TESCO PERSONAL FINANCE PLC

INTERIM FINANCIAL REPORT

FOR THE SIX MONTHS ENDED 31 AUGUST 2021

COMPANY NUMBER SC173199

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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 (TPF) and the 'Group' means the Company and its subsidiaries (in prior periods, 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.

TPF is a wholly owned subsidiary of Tesco Personal Finance Group plc (TPFG), the share capital of which is wholly owned by Tesco PLC. A reconciliation of the results contained within these Interim Condensed Consolidated Financial Statements to the Tesco Bank results presented in the Tesco PLC Interim Results 2021/22 can be found on the Tesco PLC internet page: https://www.tescoplc.com/tesco-bank/interimbrokerpackaug2021/

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 underpinning 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 7 to 8 of this Interim Management Report.

Business Model

The core objective of the Board is to create and deliver the long-term sustainable success of the Group, generating value for the Group's shareholder and contributing to wider society. The Board sets the Group's purpose, strategy and values and is accountable to the Group's shareholder for ensuring that the Group is appropriately managed and achieves its objectives in a way that is supported by the right culture and behaviours.

The Group provides financial services and products to personal customers in the United Kingdom (UK). The Company is incorporated and registered in Scotland. Previously, the Company owned 49.9% of Tesco Underwriting Limited (TU), an authorised insurance company, which was accounted for as a joint venture. On 4 May 2021 the Company purchased the remaining 50.1% share capital of TU from Ageas (UK) Limited (Ageas), its joint venture partner. TU is now accounted for as a subsidiary of the Group.

Strategic Review

Covid-19

The Group returned to profitability in the six months to 31 August 2021 but continued to be impacted by the ongoing economic and social disruption resulting from the Covid-19 pandemic. The Group's continued priority throughout the period has been helping customers and colleagues through the many challenges created by the Covid-19 pandemic. The Group has served and supported its customers while maintaining the safety and wellbeing of colleagues and has transitioned new working practices to business-as-usual, with ongoing, stable operational performance.

The Group is committed to providing a safe, accessible working environment for its colleagues, providing them with the right tools and technology to work and be at their best. In support of this commitment, the Group has been testing different ways of working for colleagues, seeking feedback on which roles are best suited to an office or homeworking environment and those which are more suited to a blended approach. The Group has invested in homeworking technology which provides more colleagues with the opportunity to work from home and is testing different configurations of office space to understand what colleagues' needs might be when working together.

The Group continues to closely monitor that critical functions remain resilient and continues to engage with suppliers to ensure that service levels can be maintained throughout a prolonged Covid-19 pandemic. Regulators have been consistently updated with progress through regular and ad-hoc management information and relationship meetings.

The Group reviewed its stress testing scenarios to ensure it has sufficient capital and liquidity to trade through a plausible range of economic outcomes.

Covid-19 (continued)

The Board has received frequent operational, financial and colleague updates from the Executive team throughout the pandemic and provided challenge and support. There has also been a focus on both conduct and prudential impacts and close tracking of all government and regulator correspondence to gauge the potential impact on the Group, now and in the future.

The Group provided support to those customers who advised the Group that they were experiencing financial difficulty as a result of the Covid-19 pandemic. The Group granted temporary payment holidays to 146,325 Credit Card and Personal Loan customers. These were for an initial period of up to three months and in some cases were extended by a further three months. Of the payment holidays and extensions granted, 146,261 have ended, with 82.4% of customers returning to normal payment schedules. Only 64 payment holidays remained at 31 August 2021, in respect of which combined outstanding balances were £0.3m (£0.1m in Stage 1 and £0.2m in Stage 2). The Group ceased granting initial payment holidays in March 2021.

There has been a significant reduction in expected credit losses (ECLs) for potential bad debts in the period, with the Group recognising a charge for the period of £21.4m (August 2020: charge of £256.6m, including the day 1 impact of Covid-19 on the ECL charge for the period of £194.9m). The charge for the current period reflects the impact on the Group's ECL provision of the improving economic outlook, lower defaults and improved recoveries.

The extension of government support measures such as furlough has been unprecedented and this, coupled with the granting of payment holidays by the Group, has distorted the historically observed relationship between unemployment and default. Projected levels of unemployment have fallen from the expectation held at year end. However, the Group has yet to see significant defaults emerge from its lending portfolio as a result of the economic downturn and as such, Management has applied Covid-19 specific adjustments to the Group's modelled ECL provision to capture the estimated impact of the stress within the Group's ECL provision. Further information in respect of these adjustments, along with the impact of the current economic outlook on ECLs, is set out at note 23.

Notwithstanding the impact of the Covid-19 pandemic on the Group, its capital and liquidity ratios, which are set out on page 7, remain above regulatory requirements over the periods used by Management to monitor these ratios.

The Board considered in depth the impact of the Covid-19 pandemic on the Group's going concern status. The relevant disclosures are set out on pages 8 and 9.

During the period, the Group expanded its insurance offering with the launch of Travel Insurance, further demonstrating its commitment to the insurance market and better serving Tesco shoppers' insurance needs. Covid-19 cover is a key feature of this product, helping to give the Group's customers peace of mind if they experience Covid-19 related disruption to their travel plans.

Acquisition of Tesco Underwriting Limited

On 4 May 2021 the Company acquired the remaining 50.1% ordinary share capital of its joint venture entity, TU, from its joint venture partner, Ageas, following regulatory approval received in March 2021. TU is an authorised insurance company which provides the insurance underwriting service for a number of the Group’s general insurance products.

The acquisition is in line with the Group's strategy of focusing on propositions which better meet the needs of Tesco shoppers. The investment will significantly enhance the Group's insurance capability and enable the Group to create an insurance business that is uniquely positioned to help Tesco shoppers manage their money a little better every day.

The transaction has been accounted for as an acquisition of a business in accordance with International Financial Reporting Standard (IFRS) 3 ‘Business Combinations’. Total cash consideration of £89.7m has been paid to date, with an additional deferred payment of £5.0m due to be paid on expiry of the exit period, subject to the fulfilment of Ageas' obligations in relation to the migration and transition of the TU business to the Company. Expiry of the exit period is expected to be one year from the acquisition date.

Acquisition of Tesco Underwriting Limited (continued)

In line with the requirements of IFRS 3, the existing equity interest in TU held by the Company immediately before the acquisition date was remeasured to a fair value of £89.4m in the Interim Condensed Consolidated Statement of Financial Position. This resulted in a consolidated remeasurement gain for the Group of £4.6m, which is included in other income in the Interim Condensed Consolidated Income Statement. In line with the requirements of IFRS 3, the Group also recognised a consolidated gain of £5.0m, representing the Group's share of TU's available-for-sale (AFS) reserve immediately prior to acquisition, which is also included in other income in the Interim Condensed Consolidated Income Statement.

In addition to the purchase of the ordinary share capital of TU, the Company also acquired the holding of £21.2m in TU subordinated debt from Ageas on the same date. Further information in respect of the impact on the Group of the acquisition of TU is set out at note 2.

Following the acquisition of TU, the Group has brought in-house the writing of those Home and Motor Insurance policies which were previously underwritten through its broker panel, furthering the Group's objective to build a world class insurance proposition.

Closure of Personal Current Accounts

During the period, the Group announced its decision to close its Personal Current Account (PCA) product to its existing customers with effect from 30 November 2021, enabling it to focus on new propositions that are specifically designed to meet the everyday needs of Tesco shoppers.

The Group has written to customers explaining their options. The Group is supporting those customers using their PCA as their primary current account to find a suitable alternative, dependent on their circumstances and paying particular attention to supporting vulnerable customers and those in need of financial assistance.

For customers who have been using their PCA as a savings product, the Group has provided information on its tailored savings products for customers to consider as an alternative to their PCA.

Outsourcing of Support to Customers in Financial Difficulties

During the period, the Group announced its decision to outsource its collections and recoveries capability to a third-party provider which specialises in providing support for customers in financial difficulty. This change will allow the Group to deliver the necessary support and flexibility which its customers will need in the future and provide colleagues with access to technology platforms which will support them in meeting the needs of customers in financial difficulty.

Headlines

Income Statement

- Profit before tax from continuing operations is £79.1m (August 2020: loss of £143.5m).
- Underlying profit before tax, which excludes items which are not reflective of ongoing trading performance, is £80.1m (August 2020: loss of £142.2m). A reconciliation of statutory to underlying profit/(loss) for the current and prior periods is set out at note 5.
- Profit after tax from discontinued operations is £nil (August 2020: profit of £0.3m).

Profit/(loss) before tax from continuing operations

The key drivers of the profit/(loss) before tax from continuing operations are:

  - a 9.4% decrease in net interest income to £215.6m (August 2020: £237.9m), reflecting lower interest earnings on the reduced average customer lending balances. Also included is an amount of £3.4m (August 2020: £nil) due to a revision during the period of the estimation of interest earned on the Group's Personal Loan portfolio using the effective interest rate methodology (refer to note 1 for further details). Net interest margin has increased to 5.1% (August 2020: 4.6%[1]), reflecting lower funding costs as the Group has continued to reduce its savings balances to reflect its lending book profile;

[1] The prior period net interest margin has been restated from 5.0% to 4.6% following the inclusion of average interest-bearing balances of £892.0m in respect of investment securities at amortised cost which were previously excluded in calculating the prior period net interest margin.

Profit/(loss) before tax from continuing operations (continued)

- a 3.6% increase in net fees and commissions income to £90.9m (August 2020: £87.7m). Credit Card fees and ATM income have increased as the result of increased customer activity as the economy recovers. Offsetting this, there was a reduction in insurance commission income earned by the Group, reflecting the acquisition of TU during the period. Commission previously recognised by the Group on sale of a TU policy is now eliminated on consolidation;
- net insurance premium income of £52.5m (August 2020: £nil) relating to Home and Motor Insurance policies underwritten by TU;
- a gain on investment securities at fair value through profit and loss (FVPL) of £1.5m (August 2020: £nil). This includes a fair value gain of £1.0m (August 2020: £nil) relating to TU's investment in a property fund which is now consolidated following the acquisition of TU on 4 May 2021. Also included is a gain of £0.5m (August 2020: £nil) following the reclassification during the period of the Group's investment in VISA Inc. shares from fair value through other comprehensive income (FVOCI) to FVPL (refer to note 1 for further details);
- a loss on other financial instruments at FVPL of £1.0m (August 2020: loss of £1.3m);
- other income of £9.6m, representing the consolidated remeasurement gain recognised by the Group in respect of its existing equity interest in TU immediately before the Company's acquisition of TU of £4.6m, and a consolidated gain of £5.0m representing the Group's share of TU's AFS reserve immediately prior to acquisition. There was no such other income in the prior period. Refer to note 2 for further details;
- net insurance claims of £27.4m (August 2020: £nil) relating to Home and Motor Insurance policies underwritten by TU;
- a 10.7% increase in operating expenses to £243.8m (August 2020: £220.2m). Operating expenses have increased following the acquisition of TU and also reflect increased change activity;
- a 91.7% decrease in charges for ECLs on financial assets to £21.4m (August 2020: £256.6m, including the day 1 increase to ECLs of £194.9m). The charge for the current period reflects the impact on the Group's ECL provision of the improving economic outlook, lower defaults and improved recoveries. Although the Group has yet to see significant defaults emerge in its lending portfolio, Management has applied Covid-19 specific adjustments to the Group's modelled ECL provision to capture the estimated impact of the stress within the Group's ECL provision. Further information in respect of these adjustments is set out at note 23. The bad debt:asset ratio in respect of continuing operations decreased to 0.7% (August 2020: 6.7%); and
- a 71.1% decrease in the Group's share of profit from its joint venture, TU, to £2.6m (August 2020: £9.0m). This reflects the change in control of TU which took place on 4 May 2021, at which point TU became a wholly owned subsidiary of the Group, with its results being fully consolidated from that date.

Income tax (charge)/credit on profit/(loss) from continuing operations

Income tax on the Group's profit from continuing operations for the period is a charge of £7.6m (August 2020: credit of £46.6m). The tax charge for the period is primarily driven by the increase in the corporation tax rate from 19% to 25% and its impact on the Group’s deferred tax assets as set out at note 11. The prior period credit was driven predominantly by increased ECL charges due to Covid-19.

Profit after tax from discontinued operations

Profit after tax from discontinued operations in the prior period was £0.3m, relating to completion of the sale of the Group's Mortgage business, the majority of which took place in the year ended 29 February 2020. There were no such discontinued operations in the current period.

Balance Sheet

- Loans and advances to customers have remained flat at £6.4bn (February 2021: £6.4bn).
- Reinsurance assets of £256.8m, insurance funds withheld of £106.4m and insurance contract provisions of £654.7m have been recognised in the Interim Condensed Consolidated Statement of Financial Position following the Company's acquisition of TU on 4 May 2021. Further information in respect of these balances is set out at notes 20 and 21.

Balance Sheet (continued)

- Customer deposits, which continue to be the Group's main source of funding, have decreased by 12.2% to £5.0bn (February 2021: £5.8bn) as the Group has continued to reduce its savings balances to reflect its lending book profile.
- At the period end, the Group had accessed £400.0m of funds from the Bank of England's (BoE) Term Funding Scheme (TFS) (February 2021: £500.0m), having made repayments of £100.0m during the period, and £725.0m under the BoE's TFS with Incentives for Small and Medium Sized Entities (February 2021: £100.0m).
- The balance sheet remains well positioned to support future lending growth from both a liquidity and capital standpoint. At 31 August 2021, the total capital ratio was 26.6% (February 2021: 28.3%[1]) and net stable funding ratio (NSFR) was 118.5% (February 2021: 127.4%).

[1] This ratio has been restated following restatement of the Company Statement of Financial Position at 1 March 2020. This was in respect of a £7.0m dividend received from TU prior to 1 March 2020, which was recognised as a deduction from the carrying value of the investment in the Company Statement of Financial Position rather than through the Company Income Statement. Refer to note 26 for further details.

Regulatory Developments

Onshoring of European Union (EU) Regulations After Brexit

Following the UK's withdrawal from the EU and the ending of the transition period, any reference to EU regulations and directives (including technical standards) should be read as a reference to the UK's version of such regulation or directive, as onshored into UK law under the European Union (Withdrawal) Act 2018, as amended.

Capital Requirements Regulation

On 16 November 2020, HM Treasury, the Prudential Regulation Authority (PRA) and the Financial Conduct Authority confirmed an implementation date of 1 January 2022 for those Basel III reforms which make up the UK equivalent to the outstanding elements of the EU's second Capital Requirements Regulation (CRR). To enable this, HM Treasury will revoke sections of the CRR where the PRA will be implementing requirements through the PRA Rulebook. In the interim, the near final PRA rules (excluding leverage) are included in Policy Statement 17/21 ‘Implementation of Basel Standards’. The PRA intends that the final Policy Statement will take effect at the same time as HM Treasury’s revocation of the relevant parts of the CRR, which will be on 1 January 2022.

The PRA and the BoE's Financial Policy Committee (FPC) have published CP14/21 ‘Consultations by the FPC and PRA on changes to the UK leverage ratio framework’. This is expected to be implemented on 1 January 2022.

In addition, UK regulators are expected to publish a consultation on the UK implementation of the final Basel III changes in Q4 2021. These changes are targeted to apply by 1 January 2023.

Minimum Requirements for Own Funds and Eligible Liabilities

The Group became subject to the minimum requirements for own funds and eligible liabilities (MREL) on an interim basis from 1 January 2020, with end-state requirements applicable from 1 January 2023. The interim requirement is set at 18% of risk-weighted assets until 31 December 2022. The requirements are factored into the Group's funding and capital plans. TPFG undertook an initial £250.0m issuance of MREL-compliant debt in July 2019 in support of the interim requirements. Further issuances are planned in order to meet the future end-state requirements. Refer to page 67 for details of the Group's compliance with MREL requirements as at 31 August 2021.

The end-state MREL requirement will be set on a bank-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, based on the regulatory Total Capital Requirement; and a recapitalisation amount, which reflects the capital that a firm would be likely to need post-resolution.

Regulatory Developments (continued)

Countercyclical Capital Buffer

The Financial Policy Committee of the BoE is responsible for setting the UK countercyclical capital buffer (CCyB), being the rate that applies to UK exposures of banks, building societies and large investment firms incorporated in the UK. In response to the economic shock from the Covid-19 pandemic, the Financial Policy Committee reduced the UK CCyB from 1.0% to 0.0% on 11 March 2020, to support further the ability of banks to supply the credit needed to bridge a potentially challenging period. Following its meeting in December 2020, the Financial Policy Committee confirmed that it expects the 0% rate to remain until at least Q4 of 2021. Due to the usual 12-month implementation lag, any subsequent increase in the CCyB requirement is not expected to take effect until Q4 2022 at the earliest.

Climate Change

The Group is on track to have its approach for the management of climate change risk embedded by the end of 2021, in line with regulatory expectations. A Steering Group, with Senior Executive attendance from across the Group, meets monthly to oversee the Group's climate change programme. The Group has a target to be net zero from its own operations by 2035, with a programme of initiatives under development to achieve this. The Group plans to make disclosures aligned with the recommendations of the Science Based Targets initiative and Task Force on Climate-Related Financial Disclosures principles in its year-end Financial Statements.

IBOR Reform

The Group has transitioned the majority of its London Inter Bank Offered Rate (LIBOR) exposures to Sterling Overnight Index Average (SONIA). The only remaining LIBOR exposure relates to the Company’s investment in subordinated debt issued by TU, which the Group expects to transition to SONIA by 31 December 2021.

Key Performance Indicators

The Directors consider the following to be Key Performance Indicators (KPIs) for the Interim Condensed Consolidated Income Statement and are quoted in respect of the Group's continuing operations. The methodology applied in calculating the Group's KPIs is set out in the Glossary of Terms:

	31 August 2021	31 August 2020
Net interest margin	5.1%	4.6%[1]
Underlying cost:income ratio	71.1%	67.6%
Cost: income ratio	71.3%	67.9%
Gross insurance premiums written	£99.7m	n/a
Bad debt:asset ratio	0.7%	6.7%
Loans and advances to customers loss allowance coverage ratio	8.3%	8.2%

[1] The prior period net interest margin has been restated from 5.0% to 4.6% following the inclusion of average interest-bearing balances of £892.0m in respect of investment securities at amortised cost which were previously excluded in calculating the prior period net interest margin.

Capital and Liquidity Ratios

The Directors consider the following to be KPIs for capital and liquidity reporting:

	31 August 2021	28 February 2021	31 August 2020
Common equity tier 1 ratio	23.9%	25.1%[1]	21.6%[1]
Total capital ratio	26.6%	28.3%[1]	24.3%[1]
MREL ratio	30.2%	31.9%	27.6%
Net stable funding ratio	118.5%	127.4%	122.8%
Loan to deposit ratio	126.8%	111.3%	109.6%

The Group continues to phase in the IFRS 9 'Financial Instruments' impact on capital over a period of 5 years. On 27 June 2020, the CRR was further amended to accelerate specific CRR2 measures and implement a new IFRS 9 transitional relief calculation. The Group's total capital ratio remains above regulatory requirements at 26.6% (February 2021: 28.3%[1]) on a transitional basis and leaves the Group well placed to support future growth. On an end-point basis, the Group's total capital ratio is 24.0% (February 2021: 24.8%[1]), which is also above regulatory requirements. Refer to note 26 for full details of the impact of these amendments on the Group.

The NSFR, a measure of the Group's liquidity position, is within appetite at 118.5% as at 31 August 2021 (February 2021: 127.4%). The Group maintains a liquid asset portfolio of high-quality securities of £2.2bn (February 2021: £1.7bn).

[1] These ratios have been restated following restatement of the Company Statement of Financial Position at 1 March 2020. This was in respect of a £7.0m dividend received from TU prior to 1 March 2020, which was recognised as a deduction from the carrying value of the investment in the Company Statement of Financial Position rather than through the Company Income Statement. Refer to note 26 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 an 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, creating an integrated approach to managing risk. The RMF brings together governance, Risk Appetite, the three lines of defence, the Policy Framework and risk management tools to support the business in managing risk as part of day-to-day activity, 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.

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 their position with the approval of the Board.

Principal risks and uncertainties (continued)

The principal risks and uncertainties faced by the Group remain unchanged from the Annual Report and Financial Statements as at 28 February 2021 (pages 10 to 16). See below for further details.

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 loss resulting from inadequate or failed internal processes, people and systems or from external events.
Liquidity and Funding risk	Liquidity risk is 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. Funding risk is the risk that the Group does not have sufficiently stable and diverse sources of funding.
Market risk	The risk that movements in market prices (such as interest rates, foreign exchange rates and the market value of financial instruments) lead to a reduction in either the Group's earnings or capital.
Insurance risk	The risks accepted 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.
Covid-19	The ECLs recognised by the Group for the period reflect the impact on the Group's ECL provision of the improving economic outlook, lower defaults and improved recoveries. The Group's future performance is sensitive to the speed of the economic recovery.
Brexit	The Brexit transition period ended on 31 December 2020, with the UK agreeing a trade deal with the EU. The Group continues to monitor the impact of Brexit on both the UK financial services market, the wider UK economy and the Group itself. The Group also continues to monitor related developments to the UK's exit from the EU, including the possibility of a second Scottish independence vote.

Going Concern

The Directors have made an assessment of going concern, which took into account both current performance and the Group's outlook, which considered the impact of the Covid-19 pandemic, and included consideration of projections incorporating the impact of the Covid-19 pandemic on the Group's capital and funding position.

As part of this assessment the Board considered:

- The impact on the Group's profits as income and charges for ECLs continue to be affected by the Covid-19 pandemic. As part of this, the Board considered the latest macro-economic scenarios which were received from the Group's third-party supplier. These are discussed in note 23;

Going Concern (continued)

- The sufficiency of the Group's capital base throughout the Covid-19 pandemic. The revised macro-economic scenarios received were significantly less severe than those used in the Internal Capital Adequacy Assessment Process (ICAAP) reverse stress test. The Group reviewed its stress testing scenarios to ensure it has sufficient capital and liquidity to trade through a plausible range of economic outcomes;
- The adequacy of the Group's liquidity as the Group supports customers through a period of financial stress;
- The operational resilience of the Group's critical functions including call centres, mobile and online channels and the Group's ability to provide continuity of service to its customers throughout a prolonged stress;
- The resilience of the Group's IT systems;
- A detailed assessment of the Group's supplier base, considering any single points of failure and focussing on suppliers experiencing financial stress. This included consideration of contingency plans should suppliers be deemed at risk;
- The regulatory and legal environment and any potential conduct risks which could arise;
- Any potential valuation concerns in respect of the Group's assets as set out in the Interim Condensed Consolidated Statement of Financial Position;
- The impact of the Covid-19 pandemic on TU, the Group's insurance subsidiary; and
- The structural protections of the Group's securitisation vehicles.

The Board also considered the results of stress testing which is performed as an integral part of both the ICAAP and Internal Liquidity Adequacy Assessment Process, with the Group having sufficient capital and liquidity to fund the balance sheet in each scenario.

As a result of this assessment, the Directors consider that it is appropriate to adopt the going concern basis of accounting in preparing the Interim Condensed Consolidated Financial Statements.

TESCO PERSONAL FINANCE PLC
INTERIM CONDENSED CONSOLIDATED INCOME STATEMENT (UNAUDITED)
FOR THE SIX MONTHS ENDED 31 AUGUST 2021

	Note	6 months ended 31 August 2021 £m	6 months ended 31 August 2020 £m
Continuing operations			
Interest and similar income	6	246.2	300.3
Interest expense and similar charges	6	(30.6)	(62.4)
Net interest income		**215.6**	**237.9**
Fees and commissions income	7	108.3	102.3
Fees and commissions expense	7	(17.4)	(14.6)
Net fees and commissions income		**90.9**	**87.7**
Insurance premium income	8	94.4	–
Insurance premium income ceded to reinsurers	8	(41.9)	–
Net insurance premium income		**52.5**	**–**
Net gain on investment securities at fair value through profit or loss (FVPL)		1.5	–
Net loss on other financial instruments at FVPL		(1.0)	(1.3)
Other income	2	9.6	–
Net other income		**10.1**	**(1.3)**
Total income		**369.1**	**324.3**
Insurance claims incurred	9	(61.2)	
Insurance claims ceded to reinsurers	9	33.8	
Net insurance claims		**(27.4)**	–
Total income, net of insurance claims		**341.7**	**324.3**
Administrative expenses		(213.9)	(190.4)
Depreciation and amortisation		(29.9)	(29.8)
Operating expenses		**(243.8)**	**(220.2)**
Expected credit loss on financial assets	10	(21.4)	(256.6)
Operating profit/(loss)		**76.5**	**(152.5)**
Share of profit of joint venture	16	2.6	9.0
Profit/(loss) before tax		**79.1**	**(143.5)**
Analysed as:			
Underlying profit/(loss) before tax	5	80.1	(142.2)
Non-underlying items	5	(1.0)	(1.3)
		79.1	(143.5)
Income tax (charge)/credit	11	(7.6)	46.6
Profit/(loss) for the period from continuing operations		**71.5**	**(96.9)**
Discontinued operations			
Profit for the period after tax from discontinued operations		–	0.3
Profit/(loss) for the period attributable to owners of the parent		**71.5**	**(96.6)**

INTERIM CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (UNAUDITED)

FOR THE SIX MONTHS ENDED 31 AUGUST 2021

	Note	6 months ended 31 August 2021 £m	6 months ended 31 August 2020 £m
Profit/(loss) for the period		71.5	(96.6)
Items that may be reclassified subsequently to the income statement			
Debt securities at fair value through other comprehensive income (FVOCI)			
Fair value movements		3.8	(3.1)
Taxation		(0.2)	0.8
		3.6	(2.3)
Cash flow hedges			
Fair value movements		0.8	(0.5)
Taxation		(0.2)	0.1
		0.6	(0.4)
Currency basis reserve			
Foreign currency movements		–	0.1
		–	0.1
Share of other comprehensive (expense)/income of joint venture		(0.6)	0.8
Transfer of share of other comprehensive income of joint venture to the Income Statement on change of control		(5.0)	–
		(5.6)	0.8
Items that will not be reclassified subsequently to the income statement			
Equity securities at FVOCI			
Fair value movements		–	0.3
Taxation		–	(0.1)
		–	0.2
Other comprehensive expense for the period, net of tax		**(1.4)**	**(1.6)**
Total comprehensive income/(expense) for the period		**70.1**	**(98.2)**
Total comprehensive income/(expense) attributable to owners of the parent arising from:			
Continuing operations		70.1	(98.5)
Discontinued operations		–	0.3

INTERIM CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION (UNAUDITED)

AS AT 31 AUGUST 2021

	Note	31 August 2021 £m	28 February 2021 (audited) £m	31 August 2020 £m
Assets				
Cash and balances with central banks		555.4	802.6	1,604.5
Loans and advances to banks	13	51.4	–	–
Loans and advances to customers	14	6,403.9	6,402.2	7,285.2
Derivative financial instruments		5.6	6.1	6.8
Investment securities	15	1,557.6	953.5	875.9
Reinsurance assets	21	256.8	–	–
Prepayments and accrued income		51.6	41.6	46.1
Current income tax asset		24.9	36.1	25.2
Other assets		217.0	211.2	430.2
Investment in joint venture	16	–	92.8	95.9
Deferred income tax asset		69.0	67.3	74.1
Intangible assets	17	159.9	130.9	130.1
Property, plant and equipment		77.2	77.5	75.7
Total assets		**9,430.3**	**8,821.8**	**10,649.7**
Liabilities				
Deposits from banks		1,125.0	600.0	500.0
Deposits from customers		5,048.6	5,751.2	6,648.4
Debt securities in issue	18	–	–	762.1
Derivative financial instruments		36.4	47.5	72.3
Provisions for liabilities and charges	19	49.3	60.1	50.2
Accruals and deferred income		93.5	86.1	156.3
Other liabilities		152.2	184.2	335.6
Insurance funds withheld	20	106.4	–	–
Insurance contract provisions	21	654.7	–	–
Subordinated liabilities and notes	22	485.8	486.6	489.4
Total liabilities		**7,751.9**	**7,215.7**	**9,014.3**
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		430.8	355.6	377.5
Other reserves		27.7	30.6	38.0
Total equity		**1,678.4**	**1,606.1**	**1,635.4**
Total liabilities and equity		**9,430.3**	**8,821.8**	**10,649.7**

INTERIM CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (UNAUDITED)

FOR THE SIX MONTHS ENDED 31 AUGUST 2021

	Share capital £m	Share premium £m	Retained earnings £m	FV/AFS reserve £m	Cash flow hedge reserve £m	Currency basis reserve £m	Share based payment reserve £m	Total equity £m
Balance at 1 March 2021	**122.0**	**1,097.9**	**355.6**	**9.3**	**(0.6)**	**–**	**21.9**	**1,606.1**
Comprehensive income								
Profit for the period	–	–	71.5	–	–	–	–	71.5
Net fair value movement on investment securities held at FVOCI	–	–	–	3.6	–	–	–	3.6
Net movement on cash flow hedges	–	–	–	–	0.6	–	–	0.6
Share of other comprehensive expense of joint venture (refer note 16)	–	–	–	(0.6)	–	–	–	(0.6)
Transfer of share of other comprehensive income of joint venture to the Income Statement on change of control	–	–	–	(5.0)	–	–	–	(5.0)
Transfer of net gains to retained earnings on reclassification during the period of investment securities held at FVOCI to FVPL[1] (refer note 15)	–	–	3.7	(3.7)	–	–	–	–
Total comprehensive income	**–**	**–**	**75.2**	**(5.7)**	**0.6**	**–**	**–**	**70.1**
Transactions with owners								
Share based payments	–	–	–	–	–	–	2.2	2.2
Total transactions with owners	**–**	**–**	**–**	**–**	**–**	**–**	**2.2**	**2.2**
Balance at 31 August 2021	**122.0**	**1,097.9**	**430.8**	**3.6**	**–**	**–**	**24.1**	**1,678.4**
Balance at 1 March 2020	**122.0**	**1,097.9**	**474.1**	**12.3**	**(0.3)**	**(0.1)**	**25.1**	**1,731.0**
Comprehensive income								
Loss for the period	–	–	(96.6)	–	–	–	–	(96.6)
Net fair value movement on equity investment securities held at FVOCI	–	–	–	(2.1)	–	–	–	(2.1)
Net movement on cash flow hedges	–	–	–	–	(0.4)	0.1	–	(0.3)
Share of other comprehensive income of joint venture	–	–	–	0.8	–	–	–	0.8
Total comprehensive income	**–**	**–**	**(96.6)**	**(1.3)**	**(0.4)**	**0.1**	**–**	**(98.2)**
Transactions with owners								
Share based payments	–	–	–	–	–	–	2.6	2.6
Total transactions with owners	**–**	**–**	**–**	**–**	**–**	**–**	**2.6**	**2.6**
Balance at 31 August 2020	**122.0**	**1,097.9**	**377.5**	**11.0**	**(0.7)**	**–**	**27.7**	**1,635.4**

[1] The Group holds an investment in preferred stock issued by VISA Inc. which was designated at FVOCI in previous years. Following a review of industry practice and the requirements of IFRS 9, this investment has been reclassified to FVPL with effect from 1 March 2021. As this amount is not material, no prior year restatement has been recognised in respect of this reclassification.

INTERIM CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (UNAUDITED)

FOR THE SIX MONTHS ENDED 31 AUGUST 2021

	Note	6 months ended 31 August 2021 £m	6 months ended 31 August 2020 £m
Operating Activities			
Profit/(loss) before tax from continuing operations		79.1	(143.5)
Profit before tax from discontinued operations		–	0.4
Total profit/(loss) before tax		**79.1**	**(143.1)**
Adjusted for:			
Non-cash items included in operating profit/(loss) before taxation and other adjustments		47.1	303.9
Changes in operating assets and liabilities		(258.0)	(84.0)
Income taxes paid		(1.0)	(8.8)
Cash flows (used in)/generated from operating activities		**(132.8)**	**68.0**
Investing Activities			
Purchase of intangible assets and property, plant and equipment		(19.9)	(35.1)
Purchase of debt investment securities		(43.7)	–
Sale of debt investment securities		51.0	201.8
Investment in subsidiary		(89.7)	–
Cash and cash equivalents acquired on investment in subsidiary		42.3	–
Purchase of subordinated debt issued by subsidiary		(21.2)	–
Dividends received from TU		10.0	–
Cash flows (used in)/generated from investing activities		**(71.2)**	**166.7**
Financing Activities			
Interest paid on debt securities in issue		–	(8.2)
Interest paid on assets held to hedge debt securities in issue		(0.6)	(1.6)
Interest paid on subordinated liabilities and notes		(6.2)	(6.5)
Principal repayments on lease liabilities		(1.0)	(0.9)
Interest paid on lease liabilities		(1.8)	(1.8)
Cash flows used in financing activities		**(9.6)**	**(19.0)**
Net (decrease)/increase in cash and cash equivalents		**(213.6)**	**215.7**
Cash and cash equivalents[1] at beginning of period		**777.9**	**1,362.3**
Cash and cash equivalents[1] at end of period		**564.3**	**1,578.0**

[1] Cash and cash equivalents comprise cash and balances with central banks, excluding certain reserve deposits of £42.5m which do not have a maturity of less than three months (August 2020: £26.5m), and loans and advances to banks of £51.4m (August 2020: £nil).

1. Accounting Policies

The Interim Condensed Consolidated Financial Statements for the six months ended 31 August 2021 were approved by the Board of Directors on 4 October 2021.

Basis of Preparation

The Interim Condensed Consolidated Financial Statements have been prepared in accordance with International Accounting Standard (IAS) 34 'Interim Financial Reporting'.

Unless otherwise stated, the accounting policies applied, and the judgements, estimates and assumptions made in applying those policies, are consistent with those described in the Consolidated Financial Statements of the Group for the year ended 28 February 2021. 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 2021, which have been prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006 and International Financial Reporting Standards (IFRSs) and interpretations issued by the International Financial Reporting Interpretations Committee of the International Accounting Standards Board (IASB) and those parts of the Companies Act 2006 applicable to Companies reporting under IFRSs.

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 2021 were approved by the Board of Directors on 12 April 2021 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.

The Group holds an investment in preferred stock issued by VISA Inc. which was designated at fair value through other comprehensive income (FVOCI) in previous years. Following a review of industry practice and the requirements of IFRS 9, this investment has been reclassified to fair value through profit or loss (FVPL) with effect from 1 March 2021. As a result, £5.1m (£3.7m net of deferred tax) in respect of the opening fair value reserve at 1 March 2020 was released from the fair value reserve in the period and recognised directly in retained earnings in the Interim Condensed Consolidated Statement of Changes in Equity. As this amount is not material, no prior year restatement has been recognised in respect of this reclassification.

In addition, a revision has been made during the period to the estimation of interest earned on the Group's Loans portfolio using the effective interest rate (EIR) methodology. This has resulted in the recognition of additional interest income in the period of £3.4m, with a corresponding increase in the related Personal Loan asset. As this amount is not material, no prior year restatement has been recognised in respect of this revision.

Onshoring of European Union (EU) Regulations After Brexit

Following the UK's withdrawal from the EU and the ending of the transition period, any reference to EU regulations and directives (including technical standards) should be read as a reference to the UK's version of such regulation or directive, as onshored into UK law under the European Union (Withdrawal) Act 2018, as amended.

Going concern

The Directors have made an assessment of going concern, which took into account both current performance and the Group's outlook, which considered the impact of the Covid-19 pandemic, and included consideration of projections incorporating the impact of the Covid-19 pandemic on the Group's capital and funding position.

As part of this assessment the Board considered:

- The impact on the Group's profits as income and charges for expected credit losses (ECLs) continue to be affected by the Covid-19 pandemic. As part of this, the Board considered the latest macro-economic scenarios which were received from the Group's third-party supplier. These are discussed in note 23;

1. Accounting Policies (continued)

Going concern (continued)

- The sufficiency of the Group's capital base throughout the Covid-19 pandemic. The revised macro-economic scenarios received were significantly less severe than those used in the Internal Capital Adequacy Assessment Process (ICAAP) reverse stress test. The Group reviewed its stress testing scenarios to ensure it has sufficient capital and liquidity to trade through a plausible range of economic outcomes;
- The adequacy of the Group's liquidity as the Group supports customers through a period of financial stress;
- The operational resilience of the Group's critical functions including call centres, mobile and online channels and the Group's ability to provide continuity of service to its customers throughout a prolonged stress;The resilience of the Group's IT systems;
- A detailed assessment of the Group's supplier base, considering any single points of failure and focussing on suppliers experiencing financial stress. This included consideration of contingency plans should suppliers be deemed at risk;
- The regulatory and legal environment and any potential conduct risks which could arise;
- Any potential valuation concerns in respect of the Group's assets as set out in the Interim Condensed Consolidated Statement of Financial Position;
- The impact of the Covid-19 pandemic on Tesco Underwriting Limited (TU), the Group's insurance subsidiary; and
- The structural protections of the Group's securitisation vehicles.

The Board also considered the results of stress testing which is performed as an integral part of both the ICAAP and Internal Liquidity Adequacy Assessment Process, with the Group having sufficient capital and liquidity to fund the balance sheet in each scenario.

As a result of this assessment, the Directors consider that it is appropriate to adopt the going concern basis of accounting in preparing the Interim Condensed Consolidated Financial Statements.

Adoption of new and amended IFRS

Details of new accounting standards and amendments to standards which will impact the Group in future reporting periods are included in the Consolidated Financial Statements of the Group for the year ended 28 February 2021.

During the period to 31 August 2021, the Group did not adopt any new accounting standards or amendments to standards which had any impact on the Group.

New accounting policies

Several new accounting policies relating to the insurance business of TU have been adopted by the Group following the acquisition of TU on 4 May 2021 and some existing policies have been updated as noted in the following pages 16 to 21.

(a) Basis of consolidation

The Consolidated Financial Statements of the Group comprise the Financial Statements of the Company and all consolidated subsidiaries, including certain securitisation structured entities.

Investment in Group undertakings

Subsidiaries are all entities (including structured entities) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The results of subsidiaries are included in the Consolidated Financial Statements from the date that control commences until the date that control ceases. The Company's investments in its subsidiaries are stated at cost less any impairment, except in the case of a subsidiary acquired via a step acquisition, where the original investment is revalued to fair value at the date on which the Company obtains control.

1. Accounting Policies (continued)

(a) Basis of consolidation (continued)

Intragroup balances, and any unrealised gains and losses or income and expenses arising from intragroup transactions, are eliminated in preparing the Consolidated Financial Statements.

Securitisation structured entities

The Group enters into securitisation transactions in which it assigns Credit Card receivables to a securitisation structured entity which supports the issuance of securities backed by the cash flows from the securitised Credit Card receivables. Although none of the equity of the securitisation structured entities is owned by the Company, the nature of these entities means that the Group has the rights to variable returns from its involvement with these securitisation structured entities and has the ability to affect those returns through its power over them. As such they are effectively controlled by the Group and are consolidated on a line by line basis in the Consolidated Financial Statements.

Investment in joint venture

A joint arrangement is an arrangement over which the Group has joint control. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control. A joint venture is a joint arrangement whereby the Group has rights to a share of the net assets of the joint arrangement.

On 4 May 2021 the Company purchased the remaining 50.1% share capital of TU from Ageas (UK) Limited (Ageas), its joint venture partner. At this point, TU became a wholly owned subsidiary of the Group. Prior to this date, the Group's share of the results of the joint venture were included in the Consolidated Income Statement using the equity method of accounting. The Group's investment in its joint venture was carried in the Consolidated Statement of Financial Position at cost plus post-acquisition changes in the Group's share of the net assets of the entity, less any impairment.

If the Group's share of losses in its joint venture equalled or exceeded its investment in the joint venture, the Group did not recognise further losses, unless it had incurred obligations to do so or made payments on behalf of the joint venture. The Company's investment in a joint venture was stated at cost less any impairment.

(b) Business combinations

The Group accounts for all business combinations where the acquisition meets the definition of a business by applying the acquisition method of accounting.

On acquisition, the assets (including intangible assets), liabilities and contingent liabilities of an acquired entity are measured at their fair values.

On acquisition, the purchase consideration is measured as the fair value of assets transferred. The excess of the purchase consideration over the fair value of the identifiable net assets acquired is recorded as goodwill. If the purchase consideration is less than the fair value of the identifiable net assets acquired the difference is recognised directly in the Consolidated Income Statement. All acquisition-related costs are expensed.

When the Group obtains control of a joint venture, the Group's previously held interest in the acquired entity is remeasured to its acquisition-date fair value and the resulting gain or loss, if any, is recognised in the Consolidated Income Statement.

(c) Revenue recognition

Net interest income recognition

Interest income and expense for all financial instruments measured at amortised cost are recognised using the EIR method.

The EIR method is a method of calculating the amortised cost of a financial asset or financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the expected life of the financial asset or financial liability. The EIR is the rate that exactly discounts estimated future cash flows to the instrument's initial carrying amount.

1. Accounting Policies (continued)

(c) Revenue recognition (continued)

Net interest income recognition (continued)

Calculation of the EIR takes into account fees receivable that are an integral part of the instrument's yield, premiums or discounts on acquisition or issue, early redemption fees and transaction costs. All contractual and behavioural terms of a financial instrument are considered when estimating future cash flows.

Interest income is calculated on the gross carrying amount of a financial asset unless the financial asset is impaired, in which case interest income is calculated on the net carrying amount, after allowance for ECLs.

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.

Prior to the acquisition of TU on 4 May 2021, the Group generated commission from the sale and service of Motor and Home Insurance policies underwritten by TU. Following the acquisition, these amounts represent intercompany transactions which are fully eliminated in the Consolidated Income Statement. The Group also generated commission from the sale and service of Motor and Home Insurance policies underwritten by a third-party underwriter until August 2021 when the Group brought in-house the writing of Home and Motor Insurance policies which were previously underwritten through its broker panel. This commission income was based on commission rates which were 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.

The Group also generates fee income from the referral of insurance customers to third-parties for car hire and legal services. This income is recognised at the time a referral is made, in line with the satisfaction of the performance obligation for the Group.

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, 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.

1. Accounting Policies (continued)

(c) Revenue recognition (continued)

Customer loyalty programmes

The Group participates in the customer loyalty programme operated by Tesco Stores Limited (TSL). The programme operates by allowing customers to accumulate Clubcard points on purchases for future redemption against a range of Tesco products. Revenue in respect of these points is recognised at the time of the customer transaction as the Group has no obligation to customers in respect of Clubcard points once the points are allocated to a customer account. The revenue is recognised net of the cost of providing Clubcard points to customers, which is recharged by TSL to the Group.

Net insurance premium income recognition

Gross written premiums comprise the premiums on contracts entered into during the year, irrespective of whether they relate in whole or in part to a later accounting period. Premiums exclude taxes and levies based on premiums. An estimate is made at the Statement of Financial Position date to recognise retrospective adjustments to premiums. The earned portion of premiums received is recognised as revenue. Premiums are earned from the date of attachment of risk, over the indemnity period, based on the pattern of risks underwritten. Outward reinsurance premiums are recognised as a deduction from net insurance revenue in accordance with the contractual arrangements with reinsurers.

Net insurance claims

Claims incurred consist of claims paid during the financial year, together with the movement in the provision for outstanding claims. Claims are recognised net of benefits reimbursed in accordance with the contractual arrangements with reinsurers.

Dividend income recognition

Dividends are recognised in the Consolidated Income Statement when the entity's right to receive payment is established.

(d) Insurance contracts and reinsurance assets

Classification of insurance contracts

Contracts under which the Group accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder or other beneficiary if a specified uncertain future event (the insured event) adversely affects the policyholder or other beneficiary are classified as insurance contracts. These contracts remain insurance contracts until all rights and obligations are extinguished or expire. Insurance contracts may also transfer some financial risk.

Reinsurance

The Group cedes reinsurance in the normal course of business for the purpose of limiting its net loss potential through the diversification of its risks. Reinsurance ceded includes quota share (QS), excess of loss and adverse development cover (ADC) contracts. Reinsurance arrangements do not relieve the Group from its direct obligations to its policyholders.

Only contracts that give rise to a significant transfer of insurance risk are accounted for as reinsurance contracts. Amounts recoverable under such contracts are recognised in the same year as the related claim. Contracts that do not transfer significant insurance risk (i.e. financial reinsurance) are accounted for as financial instruments.

Reinsurance assets include balances due from reinsurance companies for reinsurance claims. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision or settled claims associated with the reinsured policy.

1. Accounting Policies (continued)

(d) Insurance contracts and reinsurance assets (continued)

Reinsurance

Amounts recoverable under reinsurance contracts are assessed for impairment at each year end date. Such assets are deemed impaired if there is objective evidence, as a result of an event that occurred after initial recognition, that the Group may not recover all amounts due and that the event has a reliably measurable impact on the amounts that the Group will receive from the reinsurer.

For the QS reinsurance ceded, amounts payable for funds withheld, net of the associated QS profit commission, are maintained in accordance with contract terms for each underwriting year. A commutation is performed for the purposes of settling the profit commission and funds withheld balance within the terms of the contract, four years after commencement. For further details on funds withheld see note 20.

Provision for outstanding claims

The provision for outstanding claims represents the Group's estimate of the ultimate cost of settling all claims incurred but unpaid at the reporting date whether reported or not, and related internal and external claims handling expenses. Claims outstanding are assessed by reviewing individual claims data and making an allowance for claims incurred but not yet reported, adjusted for the effect of both internal and external foreseeable events, such as changes in claims handling procedures, inflation, judicial trends, legislative changes and past experience and trends. Reinsurance and other recoveries are assessed in a manner similar to the claims outstanding and presented separately as assets.

Unexpired risk provision

If required, a provision is made for unexpired risks arising from business where the expected value of claims and expenses attributable to the unexpired periods of policies in force at the reporting date exceeds the unearned premiums provision in relation to such policies. The provision for unexpired risks is calculated separately by reference to classes of business which are managed together, after taking into account the relevant investment return.

Unearned premium provision

The provision for unearned premiums comprises the proportion of gross premiums written which is estimated to be earned in the following or subsequent financial years, calculated separately for each insurance contract using the daily pro rata method, adjusted if necessary to reflect any variation in the incidence of risk during the period covered by the contract.

Deferred acquisition costs

Commission payable to agents and other acquisition costs, which are incurred for acquiring new and renewal insurance business that is primarily related to the production of that business, are deferred. Any balances not considered recoverable are written-off.

Such deferred acquisition costs are finite and are amortised by reference to the basis on which the related premiums are earned, which is over a period of one year.

(e) Intangible assets

Goodwill

Goodwill arising on consolidation represents the excess of the purchase consideration transferred over the fair value of the Group's share of the net assets and contingent liabilities of the acquired subsidiary at the date of acquisition. If the consideration is less than the fair value of the Group's share of the net assets, liabilities and contingent liabilities of the acquired entity (i.e. a bargain purchase), the difference is credited to the Consolidated Income Statement in the period of acquisition.

At the acquisition date of a subsidiary, goodwill acquired is recognised as an asset and is allocated to each of the cash generating units or groups of cash-generating units expected to benefit from the business combination's synergies and to the lowest level at which Management monitor the goodwill.

1. Accounting Policies (continued)

(e) Intangible assets (continued)

Goodwill (continued)

Goodwill is not subject to amortisation and is tested for impairment on an annual basis. Refer to accounting policy 1(f) for further details.

Other intangible assets acquired in a business combination

As part of the acquisition of TU on 4 May 2021, the Group has recognised separately identified intangible assets in relation to internally generated computer software. These are being amortised over a period of 5 years.

Purchased intangible assets

Intangible assets that are acquired by the Group, excluding those acquired as part of a business combination, are stated at historical cost less accumulated amortisation and any impairment losses. Amortisation is charged to the Consolidated Income Statement on a straight-line basis over the estimated useful lives. The Group's intangible assets are computer software, for which the estimated useful lives are 3 to 10 years.

Internally generated intangible assets - research and development expenditure

Research costs are expensed in the Consolidated Income Statement as incurred.

Development expenditure incurred on an individual project is capitalised only if all of the following criteria are demonstrated:

- an asset is created that can be identified (such as software);
- it is probable that the asset created will generate future economic benefits; and
- the development cost of the asset can be measured reliably.

Internally generated intangible assets - research and development expenditure (continued)

Following the initial recognition of development expenditure, the cost is amortised over the estimated useful life of the asset created. Amortisation commences on the date that the asset is brought into use. Work-in-progress assets are not amortised until they are brought into use and transferred to the appropriate category of intangible assets.

(f) Impairment of non-financial assets

Goodwill is tested annually for impairment. Other non-financial assets are reviewed for impairment when there are indications that the carrying value may not be recoverable. If an asset’s carrying amount is determined to be greater than its recoverable amount, an impairment loss is recognised immediately in the Consolidated Income Statement and the carrying value of the asset is written down by the amount of the loss. The recoverable amount is the higher of the asset’s fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets for which an impairment loss has been recognised are reviewed for possible reversal of the impairment at each reporting date. Impairment losses on goodwill are not reversed.

2. Acquisition of Tesco Underwriting Limited

On 4 May 2021 the Company acquired the remaining 50.1% ordinary share capital of its joint venture entity, TU, from its joint venture partner, Ageas. TU is an authorised insurance company which provides the insurance underwriting service for a number of the Group’s general insurance products.

The acquisition is in line with the Group's strategy of focusing on propositions which better meet the needs of Tesco shoppers. The investment will significantly enhance the Group's insurance capability and enable the Group to create an insurance business that is uniquely positioned to help Tesco shoppers manage their money a little better every day.

The transaction has been accounted for as an acquisition of a business in accordance with IFRS 3 ‘Business Combinations’. Total cash consideration of £89.7m has been paid to date, with an additional deferred payment of £5.0m due to be paid on expiry of the exit period, subject to the fulfilment of Ageas' obligations in relation to the migration and transition of the TU business to the Company. Expiry of the exit period is expected to be one year from the acquisition date.

2. Acquisition of Tesco Underwriting Limited (continued)

In line with the requirements of IFRS 3, the existing equity interest in TU held by the Company immediately before the acquisition date was remeasured to a fair value of £89.4m in the Interim Condensed Consolidated Statement of Financial Position. This resulted in a consolidated remeasurement gain for the Group of £4.6m which is included in other income in the Interim Condensed Consolidated Income Statement. In line with the requirements of IFRS 3, the Group also recognised a consolidated gain of £5.0m, representing the Group's share of TU's available-for-sale (AFS) reserve immediately prior to acquisition, which is also included in other income in the Interim Condensed Consolidated Income Statement.

In addition to the purchase of the ordinary share capital of TU, the Company also acquired the holding in TU subordinated debt from Ageas on the same date at an amount of £21.2m.

The table below shows the total cost of obtaining control of TU in the period:

	Cost £m
Cash consideration paid	89.7
Contingent consideration	5.0
Effective settlement of pre-existing balances with TU	11.8
Deemed consideration	**106.5**
Fair value of Group's initial 49.9% investment	89.4
Total cost	**195.9**

The table below sets out the fair values of the identifiable assets and liabilities acquired:

	Fair Value £m
Assets	
Cash and balances with central banks	8.8
Loans and advances to banks	33.5
Investment securities	634.8
Reinsurance assets	246.7
Prepayments and accrued income	2.7
Other assets	23.7
Intangible assets	18.0
Property, plant and equipment	0.8
Total assets	969.0
Liabilities	
Accruals and deferred income	15.0
Current income tax liability	0.4
Other liabilities	4.0
Deferred income tax liability	2.0
Insurance funds withheld	100.2
Insurance contract provisions	650.3
Subordinated liabilities	21.2
Total liabilities	793.1
Net assets	175.9
Fair value of net assets acquired	175.9
Goodwill arising on acquisition	20.0
Total cost	**195.9**

2. Acquisition of Tesco Underwriting Limited (continued)

The goodwill arising on the acquisition is primarily attributable to synergies which are expected to be realised from the acquisition and having full control over the Group's end-to-end insurance business. None of the goodwill is expected to be deductible for tax purposes. Acquired intangible assets comprise internally generated computer software of £18.0m, which is amortised over a period of 5 years. Refer to note 17 for further details.

The fair value of acquired insurance and other receivables is £26.4m, included within prepayments and accrued income and other assets in the above table. This includes salvage and subrogation recoveries of £16.0m and receivables arising from reinsurance contracts of £7.6m. The fair value is equal to the gross contractual amount due for these receivables and the best estimate of the amounts not expected to be collected at the acquisition date was £nil.

The amounts of total income net of insurance claims and profit before tax contributed to the Group's Interim Condensed Consolidated Income Statement since the acquisition date from the acquired TU business were £23.6m and £12.0m respectively. This includes the impact of consolidation adjustments, primarily £0.5m of amortisation expense on acquired intangible assets, and the effect of the elimination of intercompany transactions. If the acquisition had occurred on 1 March 2021, the Group's total income net of insurance claims for the year would have increased by £12.0m to £353.7m and the profit before tax would have increased by £3.6m to £82.7m[1].

Acquisition-related costs of £7.3m have been incurred by the Company in relation to the acquisition to date, of which £0.8m (August 2020: £1.7m) has been included in administrative expenses in the Interim Condensed Consolidated Income Statement. Total prior year acquisition-related costs amounted to £2.9m, with the balance of acquisition-related costs of £3.6m being recognised prior to 1 March 2020.

[1] These amounts include TU income and profits net of intercompany amounts and consolidation adjustments, and also exclude the equity accounted share of TU profit of £2.6m that was recognised during the period until the date of acquisition.

3. Critical Accounting Estimates and Judgements in Applying Accounting Policies

In the course of preparing the Interim Condensed Consolidated Financial Statements, no judgements have been made in the process of applying the Group's accounting policies, other than those using estimations (which are presented separately below), that have had a significant effect on the amounts recognised in the Financial Statements.

The reported results of the Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its Financial Statements. United Kingdom (UK) company law and IFRS require the Directors, in preparing the Group's Financial Statements, to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent. Where accounting standards are not specific and Management have to choose a policy, IAS 8, 'Accounting Policies, Changes in Accounting Estimates and Errors', requires Management to adopt policies that will result in relevant and reliable information in the light of the requirements and guidance in IFRS dealing with similar and related issues and the IASB Framework for the Preparation and Presentation of Financial Statements.

The judgements and estimates involved in the Group's accounting policies that are considered to be the most important to the portrayal of its financial condition are consistent with those described in the Consolidated Financial Statements of the Group for the year ended 28 February 2021, with the exception of those relating to the insurance business following the acquisition of TU on 4 May 2021, as set out below. The use of estimates, assumptions or models that differ from those adopted by the Group would affect its reported results.

Outstanding insurance claims and provisions

The Group establishes reserves in respect of the anticipated losses incurred in respect of business it has underwritten. These reserves reflect the expected ultimate cost of settling claims occurring prior to the Statement of Financial Position date, but remaining unsettled at that time, and take into account any related reinsurance recoveries. Such reserves are established separately for each line of business underwritten by the Group and fall into two categories – reserves for reported losses and reserves for losses incurred but not reported (IBNR) as of the Statement of Financial Position date.

3. Critical Accounting Estimates and Judgements in Applying Accounting Policies (continued)

Outstanding insurance claims and provisions (continued)

Case reserves for reported losses are estimates prepared by claim handlers established on a case-by-case basis and are based largely on past experience of settlements managed within the Group, as well as market experience on similar claims. The case reserves are set on an undiscounted basis and reflect the anticipated cost of final settlement, taking into account inflation and other factors which might influence the final outcome. Such reserves are reviewed on a regular basis to take account of changing circumstances, such as changes in the law and changes in costs relating to settlement.

Technical provisions for losses IBNR as of the Statement of Financial Position date are mostly established on an undiscounted basis. They are estimated based on historical data using a variety of assumptions and making use of various actuarial techniques and statistical modelling methodologies, calculated separately for each line of business underwritten, and take into account trends in settlement costs in arriving at the final estimates.

Technical provisions on a discounted basis are set up in respect of Periodic Payment Orders (PPOs) only. The expected cashflows arising from known and potential PPO claims are assessed using a variety of assumptions and making use of various actuarial techniques and are calculated at a gross level and a related calculation is carried out to consider expected reinsurance cashflows. The future PPO-related cashflows are discounted using a long-term expected investment return to derive discounted claims provisions and discounted reinsurance provisions.

Scenarios are assessed for the material components of the Group's reserves. For motor damage and smaller bodily injury claims, material scenarios lie in a range between £10m above and £10m below the chosen actuarial best estimate (ABE). Those associated with larger bodily injury claims and PPO claims are in a range between £30m above and £30m below the chosen ABE. This assumes an Ogden discount rate for valuing larger claims of minus 0.25%.

For further details refer to note 21.

4. 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's two operating segments are as follows:

- Banking - incorporating Credit Cards, Personal Loans, Savings, Personal Current Accounts, ATMs, Gift Cards and Travel Money; and
- Insurance - incorporating Motor, Home, Pet and Travel Insurance.

There are no transactions between operating segments.

Following the redemption of the Group's remaining debt securities in issue during the year ended 28 February 2021, the Group is no longer required to provide segmental information. Consequently, the information disclosed in this note relates only to the period ended 31 August 2020.

Segmental assets and liabilities comprise operating assets and liabilities, being the majority of the Interim Condensed Consolidated Statement of Financial Position, but exclude unallocated reconciling items such as taxation.

4. Segmental Reporting (continued)

Segmental results of continuing operations and a reconciliation of segmental results of continuing operations to the total results of continuing operations for the six months to 31 August 2020 are presented below.

	Banking	Insurance	Central costs	Total management reporting	Total consolidated
Continuing operations	**£m**	**£m**	**£m**	**£m**	**£m**
6 months ended 31 August 2020					
Total income	285.0	39.3	–	324.3	324.3
(Loss)/profit before tax from continuing operations[1]	(24.1)	29.6	(149.0)	(143.5)	(143.5)

[1] The Banking and Insurance segments include only directly attributable administrative costs such as marketing and operational costs. Central overhead costs, which reflect the overhead of operating both the Insurance and Banking businesses, are not allocated against an operating segment for internal reporting purposes.

	Banking	Insurance	Total management reporting	Consolidation and other adjustments	Total consolidated
31 August 2020	**£m**	**£m**	**£m**	**£m**	**£m**
Total assets[1]	10,390.0	160.4	10,550.4	99.3	10,649.7
Total liabilities	8,995.3	19.0	9,014.3	-	9,014.3

[1] The investment of £95.9m in TU, a joint venture company accounted for using the equity method, is shown within the total assets of the Insurance segment.

5. Underlying Profit/(Loss)

The Group's financial performance is presented in the Interim Condensed Consolidated Income Statement on page 10. A summary of the Group's financial performance in respect of its continuing operations on an underlying basis, excluding items which are not reflective of ongoing trading performance, is presented below.

	Statutory basis £m	Financial instruments[1] £m	Underlying basis £m
6 months ended 31 August 2021			
Net interest income	215.6	–	215.6
Other income, net of insurance claims	126.1	1.0	127.1
Total income, net of insurance claims	**341.7**	**1.0**	**342.7**
Total operating expenses	(243.8)	–	(243.8)
Expected credit losses	(21.4)	–	(21.4)
Operating profit	**76.5**	**1.0**	**77.5**
Share of profit of joint venture	2.6	–	2.6
Profit before tax	**79.1**	**1.0**	**80.1**

	Statutory basis £m	Financial instruments[1] £m	Underlying basis £m
6 months ended 31 August 2020			
Net interest income	237.9	–	237.9
Other income	86.4	1.3	87.7
Total income	**324.3**	**1.3**	**325.6**
Total operating expenses	(220.2)	–	(220.2)
Expected credit losses	(256.6)	–	(256.6)
Operating loss	**(152.5)**	**1.3**	**(151.2)**
Share of profit of joint venture	9.0	–	9.0
Loss before tax	**(143.5)**	**1.3**	**(142.2)**

[1] Comprising:

- Losses on other financial instruments at FVPL of £1.0m (August 2020: losses of £1.3m) presented within total income on page 10. Fair value movements on other financial instruments at FVPL 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/(loss) 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.

6. Net Interest Income

	6 months ended 31 August 2021 £m	6 months ended 31 August 2020 £m
Continuing operations		
Interest and similar income		
On financial assets measured at amortised cost		
Loans and advances to customers	241.3	291.9
Cash and balances with central banks	0.2	1.0
Investment securities	2.5	7.4
	244.0	300.3
On financial assets measured at fair value		
Investment securities - FVPL	0.2	–
Investment securities - FVOCI	2.0	–
	2.2	–
Total interest and similar income	**246.2**	**300.3**
Interest expense and similar charges		
On financial liabilities measured at amortised cost		
Deposits from customers	(15.0)	(40.0)
Deposits from banks	(1.0)	(0.6)
Debt securities in issue	–	(8.2)
Lease liabilities	(1.1)	(1.2)
Subordinated liabilities and notes	(6.3)	(6.3)
	(23.4)	(56.3)
On financial liabilities measured at fair value		
Derivative financial liabilities - FVPL	(7.2)	(6.1)
	(7.2)	(6.1)
Total interest and similar charges	**(30.6)**	**(62.4)**
Net interest income	**215.6**	**237.9**

7. Net Fees and Commissions Income

	6 months ended 31 August 2021 £m	6 months ended 31 August 2020 £m
Continuing operations		
Fees and commissions income		
Banking revenue from contracts with customers	84.5	74.3
Insurance revenue from contracts with customers	21.2	27.4
Other revenue from contracts with customers	2.6	0.6
Total fees and commissions income	**108.3**	**102.3**
Fees and commissions expense		
Banking expense	(17.4)	(14.6)
Total fees and commissions expense	**(17.4)**	**(14.6)**
Net fees and commissions income	**90.9**	**87.7**

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.

8. Net insurance premium income

	6 months to 31 August 2021 £m	6 months to 31 August 2020 £m
Gross premium written	99.7	–
Change in the gross provision for unearned premium	(5.3)	–
Insurance premium income	94.4	–
Written premium ceded to reinsurers	(42.7)	–
Reinsurers share of change in the provision for unearned premium	0.8	–
Insurance premium income ceded to reinsurers	(41.9)	–
Net insurance premium income	52.5	–

The above net insurance premium income represents income recognised in the Interim Condensed Consolidated Income Statement following acquisition of TU by the Group on 4 May 2021.

9. Net insurance claims

	6 months to 31 August 2021 £m	6 months to 31 August 2020 £m
Current period claims paid	34.5	–
Change in prior year claims provision	(14.0)	–
Additional liabilities arising during the period	40.7	
Insurance claims incurred	61.2	–
Reinsurers share of claims and benefits incurred	(33.8)	–
Insurance claims ceded to reinsurers	(33.8)	–
Net insurance claims	27.4	–

The above net insurance claims represent the claims expense incurred by TU following acquisition by the Group on 4 May 2021.

10. Expected Credit Loss on Financial Assets

	6 months ended 31 August 2021 £m	6 months ended 31 August 2020 £m
Continuing operations		
Expected credit loss on loans and advances to customers[1]	21.1	256.6
Expected credit loss on investment securities at FVOCI	0.9	–
Expected credit loss on investment securities at amortised cost	(0.6)	–
Total expected credit loss on financial assets	**21.4**	**256.6**

Refer to note 23 for further detail on factors impacting expected credit loss charges.

[1] Included within the expected credit loss on loans and advances to customers is an amount of £4.8m (August 2020: £nil) received through the sale of debt to third-parties.

11. 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 2022.

The March 2016 Budget Statement included an announcement that the standard rate of corporation tax in the UK would be reduced from 19% to 17% from 1 April 2020. Subsequently, at the March 2020 Budget Statement, the Chancellor announced that this reduction to 17% would no longer take place, with the standard rate of corporation tax instead being maintained at 19%. The cancellation of the rate reduction resulted in the Group's deferred tax asset increasing by £5.5m during the prior period. The Group's corporation tax rate is 19.0% (August 2020: 19.0%). In addition, a banking surcharge of 8.0% (August 2020: 8.0%) is applied to the results of the Group's banking activities.

In the March 2021 Budget Statement, the Chancellor announced that the standard rate of corporation tax in the UK will increase from 19% to 25% from 1 April 2023. This increase in the corporation tax rate resulted in the Group's deferred tax asset increasing by £9.7m during the period. It was also announced that the level of banking surcharge may be reduced from its current level of 8% from 1 April 2023, although the extent of any such reduction is not expected to be known until mid-2022. For every 1% decrease in the level of banking surcharge, the Group's deferred tax asset would reduce by approximately £1.6m.

Income tax on the Group's profit from continuing operations was a charge of £7.6m (August 2020: £46.6m credit relating to the Group's loss from continuing operations). The tax charge for the period is primarily driven by the increase in the corporation tax rate from 19% to 25% and its impact on the Group's deferred tax assets as outlined above. The prior period credit was driven predominantly by increased ECL charges due to Covid-19.

Income tax on the Group's profit from discontinued operations in the prior period was £0.1m. There were no such discontinued operations in the current period.

12. Capital Expenditure and Commitments

In the six months ended 31 August 2021 there were additions to property, plant and equipment and intangible assets of £19.9m (August 2020: £25.0m). Commitments for capital expenditure contracted for but not provided at 31 August 2021 were £1.9m (February 2021: £0.5m) on property, plant and equipment and £1.4m (February 2021: £2.1m) on intangible assets. The Group's Management are confident that future net revenues and funding will be sufficient to cover these commitments.

13. Loans and Advances to Banks

	31 August 2021 £m	28 February 2021 £m	31 August 2020 £m
Liquidity funds	25.4	–	–
Custodian funds	26.0	–	–
Total loans and advances to banks	**51.4**	–	–

Following the acquisition of TU on 4 May 2021, TU short term liquidity and custodian funds are now included in the Interim Condensed Consolidated Statement of Financial Position.

14. Loans and Advances to Customers

	31 August 2021 £m	28 February 2021 £m	31 August 2020 £m
Unsecured lending	6,981.6	7,020.1	7,918.1
Total secured and unsecured lending	**6,981.6**	**7,020.1**	**7,918.1**
Fair value hedge adjustment	1.7	6.7	16.9
Gross loans and advances to customers	**6,983.3**	**7,026.8**	**7,935.0**
Less: ECL allowance (Refer to note 23)	(579.4)	(624.6)	(649.8)
Net loans and advances to customers	**6,403.9**	**6,402.2**	**7,285.2**

Contractual lending commitments and ECL provision

At 31 August 2021, the Group had contractual lending commitments of £12,506.3m (February 2021: £12,668.0m). An additional ECL provision of £23.7m was also recognised at 31 August 2021 (February 2021: £28.3m). This represents the excess of total ECLs for both drawn and undrawn balances over the gross carrying balances as above. Refer to notes 19 and 23 for further details.

Fair value hedge adjustments

Fair value hedge adjustments amounting to £1.7m (February 2021: £6.7m) are in respect of fixed rate Loans. 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.

15. Investment Securities

	31 August 2021 £m	28 February 2021 £m	31 August 2020 £m
Investment securities measured at FVPL	25.2	–	–
Investment securities measured at FVOCI - debt	603.6	–	–
Investment securities measured at FVOCI - equity	–	5.1	3.6
Investment securities measured at amortised cost	928.8	948.4	872.3
Total investment securities	**1,557.6**	**953.5**	**875.9**

Investment Securities measured at FVPL

	31 August 2021 £m	28 February 2021 £m	31 August 2020 £m
Equity investment	5.6	–	–
Property fund	19.6	–	–
Total investment securities measured at FVPL	**25.2**	**–**	**–**

The Group holds an investment in preferred stock issued by VISA Inc. which was designated at FVOCI in previous years. Following a review of industry practice and the requirements of IFRS 9, this investment has been reclassified to FVPL with effect from 1 March 2021. As this amount is not material, no prior year restatement has been recognised in respect of this reclassification.

During the year ended 28 February 2021, a proportion of these shares became eligible for conversion to ordinary shares, resulting in an unrealised gain of £1.7m which was recognised in the fair value reserve at 28 February 2021. Following the change in classification with effect from 1 March 2021, the opening unrealised gain in respect of the Group's total investment in VISA Inc. preferred stock, amounting to £5.1m (£3.7m net of deferred tax), was transferred from the fair value reserve to retained earnings within the Interim Condensed Consolidated Statement of Changes in Equity. Gains and losses from 1 March 2021 are recognised through the Interim Condensed Consolidated Income Statement.

The remaining stock may be convertible into Class A Common Stock of VISA Inc. at certain future dates, the earliest point at which was June 2021. Conversion is contingent upon future events, principally related to the outcome of interchange litigation against VISA Europe Limited. As such, the valuation of £5.6m (February 2021: £5.1m) 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.

Following the acquisition of TU on 4 May 2021, the TU property fund investment held at FVPL is now included in the Interim Condensed Consolidated Statement of Financial Position.

Investment Securities measured at FVOCI - debt

	31 August 2021 £m	28 February 2021 £m	31 August 2020 £m
Government backed investment securities	49.6	–	–
Supranational investment securities	30.1	–	–
Corporate bonds	523.9	–	–
Total investment securities measured at FVOCI - debt	**603.6**	**–**	**–**

Following the acquisition of TU on 4 May 2021, the TU debt investment securities held at FVOCI at 31 August 2021 are now included in the Interim Condensed Consolidated Statement of Financial Position. Included in investment securities are fixed-interest investment securities totalling £603.6m.

15. Investment Securities (continued)

Investment securities measured at amortised cost

	31 August 2021 £m	28 February 2021 £m	31 August 2020 £m
Government backed investment securities	122.5	126.9	113.9
Gilts	39.0	39.2	40.2
Supranational investment securities	455.1	438.4	393.5
Other investment securities	312.3	323.6	304.6
Investment in subordinated debt issued by TU	–	21.1	21.1
Gross investment securities measured at amortised cost	**928.9**	**949.2**	**873.3**
Less: Allowance for ECL (Refer note 23)	(0.1)	(0.8)	(1.0)
Net investment securities measured at amortised cost	**928.8**	**948.4**	**872.3**

Included in investment securities at amortised cost at 31 August 2021 were fixed-interest investment securities totalling £503.6m (February 2021: £502.5m), and variable-interest investment securities amounting to £425.2m (February 2021: £424.8m).

The investment in subordinated debt issued by TU with a gross carrying value of £21.1m at February 2021 is now fully eliminated on consolidation in the Interim Condensed Consolidated Statement of Financial Position following the acquisition of TU on 4 May 2021. Interest receivable on these notes was based on a rate of three-month London Inter Bank Offered Rate plus a spread ranging from 350-450 basis points.

16. Investment in Joint Venture

The following table shows the aggregate movement in the Group’s investment in its joint venture in the period:

	31 August 2021 £m	28 February 2021 £m	31 August 2020 £m
At beginning of period	92.8	86.0	86.0
Dividends received	(10.0)	(7.5)	–
Share of profit of joint venture	2.6	16.2	9.0
Share of other comprehensive (expense)/income of joint venture	(0.6)	(1.9)	0.9
Reclassification of investment to investment in Group undertakings (refer note 2)	(84.8)	–	–
At end of period	**–**	**92.8**	**95.9**

Details of the Group's joint venture

Name of company	Nature of business	Place of incorporation	Registered address	Ownership Interest 31 August 2021	Ownership Interest 28 February 2021
Tesco Underwriting Limited	Insurance	UK	London Court, 39 London Road, Reigate, Surrey, United Kingdom, RH2 9AQ	100%	49.9%

TU is an authorised insurance company which provides the insurance underwriting service for a number of the Group’s general insurance products. Prior to 4 May 2021, the Group owned 49.9% of TU and the Group accounted for TU as a joint venture, using the equity method of accounting. On 4 May 2021. the Company acquired the remaining 50.1% of TU's ordinary share capital from its joint venture partner. Refer to note 2 for full details of the acquisition.

17. Intangible Assets

	Work-in-Progress	Goodwill	Computer Software	Total
	£m	£m	£m	£m
Cost				
At 1 March 2021	44.4	–	717.6	762.0
Acquisition of TU	–	20.0	18.0	38.0
Additions	9.8	–	5.2	15.0
Transfers	(32.3)	–	32.3	–
Disposals	(0.2)	–	–	(0.2)
At 31 August 2021	**21.7**	**20.0**	**773.1**	**814.8**
Accumulated amortisation				
At 1 March 2021	–	–	(631.1)	(631.1)
Charge for the year	–	–	(23.8)	(23.8)
Disposals	–	–	–	–
At 31 August 2021	**–**	**–**	**(654.9)**	**(654.9)**
Net carrying value				
At 31 August 2021	**21.7**	**20.0**	**118.2**	**159.9**
Cost				
At 1 March 2020	27.8	-	722.4	750.2
Additions	11.7	-	5.9	17.6
Transfers	(1.5)	-	1.3	(0.2)
Disposals	(0.6)	-	(26.8)	(27.4)
At 31 August 2020	37.4	-	702.8	740.2
Accumulated amortisation				
At 1 March 2020	-	-	(612.0)	(612.0)
Charge for the year	-	-	(24.6)	(24.6)
Disposals	-	-	26.5	26.5
At 31 August 2020	-	-	(610.1)	(610.1)
Net carrying value				
At 31 August 2020	37.4	-	92.7	130.1

Goodwill

The acquisition of TU on 4 May 2021 resulted in the recognition of goodwill of £20.0m. Refer to note 2 for further details. This goodwill is supported by the expected increase in cash flows for the combined insurance business.

Impairment methodology

Goodwill is tested annually for impairment or more frequently where there are indicators of impairment. Goodwill recognised on the acquisition of TU is allocated to the insurance segment of the Group which is treated as a separate group of cash-generating units for impairment testing.

The recoverable amount of the cash-generating unit is determined based on value-in-use calculations. Head office and central costs are allocated to the insurance cash-generating unit based on its consumption of the Group's supported services on a cost-plus margin basis.

17. Intangible Assets (continued)

Estimates for value-in-use calculations include discount rates, long-term growth rates and expected changes to future cash flows, including insurance volumes and pricing. Estimates are based on past experience and expectations of future changes in the market, including the prevailing economic climate and global economy, competitor activity, market dynamics and changing customer behaviours.

Cash flow projections are based on the Group's three-year internal forecasts, the results of which are reviewed by the Board. The forecasts are extrapolated to five years based on Management's expectations, and beyond five years based on estimated long-term average growth rates. Long-term growth rates for the Group are based on inflation and gross domestic product (GDP) growth forecasts provided by recognised bodies.

Management estimate discount rates using pre-tax rates that reflect the market assessment as at the Statement of Financial Position date of the time value of money. The pre-tax discount rates are derived from the Group's post-tax weighted average cost of capital, as adjusted for the specific risks relating to each geographical region. Risk-free rates are based on government bond rates in each geographical region and equity risk premia are based on forecasts by recognised bodies.

There were no indicators of impairment at 31 August 2021.

Computer Software

As part of the acquisition of TU on 4 May 2021, the Group has recognised separately identified intangible assets within Computer Software. These represent the fair value of the insurance software acquired.

18. Debt Securities in Issue

	Interest rate	Par value £m	Term (years)	Maturity date	31 August 2021 £m	28 February 2021 £m	31 August 2020 £m
Fixed rate retail bond[1]	5.0%	200.0	8.5	2020	–	–	200.8
Floating rate AAA bond (A1)[2]	1M LIBOR + 0.53%	300.0	5	2022	–	–	300.0
Floating rate AAA bond (A1)[3]	1M USD LIBOR + 0.84%	272.2	7	2025	–	–	261.3
					–	**–**	**762.1**

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

[1] This bond was issued on 21 May 2012.This bond was redeemed in November 2020.

[2] This Bond was issued on 7 November 2017. This bond was redeemed in October 2020.

[3] This bond was issued on 27 November 2018. This bond was redeemed in November 2020.

19. Provisions for Liabilities and Charges

	Customer redress provision	Restructuring provision	Expected credit loss provision	Other provisions	Total
	£m	£m	£m	£m	£m
6 months to 31 August 2021					
At beginning of period	22.4	0.8	28.3	8.6	60.1
Provided during the period	–	–	–	1.7	1.7
Utilised during the period	(3.8)	(0.8)	–	(2.9)	(7.5)
Released during the period	–	–	–	(0.4)	(0.4)
Transfer to ECL	–	–	(4.6)	–	(4.6)
At end of period	**18.6**	**–**	**23.7**	**7.0**	**49.3**

Customer redress provision - Payment protection insurance (PPI)

Of the total customer redress provision balance at 31 August 2021, £18.6m (February 2021: £22.4m) 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 general claims deadline passed on 29 August 2019, albeit legal claims continue to be received. Although a significant degree of uncertainty remains with regard to the ultimate cost of settling PPI claims, the provision balance represents Management's best estimate at the reporting date of that cost and is based on historical uphold rates, average redress and the associated administrative expenses. The PPI provision and the impact of regulatory changes will continue to be monitored as Management finalise their assessment of the significant level of claims received in advance of the claims deadline, ongoing legal claims and levels of redress thereon.

Customer redress provision - Payment protection insurance (continued)

The table below details, for each key assumption, actual data to 31 August 2021 and a sensitivity assessment demonstrating the impact on the provision of a variation in the key assumptions. The key sensitivity in relation to PPI claims received is the conversion rate into an upheld complaint.

		Sensitivity		
Assumption	**Cumulative actual**	**Outstanding claims**	**Change in assumption**	**Consequential change in provision**
				£m
Valid legal PPI claims settled	221	1,725	+/- 100 successful claims	+/- £0.5m
Average redress per valid legal PPI claim	£4,542	£4,542	+/- £100	+/- £0.2m

19. Provisions for Liabilities and Charges (continued)

Restructuring provision

The restructuring provision was in respect of costs related to the Group's strategic review.

Expected Credit Loss provision

The ECL provision represents the amount of ECL allowance recognised under IFRS 9 which exceeds the gross carrying amount of the financial asset as set out at note 23.

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;
- 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 bought back under the terms of the debt sale agreements; and
- a provision in respect of the potential cost of refunding fees to customers.

20. Insurance Funds Withheld

Following the acquisition of TU on 4 May 2021, insurance funds withheld are now included in the Interim Condensed Consolidated Statement of Financial Position.

	31 August 2021
	£m
Insurance funds withheld	106.4
Total insurance funds withheld	**106.4**

TU has put in place a QS contract as part of its overall reinsurance protection strategy. A funds withheld account is maintained which represents the balance due to reinsurers in accordance with the terms of this reinsurance agreement. The balance is made up of QS funds withheld of £138.8m and a profit commission of (£32.4m) (which is part of the contract but is a separate payable).

21. Insurance Contracts Provisions and Reinsurance Assets

Following the acquisition of TU on 4 May 2021, insurance contracts provisions and reinsurance assets are now included in the Interim Condensed Consolidated Statement of Financial Position.

The following tables show the breakdown of the Group's insurance contract provisions and reinsurance assets at 31 August 2021:

	31 August 2021		
	Gross	Reinsurance	Net
	£m	£m	£m
Unearned premiums	146.3	(60.0)	86.3
Claims reported by policy holders	539.1	(283.8)	255.3
Claims incurred but not reported	(30.7)	87.0	56.3
Total insurance contract provisions	**654.7**	**(256.8)**	**397.9**

	31 August 2021		
	Gross	Reinsurance	Net
	£m	£m	£m
Current	189.7	(52.0)	137.7
Non-current	465.0	(204.8)	260.2
Total insurance contract provisions	**654.7**	**(256.8)**	**397.9**

Recoveries are not included above. For details see movement in outstanding claims analysis below.

21. Insurance Contracts Provisions and Reinsurance Assets (continued)

Analysis of movement in insurance provisions

	31 August 2021		
	Gross	Reinsurance	Net
	£m	£m	£m
Balance at 1 March 2021	–	–	–
Acquisition of TU	650.3	(246.7)	403.6
Claims (paid)/recovered from insurers	(61.4)	20.3	(41.1)
Movement in claims incurred but not reported	(14.5)	10.9	(3.6)
Claims reported in the period	75.0	(40.5)	34.5
Change in provisions from unearned premiums	5.3	(0.8)	4.5
At 31 August 2021	**654.7**	**(256.8)**	**397.9**

Analysis of movement in provision for gross unearned premium

	31 August 2021 £m
Balance at 1 March 2021	–
Acquisition of TU	141.0
Premium written during the period	99.7
Less: premiums earned during the period	(94.4)
At 31 August 2021	**146.3**

Analysis of movement in outstanding claims

Gross outstanding claims	31 August 2021 £m
Balance at 1 March 2021	–
Acquisition of TU	509.3
Current period claims	76.5
Change in prior period claims	(16.0)
Current period claims paid	(34.5)
Prior period claims paid	(26.9)
At 31 August 2021	**508.4**

Salvage and subrogation recoveries	31 August 2021 £m
Balance at 1 March 2021	–
Acquisition of TU	16.0
Current period claims	3.2
Change in prior period claims	(3.9)
At 31 August 2021	**15.3**

Gross outstanding claims, net of recoveries	31 August 2021 £m
Balance at 1 March 2021	–
Acquisition of TU	493.3
Current period claims	73.2
Change in prior period claims	(12.0)
Current period claims paid	(34.5)
Prior period claims paid	(26.9)
At 31 August 2021	**493.1**

21. Insurance Contracts Provisions and Reinsurance Assets (continued)

Process used to determine the assumptions

The sources of data used as inputs for the assumptions behind insurance provisions are internal, using detailed studies that are carried out at least annually. The assumptions are checked to ensure that they are consistent with observable market prices or other published information. There is more emphasis on current trends, and where in more recent periods there is insufficient information to make a reliable best estimate of claims development, suitable benchmark assumptions are used.

The nature of the business makes it very difficult to predict with certainty the likely outcome of any particular claim and the ultimate cost of notified claims. Each notified claim is assessed on a separate, case-by-case, basis with due regard to the claim circumstances and historical evidence of the size of similar claims. Case estimates are reviewed regularly and are updated as and when new information arises. The provisions are based on information currently available. However, the ultimate liabilities may vary as a result of subsequent developments. The impact of many of the items affecting the ultimate costs of the loss is difficult to estimate. The degree of complexity involved will also differ by book of business due to differences in the underlying insurance contract, claim complexity, the volume of claims and the individual severity of claims, determining the occurrence date of a claim, and reporting lags.

The cost of outstanding claims and the IBNR provisions are estimated using various statistical methods. Such methods extrapolate the development of paid and incurred claims, average cost per claim and ultimate claim numbers for each accident period based upon observed development of earlier periods, with reference to suitable benchmarks.

The key methods are:

- Development factor methods, which use historical data to estimate the paid and incurred to date as proportions of the ultimate claim cost;
- Individual claim assessment methods, which use claim-specific details for large individual claims to estimate the ultimate claim cost; and
- Benchmarking methods, which use the experience of comparable, more mature classes, or market data to estimate the cost of claims.

The actual method or blend of methods used varies by accident period being considered and the class of business and observes historical claims development.

To the extent that these methods use historical claims development information, they assume that the historical claims development pattern will occur again in the future. There are reasons why this may not be the case, which, insofar as they can be identified, have been allowed for by modifying the methods. Such reasons include:

- Changes in processes that affect the development and/or recording of claims paid and incurred (such as changes in claim reserving procedures and/or the introduction of a new claims system);
- Economic, legal, political and social trends (resulting in, for example, a difference in expected levels of inflation);
- Changes in mix of business; and
- Random fluctuations, including the impact of large losses.

IBNR provisions are initially estimated at a gross level and a separate calculation is carried out to estimate the size of reinsurance recoveries. The Group is covered by a variety of excess of loss reinsurance programmes. The methods used by the Group take account of historical data, specific details for individual large claims and details of the reinsurance programme, to assess the expected size of reinsurance recoveries.

21. Insurance Contracts Provisions and Reinsurance Assets (continued)

Process used to determine the assumptions (continued)

The Group considers that the liability for claims reported in the Interim Condensed Consolidated Statement of Financial Position is adequate. However, it recognises that the process of estimation is based upon certain variables and assumptions, which could differ when claims arise.

Recoveries through salvage and subrogation are estimated and recorded separately within other assets based on a combination of suitable benchmark assumptions and the observed development to date.

Ogden rate

The personal injury discount rate (Ogden rate) is set by the Ministry of Justice and is used by the courts to calculate lump sum personal injury payments. Reserves are assessed at the current rate of -0.25%.

Analysis of claims development – gross of reinsurance and net of salvage and subrogation recoveries

	Accident year										
	2012 £m	**2013 £m**	**2014 £m**	**2015 £m**	**2016 £m**	**2017 £m**	**2018 £m**	**2019 £m**	**2020 £m**	**2021 £m**	**Total £m**
Estimate of gross ultimate claim costs											
At end of accident year	529.8	390.6	349.3	327.1	370.7	304.3	317.4	282.2	219.7	144.1	3,235.2
One year later	534.4	388.4	352.7	343.2	372.1	298.8	296.7	288.1	220.3	–	3,094.7
Two years later	522.5	372.6	379.1	343.1	335.0	269.3	267.9	294.2	–	–	2,783.7
Three years later	517.3	382.8	352.9	322.7	324.5	258.3	266.8	–	–	–	2,425.3
Four years later	526.8	362.5	359.7	311.5	322.9	255.6	–	–	–	–	2,139.0
Five years later	517.7	360.3	346.9	304.9	311.2	–	–	–	–	–	1,841.0
Six years later	520.3	360.8	349.9	303.8	–	–	–	–	–	–	1,534.8
Seven years later	518.9	360.3	347.3	–	–	–	–	–	–	–	1,226.5
Eight years later	526.8	360.3	–	–	–	–	–	–	–	–	887.1
Nine years later	527.9	–	–	–	–	–	–	–	–	–	527.9
Current estimate of cumulative claims	527.9	360.3	347.3	303.8	311.2	255.6	266.8	294.2	220.3	144.1	3,031.5
Cumulative payments to date	(504.2)	(347.8)	(326.8)	(287.4)	(285.3)	(237.2)	(216.6)	(179.9)	(114.2)	(53.9)	(2,553.3)
Claims outstanding prior to 2012 accident year											6.3
Current gross claims provision	**23.7**	**12.5**	**20.5**	**16.4**	**25.9**	**18.4**	**50.2**	**114.3**	**106.1**	**90.2**	**484.5**
Provision for claims handling costs	–	–	–	–	–	–	–	–	–	–	8.6
Total gross claims outstanding provisions	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**493.1**

21. Insurance Contracts Provisions and Reinsurance Assets (continued)

Analysis of claims development – net of reinsurance and net of salvage and subrogation recoveries

	Accident year										
	2012	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Estimate of net ultimate claim costs											
At end of accident year	–	–	–	–	–	–	–	–	–	–	–
One year later	–	–	–	–	–	–	–	–	–	–	–
Two years later	515.5	378.8	336.0	319.5	310.5	276.0	259.0	235.7	143.9	92.4	2,867.3
Three years later	521.9	380.3	338.2	327.2	319.2	269.7	259.3	254.7	126.2	–	2,796.7
Four years later	512.4	367.9	348.9	330.7	302.0	252.0	233.4	257.9	–	–	2,605.2
Five years later	506.6	371.5	342.6	314.8	291.7	241.5	233.8	–	–	–	2,302.5
Six years later	505.4	358.9	339.1	305.8	292.5	241.5	–	–	–	–	2,043.2
Seven years later	500.3	355.2	338.0	300.7	287.3	–	–	–	–	–	1,781.5
Eight years later	503.6	356.2	339.9	299.5	–	–	–	–	–	–	1,499.2
Nine years later	503.3	355.1	337.8	–	–	–	–	–	–	–	1,196.2
Current estimate of cumulative claims	505.8	354.5	337.8	299.5	287.3	241.5	233.8	257.8	126.2	92.4	2,736.6
Cumulative payments to date	(497.9)	(346.8)	(322.5)	(285.1)	(274.8)	(228.5)	(207.1)	(179.1)	(84.7)	(27.0)	(2,453.5)
Claims outstanding prior to 2012 accident year											4.6
Current net claims provision	**7.9**	**7.7**	**15.3**	**14.4**	**12.5**	**13.0**	**26.7**	**78.7**	**41.5**	**65.4**	**287.7**
Provision for claims handling costs	–	–	–	–	–	–	–	–	–	–	8.6
Total net claims outstanding provisions	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**296.3**

22. Subordinated Liabilities and Notes

	31 August 2021	28 February 2021	31 August 2020
	£m	£m	£m
Amortised cost:			
Fixed rate subordinated loan	250.8	251.6	254.4
Floating rate subordinated loans	190.0	190.0	190.0
Undated floating rate notes	45.0	45.0	45.0
Total subordinated liabilities and notes	**485.8**	**486.6**	**489.4**

Subordinated liabilities and notes comprise loan capital issued to Tesco Personal Finance Group plc (TPFG). This includes £250.0m notional (February 2021: £250.0m notional)[1] of subordinated loans maturing in 2025, £190.0m (February 2021: £190.0m) of subordinated loans maturing in 2030 and £45.0m (February 2021: £45.0m) of undated notes with no fixed maturity date.

Interest payable on the fixed rate intercompany subordinated loan is 3.5%. Interest payable on the floating rate subordinated loans and notes is based on three-month Sterling Overnight Index Average (SONIA) plus a margin of 67 to 227 basis points (February 2021: three month SONIA plus a margin of 67 to 227 basis points).

[1] The Group is 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 2023. The requirements are factored into the Group's funding and capital plans.

23. Credit risk management

Full details of the Group's risk management are included in the Group's Consolidated Financial Statements for the year ended 28 February 2021. Updates on key areas of credit risk management and ECL measurement are included below.

- **Credit risk: ECL measurement**

Incorporation of forward-looking information

The ECL 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 historical patterns observed over a range of economic cycles.

Past due and impaired definitions

The Group considers exposures to be past due where a customer does not make the minimum contractual monthly payment of principal, interest or fee. For Personal Current Accounts, past due status can also arise when the account is in excess of its contractual overdraft limit. Accounts remain as past due but not impaired until the point where a loss trigger has occurred.

An asset will be initially recognised as impaired in response to the following loss triggers:

- Where the customer makes a declaration of significant financial difficulty and is placed on a temporary interest free repayment plan or permanent reduction in annual percentage rate;
- Where the customer or third-party agency communicates that it is probable that the customer will enter bankruptcy or another form of financial re-structure, e.g. insolvency or repossession;
- Where the account has been transferred to recoveries and the relationship is terminated;
- When the customer is more than 90 days past due (the equivalent of four payments down) for Personal Loans and Credit Cards; or
- Where the customer is deceased.

These definitions align to both statutory and regulatory reporting and comply with the requirements of each. The Group has no past-due exposures of more than 90 days that are not considered to be impaired.

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.

At 31 August 2020, the Group commissioned four scenarios from its third-party provider, all of which were based on an economic outlook that sought to take account of the potential ramifications of the current COVID-19 pandemic. These scenarios included a Base scenario, an Upside scenario and two different Downside scenarios. These scenarios were assigned weightings of 50%, 34%, 15% and 1% respectively:

- The Base scenario anticipated a delayed economic recovery, with consumer confidence remaining weak in the near term and unemployment peaking in Q4 2020.
- The Upside scenario involved a sharper economic recovery.
- Downside 1 scenario assumed a longer delay until the economy recovered.
- Downside 2 scenario assumed a prolonged and sustained recession with a slow economic recovery thereafter.

In selecting the Downside scenarios, the Group explored the extremities of potential economic impacts and, as a result, these Downside scenarios were given a lesser weighting due to the context of the Base and Upside scenarios also taking into account the severe impact of the pandemic on the UK economy.

23. Credit risk management (continued)

Past due and impaired definitions (continued)

At 28 February 2021, the Group commissioned four scenarios from its third-party provider, all of which were based on an economic outlook that sought to take account of the potential ramifications of the current COVID-19 pandemic. These scenarios included a Base scenario, an Upside scenario and two different Downside scenarios. These scenarios were assigned weightings of 40%, 30%, 25% and 5% respectively. As the economic outlook remained uncertain, the Group's scenarios were based on the success of the Covid-19 vaccine roll out against emerging strains of the virus and, as the restrictions were lifted, the speed at which consumer and business confidence would support the recovery of GDP and the labour market:

- The Base scenario anticipated GDP in Q4 2021 would be 3.7% lower than Q4 2019 and it would take until Q3 2023 to recover the loss of output. Unemployment was expected to peak in Q3 2021 at 8.0%.
- The Upside scenario involved a sharper economic recovery with the loss of output due to the Covid-19 pandemic fully recovered by Q4 2021. Unemployment was expected to peak in Q2 2021 at 6.7%.
- Downside 1 scenario assumed a longer delay, with GDP not expected to recover from its pre-Covid-19 pandemic level until Q3 2024. Unemployment was expected to peak in Q4 2021 at 9.6%.
- Downside 2 scenario assumed an even longer recovery, with pre-Covid-19 pandemic output only recovered by Q3 2025. Unemployment was expected to peak in Q4 2021 at 10.8%.

At 31 August 2021, the Group continued to use four economic scenarios, which projected different shapes of recovery from the Covid-19 pandemic. These scenarios included a Base scenario, an Upside scenario and two different Downside scenarios. These scenarios were assigned weightings of 40%, 30%, 25% and 5% respectively.

- The Base scenario anticipates a return to pre-pandemic GDP level by Q4 2021 driven by strong consumer spending following easing of restrictions. This is discussed in more detail below.
- The Upside scenario expects a stronger response to the easing of restrictions, with consumers utilising savings built up during lockdown. Unemployment was expected to peak in Q2 2021 at 6.7%.
- The Downside 1 scenario assumes a slower recovery, with transmission of the Delta variant resulting in a tiered system of restrictions remaining until Q1 2022. Unemployment is expected to peak in Q1 2022 at 8.4%.
- The Downside 2 scenario assumes further mutations of the Covid-19 virus, with vaccines proving ineffective against new variants, resulting in further national lockdowns across Q4 2021. Unemployment is expected to peak in Q1 2022 at 10.2%.

These scenarios are also reviewed to ensure an unbiased estimate of ECLs by ensuring the credit loss distribution under a larger number of scenarios is adequately captured using these scenarios and their respective weightings.

Central Scenario

Following the significant negative impact on UK economic activity in 2020 as a result of government measures to combat Covid-19, the Group’s central scenario projects an effective recovery in 2021, with GDP expected to rebound to its 2019 position by Q4 of this year.

The UK government announced the lifting of almost all Covid-19 legal restrictions on 19 July 2021, while the Scottish government followed suit on 9 August 2021. As indoor hospitality businesses have been allowed to resume trading, a strong rebound in the hospitality sector across the period has been observed. The removal of social distancing restrictions is expected to drive further strong growth across Q3, with consumer spending expected to increase significantly as a result of growing confidence driven by the vaccine rollout, supported by households utilising savings balances accrued during lockdowns.

In the latter stages of 2021, GDP growth is expected to slow as pent-up demand is satisfied, and unemployment levels are expected to rise following the end of the government furlough scheme. Unemployment is expected to peak at 6.9% in the fourth quarter of the year as firms are required to make a greater contribution to the wages of furloughed workers.

23. Credit risk management (continued)

Central Scenario (continued)

The Bank of England base rate is assumed to follow market expectations, with the first increases from the current rate of 0.1% expected to occur in Q3 2022. The scenario expects a tightening of credit conditions across the near to medium term. However, financial institutions are better capitalised than they were going into the 2008/09 recession and are therefore expected to be able to avoid a credit crunch.

The central scenario in place for the half year is more optimistic than the one that was applied at 28 February 2021. Previously, the long-term outlook was for GDP to be around 5% lower than the pre-pandemic central scenario. However, the revised central scenario now assumes this to only be 2% lower, highlighting the improvement in the macro-economic environment. The previous scenario also assumed an end to the furlough scheme on 30 April 2021. This has been revised as a result of the extension of government support. This enhanced support reduces the peak of unemployment from 7.2% assumed at 28 February 2021 to 6.9% at 31 August 2021.

23. Credit risk management (continued)

The tables below show the key macro-economic variables in each scenario at each reporting date, across a five calendar year period. The 2022 variables represent a full calendar year forecast containing six months of actual figures.

The economic scenarios used include the following ranges of key indicators:

As at 31 August 2021

Scenario	Weighting	Sensitivity (100% weighted)[3]	Economic measure	2021	2022	2023	2024	2025
		£m		%	%	%	%	%
Base	40%	(7.8)	Bank of England base rate[1]	0.1	0.2	0.5	0.6	0.8
			Gross domestic product[2]	8.6	2.6	1.7	1.3	1.6
			Unemployment rate[1]	6.3	5.7	4.8	4.3	4.1
			Unemployment rate peak in year	6.9	6.3	5.0	4.5	4.1
Upside	30%	(28.0)	Bank of England base rate[1]	0.1	0.4	0.7	0.9	1.0
			Gross domestic product[2]	12.0	2.1	1.5	1.3	1.6
			Unemployment rate[1]	5.8	4.5	4.1	4.1	4.0
			Unemployment rate peak in year	6.7	4.9	4.2	4.1	4.1
Downside 1	25%	31.3	Bank of England base rate[1]	0.1	0.1	0.2	0.3	0.4
			Gross domestic product[2]	5.6	3.5	1.8	1.3	1.6
			Unemployment rate[1]	7.0	7.9	6.5	5.3	4.4
			Unemployment rate peak in year	8.3	8.4	7.1	5.8	4.7
Downside 2	5%	78.9	Bank of England base rate[1]	0.1	(0.1)	(0.1)	0.1	0.2
			Gross domestic product[2]	3.4	3.1	2.0	1.3	1.6
			Unemployment rate[1]	7.7	10.1	9.3	7.9	6.2
			Unemployment rate peak in year	10.0	10.2	9.7	8.6	6.9
Weighted scenarios			Bank of England base rate[1]	0.1	0.2	0.5	0.6	0.7
			Gross domestic product[2]	8.6	2.7	1.7	1.3	1.6
			Unemployment rate[1]	6.4	6.1	5.3	4.7	4.3
			Unemployment rate peak in year	7.1	6.6	5.5	4.9	4.4

[1] Simple average
[2] Annual growth rates
[3] Represents the impact on ECL provision if 100% weighting applied to each macro-economic scenario.

23. Credit risk management (continued)

As at 28 February 2021

Scenario	Weighting	Sensitivity (100% weighted)[3]	Economic measure	2021	2022	2023	2024	2025
		£m		%	%	%	%	%
Base	40%	(1.1)	Bank of England base rate[1]	0.1	0.1	0.1	0.1	0.2
			Gross domestic product[2]	4.7	3.2	1.8	1.6	1.6
			Unemployment rate	7.7	6.4	4.9	4.3	4.1
			Unemployment rate peak in year	8.0	7.2	5.3	4.5	4.1
Upside	30%	(65.8)	Bank of England base rate[1]	0.1	0.1	0.1	0.2	0.4
			Gross domestic product[2]	9.5	2.6	1.6	1.8	1.8
			Unemployment rate	6.4	4.7	4.2	4.1	4.0
			Unemployment rate peak in year	6.7	5.2	4.2	4.1	4.1
Downside 1	25%	56.8	Bank of England base rate[1]	–	–	0.1	0.1	0.1
			Gross domestic product[2]	2.0	3.5	1.9	1.8	1.8
			Unemployment rate	8.6	8.6	6.8	5.3	4.4
			Unemployment rate peak in year	9.6	9.3	7.5	5.8	4.7
Downside 2	5%	116.8	Bank of England base rate[1]	–	(0.1)	0.1	0.1	0.1
			Gross domestic product[2]	(1.0)	4.4	2.2	1.8	1.8
			Unemployment rate	9.4	10.4	9.3	7.8	6.2
			Unemployment rate peak in year	10.8	10.7	9.7	8.4	6.8
Weighted scenarios			Bank of England base rate[1]	0.1	0.1	0.1	0.1	0.3
			Gross domestic product	5.2	3.2	1.8	1.7	1.7
			Unemployment rate	7.6	6.6	5.4	4.7	4.3
			Unemployment rate peak in year	8.2	7.3	5.7	4.9	4.4

[1] Simple average
[2] Annual growth rates
[3] Represents the impact on ECL provision if 100% weighting applied to each macro-economic scenario.

23. Credit risk management (continued)

As at 31 August 2020

Scenario	Weighting	Sensitivity (100% weighted)[3]	Economic measure	2020	2021	2022	2023	2024
		£m		%	%	%	%	%
Base	50%	24.4	Bank of England base rate[1]	0.3	0.1	0.1	0.1	0.1
			Gross domestic product[2]	(9.6)	9.2	2.6	1.6	1.6
			Unemployment rate[1]	6.8	8.4	6.4	5.2	4.5
			Unemployment rate peak in year	9.4	9.2	7.0	5.5	4.7
Upside	34%	(82.9)	Bank of England base rate[1]	0.3	0.1	0.1	0.1	0.1
			Gross domestic product[2]	0.4	2.5	1.8	1.8	1.8
			Unemployment rate[1]	5.6	5.3	4.6	4.3	4.2
			Unemployment rate peak in year	6.2	5.8	4.8	4.3	4.2
Downside 1	15%	99.0	Bank of England base rate[1]	0.3	0.1	0.1	0.1	0.1
			Gross domestic product[2]	(11.8)	8.1	2.1	1.8	1.8
			Unemployment rate[1]	7.5	10.8	10.3	9.1	7.9
			Unemployment rate peak in year	11.0	11.0	10.6	9.7	8.3
Downside 2	1%	180.8	Bank of England base rate[1]	0.3	0.1	0.1	0.1	0.1
			Gross domestic product[2]	(13.3)	7.2	2.7	2.0	1.8
			Unemployment rate[1]	8.4	13.2	13.1	12.7	11.4
			Unemployment rate peak in year	13.3	13.3	13.2	13.0	12.1
Weighted scenarios			Bank of England base rate[1]	0.3	0.1	0.1	0.1	0.1
			Gross domestic product[2]	(6.5)	6.7	2.2	1.7	1.7
			Unemployment rate[1]	6.5	7.8	6.4	5.5	5.0
			Unemployment rate peak in year	8.6	8.3	6.8	5.8	5.2

[1] Simple average
[2] Annual growth rates
[3] Represents the impact on ECL provision if 100% weighting applied to each macro-economic scenario.

23. Credit risk management (continued)

Sensitivity analysis

As the calculation of ECLs is complex and involves use of judgement, sensitivity analysis has been performed to illustrate the impact on ECLs of any changes to the main components of the calculation. The effect of applying a 100% weighting to each of the macro-economic scenarios, as well as the impact on ECLs as a result of changes in LGD, staging, PD and expected lifetime, have been assessed.

Most of the sensitivities have been calculated as single-factor sensitivities and any impact on ECL reflects the sensitivity of the estimate to each key component in isolation. However, the PD and macro-economic sensitivities also include a rebasing of the staging allocation and thresholds. The impact of these is therefore incorporated within the impact disclosed for these sensitivities.

The most significant assumptions affecting the ECL calculation are as follows:

- PD;
- LGD;
- Macro-economic scenarios;
- PD threshold (staging); and
- Expected lifetime of revolving credit facilities.

For further details on each of these assumptions refer to the Consolidated Financial Statements of the Group for the year ended 28 February 2021.

Set out below are changes in the ECL allowance that would arise from reasonably possible changes in these assumptions from those used in the Group's calculations at 31 August 2021:

		Impact on the loss allowance		
		31 August 2021 £m	28 February 2021 £m	31 August 2020 £m
Closing ECL allowance		**579.4**	624.6	649.8
Macro economic (100% weighting)	Upside	(28.0)	(65.8)	(82.9)
	Base	(7.8)	(1.1)	24.4
	Downside 1	31.3	56.8	99.0
	Downside 2	78.9	116.8	180.8
PD	Increase of 2.5%	7.3	7.5	13.1
	Decrease of 2.5%	(7.1)	(7.5)	(13.2)
LGD	Increase of 2.5%	8.9	10.3	14.9
	Decrease of 2.5%	(8.9)	(10.4)	(15.0)
Staging - change in threshold	Increase of 20%	(9.2)	(7.4)	(18.6)
	Decrease of 20%	12.4	10.6	20.6
Expected lifetime (revolving credit facilities)	Increase of 1 year	10.9	9.3	3.8
	Decrease of 1 year	(9.7)	(8.7)	(4.0)

23. Credit risk management (continued)

Management Overlays

The Covid-19 pandemic has had a significant impact on the global economy and there remains a large degree of uncertainty around the impact on unemployment and the speed and shape of any economic recovery. The extension of government support measures such as furlough has been unprecedented and this, coupled with the granting of payment holidays by the Group, has distorted the historically observed relationship between unemployment and defaults.

Projected levels of unemployment have fallen from the expectation held at year end. However, the Group has yet to see significant defaults emerge from its lending portfolio and, as such, Covid-19 specific adjustments to the Group's modelled ECL provision to capture the estimated impact of the stress have been recognised as follows:

- Management has assessed that the beneficial impact of lower consumer spending through the Covid-19 pandemic, which has resulted in an improvement in credit scores, as well as other inputs to ECL such as lower EADs on the Credit Cards portfolio, will have suppressed ECLs. A post-model adjustment (PMA) of £173.6m is held in this respect, calculated from pre Covid-19 pandemic coverage rates and based upon credit limits but reduced in line with the reduction in portfolio utilisation observed during the period. An increase or decrease of 10% on the adjustment for lower drawn balances would increase or decrease this overlay by £14.1m. This PMA reflects Management's belief that the level of risk prior to the emergence of Covid-19 is more reflective of future ECLs.
- Management has assessed that the emergence of customer defaults will be much more aligned with previous economic downturns. A PMA of £57.3m is held at 31 August 2021 in respect of this uncertainty. Extending the emergence of defaults by 6 months increases the overlay by £39.8m, while reducing it by 6 months decreases the overlay by £46.4m.
- A review of arrears emergence from those customers who sought an extension to their initial payment holiday has suggested there has been an increase in credit risk in respect of these customers and, as such, these accounts have been moved to Stage 2 with a PMA of £8.7m held to reflect the estimated increase in ECLs for these customers.
- A PMA of £63.6m was held at 28 February 2021 as Management assessed that the impact of customer support measures was suppressing arrears and defaults. With the ending of these measures, Management has assessed that this PMA is not required at 31 August 2021.

Credit risk: credit risk exposure

Maximum exposure to credit risk

The table below represents the Group's maximum exposure to credit risk, by IFRS 9 stages at the reporting date, in respect of financial assets held.

For financial assets, the balances are based on gross carrying amounts as reported in the Interim Condensed Consolidated Statement of Financial Position. For loan commitments, the amounts in the table represent the amounts for which the Group is contractually committed.

23. Credit risk management (continued)

Maximum exposure to credit risk (continued)

As at 31 August 2021	Stage 1	Stage 2				Stage 3	Total
		Not past due	<30 days past due	>30 days past due	Total		
	£m	£m	£m	£m	£m	£m	£m
Gross Exposure							
Loans and advances to customers	5,955.4	777.0	21.4	19.8	818.2	208.0	6,981.6
Investment securities at FVOCI	603.6	–	–	–	–	–	603.6
Investment securities at amortised cost	928.9	–	–	–	–	–	928.9
Loan commitments - Loans and advances to customers[1]	12,196.3	302.7	1.8	0.5	305.0	5.0	12,506.3
Total gross exposure	19,684.2	1,079.7	23.2	20.3	1,123.2	213.0	21,020.4
Loss allowance							
Loans and advances to customers[1]	132.4	300.8	8.6	11.8	321.2	125.8	579.4
Investment securities at FVOCI[2]	0.9	–	–	–	–	–	0.9
Investment securities at amortised cost	0.1	–	–	–	–	–	0.1
Total loss allowance	133.4	300.8	8.6	11.8	321.2	125.8	580.4
Net exposure							
Loans and advances to customers	5,823.0	476.2	12.8	8.0	497.0	82.2	6,402.2
Investment securities at FVOCI	602.7	–	–	–	–	–	602.7
Investment securities at amortised cost	928.8	–	–	–	–	–	928.8
Total net exposure	**7,354.5**	**476.2**	**12.8**	**8.0**	**497.0**	**82.2**	**7,933.7**
Coverage							
Loans and advances to customers	2.2%	38.7%	40.2%	59.6%	39.3%	60.5%	8.3%

[1] The loss allowance in respect of loan commitments is included within the total loss allowance for loans and advances to customers as above to the extent that it is below the gross carrying amount of loans and advances to customers. Where the loss allowance exceeds the gross carrying amount, any excess is included within provisions as set out at note 19.

[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.

23. Credit risk management (continued)

Maximum exposure to credit risk (continued)

	Stage 1	Stage 2				Stage 3	Total
As at February 2021		Not past due	<30 days past due	>30 days past due	Total		
Group and Company	£m	£m	£m	£m	£m	£m	£m
Gross Exposure							
Loans and advances to customers	5,748.5	980.5	24.9	24.6	1,030.0	241.6	7,020.1
Investment securities at FVOCI[1]	5.1	–	–	–	–	–	5.1
Investment securities at amortised cost[1]	949.2	–	–	–	–	–	949.2
Loan commitments - Loans and advances to customers[2]	12,378.9	282.9	2.3	0.3	285.5	3.6	12,668.0
Total gross exposure	**19,081.7**	**1,263.4**	**27.2**	**24.9**	**1,315.5**	**245.2**	**20,642.4**
Loss allowance							
Loans and advances to customers[2]	132.3	312.5	11.1	15.7	339.3	153.0	624.6
Investment securities at FVOCI[3]	–	–	–	–	–	–	–
Investment securities at amortised cost[1]	0.8	–	–	–	–	–	0.8
Total loss allowance	**133.1**	**312.5**	**11.1**	**15.7**	**339.3**	**153.0**	**625.4**
Net Exposure							
Loans and advances to customers	5,616.2	668.0	13.8	8.9	690.7	88.6	6,395.5
Investment securities at FVOCI	5.1	–	–	–	–	–	5.1
Investment securities at amortised cost	948.4	–	–	–	–	–	948.4
Total net exposure	**6,569.7**	**668.0**	**13.8**	**8.9**	**690.7**	**88.6**	**7,349.0**
Coverage							
Loans and advances to customers	2.3%	31.9%	44.6%	63.8%	32.9%	63.3%	8.9%

[1] On 1 March 2020 the Group's portfolio of debt investment securities measured at FVOCI was reclassified to amortised cost following a change in business model.

[2] The loss allowance in respect of loan commitments is included within the total loss allowance for loans and advances to customers and assets of the disposal group as above to the extent that it is below the gross carrying amount of loans and advances to customers or assets of the disposal group. Where the loss allowance exceeds the gross carrying amount, any excess is included within provisions as set out at note 19.

[3] 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.

23. Credit risk management (continued)

Maximum exposure to credit risk (continued)

As at 31 August 2020	Stage 1	Stage 2				Stage 3	Total
		Not past due	<30 days past due	>30 days past due	Total		
	£m	£m	£m	£m	£m	£m	£m
Gross Exposure							
Loans and advances to customers	6,396.8	1,176.8	25.8	14.9	1,217.5	303.8	7,918.1
Investment securities at FVOCI[1]	3.6	–	–	–	–	–	3.6
Investment securities at amortised cost[1]	873.3	–	–	–	–	–	873.3
Loan commitments - Loans and advances to customers[2]	12,080.5	243.2	–		243.2	1.2	12,324.9
Total gross exposure	19,354.2	1,420.0	25.8	14.9	1,460.7	305.0	21,119.9
Loss allowance							
Loans and advances to customers[2]	109.1	302.3	15.4	11.3	329.0	211.7	649.8
Investment securities at FVOCI[3]	–	–	–	–	–	–	–
Investment securities at amortised cost[1]	1.0	–	–	–	–	–	1.0
Total loss allowance	110.1	302.3	15.4	11.3	329.0	211.7	650.8
Net exposure							
Loans and advances to customers	6,287.7	874.5	10.4	3.6	888.5	92.1	7,268.3
Investment securities at FVOCI	3.6	–	–	–	–	–	3.6
Investment securities at amortised cost	872.3	–	–	–	–	–	872.3
Total net exposure	**7,163.6**	**874.5**	**10.4**	**3.6**	**888.5**	**92.1**	**8,144.2**
Coverage							
Loans and advances to customers	1.7%	25.7%	59.7%	75.8%	27.0%	69.7%	8.2%

[1] On 1 March 2020 the Group's portfolio of debt investment securities measured at FVOCI was reclassified to amortised cost following a change in business model.

[2] The loss allowance in respect of loan commitments is included within the total loss allowance for loans and advances to customers and assets of the disposal group as above to the extent that it is below the gross carrying amount of loans and advances to customers or assets of the disposal group. Where the loss allowance exceeds the gross carrying amount, any excess is included within provisions as set out at note 19.

[3] 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.

The table below provides details of financial assets held at FVPL which are not subject to impairment.

	Maximum exposure to credit risk		
	31 August 2021	28 February 2021	31 August 2020
	£m	£m	£m
Derivative financial assets	5.6	6.1	6.8
Investment securities - property fund	19.6	–	–
Investment securities - equity investment	5.6	5.1	3.6
Cash and balances with central banks	25.5	13.2	24.1
Total	**56.3**	**24.4**	**34.5**

23. Credit risk management (continued)

Maximum exposure to credit risk (continued)

The table below shows a breakdown of Stage 2 loans and advances to customers.

	Maximum exposure to credit risk	
	Gross Loans and Advances	Total ECL
	£m	£m
At 31 August 2021		
Currently > 30 days past due	19.8	11.8
Currently < 30 days past due	798.4	309.4
- PD threshold	764.0	292.9
- Business rules only	34.4	16.5
Total Stage 2 at 31 August 2021	818.2	321.2

	Maximum exposure to credit risk	
	Gross Loans and Advances	Total ECL
	£m	£m
At 31 August 2020		
Currently > 30 days past due	14.9	11.3
Currently < 30 days past due	1,202.6	317.7
- PD threshold	1,101.5	280.0
- Business rules only	101.1	37.7
Total Stage 2 at 31 August 2020	1,217.5	329.0

23. Credit risk management (continued)

Credit risk: Loss allowance

Loss allowance reconciliation

The following table provides a reconciliation of the movements in the loss allowance in the period:

6 months to 31 August 2021	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Loans and advances to customers - loss allowance				
At 1 March 2021	132.3	339.3	153.0	624.6
Transfers[1,3]				
Transfers from stage 1 to stage 2	(5.1)	5.1	–	–
Transfers from stage 2 to stage 1	17.1	(17.1)	–	–
Transfers to stage 3	(3.5)	(28.5)	32.0	–
Transfers from stage 3	0.9	2.8	(3.7)	–
Income statement charge				
Net remeasurement[2] following transfer of stage[3]	(12.0)	1.3	26.8	16.1
New financial assets originated[4]	14.8	1.8	0.5	17.1
Financial assets derecognised during the period	(6.8)	(7.7)	(2.4)	(16.9)
Changes in risk parameters and other movements[3,5]	(7.3)	22.6	12.1	27.4
Other movements				
Write-offs and asset disposals[6]	–	(1.0)	(92.5)	(93.5)
Transfer from provisions for liabilities and charges[7]	2.0	2.6	–	4.6
ECL allowance at 31 August 2021	**132.4**	**321.2**	**125.8**	**579.4**
Investment securities at FVOCI - loss allowance				
At 1 March 2021	–	–	–	–
Income statement charge				
Acquisition of TU	1.0	–	–	1.0
Changes in risk parameters and other movements	(0.1)	–	–	(0.1)
ECL allowance at 31 August 2021	**0.9**	**–**	**–**	**0.9**
Investment securities at amortised cost - loss allowance				
At 1 March 2021	0.8	–	–	0.8
Income statement charge				
Changes in risk parameters and other movements	(0.6)	–	–	(0.6)
Other movements				
TU sub debt[8]	(0.1)	–	–	(0.1)
ECL allowance at 31 August 2021	**0.1**	**–**	**–**	**0.1**
Reconciliation to income statement				
Net expected credit loss charge	(11.0)	18.0	37.0	44.0
Recoveries and write-offs	–	–	(22.6)	(22.6)
Total income statement charge	**(11.0)**	**18.0**	**14.4**	**21.4**

[1] Transfers - The opening loss allowance on financial assets in respect of continuing operations which transferred stage during the period.

[2] Net remeasurement - The increase/(decrease) in the opening loss allowance as a result of a stage transfer.

[3] Includes a charge in stages 1 and 2 of £57.1m due to a change in macro-economic assumptions.

[4] New financial assets originated or purchased - The loss allowance on new financial assets originated or purchased during the period, representing their stage at 31 August 2021.

[5] Changes in risk parameters and other movements - The change in loss allowance due to changes in macro-economic scenarios, PD, LGD and exposure at default (EAD) changes during the period.

[6] Write-offs and asset disposals - The release of the loss allowance following the write off and/or disposal of a financial asset during the period.

[7] Transfer from provisions for liabilities and charges - The movement in loss allowance which exceeds the gross carrying amount of the financial asset.

[8] The Group investment in subordinated debt issued by TU is now fully eliminated in the Interim Condensed Consolidated Statement of Financial Position following the acquisition of TU on 4 May 2021.

23. Credit risk management (continued)

Credit risk: Loss allowance (continued)

Loss allowance reconciliation (continued)

6 months to 31 August 2020	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Loans and advances to customers - loss allowance				
At 1 March 2020	84.1	218.6	185.7	488.4
Transfers[1,3]				
Transfers from stage 1 to stage 2	(18.8)	18.8	–	–
Transfers from stage 2 to stage 1	8.9	(8.9)	–	–
Transfers to stage 3	(1.1)	(33.7)	34.8	–
Transfers from stage 3	0.9	1.7	(2.6)	–
Income statement charge				
Net remeasurement[2] following transfer of stage[3]	(5.9)	35.5	42.4	72.0
New financial assets originated[4]	4.8	1.0	0.3	6.1
Financial assets derecognised during the period	(3.4)	(4.6)	(2.1)	(10.1)
Changes in risk parameters and other movements[3,5]	44.2	105.3	40.2	189.7
Other movements				
Write-offs and asset disposals[6]	–	(1.3)	(87.0)	(88.3)
Transfer to provisions for liabilities and charges[7]	(4.6)	(3.4)	–	(8.0)
ECL allowance at 31 August 2020	**109.1**	**329.0**	**211.7**	**649.8**
Investment securities at FVOCI - loss allowance				
At 1 March 2020	0.9	–	–	0.9
Other movements				
Transfers to investment securities at amortised cost[8]	(0.9)	–	–	(0.9)
ECL allowance at 31 August 2020	**–**	**–**	**–**	**–**
Investment securities at amortised cost - loss allowance				
At 1 March 2020	0.1	–	–	0.1
Income statement charge				
Financial assets derecognised during the period	(0.1)	–	–	(0.1)
Changes in risk parameters and other movements	0.1	–	–	0.1
Other movements				
Transfers from investment securities at FVOCI	0.9	–	–	0.9
ECL allowance at 31 August 2020	**1.0**	**–**	**–**	**1.0**
Reconciliation to income statement				
Net expected credit loss charge	39.7	137.2	80.8	257.7
Recoveries and write-offs	–	–	(1.1)	(1.1)
Total income statement charge	**39.7**	**137.2**	**79.7**	**256.6**

[1] Transfers - The opening loss allowance on financial assets in respect of continuing operations which transferred stage during the period.
[2] Net remeasurement - The increase/(decrease) in the opening loss allowance as a result of a stage transfer.
[3] Includes a charge in stages 1 and 2 of £194.4m due to a change in macro-economic assumptions.
[4] New financial assets originated or purchased - The loss allowance on new financial assets originated or purchased during the period, representing their stage at 31 August 2020.
[5] Changes in risk parameters and other movements - The change in loss allowance due to changes in macro-economic scenarios, PD, LGD and EAD changes during the period.
[6] Write-offs and asset disposals - The release of the loss allowance following the write off and/or disposal of a financial asset during the period.
[7] Transfer to provisions for liabilities and charges - The movement in loss allowance which exceeds the gross carrying amount of the financial asset.
[8] On 1 March 2020 the Group's portfolio of debt investment securities measured at FVOCI was reclassified to amortised cost following a change in business model.

23. Credit risk management (continued)

Credit risk: Loss allowance (continued)

Loss allowance reconciliation (continued)

The following table provides a reconciliation of movements in the gross carrying amounts of financial instruments to help explain their significance to the changes in the loss allowance during the period as set out in the above table:

6 months to 31 August 2021	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Loans and advances to customers				
Gross carrying amount				
At 1 March 2021	5,748.5	1,030.0	241.6	7,020.1
Transfers[1]				
Transfers from stage 1 to stage 2	(51.3)	51.3	–	–
Transfers from stage 2 to stage 1	61.2	(61.2)	–	–
Transfers to stage 3	(28.2)	(59.4)	87.6	–
Transfers from stage 3	2.4	5.1	(7.5)	–
Other movements				
New financial assets originated[2]	850.3	6.8	1.7	858.8
Net decrease in lending[3]	(627.4)	(151.6)	(16.3)	(795.3)
Write-offs and asset disposals[4]	–	(1.0)	(95.9)	(96.9)
Changes in interest accrual and other movements	(0.1)	(1.8)	(3.2)	(5.1)
Gross balances at 31 August 2021	**5,955.4**	**818.2**	**208.0**	**6,981.6**
Investment securities at FVOCI				
Gross carrying amount				
At 1 March 2021	5.1	–	–	5.1
Acquisition of TU	616.1	–	–	616.1
New financial assets purchased	11.4	–	–	11.4
Financial assets derecognised during the period	(23.3)	–	–	(23.3)
Reclassification to FVPL during the period[5]	(5.1)	–	–	(5.1)
Other movements	(0.6)	–	–	(0.6)
Gross balances at 31 August 2021	**603.6**	**–**	**–**	**603.6**
Investment securities at amortised cost				
Gross carrying amount				
At 1 March 2021	949.2	–	–	949.2
New financial assets purchased	32.3	–	–	32.3
Financial assets derecognised during the period	(27.6)			(27.6)
Other movements	(3.9)	–	–	(3.9)
TU sub debt[6]	(21.1)	–	–	(21.1)
Gross balances at 31 August 2021	**928.9**	**–**	**–**	**928.9**

[1] Transfers - The opening gross carrying amount of financial assets held which transferred stage as at period end.

[2] New financial assets originated or purchased - The gross carrying amount of financial assets originated or purchased during the period, representing their stage as at 31 August 2021.

[3] Net decrease in lending - The changes in gross carrying amount of financial assets after taking account of additional borrowing and/or payments received from customers.

[4] Write-offs and asset disposals -The write-off of the gross carrying amount when a financial asset is deemed uncollectible and/or has been disposed of.

[5] During the period, following a review of industry practice and the requirements of IFRS 9, the Group reclassified its investment in preferred stock issued by VISA Inc. from FVOCI to FVPL.

[6] The Group investment in subordinated debt issued by TU is now fully eliminated in the Interim Condensed Consolidated Statement of Financial Position following the acquisition of TU on 4 May 2021.

23. Credit risk management (continued)

Credit risk: Loss allowance (continued)

Loss allowance reconciliation (continued)

6 months to 31 August 2020	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Loans and advances to customers				
Gross carrying amount				
At 1 March 2020	7,688.0	953.3	288.7	8,930.0
Transfers[1]				
Transfers from stage 1 to stage 2	(581.1)	581.1	–	–
Transfers from stage 2 to stage 1	50.7	(50.7)	–	–
Transfers to stage 3	(38.3)	(84.7)	123.0	–
Transfers from stage 3	2.2	4.6	(6.8)	–
Other movements				
New financial assets originated[2]	582.5	2.8	0.4	585.7
Net decrease in lending[3]	(1,301.2)	(188.2)	(9.8)	(1,499.2)
Write-offs and asset disposals[4]	(0.1)	(1.2)	(97.5)	(98.8)
Changes in interest accrual and other movements	(5.9)	0.5	5.8	0.4
Gross balances at 31 August 2020	**6,396.8**	**1,217.5**	**303.8**	**7,918.1**
Investment securities at FVOCI				
Gross carrying amount				
At 1 March 2020	1,060.6	–	–	1,060.6
Transfer to investment securities at amortised cost[5]	(1,057.3)	–	–	(1,057.3)
Other movements	0.3	–	–	0.3
Gross balances at 31 August 2020	**3.6**	**–**	**–**	**3.6**
Investment securities at amortised cost				
Gross carrying amount				
At 1 March 2020	21.1	–	–	21.1
Transfer from investment securities at FVOCI[5]	1,057.3	–	–	1,057.3
Financial assets derecognised during the period	(201.8)	–	–	(201.8)
Other movements	(3.3)	–	–	(3.3)
Gross balances at 31 August 2020	**873.3**	**–**	**–**	**873.3**

[1] Transfers - The opening gross carrying amount of financial assets held which transferred stage as at period end.

[2] New financial assets originated or purchased - The gross carrying amount of financial assets originated or purchased during the period, representing their stage as at 31 August 2020.

[3] Net decrease) in lending - The changes in gross carrying amount of financial assets after taking account of additional borrowing and/or payments received from customers.

[4] Write-offs and asset disposals -The write-off of the gross carrying amount when a financial asset is deemed uncollectible and/or has been disposed of.

[5] On 1 March 2020 the Group's portfolio of debt investment securities measured at FVOCI was reclassified to amortised cost following a change in business model.

24. Insurance Risk Management

The Group is exposed to insurance risk through its wholly owned subsidiary, TU, an authorised insurance company.

The Group defines insurance risk as the risks accepted 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 (e.g. flood or vehicular accident).

TU operates a separate risk framework with dedicated risk and compliance teams and a suite of TU risk policies to ensure that the TU insurance portfolio is operating within agreed Risk Appetite.

Types of insurance risk

Underwriting risk

Underwriting risk is the risk that future claims experience on business written is materially different from the results expected based on the assumptions made at the point of underwriting policies, resulting in current year losses. Contracts are typically issued on an annual basis, meaning that the Group's liability usually extends for a 12-month period, after which the Group is entitled to decline to renew or can revise renewal terms by amending the premium or other policy terms and conditions such as the excess.

Controls and risk mitigants

Products are priced based on the Group's knowledge using past exposures, historical losses (plus an appropriate allowance for IBNR losses) and external data sources, with the appropriate adjustments to reflect anticipated future market conditions and expenses.

The Group reinsures a portion of the risks it underwrites in order to control its exposure to losses and protect capital resources. The Group buys primarily excess of loss (non-proportional) reinsurance treaties to reduce its net exposure to agreed levels for each line of business in accordance with the Group's risk appetite. The Group has also purchased ADC against the risk of low frequency high impact scenarios. The Group is also party to a QS reinsurance treaty in which the Group and the reinsurer share premiums and losses at an agreed percentage.

Claims reserving risk

Reserving and the ultimate cost of claims risk occurs where the Group's estimates of its insurance liabilities prove to be insufficient through inaccurate forecasting, adverse random variation, additional expenses or reinsurance bad debts.

The methods used to estimate the insurance liabilities in respect of outstanding claims and provisions are detailed in note 21.

Controls and risk mitigants

The aim of the reserving policy of the Group is to provide estimates of insurance liabilities that are accurate and reliable across each line of business and are consistent over the time period required to settle all the claims.

The Group's reserving position is reviewed at the TU Reserving Committee and is presented to the TU Board. In addition, an annual independent reserve review is undertaken.

Claims management risk

Claims management risk may arise in the event of inaccurate or incomplete case reserving or settlement, poor customer service, claims fraud, ineffective or inefficient claim processes or excessive costs of handling claims.

Controls and risk mitigants

The Group's approach to claims management focuses upon creating a successful balance between satisfying the needs of the customer against control of the overall cost of the provision of the service that meets those needs in agreement with its service provider. Customers include both the insured as well as others that believe the insured has breached a duty of care.

24. Insurance Risk Management (continued)

Reinsurance risk

Reinsurance is placed to reduce the Group's exposure to specific risks, events and accumulations. The risk is that the reinsurance contracts fail to perform as planned and do not reduce the gross cost of claims in terms of the limits purchased, either by risks not being appropriately covered or by there not being gaps in the programme.

Controls and risk mitigants

The reinsurance programme is subject to considerable scenario planning, including by the TU brokers, and is approved by the TU Reinsurance Committee and the TU Board.

- **Sensitivity of insurance risk**

A Stress and Scenario Testing programme is part of TU's contingency planning. The tables below show more details for the tests that relate to insurance risk with an assessed return period.

24. Insurance Risk Management (continued)

- **Sensitivity of insurance risk (continued)**

Test name (Return period)	Description - Insurance risk stress	Rationale
Motor soft market (1-in-5 Yr)	TU's market competitiveness reduces more than anticipated leading to a contraction in Policies in Force of c.30% over 2021-2023.	To assess the impact of lower profitability from writing lower than expected volumes.
Motor hard market (1-in-5 Yr)	TU's market competitiveness improves more than anticipated leading to a growth in Policies in Force of c.20% over 2021-2023.	To assess the new business capital strain from writing higher than expected volumes.
Multiple weather events (1-in-200 Yr)	A number of events occurring recurrently over 2021 to 2023 as a result of increasingly aggravating climate changes - each event is below the reinsurance retention, so no recoveries are made.	TU's Catastrophe reinsurance covers up to a 1-in-200 return period. The Non-Life Internal Model shows that multiple smaller events drive the Solvency Capital Requirement (SCR) figure.
PPO severity shock (1-in-30 Yr)	Assume all TU PPO claimants have unimpaired life expectancy. Knock-on impact is that this element of the premium is too low and hence the 2021 Loss Ratio is 3% higher than Plan.	A key assumption in the calculation of the Claims Reserve.
Adverse large loss experience (1-in-30 Yr)	Existing bodily injury large loss reserves are insufficient (case reserves run-off neutrally compared with a favourable assumption of approximately 20% in ABE). The knock-on impact is that the bodily injury Large loss component of the premium is too low by 20% (relative) and hence the 2021 Loss Ratio is 5% higher than Plan.	A key assumption in the calculation of the Claims Reserve.
Non-Renewal of ADC and QS reinsurance (1-in-10 Yr)	Significant reserve deterioration leads to a claim on the ADC contract, this leads to an increase in the ADC and QS costs and TU makes the decision not to renew the covers on 1 January 2022.	Non-renewal of the reinsurance covers (particularly the ADC) would lead to a significant increase in the SCR figure.

24. Insurance Risk Management (continued)

- **Concentration of insurance risk**

Concentration of insurance risk may exist where a particular event or series of events could impact significantly upon the Group's liabilities. Such concentrations may arise from a single insurance contract or through a small number of related contracts.

Concentrations of risk can arise in both high-severity, low frequency events, such as natural and other disasters and in situations where underwriting is biased towards a particular group, such as a particular geographical concentration or demographic trend. Material geographical concentrations or risk can exist in property portfolios such that natural perils of windstorm and floods may give rise to a large number of material damage and business interruption claims.

High severity, low frequency concentrations

The timing and frequency of high severity events are, by their nature, uncertain. They represent a material risk as the occurrence of such an event would have a significant adverse impact on TU's cash flows and profitability.

TU manages these risks by making appropriate allowance within the price calculated by underwriters and by purchasing a reinsurance programme that limits the impact of these events. TU uses non-proportional reinsurance treaties to manage retention levels and the limits of protection.

Geographic and demographic concentrations

Material geographical concentrations or risk exist in property portfolios such that natural perils of windstorm and floods may give rise to a large number of material damage and business interruption claims. TU only writes policies in the UK and Channel Islands. TU models its exposure to this risk to estimate its probable maximum loss and purchases reinsurance to significantly reduce its exposure to such events.

Economic conditions

TU's insurance portfolio exposes it to a potential accumulation of different risks in the event of difficult economic conditions or more challenging points in the underwriting cycle. TU's strategy has been to ensure that it charges the right premium for the business underwritten and it focuses on maintaining prices in such difficult market conditions. It also monitors claims closely to identify any that may be exaggerated or fraudulent.

Total aggregate exposure

TU identifies the total aggregate exposure that it is prepared to accept in relation to concentrations of risk. It monitors these exposures on a regular basis by reviewing reports which show the key aggregations to which TU is exposed. TU uses a number of modelling tools to monitor aggregation and to simulate catastrophe losses in order to measure the effectiveness of the reinsurance programmes, and to quantify the net exposure to which TU is exposed. Additional stress and scenario tests are run using these models during the year.

Third-party injury claims and credit hire

In recent years, the insurance market in general has experienced an increase in the frequency and value of third-party injury claims, arising mainly in the motor market.

These increases have been driven by an increased propensity for the population to be litigious and the extensive activities of companies actively persuading potential victims to instigate claims. In addition, the growth in credit hire has also had a significant impact. TU is aware of this trend and monitors its development closely, adjusting the prices of its products accordingly.

24. Insurance Risk Management (continued)

Capital

Solvency II (SII) came into force on 1 January 2016. It provides a framework for managing and measuring the risks and the solvency position for all insurance companies in the EU. Following the UK's departure from the EU, the SII framework continues to be applied in the UK and its requirements are applicable to TU. TU assess its SCR using a Partial Internal Model for capital which was approved by the PRA in 2020. TU models a range of stress and scenario tests that are published in its annual Solvency and Financial Condition Report. These show that TU's capital position is resilient to a range of possible scenarios. TU also maintains a capital contingency plan supported by its shareholder, Tesco Personal Finance plc. The Company's available capital has remained above its SCR requirement during the period since the end of December 2020; and capital coverage of TU's SCR at the end of August 2021 as assessed as materially the same as the position at the end of December 2020.

Following its purchase of Ageas's 50.1% shareholding in May 2021, the Company owns 100% of the TU's share capital (£129.7m) and provides 100% of its subordinated debt of £42.3m.

25. Fair Values

Except as detailed in the following table, the Directors consider that the carrying value amounts of financial assets and financial liabilities recorded in the Interim Condensed Consolidated Statement of Financial Position are approximately equal to their fair values[1].

	31 August 2021		28 February 2021		31 August 2020	
	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	6,403.9	6,558.8	6,402.2	6,617.6	7,285.2	7,454.2
Investment securities - amortised cost	928.8	933.9	948.4	959.1	872.3	880.8
	7,332.7	**7,492.7**	**7,350.6**	**7,576.7**	**8,157.5**	**8,335.0**
Financial liabilities:						
Deposits from customers	5,048.6	5,051.4	5,751.2	5,757.5	6,648.4	6,657.8
Debt securities in issue	–	–	–	–	762.1	763.9
Subordinated liabilities and notes	485.8	473.6	486.6	458.3	489.4	449.9
	5,534.4	**5,525.0**	**6,237.8**	**6,215.8**	**7,899.9**	**7,871.6**

The only financial assets and financial liabilities which are carried at fair value in the Interim Condensed Consolidated Statement of Financial Position at period end are cash balances relating to the Group's Travel Money offering, FVPL and 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.

[1] Fair value disclosures are not required for lease liabilities.

25. Fair Values (continued)

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.

As at 31 August 2021	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets carried at fair value				
Cash in hand[1]	–	25.5	–	25.5
Investment securities - FVOCI	603.6	–	–	603.6
Investment securities - FVPL	–	23.3	1.9	25.2
Derivative financial instruments:				
- Interest rate swaps	–	5.6	–	5.6
Financial assets carried at amortised cost				
Loans and advances to customers	–	–	6,558.8	6,558.8
Investment securities – amortised cost	933.9	–	–	933.9
Total	**1,537.5**	**54.4**	**6,560.7**	**8,152.6**
Financial liabilities carried at fair value				
Derivative financial instruments:				
- Interest rate swaps	–	36.2	–	36.2
- Forward foreign currency contracts	–	0.2	–	0.2
Financial liabilities carried at amortised cost				
Deposits from customers	–	–	5,051.4	5,051.4
Subordinated liabilities	–	473.6	–	473.6
Total	**–**	**510.0**	**5,051.4**	**5,561.4**

As at 28 February 2021	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets carried at fair value				
Cash and balances with central banks	–	13.2	–	13.2
Investment securities - FVOCI[1]	–	3.4	1.7	5.1
Derivative financial instruments:				
- Interest rate swaps	–	6.0	–	6.0
- Forward foreign currency contracts	–	0.1	–	0.1
Financial assets carried at amortised cost				
Loans and advances to customers	–	–	6,617.6	6,617.6
Investment securities – amortised cost[1]	932.3	26.8	–	959.1
Total	**932.3**	**49.5**	**6,619.3**	**7,601.1**
Financial liabilities carried at fair value				
Derivative financial instruments:				
- Interest rate swaps	–	46.5	–	46.5
- Forward foreign currency contracts		1.0		1.0
Financial liabilities carried at amortised cost				
Deposits from customers	–	–	5,757.5	5,757.5
Subordinated liabilities	–	458.3	–	458.3
Total	**–**	**505.8**	**5,757.5**	**6,263.3**

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

25. Fair Values (continued)

As at 31 August 2020	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets carried at fair value				
Cash in hand[1]	–	24.1	–	24.1
Investment securities - FVOCI	–	–	3.6	3.6
Derivative financial instruments:				
- Interest rate swaps	–	6.8	–	6.8
Financial assets carried at amortised cost				
Loans and advances to customers	–	–	7,454.2	7,454.2
Investment securities – amortised cost	853.7	27.1	–	880.8
Total	**853.7**	**58.0**	**7,457.8**	**8,369.5**
Financial liabilities carried at fair value				
Derivative financial instruments:				
- Interest rate swaps	–	60.9	–	60.9
- Forward foreign currency contracts	–	0.7	–	0.7
- Cross currency swaps	–	10.7	–	10.7
Financial liabilities carried at amortised cost				
Deposits from customers	–	–	6,657.8	6,657.8
Debt securities in issue	763.9	–	–	763.9
Subordinated liabilities	–	449.9	–	449.9
Total	**763.9**	**522.2**	**6,657.8**	**7,943.9**

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

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 they 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 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.

Fair values of investment in subordinated debt classified as amortised cost are calculated using 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.

Financial assets classified as FVPL comprise the Group's interest in VISA Inc, and TU's property fund. The estimated fair value of the Group's interest in VISA Inc. is described in note 15. The estimated fair value of TU's property fund is derived from market prices.

25. 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 FVPL, being the Group's interest in VISA Inc., is described in note 15.

Transfers

There were no transfers between Levels 1 and Level 2 during the period (February 2021: no transfers).

There were no transfers between Level 2 and Level 3 during the period. During the year ended 28 February 2021 the Group transferred investment securities totalling £1.7m from Level 3 to Level 2.

26. Capital Resources

IFRS 9 'Financial Instruments' became effective for annual periods beginning on or after 1 January 2018 and is reflected in the Group disclosures. The Group has elected to use the transitional arrangements available under Article 473a of the Capital Requirements Regulations (CRR). These arrangements allow the IFRS 9 impact on capital to be phased in over a period of 5 years. On 27 June 2020, the CRR was further amended to accelerate specific CRR2 measures and implement a new IFRS 9 transitional relief calculation which applies additional relief to increases in ECL provisions arising as a result of the Covid-19 pandemic. As a result, the IFRS 9 transitional arrangements have been extended by two years and a new modified calculation has been introduced. Full relief will be applied to increases in stage 1 and stage 2 provisions from 1 January 2020 throughout 2020 and 2021, reducing to 75% in 2022, 50% in 2023 and 25% in 2024, with no relief applied from 2025. The phasing out of transitional relief on the 'day 1' impact of IFRS 9 as well as increases in stage 1 and stage 2 provisions between 1 March 2018 and 31 December 2019 under the modified calculation remain unchanged and continue to be subject to 70% transitional relief throughout 2020, 50% relief for 2021 and 25% for 2022, with no relief applied from 2023.

26. Capital Resources (continued)

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 period as related to the IFRS 9 transitional period:

	Transitional 31 August 2021 £m	End Point 31 August 2021 £m	Transitional 28 February 2021 £m	Transitional 31 August 2020[1] £m
Common equity tier 1				
Shareholders' equity (accounting capital)	1,665.9	1,665.9	1,580.7[1]	1,607.1[1]
Regulatory adjustments				
Unrealised gains on cash flow hedge reserve	–	–	0.6	0.5
Adjustment to own credit/Additional value adjustments	–	–	–	–
Foreseeable dividends	(50.0)	(50.0)	–	(50.0)
Intangible assets	(121.6)	(121.6)	(130.9)	(130.1)
Material holdings in financial sector entities	(34.6)	(34.6)	–	–
IFRS 9 transitional relief	213.8	–	262.9	229.3
Common equity tier 1 capital	**1,673.5**	**1,459.7**	**1,713.3[1]**	**1,656.8[1]**
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
Tier 2 capital (instruments and provisions) before regulatory adjustments	**235.0**	**235.0**	**235.0**	**235.0**
Regulatory adjustments				
Material holdings in financial sector entities	(42.2)	(42.2)	(21.1)	(21.0)
Total regulatory adjustments to tier 2 capital (instruments and provisions)	**(42.2)**	**(42.2)**	(21.1)	**(21.0)**
Total tier 2 capital (instruments and provisions)	**192.8**	**192.8**	**213.9**	**214.0**
Total capital	**1,866.3**	**1,652.5**	**1,927.2[1]**	**1,870.8[1]**
Total risk-weighted assets (unaudited)	7,004.0	6,894.1	6,820.2	7,683.2
Common equity tier 1 ratio (unaudited)	23.9%	21.1%	25.1%[1]	21.6%[1]
Tier 1 ratio (unaudited)	23.9%	21.1%	25.1%[1]	21.6%[1]
Total capital ratio (unaudited)	26.6%	24.0%	28.3%[1]	24.3%[1]

As a result of the acquisition of Ageas's 50.1% share of TU and in accordance with the CRR, the Company has made the required deductions from Tier 1 and Tier 2 capital and risk-weighted the remaining value of the investment at 250%.

[1] The above balances and ratios at 28 February 2021 and 31 August 2020 have been restated following restatement of the Company Statement of Financial Position at 1 March 2020. This was in respect of a £7.0m dividend received from TU prior to 1 March 2020, which was recognised as a deduction from the carrying value of the investment in the Company Statement of Financial Position rather than through the Company Income Statement.

26. Capital Resources (continued)

The impact of these restatements is as follows:

	As previously reported £m	Dividend restatement £m	Restated £m
At 31 August 2020			
Capital resources			
Shareholders' equity (accounting capital)	1,600.1	7.0	1,607.1
Common equity tier 1 capital	1,649.8	7.0	1,656.8
Total capital	1,863.8	7.0	1,870.8
Share of joint venture's retained earnings	(26.9)	7.0	(19.9)
Common equity tier 1 ratio	21.5%		21.6%
Tier 1 ratio	21.5%		21.6%
Total capital ratio - transitional	24.3%		24.3%
At 28 February 2021			
Capital resources			
Shareholders' equity (accounting capital)	1,573.7	7.0	1,580.7
Common equity tier 1 capital	1,706.3	7.0	1,713.3
Total capital	1,920.2	7.0	1,927.2
Share of joint venture's retained earnings	(26.6)	7.0	(19.6)
Common equity tier 1 ratio	25.1%		25.1%
Tier 1 ratio	25.1%		25.1%
Total capital ratio - transitional	28.2%		28.3%
Total capital ratio - end-point	24.8%		24.8%

Total capital requirement (TCR) refers to the amount and quality of capital the Company must maintain to comply with the CRR Pillar 1 and 2A capital requirements. The TCR for TPFG as at 31 August 2021 is 11.59% plus £52m as a static add-on for pension obligation risk.

In line with guidance issued by the European Banking Authority, the Group has included a foreseeable dividend, based on historic actual pay-out levels, within its capital resources disclosure. No final decision has yet been taken on whether to pay a dividend for the year ending 28 February 2022.

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

	31 August 2021 £m	28 February 2021 £m	31 August 2020 £m
Tesco Personal Finance plc (Group) shareholders' equity	1,678.4	1,606.1	1,635.4
Share of joint venture's retained earnings[1]	–	(19.6)[2]	(19.9)[2]
Subsidiaries' retained earnings[1]	(8.9)	(0.2)	–
Share of joint venture's AFS reserve[1]	–	(5.6)	(8.4)
Subsidiary's fair value reserve[1]	(3.6)	–	–
Tesco Personal Finance Plc (Company) shareholders' equity	**1,665.9**	**1,580.7[2]**	**1,607.1[2]**

[1] Following the acquisition of 50.1% of TU on 4 May 2021 it is now a wholly owned subsidiary of the Group. Prior to this TU was a joint venture of the Group.

[2] The above balances at 28 February 2021 and 31 August 2020 have been restated following restatement of the Company Statement of Financial Position at 1 March 2020. This was in respect of a £7.0m dividend received from TU prior to 1 March 2020, which was recognised as a deduction from the carrying value of the investment in the Company Statement of Financial Position rather than through the Company Income Statement.

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 Prudential Regulatory Authority (PRA).

26. Capital Resources (continued)

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

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, 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.

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

Exposures for leverage ratio (unaudited)	**Transitional 31 August 2021 £m**	**End Point 31 August 2021 £m**	**Transitional 28 February 2021 £m**	**Transitional 31 August 2020 £m**
Total balance sheet exposures	9,430.3	9,430.3	8,821.8	10,649.7
Adjustments for entities which are consolidated for accounting purposes but outside scope of regulatory consolidation	(790.6)	(790.6)	(32.6)	(35.3)
Removal of accounting value of derivatives and Securities Financing Transactions (SFTs)	(5.6)	(5.6)	(6.1)	(6.8)
Exposure value for derivatives and SFTs	4.1	4.1	4.4	4.4
Off balance sheet: unconditionally cancellable (10%)	1,250.6	1,250.6	1,266.8	1,232.5
Off balance sheet: other (20%)	–	–	–	–
Regulatory adjustment – intangible assets	(121.6)	(121.6)	(130.9)	(130.1)
Regulatory adjustment – other, including IFRS 9	148.2	(65.6)	212.9	177.2
Total	**9,915.4**	**9,701.6**	**10,136.3**	**11,891.6**
Common equity tier 1	**1,673.5**	**1,459.7**	**1,713.3**	**1,656.8**
Leverage ratio	**16.9%**	**15.1%**	**16.9%**	**13.9%**

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 Management Committee and Treasury Committee.

26. Capital Resources (continued)

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 proportionate by addressing some of the concerns over the differences between Standardised Approach (SA) and internal ratings-based risk weights. This will continue to be managed as part of the Group'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 banking activities where core deposits are in excess of £25bn came into effect from 1 January 2019. The Group has not exceeded this threshold and was not therefore automatically required to ring-fence the Group's core activities by the 2019 implementation date.

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 risk-sensitivity of the SAs 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 risk-sensitive floor based on the Committee's Basel III standardised approaches. The final Basel III reforms will be implemented in January 2023.

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 SA to be used by all banks. The new SA increases the sensitivity by combining a refined measure of gross income with the bank's internal historical losses. The final Basel III reforms will be implemented in January 2023.

Leverage

At present the Group has no minimum UK leverage requirement as it is currently exempt from the UK Leverage Framework Regime (LFR), which only applies to institutions with retail deposits over £50 billion. In December 2017, the BCBS finalised Basel III reforms for the leverage ratio. The final Basel III reforms will be implemented in January 2023.

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

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

Upon full implementation, MREL targets will be set on a bank-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 would be likely to need post-resolution.

The Group became subject to MREL on an interim basis from 1 January 2020, with full implementation applicable from 1 January 2023. The interim target remains at 18% of risk-weighted assets until 31 December 2022. The requirements are factored into the Group's funding and capital plans. TPFG undertook an initial £250.0m issuance of MREL-compliant debt in July 2019 in support of the interim requirements and subsequently invested the proceeds in the Company via an intercompany subordinated loan. Further issuances may be required to support end-state requirements.

At 31 August 2021, the MREL ratio was 30.2% (February 2021: 31.9%).

27. 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 2021.

Following the acquisition of the remaining 50.1% share capital of the Group's joint venture, TU, on 4 May 2021 TU became a subsidiary of the Group. Transactions with TU during the period continued to be similar in nature to those for the year ended 28 February 2021.

28. 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.

29. Ultimate Parent Undertaking

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

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'.

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,

Richard Henderson
Director
4 October 2021

Directors:	Sir John Kingman	Non-Executive Chairman
	Julie Currie	Independent Non-Executive Director
	Robert Endersby	Independent Non-Executive Director
	Jacqueline Ferguson	Senior Independent Non-Executive Director
	Richard Henderson	Chief Financial Officer [1]
	Simon Machell	Independent Non-Executive Director
	Gerard Mallon	Chief Executive
	Adrian Morris	Non-Executive Director
	Amanda Rendle	Independent Non-Executive Director
Company Secretary:	Michael Mustard	

[1] Richard Henderson moved from the position of Chief Risk Officer to Chief Financial Officer as of 30 June 2021. Deborah Walker has been appointed Chief Risk Officer on an interim basis and is currently not a Director of the Company.

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 2021 which comprise 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 29. 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.

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 International Accounting Standard 34 'Interim Financial Reporting' (IAS 34).

As disclosed in note 1, the annual Financial Statements of the Company are prepared in accordance with United Kingdom adopted IFRSs. The Interim Condensed Consolidated Financial Statements included in this Interim Financial Report have been prepared in accordance with United Kingdom adopted IAS 34.

Our responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of 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 2021 are not prepared, in all material respects, in accordance with United Kingdom adopted International Accounting Standard 34.

Use of our report

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.

Deloitte LLP

Statutory Auditor

Leeds, United Kingdom

4 October 2021

ABE	Actuarial best estimate
ADC	Adverse development cover
AFS	Available-for-sale
Ageas	Ageas (UK) Limited
BCBS	Basel Committee on Banking Supervision
BoE	Bank of England
CCyB	Countercyclical capital buffer
CRD	Capital Requirements Directive
CRO	Chief Risk Officer
CRR	Capital Requirements Regulation
EAD	Exposure at default
ECLs	Expected credit losses
EIR	Effective interest rate
EU	European Union
FCA	Financial Conduct Authority
FPC	Financial Policy Committee
FVOCI	Fair value through other comprehensive income
FVPL	Fair value through profit or loss
IAS	International Accounting Standard
IAS 34	IAS 34 'Interim Financial Reporting'
IASB	International Accounting Standards Board
ICAAP	Internal capital adequacy assessment process
IBNR	Incurred but not reported
IFRS	International Financial Reporting Standard
IFRS 3	IFRS 3 'Business combinations
IFRS 9	IFRS 9 ‘Financial Instruments’
KPI	Key performance indicator
LFR	Leverage Framework Regime
LGD	Loss given default
LIBOR	London Inter Bank Offered Rate
MREL	Minimum requirements for own funds and eligible liabilities
NSFR	Net stable funding ratio
PCA	Personal Current Account
PD	Probability of default
Plevin	Plevin v Paragon Personal Finance Limited
PMA	Post-model adjustment
PPI	Payment protection insurance
PPO	Periodic payment order
PRA	Prudential Regulation Authority
QS	Quota share
RMF	Risk management framework
SA	Standardised approach
SCR	Solvency Capital Requirement
SFTs	Securities financing transactions
SONIA	Sterling Overnight Index Average
TCR	Total capital requirement
TPF	Tesco Personal Finance plc
TPFG	Tesco Personal Finance Group plc
TPP	Third-party provider
TSL	Tesco Stores Limited
TU	Tesco Underwriting Limited
UK	United Kingdom

A

Actuarial best estimate	An estimate of ultimate claims or claims reserve that is intended to be neither too high, nor too low, taking into account known information.
Adverse development cover	Reinsurance cover that will pay the reinsured if claims develop adversely over a certain limit.
Amortised cost	The amount at which the financial asset or financial liability is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the EIR method of any difference between the initial amount and the maturity amount and minus any reduction (directly through the use of an allowance account) for impairment or uncollectability.
Annual percentage rate	The yearly interest generated by a sum that is charged to borrowers or paid to investors.

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.
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, excluding any interest-bearing assets held within a disposal group.
Brexit	The process by which the United Kingdom left 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.
Claims reserve	A provision held to cover the settlement of claims, including claims that may not yet have been notified.
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.
Company	Tesco Personal Finance plc.
Cost:income ratio	The cost:income ratio is calculated by dividing operating expenses by total income.
Countercyclical capital buffer	The countercyclical capital buffer is a time varying capital requirement which applies to banks and investment firms. It aims to promote a sustainable provision of credit to the economy by making the banking system more resilient and less pro-cyclical.
CRD IV	Legislation published in June 2013 (in force from 1 January 2014) by the European Commission, comprising the CRD and CRR 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.
Discontinued operations	The operations and cash flows of a major component of a business, the carrying amount in respect of which is to be recovered principally through a sale transaction, when the sale is considered highly probable at the reporting date.

E

Expected credit loss	The probability-weighted estimate of credit losses over the expected life of a financial instrument.
Exposure	A claim, contingent claim or position which carries a risk of financial loss.
Exposure at default or exposure value	The amount expected to be outstanding after any credit risk mitigation, if and when the counterparty defaults. EAD 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 statutory body responsible for conduct of business regulation and supervision of UK authorised firms from 1 April 2013. The FCA also has responsibility for the prudential regulation of firms that do not fall within the PRA's scope.
Financial instrument	A contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.
Financial Policy Committee	The BoE's Financial Policy Committee identifies, monitors and takes action to remove or reduce systemic risks with a view to protecting and enhancing the resilience of the UK financial system.
Funding risk	The risk that the Group does not have sufficiently stable and diverse sources of funding.

G

Gross domestic product	The total value of goods produced and services provided in a country during one year.
Gross insurance premiums written	Premiums paid by policyholders for their insurance, inclusive of commission and insurance premium tax over a given period.
Group	The Company and its subsidiaries.

I

Impairment losses	The reduction in value that arises following an impairment review of an asset outwith the scope of IFRS 9 which has determined that the asset's value is lower than its carrying value.
Insurance risk	The risks accepted 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.
Internal liquidity adequacy assessment process	An ongoing exercise as part of the PRA's regulatory framework to ensure that the Group maintains adequate liquid assets to survive a defined stress scenario for a sufficient period as defined by Risk Appetite.

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:deposit ratio	The loan to deposit ratio is calculated by dividing loans and advances to customers by deposits from customers.
Loans and advances to customers loss allowance coverage ratio	The loans and advances to customers loss allowance coverage ratio is calculated by dividing the ECL provision in respect of loans and advances to customers by the gross carrying amount of loans and advances to 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.
Minimum requirements for own funds and eligible liabilities	A requirement for minimum loss-absorbing capacity institutions must hold.
N	
Net interest margin	Net interest margin is calculated by dividing net interest income by average interest bearing assets, excluding any interest bearing assets held within a disposal group.
Net stable funding ratio	The net stable funding ratio is calculated under the CRD IV methodology.
O	
Ogden tables	Tables which are used to calculate the cost of any claim that involves compensation for loss of future benefits. The tables provide an estimate of the return to be expected from the investment of a lump sum damages award.
Operational risk	The risk of loss resulting from inadequate or failed internal processes, people and systems 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.
PD threshold	The maximum lifetime PD for each financial asset that was expected at the reporting date at initial recognition before a significant increase in credit risk is deemed to have occurred.
Periodic payment order	Large bodily injury claims that are settled by means of periodic payments, approved in a court of law and typically pay for the cost of care and lost earnings.
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.
Pillar 2A	Pillar 2A addresses risks to an individual firm which either are not captured, or not fully captured, under the Pillar 1 capital requirements applicable to all banks.
Policies in Force	The number of live policies in the Group's insurance portfolio for which the Group is obliged to provide cover.
Probability of default	Represents the likelihood a customer will default over the relevant period, being either 12 months or the expected lifetime.
Prudential Regulatory Authority	The statutory body responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms in the UK.
Q	
Quota share	A type of reinsurance where the insured shares a portion (quota) of its premium and risk with one of more reinsurer(s).
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 securitisation is defined as a transaction where the payments are dependent upon the performance of a single exposure or pool of exposures, where the subordination of tranches determines the distribution of losses during the life of the transaction.
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.
Solvency capital requirement	A statutory amount that the Group needs to hold over and above its best estimate for claims under the Solvency II regulations. It is calibrated to a 1:200 year adverse scenario.
Standardised Approach	In relation to credit risk, the method for calculating credit risk capital requirements using risk-weightings that are prescribed by the regulator. SA's 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

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.
Underwriting risk	Underwriting risk is the risk that future claims experience on business written is materially different from the results expected based on the assumptions made at the point of underwriting policies, resulting in current year losses.