ROYAL BANK OF SCOTLAND GROUP PLC
Form 6-K
August 10, 2012

FORM 6-K

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Report of Foreign Private Issuer

Pursuant to Rule 13a-16 or 15d-16 of
the Securities Exchange Act of 1934

For August 10, 2012

Commission File Number: 001-10306

The Royal Bank of Scotland Group plc

RBS, Gogarburn, PO Box 1000
Edinburgh EH12 1HQ

(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.
Form 20-F __X__ Form 40-F _____

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1):

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7):

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes _____ No __X_–_

If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-_____

This report on Form 6-K shall be deemed incorporated by reference into the company's Registration Statement on Form F-3 (File Nos. 333-162219 and 333-162219-01) and to be a part thereof from the date which it was filed, to the extent not superseded by documents or reports subsequently filed or furnished.

Presentation of information

In this document and unless specified otherwise, the term ‘company’ or ‘RBSG’ means The Royal Bank of Scotland Group plc, ‘RBS’, ‘RBS Group’ or the ‘Group’ means the company and its subsidiaries, ‘the Royal Bank’ means The Royal Bank of Scotland plc and ‘NatWest’ means National Westminster Bank Plc.

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

Certain information in this report is presented separately for domestic and foreign activities. Domestic activities primarily consist of the UK domestic transactions of the Group. Foreign activities comprise the Group's transactions conducted through those offices in the UK specifically organised to service international banking transactions and transactions conducted through offices outside the UK.

The geographic analysis in the Business Review, including the average balance sheet and interest rates, changes in net interest income and average interest rates, yields, spreads and margins in this report have been compiled on the basis of location of office - UK and overseas. Management believes that this presentation provides more useful information on the Group's yields, spreads and margins of the Group's activities than would be provided by presentation on the basis of the domestic and foreign activities analysis used elsewhere in this report as it more closely reflects the basis on which the Group is managed. ‘UK’ in this context includes domestic transactions and transactions conducted through the offices in the UK which service international banking transactions.

The results, assets and liabilities of individual business units are classified as trading or non-trading based on their predominant activity. Although this method may result in some non-trading activity being classified as trading, and vice versa, the Group believes that any resulting misclassification is not material.

International Financial Reporting Standards
As required by the Companies Act 2006 and Article 4 of the European Union IAS Regulation, the consolidated financial statements of the Group are prepared in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board (IASB) and interpretations issued by the IFRS Interpretations Committee of the IASB as adopted by the European Union (together ‘IFRS’). They also comply with IFRS as issued by the IASB.

RBS Holdings N.V. (formerly ABN AMRO Holding N.V.)
In 2007, RFS Holdings B.V., which was jointly owned by the Group, the Dutch State (successor to Fortis) and Santander (together, the “Consortium Members”) completed the acquisition of ABN AMRO Holding N.V.

On 6 February 2010, the businesses of ABN AMRO Holding N.V. acquired by the Dutch State were legally demerged to a newly established company, ABN AMRO Bank N.V., which on 1 April 2010 was transferred to ABN AMRO Group N.V., itself owned by the Dutch State. Following legal separation, RBS Holdings N.V. (formerly ABN AMRO Holding N.V.) has one operating subsidiary, The Royal Bank of Scotland N.V. (“RBS N.V.”), a fully operational bank within the Group. RBS N.V. is independently rated and regulated by the Dutch Central Bank. Certain assets within RBS N.V. continue to be shared by the Consortium Members.

On 19 April 2011, the Group announced the proposed transfers of a substantial part of the business activities of RBS N.V. to the Royal Bank. Subject to, among other matters, regulatory and other approvals and procedures, it is expected that the transfers will be implemented on a phased basis over a period ending 31 December 2013. A large part of the transfers is expected to have taken place by the end of 2012.

On 17 October 2011, the Group completed the transfer of a substantial part of the UK activities of RBS N.V. to the Royal Bank pursuant to Part VII of the UK Financial Services and Markets Act 2000.

Approximately 98% of the issued share capital of RFS Holdings B.V. is held by the Group.

Non-GAAP financial information

The directors manage the Group's performance by class of business, before certain reconciling items, as is presented in the segmental analysis on pages 371 to 375 (the "managed basis"). Discussion of the Group's performance focuses on the managed basis as the Group believes that such measures allow a more meaningful analysis of the Group's financial condition and the results of its operations. These measures are non-GAAP financial measures. A body of generally accepted accounting principles such as IFRS is commonly referred to as 'GAAP'. A non-GAAP financial measure is defined as one that measures historical or future financial performance, financial position or cash flows but which excludes or includes amounts that would not be so adjusted in the most comparable GAAP measure. Reconciliations of these non-GAAP measures are presented throughout this document or in the segmental analysis on pages 371 to 375. These non-GAAP financial measures are not a substitute for GAAP measures. Furthermore, RBS has divided its operations into "Core" and "Non- Core". Certain measures disclosed in this document for Core operations and used by RBS management are non-GAAP financial measures as they represent a combination of all reportable segments with the exception of Non-Core. In addition, RBS has further divided parts of the Core business into "Retail & Commercial" consisting of the UK Retail, UK Corporate, Wealth, International Banking, Ulster Bank and US Retail & Commercial divisions. This is a non-GAAP financial measure. Lastly, the Basel III net stable funding ratio (see page 81) represents a non-GAAP financial measure given it is a metric that is not yet required to be disclosed by a government, governmental authority or self-regulatory organisation.

Glossary

A glossary of terms is provided on pages 440 to 447.

Forward-looking statements

Certain sections in this document contain ‘forward-looking statements’ as that term is defined in the United States Private Securities Litigation Reform Act of 1995, such as statements that include the words ‘expect’, ‘estimate’, ‘project’, ‘anticipate’, ‘believes’, ‘should’, ‘intend’, ‘plan’, ‘could’, ‘probability’, ‘risk’, ‘Value-at-Risk (VaR)’, ‘target’, ‘goal’, ‘objectiv ‘endeavour’, ‘outlook’, ‘optimistic’, ‘prospects’ and similar expressions or variations on such expressions.

In particular, this document includes forward-looking statements relating, but not limited to: the Group’s restructuring plans, divestments, capitalisation, portfolios, net interest margin, capital ratios, liquidity, risk weighted assets (RWAs), return on equity (ROE), profitability, cost:income ratios, leverage and loan:deposit ratios, funding and risk profile; certain ring-fencing proposals; sustainability targets; the Group’s future financial performance; the level and extent of future impairments and write-downs, including sovereign debt impairments; the protection provided by the Asset Protection Scheme (APS); and the Group’s potential exposures to various types of market risks, such as interest rate risk, foreign exchange rate risk and commodity and equity price risk. These statements are based on current plans, estimates and projections, and are subject to inherent risks, uncertainties and other factors which could cause actual results to differ materially from the future results expressed or implied by such forward-looking statements. For example, certain market risk disclosures are dependent on choices about key model characteristics and assumptions and are subject to various limitations. By their nature, certain of the market risk disclosures are only estimates and, as a result, actual future gains and losses could differ materially from those that have been estimated.

Other factors that could cause actual results to differ materially from those estimated by the forward-looking statements contained in this document include, but are not limited to: the global economic and financial market conditions and other geopolitical risks, and their impact on the financial industry in general and on the Group in particular; the ability to access sufficient sources of liquidity and funding; the recommendations made by the Independent Commission on Banking (ICB) and their potential implications; the ability to implement strategic plans on a timely basis, or at all, including the disposal of certain Non-Core assets and assets and businesses required as part of the State Aid restructuring plan; organisational restructuring, including any adverse consequences of a failure to transfer, or delay in transferring, certain business assets and liabilities from RBS N.V. to RBS; the full nationalisation of the Group or other resolution procedures under the Banking Act 2009; deteriorations in borrower and counterparty credit quality; costs or exposures borne by the Group arising out of the origination or sale of mortgages or mortgage-backed securities in the United States; the extent of future write-downs and impairment charges caused by depressed asset valuations; the value and effectiveness of any credit protection purchased by the Group; unanticipated turbulence in interest rates, yield curves, foreign currency exchange rates, credit spreads, bond prices, commodity prices, equity prices and basis, volatility and correlation risks; changes in the credit ratings of the Group; ineffective management of capital or changes to capital adequacy or liquidity requirements; litigation and regulatory investigations; changes to the valuation of financial instruments recorded at fair value; competition and consolidation in the banking sector; the ability of the Group to attract or retain senior management or other key employees; regulatory or legal changes (including those requiring any restructuring of the Group’s operations) in the United Kingdom, the United States and other countries in which the Group operates or a change in United Kingdom Government policy; changes to regulatory requirements relating to capital and liquidity; changes to the monetary and interest rate policies of central banks and other governmental and regulatory bodies; changes in UK and foreign laws, regulations, accounting standards and taxes, including changes in regulatory capital regulations and liquidity requirements; impairments of goodwill; pension fund shortfalls; general operational risks; HM Treasury exercising influence over the operations of the Group; insurance claims; reputational risk; the ability to access the contingent capital arrangements with HM Treasury; the participation of the Group in the APS and the effect of the APS on the Group’s financial and capital position; the conversion of the B Shares in accordance with their terms; limitations on, or additional requirements imposed on, the Group’s activities as a result of HM Treasury’s investment in the Group; and the success of the Group in managing the risks involved in the foregoing.

The forward-looking statements contained in this document speak only as of the date of this announcement, and the Group does not undertake to update any forward-looking statement to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

The information, statements and opinions contained in this document do not constitute a public offer under any applicable legislation or an offer to sell or 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.

Explanatory note

Divisional reorganisation and Group reporting changes

The company is filing this Form 6-K to restate certain segmental disclosures that were made in the company's annual report on Form 20-F for the year ended 31 December 2011, filed with the Securities and Exchange Commission on 27 March 2012 (the "2011 Form 20-F") to reflect the Group's new organisational structure, the revised allocation of Group Treasury costs, and the revised divisional return on equity ratios, and to combine movements in the fair value of own derivative liabilities, previously incorporated within Markets' operating performance, with changes in the fair value of own debt, in a single measure Own Credit Adjustments.

The Group presented segmental disclosures that reflect the new organisational structure in its interim results for the half year ended 30 June 2012, which were filed with the Securities and Exchange Commission on a separate Form 6-K on 8 August 2012. To facilitate comparison with these interim results, the segmental disclosures in the 2011 Form 20-F have been restated in this Form 6-K.

Consolidating financial information

As a result of filing this Form 6-K, the Group has presented a statement of comprehensive income within the consolidating financial information note, for all applicable periods.

Share consolidation

Following approval at the Annual General Meeting of the Company held on 30 May 2012, an ordinary share sub-division and one-for-ten consolidation took effect on 6 June 2012. This resulted in the 59,554,319,127 ordinary shares of 25p each, in issue at the record date of 1 June 2012, being sub-divided and consolidated into 5,955,431,912 ordinary shares of £1 each. Consequently, the Group has also restated in this Form 6-K certain disclosures relating to or impacted by numbers of ordinary shares or share prices.

The Group presented disclosures that reflect the changes discussed above in its interim results, which were filed with the Securities and Exchange Commission on a separate Form 6-K on 8 August 2012. To facilitate comparison with these interim results, the disclosures included in the 2011 Form 20-F have been restated in this Form 6-K.

Accordingly, the following pages that correspond to the 2011 Form 20-F have been restated to reflect the amendments identified above.

Item 3 - Key information	
Pages 8-9	(Business review)
Pages 408-409	(Risk factors)
Item 4 - Information on the Company	
Pages 4-5	(Business review - Description of business)
Page 6	(Business review - Competition)
Page 102	(Risk and balance sheet management - Divisional analysis of credit risk assets)
Page 104	(Risk and balance sheet management - AQ credit risk assets)
Page 108	(Risk and balance sheet management - Commercial real estate)
Page 110	(Risk and balance sheet management - Commercial real estate - Maturity profile of portfolio)
Page 111	

Page 150	(Risk and balance sheet management - REIL by division)
Pages 162-163	(Risk and balance sheet management - Movement in loan impairment provisions)
Pages 171, 174	(Risk and balance sheet management - Country risk - key points)
Pages 188-190	(Risk and balance sheet management - Market risk)
Page 191	(Risk and balance sheet management - Trading VaR)
Page 194	(Risk and balance sheet management - Insurance risk)
Pages 205, 207	(Risk and balance sheet management - Asset Protection Scheme)

This Form 6-K includes items 3, 4, 5, 6, 7, 8, 9, 10, 11 and 18 from the 2011 Form 20-F in their entirety and also retains the page numbering in respect of items 3, 4, 5, 6, 7, 8, 9, 10, 11 and 18 for ease of reference.

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Description of business

Introduction

The Royal Bank of Scotland Group plc is the holding company of a large global banking and financial services group. Headquartered in Edinburgh, the Group operates in the United Kingdom, the United States and internationally through its principal subsidiaries, the Royal Bank and NatWest. Both the Royal Bank and NatWest are major UK clearing banks. In the United States, the Group's subsidiary Citizens is a large commercial banking organisation. Globally, the Group has a diversified customer base and provides a wide range of products and services to personal, commercial and large corporate and institutional customers.

Following the placing and open offers in December 2008 and in April 2009, HM Treasury owned approximately 70.3% of the enlarged ordinary share capital of the company. In December 2009, the company issued a further £25.5 billion of new capital to HM Treasury. This new capital took the form of B shares, which do not generally carry voting rights at general meetings of ordinary shareholders but are convertible into ordinary shares and qualify as Core Tier 1 capital. Following the issuance of the B shares, HM Treasury's holding of ordinary shares of the company remained at 70.3% although its economic interest rose to 84.4%.

At 31 December 2011, HM Treasury’s holding in the company’s ordinary shares was 66.9% and its economic interest was 82.2%.

The Group had total assets of £1,506.9 billion and owners' equity of £74.8 billion at 31 December 2011. The Group's risk asset ratios at 31 December 2011, were a Total capital ratio of 13.8%, a Core Tier 1 capital ratio of 10.6% and a Tier 1 capital ratio of 13.0%.

Organisational change

In January 2012, the Group announced changes to its wholesale banking operations in light of a changed market and regulatory environment. The changes saw the reorganisation of the Group’s wholesale businesses into ‘Markets’ and ‘International Banking’ and the exit and downsizing of selected activities. The changes ensure the wholesale businesses continue to deliver against the Group’s strategy.

The changes include an exit from cash equities, corporate brokering, equity capital markets and mergers and acquisitions businesses. Significant reductions in balance sheet, funding requirements and cost base in the remaining wholesale businesses will be implemented.

GBM and GTS divisions have been reorganised as follows:

- The ‘Markets’ business maintains its focus on fixed income, with strong positions in debt capital raising, securitisation, risk management, foreign exchange and rates. It will serve the corporate and institutional clients of all Group businesses.

- GBM's corporate banking business has been combined with the international businesses of the GTS arm into a new ‘International Banking’ unit and provides clients with a 'one-stop shop' access to the Group’s debt financing, risk management and payments services. This international corporate business will be self-funded through its stable corporate deposit base.

- The domestic small and mid-size corporates previously served within GTS is now managed within RBS's domestic corporate banking businesses in the UK, Ireland (Ulster Bank) and the US (US Retail & Commercial).

Our wholesale business retains its international footprint ensuring that it can serve our customers' needs globally. We believe, that despite current challenges to the sector, wholesale banking services can play a central role in supporting cross border trade and capital flows, financing requirements and risk management and we remain committed to this business.

Organisational structure and business overview
The Group's activities are organised on a divisional basis as follows:

UK Retail offers a comprehensive range of banking products and related financial services to the personal market. It serves customers through a number of channels including: the RBS and NatWest network of branches and ATMs in the United Kingdom, telephony, online and mobile. UK Retail remains committed to delivering 'Helpful and Sustainable' banking and to the commitments set out in its Customer Charter - the results of which are externally assessed and published every six months.

UK Corporate is a leading provider of banking, finance and risk management services to the corporate and SME sector in the United Kingdom. It offers a full range of banking products and related financial services through a nationwide network of relationship managers, and also through telephone and internet channels. The product range includes asset finance through the Lombard brand.

Wealth provides private banking and investment services in the UK through Coutts & Co and Adam & Company, offshore banking through RBS International, NatWest Offshore and Isle of Man Bank, and international private banking through Coutts & Co Ltd.

International Banking serves the world's largest companies with a leading client proposition focused on financing, transaction services and risk management. International Banking serves as the delivery channel for Markets products to corporate clients and serves international subsidiaries of both International Banking and clients from UK Corporate, Ulster Bank and US Retail & Commercial through its international network.

Ulster Bank is a leading retail and commercial bank in Northern Ireland and the Republic of Ireland. It provides a comprehensive range of financial services through both its Retail Banking division, which has a network of branches and operates in the personal and bancassurance sectors, and its Corporate Banking division, which provides services to business customers, corporate customers and institutional markets.

Business review continued

US Retail & Commercial provides financial services primarily through the Citizens and Charter One brands. US Retail & Commercial is engaged in retail and corporate banking activities through its branch network in 12 states in the United States and through non-branch offices in other states.

The divisions discussed above are collectively referred to as Retail & Commercial.

Markets is a leading origination, sales and trading business across debt finance, fixed income, currencies, investor products and equity derivatives. The division offers a unified service to the Group’s corporate and institutional clients. The Markets’ sales and research teams build strong ongoing client partnerships, provide market perspective and access, and work with the division’s trading and structuring teams to meet the client’s objectives across financing, risk management, investment, securitisation and liquidity.

Direct Line Group provides a wide range of general insurance products to consumers through a number of well known brands including; Direct Line, Churchill and Privilege. It also provides insurance services via a number of partner brands. In the commercial sector, its NIG and Direct Line for Business operations provide insurance products for businesses via brokers or direct respectively. Through its international division, Direct Line Group sells general insurance, mainly motor, in Germany and Italy. In addition to insurance services, Direct Line Group continues to provide support and reassurance to millions of UK motorists through its Green Flag breakdown recovery service and stolen vehicle recovery and telematics business (Tracker). On 15 February 2012, a new corporate brand, Direct Line Group, was announced.

To comply with EC State Aid requirements, the Group has agreed to dispose of Direct Line Group. It continues to be reported as a separate operating segment rather than within the Non-Core division as its business is distinct from the activities of the Non-Core division.

Central Functions comprises Group and corporate functions, such as treasury, funding and finance, risk management, legal, communications and human resources. The Centre manages the Group's capital resources and Group-wide regulatory projects and provides services to the operating divisions.

Non-Core division manages separately assets that the Group intends to run off or dispose of. The division contains a range of businesses and asset portfolios primarily from the legacy GBM businesses, higher risk profile asset portfolios including excess risk concentrations, and other illiquid portfolios. It also includes a number of other portfolios and businesses including regional markets businesses that the Group has concluded are no longer strategic.

Business Services supports the customer-facing businesses and provides operational technology, customer support in telephony, account management, lending and money transmission, global purchasing, property and other services. Business Services drives efficiencies and supports income growth across multiple brands and channels by using a single, scalable platform and common processes wherever possible. It also leverages the Group's purchasing power and is the Group's centre of excellence for managing large-scale and complex change. For reporting purposes, Business Services costs are allocated to the divisions above. It is not deemed a reportable segment.

Business divestments
To comply with EC State Aid requirements the Group agreed a series of restructuring measures to be implemented over a four year period from December 2009. This supplements the measures in the Strategic Plan previously announced by the Group. These include divesting Direct Line Group, 80.01% of GMS (completed in 2010) and substantially all of RBS Sempra Commodities JV business (largely completed in 2010), as well as divesting the RBS branch-based business in England and Wales and the NatWest branches in Scotland, along with the Direct SME customers across the UK.

Recent developments

Share consolidation
Following approval at the Group's Annual General Meeting on 30 May 2012, the sub-division and consolidation of the Group's ordinary shares on a one-for-ten basis took effect on 6 June 2012.There was a corresponding change in the Group's share price to reflect this.

The Board believes that the consolidation will result in a more appropriate share price for a company of the Group's size in the UK market. It may also help reduce volatility, thereby enabling a more consistent valuation of the Group.

Liability management: Exchange offer
On 28 February 2012, The Royal Bank of Scotland plc announced an invitation to offer to exchange certain Canadian Dollar, Australian Dollar, US Dollar, Euro and Swiss Franc denominated subordinated notes for new Canadian Dollar, Australian Dollar, US Dollar, Euro and Swiss Franc denominated subordinated notes, due 2022 and callable 2017. The new notes, other than the Australian Dollar denominated new notes, were issued on 16 March 2012, and the Australian Dollar denominated new notes were issued on 19 March 2012, in each case under the £90,000,000,000 Euro Medium Term Note Programme of The Royal Bank of Scotland plc and The Royal Bank of Scotland Group plc.

Business review continued

National Loan Guarantee Scheme
On 20 March 2012, RBS agreed to participate in the National Loan Guarantee Scheme (the Scheme), pursuant to which The Commissioners of Her Majesty's Treasury (HM Treasury) have agreed to unconditionally and irrevocably guarantee the due payment of all sums due and payable by RBS under any senior unsecured notes issued by RBS in accordance with the terms of the Scheme in respect of which HM Treasury issues a Guarantee Certificate (as defined in a deed of guarantee dated 20 March 2012 (the "Deed of Guarantee")). The Guarantor's obligations in that respect, are contained in the Deed of Guarantee, the form of which is available at www.dmo.gov.uk.

2012 Budget
In the Budget statement on 21 March 2012, the Chancellor of the Exchequer announced a further reduction of 1% in the rate of corporation tax such that the rate will fall by 2% from 26% to 24% in April 2012, to 23% in April 2013 and to 22% in April 2014. It was also announced in the Budget statement that the full rate of the bank levy will increase to 0.105 per cent. from 1 January 2013.

Competition
The Group faces strong competition in all the markets it serves. Banks' balance sheets have strengthened whilst loan demand has been subdued as many customers have sought to delever and the UK economy has remained weak. Competition for retail deposits remains intense as institutions continue to target strong and diverse funding platforms for their balance sheets.

Competition for corporate and institutional customers in the UK is from UK banks and from large foreign financial institutions who are also active and offer combined investment and commercial banking capabilities. In asset finance, the Group competes with banks and specialist asset finance providers, both captive and non-captive. In European and Asian corporate and institutional banking markets the Group competes with the large domestic banks active in these markets and with the major international banks.

In the small business banking market, the Group competes with other UK clearing banks, specialist finance providers and building societies.

In the personal banking segment, the Group competes with UK clearing banks and building societies, major retailers and life assurance companies. In the mortgage market, the Group competes with UK clearing banks and building societies. The ambitions of non-traditional players in the UK market remain strong, with new entrants active and potentially seeking to build their platforms by acquiring businesses made available through restructuring of incumbents. The Group distributes life assurance products to banking customers in competition with independent advisors and life assurance companies.

In the UK credit card market large retailers and specialist card issuers are active in addition to the UK banks. In addition to physical distribution channels, providers compete through direct marketing activity and the internet.

In Wealth Management, The Royal Bank of Scotland International competes with other UK and international banks to offer offshore banking services. Coutts and Adam & Company compete as private banks with UK clearing and private banks, and with international private banks. Competition in wealth management remains strong as banks maintain their focus on competing for affluent and high net worth customers.

Direct Line Group competes in personal lines insurance and, to a more limited extent, in commercial insurance. There is strong competition from a range of insurance companies which now operate telephone and internet direct sales businesses. Competition in the UK motor market remains intense, and price comparison internet sites now play a major role in the marketplace. These sites are now extending their scope to home insurance and other lines. Direct

Line Group also competes with local insurance companies in the direct motor insurance markets in Italy and Germany.

In Ireland, Ulster Bank competes in retail and commercial banking with the major Irish banks and building societies, and with other UK and international banks and building societies active in the market. The challenging conditions in the Irish economy persist and many of the domestic Irish banks have required State support and are engaged in significant restructuring actions.

In the United States, Citizens competes in the New England, Mid-Atlantic and Mid-West retail and mid-corporate banking markets with local and regional banks and other financial institutions. The Group also competes in the US in large corporate lending and specialised finance markets, and in fixed-income trading and sales. Competition is principally with the large US commercial and investment banks and international banks active in the US. The economic recovery in the US is proving weaker than expected and loan demand is weak in Citizens' markets.

Risk factors

Set out below is a summary of certain risks which could adversely affect the Group; it should be read in conjunction with the Risk and balance sheet management section of the Business review (pages 58 to 207). This summary should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties. A fuller description of these and other risk factors is included on pages 405 to 418.

- The Group's businesses, earnings and financial condition have been and will continue to be affected by geopolitical conditions, the global economy, the instability in the global financial markets and increased competition. Together with a perceived increased risk of default on the sovereign debt of certain European countries and unprecedented stresses on the financial system within the eurozone, these factors have resulted in significant changes in market conditions including interest rates, foreign exchange rates, credit spreads, and other market factors and consequent changes in asset valuations.

- The Group's ability to meet its obligations' including its funding commitments, depends on the Group's ability to access sources of liquidity and funding. The inability to access liquidity and funding due to market conditions or otherwise could adversely affect the Group's financial condition. Furthermore, the Group's borrowing costs and its access to the debt capital markets and other sources of liquidity depend significantly on its and the UK Government's credit ratings.

- The Independent Commission on Banking has published its final report on competition and possible structural reforms in the UK banking industry. The Government has indicated that it supports and intends to implement the recommendations substantially as proposed which could have a material adverse effect on the Group.

- The Group's ability to implement its Strategic Plan depends on the success of its efforts to refocus on its core strengths and its balance sheet reduction programme. As part of the Group's Strategic Plan and implementation of the State Aid restructuring plan agreed with the European Commission and HM Treasury, the Group is undertaking an extensive restructuring which may adversely affect the Group's business, results of operations and financial condition and give rise to increased operational risk and may impair the Group's ability to raise new Tier 1 capital due to restrictions on its ability to make discretionary dividend or coupon payments on certain securities.

- The occurrence of a delay in the implementation of (or any failure to implement) the approved proposed transfers of a substantial part of the business activities of RBS N.V. to the Royal Bank may have a material adverse effect on the Group.

- The Group or any of its UK bank subsidiaries may face the risk of full nationalisation or other resolution procedures and various actions could be taken by or on behalf of the UK Government, including actions in relation to any securities issued, new or existing contractual arrangements and transfers of part or all of the Group's businesses.

- The actual or perceived failure or worsening credit of the Group's counterparties or borrowers and depressed asset valuations resulting from poor market conditions have adversely affected and could continue to adversely affect the Group.

- The value of certain financial instruments recorded at fair value is determined using financial models incorporating assumptions, judgements and estimates that may change over time or may ultimately not turn out to be accurate.

- The Group's insurance businesses are subject to inherent risks involving claims on insured events.

- The Group's business performance, financial condition and capital and liquidity ratios could be adversely affected if its capital is not managed effectively or as a result of changes to capital adequacy and liquidity requirements, including those arising out of Basel III implementation (globally or by European or UK authorities), or if the Group is unable to issue Contingent B Shares to HM Treasury under certain circumstances.

- The Group could fail to attract or retain senior management, which may include members of the Group Board, or other key employees, and it may suffer if it does not maintain good employee relations.

- Any significant developments in regulatory or tax legislation could have an effect on how the Group conducts its business and on its results of operations and financial condition, and the recoverability of certain deferred tax assets recognised by the Group is subject to uncertainty.

- The Group is subject to substantial regulation and oversight, and any significant regulatory or legal developments could have an adverse effect on how the Group conducts its business and on its results of operations and financial condition. In addition, the Group is, and may be, subject to litigation and regulatory investigations that may impact its business, results of operations and financial condition.

- Operational and reputational risks are inherent in the Group's operations.

- The Group may be required to make contributions to its pension schemes and government compensation schemes, either of which may have an adverse impact on the Group's results of operations, cash flow and financial condition.

- As a result of the UK Government's majority shareholding in the Group it can, and in the future may decide to, exercise a significant degree of influence over the Group including on dividend policy, modifying or cancelling contracts or limiting the Group's operations. The offer or sale by the UK Government of all or a portion of its shareholding in the company could affect the market price of the equity shares and other securities and acquisitions of ordinary shares by the UK Government (including through conversions of other securities or further purchases of shares) may result in the delisting of the Group from the Official List.

Business review continued

Key financials

for the year ended 31 December	2011 £m	2010 £m	2009 £m
Total income	28,937	31,868	33,026
Operating loss before tax	(766)	(399)	(2,647)
Loss attributable to ordinary and B shareholders	(1,997)	(1,125)	(3,607)
Cost:income ratio	62%	57%	52%
Basic loss per ordinary and B share from continuing operations (pence) (1)	(18.5p)	(4.5p)	(63.1p)

at 31 December		2011 £m	2010 £m	2009 £m
Funded balance sheet (2)		977,249	1,026,499	1,255,032
Total assets		1,506,867	1,453,576	1,696,486
Loans and advances to customers		515,606	555,260	728,393
Deposits		611,759	609,483	756,346
Owners' equity		74,819	75,132	77,736
Risk asset ratios	- Core Tier 1	10.6%	10.7%	11.0%
	- Tier 1	13.0%	12.9%	14.1%
	- Total	13.8%	14.0%	16.1%

Notes:

(1) Adjusted for the sub-division and one-for-ten consolidation of ordinary shares, which took effect in June 2012.

(2) Funded balance sheet represents total assets less derivatives.

Overview of results

The results of RFS Holdings B.V., the entity that acquired ABN AMRO, are fully consolidated in the Group’s financial statements. The interests of the State of the Netherlands and Santander in RFS Holdings are included in non-controlling interests. Legal separation of ABN AMRO Bank N.V. took place on 1 April 2010. As a result, RBS presents the interests of the Consortium Members in ABN AMRO as discontinued operations.

Summary consolidated income statement
for the year ended 31 December 2011

	2011 £m	2010 £m	2009 £m
Net interest income	12,679	14,209	13,388
Fees and commissions receivable	6,384	8,193	8,738
Fees and commissions payable	(1,460)	(2,211)	(2,790)
Other non-interest income	7,078	6,549	8,424
Insurance net premium income	4,256	5,128	5,266
Non-interest income	16,258	17,659	19,638
Total income	28,937	31,868	33,026
Operating expenses	(18,026)	(18,228)	(17,417)
Profit before insurance net claims and impairment losses	10,911	13,640	15,609
Insurance net claims	(2,968)	(4,783)	(4,357)
Impairment losses	(8,709)	(9,256)	(13,899)
Operating loss before tax	(766)	(399)	(2,647)
Tax (charge)/credit	(1,250)	(634)	429
Loss from continuing operations	(2,016)	(1,033)	(2,218)
Profit/(loss) from discontinued operations, net of tax	47	(633)	(105)
Loss for the year	(1,969)	(1,666)	(2,323)
Non-controlling interests	(28)	665	(349)
Other owners' dividends	—	(124)	(935)
Loss attributable to ordinary and B shareholders	(1,997)	(1,125)	(3,607)
Basic loss per ordinary and B share from continuing operations (1)	(18.5p)	(4.5p)	(63.1p)

Note:
(1) Adjusted for the sub-division and one-for-ten consolidation of ordinary shares, which took effect in June 2012.

Results summary
2011 compared with 2010
Operating profit
Group operating loss before tax for the year was £766 million compared with £399 million in 2010. Group operating profit on a managed basis was £1,824 million compared with £1,845 million in 2010. Adjusting for the impact of the disposal of GMS in 2010, which recorded an operating profit of £207 million, Group operating profit on a managed basis was up 11%. The improvement was driven by a strong Retail & Commercial (R&C) operating performance and the return to profit of Direct Line Group. Ulster Bank and Markets faced more difficult conditions, leaving total Core operating profit on a managed basis at £6,045 million. Non-Core operating loss in 2011 was 26% lower compared with 2010, despite the acceleration of disposals in the second half of the year.

Total income
Total income fell by 9% to £28,937 million, primarily reflecting lower net interest income, lower trading income in Markets and Non-Core and a fall in insurance net premium income.

Net interest income
Group net interest income fell 11% to £12,679 million largely driven by the run-off of balances and exit of higher margin and higher risk segments in Non-Core. Group NIM was 14 basis points lower, reflecting the cost of carrying a higher liquidity portfolio and by the impact of non-performing assets in the Non-Core division. However, R&C NIM

was up 6 basis points, with strengthening asset margins in the first half of the year offsetting the impact of a competitive deposit market.

Non-interest income

Non-interest income decreased to £16,258 million from £17,659 million in 2010. This included movements in the fair value of the Asset Protection Scheme resulting in a £906 million charge (2010 - £1,550 million), gain on redemption of own debt of £255 million (2010 - £553 million) and a gain in own credit adjustments of £1,914 million (2010 - £242 million gain). Excluding these items, non-interest income was down 19% primarily reflecting a reduction in income from trading activities and lower net fees and commissions.

Operating expenses
Operating expenses decreased to £18,026 million (2010 - £18,228 million). Operating expenses on a managed basis fell to £15,478 million from £16,710 million in 2010.

This decrease was primarily driven by cost savings achieved as a result of the cost reduction programme and Non-Core run-off, largely reflecting the disposal of RBS Sempra and specific country exits. Staff costs fell 9%, driven by lower Markets and International Banking variable compensation as a result of its decrease in revenues, and in Non-Core, given the impact of a 32% reduction in headcount and continued business disposals and country exits.

The Group cost:income ratio was 62% in 2011 compared with 57% in 2010.

Net insurance claims
Bancassurance and general insurance claims, after reinsurance, reduced by 38% to £2,968 million.

General insurance claims were £1,730 million lower, mainly due to the non-repeat of bodily injury reserve strengthening in 2010, de-risking of the motor book, more benign weather in 2011 and claims in Non-Core decreasing as legacy policies ran-off.

Impairment losses
Impairment losses were £8,709 million compared with £9,256 million in 2010, with Core loan impairments falling by £260 million and Non-Core by £1,557 million, despite continuing challenges in Ulster Bank and corporate real estate portfolios, partially offset by an impairment of £1,099 million and interest rate hedge adjustments on impaired available-for-sale Greek government bonds of £169 million.

Risk elements in lending represented 8.6% of gross loans and advances to customers excluding reverse repos at 31 December 2011 (2010 - 7.3%).

Provision coverage of risk elements in lending was 49% (2010 - 47%).

Tax
The tax charge was £1,250 million in 2011, compared with £634 million in 2010. The high tax charge in the year reflects profits in high tax regimes (principally US) and losses in low tax regimes (principally Ireland), losses in overseas subsidiaries for which a deferred tax asset has not been recognised (principally Ireland and the Netherlands) and the effect of the two reductions of 1% in the rate of UK corporation tax enacted in March 2011 and July 2011 on the net deferred tax balance.

Earnings
Basic loss per ordinary and B share from continuing operations increased from a loss of 4.5p to a loss of 18.5p.

Business review continued

Results summary continued
2010 compared with 2009

Operating loss
Operating loss before tax for the year was £399 million compared with a loss of £2,647 million in 2009. The improvement in performance is primarily driven by stronger Core Retail & Commercial operating profits offsetting more normal results from Markets, coupled with lower impairments in the Non-Core division.

After tax, non-controlling interests and preference share and other dividends, the loss attributable to ordinary and B shareholders was £1,125 million, compared with an attributable loss of £3,607 million in 2009.

Total income
Total income decreased 4% to £31,868 million in 2010 reflecting the return to more normal levels in Markets compared with the favourable market conditions seen in 2009. This was offset by good growth in Core Retail & Commercial and the improvement in Non-Core.

Net interest income
Net interest income increased by 6% to £14,209 million, reflecting improvements in net interest margin which more than offset lower interest-earning assets and interest-bearing liabilities. Group net interest margin increased from 1.83% to 2.06% largely reflecting expanding asset margins in UK Retail and UK Corporate divisions as well as in US Retail & Commercial. The run-off of low-yielding Non-Core assets also contributed to this increase. The Group net interest margin was also affected by increased funding costs.

Non-interest income
Non-interest income decreased to £17,659 million from £19,638 million in 2009. This included movements in the fair value of the Asset Protection Scheme - credit default swap resulting in a £1,550 million charge and gain on redemption of own debt of £553 million (2009 - £3,790 million). Excluding these items, non-interest income was up 18% primarily reflecting an increase in income from trading activities.

Operating expenses
Operating expenses increased to £18,228 million (2009 - £17,417 million). The main driver of this 5% increase was the impact of a £2,148 million gains on pension curtailment in 2009. This was partially offset by gains on the recognition of benefits from the Group-wide efficiency programme. The programme continues to deliver material savings which have been funding investments to strengthen our Core franchises. Annualised savings are now just ahead of the £2.5 billion target for 2011 and are forecast to exceed £3 billion by 2013. Integration and restructuring costs were £1,032 million compared with £1,286 million in 2009. Write-down of goodwill and other intangible assets was £10 million compared with £363 million in 2009. Premises and equipment costs fell by 7% in the year largely driven by efficiency cost savings, significant one-off property impairments recognised in 2009 and country exits following Non-Core disposals.

Net insurance claims
Bancassurance and general insurance claims, after reinsurance, increased by 10% to £4,783 million.

Impairment losses
Impairment losses were £9,256 million compared with £13,899 million in 2009, with Core impairments falling by £898 million and Non-Core by £3,745 million. The decrease reflects an overall improvement in the economic environment. Impairments fell in all businesses, except Ulster Bank, which has faced an economic environment that remains challenging.

Risk elements in lending and potential problem loans represented 7.4% of gross loans and advances to customers excluding reverse repos at 31 December 2010 (2009 - 5.5%).

Provision coverage of risk elements in lending and potential problem loans was 46% (2009 - 45%).

Tax

The Group recorded a tax charge of £634 million in 2010, compared with a tax credit of £429 million in 2009.

Earnings

Basic loss per ordinary and B share from continuing operations improved from a loss of 63.1p to a loss of 4.5p.

Business review continued

Analysis of results
Net interest income

	2011	2010	2009
	£m	£m	£m
Interest receivable	21,410	22,776	33,836
Interest payable	(8,731)	(8,567)	(17,332)
Net interest income	12,679	14,209	16,504
	%		
Gross yield on interest-earning assets of the banking business (1)	3.24	3.30	3.76
Cost of interest-bearing liabilities of the banking business	(1.68)	(1.47)	(2.18)
Interest spread of the banking business (2)	1.56	1.83	1.58
Benefit from interest-free funds	0.36	0.23	0.25
Net interest margin of the banking business (3)	1.92	2.06	1.83
Yields, spreads and margins of the banking business	%	%	%
Gross yield (1)			
- Group	3.24	3.30	3.76
- UK	3.56	3.42	3.35
- Overseas	2.77	3.15	4.09
Interest spread (2)			
- Group	1.56	1.83	1.58
- UK	1.81	2.01	1.50
- Overseas	1.22	1.59	1.67
Net interest margin (3)			
- Group	1.92	2.06	1.83
- UK	2.07	2.22	1.81
- Overseas	1.70	1.84	1.85
The Royal Bank of Scotland plc base rate (average)	0.50	0.50	0.64
London inter-bank three month offered rates (average)			
- Sterling	0.87	0.70	1.21
- Eurodollar	0.33	0.34	0.69
- Euro	1.36	0.75	1.21

Notes:
(1) Gross yield is the interest earned on average interest-earning assets of the banking book.
(2) Interest spread is the difference between the gross yield and the interest rate paid on average interest-bearing liabilities of the banking business.
(3) Net interest margin is net interest income of the banking business as a percentage of average interest-earning assets of the banking business.
(4) The analysis into UK and overseas has been compiled on the basis of location of office.
(5) Interest receivable and interest payable on trading assets and liabilities are included in income from trading activities.

Average balance sheet and related interest

		2011			2010		
		Average Balance £m	Interest £m	Rate %	Average balance £m	Interest £m	Rate %
Assets							
Loans and advances to banks	- UK	31,994	293	0.92	22,714	222	0.98
	- Overseas	41,840	404	0.97	30,148	369	1.22
Loans and advances to		294,301	12,105	4.11			
customers	- UK				310,712	11,989	3.86
	- Overseas	171,979	5,864	3.41	195,858	6,900	3.52
Debt securities	- UK	62,231	1,449	2.33	66,765	1,459	2.19
	- Overseas	58,773	1,295	2.20	63,334	1,837	2.90
Interest-earning assets	- UK	388,526	13,847	3.56	400,191	13,670	3.42
	- Overseas	272,592	7,563	2.77	289,340	9,106	3.15
Total interest-earning assets	- banking business	661,118	21,410	3.24	689,531	22,776	3.30
	- trading business	278,975			276,330		
Interest-earning assets		940,093			965,861		
Non-interest-earning assets (5)		595,062			706,343		
Total assets		1,535,155			1,672,204		
Percentage of assets applicable to overseas operations		40.2%			44.0%		
Liabilities							
Deposits by banks	- UK	17,224	242	1.41	21,816	334	1.53
	- Overseas	47,371	740	1.56	59,799	999	1.67
Customer accounts: demand deposits	- UK	112,522	664	0.59	120,796	621	0.51
	- Overseas	43,177	483	1.12	39,127	607	1.55
Customer accounts: savings deposits	- UK	76,719	1,177	1.53	68,142	935	1.37
	- Overseas	25,257	130	0.51	25,587	213	0.83
Customer accounts: other time deposits	- UK	39,672	481	1.21	39,934	431	1.08
	- Overseas	33,971	594	1.75	43,996	914	2.08
Debt securities in issue	- UK	108,406	2,606	2.40	111,277	2,212	1.99
	- Overseas	42,769	765	1.79	72,175	1,065	1.48
Subordinated liabilities	- UK	16,874	470	2.79	19,442	398	2.05
	- Overseas	5,677	270	4.76	8,714	19	0.22
Internal funding of trading		(40,242)	149	(0.37)			
business	- UK				(41,451)	(140)	0.34
	- Overseas	(8,783)	(40)	0.46	(6,864)	(41)	0.60
Interest-bearing liabilities	- UK	331,175	5,789	1.75	339,956	4,791	1.41
	- Overseas	189,439	2,942	1.55	242,534	3,776	1.56
Total interest-bearing liabilities	- banking business	520,614	8,731	1.68	582,490	8,567	1.47
	- trading business (5)	307,564			293,993		
Interest-bearing liabilities		828,178			876,483		

Non-interest-bearing liabilities:			
Demand deposits	- UK	46,495	46,692
	- Overseas	19,909	23,994
Other liabilities (5)		565,534	648,129
Owners' equity		75,039	76,906
Total liabilities and owners' equity		1,535,155	1,672,204
Percentage of liabilities applicable to overseas operations		37.1%	41.7%

For notes relating to this table refer to page 12.

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Business review continued

Average balance sheet and related interest continued

		2009		
		Average balance £m	Interest £m	Rate %
Assets				
Loans and advances to banks	- UK	21,616	310	1.43
	- Overseas	32,367	613	1.89
Loans and advances to customers	- UK	333,230	11,940	3.58
	- Overseas	376,382	16,339	4.34
Debt securities	- UK	52,470	1,414	2.69
	- Overseas	84,822	3,220	3.80
Interest-earning assets	- UK	407,316	13,664	3.35
	- Overseas	493,571	20,172	4.09
Total interest-earning assets	- banking business	900,887	33,836	3.76
	- trading business (5)	291,092		
Interest-earning assets		1,191,979		
Non-interest-earning assets		831,501		
Total assets		2,023,480		
Percentage of assets applicable to overseas operations		47.4%		
Liabilities				
Deposits by banks	- UK	24,837	679	2.73
	- Overseas	104,396	2,362	2.26
Customer accounts: demand deposits	- UK	110,294	569	0.52
	- Overseas	82,177	1,330	1.62
Customer accounts: savings deposits	- UK	54,270	780	1.44
	- Overseas	83,388	2,114	2.54
Customer accounts: other time deposits	- UK	68,625	932	1.36
	- Overseas	71,315	2,255	3.16
Debt securities in issue	- UK	116,536	2,830	2.43
	- Overseas	117,428	2,500	2.13
Subordinated liabilities	- UK	26,053	834	3.20
	- Overseas	12,468	656	5.26
Internal funding of trading business	- UK	(60,284)	(317)	0.53
	- Overseas	(14,845)	(192)	1.29
Interest-bearing liabilities	- UK	340,331	6,307	1.85
	- Overseas	456,327	11,025	2.42
Total interest-bearing liabilities	- banking business	796,658	17,332	2.18
	- trading business (5)	331,380		
Interest-bearing liabilities		1,128,038		
Non-interest-bearing liabilities:				
Demand deposits	- UK	38,220		
	- Overseas	27,149		
Other liabilities (5)		772,770		
Owners' equity		57,303		

Total liabilities and owners' equity	2,023,480
Percentage of liabilities applicable to overseas operations	45.8%

For notes relating to this table refer to page 12.

Analysis of change in net interest income - volume and rate analysis
Volume and rate variances have been calculated based on movements in average balances over the period and changes in interest rates on average interest-earning assets and average interest-bearing liabilities. Changes due to a combination of volume and rate are allocated pro rata to volume and rate movements.

	2011 over 2010 Increase/(decrease) due to changes in:		
	Average volume £m	Average rate £m	Net change £m
Interest-earning assets			
Loans and advances to banks			
UK	86	(15)	71
Overseas	124	(89)	35
Loans and advances to customers			
UK	(652)	768	116
Overseas	(820)	(216)	(1,036)
Debt securities			
UK	(102)	92	(10)
Overseas	(125)	(417)	(542)
Total interest receivable of the banking business			
UK	(668)	845	177
Overseas	(821)	(722)	(1,543)
	(1,489)	123	(1,366)
Interest-bearing liabilities			
Deposits by banks			
UK	66	26	92
Overseas	197	62	259
Customer accounts: demand deposits			
UK	45	(88)	(43)
Overseas	(58)	182	124
Customer accounts: savings deposits			
UK	(125)	(117)	(242)
Overseas	3	80	83
Customer accounts: other time deposits			
UK	3	(53)	(50)
Overseas	189	131	320
Debt securities in issue			
UK	58	(452)	(394)
Overseas	494	(194)	300
Subordinated liabilities			
UK	58	(130)	(72)
Overseas	9	(260)	(251)
Internal funding of trading business			
UK	(4)	(285)	(289)
Overseas	10	(11)	(1)
Total interest payable of the banking business			
UK	101	(1,099)	(998)

Overseas	844	(10)	834
	945	(1,109)	(164)
Movement in net interest income			
UK	(567)	(254)	(821)
Overseas	23	(732)	(709)
	(544)	(986)	(1,530)

Business review continued

Analysis of change in net interest income - volume and rate analysis continued

	2010 over 2009 Increase/(decrease) due to changes in:		
	Average volume £m	Average rate £m	Net change £m
Interest-earning assets			
Loans and advances to banks			
UK	15	(103)	(88)
Overseas	(40)	(204)	(244)
Loans and advances to customers			
UK	(836)	885	49
Overseas	(6,776)	(2,663)	(9,439)
Debt securities			
UK	342	(297)	45
Overseas	(716)	(667)	(1,383)
Total interest receivable of the banking business			
UK	(479)	485	6
Overseas	(7,532)	(3,534)	(11,066)
	(8,011)	(3,049)	(11,060)
Interest-bearing liabilities			
Deposits by banks			
UK	75	270	345
Overseas	845	518	1,363
Customer accounts: demand deposits			
UK	(54)	2	(52)
Overseas	670	53	723
Customer accounts: savings deposits			
UK	(192)	37	(155)
Overseas	965	936	1,901
Customer accounts: other time deposits			
UK	336	165	501
Overseas	708	633	1,341
Debt securities in issue			
UK	123	495	618
Overseas	799	636	1,435
Subordinated liabilities			
UK	180	256	436
Overseas	152	485	637
Internal funding of trading business			
UK	(83)	(94)	(177)
Overseas	(75)	(76)	(151)
Total interest payable of the banking business			
UK	385	1,131	1,516
Overseas	4,064	3,185	7,249
	4,449	4,316	8,765

Movement in net interest income			
UK	(94)	1,616	1,522
Overseas	(3,468)	(349)	(3,817)
	(3,562)	1,267	(2,295)

Non-interest income

	2011	2010	2009
	£m	£m	£m
Fees and commissions receivable	6,384	8,193	8,738
Fees and commissions payable	(1,460)	(2,211)	(2,790)
Income from trading activities			
- managed basis	3,314	6,074 3,909	
- Asset Protection Scheme	(906)	(1,550)—	
- own credit adjustments	293	(7)(148)	
	2,701	4,517	3,761
Gain on redemption of own debt	255	553	3,790
Other operating income (excluding insurance net premium income)			
- managed basis	2,525	1,059	690
- strategic disposals	(24)	171	132
- own credit adjustments	1,621	249	51
	4,122	1,479	873
Insurance net premium income	4,256	5,128	5,266
Total non-interest income	16,258	17,659	19,638

2011 compared with 2010
Non-interest income decreased by £1,401 million in 2011 principally driven by lower trading income in Markets and Non-Core and a fall in insurance net premium income, partially offset by a higher gain on movements in own credit adjustments.

Volatile market conditions led to a reduction in Markets trading income, driven by the deterioration in global credit markets as sovereign difficulties in the eurozone grew.

Non-Core trading losses increased by £704 million, reflecting costs incurred as part of the division's focus on reducing capital trading assets, with activity including the restructuring of monoline exposures, which mitigated both significant immediate and future regulatory uplifts in risk-weighted assets.

A gain in own credit adjustments of £1,914 million was recorded as a result of Group credit spreads widening, partially offset by the 2011 charges. This compares with a smaller gain of £242 million in 2010.

Insurance net premium income fell by 17% largely driven by Direct Line Group's exit from certain business segments, along with reduced volumes driven by the de-risking of the motor book. Insurance net premium income in Non-Core also decreased as legacy policies ran-off.

2010 results included £482 million of income recorded for GMS prior to its disposal in November 2010.

2010 compared with 2009
Net fees and commissions increased by £34 million to £5,982 million primarily due to improved performance in Markets (£173 million), driven by higher portfolio management and origination income, and UK Corporate (£123 million), principally reflecting strong refinancing levels and increased operating lease activity. This increase was partially offset by reduced fees in UK Retail (£160 million) and Ulster Bank (£73 million) principally reflecting the restructuring of current account overdraft fees.

Income from trading activities, excluding fair value movements in the Asset Protection Scheme, rose substantially during the year by £2,306 million to £6,067 million. Trading revenues in Markets were lower than 2009, which saw unusually buoyant market conditions as rapidly falling interest rates generated significant revenue opportunities. This was more than offset by the improvement in Non-Core trading losses from £5,122 million for 2009 to £16 million for 2010 as underlying asset prices recovered and monoline spreads tightened. The unwinding of some banking book hedges also helped reduce trading losses.

The Asset Protection Scheme is accounted for as a credit derivative, and movements in the fair value of the contract are recorded as income from trading activities. The charge of £1,550 million in 2010 reflects improving credit spreads on the portfolio of covered assets.

A gain of £553 million was booked associated with the liability management exercise undertaken in May 2010, through which the Group strengthened its Core Tier 1 capital base by repurchasing existing Tier 1 securities and exchanging selected existing Upper Tier 2 securities for new senior debt securities. A similar series of exchange and tender offers concluded in April 2009 resulted in a gain of £3,790 million.

Other operating income increased by £606 million to £1,479 million. This improvement principally reflected a profit on sale of securities of £496 million compared with £162 million in 2009, higher profits from associated entities and an increased credit of £249 million compared with £51 million in 2009 relating to movements in own credit adjustments. These were partially offset by losses in the fair value of securities and investment properties.

Insurance net premium income fell by £138 million to £5,128 million principally reflecting lower general insurance premiums, driven by a managed reduction in the risk of the UK motor book, largely offset by price increases.

Business review continued

Operating expenses and insurance claims

	2011 £m	2010 £m	2009 £m
Staff costs			
- excluding gains on pensions curtailment	8,678	9,671	9,993
- gains on pensions curtailment	—	—	(2,148)
Premises and equipment	8,678	9,671	7,845
Other administrative expenses	2,451	2,402	2,594
- managed basis	2,722	2,963	3,163
- Payment Protection Insurance costs	850	—	—
- integration and restructuring costs	1,059	1,032	1,286
- bank levy	300	—	—
	4,931	3,995	4,449
Administrative expenses	16,060	16,068	14,888
Depreciation and amortisation	1,875	2,150	2,166
Write-down of goodwill and other intangible assets	91	10	363
Operating expenses	18,026	18,228	17,417
General insurance	2,968	4,698	4,223
Bancassurance	—	85	134
Insurance net claims	2,968	4,783	4,357
Staff costs as a percentage of total income	30%	30%	30%

2011 compared with 2010

Group operating expenses fell by 1% in 2011, driven by cost savings achieved as a result of the cost reduction programme and Non-Core run-off, largely reflecting the disposal of RBS Sempra and specific country exits, partially offset by Payment Protection Insurance costs.

Staff costs fell 10%, driven by lower Markets and International Banking discretionary compensation as a result of its decrease in revenues, and in Non-Core, given the impact of a 32% reduction in headcount and continued business disposals and country exits.

In May 2011, following the decision of the British Bankers' Association not to appeal the judgement of the judicial review, the Group recorded a provision of £850 million in respect of the costs of Payment Protection Insurance redress.

General insurance claims were £1,730 million lower, mainly due to the non-repeat of bodily injury reserve strengthening in 2010, de-risking of the motor book, more benign weather in 2011 and claims in Non-Core decreasing as legacy policies ran-off.

The Group's cost reduction programme delivered cost savings with an underlying run rate of over £3 billion by the end of 2011.

Business review continued

Operating expenses and insurance claims continued
2010 compared with 2009
The main driver of a 7% decrease in operating expenses, excluding gains on pensions curtailment of £2,148 million, is the recognition of benefits from the Group-wide efficiency programme. The programme continues to deliver material savings which have been funding investments to strengthen our Core franchises. Annualised savings are now just ahead of the £2.5 billion target for 2011 and are forecast to exceed £3 billion by 2013.

Staff costs, excluding pension schemes curtailment gains, fell by £322 million to £9,671 million, driven by savings in Markets, UK Retail, International Banking and Non-Core partially offset by higher costs in Group Centre.

Premises and equipment costs fell by 7% in the year to £2,402 million largely driven by efficiency cost savings, significant one-off property impairments recognised in 2009 and country exits following Non-Core disposals.

Other administrative expenses fell by £454 million to £3,995 million principally reflecting continued savings from the Group's efficiency programme.

Insurance net claims increased 10% to £4,783 million.

Integration costs

	2011 £m	2010 £m	2009 £m
Staff costs	38	210	365
Premises and equipment	6	3	78
Other administrative expenses	51	143	398
Depreciation and amortisation	11	20	18
	106	376	859

Note:
(1) Integration costs for 2011 above exclude £2 million charge included within net interest income and a loss of £3 million within other operating income in respect of integration activities.

2011 compared with 2010
Integration costs were £106 million compared with £376 million in 2010. Integration costs decreased primarily due to a reduction of RBS N.V. (formerly ABN AMRO) integration activity during the year.

2010 compared with 2009
Integration costs were £376 million compared with £859 million in 2009. The fall in integration costs primarily relates to RBS N.V., as they migrate onto RBS systems.

Accruals in relation to integration costs are set out below.

	At 1 January 2011 £m	Charge to income statement £m	Utilised during the year £m	At 31 December 2011 £m
Staff costs - redundancy	—	8	(8)	—
Staff costs - other	—	30	(30)	—
Premises and equipment	24	6	(19)	11

Other administrative expenses	—	51	(48)	3
Depreciation and amortisation	—	11	(11)	—
	24	106	(116)	14

Business review continued

Restructuring costs

	2011 £m	2010 £m	2009 £m
Staff costs	356	353	328
Premises and equipment	156	117	48
Other administrative expenses	276	104	51
	788	574	427

2011 compared with 2010
Restructuring costs were £788 million compared with £574 million in 2010. The increase is due to the number of Group restructuring projects increasing during the year.

2010 compared with 2009
Restructuring costs were £574 million compared with £427 million in 2009. The increase is a result of the number of restructuring projects being undertaken.

Accruals in relation to restructuring costs are set out below.

	At 1 January 2011 £m	Currency translation adjustments £m	Charge to income statement £m	Utilised during the year £m	At 31 December 2011 £m
Staff costs - redundancy	201	—	274	(349)	126
Staff costs - other	17	(1)	82	(58)	40
Premises and equipment	117	—	156	(107)	166
Other administrative expenses	46	(2)	276	(210)	110
	381	(3)	788	(724)	442

Divestment costs

	2011 £m	2010 £m	2009 £m
Staff costs	95	51	—
Premises and equipment	11	6	—
Other administrative expenses	59	25	—
	165	82	—

2011 compared with 2010
Divestment costs of £165 million compared to £82 million in 2010 related to the European Commission mandated divestments.

2010 compared with 2009
Divestment costs of £82 million in the year relate to the European Commission mandated divestments.

Accruals in relation to divestment costs are set out below.

At	Charge	Utilised	At

	1 January 2011	to income statement	during the year	31 December 2011
	£m	£m	£m	£m
Staff costs - redundancy	22	36	(13)	45
Staff costs - other	8	59	(66)	1
Premises and equipment	—	11	(11)	—
Other administrative expenses	2	59	(40)	21
	32	165	(130)	67

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Business review continued

Impairment losses

	2011	2010	2009
	£m	£m	£m
New impairment losses	9,236	9,667	14,224
Less: recoveries of amounts previously written-off	(527)	(411)	(325)
Charge to income statement	8,709	9,256	13,899
Comprising:			
Loan impairment losses	7,241	9,144	13,090
Securities			
- managed basis	200	112	809
- sovereign debt impairment	1,099	—	—
- interest rate hedge adjustments on impaired available-for-sale sovereign debt	169	—	
	1,468	112	809
Charge to income statement	8,709	9,256	13,899

2011 compared with 2010
Impairment losses decreased by 6% compared with 2010, driven largely by a £1,569 million reduction in Non-Core loan impairments, despite continuing challenges in Ulster Bank and corporate real estate portfolios. This was partially offset by impairments taken on the Group's available-for-sale bond portfolio, as a result of the decline in the value of Greek sovereign bonds.

Retail & Commercial impairment losses fell by £227 million, driven by improving credit metrics in UK Retail and US Retail & Commercial partially offset by increases in Ulster Bank, largely reflecting a deterioration in credit metrics on the mortgage portfolio, and a single name provision in International Banking.

Total Core and Non-Core Ulster Bank impairment losses decreased by 4%, as the £223 million increase in Core Ulster Bank losses was more than offset by a decrease in losses recognised in Non-Core.

The Group holds Greek government bonds with a notional amount of £1.45 billion. As a result of Greece's continuing fiscal difficulties, the Group recorded impairment charges on these bonds totalling £1,099 million during the year. These charges were recorded to write the bonds down to their market price as at 31 December 2011 (c.21% of notional).

2010 compared with 2009
Impairment losses were £9,256 million, compared with £13,899 million in 2009. The 33% decrease reflects an overall improvement in the economic environments in which the Group operates.

Impairments fell in all Core businesses, except Ulster Bank Group, which faced an economic environment that remains challenging, with rising default levels across both personal and corporate portfolios.

Impairments for Ulster Bank Group (Core and Non-Core) increased to £3,843 million compared with £1,927 million in 2009.

A significant proportion of the reduction in Core impairments relates to lower specific and latent provisions in UK Retail, UK Corporate, International Banking, US Retail & Commercial and Markets.

Non-Core impairments fell by 41% in 2010 reflecting the gradual improvement in the economic environment through 2010 and lower specific provisions, alongside a non-repeat of the large single name losses seen in 2009.

Business review continued

Tax

	2011	2010	2009
	£m	£m	£m
Tax (charge)/credit	(1,250)	(634)	429
	%	%	%
UK corporation tax rate	26.5	28.0	28.0
Effective tax rate	nm	nm	16.2

nm = not meaningful

The actual tax (charge)/credit differs from the expected tax credit computed by applying the standard rate of UK corporation tax as follows:

	2011	2010	2009
	£m	£m	£m
Expected tax credit	203	112	741
Sovereign debt impairment where no deferred tax asset recognised	(275)	—	—
Other losses in year where no deferred tax asset recognised	(530)	(450)	(780)
Foreign profits taxed at other rates	(417)	(517)	(276)
UK tax rate change - deferred tax impact	(110)	(82)	—
Unrecognised timing differences	(20)	11	274
Non-deductible goodwill impairment	(24)	(3)	(102)
Items not allowed for tax			
- losses on strategic disposals and write-downs	(72)	(311)	(152)
- UK Bank levy	(80)	—	—
- employee share schemes	(113)	(32)	(29)
- other disallowable items	(271)	(296)	(327)
Non-taxable items			
- gain on sale of Global Merchant Services	12	221	—
- gain on redemption of own debt	—	11	693
- other non-taxable items	245	341	410
Taxable foreign exchange movements	4	4	1
Losses brought forward and utilised	2	2	94
Adjustments in respect of prior years	196	355	(118)
Actual tax (charge)/credit	(1,250)	(634)	429

2011 compared with 2010
The high tax charge in 2011 reflects profits in high tax regimes (principally US) and losses in low tax regimes (principally Ireland), losses in overseas subsidiaries for which a deferred tax asset has not been recognised (principally Ireland and the Netherlands) and the effect of two reductions of 1% in the rate of UK corporation tax enacted in March 2011 and July 2011 on the net deferred tax balance.

2010 compared with 2009
The high tax charge in 2010 reflects profits in high tax regimes and losses in low tax regimes, together with £450 million relating to losses in overseas subsidiaries for which a deferred tax asset has not been recognised, and £311 million mainly in respect of losses on disposal of businesses for which no tax relief if available. This was offset in part by the non-taxable gain arising on the disposal of 80.01% of the GMS business.

Business review continued

Divisional performance

Operating profit/(loss) by division	2011 £m	2010 £m	2009 £m
UK Retail	2,021	1,348	375
UK Corporate	1,924	1,893	1,392
Wealth	248	283	373
International Banking	755	1,311	1,118
Ulster Bank	(984)	(683)	(385)
US Retail & Commercial	537	349	(52)
Retail & Commercial	4,501	4,501	2,821
Markets	899	2,724	4,991
Direct Line Group	454	(295)	58
Central items	191	630	456
Core	6,045	7,560	8,326
Non-Core	(4,221)	(5,715)	(14,461)
Managed basis	1,824	1,845	(6,135)
Reconciling items			
Own credit adjustments	1,914	242	(97)
Asset Protection Scheme	(906)	(1,550)	—
Payment Protection Insurance costs	(850)	—	—
Sovereign debt impairment	(1,099)	—	—
Amortisation of purchased intangible assets	(222)	(369)	(272)
Integration and restructuring costs	(1,064)	(1,032)	(1,286)
Gain on redemption of own debt	255	553	3,790
Strategic disposals	(104)	171	132
Gains on pension curtailment	—	—	2,148
Bank levy	(300)	—	—
Write-down of goodwill and other intangible assets	(11)	(10)	(363)
Bonus tax	(27)	(99)	(208)
Interest rate hedge adjustments on impaired available-for-sale sovereign debt	(169)	—	—
RFS Holdings minority interest	(7)	(150)	(356)
Group operating loss before tax	(766)	(399)	(2,647)

Impairment losses/(recoveries) by division	2011 £m	2010 £m	2009 £m
UK Retail	788	1,160	1,679
UK Corporate	793	767	936
Wealth	25	18	33
International Banking	168	86	418
Ulster Bank	1,384	1,161	649
US Retail & Commercial	326	519	705
Retail & Commercial	3,484	3,711	4,420
Markets	38	65	250
Direct Line Group	—	—	8
Central items	(2)	4	—
Core	3,520	3,780	4,678
Non-Core	3,919	5,476	9,221
Managed basis	7,439	9,256	13,899
Reconciling items			
Sovereign debt impairment	1,099	—	—
Interest rate hedge adjustments on impaired available-for-sale sovereign debt	169	—	—
RFS Holdings minority interest	2	—	—
Group impairment losses	8,709	9,256	13,899

Net interest margin by division	2011 %	2010 %	2009 %
UK Retail	3.95	3.89	3.74
UK Corporate	3.06	2.89	2.53
Wealth	3.23	3.26	4.07
International Banking	1.73	1.92	1.86
Ulster Bank	1.87	2.03	1.83
US Retail & Commercial	3.06	2.82	2.34
Retail & Commercial	2.97	2.91	2.62
Non-Core	0.63	1.02	0.74
Group net interest margin	1.92	2.06	1.76

Risk-weighted assets by division	2011 £bn	2010 £bn	2009 £bn
UK Retail	48.4	48.8	51.3
UK Corporate	79.3	84.2	92.5
Wealth	12.9	12.5	11.2
International Banking	43.2	51.7	67.7
Ulster Bank	36.3	31.6	29.9
US Retail & Commercial	59.3	57.4	60.1
Retail & Commercial	279.4	286.2	312.7
Markets	120.3	110.3	72.4
Other	12.0	18.0	9.4
Core	411.7	414.5	394.5
Non-Core	93.3	153.7	171.3
Group before benefit of Asset Protection Scheme	505.0	568.2	565.8
Benefit of Asset Protection Scheme	(69.1)	(105.6)	(127.6)

Group before RFS Holdings minority interest	435.9	462.6	438.2
RFS Holdings minority interest	3.1	2.9	102.8
Group	439.0	465.5	541.0

Divisional performance continued
Employee numbers at 31 December
(full time equivalents in continuing operations rounded to the nearest hundred)

	2011	2010	2009
UK Retail	27,700	28,200	30,000
UK Corporate	13,600	13,200	12,400
Wealth	5,700	5,200	4,600
International Banking	5,400	5,300	6,800
Ulster Bank	4,200	4,200	4,500
US Retail & Commercial	15,400	15,900	15,700
Retail & Commercial	72,000	72,000	74,000
Markets	13,900	15,700	14,300
Direct Line Group	14,900	14,500	13,900
Central items	6,200	4,700	4,200
Core	107,000	106,900	106,400
Non-Core	4,700	6,900	15,100
	111,700	113,800	121,500
Business Services	34,000	34,400	38,600
Integration and restructuring	1,100	300	500
RFS Holdings minority interest	—	—	300
Group	146,800	148,500	160,900

UK Retail

	2011	2010	2009
	£m	£m	£m
Net interest income	4,302	4,054	3,598
Net fees and commissions	1,066	1,100	1,244
Other non-interest income	140	322	391
Non-interest income	1,206	1,422	1,635
Total income	5,508	5,476	5,233
Direct expenses			
- staff	(839)	(889)	(968)
- other	(437)	(480)	(458)
Indirect expenses	(1,423)	(1,514)	(1,619)
	(2,699)	(2,883)	(3,045)
Profit before insurance net claims and impairment losses	2,809	2,593	2,188
Insurance net claims	—	(85)	(134)
Impairment losses	(788)	(1,160)	(1,679)
Operating profit	2,021	1,348	375
Analysis of income by product			
Personal advances	1,089	993	1,192
Personal deposits	961	1,102	1,349
Mortgages	2,277	1,984	1,214
Cards	950	962	869
Other, including bancassurance	231	435	609
Total income	5,508	5,476	5,233
Analysis of impairments by sector			
Mortgages	182	177	124
Personal	437	682	1,023
Cards	169	301	532
Total impairment losses	788	1,160	1,679
Loan impairment charge as % of gross customer loans and advances (excluding reverse repurchase agreements) by sector			
Mortgages	0.2%	0.2%	0.1%
Personal	4.3%	5.8%	7.5%
Cards	3.0%	4.9%	8.6%
Total	0.7%	1.1%	1.6%
Performance ratios			
Return on equity (1)	24.5%	16.3%	4.8%
Net interest margin	3.95%	3.89%	3.74%
Cost:income ratio	49%	53%	58%
Adjusted cost:income ratio (2)	49%	53%	60%
	£bn	£bn	£bn
Capital and balance sheet			
Loans and advances to customers (gross) (3)			
- mortgages	95.0	90.6	83.2

- personal	10.1	11.7	13.6
- cards	5.7	6.1	6.2
	110.8	108.4	103.0
Customer deposits (excluding bancassurance) (3)	101.9	96.1	87.2
Assets under management (excluding deposits)	5.5	5.7	5.3
Risk elements in lending (3)	4.6	4.6	5.7
Loan:deposit ratio (excluding repos)	106%	110%	115%
Risk-weighted assets	48.4	48.8	51.3

Notes:

(1) Divisional return on equity is based on divisional operating profit after tax divided by average notional equity (based on 10% of the monthly average of divisional RWAs, adjusted for capital deductions).

(2) Adjusted cost:income ratio is based on total income after netting insurance claims, and operating expenses.

(3) Includes disposal groups: loans and advances to customers - £7.3 billion; customer deposits - £8.8 billion; risk elements in lending - £0.5 billion.

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Business review continued

UK Retail continued

In 2010, UK Retail set out an aspiration to become the UK's most helpful bank and launched the Customer Charter. In 2011, we made good progress on our Customer Charter commitments and the roll-out of innovation that actually helps customers. In December 2011, UK Retail refined its staff incentive scheme to further strengthen the role of customer service and to help build long lasting customer relationships.

Progress against the Customer Charter commitments is independently assessed and has shown encouraging results. By the end of 2011, we achieved the goal of serving 80% of our customers in less than 5 minutes in our busiest branches. Branch opening hours have also been extended and standardised, which means that our branches are now open for an additional 5,000 hours per week at times our customers have told us suit them.

Innovation has supported the delivery of Helpful Banking by focusing on solutions that make it easier for customers to bank with RBS and NatWest. An important example has been giving customers access to 24 hour emergency cash from NatWest and RBS ATMs when their cards are lost or stolen. We also updated our market-leading iPhone application and by the end of the year 1 million customers had downloaded the application. With successful apps also launched for iPad, Android and Blackberry, RBS is now the leading mobile bank in the UK.

2011 compared with 2010

UK Retail delivered strong full year results, as operating profit increased by £673 million to £2,021 million, despite continued uncertainty in the economic climate and the low interest rate environment. Impairments fell by £372 million, with further improvements in the unsecured book and continued careful mortgage underwriting. Return on equity improved to 24.5%.

The division continued to focus on growing secured lending while at the same time building customer deposits, thereby reducing the Group's reliance on wholesale funding. Loans and advances to customers grew 2%, with a change in mix from unsecured to secured as the Group actively sought to improve its risk profile. Mortgage balances grew by 5%, while unsecured lending contracted by 11%.

- Mortgage growth reflected continued strong new business levels. Gross mortgage lending market share of 10% continues above our stock position of 8%.

- Customer deposits grew 6%, outperforming the market total deposit growth of 3%. Savings balances grew by £6 billion, or 9%, with 1.5 million accounts opened, demonstrating the strength of our customer franchise and our strategy to further develop primary banking relationships.

Net interest income increased by 6% to £4,302 million, driven by strong balance sheet growth. Net interest margin decreased 6 basis points with recovering asset margins more than offset by more competitive savings rates and lower long term swap rate returns adversely impacting liability margins.

Non-interest income declined 15% to £1,206 million, primarily driven by lower investment and protection income as a result of the dissolution of the bancassurance joint venture. In addition, a number of changes have been made to support delivery of Helpful Banking, such as 'Act Now' text alerts, which have decreased fee income.

Overall expenses decreased by 6%, with the adjusted cost:income ratio improving from 53% to 49%. Cost reductions were driven by a clear management focus on process re-engineering and operational efficiency together with benefits from the dissolution of the bancassurance joint venture, partly offset by higher inflation rates in utility and mail costs.

Impairment losses decreased 32% to £788 million reflecting the impact of a strengthened risk appetite, and a more stable economic environment.

Risk-weighted assets were broadly stable, with volume growth in lower risk secured mortgages partly offset by a decrease in the unsecured portfolio.

2010 compared with 2009
Operating profit recovered strongly from the low levels recorded in 2008 and 2009 to £1,348 million and impairments fell by £519 million as the economic environment continued to recover.

The division has continued to focus in 2010 on growing secured lending while at the same time building customer deposits, thereby reducing the Group's reliance on wholesale funding. Loans and advances to customers grew 5%, with a change in mix from unsecured to secured as the Group actively sought to improve its risk profile. Mortgage balances increased by 9% while unsecured lending contracted by 10%.

- Mortgage growth was due to good retention of existing customers and new business, the majority of which comes from the existing customer base. Gross mortgage lending market share remained broadly in line with 2009 at 12%, with the Group on track to meet its Government target on net mortgage lending.

- Customer deposits grew 10% on 2009, reflecting the strength of the UK Retail customer franchise, which outperformed the market in an increasingly competitive environment. Savings balances grew by £8 billion or 13% with 1.8 million accounts opened, outperforming the market total deposit growth of 3%. Personal current account balances increased by 3% on 2009.

Net interest income increased significantly by 13% to £4,054 million, driven by strong balance sheet growth and repricing. Net interest margin improved by 15 basis points to 3.89%, with widening asset margins partially offset by contracting liability margins in the face of a competitive deposit market.

Non-interest income declined 13% to £1,422 million, principally reflecting the restructuring of current account overdraft fees in the final quarter of 2009.

Expenses decreased by 5%, with the cost:income ratio (net of insurance claims) improving from 60% to 53%.

- Direct staff costs declined by 8%, largely driven by a clear management focus on process re-engineering enabling a 7% reduction in headcount.

- RBS continues to progress towards a more convenient, lower cost operating model, with over 4.8 million active users of online banking and a record share of new sales achieved through direct channels. More than 7.8 million accounts have switched to paperless statements and 276 branches now utilise automated cash deposit machines.

Impairment losses decreased 31% to £1,160 million primarily reflecting the recovery in the economic environment.

- The mortgage impairment charge was £177 million (2009 - £124 million) on a total book of £91 billion. Mortgage arrears rates marginally increased in 2010 but remain below the industry average, as reported by the Council of Mortgage Lenders. Repossessions showed only a small increase on 2009, as the Group continues to support customers facing financial difficulties.

- The unsecured lending impairment charge was £983 million (2009 - £1,555 million) on a total book of £18 billion.

Risk-weighted assets decreased by 5% to £48.8 billion, with lower unsecured lending, improving portfolio credit metrics and small procyclicality benefits more than offsetting growth in mortgages.

Business review continued

UK Corporate

	2011 £m	2010 £m	2009 £m
Net interest income	3,092	3,000	2,633
Net fees and commissions	1,375	1,353	1,230
Other non-interest income	396	443	499
Non-interest income	1,771	1,796	1,729
Total income	4,863	4,796	4,362
Direct expenses			
- staff	(922)	(912)	(882)
- other	(390)	(411)	(311)
Indirect expenses	(834)	(813)	(841)
	(2,146)	(2,136)	(2,034)
Profit before impairment losses	2,717	2,660	2,328
Impairment losses	(793)	(767)	(936)
Operating profit	1,924	1,893	1,392
Analysis of income by business			
Corporate and commercial lending	2,643	2,571	2,100
Asset and invoice finance	660	616	500
Corporate deposits	694	738	984
Other	866	871	778
Total income	4,863	4,796	4,362
Analysis of impairments by sector			
Banks and financial institutions	20	20	15
Hotels and restaurants	59	52	98
Housebuilding and construction	103	131	106
Manufacturing	34	1	51
Other	171	133	159
Private sector education, health, social work, recreational and community services	113	30	59
Property	170	245	259
Wholesale and retail trade, repairs	85	91	76
Asset and invoice finance	38	64	113
Total impairment losses	793	767	936
Loan impairment charge as % of gross customer loans and advances (excluding reverse repurchase agreements) by sector			
Banks and financial institutions	0.3%	0.3%	0.2%
Hotels and restaurants	1.0%	0.8%	1.5%
Housebuilding and construction	2.6%	2.9%	2.5%
Manufacturing	0.7%	-	0.9%
Other	0.5%	0.4%	0.5%
Private sector education, health, social work, recreational and community services	1.3%	0.3%	0.9%
Property	0.6%	0.8%	0.8%
Wholesale and retail trade, repairs	1.0%	0.9%	0.7%
Asset and invoice finance	0.4%	0.6%	1.3%

Total	0.7%	0.7%	0.8%
Performance ratios			
Return on equity (1)	15.2%	13.6%	10.4%
Net interest margin	3.06%	2.89%	2.53%
Cost:income ratio	44%	45%	47%

Note:
(1) Divisional return on equity is based on divisional operating profit after tax, divided by average notional equity (based on 10% of the monthly average of divisional RWAs, adjusted for capital deductions).

	2011	2010	2009
	£bn	£bn	£bn
Capital and balance sheet			
Total third party assets	114.2	117.0	116.7
Loans and advances to customers (gross) (1)			
- banks and financial institutions	5.8	6.2	6.3
- hotels and restaurants	6.1	6.8	6.7
- housebuilding and construction	3.9	4.5	4.3
- manufacturing	4.7	5.4	6.0
- other	34.2	32.6	31.0
- private sector education, health, social work, recreational and community services	8.7	9.0	6.5
- property	28.2	29.5	33.0
- wholesale and retail trade, repairs	8.7	9.9	10.4
- asset and invoice finance	10.4	9.9	8.8
	110.7	113.8	113.0
Customer deposits (1)	126.3	124.5	110.8
Risk elements in lending (1)	5.0	4.0	2.3
Loan:deposit ratio (excluding repos)	86%	90%	101%
Risk-weighted assets	79.3	84.2	92.5

Note:
(1) Includes disposal groups: loans and advances to customers - £12.2 billion; customer deposits - £21.8 billion; risk elements in lending - £1.0 billion.

In 2011, UK Corporate focused on supporting its customers through challenging economic times. As a result of over 5,000 hours of customer research, UK Corporate launched the 'Ahead for Business' promise to its small and medium-sized enterprise (SME) customers.

To deliver on this, the division launched a number of initiatives to improve the service it offers to customers. For example, the 'Working with You' initiative, has seen over 4,600 visits to customer businesses since its launch in Q2 2011. Additionally, following the launch of the relationship manager accreditation programme, also in Q2 2011, almost all relationship managers have gained full accreditation in the initial phase.

UK Corporate continued to support new and existing businesses during 2011:
- launching its best ever fixed rate loan product for SMEs;
- reacting quickly after the August riots to give affected businesses access to special interest rate and fee free lending products;
- answering over 4,000 calls on the Start-up Hotline, offering free advice and a complementary business plan review service; and
- supporting more debt capital and loan market deals for larger corporates than any other bank.

The division also took measures to reduce the risk retained in the business allowing for quicker and more consistent decisions by
simplifying the credit underwriting process and improving automated decision making.

2011 compared with 2010
Operating profit increased 2% to £1,924 million, as higher income was only partially offset by higher impairments and an increase in expenses. Net interest income remained broadly flat. Net interest margin improved 17 basis points with benefits from re-pricing the lending portfolio and the revision to income deferral assumptions in Q1 2011 partially

offset by increased funding costs together with continued pressure on deposit margins. A 1% increase in deposit balances supported an improvement in the loan:deposit ratio to 86%.

Non-interest income decreased by 1% as a result of lower Markets cross-sales and fee income, partially offset by increased Invoice Finance and Lombard income.

Excluding the £29 million OFT penalty in 2010, total costs increased by 2%, largely reflecting increased investment in the business and higher costs of managing the non-performing book.

Impairments of £793 million were 3% higher due to increased specific impairments and collectively assessed provisions, partially offset by lower latent loss provisions.

2010 compared with 2009
Operating profit grew by £501 million, 36%, compared with 2009, driven by strong income growth and significantly lower impairments, partially offset by higher costs.

UK Corporate performed strongly in the deposit market, with customer deposit balance growth of £14 billion contributing to a 11 percentage point improvement in the loan:deposit ratio in 2010. While customer lending increased only marginally (with gross lending largely offset by customer deleveraging) net interest income rose by £367 million, 14%, and net interest margin rose by 36 basis points driven primarily by the good progress made on loan repricing.

Non-interest income increased 4% reflecting strong refinancing levels and increased operating lease activity, partially offset by lower sales of financial market products.

Total costs increased 5% (£102 million) or 4% excluding the OFT penalty in 2010.

Impairments were 18% lower, primarily as a result of higher charges taken during the first half of 2009 to reflect potential losses in the portfolio not yet specifically identified.

Return on equity increased from 10.4% to 13.6%, reflecting higher operating profit and lower RWAs as a result of improved risk metrics.

Wealth

	2011	2010	2009
	£m	£m	£m
Net interest income	645	588	616
Net fees and commissions	375	376	363
Other non-interest income	84	71	83
Non-interest income	459	447	446
Total income	1,104	1,035	1,062
Direct expenses			
- staff	(413)	(382)	(357)
- other	(195)	(142)	(144)
Indirect expenses	(223)	(210)	(155)
	(831)	(734)	(656)
Profit before impairment losses	273	301	406
Impairment losses	(25)	(18)	(33)
Operating profit	248	283	373
Analysis of income			
Private banking	902	836	869
Investments	202	199	193
Total income	1,104	1,035	1,062
Performance ratios			
Return on equity (1)	13.1%	15.9%	24.8%
Net interest margin	3.23%	3.26%	4.07%
Cost:income ratio	75%	71%	62%
	£bn	£bn	£bn
Capital and balance sheet			
Loans and advances to customers (gross)			
- mortgages	8.3	7.8	6.5
- personal	6.9	6.7	4.9
- other	1.7	1.6	2.3
	16.9	16.1	13.7
Customer deposits (2)	38.2	37.1	35.7
Assets under management (excluding deposits) (2)	30.9	33.9	32.5
Risk elements in lending	0.2	0.2	0.2
Loan:deposit ratio (excluding repos) (2)	44%	43%	38%
Risk-weighted assets	12.9	12.5	11.2

Notes:

(1) Divisional return on equity is based on divisional operating profit after tax divided by average notional equity (based on 10% of the monthly average of divisional RWAs, adjusted for capital deductions).

(2) 2010 and 2009 comparatives have been revised to reflect the current reporting methodology.

2011 has been a significant year for the Coutts businesses from a strategic perspective. In Q1 2011, a new divisional strategy was
defined with the execution of early changes already making an impact.

Key strategic changes in 2011 included:

- A refreshed Coutts brand bringing Coutts UK and RBS Coutts under one single contemporary brand.
- A refocus on territories where the businesses have the opportunity for greatest scale or growth such as UK, Asia, Middle East, and Eastern Europe.
- Further development of client propositions as well as the portfolio of products and services for key international markets.
- Strategic investment in technology leading to the development of a single global technology platform for the Wealth division. The platform was successfully deployed in Adam & Company in 2011 with Coutts UK to follow in 2012.
- Strengthening the connectivity between Wealth and other Group divisions including referrals in international jurisdictions and improved connectivity with UK Corporate.
- Continued activity to ensure the division responds to new or expected regulatory changes with proactive solution design and preparation.
- Injection of new management into key roles from both internal and external sources including key segment heads, marketing, products & services, and international executive leadership.

Following the establishment of a single global brand in Q4 2011, focus turned to the reorganisation of key global functions such as marketing and product & services, as well as some local management structures. These reorganisations have realigned the division to maximise execution of the divisional strategy. The execution plan for the strategy will continue into 2012 and position Wealth strongly against its peers.

2011 compared with 2010
Operating profit decreased by 12% on 2010 to £248 million, driven by increases in expenses (13%) and impairments (39%) partially offset by a 7% growth in income.

Income increased by £69 million with a 24 basis points improvement in lending margins, strong treasury income and increases in lending and deposit volumes. Non-interest income rose 3%, with investment income growing 2% despite turbulent market conditions.

Expenses increased by £97 million, largely driven by adverse foreign exchange movements and headcount growth to service the increased revenue base. Additional strategic investment in technology enhancement, rebranding and programmes to support regulatory change also contributed to the increase.

Client assets and liabilities managed by the division decreased by 1%. Customer deposits grew 3% in a competitive environment and lending volumes grew 5%. Assets under management declined 9%, with fund outflows contributing 3% of the decrease and market conditions making up the balance.

2010 compared with 2009

2010 operating profit fell by 24% driven by lower net interest income and higher expenses, partly offset by a 45% decline in impairments in the year.

Income declined by 3% primarily due to lower net interest income. Strong lending and investment income was offset by the impact of a competitive deposit market.

Expenses grew by 12% to £734 million. Direct expenses were up 5%, £23 million reflecting additional strategic investment. Indirect expenses increased by £55 million reflecting a change in allocation of Business Services costs.

Assets under management grew by 4% largely through improving market conditions.

Business review continued

International Banking

	2011	2010	2009
	£m	£m	£m
Net interest income from banking activities	1,199	1,353	1,665
Funding costs of rental assets	(42)	(37)	(49)
Net-interest income	1,157	1,316	1,616
Non-interest income	1,398	1,961	1,940
Total income	2,555	3,277	3,556
Direct expenses			
- staff	(706)	(871)	(934)
- other	(226)	(274)	(317)
Indirect expenses	(700)	(735)	(769)
	(1,632)	(1,880)	(2,020)
Profit before impairment losses	923	1,397	1,536
Impairment losses	(168)	(86)	(418)
Operating profit	755	1,311	1,118
Of which:			
Ongoing businesses	773	1,348	1,136
Run-off businesses	(18)	(37)	(18)
Analysis of income by product			
Cash management	940	1,368	1,298
Trade finance	275	243	246
Portfolio	1,265	1,578	1,886
Ongoing businesses	2,480	3,189	3,430
Run-off businesses	75	88	126
Total income	2,555	3,277	3,556
Analysis of impairments by sector			
Manufacturing and infrastructure	254	(17)	89
Property and construction	17	102	50
Transport and storage	11	—	2
Telecommunications, media and technology	—	7	—
Banks and other financial institutions	(42)	49	174
Other	(72)	(55)	103
	168	86	418
Performance ratios (ongoing businesses)			
Return on equity (1)	11.5%	15.4%	11.5%
Net interest margin	1.73%	1.92%	1.86%
Cost:income ratio	62%	55%	55%
	£bn	£bn	£bn
Capital and balance sheet			
Total third party assets (excluding derivatives mark-to-market)	69.9	77.9	75.3
Loans and advances	60.3	66.0	66.9

Customer deposits (excluding repos)	45.1	43.7	38.1
Risk elements in lending	1.6	1.5	1.0
Loan:deposit ratio (excluding repos)	126%	142%	171%
Risk-weighted assets	43.2	51.7	67.7
	£m	£m	£m
Run-off businesses (2)			
Total income	75	88	126
Direct expenses	(93)	(125)	(144)
Operating loss	(18)	(37)	(18)

Notes:

(1) Divisional return on equity is based on divisional operating profit after tax divided by average notional equity (based on 10% of the monthly average of divisional RWAs, adjusted for capital deductions).

(2) Run-off businesses consist of the exited corporate finance businesses.

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International Banking serves companies with a leading client proposition focused on financing, transaction services and risk management. The International Banking structure and governance were complete by the end of June 2012. Management is focused on leveraging the International network and the Transaction Services offering to ensure relevance and intimacy with the division's client base.

During the year, International Banking invested in improving existing products and services and also in developing new ones. To help corporate treasurers manage their global positions, the division launched a global Liquidity Solutions Portal, giving its customers a view of their operational and investment balances and rates all in one place, improving transparency, and enabling them to execute and redeem investments effectively.

2011 compared with 2010
Operating profit was down 42%, partly reflecting the sale of Global Merchant Services (GMS) which completed on 30 November 2010. Adjusting for the disposal, operating profit decreased 32%, driven by an impairment provision on a single name in 2011.

Excluding GMS income of £451 million, income was 10% lower despite the success of deposit-gathering initiatives, as deposits increased £2 billion in a competitive environment.

Excluding GMS expenses of £244 million, expenses decreased by £4 million, reflecting business improvement initiatives and investment in technology and support infrastructure.

Impairment losses increased to £168 million compared with £86 million in 2010 reflecting a single name impairment.

For the eleven months in 2010 before completion of the disposal, GMS generated income of £451 million, total expenses of £244 million and an operating profit of £207 million.

2010 compared with 2009
Operating profit increased 17%, driven by lower costs and impairment losses (which has more than compensated for the loss of Global Merchant Services (GMS) income). Adjusting for the disposal operating profit increased 28%.

For the eleven months before disposal, International Banking booked income of £451 million (2009 - £505 million) and total expenses of £244 million (2009 - £249 million) for GMS, generating an operating profit of £207 million (2009 - 256 million).

Income was down 8%, or 7% excluding GMS, reflecting lower deposit volumes in Cash Management business, a decline in the Trade Finance business.

Expenses decreased 7% to £1,880 million, as increased investment in front office and support infrastructure was offset by tight management of business costs.

Third party assets increased by £2.6 billion, or £1.5 billion excluding GMS, as Yen clearing activities were brought in-house and loans and advances increased.

Business review continued

Ulster Bank

	2011	2010	2009
	£m	£m	£m
Net interest income	736	839	763
Net fees and commissions	142	156	228
Other non-interest income	69	58	26
Non-interest income	211	214	254
Total income	947	1,053	1,017
Direct expenses			
- staff	(221)	(237)	(325)
- other	(67)	(74)	(86)
Indirect expenses	(259)	(264)	(342)
	(547)	(575)	(753)
Profit before impairment losses	400	478	264
Impairment losses	(1,384)	(1,161)	(649)
Operating loss	(984)	(683)	(385)
Analysis of income by business			
Corporate	435	521	580
Retail	428	465	412
Other	84	67	25
Total income	947	1,053	1,017
Analysis of impairments by sector			
Mortgages	570	294	74
Corporate			
- property	324	375	306
- other corporate	434	444	203
Other lending	56	48	66
Total impairment losses	1,384	1,161	649
Loan impairment charge as % of gross customer loans and advances (excluding reverse repurchase agreements) by sector			
Mortgages	2.8%	1.4%	0.5%
Corporate			
- property	6.8%	6.9%	3.0%
- other corporate	5.6%	4.9%	1.8%
Other lending	3.5%	3.7%	2.7%
Total	4.1%	3.1%	1.6%
Performance ratios			
Return on equity (1)	(22.8%)	(16.8%)	(12.7%)
Net interest margin	1.87%	2.03%	1.83%
Cost:income ratio	58%	55%	74%

Note:
(1) Divisional return on equity is based on divisional operating loss after tax divided by average notional equity (based on 10% of the monthly average of divisional RWAs, adjusted for capital deductions).

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	2011	2010	2009
	£bn	£bn	£bn
Capital and balance sheet			
Loans and advances to customers (gross)			
- mortgages	20.0	21.2	16.2
- corporate			
- property	4.8	5.4	10.1
- other corporate	7.7	9.0	11.0
- other lending	1.6	1.3	2.4
	34.1	36.9	39.7
Customer deposits	21.8	23.1	21.9
Risk elements in lending			
- mortgages	2.2	1.5	0.6
- corporate			
- property	1.3	0.7	0.7
- other corporate	1.8	1.2	0.8
- other lending	0.2	0.2	0.2
Total risk elements in lending	5.5	3.6	2.3
Loan:deposit ratio (excluding repos)	143%	152%	177%
Risk-weighted assets	36.3	31.6	29.9
Spot exchange rate - €/£	1.196	1.160	1.126

2011 was another difficult year for the business due to the continued challenging economic environment. This was reflected in the financial performance, with ongoing pressure on income and a further increase in impairment losses.

Ulster Bank continues to make progress on its customer commitments and deposit gathering strategy, while cost management and targeting growth in areas that leverage competitive advantage, remain priorities. In 2011, customer numbers increased by 2%, representing a strong performance in current and savings accounts, driven by the enhanced customer service highlighted by our 'Help for what matters' programme.

Following a review of the cost base and operating model, 950 proposed job losses were announced in January 2012, the majority of which are expected by the end of 2012. This decision is a necessary part of the changes required to build a stronger sustainable business for the future.

2011 compared with 2010
Operating profit before impairment losses decreased by £78 million in 2011 with lower income partially mitigated by cost savings. Impairment losses of £1,384 million increased by 19% from 2010 resulting in an operating loss of £984 million, 44% higher than 2010.

Income fell by 10% driven by a contracting performing loan book coupled with higher funding costs. Loans and advances to customers decreased by 8% during 2011.

Expenses fell by 5% reflecting tight management of the cost base across the business.

Impairment losses increased by 19% largely reflecting the deterioration in credit metrics on the mortgage portfolio driven by a combination of higher debt flow and further fall in asset prices.

Despite intense competition, retail and small business deposit balances have grown strongly throughout 2011, driven by the benefits of a focused deposit gathering strategy. However, total customer deposit balances fell by 6% terms largely driven by the outflow of wholesale customer balances due to rating downgrades.

Risk-weighted assets increased by 15% in 2011 reflecting the deterioration in credit risk metrics.

Ulster Bank continued

2010 compared with 2009
Overall performance deteriorated in 2010, largely as a result of an increase in impairment losses of £512 million. Operating profit before impairment increased to £478 million, up 81%, driven by the culmination of a bank-wide cost saving programme during 2010.

Net interest income increased by 10%, as tightening deposit margins due to intensive market competition and movements in foreign exchange rates were offset by actions to increase asset margins.

Non-interest income was 16% lower, basis reflecting a non-recurring gain in 2009.

Loans to customers fell by 7%. On 1 July 2010 the division transferred a portfolio of development property assets to the Non-Core division, partially offset by a simultaneous transfer of a portfolio of retail mortgage assets to the core business.

Despite intense competition, customer deposit balances increased by 5% over the year with strong growth across all deposit categories, driven by a focus on improving the bank's funding profile.

Expenses were 24% lower. The strong year-on-year performance in expenses was primarily driven by an increased focus on active management of the cost base, and the benefits derived from the business restructuring and cost-saving programme which commenced in 2009.

Impairment losses increased by £512 million to £1,161 million reflecting the deteriorating economic environment in Ireland and rising default levels across both personal and corporate portfolios. Lower asset values, particularly in property-related lending together with pressure on borrowers with a dependence on consumer spending have resulted in higher corporate loan losses, while higher unemployment, lower incomes and increased taxation have driven mortgage impairment increases.

Risk-weighted assets have increased due to deteriorating credit risk metrics.

Customer numbers increased by 3% during 2010, with a strong performance in current and savings accounts switchers.

US Retail & Commercial

	2011 US$m	2010 US$m	2009 US$m	2011 £m	2010 £m	2009 £m
Net interest income	3,048	2,940	2,755	1,900	1,902	1,758
Net fees and commissions	1,350	1,328	1,335	841	859	853
Other non-interest income	473	464	368	296	301	235
Non-interest income	1,823	1,792	1,703	1,137	1,160	1,088
Total income	4,871	4,732	4,458	3,037	3,062	2,846
Direct expenses						
- staff	(1,344)	(1,238)	(1,239)	(838)	(801)	(792)
- other	(893)	(897)	(941)	(557)	(580)	(600)
Indirect expenses	(1,250)	(1,255)	(1,255)	(779)	(813)	(801)
	(3,487)	(3,390)	(3,435)	(2,174)	(2,194)	(2,193)
Profit before impairment losses	1,384	1,342	1,023	863	868	653
Impairment losses	(524)	(802)	(1,104)	(326)	(519)	(705)
Operating profit/(loss)	860	540	(81)	537	349	(52)
Average exchange rate - US$/£				1.604	1.546	1.566
Analysis of income by product						
Mortgages and home equity	744	786	781	463	509	499
Personal lending and cards	709	761	707	442	492	451
Retail deposits	1,487	1,465	1,518	927	948	969
Commercial lending	936	901	855	584	583	546
Commercial deposits	667	627	631	416	406	403
Other	328	192	(34)	205	124	(22)
Total income	4,871	4,732	4,458	3,037	3,062	2,846
Analysis of impairments by sector						
Residential mortgages	44	85	114	28	55	73
Home equity	165	164	261	103	106	167
Corporate and commercial	88	354	518	55	228	331
Other consumer	101	146	211	61	96	134
Securities	126	53	—	79	34	—
Total impairment losses	524	802	1,104	326	519	705
Loan impairment charge as % of gross customer loans and advances (excluding reverse repurchase agreements) by sector						
Residential mortgages	0.5%	0.9%	1.1%	0.5%	0.9%	1.1%
Home equity	0.7%	0.7%	1.0%	0.7%	0.7%	1.1%
Corporate and commercial	0.2%	1.1%	1.6%	0.2%	1.1%	1.7%
Other consumer	0.8%	1.4%	1.7%	0.8%	1.4%	1.8%
Total	0.5%	1.0%	1.4%	0.5%	1.0%	1.4%
Performance ratios						
Return on equity (1)	6.3%	3.7%	(0.6%)	6.3%	3.7%	(0.6%)
Net interest margin	3.06%	2.82%	2.34%	3.06%	2.82%	2.34%

Cost:income ratio	72%	72%	77%	72%	72%	77%

Note:
(1) Divisional return on equity is based on divisional operating profit/(loss) after tax divided by average notional equity (based on 10% of the monthly average of divisional RWAs, adjusted for capital deductions).

Business review continued

US Retail & Commercial continued

	2011 US$bn	2010 US$bn	2009 US$bn	2011 £bn	2010 £bn	2009 £bn
Capital and balance sheet						
Total third party assets	117.3	112.4	124.2	75.8	72.4	76.5
Loans and advances to customers (gross)						
- residential mortgages	9.4	9.4	10.6	6.1	6.1	6.5
- home equity	23.1	23.6	25.0	14.9	15.2	15.4
- corporate and commercial	35.3	31.7	31.6	22.9	20.5	19.5
- other consumer	12.0	10.7	12.2	7.7	6.9	7.5
	79.8	75.4	79.4	51.6	48.7	48.9
Customer deposits (excluding repos)	92.8	92.1	98.0	60.0	59.3	60.4
Risk elements in lending						
- retail	1.0	0.7	0.6	0.6	0.4	0.4
- commercial	0.6	0.7	0.4	0.4	0.5	0.2
Total risk elements in lending	1.6	1.4	1.0	1.0	0.9	0.6
Loan:deposit ratio (excluding repos)	85%	81%	80%	85%	81%	80%
Risk-weighted assets	91.8	89.1	97.5	59.3	57.4	60.1
Spot exchange rate - US$/£				1.548	1.552	1.622

Sterling weakened relative to the US dollar during the fourth quarter, with the average exchange rate decreasing by 2% compared with Q3 2011.

US R&C continued to focus on its back-to-basics strategy, with good progress made in developing the division’s customer franchise during 2011. The bank continued to re-energise the franchise through new branding, product development and competitive pricing.

To strengthen retail alignment and improve efficiencies, US R&C formed a consolidated Consumer Banking division by combining management of the retail banking franchise with the consumer lending division during H2 2011. This continued focus on alignment is expected to further contribute to the improved penetration of loan products to deposit households, which has already increased in ten consecutive quarters. The penetration of on-line banking customers, a key indicator of customer retention, also continued to improve during 2011.

To enhance the customer experience, in Q4 2011, Consumer Banking introduced four core Customer Commitments, built around feedback received from customers in Massachusetts. In Q1 2012, the Commitments will be rolled out to Citizens Financial Group’s (CFG’s) entire branch footprint.

Significant organisational changes and investment in Commercial Banking, including unification under the RBS Citizens brand, has been important in positioning the business for growth. The enhanced sales training programme for managers and sales colleagues in this business has begun to deliver results with both higher credit balances and increased client satisfaction. External researchers TNS awarded Citizens the second highest score in relationship manager satisfaction among its competitors for 2011.

Risk management was also an important focus for 2011 and in Q4 2011, CFG’s Board of directors approved a new formal risk appetite statement aimed at ensuring sustained predictable earnings and further strengthening the control environment.

2011 compared with 2010

Operating profit increased to £537 million ($860 million) from £349 million ($540 million), an increase of £188 million ($320 million), or 54%. Excluding a credit of £73 million ($113 million) related to changes to the defined benefit plan in Q2 2010, operating profit increased by £261 million ($433 million), or 95%, substantially driven by lower impairments and improved income.

The macroeconomic operating environment remained challenging, with low rates, high unemployment, a soft housing market, sluggish consumer activity and the continuing impact of legislative changes including the Durbin Amendment in the Dodd-Frank Act which became effective on 1 October 2011.

The Durbin Amendment lowers the allowable interchange on debit transactions to $0.23-$0.24 per transaction. The current annualised impact of the Durbin Amendment is estimated at £94 million ($150 million).

Net interest income was down £2 million. In US dollar terms, net interest income increased by $108 million, 4%. Net interest margin improved by 24 basis points to 3.06% reflecting changes in deposit mix, continued discipline around deposit pricing and the positive impact from the balance sheet restructuring programme carried out during Q3 2010 combined with strong commercial loan growth, partially offset by run-off of consumer loans.

Non-interest income was down £23 million, 2%. In US dollar terms, non-interest income increased by $31 million, 2%. The increase is primarily driven by higher account and transaction fees, partially offset by the impact of legislative changes on debit card and deposit fees.

Excluding the defined benefit plan credit of £73 million ($113 million) in Q2 2010, total expenses were down £93 million, 4% ($16 million in US dollar terms) due to a number of factors including lower Federal Deposit Insurance Corporation (FDIC) deposit insurance levies, and lower litigation and marketing costs, partially offset by higher regulatory costs.

Impairment losses declined by £193 million ($278 million), or 37%, largely reflecting an improved credit environment slightly offset by higher impairments related to securities. Loan impairments as a percent of loans and advances improved to 0.5% from 1.0%.

Customer deposits were up 1% with particularly strong growth achieved in checking balances. Consumer checking balances grew by 6%, while small business checking balances grew by 5% over the year.

2010 compared with 2009

Operating profit of £349 million ($540 million) represented a marked improvement from an operating loss of £52 million ($81 million) with income up 8% and impairment losses down 26%.

Net interest income was up 8%, despite a smaller balance sheet, with net interest margin improving by 48 basis points to 2.82%.

Non-interest income was up 7% reflecting higher mortgage banking and debit card income, commercial banking fees and higher gains on securities realisations. This was partially offset by lower deposit fees which were impacted by Regulation E legislative changes in 2010. In addition, gains of £213 million ($330 million) were recognised on the sale of available-for-sale securities as part of the balance sheet restructuring exercise, but these were almost wholly offset by losses crystallised on the termination of swaps hedging fixed-rate funding.

Total expenses were up £1 million ($45 million), reflecting a £73 million ($113 million) credit related to changes to the defined benefit pension plan, and lower Federal Deposit Insurance Corporation (FDIC) deposit insurance levies, partially offset by the impact of changing rates on the valuation of mortgage servicing rights and litigation costs.

Impairment losses declined 26%, following significant loan reserve building in 2009 and a gradual improvement in the underlying credit environment, offset by higher impairments related to securities. Loan impairments as a percentage of loans and advances decreased from 1.4% to 1.0%.

Business review continued

Markets

	2011	2010	2009
	£m	£m	£m
Net interest income	67	581	1,095
Net fees and commissions receivable	371	520	347
Income from trading activities	4,601	5,234	7,669
Other operating income	(624)	(102)	(321)
Non-interest income	4,348	5,652	7,695
Total income	4,415	6,233	8,790
Direct expenses			
- staff	(1,963)	(2,082)	(2,197)
- other	(746)	(663)	(560)
Indirect expenses	(769)	(699)	(792)
	(3,478)	(3,444)	(3,549)
Profit before impairment losses	937	2,789	5,241
Impairment losses	(38)	(65)	(250)
Operating profit	899	2,724	4,991
Of which:			
Ongoing businesses	943	2,743	4,764
Run-off businesses	(44)	(19)	227
Analysis of income by product			
Rates	1,474	2,312	4,111
Currencies	1,060	1,047	1,220
Asset backed products (ABP)	1,254	1,479	1,534
Credit markets	616	1,350	1,612
Investor products and equity derivatives	593	672	862
Total income continuing businesses	4,997	6,860	9,339
Inter-divisional revenue share	(767)	(883)	(987)
Run-off businesses	185	256	438
Total income	4,415	6,233	8,790
Memo - Fixed income and currencies			
Rates/currencies/ABP/credit markets	4,402	6,191	8,477
Less primary credit markets	(688)	(863)	(1,069)
Total fixed income and currencies	3,714	5,328	7,408
Performance ratios (ongoing businesses)			
Return on equity (1)	6.1%	19.1%	44.1%
Cost:income ratio	79%	55%	40%
Compensation ratio (2)	44%	33%	25%

Notes:

(1) Divisional return on equity is based on divisional operating profit after tax divided by average notional equity (based on 10% of the monthly average of divisional RWAs, adjusted for capital deductions).

(2) Compensation ratio is based on staff costs as a percentage of total income.

	2011	2010	2009
	£bn	£bn	£bn
Capital and balance sheet			
Loans and advances	61.2	68.6	73.1
Reverse repos	100.4	94.7	73.3
Securities	108.1	115.8	102.1
Cash and eligible bills	28.1	38.8	74.0
Other	14.8	20.1	27.5
Total third party assets (excluding derivatives mark-to-market)	312.6	338.0	350.0
Net derivative assets (after netting)	37.0	37.4	68.0
Risk-weighted assets	120.3	110.3	72.4
Run-off businesses (£m)			
Total income	185	256	438
Direct expenses	(229)	(275)	(211)
Operating (loss)/profit	(44)	(19)	(227)
Balance sheet - run-off businesses (£bn)			
Total third party assets (excluding derivatives mark-to-market)	1.3	2.4	2.3

During Q4 2011, the market environment continued to weaken. Market volatility remained elevated and liquidity depressed as markets reacted to developments in the European sovereign debt crisis. Deal flow was weak reflecting investor pessimism about the outlook for the world economy. Throughout the year, Markets continued to deliver core products and innovative solutions to clients, while also focusing on management of its cost base and on tight control of its risk positions.

On 12 January 2012 the Group announced changes to its wholesale banking operations in light of a changed market and regulatory environment. The changes saw the reorganisation of RBS's wholesale businesses into 'Markets' and 'International Banking' and the exit and downsizing of selected activities. The changes will ensure the wholesale businesses continue to deliver against the Group's strategy.

2011 compared with 2010

Operating profit fell by 67%, from £2,724 million for 2010 to £899 million for 2011, driven by a 29% decrease in revenue. The year was characterised by volatile and deteriorating credit markets, especially during the second half of the year when the European sovereign debt crisis drove a sharp widening in credit spreads.

Due to this deterioration in the markets both the Rates and Credit businesses suffered significantly, and income from trading activities, which is after funding costs both internal and external, fell from £5,234 million in 2010, to £4,601 million in 2011. The heightened volatility increased risk aversion amongst clients and limited opportunities for revenue generation in the secondary markets.

Total costs increased by 1% due increased investment costs in 2011, which included a programme to meet new regulatory requirements. The compensation ratio in Markets was 44%, driven by fixed salary costs and prior year deferred awards.

Variable compensation accrued in the first half of the year were reduced in the second half of the year, leaving the former GBM 2011 variable compensation awards 58% lower than 2010.

Third party assets fell from £338.0 billion in 2010 to £312.6 billion in 2011 as a result of lower levels of activity and careful management of balance sheet exposures.

A 9% increase in risk-weighted assets reflected the impact of significant regulatory changes, with a £21 billion uplift as a result of CRD III, largely offset by the impact of the division's focus on risk management.

2010 compared with 2009
A fall in operating profit, of 45% year on year reflects sharply reduced revenue partially offset by lower costs and a significant improvement in impairments.

Total income was £2,557 million lower in 2010 driven by increased risk aversion in the market during Q3 and Q4 2010, combined with the non-repeat of favourable market conditions seen in the first half of 2009.

- Higher revenue across the Rates and Currencies businesses during 2009 was driven by rapidly falling interest rates and wide bid-offer spreads generating exceptional revenue opportunities, which have not been repeated in 2010.
- The Credit Markets business weakened by 16%, reflecting lower levels of activity in debt capital markets.

Expenses fell by 3% to £3,444 million. This was largely driven by a decrease in staff costs, including on-going benefits from cost synergies.

The low level of impairments in 2010 reflected a small number of specific cases partially offset by an improved picture on latent loss provisions. This contrasted with 2009, which witnessed a significantly higher level of specific impairments.

Business review continued

Direct Line Group

	2011	2010	2009
	£m	£m	£m
Earned premiums	4,221	4,459	4,519
Reinsurers' share	(252)	(148)	(165)
Net premium income	3,969	4,311	4,354
Fees and commissions	(400)	(410)	(367)
Instalment income	138	159	171
Investment income	265	277	305
Other income	100	179	151
Total income	4,072	4,516	4,614
Direct expenses			
- staff expenses	(288)	(287)	(304)
- other expenses	(333)	(325)	(368)
Indirect expenses	(225)	(267)	(270)
	(846)	(879)	(942)
Impairment losses	-	-	(8)
Net claims	(2,772)	(3,932)	(3,606)
Operating profit/(loss)	454	(295)	58
Analysis of income by product			
Personal lines motor excluding broker			
- own brands	1,874	1,962	1,814
- partnerships	228	373	360
Personal lines home excluding broker			
- own brands	490	488	442
- partnerships	378	408	389
Personal lines rescue and other excluding broker			
- own brands	185	197	191
- partnerships	132	168	220
Commercial	365	341	305
International	346	333	288
Other (1)	74	246	605
Total income	4,072	4,516	4,614
In-force policies (000s)			
Personal lines motor excluding broker			
- own brands	3,787	4,162	4,762
- partnerships	320	645	844
Personal lines home excluding broker			
- own brands	1,811	1,797	1,774
- partnerships	2,497	2,530	2,566
Personal lines rescue and other excluding broker			
- own brands	1,844	1,966	2,262
- partnerships	7,307	7,497	6,688
Commercial	422	352	346
International	1,387	1,082	944

Other (1)	1	644	1,049
Total in-force policies (2)	19,376	20,675	21,235

For notes relating to this table refer to page 44.

	2011	2010	2009
	£m	£m	£m
Gross written premium			
Personal lines motor excluding broker			
- own brand	1,584	1,647	1,738
- partnerships	137	257	311
Personal lines home excluding broker			
- own brand	474	478	462
- partnerships	549	556	560
Personal lines rescue and other excluding broker			
- own brand	174	178	176
- partnerships	174	159	141
Commercial	435	397	395
International	570	425	354
Other (1)	1	201	343
Total gross written premium	4,098	4,298	4,480
Performance ratios			
Return on regulatory capital (3)	11.3%	(7.9%)	1.7%
Return on tangible equity (4)	10.3%	(6.8%)	1.4%
Loss ratio (5)	70%	91%	83%
Commission ratio (6)	10%	10%	8%
Expense ratio (7)	20%	20%	21%
Combined operating ratio (8)	100%	121%	112%
Balance sheet			
Total insurance reserves (£m) (9)	7,284	7,643	7,139

Notes:

(1) 'Other' predominately consists of the personal lines broker business.

(2) Total in-force policies include travel and creditor policies sold through RBS Group. These comprise travel policies included in bank accounts e.g. Royalties Gold Account, and creditor policies sold with bank products including mortgage, loan and card payment protection.

(3) Return on regulatory capital required is based on annualised operating profit/(loss) after tax divided by average notional regulatory equity.

(4) Return on tangible equity is based on annualised operating profit/(loss) after tax divided by average tangible equity.

(5) Loss ratio is based on net claims divided by net premium income.

(6) Commission ratio is based on fees and commissions divided by gross written premium income.

(7) Expense ratio is based on expenses divided by gross written premium.

(8) Combined operating ratio is the sum of the loss, commission and expense ratios.

(9) Consists of general and life insurance liabilities, unearned premium reserves and liability adequacy reserve.

Business review continued

Direct Line Group continued
Direct Line Group continues to make good progress ahead of its divestment from the Group. Operating profit of £454 million for 2011 shows a return to full year profitability and represents close to a £750 million turnaround from 2010. These results demonstrate the success of the first phase of management’s transformation plan - to return to profit in 2011. The full year combined operating ratio improved to 100% (2010 - 121%) with a full year return on equity of 10.3% compared with a negative return of 6.8% in 2010.

The second phase of the Direct Line Group transformation plan, to build competitive advantage, is underway and tangible benefits are already being delivered. All new Churchill, Direct Line and Privilege motor claims, as well as all new Churchill home claims, are now being processed through a new claims management system. Within motor, the rollout of a new rating engine and new pricing tools ensured more accurate and tailored pricing with the aim of generating greater value from Direct Line Group's multi-brand, multi-distribution strategy.

As part of the plan to build competitive advantage, the rationalisation of occupied sites continues, with 15 site exits by the end of 2011. The consolidation of the four UK general insurance underwriting entities within the Direct Line Group was successfully completed in December 2011. All UK general insurance business is now written through one underwriter with the aim of improving operational and capital efficiency.

Marking a significant new partnership, Direct Line Group signed a five-year contract with Sainsbury’s Finance in 2011 to provide underwriting, sales, service and claims management for its car insurance customers. Following the successful launch and development of the car insurance partnership, a further contract was signed early in 2012 to provide home insurance for Sainsbury’s customers. Building on Direct Line Group’s established successful relationship with Nationwide Building Society, a deal was concluded to extend its provision of home insurance until the end of 2015. Direct Line Group is also concluding terms with RBS Group’s UK Retail bank on the details of a five-year agreement for the continued provision of general insurance products post separation. The term would commence from the point of initial divestment.

While overall gross written premium fell by 5% in 2011, it increased by 10% in Commercial, which includes NIG, the commercial broker business, and Direct Line for Business, the direct SME insurer. A new brand identity was unveiled for NIG and work continued to improve its product offering and service to brokers. Direct Line for Business continued to develop well.

Direct Line Group’s international division showed strong growth in gross written premiums primarily in Italy, assisted by the first full year of its sales agreements with FGA Capital, a joint venture between Fiat and Credit Agricole. The German business also showed good growth following improvements in the second half of 2011 to its direct and partnership business, including strengthening its relationship with Renault.

Ahead of the planned divestment in the second half of 2012, Direct Line Group has begun separating its activities and operations from RBS Group. Its corporate functions have been strengthened, arm’s length agreements are under discussion with the Group where appropriate, a new corporate brand, Direct Line Group was announced on 15 February 2012 and a new risk and control framework has been implemented, in readiness for standalone status.

Overall, Direct Line Group has powerful brands, improved earnings, a robust balance sheet and is executing the second phase of its transformation plan to rebuild competitive advantage.

2011 compared with 2010
Operating profit rose by £749 million in 2011, principally due to the non repeat of the bodily injury reserve strengthening in 2010, derisking of the motor book, exit of certain business segments and more benign weather in 2011.

Gross written premium fell £200 million, 5%, as the business continued to drive improved profitability through reduced volumes in unattractive segments. This was partially offset by growth in Commercial and International.

Total income fell £444 million, 10%, following the exit of personal lines broker, a decline in premiums reflecting reduced motor volumes and higher reinsurance costs to reduce the risk profile of the book. Investment income fell £12 million, 4%, reflecting decreased yields on the portfolio in 2011, partially offset by higher realised gains.

Total direct expenses rose by £9 million principally driven by project activity to support the transformation plan.

Net claims fell £1,160 million, 30%, due to the non recurrence of bodily injury reserve strengthening in 2010, actions taken to de-risk the book, the exit of certain business segments and more benign weather in 2011.

At the end of 2011, Direct Line Group 's investment portfolios comprised primarily cash, gilts and investment grade bonds. Within the UK portfolio, £8.9 billion, and the International portfolio, £827 million, there was no exposure to sovereign debt issued by Portugal, Ireland, Italy, Greece or Spain.

Total in-force policies fell 6% in the year due to planned de-risking of the motor book and the exiting of certain other segments and partnerships, including personal lines broker.

2010 compared with 2009
Direct Line Group has embarked on a significant programme of investment designed to achieve a substantial lift in operational and financial performance, ahead of the planned divestment of the business, with a current target date of 2012. This programme encompasses the enhancement of pricing capability, transformation of claims operations and expense reduction, together with a range
of other improvements across the business, including a greater focus on capital management.

2010 as a whole was a disappointing profit year, impacted by significant reserve strengthening for bodily injury claims and severe weather, resulting in a loss of £295 million.

Income was down 2% (£98 million) against 2009, driven by a managed reduction in the risk of the UK motor book, largely offset by significant price increases:

- This de-risking was achieved by a combination of rating action to reduce the mix of higher-risk drivers, and the partial or total exit of higher risk business lines (significantly scaling back the fleet and taxi business and the exit of personal lines business sold through insurance brokers). As a result in-force motor policies fell 14% compared with 2009.

- Even with the significant reduction in the risk mix of the book, average motor premiums were up 7% in the year, due to significant price increases. The prices of like-for-like policies have increased by 35-40% over the last year. These increases were in addition to the significant increases achieved in 2009.

Initiatives to grow ancillary income were also implemented during the year resulting in revenues of £46 million in 2010 (£25 million in 2009). Away from UK motor, overall home gross written premiums grew by 1%. This included the exit from less profitable business in line with overall strategy. Our underlying own brands business continues to grow successfully, with gross written premiums increasing 4%.

The International business continued to invest in growth in 2010 with gross written premiums of £425 million up 20% on 2009. The Italian business successfully grew to a market share approaching 30% of the direct insurer market. The German business grew 7% and is well positioned to take advantage of the emerging shift to direct/internet distribution in that market.

Several programmes to further improve the overall efficiency of the business took effect during the year, including a reduction of six sites and operational process improvements, which will continue to improve efficiency.

Total in-force policies declined by 3%, driven by a fall of 14% in motor policies. This was partly offset by higher travel policies, up 64% with new business from a partnership with Nationwide Building Society commencing in Q4 2010. The personal lines broker segment overall declined by 43%, in line with business strategy.

Total income declined by £98 million, with lower motor premium income, driven by rating action. Increased fees and commissions reflected profit sharing arrangements with UK Retail in relation to insurance distribution to bank customers. Investment income was £28 million lower, reflecting the impact of low interest rates on returns on the investment portfolio as well as lower gains realised on the sale of investments.

Net claims were £326 million higher than in 2009, driven by increases to bodily injury reserves relating to prior years, including allowance for higher claims costs in respect of Periodic Payment Orders due to an increased settlement rate of such claims. Although bodily injury frequency has stabilised, severity has continued to deteriorate. Claims were also impacted by the adverse weather experienced in the first and fourth quarters.

Expenses were down 7%, driven by lower industry levies and marketing costs.

Business review continued

Central items

	2011	2010	2009
	£m	£m	£m
Central items not allocated	191	630	456

Funding and operating costs have been allocated to operating divisions, based on direct service usage, requirement for market funding and other appropriate drivers where services span more than one division.

Residual unallocated items relate to volatile corporate items that do not naturally reside within a division.

2011 compared with 2010
Central items not allocated represented a credit of £191 million in 2011, a decline of £439 million compared with 2010. 2010 benefited from c.£300 million of accounting gains on hybrid securities, c.£150 million of which was amortised during 2011. A VAT recovery of £176 million in 2010 compared with £85 million recovered in 2011.

2010 compared with 2009
Central items not allocated including available-for-sale (AFS) gains of £237 million and one-off VAT recovery in 2010 of £170 million, amounted to a net credit of £630 million, an increase of £174 million on 2009.

The Group’s credit spreads have fluctuated over the course of the year, but ended the year slightly wider, resulting in an overall annual decrease in the carrying value of own debt.

Non-Core

	2011	2010	2009
	£m	£m	£m
Net interest income	858	1,756	1,603
Funding costs of rental assets	(210)	(283)	(256)
Net interest income	648	1,473	1,347
Net fees and commissions	(38)	471	510
Loss from trading activities	(721)	(31)	(5,161)
Insurance net premium income	286	702	784
Other operating income			
- rental income	953	1,035	946
- other (1)	60	(896)	(700)
Non-interest income/(loss)	540	1,281	(3,621)
Total income/(loss)	1,188	2,754	(2,274)
Direct expenses			
- staff	(375)	(731)	(851)
- operating lease depreciation	(347)	(452)	(402)
- other	(256)	(573)	(573)
Indirect expenses	(317)	(500)	(552)
	(1,295)	(2,256)	(2,378)
Profit before insurance net claims and impairment losses	(107)	498	(4,652)
Insurance net claims	(195)	(737)	(588)
Impairment losses	(3,919)	(5,476)	(9,221)
Operating loss	(4,221)	(5,715)	(14,461)
Analysis of income/(loss) by business			
Banking and portfolios	1,465	1,463	(148)
International businesses	411	778	1,296
Markets	(688)	513	(3,422)
Total income/(loss)	1,188	2,754	(2,274)
Loss from trading activities			
Monoline exposures	(670)	(5)	(2,387)
Credit derivative product companies	(85)	(139)	(947)
Asset-backed products (2)	29	235	(288)
Other credit exotics	(175)	77	(558)
Equities	(11)	(17)	(47)
Banking book hedges	(1)	(82)	(1,613)
Other (3)	192	(100)	679
	(721)	(31)	(5,161)
Impairment losses			
Banking and portfolios	3,833	5,328	8,350
International businesses	82	200	499
Markets	4	(52)	372
Total impairment losses	3,919	5,476	9,221

Loan impairment charge as % of gross customer loans and advances (excluding reverse repurchase agreements) (4)			
Banking and portfolios	4.9%	5.0%	5.8%
International businesses	3.7%	4.4%	4.1%
Markets	(3.0%)	0.2%	7.5%
Total	4.8%	4.9%	5.7%

Notes:

(1) Includes losses on disposals of £127 million for 2011 (2010 - £504 million).

(2) Asset-backed products include super asset backed structures and other asset-backed products.

(3) Includes profits in RBS Sempra Commodities JV of £4 million for 2011 (2010 - £372 million).

(4) Includes disposal groups.

Business review continued

Non-Core continued

	2011	2010	2009
Performance ratios			
Net interest margin	0.63%	1.02%	0.74%
Cost:income ratio	109%	82%	(105%)
Adjusted cost:income ratio	130%	112%	(83%)
	£bn	£bn	£bn
Capital and balance sheet			
Total third party assets (excluding derivatives) (1)	93.7	137.9	201.0
Total third party assets (including derivatives) (1)	104.7	153.9	220.9
Loans and advances to customers (gross) (2)	79.4	108.4	149.5
Customer deposits (2)	3.5	6.7	12.6
Risk elements in lending (2)	24.0	23.4	22.9
Risk-weighted assets (1)	93.3	153.7	171.3
Gross customer loans and advances			
Banking and portfolios	77.3	104.9	138.3
International businesses	2.0	3.5	9.4
Markets	0.1	-	1.8
	79.4	108.4	149.5
Risk-weighted assets			
Banking and portfolios	64.8	83.5	92.5
International businesses	4.1	5.6	11.5
Markets	24.4	64.6	67.3
	93.3	153.7	171.3
Third party assets (excluding derivatives)			
Banking and portfolios	81.3	113.9	153.2
International businesses	2.9	4.4	10.9
Markets	9.5	19.6	36.9
	93.7	137.9	201.0

Third party assets (excluding derivatives)	31 December 2010 £bn	Run-off £bn	Disposals/ restructuring £bn	Drawings/ roll overs £bn	Impairments £bn	FX £bn	31 December 2011 £bn
Commercial real estate	42.6	(5.6)	(2.4)	0.7	(3.4)	(0.4)	31.5
Corporate	59.8	(8.5)	(11.3)	2.5	(0.1)	(0.2)	42.2
SME	3.7	(1.6)	-	0.1	(0.1)	-	2.1
Retail	9.0	(1.1)	(1.4)	-	(0.3)	(0.1)	6.1
Other	2.5	(0.6)	-	-	-	-	1.9
Markets	13.6	(2.9)	(1.8)	1.0	-	(0.1)	9.8
Total (excluding derivatives)	131.2	(20.3)	(16.9)	4.3	(3.9)	(0.8)	93.6
	6.7	(1.3)	(5.0)	-	-	(0.3)	0.1

Markets - RBS Sempra Commodities JV							
Total (3)	137.9	(21.6)	(21.9)	4.3	(3.9)	(1.1)	93.7

Notes:
(1) Includes RBS Sempra Commodities JV (2011 third party assets, excluding derivatives (TPAs) £0.1 billion, RWAs £1.6 billion; 2010 TPAs £6.7 billion, RWAs £4.3 billion).
(2) Excluding disposal groups.
(3) Disposals of £0.2 billion have been signed as at 31 December 2011 (2010 - £12 billion).

Impairment losses by donating division and sector	2011 £m	2010 £m	2009 £m
UK Retail			
Mortgages	5	5	6
Personal	(27)	8	47
Total UK Retail	(22)	13	53
UK Corporate			
Manufacturing and infrastructure	76	26	87
Property and construction	224	437	651
Transport	52	3	10
Financial institutions	5	69	102
Lombard	75	129	95
Other	96	166	732
Total UK Corporate	528	830	1,677
Ulster Bank			
Mortgages	-	42	42
Commercial real estate			
- investment	609	630	286
- development	1,552	1,759	733
Other corporate	173	251	217
Other EMEA	15	52	106
Total Ulster Bank	2,349	2,734	1,384
US Retail & Commercial			
Auto and consumer	58	82	136
Cards	(9)	23	130
SBO/home equity	201	277	452
Residential mortgages	16	4	54
Commercial real estate	40	185	224
Commercial and other	(3)	17	83
Total US Retail & Commercial	303	588	1,079
International Banking			
Manufacturing and infrastructure	57	(290)	1,404
Property and construction	752	1,296	1,413
Transport	(3)	33	178
Telecoms, media and technology	68	9	545
Financial institutions	(98)	196	620
Other	(19)	14	616
Total International Banking	757	1,258	4,776
Other			
Wealth	1	51	251
Central items	3	2	1
Total Other	4	53	252
Total impairment losses	3,919	5,476	9,221

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Business review continued

Non-Core continued

Gross loans and advances to customers (excluding reverse repurchase agreements) by donating division and sector	2011 £bn	2010 £bn	2009 £bn
UK Retail			
Mortgages	1.4	1.6	1.9
Personal	0.1	0.4	0.7
Total UK Retail	1.5	2.0	2.6
UK Corporate			
Manufacturing and infrastructure	0.1	0.3	0.3
Property and construction	5.9	11.4	14.1
Transport	4.5	5.4	—
Financial institutions	0.6	0.8	—
Lombard	1.0	1.7	2.9
Other	7.5	7.4	17.6
Total UK Corporate	19.6	27.0	34.9
Ulster Bank			
Mortgages	—	—	6.0
Commercial real estate			
- investment	3.9	4.0	2.1
- development	8.5	8.4	6.3
Other corporate	1.6	2.2	1.3
Other EMEA	0.4	0.4	1.0
Total Ulster Bank	14.4	15.0	16.7
US Retail & Commercial			
Auto and consumer	0.8	2.6	3.2
Cards	0.1	0.1	0.5
SBO/home equity	2.5	3.2	3.7
Residential mortgages	0.6	0.7	0.8
Commercial real estate	1.0	1.5	1.9
Commercial and other	0.4	0.5	0.9
Total US Retail & Commercial	5.4	8.6	11.0
International Banking			
Manufacturing and infrastructure	6.6	8.7	17.5
Property and construction	15.3	19.6	25.7
Transport	3.2	5.5	5.8
Telecoms, media and technology	0.7	0.9	3.2
Financial institutions	5.6	12.0	16.0
Other	7.0	9.3	14.3
Total International Banking	38.4	56.0	82.5
Other			
Wealth	0.2	0.4	2.6
Direct Line Group	-	0.2	0.2

Central items	(0.2)	(1.0)	(3.2)
Total Other	-	(0.4)	(0.4)
Gross loans and advances to customers (excluding reverse repurchase agreements)	79.3	108.2	147.3

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Non-Core third party assets fell to £94 billion, below the revised year end target of £96 billion and significantly ahead of the original guidance of £118 billion. Further reductions will include the sale of RBS Aviation Capital for £4.7 billion, which was signed in January 2012. Since the division was formed in 2009, the reduction totals £164 billion, or 64%. By the end of 2011, the Non-Core funded balance sheet equated to less than 10% of the Group funded balance sheet compared with 21% when the division was created.

The division focused on reducing capital intensive trading assets, with activity including the restructuring of monoline exposures, which, at a cost of c.£600 million in 2011, achieved a reduction of £60 billion in risk-weighted assets.

An operating loss of £4,221 million for 2011 was £1,494 million lower than 2010. Income declined by £1,566 million reflecting continued divestment, including business and country exits. The decrease was partially offset by a reduction in expenses of £961 million, largely driven by the fall in headcount. Impairment losses fell by £1,557 million despite ongoing challenges in the real estate and Ulster Bank portfolios.

2011 compared with 2010
Operating loss of £4,221 million in 2011 was £1,494 million lower than the loss recorded in 2010. The continued divestment of Non-Core businesses and portfolios has reduced revenue streams as well as the cost base.

Losses from trading activities increased by £704 million compared with 2010, principally as a result of the disposal of RBS Sempra Commodities in 2010 and costs incurred as part of the division's focus on reducing capital intensive trading assets and mitigating future regulatory uplifts in risk-weighted assets.

Impairment losses fell by £1,557 million despite ongoing challenges in the real estate and Ulster Bank portfolios, reflecting improvements in other asset classes.

Third party assets declined by £44 billion (32%) reflecting disposals of £22 billion and run-off of £22 billion.

Risk-weighted assets were £60 billion lower than 2010, principally driven by significant disposal activity on trading book assets combined with run-off.

Headcount declined by 2,189 (32%) to 4,669 in 2011, largely reflecting the divestment activity in relation to Asia, Non-Core Insurance and RBS Sempra Commodities.

2010 compared with 2009
By the end of 2010 third party assets (excluding derivatives) had decreased to £138 billion, £5 billion lower than the end of year target, as a result of a successful disposal strategy, managed portfolio run-off and impairments.

2010 operating losses in Non-Core were 60% lower than those recorded in 2009. The improvement in performance was driven by significantly lower trading losses, reduced expenses and a marked decline in impairments.

Losses from trading activities declined from £5,122 million for 2009 to £16 million for 2010 as underlying asset prices recovered, offset by continuing weakness in credit spreads. The division has recorded profits on the disposal of many asset-backed securities positions. In addition, a significantly smaller loss of £82 million was recorded on banking book hedges as spreads tightened, compared with £1,727 million in 2009.

Staff expenses fell by 14% over the year, largely driven by the impact of business divestments, including a number of country exits and the disposal of substantially all of the Group's interest in the RBS Sempra Commodities JV.

Impairments were £3,745 million lower than 2009. The decline reflects the overall improvement in the economic environment, although still high loss rates reflect the difficult conditions experienced in specific sectors, including both UK and Irish commercial property sectors.

Wholesale country exits completed during 2010 were Chile, Colombia, Pakistan and Taiwan.

Risk-weighted assets decreased by £18 billion (10%), reflecting active management to reduce trading book risk and disposals, partially offset by the impact of regulatory changes (£30 billion) and more conservative weightings applied to large corporate exposures.

Consolidated balance sheet at 31 December 2011

	2011 £m	2010 £m	2009 £m
Assets			
Cash and balances at central banks	79,269	57,014	52,261
Net loans and advances to banks	43,870	57,911	56,656
Reverse repurchase agreements and stock borrowing	39,440	42,607	35,097
Loans and advances to banks	83,310	100,518	91,753
Net loans and advances to customers	454,112	502,748	687,353
Reverse repurchase agreements and stock borrowing	61,494	52,512	41,040
Loans and advances to customers	515,606	555,260	728,393
Debt securities	209,080	217,480	267,254
Equity shares	15,183	22,198	19,528
Settlement balances	7,771	11,605	12,033
Derivatives	529,618	427,077	441,454
Intangible assets	14,858	14,448	17,847
Property, plant and equipment	11,868	16,543	19,397
Deferred tax	3,878	6,373	7,039
Prepayments, accrued income and other assets	10,976	12,576	20,985
Assets of disposal groups	25,450	12,484	18,542
Total assets	1,506,867	1,453,576	1,696,486
Liabilities			
Bank deposits	69,113	66,051	104,138
Repurchase agreements and stock lending	39,691	32,739	38,006
Deposits by banks	108,804	98,790	142,144
Customers deposits	414,143	428,599	545,849
Repurchase agreements and stock lending	88,812	82,094	68,353
Customer accounts	502,955	510,693	614,202
Debt securities in issue	162,621	218,372	267,568
Settlement balances	7,477	10,991	10,413
Short positions	41,039	43,118	40,463
Derivatives	523,983	423,967	424,141
Accruals, deferred income and other liabilities	23,125	23,089	30,327
Retirement benefit liabilities	2,239	2,288	2,963
Deferred tax	1,945	2,142	2,811
Insurance liabilities	6,312	6,794	10,281
Subordinated liabilities	26,319	27,053	37,652
Liabilities of disposal groups	23,995	9,428	18,890
Total liabilities	1,430,814	1,376,725	1,601,855
Non-controlling interests	1,234	1,719	16,895
Owners' equity	74,819	75,132	77,736
Total equity	76,053	76,851	94,631
Total liabilities and equity	1,506,867	1,453,576	1,696,486

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Commentary on consolidated balance sheet
2011 compared with 2010
Total assets of £1,506.9 billion at 31 December 2011 were up £53.3 billion, 4%, compared with 31 December 2010. This principally reflects an increase in cash and balances at central banks and the mark-to-market value of derivatives in Markets, partly offset by decreases in debt securities and equity shares and the continuing disposal and run-off of Non-Core assets.

Cash and balances at central banks were up £22.3 billion, 39%, to £79.3 billion due to improvements in the Group's structured liquidity position during 2011.

Loans and advances to banks decreased by £17.2 billion, 17%, to £83.3 billion. Reverse repurchase agreements and stock borrowing ('reverse repos') were down £3.2 billion, 7%, to £39.4 billion and bank placings declined £14.0 billion, 24%, to £43.9 billion, primarily as a result of the reduction in exposure to eurozone banks and lower cash collateral requirements.

Loans and advances to customers were down £39.7 billion, 7%, to £515.6 billion. Within this, reverse repurchase agreements were up £9.0 billion, 17%, to £61.5 billion. Customer lending decreased by £48.7 billion, 10%, to £454.1 billion or £46.9 billion, 9%, to £473.9 billion before impairment provisions. This reflected the transfer to disposal groups of £19.5 billion of customer balances relating to the UK branch-based businesses. There were also planned reductions in Non-Core of £28.1 billion, together with declines in International Banking, £4.7 billion, UK Corporate, £3.0 billion and Ulster Bank, £2.0 billion, together with the effect of exchange rate and other movements, £1.9 billion. These were partially offset by growth in Markets, £6.4 billion, Wealth, £0.8 billion, UK Retail, £2.3 billion and US Retail & Commercial, £2.8 billion.

Debt securities were down £8.4 billion, 4%, to £209.1 billion driven mainly by a reduction in holdings of government and financial institution bonds in Markets and Group Treasury.

Equity shares decreased £7.0 billion, 32%, to £15.2 billion which largely reflects the closure of positions to reduce the Group's level of unsecured funding requirements to mitigate the potential impact of unfavourable market conditions.

Settlement balances declined £3.8 billion, 33% to £7.8 billion as a result of decreased customer activity.

Movements in the value of derivative assets up £102.5 billion, 24%, to £529.6 billion, and liabilities, up £100.0 billion, 24%, to £524.0 billion, primarily reflect increases in interest rate contracts as a result of a significant downward shift in interest rates across all major currencies, together with increases in the mark-to-market value of credit derivatives as a result of widening credit spreads and rising credit default swap prices.

Property, plant and equipment declined £4.7 billion, 28%, to £11.9 billion, primarily as a result of the transfer of RBS Aviation Capital's operating lease assets to disposal groups.

Deferred taxation was down £2.5 billion, 39%, to £3.9 billion, largely as a result of the utilisation of brought forward tax losses in the UK.

The increase in assets and liabilities of disposal groups reflects the reclassification of the UK branch-based businesses and RBS Aviation Capital pending their disposal, partly offset by the completion of disposals, primarily RBS Sempra Commodities JV and certain Non-Core project finance assets.

Deposits by banks increased £10.0 billion, 10%, to £108.8 billion, with higher repurchase agreements and stock lending ('repos'), up £6.9 billion, 21%, to £39.7 billion and higher inter-bank deposits, up £3.1 billion, 5%, to £69.1

billion.

Customer accounts fell £7.7 billion, 2%, to £503.0 billion. Within this, repos increased £6.7 billion, 8%, to £88.8 billion. Excluding repos, customer deposits were down £14.4 billion, 3%, to £414.1 billion, reflecting the transfer to disposal groups of £21.8 billion of customer accounts relating to the UK branch-based businesses. This was partly offset by the net effect of growth in International Banking £1.7 billion, UK Corporate, £1.8 billion, UK Retail, £5.8 billion, US Retail & Commercial, £0.5 billion and Wealth, £1.8 billion, together with exchange rate and other movements of £0.5 billion and declines in Markets, £1.1 billion, Ulster Bank, £0.8 billion and Non-Core, £2.9 billion.

Debt securities in issue were down £55.8billion, 26% to £162.6 billion driven by reductions in the level of certificates of deposit and commercial paper in Markets and Group Treasury.

Settlement balances declined £3.5 billion, 32%, to £7.5 billion and short positions were down £2.1 billion, 5%, to £41.0 billion due to decreased customer activity.

Subordinated liabilities were down £0.7 billion, 3%, to £26.3 billion, primarily reflecting the redemption of £0.2 billion US dollar and £0.4 billion Euro denominated dated loan capital.

The Group’s non-controlling interests decreased by £0.5 billion, 28%, to £1.2 billion, primarily due to the disposal of the majority of the RBS Sempra Commodities JV business, £0.4 billion.

Owners’ equity decreased by £0.3 billion to £74.8 billion. This was driven by the attributable loss for the year, £2.0 billion, together with the recognition of actuarial losses in respect of the Group’s defined benefit pension schemes, net of tax, £0.5 billion and exchange rate and other movements of £0.3 billion. Offsetting these reductions were gains in available-for-sale reserves, £1.1 billion and cashflow hedging reserves, £1.0 billion and the issue of shares under employee share schemes, £0.4 billion.

Business review continued

Commentary on consolidated balance sheet
2010 compared with 2009
Total assets of £1,453.6 billion at 31 December 2010 were down £242.9 billion, 14%, compared with 31 December 2009. This principally reflects the disposal of the RFS minority interest, the continuing planned disposal of Non-Core assets, together with a reduction in the level of debt securities and the mark-to-market value of derivatives.

Cash and balances at central banks were up £4.8 billion, 9%, to £57.0 billion principally due to an improvement in the Group's structural liquidity position during 2010.

Loans and advances to banks increased by £8.8 billion, 10%, to £100.5 billion. Adjusting for the disposal of the RFS minority interest, the increase was £16.6 billion, 20%. Reverse repurchase agreements and stock borrowing (‘reverse repos’) were up £7.5 billion, 21% to £42.6 billion and bank placings rose £9.1 billion, 19%, to £57.9 billion, primarily as a result of the investment of surplus liquidity in short-term assets.

Loans and advances to customers decreased £173.1 billion, 24%, to £555.3 billion. Excluding the disposal of the RFS minority interest, lending to customers was down £40.4 billion, 7%. Within this, reverse repurchase agreements were up £11.5 billion, 28%, to £52.5 billion. Customer lending decreased by £51.9 billion to £502.7 billion or £48.9 billion before impairment provisions. This reflected planned reductions in Non-Core of £39.6 billion along with declines in Markets, £11.9 billion, International Banking, £3.6 billion, US Retail & Commercial, £2.6 billion and Ulster Bank, £1.9 billion. These were partially offset by growth in UK Retail, £5.4 billion, Wealth, £2.4 billion and UK Corporate, £0.8 billion, together with the effect of exchange rate and other movements, £2.1 billion.

Debt securities were down £49.8 billion, 19%, to £217.5 billion, or £31.6 billion, 13%, adjusting for the disposal of the RFS minority interest, driven mainly by reductions in Markets.

The value of derivative assets were down £14.4 billion, 3%, to £427.1 billion, primarily reflecting a decrease in interest contracts, movements in five to ten year interest yields, and the combined effect of currency movements, with Sterling weakening against the dollar but strengthening against the Euro.

The reduction in assets and liabilities of disposal groups resulted from the completion of disposals of certain of the Group’s Asian and Latin American businesses, and substantially all of the RBS Sempra Commodities JV business.

Deposits by banks declined £43.4 billion, 31%, to £98.8 billion or £66.1 billion, 36% following the disposal of the RFS minority interest, with reduced inter-bank deposits, down £49.7 billion, 43%, to £66.1 billion and lower repurchase agreements and stock lending (‘repos’), down £5.3 billion, 14%, to £32.7 billion.

Customer accounts decreased £103.5 billion, 17%, to £510.7 billion but excluding the disposal of the RFS minority interest were up £28.1 billion, 6%. Within this, repos increased £13.7 billion, 20%, to £82.1 billion. Excluding repos, customer deposits were up £14.3 billion, 3%, to £428.6 billion, reflecting growth in UK Corporate, £13.7 billion, International Banking, £5.4 billion, UK Retail, £7.0 billion, Ulster Bank, £1.7 billion and Wealth, £0.7 billion, together with exchange rate and other movements of £3.4 billion. This was partially offset by decreases in Markets, £7.8 billion, US Retail & Commercial, £3.8 billion and Non-Core, £6.0 billion.

Debt securities in issue were down £49.2 billion, 18%, to £218.4 billion. Excluding the RFS minority interest disposal, they declined £28.0 billion, 11%, to £218.4 billion. Reductions in the level of certificates of deposit and commercial paper in Markets were partially offset by a programme of new term issuances totalling £38.4 billion.

Subordinated liabilities decreased by £10.6 billion, 28% to £27.1 billion or £4.5 billion, 14% excluding the disposal of the RFS minority interest. This reflected the redemption of £2.6 billion undated loan capital, debt preference shares and trust preferred securities under the liability management exercise completed in May, together with the conversion of £0.8 billion US dollar and Sterling preference shares and the redemption of £1.6 billion of other dated and undated loan capital, which were partially offset by the effect of exchange rate movements and other adjustments of £0.5 billion.

The Group's non-controlling interests decreased by £15.2 billion, primarily reflecting the disposal of the RFS minority interest, £14.4 billion, the majority of the RBS Sempra Commodities JV business, £0.6 billion, and the life assurance business, £0.2 billion.

Owner's equity decreased by £2.6 billion, 3%, to £75.1 billion. This was driven by the partial redemption of preference shares and paid-in equity, £3.1 billion less related gains of £0.6 billion, the attributable loss for the period, £1.1 billion, together with an increase in own shares held of £0.7 billion and higher losses in available-for-sale reserves, £0.3 billion. Offsetting these reductions were the issue of £0.8 billion ordinary shares on conversion of US dollar and Sterling non-cumulative preference shares classified as debt and exchange rate and other movements, £1.2 billion.

Business review continued

Cash flow

	2011	2010	2009
	£m	£m	£m
Net cash flows from operating activities	3,325	19,291	(992)
Net cash flows from investing activities	14	3,351	54
Net cash flows from financing activities	(1,741)	(14,380)	18,791
Effects of exchange rate changes on cash and cash equivalents	(1,473)	82	(8,592)
Net increase in cash and cash equivalents	125	8,344	9,261

2011

The major factors contributing to the net cash inflow from operating activities of £3,325 million were the elimination of foreign exchange differences of £2,702 million, depreciation and amortisation of £1,875 million and inflow from other items of £2,900 million, partially offset by the net operating loss before tax of £708 million from continuing and discontinued operations and the decrease of £3,444 million in operating assets and liabilities.

Net cash inflows from investing activities of £14 million related to the net inflows from sales of securities of £3,074 million, and sale of property, plant and equipment of £1,840 million offset by net cash outflows from investments in business interests and intangible assets of £1,428 million and from the purchase of property, plant and equipment of £3,472 million.

Net cash outflows from financing activities of £1,741 million relate primarily to interest on subordinated liabilities of £714 million, repayment of subordinated liabilities of £627 million and redemption of non-controlling interests of £382 million.

2010

The major factors contributing to the net cash inflow from operating activities of £19,291 million were the increase of £17,095 million in operating assets less operating liabilities, depreciation and amortisation of £2,220 million and income taxes received of £565 million, partly offset by the net operating loss before tax of £940 million from continuing and discontinued operations.

Net cash flows from investing activities of £3,351 million relate to the net inflows from sales of securities of £4,119 million and investments in business interests and intangibles of £3,446 million. This was partially offset by the outflow of £4,112 million from investing activities of discontinued operations.

Net cash outflow from financing activities of £14,380 million primarily arose from the redemption of non-controlling interests of £5,282 million, dividends paid of £4,240 million, repayment of subordinated liabilities of £1,588 million and the redemption of preference shares of £2,359 million.

2009

The major factors contributing to the net cash outflow from operating activities of £992 million were the net operating loss before tax of £2,696 million from continuing and discontinued operations, the decrease of £15,964 million in operating liabilities less operating assets, partly offset by the elimination of foreign exchange differences of £12,217 million and other items of £5,451 million.

Net cash flows from investing activities of £54 million relate to the net sales and maturities of securities of £2,899 million and a net cash inflow of £105 million in respect of other acquisitions and disposals less the net cash outflow on disposals of property, plant and equipment of £2,950 million.

Net cash flows from financing activities of £18,791 million primarily arose from the capital raised from the issue of B shares of £25,101 million, the placing and open offer of £5,274 million and the issue of subordinated liabilities of £2,309 million. This was offset in part by the cash outflow on repayment of subordinated liabilities of £5,145 million, redemption of preference shares of £5,000 million, interest paid on subordinated liabilities of £1,746 million and dividends paid of £1,248 million.

Capital resources
The following table analyses the Group's regulatory capital resources on a fully consolidated basis at 31 December as monitored by the FSA for regulatory purposes.

	2011	2010	2009	2008	2007
	£m	£m	£m	£m	£m
Capital base					
Tier 1 capital	56,990	60,124	76,421	69,847	44,364
Tier 2 capital	8,546	9,897	15,389	32,223	33,693
Tier 3 capital	—	—	—	260	200
	65,536	70,021	91,810	102,330	78,257
Less: Supervisory deductions	(4,828)	(4,732)	(4,565)	(4,155)	(10,283)
Total regulatory capital	60,708	65,289	87,245	98,175	67,974
Risk-weighted assets (1)					
Credit risk	344,300	385,900	513,200	551,300	
Counterparty risk	61,900	68,100	56,500	61,100	
Market risk	64,000	80,000	65,000	46,500	
Operational risk	37,900	37,100	33,900	36,900	
	508,100	571,100	668,600	695,800	
Asset Protection Scheme relief	(69,100)	(105,600)	(127,600)	n/a	
	439,000	465,500	541,000	695,800	
Banking book:					
On-balance sheet					480,200
Off-balance sheet					84,600
Trading book					44,200
					609,000
Risk asset ratios	%	%	%	%	%
Core Tier 1	10.6	10.7	11.0	6.6	4.5
Tier 1	13.0	12.9	14.1	10.0	7.3
Total	13.8	14.0	16.1	14.1	11.2

Note:
(1) The data for 2008 onwards are on a Basel II basis; 2007 is on a Basel I basis.

It is the Group's policy to maintain a strong capital base, to expand it as appropriate and to utilise it efficiently throughout its activities to optimise the return to shareholders while maintaining a prudent relationship between the capital base and the underlying risks of the business. In carrying out this policy, the Group has regard to the supervisory requirements of the Financial Services Authority (FSA). The FSA uses Risk Asset Ratio (RAR) as a measure of capital adequacy in the UK banking sector, comparing a bank's capital resources with its risk-weighted assets (the assets and off-balance sheet exposures are 'weighted' to reflect the inherent credit and other risks); by international agreement, the RAR should be not less than 8% with a Tier 1 component of not less than 4%. At 31 December 2011, the Group's total RAR was 13.8% (2010 - 14.0%) and the Tier 1 RAR was 13.0% (2010 -12.9%). For further information refer to Balance sheet management: Capital management on pages 68 to 73.

Risk and balance sheet management

In this section (pages 58 to 207) of the Business review, certain information has been audited and is part of the Group's financial statements as permitted by IFRS 7. Other disclosures are unaudited and are labelled with an asterisk (*). In this section, the 2009 data relate to the Group before RFS Holdings minority interest (RFS MI).

Introduction*

All the disclosures in this section (pages 58 to 67) are unaudited as indicated by an asterisk (*).

Risk management plays an integral role in the delivery of the Group's strategic goal to be a safe and secure banking group. The implementation of a stronger and more effective culture of risk management and control provides the platform necessary to address historical vulnerabilities, rebuild upon the Group's core strengths and position it on a sustainable and profitable path for future growth.

Financial strength and resilience are at the heart of the Group's Strategic Plan. The Group has defined this level of robustness as that which is capable of achieving and sustaining a standalone credit rating (i.e. without government support) that is in line with those of its strongest international peers.

Given this central aim, in 2009 the Group Board set out four key strategic risk objectives, aligned to the Group's Strategic Plan. These are to:

- maintain capital adequacy: to ensure that the Group has sufficient (and easily accessible) capital resources to meet regulatory requirements and to cover the potential for unexpected losses in its asset portfolio;

- deliver stable earnings growth: to ensure that strategic growth is based around a longer-term risk versus reward consideration, with significantly lower volatility in underlying profitability than was seen over the previous five years;

- ensure stable and efficient access to funding and liquidity: such that the Group has sufficient funding to meet its obligations, taking account of the constraint that some forms of funding may not be available when they are most needed; and

- maintain stakeholder confidence: to ensure that stakeholders have confidence in the Group's recovery plan, its ability to deliver its strategic objectives and the effectiveness of its business culture and operational controls.

Each objective is essential in its own right, but also mutually supportive of the others.

These strategic risk objectives are the bridge between the Group-level business strategy and the frameworks, limits and tolerances that are used to set risk appetite and manage risk in the business divisions on a day-to-day basis.

In 2011, the Group made significant progress in strengthening its approach to risk management in an external environment that remained challenging.

The task of setting a comprehensive risk appetite and aligning it with the Group's business strategy demands a clear understanding of the types of risk the Group faces and their potential size. With this goal in mind, over the past year the Group has developed a catalogue of the risks it faces (a risk taxonomy) and undertaken a Group-wide material risk assessment to analyse the scale of each risk and the potential interactions between them (for a detailed discussion of risk appetite, see page 59).

The delivery of proactive and effective risk management relies on high quality data inputs on which to make assessments. It also requires robust forward-looking measurement and stress testing capabilities (see stress testing on page 60). Both of these areas continue to be enhanced and improvements embedded across the Group.

Risk control frameworks are used to identify and address concentrations of risk. These systems are reinforced by a Group Policy Framework (see page 60), which was enhanced during 2011, with assurance activity ongoing to ensure the policy standards it comprises remain appropriate.

Effective risk management also requires a robust governance framework. During 2011, the roles and responsibilities of the Executive Risk Forum and its supporting committees were reviewed and more clearly defined (see pages 62 to 64).

The Group has launched a common set of values for the risk community that impact directly on behaviours and help to engender a risk management function that is widely respected and valued across the Group. A Group-wide policy that explicitly aligns remuneration with effective risk management has also been put in place.

The focus is now on fully embedding the Group's strategy for risk management into the day-to-day management of its businesses, as well as preparing the Group to face future challenges in a rapidly evolving external environment. More detailed discussions on how the Group strengthened its approach to risk management in 2011 and the areas of focus going forward is contained within the relevant sub-sections on the following pages.

* unaudited

Risk appetite*

The Group's focus on setting a clear risk appetite and embedding a strong culture of risk management and control is designed to ensure it is able to proactively identify and reduce risk exposures and has the resilience to respond effectively to any unforeseen shocks.

The Group's risk appetite identifies and establishes the level and type of risks that it is able and willing to take in order to:

- meet its strategic objectives - this includes the Group's stated objective of achieving and sustaining a standalone credit rating in line with those of its strongest international peers; and

- meet its wider obligations to stakeholders - the Group's Strategic Plan is built on the core foundations of serving its customers well, acting responsibly and creating sustainable value for its shareholders.

A clear risk appetite provides a greater understanding across the Group of the acceptable levels of risk for each business. It provides a solid platform from which the Group can focus on its key business strengths and competitive advantages over the long-term.

Approach and key principles

The Strategic Plan set key performance indicators for capital, leverage, liquidity and funding, aligned with the Group's strategic objectives. It also established a Non-Core division to manage, dispose of and run-off assets that the Group was seeking to exit from, which by definition were outside its appetite.

Building on these core foundations, the Group has developed a framework that sets and implements an appropriate risk appetite for the Group (and its main businesses), supported by a regular monitoring and review process.

Under this framework, risk appetite targets - based on both the quantitative and qualitative aspects of risk - have been set by the Group Board, aligned with Group and divisional strategic objectives. These targets support and augment the strategic, financial and risk controls that are already in place and help to shape the way the Group operates at all levels. Clear roles and responsibilities are established to measure, cascade and report performance against risk appetite and to provide assurances that business is being conducted within approved risk limits and tolerances.

The development of this framework has been based on the following best practice principles:

- strong leadership from the Group Board in establishing and setting risk appetite and in ensuring its purpose is understood and its use promoted as good business practice;

- a strong risk management culture, in which risk is clearly and meaningfully aligned with business behaviours and outcomes;

- a close collaborative partnership between the risk, strategy, treasury and finance functions that facilitates a broader internal debate on key issues; and

- clear accountability by each division (and business unit) for the level of risk it is prepared to take to achieve its business objectives.

Group-wide stress testing is used to assess whether strategic plans are consistent with risk appetite and to measure the key drivers of risk (down to business unit level), with mitigating actions identified whenever the risk profile is considered to be outside (or close to) acceptable levels (see page 60).

Design to delivery

The Group's risk appetite has been set by the Group Board and is now operational. Significant progress has been made in establishing the underlying framework and rolling it out across the Group and its divisions.

The key channels through which risk appetite is cascaded throughout and embedded in each division are:

- divisional risk appetite statements - each division has developed its own risk appetite statement, which is based on the four strategic risk objectives and is appropriate for its business plans but also aligned with the Group's risk appetite targets;

- risk control frameworks and limits - risk control frameworks set clear guidance on acceptable limits and tolerances for all material risk types (e.g. credit, market and country risk), aligned with the Group's risk appetite targets;

- Group operational and conduct risk appetite - the Group has developed a robust control environment to ensure it conducts its activities in accordance with its regulatory and other obligations; and

- culture, values and remuneration - a programme of communication, engagement and training is being rolled out across the Group to engender a wide understanding of the purpose of risk appetite.

The Group regards the implementation of its risk appetite framework as an essential step in driving the cultural change required to achieve its strategic objectives and a dynamic, ongoing process. The Board Risk Committee (see the Report of the Board Risk Committee on pages 226 to 229) reviews both the targets and the framework on a regular basis, to ensure they remain aligned to strategic objectives, business performance, emerging risks and changes in the external environment.

* unaudited

Business review Risk and balance sheet management continued

Introduction*: Stress testing

Stress testing describes the evaluation of a bank's financial position under severe but plausible stress scenarios. Stress testing refers to the application of individual stress tests and the broader framework under which these tests are developed, evaluated and used within the Group's decision-making process in the context of the wider economic environment.

Internal stress tests

The Group's stress testing framework is designed to embed stress testing as a key risk management technique into mainstream risk reporting, capital planning and business processes at both Group and divisional levels.

The Executive Risk Forum (see Risk governance on page 61) is the main body overseeing the Group's stress testing approach, processes and results. The forum is primarily responsible for reviewing and challenging the results of any Group-wide stress test and ensuring that, where necessary, appropriate management actions are undertaken. The Board Risk Committee will provide oversight and challenge as appropriate.

Stress testing forms part of the Group's risk and capital management framework and is a major component of the Basel III requirements. It highlights to senior management potential adverse unexpected outcomes related to a mixture of risks and provides an indication of how much capital might be required to absorb losses should adverse scenarios materialise.

Stress testing is used at both divisional and Group levels to assess risk concentrations and estimate the impact of stressed earnings, impairments and write-downs on capital as well as the liquidity and funding position of the Group. It determines overall capital adequacy under a variety of adverse scenarios.

A series of stress events are monitored on a regular basis to assess the potential impact of a severe yet plausible event on the Group. There are four core types of scenario stress testing:

- macroeconomic stress testing, which considers the impact on both earnings and capital for a range of scenarios;
- enterprise-wide stress testing, which considers scenarios that are not macroeconomic in nature but are sufficiently broad to entail multiple risks or affect multiple divisions and are likely to affect earnings, capital and funding;
- cross-divisional stress testing, which includes scenarios that affect multiple divisions due to their sensitivity to a common risk factor; and
- divisional and risk-specific stress testing, which is undertaken to support risk identification and management.

Portfolio analysis, using historical performance and forward-looking indicators of change, uses stress testing to assess potential exposure to events and seeks to quantify the impact of an adverse change in factors that drive the performance and profitability of a portfolio.

Industry-wide stress tests

The Group takes part in a number of industry-wide stress tests, in particular, the European Banking Authority Stress Test and IMF UK Financial Sector Assessment Program, results of which were published in July 2011. These confirmed that the Group remains well capitalised with a strong Core Tier 1 capital ratio and a strong Total capital ratio under both baseline and adverse scenarios. During 2011, the Group also undertook the FSA anchor scenario test.

In December 2011, the European Banking Authority published the results of its recapitalisation exercise - a review of banks' actual capital positions on sovereign exposures - showing the Group had no overall capital shortfall after including the sovereign capital buffer.

Group Policy Framework*

Achieving and sustaining a robust control framework in line with those of the Group's strongest international peers is critical to achieving the successful delivery of the Group's risk objectives.

With this goal in mind, the Group Policy Framework (GPF) has been revised and broadened. The GPF consolidates a large number of individual policies under a consistent and structured overarching framework for conduct, control and governance. It provides clear guidance and controls on how the Group does business, linked to its risk appetite, its business conduct and compliance responsibilities and its focus on delivering a control environment consistent with best practice against relevant external benchmarks.

The GPF and related initiatives aim to ensure that:

- the Group has clear control standards and ethical principles to cover the risks that it faces to support effective risk management and meet regulatory and legal requirements;
- policies are followed across the Group and compliance can be clearly evidenced, assessed and reported by line management; and
- the control environment is monitored and overseen through good governance.

Communication and training programmes are provided to all relevant staff as the policies are embedded, ensuring that staff are aware of their responsibilities. The GPF is structured to ensure that policy standard owners and sponsors review their policies on a regular basis, with any identified shortfalls against industry best practice documented and addressed within an agreed time frame.

* unaudited

The GPF was introduced in 2009. Enhancements applied in 2011 included the following:

- the Group's policy standards, which comprise the GPF, were rewritten to ensure they clearly express the mandatory controls required to mitigate the key risks the Group faces;
- all of the Group's policy standards were benchmarked against relevant external reference points such as peer organisations to challenge and verify the content of the policy standards. Where identified, further improvements to the policy standards are now being implemented;
- for each policy standard, appropriate risk based assurance activity was introduced to ensure each division is appropriately controlled and compliance with policy can be demonstrated; and
- risk appetite has its own policy standard within the GPF that clearly sets out roles and responsibilities in relation to the implementation of the risk appetite framework and provides assurance that risks are being actively managed within approved levels and tolerances.

The GPF will continue to be improved and embedded. The results of assurance activity, monitoring and analysis of the internal and external environment will be used to reassess the policy standards on a regular basis.

Risk governance*

The Group is committed to the highest standards of corporate governance in every aspect of the business, including risk management. A key aspect of the Group Board's responsibility as the main decision making body at Group level is the setting of Group risk appetite to ensure that the levels of risk that the Group is willing to accept in the attainment of its strategic business and financial objectives are clearly understood.

To enable the Group Board to carry out its objectives, it has delegated authority to senior Board and executive committees, as required and appropriate. A number of key committees specifically consider risk across the Group, as set out in the diagram below.

Notes:

(1) The Capital and Stress Testing Committee is a sub-committee of the Group Asset and Liability Management Committee.

(2) The following specialist sub-committees report directly to the Group Risk Committee: Global Markets Risk Committee, Group Country Risk Committee, Group Models Committee, Group Credit Risk Committee and Operational Risk Executive Committee. In addition, Divisional Risk Committees report to the Group Risk Committee.

* unaudited

Business review Risk and balance sheet management continued

Introduction*: Risk governance continued
The key risk responsibilities of each of these committees as well as their membership are set out in the table below. Further information on the Group Board and Board Committees is available on page 210.

These committees are supported at a divisional level by a risk governance structure embedded in the business. These committees play a key role in ensuring that the Group's risk appetite is supported by effective risk management frameworks, limits and policies, together with clear accountabilities for approval, monitoring, oversight, reporting and escalation.

During 2011, the roles and responsibilities of the Executive Risk Forum and its supporting committees were reviewed and more clearly defined, to meet the future needs of the Group.

In particular, the Executive Risk Forum was repositioned as a strategic committee focusing on strategic level risks and issues, and retaining the approval authority for the most material risk limits and decisions. The Group Risk Committee was refocused to operate primarily as an oversight committee across risk types, concentrating particularly on thematic and emerging risks and issues.

The committees that sit below the Group Risk Committee were streamlined significantly, aligned more closely to key risk types and given clearer empowerment and accountability where required.

A Capital and Stress Testing Committee was created as a sub-committee of the Group Asset and Liability Management Committee to cover risk and capital matters.

The improvements made in 2011 provide further clarity of roles and responsibilities, as well as clear reporting lines and accountabilities. They promote clearer and timelier decision making and more effective risk management and oversight.

The role and remit of the Group committees is set out below. These committees are supported at a divisional level by a risk governance structure embedded in the business.

Board/Committee	Risk focus	Membership
Group Board	The Group Board ensures that the Group manages risk effectively through approving and monitoring the Group's risk appetite, considering Group stress scenarios and agreed mitigants and identifying longer-term strategic threats to the Group's business operations.	The Board of directors
Executive Committee	The Executive Committee considers recommendations on risk management matters referred by the Executive Risk Forum and/or Group Risk Committee, including recommendations on risk appetite, risk policies and risk	Group Chief Executive Group Finance Director Chief Administrative Officer Chief Executive Officers of divisions Head of Restructuring and Risk

	management strategies.	
Board Risk Committee	The Board Risk Committee provides oversight and advice to the Group Board on current and potential future risk exposures of the Group and future risk strategy, including determination of risk appetite and tolerance. It also provides a risk review of remuneration arrangements and provides advice to the Remuneration Committee. It operates under delegated authority from the Group Board.	At least three independent non-executive directors, one of whom is the Chairman of the Group Audit Committee.

* unaudited

Board/Committee	Risk focus	Membership
Group Audit Committee	The Group Audit Committee reviews accounting policies and practices, controls and procedures established by management for compliance with regulatory and financial reporting requirements and requirements of external regulations. It has responsibility for monitoring relationships with regulatory authorities. It operates under delegated authority from the Group Board.	At least three independent non-executive directors, at least one of whom is a financial expert as defined in the SEC rules under the US Exchange Act and one of whom is Chairman of the Board Risk Committee.
Group Remuneration Committee	The Group Remuneration Committee is responsible for the overview of the Group's policy on remuneration and receives advice from Risk Management and the Board Risk Committee to ensure that there is thorough risk input into incentive plan design and target setting as well as risk review of performance bonus pools and clawback. It operates under delegated authority from the Group Board.	At least three independent non-executive directors
Executive Risk Forum	The Executive Risk Forum operates as a committee of the Executive Committee with full authority to act on all risk and control matters across the Group. The Executive Risk Forum approves the most material limits and decisions above defined thresholds and delegates decisions below these thresholds to sub-committees and appropriate individuals.	Group Chief Executive Group Finance Director Chief Administrative Officer Chief Executive Officers of divisions Head of Restructuring and Risk Deputy Chief Risk Officer
Group Asset and Liability Management Committee	The Group Asset and Liability Management Committee (GALCO) is a sub-committee of the Executive Risk Forum and is responsible for identifying, managing and controlling Group balance sheet risks in executing its chosen business strategy.	Group Finance Director Group Treasurer Chief Executive Officers of divisions Head of Restructuring and Risk Key Group Finance function heads Global Head of Markets
Group Risk Committee	The Group Risk Committee is a sub-committee of the Executive Risk Forum. It is an oversight committee which reviews and challenges risks and limits across the functional areas and plays a key role exercising and demonstrating effective risk oversight across the Group.	Deputy Chief Risk Officer Divisional Chief Risk Officers Key Group Risk function heads

It reviews risks and issues on a thematic as well as a specific basis and focuses on forward-looking, emerging risks. It considers the overall risk profile across the Group and identifies any key issues for escalation to the Executive Risk Forum.

* unaudited

Business review Risk and balance sheet management continued

Introduction*: Risk governance continued

Board/Committee	Risk focus	Membership
Capital and Stress Testing Committee	The Capital and Stress Testing Committee is a sub-committee of the Group Asset and Liability Management Committee and focuses on the broad risk capital agenda, including risk appetite, capital usage, stress testing, Internal Capital Adequacy Assessment Process, capital planning, allocation and management, economic capital and prudential developments, including Basel oversight.	Group Finance Director Key Group Finance function heads Key Group Risk function heads
Executive Credit Group	The Executive Credit Group decides on requests for the extension of existing or new credit limits on behalf of the Group Board where the proposed aggregate facility limits are in excess of the credit approval authorities granted to individuals in divisions or in Group Risk Management, or where an appeal against a decline decision of the Group Chief Credit Officer (or delegates) or Group Chief Risk Officer is referred for final decision.	Group A members (1) Head of Restructuring and Risk Deputy Chief Risk Officer Group Chief Credit Officer/Chief Credit Officer N.V. Head of Global Restructuring Group Chief Risk Officer, Non-Core division/APS (alternate) Group B members (1) Group Chief Executive Group Finance Director Chief Executive officers of divisions (1) Decisions require input from at least one member from each of Group A and Group B.
Divisional Risk and Audit Committees	Divisional Risk and Audit Committees report to the Board Risk Committee and the Group Audit Committee on a quarterly basis. Their main responsibilities are to: · monitor the performance of the divisions relative to divisional and Group risk appetite; · review matters relative to accounting policies, internal control, financial reporting, internal audit, external audit and regulatory compliance as set out in their terms of reference; and	Members: at least three non-executive members who are executives of the Group who do not have executive responsibility in the relevant division. Attendees: at least two executives of the division, as appropriate. Representatives from finance, risk, internal audit and external audit. Members of the Board Risk Committee and Group Audit Committee also have the right to attend.

· assist on such other matters as may be referred to them by the relevant divisional Executive Committee, the Group Audit Committee or the Board Risk Committee.

* unaudited

Introduction*:Risk coverage

The main risk types faced by the Group are presented below, together with a summary of the key areas of focus and how the Group managed these risks in 2011.

Risk type	Definition	Features	How the Group managed risk and the focus in 2011
Capital, liquidity and funding risk	The risk that the Group has insufficient capital or is unable to meet its financial liabilities as they fall due.	Potential to disrupt the business model and stop normal functions of the Group. Potential to cause the Group to fail to meet the supervisory requirements of regulators. Significantly driven by credit risk losses.	The Group plans for and maintains an adequate amount and mix of capital consistent with its risk profile. This ensures that in any foreseeable scenario the Group holds minimum capital to meet the standards and requirements of investors, regulators and depositors. The amount of capital required is determined through risk assessments and stress testing. Active run-off of capital intensive assets in Non-Core and other risk mitigation left the Core Tier 1 ratio strong at 10.6%, despite a £21 billion uplift in RWAs from the implementation of CRD III in December 2011. Refer to pages 68 to 73. Maintaining the structural integrity of the Group's balance sheet requires active management of both asset and liability portfolios as necessary. Strong term debt issuance and planned reductions in the funded balance sheet enabled the Group to strengthen its liquidity and funding position as market conditions worsened. Refer to pages 74 to 88.
Credit risk (including counterparty risk)	The risk that the Group will incur losses owing to the failure of a customer to meet its obligation to settle outstanding amounts.	Loss characteristics vary materially across portfolios. Significant link between losses and the macroeconomic environment. Can include concentration risk - the risk of loss due to the concentration of credit risk to a specific product, asset class, sector or counterparty.	The Group manages credit risk based on a suite of credit approval and risk concentration frameworks and associated risk management systems and tools. It also continues to reduce the risk associated with legacy exposures through further reductions in Non-Core assets. During 2011, asset quality continued to improve, resulting in loan impairment charges 21% lower than in 2010 despite continuing challenges in Ulster Bank Group (Core and Non-Core) and corporate real estate portfolios. The Group continued to make progress in reducing key credit concentration risks, with credit exposures in excess of single name concentration limits

			declining 15% during the year and exposure to commercial real estate declining 14%. Refer to pages 92 to 165.
Country risk	The risk of material losses arising from significant country-specific events.	Can arise from sovereign events, economic events, political events, natural disasters or conflicts. Potential to affect parts of the Group's credit portfolio that are directly or indirectly linked to the country in question.	All country exposures are covered by the Group's country risk management framework. This includes active management of portfolios either when these have been identified as exhibiting signs of stress through the Group's country Watchlist process or when it is otherwise considered appropriate. Portfolio reviews are undertaken to align country risk profiles to the Group's country risk appetite in light of economic and political developments. Sovereign risk increased in 2011, resulting in rating downgrades for a number of countries, including several eurozone members. This resulted in an impairment charge recognised by the Group in 2011 in respect of available-for-sale Greek government bonds. In response, the Group further strengthened its country risk appetite setting and risk management systems during the year and brought a number of advanced countries under limit control. This contributed to a reduction in exposure to a range of countries. Refer to pages 166 to 186.

* unaudited

Business review Risk and balance sheet management continued

Introduction*: Risk coverage continued

Risk type	Definition	Features	How the Group managed risk and the focus in 2011
Market risk	The risk arising from changes in interest rates, foreign currency, credit spreads, equity prices and risk related factors such as market volatilities.	Frequent small losses which are material in aggregate. Infrequent large material losses due to stress events.	A comprehensive structure is in place aimed at ensuring the Group does not exceed its qualitative and quantitative tolerance for market risk. The Group's market risk policy statements set out its qualitative tolerance for market risk. They define the governance, responsibilities and requirements for the identification, measurement, analysis, management and communication of the market risk arising from the Group's trading and non-trading investment activities. The Group Market Risk limit framework expresses the Group's quantitative tolerance for market risk. The Group limit metrics capture, in broad terms, the full range of market risk exposures, ensuring the risk is appropriately defined and communicated. During 2011, the Group continued to manage down its market risk exposure in Non-Core and reduce the asset-backed securities trading inventory such that the trading portfolio became less exposed to credit risk. Refer to pages 187 to 193.
Insurance risk	The risk of financial loss through fluctuations in the timing, frequency and/or severity of insured events, relative to the expectations at the time of underwriting.	Frequent small losses which are material in aggregate. Infrequent large material losses.	The Group's framework for managing insurance risk, with associated risk appetite and policy frameworks, is designed to ensure insurance risks are appropriately identified, controlled, managed, monitored, reported and mitigated. Procedures are in place to address any issues, such as breaches of risk appetite that are identified through monitoring and reporting activities. If a breach occurs, an action plan to address the issue is developed, implemented and monitored to ensure the risk is adequately mitigated or a decision is taken to accept it.

			During 2011, focus on insurance risk appetite resulted in the de-risking and significant re-pricing of certain classes of business and exiting some altogether. Refer to page 194.
Operational risk	The risk of loss resulting from inadequate or failed processes, people, systems or from external events.	Frequent small losses. Infrequent material losses.	The objective of operational risk management is to manage it to an acceptable level. Processes to achieve this objective take into account the cost of minimising the risk against the resultant reduction in exposure. During 2011, the Group took steps to enhance its management of operational risks. This was particularly evident in respect of risk appetite, the Group Policy Framework, risk assessment, scenario analysis and statistical modelling for capital requirements. The level of operational risk remains high due to the scale of structural change occurring across the Group, the pace of regulatory change, the economic downturn and other external threats, such as e-crime. Refer to pages 194 to 197.

* unaudited

Risk type	Definition	Features	How the Group managed risk and the focus in 2011
Compliance risk	The risk arising from non-compliance with national and international laws, rules and regulations.	Adverse impacts on strategy, capital structure, business models and operational effectiveness. Financial cost of adapting to changes in laws, rules or regulations or of penalties for non-compliance.	Management of compliance risk entails early identification and effective management of changes in legislative, regulatory and other requirements that may affect the Group. It also requires active engagement with regulators, close analysis of emerging regulatory themes, and interaction with rule-makers and legislators. Within the GPF, compliance risk policies define minimum standards to which all businesses must adhere. GPF policies are supplemented, where appropriate, by divisional policies to meet local product or market requirements. During 2011, the Group managed the increased levels of scrutiny and legislation by enlarging the capacity of its compliance, anti-money laundering and regulatory affairs teams and taking steps to improve its operating models, tools, systems and processes. Refer to pages 197 to 202.
Reputational risk	The risk of brand damage arising from financial and non-financial events arising from the failure to meet stakeholders' expectations of the Group's performance and behaviour.	Potential to put the entire business at risk. Otherwise, could lead to negative publicity, loss of revenue, costly litigation or a decline in customer base. Can arise from actions taken by the Group or a failure to take action.	The Group Sustainability Committee and risk committees continue to assess reputational risk issues. In 2011, an Environmental, Social and Ethical (ESE) Risk Policy was developed with sector ESE risk appetite positions drawn up to assess the Group's appetite to support customers in sensitive sectors including defence, oil and gas. This also included the establishment of divisional reputational risk committees. Stakeholder engagement was broadened with the implementation of formal sessions between the Group Sustainability Committee and relevant advocacy groups and non-governmental organisations. Refer to page 202.
Business risk	The risk of lower-than-expected revenues and/or	Influenced by many factors such as pricing, sales volume,	Forecasts of revenues and costs are tested against a range of stress scenarios to identify key risk drivers and the

	higher-than-expected operating costs.	input costs, regulations and market and economic conditions.	appropriate actions to address and manage them. Business risk is incorporated within the Group's risk appetite target for earnings volatility that was set in 2011. Refer to page 202.
Pension risk	The risk that the Group will have to make additional contributions to its defined benefit pension schemes.	Funding position can be volatile due to the uncertainty of future investment returns and the projected value of schemes' liabilities.	The Group manages pension risk from a sponsor perspective using a framework that encompasses risk reporting and monitoring, stress testing, modelling and an associated governance structure that helps ensure the Group is able to fulfil its obligation to support the defined benefit pension schemes to which it has exposure. In 2011, the Group focused on improved stress testing and risk governance mechanisms. This included the establishment of the Pension Risk Committee and the articulation of its view of risk appetite for the various Group pension schemes. Refer to pages 203 and 204.

Each risk type maps into the Group's risk appetite framework and contributes to the overall achievement of its strategic objectives with underlying frameworks and limits. The key frameworks and developments over the past year are described in the relevant sections of the following pages.

* unaudited

Balance sheet management

All disclosures in this section (pages 68 to 91) are audited unless otherwise indicated by an asterisk (*).

Two of the Group's four key strategic risk objectives relate to the maintenance of capital adequacy and ensuring stable and efficient access to liquidity and funding. This section on balance sheet management explains how the Group is performing on achieving these objectives.

Capital management

Introduction*

The Group aims to maintain an appropriate level of capital to meet its business needs and regulatory requirements as capital adequacy and risk management are closely aligned. The Group operates within an agreed risk appetite whilst optimising the use of shareholders' funds to deliver sustainable returns.

The appropriate level of capital is determined based on the dual aims of: (i) meeting minimum regulatory capital requirements; and (ii) ensuring the Group maintains sufficient capital to uphold investor and rating agency confidence in the organisation, thereby supporting the business franchise and funding capacity.

Governance*

The Group Asset and Liability Management Committee (GALCO) is responsible for ensuring the Group maintains adequate capital at all times. The newly established Capital and Stress Testing Committee (CAST) is a cross-functional body driving and directing integrated risk capital activities including stress testing economic capital and capital allocation. These activities have linkages to capital planning, risk appetite and regulatory change. CAST reports through GALCO and comprises senior representatives from Risk Management, Group Finance and Group Treasury.

Determining appropriate capital*

The minimum regulatory capital requirements are identified by the Group through the Internal Capital Adequacy Assessment Process and then agreed between the Group Board and the appropriate supervisory authority.

The Group's own determination of how much capital is sufficient is derived from the desired credit rating level and the application of both internally and externally defined stress tests that identify potential changes in capital ratios over time.

Monitoring and maintenance*

Based on these determinations, which are continually reassessed, the Group aims to maintain capital adequacy both at Group level and in each regulated entity.

The Group operates a rigorous capital planning process aimed at ensuring the capital position is controlled within the agreed parameters. This incorporates regular re-forecasts of the capital positions of the regulated entities and the overall Group. In the event that the projected position deteriorates beyond acceptable levels, the Group would issue further capital and/or revise business plans accordingly.

Stress testing approaches are used to determine the level of capital required to ensure the Group remains adequately capitalised.

Capital allocation*

Capital resources are allocated to the Group's businesses based on key performance parameters agreed by the Group Board in the annual strategic planning process. Principal among these is a profitability metric which assesses the effective use of the capital allocated to the business. Projected and actual return on equity is assessed against target returns set by the Group Board. The allocations also reflect strategic priorities and balance sheet and funding metrics.

Economic profit is also planned and measured for each division during the annual planning process. It is calculated by deducting the cost of equity utilised in the particular business from its operating profit and measures the value added over and above the cost of equity.

The Group aims to deliver sustainable returns across the portfolio of businesses with projected business returns stressed to test key vulnerabilities.

The divisions use return on capital metrics when making pricing decisions on products and transactions with a view to ensuring customer activity is appropriately aligned with Group and divisional targets and allocations.

The FSA uses the risk asset ratio as a measure of capital adequacy in the UK banking sector, comparing a bank's capital resources with its RWAs (the assets and off-balance sheet exposures are weighted to reflect the inherent credit and other risks); by international agreement the risk asset ratios should not be less than 8% with a Tier 1 component of not less than 4%.

* unaudited

Capital adequacy*

The Group's RWAs and risk asset ratios, calculated in accordance with FSA definitions, are set out below.

	Statutory			Proportional
	2011	2010	2009	2009
Risk-weighted assets by risk	£bn	£bn	£bn	£bn
Credit risk	344.3	385.9	513.2	410.4
Counterparty risk	61.9	68.1	56.5	56.5
Market risk	64.0	80.0	65.0	65.0
Operational risk	37.9	37.1	33.9	33.9
	508.1	571.1	668.6	565.8
Asset Protection Scheme relief	(69.1)	(105.6)	(127.6)	(127.6)
	439.0	465.5	541.0	438.2
Risk asset ratios	%	%	%	%
Core Tier 1	10.6	10.7	11.0	11.0
Tier 1	13.0	12.9	14.1	14.4
Total	13.8	14.0	16.1	16.3

Key points*

- Market risk RWAs were impacted by the new CRD III rules but decreased overall by £16 billion in 2011 reflecting de-risking of Non-Core and a reduction in trading VaR.

- APS relief decreased by £36.5 billion, reflecting pool movements, assets moving into default and changes in risk parameters.

Pillar 3*

The Group publishes its Pillar 3 Disclosures on its website, providing a range of additional information relating to Basel II and risk and capital management across the Group. The disclosures focus on capital resources and adequacy and discuss a range of credit risk measures and management methods (such as credit risk mitigation, counterparty credit risk and provisions) and their associated RWAs under the various Basel II approaches. Detailed disclosures are also made on equity exposures, securitisations, operational risk, market risk and interest rate risk in the banking book.

* unaudited

Business review Risk and balance sheet management continued

Balance sheet management: Capital management continued

Capital resources

The Group's regulatory capital resources in accordance with FSA definitions were as follows:

	Statutory			Proportional*
	2011	2010	2009	2009
Shareholders' equity (excluding non-controlling interests)	£m	£m	£m	£m
Shareholders' equity per balance sheet	74,819	75,132	77,736	77,736
Preference shares - equity	(4,313)	(4,313)	(7,281)	(7,281)
Other equity instruments	(431)	(431)	(565)	(565)
	70,075	70,388	69,890	69,890
Non-controlling interests				
Non-controlling interests per balance sheet	1,234	1,719	16,895	2,227
Non-controlling preference shares	(548)	(548)	(656)	(656)
Other adjustments to non-controlling interests for regulatory purposes	(259)	(259)	(497)	(497)
	427	912	15,742	1,074
Regulatory adjustments and deductions				
Own credit	(2,634)	(1,182)	(1,057)	(1,057)
Unrealised losses on AFS debt securities	1,065	2,061	1,888	1,888
Unrealised gains on AFS equity shares	(108)	(25)	(134)	(134)
Cash flow hedging reserve	(879)	140	252	252
Other adjustments for regulatory purposes	571	204	(193)	41
Goodwill and other intangible assets	(14,858)	(14,448)	(17,847)	(14,786)
50% excess of expected losses over impairment provisions (net of tax)	(2,536)	(1,900)	(2,558)	(2,558)
50% of securitisation positions	(2,019)	(2,321)	(1,353)	(1,353)
50% of APS first loss	(2,763)	(4,225)	(5,106)	(5,106)
	(24,161)	(21,696)	(26,108)	(22,813)
Core Tier 1 capital	46,341	49,604	59,524	48,151
Other Tier 1 capital				
Preference shares - equity	4,313	4,313	7,281	7,281
Preference shares - debt	1,094	1,097	3,984	3,984
Innovative/hybrid Tier 1 securities	4,667	4,662	5,213	2,772
	10,074	10,072	16,478	14,037
Tier 1 deductions				
50% of material holdings	(340)	(310)	(601)	(310)
Tax on excess of expected losses over impairment provisions	915	758	1,020	1,020
	575	448	419	710
Total Tier 1 capital	56,990	60,124	76,421	62,898

* unaudited

	Statutory			Proportional*
	2011	2010	2009	2009
Qualifying Tier 2 capital	£m	£m	£m	£m
Undated subordinated debt	1,838	1,852	4,950	4,200
Dated subordinated debt - net of amortisation	14,527	16,745	20,063	18,120
Reserves arising on revaluation of property	—	—	73	73
Unrealised gains on AFS equity shares	108	25	134	134
Collectively assessed impairment provisions	635	778	796	796
Non-controlling Tier 2 capital	11	11	11	11
	17,119	19,411	26,027	23,334
Tier 2 deductions				
50% of securitisation positions	(2,019)	(2,321)	(1,353)	(1,353)
50% excess of expected losses over impairment provisions	(3,451)	(2,658)	(3,578)	(3,578)
50% of material holdings	(340)	(310)	(601)	(310)
50% of APS first loss	(2,763)	(4,225)	(5,106)	(5,106)
	(8,573)	(9,514)	(10,638)	(10,347)
Total Tier 2 capital	8,546	9,897	15,389	12,987
Supervisory deductions				
Unconsolidated investments				
- Direct Line Group	(4,354)	(3,962)	(4,068)	(4,068)
- Other investments	(239)	(318)	(404)	(404)
Other deductions	(235)	(452)	(93)	(93)
	(4,828)	(4,732)	(4,565)	(4,565)
Total regulatory capital (1)	60,708	65,289	87,245	71,320

	2011
Movement in Core Tier 1 capital	£m
At beginning of the year	49,604
Attributable loss net of movements in fair value of own debt	(3,449)
Foreign currency reserves	(363)
Decrease in non-controlling interests	(485)
Decrease in capital deductions including APS first loss	1,128
Other movements	(94)
At end of the year	46,341

Note:

(1) Total capital includes certain instruments issued by RBS N.V. Group that are treated consistent with the local implementation of the Capital Requirements Directive (including the transitional provisions of that Directive). The FSA formally confirmed this treatment in 2012.

* unaudited

Business review Risk and balance sheet management continued

Balance sheet management: Capital management continued
Risk-weighted assets by division*
Risk-weighted assets by risk category and division are set out below:

2011	Credit risk £bn	Counterparty risk £bn	Market risk £bn	Operational risk £bn	Gross RWAs £bn
UK Retail	41.1	-	-	7.3	48.4
UK Corporate	71.2	-	-	8.1	79.3
Wealth	10.9	-	0.1	1.9	12.9
International Banking	38.9	-	-	4.3	43.2
Ulster Bank	33.6	0.6	0.3	1.8	36.3
US Retail & Commercial	53.6	1.0	-	4.7	59.3
Retail & Commercial	249.3	1.6	0.4	28.1	279.4
Markets	16.7	39.9	50.6	13.1	120.3
Other	9.8	0.2	-	2.0	12.0
Core	275.8	41.7	51.0	43.2	411.7
Non-Core	65.6	20.2	13.0	(5.5)	93.3
Group before RFS MI	341.4	61.9	64.0	37.7	505.0
RFS MI	2.9	-	-	0.2	3.1
Group	344.3	61.9	64.0	37.9	508.1
APS relief	(59.6)	(9.5)	-	-	(69.1)
Net RWAs	284.7	52.4	64.0	37.9	439.0
2010					
UK Retail	41.7	-	-	7.1	48.8
UK Corporate	76.4	-	-	7.8	84.2
Wealth	10.4	-	0.1	2.0	12.5
International Banking	44.0	-	-	7.7	51.7
Ulster Bank	29.2	0.5	0.1	1.8	31.6
US Retail & Commercial	52.1	0.9	-	4.4	57.4
Retail & Commercial	253.8	1.4	0.2	30.8	286.2
Markets	21.5	34.5	44.7	9.6	110.3
Other	16.4	0.3	0.2	1.0	18.0
Core	291.7	36.3	45.1	41.4	414.5
Non-Core	91.3	31.8	34.9	(4.3)	153.7
Group before RFS MI	383.0	68.1	80.0	37.1	568.2
RFS MI	2.9	-	-	-	2.9
Group	385.9	68.1	80.0	37.1	571.1
APS relief	(88.2)	(17.4)	-	-	(105.6)
Net RWAs	297.7	50.7	80.0	37.1	465.5

Asset Protection Scheme*
The Group acceded to the Asset Protection Scheme (APS or ‘the Scheme’) in December 2009.

Following the accession to the APS, HM Treasury provides loss protection against potential losses arising in a pool of assets. HM Treasury also subscribed to £25.5 billion of capital in the form of B shares and a Dividend Access Share, with a further £8 billion of capital in the form of B shares potentially available as contingent capital. The Group pays fees in respect of the protection and contingent capital. The Group has the option, subject to HM Treasury consent, to pay the premium, contingent capital and the exit fee payable in connection with any termination of the Group's participation in the APS in whole or in part, by waiving the entitlements of members of the Group to certain UK tax reliefs.

Following accession to the APS, arrangements were put in place within the Group that extended effective APS protection to all other regulated entities holding assets covered by the APS.

* unaudited

Regulatory capital impact of the APS*

Methodology

The regulatory capital requirements for assets covered by the Scheme are calculated using the securitisation framework under the FSA prudential rules. The calculation is as follows (the output is known as 'the uncapped amount'):

- First loss - the residual first loss, after impairments and write-downs, to date, is deducted from available capital split equally between Core Tier 1 and Tier 2 capital;
- HM Treasury share of covered losses - after the first loss has been deducted, 90% of assets covered by HM Treasury are risk-weighted at nil; and
- RBS share of covered losses - the remaining 10% share of loss is borne by RBS and is risk-weighted in the normal way.

Should the uncapped amount be higher than the capital requirements for the underlying assets calculated as normal, ignoring the Scheme, the capital requirements for the Scheme are capped at the level of the requirements for the underlying assets ('capped amount'). Where capped, the Group apportions the capped amount up to the level of the first loss as calculated above; any unused capped amount after the first loss capital deduction will be taken as RWAs for the Group's share of covered losses.

Adjustments to the regulatory capital calculation can be made for either currency or maturity mismatches. These occur where there is a difference between the currency or maturity of the protection and that of the underlying asset. These mismatches will have an impact upon the timing of the removal of the cap and level of regulatory capital benefit on the uncapped amount, but this effect is not material.

Impact

The Group calculates its capital requirements in accordance with the capped basis. Accordingly, the APS has no impact on the Pillar 1 regulatory capital requirement in respect of the assets covered by the APS. It does, however, improve the Core Tier 1 capital ratio of the Group. The protection afforded by the APS assists the Group in satisfying the forward-looking stress testing framework applied by the FSA.

Future regulatory capital effects

As impairments or write-downs on the pool of assets are recognised, they reduce Core Tier 1 capital in the normal way. This will reduce the first loss deduction for the Scheme, potentially leading to a position where the capital requirement on the uncapped basis would no longer, for the assets covered by the APS, exceed the non-APS requirement and as a result, the Group would expect to start reporting the regulatory capital treatment on the uncapped basis.

For further information on the assets covered by APS see pages 205 to 207.

Basel III*

The rules issued by the Basel Committee on Banking Supervision (BCBS), commonly referred to as Basel III, are a comprehensive set of reforms designed to strengthen the regulation, supervision, risk and liquidity management of the banking sector. In the EU they will be enacted through a revised Capital Requirements Directive referred to as CRD IV.

In December 2010, the BCBS issued the final text of the Basel III rules, providing details of the global standards agreed by the Group of Governors and Heads of Supervision, the oversight body of the BCBS and endorsed by the G20 leaders at their November 2010 Seoul summit. There are transition arrangements proposed for implementing these new standards as follows:

- National implementation of increased capital requirements will begin on 1 January 2013;
- There will be a phased five year implementation of new deductions and regulatory adjustments to Core Tier 1 capital commencing on 1 January 2014;
- The de-recognition of non-qualifying non-common Tier 1 and Tier 2 capital instruments will be phased in over 10 years from 1 January 2013; and
- Requirements for changes to minimum capital ratios, including conservation and countercyclical buffers, as well as additional requirements for Global Systemically Important Banks, will be phased in from 2013 to 2019.

The Group, in conjunction with the FSA, regularly evaluates its models for the assessment of RWAs ascribed to credit risk across various classes. This, together with the changes introduced by CRD IV relating primarily to counterparty risk, is expected to increase RWA requirements by the end of 2013 by £50 billion to £65 billion. These estimates are still subject to change; a degree of uncertainty remains around implementation details as the guidelines are not finalised and must still be enacted into EU law. There could be other future changes and associated impacts from these model reviews.

Other regulatory capital changes*

The Group is in the process of implementing changes to the RWA requirements for commercial real estate portfolios consistent with revised industry guidance from the FSA. This is projected to increase RWA requirements by circa £20 billion by the end of 2013, of which circa £10 billion will apply in 2012.

The Group is managing the changes to capital requirements from new regulation and model changes and the resulting impact on the common equity Tier 1 ratio, focusing on risk reduction and deleveraging. This is principally being achieved through the continued run-off and disposal of Non-Core assets and deleveraging in Markets as the business focuses on the most productive returns on capital.

The major categories of new deductions and regulatory adjustments which are being phased in over a five year period from 1 January 2014 include:

- Expected loss net of provisions;
- Deferred tax assets not relating to timing differences;
- Unrealised losses on available-for-sale securities; and
- Significant investments in non-consolidated financial institutions.

The net impact of these changes is expected to be manageable as the aggregation of these drivers is projected to be lower by 2014 and declining during the phase-in period.

* unaudited

Balance sheet management: Liquidity and funding risk
All disclosures in this section (pages 74 to 91) are audited unless otherwise indicated with an asterisk (*).

Liquidity risk
Liquidity risk is the risk that the Group is unable to meet its obligations, including financing maturities as they fall due. Liquidity risk is heavily influenced by the maturity profile and mix of the Group's funding base, as well as the quality and liquidity value of its liquidity portfolio.

Liquidity risk is dynamic, being influenced by movements in markets and perceptions that are driven by firm specific or external factors. Managing liquidity risk effectively is a key component of the Group's risk reduction strategy. The Group's 2011 performance demonstrates continued improvements in managing liquidity risk and reflects actions taken in light of an uncertain economic outlook, which resulted in improvements in key measures:

- Deposit growth - Core Retail & Commercial deposits increased, and together with Non-Core deleveraging, took the Group loan:deposit ratio to 108%, compared with 118% at the end of 2010.

- Wholesale funding - £21 billion of net term wholesale debt was issued in 2011 from secured and unsecured funding programmes, across a variety of maturities and currencies.

- Short-term wholesale funding (STWF) - the overall level of STWF fell by £27 billion to £102 billion, below the 2013 target of circa £125 billion.

- Liquidity portfolio - the liquidity portfolio of £155 billion was maintained above the 2013 target level of £150 billion against a backdrop of heightened market uncertainty in the second half of the year and was higher than STWF. This represents a £53 billion cushion over STWF.

Funding issuance
The Group has access to a variety of funding sources across the globe, including short-term money markets, repurchase agreement markets and term debt investors through its secured and unsecured funding programmes. Diversity in funding is provided by its active role in the money markets, along with access to global capital flows through its international client base. The Group's wholesale funding franchise is well diversified by currency, geography, maturity and type.

The Group has been a regular issuer in the debt capital markets in both secured and unsecured arrangements. 2011 net new term debt issuance was £21 billion, with 49% secured and 51% unsecured, of which 71% were public transactions and 29% were private.

Balance sheet composition
The Group's balance sheet composition is a function of the broad array of product offerings and diverse markets served by its Core divisions. The structural composition of the balance sheet is augmented as needed through active management of both asset and liability portfolios. The objective of these activities is to optimise liquidity transformation in normal business environments, while ensuring adequate coverage of all cash requirements under extreme stress conditions.

Diversification of the Group's funding base is central to its balance sheet management strategy. The Group's businesses have developed large customer franchises based on strong relationship management and high quality service. These customer franchises are strongest in the UK, the US and Ireland, but extend into Europe and Asia. Customer deposits provide large pools of stable funding to support the majority of the Group's lending. Improvement of the Group's loan:deposit ratio to 100% or better, by 2013, is a strategic objective.

The Group also accesses professional markets funding by way of public and private debt issuances on an unsecured and secured basis. These debt issuance programmes are spread across multiple currencies and maturities, to appeal to a broad range of investor types and preferences around the world. This market-based funding supplements the Group's structural liquidity needs and, in some cases, achieves certain capital objectives.

Stress testing
The strength of a bank's liquidity risk management can only be evaluated based on its ability to survive under stress. The Group evaluates the survivability of the major legal entities and legal entity groups when subjected to simulated stress conditions.

Simulated liquidity stress testing is periodically performed for each business as well as the major operating subsidiaries. A variety of firm-specific and market-related scenarios are used at the consolidated level and in individual countries. These scenarios include assumptions about significant changes in key funding sources, credit ratings, contingent uses of funding, and political and economic conditions in certain countries.

The Group's actual experiences from the 2008 and 2009 period factor heavily into the liquidity analysis. This systemic and name-specific crisis provides important data points in estimating stress severity.

Stress scenarios are applied to both on-balance sheet and off-balance sheet commitments, to provide a comprehensive view of potential cash flows.

Contingency planning
The Group has a Contingency Funding Plan (CFP), which is updated as the balance sheet evolves. The CFP is linked to stress test results and forms the foundation for liquidity risk limits. Limits in the business-as-usual environment are bounded by capacity to satisfy the Group's liquidity needs in the stress environments. The CFP provides a detailed description of the availability, size and timing of all sources of contingent liquidity available to the Group in a stress event. These are ranked in order of economic impact and effectiveness to meet the anticipated stress requirement. The CFP includes documented procedures and sign-offs for actions that may require businesses to provide access to customer assets for collateralised borrowing, securitisation or sale. Roles and responsibilities for the effective implementation of the CFP are also documented.

Liquidity reserves
The Group maintains liquidity reserves sufficient to satisfy cash requirements, in the event of a severe disruption in its access to funding sources. The reserves consist of cash held on deposit at central banks, high quality unencumbered government securities and other unencumbered collateral. Government securities vary by type and jurisdiction based on local regulatory considerations. The currency mix of the reserves reflects the underlying balance sheet composition.

Regulatory oversight
The Group operates in multiple jurisdictions and is subject to a number of regulatory regimes.

The Group's lead regulator is the UK Financial Services Authority (FSA). The FSA implemented a new liquidity regime on 1 June 2010. The new rules provide a standardised approach applied to all UK banks. At RBS Group, the rules focus on the UK Defined Liquidity Group (a subset comprising the Group's five UK banks, The Royal Bank of Scotland plc, National Westminster Bank Plc, Ulster Bank Limited, Coutts & Co and Adam & Co) and cover adequacy of liquidity resources, controls, stress testing and the Individual Liquidity Adequacy Assessment (ILAA). The ILAA informs the Group Board and the FSA of the assessment and quantification of the Group's liquidity risks and their mitigation, and how much current and future liquidity is required.

In the US, the Group's operations must meet liquidity requirements set out by the US Federal Reserve Bank, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation and the Financial Industry Regulatory Authority. In the Netherlands, the Group is subject to the De Nederlandsche Bank liquidity oversight regime.

Regulatory developments*
There have been a number of significant developments in the regulation of liquidity risk.

In December 2010, the Basel Committee on Banking Supervision issued the 'International framework for liquidity risk measurement, standards and monitoring' which confirmed the introduction of two liquidity ratios: the liquidity coverage ratio (LCR) and the net stable funding ratio (NSFR).

The introduction of both of these ratios will be subject to an observation period, which includes review clauses to identify and address any unintended consequences.

After an observation period beginning in 2011, the LCR, including any revisions, will be introduced on 1 January 2015. The NSFR, including any revisions, will move to a minimum standard by 1 January 2018.

* unaudited

Business review Risk and balance sheet management continued

Balance sheet management: Liquidity and funding risk continued

Funding sources

The table below shows the Group's primary funding sources including deposits in disposal groups and excluding repurchase agreements.

	2011		2010		2009	
	£m	%	£m	%	£m	%
Deposits by banks						
- central banks	3,680	0.5	6,655	0.9	8,535	1.0
- derivative cash collateral	31,807	4.6	28,074	3.8	32,552	4.0
- other	33,627	4.8	31,588	4.3	75,173	9.2
	69,114	9.9	66,317	9.0	116,260	14.2
Debt securities in issue						
- conduit asset backed commercial paper (ABCP)	11,164	1.6	17,320	2.3	25,583	3.1
- other commercial paper (CP)	5,310	0.8	8,915	1.2	18,724	2.3
- certificates of deposit (CDs)	16,367	2.4	37,855	5.1	58,195	7.1
- medium-term notes (MTNs)	105,709	15.2	131,026	17.6	125,800	15.4
- covered bonds	9,107	1.3	4,100	0.6	—	—
- securitisations	14,964	2.1	19,156	2.6	18,027	2.2
	162,621	23.4	218,372	29.4	246,329	30.1
Subordinated liabilities	26,319	3.8	27,053	3.6	31,538	3.9
Notes issued	188,940	27.2	245,425	33.0	277,867	34.0
Wholesale funding	258,054	37.1	311,742	42.0	394,127	48.2
Customer deposits						
- cash collateral	9,242	1.4	10,433	1.4	9,934	1.2
- other	427,511	61.5	420,433	56.6	413,224	50.6
Total customer deposits	436,753	62.9	430,866	58.0	423,158	51.8
Total funding	694,807	100.0	742,608	100.0	817,285	100.0
Disposal group deposits included above						
- banks	1		266		618	
- customers	22,610		2,267		8,907	
	22,611		2,533		9,525	

	2011	2010	2009
Short-term wholesale funding	£bn	£bn	£bn
Deposits	32.9	34.7	77.3
Notes issued	69.5	95.0	139.0
STWF excluding derivative collateral	102.4	129.7	216.3
Derivative collateral	31.8	28.1	32.6
STWF including derivative collateral	134.2	157.8	248.9
Interbank funding excluding derivative collateral			
- bank deposits	37.3	38.2	83.7

- bank loans	(24.3)	(31.3)	(31.3)
Net interbank funding	13.0	6.9	52.4

Key points

- Short-term wholesale funding excluding derivative collateral declined £27.3 billion in 2011, from £129.7 billion to £102.4 billion. This is £52.9 billion lower than the Group's liquidity portfolio. Deleveraging in Non-Core and Markets has led to the reduced need for funding.

- The Group's customer deposits excluding cash collateral grew by approximately £7.1 billion in 2011.

The table below shows the Group’s debt securities in issue and subordinated liabilities by remaining maturity.

	Debt securities in issue								
	Conduit ABCP	Other CP and CDs	MTNs	Covered bonds	Securitisations	Total	Subordinated liabilities	Total notes issued	Total notes issued
2011	£m	£m	£m	£m	£m	£m	£m	£m	%
Less than 1 year	11,164	21,396	36,302	—	27	68,889	624	69,513	36.8
1-3 years	—	278	26,595	2,760	479	30,112	3,338	33,450	17.7
3-5 years	—	2	16,627	3,673	—	20,302	7,232	27,534	14.6
More than 5 years	—	1	26,185	2,674	14,458	43,318	15,125	58,443	30.9
	11,164	21,677	105,709	9,107	14,964	162,621	26,319	188,940	100.0
2010									
Less than 1 year	17,320	46,051	30,589	—	88	94,048	964	95,012	38.7
1-3 years	—	702	47,357	1,078	12	49,149	754	49,903	20.3
3-5 years	—	12	21,466	1,294	34	22,806	8,476	31,282	12.8
More than 5 years	—	5	31,614	1,728	19,022	52,369	16,859	69,228	28.2
	17,320	46,770	131,026	4,100	19,156	218,372	27,053	245,425	100.0
2009									
Less than 1 year	25,583	76,008	33,696	—	1,614	136,901	2,144	139,045	50.0
1-5 years	—	895	69,400	—	142	70,437	4,235	74,672	26.9
More than 5 years	—	16	22,704	—	16,271	38,991	25,159	64,150	23.1
	25,583	76,919	125,800	—	18,027	246,329	31,538	277,867	100.0

Key point

- Debt securities in issue with a maturity of less than one year declined £25.1 billion from £94.0 billion at 31 December 2010 to £68.9 billion at 31 December 2011, largely due to the maturity of £20.1 billion of notes issued under the UK Government’s Credit Guarantee Scheme (CGS). The remaining notes issued under the CGS are due to mature in 2012, £15.6 billion in the first quarter of the year and £5.7 billion in the second quarter.

Short-term borrowings*

Short-term borrowings comprise repurchase agreements, borrowings from financial institutions, commercial paper and certificates of deposit. Derivative collateral received from financial institutions is excluded from the table below, as are certain long-term borrowings.

The table below shows details of the Group’s short-term borrowings.

	Repurchase agreements	Financial institutions (1,2)	CP	CDs	2011 Total	Repurchase agreements	Financial institutions (1,2)	CP	CDs	2010 Total	2009 Total
At year end											
- balance (£bn)	129	93	16	16	254	115	92	26	38	271	242
- weighted average interest rate	0.6%	0.9%	0.9%	1.4%	0.8%	0.5%	0.6%	0.7%	0.6%	0.6%	0.8%

During the year

- maximum balance (£bn)	175	111	32	39	357	157	127	37	57	378	357
- average balance (£bn)	142	93	22	31	288	137	109	34	50	330	292
- weighted average interest rate	0.9%	1.1%	0.7%	1.2%	1.0%	0.6%	0.8%	0.9%	1.0%	0.7%	1.9%

Notes:

(1) Excludes derivative cash collateral of £41 billion at 31 December 2011 (2010 - £38 billion; 2009 - £33 billion), 2011 average of £35 billion (2010 - £34 billion; 2009 - £40 billion).

(2) Excludes Federal Home Loan Bank's long-term borrowings of £1 billion at 31 December 2011 (2010 - £1 billion), 2011 average of £1 billion (2010 - £1 billion).

Balances are generally based on monthly data. Average interest rates during the year are computed by dividing total interest expense by the average amount borrowed. Average interest rates at year end are average rates for a single day and as such may reflect one-day market distortions, which may not be indicative of generally prevailing rates.

* unaudited

Business review Risk and balance sheet management continued

Balance sheet management: Liquidity and funding risk continued

Long-term debt issuances

The table below shows debt securities issued by the Group with an original maturity of one year or more. The Group also executes other long-term funding arrangements (predominantly term repurchase agreements) which are not reflected in the following tables.

	2011 £m	2010 £m	2009 £m
Public			
- unsecured	5,085	12,887	8,386
- unsecured: guaranteed	—	—	19,663
- secured	9,807	8,041	—
Private			
- unsecured	12,414	17,450	14,895
- unsecured: guaranteed	—	—	15,459
- secured	500	—	—
Gross issuance	27,806	38,378	58,403
Buybacks	(6,892)	(6,298)	(7,264)
Net issuance	20,914	32,080	51,139

Key points

- In line with the Group's Strategic Plan, it has been an active issuer in recent years as it improved its liquidity and funding profile. Secured funding has increased as a proportion of total wholesale funding more recently as market dislocation and uncertainty over future regulatory developments have made unsecured markets less liquid.

- As the Group delevers, with Non-Core and Markets third party assets decreasing and Retail & Commercial deposits increasing, net term debt issuance decreased from £32 billion in 2010 to £21 billion in 2011. The net requirement in 2012 is not expected to exceed £10 billion as further deleveraging should cover the differences.*

- The Group undertakes voluntary buybacks of its privately issued debt in order to maintain client relationships and as part of its normal market making activities. These transactions are conducted at prevailing market rates.

The table below shows the original maturity of public long-term debt securities issued.

	1-3 years	3-5 years	5-10 years	>10 years	Total
2011	£m	£m	£m	£m	£m
MTNs	904	1,407	1,839	935	5,085
Covered bonds	—	1,721	3,280	—	5,001
Securitisations	—	—	—	4,806	4,806
	904	3,128	5,119	5,741	14,892
% of total	6	21	34	39	100
2010					
MTNs	1,445	2,150	6,559	2,733	12,887

Covered bonds	—	1,030	1,244	1,725	3,999
Securitisations	—	—	—	4,042	4,042
	1,445	3,180	7,803	8,500	20,928
% of total	7	15	37	41	100
2009					
MTNs	13,450	7,457	3,477	3,665	28,049
% of total	48	27	12	13	100

* unaudited

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The table below shows the currency breakdown of public and private long-term debt securities issued.

2011	GBP £m	EUR £m	USD £m	AUD £m	Other £m	Total £m
Public						
- MTNs	—	1,808	2,181	1,096	—	5,085
- covered bonds	—	5,001	—	—	—	5,001
- securitisations	478	1,478	2,850	—	—	4,806
Private	2,872	3,856	3,183	302	2,701	12,914
	3,350	12,143	8,214	1,398	2,701	27,806
% of total	12	44	29	5	10	100
2010						
Public						
- MTNs	1,260	3,969	5,131	1,236	1,291	12,887
- covered bonds	—	3,999	—	—	—	3,999
- securitisations	663	1,629	1,750	—	—	4,042
Private	2,184	10,041	2,879	174	2,172	17,450
	4,107	19,638	9,760	1,410	3,463	38,378
% of total	11	51	25	4	9	100
2009						
Public						
- MTNs	7,267	4,795	10,940	3,173	1,874	28,049
Private	4,932	9,773	9,668	2,738	3,243	30,354
	12,199	14,568	20,608	5,911	5,117	58,403
% of total	21	25	35	10	9	100

Key points

- In line with the Group’s plan to diversify its funding mix, issuances were spread across G10 currencies and maturity bands, including £5.7 billion of public issuance with an original maturity of greater than 10 years.
- The Group has issued approximately £2.8 billion since year end, including a £1 billion public covered bond issuance and a US$1.2 billion securitisation.

Secured funding

The Group has access to secured funding markets through own-asset securitisation and covered bond funding programmes to complement existing wholesale funding programmes and access to the repo markets. The Group monitors and manages encumbrance levels related to these secured funding programmes. This includes the potential encumbrance of Group assets that could be used in own-asset securitisations and/or covered bonds that could be used as contingent liquidity.

For information on the Group’s own-asset securitisations, covered bond programme and securities repurchase agreements, refer to Note 30 on the consolidated accounts on pages 355 and 356.

Liquidity management

Liquidity risk management requires ongoing assessment and calibration of: how the various sources of the Group's liquidity risk interact with each other; market dynamics; and regulatory developments to determine the overall size of the Group's liquid asset buffer. In addition to the size determination, the composition of the buffer is also important. The composition is reviewed on a continuous basis in order to ensure that the Group holds an appropriate portfolio of high quality assets that can provide a cushion against market disruption and dislocation, even in the most extreme stress circumstances.

Business review Risk and balance sheet management continued

Balance sheet management: Liquidity and funding risk continued

Liquidity portfolio

The table below shows the composition of the Group's liquidity portfolio (at estimated liquidity value). All assets within the liquidity portfolio are unencumbered.

	2011		2010	2009
	Average	Period end	Period end	Period end
	£m	£m	£m	£m
Cash and balances at central banks	74,711	69,932	53,661	51,500
Treasury bills	5,937	—	14,529	30,010
Central and local government bonds (1)				
- AAA rated governments and US agencies	37,947	29,632	41,435	30,140
- AA- to AA+ rated governments (2)	3,074	14,102	3,744	2,011
- governments rated below AA	925	955	1,029	1,630
- local government	4,779	4,302	5,672	5,706
	46,725	48,991	51,880	39,487
Other assets (3)				
- AAA rated	21,973	25,202	17,836	20,246
- below AAA rated and other high quality assets	12,102	11,205	16,693	29,418
	34,075	36,407	34,529	49,664
Total liquidity portfolio	161,448	155,330	154,599	170,661

Notes:

(1) Includes FSA eligible government bonds of £36.7 billion at 31 December 2011 (2010 - £34.7 billion; 2009 - £19.9 billion).

(2) Includes AAA rated US government guaranteed and US government sponsored agencies. The US government was downgraded from AAA to AA+ by S&P on 5 August 2011, although not by Moody's or Fitch. These securities are reflected here.

(3) Includes assets eligible for discounting at central banks.

Key point

- In view of the continuing uncertain market conditions, the liquidity portfolio was maintained above the Group's target level of £150 billion at £155.3 billion, with an average balance in 2011 of £161.4 billion. In anticipation of challenging market conditions, the composition was altered to become more liquid and conservative, as cash and balances at central banks rose to 45% of the total portfolio at 31 December 2011, from 35% at 31 December 2010.

Liquidity and funding metrics

The Group continues to improve and augment liquidity and funding risk management practices, in light of market experience and emerging regulatory and industry standards. The Group monitors a range of liquidity and funding indicators. These metrics encompass short and long-term liquidity requirements under stress and normal operating conditions. Two key structural ratios are described below.

Loan to deposit ratio and funding gap

The table below shows the Group's loan:deposit ratio and customer funding gap, including disposal groups.

	Loan:deposit ratio		Customer
	Group	Core	

	%	%	funding gap Group £bn
2011	108	94	37
2010	118	96	77
2009	132	103	137

Note:
(1) Loans are net of provisions, excluding repos. For Group before RFS MI only for 2009.

Key points

- The Group's loan:deposit ratio improved 1,000 basis points to 108% during 2011, as loans declined and deposits grew.

- The customer funding gap almost halved with Non-Core contributing £27 billion of the £40 billion reduction.

Net stable funding ratio*

The table below shows the Group's net stable funding ratio (NSFR), estimated by applying the Basel III guidance issued in December 2010, which represents a non-GAAP measure as described on page 2. The Group is aiming to meet the minimum required NSFR of 100% over the longer term. This measure seeks to show the proportion of structural term assets which are funded by stable funding, including customer deposits, long-term wholesale funding and equity. One of the main components of the ratio entails categorising retail and SME deposits as either 'more stable' or 'less stable'. The Group's NSFR will also continue to be refined over time in line with regulatory developments. It may be calculated on a basis that is not consistent with that used by other financial institutions.

	2011		2010		2009		
		ASF(1)		ASF(1)		ASF(1)	Weighting
	£bn	£bn	£bn	£bn	£bn	£bn	%
Equity	76	76	77	77	80	80	100
Wholesale funding > 1 year	124	124	154	154	144	144	100
Wholesale funding < 1 year	134	—	157	—	250	—	—
Derivatives	524	—	424	—	422	—	—
Repurchase agreements	129	—	115	—	106	—	—
Deposits							
- Retail and SME - more stable	227	204	172	155	166	149	90
- Retail and SME - less stable	31	25	51	41	50	40	80
- Other	179	89	206	103	199	99	50
Other (2)	83	—	98	—	105	—	—
Total liabilities and equity	1,507	518	1,454	530	1,522	512	
Cash	79	—	57	—	52	—	—
Inter-bank lending	44	—	58	—	49	—	—
Debt securities > 1 year							
- central and local governments AAA to AA-	77	4	89	4	84	4	5
- other eligible bonds	73	15	75	15	87	17	20
- other bonds	14	14	10	10	9	9	100
Debt securities < 1 year	45	—	43	—	69	—	—
Derivatives	530	—	427	—	438	—	—
Reverse repurchase agreements	101	—	95	—	76	—	—
Customer loans and advances > 1 year							
- residential mortgages	145	94	145	94	137	89	65
- other	173	173	211	211	241	241	100
Customer loans and advances < 1 year							
- retail loans	19	16	22	19	24	20	85
- other	137	69	125	63	153	77	50
Other (3)	70	70	97	97	103	103	100
Total assets	1,507	455	1,454	513	1,522	560	
Undrawn commitments	240	12	267	13	289	14	5
Total assets and undrawn commitments	1,747	467	1,721	526	1,811	574	
Net stable funding ratio		111%		101%		89%	

Notes:

(1) Available stable funding.

(2) Deferred tax, insurance liabilities and other liabilities.

(3) Prepayments, accrued income, deferred tax and other assets.

Key points*

- The NSFR increased by 10% in the year to 111%, with the funding cushion over term assets and undrawn commitments increasing from £4 billion to £51 billion.

- Available stable funding decreased by £12 billion in the year as a result of a £30 billion reduction in long-term wholesale funding, including the move into short-term of approximately £20 billion of balances under the CGS. This was offset by a £19 billion increase in qualifying deposit balances, including classification of certain deposits as more stable, as some assumptions and methodologies were refined.

- Term assets decreased in the year by £38 billion primarily reflecting Non-Core disposals and run-offs. The decrease in other assets is primarily due to the closure of certain equities businesses in Markets and other asset movements.

* unaudited

Balance sheet management: Liquidity and funding risk continued

Special purpose entities

The Group arranges securitisations to facilitate client transactions and undertakes securitisations to sell financial assets or to fund specific portfolios of assets. The Group also acts as an underwriter and depositor in securitisation transactions involving both client and proprietary transactions. In a securitisation, assets, or interests in a pool of assets, are transferred generally to a special purpose entity (SPE) which then issues liabilities to third party investors. SPEs are vehicles established for a specific, limited purpose, usually do not carry out a business or trade and typically have no employees. They take a variety of legal forms - trusts, partnerships and companies - and fulfil many different functions. As well as being a key element of securitisations, SPEs are also used in fund management activities to segregate custodial duties from the fund management advice provided by the Group.

The Group applies the guidance in IAS 27 'Consolidated and Separate Financial Statements' and SIC 12 'Consolidation - Special Purpose Entities' in determining whether or not to consolidate an SPE. SPEs are consolidated where the substance of the relationship between the Group and the SPE is such that the SPE is controlled by the Group. In determining whether the SPE is controlled by the Group, the Group considers whether the activities of the SPE are being conducted on its behalf so that it obtains benefits from its operation; whether the Group has the decision-making powers to obtain the majority of the benefits of the SPE's activities; whether the Group has rights to obtain the majority of the benefits of the SPE; and whether the Group retains the majority of the residual or ownership risks related to the SPE or its assets so as to obtain benefits from its activities. As a result of applying these principles, the Group does not consolidate those SPEs where its interests in the SPE do not provide the Group with a majority of the benefits and/or residual or ownership risks and therefore the SPE is not controlled by the Group. SPEs that are in substance controlled by the Group are consolidated. The Group accounts for its interests, for example, holdings of securities issued and liquidity commitments, in SPEs it does not consolidate in accordance with its accounting policy for these items.

The Group sponsors and arranges own-asset securitisations, whereby the sale of assets or interests in a pool of assets into an SPE is financed by the issuance of securities to investors. The pool of assets held by the SPE may be originated by the Group, or (in the case of whole loan programmes) purchased from third parties, and may be of varying credit quality. Investors in the debt securities issued by the SPE are rewarded through credit-linked returns, according to the credit rating of their securities. The majority of securitisations are supported through liquidity facilities, other credit enhancements and derivative hedges extended by financial institutions, some of which offer protection against initial defaults in the pool of assets. Thereafter, losses are absorbed by investors in the lowest ranking notes in the priority of payments. Investors in the most senior ranking debt securities are typically shielded from loss, since any subsequent losses may trigger repayment of their initial principal.

The Group also employs synthetic structures, where assets are not sold to the SPE, but credit derivatives are used to transfer the credit risk of the assets to an SPE. Securities may then be issued by the SPE to investors, on the back of the credit protection sold to the Group by the SPE.

Residential and commercial mortgages and credit card receivables form the types of assets generally included in cash securitisations, while corporate loans and commercial mortgages typically serve as reference obligations in synthetic securitisations.

The Group sponsors own-asset securitisations primarily as a way of diversifying funding sources. The Group purchases the securities issued in own-asset securitisations and may pledge as collateral for repurchase agreements with major central banks.

Refer to Note 30 on the consolidated accounts on page 355 for the asset categories, together with the carrying value of the assets and associated liabilities for those securitisations and other asset transfers, other than conduits (refer to page 83), where the assets continue to be recorded on the Group's balance sheet.

Conduits

The Group sponsors and administers a number of asset-backed commercial paper (ABCP) conduits. A conduit is a SPE that issues commercial paper and uses the proceeds to purchase or fund a pool of assets. The commercial paper is secured on the assets and is redeemed by further commercial paper issuance, repayment of assets or funding from liquidity facilities. Commercial paper is typically short-dated, usually up to three months.

Group-sponsored conduits can be divided into multi-seller conduits and own-asset conduits. In determining whether or not to consolidate a conduit the Group applies the same criteria as to SPEs. Liquidity commitments from the Group to the conduit exceed the nominal amount of assets funded by the conduit as liquidity commitments are sized to cover the funding cost of the related assets.

The ways the Group may be involved with conduits and other special purpose entities are described on page 82.

The Group's involvement in conduits takes a number of forms. It may:

- Sponsor an ABCP programme i.e. establish the programme and approve the sellers permitted to participate in the programme and the asset pools to be purchased by the programme;
- Administer an ABCP programme;
- Provide the ABCP conduit with liquidity facilities;
- Provide the ABCP conduit with a programme-wide credit enhancement facility; or
- Purchase commercial paper from an ABCP conduit.

Total assets and other aspects relating to the Group's conduits are set out below.

	2011			2010			2009		
	Core	Non-Core	Total	Core	Non-Core	Total	Core	Non-Core	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Total assets held by the conduits	11,208	1,893	13,101	16,390	3,624	20,014	23,409	3,957	27,366
Commercial paper issued (1)	10,590	859	11,449	15,522	2,540	18,062	22,644	2,939	25,583
Liquidity and credit enhancements									
Deal specific liquidity									
- drawn	321	1,051	1,372	868	1,109	1,977	738	1,059	1,797
- undrawn	15,324	1,144	16,468	21,935	2,980	24,915	28,628	3,852	32,480
PWCE (2)	795	193	988	1,025	257	1,282	1,167	341	1,508
	16,440	2,388	18,828	23,828	4,346	28,174	30,533	5,252	35,785
Maximum exposure to loss (3)	15,646	2,194	17,840	22,803	4,089	26,892	29,365	4,911	34,276

Notes:

(1) Includes £0.3 billion of ABCP issued to RBS plc at 31 December 2011 (2010 - £0.7 billion).

(2) Programme-wide credit enhancement (PWCE) is an additional programme-wide credit support which would absorb first loss on transactions where liquidity support is provided by a third party.

(3)

Maximum exposure to loss quantifies the Group's exposure to its sponsored conduits. It is determined as the Group's liquidity commitment to its sponsored conduits and additional PWCE which would absorb first loss on transactions where liquidity support is provided by third parties. Historically, PWCE has been greater than third party liquidity. Therefore the maximum exposure to loss is total deal specific liquidity.

(4) Liquidity commitments from the Group to the conduit exceed the nominal amount of assets funded by the conduit given that liquidity commitments are sized to cover the accrued funding cost of the related assets.

Key points

- During 2011, both multi-seller and own-asset conduit assets decreased, as deals terminated and Non-Core assets were sold. The total assets held by Group-sponsored conduits were £13.1 billion at 31 December 2011 (2010 - £20.0 billion; 2009 - £27.4 billion).

- The average maturity of ABCP issued by the Group's conduits at 31 December 2011 was 42.6 days (2010 - 69.4 days; 2009 - 58.4 days).

- The maturity of the commercial paper issued by the Group's conduits is managed to mitigate the short-term contingent liquidity risk of providing back-up facilities. The Group's limits sanctioned for such liquidity facilities in 2011 totalled approximately £16.8 billion for multi-seller conduits (2010 - £22.6 billion; 2009 - £25.0 billion).

- The weighted average life of the funded assets was 1.9 years at 31 December 2011 (2010 - 2.3 years; 2009 - 1.9 years).

- The Group's maximum exposure to loss on its multi-seller conduits is £16.7 billion (2010 - £22.8 billion; 2009 - £25.2 billion), being the total amount of the Group's liquidity commitments plus the extent of the programme-wide credit enhancement of conduit assets for which facilities were not provided by third parties.

- The Group holds a single own-asset conduit, which has assets funded by the Group. The Group's maximum exposure to loss on own-asset conduits was £1.1 billion in 2011 (2010 - £4.1 billion; 2009 - £9.1 billion), with no ABCP outstanding at that date (2010 - £2.2 billion; 2009 - £7.7 billion).

- Multi-seller conduits accounted for 93% of the total liquidity and credit enhancements committed by the Group at 31 December 2011 (2010 - 84%; 2009 - 73%). The Group's multi-seller conduits have continued to fund the vast majority of their assets solely through ABCP issuance.

Business review Risk and balance sheet management continued

Balance sheet management: Liquidity and funding risk continued
Conduits continued
The Group has not utilised its own-asset conduit with a committed liquidity of £26 billion (2010 - £26 billion) to access the Bank of England's open market operations for contingent funding purposes. This conduit is not included above, or in the tables on pages 84 and 85.

Collateral analysis, profile, credit ratings and weighted average lives relating to the Group's consolidated conduits are detailed below.

	Funded assets			Undrawn	Liquidity	
				commitments	from third	Total
	Loans	Securities	Total	to fund assets	parties	exposure
2011	£m	£m	£m	£m	£m	£m
Auto loans	3,663	390	4,053	2,241	—	6,294
Corporate loans	146	72	218	16	—	234
Credit card receivables	865	—	865	699	—	1,564
Trade receivables	1,136	126	1,262	649	—	1,911
Student loans	488	—	488	352	—	840
Consumer loans	1,362	—	1,362	101	—	1,463
Mortgages						
- prime	2,239	—	2,239	308	—	2,547
- non-conforming	727	—	727	34	—	761
- commercial	21	489	510	8	—	518
Other	760	617	1,377	331	—	1,708
	11,407	1,694	13,101	4,739	—	17,840
2010						
Auto loans	4,943	346	5,289	2,964	—	8,253
Corporate loans	115	2,340	2,455	106	—	2,561
Credit card receivables	2,088	—	2,088	1,209	—	3,297
Trade receivables	761	—	761	1,090	—	1,851
Student loans	757	—	757	532	(132)	1,157
Consumer loans	1,889	—	1,889	111	—	2,000
Mortgages						
- prime	2,569	3	2,572	752	—	3,324
- non-conforming	1,371	—	1,371	20	—	1,391
- sub-prime	103	—	103	19	—	122
- commercial	210	450	660	76	(21)	715
Other	1,072	997	2,069	(1)	(10)	2,058
	15,878	4,136	20,014	6,878	(163)	26,729
2009						
Auto loans	4,293	356	4,649	2,526	—	7,175
Corporate loans	106	7,695	7,801	161	—	7,962
Credit card receivables	4,083	—	4,083	1,058	—	5,141
Trade receivables	806	—	806	1,351	—	2,157

Student loans	915	—	915	263	(132)	1,046
Consumer loans	1,686	—	1,686	222	—	1,908
Mortgages						
- prime	2,739	3	2,742	750	—	3,492
- non-conforming	1,548	—	1,548	193	—	1,741
- commercial	413	458	871	155	(22)	1,004
Other	872	1,393	2,265	232	(12)	2,485
	17,461	9,905	27,366	6,911	(166)	34,111

	CP funded assets					Credit ratings (S&P equivalent)				
	UK	Europe	US	RoW	Total	AAA	AA	A	BBB	Below BBB
2011	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Auto loans	518	1,145	2,141	249	4,053	3,323	683	40	7	—
Corporate loans	—	160	58	—	218	9	94	27	88	—
Credit card receivables	—	—	865	—	865	774	—	91	—	—
Trade receivables	—	567	695	—	1,262	449	343	426	44	—
Student loans	—	—	488	—	488	488	—	—	—	—
Consumer loans	716	—	646	—	1,362	—	—	1,362	—	—
Mortgages										
- prime	182	—	—	2,057	2,239	1,446	737	39	17	—
- non-conforming	667	60	—	—	727	157	265	287	18	—
- commercial	489	—	—	21	510	2	5	498	5	—
Other	124	201	531	521	1,377	363	42	402	180	390
	2,696	2,133	5,424	2,848	13,101	7,011	2,169	3,172	359	390
2010										
Auto loans	429	962	3,434	464	5,289	4,827	354	101	7	—
Corporate loans	22	1,513	709	211	2,455	2,166	161	128	—	—
Credit card receivables	144	—	1,944	—	2,088	1,912	125	—	51	—
Trade receivables	—	261	500	—	761	265	353	95	48	—
Student loans	116	—	641	—	757	641	116	—	—	—
Consumer loans	766	462	661	—	1,889	16	—	1,873	—	—
Mortgages										—
- prime	161	—	—	2,411	2,572	1,043	1,476	32	21	—
- non-conforming	712	659	—	—	1,371	782	273	316	—	—
- sub-prime	103	—	—	—	103	—	68	—	35	—
- commercial	627	—	—	33	660	16	5	635	4	—
Other	447	455	353	814	2,069	95	52	1,242	680	—
	3,527	4,312	8,242	3,933	20,014	11,763	2,983	4,422	846	—
2009										
Auto loans	476	982	2,621	570	4,649	2,965	1,547	137	—	—
Corporate loans	312	5,213	1,411	865	7,801	7,584	111	106	—	—
Credit card receivables	177	—	3,823	83	4,083	2,781	759	420	123	—
Trade receivables	—	334	438	34	806	446	266	60	34	—
Student loans	117	—	798	—	915	798	117	—	—	—
Consumer loans	733	800	153	—	1,686	68	50	1,553	15	—
Mortgages										
- prime	138	—	—	2,604	2,742	949	1,746	28	3	16
- non-conforming	599	949	—	—	1,548	1,070	379	99	—	—
- commercial	641	194	—	36	871	25	3	840	—	3
Other	121	670	298	1,176	2,265	170	249	950	896	—
	3,314	9,142	9,542	5,368	27,366	16,856	5,227	4,193	1,071	19

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Business review Risk and balance sheet management continued

Balance sheet management: Liquidity and funding risk continued
Assets and liabilities by contractual cash flow maturity
The tables below show the contractual undiscounted cash flows receivable and payable, up to a period of twenty years, including future receipts and payments of interest of on-balance sheet assets by contractual maturity. The balances in the table below do not agree directly with the consolidated balance sheet, as the table includes all cash flows relating to principal and future coupon payments, presented on an undiscounted basis. The tables have been prepared on the following basis:

The contractual maturity of on-balance sheet assets and liabilities highlights the maturity transformation which underpins the role of banks to lend long-term, but to fund themselves predominantly by short-term liabilities such as customer deposits. This is achieved through the diversified funding franchise of the Group across an extensive retail, wealth and SME customer base, and across a wide geographic network. In practice, the behavioural profiles of many assets and liabilities exhibit greater stability and longer maturity than the contractual maturity.

Financial assets have been reflected in the time band of the latest date on which they could be repaid, unless earlier repayment can be demanded by the Group. Financial liabilities are included at the earliest date on which the counterparty can require repayment, regardless of whether or not such early repayment results in a penalty. If the repayment of a financial instrument is triggered by, or is subject to, specific criteria such as market price hurdles being reached, the asset is included in the time band that contains the latest date on which it can be repaid, regardless of early repayment. The liability is included in the time band that contains the earliest possible date on which the conditions could be fulfilled, without considering the probability of the conditions being met.

For example, if a structured note is automatically prepaid when an equity index exceeds a certain level, the cash outflow will be included in the less than three months period, whatever the level of the index at the year end. The settlement date of debt securities in issue, issued by certain securitisation vehicles consolidated by the Group, depends on when cash flows are received from the securitised assets. Where these assets are prepayable, the timing of the cash outflow relating to securities assumes that each asset will be prepaid at the earliest possible date. As the repayments of assets and liabilities are linked, the repayment of assets in securitisations is shown on the earliest date that the asset can be prepaid, as this is the basis used for liabilities.

The principal amounts of financial assets and liabilities that are repayable after twenty years or where the counterparty has no right to repayment of the principal are excluded from the table, as are interest payments after twenty years.

2011	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
Assets by contractual maturity						
Cash and balances at central banks	79,269	—	—	—	—	—
Loans and advances to banks	26,326	1,294	544	121	114	—
Debt securities	7,237	9,569	23,137	21,003	39,148	15,869
Settlement balances	7,759	8	—	1	—	—
Other financial assets	397	158	—	16	738	—
Total maturing assets	120,988	11,029	23,681	21,141	40,000	15,869
Loans and advances to customers	97,318	90,894	108,331	55,785	62,085	56,259
Derivatives held for hedging	519	1,556	3,438	1,695	596	138
	218,825	103,479	135,450	78,621	102,681	72,266

Liabilities by contractual maturity						
Deposits by banks	39,139	5,104	5,513	461	1,121	364
Debt securities in issue	66,253	15,756	25,099	17,627	18,833	4,190
Subordinated liabilities	133	1,116	4,392	7,872	8,654	3,488
Settlement balances and other liabilities	9,015	37	36	62	16	15
Total maturing liabilities	114,540	22,013	35,040	26,022	28,624	8,057
Customer accounts	379,692	23,068	12,643	5,389	1,483	779
Derivatives held for hedging	525	788	1,981	1,186	1,101	821
	494,757	45,869	49,664	32,597	31,208	9,657
Maturity gap	6,448	(10,984)	(11,359)	(4,881)	11,376	7,812
Cumulative maturity gap	6,448	(4,536)	(15,895)	(20,776)	(9,400)	(1,588)
Guarantees and commitments notional amount						
Guarantees (1)	24,886	—	—	—	—	—
Commitments (2)	239,963	—	—	—	—	—

For notes relating to this table refer to page 88.

2010	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
Assets by contractual maturity						
Cash and balances at central banks	56,988	—	—	1	—	25
Loans and advances to banks	33,809	1,377	711	120	193	79
Debt securities	11,247	9,816	25,059	22,400	40,600	22,128
Settlement balances	11,334	231	—	—	41	—
Other financial assets	458	221	207	15	405	—
Total maturing assets	113,836	11,645	25,977	22,536	41,239	22,232
Loans and advances to customers	112,465	86,592	120,139	69,304	78,131	63,015
Derivatives held for hedging	530	1,588	2,612	638	210	101
	226,831	99,825	148,728	92,478	119,580	85,348
Liabilities by contractual maturity						
Deposits by banks	43,396	4,417	1,243	304	651	374
Debt securities in issue	89,583	43,032	31,862	22,569	24,209	6,697
Subordinated liabilities	2,485	2,611	6,570	8,691	8,672	4,607
Settlement balances and other liabilities	12,423	59	136	177	385	25
Total maturing liabilities	147,887	50,119	39,811	31,741	33,917	11,703
Customer accounts	402,457	18,580	8,360	4,651	4,393	2,384
Derivatives held for hedging	608	936	2,103	969	681	253
	550,952	69,635	50,274	37,361	38,991	14,340
Maturity gap	(34,051)	(38,474)	(13,834)	(9,205)	7,322	10,529
Cumulative maturity gap	(34,051)	(72,525)	(86,359)	(95,564)	(88,242)	(77,713)
Guarantees and commitments notional amount						
Guarantees (1)	31,026	—	—	—	—	—
Commitments (2)	266,822	—	—	—	—	—

For notes relating to this table refer to page 88.

Business review Risk and balance sheet management continued

Balance sheet management: Liquidity and funding risk continued
Assets and liabilities by contractual cash flow maturity continued

2009	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
Assets by contractual maturity						
Cash and balances at central banks	52,239	—	—	1	25	—
Loans and advances to banks	42,615	1,757	966	282	868	71
Debt securities	17,581	14,484	29,675	26,788	52,104	30,335
Settlement balances	12,020	6	1	—	8	1
Other financial assets	265	215	402	127	421	—
Total maturing assets	124,720	16,462	31,044	27,198	53,426	30,407
Loans and advances to customers	126,238	65,946	130,323	101,984	180,595	202,809
Derivatives held for hedging	488	1,547	3,049	1,076	751	10
	251,446	83,955	164,416	130,258	234,772	233,226
Liabilities by contractual maturity						
Deposits by banks	65,966	15,541	3,934	2,301	632	12
Debt securities in issue	100,220	49,300	56,869	25,915	27,326	3,819
Subordinated liabilities	1,929	1,892	3,654	4,963	20,157	6,105
Settlement balances and other liabilities	12,048	100	139	104	239	83
Total maturing liabilities	180,163	66,833	64,596	33,283	48,354	10,019
Customer accounts	521,400	15,619	5,944	4,221	8,490	4,392
Derivatives held for hedging	660	1,566	3,232	1,264	1,674	1,508
	702,223	84,018	73,772	38,768	58,518	15,919
Maturity gap	(55,443)	(50,371)	(33,552)	(6,085)	5,072	20,388
Cumulative maturity gap	(55,443)	(105,814)	(139,366)	(145,451)	(140,379)	(119,991)
Guarantees and commitments notional amount						
Guarantees (1)	39,952	—	—	—	—	—
Commitments (2)	291,634	—	—	—	—	—

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

Held-for-trading assets of £763 billion and liabilities of £708 billion (2010 - £665 billion assets, £586 billion liabilities; 2009 - £651 billion assets, £568 billion liabilities) have been excluded from the table in view of their short-term nature.

Interest rate risk
The banking book consists of interest bearing assets, liabilities and derivative instruments used to mitigate risks which are accounted for on an accrual basis, as well as non-interest bearing balance sheet items, which are not subjected to fair value accounting.

The Group provides financial products to satisfy a variety of customer requirements. Loans and deposits are designed to meet customer objectives with regard to repricing frequency, tenor, index, prepayment, optionality and other features. When aggregated, they form portfolios of assets and liabilities with varying degrees of sensitivity to changes in market rates.

However, mismatches in these sensitivities give rise to net interest income (NII) volatility as interest rates rise and fall. For example, a bank with a floating rate loan portfolio and largely fixed rate deposits will see its NII rise as interest rates rise and fall as rates decline. Due to the long-term nature of many banking book portfolios, varied interest rate repricing characteristics and maturities, it is likely the NII will vary from period to period, even if interest rates remain the same. New business volumes originated in any period will alter the interest rate sensitivity of a bank if the resulting portfolio differs from portfolios originated in prior periods.

The Group assesses interest rate risk in the banking book (IRRBB) using a set of standards to define, measure and report the market risk. It is the Group’s policy to minimise interest rate sensitivity in banking book portfolios and where interest rate risk is retained, to ensure that appropriate measures and limits are applied. Key measures used to evaluate IRRBB are subjected to approval of divisional Asset and Liability Management Committees (ALCOs) and the Group Asset and Liability Management Committee (GALCO).

Limits on IRRBB are proposed by the Group Treasurer for approval by the Executive Risk Forum annually.

The Group uses a variety of approaches to quantify its interest rate risk. IRRBB is measured using a version of the same value-at-risk (VaR) methodology that is used for the Group’s trading portfolios. Net interest income exposures are measured in terms of sensitivity over time to movements in interest rates. Additionally, Citizens measures the sensitivity of the market value of equity to changes in forward interest rates.

With the exception of Citizens and Markets, divisions are required to manage IRRBB through internal transactions with Group Treasury, to the greatest extent possible. Residual risks in divisions must be measured and reported as described below.

Group Treasury aggregates exposures arising from its own external activities and positions transferred to it from divisions. Where appropriate, Group Treasury nets off-setting risk exposures to determine a residual exposure to interest rate movements. Hedging transactions using cash and derivative instruments are executed to manage IRRBB exposures, within the GALCO approved VaR limits.

Citizens and Markets manage their own IRRBB exposures within approved limits to satisfy their business objectives.

IRRBB VaR for the Group’s retail and commercial banking activities at a 99% a confidence level was as follows:

	Average	Period end	Maximum	Minimum
	£m	£m	£m	£m
2011	63	51	80	44
2010	58	96	96	30
2009	86	101	123	53

A breakdown of the Group's IRRBB VaR by currency is shown below.

	2011	2010	2009
Currency	£m	£m	£m
Euro	26	33	32
Sterling	57	79	111
US dollar	61	121	42
Other	5	10	9

Key points

- Interest rate exposure at 31 December 2011 was considerably lower than at 31 December 2010 but average exposure was 9% higher in 2011 than in 2010.

- The reduction in US dollar VaR reflects, in part, changes in holding period assumptions following changes in Non-Core assets.*

* unaudited

Balance sheet management: Interest rate risk continued

Sensitivity of net interest income*

The Group seeks to mitigate the effect of prospective interest rate movements, which could reduce future net interest income (NII) in the Group's businesses, whilst balancing the cost of such activities on the current net revenue stream. Hedging activities also consider the impact on market value sensitivity under stress.

The following table shows the sensitivity of NII, over the next twelve months, to an immediate upward or downward change of 100 basis points to all interest rates. In addition, the table includes the impact of a gradual 400 basis point steepening and a gradual 300 basis point flattening of the yield curve at tenors greater than a year. This scenario differs from that applied in the previous year in both the severity of the rate shift and the tenors to which this is applied.

	2011	2010	2009
Potential favourable/(adverse) impact on NII	£m	£m	£m
+ 100 basis points shift in yield curves	244	232	510
– 100 basis points shift in yield curves	(183)	(352)	(687)
Bear steepener	443		
Bull flattener	(146)		

Key points*

- The Group's interest rate exposure remains slightly asset sensitive, driven in part by changes to underlying business assumptions as rates rise. The impact of the steepening and flattening scenarios is largely driven by the investment of net free reserves.

- The reported sensitivity will vary over time due to a number of factors such as market conditions and strategic changes to the balance sheet mix and should not therefore be considered predictive of future performance.

* unaudited

Structural foreign currency exposures

Structural foreign exchange exposures represent net investment in subsidiaries, associates and branches, the functional currencies of which are currencies other than sterling. The Group hedges structural foreign currency exposures only in limited circumstances. The Group's objective is to ensure, where practical, that its consolidated capital ratios are largely protected from the effect of changes in exchange rates. The Group seeks to limit the sensitivity to its Core Tier 1 ratio to 20 basis points in a 10% rate shock scenario. The Group's structural foreign currency position is reviewed by GALCO regularly.

The table below shows the Group's structural foreign currency exposures.

2011	Net assets of overseas operations £m	RFS MI £m	Net investments in foreign operations £m	Net investment hedges £m	Structural foreign currency exposures pre-economic hedges £m	Economic hedges (1) £m	Residual structural foreign currency exposures £m
US dollar	17,570	1	17,569	(2,049)	15,520	(4,071)	11,449
Euro	8,428	(3)	8,431	(621)	7,810	(2,236)	5,574
Other non-sterling	5,224	272	4,952	(4,100)	852	—	852
	31,222	270	30,952	(6,770)	24,182	(6,307)	17,875
2010							
US dollar	17,137	2	17,135	(1,820)	15,315	(4,058)	11,257
Euro	8,443	33	8,410	(578)	7,832	(2,305)	5,527
Other non-sterling	5,320	244	5,076	(4,135)	941	—	941
	30,900	279	30,621	(6,533)	24,088	(6,363)	17,725
2009							
US dollar	15,589	(2)	15,591	(3,846)	11,745	(5,696)	6,049
Euro	21,900	13,938	7,962	(2,351)	5,611	(3,522)	2,089
Other non-sterling	5,706	511	5,195	(4,001)	1,194	—	1,194
	43,195	14,447	28,748	(10,198)	18,550	(9,218)	9,332

Note:

(1) The economic hedges represent US dollar and euro preference shares in issue that are treated as equity under IFRS, and do not qualify as hedges for accounting purposes.

Key points

- The Group's structural foreign currency exposure at 31 December 2011 was £24.2 billion and £17.9 billion before and after economic hedges respectively, broadly unchanged from the end of 2010 position.

- Changes in foreign currency exchange rates will affect equity in proportion to structural foreign currency exposure. A 5% strengthening in foreign currencies against sterling would result in a gain of £1.27 billion (2010 - £1.27 billion; 2009 - £0.98 billion) in equity, while a 5% weakening would result in a loss of £1.15 billion (2010 - £1.15 billion; 2009 - £0.88 billion) in equity.

Equity risk

The Group holds equity positions in the banking book in order to achieve strategic objectives, such as membership of an exchange or clearing house, or to support venture capital transactions or customer restructuring arrangements. The

Group is exposed to market risk on these banking book equity positions because they are measured at fair value. Fair values are based on available market prices where possible. In the event that market prices are not available, fair value is based on appropriate valuation techniques or management estimates.

The table below sets out the Group's banking book equity positions.

	Listed	Unlisted	Total
2011	£m	£m	£m
Group	576	1,768	2,344
2010			
Group	535	2,080	2,615
2009			
Group before RFS Holdings minority interest	401	2,388	2,789
RFS Holdings minority interest	60	211	271
Group	461	2,599	3,060

Note:
(1) The table above excludes equity exposures held-for-trading and those held by insurance/assurance entities.

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Risk management

Introduction

This section focuses on each of the key types of risk that RBS Group faces - explaining how the Group manages these risks and highlighting the enhancements made as a result of progress under the Group's ongoing initiatives to strengthen its approach to risk management.

Credit risk

All the disclosures in this section (pages 92 to 118) are audited unless otherwise indicated by an asterisk (*).

Credit risk is the risk of financial loss owing to the failure of a customer to meet its obligation to settle outstanding amounts. The quantum and nature of credit risk assumed across the Group's different businesses vary considerably, while the overall credit risk outcome usually exhibits a high degree of correlation with the macroeconomic environment.

Organisation

The existence of a strong credit risk management function is vital to support the ongoing profitability of the Group. The potential for loss through economic cycles is mitigated through the embedding of a robust credit risk culture within the business units and through a focus on the importance of sustainable lending practices. The role of the credit risk management function is to own the credit approval, concentration and credit risk control frameworks and to act as the ultimate authority for the approval of credit. This, together with strong independent oversight and challenge, enables the business to maintain a sound lending environment within risk appetite.

Responsibility for development of Group-wide policies, credit risk frameworks, Group-wide portfolio management and assessment of provision adequacy, sits within the Group Credit Risk (GCR) function under the management of the Group Chief Credit Officer. Execution of these policies and frameworks is the responsibility of the risk management functions, located within the Group's business divisions. These divisional credit risk functions work together with GCR to ensure that the Group Board's expressed risk appetite is met, within a clearly defined and managed control environment. The credit risk function within each division is managed by a Chief Credit Officer, who reports jointly to a divisional Chief Risk Officer and to the Group Chief Credit Officer. Divisional activities within credit risk include credit approval, transaction and portfolio analysis, early problem recognition and ongoing credit risk stewardship.

GCR is additionally responsible for verifying compliance by the divisions with all Group credit policies.

In the final quarter of 2011, the Executive Risk Forum (ERF) approved a change to the management of the credit portfolio, delegating greater authority to the Group Chief Credit Officer as chair of the functional credit committees that analyse and recommend the limits to the ERF. With effect from October 2011, the Group Chief Credit Officer chairs a single Credit Risk Committee, with the authority to approve limits for the majority of portfolios across the Group. The ERF retains its strategic role as the most senior risk committee outside the Group Board and will continue to approve material portfolio concentrations and higher risk portfolios such as commercial real estate. This change strengthens individual accountability across the risk organisation and encourages the engagement of business leaders in first line of defence risk activity.

Risk appetite

Credit concentration risk is managed and controlled through a series of frameworks designed to limit concentration by product/asset class, sector, single name and country. These are supported by a suite of Group-wide and divisional policies, setting out the risk parameters within which business units may operate. Information on the Group's credit portfolios is reported to the Group Board by way of the divisional and Group-level risk committees.

Throughout 2011, GCR's emphasis was on embedding the new risk management frameworks introduced in 2009 and 2010 and on ensuring alignment with the strategic risk objectives being pursued across the Group. Risk appetite has been expressed by the Group Board by reference to earnings volatility and stable capital and these principles underpin the frameworks that GCR has established, and is continuing to refine, to manage the Group's concentration risks in the Core balance sheet, by product/asset class, sector, single name and country.

In the two years since the new concentration framework was rolled out across the Group, the ERF has reviewed all material industry and product portfolios and agreed a risk appetite commensurate with the franchises represented in these reviews. In particular