

ROYAL BANK OF SCOTLAND GROUP PLC

Form 6-K

August 03, 2004

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## **FORM 6-K**

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# **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 the month of August 2004**

**Commission File Number: 001-10306**

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## **The Royal Bank of Scotland Group plc**

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**42 St Andrew Square**

**Edinburgh EH2 2YE**

**Scotland**

**(Address of principal executive offices)**

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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  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

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

The following information was issued as Company announcements, in London, England and is furnished pursuant to General Instruction B to the General Instructions to Form 6-K: \_\_\_\_\_

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**Interim Results**

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**RESULTS SUMMARY**

|  | First half    | First half<br>2003 | Increase     |           | Full year<br>2003 |
|--|---------------|--------------------|--------------|-----------|-------------------|
|  | 2004          |                    |              |           |                   |
|  | £m            |                    | £m           | £m        |                   |
| Total income   | <b>10,940</b> | 9,080              | <b>1,860</b> | <b>20</b> | 19,229            |
| Operating expenses*  | <b>4,615</b>  | 4,051              | <b>564</b>   | <b>14</b> | 8,389             |
| Operating profit before provisions*                            | <b>4,602</b>  | 4,193              | <b>409</b>   | <b>10</b> | 8,645             |
| Profit before tax, goodwill amortisation and integration costs | <b>3,851</b>  | 3,451              | <b>400</b>   | <b>12</b> | 7,151             |
| Profit before tax  | <b>3,381</b>  | 2,896              | <b>485</b>   | <b>17</b> | 6,159             |
| Cost:income ratio**  | <b>40.5%</b>  | 43.0%              |              |           | 42.0%             |
| Basic earnings per ordinary share                              | <b>69.9p</b>  | 60.0p              | <b>9.9p</b>  | <b>17</b> | 79.0p             |
| Adjusted earnings per ordinary share                           | <b>84.4p</b>  | 76.5p              | <b>7.9p</b>  | <b>10</b> | 159.3p            |
| Dividends per ordinary share                                   | <b>16.8p</b>  | 14.6p              | <b>2.2p</b>  | <b>15</b> | 50.3p             |

\* excluding goodwill amortisation and integration costs.

\*\* the cost:income ratio is based on operating expenses excluding goodwill amortisation and integration costs, and after netting operating lease depreciation against rental income.

**Sir Fred Goodwin, Group Chief Executive, said:**

Whilst the trends of strong organic growth, and improving efficiency are entirely consistent with prior periods, the range of recent acquisitions and investments in our infrastructure has created significant momentum for growth in our business. The full benefit to earnings of these initiatives will be felt over the next few years, which combined with an unquestionably further improved economic outlook, gives us confidence in the future prospects for the Group .

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**2004 FIRST HALF HIGHLIGHTS**

Income up 20% to £10,940 million.

Underlying margin stable and in line with expectations.

Further efficiency gains - cost:income ratio 40.5%, improved from 43.0% in 2003.

Profit before tax, goodwill amortisation and integration costs up £400 million, 12% to £3,851 million.

Profit before tax up 17% to £3,381 million.

Customer growth in all divisions.

Average loans and advances to customers up 15%.

Average customer deposits up 8%.

Credit quality remains strong and problem loan metrics continue to improve.

Basic earnings per ordinary share up 17%.

Adjusted earnings per ordinary share up 10%.

Interim dividend 16.8p per ordinary share, up 15%.

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THE ROYAL BANK OF SCOTLAND GROUP plc

### **GROUP CHIEF EXECUTIVE'S REVIEW**

Our results for the first half of 2004 demonstrate continuing strong organic growth and the positive impact of recent acquisitions. By delivering strong income growth, a further improvement in our cost:income ratio and stable provisions for bad debts, we increased our profit before tax, goodwill amortisation and integration costs by 12% to £3,851 million, or, at constant exchange rates, by 15% to £3,971 million. Our profit before tax increased by 17% to £3,381 million, and our adjusted earnings per share by 10%.

It is a positive reflection of the ongoing commitment of our employees that we maintained the momentum of our income growth on top of the substantial increase already delivered since the acquisition of NatWest, and achieved a further improvement in efficiency beyond the very competitive position already established, while managing successfully important acquisitions in a number of divisions. These acquisitions have already strengthened the market position of these divisions and are enhancing their ability to continue to grow their income in future.

In the first half of 2004 we increased our total income by 20%, or 23% on a constant exchange rate basis. All divisions achieved good income growth, reflecting increased customer numbers across the Group, although the results of our US businesses reported in sterling have been impacted by the decline of the US dollar relative to sterling.

The diversity of our income has contributed to the consistency of its growth over recent years. In the first half of 2004, the proportion of total income in the form of non-interest income increased to 60% - a level higher than that achieved by most large banks in the UK and internationally. Furthermore, the composition of our net interest income and non-interest income is well spread. This diversity means that our future income growth is not unduly dependent on any single activity. In particular, the amount of our net interest income derived from UK personal lending amounts to only 9% of our total income.

Net interest income increased by 9%, reflecting strong growth in average loans and advances to customers, which were up by 15%, and in average customer deposits, up by 8%. The Group net interest margin was 2.92%, four basis points lower than in the first half of 2003. Several factors contributed to this small reduction in the Group net interest margin, including increased funding of rental assets, strong organic growth in mortgages, the successful launch of the MINT credit card which attracted significant balances with a 0% interest rate for nine months and the acquisition of First Active plc ( First Active ), with its portfolio of low-risk mortgages. Against this, the Group net interest margin benefited from the growth in lending to commercial and mid-corporate customers and from the impact of rising interest rates. Non-interest income increased by 30%, as a result of both higher insurance premium income, reflecting organic growth in motor and home insurance and the acquisition in September 2003 of Churchill Insurance Group PLC ( Churchill ), and good growth in fees and commissions.

Our Group cost:income ratio improved from 43.0% in the first half of 2003 to 40.5% in the first half of 2004. This improvement has been achieved despite two areas of increased investment activity. First, as indicated previously, we have continued to invest in the three-year Group Efficiency Programme which was launched last year. A number of initiatives have been introduced in the first half of 2004 and others will follow in the second half. These initiatives will make significant improvements to our processes, which will be visible to our employees and our customers. To date, the Group Efficiency Programme has been self-financing. We remain confident that it will now begin to deliver good payback on the investment made, and will lead to a long term improvement in the Group cost:income ratio. Secondly, CBFM has been investing to enhance its debt capital market capability overseas, particularly in the US. In the first half of 2004, the Group cost:income ratio benefited from the acquisition of Churchill.





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### **GROUP CHIEF EXECUTIVE'S REVIEW (continued)**

The charge for provisions for bad and doubtful debts in the first half of 2004 was similar to the second half of 2003, and represented a smaller proportion of total loans and advances to customers. Credit metrics continue to point to stable credit quality overall, with improvements in some areas. The total of risk elements in lending and potential problem loans continues to decline, despite the strong growth in loans and advances. Balance sheet provisions as a percentage of risk elements in lending and potential problem loans have increased from 65% in June 2003 to 68% in December 2003 and 71% in June 2004.

At 30 June 2004 our tier 1 capital ratio was 8.1% and our total capital ratio was 12.5%; both ratios have been increased by the placing of new ordinary shares in May, when the acquisition of Charter One Financial, Inc ( Charter One ) was announced.

### **REVIEW OF DIVISIONS**

**Corporate Banking and Financial Markets (CBFM)** increased its income by 12% and its contribution by 17% to £2,041 million (2003 - £1,739 million). At constant exchange rates, CBFM's income was up by 14% and its contribution by 20%.

Net interest income was up by 7% (or by 10%, excluding the cost of funding rental assets), non-interest income by 14%. The increase in net interest income reflects 7% growth in average loans and advances to customers and 7% growth in average customer deposits. Within loans and advances CBFM achieved good growth in lending to commercial and mid-corporate customers, while lending to large corporates remained subdued. Net interest margin was higher, as a result of the change in mix between corporate and commercial lending. The growth in non-interest income reflects increases in net fees and commissions, dealing profits and income from rental assets.

CBFM's expenses were up by 15% (or by 14%, excluding operating lease depreciation). This increase included costs necessary to support strong growth in overseas operations and investments in revenue-growth initiatives, particularly in the US. Provisions were down from £404 million in the first half of 2003 to £315 million in the first half of 2004.

**Retail Banking** increased its income by 8% and its contribution by 6% to £1,642 million (2003 - £1,554 million).

Net interest income was up by 5%, non-interest income by 12%. The increase in net interest income reflects 15% growth in average loans and advances to customers, within which mortgages were up by 18%, personal loans by 12% and business loans by 11%. Average customer deposits were up by 8%. The mix effect of the increased proportion of mortgages resulted in a reduction in Retail Banking's net interest margin. The increase in non-interest income reflects good growth in the distribution of general insurance and bancassurance and other long-term savings products. The number of Retail Banking personal customers increased by 459,000, and small business customers by 26,000, since June 2003.

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Against the 8% growth in income, the increase in Retail Banking's costs was contained to 5%. Provisions were up from £135 million in the first half of 2003 to £186 million in the first half of 2004, reflecting the seasoning of the NatWest personal loan portfolio which had grown strongly in previous years, together with a higher incidence of fraud.

**Retail Direct** increased its income by 15% and its contribution by 17% to £480 million (2003 - £411 million). Higher interest income reflected 21% growth in average loans and advances to customers, spread across credit cards, mortgages and personal loans. The new MINT branded credit card was launched successfully in December 2003 to replace RBS Advanta. By the end of June, MINT had issued 560,000 credit cards and had attracted significant balances with a 0% introductory interest rate for nine months, leading to a reduction in Retail Direct's net interest margin in the first half of 2004. Retail Direct increased its customer accounts by 3.1 million since June 2003 (including through acquisitions). Retail Direct acquired the US credit card business of People's Bank in March 2004 and the leading European internet payment specialist Bibit in May 2004. Since the end of June, Retail Direct has reached agreement to acquire Lynk Systems, Inc., a merchant acquisition business in the United States.

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**GROUP CHIEF EXECUTIVE'S REVIEW (continued)**

**Manufacturing** costs increased by 17% to £1,122 million (2003 - £962 million). Of the £160 million increase, £50 million reflects manufacturing activities transferred from Churchill with effect from January 2004 to Manufacturing, which is now supporting both Direct Line and Churchill. The balance of the increase in costs was required to support higher business volumes, to upgrade the Group's regional property portfolio and to invest in Group Efficiency Programme initiatives which are expected to improve the Group's efficiency in future. A number of initiatives were introduced in the first half of 2004, including a sales prompt system on screens in NatWest branches and in RBS and NatWest telephony, enhanced fraud prevention and the conversion of branch reports from paper to screen. Further initiatives planned for the second half of 2004 include the roll-out of image and workflow capability to service centres, the introduction of a new mortgage platform (replacing seven separate mortgage platforms across the Group) and the introduction of an on-line customer query management system.

**Wealth Management** increased its income by 14% and its contribution by 13% to £231 million (2003 - £204 million). These results reflect good growth in business volumes, higher net interest margin, higher fee income related to improving stock markets and the initial contribution from Bank von Ernst, which was acquired in November 2003. Investment assets under management increased to £21.9 billion (2003 - £16.8 billion).

**RBS Insurance** increased its income by 89% and its contribution by 55% to £395 million (2003 - £255 million). As a result of organic growth in Direct Line and the acquisition of Churchill, RBS Insurance increased the numbers of its in-force motor and home insurance policies which both grew by 3.5 million since June 2003. RBS Insurance now has 13.2 million motor and home policies in the UK and 1.5 million motor policies in Continental Europe, and is the second largest general insurer in the UK. The first stages of the technology conversion from Churchill's to Direct Line's technology platform have been completed successfully. Excluding Churchill, which was acquired in September 2003, RBS Insurance increased its income by 17% and its contribution by 13%.

**Ulster Bank** increased its income by 25% and its contribution by 30% to £170 million (2003 - £131 million). As a result of organic growth in Ulster Bank and the acquisition of First Active, which was completed on 5 January 2004, average loans and advances grew by 67% and average customer deposits by 37%, while customers increased by 431,000 since June 2003. Direct mortgages branded First Active were launched in the UK in June. The inclusion of First Active, with its focus on personal mortgages and deposits, and strong organic growth in mortgage lending gave rise to a reduction in Ulster Bank's net interest margin. Excluding the acquisition of First Active and the disposal of NCB Stockbrokers in October 2003, Ulster Bank increased its income by 9% and its contribution by 12%.

**Citizens** increased its US dollar income by 11% and its contribution by 13% to \$771 million (2003 - \$685 million). Average loans and advances to customers grew by 32% and average customer deposits by 19%, while personal customers increased by 262,000 and business customers by 34,000 since June 2003. Between the first half of 2003 and the first half of 2004, the average US dollar/sterling exchange rate declined from 1.611 to 1.822. As a result, Citizens' income in sterling was down by 2% and its contribution was flat at £423 million (2003 - £425 million). In May 2004, Citizens announced the acquisition of Charter One, subject to regulatory and shareholder approvals. The acquisition will extend its branch network into adjacent north-eastern and mid-western states. The combination of Citizens and Charter One will create a top ten bank in the United States, by assets and by deposits.

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**GROUP CHIEF EXECUTIVE'S REVIEW (continued)**

**Acquisitions**

In the first half of 2004 we completed the acquisitions of First Active in Ireland, Roxborough Manayunk Bank and the credit card business of People's Bank in the United States and the internet payment specialist Bibit in Continental Europe. The integrations of these acquisitions, and the various acquisitions made last year, are fully on track, and we remain confident that they will deliver the benefits expected at the time of their acquisitions. In May, we announced the acquisition of Charter One, which is expected to be completed by the fourth quarter of 2004. In addition to these acquisitions, we have reached agreement to distribute credit cards to the customers of Kroger, one of the largest supermarket groups in the United States, and to distribute consumer loan products to the customers of Tchibo, a leading retailer in Germany. Since the end of June, we have reached agreement to acquire Lynk Systems, Inc., a merchant acquisition business in the United States.

**Outlook**

We remain positive about the prospects for our businesses. During the last twelve months we have enhanced significantly the Group's ability to continue to grow income and to improve efficiency through a number of important acquisitions and internal investment initiatives. While these are already having a positive impact, the key benefits will flow through in 2005 and beyond, giving us confidence in our ability to maintain the consistency of growth that has been achieved by the Group over a long period.

While some elements of fragility remain, the prospects for the economies in which we operate have unquestionably improved still further from the position six months ago, and, although this may lead to further interest rate increases, our balance sheet positioning, our strong customer franchise and the diversity of our income streams leave us well placed for the future.

**Sir Fred Goodwin**

**Group Chief Executive**

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THE ROYAL BANK OF SCOTLAND GROUP plc

## **FINANCIAL REVIEW**

### **Profit**

Profit before tax, goodwill amortisation and integration costs increased by 12% or £400 million, from £3,451 million to £3,851 million.

Profit before tax was up 17%, from £2,896 million to £3,381 million.

### **Total income**

The Group achieved strong growth in income during the first half of 2004. Total income was up 20% or £1,860 million to £10,940 million. Excluding acquisitions and at constant exchange rates, total income was up by 11%, £1,022 million.

**Net interest income** increased by 9% to £4,378 million and represents 40% of total income (2003 - 44%). Excluding acquisitions and at constant exchange rates, net interest income was up 8%. Average loans and advances to customers and average customer deposits grew by 15% and 8% respectively.

**Non-interest income** increased by 30% to £6,562 million and represents 60% of total income (2003 - 56%). Excluding acquisitions and at constant exchange rates, non-interest income was up 14%. Fees receivable were up 14% with good growth in lending, transmission and card related fees reflecting higher volumes. General insurance premium income more than doubled, reflecting volume growth in both motor and home insurance products, and the acquisition of Churchill in September 2003. In Financial Markets, volumes increased reflecting growth in customer-driven products such as interest rate protection, mortgage securitisation and foreign exchange. Income from rental assets grew by 22% to £618 million, reflecting growth in both the operating lease and investment property portfolios.

### **Net interest margin**

The Group's net interest margin at 2.92% was in line with expectations. Excluding the acquisition of First Active, the Group's net interest margin was 2.94% down from 2.96% in 2003, principally as a result of the increased levels of mortgage business and the funding cost of growth in rental assets, the income from which is included in other income.

### **Operating expenses**

Operating expenses, excluding goodwill amortisation and integration costs, rose by 14% to £4,615 million in support of strong growth in business volumes together with investment expenditure relating to efficiency enhancement and business development initiatives. Excluding acquisitions and at constant exchange rates, operating expenses were up by 10%, £422 million.

**Cost:income ratio**

As income growth has exceeded the growth in expenses, the Group's ratio of operating expenses (excluding goodwill amortisation and integration costs and after netting operating lease depreciation against rental income) to total income improved further to 40.5% from 43.0%.

**Net insurance claims**

General insurance claims, after reinsurance, increased by 106% to £1,723 million. Excluding Churchill, the increase was 21%, consistent with volume growth in the component parts of RBS Insurance.

**Provisions**

The profit and loss charge for bad and doubtful debts and amounts written off fixed asset investments was £751 million compared with £742 million in the first half of 2003. This reflects an improving trend overall, with the annualised charge for bad and doubtful debts in 2004 representing 0.49% of gross loans and advances to customers compared with 0.59% for the first half of 2003.

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THE ROYAL BANK OF SCOTLAND GROUP plc

### **Financial Review (continued)**

#### **Credit quality**

There has been no material change during the first half of 2004 in the distribution by grade of the Group's total risk assets.

The ratio of risk elements in lending to gross loans and advances to customers improved to 1.76% at 30 June 2004 (31 December 2003 2.01%; 30 June 2003 2.01%).

Risk elements in lending and potential problem loans represented 1.92% of gross loans and advances to customers at 30 June 2004 (31 December 2003 2.24%; 30 June 2003 2.40%).

Provision coverage of risk elements in lending and potential problem loans improved to 71% at 30 June 2004 (31 December 2003 68%; 30 June 2003 65%).

#### **Integration**

Integration costs in the first half of 2004 were £57 million principally relating to the integration of Churchill and Citizens' acquisitions.

#### **Earnings and dividends**

Basic earnings per ordinary share increased by 17%, from 60.0p to 69.9p. Earnings per ordinary share, adjusted for goodwill amortisation and integration costs, increased by 10%, from 76.5p to 84.4p.

An interim dividend of 16.8p per ordinary share, an increase of 15%, will be paid on 8 October 2004 to shareholders registered on 13 August 2004. The interim dividend is covered 4.8 times by earnings before goodwill amortisation and integration costs.

#### **Balance sheet**



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Total assets were £519 billion at 30 June 2004, 14% higher than total assets of £455 billion at 31 December 2003.

Lending to customers, excluding repurchase agreements and stock borrowing ( reverse repos ), increased in the first half of 2004 by 12% or £27 billion to £255 billion. Customer deposits, excluding repurchase agreements and stock lending ( repos ), grew in the first half of 2004 by 5% or £11 billion to £221 billion. Compared with 30 June 2003, average loans and advances to customers increased by 15%, £30 billion, and average customer deposits were up 8%, £15 billion.

Capital ratios at 30 June 2004 were 8.1% (tier 1) and 12.5% (total), against 7.4% (tier 1) and 11.8% (total) at 31 December 2003.

### **Profitability**

The adjusted after-tax return on ordinary equity was 18.9% compared with 18.2% for the first half of 2003. This is based on profit attributable to ordinary shareholders before goodwill amortisation and integration costs, and average ordinary equity.

### **Acquisitions**

The Group made a number of acquisitions during the first half of 2004. These included:

In January 2004, Ulster Bank completed the acquisition of First Active plc, for a cash consideration of 887 million.

In March 2004, RBS completed the purchase of the credit card portfolio of People's Bank in the US.

In May 2004, Citizens announced the acquisition of Charter One Financial, Inc. for a cash consideration of approximately US\$10.5 billion. This transaction is subject to regulatory and Charter One shareholder approval and is expected to be completed by the fourth quarter of 2004.

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THE ROYAL BANK OF SCOTLAND GROUP plc

**SUMMARY CONSOLIDATED PROFIT AND LOSS ACCOUNT****FOR THE HALF YEAR ENDED 30 JUNE 2004 (unaudited)**

In the profit and loss account set out below goodwill amortisation and integration costs are shown separately. In the statutory profit and loss account on page 27, these items are included in the captions prescribed by the Companies Act 1985.

|   | First half    | First half | Full year |
|---|---------------|------------|-----------|
|   | 2004          | 2003       | 2003      |
|   | £m            | £m         | £m        |
| <b>Net interest income</b>  | <b>4,378</b>  | 4,025      | 8,301     |
| Non-interest income (excluding general insurance)                     | 4,146         | 3,878      | 7,805     |
| General insurance net premium income                                  | 2,416         | 1,177      | 3,123     |
| <b>Non-interest income</b>  | <b>6,562</b>  | 5,055      | 10,928    |
| <b>Total income</b>   | <b>10,940</b> | 9,080      | 19,229    |
| <b>Operating expenses</b>   | <b>4,615</b>  | 4,051      | 8,389     |
| <b>Profit before other operating charges</b>                          | <b>6,325</b>  | 5,029      | 10,840    |
| General insurance net claims  | 1,723         | 836        | 2,195     |
| <b>Operating profit before provisions</b>                             | <b>4,602</b>  | 4,193      | 8,645     |
| Provisions  | 751           | 742        | 1,494     |
| <b>Profit before tax, goodwill amortisation and integration costs</b> | <b>3,851</b>  | 3,451      | 7,151     |
| Goodwill amortisation   | 413           | 373        | 763       |
| Integration costs   | 57            | 182        | 229       |
| <b>Profit before tax</b>  | <b>3,381</b>  | 2,896      | 6,159     |
| Tax   | 1,048         | 927        | 1,910     |
| <b>Profit after tax</b>   | <b>2,333</b>  | 1,969      | 4,249     |
| Minority interests (including non-equity)                             | 111           | 87         | 210       |
| Preference dividends  | 116           | 137        | 261       |
|   | <b>2,106</b>  | 1,745      | 3,778     |
| Additional Value Shares dividend                                      |               |            | 1,463     |
| <b>Profit attributable to ordinary shareholders</b>                   | <b>2,106</b>  | 1,745      | 2,315     |

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|  |              |              |               |
|--|--------------|--------------|---------------|
| Ordinary dividends                                   | <u>529</u>   | <u>431</u>   | <u>1,490</u>  |
| <b>Retained profit</b>                               | <u>1,577</u> | <u>1,314</u> | <u>825</u>    |
| <b>Basic earnings per ordinary share (Note 4)</b>    | <u>69.9p</u> | <u>60.0p</u> | <u>79.0p</u>  |
| <b>Adjusted earnings per ordinary share (Note 4)</b> | <u>84.4p</u> | <u>76.5p</u> | <u>159.3p</u> |

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**DIVISIONAL PERFORMANCE**

The contribution of each division before goodwill amortisation and integration costs and, where appropriate, Manufacturing costs is detailed below.

|  | First half<br>2004 | First half<br>2003 | Increase  | Full year<br>2003 |
|--|--------------------|--------------------|-----------|-------------------|
|  | £m                 | £m                 | %         | £m                |
| Corporate Banking and Financial Markets                          | 2,041              | 1,739              | 17        | 3,620             |
| Retail Banking*  | 1,642              | 1,554              | 6         | 3,170             |
| Retail Direct*   | 480                | 411                | 17        | 881               |
| Manufacturing*   | (1,122)            | (962)              | (17)      | (2,033)           |
| Wealth Management*   | 231                | 204                | 13        | 402               |
| RBS Insurance*   | 395                | 255                | 55        | 609               |
| Ulster Bank  | 170                | 131                | 30        | 273               |
| Citizens   | 423                | 425                |           | 857               |
| Central items  | (409)              | (306)              | (34)      | (628)             |
| <b>Profit before goodwill amortisation and integration costs</b> | <b>3,851</b>       | <b>3,451</b>       | <b>12</b> | <b>7,151</b>      |

\* prior periods have been restated to reflect the transfer in 2004 of certain activities from Wealth Management to Retail Banking and from other divisions, principally RBS Insurance, to Manufacturing (see page 50).

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THE ROYAL BANK OF SCOTLAND GROUP plc

**CORPORATE BANKING AND FINANCIAL MARKETS**

|   | First half<br>2004 | First half<br>2003 | Full year<br>2003 |
|---|--------------------|--------------------|-------------------|
|   | £m                 | £m                 | £m                |
| Net interest income excluding funding cost of rental assets | 1,425              | 1,297              | 2,653             |
| Funding cost of rental assets                               | (197)              | (151)              | (329)             |
| <b>Net interest income</b>                                  | <b>1,228</b>       | <b>1,146</b>       | <b>2,324</b>      |
| Fees and commissions receivable                             | 808                | 704                | 1,537             |
| Fees and commissions payable                                | (137)              | (101)              | (220)             |
| Dealing profits (before associated direct costs)            | 1,005              | 913                | 1,661             |
| Income on rental assets                                     | 618                | 507                | 1,088             |
| Other operating income                                      | 160                | 125                | 307               |
| <b>Non-interest income</b>                                  | <b>2,454</b>       | <b>2,148</b>       | <b>4,373</b>      |
| <b>Total income</b>   | <b>3,682</b>       | <b>3,294</b>       | <b>6,697</b>      |
| Direct expenses   |                    |                    |                   |
| - staff costs   | 813                | 710                | 1,410             |
| - other   | 210                | 189                | 394               |
| - operating lease depreciation                              | 303                | 252                | 518               |
|   | <b>1,326</b>       | <b>1,151</b>       | <b>2,322</b>      |
| <b>Contribution before provisions</b>                       | <b>2,356</b>       | <b>2,143</b>       | <b>4,375</b>      |
| Provisions  | 315                | 404                | 755               |
| <b>Contribution</b>   | <b>2,041</b>       | <b>1,739</b>       | <b>3,620</b>      |
|   | <b>£bn</b>         | <b>£bn</b>         | <b>£bn</b>        |
| <b>Total assets**</b>                                       | <b>251.0</b>       | <b>234.4</b>       | <b>219.0</b>      |
| Loans and advances to customers gross**                     |                    |                    |                   |
| - banking book  | 106.4              | 98.1               | 99.3              |
| - trading book  | 6.5                | 5.9                | 5.0               |
| Rental assets   | 10.8               | 7.7                | 10.1              |
| Customer deposits**   | 71.3               | 67.6               | 68.6              |
| Weighted risk assets banking                                | 150.0              | 139.9              | 140.0             |
| trading   | 13.6               | 13.2               | 12.6              |

\*\* excluding reverse repos and repos

**Corporate Banking and Financial Markets ( CBFM )** is the largest provider of banking services and structured financing to medium and large businesses in the UK with a growing presence for debt financing and risk management solutions to large businesses in Europe and North America. It supplies an integrated range of products and services to mid-sized and large corporate and institutional customers in the UK and overseas, including corporate and commercial banking, treasury and capital markets products, structured and acquisition finance, trade finance, leasing and factoring. Treasury and capital markets products are offered through Financial Markets, which is a leading provider of debt, foreign exchange and derivatives products.

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**CORPORATE BANKING AND FINANCIAL MARKETS (continued)**

Contribution increased compared with the first half of 2003 by 17% or £302 million to £2,041 million reflecting growth in all business areas.

Total income was up 12% or £388 million to £3,682 million. Strong growth in all locations was partially masked by the effect of stronger sterling on the translation of income from businesses in Europe and North America. At constant exchange rates, income rose by 14% and contribution was up by 20%.

Net interest income, excluding the cost of funding rental assets, increased 10% or £128 million to £1,425 million. In the banking businesses, average loans and advances to customers increased by 7% or £6.6 billion to £99.6 billion and average customer deposits increased by 7% or £4.4 billion to £64.1 billion. Net interest margin improved due to strong growth in our UK small and medium sized relationships.

Despite subdued demand from the large corporate sector, fees receivable rose by £104 million, 15% to £808 million with growth driven by lending, structured finance and capital markets activities. Fees payable including brokerage were up £36 million to £137 million due to greater volumes in the trading and structuring businesses.

Dealing profits, which is income before associated direct costs from our role in servicing customer demand for interest and currency rate protection and asset-backed securitisation, rose by 10% to £1,005 million. Favourable customer activity resulting from the movements in the major world currencies assisted the growth in the currency rate protection business. In addition, increased diversification in customer dealing revenues in the US compensated for lower market volumes for residential mortgage re-financing than in the same period in 2003.

The asset rental business, comprising operating lease assets and investment properties continued to grow strongly. Average rental assets increased to £10.6 billion and net income after deducting funding costs and operating lease depreciation increased by 13%, £14 million to £118 million.

Other operating income also grew strongly, up £35 million, 28% to £160 million.

Direct expenses increased by 15% or £175 million to £1,326 million. Excluding operating lease depreciation, operating expenses were up 14%, £124 million. This was mainly due to the mix effect of faster growth in businesses with inherently higher cost income ratios, such as Capital Markets and our overseas businesses together with the impact of investment spend in new revenue initiatives in the US. Revenue in our UK franchise continued to grow at a rate faster than costs.

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The charge for provisions for bad debts and amounts written off fixed asset investments amounted to £315 million, a decrease of 22%, £89 million compared with the first half of 2003. The reduction reflects a continuing improvement in corporate credit quality and economic environment.



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THE ROYAL BANK OF SCOTLAND GROUP plc

**RETAIL BANKING**

|                                       | First half<br>2004<br>£m | First half<br>2003*<br>£m | Full year<br>2003*<br>£m |
|---------------------------------------|--------------------------|---------------------------|--------------------------|
| Net interest income                   | 1,514                    | 1,437                     | 2,959                    |
| Non-interest income                   | 817                      | 731                       | 1,514                    |
| <b>Total income</b>                   | <b>2,331</b>             | <b>2,168</b>              | <b>4,473</b>             |
| <b>Direct expenses</b>                |                          |                           |                          |
| - staff costs                         | 403                      | 381                       | 793                      |
| - other                               | 100                      | 98                        | 237                      |
|                                       | <b>503</b>               | <b>479</b>                | <b>1,030</b>             |
| <b>Contribution before provisions</b> | <b>1,828</b>             | <b>1,689</b>              | <b>3,443</b>             |
| Provisions                            | 186                      | 135                       | 273                      |
| <b>Contribution</b>                   | <b>1,642</b>             | <b>1,554</b>              | <b>3,170</b>             |
|                                       | <b>£bn</b>               | <b>£bn</b>                | <b>£bn</b>               |
| Total banking assets                  | 70.2                     | 60.0                      | 63.9                     |
| Loans and advances to customers gross |                          |                           |                          |
| - mortgages                           | 41.2                     | 33.6                      | 36.6                     |
| - other                               | 26.9                     | 24.2                      | 25.2                     |
| Customer deposits                     | 68.9                     | 64.2                      | 66.5                     |
| Weighted risk assets                  | 47.6                     | 41.2                      | 42.9                     |

\* prior periods have been restated to reflect the transfer in 2004 of certain activities from Wealth Management.

**Retail Banking** comprises both The Royal Bank of Scotland and NatWest retail brands. It offers a full range of banking products and related financial services to the personal, premium and small business markets through a network of branches, telephone, ATMs and the internet.

The division continued to achieve strong volume growth across all key product areas – current accounts, mortgages, loans and savings. Income increased by 8% or £163 million to £2,331 million, and contribution by 6% or £88 million to £1,642 million.

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Net interest income rose by 5% or £77 million to £1,514 million, reflecting the continued growth in customer advances and the strong growth in mortgage lending which is lower risk and finer margin. Average loans to customers, excluding mortgages, grew by 11% or £2.5 billion to £25.7 billion. Average mortgage lending grew by 18% or £6.0 billion to £38.6 billion. Average customer deposits increased by 8% or £4.9 billion to £64.6 billion. A change in the mix with a higher bias towards mortgage lending led to a reduction in net interest margin. The number of personal customers increased by 459,000 and small business customers by 26,000 since June 2003.

Non-interest income rose by 12% or £86 million to £817 million. This reflected solid growth in general insurance commission income and higher investment business income, including bancassurance.

Direct expenses increased by 5% or £24 million to £503 million. Staff expenses increased 6% or £22 million to £403 million partly due to investment in additional customer facing staff. Other expenses increased by 2% or £2 million to £100 million reflecting tight cost management.

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**RETAIL BANKING (continued)**

The charge for provisions for bad and doubtful debts increased by £51 million to £186 million. The increased charge reflects growth in lending over recent years particularly in NatWest since its acquisition, together with a higher incidence of fraud, which has resulted in some deterioration in recovery rates.

The overall quality of the loan portfolio, by probability of default gradings, is in line with expectations.

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THE ROYAL BANK OF SCOTLAND GROUP plc

**RETAIL DIRECT**

|   | First half | First half | Full year    |
|---|------------|------------|--------------|
|   | 2004       | 2003*      | 2003*        |
|   | £m         | £m         | £m           |
| Net interest income                     | 453        | 400        | 849          |
| Non-interest income                     | 544        | 468        | 986          |
| <b>Total income</b>                     | <b>997</b> | <b>868</b> | <b>1,835</b> |
| <b>Direct expenses</b>                  |            |            |              |
| - staff costs                           | 120        | 101        | 211          |
| - other                                 | 225        | 209        | 446          |
|   | <b>345</b> | <b>310</b> | <b>657</b>   |
| Contribution before provisions          | 652        | 558        | 1,178        |
| Provisions                              | 172        | 147        | 297          |
| <b>Contribution</b>                     | <b>480</b> | <b>411</b> | <b>881</b>   |
|   | <b>£bn</b> | <b>£bn</b> | <b>£bn</b>   |
| Total assets                            | 25.9       | 20.3       | 21.9         |
| Loans and advances to customers - gross |            |            |              |
| - mortgages                             | 8.8        | 7.6        | 8.2          |
| - other                                 | 16.4       | 12.9       | 13.8         |
| Customer deposits                       | 4.4        | 4.5        | 4.4          |
| Weighted risk assets                    | 20.4       | 15.3       | 16.8         |

\* prior periods have been restated to reflect the transfer in 2004 of certain activities to Manufacturing.

**Retail Direct** issues a comprehensive range of credit, charge and debit cards to personal and corporate customers and engages in merchant acquisition and processing facilities for retail businesses. It also includes: Tesco Personal Finance ( TPF ), The One account, Direct Line Financial Services, Lombard Direct, WorldPay Limited, the Group's internet banking platform, the Primeline brand, and the consumer lending business in Continental Europe, all of them offering products to customers through direct channels. In March 2004, RBS completed the purchase of the credit card portfolio from People's Bank in the US and, in May 2004, completed the acquisition of Bibit, the international internet payment specialist.

Contribution increased by 17% or £69 million to £480 million.

Total income was up 15% or £129 million to £997 million, reflecting continued strong growth in cards, supermarket banking (TPF), mortgages and personal loans. Net interest income was up 13% or £53 million to £453 million. Average lending rose by 21% to £23.4 billion, of which average mortgage lending was 18% higher at £8.5 billion mainly in The One account. Average customer deposits were £4.3 billion. The new MINT branded credit card was launched successfully in December 2003 to replace RBS Advanta. By the end of June, MINT had issued 560,000 credit cards and had attracted significant balances with a 0% introductory interest rate for nine months, leading to a reduction in Retail Direct's net interest margin in the first half of 2004. During the twelve months to 30 June 2004, the total number of customer accounts increased by 3.1 million, of which 1.9 million was in the first half of 2004.

Non-interest income was up 16% or £76 million to £544 million. Increased volumes led to good growth in fee income generally.

Direct expenses increased by 11% or £35 million to £345 million. Staff costs were up 19%, due to increased headcount to support higher business volumes and the impact of acquisitions. Other expenses increased by 8%, with increased processing and operational costs in support of significantly higher business levels.

The charge for provisions for bad debts increased by £25 million or 17% to £172 million, reflecting the growth in lending volumes and the acquisition of the credit card portfolio from People's Bank. Credit metrics across the portfolio remain stable.

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THE ROYAL BANK OF SCOTLAND GROUP plc

**MANUFACTURING**

|  | First half<br>2004 | First half<br>2003* | Full year<br>2003* |
|--|--------------------|---------------------|--------------------|
|  | £m                 | £m                  | £m                 |
| Staff costs                              | 377                | 293                 | 644                |
| Other costs                              | 745                | 669                 | 1,389              |
| <b>Total manufacturing costs</b>         | <b>1,122</b>       | <b>962</b>          | <b>2,033</b>       |
| <b>Analysis:</b>                         |                    |                     |                    |
| Group Technology                         | 391                | 319                 | 686                |
| Group Purchasing and Property Operations | 403                | 352                 | 718                |
| Customer Support and other operations    | 328                | 291                 | 629                |
| <b>Total manufacturing costs</b>         | <b>1,122</b>       | <b>962</b>          | <b>2,033</b>       |

\* prior periods have been restated to reflect the transfer in 2004 of certain activities from RBS Insurance. These increased costs by £78 million in the first half of 2004; £37 million in the first half of 2003 and £109 million for the full year 2003.

**Manufacturing** 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.

*Manufacturing drives optimum 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 has become the centre of excellence for managing large scale and complex change.*

*The expenditure incurred by Manufacturing relates to shared costs principally in respect of the Group's UK banking and insurance operations. These costs reflect activities which are shared between the various customer-facing divisions and consequently cannot be directly attributed to individual divisions. Instead, the Group monitors and controls each of its customer-facing divisions on revenue generation and direct costs whilst in Manufacturing such control is exercised through appropriate efficiency measures and targets.*

Manufacturing's costs increased by £160 million, 17% to £1,122 million.

Of the £160 million increase, £50 million reflects technology and property operations transferred from Churchill with effect from January 2004 to Manufacturing, which is now supporting both Direct Line and Churchill. The balance of the increase in costs was required to support higher business volumes, to upgrade the Group's regional property portfolio and to invest in Group Efficiency Programme initiatives which are expected

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to improve the Group's efficiency in future. A number of initiatives were introduced in the first half of 2004, including a sales prompt system on screens in NatWest branches and in RBS and NatWest telephony, enhanced fraud prevention and the conversion of branch reports from paper to screen. Further initiatives planned for the second half of 2004 include the roll-out of image and workflow capability to service centres, the introduction of a new mortgage platform which will replace seven separate mortgage platforms across the Group and the introduction of an on-line customer query management system.

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THE ROYAL BANK OF SCOTLAND GROUP plc

**WEALTH MANAGEMENT**

|   | First half<br>2004 | First half<br>2003* | Full year<br>2003* |
|---|--------------------|---------------------|--------------------|
|   | £m                 | £m                  | £m                 |
| Net interest income                             | 243                | 221                 | 457                |
| Non-interest income                             | 210                | 176                 | 352                |
| <b>Total income</b>                             | <b>453</b>         | <b>397</b>          | <b>809</b>         |
| <b>Expenses</b>                                 |                    |                     |                    |
| - staff costs                                   | 141                | 131                 | 259                |
| - other   | 79                 | 65                  | 139                |
|   | 220                | 196                 | 398                |
| Contribution before provisions                  | 233                | 201                 | 411                |
| Provisions                                      | (2)                | 3                   | (9)                |
| <b>Contribution</b>                             | <b>231</b>         | <b>204</b>          | <b>402</b>         |
|   | £bn                | £bn                 | £bn                |
| Total assets                                    | 14.4               | 14.0                | 15.2               |
| Investment management assets excluding deposits | 21.9               | 16.8                | 22.3               |
| Customer deposits                               | 30.7               | 29.5                | 29.1               |
| Weighted risk assets                            | 8.8                | 8.7                 | 9.1                |

\* prior periods have been restated to reflect the transfer in 2004 of certain activities to Retail Banking and Manufacturing. This includes £5 billion of investment assets managed by the Affluent Banking business.

**Wealth Management** comprises Coutts Group, Adam & Company, The Royal Bank of Scotland International, and NatWest Offshore. The Miami based private banking operations of Coutts Group were sold to Santander Central Hispano in July 2003, and in November 2003, Coutts Group completed the acquisition of Bank von Ernst.

Contribution at £231 million was £27 million or 13% higher than 2003.

Total income increased by 14% or £56 million to £453 million.



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Net interest income increased by 10% or £22 million to £243 million. The increase is largely due to growth in lending volumes and the benefit of higher interest rates on deposit income together with the initial contribution from Bank von Ernst, which was acquired in November 2003.

Non-interest income increased by 19% or £34 million to £210 million, reflecting higher fee income as a result of the improvement in equity markets.

Investment management assets increased by £5.1 billion or 30% to £21.9 billion.

Expenses were up by 12% or £24 million to £220 million, reflecting inflation related increases together with the impact of the acquisition of Bank von Ernst.

The charge for provisions for bad and doubtful debts was £2 million compared with a net release of provisions of £3 million in the first half of 2003.

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**RBS INSURANCE**

|                                     | First half<br>2004 | First half<br>2003* | Full year<br>2003* |
|-------------------------------------|--------------------|---------------------|--------------------|
|                                     | £m                 | £m                  | £m                 |
| Earned premiums                     | 2,631              | 1,387               | 3,627              |
| Reinsurers share                    | (215)              | (210)               | (504)              |
| Insurance premium income            | 2,416              | 1,177               | 3,123              |
| Net fees and commissions            | (210)              | (7)                 | (161)              |
| Other income                        | 213                | 111                 | 283                |
| <b>Total income</b>                 | <b>2,419</b>       | <b>1,281</b>        | <b>3,245</b>       |
| <b>Expenses</b>                     |                    |                     |                    |
| - staff costs                       | 152                | 90                  | 222                |
| - other                             | 149                | 100                 | 219                |
|                                     | 301                | 190                 | 441                |
| Gross claims                        | 1,827              | 1,002               | 2,644              |
| Reinsurers share                    | (104)              | (166)               | (449)              |
| Net claims                          | 1,723              | 836                 | 2,195              |
| Contribution                        | 395                | 255                 | 609                |
| <b>In-force policies (000)</b>      |                    |                     |                    |
| - motor: UK                         | 8,109              | 4,861               | 8,086              |
| - motor: Continental Europe         | 1,538              | 1,308               | 1,425              |
| - home: UK                          | 5,125              | 1,647               | 5,154              |
| Gross insurance reserves total (£m) | 7,024              | 3,323               | 6,582              |

\* prior periods have been restated to reflect the transfer in 2004 of certain activities to Manufacturing and to recognise a reclassification of income from net fees and commissions to insurance premium income.

**RBS Insurance** comprising Direct Line Group and Churchill Insurance Group, which was acquired in September 2003, sells and underwrites retail, commercial and wholesale insurance on the telephone, the internet, and through brokers and intermediaries. The Retail Divisions of Direct Line and Churchill sell general insurance and motor breakdown services direct to the customer. The Partnership Division is a leading wholesale provider of insurance and motoring related services. Through its International Division, Direct Line sells insurance in Spain, Germany and Italy. The Intermediary and Broker Division sells general insurance products through its network of brokers and intermediaries.

Contribution was boosted by the acquisition of Churchill and increased by 55% or £140 million to £395 million.

Total income was up 89% or £1,138 million to £2,419 million. Excluding Churchill, total income grew by 17%.

After reinsurance, insurance premium income was up 105% or £1,239 million to £2,416 million. Excluding Churchill, insurance premium income (net of reinsurance) grew by 18%. At 30 June 2004, the number of UK in-force motor insurance policies was 8.1 million, the number of UK in-force home insurance policies was 5.1 million and the number of in-force motor policies in Continental Europe was 1.5 million.

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**RBS INSURANCE (continued)**

Other income net of commissions payable was down from £104 million to £3 million. Excluding Churchill, which included £180 million commissions payable to brokers and intermediaries, other income was up 7% due to higher investment income.

Expenses increased by 58% or £111 million to £301 million. Excluding Churchill, expenses increased by 4%.

Net claims, after reinsurance, increased by 106% or £887 million to £1,723 million. Excluding Churchill, net claims increased by 21%, consistent with volume growth in the component parts and reflect a slight change in the mix of products.

The UK combined operating ratio, which includes manufacturing costs, was 92.7% compared with 91.2% for the full year 2003. Excluding Churchill, the UK ratio improved from 89.1% for the first half of 2003 to 89.0%.

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**ULSTER BANK**

|   | First half<br>2004 | First half<br>2003 | Full year<br>2003 |
|---|--------------------|--------------------|-------------------|
|   | £m                 | £m                 | £m                |
| Net interest income                     | 256                | 190                | 396               |
| Non-interest income                     | 95                 | 91                 | 185               |
| <b>Total income</b>                     | <b>351</b>         | <b>281</b>         | <b>581</b>        |
| <b>Expenses</b>                         |                    |                    |                   |
| - staff costs                           | 95                 | 79                 | 164               |
| - other                                 | 68                 | 53                 | 112               |
|   | <b>163</b>         | <b>132</b>         | <b>276</b>        |
| Contribution before provisions          | 188                | 149                | 305               |
| Provisions                              | 18                 | 18                 | 32                |
| <b>Contribution</b>                     | <b>170</b>         | <b>131</b>         | <b>273</b>        |
|   | <b>£bn</b>         | <b>£bn</b>         | <b>£bn</b>        |
| Total assets                            | 22.8               | 14.2               | 15.6              |
| Loans and advances to customers - gross |                    |                    |                   |
| - mortgages                             | 6.6                | 2.2                | 2.8               |
| - other                                 | 11.1               | 8.2                | 8.8               |
| Customer deposits                       | 11.9               | 9.0                | 9.7               |
| Weighted risk assets                    | 15.7               | 10.3               | 11.0              |
| Average exchange rate - /£              | 1.485              | 1.460              | 1.445             |
| Spot exchange rate - /£                 | 1.490              | 1.437              | 1.416             |

**Ulster Bank** provides a comprehensive range of retail and wholesale financial services in Northern Ireland and the Republic of Ireland. Retail Banking has a network of branches throughout Ireland and operates in the personal, commercial and wealth management sectors. Corporate Banking and Financial Markets provides a wide range of services in the corporate and institutional markets. In January 2004, Ulster Bank completed the acquisition of First Active plc.

Contribution increased by 30% or £39 million to £170 million.

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Total income increased by 25% or £70 million to £351 million reflecting strong volume growth, particularly in residential mortgages. Adjusting for First Active and the disposal in October 2003 of NCB Stockbrokers ( NCB ), income increased by 9%. The number of customers increased since June 2003 by 431,000, of which 376,000 relate to First Active.

Net interest income rose by 35% or £66 million to £256 million, reflecting strong growth in both average customer lending and deposits. Excluding First Active and NCB, net interest income increased by 9%. Overall net interest margin declined reflecting organic growth in mortgage loans together with the acquisition of First Active which has a preponderance of mortgage lending.

Non-interest income increased by £4 million to £95 million. Strong growth in lending fees and sales of treasury products was partially offset by reduced brokerage fees following the disposal of NCB.

Expenses increased by 23% or £31 million to £163 million. This reflected the annual pay award, additional costs to support the growth in business and the acquisition of First Active.

The charge for provisions for bad debts including First Active, was unchanged at £18 million reflecting improved asset quality.

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**CITIZENS**

|                                       | First half  | First half  | Full year    |
|---------------------------------------|-------------|-------------|--------------|
|                                       | 2004        | 2003        | 2003         |
|                                       | £m          | £m          | £m           |
| Net interest income                   | 645         | 638         | 1,310        |
| Non-interest income                   | 244         | 271         | 514          |
| <b>Total income</b>                   | <b>889</b>  | <b>909</b>  | <b>1,824</b> |
| <b>Expenses</b>                       |             |             |              |
| - staff costs                         | 242         | 254         | 505          |
| - other                               | 184         | 186         | 374          |
|                                       | <b>426</b>  | <b>440</b>  | <b>879</b>   |
| Contribution before provisions        | 463         | 469         | 945          |
| Provisions                            | 40          | 44          | 88           |
| <b>Contribution</b>                   | <b>423</b>  | <b>425</b>  | <b>857</b>   |
|                                       | <b>\$bn</b> | <b>\$bn</b> | <b>\$bn</b>  |
| Total assets                          | 79.5        | 68.2        | 76.8         |
| Loans and advances to customers gross | 47.4        | 37.5        | 43.5         |
| Customer deposits                     | 66.4        | 57.5        | 62.8         |
| Weighted risk assets                  | 52.6        | 44.1        | 50.8         |
| Average exchange rate - US\$/£        | 1.822       | 1.611       | 1.635        |
| Spot exchange rate - US\$/£           | 1.814       | 1.650       | 1.786        |

*Citizens is engaged in retail and corporate banking activities through its branch network in the states of Rhode Island, Connecticut, Massachusetts, New Hampshire, Pennsylvania, Delaware and New Jersey. Citizens was ranked eleventh largest commercial banking organisation in the US based on deposits as at 31 March 2004. In January 2004, Citizens completed the acquisition of Thistle Group Holdings, Co. the holding company of Roxborough Manayunk Bank which was converted to Citizens systems in February 2004. In May 2004, Citizens announced the acquisition of Charter One Financial, Inc. This transaction is subject to regulatory and Charter One shareholder approval and is expected to be completed by the fourth quarter of 2004.*

Contribution was affected by the weakening of the US dollar relative to sterling and at £423 million was down £2 million. In US dollar terms, contribution increased by 13% or \$86 million to \$771 million.

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Total income was up 11% or \$155 million to \$1,620 million. Since June 2003, Citizens increased its personal customer base by 262,000 accounts and its business customers by 34,000 due to growth through both traditional and supermarket branches, and the acquisitions of Port Financial, Community Bancorp and Roxborough Manayunk Bank.

Net interest income increased by 14% or \$147 million to \$1,176 million, reflecting strong organic growth in personal loans and deposits. Excluding the acquisitions, average loans were up 28% or \$9.6 billion and average deposits were up 15% or \$8.3 billion. The benefit from higher volumes more than offset the impact of lower interest rates on margins.

Non-interest income rose by 2% or \$8 million to \$444 million, reflecting growth in customer fees and a lower level of securities gains than in 2003.



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**CITIZENS (continued)**

Expenses increased by 9% or \$67 million to \$776 million, to support higher business volumes, a branch automation programme, and the expansion of traditional and supermarket banking in Mid Atlantic and New England.

Provisions were up \$2 million from \$71 million to \$73 million. Credit quality metrics remain strong.

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**CENTRAL ITEMS**

|                                  | First half | First half | Full year  |
|----------------------------------|------------|------------|------------|
|                                  | 2004       | 2003       | 2003       |
|                                  | £m         | £m         | £m         |
| Funding costs                    | 122        | 85         | 215        |
| Departmental and corporate costs | 287        | 221        | 413        |
| <b>Total Central items</b>       | <b>409</b> | <b>306</b> | <b>628</b> |

**The Centre** comprises group and corporate functions, such as capital raising, finance and human resources, which manage capital requirements and provide services to the operating divisions.

Total Central items increased by £103 million to £409 million.

Funding costs at £122 million, were up 44% or £37 million reflecting the funding of the various acquisitions undertaken by the Group since June 2003.

Central departmental costs and other corporate items at £287 million were £66 million or 30% higher than the first half of 2003. This is principally due to the centralisation of certain functions, higher pension costs and expenditure on Group-wide projects such as International Accounting Standards and Basel II.

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**AVERAGE BALANCE SHEET**

|  | First half 2004          |                |           | First half 2003          |                |           |
|--|--------------------------|----------------|-----------|--------------------------|----------------|-----------|
|  | Average<br>balance<br>£m | Interest<br>£m | Rate<br>% | Average<br>balance<br>£m | Interest<br>£m | Rate<br>% |
| <b>Assets</b>  |                          |                |           |                          |                |           |
| Treasury and other eligible bills                      |                          |                |           |                          |                |           |
| UK   | 620                      | 11             | 3.55      | 1,656                    | 27             | 3.26      |
| Overseas   | 63                       | 1              | 3.17      |                          |                |           |
| Loans and advances to banks                            |                          |                |           |                          |                |           |
| UK   | 13,870                   | 255            | 3.68      | 13,212                   | 230            | 3.48      |
| Overseas   | 9,617                    | 107            | 2.23      | 9,406                    | 107            | 2.28      |
| Loans and advances to customers                        |                          |                |           |                          |                |           |
| UK   | 181,086                  | 5,187          | 5.73      | 166,743                  | 4,671          | 5.60      |
| Overseas   | 56,105                   | 1,332          | 4.75      | 40,023                   | 1,020          | 5.10      |
| Debt securities  |                          |                |           |                          |                |           |
| UK   | 21,152                   | 373            | 3.53      | 22,683                   | 382            | 3.37      |
| Overseas   | 17,352                   | 362            | 4.17      | 18,160                   | 413            | 4.55      |
| Interest-earning assets - banking business             |                          |                |           |                          |                |           |
| UK   | 216,728                  | 5,826          | 5.38      | 204,294                  | 5,310          | 5.20      |
| Overseas   | 83,137                   | 1,802          | 4.34      | 67,589                   | 1,540          | 4.56      |
|  | 299,865                  | 7,628          | 5.09      | 271,883                  | 6,850          | 5.04      |
| - trading business                                     |                          |                |           |                          |                |           |
|  | 116,605                  |                |           | 91,946                   |                |           |
| Total interest-earning assets                          |                          |                |           |                          |                |           |
|  | 416,470                  |                |           | 363,829                  |                |           |
| Non-interest-earning assets                            |                          |                |           |                          |                |           |
|  | 68,672                   |                |           | 67,300                   |                |           |
| Total assets   |                          |                |           |                          |                |           |
|  | 485,142                  |                |           | 431,129                  |                |           |
| Percentage of assets applicable to Overseas operations |                          |                |           |                          |                |           |
|  | 31.9%                    |                |           | 32.0%                    |                |           |
| <b>Liabilities</b>                                     |                          |                |           |                          |                |           |
| Deposits by banks                                      |                          |                |           |                          |                |           |
| UK   | 33,253                   | 455            | 2.74      | 26,515                   | 338            | 2.55      |
| Overseas   | 13,628                   | 146            | 2.14      | 9,819                    | 110            | 2.24      |
| Customer accounts                                      |                          |                |           |                          |                |           |
| UK   | 139,263                  | 1,726          | 2.48      | 130,902                  | 1,513          | 2.31      |
| Overseas   | 45,604                   | 360            | 1.58      | 40,953                   | 366            | 1.79      |
| Debt securities in issue                               |                          |                |           |                          |                |           |

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|   |                 |       |      |          |       |       |
|---|-----------------|-------|------|----------|-------|-------|
| UK  | <b>34,054</b>   | 519   | 3.05 | 29,034   | 495   | 3.41  |
| Overseas  | <b>11,474</b>   | 88    | 1.53 | 9,674    | 64    | 1.32  |
| <b>Loan capital</b>   |                 |       |      |          |       |       |
| UK  | <b>16,834</b>   | 302   | 3.59 | 14,435   | 228   | 3.16  |
| Overseas  | <b>164</b>      | 5     | 6.10 | 156      | 8     | 10.26 |
| Internal funding of trading business                        | <b>(30,993)</b> | (351) | 2.27 | (22,218) | (297) | 2.67  |
| <b>Interest-bearing liabilities - banking business</b>      |                 |       |      |          |       |       |
| UK  | <b>193,325</b>  | 2,661 | 2.75 | 180,767  | 2,292 | 2.54  |
| Overseas  | <b>69,956</b>   | 589   | 1.68 | 58,503   | 533   | 1.82  |
|   | <b>263,281</b>  | 3,250 | 2.47 | 239,270  | 2,825 | 2.36  |
| - trading business  | <b>114,402</b>  |       |      | 88,778   |       |       |
| Total interest-bearing liabilities                          | <b>377,683</b>  |       |      | 328,048  |       |       |
| <b>Non-interest-bearing liabilities</b>                     |                 |       |      |          |       |       |
| - demand deposits   | <b>26,060</b>   |       |      | 24,130   |       |       |
| - other liabilities   | <b>51,660</b>   |       |      | 51,326   |       |       |
| Shareholders funds  | <b>29,739</b>   |       |      | 27,625   |       |       |
| Total liabilities   | <b>485,142</b>  |       |      | 431,129  |       |       |
| Percentage of liabilities applicable to Overseas operations | <b>30.3%</b>    |       |      | 31.1%    |       |       |

The analysis between UK and Overseas has been compiled on the basis of location of office. Interest receivable and interest payable on trading assets and liabilities are included in dealing profits.

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**AVERAGE INTEREST RATES, YIELDS, SPREADS AND MARGINS**

| <b>Average rate</b>                                  | <b>First half</b> | <b>First half</b> |
|--|-------------------|-------------------|
|  | <b>2004</b>       | <b>2003</b>       |
|  | <b>%</b>          | <b>%</b>          |
| The Group's base rate                                | <b>4.06</b>       | 3.80              |
| London inter-bank three month offered rates:         |                   |                   |
| Sterling   | <b>4.37</b>       | 3.72              |
| Eurodollar   | <b>1.21</b>       | 1.29              |
| Euro   | <b>2.07</b>       | 2.52              |
| Yields, spreads and margins of the banking business: |                   |                   |
| Gross yield  | <b>5.09</b>       | 5.04              |
| Group  | <b>5.38</b>       | 5.20              |
| UK   | <b>4.34</b>       | 4.56              |
| Overseas   |                   |                   |
| Interest spread                                      |                   |                   |
| Group  | <b>2.62</b>       | 2.68              |
| UK   | <b>2.63</b>       | 2.66              |
| Overseas   | <b>2.66</b>       | 2.74              |
| Net interest margin                                  |                   |                   |
| Group  | <b>2.92</b>       | 2.96              |
| UK   | <b>2.92</b>       | 2.95              |
| Overseas   | <b>2.92</b>       | 2.98              |

|  | <b>First half</b> | <b>First half</b> | <b>Full year</b> |
|--|-------------------|-------------------|------------------|
|  | <b>2004</b>       | <b>2003</b>       | <b>2003</b>      |
|  | <b>%</b>          | <b>%</b>          | <b>%</b>         |
| Gross yield on interest-earning assets of banking business | <b>5.09</b>       | 5.04              | 5.00             |
| Cost of interest-bearing liabilities of banking business   | <b>(2.47)</b>     | (2.36)            | (2.32)           |
| <b>Interest spread of banking business</b>                 | <b>2.62</b>       | 2.68              | 2.68             |
| Benefit from interest-free funds                           | <b>0.30</b>       | 0.28              | 0.29             |
| <b>Net interest margin of banking business</b>             | <b>2.92</b>       | 2.96              | 2.97             |

**Group**

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The net interest margin decreased from 2.96% to 2.92%. The interest spread declined 6 basis points from 2.68% to 2.62% principally reflecting a change in mix towards relatively lower margin mortgage business including the acquisition of First Active. This was partially offset by an increase in the benefit from interest-free funds, 2 basis points higher, reflecting both increased volumes, up £4 billion, and movements in interest rates.

### **UK**

Interest spread decreased by 3 basis points to 2.63% reflecting growth in the mortgage business partly offset by improvements in corporate lending margins. The benefit from interest-free funds was unchanged with a small decline in volumes compensated by movements in interest rates.

### **Overseas**

The continued tightening of asset spreads in the US, together with the growth in mortgage business following the acquisition of First Active, has resulted in an 8 basis point reduction in spread to 2.66%. This was partially offset by an increase in the benefit from interest-free funds, with higher volumes more than offsetting the effect of lower US dollar and Euro interest rates.

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**STATUTORY CONSOLIDATED PROFIT AND LOSS ACCOUNT****FOR THE HALF YEAR ENDED 30 JUNE 2004 (unaudited)**

In the consolidated profit and loss account set out below, goodwill amortisation and integration costs are included in the captions prescribed by the Companies Act 1985.

|   | First half<br>2004 | First half<br>2003 | Full year<br>2003<br>(Audited) |
|---|--------------------|--------------------|--------------------------------|
|   | £m                 | £m                 | £m                             |
| <b>Net interest income</b>                        | <b>4,378</b>       | 4,025              | 8,301                          |
| Non-interest income (excluding general insurance) | 4,146              | 3,878              | 7,805                          |
| General insurance net premium income              | 2,416              | 1,177              | 3,123                          |
| <b>Non-interest income</b>                        | <b>6,562</b>       | 5,055              | 10,928                         |
| <b>Total income</b>                               | <b>10,940</b>      | 9,080              | 19,229                         |
| Administrative expenses                           | 4,163              | 3,784              | 7,699                          |
| Depreciation and amortisation                     |                    |                    |                                |
| - tangible fixed assets                           | 509                | 449                | 919                            |
| - goodwill  | 413                | 373                | 763                            |
| <b>Operating expenses*</b>                        | <b>5,085</b>       | 4,606              | 9,381                          |
| <b>Profit before other operating charges</b>      | <b>5,855</b>       | 4,474              | 9,848                          |
| General insurance net claims                      | 1,723              | 836                | 2,195                          |
| <b>Operating profit before provisions</b>         | <b>4,132</b>       | 3,638              | 7,653                          |
| Provisions  | 751                | 742                | 1,494                          |
| <b>Profit on ordinary activities before tax</b>   | <b>3,381</b>       | 2,896              | 6,159                          |
| Tax on profit on ordinary activities              | 1,048              | 927                | 1,910                          |
| <b>Profit on ordinary activities after tax</b>    | <b>2,333</b>       | 1,969              | 4,249                          |
| Minority interests (including non-equity)         | 111                | 87                 | 210                            |
| <b>Profit after minority interests</b>            | <b>2,222</b>       | 1,882              | 4,039                          |
| Preference dividends                              | 116                | 137                | 261                            |

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|  |              |              |               |
|--|--------------|--------------|---------------|
|  | 2,106        | 1,745        | 3,778         |
| Additional Value Shares dividend                     |              |              | 1,463         |
| <b>Profit attributable to ordinary shareholders</b>  | <b>2,106</b> | <b>1,745</b> | <b>2,315</b>  |
| Ordinary dividends                                   | 529          | 431          | 1,490         |
| <b>Retained profit</b>                               | <b>1,577</b> | <b>1,314</b> | <b>825</b>    |
| <b>Basic earnings per ordinary share (Note 4)</b>    | <b>69.9p</b> | <b>60.0p</b> | <b>79.0p</b>  |
| <b>Adjusted earnings per ordinary share (Note 4)</b> | <b>84.4p</b> | <b>76.5p</b> | <b>159.3p</b> |
| <b>Diluted earnings per ordinary share (Note 4)</b>  | <b>69.5p</b> | <b>59.5p</b> | <b>78.4p</b>  |

\* Integration costs included in operating expenses comprise:

|                         | £m        | £m         | £m         |
|-------------------------|-----------|------------|------------|
| Administrative expenses | 55        | 181        | 229        |
| Depreciation            | 2         | 1          |            |
|                         | <b>57</b> | <b>182</b> | <b>229</b> |



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THE ROYAL BANK OF SCOTLAND GROUP plc

**CONSOLIDATED BALANCE SHEET****AT 30 JUNE 2004 (unaudited)**

|   | 30 June<br>2004 | 31 December<br>2003<br>(Audited) | 30 June<br>2003 |
|---|-----------------|----------------------------------|-----------------|
|   | £m              | £m                               | £m              |
| <b>Assets</b>   |                 |                                  |                 |
| Cash and balances at central banks                            | 3,140           | 3,822                            | 3,268           |
| Items in the course of collection from other banks            | 3,149           | 2,501                            | 3,729           |
| Treasury bills and other eligible bills                       | 6,902           | 4,846                            | 7,047           |
| Loans and advances to banks                                   | 60,152          | 51,891                           | 44,923          |
| Loans and advances to customers                               | 290,154         | 252,531                          | 248,726         |
| Debt securities   | 89,813          | 79,949                           | 73,328          |
| Equity shares   | 2,315           | 2,300                            | 2,150           |
| Interests in associated undertakings                          | 122             | 106                              | 91              |
| Intangible fixed assets                                       | 13,589          | 13,131                           | 12,514          |
| Tangible fixed assets   | 14,866          | 13,927                           | 11,638          |
| Settlement balances   | 10,288          | 2,857                            | 15,169          |
| Other assets  | 14,997          | 18,436                           | 19,026          |
| Prepayments and accrued income                                | 6,060           | 5,421                            | 4,074           |
|   | <b>515,547</b>  | <b>451,718</b>                   | <b>445,683</b>  |
| Long-term assurance assets attributable to policyholders      | 3,531           | 3,557                            | 3,462           |
| <b>Total assets</b>   | <b>519,078</b>  | <b>455,275</b>                   | <b>449,145</b>  |
| <b>Liabilities</b>  |                 |                                  |                 |
| Deposits by banks   | 84,120          | 67,323                           | 62,039          |
| Items in the course of transmission to other banks            | 996             | 958                              | 1,367           |
| Customer accounts   | 253,949         | 236,963                          | 225,697         |
| Debt securities in issue                                      | 51,721          | 41,016                           | 40,156          |
| Settlement balances and short positions                       | 38,058          | 21,369                           | 36,749          |
| Other liabilities   | 17,301          | 20,584                           | 22,343          |
| Accruals and deferred income                                  | 13,945          | 13,173                           | 8,399           |
| Provisions for liabilities and charges                        | 2,532           | 2,522                            | 2,202           |
| Subordinated liabilities                                      | 17,832          | 16,998                           | 15,696          |
| Minority interests  |                 |                                  |                 |
| - equity  | 27              | (11)                             | (23)            |
| - non-equity  | 2,658           | 2,724                            | 2,444           |
| Shareholders' funds   |                 |                                  |                 |
| - equity  | 29,541          | 25,176                           | 25,496          |
| - non-equity  | 2,867           | 2,923                            | 3,118           |
|   | <b>515,547</b>  | <b>451,718</b>                   | <b>445,683</b>  |
| Long-term assurance liabilities attributable to policyholders | 3,531           | 3,557                            | 3,462           |

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|  |                |         |         |
|--|----------------|---------|---------|
| <b>Total liabilities</b>               | <b>519,078</b> | 455,275 | 449,145 |
| <b>Memorandum items</b>                |                |         |         |
| Contingent liabilities and commitments | <b>173,316</b> | 154,557 | 138,933 |

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### **OVERVIEW OF CONSOLIDATED BALANCE SHEET**

Total assets of £519.1 billion at 30 June 2004 were up £63.8 billion, 14%, compared with 31 December 2003, reflecting business growth and acquisitions.

Treasury bills and other eligible bills increased by £2.1 billion, 42%, to £6.9 billion, reflecting trading activity.

Loans and advances to banks rose £8.3 billion, 16%, to £60.2 billion. Bank placings were up £5.1 billion, 20% to £30.5 billion, and reverse repurchase agreements and stock borrowing ( reverse repos ), were up £3.1 billion, 12%, to £29.7 billion.

Loans and advances to customers were up £37.6 billion, 15%, to £290.2 billion. Within this, reverse repos increased by 45%, £10.8 billion to £34.9 billion. Excluding reverse repos, lending increased by £26.8 billion, 12% to £255.3 billion reflecting organic growth across all divisions and £5.4 billion arising from acquisitions, principally First Active, £4.1 billion, and the People's Bank credit card business, £1.0 billion. Compared with 30 June 2003, loans and advances to customers were up £41.4 billion, 17%; excluding acquisitions, the growth was £34.5 billion, 14%.

Debt securities increased by £9.9 billion, 12%, to £89.8 billion, principally due to increased holdings in Financial Markets and the acquisition of First Active. This was partially offset by a reduction in Wealth Management's investment portfolio of investment grade asset-backed securities.

Intangible fixed assets increased by £0.5 billion, 3% to £13.6 billion. Goodwill arising on the acquisitions made during the first half of 2004 amounted to £0.9 billion. This was partially offset by goodwill amortisation, £0.4 billion and the adverse effect of exchange rate movements, £0.1 billion.

Tangible fixed assets were up £0.9 billion, 7% to £14.9 billion, reflecting growth in operating lease assets, up £0.8 billion, 12% to £7.1 billion.

Settlement balances increased by £7.4 billion to £10.3 billion as a result of increased levels of customer activity.

Other assets declined by £3.4 billion, 19% to £15.0 billion, mainly due to a decrease in the mark-to-market value of trading derivatives.

Deposits by banks increased by £16.8 billion, 25% to £84.1 billion to fund business growth, with repurchase agreements and stock lending ( repos ) up £6.0 billion, 22%, to £33.1 billion and inter-bank deposits up £10.8 billion, 27% to £51.0 billion.

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Customer accounts were up £17.0 billion, 7% at £253.9 billion. Within this, repos were up £6.3 billion, 23% to £33.3 billion. Excluding repos, deposits rose by £10.7 billion, 5%, to £220.6 billion with growth in CBFM, £2.7 billion, Retail Banking, £2.4 billion, Wealth Management, £1.6 billion, Citizens, £1.7 billion and Ulster Bank £2.5 billion, including First Active. In \$ terms, Citizens grew US\$4.0 billion, 7%, including US\$0.6 billion related to acquisitions. Customer accounts were up £28.3 billion, 13% compared with 30 June 2003; excluding acquisitions the increase was £23.9 billion, 11%.

Debt securities in issue increased by £10.7 billion, 26%, to £51.7 billion primarily to meet the Group's funding requirements.

The increase in settlement balances and short positions reflected growth in customer activity.

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**OVERVIEW OF CONSOLIDATED BALANCE SHEET (continued)**

Other liabilities declined by £3.3 billion, 16% to £17.3 billion, mainly due to a decrease in the mark-to-market value of trading derivatives.

Subordinated liabilities were up £0.8 billion, 5% to £17.8 billion. This reflected the issue of £0.7 billion (US\$1,250 million) US\$ denominated dated loan capital, and £0.5 billion undated loan capital, together with £0.1 billion of dated and undated loan capital arising from the acquisition of First Active. This was partially offset by the redemption of dated loan capital, £0.2 billion (US\$250 million and £40 million) and the effect of exchange rate movements, £0.3 billion.

Shareholders' funds increased by £4.3 billion, 15% to £32.4 billion including £2.6 billion from the placing of 165 million ordinary shares in connection with the proposed acquisition of Charter One. The remainder reflects retentions of £1.6 billion and the issue of £0.2 billion of ordinary shares in respect of scrip dividends and the exercise of share options which were partly offset by the adverse effect of exchange rate movements on share premium account, £0.1 billion.

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**STATEMENT OF CONSOLIDATED TOTAL RECOGNISED GAINS AND LOSSES****FOR THE HALF YEAR ENDED 30 JUNE 2004 (unaudited)**

|  | First half   | First half   | Full year    |
|--|--------------|--------------|--------------|
|  | 2004         | 2003         | 2003         |
|  | £m           | £m           | (Audited)    |
|  | £m           | £m           | £m           |
| Profit attributable to ordinary shareholders         | 2,106        | 1,745        | 2,315        |
| Currency translation adjustments and other movements | (30)         | 47           | 43           |
| Revaluation of premises                              |              |              | (69)         |
| <b>Total recognised gains in the period</b>          | <b>2,076</b> | <b>1,792</b> | <b>2,289</b> |

**RECONCILIATION OF MOVEMENTS IN CONSOLIDATED SHAREHOLDERS FUNDS****FOR THE HALF YEAR ENDED 30 JUNE 2004 (unaudited)**

|  | First half   | First half   | Full year  |
|--|--------------|--------------|------------|
|  | 2004         | 2003         | 2003       |
|  | £m           | £m           | (Audited)  |
|  | £m           | £m           | £m         |
| Profit attributable to ordinary shareholders             | 2,106        | 1,745        | 2,315      |
| Ordinary dividends                                       | (529)        | (431)        | (1,490)    |
| <b>Retained profit for the period</b>                    | <b>1,577</b> | <b>1,314</b> | <b>825</b> |
| Issue of ordinary shares                                 | 2,829        | 555          | 775        |
| Redemption of preference shares                          |              | (364)        | (364)      |
| Own shares held in relation to employee share schemes    | (7)          |              |            |
| Goodwill previously written off to reserves              |              | 40           | 40         |
| Other recognised gains and losses                        | (30)         | 47           | (26)       |
| Currency translation adjustment on share premium account | (60)         | (30)         | (203)      |

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|                                    |               |        |        |
|------------------------------------|---------------|--------|--------|
| Net increase in shareholders funds | <b>4,309</b>  | 1,562  | 1,047  |
| Opening shareholders funds         | <b>28,099</b> | 27,052 | 27,052 |
| Closing shareholders funds         | <b>32,408</b> | 28,614 | 28,099 |

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**CONSOLIDATED CASH FLOW STATEMENT****FOR THE HALF YEAR ENDED 30 JUNE 2004 (unaudited)**

|  | First half<br>2004<br>£m | First half<br>2003<br>£m | Full year<br>2003<br>(Audited)<br>£m |
|--|--------------------------|--------------------------|--------------------------------------|
| Net cash inflow from operating activities (note 10)                        | 3,689                    | 14,428                   | 19,708                               |
| Dividends received from associated undertakings                            | 8                        | 1                        | 9                                    |
| <b>Returns on investments and servicing of finance</b>                     |                          |                          |                                      |
| Preference dividends paid  | (136)                    | (140)                    | (269)                                |
| Additional Value Shares dividend paid                                      |                          |                          | (1,463)                              |
| Dividends paid to minority shareholders in subsidiary undertakings         | (72)                     | (60)                     | (130)                                |
| Interest paid on subordinated liabilities                                  | (340)                    | (322)                    | (557)                                |
| Net cash outflow from returns on investments and servicing of finance      | (548)                    | (522)                    | (2,419)                              |
| <b>Taxation</b>  |                          |                          |                                      |
| UK tax paid  | (212)                    | (359)                    | (933)                                |
| Overseas tax paid  | (237)                    | (233)                    | (521)                                |
| Net cash outflow from taxation   | (449)                    | (592)                    | (1,454)                              |
| <b>Capital expenditure and financial investment</b>                        |                          |                          |                                      |
| Purchase of investment securities  | (22,068)                 | (24,343)                 | (44,861)                             |
| Sale and maturity of investment securities                                 | 22,485                   | 20,775                   | 41,805                               |
| Purchase of tangible fixed assets  | (2,330)                  | (1,533)                  | (5,017)                              |
| Sale of tangible fixed assets  | 853                      | 395                      | 1,108                                |
| Net cash outflow from capital expenditure and financial investment         | (1,060)                  | (4,706)                  | (6,965)                              |
| <b>Acquisitions and disposals</b>  |                          |                          |                                      |
| Purchases of businesses and subsidiary undertakings (net of cash acquired) | (2,098)                  | (318)                    | (1,748)                              |
| Investment in associated undertakings                                      | (25)                     | (3)                      | (2)                                  |
| Sale of subsidiary and associated undertakings (net of cash sold)          | 3                        | 105                      | 179                                  |
| Net cash outflow from acquisitions and disposals                           | (2,120)                  | (216)                    | (1,571)                              |
| Ordinary equity dividends paid   | (999)                    | (396)                    | (772)                                |



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|   |         |       |        |
|---|---------|-------|--------|
| Net cash (outflow)/inflow before financing        | (1,479) | 7,997 | 6,536  |
| <b>Financing</b>                                  |         |       |        |
| Proceeds from issue of ordinary share capital     | 2,769   | 9     | 184    |
| Proceeds from issue of trust preferred securities |         | 512   | 883    |
| Redemption of preference share capital            |         | (364) | (364)  |
| Issue of subordinated liabilities                 | 1,193   | 1,731 | 3,817  |
| Repayment of subordinated liabilities             | (174)   | (40)  | (336)  |
| (Decrease)/increase in minority interests         | (1)     | 19    | (56)   |
| Net cash inflow from financing                    | 3,787   | 1,867 | 4,128  |
| Increase in cash                                  | 2,308   | 9,864 | 10,664 |

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**NOTES****1. Accounting policies**

There have been no changes to the Group's principal accounting policies as set out on pages 137 to 140 of the 2003 Report and Accounts.

**2. Provisions for bad and doubtful debts**

Operating profit is stated after charging provisions for bad and doubtful debts of £719 million (30 June 2003 - £746 million) and amounts written off fixed asset investments of £32 million (30 June 2003 - recovery of £4 million). The balance sheet provisions for bad and doubtful debts increased in the six months to 30 June 2004 from £3,929 million to £4,038 million, and the movements thereon were:

|  | Specific     | General    | First half<br>2004 | First half<br>2003 |
|--|--------------|------------|--------------------|--------------------|
|  | £m           | £m         | £m                 | £m                 |
| At 1 January                                 | 3,363        | 566        | 3,929              | 3,927              |
| Currency translation and other adjustments   | 29           | (71)       | (42)               | (6)                |
| Acquisitions                                 | 72           | 28         | 100                | 10                 |
| Amounts written off                          | (712)        |            | (712)              | (740)              |
| Recoveries of amounts previously written off | 44           |            | 44                 | 34                 |
| Charge to profit and loss account            | 691          | 28         | 719                | 746                |
| <b>At 30 June</b>                            | <b>3,487</b> | <b>551</b> | <b>4,038</b>       | <b>3,971</b>       |

The provision at 30 June 2004 includes provision against loans and advances to banks of £6 million (31 December 2003 - £7 million; 30 June 2003 - £7 million).

**3. Taxation**

The charge for taxation is based on a UK corporation tax rate of 30% and comprises:

| First half | First half | Full year |
|------------|------------|-----------|
|------------|------------|-----------|

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|  | 2004         | 2003       | 2003         |
|--|--------------|------------|--------------|
|  | £m           | £m         | £m           |
| Tax on profit before goodwill amortisation and integration costs | 1,081        | 1,001      | 2,012        |
| Tax relief on goodwill amortisation and integration costs        | (33)         | (74)       | (102)        |
|  | <u>1,048</u> | <u>927</u> | <u>1,910</u> |

The actual tax charge differs from the expected tax charge computed by applying the standard UK corporation tax rate of 30% as follows:

|   | First half   | First half | Full year    |
|---|--------------|------------|--------------|
|   | 2004         | 2003       | 2003         |
|   | £m           | £m         | £m           |
| Expected tax charge                     | 1,014        | 869        | 1,848        |
| Goodwill amortisation                   | 109          | 95         | 203          |
| Non-deductible items                    | 27           | 3          | 106          |
| Non-taxable items                       | (8)          | (34)       | (111)        |
| Other                                   | (14)         | (1)        | (24)         |
| Adjustments in respect of prior periods | (80)         | (5)        | (112)        |
|   | <u>1,048</u> | <u>927</u> | <u>1,910</u> |

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**NOTES (continued)****4. Earnings per share**

Earnings per share have been calculated based on the following:

|  | First half<br>2004<br>£m | First half<br>2003<br>£m | Full year<br>2003<br>£m |
|--|--------------------------|--------------------------|-------------------------|
| <b>Earnings</b>  |                          |                          |                         |
| Profit attributable to ordinary shareholders                         | 2,106                    | 1,745                    | 2,315                   |
|  | <b>Number of shares</b>  |                          |                         |
|  | <b>millions</b>          |                          |                         |
| <b>Weighted average number of ordinary shares</b>                    |                          |                          |                         |
| In issue during the period   | 3,013                    | 2,908                    | 2,931                   |
| Effect of dilutive share options and convertible non-equity shares   | 18                       | 26                       | 22                      |
| Diluted weighted average number of ordinary shares during the period | 3,031                    | 2,934                    | 2,953                   |
| <b>Basic earnings per share</b>                                      |                          |                          |                         |
| AVS dividend   | 69.9p                    | 60.0p                    | 79.0p                   |
|  |                          |                          | 49.9p                   |
|  | 69.9p                    | 60.0p                    | 128.9p                  |
| Goodwill amortisation  | 13.2p                    | 12.2p                    | 25.0p                   |
| Integration costs  | 1.3p                     | 4.3p                     | 5.4p                    |
| <b>Adjusted earnings per share</b>                                   | <b>84.4p</b>             | <b>76.5p</b>             | <b>159.3p</b>           |
| <b>Diluted earnings per share</b>                                    | <b>69.5p</b>             | <b>59.5p</b>             | <b>78.4p</b>            |

**5. Interim dividend**

The directors have declared an interim dividend of 16.8p per ordinary share which will be paid on 8 October 2004 to shareholders registered on 13 August 2004. As an alternative to cash, a scrip dividend election is to be offered and shareholders will receive details of this by letter.

## 6. Analysis of repurchase agreements

|  | 30 June | 31 December | 30 June |
|--|---------|-------------|---------|
|  | 2004    | 2003        | 2003    |
|  | £m      | £m          | £m      |
| <b>Reverse repurchase agreements and stock borrowing</b> |         |             |         |
| Loans and advances to banks                              | 29,659  | 26,522      | 15,140  |
| Loans and advances to customers                          | 34,892  | 24,069      | 30,443  |
| <b>Repurchase agreements and stock lending</b>           |         |             |         |
| Deposits by banks  | 33,067  | 27,044      | 20,644  |
| Customer accounts  | 33,343  | 27,021      | 19,595  |

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**NOTES (continued)****7. Contingent liabilities and commitments**

|   | 30 June           | 31 December       | 30 June           |
|---|-------------------|-------------------|-------------------|
|   | 2004              | 2003              | 2003              |
|   | £m                | £m                | £m                |
|   | <u>          </u> | <u>          </u> | <u>          </u> |
| <b>Contingent liabilities</b>   |                   |                   |                   |
| Acceptances and endorsements  | 349               | 595               | 2,268             |
| Guarantees and assets pledged as collateral security                          | 8,872             | 8,787             | 5,683             |
| Other contingent liabilities  | 5,827             | 5,482             | 8,232             |
|   | <u>15,048</u>     | <u>14,864</u>     | <u>16,183</u>     |
| <b>Commitments</b>  |                   |                   |                   |
| Documentary credits and other short-term trade related transactions           | 618               | 605               | 244               |
| Undrawn formal standby facilities, credit lines and other commitments to lend | 155,726           | 137,251           | 121,515           |
| Other commitments   | 1,924             | 1,837             | 991               |
|   | <u>158,268</u>    | <u>139,693</u>    | <u>122,750</u>    |
| <b>Total contingent liabilities and commitments</b>                           | <u>173,316</u>    | <u>154,557</u>    | <u>138,933</u>    |

**8. Derivatives****Replacement cost of over-the-counter contracts (trading and non-trading)**

The following table shows the gross replacement cost, which is the sum of the fair values, of all over-the-counter contracts with third parties (trading and non-trading) with positive value. This measure makes no allowance for netting arrangements.

|                         | 30 June           | 31 December       | 30 June           |
|-------------------------|-------------------|-------------------|-------------------|
|                         | 2004              | 2003              | 2003              |
|                         | £m                | £m                | £m                |
|                         | <u>          </u> | <u>          </u> | <u>          </u> |
| Exchange rate contracts | 16,269            | 28,163            | 20,941            |

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|                                |               |        |        |
|--------------------------------|---------------|--------|--------|
| Interest rate contracts        | <b>48,686</b> | 54,974 | 76,548 |
| Credit derivatives             | <b>185</b>    | 272    | 335    |
| Equity and commodity contracts | <b>1,437</b>  | 1,020  | 924    |
|                                | <b>66,577</b> | 84,429 | 98,748 |

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**NOTES (continued)****8. Derivatives (continued)****Derivatives held for trading purposes**

The table below shows the notional principal amounts of trading instruments entered into with third parties.

|                                | 30 June<br>2004<br>£bn | 31 December<br>2003<br>£bn | 30 June<br>2003<br>£bn |
|--------------------------------|------------------------|----------------------------|------------------------|
| <b>Exchange rate contracts</b> | <b>1,542.7</b>         | 1,144.7                    | 1,241.8                |
| Interest rate contracts        | <b>6,441.7</b>         | 5,307.8                    | 5,046.6                |
| Credit derivatives             | <b>32.3</b>            | 28.5                       | 25.6                   |
| Equity and commodity contracts | <b>47.8</b>            | 34.1                       | 28.3                   |

The table below shows the fair values (which, after netting, are the balance sheet values) of trading instruments entered into with third parties.

|                                | 30 June 2004    |                 | 31 December 2003 |             | 30 June 2003 |             |
|--------------------------------|-----------------|-----------------|------------------|-------------|--------------|-------------|
|                                | Fair value      |                 | Fair value       |             | Fair value   |             |
|                                | Assets          | Liabilities     | Assets           | Liabilities | Assets       | Liabilities |
|                                | £m              | £m              | £m               | £m          | £m           | £m          |
| Exchange rate contracts        | <b>16,219</b>   | <b>17,066</b>   | 28,102           | 29,564      | 20,905       | 22,392      |
| Interest rate contracts        | <b>48,006</b>   | <b>48,757</b>   | 54,266           | 54,212      | 76,030       | 76,418      |
| Credit derivatives             | <b>185</b>      | <b>114</b>      | 273              | 155         | 334          | 138         |
| Equity and commodity contracts | <b>1,315</b>    | <b>917</b>      | 924              | 720         | 867          | 599         |
|                                | <b>65,725</b>   | <b>66,854</b>   | 83,565           | 84,651      | 98,136       | 99,547      |
| Netting                        | <b>(55,319)</b> | <b>(55,319)</b> | (69,478)         | (69,478)    | (83,374)     | (83,374)    |
|                                | <b>10,406</b>   | <b>11,535</b>   | 14,087           | 15,173      | 14,762       | 16,173      |



**Derivatives held for purposes other than trading**

The Group uses derivatives to manage specific interest rate positions relating to assets and liabilities and to hedge foreign currency exposures. The Group establishes non-trading derivative positions with third parties and through intra-company and intra-Group transactions with the Group's independent trading operations. The table below shows the notional principal amounts of the Group's non-trading derivatives (third party and internal).

|                                | <b>30 June</b>    | <b>31 December</b> | <b>30 June</b>    |
|--------------------------------|-------------------|--------------------|-------------------|
|                                | <b>2004</b>       | <b>2003</b>        | <b>2003</b>       |
|                                | <b>£bn</b>        | <b>£bn</b>         | <b>£bn</b>        |
|                                | <u>          </u> | <u>          </u>  | <u>          </u> |
| Exchange rate contracts        | 22.4              | 26.5               | 16.3              |
| Interest rate contracts        | 158.6             | 135.1              | 126.1             |
| Credit derivatives             | 1.2               | 1.0                | 1.5               |
| Equity and commodity contracts | 2.1               | 1.7                | 1.7               |

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**NOTES (continued)****9. Analysis of consolidated shareholders funds**

|   | First half<br>2004 | First half<br>2003 | Full year<br>2003 |
|---|--------------------|--------------------|-------------------|
|   | £m                 | £m                 | £m                |
| <b>Called-up share capital</b>                                |                    |                    |                   |
| At beginning of period  | 769                | 754                | 754               |
| Shares issued during the period                               | 44                 | 10                 | 15                |
| At end of period  | 813                | 764                | 769               |
| <b>Share premium account</b>                                  |                    |                    |                   |
| At beginning of period  | 8,175              | 7,608              | 7,608             |
| Currency translation adjustments                              | (60)               | (30)               | (203)             |
| Shares issued during the period                               | 2,785              | 557                | 760               |
| Other movements   | 4                  | 6                  | 10                |
| At end of period  | 10,904             | 8,141              | 8,175             |
| <b>Merger reserve</b>   |                    |                    |                   |
| At beginning of period  | 10,881             | 11,455             | 11,455            |
| Transfer to profit and loss account                           | (287)              | (287)              | (574)             |
| At end of period  | 10,594             | 11,168             | 10,881            |
| <b>Revaluation reserve</b>                                    |                    |                    |                   |
| At beginning of period  | 7                  | 80                 | 80                |
| Revaluation of premises                                       |                    |                    | (69)              |
| Transfer to profit and loss account                           |                    |                    | (4)               |
| At end of period  | 7                  | 80                 | 7                 |
| <b>Other reserves</b>   |                    |                    |                   |
| At beginning of period  | 419                | 387                | 387               |
| Transfer of increase in value of long-term assurance business | 17                 | 10                 | 32                |
| At end of period  | 436                | 397                | 419               |
| <b>Profit and loss account</b>                                |                    |                    |                   |
| At beginning of period  | 7,848              | 6,768              | 6,768             |
| Currency translation adjustments and other movements          | (34)               | 29                 | 33                |
| Retention for the period                                      | 1,577              | 1,314              | 825               |
| Own shares held in relation to employee share schemes         | (7)                |                    |                   |

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|   |                   |                   |                   |
|---|-------------------|-------------------|-------------------|
| Redemption of preference shares                               |                   | (364)             | (364)             |
| Goodwill previously written off                               |                   | 40                | 40                |
| Transfer from merger reserve                                  | 287               | 287               | 574               |
| Transfer from revaluation reserve                             |                   |                   | 4                 |
| Transfer of increase in value of long-term assurance business | (17)              | (10)              | (32)              |
|   |                   | <u>          </u> | <u>          </u> |
| At end of period  | 9,654             | 8,064             | 7,848             |
|   | <u>          </u> | <u>          </u> | <u>          </u> |
| <b>Closing shareholders funds</b>                             | <b>32,408</b>     | <b>28,614</b>     | <b>28,099</b>     |
|   | <u>          </u> | <u>          </u> | <u>          </u> |

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**NOTES (continued)****10. Analysis of net cash inflow from operating activities**

|   | First half<br>2004 | First half<br>2003 | Full<br>year<br>2003 |
|---|--------------------|--------------------|----------------------|
|   | £m                 | £m                 | £m                   |
| Net cash inflow from trading activities               | 4,674              | 3,920              | 9,028                |
| Increase in loans and advances to banks and customers | (37,416)           | (14,452)           | (23,343)             |
| Increase in deposits by banks and customers           | 28,754             | 11,677             | 26,857               |
| Increase in securities                                | (9,322)            | (2,901)            | (9,871)              |
| Increase in debt securities in issue                  | 10,014             | 6,218              | 7,078                |
| Increase in settlement balances and short positions   | 9,258              | 6,270              | 3,202                |
| (Decrease)/increase in other assets and liabilities   | (2,273)            | 3,696              | 6,757                |
| Net cash inflow from operating activities             | 3,689              | 14,428             | 19,708               |

**11. Litigation**

In December 2003, members of the Group were joined as defendants in a number of legal actions in the United States following the collapse of Enron. Collectively the claims are, to a substantial degree, unquantified and in each case they are made against large numbers of defendants. The Group intends to defend these claims vigorously. The US Courts dealing with the main Enron actions have ordered that the Group join the non-binding, multi-party mediation which commenced in late 2003. Based on current knowledge including applicable defences and given the unquantified nature of these claims, the directors are unable at this stage to predict with certainty the eventual loss, if any, in these matters. In addition, pursuant to requests received from the US Securities and Exchange Commission and the US Department of Justice, the Group has been providing copies of Enron-related materials to these authorities and the Group continues to co-operate fully with them.

Members of the Group are engaged in other litigation in the United Kingdom and a number of overseas jurisdictions, including the United States, involving claims by and against them arising in the ordinary course of business. The directors of the company have reviewed these other actual, threatened and known potential claims and proceedings and, after consulting with the Group's legal advisers are satisfied that the outcome of these claims and proceedings will not have a material adverse effect on the Group's consolidated net assets, results of operations or cash flows.

**12. International Financial Reporting Standards**

The Group's 2005 interim and annual accounts will be prepared in accordance with International Reporting Financial Standards (IFRS). In the first half of 2004 IFRS implementation activities have included building IT solutions, revising processes and reporting structures, Group-wide IFRS training and analysis of new standards and amendments to existing standards. The Group remains on track to produce IFRS compliant accounts in 2005. A summary of the key differences between the Group's current accounting policies and IFRS is included in the Group's 2003



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**NOTES (continued)**

**13. Statutory accounts**

Financial information contained in this document does not constitute statutory accounts within the meaning of section 240 of the Companies Act 1985 ( the Act ). The statutory accounts for the year ended 31 December 2003 have been filed with the Registrar of Companies and have been reported on by the auditors under section 235 of the Act. The report of the auditors was unqualified and did not contain a statement under section 237(2) or (3) of the Act.

**14. Auditors review**

The interim results have been reviewed by the Group s auditors, Deloitte & Touche LLP, and their review report is set out on page 49.

**15. Form 6-K**

A report on Form 6-K will be filed with the Securities and Exchange Commission in the United States.

The profit and loss account presented in the Form 6-K will be the statutory profit and loss account as set out on page 27 of this announcement, which includes goodwill amortisation and integration costs in the captions prescribed by the Companies Act 1985. The Financial Review included in the Form 6-K will be based on the statutory profit and loss account.

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**ANALYSIS OF INCOME, EXPENSES AND PROVISIONS**

|   | First half   | First half | Full year |
|---|--------------|------------|-----------|
|   | 2004         | 2003       | 2003      |
|   | £m           | £m         | £m        |
| <b>Non-interest income</b>  |              |            |           |
| <b>Dividend income</b>  | <b>31</b>    | 30         | 58        |
| Fees and commissions receivable                                   | 3,065        | 2,691      | 5,693     |
| Fees and commissions payable - banking                            | (632)        | (527)      | (1,099)   |
| - insurance related   | (208)        | (27)       | (238)     |
| <b>Net fees and commissions</b>                                   | <b>2,225</b> | 2,137      | 4,356     |
| Foreign exchange  | 295          | 267        | 540       |
| Securities  | 501          | 486        | 798       |
| Interest rate derivatives   | 252          | 232        | 455       |
| <b>Dealing profits</b>  | <b>1,048</b> | 985        | 1,793     |
| Income on rental assets   | 618          | 507        | 1,088     |
| Embedded value profits  | 42           | 23         | 73        |
| Other   | 182          | 196        | 437       |
| <b>Other operating income</b>                                     | <b>842</b>   | 726        | 1,598     |
| <b>Non-interest income (excluding general insurance premiums)</b> | <b>4,146</b> | 3,878      | 7,805     |
| <b>General insurance net premium income</b>                       | <b>2,416</b> | 1,177      | 3,123     |
| <b>Total non-interest income</b>                                  | <b>6,562</b> | 5,055      | 10,928    |
| Staff costs - wages, salaries and other staff costs               | 2,184        | 1,973      | 3,997     |
| - social security costs   | 152          | 131        | 248       |
| - pension costs   | 185          | 134        | 273       |
| Premises and equipment  | 530          | 520        | 1,073     |
| Other   | 1,112        | 1,026      | 2,108     |
| <b>Administrative expenses*</b>                                   | <b>4,163</b> | 3,784      | 7,699     |
| * Integration costs included in administrative expenses comprise: |              |            |           |
| Staff costs   | 35           | 112        | 125       |
| Premises and equipment costs                                      | 3            | 31         | 31        |
| Other administrative costs  | 17           | 38         | 73        |

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|   |                   |                   |                     |
|---|-------------------|-------------------|---------------------|
|   | <u>55</u>         | <u>181</u>        | <u>229</u>          |
| Provisions for bad and doubtful debts       | <b>719</b>        | 746               | 1,461               |
| Amounts written off fixed asset investments | <b>32</b>         | (4)               | 33                  |
| <b>Provisions</b>                           | <b><u>751</u></b> | <b><u>742</u></b> | <b><u>1,494</u></b> |



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**ASSET QUALITY****Analysis of loans and advances to customers**

The following table analyses loans and advances to customers (including reverse repurchase agreements and stock borrowing) by industry.

|  | 30 June<br>2004 | 31 December<br>2003 | 30 June<br>2003 |
|--|-----------------|---------------------|-----------------|
|  | £m              | £m                  | £m              |
| Central and local government   | 2,378           | 2,100               | 1,714           |
| Finance  | 52,549          | 38,936              | 43,018          |
| Individuals - home   | 73,649          | 61,960              | 56,438          |
| Individuals - other  | 39,580          | 35,027              | 32,657          |
| Other commercial and industrial comprising:  |                 |                     |                 |
| Manufacturing  | 13,385          | 12,769              | 13,635          |
| Construction   | 6,946           | 5,839               | 5,881           |
| Service industries and business activities   | 50,800          | 50,772              | 51,419          |
| Agriculture, forestry and fishing  | 3,091           | 3,081               | 3,387           |
| Property   | 36,654          | 31,629              | 30,253          |
| Finance leases and instalment credit   | 15,154          | 14,340              | 14,288          |
| <b>Loans and advances to customers gross</b>   | <b>294,186</b>  | <b>256,453</b>      | <b>252,690</b>  |
| <b>Provisions for bad and doubtful debts</b>   | <b>(4,032)</b>  | <b>(3,922)</b>      | <b>(3,964)</b>  |
| <b>Total loans and advances to customers</b>   | <b>290,154</b>  | <b>252,531</b>      | <b>248,726</b>  |
| <b>Reverse repurchase agreements included in the analysis above:</b>                 |                 |                     |                 |
| Central and local government   | 1,389           | 1,079               | 358             |
| Finance  | 33,464          | 22,883              | 30,085          |
| Service industries and business activities   | 39              | 107                 |                 |
| <b>Total</b>   | <b>34,892</b>   | <b>24,069</b>       | <b>30,443</b>   |
| <b>Loans and advances to customers excluding reverse repurchase agreements - net</b> | <b>255,262</b>  | <b>228,462</b>      | <b>218,283</b>  |

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**ASSET QUALITY (continued)****Cross border outstandings**

The table below sets out the Group's cross border outstandings in excess of 0.75% of Group total assets (including acceptances) of £519.4 billion (31 December 2003 - £455.9 billion; 30 June 2003 - £451.4 billion). None of these countries have experienced repayment difficulties which have required refinancing of outstanding debt.

|                | 30 June<br>2004 | 31 December<br>2003 | 30 June<br>2003 |
|----------------|-----------------|---------------------|-----------------|
|                | £m              | £m                  | £m              |
| US             | 20,135          | 14,618              | 14,504          |
| Germany        | 16,020          | 15,073              | 10,648          |
| France         | 13,433          | 7,524               | 7,242           |
| Netherlands    | 6,686           | 6,830               | 7,090           |
| Cayman Islands | 6,478           | 6,666               | 6,611           |
| Japan          | 4,023           | 4,141               | 5,250           |
| Belgium        | 3,918           | *                   | *               |
| Spain          | *               | 3,421               | 3,997           |
| Italy          | *               | *                   | 3,978           |
| Canada         | *               | *                   | 3,426           |

\* less than 0.75% of Group total assets (including acceptances).

**Selected country exposures**

The table below details exposures to countries that are sometimes considered as having a higher credit and foreign exchange risk.

|           | 30 June 2004 |          |       | 31 December 2003 |          |       | 30 June 2003 |          |       |
|-----------|--------------|----------|-------|------------------|----------|-------|--------------|----------|-------|
|           | Bank         | Non-bank | Total | Bank             | Non-bank | Total | Bank         | Non-bank | Total |
|           | £m           | £m       | £m    | £m               | £m       | £m    | £m           | £m       | £m    |
| Argentina | 16           |          | 16    | 26               | 4        | 30    | 29           | 11       | 40    |
| Brazil    | 29           | 7        | 36    | 15               | 2        | 17    |              | 10       | 10    |
| Turkey    | 6            | 78       | 84    | 5                | 65       | 70    | 7            | 83       | 90    |

|           |           |           |    |    |     |     |
|-----------|-----------|-----------|----|----|-----|-----|
| Venezuela | <b>80</b> | <b>80</b> | 87 | 87 | 108 | 108 |
|-----------|-----------|-----------|----|----|-----|-----|

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**ASSET QUALITY (continued)****Risk elements in lending**

The Group's loan control and review procedures do not include the classification of loans as non-accrual, accruing past due, restructured and potential problem loans, as defined by the Securities and Exchange Commission (SEC) in the US. The following table shows the estimated amount of loans which would be reported using the SEC's classifications. The figures are stated before deducting the value of security held or related provisions.

|   | 30 June<br>2004<br>£m | 31 December<br>2003<br>£m | 30 June<br>2003<br>£m |
|---|-----------------------|---------------------------|-----------------------|
| Loans accounted for on a non-accrual basis (2):   |                       |                           |                       |
| Domestic  | 3,442                 | 3,221                     | 3,404                 |
| Foreign   | 1,043                 | 1,211                     | 1,177                 |
|   | <u>4,485</u>          | <u>4,432</u>              | <u>4,581</u>          |
| Accruing loans which are contractually overdue 90 days or more as to principal or interest (3): |                       |                           |                       |
| Domestic  | 554                   | 561                       | 306                   |
| Foreign   | 73                    | 81                        | 61                    |
|   | <u>627</u>            | <u>642</u>                | <u>367</u>            |
| Loans not included above which are troubled debt restructurings as defined by the SEC:          |                       |                           |                       |
| Domestic  | 38                    | 53                        | 96                    |
| Foreign   | 19                    | 30                        | 39                    |
|   | <u>57</u>             | <u>83</u>                 | <u>135</u>            |
| Total risk elements in lending  | <u>5,169</u>          | <u>5,157</u>              | <u>5,083</u>          |
| Potential problem loans (4)   |                       |                           |                       |
| Domestic  | 319                   | 492                       | 871                   |
| Foreign   | 163                   | 99                        | 104                   |
|   | <u>482</u>            | <u>591</u>                | <u>975</u>            |
| Closing provisions for bad and doubtful debts as a % of total risk elements in lending          | <u>78%</u>            | <u>76%</u>                | <u>78%</u>            |

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|  |              |              |              |
|--|--------------|--------------|--------------|
| Closing provisions for bad and doubtful debts as a % of total risk elements in lending and potential problem loans | <u>71%</u>   | <u>68%</u>   | <u>65%</u>   |
| Risk elements in lending as a % of gross loans and advances to customers   | <u>1.76%</u> | <u>2.01%</u> | <u>2.01%</u> |

Notes:

1. For the analysis above, Domestic consists of the United Kingdom domestic transactions of the Group. Foreign comprises the Group's transactions conducted through offices outside the UK and through those offices in the UK specifically organised to service international banking transactions.
2. The Group's UK banking subsidiary undertakings account for loans on a non-accrual basis from the point in time at which the collectability of interest is in significant doubt. Certain subsidiary undertakings of the Group generally account for loans on a non-accrual basis when interest or principal is past due 90 days.
3. Overdrafts generally have no fixed repayment schedule and consequently are not included in this category.
4. Loans that are current as to payment of principal and interest but in respect of which management has serious doubts about the ability of the borrower to comply with contractual repayment terms. Substantial security is held in respect of these loans and appropriate provisions have already been made in accordance with the Group's provisioning policy for bad and doubtful debts.

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**ASSET QUALITY (continued)****Provisions for bad and doubtful debts**

|   | First half<br>2004 | Full year<br>2003 | First half<br>2003 |
|---|--------------------|-------------------|--------------------|
|   | £m                 | £m                | £m                 |
| Provisions at beginning of period                       | 3,929              | 3,927             | 3,927              |
| Currency translation and other adjustments              | (42)               | (62)              | (6)                |
| Acquisitions  | 100                | 50                | 10                 |
| Amounts written-off                                     |                    |                   |                    |
| - Domestic  | (452)              | (1,097)           | (506)              |
| - Foreign   | (260)              | (422)             | (234)              |
|   | <u>(712)</u>       | <u>(1,519)</u>    | <u>(740)</u>       |
| Recoveries  |                    |                   |                    |
| - Domestic  | 25                 | 38                | 15                 |
| - Foreign   | 19                 | 34                | 19                 |
|   | <u>44</u>          | <u>72</u>         | <u>34</u>          |
| Sub-total   | <u>3,319</u>       | <u>2,468</u>      | <u>3,225</u>       |
| Provisions charged against profit:                      |                    |                   |                    |
| Net specific provisions                                 |                    |                   |                    |
| - Domestic  | 463                | 926               | 482                |
| - Foreign   | 228                | 533               | 259                |
|   | <u>691</u>         | <u>1,459</u>      | <u>741</u>         |
| General provision                                       | <u>28</u>          | <u>2</u>          | <u>5</u>           |
| Total bad and doubtful debt provisions charge to profit | <u>719</u>         | <u>1,461</u>      | <u>746</u>         |
| Provisions at end of period                             | <u>4,038</u>       | <u>3,929</u>      | <u>3,971</u>       |
| Provisions at end of period comprise:                   |                    |                   |                    |
| Specific  |                    |                   |                    |
| - Domestic  | 2,232              | 2,097             | 2,227              |
| - Foreign   | 1,255              | 1,266             | 1,140              |
| Total specific provisions                               | <u>3,487</u>       | <u>3,363</u>      | <u>3,367</u>       |

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|                    |              |              |              |
|--------------------|--------------|--------------|--------------|
| General provisions | <u>551</u>   | <u>566</u>   | <u>604</u>   |
|                    | <u>4,038</u> | <u>3,929</u> | <u>3,971</u> |

The closing provisions include provision against loans and advances to banks of £6 million (31 December 2003 - £7 million; 30 June 2003 - £7 million).

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**MARKET RISK**

The Group manages the market risk in its trading and treasury portfolios through value-at-risk (VaR) limits as well as stress testing, position and sensitivity limits. VaR is a technique that produces estimates of the potential negative change in the market value of a portfolio over a specified time horizon at a given confidence level. The table below sets out the trading and treasury VaR for the Group, which assumes a 95% confidence level and a one-day time horizon.

|                     | Period end | Maximum | Minimum | Average |
|---------------------|------------|---------|---------|---------|
|                     | £m         | £m      | £m      | £m      |
| <b>Trading VaR</b>  |            |         |         |         |
| 30 June 2004        | 13.1       | 13.6    | 6.4     | 9.5     |
| 31 December 2003    | 7.4        | 14.2    | 5.6     | 9.4     |
| 30 June 2003        | 11.5       | 12.8    | 8.0     | 10.8    |
| <b>Treasury VaR</b> |            |         |         |         |
| 30 June 2004        | 7.8        | 8.3     | 5.7     | 7.0     |
| 31 December 2003    | 8.1        | 11.0    | 5.6     | 8.3     |
| 30 June 2003        | 10.0       | 10.0    | 5.6     | 7.3     |

The Group's VaR should be interpreted in light of the limitations of the methodologies used. These limitations include:

Historical data may not provide the best estimate of the joint distribution of risk factor changes in the future and may fail to capture the risk of possible extreme adverse market movements which have not occurred in the historical window used in the calculations.

VaR using a one-day time horizon does not fully capture the market risk of positions that cannot be liquidated or hedged within one day.

VaR using a 95% confidence level does not reflect the extent of potential losses beyond that percentile.

The Group largely computes the VaR of the trading portfolios at the close of business and positions may change substantially during the course of the trading day. Controls are in place to limit the Group's intra-day exposure such as the calculation of VaR for selected portfolios.



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These limitations and the nature of the VaR measure mean that the Group cannot guarantee that losses will not exceed the VaR amounts indicated nor that losses in excess of the VaR amounts will not occur more frequently than once in 20 business days.

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**REGULATORY RATIOS AND OTHER INFORMATION**

|  | <b>30 June<br/>2004</b> | <b>31 December<br/>2003</b> | <b>30 June<br/>2003</b> |
|--|-------------------------|-----------------------------|-------------------------|
| <b>Capital base (£m)</b>   |                         |                             |                         |
| Ordinary shareholders funds and minority interests   | 17,268                  | 13,235                      | 13,321                  |
| Preference shares and tax deductible securities  | 6,048                   | 6,164                       | 6,137                   |
|  | <b>23,316</b>           | 19,399                      | 19,458                  |
| Tier 1 capital   | 17,252                  | 16,439                      | 14,941                  |
| Tier 2 capital   | <b>40,568</b>           | 35,838                      | 34,399                  |
| Less: investments in insurance companies, associated undertakings and other supervisory deductions | (4,718)                 | (4,618)                     | (2,707)                 |
|  | <b>35,850</b>           | 31,220                      | 31,692                  |
| <b>Weighted risk assets (£m)</b>   |                         |                             |                         |
| Banking book   |                         |                             |                         |
| - on-balance sheet   | 232,600                 | 214,400                     | 209,500                 |
| - off-balance sheet  | 41,300                  | 36,400                      | 34,200                  |
| Trading book   | 13,700                  | 12,900                      | 13,400                  |
|  | <b>287,600</b>          | 263,700                     | 257,100                 |
| <b>Risk asset ratio</b>  |                         |                             |                         |
| - tier 1   | 8.1%                    | 7.4%                        | 7.6%                    |
| - total  | 12.5%                   | 11.8%                       | 12.3%                   |
| <b>Share price</b>   | £ 15.88                 | £ 16.46                     | £ 17.00                 |
| <b>Number of shares in issue</b>   | 3,141m                  | 2,963m                      | 2,942m                  |
| <b>Market capitalisation</b>   | £ 49.9bn                | £ 48.8bn                    | £ 50.0bn                |
| <b>Net asset value per ordinary share</b>  | £ 9.40                  | £ 8.50                      | £ 8.67                  |
| <b>Employee numbers</b>  |                         |                             |                         |
| Corporate Banking and Financial Markets  | 16,100                  | 15,900                      | 16,100                  |
| Retail Banking*  | 30,600                  | 31,100                      | 30,400                  |
| Retail Direct  | 8,400                   | 7,300                       | 7,000                   |
| Manufacturing*   | 24,000                  | 22,400                      | 21,400                  |
| Wealth Management*   | 5,200                   | 5,200                       | 5,100                   |
| RBS Insurance*   | 19,500                  | 18,800                      | 10,800                  |
| Ulster Bank  | 5,200                   | 4,400                       | 4,500                   |
| Citizens   | 14,200                  | 14,100                      | 13,800                  |
| Centre   | 1,900                   | 1,700                       | 1,700                   |
| <b>Group total</b>   | <b>125,100</b>          | 120,900                     | 110,800                 |
| Acquisitions in the year ended 30 June 2004  | (10,700)                | (9,100)                     |                         |

|                   |                |         |         |
|-------------------|----------------|---------|---------|
| <b>Underlying</b> | <b>114,400</b> | 111,800 | 110,800 |
|-------------------|----------------|---------|---------|

\* prior periods have been restated to reflect the transfer in 2004 of certain activities from Wealth Management to Retail Banking and from RBS Insurance to Manufacturing.

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**ADDITIONAL FINANCIAL DATA FOR US INVESTORS****Reconciliation between UK and US GAAP**

The following tables summarise the significant adjustments, which would result from the application of US generally accepted accounting principles ( US GAAP ) instead of UK GAAP.

|  | First half<br>2004 | First half<br>2003 | Full year<br>2003 |
|--|--------------------|--------------------|-------------------|
|  | £m                 | £m                 | £m                |
| <b>Consolidated statement of income</b>                  |                    |                    |                   |
| Profit attributable to ordinary shareholders - UK GAAP   | 2,106              | 1,745              | 2,315             |
| Amortisation of goodwill                                 | 375                | 366                | 721               |
| Pension costs  | (138)              | (168)              | (369)             |
| Securities, derivatives and hedging                      | 278                | (243)              | 281               |
| Software development costs                               | (81)               | (123)              | (300)             |
| Others (net)   | (168)              | (56)               | (258)             |
| Taxation   | 18                 | 160                | 174               |
| Net income available for ordinary shareholders - US GAAP | 2,390              | 1,681              | 2,564             |
|  | <b>30 June</b>     | <b>31 December</b> | <b>30 June</b>    |
|  | <b>2004</b>        | <b>2003</b>        | <b>2003</b>       |
|  | £m                 | £m                 | £m                |
| <b>Consolidated shareholders equity</b>                  |                    |                    |                   |
| Shareholders funds - UK GAAP                             | 32,408             | 28,099             | 28,614            |
| Goodwill   | 2,597              | 2,222              | 1,867             |
| Proposed dividend  | 529                | 1,059              | 431               |
| Recognition of pension scheme minimum liability          |                    |                    | (3,393)           |
| Perpetual regulatory tier one securities                 | 668                | 678                | 733               |
| Software development costs                               | 579                | 660                | 837               |
| Pension costs  | (165)              | (27)               | 174               |
| Taxation   | 69                 | (166)              | 565               |
| Others (net)   | (792)              | (182)              | 348               |
| Shareholders equity - US GAAP                            | 35,893             | 32,343             | 30,176            |

**Total assets**

Total assets under US GAAP, which include acceptances and the grossing-up of certain repurchase balances offset under UK GAAP, together with the effect of adjustments made to net income and shareholders' equity were £556 billion (31 December 2003 - £488 billion; 30 June 2003 - £472 billion).

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**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, should, intend, plan, probability, Value-at-Risk ( VaR ), target, goal, objective, will, endeavour, outlook, optimistic, prospects and similar expressions or variations. Other sections such as Group Chief Executive's review and Financial review contain forward-looking statements.

In particular, this document includes forward-looking statements relating, but not limited, to 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. Such statements are subject to risks and uncertainties. For example, certain of the 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: general economic conditions in the UK and in other countries in which the Group has significant business activities or investments, including the United States; the monetary and interest rate policies of the Bank of England, the Board of Governors of the Federal Reserve System and other G-7 central banks; inflation; deflation; unanticipated turbulence in interest rates, foreign currency exchange rates, commodity prices and equity prices; changes in UK and foreign laws, regulations and taxes; changes in competition and pricing environments; natural and other disasters; the inability to hedge certain risks economically; the adequacy of loss reserves; acquisitions or restructurings; technological changes; changes in consumer spending and saving habits; 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 report, 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.

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## **INDEPENDENT REVIEW REPORT TO THE ROYAL BANK OF SCOTLAND GROUP plc**

### **Introduction**

We have been instructed by the company to review the financial information for the six months ended 30 June 2004 which comprises the statutory consolidated profit and loss account, the consolidated balance sheet, the statement of consolidated total recognised gains and losses, the reconciliation of movements in consolidated shareholders' funds, the consolidated cash flow statement, the divisional performance disclosures and related notes 1 to 15. We have read the other information contained in this interim results announcement and, solely on that basis, have considered whether it contains any apparent misstatements or material inconsistencies with the financial information.

This report is made solely to the company in accordance with Bulletin 1999/4 issued by the Auditing Practices Board (the Bulletin). Our work has been undertaken so that we might state to the company those matters we are required to state to them in an independent review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company, for our review work, for this report, or for the conclusions we have formed.

### **Directors' responsibilities**

The interim results announcement, including the financial information contained therein, is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the interim results announcement in accordance with the Listing Rules of the Financial Services Authority which require that the accounting policies and presentation applied to the interim figures should be consistent with those applied in preparing the preceding annual accounts except where any changes, and the reasons for them, are disclosed.

### **Review work performed**

We conducted our review in accordance with the guidance contained in the Bulletin for use in the United Kingdom. A review consists principally of making enquiries of management and applying analytical procedures to the financial information and underlying financial data and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit performed in accordance with United Kingdom auditing standards and therefore provides a lower level of assurance than an audit. Accordingly, we do not express an audit opinion on the financial information.

### **Review conclusion**

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On the basis of our review we are not aware of any material modifications that should be made to the financial information as presented for the six months ended 30 June 2004.

Deloitte & Touche LLP

Chartered Accountants

Edinburgh

2 August 2004



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**RESTATEMENTS**

During the first half of 2004, a number of activities were transferred between divisions. The Affluent Banking business was transferred from Wealth Management to Retail Banking; further activities were transferred from Retail Direct, Wealth Management and RBS Insurance to Manufacturing; and, within RBS Insurance, certain income has been re-classified from net fees and commissions to insurance premium income in order to conform the accounting policies of Direct Line and Churchill.

|                            | First half 2003           |                |                | Full year 2003            |                |                |
|----------------------------|---------------------------|----------------|----------------|---------------------------|----------------|----------------|
|                            | Previously reported<br>£m | Transfer<br>£m | Restated<br>£m | Previously reported<br>£m | Transfer<br>£m | Restated<br>£m |
| <b>Retail Banking</b>      |                           |                |                |                           |                |                |
| - Net interest income      | 1,433                     | 4              | <b>1,437</b>   | 2,951                     | 8              | <b>2,959</b>   |
| - Non-interest income      | 703                       | 28             | <b>731</b>     | 1,452                     | 62             | <b>1,514</b>   |
| - Staff costs              | 373                       | 8              | <b>381</b>     | 777                       | 16             | <b>793</b>     |
| - Other costs              | 93                        | 5              | <b>98</b>      | 227                       | 10             | <b>237</b>     |
| <b>Contribution</b>        | <b>1,535</b>              | <b>19</b>      | <b>1,554</b>   | <b>3,126</b>              | <b>44</b>      | <b>3,170</b>   |
| <b>Retail Direct</b>       |                           |                |                |                           |                |                |
| - Other costs              | 213                       | (4)            | <b>209</b>     | 454                       | (8)            | <b>446</b>     |
| <b>Contribution</b>        | <b>407</b>                | <b>4</b>       | <b>411</b>     | <b>873</b>                | <b>8</b>       | <b>881</b>     |
| <b>Manufacturing</b>       |                           |                |                |                           |                |                |
| - Staff costs              | 287                       | 6              | <b>293</b>     | 625                       | 19             | <b>644</b>     |
| - Other costs              | 613                       | 56             | <b>669</b>     | 1,250                     | 139            | <b>1,389</b>   |
| <b>Contribution</b>        | <b>(900)</b>              | <b>(62)</b>    | <b>(962)</b>   | <b>(1,875)</b>            | <b>(158)</b>   | <b>(2,033)</b> |
| <b>Wealth Management</b>   |                           |                |                |                           |                |                |
| - Net interest income      | 225                       | (4)            | <b>221</b>     | 465                       | (8)            | <b>457</b>     |
| - Non-interest income      | 204                       | (28)           | <b>176</b>     | 414                       | (62)           | <b>352</b>     |
| - Staff costs              | 139                       | (8)            | <b>131</b>     | 275                       | (16)           | <b>259</b>     |
| - Other costs              | 74                        | (9)            | <b>65</b>      | 157                       | (18)           | <b>139</b>     |
| <b>Contribution</b>        | <b>219</b>                | <b>(15)</b>    | <b>204</b>     | <b>438</b>                | <b>(36)</b>    | <b>402</b>     |
| <b>RBS Insurance</b>       |                           |                |                |                           |                |                |
| - Insurance premium income | 1,149                     | 28             | <b>1,177</b>   | 3,061                     | 62             | <b>3,123</b>   |
| - Net fees and commissions | 21                        | (28)           | <b>(7)</b>     | (99)                      | (62)           | <b>(161)</b>   |
| - Staff costs              | 96                        | (6)            | <b>90</b>      | 241                       | (19)           | <b>222</b>     |
| - Other costs              | 147                       | (47)           | <b>100</b>     | 341                       | (122)          | <b>219</b>     |
| <b>Contribution</b>        | <b>202</b>                | <b>53</b>      | <b>255</b>     | <b>468</b>                | <b>141</b>     | <b>609</b>     |

Group profit is unaffected by these changes.



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**FINANCIAL CALENDAR**

|                                   |                  |
|-----------------------------------|------------------|
| 2004 interim dividend payment     | 8 October 2004   |
| 2004 annual results announcement  | 24 February 2005 |
| Annual general meeting            | 20 April 2005    |
| 2004 final dividend payment       | June 2005        |
| 2005 interim results announcement | 4 August 2005    |

**CONTACTS**

|                  |                            |                                |
|------------------|----------------------------|--------------------------------|
| Sir Fred Goodwin | Group Chief Executive      | 020 7672 0008<br>0131 523 2033 |
| Fred Watt        | Group Finance Director     | 020 7672 0008<br>0131 523 2028 |
| Richard O Connor | Head of Investor Relations | 020 7672 1758                  |

**For media enquiries:**

|                |                                |                               |
|----------------|--------------------------------|-------------------------------|
| Howard Moody   | Group Director, Communications | 020 7672 1916<br>07768 033562 |
| Carolyn McAdam | Head of Group Communications   | 020 7672 1915<br>07796 274968 |

2 August 2004

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**Signatures**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: 03 August, 2004

THE ROYAL BANK OF SCOTLAND GROUP plc  
(Registrant)

By:           /s/ H Campbell          

Name: H Campbell  
Title: Head of Group Secretariat