

The TESCO logo is displayed in white on a dark purple background. It consists of the word "TESCO" in a bold, sans-serif font, with a stylized graphic of five slanted parallel lines underneath.

Retailing Services Seminar 2009

The TESCO logo is displayed in red on a white background. It consists of the word "TESCO" in a bold, sans-serif font, with a stylized graphic of five slanted parallel lines underneath.

## **Finance overview**

Iain Clink, Finance and International Director, Tesco Bank

Retailing Services Seminar, 19-20 November 2009

The TESCO Bank logo is displayed in red on a white background. It consists of the word "TESCO" in a bold, sans-serif font, with a stylized graphic of five slanted parallel lines underneath, followed by the word "Bank" in a smaller, sans-serif font.

## Agenda

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- The Balance Sheet
- The P&L
- Managing risk
- Summary

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The Balance Sheet

## Summary balance sheet

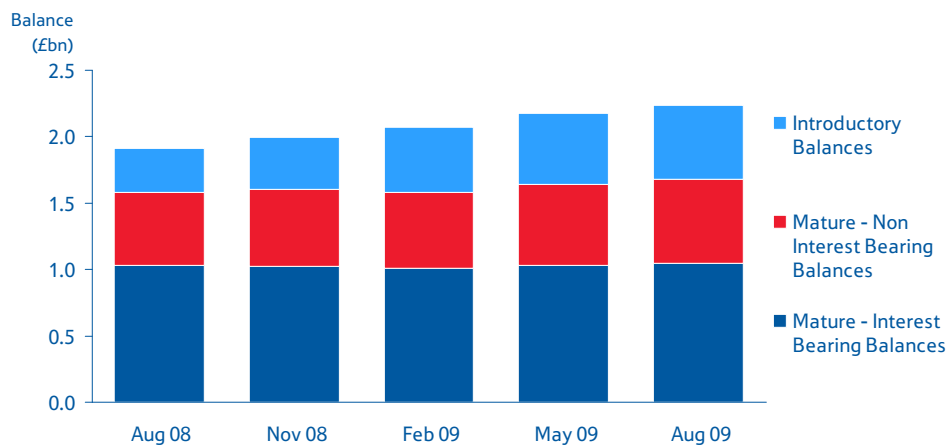
- Strong funding position
  - Not reliant on wholesale funding
  - High level of liquidity and surplus cash

Feb 2009 (£m)		Aug 2009 (£m)
	Loans and advances to customers	
2,023	– Cards	2,183
1,366	– Loans	1,614
2,129	Loans and advances to banks	1,802
259	Loan to RBS Insurance	259
420	Other assets	377
<b>6,197</b>	<b>Total assets</b>	<b>6,235</b>
4,538	Customer deposits	4,425
612	Debt securities issued	501
237	Intra-group liabilities	235
222	Corporate bond	222
581	Other liabilities	301
465	Equity	551
<b>6,197</b>	<b>Total liabilities</b>	<b>6,235</b>

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## The credit card portfolio

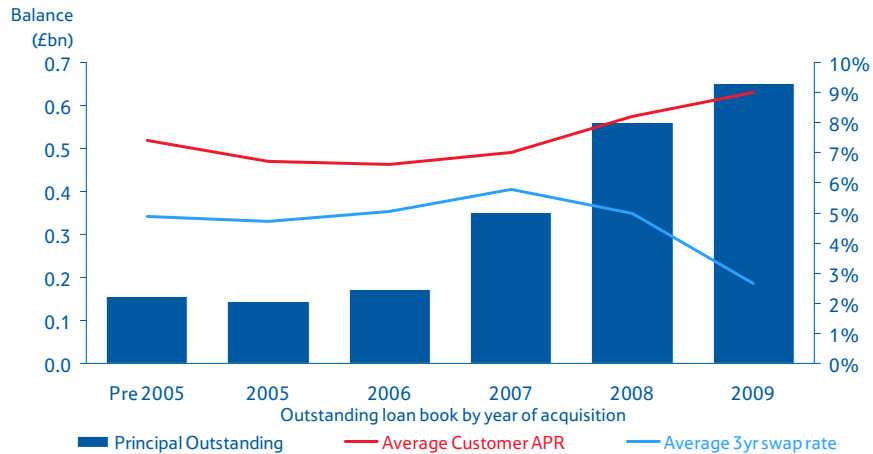
- New business is driving growth in the cards book
- As introductory balances mature, interest paid by customers will increase



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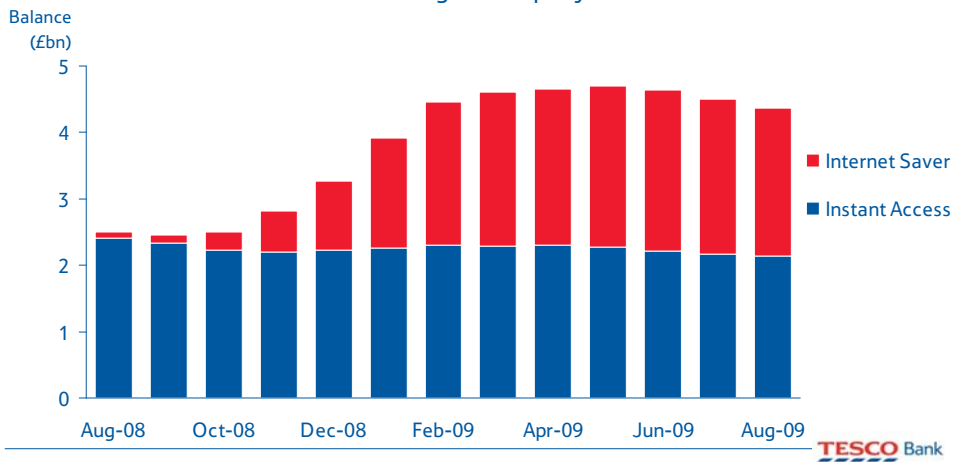
## The loan portfolio

- Margins started to widen in 2008
- Low margin loans are rolling off

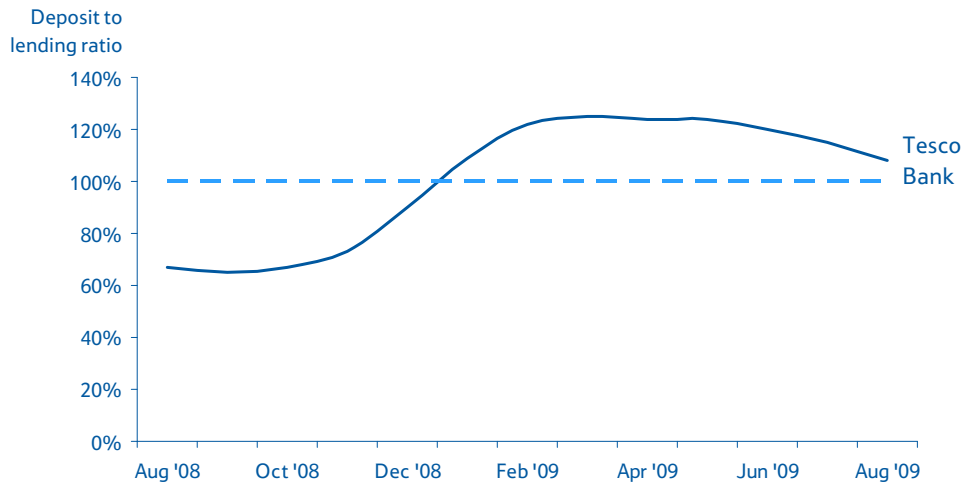


## The savings portfolio

- The savings back book is highly stable – c.60% of instant access balances have been with us since 2000
- Since launch the internet saver has grown rapidly



## Customer deposits are now funding customer lending



Source: Internal data, Bank of England

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## Liquid assets and short-term cash

Aug 2009	£m
Loans and advances to customers	
– Cards	2,183
– Loans	1,614
Loans and advances to banks	1,802
Loan to RBS Insurance	259
Other assets	377
<b>Total assets</b>	<b>6,235</b>
Customer deposits	4,425
Debt securities issued	501
Intra-group liabilities	235
Corporate bond	222
Other liabilities	301
Equity	551
<b>Total liabilities</b>	<b>6,235</b>

Liquid Assets and Short-term Cash	£m
UK Government Treasury Bills	501
Surplus cash / investment portfolio	1,301
<b>Loans and advances to banks</b>	<b>1,802</b>

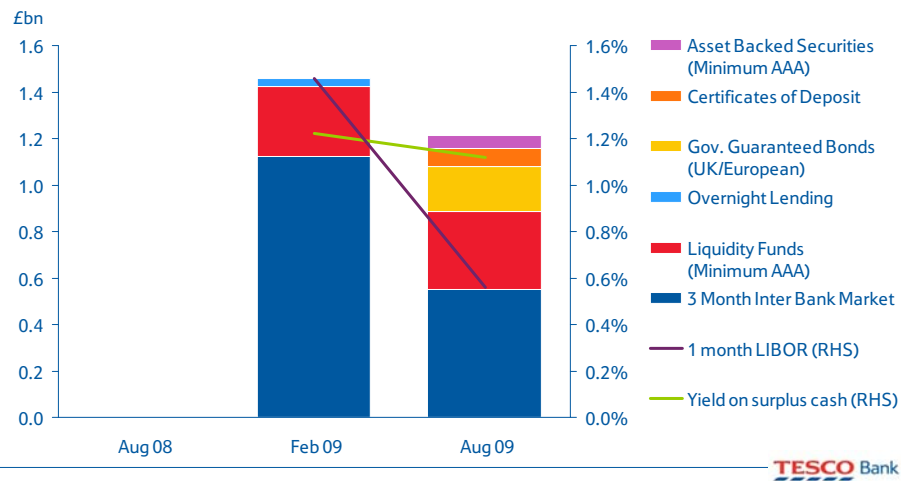
Of the £1.8bn liquid assets and short-term cash, £501m is held in highly liquid UK Treasury Bills. These are held to satisfy our FSA liquidity requirements

The remainder is invested in a variety of high quality assets

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## Surplus cash / investment portfolio

- While market interest rates have fallen, our yield on surplus cash has been maintained through active management and diversification of the portfolio whilst adopting a conservative position on risk



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## Managing interest rate risk

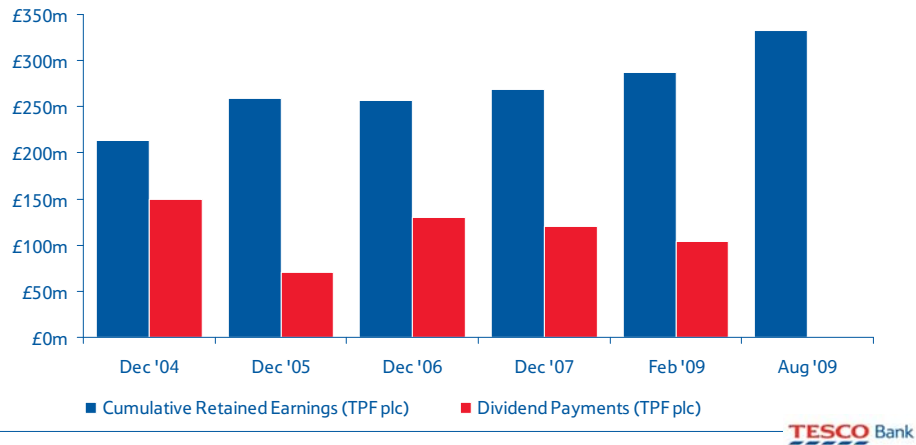
- Tesco Bank does not speculate on movements in interest rates
  - We do not run a trading book
- Our main interest rate risk comes from the sale of personal loans
  - Interest received is fixed, but our funding cost is variable
- To ensure stable margins, we manage this interest rate risk using swaps

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## The capital position – Tesco Personal Finance plc

- Tesco Bank has strong and stable capital ratios
- Retained earnings can contribute significant funds for further expansion

31 August 2009	£m	%
Tier 1 capital	574	12.6
Total capital	538	11.8



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The P&L

## The Profit & Loss account

- Current year profitability is being impacted by higher bad debts and increased costs

Pro Forma year to 28 Feb 2009 £m		Half year to 31 Aug 2009 £m
185	Net-interest income	156
443	Non-interest income	203
<b>627</b>	<b>Total income</b>	<b>359</b>
272	Expenses*	152
134	Bad and doubtful debts	92
<b>222</b>	<b>Operating profit/loss before amortisation</b>	<b>115</b>
32	Amortisation on intangibles arising on acquisition	62
<b>189</b>	<b>Profit before tax</b>	<b>53</b>

\* For consistency with Aug. 09 reporting, the proforma year to 28 Feb. 09 P&L includes ATM minority interest payable to Tesco Group of £25m within the expenses line

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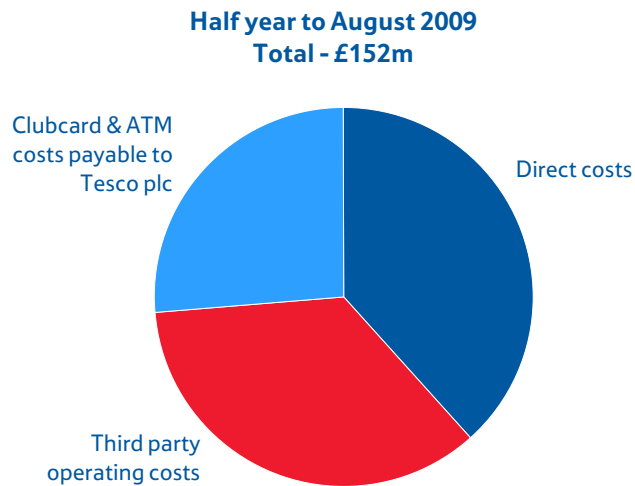
## Income

Net interest income	Half year to Aug 2009 £m	Non-interest income	Half year to Aug 2009 £m
Interest receivable and similar income:		ATMs	66
– Credit cards	103	Credit cards and loans	68
– Loans	105	Insurance	69
– Other	(3)	<b>Non-interest income</b>	<b>203</b>
<b>Total interest income</b>	<b>205</b>		
Interest payable:			
– Savings accounts	(46)		
– Other	(3)		
<b>Net interest income</b>	<b>156</b>		

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## Operating expenses



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## Accounting for motor and home insurance pre/post Fortis – P&L

Current Operating Model		Future Operating Model		
RBS Insurance (Underwriter)	Tesco Bank (Introducer)		Tesco Bank (Sales & Distribution)	Tesco Insurance (Underwriter)
✓		Insurance premium	✓ (Commission)	✓ (Net premium)
✓		Add-on income	✓	
✓		Cost of reinsurance		✓
✓		Investment income		✓
✓		Operating costs	✓	✓
✓		Marketing costs	✓	
✓		Insurance claims		✓
	✓	Profit / Commission	✓	✓

49.9% of Tesco Insurance will be equity accounted in Tesco Bank

Note: Shaded areas do not impact the Tesco Bank P&L

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## Accounting for motor and home insurance pre/post Fortis – balance sheet and capital

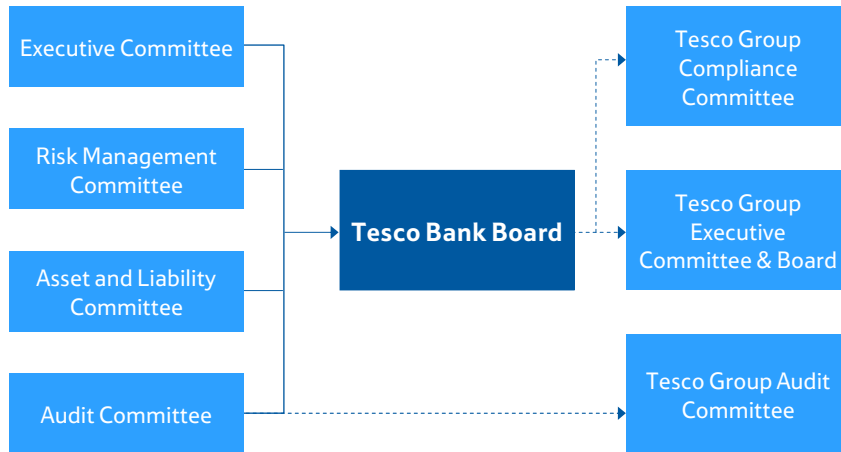
<b>Balance Sheet</b>	<ul style="list-style-type: none"><li>• Insurance reserves and funds invested are currently in RBS Insurance</li><li>• In future they will be in the jointly owned underwriter with Fortis</li><li>• There is a limited impact on TPF Group, being our share of net assets of the joint underwriter and the cash flows arising from premium collection</li></ul>
<b>Capital</b>	<ul style="list-style-type: none"><li>• TPF currently provides a £259m loan to RBS Insurance as a proxy for capital</li><li>• This will be repaid when RBS Insurance capital requirement runs off</li><li>• We will inject 49.9% of capital required into the new joint underwriter with Fortis</li></ul>
<b>TPF plc Capital Ratio</b>	<ul style="list-style-type: none"><li>• Currently the loan to RBS Insurance is a deduction in arriving at the Total Capital Ratio</li><li>• In future, the investment in the joint underwriter will be a deduction</li></ul>

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Managing Risk

## Risk framework and organisation



## Key risks



## Credit risk management and the customer journey

### Acquire

Criteria set to take on good quality, profitable business

### Monitor and Manage

Customer accounts are constantly monitored

### Collect

When a customer misses a payment, they move to the collection process with the aim of bringing customers back up-to-date

### Recover

When a customer enters the recovery process our objective is to recover cash.  
Customers move to the recovery process for a number of reasons.

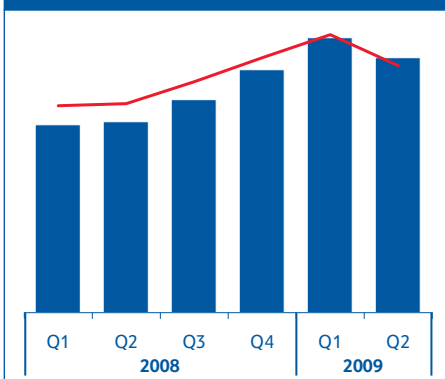
Examples include:

- 4 missed payments
- Bankruptcy

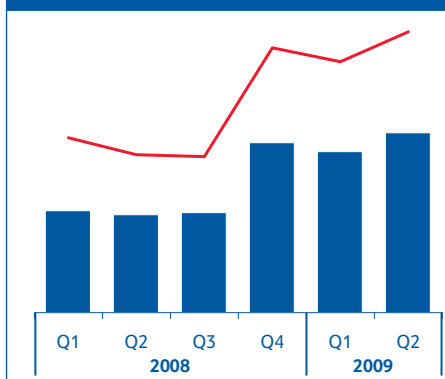
## Bad debts – default balances and rates

- Bad debt flows deteriorated during the second half of 2008 but have stabilised in 2009, albeit at a higher level

### Credit cards



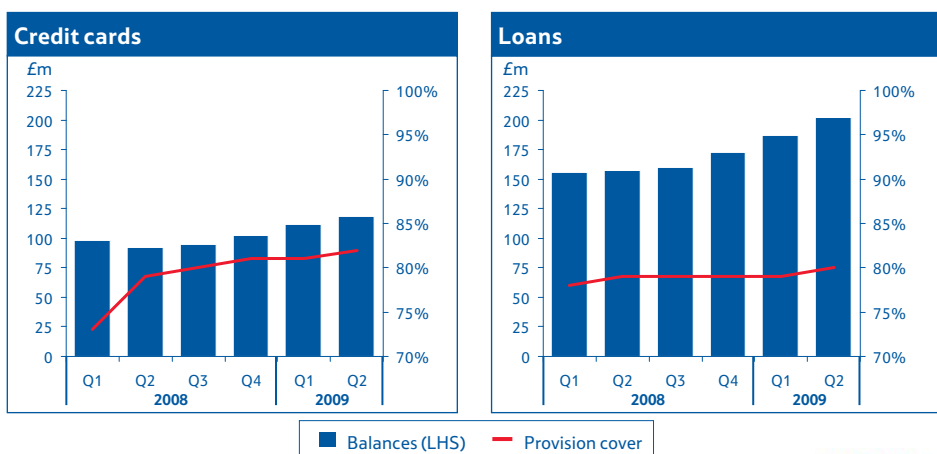
### Loans



■ Balance — Rate

## Bad debt provisions

- Provisions cover over 80% of balances where customers have defaulted
- The percentage cover has grown modestly as we experience lower cash recovery from customers



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## New business asset quality

- During the first half of 2009, Tesco Bank has gained market share in both credit cards and personal loans
- New business asset quality has improved
  - The credit card offer has been repositioned
  - Loans competitive positioning has improved
  - Credit policy has tightened

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The TESCO logo is displayed in red, bold, uppercase letters. Below the text are three horizontal blue lines of varying lengths, creating a stylized underline effect.

## Summary

### **Summary**

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- Simple balance sheet structure
- Strong liquidity and funding position
- Well capitalised
- Good spread of income and profit
- Corporate governance established and integrated to Tesco Group plc
- Well provisioned for bad and doubtful debts