ANNUAL REPORT & ACCOUNTS 2020

Coutts

STRATEGIC REPORT

The directors of Coutts & Company (the Bank) present their Annual Report, together with audited consolidated financial statements of the Bank and its subsidiaries (together the Group) for the year ended 31 December 2020. The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and in conformity with the requirements of the Companies Act 2006 which constitutes a body of generally accepted accounting principles.

Principal activities

The principal activity of the Group is to provide a wide range of banking, lending and wealth management services to UK connected high net worth individuals and their business interests. We continue to focus on delivering the best client experience through a proactive engagement model which supports clients across both sides of their balance sheet. Our client centric strategy is focussed on improving returns by deepening client relationships and improving our digital banking capabilities to make it easier for clients to deal with us.

The Group earns income from interest gained on loans to clients, as well as fees from client transactions and through our asset management service. We also pay interest to clients who have placed interest bearing deposits with us.

The Group is a subsidiary of NatWest Group plc (renamed from The Royal Bank of Scotland Group plc (RBS Group) on 22 June 2020), which provides support and access to all central resources. The Group leverages its relationship with its immediate parent National Westminster Bank Plc (NWB Plc), NatWest Holdings Limited (NWH Ltd), the parent of the ring-fenced sub-group and the NatWest Group, which comprises NatWest Group plc and its subsidiary and associated undertakings, to continue to improve the quality and efficiency of the services and products provided. Copies of the annual report of NatWest Group plc can be obtained from Legal, Governance and Regulatory Affairs, Gogarburn, Edinburgh EH12 1HQ, the Registrar of Companies or through the NatWest Group website, www.natwestgroup.com.

Business review

Our vision is to be the best Private Bank for the UK and *Our Purpose* is to champion potential, helping people, families and businesses to thrive. Our strategy is to deliver on *Our Purpose* and drive sustainable returns to our shareholder through four strategic priorities. We strive to support our clients at every stage of their lives by being more relevant to them and by building deeper relationships as we evolve our propositions to meet their needs throughout their lives. We will continue to become much simpler as a bank and much simpler to deal with for our clients, through a focus on great client service and technology and improving client journeys. We will further be powered by partnerships and innovation by using new technology and digital expertise to deliver an excellent client experience - harnessing our internal knowledge and experience and partnering with leading external organisations. We will allocate our capital better to drive growth and optimise returns from a safe and secure base.

We will deliver these priorities from a strong balance sheet and capital generative business, which give us the necessary flexibility to navigate an uncertain outlook, to support our clients, and deliver sustainable returns to our shareholder.

Against the backdrop of the Coronavirus Disease 2019 (COVID-19) crisis, *Our Purpose* could be seen in action throughout 2020 as we put in place extraordinary measures to support our clients, colleagues and communities through the pandemic, whilst also making good progress against each of our strategic priorities.

Robust governance structures enabled us to react quickly in the early stages of the COVID-19 crisis, supporting our most in-need clients through the provision of repayment deferrals and government supported loans, with over £315 million drawn down against UK Government lending schemes in 2020. We also proactively contacted our vulnerable clients. Our colleagues embraced remote working practices through the provision of technology and equipment. Training on the use of video calls for client interactions ensured appropriate steps were taken to meet regulatory standards whilst enabling us to continue to meet client needs.

We increased communication channels for our clients and encouraged more clients to interact digitally. As a result, we saw digital adoption increase significantly during the year. After a period of initial disruption, our Coutts 24 service provided a substantially uninterrupted service to our clients, responding to queries throughout 2020. Our Net Promoter Score (NPS) continued to improve, reaching a new high of 45 (an increase of 2 points from the end of 2019), which is especially pleasing during these unprecedented and turbulent times.

Despite the significant changes impacting our colleagues' ways of working during the year, colleague engagement remains high with survey results placing it ahead of the Global Financial Services (GFS) norm in all categories, with particular strengths reported in the areas of culture, leadership, purpose and values. A key priority during the coronavirus pandemic has been to look after the safety and wellbeing of our colleagues. We have created a safe working environment through rigorous health and safety procedures in our buildings and have provided the right support and technology to enable our colleagues to work remotely, alongside wellbeing support to help them in adapting to home working and manage work life balance.

STRATEGIC REPORT

The Group's financial performance in 2020 has been resilient despite the challenging circumstances and continued low interest rate environment. Operating profit was £127 million compared to £300 million in 2019, which included net loan impairments of £108 million due to the expected deterioration in asset quality resulting from the economic impact of COVID-19. Operating profit also benefited from net litigation and conduct provision release of £31 million during the year. However, despite Return on Equity (RoE) reducing by 9.7 percentage points to 6.6% in 2020, our capital position remains strong with a Common Equity Tier 1 (CET1) ratio of 12.0% at December 2020, and we are pleased with the solid growth seen across deposits, lending, investments and new clients during the year.

It is testimony to the strength of our business that we have remained resilient and continued to thrive in these unprecedented times.

Assets under Management and Administration (AuMA) have continued to grow, with net new inflows of £820 million during the year. We have also formed a new investment relationship with the world's largest asset manager, BlackRock, leading to the creation of new funds. This exciting development allows us to invest more quickly, more efficiently and at a lower cost than we've been able to before, enabling savings to be passed on to our clients through reduced fees, and we share a desire with BlackRock to invest more sustainably. We believe putting purpose at the heart of what we do helps to improve long-term investment performance on behalf of our clients.

There are three particular focus areas of *Our Purpose* where we seek to make a meaningful contribution to our clients, colleagues and communities: climate, enterprise and learning. We will be a leader on the fight against climate change by playing an active role in the transition to a low-carbon economy. We will champion businesses in the UK removing barriers to enterprise and help the economy build back better. And we will build financial capability by helping those who want to take control of their finances and their futures to make the most of their money. We have made good progress in each of these focus areas throughout 2020:

Climate
We issued our first investment sustainability report in the year, which can be found at www.coutts.com/about/sustainability.html, outlining what we're doing to create lasting, positive change in the world, while protecting our clients' wealth for future generations. In September 2020, Coutts became a signatory of the Green Finance Institute's Green Home Retrofit Principles and in November launched the green mortgage pilot to help our clients improve the EPC ratings of their homes.

This was our second year as signatory to Principles for Responsible Investment (PRI). Our Asset Management business significantly reduced the carbon intensity of equity holdings in its portfolios. Our Strategy and Governance score of A+ is the highest rating possible, higher than the industry median rating of A. This category rates the Group's overarching approach to responsible investment and incorporation of environmental, social and governance (ESG) issues into its asset allocation, recognising the action we are taking to create a better future (more information can be found on page 7).

We are proud to be founding partners of His Royal Highness The Prince of Wales' Sustainable Markets Initiative; focused on the need to accelerate global progress towards a sustainable future. Peter Flavel, Coutts Chief Executive, is a member of the Sustainable Markets Initiative Financial Services Taskforce. The Bank provided secondees to the taskforce to support its efforts.

Enterprise
We support our Entrepreneur clients through a dedicated service which provides capital and connections to business founders. Coutts Investment Club introduces financially sophisticated high net worth individuals to private companies. In March 2020 we agreed to collaborate with the Business Growth Fund to develop the UK Enterprise Fund (aiming to raise £50 - £100 million). The Fund is committed to providing growth capital, regardless of gender or background. This is one way in which we will support female entrepreneurs to overcome the barriers that they face.

Learning
Our award-winning Coutts Institute continued to support clients with their philanthropic needs. In 2020, we supported over 230 clients with a fraud awareness webinar and more than 4,000 clients attended our 'Coutts in Conversation' speaker series. Internally, we launched a mentor scheme for BAME colleagues and provided 220 frontline colleagues with sales skills training, using psychology and behavioural science.

During these challenging times it is more important than ever that we continue to support our communities. This year we have donated produce from the roof garden at our building on The Strand to The Connection and The Felix Project, charities dedicated to helping disadvantaged and vulnerable people. We have also continued our support to St Saviour's & St Olave's, a local girl's school, and of MoneySense, the NatWest financial education for children programme, as well as to The Conservation Volunteers, where our colleagues help plant trees in local areas. In addition to fundraising for our two nominated charities, Place2Be and MQ (more information on page 7) we have also raised funds to support the National Emergencies Trust COVID-19 appeal.

The Bank continues to be recognised externally, winning awards during 2020 including:

- Best HNW Team – UK (WealthBriefing European Awards),
- Best Overall UK Private Bank (WealthBriefing European Awards),
- Best in Corporate Social Responsibility/ Diversity (WealthBriefing European Awards),
- Best Private Bank for Philanthropic Services (Global Finance – World's Best Private Bank Awards).
- Best Private Bank for Millennials (The Financial Times' Banker and Professional Management award)

A continuous process is used to identify and manage the Group's top and emerging risks. These are risks that could have a significant impact on its ability to operate or meet its strategic goals. Details of the principal risks can be found in the Risk and Capital Management section on page 10.

STRATEGIC REPORT

Performance highlights	2020 £m	2019 £m
Total income	634	690
Operating expenses	(399)	(397)
Impairment (losses)/releases	(108)	7
Operating profit before tax	127	300
Tax charge	(33)	(80)
Profit and total comprehensive income for the year	94	220
Loans to customers - amortised cost	16,317	14,792
Customer deposits	30,142	26,390
AuMA	30,246	28,473
Customer loan:deposit ratio	54.1%	56.1%
RoE(1)	6.6%	16.3%
Cost:income ratio (C:I ratio)	62.9%	57.5%
Net Interest Margin (NIM)	2.68%	3.19%

Note:
(1) Return on equity is calculated using annual profit for the period attributable to ordinary shareholders' and owner's equity at the year end.

Financial performance

The Group's financial performance is presented in the Consolidated Statement of Comprehensive Income on page 57.

RoE has decreased 9.7 percentage points, down from 16.3% to 6.6% as a result of the challenging economic environment.

Operating profit before tax has declined by 58% (£173 million) from £300 million to £127 million, driven by the lower interest rate environment and higher impairment losses due primarily to the economic impact of COVID-19.

Income has decreased by £56 million in the year, due primarily to lower interest rates partially offset by balance sheet growth.

NIM has decreased 51 bps from 3.19% to 2.68% as a result of the lower funding benefit we received on our deposits.

Despite the challenging environment we have continued to grow our loan book with balances increasing from £14.8 billion to £16.3 billion, driven by strong net new lending and £315 million loans issued to clients under government backed schemes.

Deposit balances grew by £3.7 billion from £26.4 billion to £30.1 billion in the year as a result of commercial inflows and increases in current account balances as our clients have sought to increase their levels of liquidity in these uncertain times.

The Group is the Centre of Expertise (CoE) for client investment AuMA for the whole of NWH Ltd. It manages portfolios totalling £30.2 billion as at 31 December 2020 (2019 - £28.5 billion), with £7.2 billion of these assets relating to clients of other NatWest Group members for which the Bank receives a management fee. AuMAs have increased on prior year driven by net new inflows of £820 million and positive market movements.

Our investment portfolios continue to perform strongly and compare favourably to peers over most time periods. We have delivered significant progress in reducing the carbon intensity of the investments we manage and are on track to significantly exceed a 25% reduction (since June 2019) well in advance of our target date of December 2021. The UN's PRI annual assessment also increased its rating to A+ for how we adopt responsible investing – the highest possible grade and above the industry average of A.

Operating expenses increased £2 million from £397 million to £399 million in 2020. £16 million of this was due to higher service charges from other NatWest Group companies, with a further £18 million from investment spend as the Group continues to invest in its strategic goals, offset in part by litigation and conduct provision release of £31 million. The C:I ratio has increased 5.4 percentage points from 57.5% to 62.9% reflecting the impact of lower income.

The Group has recognised net loan impairments of £108 million in 2020 (2019 – release of £7 million), driven primarily by IFRS 9 stage one and stage two charges reflecting the deterioration in the economic environment arising from the COVID-19 pandemic. As a result, the expected credit loss (ECL) coverage ratio increased from 0.3% to 0.8% overall.

The CET1 ratio as at 31 December 2020 was 12.0%. Risk Weighted Assets (RWAs) increased by £0.9 billion in 2020 to £10.2 billion, which is less than lending growth in the year, reflecting the impact of the Group's capital savings from data clean-up activities.

As at 31 December 2020, the balance sheet (on page 58) showed total assets of £38 billion (2019 - £34 billion), reflecting £16.3 billion of loans to clients (2019 - £14.8 billion) and £21.3 billion (2019 - £18.7 billion) of funds placed with NWB.

The principal source of funds for the Group is its client deposits. The balance sheet at 31 December 2020 showed total liabilities and equity of £38 billion (2019 - £34 billion), including client deposits of £30.1 billion (2019 - £26.4 billion).

Accounting policies

The reported results of the Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. Details of the Group's critical accounting policies and key sources of estimation uncertainty are included in the accounting policies on page 65.

Stakeholder engagement and s.172 (1) statement

For the financial year ended 31 December 2020 the Bank has chosen to report against the Wates Corporate Governance Principles for Large Private Companies, published by the Financial Reporting Council (FRC) in December 2018 and available on the FRC website (the Wates Principles). The disclosures below explain how the Bank has applied the Wates Principles in the context of our corporate governance arrangements.

The priorities for 2020 agreed by the Board support *Our Purpose* – "*We champion potential, helping people, families and businesses to thrive*" – and reflect the Bank's vision to be the best Private Bank for the UK. These objectives include a continued focus on promoting stakeholder voices in the boardroom.

Principal stakeholders in 2020 remained those previously identified by the Board – namely the Bank's clients, colleagues and shareholder, as well as suppliers, business partners and the local communities in which we operate. Three of these stakeholder groups provide the core metrics on which the Bank's performance is measured – namely client satisfaction (measured through NPS), colleague sentiment (measured through regular 'Our View' staff surveys), and shareholder returns (measured through RoE).

The level of engagement across these stakeholder groups intensified significantly during 2020 in response to the coronavirus pandemic. Whilst COVID-19 posed a range of significant challenges, the Bank's focus on its stakeholders and its over-arching purpose helped guide our response. Both NPS and colleague feedback scores reached record highs during the year. More details are provided below, in the various sections covering the Bank's different stakeholder groups.

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

Board training and support on s.172(1) duties

Directors are supported in the discharge of their duties by the Company Secretary. All directors receive guidance on their statutory duties, including on section 172(1), and receive regular 'teach-ins' on relevant topics outside of formal Board meetings. The Bank, as part of the NatWest Group, maintains an ongoing focus on stakeholder considerations; this is encouraged through templates for formal Board and Committee papers that require stakeholder considerations to be identified.

Clients

Meeting the needs of clients is central to the Bank's long-term success and is a constant feature of Board discussions and decisions. Client Net Promoter Scores are regularly reviewed by the Board and Executive Committee, and represent a key performance metric. Whilst the ability of the directors to meet clients was severely curtailed on account of the pandemic, the Bank intensified its client communications to support and inform clients throughout the year. Directors also participated in virtual sessions with clients. These included a series of "Coutts in Conversation" events, led by the Chairman, involving distinguished external speakers engaging with Coutts clients on topics of current interest.

The Bank also operates a Client Council, bringing together circa 700 clients from across the spectrum of our client base. Through the Client Council the Bank undertakes research several times a year to better understand clients' views and to help the Bank evolve in line with clients' needs. For instance, during 2020 13 members of the Client Council particpated in a pilot scheme between the Bank and CoGo to measure their carbon footprint.

Entrepreneur Month events and interaction with NWB accelerator hubs provided support for circa 2,500 entrepreneurs in the year. We are also partnering with the British Growth Fund (BGF) to establish a UK Enterprise Fund.

COVID-19 has inevitably had a significant impact on our clients. As a Bank we are proud to have assisted our clients through this turbulent period through participation in government backed lending schemes, which have seen advances of over £315 million across the various categories, and by implementing payment deferrals for our clients where appropriate.

Colleagues

Our colleagues

As at 31 December 2020, NWB had seconded 1,724 colleagues to the Group (2019 – 1,584) (full time equivalent basis, including temporary workers). Details explaining the increase in staff numbers and their related costs are included in note 3 to the consolidated accounts.

Engaging our colleagues

A highly engaged workforce is crucial in helping the Bank to achieve its vision to be the best Private Bank for the UK. To achieve this the Bank is striving to ensure it is a really great place to work.

Twice a year our colleagues are asked to share their views on what it is like to work for the Bank via a collective opinion survey. This year has been slightly different in that, as well as the main survey, we undertook several ad hoc pulse surveys in response to COVID-19. Most experiences have been positive, with the Bank enabling colleagues to work from home and encouraging flexible working. However, for some of our colleagues this has been a challenging time, particularly with physical and mental health and overall wellbeing. The main survey shows that our handling of the pandemic has helped to increase engagement levels to an all-time high. We are now ahead of benchmark GFS on all key measures.

During the COVID-19 pandemic we acted quickly to implement practical support for colleagues, and it remains imperative that we have the right support and channels available to our colleagues to help them recover and ultimately thrive throughout these challenging times. We have focused on ensuring that colleagues working from home have appropriate equipment, including laptops, mobile phones and furniture such as desks and chairs. In addition, we have temporarily moved colleagues with transferable skills to support our clients and cover workloads of colleagues, such as those required to self-isolate or with caring responsibilities, and we have adjusted our policies where necessary to support our colleagues and ensure that they are aware of the practical and emotional wellbeing support in place across the Bank.

Colleague voice
The Board promotes colleague voice in the boardroom through a variety of channels, including the operation of an 'open chair', which provides the opportunity for junior colleagues to attend board and committee meetings. The Bank established a People Council in 2018 to represent colleagues at all levels, and to act as custodian of the Bank's culture plan. The Council is made up of circa 50 colleagues from across all parts of the Bank and is instrumental in shaping the agenda following the outputs of colleague surveys. It also provides an opportunity for the Bank's Executive Committee and Board to engage directly with colleagues and hear first-hand about what it is like to work for the Bank, what is working well, where we could improve, and any challenges we face. Regular meetings are held with the Co-Chairs of the Council and the Chairman.

Colleague consultation
The Bank's work with the People Council and the Respect, Diversity & Inclusion Council (RD&I Council) is further supplemented by NatWest Group's colleague listening strategy. A NatWest Colleague Advisory Panel (made up of circa 30 colleagues, including representation from trade unions, works councils, colleague volunteers and colleague-led networks from across the NatWest Group) was established in 2018 and allows direct input from colleagues on a range of issues. The outputs of these sessions are also shared with the Bank.

Speak Up
One of the ways colleagues can report any concerns relating to wrong-doing or misconduct is by raising their concerns via Speak Up, NatWest Group's independent whistleblowing service. The 2020 colleague opinion survey showed the highest ever score when asking colleagues if they feel safe to speak up, as well as understanding the process of how they do that. In 2020 21 cases, which relate to the Bank (2019 - 27), were reported to Speak Up, and 19 of those were deemed as qualifying cases. All cases related to colleague conduct. No systemic issues were identified.

Building a healthy culture
The Board views building a high performing and healthy culture as essential to the Bank's long-term success. The Bank's culture plan focusses on becoming a purpose led organisation, helping people, families and businesses to thrive. It is underpinned by the Bank's vision to be the best Private Bank for the UK and by 'Our Values'. Our Values guide the way we serve our clients, how we work together and manage and mitigate risk. They help us to focus on the long term rather than the short term. 92% of colleagues tell us that Our Values and Purpose guide them every day, this is the highest ever score in this area.

Data from NatWest Group's participation in the Banking Standard Board (BSB) annual independent culture assessments supports improving colleague sentiment and the building of a healthy culture. Data from the 2020 survey shows we have continued to make good progress, improving in the majority of BSB categories, remaining static in one but not declining in any category. Key measures of Honesty, Accountability and Reliability improved by 2 points.

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

Rewarding our colleagues
Individual performance objectives are clearly linked to our vision and strategy. We take a balanced approach to managing performance that is linked to reward. This includes the conduct and behaviour of individuals in addition to financial performance. Delivering for our clients is key, as is the management of risk. This balanced approach to reward recognises both what the individual has achieved and how they have achieved it. The overall contribution is underpinned by Our Values, and we hold colleagues and leaders to account for performance and behaviours, both of themselves and their team.

Health and wellbeing of our Colleagues
Part of our culture plan is 'Our Way of Life'. We believe that the wellbeing of colleagues forms a large part of making the Bank a great place to work. As an employer we want to make sure our colleagues have the right support to be healthy and happy at work and feel able to bring their whole self to work.

Within the Bank we have a network of over 100 Wellbeing Ambassadors. They are there for colleagues to reach out to and can provide practical support and advice. The Bank has a programme of events throughout the year that focus on physical, mental and financial wellbeing with a host of resources and tool kits available to colleagues.

2020 has brought significant change for our colleagues, with the majority working from home as a result of restrictions introduced because of the COVID-19 pandemic, and many are continuing to live with local and regional lockdowns. These are challenging and anxious times for everyone. In response, in addition to its Employee Assistance Programme, the Bank has expanded its suite of wellbeing support with the launch of SilverCloud, our new wellbeing programme that provides a range of support with COVID-19 concerns, sleep, mindfulness, resilience and anxiety.

Developing our colleagues
At the heart of our culture plan is 'Our Potential'. We believe everyone has the ability to grow, and the right to be supported to reach their potential. We invest in the future with ongoing coaching, training, support and encouragement. Every colleague has a personal development plan, and core requirements for Continued Professional Development are mandatory. 100% of our frontline advisors hold professional qualifications and 100% of our frontline support colleagues qualify in their first 18 months in the Bank.

Our focus in 2020 has been on personal resilience and team effectiveness during times of change, supporting our leaders to lead effectively through this complex time.

Youth employment
In September 2020 we welcomed 12 graduates into our graduate schemes, plus 11 interns on a 4-week virtual programme given the circumstances around COVID-19. Gender balance and diversity are critical for these schemes in order to support a balanced workforce for the future. In 2020 we had above 50% BAME representation on all early career programmes including insight weeks, apprenticeships, internships and graduate schemes. Gender balance was above 50% representation for female hires on all programmes except apprentices (30%) and insight weeks (30%).

To support an inclusive workforce and social mobility we hold two insight weeks per year to encourage young people from all backgrounds, genders and ethnicities to come along and find out about career options within the Bank. In addition, this year we took part in the social mobility apprenticeship scheme where we partner with Leadership in Sport to take 10 apprentices from less privileged backgrounds onto apprenticeship schemes. We have also signed up to the 100 Black Interns initiative to get more Black people into the Investment Management Industry, and we intend to take on three Black interns in 2021 through this initiative.

Employment of people with disabilities
Within NatWest Group we have a network called Enable that is dedicated to making sure we are fully inclusive and that everyone is valued as an individual, regardless of disability.

In line with NatWest Group policy, the Bank ensures that prospective candidates with disabilities are considered for employment. Once they become a colleague we are committed to their training, career development and promotion based on merit. If a colleague becomes disabled during their career, it is the Bank's policy, wherever possible, to retain them in their existing role or to re-deploy to a more suitable role. Training is available for all line managers to help raise disability awareness across the Bank.

Inclusion
We know that more diverse and inclusive organisations perform better – inclusivity is not only the right thing to do but there is a strong business case for it. This year has seen a spotlight put on inclusion, particularly for our Black colleagues. This follows the events that happened in the US and the impact of the Black Lives Matter movement in the UK. Several listening events were held by the Ethnicity network and supported by senior colleagues. This resulted in a BAME Inclusion Plan that outlines the actions we are taking to improve diversity and inclusion. This plan underpins the NatWest Group's 10 commitments to improving diversity and inclusion following a report from a BAME task force – 'Banking on Racial Equality – a roadmap for positive change.'

Our vision to be the best Private Bank for the UK is dependent on having the best people that reflect our client base and wider society. It is therefore essential that we continue to build a diverse and inclusive organisation. This means that everyone has a seat at the table and everyone's voice is heard. We have a strong and active Respect, Diversity & Inclusion (RD&I) Council that is led by a group of colleagues who do a great job at all levels. The strands of the RD&I Council include faith, disability, ethnicity, age, gender, LGBT+ and social mobility.

The Board monitors diversity and inclusion on a quarterly basis to check progress against key measures. Internal policies such as on recruitment and promotion support this agenda. The overall aim is to have a fully gender balanced workforce by 2030 and that 14% of senior roles will be held by BAME colleagues by 2025. The latest data demonstrates good progress towards both targets over the last two years: Females at the top 3 levels of the organisation has increased from *25% to 33.6% (as at 31 December 2020) and BAME colleagues in the top 4 levels of the organisation have increased from *7% to 10.9% (as at 31 December 2020). Both targets remain a top priority on the people agenda, as we build a fully inclusive organisation.

Gender and Ethnicity pay gap data now forms part of NatWest Group's reporting: these are determined by the legal entity employer.

*Data relates to Wealth Businesses, including Coutts.

Community, Environment and Sustainability
We have a long and distinguished history of supporting philanthropic causes, derived from the work of Angela Burdett-Coutts. Angela was a progressive 19th century philanthropist who was concerned with breaking cycles of poverty, and the provision of basic human need. The Bank draws on this legacy in its support for the Coutts Charitable Foundation (the Foundation). Set up in 2013, the Foundation was established to support sustainable solutions that tackle the causes and consequences of poverty. The core focus of the Foundation is supporting women and girls in the UK.

In addition to supporting the Foundation, the Bank supports our communities in a variety of ways, recognising that our support this year was even more critical than usual given the impact of COVID-19 on our local communities and charities. Since March 2020, we have donated the food produce from our Sky-line Garden to The Connection and The Felix Project, charities dedicated to helping disadvantaged and vulnerable people. Our Coutts Cookbook also supports The Felix Project, with full sale proceeds being donated (over £5k). We also partnered with NatWest Group to raise £882k for the National Emergencies Trust COVID-19 fundraiser through a silent auction we ran for our clients. We continued our support for MoneySense, the NatWest financial education for children programme; for St Saviour's & St Olave's, a local girl's school; as well as for The Conservation Volunteers, where our staff help plant trees in local areas.

The Bank also has colleague nominated charities on which we focus fundraising efforts and events throughout the year. During 2020 the chosen theme was mental health and we have supported MQ and Place-2-Be, raising over £100k. Every colleague can take three days paid leave per year to volunteer in their local community or for a charity of their choice. We also encourage charitable donations using payroll giving.

The Board is committed to managing the wider social, environmental and economic impacts of the Bank's operations, products and propositions. Climate change, in particular, is recognised as a key risk for the Bank and governance has been established to manage the risks and opportunities related to this, as set out in the Task Force for Climate-Related Financial Disclosures (TCFD) statement (see page 7).

Suppliers
The Board recognises the key role suppliers play in ensuring the Bank delivers a reliable service to its clients. During the year, the Board continued to focus on the framework for managing intra-group as well as third-party suppliers. NatWest Group plc also launched a new Supplier Charter, replacing its previous Supplier Code of Conduct. The Charter sets out expectations in terms of ethical business conduct, human rights, environmental sustainability, and diversity and inclusion. In line with *Our Purpose*, it details not only what we expect from our suppliers but also outlines what our own commitments are in these key areas.

The Bank also publishes, as part of NatWest Group plc's statement, an annual statement on Modern Slavery and Human Trafficking, made in accordance with section 54 of the UK's Modern Slavery Act 2015.

Regulators
The Board recognises the importance of open and continuous dialogue with regulators. The Chair, CEO and Chair of the Risk and the Audit Committee meet regularly with the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA) through Continuous Assessment and Proactive Engagement meetings.

Shareholder
The Bank recognises the benefits that being part of the wider Group provides, for example in terms of the ability to call on extensive IT and other specialist resources, including in relation to cyber-crime defences. The shareholder's perspective is provided through interactions at both management and Board levels. Cross referrals between clients of the Bank and clients of the wider NatWest Group have continued to increase.

How stakeholder interests have influenced decision making
The Bank's key stakeholders and the range of engagement methods used by directors to understand their views and interests are described above.

The Bank recognises the importance of engaging with stakeholders to help inform its strategy and board decision-making. Relevant stakeholder interests, including those of clients, colleagues, its shareholder and others, are considered by the Board when it takes decisions.

The Bank defines principal decisions as those that are material or of strategic importance but also those that are significant to any of its key stakeholder groups.

In making its decisions, the Board considers the outcomes of relevant stakeholder engagement, as well as the need to maintain a reputation for high standards of business conduct, and to consider the long-term consequences of its decisions.

A key decision in this respect was taken by the Board during the year, later ratified by the Bank's shareholder, to seek accreditation as a Benefit Corporation (B-Corp). B-Corps are businesses that have been accredited as having reached a minimum threshold across ESG metrics and commit to continuous improvement.

In reaching its decision, the Board considered the implications of becoming a B-Corp in terms of all its stakeholders, including its clients, colleagues and shareholder. It concluded that, by setting out to achieve high standards across the areas specified for B-Corps, accreditation would provide further momentum to the Bank's efforts to take into account stakeholder considerations in all its activities, and to develop further as a purpose-led organisation.

Task Force for Climate-Related Financial Disclosures (TCFD) Statement

We recognise that climate change is a critical global issue, which has significant implications for all our stakeholders. NatWest Group Board is responsible for addressing climate change risks within the NatWest Group's overall business strategy and risk appetite, and for ensuring adequate resources are devoted to addressing the issue. The Bank operates within the NatWest Group-wide framework and is responsible for the long-term success of the Bank and delivery of sustainable value to its shareholder. The Bank is a signatory to the UN's PRI and, by being a subsidiary of NatWest Group, is also aligned to the UN Principles of Responsible Banking.

Our ambition is to be a leading bank in the UK, helping to address climate change and support the UK's transition to a net-zero economy. We have the following ambitions in place:

- For our own operations to be climate positive by 2025
- At least halve the climate impact of our financing activity by 2030, doing what is necessary to achieve alignment with the 2015 Paris Agreement
- 50% of our mortgage book being secured against homes with an Energy Performance Certificate (EPC) rated C or above by 2030
- Carbon intensity reductions of 25% in the equity parts of our discretionary portfolios and funds by the end of 2021, and a 50% overall carbon intensity reduction in our discretionary portfolios and funds by the end of 2030, which is in line with Intergovernmental Panel on Climate Change (IPCC) targets

Note - the baseline for all targets in December 2019

Governance

The Board has endorsed the Bank's climate goals and oversees the Bank's response to climate change risk and opportunities, including oversight of climate-related materiality assessments and disclosures. We have set up a Private Banking Climate Change Working Group, which has been established as a sub-committee of the Wealth Businesses Risk Committee, which is overseen by the Bank's CEO.

The Board's Risk Committee has a focus on the development of the Bank's risk management framework to address climate risks, oversee the Bank's risk appetite and performance against appetite.

Climate strategy

As an indispensable partner to our clients, we see it as our role to educate, remove barriers and actively support clients to reduce their carbon footprint via the provision of innovative and competitive financial products covering both lending and investments.

Our lending portfolios are principally focussed on UK residential mortgages (68% of our lending book) and we see this as a significant opportunity to make a positive impact in our banking business. The Bank has set challenging targets to increase the energy efficiency of our mortgage book. We believe that encouraging our clients to improve the EPC rating of their homes is one of the most constructive ways of meeting our climate ambitions.

To achieve our ambition of 50% of our mortgage book being secured against homes with an EPC rating C or above by 2030, we need 13% of existing mortgages to move above an EPC rating of D, while ensuring that the EPC distribution of new originations is aligned to our target. We have been working to identify opportunities and products to promote energy efficient lending, including ways of addressing the financial and non-financial barriers that prevent clients from increasing the energy efficiency of their homes.

Over the coming years we intend to continue to enhance the incorporation of climate-related risks in our banking and lending processes, capturing relevant information on climate variables at the point of application and from a wide range of external sources. To expand our reporting capabilities, we will leverage the NatWest Group's analytical capabilities and also engage with government bodies and third-party suppliers. Where possible, we seek to align with principles and approaches outlined by the Green Finance Institute.

With regard to our investment strategy, the Bank has made strong progress against the aforementioned carbon intensity goals: achieving a 29% reduction in the six months from 1 January to 30 June 2020 across all investment products, Coutts UK Multi-Asset Fund, Discretionary Portfolio Service and Coutts Invest Personal Portfolio Funds; and achieving the targets we set out for our Coutts Invest Personal Portfolio Funds 18 months ahead of the deadline. We did this by switching from traditional funds into funds that focus on companies with lower carbon footprints, lower fossil fuel reserves and strong consideration for ESG factors. In addition, in June 2020 we launched our first Sustainability report, focussed on our Responsible Investing journey and highlighting our climate commitments.

The Bank's asset management business is a signatory of the PRI, a network of Investors supported by the UN that encourages the use of responsible investment in order to enhance returns and better manage risks. Since 2019, the Bank has reported annually to the PRI on our investment and governance practices. We scored strongly in our 2020 submission, notably achieving an A+ for our Strategy and Governance, the highest rating possible and higher than the industry median rating of A. We also comply with the UK Stewardship Code, published by the UK's FRC, and have joined Climate Action 100+, an initiative led by over 300 asset managers and owners to engage with the world's largest corporate greenhouse gas emitters to improve their climate performance and ensure transparent disclosure of emissions.

For our voting and engagement activity we partner with EOS at Federated Hermes, who actively focus their stewardship activity on climate issues with the greatest potential for long-term positive outcomes. They do this by engaging on our behalf with the companies we are invested in, public policymakers, governments and sector organisations globally, to encourage policy that facilitates the transition to a low-carbon economy. Our new relationship with BlackRock, which saw the launch of five Coutts funds, is instrumental in helping us accelerate our influence on ESG activities.

We are currently working with an external provider to model the resilience of our funds and portfolios under several different climate warming scenarios, with the goal of enriching our investment process and incorporating physical and transition risks and opportunities into our investment decision-making.

Risk management

Identified financial risk from climate change, including both transition and physical risks, is being embedded into the Bank's existing enterprise-wide risk management frameworks. This will enable informed risk-based decisions that support the delivery of the Bank's strategic objectives within the Board-approved risk appetite.

NatWest Group is undertaking scenario testing and reviewing the emissions associated with mortgages across NWG, including Coutts. In response to this analysis, targeted sector and product reviews will be executed to improve measurement and assessment of climate-related risk factors (e.g. flood risk and energy efficiency regulations for UK mortgages and Commercial Real Estate) and incorporated into our established sector and product concentration risk frameworks. Credit Risk ensure co-ordination with frontline Banking and Lending Client Journey teams to assess the impact of the changing risk environment and policy response on our client base across these frameworks.

As an asset manager working on behalf of our clients, we are mandated to make asset allocation decisions that serve the long-term investment shared values of both our clients and the Bank in regard to climate change. We are working with industry leading experts and are leveraging external models to build climate-related scenarios that will help to inform the investment committee on appropriate action to take within portfolios in order to minimise the risks associated with the transition to a lower carbon economy. It will also help with identifying opportunities that will support the transition to a net-zero carbon economy.

Metrics

We are working to further enhance our climate reporting over the next 12 months, and have committed to improving disclosure around climate risks in our loan book and investment portfolios. Our current lending metrics focus on EPC and flood risk measurement; with investment metrics focussed on carbon intensity.

We are working with a third party to analyse the different possible outcomes for climate change and the policies to mitigate it, assessing the financial impact and determining the timeframes during which risks could materialise. We will also use these findings to assess any vulnerabilities on our own balance sheet.

By order of the Board:

Waldegrave of North Hill
Waldegrave of North Hill (Mar 18, 2021 14:25 GMT)

The Rt Hon Lord Waldegrave of North Hill
Chair

Date: Mar 18, 2021

Coutts & Company is registered in England and Wales No. 00036695

BOARD OF DIRECTORS AND SECRETARY

Chair and Independent Non-Executive Director
The Rt Hon Lord Waldegrave of North Hill
Remuneration, Nominations (Chair)

Executive Directors
Peter Gordon Flavel
Chief Executive

Andrew Richard Kyle
Finance Director

Independent Non-Executive Directors
Francesca Barnes
Audit (Chair), Risk (Chair), Remuneration, Nominations

Mark Joseph Lund
Audit, Risk, Remuneration, Nominations

Linda Hamilton Urquhart OBE
Audit, Risk, Remuneration (Chair), Nominations

Non-Independent Non-Executive Director
Matthew Edward James Waymark
Audit, Risk

Company Secretary
Ralph Ricks

Audit	Member of the Audit Committee
Risk	Member of the Risk Committee
Remuneration	Member of the Performance and Remuneration Committee
Nominations	Member of the Nominations Committee

For additional detail on the activities of the Committees above, refer to the Report of the directors.

Appointments & Resignations
Matthew Edward James Waymark (Non-Executive Director) appointed on 9 March 2020

Auditors
Ernst & Young LLP
Statutory Auditor
25 Churchill Place
London
United Kingdom
E14 5EY

Registered office
440 Strand
London
United Kingdom
WC2R 0QS

Coutts & Company
Registered in England and Wales No. 00036695

RISK AND CAPITAL MANAGEMENT

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

Update on COVID-19

The unprecedented challenge posed by the global pandemic – for families, businesses and governments around the world – also led to a number of significant risk management challenges. The Group remained committed to supporting its clients while operating safely and soundly in line with its strategic objectives. Most notably, the credit risk profile was heightened due to deteriorating economic conditions. The Group provided a significant level of payment deferrals during the crisis, and facilitated support through the government's Bounce-Back Loan Scheme (BBLS), Coronavirus Business Interruption Loan Scheme (CBILS) and Coronavirus Large Business Interruption Loan Scheme (CLBILS) initiatives. This is detailed in the Credit risk section.

In addition, the Group's operational risk profile became heightened due to the need to adapt working methods and practices to large-scale working from home and the requirement to respond to the crisis – and provide client support – at pace.

As a result of its strong balance sheet and prudent approach to risk management, the Group remains well placed to withstand the impacts of COVID-19 as well as providing support to clients when they need it most.

Risk management framework

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

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

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

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

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

Culture
Culture is at the centre of both the risk management framework and risk management practice. The target culture across the Group is one in which risk is part of the way colleagues work and think. The target risk culture behaviours are aligned to the Group's core values. They are embedded in Our Standards, how we approach supporting *Our Purpose,* and therefore form an effective basis for risk culture since these are used for performance management, recruitment and development.

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

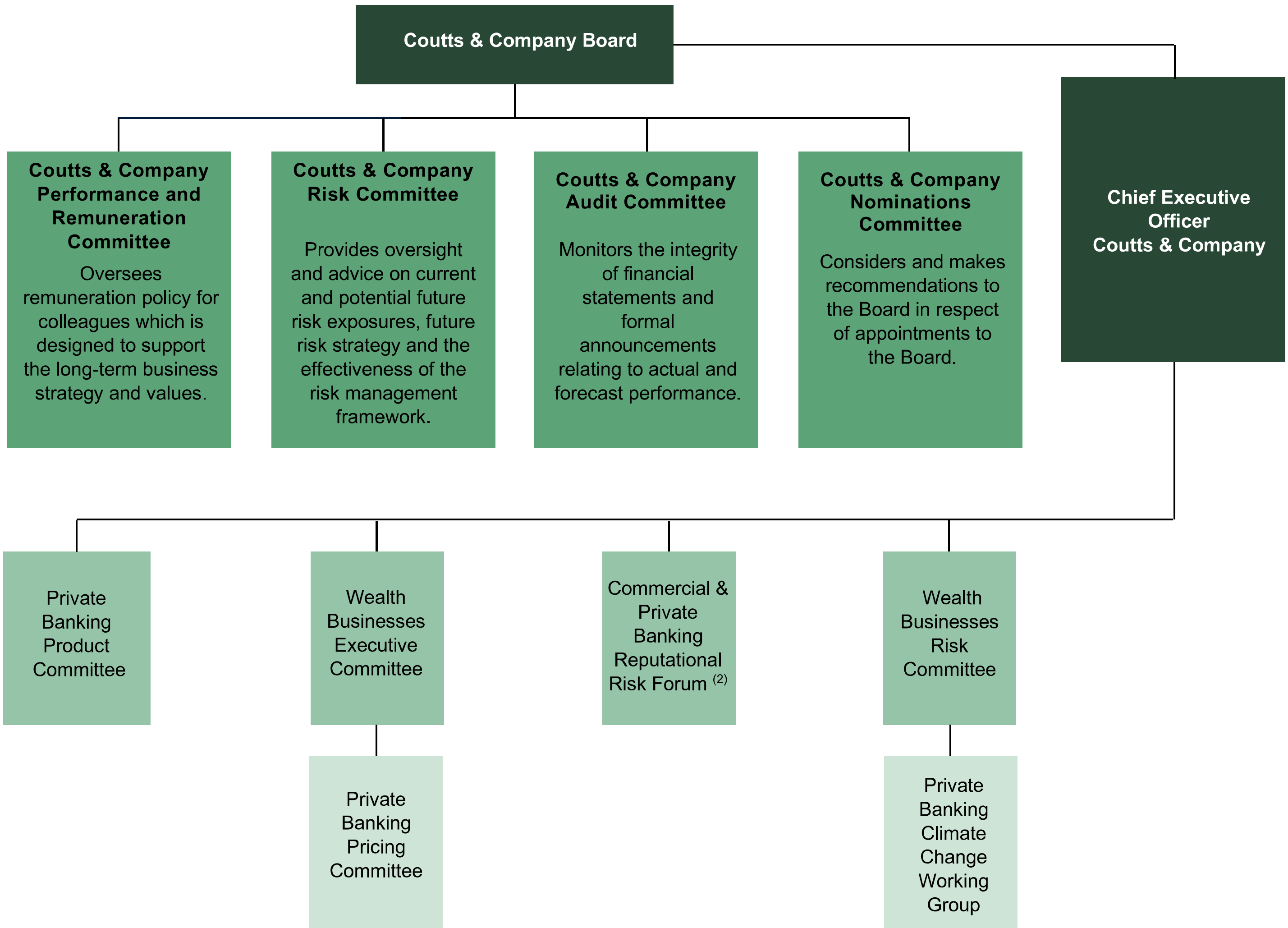
Code of Conduct
NatWest Group's conduct guidance Our Code provides direction on expected behaviour and sets out the standards of conduct that support the values. The code explains the effect of decisions that are taken and describes the principles that must be followed.

Risk management framework continued

Governance

Committee structure

The diagram shows the Group's risk committee structure in 2020 and the main purposes of each committee.



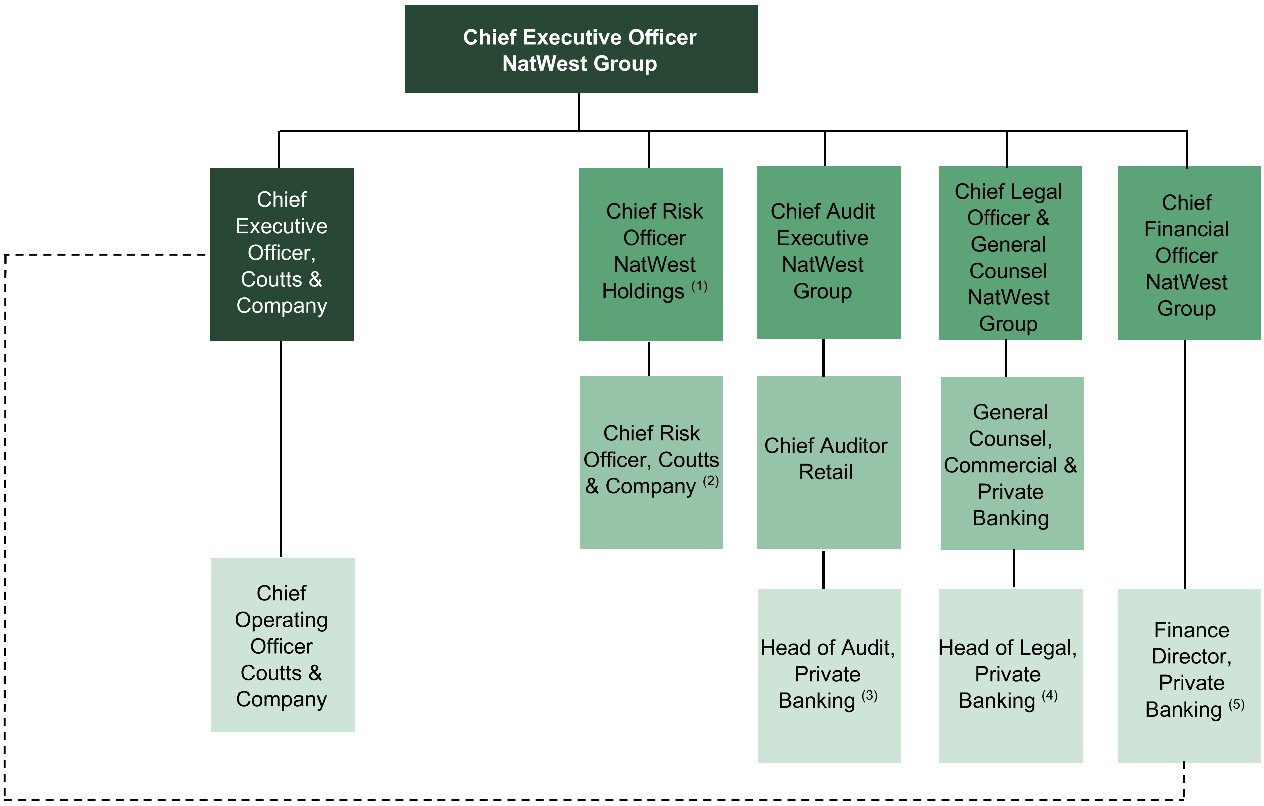
Notes:

(1) NatWest Holdings' Wealth businesses, including Private Banking, were brought together under the Chief Executive Officer, Wealth Businesses (who is also the Chief Executive Officer, Coutts & Company) during Q3 2020. The Private Banking committees are in the process of being renamed and this will be completed in 2021. Corporate Governance & Regulatory Affairs, Audit, Risk, Finance and Legal provide support and oversight to Wealth Businesses and are unaffected by this restructure.

(2) The Commercial & Private Banking Reputational Risk Forum is accountable to the Chief Executive Officer, Coutts & Company and the Chief Executive Officer, Commercial Banking.

Risk management framework continued

Management structure
The diagram shows the Group's risk management structure in 2020.



Notes:

(1) The Chief Risk Officer NatWest Holdings is also NatWest Group's Chief Risk Officer.
(2) The Chief Risk Officer Coutts & Company reports directly to the Chief Risk Officer NatWest Holdings. The Chief Risk Officer, Coutts & Company also has a right of access to the Coutts & Company Risk Committee.
(3) The Head of Audit, Private Banking reports directly to the Chief Auditor, Retail.
(4) The Head of Legal, Private Banking reports directly to the General Counsel, Commercial & Private Banking.
(5) The Finance Director, Private Banking reports directly to the Chief Financial Officer, with a secondary reporting line to the Chief Executive Officer, Coutts & Company.

Risk management framework continued

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

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

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

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

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

The risk appetite framework, which is approved annually by the Board, bolsters effective risk management by promoting sound risk-taking through a structured approach, within agreed boundaries. It also ensures emerging risks and risk-taking activities that would be out of appetite are identified, assessed, escalated and addressed in a timely manner.

Risk appetite is maintained across the Group through risk appetite statements. These provide clarity on the scale and type of activities that can be undertaken in a manner that is easily conveyed to staff.

The annual process of establishing risk appetite statements is completed alongside the business and financial planning process. This ensures plans and risk appetite are appropriately aligned. The Board sets risk appetite for the most material risks to help ensure the Group is well placed to meet its priorities and long-term targets even in challenging economic environments. It is the basis on which the Group remains safe and sound while implementing its strategic business objectives.

The Group's risk profile is frequently reviewed and monitored and management focus is concentrated on all strategic risks, material risks and emerging risk issues. Risk profile relative to risk appetite is reported regularly to the Board and senior management.

Risk controls and their associated limits are an integral part of the risk appetite approach and a key part of embedding risk appetite in day-to-day risk management decisions. A clear tolerance for material risk types is set in alignment with business activities.

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

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

The financial and non-financial risks that the Group faces are detailed in the Risk Directory. This provides a common risk language to ensure consistent terminology is used across NatWest Group. The Risk Directory is subject to annual review. This ensures that it continues to provide a comprehensive and meaningful list of the inherent risks within the Group.

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

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

Testing and monitoring
Targeted credit risk, compliance & conduct risk and financial crime risk activities are subject to testing and monitoring to confirm to both internal and external stakeholders – including the Board, senior management, the client-facing businesses, Internal Audit and the Group's regulators – that policies and procedures are being correctly implemented and operating adequately and effectively. Selected key controls are also reviewed. Thematic reviews and deep dives are also carried out where appropriate.

Risk management framework continued

The adequacy and effectiveness of selected key controls owned and operated by the second line of defence are also tested (with a particular focus on credit risk controls). Selected controls within the scope of Section 404 of the US Sarbanes-Oxley Act 2002, as well as selected controls supporting risk data aggregation and reporting, are also reviewed.

Anti-money laundering, sanctions, anti-bribery and corruption and tax evasion processes and controls are also tested and monitored. This helps provide an independent understanding of the financial crime control environment, whether or not controls are adequate and effective and whether financial crime risk is appropriately identified, managed and mitigated.

Stress testing

Stress testing – capital management

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

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

The process for stress testing consists of four broad stages:

Define scenarios	• Identify specific NatWest Group vulnerabilities and risks. • Define and calibrate scenarios to examine vulnerabilities and risks. • Formal governance process to agree scenarios.
Assess impact	• Translate scenarios into risk drivers. • Assess impact to current and projected P&L and balance sheet. • Impact assessment captures input from across NatWest Group.
Calculate results and assess implications	• Aggregate impacts into overall results. • Results form part of risk management process. • Scenario results are used to inform NatWest Group's business and capital plans.
Develop and agree management actions	• Scenario results are analysed by subject matter experts and appropriate management actions are then developed. • Scenario results and management actions are reviewed and agreed by senior management through executive committees, including the Executive Risk Committee, the Board Risk Committee and the Board.

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

Capital sufficiency – going concern forward-looking view

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

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

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

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

Capital allocation

NatWest Group has mechanisms to allocate capital across its legal entities and businesses. These aim to optimise the use of capital resources taking into account applicable regulatory requirements, strategic and business objectives and risk appetite. The framework for allocating capital is approved by the NatWest Group Asset & Liability Management Committee.

Risk management framework continued

Governance

Capital management is subject to substantial review and governance. The Board approves the capital plans, including those for key legal entities and businesses as well as the results of the stress tests relating to those capital plans.

Stress testing – liquidity

Liquidity risk monitoring and contingency planning

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

Internal assessment of liquidity

Under the liquidity risk management framework, NatWest Group maintains the Individual Liquidity Adequacy Assessment Process. This includes assessment of net stressed liquidity outflows under a range of extreme but plausible stress scenarios detailed in the table below.

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

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

Stress testing – recovery and resolution planning

The NatWest Group recovery plan explains how NatWest Group and its subsidiaries – as a consolidated group – would identify and respond to a financial stress event and restore its financial position so that it remains viable on an ongoing basis.

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

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

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

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

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

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

Stress testing – climate

NatWest Group will be carrying out climate scenario and stress-testing analysis as part of the BoE's 2021 biennial exploratory scenario. The exercise will explore three distinct climate scenarios over a 30 year horizon to test the financial system's resilience to climate-related risks

NatWest Group is also participating in the United Nations Environment Programme Finance Initiative focusing on analysis of how physical and transition risks could affect the agriculture and real estate sectors.

Risk management framework continued

Stress testing – non-traded market risk

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

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

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

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

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

Regulatory stress testing

NatWest Group has participated in the regulatory stress tests conducted annually by the BoE and biennially by the EBA. The results of these regulatory stress tests are carefully assessed and form part of the wider risk management of NatWest Group. However, in 2020 due to the impacts of COVID-19, the BoE and the EBA suspended their stress tests. Following the UK's exit from the European Union on 31 December 2020, only relevant European subsidiaries of NatWest Group will take part in the EBA tests going forward. NatWest Group itself will not participate.

Internal scenarios

During 2020, NatWest Group continuously refined and reviewed a series of internal scenarios - benchmarked against the BoE's illustrative scenario - as the impact of COVID-19 evolved, including actual and potential effects on economic fundamentals. These scenarios included:

- The impact of travel restrictions, social distancing policies, self-isolation and sickness on GDP, employment and consumer spending.
- The impacts on business investment in critical sectors.
- The effect on house prices, commercial real estate values and major project finance.
- The effect of government interventions such as the Job Retention Scheme and the Coronavirus Business Interruption Loan Scheme.

Applying the macro-scenarios to NatWest Group's earnings, capital, liquidity and funding positions did not result in a breach of any regulatory thresholds.

Credit risk

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

Sources of risk
The principal sources of credit risk are lending and related undrawn commitments.

The Group has both Retail and Commercial portfolios, with exposure materially concentrated within Retail.

Governance
The Credit Risk function provides oversight of frontline credit risk management activities on behalf of the Group.
Governance activities include:
- Defining credit risk appetite for the management of concentration risk and credit policy to establish the key causes of risk in the process of providing credit and the controls that must be in place to mitigate them.
- Approving and monitoring credit limits.
- Oversight of the first line of defence to ensure that credit risk remains within the appetite set by the Board and that controls are being operated adequately and effectively.
- Assessing the adequacy of expected credit loss (ECL) provisions including approving any necessary in-model and Post Model Adjustments (PMA) through provisions and model committees.

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

Retail
The Retail credit risk appetite framework sets limits that measure and control the quality and concentration of both existing and new business for each relevant business segment. The actual performance of each portfolio is tracked relative to these limits and management action is taken where necessary. The limits apply to a range of credit risk-related measures including expected loss at both portfolio and product level, projected credit default rates across products and the loan-to-value (LTV) ratio of the mortgage portfolios.

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

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

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

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

Identification and measurement
Credit stewardship
Risks are identified through relationship management and credit stewardship of clients and portfolios.

Credit risk stewardship takes place throughout the client relationship, beginning with the initial approval. It includes the application of credit assessment standards, credit risk mitigation and collateral, ensuring that credit documentation is complete and appropriate, carrying out regular portfolio or client reviews and problem debt identification and management. Additional stewardship measures were put in place in response to COVID-19. Refer to the Impact of COVID-19 section for further details.

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

Stage 1 loans are classified as performing with no significant increase in credit risk since initial recognition. Loans are classified as Stage 2 where they exhibit signs of a significant increase in credit risk since initial recognition but have no objective evidence of impairment. Stage 3 loans are classified as non-performing with objective evidence of impairment.

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

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

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

Residential mortgages – the Group takes collateral in the form of residential property to mitigate the credit risk arising from mortgages. The Group values residential property during the loan underwriting process by obtaining either a formal valuation or a desk top valuation (post COVID-19) at origination of the debt. The Group updates residential property values using the relevant residential property index, for example, the Office for National Statistics House Price Index.

CRE valuations – the Group has a panel of chartered surveying firms that cover the spectrum of geography and property sectors in which the Group takes collateral. Suitable valuers for particular assets are contracted through a single service agreement to ensure consistency of quality and advice. Valuations are generally commissioned when an asset is taken as security; a material increase in a facility is requested; or a default event is anticipated or has occurred.

Credit risk continued

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

Retail
To ensure that lending decisions are made consistently, the Group analyses internal credit information as well as external data supplied by credit reference agencies (including historical debt servicing behaviour of clients with respect to both the Group and other lenders). The Group then sets its lending rules accordingly, developing different rules for different products.

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

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

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

A credit assessment is carried out before credit facilities are made available to clients. The assessment process is dependent on the complexity of the transaction. Credit approvals are subject to ESG risk policies which restrict exposure to certain highly carbon intensive industries as well as those with potentially heightened reputational impacts.

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

Credit grades (PD) and loss given default (LGD) are reviewed and, if appropriate, re-approved.

Problem debt management

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

Retail clients experiencing financial difficulty are managed by the Risk Management team. If the Risk Management team is unable to provide appropriate support after discussing suitable options with the client, management of that client moves to the Recoveries team. If at any point in the collections and recoveries process, the client is identified as being potentially vulnerable, the client will be separated from the regular process and supported by a specialist team to ensure the client receives appropriate support for their circumstances.

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

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

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

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

Credit risk continued

Clients classified in the Heightened Monitoring category are those who are still performing but have certain characteristics – such as trading issues, covenant breaches, material PD downgrades and past due facilities – that may affect the ability to meet repayment obligations. Heightened Monitoring clients require pre-emptive actions to return or maintain their facilities within risk appetite prior to maturity.

Risk of Credit Loss clients are performing clients that have met the criteria for Heightened Monitoring and also pose a Risk of Credit Loss to the Group in the next 12 months should mitigating action not be taken or not be successful.

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

Restructuring

Where clients are categorised as Risk to Credit Loss, relationships are mainly managed by the Restructuring team. The purpose of Restructuring is to protect the Group's capital. Restructuring does this by working with corporate and commercial clients in financial difficulty on their restructuring and repayment strategies. Restructuring will always aim to recover capital fairly and efficiently.

Specialists in Restructuring work with clients experiencing financial difficulties and showing signs of financial stress. Throughout Restructuring's involvement, the mainstream relationship manager will remain an integral part of the client relationship, unless a repayment strategy is deemed appropriate. The objective is to find a mutually acceptable solution, including restructuring of existing facilities, repayment or refinancing.

Where a solvent outcome is not possible, insolvency may be considered as a last resort. However, helping the client return to financial health and restoring a normal banking relationship is always the preferred outcome.

Forbearance

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

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

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

In the Retail portfolio, loans are reported as forborne until they meet the exit criteria set out by the EBA. These include being classified as performing for two years since the last forbearance event, making regular repayments and the loan/debt being less than 30 days past due. Exit criteria are not currently applied for Commercial portfolios.

Types of forbearance

Retail

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

Commercial

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

Monitoring of forbearance

Retail

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

Commercial

In the Commercial portfolio, client PDs and facility LGDs are reassessed prior to finalising any forbearance arrangement.

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

Impact of COVID-19

COVID-19 has necessitated various changes to the "business as usual" credit risk management approaches set out above. Specific adjustments made to credit risk management as a result of COVID-19 are set out below.

Risk appetite

Retail

The onset of COVID-19 resulted in a significant deterioration in the economic outlook and consequently the credit environment. In response, credit risk appetite was tightened including changes to certain credit policy criteria, for example, maximum loan-to-values on new mortgage business. The criteria were reviewed and adapted on an ongoing basis throughout the year.

Commercial

At the outset of COVID-19, Wholesale Credit Risk undertook a vulnerability assessment of sectors and conducted more frequent monitoring of these portfolios, including sub-sector and single name analysis. Additional oversight forums for both new and existing client requests linked to sector, client viability and transaction value were also introduced. Monitoring of government support scheme lending, including tracking client lending journeys to prioritise resources, ensured clients could be supported in a timely manner. Risk appetite limits were reduced to reflect current risks and remain under constant review.

Identification and measurement

Credit stewardship

Commercial

The Group's credit stewardship included carrying out regular portfolio or client reviews and problem debt identification and management.

In line with existing credit policy parameters, relationship managers were able to defer annual reviews for a maximum of three months. These deferrals were used during 2020 to provide capacity to focus on supporting government lending scheme requests. Client review meetings took place virtually unless a specific client request was made, prior approval obtained and a risk assessment carried out.

Credit risk continued

Mitigation

Retail

During the COVID-19 lockdown from April to June in the UK, valuers were prohibited from conducting physical property inspections. As a result, mortgage application processing was suspended where a physical valuation was required. Applications eligible for remote valuations (known as desktops) were able to continue and the Group increased its valuation capacity to provide an additional quality assurance benchmark for ongoing assessment of desktop standards. Following the April to June lockdown, the application backlog was cleared once valuers were able to safely return to physical property inspections.

Commercial real estate valuations

Commercial property valuations were not conducted during the initial national lockdown due to travel restrictions, during which time physical valuations were postponed. Following this period, government guidance across the UK nations in respect of local and national lockdowns, confirmed that full internal property inspections could continue subject to adopting COVID-19 secure protocols. However, this required the full co-operation of occupiers and in addition, some commercial premises remained closed. Due to the limitations of some property valuations, The Royal Institute for Chartered Surveyors introduced a Material Valuation Uncertainty Clause (MVUC) for use at the time. There was a general lifting of the MVUC for all UK real estate valuations in September. However, where there is still considerable uncertainty for a location or particular sub-sector (for example, assets valued with reference to their trading potential such as hotels), the MVUC may still apply. This position has not changed with second wave local or subsequent national lockdowns.

Assessment and monitoring

Retail

Reflecting the deteriorated economic outlook, underwriting standards were tightened including additional information requirements from self-employed applicants.

Clients requesting a COVID-19 related payment deferral were not subject to a credit assessment for these requests.

Portfolio performance monitoring was expanded to include insight on clients accessing payment deferral support and their performance at the end of the payment deferral.

Commercial

The Group established guidance on credit grading in response to COVID-19 to ensure consistent and fair outcomes for clients, whilst appropriately reflecting the economic outlook.

- Within the Commercial portfolio, client credit grades were reassessed when a request for financing was made, a scheduled client credit review undertaken or a material event specific to that client occurred.
- A request for support using one of the government-backed COVID-19 support schemes was not, in itself, a reason for a client's credit grade to be amended.
- Large or complex clients were graded using financial forecasts, incorporating both the effect of COVID-19 and the estimated length of time to return to within credit appetite metrics.
- All other clients who were not subject to any wider significant increase in credit risk (SICR) triggers and who were assessed as having the ability in the medium-term post-COVID-19 to be viable and meet credit appetite metrics were graded using audited accounts.
- The Group identified those clients for whom additional borrowing would require remedial action to return to within risk appetite over the medium term, and clients who were exhibiting signs of financial stress before COVID-19. These clients were graded with reference to the impact COVID-19 had on their business.

Within the Commercial portfolio, additional monitoring was implemented to identify and monitor specific sectors which had been particularly adversely affected by COVID-19 and the use of government support schemes.

Problem debt management

Retail

In accordance with regulatory guidance, Retail clients were able to obtain a payment deferral of up to three months, twice, if requested. Such payment deferrals would not necessarily have been considered forbearance (refer to Forbearance below).

In addition, the Group suspended new formal repossession recovery action for Retail clients.

Commercial

In response to COVID-19, a new framework was introduced to categorise clients in a consistent manner across the Commercial portfolio, based on the impact of COVID-19 on their financial position and outlook in relation to the sector risk appetite. This framework was extended to all Commercial clients and supplemented the Risk of Credit Loss framework in assessing whether clients exhibited a SICR, and if support was considered to be granting forbearance.

Forbearance

Retail

In the absence of any other forbearance or SICR triggers, clients granted COVID-19 related payment deferrals were not considered forborne and were not subject to Risk Management team engagement. However, a subset of clients who had accessed payment deferral support, and where their risk profile was identified as relatively high risk, were collectively migrated to Stage 2. Any support provided beyond the completion of a second payment deferral is considered forbearance, provided the client's circumstances met the definitions for forbearance as described above.

Commercial

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

ECL modelling

The unprecedented nature of COVID-19 required various interventions in ECL modelling to ensure reasonable and supportable ECL estimates. These are detailed in the Model monitoring and enhancement section.

Credit grading models

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

Credit risk continued

Credit grading models are designed to provide:
- An assessment of client and transaction characteristics.
- A meaningful differentiation of credit risk.
- Accurate internal default, loss and EAD estimates that are used in the capital calculation or wider risk management purposes.

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

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

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

- Model build:
    - The determination of economic indicators that have most influence on credit loss for each portfolio and the severity of impact (this leverages existing stress testing models which are reviewed annually).
    - The build of term structures to extend the determination of the risk of loss beyond 12 months that will influence the impact of lifetime loss for assets in Stage 2.
- Model application:
    - The assessment of the SICR and the formation of a framework capable of consistent application.
    - The determination of asset lifetimes that reflect behavioural characteristics while also representing management actions and processes (using historical data and experience).
    - The choice of forward-looking economic scenarios and their respective probability weights.

IFRS 9 ECL model design principles
Modelling of ECL for IFRS 9 follows the conventional approach to divide the problem of estimating credit losses for a given account into its component parts of PD, LGD and EAD.

To meet IFRS 9 requirements, the PD, LGD and EAD parameters differ from their Pillar 1 internal ratings based counterparts in the following aspects:
- Unbiased – material regulatory conservatism has been removed from IFRS 9 parameters to produce unbiased estimates.
- Point-in-time – IFRS 9 parameters reflect actual economic conditions at the reporting date instead of long-run average or downturn conditions.
- Forward-looking – IFRS 9 PD estimates and, where appropriate, EAD and LGD estimates reflect forward-looking economic conditions.

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

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

The Group bases its calculations on the most appropriate NWB risk models; in particular NWB Premier for Retail and NWB Wholesale for Commercial.

The output of credit risk models is used in the credit approval process – as well as for ongoing assessment, monitoring and reporting – to inform risk appetite decisions. These models are divided into different categories. Where the calculation method is on an individual counterparty or account level, the models used will be:

- PD, based on the prevailing economic conditions.
- LGD, current assessment of the amount that will be recovered in the event of a default, taking into account future conditions.
- EAD, expected balance sheet EAD including the effects of amortisation, exposure is capped at the contractual limit.

Lifetime PDs are used in the assessment of a significant increase in credit risk, which also considers quantitative and qualitative measures.

PD estimates
Retail models
Retail PD models use the Exogenous, Maturity and Vintage (EMV) approach to model default rates. The EMV approach separates portfolio default risk trends into three components: vintage effects (quality of new business over time), maturity effects (changes in risk relating to time on book) and exogenous effects (changes in risk relating to changes in macro-economic conditions). The EMV methodology has been widely adopted across the industry because it enables forward-looking economic information to be systematically incorporated into PD estimates.

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

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

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

Retail
Forward-looking information has only been incorporated for the secured portfolios, where changes in property prices can be readily accommodated. Analysis has shown minimal impact of economic conditions on LGDs for the other Retail portfolios.

Credit risk continued

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

EAD estimates
Retail
The IFRS 9 Retail modelling approach for EAD is dependent on product type.

- Amortising products use an amortising schedule, where a formula is used to calculate the expected balance based on remaining terms and interest rates.
- There is no EAD model for Retail loans. Instead, debt flow (i.e. combined PD x EAD) is modelled directly.

Analysis has indicated that there is minimal impact on EAD arising from changes in the economy for all Retail portfolios except mortgages. Therefore, forward-looking information is only incorporated in the mortgage EAD model (through forecast changes in interest rates).

Commercial
For Commercial, EAD values are projected using product specific credit conversion factors (CCFs), closely following the product segmentation and approach of the respective Basel model. However, the CCFs are estimated over multi-year time horizons to produce unbiased model estimates.

No explicit forward-looking information is incorporated, on the basis that analysis has shown that temporal variations in CCFs are mainly attributable to changes in exposure management practices rather than economic conditions.

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

- Deferred model calibrations – ECL adjustments where model monitoring indicated that losses were being over predicted but where it was judged that an implied ECL release was not supportable. As a consequence, any potential ECL release was deferred and retained on the balance sheet.
- Economic uncertainty – ECL adjustments primarily arising from the economic uncertainty associated with COVID-19 (and Brexit for 2019) where management judged that additional ECL was required until further credit performance data is available on the effects of the various support mechanisms.
- Other adjustments – ECL adjustments where it was judged that the modelled ECL required to be amended.

ECL PMAs	2020 £m	2019 £m
Deferred model calibrations	—	—
Economic uncertainty (primarily within Commercial)	7.9	0.5
Other adjustments	—	—
Total	7.9	0.5

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

The framework comprises the following elements:
IFRS 9 lifetime PD assessment (the primary driver) – in commercial modelled portfolios the assessment is based on the relative deterioration in forward-looking lifetime PD and is assessed monthly. To assess whether credit deterioration has occurred, the residual lifetime PD at balance sheet date (which PD is established at date of initial recognition) is compared to the current PD. If the current lifetime PD exceeds the residual origination PD by more than a threshold amount deterioration is assumed to have occurred and the exposure transferred to Stage 2 for a lifetime loss assessment. For Commercial, a doubling of PD would indicate a SICR subject to a minimum PD uplift of 0.1%. For Retail portfolios, a simplified backstop based SICR method is used.

Qualitative high-risk backstops – the PD assessment is complemented with the use of qualitative high-risk backstops to further inform whether significant deterioration in lifetime risk of default has occurred. The qualitative high-risk backstop assessment includes features such as forbearance support, Commercial exposures managed within the Risk of Credit Loss framework, and adverse credit bureau results for Retail clients. Where a Retail client was granted a payment deferral in response to COVID-19, they were not automatically transferred into Stage 2. However, a subset of Retail clients who had accessed payment deferral support, and where their risk profile was identified as relatively high risk, were collectively migrated to Stage 2 (if not in Stage 2 already). Any support provided beyond completion of the second payment deferral was considered forbearance. Commercial clients accessing the various COVID-19 support mechanisms were assessed as detailed in the Impact of COVID-19 section.

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

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

Provisioning for forbearance
Retail
The methodology used for provisioning in respect of Retail forborne loans will differ depending on whether the loans are performing or non-performing.

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

Credit risk continued

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

For ECL provisioning, all forborne but performing exposures are categorised as Stage 2 and are subject to a lifetime loss provisioning assessment.

For non-performing forborne loans, the Stage 3 loss assessment process is the same as for non-forborne loans.

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

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

Forbearance may result in the value of the outstanding debt exceeding the present value of the estimated future cash flows. This difference will lead to a client being classified as non-performing.

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

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

Clients seeking COVID-19 related support, including payment deferrals, who were not subject to any wider SICR triggers and who were assessed as having the ability in the medium term post-COVID-19 to be viable and meet credit appetite metrics, were not considered to have been granted forbearance. Refer to the Impact of COVID-19 section for further details.

Asset lifetimes
The choice of initial recognition and asset duration is another critical judgement in determining the quantum of lifetime losses that apply.

- The date of initial recognition reflects the date that a transaction (or account) was first recognised on the balance sheet; the PD recorded at that time provides the baseline used for subsequent determination of SICR as detailed above.
- For asset duration, the approach applied (in line with IFRS 9 requirements) is:
  - Term lending – the contractual maturity date, reduced for behavioural trends where appropriate (such as, expected prepayment and amortisation).
  - Revolving facilities – for Retail portfolios, asset duration is based on behavioural life and this is normally greater than contractual life (which would typically be overnight). For Commercial portfolios, asset duration is based on annual counterparty review schedules and will be set to the next review date.

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

The most material economic loss drivers for Retail portfolios include house price index and base rate for the UK.

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

Economic scenarios
As at 31 December 2020, the range of anticipated future economic conditions was defined by a set of four internally developed scenarios and their respective probabilities. They comprised upside, base case, downside and extreme downside scenarios. The scenarios primarily reflect a range of outcomes for the path of COVID-19 and associated effects on labour and asset markets. The scenarios were consistent with the UK-EU Trade and Cooperation Agreement and are summarised as follows:

Upside – This scenario assumes a very strong recovery through 2021, facilitated by a very rapid rollout of the vaccine. Economic output regains its pre-COVID-19 peak by the end of the year. The rebound in consumer spending from an easing in lockdown restrictions is rapid, enabling a more successful reabsorption of furloughed labour compared to the base case. That limits the rise in unemployment. Consequently, the effect on asset prices is more limited compared to the base case.

Base case – The current lockdown restrictions are gradually loosened enabling a recovery over the course of 2021. The rollout of the vaccines proceeds as planned. Consumer spending rebounds as accumulated household savings are spent, providing support to the recovery in consumer-facing service sectors. Unemployment rises through to the second half of 2021, peaking at 7%, before gradually retreating. Housing activity slows in the second half of 2021 with a very limited decline in prices.

Downside – This scenario assumes the rollout of the COVID-19 vaccine is slower compared to base case, leading to a more sluggish recovery. Business confidence is slower to return while households remain more cautious. This scenario assumes that the labour market and asset market damage is greater than in the base case. Unemployment peaks at 9.4%, surpassing the financial crisis peak and causing more scarring.

Credit risk continued

Extreme downside – This scenario assumes a new variant of COVID-19 necessitates a new vaccine, which substantially slows the speed of rollout, delaying the recovery. There is a renewed sharp downturn in the economy in 2021. Firms react by shedding labour in significant numbers, leading to a very difficult recovery with the unemployment rate surpassing the levels seen in the 1980s. There are very sharp declines in asset prices. The recovery is tepid throughout the five-year period, meaning only a gradual decline in joblessness.

In contrast, as at 31 December 2019, the Group used five discrete scenarios to characterise the distribution of risks in the economic outlook. For 2020, the four scenarios were deemed appropriate in capturing the uncertainty in economic forecasts and the non-linearity in outcomes under different scenarios.

These four scenarios were developed to provide sufficient coverage across potential rises in unemployment, asset price falls and the degree of permanent damage to the economy, around which there are pronounced levels of uncertainty at this stage.

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

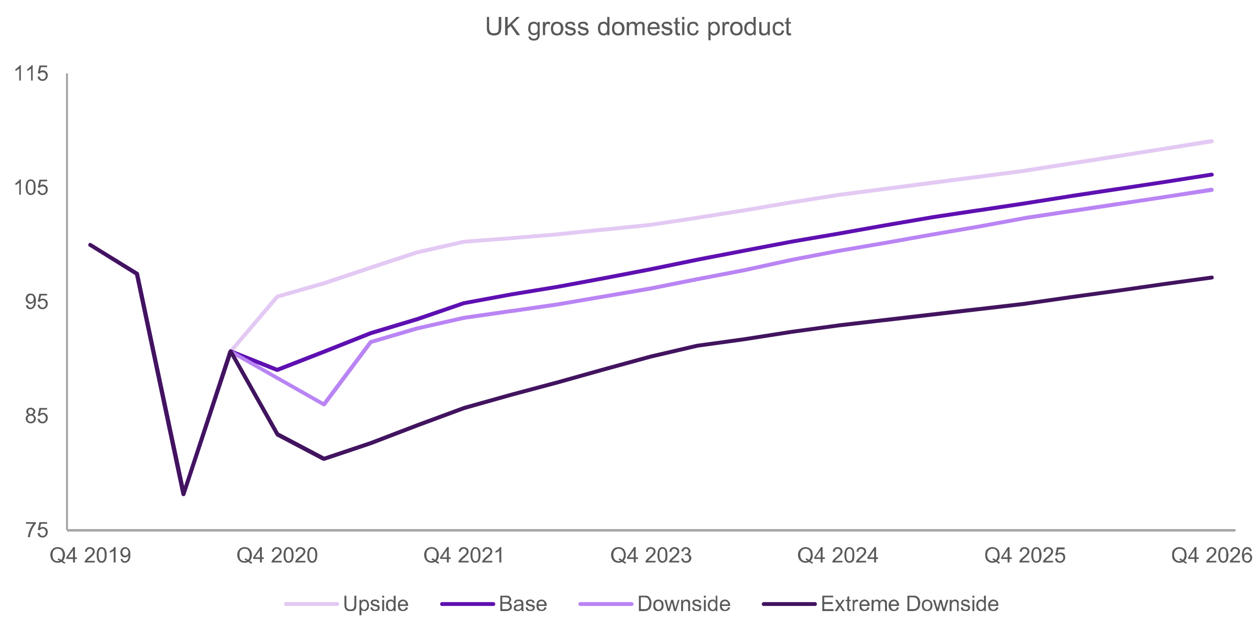
The main macroeconomic variables for each of the four scenarios used for ECL modelling are set out in the main macroeconomic variables table below. The compound annual growth rate (CAGR) for GDP is shown. It also shows the five-year average for unemployment and the BoE base rate. The House Price Inflation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

Main macroeconomic variables

	2020				2019				
Five-year summary	Upside %	Base case %	Downside %	Extreme downside %	Upside 2 %	Upside 1 %	Base case %	Downside 1 %	Downside 2 %
UK									
GDP - CAGR	3.6	3.1	2.8	1.3	2.5	2.3	1.6	1.3	0.9
Unemployment - average	4.4	5.7	7.1	9.7	3.6	3.9	4.4	4.6	5.2
House Price Inflation - total change	12.5	7.6	4.4	(19.0)	22.4	17.6	8.3	4.0	(5.1)
BoE base rate - average	0.2	—	(0.1)	(0.5)	1.0	0.7	0.3	—	—
Commercial real estate price - total change	4.3	0.7	(12.0)	(31.5)	13.0	8.1	(1.3)	(5.8)	(15.1)
World GDP - CAGR	3.5	3.4	2.9	2.8	3.9	3.3	2.8	2.5	2.0
Probability weight	20.0	40.0	30.0	10.0	12.7	14.8	30.0	29.7	12.7

Note:

- The five year period starts at Q3 2020 for 2020 and Q3 2019 for 2019.



Credit risk continued

Annual figures

UK GDP - annual growth

	Upside %	Base case %	Downside %	Extreme downside %
2020	(9.3)	(10.9)	(11.1)	(12.3)
2021	9.0	4.5	2.6	(4.6)
2022	2.6	4.2	4.6	6.1
2023	2.2	3.2	3.2	4.0
2024	2.3	2.8	3.1	2.3
2025	2.3	2.4	2.6	2.3

UK unemployment rate - annual average

	Upside %	Base case %	Downside %	Extreme downside %
2020	4.4	4.4	4.9	5.4
2021	5.6	6.3	8.5	12.3
2022	4.5	6.3	7.7	12.0
2023	3.8	5.5	6.7	9.0
2024	3.8	5.1	6.2	7.5
2025	3.9	5.1	6.2	7.3

UK House Price Inflation - four quarter growth

	Upside %	Base case %	Downside %	Extreme downside %
2020	2.7	1.5	(1.8)	(5.2)
2021	2.2	(3.0)	(7.4)	(26.9)
2022	1.7	3.6	6.5	5.1
2023	2.2	2.2	4.6	5.0
2024	2.8	2.8	2.8	5.6
2025	3.1	3.1	3.1	3.1

Commercial real estate price - four quarter growth

	Upside %	Base case %	Downside %	Extreme Downside %
2020	(7.7)	(9.5)	(16.6)	(21.4)
2021	2.6	(2.6)	(15.9)	(26.6)
2022	0.3	5.7	10.8	3.2
2023	0.4	(0.4)	3.2	3.2
2024	1.2	0.4	1.6	3.2
2025	1.2	1.2	1.2	1.2

Worst points

The worst points refer to the worst four-quarter rate of change for GDP, House Price Inflation and commercial real estate price and the worst quarterly figures for unemployment between 2020 and 2025.

	31 December 2020				31 December 2019	
	Upside	Base case	Downside	Extreme downside	Downside 1	Downside 2
UK	%	%	%	%	%	%
GDP (year-on-year)	(21.5)	(21.5)	(21.5)	(21.5)	(0.2)	(1.8)
Unemployment	5.9	7.0	9.4	13.9	4.9	5.5
House Price Inflation (year-on-year)	1.4	(3.6)	(11.2)	(29.8)	(3.5)	(8.4)
Commercial real estate price (year-on-year)	(7.7)	(12.3)	(29.7)	(41.1)	(8.2)	(12.6)

Peak (Q3 2020) to trough

	31 December 2020			
	Upside	Base case	Downside	Extreme downside
UK	%	%	%	%
GDP	—	(1.8)	(5.1)	(10.4)
House Price Inflation	—	(3.6)	(11.2)	(32.0)
Commercial real estate price	(3.4)	(10.1)	(28.9)	(40.4)

Credit risk continued

Probability weightings of scenarios

The Group's approach to IFRS 9 multiple economic scenarios (MES) involves selecting a suitable set of discrete scenarios to characterise the distribution of risks in the economic outlook and assigning appropriate probability weights. The scale of the economic impact of COVID-19 and the range of recovery paths necessitates a change of approach to assigning probability weights from that used in recent updates. Previously GDP paths for the Group's scenarios were compared against a set of 1,000 model runs, following which a percentile in the distribution was established that most closely corresponded to the scenario. This approach does not produce meaningful outcomes in the current circumstances because GDP is highly volatile and highly uncertain.

Instead, the Group has subjectively applied probability weights, reflecting internal expert views. The probability weight assignment was judged to present good coverage to the central scenarios and the potential for a far more robust recovery on the upside and exceptionally challenging outcomes on the downside. A 20% weighting was applied to the upside scenario, a 40% weighting applied to the base case scenario, a 30% weighting applied to the downside scenario and a 10% weighting applied to the extreme downside scenario. The Group judged a downside-biased weighting as appropriate given the risk to the outlook posed by the numerous factors influencing the path of COVID-19, the rollout of the vaccine and the pace at which social distancing restrictions can be relaxed.

Use of the scenarios in Retail lending

Personal lending follows a discrete scenario approach which means that for each account, PD and LGD values are calculated as probability weighted averages across the individual, discrete economic scenarios. The PD values for each discrete scenario are in turn calculated using product specific econometric models that aggregate forecasts of the relevant economic loss drivers into forecasts of the exogenous component of the respective PD models (refer to IFRS 9 ECL model design principles).

Use of the scenarios in Commercial lending

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

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

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

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

UK economic uncertainty

Treatment of COVID-19 relief mechanisms

Use of COVID-19 relief mechanisms (for example, payment deferrals, CBILS and BBLS) will not automatically merit identification of SICR and trigger a Stage 2 classification in isolation. However, a subset of Personal clients who had accessed payment deferral support, and where their risk profile was identified as relatively high risk were collectively migrated to Stage 2 (if not already captured by other SICR criteria).

For Commercial clients, the Group continues to provide support, where appropriate, to existing clients. Those who are deemed either (a) to require a prolonged timescale to return to within the Group's risk appetite, (b) not to have been viable pre-COVID-19, or (c) not to be able to sustain their debt once COVID-19 is over, will trigger a SICR and, if concessions are sought, be categorised as forborne, in line with regulatory guidance.

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

- The timing and nature of governmental exit plans from lockdown, notably in the UK, and any future repeated lockdown requirements.
- The progress of COVID-19, with potential for changes in worker/consumer behaviour and sickness levels.
- The efficacy of the various government support initiatives in terms of their ability to defray client defaults is yet to be proven, notably over an extended period.
- Any further damage to certain supply chains, most notably in the case of any re-tightening of lockdown rules but also delays caused by social distancing measures and possible export/import controls.
- The level of revenues lost by corporate clients and pace of recovery of those revenues may affect the Group's clients' ability to service their borrowing, especially in those sectors most exposed to the impacts of COVID-19.
- Higher unemployment if companies fail to restart jobs after periods of staff furlough.

This could potentially lead to further ECL increases. However, the income statement impact of this will be mitigated to some extent by the forward-looking provisions taken as at 31 December 2020.

Credit risk continued

Model monitoring and enhancement

The abrupt and prolonged interruption of a wide range of economic activities due to COVID-19 and the subsequent government interventions to support businesses and individuals, has resulted in patterns in the data of key economic loss drivers and loss outcomes, that are markedly different from those that the Group's models have been built on.

Government support

Most notably as a result of various government support measures, the increase in model-predicted defaults caused by the sharp contraction in GDP and consumer spending in Q2 2020, has to date, not materialised.

Accordingly, model-projected default rates in Commercial and Retail have been adjusted by introducing lags of up to 12 months. These lags are based partly on objective empirical data (i.e. the absence of increases in realised default rates by the reporting date) and partly judgmental, based on the extension of government support measures into 2021 and their expected effectiveness.

In Commercial lending, most importantly business and commercial banking, model-projected default rates have also been scaled down based on the expectation that credit extended under various government support loan schemes will allow many businesses, not only to delay, but to sustainably mitigate their default risk profile.

Extreme GDP movements – Commercial only

Due to the specific nature of COVID-19, GDP year-on-year movements in both directions are extremely sharp, many multiples of their respective extremes observed previously.

This creates a risk of overstretched, invalid extrapolations in statistical models. Therefore, all Commercial econometric models were updated to make them robust against extreme GDP movements by capping projected CCI values at levels corresponding to three times the default rates observed at the peak of the global financial crisis and using quarterly averages rather than spot values for CCI projections.

Industry sector detail – Commercial only

The economic impact of COVID-19 is highly differentiated by industry sector, with hospitality and other contact-based leisure, service, travel and passenger transport activities significantly more affected than the overall economy. On the other hand, the corporate and commercial econometric forecasting models used in Commercial are sector agnostic. Sector performance was therefore monitored throughout the year and additional adjustments were applied when PDs were deemed inconsistent with expected loss outcomes at sector level. No such interventions were necessary at the year end.

Scenario sensitivity – Retail only

For the Retail lending portfolio the forward-looking components of the IFRS 9 PD models were modified, leveraging existing econometric models used in stress testing to ensure that PDs appropriately reflect the forecasts for unemployment and house prices in particular.

All in-model adjustments described, have been applied by correcting the PD and LGD estimates within the core ECL calculation process and therefore consistently and systematically inform SICR identification and ECL measurement.

Additionally, post model ECL adjustments were made in Retail to ensure that the ECL was adjusted for known model over and under-predictions pre-existing COVID-19, pending the systematic re-calibration of the underlying models.

Measurement uncertainty and ECL sensitivity analysis

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

The focus of the simulations is on ECL provisioning requirements on performing exposures in Stage 1 and Stage 2. The simulations are run on a stand-alone basis and are independent of each other; the potential ECL impacts reflect the simulated impact as at 31 December 2020. Scenario impacts on SICR should be considered when evaluating the ECL movements of Stage 1 and Stage 2. In all scenarios the total exposure was the same but exposure by stage varied in each scenario.

Stage 3 provisions are not subject to the same level of measurement uncertainty – default is an observed event as at the balance sheet date.

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

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

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

Credit risk continued

Measurement uncertainty and ECL sensitivity analysis

2020	Actual	Upside	Downside	Extreme downside
Stage 1 modelled exposure (£m)				
Commercial	2,377	2,851	2,290	1,636
Stage 1 modelled ECL (£m)				
Commercial	24	21	25	20
Stage 1 coverage (%)				
Commercial	1.0%	0.7%	1.1%	1.2%
Stage 2 modelled exposure (£m)				
Commercial	1,778	1,304	1,865	2,519
Stage 2 modelled ECL (£m)				
Commercial	65	44	73	115
Stage 2 coverage (%)				
Commercial	3.7%	3.4%	3.9%	4.6%
Stage 1 and Stage 2 modelled exposure (£m)				
Commercial	4,155	4,155	4,155	4,155
Stage 1 and Stage 2 modelled ECL (£m)				
Commercial	89	65	98	135
Stage 1 and Stage 2 coverage (%)				
Commercial	2.1%	1.6%	2.4%	3.2%
Reconciliation to Stage 1 and Stage 2 ECL (£m)				
ECL on modelled exposures	89	65	98	135
ECL on non-modelled exposures	8	8	8	8
Total Stage 1 and Stage 2 ECL	97	73	106	143
Variance – (lower)/higher to actual total Stage 1 and Stage 2 ECL		(24)	9	46

Notes:

- Variations in future undrawn exposure values across the scenarios are modelled, however the exposure position reported is that used to calculate modelled ECL as at 31 December 2020 and therefore does not include variation in future undrawn exposure values.
- Reflects ECL for all modelled exposure in scope for IFRS 9; in addition to loans this includes bonds and cash. The analysis excludes non-modelled portfolios.
- All simulations are run on a stand-alone basis and are independent of each other, with the potential ECL impact reflecting the simulated impact as at 31 December 2020.
- Refer to the Economic loss drivers section for details of economic scenarios.
- 2019 comparatives are not included as the sensitivity scenario analysis relates to the 31 December 2020 balance sheet position.

Credit risk continued

Banking activities

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

Refer to Accounting policy 14 and Note 8 to the accounts for policies and critical judgements relating to impairment loss determination.

Portfolio summary - sector analysis

The table below summarises financial assets gross of ECL, related ECL provisions, impairment and past due by sector and asset quality.

	Group			Bank		
	Retail	Commercial	Total	Retail	Commercial	Total
2020	£m	£m	£m	£m	£m	£m
Loans by asset quality (1)	12,508	4,333	16,841	12,079	4,306	16,385
- AQ1-AQ4	4,678	1,262	5,940	4,475	1,240	5,715
- AQ5-AQ8	7,346	3,030	10,376	7,162	3,025	10,187
- AQ9	234	6	240	223	6	229
- AQ10	250	35	285	219	35	254
Loans by stage	12,508	4,333	16,841	12,079	4,306	16,385
- Stage 1	12,117	2,558	14,675	11,723	2,532	14,255
- Stage 2	141	1,740	1,881	137	1,739	1,876
- Stage 3	250	35	285	219	35	254
Loans - past due analysis	12,508	4,333	16,841	12,079	4,306	16,385
- Not past due	12,229	4,325	16,554	11,832	4,298	16,130
- Past due 1-30 days	18	-	18	18	-	18
- Past due 31-90 days	30	1	31	30	1	31
- Past due 91-180 days	144	-	144	130	-	130
- Past due > 180 days	87	7	94	69	7	76
Loans - Stage 2	141	1,740	1,881	137	1,739	1,876
- Not past due	113	1,739	1,852	109	1,738	1,847
- Past due 1-30 days	17	-	17	17	-	17
- Past due 31-90 days	11	1	12	11	1	12
Weighted average life*						
- ECL measurement (years)	2	4	4	2	4	4
Weighted average 12 month PDs*						
IFRS 9 (%)	0.1	5.6	1.5	0.1	5.6	1.5
Basel (%)	1.8	1.3	1.7	1.8	1.3	1.6
ECL provisions by stage	26	108	134	23	108	131
- Stage 1	6	24	30	6	24	30
- Stage 2	2	65	67	2	65	67
- Stage 3	18	19	37	15	19	34
ECL provisions coverage (%)	0.2	2.5	0.8	0.2	2.5	0.8
- Stage 1 (%)	-	0.9	0.2	0.1	1.0	0.2
- Stage 2 (%)	1.4	3.7	3.6	1.5	3.7	3.6
- Stage 3 (%)	7.2	54.3	13.0	6.8	54.3	13.4
ECL charges/(releases) - Third party	(4)	104	100	(4)	104	100
ECL loss rate - annualised (basis point)	-	2.4	0.6	-	2.4	0.6
Amounts written-off	-	3	3	-	3	3

*Not within audit scope

For the notes to this table refer to page 31.

Credit risk continued

	Group					
		Stage 2				
	Total credit exposure	Past due 1-30 days	Past due > 30 days	Total	Stage 3	ECL provisions
2020	£m	£m	£m	£m	£m	£m
Retail	12,508	17	11	28	250	26
Commercial	4,000	-	1	1	35	108
of which Property	*2,085*	-	*1*	*1*	*30*	*55*
Total financial assets excluding balances at central banks	16,508	17	12	29	285	134
Balances at and due from banks	333	-	-	-	-	-
Total financial assets	16,841	17	12	29	285	134
Total contingent liabilities and commitments	3,360	-	-	-	-	-
Total exposure	20,201	17	12	29	285	134

Included within total retail exposures of £12,508 million at 31 December 2020 are £11,213 million of balances which are covered by collateral and £1,269 million of balances which are exposed to credit risk without any collateral.

Included within total commercial exposures (including balances at and due from banks) of £4,333 million at 31 December 2020 are £3,219 million of balances which are covered by collateral and £1,006 million of balances which are exposed to credit risk without any collateral.

	Bank					
		Stage 2				
	Total credit exposure	Past due 1-30 days	Past due > 30 days	Total	Stage 3	ECL provisions
2020	£m	£m	£m	£m	£m	£m
Retail	12,079	17	11	28	219	23
Commercial	3,994	-	1	1	35	108
of which Property	*2,085*	-	*1*	*1*	*30*	*55*
Total financial assets excluding balances at central banks	16,073	17	12	29	254	131
Balances at and due from banks	312	-	-	-	-	-
Total financial assets	16,385	17	12	29	254	131
Total contingent liabilities and commitments	3,360	-	-	-	-	-
Total exposure	19,745	17	12	29	254	131

Credit risk continued

	Group			Bank		
	Retail	Commercial	Total	Retail	Commercial	Total
2019	£m	£m	£m	£m	£m	£m
Loans by asset quality [1]	11,439	3,585	15,024	10,813	3,565	14,378
- AQ1-AQ4	6,406	960	7,366	6,025	941	6,966
- AQ5-AQ8	4,805	2,608	7,413	4,601	2,607	7,208
- AQ9	63	2	65	58	2	60
- AQ10	165	15	180	129	15	144
Loans by stage	11,439	3,585	15,024	10,813	3,565	14,378
- Stage 1	11,007	3,285	14,292	10,429	3,265	13,694
- Stage 2	267	285	552	255	285	540
- Stage 3	165	15	180	129	15	144
Loans - past due analysis	11,439	3,585	15,024	10,813	3,565	14,378
- Not past due	11,182	3,566	14,748	10,600	3,546	14,146
- Past due 1-30 days	55	2	57	51	2	53
- Past due 31-90 days	66	5	71	59	5	64
- Past due 91-180 days	61	-	61	50	-	50
- Past due > 180 days	75	12	87	53	12	65
Loans - Stage 2	267	285	552	255	285	540
- Not past due	175	278	453	171	278	449
- Past due 1-30 days	52	2	54	48	2	50
- Past due 31-90 days	40	5	45	36	5	41
Weighted average life*						
- ECL measurement (years)	2	5	-	2	5	4
Weighted average 12 month PDs*						
IFRS 9 (%)	0.6	0.7	0.7	0.6	0.7	0.7
Basel (%)	1.0	1.2	1.1	1.0	1.2	1.1
ECL provisions by stage	25	14	39	20	14	34
- Stage 1	3	4	7	3	4	7
- Stage 2	2	4	6	2	4	6
- Stage 3	20	6	26	15	6	21
ECL provision coverage (%)	0.2	0.4	0.3	0.2	0.4	0.2
- Stage 1 (%)	-	0.1	-	-	0.1	0.1
- Stage 2 (%)	0.8	1.4	1.1	0.8	1.4	1.1
- Stage 3 (%)	12.1	40.0	14.4	11.6	40.0	14.6
ECL charges/(releases) - Third party	(2)	(5)	(7)	(2)	(5)	(7)
ECL loss rate (basis point) [2]	NA	NA	NA	NA	NA	NA
Amounts written-off	-	1	1	-	1	1

*Not within audit scope

Notes:

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

Internal asset quality band	PD range
AQ1	0% - 0.034%
AQ2	0.034% - 0.048%
AQ3	0.048% - 0.095%
AQ4	0.095% - 0.381%
AQ5	0.381% - 1.076%
AQ6	1.076% - 2.153%
AQ7	2.153% - 6.089%
AQ8	6.089% - 17.222%
AQ9	17.222% - 100%
AQ10	100%

(2) There was no ECL loss in 2019, therefore the ECL loss rate was not applicable.

Credit risk continued

	Group					
		Stage 2				
	Total credit exposure	Past due 1-30 days	Past due > 30 days	Total	Stage 3	ECL provisions
2019	£m	£m	£m	£m	£m	£m
Retail	11,439	52	40	92	165	25
Commercial	3,442	2	5	7	15	14
of which Property	*1,973*	-	-	-	*10*	*5*
Total financial assets excluding balances at central banks	14,881	54	45	99	180	39
Balances at and due from banks	143	-	-	-	-	-
Total financial assets	15,024	54	45	99	180	39
Total contingent liabilities and commitments	2,916	-	-	-	-	-
Total exposure	17,940	54	45	99	180	39

	Bank					
		Stage 2				
	Total credit exposure	Past due 1-30 days	Past due > 30 days	Total	Stage 3	ECL provisions
2019	£m	£m	£m	£m	£m	£m
Retail	10,813	48	36	84	129	20
Commercial	3,441	2	5	7	15	14
of which Property	*1,973*	-	-	-	*10*	*5*
Total financial assets excluding balances at central banks	14,254	50	41	91	144	34
Balances at and due from banks	124	-	-	-	-	-
Total financial assets	14,378	50	41	91	144	34
Total contingent liabilities and commitments	2,916	-	-	-	-	-
Total exposure	17,294	50	41	91	144	34

Credit risk continued

Retail portfolio

Mortgages represent the largest product in the loan portfolio. The table below shows the spread and risk of these exposures.

At 31 December 2020, LTV ratios were split by stage under IFRS 9.

	Group		Bank	
	2020 £m	2019 £m	2020 £m	2019 £m
Gross new mortgage lending (1)	2,078	2,027	2,078	2,027
Owner occupied exposure	1,860	1,810	1,860	1,810
Weighted average LTV	66%	65%	66%	65%
Buy-to-let	218	217	218	217
Weighted average LTV	62%	59%	62%	59%
Interest only - variable	1,053	665	1,053	665
Interest only - fixed	675	951	675	951
Retail lending				
Mortgages	10,345	9,377	9,915	8,754
Owner occupied	9,092	8,196	8,712	7,637
Buy-to-let	1,253	1,181	1,203	1,117
Interest only - variable	4,203	3,464	4,020	3,212
Interest only - fixed	4,509	4,356	4,392	4,157
ECL provisions	5	13	5	11
Other lending	2,163	2,062	2,164	2,059
ECL provisions	21	12	18	9
Total Retail lending	12,508	11,439	12,079	10,813
Mortgage LTV ratios				
- Total portfolio	58%	57%	59%	57%
- Stage 1/performing	58%	57%	58%	57%
- Stage 2/performing	62%	61%	62%	61%
- Stage 3/non-performing	64%	70%	65%	61%
- Buy-to-let	56%	54%	56%	55%
- Stage 1	56%	54%	56%	55%
- Stage 2	59%	57%	57%	60%
- Stage 3	53%	57%	53%	57%

Note:
(1) Excludes additional lending to existing clients.

The Group holds collateral in respect of net exposures. For individual loans and advances to banks and clients, the collateral includes mortgages over property and charges over business assets.

Credit risk continued

Flow statements

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

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

	Stage 1		Stage 2		Stage 3		Total	
Group	Financial assets £m	ECL £m	Financial assets £m	ECL £m	Financial assets £m	ECL £m	Financial assets £m	ECL £m
At 1 January 2020	14,184	7	542	6	175	26	14,901	39
Currency translation and other adjustments	3	-	(1)	-	-	-	2	-
Transfers from Stage 1 to Stage 2	(2,555)	(19)	2,555	19	-	-	-	-
Transfers from Stage 2 to Stage 1	1,096	17	(1,096)	(17)	-	-	-	-
Transfers to Stage 3	(75)	-	(85)	(1)	160	1	-	-
Transfers from Stage 3	25	-	6	-	(31)	-	-	-
Net re-measurement of ECL on stage transfer	-	(12)	-	41	-	7	-	36
Changes in risk parameters (model inputs)	-	31	-	16	-	12	-	59
Other changes in net exposure	1,715	7	(5)	2	(44)	(4)	1,666	5
Income statement charges	-	26	-	59	-	15	-	100
Amounts written-off	-	-	-	-	(3)	(3)	(3)	(3)
Other	-	(1)	-	1	-	(2)	-	(2)
At 31 December 2020	14,393	30	1,916	67	257	37	16,566	134
Net carrying amount	14,363		1,849		220		16,432	

Key point:

- The increase in ECL across all stages was primarily due to deterioration in the economic outlook.

Capital, liquidity and funding risk

Definitions

Capital

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

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

Liquidity and Funding

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

Funding consists of on-balance sheet liabilities that are used to provide cash to finance assets. Funding risk is the risk of not maintaining a diversified, stable and cost-effective funding base.

Liquidity and funding risks arise in a number of ways, including through the maturity transformation role that the Bank performs. The risks are dependent on factors such as:
- Maturity profile;
- Composition of sources and uses of funding;
- The quality and size of the liquidity portfolio;
- Commercial market conditions; and
- Depositor and investor behaviour.

Sources of risk

Capital

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

There are three broad categories of capital across these two tiers:
- CET1 capital - CET1 capital must be perpetual and capable of unrestricted and immediate use to cover risks or losses as soon as these occur. This includes ordinary shares issued and retained earnings.
- Additional Tier 1 (AT1) capital - This is the second type of loss absorbing capital and must be capable of absorbing losses on a going concern basis. The instruments are either written down or converted into CET1 capital when a pre-specified CET1 ratio is reached.
- Tier 2 capital - Tier 2 capital is supplementary capital and provides loss absorption on a gone concern basis. Tier 2 capital absorbs losses after Tier 1 capital. It typically consists of subordinated debt securities with a minimum maturity of five years.

Minimum requirement for own funds and eligible liabilities (MREL) - In addition to capital, other specific loss absorbing instruments, including senior notes issued by the Bank, may be used to cover certain gone concern capital requirements which, in the EU, is referred to as MREL. Gone concern refers to the situation in which resources must be available to enable an orderly resolution, in the event that the BoE deems that the Bank has failed or is likely to fail.

Liquidity

Liquidity risk is managed as part of the UK Domestic Liquidity Sub Group (UK DoLSub), which is regulated by the PRA and comprises NWH's four licensed deposit taking UK banks: National Westminster Bank Plc, The Royal Bank of Scotland plc, Coutts & Company, and Ulster Bank Limited.

NWH maintains a prudent approach to the definition of liquidity resources. NWH manages its liquidity to ensure it is always available when and where required, taking into account regulatory, legal and other constraints.

Liquidity resources are divided into primary and secondary liquidity as follows:
- Primary liquid assets include cash and balances at central banks, Treasury bills and other high quality government and US agency bonds.
- Secondary liquid assets are eligible as collateral for local central bank liquidity facilities. These assets include own-issued securitisations or whole loans that are retained on balance sheet and pre-positioned with a central bank so that they may be converted into additional sources of liquidity at very short notice.

Funding

The Bank is funded principally by its client deposits. Through NWB, the Bank retains access to a diversified set of funding sources, including Tier 2 capital and subordinated debt. The Bank also retains access to BoE funding facilities.

Managing capital requirements

In line with paragraph 135 of IAS 1 'Presentation of Financial Statements', the Bank manages capital having regard to regulatory requirements. Regulatory capital is monitored and reported on an individual basis by the Bank.

Risk management

Capital

Capital management is the process by which the Bank ensures that it has sufficient capital and other loss absorbing instruments to operate effectively including meeting minimum regulatory requirements, operating within Board approved risk appetite, maintaining credit ratings and supporting strategic goals. Capital management is critical in supporting the Bank's business.

Capital planning is integrated into the Bank's wider annual budgeting process and is assessed and updated at least monthly. Other elements of capital management, including risk appetite and stress testing, are set out on page 13 and 14 respectively.

Liquidity

Liquidity risk takes into account regulatory, legal and other constraints to ensure sufficient liquidity is available where required to cover liquidity stresses. The size of the liquidity portfolio held in the UK DoLSub is determined by referencing NWH's liquidity risk appetite. NWH retains a prudent approach to setting the composition of the liquidity portfolio, which is subject to internal policies and limits over quality of counterparty, maturity mix and currency mix.

NWB manages the majority of the UK DoLSub's liquidity portfolio under the responsibility of the NatWest Group Treasurer.

Funding

The Bank manages funding risk through a comprehensive framework which measures and monitors the funding risk on the balance sheet. Client deposits provide substantially more funding than client loans utilise.

Capital, liquidity and funding risk continued

Relief measures

The economic impact of COVID-19 was significant. While liquidity, capital and funding were closely monitored throughout, NatWest Group benefited from its strong positions, particularly in relation to CET1, going into the crisis. Prudent risk management continues to be important as the full economic effects of the global pandemic unfold.
In response to COVID-19 a number of relief measures to alleviate the financial stability impact have been announced and recommended by regulatory and supervisory bodies. One significant announcement in the quarter was on 26 June when the European Parliament passed an amended regulation to the CRR in response to the COVID-19 pandemic (the CRR COVID-19 amendment); NatWest Group has applied a number of the CRR amendments for FY 2020 reporting. The impact on capital and leverage of the CRR amendment and other relief measures are set out below.

- IFRS 9 transition - NatWest Group has elected to take advantage of the transitional regulatory capital rules in respect of ECL following the adoption of IFRS 9; it had previously had a negligible impact up to Q4 2019. The CRR COVID-19 amendment now requires a full CET1 addback for the movement in stage 1 and stage 2 ECL from 1 January 2020 for the next two years. The IFRS 9 transitional arrangement impact on Bank CET1 regulatory capital at 31 December 2020 is £80 million.
- CRR Leverage exposure - The CRR COVID-19 amendment accelerated a change in CRR2 to allow the netting of regular-way purchase and sales settlement balances. This has had no impact on Bank leverage exposure as at 31 December 2020.
- Infrastructure and SME RWA supporting factors - The CRR COVID-19 amendment allowed an acceleration of the planned changes to the SME supporting factor and the introduction of an Infrastructure supporting factor. Bank has implemented these beneficial changes to supporting factors which have reduced RWAs by c.£0.1 billion for SMEs.
- Capital buffers - Many countries announced reductions in their countercyclical capital buffer rates in response to COVID-19. Most notably for NatWest Group, the Financial Policy Committee reduced the UK rate from 1% to 0% effective from 11 March 2020. The CBI also announced a reduction of the Republic of Ireland rate from 1% to 0% effective from 1 April 2020.
- Software Assets - The CRR COVID-19 amendment accelerated the change to the regulatory treatment of software assets, so this revision came in prior to the year end. The change introduces the concept of prudential amortisation for software assets so that unamortised software is no longer deducted from CET1. By applying this amendment, the impact to Bank is an increase of 18 bps.

Minimum capital requirements

Capital adequacy ratios

The Bank is subject to minimum capital requirements relative to RWAs. The table below summarises the minimum ratios of capital to RWAs that the Bank is expected to have to meet.

Type	CET1	Total Tier 1	Total capital
Minimum capital requirements	4.5%	6.0%	8.0%
Capital conservation buffer	2.5%	2.5%	2.5%
UK countercyclical capital buffer (1)	-	-	-
Total (2)	7.0%	8.5%	10.5%

Notes:
(1) Many countries announced reductions in their countercyclical capital buffer rates in response to COVID-19. Most notably for NatWest Group, the Financial Policy Committee reduced the UK rate from 1% to 0% effective from 11 March 2020.
(2) The minimum requirements do not include any capital that the Bank may be required to hold as a result of the Pillar 2 assessment.

Leverage ratio

Following the joint announcement of UK Treasury, PRA and FCA on 16 November 2020, we expect the PRA to consult on the application of leverage ratios to individual legal entities and Groups during 2021.

Liquidity and funding ratios

The Bank is a member of the UK DoLSub, which is collectively subject to the minimum Liquidity Coverage Ratio requirement of 100%. The CRR2 amendments to the CRR will introduce a binding Net stable funding ratio (NSFR) requirement from 1 January 2022.

Net stable funding ratio

Following the joint announcement of UK Treasury, PRA and FCA on 16 November 2020 to postpone the future EU CRR2 element of the Basel 3 package, we understand the PRA is due to consult on a binding Net Stable Funding ratio (NSFR) requirement to be introduced from January 2022.

Capital, liquidity and funding risk continued

Measurement

Capital
(Unaudited)

	Bank	
	2020	2019
Composition of regulatory capital	£m	£m
Shareholders' equity	1,456	1,375
Other equity instruments	(200)	(200)
	1,256	1,175
Regulatory adjustments and deductions		
Goodwill and other intangible assets	(28)	(38)
Adjustments under IFRS9 transition arrangements	80	-
Other regulatory adjustments	(81)	(20)
	(29)	(58)
CET1 capital	1,227	1,117
Additional Tier 1 capital		
Qualifying instruments and related share premium	202	202
Tier 1 capital	1,429	1,319
Qualifying Tier 2 capital		
Paid up capital instruments and subordinated loans	266	266
Tier 2 capital	266	266
Total regulatory capital	1,695	1,585
Risk-weighted assets by risk		
Credit risk	9,107	8,262
Counterparty risk	31	35
Market risk	6	9
Operational risk	1,068	1,004
Total risk-weighted assets	10,212	9,310
Key capital ratios (1)		
CET1	12.0%	12.0%
Tier 1	14.0%	14.2%
Total capital	16.6%	17.0%

Note:
(1) Key capital ratios represent capital as a proportion of risk-weighted assets.

Capital, liquidity and funding risk continued

Liquidity and funding Risk

Key liquidity and related metrics monitored in relation to the UK DoLSub includes:

- Liquidity coverage ratio;
- Stressed outflow coverage;
- Net stable funding ratio; and
- Loan to Deposit ratio.

These metrics are compiled in line with regulatory guidance or industry standards, with own interpretation applied where appropriate. Monitoring of these measures allows for ongoing assessment of the position of the overall UK DoLSub liquidity portfolio, and ensures regulatory targets are, at minimum met or exceeded. The Bank's Liquidity metrics are monitored at the NWH Asset and Liabilities Committee.

Contractual maturity

The table shows the residual maturity of third party financial instruments, based on contractual date of maturity of the Group's banking activities.

	Group								
2020	Less than 1 month £m	1-3 months £m	3-6 months £m	6 months - 1 year £m	1-3 years £m	3-5 years £m	More than 5 years £m	Impairment provision £m	Total £m
Cash and balances at central banks	3	-	-	-	-	-	-	-	3
Loans to banks	284	-	-	49	-	-	-	-	333
Loans to customers	1,907	896	1,028	1,573	4,056	2,307	4,682	(132)	16,317
Total financial assets	2,194	896	1,028	1,622	4,056	2,307	4,682	(132)	16,653
Bank deposits	4	-	-	-	-	-	-	-	4
Customer deposits	27,953	1,144	1,007	38	-	-	-	-	30,142
Other financial liabilities	-	-	-	-	-	310	-	-	310
Subordinated liabilities	-	-	-	-	-	-	265	-	265
Total financial liabilities	27,957	1,144	1,007	38	-	310	265	-	30,721

	Group								
2019	Less than 1 month £m	1-3 months £m	3-6 months £m	6 months - 1 year £m	1-3 years £m	3-5 years £m	More than 5 years £m	Impairment provision £m	Total £m
Cash and balances at central banks	3	-	-	-	-	-	-	-	3
Loans to banks	104	-	-	39	-	-	-	-	143
Loans to customers	1,888	802	879	1,391	3,680	2,089	4,102	(39)	14,792
Total financial assets	1,995	802	879	1,430	3,680	2,089	4,102	(39)	14,938
Bank deposits	12	-	-	-	-	-	-	-	12
Customer deposits	23,360	2,680	183	167	-	-	-	-	26,390
Other financial liabilities	-	-	-	-	-	50	260	-	310
Subordinated liabilities	-	-	-	-	220	-	45	-	265
Total financial liabilities	23,372	2,680	183	167	220	50	305	-	26,977

Capital, liquidity and funding risk continued

Contractual maturity continued

2020	Less than 1 month £m	1-3 months £m	3-6 months £m	6 months - 1 year £m	1-3 years £m	3-5 years £m	More than 5 years £m	Impairment provision £m	Total £m
	Bank								
Cash and balances at central banks	3	-	-	-	-	-	-	-	3
Loans to banks	263	-	49	-	-	-	-	-	312
Loans to customers	1,866	875	1,006	1,535	3,932	2,236	4,566	(129)	15,887
Total financial assets	2,132	875	1,055	1,535	3,932	2,236	4,566	(129)	16,202
Bank deposits	4	-	-	-	-	-	-	-	4
Customer deposits	27,953	1,144	1,007	38	-	-	-	-	30,142
Other financial liabilities	-	-	-	-	-	310	-	-	310
Subordinated liabilities	-	-	-	-	-	-	265	-	265
Total financial liabilities	27,957	1,144	1,007	38	-	310	265	-	30,721

2019	Less than 1 month £m	1-3 months £m	3-6 months £m	6 months - 1 year £m	1-3 years £m	3-5 years £m	More than 5 years £m	Impairment provision £m	Total £m
	Bank								
Cash and balances at central banks	3	-	-	-	-	-	-	-	3
Loans to banks	85	-	39	-	-	-	-	-	124
Loans to customers	1,807	760	843	1,345	3,541	1,981	3,929	(34)	14,172
Total financial assets	1,895	760	882	1,345	3,541	1,981	3,929	(34)	14,299
Bank deposits	12	-	-	-	-	-	-	-	12
Customer deposits	23,360	2,680	183	167	-	-	-	-	26,390
Other financial liabilities	-	-	-	-	-	50	260	-	310
Subordinated liabilities	-	-	-	-	220	-	45	-	265
Total financial liabilities	23,372	2,680	183	167	220	50	305	-	26,977

Non-traded market risk

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

Sources of risk
The key sources of non-traded market risk largely comprise interest rate risk and foreign exchange risk.

Governance
Responsibility for identifying, measuring, monitoring and controlling market risk arising from non-trading activities lies with the relevant business. Market risk policy statements set out the governance and risk management framework.

Risk appetite
The Group's qualitative appetite is set out in the non-traded market risk appetite statement. Its quantitative appetite is expressed in terms of exposure limits. These limits are approved and monitored by the Asset & Liability Management Committee.

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

NTIRR comprises the following three primary risk types:

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

NTIRR can be measured from either an economic value-based or earnings-based perspective, or a combination of the two. Value-based approaches measure the change in value of the balance sheet assets and liabilities including all cash flows. Earnings-based approaches measure the potential impact on the income statement of changes in interest rates over a defined horizon, generally one to three years.

Value-at-risk
The Group uses VaR as its value-based approach and sensitivity of net interest earnings as its earnings-based approach.

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

Foreign exchange risk
Non-traded foreign exchange risk arises from client transactions and profits and losses that are in a currency other than the functional currency of the transacting operation.

The Group has no foreign subsidiaries and manages its exposures to overseas suppliers within specified limits.

Sensitivity of net interest earnings
Net interest earnings are sensitive to changes in the level of interest rates, mainly because maturing structural hedges are replaced at higher or lower rates and changes to coupons on managed rate client products do not always match changes in market rates of interest or central bank policy rates.

Earnings sensitivity is derived from a market-implied forward rate curve. Assumptions are applied to this curve to derive central bank policy rates. A simple scenario is shown that projects forward earnings over a 12-month period based on the 31 December 2019 balance sheet. A base-case earnings forecast is derived from the market-implied rate curve, which is then subject to interest rate shocks. The difference between the base-case forecast and the shock gives an indication of underlying sensitivity to interest rate movements.

The sensitivity of the net interest earnings table shows the expected impact, over 12 months, to an immediate upward or downward change of 25 and 100 basis points to all interest rates. Yield curves move in parallel in upward rate shocks. However, in downward rate shocks, interest rates are assumed to floor at 0% or, for euro rates, at the current negative rate. At 31 December 2020, the floor also affects sterling interest rates, reducing the size of the downward rate shock at most maturities.

Reported sensitivities should not be considered a forecast of future performance in these rate scenarios. The projections do not capture potential management action in response to unexpected changes in the interest rate environment. Actions that could reduce interest earnings sensitivity include changes in pricing strategies on client loans and deposits as well as hedging. Management action may also be taken to stabilise total income also taking into account non-interest income.

Non-traded market risk continued

The table below sets out the expected impact on net interest earnings of a movement in yield curves:

			Group		
	Euro	Sterling	US Dollar	Other	Total
2020	£m	£m	£m	£m	£m
+25bps shift in yield curves	1	31	2	-	34
-25bps shift in yield curves	-	(3)	(3)	-	(6)
+100bps shift in yield curves	4	77	10	1	92
-100bps shift in yield curves	-	(4)	(3)	-	(7)
2019					
+25bps shift in yield curves	1	11	1	-	13
-25bps shift in yield curves	-	(5)	(2)	-	(7)
+100bps shift in yield curves	5	46	5	1	57
-100bps shift in yield curves	-	(55)	(8)	(1)	(64)

Compliance & Conduct risk

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

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

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

Key developments in 2020
- A client-focused COVID-19 response was mobilised, which included prioritised resource and operational capacity, forbearance and participation in government schemes.
- In-life monitoring of client outcomes was extended to ensure treatment strategies remained timely, relevant and consistent, as a result of the continued economic uncertainty arising from COVID-19 and Brexit.
- Specialist training was delivered to support the continuous oversight of ring-fencing embeddedness.
- Work to develop a Digitised Rules Mapping platform was a significant management focus. The platform aims to facilitate risk-based rules mapping to regulatory obligations. This will enable more efficient risk management of regulatory compliance matters as well as intelligent risk taking.

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

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

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

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

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

Financial crime

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

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

Key developments in 2020
- In view of the challenges presented by COVID-19, financial crime policies were reviewed and, where appropriate, reviewed management approaches were adapted in line with regulatory guidance.
- A new enterprise-wide Financial Crime Hub was established in the first line to detect and prevent financial crime. The Hub will facilitate a common, consistent approach to managing financial crime.
- A multi-year transformation plan was developed to ensure that, as the financial crime threat evolves with changes in technology, the economy and wider society, risks relating to money-laundering, terrorist-financing, tax evasion, bribery and corruption and financial sanctions are managed, mitigated and controlled as effectively as possible.
- A new Financial Crime Executive Steering Group was established to provide oversight of the transformation plan and its implementation.

Governance
The Group participates in NatWest Group's principal financial crime risk management forum, the Financial Crime Risk Executive Committee, which is chaired by NatWest Group's Chief Financial Crime Risk Officer. The committee reviews and, where appropriate, escalates material financial crime risks and issues within the Group, initially to the Wealth Risk Committee and then to the Coutts Risk Committee, in addition to the NatWest Group Executive Risk Committee and the NatWest Group Board Risk Committee. The Bank is also represented on NatWest Group's Financial Crime Executive Steering Group, which includes members from both the first and second lines of defence. The Executive Steering Group provides oversight of processes, major projects, programme design and performance management. While fraud risk is managed separately in the first line of defence, the second line Financial Crime risk function provides oversight.

Risk appetite
There is no appetite to operate in an environment where systems and controls do not enable the identification, assessment, monitoring, management and mitigation of financial crime risk. The Group's systems and controls must be proportionate to the nature, scale and complexity of its businesses.

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

Monitoring and measurement
Financial crime risks are identified and reported through continuous risk management and regular reporting to the Coutts Board Risk Committee as well as to NatWest Group's senior risk committees and Board. Quantitative and qualitative data is reviewed and assessed to measure whether financial crime risk is within risk appetite.

Mitigation
Through the financial crime framework, relevant policies, systems, processes and controls are used to mitigate financial crime risk. This includes the use of dedicated screening and monitoring controls to identify people, organisations, transactions and behaviours that may require further investigation or other actions. Regular risk assessments ensure the Group has appropriate procedures to manage its inherent risks. In addition, mandatory training for colleagues ensures that all staff are aware of financial crime issues and the role they play in tackling financial crime. Centralised expertise within NatWest Group is available to detect and disrupt threats to the Group and its clients. Intelligence is also shared with law enforcement, regulators and government bodies to strengthen national and international defences against those who would misuse the financial system for criminal motives.

Climate-related risk

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

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

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

Within these broad categories specific climate risk factors have been identified, which give rise to climate-related risks over the short, medium and long-term.

Key developments in 2020
- Climate-related risk was elevated to a principal risk. In line with NatWest Group's risk management framework, the elevation will see the implementation of a dedicated risk policy, risk appetite statement and risk appetite measures, which are reportable to the NatWest Group Board Risk Committee.
- To support alignment with the 2015 Paris Agreement, NatWest Group developed the capability to estimate financed emissions and emissions intensities for the following: residential mortgages, agriculture (primary farming), automotive manufacturers and oil & gas extractors. The residential mortgage portfolio and these three sectors were deemed the most material in terms of their proportion of the Group's total loans and investments and susceptibility to disruption resulting from climate change.

Climate-related risk continued

- In preparation for the BoE's 2021 Climate Biennial Exploratory Scenario, NatWest Group developed and tested a scenario analysis methodology to quantify a range of climate-related risks to support business decision making and the development of management actions.
- Climate-related risk was included as a factor in setting sector oversight classifications, which drive the frequency and level at which sector credit risk appetite is reviewed.
- Guidance was issued to ensure appropriate consideration of climate-related risk in internal risk and control assessments.
- Enhancements have been made to the Environmental, Social & Ethical risk management framework to mitigate reputational risk from carbon intensive sectors and support the transition to a lower carbon economy.

Governance
The NatWest Group Board is responsible for monitoring and overseeing climate-related risk within the Group's overall business strategy and risk appetite.

NatWest Group Board approved the allocation of Senior Management Function responsibility for identifying and managing financial risks from climate change jointly to the Group Chief Executive Officer (CEO) and the Group Chief Risk Officer. This updated accountability supports the CEO's ownership of the Group's strategic climate purpose.

A Group-wide Climate Change Programme (GCCP) supports the delivery of climate-related objectives. The GCCP is overseen by an Executive Steering Group which is responsible for coordinating NatWest Group's response across climate-related regulations, risks and opportunities. The Executive Steering Group is co-chaired by the CEO and Chief Risk Officer.

Risk appetite
NatWest Group's ambition is to be a leading bank in the UK and the Republic of Ireland in the response to climate change. Its stated purpose is to reduce the climate impact of its financing activity by at least 50% before 2030 and to do what is necessary to achieve alignment with the 2015 Paris Agreement.

Work continued in 2020 to integrate climate-related risk into the risk management framework, including the development of appropriate risk appetite, metrics and targets. Where climate-related risk is deemed to have a material impact on a particular risk discipline, then changes to policies and procedures will be made accordingly. Availability of data and the robustness of risk measurement methodologies will influence the timing of any proposed changes.

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

In 2020, NatWest Group became the first major UK bank to join the Partnership for Carbon Accounting (PCAF), underlining its commitment to measuring and reducing its climate impact in accordance with the 2015 Paris Agreement.

To align the Group's financing activity with the goals of the 2015 Paris Agreement, work has focused on formulating estimated emissions intensities that are consistent with limiting global warming to well-below 2°C.

Operational risk

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

Sources of risk
Operational risk may arise from a failure to manage operations, systems, transactions and assets appropriately. This can take the form of human error, an inability to deliver change adequately or on time, the non-availability of technology services, or the loss of client data. Fraud and theft – as well as the threat of cyber attacks – are sources of operational risk, as is the impact of natural and man-made disasters. Operational risk can also arise from a failure to account for changes in law or regulations or to take appropriate measures to protect assets.

Key developments in 2020
- The impact of COVID-19 led to significant disruption and heightened the operational risk profile as the Group adapted to new ways of working, particularly due to lockdown protocols. The control environment was continually monitored to ensure the resulting challenges were safely addressed.
- A NatWest Group-wide response was mobilised – supported by additional reporting on client needs, people, processes and systems – to ensure the Board and senior management were regularly updated and to facilitate decision-making as COVID-19 evolved.
- The transformation agenda was reprioritised as a result of COVID-19, with some activities stopped or deferred. A full risk assessment on the impact of the reprioritised activity was completed to ensure the potential impacts were understood and mitigated.
- Operational resilience remained a key focus. A series of scenarios – setting out the crystallisation of severe but plausible combinations of significant risks – were developed in order to support planning and appropriate forward-looking risk management strategies.
- Despite the impact of COVID-19, the security threat was not significantly changed. The potential for cyber attacks on the Group's supply chain remained a focus. Significant enhancements in managing such incidents and the broader security control environment were made. This included completion of work in response to the outcome of the 2019 CBEST test.
- There was also continued oversight of the Group's preparations for the end of the transition period, following the UK's exit from the EU, to ensure processes and systems were appropriate to ensure continuity of service for clients.

Governance
A strong operational risk management function is vital to support the Group's ambitions to serve its clients better. Improved management of operational risk against defined appetite is vital for stability and reputational integrity.

The first line of defence is responsible for managing operational risks directly while the second line Operational Risk function is responsible for proactive oversight and continuous monitoring of operational risk management across the Group. The second line function is responsible for

Operational risk continued

reporting and escalating key concerns to Audit Committee, Risk Committee and the Board.

Risk appetite
Operational risk appetite supports effective management of material operational risks. It expresses the level and types of operational risk the Group is willing to accept to achieve its strategic objectives and business plans. The Group's operational risk appetite statement encompasses the full range of operational risks faced by its legal entities, businesses and functions.

Mitigation
The Control Environment Certification (CEC) process is a half-yearly self-assessment by the CEO. It provides a consistent and comparable view on the adequacy and effectiveness of the internal control environment.

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

The CEC process helps to ensure compliance with the NatWest Group Policy Framework, Sarbanes-Oxley 404 requirements concerning internal control over financial reporting (as referenced in the Compliance report on page 152 of the NatWest Group Annual Report and Accounts), and certain requirements of the UK Corporate Governance Code.

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

In H1 2020, due to the impacts of COVID-19, the formal certification process was suspended. It resumed again in H2.

Monitoring and measurement
Risk and control assessments are used across all business areas and support functions to identify and assess material operational and conduct risks and key controls. All risks and controls are mapped to the NatWest Group's Risk Directory. Risk assessments are refreshed at least annually to ensure they remain relevant and capture any emerging risks and also ensure risks are reassessed.

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

The Group uses the standardised approach to calculate its Pillar 1 operational risk capital requirement. This is based on multiplying three years' average historical gross income by coefficients set by the regulator based on business line.

As part of the wider Internal Capital Adequacy Assessment Process an operational risk economic capital model is used to assess Pillar 2A, which is a risk-sensitive add-on to Pillar 1. The model uses historical loss data (internal and external) and forward-looking scenario analysis to provide a risk-sensitive view of the Group's Pillar 2A capital requirement.

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

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

Operational resilience
The Group manages and monitors operational resilience through its risk and control assessment methodology. This is underpinned by setting and monitoring risk indicators and performance metrics for key business services. Progress continues on the response to regulator expectations on operational resilience, with involvement in a number of industry-wide operational resilience forums. This enables a more holistic view of the operational resilience risk profile and the pace of ongoing innovation and change, both internally and externally.

Event and loss data management
The operational risk event and loss data management process ensures the Group captures and records operational risk financial and non-financial events that meet defined criteria. Loss data is used for regulatory and industry reporting and is included in capital modelling when calculating economic capital for operational risk. The most serious events are escalated in a simple, standardised process to all senior management through the Group Notifiable Event Process.

Reputational risk

Definition
Reputational risk is defined as the risk of damage to stakeholder trust due to negative consequences arising from internal actions or external events.

Sources of risk
Reputational risks originate from internal actions and external events. The three primary drivers of reputational risk have been identified as: failure in internal execution; a conflict between the Group's values and the public agenda; and contagion (when the Group's reputation is damaged by failures in the wider financial sector).

Key developments in 2020
- Reputational risks arising from COVID-19 remained a key focus from Q1 onwards.
- A review of the reputational risk framework and policy began in 2020. This was required to reflect the purpose, capture a more complete view of reputation at a strategic level and align with more progressive industry leaders.
- The correlation between reputational risk and climate change issues remained a significant area of focus, supported by work to enhance the consideration of such issues within the reputational risk framework.

Reputational risk continued

Governance
A reputational risk policy supports reputational risk management across NatWest Group. The NatWest Group's Reputational Risk Committee – which has delegated authority from the NatWest Group Executive Risk Committee – opines on cases, issues, sectors and themes that represent a material reputational risk. The NatWest Group Board Risk Committee oversees the identification and reporting of reputational risk. The NatWest Group Sustainable Banking Committee has a specific focus on environmental, social and ethical issues.

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

Standards of conduct are in place across the Group requiring strict adherence to policies, procedures and ways of working to ensure business is transacted in a way that meets – or exceeds – stakeholder expectations.

Monitoring and measurement
Relevant internal and external factors are monitored through regular reporting to the Reputational Risk Committee and escalated, where appropriate, to NatWest Group's Reputational Risk Committee, Board Risk Committee or Sustainable Banking Committee.

Mitigation
Reputational risk is mitigated through the policy and governance framework, with ongoing staff training to ensure early identification, assessment and escalation of material issues. External events that could cause reputational damage are identified and mitigated through the Group's top and emerging risks process. The most material reputational threats continued to originate from historical and more recent conduct issues. NatWest Group has in recent years been the subject of investigations and reviews by a number of regulators and governmental authorities, some of which have resulted in past fines, settlements and public censure. Refer to the Litigation and regulatory matters section of note 27 to the NatWest Group consolidated financial statements for details of material matters currently impacting NatWest Group.

Model risk

The Group uses a variety of models in the course of its business activities. To mitigate the risk that decisions are made based on model results that are incorrect, misinterpreted, used inappropriately or based on an outdated model, independent validation and regular reviews are carried out. Oversight is provided by Model Risk Officers and by a NatWest Group model risk governance committee in accordance with relevant policies and procedures.

REPORT OF THE DIRECTORS

The directors present their report together with the audited accounts for the year ended 31 December 2020. It should be read in conjunction with the Strategic report.

Directors and secretary

The names of the current members of the Board of Directors are shown on page 9.

From 1 January 2020 to date, changes that have taken place are shown under 'Appointments and Resignations' on page 9.

Share capital

Analysis of share capital and paid-in equity can be found in notes 17 and 18 respectively to the financial statements.

Dividends

No interim dividend was paid during the year (2019 - £215 million).

The Bank declared coupon payments of £12 million during the year (2019 - £13 million) on Additional Tier 1 notes.

During the year, the Bank received a dividend of £25 million from Coutts Finance Co (2019 - £35 million). No dividend was received from AMH (2019 - £24 million).

The directors do not recommend the payment of a final dividend (2019 - nil).

Going concern

The Group business activities and financial position, together with the factors likely to affect its future development, performance and position are set out in the Strategic report on pages 1 to 8.

Having reviewed the content of these and the Bank forecasts, projections and other relevant evidence, the directors have a reasonable expectation that the Bank will continue in operational existence for a period of not less than twelve months. Accordingly, the financial statements of the Bank have been prepared on a going concern basis.

Governance

Our Board

The Board has seven directors comprising the Independent Non-Executive Chair, two Executive Directors, one Non-Independent Non-Executive Director and three Independent Non-Executive Directors. Director biographies can be found at www.coutts.com.

The Board is collectively responsible for the long-term success of the Bank; approving the strategic priorities and delivering sustainable value to its shareholder. It monitors and maintains the consistency of the Bank's activities within the strategic direction of NatWest Group. It reviews and approves risk appetite for strategic and material risks in accordance with NatWest Group Risk Appetite Framework, and it monitors performance against risk appetite for the Bank. It approves the Bank's key financial objectives and keeps the capital and liquidity positions of the Bank under review. The Board is also responsible for purpose and culture, which underpins all of the Bank's activities and its long-term sustainability.

In order to extend its effective oversight and leadership, the Board has an Audit Committee, Risk Committee, Nominations Committee and Performance and Remuneration Committee.

There is regular reporting to the Board on risk culture which allows the Board to have appropriate oversight of risk culture matters.

Audit Committee

The Committee is responsible for discharging the Board's responsibilities for monitoring the quality of the financial statements. It reviews the accounting policies, financial reporting and relevant compliance practices of the Bank. It also reviews the Bank's systems and standards of internal controls and monitors the Bank's processes for internal and external audit.

Risk Committee

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

Performance and Remuneration Committee

The Committee is responsible for overseeing the implementation within the Bank of NatWest Group's remuneration policy, and of performance and remuneration arrangements.

Nominations Committee

The Committee is responsible for assisting the Board in the formal selection and appointment of directors. It reviews the structure, size and composition of the Board, and the membership and chairmanship of Board committees.

Executive Committee

The Board is supported by the Executive Committee comprising the executive directors and other senior executives. It supports the Chief Executive Officer (CEO) in managing the Bank's businesses and reviewing relevant items before consideration by the Board. It is responsible for developing and delivering the Bank's strategy and culture and it monitors and manages financial performance, capital allocation, risk strategy and policy, risk management, operational issues and client issues for the Bank.

Directors' indemnities

In terms of Section 236 of the Companies Act 2006, all directors listed on page 9 have been granted Qualifying Third Party Indemnity Provisions by NatWest Group.

The Wates Corporate Governance Principles

The Companies (Miscellaneous Reporting) Regulations 2018 introduced new statutory reporting requirements for financial years beginning on or after 1 January 2019. As a result of these new requirements, the directors of the Bank are required to provide a statement in the Report of the directors stating which corporate governance code the Bank followed during the year, how it applied the code and any part of the code it did not follow.

For the financial year ended 31 December 2020 the Bank has chosen to report against the Wates Corporate Governance Principles for Large Private Companies, published by the FRC in December 2018 and available on the FRC website (the Wates Principles). The disclosures below explain how the Bank has applied the Wates Principles in the context of its corporate governance arrangements.

1. Purpose and Leadership

Aligned to NatWest Group, the Bank's purpose is to champion potential, helping people, families and businesses to thrive. Further information on NatWest Group's purpose can be found in the 2020 Annual Report and Accounts of NatWest Group plc.

The purpose and strategy for the NatWest Group is approved by the NatWest Group Board and cascaded to subsidiaries. The Board of the Bank approves and monitors the purpose and strategic direction of the Bank within the parameters set by the NatWest Group.

The Bank's vision is to be the best Private Bank for the UK, measured through client satisfaction, colleague engagement and financial returns. The Board oversees the execution of strategy and holds management to account for its delivery. This is done through a mix of reporting, Board and other meetings and Board strategy sessions.

Building a healthy culture that embodies Our Values is also a core priority for the Bank as well as the NatWest Group more generally. Our Values, which guide the way NatWest Group identifies the right people to serve clients well, and how to manage, engage and reward colleagues, are at the heart of Our Code (the NatWest Group-wide Code of Conduct).

There is regular reporting to the Board on culture which allows the Board to have appropriate oversight of culture matters. This includes 6-monthly reviews of 'Our View' colleague survey and culture measurement reports, as well as of the Bank's risk culture. Additional extensive engagement with colleagues was also undertaken, and support provided, in response to the COVID-19 pandemic, as detailed in the Strategic report. The Board also considers the overall alignment of purpose and strategy with culture and values.

2. Board Composition

Details on the Board and its Committees are presented in the section Governance above (see page 46).

The Board's Nominations Committee regularly reviews the structure, size and composition of the Board, and ensures there is an appropriate mix of skills, knowledge, experience and diversity, as well as independence. The Nominations Committee further supports the Board in succession planning.

Board diversity is supported by a Boardroom Inclusion Policy, which includes gender and ethnicity diversity targets. The policy sets out the aspiration to meet the targets set by the Hampton-Alexander Report on "FTSE100 Women Leaders" (33% female balance) and the Parker Report "Beyond 1 by '21" (at least one director from an ethnic minority background to be included on the list of candidates by 2020/21). Changes in Board composition in 2020 resulted in the Board slipping below the gender target, but it remains focused on developing its diversity, both across gender and ethnic diversity, and has factored these considerations into its current succession planning activities.

The size of the Board is considered appropriate, taking into account the size and scale of the Bank's business.
The independent non-executive directors combine broad business and commercial experience with independent and objective judgement and provide independent challenge to the executive directors and the leadership team. The balance between independent non-executive and executive directors enables the Board to provide clear and effective leadership across the Bank's business activities. The role of the Chair is to lead the Board and ensure its overall effectiveness and is distinct and separate from that of the CEO, who manages the business day-to-day.

A review of the effectiveness of the Board is conducted at least annually. The 2020 evaluation was facilitated by the Company Secretary in December 2020, with conclusions finalised the following month. The evaluation examined a number of areas, including the Board's response to COVID-19; its focus on purpose, strategy and stakeholders; the Board's culture, dynamics and operation; and relationship with the NatWest Group. Positive feedback was given across all these areas, and the evaluation concluded that the Board had operated effectively throughout 2020. A number of recommendations were also agreed for the Board to focus on during 2021.

Non-executive directors participate in scheduled Board training sessions and other external sessions, as required. An active Board 'teach-in' training programme was maintained through 2020, with a particular focus on climate change training. Other topics included NatWest Group's Enterprise Wide Risk Framework and Risk Appetite Framework, the Bank's digital architecture and asset management developments. Directors also request individual in-depth briefings from time to time on areas of particular interest and would ordinarily also undertake visits to regional offices – albeit none were undertaken in 2020 on account of the pandemic. An induction programme is provided for all new directors, which is tailored to their specific experience and knowledge.

3. Director Responsibilities

All directors receive guidance on their statutory duties under the Companies Act 2006 and are supported in the discharge of their duties by the Company Secretary.

NatWest Group has a Corporate Governance Framework, including a Corporate Governance Policy, which sets out the key aspects of the governance framework as they relate to its key subsidiaries. The Corporate Governance Policy provides high-level guidance to the Board on how the Bank should be managed in line with NatWest Group policy and best practice. The Board and its Committees have Terms of Reference which clearly map out their respective authority, responsibilities and accountabilities. Each director has a role profile which clearly articulates their responsibilities and accountabilities, and any additional regulatory responsibilities are set out in their Statement of Responsibilities, as provided for under the UK's Senior Managers Regime. The Board holds regular quarterly meetings, a number of strategy sessions, and other meetings as required. The number and frequency of ad-hoc Board meetings increased significantly from March 2020, for a period of several months, as part of the initial response to the COVID-19 pandemic.

Directors' conflicts of interest are managed in accordance with conflicts of interest guidance. The Bank maintains a register of directors' interests and appointments, and this is presented at each quarterly Board meeting for review.

The Chair, CEO and Company Secretary are responsible for the quality and integrity of information provided to directors. The Board receives regular information on key aspects of the business, including monthly reports from the CEO, in addition to reporting provided to the quarterly Board meetings.

Extensive internal processes are in place to ensure that the quality and integrity of information provided to the Board is reliable and able to support effective decision making. This is supported by assurance undertaken by second and third lines of defence teams, who respectively provide quarterly Risk and Internal Audit opinions to the quarterly Board Risk and Audit Committees.

REPORT OF THE DIRECTORS

4. Opportunity and Risk

The role of the Board is to promote the long-term, sustainable success of the Bank, which already has a heritage of over 300 years. Opportunities are primarily identified through regular Board reviews of the different parts of the Bank's business and an annual Board strategy session, drawing on client and external market insights, and are framed within the overall strategy of the NatWest Group.

The Board reviews and approves risk appetite for strategic and material risks in accordance with the NatWest Group Risk Appetite Framework, monitors performance against risk appetite for the Bank, considers any material risks and approves, as appropriate, recommended actions escalated by the Coutt's Board Risk Committee.

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

The Bank complies with NatWest Group's risk appetite framework, which is approved annually by the NatWest Group plc Board, in line with NatWest Group's risk appetite statements, frameworks and policies. NatWest Group risk appetite is set in line with overall strategy.

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

During 2020, a number of enhancements to the risk management framework were developed. The increasing significance of climate risk was considered as part of these developments and will be fully integrated as part of the implementation of the enhanced framework in 2021.

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

Further information on the Bank's risk management framework including risk culture, risk governance, risk appetite, risk controls and limits, and risk identification and measurement can be found in the Risk and Capital management section of this report (pages 10 to 45).

5. Remuneration

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

The Bank has a Performance & Remuneration Committee (RemCo) with non-executive directors as members. In addition to reviewing remuneration for executives of the Bank, the RemCo considers reports on the wider workforce including annual pay outcomes and diversity information. The RemCo helps to ensure that the remuneration policies, procedures and practices being applied are appropriate at the Bank level.

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

The NatWest Group is committed to providing a fair wage for the role performed. The Bank is a fully accredited Living Wage Employer with rates of pay that continue to exceed the Living Wage Foundation Benchmarks.

6. Stakeholder Relationships and Engagement

The Bank is committed to engaging with its stakeholders and to bringing their voice into key decisions, as well as managing the wider social, environmental and economic impacts of its operations, as a cornerstone of building a sustainable business.

The Board recognises the importance of engaging with stakeholders and discussions at Board meetings are focused around the impact that the Bank's activities may have on key stakeholder groups. For further details on the Board's engagement with colleagues, clients, suppliers and others, and how these stakeholder interests have been taken into account, see pages 4 to 6 of the Strategic report, which includes a section 172(1) statement.

Post balance sheet events

Settlement of a litigation and conduct matter after the balance sheet date has been deemed non material by management and not adjusted. On 26 February 2021 the Group issued debt securities of €290m at EURIBOR +0.949% per annum. There have been no other significant events between the year end and the date of approval of the financial statements which would require a change to, or additional disclosure or amendment in, the financial statements.

Political donations

During 2020, no political donations were made in the UK or EU, nor any political expenditure incurred in the UK or EU.

Directors' disclosure to auditor

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

- so far as the director is aware, there is no relevant audit information of which the Group and the Bank's auditor is unaware; and
- the directors have taken all steps they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the Group and the Bank's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

Auditor

Ernst & Young LLP has expressed its willingness to continue in office as auditor.

A resolution to re-appoint Ernst & Young LLP as the Group's auditor will be proposed at the forthcoming Annual General Meeting.

By order of the Board: Waldegrave of North Hill
Waldegrave of North Hill (Mar 18, 2021 14:25 GMT)

The Rt Hon Lord Waldegrave of North Hill
Chair

Date: Mar 18, 2021

Coutts & Company is registered in England and Wales No. 00036695

STATEMENT OF DIRECTORS' RESPONSIBILITIES

This statement should be read in conjunction with the responsibilities of the auditor set out in their report on page 55.

The directors are responsible for the preparation of the Annual Report and Accounts. The directors are required by the Companies Act 2006 to prepare company accounts for each financial year in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006. They are responsible for preparing accounts that present fairly the financial position, financial performance and cash flows of the Group and the Bank. In preparing those accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts; and
- make an assessment of the Group and the Bank's ability to continue as a going concern.

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

The directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with IFRS, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and the Bank; and
- the Strategic report (incorporating the Business review) and Report of the directors includes a fair review of the development and performance of the business and the position of the Group and the Bank.

By order of the Board:

Waldegrave of North Hill
Waldegrave of North Hill (Mar 18, 2021 14:25 GMT)

The Rt Hon Lord Waldegrave of North Hill
Chair

Date: 18th March 2021

Board of Directors

Chair, Non-Executive Director
The Rt Hon Lord Waldegrave of North Hill

Executive Directors
Peter Gordon Flavel
Andrew Richard Kyle

Non-Executive Directors
Francesca Barnes
Mark Joseph Lund
Linda Hamilton Urquhart OBE
Matthew Edward James Waymark

INDEPENDENT AUDITOR'S REPORT TO THE MEMBER OF COUTTS & COMPANY

Opinion

In our opinion:

- the financial statement of Coutts & Company (the 'Bank') and its subsidiaries (together, the 'Group') give a true and fair view of the state of the Group's and of the Bank's affairs as at 31 December 2020 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006;
- the Bank's financial statements have been properly prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006 as applied in accordance with section 408 of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements of the Bank and the Group for the year ended 31 December 2020 which comprise:

Group	Bank
• Consolidated balance sheet as at 31 December 2020; • Consolidated statement of comprehensive income for the year then ended; • Consolidated statement of changes in equity for the year then ended; • Consolidated cash flow statement for the year then ended; • Related notes 1 to 25 to the financial statements; • Accounting Policies on pages 61 to 65 • Information included in the Risk and capital management section identified as 'audited'	• Balance sheet as at 31 December 2020; • Statement of changes in equity for the year then ended; • Cash flow statement for the year then ended; • Related notes 1 to 25 to the financial statements, as applicable to the Bank; • Accounting Policies on pages 61 to 65, as applicable to the Bank; and • Risk and capital management section identified as 'audited', as applicable to the Bank

The financial reporting framework that has been applied in their preparation is applicable law and International Accounting Standards in conformity with the requirements of the Companies Act 2006 and, as regards to the Bank financial statements, as applied in accordance with section 408 of the Companies Act 2006.

Basis for opinion

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

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

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate. Our evaluation of the directors' assessment of the Group and Bank's ability to continue to adopt the going concern basis of accounting included:

- In conjunction with our walkthrough of the Group's financial close process, we confirmed our understanding of the director's Going Concern assessment process to ensure all key factors were considered in their assessment;
- We evaluated the directors' going concern assessment, which covered a period of 12 months from the date of our audit report, by reviewing their evaluation of long-term business and strategic plans, capital adequacy, liquidity and funding positions. In addition we also assessed these positions considering internal stress tests which included consideration of principal and emerging risks. The Group's risk profile and risk management practices were considered including credit risk, market risk, compliance and conduct risk, and operational risk. We also evaluated the accuracy of the group forecasts and assessed their reasonableness;
- We evaluated the director's assessment by considering the going concern basis for accounting in different scenarios considering the economic impact of COVID-19. We used economic specialists in assessing the macroeconomic assumptions in the forecast through benchmarking to institutional forecasts, HM Treasury consensus and peer comparative economic forecasts;
- We considered the Group's operational resilience and their response to the impact COVID-19 had on its business operations, including the operations of its third-party providers and the dependencies of the Bank to the Natwest Group; and
- We reviewed the Group's going concern disclosures included in the annual report in order to assess that the disclosures were appropriate and in conformity with the reporting standards.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Group and Bank's ability to continue as a going concern for a period of up of 12 months up to 18 March 2022, being not less than twelve months from when the financial statements are authorised for issue.

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

INDEPENDENT AUDITOR'S REPORT TO THE MEMBER OF COUTTS & COMPANY

Overview of our audit approach

Audit scope	• We performed an audit of the complete financial information of the Group
Key audit matters	• Impairment of loans • Provisions for conduct, litigation and regulatory matters • Legal entity recharges, including intercompany balances
Materiality	• Overall Group materiality has been set at £15 million which represents 8% of adjusted profit before tax.

Tailoring the audit scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for the Group. We take into account the size and risk profile of the Bank's subsidiaries and its activities, the organisation of the Group and effectiveness of group wide controls, changes in the business environment and other factors such as recent internal audit results when assessing the level of work to be performed. The audit scope is consistent with prior year.

As a result of the COVID-19 outbreak and resulting lockdown restrictions we have modified our audit strategy to allow for the audit to be performed remotely. This approach was supported through remote user access to the Group's financial systems and the use of EY software collaboration platforms for the secure and timely delivery of requested audit evidence.

Key audit matters

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

Risk	Our response to the risk
Impairment of loans	
At 31 December 2020 the Group reported total gross loans of £16.84 billion (2019: £15.02 billion) and £134 million (2019: £39 million) of expected credit loss provisions. Management's judgements and estimates are especially subjective due to significant uncertainty associated with the assumptions used. Uncertainty associated with COVID-19 and its consequent implications including lockdowns and recovery assumptions as well as government intervention, increased the level of judgement in determining ECL. Assumptions with increased complexity in respect of the timing and measurement of ECL include: • Staging - Allocation of assets to stage 1, 2, or 3 on a timely basis using criteria in accordance with IFRS 9 considering the impact of COVID-19 and related government support measures, such as payment deferrals, on client behaviours and the identification of underlying significant deterioration in credit risk; • Model estimations - Accounting interpretations, modelling assumptions and data used to build and select the most appropriate models that calculate the ECL considering the impact of COVID-19 on model performance, any additional data to be considered in the ECL calculation; • Economic scenarios - Inputs, assumptions and weightings used to estimate the impact of multiple economic scenarios particularly those influenced by COVID-19 and Brexit including any changes to scenarios required through 31 December 2020; • Adjustments - Appropriateness, completeness and valuation of model adjustments including any COVID-19 specific adjustments due to the increased uncertainty and less reliance on modelled outputs which increases the risk of management override; • Individual provisions - Measurement of individual provisions including the assessment of multiple scenarios considering the impact of COVID-19 on exit strategies, collateral valuations and time to collect;	Controls testing: We tested the design and operating effectiveness of controls across the processes relevant to ECL, including the judgements and estimates noted. These controls, among others, included: • the allocation of assets into stages including management's monitoring of stage effectiveness; • recording and approval of payment deferrals and government supported lending such as Corona Business Interruption Loans ('CBILs') and Bounce Back Loans ('BBLs'); • model governance including monitoring, the governance and model validation; data accuracy and completeness; • credit monitoring; • multiple economic scenarios; • individual provisions and • production of journal entries and disclosures. In evaluating the governance process we observed the executive finance and risk committee meetings where the inputs, assumptions and adjustments to the ECL were discussed and approved, among other procedures. We performed an overall assessment of the ECL provision levels by stage to assess if they were reasonable by considering the overall credit quality of the Group's portfolios, risk profile, impact of the COVID-19 including geographic considerations and high risk industries, the impact government support measures, such as payment deferrals, may have had on delaying expected defaults, credit risk management practices and the macroeconomic environment by considering trends in the economy and industries to which the Group is exposed. We also considered the appropriateness of provisions applied to government supported lending such as bounce back loans and CBILs which included assessing the respective eligibility criteria. We performed peer benchmarking where available to assess overall staging and provision coverage levels. We evaluated the criteria used to allocate a financial asset to stage 1, 2 or 3 in accordance with IFRS 9; this included peer benchmarking to assess staging levels. We recalculated the assets in stage 1, 2 and 3 to assess if they were allocated to the appropriate stage and performed sensitivity analysis to assess the impact of different criteria on the ECL. To test credit monitoring which drives the probability of default estimates used in the staging calculation, we recalculated the risk ratings for a sample of performing loans and focused our testing on high risk industries impacted by COVID-19. For commercial exposures, we also assessed the timing of the annual review performed by management to evaluate whether it appropriately considered COVID-19 risk factors by considering independent publicly available information. We involved modelling specialists to assist us to test a sample of ECL models by testing the assumptions, inputs and formulae used. This included a combination of assessing the appropriateness of model design and formulae used, alternative modelling techniques, recalculating the Probability of Default, Loss Given Default and Exposure at Default, and model implementation. We also considered the results of internal model validation results. We also assessed and challenged the appropriateness of the models selected by management and evaluated the justification for their use. To evaluate data quality, we agreed a sample of ECL calculation data points to source systems, including balance sheet data used to run the models and historic loss data to monitor models. We also tested the ECL data points from the calculation engine through to the general ledger and disclosures. We included COVID-19 specific data points in this testing We involved economic specialists to assist us to evaluate the base case and alternative economic scenarios, including evaluating probability weights and comparing these to other scenarios from a variety of external sources. This assessment included the latest developments related to COVID-19 and BREXIT at 31 December 2020, including the announcement of planned vaccines. We assessed whether forecasted macroeconomic variables were complete and appropriate, such as GDP, unemployment rate, interest rates and the House Price Index. With the support of our modelling specialists we evaluated the correlation and translation of the macroeconomic factors to the ECL. We involved valuation specialists to recalculate a sample of individual provisions including the alternative scenarios and evaluating probability weights assigned. The sample was based on a number of factors, including higher risk sectors such as commercial real estate and retail and. We considered the impact that COVID-19 had on collateral valuations and time to collect as well as whether planned exit strategies remained viable. We tested material in-model and post-model adjustments including those which were applied as a result of COVID-19. With our modelling specialists, we assessed the completeness of these adjustments and their appropriateness by considering the data, judgments, methodology, sensitivities, and governance of these adjustments as well as considering model shortcomings.

• Disclosure - The completeness and preparation of disclosures considering the key judgments, sources of data and the design of the disclosures.	We tested the data flows used to populate the disclosures and assessed the adequacy of disclosures for compliance with the accounting standards and regulatory considerations including expectations of COVID-19 specific disclosures.

Key observations communicated to the Audit Committee

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

- Our testing on the IFRS 9 staging criteria identified errors in the data inputs resulting in differences related to the Bank's staging allocation. These disclosure differences remained uncorrected and were considered by management not to be material, including the associated ECL impact. We concurred with management.
- Our testing of the selection of Models, Model estimations, Economic scenarios, Adjustments and Individual provisions did not highlight material differences.

We noted improvements to the governance framework throughout the year to respond to the challenge posed by Covid-19, but noted certain data quality related control deficiencies, some of which were identified in prior periods. We identified and tested compensating controls with no issues noted.

Relevant references in the Annual Report and Accounts

Credit risk section of the Risk and Capital management section
Accounting policies
Note 8 on the financial statements

Risk	Our response to the risk
Provisions for conduct, litigation and regulatory matters	
The continued litigious environment and the heightened regulatory scrutiny gives rise to a high level of judgement in determining appropriate provisions and disclosures. At the year-end, the Group has reported £13 million (2019: £50 million) of provisions for liabilities and charges for conduct and litigation claims as detailed in Note 15 of the financial statements on page 82. Management judgement is needed to determine whether an obligation exists and the extent to which a provision should be recorded at 31 December 2020 in accordance with the accounting criteria set under IAS 37. This is therefore subject to the risk of management override. The most significant areas of judgement, therefore, include the determination of the following: • It is probable that an economic outflow such as a payment will occur; • The amount of the payment (or other economic outflow) can be estimated reliably including the appropriateness of the assumptions and judgements to determine this amount; • Reversal assessment in case it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and • The disclosures are adequate and in accordance with accounting standards.	We tested the design and operating effectiveness of controls over the identification, estimation, monitoring and disclosure of provisions related to legal and conduct matters considering the potential for management override of controls. The controls tested, among others, included those to identify and monitor claims, determine when a provision is required, when a provision release is appropriate and to ensure the completeness and accuracy of data used to estimate provisions. We examined the relevant regulatory information and legal correspondence to assess developments in certain cases. We also considered regulatory developments to identify actual or possible noncompliance with laws and regulations that might have a material effect on the financial statements. For cases which were settled during the period, we compared the actual outflows with the provision that had been recorded, considered whether further risk existed, and evaluated the level of disclosures provided. For significant legal matters, we received confirmations from the Bank's external legal counsel for significant matters to evaluate the existence of the obligation and management's estimate of the outflow at year-end. We also conducted inquiries with internal legal counsel over the existence of the legal obligations and related provision. With the involvement of our conduct specialists, we held discussion with internal counsel, reviewed and assessed the completeness of provisions included in the balance sheet at year end. We evaluated the disclosures provided on conduct, litigation, regulatory, provisions to assess whether they complied with accounting standards.

Key observations communicated to the Audit Committee

- We are satisfied that provisions for conduct, litigation and regulatory matters, client remediation and claims are reasonable and recognised in accordance with IFRS and appropriately disclosed in the financial statements.

Relevant references in the Annual Report and Accounts
Accounting policies Note 15 of the financial statements

Risk	Our response to the risk
Legal entity recharges, including intercompany balances	
The majority of Natwest Group-wide costs are paid centrally by the ultimate holding company, and recharged to other Natwest Group companies, including the Bank. Natwest Group recharges currently constitute the majority of the Bank's total cost base (2020: £212 million, 2019: £174 million). These costs are recharged in line with Inter-group Agreements ("IGA") and transfer pricing policy. Accounting and reporting risk arising includes: • recharged costs may not be calculated in accordance with the revised Natwest Group IGA and transfer pricing methodology; • risk of errors in the computation of recharges; and • inappropriate or inadequate reconciliation of recharges and intercompany transactions and resultant balances among entities of the Natwest Group.	We tested the design and operating effectiveness of the Group's key controls, including the review of the service catalogue, the allocation metrics and net recharge balance by management as well as the application controls to calculate the allocation of costs and the mark-ups applied, over the completeness and accuracy of cost recharges. This included understanding Natwest Group's recharging processes and controls, including how management ensures the assessment is complete. The transfer pricing methodology was reviewed by our tax specialists. We tested the intercompany reconciliation process at year-end and confirmed the year-end intra-group balances. We also tested a sample of costs recharged and agreed them to supporting documentation.

Key observations communicated to the Audit Committee
We are satisfied that the cost recharged in the year were reasonable. We highlighted to the Audit Committee control deficiencies identified within the NW Group's recharging process and we performed additional testing in response to those deficiencies.

Relevant references in the Annual Report and Accounts
Accounting policies Note 3 of the financial statements

Our application of materiality

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

Materiality

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

We determined materiality for the Group to be £15 million (2019: £24 million), which is 8% of profit before tax of the Group adjusted for certain loan impairment charges arising from COVID-19, conduct releases, strategic costs and certain non-recurring transactions. We believe that this measure is consistent with the basis from the prior year and is consistent with the wider industry and is the standard for regulated entities and we believe it reflects the most useful measure for users of the financial statements. The significant decrease in materiality is driven by a lower profit before tax in 2020.

Performance materiality

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

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality was 75% of our planning materiality, namely £11 million (2019: £18 million). We have set performance materiality at this percentage (which is at the highest end of the range of our audit methodology) based on various considerations including the past history of misstatements, the effectiveness of the control environment and other factors affecting the entity and its financial reporting. The reduction is driven by the decrease of the above-mentioned materiality.

Reporting threshold

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

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.7 million (2019: £1.2 million), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

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

Other information

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

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

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

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006

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

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the Directors' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the directors' report.

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

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 49, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

Auditor's responsibilities for the audit of the financial statements

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

INDEPENDENT AUDITOR'S REPORT TO THE MEMBER OF COUTTS & COMPANY

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

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

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Group and determined that the most significant are the regulations, licence conditions and supervisory requirements of the Prudential Regulation Authority (PRA) and the FCA; Tax Legislation as governed by HM revenue and Customs; and Companies Act 2006.
- We understood how the Group is complying with those frameworks by making inquiries of management, internal audit and those responsible for legal and compliance matters. We also reviewed correspondence between the Group and regulatory bodies; reviewed minutes of the Board and Risk Committees; and gained an understanding of the Group's governance framework.
- We assessed the susceptibility of the Group's financial statements to material misstatement, including how fraud might occur by considering the controls established to address risks identified to prevent or detect fraud. We also identified the risks of fraud in our key audit matters as described above and identified areas that we considered when performing our fraud procedures, such as cybersecurity, the impact of remote working, implementation of new government supported lending products, and the appropriateness of sources used when performing confirmation testing on accounts such as cash, loans and securities.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved inquiries of legal counsel, executive management, and internal audit. We also tested controls and performed procedures to respond to the fraud risks as identified in our key audit matters.
- The Group operates in the banking industry which is a highly regulated environment. As such, the Senior Statutory Auditor considered the experience and expertise of the engagement team to ensure that the team had the appropriate competence and capabilities, involving specialists where appropriate.

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

Other matters we are required to address

- We were appointed by the Group at its annual general meeting on 4 May 2016 to audit the financial statements of the Group for the period ending 31 December 2016 and subsequent financial periods.
- The period of total uninterrupted engagement including previous renewals and reappointments is 5 years, covering periods from our appointment through 31 December 2020.
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Bank and we remain independent of the group and the parent company in conducting the audit.
- The audit opinion is consistent with the additional report to the Audit Committee.

Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Ernst and Young LLP
Ernst and Young LLP (Mar 18, 2021 21:31 GMT)

Michael-John Albert (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London
Date: 18 March 2021

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2020

	Note	2020 £m	2019 £m
Interest receivable		520	607
Interest payable		(101)	(157)
Net interest income	1	419	450
Fees and commissions receivable		223	230
Fees and commissions payable		(25)	(14)
Other operating income		17	24
Non-interest income	2	215	240
Total income		634	690
Staff costs		(149)	(142)
Premises and equipment		(20)	(13)
Depreciation & amortisation		(17)	(12)
Other administrative expenses		(212)	(230)
Impairment of other intangible assets		(1)	-
Operating expenses	3	(399)	(397)
Profit before impairment (losses)/releases		235	293
Impairment (losses)/releases on loans and advances	8	(107)	7
Impairment losses on other assets		(1)	-
Operating profit before tax		127	300
Tax charge	6	(33)	(80)
Profit and total comprehensive income for the year		94	220

The accompanying notes, on pages 66 to 88, and the accounting policies, on pages 61 to 65, form an integral part of these financial statements.

BALANCE SHEETS AS AT 31 DECEMBER 2020

		Group		Bank	
		2020	2019	2020	2019
	Note	£m	£m	£m	£m
Assets					
Cash and balances at central banks	7	3	3	3	3
Loans to banks - amortised cost	7	333	143	312	124
Loans to customers - amortised cost	7	16,317	14,792	15,887	14,172
Amount due from holding companies and fellow subsidiaries	7	21,343	18,690	21,714	19,249
Derivatives	7, 9	29	22	29	22
Investment in Group undertakings	7, 10	-	-	110	110
Property, plant and equipment	7, 11	298	294	298	294
Other assets	7, 13	111	93	93	76
Total assets		38,434	34,037	38,446	34,050
Liabilities					
Bank deposits	7	4	12	4	12
Customer deposits	7	30,142	26,390	30,142	26,390
Amount due to holding companies and fellow subsidiaries	7	6,113	5,463	6,111	5,463
Derivatives	7, 9	28	20	28	20
Other financial liabilities	7, 14	310	310	310	310
Other liabilities	7, 15	137	224	130	215
Subordinated liabilities	7, 16	265	265	265	265
Total liabilities		36,999	32,684	36,990	32,675
Owner's equity		1,435	1,353	1,456	1,375
Total equity		1,435	1,353	1,456	1,375
Total liabilities and equity		38,434	34,037	38,446	34,050

Owner's equity of the Bank as at 31 December 2020 includes the profit for the year then ended of £93 million (2019 - £247 million).

As permitted by section 408(3) of the Companies Act 2006, no income statement for the Bank has been presented as a primary financial statement.

The accompanying notes, on pages 66 to 88, and the accounting policies, on pages 61 to 65, form an integral part of these financial statements.

The accounts were approved by the Board of Directors on 17th March 2021 and signed on its behalf by:

Andrew Kyle
Andrew Kyle (Mar 18, 2021 14:50 GMT)

Andrew Richard Kyle
Executive Director

Waldegrave of North Hill
Waldegrave of North Hill (Mar 18, 2021 14:25 GMT)

The Rt Hon Lord Waldegrave of North Hill
Chair

STATEMENTS OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2020

		Group		Bank	
		2020	2019	2020	2019
	Note	£m	£m	£m	£m
Called-up share capital at 1 January and 31 December	17	41	41	41	41
Paid-in equity at 1 January and 31 December	18	200	200	200	200
Retained earnings at 1 January		773	782	752	734
Implementation of IFRS 16 on 1 January 2019		-	(1)	-	(1)
Profit and total comprehensive income for the year		94	220	93	247
Paid-in equity coupon payments		(12)	(13)	(12)	(13)
Dividends paid		-	(215)	-	(215)
At 31 December		855	773	833	752
Capital contribution at 1 January and 31 December	21	339	339	382	382
Owner's equity at 31 December		1,435	1,353	1,456	1,375

The accompanying notes, on pages 66 to 88, and the accounting policies, on pages 61 to 65, form an integral part of these financial statements.

CASH FLOW STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2020

		Group		Bank	
		2020	2019	2020	2019
	Note	£m	£m	£m	£m
Cash flows from operating activities					
Operating profit before tax		127	300	119	319
Adjustments for:					
Depreciation, amortisation and impairment of other assets		25	17	25	17
Impairment losses/(releases) on loans to customers		107	(7)	107	(7)
Other non-cash items		-	(1)	-	(3)
Provision (release)/charges		(28)	11	(28)	11
Elimination of foreign exchange differences		57	82	57	82
Dividends receivable from group undertakings		-	-	(25)	(59)
Net cash flows from trading activities		288	402	255	360
Increase in derivative assets		(7)	(2)	(7)	(2)
Increase in net loans to banks		(11)	(22)	(11)	(24)
Increase in net loans to customers		(1,632)	(1,219)	(1,822)	(1,578)
Decrease/(increase) in amounts due from holding companies and fellow subsidiaries		159	(42)	315	294
Increase in other assets		(18)	(55)	(17)	(55)
(Decrease)/increase in bank deposits		(8)	7	(8)	7
Increase/(decrease) in customer deposits		3,752	(137)	3,752	(137)
Increase/(decrease) in amounts due to holding companies and fellow subsidiaries		650	(481)	648	(481)
Increase in derivative liabilities		8	-	8	-
Increase in other liabilities		5	33	3	45
Changes in operating assets and liabilities		2,898	(1,918)	2,861	(1,931)
Income taxes paid		(97)	(6)	(85)	(1)
Net cash flows from operating activities(1)		3,089	(1,522)	3,031	(1,572)
Cash flows from investing activities					
Purchase of property, plant and equipment	11	(10)	(6)	(10)	(6)
Sale of property, plant & equipment	11	-	1	-	1
Purchase of intangible assets	12	(20)	(12)	(20)	(12)
Sale of intangible assets	12	1	-	-	-
Dividends received from group undertakings		-	-	25	59
Net cash flows from investing activities		(29)	(17)	(5)	42
Cash flows from financing activities					
Paid-in equity coupon payments		(12)	(13)	(12)	(13)
Issue of debt securities	14	-	260	-	260
Dividends paid		-	(215)	-	(215)
Net cash flows from financing activities		(12)	32	(12)	32
Effects of exchange rate changes on cash & cash equivalents		(57)	(82)	(57)	(82)
Net increase/ (decrease) in cash and cash equivalents		2,991	(1,589)	2,957	(1,580)
Cash and cash equivalents 1 January	22	9,232	10,821	9,203	10,783
Cash and cash equivalents 31 December		12,223	9,232	12,160	9,203

The accompanying notes, on pages 66 to 88, and the accounting policies, on pages 61 to 65, form an integral part of these financial statements.

Note:
(1) Includes interest received for Group of £535 million (2019 - £603 million) and interest paid of £107 million (2019 - £159 million), and for Bank interest received of £523 million (2019 - £593 million) and interest paid of £107 million (2019 - £159 million).

ACCOUNTING POLICIES

1. Presentation of accounts

The accounts, set out on pages 57 to 91, including these accounting policies on pages 61 to 65 and the audited sections of the Risk and Capital Management on pages 10 to 45, are prepared on a going concern basis (see the Report of the directors, page 46) and in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006. The significant accounting policies and related judgements are set out below.

The Bank, a private unlimited company, is incorporated in the UK and registered in England and Wales. The Group and Bank accounts are presented in accordance with the Companies Act 2006.

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

With the exception of investment property and certain financial instruments as described in accounting policies 9, 13, 15 and 16, the accounts are prepared on an historical cost basis.

The Group improved presentation of disclosures and comparative figures have been adjusted to be consistent with new preparation.

Accounting changes effective 1 January 2020

Amendments to IFRS 3 Business Combinations (IFRS 3) - Changes to the definition of a business

The IASB amended IFRS 3 to provide additional guidance on the definition of a business. The amendment aims to help entities when determining whether a transaction should be accounted for as a business combination or as an asset acquisition. The amendments are in line with current accounting policy and therefore did not affect the accounts.

Definition of material – Amendments to IAS 1 – Presentation of Financial Statements (IAS 1) and IAS 8 - Accounting Policies, Changes in Accounting Estimates and Errors (IAS 8)

The IASB clarified the definition of 'material' and aligned the definition of material used in the Conceptual Framework and in other IFRS standards. The amendments clarify that materiality will depend on the nature or magnitude of information. Under the amended definition of materiality, an entity will need to assess whether the information, either individually or in combination with other information, is material in the context of the accounts. A misstatement of information is material if it could reasonably be expected to influence decisions made by the primary users. NatWest Group's definition and application of materiality is in line with the definition in the amendments.

Interest Rate Benchmark Reform (IBOR reform) Phase 1 amendments to IFRS 9 and IAS 39

The IASB issued 'Interest Rate Benchmark Reform (Amendments to IFRS 9, IAS 39 and IFRS 7)' as a first reaction to the potential effects the IBOR reform could have on financial reporting. The amendments focused on hedge accounting and allow hedge relationships affected by the IBOR reform to be accounted for as continuing hedges. Amendments are effective for annual reporting periods beginning on or after 1 January 2020 with early application permitted.

Interest Rate Benchmark Reform (IBOR reform) Phase 2 amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16

Phase 2 of the IASB's IBOR project addresses the wider Accounting issues arising from the IBOR reform. This was published in August 2020. The amendments are effective for annual reporting periods beginning on or after 1 January 2021 with early application permitted. As NatWest Group early adopted these amendments for the annual period ending on 31 December 2020, which have been endorsed by the EU and UK in January 2021, the Group has applied international accounting standards which have been adopted for use within the UK. The Group's IBOR transition program remains on track and key milestones have been met. Conversion from rates subject to reform to alternative RFRs is expected to increase as RFR-based products become more widely available and key market-driven conversion events occur.

2. Basis of consolidation

The consolidated accounts incorporate the financial statements of the Bank and entities that are controlled by the Group (its subsidiaries). Control is assessed by reference to our ability to enforce our will on the other entity, typically through voting rights.

On acquisition of a subsidiary from outside of NatWest Group, its identifiable assets, liabilities and contingent liabilities are included in the consolidated accounts at their fair value. A subsidiary is included in the consolidated financial statements from the date it is controlled by the Group until the date the Group ceases to control it through a sale or a significant change in circumstances.

On the acquisition of a business from a NatWest Group company, the assets, liabilities and IFRS reserves are recognised at their inherited values taken from the consolidated accounts of NatWest Group and include the accounting history since initial recognition. The acquirer recognises in the capital contribution reserve any difference between the consideration and the net items recognised at inherited values.

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

3. Revenue recognition

Interest income or expense relates to financial instruments measured at amortised cost using the effective interest rate method, the effective part of any related accounting hedging instruments, and finance lease income recognised at a constant periodic rate of return before tax on the net investment on the lease. Negative effective interest accruing to financial assets is presented in interest payable.

Other interest relating to financial instruments measured at fair value is recognised as part of movement in fair value.

Commitment and utilisation fees are determined as a percentage of the outstanding facility. The fees are deferred and included in the effective interest rate on the advance.

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

4. Colleague benefits

Short-term colleague benefits, such as salaries, paid absences, and other benefits are accounted for on an accruals basis over the period in which the colleagues provide the related services. Colleagues may receive variable compensation satisfied by cash, by debt instruments issued by NatWest Group or NatWest Group plc shares.

Variable compensation that is settled in cash or debt instruments is charged to the statement of comprehensive income over the period from the start of the year to which the variable compensation relates to the expected settlement date taking account of forfeiture and claw back criteria.

NatWest Group provides post-retirement benefits in the form of pensions and healthcare plans to eligible colleagues on behalf of the Group.

There is no contractual agreement or policy on the way that the cost of NWB defined benefit pension schemes and healthcare plans are allocated to the Group. It therefore accounts for the charges it incurs as payments to a defined contribution scheme.

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

5. Intangible assets and goodwill

Intangible assets acquired by the Group, excluding goodwill, are stated at cost less accumulated amortisation and impairment losses. Amortisation is charged to the statement of comprehensive income over the assets' estimated economic lives.

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

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

Where a subsidiary acquires a business from a NatWest Group company, goodwill is acquired at the value inherited from NatWest Group's accounts.

Direct costs relating to the development of internal-use computer software are capitalised once technical feasibility and economic viability have been established. These costs include payroll, the costs of materials and services, and directly attributable overheads.

Capitalisation of costs ceases when the software is capable of operating as intended. During and after development, accumulated costs are reviewed for impairment against the benefits that the software is expected to generate.

Costs incurred prior to the establishment of technical feasibility and economic viability are expensed as incurred as are all training costs and general overheads.

The costs of licences to use computer software that are expected to generate economic benefits beyond one year are also capitalised.

6. Property, plant and equipment

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

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

The estimated useful lives of the Group's property, plant and equipment are:

Freehold buildings	50 years
Long leasehold property (leases with more than 50 years to run)	50 years
Short leaseholds	unexpired period of lease
Property adaptation costs	10 to 15 years
Computer equipment	up to 5 years
Other equipment	4 to 15 years
Right of use	unexpired period of lease

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

7. Impairment of non-financial assets

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

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

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

8. Investment property

Investment property comprises leasehold properties that are held to earn rentals or for capital appreciation or both. Investment property is not depreciated but is stated at fair value. Fair value is based on the current prices for similar properties in the same location and condition. Further details are included in note 11.

Any gain or loss arising from a change in fair value is recognised in profit or loss. Rental income from investment property is recognised on a straight-line basis over the term of the lease in Other operating income. Lease incentives granted are recognised as an integral part of the total rental income.

9. Foreign currencies

The Group's consolidated financial statements are presented in sterling, which is the functional currency of the Group and the Bank. Transactions in foreign currencies are recorded in the functional currency at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the relevant functional currency at the foreign exchange rates ruling at the balance sheet date. Foreign exchange differences arising on the settlement of foreign currency transactions and from the translation of monetary assets and liabilities are reported in income from trading activities.

Non-monetary items denominated in foreign currencies are translated into the relevant functional currency at the foreign exchange rates ruling at the dates the values are determined. Translation differences arising on non-monetary items are recognised in profit or loss.

10. Leases

As lessor

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

Loans to customers include finance lease receivables measured at the net investment in the lease, comprising the minimum lease payments and any unguaranteed residual value discounted at the interest rate implicit in the lease. Interest receivable includes finance lease income recognised at a constant periodic rate of return before tax on the net investment. Unguaranteed residual values are subject to regular review; if there is a reduction in their value, income allocation is revised and any reduction in respect of amounts accrued is recognised immediately.

Rental income from operating leases is recognised in other operating income on a straight-line basis over the lease term unless another systematic basis better represents the time pattern of the asset's use. Operating lease assets are included within property, plant and equipment and depreciated over their useful lives.

As lessee

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

11. Provisions and contingent liabilities

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

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

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

12. Tax

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

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

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

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

Deferred tax assets and liabilities are offset where the Group has a legally enforceable right to offset and where they relate to income taxes levied by the same taxation authority either on an individual Group company or on Group companies in the same tax group that intend, in future periods, to settle current tax liabilities and assets on a net basis or on a gross basis simultaneously.

Accounting for taxes is judgmental and carries a degree of uncertainty because tax law is subject to interpretation, which might be questioned by the relevant tax authority. The Group recognises the most likely current and deferred tax liability or asset, assessed for uncertainty using consistent judgments and estimates. Current and deferred tax assets are only recognised where their recovery is deemed probable, current and deferred tax liabilities are recognised at the amount that represents the best estimate of the probable outcome having regard to their acceptance by the tax authorities.

13. Financial instruments

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

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

The product classifications apply to financial assets that are either designated as at fair value through profit or loss (DFV), or to equity investments designated as at fair value through other comprehensive income (FVOCI). In all other instances, fair value through profit or loss (MFVTPL) is the default classification and measurement category for financial assets.

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

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

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

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

14. Impairment: expected credit losses

At each balance sheet date each financial asset or portfolio of loans measured at amortised cost or at FVOCI, issued financial guarantee and loan commitment is assessed for impairment. Loss allowances are forward-looking based on 12-month ECL where there has not been a significant increase in credit risk rating, otherwise allowances are based on lifetime expected losses.

ECL are a probability-weighted estimate of credit losses. The probability is determined by the risk of default which is applied to the cash flow estimates. In the absence of a change in credit rating, allowances are recognised when there is reduction in the net present value of expected cash flows. On a SICR, allowances are recognised without a change in the expected cash flows, although typically expected cash flows do also change; and ECL are rebased from 12-month to lifetime expectations.

Judgement is exercised as follows:

- Models – in certain low default portfolios, Basel parameter estimates are also applied for IFRS 9.
- Non-modelled portfolios use a standardised capital requirement under Basel II. Under IFRS 9, they have bespoke treatments for the identification of significant increase in credit risk. Benchmark PDs, EADs and LGDs are reviewed annually for appropriateness. The ECL calculation is based on expected future cash flows, which is typically applied at a portfolio level.
- Multiple economic scenarios (MES) – the central, or base, scenario is most critical to the ECL calculation, independent of the method used to generate a range of alternative outcomes and their probabilities.
- SICR – IFRS 9 requires that at each reporting date, an entity shall assess whether the credit risk on an account has increased significantly since initial recognition. Part of this assessment requires a comparison to be made between the current lifetime PD (i.e. the current PD over the remaining lifetime) with the equivalent lifetime PD as determined at the date of initial recognition.

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

Where, in the course of the orderly realisation of a loan, it is exchanged for equity shares or property, the exchange is accounted for as the sale of the loan and the acquisition of equity securities or investment property. Where the Group's interest in equity shares following the exchange is such that the Group controls an entity, that entity is consolidated.

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

- Retail mortgages – write off usually occurs within five years, or when an account is closed, if earlier.
- Credit cards – the irrecoverable amount is written off after 12 months; three years later any remaining amounts outstanding are written off.
- Overdrafts and other unsecured loans – write off occurs within six years
- Commercial loans – write offs are determined in the light of individual circumstances; the period does not exceed five years.
- Business loans are generally written off within five years.

15. Financial guarantee contracts

Under a financial guarantee contract the Group, in return for a fee, undertakes to meet a client's obligations under the terms of a debt instrument if the client fails to do so. A financial guarantee is recognised as a liability; initially at fair value and, if not designated at FVPL, subsequently at the higher of its initial value less cumulative amortisation and any provision under the contract measured in accordance with accounting policy 14. Amortisation is calculated so as to recognise fees receivable in profit or loss over the period of the guarantee.

16. Derecognition

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

A financial liability is removed from the balance sheet when the obligation is discharged, is cancelled, or expires. Cancellation includes the issuance of a substitute instrument on substantially different terms.

17. Capital Instruments

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

18. Derivatives

Derivative financial instruments are initially recognised, and subsequently measured, at fair value. Derivative fair values are determined from quoted prices in active markets where available. Where there is no active market for an instrument, fair value is derived from prices for the derivative's components using appropriate pricing or valuation models. A derivative embedded in a contract is accounted for as a standalone derivative if its economic characteristics are not closely related to the economic characteristics of the host contract; unless the entire contract is carried at FVPL.

The Bank's client derivatives are economically hedged directly with NWB with no material fair value impact to the profit or loss.

19. Cash and cash equivalents

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

20. Investment in Group undertakings

The Bank's investments in its subsidiaries are stated at cost less any impairment.

Critical accounting policies and key sources of estimation uncertainty

The reported results of the Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its accounts. UK company law and IFRS require the directors, in preparing the Group's accounts, to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent. In the absence of an applicable standard or interpretation, IAS 8 'Accounting Policies, Changes in Accounting Estimates and Errors', requires management to develop and apply an accounting policy that results in relevant and reliable information in the light of the requirements and guidance in IFRS dealing with similar and related issues and the IASB's 'Conceptual Framework for Financial Reporting'. The judgements and assumptions involved in the Group's accounting policies that are considered by the Board to be the most important to the portrayal of its financial condition are discussed below. The use of estimates, assumptions or models that differ from those adopted by the Group would affect its reported results. During 2020, estimation uncertainty has been affected by the COVID-19 pandemic. Consideration of this source of estimation uncertainty has been set out in the notes below (as applicable).

Critical accounting policy	Note
Loan impairment provisions	8
Provisions for liabilities and charges	15

Future accounting developments

International Financial Reporting Standards

COVID-19 amendments on lease modifications – Amendments to IFRS 16 – Leases (IFRS 16)

The IASB published 'amendments to IFRS 16 covering COVID-19-Related Rent Concessions'. These provide lessees with an exemption from assessing whether a COVID-19 related rent concession is a lease modification. The amendment is effective for annual reporting periods beginning on or after 1 June 2020. The effect of the amendment on the Group's accounts is immaterial and will be adopted from 1 January 2021.

Other new standards and amendments that are effective for annual periods beginning after 1 January 2022, with earlier application permitted, are set out below. Effective 1 January 2022

- Property, Plant and Equipment: Proceeds before Intended Use (Amendments to IAS 16).
- Reference to Conceptual Framework (Amendments to IFRS 3).
- Classification of Liabilities as Current or Non-current (Amendments to IAS 1).
- Fees in the "10 per cent" test for Derecognition of Financial Liabilities (Amendments to IFRS 9).

Effective 1 January 2023

- IFRS 17 Insurance Contracts (Amendments to IFRS 17 Insurance Contracts).

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

NOTES TO THE ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2020

1. Net interest income

	2020 £m	2019 £m
Loans to customers - amortised cost	393	413
Loans to banks - amortised cost	127	194
Interest receivable (1)	520	607
Bank deposits	(70)	(65)
Customer deposits	(29)	(91)
Other liabilities (Note 19)	(2)	(1)
Interest payable (2)	(101)	(157)
Net interest income	419	450

Notes:

(1) Includes interest receivable on amount due from holding companies and fellow subsidiaries £127 million (2019 - £194 million)

(2) Includes interest payable on amount due to holding companies and fellow subsidiaries £70 million (2019 - £65 million).

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

2. Non-interest income

	2020 £m	2019 £m
Fees and commission receivable		
Investment management	149	148
Payment services	26	31
Other	26	31
Credit and debit card fees	9	12
Brokerage	6	5
Lending and financing	7	3
	223	230
Fees and commission payable	(25)	(14)
Other operating income		
Cost of economic hedging	22	27
Operating lease and other rental income	2	4
Changes in the fair value of investment properties	(7)	(5)
Other income	-	(2)
	17	24
Non-interest income	215	240

NOTES TO THE ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2020

3. Operating expenses

	2020	2019
	£m	£m
Wages, salaries and other staff costs	110	103
Bonus awards	13	15
Social security costs	14	13
Pension costs	12	11
Staff costs	149	142
Premises and equipment	20	13
Depreciation & amortisation (Note 11 and 12)	17	12
Other administrative expenses(1)	212	230
Administrative expenses	249	255
Impairment of intangible assets	1	
Operating expenses	399	397

Note:

(1) Other administrative expenses includes recharges from NatWest Group companies and other miscellaneous costs included in which are litigation and conduct costs. Further details of conduct and litigation are provided in Note 15.

The average number of colleagues, 1,686 (2019 - 1,569) are contractually employed by NWB with all related staff costs paid by the Group.

4. Auditor's remuneration

All audit-related and other services are approved by the NatWest Group Audit Committee and are subject to strict controls to ensure the external auditor's independence is unaffected by the provision of other services. The NatWest Group Audit Committee recognises that for certain assignments the auditor is best placed to perform the work economically; for other work the Group selects the supplier best placed to meet its requirements. The Group's auditor is permitted to tender for such work in competition with other firms where the work is permissible under audit independence rules. The Bank's Audit Committee reviews the amount of audit and non audit services provided by the Group's auditor.

Amounts paid to the Group's auditors for statutory audit and other services are set out below:

	2020	2019
	£m	£m
Fees payable for the audit of the Group's annual accounts	0.5	0.4
- Non audit work	-	-
- Other services pursuant to legislation	0.2	0.2
Total audit and audit-related assurance services fees	0.7	0.6

In addition, the auditor received remuneration of £0.4m (2019 - £0.3m) for NWG reporting audit work; this fee was borne by NWG.

5. Emoluments of directors

	2020	2019
	£m	£m
Chairman and non-executive directors - emoluments	0.4	0.3
Executive directors - emoluments	1.2	1.5
	1.6	1.8
Number of directors to whom retirement benefits are accruing in respect of qualifying service:		
- money purchase schemes	1	2

The total emoluments of the highest paid director were £0.9 million (2019 - £1.1 million). This includes long term benefits consisting of Long Term Incentive Plans (LTIPs) and deferred pay awards. The accrued pension attributable to that director was £0.1 million (2019 - £0.1 million). The executive directors may also participate in the NatWest Group plc executive share option and share save schemes.

6. Tax

	2020	2019
	£m	£m
Current tax		
Charge for the year	29	82
Under/(over) provision in respect of prior years	4	(3)
	33	79
Deferred tax		
Charge for the year	-	1
	-	1
Tax charge for the year	33	80

The actual tax charge differs from the expected tax charge computed by applying the UK corporation tax rate of 19% (2019 - 19%) as follows:

	2020	2019
	£m	£m
Expected tax charge[(1)]	24	57
Items not allowed for tax	7	5
Non taxable item	(6)	-
Tax credit paid in equity	(3)	(3)
Banking surcharge	8	24
Rate difference due to movement of deferred tax liability at lower rate	(1)	-
Adjustments in respect of prior years	4	(3)
Actual tax charge	33	80

Note:

(1) In the current period, the substantively enacted UK Corporation tax rate applicable to the company from 1 April 2020 was increased from 25% to 27%. The combined rate of 27% consists of the main UK Corporation tax rate of 19% and a bank surcharge of 8%. The closing deferred tax assets and liabilities have been calculated at 27% and accordingly a rate change adjustment has arisen as the opening deferred tax balance had been calculated taking into account the previously enacted rate of 25%.
Since the balance sheet date, it was announced in the UK Government's Budget on 3 March 2021 that the main UK corporation tax rate will increase from 19% to 25% from 1 April 2023. This change has not yet been substantively enacted.
The UK Government has also announced a review of the current bank surcharge rate of 8% to ensure that the combined rate of Corporation tax, applicable to banking entities, does not increase substantially from its current level when the proposed change to the main UK corporation tax rate comes into effect. Therefore, the company has not made an estimate of the impact of the post balance sheet date change in the main UK Corporation tax rate on the basis that it is uncertain what the combined rate of Corporation tax, applicable to banking entities from 1 April 2023, will be until the UK government has completed its review of the bank surcharge.

Deferred tax

	Group		Bank	
	2020	2019	2020	2019
	£m	£m	£m	£m
Deferred tax asset	8	8	9	9

Net deferred tax asset comprised:

	Group			Bank		
	Other temporary differences	IFRS Transition	Total	Other temporary differences	IFRS Transition	Total
	£m	£m	£m	£m	£m	£m
At 1 January 2019	4	5	9	4	6	10
Charge to income statement	(1)	-	(1)	(1)	-	(1)
At 31 December 2019	3	5	8	3	6	9
Charge to income statement	1	(1)	-	1	(1)	-
At 31 December 2020	4	4	8	4	5	9

Deferred tax

A deferred tax asset of £8 million (2019 - £8 million) has been recognised for the Group at 31 December 2020. This asset has been recognised in the financial statements in respect of the deferral of bonuses under the medium-term incentive plan; the provision for litigation, redress and sundry losses; and fixed asset temporary differences. Based on recent and forecast trading, the tax due on future profits in the current and next financial year will exceed the value of the deferred tax asset.

The directors are of the opinion that, in view of the type and use of properties involved, the likelihood of any material tax liabilities arising on the disposal of the Group's non-investment properties at current market value is so remote that no useful purpose would be served in attempting to quantify it. The Group's principal property is occupied for the purposes of the Group's trade and consequently any gains arising on disposal are expected to be rolled-over pursuant to Taxation of Chargeable Gains Act 1992, Section 152.

7. Financial instruments

Financial instruments - classification

The following tables analyse the Group's financial assets and liabilities in accordance with the categories of financial instruments on an IFRS 9 basis. Assets and liabilities outside the scope of IFRS 9 are shown within other assets and other liabilities.

	Group			
Assets	Mandatory fair value through profit or loss £m	Amortised cost £m	Other assets £m	Total £m
Cash and balances at central bank	-	3	-	3
Loans to banks - amortised cost	-	333	-	333
Loans to customers - amortised cost	-	16,317	-	16,317
Amount due from holding companies and fellow subsidiaries	-	21,343	-	21,343
Derivatives	29	-	-	29
Property, plant and equipment	-	-	298	298
Other assets	-	35	76	111
31 December 2020	29	38,031	374	38,434
Cash and balances at central bank	-	3	-	3
Loans to banks - amortised cost	-	143	-	143
Loans to customers - amortised cost	-	14,792	-	14,792
Amount due from holding companies and fellow subsidiaries	-	18,690	-	18,690
Derivatives	22	-	-	22
Property, plant and equipment	-	-	294	294
Other assets	-	34	59	93
31 December 2019	22	33,662	353	34,037

	Group			
Liabilities	Mandatory fair value through profit or loss £m	Amortised cost £m	Other liabilities £m	Total £m
Bank deposits	-	4	-	4
Customer deposits	-	30,142	-	30,142
Amount due to holding companies and fellow subsidiaries	-	6,113	-	6,113
Derivatives	28	-	-	28
Other financial liabilities	-	310	-	310
Other liabilities (1)	-	69	68	137
Subordinated liabilities	-	265	-	265
31 December 2020	28	36,903	68	36,999
Bank deposits	-	12	-	12
Customer deposits	-	26,390	-	26,390
Amount due to holding companies and fellow subsidiaries	-	5,463	-	5,463
Derivatives	20	-	-	20
Other financial liabilities	-	310	-	310
Other liabilities (1)	-	60	164	224
Subordinated liabilities	-	265	-	265
31 December 2019	20	32,500	164	32,684

Note:
(1) Includes lease liabilities of £66 million (31 December 2019 - £57 million), held at amortised cost.

7. Financial instruments continued

Financial instruments – classification continued

	Bank			
Assets	Mandatory fair value through profit or loss £m	Amortised cost £m	Other assets £m	Total £m
Cash and balances at central bank	-	3	-	3
Loans to banks - amortised cost	-	312	-	312
Loans to customers - amortised cost	-	15,887	-	15,887
Amount due from holding companies and fellow subsidiaries	-	21,714	-	21,714
Derivatives	29	-	-	29
Investment in Group undertakings	-	-	110	110
Property, plant and equipment	-	-	298	298
Other assets	-	29	64	93
31 December 2020	29	37,945	472	38,446
Cash and balances at central bank	-	3	-	3
Loans to banks - amortised cost	-	124	-	124
Loans to customers - amortised cost	-	14,172	-	14,172
Amount due from holding companies and fellow subsidiaries	-	19,249	-	19,249
Derivatives	22	-	-	22
Investment in Group undertakings	-	-	110	110
Property, plant and equipment	-	-	294	294
Other assets	-	28	48	76
31 December 2019	22	33,576	452	34,050

	Bank			
Liabilities	Mandatory fair value through profit or loss £m	Amortised cost £m	Other liabilities £m	Total £m
Bank deposits	-	4	-	4
Customer deposits	-	30,142	-	30,142
Amount due to holding companies and fellow subsidiaries	-	6,111	-	6,111
Derivatives	28	-	-	28
Other financial liabilities	-	310	-	310
Other liabilities (1)	-	67	63	130
Subordinated liabilities	-	265	-	265
31 December 2020	28	36,899	63	36,990
Bank deposits	-	12	-	12
Customer deposits	-	26,390	-	26,390
Amount due to holding companies and fellow subsidiaries	-	5,463	-	5,463
Derivatives	20	-	-	20
Other financial liabilities	-	310	-	310
Other liabilities (1)	-	62	153	215
Subordinated liabilities	-	265	-	265
31 December 2019	20	32,502	153	32,675

Note:
(1) Includes lease liabilities of £66 million (31 December 2019 - £57 million), held at amortised cost.

7. Financial instruments continued

Financial instruments – classification continued

Interest rate benchmark reform
In 2020 the Group continued to implement its LIBOR program with the view of being ready for the various transition events that are expected to occur prior to the cessation of the vast majority of the IBOR benchmark rates at the end of 2021 and the USD LIBOR in 2023. In the UK, regulators most notably the BoE and the FCA have issued guidance on how market participants are expected to approach transition as well as the regulatory expectations in relation to the credit adjustment spread calculation methodologies, conversion strategies, existence of products referencing IBOR benchmark rates amongst other items.
Our programme continues to address the key areas that will be affected by the IBOR reform most notably:

- Client stratification, engagement and education
- Contract fall-back remediation;
- Transition on an economically equivalent basis;
- Effect of modifications to existing terms beyond those that are attributable to the IBOR reform.
- Funding and liquidity management, planning and forecast;
- Risk management;
- Financial reporting and valuation;
- Changes to processes and systems covering front-end, risk and finance systems.

The Group continued to develop new products that will reference the new alternative risk-free rates and worked with clients to assess their readiness and ability to adopt new products or transition existing products. A comprehensive review of the effect of IBOR reform on funding, liquidity and risk management has also been conducted. This is expected to be fully implemented over the course of 2021. The Bank is focused on adapting its key systems, methodologies and processes to meet the requirements of the new risk-free rates. This is expected to be concluded in advance of the LIBOR cessation date at the end of 2021.

The Bank remains engaged with regulators, standard setters and other market participants on key matters related with IBOR reform and an open dialogue is expected throughout 2021.

The table below provides an overview of the Group's IBOR related exposure by currency and nature of financial instruments. Non-derivative financial instruments are presented on the basis of their carrying amounts excluding ECL while derivative financial instruments are presented on the basis of their notional amount.

	Group						
	Rates subject to IBOR reform				Balances not subject to IBOR reform	Expected credit losses	Total
	GBP LIBOR	USD IBOR[1]	EURO IBOR	Other IBOR			
2020	£m	£m	£m	£m	£m	£m	£m
Loans to banks - amortised cost	-	-	-	-	333	-	333
Loans to customers - amortised cost	2,662	66	57	3	13,663	(134)	16,317
Amounts due from holding companies and fellow subsidiaries	-	-	-	-	21,352	(9)	21,343
Bank deposits	-	-	-	-	4		4
Customer accounts	-	-	-	-	30,142		30,142
Other financial liabilities	310	-	-	-	-		310
Subordinated liabilities	265	-	-	-	-		265
Amounts due to holding companies and fellow subsidiaries	-	-	-	-	6,113		6,113
Loan commitments	96	1	13	-	3,183	-	3,293
Derivatives notional	508	-	7	-	61	-	576

For notes to this table refer to the following page.

7. Financial instruments continued

Financial instruments – classification continued

	Bank						
	Rates subject to IBOR reform				Balances not subject to IBOR reform	Expected credit losses	Total
	GBP LIBOR	USD IBOR(1)	EURO IBOR	Other IBOR			
2020	£m	£m	£m	£m	£m	£m	£m
Loans to banks - amortised cost	-	-	-	-	312	-	312
Loans to customers - amortised cost	2,662	66	57	3	13,230	(131)	15,887
Amounts due from holding companies and fellow subsidiaries	-	-	-	-	21,723	(9)	21,714
Bank deposits	-	-	-	-	4	-	4
Customer accounts	-	-	-	-	30,142	-	30,142
Other financial liabilities	310	-	-	-	-	-	310
Subordinated liabilities	265	-	-	-	-	-	265
Amounts due to holding companies and fellow subsidiaries	-	-	-	-	6,111	-	6,111
Loan commitments	96	1	13	-	3,183	-	3,293
Derivatives notional	508	-	7	-	61	-	576

Note:
(1) USD LIBOR is now expected to convert to alternative RFRs in mid 2023 subject to consultation.

AT1 issuances

The Bank has issued certain capital instruments (AT1) under which reset clauses are linked to IBOR rates subject to reform. Where under the contractual terms of the instrument the coupon resets to a rate which has IBOR as a specified component of its pricing structure these are subject to IBOR reform and are shown in Note 18.

Financial instruments – valuations

All financial instruments carried at fair value are valued at level 2.

These are valued using techniques based significantly on observable market data. Instruments in this category are valued using quoted prices for similar instruments.

Fair value - financial instruments
In accordance with accounting policy 18, all derivatives are measured at fair value.

7. Financial instruments continued

Financial instruments – valuations continued

The following table shows the carrying values and the fair values of financial instruments carried at amortised cost on the balance sheet:

	Group					
				Fair value hierarchy level		
2020	Items where fair value approximates carrying value £m	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets						
Cash and balances at central banks	3	-	-	-	-	-
Loan to banks	333	-	-	-	-	-
Loan to customers	1,106	15,211	15,024	-	-	15,024
Amount due from holding companies and fellow subsidiaries	11,925	9,418	9,448	-	-	9,448
Other assets	35	-	-	-	-	-
Financial liabilities						
Bank deposits	4	-	-	-	-	-
Customer deposits	30,142	-	-	-	-	-
Amount due to holding companies and other fellow subsidiaries	228	5,885	5,932	-	-	5,932
Other financial liabilities	310	-	-	-	-	-
Subordinated liabilities	-	265	270	-	-	270

	Group					
				Fair value hierarchy level		
2019	Items where fair value approximates carrying value £m	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets						
Cash and balances at central banks	3	-	-	-	-	-
Loan to banks	143	-	-	-	-	-
Loan to customers	1,223	13,569	13,474	-	-	13,474
Amount due from holding companies and fellow subsidiaries	8,292	10,398	10,347	26	-	10,321
Other assets	34	-	-	-	-	-
Financial liabilities						
Bank deposits	12	-	-	-	-	-
Customer deposits	26,390	-	-	-	-	-
Amount due to holding companies and other fellow subsidiaries	108	5,355	5,332	-	-	5,332
Other financial liabilities	310	-	-	-	-	-
Subordinated liabilities	-	265	256	-	-	256

7. Financial instruments continued

Financial instruments – valuations continued

2020	Bank Items where fair value approximates carrying value £m	Carrying value £m	Fair value £m	Fair value hierarchy level Level 1 £m	Level 2 £m	Level 3 £m
Financial assets						
Cash and balances at central banks	3	-	-	-	-	-
Loan to banks	312	-	-	-	-	-
Loan to customers	1,085	14,802	14,630	-	-	14,630
Amount due from holding companies and fellow subsidiaries	12,210	9,504	9,536	-	-	9,536
Other assets	29	-	-	-	-	-
Financial liabilities						
Bank deposits	4	-	-	-	-	-
Customer deposits	30,142	-	-	-	-	-
Amount due to holding companies and other fellow subsidiaries	227	5,884	5,932	-	-	5,932
Other financial liabilities	310	-	-	-	-	-
Subordinated liabilities	-	265	270	-	-	270

2019	Bank Items where fair value approximates carrying value £m	Carrying value £m	Fair value £m	Fair value hierarchy level Level 1 £m	Level 2 £m	Level 3 £m
Financial assets						
Cash and balances at central banks	3	-	-	-	-	-
Loan to banks	124	-	-	-	-	-
Loan to customers	1,202	12,970	12,889	-	-	12,889
Amount due from holding companies and fellow subsidiaries	8,670	10,579	10,532	26	-	10,506
Other assets	28	-	-	-	-	-
Financial liabilities						
Bank deposits	12	-	-	-	-	-
Customer deposits	26,390	-	-	-	-	-
Amount due to holding companies and other fellow subsidiaries	108	5,355	5,332	-	-	5,332
Other financial liabilities	310	-	-	-	-	-
Subordinated liabilities	-	265	256	-	-	256

The fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Quoted market values are used where available, otherwise, fair values have been established based on discounted expected future cash flows and other valuation techniques. These techniques involve uncertainties and require assumptions and judgements covering prepayments, credit risk and discount rates. Furthermore there is a wide range of potential valuation techniques. Changes in these assumptions would significantly affect estimated fair values. The fair values reported would not necessarily be realised in an immediate sale or settlement. The assumptions and methodologies underlying the calculation of fair values of financial instruments at the balance sheet date are set out below:

Short-term financial instruments

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

7. Financial instruments continued

Financial instruments - valuations continued

Loans to banks and customers – amortised cost
In estimating the fair value of loans to banks and customers measured at amortised cost, loans are segregated into appropriate portfolios reflecting the characteristics of the constituent loans. Two principal methods are used to estimate fair value:

(a) Contractual cash flows are discounted using a market discount rate that incorporates the current spread for the borrower or where this is not observable, the spread for borrowers of a similar credit standing.
(b) Expected cash flows (unadjusted for credit losses) are discounted at the current offer rate for the same or similar products.

Bank and customer deposits
Fair values of deposits are estimated using discounted cash flow valuation techniques.

Debt securities in issue and subordinated liabilities
Fair values are determined by using internal valuation models or using quoted prices for similar liabilities.

Financial instruments - maturity analysis

Remaining maturity
The following table shows the residual maturity of financial instruments, based on contractual date of maturity:

	Group					
	2020			2019		
	Less than 12 months £m	More than 12 months £m	Total £m	Less than 12 months £m	More than 12 months £m	Total £m
Assets						
Cash and balances at central bank	3	-	3	3	-	3
Loans to banks - amortised cost	333	-	333	143	-	143
Loans to customers - amortised cost	5,272	11,045	16,317	4,921	9,871	14,792
Amount due from holding companies and fellow subsidiaries	13,422	7,921	21,343	11,702	6,988	18,690
Derivatives	1	28	29	1	21	22
Other assets	35	-	35	34	-	34
Liabilities						
Bank deposits	4	-	4	12	-	12
Customer deposits	30,142	-	30,142	26,390	-	26,390
Amount due to holding companies and fellow subsidiaries	970	5,143	6,113	1,061	4,402	5,463
Derivatives	2	26	28	1	19	20
Other financial liabilities	-	310	310	-	310	310
Subordinated liabilities	-	265	265	-	265	265
Lease liabilities	1	65	66	1	56	57

7. Financial instruments continued

Financial instruments - maturity analysis continued

	Bank					
	2020			2019		
	Less than 12 months £m	More than 12 months £m	Total £m	Less than 12 months £m	More than 12 months £m	Total £m
Assets						
Cash and balances at central bank	3	-	3	3	-	3
Loans to banks - amortised cost	312	-	312	124	-	124
Loans to customers - amortised cost	5,152	10,735	15,887	4,721	9,451	14,172
Amount due from holding companies and fellow subsidiaries	13,713	8,001	21,714	12,177	7,072	19,249
Derivatives	1	28	29	1	21	22
Other assets	29	-	29	28	-	28
Liabilities						
Bank deposits	4	-	4	12	-	12
Customer deposits	30,142	-	30,142	26,390	-	26,390
Amount due to holding companies and fellow subsidiaries	968	5,143	6,111	1,061	4,402	5,463
Derivatives	2	26	28	1	19	20
Other financial liabilities	-	310	310	-	310	310
Subordinated liabilities	-	265	265	-	265	265
Lease liabilities	1	65	66	1	56	57

Liabilities by contractual cash flow maturity

The tables below show the timing of cash outflows to settle financial liabilities, prepared on the following basis:

Financial liabilities are included at the earliest date on which the counterparty can require repayment regardless of whether or not such early repayment results in a penalty. If repayment is triggered by, or is subject to, specific criteria such as market price hurdles being reached, the liability is included at the earliest possible date that conditions could be fulfilled without considering the probability of the conditions being met. For example, if a structured note automatically repays when an equity index exceeds a certain level, the cash outflow will be included in the less than three months period whatever the level of the index at year end.

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

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

	Group					
2020	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
Liabilities by contractual maturity						
Bank deposits	4	-	-	-	-	-
Customer deposits	29,097	1,045	-	-	-	-
Amounts due to holding companies and fellow subsidiaries	250	782	2,715	1,854	648	39
Other financial liabilities	1	4	9	318	-	-
Subordinated liabilities	2	5	14	14	285	-
	29,354	1,836	2,738	2,186	933	39
Guarantees and commitments - notional amounts						
Guarantees[(1)]	67	-	-	-	-	-
Commitments[(2)]	3,293	-	-	-	-	-
	3,360	-	-	-	-	-

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

7. Financial instruments continued

Financial instruments - maturity analysis continued

	Group					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2019	£m	£m	£m	£m	£m	£m
Liabilities by contractual maturity						
Bank deposits	12	-	-	-	-	-
Customer deposits	26,041	352	-	-	-	-
Amounts due to holding companies and fellow subsidiaries	290	740	2,095	2,024	493	-
Other financial liabilities	-	-	-	50	260	-
Subordinated liabilities	-	-	-	-	265	-
Total liabilities	26,343	1,092	2,095	2,074	1,018	-
Guarantees and commitments - notional amounts						
Guarantees(1)	73	-	-	-	-	-
Commitments(2)	2,843	-	-	-	-	-
	2,916	-	-	-	-	-

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

	Bank					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2020	£m	£m	£m	£m	£m	£m
Liabilities by contractual maturity						
Bank deposits	4	-	-	-	-	-
Customer deposits	29,097	1,045	-	-	-	-
Amounts due to holding companies and fellow subsidiaries	242	782	2,715	1,854	648	39
Other financial liabilities	1	4	9	318	-	-
Subordinated liabilities	2	5	14	14	285	-
	29,346	1,836	2,738	2,186	933	39
Guarantees and commitments - notional amounts						
Guarantees(1)	67	-	-	-	-	-
Commitments(2)	3,293	-	-	-	-	-
	3,360	-	-	-	-	-

	Bank					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2019	£m	£m	£m	£m	£m	£m
Liabilities by contractual maturity						
Bank deposits	12	-	-	-	-	-
Customer deposits	26,041	352	-	-	-	-
Amounts due to holding companies and fellow subsidiaries	407	705	2,079	1,975	469	-
Other financial liabilities	-	-	-	50	260	-
Subordinated liabilities	-	-	-	-	265	-
Total liabilities	26,460	1,057	2,079	2,025	994	-
Guarantees and commitments - notional amounts						
Guarantees(1)	73	-	-	-	-	-
Commitments(2)	2,843	-	-	-	-	-
	2,916	-	-	-	-	-

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

8. Loan impairment provisions

Loan exposure and impairment metrics

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

	2020 £m	2019 £m
Loans - amortised cost		
Stage 1	14,675	14,292
Stage 2	1,881	552
Stage 3	285	180
Inter-Group (1)	21,343	18,690
	38,184	33,714
ECL provisions (2)		
Stage 1	30	7
Stage 2	67	6
Stage 3	37	26
Inter-Group	9	2
	143	41
ECL provision coverage (3,4)		
Stage 1 (%)	0.2	0.0
Stage 2 (%)	3.6	1.1
Stage 3 (%)	13.0	14.4
Inter-Group (%)	-	-
	0.4	0.1
Impairment losses/(releases)		
ECL charge/(release)		
Stage 1	26	(14)
Stage 2	59	3
Stage 3	15	5
Third party	100	(6)
Inter-Group	7	(1)
	107	(7)
ECL loss rate - annualised (basis point) (5)	59.4	NA
Amounts written off	3	1

Notes:
(1) The Group's intercompany assets are classified in Stage 1.
(2) Includes £2 million (2019 – nil) related to contingent liabilities.
(3) ECL provisions coverage is calculated as ECL provisions divided by loans - amortised cost.
(4) ECL provisions coverage and ECL loss rates are calculated on third party loans and related ECL provisions and charge respectively. ECL loss rate is calculated as annualised third party ECL charge divided by loans - amortised cost.
(5) No ECL loss for the prior year, hence ECL loss rate is not applicable.
(6) The table shows gross loans only and excludes amounts that are outside the scope of the ECL framework.

Critical accounting policy: Loan impairment provisions

The loan impairment provisions have been established in accordance with IFRS 9. Accounting policy 14 sets out how the expected loss approach is applied. At 31 December 2020, client loan impairment provisions amounted to £134 million (2019 - £39 million). A loan is impaired when there is objective evidence that the cash flows will not occur in the manner expected when the loan was advanced. Such evidence includes changes in the credit rating of a borrower, the failure to make payments in accordance with the loan agreement; significant reduction in the value of any security; breach of limits or covenants; and observable data about relevant macroeconomic measures.

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

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

Refer to page 21 for IFRS 9 ECL model design principles.

9. Derivatives

Companies in the Group transact derivatives to manage balance sheet foreign exchange, interest rate and credit risk.

	Group and Bank					
	2020			2019		
	Notional amounts £m	Assets £m	Liabilities £m	Notional amounts £m	Assets £m	Liabilities £m
Exchange rate contracts:						
Spot, forwards and futures	37	1	1	108	1	1
Currency swaps	3	-	-	18	-	-
Interest rate contracts:						
Interest Rate swaps	1,069	28	27	1,071	21	19
	1,109	29	28	1,197	22	20

10. Investments in Group undertakings

Investments in Group undertakings are carried at cost less impairment.

	Bank	
	2020 £m	2019 £m
At 1 January and 31 December	110	110

The subsidiary undertakings of the Bank are shown below. Their capital consists of ordinary shares which are unlisted.

All of the subsidiary undertakings are owned, directly or indirectly, through intermediate holding companies and are all wholly owned. They are included in the Group's consolidated financial statements and have an accounting reference date of 31 December.

	Proportion of ownership (%)	Nature of business	Country of incorporation
Coutts Finance Co. (1)	100%	Provision of residential mortgages	Great Britain
RBS Asset Management (Dublin) Limited (2)	100%	Provision of investment management services	Ireland
RBS Collective Investment Funds Limited (3)	100%	Provision of investment management services	Great Britain
RBS Asset Management Holdings (1)	100%	Holding company	Great Britain
RBS Asset Management (ACD) Limited (1)	100%	Provision of investment management services	Great Britain
RBSG Collective Investments Holdings Limited (3)	100%	Holding company	Great Britain
RBSG Collective Investments Nominees Limited (3)	100%	Nominee	Great Britain
Strand Nominees Limited (1)	100%	Nominee	Great Britain

No impairment was recognised in 2020 or 2019.

Notes:
(1) Registered office is 440 Strand, London, WC2R OQS.
(2) Registered office is One Dockland Central, Guild Street, IFSC, Dublin.
(3) Registered office is 6-8 George Street, Edinburgh, EH2 2PF.

NOTES TO THE ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2020

11. Property, plant and equipment

2020	Group and Bank Investment properties £m	Land £m	Building £m	Short Leasehold £m	Computer and other equipment £m	Right of use property £m	Total £m
Cost or valuation							
At 1 January	50	47	155	1	18	61	332
Additions	-	-	2	-	8	10	20
Reclassification of assets	-	-	1	-	(1)	-	-
Change in fair value of investment properties	(7)	-	-	-	-	-	(7)
At 31 December	43	47	158	1	25	71	345
Accumulated depreciation and amortisation							
At 1 January	-	-	20	1	12	5	38
Charge for the year	-	-	6	-	2	1	9
At 31 December	-	-	26	1	14	6	47
Net book value at 31 December	43	47	132	-	11	65	298

2019	Group and Bank Investment properties £m	Land £m	Building £m	Short Leasehold £m	Computer and other equipment £m	Right of use property £m	Total £m
Cost or valuation							
At 1 January	55	47	153	3	16	-	274
Implementation of IFRS 16 on 1 January 2019	-	-	-	-	-	60	60
Additions	-	-	2	-	3	1	6
Disposals	-	-	-	(2)	(1)	-	(3)
Change in fair value of investment properties	(5)	-	-	-	-	-	(5)
At 31 December	50	47	155	1	18	61	332
Accumulated depreciation and amortisation							
At 1 January	-	-	14	3	11	-	28
Implementation of IFRS 16 on 1 January 2019	-	-	-	-	-	4	4
Charge for the year	-	-	6	-	1	1	8
Disposals	-	-	-	(2)	-	-	(2)
At 31 December	-	-	20	1	12	5	38
Net book value at 31 December	50	47	135	-	6	56	294

There was no loss on disposal of assets during the year (2019 - nil).

Investment property valuations principally employ present value techniques that discount expected cash flows. Expected cash flows reflect rental income, occupancy and residual market values; valuations are sensitive to changes in these factors. The investment property fair value measurements are categorised as level 3.

Valuations were carried out by qualified surveyors who are members of the Royal Institution of Chartered Surveyors, or an equivalent overseas body.

Rental income from investment properties was £2 million (2019 - £4 million).

NOTES TO THE ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2020

12. Intangible assets

	Group					
	2020			2019		
	Goodwill £m	Other(1) £m	Total £m	Goodwill £m	Other(1) £m	Total £m
Cost						
At 1 January	9	45	54	9	33	42
Additions	-	20	20	-	12	12
Disposals	-	(1)	(1)	-	-	-
At 31 December	9	64	73	9	45	54
Accumulated amortisation						
At 1 January	-	7	7	-	3	3
Impairment of intangible assets	-	1	1	-	-	-
Charge for the year	-	8	8	-	4	4
At 31 December	-	16	16	-	7	7
Net book value at 31 December	9	48	57	9	38	47

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	Bank	
	2020 £m	2019 £m
Cost		
At 1 January	45	33
Disposals	(1)	-
Additions	20	12
At 31 December	64	45
Accumulated amortisation		
At 1 January	7	3
Impairment of intangible assets	1	-
Charge for the year	8	4
At 31 December	16	7
Net book value at 31 December	48	38

Note:
(1) Principally internally generated software.

Intangible assets are reviewed for indicators of impairment. In 2020 £1 million (2019 - nil) of previously capitalised software was impaired primarily as a result of software which was no longer expected to yield future economic benefit. Refer to accounting policy 7 for further details.

13. Other assets

	Group		Bank	
	2020 £m	2019 £m	2020 £m	2019 £m
Due within 12 months:				
Prepayments	5	3	5	2
Accrued income and other assets(1)	41	35	31	27
Due after 12 months:				
Deferred tax (Note 6)	8	8	9	9
Intangible assets (Note 12)	57	47	48	38
	111	93	93	76

Note:
(1) Balances primarily consist of accrued fee income.

14. Other financial liabilities

	Group and Bank	
	2020	2019
	£m	£m
Debt securities in issue - amortised cost	310	310
	310	310

15. Other liabilities

	Group		Bank	
	2020	2019	2020	2019
	£m	£m	£m	£m
Due within 12 months:				
Accruals	22	14	20	12
Deferred income	15	19	15	19
Other liabilities	3	3	1	5
Lease liabilities (Note 19)	66	57	66	57
Current tax	13	77	10	68
Due after 12 months:				
Provisions for liabilities and charges	18	54	18	54
	137	224	130	215

Provisions for liabilities and charges:

	Group and Bank		
	Provision for severance	Other	Total
	£m	£m	£m
At 1 January 2020	4	50	54
Charge to income statement	4	6	10
Releases to income statement	(3)	(34)	(37)
Provisions utilised	(2)	(9)	(11)
ECL impairment charge	-	2	2
At 31 December 2020	3	15	18

Critical accounting policy: Provision for liabilities

The key judgement involved is in determining whether a present obligation exists. There is often a high degree of uncertainty and judgement is based on the specific facts and circumstances relating to individual events in determining whether there is a present obligation. Judgement is involved in determining whether an obligation exists, and in estimating the probability, timing and amount of any outflows. Where the Group can look to another party such as an insurer to pay some or all of the expenditure required to settle a provision, any reimbursement is recognised when, and only when, it is virtually certain that it will be received. The Group generally does not disclose information about the establishment or existence of a provision for a particular matter where disclosure of the information can be expected to prejudice seriously the Group's position in the matter.

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

16. Subordinated liabilities

	Group and Bank				
	2020 Interest rate	2020 £m	2019 Interest rate	2019 £m	Maturity
Due to:					
National Westminster Bank Plc					
£221,000,000	LIBOR + 2.38%	220	LIBOR + 2.38%	220	2027
£45,000,000	LIBOR + 3.85%	45	LIBOR + 3.85%	45	2028
		265		265	

The loans are unsecured and subordinated to the claims of senior creditors. The loan capital is available to absorb losses but ranks ahead of other existing capital in the event of liquidation. The Bank has a contractual obligation to pay interest.

NOTES TO THE ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2020

17. Share Capital and reserves

	Group and Bank			
	Allotted, called up and fully paid		Authorised	
	2020	2019	2020	2019
	£m	£m	£m	£m
Equity shares:				
Ordinary shares of £1	41	41	50	50
	41	41	50	50

Ordinary shares
During the year, no ordinary dividends were paid by the Bank (2019 - £215 million) to NWB plc.

18. Paid-in equity

Paid-in equity comprises equity instruments issued by the Bank other than those legally constituted as shares.

	Group and Bank	
	2020	2019
	£m	£m
AT1 instruments:		
£167 million 6.0% notes repayable from September 2022	165	165
£35 million LIBOR + 6.09% notes repayable from December 2023	35	35
	200	200

AT1 instruments issued by the Bank having the legal form of debt are classified as equity under IFRS. The coupons on this instrument are non-cumulative and payable at the Bank's discretion. In the event of winding up, any amounts outstanding on the loan will be subordinated.

Equity coupon payments
During the year, equity coupon payments totalling £12 million were paid (2019 - £13 million).

19. Leases

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

Lessees

	Group	
	2020	2019
	£m	£m
Amounts recognised in consolidated income statement		
Interest payable	2	1
Depreciation	1	1

	Group and Bank	
	2020	2019
	£m	£m
Amounts recognised on balance sheet		
Right of use assets included in property, plant and equipment(1)	65	56
Additions to right of use assets	10	1
Lease liabilities(2)	(66)	(57)

The total cash outflow for leases in 2020 is £2 million (2019 - £1 million).

Notes:
(1) Includes right of use asset for plant and equipment of £71 million (2019 - £61 million) and depreciation of £6 million (2019 - £5 million).
(2) Contractual cashflows of lease liabilities is shown in Note 7.

20. Memorandum items

Contingent liabilities and commitments

The amounts shown in the table below are intended only to provide an indication of the volume of business outstanding at 31 December 2020. Although the Group and the Bank are exposed to credit risk in the event of non-performance of the obligations undertaken by clients, the amounts shown do not, and are not intended to, provide any indication of the Group and Bank's expectation of future losses.

	Group and Bank	
	2020	2019
	£m	£m
Contingent liabilties:		
Guarantees and assets pledged as collateral security:		
- Guarantees and irrevocable letters of credit	67	73
	67	73
Commitments:		
Undrawn formal standby facilities, credit lines and other commitments to lend:		
- 1 year and over	347	436
- Less than 1 year	2,946	2,407
	3,293	2,843

Banking commitments and contingent obligations, which have been entered into on behalf of clients and for which there are corresponding obligations from clients, are not included in assets and liabilities. The Group and Bank's maximum exposure to credit loss, in the event of its obligation crystallising and all counterclaims, collateral or security proving valueless, is represented by the contractual nominal amount of these instruments included in the table above. These commitments and contingent obligations are subject to the Group and Bank's normal credit approval processes.

Standby facilities and credit lines – under a loan commitment the Bank agrees to make funds available to a client in the future. Loan commitments, which are usually for a specified term may be unconditionally cancellable or may persist, provided all conditions in the loan facility are satisfied or waived. Commitments to lend include commercial standby facilities and credit lines and unutilised overdraft facilities.

Other commitments - these include documentary credits, which are commercial letters of credit providing for payment by the Bank to a named beneficiary against presentation of specified documents, forward asset purchases, forward deposits placed and undrawn note issuance and revolving underwriting facilities, and other short-term trade related transactions.

Guarantees – the Bank gives guarantees on behalf of clients. A financial guarantee represents an irrevocable undertaking that the Bank will meet a client's specified obligations to a third party if the client fails to do so. The maximum amount that the Bank could be required to pay under a guarantee is its principal amount as disclosed in the table. The Bank expects most guarantees it provides to expire unused.

Other contingent liabilities – these include standby letters of credit, supporting client debt issues and contingent liabilities relating to client trading activities such as those arising from performance and customs bonds, warranties and indemnities.

Additional contingent liabilities arise in the normal course of the Bank's business, associated with ongoing legal, regulatory or tax situations at both individual client and Bank levels. These situations are monitored by management and where it is possible to quantify reliably, provisions are booked. However given uncertainties such as establishing detailed fact patterns, legal status and regulatory status, in certain cases this is not feasible until further investigation has been conducted. In relation to such matters, looking at the range of potential outcomes, it is not anticipated that any material loss will arise from these transactions.

Litigation, investigations and reviews

As a participant in the financial services industry, the Group operates in a highly regulated environment. At any moment in time it is likely that the Group will be involved in a number of investigations and disputes. Such matters are subject to many uncertainties and their outcome is often difficult to predict, particularly in the early stages. The directors of the Bank have reviewed these actual, threatened and known potential claims and proceedings and, after consulting with the relevant legal advisers are satisfied that the outcome of these claims and proceedings will not have a material adverse effect on the Group's consolidated net assets, results of operations or cash flows.

The Group recognises a provision for a liability in relation to such matters when it is probable that an outflow of economic benefits will be required to settle an obligation resulting from past events, and a reliable estimate can be made of the amount of the obligation.

In many proceedings and investigations, it is not possible to determine whether any loss is probable or to estimate reliably the amount of any loss, either as a direct consequence of the relevant proceedings and investigations or as a result of adverse impacts or restrictions on the Group's reputation, business and operations.

Numerous legal and factual issues may need to be resolved, including through potentially lengthy discovery and document production exercises and determination of important factual matters, and by addressing novel or unsettled legal questions relevant to the proceedings in question, before a liability can reasonably be estimated for any claim. The Group cannot predict if, how, or when such claims will be resolved or what the eventual settlement, damages, fine, penalty or other relief, if any, may be, particularly for claims that are at an early stage in their development or where claimants seek substantial or indeterminate damages.

20. Memorandum items continued

There are situations where the Group may pursue an approach that in some instances leads to a settlement agreement. This may occur in order to avoid the expense, management distraction or reputational implications of continuing to contest liability, or in order to take account of the risks inherent in defending claims or investigations even for those matters for which the Group believes it has credible defences and should prevail on the merits. The uncertainties inherent in all such matters affect the amount and timing of any potential outflows, for both matters with respect to which provisions have been established and other contingent liabilities.

The future outflow of resources in respect of any matter may ultimately prove to be substantially greater than or less than the aggregate provision that the Group has recognised. Where (and as far as) liability cannot be reasonably estimated, no provision has been recognised.

There were £29 million of net releases in the year for conduct and litigation matters (2019 - £10 million net charge). The Group generally does not disclose information about the establishment or existence of a provision for a particular matter where disclosure of the information can be expected to prejudice seriously the Group's position in the matter.

The Financial Services Compensation Scheme

The Financial Services Compensation Scheme (FSCS), the UK's statutory fund of last resort for clients of authorised financial services firms, pays compensation if a firm is unable to meet its obligations. The FSCS funds compensation for clients by raising management expenses levies and compensation levies on the industry. In relation to protected deposits, each deposit-taking institution contributes towards these levies in proportion to their share of total protected deposits on 31 December of the year preceding the scheme year (which runs from 1 April to 31 March), subject to annual maxima set by the FCA. In addition, the FSCS has the power to raise levies on a firm that has ceased to participate in the scheme and is in the process of ceasing to be authorised for the costs that it would have been liable to pay had the FSCS made a levy in the financial year it ceased to be a participant in the scheme.

Capital Support Deed

The Bank, together with other subsidiaries of NWH Ltd, is party to a Capital Support Deed (CSD). Under the terms of the CSD, the Bank may be required, if compatible with its legal obligations, to make distributions on, or repurchase or redeem, its ordinary shares. The amount of this obligation is limited to the Bank's capital resources in excess of the capital and financial resources needed to meet its regulatory requirements. The Bank may also be obliged to make onward distribution to its ordinary shareholders of dividends or other capital distributions received from subsidiaries that are party to the CSD. The CSD also provides that, in certain circumstances, funding received by the Bank from other parties to the CSD becomes immediately repayable, such repayment being limited by the Bank's available resources.

21. Analysis of changes in financing during the year

	Group					
	Share capital		Capital contribution reserve		Subordinated liabilities	
	2020 £m	2019 £m	2020 £m	2019 £m	2020 £m	2019 £m
At 1 January	241	241	339	339	265	315
Transfer to debt securities in issue	-	-	-	-	-	(50)
At 31 December	241	241	339	339	265	265

	Bank					
	Share capital		Capital contribution reserve		Subordinated liabilities	
	2020 £m	2019 £m	2020 £m	2019 £m	2020 £m	2019 £m
At 1 January	241	241	382	382	265	315
Transfer to debt securities in issue	-	-	-	-	-	(50)
At 31 December	241	241	382	382	265	265

22. Analysis of cash and cash equivalents

	Group		Bank	
	2020	2019	2020	2019
	£m	£m	£m	£m
At 1 January				
- cash	3	2	3	2
- cash equivalents	9,229	10,819	9,200	10,781
	9,232	10,821	9,203	10,783
Net cash inflow/(outflow)	3,048	(1,671)	3,014	(1,662)
Effect of exchange rate changes on cash and cash equivalents	(57)	82	(57)	82
At 31 December	12,223	9,232	12,160	9,203
Comprising:				
Cash and balances at central bank	3	3	3	3
Loans to banks including intragroup balances - amortised cost	12,220	9,229	12,157	9,200
Cash and cash equivalents	12,223	9,232	12,160	9,203

23. Related parties

UK Government

The UK Government through HM Treasury is the ultimate controlling party of NatWest Group plc. Its shareholding is managed by UK Government Investments Limited, a company it wholly-owns and as a result, the UK Government and UK Government controlled bodies are related parties of the Bank.

Transactions between the Bank, the UK Government and UK Government controlled bodies, consisted of Corporation Tax and Value Added Tax.

The Group may participate in a number of schemes operated by the BoE in the normal course of business. Members of the Group that are UK authorised institutions are required to maintain non-interest bearing (cash ratio) deposits with the BoE amounting to 0.324% of their average eligible liabilities in excess of £600 million. They also have access to BoE reserve accounts: sterling current accounts that earn interest at the BoE Rate.

Group undertakings

The Group's ultimate holding company is NatWest Group plc, registered in Scotland, and its immediate parent company is NWB, registered in England and Wales. Both companies are incorporated in Great Britain.

As at 31 December 2020, NatWest Group plc heads the largest group in which the Group is consolidated, and NWB heads the smallest group in which the Group is consolidated. Copies of the consolidated financial statements of both companies may be obtained from Legal, Governance and Regulatory Affairs, Gogarburn, Edinburgh EH12 1HQ.

(a) Directors and key management

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

	2020	2019
	£m	£m
Interest receivable	-	-

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

(b) Compensation of directors and key management

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

	2020	2019
	£m	£m
Short term benefits	4	4
Post-employment benefits	1	1
Long term benefits(1)	1	2
	6	7

Note:
(1) Long term benefits consist of LTIPs and deferred pay awards.

23. Related parties continued

(c) Related party transactions

The table below discloses transactions between the Bank and Group and other NatWest Group companies.

	Group	
	2020	2019
	£m	£m
Fees and commissions payable	26	18

	Bank	
	2020	2019
	£m	£m
Interest receivable	128	199
Interest payable	70	65
Fees and commissions receivable	26	27
Fees and commissions payable	26	18
Dividends receivable	25	59

At the balance sheet dates, the following balances were held with related parties:

	Group		Bank	
	2020	2019	2020	2019
	£m	£m	£m	£m
Assets				
Loans to customers:				
Parent companies(1)	21,343	18,690	21,309	18,676
Amount due from subsidiary company	-	-	405	573
Derivatives:				
Parent companies	1	2	1	2
Total assets	21,344	18,692	21,715	19,251
Liabilities				
Bank deposits:				
Parent companies(1)	6,113	5,463	6,111	5,463
Subordinated loans:				
Parent companies	265	265	265	265
Debt securities in issue:				
Parent companies	310	310	310	310
Derivatives:				
Parent companies	27	19	27	19
Total liabilities	6,715	6,057	6,713	6,057

Note:
(1) £1.9 billion of short dated intercompany assets and liabilities, which meet the IAS 32 criteria, have been netted in 2019.

Operating expenses includes management recharge of £191 million (2019 - £174 million) from other entities with the NatWest Group. Included in the management recharge are payments of non-cancellable operating leases and pension costs.

24. Transactions with directors

At 31 December 2020, amounts outstanding in relation to transactions, arrangements and agreements entered into by authorised institutions across the Group, are shown in the table below.

	2020		2019	
	Aggregate amount outstanding £m	Number of persons	Aggregate amount outstanding £m	Number of persons
Directors:				
Loans to customers	1	4	-	4
Customer deposits	3	4	4	5
Officers:				
Loans to customers	1	7	-	6
Customer deposits	2	7	1	7

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

25. Post balance sheet events

Settlement of a litigation and conduct matter after the balance sheet date has been deemed non material by management and not adjusted. On 26 February 2021 the Group issued debt securities of €290m at EURIBOR +0.949% per annum. There have been no other significant events between the year end and the date of approval of the financial statements which would require a change to, or additional disclosure or amendment in, the financial statements.

RISK FACTORS

Principal Risks and Uncertainties

Set out below are certain risk factors that could adversely affect the Group's future results, its financial condition and prospects and cause them to be materially different from what is forecast or expected, and directly or indirectly impact the value of its securities in issue. These risk factors are broadly categorised and should be read in conjunction with other sections of this annual report, including the Strategic report and the Capital and risk management section. They should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties facing the Group. The current COVID-19 pandemic may exacerbate any of the risks described below.

Economic and political risk

Continuing uncertainty regarding the effects of the UK's withdrawal from the European Union may continue to adversely affect the Group and its operating environment.

Following the 2016 EU Referendum, the UK ceased to be a member of the EU and the European Economic Area (EEA) on 31 January 2020 (Brexit) and the transition period ended on 31 December 2020.

As a result, the Group has engaged in significant Brexit planning and contingency planning. The Group continues to monitor regulatory developments as a result of the UK's departure from the EU. The changes to the Group's operating model may require further changes to its business operations, product offering and client engagement.

The longer-term effects of Brexit on the Group's operating environment are difficult to predict. They may be impacted by wider global macro-economic trends and events, particularly COVID-19 pandemic related uncertainties, which may significantly impact the Group and its clients and counterparties who are themselves dependent on trading with the EU or personnel from the EU. They may exacerbate the economic impacts of the COVID-19 pandemic on the UK, the ROI and the rest of the EU/EEA.

Significant uncertainty remains as to the extent to which EU/EEA laws will diverge from UK law, whether and what equivalence determinations will be made by the various regulators and therefore what the respective legal and regulatory arrangements will be, under which the Group and its subsidiaries will operate.

Risks relating to the COVID-19 pandemic

The effects of the COVID-19 pandemic on the UK, global economies and financial markets, the Group's clients, as well as the Group's competitive environment may continue to have a material adverse effect on the Group's financial results and operations.

In March 2020, the World Health Organization declared the spread of the COVID-19 virus as a pandemic. Since then many countries, including the UK (the Group's most significant market), have at times imposed strict social distancing measures, restrictions on non-essential activities and travel quarantines in an attempt to slow the spread and reduce the impact of the COVID-19 pandemic.

The UK economy, as well as most countries, went into recession in 2020 as measures were introduced to reduce the spread of the virus. UK economic output fell again in November 2020, according to estimates from the Office for National Statistics, as many restrictions were re-introduced towards the end of 2020 and at the start of 2021. The COVID-19 pandemic has caused significant reductions in levels of personal and commercial activity, increased unemployment and significant market volatility in asset prices, interest rates and foreign exchange rates. It has also caused physical disruption and slowdown to global supply chains and working practices, all of which have affected the Group's clients. The Group has exposures to many of the commercial sectors economically impacted by the COVID-19 pandemic, including property, retail, leisure and travel.

Further waves of infection may result in further restrictions and relaxations in affected countries and regions, at least until a vaccine or effective treatment can be widely administered. Vaccine treatments may also fail to achieve immunisation and therefore significant uncertainties remain as to how long the COVID-19 pandemic will last. Even when restrictions are relaxed, they may be re-imposed, sometimes at short notice if either immunisation is ineffective or new strains of the COVID-19 virus or other diseases develop into new epidemics or pandemics.

Significant uncertainties continue as to the extent of the economic contraction and the path and length of time required to achieve economic recovery. In response to the COVID-19 pandemic, central banks, governments, regulators and legislatures in the UK and elsewhere have announced historic levels of support and various schemes for impacted businesses and individuals including forms of financial assistance and legal and regulatory initiatives, including further reductions in interest rates. Whether or not these measures effectively mitigate the negative impacts of the COVID-19 pandemic on the Group, some of these measures, or further measures, such as negative interest rates, may also have an adverse effect on the Group's business and performance.

It is uncertain as to how long the aforementioned financial assistance and legal and regulatory initiatives may last, how they may evolve in the future and how consumers and businesses may react to such initiatives. The Group's consumer clients and corporate clients may be negatively impacted when these support schemes and initiatives are scaled back and ultimately ended, which in turn could expose the Group to increased credit and counterparty risk.

In addition, the COVID-19 pandemic related uncertainties and the range of prudential regulatory support has made reliance on analytical models, planning and forecasting for the Group more complex, and may result in uncertainty impacting the risk profile of the Group and/or that of the wider banking industry.

The medium and long-term implications of the COVID-19 pandemic for the Group clients, the UK housing market, and the UK and global economies and financial markets remain uncertain and may continue to have a material adverse effect on the Group's business, operating results and outlook.

The adverse impact of the COVID-19 pandemic on the credit quality of the Group's counterparties and the implementation of mandated support schemes in response to the COVID-19 pandemic has increased the Group's exposure to counterparty risk, which may adversely affect its financial results and operations.

The effects of the COVID-19 pandemic have adversely affected the credit quality of the Group's borrowers and other counterparties. As a result, we have experienced elevated exposure to credit risk and demands on the Group's funding. If borrowers or other counterparties default or suffer deterioration in credit, this would increase impairment charges, credit reserves, write-downs and regulatory expected loss. An increase in drawings on committed credit facilities may also increase the Group's RWAs. In addition, the level of household indebtedness in the UK remains high and is increasing. The ability of households to service their debts could be challenged by the current period of high unemployment caused by the COVID-19 pandemic. The Group's mortgage and commercial property loans portfolio may also be subject to higher impairment charges as a result of the COVID-19 pandemic if volatility in the property market results in weakened property prices, particularly if default rates increase. If the Group experiences losses and a reduction in future profitability, this is likely to affect the recoverable value of fixed assets, including goodwill and deferred taxes, which may lead to further write-downs.

The Group has applied an internal analysis of MES together with the determination of specific overlay adjustments to inform its IFRS 9 ECL. The recognition and measurement of ECL is complex and involves the use of significant judgement and estimation. This includes the formulation and incorporation of multiple forward-looking economic scenarios into ECL to meet the measurement objective of IFRS 9. The ECL provision is sensitive to the model inputs and economic assumptions underlying the estimate. Going forward, the Group anticipates observable credit deterioration of a proportion of assets resulting in a systematic uplift in defaults, which is mitigated by those economic assumption scenarios being reflected in the Stage 2 ECL across portfolios, along with a combination of post model overlays in both commercial and retail portfolios reflecting the uncertainty of credit outcomes. See also, 'Risk and capital management — Credit Risk'. A credit deterioration would also lead to RWA increases. Furthermore, the assumptions and judgments used in the MES and ECL assessment at 31 December 2020 may not prove to be adequate, resulting in incremental ECL provisions for the Group. As government support schemes reduce, defaults are expected to rise with more ECLs cases moving from Stage 2 to Stage 3.

In line with certain mandated COVID-19 pandemic support schemes, we have sought to assist affected clients with a number of initiatives including the Group's participation in the BBLS, CBILS and CLBILS. In approving CBILS, CLBILS and BBLS, the Group has sought to manage the risks of fraud and money laundering against the need for the fast and efficient release of funds to clients and businesses.

The Group may be exposed to fraud, which may taint the availability of any government guarantee of the BBLS, and conduct and litigation risks arising from approving (or denying) CBILS, CLBILS and BBLS without appropriate due diligence, or the enforcing or pursuing repayment of CBILS,CLBILS and BBLS (or a failure to exercise forbearance), which may have a material adverse effect on the Group's reputation and results of operations. The implementation of the initiatives and efforts mentioned above may result in litigation, regulatory and government actions and proceedings. These actions may result in judgements, settlements, penalties or fines. Any of the above could have an adverse effect on the Group's financial results and operations.

The COVID-19 pandemic may adversely affect the Group's strategy and impair its ability to meet its targets and to achieve its strategic objectives.

The COVID-19 pandemic may impact the Group's ability to meet the financial, capital and operational targets which it has set as part of its strategy. It is uncertain as to how the broader macroeconomic business environment and societal norms may be impacted by the COVID-19 pandemic, which is already resulting in several significant wider societal changes. For example, one of the most visible effects of the COVID-19 pandemic has been the impact on the most vulnerable groups of society and concerns about systemic racial biases and social inequalities.

In addition, the COVID-19 pandemic has accelerated existing economic trends that may radically change the way businesses are run and people live their lives. These trends include digitalisation, decarbonisation, automation, e-commerce and agile working, each of which has resulted in significant market volatility in asset prices. There is also increasing investor, regulatory and client scrutiny regarding how businesses address these changes and related climate, environmental, social, governance and other sustainability related issues, including workplace health, safety and wellbeing, diversity and inclusion, data privacy, workforce management, human rights and supply chain management. Any failure or delay by the Group to adapt its business strategy and to establish and maintain effective governance, procedures, systems and controls in response to these changes and to manage emerging climate, environmental, social, governance and other sustainability related risks and opportunities may have an adverse effect on the Group's reputation, business and results of operations.

The COVID-19 pandemic may also result in unexpected developments or changes in financial markets, the fiscal, tax and regulatory frameworks and consumer client and corporate client behaviour, which could intensify competition in the financial services industry. If the Group is not able to adapt or compete effectively it could experience loss of business, which in turn could adversely affect its business, results of operations and outlook.

The COVID-19 pandemic has heightened the Group's operational risks as most of its colleagues are working remotely, which may also adversely affect the Group's ability to maintain effective internal controls.
As at 31 December 2020, approximately 83% of colleagues were working from home and most of the Group's colleagues continue to work remotely in response to the COVID-19 pandemic. This has increased reliance on the IT systems that enable remote working and increased exposure to fraud, conduct, operational and other risks and may place additional pressure on the Group's ability to maintain effective internal controls and governance frameworks. The IT systems that enable remote working interface with third-party systems, and the Group could experience service denials or disruptions if such systems exceed capacity or if a third-party system fails or experiences any interruptions, all of which could result in reputational damage, significant compensation costs, regulatory sanctions and/or a breach of applicable regulations.

The Group has taken measures to maintain the health, wellbeing and safety of its colleagues during the COVID-19 pandemic. These measures may be ineffective over the longer term and could result in increased expenses, and widespread illness could negatively affect staffing within certain functions, businesses or geographies. Certain areas of the Group also continue to experience workloads that are heavier than usual as a result of increased client requirements and the Group's COVID-19-specific product offerings or other related direct and indirect effects. Resources have been diverted from certain ordinary course activities and regulatory and other change projects, which may have implications on the execution of related deliverables and meeting regulatory and other deadlines. The economic impact of the COVID-19 pandemic may also necessitate changes in the remuneration of the Group's colleagues, particularly at a senior level.

For example, in March 2020 the PRA requested that, in response to the COVID-19 pandemic, bank boards should consider taking appropriate actions regarding the accrual, payment and vesting of variable remuneration. Any of the above could impair the Group's ability to hire, retain and engage qualified colleagues, especially at a senior level, which in turn may adversely impact the Group's ability to serve its clients efficiently and impact productivity across the Group. This could also adversely affect the Group's reputation, its ability to retain and attract critical staff and its ability to retain or grow its client business and/or on its competitive position.

The effects of the COVID-19 pandemic could affect the Group's ability to access sources of liquidity and funding, which may result in higher funding costs and failure to comply with regulatory capital, funding and leverage requirements.
Depending on the severity and duration of market volatility resulting from COVID-19 pandemic related uncertainties and the impact on capital and RWAs, the Group and its subsidiaries may be required to adapt their funding plans in order to satisfy their respective capital and funding requirements, which may have a material adverse effect on the Group. In response to the COVID-19 pandemic, there have been relaxations on certain countercyclical buffer requirements and stress tests as well as the calculation of RWAs and leverage, which may be reinstated in the future.

The COVID-19 pandemic has caused significant market volatility which has increased the Group's market risk, which has in turn increased certain RWAs. Any downgrading to the credit ratings and/or outlooks assigned to NatWest Group plc, NWB Plc or other NatWest Group subsidiaries and their respective debt securities could exacerbate funding and liquidity risk in the Group.

Legal, regulatory and conduct risk

The Bank may not effectively manage the transition of London interbank offer rates (LIBOR) and other interbank offer rates (IBORs) to alternative risk-free rates.
UK and international regulators are driving the transition from the use of IBORs, including LIBOR, to alternative risk-free rates (RFRs). Interest rate benchmark reform is a key priority of the Financial Stability Board and working groups have been established in a number of jurisdictions to support the transition. Major central banks and regulators including the FCA, BoE, and the Federal Reserve, have strongly urged market participants to transition to RFRs, given the FCA have indicated that the availability of LIBOR beyond the end of 2021 cannot be guaranteed. The Group has exposure to IBORs, and continues to reference it in certain products, primarily derivatives and cash products. The Group has started to phase out its use of IBOR in line with the BoE transition roadmap and has embedded appropriate fall-back mechanisms in most new IBOR activities.

The Group is actively engaged with clients and industry working groups to manage the risks relating to this exposure, and explore ways to transition IBOR exposures to RFRs to the extent possible. Any economic impacts will be dependent on, inter alia, the establishment of deep and liquid RFR markets, and the establishment of clear and consistent market conventions for all replacement products, as well as counterparties' willingness to accept, and transition to, these conventions. Furthermore, certain IBOR obligations may not be able to be changed, thus resulting in fundamentally different economic outcomes than originally intended. The uncertainties around the timing and manner of transition to RFRs expose the Group, its clients and the financial services industry more widely to risk.