VIRGIN MONEY UK PLC
INTERIM FINANCIAL REPORT
SIX MONTHS TO 31 MARCH 2021

BASIS OF PRESENTATION

Virgin Money UK PLC ('Virgin Money', 'VMUK' or 'the Company'), together with its subsidiary undertakings (which together comprise the 'Group'), operate under the Clydesdale Bank, Yorkshire Bank, B and Virgin Money brands. This release covers the results of the Group for the six months ended 31 March 2021.

Statutory basis: Statutory information is set out on page 19 and within the interim condensed consolidated financial statements.

Underlying basis: The results are adjusted to remove certain items that do not promote an understanding of historical or future trends of earnings or cash flows, which enables a more meaningful comparison of the Group's underlying performance. A reconciliation from the underlying results to the statutory basis is shown on page 20 and rationale for the adjustments is shown on page 100.

Alternative performance measures: the financial key performance indicators (KPIs) used in monitoring the Group's performance and reflected throughout this report are determined on a combination of bases (including statutory, regulatory and alternative performance measures), as detailed at 'Measuring financial performance – glossary' on pages 257 to 258 of the Group Annual Report and Accounts for the year ended 30 September 2020. APMs are closely scrutinised to ensure that they provide genuine insights into the Group's progress; however, statutory measures are the key determinant of dividend paying capability.

Certain figures contained in this document, including financial information, may have been subject to rounding adjustments and foreign exchange conversions. Accordingly, in certain instances, the sum or percentage change of the numbers contained in this document may not conform exactly to the total figure given.

FORWARD-LOOKING STATEMENTS

The information in this document may include forward-looking statements, which are based on assumptions, expectations, valuations, targets, estimates, forecasts and projections about future events. These can be identified by the use of words such as 'expects', 'aims', 'targets', 'seeks', 'anticipates', 'plans', 'intends', 'prospects', 'outlooks', 'projects', 'forecasts', 'believes', 'estimates', 'potential', 'possible', and similar words or phrases. These forward-looking statements, as well as those included in any other material discussed at any presentation, are subject to risks, uncertainties and assumptions about the Group and its securities, investments and the environment in which it operates, including, among other things, the development of its business and strategy, any acquisitions, combinations, disposals or other corporate activity undertaken by the Group (including but not limited to the integration of the business of Virgin Money Holdings (UK) PLC and its subsidiaries into the Group), trends in its operating industry, changes to customer behaviours and covenant, macroeconomic and/or geopolitical factors, the repercussions of the outbreak of coronaviruses (including but not limited to the COVID-19 outbreak), changes to its Board and/or employee composition, exposures to terrorist activity, IT system failures, cybercrime, fraud and pension scheme liabilities, changes to law and/or the policies and practices of the Bank of England (BoE), the Financial Conduct Authority (FCA) and/or other regulatory and governmental bodies, inflation, deflation, interest rates, exchange rates, changes in the liquidity, capital, funding and/or asset position and/or credit ratings of the Group, future capital expenditures and acquisitions, the repercussions of the UK's exit from the European Union (EU) (including any change to the UK's currency and the terms of any trade agreements (or lack thereof) between the UK and the EU), Eurozone instability, and any referendum on Scottish independence.

In light of these risks, uncertainties and assumptions, the events in the forward-looking statements may not occur. Forward-looking statements involve inherent risks and uncertainties. Other events not taken into account may occur and may significantly affect the analysis of the forward-looking statements. No member of the Group or their respective directors, officers, employees, agents, advisers or affiliates gives any assurance that any such projections or estimates will be realised or that actual returns or other results will not be materially lower than those set out in this document and/or discussed at any presentation. All forward-looking statements should be viewed as hypothetical. No representation or warranty is made that any forward-looking statement will come to pass. No member of the Group or their respective directors, officers, employees, agents, advisers or affiliates undertakes any obligation to update or revise any such forward-looking statement following the publication of this document nor accepts any responsibility, liability or duty of care whatsoever for (whether in contract, tort or otherwise) or makes any representation or warranty, express or implied, as to the truth, fullness, fairness, merchantability, accuracy, sufficiency or completeness of, the information in this document.

The information, statements and opinions contained in this document do not constitute or form part of, and should not be construed as, any public offer under any applicable legislation or an offer to sell or solicitation of any offer to buy any securities or financial instruments or any advice or recommendation with respect to such securities or other financial instruments.

Interim financial report

For the six months ended 31 March 2021

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Virgin Money UK PLC Interim Results 2021

David Duffy, Chief Executive Officer:

"Virgin Money had a strong first half. We doubled underlying profit compared to last year and returned to statutory profit. The quality of our loan book remained resilient in the period, and we've continued to support customers and look after our colleagues and communities, while safeguarding the bank. We've made significant strategic progress to transform Virgin Money into a leading digital bank and our rebranding is largely complete. We've launched a range of innovative and compelling Virgin Money personal and business products as well as differentiated loyalty offers, which are showing early signs of success. Our ESG strategy continues to gain momentum across the business including developing sustainability-linked business loans and a green mortgage product as we look to further embed sustainability across everything we do. This lays the foundation for efficient, sustainable growth of deep, long-lasting customer relationships.

We are cautiously optimistic about the improving outlook as the impact of the vaccination programme in the UK delivers positive revisions to economic expectations. We're continuing to manage through what is still an uncertain economic backdrop, but the bank is well placed, with a strong balance sheet, and through ongoing strategic delivery we have a clear path to long-term, improved sustainable returns."

Significantly stronger financial performance in H1

- Returned to statutory profit, with underlying profit more than doubling YoY to £245m (H1 2020: £120m) given significantly lower impairment charge; underlying RoTE improved to 10.1% (H1 2020: 4.6%)
- Income 9% lower YoY saw pre-provision operating profit decline to £283m, although this recovered by 4% compared to H2 2020:
    - H1 NIM declined 6bps YoY to 1.56% but with improved momentum as Q2 increased to 1.60%; continued deposit repricing and mix benefit, and stronger mortgage spreads more than offset lower hedge income and higher liquidity
    - Deposit costs now 61bps (FY20: 90bps) underpinning overall cost of funds reduction compared to FY20
    - Subdued non-interest income of £66m primarily reflects low activity; expected to improve with the easing of lockdown and as broader economic activity rebounds
- Operating costs of £460m reduced 1% YoY but remained stable in the half as cost savings were offset by one-off costs and the impact of higher investment; expect stronger H2 reduction given benefit of transformation savings and lower investment
- Low impairment charge of £38m (11bps cost of risk) given continuing support reducing the impact on customers; updated macroeconomics and limited specific provisions or changes in portfolio asset quality metrics in the period
- Statutory profit before tax of £72m after deducting £173m of exceptional items: £49m of integration & transformation costs, £47m of acquisition accounting unwind, £71m of conduct charges (£59m related to PPI, including charge taken in Q1); working towards closing down PPI programme
- Prudent volume management saw a stable loan book at £72.2bn:
    - Stable mortgages balances at £58.3bn with volumes carefully managed through an uncertain backdrop, prioritising margin over volume
    - Business lending declined 0.6% to £8.9bn which includes £1.4bn of government-guaranteed lending
    - Personal lending declined 3.2% to £5.1bn due to subdued customer demand across the market
- Deposits grew 1.5% to £68.5bn; strong relationship deposits growth of 12% to £28.7bn across both consumers and businesses
- Restarted structural hedging programme: c.£25.9bn of eligible liabilities now >95% re-invested since March; avg. yield c.0.3%; No impact on unwound hedge NII profile

Prudent balance sheet well positioned for an uncertain outlook

- Maintained considerable credit provisions of £721m (FY20: £735m); total coverage ratio of 1.00% (FY20: 1.02%)
- Fully updated economic scenarios: remain cautiously positioned despite greater optimism in recent economic data
- Arrears across most portfolios increased from subdued FY20 levels but remain at low levels
- Low remaining payment holidays representing <1% of balances across mortgages & personal; vast majority returned to payments
- Robust capital base: transitional CET1 ratio strengthened to 14.4% or 13.9% excluding software intangible benefit:
    - Improved 99bps in the half driven by stronger profitability and limited RWA inflation to date
    - Significant c.£1.3bn management buffer above regulatory minimum of 9.2%; CET1 ratio 13.2% on fully loaded basis

Good progress on strategic execution

- Innovative propositions launched: Brighter Money bundles campaign drove >90% increase in monthly PCA sales vs H2 20; c80k total sales in H1; 100k credit card cashback signups; re-launched BCA with Working Capital Health solutions to launch in H2
- Laying the foundations for future growth: rebranding substantially complete; expanded digital distribution capability with c.90% of Personal sales now digital; Mortgage APIs now integrated across c.6k brokers
- Building long-term customer loyalty: Virgin Red programme pilot launched - ability to earn and spend Virgin Points, significant customer opportunity; Virgin Money Rewards positively received, reflected in strong customer advocacy
- Momentum on ESG agenda: Improved Board-level gender diversity; leading edge initiatives on the Poverty Premium; reducing operating emissions; progressing climate scenario analysis and TCFD disclosure; sustainable product development underway

Outlook and guidance

- Net interest margin expected to be around 160bps for FY21
- Structural hedge programme restarted: Expected benefit to NII of c.£25m in FY21; c.£60m of benefit in FY22
- Underlying operating expenses expected to be <£890m in FY21 reflecting the impact of COVID restrictions and updated phasing; committed to long-term cost reduction and will provide a further update on incremental cost opportunities from digital transformation alongside FY21 results
- Cost of risk expected to be subdued in the near term through FY21
- CET1 ratio expected to continue to exceed 13% (excluding software intangible benefit) at FY21
- SST outcome in December and impairment outlook will be key inputs into our approach to considering dividends; expect a further update on our capital framework post-SST
- Clear path to delivering double digit statutory returns on tangible equity in the medium term

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Virgin Money UK PLC will today be hosting a presentation for analysts and investors covering the 2021 interim financial results starting at 08:30 BST (17:30 AEST) with a pre-recorded presentation followed by live Q&A call:

https://webcast.openbriefing.com/vmuk-interim21/

A recording of the webcast and conference call will be made available on our website shortly after the meeting at:

https://www.virginmoneyukplc.com/investor-relations/results-and-reporting/financial-results/

A call for fixed income investors will be held at 09:00 BST on Friday 7 May 2021: Dial-in details: UK: 0800 640 6441; All other locations: +44 20 3936 2999; Access code: 983095

Financial performance - underlying basis

Summary income statement

	6 months to 31 Mar 2021 £m	6 months to 31 Mar 2020 £m	Change %	6 months to 30 Sep 2020 £m	Change %
Underlying net interest income (NII)	**677**	702	(4)	649	4
Underlying non-interest income	**66**	115	(43)	76	(13)
Total underlying operating income	**743**	817	(9)	725	2
Underlying operating and administrative expenses	**(460)**	(465)	(1)	(452)	2
Underlying operating profit before impairment losses	**283**	352	(20)	273	4
Impairment losses on credit exposures	**(38)**	(232)	(84)	(269)	(86)
Underlying profit on ordinary activities before tax	**245**	120	104	4	n/a
- Integration and transformation costs	**(49)**	(61)	(20)	(78)	(37)
- Acquisition accounting unwinds	**(47)**	(57)	(18)	(56)	(16)
- Legacy conduct costs	**(71)**	-	n/a	(26)	173
- Other items	**(6)**	(9)	(33)	(5)	20
Statutory profit/(loss) on ordinary activities before tax	**72**	(7)	n/a	(161)	n/a
Tax credit/(charge)	**8**	29	(72)	(2)	n/a
Statutory profit/(loss) after tax	**80**	22	264	(163)	n/a

Key performance indicators(1)

	6 months to 31 Mar 2021	6 months to 31 Mar 2020	Change	6 months to 30 Sep 2020	Change
Profitability:					
Net interest margin (NIM)	**1.56%**	1.62%	(6)bps	1.49%	7bps
Underlying return on tangible equity (RoTE)	**10.1%**	4.6%	5.5%pts	(3.5)%	13.6%pts
Underlying cost to income ratio (CIR)	**62%**	57%	5%pts	62%	-%pts
Underlying return on assets	**0.47%**	0.25%	22bps	(0.07)%	54bps
Underlying earnings per share (EPS)	**12.6p**	5.7p	6.9p	(4.3)p	16.9p

(1) For a definition of each of the KPIs, refer to ‘Measuring financial performance – glossary’ on pages 257 to 258 of the Group's 2020 Annual Report and Accounts. The KPIs include statutory, regulatory and alternative performance measures. Where applicable certain KPIs are calculated on an annualised basis for the periods to 31 March.

Financial performance - underlying basis

Key performance indicators (continued)

As at:	31 Mar 2021	31 Mar 2020	Change	30 Sep 2020	Change
Asset quality					
Cost of risk[1]	**0.11%**	0.63%	(52)bps	0.68%	(57)bps
Total provision to customer loans	**1.00%**	0.75%	25bps	1.02%	(2)bps
Indexed loan to value ratio (LTV) of mortgage portfolio[2]	**55.2%**	57.1%	(1.9)%pts	57.3%	(2.1)%pts
Regulatory Capital:					
Common equity tier 1 (CET1) ratio (IFRS 9 transitional)	**14.4%**	13.0%	1.4%pts	13.4%	1.0%pts
CET1 ratio (IFRS 9 fully loaded)	**13.2%**	12.4%	0.8%pts	12.2%	1.0%pts
Total capital ratio	**21.2%**	19.5%	1.7%pts	20.2%	1.0%pts
Minimum requirement for own funds and eligible liabilities (MREL) ratio	**29.3%**	25.6%	3.7%pts	28.4%	0.9%pts
Capital Requirement Directive IV (CRD IV) leverage ratio	**5.2%**	4.4%	0.8%pts	4.8%	0.4%pts
UK leverage ratio	**5.2%**	4.9%	0.3%pts	4.9%	0.3%pts
Tangible net asset value (TNAV) per share	**257.5p**	252.5p	5.0p	244.2p	13.3p
Funding and Liquidity:					
Loan to deposit ratio (LDR)	**105%**	113%	(8)%pts	107%	(2)%pts
Liquidity coverage ratio (LCR)	**151%**	139%	12%pts	140%	11%pts
Net stable funding ratio (NSFR)	**134%**	129%	5%pts	131%	3%pts

(1) Cost of risk is calculated on an annualised basis.
(2) LTV of the mortgage portfolio is defined as mortgage portfolio weighted by balance.

Summary balance sheet

	As at		
	31 Mar 2021 £m	30 Sep 2020 £m	Change %
Customer loans	**72,211**	72,457	(0.3)
of which Mortgages	***58,270***	*58,290*	-
of which Personal	***5,050***	*5,219*	*(3.2)*
of which Business	***8,891***	*8,948*	*(0.6)*
Other financial assets	**15,884**	15,608	1.8
Other non-financial assets	**2,044**	2,194	(6.8)
Total assets	**90,139**	90,259	(0.1)
Customer deposits	**68,538**	67,511	1.5
of which relationship deposits[1]	***28,744***	*25,675*	*12.0*
of which non-linked savings	***21,506***	*20,729*	*3.7*
of which term deposits	***18,288***	*21,107*	*(13.4)*
Wholesale funding	**13,289**	14,227	(6.6)
Other liabilities	**3,232**	3,589	(9.9)
Total liabilities	**85,059**	85,327	(0.3)
Ordinary shareholders' equity	**4,165**	4,017	3.7
Additional Tier 1 (AT1) equity	**915**	915	-
Equity	**5,080**	4,932	3.0
Total liabilities and equity	**90,139**	90,259	(0.1)
Risk Weighted Assets (RWAs)	**24,152**	24,399	(1.0)

(1) Current account and linked savings balances

Chief Executive Officer's statement

Laying the Foundations for growth

"Virgin Money had a strong first half. We doubled underlying profit compared to last year and returned to statutory profit. The quality of our loan book remained resilient in the period, and we've continued to support customers and look after our colleagues and communities, while safeguarding the bank. We've made significant strategic progress to transform Virgin Money into a leading digital bank and our rebranding is largely complete. We've launched a range of innovative and compelling Virgin Money personal and business products as well as differentiated loyalty offers, which are showing early signs of success. Our ESG strategy continues to gain momentum across the business including developing sustainability-linked business loans and a green mortgage product as we look to further embed sustainability across everything we do. This lays the foundation for efficient, sustainable growth of deep, long-lasting customer relationships.

We are cautiously optimistic about the improving outlook as the impact of the vaccination programme in the UK delivers positive revisions to economic expectations. We're continuing to manage through what is still an uncertain economic backdrop, but the bank is well placed, with a strong balance sheet, and through ongoing strategic delivery we have a clear path to long-term, improved sustainable returns." **David Duffy, CEO**

Dear stakeholder,

Our business performance has been encouraging during the first half of the year against a currently challenging but improving economic backdrop. Ensuring that we support customers through the pandemic, provide flexibility for our colleagues, and deliver for the communities in which we operate, continue to be key priorities for the bank. Alongside a stronger financial performance with underlying profit more than doubling and a return to statutory profit, we have also driven significant strategic execution through the period. We now have a substantially rebranded set of distribution channels, a series of innovative, new propositions for customers and early signs of improved customer advocacy as we move into the next phase of our journey to becoming a digital bank. The rollout of the UK vaccination programme has given the country an exit route from the restrictions of the pandemic, although there may still be implications for customers once the current levels of support for the economy are removed. We have made substantial progress in the period on the key drivers of our strategy, and there's more to follow over the remainder of the year. While we have managed volumes carefully through the pandemic, we are well placed to exit lockdown with growing strategic momentum as we continue to support all our stakeholders.

Stronger financial performance against an improving backdrop

I am pleased to report an improvement in the financial performance of the Group during the first half of the year as impairments fell significantly compared to the elevated levels seen in response to the deterioration in the macroeconomic outlook last year. Underlying profit before tax more than doubled in the period to £245m (H1 2020: £120m), with a return to statutory profit before tax of £72m.

Lending volumes remained broadly stable as we deliberately managed our portfolios carefully through an uncertain period, focusing on customer support, loan quality and delivering the improved returns that will drive long-term profitable growth. Deposit balances increased 1.5%, driven by growth in lower-cost relationship deposit balances which increased 12% in the period.

The lower rate environment and a subdued economic backdrop given UK lockdown restrictions saw income down 9% year-on-year, although with signs of recovery from H2 2020, with a 2% improvement half-on-half. NIM has improved through the period, rising from 152bps in Q4 2020 to 160bps in Q2 2021 and resulting in an overall NIM for H1 2020 of 156bps. The combination of deposit repricing and a shift in mix towards lower-cost relationship deposits more than offset lower lending yields and the drag of additional liquidity. Other income remained subdued given the impacts of the most recent restrictions on UK economic activity and customer spending.

Costs were controlled, down 1% compared to the same period last year, but stable when compared to H2 2020 as the cost savings delivered by our transformation programme were offset by higher one-off costs and higher investment that will underpin our cost delivery in to H2 and beyond. We remain focused on delivering the cost savings of our transformation programme, although additional UK lockdown restrictions have meant a delay in the delivery of our plans and we now expect H2 costs of <£430m leading to total costs for FY21 of <£890m, with a strong exit rate into FY22.

Asset quality remained resilient in the period. The successful rollout of the vaccination programme together with ongoing customer support continue to inform improving economic forecasts. Gross Domestic Product (GDP), unemployment and house prices are all performing better than initially feared. Despite this, whilst there is scope for increased optimism, we remain cautious in the near term until the impact of the removal of government support becomes clear.

Overall provisions at H1 of £721m were equivalent to a coverage level of 100bps, broadly stable on our position at FY20. Together with the improved economic outlook, this led to the low impairment charge of 0.11% taken in the period.

Chief Executive Officer's statement

Accelerating our digital ambition

Our strategy outlined at Capital Markets Day in 2019 set out our ambition to become a purpose-led digitally-focused bank over time. The lessons learned over the past year have reaffirmed that intention is the right one, and the need to accelerate our digital agenda. Across our business three major themes to emerge from the COVID-19 pandemic have been: increased levels of digital engagement from customers, higher numbers of colleagues aspiring to work remotely, and improved technology optionality. By accelerating our digital ambitions we will not only deliver a better experience for our customers and colleagues but it will also support a reduction in costs over time.

The way customers engage with us has changed over the past year. Increasingly they're choosing to interact with us through digital channels. As digital adoption levels increase and more customers use self-managed processes, there's consequentially lower branch footfall and reduced cash usage. Our business customers have increasingly been using technology to improve their productivity and we're focused on supporting their preference. Our successful and growing fintech partnerships will allow us to provide insights and analytics in a way that will be industry-leading, providing a great customer experience.

From a colleague perspective, with c.6k colleagues working from home, and following employee feedback we're implementing a predominantly remote working model. Our “Life More Virgin” approach will offer colleagues the flexibility to work remotely, on a sustainable basis, with offices increasingly being used as hubs for collaboration and innovation, providing greater flexibility in our property footprint over time.

Finally, the pandemic has highlighted that technology solutions can be delivered in days, rather than weeks and months, and we remain determined to leverage that capability to drive additional efficiency improvements. With customer expectations rising it's important we make sure we focus on the opportunity to go further and faster. Delivering an automated and digitised customer journey will support better customer experience and improved efficiency.

In the near term, we remain focused on delivering further efficiencies and whilst we've rephased some of the FY21 cost reductions as a result of COVID-19, we're committed to delivering these in H1 2022. Longer term, the acceleration of our digital transformation will deliver further cost savings. The overall potential is something we're currently analysing carefully in the context of investment needed in the business. We'll give more detail alongside our full year results but what's clear is that accelerating our delivery represents a strong opportunity for further cost savings in the coming years.

Laying the foundations for future customer growth

Despite the impacts of COVID-19, we have good momentum in the business and have made progress in laying the foundations for our future customer growth. During the first half, we delivered strong improvements in our digital sales capability and c90% of personal sales are now through digital channels with a rising proportion of business banking sales as well. This continued increase in our digital sales channels will be key to our success over the coming years.

The vast majority of our stores are now rebranded, and most new sales are now also being completed under the Virgin Money brand. In total over >95% of new personal current account (PCA) sales and all new business current account (BCA) sales in business banking are now completely rebranded. We're also increasingly incorporating Virgin lifestyle propositions. Our Brighter Money Bundles, which partner with other Virgin companies, have seen a positive initial reaction with PCA sales >90% higher compared to H2 2020, delivering a total of c.80k in the period. Cashback credit cards have already seen 100k sign ups and we'll continue to expand and develop these propositions over the coming months.

Alongside our own proposition developments, we've also continued to expand our fintech partnership model in the half. We have a number of existing retail fintech partnerships, but more recently we've signed 7 new fintech partnerships within Business and are targeting 20 partnerships by 2022. Leveraging the additional capabilities will be a key element of our Working Capital health proposition to be launched in H2 for SMEs. This will provide unique analysis for business owners giving them access to real-time cash flow data, account tracking and insights. Using the power of our fintech partners, we're not just allowing SMEs to take control of their finances, but we're also staying true to the entrepreneurial spirit of the brand.

In Mortgages, our new application programming interfaces (APIs) have now been rolled out to c.6k mortgage brokers, offering them significant time efficiencies. As we come to the end of the testing phase there has already been a positive initial reaction. We have also seen a good response to our Mortgage Home Coach app, with 22k downloads to date and we see good signs of the potential to generate significant additional lending from the app over time.

Chief Executive Officer's statement

Building long term customer loyalty

Alongside the significant development in our propositions and our distribution channels, we've continued to focus on developing our loyalty strategy to support our future growth ambitions. The core Virgin Group loyalty programme Virgin Red, which offers users the ability to earn and spend points inside and outside the Group, was launched in February and is expanding rapidly. Whilst still a soft launch, the Virgin Red app already has over 100k users, with plans to grow to over 1m within a year of its launch. The opportunity to switch to a Virgin Money PCA has already launched through the app, with a good early reception from customers who are able to earn 15,000 Virgin Red points for switching. We continue to explore this and other opportunities to target the c.17m Virgin Group UK customer relationships with a known affinity for the Virgin brand.

We have also had strong early success with our Virgin Money Rewards and we'll continue to focus on further developing these. This will include refreshed Brighter Money Bundles offers and expanding cashback opportunities, with more to follow as we'll be launching in-app rewards in H2 and continuing to develop and expand our loyalty schemes. The potential to expand further across our other products such as debit cards and to businesses, as well as offer rewards from a growing number of companies within and outside the Virgin Group, is something to be explored over time.

The opportunities from a compelling loyalty strategy across both Virgin Red and our own Rewards will support our growth ambitions over the coming years. Delivering lower acquisition costs and ongoing value for customers will be key in delivering deeper, and more valuable, customer relationships over the coming years.

Adapting our leadership to our digital transformation agenda

I wish to welcome our new CFO Clifford Abrahams to the Group; I am delighted he has chosen to join us and he is already having a big impact. I look forward to working with him to deliver our agenda in the years ahead. I should also like to take this opportunity to thank Enda Johnson, who had been acting as interim CFO since Autumn 2020, for taking on that role during the last few months, as well as for his significant contribution to the Group since 2015.

I am also pleased that we have been able to welcome Elena Novokreshchenova to the Board, bringing her unique mix of banking, technology and customer-centric leadership experience from an international career spanning 20 years. Elena's appointment helps ensure the Board has the right mix of skills to help us deliver our digital ambitions.

As the Group accelerates its digital agenda, developing digital solutions, with one product set, on a single platform, and a unified customer experience will be key. Developing strategic data, artificial intelligence, cloud and partnership capabilities will become core competencies in time. To ensure we deliver these I've created a new role of Chief Digital and Innovation Officer to focus on the delivery of our planned digital propositions for both customers and colleagues and have appointed Fraser Ingram to the position.

The success of a digital bank will be defined by the experience it creates for customers both on acquisition and throughout the lifecycle of that product. Our customers' expectations are rising on all fronts. To ensure we deliver against those expectations, I have created a new Chief Customer Experience Officer role within my Leadership Team, responsible for the design and delivery of a brilliant, purpose-led customer experience. Fergus Murphy has taken up this role and is working closely with Fraser.

Finally, I've taken the opportunity to bring together all commercial aspects of our existing customer propositions, under a newly created role of Chief Commercial Officer. This role is responsible for ensuring that our products and propositions are customer-focused and competitive in the market while achieving the required return for our investors. We have commenced an external recruitment process for this role, but I am pleased to say Hugh Chater has taken on this role on an interim basis.

The extent of our digital ambition is clear and configuring our leadership to this new future will help us to deliver on our strategic ambition to disrupt the status quo.

Building momentum in delivering our Environmental, Social and Governance (ESG) ambitions

The pandemic has highlighted the interconnections between business and society and that successful brands must demonstrate the value they add to all stakeholders – customers, employees, shareholders and broader society.

Virgin Money continues to develop its ESG agenda and, after laying out the key elements of our strategy at our FY20 results, we are already seeing some early signs of success. From a climate perspective, we have put our carbon foot down, with the latest data (six months to December 2020) showing a 14% reduction in operational (scope 1 and 2) emissions compared to the previous six-month period. This gives us a Greenhouse Gas intensity ratio of 1.50 for the period, down from the 1.70 reported at FY20. From 1 April 2021, all the energy that the Bank is responsible for supplying is renewably sourced following a switch to biogas which will save an estimated 9 tonnes of carbon per day.

Chief Executive Officer's statement

Building momentum in delivering our Environmental, Social and Governance (ESG) ambitions (continued)

As we look to build a brighter future, we are developing a product framework that will help customers make a positive impact on society and the environment. In the period we launched a pilot scheme for our Business customers in the agricultural sector to undertake carbon audits and became one of the first banks in Europe to rate counterparties based on ESG across companies of all sizes. This will enable us to offer sustainability-linked loans in the second half which will reduce the cost of finance for businesses whose core activities proactively help the economy transition to a more sustainable model. Later in the year we'll also follow this with the launch of our green mortgage framework designed to support customers in making green choices around their home. Finally, our latest Brighter Money bundles offer, which supports Personal customers to donate £50 to a charity of their choice, has raised over £180k for good causes to date.

We also look to open doors for customers, colleagues and communities through our activities. We are stepping up our efforts to ensure no Virgin Money customer pays a Poverty Premium, launching a call to action in the first half and identifying c.21k customers at risk of paying an energy premium who we will commence contact with in the second half. We are also actively migrating existing PCA customers to our best accounts with more favourable terms.

We firmly believe that successful organisations need a diverse and inclusive workforce. We improved our Board diversity balance to 33% in the period, and improving diversity remains a key priority for the Group. We are also focused on accelerating our Black, Asian and Ethnic minority diversity strategy and we'll say more about our revised targets at year end.

We are also committed to 'Straight-up ESG', aligning our strategic goals to ESG and embedding an ESG focus across the business while improving our disclosure and further developing our targets. We are planning to roll out ESG training for Board, Leadership and all colleagues in the second half, develop further role-specific training, and have embedded ESG considerations in our business case templates. In the second half, we will focus on developing our climate impact modelling capability and continuing the development of our Task Force on Climate-related Financial Disclosures (TCFD) disclosures which we will update on at the full year.

Outlook

Over the first half of the year, we've deliberately controlled growth as we managed carefully through the pandemic and our overriding priorities remain the health and economic well-being of our customers, colleagues and communities while safeguarding our bank. We've had a strong first half, achieving a number of strategic milestones, including substantially completing the rebranding activity of all physical channels and delivering innovative new propositions across all key customer sets, and there's more to come in the second half as we launch additional propositions and continue improving the digital customer experience. As we exit from COVID-19 restrictions, we aim to do so with high momentum in our strategic delivery and all the foundations in place to support sustainable future growth based on deep customer relationships.

The Group's financial performance has improved significantly with lower impairment charges, better capital ratios and a stronger NIM outlook for the year. We remain disciplined and are cautiously optimistic as we wait to see how the economic backdrop evolves after the removal of government support into our next financial year. We continue to analyse how we adapt to the shift in customer preferences for digital channels and our colleagues' needs for flexibility with potential opportunities around physical presence. We are also looking at ways in which we can leverage fintech partnership capabilities further within a tight investment envelope, and we'll provide more detail around the potential cost opportunities of our digital transformation alongside full year results.

Whilst we remain alert to the needs of customers as we exit the pandemic, it has been a good first half for the Group and I'm proud of all the hard work from our colleagues. We continue to have the right strategy and are executing on the key pillars that will underpin our delivery of improved returns and profitable growth over the coming years as we fulfil our ambition to Disrupt the Status Quo of the UK banking market.

David Duffy, Chief Executive Officer - 4 May 2021

Driving sustainable improvements in returns

"Underlying profit more than doubled in the period, with good financial momentum across the business. While the backdrop remains uncertain, the Group remains focused on delivering the key pillars of our strategy which are the foundations of driving improved returns and then profitable growth, in the medium term." **Clifford Abrahams, Group CFO**

Financial Highlights

Statutory profit before tax	Underlying profit before tax	Underlying RoTE
£72m	£245m	10.1%
H1 2020: £(7)m	H1 2020: £120m	H1 2020: 4.6%

NIM	Underlying CIR	Cost of risk
1.56%	62%	11bps
H1 2020: 1.62%	H1 2020: 57%	H1 2020: 63bps

CET1 ratio	Loan growth	Relationship deposit growth
14.4%	(0.3)%	+12.0%
2020: 13.4%	H1 2020: +0.3%	H1 2020: +4.3%

Chief Financial Officer's review

Strategic pillars to deliver shareholder value over time

In my first report as CFO of Virgin Money, I'm pleased to note the Group has continued to make good progress with a strong set of financial results, ongoing strategic delivery, and that it remains well positioned as the UK looks to exit the pandemic, all of which has been delivered against a challenging external backdrop. My initial impressions on joining the Group have been very positive and I'd like to thank my colleagues for their warm welcome.

Despite the impacts of COVID-19 we've continued to deliver the strategy laid out at the Capital Markets Day and as we move towards a more normalised environment, the Group's strategy continues to be the right one. Delivering on our four strategic pillars – Super Straight-forward Efficiency, Delighted Customers and Colleagues, Discipline and Sustainability, and Pioneering Growth – remains key. We have a clear roadmap to double digit statutory returns and then profitable growth, which will deliver increased shareholder value over the coming years.

Demonstrating resilience through COVID-19

In the near term, the Group's focus remains on managing the business carefully as the UK exits the pandemic. The balance sheet is resilient, we have a strong capital position, and there is improving momentum in the financials. Credit provision coverage was stable at 1.00% in the period, and to date we've seen limited specific provisions or material signs of deterioration in asset quality across any of our portfolios. Capital strengthened in the period, with the transitional CET1 ratio improving c.100bps to 14.4% (13.9% excluding software intangibles benefit) and we now have c£1.3bn of management buffer over the Group's regulatory requirement. Pleasingly, the key driver of that improvement was stronger profitability as the Group returned to statutory profit. We remain focused on delivering the Group's inaugural participation in the Solvency Stress Test (SST) run by the Prudential Regulation Authority (PRA) later this year.

Continuing to transform the bank

As we exit the pandemic, the Group must maintain focus on transforming the bank as we move into FY22. The Group has a good track record of reducing costs since IPO, but we need to maintain that focus and redouble efforts to ensure that we continue to drive greater efficiencies as we deliver the transformation agenda. We are assessing the potential for further cost reduction as we progress our journey towards becoming a digital bank, but we will balance this carefully against the restructuring costs and investment needed. We'll talk more about the opportunities at full year.

The business has made good progress this year on improving its funding cost, reducing its cost of deposits by 29bps in the period compared with FY20, and the overall cost of funds by 28bps over the same period. A continued focus on optimising the cost of funds will support the drivers of an improved statutory RoTE and strengthen CET1 generation. This provides the support for the Group's future growth ambitions and progressive dividends over time.

Building an exciting, growth-led future

As RoTE and capital generation improve, we have a clear roadmap to an exciting growth-led future that becomes a focus for FY22 and beyond. The early customer reaction to our completed rebranding activity is encouraging for our future growth prospects. Combined with stronger digital advocacy levels, and our focus on delivering a low cost-to-serve, there are substantial opportunities for us.

Relationship deposit growth has been strong year-to-date as customers save more and businesses carry additional liquidity. Longer term these relationship deposits will continue to be a key area of focus for the Group, underpinning NIM and providing a low-cost base for above market asset growth over time. The launch of our Brighter Money Bundles proposition in the PCA market saw c80k sales in H1, and the relaunch of our newly rebranded Virgin Money BCA will continue to support the delivery of a stronger NIM as we grow our funding cost-effectively and expand our lending profitably. The improvement in returns will position the Group well for future growth, alongside consistent capital generation and the establishment of ongoing dividends, and I'm looking forward to helping drive the business towards those ambitions.

Significantly stronger financial performance in H1

Against a tough external backdrop, the Group delivered an underlying profit in H1 of £245m, a significant improvement compared to last year and supporting an improvement in underlying RoTE to 10.1% (H1 2020: 4.6%). NIM of 1.56% (H1 2020: 1.62%) was lower year-on-year due to the lower rate environment, but showed momentum through the period, with the second quarter NIM increasing to 1.60%. Subdued non-interest income of £66m was 43% lower year-on-year driven by the non-repeat of gilt sales, the impact of the high cost of credit review and lower activity levels. Total income declined 9% compared to a year ago, although the improved margin backdrop underpinned a 2% improvement when compared to H2 2020. Operating costs were 1% lower compared to H1 2020 and we expect to see an improvement in the second half of the year. The reduction in income resulted in a 5%pts increase in the cost: income ratio to 62% and drove a 20% reduction in pre-provision profit, year-on-year. However, despite the impact on pre-provision earnings, the reduction in impairment charges was significant, falling 84% to £38m compared to H1 2020 resulting in a cost of risk of 11bps and driving a more than doubling of underlying profit before tax.

The Group also returned to statutory profit in the period delivering £72m before tax after deducting £173m of exceptional items including £49m of restructuring charges, £47m of acquisition accounting unwind, £71m of legacy conduct costs primarily relating to payment protection insurance (PPI), and £6m of other charges.

Chief Financial Officer's review

Resilient balance sheet with robust capital, liquidity and funding position

The Group maintained a conservative balance sheet position with stable credit provisions totalling £721m (FY20: £735m) equivalent to a coverage ratio of 1.00% (FY20: 1.02%). The Group continues to have a defensive portfolios comprising 81% low-risk mortgages, 12% business lending and 7% in our high-quality, affluence-focused unsecured book. The Group had already adopted a prudent set of economics in the fourth quarter of 2020 and these have been fully refreshed in the period. Whilst latest data provides some optimism in the outlook, the Group is maintaining a cautious stance on the ultimate impact and consequently held provision coverage broadly stable.

During the period, prudent balance management held lending volumes stable at £72.2bn. Deposit balances rose 1.5% to £68.5bn driven by 12% growth in relationship deposits as retail customers saved more and businesses opted to maintain higher levels of liquidity given the uncertain economic backdrop. The CET1 ratio improved to 14.4% (or 13.9% excluding software intangible benefit), benefiting from the stronger profitability and limited RWA inflation to date. The Group continues to prepare for our inaugural participation in the SST exercise run by the PRA with the results published later in the year.

Outlook

Despite the impact of COVID-19, we have made good progress on driving our strategy, which remains the right one to deliver value for investors over time. Whilst this year is primarily about maintaining resilience through the pandemic, we are focused on digitally transforming the business, as we work hard to further reduce costs. The completion of the transformation agenda alongside the reduced deposit costs and momentum on new propositions will be key enablers of the Group delivering double-digit statutory returns. With all the elements in place, the Group has an exciting growth-led future as strengthened customer advocacy and loyalty, combined with improved digital capability, allow strong profitable growth at low incremental costs. We have the right building blocks in place, and it has been a good first half for Virgin Money.

Underlying income

	6 months to 31 Mar 2021 £m	6 months to 31 Mar 2020 £m	Change	6 months to 30 Sep 2020 £m	Change
Underlying net interest income	**677**	702	(4)%	649	4%
Underlying non-interest income	**66**	115	(43)%	76	(13)%
Total underlying operating income	**743**	817	(9)%	725	2%
NIM	**1.56%**	1.62%	(6)bps	1.49%	7bps
Average interest-earning assets	**87,134**	86,847	-	86,885	-

Overview

Operating income of £743m was 2% higher compared to H2 2020, although 9% lower than H1 2020. The effects of the pandemic impacted the H2 2020 results and whilst year-on-year income remained lower there was some improvement in the first half. In that context, NII declined 4% compared to H1 2020 to £677m as NIM reduced 6bps to 1.56%. Despite the reduction, there was increased momentum through the period as NIM improved from 1.52% in Q4 2020 to 1.60% in Q2 2021. Other income of £66m was 43% lower compared to H1 2020 driven by the impact of the High Cost of Credit Review, lower activity levels and the non-repeat of gilt sales.

NII and NIM

Asset yields declined 42bps compared to H1 2020 with headline mortgage pricing, where yields declined 16bps, the primary contributor. The Group remained selective in terms of participation in the market in the first half, with lower average balances also driving a reduction in NII.

In Business, a 74bps reduction in yields was driven by mix impact as new volumes were primarily lower-yielding government-backed lending. The strong average balance sheet growth associated with this was more than offset by the lower yield.

In Personal, average balances remained stable relative to H1 2020, while yields contracted 93bps. The key driver of the reduction compared to H2 2020 was the credit card book which was impacted by mix changes as customers paid down higher-yielding unsecured balances. Elsewhere, the average yield on the Group's liquid assets fell 60bps reflecting the lower rate environment.

Liability rates also decreased 39bps relative to H1 2020, with the reduction driven broadly across lower savings costs, lower term deposit costs and reduced wholesale funding costs. Consumer and business pandemic-related deposit growth saw an increase in average balances across lower-cost current accounts and savings products. Term deposits fell as a proportion of the book and were also 27bps cheaper, while savings costs almost halved in the period to 48bps (H1 2020: 94bps), both reflecting the impact of the lower rate environment and repricing activity. Wholesale funding costs declined in the period, driven by a reduction in average balances following the Group's initial Term Funding Scheme (TFS) repayments, and the continued optimisation of overall funding.

Chief Financial Officer's review

NII and NIM (continued)

Following the Bank of England's confirmation that negative interest rates are now explicitly within its policy toolkit, the Group has reinitiated its structural hedging programme. Balances of qualifying non-interest bearing liabilities have increased to £25.9bn with the Group expected to return to a fully hedged position early in H2; the Group anticipates a c£25m benefit in FY21 NII with a further c£60m of annualised benefit in FY22.

In FY21 we now anticipate a full year NIM of around 1.60%. This reflects continued momentum in deposit repricing and the benefit of a higher proportion of low-cost relationship deposits, optimisation of wholesale funding and structural hedge contributions partially mitigated by competitive pressure on asset yields.

Net interest income

	6 months ended 31 March 2021			6 months ended 31 March 2020		
Average balance sheet	**Average balance £m**	**Interest income/ (expense) £m**	**Average yield/ (rate)[1] %**	Average balance £m	Interest income/ (expense) £m	Average yield/ (rate)[1] %
Interest-earning assets:						
Mortgages	**58,303**	**673**	**2.32**	59,823	742	2.48
Personal lending	**5,344**	**194**	**7.26**	5,344	219	8.19
Business lending[2]	**8,916**	**149**	**3.34**	7,963	162	4.08
Liquid assets	**12,860**	**13**	**0.20**	11,982	48	0.80
Due from other banks	**1,707**	**-**	**(0.03)**	1,730	4	0.44
Swap income/other	**-**	**(55)**	**n/a**	-	(20)	n/a
Other interest earning assets	**4**	**-**	**n/a**	5	-	n/a
Total average interest earning assets	**87,134**	**974**	**2.24**	86,847	1,155	2.66
Total average non-interest earning assets	**3,450**			3,416		
Total average assets	**90,584**			90,263		
Interest-bearing liabilities:						
Current accounts	**14,000**	**(4)**	**(0.06)**	11,748	(9)	(0.16)
Savings accounts	**29,284**	**(71)**	**(0.48)**	27,221	(128)	(0.94)
Term deposits	**19,892**	**(133)**	**(1.34)**	22,151	(178)	(1.61)
Wholesale funding	**13,767**	**(87)**	**(1.27)**	17,172	(136)	(1.59)
Other interest earning liabilities	**168**	**(2)**	**n/a**	179	(2)	n/a
Total average interest bearing liabilities	**77,111**	**(297)**	**(0.77)**	78,471	(453)	(1.16)
Total average non-interest bearing liabilities	**8,477**			6,986		
Total average liabilities	**85,588**			85,457		
Total average equity	**4,996**			4,806		
Total average liabilities and average equity	**90,584**			90,263		
Net interest income		**677**	**1.56**		702	1.62

(1) Average yield is calculated by annualising the interest income/expense for the period.
(2) Includes loans designated at fair value through profit or loss (FVTPL).

Chief Financial Officer's review

Non-interest income

Non-interest income declined £49m relative to H1 2020 to £66m but was much more aligned to H2 20 levels. The key drivers of the reduction compared to a year ago was the non-repeat of the £16m one-off gilt sales gain during H1 2020, a £9m impact from fair value movements, and £20m lower income in Personal. The £20m reduction in Personal fee income was driven by the impacts of restrictions on customer activity, including lower card fees with reduced transaction volumes and also the impact of the High Cost of Credit Review. Business fee income reduced by £3m relative to H1 2020, reflecting lower activity-based fees whilst Mortgage non-interest income was broadly stable.

Non-interest income remains linked to activity levels and is expected to improve with the easing of lockdown and broader economic rebound.

Costs

Operating and administrative expenses	**6 months to 31 Mar 2021 £m**	6 months to 31 Mar 2020 £m	Change	6 months to 30 Sep 2020 £m	Change
Personnel expenses	**164**	169	(3)%	167	(2)%
Depreciation and amortisation expenses	**81**	71	14%	68	19%
Other operating and administrative expenses	**215**	225	(4)%	217	(1)%
Total underlying operating and administrative expenses	**460**	465	(1)%	452	2%
Underlying CIR	**62%**	57%	5%pts	62%	-%pts

Overview

Underlying operating expenses reduced 1% relative to H1 2020 to £460m with the cost: income ratio increasing 5% pts to 62% compared with H1 2020 due primarily to the impact on income from the challenging operating environment. In the half year additional investment in cost saving programmes and one-off costs drove an increase compared to H2 2020 and more than offset cost savings from our transformation programme. The Group also had to delay some initiatives due to the UK lockdown measures introduced in late December 2020. Over the remainder of the year, stronger cost delivery will be underpinned by additional transformation programme savings and lower investment spend.

Given the rephasing of savings delivery the Group now expects FY21 costs to be <£890m. The Group remains committed to delivering cost reduction in the longer term and we'll provide a further update on the digital transformation opportunities alongside full year results.

Impairments

As at 31 March 2021	Credit provisions £m	Gross lending £bn	Coverage ratio bps	Net cost of risk[1] bps	% of loans in Stage 2	% of loans in Stage 3
Mortgages	**132**	**58.6**	**23**	**0**	**12%**	**1.2%**
Personal:	**293**	**5.4**	**603**	**107**	**18%**	**1.4%**
of which credit cards	*219*	*4.3*	*550*	*128*	*14%*	*1.4%*
of which personal loans and overdrafts	*74*	*1.1*	*839*	*9*	*34%*	*1.3%*
Business	**296**	**8.8**	**398[2]**	**26**	**40%**	**2.7%**
Total	**721**	**72.8**	**100**	**11**	**16%**	**1.4%**
of which Stage 2	*480*	*11.7*	*415*			
of which Stage 3	*101*	*1.0*	*1,032*			

(1) Cost of risk is calculated on an annualised basis.
(2) Government-guaranteed loan balances excluded for purposes of calculating the Business division coverage ratio.

As at 30 September 2020	Credit provisions £m	Gross lending £bn	Coverage ratio bps	Net cost of risk bps	% of loans in Stage 2	% of loans in Stage 3
Mortgages	131	58.6	23	16	14%	0.9%
Personal:	301	5.6	591	423	15%	1.2%
of which credit cards	*222*	*4.5*	*537*	*355*	*12%*	*1.2%*
of which personal loans and overdrafts	*79*	*1.1*	*824*	*721*	*28%*	*1.4%*
Business	303	8.7	391[1]	212	44%	3.2%
Total	735	72.9	102	68	18%	1.2%
of which Stage 2	*465*	*12.8*	*366*			
of which Stage 3	*134*	*0.9*	*1,574*			

(1) Government-guaranteed loan balances excluded for purposes of calculating the Business division coverage ratio.

Chief Financial Officer's review

Overview

The Group has maintained broadly stable total credit provisions at £721m (FY20: £735m) retaining appropriate levels of provision coverage across its portfolios, equating to an aggregate coverage level of 100bps (FY20: 102 bps).

The key macroeconomic inputs and weightings have been updated based on scenarios provided by our 3rd party provider Oxford Economics. Overall, the Group remains cautiously positioned but with less severe weightings than previously assumed, incorporating a 20% weighting to the Upside scenario, 50% to the Base scenario and 30% to the Downside. The weighted economic scenarios include a more significant recovery in GDP in 2022 of 6.7%, peak unemployment of 7.5% and a less severe 8% peak-to-trough decline in HPI.

To supplement the models, the Group also applied expert credit risk judgement through PMAs. These are designed to account for factors that the models cannot incorporate, where the sensitivity is not as would be expected under what is an unprecedented economic stress scenario. Through this process, the Group applied PMAs of £222m (FY20: £186m) which are deemed to be balanced and appropriate for our portfolio at the current time.

The model updates and overlays have resulted in limited portfolio stage migration, with loans classified as Stage 2 reducing marginally from 18% of the portfolio to 16% at H1 2021. Although this is higher relative to pre-pandemic levels, 97% of Stage 2 lending balances remain <30 days past due (DPD) and the stage migration seen to date through the pandemic largely reflects the modelled PD migration impact from the economic updates and overlays applied.

The Group has broadly maintained its provision coverage levels across all portfolios. In Mortgages, the coverage ratio of 23bps is deemed appropriate for the conservative loan book. The mortgage portfolio continues to evidence strong underlying credit performance, with no notable deterioration in asset quality.

Our Personal lending book coverage ratio of 603bps includes 550bps of coverage for our high-quality credit card portfolio which focuses on more affluent customers, and 839bps of coverage for our smaller personal loans and overdrafts book. Balances fell over the period as tighter lending criteria and muted customer demand reduced new originations. Arrears levels remain modest across the portfolio and the reduction in the book drove a small increase in the coverage level which increased 12bps over the period.

In Business, the coverage ratio of 398bps reflects a 7bps increase in the period. There has been no deterioration in underlying asset quality performance and, as yet, no significant increase in specific provision recognition. The lending book continues to be biased away from sectors likely to experience more disruption such as hospitality and retail, towards sectors expected to be resilient, such as agriculture and health and social care.

Payment holidays

The Group continues to support its Mortgage, Personal and Business customers through this difficult time with payment holidays where appropriate, although the level of new requests has reduced significantly. Across the Mortgage, Credit Cards and Personal loan portfolios we have only c.1% of portfolio balances still on a payment holiday and of those payment holidays that have matured the vast majority of customers have returned to payments. The key payment holiday statistics are set out below.

Payment holiday status

Product	Total balances of payment holidays granted to date	Representing % of balances	Total balances of payment holidays still in force	Representing % of balances	% of matured payment holiday customers returning to payment	% of matured payment holiday customers requiring support or in arrears
Mortgages	£12.3bn	21%	£377m	1%	94%	6%
Credit Cards	£267m	7%	£28m	1%	87%	13%
Personal Loans	£120m	14%	£5m	1%	90%	10%

Outlook

Overall, with muted levels of pandemic related defaults and impairments to date and prudent coverage levels, the Group continues to be resiliently positioned. The cost of risk is expected to remain subdued in the near term through FY21 given continued economic support.

Chief Financial Officer’s review

Exceptional items and statutory profit

	6 months to		
	31 Mar 2021 £m	31 Mar 2020 £m	30 Sep 2020 £m
Underlying profit on ordinary activities before tax	**245**	120	4
Exceptional items			
- Integration and transformation costs	**(49)**	(61)	(78)
- Acquisition accounting unwinds	**(47)**	(57)	(56)
- Legacy conduct costs	**(71)**	-	(26)
- Other items	**(6)**	(9)	(5)
Statutory profit/(loss) on ordinary activities before tax	**72**	(7)	(161)
Tax credit/(expense)	**8**	29	(2)
Statutory profit/(loss) for the period	**80**	22	(163)
Underlying RoTE	**10.1%**	4.6%	(3.5)%
Statutory RoTE	**2.2%**	(1.0)%	(11.6)%
TNAV per share	**257.5p**	252.5p	244.2p

Overview

The Group made a statutory profit before tax of £72m after deducting £173m of exceptional costs. The exceptional items charged in H1 2021 were higher than H1 2020 due to additional legacy conduct charges primarily relating to the Group’s PPI programme, whilst integration & acquisition costs, acquisition accounting unwind costs and other items all reduced.

TNAV per share increased 13.3p in H1 2021 to 257.5p. The key drivers of the increase were 2.1p of retained earnings, a further 8.1p of positive reserve movements and a 3.1p increase driven by lower goodwill and intangibles and other movements.

Integration and transformation costs

The Group continued with restructuring activity, spending £49m in the period as part of its ongoing integration and transformation programme. Overall, the Group now anticipates a total of c.£100m of costs during the year as it accelerates further cost saving activity.

Acquisition accounting unwinds

The Group recognised fair value accounting adjustments at the time of the Virgin Money acquisition that unwind through the income statement over the remaining life of the related assets and liabilities (c.5 years). £47m was reflected in H1 2021. The Group expects a further c.£100m of total acquisition accounting unwind charges over the next five years, with the majority anticipated to be incurred in H2 2021 and FY22.

Legacy conduct

Charges of £71m were incurred in H1, the key element being a further £59m charge in relation to the finalisation of the Group's PPI programme. The Group has now dealt with complaints received in the period up to the time bar in August 2019 including the settlement of claims received from the Official Receiver which are currently being finalised. The Group is working towards closing down the operation later this year. The remaining provision is expected to be sufficient to cover all outstanding liabilities in respect of the mis-selling of PPI policies.

Other items

The Group incurred £6m of other one-off exceptional costs during the first half of the year, primarily costs relating to the Virgin Money Aberdeen Asset Management PLC (AAM) UTM joint venture (JV).

Taxation

On a statutory basis, on a pre-tax profit of £72m, there was an £8m tax credit as the current period tax charge was more than offset by a deferred tax credit for additional historical losses recognised in the period and the tax credit on AT1 distributions.

Chief Financial Officer's review

Balance sheet

	As at		
	31 Mar 2021 £m	30 Sep 2020 £m	Change
Mortgages	**58,270**	58,290	-%
Personal	**5,050**	5,219	(3.2)%
Business	**8,891**	8,948	(0.6)%
of which Bounce Back Loan Scheme (BBLS)	***972***	*809*	*20.1%*
of which Coronavirus Business Interruption Loan Scheme (CBILS)	***415***	*334*	*24.3%*
Total customer lending	**72,211**	72,457	(0.3)%
Relationship deposits[(1)]	**28,744**	25,675	12.0%
Non-linked savings	**21,506**	20,729	3.7%
Term deposits	**18,288**	21,107	(13.4)%
Total customer deposits	**68,538**	67,511	1.5%
Wholesale funding	**13,289**	14,227	(6.6)%
of which TFS	***2,608***	*4,108*	*(36.5)%*
of which TFSME	***3,050***	*1,300*	*134.6%*
LDR	**105%**	107%	(2)%pts
LCR	**151%**	140%	11%pts

(1) Current account and linked savings balances.

Overview

At an aggregate level, Group lending reduced by 0.3% to £72.2bn as the Group carefully managed volumes against an uncertain backdrop. The reduction was primarily due to a small contraction in the Personal book, whilst Business and Mortgage lending remained broadly stable. Total customer deposits increased by 1.5% to £68.5bn reflecting pandemic-related consumer and business behaviours as customers have built up additional savings balances and liquidity.

Mortgage balances were stable at £58.3bn as the Group maintained pricing discipline, prioritising margin over volume growth in an uncertain environment albeit with some strong temporary drivers. The extension of the Stamp Duty holiday and continued levels of Government support, as well as strong buyer demand, have seen a relatively buoyant market during H1. However, market competition increased in Q2 with reduced customer rates being offered whilst higher swap rates have eroded some of the stronger spreads seen earlier in the period.

Personal balances reduced by 3.2% to £5.1bn against a challenging market environment with lower customer demand during the pandemic. Our credit card balances have been more resilient than the market due to our high proportion of balance transfer cards which make up a significant proportion (c.70%) of our portfolio and which are more stable than revolving credit facilities that rely on consumer spending. Personal loan volumes have also been impacted by lower demand through recent COVID-19 lockdown restrictions.

Business lending reduced 0.6% to £8.9bn, as growth in government-guaranteed lending schemes (BBLS/CBILS/Coronavirus Large Business Interruption Loan Scheme (CLBILS)) through which the Group has lent £1.4bn to businesses, was offset by lower non-government lending demand.

Customer deposit balances grew 1.5% in the period to £68.5bn. We continued to optimise the deposit base with a 13% reduction in term deposits, which also saw their cost to the Group reduce significantly. We saw continued growth in relationship deposits which rose 12% to £28.7bn as consumer spending slowed dramatically under tighter lockdown restrictions, and as we leveraged the successful launch of innovative new PCA propositions such as Brighter Money Bundles.

Wholesale funding and liquidity

The Group maintains a strong funding and liquidity position and has no reliance on short-term wholesale funding. The Group's LDR reduced 2% points in the period to 105% (FY20: 107%), principally as a result of the growth in customer deposits. At the same time, the Group's LCR of 151% (FY20: 140%) continues to comfortably exceed both regulatory requirements and our more prudent internal risk appetite metrics, ensuring a substantial buffer in the event of any sudden outflows and significant potential to support any increase in lending as the economy recovers.

The Group repaid a further £1.5bn of its TFS drawings, leaving £2.6bn outstanding. In addition to the £1.3bn drawn in FY20, the Group made further drawings of £1.8bn in H1 2021 from the BoE's new Term Funding Scheme with additional incentives for SMEs (TFSME), taking the total outstanding amount to £3.1bn at 31 March 2021. Overall, wholesale funding has reduced to £13.3bn in H1 2021 (FY20: £14.2bn) due to the increase in customer deposits meaning that maturing secured funding has not needed to be replaced.

Chief Financial Officer's review

Capital

	As at		
	31 Mar 2021	30 Sep 2020	Change
CET1 ratio (IFRS 9 transitional)	**14.4%**	13.4%	1.0%pts
CET1 ratio (IFRS 9 fully loaded)	**13.2%**	12.2%	1.0%pts
Total capital ratio	**21.2%**	20.2%	1.0%pts
MREL ratio	**29.3%**	28.4%	0.9%pts
UK leverage ratio	**5.2%**	4.9%	0.3%pts
RWAs (£m)	**24,152**	24,399	(1.0)%
of which Mortgages (£m)	***9,627***	*9,484*	*1.5%*
of which Business (£m)	***6,436***	*6,716*	*(4.2)%*
of which Personal (£m)	***4,018***	*4,151*	*(3.2)%*

(1) Unless where stated, data in the table shows the capital position on a CRD IV 'fully loaded' basis with IFRS 9 transitional adjustments applied.
(2) The capital ratios include unverified profits.

Overview

The Group has maintained a robust capital position with a CET1 ratio (IFRS 9 transitional basis) of 14.4%, or 13.9% excluding software intangible assets, and a total capital ratio of 21.2%. The significant impairment provision charges recognised since the start of the pandemic have been largely offset by IFRS 9 transitional relief. The Group's CET1 ratio on an IFRS 9 fully loaded basis improved to 13.2%. The Group's latest Pillar 2A requirement has a CET1 element of 2.2%. Overall, the Group's CRD IV minimum CET1 capital requirement (or MDA threshold) reduced by 0.3% in the period to 9.2%.

CET1 capital

CET1 increased by 99bps in the period with the movements set out in the table below. A reduction of c.£0.2bn (1%) in RWAs during the period, largely reflecting the impact of Business model updates and stable lending volumes, contributed 22bps to CET1. The change in the treatment of intangible software assets introduced as part of the CRR Quick Fix increased the CET1 ratio by 46bps.

CET1 Capital movements

	6 months to 31 Mar 2021 %/bps
Opening CET1 ratio	**13.4%**
Capital generated (bps)	**100**
RWA growth (bps)	**22**
AT1 distributions (bps)	**(12)**
Underlying capital generated (bps)	**110**
Integration and transformation costs (bps)	**(15)**
Acquisition accounting unwind (bps)	**(13)**
Conduct (bps)	**(27)**
Other (bps)	**(2)**
Impact of intangible asset relief (bps)	**46**
Net capital generated (bps)	**99**
Closing CET1 ratio	**14.4%**
Closing CET1 ratio excluding intangible asset relief	**13.9%**

(1) The table shows the capital position on a CRD IV 'fully loaded' basis with IFRS 9 transitional adjustments applied

MREL

The Group's MREL ratio increased to 29.3% in the period (FY20: 28.4%), comfortably exceeding both its interim and expected 2022 end-state MREL requirement. A further £0.5bn of MREL senior debt issuance is planned later in the year as the Group continues to build a prudent management buffer to regulatory requirements.

Chief Financial Officer's review

Outlook and guidance

FY21 financial guidance

NIM

NIM expected to be around 160bps

Underlying costs

Expect underlying costs of <£890m

Cost of risk

Subdued in the near term through FY21

Medium-term outlook:

The Board believes that, assuming no significant further deterioration in expectations for the economic outlook or change in interest rates, Virgin Money has a clear path to delivering double digit statutory returns on tangible equity over time

Based on the latest outlook and good momentum in NIM in H1, the Group expects NIM for FY21 to be around 160bps, assuming no change in the rate environment.

The Group expects underlying operating expenses of <£890m in FY21 reflecting the impact of COVID-19 restrictions and updated phasing. The Group remains committed to long-term cost reduction and will provide a further update on incremental cost opportunities from digital transformation alongside its full year results. The Group anticipates exceptional integration and transformation costs of c.£100m for the year.

Cost of risk is expected to remain subdued in the near term through FY21.

The CET1 ratio strengthened further in the half and the Group expects it will continue to exceed 13% (ex-software intangible benefit) at FY21.

Medium-term expectations

In the medium term, the Board believes that, assuming no significant further deterioration in expectations for the economic outlook or change in interest rates, Virgin Money has a clear path to delivering double digit statutory returns on tangible equity over time. The improvement in returns will be underpinned by continued cost reductions, the normalisation of impairments and exceptional costs, delivering capital efficiency, and optimising our balance sheet mix.

On capital, in the near term we expect to continue operating with a significant buffer in excess of our maximum distributable amount (MDA) threshold of 9.2%. Over the medium term, as economic conditions stabilise we expect the Counter Cyclical Buffer to be restored and therefore we intend to operate a dynamic CET1 ratio target. This will comprise an appropriate management buffer in excess of our end state MDA threshold that will be calibrated to ensure that the Group remains well capitalised. This assessment will take into account regulatory developments including the results of the SST later in the year and our view of the prevailing risk environment which will be calibrated to withstand our view of stressed conditions. The SST outcome in December and impairment outlook will be key inputs into our approach to considering dividends, and the Group expects to provide a further update on its capital framework post-SST.

Clifford Abrahams, Chief Financial Officer - 4 May 2021

Financial review - statutory basis

Summary income statement- statutory basis

	6 months to 31 Mar 2021 £m	6 months to 31 Mar 2020 £m	Change %	6 months to 30 Sep 2020 £m	Change %
Net interest income	**646**	671	(4)	612	6
Non-interest income	**49**	96	(49)	64	(23)
Total operating income	**695**	767	(9)	676	3
Operating and administrative expenses	**(585)**	(537)	9	(567)	3
Operating profit before impairment losses	**110**	230	(52)	109	1
Impairment losses on credit exposures	**(38)**	(237)	(84)	(270)	(86)
Statutory profit/(loss) on ordinary activities before tax	**72**	(7)	n/a	(161)	n/a
Tax credit/(expense)	**8**	29	(72)	(2)	n/a
Statutory profit/(loss) after tax	**80**	22	264	(163)	n/a

The Group has recognised a statutory profit before tax of £72m (31 March 2020: loss before tax of £7m). The increase in statutory profit is largely reflective of a significant reduction in impairment charges. The Group continues to expect that the difference between underlying and statutory profit will reduce over time as we deliver our strategy and the exceptional charges reduce.

Key performance indicators(1)

	6 months to 31 Mar 2021	6 months to 31 Mar 2020	Change	12 months to 30 Sep 2020(2)	Change
Profitability:					
Statutory RoTE	**2.2%**	(1.0)%	3.2%pts	(6.2)%	8.4%pts
Statutory CIR	**84%**	70%	14%pts	76%	8%pts
Statutory return on assets	**0.09%**	0.02%	0.07%pts	(0.16)%	0.25%pts
Statutory EPS	**2.8p**	(1.2)p	4.0p	(15.3)p	18.1p

(1) For a definition of each of the KPIs, refer to 'Measuring financial performance – glossary' on pages 257 to 258 of the Group's 2020 Annual Report and Accounts. The KPIs include statutory, regulatory and alternative performance measures. Where applicable certain KPIs are calculated on an annualised basis for the periods to 31 March.

(2) Profitability KPIs are provided with a full year to 30 September 2020 comparative in line with the statutory income statement presentation in the financial statements and as previously reported in the Group's 2020 Annual Report and Accounts.

Reconciliation of statutory to underlying results

The statutory basis presented within this section reflects the Group's results as reported in the financial statements. The underlying results reflect the Group's results prepared on an underlying basis as presented to the CEO, Executive Leadership Team and Board. These exclude certain items that are included in the statutory results, as management believes that these items are not reflective of the underlying business and do not aid meaningful period-on-period comparison. The table below reconciles the statutory results to the underlying results, and full details on the adjusted items to the underlying results are included on page 100.

6 months to 31 Mar 2021	**Statutory results £m**	**Integration and transformation costs £m**	**Acquisition accounting unwinds £m**	**Legacy conduct £m**	**Other £m**	**Underlying basis £m**
Net interest income	**646**	**-**	**31**	**-**	**-**	**677**
Non-interest income	**49**	**-**	**12**	**-**	**5**	**66**
Total operating income	**695**	**-**	**43**	**-**	**5**	**743**
Total operating and administrative expenses before impairment losses	**(585)**	**49**	**4**	**71**	**1**	**(460)**
Operating profit before impairment losses	**110**	**49**	**47**	**71**	**6**	**283**
Impairment losses on credit exposures	**(38)**	**-**	**-**	**-**	**-**	**(38)**
Profit on ordinary activities before tax	**72**	**49**	**47**	**71**	**6**	**245**
Financial performance measures						
RoTE	**2.2%**	**2.2%**	**2.2%**	**3.2%**	**0.3%**	**10.1%**
CIR	**84.2%**	**(6.3)%**	**(6.1)%**	**(9.1)%**	**(0.8)%**	**61.9%**
Return on assets	**0.09%**	**0.11%**	**0.10%**	**0.16%**	**0.01%**	**0.47%**
Basic EPS	**2.8p**	**2.8p**	**2.7p**	**4.0p**	**0.3p**	**12.6p**

6 months to 30 Sep 2020	Statutory results £m	Integration and transformation costs £m	Acquisition accounting unwinds £m	Legacy conduct £m	Other £m	Underlying basis £m
Net interest income	612	-	37	-	-	649
Non-interest income	64	-	13	-	(1)	76
Total operating income	676	-	50	-	(1)	725
Total operating and administrative expenses before impairment losses	(567)	78	5	26	6	(452)
Operating profit before impairment losses	109	78	55	26	5	273
Impairment losses on credit exposures	(270)	-	1	-	-	(269)
(Loss)/profit on ordinary activities before tax	(161)	78	56	26	5	4

6 months to 31 Mar 2020	Statutory results £m	Integration and transformation costs £m	Acquisition accounting unwinds £m	Legacy conduct £m	Other £m	Underlying basis £m
Net interest income	671	-	31	-	-	702
Non-interest income	96	-	15	-	4	115
Total operating income	767	-	46	-	4	817
Total operating and administrative expenses before impairment losses	(537)	61	6	-	5	(465)
Operating profit before impairment losses	230	61	52	-	9	352
Impairment losses on credit exposures	(237)	-	5	-	-	(232)
(Loss)/profit on ordinary activities before tax	(7)	61	57	-	9	120
Financial performance measures						
RoTE	(1.0)%	2.7%	2.5%	-%	0.4%	4.6%
CIR	70.0%	(6.3)%	(5.8)%	-%	(0.9)%	57.0%
Return on assets	0.02%	0.11%	0.10%	-%	0.02%	0.25%
Basic EPS	(1.2)p	3.3p	3.1p	-p	0.5p	5.7p

Risk Report

Risk overview

Effective risk management is critical to realising the Group's strategy of pioneering growth, with delighted customers and colleagues, while operating with super straightforward efficiency, discipline and sustainability. The safety and soundness of the Group is aligned to Our Purpose and is a fundamental requirement to enable our customers and stakeholders to be 'happier about money'.

Risk appetite is defined as the level and types of risk the Group is willing to assume within the boundaries of its risk capacity, to achieve its strategic objectives. The Risk Appetite Statement (RAS) articulates the Group's risk appetite to internal stakeholders and provides a view on the risk-taking activities the Board is comfortable with, guiding decision-makers in their strategic and business decisions.

The Group identifies and manages risk in line with the Risk Management Framework (RMF), which is the totality of systems, structures, policies, processes and people that identifies, measures, evaluates, controls, mitigates, monitors and reports all internal and external sources of material risk. The RMF aligns to Our Purpose by establishing a single and complete view of the end to end risk lifecycle, in a clear concise manner, which provides an overarching framework for the identification, measurement, management and reporting of risk

Principal risks

The Group's principal risks are those which could result in events or circumstances that might threaten the Group's business model, future performance, solvency, liquidity and reputation.

COVID-19 continues to have a significant impact on all of the Group's principal risk types. The range of governmental, regulatory and central bank support measures introduced create new operational, conduct, enforceability and financial risks for the Group. These risks have a variety of implications and, as such, COVID-19 has not been classified as a principal or emerging risk, but rather a major external event, which triggers a cascade of risks that will be monitored and managed proactively over time.

The table below sets out the Group's principal risks, which remain as disclosed in the 2020 Annual Report and Accounts. The key impacts of COVID-19 on each risk and the mitigating actions taken are also shown.

<table>
<tr><td colspan="2">Credit risk: The risk of loss of principal or interest stemming from a borrower's failure to meet contractual obligations to the Group in accordance with their agreed terms. Credit risk manifests at both a portfolio and transactional level.</td></tr>
<tr><td>COVID-19 impacts</td><td>COVID-19 mitigating actions</td></tr>
<tr><td>Although the impacts on the Group's retail and business credit portfolios are yet to fully manifest, it is clear that credit risk remains heightened, with default levels expected to increase over time, particularly once government support schemes come to an end.</td><td>The Group continues to participate in all regulatory and government support schemes, including the Recovery Loan Scheme, which was launched on 6 April 2021 to replace the previous business support schemes in place (CBILS, CLBILS and BBLS). The Group is also participating in the Mortgage Guarantee Scheme which aims to increase availability of 95% LTV mortgage products.

A priority focus on supporting existing customers through COVID-19 is maintained. Capital repayment holidays, interest free overdrafts (for retail customers) and extensions of credit, as well as other flexible supporting measures, continue to be provided and monitored.

Policies, risk appetite, credit decisioning and supporting frameworks have been rebased, reviewed and updated to reflect the changing environment and risk profiles.</td></tr>
<tr><td colspan="2">Financial risk: Includes capital risk, funding risk, liquidity risk, market risk and pension risk, all of which have the ability to impact the financial performance of the Group, if managed improperly.</td></tr>
<tr><td>COVID-19 impacts</td><td>COVID-19 mitigating actions</td></tr>
<tr><td>Changing trends in customers' use of deposits and the impacts of loan payment holidays across mortgage, credit card and unsecured loan portfolios, have affected capital, liquidity and funding forecasting.

The economic impact of COVID-19 has increased the likelihood of lower, or even negative, interest rates in the UK. Changes to interest rates increase the potential for volatility in margins.</td><td>Additional monitoring and controls over capital, funding and liquidity risks resulting from COVID-19 have been put in place. The Group has early visibility of movements in RWA or potential impacts to capital from higher credit losses and stands ready to take a range of management actions. The Group increased impairment provisions at the end of FY20 reflecting a cautious approach to an uncertain economic environment.

The BoE's TFSME provides an alternative source of funding to wholesale markets and is included in the Group's funding plans.

The decision to restart the Group's structural hedging programme limits interest rate risk and supports NII going forward.</td></tr>
</table>

Risk overview

Model risk: The potential for adverse consequences from decisions based on incorrect or misused model outputs and reports.	
COVID-19 impacts	***COVID-19 mitigating actions***
The uncertain economic environment has affected all model components including input data, default markers, outputs, model accuracy and performance. The rapid application of COVID-19 model adjustments has increased the risk that particular implementations contain errors or unexpected outcomes.	Model Risk Oversight remain actively engaged with model owners, carrying out pre-emptive model assessments to recognise and address key model risks and to validate COVID-19 driven adjustments or recalibrations. Further oversight is provided by the Model Governance Committee. Due to the impact of COVID-19 government support measures and payment holidays the Group is operating with carefully managed PMAs.

Regulatory and compliance risk: The risk of failing to comply with relevant laws and regulatory requirements, not keeping regulators informed of relevant issues, not responding effectively to information requests, not meeting regulatory deadlines or obstructing the regulator.	
COVID-19 impacts	***COVID-19 mitigating actions***
The Group has deployed multiple new policies and processes to implement government, regulatory and central bank COVID-19 support measures. Additional regulatory and compliance risks are associated with adherence to both COVID-19 specific regulatory guidance and with existing regulation.	Additional risk assessments, governance processes and assurance activities have been deployed across the Group to ensure compliance with existing regulation and COVID-19 specific regulatory guidance.

Conduct risk: The risk of undertaking business in a way that is contrary to the interests of customers, resulting in inappropriate customer outcomes or detriment, regulatory censure, redress costs and/or reputational damage.	
COVID-19 impacts	***COVID-19 mitigating actions***
There is an increased risk of failure to recognise and appropriately manage financial difficulties or vulnerabilities.	Additional monitoring and controls are in place to mitigate conduct risks arising from the execution of new customer support policies and processes deployed in response to COVID-19, and in the delivery and oversight of the government and regulatory support requirements that have continued to evolve over the last year. Significant work has gone into planning for impacts on personal customers that might result as support schemes such as payment deferrals and furlough are withdrawn. This has included increasing capacity within the operational areas supporting customers in financial difficulty. There are also ongoing areas of focus for supporting our business customers, including delivery of the government's 'Pay As You Grow' options and the new Recovery Loan Scheme. Risk assurance plans contain a significant focus on areas affected by COVID-19, including the impacts on customers in financial difficulties and vulnerable customers.

Operational risk: The risk of loss resulting from inadequate or failed internal processes, people or systems or from external events.	
COVID-19 impacts	***COVID-19 mitigating actions***
Increased remote working, amended processes and controls and pressure on customer support areas arising from changing customer needs all have the potential to increase the Group's operational risk profile, which could lead to increased errors or delays and subsequent loss. Operational readiness for negative interest rates is required by the BoE. This requires investment spend and system adaptations to allow pass-through of rates to relevant customers; if not carefully managed, these changes could increase operational risks.	Individual change assessments that were implemented as part of a temporary 'COVID-19 Process Change Risk' process are continually reviewed with business areas to understand the permanency of each change, the associated control changes and planned reversal timescales. Work to deliver operational readiness for negative interest rates is carefully controlled to ensure that timelines are met in a way that manages operational risks and prevents customer harm.

Risk overview

Technology risk: The risk of loss resulting from inadequate or failed information technology processes. Technology risk includes cybersecurity, IT resilience, information security, data risk and payment risk.	
COVID-19 impacts	***COVID-19 mitigating actions***
An increased risk of cyberattacks, due to phishing emails which use a COVID-19 theme, and breaches could have legal, regulatory or privacy implications. Reliance on the availability of digital banking and remote network access has increased with solutions implemented to address system constraints and safeguard our connections.	Additional fraud monitoring is in place and temporary process changes are being continually risk assessed. A significant number of colleagues continue to work from home. System monitoring, incident management and escalation processes are in place with regular oversight performed. There continues to be enhanced focus on supplier service level agreements and contingency plans.

Financial crime risk: The risk that the Group's products and services will be used to facilitate financial crime against the Group, its customers or third parties. This includes money laundering, counter-terrorist financing, sanctions, fraud and bribery and corruption.	
COVID-19 impacts	***COVID-19 mitigating actions***
There remains a risk that criminals may take advantage of customer and organisational vulnerabilities created by COVID-19.	Additional risk assessments, governance processes and assurance activity continue to be undertaken across the Group, to ensure the ongoing balance between customer impacts and support and maintaining fraud loss within risk appetite.

Strategic and enterprise risk: The risk of significant loss of earnings or damage arising from decisions or actions that impact the long-term interests of the Group's stakeholders or from an inability to adapt to external developments, including potential execution risk as a result of transformation activity.	
COVID-19 impacts	***COVID-19 mitigating actions***
COVID-19 has increased the pace of change and unpredictability within the external environment, including in relation to economic conditions, regulation, and culture. There is a risk that the Strategic and Financial Plan does not adequately reflect these changes, or that we respond ineffectively to the cultural and societal changes it has brought about.	The Strategic and Financial Plan is refreshed biannually to ensure the Group remains resilient and well placed to continue to support our customers and colleagues. Recent re-forecasting has accounted for measures announced at the March 2021 Budget and the anticipated profile of governmental and regulatory support schemes, noting the potential for an increase in impairments as support schemes come to an end. The Group's RAS has been reassessed alongside the refreshed plan, with changes made to account for the risk profile impacts of the initiatives being proposed.

People risk: The risk of not having sufficiently skilled and motivated colleagues, who are clear on their responsibilities and accountabilities and who behave in an ethical way.	
COVID-19 impacts	***COVID-19 mitigating actions***
An increased risk of colleague illness and absence, in addition to longer-term well-being risks, such as mental health impacts, may arise from the tighter restrictions introduced to curb the spread of COVID-19. These factors could increase pressure and reduce skills availability in key areas. The increase in remote working as a result of COVID-19 means there is often no longer a requirement to live in close proximity to an employer's office, which may result in increased competition for skilled and experienced colleagues.	The Group follows government advice with colleagues working from home where possible, and social distancing and additional cleaning measures in place to support key workers based in offices and branches. Vulnerable colleagues are being given additional support from our healthcare provider. The Group is moving to a 'Life More Virgin' model which will use colleague feedback to create working arrangements to optimise well-being, engagement and productivity. Opportunities afforded by our new ways of working mean we will be able to attract and hire candidates from across the UK in future.

Further detail on these risks and how they are managed is available in the Group's 2020 Annual Report and Accounts.

Risk overview

Cross-cutting risks

Operational resilience and climate risk are treated as cross-cutting risks in the Group's RMF, manifesting through the established principal risk framework.

Operational Resilience

Operational resilience is defined as the ability of the Group to protect and sustain its most critical functions and underlying assets, while adapting to expected or unexpected operational stress or disruption and having the capacity to recover from issues as and when they arise.

The Group assesses its operational resilience risk for the people, technology, third parties and premises that underpin the principal risks, ensuring that the Group aims to provide a superior level of support and services to customers and stakeholders on a consistent and uninterrupted basis. It is accepted that, on occasion, this will not be possible and, at such times, the Group aims to recover critical services within tight timelines to minimise customer disruption.

Climate Risk

The Group is exposed to physical, transition and reputational risks arising from climate change. Aligned with our wider ESG ambitions, the Group continues work to understand, evaluate and integrate the management of climate risks into our decision-making frameworks.

The Group is developing scenario analysis capability which will further inform strategy. Using scenario analysis will also improve the assessment of future risks across the Group's lending portfolios given the very long-term impacts of climate change and the high degree of uncertainty as to how the risks may crystallise. Outputs will be used to support Credit Policy and risk mitigation activities.

Transition risk within the mortgage portfolio has been considered with an assessment of the energy efficiency of properties. The portfolio is in line with market averages and the Group increasingly intends to use this information to support our customers to 'green' their homes.

Work has been completed to analyse transition risks within the business lending book. This assessment has been used to establish risk appetite for climate risk and is calculated and reported to the relevant governance committees. Where a heightened environmental or climate-related risk is identified during customer due diligence or credit processes, additional scrutiny under the Group's ESG policy is triggered which may lead to additional environmental reports being required.

Emerging risks

The Group considers an emerging risk to be any risk which has a material unknown and unpredictable component, with the potential to significantly impact the future performance of the Group. The Group's emerging risks are continually reassessed and reviewed through a horizon scanning process, with escalation and reporting to the Board. The horizon scanning process fully considers all relevant internal and external factors and is designed to capture those risks which are current but have not yet fully crystallised, as well as those which are expected to crystallise in future periods.

Emerging risks are allocated a status based on their expected impact (from low to very high) and time to fully crystallise (from >12 months to >3 years), in line with the definitions outlined in the RMF, and are subject to regular review across senior governance forums.

The emerging risk classifications reported in the Group's 2020 Annual Report and Accounts are retained. Following consideration of the current and future risk landscape, two additional emerging risks are included. These are data management and critical infrastructure. The table overleaf shows a summary of the Group's emerging risks.

Risk overview

Key impacts	*Mitigating actions*
Geopolitical and macroeconomic environment	
Due primarily to the impact of COVID-19 on the economy, the future trajectory of macroeconomic variables, such as GDP, unemployment, interest rates and the HPI, remains uncertain and subject to volatile change depending on a complex mix of outcomes. Higher levels of corporate and government indebtedness and the potential for negative interest rates create further uncertainty over the path to economic recovery. Changes to the UK's trading arrangements with the EU following the Brexit trade deal are beginning to emerge, with uncertainty around future levels of inward foreign investment having the potential to adversely affect certain sectors of the UK economy. There is an increased possibility of a second Scottish independence referendum. The direction this could take should become clearer following the outcome of the Scottish Parliamentary Elections being held on 6 May 2021.	The Group continues to monitor economic and political developments in light of the ongoing uncertainty, considering potential consequences for its customers, products and operating model, including its sources of funding. The Group actively monitors its credit portfolios and undertakes robust internal analysis to identify sectors that may come under stress as a result of an economic slowdown in the UK. Stress testing is performed to demonstrate the Group's financial resilience and to evidence its capability to withstand a range of severe but plausible economic scenarios.
Climate risk	
There is significant uncertainty around the time horizon over which climate risks will materialise as well as the exact way in which they will occur. Stakeholder expectations and regulatory attention are developing at pace, impacting all of the Group's activities. Sudden shifts in sentiment, if not in line with the lending practices and customer profile of the Group at that time, could lead to increased scrutiny and reputational damage.	The Group continues to embed climate risk into its RMF and is working to understand how these risks can be monitored, managed and incorporated into planning, in order to support the Group's sustainability aspirations, as well as those of society. Climate risks are also considered by the Board in its review and challenge of the Strategic and Financial Plan and the Group's Sustainability Strategy.
Regulatory and governmental change	
The Group remains subject to significant levels of regulatory change and scrutiny, with complex pieces of legislation being passed at pace by various bodies. The suite of government support measures introduced to help support the economy through the pandemic are multifaceted and nuanced. Changes to the rules and regulations governing the measures, for example eligibility criteria or the timing of scheme run-off, require careful management of potential conduct, reputational and fraud risks. Beyond COVID-19, there is continued evolution of the regulatory landscape, and the requirement to respond to ongoing prudential and conduct driven initiatives including the likely reintroduction of full capital deductions for intangible assets. The PRA has also commenced a consultation on mortgage risk weights that, if implemented, would increase RWAs. The Group is also participating in the BoEs annual SST in 2021.	The Group continues to monitor emerging regulatory initiatives to identify potential impacts on its business model and ensure it is well placed to respond with effective regulatory change management. The Group continues to work with regulators to ensure it meets all regulatory obligations, with identified implications of upcoming regulatory activity incorporated into the strategic planning cycle. The Group has put multiple new policies in place to help ensure COVID-19 related government, regulatory and Group customer support arrangements are deployed correctly.

Risk overview

Key impacts	***Mitigating actions***
Technology and cyber risk	
The Group continues to operate in a highly competitive environment, with growth across a number of digital-only providers and emerging signs of participation from large technology companies. There is a rapid pace of technological change which, coupled with increasing digital demands from customers for the access and use of our products and services, means there is increased demand on systems resilience and our people. The resilience of systems security, payment and overall technology solutions is a focus of the Group. Fast-moving global cyber risk challenges, including those driven by large nation states, continue to pose risks to the security of company and government systems and protection of customer data.	The potential impacts from new technologies, and from the changing ways in which customers use the Group's services, are continuously risk assessed, with action pre-emptively taken to safeguard the end-to-end resilience of critical processes. The Group continues to invest in the security and resilience of its infrastructure in order to improve services and minimise the risk of disruption to customers. The Group has resilient continuity frameworks in place to support activities in an open banking, digitally reliant market.
Data management	
The Group's digitisation strategy coupled with the changing regulatory requirements and advancements in technology, for example the increasing use of Cloud solutions or Big Data for analysis purposes, means there is a growing importance attached to the effective and ethical use, governance and protection of data. Failure to effectively mitigate data management risks could result in unethical decisions, regulatory breaches, poor customer outcomes, mistrust and loss of value to the Group.	The Group has a data management framework governing the creation, storage, distribution, usage and retirement of data. This framework also encompasses data ethics. The Group continues to invest in data management capabilities alongside the introduction of new technologies and services. New and existing data management regulations are continuously assessed with proactive action taken to ensure compliance.
Critical infrastructure	
The Group is dependent on critical infrastructure provided by third parties to maintain its day-to-day operations without interruption. Important services include: • internet and telephone access; • credit rating agencies and decisioning; • software applications; • cloud systems; and • payment networks (Mastercard, LINK, FPS, CHAPS, SWIFT etc). Failure of one of these systems could result in colleagues or customers being unable to provide/receive fundamental banking services.	Dependencies on critical infrastructure assets are managed in line with the Group's third-party supplier risk management policies. The Group undertakes extensive scenario planning to assess potential dependencies in end-to-end systems processing. Safeguarding the operational resilience of services is of critical importance to the Group.

Credit risk

Credit risk

The economic challenges and disruption from COVID-19 continue to impact the Group's customers. In response, the Group has continued to provide customer support and has maintained the defensive shape and credit quality of its well diversified lending portfolio, with 81% of the lending portfolio from a low LTV mortgage book, 12% from a diversified business lending portfolio and the remaining 7% from a high quality personal lending portfolio. The Group adhered to its principles, managing the lending portfolio within a controlled risk appetite alongside a prudent approach to underwriting with additional tightening of origination criteria introduced in response to economic events.

An unprecedented variety of support measures including furlough, payment holidays and government-backed loans for businesses, has buffered the observed linkage between economic stress and default. As a result of the effectiveness of those support measures, the emergence of default and impairment through the pandemic has to date been relatively muted. This is reflected in the underlying impairment charge of £38m for the six months to 31 March 2021, a reduction of £194m from the six months to 31 March 2020, a figure which did include an increase reflecting the Group's initial estimate of the pandemic driven provisioning requirement.

Arrears levels have remained largely stable across all portfolios as extensions to government interventions and payment holiday support have been granted. There has been an improvement in staging, with 83% of the Group's lending portfolio now in stage 1 at 31 March 2021 (30 September 2020: 81%). This is principally due to more optimistic economic forecasts driving an improvement in PD for the mortgage and business portfolios. Stage 2 balances have similarly improved, in particular the proportion <30 DPD which reduced to 16% at 31 March 2021 (30 September 2020: 17%). Stage 3 balances have remained broadly stable. In summary, while the proportion of the lending portfolio in Stage 2 reflects a level of financial challenge for many customers, stage migrations have moved in a positive direction reflective of more optimistic macroeconomic forecasts. The vast majority of customers who have taken advantage of the COVID-19 payment holiday options available have already resumed their normal payment patterns and the Group will continue to closely evaluate the performance of these customers going forward.

The Group's assessment of the economic environment, while more optimistic than six months ago, does remain cautious given the degree of uncertainty around customer performance when the broad suite of support measures is withdrawn. We recognise the need for additional customer support as furlough ceases, government-backed loan schemes are phased out, repayments commence and the economy normalises. The Group has planned for this and is operationally ready to deliver the support required. This normalisation in the economy will result in increased defaults and the potential for weaker recoveries from customers already in default, which has led to the Group broadly maintaining the level of provision coverage held for future ECL at 1.00% (30 September 2020: 1.02%). Management has applied adjustments to the Group's modelled ECL provision to capture the estimated impact of future risk in its lending portfolios. Where it has not been possible to fully quantify the impact of current and future risk in modelled outcomes, or we have assessed limitations in our models, expert judgement has been applied to determine an appropriate level of additional post-model adjustments (PMAs). The level of PMAs has increased to £222m (30 September 2020: £186m) due to the level of uncertainty prevailing. The combination of modelled ECL and PMA ensures the Group has suitably provided against expected future losses, with a provision of £721m at 31 March 2021 (30 September 2020: £735m). This level of provision and resultant coverage is considered to be balanced and appropriate for our portfolio at the present time.

Notwithstanding the recent positive progress in easing lockdown restrictions and the success in rolling out the COVID-19 vaccine, uncertainty in the economic outlook remains. The Group will continue to actively monitor and assess the performance of our credit portfolios as we navigate through these difficult times.

Group credit highlights

		31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m	31 Mar 2020 (unaudited) £m
Underlying impairment charge on credit exposures		**38**	501	232
Impairment provisions:	Modelled	**462**	496	303
	PMA	**222**	186	184
	Individually assessed	**37**	53	55
Impairment provisions held on credit exposures		**721**	735	542

Credit risk

Managing risk within our credit portfolios

Risk appetite

The Group controls its levels of credit risk by placing limits on the amount of risk it is willing to take in order to achieve its strategic objectives. This involves a defined set of qualitative and quantitative limits in relation to its credit risk concentrations to one borrower, or group of borrowers, and to geographical, product and industry segments. The management of credit risk within the Group is achieved through ongoing approval and monitoring of individual transactions, regular asset quality reviews and the independent oversight of credit decisions and portfolios.

The COVID-19 pandemic continues to present significant risks to the Group's credit portfolios. However, the Group remains focused on supporting customers and colleagues through the exceptional challenges that have crystallised over the past 12 months. The HY21 RAS recognised and responded to the impact that the extension of government backed lending, furlough and payment holiday support to customers has had, particularly to underlying asset quality metrics and to the timing of expected future credit losses. Such factors are under continual review to ensure we are addressing new and developing risks in a safe and controlled manner.

Measurement

The Group uses a range of statistical models, supported by both internal and external data, to measure credit risk exposures. These models underpin the IRB capital calculation for the mortgage and business portfolios and account management activity for all portfolios. Further information on the measurement and calculation of ECL and the Group's approach to the impairment of financial assets can be found on page 31.

The Group's portfolios are subject to regular stress testing, including participation in the PRA's Solvency Stress Test for the first time in 2021. Stress test scenarios are regularly prepared to assess the adequacy of the Group's impairment provision and the impact on RWAs and capital. Management will consider how each stress scenario may impact on different components of the credit portfolio. The primary method applied uses migration matrices, modelling the impact of PD rating migrations and changes in portfolio default rates to changes in macroeconomic factors to obtain a stressed position for the credit portfolios. Loss given default (LGD) is stressed based on a range of factors, including property price movements.

Mitigation

The Group maintains a dynamic approach to credit management and takes necessary steps if individual issues are identified or if credit performance has, or is expected to, deteriorate due to borrower, economic or sector-specific weaknesses.

The mitigation of credit risk within the Group is achieved through approval and monitoring of individual transactions and asset quality, analysis of the performance of the various credit risk portfolios, and independent oversight of credit portfolios across the Group. Portfolio monitoring techniques cover such areas as product, industry, geographic concentrations and delinquency trends.

There is regular analysis of the borrower's ability to meet their interest and capital repayment obligations with early support and mitigation steps taken where required. Credit risk mitigation (CRM) is also supported, in part, by obtaining collateral and corporate and personal guarantees where appropriate.

Further details on the Group's mitigating measures can be found on page 120 of the 2020 Annual Report and Accounts.

Managing risk within our credit portfolios (continued)

Monitoring

Credit policies and procedures, which are subject to ongoing review, are documented and disseminated in a form that supports the credit operations of the Group.

- Credit Risk Committee: The Credit Risk Committee ensures that the credit RMF and associated policies remain effective. The Committee has oversight of the quality, composition and concentrations of the credit risk portfolio and considers strategies to adjust the portfolio to react to changes in market conditions including the response to the pandemic.
- RAS measures: Measures are monitored monthly and reviewed bi-annually, at a minimum, or where specific action is merited. Regular review ensures that the measures accurately reflect the Group's risk appetite, strategy and concerns relative to the wider macro environment. All measures are subject to extensive engagement with the Executive Leadership Team and the Board and are subject to endorsement from executive governance committees prior to Board approval. Regulatory engagement is also scheduled as appropriate.
- Risk concentration: Concentration of risk is managed by counterparty, product, geographical region and industry sector. In addition, single name exposure limits exist to control exposures to a single counterparty. Concentrations are also considered through the RAS process, focusing particularly on the external environment, outlook and comparison against market benchmarks.
- Single large exposure excesses: All excesses are reported to the Transactional Credit Committee and the Chief Credit Officer. Any exposure which continues, or is expected to continue, beyond 30 days will also be considered by the Transactional Credit Committee along with proposals to correct the exposure within an agreed period, not to exceed 12 months.

Forbearance

Forbearance is considered to exist where customers are experiencing or about to experience financial difficulty and the Group grants a concession on a non-commercial basis. The Group's forbearance policies and definitions comply with the guidance established by the EBA for financial reporting. Forbearance concessions include the granting of more favourable terms and conditions than those provided either at drawdown of the facility, or which would not ordinarily be available to other customers with a similar risk profile. Forbearance parameters are regularly reviewed and refined as necessary to ensure they are consistent with the latest industry guidance and prevailing practice, as well as ensuring that they adequately capture and reflect the most recent customer behaviours and market conditions.

Measuring and calculating ECL

At each reporting date, the Group assesses financial assets measured at amortised cost, as well as loan commitments and financial guarantees not measured at FVTPL, for impairment. The impairment loss allowance is calculated using an ECL methodology and reflects: (i) an unbiased and probability weighted amount; (ii) the time value of money which discounts the impairment loss; and (iii) reasonable and supportable information that is available without undue cost or effort about past events, current conditions and forecasts of future economic conditions.

The ECL is then calculated as either 12 month (Stage 1) or lifetime (Stage 2 or Stage 3). Stage 2 is applied where there has been a SICR since origination. Stage 3 applies where the loan is credit impaired or is a purchased or originated credit impaired asset (POCI).

ECLs under IFRS 9 use economic forecasts, models and judgement to provide a forward-looking assessment of the required provisions. Adjustments have been made to address known limitations in the Group's models or data; this includes early adoption of a limited number of enhancements to better reflect the Group's assessment of risk. Due to the current severe economic conditions, government and Group interventions to support customers, and uncertainty arising from COVID-19, the Group has not relied upon modelled outcomes alone. Following detailed analysis, expert credit judgement has been applied, resulting in additional adjustments to ensure the ECL calculation reflects the full set of plausible circumstances including data limitations, customer support measures, rapidly changing customer behaviours and the emerging nature of COVID-19 risks.

Further details on the Group's measurement of credit risk can be found on page 122 of the 2020 Annual Report and Accounts.

Credit risk

Portfolio performance

How our portfolios have performed

Credit risk exposures are classified into mortgage, personal and business portfolios. In terms of loans and advances, credit risk arises both from amounts loaned and commitments to extend credit to customers. To ensure appropriate credit limits exist, especially for business lending, a single large exposure policy is in place and forms part of the risk appetite measures that are monitored and reported on a monthly basis. The overall composition and quality of the credit portfolio is monitored and regularly reported to the Board and, where required, to the relevant supervisory authorities.

Exposures are also managed in accordance with the large exposure reporting requirements of the Capital Requirements Regulation (CRR). Unless otherwise noted, the amount that best represents the maximum credit exposure at the reporting date is the carrying value of the financial asset.

Concentration of lending assets

The following tables show the levels of concentration of the Group's loans and advances, contingent liabilities and credit-related commitments:

March 2021 (unaudited)	Gross loans and advances to customers £m	Contingent liabilities and credit-related commitments £m	Total £m
Property – mortgage	58,620	3,641	62,261
Instalment loans to individuals and other personal lending (including credit cards)	5,403	10,380	15,783
Agriculture, forestry, fishing and mining	1,622	362	1,984
Manufacturing	824	673	1,497
Wholesale and retail	961	519	1,480
Property – construction	351	128	479
Financial, investment and insurance	102	95	197
Government and public authorities	36	347	383
Other commercial and industrial	4,834	1,918	6,752
	72,753	18,063	90,816
Impairment provisions on credit exposures	(711)	(10)	(721)
Fair value hedge adjustment	(35)	-	(35)
Maximum credit risk exposure on lending assets	72,007	18,053	90,060
Cash and balances with central banks			10,441
Financial instruments at fair value through other comprehensive income (FVOCI)			4,532
Due from other banks			722
Other financial assets at fair value			171
Derivative financial assets			222
Maximum credit risk exposure on all financial assets			106,148

Credit risk

Concentration of lending assets (continued)

September 2020 (audited)	Gross loans and advances to customers £m	Contingent liabilities and credit-related commitments £m	Total £m
Property – mortgage	58,652	3,088	61,740
Instalment loans to individuals and other personal lending (including credit cards)	5,550	9,674	15,224
Agriculture, forestry, fishing and mining	1,634	375	2,009
Manufacturing	884	692	1,576
Wholesale and retail	961	563	1,524
Property – construction	339	136	475
Financial, investment and insurance	97	173	270
Government and public authorities	19	348	367
Other commercial and industrial	4,789	1,821	6,610
	72,925	16,870	89,795
Impairment provisions on credit exposures	(735)	-	(735)
Fair value hedge adjustment	240	-	240
Maximum credit risk exposure on lending assets	72,430	16,870	89,300
Cash and balances with central banks			9,107
Financial instruments at FVOCI			5,080
Due from other banks			927
Other financial assets at fair value			203
Derivative financial assets			318
Maximum credit risk exposure on all financial assets			104,935

Key credit metrics

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m	31 Mar 2020 (unaudited) £m
Impairment provisions held on credit exposures			
Mortgage lending	**132**	131	50
Personal lending	**293**	301	231
Business lending	**296**	303	261
Total impairment provisions(1)	**721**	735	542

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m	31 Mar 2020 (unaudited) £m
Underlying impairment (credit)/charge on credit exposures			
Mortgage lending	**(1)**	95	12
Personal lending	**27**	223	100
Business lending	**12**	183	120
Total underlying impairment charge	**38**	501	232
Asset quality measures:			
Underlying impairment charge(2) to average customer loans (cost of risk)	**0.11%**	0.68%	0.63%
% Loans in Stage 2	**16.06%**	17.70%	7.14%
% Loans in Stage 3	**1.37%**	1.19%	1.13%
Total provision to customer loans(3)	**1.00%**	1.02%	0.75%
Stage 2 provision to Stage 2 loans	**4.15%**	3.63%	5.16%
Stage 3 provision to Stage 3 loans	**10.32%**	15.62%	18.38%

(1) The impairment provision of £721m includes £10m for off-balance sheet exposures. A change to the accounting presentation was made in the period, with the on-balance sheet ECL continuing to be reflected in loans and advances to customers (note 3.1) and the off-balance ECL now separately disclosed as part of the provision for liabilities and charges balance in note 3.7 to the interim financial statements which were not restated. All tables and ratios that follow are calculated using the combined on and off-balance sheet ECL, which is consistent for all periods reported.

(2) Inclusive of gains/losses on assets held at fair value and elements of fraud loss but excludes the acquisition accounting impact on impairment losses shown on page 20.

(3) This includes the government-backed portfolio of BBLs, CBILs and CLBILs.

Credit risk

Group credit performance

Total gross loans and advances to customers decreased by £0.1bn to £72.8bn, due to a small contraction in personal lending while mortgage and business lending remained broadly stable. This reflects the Group's focus on supporting existing customers, muted demand for new borrowing and the impact of changing customer behaviours as lending was paid down more rapidly.

The Group's impairment provision reduced by £14m to £721m as at 31 March 2021. The small movement is driven by the utilisation or release of a small number of individually assessed provisions with limited movement in the aggregate IFRS 9 provisions, including the net impact of movements in PMAs. The continued risk of volatility in the economy, particularly as customer support mechanisms are withdrawn, and the intent to maintain a level of stability in the on balance sheet provisions until the impact of the withdrawal of the support mechanisms is understood, has resulted in total provisions to customer loans remaining broadly stable at 1.00% (30 September 2020: 1.02%). This reflects the expectation that losses will emerge as the level of COVID-19 support subsides.

The composition and weighting of the economic scenarios used in the provision assessment have been updated to reflect an improving view of the economic outlook, resulting in a £34m reduction in modelled provision to £462m. Offsetting the reduction in model provision is a £36m increase in PMAs to £222m. This increase is driven by the introduction of a £93m PMA for Economic Resilience Uncertainty (ERU) to reflect concerns that the economic impact on customers from COVID-19 has been suppressed as a result of the various support mechanisms, and that the level of distress that may emerge post withdrawal of the various forms of customer support will exceed the level calculated through the current model inputs and updated economic scenarios. ERU addresses concern that some of the most severe longer term impacts of the pandemic are not fully reflected in the model inputs under the current, more positive economic outlook and its introduction offsets some of the reductions in PMAs previously held, such as a reduced PMA relating to payment holidays. The other key movements to PMAs are an increase in the mortgage buy-to-let (BTL) PMA to reflect the potential risk in the portfolio, notwithstanding the recent low default experience and low average LTV; a new PMA for commercial real estate to offset the modelled release following improved GDP and asset price assumptions; and a modest PMA for cladding risk in the mortgage portfolio.

The Group's underlying impairment charge of £38m for the six months to 31 March 2021 is reflective of the already prudent coverage levels and muted emergence of COVID-19 influenced default and impairment to date. This has resulted in cost of risk of 11bps as at 31 March 2021 (30 September 2020: 68bps).

Underlying credit portfolio performance remains broadly stable, as evidenced by the proportion of Stage 3 loans to total customer loans of 1.37% (30 September 2020: 1.19%). There has been no material deterioration in asset quality measures. Arrears and default levels remain low, and forbearance levels remain static. This has been influenced by the extended period of customer support measures, combined with the Group's controlled risk appetite and continued focus on responsible lending decisions.

Credit quality of loans and advances

The following tables highlight the distribution of the Group's gross loans and advances, ECL and coverage by IFRS 9 stage allocation:

Gross loans and advances[(1)] ECL and coverage

As at 31 March 2021 (unaudited)	Mortgages £m	Mortgages %	Personal Cards £m	Personal Cards %	Personal Loans & Overdrafts £m	Personal Loans & Overdrafts %	Personal Combined £m	Personal Combined %	Business[(2)] £m	Business[(2)] %	Total £m	Total %
Stage 1	**50,753**	**86.5%**	**3,676**	**84.6%**	**687**	**64.9%**	***4,363***	***80.8%***	**4,986**	**57.1%**	**60,102**	**82.6%**
Stage 2 < 30 DPD	*6,906*	*11.8%*	*592*	*13.7%*	*353*	*33.3%*	*945*	*17.4%*	*3,482*	*39.9%*	*11,333*	*15.6%*
Stage 2 > 30 DPD	*280*	*0.5%*	*14*	*0.3%*	*5*	*0.5%*	*19*	*0.4%*	*27*	*0.3%*	*326*	*0.4%*
Stage 2 – total	**7,186**	**12.3%**	**606**	**14.0%**	**358**	**33.8%**	***964***	***17.8%***	**3,509**	**40.2%**	**11,659**	**16.0%**
Stage 3[(3)]	**681**	**1.2%**	**62**	**1.4%**	**14**	**1.3%**	***76***	***1.4%***	**235**	**2.7%**	**992**	**1.4%**
	58,620	**100.0%**	**4,344**	**100.0%**	**1,059**	**100.0%**	***5,403***	***100.0%***	**8,730**	**100.0%**	**72,753**	**100.0%**
ECLs												
Stage 1	**14**	**10.6%**	**42**	**19.2%**	**12**	**16.2%**	***54***	***18.5%***	**72**	**24.3%**	**140**	**19.4%**
Stage 2 < 30 DPD	*91*	*68.9%*	*136*	*62.1%*	*52*	*70.3%*	*188*	*64.1%*	*181*	*61.2%*	*460*	*63.8%*
Stage 2 > 30 DPD	*5*	*3.8%*	*11*	*5.0%*	*3*	*4.0%*	*14*	*4.8%*	*1*	*0.3%*	*20*	*2.8%*
Stage 2 – total	**96**	**72.7%**	**147**	**67.1%**	**55**	**74.3%**	**202**	***68.9%***	**182**	**61.5%**	**480**	**66.6%**
Stage 3[(3)]	**22**	**16.7%**	**30**	**13.7%**	**7**	**9.5%**	***37***	***12.6%***	**42**	**14.2%**	**101**	**14.0%**
	132	**100.0%**	**219**	**100.0%**	**74**	**100.0%**	***293***	***100.0%***	**296**	**100.0%**	**721**	**100.0%**
Coverage												
Stage 1		**0.03%**		**1.24%**		**2.12%**		***1.37%***		**1.82%**		**0.24%**
Stage 2 < 30 DPD		*1.33%*		*25.01%*		*17.40%*		*22.31%*		*5.64%*		*4.10%*
Stage 2 > 30 DPD		*1.71%*		*81.57%*		*74.14%*		*79.52%*		*1.89%*		*6.08%*
Stage 2 – total		**1.35%**		**26.34%**		**18.34%**		***23.51%***		**5.61%**		**4.15%**
Stage 3[(3)]		**3.14%**		**54.15%**		**60.98%**		***55.34%***		**18.94%**		**10.32%**
		0.23%		**5.50%**		**8.39%**		***6.03%***		**3.98%**		**1.00%**

(1) Excludes loans designated at FVTPL, balances due from customers on acceptances, accrued interest and deferred and unamortised fee income.
(2) Business coverage has been adjusted to exclude government-backed loans.
(3) Stage 3 includes POCI for gross loans and advances of £78m for Mortgages and £3m Personal; and ECL of (£0.4m) for Mortgages and (£1.9m) for Personal.

As at 30 September 2020 (audited)	Mortgages £m	Mortgages %	Personal Cards £m	Personal Cards %	Personal Loans & Overdrafts £m	Personal Loans & Overdrafts %	Personal Combined £m	Personal Combined %	Business[(2)] £m	Business[(2)] %	Total £m	Total %
Stage 1	49,970	85.2%	3,893	87.2%	767	70.6%	4,660	84.0%	4,589	52.6%	59,219	81.2%
Stage 2 < 30 DPD	*7,976*	*13.6%*	*512*	*11.4%*	*298*	*27.4%*	*810*	*14.6%*	*3,845*	*44.1%*	*12,631*	*17.3%*
Stage 2 > 30 DPD	*190*	*0.3%*	*7*	*0.2%*	*6*	*0.6%*	*13*	*0.2%*	*10*	*0.1%*	*213*	*0.3%*
Stage 2 – total	8,166	13.9%	519	11.6%	304	28.0%	823	14.8%	3,855	44.2%	12,844	17.6%
Stage 3[(3)]	516	0.9%	52	1.2%	15	1.4%	67	1.2%	279	3.2%	862	1.2%
	58,652	100.0%	4,464	100.0%	1,086	100.0%	5,550	100.0%	8,723	100.0%	72,925	100.0%
ECLs												
Stage 1	14	10.7%	48	21.6%	22	27.8%	70	23.3%	52	17.1%	136	18.5%
Stage 2 < 30 DPD	*84*	*64.1%*	*141*	*63.5%*	*44*	*55.7%*	*185*	*61.4%*	*176*	*58.1%*	*445*	*60.6%*
Stage 2 > 30 DPD	*11*	*8.4%*	*6*	*2.7%*	*3*	*3.8%*	*9*	*3.0%*	-	-	*20*	*2.7%*
Stage 2 – total	95	72.5%	147	66.2%	47	59.5%	194	64.4%	176	58.1%	465	63.3%
Stage 3[(3)]	22	16.8%	27	12.2%	10	12.7%	37	12.3%	75	24.8%	134	18.2%
	131	100.0%	222	100.0%	79	100.0%	301	100.0%	303	100.0%	735	100.0%
Coverage												
Stage 1		0.03%		1.34%		3.22%		1.64%		1.42%		0.24%
Stage 2 < 30 DPD		*1.06%*		*29.73%*		*16.67%*		*25.03%*		*4.60%*		*3.56%*
Stage 2 > 30 DPD		*5.98%*		*76.86%*		*74.28%*		*75.83%*		*5.12%*		*9.73%*
Stage 2 – total		1.17%		30.40%		17.64%		25.81%		4.61%		3.66%
Stage 3[(3)]		4.31%		57.48%		79.43%		62.05%		26.77%		15.74%
		0.23%		5.37%		8.24%		5.91%		3.91%		1.03%

(1) Excludes loans designated at FVTPL, balances due from customers on acceptances, accrued interest and deferred and unamortised fee income.
(2) Business coverage has been adjusted to exclude government-backed loans.
(3) Stage 3 includes POCI for gross loans and advances of £86m for Mortgages and £4m Personal; and ECL of £Nil for Mortgages and (£2m) for Personal.

Credit quality of loans and advances (continued)

Stage 2 balances

There can be a number of reasons that require a financial asset to be subject to a Stage 2 lifetime ECL calculation other than reaching the 30 DPD backstop. The following table highlights the relevant trigger point leading to a financial asset being classed as Stage 2:

As at 31 March 2021 (unaudited)	**Mortgages**		**Personal: Cards**		**Personal: Loans & Overdrafts**		**Personal: Combined**		**Business[2]**		**Total**	
	£m	**%**	**£m**	**%**	**£m**	**%**	**£m**	**%**	**£m**	**%**	**£m**	**%**
PD deterioration	**5,993**	**83%**	**409**	**68%**	**350**	**98%**	*759*	**79%**	**2,437**	**69%**	**9,189**	**78%**
Forbearance	**182**	**3%**	**15**	**2%**	**3**	**1%**	**18**	**2%**	**339**	**10%**	**539**	**5%**
AFD or Watch List[1]	**11**	**-%**	**-**	**-%**	**-**	**-%**	**-**	**-%**	**631**	**18%**	**642**	**6%**
> 30 DPD	**280**	**4%**	**14**	**2%**	**5**	**1%**	*19*	**2%**	**27**	**1%**	**326**	**3%**
Other[2]	**720**	**10%**	**168**	**28%**	**-**	**-%**	*168*	**17%**	**75**	**2%**	**963**	**8%**
	7,186	**100%**	**606**	**100%**	**358**	**100%**	*964*	**100%**	**3,509**	**100%**	**11,659**	**100%**
ECLs												
PD deterioration	**65**	**68%**	**85**	**59%**	**51**	**93%**	*136*	**67%**	**95**	**51%**	**296**	**62%**
Forbearance	**11**	**11%**	**5**	**3%**	**1**	**2%**	**6**	**3%**	**28**	**15%**	**45**	**9%**
AFD or Watch List[1]	**-**	**-%**	**-**	**-%**	**-**	**-%**	**-**	**-%**	**44**	**24%**	**44**	**9%**
> 30 DPD	**5**	**5%**	**11**	**7%**	**3**	**5%**	*14*	**7%**	**1**	**1%**	**20**	**4%**
Other[2]	**15**	**16%**	**46**	**31%**	**-**	**-%**	*46*	**23%**	**14**	**9%**	**75**	**16%**
	96	**100%**	**147**	**100%**	**55**	**100%**	*202*	**100%**	**182**	**100%**	**480**	**100%**

As at 30 September 2020 (audited)	Mortgages		Personal: Cards		Personal: Loans & Overdrafts		Personal: Combined		Business[2]		Total	
	£m	%	£m	%	£m	%	£m	%	£m	%	£m	%
PD deterioration	7,085	87%	342	66%	293	96%	635	77%	2,883	75%	10,603	82%
Forbearance	174	2%	14	3%	3	1%	17	2%	353	9%	544	4%
AFD or Watch List[1]	13	-%	-	-	-	-	-	-	586	15%	599	5%
> 30 DPD	190	2%	7	1%	6	2%	13	2%	10	-%	213	2%
Other[2]	704	9%	156	30%	2	1%	158	19%	23	1%	885	7%
	8,166	100%	519	100%	304	100%	823	100%	3,855	100%	12,844	100%
ECLs												
PD deterioration	65	68%	86	59%	42	89%	128	66%	103	58%	296	64%
Forbearance	3	3%	5	3%	2	5%	7	4%	31	18%	41	9%
AFD or Watch List[1]	-	-	-	-	-	-	-	-	37	21%	37	8%
> 30 DPD	11	12%	6	4%	3	6%	9	5%	-	-	20	4%
Other[2]	16	17%	50	34%	-	-	50	25%	5	3%	71	15%
	95	100%	147	100%	47	100%	194	100%	176	100%	465	100%

(1) Approaching Financial Difficulty (AFD) and Watch markers are early warning indicators of Business customers who may be approaching financial difficulties. If these indicators are not reversed, they may lead to a requirement for more proactive management by the Group.
(2) Other includes eCRS (internal rating scale) changes as well as a number of smaller value drivers.

Credit quality of loans and advances (continued)

Credit risk exposure, by internal PD rating, by IFRS 9 stage allocation

The distribution of the Group's credit exposures by internal PD rating is analysed below:

		Gross carrying amount			
As at 31 March 2021 (unaudited)		**Stage 1 £m**	**Stage 2 £m**	**Stage 3[(1)] £m**	**Total £m**
Mortgages	**PD range**				
Strong	0 – 0.74	**49,707**	**4,994**	**-**	**54,701**
Good	0.75 – 2.49	**1,019**	**1,308**	**-**	**2,327**
Satisfactory	2.50 – 99.99	**27**	**882**	**-**	**909**
Default	100	**-**	**2**	**681**	**683**
Total		**50,753**	**7,186**	**681**	**58,620**
Personal					
Strong	0 – 2.49	**3,951**	**279**	**-**	**4,230**
Good	2.50 – 9.99	**410**	**489**	**-**	**899**
Satisfactory	10.00 – 99.99	**2**	**196**	**-**	**198**
Default	100	**-**	**-**	**76**	**76**
Total		**4,363**	**964**	**76**	**5,403**
Business					
Strong	0 – 0.74	**670**	**91**	**-**	**761**
Good	0.75 – 9.99	**3,978**	**2,026**	**-**	**6,004**
Satisfactory	10.00 – 99.99	**338**	**1,392**	**-**	**1,730**
Default	100	**-**	**-**	**235**	**235**
Total		**4,986**	**3,509**	**235**	**8,730**

(1) Stage 3 includes POCI of £78m for Mortgages and £3m for Personal.

Of the Group's total loan commitments and financial guarantee contracts of £18,063m, £16,560m (92%) are held under Stage 1 for IFRS 9 purposes, with £1,455m in Stage 2 and £48m in Stage 3. ECLs of £10m (30 September 2020: £7m) are held for undrawn exposures, of which £3m was held under Stage 1 and £7m under Stage 2. In terms of credit quality, 97% of the loan commitments and financial guarantee contracts were classed as either 'Good' or 'Strong' under the Group's internal PD rating scale.

		Gross carrying amount			
As at 30 September 2020 (audited)		Stage 1 £m	Stage 2 £m	Stage 3[(1)] £m	Total £m
Mortgages	**PD range**				
Strong	0 – 0.74	44,038	3,785	-	47,823
Good	0.75 – 2.49	5,246	2,879	-	8,125
Satisfactory	2.50 – 99.99	686	1,502	-	2,188
Default	100	-	-	516	516
Total		49,970	8,166	516	58,652
Personal					
Strong	0 – 2.49	4,144	183	-	4,327
Good	2.50 – 9.99	500	478	-	978
Satisfactory	10.00 – 99.99	16	162	-	178
Default	100	-	-	67	67
Total		4,660	823	67	5,550
Business					
Strong	0 – 0.74	791	152	-	943
Good	0.75 – 9.99	3,674	2,733	-	6,407
Satisfactory	10.00 – 99.99	124	970	-	1,094
Default	100	-	-	279	279
Total		4,589	3,855	279	8,723

(1) Stage 3 includes POCI of £86m for Mortgages and £4m for Personal.

Credit quality of loans and advances (continued)

Reconciliation of movement in gross balances and impairment loss allowance

The following table shows the changes in the loss allowance and gross carrying value of the portfolios. Values are calculated using the individual customer account balances, and the stage allocation is taken as at the end of each month. The monthly position of each account is aggregated to report a net closing position for the period, thereby incorporating all movements an account has made during the year.

	Stage 1		**Stage 2**		**Stage 3**(1)		**Total**	
	Gross		**Gross**		**Gross**		**gross**	**Total**
	loans	**ECL**	**loans**	**ECL**	**loans**	**ECL**	**loans**	**provisions**
March 2021 (unaudited)	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Opening balance at 1 October 2020	**59,219**	**136**	**12,844**	**465**	**862**	**134**	**72,925**	**735**
Transfers from Stage 1 to Stage 2	**(6,081)**	**(38)**	**6,059**	**215**	**-**	**-**	**(22)**	**177**
Transfers from Stage 2 to Stage 1	**5,575**	**24**	**(5,609)**	**(114)**	**-**	**-**	**(34)**	**(90)**
Transfers to Stage 3	**(71)**	**(1)**	**(386)**	**(45)**	**455**	**62**	**(2)**	**16**
Transfers from Stage 3	**19**	**-**	**138**	**14**	**(160)**	**(20)**	**(3)**	**(6)**
Changes to model methodology	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
New assets originated or purchased	**9,175**	**90**	**827**	**61**	**68**	**11**	**10,070**	**162**
Repayments and other movements	**(1,085)**	**(7)**	**(313)**	**(31)**	**9**	**(51)**	**(1,389)**	**(89)**
Repaid or derecognised	**(6,649)**	**(64)**	**(1,901)**	**(85)**	**(185)**	**(30)**	**(8,735)**	**(179)**
Write-offs	**-**	**-**	**-**	**-**	**(57)**	**(57)**	**(57)**	**(57)**
Cash recoveries	**-**	**-**	**-**	**-**	**-**	**15**	**-**	**15**
Individually assessed impairment charge	**-**	**-**	**-**	**-**	**-**	**37**	**-**	**37**
Closing balance at 31 March 2021	**60,102**	**140**	**11,659**	**480**	**992**	**101**	**72,753**	**721**

(1) Stage 3 includes POCI for gross loans and advances of £78m for Mortgages and £3m Personal; and ECL of (£0.4m) for Mortgages and (£1.9m) for Personal.

	Stage 1		Stage 2		Stage 3(1)		Total	
	Gross		Gross		Gross		gross	Total
	loans	ECL	loans	ECL	loans	ECL	loans	provisions
September 2020 (audited)	£m	£m	£m	£m	£m	£m	£m	£m
Opening balance at 1 October 2019	67,925	79	4,514	168	807	115	73,246	362
Transfers from Stage 1 to Stage 2	(14,972)	(81)	9,513	436	-	-	(5,459)	355
Transfers from Stage 2 to Stage 1	5,032	37	(2,813)	(190)	-	-	2,219	(153)
Transfers to Stage 3	(102)	(1)	(328)	(84)	384	129	(46)	44
Transfers from Stage 3	44	-	76	9	(93)	(18)	27	(9)
Changes to model methodology	24	(8)	(24)	(6)	-	-	-	(14)
New assets originated or purchased	18,380	96	1,349	90	150	15	19,879	201
Repayments and other movements	(3,454)	67	2,304	150	40	(49)	(1,110)	168
Repaid or derecognised	(13,658)	(53)	(1,747)	(108)	(267)	(63)	(15,672)	(224)
Write-offs	-	-	-	-	(159)	(159)	(159)	(159)
Cash recoveries	-	-	-	-	-	25	-	25
Individually assessed impairment charge	-	-	-	-	-	139	-	139
Closing balance at 30 September 2020	59,219	136	12,844	465	862	134	72,925	735

(1) Stage 3 includes POCI for gross loans and advances of £86m for Mortgages and £4m Personal; and ECL of £nil for Mortgages and (£2m) for Personal.

Credit risk

Mortgage credit performance

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m	31 Mar 2020 (unaudited) £m
Gross loans and advances	**£58.6bn**	£58.7bn	£59.8bn
Impairment (credit)/charge	**(£1m)**	£95m	£12m
Cost of risk	**0bps**	16bps	4bps
Impairment provision	**£132m**	£131m	£50m
Provision to customer loan ratio	**23bps**	23bps	9bps
% Loans in Stage 2	**12.3%**	13.9%	4.0%
% Loans in Stage 3	**1.2%**	0.9%	0.8%
% Forborne loans	**1.39%**	1.08%	1.06%
90+ DPD	**0.44%**	0.43%	0.36%
LTV of mortgage portfolio	**55.2%**	57.3%	57.1%

Portfolio and impairment

The Group's mortgage lending remained broadly stable at £58.6bn at 31 March 2021, as during the period the Group balanced new lending growth alongside the continuation of support for existing customers.

The mortgage portfolio continues to evidence strong underlying credit performance, with no notable deterioration in asset quality. 90+ DPD arrears of 0.44% (30 September 2020: 0.43%) remains low and less than the market average of 0.9%. Mild deterioration in delinquency has occurred as customers reach the end of payment holiday terms however a moratorium on repossessions has prevented action being taken resulting in a small number of loans being in arrears longer than would typically be expected under normal circumstances. The underlying arrears continue to evidence a stable portfolio, with improving bureau scores and reduced customer indebtedness, accepting that payment holidays will have benefited customers and challenges will remain for some going forward.

Mortgage portfolio performance is supported by early intervention when customer support is needed, prudent risk appetite setting, robust credit underwriting disciplines and a continued focus on responsible lending.

The impairment provision has remained stable at £132m (30 September 2020: £131m), with the provision to customer loan coverage ratio unchanged at 23bps. While the modelled component of the provision has reduced as a result of HPI increases reducing portfolio LTV and the impact of the updated economic scenarios, the overall provision remained stable as the risks in the portfolio remain, particularly until such time as there is greater clarity on the impact of the withdrawal of customer support mechanisms. As a result, a £37m PMA has been raised for ERU, in part offset by a £14m reduction in the payment holiday PMA. The PMA for BTL has been increased by £20m reflecting the potential for the sector to be more susceptible to factors such as higher levels of unemployment adversely affecting rental income (tenant) and consequently customers' (landlord) ability to pay. This level of PMA ensures an appropriate level of provision is held, as the strong, recent default experience and low average LTV resulted in only a modest modelled provision requirement for BTL. A further £1m PMA has been held to reflect the potential impact of cladding remediation on loss expectations. Individually assessed provisions remained stable. The changes in the provision composition reflect the continued resilience of the underlying portfolio but also the risk and uncertainty that remains until greater clarity is obtained on portfolio performance post the phasing down of COVID-19 support mechanisms.

The impairment credit of £1m for the six months to 31 March 2021 is a significant reduction from the £95m charge in the year to 30 September 2020. This reflects the additional ECL charge recognised during FY20 in respect of future losses and the muted emergence of default and loss in the mortgage portfolio to date.

Credit risk

Mortgage credit performance (continued)

IFRS 9 staging	**Stage 1**		**Stage 2**		**Stage 3(1)**			
March 2021 (unaudited)	**Gross loans £m**	**ECL £m**	**Gross loans £m**	**ECL £m**	**Gross loans £m**	**ECL £m**	**Total gross loans £m**	**Total provisions £m**
Opening balance at 1 October 2020	**49,970**	**14**	**8,166**	**95**	**516**	**22**	**58,652**	**131**
Transfers from Stage 1 to Stage 2	**(4,261)**	**(2)**	**4,250**	**56**	**-**	**-**	**(11)**	**54**
Transfers from Stage 2 to Stage 1	**4,411**	**3**	**(4,434)**	**(50)**	**-**	**-**	**(23)**	**(47)**
Transfers to Stage 3	**(39)**	**-**	**(250)**	**(6)**	**288**	**4**	**(1)**	**(2)**
Transfers from Stage 3	**11**	**-**	**53**	**8**	**(67)**	**(2)**	**(3)**	**6**
Changes to model methodology	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
New assets originated or purchased	**4,372**	**1**	**56**	**1**	**-**	**-**	**4,428**	**2**
Repayments and other movements	**(522)**	**(1)**	**(45)**	**(1)**	**(3)**	**-**	**(570)**	**(2)**
Repaid or derecognised	**(3,189)**	**(1)**	**(610)**	**(7)**	**(52)**	**(1)**	**(3,851)**	**(9)**
Write-offs	**-**	**-**	**-**	**-**	**(1)**	**(1)**	**(1)**	**(1)**
Cash recoveries	**-**	**-**	**-**	**-**	**-**	**1**	**-**	**1**
Individually assessed impairment charge	**-**	**-**	**-**	**-**	**-**	**(1)**	**-**	**(1)**
Closing balance at 31 March 2021	**50,753**	**14**	**7,186**	**96**	**681**	**22**	**58,620**	**132**

(1) Stage 3 includes POCI for gross loans and advances of £78m and ECL of (£0.4m).

September 2020 (audited)	Stage 1		Stage 2		Stage 3(1)			
	Gross loans £m	ECL £m	Gross loans £m	ECL £m	Gross loans £m	ECL £m	Total gross loans £m	Total provisions £m
Opening balance at 1 October 2019	58,120	6	1,805	9	466	25	60,391	40
Transfers from Stage 1 to Stage 2	(10,390)	(10)	4,976	75	-	-	(5,414)	65
Transfers from Stage 2 to Stage 1	3,525	3	(1,260)	(17)	-	-	2,265	(14)
Transfers to Stage 3	(63)	-	(69)	(6)	86	13	(46)	7
Transfers from Stage 3	38	-	24	3	(34)	(6)	28	(3)
Changes to model methodology	-	-	-	-	-	-	-	-
New assets originated or purchased	6,981	1	16	-	3	-	7,000	1
Repayments and other movements	(2,018)	15	2,784	32	32	(6)	798	41
Repaid or derecognised	(6,223)	(1)	(110)	(1)	(34)	(4)	(6,367)	(6)
Write-offs	-	-	-	-	(3)	(3)	(3)	(3)
Cash recoveries	-	-	-	-	-	-	-	-
Individually assessed impairment charge	-	-	-	-	-	3	-	3
Closing balance at 30 September 2020	49,970	14	8,166	95	516	22	58,652	131

(1) Stage 3 includes POCI for gross loans and advances of £86m and ECL of £Nil.

The application of more positive economic forecasts has increased the level of mortgage lending classed as Stage 1 to 86.6% (30 September 2020: 85.2%). This increase is driven by the improvement in PDs and has led to a corresponding decrease of 1.6% in Stage 2 to 12.3% (30 September 2020: 13.9%).

Mortgage IFRS 9 PDs are driven by underlying internal credit scores adjusted for forward-looking macroeconomics. Of the Stage 2 mortgage balances, 83% are as a result of PD deterioration influenced by revised macroeconomic forecasts. The changes in PD grades observed at 31 March 2021 do not reflect any material movement in underlying portfolio quality but rather the migration to more positive macroeconomic forecasts. This has also resulted in an increase from 81% (30 September 2020) to 93% of assets classed as ‘Strong’, with over 97% of the mortgage portfolio now classed as ‘Good’ or ‘Strong’.

The proportion of mortgages classified as Stage 3 remains modest at 1.2% (30 September 2020: 0.9%).

Mortgage credit performance (continued)

Collateral and LTV

March 2021 (unaudited)	**Stage 1**			**Stage 2**			**Stage 3[(2)]**			**Total**		
LTV[(1)]	**Loans £m**	**%**	**ECL £m**	**Loans £m**	**%**	**ECL £m**	**Loans £m**	**%**	**ECL £m**	**Loans £m**	**%**	**ECL £m**
Less than 50%	**20,498**	**40%**	**1**	**2,594**	**36%**	**8**	**285**	**42%**	**4**	**23,377**	**40%**	**13**
50% to 75%	**23,918**	**47%**	**5**	**3,425**	**48%**	**43**	**276**	**40%**	**6**	**27,619**	**47%**	**54**
76% to 80%	**2,830**	**6%**	**2**	**491**	**7%**	**12**	**42**	**6%**	**2**	**3,363**	**6%**	**16**
81% to 85%	**2,419**	**5%**	**3**	**415**	**6%**	**14**	**32**	**5%**	**3**	**2,866**	**5%**	**20**
86% to 90%	**968**	**2%**	**2**	**223**	**3%**	**10**	**15**	**2%**	**2**	**1,206**	**2%**	**14**
91% to 95%	**73**	**-%**	**-**	**28**	**-%**	**2**	**8**	**1%**	**1**	**109**	**-%**	**3**
96% to 100%	**9**	**-%**	**-**	**2**	**-%**	**1**	**5**	**1%**	**-**	**16**	**-%**	**1**
Greater than 100%	**38**	**-%**	**1**	**8**	**-%**	**6**	**18**	**3%**	**4**	**64**	**-%**	**11**
	50,753	**100%**	**14**	**7,186**	**100%**	**96**	**681**	**100%**	**22**	**58,620**	**100%**	**132**

(1) LTV of the mortgage portfolio is defined as mortgage portfolio weighted by balance. The portfolio is indexed using the MIAC Acadametrics indices at a given date.
(2) Stage 3 includes £78m of POCI gross loans and advances.

September 2020 (audited)	Stage 1			Stage 2			Stage 3[(1)]			Total		
LTV	Loans £m	%	ECL £m	Loans £m	%	ECL £m	Loans £m	%	ECL £m	Loans £m	%	ECL £m
Less than 50%	18,495	37%	2	2,705	33%	6	214	41%	4	21,414	37%	12
50% to 75%	23,215	46%	5	3,754	46%	40	192	37%	6	27,161	46%	51
76% to 80%	2,896	6%	1	641	8%	12	33	7%	2	3,570	6%	15
81% to 85%	2,336	5%	2	437	6%	12	21	4%	2	2,794	5%	16
86% to 90%	2,131	4%	2	428	5%	15	19	4%	2	2,578	4%	19
91% to 95%	798	2%	1	170	2%	8	9	2%	1	977	2%	10
96% to 100%	56	-%	-	21	-%	1	6	1%	1	83	-%	2
Greater than 100%	43	-%	1	10	-%	1	22	4%	4	75	-%	6
	49,970	100%	14	8,166	100%	95	516	100%	22	58,652	100%	131

(1) Stage 3 includes £86m of POCI gross loans and advances

The mortgage portfolio remains very well secured with 87% of mortgages, by loan value, having an indexed LTV less than 75% (30 September 2020: 83%), and an average portfolio LTV of 55.2% (30 September 2020: 57.3%). There are only £189m of loans with an LTV greater than 90%, which represents 0.3% of the portfolio (30 September 2020: 2%) whilst the proportion over 80% LTV has reduced to 7% as at 31 March 2021 (30 September 2020: 11%) reflecting the extent to which property prices have shown resilience during the past six months with strong demand and support, for example in the form of the Stamp Duty holiday which has been extended through to 30 June 2021.

Mortgage credit performance (continued)

Payment holidays

31 March 2021 (unaudited)	**Payment holidays granted to date**		**Payment holidays currently in force at 31 March 2021**		**Of matured payment holidays**	
	Total balances £m	**% of Total balances**	**Total balances £m**	**% of Total balances**	**% Resumed repayment**	**% Further treatment/ arrears**
Mortgages	**12,256**	**21%**	**377**	**1%**	**94%**	**6%**

30 September 2020 (audited)	Payment holidays granted to date		Payment holidays currently in force at 30 September 2020		Of matured payment holidays	
	Total balances £m	% of Total balances	Total balances £m	% of Total balances	% Resumed repayment	% Further treatment/ arrears
Mortgages	11,908	20%	2,525	4%	98%	2%

21% of mortgage customers, by balance, applied for and were granted a payment holiday. Of the payment holidays which have matured by 31 March 2021, 94% of customers have resumed payment in line with previously contracted terms with only 6% requiring further support or having moved into arrears. Only 1% of customers, by balance, have an active payment holiday in force at 31 March 2021. The Group will continue to support customers in line with their needs and revised regulatory guidance.

Mortgage credit performance (continued)

Forbearance

In dealing with the exceptional challenges posed by COVID-19 and to ensure the appropriate delivery of customer support, a number of concessions have been granted in response to the short-term financial consequences for customers in line with regulatory guidance, including for example payment holidays. These measures are not considered to be forbearance, as confirmed by the regulatory guidance, and have not been reflected in the Group's forbearance disclosures up to and including 31 March 2021. Where underlying, longer-term financial difficulties that are not COVID-19 related are evident the Group's normal forbearance assessment applies, which includes using judgement in assessing whether SICR, an impairment or default event has occurred.

The Group utilises tailored forbearance measures for mortgage customers, specific to the individual customer and their circumstances. Customers may potentially be subject to more than one forbearance strategy at any one time where this is considered to be the most appropriate course of action.

The table below summarises the level of forbearance in respect of the Group's mortgage portfolio at each balance sheet date. All balances subject to forbearance are classed as either Stage 2 or Stage 3 for ECL purposes.

	Total loans and advances subject to forbearance measures			Impairment allowance on loans and advances subject to forbearance measures	
As at 31 March 2021 (unaudited)	**Number of loans**	**Gross carrying amount £m**	**% of total portfolio**	**Impairment allowance £m**	**Coverage %**
Formal arrangements	**1,123**	**132**	**0.23**	**6.3**	**4.75**
Temporary arrangements	**734**	**104**	**0.18**	**5.3**	**5.11**
Payment arrangement	**1,677**	**158**	**0.27**	**1.2**	**0.73**
Payment holiday	**1,417**	**136**	**0.23**	**1.0**	**0.70**
Interest only conversion	**1,222**	**256**	**0.44**	**1.3**	**0.49**
Term extension	**133**	**11**	**0.02**	**0.1**	**0.71**
Other	**24**	**2**	**-**	**-**	**1.07**
Legal	**127**	**12**	**0.02**	**0.9**	**7.73**
Total mortgage forbearance	**6,457**	**811**	**1.39**	**16.1**	**1.97**
As at 30 September 2020 (audited)					
Formal arrangements	1,194	145	0.25	7.2	4.94
Temporary arrangements	792	100	0.17	5.2	5.21
Payment arrangement	1,475	141	0.24	2.8	1.96
Payment holiday	1,454	157	0.26	2.3	1.45
Interest only conversion	379	64	0.11	0.4	0.58
Term extension	163	13	0.02	0.1	0.89
Other	28	3	0.01	-	1.13
Legal	136	13	0.02	1.0	7.87
Total mortgage forbearance	5,621	636	1.08	19.0	2.98

A key indicator of underlying mortgage portfolio health is the level of loans subject to forbearance measures. As at 31 March 2021, forbearance totalled £811m (6,457 customers), an increase from the 30 September 2020 position of £636m (5,621 customers). This represents 1.39% of total mortgage balances (30 September 2020: 1.08%) and is primarily driven by temporary interest only conversion. This concession has been offered to support those customers who, in reaching the end of their payment deferral term, continued to experience short-term financial difficulty or who opted to make a partial payment rather than full payment deferral. Payment deferrals granted in line with regulation have not been classified as forbearance.

When all other avenues of resolution, including forbearance, have been explored, the Group will take steps to repossess and sell underlying collateral. In the six months to 31 March 2021, there were 13 repossessions of which 7 were voluntary (12 months to 30 September 2020: 57 including 21 voluntary). The key driver of the significant reduction is the possession moratorium, part of the government's measures to support borrowers throughout the COVID-19 pandemic.

Credit risk

Personal credit performance

	31 March 2021 (unaudited)			30 September 2020 (audited)			31 March 2020 (unaudited)		
	Credit cards	**Loans & overdrafts**	**Total Personal**	Credit cards	Loans & overdrafts	Total personal	Credit cards	Loans & overdrafts	Total personal
Gross loans and advances	**£4.3bn**	**£1.1bn**	**£5.4bn**	£4.5bn	£1.1bn	£5.6bn	£4.3bn	£1.2bn	£5.5bn
Impairment charge	**£27m**	**-**	**£27m**	£153m	£70m	£223m	£82m	£18m	£100m
Cost of risk	**128bps**	**9bps**	**107bps**	355bps	721bps	423bps	381bps	355bps	376bps
Impairment provision	**£219m**	**£74m**	**£293m**	£222m	£79m	£301m	£193m	£38m	£231m
Provision to customer loan ratio	**550bps**	**839bps**	**603bps**	537bps	824bps	591bps	456bps	371bps	440bps
% Loans in Stage 2	**14.0%**	**33.9%**	**17.6%**	11.6%	28.0%	14.8%	9.5%	4.3%	8.5%
% Loans in Stage 3	**1.4%**	**1.3%**	**1.4%**	1.2%	1.4%	1.2%	1.3%	1.4%	1.3%
% Forborne loans	**0.85%**	**0.93%**	**0.87%**	0.63%	0.88%	0.67%	0.61%	1.08%	0.75%
90+ DPD	**0.63%**	**0.72%**	**0.65%**	0.38%	0.52%	0.41%	0.59%	0.73%	0.61%

Portfolio and impairment

Of the £5.4bn total personal lending, credit cards continue to represent the majority at £4.3bn, with the remaining balance comprising personal loans and overdrafts. The reduction in portfolio balance partly reflects the challenging market environment, plus risk appetite revisions along with muted customer demand impacting new lending origination. Customers' prudent actions in response to COVID-19 have resulted in pay down of lending where they have been able to do so, with this deleveraging increasing asset quality across the personal portfolios.

The impairment provision has reduced by £8m to £293m at 31 March 2021, however the provision coverage ratio increased by 12bps from 591bps to 603bps, driven by the reduction in portfolio balance. Modelled ECL has increased by £36m to £226m with the positive impact of the revised economic scenarios being offset by model updates, including an adjustment to the modelled default rate for personal loans to better reflect the potential for an increase in defaults across this portfolio. PMAs have reduced by £44m, in part due to the model adjustment for the personal loan default replacing a previously held PMA and also as a result of the PMA for payment holidays, and their consequential impact on bureau data, unwinding as the level of outstanding payment holidays has reduced. A £26m ERU PMA has been introduced for the credit cards portfolio to reflect the uncertainty on portfolio performance and modelled ECL that remains until customer support mechanisms are withdrawn.

Arrears levels remain modest as customers continue to behave responsibly and benefit from the various forms of support, including payment holidays. Asset quality has been assisted by the credit strategies deployed during the year to control and, where determined, tighten origination controls. New lending continues to focus on segments with lower levels of economic volatility with portfolio level exposures to non-homeowners, lower age demographics and self-employed remaining low, driving record low early month on book arrears. While modest, 90+ DPD measures have increased to 0.65% in the six months to 31 March 2020 (30 September 2020: 0.41%), reflective of the vast majority of payment holidays ending and a small number of customers entering arrears when those have come to an end.

The impairment charge of £27m for the six months to 31 March 2021 is a significant reduction from the £223m in the year to 30 September 2020 given the additional ECL charge recognised during FY20 in respect of future estimated losses. Together with cost of risk of 107bps (30 September 2020: 423bps), this reflects the muted emergence of default and loss across the personal portfolios to date.

Credit risk

Personal credit performance (continued)

IFRS 9 staging

March 2021 (unaudited)	**Stage 1 Gross loans £m**	**Stage 1 ECL £m**	**Stage 2 Gross loans £m**	**Stage 2 ECL £m**	**Stage 3[1] Gross loans £m**	**Stage 3[1] ECL £m**	**Total gross loans £m**	**Total provisions £m**
Opening balance at 1 October 2020	**4,660**	**70**	**823**	**194**	**67**	**37**	**5,550**	**301**
Transfers from Stage 1 to Stage 2	**(544)**	**(20)**	**541**	**118**	**-**	**-**	**(3)**	**98**
Transfers from Stage 2 to Stage 1	**246**	**7**	**(256)**	**(33)**	**-**	**-**	**(10)**	**(26)**
Transfers to Stage 3	**(11)**	**(1)**	**(49)**	**(32)**	**60**	**43**	**-**	**10**
Transfers from Stage 3	**1**	**-**	**1**	**1**	**(3)**	**(3)**	**(1)**	**(2)**
Changes to model methodology	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
New assets originated or purchased	**596**	**9**	**8**	**1**	**-**	**-**	**604**	**10**
Repayments and other movements	**(487)**	**(8)**	**(78)**	**(41)**	**12**	**(26)**	**(553)**	**(75)**
Repaid or derecognised	**(98)**	**(3)**	**(26)**	**(6)**	**(14)**	**(14)**	**(138)**	**(23)**
Write-offs	**-**	**-**	**-**	**-**	**(46)**	**(46)**	**(46)**	**(46)**
Cash recoveries	**-**	**-**	**-**	**-**	**-**	**12**	**-**	**12**
Individually assessed impairment charge	**-**	**-**	**-**	**-**	**-**	**34**	**-**	**34**
Closing balance at 31 March 2021	**4,363**	**54**	**964**	**202**	**76**	**37**	**5,403**	**293**

September 2020 (audited)	Stage 1 Gross loans £m	Stage 1 ECL £m	Stage 2 Gross loans £m	Stage 2 ECL £m	Stage 3[1] Gross loans £m	Stage 3[1] ECL £m	Total gross loans £m	Total provisions £m
Opening balance at 1 October 2019	4,787	53	424	87	69	35	5,280	175
Transfers from Stage 1 to Stage 2	(1,326)	(47)	1,356	270	-	-	30	223
Transfers from Stage 2 to Stage 1	723	29	(768)	(151)	-	-	(45)	(122)
Transfers to Stage 3	(23)	(1)	(110)	(65)	135	96	2	30
Transfers from Stage 3	2	-	3	2	(6)	(5)	(1)	(3)
Changes to model methodology	24	(8)	(24)	(6)	-	-	-	(14)
New assets originated or purchased	1,621	26	5	1	1	-	1,627	27
Repayments and other movements	(925)	23	(45)	62	36	(52)	(934)	33
Repaid or derecognised	(223)	(5)	(18)	(6)	(40)	(36)	(281)	(47)
Write-offs	-	-	-	-	(128)	(128)	(128)	(128)
Cash recoveries	-	-	-	-	-	23	-	23
Individually assessed impairment charge	-	-	-	-	-	104	-	104
Closing balance at 30 September 2020	4,660	70	823	194	67	37	5,550	301

The balance of personal lending in Stage 2 increased by 3.0% to 17.8% (30 September 2020: 14.8%), driven by technical changes to the SICR criteria for credit cards and to a model change for personal loans. This resulted in a corresponding reduction in Stage 1 from 84.0% to 80.8% while Stage 3 personal lending remains modest and stable at 1.4% (30 September 2020: 1.2%).

Personal portfolio PD is most sensitive to the rate of unemployment, which is forecast to peak at c.9%. This forecast assumption results in a deterioration in PD and, of the Stage 2 personal balance, 79% results from PD deterioration.

Personal credit performance (continued)

Payment holidays

31 March 2021 (unaudited)	Payment holidays granted to date		Payment holidays currently in force at 31 March 2021		Of matured payment holidays	
	Total balances £m	**% of Total balances**	**Total balances £m**	**% of Total balances**	**% Resumed repayment**	**% Further treatment/ arrears**
Credit cards	**267**	**7%**	**28**	**1%**	**87%**	**13%**
Loans and overdrafts	**120**	**14%**	**5**	**1%**	**90%**	**10%**

30 September 2020 (audited)	Payment holidays granted to date		Payment holidays currently in force at 30 September 2020		Of matured payment holidays	
	Total balances £m	% of Total balances	Total balances £m	% of Total balances	% Resumed repayment	% Further treatment/ arrears
Credit cards	219	5%	31	1%	92%	8%
Loans and overdrafts	103	11%	26	3%	95%	5%

By balance, 7% of credit card customers were granted a payment holiday. Where those holidays have matured, 87% of customers have reverted to repay in line with previously contracted terms and 13% have either sought additional support or fallen into arrears. Of the 14% of personal loan and overdraft customers granted a payment holiday, 90% of those which have matured have reverted to normal terms with 10% seeking further support or in arrears. 1% of both credit cards and personal loan customers had an active payment holiday arrangement in place at 31 March 2021. The Group will continue to support customers in line with their needs and revised regulatory guidance.

Forbearance

The table below summarises the level of forbearance in respect of the Group's personal portfolios at each balance sheet date. All balances subject to forbearance are classed as either Stage 2 or Stage 3 for ECL purposes.

As at 31 March 2021 (unaudited)	Total loans and advances subject to forbearance measures			Impairment allowance on loans and advances subject to forbearance measures	
	Number of loans	**Gross carrying amount £m**	**% of total portfolio**	**Impairment allowance £m**	**Coverage %**
Credit cards arrangements	**8,007**	**35**	**0.85%**	**17.5**	**49.95%**
Loans arrangements	**1,297**	**7**	**0.87%**	**4.9**	**67.79%**
Overdraft arrangements	**287**	**1**	**2.63%**	**0.3**	**33.41%**
Total personal forbearance	**9,591**	**43**	**0.87%**	**22.7**	**52.62%**
As at 30 September 2020 (audited)					
Credit cards arrangements	6,309	27	0.63%	12.5	47.23%
Loans arrangements	1,385	7	0.82%	3.2	42.42%
Overdraft arrangements	398	1	2.48%	0.3	26.39%
Total personal forbearance	8,092	35	0.67%	16.0	45.63%

As at 31 March 2021, credit cards forbearance totalled £35m (8,007 customers), an increase from the 30 September 2020 position of £27m (6,309 customers). This represents 0.85% of total credit cards balances (30 September 2020: 0.63%). The increase in credit cards forbearance is the result of payment arrangements being extended to customers who have come to the end of their payment holiday term and require additional short-term support. The level of impairment coverage on forborne loans has increased to 49.9% from 47.2% at 30 September 2020 reflecting a more prudent approach to ECL. Limited forbearance is exercised in relation to personal loans and overdrafts, with a modest reduction to £8.1m (0.93% of the loans and overdrafts portfolio) from £8.4m (0.88%) at 30 September 2020. Payment holidays granted in line with regulation have not been classified as forbearance.

Credit risk

Business credit performance

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m	31 Mar 2020 (unaudited) £m
Gross loans and advances	**£8.8bn**[(1)]	£8.7bn	£8.3bn
Impairment charge	**£12m**	£183m	£120m
Cost of risk	**26bps**	212bps	289bps
Impairment provision	**£296m**	£303m	£261m
Provision to customer loan ratio[(2)]	**398bps**	391bps	323bps
% Loans in Stage 2	**40.2%**	44.2%	29.6%
% Loans in Stage 3	**2.7%**	3.2%	3.3%
% Forborne loans	**5.45%**	5.92%	6.00%
90+ DPD	**0.24%**	0.27%	0.51%

(1) Inclusive of government-backed loan schemes.
(2) Coverage ratio excludes government-backed loan schemes.

Portfolio and impairment

Business lending has remained stable at £8.8bn as at 31 March 2021. This includes lending under government-backed loan schemes, which, in aggregate, now totals £1.4bn.

There has been no deterioration in underlying asset quality performance and, as yet, no observed increase in impairment or specific provision recognition. The Group entered the pandemic with a defensively positioned portfolio biased away from sectors likely to experience more disruption such as hospitality and retail, towards sectors expected to be resilient, such as agriculture and health and social care. This portfolio distribution remains.

The impairment provision has remained broadly stable at £296m as at 31 March 2021 (30 September 2020: £303m). The modelled ECL for business lending reduced due to the updated composition and weighting of the economic scenarios. However, a £58m PMA has been introduced for business lending, which includes £21m for real estate exposures to offset the reduction in modelled provision resulting from the economic scenario update. Given the sectoral risk inherent with real estate a PMA for the limited exposure to this sector is considered appropriate to avoid a reduction in provision at this stage in the COVID-19 cycle. The remaining PMA is primarily made up of £30m for ERU, which has been applied to reflect the concern that the impact on customers has been suppressed by the government support schemes and other mechanisms which have underpinned customer liquidity such as HMRC, rent, and rates deferrals etc where payments will once again fall due. The individually assessed provisions for Business have reduced due to the utilisation or release of a small number of provisions as losses have crystallised or recoveries have been achieved. The combination of modelled ECL, PMA and individually assessed provisions results in provision coverage for business lending of 398bps, marginally higher than the 391bps at September 2020, and ensures suitable provision coverage is maintained while the COVID-19 support mechanisms are withdrawn and the uncertainty this has on the improving view of the economic outlook is removed. The coverage ratio also reflects historically selective risk appetite choices which have limited the Group's exposures to more sensitive sectors such as hospitality, retail, travel, construction and real estate. While the Group has yet to see the emergence of increased default or arrears experience, coverage is reflective of the expected impact of COVID-19 through increased PDs including migrations from 12-month to lifetime loss coverage.

Asset quality continues to be influenced by the extended support provided to customers, including government-backed loan schemes, the Group's prudent risk appetite and credit frameworks which seek to ensure early identification of customers in difficulty. The early identification and escalation of customers evidencing deteriorating positions ensures the Group is intervening early and providing appropriate types of support to changing customer circumstances.

Arrears measures are stable to improving, with 90+ DPD of 0.24% at 31 March 2021 (30 September 2020: 0.27%). Over the course of the first half of the financial year, the proportion of business lending classed as categorised (watch, default and impaired), by value, has remained stable at 8.6% of the total business book. The Group has clear strategies in place to work with customers experiencing or likely to experience financial difficulty and the proportions highlighted the lack of significant increase in the value and volume of customers evidencing financial distress up to this point.

The impairment charge for the six months to 31 March 2021 was £12m giving a cost of risk of 26bps.

Business credit performance (continued)

IFRS 9 staging

March 2021 (unaudited)	Stage 1 Gross loans £m	Stage 1 ECL £m	Stage 2 Gross loans £m	Stage 2 ECL £m	Stage 3(1) Gross loans £m	Stage 3(1) ECL £m	Total gross loans £m	Total provisions £m
Opening balance at 1 October 2020	**4,589**	**52**	**3,855**	**176**	**279**	**75**	**8,723**	**303**
Transfers from Stage 1 to Stage 2	**(1,276)**	**(16)**	**1,268**	**41**	**-**	**-**	**(8)**	**25**
Transfers from Stage 2 to Stage 1	**918**	**14**	**(919)**	**(31)**	**-**	**-**	**(1)**	**(17)**
Transfers to Stage 3	**(21)**	**-**	**(87)**	**(7)**	**107**	**15**	**(1)**	**8**
Transfers from Stage 3	**7**	**-**	**84**	**5**	**(90)**	**(15)**	**1**	**(10)**
Changes to model methodology	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
New assets originated or purchased	**4,207**	**80**	**763**	**59**	**68**	**11**	**5,038**	**150**
Repayments and other movements	**(76)**	**2**	**(190)**	**11**	**-**	**(25)**	**(266)**	**(12)**
Repaid or derecognised	**(3,362)**	**(60)**	**(1,265)**	**(72)**	**(119)**	**(15)**	**(4,746)**	**(147)**
Write-offs	**-**	**-**	**-**	**-**	**(10)**	**(10)**	**(10)**	**(10)**
Cash recoveries	**-**	**-**	**-**	**-**	**-**	**2**	**-**	**2**
Individually assessed impairment charge	**-**	**-**	**-**	**-**	**-**	**4**	**-**	**4**
Closing balance at 31 March 2021	**4,986**	**72**	**3,509**	**182**	**235**	**42**	**8,730**	**296**

September 2020 (audited)	Stage 1 Gross loans £m	Stage 1 ECL £m	Stage 2 Gross loans £m	Stage 2 ECL £m	Stage 3(1) Gross loans £m	Stage 3(1) ECL £m	Total gross loans £m	Total provisions £m
Opening balance at 1 October 2019	5,018	20	2,285	72	272	55	7,575	147
Transfers from Stage 1 to Stage 2	(3,256)	(24)	3,181	91	-	-	(75)	67
Transfers from Stage 2 to Stage 1	784	5	(785)	(22)	-	-	(1)	(17)
Transfers to Stage 3	(16)	-	(149)	(13)	163	20	(2)	7
Transfers from Stage 3	4	-	49	4	(53)	(7)	-	(3)
Changes to model methodology	-	-	-	-	-	-	-	-
New assets originated or purchased	9,778	69	1,328	89	146	15	11,252	173
Repayments and other movements	(511)	29	(435)	56	(28)	9	(974)	94
Repaid or derecognised	(7,212)	(47)	(1,619)	(101)	(193)	(23)	(9,024)	(171)
Write-offs	-	-	-	-	(28)	(28)	(28)	(28)
Cash recoveries	-	-	-	-	-	2	-	2
Individually assessed impairment charge	-	-	-	-	-	32	-	32
Closing balance at 30 September 2020	4,589	52	3,855	176	279	75	8,723	303

The application of more positive economic forecasts has increased the level of business lending classed as Stage 1 to 57.1% (30 September 2020: 52.6%), with a corresponding decrease of 4.0% in Stage 2 to 40.2% (30 September 2020: 44.2%). The proportion of the portfolio in Stage 2 does remain heightened, reflective of the Group's prudent assumptions. Business migration to Stage 2 can result from a range of triggers. As at 31 March 2021, 69% of balances in Stage 2 are associated with a deterioration in PD. Business loans in Stage 3 remain modest with a slight reduction at 2.7% (30 September 2020: 3.2%).

The PDs for business lending combine both internal ratings information and forward-looking economic forecasts. The positive economic forecasts, which include a modest GDP rise in 2021 and a stronger recovery, are the material drivers of the PD and stage migrations in the six months to 31 March 2021. The improvements in PD and staging have not been driven to any material extent by the lack of observed impairment through either internal downgrades or the emergence of arrears or defaults. Model changes within the Business portfolio have driven a retiming of expected default risk, with higher short-term default rates but lower cumulative default expectations. This has led to a reduction in the proportion of assets classed as 'Strong' to 9% (30 September 2020: 11%), with assets classed as 'Good' also decreasing to 69% (30 September 2020: 73%). Over 78% of the business portfolio still remains 'Good' or better.

Business credit performance (continued)

Government-backed loan schemes

The Group was an accredited lender in the three UK Government backed loan schemes launched in 2020 and continued to lend under these schemes to eligible customers until their closure on 31 March 2021. These were:

- BBLS: for loans of between £2,000 and £50,000 with a fixed rate of lending available for up to ten years, with no repayments due in the first year. The UK Government guarantees 100% of the lending;
- CBILS: for loans of over £50,000 to a maximum of £5m, with a variable rate of lending and available for a maximum loan term of six years. The UK Government guarantees 80% of the lending; and
- CLBILS: for loans of over £50,000, up to a maximum of £200m (in aggregate) with a variable rate of lending and terms of between three months and three years. The UK Government guarantees 80% of the lending.

The Group has the following lending under these schemes:

31 March 2021 (unaudited)	**No of customers**	**Drawn balance (£m)**	**Average loan size (£m)**	**% of total Business lending**
BBLs	**33,646**	**971**	**0.03**	**c11%**
CBILs	**1,081**	**414**	**0.38**	**c5%**
CLBILs	**5**	**35**	**6.99**	**Immaterial**

30 September 2020 (audited)	No of customers	Drawn balance (£m)	Average loan size (£m)	% of total Business lending
BBLs	28,077	809	0.03	9%
CBILs	907	334	0.37	3%
CLBILs	3	20	6.59	Immaterial

As part of the March 2021 Budget, the UK Government announced that a new scheme (the Recovery Loan Scheme) will replace the three existing schemes from 6 April 2021. The new scheme provides an 80% UK Government guarantee, with lending limits of £10m and no personal guarantees to be taken on facilities of up to £250,000. The Group is an accredited lender to this new scheme, which is set to remain open for applications until 31 December 2021.

Payment holidays

In addition to the above UK Government-backed lending, the Group has also provided capital repayment holidays to those customers whose businesses were financially impacted by economic measures imposed throughout the UK as a result of COVID-19:

	Payment holidays granted to date		**Payment holidays currently in force at 31 March 2021**		**Of matured payment holidays**	
31 March 2021 (unaudited)	**Total balances £m**	**% of Total balances**	**Total balances £m**	**% of Total balances**	**% Resumed repayment**	**% Further treatment/ arrears**
Business	**2,097**	**23%**	**195**	**1%**	**96%**	**4%**

	Payment holidays granted to date		Payment holidays currently in force at 30 September 2020		Of matured payment holidays	
30 September 2020 (audited)	Total balances £m	% of Total balances	Total balances £m	% of Total balances	% Resumed repayment	% Further treatment/ arrears
Business	2,072	23%	108	1%	98%	2%

23% of eligible customers took advantage of a repayment holiday and, of those which have matured, 96% have returned to regular payment by 31 March 2021 (30 September 2020: 98%). Only 1% of business customer balances, equating to £195m, have an active payment holiday in force at 31 March 2021 (30 September 2020: 1% and £108m). Of the initial population granted a holiday, 4% have sought further support or have fallen into arrears. The Group will continue to support customers in line with their needs and revised regulatory guidance.

Business credit performance (continued)

Forbearance

Forbearance is considered to exist where customers are experiencing or about to experience financial difficulty and the Group grants a concession on a non-commercial basis. The Group reports business forbearance at a customer level and at a value which incorporates all facilities and the related impairment allowance, irrespective of whether each individual facility is subject to forbearance. Authority to grant forbearance measures for business customers is held by the Group's Strategic Business Services unit and is exercised, where appropriate, on the basis of detailed consideration of the customer's financial position and prospects.

Where a customer is part of a larger group, forbearance is exercised and reported across the Group at the individual entity level. Where modification of the terms and conditions of an exposure meeting the criteria for classification as forbearance results in derecognition of loans and advances from the balance sheet and the recognition of a new exposure, the new exposure shall be treated as forborne.

The tables below summarise the total number of arrangements in place and the loan balances and impairment provisions associated with those arrangements. All balances subject to forbearance are classed as either Stage 2 or Stage 3 for ECL purposes.

	Total loans and advances subject to forbearance measures			Impairment allowance on loans and advances subject to forbearance measures	
As at 31 March 2021 (unaudited)	**Number of loans**	**Gross carrying amount £m**	**% of total portfolio**	**Impairment allowance £m**	**Coverage %**
Term extension	**192**	**188**	**2.09%**	**12.1**	**6.45%**
Deferral of contracted capital repayments	**89**	**111**	**1.23%**	**13.1**	**11.82%**
Reduction in contracted interest rate	**1**	**1**	**0.01%**	**-**	**2.14%**
Alternative forms of payment	**1**	**-**	**-**	**-**	**64.36%**
Debt forgiveness	**2**	**4**	**0.04%**	**0.1**	**1.53%**
Refinancing	**13**	**5**	**0.06%**	**1.5**	**30.34%**
Covenant breach/reset/waiver	**51**	**182**	**2.02%**	**26.4**	**14.49%**
Total business forbearance	**349**	**491**	**5.45%**	**53.2**	**10.85%**
As at 30 September 2020 (audited)					
Term extension	199	211	2.31%	27.5	13.05%
Deferral of contracted capital repayments	92	115	1.26%	23.1	20.08%
Reduction in contracted interest rate	2	1	0.01%	0.1	6.75%
Alternative forms of payment	1	-	-	-	64.36%
Debt forgiveness	2	4	0.05%	0.2	4.66%
Refinancing	15	6	0.07%	1.8	29.37%
Covenant breach/reset/waiver	57	202	2.22%	24.4	12.10%
Total business forbearance	368	539	5.92%	77.1	14.30%

Business portfolio forbearance has reduced from £539m (368 customers) at 30 September 2020 to £491m (349 customers) at 31 March 2021. Forbearance remains an important metric, reflecting the volume and value of concessions granted to customers on a non-commercial basis. Moves in forbearance reflect the proportion of business customers requiring support on non-standard terms and evidencing financial difficulty. As a percentage of the business portfolio, forborne balances have reduced to 5.45% (30 September 2020: 5.92%) with impairment coverage, in line with actions taken on ECLs, also reducing to 10.85% (30 September 2020: 14.30%). The majority of forbearance arrangements relate to term extensions allowing customers a longer term to repay their obligations in full than initially contracted. Payment holidays granted in line with regulation have not been classified as forbearance.

Customers within the forbearance portfolio have received £32m of COVID-19 related support loans: £6m CLBIL, £20m CBIL and £6m BBL. There are only 9 newly forborne connections (£3.9m exposure) where the impact of COVID-19 is the primary driver of trading deterioration.

The table includes a portfolio of financial assets at fair value. The gross value of fair value loans subject to forbearance as at 31 March 2021 is £6m (30 September 2020: £7m), representing 0.07% of the total business portfolio (30 September 2020: 0.08%). The credit risk adjustment on these amounts totalled £0.3m (30 September 2020: £0.7m), a coverage of 4.85% (30 September 2020: 9.77%).

Macroeconomic assumptions, scenarios and weightings

The Group's ECL allowance as at 31 March 2021 was £721m (30 September 2020: £735m).

Macroeconomic assumptions

A range of future macroeconomic forecasts is used in the scenarios over the five-year forecast period, reflecting the best estimate of future conditions under each scenario. The Group has identified the following key macroeconomic conditions as the most significant inputs for IFRS 9 modelling purposes: UK GDP growth, inflation, house prices, base rates, and unemployment rates. These are assessed and reviewed on a quarterly basis to ensure appropriateness and relevance to the ECL calculation, with more frequent updates provided as and when the circumstances require them. Management adjustments supplement the modelled output when it is considered that not all the risks identified in a product segment have been accurately reflected within the models or for other situations where it is not possible to provide a modelled outcome.

The shock to the economy as a result of COVID-19 continues to be more severe than any in history, with unprecedented lockdowns imposed which places many restrictions on customers. The recent vaccination programme has begun to make an impact in reducing the spread of infection rates which, combined with the gradual easing of lockdown restrictions, is also encouraging and influencing the changing economic outlook. The Group has continued to assess the possible IFRS 9 economic scenarios to select appropriate forecasts and weightings. The scenario weightings are considered by an internal review panel and then recommended and approved for use in the IFRS 9 models by the Asset and Liability Committee (ALCO). The three scenarios selected, together with the weightings applied, have been updated to reflect the current economic environment:

Scenario	**31 Mar 2021 (%)**	30 Sep 2020 (%)
Upside	**20**	5
Base	**50**	50
Downside	**30**	45

The Group continued to select three scenarios and apply a 50% weighting to the base scenario. There is a 15% shift in the weightings from the Downside scenario towards the Upside scenario in the period reflecting a more optimistic view of the Upside scenario over the short term as a result of the updated assumptions which included the start of a UK wide COVID-19 vaccination programme and a gradual easing of lockdown restrictions.

Upside (20%)

- GDP declines by 7.8% in the first quarter of 2021 (Q1 2021 v Q1 2020) before rising steeply in Q2 2021 and settling to pre-crisis levels by Q3 2021, with overall year-on-year growth in 2021 forecast at 8.7%, reducing to 6.7% in 2022.
- BoE base rate rises are anticipated in the latter half of 2021 and expected to continue throughout 2022 and 2023 and reach 1.0% in Q2 2023. These rises continue gradually over the remaining forecast horizon reaching 1.4% in Q4 2025.
- HPI stagnates with little movement between Q3 2021 and Q3 2022 but then increases in each quarter until the end of the forecast period. Overall, HPI sees year-on-year growth of 4.3% in 2021 declining to 0.4% in 2022.
- Unemployment peaks in Q4 2020, at 5.5%, and is forecast to recover to 4.0% by the end of 2022. From then, there is a gradual improvement over the following years, reaching 3.6% in Q2 2024 and remaining there until the end of the forecast period.

Base (50%)

- GDP contracts by 13.8% in the first quarter of 2021 (Q1 2021 v Q1 2020) before recovering in Q2 2021 and flattening by Q3 2021, with overall year-on-year growth in 2021 forecast at 0.6%, increasing to 6.6% in 2022. GDP eventually recovers to pre COVID-19 levels by Q2 2024.
- BoE base rates remain flat at 0.1% for the entire forecast period.
- HPI sees a steady decline between Q1 2021 to Q3 2023 but then rebounds slowly in each quarter after this until the end of the forecast period to finish higher than it was in 2020. Overall, HPI sees year-on-year growth of just 0.7% in 2021 and regresses further to (3.9%) in 2022.
- Unemployment peaks at over 7.8% in Q2 2021 before beginning to fall again. However, by the end of 2025 the rate is sitting at 5.9% which is over 2% higher than the historic lows seen pre COVID-19.

Macroeconomic assumptions (continued)

Downside (30%)

- GDP contracts by 17.5% in the first quarter of 2021 (Q1 2021 v Q1 2020) before rising, but not to the same extent, in Q2 2021 (v Q2 2020) and a forecast further decline in Q3 2021 (v Q3 2020), with overall year-on-year growth in 2021 forecast at (4.3%), rising to 6.7% in 2022. Overall recovery is slow and by the end of 2025 GDP is still below pre COVID-19 levels.
- The BoE base rate is cut to -0.5% by the end of 2021 and remains there for the remainder of the forecast horizon.
- HPI falls steadily and deeply from Q1 2021 to Q4 2023 but then experiences modest increases in each quarter until the end of the forecast period but finishes below the levels experienced in 2020. Overall, HPI sees a year-on-year decline of (3.7%) in 2021 worsening to (10.3%) in 2022.
- Unemployment peaks at 9.3% in Q2 2021 and does not get below 8.0% until Q4 2022. From there unemployment steadily improves and reaches 6.5% by the end of the forecast period.

Five-year simple averages for the most sensitive inputs of unemployment, GDP and HPI are:

	Unemployment %	GDP %	HPI %
At 31 March 2021 (unaudited)			
Upside	**4.0**	**4.2**	**3.2**
Base	**6.8**	**2.7**	**0.7**
Downside	**7.6**	**1.8**	**(2.4)**
At 30 September 2020 (audited)			
Upside	4.4	1.3	1.7
Base	6.5	0.5	(1.6)
Downside	7.4	(0.4)	(6.2)

The full range of the key macroeconomic assumptions is included in the table on page 54.

The use of estimates, judgements and sensitivity analysis

The following are the main areas where estimates and judgements are applied to the ECL calculation:

The use of estimates

<u>Asset lifetimes</u>

The calculation of the ECL allowance is dependent on the expected life of the Group's portfolios. The Group assumes the remaining contract term as the maximum period to consider credit losses wherever possible. For the Group's credit card and overdraft portfolios, behavioural factors such as observed retention rates and other portfolio level assumptions are taken into consideration in determining the estimated asset life.

<u>Economic scenarios</u>

The calculation of the Group's impairment provision is sensitive to changes in the chosen weightings as highlighted above. The effect on the closing modelled provision of each portfolio as a result of applying a 100% weighting to each of the selected scenarios is shown below:

31 March 2021 (unaudited)	**Probability Weighted[(1)] £m**	**Upside £m**	**Base £m**	**Downside £m**
Mortgages	**25**	**17**	**24**	**32**
Personal of which:	**227**	**201**	**229**	**240**
Cards	*172*	*154*	*173*	*181*
Personal loans and overdrafts	*55*	*47*	*56*	*59*
Business	**210**	**93**	**195**	**310**
Total	**462**	**311**	**448**	**582**

(1) In addition to the probability weighted modelled provision shown in the table, the Group holds £222m relative to PMAs (2020: £186m) and £37m of individually assessed provision (2020: £53m).

The use of estimates (continued)

30 September 2020 (audited)	Probability Weighted £m	Upside £m	Base £m	Downside £m
Mortgages	46	7	28	76
Personal of which	190	162	183	204
Cards	*165*	*139*	*158*	*179*
Personal loans and overdrafts	*25*	*23*	*25*	*25*
Business	260	156	214	324
Total	496	325	425	604

One of the criteria for moving an exposure between stages is the PD which incorporates macroeconomic factors. As a result, the stage allocation will be different in each scenario and so the probability-weighted ECL cannot be recalculated using the scenario ECL provided and the scenario weightings.

Certain asset classes are less sensitive to specific macroeconomic factors, showing lower relative levels of sensitivity. To ensure appropriate levels of ECL, the relative lack of sensitivity is compensated for through the application of PMAs, further detail of which can be found on page 54.

The use of judgement

SICR
Considerable judgement is required in determining the point at which a SICR has occurred, as this is the point at which a 12-month ECL is replaced by a lifetime ECL. The Group has developed a series of triggers that indicate where a SICR has occurred when assessing exposures for the risk of default occurring at each reporting date compared to the risk at origination. There is no single factor that influences this decision, rather a combination of different criteria that enables the Group to make an assessment based on the quantitative and qualitative information available. This includes the impact of forward-looking macroeconomic factors but excludes the existence of any collateral implications.

Indicators of a SICR include deterioration of the residual lifetime PD by set thresholds which are unique to each product portfolio, non-default forbearance programmes, and watch list status. The Group adopts the backstop position that a SICR will have taken place when the financial asset reaches 30 DPD. Customers who requested COVID-19 related support, including payment holidays, and who were not the subject of any wider SICR triggers or who were otherwise assessed as having the ability in the medium term to be viable and meet our risk appetite criteria, were not considered to have been granted forbearance or to have a SICR.

The Group does not have a set absolute threshold by which the PD would have to increase by in establishing that a SICR has occurred, and has established an approach with the required SICR threshold trigger varying on a portfolio basis according to the origination PD.

The table below illustrates this with reference to the Group's business and credit card portfolios:

		Origination PD	SICR Trigger
Business	Low origination PD	0.04%	0.23%
	High origination PD	10.09%	13.20%
Credit cards	Low origination PD	1.00%	23.86%
	High origination PD	11.00%	28.11%

Changes to the overall SICR thresholds can also impact staging, driving accounts into higher stages with the resultant impact on the ECL allowance:

	31 Mar 2021 £m	30 Sep 2020 £m
A 10% movement in the mortgage portfolio from Stage 1 to Stage 2	**+8**	+18
A 10% movement in the credit card portfolio from Stage 1 to Stage 2	**+50**	+56
A 10% movement in the business portfolio from Stage 1 to Stage 2	**+12**	+11
A PD stress which increases PDs upwards by 20% for all portfolios	**+123**	+151

The use of judgement (continued)

Definition of default
The PD of a credit exposure is a key input to the measurement of the ECL allowance. Default under Stage 3 occurs when there is evidence that a customer is experiencing significant financial difficulty which is likely to affect the ability to repay amounts due. The Group utilises the 90 DPD backstop for default purposes. The definition of default used for Stage 3 is materially aligned to the regulatory definition with full alignment expected later this year.

PMAs
The ECL provision is further impacted by management judgements that increase the collectively assessed modelled output where not all of the known risks identified in a particular product segment have been accurately reflected within the models. These are allocated as either (i) PMAs to address other significant portfolio related future headwinds that are outside the remit of the modelled output; or (ii) PMAs to capture a wider ERU at a portfolio level. The Group has £222m of PMAs, of which £93m (30 September 2020: £Nil) relates to ERU. These are allocated by division as shown below, with further detail provided in the relevant divisional performance sections.

	As at 31 Mar 2021 £m	As at 30 Sep 2020 £m	As at 31 Mar 2020 £m
Mortgages	**97**	75	24
Personal	**67**	111	49
Business	**58**	-	110
Total	**222**	186	183

Macroeconomic assumptions
The annual macroeconomic assumptions used over the five year forecast period in the scenarios and their weighted averages are[(1)]:

Scenario	VMUK weighting	Economic measure[(2)]	2021 %	2022 %	2023 %	2024 %	2025 %
		Base rate	0.3	0.7	1.0	1.1	1.3
		Unemployment	4.7	4.1	3.8	3.6	3.6
Upside	20%	GDP	8.7	6.7	2.1	1.9	1.7
		Inflation	3.2	2.7	0.9	1.4	2.2
		HPI	4.3	0.4	3.5	4.4	3.6
		Base rate	0.1	0.1	0.1	0.1	0.1
		Unemployment	7.7	7.2	6.7	6.2	6.0
Base	50%	GDP	0.6	6.6	2.5	2.0	1.8
		Inflation	0.5	0.8	2.0	1.8	1.3
		HPI	0.7	(3.9)	(0.6)	3.1	4.1
		Base rate	(0.3)	(0.5)	(0.5)	(0.5)	(0.5)
		Unemployment	9.1	8.1	7.4	6.9	6.6
Downside	30%	GDP	(4.3)	6.7	2.7	2.2	1.9
		Inflation	(0.5)	(0.2)	2.5	1.9	0.7
		HPI	(3.7)	(10.3)	(6.0)	2.2	5.8
		Base rate	0.0	0.0	0.1	0.1	0.2
		Unemployment	7.5	6.9	6.3	5.9	5.7
Weighted average		GDP	0.7	6.7	2.5	2.0	1.8
		Inflation	0.8	0.9	1.9	1.7	1.3
		HPI	0.1	(4.9)	(1.4)	3.1	4.5

(1) Economic assumptions are on a calendar year basis unless otherwise stated.
(2) The percentages shown for base rate, unemployment and inflation are averages. Those for GDP and HPI are year-on-year.

Financial risk

Financial risk

Financial risk covers several categories of risk which impact the way in which the Group can support its customers in a safe and sound manner. They include capital risk, funding risk, liquidity risk, market risk and pension risk.

Capital risk

Capital is held by the Group to protect its depositors, to cover inherent risks in a normal and stressed operating environment and to support the Group's strategy of pioneering growth. Capital risk is the risk that the Group has insufficient quantity or quality of capital to support its operations.

Included in this section are certain Pillar 3 disclosures which the Group has assessed as requiring semi-annual disclosure.

Regulatory capital developments

COVID-19

Following the BoE's announcements in 2020 regarding supervisory and prudential policy measures to address the challenges of COVID-19, the requirements to comply with updates to definition of default, mortgage Hybrid PD and LGD will now be approved and implemented by 1 January 2022, a year later than the original timeline.

The Group continues to apply relevant relief measures introduced by regulatory and supervisory bodies to help address and alleviate various COVID-19 driven financial impacts. These include amendments to the CRR introduced by the 'Quick Fix' package in June 2020, which introduced a number of beneficial modifications, including changes to IFRS 9 transitional arrangements for capital and the accelerated implementation of revised SME supporting factors under CRR II.

IRB approach to UK Mortgage Risk Weights

In September 2020, the PRA issued a consultation setting out proposals to introduce certain floors in respect of the IRB approach to UK mortgage risk weights. The consultation closed on 30 January 2021, with any resulting final policy expected to take effect from 1 January 2022. As this could have significant implications for the UK banking industry, the Group has responded to the consultation.

UK implementation of Basel Standards

The Group is currently reviewing the PRA's 'Implementation of Basel standards' consultation paper (CP5/21), which sets out how the PRA will implement those Basel III standards in the UK that the EU is enacting via CRR II. The consultation covers a range of areas including: definition of capital; market risk; collective investment undertakings; counterparty credit risk; operational risk; large exposures; LCR; NSFR; reporting; and disclosure. These standards are expected to be implemented in the UK by 1 January 2022.

Whilst no material issues are anticipated with the consultation, the definition of capital section does include the PRA's proposal to fully deduct software assets from CET1 capital. This is a reversal of the preferential treatment permitted under the CRR Quick Fix in December 2020 whereby the CET1 deduction was replaced with a simple approach based on a prudential amortisation of software assets calibrated over a period of maximum three years. The PRA's view is that intangible assets are not sufficiently loss absorbent on a going concern basis to warrant recognition as CET1 capital.

Her Majesty's Treasury (HMT) also published a consultation in February 2021 seeking views on the proposed exercise of the delegated powers provided to it by the Financial Services Bill to ensure the effective implementation of those outstanding Basel 3 standards contained in CRR II. The Group has reviewed this and does not anticipate any material issues.

Basel 3.1

The Basel Committee published its final reforms to the Basel III framework in December 2017. The amendments include changes to the standardised approaches to credit and operational risks and the introduction of a new RWA output floor. The reforms are subject to a transition period from 2023 to 2028. The PRA and HMT have noted that they remain committed to the implementation of these 'Basel 3.1 standards' from 1 January 2023.

Solvency Stress Test (SST)

The Group will participate in the BoE UK-wide SST for the first time in 2021. A significant amount of work has been undertaken to ensure that the Group is prepared.

Financial risk

Capital

The Group's capital position as at 31 March 2021 is summarised below:

Regulatory capital (unaudited)[1]	31 Mar 2021 £m	30 Sep 2020 £m
Statutory total equity	**5,080**	4,932
CET1 capital: Regulatory adjustments[2]		
AT1 capital instruments	**(915)**	(915)
Defined benefit pension fund assets	**(471)**	(470)
Prudent valuation adjustment	**(5)**	(6)
Intangible assets	**(301)**	(477)
Goodwill	**(11)**	(11)
Deferred tax asset relying on future profitability[3]	**(173)**	(151)
Cash flow hedge reserve	**(18)**	80
AT1 coupon accrual	**(21)**	(21)
IFRS 9 transitional adjustments	**312**	310
Total regulatory adjustments to CET1	**(1,603)**	(1,661)
Total CET1 capital	**3,477**	3,271
AT1 capital		
AT1 capital instruments	**915**	915
Total AT1 capital	**915**	915
Total Tier 1 capital	**4,392**	4,186
Tier 2 capital		
Subordinated debt	**720**	749
Total Tier 2 capital	**720**	749
Total regulatory capital	**5,112**	4,935

(1) Data in the table is reported under CRD IV on a fully loaded basis with IFRS 9 transitional arrangements applied.
(2) A number of regulatory adjustments to CET1 capital are required under CRD IV regulatory capital rules.
(3) Includes deferred tax on losses in relation to UTM which is proportionately consolidated under prudential rules.

Financial risk

Capital (continued)

Regulatory capital flow of funds (unaudited)[1]	31 Mar 2021 £m	30 Sep 2020 £m
CET1 capital[2]		
CET1 capital at 1 October	**3,271**	3,204
Share capital and share premium	**2**	1
Retained earnings and other reserves (including special purpose entities)	**48**	(37)
Prudent valuation adjustment	**1**	(1)
Amendment to software asset deduction rules[3]	**132**	-
Intangible assets	**44**	24
Deferred tax asset relying on future profitability	**(22)**	(5)
Defined benefit pension fund assets	**(1)**	(213)
Excess expected losses	**-**	88
IFRS 9 transitional adjustments	**2**	210
Total CET1 capital	**3,477**	3,271
AT1 capital		
AT1 capital at 1 October	**915**	915
Total AT1 capital	**915**	915
Total Tier 1 capital	**4,392**	4,186
Tier 2 capital		
Tier 2 capital at 1 October	**749**	721
Capital instruments issued: subordinated debt	**-**	472
Reduction in capital instruments: subordinated debt	**(29)**	(444)
Total Tier 2 capital	**720**	749
Total capital	**5,112**	4,935

(1) Data in the table is reported under CRD IV on a fully loaded basis with IFRS 9 transitional arrangements applied.
(2) CET1 capital is comprised of shares issued and related share premium, retained earnings and other reserves less specified regulatory adjustments.
(3) Regulatory capital is calculated in line with current rules which incorporate the amendments introduced by the CRR Quick Fix in December 2020, which calculate the CET1 software asset deduction on a prudential amortisation basis over a period of three years.

The Group's CET1 capital increased by £206m in the first six months of the year, primarily due to statutory profit after tax of £80m and the beneficial effect of the CRR Quick Fix amendments in relation to software assets (£132m). The Group notes the PRA's current consultation regarding the potential reversal of this benefit and awaits the outcome of the consultation.

AT1 capital remained stable during the first six months of the year, whilst £29m of Tier 2 capital was redeemed.

Minimum Pillar 1 capital requirements (unaudited)	31 Mar 2021 £m	30 Sep 2020 £m
Credit risk	**1,703**	1,720
Operational risk	**205**	205
Counterparty credit risk	**13**	14
Credit valuation adjustment	**11**	14
Total Pillar 1 regulatory capital requirements	**1,932**	1,953

Capital (continued)

RWA movements (unaudited)

RWA flow statement	**6 months to 31 March 2021**					6 months to 30 September 2020				
	IRB RWA £m	**STD RWA £m**	**Other RWA £m**	**Total £m**	**Capital Required £m**	IRB RWA £m	STD RWA £m	Other RWA £m	Total £m	Capital required £m
Opening RWA	**15,846**	**5,642**	**2,911**	**24,399**	**1,953**	15,721	6,415	3,037	25,173	2,014
Asset size	**(97)**	**(134)**	**-**	**(231)**	**(19)**	(271)	(73)	-	(344)	(27)
Asset quality	**(511)**	**(17)**	**-**	**(528)**	**(42)**	334	(154)	-	180	14
Model updates[(1)]	**508**	**-**	**-**	**508**	**40**	297	-	-	297	24
Methodology and policy	**(36)**	**132**	**-**	**96**	**8**	(704)	(48)	-	(752)	(60)
IRB accreditation	**-**	**-**	**-**	**-**	**-**	457	(473)	-	(16)	(1)
Other[(2)]	**-**	**(42)**	**(50)**	**(92)**	**(8)**	12	(25)	(126)	(139)	(11)
Closing RWA	**15,710**	**5,581**	**2,861**	**24,152**	**1,932**	15,846	5,642	2,911	24,399	1,953

(1) Model updates include the mortgage quarterly PD calibrations.
(2) 'Other' includes operational risk, credit valuation adjustment (CVA) and counterparty credit risk.

RWA reduced c.£0.2bn (1%) to £24.2bn primarily due to the impact of business effective maturity methodology changes in the period and as lending volumes remained stable.

Methodology and policy movement is largely driven by the inclusion of £132m RWA in relation to the CRR Quick Fix amendments in respect of intangible assets, which became effective from December 2020 reporting.

In addition, the migration of the heritage Virgin Money House Price Index (HPI) from Markit to MIAC, which now aligns the source of the indexation across both heritages, resulted in a £161m RWA uplift in February. Offsetting this was the move to using Effective Maturity within the FIRB calculations, which resulted in a £197m reduction in RWA (previously only residual maturity had been used). This was implemented in November 2020 following PRA approval.

Model updates includes a £513m uplift in RWA specific to COVID-19 related PMAs, which is offset by a net £5m PD recalibration reduction.

There have been no further material changes in asset quality or specific credit risk adjustments in the period, meaning the Group has not experienced RWA inflation. The expected RWA and capital position for FY21 remain subject to economic developments and delivery of RWA initiatives, subject to PRA approval.

Capital (continued)

Pillar 1 RWA and capital requirements by business line (unaudited)

	At 31 March 2021			At 30 September 2020		
Capital requirements for calculating RWA	**Capital required £m**	**RWA £m**	**Exposure £m**	Capital required £m	RWA £m	Exposure £m
Corporates	**487**	**6,083**	**9,234**	509	6,362	9,468
Retail	**770**	**9,627**	**63,206**	759	9,484	62,683
Total IRB approach	**1,257**	**15,710**	**72,440**	1,268	15,846	72,151
Central governments or central banks	**-**	**-**	**13,292**	-	-	12,264
Regional governments or local authorities	**1**	**13**	**151**	1	13	219
Public sector entities	**-**	**5**	**385**	-	5	409
Multilateral development banks	**-**	**-**	**1,341**	-	-	1,268
Financial institutions	**12**	**145**	**696**	15	186	898
Corporates	**17**	**215**	**243**	17	210	233
Retail	**316**	**3,947**	**5,263**	327	4,090	5,453
Secured by mortgages on immovable property	**11**	**135**	**405**	12	144	433
Exposures in default	**6**	**73**	**67**	5	62	58
Equity exposures	**1**	**13**	**13**	1	14	13
Covered bonds	**12**	**146**	**1,460**	12	144	1,442
Other items	**70**	**889**	**789**	62	774	746
Total standardised approach	**446**	**5,581**	**24,105**	452	5,642	23,436
Total credit risk	**1,703**	**21,291**	**96,545**	1,720	21,488	95,587
Operational risk	**205**	**2,557**		205	2,557	
Counterparty credit risk	**13**	**165**		14	179	
Credit valuation adjustment	**11**	**139**		14	175	
Total Pillar 1 regulatory capital requirements	**1,932**	**24,152**		1,953	24,399	

The exposure amounts disclosed in the Pillar 1 RWA and capital requirements by business line table are post-credit conversion factors (CCF) and pre-credit mitigation.

Additional breakdown analysis of the IRB portfolios can be seen within the ‘EU CR6 – IRB Approach – Credit risk by exposure class and PD range’ and ‘EU CR10 – IRB specialised lending and equity exposures under the simple risk-weighted approach’ tables on pages 63 to 65.

Capital (continued)

RWA[(1)] (unaudited)	31 Mar 2021 £m	30 Sep 2020 £m
Retail mortgages	**9,627**	9,484
Business lending	**6,436**	6,716
Other retail lending	**4,018**	4,151
Other lending	**237**	343
Other[(2)]	**973**	794
Total credit risk RWA	**21,291**	21,488
Operational risk	**2,557**	2,557
Credit valuation adjustment	**139**	175
Counterparty credit risk	**165**	179
Total RWA	**24,152**	24,399

(1) RWA are calculated under the AIRB approach for the mortgage portfolio and the FIRB approach for the business portfolio. In March 2020, the Group received approval to move the specialised lending portfolio from a standardised approach to IRB slotting, with this change first being reported in June 2020. All other portfolios are calculated under the standardised approach, via either sequential IRB implementation or Permanent Partial Use.
(2) The items included in the Other exposure class that attract a capital charge include items in the course of collection, fixed assets, prepayments, other debtors and deferred tax assets that are not deducted.

IFRS 9 transitional arrangements (unaudited)

This table shows a comparison of capital resources, requirements and ratios with and without the application of transitional arrangements for IFRS 9:

	31 March 2021 (£m)	
Available capital (amounts)	**IFRS 9 Transitional basis**	**IFRS 9 Fully loaded basis**
CET1 capital	**3,477**	**3,165**
Tier 1 capital	**4,392**	**4,080**
Total capital	**5,112**	**4,894**
RWA (amounts)		
Total RWA	**24,152**	**24,018**
Capital ratios		
CET1 (as a percentage of risk exposure amount)	**14.4%**	**13.2%**
Tier 1 (as a percentage of risk exposure amount)	**18.2%**	**17.0%**
Total capital (as a percentage of risk exposure amount)	**21.2%**	**20.4%**
Leverage ratio		
Leverage ratio total exposure measure	**84,658**	**84,347**
CRD IV leverage ratio	**5.2%**	**4.8%**
UK leverage ratio	**5.2%**	**4.9%**

Transitional arrangements in CRR mean the regulatory capital impact of ECL is being phased in over time. Following the CRR Quick Fix amendments package, which applied from 27 June 2020, relevant provisions raised from 1 January 2020 through to 2021 have a CET1 add-back percentage of 100%, reducing to 75% in 2022, 50% in 2023 and 25% in 2024.

At 31 March 2021, £312m of IFRS 9 transitional adjustments (30 September 2020: £310m) have been applied to the Group's capital position in accordance with CRR: £10m of static and £302m of dynamic adjustments (30 September 2020: £12m static and £298m dynamic).

Capital (continued)

The Group measures the amount of capital it is required to hold by applying CRD IV as implemented in the UK by the PRA and supplemented through additional regulation under the PRA Rulebook. The table below summarises the amount of capital in relation to RWA the Group is currently required to hold, excluding any PRA Buffer.

Capital requirements

	As at 31 March 2021	
Minimum requirements (unaudited)	**CET1**	**Total capital**
Pillar 1[(1)]	4.5%	8.0%
Pillar 2A	2.2%	3.9%
Total capital requirement	**6.7%**	**11.9%**
Capital conservation buffer	2.5%	2.5%
UK countercyclical capital buffer	0.0%	0.0%
Total (excluding PRA buffer)[(2)]	**9.2%**	**14.4%**

(1) The minimum amount of total capital under Pillar 1 of the regulatory framework is determined as 8% of RWA, of which at least 4.5% of RWA is required to be covered by CET1 capital.

(2) The Group may be subject to a PRA buffer as set by the PRA but is not permitted to disclose the level of any buffer. A PRA buffer can consist of two components:
- a risk management and governance buffer that is set as a scalar of the Pillar 1 and Pillar 2A requirements; and
- a buffer relating to the results of the BoE's stress tests.

The Group continues to maintain a significant buffer of 5.2% (equivalent to c.£1.3bn) over its CRD IV minimum CET1 requirement of 9.2%.

The Group's total Pillar 2A capital requirement has reduced from 4.4% at September 2020 to 3.9% at March 2021 following an updated set of requirements received from the PRA in Q1 2021.

The UK countercyclical capital buffer (UK CCyB) may be set between 0% and 2.5%. On 11 March 2020, as part of a package of measures to support the economy from the impact of COVID-19, the Financial Policy Committee (FPC) announced a reduction in the UK CCyB to 0% with immediate effect. There have been no updates to this guidance.

Distributable reserves are determined as required by the Companies Act 2006 by reference to a company's individual financial statements. At 31 March 2021, the Company had accumulated distributable reserves of £790m (30 September 2020: £789m).

MREL

An analysis of the Group's current MREL position is provided below:

	As at	
	31 Mar 2021	30 Sep 2020
	£m	£m
Total capital resources[(1)]	**5,112**	4,935
Eligible senior unsecured securities issued by Virgin Money UK PLC[(2)]	**1,976**	2,002
Total MREL resources	**7,088**	6,937
Risk-weighted assets	**24,152**	24,399
MREL Ratio	**29.3%**	28.4%

(1) Capital is reported on a CRD IV 'fully loaded' basis with transitional IFRS 9 arrangements applied.

(2) Excludes instruments with less than one year to maturity.

In January 2021, the BoE published interim and end-state MREL for banks and building societies with a resolution entity incorporated in the UK for which an MREL has been communicated above minimum capital requirements, including the Group.

In 2021, the Group is subject to a binding interim MREL requirement of 18% of risk-weighted assets, or 20.5% of risk-weighted assets when including its combined buffer requirements. From 1 January 2022, the Group expects to have to meet an end-state MREL requirement of 23.8% of risk-weighted assets, or 26.3% of risk-weighted assets when including its combined buffer requirements.

The Group's IFRS 9 transitional MREL ratio of 29.3% as at 31 March 2021 exceeds both its interim and end-state MREL requirement, with a modest £0.5bn of MREL senior debt issuance over the remainder of 2021 anticipated, as the Group continues to build a prudent management buffer to regulatory requirements.

Capital (continued)

EU CR6 – IRB approach - Credit risk by exposure class and PD range

The Group operates with two sets of IRB models for Retail Mortgages reflecting the portfolios that have been brought together as a result of the merger of Clydesdale Bank PLC and Virgin Money PLC. The models have different modelling methodologies and risk profiles. Combining these into a single table does not provide a valid representation of risk, therefore the position of each portfolio as at 31 March 2021 (unaudited) is presented separately below. The exposure amounts shown are disclosed after, where applicable, on- or off-balance sheet netting.

Clydesdale Bank PLC Retail Mortgages[1]
(AIRB) Retail Secured by Immovable Property non-SME

PD scale	Original on-balance sheet gross exposures £m	Off-balance sheet exposures pre CCF £m	Average CCF	EAD post-CRM and post-CCF £m	Average PD	Number of obligors	Average LGD	Average maturity	RWA £m	RWA density[2]	EL £m	Value adjustments and provisions £m
At 31 Mar 2021												
0.00 to <0.15	1,585	629	102.2%	2,263	0.14%	11,069	13.92%	-	106	4.7%	1	
0.15 to <0.25	2,953	290	102.1%	3,320	0.19%	30,655	11.55%	-	198	6.0%	1	
0.25 to <0.50	9,991	532	102.1%	10,774	0.38%	57,471	14.04%	-	1,236	11.5%	8	
0.50 to <0.75	2,683	90	102.0%	2,838	0.62%	12,041	17.16%	-	537	18.9%	4	
0.75 to <2.50	4,463	114	102.3%	4,678	1.28%	21,952	15.96%	-	1,237	26.4%	11	
2.50 to <10.00	617	13	102.1%	645	4.71%	4,526	15.46%	-	330	51.2%	6	
10.00 to <100.00	156	3	100.0%	163	34.93%	1,108	15.81%	-	133	81.9%	11	
100.00 (Default)	471	8	-%	479	100.00%	3,183	17.49%	-	978	204.3%	8	
Subtotal	22,919	1,679	102.0%	25,160	2.76%	142,005	14.52%	-	4,755	18.9%	50	81
At 30 Sep 2020												
0.00 to <0.15	1,054	481	102.2%	1,570	0.12%	13,927	13.74%	-	57	3.6%	-	
0.15 to <0.25	3,677	293	102.1%	4,065	0.19%	34,564	12.48%	-	210	5.2%	1	
0.25 to <0.50	10,639	441	102.1%	11,342	0.36%	55,851	15.72%	-	1,188	10.5%	6	
0.50 to <0.75	2,130	56	102.1%	2,238	0.62%	9,936	18.48%	-	397	17.7%	2	
0.75 to <2.50	4,596	106	102.3%	4,805	1.32%	23,159	17.60%	-	1,294	26.9%	11	
2.50 to <10.00	841	14	102.2%	875	4.67%	5,755	17.24%	-	501	57.3%	7	
10.00 to <100.00	159	4	100.0%	166	34.99%	1,175	16.56%	-	145	87.2%	10	
100.00 (Default)	319	7	-%	326	100.00%	2,528	19.40%	-	728	223.6%	8	
Subtotal	23,415	1,402	102.1%	25,387	2.18%	146,895	15.78%	-	4,520	17.8%	45	74

(1) Clydesdale Bank PLC retail mortgages excluding the portfolio of heritage Virgin Money mortgages transferred on completion of the Financial Services and Markets Act 2000 (FSMA) Part VII transfer in October 2019.
(2) RWA density calculation has been performed on unrounded figures.

Virgin Money Retail Mortgages[1]
(AIRB) Retail Secured by Immovable Property non-SME

PD scale	Original on-balance sheet gross exposures £m	Off-balance sheet exposures pre CCF £m	Average CCF	EAD post-CRM and post-CCF £m	Average PD	Number of obligors	Average LGD	Average maturity	RWA £m	RWA density[2]	EL £m	Value adjustments and provisions £m
At 31 Mar 2021												
0.00 to <0.15	3,269	760	100.0%	4,083	0.12%	24,279	10.82%	-	133	3.3%	1	
0.15 to <0.25	4,975	252	100.0%	5,287	0.18%	32,969	10.75%	-	233	4.4%	1	
0.25 to <0.50	15,039	626	100.0%	15,838	0.37%	100,406	11.72%	-	1,283	8.1%	7	
0.50 to <0.75	1,859	181	100.0%	2,065	0.60%	14,334	11.95%	-	230	11.1%	1	
0.75 to <2.50	8,636	136	100.0%	8,874	1.03%	56,356	16.64%	-	1,953	22.0%	15	
2.50 to <10.00	1,149	23	100.0%	1,186	4.45%	9,184	14.84%	-	547	46.2%	8	
10.00 to <100.00	613	13	100.0%	634	32.89%	5,094	12.59%	-	416	65.6%	23	
100.00 (Default)	78	1	100.0%	79	100.00%	640	9.62%	-	77	97.0%	5	
Subtotal	35,618	1,992	100.0%	38,046	1.58%	243,262	12.76%	-	4,872	12.8%	61	48
At 30 Sep 2020												
0.00 to <0.15	2,800	571	100.0%	3,419	0.11%	22,324	10.25%	-	96	2.8%	-	
0.15 to <0.25	5,650	329	100.0%	6,051	0.19%	40,279	13.55%	-	341	5.6%	1	
0.25 to <0.50	14,332	366	100.0%	14,859	0.36%	92,867	10.69%	-	1,052	7.1%	6	
0.50 to <0.75	3,531	90	100.0%	3,662	0.66%	22,637	12.72%	-	471	12.9%	3	
0.75 to <2.50	7,061	314	100.0%	7,467	1.11%	49,107	18.52%	-	1,891	25.3%	15	
2.50 to <10.00	1,078	22	100.0%	1,114	4.48%	8,609	16.73%	-	571	51.3%	8	
10.00 to <100.00	638	13	100.0%	659	31.14%	5,283	13.73%	-	474	72.0%	25	
100.00 (Default)	65	1	100.0%	66	100.00%	550	10.04%	-	68	102.5%	4	
Subtotal	35,155	1,706	100.0%	37,297	1.53%	241,656	13.12%	-	4,964	13.3%	62	55

(1) Retail mortgages written under the Virgin Money brand which were previously held in Virgin Money PLC prior to completion of the FSMA Part VII transfer in October 2019.
(2) RWA density calculation has been performed on unrounded figures.

Capital (continued)

Clydesdale Bank PLC Corporates - Other
(FIRB) Corporates – Other

PD scale	Original on-balance sheet gross exposures £m	Off-balance sheet exposures pre CCF £m	Average CCF	EAD post-CRM and post-CCF £m	Average PD	Number of obligors	Average LGD	Average maturity	RWA £m	RWA density[(1)]	EL £m	Value adjustments and provisions £m
At 31 Mar 2021												
0.00 to <0.15	**3**	**57**	**72.4%**	**55**	**0.09%**	**20**	**35.57%**	**727**	**12**	**22.2%**	**-**	
0.15 to <0.25	**21**	**114**	**74.0%**	**108**	**0.18%**	**30**	**43.90%**	**640**	**39**	**35.7%**	**-**	
0.25 to <0.50	**132**	**204**	**56.9%**	**249**	**0.38%**	**44**	**43.68%**	**814**	**147**	**59.2%**	**-**	
0.50 to <0.75	**112**	**61**	**73.2%**	**157**	**0.62%**	**24**	**44.80%**	**802**	**120**	**76.7%**	**-**	
0.75 to <2.50	**1,063**	**340**	**54.2%**	**814**	**1.88%**	**9,998**	**43.90%**	**981**	**903**	**111.0%**	**6**	
2.50 to <10.00	**242**	**132**	**72.3%**	**309**	**4.14%**	**279**	**43.43%**	**787**	**429**	**138.7%**	**5**	
10.00 to <100.00	**97**	**29**	**69.1%**	**51**	**23.29%**	**1,568**	**44.52%**	**907**	**127**	**248.0%**	**5**	
100.00 (Default)	**73**	**31**	**28.4%**	**76**	**100.00%**	**176**	**44.33%**	**735**	**-**	**-%**	**34**	
Subtotal	**1,743**	**968**	**61.1%**	**1,819**	**6.18%**	**12,139**	**43.34%**	**851**	**1,777**	**97.7%**	**50**	**76**
At 30 Sep 2020												
0.00 to <0.15	3	76	70.0%	69	0.10%	30	36.20%	799	17	24.3%	-	
0.15 to <0.25	60	66	73.0%	115	0.20%	18	41.94%	871	49	42.7%	-	
0.25 to <0.50	224	174	56.2%	321	0.42%	47	43.80%	976	217	67.6%	1	
0.50 to <0.75	96	64	56.5%	132	0.62%	26	44.18%	994	108	82.0%	-	
0.75 to <2.50	976	426	58.9%	847	1.82%	8,775	43.54%	1,311	964	113.9%	6	
2.50 to <10.00	164	101	69.8%	236	4.19%	147	43.13%	889	337	142.6%	4	
10.00 to <100.00	102	30	69.4%	63	23.33%	1,492	44.24%	1,350	158	249.8%	6	
100.00 (Default)	122	23	37.6%	130	100.00%	123	42.66%	839	-	-%	55	
Subtotal	1,747	960	61.1%	1,913	7.86%	10,658	42.85%	992	1,850	96.7%	72	69

(1) RWA density calculation has been performed on unrounded figures.

Clydesdale Bank PLC Business Lending
(FIRB) Corporates – Business

PD scale	Original on-balance sheet gross exposures £m	Off-balance sheet exposures pre CCF £m	Average CCF	EAD post-CRM and post-CCF £m	Average PD	Number of obligors	Average LGD	Average maturity	RWA £m	RWA density[(1)]	EL £m	Value adjustments and provisions £m
At 31 Mar 2021												
0.00 to <0.15	**67**	**50**	**68.9%**	**96**	**0.11%**	**124**	**41.35%**	**679**	**16**	**16.2%**	**-**	
0.15 to <0.25	**218**	**168**	**66.7%**	**309**	**0.20%**	**612**	**40.14%**	**780**	**72**	**23.5%**	**-**	
0.25 to <0.50	**903**	**442**	**68.6%**	**1,167**	**0.40%**	**1,694**	**39.19%**	**791**	**400**	**34.3%**	**2**	
0.50 to <0.75	**340**	**128**	**69.2%**	**401**	**0.62%**	**578**	**39.27%**	**975**	**179**	**44.6%**	**1**	
0.75 to <2.50	**3,029**	**1,021**	**68.2%**	**3,441**	**1.47%**	**6,072**	**39.85%**	**848**	**2,091**	**60.7%**	**20**	
2.50 to <10.00	**1,138**	**307**	**67.1%**	**1,191**	**4.48%**	**2,977**	**41.02%**	**722**	**967**	**81.2%**	**21**	
10.00 to <100.00	**116**	**25**	**68.7%**	**112**	**18.14%**	**487**	**40.24%**	**618**	**141**	**126.0%**	**8**	
100.00 (Default)	**88**	**8**	**70.5%**	**91**	**100.00%**	**172**	**40.24%**	**739**	**-**	**-%**	**36**	
Subtotal	**5,899**	**2,149**	**68.1%**	**6,808**	**3.23%**	**12,716**	**39.53%**	**810**	**3,866**	**56.8%**	**88**	**199**
At 30 Sep 2020												
0.00 to <0.15	79	64	69.6%	114	0.11%	170	40.80%	850	20	17.7%	-	
0.15 to <0.25	195	174	67.0%	297	0.20%	671	39.56%	868	70	23.5%	-	
0.25 to <0.50	798	433	68.0%	1,055	0.38%	1,707	39.32%	923	369	35.0%	1	
0.50 to <0.75	386	142	64.2%	465	0.62%	655	38.26%	875	197	42.4%	1	
0.75 to <2.50	3,333	1,023	67.9%	3,771	1.50%	6,414	40.01%	1,016	2,426	64.4%	23	
2.50 to <10.00	902	297	65.3%	1,009	4.62%	2,069	40.37%	878	839	83.1%	19	
10.00 to <100.00	107	23	72.8%	115	18.76%	203	40.49%	715	151	131.3%	9	
100.00 (Default)	105	9	62.7%	108	100.00%	168	41.04%	895	-	-%	44	
Subtotal	5,905	2,165	67.3%	6,934	3.40%	12,057	39.52%	916	4,072	58.7%	97	185

(1) RWA density calculation has been performed on unrounded figures.

Capital (continued)

EU CR10 – IRB specialised lending and equity exposures under the simple risk-weighted approach

IRB accreditation for specialised lending exposures was received in March 2020, with the first formal submission in June 2020. EU CR10 is therefore reported for the first time in this interim report.

Specialised lending: Project finance (Slotting approach)

		31 March 2021					
		On-balance sheet exposure £m	Off-balance sheet exposure £m	Risk weight	Exposure value £m	Risk-weighted exposure amount £m	Expected loss amount £m
Regulatory categories	Remaining maturity	A	B	C	D	E	F
Strong	< 2.5 years	-	-	50%	-	-	-
	≥ 2.5 years	4	-	70%	4	2	-
Good	< 2.5 years	221	11	70%	228	134	1
	≥ 2.5 years	211	11	90%	219	165	2
Satisfactory	< 2.5 years	49	2	115%	50	46	1
	≥ 2.5 years	54	-	115%	54	49	1
Weak	< 2.5 years	12	-	250%	13	25	1
	≥ 2.5 years	10	-	250%	10	19	1
Default	< 2.5 years	18	-	-%	26	-	13
	≥ 2.5 years	2	-	-%	3	-	2
Total	< 2.5 years	300	13		317	205	16
	≥ 2.5 years	281	11		290	235	6

		30 September 2020					
		On-balance sheet exposure £m	Off-balance sheet exposure £m	Risk weight	Exposure value £m	Risk-weighted exposure amount £m	Expected loss amount £m
Regulatory categories	Remaining maturity	A	B	C	D	E	F
Strong	< 2.5 years	-	-	50%	-	-	-
	≥ 2.5 years	1	-	70%	1	-	-
Good	< 2.5 years	220	15	70%	243	142	1
	≥ 2.5 years	217	18	90%	239	183	2
Satisfactory	< 2.5 years	42	2	115%	47	43	1
	≥ 2.5 years	46	-	115%	46	41	1
Weak	< 2.5 years	7	-	250%	9	18	1
	≥ 2.5 years	6	-	250%	6	12	1
Default	< 2.5 years	11	-	-%	21	-	11
	≥ 2.5 years	6	-	-%	8	-	4
Total	< 2.5 years	280	17		320	203	14
	≥ 2.5 years	276	18		300	236	8

Leverage

Leverage ratio (unaudited)	31 Mar 2021 £m	30 Sep 2020 £m
Total Tier 1 capital for the leverage ratio		
Total CET1 capital	**3,477**	3,271
AT1 capital	**915**	915
Total Tier 1	**4,392**	4,186
Exposures for the leverage ratio		
Total assets as per published financial statements	**90,139**	90,259
Adjustment for off-balance sheet items	**3,049**	2,892
Adjustment for derivative financial instruments	**121**	81
Adjustment for securities financing transactions	**2,166**	2,072
Adjustment for qualifying central bank claims	**(10,150)**	(8,088)
Other adjustments	**(667)**	(726)
Leverage ratio exposure	**84,658**	86,490
CRD IV leverage ratio(1)	**5.2%**	4.8%
UK leverage ratio(2)	**5.2%**	4.9%
Average UK leverage ratio exposure(3)	**83,493**	85,713
Average UK leverage ratio(3)	**4.9%**	4.6%

(1) IFRS 9 transitional capital arrangements have been applied to the CRD IV leverage ratio calculation.
(2) The Group's leverage ratio on a modified basis, excluding qualifying central bank claims and loans under the UK BBLS from the exposure measure.
(3) The fully loaded average leverage exposure measure is based on the daily average of on-balance sheet items and three month-end average of off-balance sheet items. The average leverage ratio is based on the average of the month end tier 1 capital position.

The UK leverage ratio framework, which came into force on 1 January 2016, is relevant to PRA regulated banks and building societies with consolidated retail deposits equal to or greater than £50bn. The Group exceeds this threshold and accordingly the average UK leverage ratio exposure and average UK leverage ratio are disclosed.

The leverage ratio is monitored against a Board-approved RAS, with the responsibility for managing the ratio delegated to the Group's ALCO, which monitors it on a monthly basis.

The leverage ratio is the ratio of Tier 1 capital to total exposures, defined as:

- capital: Tier 1 capital defined on a CRD IV fully loaded and IFRS 9 transitional basis; and
- exposures: total on- and off-balance sheet exposures (subject to credit conversion factors) as defined in the delegated act amending CRR article 429 (Calculation of the Leverage Ratio), which includes deductions applied to Tier 1 capital.

Other regulatory adjustments consist of adjustments that are required under CRD IV to be deducted from Tier 1 capital. The removal of these from the exposure measure ensures consistency is maintained between the capital and exposure components of the ratio.

The Group's CRD IV leverage ratio of 5.2% (30 September 2020: 4.8%) exceeds the Basel Committee's proposed minimum of 3% and the Group's UK leverage ratio of 5.2% (30 September 2020: 4.9%) exceeds the UK minimum ratio of 3.25%.

Following the FPC announcement on 11 March 2020, the Group's CCyB rate reduced to 0% which also moved the leverage ratio buffer to 0%.

Financial risk

Funding and liquidity risk

Funding risk occurs where the Group is unable to raise or maintain funds of sufficient quantity and quality to support the delivery of the business plan or sustain lending commitments. Prudent funding risk management reduces the likelihood of liquidity risks occurring, increases the stability of funding sources, minimises concentration risks and controls future balance sheet growth.

Liquidity risk occurs when the Group is unable to meet its current and future financial obligations as they fall due or at acceptable cost, or when the Group reduces liquidity resource below internal or regulatory stress requirements.

The Group is predominantly funded by personal and business customers. Customer funding is supported by the Group's ongoing wholesale funding programmes, medium-term secured funding issuance (e.g. the Group's securitisation programmes), Regulated Covered Bonds and unsecured medium-term notes. The Group also has access to and has drawn against the BoE TFS and TFSME, both schemes having been introduced to support the UK through periods of instability.

Funding risk exposures arise from an unsustainable or undiversified funding base, for example, a reliance on short-term wholesale deposits. The risk may result in deviation from funding strategy, requiring funding to be originated rapidly and at excessive cost, or require a reduction in lending growth, which are outcomes that may adversely affect customers or shareholders.

The Group's primary liquidity risk exposure arises through the redemption of retail deposits where customers have the ability to withdraw funds with limited or no notice. Exposure also arises from the refinancing of customer and wholesale funding at maturity and the requirement to fund new and existing committed lending obligations including mortgage pipeline and credit card facilities.

Sources of funding

The table below provides an overview of the Group's sources of funding as at 31 March 2021:

	31 Mar 2021 (unaudited)	30 Sep 2020 (audited)
	£m	£m
Total assets	**90,139**	90,259
Less: Other liabilities(1)	**(3,096)**	(3,390)
Funding requirement	**87,043**	86,869
Funded by:		
Customer deposits	**68,674**	67,710
Debt securities in issue	**7,597**	8,758
Due to other banks	**5,692**	5,469
of which:		
Secured loans	*5,659*	*5,397*
Transaction balances with other banks	*10*	*15*
Deposits with other banks	*23*	*57*
Equity	**5,080**	4,932
Total funding	**87,043**	86,869

(1) Other liabilities include derivative financial instruments, deferred tax liabilities, provisions for liabilities and charges, and other liabilities as per the balance sheet line item.

The Group's funding objective is to prudently manage the sources and tenor of funds in order to provide a sound base from which to support sustainable lending growth. At 31 March 2021, the Group had a funding requirement of £87,043m (30 September 2020: £86,869m) with the majority being used to support loans and advances to customers.

Customer deposits

The majority of the Group's funding requirement was met by customer deposits of £68,674m (30 September 2020: £67,710m). Customer deposits are comprised of interest bearing deposits, term deposits and non-interest bearing demand deposits from a range of sources including personal and business customers. The increase of £964m in the six month period ended 31 March 2021 is primarily due to elevated deposit balances from consumers and businesses, which have been driven by lower levels of spending as a result of COVID-19 related societal restrictions.

Sources of funding (continued)

Equity
Equity of £5,080m (30 September 2020: £4,932m) was also used to meet the Group's funding requirement. Equity is comprised of ordinary share capital, retained earnings, other equity investments and a number of other reserves. For full details on equity refer to note 4.1.

Liquid assets

The quantity and quality of the Group's liquid assets are calibrated to the Board's view of liquidity risk appetite and remain at a prudent level above regulatory requirements.

Liquidity coverage ratio	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m
Eligible liquidity buffer	**11,687**	10,675
Net stress outflows	**7,755**	7,609
Surplus	**3,932**	3,066
Liquidity coverage ratio	**151%**	140%

The liquid asset portfolio provides a buffer against sudden and potentially sharp outflows of funds. Liquid assets must therefore be of a high quality, so they can be realised for cash and cannot be encumbered for any other purpose (e.g. to provide collateral for payments systems).

The volume and quality of the Group's liquid asset portfolio is defined through a series of internal stress tests across a range of time horizons and stress conditions, including most recently the Group's view of liquidity risk due to impacts of COVID-19 and the UK's withdrawal from the EU. The liquid asset portfolio is primarily comprised of cash at the BoE, UK Government securities (Gilts) and listed securities (e.g. bonds issued by supra-nationals and AAA-rated covered bonds).

Liquid asset portfolio[1]	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m	Change %	Average 2021 £m	Average 2020 £m
Level 1					
Cash and balances with central banks	**7,809**	6,255	25	**7,202**	6,430
UK Government treasury bills and gilts	**626**	1,232	(49)	**727**	1,301
Other debt securities	**3,333**	3,262	2	**3,327**	3,186
Total level 1	**11,768**	10,749	9	**11,256**	10,917
Level 2[2]	**23**	29	(21)	**24**	33
Total LCR eligible assets	**11,791**	10,778	9	**11,280**	10,950

(1) Excludes encumbered assets.
(2) Includes Level 2A and Level 2B.

Encumbered assets by asset category

The Group manages the level of asset encumbrance to ensure appropriate volumes of assets are maintained to support future planned and potential stressed funding requirements. Encumbrance limits are set in the Group RAS and calibrated to ensure that after a stress scenario is applied, the balance sheet can recover over an acceptable period of time. Examples of reasons for asset encumbrance include, among others, supporting the Group's secured funding programmes to provide stable term funding to the Group, the posting of assets in respect of drawings under the TFS and TFSME schemes, use of assets as collateral for payments systems in order to support customer transactional activity, and providing security for the Group's issuance of Scottish bank notes.

31 March 2021 (unaudited)	**Assets encumbered with non-central bank counterparties**				**Positioned at the central bank (including encumbered)**	**Assets not positioned at the central bank**				
	Covered bonds £m	**Securiti-sations £m**	**Other £m**	**Total £m**	**£m**	**Readily available for encumbrance £m**	**Other assets capable of being encumbered £m**	**Cannot be encumbered £m**	**Total £m**	**Total £m**
Loans and advances to customers	**2,625**	**5,844**	**-**	**8,469**	**14,119**	**28,990**	**17,688**	**2,899**	**63,696**	**72,165**
Cash and balances with central banks	**-**	**-**	**-**	**-**	**2,796**	**7,645**	**-**	**-**	**10,441**	**10,441**
Due from other banks	**271**	**309**	**78**	**658**	**-**	**-**	**64**	**-**	**64**	**722**
Derivative financial instruments	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**222**	**222**	**222**
Financial instruments at FVOCI	**-**	**-**	**831**	**831**	**-**	**3,701**	**-**	**-**	**3,701**	**4,532**
Other assets	**-**	**-**	**417**	**417**	**-**	**-**	**285**	**1,355**	**1,640**	**2,057**
Total assets	**2,896**	**6,153**	**1,326**	**10,375**	**16,915**	**40,336**	**18,037**	**4,476**	**79,764**	**90,139**

30 September 2020 (unaudited)	Assets encumbered with non-central bank counterparties				Positioned at the central bank (including encumbered)	Assets not positioned at the central bank				
	Covered bonds £m	Securiti-sations £m	Other £m	Total £m	£m	Readily available for encumbrance £m	Other assets capable of being encumbered £m	Cannot be encumbered £m	Total £m	Total £m
Loans and advances to customers	2,551	7,253	-	9,804	15,604	26,736	17,406	3,070	62,816	72,620
Cash and balances with central banks	-	-	-	-	2,994	6,113	-	-	9,107	9,107
Due from other banks	337	424	93	854	-	-	73	-	73	927
Derivative financial instruments	-	-	-	-	-	-	-	318	318	318
Financial instruments at FVOCI	-	-	826	826	-	4,254	-	-	4,254	5,080
Other assets	-	-	910	910	-	-	301	996	1,297	2,207
Total assets	2,888	7,677	1,829	12,394	18,598	37,103	17,780	4,384	77,865	90,259

Financial risk

The table below shows the residual maturity of the Group's debt securities in issue:

Analysis of debt securities in issue by residual maturity (unaudited)

	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Total at 31 Mar 2021 £m	Total at 30 Sep 2020 £m
Covered bonds	**27**	**-**	**614**	**1,240**	**1,881**	1,928
Securitisation	**214**	**604**	**2,165**	**-**	**2,983**	4,005
Medium-term notes	**18**	**-**	**1,589**	**403**	**2,010**	2,068
Subordinated debt	**13**	**-**	**710**	**-**	**723**	757
Total debt securities in issue	**272**	**604**	**5,078**	**1,643**	**7,597**	8,758
Of which issued by Virgin Money UK PLC	**31**	**-**	**2,299**	**403**	**2,733**	2,825

External credit ratings

The Group's long-term credit ratings are summarised below:

	Outlook as at 31 Mar 2021[1]	As at 31 Mar 2021	As at 30 Sep 2020
Virgin Money UK PLC			
Moody's	**Stable**	**Baa3**	Baa3
Fitch	**Negative**	**BBB+**	BBB+
Standard & Poor's	**Negative**	**BBB-**	BBB-
Clydesdale Bank PLC			
Moody's[2]	**Stable**	**Baa1**	Baa1
Fitch	**Negative**	**A-**	A-
Standard & Poor's	**Negative**	**A-**	BBB+

(1) For detailed background on the latest credit opinions please refer to the respective rating agency websites.
(2) Long-term deposit rating.

On 22 January 2021, Standard & Poor's affirmed Virgin Money UK PLC's ratings and upgraded the long-term rating of Clydesdale Bank PLC by one notch to A-. The upgrade reflects the Group's improved additional loss-absorbing capacity following Virgin Money UK PLC's MREL issuance, which provides additional protection for Clydesdale Bank's senior creditors in resolution and now exceeds S&P's threshold for an additional notch of benefit. All ratings remain on negative outlook.

As at 4 May 2021, there have been no other changes to the Group's long-term credit ratings or outlooks since the report date.

Financial risk

LIBOR replacement

The Group has a LIBOR transition programme to manage the impact of the BoE's plan to discontinue the use of LIBOR as a reference rate after 2021. Work to decommission LIBOR has involved ceasing the issuance of new LIBOR lending, developing and delivering alternative reference rate products, and implementing a back-book migration strategy based on consensual customer agreement and transition before the end of 2021. A similar approach is being taken with new and existing derivatives. As at 31 March 2021, all market-facing derivative flows are executed against the Sterling Overnight Index Average and the strategy to proactively manage the back-book of LIBOR derivatives is underway.

The Group has early adopted the Interest Rate Benchmark Reform - Phase 2 (Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16) issued in August 2020. This introduced amendments to IFRS, addressing some of the financial reporting issues arising from changes to contractual cash flows or hedging relationships which result from interest rate benchmark reform. The Group has adopted the Phase 2 amendments from 1 October 2020. See note 1.4 for further details.

Financial instruments that have yet to transition to alternative benchmark rates are summarised below:

31 March 2021 (unaudited)	Non derivative financial assets - carrying value(1)(2) £m	Non derivative financial liabilities - carrying value(1)(5) £m	Derivatives - nominal amount(1)(3) £m
GBP LIBOR	**2,917**	**207**	**5,550**
Other(4)	**184**	**127**	**-**
Cross currency swaps			
GBP LIBOR to USD LIBOR			**147**
Total	**3,101**	**334**	**5,697**

(1) Excludes exposures that are expected to expire or mature before the IBOR ceases.
(2) Gross carrying amount excluding allowances for ECLs.
(3) The IBOR exposures for derivative nominal amounts include loan commitments.
(4) Comprises financial instruments referencing other IBOR rates yet to transition to alternative benchmark rates (Euro, USD, AUD, CHF).
(5) In addition to financial liabilities included in the table, £784m issued Covered Bonds are currently fixed rate but have an option to convert to GBP LIBOR if not redeemed on the scheduled maturity date.

The Group maintains engagement with the BoE's Working Group on Sterling Risk Free Reference Rates and other industry forums. The programme ensures that the risks of being unable to offer products with suitable reference rates will be mitigated and that full consideration is given to the other risks, including legal, conduct, financial and operational risks, that may arise. Whilst no material changes to the Group's risk management strategy are expected, the programme will continuously monitor progress and amend the approach accordingly.

Statement of Directors' responsibilities

The Directors confirm that to the best of their knowledge these interim condensed consolidated financial statements have been prepared in accordance with International Accounting Standard 34 'Interim Financial Reporting' (IAS 34) as adopted by the EU and that the interim management report includes a fair review of the information required by DTR 4.2.7R and DTR 4.2.8R, namely:

a) an indication of important events that have occurred during the six months ended 31 March 2021 and their impact on the condensed consolidated interim financial statements and a description of the principal risks and uncertainties for the remaining six months of the financial year; and

b) material related party transactions in the six months ended 31 March 2021 and any material changes in the related party transactions described in the last Annual Report of Virgin Money UK PLC.

Signed by order of the Board

David Duffy
Chief Executive Officer
4 May 2021

Independent review report to Virgin Money UK PLC

Introduction

We have been engaged by Virgin Money UK PLC to review the condensed set of financial statements in the interim financial report for the six months ended 31 March 2021 which comprises the interim condensed consolidated income statement, interim condensed consolidated statement of comprehensive income, interim condensed consolidated balance sheet, interim condensed consolidated statement of changes in equity, interim condensed consolidated statement of cash flows and the related explanatory notes 1.1 to 5.3. We have read the other information contained in the interim financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Company in accordance with guidance contained in International Standard on Review Engagements 2410 (UK and Ireland) "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Auditing Practices Board. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company, for our work, for this report, or for the conclusions we have formed.

Directors' Responsibilities

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

As disclosed in note 1, the annual financial statements of the Group are prepared in accordance with International Financial Reporting Standards as adopted by the European Union. The condensed set of financial statements included in this interim financial report has been prepared in accordance with International Accounting Standard 34 "Interim Financial Reporting", as adopted by the European Union.

Our Responsibility

Our responsibility is to express to Virgin Money UK PLC a conclusion on the condensed set of financial statements in the interim financial report based on our review.

Scope of Review

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

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the interim financial report for the six months ended 31 March 2021 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure Guidance and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Ernst & Young LLP
London
4 May 2021

Interim condensed consolidated income statement

	Note	**6 months to 31 Mar 2021 (unaudited) £m**	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Interest income		**953**	1,135	2,129
Other similar interest		**2**	5	8
Interest expense and similar charges		**(309)**	(469)	(854)
Net interest income	2.2	**646**	671	1,283
Gains less losses on financial instruments at fair value		**(15)**	(9)	(11)
Other operating income		**64**	105	171
Non-interest income	2.3	**49**	96	160
Total operating income		**695**	767	1,443
Operating and administrative expenses before impairment losses	2.4	**(585)**	(537)	(1,104)
Operating profit before impairment losses		**110**	230	339
Impairment losses on credit exposures		**(38)**	(237)	(507)
Profit/(loss) on ordinary activities before tax		**72**	(7)	(168)
Tax credit	2.5	**8**	29	27
Profit/(loss) for the period		**80**	22	(141)
Attributable to:				
Ordinary shareholders		**40**	(18)	(220)
Other equity holders		**40**	40	79
Profit/(loss) for the period		**80**	22	(141)
Basic earnings/(loss) per share (pence)	2.6	**2.8**	(1.2)	(15.3)
Diluted earnings/(loss) per share (pence)	2.6	**2.8**	(1.2)	(15.3)

All material items dealt with in arriving at the profit/(loss) before tax for the periods relate to continuing activities.

The notes on pages 79 to 99 form an integral part of these interim condensed consolidated financial statements.

Interim condensed consolidated statement of comprehensive income

	6 months to 31 Mar 2021 (unaudited) £m	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Profit/(loss) for the period	**80**	22	(141)
Items that may be reclassified to the income statement			
Change in cash flow hedge reserve			
Gains/(losses) during the period	**111**	(52)	(133)
Transfers to the income statement	**22**	18	60
Taxation thereon - deferred tax (charge)/credit	**(34)**	8	20
Taxation thereon - current tax (charge)/credit	**(1)**	1	(1)
	98	(25)	(54)
Change in FVOCI reserve			
Gains/(losses) during the period	**27**	(13)	15
Transfers to the income statement	**-**	(16)	(16)
Taxation thereon - deferred tax (charge)/credit	**(7)**	9	1
	20	(20)	-
Total items that may be reclassified to the income statement	**118**	(45)	(54)
Items that will not be reclassified to the income statement			
Change in defined benefit pension plan	**(16)**	197	292
Taxation thereon - deferred tax charge	**(1)**	(77)	(117)
Taxation thereon - current tax credit	**5**	4	9
Total items that will not be reclassified to the income statement	**(12)**	124	184
Other comprehensive income, net of tax	**106**	79	130
Total comprehensive income/(losses) for the period, net of tax	**186**	101	(11)
Attributable to:			
Ordinary shareholders	**146**	61	(90)
Other equity holders	**40**	40	79
Total comprehensive income/(losses) attributable to equity holders	**186**	101	(11)

The notes on pages 79 to 99 form an integral part of these interim condensed consolidated financial statements.

Interim condensed consolidated balance sheet

	Note	**31 Mar 2021 (unaudited) £m**	30 Sep 2020 (audited) £m
Assets			
Financial assets at amortised cost			
Loans and advances to customers	3.1	**72,007**	72,430
Cash and balances with central banks		**10,441**	9,107
Due from other banks		**722**	927
Financial assets at FVTPL			
Loans and advances to customers	3.2	**158**	190
Derivative financial instruments	3.3	**222**	318
Other financial assets	3.2	**13**	13
Financial assets at FVOCI		**4,532**	5,080
Property, plant and equipment		**272**	288
Intangible assets and goodwill		**446**	491
Current tax assets		**7**	27
Deferred tax assets	3.4	**324**	326
Defined benefit pension assets	3.8	**724**	723
Other assets		**271**	339
Total assets		**90,139**	90,259
Liabilities			
Financial liabilities at amortised cost			
Customer deposits		**68,674**	67,710
Debt securities in issue	3.5	**7,597**	8,758
Due to other banks	3.6	**5,692**	5,469
Financial liabilities at FVTPL			
Derivative financial instruments	3.3	**266**	250
Deferred tax liabilities	3.4	**292**	274
Provisions for liabilities and charges	3.7	**101**	172
Other liabilities		**2,437**	2,694
Total liabilities		**85,059**	85,327
Equity			
Share capital and share premium	4.1	**149**	147
Other equity instruments	4.1	**915**	915
Capital reorganisation reserve	4.1	**(839)**	(839)
Merger reserve	4.1	**2,128**	2,128
Other reserves		**74**	(43)
Retained earnings		**2,653**	2,624
Total equity		**5,080**	4,932
Total liabilities and equity		**90,139**	90,259

The notes on pages 79 to 99 form an integral part of these interim condensed consolidated financial statements.

These interim condensed consolidated financial statements were approved by the Board of Directors on 4 May 2021 and were signed on its behalf by:

David Duffy
Chief Executive Officer

Clifford Abrahams
Chief Financial Officer

Company name: Virgin Money UK PLC, Company number: 09595911

Interim condensed consolidated statement of changes in equity

					Other reserves							
	Share capital and share premium	Capital reorg' reserve	Merger reserve	Other equity instruments	Own shares held	Deferred shares reserve	Equity based comp' reserve	Asset reval' reserve	FVOCI reserve	Cash flow hedge reserve	Retained earnings	Total equity
Note	4.1.1	4.1.3	4.1.4	4.1.2						4.1.5		
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
As at 1 October 2019[(1)]	146	(839)	2,128	915	(1)	19	6	1	11	(26)	2,662	5,022
Profit for the period	-	-	-	-	-	-	-	-	-	-	22	22
Other comprehensive (losses)/income net of tax	-	-	-	-	-	-	-	-	(20)	(25)	124	79
Total comprehensive (losses)/income for the period	-	-	-	-	-	-	-	-	(20)	(25)	146	101
AT1 distributions paid	-	-	-	-	-	-	-	-	-	-	(40)	(40)
Ordinary shares issued	1	-	-	-	-	-	-	-	-	-	-	1
Transfer from equity based compensation reserve	-	-	-	-	-	-	(2)	-	-	-	2	-
Equity based compensation expensed	-	-	-	-	-	-	4	-	-	-	-	4
Settlement of Virgin Money Holdings (UK) PLC share awards	-	-	-	-	1	(3)	-	-	-	-	1	(1)
FSMA Part VII transfer from Virgin Money PLC	-	-	-	-	-	-	-	-	-	-	(13)	(13)
As at 31 March 2020[(1)]	147	(839)	2,128	915	-	16	8	1	(9)	(51)	2,758	5,074
Loss for the period	-	-	-	-	-	-	-	-	-	-	(163)	(163)
Other comprehensive income/(losses) net of tax	-	-	-	-	-	-	-	-	20	(29)	60	51
Total comprehensive income/(losses) for the period	-	-	-	-	-	-	-	-	20	(29)	(103)	(112)
AT1 distributions paid	-	-	-	-	-	-	-	-	-	-	(39)	(39)
Transfer from equity-based compensation reserve	-	-	-	-	-	-	(4)	-	-	-	4	-
Release of asset revaluation reserve	-	-	-	-	-	-	-	(1)	-	-	-	(1)
Equity based compensation expensed	-	-	-	-	-	-	6	-	-	-	-	6
FSMA Part VII transfer from Virgin Money PLC	-	-	-	-	-	-	-	-	-	-	4	4
As at 30 September 2020[(1)]	147	(839)	2,128	915	-	16	10	-	11	(80)	2,624	4,932
Profit for the period	-	-	-	-	-	-	-	-	-	-	80	80
Other comprehensive income/(losses) net of tax	-	-	-	-	-	-	-	-	20	98	(12)	106
Total comprehensive income for the period	-	-	-	-	-	-	-	-	20	98	68	186
AT1 distributions paid	-	-	-	-	-	-	-	-	-	-	(40)	(40)
Ordinary shares issued	2	-	-	-	-	-	-	-	-	-	-	2
Transfer from equity based compensation reserve	-	-	-	-	-	-	(1)	-	-	-	1	-
Equity based compensation expensed	-	-	-	-	-	-	2	-	-	-	-	2
Settlement of Virgin Money Holdings (UK) PLC share awards	-	-	-	-	-	(2)	-	-	-	-	-	(2)
As at 31 March 2021[(1)]	**149**	**(839)**	**2,128**	**915**	**-**	**14**	**11**	**-**	**31**	**18**	**2,653**	**5,080**

(1) The balances as at 1 October 2019 and 30 September 2020 have been audited; the movements in the individual six month periods to 31 March 2020 and 31 March 2021 are unaudited.

The notes on pages 79 to 99 form an integral part of these interim condensed consolidated financial statements.

Interim condensed consolidated statement of cash flows

	Note	**6 months to 31 Mar 2021 (unaudited) £m**	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Operating activities				
Profit/(loss) on ordinary activities before tax		**72**	(7)	(168)
Adjustments for:				
Non-cash or non-operating items included in profit/(loss) before tax		**(498)**	(357)	(606)
Changes in operating assets		**522**	(422)	(75)
Changes in operating liabilities		**686**	(676)	1,877
Payments for short-term and low value leases		**(1)**	(1)	(2)
Interest received		**1,033**	1,151	2,152
Interest paid		**(273)**	(383)	(684)
Tax received/(paid)		**9**	(12)	(12)
Net cash provided by/(used in) operating activities		**1,550**	(707)	2,482
Cash flows from investing activities				
Interest received		**23**	22	35
Proceeds from maturity of financial assets at FVOCI		**770**	691	1,568
Proceeds from sale of financial assets at FVOCI		**-**	551	587
Purchase of financial assets at FVOCI		**(369)**	(1,519)	(2,838)
Purchase of shares issued by UTM		**(7)**	-	(2)
Proceeds from sale of property, plant and equipment		**3**	-	5
Purchase of property, plant and equipment		**(10)**	(3)	(14)
Purchase and development of intangible assets		**(22)**	(51)	(78)
Net cash provided by/(used in) investing activities		**388**	(309)	(737)
Cash flows from financing activities				
Interest paid		**(58)**	(78)	(195)
Repayment of principal portions of lease liabilities	5.3	**(14)**	(15)	(30)
Redemption and principal repayment on RMBS and covered bonds	5.3	**(943)**	(876)	(1,492)
Redemption and principal repayment on medium-term notes/subordinated debt	5.3	**(30)**	-	(745)
Issuance of RMBS and covered bonds	5.3	**-**	491	491
Issuance of medium-term notes/subordinated debt	5.3	**-**	-	922
Amounts drawn under the TFSME	5.3	**1,750**	-	1,300
Amounts repaid under the TFS	5.3	**(1,500)**	(200)	(3,234)
AT1 distributions	4.1	**(40)**	(40)	(79)
Net cash used in financing activities		**(835)**	(718)	(3,062)
Net increase/(decrease) in cash and cash equivalents		**1,103**	(1,734)	(1,317)
Cash and cash equivalents at the beginning of the period		**9,814**	11,131	11,131
Cash and cash equivalents at the end of the period		**10,917**	9,397	9,814

The notes on pages 79 to 99 form an integral part of these interim condensed consolidated financial statements.

Notes to the interim condensed consolidated financial statements

Section 1: Basis of preparation and accounting policies

Overview

These interim condensed consolidated financial statements for the six months ended 31 March 2021 have been prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006, including IAS 34 'Interim Financial Reporting', and have been prepared in accordance with IFRSs as issued by the International Accounting Standards Board (IASB), including interpretations issued by the IFRS Interpretations Committee adopted pursuant to regulation (EC) No 1606/2002 as it applies in the EU[(1)]. They do not include all the information required by IFRS in full annual financial statements and should therefore be read in conjunction with the Group's 2020 Annual Report and Accounts. Copies of the 2020 Annual Report and Accounts are available from the Group's website at https://www.virginmoneyukplc.com/investor-relations/results-and-reporting/annual-reports/.

The information in these interim condensed consolidated financial statements is unaudited and does not constitute annual accounts within the meaning of Section 434 of the Companies Act 2006 ('the Act'). Statutory accounts for the year ended 30 September 2020 have been delivered to the Registrar of Companies and contained an unqualified audit report under Section 495 of the Act, which did not draw attention to any matters by way of emphasis and did not contain any statements under Section 498 of the Act.

1.1 Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position, are set out in the business and financial review section of these interim condensed consolidated financial statements. This should be read in conjunction with the strategic report which can be found in the Group's 2020 Annual Report and Accounts. In addition, the Risk report contained in the 2020 Annual Report and Accounts includes the Group's risk management objectives. The Group's objectives, policies and processes for managing capital can be found in the risk management section of this report.

The Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future and that the Group is well placed to manage its business risks successfully. Accordingly, they continue to adopt the going concern basis in preparing these interim condensed consolidated financial statements. In reaching this assessment, the Directors have considered a wide range of information relating to present and future conditions. These include the implications of the COVID-19 pandemic, as well as potential impacts from other top and emerging risks, and the related impact on profitability, capital and liquidity.

1.2 Accounting policies

The accounting policies adopted in the preparation of these interim condensed consolidated financial statements are consistent with those policies followed in the preparation of the Group's 2020 Annual Report and Accounts except for those policies highlighted below. Comparatives are presented on a basis that conforms to the current presentation except where stated otherwise.

Change in presentation – ECLs on off-balance sheet exposures

ECLs on off-balance sheet exposures of £10m are now presented as part of the provisions for liabilities and charges balance (note 3.7). In previous periods, these had been presented as part of the impairment provision on credit exposures offset against loans and advances to customers (£7m as at 30 September 2020). The prior period comparative has not been restated for this change in presentation.

(1) As the Group's accounting period straddles 31 December 2020, the date the UK ceased to be subject to EU law, the 2021 published financial reports are required to follow and refer to EU adopted international accounting standards. From 1 October 2021, the Group will follow and refer only to UK adopted international accounting standards, with the UK Endorsement Board being the body responsible for providing authorisation for the use of new IASB standards, amendments or interpretations in the UK from 1 January 2021. As at 31 March 2021, there were no endorsement disparities between the UK and EU.

Notes to the interim condensed consolidated financial statements

Section 1: Basis of preparation and accounting policies (continued)

1.3 Critical accounting estimates and judgements

The preparation of financial statements requires the use of certain critical accounting estimates and judgements that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosed amounts of contingent liabilities. Assumptions made at each balance sheet date are based on best estimates at that date. Although the Group has internal control systems in place to ensure that best estimates can be reliably measured, actual amounts may differ from those estimated. The only change to the Group's critical accounting estimates and judgements compared to those shown in the Group's 2020 Annual Report and Accounts relates to PPI redress provisions. The Group has finalised all complaints received up to the time bar of August 2019 and is currently in the process of closing down PPI operations. Consequently, the level of management estimate and judgement required has significantly reduced to a level where this is no longer assessed as critical.

An update on ECLs and the allowance for impairment losses on credit exposures is provided within the credit risk section of the Risk report, and an update on the effective interest rate (EIR) is provided below:

EIR

EIR is determined at initial recognition based upon management's best estimate of the future cash flows of the financial instrument. In the event these estimates are revised at a later date, a present value adjustment to the carrying value of the EIR asset may be recognised in profit or loss. Such adjustments can introduce income statement volatility and consequently the EIR method introduces a source of estimation uncertainty. Management considers that material risk of adjustments exists in relation to the application of EIR to the Group's mortgage and credit card portfolios.

Mortgages

The main accounting judgement when assessing the cash flows within the Group's secured lending EIR model is the product life (including assumptions based on observed historic customer behaviour when in a standard variable rate period) and the early repayment charge income receivable. If customer repayments, redemptions or product transfers were to take place one month earlier, the loans and advances to customers balance would reduce by £10m with the adjustment recognised in net interest income.

Credit cards

The Group measures credit card EIR by modelling expected cash flows based on assumptions of future customer behaviour, which is supported by observed experience. Key behavioural assumptions include an estimation of utilisation of available credit, transaction and repayment activity and the retention of the customer balance after the end of a promotional period.

The EIR of new business written in the current period remains in line with 2020 at 5.6%.

The Group continues to monitor the impact of COVID-19 on the expected cash flows. Adjustments have been made to assumptions of future customer behaviour, with specific consideration to retail transactions and repayment activity. In the weeks following the easing of the summer lockdown restrictions, retail spend recovered to 85% of pre-COVID-19 volumes however dropped to 65% during the most recent lockdown. The Group currently assumes that retail and cash transaction activity will recover during 2021 as the UK economy reopens. In addition to the changes in retail spend, the Group also observed elevated levels of repayments as customers have taken the opportunity to deleverage. If the elevated customer repayment levels continue for the next 6 months to 30 September 2021, the Group estimates this will result in a negative present value adjustment of approximately £16m.

The Group holds an appropriate level of model risk reserve across both asset classes to mitigate the risk of estimation uncertainty.

Section 1: Basis of preparation and accounting policies (continued)

1.4 Accounting developments

The Group has also adopted the following IASB pronouncements in the current financial period which have all been endorsed for use in the EU. Unless stated otherwise, these do not have a material impact on the interim condensed consolidated financial statements:

- amendments to IFRS 3 'Business Combinations' issued October 2018 and effective for financial years beginning on or after 1 January 2020. This amendment revises the definition of a business and will assist in clarifying whether a transaction is an asset acquisition or a business combination;
- amendment to IAS 1 and IAS 8 'Definition of Material' issued in October 2018 and effective prospectively for financial years beginning on or after 1 January 2020. The amendments are intended to make the definition of material easier to understand and are not intended to alter the underlying concept of materiality in IFRS Standards. The concept of obscuring' material information with immaterial information has been included as part of the new definition; and
- amendment to IFRS 16 and COVID-19 related rent concessions issued in May 2020 and effective for financial years beginning on or after 1 June 2020. The amendment provides an optional practical expedient for lessees from assessing whether a rent concession related to COVID-19 is a lease modification. The Group does not receive rent concessions.

Early adoption - Interest Rate Benchmark Reform – Phase 2 (Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16)

Following completion of the second part of the IASB's two-phased project, amendments were issued in August 2020 (adopted for use in both the UK and EU in January 2021) and effective for financial years beginning on or after 1 January 2021. The Group early adopted the amendments from 1 October 2020.

The amendments address issues that might affect financial reporting as a result of the reform of an interest rate benchmark, including the effects of changes to contractual cash flows or hedging relationships arising from the replacement of an interest rate benchmark with an alternative benchmark rate. The amendments provide practical relief from certain requirements in IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 relating to:

- changes in the basis for determining contractual cash flows of financial assets, financial liabilities and lease liabilities; and
- hedge accounting.

There was no impact on amounts reported for prior years as a result of early adoption. Further detail is provided in note 3.3.

During the period, there have been no further pronouncements issued by the IASB that are considered relevant and material to the Group.

1.5 Presentation of risk disclosures

Certain disclosures outlined in IFRS 7 'Financial Instruments: Disclosure' concerning the nature and extent of risks relating to financial instruments have been included within the risk management section of this report.

Section 2: Results for the period

2.1 Segment information

The Group's operating segments are operating units engaged in providing different products or services and whose operating results and overall performance are regularly reviewed by the Group's Chief Operating Decision Maker, the Executive Leadership Team.

In March 2021, the business announced changes in the Executive Leadership Team. The Group will continue to operate under a three segments model: Mortgages, Personal and Business, which will now be reported through the Chief Commercial Officer. At this point in time, the business continues to be reported to the Group's Chief Operating Decision Maker as a single segment and decisions made on the performance of the Group on that basis. Segmental information will therefore continue to be presented on this single segment basis.

	6 months to 31 Mar 2021 (unaudited) £m	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Net interest income	**646**	671	1,283
Non-interest income	**49**	96	160
Total operating income	**695**	767	1,443
Operating and administrative expenses	**(585)**	(537)	(1,104)
Impairment losses on credit exposures	**(38)**	(237)	(507)
Segment profit/(loss) before tax	**72**	(7)	(168)
Average interest earning assets	**87,134**	86,847	86,826

2.2 Net interest income

	6 months to 31 Mar 2021 (unaudited) £m	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Interest income			
Loans and advances to customers	**940**	1,083	2,062
Loans and advances to other banks	**4**	30	35
Financial assets at FVOCI	**9**	22	32
Total interest income	**953**	1,135	2,129
Other similar interest			
Financial assets at FVTPL	**5**	8	15
Derivatives economically hedging interest bearing assets	**(3)**	(3)	(7)
Total other similar interest	**2**	5	8
Less: interest expense and similar charges			
Customer deposits	**(208)**	(315)	(588)
Debt securities in issue	**(83)**	(106)	(193)
Due to other banks	**(16)**	(46)	(68)
Other interest expense	**(2)**	(2)	(5)
Total interest expense and similar charges	**(309)**	(469)	(854)
Net interest income	**646**	671	1,283

Section 2: Results for the period (continued)

2.3 Non-interest income

	6 months to 31 Mar 2021 (unaudited) £m	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Gains less losses on financial instruments at fair value			
Held for trading derivatives	**3**	9	15
Financial assets and liabilities at fair value[1]	**(8)**	(2)	2
Ineffectiveness arising from fair value hedges	**(6)**	(8)	(17)
Amounts recycled to profit and loss from cash flow hedges[2]	**(3)**	-	(5)
Ineffectiveness arising from cash flow hedges	**(1)**	(8)	(6)
	(15)	(9)	(11)
Other operating income			
Net fee and commission income	**59**	81	142
Margin on foreign exchange derivative brokerage	**8**	9	17
Gain on sale of financial assets at FVOCI	**-**	16	16
Share of JV loss after tax	**(4)**	(3)	(7)
Other income	**1**	2	3
	64	105	171
Total non-interest income	**49**	96	160

(1) Included within financial assets and liabilities at fair value is a credit risk gain on loans and advances at fair value of £Nil and a fair value loss of £9m (31 March 2020: £1m gain and £3m loss, 30 September 2020: £1m gain and £5m loss).
(2) In respect of terminated hedges.

Non-interest income includes the following fee and commission income disaggregated by income type:

	6 months to 31 Mar 2021 (unaudited) £m	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Current account and debit card fees	**43**	55	94
Credit cards	**16**	22	41
Insurance, protection and investments	**6**	12	16
Other fees[1]	**13**	14	31
Total fee and commission income	**78**	103	182
Total fee and commission expense	**(19)**	(22)	(40)
Net fee and commission income	**59**	81	142

(1) Other fees include mortgages, invoice and asset finance and ATM fees.

2.4 Operating and administrative expenses

	6 months to 31 Mar 2021 (unaudited) £m	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Personnel expenses	**183**	203	396
Depreciation and amortisation expense	**87**	76	149
Other operating and administrative expenses	**315**	258	559
Total operating and administrative expenses	**585**	537	1,104

Personnel expenses comprise the following items:

	6 months to 31 Mar 2021 (unaudited) £m	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Salaries, wages and non-cash benefits and social security costs	**131**	121	252
Defined contribution pension expense	**25**	25	49
Defined benefit pension credit	**(2)**	(1)	-
Equity based compensation	**2**	4	10
Other personnel expenses	**27**	54	85
Personnel expenses	**183**	203	396

Section 2: Results for the period (continued)

2.5 Taxation

	6 months to 31 Mar 2021 (unaudited) £m	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Current tax			
Current period	**16**	7	10
Adjustment in respect of prior periods	**-**	1	(6)
	16	8	4
Deferred tax			
Current period	**(23)**	(37)	(38)
Adjustment in respect of prior periods	**(1)**	-	7
	(24)	(37)	(31)
Tax credit for the period	**(8)**	(29)	(27)

The tax assessed for the period differs from that arising from applying the standard rate of corporation tax in the UK of 19%. A reconciliation from the expense/(credit) implied by the standard rate to the actual tax credit is as follows:

	6 months to 31 Mar 2021 (unaudited) £m	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Profit/(loss) on ordinary activities before tax	**72**	(7)	(168)
Tax expense/(credit) based on the standard rate of corporation tax in the UK of 19% (March and September 2020: 19%)	**14**	(1)	(32)
Effects of:			
Disallowable expenses	**12**	1	5
Conduct indemnity adjustment	**32**	8	(39)
Deferred tax assets (recognised)/derecognised	**(55)**	4	90
Impact of rate changes	**(7)**	(34)	(37)
AT1 distribution	**(8)**	(8)	(15)
Banking surcharge	**5**	-	-
Adjustments in respect of prior periods	**(1)**	1	1
Tax credit for the period	**(8)**	(29)	(27)

Deferred tax assets recognised represent historic losses, previously derecognised, that are now brought onto the balance sheet in accordance with the Group's established methodology, reflecting their expected utilisation against future taxable profits. The recognition of historic losses has been partially offset by an increase in the conduct indemnity adjustment.

Section 2: Results for the period (continued)

2.6 Earnings per share

	6 months to 31 Mar 2021 (unaudited) £m	6 months to 31 Mar 2020 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
Profit/(loss) attributable to ordinary equity holders for the purposes of basic and diluted EPS	**40**	(18)	(220)

	31 Mar 2021 Number of shares	31 Mar 2020 Number of shares	30 Sep 2020 Number of shares
Weighted-average number of ordinary shares in issue (millions)			
- Basic	**1,442**	1,440	1,440
- Diluted	**1,444**	1,440	1,440
Basic earnings/(loss) per share (pence)	**2.8**	(1.2)	(15.3)
Diluted earnings/(loss) per share (pence)	**2.8**	(1.2)	(15.3)

Basic earnings/(loss) per share has been calculated after deducting 0.2m (31 March 2020: 0.5m, 30 September 2020: 0.3m) ordinary shares representing the weighted average of the Group’s holdings of its own shares. The calculation of the diluted EPS for the comparative periods excluded conditional awards of 1m ordinary shares made under equity based compensation schemes. These were considered anti-dilutive due to the Group making a loss in these periods.

Section 3: Assets and liabilities

3.1 Loans and advances to customers

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m
Gross loans and advances to customers(1)	**72,753**	72,925
Impairment provisions on credit exposures(2)	**(711)**	(735)
Fair value hedge adjustment	**(35)**	240
	72,007	72,430

(1) Included within gross loans and advances is £653m (30 September 2020: £706m) relating to finance lease receivables.

(2) ECLs on off-balance sheet exposures are now presented as part of the provisions for liabilities and charges balance (note 3.7). In previous periods, these had been presented as part of the overall ECL allowance (£7m as at 30 September 2020). Prior periods have not been restated for this change in presentation.

The Group has a portfolio of fair valued business loans of £158m (30 September 2020: £190m) which are classified separately as financial assets at FVTPL on the balance sheet (note 3.2). Combined with the above this is equivalent to total loans and advances of £72,165m (30 September 2020: £72,620m).

The fair value hedge adjustment represents an offset to the fair value movement on derivatives designated in hedge relationships to manage the interest rate risk inherent in the Group's fixed rate mortgage portfolio.

The Group has transferred a proportion of mortgages to the securitisation and covered bond programmes.

3.2 Financial assets at fair value through profit or loss

Loans and advances

Included in financial assets at FVTPL is a historical portfolio of loans. Interest rate risk associated with these loans is managed using interest rate derivative contracts and the loans are recorded at fair value to avoid an accounting mismatch. The maximum credit exposure of the loans is £158m (30 September 2020: £190m) including accrued interest receivable of £Nil (30 September 2020: £1m). The cumulative loss in the fair value of the loans attributable to changes in credit risk amounts to £3m (30 September 2020: £3m); the change for the current period is £Nil (30 September 2020: decrease of £1m).

Other financial assets

Other financial assets of £13m (30 September 2020: £13m) consist of £12m (30 September 2020: £12m) of unlisted securities and £1m (30 September 2020: £1m) of debt instruments.

Refer to note 3.9 for further information on the valuation methodology applied to financial assets held at FVTPL and their classification within the fair value hierarchy. Details of the credit quality of financial assets is provided in the Risk report.

Section 3: Assets and liabilities (continued)

3.3 Derivative financial instruments

The tables below analyse derivatives between those designated as hedging instruments and those classified as held for trading:

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m
Fair value of derivative financial assets		
Designated as hedging instruments	**165**	198
Designated as held for trading	**57**	120
	222	318
Fair value of derivative financial liabilities		
Designated as hedging instruments	**183**	158
Designated as held for trading	**83**	92
	266	250

In respect of derivatives with other banks, cash collateral totalling £21m (30 September 2020: £53m) has been pledged and £78m has been received (30 September 2020: £93m). These amounts are included within due from and due to other banks respectively. Collateral placed with clearing houses, which did not meet offsetting criteria, totalled £123m (30 September 2020: £202m) and is included within other assets.

The derivative financial instruments held by the Group are further analysed below. The notional contract amount is the amount from which the cash flows are derived and does not represent the principal amounts at risk relating to these contracts.

	31 March 2021 (unaudited)			30 September 2020 (audited)		
Total derivative contracts	**Notional contract amount £m**	**Fair value of assets £m**	**Fair value of liabilities £m**	Notional contract amount £m	Fair value of assets £m	Fair value of liabilities £m
Derivatives designated as hedging instruments						
Cash flow hedges						
Interest rate swaps (gross)	**24,201**	**88**	**87**	29,645	74	215
Less: net settled interest rate swaps(1)	**(16,395)**	**(46)**	**(74)**	(19,187)	(13)	(171)
Interest rate swaps (net)(2)	**7,806**	**42**	**13**	10,458	61	44
Cross currency swaps(2)	**197**	**11**	**8**	420	28	-
	8,003	**53**	**21**	10,878	89	44
Fair value hedges						
Interest rate swaps (gross)	**42,541**	**313**	**535**	37,803	182	751
Less: net settled interest rate swaps(1)	**(34,870)**	**(202)**	**(461)**	(30,603)	(92)	(642)
Interest rate swaps (net)(2)	**7,671**	**111**	**74**	7,200	90	109
Cross currency swaps(2)	**1,448**	**1**	**88**	1,448	19	5
	9,119	**112**	**162**	8,648	109	114
Total derivatives designated as hedging instruments	**17,122**	**165**	**183**	19,526	198	158
Derivatives designated as held for trading						
Foreign exchange rate related contracts						
Spot and forward foreign exchange(2)	**1,169**	**23**	**22**	1,003	15	15
Cross currency swaps(2)	**598**	**3**	**10**	1,263	56	7
Options(2)	**1**	**-**	**-**	1	-	-
	1,768	**26**	**32**	2,267	71	22
Interest rate related contracts						
Swaps(2)	**731**	**17**	**36**	704	28	47
Swaptions(2)	**10**	**-**	**1**	10	-	2
Options(2)	**416**	**1**	**2**	426	2	3
	1,157	**18**	**39**	1,140	30	52
Commodity related contracts	**145**	**13**	**12**	131	19	18
Total derivatives designated as held for trading	**3,070**	**57**	**83**	3,538	120	92

(1) Presented within other assets
(2) Presented within derivative financial instruments

Section 3: Assets and liabilities (continued)

3.3 Derivative financial instruments (continued)

Derivatives transacted to manage the Group's interest rate exposure on a net portfolio basis are accounted for as either cash flow hedges or fair value hedges as appropriate. Cash flow hedged derivatives include vanilla interest rate swaps and cross currency swaps. Derivatives traded to manage interest rate risk on certain fixed rate assets, such as UK Government Gilts, are accounted for as fair value hedges.

The Group hedging positions also include those designated as foreign currency and interest rate hedges of debt issued from the Group's securitisation and covered bond programmes. As such, certain derivative financial assets and liabilities have been booked in structured entities and consolidated within these financial statements.

Interest Rate Benchmark Reform – Phase 1

The Group has early adopted and applied the Amendments to IAS 39 and IFRS 7 on Interest Rate Benchmark Reform (the Phase 1 amendments). The Phase 1 amendments provide temporary exceptions from applying specific hedge accounting requirements during the period of uncertainty resulting from interest rate benchmark reform. However, any hedge ineffectiveness continues to be recorded in the income statement.

The Group has cash flow and fair value hedge accounting relationships that are exposed to GBP LIBOR, which are subject to the interest rate benchmark reform.

As at 31 March 2021, the notional amount of hedged items and hedging instruments to which these Phase 1 amendments apply was £772m, of which £702m relates to fair value hedges (principally a fixed rate issuance) and £70m relates to cash flow hedges (principally debt securities in issue).

The Group will continue to apply the Phase 1 amendments to IAS 39 until the uncertainty arising from interest rate benchmark reform is no longer present. The Group has assumed that this uncertainty will not end until items that reference IBORs are amended to specify the alternative benchmark rate, the relevant spread adjustment and the date on which the interest rate benchmark will be replaced.

Interest Rate Benchmark Reform – Phase 2

As highlighted in note 1.4, the Group has early adopted and applied the Interest Rate Benchmark Reform – Phase 2 (Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16) from 1 October 2020.

During the period, the Group has applied the relief which permits the amount in the cash flow hedge reserve relating to a de-designated hedge to be deemed based on the alternative benchmark rate on which the future cash flows will be based. There was no impact on amounts reported for prior years as a result of early adoption of the Phase 2 amendments.

Further detail on the Group's approach to managing the risk of LIBOR replacement is provided on page 71.

Section 3: Assets and liabilities (continued)

3.4 Deferred tax

The Group has recognised deferred tax in relation to the following items:

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m
Deferred tax assets		
Tax losses carried forward	**170**	151
Capital allowances	**115**	113
Cash flow hedge reserve	**-**	23
Acquisition accounting adjustments(1)	**-**	1
Transitional adjustment - IFRS 9	**14**	15
Employee equity based compensation	**7**	5
Unamortised issue costs	**2**	4
Pension spreading	**8**	9
Other	**8**	5
	324	326
Deferred tax liabilities		
Defined benefit pension scheme surplus	**(253)**	(253)
Acquisition accounting adjustments(1)	**(9)**	(11)
Gains on financial instruments at FVOCI	**(13)**	(6)
Cash flow hedge reserve	**(11)**	-
Intangible assets	**(3)**	(3)
Other	**(3)**	(1)
	(292)	(274)
Net deferred tax asset	**32**	52

(1) Following the execution of FSMA part VII, the deferred tax assets and liabilities in respect of acquisition accounting adjustments have been offset to provide a single number that will unwind in the same entity over coming years.

The deferred tax assets and liabilities detailed above arise primarily in Clydesdale Bank PLC.

The value of tax losses carried forward of £170m (30 September 2020: £151m) has increased due to the additional recognition in the current period of historic losses, previously derecognised, that are now brought onto the balance sheet in accordance with the Group's established methodology, reflecting their expected utilisation against future taxable profits. The recognition of historic losses has been partially offset by an increase in the conduct indemnity adjustment. In addition, the Group had an unrecognised deferred tax asset at 31 March 2021 of £163m (30 September 2020: £217m) representing trading losses with a gross value of £856m valued at 19% (30 September 2020: £1,142m valued at 19%).

It was announced in the March 2021 Budget that the UK main rate of corporation will increase from 19% to 25% with effect from 1 April 2023. The impact of the change on the net deferred tax asset recognised at 31 March 2021 is estimated to be an increase of approximately £50m. The potential impact of the rate change is calculated on the basis that the banking surcharge rate will remain at 8% for relevant profits in excess of £25m. The government has announced it will undertake a review of the banking surcharge and set out proposals in the autumn to ensure that the combined rate of tax on banks' profits does not increase substantially from its current level. No proposals have been announced as at the date of this report.

Section 3: Assets and liabilities (continued)

3.5 Debt securities in issue

The breakdown of debt securities in issue is shown below:

31 March 2021 (unaudited)	**Medium-term notes £m**	**Subordinated debt £m**	**Securitisation £m**	**Covered bonds £m**	**Total £m**
Amortised cost	**1,964**	**720**	**2,974**	**1,808**	**7,466**
Fair value hedge adjustments	**28**	**(10)**	**6**	**46**	**70**
Total debt securities	**1,992**	**710**	**2,980**	**1,854**	**7,536**
Accrued interest payable	**18**	**13**	**3**	**27**	**61**
	2,010	**723**	**2,983**	**1,881**	**7,597**

30 September 2020 (audited)	Medium-term notes £m	Subordinated debt £m	Securitisation £m	Covered bonds £m	Total £m
Amortised cost	1,991	750	3,992	1,842	8,575
Fair value hedge adjustments	64	-	10	76	150
Total debt securities	2,055	750	4,002	1,918	8,725
Accrued interest payable	13	7	3	10	33
	2,068	757	4,005	1,928	8,758

The following tables provide a breakdown of the medium-term notes and subordinated debt by instrument:

Medium-term notes (excluding accrued interest)

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m
VM UK 3.125% fixed-to-floating rate callable senior notes due 2025	**299**	298
VM UK 4% fixed rate reset callable senior notes due 2026	**517**	529
VM UK 3.375% fixed rate reset callable senior notes due 2026	**361**	369
VM UK 4% fixed rate reset callable senior notes due 2027	**395**	406
VM UK 2.875% fixed rate reset callable senior notes due 2025	**420**	453
	1,992	2,055

Subordinated debt (excluding accrued interest)

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m
VM UK 5% fixed rate reset callable subordinated notes due 2026	**-**	31
VM UK 7.875% fixed rate reset callable subordinated notes due 2028	**248**	247
VM UK 5.175% fixed rate reset callable subordinated notes due 2030	**462**	472
	710	750

The Group has not issued any medium-term notes, subordinated debt or covered bonds during the period (30 September 2020: £922m) or any notes from the securitisation programmes (30 September 2020: £491m). The reduction in the securitisation carrying value is as a result of scheduled principal redemptions on outstanding securitisation notes.

3.6 Due to other banks

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m
Secured loans	**5,659**	5,397
Transaction balances with other banks	**10**	15
Deposits from other banks	**23**	57
	5,692	5,469

Secured loans comprise amounts drawn under the TFS and TFSME schemes (including accrued interest).

Section 3: Assets and liabilities (continued)

3.7 Provisions for liabilities and charges

	6 months to 31 Mar 2021 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
PPI redress provision		
Opening balance	**107**	379
Charge to the income statement	**59**	-
Utilised	**(133)**	(272)
Closing balance	**33**	107
Customer redress and other provisions		
Opening balance	**31**	33
Charge to the income statement	**12**	28
Utilised	**(14)**	(30)
Closing balance	**29**	31
Property closure and redundancy provision		
Opening balance	**34**	44
Charge to the income statement	**18**	19
Utilised	**(23)**	(29)
Closing balance	**29**	34
Off-balance sheet ECL provision(1)		
Opening balance	**-**	-
Transfer of ECL provision from loans and advances	**7**	-
Charge to the income statement	**3**	-
Closing balance	**10**	-
Total provisions for liabilities and charges	**101**	172

(1) During the period, the Group changed its presentation of off-balance sheet ECLs. These are now presented as part of the provision for liabilities and charges instead of as part of the impairment provision offset against loans and advances. At 31 March 2021, the £10m off-balance sheet ECLs represented £3m in Stage 1 and £7m in Stage 2 (30 September 2020: £1m in Stage 1 and £6m in Stage 2).

PPI redress provision

The Group has now dealt with complaints received in the period up to the time bar in August 2019, including the settlement of claims received from the Official Receiver which is currently being finalised. The Group is working towards closing down the operation later this year. The remaining provision is expected to be sufficient to cover all outstanding liabilities in respect of the mis-selling of PPI policies. The total provision raised to date in respect of PPI is £3,114m (30 September 2020: £3,055m), with £33m of this remaining (30 September 2020: £107m).

Customer redress and other provisions

Other provisions include amounts in respect of a number of non-PPI customer redress matters, legal proceedings, claims arising in the ordinary course of the Group's business and other matters. A number of these matters are now reaching a conclusion and the risk that the final amount required to settle the Group's potential liabilities in these matters being materially more than the remaining provision is now considered to be low.

Section 3: Assets and liabilities (continued)

3.8 Retirement benefit obligations

The Group funds a defined benefit pension scheme, the Yorkshire and Clydesdale Bank Pension Scheme ('the Scheme'). The Group's trading subsidiary, Clydesdale Bank PLC, is the sponsoring employer in the Scheme, which was closed to future benefit accrual for the majority of current employees on 1 August 2017. The assets of the Scheme are held in a trustee administered fund, with the Trustee responsible for the operation and governance of the Scheme, including making decisions regarding the Scheme's funding and investment strategy.

The following table provides a summary of the fair value of plan assets and present value of the defined benefit obligation for the Scheme:

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m
Fair value of Scheme assets	**4,392**	4,681
Total defined benefit obligation	**(3,668)**	(3,958)
Net defined benefit pension asset	**724**	723

The latest formal triennial valuation for the Scheme was undertaken as at 30 September 2019 and reported a surplus of £144m (previously a deficit of £290m). Whilst no additional contributions are due in respect of the 2019 valuation due to the surplus position, the Group continues to make deficit contributions in respect of the previous 2016 valuation following a payment holiday agreed between the Group and the Trustee. As at 31 March 2021, contributions of £46m remain outstanding, which will be paid at a rate of £2m per month until April 2023. These deficit contributions rank senior to ordinary dividend payments.

3.9 Fair value of financial instruments

This section should be read in conjunction with note 3.16 of the Group's 2020 Annual Report and Accounts, which provides more detail about accounting policies adopted and valuation methodologies used in calculating fair value. There have been no changes in the accounting policies adopted or the valuation methodologies used.

(a) Fair value of financial instruments recognised on the balance sheet at amortised cost

The tables below show a comparison of the carrying amounts of financial assets and liabilities measured at amortised cost, as reported on the balance sheet, and their fair values where these are not approximately equal.

There are various limitations inherent in this fair value disclosure, particularly where prices are derived from unobservable inputs due to some financial instruments not being traded in an active market. The methodologies and assumptions used in the fair value estimates are therefore described in the notes to the tables. The difference between carrying value and fair value is relevant in a trading environment but is not relevant to assets such as loans and advances.

	31 Mar 2021 (unaudited)		30 Sep 2020 (audited)	
	Carrying value £m	**Fair value £m**	Carrying value £m	Fair value £m
Financial assets				
Loans and advances to customers[(1)]	**72,007**	**72,653**	72,430	71,788
Financial liabilities				
Customer deposits[(2)]	**68,674**	**68,920**	67,710	67,809
Debt securities in issue[(3)]	**7,597**	**7,952**	8,758	8,836

(1) Loans and advances to customers are categorised as Level 3 in the fair value hierarchy with the exception of £1,062m (30 September 2020: £1,060m) of overdrafts which are categorised as Level 2.
(2) Categorised as Level 2 in the fair value hierarchy.
(3) Categorised as Level 2 in the fair value hierarchy with the exception of £2,964m of listed debt (30 September 2020: £2,846m) which is categorised as level 1.

Section 3: Assets and liabilities (continued)

3.9 Fair value of financial instruments (continued)

(b) Fair value of financial instruments recognised on the balance sheet at fair value

The following tables provide an analysis of financial instruments that are measured at fair value, using the fair value hierarchy described above:

	Fair value measurement as at 31 Mar 2021 (unaudited)				Fair value measurement as at 30 Sep 2020 (audited)			
	Level 1 £m	**Level 2 £m**	**Level 3 £m**	**Total £m**	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets								
Financial assets at FVOCI	**4,532**	**-**	**-**	**4,532**	5,080	-	-	5,080
Loans and advances at FVTPL	**-**	**158**	**-**	**158**	-	190	-	190
Other financial assets at FVTPL	**-**	**8**	**5**	**13**	-	8	5	13
Derivative financial assets	**-**	**222**	**-**	**222**	-	318	-	318
Total financial assets at fair value	**4,532**	**388**	**5**	**4,925**	5,080	516	5	5,601
Financial liabilities								
Derivative financial liabilities	**-**	**266**	**-**	**266**	-	250	-	250
Total financial liabilities at fair value	**-**	**266**	**-**	**266**	-	250	-	250

There were no transfers between Level 1 and 2 in the current or prior period.

Additional analysis on assets and liabilities measured at fair value based on valuation techniques for which any significant input is not based on observable market data (Level 3):

Level 3 movement analysis: **Financial assets at FVTPL**	**6 months to 31 Mar 2021 (unaudited) £m**	12 months to 30 Sep 2020 (audited) £m
Balance at the beginning of the period	**5**	14
Fair value gains recognised[(1)]		
In profit or loss - unrealised	**-**	1
In profit or loss - realised	**-**	5
Sales	**-**	(10)
Settlements	**-**	(5)
Balance at the end of the period	**5**	5

(1) Net gains or losses were recorded in non-interest income or FVOCI reserve as appropriate.

Section 3: Assets and liabilities (continued)

3.9 Fair value of financial instruments (continued)

Quantitative information about significant unobservable inputs in Level 3 valuations

The table below lists key unobservable inputs to Level 3 financial instruments, and provides the range of those inputs as at 31 March 2021:

	Fair value £m	Valuation technique	Unobservable inputs	Low range	High range
Other financial assets at FVTPL					
Equity investments	4	Discounted cash flow	Contingent litigation risk	0%	100%
Debt investments	1	Discounted cash flow	Recoverable amount	0%	100%

Sensitivity of Level 3 fair value measurements to reasonably possible alternative assumptions

Where valuation techniques use non-observable inputs that are significant to a fair value measurement in its entirety, changing these inputs will change the resultant fair value measurement.

The most significant input into the FVTPL equity investment is the contingent litigation risk. Were this to crystallise in its entirety, the carrying value of the equity investments would reduce by £3m.

Other than this significant Level 3 measurement, the Group has a limited remaining exposure to Level 3 fair value measurements and changing one or more of the inputs for fair value measurements in Level 3 to reasonable alternative assumptions would not change the fair value significantly with respect to profit or loss, total assets, total liabilities or equity on these remaining Level 3 measurements.

Section 4: Capital

4.1 Equity

4.1.1 Share capital and share premium

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m
Share capital	**144**	144
Share premium	**5**	3
Share capital and share premium	**149**	147

	31 Mar 2021 (unaudited) Number of shares	30 Sep 2020 (audited) Number of shares	**31 Mar 2021 (unaudited) £m**	30 Sep 2020 (audited) £m
Ordinary shares of £0.10 each - allotted, called up, and fully paid				
Opening ordinary share capital	**1,438,574,687**	1,434,485,689	**144**	143
Issued under employee share schemes	**1,246,491**	4,088,998	**-**	1
Closing ordinary share capital	**1,439,821,178**	1,438,574,687	**144**	144

The holders of ordinary shares are entitled to dividends as declared from time to time and are entitled to one vote per share at meetings of the shareholders of the Company. All shares in issue at 31 March 2021 rank equally with regard to the Company's residual assets.

During the period 1,246,491 (30 September 2020: 4,088,998) ordinary shares were issued under employee share schemes with a nominal value of £0.1m (30 September 2020: £0.4m).

No dividend was declared or paid in respect of the year ended 30 September 2020. In light of the current uncertainty as to the economic impact of the COVID-19 pandemic, the Directors do not recommend payment of a dividend in respect of the period ended 31 March 2021. In addition, as detailed within note 3.8, pension deficit contributions in respect of the 2016 triennial valuation rank senior to ordinary dividend payments.

Share premium represents the aggregate of all amounts that have ever been paid above par value to the Company when it has issued ordinary shares.

4.1.2 Other equity instruments

Other equity instruments consist of the following Perpetual Contingent Convertible Notes:

- Perpetual securities (fixed 8% up to the first reset date) issued on 8 February 2016 with a nominal value of £450m and optional redemption on 8 December 2022;
- Perpetual securities (fixed 8.75% up to the first reset date) issued on 10 November 2016 with a nominal value of £230m and optional redemption on 10 November 2021; and
- Perpetual securities (fixed 9.25% up to the first reset date) issued on 13 March 2019 with a nominal value of £250m and optional redemption on 8 June 2024.

The issues are treated as equity instruments in accordance with IAS 32 'Financial Instruments: Presentation' with the proceeds included in equity, net of transaction costs of £15m (30 September 2020: £15m). AT1 distributions of £40m were paid in the period (30 September 2020: £79m; 31 March 2020: £40m).

4.1.3 Capital reorganisation reserve

The capital reorganisation reserve of £839m was recognised on the issuance of the Company's ordinary shares in February 2016 in exchange for the acquisition of the entire share capital of the Group's previous parent company, CYB Investments Limited (CYBI). The reserve reflects the difference between the consideration for the issuance of the Company's shares and CYBI's share capital and share premium.

Section 4: Capital (continued)

4.1.4 Merger reserve

A merger reserve of £633m was recognised on the issuance of the Company's ordinary shares in February 2016 in exchange for the acquisition of the entire share capital of CYBI. An additional £1,495m was recognised on the issuance of the Company's ordinary shares in October 2018 in exchange for the acquisition of the entire share capital of Virgin Money Holdings (UK) PLC. The merger reserve reflects the difference between the consideration for the issuance of the Company's shares and the nominal value of the shares issued.

4.1.5 Cash flow hedge reserve

The cash flow hedge reserve represents the effective portion of cumulative post-tax gains and losses on derivatives designated as cash flow hedging instruments that will be recycled to the income statement when the hedged items affect profit or loss.

	6 months to 31 Mar 2021 (unaudited) £m	12 months to 30 Sep 2020 (audited) £m
At 1 October	**(80)**	(26)
Amounts recognised in other comprehensive income:		
Cash flow hedge – interest rate risk		
Effective portion of changes in fair value of interest rate swaps	**136**	(74)
Amounts transferred to the income statement	**(3)**	1
Taxation	**(35)**	19
Cash flow hedge – foreign exchange risk		
Effective portion of changes in fair value of cross currency swaps	**(25)**	(59)
Amounts transferred to the income statement	**25**	59
Closing cash flow hedge reserve	**18**	(80)

Section 5: Other notes

5.1 Contingent liabilities and commitments

The table below sets out the amounts of financial guarantees and commitments which are not recorded on the balance sheet. Financial guarantees and commitments are credit-related instruments which include acceptances, letters of credit, guarantees and commitments to extend credit. The amounts do not represent the amounts at risk at the balance sheet date but the amounts that would be at risk should the contracts be fully drawn upon and the customer default. Since a significant portion of guarantees and commitments is expected to expire without being drawn upon, the total of the contract amounts is not representative of future liquidity requirements.

	31 Mar 2021 (unaudited) £m	30 Sep 2020 (audited) £m
Guarantees and assets pledged as collateral security:		
Due in less than 3 months	**19**	18
Due between 3 months and 1 year	**28**	15
Due between 1 year and 3 years	**11**	14
Due between 3 years and 5 years	**2**	2
Due after 5 years	**48**	46
	108	95
Other credit commitments		
Undrawn formal standby facilities, credit lines and other commitments to lend at call	**17,955**	16,775

Capital commitments

The Group has committed to providing additional funding of up to £12.5m over a 12 month period from June 2020 to support the strategic and customer proposition development of the Group's JV, UTM, of which £3.9m was the remaining commitment as at 31 March 2021. This was subsequently paid on 1 April 2021. Further detail on UTM can be found in the JVs and associates section of note 5.2.

Other contingent liabilities

Conduct risk related matters

There continues to be uncertainty and thus judgement is required in determining the quantum of conduct risk related liabilities, with note 3.7 reflecting the Group's current position in relation to a number of these matters where a provision can be reliably estimated. Until all matters are closed the final amount required to settle the Group's potential liabilities for conduct related matters remains uncertain.

The Group will continue to reassess the adequacy of provisions for these matters and the assumptions underlying the calculations at each reporting date based upon experience and other relevant factors at that time.

Legal claims

The Group is named in and is defending a number of legal claims arising in the ordinary course of business. No material adverse impact on the financial position of the Group is expected to arise from the ultimate resolution of these legal actions.

Section 5: Other notes (continued)

5.2 Related party transactions

The Group undertakes activity with the following entities which are considered to be related party transactions:

Yorkshire and Clydesdale Bank Pension Scheme ('the Scheme')

The Group provides banking services to the Scheme, with customer deposits of £21m (30 September 2020: £17m). Pension contributions of £14m were made to the Scheme in the period (period ended 31 March 2020: £25m; year ended 30 September 2020: £35m).

The Group and the Trustee to the Scheme (note 3.8) have entered into a contingent Security Arrangement which provides additional support to the Scheme by underpinning recovery plan contributions and some additional investment risk. The security is in the form of a pre-agreed maximum level of assets that are set aside for the benefit of the Pension Scheme in certain trigger events. These assets are held by Red Grey Square Funding LLP, an insolvency remote consolidated structured entity.

Joint ventures and associates

The Group holds investments in JVs of £6m (30 September 2020: £3m). The total share of loss for the period was £4m (period ended 31 March 2020: £3m; year ended 30 September 2020: £7m). In addition, the Group had the following transactions with JV entities during the period:

- Salary Finance Loans Limited ('Salary Finance') - the Group provides Salary Finance with a revolving credit facility funding line, of which the current gross lending balance at 31 March 2021 was £171m (30 September 2020: £119m) and the undrawn facility was £29m (30 September 2020: £81m). The facility is held under Stage 1 for credit risk purposes.
- UTM - the Group provides banking services to UTM which has resulted in amounts due of £3m (30 September 2020: £3m). Additionally, the Group received £4m of recharge income in the period (period ended 31 March 2020: £3m; year ended 30 September 2020: £7m) from UTM in accordance with a Service Level Agreement in respect of resourcing, infrastructure and marketing.

During the period, the Group provided £7m of additional funding to UTM with a further commitment of £3.9m as at 31 March 2021; this amount was paid on 1 April 2021.

Other related party transactions with Virgin Group

The Group has related party transactions with other Virgin Group companies:

- License fees due to Virgin Enterprises Limited for the use of the Virgin Money brand trademark resulted in payables of £4m (30 September 2020: £4m), with expenses incurred in the period of £7m (period ended 31 March 2020: £6m; year ended 30 September 2020: £13m).
- The Group also incurs credit card commissions and air mile charges with VAA in respect of an agreement between the two parties. Amounts payable to VAA totalled £1m (30 September 2020: £1m) and expenses of £5m were incurred in the period (period ended 31 March 2020: £8m; year ended 30 September 2020: £12m).

Charities

The Group provides banking services to Virgin Money Foundation which has resulted in customer deposits of £0.4m (30 September 2020: £Nil). The Group made donations of £1m in the period (period ended 31 March 2020: £1m; year ended 30 September 2020: £1m) to the Foundation to enable it to pursue its charitable objectives. The Group has also provided a number of support services to the Foundation on a pro bono basis, including use of facilities and employee time. The estimated gift in kind for support services provided during the period was £0.2m (period ended 31 March 2020: £0.1m; year ended 30 September 2020: £0.4m).

Section 5: Other notes (continued)

5.3 Notes to the statement of cash flows

	Term Funding Schemes[1] £m	Debt securities in issue £m	Lease liabilities £m	Total £m
1 October 2019	7,308	9,591	205	17,104
Cash flows:				
Issuances	-	1,413	-	1,413
Drawdowns	1,300	-	-	1,300
Redemptions	-	(2,237)	-	(2,237)
Repayment	(3,234)	-	(30)	(3,264)
Non-cash flows				
Fair value adjustments and associated unwind on acquired TFS and debt securities in issue	36	27	-	63
Additions to right-of-use asset in exchange for increased lease liabilities	-	-	2	2
Remeasurement	-	-	(6)	(6)
Movement in accrued interest	(13)	(7)	4	(16)
Unrealised foreign exchange movements	-	(23)	-	(23)
Unamortised costs	-	(6)	-	(6)
At 30 September 2020	5,397	8,758	175	14,330
Cash flows:				
Drawdowns	1,750	-	-	1,750
Redemptions	-	(973)	-	(973)
Repayment	(1,500)	-	(14)	(1,514)
Non-cash flows				
Fair value adjustments and associated unwind on acquired TFS and debt securities in issue	12	(81)	-	(69)
Additions to right-of-use asset in exchange for increased lease liabilities	-	-	4	4
Remeasurement	-	-	(1)	(1)
Movement in accrued interest	-	28	1	29
Unrealised foreign exchange movements	-	(136)	-	(136)
Unamortised costs	-	1	-	1
At 31 March 2021	**5,659**	**7,597**	**165**	**13,421**

(1) This includes amounts drawn under the TFS and TFSME

Measuring financial performance - glossary

Underlying adjustments

On arriving at an underlying basis, the effects of certain items that do not promote an understanding of historical or future trends of earnings or cash flows are removed, as the Directors consider that this presents more comparable results period on period. These items are all significant and are typically one-off in nature. Additional detail is provided below where considered necessary to further explain the rationale for their exclusion from underlying performance, in particular for new items in the current period or recurring non-underlying items:

Item	**6 months to 31 Mar 2021 £m**	6 months to 31 Mar 2020 £m	6 months to 30 Sep 2020 £m	Reason for exclusion from the Group's current underlying performance
Integration and transformation costs	**(49)**	(61)	(78)	These are part of the Group's publicised three-year integration plan following the acquisition of Virgin Money Holdings (UK) PLC and comprise a number of one-off expenses that are required to realise the anticipated cost synergies. Also included are one-off costs to support transformation. This programme will improve our digital capability and consequently enable super straightforward efficiency. Costs are generally restructuring in nature.
Acquisition accounting unwinds	**(47)**	(57)	(56)	This consists principally of the unwind of the IFRS 3 fair value adjustments created on the acquisition of Virgin Money Holdings (UK) PLC in October 2018 (£42m charge) and other smaller items amounting to £5m. These represent either one-off adjustments or are the scheduled reversals of the accounting adjustments that arose following the fair value exercise required by IFRS 3. These will continue to be treated as non-underlying adjustments over the expected three to five-year period until they have been fully reversed.
Legacy conduct	**(71)**	-	(26)	These costs are historical in nature and are not indicative of the Group's current practices.
Other:				
SME transformation	**(1)**	(5)	(6)	These costs related to transformation of the Group's Business lending proposition and mainly comprised costs associated with the RBS incentivised switching scheme.
UTM transition costs	**(5)**	(4)	(4)	These costs relate to UTM's transformation costs principally for the build of a new platform for administration and servicing.
VISA shares	**-**	-	5	A one-off gain on conversion of Visa B Preference shares to Series A preference shares.
Total other	**(6)**	(9)	(5)	

Glossary

For a glossary of terms and abbreviations used within this report refer to pages 260 to 265 of the Group's 2020 Annual Report and Accounts.

For terms not previously included within the Glossary, or where terms have been redefined or amounts have been quantified, refer below:

IFRS 9 transitional adjustments - dynamic	That part of the transitional adjustments on regulatory capital arising from the increase in impairment provisions (on non-credit impaired exposures) from the date of initial adoption of IFRS 9 to the reporting date.
IFRS 9 transitional adjustments - static	That part of the transitional adjustments on regulatory capital arising from the increase in impairment provisions on initial adoption of IFRS 9 from those calculated under IAS 39.
Minimum requirement for own funds and eligible liabilities (MREL) ratio	Total capital resources less ineligible AT1 and Tier 2 instruments at the period end of £5,093m (30 September 2020: £4,935m) plus senior unsecured securities issued by Virgin Money UK PLC with greater than one year to maturity at the period end of £1,976m (30 September 2020: £2,002m) divided by RWAs at the period end of £24,152m (30 September 2020: £24,399m).
Net interest margin (NIM)	Underlying net interest income as a percentage of average interest earning assets for a given period. Underlying net interest income of £677m (30 September 2020: £1,351m) is annualised and divided by average interest earning assets for a given period of £87,134m (30 September 2020: £86,826m) (which is adjusted to exclude short-term repos used for liquidity management purposes). As a result of the exclusions noted above, average interest earning assets used as the denominator have been reduced by £22m (30 September 2020: £16m).
Statutory basic earnings per share (EPS)	Statutory profit after tax attributable to ordinary equity holders of £40m (30 September 2020: loss of £220m), divided by the weighted average number of ordinary shares in issue for a given period of 1,442m shares (30 September 2020: 1,440m) (which includes deferred shares and excludes own shares held or contingently returnable shares).
Statutory return on tangible equity (RoTE)	Statutory profit after tax attributable to ordinary equity holders of £40m (30 September 2020: loss of £220m), as a percentage of average tangible equity of £3,612m (30 September 2020: £3,554m) (average total equity less intangible assets and AT1) for a given period.
Tangible net asset value (TNAV) per share	Tangible equity (total equity less intangible assets and AT1) as at the period end of £3,719m (30 September 2020: £3,526m) divided by the number of ordinary shares in issue at the period end of 1,444m (30 September 2020: 1,444m) (which includes deferred shares of 5m (30 September 2020: 6m) and excludes own shares held of 0.1m (30 September 2020: 0.2m)).
Underlying basic EPS	Underlying profit after tax attributable to ordinary equity holders of £182m (30 September 2020: £20m), divided by the weighted average number of ordinary shares in issue for a given period of 1,442m shares (30 September 2020: 1,440m) (which includes deferred shares and excludes own shares held or contingently returnable shares).
Underlying profit after tax attributable to ordinary equity holders	Underlying profit before tax of £245m (30 September 2020: £124m) less underlying tax charge of £23m (30 September 2020: £25m), less AT1 distributions of £40m (30 September 2020: £79m) and was equal to £182m (30 September 2020: £20m). The underlying tax charge (or credit) is the difference between the statutory tax charge (or credit) and the tax attributable to exceptional items.
Underlying RoTE	Underlying profit after tax attributable to ordinary equity holders of £182m (30 September 2020: £20m), annualised, as a percentage of average tangible equity of £3,612m (30 September 2020: £3,554m) (average total equity less intangible assets and AT1) for a given period.

Abbreviations

CVA	Credit valuation adjustment
ERU	Economic resilience uncertainty
HMT	Her Majesty's Treasury
SST	Solvency Stress Test

Officers and professional advisers

Non-Executive Directors

Chairman	David Bennett[(1) (4)]
Senior Independent Non-Executive Director	Tim Wade[(1) (2) (3) (4)]
Independent Non-Executive Directors	Paul Coby[(1) (2) (3) (4)] Geeta Gopalan[(1) (2) (3) (4)] Elena Novokreshchenova[(3) (4)] Darren Pope[(1) (2) (3) (4)]
Non-Executive Director	Amy Stirling[(4)]
Executive Directors	David Duffy Clifford Abrahams
Company Secretary	Lorna McMillan
Group General Counsel	James Peirson
Independent auditors	Ernst & Young LLP 25 Churchill Place Canary Wharf London E14 5EY

(1) Member of the Remuneration Committee
(2) Member of the Audit Committee
(3) Member of the Risk Committee
(4) Member of the Governance and Nomination Committee

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