavioural life of 33 months was used to amortise the fees below £50k in 2021 (2020: 33 months). The average behaviour life is calculated based on the contractual life of the loans and judgment is applied to determine the appropriate length of time over which fees should be deferred and hence booked into the Income statement. The Board does not believe there is a significant risk of a material adjustment as a result of possible changes in the length of the behaviour life. This is broadly split into 4 areas being: Financial and Corporate services, Funds, Real Estate & Corporate and Commercial.

The average behavioural lives of these four areas are:

Financial and Corporate services	24 months (2020: 24 months)
Funds	20 months (2020: 20 months)
Real Estate	33 months (2020: 33 months)
Corporate and Commercial	54 months (2020: 54 months)

Interest receivable on loans to customers includes amortisation of arrangement fees of £43 million (2020: £43 million).

2. Non-interest income

	Group		Bank	
	2021 £m	2020 £m	2021 £m	2020 £m
Fees and commissions receivable				
- Payment Services	19	18	18	18
- Credit & Debit Card Fees	2	2	2	2
- Lending - (Credit Facilities)	51	30	52	30
- Trade Finance	3	3	3	3
- Investment Management	45	38	5	4
- Other services	5	4	5	4
Fees and commissions payable	(1)	(1)	(1)	(1)
Other operating income (1)	41	28	40	28
Total Non- interest income	165	122	124	88

(1) Other operating income primarily includes dealing profits previously reported under other commission in 2020.

3. Operating expenses

	Group		Bank	
	2021 £m	2020 £m	2021 £m	2020 £m
Wages, salaries and other staff costs	82	88	72	78
Temporary and contractor costs(2)	15	21	14	20
Social security costs	7	7	6	6
Restructure costs	1	14	1	14
Pension costs:				
- defined benefit schemes (see note 4)	7	6	7	5
- defined contribution schemes (see note 4)	5	3	3	3
Staff costs	117	139	103	126
Premises and equipment (1)	21	32	19	31
Provision for property costs	3	1	3	1
Depreciation, impairment and amortisation:				
- Property, plant and equipment (see note 11)	13	18	13	18
- Intangible assets (see note 12)	1	1	1	1
Other administrative expenses	96	103	87	95
Administrative expenses	134	155	123	146
Total operating expenses	251	294	226	272

(1) Includes £12 million provision for property exits in 2021.
(2) Temporary and contractor costs for 2021 are net of £2.4 million recharged to NWG as supporting NWG-wide programmes (2020 £0.1 million)

	Group		Bank	
Auditor's remuneration	2021 £'000	2020 £'000	2021 £'000	2020 £'000
Fees payable for:				
- the audit of RBSI Group's annual accounts	40	40	—	—
- the audit of RBSIH subsidiaries	1,240	1,135	1,074	1,011
- audit-related assurance services	294	239	97	84
- Other services	49	5	49	6
	1,623	1,419	1,220	1,101

Staff

The average number of persons employed by the RBSI Group during the year, excluding temporary staff was 1,398 (2020: 1,538). The average number of temporary employees during 2021 was 206 (2020: 225).

4. Pensions

Defined contribution schemes

The RBSI Group made contributions of £7.1 million to its own defined contribution schemes in 2021 (2020: £3 million).

Eligible employees of the RBSI Group can participate in membership of NWG operated pension schemes. Employees are members of The Royal Bank of Scotland Retirement Savings Plan, a defined contribution pension scheme. Detailed disclosure of the NWG pension schemes is available in the NWG Annual Report and Accounts 2021.

Defined benefit schemes

The RBSI Group sponsors two defined benefit pension schemes: one in Jersey and one in the UK. The most significant of these is The Royal Bank of Scotland International Pension Trust (RBSIPT). The assets of these schemes are independent of the RBSI Group's finances, and the schemes are each overseen by a board of trustees.

Pension fund trustees are appointed to operate each fund and ensure benefits are paid in accordance with the scheme and national law. The trustees are the legal owners of a scheme's assets, and have a duty to act in the best interest of all scheme members.

The RBSIPT operates under Jersey trust law and is managed and administered on behalf of its members in accordance with the terms of the trust deed, the scheme rules and the Jersey legislation and, where applicable, that of its constituent plans (primarily in Guernsey and the Isle of Man). There is no pension scheme funding legislation in Jersey, Guernsey or the Isle of Man.

However, statutory debt rules do apply in respect of the Isle of Man liabilities of the RBSIPT such that a debt may be due on an employer if it becomes insolvent, the scheme winds up, or, in the case of a multi-employer scheme, stops participating in the scheme while the scheme continues.

The RBSIPT's corporate trustee is RBS International Employees' Pension Trustees Limited ("RBSIEPTL"), a subsidiary of The Royal Bank of Scotland International (Holdings) Limited. RBSIEPTL is the legal owner of the RBSIPT's assets which are held separately from the assets of RBS International.

The Board of RBSIEPTL comprises two trustee directors nominated by members selected from eligible active staff and pensioner members who apply; four directors appointed by the RBSI Group; and one independent Trustee. The Board is responsible for operating the scheme in line with its formal rules and pensions law. It has a duty to act in the best interests of all scheme members, including pensioners and those who are no longer employed by RBSI, but who still have benefits in the scheme.

Merger of Isle of Man schemes into RBSIPT

Two Isle of Man defined benefit schemes previously operated by the RBSI Group were merged into the IPT on 1st March 2021, with all assets and liabilities now forming part of the IPT. The merger provides clear benefits to both the RBSI Group and to members. It also simplifies governance and reduces the operational risk and cost of running three separate pension schemes. Transferring members saw benefits from changes to some scheme terms, which resulted in an increase in the past service costs of £3.1 million. The merger was a remeasurement event under IAS 19. The outcome was a reduction of £1.2 million in pension expenses for 2021, primarily due to a higher discount rate at the point of remeasurement.

The RBSI Group has created a new contingent asset (RBSI Widows & Orphans Purpose Trust) by providing an additional £5.35 million in funding which will be kept separate in the Trust held for 20 years. It will be payable to members on RBS International Ltd.'s insolvency or the wind up of the RBSIPT, and if not used will revert to the RBSI Group after 20 years.

Investment strategy

The assets of both schemes are invested in a diversified portfolio of quoted equities, government and corporate fixed-interest and index-linked bonds. The RBSIPT equity holdings are held in passive pooled funds managed by State Street. The Trustee's investment benchmark is for the majority to be invested in global developed markets, with a small proportion invested in emerging markets.

The RBSIPT employs both physical and derivative instruments to achieve a desired asset class exposure and to reduce the scheme's interest rate, inflation and currency risk. This means that the net funding position is considerably less sensitive to changes in market conditions than the value of the assets or liabilities in isolation. In particular, the Trustee hedges movements in interest rates and inflation.

	Group and Bank					
	2021			2020		
Major classes of plan assets as a weighted percentage of total plan assets of the schemes	Quoted %	Unquoted %	Total %	Quoted %	Unquoted %	Total %
Equities	23.4%	—	23.4%	21.8%	—	21.8%
Index-linked bonds	47.1%	—	47.1%	51.8%	—	51.8%
Government fixed interest bonds	10.6%	—	10.6%	5.3%	—	5.3%
Corporate and other bonds	16.4%	—	16.4%	16.9%	—	16.9%
Hedge funds	—	—	—	—	—	—
Property	—	—	—	—	2.5%	2.5%
Derivatives	—	—	—	—	—	—
Cash and other assets	—	2.5%	2.5%	—	1.7%	1.7%
	97.5%	2.5%	100.0%	95.8%	4.2%	100.0%

4. Pensions continued

Changes in value of net pension asset/(liability)	Group and Bank All schemes Fair value of plan assets £m	Present value of defined benefit obligations £m	Asset Ceiling (1) £m	Net pension asset £m
At 1 January 2020	969	(780)	(42)	147
Income statement	19	(24)	(1)	(6)
Statement of comprehensive income	141	(122)	4	23
Contributions by employer	9	—	—	9
Benefits paid	(62)	62	—	—
At 1 January 2021	1,076	(864)	(39)	173
Currency translation and other adjustments	—	—	(1)	(1)
Income statement:				
Interest income	18	(14)	—	4
Interest expense	—	(8)	—	(8)
Current service cost	—	(3)	—	(3)
Expenses	—	—	—	—
	18	(25)	—	(7)
Statement of comprehensive income:				
Actuarial gains due to experience gains	38	13	—	51
Actuarial losses due to changes in financial assumptions	—	(28)	—	(28)
Actuarial losses due to changes in demographic assumptions	—	(3)	—	(3)
Asset ceiling adjustment	—	—	14	14
	38	(18)	14	34
Contributions by employer	7	—	—	7
Benefits paid	(57)	57	—	—
At 31 December 2021	1,082	(850)	(26)	206

(1) Defined benefit obligations are subject to annual valuation by independent actuaries.
(2) In recognising the net surplus or deficit of a pension scheme, the funded status of each scheme is adjusted to reflect any minimum funding requirement imposed on the sponsor and any ceiling on the amount that the sponsor has an unconditional right to recover from a scheme.
(3) The RBSI Group expects to make contributions to the RBSIPT of £3.9 million in 2022.

4. Pensions continued

Amounts recognised on the balance sheet	Group and Bank 2021 £m	2020 £m
Fund assets at fair value	1,082	1,076
Present value of fund liabilities	(850)	(864)
Funded status	232	212
Asset ceiling	(26)	(39)
	206	173

Net pension asset/(liability) comprises	Group and Bank 2021 £m	2020 £m
Net assets of schemes in surplus - IPT	206	171
Net assets of schemes in surplus - UK Scheme	26	25
Net assets of schemes in surplus - IOMB	—	16
Asset ceiling - UK Scheme	(26)	(25)
Asset ceiling - IOMB	—	(14)
	206	173

Funding and contributions by the RBSI Group

In the UK, the Trustees of defined benefit pension schemes are required to perform funding valuations every three years. The Trustees and the sponsor, with the support of the scheme actuary, agree the assumptions used to value the liabilities and determine further contribution requirements. The funding assumptions incorporate a margin for prudence over and above the expected cost of providing the benefits promised to members, taking into account the sponsor's covenant and the investment strategy of the scheme.

The last triennial funding valuation of the RBSIPT was as at 31 March 2021. This determined the funding level of the RBSIPT to be 101%, based on pension liabilities of £894 million. No further deficit contributions are due.

Critical accounting policy: Pensions

The assets of defined benefit schemes are measured at their fair value at the balance sheet date. Scheme liabilities are measured using the projected unit method, which takes account of projected earnings increases, using actuarial assumptions that give the best estimate of the future cash flows that will arise under the scheme liabilities. These cash flows are discounted at an interest rate based on the yields of high-quality corporate bonds of appropriate duration, with high-quality almost universally understood to mean AA-rated.

The choice of discount rate is a source of estimation uncertainty, due to a lack of appropriate UK denominated AA-rated bonds of equivalent duration to the pension schemes' liabilities.

The approach used is to fit a yield curve to an appropriate dataset of AA bonds, and derive the discount rate from that curve.

To increase the number of reference bonds available at the end of the reporting period, equivalent AA yields were extrapolated for longer dated A and AAA rated bonds by applying a credit spread adjustment to their actual yields. These were then included in the dataset used to create the yield curve.

Accounting assumptions

Placing a value on the RBSI Group's defined benefit pension schemes' liabilities requires the RBSI Group's management to make a number of assumptions, with the support of independent actuaries who provide advice and guidance. In determining the value of scheme liabilities, financial and demographic assumptions are made as to price inflation, pension increases, earnings growth and employee life expectancy. A range of assumptions could be adopted in valuing the schemes' liabilities. The ultimate cost of the defined benefit obligations to the RBSI Group will depend upon actual future events and the assumptions made are unlikely to be exactly borne out in in practice, meaning the final cost may be higher or lower than expected.

A year end valuation of the RBSI Group's pension schemes was prepared to 31 December 2021 by independent actuaries, using the following assumptions for the material pension schemes:

	Group and Bank 2021	2020
Discount rate	1.80%	1.40%
Rate of increase in salaries	1.75%	1.75%
Rate of increase in pensions in payment	3.25%	2.36%
Rate of increase in deferred pensions	3.65%	3.00%
Inflation assumption	3.65%	2.85%

Post–retirement mortality assumptions	2021	2020
Longevity at age 60 for current pensioners aged 60 (years)		
Males	28.7	28.3
Females	30.0	29.9
Longevity at age 60 for future pensioners currently aged 40 (years)		
Males	30.2	29.8
Females	31.5	31.4

4. Pensions continued

These post-retirement mortality assumptions are derived from standard mortality tables used by the scheme actuary to value the liabilities for the main scheme.

The weighted average duration of the RBSI Group's defined benefit obligation is 22.6 years (2020: 24 years).

Discount rate

The IAS 19 valuation uses a single discount rate set by reference to the yield on a basket of 'high quality' sterling corporate bonds. Significant judgment is required when setting the criteria for bonds to be included in the basket of bonds that determines the discount rate used in the IAS 19 valuations. The criteria include issue size, quality of pricing and the exclusion of outliers. Judgment is also required in determining the shape of the yield curve at long durations: a constant credit spread relative to gilts is assumed. Sensitivity to the main assumptions is presented below:

	Group and Bank			
	(Decrease)/increase in pension cost for the year		(Decrease)/increase in obligation at 31 December	
	2021 £m	2020 £m	2021 £m	2020 £m
0.25% increase in the discount rate	(2)	(2)	(42)	(52)
0.25% increase in inflation	1	1	29	40
0.25% additional rate of increase in pensions in payment	1	—	30	25
0.25% additional rate of increase in deferred pensions	—	—	12	15
0.25% additional rate of increase in salaries	—	—	1	3
Longevity increase of one year	1	1	33	32

Pension liabilities are calculated on the central assumptions and under the relevant sensitivity scenarios. The sensitivity to pension liabilities is the difference between these calculations.

The sensitivity analysis presented above may not be representative of the actual change in the defined benefit obligation as it is unlikely that the changes in assumptions would occur in isolation of one another as some of the assumptions may be correlated.

The experience history of the scheme is shown below.

	Group and Bank				
History of defined benefit schemes	2021 £m	2020 £m	2019 £m	2018 £m	2017 £m
Fair value of plan assets	1,082	1,076	969	786	789
Present value of plan obligations	(850)	(864)	(780)	(672)	(725)
Fund status	232	212	189	114	64
Asset ceiling	(26)	(39)	(42)	(49)	(17)
Net surplus	206	173	147	65	47
Experience gains/(losses) on plan liabilities	13	5	(2)	32	7
Experience gains/(losses) on plan assets	38	141	106	(53)	44
Actual return on pension scheme assets	56	160	128	(33)	66

5. Tax

	Group		Bank	
	2021 £m	2020 £m	2021 £m	2020 £m
Current tax:				
Charge for the year	54	22	51	20
Over provision in respect of prior years	(3)	—	(2)	—
	51	22	49	20
Deferred tax:				
Charge for the year	3	3	3	3
Prior year adjustment	—	1	—	1
Tax charge for the year	54	26	52	24

The actual tax charge differs from the expected tax charge computed by applying the standard rate of income tax as follows: Jersey, Guernsey, Isle of Man and Gibraltar 10% (2020: 10%), UK 27% (2020: 27%), Luxembourg 24.94% (2020: 24.94%) and Natwest Trustee And Depositary Services Limited (NWTDS) 19% (2020: 19%).

	Group		Bank	
	2021 £m	2020 £m	2021 £m	2020 £m
Expected tax charge	36	9	33	8
Non-deductible items	—	6	—	7
Deferred tax	—	3	—	—
Rate differences on current tax	21	7	21	8
Adjustments in respect of prior years	(3)	1	(2)	1
Actual tax charge	54	26	52	24

Deferred tax

	Group and Bank	
	2021 £m	2020 £m
Deferred tax assets	5	3
Deferred tax liabilities	(24)	(19)
Net deferred tax liabilities	(19)	(16)

	Group and Bank			
	Pension £m	Accelerated capital allowances £m	Other £m	Total £m
At 1 January 2020	(15)	(2)	8	(9)
Charge to income statement	—	—	(4)	(4)
Charge to other comprehensive income	(2)	—	(1)	(3)
At 1 January 2021	(17)	(2)	3	(16)
Charge to income statement	—	—	(3)	(3)
Charge to other comprehensive income	(4)	—	4	—
At 31 December 2021	(21)	(2)	4	(19)

6. Derivatives

Companies within the RBSI Group transact derivatives as principal to manage balance sheet foreign exchange and interest rate risk.

	Group and Bank					
	2021			2020		
	Notional £m	Assets £m	Liabilities £m	Notional £m	Assets £m	Liabilities £m
Exchange rate contracts						
Spots and forwards - NatWest Group	6,098	18	42	4,549	32	65
Spots and forwards - third party	699	9	5	1,030	8	17
Interest rate swaps						
NatWest Group	5,477	131	70	1,729	1	44
	12,274	158	117	7,308	41	126

The RBSI Group applies hedge accounting to manage interest rate risk.

RBSI Group's interest rate hedging relate to the management of non-trading structural interest rate risk, caused by the mismatch between fixed interest rates and floating interest rates. The RBSI Group manages this risk within approved limits. Residual risk positions are hedged with derivatives principally interest rate swaps. Suitable larger financial instruments are fair value hedged, the remaining exposure, where possible, is hedged by derivatives documented as cash flow hedges.

Cash flow hedges of interest rate risk relate to exposures to the variability in future interest payments and receipts due to the movement of benchmark interest rates on forecast transactions and on recognised financial assets and financial liabilities. This variability in cash flows is hedged by interest rate swaps, fixing the hedged cash flows. For these cash flow hedge relationships, the hedged items are actual and forecast variable interest rate cash flows arising from financial assets and financial liabilities with interest rates linked to the relevant benchmark rate LIBOR, EURIBOR, SONIA or the Bank of England Official Bank Rate. The variability in cash flows due to movements in the relevant benchmark rate is hedged, this risk component is identified using the risk management systems of the RBSI Group. This risk component comprises the majority of cash flow variability risk.

Fair value hedges of interest rate risk involve interest rate swaps transforming the fixed interest rate risk in recognised financial assets and financial liabilities to floating. The hedged risk is the risk of changes in the hedged items fair value attributable to changes in the benchmark interest rate embedded in the hedged item. The significant embedded benchmarks are LIBOR, EURIBOR and SONIA. This risk component is identified using the risk management systems of the group. This risk component comprises the majority of the hedged items fair value risk.

For all cash flow hedging and fair value hedge relationships the RBSI Group determines that there is an adequate level of offsetting between the hedged item and hedging instrument via assessing the initial and ongoing effectiveness by comparing movements in the fair value of the expected highly probable forecast interest cash flows fair value of the hedged item attributable to the hedged risk with movements in the fair value of the expected changes in cash flows from the hedging interest rate swap. Hedge ineffectiveness is measured and recognised in the income statement as it arises.

IBOR reform – During the year, the RBSI Group continued to apply, for relationships directly affected by interest rate benchmark reform, Interest Rate Benchmark Reform Amendments to IAS 39 and IFRS 7 issued September 2019 ("Phase 1 relief") and Interest Rate Benchmark Reform – Phase 2 Amendments to IAS 39 and IFRS 7 issued August 2020 ("Phase 2 relief"). For additional information relating to IBOR reform, and its impact on the RBSI Group, refer to Note 7.

Included in the table on previous page are derivatives held for hedging purposes as follows:

	Group and Bank							
	2021				2020			
	Notional £m	Assets £m	Liabilities £m	Changes in fair value used for hedge ineffectiveness (1) £m	Notional £m	Assets £m	Liabilities £m	Changes in fair value used for hedge ineffectiveness (1) £m
Fair Value hedging								
Interest rate contracts	2,074	96	26	138	1,388	—	40	(23)
Cash flow hedging								
Interest rate contracts	1,379	—	38	(40)	277	1	—	1

(1) The change in fair value used for hedge ineffectiveness includes instruments that were derecognised in the year.

6. Derivatives continued

The notional of hedging instruments affected by interest rate benchmark reform is as follows:

	Group and Bank 2021 £m	2020 £m
Fair Value hedging		
- LIBOR	—	265
- EURIBOR (1)	—	69
- USD LIBOR (2)	291	9
	291	343
Cash flow hedging		
- USD LIBOR (2)	37	22
- BOE Base rate (3)	—	100
	37	122

(1) In 2021 management concluded that EURIBOR is not expected to be significantly reformed further and therefore any uncertainty due to interest benchmark rate reform for EURIBOR has ended.
(2) In 2021 the FCA declared that USD LIBOR will be non-representative post 30 June 2023; at the time of preparing the 2020 disclosures this date was expected to be 31 December 2021.
(3) Hedge relationships subject to reform are those where either the hedged item or the hedging instrument is subject to the IBOR reform.

The following table shows the period in which the hedging contract ends:

	Group and Bank						
2021	0-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m	> 20 years £m	Total £m
Fair Value hedging							
Hedging assets - interest rate risk	106	308	288	108	579	685	2,074
Hedging liabilities - interest rate risk	—	—	—	—	—	—	—
Cash flow hedging							
Hedging assets - interest rate risk	—	185	1,009	185	—	—	1,379
Average fixed interest rate (%)	—	0.29	0.29	0.48	—	—	0.32

	Group and Bank						
2020	0-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m	> 20 years £m	Total £m
Fair Value hedging							
Hedging assets - interest rate risk	—	285	60	388	441	214	1,388
Hedging liabilities - interest rate risk	—	—	—	—	—	—	—
Cash flow hedging							
Hedging assets - interest rate risk	—	5	172	100	—	—	277
Average fixed interest rate (%)	—	(0.07)	0.10	0.27	—	—	0.16

The table below analyses assets and liabilities subject to hedging derivatives:

	Group and Bank		
2021	Carrying value of hedged assets and liabilities £m	Impact on hedged items included in carrying value £m	Change in fair value used as a basis to determine ineffectiveness (1) £m
Fair Value hedging - interest rate			
Loans to customers - amortised cost	651	7	(15)
Other financial assets - securities	1,631	(81)	(123)
Total	2,282	(74)	(138)
Cash flow hedging - interest rate			
Loans to customers - amortised cost	1,395	—	40
2020			
Fair Value hedging - interest rate			
Loans to customers - amortised cost	389	22	23
Other financial assets - securities	1,089	14	—
Total	1,478	36	23
Cash flow hedging - interest rate			
Loans to customers - amortised cost	285	—	(1)

Comparatives have been re-presented to aid comparability.
(1) The change in fair value used for hedge ineffectiveness instruments derecognised in the year.

6. Derivatives continued

The following risk exposures will be affected by interest rate benchmark reform (notional, hedged adjustment):

	Group and Bank	
2021	Notional £m	Hedged adjustment £m
Fair Value hedging		
- USD LIBOR (2)	291	(6)
	291	(6)
Cash flow hedging		
- USD LIBOR (2)	37	1
	37	1
2020		
Fair Value hedging		
- LIBOR	265	22
- EURIBOR (1)	69	1
- USD LIBOR (2)	9	—
	343	23
Cash flow hedging		
- USD LIBOR (2)	22	—
- BOE Base rate	100	—
	122	—

(1) In 2021 management concluded that EURIBOR is not expected to be significantly reformed further and therefore any uncertainty due to interest benchmark rate reform for EURIBOR has ended.
(2) In 2021 the FCA declared that USD LIBOR will be non-representative post 30 June 2023; at the time of preparing the 2020 disclosures this date was expected to be 31 December 2021.
(3) Hedge relationships subject to reform are those where either the hedged item or the hedging instrument is subject to the IBOR reform.

The following shows analysis of cash flow hedging reserve:

	Group and Bank 2021 £m	2020 £m
Continuing		
Cash flow hedging-interest rate risk	(40)	1

	Group and Bank 2021 £m	2020 £m
Interest rate risk		
Amount recognised in equity	—	1

Hedge ineffectiveness recognised in other operating income comprises:

	Group and Bank 2021 £m	2020 £m
Fair Value hedging		
(Losses)/gains on the hedged items attributable to the hedged risk	(138)	23
Gains/(losses) on the hedging instruments	138	(23)
Fair value hedging ineffectiveness	—	—
Cash flow hedging		
- interest rate risk	—	—
Cash flow hedging ineffectiveness	—	—

The main sources of ineffectiveness for interest rate risk hedge accounting relationships are:

- The effect of the counterparty credit risk on the fair value of the interest rate swap, which is not reflected in the fair value of the hedged item attributable to the change in interest rate (fair value hedge).
- Differences in the repricing basis between the hedging instrument and hedged cash flows (cash flow hedge).
- Upfront present values on the hedging derivatives where hedge accounting relationships have been designated after the trade date (cash flow hedge and fair value hedge).

7. Financial instruments - classification

The following tables analyse financial assets and financial liabilities in accordance with the categories of financial instruments on an IFRS 9 basis.

	Group				
2021	MFVTPL £m	FVOCI £m	Amortised cost £m	Other assets £m	Total £m
Assets					
Cash and balances at central banks			17,220		17,220
Derivatives	158				158
Loans to banks - amortised cost [1]			1,305		1,305
Loans to customers - amortised cost [1] [2]			15,463		15,463
Amounts due from holding companies and fellow subsidiaries	—	—	579	—	579
Other financial assets	—	3,134	2,789		5,923
Intangible assets				28	28
Other assets				330	330
	158	3,134	37,356	358	41,006

	Held-for-trading £m	Amortised cost £m	Other liabilities £m	Total £m
Liabilities				
Banks deposits [1]		266		266
Customer deposits [1]		37,539		37,539
Derivatives	117			117
Other financial liabilities	17	459		476
Amounts due to holding companies and fellow subsidiaries	—	242	—	242
Other liabilities [3]		38	111	149
	134	38,544	111	38,789

2020	MFVTPL £m	FVOCI £m	Amortised cost £m	Other assets £m	Total £m
Assets					
Cash and balances at central banks			13,531		13,531
Derivatives	41				41
Loans to banks - amortised cost [1]			1,231		1,231
Loans to customers - amortised cost [1] [2]			13,262		13,262
Amounts due from holding companies and fellow subsidiaries	—	—	637	—	637
Other financial assets	—	1,796	3,567		5,363
Intangible assets				14	14
Other assets				284	284
	41	1,796	32,228	298	34,363

	Held-for-trading £m	Amortised cost £m	Other liabilities £m	Total £m
Liabilities				
Banks deposits [1]	2	3		5
Customer deposits [1]		31,280		31,280
Derivatives	126			126
Other financial liabilities		542		542
Amounts due to holding companies and fellow subsidiaries	—	236	—	236
Other liabilities [3]		40	118	158
	128	32,101	118	32,347

Refer to the following page for footnotes.

7. Financial instruments – classification continued

2021	MFVTPL £m	FVOCI £m	Bank Amortised cost £m	Other assets £m	Total £m
Assets					
Cash and balances at central banks			17,220		17,220
Derivatives	158		—		158
Loans to banks - amortised cost (1)			1,278		1,278
Loans to customers - amortised cost (1) (2)			15,463		15,463
Amounts due from holding companies and fellow subsidiaries	—	—	579	7	586
Other financial assets		3,134	2,789		5,923
Intangible assets				14	14
Other assets				319	319
	158	3,134	37,329	340	40,961

	Held-for-trading £m	Amortised cost £m	Other liabilities £m	Total £m
Liabilities				
Banks deposits (1)		266		266
Customer deposits (1)		37,539		37,539
Derivatives	117			117
Other financial liabilities	17	459		476
Amounts due to holding companies and fellow subsidiaries	—	308	—	308
Other liabilities (3)		38	105	143
	134	38,610	105	38,849

2020	MFVTPL £m	FVOCI £m	Amortised cost £m	Other assets £m	Total £m
Assets					
Cash and balances at central banks			13,531		13,531
Derivatives	41		—		41
Loans to banks - amortised cost (1)			1,204		1,204
Loans to customers - amortised cost (1) (2)			13,262		13,262
Amounts due from holding companies and fellow subsidiaries	—	—	646	—	646
Other financial assets		1,796	3,567		5,363
Intangible assets				8	8
Other assets				278	278
	41	1,796	32,210	286	34,333

	Held-for-trading £m	Amortised cost £m	Other liabilities £m	Total £m
Liabilities				
Banks deposits (1)	2	3		5
Customer deposits (1)		31,280		31,280
Derivatives	126			126
Other financial liabilities		542		542
Amounts due to holding companies and fellow subsidiaries	—	322	—	322
Other liabilities (3)		40	115	155
	128	32,187	115	32,430

(1) The RBSI Group and the Bank balance sheet lines include instruments that are subject to IAS 32 netting, or contracts covered by legally enforceable master netting agreements with the right to offset assets and liabilities with the same counterparty, subject to certain conditions. Netting applied primarily relates to IAS 32 netting for reverse repo and repo contracts. Total netting adjustments recorded are:
   a. Loans to banks and bank deposits: £1,262 million (2020: £1,017 million).
   b. Loans to customers and customer deposits: £264 million (2020: nil).

(2) Includes RBSI Group and Bank finance lease receivables of £59 million (2020 - £72 million).

(3) Includes RBSI Group and Bank lease liabilities of £37 million (2020: £40 million), held at amortised cost.

7. Financial instruments – classification continued

Interest rate benchmark reform

The NWG IBOR program successfully delivered the conversion of the vast majority of the IBOR exposures to risk free rates (RFR) in advance of the cessation date. This encompasses loans, deposits, capital instruments and derivatives, which, have been converted using fallback provisions, switch provisions or as part of market-wide conversion events in the case of derivatives subject to clearing. These instruments will convert at the first repricing date post cessation.

The total amount of exposure for RBSI Group and Bank at 31 December 2021, subject to above conversion provisions is £413 million of assets and £1,570 million of loan commitment.

Despite the above, certain instruments remain in discussion with customers and counterparties to achieve consensual conversion. If consensual conversion is not achieved these instruments will default to synthetic LIBOR in line with relevant legislation.

The level of exposures without explicit or agreed conversion provisions as of 31 December 2021 is as follows:

	Group and Bank			
	Rate subject to IBOR reform			
2021	GBP LIBOR £m	USD IBOR (1) £m	Other IBOR (2) £m	Total £m
Loans to customers - amortised cost	2,132	68	261	2,461
Loan commitments (2)	30	407	—	437
Derivatives notional	—	—	—	—

	Group and Bank				
	Rate subject to IBOR reform				
2020	GBP LIBOR £m	USD IBOR (1) £m	EURIBOR (2) £m	Other IBOR £m	Total £m
Loans to customers - amortised cost	3,341	825	1,750	131	6,047
Loan commitments (3)	1,690	706	—	—	2,396
Derivatives notional	377	31	69	—	477

(1) In 2021 the FCA declared that USD IBOR will be non-representative post 30 June 2023; at the time of preparing the 2020 disclosures this date was expected to be 31 December 2021.

(2) In 2021 management concluded that EURIBOR is not expected to be significantly reformed further and therefore any uncertainty due to interest benchmark rate reform for EURIBOR has ended. December 2020 data includes EURIBOR exposure as subject to reform

(3) Certain loan commitments are multi-currency facilities. Where these are fully undrawn, they are allocated to the principal currency of the facility. Where the facilities are partly drawn, the remaining loan commitment is allocated to the currency with the largest drawn amount.

7. Financial instruments – classification continued

AT1 issuances

The RBSI Group has also issued certain capital instruments (AT1) within RBSI under which reset clauses are linked to IBOR rates subject to reform. Where under the contractual terms of the instrument the coupon reset to a rate which has IBOR as a specified component of its pricing structure these are subject to IBOR reform and are shown in note 16.

Financial instruments - valuation

Critical accounting policy: Fair value - financial instruments

In accordance with accounting policies 12 and 18, financial instruments classified as mandatory fair value through profit or loss and financial assets classified as fair value through other comprehensive income are recognised in the financial statements at fair value. All derivatives are measured at fair value.
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 measurement date. A fair value measurement takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. It also uses the assumptions that market participants would use when pricing the asset or liability. In determining fair value the RBSI Group maximises the use of relevant observable inputs and minimises the use of unobservable inputs.

Modelled approaches may be used to measure instruments classed as level 2 or 3. Estimation expertise is required in the selection, implementation and calibration of appropriate models. The resulting modelled valuations are considered for accuracy and reliability. Portfolio level adjustments consistent with IFRS 13 are raised to incorporate counterparty credit risk, funding and margining risks. Expert judgment is used in the initial measurement of modelled products by control teams.

Where the RBSI Group manages a group of financial assets and financial liabilities on the basis of its net exposure to either market risks or credit risk, it measures the fair value of a group of financial assets and financial liabilities on the basis of the price that it would receive to sell a net long position (i.e. an asset) for a particular risk exposure or to transfer a net short position (i.e. a liability) for a particular risk exposure in an orderly transaction at the measurement date under current market conditions.

Credit valuation adjustments are made when valuing derivative financial assets to incorporate counterparty credit risk. Adjustments are also made when valuing financial liabilities measured at fair value to reflect the RBSI Group's own credit standing.

Where the market for a financial instrument is not active, fair value is established using a valuation technique. These valuation techniques involve a degree of estimation, the extent of which depends on the instrument's complexity and the availability of market-based data. Further details about the valuation methodologies and the sensitivity to reasonably possible alternative assumptions of the fair value of financial instruments valued using techniques where at least one significant input is unobservable are given below.

Fair Value Hierarchy

Financial instruments carried at fair value have been classified under the IFRS fair value hierarchy as follows:

Level 1 – Instruments valued using unadjusted quoted prices in active and liquid markets, for identical financial instruments. Examples include government bonds, listed equity shares and certain exchange-traded derivatives.

Level 2 - Instruments valued using valuation techniques that have observable inputs. Examples include most government agency securities, investment-grade corporate bonds, certain mortgage products, including collateralised loan obligations (CLO), most bank loans, repos and reverse repos, less liquid listed equities, state and municipal obligations, most notes issued, certain money market securities, loan commitments and most over-the-counter (OTC) derivatives.

Level 3 - Instruments valued using a valuation technique where at least one input, which could have a significant effect on the instrument's valuation, is not based on observable market data. Examples include cash instruments which trade infrequently, certain syndicated and commercial mortgage loans, certain emerging markets and derivatives with unobservable model inputs.

Valuation techniques

The RBSI Group derives fair value of its instruments differently depending on whether the instrument is a non-modelled or a modelled product.

Non-modelled products are valued directly from a price input typically on a position by position basis and include cash, equities and most debt securities.

Modelled products valued using a pricing model range in complexity from comparatively vanilla products such as interest rate swaps and options (e.g. interest rate caps and floors) through to more complex derivatives. The valuation of modelled products requires an appropriate model and inputs into this model. Sometimes models are also used to derive inputs (e.g. to construct volatility surfaces). The RBSI Group uses a number of modelling methodologies.

7. Financial instruments – valuation

	Group and Bank					
	2021			2020		
	Level 1	Level 2	Total	Level 1	Level 2	Total
	£m	£m	£m	£m	£m	£m
Assets						
Derivatives	—	158	158	—	41	41
Other financial assets - securities	3,134	—	3,134	1,795	1	1,796
Total financial assets at fair value	3,134	158	3,292	1,795	42	1,837
Liabilities						
Bank deposits	—	11	11	—	2	2
Customer deposits	—	6	6	—	—	—
Derivatives	—	117	117	—	126	126
Total financial liabilities at fair value	—	134	134	—	128	128

Inputs to valuation models

Values between and beyond available data points are obtained by interpolation and extrapolation. When utilising valuation techniques, the fair value can be significantly affected by the choice of valuation model and by underlying assumptions concerning factors such as the amounts and timing of cash flows, discount rates and credit risk. The principal inputs to these valuation techniques are as follows:

Bond prices - quoted prices are generally available for government bonds, certain corporate securities and some mortgage-related products.

Credit spreads - where available, these are derived from prices of credit default swaps or other credit based instruments, such as debt securities. For others, credit spreads are obtained from third party benchmarking services.

Interest rates - these are principally benchmark interest rates such as the London Inter-Bank Offered Rate (LIBOR) and quoted interest rates in the swap, bond and futures.

Equity and equity index prices – quoted prices are generally readily available for equity shares listed on the world's major stock exchanges major indices on such shares.

Commodity prices - many commodities are actively traded in spot and forward contracts and futures on exchanges in London, New York and other commercial centres.

Price volatilities and correlations - volatility is a measure of the tendency of a price to change with time. Correlation measures the degree which two or more prices or other variables are observed to move together.

Prepayment rates - the fair value of a financial instrument that can be prepaid by the issuer or borrower differs from that of an instrument that cannot be prepaid. In valuing prepayable instruments that are not quoted in active markets, the RBSI Group considers the value of the prepayment option.

Recovery rates/loss given default - these are used as an input to valuation models and reserves for asset-backed securities and other credit products as an indicator of severity of losses on default. Recovery rates are primarily sourced from market data providers or inferred from observable credit spreads.

7. Financial instruments – valuation continued

Fair value of Financial Instruments not carried at fair value

The following table shows the carrying values and the fair values of financial instruments on the balance sheet carried at amortised cost. All assets and liabilities carried at amortised cost on the balance sheet fall within level 3 (except other financial assets that fall within level 1, and other financial liabilities that fall within level 2), of the valuation methodologies.

	Group			
	2021 Carrying value £m	2021 Fair value £m	2020 Carrying value £m	2020 Fair value £m
Financial assets				
Cash and balances at central banks	17,220	17,220	13,531	13,531
Loans to banks - amortised cost	1,305	1,305	1,231	1,231
Loans to customers - amortised cost	15,463	15,336	13,262	13,204
Amounts due from holding companies and fellow subsidiaries	579	579	637	637
Other financial assets	2,789	2,793	3,567	3,662
Financial liabilities				
Bank deposits	266	266	3	3
Customer deposits	37,539	37,539	31,280	31,280
Other financial liabilities	459	459	542	542
Amounts due to holding companies and fellow subsidiaries	242	242	236	236

	Bank			
	2021 Carrying value £m	2021 Fair value £m	2020 Carrying value £m	2020 Fair value £m
Financial assets				
Cash and balances at central banks	17,220	17,220	13,531	13,531
Loans to banks - amortised cost	1,278	1,278	1,204	1,204
Loans to customers - amortised cost	15,463	15,336	13,262	13,204
Amounts due from holding companies and fellow subsidiaries	577	577	646	646
Other financial assets	2,789	2,793	3,567	3,662
Financial liabilities				
Bank deposits	266	266	3	3
Customer deposits	37,539	37,539	31,280	31,280
Other financial liabilities	459	459	542	542
Amounts due to holding companies and fellow subsidiaries	308	308	322	322

7. Financial instruments - valuation continued

The 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 measurement date. Quoted market values are used where available, otherwise, fair values have been estimated based on discounted expected future cash flows and other valuation techniques. These techniques involve uncertainties and require assumptions and judgments covering prepayments, credit risk and discount rates. Changes in these assumptions would significantly affect estimated fair values. The fair values reported would not necessarily be realised in an immediate sale or settlement.

The assumptions and methodologies underlying the calculation of fair values of financial instruments at the balance sheet date are as follows:

Short term financial instruments

For certain short-term financial instruments: cash and balances at central banks, items in the course of collection from other banks, settlement balances, items in the course of transmission to other banks, customer demand deposits and notes in circulation, carrying value is a reasonable approximation of fair value.

Loans to banks and customers

In estimating the fair value of net loans to customers and banks measured at amortised cost, the RBSI Group's loans are segregated into appropriate portfolios reflecting the characteristics of the constituent loans.

Two principal methods are used to estimate fair value:

(a) Contractual cash flows are discounted using a market discount rate that incorporates the current spread for the borrower or where that is not observable, the spread for borrowers of a similar credit standing.

(b) Expected cash flows (unadjusted for credit losses) are discounted at the current offer rate for the same or similar products.

Other financial assets

The majority of other financial assets consist of debt securities which are valued using quoted prices in active markets, or using quoted prices for similar assets in active markets. Fair values of the rest are determined using discounted cash flow valuation techniques.

Deposits by banks and customer accounts

The fair values of deposits are estimated using discounted cash flow valuation techniques.

Debt securities in issue

Fair values are determined using quoted prices for similar liabilities where available or by reference to valuation techniques, adjusting for own credit spreads where appropriate.

7. Financial instruments - maturity analysis

Remaining maturity

The following table shows the residual maturity of financial instruments based on contractual date of maturity.

	Group					
	2021			2020		
	Less than 12 months £m	More than 12 months £m	Total £m	Less than 12 months £m	More than 12 months £m	Total £m
Assets						
Cash and balances at central banks	17,220	—	17,220	13,531	—	13,531
Derivatives	25	133	158	38	3	41
Loans to banks - amortised cost	1,305	—	1,305	1,231	—	1,231
Loans to customers - amortised cost	6,906	8,557	15,463	4,911	8,351	13,262
Amounts due from holding companies and fellow subsidiaries	579	—	579	637	—	637
Other financial assets	2,160	3,763	5,923	1,260	4,103	5,363
Liabilities						
Banks deposits	266	—	266	5	—	5
Customer deposits	37,536	3	37,539	31,277	3	31,280
Derivatives	46	71	117	81	45	126
Other financial liabilities	476	—	476	542	—	542
Lease liabilities	4	33	37	4	36	40
Amounts due to holding companies and fellow subsidiaries	242	—	242	236	—	236

	Bank					
	2021			2020		
	Less than 12 months £m	More than 12 months £m	Total £m	Less than 12 months £m	More than 12 months £m	Total £m
Assets						
Cash and balances at central banks	17,220	—	17,220	13,531	—	13,531
Derivatives	25	133	158	38	3	41
Loans to banks - amortised cost	1,278	—	1,278	1,204	—	1,204
Loans to customers - amortised cost	6,906	8,557	15,463	4,911	8,351	13,262
Amounts due from holding companies and fellow subsidiaries	579	—	579	646	—	646
Other financial assets	2,160	3,763	5,923	1,260	4,103	5,363
Liabilities						
Banks deposits	266	—	266	5	—	5
Customer deposits	37,536	3	37,539	31,277	3	31,280
Derivatives	46	71	117	81	45	126
Other financial liabilities	476	—	476	542	—	542
Lease liabilities	4	33	37	4	36	40
Amounts due to holding companies and fellow subsidiaries	308	—	308	332	—	332

7. Financial instruments - maturity analysis continued

Assets and liabilities by contractual cash flows up to 20 years

The tables on the following page, show the contractual undiscounted cash flows receivable and payable, up to a period of 20 years, including future receipts and payments of interest of financial assets and liabilities by contractual maturity. The balances in the following tables do not agree directly with the consolidated balance sheet, as the tables include all cash flows relating to principal and future coupon payments, presented on an undiscounted basis. The tables have been prepared on the following basis:

Financial assets have been reflected in the time band of the latest date on which they could be repaid, unless earlier repayment can be demanded by the RBSI Group. Financial liabilities are included at the earliest date on which the counterparty can require repayment, regardless of whether or not such early repayment results in a penalty. If the repayment of a financial instrument is triggered by, or is subject to, specific criteria such as market price hurdles being reached, the asset is included in the time band that contains the latest date on which it can be repaid, regardless of early repayment.

The liability is included in the time band that contains the earliest possible date on which the conditions could be fulfilled, without considering the probability of the conditions being met.

For example, if a structured note is automatically prepaid when an equity index exceeds a certain level, the cash outflow will be included in the less than three months period, whatever the level of the index at the year end. The settlement date of debt securities in issue depends on when cash flows are received from the securitised assets. Where these assets are prepayable, the timing of the cash outflow relating to securities assumes that each asset will be prepaid at the earliest possible date. As the repayments of assets and liabilities are linked, the repayment of assets in securitisations is shown on the earliest date that the asset can be prepaid, as this is the basis used for liabilities.

The principal amounts of financial assets and liabilities that are repayable after 20 years or where the counterparty has no right to repayment of the principal are excluded from the table, as are interest payments after 20 years.

The maturity of guarantees and commitments is based on the earliest possible date they would be drawn in order to evaluate the RBSI Group's liquidity position.

MFVTPL assets of £158 million (2020 - £41 million) and HFT liabilities of £134 million (2020 - £128 million) have been excluded from the following tables.

7. Financial instruments - maturity analysis continued

2021	Group 0–3 months £m	3–12 months £m	1–3 years £m	3–5 years £m	5–10 years £m	10–20 years £m
Assets by contractual maturity up to 20 years						
Cash and balances at central banks	17,220	—	—	—	—	—
Loans to banks - amortised cost	1,305	—	—	—	—	—
Loans to customers - amortised cost	2,172	4,925	5,134	998	780	1,340
Finance lease	2	9	29	14	23	2
Amounts due from holding companies and fellow subsidiaries	489	90	—	—	—	—
Other financial assets	13	2,191	926	893	790	749
Liabilities by contractual maturity up to 20 years						
Bank deposits	266	—	—	—	—	—
Customer deposits	37,124	416	—	—	—	—
Other financial liabilities	295	166	—	—	—	—
Lease liabilities	1	3	9	7	12	12
Amounts due to holding companies and fellow subsidiaries	220	21	—	—	—	—
Guarantees and commitments notional amount						
Guarantees(1)	263	—	—	—	—	—
Commitments(2)	9,350	—	—	—	—	—

2020	Group 0-3 months £m	3–12 months £m	1–3 years £m	3–5 years £m	5–10 years £m	10–20 years £m
Assets by contractual maturity up to 20 years						
Cash and balances at central banks	13,531	—	—	—	—	—
Loans to banks - amortised cost	1,231	—	—	—	—	—
Loans to customers - amortised cost	1,745	3,331	4,937	1,067	693	1,349
Finance lease	10	11	33	14	26	2
Amounts due from holding companies and fellow subsidiaries	538	99	—	—	—	—
Other financial assets	527	833	1,361	945	1,413	665
Liabilities by contractual maturity up to 20 years						
Bank deposits	3	—	—	—	—	—
Customer deposits	30,673	606	3	—	—	—
Other financial liabilities	35	507	—	—	—	—
Lease liabilities	1	4	9	8	11	13
Amounts due to holding companies and fellow subsidiaries	212	24	—	—	—	—
Guarantees and commitments notional amount						
Guarantees(1)	198	—	—	—	—	—
Commitments(2)	9,444	—	—	—	—	—

7. Financial instruments - maturity analysis continued

2021	Bank 0–3 months £m	3–12 months £m	1–3 years £m	3–5 years £m	5–10 years £m	10–20 years £m
Assets by contractual maturity up to 20 years						
Cash and balances at central banks	17,220	—	—	—	—	—
Loans to banks - amortised cost	1,278	—	—	—	—	—
Loans to customers - amortised cost	2,172	4,925	5,134	998	780	1,340
Finance lease	2	9	29	14	23	2
Amounts due from holding companies and fellow subsidiaries	481	96	—	—	—	—
Other financial assets	13	2,191	926	893	790	749
Liabilities by contractual maturity up to 20 years						
Bank deposits	266	—	—	—	—	—
Customer deposits	37,124	416	—	—	—	—
Other financial liabilities	295	166	—	—	—	—
Lease liabilities	1	3	9	7	12	12
Amounts due to holding companies and fellow subsidiaries	286	21	—	—	—	—
Guarantees and commitments notional amount						
Guarantees[1]	263	—	—	—	—	—
Commitments[2]	9,350	—	—	—	—	—

2020	Bank 0-3 months £m	3–12 months £m	1–3 years £m	3–5 years £m	5–10 years £m	10–20 years £m
Assets by contractual maturity up to 20 years						
Cash and balances at central banks	13,531	—	—	—	—	—
Loans to banks - amortised cost	1,204	—	—	—	—	—
Loans to customers - amortised cost	1,745	3,331	4,937	1,067	693	1,349
Finance lease	10	11	33	14	26	2
Amounts due from holding companies and fellow subsidiaries	546	100	—	—	—	—
Other financial assets	527	833	1,361	945	1,413	665
Liabilities by contractual maturity up to 20 years						
Bank deposits	3	—	—	—	—	—
Customer deposits	30,673	606	3	—	—	—
Other financial liabilities	35	507	—	—	—	—
Lease liabilities	1	4	9	8	11	13
Amounts due to holding companies and fellow subsidiaries	298	24	—	—	—	—
Guarantees and commitments notional amount						
Guarantees[1]	198	—	—	—	—	—
Commitments[2]	9,444	—	—	—	—	—

(1) The RBSI Group is only called upon to satisfy a guarantee when the guaranteed party fails to meet its obligations. The RBSI Group expects most guarantees it provides to expire unused.
(2) The RBSI Group has given commitments to provide funds to customers under undrawn formal facilities, credit lines and other commitments to lend subject to certain conditions being met by the counterparty. The RBSI Group does not expect all facilities to be drawn, and some may lapse before drawdown.

8. Loan impairment provisions

Loan exposure and impairment metrics

The table below summarises loans and related credit impairment measures within the scope of ECL framework.

	Group		Bank	
	31 December 2021 £m	31 December 2020 £m	31 December 2021 £m	31 December 2020 £m
Loans - amortised cost				
Stage 1	16,185	12,143	16,158	12,143
Stage 2	477	2,242	477	2,215
Stage 3	162	211	162	211
Inter- group (1)	579	637	577	646
Total	17,403	15,233	17,374	15,215
Loans impairment provisions				
ECL provisions				
-Stage 1	8	14	8	14
-Stage 2	23	74	23	74
-Stage 3	24	48	24	48
Total	55	136	55	136
ECL provision coverage (2,3)				
-Stage 1 (%)	0.05	0.12	0.05	0.12
-Stage 2 (%)	4.82	3.30	4.82	3.34
-Stage 3 (%)	14.81	22.75	14.81	22.75
	0.33	0.93	0.33	0.93
Impairment losses/(releases)				
ECL charge	(52)	107	(53)	107
ECL (release)/loss rate - annualised (basis points) (4)	(0.3)	0.7	(0.3)	0.7
Amounts written off	28	3	28	3

(1) Amounts due from holding companies and fellow subsidiaries (Inter-Group) are all considered as Stage 1.
(2) ECL provisions coverage is ECL provisions divided by loans - amortised cost.
(3) ECL provisions coverage and ECL loss rates are calculated on third party loans and related ECL provisions and charge respectively.
(4) ECL loss rate is calculated as annualised third party ECL charge divided by loans – amortised cost.
(5) The table shows gross loans only and excludes amounts that are outside the scope of the ECL framework. Other financial assets within the scope of the IFRS 9 ECL framework were cash and balances at central banks totalling £17.2 billion (2020: £13.5 billion) and debt securities of £6.0 billion (2020: £5.4 billion).

8. Loan impairment provisions continued

Credit risk enhancement and mitigation

For information on credit risk enhancement and mitigation held as security, refer to Risk management – credit risk.

Critical accounting estimates

The loan impairment provisions have been established in accordance with IFRS 9. Accounting policy 13 sets out how the expected loss approach is applied. At 31 December 2021, customer loan impairment provisions amounted to £55 million (2020: £136 million). A loan is impaired when there is objective evidence that the cash flows will not occur in the manner expected when the loan was advanced. Such evidence includes changes in the credit rating of a borrower, the failure to make payments in accordance with the loan agreement; significant reduction in the value of any security breach of limits or covenants and observable data about relevant macroeconomic measures.

There is a risk that customers and counterparties fail to meet their contractual obligation to settle outstanding amounts, known as expected credit losses ('ECL'). The calculation of ECL considers historic, current and forward-looking information to determine the amount we do not expect to recover. ECL is recognised on current and potential exposures, and contingent liabilities.

The impairment loss is the difference between the carrying value of the loan and the present value of estimated future cash flows at the loan's original effective interest rate.

The measurement of credit impairment under the IFRS expected loss model depends on management's assessment of any potential deterioration in the creditworthiness of the borrower, its modelling of expected performance and the application of economic forecasts. All three elements require judgments that are potentially significant to the estimate of impairment losses. For further information and sensitivity analysis, refer to Risk management Note 18.

IFRS 9 ECL model design principles

To meet IFRS 9 requirements for ECL estimation, Probability Of Default (PD), Loss Given Default (LGD) and Exposure At Default (EAD) used in the calculations must be:

- Unbiased - material regulatory conservatism has been removed to produce unbiased model estimates;
- Point-in-time - recognise current economic conditions;
- Forward-looking - incorporated into PD estimates and, where appropriate, EAD and LGD estimates; and
- For the life of the loan - all models produce a term structure to allow a lifetime calculation for assets in Stage 2 and Stage 3.

IFRS 9 requires that at each reporting date, an entity shall assess whether the credit risk on an account has increased significantly since initial recognition. Part of this assessment requires a comparison to be made between the current lifetime PD (i.e. the current probability of default over the remaining lifetime) with the equivalent lifetime PD as determined at the date of initial recognition.

The general approach for the IFRS 9 LGD models is to leverage corresponding Basel LGD models with bespoke adjustments to ensure estimates are unbiased and where relevant forward-looking.

For Wholesale, while conversion ratios in the historical data show temporal variations, these cannot (unlike in the case of PD and some LGD models) be sufficiently explained by the Credit-Cycle Index ('CCI') measure and are presumed to be driven to a larger extent by exposure management practices. Therefore point-in-time best estimates measures for EAD are derived by estimating the regulatory model specification on a rolling five year window. For more details refer note 18.

Approach for multiple economic scenarios (MES)

The base scenario plays a greater part in the calculation of ECL than the approach to MES. This is discussed further in Note 18.

9. Other financial assets

	Group and Bank					
	Debt securities					
	Central and local government				Equity	
	UK	US	Other	Total	shares	Total
2021	£m	£m	£m	£m	£m	£m
Fair value through other comprehensive income	**1,459**	**640**	**1,035**	**3,134**	**—**	**3,134**
Amortised cost	**2,240**	**156**	**393**	**2,789**	**—**	**2,789**
Total	**3,699**	**796**	**1,428**	**5,923**	**—**	**5,923**
2020						
Fair value through other comprehensive income	1,155	501	139	1,795	1	1,796
Amortised cost	2,901	235	431	3,567	—	3,567
	4,056	736	570	5,362	1	5,363

10. Investments in subsidiaries

The table below shows the details of the wholly owned subsidiaries of RBSIH:

Name of subsidiary	Place of incorporation	Ownership	Principal activities
The Royal Bank of Scotland International Limited	Jersey	100%	The main activity of the Company is the provision of banking services, including the taking of deposits and lending.
NatWest Trustee and Depositary Services Limited (NWTDS)	UK	100%	The main activity of the Company is the provision of depositary services.
RBS International Depositary Services S.A	Luxembourg	100%	The main activity of the Company is the provision of depositary services.
Coutts & Co Cayman Limited	Cayman Islands	100%	Since 2020, entity is inactive.
Tilba Limited (formerly known as Isle of Man Bank Limited)	Isle of Man	100%	Since 2019, entity is inactive.

11. Property, plant and equipment

	Group					
2021	Freehold premises £m	Short leasehold premises £m	Long leasehold premises £m	Computers and other equipment £m	Right of use property £m	Total £m
Cost or valuation						
At 1 January	26	2	—	95	72	195
Transfers to disposal group	(1)	—	—	(1)	—	(2)
Other adjustments	—	—	—	2	—	2
Additions	1	1	—	13	2	17
Disposals	—	—	—	(4)	—	(4)
At 31 December	26	3	—	105	74	208
Accumulated impairment, depreciation and amortisation:						
At 1 January	6	—	—	69	42	117
Transfers to disposal group	—	—	—	(1)	—	(1)
Other adjustments	—	—	—	(1)	—	(1)
Charge for the year	1	—	—	7	5	13
At 31 December	7	—	—	74	47	128
Net book value at 31 December 2021	19	3	—	31	27	80

	Group					
2020	Freehold premises £m	Short leasehold premises £m	Long leasehold premises £m	Computers and other equipment £m	Right of use property £m	Total £m
Cost or valuation						
At 1 January	28	4	2	98	70	202
Additions	—	—	—	14	2	16
Disposals	(2)	(2)	(2)	(17)	—	(23)
At 31 December	26	2	—	95	72	195
Accumulated depreciation and amortisation:						
At 1 January	6	1	2	77	31	117
Disposals	—	(1)	(2)	(15)	—	(18)
Impairment losses	—	—	—	—	6	6
Charge for the year	—	—	—	7	5	12
At 31 December	6	—	—	69	42	117
Net book value at 31 December 2020	20	2	—	26	(30)	78

11. Property, plant and equipment continued

2021	Freehold premises £m	Short leasehold premises £m	Bank Long leasehold premises £m	Computers and other equipment £m	Right of use property £m	Total £m
Cost or valuation						
At 1 January	26	2	—	94	72	194
Transfers to disposal group	(1)			(1)		(2)
Other adjustments	—			2		2
Additions	1	1	—	13	2	17
Disposals	—	—	—	(4)	—	(4)
At 31 December	26	3	—	104	74	207
Accumulated impairment, depreciation and amortisation:						
At 1 January	6	—	—	68	42	116
Transfers to disposal group	—	—	—	(1)	—	(1)
Other adjustments	—	—	—	(1)	—	(1)
Charge for the year	1	—	—	7	5	13
At 31 December	7	—	—	73	47	127
Net book value at 31 December 2021	19	3	—	31	27	80

2020	Freehold premises £m	Short leasehold premises £m	Bank Long leasehold premises £m	Computers and other equipment £m	Right of use property £m	Total £m
Cost or valuation						
At 1 January	28	4	2	96	70	200
Additions	—	—	—	14	2	16
Disposals	(2)	(2)	(2)	(16)	—	(22)
At 31 December	26	2	—	94	72	194
Accumulated depreciation and amortisation:						
At 1 January	5	1	2	76	31	115
Disposals	—	(1)	(2)	(14)	—	(17)
Impairment losses	—	—	—	—	6	6
Charge for the year	1	—	—	6	5	12
At 31 December	6	—	—	68	42	116
Net book value at 31 December 2020	20	2	—	26	30	78

12. Intangible assets

2021	Group Goodwill £m	Other (1) £m	Total £m
Cost:			
At 1 January	7	10	17
Additions	—	15	15
Disposals	—	—	—
At 31 December	7	25	32
Accumulated Amortisation:			
At 1 January	—	3	3
Disposals	—	—	—
Charge for the year	—	1	1
At 31 December	—	4	4
Net book value at 31 December 2021	7	21	28

2020	Goodwill £m	Other (1) £m	Total £m
Cost:			
At 1 January	7	5	12
Additions	—	7	7
Disposals	—	(2)	(2)
At 31 December	7	10	17
Accumulated Amortisation:			
At 1 January	—	4	4
Disposals	—	(2)	(2)
Charge for the year	—	1	1
At 31 December	—	3	3
Net book value at 31 December 2020	7	7	14

12. Intangible assets continued

	Bank		
2021	Goodwill £m	Other (1) £m	Total £m
Cost:			
At 1 January	6	5	11
Additions	—	7	7
Disposals	—	—	—
At 31 December	6	12	18
Accumulated Amortisation:			
At 1 January	—	3	3
Disposals	—	—	—
Charge for the year	—	1	1
At 31 December	—	4	4
Net book value at 31 December 2021	6	8	14

2020	Goodwill £m	Other (1) £m	Total £m
Cost:			
At 1 January	6	5	11
Additions	—	2	2
Disposals	—	(2)	(2)
At 31 December	6	5	11
Accumulated Amortisation:			
At 1 January	—	4	4
Disposals	—	(2)	(2)
Charge for the year	—	1	1
At 31 December	—	3	3
Net book value at 31 December 2020	6	2	8

The amortisation period for software development costs is 5 years. The amortisation is calculated using the straight-line method.

(1) The additions to other intangibles of £14 million includes £7.6 million (2020: £4.7 million) relates to programme costs in NWTDS and £6.4 million (2020: £1.2 million) for RBSI. The programme is automating and digitalising customer journeys in NWTDS, including building connectivity to the cloud. As the programme is not yet live, no amortisation has taken place to date. (Bank: The additions to other intangibles £6.4 million (2020: £1.2 million) relates to costs of Cloud development and internally developed software).

13. Other assets

	Group		Bank	
	2021 £m	2020 £m	2021 £m	2020 £m
Property plant and equipment (refer Note 11)	80	78	80	78
Prepayments	3	4	3	4
Accrued income	21	11	11	3
Other assets	15	1	14	1
Current and deferred tax (refer Note 5)	5	17	5	19
Retirement benefit assets (refer Note 4)	206	173	206	173
	330	284	319	278

14. Other financial liabilities

	Group and Bank	
	2021 £m	2020 £m
Bank deposits - held for trading (1)	11	—
Customer deposits - held for trading (1)	6	—
Debt securities in issue - amortised cost	459	542
	476	542

(1) Deposits relate to collateral received.

The above debt securities in issue balance is related to 17 short term Euro debt securities issued by the Bank in 2021 and mature in 2022. These papers were issued at total premium of £0.8 million.

15. Other liabilities

	Group		Bank	
	2021 £m	2020 £m	2021 £m	2020 £m
Lease liabilities (refer Note 17)	37	40	37	40
Provisions for liabilities and charges	19	34	19	34
Accruals	26	13	23	10
Deferred income	40	51	40	51
Current tax and deferred tax (refer Note 5)	21	19	18	19
Other liabilities	6	1	6	1
	149	158	143	155

The following amounts are included within provisions:

	Group and Bank				
	Provision for property (1) £m	Integration restructuring divested provision (2) £m	ECL provision (3) £m	Others (4) £m	Total £m
At 1 January 2020	1	5	1	3	10
Charged to the income statement	13	15	—	—	28
Released during the year	—	—	—	(3)	(3)
Other movements	—	—	5	—	5
Utilised in year	(1)	(5)	—	—	(6)
At 1 January 2021	13	15	6	—	34
Charged to the income statement	—	2	—	3	5
Released during the year	—	(1)	—	—	(1)
Other movements	—	—	(4)	—	(4)
Utilised in year	(1)	(14)	—	—	(15)
At 31 December 2021	12	2	2	3	19

(1) Provision for Property - The property provisions represent costs related to closure of properties.
(2) Integration restructuring divested provision - The restructuring provisions principally comprise redundancy costs. The RBSI Group expects the majority of these provisions to be utilised within the next 12 months.
(3) ECL provision - ECL provision is made up of provisions on contingent liabilities and commitments, as calculated in accordance with IFRS 9.
(4) Other - Other provisions is made up of contingent liabilities relating to conduct. This includes amount for potential fines and customer redress.

Critical accounting policy: Provisions for liabilities

The key judgment is involved in determining whether an obligation exists. There is often a high degree of uncertainty and judgment is based on the specific facts and circumstances relating to individual events in determining whether there is a present obligation. Judgment is also involved in estimation of the probability, timing and amount of any outflows. Where the RBSI Group can look to another party such as an insurer to pay some or all of the expenditure required to settle a provision, any reimbursement is recognised when, and only when, it is virtually certain that it will be received.

Estimates - Provisions are liabilities of uncertain timing or amount and are recognised when there is a present obligation as a result of a past event, the outflow of economic benefit is probable and the outflow can be estimated reliably. Any difference between the final outcome and the amounts provided will affect the reported results in the period when the matter is resolved.

16. Share capital and other equity

	Group			
			Number of shares	
	2021	2020	2021	2020
Allotted, called up and fully paid	£m	£m	000s	000s
Equity shares:				
A' Ordinary shares of £1	176	176	175,445	175,445
B' Ordinary shares of £1	135	135	135,290	135,290
	311	311	310,735	310,735

The RBSI Group has two classes of ordinary shares which carry no right to fixed income. There are no differences in the rights attached to the 'A' and 'B' ordinary shares.

	Bank			
			Number of shares	
	2021	2020	2021	2020
Allotted, called up and fully paid	£m	£m	000s	000s
Equity shares:				
Ordinary shares of £1	97	97	96,540	96,540
	97	97	96,540	96,540

The whole of the issued share capital of the Bank comprises one class of Ordinary Share held by its holding company, RBSIH and its nominee, each share being entitled to one vote.

Paid-in equity

Paid-in equity comprises equity instruments issued by RBSI to NWG other than those legally constituted as shares.

	Group and Bank	
	31 December 2021	31 December 2020
	£m	£m
Additional Tier 1 capital notes:		
£300m 6.604% notes repayable from September 2025	300	300
	300	300

The coupons on this instrument are non-cumulative and payable at the RBSI Group's discretion. In the event of winding up, any amounts outstanding on the loan will be subordinated. While taking the legal form of debt, these notes are classified as equity under IFRS.

17. Leases

Lessee

The RBSI Group is party to lease contracts as lessee to support its operations. The following table provides information in respect of those lease contracts as lessee.

	Group and Bank	
	2021	2020
	£m	£m
Amounts recognised in consolidated income statement		
Interest payable	1	1
Depreciation[1]	5	11
Rental expense on short leases	—	1

	Group and Bank	
	2021	2020
	£m	£m
Amounts recognised on Balance Sheet		
Right of use assets included in property, plant and equipment	27	30
Additions to right of use assets	1	2
Lease liabilities	(37)	(40)

(1) Includes impairment of right of use assets of nil (2020: £6m).

17. Leases continued

Lessor

Acting as a lessor, the RBSI Group provides asset finance to its customers. It purchases plant, equipment and intellectual property, renting them to customers under lease arrangements that, depending on their terms, qualify as either operating or finance leases.

	Group and Bank	
	2021	2020
	£m	£m
Amounts included in consolidated income statement		
Finance leases		
Finance income on the net investment in leases	(4)	(5)

	2021	2020
	£m	£m
Amount receivable under finance leases		
Within 1 year	8	18
1 to 2 years	20	11
2 to 3 years	6	19
3 to 4 years	6	6
4 to 5 years	6	6
After 5 years	32	35
Lease payments total	78	95
Unearned income	(19)	(23)
Present value of lease payments	59	72
Impairments	—	—
Net investment in finance leases	59	72

18. Risk management

Presentation of information

Risk and capital management is generally conducted on an overall basis within NWG such that common policies, procedures, frameworks and models apply across NWG. Therefore, for the most part, discussion on these qualitative aspects reflects those in NWG as relevant for the businesses and operations in RBSI Group and Bank.

Update on COVID-19

While the immediate disruption diminished during the year, the ongoing impacts of the global pandemic remained a significant focus for risk management in 2021 and uncertainty in the operating environment continued. RBSI Group remained committed to supporting its customers while operating safely and soundly in line with its strategic objectives.

Against the backdrop of a slowly recovering economy, the credit risk profile remains heightened and there is an expectation that the impacts of the pandemic will continue to be seen in the performance of RBSI Group's portfolios for some time.

While the direct impact on RBSI Group's operational risk profile reduced, RBSI Group continued to closely monitor the second-order impacts on its transformation agenda, with a significant focus on managing resource to protect key regulatory deliveries. The continued evolution of RBSI Group's ways of working – to include large-scale working from home – also required significant operational risk focus, particularly in terms of business resilience.

As a result of its strong balance sheet and prudent approach to risk management, RBSI Group remains well placed to withstand these aftershocks as well as providing support to customers when they need it most.

Risk management framework

RBSI Group operates under NWG's enterprise-wide risk management framework, which is centred around the embedding of a strong risk culture. The framework ensures the governance, capabilities and methods are in place to facilitate risk management and decision-making across the organisation.

The framework ensures that RBSI Group's principal risks – which are detailed in this section – are appropriately controlled and managed. In addition, there is a process to identify and manage top risks, which are those which could have a significant negative impact on RBSI Group's ability to meet its strategic objectives. A complementary process operates to identify emerging risks. Both top and emerging risks are reported to the Board on a regular basis alongside reporting on the principal risks.

Risk appetite, supported by a robust set of principles, policies and practices, defines the levels of tolerance for all risks identified within the framework and provides a structured approach to risk-taking within agreed boundaries.

All RBSI Group colleagues share ownership of the way risk is managed, working together to make sure business activities and policies are consistent with risk appetite.

18. Risk management continued

Culture

Risk culture is at the heart of RBSI Group's risk management framework and its risk management practice. The risk culture target is to make risk part of the way employees work and think. A focus on leaders as role models and action to build clarity, develop capability and motivate employees to reach the required standards of behaviour are key to achieving the risk culture target. The target risk culture behaviours are embedded in Critical People Capabilities and are clearly aligned to the core values of "serving customers", "working together", "doing the right thing" and "thinking long term." Critical People Capabilities form the basis of all recruitment and selection processes.

Training

Enabling employees to have the capabilities and confidence to manage risk is core to NWG's learning strategy. NWG offers a wide range of learning, both technical and behavioural, across the risk disciplines. This training can be mandatory, role-specific or for personal development. Mandatory learning for all staff is focused on keeping employees, customers and RBSI Group safe. This is easily accessed online and is assigned to each person according to their role and business area. The system allows monitoring at all levels to ensure completion.

Our Code

NWG's conduct guidance, Our Code, provides direction on expected behaviour and sets out the standards of conduct that support the values. The code explains the effect of decisions that are taken and describes the principles that must be followed.

These principles cover conduct-related issues as well as wider business activities. They focus on desired outcomes, with practical guidelines to align the values with commercial strategy and actions. The embedding of these principles facilitates sound decision-making and a clear focus on good customer outcomes.

Where appropriate, if conduct falls short of NWG's required standards, the accountability review process is used to assess how this should be reflected in pay outcomes for the individuals concerned. Any employee falling short of the expected standards would also be subject to internal disciplinary policies and procedures. If appropriate, the relevant authority would be notified.

Three lines of defence

RBSI Group uses the industry-standard three lines of defence model to articulate accountabilities and responsibilities for managing risk. This supports the embedding of effective risk management throughout the organisation.

The first line of defence incorporates most roles in RBSI Group, including customer-facing and support functions roles. The first line of defence is empowered to take risks within the constraints of the risk management framework and policies as well as the risk appetite statements set by NatWest Group and measures set by the Board. The first line of defence is responsible for managing its direct risks. With the support of specialist functions such as Legal, Human Resources and Technology, it is also responsible for managing its consequential risks by identifying, assessing, mitigating, monitoring and reporting risks.

The second line of defence comprises the Risk function and is independent of the first line. The second line of defence is empowered to design and maintain the risk management framework and its components. It undertakes proactive risk oversight and continuous monitoring activities to confirm that RBSI Group engages in permissible and sustainable risk-taking activities. The second line of defence advises on, monitors, challenges, approves, escalates and reports on the risk-taking activities of the first line, ensuring that these are within the constraints of the risk management framework and policies as well as the risk appetite statements set by NatWest Group and measures set by the Board.

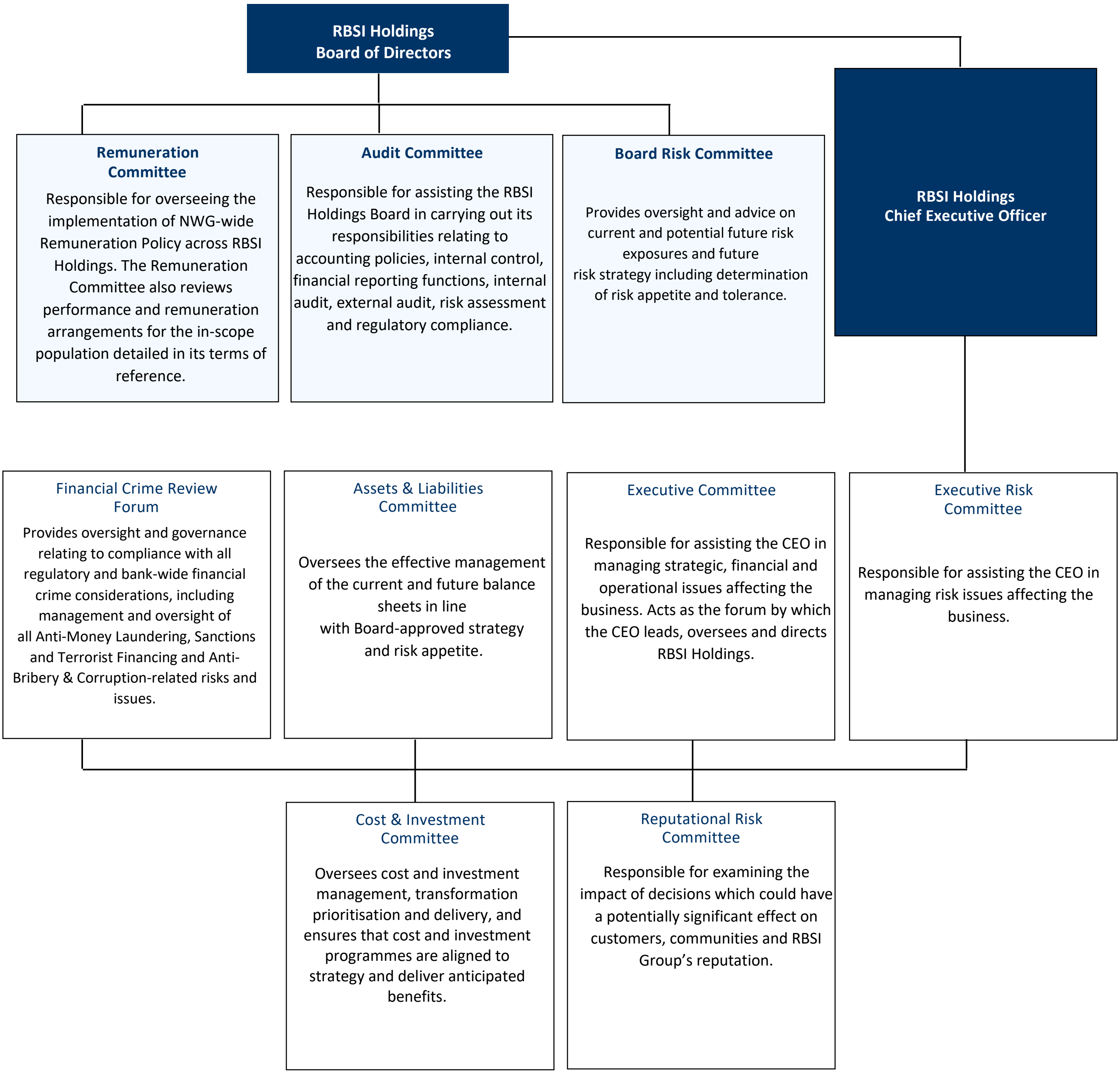
The third line of defence is the Internal Audit function and is independent of the first and second lines. The third line of defence is responsible for providing independent and objective assurance to the Board and executive management on the adequacy and effectiveness of key internal controls, governance and the risk management in place to monitor, manage and mitigate the key risks to RBSI Group achieving its objectives. The third line of defence executes its duties freely and objectively in accordance with the Chartered Institute of Internal Auditors' Code of Ethics and International Standards.

18. Risk management continued

Governance

Committee structure

The diagram shows RBSI Group's risk committee structure in 2021 and the main purposes of each committee.



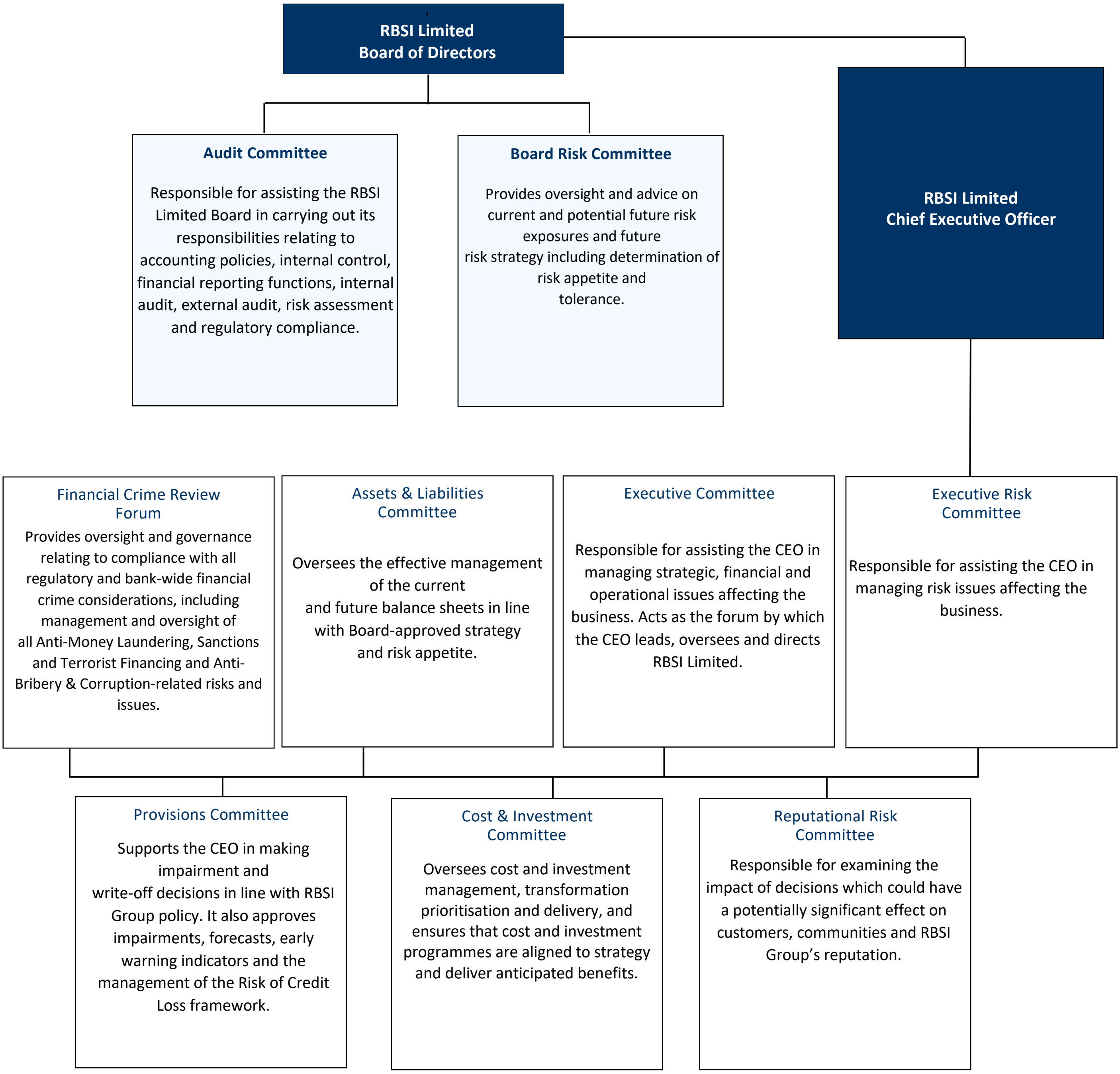
(1) RBSI Holdings is a Jersey incorporated holding company. It has three principal operating subsidiaries: The Royal Bank of Scotland International Limited, a Jersey incorporated and regulated bank; NatWest Trustee and Depository Services Limited, a company incorporated in England and Wales; and RBS International Depository Services S.A., a company incorporated in Luxembourg.
(2) The chart does not show all management-level committees, only material committees which consider risk are shown.
(3) The NatWest Holdings Group Risk function provides risk management services across NWG, including – where agreed – to the RBSI Holdings Chief Risk Officer. These services are managed, as appropriate, through service level agreements.

18. Risk management continued

Governance

Committee structure

The diagram shows the Bank's risk committee structure in 2021 and the main purposes of each committee.

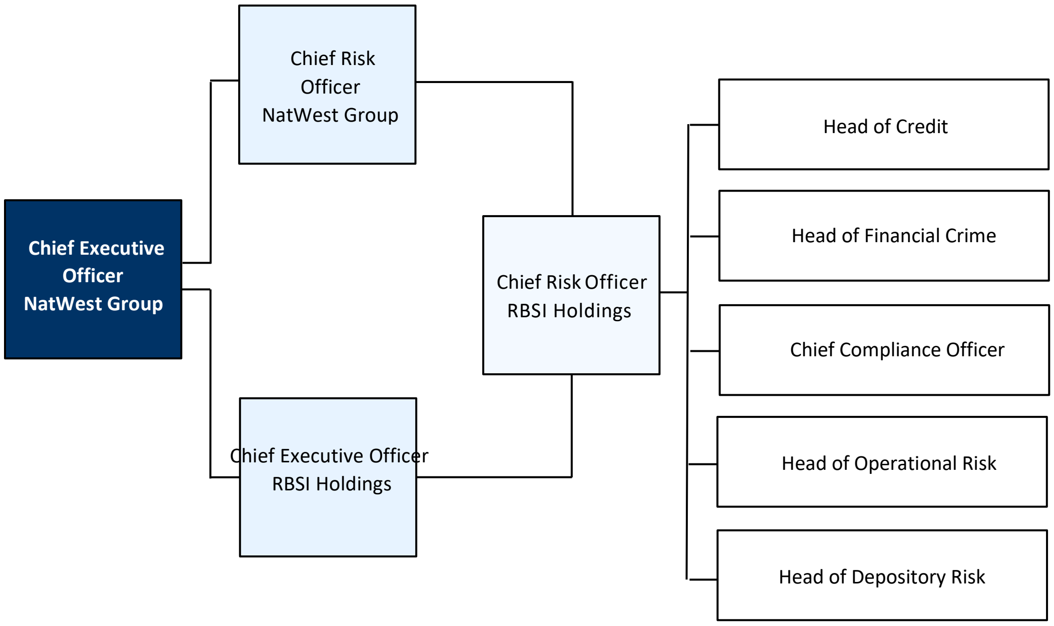


(1) The Royal Bank of Scotland International Limited is one of the principal operating subsidiaries of RBSI Holdings.
(2) The chart does not show all management-level committees, only material committees which consider risk are shown.
(3) The NWH Group Risk function provides risk management services across NWG, including – where agreed – to the RBSI Limited Chief Risk Officer. These services are managed, as appropriate, through service level agreements.

18. Risk management continued

Risk management structure

The diagram shows RBSI Group's risk management structure in 2021.



(1) The RBSI Holdings Chief Risk Officer reports directly to the RBSI Holdings Chief Executive Officer and the NWG Chief Risk Officer. The RBSI Holdings Chief Risk Officer also has an additional reporting line to the chair of the RBSI Holdings Board Risk Committee, and a right of access to the committee.

18. Risk management continued

Risk appetite

Risk appetite defines the type and aggregate level of risk RBSI Group is willing to accept in pursuit of its strategic objectives and business plans. Risk appetite supports sound risk taking, the promotion of robust risk practices and risk behaviours, and is calibrated annually.

For certain principal risks, risk capacity defines the maximum level of risk RBSI Group can assume before breaching constraints determined by regulatory capital and liquidity requirements, the operational environment, and from a conduct perspective. Establishing risk capacity helps determine where risk appetite should be set, ensuring there is a buffer between internal risk appetite and RBSI Group's ultimate capacity to absorb losses.

Risk appetite framework

The risk appetite framework supports effective risk management by promoting sound risk-taking through a structured approach, within agreed boundaries. It also ensures emerging risks and risk-taking activities that might be out of appetite are identified, assessed, escalated and addressed in a timely manner.

To facilitate this, a detailed annual review of the framework is carried out. The review includes:

- Assessing the adequacy of the framework when compared to internal and external expectations.
- Ensuring the framework remains effective and acts as a strong control environment for risk appetite.
- Assessing the level of embedding of risk appetite across the organisation.

The Board approves the risk appetite framework annually.

Establishing risk appetite

In line with NWG's risk appetite framework, risk appetite is maintained across RBSI Group through risk appetite statements. These are in place for all principal risks and describe the extent and type of activities that can be undertaken.

Risk appetite statements consist of qualitative statements of appetite supported by risk limits and triggers that operate as a defence against excessive risk-taking. Risk measures and their associated limits are an integral part of the risk appetite approach and a key part of embedding risk appetite in day-to-day risk management decisions. A clear tolerance for each principal risk is set in alignment with business activities.

The annual process of reviewing and updating risk appetite statements is completed alongside the business and financial planning process. This ensures that plans and risk appetite are appropriately aligned.

The Board sets risk appetite for all principal risks to help ensure RBSI Group is well placed to meet its priorities and long-term targets even in challenging economic environments. This supports RBSI Group in remaining resilient and secure as it pursues its strategic business objectives.

RBSI Group's risk profile is frequently reviewed and monitored. Management focus is concentrated on all principal risks as well as the top and emerging risk issues which may correlate to them. Risk profile relative to risk appetite is reported regularly to executive management and the Board.

NWG policies directly support the qualitative aspects of risk appetite. They define the qualitative expectations, guidance and standards that stipulate the nature and extent of permissible risk taking and are consistently applied across NWG and its subsidiaries.

Identification and measurement

Identification and measurement within the risk management process comprise:

- Regular assessment of the overall risk profile, incorporating market developments and trends, as well as external and internal factors.
- Monitoring of the risks associated with lending and credit exposures.
- Assessment of trading and non-trading portfolios.
- Review of potential risks in new business activities and processes.
- Analysis of potential risks in any complex and unusual business transactions.

The financial and non-financial risks that RBSI Group faces are detailed in its Risk Directory. This provides a common risk language to ensure consistent terminology is used across RBSI Group. The Risk Directory is subject to annual review to ensure it continues to fully reflect the risks that RBSI Group faces.

Mitigation

Mitigation is a critical aspect of ensuring that risk profile remains within risk appetite. Risk mitigation strategies are discussed and agreed within RBSI Group.

When evaluating possible strategies, costs and benefits, residual risks (risks that are retained) and secondary risks (those that arise from risk mitigation actions themselves) are also considered. Monitoring and review processes are in place to evaluate results. Early identification, and effective management of changes in legislation and regulation are critical to the successful mitigation of compliance and conduct risk. The effects of all changes are managed to ensure the timely achievement of compliance. Those changes assessed as having a high or medium-high impact are managed more closely. Emerging risks that could affect future results and performance are also closely monitored. Action is taken to mitigate potential risks as and when required. Further in-depth analysis, including the stress testing of exposures, is also carried out.

Testing and monitoring

Targeted risk processes and controls – including controls within the scope of Section 404 of the Sarbanes-Oxley Act 2002 – are subject to independent testing and monitoring.

This activity is carried out to confirm to both internal and external stakeholders – including the Board, executive management, Internal Audit and RBSI Group's regulators – that such processes and controls are being correctly implemented and operate adequately and effectively. A consistent testing and monitoring methodology is in place across RBSI Group.

Testing and monitoring activity focuses on processes and controls relating to credit risk, financial crime risk, operational resilience, and compliance and conduct risk. However, a range of controls and processes relating to other risk types is also subject to testing and monitoring activity as deemed appropriate within the context of a robust control environment.

18. Risk management continued

Stress testing – capital management

Stress testing is a key risk management tool and a fundamental component of RBSI Group's approach to capital management. It is used to quantify and evaluate the potential impact of specified changes to risk factors on the financial strength of RBSI Group, including its capital position.

Stress testing includes:
- Scenario testing, which examines the impact of a hypothetical future state to define changes in risk factors.
- Sensitivity testing, which examines the impact of an incremental change to one or more risk factors.

The process for stress testing consists of four broad stages:

Define scenarios	– Identify specific macro RBSI Group vulnerabilities and risks. – Define and calibrate scenarios to examine risks and vulnerabilities. – Formal governance process to agree scenarios.
Assess impact	– Translate scenarios into risk drivers. – Assess impact to current and projected P&L and balance sheet across RBSI Group.
Calculate results and assess implications	– Aggregate impacts into overall results. – Results form part of the risk management process. – Scenario results are used to inform RBSI Group's business and capital plans.
Develop and agree management actions	– Scenario results are analysed by subject matter experts. Appropriate management actions are then developed. – Scenario results and management actions are reviewed by the relevant Executive Risk Committees and the Board Risk Committees and, agreed by the relevant Boards.

Stress testing is used widely across NWG. Specific areas that involve capital management include:
- *Strategic financial and capital planning* – by assessing the impact of sensitivities and scenarios on the capital plan and capital ratios.
- *Risk appetite* – by gaining a better understanding of the drivers of, and the underlying risks associated with, risk appetite.
- *Risk monitoring* – by monitoring the risks and horizon scanning events that could potentially affect RBSI Group's financial strength and capital position.
- *Risk mitigation* – by identifying actions to mitigate risks, or those that could be taken, in the event of adverse changes to the business or economic environment. Key risk mitigating actions are documented in RBSI Group's recovery plan.

Reverse stress testing is also carried out in order to identify circumstances that may lead to specific, defined outcomes such as business failure. Reverse stress testing allows potential vulnerabilities in the business model to be examined more fully.

Capital sufficiency – going concern forward-looking view

Going concern capital requirements are examined on a forward-looking basis – including as part of the annual budgeting process – by assessing the resilience of capital adequacy and leverage ratios under hypothetical future states. These assessments include assumptions about regulatory and accounting factors (such as IFRS 9). They incorporate economic variables and key assumptions on balance sheet and P&L drivers, such as impairments, to demonstrate that RBSI Group maintains sufficient capital. A range of future states are tested. In particular, capital requirements are assessed:
- Based on a forecast of future business performance, given expectations of economic and market conditions over the forecast period.
- Based on a forecast of future business performance under adverse economic and market conditions over the forecast period. Scenarios of different severity may be examined.

The examination of capital requirements under normal economic and adverse market conditions enables RBSI Group to determine whether its projected business performance meets internal plans and regulatory capital requirements.

The examination of capital requirements under adverse economic and market conditions is assessed through stress testing. The results of stress tests are not only used widely across RBSI Group but also by the regulators to set specific capital buffers. RBSI Group takes part in NWG stress tests run by regulatory authorities to test industry-wide vulnerabilities under crystallising global and domestic systemic risks.

Stress and peak-to-trough movements are used to help assess the amount of capital RBSI Group needs to hold in stress conditions in accordance with the capital risk appetite framework.

Internal assessment of capital adequacy

In the Bank, an internal assessment of material risks is carried out to enable an evaluation of the amount, type and distribution of capital required to cover these risks. This is referred to as the Internal Capital Adequacy Assessment Process (ICAAP). The Bank's ICAAP consists of a point-in-time assessment of exposures and risks at the end of the financial year together with a forward-looking stress capital assessment. The Bank's ICAAP is approved by the Board and submitted to the Jersey Financial Services Commission (JFSC).

The ICAAP is used to form a view of capital adequacy separately to the minimum regulatory requirements. The ICAAP is used by the JFSC to assess RBSI Group's specific capital requirements through the Pillar 2 framework.

Governance

Capital management is subject to substantial review and governance. The Boards of both the Bank and RBSI Group approve the capital plans, including those for key legal entities and businesses as well as the results of the stress tests relating to those capital plans.

18. Risk management continued

Stress testing – liquidity

Liquidity risk monitoring and contingency planning

A suite of tools is used to monitor, limit and stress test the risks on the balance sheet. Limit frameworks are in place to control the level of liquidity risk, asset and liability mismatches and funding concentrations. Liquidity risks are reviewed daily, with performance reported to the Assets & Liabilities Committee on a regular basis. Liquidity Condition Indicators are monitored daily. This ensures any build-up of stress is detected early and the response escalated appropriately through recovery planning.

Internal assessment of liquidity

Under the liquidity risk management framework, RBSI Group maintains the Internal Liquidity Adequacy Assessment Process. This includes assessment of net stressed liquidity outflows under a range of severe but plausible stress scenarios. Each scenario evaluates either an idiosyncratic, market-wide or combined stress event as described in the table below.

Type	Description
Idiosyncratic scenario	The market perceives RBSI Group to be suffering from a severe stress event, which results in an immediate assumption of increased credit risk or concerns over solvency.
Market-wide scenario	A market stress event affecting all participants in a market through contagion, potential counterparty failure and other market risks. RBSI Group is affected under this scenario but no more severely than any other participants with equivalent exposure.
Combined scenario	This scenario models the combined impact of an idiosyncratic and market stress occurring at once, severely affecting funding markets and the liquidity of some assets.

RBSI Group uses the most severe outcome to set the internal stress testing scenario which underpins its internal liquidity risk appetite. This complements the regulatory liquidity coverage ratio requirement.

Stress testing – recovery and resolution planning

The recovery plan explains how RBSI Group would identify and respond to a financial stress event and restore its financial position so that it remains viable on an ongoing basis. RBSI Group has its own recovery plan which forms part of the overall NWG plan.

The recovery plan ensures risks that could delay the implementation of a recovery strategy are highlighted and preparations are made to minimise the impact of these risks. Preparations include:

- Developing a series of recovery indicators to provide early warning of potential stress events.
- Clarifying roles, responsibilities and escalation routes to minimise uncertainty or delay.
- Developing a recovery playbook to provide a concise description of the actions required during recovery.
- Detailing a range of options to address different stress conditions.
- Appointing dedicated option owners to reduce the risk of delay and capacity concerns.
- Carrying out ‘fire drills’ to practise responding to recovery events.

The plan is intended to enable RBSI Group to maintain critical services and products it provides to its customers, maintain its core business lines and operate within risk appetite while restoring RBSI Group’s financial condition. It is assessed for appropriateness on an ongoing basis and is updated annually. The plan is reviewed and approved by the Board prior to submission to the JFSC each year.

Resolution would be implemented if NWG or RBSI Group was assessed by the UK or Jersey authorities to have failed and the appropriate regulator put it into resolution. The Bank (Recovery and Resolution) (Jersey) Law 2017 (the Law) came into force on 31 January 2022. The Law provides a new bank resolution regime for Jersey which is broadly consistent with the European Union Bank Recovery and Resolution Directive (2014/59) and the United Kingdom Banking Act 2009 (as amended). Specifically, it will establish the Jersey Resolution Authority which will be granted administrative powers to stabilise and/or resolve distressed banks.

Stress testing – non-traded market risk

RBSI Group produces an internal scenario analysis as part of its financial planning cycles.

Non-traded exposures are capitalised through the ICAAP. This covers gap risk, basis risk, credit spread risk, pipeline risk, structural foreign exchange risk, prepayment risk, equity risk and accounting volatility risk. The ICAAP is completed with a combination of value and earnings measures. The total non-traded market risk capital requirement is determined by adding the different charges for each sub risk type. The ICAAP methodology captures at least ten years of historical volatility, produced with a 99% confidence level. Methodologies are reviewed by NWG Model Risk and the results are approved by the NWG Technical Asset & Liability Management Committee.

18. Risk management continued

Credit risk

Definition

Credit risk is the risk that customers and counterparties fail to meet their contractual obligation to settle outstanding amounts.

Sources of risk

RBSI Group has exposure to entities by making placements and advances to those counterparties. The Board reviews the placement of deposits to other legal entities in NWG. NWG is majority owned by the UK Government and draws on support provided by central banks where required in order to meet its commitments including those to RBSI Group.

RBSI Group also has exposure to the Bank of England, the Central Bank of Luxembourg, US correspondent banks and the UK, US and various eurozone governments through holding government bonds in its liquid asset portfolio. These exposures are also reviewed by the Board of Directors.

Governance

The Credit Risk function provides oversight and challenge of frontline credit risk management activities. Governance activities include:

- Defining credit risk appetite measures for the management of concentration risk and credit policy to establish the key causes of risk in the process of providing credit and the controls that must be in place to mitigate them.
- Approving and monitoring operational limits for business segments and credit limits for customers.
- Oversight of the first line of defence to ensure that credit risk remains within the appetite set by the Board and that controls are being operated adequately and effectively.
- Assessing the adequacy of expected credit loss (ECL) provisions including approving key IFRS 9 inputs (such as significant increase in credit risk (SICR) thresholds) and any necessary in-model and post model adjustments through the Provisions Committee.

Risk appetite

Credit risk appetite aligns to the strategic risk appetite set by the Board and is set and monitored through risk appetite frameworks.

Personal

The Personal credit risk appetite framework sets limits that control the quality and concentration of both existing and new business for each relevant business segment. These risk appetite measures consider the segments' ability to grow sustainably and the level of losses expected under stress. Credit risk is further controlled through operational limits specific to customer or product characteristics.

Wholesale

For Wholesale credit, the framework has been designed to reflect factors that influence the ability to operate within risk appetite. Tools such as stress testing and economic capital are used to measure credit risk volatility and develop links between the framework and risk appetite limits.

Four formal frameworks are used, classifying, measuring and monitoring credit risk exposure and setting risk appetite limits across single name, sector and country concentrations and product and asset classes with heightened risk characteristics.

The framework is supported by a suite of transactional acceptance standards that set out the risk parameters within which businesses should operate.

Credit policy standards are in place for both the Wholesale and Personal portfolios. They are expressed as a set of mandatory controls.

Identification and measurement

Credit stewardship

Risks are identified through relationship management and credit stewardship of customers and portfolios. Credit risk stewardship takes place throughout the customer relationship, beginning with the initial approval. It includes the application of credit assessment standards, credit risk mitigation and collateral, ensuring that credit documentation is complete and appropriate, carrying out regular portfolio or customer reviews and problem debt identification and management.

Asset quality

All credit grades map to an asset quality (AQ) scale, used for financial reporting. This AQ scale is based on Basel probability of defaults. Performing loans are defined as AQ1-AQ9 (where the probability of default (PD) is less than 100%) and defaulted non-performing loans as AQ10 or Stage 3 under IFRS 9 (where the PD is 100%). Loans are defined as defaulted when the payment status becomes 90 days past due, or earlier if there is clear evidence that the borrower is unlikely to repay, for example bankruptcy or insolvency.

Counterparty credit risk

RBSI Group mitigates counterparty credit risk through collateralisation and netting agreements, which allow amounts owed by RBSI Group to a counterparty to be netted against amounts the counterparty owes RBSI Group.

18. Risk management continued

Credit risk continued

Mitigation

Mitigation techniques, as set out in the appropriate credit policies and transactional acceptance standards, are used in the management of credit portfolios across RBSI Group. These techniques mitigate credit concentrations in relation to an individual customer, a borrower group or a collection of related borrowers. Where possible, customer credit balances are netted against obligations. Mitigation tools can include structuring a security interest in a physical or financial asset, the use of credit derivatives including credit default swaps, credit-linked debt instruments and securitisation structures, and the use of guarantees and similar instruments (for example, credit insurance) from related and third parties. Property is used to mitigate credit risk across a number of portfolios, in particular residential mortgage lending and commercial real estate (CRE).

The valuation methodologies for collateral in the form of residential mortgage property and CRE are detailed below.

Residential mortgages – RBSI Group takes collateral in the form of residential property to mitigate the credit risk arising from mortgages. RBSI Group values residential property during the loan underwriting process by appraising properties individually.

Commercial real estate valuations – RBSI Group has an actively managed panel of chartered surveying firms that cover the spectrum of geography and property sectors in which RBSI Group takes collateral. Suitable valuers for particular assets are typically contracted through a service agreement to ensure consistency of quality and advice.

Assessment and monitoring

Practices for credit stewardship – including credit assessment, approval and monitoring as well as the identification and management of problem debts – differ between the Personal and Wholesale portfolios.

Personal

Personal customers are served through a lending approach that entails offering a large number of small-value loans. To ensure that these lending decisions are made consistently, RBSI Group analyses internal credit information as well as external data supplied by credit reference agencies (including historical debt servicing behaviour of customers with respect to both RBSI Group and other lenders). RBSI Group then sets its lending rules accordingly, developing different rules for different products.

The process is then largely automated, with each customer receiving an individual credit score that reflects both internal and external behaviours and this score is compared with the lending rules set. For relatively high-value, complex personal loans, including residential mortgage lending, credit managers make the final lending decisions. These decisions are made within specified delegated authority limits that are issued dependent on the experience of the individual.

Underwriting standards and portfolio performance are monitored on an ongoing basis to ensure they remain adequate in the current market environment and are not weakened materially to sustain growth.

Wholesale

Wholesale customers are grouped by industry sectors and geography as well as by product/asset class and are managed on an individual basis. Customers are aggregated as a single risk when sufficiently interconnected.

A credit assessment is carried out before credit facilities are made available to customers. The assessment process is dependent on the complexity of the transaction. Credit approvals are subject to environmental, social and governance risk policies which restrict exposure to certain highly carbon intensive industries as well as those with potentially heightened reputational impacts. Customer specific climate risk commentary is now mandatory.

In response to COVID-19, a new framework was introduced to categorise clients in a consistent manner across the Wholesale portfolio, based on the effect of COVID-19 on their financial position and outlook in relation to the sector risk appetite. This framework has been retained and updated to consider viability impacts beyond those directly related to COVID-19 and classification via the framework is now mandatory and must be refreshed annually. The framework extends to all Wholesale borrowing clients and supplements the Risk of Credit Loss framework in assessing whether customers exhibit a SICR, if support is considered to be granting forbearance and the time it would take for clients to return to operating within transactional acceptance standards.

Transactional acceptance standards provide detailed lending and risk acceptance metrics and structuring guidance. As such, these standards provide a mechanism to manage risk appetite at the customer/transaction level and are supplementary to the established credit risk appetite.

PD and loss given default (LGD) are reviewed and if appropriate reapproved annually. The review process assesses borrower performance, including reconfirmation or adjustment of risk parameter estimates; the adequacy of security; compliance with terms and conditions; and refinancing risk.

Problem debt management

Personal

Early problem identification

Pre-emptive triggers are in place to help identify customers that may be at risk of being in financial difficulty. These triggers are both internal, using RBSI Group's data, and external using information from credit reference agencies. Proactive contact is then made with the customer to establish if they require help with managing their finances. By adopting this approach, the aim is to prevent a customer's financial position deteriorating which may then require intervention from the Collections and Recoveries teams.

Personal customers experiencing financial difficulty are managed by the Collections team. If the Collections team is unable to provide appropriate support after discussing suitable options with the customer, management of that customer moves to the Recoveries team. If at any point in the collections and recoveries process, the customer is identified as being potentially vulnerable, the customer will be identified as such and supported by suitably experienced colleagues, to ensure the customer receives the appropriate support for their circumstances.

18. Risk management continued

Credit risk continued

Collections

When a customer exceeds an agreed limit or misses a regular monthly payment the customer is contacted by RBSI Group and requested to remedy the position. If the situation is not regularised then, where appropriate, the Collections team will become more involved and the customer will be supported by skilled debt management staff who endeavour to provide customers with bespoke solutions. Solutions include short-term account restructuring, refinance loans and forbearance which can include interest suspension and 'breathing space'. In the event that an affordable/sustainable agreement with a customer cannot be reached, the debt will transition to the Recoveries team. For provisioning purposes, under IFRS 9, exposure to customers managed by the Collections team is categorised as Stage 2 and subject to a lifetime loss assessment, unless it is 90 days past due or has an interest non-accrual status, in which case it is categorised as Stage 3.

Recoveries

The Recoveries team will issue a notice of intention to default to the customer and, if appropriate, a formal demand, while also registering the account with credit reference agencies where appropriate. Following this, the customer's debt may then be placed with a third-party debt collection agency, or alternatively a solicitor, in order to agree an affordable repayment plan with the customer. Exposures subject to formal debt recovery are categorised under IFRS 9, as Stage 3.

Wholesale

Early problem identification

Each sector has defined early warning indicators to identify customers experiencing financial difficulty, and to increase monitoring if needed. Early warning indicators may be internal, such as a customer's bank account activity, or external, such as a publicly-listed customer's share price. If early warning indicators show a customer is experiencing potential or actual difficulty, or if relationship managers or credit officers identify other signs of financial difficulty, they may decide to classify the customer within the Risk of Credit Loss framework.

Risk of Credit Loss framework

The Risk of Credit Loss framework is used where the credit profile of a Wholesale customer has deteriorated materially since origination. Experienced credit risk officers apply expert judgment to classify cases into categories that reflect progressively deteriorating credit risk. There are two classifications in the framework that apply to non-defaulted customers – Heightened Monitoring and Risk of Credit Loss. For the purposes of provisioning, all exposures subject to the framework are categorised as Stage 2 and subject to a lifetime loss assessment. The framework also applies to those customers that have met RBSI Group's default criteria (AQ10 exposures). Defaulted exposures are categorised as Stage 3 impaired for provisioning purposes.

Customers classified in the Heightened Monitoring category are those who are still performing but have certain characteristics – such as trading issues, covenant breaches, material PD downgrades and past due facilities – that may affect the ability to meet repayment obligations. Heightened Monitoring customers require pre-emptive actions to return or maintain their facilities within risk appetite prior to maturity. Risk of Credit Loss customers are performing customers that have met the criteria for Heightened Monitoring and also pose a risk of credit loss to RBSI Group in the next 12 months should mitigating action not be taken or not be successful.

Once classified as either Heightened Monitoring or Risk of Credit Loss, a number of mandatory actions are taken in accordance with policies. Actions include a review of the customer's credit grade, facility and security documentation and the valuation of security. Depending on the severity of the financial difficulty and the size of the exposure, the customer relationship strategy is reassessed by credit officers, by specialist credit risk or relationship management units in the relevant business, or by Restructuring.

Restructuring

Where customers are categorised as Risk of Credit Loss and the lending exposure is above £1 million, relationships are supported by the Restructuring team. The objective of Restructuring is to protect RBSI Group's capital. Restructuring does this by working with customers in financial difficulty to help them understand their options and how their restructuring or repayment strategies can be delivered. Helping the customer return to financial health and restoring a normal banking relationship is always the preferred outcome, however, where a solvent outcome is not possible, insolvency may be considered as a last resort.

Restructuring will always aim to recover capital fairly and efficiently. Throughout Restructuring's involvement, the mainstream relationship manager will remain an integral part of the customer relationship. Restructuring's work helps RBSI Group remain safe and sustainable, contributing to its ability to champion potential.

Forbearance

Forbearance takes place when a concession is made on the contractual terms of a loan/debt in response to a customer's financial difficulties.

The aim of forbearance is to support and restore the customer to financial health while minimising risk. To ensure that forbearance is appropriate for the needs of the customer, minimum standards are applied when assessing, recording, monitoring and reporting forbearance.

A credit exposure may be forborne more than once, generally where a temporary concession has been granted and circumstances warrant another temporary or permanent revision of the loan's terms.

Loans are reported as forborne until they meet the exit criteria as detailed in the appropriate regulatory guidance.

18. Risk management continued

Credit risk continued

Types of forbearance

Personal

In the Personal portfolio, forbearance may involve payment concessions and loan rescheduling (including extensions in contractual maturity) and capitalisation of arrears. Forbearance support is provided for both mortgages and unsecured lending.

Wholesale

In the Wholesale portfolio, forbearance may involve covenant waivers, amendments to margins, payment concessions and loan rescheduling (including extensions in contractual maturity), capitalisation of arrears, and debt forgiveness or debt-for-equity swaps.

Monitoring of forbearance

Personal

For Personal portfolios, forborne loans are separated and regularly monitored and reported while the forbearance strategy is implemented, until they exit forbearance.

Wholesale

In the Wholesale portfolio, customer PDs and facility LGDs are reassessed prior to finalising any forbearance arrangement. The ultimate outcome of a forbearance strategy is highly dependent on the co-operation of the borrower and a viable business or repayment outcome. Where forbearance is no longer appropriate, RBSI Group will consider other options such as the enforcement of security, insolvency proceedings or both, although these are options of last resort.

Provisioning requirements on forbearance are detailed in the Provisioning for forbearance section.

Credit grading models

Credit grading models is the collective term used to describe all models, frameworks and methodologies used to calculate PD, exposure at default (EAD), LGD, maturity and the production of credit grades. Credit grading models are designed to provide:

- An assessment of customer and transaction characteristics.
- A meaningful differentiation of credit risk.
- Accurate internal default rate, loss and exposure estimates that are used in the capital calculation or wider risk management purposes.

Impairment, provisioning and write-offs

In the overall assessment of credit risk, impairment provisioning and write-offs are used as key indicators of credit quality.

The approach that RBSI Group adopts in relation to the calculation of ECL within Personal includes the use of PD and LGD benchmarks. Refer to Personal non-modelled portfolio for further details.

RBSI Group's IFRS 9 provisioning models, which use existing Basel models as a starting point, incorporate term structures and forward-looking information. Regulatory conservatism within the Basel models has been removed as appropriate to comply with the IFRS 9 requirement for unbiased ECL estimates.

Five key areas may materially influence the measurement of credit impairment under IFRS 9 – two of these relate to model build and three relate to model application:

Model build:

- The determination of economic indicators that have most influence on credit loss for each portfolio and the severity of impact (this leverages existing stress testing models which are reviewed annually).
- The build of term structures to extend the determination of the risk of loss beyond 12 months that will influence the impact of lifetime loss for exposures in Stage 2.

Model application:

- The assessment of the SICR and the formation of a framework capable of consistent application.
- The determination of asset lifetimes that reflect behavioural characteristics while also representing management actions and processes (using historical data and experience).
- The choice of forward-looking economic scenarios and their respective probability weights.

IFRS 9 ECL model design principles

Modelling of ECL for IFRS 9 follows the conventional approach to divide the estimation of credit losses into its component parts of PD, LGD and EAD.

To meet IFRS 9 requirements, the PD, LGD and EAD parameters differ from their Pillar 1 internal ratings based counterparts in the following aspects:

- Unbiased – material regulatory conservatism has been removed from IFRS 9 parameters to produce unbiased estimates.
- Point-in-time – IFRS 9 parameters reflect actual economic conditions at the reporting date instead of long-run average or downturn conditions.
- Forward-looking – IFRS 9 PD estimates and, where appropriate, EAD and LGD estimates reflect forward-looking economic conditions.
- Lifetime measurement – IFRS 9 PD, LGD and EAD are provided as multi-period term structures up to exposure lifetimes instead of over a fixed one-year horizon.

IFRS 9 requires that at each reporting date, an entity shall assess whether the credit risk on an account has increased significantly since initial recognition. Part of this assessment requires a comparison to be made between the current lifetime PD (i.e. the PD over the remaining lifetime at the reporting date) and the equivalent lifetime PD as determined at the date of initial recognition.

For assets originated before IFRS 9 was introduced, comparable lifetime origination PDs did not exist. These have been retrospectively created using the relevant model inputs applicable at initial recognition.

18. Risk management continued

Credit risk continued

PD estimates

Wholesale PD models use a point-in-time/through-the-cycle framework to convert one-year regulatory PDs into point-in-time estimates that reflect economic conditions at the reporting date. The framework utilises credit cycle indices (CCIs) for a comprehensive set of region/industry segments. Further detail on CCIs is provided in the Economic loss drivers section.

One year point-in-time PDs are extended to forward-looking lifetime PDs using a conditional transition matrix approach and a set of econometric forecasting models.

LGD estimates

The general approach for the IFRS 9 LGD models is to leverage corresponding Basel LGD models with bespoke adjustments to ensure estimates are unbiased and, where relevant, forward-looking.

Forward-looking economic information is incorporated into Wholesale LGD estimates using the existing CCI framework. For low default portfolios, including sovereigns and banks, loss data is too scarce to substantiate estimates that vary with economic conditions. Consequently, for these portfolios, LGD estimates are assumed to be constant throughout the projection horizon.

EAD estimates

Personal

EAD is calculated as the maximum of the balance exposure, or limit which has been factored up by a credit conversion factor sourced from the benchmarked modelled portfolio.

Wholesale

For Wholesale, EAD values are projected using product specific credit conversion factors (CCFs), closely following the product segmentation and approach of the respective Basel model. However, the CCFs are estimated over multi-year time horizons and contain no regulatory conservatism or downturn assumptions.

No explicit forward-looking information is incorporated, on the basis of analysis showing the temporal variation in CCFs is mainly attributable to changes in exposure management practices rather than economic conditions.

Governance and post model adjustments

The IFRS 9 PD, EAD and LGD models are subject to NWG's model risk policy that stipulates periodic model monitoring, periodic re-validation and defines approval procedures and authorities according to model materiality. Various post model adjustments were applied where management judged they were necessary to ensure an adequate level of overall ECL provision. All post model adjustments were subject to formal approval through provisioning governance, and were categorised as follows:

- Deferred model calibrations – ECL adjustments where PD model monitoring indicated that actual defaults were below estimated levels but where it was judged that an implied ECL release was not supportable due to the influence of government support schemes. As a consequence, any potential ECL release was deferred and retained on the balance sheet.
- Economic uncertainty – ECL adjustments primarily arising from uncertainties associated with multiple economic scenarios (also for 2020) and credit outcomes as a result of the effect of COVID-19 and the consequences of government support schemes. In both cases, management judged that additional ECL was required until further credit performance data became available on the behavioural and loss consequences of COVID-19.
- Other adjustments – ECL adjustments where it was judged that the modelled ECL required to be amended.

Post model adjustments will remain a key focus area of NWG's ongoing ECL adequacy assessment process. A holistic framework has been established including reviewing a range of economic data, external benchmark information and portfolio performance trends. A key part of the assessment is also understanding the current levels of ECL coverage (portfolio by portfolio) against pre-COVID-19 levels, recognising changes in portfolio/sector mix.

ECL post model adjustments

The table below shows ECL post model adjustments.

	2021 £m	2020 £m
Deferred model calibrations	—	—
Economic uncertainty	17	7
Other adjustments	3	3
Total	20	10
Of which:		
-Stage 1	*2*	*2*
-Stage 2	*18*	*8*
-Stage 3	—	—

18. Risk management continued

Credit risk continued

Significant increase in credit risk (SICR)

Exposures that are considered significantly credit deteriorated since initial recognition are classified in Stage 2 and assessed for lifetime ECL measurement (exposures not considered deteriorated carry a 12 month ECL). RBSI Group has adopted a framework to identify deterioration based primarily on relative movements in lifetime PD supported by additional qualitative backstops. The principles applied are consistent across RBSI Group and align to credit risk management practices, where appropriate.

The framework comprises the following elements:

- IFRS 9 lifetime PD assessment (the primary driver) – on modelled portfolios the assessment is based on the relative deterioration in forward-looking lifetime PD and is assessed monthly. To assess whether credit deterioration has occurred, the residual lifetime PD at balance sheet date (which PD is established at date of initial recognition) is compared to the current PD. If the current lifetime PD exceeds the residual origination PD by more than a threshold amount, deterioration is assumed to have occurred and the exposure transferred into Stage 2 for a lifetime loss assessment. For Wholesale, a doubling of PD would indicate a SICR subject to a minimum PD uplift of 0.1%. For Personal portfolios, the criteria vary by risk band, with lower risk exposures needing to deteriorate more than higher risk exposures.

- Qualitative high-risk backstops – the PD assessment is complemented with the use of qualitative high-risk backstops to further inform whether significant deterioration in lifetime risk of default has occurred. The qualitative high-risk backstop assessment includes the use of the mandatory 30+ days past due backstop, as prescribed by IFRS 9 guidance, and other features such as forbearance support, Wholesale exposures managed within the Risk of Credit Loss framework, and adverse credit bureau results for Personal customers. Where a Personal customer was granted a payment holiday (also referred to as a payment deferral) in response to COVID-19, they were not automatically transferred into Stage 2.

The criteria are based on a significant amount of empirical analysis and seek to meet three key objectives:

- Criteria effectiveness – the criteria should be effective in identifying significant credit deterioration and prospective default population.
- Stage 2 stability – the criteria should not introduce unnecessary volatility in the Stage 2 population.
- Portfolio analysis – the criteria should produce results which are intuitive when reported as part of the wider credit portfolio.

Provisioning for forbearance

Personal

The methodology used for provisioning in respect of Personal forborne loans will differ depending on whether the loans are performing or non-performing and which business is managing them due to local market conditions.

Granting forbearance will only change the arrears status of the loan in specific circumstances, which can include capitalisation of principal and interest in arrears, where the loan may be returned to the performing book if the customer has demonstrated an ability to meet regular payments and is likely to continue to do so.

The loan would continue to be reported as forborne until it meets the exit criteria set out by the European Banking Authority.

For ECL provisioning, all forborne but performing exposures are categorised as Stage 2 and are subject to a lifetime loss provisioning assessment. Where the forbearance treatment includes the cessation of interest on the customer balance (i.e. non-accrual), this will be treated as a Stage 3 default.
For non-performing forborne loans, the Stage 3 loss assessment process is the same as for non-forborne loans.

In the absence of any other forbearance or SICR triggers, customers granted COVID-19 related payment holidays were not considered forborne. However, any support provided beyond completion of a second payment holiday is considered forbearance.

Wholesale

Provisions for forborne loans are assessed in accordance with normal provisioning policies. The customer's financial position and prospects – as well as the likely effect of the forbearance, including any concessions granted, and revised PD or LGD gradings – are considered in order to establish whether an impairment provision increase is required.

Wholesale loans granted forbearance are individually credit assessed in most cases. Performing loans subject to forbearance treatment are categorised as Stage 2 and subject to a lifetime loss assessment. Forbearance may result in the value of the outstanding debt exceeding the present value of the estimated future cash flows. This difference will lead to a customer being classified as non-performing.

In the case of non-performing forborne loans, an individual loan impairment provision assessment generally takes place prior to forbearance being granted. The amount of the loan impairment provision may change once the terms of the forbearance are known, resulting in an additional provision charge or a release of the provision in the period the forbearance is granted.

The transfer of Wholesale loans from impaired to performing status follows assessment by relationship managers and credit. When no further losses are anticipated and the customer is expected to meet the loan's revised terms, any provision is written-off or released and the balance of the loan returned to performing status. This is not dependent on a specified time period and follows the credit risk manager's assessment.

Customers seeking COVID-19 related support, including payment holidays, who were not subject to any wider SICR triggers and who were assessed as having the ability in the medium term post-COVID-19 to be viable and meet credit appetite metrics, were not considered to have been granted forbearance.

18. Risk management continued

Credit risk continued

Asset lifetimes

The choice of initial recognition and asset duration is another critical judgment in determining the quantum of lifetime losses that apply. The date of initial recognition reflects the date that a transaction (or account) was first recognised on the balance sheet; the PD recorded at that time provides the baseline used for subsequent determination of SICR as detailed above. For asset duration, the approach applied for term lending (in line with IFRS 9 requirements) is the contractual maturity date, reduced for behavioural trends where appropriate (such as, expected prepayment and amortisation).

Personal non-modelled portfolio

RBSI Personal remains Basel standardised for risk-weighted assets, therefore modelled PDs and LGDs are not available for calculating Stage 1 and Stage 2 ECLs. Instead, this is performed by sourcing the equivalent product PD and LGD from elsewhere in NWG, which was identified as the closest comparable portfolio to RBSI Personal. The PD and LGD benchmarks are then used, along with the known exposure, to calculate an account level ECL.

In order to identify accounts showing Stage 2 the RBSI Personal Watch classification is applied where accounts are identified as having clear signs of credit deterioration, increased risk of default or have been given forbearance, with days past due being checked as supplementary back stop.

Economic loss drivers

Introduction

The portfolio segmentation and selection of economic loss drivers for IFRS 9 follow closely the approach used in stress testing. To enable robust modelling the forecasting models for each portfolio segment (defined by product or asset class and where relevant, industry sector and region) are based on a selected, small number of economic factors, (typically three to four) that best explain the temporal variations in portfolio loss rates. The process to select economic loss drivers involves empirical analysis and expert judgment.

The most material economic loss drivers for the Personal portfolios include unemployment rate, house price index, and base rate for the UK, and these are applied to credit portfolios across all jurisdictions.

In addition to some of these loss drivers, world GDP is a primary loss driver for the Wholesale portfolios.

Economic scenarios

At 31 December 2021, the range of anticipated future economic conditions was defined by a set of four internally developed scenarios and their respective probabilities. In addition to the base case, they comprised upside, downside and extreme downside scenarios. The scenarios primarily reflected a range of outcomes for the path of COVID-19 as well as recovery, and the associated effects on labour and asset markets.

The four scenarios were deemed appropriate in capturing the uncertainty in economic forecasts and the non-linearity in outcomes under different scenarios. The scenarios were developed to provide sufficient coverage across potential changes in unemployment, asset price and the degree of permanent damage to the economy, around which there are pronounced levels of uncertainty at this stage.

Upside – This scenario assumes a very strong recovery through 2022 as consumers dip into excess savings built up over the last two years. The labour market remains resilient, with the unemployment rate falling below pre-COVID-19 levels. Inflation is higher than the base case but eventually comes back close to the target. The strong economic recovery enables tightening to be quicker than the base case. The housing market continues its recent strong performance.

Base case – COVID-19 related risks remain contained. After a strong recovery in 2021, the growth moderates in 2022. Most of the furloughed workers can go back to their existing job or find a new job very quickly, with the unemployment rate reaching 4.1% by the end of 2022. Inflation initially increases but retreats over 2022. Interest rates are raised, starting in early 2022. There is a gradual cool down in the housing market but activity is still at healthy levels.

Downside – This scenario assumes a reversal in recovery as inflation build up leads to a lessening of expectations. Interest rates are raised aggressively to counter the inflation risks. However, starting in 2023, the interest hikes are reversed to assist the recovery. Unemployment is higher than the base case and there is a modest decline in house prices.

Extreme downside – This scenario assumes a resurgence of COVID-19 related risks. There is a renewed downturn with declines in consumer spending and business investment. Interest rates are reduced into negative territory to -0.5%. There is wide-spread job shedding in the labour market while asset prices see deep corrections, with housing market falls higher than those seen during previous episodes. The recovery is tepid throughout the five-year period, meaning only a gradual decline in joblessness.

The approach of using four scenarios is similar to that as at 31 December 2020. Previously, RBSI Group used five discrete scenarios to characterise the distribution of risks in the economic outlook. For 2021, the four scenarios were deemed appropriate in capturing the uncertainty in economic forecasts and the non-linearity in outcomes under different scenarios. These four scenarios were developed to provide sufficient coverage across potential rises in unemployment, inflation, asset price falls and the degree of permanent damage to the economy, around which there remains pronounced levels of uncertainty.

The tables and commentary below provide details of the key economic loss drivers under the four scenarios.

The main macroeconomic variables for each of the four scenarios used for ECL modelling are set out in the main macroeconomic variables table below. The compound annual growth rate (CAGR) for GDP is shown. It also shows the five-year average for unemployment and the Bank of England base rate. The house price index and commercial real estate figures show the total change in each asset over five years.

18. Risk management continued

Credit risk continued

Main macroeconomic variables	2021				2020			
	Upside	Base case	Downside	Extreme downside	Upside	Base case	Downside	Extreme downside
Five-year summary	%	%	%	%	%	%	%	%
GDP - CAGR	2.4	1.7	1.4	0.6	3.6	3.1	2.8	1.3
Unemployment - average	3.5	4.2	4.8	6.7	4.4	5.7	7.1	9.7
House price index - total change	22.7	12.1	4.3	(5.3)	12.5	7.6	4.4	(19.0)
Bank of England base rate - average	1.5	0.8	0.7	(0.5)	0.2	—	(0.1)	(0.5)
World GDP - CAGR	3.5	3.2	2.6	0.6	3.5	3.4	2.9	2.8
Probability weight	30.0	45.0	20.0	5.0	20.0	40.0	30.0	10.0

(1) The five year period starts after Q3 2021 for 2021 and Q3 2020 for 2020.

Probability weightings of scenarios

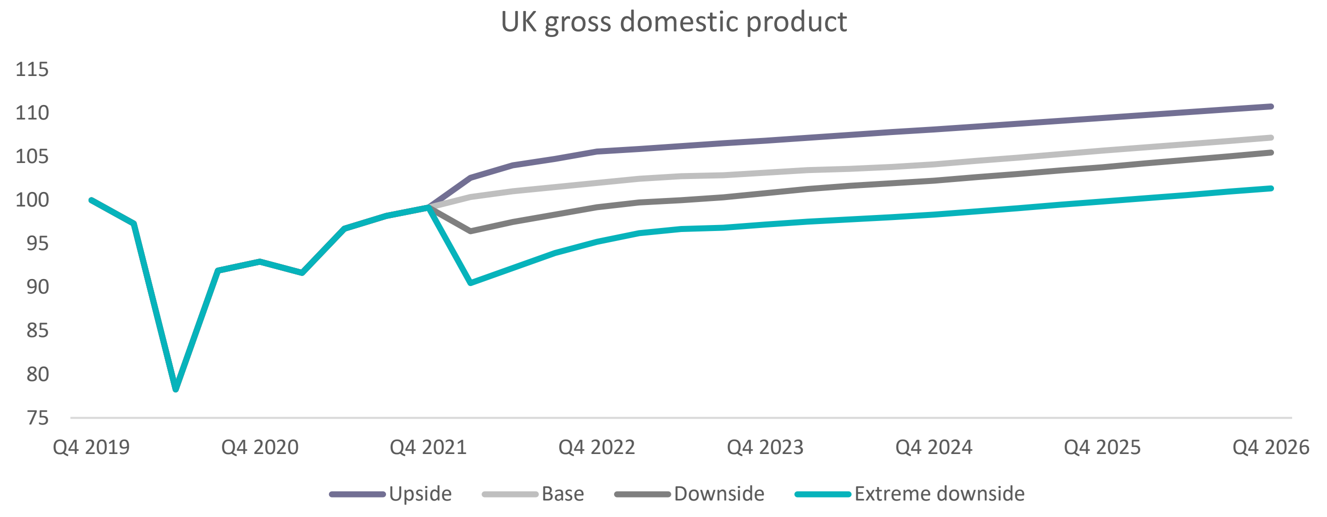
RBSI Group's approach to IFRS 9 multiple economic scenarios (MES) involves selecting a suitable set of discrete scenarios to characterise the distribution of risks in the economic outlook and assigning appropriate probability weights. The scale of the economic impact of COVID-19 and the range of recovery paths necessitates a change of approach to assigning probability weights from that used in recent updates. Prior to 2020, GDP paths for RBSI Group's scenarios were compared against a set of 1,000 model runs, following which a percentile in the distribution was established that most closely corresponded to the scenario.

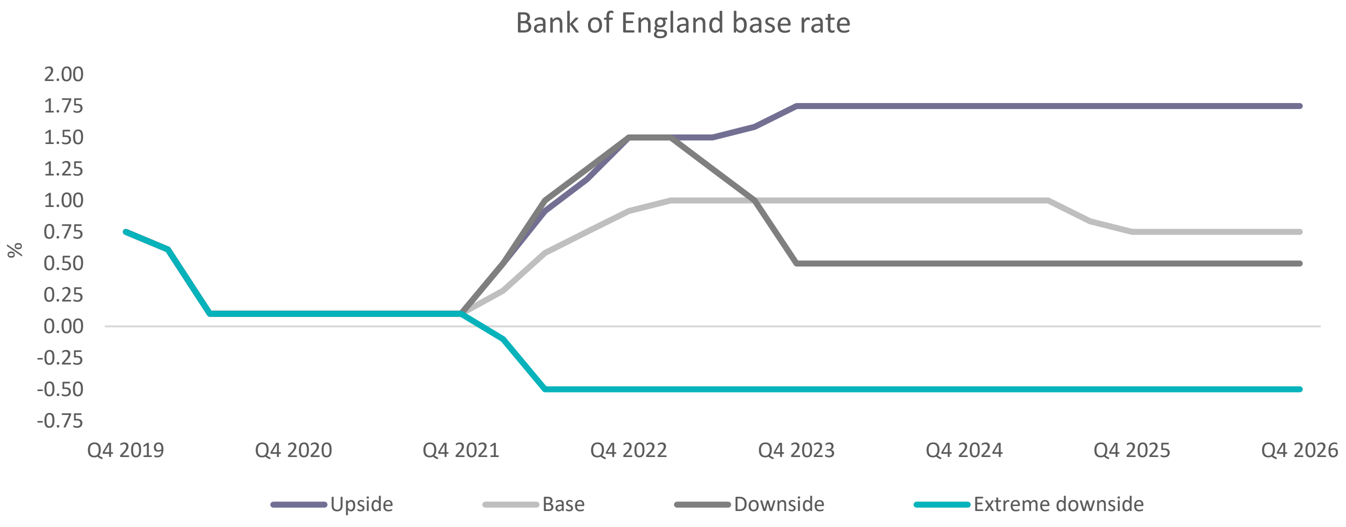
Instead, RBSI Group has subjectively applied probability weights, reflecting internal expert views. The probability weight assignment was judged to present good coverage to the central scenarios and the potential for a robust recovery on the upside and exceptionally challenging outcomes on the downside. A 30% weighting was applied to the upside scenario, a 45% weighting applied to the base case scenario, a 20% weighting applied to the downside scenario and a 5% weighting applied to the extreme downside scenario. RBSI Group assessed the downside risk posed by COVID-19 to be diminishing over the course of 2021, with the vaccination roll-out and positive economic data being observed since the gradual relaxing of lockdown restrictions. RBSI Group therefore judged it was appropriate to apply a higher probability to upside-biased scenarios than at 31 December 2020. However, compared to 31 December 2020, the base case has a higher weight reflecting reduction in uncertainty as the path of economy recovery became clearer.

The 25% weighting to the two downside scenarios gives appropriate consideration to the threats posed to the recovery, including inflation, supply and COVID-19-related risks. Balanced against that is the adaptability of the UK economy to successive waves of COVID-19, and the resilience of labour and asset markets. The potential for further better than expected outcomes is reflected in the 30% probability weighting applied to the upside scenario.

18. Risk management continued

Credit risk continued





18. Risk management continued

Credit risk continued

GDP - annual growth

	Upside %	Base case %	Downside %	Extreme downside %
2021	7.0	7.0	7.0	7.0
2022	8.1	5.0	1.5	(3.6)
2023	2.1	1.6	2.4	4.1
2024	1.2	0.9	1.6	1.2
2025	1.2	1.3	1.4	1.4
2026	1.2	1.5	1.6	1.5

Unemployment rate - annual average

	Upside %	Base case %	Downside %	Extreme downside %
2021	4.6	4.6	4.6	4.6
2022	3.5	4.1	5.1	8.3
2023	3.3	4.0	5.2	8.8
2024	3.4	4.1	4.7	6.6
2025	3.4	4.2	4.5	5.2
2026	3.6	4.2	4.5	4.9

House price index - four quarter growth

	Upside %	Base case %	Downside %	Extreme downside %
2021	6.9	6.9	6.9	6.9
2022	7.9	1.6	(2.9)	(20.4)
2023	4.2	1.6	(0.2)	(2.6)
2024	3.1	2.9	1.7	13.0
2025	3.0	2.7	3.0	4.7
2026	3.0	2.7	3.0	3.6

Bank of England base rate - annual average

	Upside %	Base case %	Downside %	Extreme downside %
2021	0.10	0.10	0.10	0.10
2022	1.02	0.63	1.06	(0.40)
2023	1.58	1.00	1.06	(0.50)
2024	1.75	1.00	0.50	(0.50)
2025	1.75	0.90	0.50	(0.50)
2026	1.75	0.75	0.50	(0.50)

18. Risk management continued

Credit risk continued

Worst points

UK	31 December 2021 Downside %	Quarter	Extreme downside %	Quarter	31 December 2020 Downside %	Quarter	Extreme downside %	Quarter
GDP	(1.8)	Q1 2022	(7.9)	Q1 2022	(5.1)	Q1 2021	(10.4)	Q1 2021
Unemployment rate (peak)	5.4	Q1 2023	9.4	Q4 2022	9.4	Q4 2021	13.9	Q3 2021
House price index	(3.0)	Q3 2023	(26.0)	Q2 2023	(11.2)	Q2 2021	(32.0)	Q4 2021
Bank of England base rate	1.5	Q4 2022	(0.5)	Q2 2022	(0.1)	Q3 2021	(0.5)	Q1 2021

(1) For the unemployment rate, the figures show the peak levels. For the Bank of England base rate, the figures show highest or lowest levels. For other parameters, the figures show falls relative to the starting period. The calculations are performed over five years, with a starting point of Q3 2021 for 31 December 2021 scenarios.

Use of the scenarios in Personal lending

Personal lending follows a discrete scenario approach. The PD and LGD values for each discrete scenario are calculated using product specific econometric models. Each account has a PD and LGD calculated as probability weighted averages across the suite of economic scenarios.

Use of the scenarios in Wholesale lending

The Wholesale lending ECL methodology is based on the concept of credit cycle indices (CCIs). The CCIs represent, similar to the exogenous component in Personal, all relevant economic loss drivers for a region/industry segment aggregated into a single index value that describes the loss rate conditions in the respective segment relative to its long-run average. A CCI value of zero corresponds to loss rates at long-run average levels, a positive CCI value corresponds to loss rates below long run average levels and a negative CCI value corresponds to loss rates above long-run average levels.

The four economic scenarios are translated into forward-looking projections of CCIs using a set of econometric models. Subsequently the CCI projections for the individual scenarios are averaged into a single central CCI projection according to the given scenario probabilities. The central CCI projection is then overlaid with an additional mean reversion assumption i.e. that after reaching their worst forecast position the CCIs start to gradually revert to their long run average of zero.

Finally, ECL is calculated using a Monte Carlo approach by averaging PD and LGD values arising from many CCI paths simulated around the central CCI projection.

The rationale for the Wholesale approach is the long-standing observation that loss rates in Wholesale portfolios tend to follow regular cycles. This allows RBSI Group to enrich the range and depth of future economic conditions embedded in the final ECL beyond what would be obtained from using the discrete macro-economic scenarios alone.

UK economic uncertainty

Treatment of COVID-19 relief mechanisms

Use of COVID-19 relief mechanisms (for example, the Disruption Guarantee Scheme) does not automatically merit identification of a SICR and trigger a Stage 2 classification in isolation.

For Wholesale customers, RBSI Group continues to provide support, where appropriate, to existing customers. Those who are deemed either (a) to require a prolonged timescale to return to within RBSI Group's risk appetite, (b) not to have been viable pre-COVID-19, or (c) not to be able to sustain their debt once COVID-19 is over, will trigger a SICR and, if concessions are sought, be categorised as forborne, in line with regulatory guidance. Payment holiday extensions beyond an aggregate of 12 months in an 18 month period to cover continuing COVID-19 business interruption are categorised as forbearance, including for customers where no other SICR triggers are present.

18. Risk management continued

Credit risk continued

Model monitoring and enhancement

The severe economic impact from COVID-19 and the ensuing government support schemes have disrupted the normal relationships between key economic loss drivers and credit outcomes. While most government support schemes have now been phased out and economic conditions are normalising, the effect of this disruption is still evident in model monitoring and accounted for in judgments applied to the use and recalibrations of models.

Most significantly, latest PD model monitoring shows general overprediction across all key portfolios, i.e., observed default rates still at or even below pre-COVID-19 levels despite increased PD estimates from a deterioration in several key economic variables. Model recalibrations to adjust for this overprediction have been deferred based on the judgment that default rate actuals are distorted due to government support.

In addition, to account for residual model uncertainty and the risk of eventual default emergence hitherto supressed by government support, lag assumptions of up to 12 months are applied in the models. These assumptions are consistent with and unchanged from previous disclosures in 2021, although their effective impact gradually reduces over time.

Industry sector detail – Wholesale only

The economic impact of COVID-19 is highly differentiated by industry sector, with hospitality and other contact-based leisure, service, travel and passenger transport activities significantly more affected than the overall economy. Additional post model adjustments, in specific sectors, were recognised where a risk of higher than expected future default levels, including their timing and value, was identified.

Scenario sensitivity – Personal only

For the NatWest UK modelled Personal portfolio, from which PDs and LGDs are sourced to facilitate the calculation of ECL in RBSI Personal, the forward-looking components of the IFRS 9 PD models continue to be modified, leveraging existing econometric models used in stress testing to ensure that PDs appropriately reflect the forecasts for unemployment and house prices in particular.

Additionally, post model ECL adjustments were made in Personal to account for known model weaknesses pre-dating COVID-19, pending the systematic re-development of the underlying models.

Measurement uncertainty and ECL sensitivity analysis

The recognition and measurement of ECL is complex and involves the use of significant judgment and estimation, particularly in times of economic volatility and uncertainty. This includes the formulation and incorporation of multiple forward-looking economic conditions into ECL to meet the measurement objective of IFRS 9. The ECL provision is sensitive to the model inputs and economic assumptions underlying the estimate.

The focus of the simulations is on ECL provisioning requirements on performing exposures in Stage 1 and Stage 2. The simulations are run on a stand-alone basis and are independent of each other; the potential ECL impacts reflect the simulated impact at 31 December 2021. Scenario impacts on SICR should be considered when evaluating the ECL movements of Stage 1 and Stage 2. In all scenarios the total exposure was the same but exposure by stage varied in each scenario.

Stage 3 provisions are not subject to the same level of measurement uncertainty – default is an observed event as at the balance sheet date. Stage 3 provisions therefore have not been considered in this analysis.

The impact arising from the base case, upside, downside and extreme downside scenarios has been simulated. These scenarios are three of the four discrete scenarios used in the methodology for Personal multiple economic scenarios as described in the Economic loss drivers section. In the simulations, RBSI Group has assumed that the economic macro variables associated with these scenarios replace the existing base case economic assumptions, giving them a 100% probability weighting and therefore serving as a single economic scenario.

These scenarios have been applied to all modelled portfolios in the analysis below, with the simulation impacting both PDs and LGDs. Modelled post model adjustments present in the underlying ECL estimates are also sensitised in line with the modelled ECL movements, but those that were judgmental in nature, primarily those for deferred model calibrations and economic uncertainty, were not (refer to the Governance and post model adjustments section). As expected, the scenarios create differing impacts on ECL by portfolio and the impacts are deemed reasonable. In this simulation, it is assumed that existing modelled relationships between key economic variables and loss drivers hold, but in practice other factors would also have an impact, for example, potential customer behaviour changes and policy changes by lenders that might impact on the wider availability of credit.

RBSI Group's core criterion to identify a SICR is founded on PD deterioration, as discussed above. Under the simulations, PDs change and result in exposures moving between Stage 1 and Stage 2 contributing to the ECL impact.

18. Risk management continued

Credit risk continued

	Group and Bank				
2021	Actual	Base case	Upside	Downside	Extreme Downside
Stage 1 modelled exposure (£m)					
Commercial	10,019	10,027	10,027	10,027	9,577
Stage 1 modelled ECL (£m)					
Commercial	5	4	4	4	4
Stage 1 coverage (%)					
Commercial	0.05%	0.04%	0.04%	0.04%	0.04%
Stage 2 modelled exposure (£m)					
Commercial	506	498	498	498	948
Stage 2 modelled ECL (£m)					
Commercial	22	22	22	22	30
Stage 2 coverage (%)					
Commercial	4.35%	4.42%	4.42%	4.42%	3.16%
Stage 1 and Stage 2 modelled exposure (£m)					
Commercial	10,525	10,525	10,525	10,525	10,525
Stage 1 and Stage 2 modelled ECL (£m)					
Commercial	27	26	26	26	34
Stage 1 and Stage 2 coverage (%)					
Commercial	0.26%	0.25%	0.25%	0.25%	0.32%
Reconciliation to Stage 1 and Stage 2 ECL (£m)					
ECL on modelled exposures	27	26	26	26	34
ECL on non-modelled exposures	4	4	4	4	4
Total Stage 1 and Stage 2 ECL	31	30	30	30	38
Variance to actual total Stage 1 and Stage 2 ECL		(1)	(1)	(1)	7

(1) Reflects ECL for all modelled exposure in scope for IFRS 9. The analysis excludes non-modelled portfolios and exposure relating to bonds and cash.
(2) All simulations are run on a stand-alone basis and are independent of each other, with the potential ECL impact reflecting the simulated impact as at 31 December 2021.
(3) Refer to the Economic loss drivers section for details of economic scenarios.
(4) Refer to the RBSI Group 2020 Annual Report and Accounts for 2020 comparatives.

Measurement uncertainty and ECL adequacy

The improvement in the economic outlook and scenarios used in the IFRS 9 MES framework in 2021 resulted in a release of modelled ECL. Given that continued uncertainty remains due to COVID-19 despite the improved economic outlook, RBSI Group utilised a framework of quantitative and qualitative measures to support the directional change and levels of ECL coverage, including economic data, credit performance insights and problem debt trends. This was particularly important for consideration of post model adjustments.

As government support schemes continued to conclude during 2021, RBSI Group anticipates further credit deterioration in the portfolios. However, the income statement effect of this will be mitigated by the forward-looking provisions retained on the balance sheet at 31 December 2021.

There are a number of key factors that could drive further downside to impairments, through deteriorating economic and credit metrics and increased stage migration as credit risk increases for more customers. A key factor would be a more adverse deterioration in GDP and unemployment in the economies in which RBSI Group operates, but also, among others:

- The ongoing trajectory of lockdown restrictions and any future repeated lockdown requirements.
- The progress of the COVID-19 vaccination roll-out and its effectiveness against new variants.
- The long-term efficacy of the various government support schemes in terms of their ability to defray customer defaults is yet to be proven over an extended period.
- The impact on customer affordability in the event of sustained inflationary pressures.
- The level of revenues lost by corporate clients and pace of recovery of those revenues may affect RBSI Group's clients' ability to service their borrowing, especially in those sectors most exposed to the effects of COVID-19.

18. Risk management continued

Credit risk continued

Financial instruments within the scope of the IFRS 9 ECL framework

Refer to Note 7 for balance sheet analysis of financial assets that are classified as amortised cost or fair value through other comprehensive income (FVOCI), the starting point for IFRS 9 ECL framework assessment.

Financial assets

	Group					
	31 December 2021			31 December 2020		
	Gross £m	ECL £m	Net £m	Gross £m	ECL £m	Net £m
Balance sheet total gross amortised cost and FVOCI	39,963			33,516		
In scope of IFRS 9 ECL framework	39,980			33,410		
% in scope	100.0%			99.7%		
Loans to customers - in scope - amortised cost	15,519	54	15,465	13,365	135	13,230
Loans to customers - in scope - FVOCI	—	—	—	—	—	—
Loans to banks - in scope - amortised cost	1,305	—	1,305	1,231	—	1,231
Total loans - in scope	16,824	54	16,770	14,596	135	14,461
Stage 1	16,185	7	16,178	12,143	13	12,130
Stage 2	477	23	454	2,242	74	2,168
Stage 3	162	24	138	211	48	163
Other financial assets - in scope - amortised cost	19,954	1	19,953	17,039	1	17,038
Other financial assets - in scope - FVOCI	3,202	—	3,202	1,775	—	1,775
Total other financial assets - in scope	23,156	1	23,155	18,814	1	18,813
Stage 1	23,156	1	23,155	18,814	1	18,813
Stage 2	—	—	—	—	—	—
Stage 3	—	—	—	—	—	—
Out of scope of IFRS 9 ECL framework	(17)	na	(17)	106	na	106
Loans to customers - out of scope - amortised cost	(3)	na	(3)	26	na	26
Loans to banks - out of scope - amortised cost	—	na	—	—	na	—
Other financial assets - out of scope - amortised cost	54	na	54	60	na	60
Other financial assets - out of scope - FVOCI	(68)	na	(68)	20	na	20

na = not applicable

18. Risk management continued
Credit risk continued

	Bank					
	31 December 2021			31 December 2020		
	Gross £m	ECL £m	Net £m	Gross £m	ECL £m	Net £m
Balance sheet total gross amortised cost and FVOCI	39,936			33,489		
In scope of IFRS 9 ECL framework	39,953			33,384		
% in scope	100.0%			99.7%		
Loans to customers - in scope - amortised cost	15,519	54	15,465	13,365	135	13,230
Loans to customers - in scope - FVOCI	—	—	—	—	—	—
Loans to banks - in scope - amortised cost	1,278	—	1,278	1,205	—	1,205
Total loans - in scope	16,797	54	16,743	14,570	135	14,435
Stage 1	16,158	7	16,151	12,143	13	12,130
Stage 2	477	23	454	2,216	74	2,142
Stage 3	162	24	138	211	48	163
Other financial assets - in scope - amortised cost	19,954	1	19,953	17,039	1	17,038
Other financial assets - in scope - FVOCI	3,202	—	3,202	1,775	—	1,775
Total other financial assets - in scope	23,156	1	23,155	18,814	1	18,813
Stage 1	23,156	1	23,155	18,814	1	18,813
Stage 2	—	—	—	—	—	—
Stage 3	—	—	—	—	—	—
Out of scope of IFRS 9 ECL framework	(17)	na	(17)	105	na	105
Loans to customers - out of scope - amortised cost	(3)	na	(3)	26	na	26
Loans to banks - out of scope - amortised cost	—	na	—	—	na	—
Other financial assets - out of scope - amortised cost	54	na	54	60	na	60
Other financial assets - out of scope - FVOCI	(68)	na	(68)	20	na	20

na = not applicable

The assets outside the IFRS 9 ECL framework were as follows:
- Settlement balances, items in the course of collection, cash balances and other non-credit risk assets of £(17) million (2020 – £105 million). These were assessed as having no ECL unless there was evidence that they were defaulted.
- Equity shares of nil (2020 – £1 million) as not within the IFRS 9 ECL framework by definition.

In scope assets also include £579 million (2020 – £637 million) of inter-Group assets not shown in the Group table above and £577 million (2020 – £646 million) of inter-Group assets not shown in the Bank table above.

Contingent liabilities and commitments
In addition to contingent liabilities and commitments disclosed in Note 19 to the consolidated financial statements, reputationally-committed limits were also included in the scope of the IFRS 9 ECL framework. Total contingent liabilities (including financial guarantees) and commitments within IFRS 9 ECL scope were £9,613 million (2020 – £9,642 million), comprised Stage 1 £9,390 million (2020 – £8,601 million); Stage 2 £222 million (2020 – £1,037 million); and Stage 3 £1 million (2020 – £4 million).

The total ECL in the remainder of the credit risk section of £55 million included ECL for both on and off balance sheet exposures.

18. Risk management continued

Credit risk continued

Flow statements

The flow statements that follow show the main ECL and related income statement movements. They also show the changes in ECL as well as the changes in related financial assets used in determining ECL. Due to differences in scope, exposures may differ from those reported in other tables, principally in relation to exposures in Stage 1 and Stage 2. These differences do not have a material ECL effect. Other points to note:

- Financial assets include treasury liquidity portfolios, comprising balances at central banks and debt securities, as well as loans. Both modelled and non-modelled portfolios are included.
- Stage transfers (for example, exposures moving from Stage 1 into Stage 2) are a key feature of the ECL movements, with the net re-measurement cost of transitioning to a worse stage being a primary driver of income statement charges. Similarly, there is an ECL benefit for accounts improving stage.
- Changes in risk parameters shows the reassessment of the ECL within a given stage, including any ECL overlays and residual income statement gains or losses at the point of write-off or accounting write-down.
- Other (P&L only items) includes any subsequent changes in the value of written-down assets (for example, fortuitous recoveries) along with other direct write-off items such as direct recovery costs. Other (P&L only items) affects the income statement but does not affect balance sheet ECL movements.
- Amounts written-off represent the gross asset written-down against accounts with ECL, including the net asset write-down for any debt sale activity.
- There were small ECL flows from Stage 3 into Stage 1. This does not, however, indicate that accounts returned from Stage 3 to Stage 1 directly. On a similar basis, there were flows from Stage 1 to Stage 3 including transfers due to unexpected default events. The small number of write-offs in Stage 1 and Stage 2 reflect the effect of portfolio debt sales and also staging at the start of the analysis period.
- The effect of any change in post model adjustments during the year is typically reported under changes in risk parameters, as are any effects arising from changes to the underlying models. Refer to the section on Governance and post model adjustments for further details.
- All movements are captured monthly and aggregated. Interest suspended post default is included within Stage 3 ECL with the movement in the value of suspended interest during the year reported under currency translation and other adjustments.

	Group							
	Stage 1		Stage 2		Stage 3		Total	
	Loans	ECL	Loans	ECL	Loans	ECL	Loans	ECL
RBS International	£m	£m	£m	£m	£m	£m	£m	£m
At 1 January 2021	29,310	14	2,073	74	213	48	31,596	136
Currency translation and other adjustments	(645)	32	(1)	(35)	(2)	1	(647)	(2)
Transfers from Stage 1 to Stage 2	(885)	(3)	885	3			—	—
Transfers from Stage 2 to Stage 1	2,333	33	(2,333)	(33)			—	—
Transfers to Stage 3	(26)	(0)	(73)	(6)	99	6	—	—
Transfers from Stage 3	28	1	52	2	(80)	(3)	—	—
Income statement (releases)/charges	9,257	(39)	(47)	(16)	(81)	3	9,129	(52)
Amounts written-off					(28)	(28)	(28)	(28)
At 31 December 2021	39,372	7	557	23	121	24	40,050	54
Net carrying amount	39,365		534		97		39,996	
At 1 January 2020	33,448	3	648	6	135	21	34,231	30
2020 movements	(4,138)	11	1,425	68	78	27	(2,635)	106
At 31 December 2020	29,310	14	2,073	74	213	48	31,596	136
Net carrying amount	29,296		1,999		165		31,460	

	Bank							
	Stage 1		Stage 2		Stage 3		Total	
	Loans	ECL	Loans	ECL	Loans	ECL	Loans	ECL
RBS International	£m	£m	£m	£m	£m	£m	£m	£m
At 1 January 2021	29,310	14	2,046	74	213	48	31,569	136
Currency translation and other adjustments	(645)	32	26	(35)	(2)	1	(620)	(2)
Transfers from Stage 1 to Stage 2	(885)	(3)	885	3			—	—
Transfers from Stage 2 to Stage 1	2,333	33	(2,333)	(33)			—	—
Transfers to Stage 3	(26)	(0)	(73)	(6)	99	6	—	—
Transfers from Stage 3	28	1	52	2	(80)	(3)	—	—
Income statement (releases)/charges	9,257	(39)	(47)	(16)	(81)	3	9,129	(52)
Amounts written-off					(28)	(28)	(28)	(28)
At 31 December 2021	39,372	7	557	23	121	24	40,050	54
Net carrying amount	39,365		534		97		39,996	—
At 1 January 2020	33,448	3	648	6	135	21	34,231	30
2020 movements	(4,138)	11	1,398	68	78	27	(2,662)	106
At 31 December 2020	29,310	14	2,046	74	213	48	31,569	136
Net carrying amount	29,296		1,972		165		31,433	

(1) Related financial asset movements are one month in arrears relative to the balance sheet reporting dates, as these are the balances used to calculate the modelled ECL (i.e. reported financial assets at 1 January 2021 in the flow statements reflect 30 November 2020 positions, and 31 December 2021 reported figures reflect 30 November 2021 positions).

18. Risk management continued

Credit risk continued

Stage 2 decomposition – arrears status and contributing factors

The tables below show Stage 2 decomposition for the Wholesale portfolios.

31 December 2021	Property Loans £m	Property ECL £m	Corporate Loans £m	Corporate ECL £m	FI Loans £m	FI ECL £m	Wholesale Loans £m	Wholesale ECL £m
Wholesale								
Currently in arrears (>30DPD)	16	—	1	—	—	—	17	—
Currently up-to-date	240	17	119	5	52	—	411	22
- PD deterioration	100	8	55	3	37	—	192	11
- Up-to-date, PD persistence	—	—	—	—	—	—	—	—
- Other driver (forbearance, RoCL etc.)	140	9	64	2	15	—	219	11
Total Stage 2	256	17	120	5	52	—	428	22

31 December 2020	Property Loans £m	Property ECL £m	Corporate Loans £m	Corporate ECL £m	FI Loans £m	FI ECL £m	Wholesale Loans £m	Wholesale ECL £m
Wholesale								
Currently in arrears (>30DPD)	6	1	1	—	—	—	7	1
Currently up-to-date	1,279	57	135	10	772	5	2,186	72
- PD deterioration	1,236	56	109	8	611	3	1,956	67
- Up-to-date, PD persistence	—	—	—	—	—	—	—	—
- Other driver (forbearance, RoCL etc.)	43	1	26	2	161	2	230	5
Total Stage 2	1,285	58	136	10	772	5	2,193	73

This section shows the credit risk profile of trading activities.

31 December 2021	Reverse repos Total £m	Reverse repos of which offsettable £m	Reverse repos Outside netting arrangements £m	Repos Total £m	Repos of which offsettable £m	Repos Outside netting arrangements £m
Gross	1,262	1,262	—	1,262	1,262	—
IFRS offset	(1,262)	(1,262)	—	(1,262)	(1,262)	—
Carrying value	—	—	—	—	—	—
Securities collateral	1,262	—	—	1,262	—	—

31 December 2020	Reverse repos Total £m	Reverse repos of which offsettable £m	Reverse repos Outside netting arrangements £m	Repos Total £m	Repos of which offsettable £m	Repos Outside netting arrangements £m
Gross	1,017	1,017	—	1,017	1,017	—
IFRS offset	(1,017)	(1,017)	—	(1,017)	(1,017)	—
Carrying value	—	—	—	—	—	—
Securities collateral	1,017	—	—	1,017	—	—

18. Risk management continued

Credit risk continued

Credit risk enhancement and mitigation

The table below shows exposures of modelled portfolios within the scope of the ECL framework and related credit risk enhancement and mitigation (CREM).

	Group										
	Gross		Maximum credit risk		CREM by type [3]			CREM coverage		Exposure post CREM	
	exposure	ECL	Total	Stage 3	Financial [1]	Property	Other [2]	Total	Stage 3	Total	Stage 3
2021	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Financial assets											
Cash and balances at central banks	17,165	—	17,165	—	—	—	—	—	—	17,165	—
Loans - amortised cost	16,824	52	16,772	138	727	4,326	27	5,080	87	11,692	51
Personal	2,753	13	2,740	47	257	2,394	—	2,651	45	89	2
Wholesale	14,071	39	14,032	91	470	1,932	27	2,429	42	11,603	49
Debt securities	5,991	1	5,990	—	—	—	—	—	—	5,990	—
Total financial assets	39,980	53	39,927	138	727	4,326	27	5,080	87	34,847	51
Contingent liabilities and commitments											
Personal	215	—	215	—	—	—	—	—	—	215	—
Wholesale	9,398	2	9,396	1	430	286	63	779	—	8,617	1
Total off-balance sheet	9,613	2	9,611	1	430	286	63	779	—	8,832	1
Total exposure	49,593	55	49,538	139	1,157	4,612	90	5,859	87	43,679	52
2020											
Financial assets											
Cash and balances at central banks	13,472	—	13,472	—	—	—	—	—	—	13,472	—
Loans - amortised cost	15,693	130	14,466	163	323	4,538	56	4,917	135	9,549	28
Personal	2,795	15	2,780	59	—	2,465	—	2,465	57	315	2
Wholesale	12,898	115	11,686	104	323	2,073	56	2,452	78	9,234	26
Debt securities	5,342	—	5,342	—	—	—	—	—	—	5,342	—
Total financial assets	34,507	130	33,280	163	323	4,538	56	4,917	135	28,363	28
Contingent liabilities and commitments											
Personal	525	—	525	—	—	—	—	—	—	525	—
Wholesale	9,117	6	9,111	4	98	441	175	714	2	8,397	2
Total off-balance sheet	9,642	6	9,636	4	98	441	175	714	2	8,922	2
Total exposure	44,149	136	42,916	167	421	4,979	231	5,631	137	37,285	30

18. Risk management continued

Credit risk continued

2021	Gross exposure £m	ECL £m	Maximum credit risk Total £m	Maximum credit risk Stage 3 £m	CREM by type (3) Financial (1) £m	CREM by type (3) Property £m	CREM by type (3) Other (2) £m	CREM coverage Total £m	CREM coverage Stage 3 £m	Exposure post CREM Total £m	Exposure post CREM Stage 3 £m
	Bank										
Financial assets											
Cash and balances at central banks	17,165	—	17,165	—	—	—	—	—	—	17,165	—
Loans - amortised cost	16,797	52	16,745	138	727	4,326	27	5,080	87	11,665	51
Personal	2,753	13	2,740	47	257	2,394	—	2,651	45	89	2
Wholesale	14,044	39	14,005	91	470	1,932	27	2,429	42	11,576	49
Debt securities	5,991	1	5,990	—	—	—	—	—	—	5,990	—
Total financial assets	39,953	53	39,900	138	727	4,326	27	5,080	87	34,820	51
Contingent liabilities and commitments											
Personal	215	—	215	—	—	—	—	—	—	215	—
Wholesale	9,398	2	9,396	1	430	286	63	779	—	8,617	1
Total off-balance sheet	9,613	2	9,611	1	430	286	63	779	—	8,832	1
Total exposure	49,566	55	49,511	139	1,157	4,612	90	5,859	87	43,652	52

2020	Gross exposure £m	ECL £m	Maximum credit risk Total £m	Maximum credit risk Stage 3 £m	CREM by type (3) Financial (1) £m	CREM by type (3) Property £m	CREM by type (3) Other (2) £m	CREM coverage Total £m	CREM coverage Stage 3 £m	Exposure post CREM Total £m	Exposure post CREM Stage 3 £m
	Bank										
Financial assets											
Cash and balances at central banks	13,472	—	13,472	—	—	—	—	—	—	13,472	—
Loans - amortised cost	15,667	130	14,400	163	323	4,538	56	4,917	135	9,523	28
Personal	2,795	15	2,780	59	—	2,465	—	2,465	58	315	1
Wholesale	12,872	115	11,660	104	323	2,073	56	2,452	77	9,208	27
Debt securities	5,342	—	5,342	—	—	—	—	—	—	5,342	—
Total financial assets	34,481	130	33,254	163	323	4,538	56	4,917	135	28,337	28
Contingent liabilities and commitments											
Personal	525	—	525	—	—	—	—	—	—	525	—
Wholesale	9,117	6	9,111	4	98	441	175	714	2	8,397	2
Total off-balance sheet	9,642	6	9,636	4	98	441	175	714	2	8,922	2
Total exposure	44,123	136	42,890	167	421	4,979	231	5,631	137	37,259	30

(1) Includes cash and securities collateral.
(2) Includes guarantees.
(3) The Group holds collateral in respect of individual loans. This collateral includes mortgages over property (both personal and commercial). Property valuations are capped at the loan value.

18. Risk management continued

Credit risk continued

Credit risk asset quality

The asset quality analysis presented below is based on RBSI Group's internal asset quality ratings which have ranges for the PD, as set out below. Customers are assigned credit grades, based on various credit grading models that reflect the key drivers of default for the customer type. All credit grades across RBSI Group map to both an asset quality scale, used for external financial reporting, and a master grading scale for Wholesale exposures used for internal management reporting across portfolios.

The table that follows details the relationship between asset quality (AQ) bands and external ratings published by Standard & Poor's (S&P), for illustrative purposes only. This relationship is established by observing S&P's default study statistics, notably the one year default rates for each S&P rating grade. A degree of judgment is required to relate the PD ranges associated with the master grading scale to these default rates given that, for example, the S&P published default rates do not increase uniformly by grade and the historical default rate is nil for the highest rating categories.

Internal asset quality band	Minimum %	Maximum %	Indicative S&P rating
AQ1	0.000	0.034	AAA to AA
AQ2	0.034	0.048	AA to AA-
AQ3	0.048	0.095	A+ to A
AQ4	0.095	0.381	BBB+ to BBB-
AQ5	0.381	1.076	BB+ to BB
AQ6	1.076	2.153	BB- to B+
AQ7	2.153	6.089	B+ to B
AQ8	6.089	17.222	B- to CCC+
AQ9	17.222	100.000	CCC to C
AQ10	100.000	100.000	D

The mapping to the S&P ratings is used by RBSI Group as one of several benchmarks for its Wholesale portfolios, depending on customer type and the purpose of the benchmark. The mapping is based on all issuer types rated by S&P. It should therefore be considered illustrative and does not, for instance, indicate that exposures reported against S&P ratings either have been or would be assigned those ratings if assessed by S&P. In addition, the relationship is not relevant for Personal portfolios, smaller corporate exposures or specialist corporate segments given that S&P does not typically assign ratings to such entities.

18. Risk management continued

Credit risk continued

Portfolio summary - sector analysis

The table below shows financial assets and off-balance sheet exposures gross of ECL, related ECL provisions, impairment and past due by sector, asset quality and geographical region.

	Group			Bank		
	Personal	Wholesale	Total	Personal	Wholesale	Total
2021	£m	£m	£m	£m	£m	£m
Loans by geography	2,753	14,071	16,824	2,753	14,044	16,797
- UK [1]	2,753	9,628	12,381	2,753	9,611	12,364
- RoI	—	2	2	—	2	2
- Other Europe	—	2,842	2,842	—	2,842	2,842
- RoW	—	1,599	1,599	—	1,589	1,589
Loans by asset quality	2,753	14,071	16,824	2,753	14,044	16,797
- AQ1	49	6,415	6,464	49	6,415	6,464
- AQ2	—	1,970	1,970	—	1,970	1,970
- AQ3	—	1,575	1,575	—	1,575	1,575
- AQ4	—	2,430	2,430	—	2,403	2,403
- AQ5	—	673	673	—	673	673
- AQ6	—	374	374	—	374	374
- AQ7	2,648	419	3,067	2,648	419	3,067
- AQ8	—	99	99	—	99	99
- AQ9	—	10	10	—	10	10
- AQ10	56	106	162	56	106	162
Loans by stage	2,753	14,071	16,824	2,753	14,044	16,797
- Stage 1	2,648	13,537	16,185	2,648	13,510	16,158
- Stage 2	49	428	477	49	428	477
- Stage 3	56	106	162	56	106	162
Loans - past due analysis	2,753	14,071	16,824	2,753	14,044	16,797
- Not past due	2,668	13,983	16,651	2,668	13,956	16,624
- Past due 1-29 days	19	66	85	19	66	85
- Past due 30-89 days	14	16	30	14	16	30
- Past due 90-180 days	25	1	26	25	1	26
- Past due >180 days	27	5	32	27	5	32
Loans - Stage 2	49	428	477	49	428	477
- Not past due	20	410	430	20	410	430
- Past due 1-29 days	18	1	19	18	1	19
- Past due 30-89 days	11	17	28	11	17	28
ECL provisions by stage	13	42	55	13	42	55
- Stage 1	2	6	8	2	6	8
- Stage 2	1	22	23	1	22	23
- Stage 3	10	14	24	10	14	24
ECL provisions coverage (%)	0.5	0.3	0.3	0.5	0.3	0.3
- Stage 1 (%)	0.1	0.0	0.1	0.1	0.0	0.1
- Stage 2 (%)	2.0	5.1	4.8	2.0	5.1	4.8
- Stage 3 (%)	17.9	13.2	14.8	17.9	13.2	14.8
ECL charge	—	(52)	(52)	—	(52)	(52)
- UK	—	(51)	(51)	—	(51)	(51)
- Other Europe	—	(1)	(1)	—	(1)	(1)
ECL loss rate (%)	—	(0.4)	(0.3)	—	(0.4)	(0.3)
Amounts written-off	1	27	28	1	27	28
Other financial assets by asset quality	—	23,156	23,156	—	23,156	23,156
- AQ1-AQ4	—	23,156	23,156	—	23,156	23,156
- AQ5-AQ8	—	—	—	—	—	—
Off-balance sheet	215	9,423	9,638	215	9,423	9,638
- Loan commitments	215	9,146	9,361	215	9,146	9,361
- Financial guarantees [2]	—	277	277	—	277	277
Off-balance sheet by asset quality	215	9,423	9,638	215	9,423	9,638
- AQ1-AQ4	—	8,604	8,604	—	8,604	8,604
- AQ5-AQ8	215	818	1,033	215	818	1,033
- AQ9	—	—	—	—	—	—
- AQ10	—	1	1	—	1	1

(1) UK includes exposures in Jersey, Guernsey, Isle of Man and Gibraltar.
(2) All Financial guarantees are considered as Stage 1.

18. Risk management continued

Credit risk continued

2020	Group Personal £m	Group Wholesale £m	Group Total £m	Bank Personal £m	Bank Wholesale £m	Bank Total £m
Loans by geography	2,795	11,801	14,596	2,795	11,774	14,569
- UK (1)	*2,795*	*8,331*	*11,126*	*2,795*	*8,314*	*11,109*
- RoI	—	*1*	*1*	—	*1*	*1*
- Other Europe	—	*2,178*	*2,178*	—	*2,178*	*2,178*
- RoW	—	*1,291*	*1,291*	—	*1,281*	*1,281*
Loans by asset quality	2,795	11,801	14,596	2,795	11,774	14,569
- AQ1	—	*5,220*	*5,220*	—	*5,219*	*5,219*
- AQ2	—	*1,330*	*1,330*	—	*1,330*	*1,330*
- AQ3	—	*1,316*	*1,316*	—	*1,316*	*1,316*
- AQ4	—	*2,275*	*2,275*	—	*2,249*	*2,249*
- AQ5	—	*551*	*551*	—	*551*	*551*
- AQ6	—	*520*	*520*	—	*520*	*520*
- AQ7	*2,725*	*329*	*3,054*	*2,725*	*329*	*3,054*
- AQ8	—	*115*	*115*	—	*115*	*115*
- AQ9	—	*4*	*4*	—	*4*	*4*
- AQ10	*70*	*141*	*211*	*70*	*141*	*211*
Loans by stage	2,795	11,801	14,596	2,795	11,774	14,569
- Stage 1	*2,676*	*9,467*	*12,143*	*2,676*	*9,467*	*12,143*
- Stage 2	*49*	*2,193*	*2,242*	*49*	*2,166*	*2,215*
- Stage 3	*70*	*141*	*211*	*70*	*141*	*211*
Loans - past due analysis	2,795	11,801	14,596	2,796	11,773	14,569
- Not past due	*2,694*	*11,677*	*14,371*	*2,695*	*11,649*	*14,344*
- Past due 1-29 days	*19*	*110*	*129*	*19*	*110*	*129*
- Past due 30-89 days	*16*	*6*	*22*	*16*	*6*	*22*
- Past due 90-180 days	*32*	—	*32*	*32*	—	*32*
- Past due >180 days	*34*	*8*	*42*	*34*	*8*	*42*
Loans - Stage 2	49	2,193	2,242	49	2,166	2,215
- Not past due	*18*	*2,158*	*2,176*	*18*	*2,131*	*2,149*
- Past due 1-29 days	*17*	*29*	*46*	*17*	*29*	*46*
- Past due 30-89 days	*14*	*6*	*20*	*14*	*6*	*20*
ECL provisions by stage	15	121	136	15	121	136
- Stage 1	*3*	*11*	*14*	*3*	*11*	*14*
- Stage 2	*1*	*73*	*74*	*1*	*73*	*74*
- Stage 3	*11*	*37*	*48*	*11*	*37*	*48*
ECL provisions coverage (%)	0.5	1.0	0.9	0.5	1.0	0.9
- Stage 1 (%)	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*
- Stage 2 (%)	*2.0*	*3.3*	*3.3*	*2.0*	*3.4*	*3.3*
- Stage 3 (%)	*15.7*	*26.2*	*22.7*	*15.7*	*26.2*	*22.8*
ECL charge	4	103	107	4	103	107
- UK	*4*	*87*	*91*	*4*	*87*	*91*
- Other Europe	—	*16*	*16*	—	*16*	*16*
ECL loss rate (%)	0.1	0.9	0.7	0.1	0.9	0.7
Amounts written-off	3	—	3	3	—	3
Other financial assets by asset quality	—	18,814	18,814	—	18,814	18,814
- AQ1-AQ4	—	*18,814*	*18,814*	—	*18,814*	*18,814*
Off-balance sheet	525	9,117	9,642	525	9,116	9,641
- Loan commitments	525	8,902	9,427	525	8,901	9,426
- Financial guarantees (2)	—	215	215	—	215	215
Off-balance sheet by asset quality	525	9,117	9,642	525	9,116	9,641
- AQ1-AQ4	—	*8,512*	*8,512*	—	*8,511*	*8,511*
- AQ5-AQ8	*525*	*600*	*1,125*	*525*	*600*	*1,125*
- AQ9	—	*1*	*1*	—	*1*	*1*
- AQ10	—	*4*	*4*	—	*4*	*4*

(1) UK includes exposures in Jersey, Guernsey, Isle of Man and Gibraltar.
(2) All Financial guarantees are considered as Stage 1.

18. Risk management continued

Non-traded market risk

Definition

Non-traded market risk is the risk to the value of assets or liabilities outside the trading book, or the risk to income, that arises from changes in market prices such as interest rates, foreign exchange rates and equity prices, or from changes in managed rates.

Sources of risk

The key sources of non-traded market risk are credit spread risk, interest rate risk and foreign exchange risk.

Credit spread risk

Credit spread risk arises from the potential adverse economic impact of a change in the spread between bond yields and swap rates, where the bond portfolios are accounted at fair value through equity.
RBSI Group's bond portfolios primarily comprise high-quality securities maintained as a liquidity buffer to ensure it can continue to meet its obligations in the event that access to wholesale funding markets is restricted.
Credit spread risk is monitored daily through sensitivities and VaR measures. The dealing authorities in place for the bond portfolios further mitigate the risk by imposing constraints by duration, asset class and credit rating. Exposures and limit utilisations are reported to senior management on a daily basis.

Interest rate risk

Non-traded interest rate risk arises from the provision to customers of a range of banking products with differing interest rate characteristics. When aggregated, these products form portfolios of assets and liabilities with varying degrees of sensitivity to changes in market interest rates. Mismatches can give rise to volatility in net interest income as interest rates vary.

RBSI Group has the benefit of a pool of stable, non and low interest-bearing liabilities, principally comprising equity and money transmission accounts. These balances are hedged, either by the use of interest rate swaps, generally booked as cash flow hedges of floating-rate assets, or by investing directly in longer-term fixed-rate assets (primarily fixed-rate mortgages or UK government gilts), in order to provide a consistent and predictable revenue stream.

Foreign exchange risk

Non-traded foreign exchange risk exposure arises principally due to investments in overseas operations. Movements in the exchange rates of the operational currency of the overseas investment will impact the balance sheet and the income statement unless the investment is financed by borrowings in the same currency.

All transactional (or non-structural) currency exposure risk is managed by Treasury and there remains an immaterial open position which is measured on a daily basis within set limits. The principal non-sterling currencies in which RBSI Group has transactional currency exposure are the US dollar and the Euro.

Value-at-risk (VaR)

VaR is a statistical estimate of the potential change in the market value of a portfolio (and, thus, the impact on the income statement) over a specified time horizon at a given confidence level.

RBSI Group's standard VaR metrics – which assume a time horizon of one trading day and a confidence level of 99% – are based on interest rate repricing gaps at the reporting date. Daily rate moves are modelled using observations from the last 500 business days. These incorporate customer products plus associated funding and hedging transactions as well as non-financial assets and liabilities. Behavioural assumptions are applied as appropriate.

The non-traded interest rate risk VaR metrics for RBSI Group's personal and commercial banking activities are included in the banking book VaR table presented below. The VaR captures the risk resulting from mismatches in the repricing dates of assets and liabilities.

It includes any mismatch between structural hedges and stable non and low interest-bearing liabilities such as equity and money transmission accounts as regards their interest rate repricing behavioural profile.

RBSI Group manages market risk through VaR limits as well as stress testing, position and sensitivity limits. The table below shows one-day internal banking book VaR at a 99% confidence level. VaR values for each year are calculated based on one-day values for each of the 12 month-end reporting dates.

VaR increased in late 2020 and early 2021 reflecting a change in the composition of the Treasury liquidity portfolio to include longer dated bond holdings, hedged via interest rate swaps.

	Group and Bank			
	31 December 2021 £m	Maximum £m	Minimum £m	Average £m
Interest rate	0.2	3.2	0.2	2.0
Credit spread (1)	16.9	17.9	12.8	14.3
Diversification (2)	(0.2)			(1.8)
Value-at-risk	16.9	17.8	12.4	14.5

	31 December 2020 £m	Maximum £m	Minimum £m	Average £m
Value-at-risk	0.24	0.24	0.02	0.10

(1) The disclosure includes credit spread from 2021. The 2020 disclosure did not include this information and has not been restated.
(2) RBSI Group benefits from diversification across various financial instrument types, currencies and markets. The extent of the diversification benefit depends on the correlation between the assets and risk factors in the portfolio at a particular time. The diversification factor is the sum of the VaR on individual risk types less the total portfolio VaR.

18. Risk management continued

Liquidity risk

Liquidity risk is the risk of being unable to meet financial obligations as and when they fall due. Funding risk is the risk of not maintaining a diversified, stable and cost-effective funding base.

Liquidity and funding risks arise in a number of ways, including through the maturity transformation role that banks perform.

The risks are dependent on factors such as:
- Maturity profile;
- Composition of sources and uses of funding;
- The quality and size of the liquidity portfolio;
- Wholesale market conditions; and
- Depositor and investor behaviour.

RBSI Group manages its liquidity risk taking-into-account regulatory, legal and other constraints to ensure sufficient liquidity resources are available to cover liquidity stresses. In line with NWG, RBSI Group maintains a prudent approach to the definition of liquidity resources comprised of cash and balances at central banks, treasury bills and other high quality government and US agency bonds.

The contractual maturity of balance sheet assets and liabilities reflects the maturity transformation role banks perform. In practice, the behavioural profiles of many liabilities generally exhibit greater stability and longer maturity than the contractual maturity. This is particularly true of many types of retail and corporate deposits which, despite being repayable on demand or at short notice, have demonstrated very stable characteristics even in periods of stress. To assess and manage asset and liability maturity gaps RBSI Group determines the expected customer behaviour through qualitative and quantitative techniques, incorporating observed customer behaviours over long periods of time. Procedures for determining expected behaviour are subject to regulatory and internal requirements and are stressed according to these requirements.

The policy and key inputs for managing maturity and behavioural analysis are subject to governance through the NWG Asset and Liability Management Committee as well as the Group Asset and Liability Management Committee. Financial assets have been reflected in the time band of the latest date on which they could be repaid unless earlier repayment can be demanded by RBSI Group. Financial liabilities are included at the earliest date on which the counterparty can require repayment regardless of whether or not such early repayment results in a penalty.

If the repayment of a financial asset or liability is triggered by, or is subject to, specific criteria such as market price hurdles being reached, the asset is included in the latest date on which it can repay regardless of early repayment, whereas the liability is included at the earliest possible date that the conditions could be fulfilled without considering the probability of the conditions being met.

18. Risk management continued

Contractual maturity

This table shows the residual maturity of financial instruments, based on contractual date of maturity. Derivatives are included in the relevant maturity bands.

	Group								
	Banking activities								
2021	Less than 1 month £m	1-3 months £m	3-6 months £m	6 months - 1 year £m	Subtotal £m	1-3 years £m	3-5 years £m	More than 5 years £m	Total £m
Cash and balances at central banks	17,220	—	—	—	17,220	—	—	—	17,220
Derivatives	12	8	3	3	26	5	9	118	158
Loans to banks	1,305	—	—	—	1,305	—	—	—	1,305
Loans to customers(1)	949	1,208	1,311	3,491	6,959	4,983	894	2,680	15,516
Personal	323	16	3	27	369	62	89	2,295	2,815
Corporate	124	132	153	672	1,081	1,194	471	385	3,131
Financial institutions excluding banks	502	1,060	1,155	2,792	5,509	3,727	334	—	9,570
Other financial assets	—	—	624	1,536	2,160	840	808	2,115	5,923
Total financial assets	19,486	1,216	1,938	5,030	27,670	5,828	1,711	4,913	40,122
2020									
Total financial assets	15,766	1,199	851	3,155	20,971	6,014	1,798	4,645	33,428
Bank deposits	152	114	—	—	266	—	—	—	266
Customer deposits	30,753	6,371	189	223	37,536	3	—	—	37,539
Personal	6,468	350	170	195	7,183	—	—	—	7,183
Corporate	7,702	1,870	5	1	9,578	—	—	—	9,578
Financial institutions excluding banks	16,583	4,151	14	27	20,775	3	—	—	20,778
Derivatives	33	7	3	3	46	6	27	38	117
Other financial liabilities	46	265	88	77	476	—	—	—	476
Lease liabilities	—	1	1	2	4	8	6	19	37
Total financial liabilities	30,984	6,758	281	305	38,328	17	33	57	38,435
2020									
Total financial liabilities	25,632	5,149	474	654	31,909	18	8	58	31,993

18. Risk management continued

	Bank								
	Banking activities								
2021	Less than 1 month £m	1-3 months £m	3-6 months £m	6 months - 1 year £m	Subtotal £m	1-3 years £m	3-5 years £m	More than 5 years £m	Total £m
Cash and balances at central banks	17,220	—	—	—	17,220	—	—	—	17,220
Derivatives	12	8	3	3	26	5	9	118	158
Loans to banks	1,278	—	—	—	1,278	—	—	—	1,278
Loans to customers[1]	949	1,208	1,311	3,491	6,959	4,983	894	2,680	15,516
Personal	323	16	3	27	369	62	89	2,295	2,815
Corporate	124	132	153	672	1,081	1,194	471	385	3,131
Financial institutions excluding banks	502	1,060	1,155	2,792	5,509	3,727	334	—	9,570
Other financial assets	—	—	624	1,536	2,160	840	808	2,115	5,923
Total financial assets	19,459	1,216	1,938	5,030	27,643	5,828	1,711	4,913	40,095
2020									
Total financial assets	15,739	1,199	851	3,155	20,944	6,014	1,798	4,645	33,401
Bank deposits	152	114	—	—	266	—	—	—	266
Customer deposits	30,753	6,371	189	223	37,536	3	—	—	37,539
Personal	6,468	350	170	195	7,183	—	—	—	7,183
Corporate	7,702	1,870	5	1	9,578	—	—	—	9,578
Financial institutions excluding banks	16,583	4,151	14	27	20,775	3	—	—	20,778
Derivatives	33	7	3	3	46	6	27	38	117
Other financial liabilities	46	265	88	77	476	—	—	—	476
Lease liabilities	—	1	1	2	4	8	6	19	37
Total financial liabilities	30,984	6,758	281	305	38,328	17	33	57	38,435
2020									
Total financial liabilities	25,632	5,149	474	654	31,909	18	8	58	31,993

(1) Excludes £53 million for Group (2020 - £129 million) and £53 million for Bank (2020- £130 million) of impairment provision.

Capital risk

Regulatory capital consists of reserves and instruments issued that are available, have a degree of permanency and are capable of absorbing losses. A number of strict conditions set by regulators must be satisfied to be eligible as capital.

Capital management ensures that there is sufficient capital and other loss-absorbing instruments to operate effectively including meeting minimum regulatory requirements, operating within Board-approved risk appetite, maintaining its credit rating and supporting its strategic goals.

RBSI Group is required to report its total capital ratio and Common Equity Tier 1 (CET1) capital ratio to its lead regulator, the JFSC, on a periodic basis. The ratios are calculated as total capital to total risk-weighted assets, expressed as a percentage and CET1 capital to total risk-weighted assets, expressed as a percentage. The JFSC has established the Codes of Practice for Deposit-taking Business and includes that a registered person's total capital ratio minimum is 10% and CET1 capital ratio minimum is 8.5%.

Constituents of capital

The determination of what instruments and financial resources are eligible to be counted as capital is laid down in applicable regulation. Capital is categorised by applicable regulation under two tiers (1 and 2) according to the ability to absorb losses, degree of permanency and the ranking of absorbing losses.

There are three broad categories of capital across these two tiers:

- CET1 capital must be perpetual and capable of unrestricted and immediate use to cover risks or losses as soon as these occur. This includes ordinary shares issued and retained earnings. CET1 capital absorbs losses before other types of capital and any loss absorbing instruments.
- Additional Tier 1 (AT1) capital is the second form of loss absorbing capital and must be capable of absorbing losses on a going concern basis. These instruments are either written down or converted into CET1 capital when a pre-specified CET1 ratio is reached. Coupons on AT1 issuances are discretionary and may be cancelled at the discretion of the issuer at any time. AT1 capital must have a minimum original maturity of five years.
- Tier 2 capital is RBSI Group's supplementary capital and provides loss absorption on a gone concern basis. Tier 2 capital absorbs losses after Tier 1 capital. RBSI Group has not issued any Tier 2 instruments.

18. Risk management continued

Pension risk

Definition

Pension risk is the risk to RBSI Group caused by its contractual or other liabilities to, or with respect to, a pension scheme (whether established for its employees or those of a related company or otherwise). It is also the risk that RBSI Group will make payments or other contributions to, or with respect to, a pension scheme because of a moral obligation or because RBSI Group considers that it needs to do so for some other reason.

Sources of risk

The main source of pension risk for RBSI Group is through its largest scheme, the International Pensions Trust (IPT). Further detail on RBSI Group's pension obligations can be found in Note 4 to the accounts.

RBSI Group is exposed to the risk that the schemes' assets, together with future investment returns and additional future contributions, are estimated to be insufficient to meet liabilities as they fall due. In such circumstances, RBSI Group could be obliged (or might choose) to make additional contributions to the schemes, or be required to hold additional capital to mitigate such risk.

Key developments in 2021

- There were no material changes to RBSI Group's exposure to pension risk during the year, and the overall positions of the schemes that RBSI Group sponsors remained broadly stable.
- The triennial actuarial valuation for the IPT, with an effective date of 31 March 2021, was completed during 2021 and agreement was reached with the Trustee that no additional contributions were needed.

Governance, risk appetite and controls

The RBSI Pension Forum receives authority from the Board and is responsible for taking decisions or making recommendations in relation to the financial, compliance, policy and operational structure of RBSI Group's pension arrangements. Where authority is not delegated, the Forum makes recommendations to RBSI Group's Chief Financial Officer or the Board, depending on the materiality of the issue. RBSI Group's Board retains ultimate authority for decision making.

Monitoring and measurement

The RBSI Pension Forum formulates RBSI Group view of pension risk and provides a governance framework for all RBSI Group's pension schemes.

RBSI Group calculates stochastic stresses on its material defined benefit pension schemes each year. The stress calculations form the basis of the pension risk Pillar 2 charge in the Bank's ICAAP.

Mitigation

The trustee board of the IPT is solely responsible for the investment of scheme assets which are held separately from the assets of RBSI Group. The trustee board has taken measures to mitigate risk including adopting a diversified investment strategy and investing in liability driven investments, so that changes in the value of the liabilities will be partially matched by changes in the asset values, thus reducing volatility of the scheme's funding position.

In managing the assets of the IPT, the trustee board also takes account of, and gives consideration to, the ability of investment managers to effectively deal with environmental, social and governance issues.

Compliance & conduct risk

Definition

Compliance risk is the risk that the behaviour of RBSI Group towards customers fails to comply with laws, regulations, rules, standards and codes of conduct. Such a failure may lead to breaches of regulatory requirements, organisational standards or customer expectations and could result in legal or regulatory sanctions, material financial loss or reputational damage.

Conduct risk is the risk that the conduct of RBSI Group and its subsidiaries and its staff towards customers – or in the markets in which it operates – leads to unfair or inappropriate customer outcomes and results in reputational damage, financial loss or both.

Sources of risk

Compliance and conduct risks exist across all stages of RBSI Group's relationships with its customers and arise from a variety of activities including product design, marketing and sales, complaint handling, staff training, and handling of confidential inside information.

Key developments in 2021

- Compliance and conduct risk appetite statements and measures were updated with an enhanced focus to provide better visibility of key risks across NWG.
- Continued collaboration across NWG to deliver good customer outcomes with a focus on forbearance strategies.

Governance

RBSI Group defines appropriate standards of compliance and conduct and ensures adherence to those standards through its risk management framework. Relevant compliance and conduct matters are escalated through the Board Risk Committee.

Risk appetite

Risk appetite for compliance and conduct risks is set at Board level. Risk appetite statements articulate the levels of risk that legal entities, businesses and functions work within when pursuing their strategic objectives and business plans.

18. Risk management continued

A range of controls is operated to ensure the business delivers good customer outcomes and is conducted in accordance with legal and regulatory requirements. A suite of policies addressing compliance and conduct risks set appropriate standards across RBSI Group. Examples of these include the Complaints Management Policy, Client Assets & Money Policy, and Product Lifecycle Policy as well as policies relating to customers in vulnerable situations, cross-border activities and market abuse. Continuous monitoring and targeted assurance is carried out as appropriate.

Monitoring and measurement

Compliance and conduct risks are measured and managed through continuous assessment and reporting to RBSI Group's senior risk committees and at Board level. The compliance and conduct risk framework facilitates the consistent monitoring and measurement of compliance with laws and regulations and the delivery of consistently good customer outcomes. The first line of defence is responsible for effective risk identification, reporting and monitoring, with oversight, challenge and review by the second line. Compliance and conduct risk management is also integrated into RBSI Group's strategic planning cycle.

Mitigation

Activity to mitigate the most-material compliance and conduct risks is carried out across RBSI Group. Examples of mitigation include consideration of customer needs in business and product planning, targeted training, complaints management, as well as independent monitoring activity. Internal policies help support a strong customer focus across RBSI Group.

Financial crime risk

Definition

Financial crime risk is presented by criminal activity in the form of money laundering, terrorist financing, bribery and corruption, sanctions and tax evasion, as well as fraud risk management.

Sources of risk

Financial crime risk may be presented if RBSI Group's customers, employees or third parties undertake or facilitate financial crime, or if RBSI Group's products or services are used to facilitate such crime. Financial crime risk is an inherent risk across all lines of business.

Key developments in 2021

- Significant investment continued to be made to support delivery of the multi-year transformation plan across financial crime risk management.
- Enhancements were made to technology and data analytics to improve the effectiveness of systems used to monitor customers and transactions.
- A new financial crime and fraud goal was introduced for RBSI Group's most senior employees to further embed financial crime risk management culture, behaviours, and accountabilities.

Governance

The Financial Crime Review Forum is the principal financial crime risk management forum. The forum reviews and, where appropriate, escalates material financial crime risks and issues across RBSI Group. It is represented by all three lines of defence.

Risk appetite

There is no appetite to operate in an environment where systems and controls do not enable the identification, assessment, monitoring, management and mitigation of financial crime risk. RBSI Group's systems and controls must be comprehensive and proportionate to the nature, scale and complexity of its businesses. There is no tolerance to systematically or repeatedly breach relevant financial crime regulations and laws.

RBSI Group operates a framework of preventative and detective controls designed to mitigate the risk that it could facilitate financial crime. These controls are supported by a suite of policies, procedures and guidance to ensure they operate effectively.

Monitoring and measurement

Financial crime risks are identified and reported through continuous risk management and regular monthly reporting to the Financial Crime Risk Forum and other risk governance committees. Quantitative and qualitative data is reviewed and assessed to measure whether financial crime risk is within risk appetite.

Mitigation

Through the financial crime framework, relevant policies, systems, processes and controls are used to mitigate and manage financial crime risk. This includes the use of dedicated screening and monitoring systems and controls to identify people, organisations, transactions and behaviours that may require further investigation or other actions. Centralised RBSI Group expertise is available to detect and disrupt threats to RBSI Group and its customers. Intelligence is shared with law enforcement, regulators and government bodies to strengthen jurisdictional defences against those who would misuse the financial system for criminal motives.

Climate risk

Definition

Climate risk is the threat of financial loss or adverse non-financial impacts associated with climate change and the political, economic and environmental responses to it.

Sources of risk

Physical risks may arise from climate and weather-related events such as heatwaves, droughts, floods, storms and sea level rises. They can potentially result in financial losses, impairing asset values and the creditworthiness of borrowers. RBSI Group could be exposed to physical risks directly by the effects on its property portfolio and, indirectly, by the impacts on the wider economy as well as on the property and business interests of its customers.

Transition risks may arise from the process of adjustment towards a low-carbon economy. Changes in policy, technology and sentiment could prompt reassessment of customers' financial risk and may lead to falls in the value of a large range of assets. RBSI Group could be exposed to transition risks directly through the costs of adaptation within economic sectors and markets as well as supply chain disruption leading to financial impacts on it and its customers. Potential indirect effects include the erosion of RBSI Group's competitiveness, profitability, or reputation damage.

18. Risk management continued

Key developments in 2021

- RBSI Group created a new dedicated Environment, Social and Governance (ESG) team alongside a refreshed climate strategy, which underpinned the focus on the climate challenge and allocate dedicated resource to address climate opportunities and risks.
- Available Energy Performance Certificate and flood risk datasets were introduced to understand exposure to climate risk across residential mortgage and commercial real estate portfolios.
- Climate commentary requirements were introduced into the transactional acceptance standards, supporting a qualitative assessment of climate risk.
- Climate risk was formally incorporated into RBSI Group's Risk Management Framework with Climate Risk recognised as a principle risk within the Risk Directory and a new Climate Risk policy launched.

Governance

The Board is responsible for monitoring and overseeing climate-related risk within RBSI Group's overall business strategy and risk appetite. The Board Risk Committee and the Board received regular strategic updates.

The Environmental, Social and Governance Steering Group (ESG SG) was established to oversee delivery of the climate strategy and discuss emerging risks as they present themselves. The ESG SG is chaired by the Senior Responsible Officer for climate, who is also a member of the executive management team.

The ESG SG has identified four focus areas: energise colleagues; driven by data; safeguard our future; and shape sustainable outcomes. The focus areas sharpen priorities across RBSI Group and cover both climate-related risk and opportunity initiatives.

Risk appetite

Work continued in 2021 to integrate climate risk into the risk management framework. This included the development of a new Climate Risk policy and appropriate risk appetite metrics.

In December 2021, the NWG Board approved the adoption of three first-generation climate risk appetite measures, for integration into business-as-usual risk management and links. Following this, RBSI Group has developed a suite of metrics that will enable reporting of climate risk appetite and links risk management to RBSI Group's strategic goals and priorities.

NWG has focused on developing the capabilities to use scenario analysis to identify the most material climate risks and opportunities for its customers, seeking to harness insights to inform risk management practices and maximise the opportunities arising from a transition to a low carbon economy. As part of NWG, RBSI Group leverages these capabilities to inform its strategy for climate-related opportunities and risk management.

Monitoring and measurement

RBSI Group regularly considers existing and emerging regulatory requirements related to climate change. The identification of climate regulation has been incorporated into the existing upstream risk management process. As part of NWG, RBSI Group is a founding signatory of the United Nations Environment Programme Finance Initiative Principles for Responsible Banking.

RBSI Group also regularly engages in climate consultations across local jurisdictions, recently providing a response to the draft Jersey Carbon Neutral Roadmap.

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or external events. It arises from day-to-day operations and is relevant to every aspect of the business.

Operational risk appetite supports effective management of material operational risks. It expresses the level and types of operational risk RBSI Group is willing to accept to achieve its strategic objectives and business plans.

Risk appetite for operational risk is set at RBSI Group Board level. Risk appetite statements articulate the levels of risk that legal entities, businesses and functions work within when pursuing their strategic objectives and business plans.

Risk and control assessments are used across all business areas and support functions to identify and assess material operational and conduct risks and key controls.

All risks and controls are mapped to the NWG's Risk Directory. Risk assessments are refreshed at least annually to ensure they remain relevant and capture any emerging risks and also ensure risks are reassessed.

The process is designed to confirm that risks are effectively managed in line with risk appetite. Controls are tested at the appropriate frequency to verify that they remain fit-for-purpose and operate effectively to reduce identified risks.

Scenario analysis is used to assess how severe but plausible operational risks will affect RBSI Group. It provides a forward-looking basis for evaluating and managing operational risk exposures.

Operational resilience is managed and monitored through the risk and control assessments methodology. This is underpinned by setting, monitoring and testing tolerances for key business services. Progress continues on the response to regulatory expectations on operational resilience.

Reputational risk

A reputational risk policy is in place to support the management of issues that could pose a threat to RBSI Group's public image. A number of measures – including some also used in the management of operational, conduct and financial risks – are used to assess risk levels against risk appetite. Where a material reputational risk is presented, this is escalated from RBSI Group's Reputational Risk Committee to the NWG Reputational Risk Committee.

Model risk

RBSI Group uses a variety of models in the course of its business activities. Examples include the use of model outputs to support customer decisioning, measuring and assessing risk exposures. A governance framework is in place to ensure policies and processes relating to models are appropriate and effective.

The NWG Model Risk Oversight Committee provides a direct escalation route to the NWG Executive Risk Committee and, where applicable, onwards to the NWG Board Risk Committee.

19. Contingent liabilities and commitments

The amounts shown in the table below are intended only to provide an indication of the volume of business outstanding at 31 December 2021. Although the RBSI Group is exposed to credit risk in the event of non-performance of the obligations undertaken by customers, the amounts shown do not, and are not intended to, provide any indication of the RBSI Group's expectation of future losses.

	Group and Bank	
	2021 £m	2020 £m
Guarantees	262	198
Other contingent liabilities	15	17
Standby facilities, credit lines and other commitments	9,336	9,427
Contingent liabilities and commitments	9,613	9,642

Banking commitments and contingent obligations, which have been entered into on behalf of customers and for which there are corresponding obligations from customers, are not included in assets and liabilities. The RBSI Group's maximum exposure to credit loss, in the event of non-performance by the other party and where all counterclaims, collateral or security proves valueless, is represented by the contractual nominal amount of these instruments included in the table. These commitments and contingent obligations are subject to the RBSI Group's normal credit approval processes.

Guarantees

The RBSI Group gives guarantees on behalf of customers. A financial guarantee represents an irrevocable undertaking that the RBSI Group will meet a customer's obligations to third parties if the customer fails to do so. The maximum amount that the RBSI Group could be required to pay under a guarantee is its principal amount as disclosed in the table above. The RBSI Group expects most guarantees it provides to expire unused.

Contingent liabilities

These include standby letters of credit, supporting customer debt issues, contingent liabilities relating to customer trading activities such as those arising from performance and customs bonds, warranties and indemnities and obligations to the NWG.

Commitments

These are a loan commitment, the RBSI Group agrees to make funds available to a customer in the future. Loan commitments, which are usually for a specified term may be unconditionally cancellable or may persist, provided all conditions in the loan facility are satisfied or waived. Commitments to lend include commercial standby facilities and credit lines, liquidity facilities to commercial paper conduits and unutilised overdraft facilities.

Litigation

The RBSI Group is involved in litigation involving claims by and against it which arise in the ordinary course of business. The directors of the RBSI Group, after reviewing the claims pending and threatened against the RBSI Group, and taking into account the advice of the relevant legal advisers, are satisfied that the outcome of these claims are unlikely to have a material adverse effect on the net assets of the RBSI Group.

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20. Analysis of cash and cash equivalents

	Group		Bank	
	2021 £m	2020 £m	2021 £m	2020 £m
At 1 January				
- cash	13,531	10,617	13,531	10,617
- cash equivalents	1,768	2,317	1,750	2,270
	15,299	12,934	15,281	12,887
Net increase in cash and cash equivalents	3,715	2,365	3,706	2,394
At 31 December	19,014	15,299	18,987	15,281
Comprising:				
Cash and balances at central banks	17,220	13,531	17,220	13,531
Net loans to banks including intragroup balances	1,794	1,768	1,767	1,750
	19,014	15,299	18,987	15,281

The RBSI Group is required by law or regulation to maintain balances with the Central banks which are included in Cash and cash equivalents, and not available for use by the RBSI Group. These are set out below.

	2021 £m	2020 £m	2021 £m	2020 £m
Central Bank of Luxembourg	123	59	123	59
Bank of England	17	8	17	8
Total	140	67	140	67

21. Related parties

The RBSI Group's immediate parent company is NWG.

The RBSI Group's ultimate holding company, and the parent of the largest group into which the RBSI Group is consolidated into is NWG.

The Bank's immediate parent company is The Royal Bank of Scotland International (Holdings) Limited.

The Bank's ultimate holding company, and the parent of the largest group into which the Bank is consolidated into is NWG.

UK Government

The UK Government through HM Treasury is the ultimate controlling party of NWG. The UK government's shareholding is managed by UK Government Investments Limited, a company wholly owned by the UK Government. As a result, the UK Government and UK Government controlled bodies are related parties of the RBSI Group including the Bank.

The RBSI Group enters into transactions with many of these bodies on an arm's length basis. Transactions include the payment of: taxes – principally UK corporation tax (paid through London branch) and value added tax; national insurance contributions; and regulatory fees and levies together with banking transactions such as loans and deposits undertaken in the normal course of banker-customer relationships.

Bank of England facilities

The RBSI Group may participate in a number of schemes operated by the Bank of England in the normal course of business.

Members of the RBSI Group that are UK authorised institutions are required to maintain non-interest bearing (cash ratio) deposits with the Bank of England amounting to 0.324% of their average eligible liabilities in excess of £600 million.

21. Related parties continued

(a) Transactions with key management

For the purposes of IAS 24 'Related Party Disclosure', key management comprise directors of the RBSI Group and members of the Executive Committee Offshore. The following amounts are attributable, in aggregate, to key management:

	Group and Bank	
	2021	2020
	£'000	£'000
Loans and advances to customers	1,514	1,591
Customer accounts	414	1,362
Interest received	20	15
Interest paid	-	2

Key management have banking relationships with NWG entities which are entered into in the normal course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with other persons of a similar standing or, where applicable, with other employees. These transactions did not involve more than the normal risk of repayment or present other unfavourable features.

(b) Related party transactions

	Group		Bank	
	2021	2020	2021	2020
	£'000	£'000	£'000	£'000
Assets				
Loans and advances to banks:				
NatWest Group entities	579	637	586	646
Liabilities				
Deposits by banks:				
NatWest Group entities	242	236	308	322
Income				
Interest received:				
NatWest Group entities	2	5	2	5
Expenses				
Interest paid:				
NatWest Group entities	6	6	6	6

Operating expenses includes inter-group cost recharges of £72 million (2020: £79 million) from NWG.

An ordinary dividend of £76 million was paid to NWG (2020: nil) by RBSIH. A preference dividends of £20 million (2020: £20 million) was paid to NWG by RBSI. An ordinary dividend of £54 million was paid from RBSI to RBSIH during the year (2020: nil).

(c) Compensation of key management

The aggregate remuneration of directors and other members of key management during the year was as follows:

	Group and Bank	
	2021	2020
	£'000	£'000
Short-term benefits	3,076	3,019
Share-based payments	1,039	1,079
Post-employment benefits	109	151
	4,224	4,249

22. Post Balance sheet events

There have been no significant events between the financial year end and the date of approval of the financial statements which would require a change to or additional disclosure in the financial statements.