



NatWest
Markets

NatWest Markets Plc
Annual Report and Accounts 2019

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Approval of Strategic Report

The Strategic Report for the year ended 31 December 2019 set out on pages 1 to 16 was approved by the Board of Directors on 13 February 2020.

By order of the Board

Company Secretary

Scott Gibson
13 February 2020

Chairman

Frank Dangeard

Executive Director

Robert Begbie,
Interim CEO

Non-Executive Directors

Brendan Nelson
Vivek Ahuja
Sarah Wilkinson
Tamsin Rowe

2019 performance highlights

A challenging year where we made progress on simplifying and de-risking the business, while maintaining strong levels of capital, funding and liquidity.

Income

2019

£719m

2018* £858m

Core income¹

2019

£978m

2018* £1,213m

Other operating expenses²

2019

£920m

2018* £1,060m

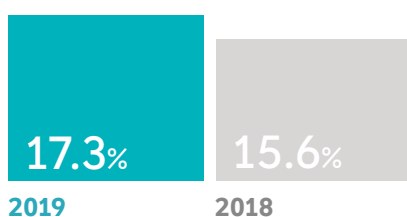
Loss before tax

2019

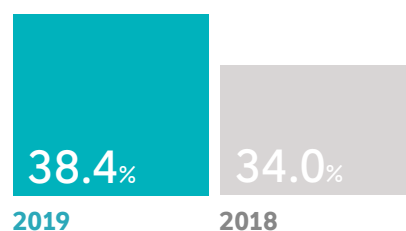
(£230m)

2018* (£1,277m)

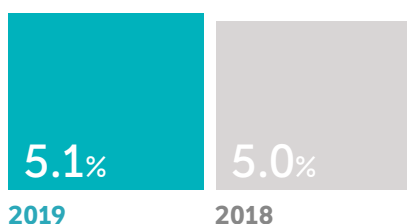
CET1 ratio³



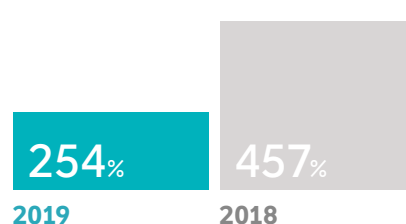
MREL ratio³



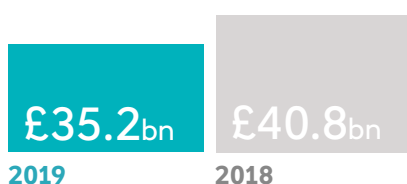
CRR leverage³



Liquidity coverage ratio³



Risk-weighted assets³



* Income statement comparatives for 2018 all relate to continuing operations.

Notes:

(1) Excludes legacy, own credit adjustments and Central items & other.

(2) Excludes strategic costs and litigation & conduct costs.

(3) These metrics are shown for NWM Plc as managed internally. Capital, leverage and RWAs are based on the PRA transitional arrangements for NWM Plc. Regulatory capital is monitored and reported at NWM Plc level.



Robert Begbie
Interim CEO,
NatWest Markets

Chief Executive's statement

I was pleased to be appointed Chief Executive in December 2019 and I look forward to leading the business.

2019 was a challenging year for the NatWest Markets Group, navigating volatile markets, political uncertainty and regulatory change. The financial performance of the business was disappointing, largely as a result of a poor third quarter reflecting lower trading income. Despite this, maintaining customer relationships has been a priority for the business and there were a number of significant achievements and industry firsts.

Supporting customers

NatWest Markets continued to play a leading role in market structural reform particularly Risk-Free Rates. The business was first-to-market with its Realised Rate calculator, and acted as the sole solicitation agent in the first LIBOR to SONIA loan amendment.

NatWest Markets also launched its Environmental, Social and Governance (ESG) Product Framework – the first of its kind – designed to provide customers with ESG linked investments. During 2019, our capital market teams helped develop the sterling green market to support the growing UK responsible investing sector following the new ESG stewardship requirements. We led on more than £2 billion of bonds issued by housing associations to help ease the UK's social housing shortage, and worked with RBS Group on its inaugural social bond to encourage UK job creation.

Safe and secure

The business continued to support European Economic Area (EEA) customers through Brexit uncertainties. In Q1 2019, NatWest Markets N.V. was ready to serve the RBS Group's EEA customers from its branch network across Western Europe and on 29 November 2019 it became a subsidiary of NatWest Markets Plc. We are well prepared to serve our EEA customers whatever the outcome of the UK's relationship with the EU.

In Q2 2019, Standard & Poor's upgraded NatWest Markets' long-term issuer credit rating up one notch to A-, helping to increase trading activity and raise funding from diversified global sources, including our first US issuance under the Rule 144A programme.

Our people

I have joined a business of talented, diverse and driven people. Engagement remained high in 2019, with the business achieving its best ever employee survey results. This year we have reported our Gender Pay Gap for the first time. While the business compares well against our industry peers, we acknowledge there's more to do to increase female representation at senior levels to meet our ambition of being a gender balanced organisation by 2030. We have made good progress on this agenda and will continue to drive momentum.

Looking forward

The RBS Group has announced that NatWest Markets will be refocused to support a more integrated corporate and institutional customer offering. This will mean a significant transformation for NatWest Markets.

We have an important role in delivering the RBS Group's future markets business, connecting its customers with international capital markets and helping them to manage their financing and risk management needs. We will become a purpose-led organisation committed to supporting a thriving economy.

Robert Begbie
Interim CEO, NatWest Markets

Our business

Refocused business

The RBS Group announced on 14 February 2020 that it will become a purpose-led organisation – championing potential, helping people, families and businesses to thrive. This strategy will mean balancing the interests and changing needs of all our stakeholders – from customers and communities, to colleagues and investors. Our current focus is on the areas where we believe we can have the most significant positive impact – enterprise, learning and climate. As part of this strategy, RBS Group will refocus NatWest Markets to support a more integrated corporate and institutional customer offering.

NatWest Markets has an important role in delivering this future strategy by connecting the RBS Group's corporate and institutional customers with international capital markets and helping them to manage their financing and risk management needs.

NatWest Markets will have a leaner operating model and will focus capital towards supporting the RBS Group's customers' needs and increasing its focus on digital solutions. Alongside this, it will be reducing its Risk Weighted Assets, managing down and optimising inefficient capital and activities. It is expected that the business will be in a period of significant transformation and incur material costs as it implements this strategy.

Our products and solutions

We help our customers manage their financial risks and achieve their short-term and long-term financial goals, while navigating changing markets and regulation.

Our products and solutions are centred on three pillars: Rates, Currencies and Financing.

We are focused on providing best in class colour, content and ideas to customers and leveraging technology and automation.

We provide liquidity and risk management in Currencies, Rates, Credit and Securitised Products through a combination of voice and electronic delivery. Our integrated financing, debt capital markets and risk management solutions are built on a foundation of insightful content and structuring.

Rates

We offer a range of interest rate products supporting customers' financing and hedging needs.

Currencies

We provide access to cash/spot FX, forwards and FX options in more than 60 currency pairs.

Financing

We are a leading partner for our customers in accessing global debt capital markets. We offer all mainstream bond financing activities, asset backed financing and primary lending products as well as Credit trading capabilities.

Digital

We have developed digital self-service applications covering FX, rates, risk management, international payments and many more services.

Colour, Content and Ideas

Our strategist and content experts across Currencies, Risk and Financing offer fresh thinking alongside market-leading economic insights in the key economies where our customers do business.

Our operations

NatWest Markets operates from trading hubs in Amsterdam, London, Singapore and Stamford with sales offices across key locations in the UK, EU, US and Asia. Global market access is offered by the NatWest Markets Group across NatWest Markets Plc (NWM Plc) and its subsidiaries, including NatWest Markets Securities Inc. and NatWest Markets N.V. (NWM N.V.).

US

Our broker-dealer in Stamford provides access to US capital markets and USD products. Sales offices in San Francisco and San Jose connect us with customers on the West Coast.

Global Service Centres

We have operations and technology teams in these locations: Warsaw, Gurugram and Chennai.

UK & Western Europe

NWM Plc has its primary trading and origination hub in London and a branch in Frankfurt.

NWM N.V. is based in Amsterdam with branches authorised in London, Dublin, Frankfurt, Madrid, Milan, Paris and Stockholm.

Asia

We have a trading and sales origination hub based in Singapore with sales offices supporting risk distribution and access to investor capital in Tokyo and Hong Kong.

Key: ■ NWM Plc ■ Global Service Centres ■ NWM N.V.

Industry recognition

Our commitment and focus continues to be on anticipating our customers' needs and providing excellent customer service and execution. This has been recognised by a number of awards and surveys in 2019:



**UK Corporate FX
Greenwich Quality
Leader:**

2018 Greenwich
Associates FX Study¹

GREENWICH
DATA | ANALYTICS | INSIGHTS

**Tied No. 1 for Interest
Rate Derivatives Service
Quality**

Greenwich Associates
European Fixed Income
Rate Derivatives 2019

GREENWICH
DATA | ANALYTICS | INSIGHTS

**#1 European
Government Bonds by
Market Share – Gilts**

Greenwich Associates
European Fixed Income
Rates 2019

**Risk
Awards**
2020
Winner

NatWest Markets
Risk solutions
house of the year

**Risk Solutions House
of the Year**

Risk Awards 2020²

dealogic

**Ranked #1 Private
Placement Agent for
European Issuers in 2019**

Dealogic European
Issuer Traditional Private
Placement full year table
for 2019

Notes: (1) Awarded in 2019. (2) Awarded in November 2019

Operating environment

NatWest Markets' performance is influenced by the environment in which we operate. Our operating environment continues to evolve at pace across economic, climate, political, technological, regulatory and technological boundaries.

Economic overview

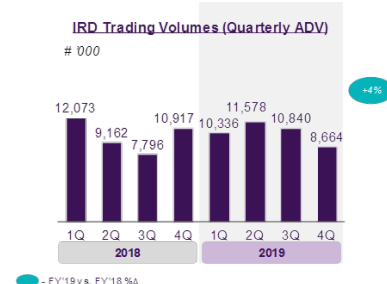
NatWest Markets' activities are primarily related to the economic environment in the UK, Europe and the US. The NatWest Markets Group (NWM Group) derives a substantial majority of its income from its operations in the UK. Accordingly, the NWM Group's business, results of operations and financial position depend upon the economic conditions prevailing in its primary market – in particular economic growth and the general level of interest rates and volume of transactions.

The UK economy continued to slow in 2019 as uncertainty about the UK's exit from the EU weighed on activity. Interest rate and foreign exchange markets were also volatile in response to the changing political landscape. The uncertainty weighed on business investment and contributed to slowing house prices. A slowing global economy and heightened geopolitical events, particularly with regard to trade tensions, further complicated the outlook. Despite an uncertain economic outlook, NatWest Markets remained focused on meeting the diverse needs of customers across the UK and internationally.

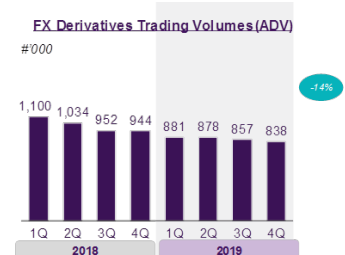
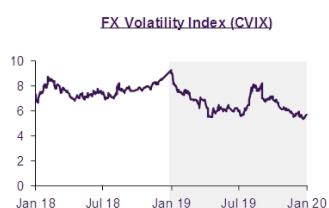
Market environment in 2019

The NWM Group's income is closely linked with market trading volumes and the levels of volatility observed in the products we offer. The graphs on this page illustrate the movements in trading volumes and volatility for Rates, FX and Credit markets during 2019.

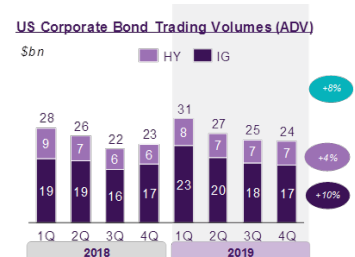
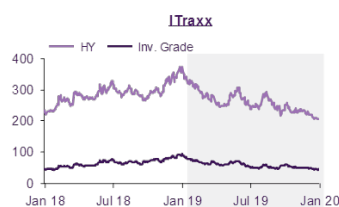
Rates



FX



Credit



Source: CME for IRD and FX; SIFMA for US Credit trading; Bloomberg for Move Index and CVIX; Markit for ITraxx.

Competitive landscape

NatWest Markets competes with large domestic banks, major international banks and a number of investment banks that also offer risk management, trading solutions and debt financing to Financial Institutions and UK and European Corporate customers. Maintaining its competitive position in the market requires NatWest Markets to continue to innovate.

Technology is disrupting a number of elements of NatWest Markets activities in the wider marketplace, with some new players targeting selected components of the value chain, providing highly targeted offerings to customers. Some of this increased competition requires NatWest Markets to become faster, more agile and more innovative in the way that it develops its technology and customer offering. To respond to growing competitive pressures from new technology and new market participants, NatWest Markets is investing in improving its customer experience, products and services.

NatWest Markets has been focused on making it easier for our customers to transact with us and in a way that adds value to their business. This has included: FXmicropay enabling customers to offer live foreign currency prices on e-commerce platforms and disintermediate payment processors from the value chain; microRates allowing automated hedging of a portfolio; CurrencyPay making it easier and cheaper for SMEs and corporates to make foreign currency payments.

One of NatWest Markets competitive advantages comes from the expertise and markets insight of its employees, producing content and ideas that customers truly value, and providing customers with tailored solutions and services. Given the nature of the market, it's essential we are able to retain key people to maintain a strong offering against competitors. NatWest Markets monitors people risk closely and has plans in place to support the retention of people in key roles, with wider programmes supporting engagement and training.

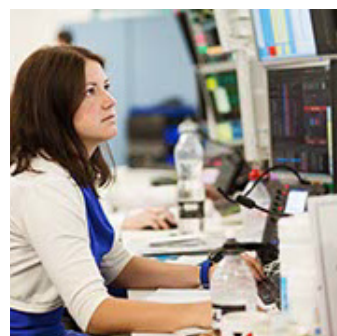
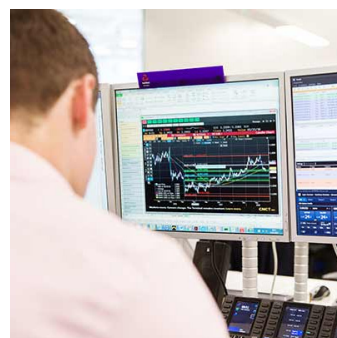
Regulatory landscape

NWM Group is comprised of NWM Plc and its operation subsidiaries: primarily regulated by the Financial Conduct Authority and Prudential Regulation Authority in the UK, the De Nederlandsche Bank, Authority for the Financial Markets and BaFin in Europe, the Securities and Exchange Commission, Commodity Futures Trading Commission, Chicago Mercantile Exchange, Federal Reserve Bank of New York, Office of the Comptroller of the Currency and National Future Association in the US and Monetary Authority of Singapore, Hong Kong Monetary Authority and Financial Services Agency in Asia.

Due to the exit of the UK from the European Union, financial institutions and some of their customers that previously accessed European markets through the UK, will need to relocate activities to Europe to ensure business continuity and minimise disruption to clients. To manage the risks of Brexit, the RBS Group has re-established NatWest Markets N.V. in the Netherlands as a European hub. The set-up has necessitated the hiring of key trading, finance and risk staff, transfer of assets and liabilities from NatWest Markets Plc and NatWest Bank Plc, as well as gaining regulatory permissions. NatWest Markets N.V. started trading new business on 25 March 2019. The RBS Group has supported customers in their own Brexit readiness activities, offering flexibility over where their trading activity with NatWest Markets is carried out.

Banking regulation continues to evolve, with future changes including Basel 3.5/4, Fundamental Review of the Trading Book (FRTB), CRR2, the replacement of IBOR rates and increasing climate change related requirements such as those detailed in PRA SS3/19.

NatWest Markets has a readiness programme in place and is actively involved in BoE Task Forces, Federal Reserve working groups, Euro Sub-working groups and industry associations. Separately, to support customers NatWest Markets has established client education initiatives including public tools such as the NatWest Markets Realised Rate Calculator (www.realisedrate.com). Our Financing teams have played a leading role in clients' transition to SONIA, including as advisor and sole agent on Associated British Ports' change of a bond from LIBOR to SONIA.



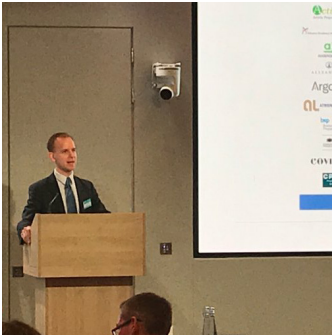


Building affordable homes

We have helped to execute over £2.4 billion of funding to the social housing sector in 2019. Helping to build more than 40,000 new homes over the next five years and ease the chronic shortage of social housing in the UK.

One of our largest customers, Sovereign Housing Association is committed to delivering 1,900 new homes per year by 2022. So we helped arrange a market-leading £250 million unsecured Revolving Credit Facility as part of a syndicate and became a Joint Lead Manager on it's £375 million, 29-year bond – giving Sovereign the finance it needed to build more social housing.

Building a more sustainable bank



Dr Arthur Krebbers, shared insights on issuing ESG debt at the ESG Financing in the Real Estate Sector seminar



US Head of Learning discussing diversity, inclusion and innovation as a panellist at the HMG Strategy CIO Leadership Summit



Welcomed disability rights advocate to our Stamford office for a discussion focused on diverse abilities in our workplace



Members of RBS's inaugural social bond deal team

Sustainable Finance

NatWest Markets is supporting our customers through the Environmental, Social, and Governance (ESG) evolution towards a carbon neutral and more sustainable economy with 'Green' or 'Social' financing ideas in the public and private markets and developing ESG friendly investment products.

In 2019, NatWest Markets supported all types of issuers to raise over £10 billion of Green, Social and Sustainable debt in a variety of currencies. We were involved with multiple debut transactions and innovative structures, including a CPI Linked Green issue. In the context of a changing regulatory and political environment, NatWest Markets realised the building demand for sustainably-minded fixed income products and lead managed some of the largest sterling green issues contributing to the growth of this market.

NatWest Markets launched the first ESG-product framework which was derived from ICMA's Sustainability Bond Guidelines and Green Bond Principles. This innovative Framework offers corporate and institutional investors the opportunity to subscribe to a range of NatWest Markets shorter dated ESG-linked liquidity and funding products.

We've partnered with our colleagues in NatWest Bank to engage with our clients around sustainability-linked loans and helped them to develop their sustainability strategy through this evolving product. In 2019, we participated in the financing of over £20 billion in sustainability-linked loans across our corporate and financial institutions client base.

In December 2019, NatWest Markets supported NatWest Bank on a £1 billion green synthetic securitisation – the first of its kind. The transaction is backed exclusively by 'green' assets, since the underlying assets are composed of renewable energy project finance loans.

We are an active participant in a variety of industry working groups focused on developing sustainable finance practises and standards. For example, we were part of AFME's Green Securitisation working group which published the first "Green Securitisation" guidelines in September 2019.

NatWest Markets regularly hosts ESG events enabling issuers and investors to have an open dialogue, exchange experiences and learn more about the challenges and opportunities offered by sustainability products. In November, we published our 2019 Global ESG investor Survey having received responses from investors around the world with assets under management totalling over \$16 trillion.

Sustainable Operations

As part of RBS Group we are committed to reducing the environmental impact of serving our customers.

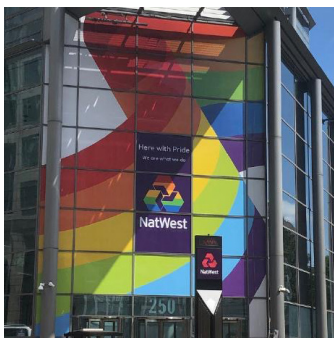
RBS Group set a carbon target of 45% reduction by 2020 to align RBS's environmental strategy and the decarbonisation required to support the Paris Agreement. They've also targeted a 50% reduction in business travel to reduce our carbon emissions footprint. These targets have both been met and you can find more detail on the sustainable banking section on [rbs.com](https://www.rbs.com) or in the RBS Group 2019 Annual Report & Accounts.

Well Controlled

NatWest Markets continued its work to embed climate change risks into its wider bank wide Risk framework in 2019. More information on the topic of climate change risk can be found in the Financial Reports Climate Risk Disclosure section.

Sustainable Engagement

In 2019, we held a number of townhall events across the bank that continued to raise the awareness and knowledge of our people on sustainability. We also have a Sustainable Finance Champions Network comprised of associates, analysts and apprentices from across NatWest Markets. This group of highly motivated juniors, utilise sustainability insights to support NatWest Markets strategy, client value and product suite. They also organised events throughout the year such as a "Teach in" at Bloomberg's new London headquarters to learn about their ESG tools delivered by sustainability experts. In addition, they spent a day cleaning up Brighton beach. While in Poland, colleagues spent the day at Kampinos National Park helping clear the forest of rubbish.



250 Bishopsgate wrapped in Pride colours in June



NWM women were inspired by advice on being a successful female leader by journalist and broadcaster Harriet Minter.



NWM India Diversity & Inclusion events encouraged colleagues to 'be yourself'



US colleagues celebrated Diwali

Diversity and inclusion

We aim to foster a culture of inclusion in everything we do, as we recognise that diversity is vital to our success.

- Our approach to recruitment, talent identification and promotion aims to make progress towards gender balance.
- We set an ambitious target of having 31% senior women in our top three leadership layers by the end of 2019. We achieved this target and are currently at 32%.
- The reported mean gender pay gap is 30.4% and the mean gender bonus gap is 49.9%. This shows progress from previous years, but also points to an area of continued focus as there is more to do.
- We continue to focus on Black, Asian and Minority Ethnic (BAME) talent within the top four leadership levels and through our graduate intake.
- We have a number of mentorship programmes that look to unite mentors and mentees across the Bank. We have a dedicated 'Mentor Matcher' tool for all employees as well as specific mentorship programmes for women, such as Rising Stars and Breakthrough.

Latest Gender Metrics (Dec 2019)

Metric	Dec 2019	2019 Target	Oct 2018	2018 Target
Females CEO - 3	32%	31%	30%	29%

Note: Data January - December 2019

A Great Place to Work

Our drive to make NatWest Markets a great place to work was recognised with two external awards this year. Our 'Come Back Programme' (offers initial short-term contracts to senior managers with finance-related backgrounds who've taken an extended career break) was shortlisted in the Working Families Best Practice Awards 2019. We were also shortlisted and won the Bronze Award at the Training Journal Awards 2019 Best Coaching/Mentoring Programme, recognising our work in building a coaching culture to support both individual and team effectiveness and performance.

Health and wellbeing

In 2019, we continued to make mental health a primary focus of our wellbeing activities. We continued to roll-out workshops across the business to help colleagues identify the signs and symptoms of mental ill-health and provide them with practical strategies to support each other. We offered enhanced training to a number of colleagues and now have Mental Health First Aiders who continue to provide support across the business.

Employee Led Networks

In addition to the RBS Group networks, we have a number of active employee led networks in NatWest Markets focused on developing a community across NatWest Markets that champions diversity whilst creating an inclusive workplace that gives our people the best opportunity to succeed and grow their careers.

Volunteering and community engagement

We are strong supporters of volunteering to support local communities across our regions. In London, we are building a strong relationship with ELBA (East London Business Alliance), supporting marginalised communities with CV surgeries and mock interviews as well as providing coaching to charity leaders.

Human rights and Modern Slavery Act

NatWest Markets are committed to our responsibilities to respect and uphold human rights across our business and sphere of influence. The Modern Slavery Act 2015 forms part of our approach to human rights, our third statement is available on nwm.com alongside our Human Rights Position Statement. Our approach covers our customers, our people and our suppliers. All of our people are legally recruited subject to local jurisdiction and in the UK must meet 1998 Immigration Act requirements.

NatWest Markets employees further support the cause of fighting modern slavery, with a team of more than 40 colleagues riding from our 250 Bishopsgate office to Brighton for TRIBE Freedom raising in excess of £15,000.

October was Diversity & Inclusion month which saw 20 events engaging 2,000 colleagues.

Outlook^(1,4)

NatWest Markets, like all companies, continues to deal with a range of significant risks and uncertainties in the external economic, political and regulatory environment. We will continue to actively monitor and react to market conditions.

NWM Plc is targeting the following in the medium-term

Metric ⁽²⁾	Estimate
RWA reduction	c.£14-18bn
CET 1 ratio	Above 15%
MREL ratio ⁽³⁾	At least 30%
Leverage ratio	At least 4%

In addition, NWM Plc plans to issue £3-5 billion of term senior unsecured instruments in 2020 and intends to meet the regulatory requirements in respect of the liquidity coverage ratio (LCR) and of the net stable funding ratio (NSFR) as it is introduced over time.

Notes:

(1) This supersedes all prior guidance.

(2) All metrics presented relate to NatWest Markets Plc.

(3) Includes total regulatory capital, non-eligible capital plus downstreamed internal MREL.

(4) The targets, expectations and trends discussed in this section represent management's current expectations and are subject to change, including as a result of the factors described in the "Risk Factors" section on pages 143 to 156 in this document. These statements constitute forward-looking statements. Refer to Forward-looking statements in this announcement.

Risk overview

Effective risk management is central to the successful delivery of the NatWest Markets strategy.

Natwest Markets Group (NWM Group) operates within the RBS Group's integrated risk management framework. The framework is centred upon the embedding of a strong risk culture and ensuring tools are in place to identify and manage both internal and external threats. Risk appetite defines the level and types of risk NWM Group is willing to accept, it is set in line with overall strategy and approved by the Board.

Areas of focus in 2019

NWM Group continued to focus on the following key risks:

Market risk arising from its trading and banking book activities that provide a range of financing, risk management and investment services to clients. Despite market volatility driven by geopolitical events throughout the year, Traded VaR remained well within appetite. Key areas of focus in 2019 included refining risk appetite levels and the Fundamental Review of the Trading Book.

Credit risk arising from derivative, financing and banking book transactions with Sovereigns, Financial Institutions and Corporate clients. There was a moderate portfolio increase largely driven by transfers from NWB Group as well as the full acquisition of NWM N.V. Key areas of focus included adapting the risk management framework to support NWM N.V. and Financial Sponsors.

Operational risk arising from inadequate or failed internal processes, people and systems, or external events. Key areas of focus in 2019 included improving the risk profile of key operational risks such as Trade & Transaction Reporting, Financial Reporting, Model Risk and Data Management. More generally we have focussed on maintaining a robust control environment across Operational Risk, Financial Crime and Conduct Risk, successfully evidenced by a continued reduction in our overall risk issue profile and higher materiality issues and a continued low level of operational risk losses.

There was significant focus on thematic risk issues. These included:

Brexit: Oversight of planning for regulatory, legislative and economic

impacts remained a critical part of forward-looking risk management throughout the year. This included stress testing, scenario modelling and capital planning. The potential second and third order effects on NWM Group and its customers were a further area of focus including planning for the results of periodic financial volatility and slower economic growth.

Innovation and technology also continued to be central. During 2019 risk management focused on regulatory requirements for Cloud service providers in the financial industry and ensuring effective third-party risk management and governance.

Cyber security remains a key consideration during the development phase of new business projects to ensure protection for both NWM Group and its customers. In 2019, the threat landscape continued to evolve. During the year further investment in control enhancements included new anti-malware controls and improved security testing tooling to quickly detect and remediate potential vulnerabilities.

Climate change: NatWest Markets continues to consider the impact of multiple risks relating to climate change, including physical and economic risks caused by extreme weather events as well as risks arising from the transition to a low-carbon economy. Climate risk is classified as a top risk and is being integrated into core risk management. NWM Group supports the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures and has a franchise-wide climate risk working group.

Financial crime: The financial crime threat continues to evolve in line with changes in technology, economy and wider society. In 2019, work to enhance policies, systems and the financial crime control environment used to combat financial crime continued. A strong emphasis was also maintained on ensuring proportionate, risk-focused customer due diligence standards are in place. Improvements to the wider

financial crime control environment remained a key focus.

Anti-bribery and corruption (ABC)

NWM Group is committed to ensuring it acts responsibly and ethically, both when pursuing its own business opportunities and when awarding business. Consequently, it has embedded appropriate policies, mandatory procedures and controls to ensure its employees, and any other parties it does business with, understand these obligations and abide by them whenever they act for NWM Group. ABC training is mandatory for all staff on an annual basis, with targeted training appropriate for certain roles. RBS considers ABC risk in its business processes including, but not limited to, corporate donations, charitable sponsorships, political activities and commercial sponsorships. Where appropriate, there is a requirement for ABC contract clauses in written agreements.

LIBOR transition: NWM Group is continuing its preparations for the full transition from LIBOR to other interest-rate benchmarks by the end of 2021. This is a major undertaking since a significant number of transactions across the industry reference LIBOR. NWM Group is aligned to the RBS Group LIBOR programme and continues to work closely with regulators and industry bodies to manage the impact. Oversight of work to prepare for the transition has been a major focus along with activities across all three lines of defence to minimise risk and disruption to customers (including the launch of a tool to allow customers using SONIA to calculate compounded rates in all major tenors). Activity to assess the conduct risk implications for NWM Group and its customers has also been a key focus.

Top and emerging risks

The NWM Group employs a regular process for identifying and managing its top and emerging risks. Top and emerging risks are those that could have a significant negative impact on the NWM Group's ability to operate or meet its strategic objectives.

Top and emerging risks

External

Economic & Political Risks	The NWM Group is exposed to economic and political risks arising from the markets in which it operates, including the risks arising from market volatility or a sustained period of low economic growth. NWM Group continues to use a range of complementary approaches to inform strategic planning and risk mitigation. This includes active management of portfolios and adjustment of risk appetite, scenario planning and stress testing. The NWM Group has implemented plans to prepare for the UK's loss of access to the European Single Market and continues to monitor geopolitical events and developments in relation to its target markets.
Climate Related Risks	Accelerating climate change may lead to heightened financial risks and faster-than-anticipated impacts on the NWM Group and the wider economy. These include financial loss as a result of deterioration in credit quality, market risk exposure and operational risk. The NWM Group continues to adapt its operation and business strategy to mitigate the risks of both climate change and the transition to a low-carbon economy. In addition, the NWM Group is embedding climate risk into its risk management framework.
Cyber Threats	Cyber-attacks continue to increase in frequency, sophistication and severity. There is a risk that a catastrophic cyber-attack damages the NWM Group's ability to do business and/or compromises data security. The NWM Group operates a multi-layered approach to its defences and continues to invest in building its resilience and cybersecurity capabilities.
Competitive Environment	NWM Group's target markets are highly competitive, with changes in technology, regulation, customer behaviour and business models continuing to accelerate competitive pressure. The NWM Group monitors the competitive environment and adapts strategy as appropriate to ensure its business model remains sustainable and viable. NWM Group remains focused on innovating to deliver compelling propositions for customers.
Regulatory, Legal & Conduct Risk	The NWM Group continues to face stringent regulatory and supervisory requirements, particularly regarding conduct, financial crime, the use of models, and capital and liquidity management. Material changes in regulation, including those that could increase the NWM Group's capital obligations, or a failure to meet regulatory expectations, could affect business strategy. While the NWM Group is subject to litigation and regulatory enforcement in relation to historical activities, it continues to embed a strong and comprehensive risk and compliance culture. The NWM Group engages with regulators to implement new regulatory requirements and incorporates the implications of proposed or potential regulatory activities in its strategic and financial plans.

Internal

Strategic Risk	The RBS Group and NWM Group have announced a new strategy for the NWM Group including an increased focus on serving the RBS Group's corporate and institutional customer base. Over the medium term, NWM Group intends to simplify its operating model and technology platform, as well as reduce its cost base and capital requirements. The changes required are substantial, will be implemented over several years and will entail material execution, commercial and operational risks for the NWM Group.
Financial Viability	In common with other banks, there is a risk that NWM Group fails to adequately manage and optimise its short-term and long-term liquidity and funding. In addition, there is a risk that the level of NWM Group's risk-weighted assets increases requiring additional capital to be raised, changes to dividend plans or resulting in weaker financial metrics. NWM Group also has a dependency on RBS Group's strategic decisions, which could affect its own strategy. To mitigate these risks, NWM Group has clear liquidity and funding targets that allow for variability and uses stress tests to assess its future needs. The NWM Group's Board maintains proactive engagement with the RBS Group to ensure strategic alignment.
Third Party Suppliers	The NWM Group has a dependency on services provided by the RBS Group's ring-fenced entities. In addition, inadequate control over selection, governance and oversight of third-party suppliers could affect operational resilience. Governance is in place to ensure NWM Group is regularly engaged with the ring-fenced bank regarding service levels and continues to be diligent in its screening of suppliers with strict contractual obligations governing supplier relationships and activity.
IT System Resilience	The RBS Group continues to invest in its IT infrastructure – including NWM Group's IT systems – to prevent customer service disruption, which could result in reputational and regulatory damage. A major investment programme has significantly improved the resilience of the systems and further progress is expected to mitigate legacy system vulnerabilities and modernise the infrastructure to deliver a future-state technology platform for NWM Group.
Culture & People Risk	There is a risk that NWM Group lacks sufficient capability or capacity at a senior level to deliver – or adapt to – change. NWM Group monitors people risk closely and has plans in place to support retention of key roles, with wider RBS Group programmes supporting engagement and training in place for all employees. Ensuring a healthy organisational culture remains a core priority, including the promotion of workforce diversity and a major focus on developing future skills and capabilities to tackle the evolving business environment. Across the RBS Group, a multi-year programme focused on enhancing culture – including risk culture – is ongoing. This aims to deliver strong customer and business outcomes, reducing the risk of material staff misconduct and supporting business sustainability. NWM Group's Conduct & Culture Committee has a specific focus on enhancing culture.
Data Management	Ineffective management of data, including a breach in data privacy, could have material negative impacts. The NWM Group operates a control and policy framework governing data usage and continued to evolve a long-term data strategy.
Control Environment	The internal system of controls is key to the NWM Group's management of its risks. Failure to maintain a sustainable control environment, due to changes in NWM Group's operating environment or business strategy, could result in an increase in risks across NWM Group. To mitigate these risks, a robust operational risk management framework is in place to support ongoing identification, management and monitoring of our risk and control profile. In addition, our overall control environment (including operational, conduct and financial crime risks) is formally assessed half-yearly to ensure that NWM Group's control environment position remains within appetite.

How stakeholder interests influenced Board discussions and decision-making

Stakeholder engagement and s.172(1) statement

This section of the Strategic Report describes how the directors have had regard to the matters set out in section 172(1) (a) to (f), and forms the directors' statement required under section 414CZA, of The Companies Act 2006.

Board training & support on s172 duties

Directors are supported in the discharge of their duties by the Company Secretary. All directors receive guidance on their statutory duties including Section 172 and were briefed on the new reporting requirements introduced by the Companies (Miscellaneous Reporting) Regulations 2018 in advance of the effective date. We have introduced a new approach to board papers with a much greater focus on ensuring relevant stakeholder interests are clearly articulated in Board and Committee papers and have refreshed our guidance on documenting decisions to ensure these are recorded in a consistent manner across RBS Group.

Customers

Customers are at the heart of everything NWM Plc does. During the year, the Board received updates on key customer issues through customer performance updates and regular reviews from customer-facing business heads. The Board also held deep-dive sessions on several individual product lines and customer segments.

The Chairman and Chief Executive Officer have regular meetings with customers to enhance relationships and understand their views.

Colleagues

The term "colleagues" when used in this Report includes all members of our workforce (e.g. contractors, agency workers).

Colleague Voice

The NWM Plc Board (the Board) promotes colleague voice in Boardroom through a variety of channels.

During 2019, the directors participated in visits to businesses and functions. There was also a 'Meet the Board' event for staff, attended by the Chairman and Executive Directors.

Engaging colleagues

Every year, colleagues are asked to share their thoughts on what it's like to work for RBS Group via a colleague opinion survey. The results from the 2019 survey showed a further improvement in colleague sentiment and demonstrate that the culture is changing for the better. Key measures of engagement, leadership and people management have increased and NWM Plc is above the global financial services norm in all comparable survey categories.

At RBS Group-wide level, the Colleague Advisory Panel (the Panel), met twice during 2019, providing a valuable mechanism for directors to engage directly with colleagues on topics of strategic interest affecting RBS Group and its workforce, and offering colleagues a greater understanding of the Board's role. Topics discussed with the Panel included purpose, future strategy, Executive pay, inclusion and sustainability.

Employee consultation

Having ongoing discussion and engagement with a number of employee representatives such as trade unions and work councils is vital and RBS Group regularly discusses developments and updates on the progress of strategic plans.

Speak Up

Colleagues may report any concerns relating to wrong doing or misconduct via RBS Group's whistleblowing service, Speak Up. The 2019 colleague opinion survey showed the highest ever score when asking colleagues if they feel safe to speak up, as well as an understanding of the process by which to do so. In 2019, 22 cases were raised compared to 14 in 2018.

Investing in colleagues

RBS Group has also transformed colleagues' experience by deploying new digital tools. Workday was implemented as a new digital HR platform in November 2019 and includes a mobile app, giving colleagues an experience on par with the digital experience which customers enjoy. ServiceNow was extended to improve how RBS Group responds to colleagues' queries, and an expanded HR chat bot has helped over 50,000 colleagues to answer their basic queries. These enhancements

are enabling RBS Group to respond to the evolving world of work and needs of its workforce.

Health and wellbeing of colleagues

As a strong component of making RBS Group a great place to work, wellbeing initiatives have been successfully delivered against four pillars; Physical, Mental, Social and Financial Wellbeing. Further details can be found in the 2019 Annual Report and Accounts of RBSG plc and on rbs.com.

Inclusion

RBS Group is proud to be building an inclusive bank which is a great place for all colleagues to work. RBS Group's inclusion guidelines apply to all colleagues globally and focus on five key priorities - LGBT Innovative, Gender Balanced, Disability Smart, Ethnically Diverse, all leading to Inclusive Culture. Detailed information can be found on rbs.com.

RBS Group has been recognised for work on Equality, Diversity and Inclusion in 2019 by retaining position in the Times Top 50 Employers for Women; being recognised again as a Top 10 Employer for Working Families; being Exemplary Level in the Scottish Carer Positive Campaign; being a Top Global Stonewall employer; being a Top Ten Employer in the Investing in Ethnicity Maturity Matrix; and rated as Gold in the Business Disability Forum benchmark.

Employment of people with disabilities

RBS Group policy is that people with disabilities are considered for employment and subsequent training, career development and promotion based on merit. If members of staff become disabled, it is the policy of RBS Group, wherever possible, to retain them in their existing jobs or re-deploy them in suitable alternative duties.

Investors

The Board recognises that increasing investors' and stakeholders' understanding of RBS Group is important for ensuring access to capital markets. In 2019, senior management spent time meeting investors in key financial centres. This investor engagement helped facilitate the planned diversification of NWM's funding base through access to new markets (SEK,

JPY and CHF) via its EMTN programme and the establishment of a 144A MTN programme for US investors.

Regulators

The Board recognises the importance of open and continuous dialogue with regulators. The Chairman and Executive Directors have regular meetings with the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA) and individual directors engage regularly with both regulators through Continuous Assessment and Proactive Engagement meetings.

Suppliers

The Board recognises the key role suppliers play in ensuring NWM delivers a reliable service to its customers. In October, the Board held a suppliers' spotlight session, which included an overview of the shared services procured from NatWest Holdings Ltd. The Board also spent time considering proposed material outsourcing arrangements to ensure they are sufficiently robust.

Community and Environment

The Board is committed to managing the wider social, environmental and economic impacts of NWM Plc's operations. This includes the way it deals with its customers and manages sustainability issues in its supply chain. Refer to [rbs.com](https://www.rbs.com) for RBS Group's Modern Slavery Statement and details of the Supplier Code of Conduct, both of which apply to NWM Plc and other relevant subsidiaries within RBS Group. It is recognised by the RBSG plc Board that climate change must have greater prominence at both senior management and board levels across RBS Group, including within NWM Plc. Further details on RBS Group's response to climate change can be found within the RBSG plc Annual Report & Accounts 2019.

How stakeholder interests have influenced decision making

The company recognises the importance of engaging with stakeholders to help inform strategy and Board decision-making. Relevant stakeholder interests, including those of colleagues, are taken into account by the Board when it takes decisions.

NWM Plc defines principal decisions as those that are material, or of strategic importance, to NWM Plc, or are significant to any of its key stakeholder groups.

The acquisition of NatWest Markets N.V. provides an example of how stakeholder interests were considered in a principal decision made by the Board.

Principal decision – Acquisition of NatWest Markets N.V.

NatWest Markets N.V. (NWM N.V.) was repurposed in March 2019 to allow NWM to continue to serve EEA clients after the UK leaves the European Union.

In November 2019, the Board approved the acquisition of RBS Holdings N.V. and its subsidiary, NWM N.V., from RBSG plc.

In reaching its decision, the Board took account of the interests of all relevant stakeholders. For example, the Board considered the interests of clients so as to ensure that none would be disadvantaged by the transfer of ownership.

The Board also ensured that the company's regulators were kept fully apprised throughout the acquisition process. The change of control was approved by the European Central Bank and the DNB on 20 November.

The Board also considered the capital, liquidity and other impacts that the transfer might have on RBS Group, being the sole shareholder of both entities.

Further details on how RBS Group engages with its stakeholders can be found in the 2019 Annual Report & Accounts of RBSG plc and on [rbs.com](https://www.rbs.com).

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Presentation of information

NatWest Markets Plc ('NWM Plc') is a wholly-owned subsidiary of The Royal Bank of Scotland Group plc ('RBSG plc' or 'the holding company'). NatWest Markets Group ('NWM Group') comprises NWM Plc and its subsidiary and associated undertakings. The term 'RBS Group' comprises RBSG plc and its subsidiary and associated undertakings.

With effect from 29 November 2019, RBS Holdings N.V. (RBSH N.V.) is a wholly-owned subsidiary of NWM Plc. RBSH N.V. is the parent company of NatWest Markets N.V. (NWM N.V.). The term 'NWM N.V. Group' comprises NWM N.V. and its subsidiary and associated undertakings. NWM N.V. is a licensed bank regulated by De Nederlandsche Bank.

NWM Group publishes its financial statements in pounds sterling ('£' or 'sterling'). The abbreviations '£m' and '£bn' represent millions and thousands of millions of pounds sterling, respectively, and references to 'pence' represent pence in the United Kingdom ('UK'). Reference to 'dollars' or '\$' are to United States of America ('US') dollars. The abbreviations '\$m' and '\$bn' represent millions and thousands of millions of dollars, respectively, and references to 'cents' represent cents in the US. The abbreviation '€' represents the 'euro', and the abbreviations '€m' and '€bn' represent millions and thousands of millions of euros, respectively.

NWM Group legal entity disclosures

There is a distinction between the disclosure of the NatWest Markets operating segment performance in RBSG plc's 2019 Annual Report and Accounts (ARA), and NWM Group's disclosures as presented in this document:

- NatWest Markets Group's legal entity disclosures include the Central items & other segment, but exclude the NWM N.V. results for the period until it was acquired by NWM Plc on 29 November 2019.
- RBSG plc's 2019 ARA reports the NatWest Markets segment including NatWest Markets N.V. for the whole year, but excludes the Central items & other segment.

Non-IFRS financial measures

NWM Group prepares its financial statements in accordance with IFRS as issued by the IASB and as adopted by the European Union, which constitutes a body of generally accepted accounting principles (GAAP). This document contains a number of adjusted or alternative performance measures, also known as non-GAAP or non-IFRS financial measures. These measures are adjusted for certain items which management believe are not representative of the underlying performance of the business and which distort period-on-period comparison. These non-IFRS financial measures are not measures within the scope of IFRS and are not a substitute for IFRS measures. These measures include:

- Management analysis of the operating expenses shows strategic costs and litigation and conduct costs in separate lines on page 19. These amounts are included in staff, premises and equipment and other administrative expenses in the statutory analysis.
- Funded assets defined as total assets less derivatives.
- Management view of core and legacy for income, funded assets and RWAs. Legacy consists predominantly of the residual exposures which were reported in Capital Resolution until its closure after Q3 2017, as well as certain funding costs.

Performance overview

NWM Group reported a loss for the year ended 31 December 2019 of £121 million compared with a loss of £1,244 million from continuing operations for the year ended 31 December 2018, reflecting the non-repeat of litigation and conduct costs from the prior year as well as certain one-off cost recoveries in 2019, offset partially by lower income in challenging market conditions.

Income, costs and legacy issues:

- Income was £719 million in 2019, compared with £858 million in 2018, reflecting lower Core income in challenging market conditions. Rates income was particularly impacted due to elevated hedging costs caused by reduced liquidity and wider bid-offer spreads as the market experienced sustained curve flattening across global fixed income markets, most notably during Q3 2019.
- Operating expenses of £997 million were lower compared with £2,237 million in 2018, largely reflecting reimbursement under indemnification agreements with third parties and other one-off cost recoveries in Central items & other during 2019 as well as the non-repeat of the RMBS settlement with the US Department of Justice (DoJ) in the prior year.

Balance sheet, capital and risk-weighted assets (RWAs):

- NWM Group's total assets and liabilities increased by £18.2 billion and £17.4 billion to £266.1 billion and £256.2 billion respectively at 31 December 2019, compared with the prior year. The increases primarily reflect derivative fair values, driven by downward shifts in interest rate yields and new business during the year, partially offset by sterling having strengthened against major currencies.
- NWM Plc issued £5.0 billion of term senior unsecured debt securities in benchmark and private placement formats during 2019, in line with the £3-5 billion funding target.
- NWM Plc paid ordinary dividends totalling £500 million to its parent company, RBSG plc, during the year ended 31 December 2019.
- Total NWM Plc RWAs reduced to £35.2 billion at 31 December 2019 from £40.8 billion at 31 December 2018 due to lower market risk, counterparty credit risk and operational risk RWAs, partially offset by an increase in credit risk RWAs resulting from the acquisition of the SABB shareholding.
- NWM Plc's Common Equity Tier 1 (CET1) ratio increased to 17.3% from 15.6% at 31 December 2018, primarily reflecting lower RWAs, offset by dividends paid and other reserve movements in the year. The CRR leverage ratio increased to 5.1% (2018 – 5.0%).

NatWest Markets N.V. and Saudi British Bank (SABB) developments:

- NWM N.V. began transacting new business on 25 March 2019 to ensure continuity of service to European Economic Area (EEA) customers following the UK's exit from the European Union (EU). NWM N.V. Group was acquired by NWM Plc and became a part of NWM Group with effect from 29 November 2019.
- On 16 June 2019, the merger of Alawwal bank and SABB was completed. RBS Group's economic interest in the newly-merged SABB entity, amounting to 4.1%, was acquired by NWM Plc from NWM N.V. on the same day.

Continuing to simplify and de-risk the business:

- NWM Group continued to reduce legacy positions during 2019. Legacy funded assets were £3.1 billion (2018 – £4.1 billion) and legacy RWAs £4.5 billion (2018 – £6.4 billion).
- Net non-investment grade exposures (banking book credit risk and counterparty credit risk for traded products), increased to £2.5 billion at 31 December 2019 (2018 – £1.8 billion) based on external credit ratings. This was largely as a result of derivative fair value increases on existing exposures, as well as credit downgrades on collateralised positions.
- Legacy non-investment grade exposures reduced to £0.7 billion (2018 – £1.1 billion).
- IFRS 9 Stage 3 exposures reduced to £0.2 billion following the exit of a legacy defaulted position (2018 – £0.7 billion). Stage 3 ECL was broadly unchanged compared with 2018.

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Performance overview [continued](#)

The table below sets out the performance key metrics and ratios.

Performance key metrics and ratios ⁽¹⁾	2019	2018
Liquidity coverage ratio (LCR) (%) ⁽²⁾	254	457
Liquidity portfolio (£bn) ⁽²⁾⁽³⁾	16.1	16.6
Stressed coverage ratio (%) ⁽²⁾	153	208
Total wholesale funding (£bn) ⁽⁴⁾	21.9	19.8
Total funding including repo (£bn)	85.0	80.0
Common Equity Tier (CET 1) ratio (%)	17.3	15.6
CRR leverage ratio (%)	5.1	5.0
Risk-weighted assets (RWAs) (£bn)	35.2	40.8
Total Capital ratio (%)	24.2	21.5
Total CRR-compliant MREL (£bn)	13.5	13.9
Total MREL ratio (%)	38.4	34.0

Notes:

(1) Capital, leverage and RWAs are based on the PRA transitional arrangements for NWM Plc. Regulatory capital is monitored and reported at NWM Plc level.

(2) These metrics are shown for NWM Plc as managed internally.

(3) Primary liquidity value at 31 December 2019 was aligned to the internal stressed outflow coverage, which is stated after discounts (or haircuts) are applied to instruments. The liquidity values for 2018 have been re-presented.

(4) Excludes derivative cash collateral received, customer deposits, repo and intra-RBS Group balances.

Simplifying and de-risking

The table below presents a summary of NWM Group's balance sheet exposures. The legacy positions consist predominantly of the residual exposures which were reported within Capital Resolution until its closure after Q3 2017. These exposures are primarily derivatives or loan agreements that are either being exited or run down over time. Non-investment grade refers to those exposures below AQ4 on the asset quality scale, refer to pages 51 and 56 for further detail.

	2019		2018	
	Total £bn	of which: Legacy £bn	Total £bn	of which: Legacy £bn
RWAs	35.2	4.5	40.8	6.4
Total net credit exposures (banking book and counterparty credit)	43.4	4.1	39.3	5.9
of which: net non-investment grade credit exposures	2.5	0.7	1.8	1.1
of which: IFRS 9 Stage 3 exposures	0.2	0.2	0.7	0.7
and: IFRS 9 Stage 3 expected credit loss (ECL)	0.1	0.1	0.1	0.1

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Performance overview continued

The table below presents a segmental analysis of key lines of NWM Group's income statement. Commentary refers to the table below as well as the statutory income statement presented on page 78.

	2019			2018			Variance £m	Variance %
	NatWest Markets £m	Central items & other £m	Total £m	NatWest Markets £m	Central items & other £m	Total £m		
Income statement								
Net interest income	(160)	10	(150)	5	(272)	(267)	117	(44%)
Non-interest income	850	19	869	1,013	112	1,125	(256)	(23%)
Total income	690	29	719	1,018	(160)	858	(139)	(16%)
Strategic costs	(162)	(9)	(171)	(178)	(30)	(208)	37	(18%)
Litigation and conduct costs	(18)	112	94	(142)	(827)	(969)	1,063	(110%)
Other operating expenses	(1,099)	179	(920)	(1,075)	15	(1,060)	140	(13%)
Operating expenses	(1,279)	282	(997)	(1,395)	(842)	(2,237)	1,240	(55%)
Operating (loss)/profit before impairments	(589)	311	(278)	(377)	(1,002)	(1,379)	1,101	(80%)
Impairment releases	48	—	48	88	14	102	(54)	(53%)
Operating (loss)/profit before tax	(541)	311	(230)	(289)	(988)	(1,277)	1,047	(82%)
Tax credit	—	—	109	—	—	33	76	230%
Loss from continuing operations	—	—	(121)	—	—	(1,244)	1,123	(90%)
Profit from discontinued operations, net of tax	—	—	—	—	—	2,461	(2,461)	(100%)
(Loss)/profit for the year	—	—	(121)	—	—	1,217	(1,338)	(110%)
Income								
Rates	374	—	374	579	—	579	(205)	(35%)
Currencies	427	—	427	430	—	430	(3)	(1%)
Financing	385	—	385	375	—	375	10	3%
Revenue share paid to other RBSG segments	(208)	—	(208)	(171)	—	(171)	(37)	22%
Core income excluding OCA	978	—	978	1,213	—	1,213	(235)	(19%)
Legacy	(208)	—	(208)	(287)	—	(287)	79	(28%)
Own credit adjustments (OCA)	(80)	—	(80)	92	—	92	(172)	(187%)
Other	—	29	29	—	(160)	(160)	189	(118%)
Total income	690	29	719	1,018	(160)	858	(139)	(16%)

The operating loss before tax was £230 million compared with a loss before tax from continuing operations of £1,277 million in 2018. Total income of £719 million was down by £139 million compared with £858 million in the prior year, primarily reflecting lower trading income in challenging market conditions. Operating expenses reduced by £1,240 million to £997 million in 2019, largely due to reimbursement under indemnification agreements with third parties in respect of legacy litigation and certain one-off cost recoveries in 2019, as well as the non-repeat of RMBS-related litigation and conduct costs in 2018.

Income

Net interest income was a net expense of £150 million compared with a net expense of £267 million in 2018. Net interest expenses largely represent funding costs of the business and are primarily reflected in the NatWest Markets segment in 2019 following the structural reorganisation in 2018.

Non-interest income decreased by £256 million to £869 million compared with £1,125 million in 2018, driven by income from trading activities which reduced to £805 million (2018 - £1,045 million) as challenging trading conditions particularly affected Rates income, most significantly during Q3 2019. Rates income was impacted due to elevated hedging costs caused by reduced liquidity and wider bid-offer spreads as the market experienced sustained curve flattening across global fixed income markets. Other operating income of £77 million in 2019 was £125 million higher than 2018, reflecting the non-recurrence of reserves recycling and disposal losses in the prior year. There was no gain on redemption of own debt during 2019 (2018 - £101 million).

Operating expenses

Operating expenses of £997 million were £1,240 million lower than in 2018. Litigation and conduct costs, a credit of £94 million, predominantly reflected £162 million reimbursement under indemnification agreements with third parties, partially offset by other charges during 2019. This compared with prior year costs of £969 million which were largely driven by the settlement with the US Department of Justice (DoJ) in relation to RMBS matters. Strategic costs reduced £37 million in 2019 to £171 million from £208 million in 2018.

Other operating expenses decreased to £920 million from £1,060 million in 2018, largely due to certain one-off cost recoveries during 2019.

Impairments

Impairment releases were £48 million in 2019 compared with £102 million in 2018. Recoveries on IFRS 9 Stage 3 defaulted assets were lower in 2019 compared with the prior year although this was partly offset by a release relating to the reduction in Stage 2 loans during 2019.

NatWest Markets segment

The operating loss before tax was £541 million compared with an operating loss of £289 million in 2018, driven by lower Core income of £978 million which was impacted by challenging market conditions, particularly impacting Rates, when compared to the prior year (£1,213 million). Legacy losses of £208 million in 2019 (2018 - £287 million) largely reflects the absorption of net interest expenses previously within Central items & other. Operating expenses reduced by £116 million to £1,279 million in 2019, mainly due to lower litigation and conduct costs and strategic costs compared with 2018. Own credit adjustments were a £80 million loss in 2019, compared with gain of £92 million in 2018, due to the tightening of spreads.

Central items & other segment

The operating profit before tax was £311 million compared with a loss of £988 million in 2018. Net interest income of £10 million was £282 million higher than the prior year, reflecting funding costs that have transferred to NatWest Markets segment. Litigation and conduct credits of £112 million compare with costs of £827 million in 2018, driven by £162 million in reimbursement under indemnification agreements with third parties partially offset by charges during 2019 as well as the non-repeat of RMBS-related costs the prior year. Other operating expense credits of £179 million, an increase from £15 million in 2018, largely relate to certain one-off cost recoveries during the year.

Financial Review

Performance overview continued

The table below presents a segmental analysis of key balance sheet asset lines for NWM Group. Commentary refers to the tables below as well as the consolidated balance sheet on page 79.

	31 December 2019			31 December 2018			Variance	
	NatWest Markets	Central items & other	Total	NatWest Markets	Central items & other	Total	Total	
	£bn	£bn	£bn	£bn	£bn	£bn	£bn	%
Balance sheet								
Funded assets	117.4	—	117.4	111.2	2.4	113.6	3.8	3.3%
of which: Core	114.3	—	114.3	107.1	2.4	109.5	4.8	4.4%
of which: Legacy	3.1	—	3.1	4.1	—	4.1	(1.0)	(24.4%)
Derivative assets	148.7	—	148.7	133.9	0.4	134.3	14.4	10.7%
Total assets	266.1	—	266.1	245.1	2.8	247.9	18.2	7.3%

Total assets and liabilities increased by £18.2 billion and £17.4 billion to £266.1 billion and £256.2 billion respectively at 31 December 2019, compared with £247.9 billion and £238.8 billion at 31 December 2018. Funded assets, which exclude derivatives, increased by £3.8 billion to £117.4 billion at 31 December 2019.

Cash and balances at central banks of £12.7 billion at 31 December 2019 were up by £1.5 billion compared with £11.2 billion in 2018, driven by a range of factors including net issuance activity in the period and the acquisition of NWM N.V..

Trading assets, which primarily relate to client-led activity as well as derivative cash collateral posted, increased to £76.6 billion at 31 December 2019, moderately higher than the prior year end as the balance sheet was managed within limits (2018 - £75.0 billion). Trading liabilities increased by £1.5 billion to £73.8 billion at 31 December 2019 (2018 - £72.3 billion).

Settlement balance assets and liabilities increased to £4.3 billion and £4.0 billion respectively, reflecting partially higher year end trading volumes (2018 - £2.7 billion and £2.9 billion respectively).

Derivative assets and derivative liabilities were up £14.4 billion to £148.7 billion and £14.2 billion to £144.1 billion respectively compared with year end 2018. The increases in mark-to-market were driven by a downward shift in interest rate yields and new business during the year, partially offset by sterling having strengthened against major currencies since year end 2018.

Other financial assets increased to £12.3 billion at 31 December 2019 (2018 - £11.3 billion) primarily driven by the equity holding in SABB. Other financial liabilities increased to £18.4 billion (2018 - £16.3 billion) largely driven by net benchmark issuance activity in the year and the acquisition of NWM N.V..

Amounts due from and to the holding company and fellow subsidiaries reduced to £1.2 billion and £8.3 billion respectively, largely as a result of the consolidation of NWM N.V. (2018 - £3.4 billion and £10.2 billion).

Owners' equity increased by £0.8 billion to £9.9 billion, primarily due to the equity contribution from RBSG plc at the time of the NWM N.V. acquisition, dividends paid and other reserves movements during 2019.

Balance sheet profile as at 31 December 2019

The NWM Group balance sheet profile is summarised as follows:

Assets	£bn	£bn	Liabilities
Cash and balances at central banks	12.7		
Trading assets	76.6	73.8	Trading liabilities
Securities	30.1	21.2	Short positions
Reverse repos (1)	24.1	27.9	Repos (2)
Derivative cash collateral posted (3)	20.5	21.5	Derivative cash collateral received (4)
Other trading assets	1.9	3.2	Other trading liabilities
Loans - amortised cost	9.5	5.8	Deposits - amortised cost
Settlement balances	4.3	4.0	Settlement balances
Amounts due from holding company and fellow subsidiaries	1.1	8.3	Amounts due to holding company and fellow subsidiaries
Other financial assets	12.3	18.5	Other financial liabilities
Other assets	0.9	1.7	Other liabilities
Funded assets	117.4	112.1	Liabilities excluding derivatives
Derivative assets	148.7	144.1	Derivative liabilities
Total assets	266.1	256.2	Total liabilities
		21.9	of which: wholesale funding (5)
		8.8	of which: short-term wholesale funding (5)
Net derivative assets	4.3	4.2	Net derivative liabilities

Notes:

- (1) Comprises bank reverse repos of £4.9 billion (2018 - £8.0 billion) and customer reverse repos of £19.2 billion (2018 - £16.8 billion).
- (2) Comprises bank repos of £6.6 billion (2018 - £5.0 billion) and customer repos of £21.3 billion (2018 - £20.6 billion).
- (3) Comprises derivative cash collateral posted relating to banks of £7.6 billion (2018 - £7.3 billion) and customers of £12.9 billion (2018 - £11.6 billion).
- (4) Comprises derivative cash collateral received relating to banks of £11.9 billion (2018 - £11.0 billion) and customers of £9.6 billion (2018 - £9.1 billion).
- (5) Excludes derivative cash collateral received, repo, customer deposits and intra-RBS Group balances.

Board of directors and secretary

Board and committees

Chairman

Frank Dangeard (appointed 16 May 2016)

[Chairman of the Nominations Committee](#)

[Chairman of the Board Risk Committee \(to 21 January 2019\)](#)

[Chairman of the Remuneration Committee \(to 13 September 2019\)](#)

Executive directors

Robert Begbie (appointed 18 December 2019)

[Interim Chief Executive Officer](#)

Independent non-executive directors

Vivek Ahuja (appointed 30 April 2018)

[Chairman of Board Risk Committee \(from 21 January 2019\)](#)

Brendan Nelson (appointed 1 April 2010)

[Chairman of Audit Committee](#)

Sarah Wilkinson (appointed 30 April 2018)

Tamsin Rowe (appointed 27 March 2019)

[Chairman of the Remuneration Committee \(from 13 September 2019\)](#)

The following executive directors resigned on 18 December 2019:

Chris Marks

Richard Place

Auditors

Ernst & Young LLP

Chartered Accountants and Statutory Auditor

25 Churchill Place

London E14 5EY

Registered office

36 St Andrew Square

Edinburgh EH2 2YB

Telephone: +44 (0)131 556 8555

Principal office

NatWest Markets Plc

250 Bishopsgate

London EC2M 4AA

NatWest Markets N.V.

Claude Debussylaan 94

1082 MD Amsterdam

The Netherlands

NatWest Markets Holdings USA Inc.

600 Washington Blvd

Stamford

CT 06901 USA

NatWest Markets Plc

Registered in Scotland No. SC90312

Capital and risk management

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Presentation of information

Where indicated in the section headers, information in the Capital and risk management section (pages 22 to 63) is within the scope of the Independent auditor's report. Where a main section header, presented in bold, is marked as audited, all subsequent sub sections are also audited, the end of the audited section is marked by Δ . Capital and risk management are generally conducted on an overall basis within RBS Group such that common policies, procedures, frameworks and models apply across RBS Group. Therefore, for the most part, discussion on these qualitative aspects reflects those in RBS Group as relevant for the businesses and operations in NWM Group.

Risk management framework

Introduction

NWM Group operates under RBS Group's integrated risk management framework, which is centred around the embedding of a strong risk culture. The framework ensures the tools and capability are in place to facilitate risk management and decision-making across the organisation.

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

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

The methodology for setting, governing and embedding risk appetite is being further enhanced with the aim of revising current risk appetite processes and increasing alignment with strategic planning and external threat assessments.

During 2019, a number of enhancements to the RBS Group risk management framework were developed. The increasing significance of climate risk was considered as part of these developments and will be fully integrated as part of the implementation of the enhanced framework in 2020.

Risk culture

Risk culture is at the centre of both the risk management framework and risk management practice. The RBS Group's 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. Colleagues are expected to:

- Take personal responsibility for understanding and proactively managing the risks associated with individual roles.
- Respect risk management and the part it plays in daily work.
- Understand the risks associated with individual roles.
- Align decision-making to the RBS Group's risk appetite.
- Consider risk in all actions and decisions.
- Escalate risks and issues early; taking action to mitigate risks and learning from mistakes and near-misses.
- Challenge others' attitudes, ideas and actions.
- Report and communicate risks transparently.

The target risk culture behaviours are embedded in Our Standards and are clearly aligned to the core values of "serving customers", "working together", "doing the right thing" and "thinking long term". These act as an effective basis for a strong risk culture because Our Standards are used for performance management, recruitment and development.

The Conduct & Culture Committee is the decision-making forum for matters related to risk culture within NWM Group.

Training

A wide range of learning, both technical and behavioural, is offered across the risk disciplines. This training can be mandatory, role-specific or for personal development and enables colleagues to develop the capabilities and confidence to manage risk effectively.

Code of Conduct

The RBS Group's Code of Conduct provides guidance 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.

If conduct falls short of the RBS Group's required standards, the accountability review process is used to assess how this should be reflected in pay outcomes for those individuals concerned. The RBS Group-wide remuneration policy ensures that the remuneration arrangements for all employees reflect the principles and standards prescribed by the PRA rulebook and the FCA handbook. 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.

Capital and risk management

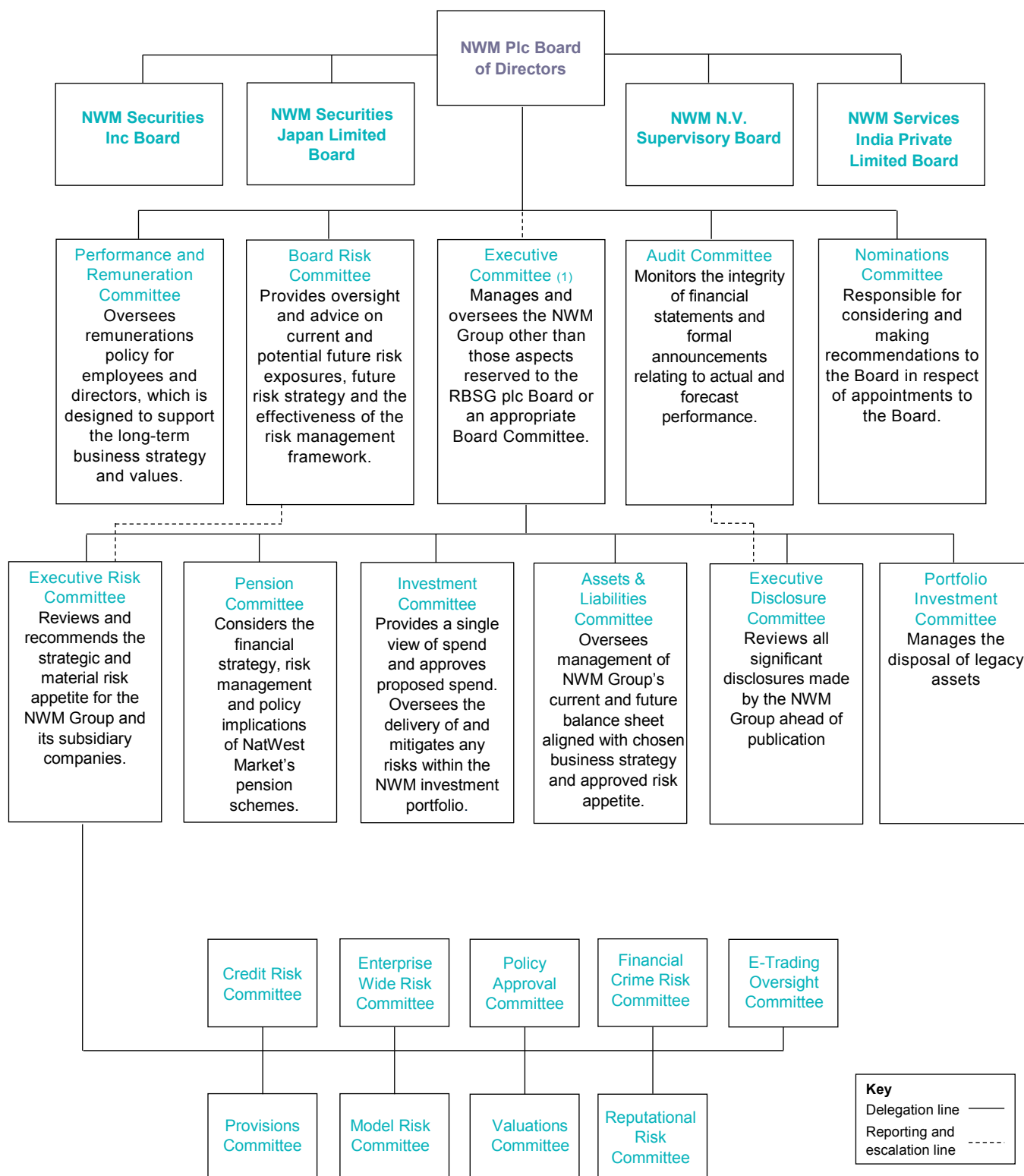
Risk management framework [continued](#)

Risk governance

Committee structure

NWM Group consists of NWM Plc and its subsidiaries which operate as a global business across a number of regions including Europe, US, Asia Pacific and India.

The diagram illustrates NWM Plc's risk committee structure in 2019 and the main purposes of each committee.



Notes:

- (1) The Executive Committee ceased to be a Board committee in September 2019, when it became accountable to the NWM Chief Executive Officer, supporting him in discharging his responsibilities.
- (2) The Conduct & Culture Committee is not shown above as it is not part of NWM Group's corporate governance - it derives its authority from its members. The committee defines and agrees a plan to agree desired Risk Culture for NWM Group, oversees and sponsors the risk culture delivery plan and reviews the Risk Culture assessment output. It also agrees the NWM Group Conduct Risk and Risk Culture strategic direction as well as considering and debating business plans, initiatives and strategic decisions and how they impact on Conduct and Culture.

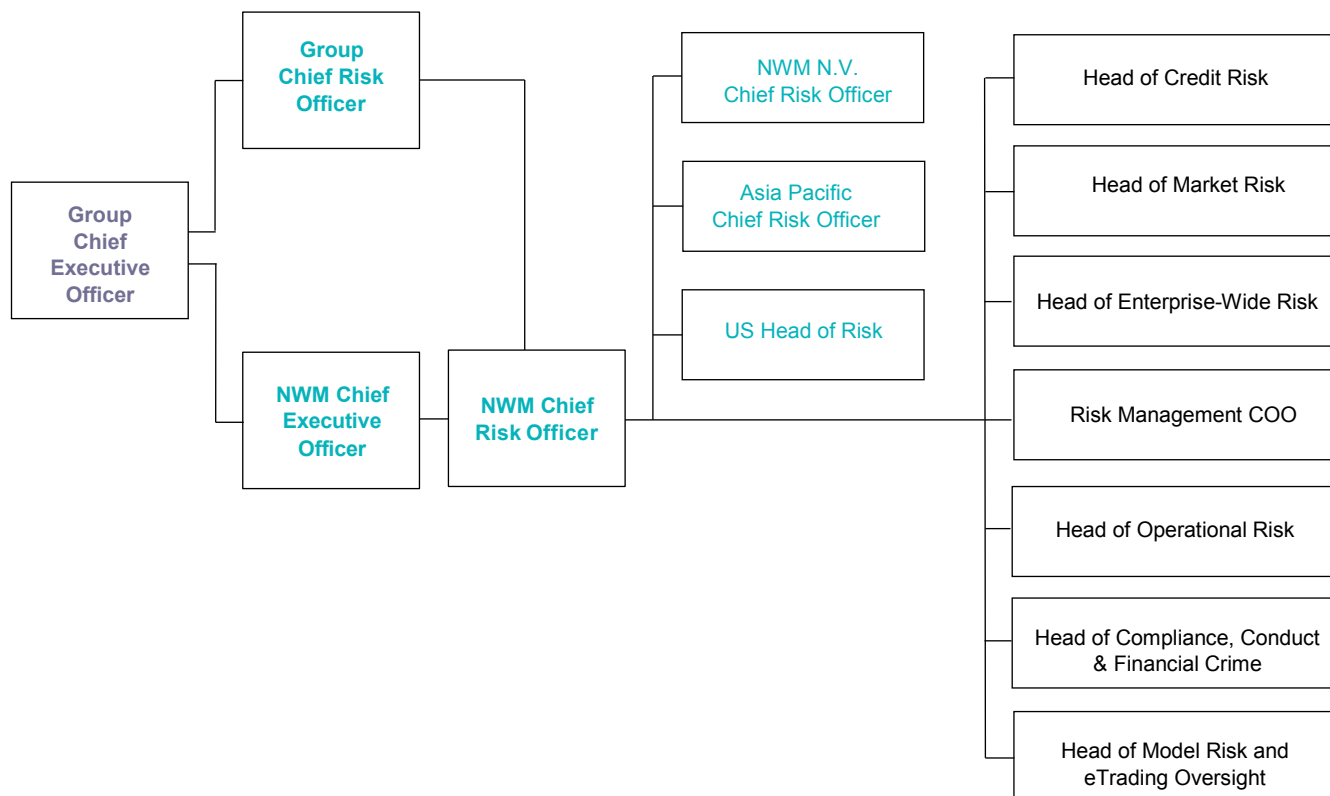
Capital and risk management

Risk management framework [continued](#)

Risk governance

Risk management structure

The diagram illustrates NWM Group's risk management structure in 2019 and key risk management responsibilities.



Notes:

- (1) The NWM Chief Risk Officer reports directly to the NWM Chief Executive Officer and the Group Chief Risk Officer (RBS Group). The NWM Chief Risk Officer also has an additional reporting line to the chair of the NWM Board Risk Committee, and a right of access to the committee.
- (2) The NWM Group Risk function is independent and provides oversight of risk management activities to ensure risks are adequately monitored and controlled. The heads of risk work closely with the NWM Chief Risk Officer, the US Head of Risk and the Chief Risk Officer Asia Pacific to ensure consistency across the international businesses.
- (3) The NWH Risk function provides risk management services across the RBS Group, including – where agreed – to the NWM Chief Risk Officer. These services are managed, as applicable, through service level agreements.

Capital and risk management

Risk management framework [continued](#)

Three lines of defence

RBS Group uses the industry-standard three lines of defence model to articulate accountabilities and responsibilities for managing risk. It supports the embedding of effective risk management throughout the organisation. All roles below the CEO sit within one of these three lines. The CEO ensures the efficient use of resources and the effective management of risks as stipulated in the risk management framework and is therefore considered to be outside the three lines of defence principles.

First line of defence

The first line of defence incorporates most roles, including those in the customer-facing franchises, Technology and Services as well as support functions such as Human Resources, Legal and Finance.

- 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 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, HR and Technology, it is also responsible for managing its consequential risks by identifying, assessing, mitigating, monitoring and reporting risks.

Second line of defence

The second line of defence is 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 the 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 and measures set by the Board.

Third line of defence

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 RBS Group Board, its subsidiary legal entity boards 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 RBS Group and its subsidiary companies achieving their objectives.
- The third line of defence executes its duties freely and objectively in accordance with the Institute of Internal Auditor's Code of Ethics & Standards.

Risk appetite

Risk appetite defines the level and types of risk NWM Group is willing to accept, within risk capacity, in order to achieve strategic objectives and business plans. It links the goals and priorities to risk management in a way that guides and empowers staff to serve customers well and achieve financial targets.

Strategic risks are those that threaten the safety and soundness of NWM Group and its ability to achieve strategic objectives. For certain strategic risks, risk capacity defines the maximum level of risk NWM Group can assume before breaching constraints determined by regulatory capital, leverage and liquidity requirements, the operational environment, and from a conduct perspective. Articulating risk capacity helps determine where risk appetite should be set, ensuring there is a buffer between internal risk appetite and NWM Group's ultimate capacity to absorb losses.

Risk appetite framework

The risk appetite framework bolsters 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 would 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 as a strong control environment for risk appetite.
- Assessing the level of embedding of risk appetite across the organisation.

RBS Group Board approves the risk appetite framework annually.

Establishing risk appetite

In line with RBS Group's risk appetite framework, risk appetite is communicated across NWM Group through risk appetite statements. The risk appetite statements provide clarity on the scale and type of activities that can be undertaken in a manner that is easily conveyed to staff.

Risk appetite statements consist of qualitative statements of appetite supported by risk limits and triggers that operate as a defence against excessive risk-taking. They are established at RBS Group-wide level for all strategic risks and material risks, and at legal entity, business, and function level for all other risks.

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

NWM Group Board sets risk appetite for the most material risks to help ensure NWM Group is well placed to meet its priorities and long-term targets even under challenging economic environments. It is the basis on which NWM Group remains safe and sound while implementing its strategic business objectives.

In addition to following RBS Group risk appetite, NWM Group sets risk appetite limits for its own most material risks. NWM Group's risk profile is frequently reviewed and monitored and management focus is concentrated on all strategic risks, material risks and emerging risk issues. Risk profile relative to risk appetite is reported regularly to NWM Group Board and senior management.

Risk controls and limits

Risk controls 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 material risk types is set in alignment with business activities.

NWM Group policies directly support the qualitative aspects of risk appetite. They ensure that appropriate controls are set and monitored.

Risk identification and measurement

Risk 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.

Capital and risk management

Risk management framework [continued](#)

- 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 RBS Group faces each day are detailed in the Risk Directory. This provides a common risk language to ensure consistent terminology is used by NWM Group and the rest of RBS Group. The Risk Directory is subject to annual review. This ensures that it continues to provide a comprehensive and meaningful list of the inherent risks within the businesses.

Risk treatment and mitigation

Risk treatment and mitigation is an important aspect of ensuring that risk profile remains within risk appetite. Risk mitigation strategies are discussed and agreed with the businesses.

When evaluating possible strategies, costs and benefits, residual risks (risks that are retained) and secondary risks (those that are due to risk mitigation actions) are 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. Significant and emerging risks that could affect future results and performance are reviewed and monitored. Action is taken to mitigate potential risks as and when required. Further in-depth analysis, including the stress testing of exposures relative to the risk, is also carried out.

Stress testing

Stress testing – capital management

Stress testing is a key risk management tool and a fundamental component of RBS'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 NWM 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 NWM-specific 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. • Impact assessment captures input from across NWM Group.
Calculate results and assess implications	• Aggregate impacts into overall results. • Results form part of risk management process. • Scenario results are used to inform NWM Group's business and capital plans.
Develop and agree management actions	• Scenario results are analysed by subject matter experts and appropriate management actions are then developed. • Scenario results and management actions are reviewed and agreed by senior management through senior committees including the Executive Risk Committee, the Board Risk Committee and the Board.

Stress testing is widely used across the RBS Group, including at NWM Group level. The diagram below summarises areas of focus:



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 identification** – by better understanding the risks that could potentially affect NWM'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 NWM 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. They are linked to economic variables and impairments and seek to demonstrate that NWM Group and its operating subsidiaries maintain sufficient CET1 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.

Capital and risk management

Risk management framework [continued](#)

The examination of capital requirements under normal economic and adverse market conditions enables NWM Group to determine whether its projected business performance meets internal 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 NWM Group but also by the regulators to set specific capital buffers. NWM Group takes part in stress tests run by regulatory authorities to test industry-wide vulnerabilities under crystallising global and domestic systemic risks. In 2019, the RBS Group took part in the Bank of England stress test exercise. Details are set out in the RBS Group 2019 Annual Report and Accounts.

Under stress testing, the peak-to-trough change in CET1 may be affected by the transitions from Stage 1 to Stage 2 in stress conditions. Stress and peak-to-trough movements are used to help assess the amount of CET1 capital NWM Group needs to hold in stress conditions in accordance with the capital risk appetite framework.

[Internal assessment of capital adequacy](#)

An internal assessment of material risks is carried out annually 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 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 ICAAP is approved by the Board and submitted to the PRA.

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

[Capital allocation](#)

NWM Group has mechanisms to allocate capital across its businesses. These aim to optimise the use of capital resources taking into account applicable regulatory requirements; strategic and business objectives; and risk appetite. The framework for allocating capital is approved by the Assets & Liabilities Committee.

[Governance](#)

Capital management is subject to substantial review and governance. The Board approves 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.

[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 at significant legal entity and business levels daily, with performance reported to the Assets & Liabilities Committee at least monthly. 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, NWM Group maintains the Individual Liquidity Adequacy Assessment Process. This includes assessment of net stressed liquidity outflows under a range of extreme but plausible stress scenarios detailed in the table below.

Type	Description
Idiosyncratic scenario	The market perceives NWM 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. NWM 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.

NWM Group uses the most severe combination of these 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 NWM Group recovery plan explains how NWM and its subsidiaries – as a consolidated group – would identify and respond to a financial stress event and restore its financial position so that it remains viable on an ongoing basis.

The recovery plan ensures risks that could delay the implementation of a recovery strategy are highlighted and preparations are made to manage 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.

The plan is intended to enable NWM Group to maintain critical services and products it provides to its customers, maintain its core business lines and operate within risk appetite while restoring the bank'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 PRA each year.

Fire drill simulations of possible recovery events are used to test the effectiveness of the NWM Group's recovery plans. The fire drills are designed to replicate possible financial stress conditions and allow senior management to rehearse the responses and decisions that may be required in an actual stress. The results and lessons learnt from the fire drills are used to enhance approaches to recovery planning.

Under the resolution assessment part of the PRA rulebook, the NWM Group is required to carry out an assessment of its preparations for resolution, submit a report of the assessment to the PRA and publish a summary of this report.

Resolution would be implemented if NWM Group was assessed by the UK authorities to have failed and the appropriate regulator put it into resolution. The process of resolution is owned and implemented by the Bank of England (as the UK resolution authority). A multi-year programme is in place to further develop resolution capability in line with regulatory requirements.

Capital and risk management

Risk management framework [continued](#)

[Stress testing – market risk](#)

[Non-traded market risk](#)

Non-traded exposures are reported to the PRA on a quarterly basis as part of the Stress Testing Data Framework. This provides the regulator with an overview of NWM Group's banking book interest rate exposure. The report includes detailed product information analysed by interest rate driver and other characteristics – including accounting classification, currency and counterparty type.

Scenario analysis based on hypothetical adverse scenarios is performed on non-traded exposures as part of the Bank of England and European Banking Authority stress exercises. NWM Group also produces an internal scenario analysis as part of its financial planning cycles.

Non-traded exposures are capitalised through the ICAAP. It covers gap risk, basis risk, credit spread risk, pipeline risk, structural foreign exchange risk, prepayment 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 99% confidence level. Methodologies are independently reviewed and the results are approved by the RBS Group Capital Management & Stress Testing Committee.

[Traded market risk](#)

NWM Group carries out daily market risk stress testing to identify vulnerabilities and potential losses in excess of, or not captured in, value-at-risk. The calculated stresses measure the impact of changes

in risk factors on the fair values of the trading and fair value through other comprehensive income portfolios.

NWM Group conducts historical, macroeconomic and vulnerability-based stress testing. Historical stress testing is a measure that is used for internal management. Using the historical simulation framework employed for value-at-risk, the current portfolio is stressed using historical data since 1 January 2005. This methodology simulates the impact of the 99.9 percentile loss that would be incurred by historical risk factor movements over the period, assuming variable holding periods specific to the risk factors and the businesses.

Historical stress tests form part of the market risk limit framework and their results are reported daily to senior management. Macroeconomic stress tests are carried out periodically as part of the bank-wide, cross-risk capital planning process. The scenario narratives are translated into risk factor shocks using historical events and insights by economists, risk managers and the first line.

Market risk stress results are combined with those for other risks into the capital plan presented to the Board. The cross-risk capital planning process is conducted once a year, with a planning horizon of five years. The scenario narratives cover both regulatory scenarios and macroeconomic scenarios.

Vulnerability-based stress testing begins with the analysis of a portfolio and expresses its key vulnerabilities in terms of plausible, vulnerability scenarios under which the portfolio would suffer material losses. These scenarios can be historical, macroeconomic or forward-looking/hypothetical. Vulnerability-based stress testing is used for internal management information and is not subject to limits. The results for relevant scenarios are reported to senior management.

Capital and risk management

Capital, liquidity and funding risk

Definitions (audited)

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 are set by applicable regulations to determine capital eligibility.

Capital adequacy risk is the risk that there is or will be insufficient capital and loss absorbing debt instruments to operate effectively including meeting minimum regulatory requirements for capital, leverage and MREL, operating within Board approved NWM Group risk appetite and supporting strategic goals.

Liquidity consists of assets that can be readily converted to cash within a short timeframe and with a reliable value. Liquidity risk is the risk of being unable to meet financial obligations as and when they fall due.

Funding consists of on-balance sheet liabilities that are used to provide cash to finance assets. 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;
- Credit ratings;
- Wholesale market conditions; and
- Depositor and investor behaviour.

Sources (audited)

Capital

The eligibility of instruments and financial resources as regulatory capital is laid down by applicable regulation. Capital is categorised by applicable regulation under two tiers (Tier 1 and Tier 2) according to the ability to absorb losses on either a going or gone concern basis, degree of permanency and the ranking of loss absorption. There are three broad categories of capital across these two tiers:

- CET1 capital - 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.
- Additional Tier 1 (AT1) capital - This is the second type of loss absorbing capital and must be capable of absorbing losses on a going concern basis. These instruments are perpetual in nature, with an initial call period of at least five years from issue, and are written off or converted into CET1 capital if a pre-specified CET1 ratio is reached. The sum of CET1 and AT1 capital is referred to as Tier 1 capital.
- Tier 2 capital - Tier 2 capital is the bank entities' supplementary capital and provides loss absorption on a gone concern basis. Gone concern refers to the situation in which resources must be available to enable an orderly resolution, in the event that the Bank of England (BoE) deems that NWM Plc has failed. Tier 2 capital absorbs losses after Tier 1 capital. It typically consists of subordinated debt securities with a minimum initial maturity of five years.

Minimum requirement for own funds and eligible liabilities (MREL)

In addition to capital, other specific loss absorbing instruments, including senior notes with a residual maturity of at least one year issued by NWM Plc, may be used to cover certain gone concern capital requirements.

Liquidity

NWM Group maintains a prudent approach to the definition of liquidity resources. Liquidity resources are divided into primary and secondary liquidity as follows:

- Primary liquid assets include cash and balances at central banks, Treasury bills and other high-quality government and US agency bonds.

- Secondary liquid assets are eligible as collateral for local central bank liquidity facilities. These assets may include lower-quality bonds and eligible loans that are retained on balance sheet and pre-positioned with a central bank so that they may be converted into additional sources of liquidity at very short notice.

Funding

NWM Group's primary funding sources are as follows:

Type	Description
Wholesale markets	Includes: • Short-term (less than 1 year) unsecured money market funding; • Commercial paper and certificates of deposit; • Secured repo market funding.
Term debt	Includes: • Issuance of long-term (typically more than 1 year) senior unsecured and secured debt securities. • Issuance of long-term subordinated liabilities.
Internal capital and MREL	Includes: • Equity, AT1, Tier 2 capital instruments and MREL issued to RBSG plc (under the Single Point of Entry regime).



Managing capital, liquidity and funding requirements: regulated entities

In line with paragraph 135 of IAS 1 'Presentation of Financial Statements', NWM Group manages capital having regard to regulatory requirements. Regulatory capital is monitored and reported on an individual regulated bank legal entity basis ('bank entity'), which is the CRR transitional basis as relevant in the jurisdiction for significant subsidiaries of RBS Group.

Liquidity metrics including the LCR and Stressed Outflow Coverage are presented for the solo legal entity (the Bank) in line with how it is regulated by the PRA. Funding sources and Notes issued disclosures are presented for NWM Group rather than for NatWest Markets Plc.

Key developments in 2019

- During 2019, NWM Plc paid ordinary dividends totalling £500 million to its parent company, RBSG plc.
- NWM Plc's CET1 ratio increased by 170 basis points to 17.3% at 31 December 2019, from 15.6% at 31 December 2018. The increase in the CET1 ratio at year end 2019 was primarily due to lower RWAs, as reductions in counterparty credit risk, market risk and operational risk were partially offset by credit risk increases. Offsetting these RWA drivers were dividends paid and other reserves movements in the year, including the impact of the decline in market value of the SABB holding, which is recognised directly in equity.
- NWM Plc's RWAs decreased by £5.6 billion to £35.2 billion at 31 December 2019, primarily related to a reduction in market, counterparty credit and operational risk RWAs, offset by increased credit risk RWAs following the acquisition of the SABB shareholding. The lower market risk RWAs were largely due to a reduction in the capital multiplier, changes in interest rate and foreign exchange risk lowering the VaR/SVaR based requirements, and reductions due to model updates. The capital multiplier also contributed to a decrease in CVA within counterparty credit risk, with additional reductions due to decreased exposures and the impact of foreign exchange. Operational risk RWAs were lower following the annual recalculation.
- CRR leverage exposure for NWM Plc decreased to £136.5 billion compared with £148.5 billion at 31 December 2018.

Capital and risk management

Capital, liquidity and funding risk *continued*

- The leverage ratio on a CRR basis, using PRA transitional capital, increased to 5.1% following the decrease in leverage exposure offset by lower Tier 1 capital.
- NWM Plc's MREL at 31 December 2019 was £13.5 billion, or 38.4% of RWAs (2018 - £13.9 billion and 34.0% respectively).
- The NWM Plc liquidity portfolio was £16.1 billion at 31 December 2019, a decrease of £0.5 billion from £16.6 billion at the prior year end.
- The LCR for NWM Plc was 254% at 31 December 2019, compared with 457% at year end 2018.
- During 2019, NWM Plc issued £5.0 billion of term senior unsecured debt securities, across benchmark and private placement formats, in line with its funding target.
- During 2019, NWM Group established a 144a MTN programme for US investors, and accessed new currency markets (including Swedish kronor, Swiss franc and Japanese yen).
- NWM Group also maintains a portfolio of bi-lateral borrowing in different formats, including unsecured loans and notes or loans secured primarily by banking book collateral.

Capital management

Capital management is the process by which banks ensure that they have sufficient capital and other loss absorbing instruments to operate effectively. This includes meeting minimum regulatory requirements, operating within Board-approved risk appetite, maintaining credit ratings and supporting strategic goals. Capital management is critical in supporting banks businesses. Capital management within NWM Group is executed in accordance with the RBS Group-wide framework.

NWM Plc's capital plans are produced and updated by the bank on a monthly basis. This process includes integration into RBS Group's wider annual budgeting process and is summarised below. Other elements of capital management, including risk appetite and stress testing, are set out on pages 25 and 26.

Produce capital plans	• A capital plan is produced for NWM Plc using a five year planning horizon under expected and stress conditions. Stressed capital plans are produced to support internal stress testing through the ICAAP or for regulatory purposes. • A shorter term (rolling 12 month) forecast is updated frequently in response to actual performance, changes in internal and external business environment and to manage risks and opportunities.
Assess capital adequacy	• Capital plans are developed to ensure that capital of sufficient quantity and quality is planned to be available to support NWM Group's business and strategic plans over the planning horizon within approved risk appetite, as determined via stress testing, and minimum regulatory requirements. • Impact assessment captures input from across NWM Group including from businesses.
Inform capital actions	• Capital planning informs potential capital actions including managing capital through new issuance, redemptions or internal transactions. • Decisions on capital actions will be influenced by strategic and regulatory requirements, the cost and prevailing market conditions. • As part of capital planning, NWM Group will monitor its portfolio of capital securities and assess the optimal blend.

Capital planning is one of the tools that NWM Group uses to monitor and manage capital adequacy risk on a going and gone concern basis, including the risk of excessive leverage.

Liquidity and funding management

Liquidity and funding management follows a similar process to that outlined above for capital.

Liquidity portfolio management

The size of the portfolio is determined by reference to NWM Group's liquidity risk appetite. NWM Group, consistent with that of RBS Group, retains a prudent approach to setting the composition of the liquidity portfolio, which is subject to internal policies and limits over quality of counterparty, maturity mix and currency mix. NWM Group categorises its liquidity portfolio, including its locally managed liquidity portfolios, into primary and secondary liquid assets. The majority of the NWM Plc portfolio is managed by NatWest Markets Treasury, for which the NatWest Markets Treasurer is responsible.

NatWest Markets Securities Inc. and NatWest Markets N.V., both of which are significant operating subsidiaries of NWM Plc, hold locally managed liquidity portfolios to comply with local regulations that may differ from PRA rules.

The liquidity value of the portfolio is determined by taking current market prices and applying a discount or haircut, to give a liquidity value that represents the amount of cash that can be generated by the asset.

Funding risk management

NWM Group manages funding risk through a comprehensive framework which measures and monitors the funding risk on the balance sheet.

The long term obligations of NWM Group must be met with diverse and stable funding sources, the behavioural maturity of these liabilities must at a minimum equal those of the assets.

Capital and risk management

Capital, liquidity and funding risk *continued*

Minimum requirements

Capital ratios

The Bank entities are subject to minimum capital requirements relative to RWAs. The table below summarises the CRR-end point minimum requirements of capital to RWAs that the UK bank entities are expected to meet.

Type	CET1	Total Tier 1	Total capital
Minimum capital requirements	4.5%	6.0%	8.0%
Capital conservation buffer ⁽¹⁾	2.5%	2.5%	2.5%
Countercyclical capital buffer ⁽¹⁾	0.5%	0.5%	0.5%
Total ⁽²⁾	7.5%	9.0%	11.0%

Notes:

- (1) The institution specific countercyclical capital buffer requirement is based on the weighted average of geographical exposures. The Financial Policy Committee (FPC) sets the UK countercyclical capital buffer, which is currently 1.0% and will rise to 2.0% from 16 December 2020. Foreign exposures may be subject to different countercyclical capital buffer rates dependent on the rate set in those jurisdictions. NWM Plc's main relevant exposures are to the UK (46%), the US (16%) and Saudi Arabia (6%). The capital conservation buffer and the countercyclical capital buffer are required to be met with CET1 capital only.
- (2) In addition, NWM Plc is subject to Pillar 2A requirements which are not disclosed publicly.

Leverage ratio

At present, NWM Plc only has a leverage ratio reporting requirement, but not a legally binding minimum leverage requirement. In June 2019, the European Commission's proposals for a legally binding 3% of Tier 1 capital minimum leverage ratio, previously announced as part of the CRR 2 package of legislation, were published into the EU's Official Journal. The leverage ratio requirement will come into force on 28 June 2021 and will be applicable to individual entities, including NWM Plc. It is expected that UK's rules will remain closely aligned with the EU's following the UK's departure from the EU, and that a minimum leverage ratio will be subject to the same or similar implementation timeframes.

Measurement

Capital, RWAs and leverage

The table below sets out the key capital and leverage ratios.

	2019 £m	2018 £m
Capital ⁽¹⁾		
CET1	6,097	6,369
Tier 1	7,003	7,352
Total	8,501	8,757
RWAs		
Credit risk	9,825	9,234
Counterparty credit risk	11,060	13,285
Market risk	11,229	14,106
Operational risk	3,039	4,152
Total RWAs	35,153	40,777
Capital adequacy ratios	%	%
CET1	17.3	15.6
Tier 1	19.9	18.0
Total	24.2	21.5
Leverage		
Tier 1 capital (£m)	7,003	7,352
CRR leverage exposure (£m)	136,505	148,502
CRR leverage ratio (%)	5.1	5.0

Note:

- (1) CRR as implemented by the PRA in the UK, with effect from 1 January 2014.

From 1 January 2015, UK banks have been required to meet their Pillar 2A capital requirement with at least 56% in CET1 capital and no more than 44% in AT1 capital and no more than 25% in Tier 2 capital. The Pillar 2A capital requirement is the capital that NWM Plc must hold, in addition to meeting its Pillar 1 requirements in order to comply with the PRA's overall financial adequacy rule.

Capital and risk management

Capital, liquidity and funding risk continued

Capital resources (audited)

Under Capital Requirements Regulation (CRR), regulators within the European Union monitor capital on a legal entity basis, with local transitional arrangements on the phasing in of end-point CRR. The capital resources based on the PRA transitional basis for NWM Plc are set out below.

	2019 £m	2018 £m
Shareholders' equity (excluding non-controlling interests)		
Shareholders' equity	9,631	8,922
Other equity instruments	(904)	(749)
	8,727	8,173
Regulatory adjustments and deductions		
Own credit	(39)	(223)
Defined benefit pension fund adjustment	(171)	(197)
Cash flow hedging reserve	(137)	(114)
Prudential valuation adjustments	(373)	(450)
Expected losses less impairments	(10)	(351)
Instruments of financial sector entities where the institution has a significant and non-significant investment	(1,900)	(445)
Other regulatory adjustments	—	(24)
	(2,630)	(1,804)
CET1 capital	6,097	6,369
Additional Tier 1 (AT1) capital		
Qualifying instruments and related share premium	904	749
Qualifying instruments and related share premium subject to phase out	226	234
	1,130	983
Tier 1 deductions		
Instruments of financial sector entities where the institution has a significant investment	(224)	—
Tier 1 capital	7,003	7,352
Qualifying Tier 2 capital		
Qualifying instruments and related share premium	1,967	2,098
Tier 2 deductions		
Instruments of financial sector entities where the institution has a significant and non-significant investment	(469)	(693)
Tier 2 capital	1,498	1,405
Total regulatory capital	8,501	8,757

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Leverage exposure

The leverage exposure is based on the CRR Delegated Act.

	2019 £m	2018 £m
Leverage		
Cash and balances at central banks	9,953	11,095
Trading assets	57,768	61,990
Derivatives	147,458	134,291
Net loans to customers	25,929	16,588
Other assets	6,945	18,077
Total assets	248,053	242,041
Derivatives		
- netting	(155,147)	(140,796)
- potential future exposures	39,997	41,663
Securities financing transactions gross up	1,559	1,800
Undrawn commitments	5,986	7,306
Regulatory deductions and other adjustments	(2,815)	(1,557)
Exclusion of core UK-group exposures	(1,128)	(1,955)
Leverage exposure	136,505	148,502

Capital and risk management

Capital, liquidity and funding risk *continued*

Liquidity portfolio

The table below shows the liquidity portfolio by LCR product, with the incorporation of discounts (or haircuts) used within the internal stressed outflow coverage. Secondary liquidity comprises assets eligible for discount at central banks, which do not form part of the liquid asset portfolio for LCR or stressed outflow coverage purposes.

	Liquidity value (1)	
	2019	2018
	£m	£m
NatWest Markets Plc		
Cash and balances at central banks	9,929	11,058
AAA to AA- rated governments	4,399	3,597
A+ and lower rated governments (2)	1,277	1,587
Government guaranteed issuers, Public sector entities and Government sponsored entities	—	—
International Organisations and Multilateral development banks	244	4
LCR level 1 bonds	5,920	5,188
LCR level 1 Assets	15,849	16,246
LCR level 2 Assets	—	—
Non-LCR Eligible Assets	5	—
Primary liquidity	15,854	16,246
Secondary liquidity (3)	244	344
Total liquidity value	16,098	16,590

The table below shows the liquidity value of the liquidity portfolio by currency.

Total liquidity portfolio	GBP £m	USD £m	EUR £m	Other £m	Total £m
2019	6,142	3,628	5,051	1,277	16,098
2018	3,929	3,219	7,855	1,587	16,590

Notes:

- (1) Liquidity value was aligned to the internal stressed outflow coverage, which is stated after discounts (or haircuts) are applied to the instruments, at 31 December 2019. The liquidity values for 2018 have been re-presented.
- (2) The split between ratings bands has been restated for 2018.
- (3) Comprises assets eligible for discounting at the Bank of England and other central banks.

Capital and risk management

Capital, liquidity and funding risk continued

Funding sources (audited)

The table below shows NWM Group's carrying values of the principal funding sources based on contractual maturity.

	2019			2018		
	Short-term less than 1 year £m	Long-term more than 1 year £m	Total £m	Short-term less than 1 year £m	Long-term more than 1 year £m	Total £m
Bank deposits	1,302	787	2,089	2,749	—	2,749
<i>of which: repos (amortised cost)</i>	380	—	380	424	—	424
Customer deposits	3,176	527	3,703	2,549	31	2,580
Trading liabilities (1)						
Repos (2)	27,885	—	27,885	25,645	—	25,645
Derivative cash collateral received	21,506	—	21,506	20,129	—	20,129
Other bank and customer deposits	600	896	1,496	1,340	446	1,786
Debt securities in issue	659	1,103	1,762	56	847	903
	50,650	1,999	52,649	47,170	1,293	48,463
Other financial liabilities						
Debt securities in issue						
commercial paper and certificates of deposits	2,699	6	2,705	2,826	—	2,826
medium term notes (MTNs)	4,386	10,218	14,604	3,543	9,252	12,795
Subordinated liabilities	107	1,029	1,136	—	658	658
	7,192	11,253	18,445	6,369	9,910	16,279
Amounts due to holding company and fellow subsidiaries (3)						
CRR-compliant internal MREL	—	5,120	5,120	—	5,125	5,125
Other bank and customer deposits	951	38	989	2,715	100	2,815
Subordinated liabilities	—	2,020	2,020	9	1,953	1,962
	951	7,178	8,129	2,724	7,178	9,902
Total funding	63,271	21,744	85,015	61,561	18,412	79,973
<i>Of which: available in resolution (4)</i>	<i>107</i>	<i>8,169</i>	<i>8,276</i>	<i>6</i>	<i>7,736</i>	<i>7,742</i>

Notes:

- (1) Funding sources excludes short positions of £21,187 million (2018 - £23,827 million) reflected as trading liabilities on the balance sheet.
- (2) Comprised Central and other bank repos of £6,636 million (2018 - £4,997 million), other financial institution repos of £18,998 million (2018 - £20,083 million) and other corporate repos of £2,251 million (2018 - £565 million).
- (3) Amount due to holding company and fellow subsidiaries relating to non-financial instruments of £171 million (2018 - £259 million) have been excluded from the table.
- (4) Eligible liabilities (as defined in the Banking Act 2009 as amended from time to time) that meet the eligibility criteria set out in the regulations, rules, policies, guidelines, or statements of the Bank of England including the Statement of Policy published in June 2018.



Capital and risk management

Capital, liquidity and funding risk *continued*

Senior notes and subordinated liabilities - residual maturity profile by instrument type (audited)

The table below shows NWM Group's debt securities in issue, subordinated liabilities and internal resolution instruments by residual maturity.

	Trading liabilities		Other financial liabilities				Amounts due to holding company and fellow subsidiaries			
	Debt securities in issue		Debt securities in issue							
	MTNs	Total	Commercial paper and CDs	MTNs	Subordinated liabilities	Total	CRR-compliant internal MREL	Subordinated liabilities	Total notes in issue	
	£m	£m	£m	£m	£m	£m	£m	£m	£m	
2019										
Less than 1 year	659	659	2,699	4,386	107	7,192	—	—	7,851	
1-3 years	321	321	3	6,885	273	7,161	2,129	—	9,611	
3-5 years	217	217	3	2,545	252	2,800	2,991	1,143	7,151	
More than 5 years	565	565	—	788	504	1,292	—	877	2,734	
Total	1,762	1,762	2,705	14,604	1,136	18,445	5,120	2,020	27,347	
2018										
Less than 1 year	56	56	2,826	3,543	—	6,369	—	9	6,434	
1-3 years	374	374	—	6,395	99	6,494	—	—	6,868	
3-5 years	92	92	—	1,932	425	2,357	5,125	328	7,902	
More than 5 years	381	381	—	925	134	1,059	—	1,625	3,065	
Total	903	903	2,826	12,795	658	16,279	5,125	1,962	24,269	

The table below shows the currency breakdown of total notes in issue.

	GBP £m	USD £m	EUR £m	Other £m	Total £m
2019					
Commercial paper and CDs	1,613	—	1,053	39	2,705
MTNs	233	2,748	11,181	2,204	16,366
External subordinated liabilities	98	316	722	—	1,136
CRR-compliant internal MREL due to RBSG plc	—	3,289	1,831	—	5,120
Subordinated liabilities due to RBSG plc	—	1,183	837	—	2,020
Total	1,944	7,536	15,624	2,243	27,347
2018 Total	2,174	5,761	14,959	1,375	24,269



Capital and risk management

Market risk (audited)

NWM Group is exposed to traded market risk through its trading activities and to non-traded market risk through its banking activities. Traded and non-traded market risk exposures are managed and discussed separately. The traded market risk section begins below. The non-traded market risk section begins on page 39.

Pension-related activities also give rise to market risk. Refer to page 59 for more information on risk related to pensions.

Traded market risk

Definition (audited)

Traded market risk is the risk arising from changes in fair value on positions, assets, liabilities or commitments in trading portfolios as a result of fluctuations in market prices.

Sources of risk (audited)

Traded market risk mainly arises from NWM Group's trading activities. These activities provide a range of financing, risk management and investment services to clients – including corporations and financial institutions – around the world. From a market risk perspective, activities are focused on rates; currencies; securitised products; and traded credit.

NWM Group undertakes transactions in financial instruments including debt securities, as well as securities financing and derivatives.

The key categories of traded market risk are interest rate risk, credit spread risk and foreign currency price risk.

Trading activities may also give rise to counterparty credit risk. For further detail, refer to the Credit risk section.

Key developments in 2019

- Geopolitical risk resulted in periods of market volatility during the year as a result of increased political and economic risks and uncertainty in the UK and global markets. Despite this volatility, traded VaR remained well within appetite throughout 2019.
- NWM Plc experienced three back-testing exceptions: two in early September and one in October. These were mainly driven by an increase in long-end sterling real rates.
- Following NWM N.V. becoming a subsidiary of NWM Plc in November 2019, all material traded market risk exposure of RBS Group is within NWM Group. At the point of acquisition, there was no significant impact on the consolidated VaR.

Risk governance (audited)

Market risk policy statements set out the governance and risk management framework. Responsibility for identifying, measuring, monitoring and controlling market risk arising from trading activities lies with the relevant trading business. The Market Risk function independently advises on, monitors and challenges the risk-taking activities undertaken by the trading business, to ensure these are within the constraints of the market risk framework, policies, and risk appetite statements and measures.

Risk appetite

NWM Group's qualitative appetite for traded market risk is set out in the traded market risk appetite statement.

Quantitative appetite is expressed in terms of exposure limits.

The limits at NWM Group level comprise VaR and stressed value-at-risk (SVaR). More details on these are provided on the following pages.

For each trading business, a document known as a dealing authority compiles details of all applicable limits and trading restrictions. The desk-level mandates comprise qualitative limits related to the product types within the scope of each desk, as well as quantitative metrics specific to the desk's market risk exposures. These additional limits and metrics aim to control various risk dimensions such as exposure size, aged inventory, currency and tenor.

The limits are reviewed to reflect changes in risk appetite, business plans, portfolio composition and the market and economic environments. The limit review has been enhanced to improve the alignment between traded market risk exposure and capital usage. This is done by analysing the relationship between VaR and SVaR and NWM Plc's solo CET1 ratio.

To ensure approved limits are not breached and that NWM Group remains within its risk appetite, triggers at NWM Group and lower levels have been set such that if exposures exceed a specified level, action plans are developed by the relevant business and the Market Risk function and implemented.

For more detail on risk appetite, refer to page 25.

Risk controls

For information on risk controls, refer to page 25.

Risk monitoring and mitigation

Traded market risk is identified and assessed by gathering, analysing, monitoring and reporting market risk information at desk, business and NWM Group-wide levels. Industry expertise, continued system developments and techniques such as stress testing are also used to enhance the effectiveness of the identification and assessment of all material market risks.

Traded market risk exposures are monitored against limits and analysed daily by market risk reporting and control functions. A daily report summarising the position of exposures against limits at desk, business and NWM Group is provided to senior business and market risk managers.

Limit reporting is supplemented with regulatory capital and stress testing information as well as ad hoc reporting.

A risk review of trading businesses is undertaken weekly with senior risk and front office staff. This includes a review of profit and loss drivers, notable position concentrations and other positions of concern.

Capital and risk management

Traded market risk *continued*

Business profit and loss performance is monitored automatically through loss triggers which, if breached, require a remedial action plan to be agreed between the Market Risk function and the business. The loss triggers are set using both a fall-from-peak approach and an absolute loss level. In addition, regular updates on traded market risk positions are provided to NWM Group's Executive Risk Committee and Board Risk Committee.

Risk measurement *(audited)*

NWM Group uses VaR, SVaR and the incremental risk charge to measure traded market risk. Risks that are not adequately captured by VaR or SVaR are captured by the risks not in VaR (RNIV) framework to ensure that NWM Group is adequately capitalised for market risk. In addition, stress testing is used to identify any vulnerabilities and potential losses.

The key inputs into these measurement methods are market data and risk factor sensitivities. Sensitivities refer to the changes in trade or portfolio value that result from small changes in market parameters that are subject to the market risk limit framework. Revaluation ladders are used in place of sensitivities to capture the impact of large moves in risk factors or the joint impact of two risk factors.

These methods have been designed to capture correlation effects and allow NWM Group to form an aggregated view of its traded market risk across risk types, markets and business lines while also taking into account the characteristics of each risk type.

One-day 99% traded internal VaR *(audited)*

The table below shows one-day 99% internal VaR for the trading portfolios of NWM Plc and NWMSI, split by exposure type. For NWM N.V., refer to the appropriate key point below the table.

Following the consolidation of NWM N.V. in November 2019, the traded market risk exposure of NWM Group is materially equivalent to that of RBS Group. For RBS Group traded VaR disclosures, refer to the Traded market risk section of the RBS Group Annual Report and Accounts.

	2019				2018			
	Average £m	Maximum £m	Minimum £m	Period end £m	Average £m	Maximum £m	Minimum £m	Period end £m
NWM Plc								
Interest rate	9.2	16.3	5.9	10.3	13.9	26.6	8.8	11.4
Credit spread	10.1	13.9	6.7	10.4	10.7	23.5	6.9	7.2
Currency	4.0	10.5	1.6	3.2	3.1	7.7	1.3	5.3
Equity	0.7	2.2	0.3	0.9	0.8	1.6	0.3	0.8
Commodity	0.1	0.6	—	0.1	0.3	0.9	—	0.1
Diversification (1)	(9.9)			(11.2)	(10.5)			(6.3)
Total	14.2	20.1	9.8	13.7	18.2	32.5	11.4	18.4
NWMSI								
Interest rate	2.8	4.9	1.7	2.4	1.9	3.2	1.0	2.3
Credit spread	1.4	2.3	0.2	1.1	0.9	2.5	0.3	1.8
Commodity	0.1	0.5	—	0.1	0.1	0.3	—	—
Diversification (1)	(1.2)			(1.1)	(0.5)			(1.3)
Total	3.1	5.9	2.0	2.5	2.3	3.6	1.2	2.8

Note:

- (1) Entities within NWM Group benefit 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.

Key points *(audited)*

NWM Plc

- Despite market volatility driven by geopolitical risk throughout the year, traded VaR remained well within appetite.
- The decrease in the average VaR compared to 2018 is attributed to peaks in H1 2018 reflecting long euro rates positioning and bond syndication activity.

Value-at-risk

For internal risk management purposes, VaR assumes a time horizon of one trading day and a confidence level of 99%.

The internal VaR model – which captures all trading book positions including those products approved by the regulator – is based on a historical simulation, utilising market data from the previous 500 days on an equally-weighted basis.

The model also captures the potential impact of: interest rate risk; credit spread risk; foreign currency price risk; equity price risk; and commodity price risk.

When simulating potential movements in such risk factors, a combination of absolute, relative and rescaled returns is used.

Testing of the performance and adequacy of the VaR model is done on a regular basis through the following processes:

- Back-testing – Internal and regulatory back-testing is conducted on a daily basis. For further information on back-testing, refer to the following page.
- Ongoing model validation – VaR model performance is assessed both regularly and on an ad-hoc basis if market conditions or portfolio profile change significantly.
- Model Risk Management review – As part of the model lifecycle, all risk models (including the VaR model) are independently reviewed to ensure the model is still fit for purpose given current market conditions and portfolio profile. For further detail on the independent model validation carried out by Model Risk Management, refer to page 62. More information relating to pricing and market risk models is presented in the RBS Group Pillar 3 report.

NWMSI

- The increase in traded VaR on an average basis was mainly driven by the US Rates business.

NWM N.V.

- Period-end VaR was £0.5 million.

Capital and risk management

Traded market risk continued

VaR back-testing

The main approach employed to assess the VaR model's ongoing performance is back-testing, which counts the number of days when a loss exceeds the corresponding daily VaR estimate, measured at a 99% confidence level. Two types of profit and loss (P&L) are used in back-testing comparisons: Actual P&L and Hypothetical (Hypo) P&L. For more details on the back-testing approach and the differences between internal and regulatory VaR, refer to the Market risk section of the RBS Group Pillar 3 report.

The table below shows regulatory back-testing exceptions in NWM Plc for the 250-business-day period to 31 December 2019 for one-day 99% traded regulatory VaR compared with Actual and Hypo P&L.

NWM Plc	Back-testing exceptions	
	Actual	Hypo
	3	3

Key points

- Statistically NWM Group would expect to see back-testing exceptions 1% of the time over a period of 250 business days. A VaR model recording four or fewer exceptions in a continuous 250-day period is regarded as satisfactory. A model recording five or more exceptions is regarded as having potential issues regarding its quality or accuracy.
- NWM Plc reached a maximum of six Actual and seven Hypo back-testing exceptions the 250-day rolling window in early October 2019. By 31 December 2019, this had decreased to three Actual and three Hypo exceptions, after earlier exceptions dropped out of the window during November and December. Of the three exceptions NWM Plc experienced during 2019, two occurred in early September and one in October. These were mainly driven by an increase in long-end sterling real rates.

The table below shows internal back-testing exceptions in the major NWM businesses for the 250-business-day period to 31 December 2019. Internal back-testing compares one-day 99% traded internal VaR with Actual and Hypo P&L.

	Back-testing exceptions	
	Actual	Hypo
Rates	2	4
Currencies	2	6
Credit	—	—

Key points

- Statistically NWM Group would expect to see back-testing exceptions 1% of the time over the 250-day period.
- The exceptions in the Rates business were mainly driven by market moves in sterling and euro rates.
- The exceptions in the Currencies business were mainly driven by volatility in the foreign exchange market, including movements in the euro/sterling and sterling/US dollar exchange rates.

Stressed VaR (SVaR)

As with VaR, the SVaR methodology produces estimates of the potential change in the market value of a portfolio, over a specified time horizon, at a given confidence level. SVaR is a VaR-based measure using historical data from a one-year period of stressed market conditions. A simulation of 99% VaR is run on the current portfolio for each 250-day period from 2005 to the current VaR date, moving forward one day at a time. The SVaR is the worst VaR outcome of the simulated results.

This is in contrast with VaR, which is based on a rolling 500-day historical data set. A time horizon of ten trading days is assumed with a confidence level of 99%. NWM Group's internal traded SVaR model captures all trading book positions.

The table below analyses 10-day 99% internal SVaR for the trading portfolios of NWM Plc and NWMSI.

	Period end 2019 £m	Period end 2018 £m
NWM Plc	89	144
NWMSI	19	32

Key points

- In NWM Plc, period-end traded SVaR decreased compared to 2018, driven by a reduction of SVaR tail risk due to hedging undertaken to address market volatility.
- In NWMSI, the risk profile remained stable throughout the year, with the period-end decrease having no material impact on NWM Group as a whole.
- In NWM N.V., traded SVaR at period-end was £5.8 million.

Capital and risk management

Traded market risk *continued*

Risks not in VaR (RNIVs)

The RNIV framework is used to identify and quantify market risks that are not fully captured by the internal VaR and SVaR models. RNIV calculations form an integral part of ongoing model and data improvement efforts to capture all market risks in scope for model approval in VaR and SVaR. For further qualitative and quantitative disclosures on RNIVs, refer to the Market risk section of the RBS Group Pillar 3 Report.

Stress testing

For information on stress testing, refer to page 26.

Incremental risk charge (IRC)

The IRC model quantifies the impact of rating migration and default events on the market value of instruments with embedded credit risk (in particular, bonds and credit default swaps) held in the trading book. It further captures basis risk between different instruments, maturities and reference entities. For further qualitative and quantitative disclosures on the IRC, refer to the Market risk section of the RBS Group Pillar 3 Report.

Non-traded market risk

Definition *(audited)*

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 *(audited)*

The key sources of non-traded market risk are interest rate risk, credit spread risk, foreign exchange risk and equity risk. Each of these risk types is managed separately. For definitions and qualitative and quantitative information on each of them, see the separate subsections starting on the following page.

Key developments in 2019

- Non-traded market risk is managed separately on both sides of the ring-fence. It continues to be aggregated and monitored against risk appetite at RBS Group level.
- Following ring-fencing implementation, NWM Plc defined its independent risk appetite, governance and control framework in the second line of defence.
- On 16 June 2019, NWM Plc acquired RBS Group's 4.1% economic interest in the newly merged Saudi British Bank (SABB) from NatWest Markets N.V. The non-traded foreign exchange and equity risks arising from this shareholding – with a total VaR of £34 million as at 31 December 2019 – are monitored separately from non-

traded market risk appetite reporting. The funding risk arising from the SABB shareholding is captured as structural interest rate exposure.

- By 31 December 2019, NWM Plc had disposed of 98% of the complex lender-option / borrower-option (LOBO) loans it had inherited as a result of ring-fencing.
- NWM Plc maintains a foreign exchange hedging programme to mitigate the downside risk to its solo CET1 capital ratio from movements in foreign exchange rates. In addition, during 2019, it increased the capitalisation of its US branch, which has reduced the branch's debt funding and NWM Plc's regulatory exposure to fluctuations in the US dollar exchange rate against sterling.
- NWM Plc maintains a structural hedge of non and low interest-bearing liabilities, principally equity. At 31 December 2019, the notional amount of the structural hedge in place was £5.6 billion.

Risk governance *(audited)*

Responsibility for identifying, measuring, monitoring and controlling market risk arising from non-trading activities lies with the relevant business. Oversight is provided by NWM Group's Market Risk function.

Risk positions are reported monthly to NWM Group's Executive Risk Committee and quarterly to the Board Risk Committee, as well as to the Assets & Liabilities Committee (ALCo).

Market risk policy statements set out the governance and risk management framework.

Risk appetite

NWM Group's qualitative appetite is set out in the non-traded market risk appetite statement. Quantitative appetite is expressed in terms of exposure limits. The limits at NWM Group level comprise VaR, SVaR, sensitivities, earnings-at-risk, economic-value-of-equity and a stress limit based on the foreign exchange sensitivity of NWM Plc's CET1 ratio.

To ensure limits are not breached and that NWM Group remains within its risk appetite, triggers at NWM Group and lower levels have been set such that if exposures exceed a specified level, action plans are developed by the business, the Market Risk function and Finance and implemented. Limits are reviewed regularly to reflect changes in risk appetite, business plans, portfolio composition and the external environment. For further information on risk appetite, refer to page 25.

Risk controls

For information on risk controls, refer to page 25.

Capital and risk management

Non-traded market risk *continued*

Non-traded internal VaR (one-day 99%) (audited)

The market risk exposures arising as a result of banking activities are measured using a combination of value-based metrics (VaR and sensitivities) and earnings-based metrics. The following table shows NWM Plc's one-day internal banking book VaR at a 99% confidence level, split by exposure type. For NWM N.V., refer to the appropriate key point below the table. The table excludes the risks arising from the SABB shareholding, which are monitored separately.

	2019 (1)				2018 (2)
	Average £m	Maximum £m	Minimum £m	Period end £m	Period end £m
NWM Plc					
Interest rate	3.5	7.3	1.4	3.7	3.1
Credit spread	5.1	8.3	3.1	3.6	7.7
Foreign exchange rate	17.2	26.9	8.2	8.7	22.7
Equity risk	1.2	3.1	0.9	1.0	4.0
Diversification (3)	(6.6)			(3.5)	(13.6)
Total	20.4	32.2	10.2	13.5	23.9

Notes:

- (1) Following approval by the NWM Board Risk Committee in September 2019, the basis of preparation for non-traded VaR was changed from a NWM Group consolidated basis to a solo legal entity basis. This approach aligns the calculation of reported VaR more closely with that of RBS Group. Non-traded VaR figures for the whole of 2019 are presented on the solo basis of preparation.
- (2) 2018 year-end figures are presented on NWM Plc solo basis of preparation.
- (3) Entities within NWM Group benefit 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.

Key points

- In NWM Plc, the decrease in period-end non-traded VaR mainly reflected a reduction in the sensitivity of the CET1 ratio to movements in foreign exchange rates. Increased structural foreign exchange exposure reduced NWM Plc's regulatory exposure to fluctuations in exchange rates against sterling. The VaR decrease was also driven by the disposals of the complex LOBO loans.
- In NWM N.V., period-end non-traded VaR was £0.4 million.



Interest rate risk

Non-traded interest rate risk (NTIRR) arises from non-match-funded positions, capital hedges and portfolios held for liquidity purposes. 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. NTIRR comprises three primary risk types: gap risk, basis risk and option risk.

NTIRR factors are grouped into the following categories:

- Gap risk – arises from the timing of rate changes in non-trading book instruments. The extent of gap risk depends on whether changes to the term structure of interest rates occur consistently across the yield curve (parallel risk) or differentially by period (non-parallel risk).
- Basis risk – captures the impact of relative changes in interest rates for financial instruments that have similar tenors but are priced using different interest rate indices, or on the same interest rate indices but with different tenors.
- Option risk – arises from option derivative positions or from optional elements embedded in assets, liabilities and/or off-balance sheet items, where NWM Group or its customer can alter the level and timing of their cash flows.

To manage exposures within appetite, NWM Group aggregates its interest rate positions and hedges these externally using cash and derivatives (primarily interest rate swaps).

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 fair-value accounted.

To ensure NWM Group can continue to meet its obligations in the event that access to wholesale funding markets is restricted, it maintains a liquidity buffer in the form of bond portfolios comprising primarily high-quality securities. Additionally, other high-quality bond portfolios are held for collateral purposes and to support payment systems. 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.

Capital and risk management

Non-traded market risk continued

Foreign exchange risk

Apart from the risk arising from the SABB shareholding (which is covered under Key developments during 2019), non-traded foreign exchange risk arises from two main sources:

- Structural foreign exchange risk – arises from the capital deployed in foreign branches, joint arrangements and related currency funding where it differs from sterling.
- Non-trading book foreign exchange risk – arises from customer transactions and profits and losses that are in a currency other than the functional currency of the transacting operation.

The structural foreign exchange exposures arising from investments in foreign branches and their related currency funding are assessed and managed by NWM Plc Treasury, taking into account the foreign exchange rate sensitivity of NWM Plc's solo CET1 ratio to predefined risk appetite levels under delegated authority from the NWM Plc ALCo.

Gains or losses arising from the retranslation of net investments in overseas operations are recognised in equity reserves and reduce the sensitivity of capital ratios to foreign exchange rate movements primarily arising from the retranslation of non-sterling-denominated RWAs.

Foreign exchange risk is managed with reference to the sensitivity of NWM Plc's solo CET1 ratio to changes in foreign exchange rates. The sensitivity of this ratio to exchange rates is monitored monthly and reported to NWM Plc senior management at least quarterly.

Foreign exchange exposures arising from customer transactions are sold down by businesses on a regular basis in line with RBS Group policy.

Foreign exchange exposures (audited)

The table below shows structural foreign currency exposures. It excludes the risk arising from the SABB shareholding, which is monitored and reported separately.

	Net investments in foreign operations £m	Net investment hedges £m	Structural foreign currency exposures £m	Economic hedges £m	Residual structural foreign currency exposures (1) £m
2019					
US dollar	1,520	—	1,520	(871)	649
Euro	1,891	(224)	1,667	—	1,667
Swiss franc	442	(439)	3	—	3
Other non-sterling	586	(45)	541	—	541
	4,439	(708)	3,731	(871)	2,860
2018					
US dollar	403	—	403	(403)	—
Euro	21	—	21	—	21
Swiss franc	472	(438)	34	—	34
Other non-sterling	597	(273)	324	—	324
	1,493	(711)	782	(403)	379

Notes:

- (1) The foreign exchange exposures table has been prepared from a NWM Group consolidated basis perspective.
- (2) The residual structural FX exposure represented the sum of the NAV of NWM Plc branches, together with any offsetting hedges against the local currency NAV valuations.
- (3) Other non-sterling mainly relates to branches that are expected to be exited over time.



Key points (audited)

- NWM Plc increased the capitalisation of its US branch. This has reduced the branch's debt funding and NWM Plc's regulatory exposure to fluctuations in the US dollar exchange rate against sterling.
- In November 2019, NWM Plc acquired NWM NV from RFSH, which increased NWM Group's residual structural foreign currency exposure to euros.



Capital and risk management

Credit risk

Definition (audited)

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

Sources of risk (audited)

The principal sources of credit risk for NWM Group are lending, off-balance sheet products, derivatives and securities financing, debt securities, and settlement risk through trading activities.

Key developments in 2019

- Credit risk RWAs for NWM Plc increased to £9.8 billion (2018 - £9.2 billion), primarily due to the transfer of the SABB shareholding from NWM N.V..
- IFRS 9 Stage 2 and Stage 3 assets decreased £0.7 billion during 2019, primarily due to the exit of a legacy defaulted exposure.

Risk governance (audited)

NWM Group operates an independent Credit Risk function, which provides oversight of frontline credit risk management activities. Authority is delegated to credit risk officers who operate within designated limits set at a customer level and a portfolio level.

Governance activities include:

- Defining credit policy to ensure controls are in place to effectively mitigate risk.
- Approving and monitoring credit limits.
- 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.

A Credit Risk Committee provides oversight of the overall credit risk profile and sector/product/asset class concentrations.

Risk appetite

NWM Group's approach to lending is governed by a comprehensive credit risk appetite framework which is operated across RBS Group. The framework is monitored and actions are taken to adapt lending criteria as appropriate. Credit risk appetite aligns to the strategic risk appetite set by the NWM Group Board. 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. The framework is supported by a suite of transaction acceptance standards that set out the risk parameters within which businesses should operate.

The four formal frameworks used – and their basis for classification – are detailed in the following table.

Framework	Basis for classification	
	Measure	Other
Single name concentration	Exposure	Risk – based on loss given default for a given probability of default
Sector		Risk – based on economic capital and other qualitative factors
Country		Risk – based on sovereign default risk, political stability and macroeconomic factors
Product and asset class		Risk – based on heightened risk characteristics

Risk controls

Credit policy standards are in place and are expressed as a set of mandatory controls.

Risk identification and measurement (audited)

Credit stewardship

Risks are identified through relationship management and/or credit stewardship of portfolios or customers. 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.

A key aspect of credit risk stewardship is monitoring signs of customer stress, and when identified, applying appropriate debt management actions.

Risk models

Credit risk models is the collective term used to describe all models, frameworks and methodologies used to calculate probability of default (PD), exposure at default (EAD), loss given default (LGD), maturity and the production of credit grades.

Credit risk models are designed to provide:

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

Asset quality

All credit grades map to an asset quality scale, used for financial reporting. For customers, a master grading scale is used for internal management reporting across portfolios. Measures of risk exposure may be aggregated and reported at differing levels of detail depending on stakeholder or business requirements. Performing loans are defined as AQ1-AQ9 (where the PD is less than 100%) and non-performing loans as AQ10 or Stage 3 under IFRS 9 (where the PD is 100%).

Counterparty credit risk

Counterparty credit risk arises from the obligations of customers under derivative and securities financing transactions. It is a material part of NWM Group's credit risk.

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

Risk mitigation

Risk mitigation techniques, as set out in the appropriate credit policies, are used in the management of credit portfolios across NWM 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.

Risk assessment and monitoring

Customers – including corporates, banks and other financial institutions – 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.

Capital and risk management

Credit risk *continued*

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 ethical risk policies which restrict exposure to certain highly carbon intensive industries as well as those with potentially heightened reputational impacts.

For lower-risk transactions below specific thresholds, credit decisions can be approved through self-sanctioning by the business, within the approved matrix limits. This process is facilitated through systems, strategies and policy rules.

For all other transactions, credit is only granted to customers following joint approval by an approver from the business and the credit risk function, or by two credit officers. The joint business and credit approvers act within a delegated approval authority under the Wholesale Credit Authorities Framework Policy. The level of delegated authority held by approvers is dependent on their experience and expertise with only a small number of senior executives holding the highest approval authority. Both business and credit approvers are accountable for the quality of each decision taken, although the credit risk approver holds ultimate sanctioning authority.

Transaction Acceptance Standards provide detailed transactional 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.

Credit grades (PD and LGD) are reviewed and, if appropriate, re-approved 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

Early problem identification

Each segment and 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 trade/transaction 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 customer has deteriorated. Experienced credit risk officers apply expert judgement 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 NWM 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 NWM 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 - including 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.

For further detail on the Risk of Credit Loss framework, refer to page 134 of the RBS Group Annual Report and Accounts.

Restructuring

Problem debt portfolio customer relationships are mainly managed by the Restructuring team in NatWest Bank Plc as a service to NWM Group. The team protects NWM Group's capital by working with corporate and commercial customers to support their turnaround and recovery strategies and enable them to return to mainstream banking. For further detail on Restructuring, refer to page 134 of the RBS Group Annual Report and Accounts.

Forbearance *(audited)*

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. The type of forbearance offered is tailored to the customer's individual circumstances and 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. For further detail on the implementation of forbearance in entities within RBS Group, refer to page 135 of the RBS Group Annual Report and Accounts.

Impairment, provisioning and write-offs *(audited)*

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

RBS Group's IFRS 9 provisioning models, which used 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 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 their 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 mechanisms).
 - 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 assets in Stage 2.
- **Model application:**
 - The assessment of the significant increase in credit risk 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 determination of a base case (or central) economic scenario which has the most material impact (of all forward-looking scenarios) on the measurement of loss (NWM Group uses consensus forecasts to remove management bias).

Refer to Accounting policy 11 for further details.

Capital and risk management

Credit risk continued

Economic loss drivers (audited)

Introduction

The most material economic loss drivers for the UK portfolios include UK GDP, world GDP, the UK unemployment rate, the UK house price index, and the UK base rate. Similar metrics are used for other key country exposures in NWM Group.

Central base case economic scenario

The internal base case scenario is the primary forward-looking economic information driving the calculation of ECL. The same base case scenario is used for financial planning by NWM Group with the exception of the yield curve, as a result of the different timing of the exercises. The key elements of the current economic base case, which includes forecasts over a five-year forecast horizon, are summarised as follows.

The central base case economic scenario projects modest growth in the UK economy, in line with the consensus outlook. Brexit-related uncertainty results in subdued confidence in the near term, placing it in the lower quartile of advanced economies. Business investment is weak at the start of the forecast, improving only gradually. Consumer spending rises steadily as households benefit from falling inflation and rising wage growth, though it is a modest upturn. The central scenario assumes slower job growth than seen in recent years, meaning unemployment edges up from its current historic lows. House price growth slows, extending the current slowdown, before picking up to low single-digit growth in later years. Monetary policy follows the market implied path for Bank of England base rate at the time the scenarios were set, therefore it is assumed there are two base rate cuts over the next five years, whereas the yield curve used for financial planning assumes one base rate cut.

For the purpose of calculating ECL, the primary input is the central base case scenario, but a further adjustment is applied to the aggregate credit cycle conditions arising from the base case to explicitly enforce a gradual reversion to long run average conditions starting from the first projected year onwards.

Key economic loss drivers

The tables and commentary below provide an update on the base case economics used at 31 December 2019. The average over the five year horizon (2020 to 2024) for the central base case used for ECL modelling is set out below. It is compared with the five year average (2019 to 2023) of the 2018 scenarios. The graph shows the quarterly GDP year-on-year growth rates. Subsequently, the annual figures for key variables across the UK are shown. The tables, commentary and graph below also summarise the upside 2 and downside 2 scenarios, used for ECL sensitivity analysis. Finally, the extreme points table show the best and worst readings for three key variables in the upside 2 and downside 2 scenarios, highlighting the most challenging points in the downside scenario and the strongest points in the upside scenario.

The 2019 base case GDP growth and interest rate assumptions are pessimistic compared to 2018 as consensus outlook and market implied interest rate projections worsened over the year. Unemployment rate projections are less extreme in the 2019 downside scenarios as RBS Group aimed to align the Downside 2 scenario with Office for Budget Responsibility's analysis of a hard Brexit scenario.

	2019			2018		
	Upside 2 %	Base case %	Downside 2 %	Upside 2 %	Base case %	Downside 2 %
UK						
GDP - change	2.4	1.6	0.9	2.6	1.7	1.1
Unemployment	3.6	4.4	5.2	3.3	5.0	6.9
House Price Inflation - change	4.1	1.6	(1.0)	4.3	1.7	(0.5)
Bank of England base rate	1.0	0.3	—	1.7	1.1	—
 World GDP - change	 3.8	 2.8	 2.1	 3.6	 2.7	 2.3
Probability weight	12.7	30.0	12.7	12.8	30.0	14.6

The application of the mean reversion adjustment is based on two empirical observations. Firstly, historic credit loss rates in Wholesale portfolios show pronounced mean reversion behaviour and secondly, the accuracy of economic forecasts tends to drop significantly for horizons beyond one or two years.

Approach for multiple economic scenarios (MES)

The response of portfolio loss rates to changes in economic conditions is typically non-linear and asymmetric. Therefore, in order to appropriately take account of the uncertainty in economic forecasts, a range of economic scenarios is considered when calculating ECL.

The approach to MES is a Monte Carlo method that involves simulating a large number of alternative scenarios around the central scenario (adjusted for mean reversion) and averaging the losses and PD values for each individual scenario into unbiased expectations of losses (ECL) and PD.

The simulation of alternative scenarios does not occur on the level of the individual economic loss drivers but operates on the aggregate Credit Cycle Indices (CCI) that underpin the Wholesale credit models. CCIs measure portfolio level default rate conditions expressed as an index value. An index value of zero represents long run average default rates. Negative and positive index values represent default rates above and below long run averages respectively.

The impact from MES is factored into account level PDs through scalars. These MES-adjusted PDs are used to assess whether a significant increase in credit risk has occurred.

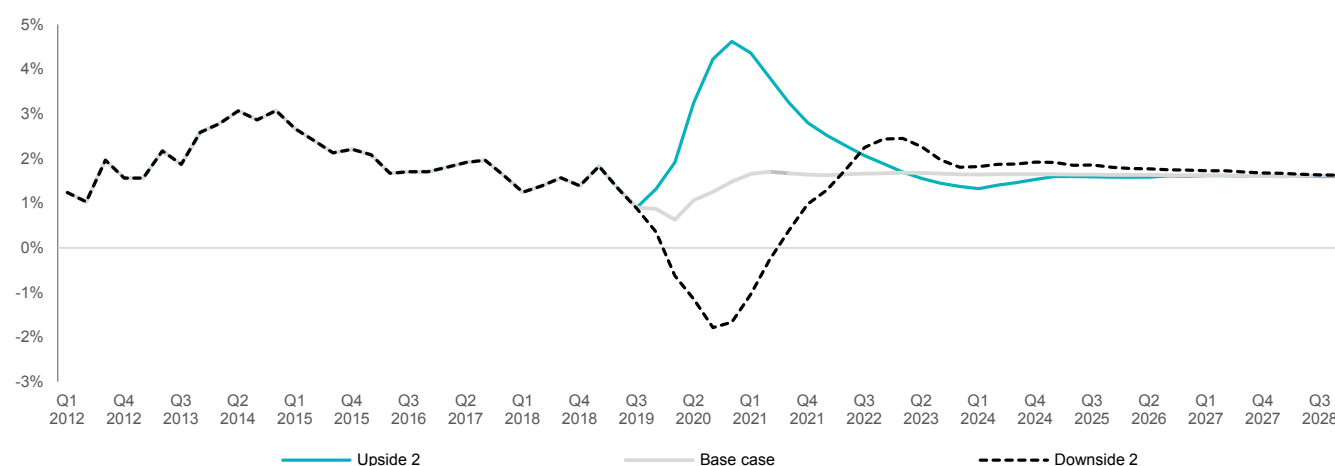
Capital and risk management

Credit risk continued

Economic loss drivers (audited)

Key economic loss drivers

UK Gross domestic product



UK GDP - annual growth

	Upside 2 %	Base case %	Downside 2 %
2019	1.3	1.2	1.1
2020	3.5	1.1	(1.3)
2021	3.6	1.7	—
2022	2.2	1.7	1.9
2023	1.5	1.7	2.1
2024	1.4	1.6	1.9

UK unemployment rate

	Upside 2 %	Base case %	Downside 2 %
Q4 2019	4.0	4.1	4.1
Q4 2020	3.7	4.4	5.1
Q4 2021	3.5	4.4	5.5
Q4 2022	3.5	4.4	5.4
Q4 2023	3.6	4.4	5.3
Q4 2024	3.8	4.4	5.1

UK House Price Inflation - annual growth

	Upside 2 %	Base case %	Downside 2 %
2019	1.7	1.5	1.4
2020	5.7	1.0	(3.6)
2021	8.2	0.9	(7.7)
2022	4.2	1.5	(1.9)
2023	1.7	2.0	3.0
2024	0.9	2.6	5.2

Extreme points

	Best points		Worst points	
	H2 2019 Upside 2 %	H2 2018 Upside 2 %	H2 2019 Downside 2 %	H2 2018 Downside 2 %
UK				
GDP (year-on-year)	4.6	5.0	(1.8)	(1.9)
Unemployment	3.5	2.8	5.5	7.4
House Price Inflation (year-on-year)	8.9	9.1	(8.4)	(7.3)

Capital and risk management

Credit risk continued

Economic loss drivers (audited)

UK economic uncertainty

NWM Group's approach is designed to capture the historic variability and distribution of economic risks. NWM Group's approach to capturing these incremental or skewed forward-looking risks is to apply an overlay to ECL of £4 million (2018 – £3 million). To calculate the value of this overlay, information was used from prevailing downside sensitivity scenario analyses. The underlying economics were broadly aligned to published International Monetary Fund and Office for Budget Responsibility hard Brexit scenarios and management judgement was applied on the likelihood of this alternative path for the economy emerging. The value of the overlay was increased once during the year, in the third quarter, when management judged uncertainty to be more pronounced. The value of the overlay was subsequently reviewed in the fourth quarter, when management concluded that it was appropriate to leave it unchanged reflecting the ongoing elevated economic uncertainty.

Credit risk modelling (audited)

ECLs are calculated using a combination of:

- Probability of default.
- Loss given default.
- Exposure at default.

In addition, lifetime PDs (as at reporting date and at date of initial recognition) are used in the assessment of the significant increase in credit risk criteria.

IFRS 9 ECL model design principles

To meet IFRS 9 requirements, PD, LGD and EAD used in ECL 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.
- **For the life of the loan** – all PD, LGD and EAD models produce term structures 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 probability of default over the remaining lifetime at the reporting date) with 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.

PD estimates

PD models use the existing CCI based point-in-time/through-the-cycle framework to convert one-year regulatory PDs into point-in-time estimates that reflect economic conditions observed at the reporting date across a comprehensive set of region/industry segments.

One-year point-in-time PDs are subsequently extended to life-time PDs using a conditional transition matrix approach. The conditional transition matrix approach allows for the incorporation of forward-looking economic information into the life-time PDs.

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 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

- △ 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 to produce unbiased model estimates.

No explicit forward-looking information is incorporated, on the basis that analysis has shown that temporal variations in CCFs are largely 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 RBS Group's model risk policy that stipulates periodic model monitoring, periodic re-validation and defines approval procedures and authorities according to model materiality. Post model adjustments (PMAs) are applied where necessary to incorporate the most recent data available and are made on a temporary basis ahead of the underlying model parameter changes being implemented. The PMAs held on a temporary basis ahead of the underlying model parameter changes being implemented were £0.3 million.

These adjustments were over and above those detailed in the UK economic uncertainty section and are also subject to oversight and governance by the Provisions Committee.



Significant increase in credit risk (audited)

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). NWM Group has adopted a framework to identify deterioration based primarily on movements in probability of default supported by additional backstops. The principles applied are consistent across NWM Group and align to credit risk management practices.

Capital and risk management

Credit risk continued

Significant increase in credit risk (audited)

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 to Stage 2 for a lifetime loss assessment. In broad terms, a doubling of PD would indicate a significant increase in credit risk. However, for Wholesale, the PD uplift must be at least 0.1%.
- **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 and exposures managed within the Risk of Credit Loss framework.

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.

Asset lifetimes (audited)

The choice of initial recognition and asset duration is another critical judgement 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 significant increase in credit risk.

For asset duration, the approach applied is:

- **Term lending** – the contractual maturity date, reduced for behavioural trends where appropriate (such as, expected pre-payment and amortisation).
- **Revolving facilities** – asset duration is based on annual counterparty review schedules and will be set to the next review date.



Measurement uncertainty and ECL sensitivity analysis (audited)

The recognition and measurement of ECL is complex and involves the use of significant judgement and estimation. 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. Set out below is the impact of some of the material sensitivities considered for 2019 year-end reporting. These ECL simulations are separate to the impact arising from MES and UK economic uncertainty as described earlier in this disclosure, which impacts are embedded in the reported ECL.

The primary 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 as at the year end balance sheet date. As default is an observed event as at the balance sheet date, Stage 3 provisions are not subject to the same level of measurement uncertainty, and therefore have not been considered in this analysis.



- **Economic uncertainty** – simulating the impact arising from the Downside 2 and Upside 2 scenarios, which are two of the five discrete scenarios used in the discrete MES methodology for RBS Group. In the simulation, RBS have assumed that the economic macro variables associated with these scenarios replace the existing base case economic assumptions, giving them a 100% probability weighting and thus serving as a single economic scenario.

Capital and risk management

Credit risk *continued*

Measurement uncertainty and ECL sensitivity analysis (audited)

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, e.g. potential customer behaviour changes, policy changes by lenders that might impact on the wider availability of credit.

These broader economic scenarios were complemented with a further specific portfolio simulation:

- **Through-the-cycle (TTC)** – simulating the impact of PDs and LGDs moving upwards to the TTC average from their current point-in-time (PIT) estimate. With the current relatively benign economic conditions, Wholesale IFRS 9 PIT PDs are significantly

lower than TTC PD. This scenario shows the increase to ECL by immediately switching to TTC measures providing an indication of long run average expectations. IFRS 9 measures have been used so there remains some differences to Basel TTC equivalent measures, where conservative assumptions are required, such as caps or floors, not permitted under the IFRS 9 best estimate approach.

NWM Group's core criterion to identify a significant increase in credit risk is founded on PD deterioration, as discussed above. Under the simulations, PDs increase and result in exposures moving from Stage 1 to Stage 2, contributing to the ECL impact.

	Actual position at 31 December 2019 Stage 1 and Stage 2 (1)			Common scenarios (2, 3)						Discrete scenarios (2, 3)		
	Exposure £bn	Of which in Stage 2 %	ECL provision (2) £m	Downside 2			Upside 2			TTC PD potential		
				Potential ECL impact £m	%	Exposure Stage 2 %	Potential ECL impact £m	%	Exposure in Stage 2 %	ECL impact £m	%	Exposure in Stage 2 %
Wholesale	33.6	0.6%	14.3	3.1	21.7%	0.7%	(2.4)	(17.1%)	0.4%	4.6	32.0%	1.2%

Notes:

- (1) Reflects drawn exposure and ECL for all modelled exposure in scope for IFRS 9; in addition to loans this includes bonds, and cash.
- (2) The ECL provision includes the ECL overlay taken to recognise elevated Brexit related economic uncertainty.
- (3) All simulations are run on a stand-alone basis and are independent of each other, with the potential ECL impact reflecting the simulated impact at the year end balance sheet date.
- (4) Refer to page 44 for details of base case economic scenarios.
- (5) 2018 comparative details are not included as the sensitivity scenario analysis relates to the 2019 balance sheet position. Refer to the 2018 Annual Report and Accounts for the sensitivity analysis carried out at that time.

Key points

- In the Downside 2 scenario, the ECL requirement overall was simulated to increase by £3 million on Stage 1 and 2 exposures from the current level of £14 million. The simulation estimates the balance sheet ECL requirement as at 31 December 2019 and assumes that the economic variables associated with the Downside 2 scenario had been RBS Group's base case economic assumption at that time.
- The Upside 2 scenario indicates a slightly lower release to ECL compared to the Downside 2 uplift. This is intuitive given the shape of the Upside 2 economics and non-linearity of losses to the downside.
- The TTC scenario has the most significant impact on ECL, highlighting that reverting to long run average PDs and LGDs is more severe than a switch to the Downside 2 scenario. The TTC scenario shows a higher ECL impact compared to the Downside 2 scenario given the relative severity of the TTC view. Furthermore, the TTC scenario assumes the higher PDs remain heightened at TTC levels over the simulation period, thus driving higher losses across the latter years of the scenario period compared to Downside 2.



Capital and risk management

Credit risk – Trading activities

This section details the credit risk profile of NWM Group's trading activities.

Securities financing transactions and collateral (audited)

The table below shows security funding transactions in NWM Group. Balance sheet captions include balances held at all classifications under IFRS 9.

	Reverse repos			Repos		
	Total £m	Of which: can be offset £m	Outside netting arrangements £m	Total £m	Of which: can be offset £m	Outside netting arrangements £m
2019						
Gross	52,829	52,021	808	56,985	54,510	2,475
IFRS offset	(28,720)	(28,720)	—	(28,720)	(28,720)	—
Carrying value	24,109	23,301	808	28,265	25,790	2,475
Master netting arrangements	(562)	(562)	—	(562)	(562)	—
Securities collateral	(22,378)	(22,378)	—	(25,228)	(25,228)	—
Potential for offset not recognised under IFRS	(22,940)	(22,940)	—	(25,790)	(25,790)	—
Net	1,169	361	808	2,475	—	2,475
2018						
Gross	56,143	53,157	2,986	57,445	56,288	1,157
IFRS offset	(31,376)	(31,376)	—	(31,376)	(31,376)	—
Carrying value	24,767	21,781	2,986	26,069	24,912	1,157
Master netting arrangements	(762)	(762)	—	(762)	(762)	—
Securities collateral	(21,009)	(21,009)	—	(24,150)	(24,150)	—
Potential for offset not recognised under IFRS	(21,771)	(21,771)	—	(24,912)	(24,912)	—
Net	2,996	10	2,986	1,157	—	1,157

Key points

- Reverse repos decreased slightly compared to 2018 on a gross basis, although carrying value was broadly unchanged. Gross repo exposure was similar to the prior year although carrying values increased moderately. These trends are consistent with trading assets and liabilities having been managed within limits at 31 December 2019.
- Reverse repo and repo transactions are primarily backed by highly-rated sovereign, supranational and agency collateral.



Debt securities (audited)

The table below shows debt securities held at mandatory fair value through profit or loss by issuer as well as ratings based on the lowest of Standard & Poor's, Moody's and Fitch.

	Central and local government			Financial institutions £m	Corporate £m	Total £m
	UK £m	US £m	Other £m			
2019						
AAA	—	—	2,197	1,188	5	3,390
AA to AA+	4,897	5,458	2,824	333	87	13,599
A to AA-	—	—	3,297	755	109	4,161
BBB- to A-	—	—	6,508	872	895	8,275
Non-investment grade	—	—	76	298	150	524
Unrated	—	—	—	420	48	468
Total	4,897	5,458	14,902	3,866	1,294	30,417
Short positions	(4,340)	(1,392)	(13,749)	(1,620)	(86)	(21,187)
2018						
AAA	—	—	2,093	1,459	7	3,559
AA to AA+	6,834	4,689	3,161	773	120	15,577
A to AA-	—	—	4,571	482	51	5,104
BBB- to A-	—	—	3,592	802	285	4,679
Non-investment grade	—	—	81	832	237	1,150
Unrated	—	—	—	570	8	578
Total	6,834	4,689	13,498	4,918	708	30,647
Short positions	(6,394)	(2,008)	(13,500)	(1,724)	(201)	(23,827)



Capital and risk management

Credit risk – Trading activities continued

Derivatives (audited)

The table below shows third party derivatives by type of contract. The master netting agreements and collateral shown do not result in a net presentation on the balance sheet under IFRS 9.

	2019					2018				
	Notional									
	GBP £bn	USD £bn	Euro £bn	Other £bn	Total £bn	Assets £m	Liabilities £m	Notional £bn	Assets £m	Liabilities £m
Gross exposure						151,557	147,104		135,133	131,173
IFRS offset						(3,876)	(4,011)		(2,072)	(2,438)
Carrying value	3,061	5,006	4,674	1,993	14,734	147,681	143,093	13,686	133,061	128,735
Of which:										
Interest rate (1)										
Interest rate swaps						87,324	82,445		81,622	73,933
Options purchased						15,299	—		14,478	—
Options written						—	13,198		—	16,370
Futures and forwards						11	10		73	68
Total	2,662	3,269	4,085	956	10,972	102,634	95,653	10,247	96,173	90,371
Exchange rate										
Spot, forwards and futures						30,336	30,714		17,897	18,605
Currency swaps						8,782	10,202		11,283	11,978
Options purchased						5,649	—		7,319	—
Options written						—	6,117		—	7,558
Total	398	1,728	579	1,037	3,742	44,767	47,033	3,422	36,499	38,141
Credit	1	6	10	—	17	280	359	16	346	208
Equity and commodity	—	3	—	—	3	—	48	1	43	15
Carrying value					14,734	147,681	143,093	13,686	133,061	128,735
Counterparty mark-to-market netting						(120,420)	(120,420)		(106,762)	(106,762)
Cash collateral						(18,682)	(17,187)		(17,930)	(15,224)
Securities collateral						(4,292)	(1,276)		(4,469)	(3,466)
Net exposure						4,287	4,210		3,900	3,283
Of which outside netting arrangements						2,048	4,145		1,933	1,599
Net exposure - intercompany						659	693		1,189	1,179
Banks (2)						607	821		359	431
Other financial institutions (3)						1,033	2,773		857	1,068
Corporate (4)						2,394	592		2,436	1,749
Government (5)						253	24		248	35
Net exposure						4,287	4,210		3,900	3,283
UK						2,004	1,783		1,867	1,246
Europe						1,374	1,868		1,117	1,366
US						428	331		588	298
RoW						481	228		328	373
Net exposure						4,287	4,210		3,900	3,283
Asset quality of uncollateralised derivative assets										
AQ1-AQ4						3,311			3,133	
AQ5-AQ8						955			743	
AQ9-AQ10						21			24	
Net exposure						4,287			3,900	

Notes:

- (1) The notional amount of interest rate derivatives includes £6,788 billion (2018 – £5,679 billion) in respect of contracts cleared through central clearing counterparties.
- (2) Transactions with certain counterparties with which NWM Group has netting arrangements but collateral is not posted on a daily basis; certain transactions with specific terms that may not fall within netting and collateral arrangements; derivative positions in certain jurisdictions, for example, China, where the collateral agreements are not deemed to be legally enforceable.
- (3) Transactions with securitisation vehicles and funds where collateral posting is contingent on NWM Group's external rating.
- (4) Mainly large corporates with which NWM Group may have netting arrangements in place, but operational capability does not support collateral posting.
- (5) Sovereigns and supranational entities with one-way collateral agreements in their favour.



Capital and risk management

Credit risk – Trading activities continued

Derivatives: settlement basis and central counterparties (audited)

The table below shows the third party derivative notional and fair value by trading and settlement method.

	Notional				Asset		Liability	
	Traded on recognised exchanges	Traded over the counter		Total	Traded on recognised exchanges	Traded over the counter	Traded on recognised exchanges	Traded over the counter
	£bn	Settled by central counterparties £bn	Not settled by central counterparties £bn	£bn	£m	£m	£m	£m
2019								
Interest rate	1,592	6,788	2,592	10,972	—	102,634	—	95,653
Exchange rate	3	—	3,739	3,742	—	44,767	—	47,033
Credit	—	—	17	17	—	280	—	359
Equity and commodity	1	—	2	3	—	—	—	48
Total	1,596	6,788	6,350	14,734	—	147,681	—	143,093
2018								
Interest rate	1,642	5,679	2,926	10,247	—	96,173	—	90,371
Exchange rate	4	—	3,418	3,422	—	36,499	—	38,141
Credit	—	—	16	16	—	346	—	208
Equity and commodity	—	—	1	1	—	43	—	15
Total	1,646	5,679	6,361	13,686	—	133,061	—	128,735

Credit risk – Net credit exposures for banking and trading activities

Asset quality (audited)

The table below shows the current and potential exposure by high-level asset class and asset quality. It represents total credit risk for assets held in the banking book in addition to counterparty credit risk for traded products. Refer to page 56 for a mapping of AQ band to probability of default range and indicative external credit rating.

	Cash & balances at central banks	Sovereign debt securities	Loans & other lending	Other debt securities	Collateralised rate risk management	Uncollateralised rate risk management	Repo & reverse repo	Off-balance sheet items	Leasing	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
2019										
AQ1-AQ4	12,729	6,854	9,217	2,142	4,150	2,517	1,454	1,060	32	40,155
AQ5-AQ8	—	—	1,628	30	625	735	116	47	1	3,182
AQ9	—	—	22	1	2	—	—	1	—	26
AQ10	—	—	44	1	—	6	—	4	4	59
Current exposure	12,729	6,854	10,911	2,174	4,777	3,258	1,570	1,112	37	43,422
Potential exposure	12,729	6,854	24,919	2,173	13,732	5,907	2,537	2,426	38	71,315
2018										
AQ1-AQ4	11,230	6,964	7,773	2,191	3,976	2,356	1,630	380	144	36,644
AQ5-AQ8	—	—	896	4	354	536	157	59	—	2,006
AQ9	—	—	23	3	2	—	—	—	—	28
AQ10	—	—	602	6	—	23	—	5	5	641
Current exposure	11,230	6,964	9,294	2,204	4,332	2,915	1,787	444	149	39,319
Potential exposure	11,230	6,964	18,516	2,204	15,097	6,634	2,882	2,594	149	66,270

Key points

- Measured against NWM Group's asset quality scale, 92% (2018 – 93%) of total current exposure was rated in the AQ1-AQ4 bands. When considered against external credit ratings, 94%, or £40.9 billion, of current exposure was equivalent to an investment grade rating of BBB- or better (2018 – 95%, £37.5 billion).
- The increase in total exposures primarily reflects the acquisition of NWM N.V. as well as increases in derivative fair values, which were largely as a result of a fall in yields during 2019.
- Net non-investment grade exposure increases were concentrated within loans & other lending, collateralised and uncollateralised rates risk management.
- This was largely driven by increases in existing derivatives exposures as well as credit downgrades on certain collateralised positions during the year.

Capital and risk management

Credit risk – Banking activities

Introduction

This section details the credit risk profile of NWM Group's banking activities.

Refer to Accounting policy 11 and Note 14 on the accounts for policies and critical judgements relating to impairment loss determination.

Presentation of interest in suspense recoveries

In March 2019, the IFRS Interpretations Committee (IFRIC) issued an agenda decision on the presentation of unrecognised interest when a credit-impaired financial asset (commonly referred to as a 'Stage 3' financial asset) is subsequently paid in full or is no longer credit-impaired. This concluded that the difference arising from the additional interest recovered must be recognised as a reversal of impairment

rather than within interest revenue. This affects both recognition and the reversal of the ECL allowance.

RBS Group changed its accounting policy in line with the IFRIC decision. Hence, the carrying amount of the financial assets within the scope of the provisions of the decision as well as the associated ECL allowance on the statement of financial position have been adjusted and the comparative period restated. The coverage ratio for the current and comparative periods have been adjusted and restated accordingly. There has been no restatement of the comparative period in statement of profit or loss on the grounds of materiality.

Refer to Accounting policy 1, Other amendments to IFRS, for further details.

Financial instruments within the scope of the IFRS 9 ECL framework (audited)

Refer to Note 11 on the accounts for balance sheet analysis of financial assets that are classified as amortised cost (AC) or fair value through other comprehensive income (FVOCI), the starting point for IFRS 9 ECL framework assessment.

Financial assets

	2019 £bn	2018* £bn
Balance sheet total gross AC/FVOCI	38.6	33.1
In scope of IFRS 9 ECL framework	33.5	30.1
% in scope	87%	91%
Loans - in scope	9.6	9.1
Stage 1	9.2	8.0
Stage 2	0.2	0.4
Stage 3	0.2	0.7
Other financial assets - in scope	23.9	21.0
Stage 1	23.9	21.0
Out of scope of IFRS 9 ECL framework	5.1	3.0

*2018 data has been restated for a change to presentation of unrecognised interest. Refer to Accounting policy 1, Other amendments to IFRS, for further details.

Those 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 £4.3 billion (2018 - £2.7 billion). These were assessed as having no ECL unless there was evidence that they were credit-impaired.
- Equity shares of £0.7 billion as not within the IFRS 9 ECL framework by definition (2018 - £0.3 billion).
- Fair value adjustments on loans hedged by interest rate swaps, where the underlying loan was within the IFRS 9 ECL scope – £0.1 billion (2018 - £nil).

In scope assets also include an additional £0.7 billion of inter-Group assets (2018 - £2.6 billion) not shown in table above.

Contingent liabilities and commitments

In addition to contingent liabilities and commitments disclosed in Note 28 on the accounts – reputationally-committed limits are also included in the scope of the IFRS 9 ECL framework. These are offset by £0.6 billion (2018 - £0.5 billion) out-of-scope balances, primarily related to facilities that, if drawn, would not be classified as AC or FVOCI, or undrawn limits relating to financial assets exclusions. Total contingent liabilities (including financial guarantees) and commitments within IFRS 9 ECL scope of £17.2 billion (2018 - £18.4 billion) comprised Stage 1; £17.1 billion (2018 - £18.1 billion); Stage 2 £0.1 billion (2018 - £0.2 billion) and Stage 3 £nil (2018 - £0.1 billion).



Capital and risk management

Credit risk – Banking activities continued

Portfolio summary (audited)

The table below shows gross loans and ECL, by segment and stage, within the scope of the IFRS 9 ECL framework.

2019	Total £m
Loans - amortised cost	
Stage 1	9,260
Stage 2	180
Stage 3	169
<i>Of which: individual</i>	158
<i>Of which: collective</i>	11
Inter-Group (1)	738
Total	10,347
ECL provisions (2)	
Stage 1	10
Stage 2	4
Stage 3	132
<i>Of which: individual</i>	123
<i>Of which: collective</i>	9
Total	146
ECL provisions coverage (3,4)	
Stage 1 (%)	0.11
Stage 2 (%)	2.22
Stage 3 (%)	78.11
Total	1.52
Impairment losses	
ECL charge (5)	
Stage 1	—
Stage 2	(7)
Stage 3	(41)
<i>Of which: individual</i>	(35)
<i>Of which: collective</i>	(6)
Third party	(48)
Total	(48)
ECL loss rate - annualised (basis points) (4)	(49.95)
Amounts written off	15
<i>Of which: individual</i>	15

For the notes to this table refer to the following page.

Key point

- Compared to 2018, there was a material reduction in Stage 2 and Stage 3 gross loans due to the resolution of several large legacy cases, which also contributed to the overall ECL net release of £48 million for 2019.

Capital and risk management

Credit risk – Banking activities continued

Portfolio summary (audited)

2018*	NatWest Markets £m	Central items & other £m	Total £m
Loans - amortised cost			
Stage 1	7,864	224	8,088
Stage 2	343	22	365
Stage 3	695	—	695
<i>Of which: individual</i>	680	—	680
<i>Of which: collective</i>	15	—	15
Inter-Group (1)	2,634	—	2,634
Total	11,536	246	11,782
ECL provisions (2)			
Stage 1	6	—	6
Stage 2	11	—	11
Stage 3	90	1	91
<i>Of which: individual</i>	84	—	84
<i>Of which: collective</i>	6	1	7
Total	107	1	108
ECL provisions coverage (3, 4)			
Stage 1 (%)	0.08	—	0.07
Stage 2 (%)	3.21	—	3.01
Stage 3 (%)	12.95	—	13.09
Total	1.20	0.41	1.18
Impairment losses			
ECL charge (5)			
Stage 1	(24)	(19)	(43)
Stage 2	—	(14)	(14)
Stage 3	(69)	19	(50)
<i>Of which: individual</i>	(45)	—	(45)
<i>Of which: collective</i>	(24)	19	(5)
Third party	(93)	(14)	(107)
Inter-Group	5	—	5
Total	(88)	(14)	(102)
ECL loss rate - annualised (basis points) (4)	(104.47)	(569.11)	(116.97)
Amounts written off	69	—	69
<i>Of which: individual</i>	63	—	63
<i>Of which: collective</i>	6	—	6

*2018 data has been restated for a change to presentation of unrecognised interest. Refer to Accounting policy 1, Other amendments to IFRS, for further details.

Notes:

- (1) NWM Group's intercompany assets were classified in Stage 1. The ECL attached to these loans was £0.3 million at 31 December 2019.
- (2) Includes £1 million (2018 – £2 million) related to assets classified as FVOCI.
- (3) ECL provisions coverage is calculated as ECL provisions divided by loans - amortised cost.
- (4) ECL provisions coverage and ECL loss rates are calculated on third party loans and related ECL provisions and charge respectively.
- (5) Includes a nil charge (2018 – £3 million charge) related to other financial assets, of which a £2 million release (2018 – £1 million charge) related to assets classified as FVOCI, offset by other charges; and a nil charge (2018 – £3 million release) related to contingent liabilities.
- (6) The table above shows gross loans only and excludes amounts that are outside the scope of the ECL framework. Refer to page 52 for Financial instruments within the scope of the IFRS 9 ECL framework for further details. Other financial assets within the scope of the IFRS 9 ECL framework were cash and balances at central banks totalling £12.7 billion and debt securities of £11.1 billion (2018 – £11.2 billion and £9.8 billion respectively).
- (7) Following the implementation of ring-fencing requirements there is no longer any exposure in NWM Plc which sits outside of the NatWest Markets franchise.



Capital and risk management

Credit risk – Banking activities continued

Portfolio summary – sector analysis (audited)

The table below shows financial assets and off-balance sheet exposures gross of ECL and related ECL provisions, impairment and past due by sector, asset quality and geographical region based on the country of operation of the customer. Except where indicated, the tables below report only third party exposures and related ECL provisions, charges and write-offs.

2019	Property £m	Corporate £m	FI £m	Sovereign £m	Total £m
Loans by geography	248	1,483	7,816	62	9,609
- UK	39	392	2,862	37	3,330
- Other Europe	209	799	2,156	22	3,186
- RoW	—	292	2,798	3	3,093
Loans by stage	248	1,483	7,816	62	9,609
- Stage 1	227	1,182	7,791	60	9,260
- Stage 2	—	157	23	—	180
- Stage 3	21	144	2	2	169
of which: individual	20	134	2	2	158
of which: collective	1	10	—	—	11
Weighted average life **					
- ECL measurement (years)	4	9	4	—	5
Weighted average 12 months PDs **					
- IFRS 9 (%)	0.31	0.67	0.26	0.02	0.27
- Basel (%)	0.46	0.83	0.23	0.02	0.30
ECL provisions by geography	12	122	10	2	146
- UK	8	5	3	1	17
- Other Europe	4	61	6	—	71
- RoW	—	56	1	1	58
ECL provisions by stage	12	122	10	2	146
- Stage 1	—	1	7	2	10
- Stage 2	—	3	1	—	4
- Stage 3	12	118	2	—	132
of which: individual	9	112	2	—	123
of which: collective	3	6	—	—	9
ECL provisions coverage (%)	4.84	8.23	0.13	3.23	1.52
- Stage 1 (%)	—	0.08	0.09	3.33	0.11
- Stage 2 (%)	—	1.91	4.35	—	2.22
- Stage 3 (%)	57.14	81.94	100.00	—	78.11
ECL charge - Third party	(35)	(5)	(8)	—	(48)
ECL loss rate (%)	(14.11)	(0.34)	(0.10)	—	(0.50)
Amounts written-off	1	11	3	—	15
Other financial assets by asset quality (1)	—	101	4,471	19,306	23,878
- AQ1-AQ4	—	101	4,078	19,285	23,464
- AQ5-AQ8	—	—	391	21	412
- AQ9	—	—	2	—	2
Off-balance sheet (2)	613	7,595	8,974	38	17,220
- Loan commitments	577	7,444	8,034	38	16,093
- Financial guarantees	36	151	940	—	1,127
Off-balance sheet by asset quality (1,2)	613	7,595	8,974	38	17,220
- AQ1-AQ4	525	7,045	8,756	38	16,364
- AQ5-AQ8	82	533	218	—	833
- AQ9	1	—	—	—	1
- AQ10	5	17	—	—	22

**Not within audit scope

For the notes to this table refer to the following page.

Capital and risk management

Credit risk – Banking activities continued

Portfolio summary – sector analysis (audited)

2018*	Property £m	Corporate £m	FI £m	Sovereign £m	Total £m
Loans by geography	666	1,852	6,570	60	9,148
- UK	41	1,424	3,238	50	4,753
- Other Europe	609	96	1,408	8	2,121
- RoW	16	332	1,924	2	2,274
Loans by stage	666	1,852	6,570	60	9,148
- Stage 1	84	1,628	6,318	58	8,088
- Stage 2	—	120	245	—	365
- Stage 3	582	104	7	2	695
of which: individual	574	100	6	—	680
of which: collective	8	4	1	2	15
Weighted average life **					
- ECL measurement (years)	4	4	9	5	5
Weighted average 12 months PDs **					
- IFRS 9 (%)	0.17	0.71	0.13	0.03	0.20
- Basel (%)	0.23	0.66	0.15	0.02	0.18
ECL provisions by geography	15	74	19	—	108
- UK	8	2	10	—	20
- Other Europe	2	42	7	—	51
- RoW	5	30	2	—	37
ECL provisions by stage	15	74	19	—	108
- Stage 1	—	—	6	—	6
- Stage 2	—	3	8	—	11
- Stage 3	15	71	5	—	91
of which: individual	11	70	3	—	84
of which: collective	4	1	2	—	7
ECL provisions coverage (%)	2.25	4.00	0.29	—	1.18
- Stage 1 (%)	—	—	0.09	—	0.07
- Stage 2 (%)	—	2.50	3.27	—	3.01
- Stage 3 (%)	2.58	68.27	71.43	—	13.09
ECL charge - Third party	(74)	(40)	6	1	(107)
ECL loss rate (%)	(11.11)	(2.16)	0.09	1.67	(1.17)
Amounts written-off	10	53	6	—	69
Other financial assets by asset quality (1)	105	64	2,721	18,099	20,989
- AQ1-AQ4	105	—	2,547	18,099	20,751
- AQ5-AQ8	—	64	167	—	231
- AQ9	—	—	4	—	4
- AQ10	—	—	3	—	3
Off-balance sheet (2)	385	2,209	12,618	3,226	18,438
- Loan commitments	338	2,032	12,376	3,226	17,972
- Financial guarantees	47	177	242	—	466
Off-balance sheet by asset quality (1,2)	385	2,209	12,618	3,226	18,438
- AQ1-AQ4	315	1,749	12,346	3,226	17,636
- AQ5-AQ8	36	440	272	—	748
- AQ9	1	—	—	—	1
- AQ10	33	20	—	—	53

*2018 data has been restated for a change to presentation of unrecognised interest. Refer to Accounting policy 1, Other amendments to IFRS, for further details.

**Not within audit scope

Notes:

(1) AQ bandings are based on Basel PDs and mapping is as follows:

Internal asset quality band	Probability of default range	Indicative S&P rating
AQ1	0% - 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%	CCC to C
AQ10	100%	D

(2) Off balance sheet exposures are managed in line with regulatory requirements. Therefore, any change in regulatory treatment is considered a business change. The decrease of £1.2 billion during the year primarily relates to revision of the treatments of nostros in line with the CRR requirements.

Key point

- **Asset quality** – Measured against NWM Group's asset quality scale, 97% (2018 - 96%) of total banking book exposure was rated in the AQ1-AQ4 bands. This equated to an indicative investment grade rating of BBB- or better.

Capital and risk management

Credit risk – Banking activities continued

Portfolio summary – sector analysis (audited)

Forbearance

The table below shows forbearance, Heightened Monitoring and Risk of Credit Loss by sector.

	Financial institution £m	Property £m	Sovereign £m	Other corporate £m	Total £m
2019					
Forbearance (flow)	—	10	—	46	56
Forbearance (stock)	—	11	—	46	57
Heightened Monitoring and Risk of Credit Loss	—	10	—	28	38
2018					
Forbearance (flow)	—	2	—	1	3
Forbearance (stock)	—	3	—	21	24
Heightened Monitoring and Risk of Credit Loss	90	1	16	197	304

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Credit risk enhancement and mitigation (audited)

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

	Gross exposure £bn	ECL £bn	Maximum credit risk Total £bn	Stage 3 £bn	CREM by type Financial (1) £bn	Property £bn	Other (2) £bn	CREM coverage Total £bn	Stage 3 £bn	Exposure post CREM Total £bn	Stage 3 £bn
2019											
Financial assets											
Cash and balances at central banks	12.7	—	12.7	—	—	—	—	—	—	12.7	—
Loans - amortised cost (3)	9.6	0.1	9.5	—	—	—	0.2	0.2	—	9.3	—
Debt securities	11.2	—	11.2	—	—	—	—	—	—	11.2	—
Total financial assets	33.5	0.1	33.4	—	—	—	0.2	0.2	—	33.2	—
Contingent liabilities and commitments	17.2	—	17.2	—	0.2	—	1.8	2.0	—	15.2	—
Total off-balance sheet	17.2	—	17.2	—	0.2	—	1.8	2.0	—	15.2	—
Total exposure	50.7	0.1	50.6	—	0.2	—	2.0	2.2	—	48.4	—
2018*											
Financial assets											
Cash and balances at central banks	11.2	—	11.2	—	—	—	—	—	—	11.2	—
Loans - amortised cost (3)	9.1	0.1	9.0	0.6	—	0.6	0.4	1.0	0.6	8.0	—
Debt securities	9.8	—	9.8	—	—	—	—	—	—	9.8	—
Total financial assets	30.1	0.1	30.0	0.6	—	0.6	0.4	1.0	0.6	29.0	—
Contingent liabilities and commitments	18.4	—	18.4	—	0.1	—	0.3	0.4	—	18.0	—
Total off-balance sheet	18.4	—	18.4	—	0.1	—	0.3	0.4	—	18.0	—
Total exposure	48.5	0.1	48.4	0.6	0.1	0.6	0.7	1.4	0.6	47.0	—

*2018 data has been restated for a change to presentation of unrecognised interest. Refer to Accounting policy 1, Other amendments to IFRS, for further details.

Notes:

- (1) Includes cash and securities collateral.
- (2) Includes guarantees and charges over trade debtors.
- (3) NWM Group holds collateral in respect of individual loans – amortised cost to banks and customers. This collateral includes mortgages over property; charges over business assets such as plant and equipment, inventories and trade debtors; and guarantees of lending from parties other than the borrower. RBS obtains collateral in the form of securities in reverse repurchase agreements. Collateral values are capped at the value of the loan.

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Capital and risk management

Credit risk – Banking activities continued

Flow statement (audited)

The flow statement that follows shows the main ECL and related income statement movements. It also shows the changes in ECL as well as the changes in related financial assets used in determining ECL. Due to differences in scope, exposures in this section may therefore 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 impact because they relate to balances at central banks. 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 to 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 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.

	Stage 1		Stage 2		Stage 3		Total	
	Financial assets £m	ECL £m	Financial assets £m	ECL £m	Financial assets £m	ECL £m	Financial assets £m	ECL £m
NWM Group								
At 1 January 2019	32,499	6	670	11	671	91	33,840	108
Currency translation and other adjustments	(1,204)	1	(9)	—	(17)	(4)	(1,230)	(3)
Inter-Group transfers	(1,139)	(1)	8	—	20	—	(1,111)	(1)
Transfers from Stage 1 to Stage 2	(235)	—	235	—	—	—	—	—
Transfers from Stage 2 to Stage 1	458	2	(458)	(2)	—	—	—	—
Acquisition of RBS Holdings N.V.	4,781	2	105	2	68	62	4,954	66
Net re-measurement of ECL on stage transfer		(1)		1		—		—
Changes in risk parameters (model inputs)		(3)		1		(2)		(4)
Other changes in net exposure	(2,283)	4	(363)	(9)	(543)	—	(3,189)	(5)
Other (P&L only items)	—	—	—	—	—	(39)	—	(39)
Income statement releases				(7)		(41)		(48)
Amounts written-off	—	—	—	—	(15)	(15)	(15)	(15)
At 31 December 2019	32,877	10	188	4	184	132	33,249	146
Net carrying amount	32,867		184		52		33,103	
At 1 January 2018	8,786	2	798	38	352	123	9,936	163
2018 movements	23,713	4	(128)	(27)	319	(32)	23,904	(55)
At 31 December 2018*	32,499	6	670	11	671	91	33,840	108
Net carrying amount	32,493		659		580		33,732	

*2018 data has been restated for a change to presentation of unrecognised interest. Refer to Accounting policy 1, Other amendments to IFRS, for further details.

2018 movements included transfers from Stage 1 to Stage 2 of £385 million (ECL – £0.3 million), transfers from Stage 2 to Stage 1 of £314 million (ECL – £28 million), transfers into Stage 3 of £2 million (ECL – nil) and transfers from Stage 3 of £35 million (ECL – nil). NWM Group recognised an ECL release of £22 million as a result of these cumulative transfers. It also included amounts written-off of £69 million.

Key points

- Stage 3 financial assets included £4 million (2018 – £166 million) purchased or originated credit impaired (POCI) assets. No ECL impairment was held on these positions and a £35 million impairment recovery was recognised on these POCI assets during the year, included in other (P&L only items).
- The reduction in Stage 3 exposure was mainly driven by the resolution and closure of one significant asset.
- Changes to risk parameters and the reduction in Stage 2 exposure during the year reflected an improvement in underlying credit risk metrics.
- Continued exit from legacy assets resulted in a net release of ECL provision.



Capital and risk management

Pension risk

Definition

Pension risk is the risk to NWM 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 NWM Group will make payments or other contributions to, or with respect to, a pension scheme because of a moral obligation or because NWM Group considers that it needs to do so for some other reason.

Sources of risk

NWM Group has exposure to pension risk through its defined benefit schemes worldwide. The two largest NWM Group schemes are the AA and the NatWest Markets sections of The Royal Bank of Scotland Group Pension Fund with a combined £1.4 billion of assets and £1.0 billion of liabilities as at 31 December 2019 (2018 – £1.3 billion of assets and £0.9 billion of liabilities). Further detail on NWM Group's pension obligations, including sensitivities to the main risk factors, can be found in Note 5 on the accounts.

Pension scheme liabilities vary with changes in long-term interest rates and inflation as well as with pensionable salaries, the longevity of scheme members and legislation. Pension scheme assets vary with changes in interest rates, inflation expectations, credit spreads, exchange rates, and equity and property prices. NWM Group is exposed to the risk that the schemes' assets, together with future returns and additional future contributions, are estimated to be insufficient to meet liabilities as they fall due. In such circumstances, NWM Group could be obliged (or might choose) to make additional contributions to the schemes, or be required to hold additional capital to mitigate this risk.

Key developments in 2019

- The triannual valuation of the AA Section and valuation of the new NWM Section as at 31 December 2018 was completed and agreed.
- The US defined benefit scheme closed and settled on 30 April 2019.

Risk governance

The Pension Committee, chaired by the Chief Financial Officer, formulates the NWM Group view of pension risk. The Pension Committee is a key component of NWM Group's approach to managing pension risk and it reviews and monitors risk management, asset and liability strategy and financing issues on behalf of NWM Group. Together with RBS Group, it also considers investment strategy proposals from the Trustee.

For further information on Risk governance, refer to page 23.

Risk appetite

NWM Group maintains an independent view of the risk inherent in its pension funds, with an associated risk appetite and defined metrics against which risk is measured.

Risk controls

A pension risk policy which sits within the NWM Group policy framework is also in place and is subject to associated framework controls.

Risk monitoring and measurement

NWM Group undertakes stress tests on its material defined benefit pension schemes each year. These tests are also used to satisfy the requests of regulatory bodies such as the Bank of England. The stress testing framework includes pension risk capital calculations for the purposes of the Internal Capital Adequacy Assessment Process as well as additional stress tests for a number of internal management purposes.

The results of the stress tests and their consequential impact on NWM Group's balance sheet, income statement and capital position are incorporated into NWM Group's and the overall RBS Group stress test results.

Risk mitigation

Following risk mitigation measures taken by the Trustee in recent years, the AA and the NatWest Markets sections of the RBS Group Pension Fund are now well protected against interest rate and inflation risks and are being run on a low risk basis with relatively small equity risk exposure. The AA and the NatWest Markets sections of the RBS Group Pension Fund also use derivatives to manage the allocation of the portfolio to different asset classes and to manage risk within asset classes.

The potential impact of climate change is one of the factors considered in managing the assets of the pension schemes. Accordingly, the Trustee monitors the risk to its investments from changes in the global environment and invests, where return justifies the risk, in sectors that reduce the world's reliance on fossil fuels, or that may otherwise promote environmental benefits. Further details regarding the Trustee's approach to managing climate change risk can be found in its Responsible Ownership Policy.

Compliance & conduct risk

Definition

Compliance risk is the risk that the behaviour of NWM 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 NWM Group, its subsidiaries or 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 NWM 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 insider information.

Key developments in 2019

- Policies were rationalised and simplified to support wider understanding and compliance.
- Targeted training was rolled out across the lines of defence to support framework embedding.
- Planning for LIBOR transition continued including an extended SONIA pilot and further industry engagement.
- Preparations continued for a number of Brexit outcomes.

Risk governance

NWM Group defines appropriate standards of compliance and conduct and ensures adherence to those standards through the risk management framework. The Conduct & Culture Committee is the decision-making forum for conduct-related matters in NWM Group. It considers business plans and initiatives, as well as strategic decisions, with the aim of ensuring conduct risk is adequately mitigated. The committee also ensures that staff receive the appropriate level of conduct training.

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.

Capital and risk management

Compliance & conduct risk continued

Risk controls

A range of controls is operated to ensure 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 RBS 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.

Risk monitoring and measurement

Compliance and conduct risks are measured and managed through continuous assessment and reporting to 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.

Risk mitigation

Activity to mitigate the most-material compliance and conduct risks is carried out across RBS Group with specific areas of focus in the customer-facing businesses and subsidiaries such as NWM Group. Examples of mitigation include consideration of customer needs in business and product planning, targeted training, complaints management, as well as independent assurance activity. Internal policies help support a strong customer focus across RBS Group. Independent assessments of compliance with applicable regulations are also carried out at NWM Group level.

Financial crime risk

Definition

Financial crime risk is the risk presented by criminal activity in the form of money laundering, terrorist financing, bribery and corruption, sanctions and tax evasion. It does not include fraud risk management.

Sources of risk

Financial crime risk may be presented if NWM Group's employees, customers or third parties undertake or facilitate financial crime, or if NWM 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 2019

- Enhanced risk assessment processes were implemented to enable improved identification and mitigation of financial crime risks.
- Progress was made on investment and planning for a new transaction monitoring system, aligned to NWM Group.
- A comprehensive review of financial crime controls across NWM Group's first and second lines of defence was completed.
- Financial crime policies were refreshed and updated to reflect changes to the regulatory environment and industry best practice.
- NWM Group financial crime risk appetite statements were revised.
- An enhanced governance structure was implemented for NWM Group's Financial Crime function.

Risk governance

The Financial Crime Risk Committee (FCRC), which is chaired by the Head of Compliance & Financial Crime, is the NWM Group's principal financial crime risk management forum. The committee reviews and, where appropriate, escalates material financial crime risks and issues across the NWM Group to the NWM Executive Risk Committee and NWM Board Risk Committee. Additionally FCRC reports to the RBS Group Financial Crime Risk Executive Committee, which escalates material financial crime risks and issues to the RBS Group Executive Risk Committee and the RBS Group Board Risk Committee.

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. 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.

Risk controls

A framework of preventative and detective controls is operated across NWM Group and is designed to mitigate the risk that it could facilitate financial crime. These controls are supported by a suite of policies, procedures and detailed instructions to ensure they operate effectively.

Risk monitoring and measurement

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

Risk mitigation

Through the financial crime framework, NWM Group employs relevant policies, systems, processes and controls to mitigate financial crime risk. This would include the use of dedicated screening and monitoring controls to identify people, organisations, transactions and behaviours which might require further investigation or other actions. RBS Group ensures that centralised expertise is available to detect and disrupt threats to NWM Group and its customers. Intelligence is shared with law enforcement, regulators and government bodies to strengthen national and international defences against those who would misuse the financial system for criminal motives.

Climate-related financial risk

Definition

Climate-related financial risk is the threat of financial loss associated with the impact of climate change and the political, economic and environmental responses to it.

Sources

Physical risks can 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. NWM Group could be exposed to physical risks directly by the impacts on its property portfolio and, indirectly, by the impacts on the wider economy as well as impacts on the property and business interests of its customers.

Transition risks can 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. NWM Group could be exposed to transition risks directly through the costs of adaptation within economic sectors and markets, while potential indirect effects include the erosion of competitiveness, profitability, or potential reputation damage.

Key developments in 2019

- Climate-related financial risk was classified as a top risk.
- A strategy has been developed to embed the financial risks arising from climate change in the risk management framework.
- A multi-phase, multi-year plan has been developed at RBS Group level to build out capabilities across risk management, governance, scenario analysis and stress testing.

Capital and risk management

Climate-related financial risk continued

Risk governance

The RBS Group Board is responsible for addressing and overseeing the financial risks from climate change within NWM Group's overall business strategy and risk appetite. The potential impact, likelihood and preparedness of climate-related financial risk on NWM Group is reported quarterly to NWM Group's senior risk committees.

The RBS Group Chief Risk Officer is accountable for ensuring the financial risks from climate change are captured in the risk management framework and for ensuring NWM Group can measure, monitor, manage and report those risks.

NWM Group is represented on the executive steering group of RBS Group's Climate Change Programme.

Risk appetite

As part of the strategy for managing climate-related financial risk, it will be incorporated in the setting of appetite for all relevant risk disciplines. If it is deemed to have a material impact on a particular risk discipline then changes to relevant policies and procedures will be made accordingly. Availability of data and the robustness of risk measurement methodologies will influence the timing of any proposed changes.

Risk monitoring and measurement

Plans have been developed to ensure climate-related financial risks are considered in the tools made available to risk disciplines for risk monitoring and measurement purposes.

A process is underway to identify where climate risk requires the use of new key data elements, new risk metrics and enhancement of risk methodologies. The outputs of the Bank of England's 2021 biennial exploratory scenario will be used to further enhance RBS's capabilities for the measurement of climate-related risks.

Operational risk

Definition

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.

Sources of risk

Operational risk may arise from a failure to manage operations systems, transactions and assets appropriately. This can take the form of an inability to deliver change adequately or on time, the non-availability of technology services, the loss of customer data and unauthorised trading as well as the external impact of cyber attacks and natural or man-made disasters.

Key developments in 2019

- There were continued improvements in the operational risk profile for NWM with particular remediation progress in the year evident across Trade & Transaction Reporting, Financial Reporting and Data Management risk types.
- To minimise disruption to customers, a focus remained on maintaining operational resilience and ensuring preparedness for external threats and challenges such as Brexit, with the NWM NV subsidiary becoming fully operational.
- NatWest Markets benefits from the RBS Group's multi-layered approach to cyber security. The RBS Group invested in control enhancements to keep pace with the evolving threat landscape. This included new anti-malware controls and improved security testing to quickly detect and remediate vulnerabilities.
- NatWest Markets also focused on the development and implementation of the RBS Group Internal Service Management framework and policy, designed to support effective intra-group management of services between legal entities and enable Operational Continuity in Resolution (OCiR) with NWM Group's attestation of compliance with OCiR requirements due to be provided in Q1 2020.

Risk governance

NWM Group's operational risk profile is overseen by the NWM Group Board Risk Committee and Executive Risk Committee.

The Operational Risk function, which is the second line of defence, is accountable for oversight of a robust operational risk management framework for NWM Group which supports the identification, assessment, management and monitoring of operational risk. It is also responsible for reporting and escalating key concerns to the Board Risk Committee and Executive Risk Committee. A strong operational risk management function is vital to support NWM Group's ambitions to serve its customers better.

Risk appetite

Management of operational risk against defined appetite directly supports the strategic risk objective of improving stakeholder confidence and is vital for stability and reputational integrity. NWM Group's operational risk appetite expresses the level and types of operational risk NWM Group is willing to accept to achieve its strategic objectives and business plans.

The NWM Group operational risk appetite statement encompasses the most material risk appetite measures which are those that align to strategy and should the limit be breached, would impact on the ability to achieve business plans and threaten stakeholder confidence.

Risk controls and mitigation

The Control Environment Certification (CEC) process is a half yearly self-assessment by NWM Group to provide a consistent and comparable view on the adequacy and effectiveness of the internal control environment.

CEC covers material risks and the underlying key controls, including operational, financial crime and compliance controls, as well as supporting risk management frameworks. The CEC outcomes, including forward-looking assessments for the next two half-yearly cycles and progress on control environment improvements, are reported to the RBS Group Audit Committee and Board Risk Committee. They are also shared with external auditors.

The CEC process helps to ensure compliance with the RBS Group Policy Framework, Sarbanes-Oxley 404 requirements concerning internal control over financial reporting (as referenced in the Compliance Report on page 106 of the RBS Group ARA), and certain requirements of the UK Corporate Governance Code.

Risks are mitigated by applying key preventative and detective controls, an integral step in the risk assessment methodology which determines residual risk exposure. Control owners are accountable for the design, execution, performance and maintenance of key controls. Key controls are regularly assessed for adequacy and tested for effectiveness. The results are monitored and, where a material change in performance is identified, the associated risk is re-evaluated.

Risk monitoring and measurement

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 RBS Group's Risk Directory. Risk assessments are refreshed as appropriate to ensure they remain relevant and capture any emerging risks and to also ensure risks are reassessed. Change Risk is also identified and managed through the delivery of change risk reviews across NWM Group's highest risk change and strategic investment programmes.

These processes are 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.

Capital and risk management

Operational Risk continued

NWM Group uses the standardised approach to calculate its Pillar 1 operational risk capital requirement. This is based on multiplying three years' average historical gross income by coefficients set by the regulator based on business line. As part of the wider Internal Capital Adequacy Assessment Process an operational risk economic capital model is used to assess Pillar 2A, which is a risk-sensitive add-on to Pillar 1. The model uses historical loss data (internal and external) and forward-looking scenario analysis to provide a risk-sensitive view of NWM Group's P2A capital requirement.

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

Refer to the Capital, liquidity and funding risk section for operational risk capital requirement figures.

Operational resilience

NWM Group currently manages and monitors business and technology resilience through its operational risk management framework, including consideration of these risks in risk and control assessments, as well as the setting and monitoring risk indicators and performance metrics for key business services. Progress continues on the response to regulator expectations on operational resilience, with involvement in a number of industry wide operational resilience forums.

Event and loss data management

The operational risk event and loss data management process ensures NWM Group captures and records operational risk financial and non-financial events that meet defined criteria. Loss data is used for regulatory and industry reporting and is included in capital modelling when calculating economic capital for operational risk. The most serious events are escalated in a simple, standardised process to all senior management, by way of a Group Notifiable Event Process. All financial impacts associated with an operational risk event are reported against the date they were recorded in NWM Group's financial accounts. A single event can result in multiple losses (or recoveries) that may take time to crystallise. Losses and recoveries with a financial accounting date in 2019 may relate to events that occurred, or were identified in, prior years. NWM Group purchases insurance against specific losses and to comply with statutory or contractual requirements.

Model risk

Definition

Model risk is the risk that a model is specified incorrectly (not achieving the objective for which it is designed), implemented incorrectly (an error in translating the model specification into the version actually used), or being used incorrectly (correctly specified but applied inappropriately).

Sources of risk

NWM Group uses a variety of models as part of its risk management process and activities. Key examples include the use of model outputs to support risk assessments in the credit approval process, ongoing credit risk management, monitoring and reporting, as well as the calculation of risk-weighted assets and bad debt provisions. Other examples include the use of models to measure market risk exposures and calculate associated capital requirements, as well as for the valuation of positions. The models used for stress-testing purposes also play a key role in ensuring NWM Group holds sufficient capital, even in stressed market scenarios.

Key developments in 2019

- Improved the model risk policy to further embed regulatory guidelines on stress test models within the model risk framework.
- Instigated the Model Risk Committee, a senior forum that has oversight of, and challenges, the entire model population that impacts NWM, including both first and second line of defence models.

Governance

A governance framework is in place to ensure policies and processes relating to models are appropriate and effective. Escalations are made to senior management through the Model Risk Committee. The committee also considers whether a model can be approved for use. Models used for regulatory reporting may additionally require regulatory approval before implementation.

Risk appetite

Model risk appetite is defined in the model risk appetite statement and approved by the Board. Model owners and model users are responsible for monitoring performance against appetite, reporting on the model population and carrying out any necessary remediation for positions outside appetite.

Risk controls

Validation for material models is conducted by an independent risk function. Validation also ensures models are developed and implemented appropriately and that their operational environment is fit for purpose. Reviews of relevant models are carried out for new models or amendments to existing models and as part of an ongoing programme to assess model performance. Reviews may test and challenge the logic and conceptual soundness of the methodology or the assumptions underlying a model. Reviews may also test whether or not all appropriate risks have been sufficiently captured as well as checking the accuracy and robustness of calculations.

Risk monitoring and measurement

The appropriateness of approved risk models is reassessed on a periodic basis. Each periodic review begins with an initial assessment. Based on the initial assessment, internal model governance, including relevant stakeholders, will decide to re-ratify a model or to carry out additional work. The initial assessment considers factors such as a change in the size or composition of the portfolio, market changes, the performance of – or any amendments to – the model and the status of any outstanding issues or scheduled activities carried over from previous reviews.

Risk mitigation

Model risk is mitigated by ensuring adherence to policies and procedures relating to the approval, validation and ongoing monitoring of material models.

Reputational risk

Definition

Reputational risk is the threat to NWM Group's public image from a failure to meet stakeholders' expectations in relation to performance, conduct or business profile. Stakeholders include customers, investors, employees, suppliers, government, regulators, special interest and consumer groups, media and the general public.

Sources of risk

Reputational risk can arise from the conduct of employees; customer activities and the sectors and countries in which they operate; provision of products and transactions; as well as operations and infrastructure. Unexpected external events can also pose a reputational risk to NWM Group.

Capital and risk management

Reputational risk *continued*

Key developments in 2019

- Updated existing environmental, social and ethical risk acceptance criteria to reflect changes in the wider external environment.
- Enhanced existing escalation processes for businesses and improved reputational risk management in functions.
- Consideration of climate change issues within the reputational risk framework.

Risk governance

A reputational risk policy supports reputational risk management across NWM Group. The NWM Reputational Risk Committee reviews relevant issues at an individual business or entity level, while the RBS Group Reputational Risk Committee – which has delegated authority from the Executive Risk Committee – opines on cases, issues, sectors and themes that represent a material reputational risk to RBS Group. The Board Risk Committee oversees the identification and reporting of reputational risk. The RBS Group Sustainable Banking Committee has a specific focus on environmental, social and ethical issues.

Risk appetite

NWM Group manages and articulates its appetite for reputational risk through a qualitative reputational risk appetite statement and quantitative measures. NWM Group seeks continuous improvement in the identification, assessment and management of customers, transactions, products and issues that present a material reputational risk.

Risk controls

For information on risk controls refer to page 25.

Risk monitoring and measurement

Primary reputational risk measures are in place to assess internal activity relating to the management of reputational risk, including training. A number of secondary risk measures – including measures also used in the management of operational, conduct and financial risks – are used to assess relevant external factors. Quarterly reports on performance against these measures are provided to the Executive Risk Committee and Board Risk Committee.

Risk mitigation

Reputational risk is mitigated through the policy and governance framework, with ongoing staff training to ensure early identification, assessment and escalation of material issues. External, unexpected, events that could cause reputational damage are generally mitigated through NWM Group's Top and Emerging Risks process.

The most material threats to NWM Group's reputation continued to originate from historical and more recent conduct issues. As a result, RBS Group has been the subject of investigations and reviews by a number of regulators and governmental authorities, some of which have resulted in fines, settlements and public censure. Refer to the Litigation, investigations and reviews section of Note 28 on the accounts.

Report of the directors

The directors present their report together with the audited accounts for the year ended 31 December 2019

Other information incorporated into this report by reference can be found at:

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Group Structure

NatWest Markets Plc ('NWM Plc') is a wholly-owned subsidiary of The Royal Bank of Scotland Group plc ('RBSG plc' or 'the holding company'). NatWest Markets Group ('NWM Group') comprises NWM Plc and its subsidiary and associated undertakings. The term 'RBS Group' comprises RBSG plc and its subsidiary and associated undertakings. RBSG plc is incorporated in the UK and has its registered office at 36 St Andrew Square, Edinburgh, EH2 2YB.

Details of NWM Plc's principal subsidiary undertakings and their activities are shown in Note 15 on the accounts. A full list of related undertakings of NWM Plc is shown in Note 37 on the accounts.

With effect from 29 November 2019, RBS Holdings N.V. (RBSH N.V.) is a wholly-owned subsidiary of NWM Plc. RBSH N.V. is the parent company of NatWest Markets N.V. (NWM N.V.). The term 'NWM N.V. Group' comprises NWM N.V. and its subsidiary and associated undertakings. NWM N.V. is a licensed bank regulated by the De Nederlandsche Bank.

The financial statements of The Royal Bank of Scotland Group plc can be obtained from RBS Legal, Governance and Regulatory Affairs, RBS Gogarburn, Edinburgh, EH12 1HQ, the Registrar of Companies or through the website [rbs.com](https://www.rbs.com).

Activities

NWM Group is engaged principally in providing financing, risk management and trading solutions to customers.

Results and dividends

The loss attributable to the ordinary shareholders of NWM Group for the year ended 31 December 2019 was £181 million compared with a profit of £1,241 million for the year ended 31 December 2018, as set out in the consolidated income statement on page 78.

NWM Plc paid two ordinary dividends to RBSG plc in 2019 totalling £500 million, £1.25 per share (2018 – £2,550 million, £6.38 per share).

Employees

As at 31 December 2019, NWM Group employed 5,000 people (full-time equivalent basis, including temporary workers). This included 1,500 central and support staff who were transferred from National Westminster Bank Plc during 2019 as part of ring-fencing implementation. Details of all related costs are included in Note 3 on the consolidated accounts.

Corporate Governance statement

The Companies (Miscellaneous Reporting) Regulations 2018 introduced new statutory reporting requirements for financial years beginning on or after 1 January 2019. As a result of these new requirements, the directors of the company are required to provide a statement in the Directors' Report stating which corporate governance code, if any, the company followed during the year; how it applied the code and any part of the code it did not follow. For the financial year ended 31 December 2019, the company has chosen to report against the Wates Corporate Governance Principles for Large Companies (the Wates Principles) and the disclosures below explain how the company has applied the Wates Principles in the context of its corporate governance arrangements.

1. Purpose and leadership

Purpose

RBS Group's Purpose is established by the RBSG plc Board, promoted across RBS Group and cascaded to subsidiaries including NWM Plc. Further information on RBS Group's Purpose can be found in the 2019 Annual Report and Accounts of RBSG plc.

Strategy

RBS Group's strategy is set and approved by the RBSG plc Board.

The NWM Plc Board (the Board) reviews and sets the strategic direction of NWM Plc and, as appropriate, the strategies for each of its businesses within the parameters set by the RBSG plc Board. It subsequently oversees the execution of the strategy and holds management to account for its delivery.

Culture

The RBSG plc Board is supported in monitoring culture across RBS Group by the Group Sustainable Banking Committee and the Group Board Risk Committee. RBS Group is on a journey towards a generative risk culture whereby "risk is simply part of the way people work and think".

Building a healthy culture that embodies Our Values is a core priority for RBS Group.

Our Values, which guide the way RBS Group identifies the right people to serve customers well, and how to manage, engage and reward colleagues, are at the heart of Our Code (the RBS Group-wide Code of Conduct).

There is regular reporting to the Board on culture, so as to provide appropriate oversight of culture matters. More specifically, with regards to risk culture, significant progress has been made towards addressing historical conduct issues, including the strengthening of the governance arrangements, improved management information and wider engagement with staff. This supports our ambition to create a positive culture and strengthen 'good conduct' outcomes for clients.

2. Board Composition

The Board

The Board has six directors comprising the Chairman, one executive director (being the Chief Executive Officer) and four further non-executive directors. The size of the Board is considered appropriate, taking into account the size and scale of NWM Plc's business. Biographies for each of the directors can be found on our website:

<https://www.nwm.com/about-us/board-and-governance/board-of-directors>

The Chairman

The role of the Chairman is to lead the Board and ensure its overall effectiveness. This is distinct and separate from that of the Chief Executive Officer who manages the business day-to-day. The Chairman is also a member of the RBSG plc Board which provides an appropriate linkage to the wider RBS Group and ensures alignment and awareness in respect of RBS Group-wide matters.

Non-Executive Directors

The majority of the Board comprises independent non-executive Directors. Their role is to challenge and scrutinise the performance of management and to help develop proposals on strategy. They also review the performance of management in meeting agreed goals and objectives and monitor the firm's risk profile. The non-executive directors combine broad business and commercial expertise and bring experience from a wealth of areas including audit, banking, finance, human resources, technology, and telecommunications.

The Board periodically undertakes an independence assessment of the non-executive directors. With the exception of the Chairman, who is a member of the RBSG plc Board, all non-executive directors are considered to be independent and there are no relationships or circumstances that are likely to affect their judgement.

Report of the directors

Induction Training

All new directors undergo a formal induction programme upon joining the Board which is coordinated by the Company Secretary and tailored to their individual needs. This includes meetings with other directors, senior executives and business heads. Meetings with the external auditor, legal counsel and other key stakeholders are arranged as appropriate. Directors also receive comprehensive guidance from the Company Secretary on NWM Plc's corporate governance framework and associated policies, including their duties as directors.

Continuous Development

Non-executive directors discuss their professional development annually with the Chairman. Directors maintain their knowledge and familiarity with NWM Plc through regular meetings with senior management (including representatives of RBS Group) and participate in scheduled Board training and other external sessions as appropriate. During 2019, bespoke training was arranged for the directors on Conflicts of Interest, Whistleblowing, and Traded Market Risk. Directors may also request individual in-depth briefings from time to time on areas of particular interest.

Board Diversity

The Board is committed to promoting diversity and inclusion in the boardroom and aims to meet industry targets and recommendations wherever possible. The Board has agreed a Boardroom Inclusion Policy which aims to promote diversity and inclusion in the composition of the Board of Directors and in the nomination and appointment process. The Policy reflects the values of the wider Group, its Inclusion Policy and relevant legal, regulatory or best practice requirements.

Committees

The responsibilities of the Board are discharged, in part, through its committees (namely, the Audit Committee, the Board Risk Committee, the Performance & Remuneration Committee and the Nominations Committee). All matters that the Board has specifically delegated to these committees are set out in their Terms of Reference (ToRs) which are reviewed at least annually. All other matters, including responsibility for the day-to-day operation of NWM Plc (that are not specifically reserved for the Board or delegated to a committee) are delegated to the NWM Plc Chief Executive Officer (CEO) in accordance with such policies and directions as the Board determines appropriate, including the NWM Plc CEO's role profile and the NWM Plc Executive Committee's ToRs.

Succession

The Board is responsible for ensuring that NWM Plc has in place succession plans for the Board and senior management so as to maintain an appropriate balance of skills and experience. The RBS Group Nominations & Governance Committee is also required to approve all appointments to the Board, thereby reflecting the company's position as a subsidiary of RBS Group.

Board Effectiveness

The effectiveness of the Board, including the Chairman, individual directors and Board committees, is assessed periodically. The Board considers such assessments to play an important role in the identification of areas for further improvement, focus and for strengthening its overall performance.

The Company Secretary

In fulfilling its role, the Board is supported by the Company Secretary. The Company Secretary is responsible for ensuring good information flows between the Board and its committees and between senior management and non-executive directors, as well as facilitating induction and assisting with professional development of non-executive directors, as required. The directors may also seek independent, professional advice, where necessary, at NWM Plc's expense.

3. Director Responsibilities Policy & Framework

RBS Group has in place a Corporate Governance Framework, including a Corporate Governance Policy. All Directors of NWM Plc are required to ensure that they are familiar with the Corporate Governance Framework and that NWM Plc complies with it. NWM Plc also produces and maintains a document ("Our Governance") which sets out the high-level governance framework for NWM Plc at both regional and global levels.

The Board has a programme of seven scheduled meetings every year plus two additional days for strategic planning with the NWM Executive Committee. The Board's ToRs include a formal schedule of matters specifically reserved for the Board which are reviewed at least annually. Each director has a role profile which clearly articulates their responsibilities and accountabilities. Similarly, any additional regulatory responsibilities and accountabilities where any of the directors undertake a Senior Manager Function (as defined under the Prudential Regulation Authority's and Financial Conduct Authority's 'Senior Manager Regimes') are set out in their Statement of Responsibilities.

To support them in the discharge of their duties, all directors receive regular and timely information on all key aspects of the business including financial performance, strategy, key risks, and market conditions.

Conflicts of Interest

The Board follows RBS Group's guidance relating to directors' conflicts of interest.

The Board has the power to authorise any actual or potential conflicts of interest in accordance with the Companies Act 2006 and NWM Plc's Articles of Association. The company maintains a register of directors' interests and appointments and there is discussion of directors' conflicts in Board meetings, as required. During the year, none of the directors declared any material interest, directly or indirectly, in any contract of significance with any company within RBS Group.

All directors were reminded of their obligations in respect of transacting in NWM Plc securities (Personal Account Dealing) and all directors have confirmed that they have complied with their obligations.

Board Committees

In order to provide effective oversight and leadership, the Board has established a number of Board committees with particular responsibilities:

The Audit Committee comprises at least two independent non-executive directors, one of whom is the Chairman of the Board Risk Committee. The Committee assists the Board in discharging its responsibilities for monitoring the integrity of the financial statements. It reviews the accounting policies, financial reporting and regulatory compliance practices of NWM Plc, its system and standards of internal controls, and monitors the processes for internal audit and external audit.

The Board Risk Committee comprises at least two independent non-executive directors, one of whom is the Chairman of the Audit Committee. The Committee provides oversight and advice to the Board in relation to current and potential future risk exposures and future risk profile, including determination of risk appetite, the effectiveness of the risk management framework and (in conjunction with the Audit Committee) internal controls required to manage risk. The Committee also reviews compliance with RBS Group Policy Framework and reviews the performance of NWM Plc relative to risk appetite.

The Performance & Remuneration Committee (RemCo) comprises at least four independent non-executive directors and assists RBS Group Performance & Remuneration Committee with the oversight and implementation of RBS Group's remuneration policy. It also considers and makes recommendations on remuneration arrangements for senior executives of NWM Plc.

The Nominations Committee comprises the Chairman and at least two other independent non-executive directors. It is responsible for assisting the Board in the formal selection and appointment of directors. It reviews the structure, size and composition of the Board and membership and chairmanship of Board committees.

Report of the directors

4. Opportunity and risk

The role of the Board is to promote the long-term sustainable success of NWM Plc.

The Board reviews and approves risk appetite for strategic and material risks in accordance with the RBS Group risk appetite framework; monitors performance against risk appetite for NWM Plc; and considers any material risks and approves (as appropriate) recommended actions escalated by the NWM Plc Board Risk Committee.

NWM Plc's risk strategy is informed and shaped by an understanding of the risk landscape including a range of significant risks and uncertainties in the external economic, political and regulatory environments.

NWM Plc complies with RBS Group's risk appetite framework, which is approved annually by the RBSG plc Board, in line with RBS Group's risk appetite statements, frameworks and policies. RBS Group risk appetite is set in line with overall strategy.

RBS Group operates an integrated risk management framework, which is centred on the embedding of a strong risk culture. The framework ensures the tools and capability are in place to facilitate sound risk management and decision-making across the organisation.

During 2019, a number of enhancements to the risk management framework were developed. The increasing significance of climate risk was considered as part of these developments and will be fully integrated as part of the implementation of the enhanced framework in 2020.

NWM Plc also complies with the RBS Group Policy Framework, the purpose of which is to ensure that RBS Group establishes and maintains RBS Group-wide policies that adequately address the material inherent risks it faces in its business activities.

Further information on the NWM Plc's risk management framework including risk culture, risk governance, risk appetite, risk controls and limits, and risk identification and measurement can be found in the capital and risk management section of this report.

5. Remuneration

RBS Group Remuneration Policy provides a consistent policy across all companies in RBS Group and ensures compliance with regulatory requirements. The policy is aligned with the business strategy, objectives, values and long-term interests of the company. The policy supports a culture where individuals are rewarded for delivering sustained performance in line with risk appetite and for demonstrating the right conduct and behaviours.

The Performance & Remuneration Committee (RemCo) reviews remuneration for executives of the company and considers reports on the wider workforce including annual pay outcomes and diversity information. The RemCo helps to ensure that the remuneration policies, procedures and practices being applied are appropriate at a NWM Plc level.

Executive remuneration structures incentivise individuals to deliver sustainable performance based on strategic objectives for RBS Group and the relevant business area. Performance is assessed against a balanced scorecard of financial and non-financial measures and variable pay is subject to deferral as well as malus and clawback provisions to ensure rewards are justified in the long-term.

The approach to performance management provides clarity for employees on how their contribution links to RBS Group's ambition and all employees have goals set across a balanced scorecard of measures. RBS Group continues to ensure employees are paid fairly for the work they do and are supported by simple and transparent pay structures in line with industry best practices. This clarity and certainty on how pay is delivered is also helping to improve employees' financial wellbeing, which is a priority. Employees are provided with flexibility in terms of how they wish to receive pay to suit their circumstances. Pay is benchmarked against the external market so that pay and benefits are competitive. RBS Group is a fully accredited Living Wage Employer in the UK with rates of pay that continue to exceed the Living Wage Foundation Benchmarks.

RBS Group ensures colleagues have a common awareness of the financial and economic factors affecting its performance through quarterly "Results Explained" communications and Workplace Live events with the Group Chief Executive Officer and Chief Financial Officer.

Further information on the remuneration policy can be found in the Directors' Remuneration Report (DRR) of the RBSG plc Annual Report & Accounts along with the steps being taken to build an inclusive and engaged workforce. The DRR also contains details of pay ratios for RBS Group. Gender and Ethnicity Pay Gap information can be found in the Strategic Report section of the RBSG plc Annual Report & Accounts.

6. Stakeholder relationships and engagement

NWM Plc is committed to managing the wider social, environmental and economic impacts of its operations which includes the way it deals with its customers and manages the sustainability of its supply chain.

The Board recognises the importance of engaging with stakeholders and discussions at Board meetings are focused around the impact that NWM Plc's activities may have on key stakeholder groups. A new Board reporting format has also been introduced and incorporates specific focus on the stakeholder impacts to support decision-making.

For further details on the Board's engagement with employees, customers, suppliers and others, and how these stakeholders' interests have influenced one of the Board's principal decisions, see pages 15 and 16 of the Strategic Report which includes a section 172(1) statement.

Internal control over financial reporting

The internal controls over financial reporting for NWM Group are consistent with those at RBS Group level. NWM Group has designed and assessed the effectiveness of its internal control over financial reporting as of 31 December 2019 based on the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in the 2013 publication of 'Internal Control – Integrated Framework'. As part of the assessment, management have considered the additional activities required for its internal control over financial reporting during the year, such as oversight on controls performed on NWM Group's behalf, to better reflect the size, scale and overall materiality of the business profile compared to the RBS Group framework. Any deficiencies identified are reported to NWM Group Audit Committee along with management's remediation plans.

Directors' interests

Where directors of NWM Plc are also directors of RBSG plc, their interests in the shares of the ultimate holding company at 31 December 2019 are shown in the Annual report on remuneration section of the 2019 Annual Report and Accounts of RBSG plc. None of the directors held an interest in the loan capital of the ultimate holding company or in the shares or loan capital of NWM Plc or any of its subsidiaries, during the period from 1 January 2019 to 13 February 2020.

Directors' indemnities

In terms of section 236 of the Companies Act 2006 (the "Companies Act"), Qualifying Third Party Indemnity Provisions have been issued by the ultimate holding company to its directors, members of NWM Plc's Executive Committee, individuals authorised by the PRA/FCA and certain directors and/or officers of RBS Group's subsidiaries and all trustees of RBS Group's pension scheme.

Report of the directors

Going concern

NWM Plc's business activities and financial position, the factors likely to affect its future development and performance and its objectives and policies in managing the financial risks to which it is exposed, and its capital are discussed in the Business review. NWM Plc's regulatory capital resources and significant developments in 2019, and anticipated future developments are detailed in the Capital, liquidity and funding sections. These sections also describe NWM Plc's funding and liquidity profile, including changes in key metrics and the build-up of liquidity reserves.

Having reviewed NWM Plc's forecasts, projections and other relevant evidence, the directors have a reasonable expectation that NWM Plc will continue in operational existence for the foreseeable future. Accordingly, the financial statements of NWM Plc have been prepared on a going concern basis.

Political donations

During 2019, no political donations were made in the UK or EU, nor any political expenditure incurred in the UK or EU.

Directors' disclosure to auditors

Each of the directors at the date of approval of this report confirms that:

- (a) so far as the director is aware, there is no relevant audit information of which NWM Plc's auditors are unaware; and
- (b) the director has taken all the steps that he/she ought to have taken as a director to make himself/herself aware of any relevant audit information and to establish that NWM Plc's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act.

Auditors

Ernst & Young LLP (EY LLP) are the auditors and have indicated their willingness to continue in office. A resolution to re-appoint EY LLP as NWM Plc's auditors will be proposed at the forthcoming Annual General Meeting.

By order of the Board

Scott Gibson
Company Secretary
13 February 2020

NatWest Markets Plc
is registered in Scotland No. SC90312

Statement of directors' responsibilities

This statement should be read in conjunction with the responsibilities of the auditor set out in their report on pages 70 to 77.

The directors are responsible for the preparation of the Annual Report and Accounts. The directors are required by Article 4 of the IAS Regulation (European Commission Regulation No 1606/2002) to prepare Group accounts, and as permitted by the Companies Act 2006 have elected to prepare company accounts, for each financial year in accordance with International Financial Reporting Standards as adopted by the European Union. They are responsible for preparing accounts that present fairly the financial position, financial performance and cash flows of NWM Group and NWM Plc. In preparing those accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent; and
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of NWM Group and to enable them to ensure that the Annual Report and Accounts complies with the Companies Act 2006. They are also responsible for safeguarding the assets of NWM Plc and NWM Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with International Financial Reporting Standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of NWM Plc and the undertakings included in the consolidation taken as a whole; and
- the Strategic Report and Directors' report (incorporating the Financial review) includes a fair review of the development and performance of the business and the position of NWM Plc and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

By order of the Board

Frank Dangeard
Chairman

Robert Begbie
Interim Chief Executive Officer

13 February 2020

Board of directors
Chairman
Frank Dangeard

Executive directors
Robert Begbie

Non-executive directors
Vivek Ahuja
Brendan Nelson
Tamsin Rowe
Sarah Wilkinson

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Independent auditor's report to the members of NatWest Markets Plc

Opinion

We have audited the financial statements (see table below) of NatWest Markets Plc (the Bank) and its subsidiaries (together, the 'Group') for the year ended 31 December 2019. In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the Bank's affairs as at 31 December 2019 and of the Group's loss for the year then ended;
- the financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the Bank financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements of NatWest Markets Plc which comprise:

Group	Bank
• Consolidated balance sheet as at 31 December 2019; • Consolidated income statement for the year then ended; • Consolidated statement of comprehensive income for the year then ended; • Consolidated statement of changes in equity for the year then ended; • Consolidated cash flow statement for the year then ended; • Accounting Policies; • Related notes 1 to 37 to the financial statements; and • Capital and risk management section of the Strategic report identified as 'audited'.	• Balance sheet as at 31 December 2019; • Statement of changes in equity for the year then ended; • Cash flow statement for the year then ended; and • Related notes 1 to 37 to the financial statements which refer to the Bank.

The financial reporting framework that has been applied in their preparation is applicable law and IFRSs as adopted by the European Union and, as regards the Bank's financial statements, as applied in accordance with the provisions of the Companies Act 2006.

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 below. We are independent of the Group and Bank in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's Ethical Standard as applied to listed public interest entities, 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 relation to the ISA's (UK) which require us to report to you, we have nothing to report in respect of the following matters:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Group's or the Bank's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Separate opinion in relation to IFRSs as issued by the IASB

As explained in the accounting policies, in addition to complying with its legal obligation to apply IFRSs as adopted by the European Union, the Group has applied IFRSs as issued by the International Accounting Standards Board (IASB). In our opinion the Group financial statements comply with IFRS's as issued by the IASB.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in our opinion thereon, and we do not provide a separate opinion on these matters.

Independent auditor's report to the members of NatWest Markets Plc

Risk	Our response to the risk
Valuation of financial instruments with higher risk characteristics including related income from trading activities At 31 December 2019 the Group reported level 3 assets of £2.5 billion (2018: £3.3 billion) and level 3 liabilities of £1.4 billion (2018: £2.1 billion). The valuation of financial instruments with higher risk characteristics involves both significant judgement and the risk of inappropriate revenue recognition through incorrect pricing as outlined in the bullets below. The judgement in estimating fair value of these instruments can involve complex valuation models and significant fair value adjustments, both of which may be reliant on data inputs where there is limited market observability. Management's estimates which required significant auditor judgement include: • Complex model-dependent valuations, which include interest rate swaps linked to pre-payment behaviour and interest rate and foreign exchange options with exotic features such as those having multiple call dates and variable notional amounts; • Pricing inputs and calibrations for illiquid instruments, including rarely traded debt securities. Additionally, derivative instruments whose valuation is dependent upon discount rates associated with complex collateral arrangements are complex; • Certain fair value adjustments made to derivatives including Funding Valuation Adjustments (FVA) and Credit Valuation Adjustments (CVA) relating to derivative counterparties whose credit spread is less readily able to be determined, and material product and deal specific adjustments on long dated derivative portfolios.	We evaluated the design and operating effectiveness of controls relating to financial instrument valuation and related measurement including independent price verification, model review and approval, collateral management, and income statement analysis and reporting. Among other procedures, we involved our financial instrument valuation and modelling specialists to assist us in performing procedures including the following: • Testing complex model-dependent valuations by performing independent calculations to assess the appropriateness of models and the adequacy of assumptions and inputs used by the Group; • Independently re-pricing instruments that had been valued using illiquid pricing inputs, using alternative pricing sources to evaluate management's valuation; and • Comparing the methodology used for fair value adjustments to current market practice. We re-valued a sample of counterparty level FVA and CVAs, compared funding spreads to third party data and independently challenged illiquid CVA inputs. Where differences between our independent valuation and management's valuation were outside our thresholds, we performed additional testing over each variance to assess the appropriateness of the valuation of financial instruments with higher risk characteristics including related income from trading activities. We also performed back-testing analysis of recent trade activity to evaluate the drivers of significant differences between book value and trade value and to assess the impact on the fair value of similar instruments within the portfolio. We considered the implications of changes to the business on the valuation of financial instruments in accordance with the relevant accounting standards.
Key observations communicated to the Group Audit Committee	
We are satisfied that the assumptions used by management to reflect the fair value of financial instruments with higher risk characteristics and the recognition of related income is reasonable and in accordance with IFRS. We highlighted the following matters to the Audit Committee: • Complex-model dependent valuations were appropriate based on the output of our independent re-valuations, analysis of trade activity and peer benchmarking; • The fair value estimates of hard-to-price portfolios appropriately reflected pricing information available at 31 December 2019; and • Valuation adjustments applied on derivative portfolios for credit, funding and other risks were appropriate based on our assessment of trade activity for positions with common risk characteristics, analysis of market data and peer benchmarking.	
Relevant references in the Annual Report and Accounts	
Accounting policies Note 12 on the financial statements	

Independent auditor's report to the members of NatWest Markets Plc

Risk	Our response to the risk
Provisions for conduct, litigation and regulatory matters, customer remediation and claims At 31 December 2019, the Group has reported £0.3 billion (2018: £0.7 billion) of provisions for litigation and other regulatory provisions, as detailed in Note 21 of the financial statements. The continued litigious environment and heightened regulatory scrutiny give rise to a high level of management judgement in determining appropriate provisions and disclosures. Management judgement is needed to determine whether a present obligation existed, and a provision should be recorded at 31 December 2019 in accordance with the accounting criteria set out under IAS 37. The most significant areas of judgement are: • Auditing the adequacy of these provisions is complex because judgement is involved in the selection and use of assumptions in the estimation of material provisions and there is a risk of management bias in the determination of whether an outflow in respect of identified material conduct or legal matters is probable and can be estimated reliably; and • Judgement is required to assess the adequacy of disclosures of provision for contingent liabilities given the underlying estimation uncertainty in the provisions.	We evaluated the design and operating effectiveness of key controls over the identification, estimation, monitoring and disclosure of provisions considering the potential for management override of controls. The controls tested included those designed and operated by management to identify and monitor claims, and to ensure the completeness and accuracy of data used to estimate provisions. Among other procedures, we examined the relevant regulatory and legal correspondence to assess developments in certain cases. For the cases which were settled during the period, we compared the actual outflows with the provision that had been recorded, considered whether further risk existed. For the significant provisions made we understood, assessed the provisioning methodology. For example, we tested the underlying data and assumptions used in the determination of the provisions recorded, legal costs, and the timing of settlement. We considered the accuracy of management's historical estimates and peer bank settlement in similar cases by comparing the actual settlement to the provision. For significant legal matters, we received confirmations from the Group's external legal counsel for key matters to evaluate the existence of the obligation and management's estimate of the outflow at year-end. We assessed management's conclusion by evaluating the underlying information used in estimating the provisions including consideration of alternate sources. We also conducted inquiries with internal legal counsel over the existence of the legal obligations and related provision. We performed a test for unrecorded provisions to determine if there were any cases not considered in the provision estimate by assessing against external legal confirmations and discussing with internal counsel. We evaluated the disclosures provided on contingent liabilities and provisions for litigation and other regulatory provisions to assess whether they complied with accounting standards.
Key observations communicated to the Audit Committee	
We are satisfied that the provision for litigation and other regulatory provisions is reasonable and recognised in accordance with IFRS. We concurred with the level of disclosure in the financial statements. We did not identify any material unrecorded provisions.	
Relevant references in the Annual Report and Accounts	
Accounting policies Notes 21 and 28 on the financial statements	

Independent auditor's report to the members of NatWest Markets Plc

Risk

Our response to the risk

Impairment of loans

At 31 December 2019 the Group reported total gross loans of £10.3 billion (2018: £11.8 billion) and £146 million of expected credit loss provisions under IFRS 9 (2018: £108 million), which includes an overlay of £4 million for economic uncertainty.

Management's judgements and estimates which are especially subjective to audit due to significant uncertainty associated with the assumptions used in the estimation in respect of the timing and measurement of expected credit losses (ECL) include:

- Allocation of assets to stage 1, 2, or 3 using criteria in accordance with the accounting standard;
- Accounting interpretations, modelling assumptions and data used to build and run the models that calculate the ECL;
- Inputs and assumptions used to estimate the impact of multiple economic scenarios;
- Completeness and valuation of post model adjustments; and;
- Measurements of individual provisions including the assessment of multiple scenarios;

We also considered the complexity of the process to design and create financial statement disclosures given their granularity and complexity.

We evaluated the design and operating effectiveness of controls across the processes relevant to ECL, including the judgements and estimates noted, involving specialists to assist us in performing our procedures where appropriate. These controls, among others, included controls over the allocation of assets into stages including management's monitoring of stage effectiveness, model monitoring including the need for post model adjustments, model validation, data accuracy and completeness, credit monitoring, and application of multiple economic scenarios, individual provisions and production of journal entries and disclosures.

Among other procedures, we observed the Group Provisions Committee meetings where the inputs, assumptions and adjustments to the ECL were discussed and approved.

We performed an overall assessment of the ECL provision levels by stage to determine if they were reasonable by considering the overall credit quality of the Group's portfolios, risk profile, credit risk management practices and the macroeconomic environment by considering trends in the economy and industries to which the Group is exposed.

We evaluated the criteria used to allocate a financial asset to stage 1, 2 or 3 in accordance with IFRS 9; this included peer benchmarking to assess staging levels. We recalculated the assets in stage 1, 2 and 3 to assess if they were allocated to the appropriate stage and performed sensitivity analysis to assess the impact of different criteria on the ECL.

We involved modelling specialists to assist us to test the assumptions, inputs and formulae used in a sample of ECL models. This included assessing the appropriateness of model design and formulae used, alternative modelling techniques, refinements made to models in the second year of IFRS 9, and recalculating the Probability of Default, Loss Given Default and Exposure at Default, and model implementation for a sample of models.

To evaluate data quality, we agreed ECL calculation data points to source systems. To test credit monitoring, we recalculated the risk ratings for a sample of performing loans.

We involved economic specialists to assist us to evaluate the base case and alternative economic scenarios, including evaluating probability weights and comparing to other scenarios from a variety of external sources, as well as EY internally developed forecasts. This included assessing whether forecasted macroeconomic variables were appropriate, such as GDP, unemployment rate and interest rates. With the support of our modelling specialists we assessed the correlation and the overall impact of the macroeconomic factors to the ECL.

We assessed the completeness and appropriateness of post model adjustments and recalculated a sample. Based on current economic conditions and market circumstances, we considered the need for sector or systemic adjustments. We assessed the scenarios used and calculation of the overlay in response to economic uncertainty.

We recalculated a sample of individual provisions including the alternative scenarios and evaluating probability weights assigned. The sample was based on a number of factors, including higher risk sectors and materiality.

We assessed the adequacy of disclosures for compliance with the accounting standards and regulatory considerations.

Key observations communicated to the Group Audit Committee

We are satisfied that provisions for the impairment of loans were reasonable and recognised in accordance with IFRS 9. We highlighted the following matters to the Audit Committee:

- Our testing and sensitivity analysis on the staging criteria did not identify material differences and overall, we concluded that the stage allocation at 31 December 2019 was reasonable;
- Our testing of models and model assumptions did not highlight material differences; and
- Our testing of individually assessed impairments did not highlight any material differences

Relevant references in the Annual Report and Accounts

Credit Risk section of the Capital and risk management section

Accounting policies

Note 14 on the financial statements

Independent auditor's report to the members of NatWest Markets Plc

Risk	Our response to the risk
IT systems and controls impacting financial reporting	
The IT environment is complex and pervasive to the operations of the Group due to the large volume of transactions processed in numerous locations daily and the reliance on automated and IT dependent manual controls. Appropriate IT controls are required to ensure that applications process data as expected and that changes are made in an appropriate manner. This risk is also impacted by the greater dependency on third-parties, increasing use of cloud platforms, decommissioning of legacy systems, and migration to new systems. Such controls contribute to mitigating the risk of potential fraud or errors as a result of changes to applications and data. Our audit approach relies upon IT applications and the related control environment including: • User access management across application, database and operating systems; • Changes to the IT environment, including transformation that changes the IT landscape including the general ledger and human resource system migrations; • IT operational controls; • IT application or IT dependent controls; and • Evaluation of IT control environment at third party service providers.	We evaluated the design and operating effectiveness of IT controls over the applications, operating systems and databases that are relevant to financial reporting. We assessed automated controls within business processes and the reliability of relevant reports used as part of a manual control. This included assessing the integrity of system interfaces, the completeness and accuracy of data feeds, automated calculations and specific input controls. We tested system migrations and related technology changes (including where relevant new systems) resulting from transformation programmes that were material to financial statement reporting. This included verifying the completeness of information transferred to new systems as well as testing the controls in place for both the migration and the new system. We tested user access by assessing the controls in place for in-scope applications and verifying the addition and removal of users. We identified an increasing number of systems outsourced to third party service providers. For these systems, we tested IT general controls through evaluating the relevant Service Organisation Controls reports produced by third parties by assessing the timing of the reporting and the controls tested. We also tested required complementary controls performed by management. Where control deficiencies were identified, we tested remediation activities performed by management and compensating controls in place and assessed where necessary to mitigate any residual risk.

Key observations communicated to the Audit Committee

We are satisfied that IT controls impacting financial reporting are designed and operating effectively. The following matters were reported to the Audit Committee:

- Improvements were made to user access management controls. Control deficiencies previously identified around access management, were remediated by year end or mitigated by compensating controls. We also performed additional testing in response to deficiencies identified, where required;
- Where IT transformation or change occurred within the year, particularly around outsourcing and the use of third parties, we updated our audit approach accordingly and tested relevant controls. Where we identified control deficiencies these were remediated by year end or mitigated by compensating controls; and
- As the Group continues to increase the use of third, and 4th parties, (including cloud service providers), focus on the identification of and accountability for, internal controls over financial reporting, will be essential.

In the prior year, our auditor's report included key audit matters in relation to the financial impact of structural reform as it was the year of implementation and restructuring provisions. We did not consider these to be key audit matters in the current year

An overview of the scope of our audit

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each component of the Group. Taken together, this enables us to form an opinion on the financial statements. We take into account the size and risk profile of each component and its activities, the organisation of the Group and effectiveness of Group-wide controls, changes in the business environment and other factors such as recent internal audit results when assessing the level of work to be performed at each component.

Our audit covers the reportable segments identified in the financial statements. This incorporates the NatWest Markets segment, with key locations in the United Kingdom, United States and the Netherlands and the Central items & Other segment.

In assessing the risk of material misstatement to the Group financial statements, and to ensure we had adequate quantitative coverage of significant accounts in the financial statements we identified two full scope reporting components of the Group, being NatWest Markets primary audit engagement team and United States. There are three specific scope components, Services, Credit and Pensions & Remuneration and one specified procedures component, Switzerland.

The table below illustrates the coverage obtained from the work performed by our audit teams. As the Group has historically made losses and several operations were moved to discontinued operations, we considered total assets, total equity and the absolute value of the amounts in the income statement (meaning the magnitude of the amounts without regard to their positive or negative value) to verify we had appropriate overall coverage on the income statement.

	Full scope (1)	Specific scope (2)	Other procedures (3)	Total
Total assets	100%	0%	0%	100%
Total equity	97%	3%	0%	100%
Absolute value of the income statement	80%	20%	0%	100%

Notes:

(1) Full scope: audit procedures on all significant accounts.

(2) Specific scope: audit procedures on selected accounts.

(3) Other procedures: considered in analytical procedures.

Independent auditor's report to the members of NatWest Markets Plc

Changes from the prior year

In 2018 the UK Personal & Business Banking, Commercial Banking and RBS Group Treasury components were included as full scope components due to their contribution to discontinued operations during the year.

Involvement with component teams

In establishing our overall approach to the Group audit, we determined the type of work that needed to be undertaken in each of the components by us, as the primary audit engagement team, or by component auditors in the United Kingdom or from other EY global network firms operating under our instruction.

The primary audit engagement team interacted regularly with the component audit teams where appropriate throughout the course of the audit, which included holding planning meetings, maintaining regular communications on the status of the audits, reviewing key working papers and taking responsibility for the scope and direction of the audit process. The primary audit engagement team also participated in meetings with key management personnel in the components and, for certain overseas locations, implemented a programme of planned visits. These visits involved discussing the audit approach with the component team and any issues arising from their work, as well as meeting with local management. This, together with the additional procedures performed at Group level, gave us appropriate evidence for our opinion on the Group financial statements.

Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality

The magnitude of omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the Group and Bank to be £96 million (2018 materiality: £90 million), which is 1% of equity of the Bank.

Performance materiality

The application of materiality at the individual account or balance level is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality should be set at 50% of our materiality (2018: 50%), namely £48 million (2018: £45 million). We have set performance materiality at this percentage based on various considerations including the past history of misstatements, the effectiveness of the control environment and other factors affecting the entity and its financial reporting.

Audit work of component teams for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component team is based on the relative scale and risk of the component to the Group as a whole and our assessment of the risk of misstatement at that component. In the current year, the range of performance materiality allocated by the primary audit engagement team to components was between £48 million and £18 million.

Reporting threshold

An amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all corrected and uncorrected audit misstatements in excess of £5 million (2018: £4 million), which is 5% of materiality, as well as misstatements below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Other information

The other information comprises the information included in the Annual Report and Accounts, including the Strategic Report, Report of the Directors, Statement of Directors' Responsibilities, Risk Factors and Forward-looking statements, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information. 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.

In connection with our audit of the financial statements, 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 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 or a material misstatement of the other information. 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.

Independent auditor's report to the members of NatWest Markets Plc

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, the part of the directors' remuneration disclosure to be audited has been properly prepared in accordance with the Companies Act 2006.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Report of the Directors for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Report of the Directors have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In light of the knowledge and understanding of the Group and the Bank and its environment obtained in the course of the audit, we have not identified material misstatements in the Strategic report or the Report of the directors.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the Group, or returns adequate for our audit have not been received from branches not visited by us; or
- the Bank financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; 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, 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 the implementation of 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 and Bank'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 the Bank 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

The objectives of our audit, in respect to fraud, are; to identify and assess the risks of material misstatement of the financial statements due to fraud; to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud, through designing and implementing appropriate responses; and to respond appropriately to fraud or suspected fraud identified during the audit. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management.

We obtained an understanding of the legal and regulatory frameworks that are applicable to the Group and have a direct impact on the preparation of the financial statements. We determined that the most significant are:

- Companies Act 2006
- Financial Reporting Council (FRC) and the UK Corporate Governance Code
- Tax Legislation (governed by HM Revenue and Customs)

We understood how the Group is complying with those frameworks by reviewing the RBS Policy Framework, holding discussions with the Group's general counsel and internal audit, amongst others. We inquired as to any known instances of non-compliance or suspected non-compliance with laws and regulations. We also reviewed RBS Group's Complaints Management Policy and Whistleblowing Policy. We assessed the susceptibility of the Group's financial statements to material misstatement, including how fraud might occur by holding discussions with senior management, including the Chief Executive, Chief Financial Officer, Chief Risk Officer, Head of Internal Audit and Audit Committee Chairman. We also reviewed the Group's fraud-related policies and mandates of different governance forums assessing fraud. Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved inquiring of key management, reviewing the key policies and reports on the aforementioned regulatory frameworks as well as reviewing the correspondence exchanged with the Regulators.

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.

Independent auditor's report to the members of NatWest Markets Plc

Other matters we are required to address

- Following the recommendation of the RBS Group Audit Committee we were appointed by the RBS Group at its annual general meeting on 4 May 2016 to audit the financial statements of the RBS Group and its major subsidiaries for the period ending 31 December 2016 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments is 4 years, covering periods from our appointment through 31 December 2019.
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Bank and we remain independent of the Group and the Bank in conducting the audit.
- The audit opinion is consistent with the additional report to the Audit Committee

Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. 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.

Simon Ludlam (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London, United Kingdom
13 February 2020

Notes:

- (1) The maintenance and integrity of the RBS Group 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 United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Consolidated income statement for the year ended 31 December 2019

	Note	2019 £m	2018 £m
Interest receivable		697	406
Interest payable		(847)	(673)
Net interest income	1	(150)	(267)
Fees and commissions receivable		324	260
Fees and commissions payable		(337)	(233)
Income from trading activities		805	1,045
Gain on redemption of own debt		—	101
Other operating income		77	(48)
Non-interest income	2	869	1,125
Total income		719	858
Staff costs		(691)	(579)
Premises and equipment		(111)	(120)
Other administrative expenses		(177)	(1,524)
Depreciation and amortisation		(18)	(14)
Operating expenses	3	(997)	(2,237)
Loss before impairment releases		(278)	(1,379)
Impairment releases	14	48	102
Operating loss before tax		(230)	(1,277)
Tax credit	7	109	33
Loss from continuing operations		(121)	(1,244)
Profit from discontinued operations, net of tax	22	—	2,461
(Loss)/profit for the year		(121)	1,217
Attributable to:			
Ordinary shareholders		(181)	1,241
Paid-in equity holders		60	—
Non- controlling interests		—	(24)
		(121)	1,217

Consolidated statement of comprehensive income for the year ended 31 December 2019

	Note	2019 £m	2018 £m
(Loss)/profit for the year		(121)	1,217
Items that do not qualify for reclassification			
Remeasurement of retirement benefit schemes	5		
- contributions in preparation for ring-fencing (1)		—	(2,053)
- other movements		(50)	(2)
(Loss)/profit on fair value of credit in financial liabilities designated at fair value through profit or loss due to own credit risk		(13)	121
FVOCI financial assets		(122)	100
Tax		32	492
		(153)	(1,342)
Items that do qualify for reclassification			
FVOCI financial assets		5	(386)
Cash flow hedges		28	(125)
Currency translation		(152)	(723)
Tax		(4)	131
		(123)	(1,103)
Other comprehensive loss after tax		(276)	(2,445)
Total comprehensive loss for the year		(397)	(1,228)
Attributable to:			
Ordinary shareholders		(458)	(1,205)
Paid-in equity holders		60	—
Non-controlling interests		1	(23)
		(397)	(1,228)

Notes:

- (1) On 17 April 2018 RBS Group agreed a Memorandum of Understanding (MoU) with the Trustees of the RBS Group Pension Fund in connection with the requirements of ring-fencing. NWM Plc could not continue to be a participant in the Main section and separate arrangements were required for its employees. Under the MoU, NWM Plc made a contribution of £2 billion on 9 October 2018 to strengthen funding of the Main section in recognition of the changes in covenant; this is within discontinued operations in NWM Group's results. Also under the MoU, NWM Plc made a £53 million contribution to the NWM section in Q1 2019; this is within continuing operations within the NWM Group results.
- (2) A profit of nil (2018 – profit £2,458 million) from discontinued operations was attributable to ordinary and equity preference shareholders.

The accompanying notes on pages 88 to 142, the accounting policies on pages 83 to 87 and the audited sections of the Financial review: Capital and risk management on pages 22 to 63 form an integral part of these financial statements.

Balance sheet as at 31 December 2019

		NWM Group		NWM Plc	
	Note	2019 £m	2018 £m	2019 £m	2018 £m
Assets					
Cash and balances at central banks	11	12,729	11,188	9,953	11,095
Trading assets	9	76,540	74,972	57,768	61,990
Derivatives	10	148,696	134,250	147,458	134,291
Settlement balances	11	4,339	2,705	3,353	1,421
Loans to banks - amortised cost	11	1,088	626	238	454
Loans to customers - amortised cost	11	8,361	8,366	6,910	7,908
Amounts due from holding company and fellow subsidiaries	11	1,231	3,398	7,145	11,800
Other financial assets	17	12,305	11,268	11,636	10,995
Investment in group undertakings	15	—	—	2,905	1,151
Other assets	18	847	1,108	687	936
Total assets		266,136	247,881	248,053	242,041
Liabilities					
Bank deposits	11	2,089	2,749	2,038	2,777
Customer deposits	11	3,703	2,580	2,247	2,390
Amounts due to holding company and fellow subsidiaries	11	8,300	10,161	16,858	23,505
Settlement balances	11	4,022	2,914	2,648	1,977
Trading liabilities	9	73,836	72,289	53,576	54,540
Derivatives	10	144,142	129,914	142,390	129,974
Other financial liabilities	19	18,445	16,279	17,470	16,279
Other liabilities	21	1,689	1,906	1,195	1,677
Total liabilities		256,226	238,792	238,422	233,119
Owners' equity	23	9,907	9,087	9,631	8,922
Non-controlling interests		3	2	—	—
Total equity		9,910	9,089	9,631	8,922
Total liabilities and equity		266,136	247,881	248,053	242,041

Owners' equity of NWM Plc as at 31 December 2019 includes the loss for the year of £269 million (2018 loss - £305 million).

The accompanying notes on pages 88 to 142, the accounting policies on pages 83 to 87 and the audited sections of the Financial review: Capital and risk management on pages 22 to 63 form an integral part of these financial statements.

The accounts were approved by the Board of directors on 13 February 2020 and signed on its behalf by:

Frank Dangeard
Chairman

Robert Begbie
Interim Chief Executive Officer

NatWest Markets Plc
Registration No. SC90312

Statement of changes in equity for the year ended 31 December 2019

	NWM Group		NWM Plc	
	2019 £m	2018 £m	2019 £m	2018 £m
Called-up share capital - at 1 January	400	6,609	400	6,609
Court approved distribution (1)	—	(6,209)	—	(6,209)
At 31 December	400	400	400	400
Share premium account - at 1 January	1,759	26,807	1,759	26,807
Court approved distribution (1)	—	(27,692)	—	(27,692)
Redemption of debt preference shares (2)	—	2,644	—	2,644
At 31 December	1,759	1,759	1,759	1,759
Paid-in equity - at 1 January	749	—	749	—
Securities issued during the year	155	749	155	749
At 31 December	904	749	904	749
Merger reserve - at 1 January	—	10,881	—	—
Transfer to retained earnings on disposal of subsidiary (3)	—	(10,881)	—	—
At 31 December	—	—	—	—
FVOCI reserve - at 1 January	134	300	38	280
Implementation of IFRS 9 on 1 January 2018	—	30	—	(15)
Unrealised (losses)/gains	(126)	141	(177)	159
Realised gains	(151)	(427)	(19)	(16)
Tax	9	90	9	(34)
Recycled on transfer to fellow subsidiary	—	—	—	—
- gross	—	—	—	(460)
- tax	—	—	—	124
At 31 December	(134)	134	(149)	38
Cash flow hedging reserve - at 1 January	114	205	114	(49)
Amount recognised in equity (4)	98	(316)	98	(109)
Amount transferred from equity to earnings (5)	(70)	(264)	(70)	(127)
Tax	(5)	34	(5)	(60)
Recycled on transfer to fellow subsidiary	—	455	—	459
At 31 December (6)	137	114	137	114
Foreign exchange reserve - at 1 January	230	953	(136)	(304)
Retranslation of net assets	(180)	(83)	(49)	(38)
Foreign currency gains on hedges of net assets	27	1	3	8
Tax	—	1	—	—
Recycled to profit or loss on disposal of businesses	—	(642)	14	198
At 31 December (6)	77	230	(168)	(136)

Statement of changes in equity for the year ended 31 December 2019

	NWM Group		NWM Plc	
	2019	2018	2019	2018
	£m	£m	£m	£m
Retained earnings - at 1 January	5,701	(10,552)	5,998	11,179
Implementation of IFRS 9 on 1 January 2018	—	(106)	—	261
Implementation of IFRS 16 on 1 January 2019 (7)	(6)	—	(6)	—
(Loss)/profit attributable to ordinary shareholders and paid-in equity holders				
- continuing operations	(121)	(1,217)	(269)	(359)
- discontinued operations	—	2,458	—	54
Ordinary dividends paid	(500)	(2,550)	(500)	(2,550)
Paid-in equity dividends paid	(60)	—	(60)	—
Court approved distribution (1)	—	10,848	—	—
Capital contribution (10)	1,845	—	1,845	—
Transfer from merger reserve on disposal of subsidiary (3)	—	10,881	—	—
Realised gains on FVOCI equity shares	160	12	52	9
Remeasurement of retirement benefit schemes				
- contributions in preparation for ring-fencing (8)	—	(2,053)	—	(53)
- other movements	(50)	(2)	(49)	(9)
- tax	4	531	4	15
Changes in fair value of credit in financial liabilities designated at fair value through profit				
- gross	(13)	121	(71)	121
- tax	20	(33)	20	(33)
Redemption of debt preference shares (2)	—	(2,644)	—	(2,644)
Shares issued under employee share schemes	—	(2)	—	(2)
Share-based payments (9)	(216)	9	(216)	9
At 31 December	6,764	5,701	6,748	5,998
Owners' equity at 31 December	9,907	9,087	9,631	8,922
Non-controlling interests - at 1 January	2	57	—	—
Currency translation adjustments and other movements	1	1	—	—
(Loss)/profit attributable to non-controlling interests				
- continuing operations	—	(27)	—	—
- discontinued operations	—	3	—	—
Equity withdrawn and disposals	—	(32)	—	—
At 31 December	3	2	—	—
Total equity at 31 December	9,910	9,089	9,631	8,922
Total equity is attributable to:				
Ordinary shareholders	9,003	8,338	8,727	8,173
Paid-in equity holders	904	749	904	749
Non-controlling interests	3	2	—	—
	9,910	9,089	9,631	8,922

Notes:

- (1) On 29 June 2018, the Court of Session in Scotland approved the reduction of the capital and cancellation of the share premium account and capital redemption reserve (together the "capital reduction") of NWM Plc. As part of the capital reduction, NatWest Holdings Ltd was transferred to RBSG plc with effect from 2 July 2018 thereby creating the legal separation of those RBS Group entities that are within the ring-fenced sub-group from those held outside the ring-fence.
- (2) Issued by NWM Plc to the parent company, RBSG plc, which were redeemed in April 2018 and December 2018.
- (3) On 2 July 2018, the merger reserve was transferred to retained earnings on the transfer of NatWest Holdings Ltd to RBSG.
- (4) Relates to interest rate hedges.
- (5) Relates to interest rate hedges transferred to net interest income.
- (6) The hedging element of the cash flow hedging reserve and foreign exchange reserve relate mainly to de-designated hedges for NWM Group and continuing for NWM Plc.
- (7) Refer to Note 24 for further information on the impact of IFRS 16 implementation.
- (8) On 17 April 2018 RBS Group agreed a Memorandum of Understanding (MoU) with the Trustees of the RBS Group Pension Fund in connection with the requirements of ring-fencing. NWM Plc could not continue to be a participant in the Main section and separate arrangements were required for its employees. Under the MoU, NWM Plc made a contribution of £2 billion on 9 October 2018 to strengthen funding of the Main section in recognition of the changes in covenant; this is within discontinued operations in NWM Group's results. Also under the MoU, NWM Plc made a £53 million contribution to the NWM section in Q1 2019; this is within continuing operations in NWM Group's results.
- (9) Includes adjustments to the allocation of deferred awards following the implementation of ring fencing and the impact of vesting during the year.
- (10) A capital contribution of £1845 million was received from RBSG plc on 29th November 2019 to facilitate the acquisition of RBS Holdings N.V..

The accompanying notes on pages 88 to 142, the accounting policies on pages 83 to 87 and the audited sections of the Financial review: Capital and risk management on 22 to 63 form an integral part of these financial statements.

Cash flow statement for the year ended 31 December 2019

	NWM Group		NWM Plc	
	2019	2018	2019	2018
Note	£m	£m	£m	£m
Cash flows from operating activities				
Operating loss before tax from continuing operations	(230)	(1,277)	(363)	(410)
Profit before tax from discontinued operations	—	2,893	—	71
Interest on subordinated liabilities	(32)	199	(24)	184
Interest on other financial assets	(257)	(92)	(284)	(135)
Interest on MRELS	248	—	248	—
Impairment releases on loans to banks and customers	(7)	(67)	(4)	(53)
(Gain)/loss on sale of subsidiaries and associates	—	(30)	9	(466)
Loss/(gain) on sale of securities	9	(961)	—	—
Defined benefit pension schemes	6	7	3	6
Change in fair value taken to profit or loss of other financial assets	(30)	(2,503)	(41)	(3,467)
Change in fair value taken to profit or loss of subordinated liabilities	—	6,264	—	—
Change in fair value taken to profit or loss of MRELS	123	—	123	—
Provisions: expenditure in excess of charge	10	895	4	361
Depreciation, amortisation and impairment of property, plant, equipment, goodwill and intangibles	12	384	22	140
Gain on sale of property, plant and equipment	—	(22)	—	—
Gain on redemption of own debt	—	(153)	—	(101)
(Gain)/loss on sale of subsidiaries and associates	(18)	—	—	182
Write-down of investments in subsidiaries	—	—	349	192
Elimination of foreign exchange differences	548	(233)	472	(84)
Other non-cash items	(79)	(3,640)	(114)	6,050
Net cash inflow from trading activities	303	1,664	400	2,470
Decrease/(increase) in net loans to banks	424	(8,127)	—	—
Decrease/(increase) in net loans to customers	75	(1,940)	(1,359)	2,622
Decrease/(increase) in trading assets	2,054	8,695	5,111	11,019
Increase in derivative assets	(10,805)	24,297	(13,069)	27,715
Increase in settlement balance assets	(4)	(197)	(1,932)	(435)
Decrease/(increase) in amounts due from holding companies and subsidiaries	1,343	(3,182)	4,286	(5,330)
Decrease/(increase) in other financial assets	603	(673)	917	(580)
Decrease/(increase) in other assets	179	(14,507)	23	118,586
(Decrease)/increase in bank and customer deposits	(240)	1,177	(882)	(1,332)
(Decrease)/increase in amounts due to holding companies and subsidiaries	(5,346)	4,946	(7,352)	3,386
Decrease in trading liabilities	(372)	(9,671)	(1,822)	(9,641)
Increase/(decrease) in derivatives liabilities	10,011	(23,422)	12,416	(25,125)
Increase in settlement balance liabilities	41	98	671	1,334
Increase in other financial liabilities	1,574	4,606	2,048	4,466
(Decrease)/increase in other liabilities	(705)	18,860	(841)	(135,661)
Changes in operating assets and liabilities	(1,168)	960	(1,785)	(8,976)
Income taxes received/(paid)	315	(116)	317	26
Net cash flows from operating activities (1)	(550)	2,508	(1,068)	(6,480)
Cash flows from investing activities				
Sale and maturity of other financial assets	3,905	5,567	(5,422)	(9,112)
Purchase of other financial assets	(4,860)	(9,112)	4,830	5,567
Interest on other financial assets	257	92	284	135
Sale of property, plant and equipment	8	60	—	—
Purchase of property, plant and equipment	(1)	(37)	(1)	—
Net divestment of business interests and intangible assets	29	3,705	1,201	21,745
Net cash flows from investing activities	3,014	(1,883)	892	18,335
Cash flows from financing activities				
Issue of other equity instruments: Additional Tier 1 capital notes	—	749	—	749
Issue of subordinated liabilities	1,047	—	1,015	—
Shares issued under employee share schemes	—	(2)	—	(2)
Non-controlling interests equity withdrawn and disposals	—	(21)	—	—
Redemption of subordinated liabilities	(896)	(3,769)	(896)	(3,769)
Issuance of MRELS	—	5,125	—	5,125
Interest on MRELS	(182)	—	(182)	—
Service cost of other equity instruments	(560)	(2,550)	(560)	(2,550)
Interest on subordinated liabilities	(4)	(238)	17	(223)
Net cash flows from financing activities (2)	(595)	(706)	(606)	(670)
Effects of exchange rate changes on cash and cash equivalents	(953)	525	(835)	332
Net increase in cash and cash equivalents	916	444	(1,617)	11,517
Cash and cash equivalents at 1 January	31	26,127	24,575	13,058
Cash and cash equivalents at 31 December	27,043	26,127	22,958	24,575

The accompanying notes on pages 88 to 142, the accounting policies on pages 83 to 87 and the audited sections of the Financial review: Capital and risk management on pages 22 to 63 form an integral part of these financial statements.

Notes:

- (1) NWM Group includes interest received of £579 million (2018 - £323 million) and interest paid of £840 million (2018 - £586 million), and NWM Plc includes interest received of £730 million (2018 - £428 million) and interest paid of £936 million (2018 - £2,479 million).
- (2) 2018 has been re-presented to align the balance sheet classification. MREL was previously presented in Operating activities and is now presented in Financing activities.

Accounting policies

1. Presentation of accounts

The accounts set out on pages 78 to 142, including these accounting policies on pages 83 to 87 and the audited sections of the Financial review: Capital and risk management on pages 22 to 63, are prepared on a going concern basis (see the Report of the directors, pages 64 to 67) and in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IASB) and interpretations as issued by the IFRS Interpretations Committee of the IASB and adopted by the European Union (EU) (together IFRS). The significant accounting policies and related judgments are set out below.

NatWest Markets Plc (NWM Plc) is incorporated in the UK and registered in Scotland. Its accounts are presented in accordance with the Companies Act 2006.

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

With the exception of certain financial instruments as described in Accounting policies 10 and 18, the accounts are presented on an historical cost basis.

Accounting policy changes effective 1 January 2019

Adoption of IFRS 16

Refer to Accounting policy 7 and Note 24 for details of the adoption of IFRS 16.

Other amendments to IFRS

IAS 12 'Income taxes' was revised with effect from 1 January 2019. The income statement now includes any tax relief on the servicing cost of instruments classified as equity. This amendment has not affected the accounts.

IAS 19 'Employee Benefits' was amended by the IASB in February 2018 to clarify the need to update assumptions whenever there is a plan amendment, curtailment or settlement. This amendment has not affected the accounts.

Presentation of interest in suspense recoveries

- In March 2019 the IFRS Interpretations Committee (IFRIC) issued an agenda decision on the presentation of unrecognised interest when a credit-impaired financial asset (commonly referred to as a 'Stage 3' financial asset) is subsequently paid in full or is no longer credit-impaired. This concluded that the difference arising from the additional interest recovered must be recognised as a reversal of impairment rather than within interest revenue. This affects both recognition and the reversal of the expected credit loss (ECL) allowance.

RBS Group changed its accounting policy in line with the IFRIC decision. Hence, the gross carrying amount of the financial assets within the scope of the provisions of the decision, as well as the associated ECL allowance on the balance sheet have been adjusted by £57 million (NWM Plc - £22 million) and the comparative period restated by £24 million with no effect on equity. The coverage ratio for the current and comparative periods have been adjusted and restated accordingly.

In addition, until 1 January 2019, interest in suspense recoveries were presented as a component of interest receivable within Net interest income. From 1 January 2019 interest in suspense recoveries are presented within Impairment losses. Amounts are immaterial.

IAS 39 'Financial Instruments: Recognition and Measurement', IFRS 9 'Financial Instruments' and IFRS 7 'Financial Instruments: Disclosures'

- In September 2019, the IASB published amendments to address the issues arising from the replacement of existing IBOR based interest rate benchmarks with alternative nearly risk-free interest rates (RFRs) in the context of hedge accounting. These amendments allow hedging relationships affected by the IBOR reform to be accounted for as continuing hedges. RBS has early adopted these amendments for the annual reporting period ending on 31 December 2019.

The amendments provide relief on key areas of hedge accounting most notably the hedge effectiveness assessment and the ability to identify LIBOR-based cash flows for the purpose of designation (re-designation) during the period of the Reform. Additional disclosures are shown in Note 10.

IFRIC decision - Disclosure of change in liabilities arising from financing activities (IAS 7 statement of cash flows) – Following the IFRIC decision on how changes in liabilities should be presented in the cash flow statement, NWM Group has revised its presentation of financing activities and applied this to the cash flow statement.

2. Basis of consolidation

The consolidated accounts incorporate the financial statements of the NWM Plc and entities (including certain structured entities) that give access to variable returns and that are controlled by NWM Group. NWM Group controls another entity (a subsidiary) when it is exposed, or has rights, to variable returns from its involvement with that entity and has the ability to affect those returns through its power over the other entity; power generally arises from holding a majority of voting rights. On acquisition of a subsidiary, its identifiable assets, liabilities and contingent liabilities are included in the consolidated accounts at their fair value. A subsidiary is included in the consolidated financial statements from the date it is controlled by NWM Group until the date NWM Group ceases to control it through a sale or a significant change in circumstances. Changes in NWM Group's interest in a subsidiary that do not result in NWM Group ceasing to control that subsidiary are accounted for as equity transactions.

On the acquisition of a business from an RBS Group company, the assets, liabilities and IFRS reserves, such as the cash flow hedging reserve, are recognised at their inherited values taken from the consolidated accounts of RBSG plc and include the accounting history since initial recognition. The acquirer recognises, in merger reserve, any difference

between the consideration paid and the net items recognised at inherited values.

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 and the effective part of any related accounting hedging instruments. Negative effective interest accruing to financial assets is presented in interest payable.

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 price is usually fixed and always determinable.

4. Assets held for sale

A non-current asset (or disposal group) is classified as held for sale if NWM Group will recover its carrying amount principally through a sale transaction rather than through continuing use and is measured at the lower of its carrying amount or fair value less cost to sell.

5. Employee benefits

Short-term employee benefits, such as salaries, paid absences, and other benefits are accounted for on an accruals 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 NWM Group or by RBSG plc shares. NWM Group operates a number of share-based compensation schemes under which it awards RBSG 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.

Accounting policies

Contributions to defined contribution pension schemes are recognised in profit or loss when payable.

For defined benefit schemes, the defined benefit obligation is measured on an actuarial basis.

Actuarial gains and losses (i.e. gains or and 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 NWM 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.

6. 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 and hedges of net investments in foreign operations (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 non-monetary financial assets classified as fair value through 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 the translation of a foreign operation 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.

7. Leases

NWM Group has adopted IFRS 16 'Leases' with effect from 1 January 2019, replacing IAS 17 'Leases'. NWM Group has applied IFRS 16 on a modified retrospective basis without restating prior years. The effect is set out in Note 24.

As lessee

On entering a new lease contract, NWM Group recognises a right of use asset and a 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.

8. Provisions and contingent liabilities

NWM 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 NWM Group has a constructive obligation to restructure. An obligation exists when NWM 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.

NWM Group recognises any onerous cost of the present obligation under a contract as a provision. An onerous cost is the unavoidable cost of meeting NWM Group's contractual obligations that exceed the expected economic benefits. When NWM 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 but information about them is disclosed unless the possibility of any outflow of economic benefits in settlement is remote.

9. 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. The tax consequences of servicing equity instruments are recognised in the 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 NWM 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 NWM Group company or on NWM 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. RBS 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.

Accounting policies

10. Financial instruments

Financial instruments are classified either by product, by business model or by reference to the IFRS default classification.

Classification by product relies on specific designation criteria which are applicable to certain classes of financial assets or circumstances where accounting mismatches would otherwise arise. Classification by business model reflects how NWM Group manages its financial assets to generate cash flows. A business model assessment determines if cash flows result from holding financial assets to collect the contractual cash flows, from selling those financial assets, or both.

The product classifications apply to financial assets that are either designated at fair value through profit or loss (DFV), or to equity investments designated as at fair value through other comprehensive income (FVOCI). Financial assets may also be irrevocably designated at fair value through profit or loss upon initial recognition if such designation eliminates, or significantly reduces, accounting mismatch. In all other instances, fair value through profit or loss (MFVTPL) is the default classification and measurement category for financial assets.

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.

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.

Most financial assets are within 'held to collect' business models, and have contractual cash flows that comprise solely payments of principal and interest and therefore measured at amortised cost.

Certain financial assets are managed under a business model of both 'held to collect and sell' and have contractual cash flows comprising solely of payments of principal and interest, and are measured at fair value through other comprehensive income ('FVOCI').

The contractual terms of a facility; 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.

All financial instruments are measured at fair value on initial recognition.

All liabilities not subsequently measured at fair value are measured at amortised cost.

11. Impairment: expected credit losses

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 rating, 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 a reduction in the net present value of expected cash flows. On a significant increase in credit risk, allowances are recognised without a change in the expected cash flows, although typically expected cash flows do also change; and expected credit losses are adjusted from 12 month to lifetime expectations.

Judgement is exercised as follows:

- **Models** – in certain low default portfolios, Basel parameter estimates are also applied for IFRS 9.
- **Non-modelled portfolios** use a standardised capital requirement under Basel II. Under IFRS 9, they have bespoke treatments for the identification of significant increase in credit risk. Benchmark PDs, EADs and LGDs are reviewed annually for appropriateness. The ECL calculation is based on expected future cash flows, which is typically applied at a portfolio level.
- **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.

Where, in the course of the orderly realisation of a loan, it is exchanged for equity shares or property, the exchange is accounted for as the sale of the loan and the acquisition of

equity securities or investment property. Where NWM Group's interest in equity shares following the exchange is such that NWM Group controls an entity, that entity is consolidated.

Impaired loans are written off and therefore derecognised from the balance sheet when NWM 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 NWM Group's collectively-assessed portfolios are:

- Commercial loans: write offs are determined in the light of individual circumstances; the period does not exceed five years.
- Business loans are generally written off within five years.

12. Financial guarantee contracts

Under a financial guarantee contract, NWM Group, in return for a fee, undertakes to meet a customer's obligations under the terms of a debt instrument if the customer fails to do so. A financial guarantee is recognised as a liability; initially at fair value and, if not designated as at fair value through profit or loss, subsequently at the higher of its initial value less cumulative amortisation and any provision under the contract measured in accordance with Accounting policy 11. Amortisation is calculated so as to recognise fees receivable in profit or loss over the period of the guarantee.

13. Loan commitments

Provision is made for expected credit loss on loan commitments, other than those classified as held-for-trading. Syndicated loan commitments in excess of the level of lending under the commitment approved for retention by NWM Group are classified as held-for-trading and measured at fair value through profit or loss.

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 NWM Group retains substantially all the risks and rewards of ownership. If substantially all the risks and rewards have been neither retained nor transferred, NWM 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 is cancelled, or expires.

Accounting policies

15. Sale and repurchase transactions

Securities subject to a sale and repurchase agreement under which substantially all the risks and rewards of ownership are retained by NWM 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 NWM 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.

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 amount presented in the balance sheet when, and only when, NWM Group currently 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. NWM 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

NWM 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 NWM Group after the deduction of liabilities. The components of a compound financial instrument issued by NWM Group are classified and accounted for separately as financial assets, financial liabilities or equity as appropriate.

Incremental costs and related tax that are directly attributable to an equity transaction are deducted from equity.

The consideration for any ordinary shares of NWM Plc purchased by NWM Group (treasury shares) is deducted from equity. On the cancellation of treasury shares their nominal value is removed from equity and any excess of consideration over nominal value is treated in accordance with the capital maintenance provisions of the Companies Act.

On the sale or re-issue of treasury shares the consideration received and related tax are credited to equity, net of any directly attributable incremental costs.

18. Derivatives and hedging

Derivative financial instruments are initially recognised, and subsequently measured, at fair value. NWM Group's approach to determining the fair value of financial instruments is set out in the Critical accounting policies section and key sources of estimation uncertainty entitled Fair value - financial instruments; further details are given in Note 12 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. NWM 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 of 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 NWM 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. Shares in NWM Group entities

NWM Plc's investments in its subsidiaries are stated at cost less any impairment.

Accounting policies

Critical accounting policies and key sources of estimation uncertainty

The reported results of NWM Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. UK company law and IFRS require the directors, in preparing NWM Group's financial statements, to select suitable accounting policies, apply them consistently and make judgements 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 judgements and assumptions involved in NWM 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. The use of estimates, assumptions or models that differ from those adopted by NWM Group would affect its reported results.

Critical accounting policy	Note
Deferred tax	7
Fair value: financial instruments	12
Loan impairment provisions	14
Provisions for liabilities and charges	21

Future accounting developments International Financial Reporting Standards

A number of IFRSs and amendments to IFRS were in issue at 31 December 2019 that would affect RBS Group from 1 January 2020 or later:

- The amendments to IAS 1 'Presentation of Financial Statements' and IAS 8 'Accounting Policy, Changes in Accounting Estimates and Errors' on the definition of material were issued in October 2018 and are effective for annual periods beginning on or after 1 January 2020 with earlier application permitted. The amendments are aimed at improving the understanding of the existing requirements rather than to significantly impact current materiality judgements. They provide a new definition of material which shall be used to assess whether information, either individually or in combination with other information, is material in the context of the financial statements.

- The amendments to IFRS 3 'Business Combinations' which clarify the definition of a Business were issued in October 2018, are effective for annual reporting periods beginning on or after 1 January 2020 and apply prospectively with earlier application permitted. They clarify the minimum requirements for a business; remove the assessment of whether market participants are capable of replacing any missing elements; add guidance to help entities assess whether an acquired process is substantive; narrow the definitions of a business and of outputs; and introduce an optional fair value concentration test.
- Effective in 2022 - IFRS 17 'Insurance contracts' was issued in May 2017 to replace IFRS 4 and to establish a comprehensive standard for inceptors of insurance policies. The effective date is 1 January 2021, subject to IASB's approval of a deferral until 1 January 2022.

NWM Group is assessing the effect of adopting these standards on its financial statements.

Notes on the accounts

1 Net interest income

	2019 £m	2018 £m
Loans to banks - amortised cost	52	21
Loans to customers - amortised cost	393	239
Amounts due from holding company and fellow subsidiaries	—	54
Other financial assets	252	92
Interest receivable (1)	697	406
Balances with banks	78	110
Customer deposits	58	53
Amounts due to holding company and fellow subsidiaries	309	210
Other financial liabilities	402	300
Interest payable (1)	847	673
Net interest income	(150)	(267)

Note:

(1) Negative interest on loans is classed as interest payable and on customer deposits 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.

2 Non-interest income

	2019 £m	2018 £m
Net fees and commissions (1)	(13)	27
Income from trading activities		
Foreign exchange	273	387
Interest rate	582	515
Credit	32	41
Changes in fair value of own debt attributable to own credit risk		
- debt securities in issue and derivative liabilities	(80)	92
Equities and other	(2)	10
	805	1,045
Gain on redemption of own debt	—	101
Other operating income		
Operating lease and other rental income	6	14
Changes in fair value of financial assets and liabilities designated at fair value through profit or loss	(31)	(16)
Changes in fair value of other financial assets fair value through profit or loss	24	(46)
Hedge ineffectiveness	6	(1)
Profit/(loss) on disposal of amortised cost assets	20	(73)
Loss on disposal of fair value through other comprehensive income assets	(9)	(8)
Profit on sale of property, plant and equipment	—	1
Dividend income	21	7
Loss on disposal of subsidiaries and associates	(9)	(12)
Other income (2)	49	86
	77	(48)
Total	869	1,125

Notes:

(1) Includes fees paid to NWM N.V. prior to its acquisition.

(2) Includes income from activities other than banking.

For 2018, amounts included in profit from discontinued operations, net of tax, were £1 million gain in relation to financial assets/liabilities as at fair value through profit or loss; and £51 million gain in relation to disposal or settlement of loans and receivables.

Notes on the accounts

3 Operating expenses

	2019 £m	2018 £m
Wages, salaries and other staff costs	477	456
Temporary and contract costs	38	21
Social security costs	50	49
Bonus awards	99	42
Pension costs	27	11
Staff costs	691	579
Premises and equipment	111	120
Depreciation and amortisation	18	14
Other administrative expenses (1,2)	177	1,524
Administrative expenses	306	1,658
	997	2,237

Notes:

- (1) Includes recharges from other RBS Group entities, mainly NWB Plc which provides the majority of shared services (including technology) and operational processes.
 (2) Includes litigation and other regulatory costs. Further details are provided in Note 21.

The average number of persons employed, rounded to the nearest hundred, in continuing operations during the year, excluding temporary staff, was 4,800 (2018 – 4,700⁽¹⁾); on the same basis there were no people employed in discontinued operations (2018 – 20,900). The number of persons employed by NWM Group in continuing operations at 31 December 2019, excluding temporary staff, was as follows:

	2019	2018
UK	2,200	2,100
USA	400	500
Europe	600	300
Rest of the World (1)	1,800	1,600
Total	5,000	4,500

Note:

- (1) In 2018, Rest of the World included 1,300 central and support staff who were paid by NWB Plc, with related costs recharged to NWM Group. These staff were transferred to NWM Plc in 2019.

No people were employed in discontinued operations at 31 December 2019 and 2018.

Bonus awards

The following tables analyse NWM Group's bonus awards for 2019.

	2019 £m	2018 £m	Change %
Non-deferred cash awards (1)	6	7	(14)
Total non-deferred bonus awards	6	7	(14)
Deferred bond awards	48	58	(17)
Deferred share awards	47	67	(30)
Total deferred bonus awards	95	125	(24)
Total bonus awards (2)	101	132	(23)

	2019 £m	2018 £m
Reconciliation of bonus awards to income statement charge		
Bonuses awarded	101	132
Less: deferral of charge for amounts awarded for current year	(38)	(65)
Income statement charge for amounts awarded in current year	63	67
Add: current year charge for amounts deferred from prior years	50	34
Less: forfeiture of amounts deferred from prior years	(14)	(59)
Income statement charge for amounts deferred from prior years	36	(25)
Income statement charge for bonus awards (2)	99	42

Notes:

- (1) Cash awards are limited to £2,000 for all employees.
 (2) Excludes other performance related compensation.

Notes on the accounts

4 Segmental analysis

Reportable operating segments

The reportable operating segments are as follows:

NatWest Markets offers its customers global market access, providing them with trading, risk management and financing solutions through its trading hubs in London, Amsterdam, Singapore and Stamford and sales offices across key locations in the UK, EU, US and Asia.

Central items & other includes corporate functions and other activity not managed in the NatWest Markets segment. In 2019, this was substantially comprised of reimbursement under indemnification agreements with third parties and certain other one-off cost recoveries. In 2018, the balances largely related to legacy litigation issues, interest expense associated with certain Treasury liabilities prior to their transfer to the NatWest Markets segment and other assets not included within the NatWest Markets segment.

	Net interest income (1) £m	Net fees and commissions £m	Other non-interest income £m	Total income £m	Operating expenses £m	Depreciation and amortisation £m	Impairment releases £m	Operating (loss)/profit £m
2019								
NatWest Markets	(160)	(19)	869	690	(1,261)	(18)	48	(541)
Central items & other	10	6	13	29	282	—	—	311
Total	(150)	(13)	882	719	(979)	(18)	48	(230)

2018								
NatWest Markets	5	32	981	1,018	(1,381)	(14)	88	(289)
Central items & other	(272)	(5)	117	(160)	(842)	—	14	(988)
Total	(267)	27	1,098	858	(2,223)	(14)	102	(1,277)

Note:

- (1) Includes interest payable of £847 million and interest receivable of £697 million in relation to NWM Group (2018 - £673 million and £406 million respectively). Within the NatWest Markets segment net interest income comprises interest receivable on external lending activities, offset by net interest payable on external funding activity managed by NatWest Markets Treasury and inter-segmental charges. Net interest expense in Central items & other predominantly comprises external interest costs associated with RBS Group Treasury managed liabilities and the impact of inter-segmental income.

	2019 Total £m	2018 Total £m
Total revenue		
NatWest Markets	2,331	2,357
Central items & other	(428)	(593)
Total	1,903	1,764

Analysis of net fees and commissions

Fees and commissions receivable

	2019			2018		
	NatWest Markets £m	Central items & other £m	Total £m	NatWest Markets £m	Central items & other £m	Total £m
- Lending (credit facilities)	80	—	80	87	—	87
- Brokerage	86	—	86	80	—	80
- Underwriting fees	152	—	152	141	—	141
- Other	—	6	6	78	(126)	(48)
Total	318	6	324	386	(126)	260
Fees and commissions payable	(337)	—	(337)	(354)	121	(233)
Net fees and commissions	(19)	6	(13)	32	(5)	27

	2019		2018	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
NatWest Markets	266,136	256,210	245,060	236,121
Central items & other	—	16	2,821	2,671
Total	266,136	256,226	247,881	238,792

Notes on the accounts

4 Segmental analysis continued

Geographical segments

The geographical analysis in the tables below has been compiled on the basis of location of office where the transactions are recorded.

2019	UK £m	USA £m	Europe £m	RoW £m	Total £m
Total revenue	1,588	225	(24)	114	1,903
Interest receivable	672	—	—	25	697
Interest payable	(814)	—	(31)	(2)	(847)
Fees and commissions receivable	192	65	(10)	77	324
Fees and commissions payable	(303)	(29)	—	(5)	(337)
Income from trading activities	650	148	—	7	805
Other operating income	55	11	7	4	77
Total income	452	195	(34)	106	719
Operating (loss)/profit before tax	(365)	187	(76)	24	(230)
Total assets	222,213	33,121	9,171	1,631	266,136
Total liabilities	216,479	31,717	7,025	1,005	256,226
Net assets attributable to equity shareholders and non-controlling interests	5,734	1,404	2,146	626	9,910
Contingent liabilities and commitments	9,837	—	7,092	2	16,931

2018	UK £m	USA £m	Europe £m	RoW £m	Total £m
Total revenue	1,512	195	(46)	103	1,764
Interest receivable	374	—	5	27	406
Interest payable	(662)	—	—	(11)	(673)
Fees and commissions receivable	144	53	—	63	260
Fees and commissions payable	(190)	(41)	—	(2)	(233)
Income from trading activities	931	106	—	8	1,045
Other operating income	19	36	(7)	5	53
Total income	616	154	(2)	90	858
Operating (loss)/profit before tax	(1,168)	(129)	(15)	35	(1,277)
Total assets	212,755	32,637	1,061	1,428	247,881
Total liabilities	206,305	31,436	88	963	238,792
Net assets attributable to equity shareholders and non-controlling interests	6,450	1,201	973	465	9,089
Contingent liabilities and commitments	10,884	—	31	208	11,123

5 Pensions

Defined contribution schemes

NWM Group sponsors a number of defined contribution pension schemes in different territories, which new employees are offered the opportunity to join.

Defined benefit schemes

NWM Group sponsors a number of pension schemes in the UK and overseas, including the AA and NatWest Markets (NWM) sections of The Royal Bank of Scotland Group Pension Fund which operate under UK trust law and are managed and administered on behalf of their members in accordance with the terms of the trust deed, the scheme rules and UK legislation.

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

The schemes generally provide a pension of one-sixtieth of final pensionable salary for each year of service prior to retirement up to a maximum of 40 years and are contributory for current members. These have been closed to new entrants for over ten years, although current members continue to build up additional pension benefits, currently subject to 2% maximum annual salary inflation, while they remain employed by NWM Group.

Major classes of plan assets as a percentage of total plan assets of the AA section

	2019			2018		
	Quoted %	Unquoted %	Total %	Quoted %	Unquoted %	Total %
Equities	2.4	1.0	3.4	2.1	0.9	3.0
Index linked bonds	40.5	—	40.5	43.2	—	43.2
Government bonds	4.9	—	4.9	1.6	—	1.6
Corporate and other bonds	24.0	7.7	31.7	30.5	4.9	35.4
Real estate	—	2.3	2.3	—	1.9	1.9
Derivatives	—	4.4	4.4	—	3.3	3.3
Cash and other assets	—	12.8	12.8	—	11.6	11.6
	71.8	28.2	100.0	77.4	22.6	100.0

The corporate trustee is RBS Pension Trustee Limited (the Trustee), a wholly owned subsidiary of National Westminster Bank Plc. The Board of the Trustee comprises four member trustee directors selected from eligible active staff, deferred and pensioner members who apply and six appointed by RBS Group. Under UK legislation, a defined benefit pension scheme is required to meet the statutory funding objective of having sufficient and appropriate assets to cover its liabilities (the pensions that have been promised to members).

Investment strategy

The assets of the AA section, which is typical of other group schemes, represent 77% of the plan assets at 31 December 2019 (2018 – 76% of the continuing plan assets) and are invested in a diversified portfolio as shown below.

The AA and NWM sections employ derivative instruments to achieve a desired asset class exposure and to reduce the schemes' interest rate, inflation and currency risk. This means that the net funding positions are considerably less sensitive to changes in market conditions than the value of the assets or liabilities in isolation.

Swaps have been executed at prevailing market rates and within standard market bid/offer spreads with a number of counterparty banks, including National Westminster Bank Plc.

Notes on the accounts

5 Pensions continued

The schemes do not invest directly in NWM Group but can have exposure to NWM Group. The trustees are responsible for ensuring that indirect investments in NWM Group do not exceed the 5% regulatory limit.

	AA section			All schemes (2)			
	Fair value of plan assets	Present value of defined benefit obligation	Net pension (asset)/liability	Fair value of plan assets	Present value of defined benefit obligation	Asset ceiling/minimum funding (1)	Net pension (asset)/liability
	£m	£m	£m	£m	£m	£m	£m
Changes in value of net pension (asset)/liability							
At 1 January 2018	1,157	867	(290)	1,272	1,036	—	(236)
Currency translation and other adjustments	—	—	—	4	4	—	—
Income statement	29	22	(7)	36	42	—	6
Statement of comprehensive income	(50)	(43)	7	(64)	(48)	39	55
Transfers to/from fellow subsidiaries	—	—	—	28	19	7	(2)
Contributions by employer	1	—	(1)	7	—	—	(7)
Benefits paid	(86)	(86)	—	(97)	(97)	—	—
Transfer of pension assets and liabilities from Main section	—	—	—	202	151	51	—
At 1 January 2019	1,051	760	(291)	1,388	1,107	97	(184)
Currency translation and other adjustments	—	—	—	1	(1)	—	(2)
Income statement							
Net interest expense	30	21	(9)	38	31	3	(4)
Current service cost	—	—	—	—	9	—	9
Loss on curtailments or settlements	—	—	—	—	1	—	1
	30	21	(9)	38	41	3	6
Statement of comprehensive income							
Return on plan assets excluding recognised interest income	56	—	(56)	84	—	—	(84)
Experience gains and losses	—	(6)	(6)	—	(4)	—	(4)
Effect of changes in actuarial financial assumptions	—	108	108	—	150	—	150
Effect of changes in demographic assumptions	—	(7)	(7)	—	(7)	—	(7)
Asset ceiling adjustments	—	—	—	—	—	(5)	(5)
	56	95	39	84	139	(5)	50
Transfers to/from fellow subsidiaries	—	—	—	(2)	7	—	9
Contributions by employer	2	—	(2)	82	—	—	(82)
Contributions by plan participants and other scheme members	—	—	—	1	1	—	—
Benefits paid	(51)	(51)	—	(60)	(60)	—	—
Liabilities extinguished upon settlement	—	—	—	(113)	(118)	—	(5)
At 31 December 2019	1,088	825	(263)	1,419	1,116	95	(208)

Notes:

- (1) 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.
- (2) Includes the NWM Section which has a net pension asset of nil at 31 December 2019 (2018: net pension liability of £53 million). This scheme has plan assets of £298 million, a defined benefit obligation of £203 million, an asset ceiling of £95 million and a minimum funding requirement of nil (2018: £204 million, £160 million, £44 million and £53 million respectively).
- (3) NWM Group expects to make contributions to the AA section of £2 million and to the NWM section of £11 million in 2020.

	All schemes	
	2019	2018
	£m	£m
Amounts recognised on the balance sheet		
Fund assets at fair value	1,419	1,388
Present value of fund liabilities	1,116	1,107
Funded status	303	281
Asset ceiling/minimum funding	95	97
	208	184
Net pension asset/(liability) comprises		
Net assets of schemes in surplus (included in Other assets, Note 18)	271	299
Net liabilities of schemes in deficit (included in Other liabilities, Note 21)	(63)	(115)
	208	184

The income statement charge comprises:

	2019	2018
	£m	£m
Continuing operations	6	6
Discontinued operations	—	81
	6	87

Notes on the accounts

5 Pensions continued

Funding and contributions by NWM Group

In the UK, the trustees of defined benefit pension schemes are required to perform funding valuations every three years. The trustees and the sponsoring company, with the support of the Scheme Actuary, agree the assumptions used to value the liabilities and a Schedule of Contributions required to eliminate any funding deficit. 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. Similar arrangements apply in the other territories where the NWM Group sponsors defined benefit pension schemes. The last funding valuation of the AA section was at 31 December 2017 and next funding valuation is due at 31 December 2020, to be agreed by 31 March 2022.

The triennial funding valuation of the AA section as at 31 December 2017 determined the funding level to be 109%, pension liabilities to be £1,063 million and the surplus to be £98 million.

The most significant assumptions used for the AA section are shown below:

	Principal IAS 19 actuarial assumptions		Principal assumptions of AA section
	2019 %	2018 %	2017 triennial valuation
Discount rate	2.1	2.9	Fixed interest gilt yield curve plus 0.4% per annum RPI gilt yield curve
Inflation assumption (RPI)	2.9	3.2	
Rate of increase in salaries	1.8	1.8	
Rate of increase in deferred pensions	2.0	2.1	Modelled allowance for relevant caps and floors
Rate of increase in pensions in payment	2.9	3.0	
Lump sum conversion rate at retirement	18	18	
Longevity at age 60:	years	years	
Current pensioners			
Males	28.1	28.2	28.8
Females	29.6	29.6	30.3
Future pensioners, currently aged 40			
Males	29.4	29.3	30.4
Females	31.3	31.6	32.3

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. For the triennial valuation discounting is by reference to a yield curve.

The weighted average duration of the AA section's defined benefit obligation at 31 December 2019 is 20 years (2018 – 20 years).

The first triennial funding valuation of the NWM section was carried out as at 31 December 2018. NWM Group made a contribution of £53m to the NWM section during 2019. Allowing for this contribution, the valuation determined the funding level at 31 December 2018 to be 127%, pension liabilities to be £220 million and the surplus to be £33 million.

Assumptions

Placing a value on NWM Group's defined benefit pension schemes' liabilities requires NWM Group's management to make a number of assumptions, with the support of independent actuaries. The ultimate cost of the defined benefit obligations depends upon actual future events and the assumptions made are unlikely to be exactly borne out in practice, meaning the final cost may be higher or lower than expected.

Significant judgement 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. Judgement 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.

Notes on the accounts

5 Pensions continued

The table below shows how the present value of the net pension asset of the AA section would change if the key assumptions used were changed independently. In practice the variables have a degree of correlation and do not move completely in isolation.

	(Decrease)/ increase in value of assets £m	(Decrease)/ increase in value of liabilities £m	Increase in net pension (obligations)/ assets £m
2019			
0.25% increase in interest rates/discount rate	(52)	(40)	(12)
0.25% increase in inflation	50	27	23
0.25% increase in credit spreads	—	(40)	40
Longevity increase of one year	—	30	(30)
0.25% additional rate of increase in pensions in payment	—	30	(30)
Increase in equity values of 10% (1)	4	—	4
2018			
0.25% increase in interest rates/discount rate	(54)	(36)	(18)
0.25% increase in inflation	46	26	20
0.25% increase in credit spreads	—	(36)	36
Longevity increase of one year	—	28	(28)
0.25% additional rate of increase in pensions in payment	—	30	(30)
Increase in equity values of 10% (1)	2	—	2

Note:

(1) Includes both quoted and private equity.

The defined benefit obligation is attributable to the different classes of AA section members in the following proportions:

Membership category	2019 %	2018 %
Active members	2.8	2.6
Deferred members	62.7	61.8
Pensioners and dependants	34.5	35.6
	100.0	100.0

The experience history of the AA section is shown below:

History of defined benefit schemes	2019 £m	2018 £m
Fair value of plan assets	1,088	1,051
Present value of plan obligations	825	760
Net surplus	263	291
Experience gains/(losses) on plan liabilities	6	(1)
Experience gains/(losses) on plan assets	56	(50)
Actual return on plan assets	86	(21)
Actual return on plan assets	8.2%	(1.8%)

6 Auditor's remuneration

Amounts paid to the NWM Group's auditors for statutory audit and other services are set out below:

	2019 £m	2018 £m
Fees payable for:		
- the audit of the NWM Group's annual accounts	6.9	7.5
- the audit of NWM Plc's subsidiaries	3.1	2.7
- audit-related assurance services	1.4	—
Total audit and audit-related assurance services fees	11.4	10.2
Corporate finance services	0.2	2.7
Total other services	0.2	2.7

Fees payable to the auditor for non-audit services are disclosed in the consolidated financial statements of The Royal Bank of Scotland Group plc.

Notes on the accounts

7 Tax

	2019 £m	2018 £m
Current tax		
Credit/(charge) for the year	90	(6)
Over provision in respect of prior years	58	111
	148	105
Deferred tax		
Credit/(charge) for the year	54	(18)
Decrease in the carrying value of deferred tax assets	(76)	—
Under provision in respect of prior year	(17)	(54)
Tax credit for the year	109	33

The actual tax credit differs from the expected tax credit computed by applying the standard rate of UK corporation tax of 19% (2018 – 19%) as follows:

	2019 £m	2018 £m
Expected tax credit	44	243
Losses and temporary differences in year where no deferred tax asset recognised	(12)	(1)
Foreign profits taxed at other rates	(6)	(16)
UK tax rate change impact	—	5
Items not allowed for tax:		
- losses on disposal and write-downs	(6)	(57)
- UK bank levy	(1)	—
- regulatory and legal actions	21	(169)
- other disallowable items	(14)	(43)
Non-taxable items	48	11
Losses brought forward and utilised	9	11
Decrease in the carrying value of deferred tax assets in respect of UK losses	(76)	—
Banking surcharge	45	(8)
Tax on paid-in equity	16	—
Adjustments in respect of prior years ⁽¹⁾	41	57
Actual tax credit	109	33

Note:

(1) Prior year tax adjustments incorporate refinements to tax computations made on submission and agreement with the tax authorities. Current taxation balances include provisions in respect of uncertain tax positions, in particular in relation to restructuring and other costs where the taxation treatment remains subject to agreement with the relevant tax authorities.

Judgment: Tax contingencies

NWM Group's income tax credit and its provisions for income taxes necessarily involves a significant degree of estimation and judgement. The tax treatment of some transactions is uncertain and tax computations are yet to be agreed with the tax authorities in a number of jurisdictions. NWM Group recognises anticipated tax liabilities based on all available evidence and, where appropriate, in the light of external advice. Any difference between the final outcome and the amounts provided will affect current and deferred income tax charges in the period when the matter is resolved.

Deferred tax

	NWM Group		NWM Plc	
	2019 £m	2018 £m	2019 £m	2018 £m
Deferred tax asset (included in Other assets, Note 18)	(1)	—	—	—
Deferred tax liability (included in Other liabilities, Note 21)	501	487	462	446
Net deferred tax liability	500	487	462	446

Notes on the accounts

7 Tax continued

Net deferred tax liability/(asset) comprised:

NWM Group							
	Pension £m	Accelerated capital allowances £m	Expense provisions £m	Financial instruments £m	Tax losses carried forward £m	Other £m	Total £m
At 1 January 2018	(387)	191	(279)	38	(939)	27	(1,349)
Implementation of IFRS9 on 1 January 2018	—	—	—	16	—	—	16
Acquisitions and disposals of subsidiaries	872	247	101	(78)	814	(77)	1,879
(Credit)/charge to income statement:							
- continuing operations	(6)	—	129	(19)	(26)	(6)	72
- discontinued operations	—	40	—	306	—	41	387
(Credit)/charge to other comprehensive income	(412)	—	(16)	(122)	—	32	(518)
At 31 December 2018	67	478	(65)	141	(151)	17	487
Implementation of IFRS16 on 1 January 2019	—	—	—	—	—	(2)	(2)
Acquisitions and disposals of subsidiaries	—	(10)	—	6	—	13	9
Charge/(credit) to income statement	6	(68)	26	(4)	76	3	39
(Credit)/charge to other comprehensive income	(1)	(1)	—	(11)	—	(20)	(33)
At 31 December 2019	72	399	(39)	132	(75)	11	500

NWM Plc							
	Pension £m	Accelerated capital allowances £m	Expense provisions £m	Financial instruments £m	Tax losses carried forward £m	Other £m	Total £m
At 1 January 2018	89	(35)	(223)	(129)	(125)	2	(421)
Implementation of IFRS9 on 1 January 2018	—	—	—	121	—	—	121
Acquisitions and disposals of subsidiaries	—	440	45	(150)	—	(22)	313
(Credit)/charge to income statement:							
- continuing operations	(6)	—	128	(20)	(26)	4	80
- discontinued operations	—	35	—	344	—	1	380
(Credit)/charge to other comprehensive income	(15)	—	(15)	(28)	—	32	(26)
Currency translations and other adjustments	—	—	—	—	—	(1)	(1)
At 31 December 2018	68	440	(65)	138	(151)	16	446
Implementation of IFRS16 on 1 January 2019	—	—	—	—	—	(2)	(2)
Acquisitions and disposals of subsidiaries	—	(10)	(1)	—	—	—	(11)
Charge/(credit) to income statement	6	(42)	27	(10)	76	4	61
(Credit)/charge to other comprehensive income	(1)	—	—	(11)	—	(20)	(32)
At 31 December 2019	73	388	(39)	117	(75)	(2)	462

Deferred tax assets in respect of unused tax losses are recognised if the losses can be used to offset probable future taxable profits after taking into account the expected reversal of other temporary differences. Recognised deferred tax assets in respect of tax losses are analysed below.

	2019 £m	2018 £m
UK tax losses carried forward		
NWM Plc	75	151

Notes on the accounts

7 Tax continued

Critical accounting policy: Deferred tax

The deferred tax liability of £501 million at 31 December 2019 (2018 – net liability of £487 million) includes a deferred tax asset on losses of £75 million. The deferred tax asset recognised on UK losses is recognised to the extent that it is probable that there will be future taxable profits to recover it.

Judgment – NWM Group has considered the carrying value of deferred tax assets and management considers that sufficient taxable profits will be generated in future years to recover the remaining deferred tax asset.

Estimate – The deferred tax asset is supported by way of future reversing temporary timing differences on which deferred tax liabilities are recognised at 31 December 2019.

UK tax losses – Under UK tax rules, tax losses can be carried forward indefinitely. As the recognised tax losses in NWM Group arose prior to 1 April 2015, credit in future periods is given against 25% of profits at the main rate of UK corporation tax, excluding the Banking Surcharge 8% rate introduced by The Finance (No. 2) Act 2015. Deferred tax assets and liabilities at 31 December 2019 take into account the reduced rates in respect of tax losses and temporary differences and where appropriate, the banking surcharge inclusive rate in respect of other banking temporary differences.

NWM Plc – NWM Plc expects that the balance of recognised deferred tax asset at 31 December 2019 of £75 million (2018 – £151 million) in respect of tax losses amounting to approximately £400 million will be recovered by the end of 2025. The movement in the current financial year reflects a £76 million decrease in the carrying value of the deferred tax asset, driven primarily by a decrease in forecast future taxable profits as a result of the strategic review of the NWM franchise. During the year, agreement was reached to transfer tax losses of £5,438 million to National Westminster Bank Plc and The Royal Bank of Scotland plc, as a consequence of the ring fencing regulations. Of the losses remaining, £5,109 million have not been recognised in the deferred tax balance at 31 December 2019; such losses will be available to offset 25% of future taxable profits in excess of those forecast in the closing deferred tax asset.

8 Profit/(loss) dealt with in the accounts of NWM Plc

As permitted by section 408(3) of the Companies Act 2006, no income statement for NWM Plc has been presented as a primary financial statement.

9 Trading assets and liabilities

Trading assets and liabilities comprise assets and liabilities held at fair value in trading portfolios.

	NWM Group		NWM Plc	
	2019	2018	2019	2018
	£m	£m	£m	£m
Assets				
Loans				
- Reverse repos	24,095	24,758	12,716	15,915
- Collateral given	20,467	18,898	19,074	18,898
- Other loans	1,854	1,302	1,486	934
Total loans	46,416	44,958	33,276	35,747
Securities				
Central and local government				
- UK	4,897	6,834	4,897	6,834
- US	5,458	4,689	293	1,498
- other	14,902	13,498	14,748	13,498
Financial institutions and Corporate	4,867	4,993	4,554	4,413
Total securities	30,124	30,014	24,492	26,243
Total	76,540	74,972	57,768	61,990
Liabilities				
Deposits				
- Repos	27,885	25,645	10,007	9,784
- Collateral received	21,506	20,129	20,945	20,129
- Other deposits	1,496	1,786	1,491	1,786
Total deposits	50,887	47,560	32,443	31,699
Debt securities in issue	1,762	902	1,762	902
Short positions	21,187	23,827	19,371	21,939
Total	73,836	72,289	53,576	54,540

Overseas tax losses

NWM N.V. – NWM N.V. Group management has considered that there are significant changes to NWM N.V. Group's activities compared to prior years as NWM N.V. has re-purposed its banking licence and new business was transferred to NWM N.V. during 2019. NWM N.V. Group management did not recognise deferred tax asset in respect of losses carried forward at 31 December 2019 due to the implications from the wider strategic review of the NWM franchise and the uncertainty in respect of Brexit.

Unrecognised deferred tax

Deferred tax assets of £3,052 million (2018 – £3,398 million) have not been recognised in respect of tax losses and other temporary differences carried forward of £12,319 million (2018 – £15,315 million) in jurisdictions where doubt exists over the availability of future taxable profits. Of these losses and other temporary differences, £837 million expire within five years and £4,798 million thereafter. The balance of tax losses and other temporary differences carried forward has no expiry date.

Deferred tax liabilities of £2 million (2018 – £3 million) have not been recognised in respect of retained earnings of overseas subsidiaries and held-over gains on the incorporation of overseas branches. Retained earnings of overseas subsidiaries are expected to be reinvested indefinitely or remitted to the UK free from further taxation. No taxation is expected to arise in the foreseeable future in respect of held-over gains. Changes to UK tax legislation largely exempts from UK tax, overseas dividends received on or after 1 July 2009.

Notes on the accounts

10 Derivatives

Companies within NWM Group transact derivatives as principal either as a trading activity or to manage balance sheet foreign exchange, interest rate and credit risk.

	NWM Group					
	2019			2018		
	Notional £bn	Assets £m	Liabilities £m	Notional £bn	Assets £m	Liabilities £m
Exchange rate contracts	3,799	44,983	47,138	3,444	36,635	38,346
Interest rate contracts	11,020	103,433	96,581	10,287	97,226	91,327
Credit derivatives	16	280	375	16	346	226
Equity and commodity contracts	3	—	48	1	43	15
		148,696	144,142		134,250	129,914

	NWM Plc					
	2019			2018		
	Notional £bn	Assets £m	Liabilities £m	Notional £bn	Assets £m	Liabilities £m
Exchange rate contracts	3,831	45,175	47,347	3,444	36,636	38,349
Interest rate contracts	9,577	102,001	94,627	10,267	97,266	91,384
Credit derivatives	18	282	368	16	346	226
Equity and commodity contracts	3	—	48	1	43	15
		147,458	142,390		134,291	129,974

Refer to Note 11 for amounts due from/to fellow RBS Group subsidiaries.

NWM Group applies hedge accounting to manage the following risks; interest rate, foreign exchange and net investment in foreign operations.

NWM Group interest rate hedging relates to the management of NWM Group non-trading structural interest rate risk, caused by the mismatch between fixed interest rates and floating interest rates. NWM 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, and 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 NWM 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 and EURIBOR. This risk component is identified using the risk management systems of NWM Group. This risk component comprises the majority of the hedged items fair value risk.

NWM Group hedges the exchange rate risk of its net investment in foreign currency denominated operations with currency borrowings and forward foreign exchange contracts. NWM Group reviews the value of the investments net assets, executing hedges where appropriate to reduce the sensitivity of capital ratios to foreign exchange rate movement. Hedge accounting relationships will be designated where required.

Exchange rate risk also arises in NWM Group where payments are denominated in different currencies than the functional currency. Residual risk positions are hedged with forward foreign exchange contracts. Exposure to the variability in future payments due to the movement of foreign exchange rates is hedged, fixing the exchange rate the payments will be settled in. The derivatives are documented as cash flow hedges.

For all cash flow hedging and fair value hedge relationships, NWM Group determines that there is an adequate level of offsetting between the hedged item and hedging instrument via assessing the initial and ongoing effectiveness. This involves 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 effectiveness is measured on a cumulative basis over a time period management determines to be appropriate. NWM Group uses either the actual ratio between the hedged item and hedging instrument(s) or one that minimises hedge ineffectiveness to establish the hedge ratio for hedge accounting.

A number of the current cash flow and fair value hedges of interest rate risk will be directly affected by interest rate benchmark reform; RBS Group currently considers all of these relationships that mature post 31 December 2021 to be directly affected. As at 31 December 2019, the exact transition dates of affected hedge accounting relationships is not known. The disclosures are prepared on these assumptions where the amendments made to IAS39 paragraphs 102D-102N and 108G are applied.

The disclosures made for the notional of hedging instruments and risk exposures affected by interest rate benchmark reform contain information for both the hedging instrument and hedged risks even if only one of these will be directly impacted by the reform.

NWM Group is managing the process to transition to alternative benchmark rates in the following ways:

- reviewed or is in the process of reviewing the fall-back language for IBOR linked instruments
- continues to liaise with regulators, standard setters, industry groups and customers on other relevant matters as the transition to risk free rates progresses
- is in the process of adjusting its products, processes and information systems to deal with the expected effects of the discontinuation of IBOR most notably the transition and calculation rules.

Notes on the accounts

10 Derivatives continued

Included in the table below are derivatives held for hedging as follows:

	NWM Group							
	2019				2018			
	Notional £bn	Assets £m	Liabilities £m	Changes in fair value used for hedge ineffectiveness (1) £m	Notional £bn	Assets £m	Liabilities £m	Changes in fair value used for hedge ineffectiveness (1) £m
Fair value hedging								
- interest rate contracts	14.2	279	89	68	8.9	79	24	15
Cash flow hedging								
- interest rate contracts	6.4	239	1	55	5.8	181	—	17
Net investment hedging								
- exchange rate contracts	0.2	—	1	—	0.7	27	9	—
	20.8	518	91	123	15.4	287	33	32
IFRS netting		(339)	(90)			(234)	(14)	
		179	1			53	19	

	NWM Plc							
	2019				2018			
	Notional £bn	Assets £m	Liabilities £m	Changes in fair value used for hedge ineffectiveness (1) £m	Notional £bn	Assets £m	Liabilities £m	Changes in fair value used for hedge ineffectiveness (1) £m
Fair value hedging								
- interest rate contracts	14.2	277	89	68	9.4	101	19	15
Cash flow hedging								
- interest rate contracts	6.4	239	1	55	5.8	181	—	17
Net investment hedging								
- exchange rate contracts	0.2	—	1	—	0.1	5	5	—
	20.8	516	91	123	15.3	287	24	32
IFRS netting		(337)	(90)			(233)	(14)	
		179	1			54	10	

For the note to the above tables refer to page 101.

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

	2019 £bn
Fair value hedging	
- LIBOR	7.5
- EURIBOR	5.2
Cash flow hedging	
- LIBOR	5.0

Notes on the accounts

10 Derivatives continued

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

	NWM Group							
2019	0-3 months £bn	3-12 months £bn	1-3 years £bn	3-5 years £bn	5-10 years £bn	10-20 years £bn	20+ years £bn	Total £bn
Fair value hedging								
Hedging assets - interest rate risk	—	—	1.4	1.0	0.2	0.1	0.1	2.8
Hedging liabilities - interest rate risk	—	0.5	4.7	5.2	0.9	0.1	—	11.4
Cash flow hedging								
Hedging assets - interest rate risk	0.2	0.6	1.3	1.4	2.9	—	—	6.4
Average fixed interest rate (%)	2.12	1.59	2.44	2.13	1.65	—	—	1.93
Net investment hedging								
Exchange rate risk	—	0.2	—	—	—	—	—	0.2

2018								
Fair value hedging								
Hedging assets - interest rate risk	—	—	0.3	0.4	0.2	—	—	0.9
Hedging liabilities - interest rate risk	—	—	4.1	3.8	0.1	—	—	8.0
Cash flow hedging								
Hedging assets - interest rate risk	—	0.5	1.8	1.5	2.0	—	—	5.8
Average fixed interest rate (%)	—	2.29	2.14	2.13	1.62	—	—	1.97
Net investment hedging								
Exchange rate risk	0.4	0.2	0.1	—	—	—	—	0.7

	NWM Plc							
2019	0-3 months £bn	3-12 months £bn	1-3 years £bn	3-5 years £bn	5-10 years £bn	10-20 years £bn	20+ years £bn	Total £bn
Fair value hedging								
Hedging assets - interest rate risk	—	—	1.4	1.0	0.2	0.1	0.1	2.8
Hedging assets - exchange rate risk	—	—	—	—	—	—	—	—
Hedging liabilities - interest rate risk	—	0.5	4.7	5.2	0.9	0.1	—	11.4
Cash flow hedging								
Hedging assets - interest rate risk	0.2	0.6	1.3	1.4	2.9	—	—	6.4
Average fixed interest rate (%)	2.12	1.59	2.44	2.13	1.65	—	—	1.93
Net investment hedging								
Exchange rate risk	—	0.2	—	—	—	—	—	0.2

2018								
Fair value hedging								
Hedging assets - interest rate risk	—	—	0.3	0.4	0.2	—	—	0.9
Hedging assets - exchange rate risk	0.4	0.1	0.1	—	—	—	—	0.6
Hedging liabilities - interest rate risk	—	—	4.1	3.7	0.1	—	—	7.9
Cash flow hedging								
Hedging assets - interest rate risk	—	0.5	1.8	1.5	2.0	—	—	5.8
Average fixed interest rate (%)	—	2.29	2.14	2.13	1.82	—	—	1.97
Net investment hedging								
Exchange rate risk	—	0.1	—	—	—	—	—	0.1

Notes on the accounts

10 Derivatives continued

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

	NWM Group				NWM Plc			
	Carrying value (CV) of hedged assets and liabilities £m	Impact on hedged items included in CV £m	Change in fair value used as a basis to determine ineffectiveness (1) £m	Impact on hedged items ceased to be adjusted for hedging gains or losses £m	Carrying value (CV) of hedged assets and liabilities £m	Impact on hedged items included in CV £m	Change in fair value used as a basis to determine ineffectiveness (1) £m	Impact on hedged items ceased to be adjusted for hedging gains or losses £m
2019								
Fair value hedging – interest rate								
Loans to banks and customers - amortised cost	—	—	—	—	—	—	—	—
Other financial assets - securities	2,837	70	64	—	2,837	70	64	—
	2,837	70	64		2,837	70	64	
Fair value hedging - foreign exchange	—	—	—	—	—	—	—	—
Total assets	2,837	70	64	—	2,837	70	64	—
Other financial liabilities - debt securities in issue	12,013	206	(133)	—	12,013	206	(133)	—
Subordinated liabilities	104	1	—	—	—	—	—	—
Total liabilities	12,117	207	(133)	—	12,013	206	(133)	—
Cash flow hedge – interest rate								
Loans to banks and customers - amortised cost	5,580	—	(41)	—	5,580	—	(41)	—
Other financial assets - securities	791	—	(6)	—	791	—	(6)	—
Total	6,371	—	(47)	—	6,371	—	(47)	—

2018

Fair value hedging – interest rate								
Loans to banks and customers - amortised cost	63	9	—	31	—	—	—	—
Other financial assets - securities	888	(14)	(15)	—	888	(14)	(15)	—
	951	(5)	(15)	31	888	(14)	(15)	—
Fair value hedging - foreign exchange	—	—	—	—	502	44	—	20
Total assets	951	(5)	(15)	31	1,390	30	(15)	20
Other financial liabilities - debt securities in issue	8,652	78	—	—	8,652	78	—	—
Subordinated liabilities	—	—	—	—	—	—	—	—
Total liabilities	8,652	78	—	—	8,652	78	—	—
Cash flow hedge – interest rate								
Loans to banks and customers - amortised cost	5,768	—	(18)	—	5,768	—	(18)	—
Other financial assets - securities	—	—	—	—	—	—	—	—
Total	5,768	—	(18.0)	—	5,768	—	(18.0)	—

Note:

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

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

	Notional £bn	Fair value £m
Fair value hedging		
- LIBOR	7.6	(83)
- EURIBOR	5.5	(52)
Cash flow hedging		
- LIBOR	2.1	(66)
- BOE Base rate	2.9	(113)

Notes on the accounts

10 Derivatives continued

Hedge ineffectiveness recognised in other operating income in continuing operations comprised:

	NWM Group	
	2019 £m	2018 £m
Fair value hedging		
Losses on the hedged items attributable to the hedged risk	(69)	(15)
Gains on the hedging instruments	68	15
Fair value hedging ineffectiveness	(1)	—
Cash flow hedging		
- Interest rate risk	7	(1)
Cash flow hedging ineffectiveness	7	(1)
Total	6	(1)

Note:

(1) Hedge ineffectiveness recognised in other operating income in discontinued operations was nil in 2019 (2018 - £88 million debit).

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); and
- 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).

Additional information on cash flow hedging and net interest hedging can be found in the Statement of Changes in Equity.

Notes on the accounts

11 Financial instruments - classification

The following tables analyse NWM Group's financial assets and liabilities in accordance with the categories of financial instruments in IFRS 9. Assets and liabilities outside the scope of IFRS 9 are shown within other assets and other liabilities.

	NWM Group				
	MFVTPL (1) £m	FVOCI (2) £m	Amortised cost £m	Other assets £m	Total £m
Assets					
Cash and balances at central banks			12,729		12,729
Trading assets	76,540				76,540
Derivatives (3)	148,696				148,696
Settlement balances			4,339		4,339
Loans to banks - amortised cost (4)			1,088		1,088
Loans to customers - amortised cost			8,361		8,361
Amounts due from holding company and fellow subsidiaries	438	—	753	40	1,231
Other financial assets	392	7,929	3,984		12,305
Other assets				847	847
31 December 2019	226,066	7,929	31,254	887	266,136

Cash and balances at central banks			11,188		11,188
Trading assets	74,972				74,972
Derivatives (3)	134,250				134,250
Settlement balances			2,705		2,705
Loans to banks - amortised cost (4)			626		626
Loans to customers - amortised cost			8,366		8,366
Amounts due from holding company and fellow subsidiaries	1,177	—	1,991	230	3,398
Other financial assets	1,134	7,436	2,698		11,268
Other assets				1,108	1,108
31 December 2018	211,533	7,436	27,574	1,338	247,881

	NWM Group				
	Held-for- trading £m	DFV (5) £m	Amortised cost £m	Other liabilities £m	Total £m
Liabilities					
Bank deposits			2,089		2,089
Customer deposits			3,703		3,703
Amounts due to holding company and fellow subsidiaries	491	—	7,641	168	8,300
Settlement balances			4,022		4,022
Trading liabilities	73,836				73,836
Derivatives (3)	144,142				144,142
Other financial liabilities (6)		2,980	15,465		18,445
Other liabilities (7)			4	1,685	1,689
31 December 2019	218,469	2,980	32,924	1,853	256,226
Bank deposits			2,749		2,749
Customer deposits			2,580		2,580
Amounts due to holding company and fellow subsidiaries	419	—	9,485	257	10,161
Settlement balances			2,914		2,914
Trading liabilities	72,289				72,289
Derivatives (3)	129,914				129,914
Other financial liabilities (6)		3,049	13,230		16,279
Other liabilities			—	1,906	1,906
31 December 2018	202,622	3,049	30,958	2,163	238,792

For the notes to the above tables refer to the following page.

Notes on the accounts

11 Financial instruments - classification continued

Amounts due from/to holding company and fellow subsidiaries are as below:

	NWM Group					
	2019			2018		
	Holding company £m	Fellow subsidiaries £m	Total £m	Holding company £m	Fellow subsidiaries £m	Total £m
Assets						
Loans to banks and customers	423	754	1,177	144	3,024	3,168
Settlement balances	—	14	14	—	—	—
Other assets	—	40	40	—	230	230
Total inter-group assets	423	808	1,231	144	3,254	3,398
<i>Not included above:</i>						
Derivatives	421	594	1,015	376	813	1,189
Liabilities						
Bank and customer deposits	—	989	989	64	2,751	2,815
CRR-compliant internal MREL	5,120	—	5,120	5,125	—	5,125
Settlement balances	—	3	3	—	2	2
Other financial liabilities - subordinated liabilities	2,020	—	2,020	1,962	—	1,962
Other liabilities	—	168	168	—	257	257
Total inter-group liabilities	7,140	1,160	8,300	7,151	3,010	10,161
<i>Not included above:</i>						
Derivatives	712	337	1,049	476	703	1,179

Notes:

- (1) Mandatory fair value through profit or loss.
- (2) Fair value through other comprehensive income.
- (3) Includes net hedging derivative assets of £179 million (2018 - £53 million) and net hedging derivative liabilities of £1 million (2018 - £19 million).
- (4) Includes items in the course of collection from other banks of £11 million (2018 - £27 million).
- (5) Designated as at fair value through profit or loss.
- (6) There are no customer accounts designated as at fair value through profit or loss (2018 - nil) with a carrying value higher than the principal amount. No amounts have been recognised in profit or loss for changes in credit risk associated with these liabilities as the changes are immaterial both during the period and cumulatively.
- (7) Includes lease liabilities.

NWM Group's financial assets and liabilities include:

	NWM Group	
	2019 £m	2018 £m
Reverse repos		
Loans to banks - amortised cost	2	—
Loans to customers - amortised cost	12	9
Trading assets	24,095	24,758
Repos		
Bank deposits	380	424
Trading liabilities	27,885	25,645

Notes on the accounts

11 Financial instruments - classification continued

The following tables show the bank's financial assets and financial liabilities in accordance with the categories of financial instruments in IFRS 9. Assets and liabilities outside the scope of IFRS 9 are shown within other assets and other liabilities.

	NWM Plc				
	MFVTPL (1) £m	FVOCI (2) £m	Amortised cost £m	Other assets £m	Total £m
Assets					
Cash and balances at central banks			9,953		9,953
Trading assets	57,768				57,768
Derivatives (3)	147,458				147,458
Settlement balances			3,353		3,353
Loans to banks - amortised cost (4)			238		238
Loans to customers - amortised cost			6,910		6,910
Amounts due from holding company and fellow subsidiaries	3,336	—	3,748	61	7,145
Other financial assets	381	7,301	3,954		11,636
Investment in group undertakings				2,905	2,905
Other assets				687	687
31 December 2019	208,943	7,301	28,156	3,653	248,053
Cash and balances at central banks			11,095		11,095
Trading assets	61,990				61,990
Derivatives (3)	134,291				134,291
Settlement balances			1,421		1,421
Loans to banks - amortised cost (4)			454		454
Loans to customers - amortised cost			7,908		7,908
Amounts due from holding company and fellow subsidiaries	2,119	—	9,451	230	11,800
Other financial assets	1,127	7,170	2,698		10,995
Investment in group undertakings				1,151	1,151
Other assets				936	936
31 December 2018	199,527	7,170	33,027	2,317	242,041
	NWM Plc				
	Held-for- trading £m	DFV (5) £m	Amortised cost £m	Other liabilities £m	Total £m
Liabilities					
Bank deposits			2,038		2,038
Customer deposits			2,247		2,247
Amounts due to holding company and fellow subsidiaries	7,118	—	9,569	171	16,858
Settlement balances			2,648		2,648
Trading liabilities	53,576				53,576
Derivatives (3)	142,390				142,390
Other financial liabilities (6)		2,430	15,040		17,470
Other liabilities (7)			4	1,191	1,195
31 December 2019	203,084	2,430	31,546	1,362	238,422
Bank deposits			2,777		2,777
Customer deposits			2,390		2,390
Amounts due to holding company and fellow subsidiaries	7,501	—	15,720	284	23,505
Settlement balances			1,977		1,977
Trading liabilities	54,540				54,540
Derivatives (3)	129,974				129,974
Other financial liabilities (6)		3,049	13,230		16,279
Other liabilities			51	1,626	1,677
31 December 2018	192,015	3,049	36,145	1,910	233,119

For the notes to the above tables refer to the following page.

Notes on the accounts

11 Financial instruments - classification continued

Amounts due from/to holding company and fellow subsidiaries are as below:

	NWM Plc							
	2019		2018		2019		2018	
	Holding company £m	Fellow subsidiaries £m	Subsidiaries £m	Total £m	Holding company £m	Fellow subsidiaries £m	Subsidiaries £m	Total £m
Assets								
Loans to banks and customers	307	501	5,522	6,330	144	2,118	9,308	11,570
Settlement balances	—	14	27	41	—	—	—	—
Other financial assets	—	—	713	713	—	—	—	—
Other assets	—	23	38	61	—	—	230	230
Total inter-group assets	307	538	6,300	7,145	144	2,118	9,538	11,800
<i>Not included above:</i>								
Derivatives	421	599	880	1,900	376	812	42	1,230
Liabilities								
Bank and customer deposits	—	925	8,571	9,496	32	2,938	12,871	15,841
CRR-compliant internal MREL	5,120	—	—	5,120	5,125	—	—	5,125
Settlement balances	—	3	48	51	—	2	291	293
Other financial liabilities - subordinated liabilities	2,020	—	—	2,020	1,962	—	—	1,962
Other liabilities	—	148	23	171	—	—	284	284
Total inter-group liabilities	7,140	1,076	8,642	16,858	7,119	2,940	13,446	23,505
<i>Not included above:</i>								
Derivatives	712	342	1,303	2,357	476	646	116	1,238

Notes:

- (1) Mandatory fair value through profit or loss.
- (2) Fair value through other comprehensive income.
- (3) Includes net hedging derivative assets of £179 million (2018 - £54 million) and net hedging derivative liabilities of £1 million (2018 - £10 million).
- (4) Includes items in the course of collection from other banks of £11 million (2018 - £27 million).
- (5) Designated as at fair value through profit or loss.
- (6) There are no customer accounts designated as at fair value through profit or loss (2018 - nil) with a carrying value higher than the principal amount. No amounts have been recognised in profit or loss for changes in credit risk associated with these liabilities as the changes are immaterial both during the period and cumulatively.
- (7) Includes lease liabilities.

NWM Plc's financial assets and liabilities include:

	NWM Plc	
	2019 £m	2018 £m
Reverse repos		
Loans to banks - amortised cost	2	—
Loans to customers - amortised cost	12	9
Trading assets	12,716	15,915
Repos		
Bank deposits	380	424
Trading liabilities	10,007	9,784

Notes on the accounts

11 Financial instruments - classification continued

The tables below present information on financial assets and liabilities that are offset on the balance sheet under IFRS or subject to enforceable master netting agreements together with financial collateral received or given.

	NWM Group								
	Instruments which can be offset			Potential to offset not recognised by IFRS				Instruments outside netting agreements	
	Gross £m	IFRS offset £m	Balance sheet £m	Effect of master netting and similar agreements £m	Cash collateral £m	Other financial collateral £m	Net amount after the effect of netting agreements and related collateral £m	£m	Balance sheet total £m
2019									
Derivative assets	150,524	(3,876)	146,648	(120,776)	(18,682)	(4,292)	2,898	2,048	148,696
Derivative liabilities	144,008	(4,011)	139,997	(120,776)	(17,187)	(1,276)	758	4,145	144,142
Net position (1)	6,516	135	6,651	—	(1,495)	(3,016)	2,140	(2,097)	4,554
Trading reverse repos	52,007	(28,720)	23,287	(562)	—	(22,262)	463	808	24,095
Trading repos	54,131	(28,720)	25,411	(562)	—	(24,808)	41	2,474	27,885
Net position	(2,124)	—	(2,124)	—	—	2,546	422	(1,666)	(3,790)
2018									
Derivative assets	134,081	(2,072)	132,009	(106,762)	(17,930)	(4,469)	2,848	2,241	134,250
Derivative liabilities	130,342	(2,438)	127,904	(106,762)	(15,224)	(3,466)	2,452	2,010	129,914
Net position (1)	3,739	366	4,105	—	(2,706)	(1,003)	396	231	4,336
Trading reverse repos	53,148	(31,376)	21,772	(762)	—	(21,000)	10	2,986	24,758
Trading repos	55,864	(31,376)	24,488	(762)	—	(23,726)	—	1,157	25,645
Net position	(2,716)	—	(2,716)	—	—	2,726	10	1,829	(887)

Note:

(1) The net IFRS offset balance of £135 million (2018 - £366 million) relates to variation margin netting reflected on other balance sheet lines.

	NWM Plc								
	Instruments which can be offset			Potential to offset not recognised by IFRS				Instruments outside netting agreements	
	Gross £m	IFRS offset £m	Balance sheet £m	Effect of master netting and similar agreements £m	Cash collateral £m	Other financial collateral £m	Net amount after the effect of netting agreements and related collateral £m	£m	Balance sheet total £m
2019									
Derivative assets	151,324	(3,872)	147,452	(120,409)	(18,183)	(4,202)	4,658	6	147,458
Derivative liabilities	146,391	(4,007)	142,384	(120,409)	(16,099)	(1,276)	4,600	6	142,390
Net position (1)	4,933	135	5,068	—	(2,084)	(2,926)	58	—	5,068
Trading reverse repos	27,327	(15,160)	12,167	(459)	—	(11,428)	280	549	12,716
Trading repos	22,692	(15,160)	7,532	(459)	—	(7,073)	—	2,475	10,007
Net position	4,635	—	4,635	—	—	(4,355)	280	(1,926)	2,709
2018									
Derivative assets	135,903	(2,072)	133,831	(106,762)	(17,930)	(4,469)	4,670	460	134,291
Derivative liabilities	131,940	(2,438)	129,502	(106,762)	(15,224)	(3,466)	4,050	472	129,974
Net position (1)	3,963	366	4,329	—	(2,706)	(1,003)	620	(12)	4,317
Trading reverse repos	30,895	(17,967)	12,928	(523)	—	(12,405)	—	2,987	15,915
Trading repos	26,593	(17,967)	8,626	(523)	—	(8,103)	—	1,158	9,784
Net position	4,302	—	4,302	—	—	(4,302)	—	1,829	6,131

Note:

(1) The net IFRS offset balance of £135 million (2018 - £366 million) relates to variation margin netting reflected on other balance sheet lines.

Notes on the accounts

12 Financial instruments - valuation

Critical accounting policy: Fair value - financial instruments

In accordance with Accounting policies 10 and 18, financial instruments at 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, NWM Group maximises the use of relevant observable inputs and minimises the use of unobservable inputs.

Where NWM 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.

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.

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. Expert judgement is used in the initial measurement of modelled products by control teams.

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.

	2019			2018		
	Level 1 £m	Level 2 £m	Level 3 £m	Level 1 £m	Level 2 £m	Level 3 £m
Assets						
Trading assets						
Loans	—	45,967	449	—	44,838	120
Securities	20,865	8,704	555	22,003	7,312	699
Derivatives	—	147,285	1,411	—	132,346	1,904
Amounts due from holding company and fellow subsidiaries	—	438	—	—	1,177	—
Other financial assets						
Loans	—	18	58	—	374	86
Securities	6,428	1,787	30	6,706	959	445
Total financial assets held at fair value	27,293	204,199	2,503	28,709	187,006	3,254
Liabilities						
Amounts due to holding company and fellow subsidiaries	—	491	—	—	413	6
Trading liabilities						
Deposits	—	50,831	56	—	47,183	377
Debt securities in issue	—	1,703	59	—	790	112
Short positions	15,565	5,622	—	18,941	4,886	—
Derivatives	—	143,009	1,133	—	128,638	1,276
Other financial liabilities						
Debt securities in issue	—	2,115	141	—	2,344	280
Subordinated liabilities	—	724	—	—	425	—
Total financial liabilities held at fair value	15,565	204,495	1,389	18,941	184,679	2,051

Notes:

- (1) Transfers between levels are deemed to have occurred at the beginning of the quarter in which the instruments were transferred. There were no significant transfers between level 1 and level 2.
- (2) For an analysis of debt securities held at mandatorily fair value through profit or loss by issuer as well as ratings and derivatives, by type and contract, refer to Capital and Risk management – Credit risk.
- (3) The determination of an instrument's level cannot be made at a global product level as a single product type can be in more than one level. For example, a single name corporate credit default swap could be in level 2 or level 3 depending on whether the reference counterparty's obligations are liquid or illiquid.

Notes on the accounts

12 Financial instruments – valuation continued

Valuation of financial instruments carried at fair value

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 CLOs, 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 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 instruments and derivatives with unobservable model inputs.

Valuation Techniques

NWM Group derives the 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. Examples include equities and most debt securities.

Products that are priced using models range in complexity from comparatively vanilla such as interest rate swaps and loans through to more complex derivatives and structured note issuance. The valuation of modelled products requires an appropriate model and inputs into this model.

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 observable prices of credit default swaps, or other credit based instruments such as debt securities, or market data providers. Where such prices are not available credit spreads are determined with reference to available prices of entities with similar characteristics.

Interest rates – these are principally benchmark interest rates such as the London Interbank Offered Rate (LIBOR), Overnight Index Swaps (OIS) rate and other quoted interest rates in the swap, bond and futures markets.

Foreign currency exchange rates – there generally are observable prices both for spot and forward contracts and futures in the world's major currencies.

Equity and equity index prices – quoted prices are generally readily available for equity shares listed on the world's major stock exchanges and for 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 to 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 pre-payable instruments that are not quoted in active markets, NWM Group considers the value of the prepayment option.

Recovery rates/loss given default – these are used as an input to valuation models and reserves as an indicator of severity of losses on default. Recovery rates are primarily sourced from market data providers, inferred from observable credit spreads or historically realised levels.

Valuation Control

NWM Group's control environment for the determination of the fair value of financial instruments includes formalised protocols for the review and validation of fair values independent of the businesses entering into the transactions.

Independent Price Verification (IPV) is a key element of the control environment. Valuations are first performed by the business which owns the transaction. Such valuations may be directly from available prices, or may be derived using a model and variable model inputs. These valuations are reviewed, and if necessary amended, by a team independent of those trading the financial instruments, in the light of available pricing evidence.

Where measurement differences are identified through the IPV process these are grouped by fair value level and quality of data. If the size of the difference exceeds defined thresholds then valuation adjustments are made reflecting the independent levels.

IPV takes place at least each month for all fair value positions. The IPV control includes formalised reporting and escalation of any valuation differences in breach of established thresholds.

The Modelled Product Review Committee sets the policy for model documentation, testing and review, and prioritises models with significant exposure being reviewed by the Model Risk team.

The NatWest Markets Valuation Committees are made up of valuation specialists and senior business representatives from various functions. The committees meet monthly to review pricing, reserving and valuation issues along with methodology changes. The RBS Group Executive Valuation Committee meets quarterly to address key material and subjective valuation issues and to review items escalated by the Valuation Committees.

Initial classification of a financial instrument is carried out by the Product Control team following the principles in IFRS 13. They base their judgment on information gathered during the IPV process for instruments which include the sourcing of independent prices and model inputs. The quality and completeness of the information gathered in the IPV process gives an indication as to the liquidity and valuation uncertainty of an instrument.

Notes on the accounts

12 Financial instruments - valuation continued

These initial classifications are subject to senior management review. Particular attention is paid to instruments crossing from one level to another, new instrument classes or products, instruments that are generating significant profit and loss and instruments where valuation uncertainty is high.

NWM Group uses consensus prices for the IPV of some instruments. The consensus service encompasses the equity, interest rate, currency, commodity, credit, property, fund and bond markets, providing comprehensive matrices of vanilla prices and a wide selection of exotic products. NWM Group contributes to consensus pricing services where there is a significant interest from a positional point of view. Data sourced from consensus pricing services are used for a combination of control processes including direct price testing, evidence of observability and model testing. In practice this means that NWM Group submits prices for all material positions for which a service is available.

Data from consensus services are subject to the same level of quality review as other inputs used for IPV process. All sources of independent data are reviewed for quality and are applied in the IPV processes using a formalised input quality hierarchy.

In order to determine a reliable fair value, where appropriate, management applies IPV valuation adjustments based on the pricing information gathered from the above sources. These adjustments reflect NWM Group's assessment of factors that market participants would consider in setting a price.

Where unobservable inputs are used, NWM Group may determine a range of possible valuations derived from different stress scenarios to determine the sensitivity associated with the valuation. When establishing the fair value of a financial instrument using a valuation technique, NWM Group considers adjustments to the modelled price which market participants would make when pricing that instrument. Such adjustments include the credit quality of the counterparty, funding and adjustments to compensate for model limitations.

When valuing financial instruments in the trading book, adjustments are made to mid-market valuations to cover bid-offer spread, funding and credit risk. These adjustments are presented in the table below.

	2019 £m	2018 £m
Funding – FVA	193	250
Credit – CVA	384	326
Bid – Offer	138	238
Product and deal specific	238	324
	953	1,138

The reduction in valuation reserves was primarily driven by a combination of market moves, trade close-out activity and risk reduction together with a reallocation of product and deal specific reserves that are now included within modelled trade valuations. There was a net increase in CVA due to the inclusion of NWM NV valuation reserves following this entity becoming part of the NWM Plc Group in the period.

Funding valuation adjustment (FVA)

FVA represents an estimate of the adjustment that a market participant would make to incorporate funding costs and benefits that arise in relation to derivative exposures. FVA is calculated as a portfolio level adjustment and can result in either a funding charge or funding benefit.

Funding levels are applied to estimated potential future exposures. For uncollateralised derivatives, the exposure reflects the future valuation of the derivative, and the counterparty contingent nature of the exposure is reflected in the calculation. For collateralised derivatives, the exposure reflects initial margin posting requirements.

Credit valuation adjustments (CVA)

CVA represents an estimate of the adjustment to fair value that a market participant would make to incorporate the counterparty credit risk inherent in derivative exposures. CVA is calculated as a portfolio level adjustment.

Collateral held under a credit support agreement is factored into the CVA calculation. In such cases where NWM Group holds collateral against counterparty exposures, CVA is held to the extent that residual risk remains.

Bid-offer

Fair value positions are adjusted to bid (long positions) or offer (short positions) levels, by marking individual cash positions directly to bid or offer or by taking bid-offer reserves calculated on a portfolio basis for derivatives exposures. The bid-offer approach is based on current market spreads and standard market bucketing of risk.

Bid-offer spreads vary by maturity and risk type to reflect different spreads in the market. For positions where there is no observable quote, the bid-offer spreads are widened in comparison to proxies to reflect reduced liquidity or observability. Bid-offer methodologies may also incorporate liquidity triggers whereby wider spreads are applied to risks above pre-defined thresholds.

Product and deal specific

On initial recognition of financial assets and liabilities valued using valuation techniques incorporating information other than observable market data, any difference between the transaction price and that derived from the valuation technique is deferred. Such amounts are recognised in profit or loss over the life of the transaction; when market data becomes observable; or when the transaction matures or is closed out as appropriate. At 31 December 2019, net gains of £88 million (2018 - £59 million) were carried forward. During the year, net gains of £183 million (2018 - £151 million) were deferred and £154 million (2018 - £148 million) were recognised in the income statement.

Where system generated valuations do not accurately recover market prices, manual valuation adjustments are applied either at a position or portfolio level. Manual adjustments are subject to the scrutiny of independent control teams and are subject to monthly review by senior management.

Own Credit

NWM Group takes into account the effect of its own credit standing when valuing financial liabilities recorded at fair value in accordance with IFRS. Own credit spread adjustments are made when valuing issued debt held at fair value, including issued structured notes. An own credit adjustment is applied to positions where it is believed that counterparties would consider NWM Group's creditworthiness when pricing trades.

Notes on the accounts

12 Financial instruments – valuation: Level 3 ranges of unobservable inputs continued

Financial instrument	Valuation Technique	Unobservable inputs	Units	2019		2018	
				Low	High	Low	High
Trading assets and Other financial assets							
Loans	Price-based	Price	%	—	101	—	132
	Credit spreads	Credit spreads	bps	53	101	—	—
Debt securities	Price-based	Price	%	—	246	—	154
Equity Shares	Price-based	Price	GBP	—	25,914	—	24,181
		Price	%	—	80	—	—
	Valuation	Discount factor	%	—	—	8	11
		Fund NAV	%	80	120	80	120
Trading liabilities and Other financial liabilities							
Deposits	DCF based on recoveries	Correlation	%	—	—	(45)	99
		Interest rate	%	—	—	(0.36)	1.74
	Price-based	Price	%	—	98	—	—
	Yield analysis	Day count	Number	65	95	—	—
Debt securities in issue	Price-based	Price	CCY	44 JPY	146 EUR	21 JPY	136 EUR
	Valuation	Fund NAV	GBP	—	—	—	622
Derivative assets and liabilities							
Credit derivatives	DCF based on recoveries	Credit spreads	bps	6	500	18	500
		Option pricing	Correlation	%	(50)	80	(50)
	Option pricing	Volatility	%	27	80	47	80
		Upfront points	%	—	99	—	100
		Recovery rate	%	10	40	10	40
		Price	%	—	—	90	110
	Price-based	Price	%	—	—	90	110
		Price	%	—	—	90	110
Interest rate & FX derivatives	Option pricing	Correlation	%	(50)	99	(45)	99
		Volatility	%	19	70	1	76
		Constant					
		Prepayment rate	%	2	15	—	—
		Mean reversion	%	—	92	—	—
		CSA Volatility	bps	8	27	—	—
Equity derivatives	Option pricing	Correlation	%	(53)	87	(57)	92
		Forward	Points	—	—	864	7,106
		Volatility	%	—	—	11	23

Notes:

- (1) The table above presents the range of values for significant inputs used in the valuation of level 3 assets and liabilities. The range represents the highest and lowest values of the input parameters and therefore is not a measure of parameter uncertainty. Movements in the underlying input may have a favourable or unfavourable impact on the valuation depending on the particular terms of the contract and the exposure. For example, an increase in the credit spread of a bond would be favourable for the issuer but unfavourable for the note holder. Whilst RBS indicates where it considers that there are significant relationships between the inputs, their inter-relationships will be affected by macro economic factors including interest rates, foreign exchange rates or equity index levels.
- (2) Credit spreads and discount margins: credit spreads and margins express the return required over a benchmark rate or index to compensate for the credit risk associated with a cash instrument. A higher credit spread would indicate that the underlying instrument has more credit risk associated with it. Consequently, investors require a higher yield to compensate for the higher risk.
- (3) Price and yield: There may be a range of prices used to value an instrument that may be a direct comparison of one instrument or portfolio with another or, movements in a more liquid instrument may be used to indicate the movement in the value of a less liquid instrument. The comparison may also be indirect in that adjustments are made to the price to reflect differences between the pricing source and the instrument being valued.
- (4) Recovery rate: reflects market expectations about the return of principal for a debt instrument or other obligations after a credit event or on liquidation. Recovery rates tend to move conversely to credit spreads.
- (5) Valuation: for private equity investments, values may be estimated by looking at past prices of similar stocks and from valuation statements where valuations are usually derived from earnings measures such as EBITDA or net asset value (NAV). Similarly for equity or bond fund investments, prices may be estimated from valuation or credit statements using NAV or similar measures.
- (6) Correlation: measures the degree by which two prices or other variables are observed to move together. If they move in the same direction there is positive correlation; if they move in opposite directions there is negative correlation. Correlations typically include relationships between: default probabilities of assets in a basket (a group of separate assets), exchange rates, interest rates and other financial variables.
- (7) Volatility: a measure of the tendency of a price to change with time.
- (8) Interest rate delta: these ranges represent the low/high marks on the relevant discounting curve.
- (9) Upfront points: where CDS contracts are standardised, the inherent spread of the trade may exceed the standard premium paid or received under the contract. Upfront points will compensate for the difference between the standard premium and the actual premium at the start of the contract.
- (10) Mean reversion: a measure of how much a rate reverts to its mean level.
- (11) Constant prepayment rate: the rate is used to reflect how fast a pool of assets pay down.
- (12) Day count: yield analysis on deposits are calculated using day count as an input, referring to the maturity of the deposit.
- (13) NWM Group does not have any material liabilities measured at fair value that are issued with an inseparable third party credit enhancement.

Notes on the accounts

12 Financial instruments – valuation: Level 3 ranges of unobservable inputs continued

Areas of judgement

Whilst the business has simplified, the diverse range of products historically traded by NWM Group results in a wide range of instruments that are classified into Level 3 of the hierarchy. Whilst the majority of these instruments naturally fall into a particular level, for some products an element of judgment is required. The majority of NWM Group's financial instruments carried at fair value are classified as level 2. IFRS requires extra disclosures in respect of level 3 instruments.

Active and inactive markets

A key input in the decision making process for the allocation of assets to a particular level is market activity. In general, the degree of valuation uncertainty depends on the degree of liquidity of an input. Where markets are liquid, little judgment is required. However, when the information regarding the liquidity in a particular market is not clear, a judgment may need to be made. This can be more difficult as assessing the liquidity of a market is not always straightforward. For an equity traded on an exchange, daily volumes of trading can be seen, but for an over-the-counter (OTC) derivative assessing the liquidity of the market with no central exchange is more difficult.

A key related matter is where a market moves from liquid to illiquid or vice versa. Where this change is considered to be temporary, the classification is not changed. For example, if there is little market trading in a product on a reporting date but at the previous reporting date and during the intervening period the market has been considered to be liquid, the instrument will continue to be classified in the same level in the hierarchy. This is to provide consistency so that transfers between levels are driven by genuine changes in market liquidity and do not reflect short term or seasonal effects.

Material movements between levels are reviewed quarterly. The breadth and depth of the IPV data allows for a rules based quality assessment to be made of market activity, liquidity and pricing uncertainty, which assists with the process of allocation to an appropriate level. Where suitable independent pricing information is not readily available, the quality assessment will result in the instrument being assessed as level 3.

Modelled products

For modelled products the market convention is to quote these trades through the model inputs or parameters as opposed to a cash price equivalent. A mark-to-market is derived from the use of the independent market inputs calculated using NWM Group's model.

The decision to classify a modelled instrument as level 2 or 3 will be dependent upon the product/model combination, the observability and quality of input parameters and other factors. All these must be assessed to classify the asset.

If an input fails the observability or quality tests then the instrument is considered to be in level 3 unless the input can be shown to have an insignificant effect on the overall valuation of the product.

The majority of derivative instruments for example vanilla interest rate swaps, foreign exchange swaps and liquid single name credit derivatives are classified as level 2 as they are vanilla products valued using observable inputs. The valuation uncertainty on these is considered to be low and both input and output testing may be available.

Non-modelled products

Non-modelled products are generally quoted on a price basis and can therefore be considered for each of the three levels. This is determined by the market activity, liquidity and valuation uncertainty of the instruments which is in turn measured from the availability of independent data used by the IPV process to allocate positions to IPV quality levels.

The availability and quality of independent pricing information are considered during the classification process. An assessment is made regarding the quality of the independent information. For example, where consensus prices are used for non-modelled products, a key assessment of the quality of a price is the depth of the number of prices used to provide the consensus price. If the depth of contributors falls below a set hurdle rate, the instrument is considered to be level 3. This hurdle rate is that used in the IPV process to determine the IPV quality rating. However, where an instrument is generally considered to be illiquid, but regular quotes from market participants exist, these instruments may be classified as level 2 depending on frequency of quotes, other available pricing and whether the quotes are used as part of the IPV process or not.

For some instruments with a wide number of available price sources, there may be differing quality of available information and there may be a wide range of prices from different sources. In these situations the highest quality source is used to determine the classification of the asset. For example, a tradable quote would be considered a better source than a consensus price.

	2019			2018		
	Level 3 £m	Favourable £m	Unfavourable £m	Level 3 £m	Favourable £m	Unfavourable £m
Assets						
Trading assets						
Loans	449	10	(10)	120	10	(10)
Securities	555	—	—	699	20	(10)
Derivatives						
Interest rate	1,015	160	(160)	1,363	110	(110)
Foreign exchange	98	10	(10)	130	10	(10)
Other	298	80	(60)	411	40	(40)
Other financial assets						
Loans	58	—	—	86	—	(10)
Securities	30	—	—	445	40	(20)
	2,503	260	(240)	3,254	230	(210)
Liabilities						
Amounts due to holding company and fellow subsidiaries	—	—	—	6	—	—
Trading liabilities						
Deposits	56	—	—	377	40	(40)
Debt securities in issue	59	—	—	112	10	(10)
Derivatives						
Interest rate	630	70	(70)	805	70	(70)
Foreign exchange	222	10	(10)	279	10	(10)
Other	281	20	(20)	192	10	(10)
Other financial liabilities - debt securities in issue	141	10	(10)	280	10	(10)
	1,389	110	(110)	2,051	150	(150)

Notes on the accounts

12 Financial instruments – valuation: Level 3 ranges of unobservable inputs continued

Reasonably plausible alternative assumptions of unobservable inputs are determined based on specified target level of certainty of 90%. The assessments recognise different favourable and unfavourable valuation movements where appropriate. Each unobservable input within a product is considered separately and sensitivity is reported on an additive basis.

Alternative assumptions are determined with reference to all available evidence including consideration of the following: quality of independent pricing information taking into account consistency between different sources, variation over time, perceived tradability or otherwise of available quotes; consensus service dispersion ranges; volume of trading activity and market bias (e.g. one-way inventory); day 1 profit or loss arising on new trades; number and nature of

market participants; market conditions; modelling consistency in the market; size and nature of risk; length of holding of position; and market intelligence.

Other considerations

Whilst certain inputs used to calculate CVA, FVA and own credit adjustments are not based on observable market data, in general the uncertainty of the inputs is not assessed to have a significant effect on the net valuation of the related derivative portfolios and issued debt. Therefore, in general, the classification of the derivative portfolios and issued debt is not determined by the observability of these inputs, and any related sensitivity does not form part of the level 3 sensitivities presented.

Level 3

The following table shows the movement in level 3 assets and liabilities in the year.

	2019				2018			
	Trading assets (2) £m	Other financial assets (3) £m	Total assets £m	Total liabilities £m	Trading assets (2) £m	Other financial assets (3) £m	Total assets £m	Total liabilities £m
At 1 January	2,723	531	3,254	2,051	2,681	282	2,963	2,096
Amounts recorded in the income statement (1)	(396)	—	(396)	126	(104)	154	50	(244)
Amounts recorded in the statement of comprehensive income	—	34	34	—	—	(2)	(2)	—
Level 3 transfers in	463	2	465	98	1,219	19	1,238	476
Level 3 transfers out	(867)	(139)	(1,006)	(577)	(624)	(1)	(625)	(235)
Transfer from/(to) to disposal groups	—	—	—	—	41	173	214	43
Issuances	—	—	—	46	—	—	—	47
Purchases	1,501	13	1,514	597	880	4	884	404
Settlements	(247)	(39)	(286)	(421)	(455)	—	(455)	(208)
Sales	(759)	(314)	(1,073)	(530)	(915)	(102)	(1,017)	(328)
Foreign exchange and other adjustments	(3)	—	(3)	(1)	—	4	4	—
At 31 December	2,415	88	2,503	1,389	2,723	531	3,254	2,051

Amounts recorded in the income statement in respect of balances held at year end:

- unrealised	(395)	10	(385)	126	(142)	203	61	(235)
- realised	—	—	—	—	(2)	3	1	—

Notes:

- (1) Net losses on trading assets and liabilities of £538 million (2018 – £128 million gains) were recorded in income from trading activities. Net gain on other instruments of £16 million (2018 – £166 million) were recorded in other operating income and interest income as appropriate.
- (2) Trading assets comprise assets held at fair value in trading portfolios.
- (3) Other financial assets comprise fair value through other comprehensive income, designated as at fair value through profit or loss and other fair value through profit or loss.

The following table shows the carrying value and fair value of financial instruments carried at amortised cost on the balance sheet:

	NWM Group					NWM Plc				
	Items where fair value approximates carrying value £bn	Carrying value £bn	Fair value £bn	Fair value hierarchy Level 2 £bn	Fair value hierarchy Level 3 £bn	Items where fair value approximates carrying value £bn	Carrying value £bn	Fair value £bn	Fair value hierarchy Level 2 £bn	Fair value hierarchy Level 3 £bn
2019										
Financial assets										
Cash and balances at central banks	12.7					10.0				
Settlement balances	4.3					3.4				
Loans to banks		1.1	1.1	0.2	0.9		0.2	0.2	—	0.2
Loans to customers		8.4	8.1	0.3	7.8		6.9	6.9	—	6.9
Amounts due from holding company and fellow subsidiaries	0.2	0.6	0.6	—	0.6	0.1	3.6	3.5	—	3.5
Other financial assets - securities		4.0	4.0	1.5	2.5		4.0	4.0	1.5	2.5
Financial liabilities										
Bank deposits		2.1	2.1	—	2.1		2.0	2.0	—	2.0
Customer deposits	0.9	2.8	2.8	—	2.8	0.5	1.7	1.8	—	1.8
Amounts due to holding company and fellow subsidiaries	0.1	7.5	7.7	7.3	0.4	0.3	9.3	9.6	7.3	2.3
Settlement balances	4.0					2.6				
Other financial liabilities										
Debt securities in issue		15.1	15.1	12.6	2.5		14.8	14.9	12.4	2.5
Subordinated liabilities		0.4	0.4	0.4	—		0.2	0.2	0.2	—

Notes on the accounts

12 Financial instruments: fair value of financial instruments not carried at fair value continued

2018	NWM Group					NWM Plc				
	Items where fair value approximates carrying value £bn	Carrying value £bn	Fair value £bn	Fair value hierarchy level		Items where fair value approximates carrying value £bn	Carrying value £bn	Fair value £bn	Fair value hierarchy level	
				Level 2 £bn	Level 3 £bn				Level 2 £bn	Level 3 £bn
Financial assets										
Cash and balances at central banks	11.2					11.1				
Settlement balances	2.7					1.4				
Loans to banks		0.6	0.6	0.3	0.3		0.5	0.4	0.2	0.2
Loans to customers		8.4	8.3	0.3	8.0		7.9	7.9	—	7.9
Amounts due from holding company and fellow subsidiaries	0.3	1.7	1.6	—	1.6	0.9	8.6	8.5	—	8.5
Other financial assets - securities		2.7	2.7	1.6	1.1		2.7	2.7	1.6	1.1
Financial liabilities										
Bank deposits		2.7	2.7	—	2.7		2.8	2.7	—	2.7
Customer deposits	0.9	1.7	1.7	—	1.7	0.7	1.7	1.7	—	1.7
Amounts due to holding company and fellow subsidiaries	3.9	5.6	5.6	—	5.6	4.5	11.2	11.2	—	11.2
Settlement balances	2.9					2.0				
Other financial liabilities										
Debt securities in issue		13.0	14.7	14.7	—		13.0	14.7	14.7	—
Subordinated liabilities		0.2	0.2	0.2	—		0.2	0.2	0.2	—

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. Furthermore there is a wide range of potential valuation techniques. 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 – amortised cost

In estimating the fair value of net loans to customers and banks measured at amortised cost, NWM Group's loans are segregated into appropriate portfolios reflecting the characteristics of the constituent loans. Two principal methods are used to estimate fair value:

- Contractual cash flows are discounted using a market discount rate that incorporates the current spread for the borrower or where this is not observable, the spread for borrowers of a similar credit standing. This method is used for institutional and corporate lending portfolios in NWM Plc, where counterparties have external ratings.
- Expected cash flows (unadjusted for credit losses) are discounted at the current offer rate for the same or similar products.

Debt securities

The majority of debt securities 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

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

Debt securities in issue and subordinated liabilities

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

Notes on the accounts

13 Financial instruments - maturity analysis

Remaining maturity

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

	NWM Group					
	2019			2018		
	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	12,729	—	12,729	11,188	—	11,188
Trading assets	51,620	24,920	76,540	48,982	25,990	74,972
Derivatives	40,667	108,029	148,696	28,606	105,644	134,250
Settlement balances	4,339	—	4,339	2,705	—	2,705
Loans to banks - amortised cost	1,083	5	1,088	588	38	626
Loans to customers - amortised cost	3,716	4,645	8,361	4,540	3,826	8,366
Amounts due from holding company and fellow subsidiaries (1)	950	241	1,191	2,980	188	3,168
Other financial assets	3,589	8,716	12,305	4,316	6,952	11,268
Liabilities						
Bank deposits	1,302	787	2,089	2,749	—	2,749
Customer deposits	3,176	527	3,703	2,549	31	2,580
Amounts due to holding company and fellow subsidiaries (2)	982	7,180	8,162	2,727	7,177	9,904
Settlement balances	4,022	—	4,022	2,914	—	2,914
Trading liabilities	52,934	20,902	73,836	50,608	21,681	72,289
Derivatives	41,214	102,928	144,142	29,250	100,664	129,914
Other financial liabilities	7,192	11,253	18,445	6,368	9,911	16,279
Lease liabilities	24	73	97			

	NWM Plc					
	2019			2018		
	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	9,953	—	9,953	11,095	—	11,095
Trading assets	36,902	20,866	57,768	39,873	22,117	61,990
Derivatives	40,729	106,729	147,458	28,607	105,684	134,291
Settlement balances	3,353	—	3,353	1,421	—	1,421
Loans to banks - amortised cost	233	5	238	416	38	454
Loans to customers - amortised cost	3,356	3,554	6,910	4,233	3,675	7,908
Amounts due from holding company and fellow subsidiaries (1)	4,004	3,080	7,084	8,027	3,543	11,570
Other financial assets	3,392	8,244	11,636	4,298	6,697	10,995
Liabilities						
Bank deposits	1,294	744	2,038	2,777	—	2,777
Customer deposits	2,217	30	2,247	2,361	29	2,390
Amounts due to holding company and fellow subsidiaries (2)	7,731	8,972	16,703	13,426	9,795	23,221
Settlement balances	2,648	—	2,648	1,977	—	1,977
Trading liabilities	34,176	19,400	53,576	34,508	20,032	54,540
Derivatives	41,356	101,034	142,390	29,198	100,776	129,974
Other financial liabilities	6,977	10,493	17,470	6,368	9,911	16,279
Lease liabilities	13	15	28			

Notes:

- (1) Amounts due from holding company and fellow subsidiaries relating to non-financial instruments of £40 million (2018 – £230 million) for NWM Group and £61 million (2018 - £230 million) for NWM Plc have been excluded from the tables.
- (2) Amounts due to holding company and fellow subsidiaries relating to non-financial instruments of £138 million (2018 - £257 million) for NWM Group and £155 million (2018 - £284 million) for NWM Plc have been excluded from the tables.

Notes on the accounts

13 Financial instruments - maturity analysis continued

Assets and liabilities by contractual cash flow maturity

The tables below 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 NWM 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 repayment 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, issued by certain securitisation vehicles consolidated by NWM Group 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 liabilities that are repayable after 20 years or where the counterparty has no right to repayment of the principal, are excluded from the table along with 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 NWM Group's liquidity position.

MFVTPL assets of £226 billion (2018 - £211 billion) for NWM Group, £209 billion (2018 - £199 billion) for NWM Plc, HFT liabilities of £218 billion (2018- £203 billion) for NWM Group and £203 billion (2018 - £192 billion) for NWM Plc have been excluded from the following tables.

2019	NWM 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						
Cash and balances at central banks	12,729	—	—	—	—	—
Settlement balances	4,339	—	—	—	—	—
Loans to banks - amortised cost	1,052	35	5	—	—	—
Amounts due from holding companies and fellow subsidiaries	511	—	1	27	7	207
Other financial assets	1,063	2,672	3,826	1,550	1,337	504
Total maturing assets	19,694	2,707	3,832	1,577	1,344	711
Loans to customers - amortised cost	1,920	1,922	2,170	1,881	455	198
Finance lease	—	4	19	7	13	25
Derivatives held for hedging	37	6	117	58	(40)	—
	21,651	4,639	6,138	3,523	1,772	934
Liabilities by contractual maturity						
Bank deposits	931	374	748	38	—	—
Amounts due to holding company and fellow subsidiaries	442	49	2,164	4,134	197	—
Settlement balances	4,022	—	—	—	—	—
Other financial liabilities	3,433	3,769	7,177	2,842	560	298
Other liabilities (1)	—	—	—	—	—	—
Total maturing liabilities	8,828	4,192	10,089	7,014	757	298
Customer deposits	1,915	1,273	520	1	—	17
Lease liabilities	11	13	35	12	20	6
Derivatives held for hedging	—	1	—	—	—	—
	10,754	5,479	10,644	7,027	777	321
Guarantees and commitments notional amount						
Guarantees (2)	972	—	—	—	—	—
Commitments (3)	14,472	—	—	—	—	—
	15,444	—	—	—	—	—

For notes to the above table refer to page 118.

Notes on the accounts

13 Financial instruments - maturity analysis continued

2018	NWM 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						
Cash and balances at central banks	11,188	—	—	—	—	—
Settlement balances	2,705	—	—	—	—	—
Loans to banks - amortised cost	526	66	39	—	—	—
Amounts due from holding companies and fellow subsidiaries	1,790	—	1	36	2	149
Other financial assets	1,701	2,628	2,759	946	816	223
Total maturing assets	17,910	2,694	2,799	982	818	372
Loans to customers - amortised cost	2,275	2,273	2,131	1,009	228	328
Finance lease	40	48	151	4	43	17
Derivatives held for hedging	40	56	152	48	7	—
	20,265	5,071	5,233	2,043	1,096	717

2018						
Liabilities by contractual maturity						
Bank deposits	2,728	21	—	—	—	—
Amounts due to holding company and fellow subsidiaries	2,094	211	41	5,453	920	59
Settlement balances	2,914	—	—	—	—	—
Other financial liabilities	1,302	5,066	6,494	2,359	837	200
Other liabilities (1)	45	—	—	—	—	—
Total maturing liabilities	9,083	5,298	6,535	7,812	1,757	259
Customer deposits	1,659	891	25	4	2	2
Derivatives held for hedging	—	10	26	6	(2)	1
	10,742	6,199	6,586	7,822	1,757	262

Guarantees and commitments notional amount

Guarantees (2)	278	—	—	—	—	—
Commitments (3)	8,927	—	—	—	—	—
	9,205	—	—	—	—	—

2019	NWM Plc					
	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						
Cash and balances at central banks	9,953	—	—	—	—	—
Settlement balances	3,353	—	—	—	—	—
Loans to banks - amortised cost	202	35	5	—	—	—
Amounts due from holding company and fellow subsidiaries	607	620	807	1,613	7	91
Other financial assets	1,045	2,490	3,695	1,382	1,258	460
Total maturing assets	15,160	3,145	4,507	2,995	1,265	551
Loans to customers - amortised cost	1,588	1,862	1,778	1,202	418	198
Finance lease	1	4	10	—	—	—
Derivatives held for hedging	37	6	81	52	2	—
	16,786	5,017	6,376	4,249	1,685	749

2019						
Liabilities by contractual maturity						
Bank deposits	922	374	706	38	—	—
Amounts due to holding company and fellow subsidiaries	736	126	2,839	4,763	421	—
Settlement balances	2,648	—	—	—	—	—
Other financial liabilities	3,428	3,548	7,158	2,614	470	234
Other liabilities (1)	—	—	—	—	—	—
Total maturing liabilities	7,734	4,048	10,703	7,415	891	234
Customer deposits	1,431	795	30	1	—	—
Lease liabilities	8	5	14	1	—	—
Derivatives held for hedging	—	1	—	—	—	—
	9,173	4,849	10,747	7,417	891	234
Guarantees and commitments notional amount						
Guarantees (2)	134	—	—	—	—	—
Commitments (3)	8,941	—	—	—	—	—
	9,075	—	—	—	—	—

For notes to the above table refer to the following page.

Notes on the accounts

13 Financial instruments - maturity analysis continued

2018	NWM Plc					
	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						
Cash and balances at central banks	11,095	—	—	—	—	—
Settlement balances	1,421	—	—	—	—	—
Loans to banks - amortised cost	354	66	39	—	—	—
Amounts due from holding company and fellow subsidiaries	3,877	1,525	1,900	1,328	903	149
Other financial assets	1,691	2,619	2,756	922	707	205
Total maturing assets	18,438	4,210	4,695	2,250	1,610	354
Loans to customers - amortised cost	2,009	2,272	2,130	1,009	214	328
Finance lease	—	48	—	—	—	—
Derivatives held for hedging	40	56	152	48	7	—
	20,487	6,586	6,977	3,307	1,831	682
Liabilities by contractual maturity						
Bank deposits	2,756	21	—	—	—	—
Amounts due to holding company and fellow subsidiaries	3,286	2,788	571	6,538	1,801	59
Settlement balances	1,977	—	—	—	—	—
Other financial liabilities	1,302	5,066	6,494	2,359	837	200
Other liabilities (1)	45	—	—	—	—	—
Total maturing liabilities	9,366	7,875	7,065	8,897	2,638	259
Customer deposits	1,469	891	25	4	2	2
Derivatives held for hedging	—	10	23	4	(5)	—
	10,835	8,776	7,113	8,905	2,635	261
Guarantees and commitments notional amount						
Guarantees (2)	278	—	—	—	—	—
Commitments (3)	8,922	—	—	—	—	—
	9,200	—	—	—	—	—

Notes:

- (1) Other liabilities includes notes in circulation.
- (2) NWM Group is only called upon to satisfy a guarantee when the guaranteed party fails to meet its obligations. NWM Group expects most guarantees it provides to expire unused.
- (3) NWM 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. NWM Group does not expect all facilities to be drawn, and some may lapse before drawdown.

Notes on the accounts

14 Loan impairment provisions

Loan exposure and impairment metrics

The table below summarises loans and related credit impairment measures on an IFRS 9 basis.

	31 December 2019 £m	31 December 2018* £m
Loans - amortised cost		
- Stage 1	9,260	8,088
- Stage 2	180	365
- Stage 3	169	695
<i>Of which: individual</i>	158	680
<i>Of which: collective</i>	11	15
- Inter-Group (1)	738	2,634
Total	10,347	11,782
ECL provisions (2)		
- Stage 1	10	6
- Stage 2	4	11
- Stage 3	132	91
<i>Of which: individual</i>	123	84
<i>Of which: collective</i>	9	7
Total	146	108
ECL provision coverage (3,4)		
- Stage 1 (%)	0.11	0.07
- Stage 2 (%)	2.22	3.01
- Stage 3 (%)	78.11	13.09
Total	1.52	1.18
Impairment losses		
ECL charge (5)		
- Stage 1	—	(43)
- Stage 2	(7)	(14)
- Stage 3	(41)	(50)
<i>Of which: individual</i>	(35)	(45)
<i>Of which: collective</i>	(6)	(5)
- Third party	(48)	(107)
- Inter-Group	—	5
Total	(48)	(102)
- ECL loss rate - annualised (basis points) (4)	(49.95)	(116.97)
- Amounts written off	15	69
<i>Of which: individual</i>	15	63
<i>Of which: collective</i>	—	6

*2018 data has been restated for a change to presentation of unrecognised interest. Refer to Accounting policy 1, Other amendments to IFRS for further details.

Notes:

- (1) NWM Group's intercompany assets were classified in Stage 1. The ECL attached to these loans was £0.3 million at 31 December 2019.
- (2) Includes £1 million (2018 – £2 million) related to assets classified as FVOCI.
- (3) ECL provisions coverage is calculated as ECL provisions divided by loans - amortised cost.
- (4) ECL provisions coverage and ECL loss rates are calculated on third party loans and related ECL provisions and charge respectively.
- (5) Includes a nil charge (2018 – £3 million charge) related to other financial assets, of which a £2 million release (2018 – £1 million charge) related to assets classified as FVOCI, offset by other charges; and nil charge (2018 – £3 million release) related to contingent liabilities.
- (6) The table above shows gross loans only and excludes amounts that are outside the scope of the ECL framework. Refer to page 52 for Financial instruments within the scope of the IFRS 9 ECL framework for further details. Other financial assets within the scope of the IFRS 9 ECL framework were cash and balances at central banks totalling £12.7 billion and debt securities of £11.1 billion (2018 – £11.2 billion and £9.8 billion respectively).
- (7) Following the implementation of ring-fencing requirements there is no longer any exposure in NWM Plc which sits outside of the NatWest Markets franchise.

Notes on the accounts

14 Loan impairment provisions continued

Credit risk enhancement and mitigation

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

Critical accounting policy: Loan impairment provisions

The loan impairment provisions have been established in accordance with IFRS 9. Accounting policy 11 sets out how the expected loss approach is applied. At 31 December 2019, customer loan impairment provisions amounted to £146 million (2018 - £108 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.

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. Further information and sensitivity analyses are on page 47.

IFRS 9 ECL model design principles

To meet IFRS 9 requirements, PD, LGD and EAD used in ECL 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.
- For the life of the loan – all PD, LGD and EAD models produce term structures 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 probability of default over the remaining lifetime at the reporting date) 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 be sufficiently explained by the CCI measure (unlike in the case of PD and some LGD models) 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.

Approach for multiple economic scenarios (MES)

The base scenario plays a greater part in the calculation of ECL than the approach to MES.

Notes on the accounts

15 Investments in Group undertakings

Investments in Group undertakings are carried at cost less impairment. Movements during the year were as follows:

	NWM Plc	
	2019 £m	2018 £m
At 1 January	1,151	496
Currency translation and other adjustments	34	27
Additions	2,069	920
Disposals	—	(100)
Impairment of investments	(349)	(192)
At 31 December	2,905	1,151

The additional investments in NWM Group undertakings relates to RBS Holdings N.V. (RBSH N.V.). RBSH N.V. is the parent company of NatWest Markets N.V. (NWM N.V.) and was acquired by NWM Plc on 29 November 2019.

The principal subsidiary undertakings of the company are shown below. Their capital consists of ordinary shares which are unlisted. All of these subsidiaries are included in NWM Group's consolidated financial statements and have an accounting reference date of 31 December.

	Nature of business	Country of incorporation and principal area of operation	Group interest
NatWest Markets Securities Inc.	Broker dealer	US	100%
NatWest Markets N.V.	Banking	Netherlands	100%

Full information on all related undertakings is included in Note 37.

16 Business acquisitions

NWM Group acquired RBS Holdings N.V. on 29 November 2019 for a consideration approximating to net asset value, funded by an equity contribution from RBSG plc to NWM Plc. In accordance with RBS Group policy, NWM Group paid book value and recognised the assets and liabilities at inherited values. Inherited values were those recognised by RBS Group and included the accounting history since initial recognition by RBS Group.

Third party assets and liabilities of RBS Holdings N.V. acquired.

	Impact of acquisition £m
Assets	
Cash and balances at central banks	2,611
Trading assets	2,693
Derivatives	3,543
Settlement balances	1,630
Loans to banks and customers - amortised cost	1,616
Liabilities	
Bank and customer deposits	703
Settlement balances	1,067
Trading liabilities	1,918
Derivatives	4,217

Notes on the accounts

17 Other financial assets

	NWM Group							
	Debt securities							
	Central and local government			Other debt		Equity shares	Loans	Total
	UK £m	US £m	Other £m	£m	Total £m	£m	£m	£m
2019								
Mandatory fair value through profit or loss	—	—	—	305	305	11	76	392
Fair value through other comprehensive income	233	3,484	2,890	627	7,234	695	—	7,929
Amortised cost	—	—	—	3,984	3,984	—	—	3,984
Total	233	3,484	2,890	4,916	11,523	706	76	12,305
2018								
Mandatory fair value through profit or loss	—	—	—	668	668	6	460	1,134
Fair value through other comprehensive income	—	2,930	4,078	139	7,147	289	—	7,436
Amortised cost	—	—	—	2,698	2,698	—	—	2,698
Total	—	2,930	4,078	3,505	10,513	295	460	11,268

	NWM Plc							
	Debt securities							
	Central and local government			Other debt	Total	Equity shares	Loans	Total
	UK £m	US £m	Other £m	£m	£m	£m	£m	£m
2019								
Mandatory fair value through profit or loss	—	—	—	305	305	—	76	381
Fair value through other comprehensive income	233	3,484	2,652	294	6,663	638	—	7,301
Amortised cost	—	—	—	3,954	3,954	—	—	3,954
Total	233	3,484	2,652	4,553	10,922	638	76	11,636
2018								
Mandatory fair value through profit or loss	—	—	—	667	667	—	460	1,127
Fair value through other comprehensive income	—	2,930	4,054	—	6,984	186	—	7,170
Amortised cost	—	—	—	2,698	2,698	—	—	2,698
Total	—	2,930	4,054	3,365	10,349	186	460	10,995

At 16 June 2019, Alawwal bank and SABB were legally combined as part of a statutory merger. Alawwal bank's assets and liabilities were absorbed by SABB. The transaction was executed through a share swap, with Alawwal bank's shareholders receiving SABB shares for each Alawwal share. The RBS Group's economic interest in SABB was acquired by NWM Plc from NWM N.V. at the same time. As at 31 December 2019, £595 million of the equity shares balance pertains to the holding in SABB. Equity shares disposed during 2019 include VISA Inc, Tradeweb Markets LLC and Big Society Capital Limited (2018 values - £98 million, £89 million and £42 million respectively).

Dividends on FVOCI equity shares during the year ended 31 December 2019 included approximately £15 million in relation to the equity holding in SABB, £4 million in relation to OTC Derivative Ltd and certain other dividends which were not individually significant. There were no material dividends received in relation to equity shares disposed during the year.

18 Other assets

	NWM Group		NWM Plc	
	2019 £m	2018 £m	2019 £m	2018 £m
Prepayments	13	11	10	8
Accrued income	31	71	23	68
Tax recoverable	264	441	279	455
Pension schemes in net surplus (Note 5)	271	299	271	299
Interests in associates	1	5	1	1
Property, plant and equipment	136	32	36	1
Other assets	104	130	67	104
Assets of disposal groups	26	119	—	—
Deferred tax (Note 7)	1	—	—	—
Total	847	1,108	687	936

Notes on the accounts

19 Other financial liabilities

	NWM Group		NWM Plc	
	2019 £m	2018 £m	2019 £m	2018 £m
Debt securities in issue				
- designated as at fair value through profit or loss	2,256	2,624	2,031	2,624
- amortised cost	15,053	12,997	14,849	12,997
Subordinated liabilities				
- designated as at fair value through profit or loss	724	425	399	425
- amortised cost	412	233	191	233
Total	18,445	16,279	17,470	16,279

20 Subordinated liabilities

	NWM Group		NWM Plc	
	2019 £m	2018 £m	2019 £m	2018 £m
Dated loan capital	1,041	524	495	524
Undated loan capital	95	134	95	134
Total	1,136	658	590	658

Note:

(1) Excludes amounts due to holding company and fellow subsidiaries of £2,020 million (2018 – £1,962 million) for NWM Group and £2,020 million (2018 – £1,962 million) for NWM Plc which are analysed in the tables below.

The following tables analyse NWM Plc third party subordinated liabilities:

	Capital treatment	2019 £m	2018 £m
Dated loan capital			
US\$125.6 million floating rate notes 2020 ⁽³⁾	Tier 2	97	99
€300 million floating rate notes 2022 ⁽³⁾	Tier 2	251	266
€144.4 million floating rate notes 2023 ⁽³⁾	Tier 2	147	159
Total		495	524

Notes:

- (1) In the event of certain changes in tax laws, dated loan capital issues may be redeemed in whole, but not in part, at the option of the issuer, at the principal amount thereof plus accrued interest, subject to prior regulatory approval.
- (2) Except as stated above, claims in respect of NWM Plc's dated loan capital are subordinated to the claims of other creditors. None of NWM Plc's dated loan capital is secured.
- (3) Interest on all floating rate subordinated notes is calculated by reference to market rates.

	Capital treatment	2019 £m	2018 £m
Undated loan capital			
£31 million 4.956% notes (not callable)	Ineligible	31	31
£35 million 5.50% notes (callable December 2019)	Ineligible	—	36
£21 million 6.20% notes (callable March 2022)	Ineligible	22	25
£16 million 5.625% (callable September 2026)	Ineligible	24	22
£19 million 5.625% notes (callable June 2032)	Ineligible	18	20
Total		95	134

Notes:

- (1) The company can satisfy interest payment obligations by issuing ordinary shares to appointed Trustees to enable them, on selling these shares, to settle the interest payment.
- (2) Except as stated above, claims in respect of NWM Plc's undated loan capital are subordinated to the claims of other creditors. None of the NWM Plc's undated loan capital is secured.
- (3) In the event of certain changes in tax laws, undated loan capital issues may be redeemed in whole, but not in part, at the option of NWM Plc, at the principal amount thereof plus accrued interest, subject to prior regulatory approval.

	Capital treatment	2019 £m	2018 £m
Third party redemptions in the period (values as at date of transaction)			
€2,000 million 6.934% subordinated notes 2018	Tier 2	—	1,743
£130 million 9.5% undated subordinated bonds (callable August 2018)	Ineligible	—	103
£35 million 5.5% fixed rate undated subordinated notes (callable December 2019)	Ineligible	35	—
Total		35	1,846

Notes on the accounts

20 Subordinated liabilities continued

The following tables analyse intercompany subordinated liabilities:

	Capital treatment	2019 £m	2018 £m
Dated loan capital			
€950 million 3.26% (redeemable March 2024)	Tier 2	836	—
US\$250 million subordinated notes 2029	Tier 2	195	—
€1,000 million 3.625% notes 2024	Tier 2	—	951
US\$389 million 6.10% notes 2023	Tier 2	307	307
		1,338	1,258

Undated loan capital

The Royal Bank of Scotland Group plc

US\$600 million floating rate perpetual notes (callable June 2018)	Tier 2	455	469
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Preference shares

US\$300 million 7.25% Series H (callable anytime)	Ineligible	227	235
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Redemptions in the period (values as at date of transaction)

The Royal Bank of Scotland Group plc

£100 million floating rate perpetual notes (callable December 2012)	Tier 2	—	100
£420 million floating rate perpetual notes (callable July 2013)	Tier 2	—	420
US\$650 million 6.425% Series N (callable January 2034)	Ineligible	—	481
US\$750 million 6.80% Series L (callable anytime)	Ineligible	—	555
US\$850 million 5.75% Series R (callable quarterly)	Ineligible	—	629
US\$2,000 million 6.00% notes 2023	Tier 2	—	1,480
€1,000 million 3.625% notes 2024	Tier 2	861	—
		861	3,665

Issuances in the period (values as at date of transaction)

The Royal Bank of Scotland Group plc

€950 million 3.2595% (redeemable March 2024)	Tier 2	818	—
US\$250 million subordinated notes 2029	Tier 2	197	—
		1,015	—

21 Other liabilities

	NWM Group		NWM Plc	
	2019 £m	2018 £m	2019 £m	2018 £m
Current tax	76	26	17	26
Accruals	283	228	186	137
Deferred income	27	44	15	45
Deferred tax (Note 7)	501	487	462	446
Retirement benefit liabilities (Note 5)	63	115	54	114
Provisions for liabilities and charges	505	895	302	651
Lease liabilities (Note 24)	97	—	28	—
Other liabilities	137	110	131	258
Liabilities of disposal groups	—	1	—	—
	1,689	1,906	1,195	1,677

Notes on the accounts

21 Other liabilities continued

	NWM Group		
	Litigation and other regulatory £m	Other (1) £m	Total £m
Provisions for liabilities and charges			
At 1 January 2019	698	197	895
Implementation of IFRS 16 on 1 January 2019 (2)	—	(8)	(8)
ECL impairment charge	—	(2)	(2)
Transfer in from accruals and other liabilities	—	13	13
Transfers	(35)	35	—
Currency translation and other movements	(45)	44	(1)
Charge to income statement	71	65	136
Releases to income statement	(78)	(68)	(146)
Provisions utilised	(286)	(96)	(382)
At 31 December 2019	325	180	505

	NWM Plc		
	Litigation and other regulatory £m	Other (1) £m	Total £m
Provisions for liabilities and charges			
At 1 January 2019	445	206	651
Implementation of IFRS 16 on 1 January 2019 (2)	—	(6)	(6)
ECL impairment charge	—	(1)	(1)
Transfer to accruals and other liabilities	—	(2)	(2)
Transfers	(35)	35	—
Currency translation and other movements	(3)	(5)	(8)
Charge to income statement	46	48	94
Releases to income statement	(35)	(55)	(90)
Provisions utilised	(260)	(76)	(336)
At 31 December 2019	158	144	302

Notes:

- (1) Materially comprises provisions relating to restructuring costs and customer redress.
(2) Refer to Note 24 for further information on the impact of IFRS 16 implementation.

There are uncertainties as to the eventual cost of redress in relation to certain of the provisions contained in the table above. Assumptions relating to these are inherently uncertain and the ultimate financial impact may be different from the amount provided.

Critical accounting policy: Provisions for liabilities

Judgment is involved in determining whether an obligation exists, and in estimating the probability, timing and amount of any outflows. Where NWM 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.

Notes on the accounts

22 Discontinued operations

As part of implementing the legislation following the recommendations of the Independent Commission on Banking, the transfer of NWM Group's Personal & Business Banking (PBB), Commercial & Private Banking (CPB) and certain parts of Central items and NatWest Markets included in the ring-fenced bank, to subsidiaries of NatWest Holdings, took place in Q2 2018. It was followed by a transfer of NatWest Holdings to RBSG.

	NWM Group 2018 £m
NatWest Holdings (1)	
Interest income	5,657
Interest expense	(1,322)
Net interest income	4,335
Other income	2,131
Total income	6,466
Operating expenses	(3,436)
Profit before impairment losses	3,030
Impairment losses	(137)
Operating profit before tax	2,893
Tax charge	(432)
Profit from discontinued operations net of tax	2,461

Notes:

- (1) Other comprehensive loss from discontinued operations for the year ended 31 December 2018 was £3,556 million including £2 billion in respect of pension contributions.
- (2) At 31 December 2018, the following items previously classified within discontinuing operations continued to be owned by NWM Group and had been reclassified out of disposal groups: Loans to customers of £1.0 billion; Other assets of £0.2 billion; and Subordinated liabilities of £0.7 billion.

Cash flows attributable to discontinued operations

Included within the NWM Group's cash flows are the following amounts attributable to discontinued operations.

	2018 £m
Net cash flows from operating activities	8,942
Net cash flows from investing activities	(3,657)
Net cash flows from financing activities	1,636
Net increase in cash and cash equivalents	7,295

23 Share capital and reserves

	2019 £m	2018 £m	Number of shares	
			2019 000s	2018 000s
Allotted, called up and fully paid				
Ordinary shares of £1	400	400	399,517	399,517
Non-cumulative preference shares of US\$0.01	—	—	12,000	12,000

	£m	Number of shares - 000s
Movement in allotted, called up and fully paid ordinary shares		
At 1 January 2018	6,609	6,608,517
Capital reduction	(6,209)	(6,209,000)
At 1 January and 31 December 2019	400	399,517

Ordinary shares

On 29 June 2018 the Court of Session in Scotland approved a capital reduction including the cancellation of the share premium account and capital redemption reserve (together the "capital reduction") in relation to NWM Plc. The capital reduction was completed on 2 July 2018 which effected, primarily through a distribution in specie, the transfer of NatWest Holdings Ltd to RBSG plc thereby creating the legal separation of those RBS Group entities that are within the ring-fenced sub-group from those held outside the ring-fence.

As a result of the capital reduction the issued ordinary share capital reduced 6,209 million to 400 million £1 shares, NWM Plc's share premium account and capital redemption reserve were also cancelled.

NWM Plc paid two ordinary dividends to RBSG plc in 2019 totalling £500 million, or £1.25 per share (2018 - £2,550 million, or £6.38 per share).

Reserves

NWM Group optimises capital efficiency by maintaining reserves in subsidiaries, including regulated entities. Certain preference shares and subordinated debt are also included within regulatory capital. The remittance of reserves to the parent or the redemption of shares or subordinated capital by regulated entities may be subject to maintaining the capital resources required by the relevant regulator.

Notes on the accounts

24 Leases

NWM Group has adopted IFRS 16 Leases retrospectively from 1 January 2019 on a modified retrospective basis without restating comparatives. Adoption of IFRS 16 resulted in the right of use assets of £56 million and £21 million, lease liabilities of £62 million and £27 million, and a decrease in retained earnings of £6 million and £6 million for NWM Group and NWM Plc respectively.

On adoption of IFRS 16, NWM Group recognised right of use assets and lease liabilities in relation to leases which had been previously classified as operating leases under IAS 17 Leases subject to certain practical expedients as allowed by the standard.

The following practical expedients permitted by the standard were used:

- A single discount rate has been applied to a portfolio of leases with reasonably similar characteristics.
- The accounting for operating leases with a remaining lease term of 12 months at 1 January 2019 for non-property leases.
- Exclusion of initial direct costs from the measurement of the right of use asset at the date of initial application.
- Reliance on assessment of onerous provisions under IAS 37 Provisions, Contingent Liabilities and Contingent Assets for the purposes of impairment.
- The use of hindsight where contracts contain options to extend or terminate the lease in determining the lease term.

The lease liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of 1 January 2019. The weighted average lessee's incremental borrowing rate applied to the lease liabilities on 1 January 2019 was 3.8% and 3.7% for NWM Group and NWM Plc respectively.

	NWM Group 2019 £m	NWM Plc 2019 £m
Operating lease commitments as disclosed as at 31 December 2018	56	36
Adjustments as a result of a different treatment of extension and termination options	14	—
Discounted using the incremental borrowing rate	(4)	(3)
Other	(4)	(6)
Lease liabilities recognised as at 1 January 2019 on adoption of IFRS 16	62	27

Lessees

	NWM Group 2019 £m	NWM Plc 2019 £m
Amounts recognised on the balance sheet		
Right of use assets included in property, plant and equipment	99	36
Additions to right of use assets	101	46
Lease liabilities ^(1,2)	(127)	(56)

The total cash outflow for leases is £20 million for NWM Group and £11 million for NWM Plc. NWM Group's consolidated income statement recognised an expense of £29 million, of which: £20 million was depreciation. Rental expense in respect of operating leases in 2018 was £12 million.

Notes:

- (1) Contractual cashflows of lease liabilities is shown in Note 13.
- (2) Lease liabilities include amounts due to fellow subsidiaries of £30 million for NWM Group and £28 million for NWM Plc.

	NWM Group 2018 £m	NWM Plc 2018 £m
Operating leases		
Minimum rentals payable under non-cancellable leases ⁽¹⁾		
- within 1 year	17	11
- after 1 year but within 5 years	39	25
- after 5 years	—	—
Total	56	36

Note:

- (1) Predominantly property leases.

Notes on the accounts

24 Leases continued

Lessor

Acting as a lessor, NWM Group holds property, plant and equipment, renting them to customers under finance lease arrangements. NWM Group's consolidated income statement recognised finance lease income of £14 million.

Amounts receivable under finance leases

	NWM Group 2019 £m	NWM Plc 2019 £m
Within 1 year	12	6
1 to 2 years	11	6
2 to 3 years	10	5
3 to 4 years	5	—
4 to 5 years	3	—
After 5 years	37	—
Lease payments total	78	17
Unearned income	(17)	(1)
Present value of lease payments	61	16
Impairments	(5)	—
Net investment in finance leases	56	16

2018	NWM Group			
	Finance lease contracts and hire purchase agreements			
	Gross amounts £m	Present value adjustments £m	Other movements £m	Present value £m
Within 1 year	117	(2)	(40)	75
1 to 5 years	120	(23)	—	97
After 5 years	40	(27)	—	13
Total	277	(52)	(40)	185

Amounts receivable under operating leases receivables

The following table shows undiscounted lease receipts from operating leases:

	NWM Group 2018 £m
Within 1 year	12
1 to 5 years	55
After 5 years	33
Total	100

Notes on the accounts

25 Structured entities

A structured entity (SE) is an entity that has been designed such that voting or similar rights are not the dominant factor in deciding who controls the entity, for example, when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. SEs are usually established for a specific, limited purpose, they do not carry out a business or trade and typically have no employees. They take a variety of legal forms - trusts, partnerships and companies - and fulfil many different functions. As well as being a key element of securitisations, SEs are also used in fund management activities to segregate custodial duties from the fund management advice.

Consolidated structured entities

Securitisations

In a securitisation, assets, or interests in a pool of assets, are transferred generally to a SE which then issues liabilities to third party investors. The majority of securitisations are supported through liquidity facilities or other credit enhancements. The NWM Group arranges securitisations to facilitate client transactions and undertakes own asset securitisations to sell or to fund portfolios of financial assets. NWM Group also acts as an underwriter and depositor in securitisation transactions in both client and proprietary transactions. NWM Group's involvement in client securitisations takes a number of forms. It may: sponsor or administer a securitisation programme; provide liquidity facilities or programme-wide credit enhancement; and purchase securities issued by the vehicle.

Covered debt programme

NWM Group has assigned certain loans to customers and other debt instruments to bankruptcy remote limited liability partnerships to provide security for issues of debt securities by NWM Group. NWM Group retains all of the risks and rewards of these assets and continues to recognise them. The partnerships are consolidated by the NWM Group and the related covered debt included within other financial liabilities. At 31 December 2019, £1,428 million (2018 - £2,838 million) of loans and other debt instruments provided security for £1,293 million (2018 - £1,260 million) debt securities in issue and other borrowing by NWM Plc and NWM Group.

Lending of own issued securities

NWM Plc has issued, retained, and lent debt securities under securities lending arrangements. Under standard terms in the UK and US markets, the recipient has an unrestricted right to sell or re-pledge collateral, subject to returning equivalent securities on maturity of the transaction. NWM Plc retains all of the risks and rewards of own issued liabilities lent under such arrangements and does not recognise them. At 31 December 2019, £1,704 million secured and £424 million unsecured (2018 - £526 million secured, £424 million unsecured) of own issued liabilities have been retained and lent under securities lending arrangements. At 31 December 2019, £1,745 million (2018 - £551 million) of loans and other debt instruments provided security for secured own issued liabilities that have been retained and lent under securities lending arrangements.

Unconsolidated structured entities

NWM Group's interests in unconsolidated structured entities are analysed below.

	2019			2018		
	Asset backed securitisation vehicles £m	Investment funds and other £m	Total £m	Asset backed securitisation vehicles £m	Investment funds and other £m	Total £m
Trading assets and derivatives						
Trading assets	760	52	812	613	148	761
Derivative assets	196	24	220	200	47	247
Derivative liabilities	(154)	(4)	(158)	(153)	(49)	(202)
Total	802	72	874	660	146	806
Non trading assets						
Loans to customers	1,508	114	1,622	1,933	212	2,145
Other financial assets	3,869	107	3,976	2,691	—	2,691
Total	5,377	221	5,598	4,624	212	4,836
Liquidity facilities/loan commitments	1,612	83	1,695	2,136	113	2,249
Guarantees	—	—	—	3	10	13
Maximum exposure	7,791	376	8,167	7,423	481	7,904

Notes on the accounts

26 Asset transfers

Transfers that do not qualify for derecognition

NWM Plc enters into securities financing, reverse repurchase and total return agreements in accordance with normal market practice which includes the provision of additional collateral if necessary. Under standard terms in the UK and US markets, the recipient has an unrestricted right to sell or repledge collateral, subject to returning equivalent securities on maturity of the transaction.

Securities sold under repurchase transactions and transactions with the substance of securities repurchase agreements are not derecognised if the NWM Group retains substantially all the risks and rewards of ownership. The fair value (and carrying value) of securities transferred under such transactions included on the balance sheet, are set out below. All of these securities could be sold or repledged by the holder.

	NWM Group		NWM Plc	
	2019 £m	2018 £m	2019 £m	2018 £m
The following assets have failed derecognition (1)				
Trading assets	23,156	14,020	13,461	12,621
Other financial assets	94	—	94	—
	23,250	14,020	13,555	12,621

Note:

(1) Associated liabilities were £23,177 million for the NWM Group (2018 - £13,511 million) and £12,827 million for NWM Plc (2018 - £11,958 million).

Assets pledged as collateral

NWM Plc pledges collateral with its counterparties in respect of derivative liabilities and bank and stock borrowings.

	NWM Group		NWM Plc	
	2019 £m	2018 £m	2019 £m	2018 £m
Assets pledged against liabilities				
Trading assets	27,918	31,098	27,138	31,098
Loans to customers - amortised cost	499	2,378	499	2,378
Other financial assets (1)	2,740	123	2,078	97
	31,157	33,599	29,715	33,573

Note:

(1) Includes pledges for stock borrowing.

The following table analyses assets that have been transferred but have failed the derecognition rules under IFRS 9 and therefore continue to be recognised on NWM Plc's balance sheet.

Asset type	2019 £m	2018 £m
Loans and other debt instruments - covered debt programme (1)	1,149	2,838

Note:

(1) The associated liabilities were £1,324 million (2018 - £2,728 million).

Notes on the accounts

27 Capital resources

Under Capital Requirements Regulation (CRR), regulators within the European Union monitor capital on a legal entity basis, with local transitional arrangements on the phasing in of end-point CRR. The capital resources based on the PRA transitional basis for NWM Plc are set out below.

	2019 £m	2018 £m
Shareholders' equity (excluding non-controlling interests)		
Shareholders' equity	9,631	8,922
Other equity instruments	(904)	(749)
	8,727	8,173
Regulatory adjustments and deductions		
Own credit	(39)	(223)
Defined benefit pension fund adjustment	(171)	(197)
Cash flow hedging reserve	(137)	(114)
Prudential valuation adjustments	(373)	(450)
Expected losses less impairments	(10)	(351)
Instruments of financial sector entities where the institution has a significant and non-significant investment	(1,900)	(445)
Other regulatory adjustments	—	(24)
	(2,630)	(1,804)
CET1 capital	6,097	6,369
Additional Tier 1 (AT1) capital		
Qualifying instruments and related share premium	904	749
Qualifying instruments and related share premium subject to phase out	226	234
	1,130	983
Tier 1 deductions		
Instruments of financial sector entities where the institution has a significant investment	(224)	—
Tier 1 capital	7,003	7,352
Qualifying Tier 2 capital		
Qualifying instruments and related share premium	1,967	2,098
Tier 2 deductions		
Instruments of financial sector entities where the institution has a significant and non-significant investment	(469)	(693)
Tier 2 capital	1,498	1,405
Total regulatory capital	8,501	8,757

In the management of capital resources, NWM Plc is governed by RBS Group's policy to maintain a strong capital base and to utilise it efficiently throughout its activities to optimise the return to shareholders while maintaining a prudent relationship between the capital base and the underlying risks of the business. In carrying out this policy, RBS Group has regard to the supervisory requirements of the PRA. The PRA uses capital ratios as a measure of capital adequacy in the UK banking sector, comparing a bank's capital resources with its risk-weighted assets (the assets and off-balance sheet exposures are 'weighted' to reflect the inherent credit and other risks); by international agreement, the Pillar 1 capital ratios, excluding capital buffers, should be not less than 8% with a Common Equity Tier 1 component of not less than 4.5%. NWM Plc has complied with the PRA's capital requirements throughout the year.

A number of subsidiaries and sub-groups within NWM Group, principally banking entities, are subject to various individual regulatory capital requirements in the UK and overseas. Furthermore, the payment of dividends by subsidiaries and the ability of members of RBS Group to lend money to other members of RBS Group may be subject to restrictions such as local regulatory or legal requirements, the availability of reserves and financial and operating performance.

Notes on the accounts

28 Memorandum items

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 2019. Although the NWM Group is exposed to credit risk in the event of a customer's failure to meet its obligations, the amounts shown do not, and are not intended to, provide any indication of NWM Group's expectation of future losses.

	NWM Group		NWM Plc	
	2019 £m	2018 £m	2019 £m	2018 £m
Contingent liabilities and commitments				
Guarantees and assets pledged as collateral security	972	278	134	278
Other contingent liabilities	155	186	152	186
Standby facilities, credit lines and other commitments	15,805	10,659	10,218	10,654
	16,932	11,123	10,504	11,118

Note:

- (1) In the normal course of business, NWM Plc guarantees specified third party liabilities of certain subsidiaries; it also gives undertakings that individual subsidiaries will fulfil their obligations to third parties under contractual or other arrangements

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. NWM Group's maximum exposure to credit loss, in the event of its obligation crystallising and all counterclaims, collateral or security proving valueless, is represented by the contractual nominal amount of these instruments included in the table above. These commitments and contingent obligations are subject to NWM Group's normal credit approval processes.

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

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

Standby facilities and credit lines - under a loan commitment NWM 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.

Other commitments - these include documentary credits, which are commercial letters of credit providing for payment by NWM Group to a named beneficiary against presentation of specified documents, forward asset purchases, forward deposits placed and undrawn note issuance and revolving underwriting facilities, and other short-term trade related transactions.

Risk-sharing arrangements

During 2019 NWM Plc and NWM N.V. have established limited risk-sharing arrangements that facilitate the smooth provision of services to NatWest Markets' customers. The arrangements include:

- The provision of a funded guarantee of up to £3.0 billion by NWM Plc to NWM N.V. that limits NWM N.V.'s exposure to large individual customer credits to 10% of NWM N.V.'s capital. Funding is provided by NWM Plc deposits placed with NWM N.V. of not less than the guaranteed amount. At 31 December 2019, the deposits amounted to £0.7 billion and the guarantee fees in the period were £1.3 million.
- The provision of credit protection and an unfunded guarantee by NWM Plc in respect of NWM N.V.'s Legacy portfolio. At 31 December 2019 the exposure at default covered by the guarantees was approximately £0.3 billion (of which £0.2 billion was cash collateralised) and £0.1 billion respectively. A fair value increase of £5 million in relation to the credit protection and fees of £1.0 million in relation to the unfunded guarantee were recognised in the period.

Indemnity deed

In April 2019, NWM Plc and National Westminster Bank Plc entered into a cross indemnity agreement for losses incurred within the entities in relation to business transferred to or from the ring-fenced bank under the RBS Group's structural re-organisation. Under the agreement, NWM Plc is indemnified by National Westminster Bank Plc against losses relating to the National Westminster Bank Plc transferring businesses and ring-fenced bank obligations and National Westminster Bank Plc is indemnified by NWM Plc against losses relating to NWM Plc transferring businesses and non ring-fenced bank obligations with effect from the relevant transfer date.

Contractual obligations for future expenditure not provided for in the accounts

The following table shows contractual obligations for future expenditure not provided for in the accounts at the year end.

	NWM Group 2019 £m	NWM Group 2018 £m
Contracts to purchase goods or services (1)	1	1
	1	1

Note:

- (1) Of which due within 1 year: £1 million (2018 - £1 million).

Notes on the accounts

28 Memorandum items continued

Litigation, investigations and reviews

NWM Plc and its subsidiary and associated undertakings ('NWM Group') are party to legal proceedings and the subject of investigation and other regulatory and governmental action ('Matters') in the United Kingdom (UK), the United States (US), the European Union (EU) and other jurisdictions.

NWM Group recognises a provision for a liability in relation to these Matters when it is probable that an outflow of economic benefits will be required to settle an obligation resulting from past events, and a reliable estimate can be made of the amount of the obligation.

In many proceedings and investigations, it is not possible to determine whether any loss is probable, or to estimate reliably the amount of any loss, either as a direct consequence of the relevant proceedings and investigations or as a result of adverse impacts or restrictions on NWM Group's reputation, businesses and operations. Numerous legal and factual issues may need to be resolved, including through potentially lengthy discovery and document production exercises and determination of important factual matters, and by addressing novel or unsettled legal questions relevant to the proceedings in question, before a liability can reasonably be estimated for any claim. NWM Group cannot predict if, how, or when such claims will be resolved or what the eventual settlement, damages, fine, penalty or other relief, if any, may be, particularly for claims that are at an early stage in their development or where claimants seek substantial or indeterminate damages.

There are situations where NWM Group may pursue an approach that in some instances leads to a settlement agreement. This may occur in order to avoid the expense, management distraction or reputational implications of continuing to contest liability, or in order to take account of the risks inherent in defending claims or investigations, even for those Matters for which NWM Group believes it has credible defences and should prevail on the merits. The uncertainties inherent in all such Matters affect the amount and timing of any potential outflows for both Matters with respect to which provisions have been established and other contingent liabilities.

The future outflow of resources in respect of any Matter may ultimately prove to be substantially greater than or less than the aggregate provision that NWM Group has recognised. Where (and as far as) liability cannot be reasonably estimated, no provision has been recognised. NWM Group expects that in future periods, additional provisions, settlement amounts and customer redress payments will be necessary, in amounts that are expected to be substantial in some instances.

For a discussion of certain risks associated with NWM Group's litigation, investigations and reviews, see the Risk Factor relating to legal, regulatory and governmental actions and investigations set out on page 155.

Litigation

Residential mortgage-backed securities (RMBS) litigation in the US
NatWest Markets Securities Inc. (NWMSI) and certain affiliates continue to defend RMBS-related claims in the US in which plaintiffs allege that certain disclosures made in connection with the relevant offerings of RMBS contained materially false or misleading statements and/or omissions regarding the underwriting standards pursuant to which the mortgage loans underlying the RMBS were issued. The remaining RMBS lawsuits against NWM Group companies consist of cases filed by the Federal Home Loan Bank of Seattle and the Federal Deposit Insurance Corporation that together involve the issuance of less than US\$1 billion of RMBS issued primarily from 2005 to 2007. A case filed by the Federal Home Loan Bank of Boston was settled during 2019. In addition, NWMSI previously agreed to settle a purported RMBS class action entitled *New Jersey Carpenters Health Fund v. Novastar Mortgage Inc. et al.* for US\$55.3 million. This was paid into escrow pending court approval of the settlement, which was granted on 11 March 2019, but which is now the subject of an appeal by a class member who does not want to participate in the settlement.

London Interbank Offered Rate (LIBOR) and other rates litigation

NWM Plc and certain other members of NWM Group, including RBSG plc, are defendants in a number of class actions and individual claims pending in the United States District Court for the Southern District of New York (SDNY) with respect to the setting of LIBOR and certain other benchmark interest rates. The complaints allege that the NWM Group defendants and other panel banks violated various federal laws, including the US commodities and antitrust laws, and state statutory and common law, as well as contracts, by manipulating LIBOR and prices of LIBOR-based derivatives in various markets through various means.

Several class actions relating to USD LIBOR, as well as more than two dozen non-class actions concerning USD LIBOR, are part of a co-ordinated proceeding in the SDNY. In December 2016, the SDNY held that it lacks personal jurisdiction over NWM Group defendants with respect to certain claims. As a result of that decision, all NWM Group defendants have been dismissed from each of the USD LIBOR-related class actions (including class actions on behalf of over-the-counter plaintiffs, exchange-based purchaser plaintiffs, bondholder plaintiffs, and lender plaintiffs), but seven non-class cases in the co-ordinated proceeding remain pending against NWM Group defendants. The dismissal of NWM Group defendants for lack of personal jurisdiction is the subject of a pending appeal to the United States Court of Appeals for the Second Circuit. In September 2019, NWM Group defendants reached a settlement in principle to resolve the class action on behalf of bondholder plaintiffs (those who held bonds issued by non-defendants on which interest was paid from 2007 to 2010 at a rate expressly tied to USD LIBOR). The settlement is subject to documentation and court approval. The amount of the settlement is covered by an existing provision.

Among the non-class claims dismissed by the SDNY in December 2016 were claims that the Federal Deposit Insurance Corporation (FDIC) had asserted on behalf of certain failed US banks. In July 2017, the FDIC, on behalf of 39 failed US banks, commenced substantially similar claims against NWM Plc, RBSG plc and others in the High Court of Justice of England and Wales. The action alleges that the defendants breached English and European competition law, as well as asserting common law claims of fraud under US law.

In addition, there are two class actions against NWM Group defendants relating to JPY LIBOR and Euroyen TIBOR, both pending before the same judge in the SDNY. In the first class action, which relates to Euroyen TIBOR futures contracts, the court dismissed the plaintiffs' antitrust claims in March 2014, but declined to dismiss their claims under the Commodity Exchange Act for price manipulation. The Commodity Exchange Act claims are now the subject of a further motion to dismiss on the ground that they are impermissibly extraterritorial. The second class action relates to other derivatives allegedly tied to JPY LIBOR and Euroyen TIBOR. The court dismissed that case in March 2017 on the ground that the plaintiffs lack standing. The plaintiffs have commenced an appeal of that decision.

In addition to the above, five other class action complaints were filed against NWM Group defendants in the SDNY, each relating to a different reference rate. The SDNY dismissed all claims against NWM Plc in the case relating to Euribor for lack of personal jurisdiction in February 2017. The SDNY dismissed, for various reasons, the case relating to the Singapore Interbank Offered Rate and Singapore Swap Offer Rate on 26 July 2019, the case relating to Pound Sterling LIBOR on 16 August 2019, and the case relating to Swiss Franc LIBOR on 16 September 2019. Plaintiffs are appealing each of these four dismissals to the United States Court of Appeals for the Second Circuit. In the fifth class action, which relates to the Australian Bank Bill Swap Reference Rate, the SDNY dismissed all claims against RBS Group companies for lack of personal jurisdiction on 26 November 2018, but plaintiffs have filed an amended complaint, which is the subject of a further motion to dismiss.

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Litigation, investigations and reviews

NWM Plc has also been named as a defendant in a motion to certify a class action relating to LIBOR in the Tel Aviv District Court in Israel. NWM Plc has filed a motion for cancellation of service. If the motion is successful then the current action will be brought to an end, although the claimants may seek to re-raise the claim in the future. If the motion is unsuccessful, or the claimants seek to re-raise the claims at a later date, NWM Plc may seek to file other potentially dispositive motions.

NWM Plc was defending a claim for £446.7 million in the High Court of Justice of England and Wales brought by London Bridge Holdings Ltd and others, which was settled on confidential terms in November 2019 without admission of liability.

Details of UK litigation claims in relation to the alleged mis-sale of interest rate hedging products (IRHPs) involving LIBOR-related allegations are set out under 'Interest rate hedging products and similar litigation' on page 133.

In January 2019, a class action antitrust complaint was filed in the SDNY alleging that the defendants (USD ICE LIBOR panel banks and affiliates) have conspired to suppress USD ICE LIBOR from 2014 to the present by submitting incorrect information to ICE about their borrowing costs. The defendants include RBSG plc, NWM Plc, NWMSI and National Westminster Bank Plc. A motion to dismiss was filed by the defendants in August 2019, and remains pending before the court.

FX antitrust litigation

NWM Plc, NWMSI and / or RBSG plc, are defendants in several cases relating to NWM Plc's foreign exchange (FX) business, each of which is pending before the same federal judge in the SDNY.

In 2015, NWM Plc paid US\$255 million to settle the consolidated antitrust class action on behalf of persons who entered into over-the-counter FX transactions with defendants or who traded FX instruments on exchanges. That settlement received final court approval in August 2018. On 7 November 2018, some members of the settlement class who opted out of the settlement filed their own non-class complaint in the SDNY asserting antitrust claims against NWM Plc, NWMSI and other banks. On 31 December 2018, some of the same claimants, as well as others, filed proceedings in the High Court of Justice of England and Wales, asserting competition claims against NWM Plc and several other banks. The claim was served on 25 April 2019.

Two other FX-related class actions remain pending in the SDNY. First, there is a class action on behalf of 'consumers and end-user businesses,' which is proceeding against NWM Plc in the discovery phase following the SDNY's denial of the defendants' motions to dismiss in March 2018. Second, there is a class action on behalf of 'indirect purchasers' of FX instruments (which plaintiffs define as persons who transacted FX instruments with retail foreign exchange dealers that transacted directly with defendant banks). In January 2020, the parties in this case reached a settlement subject to agreement on non-monetary terms, documentation, and court approval. A provision has been established to cover the amount that NWM Plc would pay pursuant to the settlement.

On 27 May 2019, a class action was filed in the Federal Court of Australia against NWM Plc and other banks on behalf of persons who bought or sold currency through FX spots or forwards between 1 January 2008 and 15 October 2013 with a total transaction value exceeding AUS \$0.5 million. RBSG plc has been named in the action as a 'cartel party', but is not a defendant. The claim was served on 28 June 2019.

On 29 July and 11 December 2019, two separate applications seeking opt-out collective proceedings orders were filed in the UK Competition Appeal Tribunal ('the CAT') against RBSG plc, NWM Plc and other banks. Both applications have been brought on behalf of persons who, between 18 December 2007 and 31 January 2013, entered into a relevant FX spot or outright forward transaction in the EEA with a relevant financial institution or on an electronic communications

network. It is anticipated that the CAT will determine which of the two opt-out applications should be permitted to represent the class.

Two motions to certify FX-related class actions have been filed in the Tel Aviv District Court in Israel. RBSG plc and NWMSI have been named as defendants in the first motion. The Royal Bank of Scotland plc has been named in the second. These motions have been consolidated but not yet served on the named RBS Group companies.

Certain other foreign exchange transaction related claims have been or may be threatened. NWM Group cannot predict whether any of these claims will be pursued, but expects that some may.

Government securities antitrust litigation

NWMSI and certain other US broker-dealers are defendants in a consolidated antitrust class action pending in the SDNY on behalf of persons who transacted in US Treasury securities or derivatives based on such instruments, including futures and options. The plaintiffs allege that defendants rigged the US Treasury securities auction bidding process to deflate prices at which they bought such securities and colluded to increase the prices at which they sold such securities to plaintiffs. The defendants' motion to dismiss this matter remains pending.

Class action antitrust claims commenced in March 2019 are pending in the SDNY against NWM Plc, NWMSI and other banks in respect of Euro-denominated bonds issued by European central banks (EGBs). The complaints allege a conspiracy among dealers of EGBs to widen the bid-ask spreads they quoted to customers, thereby increasing the prices customers paid for the EGBs or decreasing the prices at which customers sold the bonds. The class consists of those who purchased or sold EGBs in the US between 2007 and 2012. The defendants have filed a motion to dismiss this matter, which remains pending.

Swaps antitrust litigation

NWM Plc, NWMSI and RBSG plc, as well as a number of other interest rate swap dealers, are defendants in several cases pending in the SDNY alleging violations of the US antitrust laws in the market for interest rate swaps. There is a consolidated class action complaint on behalf of persons who entered into interest rate swaps with the defendants, as well as non-class action claims by three swap execution facilities (TeraExchange, Javelin, and trueEx). The plaintiffs allege that the swap execution facilities would have successfully established exchange-like trading of interest rate swaps if the defendants had not unlawfully conspired to prevent that from happening through boycotts and other means. Fact discovery in these cases is complete, and the class plaintiffs have filed a motion for class certification, which as of January 2020 is fully briefed.

In addition, in June 2017, TeraExchange filed a complaint against NWM Plc, NWMSI and RBSG plc, as well as a number of other credit default swap dealers, in the SDNY. TeraExchange alleges it would have established exchange-like trading of credit default swaps if the defendant dealers had not engaged in an unlawful antitrust conspiracy. On 1 October 2018, the court dismissed all claims against NWM Plc, NWMSI and RBSG plc.

Madoff

NWM N.V. is a defendant in two actions filed by Irving Picard, as trustee for the bankruptcy estates of Bernard L. Madoff and Bernard L. Madoff Investment Securities LLC, in bankruptcy court in New York. In both cases, the trustee alleges that certain transfers received by NWM N.V. amounted to fraudulent conveyances that should be clawed back for the benefit of the Madoff estate.

In the primary action, filed in December 2010, the trustee is asking the bankruptcy court for leave to file an amended complaint, seeking to clawback a total of US\$276.3 million in redemptions that NWM N.V. allegedly received from certain Madoff feeder funds and certain swap

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Litigation, investigations and reviews

counterparties. NWM N.V. is opposing the motion for leave to file an amended complaint and otherwise will seek dismissal of the claims. In the second action, filed in October 2011, the trustee seeks to recover an additional US\$21.8 million. In November 2016, the bankruptcy court dismissed this case on international comity grounds, and that decision was appealed. On 25 February 2019, the United States Court of Appeals for the Second Circuit reversed the bankruptcy court's decision. If the U.S. Supreme Court declines to review the matter, the case will return to the bankruptcy court for further proceedings.

Interest rate hedging products and similar litigation

NWM Plc is dealing with a number of active litigation claims in the UK in relation to the alleged mis-selling of interest rate hedging products (IRHPs). In general, claimants allege that the relevant IRHPs were mis-sold to them, with some also alleging that misrepresentations were made in relation to LIBOR. Claims have been brought by customers who were considered under the UK Financial Conduct Authority (FCA) redress programme for IRHPs, as well as customers who were outside of the scope of that programme, which was closed to new entrants in March 2015. NWM Plc remains exposed to potential claims from customers who were either ineligible to be considered for redress or who are dissatisfied with their redress offers.

Separately, NWM Plc is defending claims filed in France by three French local authorities relating to structured interest rate swaps. NWM N.V. was named as a co-defendant in two of the three claims. The plaintiffs allege, among other things, that the swaps are void for being illegal transactions, that they were mis-sold, and that information / advisory duties were breached. One of the three claims is being appealed to the Supreme Court, one is being remitted from the Supreme Court to the Court of Appeal for reconsideration of one aspect, and one remains to be heard before the lower court.

Tax dispute

HMRC issued a tax assessment in 2012 against RBSG plc for approximately £86 million regarding a value-added-tax ('VAT') matter in relation to the trading of European Union Allowances ('EUAs') by a joint venture subsidiary in 2009. RBSG plc has lodged an appeal, which is still to be heard, before the First-tier Tribunal (Tax), a specialist tax tribunal, challenging the assessment (the 'Tax Dispute'). In the event that the assessment is upheld, interest and costs would be payable, and a penalty of up to 100 per cent of the VAT held to have been legitimately denied by HMRC could also be levied. Separately, NWM Plc is a named defendant in civil proceedings before the High Court of Justice of England and Wales brought in 2015 by ten companies (all in liquidation) (the 'Liquidated Companies') and their respective liquidators (together, 'the Claimants'). The Liquidated Companies previously traded in EUAs in 2009 and are alleged to be defaulting traders within (or otherwise connected to) the EUA supply chains forming the subject of the Tax Dispute. The Claimants claim approximately £71.4 million plus interest and costs and allege that NWM Plc dishonestly assisted the directors of the Liquidated Companies in the breach of their statutory duties and/or knowingly participated in the carrying on of the business of the Liquidated Companies with intent to defraud creditors. The trial in that matter concluded on 20 July 2018 and judgment is awaited.

US Anti-Terrorism Act litigation

NWM N.V. and certain other financial institutions, are defendants in several actions pending in the United States District Courts for the Eastern and Southern Districts of New York, filed by a number of US nationals (or their estates, survivors, or heirs), most of whom are or were US military personnel, who were killed or injured in attacks in Iraq between 2003 and 2011. NWM Plc is also a defendant in some of these cases.

The attacks at issue in the cases were allegedly perpetrated by Hezbollah and certain Iraqi terror cells allegedly funded by the Islamic Republic of Iran. According to the plaintiffs' allegations, the defendants are liable for damages arising from the attacks because they allegedly conspired with Iran and certain Iranian banks to assist Iran in transferring money to Hezbollah and the Iraqi terror cells, in violation of the US Anti-Terrorism Act, by agreeing to engage in 'stripping' of

transactions initiated by the Iranian banks so that the Iranian nexus to the transactions would not be detected.

The first of these actions was filed in the United States District Court for the Eastern District of New York in November 2014. On 16 September 2019, the district court dismissed the case, finding that the claims were deficient for several reasons, including lack of sufficient allegations as to the alleged conspiracy and causation. The plaintiffs are appealing the decision to the United States Court of Appeals for the Second Circuit. Another action, filed in the SDNY in 2017, was dismissed on 28 March 2019 on similar grounds. The dismissal is subject to re-pleading by the plaintiffs or appeal. Other follow-on actions that are substantially similar to the two that have now been dismissed are pending in the same courts.

Securities underwriting litigation

NWMSI is an underwriter defendant in several securities class actions in the US in which plaintiffs generally allege that an issuer of public debt or equity securities, as well as the underwriters of the securities (including NWMSI), are liable to purchasers for misrepresentations and omissions made in connection with the offering of such securities.

Investigations and reviews

NWM Group's financial condition can be affected by the actions of various governmental and regulatory authorities in the UK, the US, the EU and elsewhere. NWM Group companies have engaged, and will continue to engage, in discussions with relevant governmental and regulatory authorities, including in the UK, the US, the EU and elsewhere, on an ongoing and regular basis, and in response to informal and formal inquiries or investigations, regarding operational, systems and control evaluations and issues including those related to compliance with applicable laws and regulations, including consumer protection, business conduct, competition / anti-trust, anti-bribery, anti-money laundering and sanctions regimes.

NWM Group companies have been providing, and continue to provide, information regarding a variety of matters, including, for example, the setting of benchmark rates and related derivatives trading, conduct in the foreign exchange market, and various issues relating to the issuance, underwriting, and sales and trading of fixed-income securities, including structured products and government securities, some of which have resulted, and others of which may result, in investigations or proceedings.

Any matters discussed or identified during such discussions and inquiries may result in, among other things, further inquiry or investigation, other action being taken by governmental and regulatory authorities, increased costs being incurred by NWM Group, remediation of systems and controls, public or private censure, restriction of NWM Group's business activities and/or fines. Any of the events or circumstances mentioned in this paragraph or below could have a material adverse effect on NWM Group, its business, authorisations and licences, reputation, results of operations or the price of securities issued by it.

NWM Group is co-operating fully with the investigations and reviews described below.

US investigations relating to fixed-income securities

In the US, NWM Group companies, including NWMSI, and its affiliates, have in recent years been involved in investigations relating to, among other things, issuance, underwriting and trading in RMBS and other mortgage-backed securities and collateralised debt obligations (CDOs). Investigations by the US Department of Justice (DoJ) and several state attorneys general relating to the issuance and underwriting of RMBS were previously resolved. Certain other state attorneys general have sought information regarding similar issues, and NWM Group is aware that at least one such investigation is ongoing.

In October 2017, NWMSI entered into a non-prosecution agreement (NPA) with the United States Attorney for the District of Connecticut (USAO) in connection with alleged misrepresentations to counterparties relating to secondary trading in various forms of asset-backed securities. In the NPA, the USAO agreed not to file criminal

Notes on the accounts

28 Memorandum items continued

Litigation, investigations and reviews

charges relating to certain conduct and information described in the NPA if NWMSI complies with the NPA's reporting and conduct requirements during its term, including by not engaging in conduct during the NPA that the USAO determines was a felony under federal or state law or a violation of the anti-fraud provisions of the United States securities law.

The NatWest Markets business is currently responding to a separate criminal investigation by the USAO concerning unrelated securities trading in 2018 by certain former traders of NWM Plc, involving alleged spoofing, which was reported to the USAO in connection with the NPA. In January 2020, the NPA was extended for a fourth time (for three additional months) to accommodate advanced discussions with the USAO and the DoJ concerning potential resolution of the criminal investigation into alleged spoofing as well as the impact of that conduct and any such resolution on the status of the NPA and the potential consequences thereof. The duration and outcome of these matters remain uncertain, including in respect of whether settlement may be reached. Material adverse collateral consequences, in addition to further substantial costs and the recognition of further provisions may occur depending on the outcome of the investigation, as further described in the Risk factor relating to legal, regulatory and governmental actions and investigations set out on page 155.

Foreign exchange related investigations

In May and June 2019, RBSG plc and NWM Plc reached settlements totalling approximately EUR 275 million in connection with the EC and certain other related competition law investigations into FX trading. The aggregate amount was fully covered by existing provisions in NWM Plc. NWM Plc continues to co-operate with ongoing investigations from competition authorities on similar issues relating to past FX trading. The exact timing and amount of future financial penalties, related risks and collateral consequences remain uncertain and may be material.

In 2014 and 2015, NWM Plc paid significant penalties to resolve investigations into its FX business by the FCA, the CFTC, the DoJ, and the Board of Governors of the Federal Reserve System (Federal Reserve). As part of its plea agreement with the DoJ, NWM Plc pled guilty to a one-count information charging an antitrust conspiracy occurring between as early as December 2007 to at least April 2010. NWM Plc admitted that it knowingly, through one of its Euro/US dollar currency traders, joined and participated in a conspiracy to eliminate competition in the purchase and sale of the Euro/US dollar currency pair exchanged in the FX spot market. On 5 January 2017, the United States District Court for the District of Connecticut imposed a sentence on NWM Plc consisting of a US\$395 million fine and a three-year probation, which ended in January 2020.

As part of the settlement with the Federal Reserve, NWM Plc and NWMSI entered into a cease and desist order (the FX Order). In the

FX Order, which is publicly available and will remain in effect until terminated by the Federal Reserve, NWM Plc and NWMSI agreed to take certain remedial actions with respect to FX activities and certain other designated market activities, including the creation of an enhanced written internal controls and compliance programme, an improved compliance risk management programme, and an enhanced internal audit programme. NWM Plc and NWMSI are obligated to implement and comply with these programmes as approved by the Federal Reserve, and are also required to conduct, on an annual basis, a review of applicable compliance policies and procedures and a risk-focused sampling of key controls.

Systematic Anti-Money Laundering Programme assessment

In December 2018, the FCA commenced a Systematic Anti-Money Laundering Programme assessment of RBS Group. The FCA provided its written findings to RBS Group on 28 June 2019, and RBS Group responded on 8 August 2019. On 28 August 2019, the FCA instructed RBS Group to appoint a Skilled Person to provide assurance on financial crime governance arrangements in relation to two financial crime change programmes. RBS Group is cooperating with the Skilled Person's review, which is expected to conclude during Q1 2020. It is not yet possible to assess the likely impact of these matters.

US/Swiss tax programme

In December 2015, Coutts & Co Ltd, a member of NWM Group, incorporated in Switzerland, entered into a four-year non-prosecution agreement (the NPA) with the DoJ that required it to pay a penalty of US\$78.5 million. This was entered into as part of the DoJ's programme for Swiss banks, related to its investigations of the role that Swiss banks played in concealing the assets of US tax payers in offshore accounts (US related accounts). On 20 December 2019, Coutts & Co. Ltd agreed to pay an additional US\$27.9 million penalty relating to additional US related accounts that it had not identified and disclosed to DOJ at the time the NPA was executed in 2015. The additional penalty amount has been paid. The four-year term of the NPA has now expired, though certain document preservation and cooperation obligations continue.

Enforcement proceedings and investigations in relation to Coutts & Co Ltd

In February 2017, the Swiss Financial Market Supervisory Authority (FINMA) took enforcement action against Coutts & Co Ltd with regard to failures of money laundering checks and controls on certain client accounts that were connected with the Malaysian sovereign wealth fund, 1MDB, and were held with Coutts & Co Ltd. FINMA accordingly required Coutts & Co Ltd to disgorge profits of CHF 6.5 million. With the exception of one administrative criminal proceeding against a former employee of Coutts & Co Ltd, there are no administrative or regulatory proceedings pending against current or former employees. In addition, the Monetary Authority of Singapore (MAS)'s supervisory examination of Coutts & Co Ltd's Singapore branch revealed breaches of anti-money laundering requirements. MAS imposed on Coutts & Co Ltd financial penalties amounting to SGD 2.4 million in December 2016.

29 Analysis of the net investment in business interests and intangible assets

Acquisitions and disposals

	NWM Group		NWM Plc	
	2019 £m	2018 £m	2019 £m	2018 £m
Fair value given for businesses acquired	2,460	(48)	(69)	—
Value recognised for business transferred from fellow subsidiary	—	(496)	—	—
Non-cash consideration on acquisition	—	—	—	292
Additional and new investments in Group undertakings	—	—	—	(920)
Net inflow/(outflow) of cash in respect of acquisitions	2,460	(544)	(69)	(628)
Net inflow of cash in respect of disposals	1,245	2,089	1,270	22,373
Dividends received from associates	—	2	—	—
Net (outflow)/inflow	3,705	1,547	1,201	21,745

Notes on the accounts

30 Analysis of changes in financing during the year

	NWM Group					
	Share capital, share premium and paid in equity		Subordinated liabilities		MREs	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
At 1 January	2,908	44,297	2,620	—	5,125	—
Issue of Additional Tier 1 Capital notes	—	749	—	—	—	—
Issue of subordinated liabilities	—	—	1,015	—	—	—
Redemption of subordinated liabilities	—	—	(896)	(3,769)	—	—
Interest on subordinated liabilities	—	—	28	—	—	—
Issue of MREs	—	—	—	—	—	5,125
Interest on MREs	—	—	—	—	(182)	—
Net cash inflow/(outflow) from financing	—	749	147	(3,769)	(182)	5,125
Release of merger reserve	—	(10,881)	—	—	—	—
Court approved distribution	—	(33,901)	—	—	—	—
Currency translation and other adjustments (1)	155	2,644	389	6,389	(177)	—
At 31 December	3,063	2,908	3,156	2,620	5,120	5,125

	NWM Plc					
	Share capital, share premium and paid in equity		Subordinated liabilities		MREs	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
At 1 January	2,908	33,416	2,620	—	5,125	—
Issue of Additional Tier 1 Capital notes	—	749	—	—	—	—
Issue of subordinated liabilities	—	—	1,015	—	—	—
Redemption of subordinated liabilities	—	—	(896)	(3,769)	—	—
Interest on subordinated liabilities	—	—	(7)	—	—	—
Issue of MREs	—	—	—	—	—	5,125
Interest on MREs	—	—	—	—	(182)	—
Net cash inflow/(outflow) from financing	—	749	112	(3,769)	(182)	5,125
Court approved distribution	—	(33,901)	—	—	—	—
Currency translation and other adjustments (1)	155	2,644	(122)	6,389	(177)	—
At 31 December	2,908	2,908	2,610	2,620	5,120	5,125

Note:

(1) Includes the redemption of preference shares issued by NWM Plc to the parent company, RBSG plc, which were redeemed in 2018.

31 Analysis of cash and cash equivalents

	NWM Group (1)		NWM Plc (1)	
	2019 £m	2018 £m	2019 £m	2018 £m
At 1 January				
- cash	11,188	153	11,095	93
- cash equivalents	14,939	25,530	13,480	12,965
	26,127	25,683	24,575	13,058
Net cash inflow/(outflow)	916	444	(1,617)	11,517
At 31 December	27,043	26,127	22,958	24,575
Comprising:				
Cash and balances at central banks	12,729	11,188	9,953	11,095
Treasury bills and debt securities	979	83	979	83
Loans to banks	13,335	14,856	12,026	13,397
Cash and cash equivalents	27,043	26,127	22,958	24,575

Note:

(1) Includes cash collateral posted with bank counterparties in respect of derivative liabilities of £7,554 million (2018 - £7,255 million, 2017 - £6,883 million).

Certain members of NWM Group are required by law or regulation to maintain balances with the central banks in the jurisdictions in which they operate. These balances are set out below.

	2019	2018	2017
Bank of England	£0.4bn	£0.9bn	£0.6bn

Notes on the accounts

32 Directors' and key management remuneration

Up to 30 April 2018 the executive and non-executive directors of NWM Plc were also directors of the ultimate holding company and were remunerated for their services to RBS Group as a whole. NWM Plc did not remunerate these executive directors in this period nor could their remuneration be apportioned in respect of their services to NWM Plc.

Robert Begbie was appointed Interim Chief Executive Officer of NWM Plc on 18 December 2019. Mr Begbie is employed and remunerated by NWM Plc for his services to RBS Group as a whole, but is not a director of RBSG plc.

The directors' emoluments in the table below represent the emoluments of the new executive and non-executive directors for the period from which they were appointed in 2018 and the remuneration of the RBSG plc directors as disclosed in the 2019 Annual Report and Accounts of RBSG plc.

	2019		2018	
	NWM Plc £000	RBS Group £000	NWM Plc £000	RBS Group £000
Directors' remuneration				
Non Executive Directors	230	96	460	519
Chairman and executive directors - emoluments	1,026	2,330	2,396	1,690
	1,256	2,426	2,856	2,209
Total	1,256	2,426	2,856	2,209

The total emoluments and amounts receivable under long-term incentive plans and share option plans of the highest paid director were £2,034,000 (2018 - £1,404,000).

No directors accrued benefits under defined benefit schemes or money purchase schemes during 2019 and 2018.

The executive directors may participate in RBS Group's long-term incentive plans, executive share option and sharesave schemes. Where directors of the Bank are also directors of RBSG, details of their share interests can be found in the 2019 Annual Report and Accounts of the RBS Group, in line with regulations applying to RBSG as a premium listed company.

Compensation of key management

The compensation of key management also changed significantly in 2018. Until the changes in April 2018 key management represented the RBS Group directors and Executive Committee members and is presented as disclosed in the RBS Group Annual Report and Accounts. From April 2018 key management is NWM Plc's directors and Executive Committee and the emoluments presented below represent the period from which they were appointed in 2018.

	2019		2018	
	NWM Plc £000	RBS Group £000	NWM Plc £000	RBS Group £000
Short term benefits	20,463	2,426	22,143	2,209
Post employment benefits	283	—	(4)	—
Share based payments	484	—	—	—
	21,230	2,426	22,139	2,209

33 Transactions with directors and key management

At 31 December 2019, amounts outstanding in relation to transactions, arrangements and agreements entered into by authorised institutions in NWM Group, as defined in UK legislation, were £93,145 in respect of loans to three persons who were directors of the company at any time during the financial period.

For the purposes of IAS 24 'Related Party Disclosures', key management comprise directors of the company and members of the Bank Executive Committee. Applying the captions in the NWM Group's primary financial statements the following amounts⁽¹⁾ are attributable, in aggregate, to key management.

	2019 £000	2018 £000
Loans to customers	93	12
Customer deposits	4,771	2,950

Key management have banking relationships with Group 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. Key management had no reportable transactions or balances with the holding company.

Note:

(1) Amounts are attributed to each person at their highest level of RBS Group key management.

Notes on the accounts

34 Related parties

UK Government

On 1 December 2008, the UK Government through HM Treasury became the ultimate controlling party of The Royal Bank of Scotland Group plc. 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 became related parties of NWM Group.

In 2015, HM Treasury sold 630 million of RBSG plc's ordinary shares and a further 925 million in June 2018. At 31 December 2019, HM Treasury's holding in RBSG plc's ordinary shares was 62.1%.

NWM 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 (refer to Note 7) and value added tax; national insurance contributions; local authority rates; 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

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

Members of NWM 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. They also have access to Bank of England reserve accounts: sterling current accounts that earn interest at the Bank of England Rate.

Service provision from NatWest Bank Plc

On 30 April 2018, in preparation for ring-fencing, NatWest Bank Plc became the main provider of shared service activities for RBS Group. This includes NatWest Bank Plc providing services to NWM Group companies.

Other related parties

- (a) In their roles as providers of finance, NWM Group companies provide development and other types of capital support to businesses. These investments are made in the normal course of business. In some instances, the investment may extend to ownership or control over 20% or more of the voting rights of the investee company. However, these investments are not considered to give rise to transactions of a materiality requiring disclosure under IAS 24.
- (b) NWM Group recharges The Royal Bank of Scotland Group Pension Fund with the cost of administration services incurred by it. The amounts involved are not material to NWM Group.
- (c) In accordance with IAS 24, transactions or balances between NWM Group entities that have been eliminated on consolidation are not reported.
- (d) The captions in the primary financial statements of the parent company include amounts attributable to subsidiaries. These amounts have been disclosed in aggregate in the relevant notes to the financial statements.

The table below discloses transactions between NWM Group and fellow subsidiaries of RBS Group.

	2019 £m	2018 £m
Interest receivable	—	53
Interest payable	(313)	(315)
Fees and commissions receivable	3	3
Fees and commissions payable	(83)	(8)
Continuing operations	(393)	(267)
Discontinued operations	—	(720)

35 Ultimate holding company

NWM Group's ultimate holding company is The Royal Bank of Scotland Group plc which is incorporated in Great Britain and registered in Scotland. As at 31 December 2019, The Royal Bank of Scotland Group plc heads the largest group in which NWM Group is consolidated. Copies of the consolidated accounts may be obtained from The Secretary, The Royal Bank of Scotland Group plc, Gogarburn, PO Box 1000, Edinburgh EH12 1HQ.

Following placing and open offers by The Royal Bank of Scotland Group plc in December 2008 and April 2009, the UK Government, through HM Treasury, currently holds 62.1% of the issued ordinary share capital of the holding company and was therefore the NWM Group's ultimate controlling party.

36 Post balance sheet events

RBS Group intends to refocus the NatWest Markets business. As a result, NWM Group estimates it will incur exit, restructuring and disposal costs of around £0.6 billion in 2020. This estimate may be revised as plans to refocus the business are finalised.

Notes on the accounts

37 Related undertakings

Legal entities and activities at 31 December 2019

In accordance with the Companies Act 2006, NWM Plc's related undertakings and the accounting treatment for each are listed below. All undertakings are wholly-owned by NWM Plc or subsidiaries of NWM Plc and are consolidated by reason of contractual control (Section 1162(2) CA 2006), unless otherwise indicated. RBS Group interest refers to ordinary shares of equal values and voting rights unless further analysis is provided in the notes. Activities are classified in accordance with Annex I to the Capital Requirements Directive ("CRD IV") and the definitions in Article 4 of the Capital Requirements Regulation.

The following table details active related undertakings incorporated in the UK which are 100% owned by NWM Group and fully consolidated for accounting purposes

Entity name	Activity	Regulatory treatment	Notes	Entity name	Activity	Regulatory treatment	Notes
280 Bishopsgate Finance Ltd	INV	FC	(1)	Property Venture Partners Ltd	INV	FC	(3)
Care Homes 1 Ltd	BF	FC	(1)	R.B. Equipment Leasing Ltd	BF	FC	(1)
Care Homes 2 Ltd	BF	FC	(1)	R.B. Leasing (April) Ltd	BF	FC	(1)
Care Homes 3 Ltd	BF	FC	(1)	R.B. Leasing (December) Ltd	BF	FC	(1)
Care Homes Holdings Ltd	BF	FC	(1)	R.B. Leasing Company Ltd	BF	FC	(3)
Churchill Management Ltd	BF	FC	(8)	R.B.S. Special Investments Ltd	BF	FC	(1)
Desertlands Entertainment Ltd	BF	FC	(1)	RB Investments 3 Ltd	OTH	FC	(1)
Distant Planet Productions Ltd	BF	FC	(1)	RBOS (UK) Ltd	BF	FC	(1)
Helena Productions Ltd	BF	FC	(1)	RBS Investment Ltd	BF	FC	(3)
Lombard Corporate Finance (6) Ltd	BF	FC	(1)	RBS Management Services (UK) Ltd	SC	FC	(1)
Lombard Corporate Finance (7) Ltd	BF	FC	(1)	RBS Mezzanine Ltd	BF	FC	(3)
Lombard Corporate Finance (11) Ltd	BF	FC	(1)	RBS Property Developments Ltd	INV	FC	(27)
Lombard Corporate Finance (13) Ltd	BF	FC	(1)	RBS Property Ventures Investments Ltd	BF	FC	(3)
Lombard Corporate Finance (15) Ltd	BF	FC	(1)	RBSM Capital Ltd	BF	FC	(3)
Nanny McPhee Productions Ltd	BF	FC	(1)	RBSSAF (6) Ltd	BF	FC	(1)
NatWest Markets Secretarial Services Ltd	SC	FC	(1)	RBSSAF (12) Ltd	BF	FC	(1)
NatWest Markets Secured Funding LLP	BF	FC	(7)	RoboScot Equity Ltd	BF	FC	(3)
P of A Productions Ltd	BF	FC	(1)	Royal Bank Investments Ltd	BF	FC	(3)
Patalex II Productions Ltd	BF	FC	(1)	Royal Bank Ventures Investments Ltd	BF	FC	(3)
Patalex III Productions Ltd	BF	FC	(1)	Sandford Leasing Ltd	BF	FC	(1)
Patalex IV Productions Ltd	BF	FC	(1)	Theobald Film Productions LLP	BF	FC	(1)
Patalex V Productions Ltd	BF	FC	(1)	West Register (Hotels Number 3) Ltd	INV	DE	(3)
Patalex Productions Ltd	BF	FC	(1)	West Register (Property Investments) Ltd	BF	DE	(3)
Price Productions Ltd	BF	FC	(1)	West Register (Realisations) Ltd	INV	DE	(3)
Priority Sites Investments Ltd	BF	DE	(1)	Winchcombe Finance Ltd	BF	FC	(1)
Priority Sites Ltd	INV	DE	(1)				

The following table details active related undertakings incorporated outside the UK which are 100% owned by NWM Group and fully consolidated for accounting purposes

Entity name	Activity	Regulatory treatment	Notes	Entity name	Activity	Regulatory treatment	Notes
AA Merchant Banking B.V.	BF	FC	(2)	RBS Acceptance Inc.	BF	FC	(11)
Alcover A.G.	BF	DE	(4)	RBS Americas Property Corp.	SC	FC	(11)
Alternative Investment Fund B.V.	BF	FC	(2)	RBS Asia Holdings B.V.	BF	FC	(2)
Candlelight Acquisition LLC	BF	FC	(11)	RBS Assessoria Ltd	SC	FC	(31)
Coutts & Co Ltd	BF	FC	(13)	RBS Commercial Funding Inc.	BF	FC	(11)
Coutts & Co Trustees (Suisse) S.A.	BF	FC	(14)	RBS Employment (Guernsey) Ltd	SC	FC	(33)
Coutts General Partner (Cayman) V Ltd	BF	FC	(15)	RBS Equity Corporation	BF	FC	(34)
Financial Asset Securities Corp.	BF	FC	(11)	RBS European Investments SARL	BF	FC	(35)
KEB Investors, L.P.	BF	FC	(22)	RBS Financial Products Inc.	BF	FC	(11)
Keep SPV Ltd	BF	FC	(23)	RBS Holdings N.V.	BF	FC	(37)
Morar ICC Insurance Ltd	BF	DE	(25)	RBS Holdings USA Inc.	BF	FC	(11)
NatWest Markets Group Holdings Corporation	BF	FC	(11)	RBS Hollandsche N.V.	BF	FC	(37)
NatWest Markets N.V.	CI	FC	(2)	RBS Investments (Ireland) Ltd	BF	FC	(16)
NatWest Markets Securities Inc.	INV	FC	(11)	RBS Netherlands Holdings B.V.	BF	FC	(2)
NatWest Markets Securities Japan Ltd	INV	FC	(28)	RBS Nominees (Ireland) Ltd	BF	FC	(16)
NWM Services India Private Ltd	SC	FC	(26)	RBS Nominees (Netherlands) B.V.	BF	FC	(2)
R.B. Leasing BDA One Ltd	BF	FC	(29)	RBS WCS Holding Company	BF	FC	(32)
Random Properties Acquisition Corp. III	INV	FC	(11)				

Notes on the accounts

37 Related undertakings continued

The following table details active related undertakings incorporated in the UK where NWM Group ownership is less than 100%

Entity name	Activity	Accounting treatment	Regulatory treatment	Group %	Notes	Entity name	Activity	Accounting treatment	Regulatory treatment	Group %	Notes
Higher Broughton (GP) Ltd	BF	EAA	PC	41	(19)	Isobel Loan Capital Ltd	BF	FC	FC	75	(21)
Higher Broughton Partnership LP	BF	EAA	DE	41	(20)	Isobel Mezzanine Borrower Ltd	BF	FC	FC	75	(21)
Isobel AssetCo Ltd	BF	FC	FC	75	(21)	Land Options (East) Ltd	BF	EAJV	DE	50	(3)
Isobel EquityCo Ltd	BF	FC	FC	75	(21)	NatWest Markets Secured Funding (LM) Ltd	BF	FC	PC	20	(38)
Isobel HoldCo Ltd	BF	FC	FC	75	(21)	RBS Sempra Commodities LLP	BF	FC	FC	51	(3)
Isobel Intermediate HoldCo Ltd	BF	FC	FC	75	(21)						

The following table details active related undertakings incorporated outside the UK where NWM Group ownership is less than 100%

Entity name	Activity	Accounting treatment	Regulatory treatment	Group %	Notes	Entity name	Activity	Accounting treatment	Regulatory treatment	Group %	Notes
Cesium Structured Funding Ltd	BF	FC	FC	0	(12)	Solar Energy Capital Europe SARL	BF	EAJV	PC	33	(35)
Eris Finance S.R.L.	BF	IA	PC	45	(24)	Thames Asset Global Securitization No.1 Inc.	BF	FC	FC	0	(39)
Galaxy Futures Company Ltd	BF	EAA	PC	17	(17)	Tulip Asset Purchase Company B.V.	BF	FC	FC	0	(40)
German Public Sector Finance B.V.	BF	EAJV	PC	50	(18)						
Lunar Funding VIII Ltd	BF	FC	DE	0	(10)						
Sempra Energy Trading LLC	BF	FC	FC	51	(11)						

The following table details related undertakings that are not active (actively being dissolved)

Entity name	Accounting treatment	Regulatory treatment	Group %	Notes	Entity name	Accounting treatment	Regulatory treatment	Group %	Notes
Alsecure Life Insurance PCC Ltd	FC	DE	100	(5)	RB Investments 2 Ltd	FC	FC	100	(1)
Alsecure US PCC Ltd	FC	DE	100	(6)	RB Investments 5 Ltd	FC	FC	100	(1)
Arran Cards Funding Plc	FC	FC	0	(7)	RBDC Administrator Ltd	FC	FC	100	(3)
Arran Residential Mortgages Funding 2010-1 Plc	FC	FC	0	(7)	RBS Asset Management Ltd	FC	FC	100	(1)
Arran Residential Mortgages Funding 2011-1 Plc	FC	FC	0	(7)	RBS Bank (Polska) S.A.	FC	FC	100	(30)
Arran Residential Mortgages Funding 2011-2 Plc	FC	FC	0	(7)	RBS Group (Australia) Pty Ltd	FC	FC	100	(36)
Greenock Funding No 5 Plc	FC	FC	0	(7)	RBS Holdings III (Australia) Pty Ltd	FC	FC	100	(36)
Heartlands (Central) Ltd	FC	DE	100	(3)	RoboScot Ventures Ltd	FC	FC	100	(3)
KUC (Public Houses) Ltd	FC	DE	100	(8)	RoyScot Financial Services Ltd	FC	FC	100	(1)
Maja Finance S.R.L.	FC	FC	98	(24)	Style Financial Services Ltd	FC	FC	100	(3)
Mulcaster Street Nominees Ltd	FC	FC	100	(9)	Total Capital Finance Ltd	FC	FC	100	(8)
Nevis Derivatives No. 3 LLP	FC	FC	100	(7)	West Register (Hotels Number 1) Ltd	FC	DE	100	(3)
					West Register (Land) Ltd	FC	DE	100	(3)
					West Register (Project Developments) Ltd	FC	DE	100	(3)
					West Register Hotels (Holdings) Ltd	FC	FC	100	(3)

The following table details related undertakings that are dormant

Entity name	Accounting treatment	Regulatory treatment	Group %	Notes	Entity name	Accounting treatment	Regulatory treatment	Group %	Notes
Buchanan Holdings Ltd	FC	FC	100	(8)	RBOS Nominees Ltd	FC	FC	100	(1)
Glyns Nominees Ltd	FC	FC	100	(1)	RBS Cards Securitisation Funding Ltd	FC	FC	100	(9)
Marigold Nominees Ltd	FC	FC	100	(8)	Sixty Seven Nominees Ltd	FC	FC	100	(8)
N.C. Head Office Nominees Ltd	FC	FC	100	(3)	The Royal Bank of Scotland (1727) Ltd	FC	FC	100	(3)
Project & Export Finance (Nominees) Ltd	FC	FC	100	(8)	Williams & Glyn's Bank Ltd	FC	FC	100	(8)

Notes on the accounts

37 Related undertakings continued

The following table details the overseas branches of NWM Group

Subsidiary	Geographic location	Subsidiary	Geographic location
Coutts & Co Ltd	Hong Kong		Germany, Hong Kong, Japan, Singapore,
	France, Germany, Hong Kong, Italy, Republic of Ireland, Spain, Sweden,	NatWest Markets Plc	Turkey, United Arab Emirates
NatWest Markets N.V.	United Kingdom		

Key:

BF	Banking and financial institution
CI	Credit institution
INV	Investment (shares or property) holding company
SC	Service company
TR	Trustee
OTH	Other
DE	Deconsolidated
FC	Full consolidation
PC	Pro-rata consolidation
EAA	Equity accounting – Associate
EAJV	Equity accounting – Joint venture
IA	Investment accounting
NC	Not consolidated

Notes	Registered addresses	Country of incorporation
(1)	250 Bishopsgate, London, EC2M 4AA, England	UK
(2)	Claude Debussylaan 94, 1082 MD, Amsterdam,	Netherlands
(3)	24/25 St Andrew Square, Edinburgh, EH2 1AF, Scotland	UK
(4)	Tirolerweg 8, Zug, CH-6300	Switzerland
(5)	Level 5, Mill Court, La Charroterie, St Peter Port, GY1 1EJ	Guernsey
(6)	3rd Floor, Dixcart House, Sir William Place, St Peter Port, GY1 1GX	Guernsey
(7)	35 Great St Helen's, London, EC3A 6AP, England	UK
(8)	1 Princes Street, London, EC2R 8BP, England	UK
(9)	Royal Bank House, 71 Bath Street, St Helier, JE4 8PJ	Jersey
(10)	Boundary Hall, Cricket Square, 171 Elgin Avenue, George Town, Grand Cayman, KY1-1104	Cayman Islands
(11)	251, Little Falls Drive, Wilmington, Delaware, 19808	USA
(12)	5 Harbourmaster Place, Dublin 1, D01 E7E8	Rol
(13)	Lerchenstrasse 18, Zurich, CH-8022	Switzerland
(14)	c/o Regus Rue du Rhone Sarl, Rue du Rhone 14, 1204, Geneva	Switzerland
(15)	c/o Maples Corporate Services Ltd, PO Box 309, 121 South Church Street, George Town, Grand Cayman, KY1-1104	Cayman Islands
(16)	Ulster Bank Group Centre, George's Quay, Dublin 2, D02 VR98	Rol
(17)	9th Floor, SOHO Century Plaza, 1501 Century Avenue, Pudong New Area, Shanghai	China
(18)	De entree 99 -197, 1101 HE Amsterdam Zuidooost	Netherlands
(19)	3rd Floor, 1 St Ann Street, Manchester, M2 7LR, England	UK
(20)	Cornwall Buildings, 45-51 Newhall Street, Birmingham, B3 3QR, England	UK
(21)	40 Berkeley Square, London, W1J 5AL, England	UK
(22)	Clarendon House, Two Church Street, Suite 104, Reid Street, Hamilton, HM 11	Bermuda
(23)	66-72, Gaspé House, Esplanade, St Helier, JE2 3QT	Jersey
(24)	Via Vittorio Alfieri 1, Conegliano TV, IT-TN 31015	Italy
(25)	PO Box 384, The Albany, South Esplanade, St Peter Port, GY1 4NF	Guernsey
(26)	c/o CE Serviced Offices Pvt Ltd, Level 1, Tower A, Building No 10, Phase III, DLF Cyber City, Gurgaon, Haryana, 122002	India
(27)	36 St Andrew Square, Edinburgh, EH2 2YB, Scotland	UK
(28)	Level 54, Hopewell Centre, 183 Queen's Road East	Hong Kong
(29)	Victoria Place, 5th Floor, 31 Victoria Street, Hamilton, HM 10	Bermuda
(30)	Wiśniowy Business Park, ul. 1-go Sierpnia 8A, Warsaw, 02-134	Poland
(31)	254, 13th Floor, Rua Boa Vista, Sao Paulo, 01014-907	Brazil
(32)	1209, Orange Street, Wilmington, Delaware, 19801	USA
(33)	Regency Court, Glatigny Esplanade, St Peter Port, GY1 3AP	Guernsey
(34)	340, Madison Avenue, New York, 10173	USA
(35)	46, Avenue John F. Kennedy, L-1855	Luxembourg
(36)	Ashurst L26, 181 William Street, Melbourne, VIC, 3000	Australia
(37)	Gustav Mahlerlaan 350, 1082 ME, Amsterdam	Netherlands
(38)	c/o Intertrust Group, 35 Great St Helens, London, EC3A 6AP, England	UK
(39)	114 West 47th Street, New York, 10036	USA
(40)	Claude Debussylaan 24, 1082 MD, Amsterdam	Netherlands

Risk Factors

Principal Risks and Uncertainties

Set out below are certain risk factors that could adversely affect the NWM Group's future results, its financial condition and prospects and cause them to be materially different from what is forecast or expected and directly or indirectly impact the value of its securities in issue. These risk factors are broadly categorised and should be read in conjunction with other sections of this annual report, including the forward looking statements section, the strategic report and the capital and risk management section, and should not be regarded as a complete and comprehensive statement on its own of all potential risks and uncertainties facing the NWM Group.

Strategic risk

The RBS Group has announced a new strategy that will require changes in the NWM Group's business, including reductions in capital allocated to the NWM Group, its cost base and complexity. This entails material execution, commercial and operational risks for the NWM Group.

On 14 February 2020, the RBS Group announced a new strategy, focused on becoming a Purpose-led business. This new strategy will require changes in the NWM Group's business, including an increased focus on serving the RBS Group's corporate and institutional customer base. Over the medium term, NWM Group intends to simplify its operating model and technology platform, as well as reduce its cost base and capital requirements. Together, these initiatives are referred to as the 'NWM Refocusing'. The changes required are substantial, will be implemented over several years, and may not result in the expected outcome within the timeline and in the manner contemplated.

A part of the NWM Refocusing is the intended reduction in NWM Group's level of Risk weighted assets (RWAs). This includes an expected reduction in NWM Plc's RWAs by £14-18 billion in the medium term, through accelerating the exit of exposures and an optimisation of inefficient capital across the NWM Group, especially in relation to its Rates products. The NWM Refocusing entails significant commercial, operational and execution risks and is based on certain material assumptions that may prove to be incorrect should, for example, RWAs take longer to exit or are more costly to reduce than anticipated or not possible to exit at all. In addition, it is anticipated that the NWM Group will generate operating losses over the course of the transition plan period and therefore the NWM Group's capital levels will also decline. Moreover, it is anticipated that NWM Plc's capital ratios will be maintained, as the level of RWAs is anticipated to fall more quickly than capital levels. However, capital levels could decline at a faster pace than expected (with a corresponding effect on the capital ratios), should RWA exit costs or operating costs be higher than anticipated, revenues reduce relatively faster than costs as a result of execution issues or market conditions, or if NWM Plc and/or NWM N.V. have difficulties accessing the funding market

on acceptable terms or at all (including if the legal entity credit ratings are negatively impacted). Should any of the above arise, additional management actions by the NWM Group or the RBS Group may be triggered. The implementation of the NWM Refocusing is also expected to result in material costs for the NWM Group and could be materially higher than anticipated, including due to material uncertainties and factors outside of the NWM Group's control, or phased in a manner other than currently expected.

The NWM Refocusing is highly complex and the NWM Group may not be able to successfully implement all aspects of it or reach any or all of the related targets or expectations within the timeframes contemplated, or at all. More generally, the targets and expectations that accompany the NWM Refocusing are based on management plans, projections and models, and are subject to a number of key assumptions and judgments, any of which may prove to be inaccurate. The scale and scope of the intended changes present material and increased operational, IT system, culture, conduct, business and financial risks to the NWM Group, especially during the planning and implementation period. The NWM Refocusing is resource-intensive and disruptive, and will divert management resources, adding to the challenge for the new senior management team of the NWM Group. In addition, the scale of changes being concurrently implemented will require the implementation and application of robust governance and controls frameworks and further consolidation of IT systems and there is no guarantee that the NWM Group will be successful in doing so.

The focus on meeting cost reduction targets will require head-count reductions and may also result in limited investment in other areas which could affect the NWM Group's long-term prospects, product offering or competitive position and its ability to meet its other targets. A significant proportion of the cost savings are dependent on simplification of the IT systems and therefore may not be realised in full if IT capabilities are not delivered in line with assumptions. These risks will be present throughout the period of refocusing and alignment which is expected to last for the medium term.

Each of these risks could jeopardise the delivery and implementation of the NWM Refocusing, result in higher than expected costs, impact the NWM Group's products and services offering, reputation with customers or business model and adversely impact the NWM Group's ability to deliver its strategy and meet its targets and guidance, any of which could in turn have a material adverse impact on the NWM Group's results of operations, financial condition and prospects. The NWM Refocusing envisages a smaller scaled business and its successful implementation will result in substantially lower revenues.

As a result, there can be no certainty that the NWM Refocusing will be successfully

executed, that the NWM Group will meet targets and expectations, or that the refocused NWM Group will be a viable, competitive business aligned to the RBS Group's corporate and institutional customer offering.

The NWM Group may not be able to successfully implement the NWM Refocusing and it may not achieve its targets and the NWM Group may not ultimately result in a viable, competitive business.

As part of the NWM Refocusing, the NWM Group has set a number of financial, capital and operational targets and expectations. These include (but are not limited to) expectations relating to reductions in RWAs and the timing thereof, and CET1 ratio.

The successful implementation of the NWM Refocusing is highly complex and the ability to meet associated targets and expectations is subject to various internal and external factors and risks. These include, but are not limited to, market, regulatory, economic and political uncertainties, operational risks, insufficient cost reduction plans, risks relating to the RBS Group's and NWM Group's business models and strategies and delays or difficulties in implementing the NWM Refocusing. The successful implementation of the NWM Refocusing will also depend on how the NWM Refocusing is perceived by its customers, regulators, rating agencies, stakeholders and the wider market, how that impacts its business, and the NWM Group's ability to retain employees required to deliver the transition and its go-forward strategic priorities.

Revenues will be negatively impacted, and the implementation may be more difficult or expensive than expected. Costs relating to the NWM Refocusing may also be higher than anticipated. The orderly run-down of certain of its portfolios and the targeted reduction of its risk-weighted assets will be accompanied by the recognition of disposal losses which may be higher than anticipated, including due to future stresses which may place NWM Plc's capital ratios under pressure. Furthermore, regulatory pressures or changes in the economic and political and regulatory environment in which the NWM Group operates or regulatory uncertainty or economic volatility, including (but not limited to) as a result of the continued uncertainty surrounding the terms of the UK's exit from the EU, or changes in the scale and timing of policy responses on climate change, may require the NWM Group to adjust aspects of the NWM Refocusing or the timeframe for its implementation.

The NWM Group's ability to serve its customers may be diminished by the implementation of the NWM Refocusing. In addition, customer reactions to the changed nature of the NWM Group's business model as a result may be more adverse than expected and previously anticipated revenue and profitability levels may not be achieved in the timescale envisaged or at all. An adverse

Risk Factors

macroeconomic environment, including sustained low interest rates, continued political and regulatory uncertainty and/or strong market competition may also pose significant challenges to the successful implementation of the NWM Refocusing and the achievement of its targets. The prolonged period of implementation and changed nature of the NWM Group's business may also adversely affect the credit rating assigned to NWM Plc and certain of its subsidiaries (including NWM N.V.) or any of their respective debt securities, which could adversely affect the availability and cost of funding for the NWM Group and negatively impact the NWM Group's liquidity position.

Should the NWM Group not be able to implement or execute the NWM Refocusing as contemplated, it may negatively impact revenues for the NWM Group, its ability to meet targets and expectations and could lead to revisions to the NWM Refocusing strategy, including management actions by the RBS Group. Such changes and revisions could have an adverse effect on the NWM Group, and may affect its ability to be a viable and competitive business.

The RBS Group has announced a new Purpose-led Strategy which will further influence the NWM Refocusing and the go-forward strategy of the NWM Group.

On 14 February 2020 the RBS Group announced a new strategy, focused on becoming a more purpose-led business, designed to champion potential, and to help individuals, families and businesses to thrive. The strategy has three areas of focus – climate change, enterprise and learning – where the RBS Group believes it can have the greatest positive impact. Together, these strategic initiatives are referred to as the RBS Group's 'Purpose-led Strategy'. To deliver against this purpose and deliver sustainable returns, the RBS Group intends to: focus on the lifecycles of its customers using insights about customers to evolve product and service offerings; re-engineer and simplify the RBS Group by updating operational capability and technology and strengthening governance and control frameworks to reduce costs and improve customer journeys; focus on innovation and partnership to drive change and achieve growth in new product areas and customer segments; and have a sharper focus on capital allocation and deploy it more effectively for customers, in particular through the NWM Refocusing.

The implementation of the new Purpose-led Strategy is highly complex and will require the NWM Group to set supporting targets and implement a large number of concurrent and interdependent actions and initiatives, including the NWM Refocusing, any of which could fail to be implemented in the manner and to the extent contemplated, due to operational, legal, execution or other issues. The anticipated changes for NWM Group to support the RBS Group's successful implementation of the Purpose-led Strategy are expected to be substantial and some will take many years to fully embed and may not

result in the expected outcome on the timeline and in the manner contemplated. See also 'The RBS Group's Purpose-led Strategy includes one area of focus on climate change which entails significant execution risk and is likely to require material changes to the business model of the RBS Group (including the NWM Group) over the next ten years'.

As part of its new Purpose-led Strategy, the RBS Group has set a number of financial, capital and operational targets and expectations, both for the short term and throughout the implementation period. In addition to the NWM Refocusing, the RBS Group will require significant reductions to its wider cost base. In addition to requiring additional cost reductions within the NWM Group, this could affect the cost and scope of the RBS Group's provision of services to the NWM Group, which individually and collectively may impact the NWM Group's competitive position and its ability to meet its other targets. The implementation and delivery of the Purpose-led Strategy by the RBS Group could have a material adverse impact on the NWM Group's results of operations, financial condition and prospects.

The RBS Group's Purpose-led Strategy includes one area of focus on climate change which entails significant execution risk and is likely to require material changes to the business model of the RBS Group (including the NWM Group) over the next ten years.

The RBS Group's new strategy on climate change, together with its commitments under the UN Principles on Responsible Banking to align its strategy to the 2015 Paris Agreement will require the NWM Group to dedicate resource to the RBS Group's efforts to develop the capacity and methodology to understand, and measure the climate impact of the emissions from its financing activity. The RBS Group must identify its approach to this on a short time scale to meet its target of setting and publishing sector-specific targets by 2021 and its goal of setting comprehensive climate impact scenario-based reduction targets and plans for alignment to the 2015 Paris Agreement by 2022, and be able to adequately define and benchmark its current climate impact to demonstrate its progress against its ambition to reduce this by half over the next ten years.

The NWM Group therefore expects to set targets for reductions to the NWM Group's financed emissions which are currently unknown in scope and nature but are expected to be significant. These targets, together with the impact of embedding climate into its risk framework and other regulatory, policy and market changes, is likely to necessitate far reaching changes to the NWM Group's operating model and existing exposures, and potentially on timescales outside of risk appetite. Whilst the risks presented by climate change are unprecedented, how the NWM Group implements the RBS Group's strategy to respond to climate change may also have a material adverse effect on the NWM Group's

business and funding, and its future profitability over the short, medium and long term. Once established, there is no certainty that the NWM Group will be able to meet its climate change targets and ambitions or that seeking to do so will not have an adverse impact on the NWM Group, including its competitive position. See also 'The NWM Group expects to face significant risks in connection with climate change and the transition to a low carbon economy'.

Financial resilience risk

The NWM Group may not meet the targets it communicates to the market, generate returns or implement its strategy effectively.

As part of the RBS Group's Purpose-led Strategy and the NWM Refocusing, the NWM Group has stated a number of internal and external financial, capital and operational targets including in respect of: balance sheet and cost reductions, CET1 ratio targets (for NWM Plc and NWM N.V.), leverage ratio targets (for NWM Plc and NWM N.V.), targets in relation to local regulation, funding plans and requirements, management of RWAs and the timing thereof, employee engagement, diversity and inclusion as well as environmental, social and customer satisfaction targets.

The NWM Group's ability to meet its targets and to successfully implement its strategy is subject to various internal and external factors and risks. These include, but are not limited to, client and staff behaviour and actions, market, regulatory, economic and political factors, developments relating to litigation, governmental actions, investigations and regulatory matters, and operational risks and risks relating to the NWM Group's business model and strategy (including risks associated with environmental, social and governance issues) and the NWM Refocusing. See also 'The NWM Group may not be able to successfully implement the NWM Refocusing and it may not achieve its targets and the NWM Group may not ultimately result in a viable, competitive, CIB-customer focused banking business'.

A number of factors may impact NWM Plc and NWM N.V.'s ability to maintain their current CET1 ratio targets, including impairments, the extent of organic capital generation or the reduction of RWAs. In addition, the exit of capital optimisation positions in NWM Plc will give rise to disposal losses which may be partially recognised prior to the disposal, and which may be higher than anticipated.

The NWM Group's ability to meet its planned reductions in annual costs may vary considerably from year to year. Furthermore, the focus on meeting balance sheet and cost reduction targets may result in limited investment in other areas which could affect the NWM Group's long-term product offering or competitive position and its ability to meet its other targets, including those related to customer satisfaction.

Risk Factors

In addition, challenging trading conditions may have an adverse impact on the NWM Group's business (in particular, the income from its Rates business) and may adversely affect its ability to achieve its targets and execute its strategy. There is no certainty that the NWM Group's strategy will be successfully executed, that it will meet its targets and expectations, or that it will be a viable, competitive or profitable banking business.

The NWM Group has recently undergone significant structural change, as a result of the implementation of the UK ring-fencing regime, and the acquisition of NatWest Markets N.V.

Prior to the implementation of the UK ring-fencing regime, NWM Plc was the RBS Group's principal operating subsidiary. As a result of the implementation of the UK ring-fencing regime and the acquisition of NWM N.V., NWM Plc is now the principal operating company for most of the RBS Group's operations outside the ring-fence (excluding RBS International). As a result, the NWM Group can no longer accept deposits from certain retail and small business customers located in the EEA (and post-Brexit, in the EEA and the UK) and the remaining operations of the NWM Group comprise the businesses serving financial institutions and UK and European corporate customers, providing them with risk management, trading solutions and debt financing. These business operations are subject to further potential changes as a result of the UK's departure from the European Union.

The implementation of the UK ring-fencing regime has had a significant impact on NWM Plc with a reduction in its operational footprint, changes in Board composition, balance sheet composition, its cost-to-income and CET1 ratios, risk profile, its funding strategy, capital requirements and credit ratings. Accordingly, NWM Plc has been required to adapt its strategy, structure and business model and has adopted processes and structures for, among other things, financial reporting, risk management and corporate governance. It has also implemented a shared services model with the ring-fenced entities for certain other services, the execution of which is subject to various internal and external factors and risks, including the implementation of the NWM Refocusing. See also, 'The RBS Group has announced a new strategy that will require changes in the NWM Group's business, including reductions in capital allocated to the NWM Group, its cost base and complexity. This entails material execution, commercial and operational risks for the NWM Group' and 'The NWM Group may not be able to successfully implement the NWM Refocusing and it may not achieve its targets and the NWM Group may not ultimately result in a viable, competitive business'. Moreover, the NWM Group has entered into Revenue Share Agreements with some entities within the RBS Group's ring-fenced sub-group (including NatWest Bank Plc, The Royal Bank of Scotland Plc and Ulster Bank Ireland DAC) as well as a non-ring-fenced entity (RBS International). It has

also entered into certain transfer pricing arrangements, a funded guarantee and revenue sharing agreements with NWM N.V. in relation to certain EEA customer transfers and Western European transfers.

Following the NWM Plc acquisition of RBS Holdings N.V. and its wholly-owned subsidiary, NatWest Markets N.V., these entities are now part of NWM Group, introducing additional risks, including in respect of: foreign exchange exposure, counterparty and borrower risk, Brexit risk (due to potential changes in regulatory approach following Brexit), operational and business risk.

There can be no certainty that the NWM Group will be a viable, competitive or profitable banking business. See also, 'The NWM Group may not be able to successfully implement the NWM Refocusing and it may not achieve its targets and the NWM Group may not ultimately result in a viable, competitive business'.

The NWM Group is reliant on access to the global capital markets to meet its funding requirements, both directly, and indirectly through its parent for the subscription to its internal MREL.

The NWM Group's funding plan currently anticipates that in 2020 the NWM Group will issue £3-5 billion in senior unsecured funding in order to meet its near-term debt re-financing and funding requirements, based on its current and anticipated business activities. The NWM Group is therefore reliant on frequent access to the global capital markets for funding, and on terms that are acceptable to it. Such access entails execution risk and could be impeded by a number of internal or external factors, including, those referred to below in 'The NWM Group faces market risk as a result of increased political and economic risks and uncertainty in the UK and global markets', 'Prevailing uncertainty regarding the terms of the UK's withdrawal from the European Union has adversely affected and will continue to affect the NWM Group' and 'Any reduction in the credit rating assigned to RBSG plc, any of its subsidiaries (including NWM Plc or NWM Group subsidiaries) or any of their respective debt securities could adversely affect the availability of funding for the NWM Group, reduce the NWM Group's liquidity position and increase the cost of funding'.

In addition, NWM Plc receives capital and funding from the RBS Group. NWM Plc has set target levels for different tiers of capital and for the internal minimum requirements for own funds and eligible liabilities ('MREL'), as percentages of its RWAs. The level of capital and funding required for NWM Plc to meet its internal targets is therefore a function of the level of RWAs and its leverage exposure in NWM Plc and this may vary over time.

NWM Plc's internal MREL comprises the regulatory value of capital instruments and loss-absorbing senior funding issued by NWM Plc to its parent, RBSG plc, in all cases with a

residual maturity of at least one year. The Bank of England has identified that the preferred resolution strategy for RBS Group is as a single point of entry. As a result, only RBSG plc is able to issue Group MREL eligible liabilities to third-party investors, using the proceeds to fund the internal capital and MREL targets and/or requirements of its operating entities, including NWM Plc. NWM Plc is therefore dependent on RBSG plc to fund its internal capital targets and its ability to source appropriate funding at an RBSG plc level to support this. NWM Plc is also dependent on RBSG plc to continue to fund NWM Plc's internal MREL target over time and its ability to issue and maintain sufficient amounts of external MREL liabilities to support this. In turn, NWM Plc is required to fund the internal capital and MREL requirements of its subsidiaries.

Any inability of the NWM Group to adequately access the capital markets, to manage its balance sheet in line with assumptions in its funding plans, or to issue internal capital and MREL, may adversely affect the NWM Group, such that the NWM Group may not constitute a viable banking business and/or NWM Plc or NWM N.V. may fail to meet their respective regulatory capital and/or MREL requirements (at present, NWM N.V. does not yet have its own MREL requirements).

NWM Plc and/or its regulated subsidiaries may not meet the prudential regulatory requirements for capital and MREL.

The NWM Group is required by regulators in the UK, the EU and other jurisdictions in which it undertakes regulated activities to maintain adequate financial resources. Adequate capital also gives the NWM Group financial flexibility in the face of turbulence and uncertainty in the global economy and specifically in its core UK and European markets.

NWM Plc's 2020 target CET1 ratio is above 15% (on a solo (i.e. unconsolidated) basis). This target CET1 ratio is based on regulatory requirements, internal modelling and risk appetite (including under stress). NWM N.V.'s 2020 target CET1 ratio is above 15% on a consolidated basis. This target CET1 ratio is based on expected regulatory requirements, internal modelling and risk appetite (including under stress), taking into account the anticipated extent of transfers of EEA clients from NWM Plc and NWB Plc to NWM N.V. due to Brexit.

As at 31 December 2019, NWM Plc's CET1 ratio was 17.3%. NWM Plc's current capital strategy is based on the management of RWAs and other capital management initiatives (including the reduction of RWAs and the periodic payment of dividends to RBSG plc, NWM Plc's parent company).

Other factors that could influence the NWM Plc and NWM N.V.'s CET1 ratios include, amongst other things (see also, 'The RBS Group has announced a new strategy that will require changes in the NWM Group's business, including reductions in capital

Risk Factors

allocated to the NWM Group, its cost base and complexity. This entails material execution, commercial and operational risks for the NWM Group):

- a depletion of NWM Plc or NWM N.V.'s capital resources through losses (which would in turn impact retained earnings) and may result from revenue attrition or increased liabilities, sustained periods of low or lower interest rates, reduced asset values resulting in write-downs or reserve adjustments, impairments, changes in accounting policy, accounting charges or foreign exchange movements;
- a change in the quantum of NWM Plc's or NWM N.V.'s RWAs, stemming from exceeding target RWA levels, the implementation of the NWM Refocusing, regulatory adjustments (for example, from additional market risk backtesting exceptions) or foreign exchange movements. An increase in RWAs would lead to a reduction in the CET1 ratio (and increase in the amount of internal MREL required for NWM Plc);
- changes in prudential regulatory requirements including the Total Capital Requirement for NWM Plc (as regulated by the PRA) or NWM N.V. (as regulated by the De Nederlandsche Bank ('DNB')), including Pillar 2 requirements and regulatory buffers (including the increased 2% countercyclical capital buffer for UK banks with effect from 16 December 2020), as well as any applicable scalars;
- further developments of prudential regulation (for example, the CCR2 and finalisation of Basel 3 standards), which will impact various areas including the approach to calculating credit risk, market risk, leverage ratio, capital floors and operational risk RWAs, as well as continued regulatory uncertainty on the details thereto;
- further losses (including as a result of extreme one-off incidents such as cyberattack, fraud or conduct issues) would deplete capital resources and place downward pressure on the CET1 ratio;
- the timing of planned liquidation, disposal and/or capital releases of capital optimisation activity or legacy entities owned by NWM Plc and NWM N.V.; or
- the risk in relation to an adverse market movement impacting the value of our SAR denominated shareholding in Saudi British Bank (SABB). NWM Plc acquired a 4.1% equity non-significant investment in SABB from NWM N.V. in June 2019 on completion of the merger of Alawal bank with SABB.

NWM Plc has a Capital Support Deed, which facilitates capital support amongst the participating entities in the NWM Group.

Any capital management actions taken under a stress scenario may affect, among other things, the NWM Group's product offering, credit ratings, ability to operate its businesses and pursue its current strategies and strategic opportunities as well as negatively impacting

investor confidence and the value of the NWM Group's securities. See also, 'NWM Plc and/or its regulated subsidiaries may not manage their capital, liquidity or funding effectively which could trigger the execution of certain management actions or recovery options.' and 'The RBS Group (including the NWM Group entities) may become subject to the application of UK statutory stabilisation or resolution powers which may result in, among other actions, the write-down or conversion of the NWM Group entities' Eligible Liabilities'.

NWM Plc may not be able to adequately access sources of liquidity and funding.

The NWM Group is required to access sources of liquidity and funding through deposits and wholesale funding, including debt capital markets and trading liabilities such as repurchase agreements. As at 31 December 2019, the NWM Group held £5.8 billion in deposits from banks and customers. The level of deposits and wholesale funding may fluctuate due to factors outside the NWM Group's control. These include loss of confidence (including in individual NWM Group entities or the UK banking sector or the banking sector as a whole) and increasing competitive pressures for bank funding or the reduction or cessation of deposits and other funding by foreign counterparties, which could result in a significant outflow of deposits or reduction in wholesale funding within a short period of time. See also, 'The NWM Group has significant exposure to counterparty and borrower risk'. An inability to grow, roll-over, or any material decrease in, the NWM Group's deposits, short-term wholesale funding and short-term liability financing could, particularly if accompanied by one of the other factors described above, materially affect the NWM Group's ability to satisfy its liquidity needs.

The NWM Group engages from time to time in "fee based borrow" transactions whereby collateral (such as government bonds) is borrowed from counterparties on an unsecured basis in return for a fee. This borrowed collateral may be used by the NWM Group to finance parts of its balance sheet, either in its repo financing business, derivatives portfolio or more generally across its balance sheet. If such "fee based borrow" transactions are unsecured whilst used to support the financing of parts of the NWM Group balance sheet, then unsecured funding from other sources would be required to replace such financing. There is a risk that the NWM Group is unable to replace such financing on acceptable terms or at all, which could adversely affect its liquidity position and have a material adverse effect on the NWM Group's financial condition and results of operations. In addition, because the "fee base borrow" transactions are conducted off-balance sheet (due to the collateral being borrowed) investors may find it more difficult to gauge the NWM Group's creditworthiness, which may be affected if these transactions were to be unwound in a stress scenario, and any lack of or perceived lack of creditworthiness may adversely affect the NWM Group.

As at 31 December 2019, the NWM Group reported a liquidity coverage ratio of 254%. If its liquidity position were to come under stress and if the NWM Group is unable to raise funds through deposits or wholesale funding sources on acceptable terms or at all, its liquidity position could be adversely affected and it might be unable to meet deposit withdrawals on demand, buy back requests, to repay borrowings as they mature, to meet its obligations under committed financing facilities, to comply with regulatory funding requirements, to undertake certain capital and/or debt management activities, or to fund new loans, investments and businesses. The NWM Group may need to liquidate unencumbered assets to meet its liabilities, including disposals of assets not previously identified for disposal to reduce its funding commitments. This could also lead to higher funding costs. In a time of reduced liquidity, or market stress, the NWM Group may be unable to sell some of its assets, or may need to sell assets at depressed prices, which in either case could negatively affect the NWM Group's results.

The NWM Group independently manages liquidity risk on a stand-alone basis, including through holding its own liquidity portfolio. It has restricted access to liquidity or funding from other RBS Group entities. As a result, NWM Plc's liquidity position could be adversely affected, which may require unencumbered assets to be liquidated or may result in higher funding costs which may adversely impact the NWM Group's margins and profitability. NWM Plc's management of its own liquidity portfolio and the new structure of capital support are subject to operational and execution risk, as NWM Plc is now required to meet its own liquidity and capital requirements.

NWM Plc and/or its regulated subsidiaries may not manage their capital, liquidity or funding effectively which could trigger the execution of certain management actions or recovery options.

Under the EU Bank Recovery and Resolution Directive ('BRRD'), as implemented in the UK, the NWM Group must maintain a recovery plan acceptable to its regulator, such that a breach of NWM Plc's applicable capital or leverage or liquidity requirements would trigger consideration of NWM Plc's recovery plan, and in turn may prompt consideration of the RBS Group's recovery plan. If, under stressed conditions, the capital or leverage ratio were to decline, there are a range of recovery management actions (focused on risk reduction and mitigation) that NWM Plc could undertake that may or may not be sufficient to restore adequate capital and leverage ratios. Additional management options relating to existing capital issuances, asset or business disposals, capital payments and dividends from NWM Plc to its parent, could also be undertaken to support NWM Plc's capital and leverage requirements. The RBS Group may also address a shortage of capital in NWM Plc by providing parental support to NWM Plc, subject to evidence that

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the conditions set out in Article 23 of the BRRD have been met. The RBS Group's (and NWM Plc's) regulator may also request that the NWM Group carry out additional capital management actions. The Bank of England has identified single point-of-entry as the preferred resolution strategy for RBS Group. However, under certain conditions set forth in the BRRD, as the UK resolution authority, the Bank of England also has the power to execute the 'bail-in' of certain securities of the NWM Group without further action at the RBS Group level.

Any capital management actions taken under a stress scenario may affect, among other things, the NWM Group's product offering, credit ratings, ability to operate its businesses and pursue its current strategies and strategic opportunities as well as negatively impacting investor confidence and the value of the NWM Group's securities. See also, 'The RBS Group (including the NWM Group) may become subject to the application of UK statutory stabilisation or resolution powers which may result in, among other actions, the write-down or conversion of the NWM Group entities' Eligible Liabilities'. In addition, if NWM Plc or NWM N.V.'s liquidity position were to be adversely affected, this may require unencumbered assets to be liquidated or may result in higher funding costs which may adversely impact the NWM Group's operating performance.

Any reduction in the credit rating assigned to RBSG plc, any of its subsidiaries (including NWM Plc or NWM Group subsidiaries) or any of their respective debt securities could adversely affect the availability of funding for the NWM Group, reduce the NWM Group's liquidity position and increase the cost of funding.

Rating agencies regularly review RBSG plc, NWM Plc and other RBS Group entity credit ratings, which could be negatively affected by a number of factors that can change over time including, the credit rating agency's assessment of the NWM Group's strategy and management's capability; its financial condition including in respect of profitability, asset quality, capital, funding and liquidity; the level of political support for the industries in which the NWM Group operates; the implementation of structural reform; the legal and regulatory frameworks applicable to the NWM Group's legal structure; business activities and the rights of its creditors; changes in rating methodologies; changes in the relative size of the loss-absorbing buffers protecting bondholders and depositors; the competitive environment, political and economic conditions in the NWM Group's key markets (including the impact of Brexit and any further Scottish independence referendum); any reduction of the UK's sovereign credit rating and market uncertainty. See also, 'The RBS Group has announced a new strategy that will require changes in the NWM Group's business, including reductions in capital allocated to the NWM Group, its cost base and complexity. This entails material execution, commercial and operational risks for the NWM Group'.

In addition, credit ratings agencies are increasingly taking into account environmental, social and governance ("ESG") factors, including climate risk, as part of the credit ratings analysis, as are investors in their investment decisions.

Any reductions in the credit ratings of RBSG plc, NWM Plc or of certain other RBS Group entities, including, in particular, downgrades below investment grade, or a deterioration in the capital markets' perception of NWM Group's financial resilience could significantly affect the NWM Group's access to money markets, reduce the size of its deposit base and trigger additional collateral or other requirements in derivatives contracts and other secured funding arrangements or the need to amend such arrangements, which could adversely affect the NWM Group's (and, in particular, NWM Plc's) cost of funding and its access to capital markets and could limit the range of counterparties willing to enter into transactions with the NWM Group (and, in particular, NWM Plc). This could in turn adversely impact its competitive position and threaten the prospects of the NWM Group in the short to medium-term.

The NWM Group operates in markets that are highly competitive, with increasing competitive pressures and technology disruption.

The markets in which the NWM Group operates are highly competitive, and competition may intensify in response to evolving customer behaviour, technological changes, competitor behaviour, new entrants to the market, industry trends resulting in increased disaggregation or unbundling of financial services, the impact of regulatory actions and other factors. Innovations such as biometrics, artificial intelligence, the cloud, blockchain, and quantum computing may also rapidly facilitate industry transformation.

Increasingly many of the products and services offered by the NWM Group are, and will become, technology intensive and the NWM Group's ability to develop such services and comply with related regulatory changes has become increasingly important to retaining and growing the NWM Group's client businesses across its geographical footprint. There can be no certainty that the NWM Group's innovation strategy (which includes investment in its IT capability intended to improve its core infrastructure and client interface capabilities as well as investments and partnerships with third party technology providers) will be successful or that it will allow the NWM Group to continue to grow such services in the future.

In addition, certain of the NWM Group's current or future competitors may be more successful in implementing innovative technologies for delivering products or services to their clients. Furthermore, these competitors may be better able to attract and retain clients and key employees and may have access to lower cost funding and/or be able to attract deposits or provide investment

banking services on more favourable terms than the NWM Group. Although the NWM Group invests in new technologies and participates in industry and research-led initiatives aimed at developing new technologies, such investments may be insufficient or ineffective, especially given the NWM Group's focus on its cost savings targets. This may limit additional investment in areas such as financial innovation and therefore could affect the NWM Group's offering of innovative products or technologies for delivering products or services to clients and its competitive position. The NWM Group may also fail to identify future opportunities or derive benefits from disruptive technologies in the context of rapid technological innovation, changing customer behaviour and growing regulatory demands. The development of innovative products depends on the NWM Group's ability to produce underlying high quality data, failing which its ability to offer innovative products may be compromised.

If the NWM Group is unable to offer competitive, attractive and innovative products that are also profitable, it will lose market share, incur losses on some or all of its activities and lose opportunities for growth. In this context, the NWM Group is investing in the automation of certain solutions and interactions within its customer-facing businesses, including through artificial intelligence. Such initiatives may result in operational, reputational and conduct risks if the technology used is defective, or is not fully integrated into the NWM Group's current solutions or does not deliver expected cost savings. The investment in automated processes will likely also result in increased short-term costs for the NWM Group.

In addition, recent and future disposals and restructurings by the NWM Group, the implementation of the NWM Refocusing and the RBS Group's Purpose-led Strategy (including its climate ambition), cost-reduction measures, as well as employee remuneration constraints, may also have an impact on its ability to compete effectively and intensified competition from incumbents, challengers and new entrants in the NWM Group's core markets could affect the NWM Group's ability to provide satisfactory returns. See also, 'The NWM Group may not be able to successfully implement the NWM Refocusing and it may not achieve its targets and the NWM Group may not ultimately result in a viable, competitive business'. Moreover, activist investors have increasingly become engaged and interventionist in recent years, which may pose a threat to the RBS Group's strategic initiatives. Furthermore, continued consolidation in certain sectors of the financial services industry could result in the NWM Group's remaining competitors gaining greater capital and other resources, including the ability to offer a broader range of products and services and geographic diversity, or the emergence of new competitors.

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The NWM Group may be adversely affected if the RBS Group fails to meet the requirements of regulatory stress tests.

The RBS Group is subject to annual stress tests by its regulator in the UK and is also subject to stress tests by European regulators with respect to RBSG plc, NWM N.V. and Ulster Bank Ireland DAC. Stress tests are designed to assess the resilience of banks to potential adverse economic or financial developments and ensure that they have robust, forward-looking capital planning processes that account for the risks associated with their business profile. If the stress tests reveal that a bank's existing regulatory capital buffers are not sufficient to absorb the impact of the stress, then it is possible that RBS Group and/or NWM Group may need to take action to strengthen their capital positions.

Failure by the RBS Group to meet its quantitative and qualitative requirements of the stress tests set forth by its UK regulators or those elsewhere may result in: the RBS Group's regulators requiring the RBS Group to generate additional capital, reputational damage, increased supervision and/or regulatory sanctions and/or loss of investor confidence.

The NWM Group has significant exposure to counterparty and borrower risk.

NWM N.V., which NWM plc acquired in late 2019, has a portfolio of loans and loan commitments to Western European corporate customers. Through the NWM N.V. business and the NWM Group's other activities, the NWM Group has exposure to many different industries, customers and counterparties, and risks arising from actual or perceived changes in credit quality and the recoverability of monies due from borrowers and other counterparties are inherent in a wide range of the NWM Group's businesses. These are particularly relevant for those businesses for which the concentration of client income is heavily weighted towards a specific geographic region, industry or client base. The NWM Group is exposed to credit risk if a customer, borrower or counterparty defaults, or under IFRS 9, suffers a sufficiently significant deterioration of credit quality such that, under SICR ('significant increases in credit risk') rules, it moves to Stage 2 for impairment calculation purposes. Credit risk may arise from a variety of business activities, including, but not limited to: extending credit to clients through various lending commitments; entering into swap or other derivative contracts under which counterparties have obligations to make payments to the NWM Group (including un-collateralised derivatives); providing short or long-term funding that is secured by physical or financial collateral whose value may at times be insufficient to fully cover the loan repayment amount; posting margin and/or collateral and other commitments to clearing houses, clearing agencies, exchanges, banks, securities firms and other financial counterparties; and investing and trading in

securities and loan pools, whereby the value of these assets may fluctuate based on realised or expected defaults on the underlying obligations or loans. See also, 'Capital and risk management — Credit Risk'. Any negative developments in the activities listed above may negatively impact the NWM Group's clients and credit exposures, which may, in turn, adversely impact the NWM Group's profitability.

The credit quality of the NWM Group's borrowers and other counterparties is impacted by prevailing economic and market conditions and by the legal and regulatory landscape in the UK and Europe in general, and any deterioration in such conditions or changes to legal or regulatory landscapes could worsen borrower and counterparty credit quality and consequently adversely impact the NWM Group's ability to enforce contractual security rights. See also, 'The NWM Group faces market risk as a result of increased political and economic risks and uncertainty in the UK and global markets'.

Concerns about, or a default by, a financial institution could lead to significant liquidity problems and losses or defaults by other financial institutions, since the commercial and financial soundness of many financial institutions is closely related and inter-dependent as a result of credit, trading, clearing and other relationships. Any perceived lack of creditworthiness of a counterparty may lead to market-wide liquidity problems and losses for the NWM Group. In addition, the value of collateral may be correlated with the probability of default by the relevant counterparty ('wrong way risk'), which would increase NWM Group's potential loss. This systemic risk may also adversely affect financial intermediaries, such as clearing agencies, clearing houses, banks, securities firms and exchanges with which the NWM Group interacts on a daily basis. See also, 'The NWM Group is reliant on access to the global capital markets to meet its funding requirements, both directly, and indirectly through its parent for the subscription to its internal MREL'.

As a result of the above, borrower and counterparty credit quality may cause accelerated impairment charges under IFRS 9, increased repurchase demands, higher costs, additional write-downs and losses for the NWM Group and an inability to engage in routine funding transactions.

The NWM Group is exposed to the financial industry, including sovereign debt securities, banks, financial intermediation providers (including providing facilities to financial sponsors and funds, backed by assets or investor commitments) and securitised products (typically senior lending to special purpose vehicles backed by pools of financial assets). Due to the NWM Group's exposure to the financial industry, it also has exposure to shadow banking entities (ie, entities which carry out banking activities outside a regulated framework). Recently, there has

been increasing regulatory focus on shadow banking. In particular, the European Banking Authority Guidelines (EBA/GL/2015/20) require NWM Group to identify and monitor its exposure to shadow banking entities, implement and maintain an internal framework for the identification, management, control and mitigation of the risks associated with exposure to shadow banking entities, and ensure effective reporting and governance in respect such exposure. If the NWM Group is unable to properly identify and monitor its shadow banking exposure, maintain an adequate framework, or ensure effective reporting and governance in respect of shadow banking exposure, this may adversely affect the financial condition and prospects of the NWM Group.

The NWM Group could incur losses or be required to maintain higher levels of capital as a result of limitations or failure of various models.

Given the complexity of the NWM Group's business, strategy and capital requirements, the NWM Group relies on analytical models for a wide range of purposes, including to manage its business, assess the value of its assets and its risk exposure, as well as to anticipate capital and funding requirements (including to facilitate the RBS Group's mandated stress testing). In addition, the NWM Group utilises models for valuations, credit approvals, calculation of loan impairment charges on an IFRS 9 basis, financial reporting and for financial crime and fraud risk management. The NWM Group's models, and the parameters and assumptions on which they are based, are periodically reviewed and updated to maximise their accuracy.

Such models are inherently designed to be predictive in nature. Failure of these models, including due to errors in model design or inputs, to accurately reflect changes in the micro and macroeconomic environment in which the NWM Group operates, to capture risks and exposures at the subsidiary level, to be updated in line with the NWM Group's current business model or operations, or findings of deficiencies by the RBS Group (and in particular, the NWM Group's) regulators (including as part of the RBS Group's mandated stress testing) may result in increased capital requirements or require management action. The NWM Group may also face adverse consequences as a result of actions based on models that are poorly developed, implemented or used, models that are based on inaccurate or compromised data or as a result of the modelled outcome being misunderstood, or by such information being used for purposes for which it was not designed.

The NWM Group's financial statements are sensitive to underlying accounting policies, judgments, estimates and assumptions.

The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, income,

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expenses, exposures and RWAs. Due to the inherent uncertainty in making estimates (particularly those involving the use of complex models), future results may differ from those estimates. Estimates, judgments, assumptions and models take into account historical experience and other factors, including market practice and expectations of future events that are believed to be reasonable under the circumstances.

The accounting policies deemed critical to the NWM Group's results and financial position, based upon materiality and significant judgments and estimates, which include loan impairment provisions, are set out in 'Critical accounting policies and key sources of estimation uncertainty' on page 87. New accounting standards and interpretations that have been issued by the International Accounting Standards Board but which have not yet been adopted by the NWM Group are discussed in 'Accounting developments' on page 87.

Changes in accounting standards may materially impact NWM Group's financial results.

Changes in accounting standards or guidance by accounting bodies or in the timing of their implementation, whether immediate or foreseeable, could result in the NWM Group having to recognise additional liabilities on its balance sheet, or in further write-downs or impairments to its assets and could also significantly impact the financial results, condition and prospects of the NWM Group.

The NWM Group's trading assets amounted to £76.5 billion as at 31 December 2019. The valuation of financial instruments, including derivatives, measured at fair value can be subjective, in particular where models are used which include unobservable inputs. Generally, to establish the fair value of these instruments, the NWM Group relies on quoted market prices or, where the market for a financial instrument is not sufficiently credible, internal valuation models that utilise observable market data. In certain circumstances, the data for individual financial instruments or classes of financial instruments utilised by such valuation models may not be available or may become unavailable due to prevailing market conditions. In such circumstances, the NWM Group's internal valuation models require the NWM Group to make assumptions, judgments and estimates to establish fair value, which are complex and often relate to matters that are inherently uncertain. Any of these factors could require the NWM Group to recognise fair value losses, which may have an adverse effect on the NWM Group's income generation and financial position.

With effect from 1 January 2019, the NWM Group adopted IFRS 16 Leases, as disclosed in the Accounting Policies. This increased Other assets by £56 million and Other liabilities by £62 million. While adoption of this standard has had no effect on the NWM Group's cash flows, it has impacted financial ratios, which may influence investors'

perception of the financial condition of the NWM Group.

The RBS Group (including the NWM Group) may become subject to the application of UK statutory stabilisation or resolution powers which may result in, among other actions, the write-down or conversion of the NWM Group entities' Eligible Liabilities.

The Banking Act 2009, as amended ('Banking Act'), implemented the BRRD in the UK and created a special resolution regime ('SRR'). Under the SRR, HM Treasury, the Bank of England and the PRA and FCA (together 'Authorities') are granted substantial powers to resolve and stabilise UK-incorporated financial institutions. Five stabilisation options exist under the current SRR: (i) transfer of all of the business of a relevant entity or the shares of the relevant entity to a private sector purchaser; (ii) transfer of all or part of the business of the relevant entity to a 'bridge bank' wholly-owned by the Bank of England; (iii) transfer of part of the assets, rights or liabilities of the relevant entity to one or more asset management vehicles for management of the transferor's assets, rights or liabilities; (iv) the write-down, conversion, transfer, modification, or suspension of the relevant entity's equity, capital instruments and liabilities ('Eligible Liabilities'); and (v) temporary public ownership of the relevant entity. These tools may be applied to RBSG plc as the parent company or to the NWM Group, as an affiliate, where certain conditions are met (such as, whether the firm is failing or likely to fail, or whether it is reasonably likely that action will be taken (outside of resolution) that will result in the firm no longer failing or being likely to fail). Moreover, the SRR provides for modified insolvency and administration procedures for relevant entities, and confers ancillary powers on the Authorities, including the power to modify or override certain contractual arrangements in certain circumstances. The Authorities are also empowered by order to amend the law for the purpose of enabling the powers under the SRR to be used effectively. Such orders may promulgate provisions with retrospective applicability. Similar powers may also be exercised with respect to NWM N.V. in the Netherlands by the relevant Dutch regulatory authorities.

Under the Banking Act, the Authorities are generally required to have regard to specified objectives in exercising the powers provided for by the Banking Act. One of the objectives (which is required to be balanced as appropriate with the other specified objectives) refers to the protection and enhancement of the stability of the financial system of the UK. Moreover, the 'no creditor worse off' safeguard contained in the Banking Act (which provides that creditors' losses in resolution should not exceed those that would have been realised in an insolvency of the relevant institution) may not apply in relation to an application of the separate write-down and conversion power relating to capital instruments under the Banking Act, in circumstances where a stabilisation power is

not also used; holders of debt instruments which are subject to the power may, however, have ordinary shares transferred to or issued to them by way of compensation.

Uncertainty exists as to how the Authorities may exercise the powers granted to them under the Banking Act including the determination of actions undertaken in relation to the ordinary shares and other securities issued by RBS Group (including the NWM Group) and may depend on factors outside of the NWM Group's control. Moreover, the relevant provisions of the Banking Act remain untested in practice.

If the NWM Group (or any other RBS Group entity) is at or is approaching the point of non-viability such that regulatory intervention is required, any exercise of the resolution regime powers by the Authorities may adversely affect holders of the NWM Group's Eligible Liabilities that fall within the scope of resolution regime powers. This may result in various actions being undertaken in relation to the NWM Group and any Eligible Liabilities of the NWM Group, including write-down, conversion, transfer or modification which may adversely affect the financial results, condition and prospects of the NWM Group.

The RBS Group is subject to Bank of England oversight in respect of resolution, and the RBS Group could be adversely affected should the Bank of England deem the RBS Group's preparations to be inadequate.

The RBS Group is subject to regulatory oversight by the Bank of England, and is required (under the PRA rulebook) to carry out an assessment of its preparations for resolution, submit a report of the assessment to the PRA, and disclose a summary of this report. The initial report is due to be submitted to the PRA on 2 October 2020 and the Bank of England's assessment of RBS Group's preparations is scheduled to be released on 11 June 2021.

The RBS Group has dedicated significant resources towards the preparation of the RBS Group for a potential resolution scenario. However, if the assessment reveals that the RBS Group is not adequately prepared to be resolved, or does not have adequate plans in place to meet resolvability requirements by 1 January 2022, the RBS Group may be required to take action to enhance its preparations to be resolvable, resulting in additional cost and the dedication of additional resources. Such actions may adversely affect the RBS Group and/or the NWM Group, resulting in restrictions on maximum individual and aggregate exposures, a requirement to dispose of specified assets, a requirement to cease carrying out certain activities and/or maintaining a specified amount of MREL. This may also result in reputational damage and/or loss of investor confidence.

Operational and IT resilience risk

Risk Factors

The NWM Group is subject to increasingly sophisticated and frequent cyberattacks.

The NWM Group is experiencing an increase in cyberattacks across both the entire NWM Group and against the NWM Group's supply chain, reinforcing the importance of due diligence and close working with the third parties on which the NWM Group relies. The NWM Group is reliant on technology, against which there is a constantly evolving series of attacks, that are increasing in terms of frequency, sophistication, impact and severity. As cyberattacks evolve and become more sophisticated, the NWM Group is required to continue to invest in additional capability designed to defend against emerging threats. In 2019, the NWM Group was subjected to a small number of Distributed Denial of Service ('DDoS') attacks, which are a pervasive and significant threat to the global financial services industry. The focus is to mitigate the impact of the attacks and sustain availability of services for NWM Group's customers. The NWM Group continues to invest significant resources in the development and evolution of cyber security controls that are designed to minimise the potential effect of such attacks.

Hostile attempts are made by third parties to gain access to and introduce malware (including ransomware) into the NWM Group's IT systems, and to exploit vulnerabilities. The NWM Group has information and cyber security controls in place, which are subject to review on a continuing basis, but given the nature of the threat, there can be no assurance that such measures will prevent all attacks in the future. See also, 'The NWM Group's operations are highly dependent on its complex IT systems, and any IT failure could adversely affect the NWM Group'.

Any failure in the NWM Group's cybersecurity policies, procedures or controls, may result in significant financial losses, major business disruption, inability to deliver customer services, or loss of data or other sensitive information (including as a result of an outage) and may cause associated reputational damage. Any of these factors could increase costs (including costs relating to notification of, or compensation for clients and credit monitoring), result in regulatory investigations or sanctions being imposed or may affect the NWM Group's ability to retain and attract clients. Regulators in the UK, US, Europe and Asia continue to recognise cybersecurity as an increasing systemic risk to the financial sector and have highlighted the need for financial institutions to improve their monitoring and control of, and resilience (particularly of critical services) to cyberattacks, and to provide timely notification of them, as appropriate.

Additionally, third parties may also fraudulently attempt to induce employees, customers, third party providers or other users who have access to the NWM Group's systems to disclose sensitive information in order to gain access to the NWM Group's data or that of the NWM Group's clients or employees. Cybersecurity and information security events can derive from groups or

factors such as: internal or external threat actors, human error, fraud or malice on the part of the NWM Group's employees or third parties, including third party providers, or may result from accidental technological failure.

The NWM Group expects greater regulatory engagement, supervision and enforcement in relation to its overall resilience to withstand IT and related disruption, either through a cyberattack or some other disruptive event. Such increased regulatory engagement, supervision and enforcement is uncertain in relation to the scope, cost, consequence and the pace of change, which could negatively impact the NWM Group. Due to the NWM Group's reliance on technology and the increasing sophistication, frequency and impact of cyberattacks, it is likely that such attacks could have a material adverse impact on the NWM Group.

In accordance with the General Data Protection Regulation ('GDPR'), the NWM Group is required to ensure it implements timely appropriate and effective organisational and technological safeguards against unauthorised or unlawful access to data of the NWM Group, its clients and its employees. In order to meet this requirement, the NWM Group relies on the effectiveness of its internal policies, controls and procedures to protect the confidentiality, integrity and availability of information held on its IT systems, networks and devices as well as with third parties with whom the NWM Group interacts. A failure to monitor and manage data in accordance with the GDPR requirements of the applicable legislation may result in financial losses, regulatory fines and investigations and associated reputational damage. In addition, whilst the NWM Group takes measures to prevent, detect and minimise attacks, the NWM Group's systems, and those of third party providers, are subject to frequent cyberattacks.

The NWM Group operations and strategy are highly dependent on the effective use and accuracy of data.

The NWM Group relies on the effective use of accurate data to support and improve its operations and deliver its strategy. Failure to produce underlying high quality data and/or the ineffective use of such data could result in a failure to satisfy its customers' expectations including by delivering innovative products and services. This could place NWM Group at a competitive disadvantage, inhibit its efforts to reduce costs and improve its systems, controls and processes, and result in a failure to deliver the NWM Group's strategy. The use of unethical or inappropriate data and/or non-compliance with customer data and privacy protection could give rise to conduct and litigation risks and could also increase the risk of an operational event or losses or other adverse consequences due to inappropriate models, systems, processes, decisions or other actions.

Operational risks are inherent in the NWM Group's businesses.

Operational risk is the risk of loss resulting from inadequate or failed internal processes, procedures, people or systems, or from external events, including legal risks. The NWM Group operates in many countries, offering a diverse range of products and services supported by 5,000 employees as at 31 December 2019; it therefore has complex and diverse operations. As a result, operational risks or losses can arise from a number of internal or external factors (including financial crime). These risks are also present when the NWM Group relies on third-party suppliers or vendors to provide services to it or its clients, as is increasingly the case as the NWM Group outsources certain functions, including with respect to the implementation of new technologies, innovation and responding to regulatory and market changes.

Operational risks continue to be heightened as a result of the implementation of the NWM Refocusing and the RBS Group's Purpose-led Strategy, the NWM Group's current cost-reduction measures and conditions affecting the financial services industry generally (including Brexit and other geo-political developments) and in particular the legal and regulatory uncertainty resulting therefrom. This may place significant pressure on the NWM Group's ability to maintain effective internal controls and governance frameworks. The NWM Group is also dependent on the RBS Group for certain shared critical services, including property, financial accounting, regulatory reporting and certain administrative and legal services, the cost for which are determined by RBS Group and which may increase from time to time. A failure to adequately supply these services may result in increased costs or other liabilities to the NWM Group should the NWM Group have to increase its capacity to provide these services internally or by outsourcing to third parties for these services. Because the NWM Group utilises certain services provided by the RBS Group, changes in the cost of these services may adversely impact the NWM Group's results of operations. The effective management of operational risks is critical to meeting customer service expectations and retaining and attracting client business. Although the NWM Group has implemented risk controls and mitigation actions, with resources and planning having been devoted to mitigate operational risk, such measures may not be effective in controlling each of the operational risks faced by the NWM Group. Ineffective management of such risks could adversely affect the NWM Group. See also, 'The RBS Group has announced a new strategy that will require changes in the NWM Group's business, including reductions in capital allocated to the NWM Group, its cost base and complexity. This entails material execution, commercial and operational risks for the NWM Group' and 'The RBS Group has announced a new Purpose-led Strategy which will further influence the NWM Refocusing and the go-forward strategy of the NWM Group'.

Risk Factors

The NWM Group's operations are highly dependent on its complex IT systems, and any IT failure could adversely affect the NWM Group.

The NWM Group's operations are highly dependent on the ability to process a very large number of transactions efficiently and accurately while complying with applicable laws and regulations. The proper functioning of the NWM Group's transactional and payment systems, financial crime and sanctions controls, risk management, credit analysis and reporting, accounting, customer service and other IT systems (some of which are owned and operated by RBSG plc or third parties), is critical to the NWM Group's operations.

Individually or collectively, any critical system failure, material loss of service availability or material breach of data security could cause serious damage to the NWM Group's ability to provide services to its clients, which could result in reputational damage, significant compensation costs or regulatory sanctions (including fines resulting from regulatory investigations) or a breach of applicable regulations. In particular, such issues could cause long-term damage to the NWM Group's reputation and could affect its regulatory approvals, competitive position, business and brands, which could undermine its ability to attract and retain clients. This risk is heightened as the NWM Group outsources certain functions and continues to innovate and offer new digital solutions to its clients as a result of the trend towards online and digital product offerings.

In 2019, the NWM Group continued to make considerable investments to further simplify, upgrade and improve its IT and technology capabilities (including migration of certain services to cloud platforms). As part of the NWM Refocusing, the NWM Group continues to develop and enhance digital services for its customers and seeks to improve its competitive position through enhancing controls and procedures and strengthening the resilience of services including cyber security. Should such investment and rationalisation initiatives fail to achieve the expected results or prove to be insufficient due to cost challenges or otherwise, this could negatively affect the NWM Group's operations, its reputation and ability to retain or grow its client business or adversely impact its competitive position, thereby negatively impacting the NWM Group's financial position. See also, 'The RBS Group has announced a new strategy that will require changes in the NWM Group's business, including reductions in capital allocated to the NWM Group, its cost base and complexity. This entails material execution, commercial and operational risks for the NWM Group'.

The NWM Group relies on attracting, retaining, developing and remunerating senior management and skilled personnel (such as market trading specialists), and is required to maintain good employee relations.

The NWM Group's current and future success depends on its ability to attract, retain, develop and remunerate highly skilled and qualified personnel, including senior management, directors, market trading specialists and key employees, in a highly competitive labour market, in an era of strategic change (including a recent change in executive management) and under internal cost reduction pressures. This entails risk, particularly in light of the implementation of the NWM Refocusing, heightened regulatory oversight of banks and the increasing scrutiny of, and (in some cases) restrictions placed upon, employee compensation arrangements, in particular those of banks in receipt of government support such as the RBS Group, which may have an adverse effect on the NWM Group's ability to hire, retain and engage well-qualified employees. The market for skilled personnel is increasingly competitive, especially for technology-focused roles, thereby raising the cost of hiring, training and retaining skilled personnel. In addition, certain economic, market and regulatory conditions and political developments (including Brexit) may reduce the pool of candidates for key management and non-executive roles, including non-executive directors with the right skills, knowledge and experience, or increase the number of departures of existing employees.

Some of the NWM Group's employees are represented by employee representative bodies, including trade unions. Engagement with its employees and such bodies is important to the NWM Group in maintaining good employee relations. Any breakdown of these relationships could affect the NWM Group's business, reputation and results of operations.

A failure in the NWM Group's risk management framework could adversely affect the NWM Group, including its ability to achieve its strategic objectives.

Risk management is an integral part of all of the NWM Group's activities and includes the definition and monitoring of the NWM Group's risk appetite and reporting on the NWM Group's risk exposure and the potential impact thereof on the NWM Group's financial condition. Financial risk management is highly dependent on the use and effectiveness of internal stress tests and models and ineffective risk management may arise from a wide variety of factors, including lack of transparency or incomplete risk reporting, unidentified conflicts or misaligned incentives, lack of accountability control and governance, lack of consistency in risk monitoring and management or insufficient challenges or assurance processes. Failure to manage risks effectively could adversely impact the NWM Group's reputation or its relationship with its regulators, clients, shareholders or other stakeholders.

The NWM Group's operations are inherently exposed to conduct risks. These include business decisions, actions or reward mechanisms that are not responsive to or aligned with the NWM Group's regulatory obligations, client needs or do not reflect the NWM Group's customer-focused strategy, ineffective product management, unethical or inappropriate use of data, implementation and utilisation of new technologies, outsourcing of customer service and product delivery, the possibility of mis-selling of financial products and mishandling of customer complaints. Some of these risks have materialised in the past and ineffective management and oversight of conduct risks may lead to further remediation and regulatory intervention or enforcement. The NWM Group's businesses are also exposed to risks from employee misconduct including non-compliance with policies and regulations, negligence or fraud (including financial crimes), any of which could result in regulatory fines or sanctions and serious reputational or financial harm to the NWM Group.

As part of the NWM Refocusing, the NWM Group is seeking to embed a strong risk culture across the organisation and has implemented policies and allocated new resources across all levels of the organisation to manage and mitigate conduct risk and expects to continue to invest in its risk management framework. However, such efforts may not insulate the NWM Group from future instances of misconduct and no assurance can be given that the NWM Group's strategy and control framework will be effective. See also, 'The RBS Group has announced a new strategy that will require changes in the NWM Group's business, including reductions in capital allocated to the NWM Group, its cost base and complexity. This entails material execution, commercial and operational risks for the NWM Group'. Any failure in the NWM Group's risk management framework could negatively affect the NWM Group and its financial condition through reputational and financial harm and may result in the inability to achieve its strategic objectives for its clients, employees and wider stakeholders.

The NWM Group's operations are subject to inherent reputational risk.

Reputational risk relates to stakeholder and public perceptions of the NWM Group arising from an actual or perceived failure to meet stakeholder expectations, including with respect to the NWM Refocusing and related targets, due to any events, behaviour, action or inaction by the NWM Group, its employees or those with whom the NWM Group is associated. This includes brand damage, which may be detrimental to the NWM Group's business, including its ability to build or sustain business relationships with clients, and may cause low employee morale, regulatory censure or reduced access to, or an increase in the cost of, funding. Reputational risk may arise whenever there is a material lapse in standards of integrity, compliance, customer or operating efficiency

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and may adversely affect the NWM Group's ability to attract and retain clients. In particular, the NWM Group's ability to attract and retain clients may be adversely affected by, amongst others: negative public opinion resulting from the actual or perceived manner in which the NWM Group or any other member of the RBS Group conducts or modifies its business activities and operations, media coverage (whether accurate or otherwise), employee misconduct, the NWM Group's financial performance, IT systems failures or cyberattacks, data breaches, financial crime, the level of direct and indirect government support for RBSG plc, or the actual or perceived practices in the banking and financial industry in general, or a wide variety of other factors. See also, 'The RBS Group has announced a new strategy that will require changes in the NWM Group's business, including reductions in capital allocated to the NWM Group, its cost base and complexity. This entails material execution, commercial and operational risks for the NWM Group'.

Modern technologies, in particular online social networks and other broadcast tools which facilitate communication with large audiences in short time frames and with minimal costs, may also significantly increase and accelerate the impact of damaging information and allegations.

Although the NWM Group has implemented a Reputational Risk Policy to improve the identification, assessment and management of customers and clients, transactions, products and issues which represent a reputational risk, the NWM Group cannot be certain that it will be successful in avoiding damage to its business from reputational risk.

Economic and political risk

The NWM Group faces market risk as a result of increased political and economic risks and uncertainty in the UK and global markets.

In the UK, significant economic and political uncertainty continues to surround the terms of Brexit and now also the future relationship between the UK and the EU (See also, 'Prevailing uncertainty regarding the terms of the UK's withdrawal from the European Union has adversely affected and will continue to affect the NWM Group.') and may adversely affect the NWM Group.

The RBS Group faces additional political uncertainty as to how the Scottish parliamentary process (including, as a result of any further Scottish independence referendum or the next Scottish Parliament elections in May 2021) may impact the NWM Group. RBSG plc and a number of other RBS Group entities (including NWM Plc) are headquartered and/or incorporated in Scotland. Any changes to Scotland's relationship with the UK or the EU (as an indirect result of Brexit or other developments) would impact the environment in which the RBS Group and its subsidiaries operate, and may require further changes to the RBS Group (including the NWM Group's structure),

independently or in conjunction with other mandatory or strategic structural and organisational changes which could adversely impact the NWM Group.

Actual or perceived difficult global economic conditions can create challenging economic and market conditions and a difficult operating environment for the NWM Group's businesses and its clients and counterparties, thereby affecting its financial performance.

The value of the NWM Group's financial instruments may be materially affected by market risk, including as a result of market fluctuations. Market volatility, illiquid market conditions and disruptions in the credit markets may make it extremely difficult to value certain of the NWM Group's financial instruments, particularly during periods of market displacement which could cause a decline in the value of the NWM Group's financial instruments. This may have an adverse effect on the NWM Group's results of operations in future periods, or inaccurate carrying values for certain financial instruments. Similarly, the NWM Group trades a considerable amount of financial instruments (including derivatives) and volatile market conditions could result in a significant decline in the NWM Group's net trading income or result in a trading loss.

In addition, financial markets are susceptible to severe events evidenced by rapid depreciation in asset values, which may be accompanied by a reduction in asset liquidity. Under these extreme conditions, hedging and other risk management strategies may not be as effective at mitigating trading losses as they would be under more normal market conditions. Moreover, under these conditions, market participants are particularly exposed to trading strategies employed by many market participants simultaneously and on a large scale, increasing the NWM Group's counterparty risk. The NWM Group's risk management and monitoring processes seek to quantify and mitigate the NWM Group's exposure to more extreme market moves. However, severe market events have historically been difficult to predict and the NWM Group could realise significant losses if extreme market events were to occur.

The outlook for the global economy over the medium-term remains uncertain due to a number of factors including: trade barriers and the increased possibility of trade wars, widespread political instability, an extended period of low inflation and low interest rates, and global regional variations in the impact and responses to these factors. Such conditions could be worsened by a number of factors including political uncertainty or macro-economic deterioration in the Eurozone, China or the US, the conflicts or tensions in the Middle East or Asia, increased instability in the global financial system and concerns relating to further financial shocks or contagion (for example, due to economic concerns in emerging markets), 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. This may be compounded by the ageing demographics of the populations in the markets that the NWM 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 NWM Group directly (for example, as a result of credit losses) or indirectly (for example, by impacting global economic growth and financial markets and the NWM Group's clients and their banking needs).

In addition, the NWM Group is exposed to risks arising out of geopolitical events or political developments, such as trade barriers, exchange controls, sanctions and other measures taken by sovereign governments that may hinder economic or financial activity levels. Furthermore, unfavourable political, military or diplomatic events, including secession movements or the exit of other member states from the EU, armed conflict, pandemics and widespread public health crises (including the recent coronavirus outbreak, the impact of which will depend on future developments, which are highly uncertain and cannot be predicted), state and privately sponsored cyber and terrorist acts or threats, and the responses to them by governments and markets, could negatively affect the business and performance of the NWM Group, including as a result of the indirect effect on regional or global trade and/or the NWM Group's customers.

Prevailing uncertainty regarding the terms of the UK's withdrawal from the European Union has adversely affected and will continue to affect the NWM Group.

Following the EU Referendum in June 2016, and pursuant to the exit process triggered under Article 50 of the Treaty on European Union in March 2017 and the ratification of the withdrawal agreement by the UK government and the EU (through the Council of Ministers), the UK ceased to be a member of the EU and the European Economic Area ('EEA') on 31 January 2020 ('Brexit') and entered a transition period, currently due to expire on 31 December 2020. During this transition period, the UK retains the benefits of membership of the EU's internal market and the customs union, but loses its representation in the EU's institutions and its role in EU decision-making.

The UK and EU are currently seeking to determine the terms of their future relationship by the end of the transition period, and the resulting economic, trading and legal relationships with both the EU and other counterparties currently remain unclear and subject to significant uncertainty. If the UK and EU do not agree a new comprehensive trade agreement by the end of the transition period and the transition period is not extended, then, subject to separate agreements being made with third countries, the UK would be expected to operate on basic World Trade Organization terms, the outcome of which for the RBS Group would be similar in certain respects to a 'no-deal' Brexit and which may result in, amongst others, loss of

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access to the EU single market for goods and services, the imposition of import duties and controls on trade between the UK and the EU and related trade disruption.

The direct and indirect effects of the UK's exit from the EU and the EEA are expected to affect many aspects of the NWM Group's business and operating environment, including as described elsewhere in these risk factors, and may be material and/or cause a near-term impact on impairments. See also 'The NWM Group faces market risk as a result of increased political and economic risks and uncertainty in the UK and global markets'. As a result of such anticipated effects, the NWM Group and the RBS Group has engaged in significant and costly Brexit planning and contingency planning and expects to continue to do so. The direct and indirect effects of the UK's exit from the EU and the EEA may also impede the NWM Group's ability to deliver the NWM Refocusing. See also, 'The RBS Group has announced a new strategy that will require changes in the NWM Group's business, including reductions in capital allocated to the NWM Group, its cost base and complexity. This entails material execution, commercial and operational risks for the NWM Group' and 'The NWM Group may not be able to successfully implement the NWM Refocusing and it may not achieve its targets and the NWM Group may not ultimately result in a viable, competitive business'.

The longer term effects of Brexit on the NWM Group's operating environment depend significantly on the terms of the ongoing relationship between the UK and EU. They are difficult to predict, and are subject to wider global macro-economic trends and events, but may significantly impact the NWM Group and its customers and counterparties who are themselves dependent on trading with the EU or personnel from the EU. They may result in, or be exacerbated by, periodic financial volatility and slower economic growth, in the UK in particular, but also in the ROI, the rest of Europe and potentially the global economy.

Significant uncertainty exists as to the respective legal and regulatory arrangements under which the NWM Group and its subsidiaries will operate once the transition period has ended. The legal and political uncertainty and any actions taken as a result of this uncertainty, as well as new or amended rules, could have a significant impact on the NWM Group's non-UK operations and/or legal entity structure, including attendant restructuring costs, level of impairments, capital requirements, regulatory environment and tax implications and as a result may adversely impact the NWM Group's profitability, competitive position, business model and product offering.

The RBS Group has obtained the requisite regulatory permissions (including third country licence branch approvals and access to TARGET2 clearing and settlement mechanisms) it currently considers are required for continuity of business as a result

of the UK's departure from the EU. These are required in order to maintain the ability to clear euro payments and to serve non-UK EEA customers if there is a loss of access to the European Single Market. These changes to the NWM Group's operating model have been costly and may require further changes to its business operations, product offering and customer engagement. The regulatory permissions from the Dutch and German authorities are conditional in nature and will require on-going compliance with certain conditions, including maintaining minimum capital level and deposit balances as well as a defined local physical presence going forward; such conditions may be subject to change in the future. Maintaining these permissions and the RBS Group's access to the euro payment infrastructure will be fundamental to its business going forward and further changes to NWM Group's business operations may be required.

The NWM Group expects to face significant risks in connection with climate change and the transition to a low carbon economy.

The risks associated with climate change are subject to rapidly increasing prudential and regulatory, political and societal focus both in the UK, the Netherlands and internationally. Embedding climate risk into the NWM Group's risk framework, and adapting the NWM Group's operations and business strategy to address the physical risks of climate change and the risk associated with a transition to a low carbon economy in line with the RBS Group's Purpose-led Strategy and ambition to reduce the climate impact of its financing activities and evolving regulatory requirements and market expectations is expected to have a significant impact on the NWM Group.

Multilateral agreements, in particular the 2015 Paris Agreement, and subsequent UK and Scottish Government commitments to achieving net zero carbon emissions by 2050 and 2045, respectively, as well as proposals stemming from the EU Sustainable Finance Action plan, will require widespread levels of adjustment across all sectors of the UK economy and markets in which the NWM Group operates including the European Union. Some sectors such as property, energy, infrastructure (including transport) and agriculture are expected to be particularly impacted. The nature and timing of the far-reaching commercial, technological, policy and regulatory changes that this transition will entail remain uncertain. The UK and Dutch Governments and regulators, including the PRA, NWM's UK prudential regulator, have indicated it is a priority issue. The impact of such regulatory, policy, commercial and technological changes is expected to be highly significant and may be disruptive, especially if such changes do not occur in an orderly or timely manner or are not effective in reducing emissions sufficiently.

Furthermore, the nature and timing of the manifestation of the physical risks of climate change (which include more extreme specific

weather events such as flooding and heat waves and longer term shifts in climate) are also uncertain, and their impact on the economy is predicted to be more acute if carbon emissions are not reduced on a timely basis or to the requisite extent. Recent data indicates that global carbon emissions are continuing to increase. The potential impact on the economy includes, but is not limited to, lower GDP growth, significant changes in asset prices and profitability of industries, higher unemployment and the prevailing level of interest rates.

See also, 'The RBS Group's Purpose-led Strategy includes one area of focus on climate change which entails significant execution risk and is likely to require material changes to the business model of the RBS Group (including the NWM Group) over the next ten years', 'The NWM Group's businesses are subject to substantial regulation and oversight, which are constantly evolving and may adversely affect the NWM Group' and 'Any reduction in the credit rating assigned to RBSG plc, any of its subsidiaries (including NWM Plc or NWM Group subsidiaries) or any of their respective debt securities could adversely affect the availability of funding for the NWM Group, reduce the NWM Group's liquidity position and increase the cost of funding.'

If the NWM Group does not adequately embed climate risk into its risk framework to appropriately measure, manage and disclose the various financial, transition and physical risks it faces associated with climate change, or if the RBS Group or the NWM Group fail to implement the RBS Group's new strategy on climate change and adapt its business model to the changing regulatory requirements and market expectations on a timely basis, it may have a material and adverse impact on the NWM Group's level of business growth, its competitiveness, profitability, prudential capital requirements, ESG ratings, credit ratings, cost of funding, reputation, results of operation and financial condition.

Changes in interest rates have affected and will continue to affect the NWM Group's business and results.

Interest rate risk exists for the NWM Group, as monetary policy has been accommodative in recent years, including as a result of certain policies implemented by the Bank of England and HM Treasury such as the Term Funding Scheme, which have helped to support demand at a time of pronounced fiscal tightening and balance sheet repair. However, there remains considerable uncertainty as to the direction of interest rates and pace of change (as set by the Bank of England and other major central banks) as well as the general UK political climate. Further decreases in interest rates and/or continued sustained low or negative interest rates could adversely affect the NWM Group's profitability and prospects. In addition, a continued period of low interest rates and flat yield curves has affected and may continue to affect the interest rate margin realised between lending and borrowing costs.

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Conversely, while increases in interest rates may support NWM Group income, sharp increases in interest rates could lead to generally weaker than expected growth, or even contracting GDP, reduced business confidence, higher levels of unemployment or underemployment and adverse changes to levels of inflation.

Changes in foreign currency exchange rates may affect the NWM Group's results and financial position.

As part of the RBS Group's strategy, the NWM Group has become the markets business for the RBS Group, and is engaged principally in providing financing, risk management and trading solutions to global customers across Europe, the USA and Asia. The NWM Group entities issue instruments in foreign currencies that assist in meeting their respective capital and/or MREL requirements. In addition, NWM Plc's acquisition of NWM N.V. from RBS Group increased NWM Plc's exposure to euro movements. NWM N.V. holds a significant loan portfolio denominated in euros (see also, 'Capital and risk management — Credit Risk'). In its day-to-day operations, the NWM Group maintains policies and procedures designed to manage the impact of exposures to fluctuations in currency rates. Nevertheless, changes in currency rates, particularly in the sterling-US dollar and euro-sterling exchange rates, can adversely affect the value of assets, liabilities (including the total amount of MREL-eligible instruments), income, RWAs, capital base and expenses and the reported earnings of NWM Plc's UK and non-UK subsidiaries and may affect the NWM Group's reported consolidated financial condition, capital ratios or its income from foreign exchange dealing.

Decisions of major central banks (including by the Bank of England, the European Central Bank and the US Federal Reserve) and political or market events (including in respect of Brexit and the general UK political climate), which are outside of the NWM Group's control, may lead to sharp and sudden variations in foreign exchange rates.

HM Treasury (or UKGI on its behalf) could exercise a significant degree of influence over the RBS Group and the NWM Group is controlled by the RBSG Group.

In its November 2018 Autumn Budget, the UK Government announced its intention to continue the process of privatisation of RBSG plc and to carry out a programme of sales of RBSG plc ordinary shares with the objective of selling all of its remaining shares in RBSG plc by 2023-2024. On 6 February 2019, RBSG plc obtained shareholder approval to participate in certain directed share buyback activities. As of 31 December 2019, the UK Government held 62.1% of the issued ordinary share capital of RBSG plc. There can be no certainty as to the continuation of the sell-down process or the timing or extent of such sell-downs.

UK Government Investments Limited ('UKGI') manages HM Treasury's shareholder relationship with the RBSG plc and, although

HM Treasury has indicated that it intends to respect the commercial decisions of the RBS Group and that the RBS Group entities (including the NWM Group) will continue to have its own independent board of directors and management team determining their own strategy, its position as a majority shareholder (and UKGI's position as manager of this shareholding) means that HM Treasury or UKGI could exercise a significant degree of influence over, among other things, the election of directors and appointment of senior management, the RBS Group's (including the NWM Group's) capital strategy, dividend policy, remuneration policy or the conduct of the RBS Group's (including the NWM Group's) operations, and HM Treasury or UKGI's approach depends on government policy, which could change, including as a result of a general election. The exertion of such influence over RBS Group could in turn have an adverse effect on the governance or business strategy of the NWM Group.

In addition, as a wholly-owned subsidiary of RBSG plc, RBSG plc controls the NWM Group's board of directors, corporate policies and strategic direction. The interests of RBSG plc as an equity holder and as the NWM Group's parent may differ from the interests of the NWM Group or of potential investors in the NWM Group's securities.

Legal, regulatory and conduct risk The NWM Group's businesses are subject to substantial regulation and oversight, which are constantly evolving and may adversely affect the NWM Group.

The NWM Group is subject to extensive laws, regulations, corporate governance practice and disclosure requirements, administrative actions and policies in each jurisdiction in which it operates. Many of these have been introduced or amended recently and are subject to further material changes, which may increase compliance and conduct risks. The NWM Group expects government and regulatory intervention in the financial services industry to remain high for the foreseeable future.

In recent years, regulators and governments have focussed on reforming the prudential regulation of the financial services industry and the manner in which the business of financial services is conducted. Amongst others, measures have included: enhanced capital, liquidity and funding requirements, implementation of the UK ring-fencing regime, implementation and strengthening of the recovery and resolution framework applicable to financial institutions in the UK, the EU and the US, financial industry reforms (including in respect of MiFID II), enhanced data privacy and IT resilience requirements, enhanced regulations in respect of the provision of 'investment services and activities', enhanced regulations in respect of the provision of 'investment services and activities', and increased regulatory focus in certain areas, including conduct, consumer protection regimes, anti-money laundering, anti-bribery, anti-tax evasion, payment systems, sanctions and anti-terrorism laws and regulations. This

has resulted in the NWM Group facing greater regulation and scrutiny in the UK, the US, the EU and other countries in which it operates.

In addition, there is significant oversight by competition authorities of the markets which the NWM Group operates in. The competitive landscape for banks and other financial institutions in the UK, the rest of Europe and the US is rapidly changing. Recent regulatory and legal changes have and may continue to result in new market participants and changed competitive dynamics in certain key areas.

Recent regulatory changes, proposed or future developments and heightened levels of public and regulatory scrutiny in the UK, the EU and the US have resulted in increased capital, funding and liquidity requirements, changes in the competitive landscape, changes in other regulatory requirements and increased operating costs, and have impacted, and will continue to impact, product offerings and business models. In particular, the NWM Group is required to ensure operational continuity in resolution; the steps required to ensure such compliance entail significant costs, and also impose significant operational, legal and execution risk. Serious consequences could arise should the NWM Group be found to be non-compliant with such regulatory requirements. Such changes may also result in an increased number of regulatory investigations and proceedings and have increased the risks relating to the NWM Group's ability to comply with the applicable body of rules and regulations in the manner and within the time frames required.

Any of these developments (including any failure to comply with new rules and regulations) could have a significant impact on the NWM Group's authorisations and licences, the products and services that the NWM Group may offer, its reputation and the value of its assets, the NWM Group's operations or legal entity structure, and the manner in which the NWM Group conducts its business. Areas in which, and examples of where, governmental policies, regulatory and accounting changes and increased public and regulatory scrutiny could have an adverse impact (some of which could be material) on the NWM Group include, but are not limited to, those set out above as well as the following:

- general changes in government, central bank, regulatory or competition policy, or changes in regulatory regimes that may influence investor decisions in the markets in which the NWM Group operates;
- amendments to the framework or requirements relating to the quality and quantity of regulatory capital to be held by the NWM Group as well as liquidity and leverage requirements, either on a solo, consolidated or subgroup level;
- changes to the design and implementation of national or supranational mandated recovery, resolution or insolvency regimes or the implementation of additional or conflicting loss-absorption requirements,

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including those mandated under UK rules, the BRRD, or MREL;

- rules and regulations relating to, and enforcement of, anti-corruption, anti-bribery, anti-money laundering, anti-terrorism, sanctions, anti-tax evasion or other similar regimes;
- the imposition of additional restrictions on the NWM Group's ability to compensate its senior management and other employees and increased responsibility and liability rules applicable to senior and key employees;
- rules relating to foreign ownership, expropriation, nationalisation and confiscation of assets;
- changes to corporate practice and disclosure governance requirements, senior manager responsibility, corporate structures and conduct of business rules;
- financial market infrastructure reforms establishing new rules applying to investment services, short selling, market abuse, derivatives markets and investment funds;
- new or increased regulations relating to customer data and privacy protection as well as IT controls and resilience, including the GDPR;
- the introduction of, and changes to, taxes, levies or fees applicable to the NWM Group's operations, such as the imposition of a financial transaction tax, changes in the scope and administration of the Bank Levy, changes in tax rates, increases in the bank corporation tax surcharge in the UK, restrictions on the tax deductibility of interest payments or further restrictions imposed on the treatment of carry-forward tax losses that reduce the value of deferred tax assets and require increased payments of tax;
- laws and regulations in respect of climate change and sustainable finance (including ESG) considerations; and
- other requirements or policies affecting the NWM Group and its profitability or product offering, including through the imposition of increased compliance obligations or obligations which may lead to restrictions on business growth, product offerings, or pricing.

To support the UK's goal of Net Zero by 2050, the UK and Scottish governments and UK and international regulators, such as the PRA and European Commission, are actively seeking to develop new and existing regulations directly and indirectly focussed on climate change and the associated financial risks. Regulatory and policy developments, may have a significant impact on the markets in which the NWM Group operates, and its associated credit, market and financial risk profile.

In a Joint Declaration on Climate Change published in July 2019, the PRA, FCA, Financial Reporting Council and The Pensions Regulator set out their commitment to working collaboratively to address the risks of climate change. In October 2019, the RBS

Group submitted its initial plan to meet the PRA's supervisory expectations in its supervisory statement (SS 3/19) which sets forth an expectation that regulated entities adopt a Board-level strategic approach to managing and mitigating the financial risks of climate change and embed the management of them into their governance frameworks, subject to existing prudential regulatory supervisory tools (including stress testing and individual and systemic capital requirements). In addition, The Bank of England announced in December 2019 that it will use the 2021 biennial exploratory scenario (BES) to stress banks on certain climate scenarios to test the resilience of the current business models of the largest banks, insurers and the financial system to the physical and transition risks from climate change. The prudential regulation of climate risk will be an important driver in how the RBS Group otherwise decides how it allocates capital and further develop its risk appetite for financing certain types of activity or engaging with counterparties that do not align to a transition to a net zero economy.

The FCA have also announced that climate change and green finance will be priorities with a focus on disclosure, integrating climate change into decision-making and consumers' access to green financial services. The NWM Group also recognises various legislative actions and proposals by, among others, the European Commission's Action Plan on Sustainable Finance which include a taxonomy on sustainable finance. Many of these legislative and regulatory initiatives, and especially the EU taxonomy, are focused on developing standardised definitions for the green and sustainable criteria of assets and liabilities, which could change over time and impact the NWM Group's recognition of its climate financing activity and lead to reputational and conduct risk on its own sustainable financing activity.

Changes in laws, rules or regulations, or in their interpretation or enforcement, or the implementation of new laws, rules or regulations, including contradictory or conflicting laws, rules or regulations by key regulators or policymakers in different jurisdictions, or failure by the NWM Group to comply with such laws, rules and regulations, may adversely affect the NWM Group's business, financial condition and results. In addition, uncertainty and insufficient international regulatory coordination as enhanced supervisory standards are developed and implemented may adversely affect the NWM Group's ability to engage in effective business, capital and risk management planning.

The NWM Group is subject to a number of legal, regulatory and governmental actions and investigations as well as associated remedial undertakings, the outcomes of which are inherently difficult to predict, and which could have an adverse effect on the NWM Group.

The NWM Group's operations are diverse and complex and it operates in legal and

regulatory environments that expose it to potentially significant legal proceedings, and civil and criminal regulatory and governmental actions. The NWM Group has settled a number of legal and regulatory actions over the past several years but continues to be, and may in the future be, involved in such actions in the US, the UK, Europe and other jurisdictions

The NWM Group is subject to a number of ongoing reviews, investigations and proceedings (both formal and informal) by governmental law enforcement and other agencies and litigation proceedings, relating to, among other matters, the offering of securities, conduct in the foreign exchange market, the setting of benchmark rates such as LIBOR and related derivatives trading, the issuance, underwriting, and sales and trading of fixed-income securities (including government securities), product mis-selling, customer mistreatment, anti-money laundering, antitrust and various other compliance issues. See also, 'Litigation, investigations and reviews' of Note 28 on the consolidated accounts on pages 133 to 136 for details of these matters. Legal and regulatory actions are subject to many uncertainties, and their outcomes, including the timing, amount of fines or settlements or the form of any settlements, which may be material and in excess of any related provisions, are often difficult to predict, particularly in the early stages of a case or investigation, and the NWM Group's expectations for resolution may change.

NWM Group companies are currently responding to a criminal investigation by the United States Attorney for the District of Connecticut (USAO) and the United States Department of Justice (DoJ), concerning securities trading in 2018 by certain former traders of NWM Plc, involving alleged spoofing. The trading activity occurred during the term of the non-prosecution agreement (NPA) that NWMSI entered into with the USAO in October 2017 in connection with alleged misrepresentations to counterparties relating to secondary trading in various forms of asset-backed securities. Under the NPA, non-prosecution was conditioned on NWMSI and affiliated companies not engaging in conduct during the NPA that the USAO determines was a felony under federal or state law or a violation of the anti-fraud provisions of the United States securities law. See also, 'Litigation, investigations and reviews' of Note 28 to the consolidated accounts for details of these matters.

The duration and outcome of the criminal investigation into alleged spoofing, which may include the extension, modification, or deemed violation of the NPA, remain uncertain. No settlement may be reached and further substantial additional provisions and costs may be recognised. Any finding of criminal liability by US authorities as to NWM Plc, NWMSI, or an affiliate (including as a result of pleading guilty), as to either the alleged spoofing or the conduct underlying the NPA, could have material collateral consequences for NWM Group's business.

Risk Factors

These may include consequences resulting from the need to reapply for various important licenses or obtain waivers to conduct certain existing activities of the NWM Group, particularly but not solely in the US, which may take a significant period of time and the results of which are uncertain. Failure to obtain such licenses or waivers could adversely impact the NWM Group's business, in particular in the US, including if it results in the NWM Group being precluded from carrying out certain activities.

Adverse outcomes or resolution of current or future legal or regulatory actions and associated remedial undertakings could result in restrictions or limitations on the NWM Group's operations, and could adversely impact the NWM Group's capital position or its ability to meet regulatory capital adequacy requirements. Failure to comply with undertakings made by the NWM Group to its regulators may result in additional measures or penalties being taken against the NWM Group.

The NWM Group may not effectively manage the transition of LIBOR and other IBOR rates to alternative risk free rates.

UK and international regulators are driving a transition from the use of interbank offer rates (IBORs), including LIBOR, to alternative risk free rates (RFRs). In the UK, the FCA has asserted that they will not compel LIBOR submissions beyond 2021, thereby jeopardising its continued availability, and have strongly urged market participants to transition to RFRs, as has the CFTC and other regulators in the US. The NWM Group has a significant exposure to IBORs, and continues to reference it in certain products, primarily its derivatives and legacy securities. Although the NWM Group is actively engaged with customers and industry working groups to manage the risks relating to such exposure, and is exploring ways to utilise RFRs to the extent possible, the legal mechanisms to effect transition cannot be confirmed, and the impact cannot be determined nor any associated costs accounted for, until such time that RFRs are utilised exclusively, and there is market acceptance on the form of alternative RFRs for different products, and certain IBOR obligations may not be able to be changed. The transition and uncertainties around the timing and manner of transition to RFRs represent a number of risks for the NWM Group, its clients and the financial services industry more widely. Following an analysis of the NWM Group's IBOR-linked financial products and instruments, the NWM Group has identified the following risks: legal risks (as changes will be required to documentation for new and the majority of existing transactions); financial risks (which may arise from any changes in valuation of financial instruments linked to benchmarks rates and may impact the NWM Group's cost of funds and its risk management related financial models); pricing risks (such as

changes to benchmark rates could impact pricing mechanisms on certain instruments); operational risks (due to the requirement to adapt IT systems, trade reporting infrastructure and operational processes); and conduct risks (which include communication regarding the potential impact on customers, and engagement with customers during the transition period).

It is therefore currently difficult to determine to what extent the changes will affect the NWM Group, or the costs of implementing any relevant remedial action. Uncertainty as to the nature and extent of such potential changes, alternative reference rates or other reforms including the potential continuation of the publication of LIBOR may adversely affect financial instruments using LIBOR as benchmarks. The implementation of any alternative RFRs may be impossible or impracticable under the existing terms of such financial instruments and could have an adverse effect on the value of, return on and trading market for certain financial instruments and on the NWM Group's profitability. There is also the risk of an adverse effect to reported performance arising from the transition rules established by accounting bodies, as certain rules (as proposed by the IASB) are still to be finalised.

Changes in tax legislation or failure to generate future taxable profits may impact the recoverability of certain deferred tax assets recognised by the NWM Group.

In accordance with IFRS (as adopted by the European Union), the NWM Group has recognised deferred tax assets on losses available to relieve future profits from tax only to the extent it is probable that they will be recovered. The deferred tax assets are quantified on the basis of current tax legislation and accounting standards and are subject to change in respect of the future rates of tax or the rules for computing taxable profits and offsetting allowable losses.

Failure to generate sufficient future taxable profits or further changes in tax legislation (including with respect to rates of tax) or accounting standards may reduce the recoverable amount of the recognised tax loss deferred tax assets, amounting to £75 million as at 31 December 2019. Changes to the treatment of certain deferred tax assets may impact the NWM Group's capital position. In addition, the NWM Group's interpretation or application of relevant tax laws may differ from those of the relevant tax authorities and provisions are made for potential tax liabilities that may arise on the basis of the amounts expected to be paid to tax authorities. The amounts ultimately paid may differ materially from the amounts provided depending on the ultimate resolution of such matters.

Forward-looking statements

Cautionary statement regarding forward-looking statements

Certain sections in this document contain 'forward-looking statements' as that term is defined in the United States Private Securities Litigation Reform Act of 1995, such as statements that include the words 'expect', 'estimate', 'project', 'anticipate', 'commit', 'believe', 'should', 'intend', 'plan', 'could', 'probability', 'risk', 'Value-at-Risk (VaR)', 'target', 'goal', 'objective', 'may', 'endeavour', 'outlook', 'optimistic', 'prospects' and similar expressions or variations on these expressions.

In particular, this document includes forward-looking statements relating, but not limited to: future profitability and performance, including financial performance targets such as return on tangible equity; cost savings and targets; implementation of the RBS Group and NWM Group's strategy; litigation and government and regulatory investigations, including the timing and financial and other impacts thereof; the continuation of the NWM Group's balance sheet reduction programme, including the reduction of risk-weighted assets (RWAs) and the timing thereof; capital and strategic plans and targets; capital, liquidity and leverage ratios and requirements, including CET1 Ratio, RWA equivalents (RWAE), Pillar 2 and other regulatory buffer requirements, minimum requirement for own funds and eligible liabilities, and other funding plans; funding and credit risk profile; capitalisation; portfolios; net interest margin; customer loan and income growth; the level and extent of future impairments and write-downs, including with respect to restructuring and remediation costs and charges; and the NWM Group's exposure to political risk, economic risk, climate change risk, operational risk, conduct risk, cyber and IT risk and credit rating risk and to various types of market risks, including interest rate risk, foreign exchange rate risk and commodity and equity price risk; customer experience including our Net Promoter Score (NPS); employee engagement and gender balance in leadership positions.

Limitations inherent to forward-looking statements

These statements are based on current plans, estimates, targets and projections, and are subject to significant inherent risks, uncertainties and other factors, both external and relating to the RBS Group and the NWM Group's strategy or operations, which may result in the NWM Group being unable to achieve the current targets, predictions, expectations and other anticipated outcomes expressed or implied by such forward-looking statements. In addition, certain of these disclosures are dependent on choices relying on key model characteristics and assumptions and are subject to various limitations, including assumptions and estimates made by management. By their nature, certain of these disclosures are only estimates and, as a result, actual future gains and losses could differ materially from those that have been estimated. Accordingly, undue reliance should not be placed on these statements. Forward-looking statements speak only as of the date we make them and we expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in the NWM Group's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

Important factors that could affect the actual outcome of the forward-looking statements

We caution you that a large number of important factors could adversely affect our results or our ability to implement our strategy, cause us to fail to meet our

targets, predictions, expectations and other anticipated outcomes or affect the accuracy of forward-looking statements we describe in this document including in the risk factors set out in the NWM Group's 2019 Annual Report and other risk factors and uncertainties discussed in this document. These include the significant risks presented by: strategic risk (including in respect of: the implementation and execution of the NWM Refocusing, the impact of the RBS Group's Purpose-led Strategy and climate ambition on the NWM Group, and the risk that the NWM Group may not achieve its targets); financial resilience risk (including in respect of: the NWM Group's ability to meet targets, generate returns or implement its strategy effectively; the recent structural change as a result of the UK ring-fencing regime and the acquisition of NWM N.V.; the NWM Group's reliance on access to global capital markets to meet its funding commitments; the ability of the NWM Group to meet prudential regulatory requirements for capital and liquidity; NWM Plc's ability to adequately access sources of liquidity and funding; NWM Plc (and its subsidiaries) ability to manage its capital, liquidity or funding effectively; changes in the credit ratings of RBSG plc, any of its subsidiaries or any of its respective debt securities; the highly competitive markets in which the NWM Group operates; the RBS Group's ability to meet requirements of regulatory stress tests; deteriorations in borrower and counterparty credit quality; possible losses or the requirement to maintain higher levels of capital as a result of limitations or failure of various models; sensitivity of the NWM Group's financial statements to underlying accounting policies, judgments, assumptions and estimates; changes in applicable accounting policies or rules; and the application of UK statutory stabilisation or resolution powers), operational and IT resilience risk (including in respect of: the NWM Group being subject to cyberattacks; operational risks inherent in the NWM Group's business; the NWM Group's operations being highly dependent on its IT systems; the NWM Group relying on attracting, retaining, developing and remunerating senior management and skilled personnel and maintaining good employee relations; the NWM Group's risk management framework; and reputational risk), economic and political risk (including in respect of: increased political and economic risks and uncertainty in the UK and global markets; prevailing uncertainty surrounding the terms of the UK's withdrawal from the European Union; climate change and the transition to a low carbon economy; changes in interest rates; changes in foreign currency exchange rates; and HM Treasury's ownership of RBSG plc and the possibility that it may exert a significant degree of influence over the RBS Group), and legal, regulatory and conduct risk (including in respect of: the NWM Group's businesses being subject to substantial regulation and oversight; legal, regulatory and governmental actions and investigations; the transition of LIBOR and IBOR rates to alternative risk free rates; and changes in tax legislation).

The forward-looking statements contained in this document speak only as at the date hereof, and the NWM Group does not assume or undertake any obligation or responsibility to update any forward-looking statement to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

The information, statements and opinions contained in this document do not constitute a public offer under any applicable legislation or an offer to sell or solicit of any offer to buy any securities or financial instruments or any advice or recommendation with respect to such securities or other financial instruments.