TESCO PERSONAL FINANCE PLC

INTERIM FINANCIAL REPORT

FOR THE SIX MONTHS ENDED 31 AUGUST 2018

COMPANY NUMBER SC173199

TESCO PERSONAL FINANCE PLC
CONTENTS

TESCO PERSONAL FINANCE PLC
INTERIM MANAGEMENT REPORT

This Interim Financial Report comprises the Interim Management Report and the Interim Condensed Consolidated Financial Statements and accompanying notes. In the Interim Financial Report, unless specified otherwise, the 'Company' means Tesco Personal Finance plc and the 'Group' means the Company and its subsidiaries and joint venture included in the Interim Condensed Consolidated Financial Statements. The Group operates using the trading name of Tesco Bank.

Tesco Personal Finance plc is a wholly owned subsidiary of Tesco Personal Finance Group Limited, the share capital of which is wholly owned by Tesco PLC. A reconciliation of the results contained within the Interim Financial Report to the Tesco Bank results presented in the Tesco PLC Interim Results 2018/19 can be found on the Tesco PLC internet page: https://www.tescoplc.com/media/475075/brokerpack_31082018.pdf

Cautionary Statement regarding forward-looking information

Where this document contains forward-looking statements, these are made by the Directors in good faith based on the information available to them at the time of their approval of this report. These statements should be treated with caution due to the inherent risks and uncertainties underlying any such forward-looking information. The Group cautions users of these Interim Condensed Consolidated Financial Statements that a number of factors, including matters referred to in this document, could cause actual results to differ materially from those contained in any forward-looking statement. Such factors include, but are not limited to, those discussed under 'Principal risks and uncertainties' on pages 6 and 7 of this Interim Management Report.

Business Model

The Group provides financial services and products to personal customers in the United Kingdom (UK). The Company owns 49.9% of Tesco Underwriting Limited (TU), an authorised insurance company. TU is accounted for as a joint venture of the Group. The Company is incorporated and registered in Scotland.

Adoption of IFRS 9 and IFRS 15

The Group adopted both International Financial Reporting Standard (IFRS) 9 'Financial Instruments' and IFRS 15 'Revenue from Contracts with Customers' with effect from 1 March 2018.

IFRS 9 has been applied retrospectively at 1 March 2018 by adjusting the opening balance sheet at that date, with no requirement to restate comparative periods. IFRS 15 has been applied fully retrospectively and prior period comparatives have been restated.

The adoption of IFRS 9 resulted in a decrease in the Group's and Company's total financial assets of £223.5m, with a related deferred income tax asset of £57.0m. The overall impact on equity was therefore a reduction in equity of £166.5m at 1 March 2018.

The adoption of IFRS 15 resulted in the earlier recognition of certain insurance renewal commission income, amounting to £18.5m at 1 March 2017, as well as the reclassification of the provision for insurance refunds of £4.2m from provisions for liabilities and charges to other liabilities. A related increase of £5.0m in the deferred income tax liability was also recognised at 1 March 2017.

Further details of the transitional impact of the adoption of IFRS 9 and IFRS 15 are set out at note 2.

Headlines

Income Statement

- Profit before tax is 24.8% lower at £83.0m (August 2017: £110.4m)[1]. The key drivers of the decrease in profit before tax are:
  - a 9.8% increase in net interest income to £267.4m (August 2017: £243.6m), reflecting higher interest earnings on the back of lending growth. Net interest margin has decreased slightly to 3.8% (August 2017: 4.0%), reflecting the impact of growth in the lower margin Mortgage book as a percentage of the Group's overall lending portfolio;
  - a 6.5% reduction in fee and commission income to £170.8m (August 2017: £182.7m)[1]. This predominantly reflects continued pressure on insurance retention rates due to a highly competitive environment, leading to a reduction in insurance commission income, and a reduction in ATM income as a result of the downward trend in ATM transactions being seen across the market as customers move towards contactless and other card payments;
  - a loss on financial instruments at fair value through profit or loss (FVPL) of £3.5m (August 2017: gain of £1.5m);
  - a gain on disposal of investment securities of £8.4m (August 2017: £nil);
  - an increase of 7.4% in operating expenses to £274.0m (August 2017: £255.1m). This includes a charge of £16.4m in respect of a regulatory provision relating to the November 2016 fraud incident and an additional payment protection insurance (PPI) charge of £7.0m (August 2017: £nil) recognised during the period, offset by a restructuring credit of £1.6m (August 2017: £nil) relating to the early exit from the Group's offices in central Edinburgh; and
  - a 29.0% increase in impairment charges to £90.2m (August 2017: £69.9m)[2]. This reflects balance growth and the implementation of a number of credit initiatives in recent years, which have been targeted at supporting the borrowing needs of Tesco customers in a profitable and controlled manner and also a lower gain on sale of non-performing debt, with £4.5m realised in the period (August 2017: £9.6m). The bad debt:asset ratio (BDAR) increased to 1.5% (August 2017: 1.3%)[3].
- Underlying profit before tax, which excludes items which are not reflective of ongoing trading performance, is 0.6% lower at £108.3m (August 2017: £108.9m)[1]. A reconciliation of statutory to underlying profit for the current and prior period is set out on page 5.
- Income tax on the Group's profit for the period is a charge of £26.4m (August 2017: £27.5m)[1]. The Group's current year effective tax rate is higher than the statutory rate principally due to the non-deductibility of the additional PPI charge and regulatory provision recognised during the period.

Balance Sheet

- Loans and advances to customers have increased by 5.4% to £12.1bn (February 2018: £11.5bn). Mortgage balances reached £3.5bn (February 2018: £3.0bn) as the Mortgage product range continues to expand into the intermediary broker channel, and the Group has also seen growth in both Credit Cards and Personal Loan balances of 3.2% and 5.5% respectively.

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

[2] The impairment charge for the half-year ended 31 August 2018 reflects impairment charges on an expected loss basis in accordance with IFRS 9. The comparative figure reflects impairment charges on an incurred loss basis, as previously reported under IAS 39.

[3] The BDAR for the half-year ended 31 August 2018 reflects impairment charges on an expected loss basis in accordance with IFRS 9. The comparative figure reflects impairment charges on an incurred loss basis, as previously reported under IAS 39.

Balance Sheet (continued)

- Customer deposits have increased by 8.9% to £10.1bn (February 2018: £9.2bn), and continue to be the main source of the Group's funding. Deposits from banks at 31 August 2018 totalled £1,813.2m (February 2018: £1,539.0m). At the period end, the Group had entered into repurchase transactions of £474.2m (February 2018: £200.0m) and accessed £1,339.0m of funds from the Bank of England's (BoE) Term Funding Scheme (TFS) (February 2018: £1,339.0m). The lower cost of funding provided by the TFS is reflected in competitive offers for the Group's borrowing customers.
- The balance sheet remains strong and well positioned to support future lending growth from both a liquidity and capital stand point. At 31 August 2018, the total capital ratio was 18.2% (February 2018: 19.4%)[1] and net stable funding ratio (NSFR) was 117.7% (February 2018: 118.1%)[1]. The decrease in the NSFR over the period reflects the relative movements in the Group's available and required funding, with additional customer deposits resulting in increased available funding of £0.8bn, offset by a £0.6bn increase in the Group's required funding, arising from the growth in customer lending referred to above.

Strategic Priorities

The vision of Tesco Bank is to 'be the bank for people who shop at Tesco'. In order to further the Group's pursuit of this vision, the Group continues to seek opportunities to make it easier for Tesco customers to bank and insure with the Group through targeted investment in technology and data, making life simpler for both customers and colleagues and driving efficiency that can be reinvested in the customer offer. The Group's strategy is to bring the best of Tesco to financial services, offering customers great value across the range of products and earning customer trust through the Group's actions.

Use of the Group's mobile banking App continues to expand, and the App has now been downloaded by more than one million users. Changes to the App in April 2018 simplified the registration journey, enhancing the customer experience by allowing customers to register for the Mobile App without having to set up online banking security beforehand.

In May 2018, the Group launched a new online banking experience, to improve how the Group's customers view their banking products, making it easier to see what matters most, at first glance. The Group's Personal Current Account customers can now see a balance beside each of their transactions, helping customers to better manage their money.

The Group's Tesco Pay+ service continues to grow, offering Tesco's shoppers the ability to pay and collect Clubcard points with one simple and convenient scan of their phone. The App now has over 600,000 registered users.

The Group continues to deliver value to its Mortgage customers and improve the customer experience. In the period, the Group launched a new Broker Product Switch Portal, which allows the Group's panel of Mortgage intermediaries to select new remortgage deals on behalf of existing customers.

The Group now has 323 Travel Money bureaux across the UK, and provided customers with over £1 billion in currency in the 12 months to 31 August 2018.

The Group's commitment to offering attractive products and good service for customers has been rewarded with recognition as 'Best Card Provider (Standard Rate)' and 'Best Variable Rate Mortgage Provider' at the 2018 Moneyfacts Awards, 'Best Direct Lender' at the What Mortgage Awards 2018, and 'Best Online Pet Insurance Provider' and 'Best Direct Car Insurance Provider' at the Your Money Awards 2018.

During the period, colleagues raised over £48,000 for the Group's charity partners and volunteered over 800 hours to their local communities. In April 2018, the Group marked its first 'Tesco Bank Turns Pink' event, showing the Group's commitment and support to Cancer Research UK's Race for Life.

In August 2018, Gerry Mallon joined the Group as Chief Executive.

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

Regulatory Developments

The Group continues to monitor and prepare for a number of regulatory changes taking effect over the next few years.

Three major components of regulatory reform relating to data regulation came into force during 2018. These are Open Banking, the second Payment Services Directive (PSD2) and the new General Data Protection Regulation (GDPR), all of which are focused on innovation, competition and consumer protection.

PSD2, the first phase of which took effect from 13 January 2018, together with Open Banking, allows customers to choose to share data from their banking products with third party providers (TPPs) and bring together all of their financial relationships and data in one place, potentially leading to a fundamental change in how customers manage both their money and data over the longer term. The aim of these changes is to promote competition and enhance customer choice, providing potential opportunities for the Group to attract new customers as well as potentially increased competition from traditional banking businesses and new providers of financial services, including technology companies with strong brand reputation. The Group continues to monitor and review the risks associated with the introduction of PSD2, including the need to ensure that there is appropriate control and ownership of sensitive and confidential customer data as the use of TPPs becomes more widespread.

The new General Data Protection Regulation came into effect on 25 May 2018, providing new and enhanced rights for individuals in respect of their personal information. The Group has undertaken a business-wide review in order to ensure the clear control and management of customer data and that compliant data retention policies are in place and adhered to.

Uncertainty remains around the implementation and impact of some regulatory developments, including the finalisation of Basel III, which will be subject to European Union (EU) and UK implementation. In addition, the Group will be subject to the minimum requirements for own funds and eligible liabilities (MREL) on an interim basis from 1 January 2020, with full implementation applicable from 1 January 2022. The requirements are factored into the Group's funding and capital plans.

Business Review

During the period, the business continued to deliver growth across its primary products (Credit Cards, Personal Loans, Mortgages, Personal Current Accounts and Savings).

Mortgage balances grew by 16.8% in the period, reaching £3,504.4m (February 2018: £3,000.7m), while Credit Card balances increased by 3.2% and Personal Loans by 5.5%.

Customer deposits of £10,073.2m (February 2018: £9,248.0m) continue to be the Group's primary source of funding. The Group's customer deposits grew by 8.9% in the period, reflecting the value offered to customers.

During the period, the Group maintained its funding from the BoE's TFS at £1,339.0m (February 2018: £1,339.0m) in order to support future lending growth.

Money Services products have performed well overall as the Group continues to enhance the product range and expand the customer base. A reduction in ATM transaction volumes, due to the declining use of cash as customers move towards contactless and other card payments, was partially offset by growth in other products, including Travel Money.

A significant and ongoing investment has been made in Motor insurance pricing in the period, across both new business and renewal policies, in response to price deflation, supporting the Group's commitment to offering value to Tesco customers. This has driven improved Motor insurance retention rates year-on-year, although the total number of in-force policies has fallen, driven by the impact of overall market price deflation on Motor insurance premiums.

Financial Performance

The Group's financial performance is presented in the Interim Condensed Consolidated Income Statement on page 8. A summary of the Group's financial performance on an underlying basis, excluding items which are not reflective of ongoing trading performance, is presented below.

	Statutory basis £m	Restructuring costs[1] £m	Customer redress[2] £m	Regulatory provision[3] £m	Financial instruments[4] £m	Underlying basis £m
6 months ended 31 August 2018						
Net interest income	267.4	-	-	-	-	267.4
Other income	175.7	-	-	-	3.5	179.2
Total income	**443.1**	-	-	-	3.5	**446.6**
Total operating expenses	(274.0)	(1.6)	7.0	16.4	-	(252.2)
Impairment	(90.2)	-	-	-	-	(90.2)
Operating profit	**78.9**	(1.6)	7.0	16.4	3.5	**104.2**
Share of profit of joint venture	4.1	-	-	-	-	4.1
Profit before tax	**83.0**	(1.6)	7.0	16.4	3.5	**108.3**

	Statutory basis £m Restated[5]	Restructuring costs £m	Customer redress £m	Regulatory provision £m	Financial instruments[4] £m	Underlying basis £m Restated[5]
6 months ended 31 August 2017						
Net interest income	243.6	-	-	-	-	243.6
Other income	184.2	-	-	-	(1.5)	182.7
Total income	**427.8**	-	-	-	**(1.5)**	**426.3**
Total operating expenses	(255.1)	-	-	-	-	(255.1)
Impairment	(69.9)	-	-	-	-	(69.9)
Operating profit	**102.8**	-	-	-	**(1.5)**	**101.3**
Share of profit of joint venture	7.6	-	-	-	-	7.6
Profit before tax	**110.4**	-	-	-	**(1.5)**	**108.9**

[1] Comprising:

- a restructuring credit of £1.6m (August 2017: £nil), reflecting a reduction in dilapidations and onerous lease provisions, presented within administrative expenses on page 8. This credit is in relation to business restructuring and not considered part of the Group's underlying results.

[2] Comprising:

- PPI provision charge of £7.0m (August 2017: £nil) presented within operating expenses on page 8. These costs relate to historic sales of PPI and are not reflective of the Group's underlying trading performance.

[3] Comprising:

- a charge of £16.4m (August 2017: £nil) in respect of the November 2016 fraud incident, presented within operating expenses on page 8. This charge relates to the financial penalty imposed by the Financial Conduct Authority in relation to this incident and is not reflective of the Group's underlying trading performance.

[4] Comprising:

- Losses on financial instruments at FVPL of £3.5m (August 2017: gains of £1.5m) presented within total income on page 8. Fair value movements on financial instruments reflect hedge ineffectiveness arising from hedge accounting and fair value movements on derivatives in economic hedges that do not meet the criteria for hedge accounting. Where these derivatives are held to maturity, fair value movements represent timing differences that will reverse over the life of the derivatives. Therefore, excluding these movements from underlying profit more accurately represents the underlying performance of the Group. Where derivatives are terminated prior to maturity, this may give rise to fair value movements that do not reverse.

[5] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

Key Performance Indicators

The Directors consider the following to be Key Performance Indicators for the Consolidated Income Statement:

	31 August 2018	28 February 2018 Restated[1]	31 August 2017 Restated[1]
Net interest margin	3.8%	3.9%	4.0%
Underlying cost:income ratio[1]	56.5%	60.0%	59.8%
Cost:income ratio[1]	61.8%	61.9%	59.6%
Bad debt:asset ratio	1.5%	1.3%	1.3%

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

Capital and Liquidity Ratios

The Directors consider the following to be Key Performance Indicators for capital and liquidity reporting:

	31 August 2018	28 February 2018 Restated[1]	31 August 2017 Restated[1]
Common equity tier 1 ratio[1]	16.0%	16.2%	16.7%
Total capital ratio[1]	18.2%	19.4%	19.8%
Net stable funding ratio[1]	117.7%	118.1%	119.1%
Loan to deposit ratio	120.6%	124.6%	121.0%

The Group's total capital ratio remains above internal targets and regulatory requirements at 18.2% (February 2018: 19.4%)[1] and leaves the Group well placed to support future growth.

The increase in impairment provisions as a result of the adoption of IFRS 9 reduced the Group's common equity tier 1 capital ratio by 164 basis points on an end point basis. The adoption of the regulatory capital transition arrangements allow the Group to spread the expected increase in provision over a 5 year period from 1 March 2018. The impact of IFRS 9 at 31 August 2018 under the transitional provisions was to reduce common equity tier 1 capital by £7.9m. The Group's common equity tier 1 capital is disclosed in note 14.

The NSFR, a measure of the Group's liquidity position, is within appetite at 117.7% as at 31 August 2018 (February 2018: 118.1%)[1]. The Group maintains a liquid asset portfolio of high quality securities of £1.9bn (February 2018: £2.2bn).

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

Principal risks and uncertainties

The Board of Directors has overall responsibility for determining the Group's strategy and related Risk Appetite. The Board's Risk Appetite comprises a suite of Risk Appetite statements, underpinned by corresponding measures with agreed triggers and limits. The Risk Appetite framework defines the type and amount of risk that the Group is prepared to accept to achieve its objectives and forms a key link between the day to day risk management of the business, its strategic objectives, long term plan, capital plan and stress testing. The Risk Appetite is formally reviewed by the Board on at least an annual basis.

The Board is also responsible for overall corporate governance, which includes overseeing a robust and effective system of risk management and that the level of capital and liquidity held is adequate and consistent with the risk profile of the business. To support this, a Risk Management Framework (RMF) has been embedded across the Group and is underpinned by governance, controls, processes, systems and policies within the first line business areas and those of the second line Risk Management Function.

Principal risks and uncertainties (continued)

The Chief Risk Officer (CRO) performs a strategic risk management role and is responsible for managing and enhancing the RMF. The CRO is independent from any commercial function, reports directly to the Chief Executive Officer and can only be removed from his position with the approval of the Board

The principal risks and uncertainties faced by the Group remain unchanged from those set out in the Group's Annual Report and Financial Statements for the year ended 28 February 2018 (pages 7 to 11).

Credit risk	The risk that a borrower will default on a debt or obligation by failing to make contractually obligated payments, or that the Group will incur losses due to any other counterparty failing to meet their financial obligations.
Operational risk	The risk of potential error, loss, harm or failure caused by ineffective or inadequately defined processes, system failure, improper conduct, human error or from external events. This includes the significant threat of cyber attacks, financial crime and fraud across the Financial Services industry.
Liquidity and Funding risk	Liquidity risk is the risk that the Group is not able to meet its obligations as they fall due. Funding risk is the risk that the Group does not have sufficiently stable and diverse sources of funding.
Market risk	The risk that the value of earnings or capital is altered through the movement of market rates. This includes interest rates, foreign exchange rates, credit spreads and equities.
Insurance risk	This risk arises through the provision of insurance products in return for a premium. These risks may or may not occur as expected and the amount and timing of these risks are uncertain and determined by events outside of the Group's control.
Regulatory risk	The risk of reputational damage, liability or material loss from failure to comply with the requirements of the financial services regulators or related codes of best practice applicable to the business areas within which the Group operates.
Capital risk	The risk that the Group holds regulatory capital which is of insufficient quality and quantity to enable it to absorb losses.
Brexit	On 29 March 2017 the UK triggered Article 50, formally beginning the process to leave the EU. The process of exiting the EU continues to contribute to political and economic uncertainty in the UK and Europe.
Libor rate replacement	On 27 July 2017 the Head of the Financial Conduct Authority announced that the London Interbank Offered Rate (LIBOR) would be phased out and replaced with an alternative reference rate by the end of 2021. The Sterling Overnight Index Average (SONIA) has now been confirmed as the reference rate. The Group has considered and identified the risks associated with moving to SONIA as the reference rate and has developed a plan to mitigate these risks, which is being implemented in accordance with the Group's governance structure. The Group also continues to monitor industry developments.

TESCO PERSONAL FINANCE PLC
INTERIM CONDENSED CONSOLIDATED INCOME STATEMENT (UNAUDITED)
FOR THE SIX MONTHS ENDED 31 AUGUST 2018

	Note	6 months ended 31 August 2018 £m	6 months ended 31 August 2017 £m Restated[1]
Interest and similar income	4	354.2	313.6
Interest expense and similar charges	4	(86.8)	(70.0)
Net interest income		**267.4**	**243.6**
Fees and commissions income	5	187.6	198.2
Fees and commissions expense	5	(16.8)	(15.5)
Net fees and commissions income		**170.8**	**182.7**
Net (loss)/gain on financial instruments at FVPL		(3.5)	1.5
Net gain on investment securities		8.4	-
Dividend income		-	-
Net other income		**4.9**	**1.5**
Total income		**443.1**	**427.8**
Administrative expenses		(207.2)	(213.7)
Depreciation and amortisation		(43.4)	(41.4)
Provision for customer redress	12	(7.0)	-
Regulatory provision	12	(16.4)	-
Operating expenses		**(274.0)**	**(255.1)**
Impairment loss on financial assets	6	(90.2)	(69.9)
Operating profit		**78.9**	**102.8**
Share of profit of joint venture		4.1	7.6
Profit before tax		**83.0**	**110.4**
Income tax charge	7	(26.4)	(27.5)
Profit for the period attributable to owners of the parent		**56.6**	**82.9**

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period (refer to note 2 for further details) and a reclassification between interest and similar income and interest expense and similar charges (refer to note 1 for further details).

TESCO PERSONAL FINANCE PLC

INTERIM CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (UNAUDITED)

FOR THE SIX MONTHS ENDED 31 AUGUST 2018

	6 months ended 31 August 2018 £m	6 months ended 31 August 2017 £m Restated[1]
Profit for the period	56.6	82.9
Items that may be reclassified subsequently to the income statement		
Available-for-sale (AFS) investment securities		
Net gains on AFS investment securities	n/a	2.9
Taxation	n/a	(0.8)
	n/a	2.1
Debt securities at fair value through other comprehensive income (FVOCI)		
Net losses on debt securities at FVOCI	(17.0)	n/a
Net gains on debt securities reclassified to the income statement on disposal	9.5	n/a
Taxation	2.0	n/a
	(5.5)	n/a
Cash flow hedges		
Net gains arising on cash flow hedges	0.3	0.2
Taxation	(0.1)	(0.1)
	0.2	0.1
Share of other comprehensive (expense)/income of joint venture	(0.1)	0.1
	(0.1)	0.1
Items that will not be reclassified to the income statement		
Equity securities at FVOCI		
Net gains on equity securities designated at FVOCI	0.5	n/a
Taxation	(0.1)	n/a
	0.4	n/a
Other comprehensive (expense)/income for the period, net of tax	**(5.0)**	**2.3**
Total comprehensive income for the period attributable to owners of the parent	**51.6**	**85.2**

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

TESCO PERSONAL FINANCE PLC
INTERIM CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION (UNAUDITED)
AS AT 31 AUGUST 2018

	Note	31 August 2018 £m	28 February 2018 £m Restated[1]	31 August 2017 £m Restated[1]
Assets				
Cash and balances with central banks		1,232.9	1,318.6	778.2
Loans and advances to banks		249.2	-	-
Loans and advances to customers	9	12,144.4	11,522.4	10,762.2
Derivative financial instruments		38.0	46.1	25.8
Investment securities		715.4	959.5	985.2
Prepayments and accrued income		62.0	49.3	56.5
Other assets		225.4	280.6	312.0
Investment in joint venture	10	83.7	90.0	94.2
Deferred income tax asset		55.8	-	-
Intangible assets		244.6	271.1	284.6
Property, plant and equipment		63.7	68.0	72.4
Total assets		**15,115.1**	**14,605.6**	**13,371.1**
Liabilities				
Deposits from banks		1,813.2	1,539.0	939.0
Deposits from customers		10,073.2	9,248.0	8,896.9
Debt securities in issue	11	922.6	1,347.6	1,053.8
Derivative financial instruments		48.6	88.4	123.5
Provisions for liabilities and charges	12	70.1	76.0	67.0
Accruals and deferred income		96.9	109.0	93.3
Current income tax liability		30.9	34.9	29.7
Other liabilities		166.6	147.7	148.6
Deferred income tax liability		-	7.7	11.7
Subordinated liabilities and notes		235.0	235.0	235.0
Total liabilities		**13,457.1**	**12,833.3**	**11,598.5**
Equity and reserves attributable to owners of parent				
Share capital		122.0	122.0	122.0
Share premium account		1,097.9	1,097.9	1,097.9
Retained earnings		398.8	508.2	502.6
Other reserves		39.3	44.2	50.1
Total equity		**1,658.0**	**1,772.3**	**1,772.6**
Total liabilities and equity		**15,115.1**	**14,605.6**	**13,371.1**

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

TESCO PERSONAL FINANCE PLC

INTERIM CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (UNAUDITED)

FOR THE SIX MONTHS ENDED 31 AUGUST 2018

	Share capital £m	Share premium £m	Retained earnings £m Restated[1]	FV/AFS reserve £m	Cash flow hedge reserve £m	Share based payment reserve £m	Total equity £m Restated[1]
Balance at 1 March 2018	**122.0**	**1,097.9**	**508.2**	**13.0**	**(0.3)**	**31.5**	**1,772.3**
Impact of initial application of IFRS 9	-	-	(166.0)	(0.5)	-	-	(166.5)
Balance at 1 March 2018 after adopting IFRS 9	**122.0**	**1,097.9**	**342.2**	**12.5**	**(0.3)**	**31.5**	**1,605.8**
Comprehensive income							
Profit for the period	-	-	56.6	-	-	-	56.6
Net fair value movement on investment securities held at FVOCI	-	-	-	(5.1)	-	-	(5.1)
Net movement on cash flow hedges	-	-	-	-	0.2	-	0.2
Share of other comprehensive expense of joint venture	-	-	-	(0.1)	-	-	(0.1)
Total comprehensive income	**-**	**-**	**56.6**	**(5.2)**	**0.2**	**-**	**51.6**
Transactions with owners							
Share based payments	-	-	-	-	-	0.6	0.6
Total transactions with owners	**-**	**-**	**-**	**-**	**-**	**0.6**	**0.6**
Balance at 31 August 2018	**122.0**	**1,097.9**	**398.8**	**7.3**	**(0.1)**	**32.1**	**1,658.0**
Balance at 1 March 2017	122.0	1,097.9	419.7	18.0	(0.6)	27.0	1,684.0
Comprehensive income							
Profit for the period	-	-	82.9	-	-	-	82.9
Net gains on AFS investment securities	-	-	-	2.1	-	-	2.1
Net movement on cash flow hedges	-	-	-	-	0.1	-	0.1
Share of other comprehensive income of joint venture	-	-	-	0.1	-	-	0.1
Total comprehensive income	**-**	**-**	**82.9**	**2.2**	**0.1**	**-**	**85.2**
Transactions with owners							
Share based payments	-	-	-	-	-	3.4	3.4
Total transactions with owners	**-**	**-**	**-**	**-**	**-**	**3.4**	**3.4**
Balance at 31 August 2017	**122.0**	**1,097.9**	**502.6**	**20.2**	**(0.5)**	**30.4**	**1,772.6**

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

INTERIM CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (UNAUDITED)

FOR THE SIX MONTHS ENDED 31 AUGUST 2018

	Note	6 months ended 31 August 2018 £m	6 months ended 31 August 2017 Restated[1] £m
Operating Activities			
Profit before tax		**83.0**	110.4
Adjusted for:			
Non-cash items included in operating profit before taxation and other adjustments		128.0	129.4
Changes in operating assets and liabilities		(70.6)	(51.8)
Income taxes paid		(35.1)	(13.9)
Cash flows generated from operating activities		**105.3**	174.1
Investing Activities			
Purchase of intangible assets and property, plant and equipment		(14.8)	(29.4)
Purchase of investment securities classified as FVOCI/AFS		(318.4)	(62.2)
Sale of investment securities classified as FVOCI/AFS		553.7	69.4
Dividends received from joint venture		10.3	-
Investment in joint venture		-	(15.5)
Redemption of subordinated debt issued by joint venture		5.2	-
Cash flows generated from/(used in) investing activities		**236.0**	(37.7)
Financing Activities			
Principal repayments on debt securities in issue	11	(425.0)	(150.0)
Interest paid on debt securities in issue		(12.8)	(11.8)
Interest received on assets held to hedge debt securities in issue		1.8	1.7
Interest paid on subordinated liabilities and notes		(2.4)	(2.0)
Cash flows used in financing activities		**(438.4)**	(162.1)
Net decrease in cash and cash equivalents		**(97.1)**	(25.7)
Cash and cash equivalents[2] at beginning of period		**1,303.5**	788.7
Cash and cash equivalents[2] at end of period		**1,206.4**	763.0

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

2 Cash and cash equivalents comprise cash and balances with central banks, excluding mandatory reserve deposits of £26.5m (August 2017: £15.2m).

The Interim Condensed Consolidated Financial Statements for the six months ended 31 August 2018 were approved by the Board of Directors on 1 October 2018.

1. Basis of Preparation

The Interim Condensed Consolidated Financial Statements have been prepared in accordance with the Disclosure and Transparency Rules of the Financial Conduct Authority (FCA) and with International Accounting Standard (IAS) 34 'Interim Financial Reporting' as endorsed by the European Union (EU).

Unless otherwise stated, the accounting policies applied are consistent with those described in the Consolidated Financial Statements of the Group for the year ended 28 February 2018. The Interim Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements of the Group for the year ended 28 February 2018, which have been prepared in accordance with International Financial Reporting Standards (IFRS) and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) of the International Accounting Standards Board (IASB) as endorsed by the EU.

In preparing these Interim Condensed Consolidated Financial Statements, the estimates, judgements and assumptions involved in the Group's accounting policies were the same as those which applied to the Consolidated Financial Statements for the year ended 28 February 2018, except as set out below.

These Interim Condensed Consolidated Financial Statements have been reviewed, not audited, and do not constitute Statutory Financial Statements as defined in section 434 of the Companies Act 2006. The Consolidated Financial Statements for the year ended 28 February 2018 were approved by the Board of Directors on 9 April 2018 and have been filed with the Registrar of Companies. The report of the auditors on those Financial Statements was unqualified, did not contain an emphasis of matter paragraph and did not contain any statement under section 498 of the Companies Act 2006.

Going concern

The Directors have completed an assessment of the Group's going concern status, taking into account both current and projected performance, including projections for the Group's capital and funding position and having regard to the Group's risk profile. As a result of this assessment, the Directors consider the Group to be in a satisfactory financial position and have a reasonable expectation that the Group has adequate resources to continue in business for the foreseeable future. Accordingly, the Directors continue to adopt the going concern basis in preparing the Interim Condensed Consolidated Financial Statements.

Adoption of new and amended IFRS

There are a number of new accounting standards which will impact the Group in future reporting periods. Further details of these are included in the Consolidated Financial Statements of the Group for the year ended 28 February 2018.

During the period to 31 August 2018, the Group has adopted the following new accounting standards and amendments to standards which became effective with relevant EU endorsement for annual periods beginning on or after 1 January 2018:

IFRS 9 'Financial instruments'

IFRS 9 is a replacement for IAS 39 'Financial instruments: Recognition and measurement', excluding the part of IAS 39 related to macro hedge accounting. Macro hedge accounting requirements are out of the scope of IFRS 9 and instead the IASB is developing a separate model. Entities are therefore permitted to continue accounting for macro hedge portfolios in line with IAS 39. In line with Tesco PLC policy, the Group has adopted IFRS 9 in respect of its micro hedge accounting from 1 March 2018. The Group continues to apply the existing hedge accounting requirements of IAS 39 for its portfolio hedge accounting until the new macro hedge accounting standard is implemented.

1. Basis of Preparation (continued)

IFRS 9 'Financial instruments' (continued)

The classification and measurement and impairment requirements of IFRS 9 have been applied retrospectively at 1 March 2018 by adjusting the opening balance sheet, with no requirement to restate comparative periods. Hedge accounting relationships within the scope of IFRS 9 have transitioned prospectively.

Further details on the impact of adoption of IFRS 9 are included in note 2.

IFRS 15 'Revenue from contracts with customers'

IFRS 15 introduces a performance-based approach to revenue recognition and is applicable to all contracts with customers, with certain exceptions. Both the Group's interest income and fee income integral to financial instruments fall outside the scope of IFRS 15 and are accounted for in line with the other applicable standards, predominantly IFRS 9 from 1 March 2018 (refer above). All other fees and commissions income falls within the scope of IFRS 15.

In accordance with the transitional provisions in IFRS 15 the new rules have been applied fully retrospectively and comparatives for the 2018 financial year have been restated.

Further details on the impact of adoption of IFRS 15 are included in note 2.

Amendments to IFRS 15 'Clarifications to IFRS 15, 'Revenue from contracts with customers'

These amendments clarify how the principles of IFRS 15 should be applied in determining recognition of contract revenue and provide transitional relief on modified and completed contracts for entities implementing the standard.

The impact of these amendments is included in the details on the full adoption of IFRS 15 above.

Amendments to IFRS 4 'Applying IFRS 9, 'Financial instruments', with IFRS 4, 'Insurance contracts'

These amendments permit insurance entities to adopt certain transitional arrangements to address the temporary accounting consequences of the different effective dates of IFRS 9 and IFRS 17, 'Insurance contracts'. These amendments have impacted the Group's share of results from its joint venture, Tesco Underwriting Limited (TU). As permitted by these amendments, TU has deferred the adoption of IFRS 9 until 2021. Additional disclosures for TU required as a result of this will be included in the year end financial statements of the Group at 28 February 2019.

Amendments to IAS 28 'Measuring an associate or joint venture at fair value'

These amendments are part of the Annual Improvements 2014-2016 process. They clarify that the option for a venture capital organisation and other similar entities to measure investments in associates and joint ventures at fair value through profit and loss is available separately for each associate or joint venture, and that election should be made at initial recognition. There has been no impact on the Group of the adoption of these amendments.

Amendments to IFRS 2 'Classification and measurement of share-based payment transactions'

These amendments clarify how to account for certain types of share-based payment transactions. There has been no impact on the Group of the adoption of these amendments.

IFRIC 22 'Foreign currency transactions and advance consideration'

This IFRIC clarifies the accounting for advance consideration in a transaction that is denominated in a foreign currency. There has been no impact on the Group of the adoption of this IFRIC.

1. Basis of Preparation (continued)

Change in presentation

During the period, the Group reclassified interest expense and similar charges relating to derivative financial instruments to interest and similar income. This reclassification more appropriately reflects within the Consolidated Income Statement the net impact of hedging activity on the interest income or expense of the hedged item. Prior period comparatives have been restated to align to the current period approach. The impact on the Consolidated Income Statement is as follows:

Line item	Total as previously stated	Adjusted	Restated total
	£m	£m	£m
Interest and similar income	331.1	(17.5)	313.6
Interest expense and similar charges	(87.5)	17.5	(70.0)
	243.6	-	243.6

2. Transition to IFRS 9 and IFRS 15

On 1 March 2018 the Group adopted both IFRS 9 and IFRS 15. Full transition disclosures and details of the new accounting policies applied since this date are set out below.

IFRS 9 'Financial instruments'

a) Accounting policies

Financial instruments

The Group classifies a financial instrument as a financial asset, financial liability or an equity instrument in accordance with the substance of the contractual arrangement. An instrument is classified as a liability if it creates a contractual obligation to deliver cash or another financial asset, or to exchange financial assets or financial liabilities on potentially unfavourable terms. An instrument is classified as equity if it evidences a residual interest in the assets of the Group after the deduction of liabilities.

Financial assets

Classification and measurement

The Group classifies its financial assets in the following categories:

- Fair value through profit or loss (FVPL);
- Fair value through other comprehensive income (FVOCI); and
- Amortised cost.

Management determine the classification of the Group's financial assets at initial recognition. Purchases and sales of financial assets are recognised on the trade date – the date on which the Group commits to purchase or sell the asset.

All financial assets are measured at initial recognition at fair value, plus transaction costs for those classified as FVOCI and amortised cost. Transaction costs on financial assets classified as FVPL are recognised in the Consolidated Income Statement at the time of initial recognition.

Classification and subsequent measurement of financial assets depend on:

- the Group's business model for managing the financial asset; and
- the cash flow characteristics of the financial asset.

The business model reflects how the Group manages its financial assets in order to generate cash flows and is determined by whether the Group's objective is solely to collect contractual cash flows from the assets or to collect both contractual cash flows and cash flows arising from the sale of assets. If neither of these models applies, the financial assets are classified at FVPL.

2. Transition to IFRS 9 and IFRS 15 (continued)

In determining the business model, the Group considers past experience in collecting cash flows, how the performance of these financial assets is evaluated and reported to Management and how risks are assessed.

Where the business model is to hold financial assets to collect contractual cash flows or to collect contractual cash flows and sell the assets, the Group assesses whether the financial asset's cash flows represent solely payments of principal and interest (the SPPI test). When making this assessment, the Group considers whether the contractual cash flows are consistent with a basic lending arrangement.

Financial assets at amortised cost

Financial assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest, and that are not designated as FVPL, are classified and subsequently measured at amortised cost. The carrying value of these financial assets is adjusted by any impairment loss allowance recognised and measured as described below.

Financial assets at FVOCI

Financial assets that are held for collection of contractual flows and for selling the assets, where those cash flows represents solely payment of principal interest, and that are not designated at FVPL, are classified and subsequently measured at FVOCI. The Group holds investments in debt securities which are classified as FVOCI. Movements in the carrying amount of debt securities classified at FVOCI are taken through OCI, except for the recognition of impairment gains or losses, interest revenue using the effective interest rate (EIR) method and foreign exchange gains and losses, which are recognised through the Consolidated Income Statement. When these debt securities are derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to the Consolidated Income Statement.

The Group also holds an investment in equity securities which has been irrevocably designated by Management at FVOCI at original recognition. Movements in the carrying amount of these equity securities are taken through OCI and are not subsequently reclassified to the Consolidated Income Statement, including on disposal. Impairment losses on these securities are not recognised separately from other changes in fair value.

For financial assets at FVOCI which are in fair value hedge relationships, the element of the fair value movement which relates to the hedged risk is recycled to the Consolidated Income Statement.

Financial assets at FVPL

Financial assets that do not meet the criteria for recognition at amortised cost or at FVOCI are measured at FVPL.

Impairment

The Group assesses on a forward-looking basis the expected credit losses (ECLs) associated with its financial assets carried at amortised cost and FVOCI, and with the exposure arising from loan commitments. The Group recognises a loss allowance for such losses at each reporting date. The measurement of ECLs reflects:

- An unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- The time value of money; and
- Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

Refer to section (b) below for further details on the calculation of the allowance for ECLs.

2. Transition to IFRS 9 and IFRS 15 (continued)

Financial liabilities

Classification and measurement

All of the financial liabilities held by the Group, other than derivative financial liabilities, are classified and measured at amortised cost using the EIR method, after initial recognition at fair value. Fair value is calculated as the issue proceeds, net of premiums, discounts and transaction costs incurred. For financial liabilities in fair value hedge relationships, the carrying value is adjusted by the hedged item (the fair value of the underlying hedged risk) through the Consolidated Income Statement.

Derivative financial liabilities are classified and measured at FVPL. Further information on the classification and measurement of derivative financial instruments is set out below.

Derecognition

Financial assets are derecognised when the contractual rights to receive cash flows have expired or where substantially all of the risks and rewards of ownership have been transferred and the transfer qualifies for derecognition. Financial liabilities are derecognised when they have been redeemed or otherwise extinguished.

Collateral furnished by the Group under standard repurchase agreements is not derecognised because the Group retains substantially all the risks and rewards of ownership on the basis of the predetermined repurchase price, therefore the criteria for derecognition are not met. Credit Card receivables assigned by the Group to a securitisation structured entity do not qualify for derecognition, as the Group retains substantially all the risks and rewards of ownership of the securitised Credit Card receivables.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the Company and Consolidated Statements of Financial Position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise an asset and settle a liability simultaneously.

Loan commitments

All loan commitments provided by the Group are as part of contracts that include both a loan and an undrawn commitment. As the Group cannot separately identify the expected credit losses on the undrawn commitment component from those on the loan component, the expected credit losses on the undrawn commitment are recognised together with the loss allowance for the loan.

Derivative financial instruments and hedge accounting

The Group uses derivative financial instruments for the purpose of providing an economic hedge to its exposures to interest rate and foreign exchange risks as they arise from operating, financing and investing activities. The Group does not hold or issue derivative financial instruments for trading purposes. Derivative financial instruments are initially recognised at fair value on the contract date and are remeasured at fair value at subsequent reporting dates.

Hedge accounting

The Group designates certain hedging instruments as either fair value hedges or cash flow hedges, where it is efficient to do so and the relevant criteria are met. From 1 March 2018, the Group has implemented IFRS 9 hedge accounting requirements in respect of its fair value hedges of the Group's existing portfolio of investment securities and its cash flow hedges. As permitted under IFRS 9, the Group has elected to continue to apply the existing hedge accounting requirements of IAS 39 for its portfolio hedge accounting until the new macro hedge accounting standard is implemented.

2. Transition to IFRS 9 and IFRS 15 (continued)

The Group applies hedge accounting as follows:

- Hedge relationships are classified as fair value hedges where the derivative financial instruments hedge the change in the fair value of fixed rate financial assets or financial liabilities due to movements in interest rates.
- Hedge relationships are classified as cash flow hedges where the derivative financial instruments hedge the cash flows associated with inflation risk on an index linked issued bond or the foreign currency risk on certain foreign currency invoices.

To qualify for hedge accounting, the Group documents, at the inception of the hedge: the hedging risk management strategy; the relationship between the hedging instrument and the hedged item or transaction; and the nature of the risks being hedged. The Group also documents the assessment of the effectiveness of the hedging relationship, to show that the hedge has been and will be highly effective on an ongoing basis.

Fair value hedges

Changes in the fair value of derivative financial instruments that are designated as fair value hedges are recognised in the Consolidated Income Statement. The hedged item is also adjusted for changes in fair value attributable to the hedged risk, with the corresponding adjustment made in the Consolidated Income Statement.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item is amortised to the Consolidated Income Statement over the remaining period to maturity.

Cash flow hedges

Changes in the fair value of the derivative financial instruments that are designated as hedges of future cash flows are recognised directly in OCI and the ineffective portion is recognised immediately in the Consolidated Income Statement. Amounts recognised in OCI are recycled to the Consolidated Income Statement when equivalent amounts of the hedged item are recognised in the Consolidated Income Statement.

When the hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time is recognised immediately in the Consolidated Income Statement.

b) Expected credit loss measurement

ECLs

ECLs are calculated in line with the requirements of IFRS 9 using the three stage model for impairment:

Stage 1	Financial asset is not credit impaired and has not had a significant increase in credit risk since initial recognition.
Stage 2	Financial asset is not credit impaired but has had a significant increase in credit risk since initial recognition.
Stage 3	Financial asset is credit impaired.

The measurement of ECLs is dependent on the classification stage of the financial asset. For financial assets in Stage 1, loss allowances are calculated based on ECLs arising from default events that are possible within 12 months from the reporting date. For financial assets in Stages 2 and 3, loss allowances are calculated based on lifetime ECLs.

The measurement of ECLs for financial assets measured at amortised cost and FVOCI is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour. A number of significant judgements are also required in applying the accounting requirements for measuring ECLs.

The sections below provide further explanations of the factors taken into account in the measurement of ECLs.

2. Transition to IFRS 9 and IFRS 15 (continued)

Significant increase in credit risk

At each reporting date, the change in credit risk of the financial asset is observed using a set of quantitative and qualitative criteria, together with a backstop based on arrears status.

Quantitative criteria:

For each financial asset, the lifetime probability of default (PD) at the reporting date has increased by more than a predetermined threshold set by the Group relative to the lifetime PD as expected at initial recognition.

Qualitative criteria:

A number of qualitative criteria are in place such as:

- Forbearance offered to distressed borrowers;
- Risk based pricing post-origination;
- Credit limit decrease; and
- Pre-delinquency information.

Backstop

As a backstop, the Group considers that if an account's contractual payments are more than 30 days past due then a significant increase in credit risk has taken place.

The Group has used the low credit risk exemption in respect of its portfolio of investment securities in the period ended 31 August 2018.

Definition of default

An account is deemed to have defaulted when it meets one or more of the following criteria:

Quantitative criteria:

An account's contractual payments are more than 90 days past due.

Qualitative criteria:

There are indications that the customer is in significant financial difficulty as they meet unlikeliness to pay criteria. These are instances where:

- The customer is insolvent;
- It has become probable the customer will become bankrupt; or
- The customer is deceased.

An instrument is considered to no longer be in default when it no longer meets any of the default criteria and has remained up-to-date on its contractual payments for a period of at least three months.

Inputs, assumptions and techniques used for estimating impairment

ECLs are determined by multiplying together the Probability of Default (PD), exposure at default (EAD) and loss given default (LGD) for the relevant time period and for each collective segment and by discounting back to the balance sheet date. Each of these inputs is explained further below.

Probability of default: Represents the likelihood a customer will default over the relevant period, being either 12 months or expected lifetime.

Exposure at default: Represents the expected amount due from the customer at the point of default. The Group derives the EAD from the current exposure to the counterparty and potential future changes to that exposure to the point of default.

Loss given default: Represents the Group’s expectation of the extent of the loss if there is a default. The LGD assumes that once an account has defaulted, the portion of the defaulted balance will be recovered over a maximum period of 60 months from the point of default. LGD models take into account, when relevant, the valuation of collateral, collection strategies and receipts from contracted debt sales.

These inputs are adjusted to reflect forward-looking information as described below.

2. Transition to IFRS 9 and IFRS 15 (continued)

Expected lifetime

The expected lifetime of a financial asset is the contractual term. In the case of revolving products, the Group measures credit losses over the period that it will be exposed to credit risk. This is estimated using historic customer data.

Incorporation of forward-looking information

The ECLs calculation and the measurement of significant deterioration in credit risk both incorporate forward-looking information using a range of macro-economic scenarios. The key economic variables are based on historic patterns observed over a range of economic cycles.

The Group has engaged a third party supplier to provide relevant economic data for this purpose which, prior to incorporation into the ECL calculation, is subject to internal review and challenge with reference to other publicly available market data and benchmarks. From this data, a base case scenario has been developed, together with two additional scenarios, each of which have been assigned a relative probability. The base case represents an estimate of the most-likely outcome whilst the other scenarios represent more optimistic and more pessimistic outcomes. These have been assigned weightings of 40%, 30% and 30% respectively, which is considered to be appropriate for the calculation of unbiased ECLs.

The economic scenarios used at 31 August 2018 include the following ranges of key indicators:

		5 Year Average
Bank of England base rate[1]	Base	1.40%
	Upside	1.10%
	Downside	1.97%
Unemployment rate[1]	Base	4.50%
	Upside	4.46%
	Downside	4.79%
House price index[2]	Base	3.79%
	Upside	5.37%
	Downside	3.08%
Gross domestic product[2]	Base	1.59%
	Upside	1.94%
	Downside	1.16%

[1] Simple average.

[2] Annualised growth rates.

Grouping of instruments for losses measured on a collective basis

For ECL provisions modelled on a collective basis, a grouping of exposures is performed on the basis of shared credit risk characteristics that include instrument type and credit risk gradings. The groupings are subject to regular review to ensure that these remain appropriate.

2. Transition to IFRS 9 and IFRS 15 (continued)

c) Transition disclosures

Classification and measurement of financial instruments

The measurement category and the carrying amount of financial assets and liabilities in accordance with IAS 39 and IFRS 9 at 1 March 2018 are as follows:

	IAS 39 Classification and measurement category	Carrying amount	IFRS 9 Classification and measurement category	Carrying amount
Financial assets		£m		£m
Cash and balances with central banks	Loans and receivables (amortised cost)	1,318.6	Amortised cost	1,296.7
			FVPL[a]	21.9
Loans and advances to customers	Loans and receivables (amortised cost)	11,522.4	Amortised cost	11,299.1
Derivative financial instruments	Derivatives held for hedging	46.1	FVPL	46.1
Investment securities:				
AFS	AFS	925.4	FVOCI- mandatory[b]	923.4
			FVOCI- designated[c]	2.0
Loans and receivables	Loans and receivables (amortised cost)	34.1	Amortised cost	33.9
Other assets	Loans and receivables (amortised cost)	280.6	Amortised cost	280.6
Total financial assets		**14,127.2**		**13,903.7**
Financial liabilities				
Deposits from banks	Amortised cost	1,539.0	Amortised cost	1,539.0
Deposits from customers	Amortised cost	9,248.0	Amortised cost	9,248.0
Debt securities in issue	Amortised cost	1,347.6	Amortised cost	1,347.6
Derivative financial instruments	Derivatives held for hedging	88.4	FVPL	88.4
Other liabilities	Amortised cost	147.7	Amortised cost	147.7
Subordinated liabilities	Amortised cost	235.0	Amortised cost	235.0
Total financial liabilities		**12,605.7**		**12,605.7**

The following explains how applying the new classification requirements of IFRS 9 led to changes in classification of certain financial assets held by the Group as shown in the table above.

(a) Reclassification of cash balances from amortised cost to FVPL

Cash balances relating to the Group's travel money offering have been reclassified at FVPL under IFRS 9 as these are held to earn fee and commission income and not solely to collect payments of principal and interest.

(b) Mandatory reclassification of debt investment securities from AFS to FVOCI

Debt instruments previously classified as AFS under IAS 39 have been reclassified to the FVOCI category under IFRS 9 as the IAS 39 category has been removed. There has been no change in the measurement basis as a result of this reclassification.

(c) Designation of equity investment securities from AFS to FVOCI

The Group has elected to designate equity instruments held in VISA Inc. at FVOCI as permitted by IFRS 9. These securities were previously classified as AFS. There has been no change in the measurement basis as a result of this reclassification. The changes in fair value of these securities will no longer be reclassified to the Consolidated Income Statement on disposal.

2. Transition to IFRS 9 and IFRS 15 (continued)

Reconciliation of Statement of Financial Position balances from IAS 39 to IFRS 9

The following table reconciles the carrying amount of financial assets from their previous measurement category in accordance with IAS 39 to their new measurement categories upon transition to IFRS 9 on 1 March 2018. There were no changes to the classification and measurement of financial liabilities.

	IAS 39 carrying amount 28 February 2018 £m	Reclassification £m	Remeasurement £m	IFRS 9 carrying amount 1 March 2018 £m
Financial Assets				
Amortised cost				
Cash and balances with central banks				
- Opening balance under IAS 39	1,318.6			
- Reclassification to FVPL		(21.9)		
- Closing balance under IFRS 9				1,296.7
Loans and advances to customers				
- Opening balance under IAS 39	11,522.4			
- Remeasurement: ECL allowance			(228.1)	
- Remeasurement: Recoverable asset balance			4.8	
- Closing balance under IFRS 9				11,299.1
Investment securities - amortised cost				
- Opening balance under IAS 39	34.1			
- Remeasurement: ECL allowance			(0.2)	
- Closing balance under IFRS 9				33.9
Other assets				
- Opening balance under IAS 39 and closing balance under IFRS 9	280.6			280.6
Total financial assets measured at amortised cost	**13,155.7**	**(21.9)**	**(223.5)**	**12,910.3**
FVPL				
Derivative financial instruments				
- Opening balance under IAS 39 and closing balance under IFRS 9	46.1			46.1
Cash and balances with central banks				
- Opening balance under IAS 39	-			
- Reclassification from amortised cost		21.9		
- Closing balance under IFRS 9				21.9
Total financial assets measured at FVPL	**46.1**	**21.9**	**-**	**68.0**

2. Transition to IFRS 9 and IFRS 15 (continued)

Reconciliation of Statement of Financial Position balances from IAS 39 to IFRS 9 (continued)

	IAS 39 carrying amount 28 February 2018 £m	Reclassification £m	Remeasurement £m	IFRS 9 carrying amount 1 March 2018 £m
FVOCI				
Investment securities - AFS				
- Opening balance under IAS 39	925.4			
- Reclassification to FVOCI (debt)		(923.4)		
- Reclassification to FVOCI (equity)		(2.0)		
- Closing balance under IFRS 9				-
Investment securities - FVOCI				
- Opening balance under IAS 39	-			
- Reclassification from AFS (debt)		923.4		
- Reclassification from AFS (equity)		2.0		
- Closing balance under IFRS 9				925.4
Total financial assets measured at FVOCI	**925.4**	**-**	**-**	**925.4**

The Group recognised a deferred tax asset of £57.0m on 1 March 2018 in relation to the transitional measurement adjustments set out in the above tables.

Reconciliation of impairment allowance balance from IAS 39 to IFRS 9

The following tables reconcile the prior period's closing impairment allowance measured in accordance with the IAS 39 incurred loss model to the new impairment allowance measured in accordance with the IFRS 9 expected loss model at 1 March 2018:

	28 February 2018 Loan loss allowance under IAS 39 £m	Reclassification £m	Remeasurement £m	1 March 2018 Loan loss allowance under IFRS 9 £m
Measurement category				
Loans and receivables (IAS 39)/ Financial assets at amortised cost (IFRS 9)				
Loans and advances to customers	238.1	-	228.1	466.2
Investment securities	-	-	0.2	0.2
Total	**238.1**	**-**	**228.3**	**466.4**
AFS financial assets (IAS 39)/Financial assets at FVOCI (IFRS 9)				
Investment securities[1]	-	-	(0.5)	(0.5)
Total	**-**	**-**	**(0.5)**	**(0.5)**

[1] The above loss allowance is not recognised in the carrying amount of investment securities as the carrying amount is their fair value.

2. Transition to IFRS 9 and IFRS 15 (continued)

d) Credit risk management

Maximum exposure to credit risk

The table below provides details of the credit quality of financial assets for which an ECL allowance is recognised. This represents a worst case scenario of credit risk exposure at the half-year end. For financial assets, the balances are based on gross carrying amounts as reported in the Consolidated Statement of Financial Position. For loan commitments, the amounts in the table represent the amounts for which the Group is contractually committed.

As at 31 August 2018	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Gross Exposure	**£m**	**£m**	**£m**	**£m**
Loans and advances to customers	11,320.2	1,067.1	241.3	12,628.6
Investment securities at FVOCI	686.6	-	-	686.6
Investment securities at amortised cost	28.9	-	-	28.9
Loan commitments[1]	12,186.9	154.2	1.5	12,342.6
Total gross exposure	**24,222.6**	**1,221.3**	**242.8**	**25,686.7**

As at 31 August 2018				
Loss Allowance				
Loans and advances to customers	92.0	219.7	161.0	472.7
Investment securities at FVOCI[2]	(0.1)	-	-	(0.1)
Investment securities at amortised cost	0.2	-	-	0.2
Total loss allowance	**92.1**	**219.7**	**161.0**	**472.8**

[1] The loss allowance in respect of loan commitments is included within the total loss allowance for loans and advances to customers as above.

[2] The loss allowance for investment securities at FVOCI is not recognised in the carrying amount of investment securities as the carrying amount is their fair value.

2. Transition to IFRS 9 and IFRS 15 (continued)

Credit risk: Loss allowance

The following table explains the movements in the loss allowance in the period:

	Stage 1	Stage 2	Stage 3	Total
	£m	£m	£m	£m
Loans and advances to customers				
At 1 March 2018	101.5	213.7	151.0	466.2
Transfers:				
- Transfer from Stage 1 to Stage 2	(10.7)	10.7	-	-
- Transfer from Stage 2 to Stage 1	36.9	(36.9)	-	-
- Transfer to Stage 3	(1.2)	(29.5)	30.7	-
- Transfers from Stage 3	0.9	1.4	(2.3)	-
New financial assets originated or purchased	19.4	7.5	1.0	27.9
Financial assets derecognised during the period	(6.0)	(5.9)	(31.1)	(43.0)
Write-offs	-	-	(52.9)	(52.9)
Change in risk parameters and other movements[1]	(48.8)	58.7	64.6	74.5
At 31 August 2018	92.0	219.7	161.0	472.7
Investment securities at FVOCI				
At 1 March 2018	(0.5)	-	-	(0.5)
New financial assets originated or purchased	0.1	-	-	0.1
Financial assets derecognised during the period	0.3	-	-	0.3
At 31 August 2018	(0.1)	-	-	(0.1)
Investment securities at amortised cost				
At 1 March 2018	0.2	-	-	0.2
At 31 August 2018	0.2	-	-	0.2

[1] Includes net remeasurement following transfer of stage.

2. Transition to IFRS 9 and IFRS 15 (continued)

IFRS 15 'Revenue from contracts with customers'

a) Accounting policies

Revenue recognition

Net fees and commissions income recognition

The Group generates fees from banking services, primarily Credit Card interchange fees. Fees in respect of banking services are recognised in line with the satisfaction of performance obligations. This can be either at a point in time or over time, in line with the provision of the service to the customer.

The majority of banking services are performed at a point in time and payment is due from a customer at the time a transaction takes place. For services performed over time, payment is generally due monthly in line with the satisfaction of performance obligations.

The costs of providing these banking services are incurred as the services are rendered. The price is usually fixed and always determinable.

The Group also generates commission from the sale and service of Motor and Home insurance policies underwritten by TU or, in a minority of cases, by a third party underwriter. This is based on commission rates which are independent of the profitability of underlying insurance policies. Similar commission income is also generated from the sale of white label insurance products underwritten by other third party providers. This commission income is recognised on a net basis as such policies are sold, in line with the satisfaction of performance obligations to customers.

In the case of certain commission income on insurance policies managed and underwritten by a third party, the Group recognises commission income from policy renewals as such policies are sold. This is when the Group has satisfied all of its performance obligations in relation to the policy sold and it is considered highly probable that a significant reversal in the amount of revenue recognised will not occur in future periods. This calculation takes into account both estimates of future renewal volumes and renewal commission rates. A contract asset is recognised in relation to this revenue. This is unwound over the remainder of the contract with the customer, in this case being the third party insurance provider.

The end policyholders have the right to cancel an insurance policy at any time. Therefore, a contract liability is recognised for the amount of any expected refunds due and the revenue recognised in relation to these sales is reduced accordingly. This contract refund liability is estimated using prior experience of customer refunds. The appropriateness of the assumptions used in this calculation is reassessed at each reporting date.

b) Transition disclosures and restatement

Changes arising from the adoption of IFRS 15

There are two changes for the Group as a result of the adoption of IFRS 15.

(i) Accounting for insurance renewal commission income

Prior to the adoption of IFRS 15, the Group recognised all insurance commission income on policy renewals at the time of the renewal. Under IFRS 15, the Group recognises commission income as policies are sold for a minority of insurance policies managed and underwritten by a third party. This is the point in time at which the Group has satisfied all of its performance obligations in relation to the policies sold and it is considered highly probable that a significant reversal in the amount of revenue recognised will not occur in future periods. A contract asset has been recognised in relation to this revenue and is included within other assets.

(ii) Presentation of insurance refund liability

Contract liabilities in relation to expected refunds to insurance customers were previously presented as provisions for liabilities and charges. These are now included within other liabilities to reflect the terminology and requirements of IFRS 15.

2. Transition to IFRS 9 and IFRS 15 (continued)

Restatement

In accordance with the transitional provisions of IFRS 15, the new rules have been applied fully retrospectively and comparatives for the 2018 financial year have been restated.

The impact of these changes on the relevant financial statement lines is as follows:

	As previously reported	IFRS 15 adjustments	Restated
At 1 March 2017	**£m**	**£m**	**£m**
Statement of Financial Position			
Other assets	299.1	18.5	317.6
Provision for liabilities and charges	(83.5)	4.2	(79.3)
Other liabilities	(148.3)	(4.2)	(152.5)
Deferred income tax liability	(13.7)	(5.0)	(18.7)
Retained earnings	(406.2)	(13.5)	(419.7)
At 31 August 2017			
Statement of Financial Position			
Other assets	295.3	16.7	312.0
Provision for liabilities and charges	(70.8)	3.8	(67.0)
Other liabilities	(144.8)	(3.8)	(148.6)
Deferred income tax liability	(7.2)	(4.5)	(11.7)
Retained earnings	(490.4)	(12.2)	(502.6)
Income Statement			
Fee and commission income	200.0	(1.8)	198.2
Income tax charge	(28.0)	0.5	(27.5)
Statement of Cash Flows			
Non-cash items included in operating profit before taxation and other adjustments	136.2	(6.8)	129.4
Changes in operating assets and liabilities	(60.4)	8.6	(51.8)
At 28 February 2018			
Statement of Financial Position			
Other assets	265.7	14.9	280.6
Provisions for liabilities and charges	(79.4)	3.4	(76.0)
Other liabilities	(144.3)	(3.4)	(147.7)
Deferred income tax liability	(3.7)	(4.0)	(7.7)
Retained earnings	(497.3)	(10.9)	(508.2)
Income Statement			
Fee and commission income	387.0	(3.5)	383.5
Income tax charge	(61.6)	1.0	(60.6)
Statement of Cash Flows			
Non-cash items included in operating profit before taxation and other adjustments	297.4	(12.8)	284.6
Changes in operating assets and liabilities	46.9	16.3	63.2

3. Segmental Reporting

Following the measurement approach of IFRS 8, 'Operating segments', the Group's operating segments are reported in accordance with the internal reporting provided to the Board of Directors, which is responsible for allocating resources to the operating segments and assessing their performance.

The Group has one operating segment covering all of the Group's activities, the results of which are set out in the Condensed Consolidated Income Statement and Condensed Consolidated Statement of Financial Position.

There are no significant seasonal fluctuations that affect the Group's results.

4. Net Interest Income

	6 months ended 31 August 2018 £m	6 months ended 31 August 2017 £m Restated[1]
Interest and similar income		
On financial assets measured at amortised cost		
Loans and advances to customers	345.2	308.7
Cash and balances with central banks	3.9	0.9
Investment securities	0.7	0.7
	349.8	310.3
On financial assets measured at fair value		
Investment securities	2.6	2.3
Derivative financial instruments	1.8	1.0
	4.4	3.3
Total interest and similar income	**354.2**	**313.6**
Interest expense and similar charges		
On financial liabilities measured at amortised cost		
Deposits from customers	(67.0)	(55.0)
Deposits from banks	(4.7)	(1.1)
Debt securities in issue	(12.8)	(12.0)
Subordinated liabilities and notes	(2.3)	(1.9)
Total interest expense and similar charges	**(86.8)**	**(70.0)**
Net interest income	**267.4**	**243.6**

[1] The prior period restatement relates to the reclassification of amounts from interest expense to interest income. Refer to note 1 for further details.

5. Net Fees and Commissions Income

	6 months ended 31 August 2018 £m	6 months ended 31 August 2017 £m Restated[1]
Fees and commissions income		
Banking revenue from contracts with customers	126.8	125.1
Insurance revenue from contracts with customers	45.6	60.1
Other revenue from contracts with customers	15.2	13.0
Total fees and commissions income	**187.6**	**198.2**
Fees and commissions expense		
Banking expense	(16.8)	(15.5)
Total fees and commissions expense	**(16.8)**	**(15.5)**
Net fees and commissions income	**170.8**	**182.7**

With the exception of other revenue from contracts with customers, all of the above fees and commissions relate to financial assets and financial liabilities measured at amortised cost. These figures exclude amounts incorporated in determining the EIR on such financial assets and financial liabilities.

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

6. Impairment Loss on Financial Assets

	6 months ended 31 August 2018 £m	6 months ended 31 August 2017 £m
Impairment loss on loans and advances to customers	89.8	69.9
Impairment loss on investment securities at FVOCI	0.4	n/a
Impairment loss on investment securities at amortised cost	-	n/a
Total impairment loss on financial assets	**90.2**	**69.9**

7. Income Tax

The tax charge in the Interim Condensed Consolidated Income Statement is based on Management's best estimate of the full year effective tax rate based on expected full year profits to 28 February 2019.

Income tax on the Group's profit for the period is a charge of £26.4m (2017: £27.5m)[1]. The Group's current effective tax rate is higher than the statutory rate principally due to the non-deductibility of the additional PPI charge and regulatory provision recognised in the period. No Group Relief is anticipated in the current year.

The March 2016 Budget Statement included an announcement that the standard rate of corporation tax in the United Kingdom (UK) would be reduced to 17% from 1 April 2020. This rate reduction was enacted during the year ended 28 February 2017 and is therefore incorporated in these Financial Statements. The rate change is expected to reduce the Group's effective tax rate in the medium term.

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

8. Capital Expenditure and Commitments

In the six months ended 31 August 2018 there were additions to property, plant and equipment and intangible assets of £12.7m (August 2017 £25.5m). Commitments for capital expenditure contracted for but not provided at 31 August 2018 were £nil (February 2018: £nil) on property, plant and equipment and £0.4m (February 2018: £1.1m) on intangible assets.

The Group's Management are confident that future net revenues and funding will be sufficient to cover these commitments.

9. Loans and Advances to Customers

	31 August 2018 £m	28 February 2018 £m	31 August 2017 £m
Secured Mortgage lending	3,515.9	3,010.2	2,548.2
Unsecured lending	9,112.7	8,766.7	8,408.5
Total secured and unsecured lending	**12,628.6**	**11,776.9**	**10,956.7**
Fair value hedge adjustment	(11.5)	(16.4)	17.5
Gross loans and advances to customers	**12,617.1**	**11,760.5**	**10,974.2**
Less: allowance for impairment (refer to note 2)	(472.7)	(238.1)	(212.0)
Net loans and advances to customers	**12,144.4**	**11,522.4**	**10,762.2**

At 31 August 2018, the Group had contractual lending commitments of £12,342.6m (February 2018: £12,225.0m).

Fair value hedge adjustments

Fair value hedge adjustments amounting to £(11.5)m (February 2018: £(16.4)m) are in respect of fixed rate Loans and Mortgages. These adjustments are largely offset by derivatives, which are used to manage interest rate risk and are designated as fair value hedges within loans and advances to customers.

10. Investment in Joint Venture

During the period ended 31 August 2018, the Group's joint venture, TU, completed a share reduction. The Group has recognised its share of this distribution, being £10.3m, through a reduction in the carrying value of its investment in TU. The Group's investment in subordinated debt issued by TU has also decreased by £5.2m, reflecting the Group's share of loan capital repaid in the period.

TU has taken advantage of the optional temporary exemption from applying IFRS 9 for entities whose predominant activity is issuing contracts within the scope of IFRS 4 'Insurance Contracts' (the 'deferral approach'). This will remove the impact of potential temporary volatility in reported results for TU until the date of adoption of the new insurance standard IFRS 17 on 1 January 2021.

The Group has similarly elected to take a temporary exemption available from the requirements of IAS 28 'Investments in Associates and Joint Ventures' regarding the use of uniform accounting policies in equity accounting for a joint venture. This exemption allows the Group to equity account for the results of TU without any adjustments to reflect the impact of IFRS 9 within these Financial Statements.

11. Debt Securities in Issue

	Interest rate	Par value £m	Term (years)	Maturity date	31 August 2018 £m	28 February 2018 £m	31 August 2017 £m
Fixed rate retail bond [1]	5.2%	125.0	7.5	2018	-	126.1	127.7
RPI bond [2]	1.0%	71.0	8	2019	71.0	69.9	68.6
Fixed rate retail bond [3]	5.0%	200.0	8.5	2020	203.4	203.9	208.3
Floating rate AAA bond (A2) [4]	1M LIBOR + 0.65%	350.0	7	2021	349.8	349.6	349.4
Floating rate AAA bond (A1) [5]	1M LIBOR + 0.65%	300.0	5	2020	-	299.9	299.8
Floating rate AAA bond (A1) [6]	1M LIBOR + 0.53%	300.0	5	2022	298.4	298.2	-
					922.6	**1,347.6**	**1,053.8**

All Floating Rate Bonds were issued by Delamare Cards MTN Issuer plc and are listed on the Irish Stock Exchange. All retail bonds are listed on the London Stock Exchange.

[1] This bond was issued on 24 February 2011 and was redeemed on its maturity date in August 2019.
[2] This bond was issued on 16 December 2011.
[3] This bond was issued on 21 May 2012.
[4] This Bond was issued on 6 June 2014. The scheduled redemption date of this Bond is May 2019.
[5] This Bond was issued on 13 May 2015 and was redeemed on its scheduled redemption date in April 2018.
[6] This Bond was issued on 7 November 2017. The scheduled redemption date of this Bond is October 2020.

12. Provisions for Liabilities and Charges

	Customer Redress Provision £m	Regulatory Provision £m	Insurance Provision £m	Restructuring Provision £m	Other Provisions £m	Total £m
6 months to 31 August 2018						
At beginning of period (restated)[1]	67.7	-	-	1.1	7.2	76.0
Provided during the period	7.0	16.4	-	-	2.7	26.1
Released in the period	-	-	-	(0.5)	(1.1)	(1.6)
Utilised during the period	(27.7)	-	-	(0.4)	(2.3)	(30.4)
At end of period	**47.0**	**16.4**	**-**	**0.2**	**6.5**	**70.1**

Customer redress provision - Payment protection insurance

Of the total customer redress provision balance at 31 August 2018, £46.5m (February 2018: £66.8m) has been provided for customer redress in respect of potential customer claims arising from historic sales of PPI.

In March 2017, the FCA issued a Policy Statement (PS17/3, 'Payment protection insurance complaints: feedback on CP16/20 and final rules and guidance') which confirmed a deadline for PPI claims of August 2019, supported by an FCA led communications campaign.

The policy statement also set out rules and guidance on the handling of PPI claims in light of the Supreme Court's decision in Plevin v Paragon Personal Finance Limited (Plevin), confirming that both up-front commission arrangements and profit share arrangements should also be considered in the calculation of total commission for Plevin claims.

The Group increased its PPI provision by £7.0m during the half-year ended 31 August 2018 to reflect an updated assessment of the current claim rate and average redress.

Although a significant degree of uncertainty remains with regard to the ultimate cost of settling PPI claims, in particular the volume of claims arising from customers ahead of the FCA confirmed time bar date of August 2019 and the impact of regulatory changes, the provision balance represents Management's best estimate at the reporting date of that cost. The PPI provision will continue to be monitored as trends in claims volumes and levels of redress develop.

The table below details for each key assumption, actual data to 31 August 2018, forecast assumptions used in assessing the PPI provision adequacy and a sensitivity assessment demonstrating the impact on the provision of a variation in the future experience.

			Sensitivity	
Assumption	**Cumulative actual**	**Future expected**	**Change in assumption**	**Consequential change in provision £m**
Valid claims settled	137,862	22,809	+/- 1,000 claims	+/- 1.5
Average redress per valid claim	£1,728	£1,474	+/- £100	+/- 2.3

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

12. Provisions for Liabilities and Charges (continued)

Customer redress provision - Consumer credit act (CCA)

The Group holds a provision of £0.5m (February 2018: £0.9m) in respect of customer redress relating to instances where certain requirements of the CCA for post-contract documentation were not fully complied with.

In arriving at the provision required, the Group has considered the legal and regulatory position with respect to these matters and has sought legal advice which it took into account when making its judgement. The provision represents Management's best estimate at the reporting date of the cost of concluding the redress programme for Loan and Credit Card customers, and in making the estimate Management have exercised judgement as to both the timescale for completing the redress campaign and the final scope of any amounts payable.

Regulatory provision

In November 2016, Tesco Bank's debit cards were the subject of an online fraudulent attack. The Group's priority throughout was to ensure customers' accounts were protected and that it communicated with customers immediately and transparently, reassuring customers that there was no data loss or breach of systems. The Group undertook immediate remedial action and an independent review of the issue and has worked closely with the authorities and regulators on this incident.

On 1 October 2018, the FCA issued a warning notice to the Group in relation to the incident and the Group has accepted this and agreed to a settlement payment of £16.4m. As a result, the Group has recognised a regulatory provision for this amount at 31 August 2018. Management expect to fully utilise this provision during the year ended 28 February 2019.

Insurance provision

The insurance provision previously disclosed within this note has been reclassified to other liabilities on adoption of IFRS 15. Refer to note 2 for further details.

Restructuring provision

The restructuring provision relates to restructuring costs. Management expect to fully utilise this provision during the year ended 28 February 2019.

Other provisions

Other provisions predominantly reflect:

- a dilapidations provision related to the anticipated costs of restoring leased assets to their original condition. Management expect that the provision will be utilised at the end of the lease terms, the longest of which is due to end in 2029; and
- a warranty provision in respect of debt sales. This represents post-determination date customer receipts payable to debt purchasers and provision for any accounts which may need to be brought back under the terms of the debt sale agreements.

13. Fair Values

Classification of financial assets and liabilities

Except as detailed in the following table, the Directors consider that the carrying value amounts of financial assets and financial liabilities recorded on the Interim Condensed Consolidated Statement of Financial Position are approximately equal to their fair values.

	31 August 2018		28 February 2018		31 August 2017	
	Carrying value £m	Fair value £m	Carrying value £m	Fair value £m	Carrying value £m	Fair value £m
Financial assets:						
Loans and advances to customers	12,144.4	12,301.4	11,522.4	11,658.8	10,762.2	10,920.6
Investment securities - amortised cost	28.7	32.4	34.1	34.7	34.1	37.7
	12,173.1	**12,333.8**	**11,556.5**	**11,693.5**	**10,796.3**	**10,958.3**
Financial liabilities:						
Deposits from customers	10,073.2	10,052.6	9,248.0	9,226.9	8,896.9	8,915.5
Debt securities in issue	922.6	929.9	1,347.6	1,354.9	1,053.8	1,059.1
Subordinated liabilities	235.0	191.3	235.0	182.9	235.0	190.6
	11,230.8	**11,173.8**	**10,830.6**	**10,764.7**	**10,185.7**	**10,165.2**

The only financial assets and financial liabilities which are carried at fair value on the Interim Condensed Consolidated Statement of Financial Position at period end are cash balances relating to the Group's travel money offering, FVOCI investment securities and derivative financial instruments. The valuation techniques and inputs used to derive fair values at the period end are described below.

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. Where an active market is considered to exist, fair values are based on quoted prices. For instruments which do not have active markets, fair value is calculated using present value models, which take individual cash flows together with assumptions based on market conditions and credit spreads, and are consistent with accepted economic methodologies for pricing financial instruments.

In each case the fair value is calculated by discounting future cash flows using benchmark, observable market interest rates.

The table below categorises all financial instruments held at fair value (recurring measurement) and the fair value of financial instruments held at amortised cost according to the method used to establish the fair value disclosed.

13. Fair Values (continued)

As at 31 August 2018	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets carried at fair value				
Cash and balances with central banks[1]	-	47.7	-	47.7
Investment securities - FVOCI	684.1	-	2.6	686.7
Derivative financial instruments:				
- Interest rate swaps	-	37.9	-	37.9
- Forward foreign currency contracts	-	0.1	-	0.1
Financial assets carried at amortised cost				
Loans and advances to customers	-	-	12,301.4	12,301.4
Investment securities – amortised cost	-	32.4	-	32.4
Total	**684.1**	**118.1**	**12,304.0**	**13,106.2**
Financial liabilities carried at fair value				
Derivative financial instruments:				
- Interest rate swaps	-	48.6	-	48.6
Financial liabilities carried at amortised cost				
Deposits from customers	-	-	10,052.6	10,052.6
Debt securities in issue	929.9	-	-	929.9
Subordinated liabilities	-	191.3	-	191.3
Total	**929.9**	**239.9**	**10,052.6**	**11,222.4**

As at 28 February 2018	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets carried at fair value				
Financial assets classified as AFS	923.4	-	2.0	925.4
Derivative financial instruments:				
- Interest rate swaps	-	45.9	-	45.9
- Forward foreign currency contracts	-	0.2	-	0.2
Financial assets carried at amortised cost				
Loans and advances to customers	-	-	11,658.8	11,658.8
Investment securities – loans and receivables	-	34.7	-	34.7
Total	**923.4**	**80.8**	**11,660.8**	**12,665.0**
Financial liabilities carried at fair value				
Derivative financial instruments:				
- Interest rate swaps	-	88.3	-	88.3
- Forward foreign currency contracts	-	0.1	-	0.1
Financial liabilities carried at amortised cost				
Deposits from customers	-	-	9,226.9	9,226.9
Debt securities in issue	1,354.9	-	-	1,354.9
Subordinated liabilities	-	182.9	-	182.9
Total	**1,354.9**	**271.3**	**9,226.9**	**10,853.1**

[1] Cash balances relating to the Group's travel money offering are carried at fair value under IFRS 9.

13. Fair Values (continued)

As at 31 August 2017	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets carried at fair value				
Financial assets classified as AFS	949.3	-	1.8	951.1
Derivative financial instruments:				
Interest rate swaps	-	25.8	-	25.8
Financial assets carried at amortised cost				
Loans and advances to customers	-	-	10,920.6	10,920.6
Investment securities – loans and receivables	-	37.7	-	37.7
Total	**949.3**	**63.5**	**10,922.4**	**11,935.2**
Financial liabilities carried at fair value				
Derivative financial instruments:				
- Interest rate swaps	-	122.2	-	122.2
- Forward foreign currency contracts	-	1.3	-	1.3
Financial liabilities carried at amortised cost				
Deposits from customers	-	-	8,915.5	8,915.5
Debt securities in issue	1,059.1	-	-	1,059.1
Subordinated liabilities and notes	-	190.6	-	190.6
Total	**1,059.1**	**314.1**	**8,915.5**	**10,288.7**

Valuation Hierarchy

There are three levels to the hierarchy as follows:

Level 1

Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2

Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (for example, as prices) or indirectly (for example, derived from prices).

Fair values of cash balances relating to the Group's travel money offering are considered to equate to their carrying value as these are short term in nature.

Derivative financial instruments which are categorised as Level 2 are those which either:

- Have future cash flows which are on known dates and for which the cash flow amounts are known or calculable by reference to observable interest and foreign currency exchange rates; or
- Have future cash flows which are not pre-defined, but for which the fair value of the instrument has very low sensitivity to changes in estimate of future cash flows.

In each case the fair value is calculated by discounting future cash flows using benchmark, observable market interest rates.

FVOCI/AFS investment securities which are categorised as Level 2 are those where no active market exists or where there are quoted prices available for similar instruments in active markets.

Fair values of investment securities classified as amortised cost/loans and receivables are based on quoted prices, where available, or by using discounted cash flows applying market rates.

The estimated fair value of subordinated liabilities is calculated using a discounted cash flow model based on a current yield curve appropriate for the remaining term to maturity.

13. Fair Values (continued)

Level 3

Inputs for the asset or liability are not based on observable market data (unobservable inputs).

Loans and advances to customers are net of charges for impairment. The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates to determine fair value.

The estimated fair value of deposits from customers represents the discounted amount of estimated future cash flows expected to be paid. Expected cash flows are discounted at current market rates to determine fair value.

The estimated fair value of financial assets classified as FVOCI/AFS, being the Group's interest in VISA Inc. preferred stock, is reflected in the table on page 35. The preferred stock may be convertible into Class A Common Stock of VISA Inc. at certain future dates, the earliest point being June 2020. Conversion is contingent upon future events, principally related to the outcome of interchange litigation against VISA Europe Limited. As such, the valuation reflects both an illiquidity discount and the risk of a reduction in the conversion rate to VISA Inc. common Stock. The reduction in the conversion rate is the most significant unobservable input to the valuation.

Transfers

There were no transfers between Level 1 and Level 2 during the period (August 2017: no transfers).

There were no transfers between Level 2 and Level 3 during the period (August 2017: no transfers).

14. Capital Resources

On 27 June 2013 the final Capital Requirements Directive IV (CRD IV) rules were published in the Official Journal of the EU. Following the publication of the CRD IV rules, the Prudential Regulatory Authority (PRA) issued a policy statement on 19 December 2013 detailing how the rules will be enacted within the UK with corresponding time frames for implementation. The transitioning period came to an end in December 2017 and is reflected in prior period comparatives. On the introduction of IFRS 9 a further transitional period was introduced, allowing the Company (being the regulated entity) to phase in the IFRS 9 impact on Capital over a period of 5 years.

The Group implemented IFRS 9 from 1 March 2018. Under the transitional provisions, the impact as at 31 August 2018 on common equity tier 1 is £7.9m. Common equity tier 1 is expected to reduce by approximately 164 basis points (unaudited) on an end point basis.

The following tables analyse the regulatory capital resources of the Company applicable as at the period end on a 'transitional' and 'end point' position for the current year as related to the IFRS 9 transitional period:

	Transitional 6 months to 31 August 2018 IFRS 9 £m	End Point 6 months to 31 August 2018 IFRS 9 £m	End Point 6 months to 28 February 2018 IAS 39 £m Restated[1]	End Point 6 months to 31 August 2017 IAS 39 £m Restated[1]
Movement in common equity tier 1 capital:				
At the beginning of the period	1,502.3	1,502.3	1,394.6	1,394.6
Impact of initial application of IFRS 9	(166.0)	(166.0)	-	-
Profit attributable to shareholders	52.3	52.3	127.6	75.1
Gains and losses on liabilities arising from own credit	0.3	0.3	0.1	-
Other reserves	(4.9)	(4.9)	6.0	5.6
Ordinary dividends	(23.3)	(23.3)	(50.0)	(25.2)
IFRS 9 transitional add back	158.2	-	-	-
Movement in intangible assets	26.5	26.5	28.9	15.4
Movement in material holdings	-	-	3.4	3.4
Deferred tax liabilities related to intangible assets	(2.7)	(2.7)	(8.3)	(7.3)
At the end of the period	**1,542.7**	**1,384.5**	**1,502.3**	**1,461.6**

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

14. Capital Resources (continued)

	Transitional 31 August 2018 IFRS 9 £m	End Point 31 August 2018 IFRS 9 £m	End Point 28 February 2018 IAS 39 £m Restated[1]	End Point 31 August 2017 IAS 39 £m Restated[1]
Common equity tier 1				
Shareholders' equity (accounting capital)	1,650.4	1,650.4	1,768.9	1,765.8
Regulatory adjustments				
Unrealised gains on cash flow hedge reserve	0.1	0.1	0.3	0.4
Adjustment to own credit/Additional value adjustments	(0.7)	(0.7)	(1.1)	(1.1)
Foreseeable dividends	(23.3)	(23.3)	-	(25.2)
Intangible assets	(244.6)	(244.6)	(271.1)	(284.6)
Deferred tax liabilities related to intangible assets	2.6	2.6	5.3	6.3
IFRS 9 transitional add back	158.2	-	-	-
Common equity tier 1 capital	**1,542.7**	**1,384.5**	**1,502.3**	**1,461.6**
Tier 2 capital (instruments and provisions)				
Undated subordinated notes	45.0	45.0	45.0	45.0
Dated subordinated notes net of regulatory amortisation	190.0	190.0	190.0	190.0
Credit risk adjustment	-	-	99.1	68.9
Tier 2 capital (instruments and provisions) before regulatory adjustments	**235.0**	**235.0**	**334.1**	**303.9**
Regulatory adjustments				
Material holdings in financial sector entities	(28.7)	(28.7)	(34.1)	(34.1)
Total regulatory adjustments to tier 2 capital (instruments and provisions)	**(28.7)**	**(28.7)**	**(34.1)**	**(34.1)**
Total tier 2 capital (instruments and provisions)	**206.3**	**206.3**	**300.0**	**269.8**
Total capital	**1,749.0**	**1,590.8**	**1,802.3**	**1,731.4**
Total risk weighted assets	9,617.2	9,580.0	9,280.6	8,757.6
Common equity tier 1 ratio (unaudited)	16.0%	14.5%	16.2%	16.7%
Tier 1 ratio (unaudited)	16.0%	14.5%	16.2%	16.7%
Total capital ratio (unaudited)	18.2%	16.6%	19.4%	19.8%

Total capital requirements (TCR) refers to the amount and quality of capital the Bank must maintain to comply with the Capital Requirements Regulation (CRR) Pillar 1 and the 2A capital requirements. The TCR for Tesco Personal Finance Group Limited as at 31 August 2018 is 11.87% plus £39.0m as a static add-on for pension risk.

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

14. Capital Resources (continued)

The table below reconciles shareholders' equity of the Group to shareholders' equity of the Company:

	31 August 2018 £m	28 February 2018 £m Restated[1]	31 August 2017 £m Restated[1]
Tesco Personal Finance plc (Group) shareholders' equity	1,658.0	1,772.3	1,772.6
Share of joint venture's retained earnings	(3.9)	0.4	3.5
Subsidiaries' retained earnings	(0.1)	(0.1)	-
Share of joint venture's AFS reserve	(3.6)	(3.7)	(10.3)
Tesco Personal Finance plc (Company) shareholders' equity	**1,650.4**	**1,768.9**	**1,765.8**

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

It is the Group's policy to maintain a strong capital base, to expand it as appropriate 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, the Group has regard to the supervisory requirements of the PRA.

The Group is required to submit Internal Capital Adequacy Assessment Process (ICAAP) reports which set out future business plans, the impact on capital availability capital requirements and the risk to capital adequacy under stress scenarios, to the PRA.

The Group also maintains a Recovery Plan that provides the framework and a series of recovery options which could be deployed in a severe stress event impacting capital or liquidity positions. The Recovery Plan is reviewed and approved by the Board on at least an annual basis.

The Group has met all relevant capital requirements throughout the period.

Leverage ratio (unaudited)

The Basel III reforms include the introduction of a capital leverage measure as defined as the ratio of tier 1 capital to total exposure. This is intended to reinforce the risk based capital requirements with a simple, non-risk based 'backstop' measure.

14. Capital Resources (continued)

The Group has published the leverage ratio on a CRD IV basis using the existing exposure approach:

Exposures for leverage ratio (unaudited)	Transitional 31 August 2018 £m	End Point 31 August 2018 £m	End Point 28 February 2018 £m Restated[1]	End Point 31 August 2017 £m Restated[1]
Total balance sheet exposures	15,115.1	15,115.1	14,605.6	13,345.2
Adjustments for entities which are consolidated for accounting purposes but outside scope of regulatory consolidation	(7.5)	(7.5)	(3.5)	-
Removal of accounting value of derivatives and Securities Financing Transactions (SFTs)	(287.2)	(287.2)	(46.1)	(22.4)
Exposure value for derivatives and SFTs	41.0	41.0	12.7	10.0
Off balance sheet: unconditionally cancellable (10%)	1,204.6	1,204.6	1,219.4	1,199.1
Off balance sheet: other (20%)	59.3	59.3	41.2	46.9
Regulatory adjustment – intangible assets	(244.6)	(244.6)	(225.8)	(324.8)
Regulatory adjustment – other, including IFRS 9	(29.2)	(187.4)	-	-
Total	**15,851.5**	**15,693.3**	**15,603.5**	**14,254.0**
Common equity tier 1	**1,542.7**	**1,384.5**	**1,502.3**	**1,461.6**
Leverage ratio	**9.7%**	**8.8%**	**9.6%**	**10.3%**

The Company's estimated end point leverage ratio is 9.7% (February 2018: 9.6%).

[1] The prior period has been restated following the retrospective adoption of IFRS 15 in the current period. Refer to note 2 for further details.

Capital Management

The Group operates an integrated risk management process to identify, quantify and manage risk in the Group. The quantification of risk includes the use of both stress and scenario testing. Where capital is considered to be an appropriate mitigant for a given risk, this is identified and reflected in the Group's internal capital assessment. The capital resources of the Group are regularly monitored against the higher of this internal assessment and regulatory requirements. Capital adequacy and performance against the Group's capital plan is monitored daily, with monthly reporting provided to the Board, Asset and Liability Committee and Capital Management Forum.

Pillar 2 capital methodologies

The PRA updated its Pillar 2 capital methodologies in July 2016 following the publication of prudential requirements for implementation of ring-fencing and issued a policy statement in October 2017 refining the Pillar 2A framework.

These proposals are aimed at promoting the safety and soundness of PRA-regulated firms, to facilitate a more effective banking sector and to make the PRA's Pillar 2A capital assessment more robust and more proportionate by addressing some of the concerns over the differences between SA and internal ratings-based risk weights. This will continue to be managed as part of the Bank's ICAAP in line with the PRA policy statement issued in October 2017. The PRA general safety and soundness objectives in relation to continuity of core services in the UK and ring-fencing of Bank activities where core deposits are in excess of £25bn will be implemented from 1 January 2019.

Management forecasts indicate that the Group will not exceed this threshold and will not automatically be required to ring-fence the Group's core activities by the 2019 implementation date.

14. Capital Resources (continued)

Credit Risk

In December 2017 the Basel Committee on Banking Supervision (BCBS) finalised Basel III reforms for credit risk, including revisions to the calculation of risk weighted assets and enhancements to the robustness and risk sensitivity of the standardised approaches to credit risk, constraining the use of internal model approaches by placing limits on certain inputs and replacing the existing Basel II output floors with a more robust risk sensitive floor based on the Committees Basel III standardised approaches. The final Basel III reforms will be implemented from January 2022.

Operational risk

In December 2017, the BCBS finalised Basel III reforms for operational risk by replacing all existing approaches in the Basel II framework with a single risk-sensitive standardised approach (SA) to be used by all banks. The new SA increases the sensitivity by combining a refined measure of gross income with the banks internal historical losses. The final Basel III reforms will be implemented in January 2022.

Leverage

At present the Group has no minimum UK leverage requirement as it is currently exempt from the UK Leverage Framework Regime, which only applies to institutions with retail deposits over £50 billion or more. In December 2017, the BCBS finalised Basel III reforms for the leverage ratio. The final Basel III reforms will be implemented in January 2022. In May 2018, the EU proposed updates to the CRR which could result in a minimum leverage requirement of 3%.

The initial assessment indicate that these reforms will have a minor impact on the Group's leverage ratio.

The Group is subject to reporting and disclosure requirements under the CRR and is not currently subject to temporary modifications of the UK Leverage Framework Regime.

The European Commission's minimum requirements for own funds and eligible liabilities (MREL)

MREL requires banks to maintain at all times a sufficient aggregate amount of own funds and eligible liabilities (that may be bailed-in if required). MREL will, on full implementation, be set on a firm-specific basis and calculated as the sum of two components: a loss absorption amount, being the amount needed to absorb losses up to and in resolution; and a recapitalisation amount which reflects the capital that a firm is likely to need post resolution.

MREL is expected to be set annually over the transitional period until 1 January 2022. Prior to 31 December 2019, MREL will be equal to an institution’s minimum regulatory capital requirements. From 1 January 2020 until 31 December 2021 an interim requirement will be set, with full compliance applicable on 1 January 2022. The Group is working towards implementation of these requirements and has reflected them in its strategic plan.

15. Related Party Transactions

The Group's related party transactions during the interim period were entered into in the normal course of business. Transactions for this period are not significant to an understanding of the Group's financial position or performance, and are similar in nature to those for the year ended 28 February 2018.

16. Contingent Liabilities

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 it is not probable that an outflow of economic benefits will be required or the amount of the obligation cannot be reliably estimated.

Contingent liabilities are not recognised but information about them is disclosed unless the possibility of any outflow of economic benefits is remote. There are a number of contingent liabilities that arise in the normal course of business which, if realised, are not expected to result in a material liability to the Group.

17. Ultimate Parent Undertaking

The Group's ultimate parent undertaking and controlling party is Tesco PLC which is incorporated in England.

18. Events After the Reporting Period

Other than receipt of the FCA's warning notice in respect of the November 2016 fraud incident, which is discussed further in note 12, there have been no significant events between 31 August 2018 and the date of approval of this Interim Financial Report which would require a change to or additional disclosure in this Interim Financial Report.

TESCO PERSONAL FINANCE PLC
RESPONSIBILITY STATEMENT

The Directors listed below confirm that to the best of their knowledge:

- these Interim Condensed Consolidated Financial Statements have been prepared in accordance with IAS 34, 'Interim Financial Reporting', as endorsed by the EU; and
- the Interim Condensed Consolidated Financial Statements and Interim Management Report contained herein includes a fair review of the information required by DTR 4.2.7R, namely an indication of important events that have occurred during the first six months and their impact on the Interim Condensed Consolidated Financial Statements, and a description of the principal risks and uncertainties for the remaining six months of the financial year.

The Directors are responsible for the maintenance and integrity of the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The Directors of Tesco Personal Finance plc as at the date of this announcement are as set out below.

By order of the Board,

Declan Hourican
Director
1 October 2018

Directors:	Graham Pimlott	Independent Non-Executive Chairman
	Karl Bedlow	Chief Customer Officer
	John Castagno	Independent Non-Executive Director
	Robert Endersby	Independent Non-Executive Director
	Jacqueline Ferguson	Independent Non-Executive Director
	Richard Henderson	Chief Risk Officer
	Declan Hourican	Chief Financial Officer
	Simon Machell	Independent Non-Executive Director
	Gerard Mallon	Chief Executive
	James McConville	Independent Non-Executive Director
	David McCreadie	Managing Director
	Amanda Rendle	Independent Non-Executive Director
	Alan Stewart	Non-Executive Director
	James Willens	Senior Independent Non-Executive Director
Company Secretary:	Michael Mustard	

TESCO PERSONAL FINANCE PLC
INDEPENDENT REVIEW REPORT TO TESCO PERSONAL FINANCE PLC

We have been engaged by Tesco Personal Finance plc ("the Company") to review the Interim Condensed Consolidated Financial Statements in the Interim Financial Report for the six months 31 August 2018 which comprises the Interim Condensed Consolidated Income Statement, the Interim Condensed Consolidated Statement of Comprehensive Income, the Interim Condensed Consolidated Statement of Financial Position, the Interim Condensed Consolidated Statement of Changes in Equity, the Interim Condensed Consolidated Statement of Cash Flows and related notes 1 to 18. We have read the other information contained in the Interim Financial Report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the Interim Condensed Consolidated Financial Statements.

This report is made solely to the Company in accordance with International Standard on Review Engagements (UK and Ireland) 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Financial Reporting Council. Our work has been undertaken so that we might state to the Company those matters we are required to state to it in an independent review 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, for our review work, for this report, or for the conclusions we have formed.

Directors' responsibilities

The Interim Financial Report is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the Interim Financial Report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

As disclosed in note 1, the Annual Financial Statements of the Company are prepared in accordance with IFRS as adopted by the European Union. The Interim Condensed Consolidated Financial Statements included in this Interim Financial Report have been prepared in accordance with International Accounting Standard 34 "Interim Financial Reporting" as adopted by the European Union.

Our responsibility

Our responsibility is to express to the Company a conclusion on the Interim Condensed Consolidated Financial Statements in the Interim Financial Report based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Financial Reporting Council for use in the United Kingdom. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the Interim Condensed Consolidated Financial Statements in the Interim Financial Report for the six months ended 31 August 2018 are not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Deloitte LLP
Statutory Auditor
Edinburgh, United Kingdom
1 October 2018

ABBREVIATONS

AFS	Available-for-sale
BCBS	Basel Committee on Banking Supervision
BDAR	Bad debt:asset ratio
BoE	Bank of England
CCA	Consumer Credit Act
CRD	Capital Requirements Directive
CRO	Chief Risk Officer
CRR	Capital Requirements Regulation
EAD	Exposure at default
ECL	Expected credit losses
EIR	Effective interest rate
EU	European Union
FCA	Financial Conduct Authority
FVOCI	Fair value through other comprehensive income
FVPL	Fair value through profit or loss
IAS	International Accounting Standard
IAS 39	IAS 39 'Financial Instruments: Recognition and Measurement'
IASB	International Accounting Standards Board
ICAAP	Internal capital adequacy assessment process
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standard
IFRS 4	IFRS 4 'Insurance Contracts'
IFRS 9	IFRS 9 'Financial Instruments'
IFRS 15	IFRS 15 'Revenue from Contracts with Customers'
IFRS 17	IFRS 17 'Insurance Contracts'
LGD	Loss given default
LIBOR	London Inter Bank Offered Rate
MREL	Minimum requirements for own funds and eligible liabilities
NSFR	Net stable funding ratio
OCI	Other comprehensive income
PD	Probability of default
PPI	Payment protection insurance
PRA	Prudential Regulation Authority
PSD2	Second Payment Services Directive
RMF	Risk management framework
SA	Standardised approach
SFTs	Securities financing transactions
SONIA	Sterling Overnight Index Average
SPPI	Solely payments of principal and interest
TCR	Total capital requirement
TFS	Term Funding Scheme
TPP	Third party provider
TU	Tesco Underwriting Limited
UK	United Kingdom

B

Basel II	The capital adequacy framework issued by the BCBS (June 2006) in the form of the 'International Convergence of Capital Measurement and Capital Standards'.
Basel III	The capital reforms and introduction of a global liquidity standard proposed by the BCBS and due to be phased in through CRD IV from 2014 onwards.
Bad debt:asset ratio	The bad debt:asset ratio is calculated by dividing the impairment loss by the average balance of loans and advances to customers.
Brexit	The withdrawal of the UK from the EU.

C

Capital requirements directive	A legislative package relating to capital adequacy, issued by the European Commission and adopted by EU member states.
Capital requirements regulation	The Capital Requirements Regulation (EU) No. 575/2013 is an EU law that aims to decrease the likelihood that banks become insolvent, reflecting Basel III rules on capital measurement and capital standards.
Capital resources	Eligible capital held in order to satisfy capital requirements.
Capital risk	The risk that the Group holds regulatory capital which is of insufficient quality and quantity to enable it to absorb losses.
Common equity tier 1 capital	The highest form of regulatory capital under CRD IV, comprising common shares issued, related share premium, retained earnings and other reserves less regulatory adjustments.
Common equity tier 1 ratio	The common equity tier 1 ratio is calculated by dividing total tier 1 capital at the end of the reporting period by total risk weighted assets and is calculated in line with the CRR.
Cost:income ratio	The cost:income ratio is calculated by dividing operating expenses by total underlying income.
CRD IV	Legislation published in June 2013 (in force from 1 January 2014) by the European Commission, comprising the Capital Requirements Directive and Capital Requirements Regulation and together forming the CRD IV package. CRD IV implements the Basel III proposals in addition to new proposals on sanctions for non-compliance with regulatory rules, corporate governance and remuneration. The rules have been implemented in the UK via PRA policy statement PS7/13, with some elements subject to transitional phase in.
Credit risk	Credit risk is the risk that a borrower will default on a debt or obligation by failing to make contractually obligated payments, or that the Group will incur losses due to any other counterparty failing to meet their financial obligations.

D

Derivatives	Financial instruments whose value is based on the performance of one or more underlying assets.

E

Exposure	A claim, contingent claim or position which carries a risk of financial loss.
Exposure at default	The amount expected to be outstanding after any credit risk mitigation, if and when the counterparty defaults. Exposure at default reflects both drawn down balances as well as an allowance for undrawn commitments and contingent exposures.

F

Fair value	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.
Financial Conduct Authority	The Financial Conduct Authority is the conduct regulator for financial services firms and financial markets in the UK.
Financial instrument	A contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of an other entity.
Forbearance	Relief granted by a lender to assist customers in financial difficulty, through arrangements which temporarily allow the customer to pay an amount other than the contractual amounts due.

F (continued)

Foreign exchange risk	The risk that the value of transactions in currencies other than Sterling is altered by the movement of exchange rates
Funding risk	The risk that the Group does not have sufficiently stable and diverse sources of funding.

I

Impaired exposures	Exposures where it is not expected that all contractual cash flows will be collected or will be collected when they are due.
Impairment charge and impairment provisions	Provisions held on the balance sheet as a result of the raising of an impairment charge against profit for the incurred loss inherent in the lending book. Impairment provisions may be individual or collective.
Impairment losses	The reduction in value that arises following an impairment review of an asset which has determined that the asset's value is lower than its carrying value. For impaired financial assets measured at amortised cost, impairment losses are the difference between the carrying value and the present value of estimated future cash flows, discounted at the asset's original effective interest rate.
Insurance risk	The risk arising through the provision of insurance products in return for a premium. These risks may or may not occur as expected and the amount and timing of these risks are uncertain and determined by events outside of the Group's control.
Interest rate risk	The risk arising from the different repricing characteristics of the Group's non-trading assets and liabilities.
Internal capital adequacy assessment process	The Group's own assessment, based on Basel II requirements, of the level of capital needed in respect of its regulatory capital requirements (for credit, market and operational risks) and for other risks including stress events

L

Leverage ratio	Tier 1 capital divided by total exposure.
Liquidity risk	The risk that the Group is not able to meet its obligations as they fall due. This includes the risk that a given security cannot be traded quickly enough in the market to prevent a loss if a credit rating falls.
Loan to deposit ratio	The loan to deposit ratio is calculated by dividing loans and advances to customers by deposits from customers.

M

Market risk	The risk that the value of earnings or capital is altered through the movement of market rates. This includes interest rates, foreign exchange rates, credit spreads and equities.

N

Net interest margin	Net interest margin is calculated by dividing net interest income by average interest bearing assets
Net stable funding ratio	The net stable funding ratio is calculated under the CRD IV methodology.

O

Open Banking	A Government initiative to improve competition in the UK by opening up information that banks hold about their services and customers.
Operational risk	The risk of potential error, loss, harm or failure caused by ineffective or inadequately defined processes, system failure, improper conduct, human error, fraud or from external events.

P

Past due	Accounts are past due when a counterparty has failed to make a payment in line with their contractual obligations.
Pension risk	The risk to the Group caused by contractual or other liabilities to or with respect to a pension scheme.
Pillar 1	The first Pillar of the Basel II framework sets out the minimum regulatory capital requirements for credit, market and operational risks.
Pillar 2	The second Pillar of the Basel II framework, known as the Supervisory Review Process, sets out the review process for a bank's capital adequacy; the process under which supervisors evaluate how well banks are assessing their risks and the actions taken as a result of these assessments.
Probability of default	Represents the likelihood a customer will default over the relevant period.
Prudential Regulatory Authority	The PRA is responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms in the UK.
Second Payment Services Directive	The second Payment Services Directive is an EU Directive regulates payment services and payment service providers throughout the European Union and European Economic Area. PSD2 updates and replaces the Payment Services Directive 2008.

R

Recovery plan	The framework and recovery options which could be deployed in a severe stress event impacting capital or liquidity positions.
Regulatory capital	The capital that a bank holds, determined in accordance with rules established by the PRA.
Regulatory risk	The risk of reputational damage, liability or material loss from failure to comply with the requirements of the financial services regulators or related codes of best practice applicable to the business area within which the Group operates.
Risk Appetite	The level and types of risk that the Group is willing to assume to achieve its strategic objectives.
Risk weighted assets	Calculated by assigning a degree of risk expressed as a percentage (risk weight) to an exposure value in accordance with the applicable standardised and IRB approach rules.

S

Securitisation	A transaction or scheme whereby the credit risk associated with an exposure, or pool of exposures, is grouped and where payments to investors is dependent upon the performance of the underlying exposure or pool of exposures.
Securities Financing Transactions	The act of lending, or borrowing, a stock, derivative, or other security to or from an investor or firm.
Stress testing	The term used to describe techniques where plausible events are considered as vulnerabilities to ascertain how this will impact the capital resources which are required to be held by the Group.
Securitisation structured entity	A corporation, trust, or other non-bank entity, established for the purpose of carrying on securitisation activities. Structured entities are designed to isolate their obligations from those of the originator and the holder of the beneficial interests in the securitisation.
Standardised Approach	In relation to credit risk, the method for calculating credit risk capital requirements using risk weightings that are prescribed by the regulator. Standardised Approaches following prescribed methodologies also exist for calculating market and operational risk capital requirements.
Subordinated liabilities	Liabilities which, in the event of insolvency or liquidation of the issuer, are subordinated to the claims of depositors and other creditors of the issuer.

T

Tesco Pay+	Tesco Pay+ is the Group's mobile payment service, which offers Tesco's shoppers the ability to pay and collect Clubcard points with one simple and convenient scan of their phone.
Tier 1 capital	A component of regulatory capital, comprising Common Equity Tier 1 capital and other Tier 1 capital. Other Tier 1 capital includes qualifying capital instruments such as non-cumulative perpetual preference shares and other Tier 1 capital securities.
Tier 2 capital	A component of regulatory capital, comprising qualifying subordinated loan capital and related non-controlling interests.
Total capital ratio	The total capital ratio is calculated by dividing total regulatory capital by total risk weighted assets.
Total capital requirements	The minimum regulatory capital that must be held in accordance with Pillar 1 requirements for credit, market and operational risk.

U

UK Leverage Framework Regime	The UK Leverage Framework Regime currently applies to firms with retail deposits equal to or greater than £50 billion on an individual or consolidated basis.
Underlying cost:income ratio	The underlying cost:income ratio is calculated by dividing underlying operating expenses by total underlying income.