

Strategic Report 2016

# Creating a simple, safe, customer-focused bank

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RBS is a UK-based banking and financial services company, headquartered in Edinburgh.

RBS provides a wide range of products and services to personal, commercial and large corporate and institutional customers through its two main subsidiaries, The Royal Bank of Scotland and NatWest, as well as through a number of other well-known brands including Ulster Bank and Coutts.

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## Approval of Strategic Report

The Strategic Report for the year ended 31 December 2016 set out on pages 3 to 56 was approved by the Board of directors on 23 February 2017.

By order of the Board.

Aileen Taylor  
**Company Secretary**  
23 February 2017

### Chairman

Howard Davies

### Executive directors

Ross McEwan  
Ewen Stevenson

### Non-executive directors

Sandy Crombie  
Frank Dangeard  
Alison Davis  
Morten Friis  
Robert Gillespie  
Penny Hughes  
Brendan Nelson  
Baroness Noakes  
Mike Rogers

# 2016 performance

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RBS reported an operating loss before tax of £4,082 million for 2016 and an attributable loss<sup>(1)</sup> of £6,955 million, which included litigation and conduct costs of £5,868 million, restructuring costs of £2,106 million, the final Dividend Access Share (DAS) dividend of £1,193 million and Capital Resolution disposal losses and impairments of £825 million. Restructuring costs included a £750 million provision in respect of the 17 February 2017 update on RBS's remaining State Aid obligation regarding Williams & Glyn.

Across our Personal & Business Banking (PBB), Commercial & Private Banking (CPB) and NatWest Markets (NWM) franchises, RBS reported a £163 million, or 4%, increase in adjusted operating profits to £4,249 million for 2016, and an adjusted return on equity of 11.1%, compared with 11.2% in 2015.

In 2016 RBS delivered against all of its operating financial targets; PBB and CPB had combined income growth of 2%, adjusting for transfers, underpinned by 10% net lending growth, expenses have been reduced by around £1 billion for the third year in succession as the bank continues to focus on digital channels and on simplification of its processes, and Capital Resolution RWAs have reduced by a further £14.5 billion, or 30%, to £34.5 billion, with 80% of RWAs now relating to PBB, CPB and NatWest Markets compared with 72% at the end of 2015. RBS is committed to achieving its sub 50% cost:income ratio and 12% return on tangible equity targets by 2020.

Common Equity Tier 1 ratio of 13.4% reduced by 210 basis points during 2016, but remains ahead of our target despite recognising significant charges relating to remaining legacy issues.

## Our 2016 performance at a glance

(£6,955m)

Loss attributable to ordinary shareholders

(£4,082m)

Operating loss before tax <sup>(2)</sup>

£4,249m

PBB, CPB & NatWest Markets adjusted operating profit <sup>(2)</sup>

66%

Cost:income ratio – adjusted <sup>(3)</sup>

2.18%

Net interest margin

123%

Liquidity coverage ratio <sup>(4)</sup>

£228.2bn

Risk-weighted assets

13.4%

Common Equity Tier 1 ratio <sup>(5)</sup>

11.1%

PBB, CPB & NatWest Markets Adjusted return on equity <sup>(2,6)</sup>

£33.7bn

Gross new mortgage lending across England, Wales and Scotland <sup>(7)</sup>

75%

Employee engagement score

£1.32bn

Total tax paid to the UK Government <sup>(8)</sup>

### Notes:

(1) Attributable to ordinary shareholders.

(2) Operating profit before tax excluding own credit adjustments, (loss)/gain on redemption of own debt, strategic disposals, restructuring costs, litigation and conduct costs and write down of goodwill.

(3) Excluding own credit adjustments, (loss)/gain on redemption of own debt and strategic disposals, restructuring costs, litigation and conduct costs and write down of goodwill.

(4) On 1 October 2015 the LCR became the Prudential Regulation Authority's (PRA) primary regulatory liquidity standard; UK banks are required to meet a minimum standard of 80% initially, rising to 100% by 1 January 2018. The published LCR excludes Pillar 2 add-ons. RBS calculates the LCR using its own interpretation of the EU LCR Delegated Act, which may change over time and may not be fully comparable with that of other institutions.

(5) Based on end-point Capital Requirements Regulation (CRR) Tier 1 capital and leverage exposure under the CRR Delegated Act.

(6) Tangible equity is equity attributable to ordinary shareholders less intangible assets.

(7) Gross new mortgage lending in UK PBB, Ulster Bank Rol and RBSI.

(8) Comprises £174 million corporate tax, £660 million irrecoverable VAT, £208 million bank levies and £279 million employer payroll taxes.

# Chairman's statement



**Howard Davies**  
Chairman

2016 was another difficult year for RBS shareholders, even though there is good progress to report on our strategy to rebuild a strong bank focused primarily on retail and commercial customers in the UK and Ireland.

The core bank performed strongly, and adjusted operating profits were up by around 4%, in a year of political and economic uncertainty. That progress reflects growth in our market share in the mortgage market and a resumption of growth in business lending, after many years of decline. It shows, too, that the strong focus on reducing costs is beginning to pay off.

Nonetheless the attributable loss, at around £7 billion, was more than three times as large as in 2015. It is hard to present that as a positive outcome for shareholders, though in fact it does reflect the impact of stronger efforts to resolve the bank's legacy problems. We settled a number of regulatory and legal actions and made a large provision for future costs, we retired the Dividend Access Share and made a large number of disposals of legacy assets. Restructuring costs were also large in the year. As a result, the bank is better placed than it was a year ago, though there are still some sizeable legacy problems to resolve. The Board and I are determined to press ahead with resolution of those issues and to continue with the strategy Ross McEwan first outlined in 2014. We are confident that we have the right management team in place to deliver effectively in both areas.

## **The Economic and Regulatory Environment**

The UK economy grew by around 2% in 2016, a little less rapidly than in 2015, but still at a healthy rate in what is now a mature recovery. Unemployment remained low, inflation stayed well below the Bank of England's target rate and house prices rose, on average, by around 5%, though the regional variations were wide. These might, overall, seem to be benign conditions for banks, but the low interest rate environment, and especially a relatively flat yield curve, are challenges to profitability. Some central banks are charging negative interest rates, and while the Bank of England has not followed them, the base rate was reduced from 0.5% to 0.25% in August, after the referendum on European Union (EU) membership.

This lower interest rate environment puts further pressure on banks to control their costs.

The vote to leave the EU was widely expected to have a negative impact on the economy. So far, we have seen a significant fall in sterling, but consumer spending has remained robust, and growth has continued. Of course the UK has not yet left the EU, and we do not know the terms of our departure, so the long-term impact remains impossible to predict. The short-term effect on banks was felt primarily through the reduction in interest rates.

There has been much debate about the impact on the City, and on UK financial services in general, if, as now seems likely, we also leave the single market. As I write, the Article 50 negotiations have not yet begun, so it is idle to speculate. RBS as a primarily UK bank will be less affected than most, but we own Ulster Bank in Ireland and have modest presences in major EU corporate markets. We will take steps to protect those assets as the regulatory environment becomes clearer.

Our prime focus through this uncertain period has been, and will continue to be, to provide high quality banking services to our customers and to help them to understand the implications of change for their businesses and their families.

The regulatory environment continues to be challenging for banks. The Basel Committee is discussing a new set of proposals which could have the effect of increasing capital requirements materially, though no agreement has yet been reached. In the UK, the Bank of England stress tests are built on very rigorous assumptions about growth and asset prices. RBS failed its stress test in 2016, primarily on the basis of assumptions reflecting the uncertainty of future conduct costs, especially from legacy problems in the US. We agreed measures to strengthen our balance sheet as a result, which are already underway.

UK banks are also now heavily engaged in preparations for the implementation of ring-fencing, as required by the legislation implementing the recommendation of the Independent Commission on

Banking. We are implementing our own plans and expect to meet the statutory deadline of 1 January 2019.

### Strategy

Set against that backdrop our strategy remains consistent. The aim is to make RBS a simpler bank focused on doing fewer things, built around a low risk UK and Irish retail and commercial bank and markets business; a safer bank with a long-term target of a CET1 ratio of at least 13%; and a customer-focused bank that is easier to do business with. Our aspiration remains to be the best UK bank for customer service, trust and advocacy by 2020. We will retain a smaller markets business, which complements our strong domestic franchises. The Board are confident that this is the right path to follow and that the bank will deliver good returns for shareholders when its legacy problems have been resolved.

In early 2016 we renewed our long-term targets of 50% for the cost to income ratio and 12% for return on tangible equity. Given expected slower economic growth over the medium-term, we now think we will achieve those objectives in 2020, a year later than previously communicated. That change aligns the timing of our financial targets with our customer service ambitions. It is not yet possible to give a reliable forecast of when the bank will be able to restore a dividend.

### Conduct, litigation and legacy issues

As I have said, during the year we made good progress in dealing with a number of legacy issues that have been clouding our performance and shareholder investment case.

We were able to remove one of the main barriers to paying a dividend by paying the final £1.2 billion to retire the Dividend Access Share.

In January 2016, the Board took the decision to make an accelerated £4.2 billion payment to our main pension scheme. Taking this action reduced the scheme deficit considerably and helped provide certainty on our capital management of the pension scheme for both members and regulators. The next valuation is scheduled for 2018.

We also resolved a number of litigation cases relating to foreign exchange and interest rate fixing allegations. These

settlements were costly reminders of past behaviours that have no place in the industry or the bank we are building.

The treatment of some of our small business customers has been under scrutiny. Although the Financial Conduct Authority (FCA) review into the historical operation of our former Global Restructuring Group (GRG) continues, I am pleased that with the endorsement of the FCA we were able to announce a new complaints process, led by Sir William Blackburne, a retired High Court judge, alongside an automatic refund for some of the complex fees charged to customers who were in GRG between 2008 - 2013. While we have acknowledged we did not treat all these troubled business customers as well as we should have done, we do not accept that the bank artificially distressed otherwise viable SME businesses or deliberately caused them to fail. The FCA's skilled person and our independent investigators have also found no evidence that the bank either inappropriately targeted businesses to transfer them into GRG or drove them to insolvency.

Another legacy problem on the way to resolution is the shareholder litigation related to the 2008 rights issue. We announced in December that we made an offer to affected shareholders to resolve that litigation and four out of five groups involved have already accepted it.

Following the Government's injection of capital into the bank in 2008, RBS undertook to carry out five major divestments as part of the State Aid commitments agreed with the European Commission (EC). Four have been successfully implemented. The fifth entailed a divestment of assets to enhance competition in the UK's SME banking market. The bank identified a collection of branches and customer relationships, identified as a new bank to be known as Williams & Glyn.

Implementing that divestment has proved extremely difficult, partly for technological reasons. In addition, the lower interest rate environment threatened the viability of the new bank.

In the light of these changed circumstances, on 17 February this year, the EC and HM Treasury

announced a consultation on a plan, intended to promote competition in different ways, which can be implemented more easily and rapidly. The plan is not yet firm, but we have prudently provided for its cost to the bank in our accounts. We are grateful to the EC for its willingness to consider alternative means to the same end. If carried through, they will relieve the bank of a major operational burden which has constrained our ability to upgrade and enhance our IT systems in the interests of our customers.

But there are other issues from the past which remain to be resolved, and where it has been frustratingly difficult to make progress. By a distance the most financially significant relates to the bank's participation in the US subprime mortgage market in the run up to the financial crisis, and especially in 2007. The Massachusetts Attorney General's Office has been investigating the circumstances of some of the transactions for some years, and we have been in parallel discussions with the Federal Housing Finance Agency. Shareholders will be aware that a number of other banks, both US and European, have settled their claims over the past year, but RBS remains under investigation and as we have said, faces potential criminal and civil action. At this point we cannot say when the issues will be resolved, as the timing is out of our hands.

#### **Remuneration**

While RBS continues to report losses it is vital that the bank remains disciplined in its approach to remuneration. On the other hand, we need to fairly reward our colleagues who work with customers from day to day and who bear no responsibility for the decisions which led to those losses, and it is important for the long-term value of shareholders' investment in the company that we attract and retain well-qualified and motivated people. We believe the decisions we have made this year, on the bonus pool (which has been further reduced) and on the proposed new long-term incentive scheme, strike that balance appropriately. They are more fully explained in the 2016 Remuneration report.

#### **Supporting our communities**

We refreshed our main customer facing brands during the year, with a new advertising campaign, emphasising their contribution to the communities in which they operate. In England our principal brand is NatWest, in Ireland it is Ulster Bank, and of course in Scotland it is The Royal Bank of Scotland, which has been providing banking services to the country since 1727. We also have a vital role to play in these communities that goes beyond traditional banking activity. Our support of small businesses continues to strengthen through our partnership with Entrepreneurial Spark. In 2016 we opened a further six accelerator hubs. These accelerator hubs, which are based in our buildings, provide start-ups with free office space, mentoring and access to our networks. Over 7,000 entrepreneurs will be supported in this way over five years, helping to grow the economy and create thousands of jobs.

Our financial education programme, MoneySense, continues to deliver vital skills to young people that will help them be more financially aware in later life. This year we have helped over 300,000 young people in the UK.

In 2016 we also celebrated our 40th anniversary of supporting The Prince's Trust. To mark this milestone, we raised over £470,000 in just five days, with 566 colleagues cycling across the country in fundraising efforts.

This year, we have taken the first step towards combining our 2016 Sustainability and Strategic reports, bringing together in one place our financial and non financial performance to demonstrate how we are building a more sustainable bank to deliver long term value to all our stakeholders.

#### **Stakeholder Engagement**

We welcomed the opportunity to participate in the Department for Business, Energy and Industrial Strategy's (BEIS) Green Paper consultation on Corporate Governance Reform. The chapter on strengthening the employee, customer and wider

stakeholder voice was of particular interest. This is a cause that we care about. As noted in our response to BEIS, we are looking at ways of improving and building upon our existing arrangements in order to promote the stakeholder voice at board level. We are supportive of the proposal to increase wide stakeholder engagement, including via a panel arrangement. As an organisation, we have maintained active engagement with stakeholders over several years through our Sustainable Banking Committee which, since 2011, has regularly met with external stakeholders and asks them to challenge the most senior decision makers in RBS. We see increased formal engagement as the natural evolution of that committee's work.

#### **Board changes**

Frank Dangeard is the one new face around the boardroom table since last year. He joined the Board in May 2016 and brings a wealth of experience from a number of senior roles and directorships across a range of technology and financial services companies. This knowledge is vital as the bank adapts to increasing customer use of digital channels, and to the need for ever heightened awareness of the risk of cyber attacks.

#### **Conclusion**

I am uncomfortably aware that the reconstruction and rehabilitation of RBS has taken longer than expected, and is still not complete. We can now see clearly the shape of a profitable bank which serves its customers and communities well. There is still a road to travel before we reach that destination, and of course the competitive environment for banks continues to evolve. I assure you that the Board and management are single-mindedly focused on delivering value for our shareholders, and are grateful for your patience as we proceed.



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# Chief Executive's review

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**Ross McEwan**  
Chief Executive

In 2016 RBS made an attributable loss of £7.0 billion, mostly reflecting charges for outstanding litigation and conduct, and costs associated with restructuring of the bank. The financial impact of these issues is a difficult but necessary step in working through the bank's legacy issues. These costs are a stark reminder of what happens to a bank when things go wrong and you lose focus on the customer, as this bank did before the financial crisis. The more progress we have made on clearing these past issues, enables us to sharpen our focus on the core bank.

Our service level and product improvements are already delivering benefits for both customers and the core bank. In 2017 our focus will turn to going even further on reducing costs and faster on digital transformation in order to deliver a more simple, safe and customer-focused bank.

#### **The bank we were**

I joined RBS because I could see that underneath all the troubles it faced, there was a strong bank, with excellent brands and great colleagues, doing outstanding things for customers each day. This underlying strength is still evident today.

In 2014 I announced a three phase strategy. We are moving to the final phase of this, after delivering much during the first two phases, which were about building a platform of strength

and stripping away unnecessary complexity. Our CET1 ratio has now materially improved to 13.4% from 8.6% at the start of 2014. We have thoroughly reshaped our investment banking business, now rebranded NatWest Markets. We have sold Citizens in the US, completing the largest bank IPO in US history in the process, and also sold our international private banking business. We have ended active operations in 26 countries, decommissioned 30% of our IT systems and applications, and almost halved the number of legal entities. We have also completed the run-down or sale of over three quarters of Capital Resolution legacy and non-core assets. We have reduced our cost base by over £3 billion, exceeding our target for the third consecutive year, with an operating cost reduction of £985 million.

**In 2016, we improved on our position in a number of rankings, including achieving our highest ever score in the Dow Jones Sustainability Index.**

The past is not completely behind us, with our dealings on Residential Mortgage Backed Securities (RMBS) and Williams & Glyn, our residual European Commission State Aid obligations, two significant issues that we still need to resolve. The recent proposal by HM Treasury on an alternative way to increase competition to allow us to meet our State Aid commitments would deliver an outcome more quickly, and with more certainty than undertaking a complex sale. We have been able to provide for both of these in our accounts, though there may still be substantial additional provisions on RMBS.

#### **The bank we are today**

We are now in a much better position to focus on our long term aspiration – to transform the bank into the number one for customer service, trust, and advocacy. While the signs of this transformation have at times been masked by our wider organisational changes, the core bank has already evolved materially since 2014. Our decision to refocus on the UK has seen our balance sheet shrink by £229 billion since the start of our plan. This is net of the continued growth in our Personal and Business Banking and Commercial and Private Banking franchises. We are seeing the benefits of our service-led strategy in the financial performance of the core bank, generating £4.2 billion in adjusted pre-tax operating profit for the year, an average of £1 billion per quarter for the last eight quarters and 4% up on 2015.

While Q4 was down from the levels seen earlier this year, our Net Promoter Scores for Commercial and NatWest Personal in 2016 were the highest they have ever been.

With £30 billion of gross new mortgage lending in UK PBB, we helped 320,000 customers with their mortgage in 2016, growing our market share for the fourth consecutive year without leading on price or risk.

We are the largest commercial bank in the UK, and are ranked joint number one by Net Promoter Score. Our ability

to generate value here is shown by the scale of support we have provided to the economy in the past year, with almost £9 billion of new net commercial lending.

#### **The bank we are becoming**

We still have more work to do. In part, that means finishing the restructuring of RBS, resolving the remaining legacy issues, and preparing the bank for ring-fencing. In the main, however, it is about adapting to the changing nature of the UK and Irish banking sectors, and investing to meet our customers' evolving needs.

Digital innovation means customers are doing more of their transactions online. We interact with our customers over 20 times more through digital channels than physical ones. 35% of all new products were taken out digitally in UK PBB, and this is rising steadily. A fifth of our customers now solely use mobile and digital to interact with us. As customers change the way they bank with us, we must change the way we serve them. This means continuing to simplify for our customers, and accelerating our deployment of digital and mobile capabilities. The role of the branch is fast moving to an advice and service centre, away from transactions. While the branch will still be a core part of our offering to customers, inevitably some branches will have to close.

We're working to blur the line between traditional and digital banking channels. We are investing in a video sales and service proposition that will connect customers, no matter where they are, to the right specialist.

This shift isn't only in personal banking. We are aiming to service 95% of our commercial customers' needs through mobile and online by 2020, up from nearly 80% today, by introducing a new digital banking service that will greatly improve experience. We're also responding to customer preferences for more innovative lending platforms and products.

We are investing heavily in technology in our NatWest Markets business.

Hundreds of separate product databases will be replaced with a single, scalable platform, which will help reduce costs significantly and dramatically increase the speed at which we can deploy new capabilities for our customers. We are also introducing a single dealer platform, an electronic front door, through which we can provide FX and Rates solutions to our clients. These are the kind of changes that will lower costs while protecting revenue and delivering even better customer service at the same time.

We are committed to running the bank as a more sustainable and responsible business, serving today's customers in a way that also helps future generations, generating long term value for all of our stakeholders and society. In 2016, we improved on our position in a number of rankings, including achieving our highest ever score in the Dow Jones Sustainability Index. We continued with our commitment to manage our impacts on climate change and support our customers to move towards the transition to a low-carbon economy. We continue to support financial education and our goal is to help a further one million more young people understand all about money by the end of 2018.

Our commitment to sustainability is also evident in our annual results, where we have replaced our annual Sustainability Report with a more integrated approach. You will see a number of new elements in the Strategic Report that explain the key influences on our operating environment, and some of the impact we have had over the past year. This is an important step towards fully integrated reporting over the coming years.

#### **Delivering our strategy**

The decision last summer by UK voters to leave the EU will have wide-reaching consequences. In light of this, we reviewed our plan to ensure that it remained valid in a changed macro and political environment. Following that review, I want to re-iterate our

commitment to the strategy we have been pursuing since I became CEO – we firmly believe that our aspiration to reach No.1 for customer service, trust and advocacy will maximise value for our shareholders.

This year we have met all our operating financial targets, though the results of some of our customer NPS and employee engagement surveys show we still have work to do. After the EU referendum result, we promised an update on our targets. We are targeting an unadjusted 12% or greater return on tangible equity, and a below 50% cost to income ratio by 2020, one year later than envisaged when we first set out our plan in 2014.

Our service levels are improving and we believe we can meet our 2020 aspirational customer and colleague targets. Our focus on capital strength remains a cornerstone of our plan. In 2017, we will continue to reduce legacy RWAs, and we will target a CET1 ratio of at least 13%.

This has also been another tough year for our colleagues. I am grateful for their determination in serving our millions of customers every day, despite many negative headlines. Our colleagues are the face of the bank for our customers, and their engagement is critical to our success. One of our five key targets in 2017 is to improve employee engagement.

We no longer have global aspirations and we need to go further still on our operating costs. We expect to take out an additional £750 million of operating costs in 2017 through our focus on simplification and digital transformation. A simpler bank is a more profitable bank and a bank that delivers a better customer experience. Where we can make it easy for our customers, the more business they will do with us and the more sustainable our earnings will become.

#### **Looking ahead**

The progress of the last three years positions us well to achieve our vision for the future. We have the right strategy, and it is starting to deliver

results. Now, we need to go further on cost reduction and faster on digital transformation.

We aren't alone in searching for efficiency gains and investing in digital capability, but the unique strength of this bank lies in the fact that we have a diverse business profile, with scale in all of our chosen markets. Investment in our market leading brands and better customer service will deliver steadier, higher quality earnings. Our focus on service rather than price has also shown that we can continue to grow in areas of strategic opportunity, such as mortgages, without compromising on risk. All of this will deliver a sustainable competitive advantage and a compelling investment case in the longer term.

This is a bank that has been on a remarkable journey. We still have further to go. But the next three years will not be the same as the past three. Legacy issues will take up a decreasing amount of our time and focus. Our customers, our cost base and the measures we plan to implement to return the bank to sustainable headline profits will be where we focus our efforts. Assuming we can conclude our issues on RMBS this year and resolve our residual State Aid obligations, we aim to have RBS back into profit in 2018 representing a significant step towards being able to start repaying UK taxpayers for their support.

# 2016 performance summary

► RBS reported an attributable loss of £6,955 million compared with £1,979 million in 2015. The loss for the year included; litigation and conduct costs of £5,868 million, restructuring costs of £2,106 million, payment of the final DAS dividend of £1,193 million, Capital Resolution disposal losses and impairments of £825 million and a £300 million deferred tax asset impairment.

► The 2016 operating loss of £4,082 million compared with an operating loss of £2,703 million in 2015. The adjusted operating profit of £3,674 million was £731 million, or 17%, lower than 2015.

► The net interest margin (NIM) of 2.18% for 2016 was 6 basis points higher than 2015, as the benefit associated with the reduction in low yielding assets more than offset modest asset margin pressure and mix impacts across the core franchises.

► Excluding expenses associated with Williams & Glyn <sup>(1)</sup>, write-down of intangible assets and the VAT recovery in Q2, adjusted operating expenses have reduced by £985 million, or 11%, compared with 2015, exceeding our target of £800 million. RBS has reduced adjusted operating expenses by over £3 billion in the last three years.

► Adjusted cost income ratio for 2016 was 66% compared with 72% in 2015.

► Risk elements in lending (REIL) as a % of gross customer loans was 3.1%, 80 basis points lower than 31 December 2015 as RBS continues to de-risk its balance sheet.

► Tangible net asset value (TNAV) per share decreased by 56p to 296p compared with 2015 principally

reflecting the attributable loss for the year.

## **PBB, CPB and NatWest Markets delivered increased profits and strong lending growth**

► RBS reported an adjusted operating profit of £4,249 million across PBB, CPB and NatWest Markets, 4% higher than 2015 and an average of over £1 billion a quarter.

► Income across PBB and CPB increased by 2% in 2016 compared with 2015, adjusting for transfers <sup>(2)</sup>, as increased lending volumes more than offset reduced margins. NatWest Markets adjusted income of £1,521 million increased by 16% compared with 2015, adjusting for transfers <sup>(2)</sup>, driven by Rates and Currencies.

► PBB and CPB net loans and advances of £272.1 billion have increased by 10% in 2016, compared with a target of 4%, reflecting strong growth across both residential mortgages and commercial lending.

► Adjusted cost income ratio improved to 63% compared with 65% in 2015 as we continue to deliver efficiencies across PBB, CPB and NatWest Markets.

## **RBS continues to address its remaining legacy issues and drive forward its restructuring programme**

► Restructuring costs were £2,106 million for 2016, compared with £2,931 million in 2015, and included a £750 million provision in respect of the plan by the Commissioner responsible for EU competition policy to propose to the College of Commissioners to open proceedings to gather evidence on an alternative plan for RBS to meet its remaining State Aid obligations in respect of Williams

& Glyn. If adopted, this alternative plan would replace the existing requirement to achieve separation and divestment by 31 December 2017. In addition, £706 million of the remaining restructuring costs related to Williams & Glyn, including £146 million of termination costs associated with the decision to discontinue the programme to create a cloned banking platform.

- ▶ Litigation and conduct costs of £5,868 million included; a £3,107 million provision in relation to various investigations and litigation matters relating to RBS's issuance and underwriting of residential mortgage-backed securities (RMBS), an additional charge in respect of the settlement with the National Credit Union Administration Board to resolve two outstanding RMBS lawsuits, a provision in respect of the UK 2008 rights issue shareholder litigation, additional PPI provisions, a provision in respect of the FCA review of RBS's treatment of SMEs and a provision in Ulster Bank Rol in respect of an industry wide examination of tracker mortgages.
- ▶ A net strategic disposal gain of £164 million includes a £246 million gain on disposal of RBS's stake in Visa Europe partially offset by losses associated with the sale of our Russian subsidiary and exit of Kazakhstan.

#### **PBB, CPB and NatWest Markets operating performance**

- ▶ Across our three customer facing franchises, PBB, CPB and NatWest Markets, adjusted operating profit of £4,249 million, was £163 million, or 4% higher than 2015.
- ▶ UK PBB adjusted operating profit of £2,202 million was £33 million, or 2%, higher than 2015 as increased

income and reduced costs were partially offset by increased impairments. Total income increased by £90 million, or 2%, to £5,290 million compared with 2015 as the benefit of increased lending more than offset reduced margins, down 17 basis points to 3.01%, and lower fee income, reflecting reduced credit card interchange fees and increased cash back payments following the launch of the Reward account. Net loans and advances increased by 10% to £132.1 billion in 2016 principally driven by mortgage growth.

- ▶ Ulster Bank Rol adjusted operating profit of £229 million was £35 million lower than 2015 principally reflecting a £28 million reduction in net impairment releases. REIL decreased by £1.3 billion in Q4 2016 largely driven by the sale of a portfolio of distressed loans.
- ▶ Commercial Banking adjusted operating profit of £1,273 million was £111 million, or 8%, lower than 2015 primarily reflecting a £137 million increase in net impairment losses, largely driven by a single name charge in respect of the oil and gas portfolio. Adjusting for business transfers, total income increased by £21 million, or 1%, reflecting higher asset and deposit volumes partially offset by asset margin pressure. Net loans and advances increased by 10% in 2016 to £100.1 billion.
- ▶ Private Banking<sup>(3)</sup> adjusted operating profit of £149 million increased by £36 million, or 32%, compared with 2015 as increased asset volumes drove a £13 million, or 2%, uplift in income and cost efficiencies resulted in a £7 million, or 1%, reduction in adjusted operating expenses. In addition, net impairment losses reduced by £16 million.

- ▶ RBS International adjusted operating profit of £195 million was £16 million, or 8%, lower than 2015 largely reflecting a £13 million, or 8%, increase in adjusted operating expenses, driven by a number of one-off charges, and a £10 million net impairment loss in 2016. Partially offsetting, total income increased by £7 million, or 2%, driven by increased asset volumes.

- ▶ NatWest Markets adjusted income of £1,521 million was 16% higher than 2015, adjusting for transfers, driven by Rates and Currencies, which benefited from sustained customer activity and favourable market conditions following the EU referendum and subsequent central bank actions. An adjusted operating profit of £201 million compared with a loss of £55 million in 2015.

#### **Capital Resolution & Central items operating performance**

- ▶ Capital Resolution adjusted operating loss of £1,432 million compared with a loss of £412 million in 2015 and included disposal losses and impairments of £825 million, of which £683 million related to the shipping portfolio. RWAs reduced by £14.5 billion in 2016 to £34.5 billion.
- ▶ Central items adjusted operating profit of £455 million compared with £272 million in 2015 and included a £349 million FX gain, principally associated with the weakening of sterling against the US dollar, a £227 million VAT recovery, a £97 million foreign exchange reserve recycling gain and other gains, partially offset by a £510 million loss in respect of IFRS volatility<sup>(4)</sup> due to reductions in long term interest rates (2015 – £15 million profit).

# Delivery against our 2016 targets

Strategy goal	2016 target	2016
Strength and sustainability	Maintain Bank CET1 ratio of 13%	CET1 ratio of 13.4%
	£2 billion AT1 issuance	£2 billion equivalent AT1 issued in Q3 2016
	Capital Resolution RWAs around £30-35 billion	RWAs down £14.5 billion to £34.5 billion
Customer experience	Narrow the gap to No.1 in NPS in every primary UK brand	Year on year Commercial Banking have narrowed the gap. NatWest Personal, Ulster Business & Commercial in Northern Ireland and Ulster Business Direct in Republic of Ireland, have seen improvements in NPS.
Simplifying the bank	Reduce operating expenses by £800 million	Operating expenses down £985 million <sup>(5)</sup>
Supporting sustainable growth	Net 4% growth in PBB and CPB customer loans	Net lending in PBB and CPB up 10%
Employee engagement	Raise employee engagement to within two points of the Global Finance Services (GFS) norm	Down 3 points to be 6 points adverse to GFS norm

## Notes:

- (1) Williams & Glyn refers to the business formerly intended to be divested as a separate legal entity and comprises RBS England and Wales branch-based businesses, along with certain small and medium enterprises and corporate activities across the UK. During the period presented Williams & Glyn has not operated as a separate legal entity.
- (2) NatWest Markets' results include the following financials for businesses subsequently transferred to Commercial Banking: total income of £98 million for the year ended 2015.
- (3) Private Banking serves high net worth individuals through Coutts and Adam & Company.
- (4) IFRS volatility arises from the changes to fair value of hedges of loans which do not qualify for hedge accounting under IFRS.
- (5) Cost saving target and progress 2016 calculated using operating expenses excluding restructuring costs £2,106 million (2015 – £2,931 million), litigation and conduct costs £5,868 (2015 – £3,568 million), write down of goodwill nil (2015 – £498 million), write down of other intangible assets of £117 million (2015 – £75 million), the operating costs of Williams and Glyn £393 million (2015 – £359 million) and the VAT recovery £227 million.



# Building a stronger RBS

RBS is progressing with its plan to build a strong, simple, fair bank for customers and shareholders.

During 2016, RBS narrowed the range of uncertainty around its capital position by addressing a number of legacy issues, and continued to strengthen its capital base.

- ▶ CET1 ratio remains ahead of our 13.0% target at 13.4%, a 210 basis points reduction compared with Q4 2015 principally reflecting the attributable loss, c.300 basis points, partially offset by a £14.4 billion reduction in RWAs, c.100 basis points. During Q4 2016, CET1 ratio reduced by 160 basis points as the benefit of the reduction in RWAs was more than offset by the attributable loss.
- ▶ RWAs reduced by £14.4 billion, or 6%, during 2016 to £228.2 billion driven by £14.5 billion of disposals and run-off in Capital Resolution and a £3.9 billion reduction associated with the removal of Citizens operational risk RWAs, partially offset by an increase associated with the weakening of sterling and lending growth across our core franchises.
- ▶ On 10 August 2016 RBS announced that it had successfully completed the pricing of \$2.65 billion 8.625% AT1 capital notes, with £4.0 billion equivalent issued since August 2015. (1.8% of Q4 2016 RWAs)
- ▶ Leverage ratio reduced by 50 basis points during 2016 to 5.1% reflecting the attributable loss for the year partially offset by the AT1 issuance and reduction in leverage exposure.
- ▶ RBS issued £4.2 billion equivalent senior debt, which it expects to be eligible to meet its 'Minimum Requirement for Own Funds and Eligible Liabilities' (MREL), in line with our targeted £3-5 billion senior debt issuance for the year. £1.5 billion seven year 2.5% notes and \$1.5 billion ten year 4.8% notes

were issued in Q1 2016 and \$2.65 billion seven year 3.875% notes were issued in Q3 2016.

- ▶ In addition, RBS successfully completed the cash tender of £2.3 billion of certain US dollar, sterling and euro senior debt securities. The tender offers were part of the ongoing transition to a holding company capital and term funding model in line with regulatory requirements and included securities that RBS considers non-compliant for MREL purposes. In total, during 2016, £10 billion has matured across our funding pools and we have redeemed £8.2 billion through calls and repurchase.
- ▶ As part of the 2016 Bank of England stress testing exercise RBS submitted a revised capital plan, incorporating further capital strengthening actions, which was accepted by the PRA Board.

## **RBS has successfully addressed a number of the remaining legacy issues and continues to de-risk its balance sheet**

- ▶ During Q1 2016 RBS made the final dividend payment in respect of the DAS, £1,193 million, an action that was taken to normalise the ownership structure of the Bank.
- ▶ In June 2016, the triennial funding valuation of the Main scheme of The Royal Bank of Scotland Group Pension Fund was agreed which showed that as at 31 December 2015 the value of liabilities exceeded the value of assets by £5.8 billion. In March 2016, to mitigate this anticipated deficit, RBS made a cash payment of £4.2 billion.

The next triennial valuation is due to occur at the end of 2018 with agreement on any additional contributions by the end of March 2020. As at 31 December 2016, the Main scheme had an unrecognised surplus reflected by a ratio of assets to liabilities of c.115% under IAS 19 valuation principles.

- ▶ On 11 April 2016, RBS completed the successful transfer of the Coutts International businesses in Asia and the Middle East to Union Bancaire Privée, the final milestone in the sale of our International Private Bank. During 2016 we also completed the sale of our Russia and Kazakhstan subsidiaries.
- ▶ Risk elements in lending (REIL) of £10.3 billion were £1.8 billion lower than 31 December 2015 and represented 3.1% of gross customer loans, compared with 3.9% as at 31 December 2015 and 3.8% at 30 September 2016.
- ▶ In line with the progress to de-risk the balance sheet, exposures to the shipping and oil and gas sectors continued to reduce during 2016, with potential exposures declining by 29% to £5.2 billion and by 22% to £5.3 billion respectively. As at the end of 2016, our total exposure to the coal mining, oil and gas and power generation sectors represented 1.4% of our total lending.

## Building the number one bank for customer service, trust and advocacy in the UK

### Supporting households and business customers

- ▶ RBS continued to deliver strong support for both household and business customers. Within UK PBB, gross new mortgage lending of £29.8 billion was 29% higher than 2015. Across 2016, our market share of new mortgages was 12%, supporting a growth in stock share to 8.8% at end 2016 from 8.2% at end 2015. As a result, total UK PBB net loans and advances increased by 10% compared with 2015. Commercial Banking net loans and advances have also grown by 10% over the course of 2016 reflecting increased borrowing across a number of sectors.
- ▶ The Reward account continued to show positive momentum and now has 1,149,000 fee-paying customers compared with 202,000 at 31 December 2015. We have seen positive evidence of increased levels of engagement, with overall current account attrition levels falling by 7% in the year. This is particularly evident across our Private and Premium customer, with attrition 12% lower. We continue to embed the product across our population of valuable main bank customers.
- ▶ RBS continues to support UK business growth through the launch of 6 new business accelerator hubs in 2016, bringing the total to 12. This included the opening of an Entrepreneurial Centre in our Edinburgh headquarters. In addition, NatWest launched a £1 billion lending fund to support small businesses.

### Investing in our operational capabilities and enhancing digital channels

- ▶ RBS continued to make better use of our digital channels to make it simpler to serve our customers and easier for them to do business with us. We now have 4.2 million customers regularly using our mobile app in the UK, 19% higher

than the end of 2015, and around 60% of our personal customers used a digital channel within the last 90 days. In 2016, we more than doubled the number of customers who purchased a product through our mobile channel compared with 2015. NatWest customers can now apply for personal loans, credit cards and overdrafts via the mobile app, facilitating approximately 8% of total applications. Our new business banking 'Online Account Opening' service now allows start up business customers to submit an application online in just ten minutes and get a sort code and account number in under an hour.

- ▶ Nearly 80% of our commercial customers' interaction with us is via digital channels, with 270,000 payments processed every day.
- ▶ In addition to our digital channels, RBS continues to provide multiple physical channels for serving customers, including access to a network of c.11,500 Post Office branches in the UK, c.1,000 An Post branches in the Republic of Ireland, and 41 mobile banking vans, alongside our existing network of 1,425 branches and 4,646 ATMs across PBB.
- ▶ RBS became the first UK Bank to be accredited by the Royal National Institute for Blind People for having an accessible mobile app for blind and partially sighted customers. In addition, we launched a new service for British Sign Language (BSL) customers, making it possible to instantly chat with an advisor through a BSL interpreter.

- ▶ Coutts won the best private bank in the UK for the fifth year running, best private bank for philanthropy services and best initiative of the year in client facing technology at the Global Private Banking Awards, and was highly commended for innovation for its 'Coutts Concierge Online'.

### Investing in our people

- ▶ In 2016, RBS was one of only two banks to achieve formal recognition from the Chartered Banker Professional Standards Board for excellence in implementing, monitoring, reporting and commitment to the Foundation Standard for Professional Bankers.
- ▶ Delivered leadership training to almost 16,000 leaders through a comprehensive 'Determined to Lead' programme.
- ▶ We continue to work towards our goal of having at least 30% senior women in our top three leadership layers across each business by 2020 and to be fully gender balanced (50/50) by 2030. As at 31 December 2016, in aggregate terms 34% of our top three leadership layers were female.
- ▶ RBS has attained silver status in the Business Disability Forum's Disability Standard, scoring 88% in its assessment of accessibility and inclusion in the workplace.
- ▶ RBS has moved up to 13th place, from 32nd last year, in Stonewall's annual Top 100 employers for lesbian, gay, bi and trans (LGBT) staff, the highest position it has achieved in the index to date.



# Looking forward

## Capital reorganisation

It is our intention to implement a capital reorganisation in 2017 in order to increase the distributable reserves of the parent company, RBSG plc, providing greater flexibility for future distributions and preference share redemptions. We intend to seek shareholder approval to reduce the share premium account by around £25 billion and to cancel the capital redemption reserve, around £5 billion. This will, subject to approval by shareholders and regulators, and confirmation by the Court of Session in Edinburgh, increase RBSG plc distributable reserves by around £30 billion.

## Ring-fenced structure

As previously announced, on 1 January 2017, RBS made a number of changes to its legal entity structure to support the move towards a ring-fenced structure, with further changes planned prior to 1 January 2019. Our new brand strategy is designed to align with our business strategy and future ring-fenced structure. NatWest will be our main customer facing brand in England, Wales and Western Europe, and in Scotland, Royal Bank of Scotland will be our core brand. In addition, our Corporate & Institutional Banking business has been rebranded as NatWest Markets in readiness for our future ring-fenced structure. The ring-fenced banking group is expected to comprise of 80% of RBS risk-weighted assets.<sup>(1)</sup>

## IFRS9

RBS continues to develop its processes to enable IFRS 9 Financial Instruments to be implemented on 1 January 2018; an estimate of the initial impact will be included in 2017 H1 interim reporting.

## Williams & Glyn

► On 17 February 2017, RBS announced that it had been informed by HM Treasury ("HMT") that the Commissioner responsible for EU competition policy plans to propose to the College of Commissioners to open proceedings to gather evidence on an alternative plan for RBS to meet its remaining State Aid obligations. If adopted, this alternative plan would replace the existing requirement to achieve separation and divestment by 31 December 2017 of Williams & Glyn. As previously disclosed, none of

the proposals to acquire the business received by RBS can deliver a full separation and divestment before the 31 December 2017 deadline.

- RBS has agreed that HMT will now seek formal amendment to RBS's State Aid commitments to pave the way for the Commissioner to propose to open proceedings, as described above. In addition to the Commission's proceedings, HMT will carry out a market testing exercise in parallel. The opening of the Commission's proceedings does not prejudice the outcome of the investigation.
- The plan envisages that RBS will deliver the following revised package of remedies to promote competition in the market for banking services to small and medium enterprises ("SMEs") in the UK:
  - A fund, administered by an independent body, that eligible challenger banks can access to increase their business banking capabilities;
  - Funding for eligible challenger banks to help them incentivise SMEs to switch their accounts from RBS paid in the form of "dowries" to eligible challenger banks;
  - RBS granting business customers of eligible challenger banks access to its branch network for cash and cheque handling, to support the measures above; and
  - An independent fund to invest in fintech to support the business banking of the future.
- The 2016 Annual Results include a £750 million restructuring provision as a consequence of this proposal.

## 2017 Outlook <sup>(2)</sup>

- Subject to providing fully for the remaining legacy issues, RMBS exposures in particular, RBS currently expects that 2017 will be its final year of substantive legacy clean up with significant one-off costs. Consequently, we anticipate that the bank will be profitable in 2018.
  - We are targeting net loans and advances growth of 3% across PBB and CPB, including taking into account the impact of balance sheet reductions associated with the RWA reduction target. We anticipate that this growth will be largely within PBB as we expect to see moderate growth in some segments in CPB, whilst at the same time selectively reducing exposures
- with weak returns and continuing to actively manage certain legacy loan exposures.
- We expect that income in 2017 will continue to be supported by balance sheet growth across PBB and CPB. Within UK PBB, we anticipate that income will increase in 2017 compared with 2016, as we have already absorbed significant margin pressure from the changing mortgage mix and the impact of the sharp fall in interchange rates. Across CPB, we expect income to be broadly stable with continued competitive pressure on margins, given the interest rate environment. NatWest Markets is expected to continue to benefit from increased market volatility and customer activity and we anticipate that 2017 income will be above previously indicated targets of £1.3 - £1.4 billion.
  - RBS plans to reduce adjusted operating expenses by a further £750 million in 2017, in addition to the £3.1 billion achieved across 2014 to 2016, and we expect that the adjusted cost:income ratio will improve across our combined PBB, CPB and NatWest Markets franchises in 2017 compared with 2016.
  - Net impairment charges should remain meaningfully below normalised levels in 2017. However, we expect the level of net impairment charges to be driven by a combination of increased gross charges and a materially reduced benefit from releases. Recent UK economic performance has been better than previous forecasts leading to improved expectations for the 2017 economic outlook. However, the medium term outlook remains less certain, and together with the increased volatility expected with the introduction of IFRS 9, quantification of future credit losses is more challenging beyond 2017 at this point. We continue to remain mindful of potential downside risks including from single name / sector driven events and lower releases of provisions.
  - We continue to expect that cumulative Capital Resolution disposal losses will total approximately £2.0 billion since the beginning of 2015, with £1,192 million of losses incurred to date (2016; £825 million, 2015; £367 million) with most of the balance expected to be incurred during 2017. Excluding RBS's stake in Alawwal Bank (previously

Saudi Hollandi Bank, £7.9 billion at 31 December 2016), we expect Capital Resolution RWAs to be in the range £15-£20 billion by the end of 2017, at which point we plan to wind up Capital Resolution and transfer the assets back into the rest of the bank.

- Excluding restructuring costs associated with the State Aid obligations relating to Williams & Glyn, we expect to incur restructuring costs of approximately £1 billion in 2017 and approximately a further £1 billion in aggregate during 2018 and 2019. Approximately 40% of this cost is expected to relate to the optimisation of our property portfolio.
- Further to the update on 17 February 2017 in respect of the remaining State Aid obligations regarding the business known as Williams & Glyn, and subject to the alternative plan being finalised and adopted by the European Commission (EC) and further discussions with the EC and HMT, RBS will assess the timing and manner in which it would reincorporate the business into the RBS franchises. This reintegration would likely create some additional restructuring charges during 2017 and 2018.
- We are targeting a CET1 ratio of at least 13% at the end of 2017. As part of the 2016 Bank of England stress testing exercise, RBS submitted a revised capital plan, incorporating further capital strengthening actions, which was accepted by the PRA Board.

► RBS issuance plans for 2017 focus on issuing £3-£5 billion MREL-compliant Senior holding company (RBSG) securities. We do not currently anticipate the need for either AT1 or Tier 2 issuances. In addition, and reflecting our strategic progress, we also target a progressive return to other funding markets to support our lending growth.

► RBS continues to deal with a range of significant risks and uncertainties in the external economic, political and regulatory environment and manage conduct-related investigations and litigation, including RMBS. Substantial additional charges and costs may be recognised in the coming quarters which would have an impact on RBS's level of capital and financial performance and condition.

#### Medium term outlook <sup>(2)</sup>

- We now target achieving our sub 50% cost:income ratio and 12% return on tangible equity targets in 2020, one year later than originally planned. Our confidence in achieving the targets is underpinned by our ability to protect income and drive cost reductions whilst managing credit and market risk and driving further capital efficiency.
- We expect to be able to grow volumes faster than market growth rates over the coming years in chosen segments across PBB and CPB.

► We plan to reduce adjusted operating expenses in the order of £2 billion in the next four years with around two thirds of this from the core bank.

► We are targeting a gross RWA reduction of approximately £20 billion across PBB, CPB and NatWest Markets by the end of 2018, with some offsetting volume growth. We expect that the reduction will be largely achieved through improvements in the quality of our risk models, exiting low return, non strategic and risk intensive asset pools, improved risk metrics in certain portfolios and benefits from data clean-up. We estimate that the income loss associated with this reduction will be in the range £250 million - £300 million on an annualised, pre tax, basis.

► We continue to monitor the ongoing discussions around the potential further tightening of regulatory capital rules and recognise that this could result in RWA inflation in the medium term.

► In view of the significant risks and uncertainties in the external economic, political and regulatory environment including uncertainties around the resolution of RMBS, the timing of returning excess capital to shareholders through dividends or buybacks remains uncertain.

#### Notes:

(1) Based on RBS future business profile business and excludes Capital Resolution.

(2) The targets, expectations and trends discussed in this section represent management's current expectations and are subject to change, including as a result of the factors described in this document and in the "Risk Factors" on pages 432 to 463 of the 2016 Annual Report and Accounts. These statements constitute forward looking statements, please see Forward Looking Statements on pages 465 and 466 of the 2016 Annual Report and Accounts.

## 2017 targets

As we work towards our long-term goals, we have set the following targets for 2017.

Strategy goal	Our long-term targets	Our 2017 goals
Strength and sustainability	CET1 ratio of 13% RoTE <sup>(1,2)</sup> ≥ 12%	Maintain bank CET1 ratio of 13%
Customer experience	Number 1 for service, trust and advocacy	Significantly increase NPS or maintain No.1 in chosen customer segments
Simplifying the bank	Headline cost:income ratio <50%	Reduce operating expenses by at least £750 million <sup>(3)</sup>
Supporting sustainable growth	Leading market positions in every franchise	Net 3% growth in total PBB and CPB loans to customers <sup>(4)</sup>
Employee engagement	Employee engagement in upper quartile of Global Financial Services (GFS) norm	Improve employee engagement

#### Notes:

(1) Calculated using (loss)/profit for the period attributable to ordinary shareholders.

(2) Tangible equity is equity attributable to ordinary shareholders less intangible assets.

(3) Cost saving target and progress 2017 calculated using operating expenses

excluding restructuring costs, litigation and conduct costs, write down of goodwill and the 2016 VAT recovery.

(4) Lending growth target is after including the impact of balance sheet reductions associated with the RWA reduction target across PBB, CPB and NatWest Markets as outlined in the outlook statement.

# Business model and strategy

## Our strategy

We are building a better bank for our customers, and one that will deliver sustainable returns for shareholders. Our purpose is to serve customers well, and to do so, we are becoming a safer, simpler, customer-focused UK and Ireland bank.

## Our plan

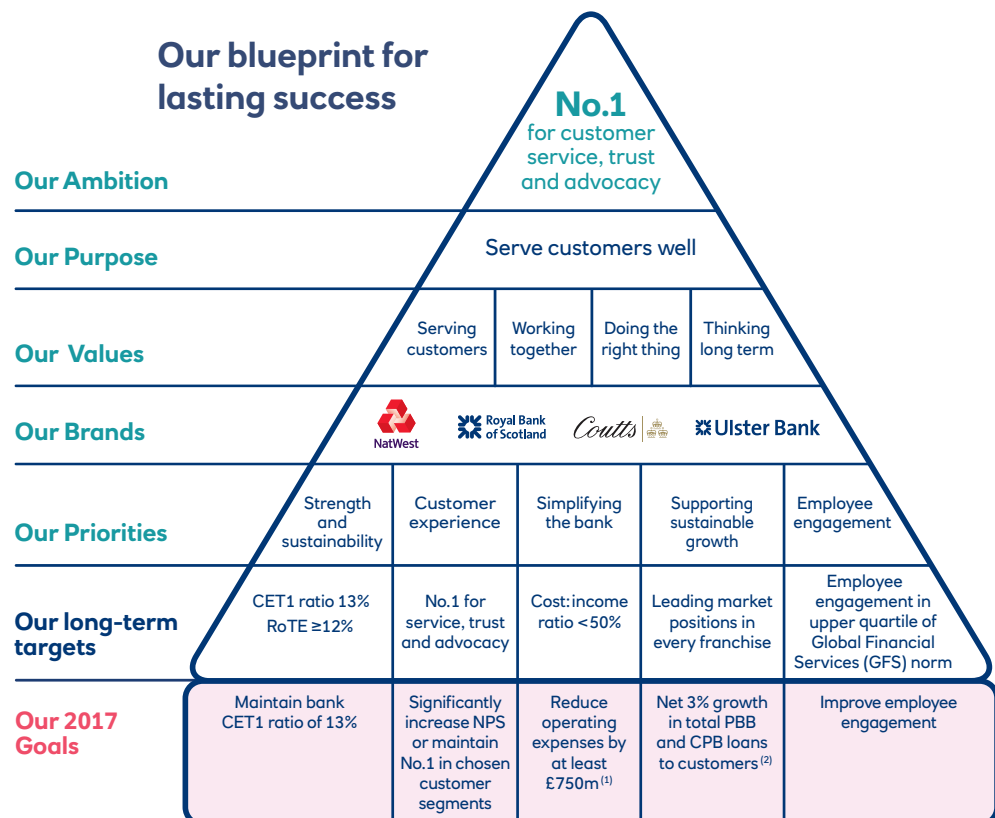
Underpinning that ambition is our blueprint for success. This is our plan which drives our strategic decision making.

RBS is continuing to build a bank that is easy to do business with, and meets customers' continually evolving needs.

Our plan focuses on delivering excellent customer service through all of our brands.

Creating lasting relationships with our customers, who advocate for our bank, is the key to generating sustainable value.

## Our blueprint for lasting success



Notes:

- (1) Cost saving target and progress calculated using operating expenses excluding restructuring costs, litigation and conduct costs, write down of goodwill and the 2016 VAT recovery.
- (2) Lending growth target is after including the impact of balance sheet reductions associated with the RWA reduction target across PBB, CPB and NatWest Markets as outlined in the outlook statement.

## Our priorities

### **Strength and sustainability**

We remain focused on building a strong and stable bank. We have continued to improve the fundamentals, by increasing our capital strength, building a robust liquidity position and balancing our loan to deposit ratio.

### **Customer experience**

We are investing in our people, service, and product proposition to ensure we provide market leading technology and signature customer experiences, through a wide variety of channels.

### **Simplifying the bank**

Streamlining of processes and removing unnecessary complexity

lowers our operating costs, and makes our customer interactions more straightforward.

### **Supporting sustainable growth**

A strong sustainable business grows with its customers. We continue to support our customers through offering products and services which meet their needs.

### **Employee engagement**

Engaged colleagues lead to engaged customers. At RBS we are committed to investing in our colleagues and creating leaders who inspire and empower their teams.

## Our structure

We have three customer franchises, and each is underpinned by a range of distinct brands, which are the route through which we engage with our customers.

Our franchises share operational and control functions, deriving economies of scale and diversification benefits. Our brands are personalised and each reflects a particular targeted customer segment.

### **Personal and Business Banking (PBB)**

With a branch network and mobile, telephone and online banking propositions, PBB services our retail banking, mass affluent and small business customers in both the UK and Republic of Ireland.

PBB provides a simple range of products, including current accounts, loans and mortgages, to meet all core banking needs.

### **Commercial and Private Banking (CPB)**

CPB serves our commercial and our high net worth customers in the UK and Western Europe.

Commercial Banking supports our corporate clients by providing comprehensive commercial banking and financing services with sector expertise. This includes specialist finance such as invoice finance, asset finance and leasing.

Our Private Banking business offers high net worth clients private banking, wealth planning and investment management services.

RBS International (RBSI) continues to focus on supporting retail, commercial, corporate and financial institution customers in Jersey, Guernsey, Isle of Man, Gibraltar and Luxembourg.

### **NatWest Markets**

Focusing on our core markets in the UK and Western Europe, NatWest Markets provides financing and risk management to our UK and Western Europe corporate customers and global financial institutions.



### Franchises

Our franchises bring together customers determined by the scale and complexity of their financial needs. This groups our business units that have the greatest economies of scale and synergies.

Teams define and deliver the customer proposition, and are accountable for end-to-end customer processes and products. The teams partner with functions and services to develop cost-effective propositions that meet customer needs.



### Services

Services provide business-aligned technology, operations and property services across the bank.

Operations are centralised to provide cost-efficient and consistently strong customer service, through simple processes and economies of scale.

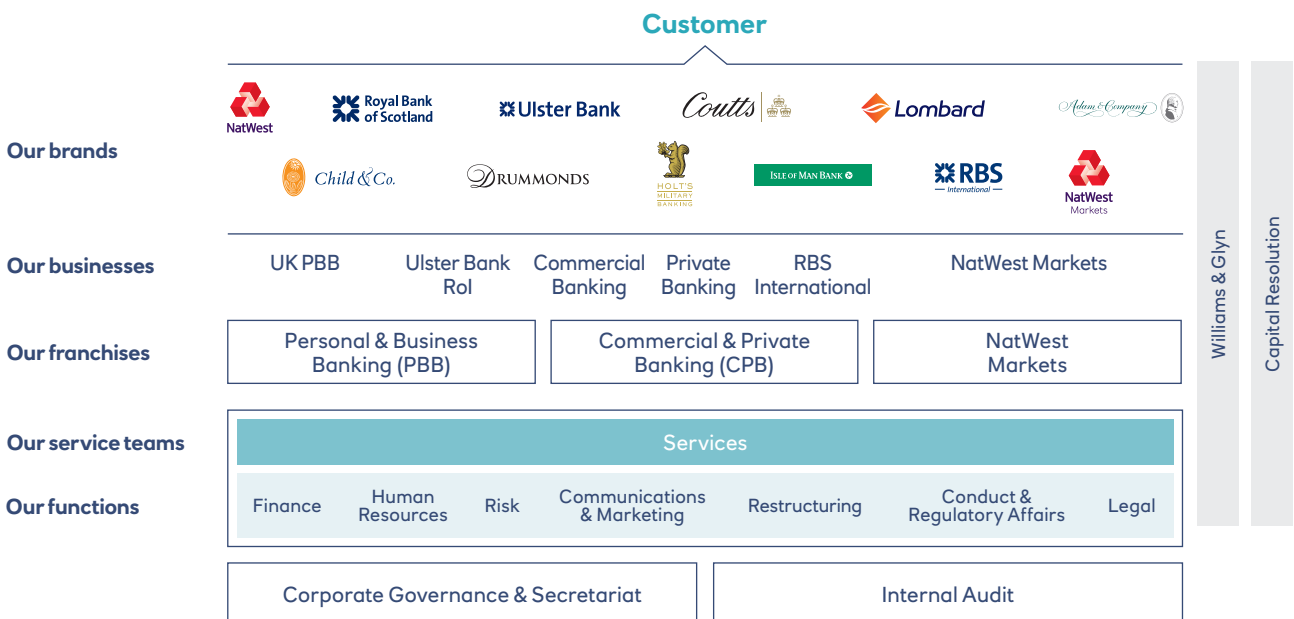
It is also accountable for technology risk, payments, data, change management and the bank's fraud and security functions.



### Functions

These teams define functional strategy and the financial plan to support the franchises and other functions.

Most functions are a mix of control, expertise and advisory. All common support activities across the organisation are included.



## Product and services

Our products and services are designed to ensure that we can create sustainable value for both our shareholders and our customers. We believe that keeping our product range simple and accessible is crucial to our success.

Banking & Risk Management	Personal Lending	Deposits	Investments	Commercial Lending	Capital Markets
<ul style="list-style-type: none"> <li>Payments</li> <li>Insurance</li> <li>Liquidity management</li> </ul>	<ul style="list-style-type: none"> <li>Secured</li> <li>Personal loans</li> <li>Credit cards</li> </ul>	<ul style="list-style-type: none"> <li>Current accounts</li> <li>Savings accounts</li> </ul>	<ul style="list-style-type: none"> <li>Portfolio management</li> <li>Unitised funds</li> <li>Financial planning</li> </ul>	<ul style="list-style-type: none"> <li>Business lending</li> <li>Invoice financing</li> <li>Asset-backed lending</li> </ul>	<ul style="list-style-type: none"> <li>Rates</li> <li>Currencies</li> <li>Financing</li> </ul>

## Our brands

Our brands are our main connection with customers. Each takes a clear and differentiated position that will help us strengthen our relationships with our customers, stand out in the market, and build the value of our brands.



NatWest serves over 14 million customers in England and Wales, supporting them with their banking needs, at all stages in their lives.



Royal Bank of Scotland is committed to serving Scottish communities.



Ulster Bank operates both in the Republic of Ireland and Northern Ireland.



Exceptional service sits at the heart of Coutts, a business that has been built on understanding the needs of their private and commercial clients.



Lombard is the UK's largest provider of asset finance, helping to take businesses to the next level with a forward-looking entrepreneurial approach.



Adam & Company provides progressive private banking, tailoring its services and solutions to match each client and their unique needs.



Child & Co is one of the oldest private banks in the UK, providing bespoke banking services from the legal heart of London.



Drummonds has served private banking customers for over 300 years, providing a discreet and professional service.



As the bank of the British Armed Forces, Holt's prides itself on understanding the complexities of serving in the military and providing a personalised service.



Isle of Man Bank is the 'community bank' and the island's oldest native bank, offering retail, private and business banking services to local customers.



RBS International is one of the world's leading offshore banks, operating under three distinct brands – RBS International, NatWest and Isle of Man Bank.



Focusing on our core markets in the UK and Western Europe, NatWest Markets provides financing and risk management to our UK and Western Europe corporate customers and global financial institutions.



## Flying high

Sarah-Jane Anthony saw her first falconry display aged seven and was hooked. Twenty years later, she decided to follow her dream and start her own business. Now she runs her own award-winning falconry centre in Essex.

"I've banked with NatWest all my life and when I needed a business account, Khaled, the local NatWest Women in Business specialist, was really supportive. Without his help and advice, I don't think I'd be here today."

Through our Chartered Banker accreditation programme in association with Everywoman, we've trained 400 Women in Business specialists across the bank. Their knowledge makes them ideally placed to help female business owners and budding entrepreneurs with their banking needs.



# Building a more sustainable bank

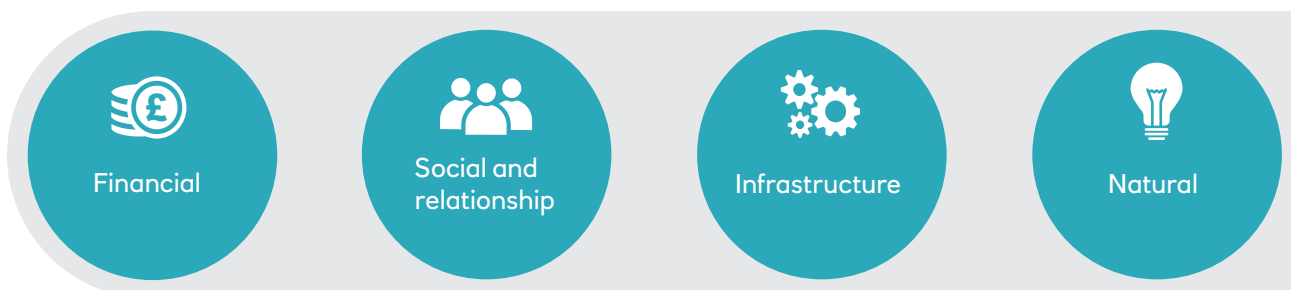
Our goal is to be No.1 for customer service, trust and advocacy. We are changing our culture and priorities for the better. We are committed to building a bank that works for all stakeholders.

By delivering the best possible service for customers to meet their needs, we aim to achieve a return for our shareholders. At the same time, we recognise our responsibility towards

the society we serve and operate in. It is only by supporting our customers and communities to succeed that we will be become a more sustainable bank.

## Our key resources and relationships

RBS provides financial services to individuals and businesses, primarily in the UK and Ireland. We rely on financial, human, intellectual, social, infrastructure and natural capital to do so. We leverage these forms of capital through our expertise, technology and customer focus across our different brands. This helps to improve customer service quality, personalised through our brands. We also seek to create sustainable value for our shareholders and other stakeholders, including customers, employees, and civil society.



We make use of shareholder capital and other forms of financial capital, including £353.5 billion in customer deposits.<sup>(1)</sup>

18.9 million customers in the UK and Republic of Ireland. In 2016, we opened 40,860 Foundation Accounts <sup>(2)</sup>, helping customers who may otherwise face difficulties when opening a bank account.

We continue to provide multiple physical channels for serving customers, including access to a network of c.12,500 Post Office and An Post branches <sup>(3)</sup> and 41 mobile banking vans alongside our existing network of 1,425 branches and 4,646 ATMs.

754 GWh of energy consumed and 9,965 tonnes of paper used in 2016.<sup>(4)</sup>



# How we create value for customers and society

Our activities generate outcomes across all parts of the economy:



Keeping money safe and accessible for our depositors, including preventing 498,000 cases of attempted fraud amounting to £303 million in the UK.<sup>(5)</sup>



Offering lending, advice and services to individuals. Supporting customers with financial life events, including £33.7 billion of gross new mortgage lending<sup>(6)</sup> to help our customers buy homes.



Enabling individuals and businesses to make payments effectively and efficiently, including more than doubling the number of products sold through our mobile channel compared with 2015.



Providing working capital and lending to help businesses meet their goals, including £30.5 billion<sup>(7)</sup> in lending to small and medium-sized enterprises across England, Scotland and Wales, and c. £1.0 billion in lending to infrastructure projects.



Supporting local communities, including £2.5 million<sup>(8)</sup> of grants made by our Skills & Opportunities Fund to 125 organisations, who support people from disadvantaged communities start-up in business or get into employment.



Supporting entrepreneurs to start up in business, including 1,736 businesses<sup>(9)</sup> helped through Entrepreneurial Spark powered by NatWest.



Investing in our people and partners to develop a skilled workforce, including the delivery of leadership training to almost 16,000 leaders through a comprehensive 'Determined to Lead' programme.



Payment of £1.32 billion<sup>(10)</sup> in tax to the UK Government, which supports central government and local authority spending.

## Notes:

- (1) Customer deposits excluding repurchase agreements and stock lending.
- (2) Number of new Foundation Accounts opened across NatWest Plc, Royal Bank of Scotland plc and Ulster Bank Ireland DAC.
- (3) Comprises c.11, 500 Post Office branches in the UK and c.1000 An Post branches in the Republic of Ireland.
- (4) For further details refer to page 35.
- (5) Data relates to reported attempted fraud cases and prevented third party losses in the UK (not including policy declines for debit cards).
- (6) Gross new mortgage lending across UK PBB, Ulster Bank Rol and RBSI.
- (7) SME lending balances in over 9960 postcode sectors across England, Scotland & Wales.
- (8) Data is compiled by Project North East (PNE) on and is based on the total spend allocated by each Regional Board.
- (9) Data is compiled by Entrepreneurial Spark. The data includes all businesses which have been part of the programme since launch in 2012.
- (10) Comprises £174 million corporate tax, £660 million irrecoverable VAT, £208 million bank levies and £279 million employer payroll taxes.

## Our business model

Our purpose is to serve our customers well; we earn income by providing lending and deposit services to our customers. We incur operating expenses in providing these services, and accept risk; including credit risk, liquidity risk and currency risk. The operating profit generated by the bank is targeted to compensate shareholders for the cost of these risks. Building a safe and customer-focused bank is central to our ability to create value.

The main source of our income is the interest income earned from loans and advances to our personal, business and commercial customers. We also earn fees from transactions and other services provided to our customers.

We pay interest to customers and other investors who have placed deposits with us and bought our debt securities. The difference between these is our net interest income. We also pay benefits to our customers, through loyalty products such as our Reward Account.

NatWest Markets puts its customers at the centre of the way it does business, making working with the bank easy and rewarding. The bank is organised around providing the right solution to meet its customers' needs. It anticipates emerging issues and provides depth of insight and innovative ideas.



Human and Intellectual

A capable, caring and motivated workforce of 79,099 (permanent headcount). In 2016, we recruited 254 graduates and 283 apprentices.

# Our approach

## Our Values

Our Values guide our actions every day, in every part of our business. The values are the foundation of how we work at RBS.



### Doing the right thing

We do the right thing.

We take risk seriously and manage it prudently.

We prize fairness and diversity and exercise judgment with thought and integrity.



### Working together

We care for each other and work best as one team.

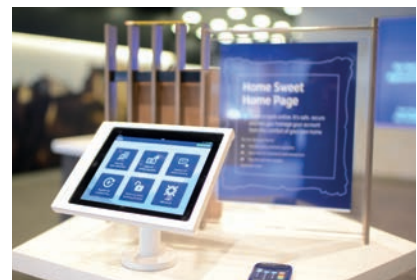
We bring the best of ourselves to work and support one another to realise our potential.



### Serving customers

We exist to serve customers.

We earn their trust by focusing on their needs and delivering excellent service.



### Thinking long term

We know we succeed only when our customers and communities succeed.

We do business in an open, direct and sustainable way.

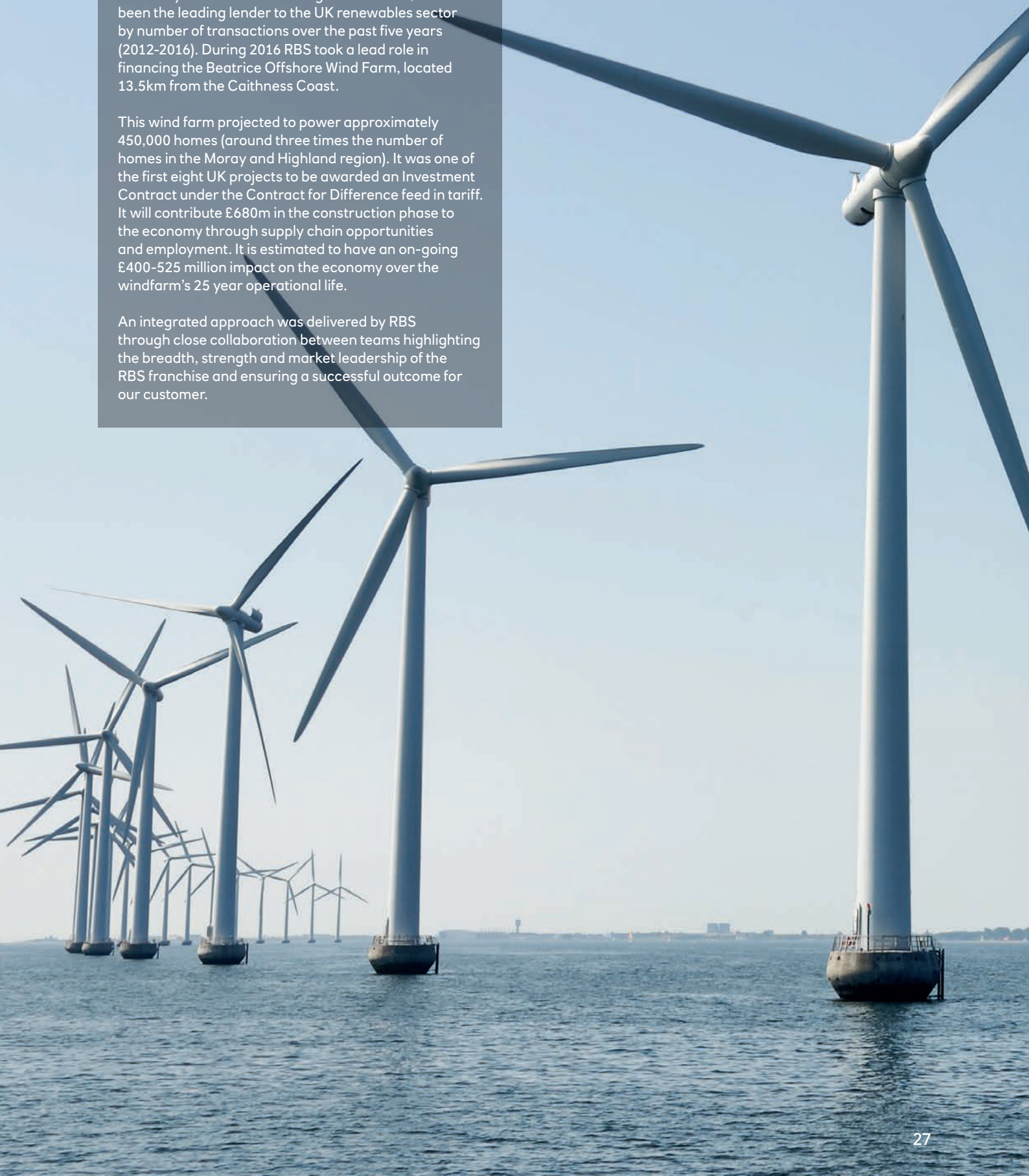
# Power to the people

We continue to play a key role in the transition to a low carbon economy by helping our customers to mitigate their emissions, save energy and reduce costs.

We have over 25 years experience in helping our customers to fund renewable energy and energy efficiency measures. According to InfraDeals, RBS has been the leading lender to the UK renewables sector by number of transactions over the past five years (2012-2016). During 2016 RBS took a lead role in financing the Beatrice Offshore Wind Farm, located 13.5km from the Caithness Coast.

This wind farm projected to power approximately 450,000 homes (around three times the number of homes in the Moray and Highland region). It was one of the first eight UK projects to be awarded an Investment Contract under the Contract for Difference feed in tariff. It will contribute £680m in the construction phase to the economy through supply chain opportunities and employment. It is estimated to have an on-going £400-525 million impact on the economy over the windfarm's 25 year operational life.

An integrated approach was delivered by RBS through close collaboration between teams highlighting the breadth, strength and market leadership of the RBS franchise and ensuring a successful outcome for our customer.



# Our Colleagues

Engaging our colleagues is critical to delivering on our strategy and ambition as a bank. Being better for our colleagues means we are better for our customers, and this makes us a better bank.

## Creating a Healthy Culture

Building a healthy culture that embodies Our Values is one of our core priorities. Our Values guide the way we identify the right people to serve our customers well, and how we manage, engage and reward our colleagues. Our Values are at the heart of both Our Standards, the bank-wide behavioural framework and Our Code, the bankwide Code of Conduct.

Our values are integral to the way we behave and do business and we continue to reinforce them in our systems, our policies and processes, our communications and our training and leadership role modelling.

We monitor our progress against our goals and gather feedback from our colleagues. Through metrics and key performance indicators we are able to assess our progress and respond accordingly. We measure our progress through internal reporting and report on progress quarterly. We participate in external benchmarking exercises and fully support the Banking Standards approach.

Our most recent survey, in which almost 63,000 colleagues took part, showed that we are changing the culture of RBS for the better. We remain above the Global Financial Services Norm for wellbeing, our inclusion scores continue to improve and there is a strong sense that managers act consistently with Our Values. However, the choices we've had to make as we move RBS forward have taken a toll on our colleagues. The scaling down of RBS and the impact of dealing with some difficult legacy issues have contributed to a decline in the improvements in engagement, pride and leadership that we saw in 2015.

We encourage colleagues to tell us what they think via the annual colleague

survey and our regular comments boards. When colleagues wish to report concerns relating to wrong doing or misconduct they can raise concerns via Speak Up, the bank's whistleblowing service. In 2016 213 cases were raised compared to 142 in 2015.

## Performance and Reward

Our approach to performance management provides clarity for our colleagues about how their contribution links to our ambition and all our colleagues have goals set across a balanced scorecard of measures. In 2016 we refreshed our behavioural framework to create one framework for all our colleagues (Our Standards).

We strive to pay the right wage to colleagues and continue to exceed the Living Wage Foundation Benchmarks. We have removed sales incentives for front line colleagues so they can concentrate on great customer service. For 2017, we have simplified how we pay our clerical colleagues, consolidating bonuses, making pay fairer and easier to understand.

More information on our remuneration policies can be found on pages 87 to 111 of the 2016 Annual Report and Accounts.

## Learning

We continue to embed 'Determined to lead' (Dtl), our core leadership programme across the bank. Dtl provides consistent tools to lead and engage our colleagues and is transforming the way we operate. In 2016 almost 16,000 leaders participated in the programme.

In October, we launched Service Excellence training, our new customer service programme. The first module introduces our Core Service Behaviours and provides an awareness of the tools and techniques that will help us

to deliver the best possible service, every time. Since October over 34,000 colleagues have completed this module.

We work closely with the Chartered Banker Institute (CBI) and Chartered Banker Professional Standards Board (CB:PSB) to professionalise our colleagues. In 2016 we achieved an Excel rating in the CB:PSB Foundation Standard review, one of only two CB:PSB member firms to have secured 'Earned Autonomy'.

We also offer a wide range of learning opportunities which can be mandatory, role specific or related to personal development. Our mandatory learning is focused on keeping our customers, our colleagues and the bank safe.

## Health and Wellbeing

Wellbeing is a fundamental part of creating a great place to work. We offer a wide range of wellbeing initiatives and benefits to help maintain physical and mental health and support our colleagues if they become unwell.

In 2016, we focused on physical, mental health and social wellbeing. More than 50,000 colleagues took part in the Global Corporate Challenge (GCC), helping us to win the GCC World Most Active Organisation Gold Award.

To support our colleagues through change we continue to promote our Employee Assistance Programme, where we have continued to see a high utilisation rate. We have supported Time to Change (the UK's biggest programme to challenge mental health stigma) since 2014 and launched a number of mindfulness support tools this year.





Platinum ranking  
from Opportunity  
Now (gender)



Gold ranking  
for Race for  
Opportunity (race)



Times Top 50  
Employers for  
Women



Top Ten Global  
Employer in  
Stonewall's Global  
Equality Index  
(LGBT)



Silver Status from  
the Business  
Disability Forum



Top 10 Employer  
by Working  
Families.

### Inclusion

Building a more inclusive RBS is essential for our customers and colleagues. Our inclusion policy applies to all our colleagues globally to make sure everyone feels included and valued, regardless of their background.

- ▶ As at 31 December 2016, our permanent headcount was 79,099. 48% were male and 52% female.
- ▶ We continue to work towards our goal of having at least 30% senior women in our top three leadership layers across each business by 2020 and to be fully gender balanced by 2030. We have a positive action approach in place, tailored by business, according to the specific challenges they face.
- ▶ During 2016, we continued to roll out unconscious bias learning to all our colleagues to create a solid platform for the wider inclusion agenda. Almost 30,000 colleagues participated in unconscious bias training in 2016.
- ▶ Our disability plan will support us becoming a disability smart organisation by 2018. It addresses areas for improvement including branch access, accessible services, improving colleague adjustment processes and inserting disability checkpoints into our key processes and practices.
- ▶ We continue to focus on building an ethnically diverse RBS. Our plan focuses on positive action and includes reciprocal mentoring, targeted development workshops and leadership programmes and ensuring we have a Black, Asian and Minority Ethnic (BAME) focus on recruitment, talent identification and promotion.
- ▶ Our LGBT agenda continues to deliver a better experience for our LGBT colleagues and customers. We have processes in place to support updating gender and title on customers' banking records and to support colleagues undergoing gender transition. And, we continue to support our 16,000-strong colleague networks.

Historically we have reported by grade, which has enabled us to track trend year on year, however as the structure of our business has changed, we have evolved our approach to reflect our organisational (CEO) levels. This method more accurately describes our gender balance at leadership/pipeline levels and is reflective of how work gets done across the bank.

Grade	#Women	#Men	%Women
CEO – 1	3	10	23
CEO – 2	33	73	31
CEO – 3	232	443	34
CEO – 4	1512	1891	44
Target population (CEO – 3 and above)	268	526	34

	Male	Female
Executive Employees	113 (78%)	32 (22%)
Directors of Subsidiaries	481 (84%)	90 (16%)

There were 716 senior managers (in accordance with the definition contained within the relevant Companies Act legislation), which comprises our executive population and individuals who are directors of our subsidiaries. The RBS Board of directors has twelve members, consisting of nine male and three female directors.

# Our Customers

RBS remains committed to achieving its target of being the number one bank for customer service, trust and advocacy by 2020.

We use independent surveys to measure our customers' experience and track our progress against our goal in each of our markets.

## Net Promoter Score (NPS)

Customers are asked how likely they would be to recommend their bank to a friend or colleague, and respond based on a 0-10 scale with 10 indicating 'extremely likely' and 0 indicating 'not at all likely'. Customers scoring 0 to 6 are termed

detractors and customers scoring 9 to 10 are termed promoters. NPS is established by subtracting the proportion of detractors from the proportion of promoters.

The table below lists all of the businesses for which we have an NPS for 2016. Year-on-year, NatWest Personal and Commercial Banking have improved, along with Ulster Bank Business and Commercial in Northern Ireland and Ulster Bank Business Direct in the Republic of

Ireland. In Great Britain, we have also narrowed the gap to number one in Commercial Banking. We do, however, acknowledge that there is still work to do, with four brands missing their year end targets.

In recent years, RBS has launched a number of initiatives to make it simpler, fairer and easier for customers to do business with the bank.

		Q4 2015	Q3 2016	Q4 2016	Year end 2016 target
Personal Banking	NatWest (England & Wales) <sup>(1)</sup>	9	11	13	15
	Royal Bank of Scotland (Scotland) <sup>(1)</sup>	-9	-2	-4	-5
	Ulster Bank (Northern Ireland) <sup>(2)</sup>	-9	-16	-16	-3
	Ulster Bank (Republic of Ireland) <sup>(2)</sup>	-14	-8	-7	-10
Business Banking	NatWest (England & Wales) <sup>(3)</sup>	9	4	-2	13
	Royal Bank of Scotland (Scotland) <sup>(3)</sup>	-7	-4	-5	2
Business Direct	Ulster Bank (Republic of Ireland) <sup>(5)</sup>	-21	n/a	-2	-15
Business & Commercial	Ulster Bank (Northern Ireland) <sup>(4)</sup>	-19	0	0	-4
Commercial Banking <sup>(6)</sup>		9	21	20	17

## Customer Trust

We also use independent experts to measure our customers' trust in the bank. Each quarter we ask customers to what extent they trust or distrust their bank to do the right thing. The score is a net measure of those customers that trust

their bank (a lot or somewhat) minus those that distrust their bank (a lot or somewhat).

Customer trust in NatWest in England & Wales has exceeded its 2016 target, improving from 48% at Q4 2015 to 55%

at Q4 2016. Trust in RBS in Scotland has fallen year on year (from 14% in Q4 2015 to 13% in Q4 2016) and has fallen behind its target for 2016. This is primarily due to ongoing reputational and legacy issues that the bank continues to work to resolve.

		Q4 2015	Q3 2016	Q4 2016	Year end 2016 target
Customer trust <sup>(7)</sup>	NatWest (England & Wales)	48%	48%	55%	51%
	Royal Bank of Scotland (Scotland)	14%	13%	13%	26%

Notes:

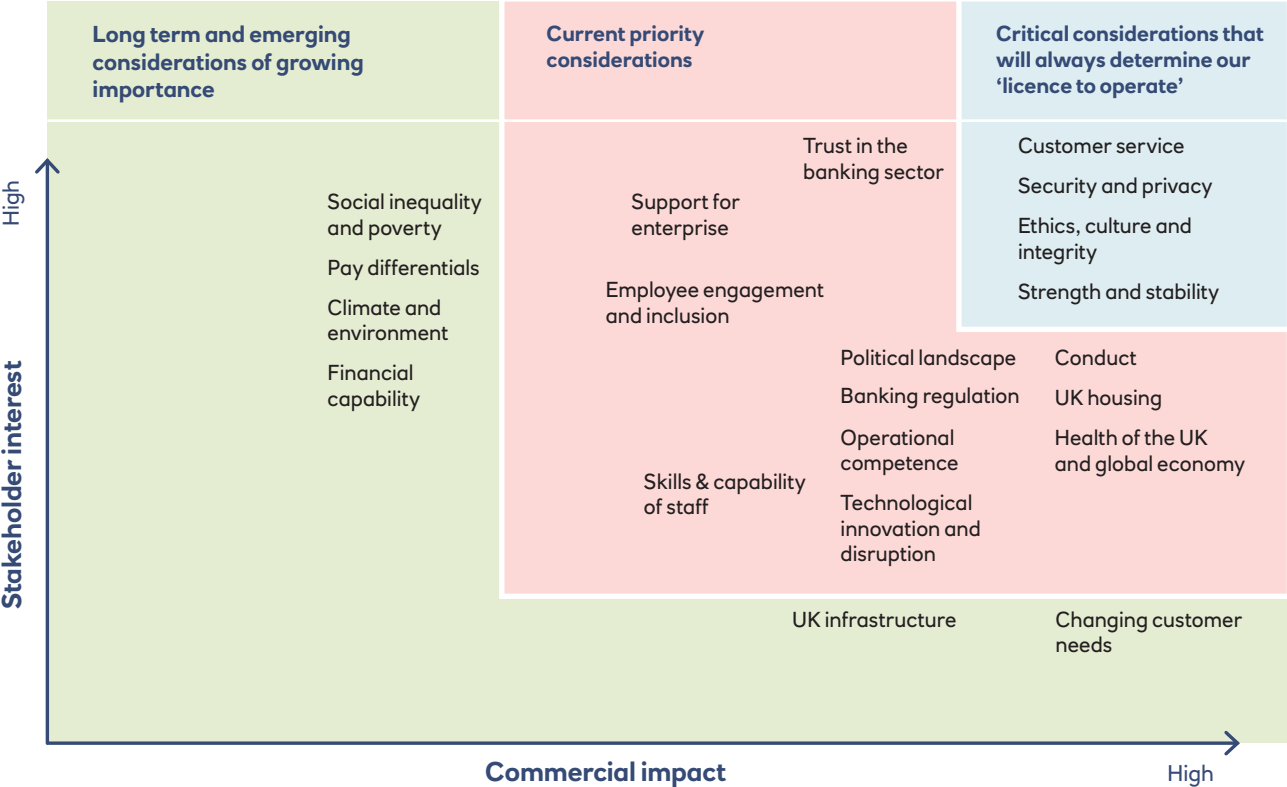
- (1) Source: GfK FRS 6 month rolling data. Latest base sizes: NatWest (England & Wales) (3313) Royal Bank of Scotland (Scotland) (527). Based on the question: "How likely is it that you would recommend (brand) to a relative, friend or colleague in the next 12 months for current account banking?"
- (2) Source: Coyne Research 12 month rolling data. Latest base sizes: Ulster Bank NI (375) Ulster Bank Rol (322) Question: "Please indicate to what extent you would be likely to recommend (brand) to your friends or family using a scale of 0 to 10 where 0 is not at all likely and 10 is extremely likely".
- (3) Source: Charterhouse Research Business Banking Survey (GB), based on interviews with businesses with an annual turnover up to £2 million. Quarterly rolling data. Latest base sizes: NatWest England & Wales (1258), RBS Scotland (422). Weighted by region and turnover to be representative of businesses in England & Wales/Scotland, 4 quarter rolling data.
- (4) Source: Charterhouse Research Business Banking Survey (NI), based on interviews with businesses with an annual turnover up to £1 billion. Latest base size: Ulster (399) Weighted by turnover and industry sector to be representative of businesses in Northern Ireland, 4 quarter rolling data.
- (5) Source: PWC ROI Business Banking Tracker 2016 (annual study only). Latest sample size: Ulster Bank (218) In 2017 we will be switching the source of advocacy measurement for Ulster Bank Business in Rol to Red C. Red C is a recognised research agency that will provide more frequent reporting of NPS, as well as additional diagnostic customer feedback to help us improve the customer experience.
- (6) Source: Charterhouse Research Business Banking Survey (GB), based on interviews with businesses with annual turnover between £2 million and £1 billion. Latest base size: RBSG Great Britain (935). Weighted by region and turnover to be representative of businesses in Great Britain, 4 quarter rolling data.
- (7) Source: Populus. Latest quarter's data. Measured as a net of those that trust RBS/NatWest to do the right thing, less those that do not. Latest base sizes: NatWest, England & Wales (871), RBS Scotland (226).

# Our operating environment

## Key influences in our operating environment

Our ability to serve customers and create value for the long term is heavily influenced by the environment in which we operate. We have assessed the importance of these influences both in terms of their relevance to our stakeholders (including customers, investors, UK government, employees and civil society) and their potential

commercial impact on us. We have categorised them accordingly, shown in the diagram below. This provides additional context for our performance and future strategy. Each influence is briefly described on the following pages, with links provided to the relevant parts of the Strategic Report for more detail.





## Influences explained and where to find out more.

### Key



CEO review



Business model



Sustainability pages on rbs.com



Risk overview



Economic indicators



Strategic report

### Customer service

Delivering excellent customer service is essential for the banking sector to build trust. Maintaining and growing a loyal and satisfied customer base requires an appropriate digital and physical presence and clear distribution strategy.



PBB, CPB & NWM review sections



### Security and privacy

Public understanding of companies' use of personal information is low and many do not trust companies to handle data responsibly. At the same time, protecting data from cyber and malicious attacks is also a vital part of providing a safe and secure banking service.



PBB review section



### Strength and stability

Banks need to demonstrate their ability to survive financial stress arising from economic turmoil, and potential large scale fines and legal cases resulting from historic events. They must also demonstrate they have sufficient capital, liquidity and resilience as well as the ability to generate sufficient returns.



### Ethics, culture and integrity

Professional integrity is a key governance consideration in the banking sector. Services provided must satisfy the highest professional standards, avoid conflicts of interest, bias, or negligence, and ensure that all stakeholders, including employees, contractors and business partners, are treated fairly and respectfully.



Our Approach review section



### UK housing

Demand for housing in some parts of the UK outstrips supply, reducing affordability and harming family disposable incomes. Quality of housing stock is also below standard in some areas. Mortgage providers play a key role in the housing market.



PBB review Section



### Technological innovation and disruption

The banking sector is changing rapidly, with the creation of new technologies, new market entrants and high potential for disruption. There is also a broad regulatory plan to deliver an "Open Banking" environment which will help to improve customers' overall banking experience. This, along with the ever increasing reliance of technology, will present a risk to traditional banking business models and impact society.



PBB & CPB review sections



### Banking regulation

Banks operate in an environment where regulatory change is frequent and increasingly complex.



### Skills and capabilities of staff

Financial services companies face competition for skilled employees, in particular with specific skillsets (e.g. IT). As the industry transforms to more digital banking, the need for such skills may become more acute.



Our Colleagues section



### Employee engagement and inclusion

Employee engagement and satisfaction is highly correlated with overall performance. A key part of this is the inclusion agenda and the need to foster corporate cultures that value diversity, teamwork, quality leadership and training.



### Operational competence

Banks need to proactively identify and manage risks and efficiencies in their operations and facilities. Delivering appropriate digital infrastructure is important to ensure a 'technically-able' bank that supports its long-term future. Providing this requires investment and resources, at a time when banks must stay cost-competitive, and manage potential future pensions liabilities.



### Conduct

Banks remain focused on putting in place measures to prevent conduct failings. At the same time, historic conduct failings, such as RMBS, continue to have major financial and reputational impacts.



### Health of the UK and global economy

UK and global economic prospects are clouded by elevated uncertainty and lower for longer interest rates. This also impacts other risks including the scale of UK pensions liabilities. Banks have to cope with a historically low interest rate and higher event risk environment, with knock-on impacts to profitability and operations.



### Political landscape

The political landscape has seen major events such as the EU and Scottish referenda. These may produce uncertainty and knock-on effects to economic confidence and the regulatory environment.



### Trust in the banking sector

Trust in traditional large UK banks often lags behind smaller competitors and new market entrants. Rebuilding trust remains a key challenge.



### Support for enterprise

A healthy economy needs a pipeline of new and growing businesses to spur innovation and growth. 'Entrepreneurs, start-ups and small businesses require particular support in terms of financing and building market share.



### UK infrastructure

The UK has a significant need for new infrastructure, such as energy, transport and communications systems. Finance is one of the requirements for providing this, meaning banks have a key role.



### Social inequality and poverty

Poverty and inequality are associated with many societal problems and can contribute to challenges in accessing financial products and services, resulting in reduced Financial Inclusion.



### Pay differentials

Shareholders, employees and the general public have shown increasing concerns about the inequality in pay in large companies between senior executives and the general workforce.



### Changing customer needs

Customer needs are changing and different types of customer often have significantly different banking needs. In order to be attractive and useful, financial products and services need to fit in with customers' lives and be flexible to differing levels of digital and financial understanding.



### Climate and environment

The transition to a low carbon and resource-efficient future is underway, affecting almost every sector of the economy. Local environmental considerations such as air quality, flooding and natural habitats also remain a major concern. The Paris Agreement provides a framework by which the world will seek to prevent dangerous climate change but further challenges remain.



### Financial capability

Enabling customers to manage money well day to day and plan for the future, increases their resilience, and their ability to manage the financial impact of major life events. This in turn helps customers avoid falling into financial difficulty and can improve their well being.



## Our direct environmental footprint

RBS is committed to reducing the environmental impact of serving our customers. We outperformed our 2020 targets of 20% carbon, 5% water and 50% paper reduction during 2016 and we will increase our ambition in these areas during 2017. Our decrease in total carbon emissions is largely attributable to a 15% per full time equivalents reduction in energy consumption since 2014. We are containing growth in Data Centre energy consumption through legacy IT decommissions and energy reduction initiatives. The rationalisation of property space and investment in building management systems in 384 branches and 17 offices are examples of a number of projects delivering energy reductions. We buy renewable electricity in the UK, reflected in our market-based CO<sub>2</sub>e emissions figure. Scope 3 business travel emissions are being driven down by a reduction in long haul flights, a focus on associated cost and improved virtual collaboration tools.

In 2016 we diverted 96% of waste from landfill in the UK, 70% globally. An increase in waste volume compared with 2015 is partly attributed to the destruction of outdated paper records which are recycled along with all paper waste. Removing paper hand towels from 800 branches and 22 offices has helped keep waste volume down. Sending food waste to anaerobic digestion and coffee waste for bio-fuel improves our recycling rate. Paper usage is linked to use of digital channels with approximately 55% of personal and business banking customers receiving online statements and a reduction in internal print of 20% in 2016.

We collaborate with colleagues and suppliers to improve performance in all areas. Our Innovation Gateway crowdsourcing community is a partnership with corporates and universities, now sourcing new solutions from 1,300 SMEs. We've tested 34 of these new products in our facilities since 2014 with notable success in reducing water usage. We engage colleagues via bank wide 'Determined to Make a Difference' campaigns. In 2016, 1,200 colleagues logged over 2500 activities to reduce our environmental impact, via our green reward app JUMP.

### Carbon emissions disclosure

#### Assessment Parameters

Baseline year for total reported CO <sub>2</sub> e emissions (tonnes) (Scope 1*, 2** and 3****)	2014
Consolidation approach	Operational control
Boundary summary	All entities and facilities either owned or under operational control
Emission factor data source	DEFRA (2016), eGRID (2015)
Assessment methodology	The Greenhouse Gas Protocol revised edition (2004)
Materiality threshold	Materiality was set at group level at 5%
Intensity ratio	Emissions per full time employee (FTE)
Independent assurance	Limited assurance provided by Ernst & Young LLP over total reported CO <sub>2</sub> e emissions (tonnes) (Scope 1*, 2** and 3**** location based emissions)

GHG Emissions	2011	2014	2015	2016	Change 2011 to 2016 (%)	Change 2014 to 2016 (%)
Location-based CO <sub>2</sub> e emissions (Scope 1, 2 and Business Travel) (tonnes)	626,851	530,467	464,107	396,133	-37%	-25%
Scope 1 CO <sub>2</sub> e emissions (tonnes)	43,361	35,433	34,175	29,408	-32%	-17%
Scope 2 Market-based CO <sub>2</sub> e emissions (tonnes) *****	512,958	418,918	377,779	165,553	-68%	-60%
Scope 2 Location-based CO <sub>2</sub> e emissions (tonnes)	442,510	388,918	333,676	275,319	-38%	-29%
Scope 1 & Scope 2 Location-based CO <sub>2</sub> e emissions per FTE (tonnes)	4.91	4.33	4.01	3.38	-31%	-22%
Scope 3 CO <sub>2</sub> e Emissions from business travel (tonnes) ****	140,97	106,117	96,256	91,406	-35%	-14%
Energy Consumption (GWh)	1,150	968	863	754	-34%	-22%
Water consumption (m <sup>3</sup> )	1,613,416	1,365,545	1,349,488	1,292,019	-20%	-5%
Paper used (tonnes)	23,581	12,044	11,049	9,965	-58%	-17%
Waste generated (tonnes)	32,066	22,798	17,643	21,850	-32%	-4%
Percentage of waste recycled	70%	69%	66%	70%	0%	2%

#### Notes:

\*Scope 1: Emissions from fluorinated gas loss and fuel combustion in RBS premises/vehicles. \*\*Scope 2: Emissions from electricity, district heating and district cooling used in RBS premises. \*\*\*Scope 3: Emissions associated with business travel (air, rail and road) by RBS employees. \*\*\*\* Scope 3 emissions have been restated and rebaselined to include Taxis in India. \*\*\*\*\* market-based emissions have been calculated using the GHG Protocol guidelines. RBS has purchased renewable electricity that meets the Good Quality Criteria since March 2016. Paper and business travel targets have a baseline year of 2011.

## Our approach to human rights and modern slavery

RBS takes a proactive approach to upholding our commitment to respect human rights. This includes regular review of our policies and procedures. Our approach is centred on identifying and mitigating potential human rights risks across our business and our sphere of influence.

A main focus during 2016 has been to meet our new obligations under the Modern Slavery Act 2015 (MSA), which aims to protect victims, bring perpetrators to justice and provide more effective tools for law enforcement. We welcome the MSA and its aim to eradicate forced labour and human trafficking.

In accordance with the requirements of the MSA, our first annual statement will be published and available on our website in Spring 2017. Ahead of this we published an interim statement in December 2016 setting out our approach and seeking the input of external stakeholders.

We are taking a human rights approach to understand the impacts of our operations and supply chain. We are also working to ensure our employees, suppliers and customers are aware of the risks and are able to address any issues when they arise.

These steps include: reviewing and updating our policy commitments; raising awareness among employees; targeted training to relevant employees, such as supply chain managers and relationship managers; incorporating requirements under the MSA into our supplier sourcing process; and embedding MSA commitments within our Environment, Social and Ethical (ESE) Risk Policy and processes. Modern slavery, forced labour and harmful child labour are prohibited within our reputational and ESE risk framework, and our Sustainable Procurement Code.

RBS's international human rights' commitments are set out in our Human Rights Position Statement. Our approach is underpinned by our values and standards. For employees this is via the RBS Code of Conduct – 'Our Code' which was updated in 2016. Our Code includes a clear commitment to respect human rights, and the Yes Check, a tool to guide good decision-making. Employees are consulted on key aspects of their working environment, and they can utilise a confidential helpline to discuss any matters of concern. We are an accredited Living Wage employer, and the process of extending the Living Wage to our suppliers continued through 2016.

For suppliers, our Sustainable Procurement Code sets out the international human rights commitments we expect of the companies that we work with, including labour standards and non-discrimination.

Our ESE Risk Policy applies to our customers, and is kept under review. Alongside our sector specific risk appetite positions we have outlined ESE risk concerns for customers operating outside of these sectors. Our policy identifies human rights risks and due diligence is carried out on clients when human rights risks are identified. We expect our customers to share our commitment to respecting human rights within their operations.

Our commitment to the international progress of human rights includes being a signatory of the United Nations Global Compact since 2003, and we reaffirm our commitment to the ten principles of the Global Compact. We are committed to the implementation of the UN Guiding Principles on Business and Human Rights and participate with our peers in initiatives such as the Thun Group and United Nations Environment Programme Finance Initiative, to understand how these can best be applied. We have adopted the Equator Principles, since their inception in 2003, to manage social and environmental risks, including human rights, in project-related transactions.

## Independent assurance

The Royal Bank of Scotland Group plc appointed Ernst & Young LLP to provide limited independent assurance over selected sustainability content within the Strategic Report ("the Report"), as at and for the period ended 31 December 2016. The assurance engagement was planned and performed in accordance with the International Standard for Assurance Engagements (ISAE) 3000 Revised, Assurance Engagements Other Than Audits or Reviews of Historical Financial Information.

These procedures were designed to conclude on:

- ▶ The consistency of selected narrative claims on sustainability with underlying performance information, and;
- ▶ The accuracy and completeness of the sustainability performance indicators listed below:
  - Value (£) of attempted fraud prevented in UK
  - Number of cases raised via Speak Up, the bank's whistleblowing service
  - Total gender balance in top 3 senior layers
  - Customer Trust score
  - % personal customers who are digitally active
  - Total scope 1 and 2 location based CO<sub>2</sub>e emissions and Scope 3 emissions from business travel
  - Number of Foundation accounts opened
  - Lending to small and medium sized enterprises (SMEs) across England, Scotland and Wales

An unqualified opinion was issued and is available on [rbs.com](http://rbs.com), along with further details of the scope, respective responsibilities, work performed, limitations and conclusions.

# Key economic indicators

The UK economy grew by 2.1% in 2016, down from 2.2% in 2015 and close to its long-run average.

In a healthy job market, the number of people in work increased by 350,000 and unemployment fell below 5% for the first time since 2005. With inflation of 1.6%, wage growth of 2.8% provided a modest boost to consumers' spending power. Business profitability remained strong and business investment fell by around 2%. House price inflation moderated, but at 5% remained high.

## Summary

The main development in 2016 was the fall in the value of sterling, which finished the year down 15%, 10% of that happening after the EU referendum. That quickly fed through to higher import costs, with producers' input prices rising by 16%, squeezing firms' margins. The Bank of England expects consumer price inflation to reach around 2.75% in 2017 and 2018, above the target set by Parliament. However, the Bank of England has not raised interest rates to moderate inflation. Rather, in August it cut Bank Rate to 0.25%. That reflected its concern that leaving the European Union would lead growth to slow and inflation to undershoot the target. In addition, the Bank of England tends to disregard inflation caused by a currency change unless it feeds through to wages.

The Republic of Ireland continued to grow at around 4%, with domestic demand contributing more, and exports less to growth than in recent years. Unemployment continued to fall, ending

the year at 7.2%. House price inflation accelerated to 9% from 4.6% in 2015.

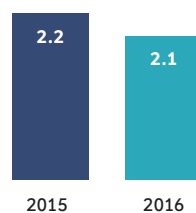
Eurozone area growth slowed slightly to 1.7% from 1.8%. Unemployment remained close to 10%. With inflation still close to zero, the European Central Bank reduced interest rates and expanded its quantitative easing programme.

Reflecting continued modest growth 1.6%, rising employment two million, and falling unemployment 4.7%, the US Federal Reserve raised the target range for its main interest rate by 0.25% to 0.5-0.75% in December.

While the year opened with considerable market volatility, which reflected concerns about the outlook for China, growth there was 6.7%, reflecting actions by the authorities to boost activity. That had beneficial spillover effects among some of China's trading partners.

Despite continued growth and low unemployment in the UK, markets continue to expect interest rates to remain low. At the year's end, the first rise in Bank Rate was expected around mid-2019. While that partly reflects the Bank of England's response to the EU referendum result, more important are structural factors; slower global growth, higher levels of desired saving and lower levels of desired investment, which have been pushing down real interest rates for some time and which are likely to persist.

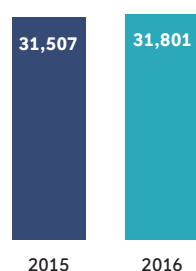
UK gross domestic product growth (%)



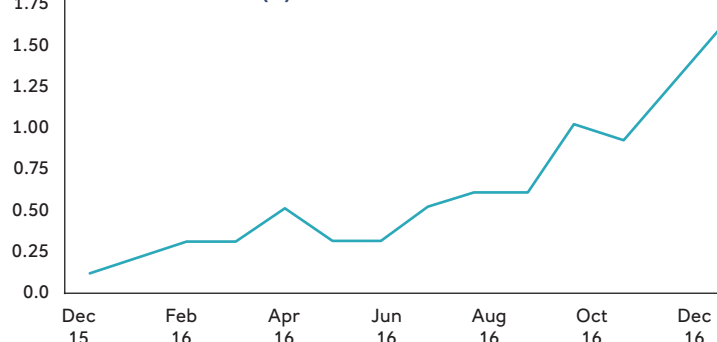
Unemployment rate, UK (%)



Number of people in employment, UK (thousands)



Consumer prices inflation 12-month rate (%)



Source: Office for National Statistics

# Risk overview

## Effective risk management plays a central role in the successful development and execution of our strategy.

Our Risk appetite is set in line with the overall strategy and approved by the board while the risk management framework identifies and manages current and emerging risks that could materially affect the delivery of the RBS strategy.

### Progress in 2016

RBS has continued to make progress against its strategic objectives of reducing risk and strengthening both the balance sheet and the capital position. Against a backdrop of uncertainty in the wider political and economic environment, risk management played a key role in positioning RBS to prepare for, and respond to developments.

In particular, there has been a focus on enhancing our risk appetite framework and communicating and embedding it across the bank. For each of our material risks, significant emphasis has been placed on reviewing current measures along with associated limits and triggers and also the way our risk profile compared to risk appetite is reported across RBS. Risk culture has continued to be at the forefront of our work as RBS moves towards the achievement of its strategic objectives. To that end, the ambition is to make risk management simply part of the way colleagues across RBS work and think. In support of this, during 2016 the RBS-wide action plan focused on assessment, identifying and taking actions to build clarity, develop capability and motivate staff.

Similarly, activity has been underway to enhance our operational risk management framework to help ensure our businesses maintain a safe and secure environment for our customers. As part of this, during 2016 there was a focus on risk and control assessment, particularly relating to our most material products, processes and services. In addition, there continued to be an emphasis on understanding and managing the risks relating to RBS's transformation agenda.

In market risk, sustained effort has been necessary to anticipate and respond to major developments in the wider environment. Managing this has required close collaboration between our first and second lines of defence but, in turn, has demonstrated RBS's continued commitment to its wholesale banking proposition.

RWAs continued to decline (6%), ending the year at £228 billion (from £243 billion in 2015). The decline was driven by continued run down in Capital Resolution, where RWAs fell by £14.5 billion during the year, offset in part by an increase in RWAs in the core franchises.

The Common Equity Tier 1 (CET1) ratio decreased by 210 basis points to 13.4% in 2016, reflecting lower CET1 capital partially offset by a reduction in RWAs. Litigation and conduct charges of £5.9 billion in 2016 contributed to a significant reduction in the CET1 capital. Management actions to normalise the ownership structure and improve the long-term resilience of RBS also contributed to the reduction. These actions included the final Dividend Access Share payment of £1.2 billion and the impact of the accelerated pension payment of £4.2 billion. Tier 1 capital benefitted from the successful issuance of £2 billion of Additional Tier 1 (AT1) capital notes.

The leverage ratio fell by 50bps to 5.1% during 2016. This reflected the fall in the CET1 position, partly offset by the successful issuance of an additional £2 billion equivalent of AT1 instruments as planned at the beginning of the year. The Bank of England leverage ratio benefitted from an additional 50bps uplift following the FPC's guidance on 4 August that allowed banks, under certain conditions, to exclude central bank reserves from the leverage exposure measure.

RBS also issued £4.2 billion of MREL-eligible senior debt as part of the issuance plan to meet its steady-state bail-in requirements by 2022.

In the Bank of England 2016 stress test, RBS did not meet its common equity Tier 1 (CET1) capital or Tier 1 leverage hurdle rates before additional Tier 1 (AT1) conversion under the hypothetical adverse scenario. After AT1 conversion, it did not meet its CET1 systemic reference point or Tier 1 leverage ratio hurdle rate. Based on RBS's own assessment of its resilience identified during the stress-testing process, RBS has already updated its capital plan to incorporate further capital strengthening actions and this revised plan has been accepted by the PRA Board. The PRA will continue to monitor RBS's progress against its revised capital plan.

RBS maintained a robust liquidity and funding risk profile in 2016. Its loan-to-deposit-ratio was 91% at 31 December 2016, compared with 89% in 2015. The latest Internal Liquidity Adequacy Assessment Process (ILAAP) showed that RBS is in a strong position to withstand liquidity stress scenarios. It suggested that RBS's liquidity portfolio was large enough to cover more than 139% of the expected outflows in the worst of three severe scenarios.

Litigation and conduct costs of £5,868 million included a £3,107 million provision in relation to various investigations and litigation matters relating to RBS's issuance and underwriting of residential mortgage-backed securities (RMBS), an additional charge in respect of the settlement with the National Credit Union Administration Board to resolve two outstanding RMBS lawsuits, a provision in respect of the UK 2008 rights issue shareholder litigation, additional PPI provisions, a provision in respect of the FCA review of RBS's treatment of SMEs and a charge in Ulster Bank Rol in respect of an industry-wide examination of tracker mortgages.



### Top and emerging risks

RBS employs a continuous process for identifying and managing its top and emerging risks. These are defined as scenarios that could have a significant negative impact on RBS's ability to operate or meet its strategic objectives. A number of scenarios attracted particular attention in 2016.

### Macro-economic and political risks:

RBS remains vulnerable to changes and uncertainty in the external economic and political environment, which have intensified in the past year. To mitigate these risks, RBS has taken actions in 2016 with its capital, liquidity and leverage positions. A number of higher-risk portfolios have been exited or reduced. Stress testing and scenario planning is used extensively to inform strategic planning and risk mitigation relating to a range of macro-economic and political risks. Scenarios identified as having a potentially material negative impact on RBS include: the impact of the UK's exit from the EU; a second Scottish independence referendum; a UK recession including significant falls in house prices; global financial market volatility linked to advanced economy interest rate increases or decreases; a protracted period of low interest rates in the UK; vulnerabilities in emerging market economies resulting in contagion in RBS's core markets; a eurozone crisis; and major geopolitical instability.

### Risks related to the competitive environment:

RBS's target markets are highly competitive, which poses challenges in terms of achieving some strategic objectives. Moreover, changes in technology, customer behaviour and business models in these markets have accelerated. RBS monitors the competitive environment and associated technological and customer developments as part of its strategy development and makes adjustments as appropriate.

### An increase in obligations to support pension schemes:

If economic growth stagnates and interest rates continue to remain low, the value of pension scheme assets may not be adequate to fund pension scheme liabilities. The actuarial deficit in RBS pension schemes – as determined by the most recent triennial valuations – has increased, requiring

RBS to increase its current and future cash contributions to the schemes. An acceleration of certain previously-committed pension contributions was made in Q1 2016 to reduce this risk. Depending on the economic and monetary conditions and longevity of scheme members prevailing at that time, the actuarial deficit may increase at subsequent valuations and is expected to be affected by ring-fencing.

### Regulatory and legal risks

#### The impacts of past business conduct:

Future litigation and conduct charges could be substantial. RBS is involved in a number of investigations, including: ongoing class action litigation, securitisation and mortgage-backed securities related litigation, investigations into foreign exchange trading and rate-setting activities, continuing LIBOR-related litigation and investigations into the treatment of small and medium-sized business customers in financial difficulty, anti-money laundering, sanctions, mis-selling (including mis-selling of payment protection insurance products). Settlements may result in additional financial penalties, non-monetary penalties or other consequences, which may be material.

More detail on these issues can be found in the Litigation, Investigations and Reviews and Risk Factors sections of the 2016 Annual Report and Accounts. To prevent future conduct from resulting in similar impacts, RBS continues to embed a strong and comprehensive risk and compliance culture.

### Risks to income, costs and business models arising from regulatory requirements:

RBS is exposed to the risk of further increases in regulatory capital requirements as well as risks related to new regulations that could affect its business models, such as Open Banking. RBS considers and incorporates the implications of proposed or potential regulatory activities in its strategic and financial plans.

### Operational and execution risks

#### Increased losses arising from a failure to execute major projects successfully:

The successful execution of major projects, including the transformation

plan, the restructuring of NatWest Markets, meeting the final European Commission State Aid requirements relating to Williams & Glyn compliance with structural reform requirements including the statutory ring-fencing requirements implemented as a result of the Independent Commission on Banking; delivering a robust control environment and the embedding of a strong and pervasive, customer centred organisational and risk culture, are essential to meet RBS's strategic objectives. These projects cover organisational structure, business strategy, information technology systems, operational processes and product offerings. RBS is working to implement change in line with its project plans while assessing the risks to implementation and is taking steps to mitigate those risks where possible.

### Impact of cyber attacks:

Cyber attacks are increasing in frequency and severity across the industry. RBS has participated in industry-wide cyber attack simulations in order to help test and develop defence planning. To mitigate the risks, a large scale programme to continue to improve controls, enhance protections and educate staff on the threat is underway.

### Inability to recruit or retain suitable staff:

There is a risk that RBS lacks sufficient capability or capacity at a senior level to deliver – or to adapt to – change. RBS monitors people risk closely and has plans in place to support retention of key roles, with wider programmes supporting engagement and training for all staff.

### Failure of information technology systems:

RBS's information technology systems may be subject to failure. As such systems are complex, recovering from failure is challenging. To mitigate these risks, a major investment programme has significantly improved the resilience of the systems and further progress is expected. Back-up system sustainability has improved, and a 'mirror bank' system, to provide basic services, if needed, has been created.



Full risk factors are discussed on pages 432 to 463 of the 2016 Annual Report and Accounts.



## Making sense of money

MoneySense is our flagship financial education programme for young people aged between 5 and 18. It aims to help young people towards a better financial future. Since we started providing financial education in schools over 22 years ago, we've helped an estimated 4.5 million young people understand all about money. By the end of 2018, we'll have helped a further one million young people.

Our programme is used to deliver lessons in primary and secondary schools in the UK and Ireland, thanks to the support of registered teachers and our dedicated volunteer network of over 2,800 employees.

We're proud of the work MoneySense does in our communities. By helping young people understand things like budgeting, saving and online security we're supporting them to become financially independent and confident money managers.



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# Business review

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RBS is structured around becoming number one for service, trust and advocacy as we meet the ambitions and needs of our retail, business, commercial and corporate customers. Organised under three customer-facing franchises, our core businesses are centred around the UK and Ireland markets with a focused international capability.



**Les Matheson**  
CEO, Personal &  
Business Banking

## Personal & Business Banking

Personal & Business Banking (PBB) serves individual and mass affluent customers together with small businesses (generally up to £2 million turnover). Our principal brands are NatWest in England and Wales, Royal Bank of Scotland in Scotland, and Ulster Bank Rol in the Republic of Ireland. The operations of Ulster Bank in Northern Ireland have been combined with the main UK businesses.

### Performance overview

- ▶ PBB recorded an operating profit of £1,401 million in 2016 compared with £1,292 million in 2015. Adjusted operating profit of £2,431 was in line with 2015 as a reduction in net impairment releases was offset by higher income associated with volume growth.
- ▶ Total income increased by £116 million, or 2%, to £5,866 million compared with 2015 as the benefit of asset volume growth has more than offset margin compression. Net interest margin declined by 13 basis points to 2.80% reflecting the impact of the overall portfolio mix being increasingly weighted towards secured lending and mortgage customers switching from standard variable rate (SVR) to lower rate products.
- ▶ Net loans and advances of £151.0 billion were £14.5 billion, or 11%, higher than in 2015 principally reflecting mortgage growth.
- ▶ Adjusted operating expenses of £3,462 million were in line with 2015.
- ▶ Credit conditions remained benign, with a net impairment release of £30 million in 2016 compared with £148 million in 2015.

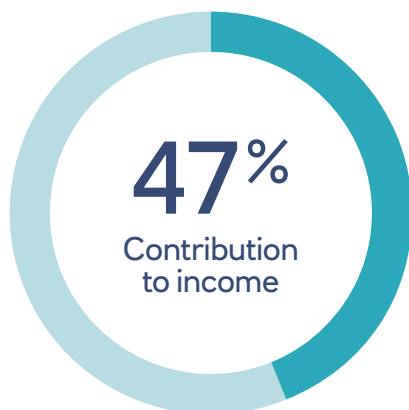


## Upwardly mobile

Whether it's logging in with your fingerprint, paying your contacts through your phone, cancelling a direct debit or amending standing orders, we've been working hard to make our apps even more convenient for customers, by making them easier to use and giving them increased functionality. In fact, over a third of all personal product sales are now completed digitally.

We're investing in our apps because increasing numbers of our customers want to be able to do their banking on the move. 4.2 million customers in the UK now use our apps.





## Performance highlights

	2016	2015
Return on equity (%)	11.6	11.4
Net interest margin (%)	2.80	2.93
Cost:income ratio (%)	77	80
Net loans and advances to customers (£bn)	151.0	136.5
Customer deposits (£bn)	161.9	150.9
Loan:deposit ratio (%)	93	90
Risk-weighted assets (£bn)	50.8	52.7

### Building a better bank that serves customers well

- ▶ PBB continue to make the bank simpler and fairer for customers by simplifying processes, professional standards training and removing sales based incentives for frontline staff.
- ▶ We continued to make better use of our digital channels to make it simpler to serve our customers and easier for them to do business with us. We now have 4.2 million customers in the UK regularly using our mobile app, 19% higher than the end of 2015, and around 60% of our personal customers used a digital channel within the last 90 days. In 2016, we more than doubled the number of customers who purchased a product through our mobile channel compared with 2015. NatWest customers can now apply for personal loans, credit cards and overdrafts via the mobile app, facilitating approximately 8% of total applications. Advocacy amongst our active mobile customers increased significantly over 2016 with NatWest mobile NPS at an all time high of +52.
- ▶ Our new business banking 'Online Account Opening' service now allows start up business customers to submit an application online in just ten minutes and get a sort code and account number in under an hour. RBS was awarded a Moneyfacts 5 star rating for Business Banking accounts.
- ▶ In addition to our digital channels, PBB continues to provide multiple physical channels for serving customers, including access to a network of c.11,500 Post Office branches in the UK, c.1,000 An Post branches in the Republic of Ireland, and 41 mobile banking vans alongside our existing network of 1,425 branches and 4,646 ATMs.
- ▶ PBB continues to help people manage their money better through; MoneySense, First Saver accounts, offering impartial advice, text alerts to customers and in-house Citizens Advice Bureau advisors to help distressed customers.
- ▶ RBS enhanced its support for social enterprises in 2016. In May, RBS launched a new SE100 Social Business Club with communications agency Matter & Co. The partnership offers a package of business support plus a special programme of regional events. In addition, RBS also increased its support to social enterprises through its lending charity Social & Community Capital.
- ▶ Following the launch of the Foundation account, an improved version of our Basic bank account, we opened a further 40,860 Foundation accounts in 2016, helping customers who would generally be declined a bank account.
- ▶ Our customers, the bank and our entire industry faced a bigger threat from fraud, scams and cyber attacks in 2016. In response, we trained our staff to spot phishing e-mails and we ran security awareness seminars and events for around 12,800 customers, staff and industry partners.





## Committed to service

In 2015, Chief Executive, Ross McEwan, signed the Armed Forces Covenant, pledging that no customers or colleagues would be disadvantaged because of their involvement with the military.

Our Holt's Military Banking colleagues have specialist knowledge of the armed forces, which helps them to better understand, and serve, our armed forces customers. Many bank colleagues are also associated with the armed forces – whether they are reservists, veterans or family members – and need support too.

This year, the bank's support of these customers and colleagues was rewarded, when we were awarded the Gold Award by the Ministry of Defence Employer Recognition scheme.

Defence Secretary Michael Fallon said: "This commitment is making a real difference to everyone who serves and their families – whether giving Reservists more time to train or supporting veterans or spouses."



**Alison Rose**  
CEO, Commercial  
& Private Banking

## Commercial & Private Banking

Commercial & Private Banking (CPB) serves commercial and corporate customers, operating principally through the NatWest, Royal Bank of Scotland and Lombard brands, and high net worth individuals, through Coutts and Adam & Company. RBS International (RBSI) continues to focus on supporting retail, commercial, corporate and financial institution customers in Jersey, Guernsey, Isle of Man, Gibraltar and Luxembourg. CPB aims to support the UK and Western European economies through its provision of credit and banking services to help businesses grow.

### Performance overview

- ▶ CPB recorded an operating profit of £1,043 million compared with £1,001 million in 2015. Adjusted operating profit of £1,617 million was £91 million lower than 2015 largely reflecting an increase in net impairment losses.
- ▶ Total income of £4,446 million was 1% higher than 2015, adjusting for transfers.
- ▶ Good growth was achieved in lending to UK businesses, with net loans and advances increasing by £11.3 billion, or 10%, to £121.1 billion, driven by increased borrowing across a number of sectors.
- ▶ Adjusted operating expenses, adjusting for transfers, increased by 3% reflecting an intangible asset write down and increased investment spend.
- ▶ Impairment losses of £213 million increased £131 million compared with 2015 largely reflecting a single name charge taken in respect of the oil and gas portfolio.



# The shipping news

The Port of Dover is Europe's busiest ferry port. It's a vital international gateway for the movement of passengers and trade, handling up to £119 billion of UK trade each year.

The Dover Western Docks Revival is the port's biggest ever single investment. RBS acted as financial advisor in raising a £200 million package of funding and provided a £35 million revolving credit facility.

This funding will support improvements to the port, transform Dover's waterfront and create up to 600 new jobs.





## Performance highlights

	2016	2015
Return on equity (%)	5.2	5.8
Net interest margin (%)	1.80	1.92
Cost:income ratio (%)	72	75
Net loans and advances to customers (£bn)	121.1	109.8
Customer deposits (£bn)	149.7	133.3
Loan:deposit ratio (%)	81	82
Risk-weighted assets (£bn)	96.6	89.3

### Building a better bank that serves customers well

- ▶ Commercial Banking reported the largest (and only significant) year on year improvement in NPS amongst major UK banks.
- ▶ Nearly 80% of our commercial customers' interaction with us is via digital channels, with around 270,000 payments processed every day.
- ▶ Coutts won the best private bank in the UK for the fifth year running, best private bank for philanthropy services and best initiative of the year in client facing technology at the Global Private Banking Awards, and was highly commended for innovation for its 'Coutts Concierge Online'.
- ▶ Our customers continue to benefit from the synergies between Commercial and Private Banking, with 1,100 referrals between Commercial and Private Banking in 2016.
- ▶ RBS continues to support UK business growth through the launch of 6 new business accelerator hubs in 2016, bringing the total to 12. In addition, NatWest launched a £1 billion lending fund to support small businesses.

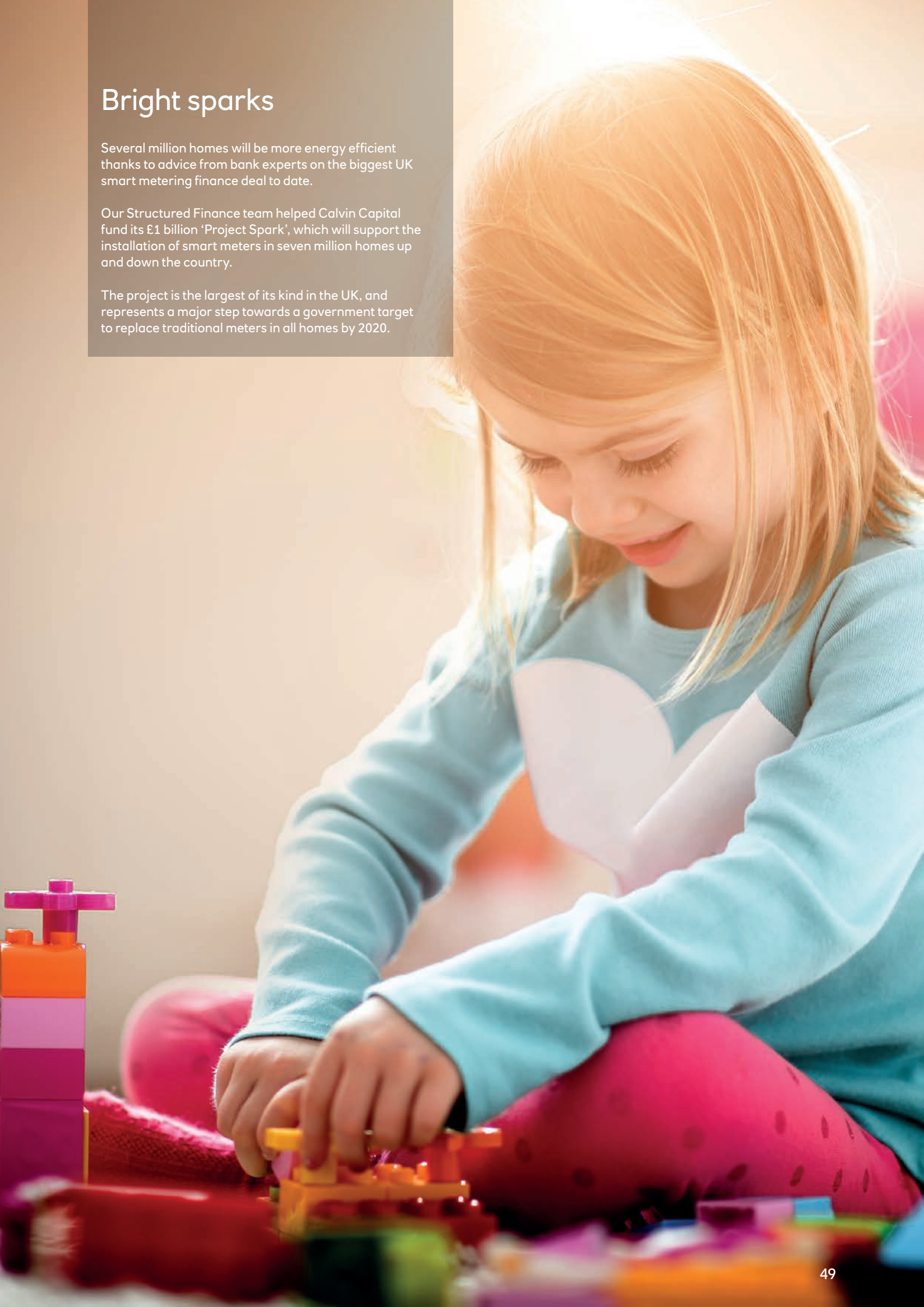


## Bright sparks

Several million homes will be more energy efficient thanks to advice from bank experts on the biggest UK smart metering finance deal to date.

Our Structured Finance team helped Calvin Capital fund its £1 billion 'Project Spark', which will support the installation of smart meters in seven million homes up and down the country.

The project is the largest of its kind in the UK, and represents a major step towards a government target to replace traditional meters in all homes by 2020.





**Chris Marks**  
CEO, NatWest Markets

## NatWest Markets

NatWest Markets provides financing and risk management solutions and is built around three product lines: Rates, Currencies and Financing. NatWest Markets puts its customers at the centre of the way it does business.

### Performance overview

- An operating loss of £386 million compared with an operating loss of £837 million in 2015 and included litigation and conduct costs of £528 million. The adjusted operating profit was £201 million compared with a loss of £55 million in 2015. The increase was driven by lower adjusted operating expenses and increased income.
- Total income increased by £47 million to £1,574 million compared with 2015. Excluding the impact of transfers (2015 – £98 million), adjusted income increased by £212 million, or 16%, to £1,521 million.
- Operating expenses decreased from £2,369 million to £1,960 million in 2016, driven by lower restructuring costs and lower adjusted expenses. Excluding business transfers, adjusted expenses reduced by £116 million, or 8%, reflecting c.£250 million of cost reductions partially offset by higher investment spend.

The increase was driven by Rates and Currencies, reflecting sustained customer activity throughout the year and favourable market conditions following the EU referendum and subsequent central bank actions.

## Simple solutions

After buying mobile phone operator EE, telecoms group BT wanted to convert the bank loan it used for the acquisition into a longer-dated format.

We acted as a lead bond arranger as well as a cross-currency swap market hedge coordinator, and billing and delivery bank on the five-year bond. By focusing on excellent customer service and through our integrated one-team approach, we were able to find the best solution and to make the process as simple as possible.

This helped BT to return to the European bond market for the first time in nearly two years.







## Performance highlights

	2016	2015
Return on equity (%)	(6.6)	(11.1)
Net interest margin (%)	0.84	0.53
Cost:income ratio (%)	125	155
Funded assets (£bn)	100.9	103.3
Risk-weighted assets (£bn)	35.2	33.1

### Building a better bank that serves customers well

- ▶ The NatWest Markets brand was introduced on 5 December 2016. The new brand is an important step towards our ambition to become No.1 for customers.
- ▶ NatWest Markets started a multi-year transformation in February 2015 and real progress is being made towards building a technology-led business with ongoing investment to improve efficiency and reduce costs while sustaining a well-controlled end-to-end model.
- ▶ The business's progress against its transformation plan is already being recognised externally:
  - No.1 for Gilts by Market Share EMEA FIs (Source: Greenwich Associates, European Fixed Income 2016 – Government Bonds)
  - No.1 for GBP Options, GBP Inflation and GBP 2Y – 10Y IRS (Source: Total Derivatives Dealer Rankings 2016)
  - Best bank for FX post-trade services (FX Week Best Bank Awards 2016)
  - No.1 for all European Issuers in the private placement market (Source: Dealogic Private Placement Review, Full Year 2016)
  - Best for putting corporate client's interest before the bank's (Source: Global Capital Bond Awards 2016)
  - NatWest Markets gained or held share in every Rates & FX product category for EMEA and the Americas (Source: Coalition Client Analytics Top 500 FI Wallets: G10 Foreign Exchange, G10 Rates)



**Mark Bailie**  
Chief Operating Officer

## Capital Resolution

Capital Resolution was established to execute the sale or wind down of most of the global footprint, from 38 countries to 13, and trade finance and cash management outside the UK and Ireland. Additionally non-strategic markets, portfolio and banking assets identified are being sold or wound down.

### Performance overview

- ▶ RWAs decreased by £14.5 billion to £34.5 billion reflecting disposal activity partially offset by an increase due to the weakening of sterling.
- ▶ Capital Resolution made an operating loss of £4,870 million, compared with an operating loss of £3,687 million in 2015, including litigation and conduct costs of £3,413 million. The adjusted operating loss was £1,432 million compared with a loss of £412 million in 2015.
- ▶ Total income included disposal losses of £572 million, £205 million higher than in 2015.
- ▶ Operating expenses reduced by £696 million to £4,255 million reflecting a £775 million reduction in adjusted operating expenses and a £1,229 million reduction in restructuring costs, partially offset by a £1,308 million increase in litigation and conduct costs. Adjusted operating expenses decreased by £775 million, or 50%, to £764 million, principally reflecting a 1,000 reduction in headcount.
- ▶ A net impairment loss of £253 million compared with a net impairment release of £725 million in 2015 and principally comprised charges relating to a number of shipping assets (£424 million).

# Governance at a glance

## Our Board

The Board has twelve directors comprising the Chairman, two executive directors and nine independent non-executive directors, one of whom is the Senior Independent Director. Biographies for each director can be found on pages 58 to 61. Mike Rogers was appointed to the Board on 26 January 2016 and Frank Dangeard was appointed to the Board on 16 May 2016.

The Board is collectively responsible for the long-term success of RBS and delivery of sustainable shareholder value. Its role is to provide leadership of RBS within a framework of prudent and effective controls which enables risks to be assessed and managed.

An internal evaluation of the effectiveness of the Board and its committees was conducted in 2016, led by the Chief Governance Officer and Board Counsel.

## Our Board committees

In order to provide effective oversight and leadership, the Board has established a number of Board committees with particular responsibilities. The work of the Board committees is discussed in their individual reports. The terms of reference for each of these committees is available on [rbs.com](http://rbs.com).

The full Governance report is on pages 57 to 111 of the 2016 Annual Report and Accounts.

### Group Audit Committee

Assists the Board in discharging its responsibilities for monitoring the quality of the financial statements of RBS. It reviews the accounting policies, financial reporting and regulatory compliance practices of RBS and RBS's systems and standards of internal controls, and monitors the work of internal audit and external audit.

### Board Risk Committee

Provides oversight and advice to the Board on current and potential future risk exposures of RBS and future risk strategy. It reviews RBS's compliance with approved risk appetite and oversees the operation of the RBS Policy Framework and submissions to regulators.

### Sustainable Banking Committee

Provides support to the Board in overseeing actions being taken by management to run a sustainable long term business, with specific focus on culture, people, customer, brand and environmental social and ethical issues.

### Group Performance and Remuneration Committee

Responsible for approving remuneration policy and reviewing the effectiveness of its implementation. It also considers senior executive remuneration and makes recommendations to the Board on the remuneration of executive directors.

### Group Nominations and Governance Committee

Assists the Board in the selection and appointment of directors. It reviews the structure, size and composition of the Board, and the membership and chairmanship of Board committees. It considers succession planning taking into account the skills and expertise which will be needed on the Board in future. Its remit also includes governance oversight.

## Board of directors

### Chairman

Howard Davies

### Executive directors

Ross McEwan

Ewen Stevenson

### Non-executive directors

Sandy Crombie  
(Senior Independent Director)

Penny Hughes

Brendan Nelson

Frank Dangeard

Baroness Noakes

Alison Davis

Mike Rogers

Morten Friis

Robert Gillespie

### Chief Governance Officer and Board Counsel

Aileen Taylor (Company Secretary)

## Executive Committee

The Board is supported by the Executive Committee comprising the executive directors and other senior executives. It supports the Chief Executive in managing RBS's businesses. It reviews and debates relevant items before consideration by the Board. It is responsible for developing and delivering RBS's strategy and it monitors and manages financial performance, capital allocation, risk strategy and policy, risk management, operational issues and customer issues.

### UK Corporate Governance Code

Throughout the year ended 31 December 2016, RBS has complied with all of the provisions of the UK Corporate Governance Code issued by the Financial Reporting Council dated April 2016 except in relation to provision (D.2.2) that the Group Performance and Remuneration Committee should have delegated responsibility for setting remuneration for the Chairman and executive directors. RBS considers that this is a matter which should rightly be reserved for the Board.

# Viability statement

In accordance with provision C.2.2 of the UK Corporate Governance Code, the Board of Directors (the “Board” of RBSG (the “bank”)) have assessed the viability of the bank taking into account the current position of the bank, the Board’s assessment of the bank’s prospects, and the bank’s principal risks, as detailed in the Strategic report on pages 38 and 39.

The Board’s assessment is further informed by the application of regulatory standards of capital and liquidity adequacy and stress test thresholds under extreme conditions.

The Board consider a period of three years to be an appropriate period for the assessment to be made. This period is within the bank’s strategic plan and regulatory and internal stress testing periods.

The bank’s business and strategic plans provide long term direction and are reviewed on, at least, an annual basis, including multi-year forecasts showing the expected financial position throughout the planning horizon. The base case plan indicates that the bank has sufficient capital and liquidity resources over the three year assessment period.

The bank’s base case plan is also tested in a series of extreme stress scenarios as part of internal and external stress testing. Results from the stress scenarios, including management’s response, are used as part of the Internal Capital Adequacy Assessment Process (ICAAP) and the Internal Liquidity Adequacy Assessment Process (ILAAP). These are summarised in the Capital and Risk Management section of the 2016 Annual Report and Accounts on pages 179 and 188.

Assessments of the risks of the greatest concern are captured through the bank’s processes for continuously identifying and effectively managing the principal top and emerging risks, as detailed on page 39 of the Strategic report. These assessments provide a view on the impact of the top risks crystallising, both individually and in combination. These risks are outlined in the Risk Overview and further discussed in the Risk Factors, both contained in the 2016 Annual Report and Accounts on pages 164 to 169 and 432 and 463, respectively, and include political, legal, macroeconomic, regulatory, operational and execution risks.

On the basis of this robust assessment of the principal risks facing the bank, the Board’s review of the business and strategic plans and other matters considered and reviewed during the year, and the results of the stress tests undertaken, the Board has a reasonable expectation that the bank will be able to continue in operation and meet its liabilities as they fall due over the period of the assessment.





## Free to dream

Through our partnership with Entrepreneurial Spark, we're helping entrepreneurs realise their dreams of owning and running their own business. We provide free facilities; free Wi-Fi, access to the bank's networks and suppliers, and free business advice. They don't need to bank with us and we take no equity; we simply believe it's right to support entrepreneurs and in turn help the economy grow.

Lawyer Sharon Amesu joined our Manchester hub in February 2016. "There was a real buzz and an immediate sense that I could be part of something quite special and significant" she says. "It's been instrumental in helping me grow my mentoring business and also a fantastically creative space to get to know, and network with, other aspirational and passionate people."

Across 12 accelerators throughout the UK, we have supported 1,736 companies with an aggregate turnover of more than £176 million. We've helped secure more than £151 million worth of investment for entrepreneurs in the Entrepreneurial Spark programme, and they in turn have created 3,152 jobs. More than 80% of the participating companies are still operating.



## Supplementary information

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## Our Board

### Chairman



#### **Howard Davies (age 66)**

*Nationality:* British

*Date of appointment:* 14 July 2015 (Board),  
1 September 2015 (Chairman)

*Experience:* Howard was Deputy Governor of the Bank of England from 1995 to 1997 and Chairman of the UK Financial Services Authority from 1997 to 2003. Howard was Director of the London School of Economics and Political Science from 2003 until May 2011. He is also Professor of Practice at the Paris Institute of Political Science (Sciences Po).

Howard was chair of the UK Airports Commission between 2012 and 2015 and is also the author of several books on financial subjects.

#### *External appointment(s):*

Independent director of Prudential plc and chair of the Risk Committee  
Member of the Regulatory and Compliance Advisory Board of Millennium Management LLC  
Chair of the International Advisory Council of the China Securities Regulatory Commission  
Member of the International Advisory Council of the China Banking Regulatory Commission  
Chairman of the London Library Trustees

#### *Committee membership(s):*

Group Nominations and Governance Committee (Chairman)

### Executive directors

#### Chief Executive



#### **Ross McEwan (age 59)**

*Nationality:* New Zealand

*Date of appointment:* 1 October 2013

*Experience:* Ross became Chief Executive of The Royal Bank of Scotland Group in October 2013. Between August 2012 and September 2013, he was Chief Executive Officer for UK Retail, joining from Commonwealth Bank of Australia where he was Group Executive for Retail Banking Services for five years. Prior to this he was Executive General Manager with responsibility for the branch network, contact centres and third party mortgage brokers.

Ross has more than 25 years experience in the finance, insurance and investment industries. Prior to Commonwealth Bank of Australia, he was Managing Director of First NZ Capital Securities. He was also Chief Executive of National Mutual Life Association of Australasia Ltd/AXA New Zealand Ltd. Ross has an MBA from Harvard.

#### *External appointment(s):*

None

#### *Committee membership(s):*

Executive Committee (Chairman)

#### Chief Financial Officer



#### **Ewen Stevenson (age 50)**

*Nationality:* British/New Zealand

*Date of appointment:* 19 May 2014

*Experience:* Prior to his current role, Ewen was at Credit Suisse for 25 years where he was latterly co-Head of the EMEA Investment Banking Division and co-Head of the Global Financial Institutions Group. He has over 20 years of experience advising the banking sector while at Credit Suisse.

Ewen has a Bachelor of Commerce and Administration majoring in Accountancy and a Bachelor of Law from Victoria University of Wellington, New Zealand.

#### *External appointment(s):*

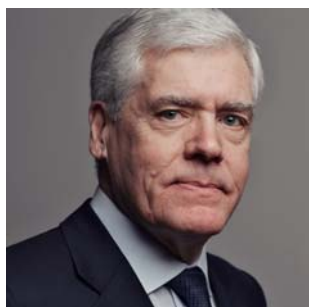
None

#### *Committee membership(s):*

Executive Committee  
US Risk Committee

## Our Board

### Independent non-executive directors



**Sandy Crombie (age 68)**

*Nationality:* British

*Date of appointment:* 1 June 2009

(Senior Independent Director)

*Experience:* Sandy spent his entire full-time career with Standard Life plc, retiring as Group Chief Executive. An actuary, he has served his profession in a variety of roles and has also served as a director of the Association of British Insurers.

Sandy has had a variety of cultural and community roles, and was previously Chairman of Creative Scotland, Chairman of the Edinburgh World City of Literature Trust and vice-Chairman of the Royal Conservatoire of Scotland.

*External appointment(s):*

President of the Cockburn Association

*Committee membership(s):*

Group Performance and Remuneration Committee (Chairman)  
Group Audit Committee  
Group Nominations and Governance Committee  
GRG Board Oversight Committee



**Frank Dangeard (age 59)**

*Nationality:* French

*Date of appointment:* 16 May 2016

*Experience:* Previously, Frank served as a non-executive director of Crédit Agricole CIB, EDF, Home Credit, Orange, Sonaecom SGPS, and as Deputy Chairman and acting Chairman of Telenor ASA. During his executive career he held various roles at Thomson S.A., including Chairman and Chief Executive Officer, and was Deputy Chief Executive Officer of France Telecom. Prior to that he was Chairman of SG Warburg France and a Managing Director of SG Warburg.

Frank is a graduate of HEC and IEP in Paris and of the Harvard Law School in the US.

*External appointment(s):*

Non-executive director of the RPX Corporation  
Non-executive director of Symantec Corporation

*Committee membership(s):*

Board Risk Committee



**Alison Davis (age 55)**

*Nationality:* British/USA

*Date of appointment:* 1 August 2011

*Experience:* Previously, Alison served as a director of City National Bank, First Data Corporation, Xoom, Diamond foods and chair of the board (and as Non-executive director) of LECG Corporation. She has also worked at McKinsey & Company, AT Kearney, as Chief Financial Officer at Barclays Global Investors (now BlackRock) and as managing partner of Belvedere Capital, a private equity firm focused on buy-outs in the financial services sector.

Alison is a graduate of Cambridge University and Stafford Business School.

*External appointment(s):*

Non-executive director and member of the compensation and audit committees of Unisys Corporation  
Non-executive director, and member of the audit committee of Fiserv Inc  
Non-executive director and chair of the audit committee of Ooma Inc

*Committee membership(s):*

Group Nominations and Governance Committee  
Group Performance and Remuneration Committee  
Sustainable Banking Committee

## Our Board

### Independent non-executive directors



#### **Morten Friis (age 64)**

*Nationality:* Norwegian

*Date of appointment:* 10 April 2014

*Experience:* Previously, Morten had a 34 year financial services career and held various roles at Royal Bank of Canada and its subsidiaries including Associate Director at Orion Royal Bank, Vice President, Business Banking and Vice President, Financial Institutions. In 1997, he was appointed as Senior Vice President, Group Risk Management and served as the Chief Credit Officer then Chief Risk Officer from 2004 to 2014. He was also previously a Director of RBC Bank (USA), Westbury Life Insurance Company, RBC Life Insurance Company and of RBC Dexia Investor Services Trust Company.

#### *External appointment(s):*

Member of the Board of Directors of The Canadian Institute for Advanced Research  
Member of the Board of Directors of the Harvard Business School Club of Toronto  
Non-executive director of Jackson National Life Insurance Company

#### *Committee membership(s):*

Group Audit Committee  
Board Risk Committee  
US Risk Committee (Chairman)



#### **Robert Gillespie (age 61)**

*Nationality:* British

*Date of appointment:* 2 December 2013

*Experience:* Robert began his career with Price Waterhouse (now PricewaterhouseCoopers) where he qualified as a chartered accountant. He then moved into banking joining SG Warburg, specialising in corporate finance, and was appointed as Co-Head and Managing Director of its US investment banking business in 1989. Following the acquisition in 1995 of Warburg by Swiss Bank Corporation (which subsequently merged with UBS), he then held the roles of Head of UK Corporate Finance, Head of European Corporate Finance and Co-Head of its global business and CEO of the EMEA region. He relinquished his management roles at the end of 2005, and was appointed Vice Chairman of UBS Investment Bank. Robert left UBS to join Evercore Partners, from where he was seconded to the UK Panel on Takeovers and Mergers, as Director General, from 2010 to 2013.

#### *External appointment(s):*

Independent board director at Ashurst LLP  
Chairman of Council at the University of Durham  
Chairman of the Boat Race Company Limited  
Director of Social Finance Limited

#### *Committee membership(s):*

Group Nominations and Governance Committee  
Group Performance and Remuneration Committee  
Sustainable Banking Committee  
GRG Board Oversight Committee



#### **Penny Hughes, CBE (age 57)**

*Nationality:* British

*Date of appointment:* 1 January 2010

*Experience:* Previously a non-executive director and Chairman of the corporate compliance and responsibility committee of Wm Morrison Supermarkets plc. Other former non-executive directorships include Skandinaviska Enskilda Banken AB, Home Retail Group plc, Vodafone Group plc, Reuters Group PLC, Cable & Wireless Worldwide plc and The Gap Inc. Penny spent the majority of her executive career at Coca-Cola where she held a number of leadership positions, latterly as President, Coca-Cola Great Britain and Ireland.

#### *External appointment(s):*

Non-executive Chairman of The Gym Group plc. Also chair of the nominations and member of the audit, risk and remuneration committees  
Non-executive director and member of the audit and nomination committees of SuperGroup plc

#### *Committee membership(s):*

Sustainable Banking Committee (Chairman)  
Board Risk Committee  
GRG Board Oversight Committee

## Our Board

### Independent non-executive directors



**Brendan Nelson (age 67)**

*Nationality:* British

*Date of appointment:* 1 April 2010

*Experience:* Brendan was global Chairman, financial services for KPMG. He previously held senior leadership roles within KPMG including as a member of the KPMG UK board from 1999 to 2006 and as vice-Chairman from 2006 until his retirement in 2010. He was Chairman of the Audit Committee of the Institute of Chartered Accountants of Scotland from 2005 to 2008. President of the Institute of Chartered Accountants of Scotland 2013/14.

*External appointment(s):*

Non-executive director and Chairman of the audit committee of BP plc  
Member of the Financial Reporting Review Panel

*Committee membership(s):*

Group Audit Committee (Chairman)  
Group Nominations and Governance Committee  
Board Risk Committee  
GRG Board Oversight Committee (Chairman)



**Baroness Noakes, DBE (age 67)**

*Nationality:* British

*Date of appointment:* 1 August 2011

*Experience:* Baroness Noakes is an experienced director on UK listed company boards with extensive and varied political and public sector experience. A qualified chartered accountant, she previously headed KPMG's European and International Government practices and has been President of the Institute of Chartered Accountants in England and Wales. She was appointed to the House of Lords in 2000 and has served on the Conservative front bench in various roles including as shadow treasury minister between 2003 and May 2010. Previously held non-executive roles on the Court of the Bank of England, Hanson, ICI, Severn Trent, Carpetright, John Laing and STThree.

*External appointment(s):*

Deputy Chairman, Ofcom

*Committee membership(s):*

Board Risk Committee (Chairman)  
Group Audit Committee  
GRG Board Oversight Committee  
US Risk Committee



**Mike Rogers (age 52)**

*Nationality:* British

*Date of appointment:* 26 January 2016

*Experience:* Mike has extensive experience in retail banking and financial services. Mike joined Barclays in 1986 where he undertook a variety of roles in the UK and overseas across business banking, wealth management and retail banking. Mike was Managing Director of Small Business, Premier Banking and UK Retail Banking and was latterly Chief Executive of Liverpool Victoria Group for 10 years.

*External appointment(s):*

None

*Committee membership(s):*

Group Performance and Remuneration Committee  
Sustainable Banking Committee



## Our Board

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### Chief Governance Officer and Board Counsel



**Aileen Taylor (age 44)**

*Nationality:* British

*Date of appointment:* 1 May 2010  
(Company Secretary)

*Experience:* A qualified solicitor, Aileen joined RBS in 2000. She was appointed Deputy Group Secretary and Head of Group Secretariat in 2007, and prior to that held various legal, secretariat and risk roles including Head of External Risk (Retail), Head of Regulatory Risk (Retail Direct) and Head of Legal and Compliance (Direct Line Financial Services).

Aileen is a fellow of the Chartered Institute of Bankers in Scotland and a member of the European Corporate Governance Council. She is also a member of the FCA's Listing Authority Advisory Panel.

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### Executive Committee

The Board is supported by the Executive Committee comprising the executive directors and other senior executives. Details of the composition of the Executive Committee and biographies of its members can be found at [rbs.com>about us>board and governance>ceo and board>executive committee](https://www.rbs.com/about-us/board-and-governance/ceo-and-board/executive-committee).

# Directors' Remuneration Report

**Annual statement from Sandy Crombie**  
**Chairman of the Group Performance and Remuneration Committee**



***“the focus is on meaningful, long-term shareholding as the mechanism for achieving alignment with shareholders”***

Dear Shareholder,

This report summarises the pay decisions that we took for the last financial year and the new remuneration policy that is being proposed to shareholders for approval at the forthcoming AGM.

## Policy developments in 2016

I know that views on executive pay are continuing to evolve. The government is consulting on areas of reform aimed at strengthening the UK's corporate governance arrangements. A separate industry-led Executive Remuneration Working Group has also set out areas where it is believed that improvement is needed to restore trust in current remuneration practices. RBS continues to contribute to consultations aimed at strengthening governance and pay arrangements.

It is clear many shareholders value simple remuneration structures. The Committee spent a great deal of time considering alternative constructs and how these would align to RBS's cultural aims on pay. The proposed new policy represents a significant change and has two principal aims: to produce greater alignment with shareholders and to discourage the potential for excessive risk taking.

The design focuses on creating alignment by ensuring executives build up larger shareholdings and retain them for longer. This intent is being reinforced by a significant increase in shareholding requirements from 250% to 400% of salary for the Chief Executive and from 125% to 250% for the Chief Financial Officer. The new policy also encourages sustainable long-term performance by having a lower maximum long-term incentive award level, but with performance assessed on factors that the executive would reasonably be expected to achieve, creating a less leveraged construct and encouraging safe and secure growth. The maximum potential long-term incentive award is being reduced by around 40% for the Chief Executive and by around 30% for the Chief Financial Officer.

It is also proposed that pro rating of long-term incentive awards will not apply for good leavers under the new policy. The Committee recognises that time pro rating is a common preference for some investors and its removal has only been included after considerable thought, and after consulting with a number of shareholders. The intention is to create high levels of shareholding that persist for a period after leaving and pro rating of awards reduces this alignment. RBS is unusual in having no annual bonus element of pay for executive directors and bonus awards would typically not be subject to pro rating. Furthermore, the policy aims broadly to maintain the expected value of pay to executive directors over their typical tenure in role.

This aim is achieved through a combination of reduced award levels, performance factors that are designed to be more within the control of management and the removal of pro rating for good leavers.

No change is proposed to the quantum of fixed pay, although fixed share allowances will be released over three, rather than five years to create a more even release of value across fixed and variable pay. A further development is that the pension allowance under the recruitment policy for new executive directors will be reduced from 35% to 25%, bringing the rate closer to that of the wider employee population.

In summary, the focus is on meaningful long-term shareholding as the mechanism for achieving alignment with shareholders. To date, the proposed remuneration policy has been well received in discussions with our largest shareholders.

## Considerations for other employees

The Committee recognises that RBS will only achieve its ambitions if all employees are engaged, motivated and supported by appropriate remuneration structures. Average salaries for our UK employees have increased by 7.5% over the last three years while executive directors' salaries have been static. Our rates of pay continue to exceed the living wage and we have removed sales incentives for front line retail staff and increased fixed pay so that they can concentrate on providing great customer service.

## Financial performance in 2016

Some important milestones were met in 2016. RBS was able to retire the Dividend Access Share in March and this was a key part in normalising RBS's capital structure. Good progress has also been made in resolving a number of major legacy and conduct issues although these continue to affect financial results. Variable pay across RBS is subject to a robust performance assessment process which allows outcomes to be adjusted if risk management or conduct has fallen short of the required standard.

The restructuring of the business has continued during 2016 but there is a strong business at the heart of RBS, capable of delivering sustainable returns for shareholders. The franchises have performed well with adjusted operating profits of £4,249 million for 2016. The Committee's decisions aim to strike a balance in rewarding employees for good performance but recognising RBS is not yet in the position that it needs to be.

## Pay decisions for 2016

The Group bonus pool has fallen from £373 million in 2015 to £343 million in 2016, a reduction of 8%. Over 93% of this pool will be paid to those below the executive level. Where employees do receive a bonus, the average amounts remain relatively modest with 50% of employees receiving £2,000 or less and a further 23% receiving less than £5,000. The amount of any immediate cash bonuses continues to be limited to £2,000.

The report sets out further information and I hope shareholders will support the resolutions on remuneration arrangements at the forthcoming AGM. I am very grateful for the guidance and support provided by my fellow Committee members as well as those who assist the Committee over the year. I would also like to thank shareholders for their constructive input as we discussed how best to shape the remuneration policy for the years ahead.

Sandy Crombie  
Chairman of the Group Performance and Remuneration Committee  
23 February 2017

# Directors' Remuneration Report

## Comparison of the current and new remuneration policy for executive directors

	Current policy	New policy
<p>Fixed remuneration</p> <p><i>overall, no change in quantum at this time</i></p>	<p><b>Salary</b> £1,000,000 for the Chief Executive £800,000 for the Chief Financial Officer</p> <p><b>Fixed share allowance</b> 100% of salary, delivered in shares released over a five year retention period.</p> <p><b>Pension allowance</b> 35% of salary, delivered in cash.</p> <p><b>Standard benefit funding</b> £26,250</p>	<p>No changes to salary levels are proposed at this time.</p> <p>No change to the fixed share allowance amount but shares will be released over a three year retention period, to create a more even release structure between fixed and variable pay.</p> <p>No change to pension allowance for current executive directors. Policy for new executive directors to be reduced to 25% of salary.</p> <p>No changes to standard benefit funding level.</p>
<p>Variable remuneration</p> <p><i>significant reduction in maximum potential</i></p>	<p><b>Long-term incentive award</b> Underlying award of 400% of salary but with pay-out capped by regulatory maximum which for performance year 2016 equates to 287% of salary.</p> <p>Pre-vest performance measures based on four categories: Economic Profit, Relative TSR, Safe &amp; Secure Bank and Customers &amp; People together with a risk and conduct underpin.</p> <p>A three year performance period and the award vests in equal amounts in years four and five.</p> <p>A six month retention period applies after vesting and the clawback period is seven years from the date of grant.</p>	<p>175% of salary for the current Chief Executive (currently £1.75 million) and 200% of salary for the current Chief Financial Officer (currently £1.6 million).</p> <p>Pre-grant and pre-vest tests, to consider performance in the round, against what would reasonably have been expected in the areas of Finance, Risk &amp; Operations, Customers and our People. Risk &amp; Control and Stakeholder Perception underpins will apply.</p> <p>Extension of the deferral period with vesting taking place in equal amounts over years three to seven.</p> <p>A 12 month retention period applies after vesting. The clawback period is extended to ten years from grant if events are under investigation at the end of the seven year period.</p>
<p>Other elements</p> <p><i>better alignment with shareholders</i></p>	<p><b>Shareholding requirement</b> 250% of salary for the Chief Executive 125% of salary for the Chief Financial Officer</p> <p>A period of five years is allowed in which to build up shareholdings to the required level. Any unvested share awards are excluded from the calculation.</p> <p><b>Leaver treatment</b> LTI awards held by good leavers are normally pro rated based on time served during the performance period.</p>	<p>400% of salary for the Chief Executive 250% of salary for the Chief Financial Officer.</p> <p>Unvested LTI awards will count towards the requirement once any pre-vest performance has been assessed, three years after grant. The number of unvested shares that count will be reduced to reflect the estimated tax liability arising on vesting. Once shares are free from their respective retention periods, executive directors will be permitted to sell a maximum of 25% of such shares until the requirement is met. It is estimated that it would take a new Chief Executive five years to meet the 400% shareholding requirement.</p> <p>Executive directors will continue to hold significant shareholdings after leaving and a post-employment shareholding requirement is therefore not considered necessary. Depending on leaver circumstances, it would take between three and eight years for an executive director to fully dispose of RBS shares due to the long vesting and retention periods.</p> <p>Future LTI awards held by good leavers will not be subject to pro rating for time. Removal of pro rating is a key part of the construct in order to achieve the reduction in maximum opportunity while broadly maintaining expected value to executive directors over their typical tenure in role. It also helps to ensure that individuals retain an appropriate long-term focus right up to the point of departure, as well as providing greater shareholder alignment post employment.</p>

Further details on the new remuneration policy can be found in the 2016 Annual Report and Accounts available on [rbs.com](http://rbs.com).

# Directors' Remuneration Report

## Wider employee considerations

To provide the best possible customer service, RBS is building a strong, simple and fair bank. Performance and pay management is part of that process.

### RBS needs to build an engaged and inclusive workforce, capable of providing excellent customer service.

- Senior leaders are subject to individual and collective performance assessment based on factors which include financial strength and customer service.
- RBS has set a target for each Executive Committee member to have at least 30% women in senior roles (the top three leadership layers) by 2020.
- Gender targets are one of three People measures, together with engagement and leadership, which are considered when assessing performance for some of our senior leaders.
- Employees are motivated by good leadership and almost 16,000 employees undertook our 'Determined to Lead' leadership programme in 2016.
- We have now trained over 60% of employees at all levels of RBS to tackle unconscious bias, helping to remove bias in our recruitment processes, build more inclusive teams, make well informed decisions and better understand and serve our customers.
- In October 2016 we launched Service Excellence, our new customer service programme with over 34,000 employees receiving training so far.
- Professional Standards Frameworks set out the relevant knowledge, skills, and behaviours expected of RBS employees to embed good conduct.
- While employee engagement has been impacted during 2016 by the ongoing restructuring of the business, it remains higher than when we set out our strategic plan in 2014.

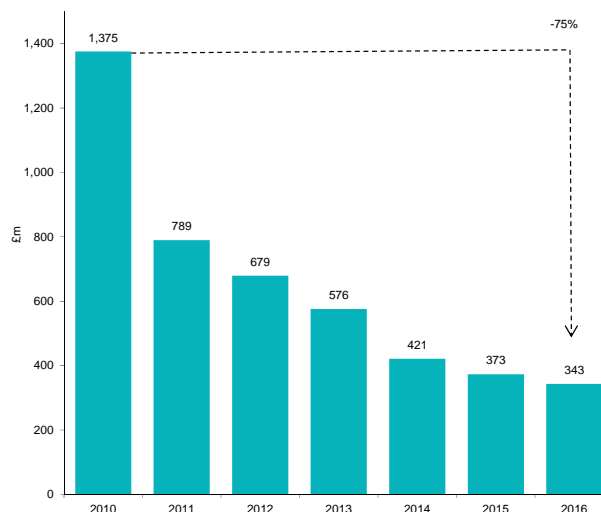
### RBS is simplifying how employees get paid.

- In Personal & Business Banking, pay for frontline roles is linked to supporting customers, rather than short-term incentive schemes, and this was extended to employees in Ulster Bank with effect from 1 January 2017.
- Our clerical population in the UK and Republic of Ireland now receives only fixed pay, making pay arrangements easier to understand.
- Salary ranges have been updated to reflect the external market and to ensure that people doing the same or similar roles are paid more consistently.

## The Committee must ensure that good behaviours are encouraged and that conduct issues are accounted for.

- The policy aims to pay people appropriately for their work and commitment to serve customers well.
- RBS continues to operate as a fully accredited living wage employer.
- If conduct falls short of the standard expected, the Committee can adjust variable pay awards through malus (reduction or cancellation of awards prior to payment) or clawback (recovering awards that have already been paid).
- Further information on the accountability review process under which malus and clawback can be applied is set out later in this report.
- The Committee aims to strike a fair balance between adjustments to variable pay as a targeted measure to change behaviour whilst not disproportionately penalising employees who are not directly responsible for events.
- As set out below, bonuses have continued to shrink at RBS, aligned with the restructuring that has taken place and the actions taken by the Committee.
- Pay levels reflect the progress made in 2016 and the bank that RBS is becoming, while ensuring our people are fairly and appropriately rewarded for the work they do.

### Bonus pool reduced steadily from 2010 to 2016





# Annual report on remuneration

## Total remuneration paid to executive directors for 2016 (audited)

	Ross McEwan		Ewen Stevenson	
	2016 £000	2015 £000	2016 £000	2015 £000
Salary	1,000	1,000	800	800
Fixed share allowance (1)	1,000	1,000	800	800
Benefits (2)	113	149	26	26
Pension	350	350	280	280
Total fixed remuneration (3)	2,463	2,499	1,906	1,906
Annual bonus	n/a	n/a	n/a	n/a
Long-term incentive award (4)	1,030	993	—	—
Total remuneration	3,493	3,492	1,906	1,906

Notes:

- (1) The value of the fixed share allowance is based on 100% of salary and, as part of fixed remuneration, it is not subject to any performance conditions. It is delivered in shares and released over a retention period.
- (2) Includes standard benefit funding of £26,250 per annum with the remainder being travel assistance in connection with company business (£74,621) and relocation expenses (£11,801) provided to Ross McEwan. The 2015 benefits figure for Ross McEwan has been restated to include a value for travel assistance during that year.
- (3) The total fixed remuneration at £2,463,000 is higher than the £2,376,250 fixed remuneration in the implementation of policy section as the lower figure includes standard benefits only.
- (4) The 2016 value for Ross McEwan relates to an LTI award granted in 2014 that is due to vest in March 2017. The performance conditions ended on 31 December 2016 and have been assessed as set out below together with an estimate of the vesting value. The value for 2015 has been amended from the estimated value of £1,347,000 provided in the 2015 report to reflect the actual value on the vesting date in March 2016.

## 2014 LTI – final assessment of performance measures (audited)

An assessment of performance of each relevant element was provided by internal control functions and PwC assessed relative Total Shareholder Return (TSR) performance against a peer group of comparator banks.

Performance Measures (and weightings)	Performance for minimum vesting	Vesting at minimum	Performance for maximum (100%) vesting	Actual Performance	Vesting outcome	Weighted Vesting %
Economic Profit (25%)	(£1 billion)	25%	£0	(£0.4 billion)	82%	20%
Relative TSR (25%)	TSR at median	20%	TSR at upper quartile	18 <sup>th</sup> percentile ranking	0%	0%
Safe & Secure Bank (25% split across two measures)	Vesting between 0% - 100% qualified by Committee discretion CET1 ratio target: >=12% Cost:income ratio target: 59%			CET1 ratio: 13.4% Cost:income ratio of 61%	88%	22%
Customers & People (25% split across two measures)	Vesting between 0% - 100% qualified by Committee discretion Net Promoter Score target: Gap to number 1 of 8.7 Engagement Index (EI) target: EI within 3 points of Global Financial Services (GFS) norm			Gap to number 1 of 13.4  EI: 6 points behind GFS norm	0%	0%
Overall vesting outcome (1)						42%

Note:

- (1) The Economic Profit outcome was determined according to the vesting scale where target performance of (£0.77 billion) would result in 62.5% vesting.

The vesting within the Safe & Secure Bank and Customers & People categories has been qualified by Committee discretion, taking into account the margin by which targets have been missed or exceeded and any other relevant factors. The CET1 ratio target was exceeded and the cost:income ratio was deemed to have been substantially met, reflecting the significant progress from the 2013 base year of 69% and recognising the significant headwinds in the external environment since that time. This resulted in 100% and 75% vesting respectively for these elements and a combined vesting outcome under the Safe & Secure category of 88%.

On the Customers measure, whilst absolute performance on the customer position had improved over the period, the target on closing the gap had been missed and in the circumstances the Committee concluded performance was not sufficient in order to justify vesting. On the People measure, the Committee recognised that engagement scores had been impacted by a number of unforeseen factors and difficult decisions required by management during the year but again it was felt that the level of vesting for this element should be nil.

The Committee also received input from the BRC. In making its final judgement, the Committee considered the overall context of performance including a number of factors such as the Williams & Glyn transaction. The Committee believed such factors were already adequately reflected across the performance categories and that the overall vesting outcome above was fair and appropriate.

# Annual report on remuneration

## 2014 LTI vesting amount included in the total remuneration table (audited)

Ross McEwan was granted an LTI award in March 2014. The performance conditions as set out on the previous page ended on 31 December 2016 and the award is due to vest in March 2017. The average share price over the last three months of the financial year has been used to estimate the vesting value.

Ross McEwan				
Performance category	% vesting	Maximum RBS shares (1)	Vested RBS shares	Value (2)
Economic Profit	82%	305,064	244,052	
Relative TSR	0%	305,064	—	
Safe & Secure Bank	88%	305,064	268,457	
Customers & People	0%	305,064	—	
Overall vesting outcome based on above	42%		512,509	£1,030,143
Maximum capped shares available to vest			915,193	

Notes:

- (1) The maximum number of shares is calculated in line with the underlying award structure where each of the four performance categories could give rise to shares worth 100% of salary at grant but with the overall maximum capped at 300% of salary at grant. The percentage vesting under the Economic Profit category has been rounded from 82% to 80% when calculating the number of vested shares in order to maintain the overall weighted vesting outcome at 42%.
- (2) Based on a RBS share price of £2.01, the average over the three month period from October to December 2016.

## Total remuneration paid to the Chairman and non-executive directors for 2016 (audited)

A new Group Nominations and Governance Committee was established at the end of January 2016, replacing the former Group Nominations Committee, with an expanded remit and a reduced number of members. The RCR BOC and CIB BOC were stood down at the end of January and February 2016 respectively. The US steering group was stood down in 2016 and a new US Risk Committee was established to comply with US Enhanced Prudential Standards and the first meeting took place in May 2016. The total fees paid during 2016 are set out below.

											Fees 2016 £000	Fees 2015 £000	Benefits 2016 £000	Benefits 2015 £000	Total 2016 £000	Total 2015 £000
Chairman (composite fee)											750	260	8	2	758	262
Howard Davies (1)																
Non-executive directors (2)	Noms & Gov										Fees 2016 £000	Fees 2015 £000	Benefits 2016 £000	Benefits 2015 £000	Total 2016 £000	Total 2015 £000
	Board £000	Gov £000	GAC £000	RemCo £000	BRC £000	SBC £000	RCR BOC £000	CIB BOC £000	GRG BOC £000	Other £000						
Sandy Crombie (3)	73	14	30	60			1		15	30	223	227	—	—	223	227
Frank Dangeard (4)	46				12						58	—	—	—	58	—
Alison Davis	73	14		30		30					147	143	—	—	147	143
Morten Friis (3)	73		30		30			3		23	159	169	—	—	159	169
Robert Gillespie (3)	73	14		30	18	30		5	15	25	210	305	—	—	210	305
Penny Hughes	73				30	60			15		178	182	—	—	178	182
Brendan Nelson	73	14	60		30		1	3	30		211	217	—	—	211	217
Baroness Noakes (3)	73		30		60		2	3	15	9	192	223	—	—	192	223
Mike Rogers (4)	68					20					88	—	—	—	88	—

Notes:

- (1) Howard Davies joined the Board on 14 July 2015 and became Chairman with effect from 1 September 2015. The Benefits column includes private medical cover.
- (2) In line with market practice, non-executive directors are reimbursed expenses incurred in connection with their attendance at Board meetings. To the extent that HMRC determines that any amounts are taxable, RBS will settle the associated tax liability on behalf of the non-executive director.
- (3) Under the 'Other' column, Sandy Crombie received fees as the Senior Independent Director and Morten Friis received fees for his work on the US steering group until April 2016. The US Risk Committee was established with Morten Friis and Baroness Noakes receiving fees as Chairman and member of the Committee respectively. Robert Gillespie received fees for his role as an advisor to the NatWest Markets (formerly CIB) CEO and senior management.
- (4) Frank Dangeard and Mike Rogers joined the Board on 16 May 2016 and 26 January 2016 respectively.

Key to table:

Noms & Gov	Group Nominations and Governance Committee
GAC	Group Audit Committee
RemCo	Group Performance and Remuneration Committee
BRC	Board Risk Committee
SBC	Sustainable Banking Committee
BOC	Board Oversight Committee for the RCR, NatWest Markets (formerly CIB) and GRG business areas

## Financial results

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### Strategic report

#### Important note

The Strategic report forms part of the 2016 Annual Report and Accounts (Report and Accounts). It does not contain sufficient information to allow for a full understanding of the results of the Group or of the state of affairs of the company. The Group's results and financial condition could be adversely affected by certain risks and uncertainties, including the outcome of litigation and investigations. For further information, the 2016 Report and Accounts, the auditor's report on those accounts and the Report of the directors should be consulted.

Shareholders can obtain a copy of the R&A and may also elect to receive all future Report and Accounts, free of charge, by contacting our Registrar, details of which can be found on page 71. A copy can be viewed on the Group's website [rbs.com/annualreport](http://rbs.com/annualreport).

#### Report of the auditor

The auditor's report on the full accounts and the auditable part of the Directors' remuneration report for the year ended 31 December 2016 was unqualified and did not include an emphasis of matter or a statement under sections 498(2) (inadequate accounting records or returns or accounts or Directors' remuneration report not agreeing with records and returns) or 498(3) (failure to obtain necessary information and explanations) of the Companies Act 2006. The auditor's statement under section 496 (whether the information in the Report of the directors' was consistent with the accounts) was unqualified.

#### RBS Group ring-fencing

The UK ring-fencing legislation requiring the separation of essential banking services from investment banking services will take effect from 1 January 2019.

To comply with these requirements it is RBS's intention to place the majority of the UK and Western European banking business in ring-fenced banking entities under an intermediate holding company. NatWest Markets will be a separate non ring-fenced bank and The Royal Bank of Scotland International (Holdings) Limited (RBSI Holdings) will also be placed outside the ring-fence, both as direct subsidiaries of RBSG.

The final ring-fenced legal structure and the actions to be taken to achieve it, remain subject to, amongst other factors, additional regulatory, Board and other approvals as well as employee information and consultation procedures. All such actions and their respective timings may be subject to change, or additional actions may be required, including as a result of external and internal factors including further regulatory, corporate or other developments.

On 1 January 2017 RBS made a number of key changes to the legal entity structure as detailed below to support the move towards a ring-fenced structure. There are also plans to make further changes prior to 1 January 2019.

#### NatWest Holdings Limited (NatWest Holdings)

RBS introduced an intermediate holding company, NatWest Holdings, as a direct subsidiary of RBS plc. This is an interim structure as NatWest Holdings is expected to become a direct subsidiary of RBSG in mid 2018.

National Westminster Bank Plc (NatWest) and Adam & Company Group PLC (Adam & Co) transferred from being direct subsidiaries of RBS plc, and Ulster Bank (Ireland) Holdings Unlimited Company (UBIH) transferred from being a direct subsidiary of Ulster Bank Limited, to become direct subsidiaries of NatWest Holdings.

#### RBS International

RBSI Holdings transferred from being an indirect subsidiary of RBS plc to become a direct subsidiary of RBSG. The intention is for RBS International's operating companies to remain as subsidiaries of RBSI Holdings.

NatWest bought Lombard North Central PLC and RBS Invoice Finance (Holdings) Limited from RBS plc and some smaller companies from other members of the Group.

## Financial results

### Summary consolidated income statement for the year ended 31 December 2016

	2016 £m	2015 £m
Net interest income	8,708	8,767
Non-interest income	3,882	4,156
<b>Total income</b>	<b>12,590</b>	<b>12,923</b>
Restructuring costs	(2,106)	(2,931)
Litigation and conduct costs	(5,868)	(3,568)
Other operating expenses	(8,220)	(9,854)
<b>Operating expenses</b>	<b>(16,194)</b>	<b>(16,353)</b>
Loss before impairment (losses)/releases	(3,604)	(3,430)
Impairment (losses)/releases	(478)	727
<b>Operating loss before tax</b>	<b>(4,082)</b>	<b>(2,703)</b>
Tax charge	(1,166)	(23)
<b>Loss from continuing operations</b>	<b>(5,248)</b>	<b>(2,726)</b>
Profit from discontinued operations, net of tax	—	1,541
<b>Loss for the year</b>	<b>(5,248)</b>	<b>(1,185)</b>
Attributable to:		
Non-controlling interests	10	409
Preference shareholders	260	297
Paid in equity holders	244	88
Dividend access share	1,193	—
Ordinary shareholders	(6,955)	(1,979)
	<b>(5,248)</b>	<b>(1,185)</b>
Per ordinary share		
Basic and diluted loss from continuing operations	(59.5p)	(27.7p)
Basic and diluted loss from continuing and discontinued operations	(59.5p)	(17.2p)

### Summary consolidated statement of comprehensive income for the year ended 31 December 2016

	2016 £m	2015 £m
<b>Loss for the year</b>	<b>(5,248)</b>	<b>(1,185)</b>
Items that do not qualify for reclassification		
Loss on remeasurement of retirement benefit schemes	(1,049)	(73)
Tax	288	306
	<b>(761)</b>	<b>233</b>
Items that do qualify for reclassification		
Available-for-sale financial assets	(94)	44
Cash flow hedges	765	(700)
Currency translation	1,263	(1,181)
Tax	(106)	108
	<b>1,828</b>	<b>(1,729)</b>
<b>Other comprehensive income/(loss) after tax</b>	<b>1,067</b>	<b>(1,496)</b>
<b>Total comprehensive loss for the year</b>	<b>(4,181)</b>	<b>(2,681)</b>
Attributable to:		
Non-controlling interests	121	370
Preference shareholders	260	297
Paid-in equity holders	244	88
Dividend access share	1,193	—
Ordinary shareholders	(5,999)	(3,436)
	<b>(4,181)</b>	<b>(2,681)</b>



## Financial results

### Summary consolidated balance sheet as at 31 December 2016

	2016 £m	2015 £m
<b>Assets</b>		
Cash and balances at central banks	74,250	79,404
Loans and advances to banks	30,138	30,646
Loans and advances to customers	351,950	333,892
Debt securities	72,522	82,097
Equity shares	703	1,361
Settlement balances	5,526	4,116
Derivatives	246,981	262,514
Intangible assets	6,480	6,537
Property, plant and equipment	4,590	4,482
Deferred tax	1,803	2,631
Prepayments, accrued income and other assets	3,700	4,242
Assets of disposal groups	13	3,486
<b>Total assets</b>	<b>798,656</b>	<b>815,408</b>
<b>Liabilities</b>		
Deposits by banks	38,556	38,296
Customer accounts	380,968	370,298
Debt securities in issue	27,245	31,150
Settlement balances	3,645	3,390
Short positions	22,077	20,809
Derivatives	236,475	254,705
Provisions for liabilities and charges	12,836	7,366
Accruals and other liabilities	6,991	7,749
Retirement benefit liabilities	363	3,789
Deferred tax	662	882
Subordinated liabilities	19,419	19,847
Liabilities of disposal groups	15	2,980
<b>Total liabilities</b>	<b>749,252</b>	<b>761,261</b>
Non-controlling interests	795	716
Owners' equity	48,609	53,431
<b>Total equity</b>	<b>49,404</b>	<b>54,147</b>
<b>Total liabilities and equity</b>	<b>798,656</b>	<b>815,408</b>
<b>Memorandum items</b>		
Contingent liabilities and commitments	150,691	153,752

## Shareholder information

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### Financial calendar

#### Dividends

#### Payment dates

Cumulative preference shares 31 May and 29 December 2017

Non-cumulative preference shares 31 March, 30 June,  
29 September  
and 29 December 2017

#### Ex-dividend date

Cumulative preference shares 4 May 2017

#### Record date

Cumulative preference shares 5 May 2017

#### Interim results

4 August 2017

### Shareholder enquiries

Shareholdings in the company may be checked by visiting the Shareholder centre section of our website, [www.rbs.com](http://www.rbs.com). You will need the shareholder reference number printed on your share certificate or tax voucher to gain access to this information.

Listed below are the most commonly used features on the website:

- holding enquiry - view balances, values, history, payments and reinvestments;
- address change - change your registered address;
- e-Comms sign-up - choose to receive email notification when your shareholder communications become available instead of paper communications;
- outstanding payments - reissue any uncashed payments using our online replacement service; and
- downloadable forms - including stock transfer and change of address forms.

You may also check your shareholding by contacting our Registrar:

Computershare Investor Services PLC  
The Pavilions  
Bridgwater Road  
Bristol BS99 6ZZ  
Telephone: +44 (0)370 702 0135  
Fax: +44 (0)370 703 6009  
Website: [www.investorcentre.co.uk/contactus](http://www.investorcentre.co.uk/contactus)

### Braille and audio Strategic report with additional information

Shareholders requiring a Braille or audio version of the Strategic report with additional information should contact the Registrar on +44 (0)370 702 0135.

### ShareGift

The company is aware that shareholders who hold a small number of shares may be retaining these shares because dealing costs make it uneconomical to dispose of them. ShareGift, the charity share donation scheme, is a free service operated by The Orr Mackintosh Foundation (registered charity 1052686) to enable shareholders to donate shares to charity.

Donating your shares in this way will not give rise to either a gain or a loss for UK capital gains tax purposes and you may be able to reclaim UK income tax on gifted shares. Further information can be obtained from HM Revenue & Customs.

Should you wish to donate your shares to charity in this way you should contact ShareGift for further information:

ShareGift, The Orr Mackintosh Foundation  
17 Carlton House Terrace, London SW1Y 5AH  
Telephone: +44 (0)20 7930 3737  
Website: [www.sharegift.org](http://www.sharegift.org)

## Shareholder information

### Share fraud warning

Investment scams are designed to look like genuine investments. If you have been contacted out of the blue, promised tempting returns and told the investment is safe, called repeatedly, or told the offer is only available for a limited time, you may have been contacted by fraudsters.

### How to avoid share fraud

#### Reject cold calls

If you have been cold called with an offer to buy or sell shares, chances are it is a high risk investment or a scam. You should treat the call with extreme caution. The safest thing to do is to hang up.

Check the firm on the Financial Services Register at [www.fca.org.uk/register](http://www.fca.org.uk/register)

The Financial Services Register is a public record of all firms and individuals in the financial services industry that are regulated by the FCA.

### Get impartial advice

Think about getting impartial financial advice before you hand over any money. Seek advice from someone unconnected to the firm that has approached you.

Remember, if it sounds too good to be true, it probably is.

### Report a scam

If you suspect that you have been approached by fraudsters please tell the FCA using the share fraud reporting form at [scamsmart.fca.org.uk](http://scamsmart.fca.org.uk), where you can find out more about investment scams. You can also call the FCA Consumer Helpline on 0800 111 6768.

If you have lost money to investment fraud, you should report it to Action Fraud on 0300 123 2040 or online at [www.actionfraud.police.uk](http://www.actionfraud.police.uk).

Find out more at [www.scamsmart.fca.org.uk](http://www.scamsmart.fca.org.uk)

### Analyses of ordinary shareholders

At 31 December 2016	Shareholdings	Number of shares - millions	%
Individuals	187,579	105.1	0.9
Banks and nominee companies	5,762	11,684.6	98.8
Investment trusts	65	0.7	—
Insurance companies	74	0.3	—
Other companies	537	8.6	0.1
Pension trusts	25	0.2	—
Other corporate bodies	79	23.7	0.2
	194,121	11,823.2	100.0
Range of shareholdings:			
1 - 1,000	168,270	41.5	0.3
1,001 - 10,000	24,335	54.8	0.5
10,001 - 100,000	938	27.7	0.2
100,001 - 1,000,000	372	132.2	1.1
1,000,001 - 10,000,000	154	505.5	4.3
10,000,001 and over	52	11,061.5	93.6
	194,121	11,823.2	100.0

## Important addresses

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### Important addresses

#### Shareholder enquiries

##### Registrar

Computershare Investor Services PLC  
The Pavilions  
Bridgwater Road  
Bristol BS99 6ZZ  
Telephone: +44 (0)370 702 0135  
Facsimile: +44 (0)370 703 6009  
Website: [www.investorcentre.co.uk/contactus](http://www.investorcentre.co.uk/contactus)

#### ADR Depository Bank

BNY Mellon Shareowner Services  
PO Box 30170  
College Station, TX 77842-3170  
Telephone: +1 866 241 9317 (US callers)  
Telephone: +1 201 680 6825 (International)  
Email: [shrrelations@cpushareownerservices.com](mailto:shrrelations@cpushareownerservices.com)  
Website: [www.mybnymdr.com](http://www.mybnymdr.com)

#### Corporate Governance and Regulatory Affairs

The Royal Bank of Scotland Group plc  
PO Box 1000  
Gogarburn Edinburgh EH12 1HQ  
Telephone: +44 (0)131 556 8555  
Facsimile: +44 (0)131 626 3081

#### Investor Relations

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Facsimile: +44 (0)207 672 1801  
Email: [investor.relations@rbs.com](mailto:investor.relations@rbs.com)

#### Registered office

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Telephone: +44 (0)131 556 8555  
Registered in Scotland No. SC45551

#### Website

[rbs.com](http://rbs.com)

#### Principal offices

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Telephone: +44 (0)131 626 0000

##### The Royal Bank of Scotland plc

PO Box 1000 Gogarburn Edinburgh EH12 1HQ 280  
Bishopsgate London EC2M 4RB

##### National Westminster Bank Plc

135 Bishopsgate London EC2M 3UR

##### Ulster Bank Limited

11-16 Donegall Square East Belfast BT1 5UB  
George's Quay Dublin 2

##### RBS Holdings USA Inc.

600 Washington Blvd  
Stamford CT  
06901 USA

##### Coutts & Company

440 Strand London WC2R 0QS

##### The Royal Bank of Scotland International Limited

Royal Bank House 71 Bath Street  
St Helier Jersey Channel Islands JE4 8PJ

##### RBS Holdings N.V.

Gustav Mahlerlaan 350  
Amsterdam  
1082 ME  
The Netherlands