

**NORTHERN ROCK PLC**  
**HALF YEAR RESULTS**  
**6 MONTHS ENDED 30 JUNE 2009**

# NORTHERN ROCK GROUP HALF YEAR RESULTS

4 August 2009

## OVERVIEW

Northern Rock plc today issued its Half Year Results for the six months ended 30 June 2009. The Company is progressing against its revised business plan and is on track for delivery of its legal and capital restructure.

## KEY POINTS

### Legal and Capital Restructure

- Plans for legal and capital restructure are progressing well, with completion expected before the end of 2009, subject to European Commission (EC) and Financial Services Authority (FSA) approval
- The intention is to split Northern Rock into two separate entities, BankCo and AssetCo
- Northern Rock continues to support the Government in its revised application for State aid

### Earnings

- Underlying loss reduced to £269.6 million for the six months to 30 June 2009, compared with an underlying loss of £443.3 million in the first half of 2008, despite incurring a loan loss impairment charge of £602.2 million
- The main drivers of the reduced underlying loss are improved underlying net interest income and a significant reduction in total costs incurred
- Statutory loss before tax for six months to 30 June 2009 of £724.2 million - including a hedge accounting volatility charge of £298.2 million and £156.4 million being the rebate for charges of Government funding and guarantee costs expected to be received upon approval of State aid from the EC

### Lending

- Gross residential lending of £1.3 billion in the first half of 2009, with a pipeline of residential lending of £1.2 billion at 30 June 2009
- Selective mortgage retention programme successfully launched in June 2009
- Northern Rock's new lending in 2009 is likely to be nearer to £4 billion than the previously envisaged £5 billion, reflecting its constrained capital position prior to completion of the legal and capital restructure
- Once the restructure and capital injection has completed (which is subject to EC approval), Northern Rock will start to increase its new lending
- All lending will be made responsibly and will be carefully underwritten on commercial terms

### Retail funding

- Retail deposits of £18.4 billion at 30 June 2009, compared with £19.6 billion at 31 December 2008 and £14.2 billion at 30 June 2008
- The net outflow reflects increased market competition, along with a more normalised customer view of the savings market and Northern Rock's place within the market
- Northern Rock continues to compete in the retail savings market within the constraints of its self-imposed competitive framework

### Government Loan

- Net borrowings provided by the Government are £10.9 billion, compared with £8.9 billion at the end of December 2008, in line with revised plan and reflecting the cessation of the active redemption programme
- This represents gross amounts outstanding of £14.5 billion, less balances held for liquidity purposes at the Bank of England of £3.6 billion
- The Government loan will increase upon completion of the legal and capital restructure

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## **Credit Quality**

- Residential mortgage accounts over three months in arrears, including Together loans, have risen to 3.92%, compared with 3.67% at 31 March 2009 and 2.92% at 31 December 2008
- Excluding Together, residential mortgage accounts over three months in arrears are 2.85% at 30 June 2009
- Northern Rock has seen improvements in early stage arrears (accounts under 3 months in arrears) in recent months

## **Assisting customers in difficulty**

- Northern Rock remains committed to assisting customers in difficulty wherever possible, via innovative mortgage rescue solutions and involvement in Government schemes
- Stock of properties in possession has fallen to 2,522, compared with 3,620 at 31 December 2008
- This reduction reflects the actions taken to assist customers in difficulty to stay in their homes and increased sales, at best price, of repossessed properties in the best interests of both customers and the Company

## **Capital**

- As announced on 1 July 2009, the Company's capital base has reduced to a level below its minimum regulatory capital requirement
- Until the legal and capital restructure is implemented the FSA has confirmed that it does not currently intend to restrict the activities of the Company

## **Northern Rock Foundation**

- Donation to The Northern Rock Foundation of £7.5 million in the first half of 2009, with total payments made since 1997 of £213 million

## **Gary Hoffman, Chief Executive of Northern Rock commented:**

“The current environment continues to be challenging, however, against this backdrop Northern Rock is making progress against its revised plan and has delivered results in line with expectations. We anticipate receiving State aid approval in the autumn and the legal and capital restructuring of the Company to be completed by the end of the year. This ultimately prepares for a return to the private sector.”

## **Further Information**

### **Press Contacts**

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## CHIEF EXECUTIVE'S STATEMENT

Northern Rock announced in February that it had concluded its strategic review, in close consultation with the Government, and agreed a revised business plan. The key features of the revised plan include:

- Supporting Government policy to increase lending capacity in the mortgage market.
- Slowing down the rate of mortgage redemptions and offering up to £14 billion of new mortgage lending in the next two years.
- Changing the repayment profile of the Government loan to reflect new mortgage lending and slower redemptions.
- Implementing a legal and capital restructure of the Company, which is designed to maximise capital efficiency and value for the taxpayer, and facilitate the new lending.

The Company has supported the Government's updated restructuring proposals included within the revised business plan notified to the European Commission (EC) for approval. The proposed restructuring, which is core to the business plan, is expected to complete in the second half of the year and will split the Company into two separate entities:

- **"BankCo"** – is proposed to be authorised by the Financial Services Authority (FSA) as a deposit taker and will undertake new lending. BankCo will hold the retail deposit book, wholesale deposits and a proportion of Northern Rock's unencumbered mortgage assets, together with Northern Rock's branches and mortgage origination capability.
- **"AssetCo"** – will hold the balance of the existing residential mortgage book, the vast majority of which is performing, including the Company's interest in those mortgages allocated to the Granite securitisation and covered bond programmes. AssetCo will also hold the existing Government loan to Northern Rock, plus Northern Rock's non-deposit wholesale funding instruments. AssetCo will not hold any retail deposits and, subject to FSA approval, will be regulated as a mortgage lender with a lower regulatory capital requirement.

The proposed structure offers the most capital efficient solution, with an additional capital requirement, for BankCo and AssetCo combined, of no more than £3 billion, as previously announced in August 2008.

Implementation of the proposed restructuring is conditional on EC and FSA approval.

### Financial Performance

Northern Rock recorded a reduced underlying loss of £269.6 million in the first half of 2009, including a loan loss impairment charge of £602.2 million. This compares with an underlying loss in the first half of 2008 of £443.3 million, and £849.7 million in the second half of 2008. The main drivers of the reduced underlying loss were improved underlying net interest income, reflecting the lower interest rate environment, a reduced impairment charge for Treasury assets and a reduction in exceptional costs incurred. The statutory loss before tax was £724.2 million (30 June 2008 - £585.4 million).

As planned, the rate of repayment of the gross Government loan slowed reflecting the revised business strategy, and particularly the slow down in the rate of mortgage redemptions.

### New Lending and Funding

Gross residential mortgage lending in the first half of the year amounted to £1.3 billion. The value of mortgage applications doubled in the second quarter of 2009, compared with the first quarter, and the Company carries a pipeline of new business yet to complete of £1.2 billion into the second half of 2009. The quality of new mortgage lending remains good with an average loan to value ratio of 57% in the first half.

Northern Rock's new lending in 2009 is likely to be nearer to £4 billion than the previously envisaged £5 billion, reflecting its constrained capital position prior to completion of the legal and capital restructure. Once the restructure and capital injection has completed (which is subject to EC and FSA approval), Northern Rock

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expects to increase its new lending. All lending will be made responsibly and will be affordable for customers. It will be carefully underwritten on commercial terms.

Retail funding balances at 30 June 2009 were £18.4 billion compared with £19.6 billion at 31 December 2008. The reduction in balances reflects lower retail funding inflows as a result of increased competition in the retail savings market, along with a more normalised customer view of the savings market and Northern Rock's place within the market. The Company continues to compete in the retail savings market within the constraints of its self-imposed competitive framework.

### **Assisting Customers in Difficulty**

Northern Rock recognises that many of its customers are impacted by the current difficult economic environment. Northern Rock is committed to assisting customers in difficulty wherever possible and has invested heavily in its debt management capabilities. It has more than doubled the number of staff within its debt management operations over the last year, with a primary focus being on increasing the level of customer contact. Customer engagement is key to maximising dialogue and ensuring that realistic and sustainable payment arrangements can be achieved.

Northern Rock has made a specific commitment to not take possession of a property until at least six months after the first arrears event and many customers have taken advantage of its innovative mortgage rescue solutions to enable them to remain in their homes wherever possible. Northern Rock has also actively engaged in the design and improvement of Government rescue schemes, which complement its range of internal solutions.

At 30 June 2009, properties in possession decreased to 2,522, representing 0.45% of accounts, compared with 3,620 (0.61%) at the end of 2008. This reflects the actions taken to assist customers in difficulty to stay in their homes and an increase in the rate of sales of repossessed properties. The vast majority of sales are made through Estate Agents as the Company attempts to secure the best price in customers' and its own best interests.

### **Outlook**

The outlook for the UK mortgage and housing market remains uncertain. The level of housing transactions remains relatively muted although there are some signs that the rate of reductions in house prices has moderated in recent months. Northern Rock expects the loan loss impairment charge in the second half of 2009 to be broadly similar to the first half of the year and then to start reducing in 2010. The impairment charge going forward will be influenced by changes in house prices and the levels of unemployment.

Lower interest rates have resulted in improved affordability for mortgage customers, but confidence remains finely balanced reflecting expectations for increased unemployment in the coming months. The current environment continues to present Northern Rock with challenges particularly in managing the quality of its loan portfolios. However, against this backdrop Northern Rock's progress is encouraging.

Northern Rock anticipates that State aid approval will be obtained from the EC during autumn 2009 which will enable the legal and capital restructure and recapitalisation of the Company to be completed before the end of the year. The restructuring of the Company is progressing in a satisfactory manner and will ultimately enable a return to the private sector.

**Gary Hoffman**  
**Chief Executive**  
**4<sup>th</sup> August 2009**

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## OPERATIONAL & FINANCIAL PERFORMANCE

### Introduction / Description of Business

Northern Rock's core business is secured residential lending, which comprises over 90% by value of loans to customers. The balance of loans to customers includes a portfolio of personal unsecured loans and a small portfolio of secured commercial loans. The distribution network consists of over 70 branches, plus postal, telephone and internet operations. The Company also uses the UK financial intermediary market to distribute products to customers.

The review of Operational & Financial Performance includes details of the principal risks and uncertainties for the remaining six months of the financial year.

### Market Conditions

The UK residential mortgage market remained subdued in the first half of 2009, with gross residential lending of £67 billion, compared with £151 billion in the equivalent period in 2008. Net residential lending also fell to £3 billion in the first six months of the year compared with £30 billion in the equivalent period in 2008. Mortgage market conditions reflect low levels of housing transactions and a significant reduction in remortgage activity, reflecting the reduced incentive to remortgage due to low interest rates, reduced risk appetite by lenders and increased loan to value ratios following falls in house prices.

House prices have continued to fall in the first half of 2009, albeit there are signs of moderation in the rate of house price reductions in recent months. House prices have fallen by 2% in the six months to June 2009. This compares to a reduction of 12% in the 12 months to 30 June 2009, and a fall of 21% from the peak in Q3 2007.

### Loans to Northern Rock Customers

An analysis of changes to each loan portfolio is set out in the following table:

	<b>Residential £m</b>	<b>Commercial £m</b>	<b>Unsecured £m</b>	<b>Total £m</b>
<b>2009 1st Half</b>				
Gross lending	1,250	-	-	1,250
Redemptions	(5,434)	-	(770)	(6,204)
Net lending	(4,184)	-	(770)	(4,954)
Closing balances	62,360	292	4,489	67,141
<b>2008 Full Year</b>				
Gross lending	2,925	2	95	3,022
Redemptions	(26,571)	(24)	(1,830)	(28,425)
Net lending	(23,646)	(22)	(1,735)	(25,403)
Closing balances	66,700	302	5,298	72,300
<b>2008 1st Half</b>				
Gross lending	1,882	2	69	1,953
Redemptions	(15,191)	(19)	(1,035)	(16,245)
Net lending	(13,309)	(17)	(966)	(14,292)
Closing balances	77,362	299	6,330	83,991

Note: Gross and net lending represent net cashflows excluding fair value adjustments. Closing balances are stated including fair value adjustments. Net movements include asset disposals where appropriate.

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### **Residential Lending**

In the first six months of 2009 Northern Rock's gross residential lending was £1.3 billion (2008 first half - £1.9 billion). The quality of new mortgage lending remains good with an average loan to value ratio of 57%. The Company has seen an increase in the level of mortgage applications reflecting its increased appetite for new lending, with the value of mortgage applications in the second quarter of 2009 almost double the level of the first quarter. At 30 June 2009, the Company had a residential pipeline yet to complete of £1.2bn.

In February 2009, the Company announced that it intended, as part of its revised strategy, to lend up to £14 billion over the next two years, 2009 and 2010, including up to £5 billion in 2009. Reflecting its constrained capital position prior to completion of the legal and capital restructure and capital injection, Northern Rock's new lending in 2009 is expected to be nearer to £4 billion than the previously envisaged £5 billion.

Residential redemptions in the first six months of the year were £5.4 billion, compared with £15.2 billion in the first half of 2008. Reflecting its revised strategy the Company has taken steps to reduce the level of its mortgage redemptions, including no longer actively encouraging its customers to remortgage away at the end of their product.

The level of remortgages has also fallen reflecting the prevailing interest rate environment where there is currently little incentive for many customers to remortgage. The level of remortgages has also been limited by falls in house prices which has affected loan to value ratios and the reduced appetite for lending by mortgage lenders. In addition the Company has recently introduced a retention proposition for selected mortgage customers who might otherwise have remortgaged to another lender.

The average indexed loan to value of the residential mortgage book increased to 74% at 30 June 2009 (31 December 2008 - 73%). The proportion of residential mortgage loans with an indexed loan to value of over 100% at 30 June 2009 was 39% (31 December 2008 - 33%), largely driven by the Together book, but reduced interest rates have resulted in better affordability for customers.

### **Unsecured Lending**

Northern Rock's personal unsecured credit portfolios comprise the unsecured element of Together lending and standalone unsecured loans not linked to a residential mortgage. Northern Rock withdrew its unsecured lending products from the market in the first quarter of 2008. As a consequence, these portfolios will continue to run-off over time.

Balances of Together unsecured loans reduced to £2.5 billion at 30 June 2009, representing 56.1% of total unsecured loan balances (31 December 2008 - £2.7 billion, 51.3%). At 30 June 2009, standalone unsecured balances were £2.0 billion and represented 43.9% (31 December 2008 - £2.6 billion, 48.7%).

### **Commercial Lending**

Northern Rock's small residual commercial loan portfolio totalled £0.3 billion at 30 June 2009 (31 December 2008 - £0.3 billion). The Company has ceased offering new commercial loans and the book will run-off over time.

### **Credit Quality and Loan Loss Impairment**

#### **Assisting Customers in Difficulty**

Northern Rock is committed to assisting customers in difficulty wherever possible and has invested heavily in its debt management capabilities. It has more than doubled the number of staff within its debt management operations over the last year, with a primary focus being on increasing the level of customer contact. Customer engagement is key to maximising dialogue and ensuring that realistic and sustainable payment arrangements can be achieved.

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Northern Rock has made a specific commitment to not take possession of a property until at least six months after the first arrears event and many customers have taken advantage of its innovative mortgage rescue solutions to enable them to remain in their homes wherever possible. Northern Rock has also actively engaged in the design and improvement of Government rescue schemes, which complement its range of internal solutions.

At 30 June 2009, properties in possession decreased to 2,522, representing 0.45% of accounts, compared with 3,620 (0.61%) at the end of 2008. This largely reflects an increase in the rate of sales of repossessed properties. The vast majority of sales are made through Estate Agents as the Company attempts to secure the best price in customers' and its own best interests.

### Arrears

The arrears position of each of the Company's main personal loan portfolios based upon the number of accounts over three months in arrears is set out in the table below:

	<b>CML residential average</b>	<b>Northern Rock residential</b>	<b>Non- Together residential</b>	<b>Together secured residential</b>	<b>Together unsecured</b>	<b>Standalone unsecured</b>
<b>30 June 2009</b>	2.39% <sup>1</sup>	3.92%	2.85%	6.47%	5.46%	2.98%
<b>31 December 2008</b>	1.88%	2.92%	2.25%	4.53%	3.90%	2.87%
<b>30 June 2008</b>	1.21%	1.18%	0.80%	2.14%	2.06%	2.00%

Source: Northern Rock and Council of Mortgage Lenders (CML)

Note 1: CML figure for 2009 is as at 31 March 2009, being the latest available data

Residential arrears expressed as a percentage of the total number of residential mortgage customer accounts are as follows:

	<b>30 June 2009</b>		<b>30 June 2008</b>		<b>31 December 2008</b>	
	Cases	%	Cases	%	Cases	%
Over 3 - 6 months	9,699	1.72	5,605	0.85	10,264	1.74
Over 6 – 12 months	8,775	1.55	1,966	0.30	6,259	1.06
Over 12 months	3,667	0.65	225	0.03	741	0.12
<b>Total</b>	<b>22,141</b>	<b>3.92</b>	<b>7,796</b>	<b>1.18</b>	<b>17,264</b>	<b>2.92</b>

Total residential accounts (including both Together and non-Together loans) over three months in arrears at 3.92% were higher than the equivalent figure of 2.92% at the end of 2008. This increase has primarily been caused by the more difficult economic and market conditions and greater forbearance to customers in arrears. Northern Rock has seen signs of early stage arrears (accounts under 3 months in arrears) improving in recent months, although it is too early to say if this is an enduring trend.

Arrears over three months within the unsecured portfolios also increased due to the background economic environment and the contraction in the size of the books. Together unsecured arrears increased to 5.46% (31 December 2008 - 3.90%).

Standalone unsecured arrears on a reported basis increased to 2.98% (31 December 2008 - 2.87%). Within the standalone unsecured portfolio there are a number of loans where the Company has agreed to a reduced payment compared to the original contractual payment in an attempt to alleviate payment difficulties for the customer. If the customer maintains their payments in line with the agreed revised amount they are not considered to be in arrears and are not included within the reported figures. If arrears were to be restated to compare against the original contractual amount then standalone unsecured arrears would be 7.70% (31 December 2008 - 7.26%).

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Going forward, the Company will continue to actively manage the credit quality of the loan books, especially given the difficult mortgage market conditions and the associated challenges for some borrowers (for example those with higher loan to values) of moving to a new lender. Northern Rock will also continue to extend forbearance wherever possible to customers in financial difficulty who are willing to work with the Company to find a solution.

### Loan Loss Impairment

The charge for customer loan loss impairment in the first half of 2009 amounted to £602.2 million, compared with £191.6 million in the first half of 2008 and £702.8 million in the second half of 2008.

	<u>30 June</u> <u>2009</u> <u>£m</u>	6 months to <u>30 June</u> <u>2008</u> <u>£m</u>	<u>31 Dec</u> <u>2008</u> <u>£m</u>	Full year <u>2008</u> <u>£m</u>
<b>Impairment charge</b>				
Secured on residential property	223.3	55.5	308.5	364.0
Secured on residential buy to let property	59.4	18.9	30.0	48.9
Secured commercial	2.9	0.7	7.5	8.2
Unsecured	316.6	116.5	356.8	473.3
	<u>602.2</u>	<u>191.6</u>	<u>702.8</u>	<u>894.4</u>
% of mean advances to customers	1.70%	0.42%	1.78%	1.04%

Loan loss impairment provisions and coverage are set out in the following table:

	Residential	Commercial	Unsecured	Total
<b>30 June 2009</b>				
Impairment provisions, £m	487.8	10.7	519.3	1,017.8
% of closing balances	0.78%	3.53%	10.37%	1.49%
<b>31 December 2008</b>				
Impairment provisions, £m	378.3	7.8	483.6	869.7
% of closing balances	0.56%	2.52%	8.36%	1.19%

Impairment charges in the first half of 2009 are lower than the second half of 2008 reflecting the slowing rate of house price deflation and a reduction in the roll rate to repossession. The charge in the second half of the year is expected to be broadly similar to the first half of the year. The impairment charge going forward will be influenced by changes in house prices and levels of unemployment.

### Funding

Northern Rock traditionally had four funding arms comprising wholesale funding, securitisation, covered bonds and retail deposits. In addition to these sources of funding, since September 2007 the Company has had a loan facility with the Government.

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Flows of each funding channel and closing balances are shown in the following table:

	Retail £m	Wholesale £m	Securitisation £m	Covered Bonds £m	Government £m
<b>2009 1st Half</b>					
Net flow	(1,173)	(940)	(3,733)	(1,341)	(1,054)
Closing balances	18,404	11,214	30,555	9,466	14,529
<b>2008 Full Year</b>					
Net flow	9,044	(1,480)	(12,211)	-	(11,347)
Closing balances	19,623	12,924	37,987	12,550	15,583
<b>2008 1st Half</b>					
Net flow	3,680	(2,112)	(6,501)	-	(5,967)
Closing balances	14,197	10,775	37,657	9,403	20,963

Note: Net flows represent net cashflows excluding fair value adjustments. Closing balances are stated including fair value adjustments. Government funding excludes open market repo funding.

### Retail

Retail funding in the first six months of the year comprised a net outflow of £1.2 billion, compared with a net inflow of £5.4 billion in the second half of 2008. The outflow reflects increased competition in the retail savings market, and a more normalised customer view of the market and Northern Rock's place within it.

Closing retail balances comprised:

	30 June 2009 £m	30 June 2008 £m	31 December 2008 £m
Branch accounts	4,400	3,045	4,313
Postal accounts	7,104	5,995	7,496
Internet accounts	4,659	3,560	5,398
Offshore accounts	1,864	1,199	2,023
Other accounts	377	398	393
<b>Total retail balances</b>	<b>18,404</b>	<b>14,197</b>	<b>19,623</b>

Northern Rock has complied at all times with the commitments set out in its Competitive Framework, subsequent to its publication in March 2008. This Framework commits Northern Rock to:

- Not promote the Government guarantees
- Not sustain a prolonged presence as market leader
- Maintain market shares well below historic levels
- Achieve competitive differentiation through service and innovation
- Treat customers fairly and regularly monitor and review adherence to the Framework

The Competitive Framework also includes commitments to restrict the Company's share of retail deposits to no more than 1.5% in the UK and 0.8% in Ireland. At 30 June 2009, Northern Rock's estimated share of UK retail deposits was 1.4% and estimated share of Ireland deposits was 0.6%. During the course of the first six months, the Company has actively managed its product range to maintain balances within the parameters defined in the Competitive Framework.

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### Wholesale

Reported wholesale funding balances of £11.2 billion at 30 June 2009 include £4.8 billion of collateral placed with the Company in respect of interest and foreign exchange swaps. Excluding this collateral, wholesale balances have reduced during the first half of 2009 in line with contractual maturities.

### Securitisation

Securitisation is the process whereby Northern Rock, through the Granite programme, has previously raised wholesale funding secured on a segregated pool of mortgage assets. These assets are held in special purpose entities (SPEs) set up for this purpose, which are fully consolidated in Northern Rock's financial statements. Northern Rock retains an economic interest in the SPEs through a combination of subordinated loans and profit retained in the SPEs.

No new securitisation issues have completed since May 2007.

From November 2008 Granite has operated under pass-through. This means holders of Granite securities receive principal repayments based on principal received on the underlying mortgage assets within Granite, rather than receiving scheduled repayments. Northern Rock, as a beneficiary of the Granite mortgages trust, will not receive any distributions of principal in respect of the mortgage loans that have been securitised and are held in the Granite mortgages trust, until holders of Granite securities have been repaid in full.

At 30 June 2009, securitised notes in the Group balance sheet amounted to £30.6 billion (31 December 2008 - £38.0 billion). Balances of securitised funding at 30 June 2009 are affected by foreign currency movements, which increase both the reported funding balance and the value of the associated derivative financial instruments which hedge against these rate movements. Excluding these fair value amounts, securitised note balances were £26.9 billion at 30 June 2009 (31 December 2008 - £30.7 billion).

### Covered Bonds

Covered bonds are secured by a pool of ring-fenced residential mortgages. No additional funds were raised through the covered bond programme in the first half of 2009. The Company repaid £1.3 billion of maturing notes in the six months to 30 June 2009.

At 30 June 2009, covered bonds in the Group balance sheet amounted to £9.5 billion (31 December 2008 - £12.6 billion). Balances of covered bonds at 30 June 2009 are affected by foreign currency movements, which increase both the reported funding balance and the value of the associated derivative financial instruments which hedge against these rate movements. Excluding these fair value amounts, covered bonds balances were £7.3 billion at 30 June 2009 (31 December 2008 - £8.6 billion).

### Government Loan

Borrowings provided by the Government under the liquidity facility amounted to £15.6 billion at the start of 2009, which had reduced to £14.5 billion at 30 June 2009. On a net basis, after taking into account liquidity deposits held at the Bank of England the net loan increased from £8.9 billion at the beginning of the year to £10.9 billion at 30 June 2009. The net increase reflects the slowdown in redemptions, movement on retail deposits and maturities on all wholesale funding programmes. At the conclusion of the legal and capital restructuring the Government loan will increase.

	<b>30 June 2009 £bn</b>	<b>30 June 2008 £bn</b>	<b>31 December 2008 £bn</b>
Amount due to Government	14.5	21.0	15.6
Liquidity deposit accounts with Bank of England	(3.6)	(3.5)	(6.7)
	<b>10.9</b>	<b>17.5</b>	<b>8.9</b>

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The cost of the Government net funding and HM Treasury guarantees will be revised once approval for State aid is granted by the European Commission. This revision will be back-dated to 1 April 2008 with a retrospective adjustment made when State aid is approved. If the post State aid approval basis of charging had been applied in the first half of 2009 the reported loss before tax would have been reduced by £156.4 million, giving a cumulative adjustment to be recovered of £356.4 million to 30 June 2009.

# NORTHERN ROCK GROUP HALF YEAR RESULTS

## FINANCIAL PERFORMANCE

### Underlying Loss Before Tax

Statutory results include certain items which are not considered by management to represent part of the underlying performance of the Group in any one financial period. A reconciliation of statutory and underlying loss before tax is set out in the following table:

	30 June 2009 £m	Six months to 30 June 2008 £m	31 Dec 2008 £m	Full Year 2008 £m
<b>Statutory (loss) before taxation</b>	(724.2)	(585.4)	(770.5)	(1,355.9)
Accounting volatility on derivatives	298.2	78.1	(215.2)	(137.1)
Impact of State aid approval on the cost of Government funding and HM Treasury guarantees	156.4	64.0	136.0	200.0
<b>Underlying (loss) before taxation</b>	<b>(269.6)</b>	<b>(443.3)</b>	<b>(849.7)</b>	<b>(1,293.0)</b>

The underlying loss in the first half of 2009 has reduced by £580.1 million compared with the second half of 2008, reflecting a lower impairment charge on customer loans of £100.6 million, a lower impairment charge on Treasury assets of £252.3 million and improved underlying net interest income (see below). Compared with the first half of 2008, the underlying loss reduced by £173.7 million, mainly reflecting total costs reducing from £307.9 million to £117.9 million, driven by the high level of exceptional costs in 2008 incurred as part of the restructure and reorganisation of Northern Rock and strong control of administrative expenses. Higher underlying net interest income of £380.9 million was offset by a higher impairment charge on customer loans of £410.6 million.

### Summary Income Statement

The summary income statement for the six months to 30 June 2009, 30 June 2008 and 31 December 2008 and the 12 months to 31 December 2008 is as follows:

	30 June 2009 £m	Six months to 30 June 2008 £m	31 Dec 2008 £m	Full Year 2008 £m
Net interest income	74.2	(51.9)	102.8	50.9
Other income	(85.3)	12.6	190.9	203.5
<b>Total income</b>	<b>(11.1)</b>	<b>(39.3)</b>	<b>293.7</b>	<b>254.4</b>
Administrative expenses	(104.7)	(134.8)	(134.9)	(269.7)
Exceptional expenses	(5.7)	(165.6)	2.0	(163.6)
Donation to the Northern Rock Foundation	(7.5)	(7.5)	(7.5)	(15.0)
Total expenses	(117.9)	(307.9)	(140.4)	(448.3)
Impairment (charges) on loans and advances	(602.2)	(191.6)	(702.8)	(894.4)
Impairment credits / (charges) on unsecured investment loans	7.0	(46.6)	(221.0)	(267.6)
<b>(Loss) before taxation</b>	<b>(724.2)</b>	<b>(585.4)</b>	<b>(770.5)</b>	<b>(1,355.9)</b>
Taxation	(15.8)	19.9	26.3	46.2
<b>(Loss) for the year</b>	<b>(740.0)</b>	<b>(565.5)</b>	<b>(744.2)</b>	<b>(1,309.7)</b>

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### Total Income and Interest Margin and Spread

The following table shows net interest income, total income and interest ratios for the six months to 30 June 2009, 30 June 2008, 31 December 2008 and the 12 months to 31 December 2008:

	<b>30 June 2009 £m</b>	<b>Six months to 30 June 2008 £m</b>	<b>31 Dec 2008 £m</b>	<b>Full Year 2008 £m</b>
<b>Statutory</b>				
Net interest income	74.2	(51.9)	102.8	50.9
Other income	(85.3)	12.6	190.9	203.5
<b>Total income</b>	<b>(11.1)</b>	<b>(39.3)</b>	<b>293.7</b>	<b>254.4</b>
<b>Underlying</b>				
Net interest income	491.1	110.2	279.8	390.0
Other income	(47.6)	(7.4)	(65.3)	(72.7)
<b>Total income</b>	<b>443.5</b>	<b>102.8</b>	<b>214.5</b>	<b>317.3</b>
Interest margin (as reported)	0.15%	(0.13)%	0.25%	0.05%
Interest spread (as reported)	0.10%	(0.33)%	0.08%	(0.13)%
Interest margin (underlying)	1.12%	0.19%	0.63%	0.41%
Interest spread (underlying)	1.08%	0.00%	0.47%	0.23%

Underlying interest margin (which primarily excludes accounting volatility on derivatives and reflects the potential impact of State aid approval) at 1.12% and underlying interest spread at 1.08% for the six months to 30 June 2009 compare with 0.41% and 0.23% respectively for the 12 months to 31 December 2008. The increases primarily reflect the interest rate environment and the changing nature of the book as fewer customers remortgage to other mortgage lenders following the end of their product term.

### Accounting Volatility on Derivatives

Volatility in reported results arises from accounting volatility on derivative instruments that hedge risk exposure on an economic basis. Such accounting volatility, which will offset over time, arises due to fair value volatility on designated hedges or because hedge accounting has not been adopted or is not achievable on certain transactions. The Company manages its risk exposures on an economic basis and does not include such accounting volatility in the assessment of its underlying performance or in assessing the effectiveness of its derivative positions in any one financial period.

An analysis of volatility and other fair value gains and losses is set out below:

	<b>30 June 2009 £m</b>	<b>Six months to 30 June 2008 £m</b>	<b>31 Dec 2008 £m</b>	<b>Full Year 2008 £m</b>
Fair value hedge volatility	(234.0)	(84.6)	(0.8)	(85.4)
Cashflow hedge volatility	(15.0)	0.2	16.3	16.5
Hedge volatility included within interest margin	(249.0)	(84.4)	15.5	(68.9)
Fair value movements on derivatives not in hedge accounting relationships	(3,366.2)	1,226.0	8,239.7	9,465.7
Translation gains / (losses) on associated instruments	3,317.0	(1,219.7)	(8,040.0)	(9,259.7)
	(49.2)	6.3	199.7	206.0
<b>Total hedge ineffectiveness and other fair value gains and losses</b>	<b>(298.2)</b>	<b>(78.1)</b>	<b>215.2</b>	<b>137.1</b>

## NORTHERN ROCK GROUP HALF YEAR RESULTS

Northern Rock enters into derivative financial instruments for economic hedging purposes. Some of these are designated and accounted for as IAS 39 compliant fair value or cash flow hedge relationships. Where effective fair value hedge relationships can be established, the movement in the fair value of the derivative instrument is offset in full or in part by opposite movements in the fair value of the instrument being hedged. Any ineffectiveness arising from different movements in fair value will offset over time. Ineffectiveness is included within interest income or expense, as appropriate.

Where derivatives are economically effective for hedging purposes but cannot be included within effective IAS 39 compliant accounting hedge relationships, e.g. for instruments included in equity, the movement in their fair value is recorded within net trading expense. These are also excluded from management's view of operational performance as these fair value adjustments are not realised in the current accounting period. The same treatment applies to the revaluation at each balance sheet date of economically hedged foreign currency assets and liabilities.

During the first half of 2009 accounting volatility on derivative instruments resulted in a charge of £298.2 million compared with a gain of £215.2 million in the second half of 2008. Of the reversal seen between the first half of 2009 and the second half of 2008, over 70% represents the change in value of swaps on equity instruments due to changes in exchange rates and interest rates. Such swaps do not qualify for hedge accounting treatment and consequently there is no offsetting fair value movement on the underlying equity instruments. The balance of the reversal reflects volatility in exchange rates and interest rates across a range of derivatives entered into to minimise risk.

### **Social Responsibility - The Northern Rock Foundation**

Between 1997 and 2007, Northern Rock donated 5% of pre tax profit to The Northern Rock Foundation. Following Northern Rock entering temporary public ownership in 2008, a commitment was made that the Foundation would receive at least £15 million per year in 2008, 2009 and 2010. In the first half of 2009 the amount donated was £7.5 million (2008 first half - £7.5 million). This results in £213 million having been paid since the Foundation's inception in 1997. Such donations are used to support community and charitable causes mainly, but not exclusively, in the North East of England and Cumbria.

Further information on The Northern Rock Foundation is available on the Company's website.

### **Capital**

During the first half of 2009 the FSA continued to waive the limits on use by the Company of Tier 2 capital. This meant that all available Tier 2 capital was included within capital resources without restriction for the purposes of meeting the Company's minimum regulatory capital requirement.

As announced on 1 July 2009 Northern Rock's capital base has now reduced to a level below its minimum regulatory capital requirement. Northern Rock proposes to address this situation through the legal and capital restructuring of the Company and HM Treasury's commitment to provide an adequate level of capital for the Company to meet its regulatory capital requirement, once the proposed restructuring is completed and subject to appropriate State aid clearance being obtained from the European Commission.

As the Company announced on 26 June 2009, the proposed restructuring will split the Company into two separate entities - BankCo and AssetCo - and is designed to achieve an efficient capital position which meets the applicable regulatory capital requirements and deliver value for money for taxpayers. Implementation of the proposed restructuring is conditional on European Commission approval and is expected to complete by the end of the year. The proposed structure offers the most capital efficient solution, with an additional capital requirement, for BankCo and AssetCo combined, of no more than £3 billion, as previously announced in August 2008.

The FSA has confirmed that it does not currently intend to restrict the activities of the Company while the plan is implemented to address its capital position. The FSA will continue to monitor the firm's position closely.

# NORTHERN ROCK GROUP HALF YEAR RESULTS

## FINANCIAL INFORMATION

### CONSOLIDATED INCOME STATEMENT

	<u>Note</u>	Six months to 30 June		Full year
		<u>2009</u>	<u>2008</u>	<u>2008</u>
		<u>(Unaudited)</u>	<u>(Unaudited)</u>	<u>(Audited)</u>
		<u>£m</u>	<u>£m</u>	<u>£m</u>
<b>Interest and similar income</b>		1,119.6	2,967.0	5,706.9
<b>Interest expense and similar charges</b>		(1,045.4)	(3,018.9)	(5,656.0)
<b>Net interest income</b>	2	74.2	(51.9)	50.9
Fee and commission income		(12.7)	35.7	55.9
Fee and commission expense		(24.3)	(22.3)	(59.3)
Other operating income		12.0	0.4	4.2
Losses on available for sale securities	3	(11.1)	(17.8)	(9.0)
Gains on disposal of loan books	4	-	39.3	49.1
Net trading (expense)/income	5	(49.2)	(22.7)	162.6
		(85.3)	12.6	203.5
<b>Total income</b>		(11.1)	(39.3)	254.4
Exceptional administrative expenses and restructuring costs		(4.7)	(130.0)	(141.5)
Exceptional impairment credits/(charges) on property, plant and equipment		5.4	(6.8)	23.6
Provisions for onerous contracts		(0.1)	(1.7)	(18.5)
Exceptional impairment charges on intangible assets		-	(27.1)	(27.2)
Strategic project development		(6.3)	-	-
	6	(5.7)	(165.6)	(163.6)
Administrative expenses	6	(93.6)	(124.8)	(247.8)
Depreciation and amortisation	6	(11.1)	(10.0)	(21.9)
Covenant to The Northern Rock Foundation		(7.5)	(7.5)	(15.0)
Operating expenses		(117.9)	(307.9)	(448.3)
Impairment losses on loans and advances	7	(602.2)	(191.6)	(894.4)
Impairment credits/(losses) on investment securities reclassified as loans and receivables and unsecured investment loans	3	7.0	(46.6)	(267.6)
<b>Loss before taxation</b>		(724.2)	(585.4)	(1,355.9)
Income tax (expense)/credit	8	(15.8)	19.9	46.2
<b>Loss for the period</b>		(740.0)	(565.5)	(1,309.7)
Attributable to:				
Appropriations	9	30.9	26.7	68.3
Loss attributable to equity shareholders		(770.9)	(592.2)	(1,378.0)
<b>Total</b>		(740.0)	(565.5)	(1,309.7)

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Six months to 30 June		Full year
	<u>2009</u>	<u>2008</u>	<u>2008</u>
	<u>(Unaudited)</u>	<u>(Unaudited)</u>	<u>(Audited)</u>
	<u>£m</u>	<u>£m</u>	<u>£m</u>
Loss for the period	(740.0)	(565.5)	(1,309.7)
<b>Other comprehensive income</b>			
Net movement in available for sale reserve	128.3	(240.5)	(531.5)
Net movement in cash flow hedge reserve	105.2	116.2	(240.5)
Actuarial gains and losses	(32.3)	(0.9)	25.5
Tax effects of the above	8.8	(2.4)	15.6
	<u>210.0</u>	<u>(127.6)</u>	<u>(730.9)</u>
Total comprehensive income and expense for the period	<u>(530.0)</u>	<u>(693.1)</u>	<u>(2,040.6)</u>
Attributable to:			
Appropriations	30.9	26.7	68.3
Comprehensive income and expense attributable to equity shareholders	(560.9)	(719.8)	(2,108.9)
Total	<u>(530.0)</u>	<u>(693.1)</u>	<u>(2,040.6)</u>

# NORTHERN ROCK GROUP HALF YEAR RESULTS

## CONSOLIDATED BALANCE SHEET

	<u>Note</u>	<b>30 June 2009 (Unaudited) £m</b>	<b>30 June 2008 (Unaudited) £m</b>	<b>31 December 2008 (Audited) £m</b>
<b>Assets</b>				
Cash and balances with central banks	10	6,666.9	3,559.4	9,336.8
Derivative financial instruments		6,724.0	3,923.5	13,314.4
Loans and advances to banks		3,386.7	2,217.4	3,384.4
Loans and advances to customers	11	67,141.3	83,990.4	72,299.4
Fair value adjustments of portfolio hedging		1,251.4	(561.6)	1,701.9
Investment securities and unsecured investment loans	12	3,129.8	5,530.6	3,809.2
Intangible assets		59.9	68.9	64.9
Property, plant and equipment		176.0	193.7	198.4
Current tax asset		38.2	3.2	21.8
Deferred income tax asset		-	-	35.2
Retirement benefit asset		8.4	3.1	31.7
Other assets		34.4	30.4	32.9
Prepayments and accrued income		128.8	52.9	115.0
<b>Total assets</b>		<b>88,745.8</b>	<b>99,011.9</b>	<b>104,346.0</b>
<b>Liabilities</b>				
Loans from Government	14	14,528.6	21,246.0	15,583.4
Deposits by banks		5,158.9	1,517.6	4,625.1
Customer accounts	15	19,601.8	14,565.4	20,722.7
Derivative financial instruments		1,922.1	1,251.0	2,220.8
Debt securities in issue				
Securitised notes	16	30,554.9	37,657.1	37,986.9
Covered bonds	13, 16	9,465.5	9,402.7	12,550.3
Other	16	4,856.6	8,889.8	7,199.1
Other liabilities		105.2	63.2	82.6
Accruals and deferred income		841.4	895.9	949.4
Deferred income tax liability		3.0	9.2	6.9
Provisions for liabilities and charges		14.0	46.8	18.5
Subordinated liabilities		1,396.3	1,249.8	1,514.9
Tier one notes		224.8	196.4	251.8
		<b>88,673.1</b>	<b>96,990.9</b>	<b>103,712.4</b>
<b>Equity</b>				
<b>Shareholders' funds</b>				
Called up share capital				
Ordinary		123.9	123.9	123.9
Preference		0.1	0.1	0.1
Share premium account				
Ordinary		6.8	6.8	6.8
Preference		396.4	396.4	396.4
Capital redemption reserve		7.3	7.3	7.3
Other reserves				
Revaluation reserve – available for sale investments	17	(473.4)	(312.6)	(602.5)
Hedging reserve – cash flow hedges		(164.5)	62.7	(269.7)
Retained earnings		(859.7)	700.6	(64.5)
<b>Total equity attributable to equity shareholders</b>		<b>(963.1)</b>	<b>985.2</b>	<b>(402.2)</b>
<b>Non shareholders' funds</b>				
Reserve capital instruments		299.3	299.3	299.3
Subordinated notes		736.5	736.5	736.5
<b>Total non shareholders' funds</b>		<b>1,035.8</b>	<b>1,035.8</b>	<b>1,035.8</b>
<b>Total equity</b>		<b>72.7</b>	<b>2,021.0</b>	<b>633.6</b>
<b>Total equity and liabilities</b>		<b>88,745.8</b>	<b>99,011.9</b>	<b>104,346.0</b>

# NORTHERN ROCK GROUP HALF YEAR RESULTS

## CONSOLIDATED STATEMENT OF CASH FLOWS

	Six months to 30 June		Full year
	<u>2009</u>	<u>2008</u>	<u>2008</u>
	<u>(Unaudited)</u>	<u>(Unaudited)</u>	<u>(Audited)</u>
	<u>£m</u>	<u>£m</u>	<u>£m</u>
<b>Net cash (outflow)/inflow from operating activities</b>			
Loss before taxation	(724.2)	(585.4)	(1,355.9)
Adjusted for:			
Depreciation and amortisation	11.1	10.0	21.9
Exceptional impairment (credits)/charges on property, plant and equipment	(5.4)	6.8	(23.6)
Exceptional impairment charges on intangible assets	-	27.1	27.2
Impairment losses on loans and advances	602.2	191.6	894.4
Impairment (credits)/losses on investment securities reclassified as loans and receivables and unsecured investment loans	(7.0)	46.6	267.6
Income taxes refunded	4.5	96.5	91.8
Fair value adjustments on financial instruments	260.0	485.0	(604.4)
Other non cash movements	328.9	280.4	333.5
Net cash inflow/(outflow) from operating losses before changes in operating assets and liabilities	<u>470.1</u>	<u>558.6</u>	<u>(347.5)</u>
<b>Changes in operating assets and liabilities</b>			
Net (increase)/decrease in deposits held for regulatory or monetary control purposes	(11.9)	38.2	16.9
Net decrease in loans and advances	4,911.8	14,200.1	24,852.0
Net decrease/(increase) in derivative financial instruments receivable	6,590.4	(1,682.5)	(11,073.4)
Net increase in other assets	(15.3)	(13.7)	(78.3)
Net decrease in debt securities in issue	(12,811.2)	(5,464.7)	(4,728.9)
Net decrease in loans from Government	(1,054.8)	(7,227.0)	(12,889.6)
Net increase in deposits from other banks	533.8	773.5	3,881.0
Net (decrease)/increase in customer accounts	(1,071.5)	3,010.3	9,044.4
Net (decrease)/increase in derivative financial instruments payable	(298.7)	(492.4)	477.4
Net increase/(decrease) in other liabilities	22.6	(3.1)	16.3
Net decrease in accruals and deferred income	(108.0)	(67.0)	(13.5)
Net cash (outflow)/inflow from operating activities	<u>(2,842.7)</u>	<u>3,630.3</u>	<u>9,156.8</u>
<b>Net cash inflow from investing activities</b>			
Net investment in intangible assets	(0.9)	(12.2)	(14.7)
Net investment in property, plant and equipment	22.6	(14.5)	5.7
Purchase of securities	(9.8)	(24.7)	(126.7)
Proceeds from sale and redemption of securities	51.6	757.9	2,424.9
	<u>63.5</u>	<u>706.5</u>	<u>2,289.2</u>
<b>Net cash outflow from financing activities</b>			
Appropriations (including tax of £nil, 30 June 2008 - £1.3m, 31 December 2008 - £3.2m)	(30.9)	(28.0)	(71.5)
	<u>(30.9)</u>	<u>(28.0)</u>	<u>(71.5)</u>
Net (decrease)/increase in cash and cash equivalents	<u>(2,810.1)</u>	<u>4,308.8</u>	<u>11,374.5</u>
Opening cash and cash equivalents	12,810.4	1,435.9	1,435.9
Closing cash and cash equivalents	<u>10,000.3</u>	<u>5,744.7</u>	<u>12,810.4</u>

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (Unaudited)

Note	Called up share capital £m	Share premium account £m	Capital redemption reserve £m	Other reserves £m	Retained earnings £m	Total shareholders' funds £m	Non shareholders' funds £m	Total equity £m
<b>Six months ended 30 June 2009</b>								
Balance at 1 January 2009	124.0	403.2	7.3	(872.2)	(64.5)	(402.2)	1,035.8	633.6
Net movement in available for sale reserve	-	-	-	128.3	-	128.3	-	128.3
Net movement in cash flow hedge reserve	-	-	-	105.2	-	105.2	-	105.2
Actuarial gains and losses	-	-	-	-	(32.3)	(32.3)	-	(32.3)
Tax effects of the above	-	-	-	0.8	8.0	8.8	-	8.8
Loss for the period	-	-	-	-	(770.9)	(770.9)	30.9	(740.0)
Appropriations	-	-	-	-	-	-	(30.9)	(30.9)
<b>Balance at 30 June 2009</b>	<b>124.0</b>	<b>403.2</b>	<b>7.3</b>	<b>(637.9)</b>	<b>(859.7)</b>	<b>(963.1)</b>	<b>1,035.8</b>	<b>72.7</b>

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (Unaudited)

Note	Called up share capital £m	Share premium account £m	Capital redemption reserve £m	Other reserves £m	Retained earnings £m	Total shareholders' funds £m	Non shareholders' funds £m	Total equity £m
<b>Six months ended 30 June 2008</b>								
	124.0	403.2	7.3	(122.9)	1,251.9	1,663.5	1,035.8	2,699.3
Balance at 1 January 2008	-	-	-	(240.5)	-	(240.5)	-	(240.5)
Net movement in available for sale reserve	-	-	-	116.2	-	116.2	-	116.2
Net movement in cash flow hedge reserve	-	-	-	-	(0.9)	(0.9)	-	(0.9)
Actuarial gains and losses	-	-	-	(2.7)	0.3	(2.4)	-	(2.4)
Tax effects of the above	-	-	-	-	(592.2)	(592.2)	26.7	(565.5)
Loss for the period	-	-	-	-	-	-	(26.7)	(26.7)
Appropriations	-	-	-	-	41.5	41.5	-	41.5
Movement in own shares	18	-	-	-	-	-	-	-
<b>Balance at 30 June 2008</b>	<b>124.0</b>	<b>403.2</b>	<b>7.3</b>	<b>(249.9)</b>	<b>700.6</b>	<b>985.2</b>	<b>1,035.8</b>	<b>2,021.0</b>

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (Audited)

Note	Called up share capital £m	Share premium account £m	Capital redemption reserve £m	Other reserves £m	Retained earnings £m	Total shareholders' funds £m	Non shareholders' funds £m	Total equity £m
<b>Year ended 31 December 2008</b>								
	124.0	403.2	7.3	(122.9)	1,251.9	1,663.5	1,035.8	2,699.3
Balance at 31 December 2007	-	-	-	(531.5)	-	(531.5)	-	(531.5)
Net movement in available for sale reserve	-	-	-	(240.5)	-	(240.5)	-	(240.5)
Net movement in cash flow hedge reserve	-	-	-	-	25.5	25.5	-	25.5
Actuarial gains and losses	-	-	-	22.7	(7.1)	15.6	-	15.6
Tax effects of the above	-	-	-	-	(1,378.0)	(1,378.0)	68.3	(1,309.7)
Loss for the year	-	-	-	-	-	-	(68.3)	(68.3)
Appropriations	-	-	-	-	43.2	43.2	-	43.2
Movement in own shares	18	-	-	-	-	-	-	-
<b>Balance at 31 December 2008</b>	<b>124.0</b>	<b>403.2</b>	<b>7.3</b>	<b>(872.2)</b>	<b>(64.5)</b>	<b>(402.2)</b>	<b>1,035.8</b>	<b>633.6</b>

# NORTHERN ROCK GROUP HALF YEAR RESULTS

## NOTES TO THE RESULTS

### **1. Basis of Preparation**

#### **Principles underlying going concern assumption**

The financial statements have been prepared on a going concern basis. The validity of this assumption depends on the European Commission approving the financing facilities provided by HM Treasury. If approval is not received it is likely the Company would then submit a solvent wind down plan for European Commission State aid approval. If State aid were not forthcoming the financing facilities may be withdrawn in which case the Company may not be able to meet its financial obligations as they fall due. The Company may then have to take appropriate insolvency proceedings and cease to trade as a going concern. Consequently this outstanding approval indicates the existence of a material uncertainty which may cast significant doubt about the Company's ability to continue as a going concern. The financial statements do not include adjustments that would result if the Company was unable to continue as a going concern. If the Company were unable to continue as a going concern, adjustments may have to be made to reduce the monetary value of assets to recoverable amounts, to provide for further liabilities that might arise and reclassify all assets and liabilities as current assets and liabilities.

In July 2008, the Company requested and was subsequently granted a waiver from the Financial Services Authority (FSA) in relation to its regulatory capital position. The FSA agreed to waive the limits on the Company's use of Tier 2 capital. The waiver enabled all available Tier 2 capital to be included within the Company's capital resources, without restriction, for the purposes of meeting its minimum regulatory capital requirements. The waiver expired in December 2008, and subsequently the FSA granted two other such waivers, the last of which expired on 30 June 2009.

The Company's capital base has now reduced to a level below its minimum regulatory capital requirement. The Company proposes to address this situation through a legal and capital restructuring and HM Treasury's commitment to provide an adequate level of capital for the Company to meet its regulatory capital requirements, once the proposed restructuring is completed and subject to State aid clearance being obtained from the European Commission.

In the period prior to the provision of further capital, the Company will continue to operate as normal. The FSA has confirmed that it does not currently intend to restrict the activities of the Company while the plan is implemented to address its capital position. The FSA will continue to monitor the firm's position closely.

The financial information contained in this half year report has been prepared in accordance with IAS 34 "Interim Financial Reporting" and the Disclosure and Transparency Rules of the Financial Services Authority as applicable to issuers of listed debt securities. The accounting policies and method used to prepare the 2009 half year results remain unchanged from those used in the preparation of the 2008 full year statutory accounts, except for those noted below.

#### **New standards, amendments and interpretations**

The following new standards, amendments to standards or interpretations are mandatory for the first time for financial years beginning on 1 January 2009 and have been endorsed for adoption by the EU:

- IAS 1 (revised) – Presentation of financial statements. This standard has resulted in changes to the Statement of Recognised Income and Expense. This has been split into two statements, one showing changes in equity resulting from transactions not reflected in the income statement and the other showing change in equity resulting from transactions with shareholders.
- Amendment to IFRS 7 Improving Disclosures about Financial Instruments. As Northern Rock does not make detailed IFRS 7 disclosures in the half year accounts this amendment will only have an impact on the statutory accounts for the year to 31 December 2009.

# NORTHERN ROCK GROUP HALF YEAR RESULTS

## NOTES TO THE RESULTS (CONTINUED)

### **1. Basis of Preparation (continued)**

The following new standards, amendments to standards or interpretations are also mandatory for the first time for financial years beginning on 1 January 2009 and have been endorsed for adoption by the EU, but have no material financial impact on the Group:

- IFRS 8 – Operating segments
- IAS 23 (amendment) – Borrowing costs
- IFRIC 13 – Customer loyalty programmes
- Amendment to IFRS 2 Share-Based Payment: Vesting Conditions and Cancellations
- IAS 32 (amendment) – Financial instruments: presentation, and consequential amendments to IAS 1
- Revised IFRS 3 Business Combinations. This standard is not relevant to Northern Rock unless an acquisition is made.
- Revised IAS 27 Consolidated and separate financial statements
- IFRIC 14 – IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirement and their Interaction
- IFRIC 16 – Hedges of a net investment in a foreign operation
- Improvements to IFRSs

The following new standards, amendments to standards or interpretations are mandatory for the first time for financial years beginning on 1 January 2009 but have not yet been endorsed for adoption by the EU, but have no material financial impact on the Group:

- IFRIC 15 – Agreements for the construction of real estate
- IFRIC 17 – Distribution of Non-cash assets to Owners
- Amendments to IFRIC 9 and IAS 39 Embedded Derivatives
- Amendment to IFRS 1 ‘First time adoption of IFRS’ and IAS 27 ‘Consolidated and separate financial statements’ on the ‘Cost of an investment in a subsidiary, jointly controlled entity or associate
- Amendment to IAS 39 Financial Instruments: Recognition and Measurement: Eligible Hedged Items

The following new standards, amendments to standards or interpretations have been issued but have not yet been endorsed for adoption by the EU are not effective for financial years beginning on 1 January 2009 and have not been early adopted:

- Amendment to IFRS 2 Share-Based Payment – Group cash-settled share-based payment transactions. This amendment will have no impact on the Group.

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### NOTES TO THE RESULTS (CONTINUED)

#### 2. Net Interest Income

	Six months to 30 June		Full year
	<u>2009</u>	<u>2008</u>	<u>2008</u>
	<u>£m</u>	<u>£m</u>	<u>£m</u>
<b>Interest and similar income</b>			
On secured advances	860.7	2,493.9	4,684.0
On other lending	102.3	243.8	446.7
On investment securities and deposits	156.6	229.3	576.2
Interest and similar income	<u>1,119.6</u>	<u>2,967.0</u>	<u>5,706.9</u>
<b>Interest expense and similar charges</b>			
On retail customer accounts	361.0	389.5	956.6
On other deposits and loans including loans from Government	669.5	2,573.0	4,573.8
Other	14.9	56.4	125.6
Interest expense and similar charges	<u>1,045.4</u>	<u>3,018.9</u>	<u>5,656.0</u>
<b>Net interest income</b>	<u>74.2</u>	<u>(51.9)</u>	<u>50.9</u>

Included within interest income is an adjustment of £5.7m (30 June 2008: £1.7m, 31 December 2008: £3.3m) with respect to the unwind of the discount included in the impairment losses on loans and advances.

Average interest earning assets excluding fair value adjustments	86,475.0	99,837.2	95,972.8
Average interest bearing liabilities excluding fair value adjustments	84,514.0	96,657.2	93,031.2
Interest margin	0.15%	(0.13)%	0.05%
Interest spread	0.10%	(0.33)%	(0.13)%

Interest margin has been calculated by reference to average interest earning assets excluding fair value adjustments. Average balances have been calculated on a monthly basis. Interest spread represents the difference between interest receivable as a % of average interest earning assets, excluding fair value adjustments, and interest payable as a % of average interest bearing liabilities, excluding fair value adjustments.

For the purpose of calculating interest margin and spread, average balances for assets and liabilities denominated in foreign currencies, where these have been economically hedged, are based on the contract rate implicit in the associated hedging instrument.

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### NOTES TO THE RESULTS (CONTINUED)

#### **3. (Losses)/Gains on Investment Securities and Unsecured Investment Loans**

(Losses)/gains on investment securities and unsecured investment loans are analysed as follows:

	<b>Six months to 30 June</b>		<b>Full year</b>
	<b><u>2009</u></b>	<b><u>2008</u></b>	<b><u>2008</u></b>
	<b><u>£m</u></b>	<b><u>£m</u></b>	<b><u>£m</u></b>
Impairment credits/(losses) on investment securities reclassified as loans and receivables and unsecured investment loans	7.0	(46.6)	(267.6)
	7.0	(46.6)	(267.6)
(Losses)/gains on disposal of available for sale securities	(5.6)	6.0	44.4
Impairment losses on available for sale securities	(5.5)	(23.8)	(53.4)
	(11.1)	(17.8)	(9.0)
<b>Total</b>	<b>(4.1)</b>	<b>(64.4)</b>	<b>(276.6)</b>

In addition to the above, net losses from changes in fair value from financial assets designated at fair value are given in note 5.

Losses of £5.6m (30 June 2008: gains of £6.0m, 31 December 2008: gains of £44.4m) previously recognised in reserves have been transferred to (losses)/gains on available for sale securities in the Group income statement on the disposal of available for sale securities.

	<b><u>30 June</u></b>	<b><u>30 June</u></b>	<b><u>31 December</u></b>
	<b><u>2009</u></b>	<b><u>2008</u></b>	<b><u>2008</u></b>
	<b><u>£m</u></b>	<b><u>£m</u></b>	<b><u>£m</u></b>
Impairment allowance on unsecured investment loans	388.5	278.5	423.2

#### **4. Gains on Disposal of Loan Books**

During 2008 the Group sold £2,240.7m (net of provisions) of its residential equity release mortgage portfolio to JP Morgan Limited. Total proceeds (net of costs) amounted to £2,289.8m (30 June 2008: £2,280.0m). The surplus on disposal amounted to £49.1m (30 June 2008: £39.3m). Included in the reported results for the year ended 31 December 2008 is net interest income of £0.9m (30 June 2008: £0.9m) in relation to those assets to the date of disposal.

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### NOTES TO THE RESULTS (CONTINUED)

#### **5. Net Trading (Expense)/Income**

Net trading (expense)/income comprises:

	<b>Six months to 30 June</b>		<b>Full year</b>
	<b><u>2009</u></b>	<b><u>2008</u></b>	<b><u>2008</u></b>
	<b><u>£m</u></b>	<b><u>£m</u></b>	<b><u>£m</u></b>
Net losses from changes in fair value from financial assets designated at fair value	-	(31.0)	(46.4)
Net income from financial assets designated at fair value	-	2.0	3.0
Fair value movements of future cash flows excluding accruals on derivatives not in hedge accounting relationships	(3,366.2)	1,226.0	9,465.7
Translation gains/(losses) on associated instruments	3,317.0	(1,219.7)	(9,259.7)
	<u>(49.2)</u>	<u>(22.7)</u>	<u>162.6</u>

#### **6. Operating Expenses**

Operating expenses, excluding the covenant to The Northern Rock Foundation, are as follows:

	<b>Six months to 30 June</b>		<b>Full year</b>
	<b><u>2009</u></b>	<b><u>2008</u></b>	<b><u>2008</u></b>
	<b><u>£m</u></b>	<b><u>£m</u></b>	<b><u>£m</u></b>
Staff costs	57.3	82.9	163.4
Other expenses	36.3	41.9	84.4
Depreciation and amortisation	11.1	10.0	21.9
Total operating expenses	<u>104.7</u>	<u>134.8</u>	<u>269.7</u>

Exceptional administrative expenses are the costs associated with the restructuring of the business and comprise:

	<b>Six months to 30 June</b>		<b>Full year</b>
	<b><u>2009</u></b>	<b><u>2008</u></b>	<b><u>2008</u></b>
	<b><u>£m</u></b>	<b><u>£m</u></b>	<b><u>£m</u></b>
Staff costs	0.1	37.0	37.0
Professional fees incurred by the Company	1.2	21.6	29.8
Professional fees recharged by the Tripartite Authorities	1.6	10.8	10.7
Corporate advisory fees	-	4.2	4.2
Reimbursement of third party expenses	-	8.7	8.7
Accelerated charge on cancellation of share schemes	-	39.6	39.6
Company valuation	1.7	-	1.5
Other exceptional administrative expenses	0.1	8.1	10.0
	<u>4.7</u>	<u>130.0</u>	<u>141.5</u>
Exceptional impairment (credits) / charges on property, plant and equipment	(5.4)	6.8	(23.6)
Provision for onerous contracts	0.1	1.7	18.5
Exceptional impairment charges on intangible assets	-	27.1	27.2
Strategic project development	6.3	-	-
	<u>5.7</u>	<u>165.6</u>	<u>163.6</u>

Exceptional staff costs of £0.1m (30 June 2008: £37.0m, 31 December 2008: £37.0m) mainly represent the costs of redundancy, payments in lieu of notice and outplacement services associated with the reduction in the workforce as part of the restructuring of the business.

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### NOTES TO THE RESULTS (CONTINUED)

#### **6. Operating Expenses (continued)**

The reimbursement of third party expenses represents costs incurred by third parties as part of the strategic review process.

The accelerated charge on cancellation of share schemes represents the charge to the income statement of all previously unexpensed costs required by IFRS 2 – Share-based Payment on cancellation of staff share schemes after the acquisition of all shares in the Company by HM Treasury on 22 February 2008.

Company valuation costs of £1.7m (30 June 2008: £nil, 31 December 2008: £1.5m) relate to work done by BDO Stoy Hayward to value the Company's shares before the Company was taken into temporary public ownership.

The exceptional impairment credits of £5.4m (30 June 2008: charge of £6.8m, 31 December 2008 £23.6m) have arisen due primarily to reversals of impairments made in 2007 in respect of properties in the course of construction.

The provisions for onerous contracts of £0.1m (30 June 2008: £1.7m, 31 December 2008: £18.5m) represent the costs associated with properties no longer required after the restructuring of the business.

The exceptional impairment charges on intangible assets of £nil (30 June 2008: £27.1m, 31 December 2008: £27.2m) represent the costs associated with the accelerated amortisation of software no longer required after the restructuring of the business.

The strategic project development costs represent the costs associated with the legal and capital restructuring and positioning the Company to increase lending in a prudent and sustainable way.

The average number of persons employed by the Group was as follows:

	<b>Six months to 30 June</b>		<b>Full year</b>
	<b><u>2009</u></b>	<b><u>2008</u></b>	<b><u>2008</u></b>
Full time	3,522	4,811	4,231
Part time	983	1,154	1,045

#### **7. Impairment Losses on Loans and Advances**

	<b>Six months to 30 June</b>		<b>Full year</b>
	<b><u>2009</u></b>	<b><u>2008</u></b>	<b><u>2008</u></b>
	<b><u>£m</u></b>	<b><u>£m</u></b>	<b><u>£m</u></b>
<b>Impairment charge</b>			
Secured on residential property	223.3	55.5	364.0
Secured on residential buy to let property	59.4	18.9	48.9
Secured commercial	2.9	0.7	8.2
Unsecured	316.6	116.5	473.3
<b>Total impairment charge on retail loans and advances</b>	<b><u>602.2</u></b>	<b><u>191.6</u></b>	<b><u>894.4</u></b>
% of mean advances to customers	1.70%	0.42%	1.04%

# NORTHERN ROCK GROUP HALF YEAR RESULTS

## NOTES TO THE RESULTS (CONTINUED)

### **7. Impairment Losses on Loans and Advances (continued)**

	<b>30 June</b> <b><u>2009</u></b> <b><u>£m</u></b>	<b>30 June</b> <b><u>2008</u></b> <b><u>£m</u></b>	<b>31 December</b> <b><u>2008</u></b> <b><u>£m</u></b>
<b>Impairment allowance</b>			
Secured on residential property	400.9	100.5	335.4
Secured on residential buy to let property	86.9	23.5	42.9
Secured commercial	10.7	1.5	7.8
Unsecured	519.3	226.3	483.6
<b>Total impairment allowance on retail loans and advances</b>	<b><u>1,017.8</u></b>	<b><u>351.8</u></b>	<b><u>869.7</u></b>
% of period end loans and advances to customers	1.49%	0.42%	1.19%

### **8. Income tax expense / (credit)**

There has been a tax charge in the period of £15.8m (30 June 2008: credit of £19.9m, 31 December 2008: credit of £46.2m). The net tax charge for the period includes a £26.7m tax credit and a £34.5m tax charge.

The £26.7m credit arises due to a change in the timing of when certain Group profits are recognised for tax purposes allowing the utilisation of 2009 taxable losses.

During 2009, the Group's securitisation special purpose entities (SPE's) elected into a new tax regime. This means that certain items which could previously be recognised as a deferred tax asset can no longer be recognised, resulting in a charge of £34.5m.

Taxes on income in the interim periods are accrued using the tax rate that would be applicable to expected total annual earnings.

### **9. Appropriations**

	<b>Six months to 30 June</b>		<b>Full year</b>
	<b><u>2009</u></b> <b><u>£m</u></b>	<b><u>2008</u></b> <b><u>£m</u></b>	<b><u>2008</u></b> <b><u>£m</u></b>
Reserve capital instruments	-	-	25.2
Subordinated notes	30.9	28.0	46.3
Tax on appropriations	-	(1.3)	(3.2)
<b>Total</b>	<b><u>30.9</u></b>	<b><u>26.7</u></b>	<b><u>68.3</u></b>

### **10. Cash and Balances with Central Banks**

	<b>30 June</b> <b><u>2009</u></b> <b><u>£m</u></b>	<b>30 June</b> <b><u>2008</u></b> <b><u>£m</u></b>	<b>31 December</b> <b><u>2008</u></b> <b><u>£m</u></b>
Cash in hand	7.5	10.4	9.4
Balances with Bank of England for liquidity purposes	6,536.1	3,466.5	9,163.6
Mandatory reserve deposits with central banks	63.3	30.1	51.4
Other balances with central banks	60.0	52.4	112.4
	<b><u>6,666.9</u></b>	<b><u>3,559.4</u></b>	<b><u>9,336.8</u></b>

Mandatory reserve deposits with central banks are not available for use in day-to-day operations.

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### NOTES TO THE RESULTS (CONTINUED)

#### **11. Loans and Advances to Customers**

	<b>30 June 2009 £m</b>	<b>30 June 2008 £m</b>	<b>31 December 2008 £m</b>
Advances secured on residential property not subject to securitisation	27,316.6	31,351.3	28,679.0
Advances secured on residential property subject to securitisation	29,493.5	40,011.3	32,325.0
	<u>56,810.1</u>	<u>71,362.6</u>	<u>61,004.0</u>
Residential buy to let loans not subject to securitisation	5,550.0	5,999.6	5,695.7
Total advances secured on residential property	<u>62,360.1</u>	<u>77,362.2</u>	<u>66,699.7</u>
Commercial secured advances not subject to securitisation	292.1	298.6	301.7
Unsecured loans not subject to securitisation	4,489.1	6,329.6	5,298.0
	<u>67,141.3</u>	<u>83,990.4</u>	<u>72,299.4</u>

Fair value adjustments of portfolio hedging amounting to £1,251.4m (30 June 2008: £(561.6)m, 31 December 2008: £1,701.9m) relate to fair value adjustments of loans and advances to customers in relation to interest rate risk as a result of their inclusion in a fair value portfolio hedge relationship.

#### **12. Investment Securities and Unsecured Investment Loans**

	<b>30 June 2009 £m</b>	<b>30 June 2008 £m</b>	<b>31 December 2008 £m</b>
Available for sale securities	186.7	5,085.6	422.5
Assets held at fair value through the income statement	10.2	80.2	11.5
Investment securities held as loans and receivables	2,588.7	-	2,952.8
Unsecured investment loans	344.2	364.8	422.4
	<u>3,129.8</u>	<u>5,530.6</u>	<u>3,809.2</u>

The investment securities held as loans and receivables are asset backed securities and floating rate notes which were reclassified in the second half of 2008 under the terms of IAS 39 paragraph 50E.

Unsecured investment loans were previously reported in loans and advances to customers but have been reclassified to investment securities and unsecured investment loans.

#### **13. Covered Bonds**

Included within loans and advances to customers not subject to securitisation are £10,443.8m (30 June 2008: £9,416.4m, 31 December 2008: £9,686.5m) of mortgage advances assigned to a bankruptcy remote special purpose vehicle. These loans provide security to issues of covered bonds made by Northern Rock, which are included within debt securities in issue amounting to £9,465.5m (30 June 2008: £9,402.7m, 31 December 2008: £12,550.3m). Northern Rock retains substantially all the risks and rewards associated with these loans and therefore these transactions do not qualify for derecognition under IAS 39.

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### NOTES TO THE RESULTS (CONTINUED)

#### 14. Loans from Government

	<b>30 June 2009 £m</b>	<b>30 June 2008 £m</b>	<b>31 December 2008 £m</b>
Amount due to Bank of England	-	20,963.0	-
Repo funding from Bank of England	-	283.0	-
Amount due to HM Treasury	14,528.6	-	15,583.4
	<u>14,528.6</u>	<u>21,246.0</u>	<u>15,583.4</u>

The amount due to the Bank of England was novated to HM Treasury on 28 August 2008 with unchanged terms and conditions.

The repo funding at 30 June 2008 represented repos with the Bank of England as part of their public open market operations and was secured against assets with a market value of £288.7m.

#### 15. Customer Accounts

	<b>30 June 2009 £m</b>	<b>30 June 2008 £m</b>	<b>31 December 2008 £m</b>
Branch accounts	4,399.7	3,044.9	4,312.8
Postal accounts	7,103.8	5,995.4	7,495.9
Internet accounts	4,658.8	3,559.7	5,397.7
Offshore accounts	1,863.6	1,199.1	2,023.2
Other accounts	377.8	398.4	393.2
Total retail balances	<u>18,403.7</u>	<u>14,197.5</u>	<u>19,622.8</u>
Non bank wholesale customer accounts	1,198.1	367.9	1,099.9
	<u>19,601.8</u>	<u>14,565.4</u>	<u>20,722.7</u>

#### 16. Debt Securities in Issue

	<b>Securitised notes £m</b>	<b>Covered bonds £m</b>	<b>Other debt securities in issue £m</b>
<b>Balance at 1 January 2009</b>	37,986.9	12,550.3	7,199.1
Issuances	-	-	652.4
Repayments	(4,477.9)	(1,784.2)	(2,468.9)
Exchange rate movements and fair value adjustments	(2,954.1)	(1,300.6)	(526.0)
<b>Balance at 30 June 2009</b>	<u>30,554.9</u>	<u>9,465.5</u>	<u>4,856.6</u>
	<b>Securitised notes £m</b>	<b>Covered bonds £m</b>	<b>Other debt securities in issue £m</b>
<b>Balance at 1 January 2008</b>	43,069.5	8,938.1	9,633.7
Repayments	(6,500.6)	-	(985.6)
Exchange rate movements and fair value adjustments	1,088.2	464.6	241.7
<b>Balance at 30 June 2008</b>	<u>37,657.1</u>	<u>9,402.7</u>	<u>8,889.8</u>

**NORTHERN ROCK GROUP HALF YEAR RESULTS**

**NOTES TO THE RESULTS (CONTINUED)**

**16. Debt Securities in Issue (continued)**

	<b>Securitised notes £m</b>	<b>Covered bonds £m</b>	<b>Other debt securities in issue £m</b>
<b>Balance at 1 January 2008</b>	43,069.5	8,938.1	9,633.7
Issuances	-	-	736.1
Repayments	(13,164.6)	-	(4,950.6)
Exchange rate movements and fair value adjustments	8,082.0	3,612.2	1,779.9
<b>Balance at 31 December 2008</b>	<b>37,986.9</b>	<b>12,550.3</b>	<b>7,199.1</b>

**17. Revaluation Reserve – Available for Sale Investments**

	<b>Six months to 30 June</b>		<b>Full year</b>
	<b>2009</b>	<b>2008</b>	<b>2008</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
<b>Balance at 1 January</b>	(602.5)	(93.7)	(93.7)
Net losses from changes in fair value	(6.9)	(258.3)	(562.0)
Losses transferred to net income due to impairment	5.5	23.8	53.4
Net losses/(profits) on disposal transferred to net income	5.6	(6.0)	(44.4)
Amortisation of fair value differences in respect of securities transferred to loans and receivables	154.3	-	(21.8)
Losses transferred (from)/to net income due to impairment of securities transferred to loans and receivables	(30.2)	-	43.3
Deferred income taxes	0.8	22.0	23.1
Effect of UK tax rate change on deferred tax items	-	(0.4)	(0.4)
<b>Balance at 30 June / 31 December</b>	<b>(473.4)</b>	<b>(312.6)</b>	<b>(602.5)</b>

**18. Own Shares**

The credit to retained earnings in respect of movements on own shares for the period is as follows:

	<b>Six months to 30 June</b>		<b>Full year</b>
	<b>2009</b>	<b>2008</b>	<b>2008</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Accelerated charge on cancellation of share schemes (see note 6)	-	39.6	39.6
Tax impact of share based payments	-	1.9	3.6
	<b>-</b>	<b>41.5</b>	<b>43.2</b>

As a result of The Northern Rock plc Transfer Order 2008, all shares were transferred to the Treasury Solicitor as nominee for the Treasury on 22 February 2008. Consequently, Northern Rock plc no longer owns any of its own shares. The consideration it will receive for these shares has not yet been determined and therefore no asset has been recognised for the proceeds in these accounts.

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### NOTES TO THE RESULTS (CONTINUED)

#### **19. Related Party Transactions**

As a consequence of the transfer of all shares in Northern Rock plc to the Treasury Solicitor on 22 February 2008, the Company regards the Government as a related party from this date. Details of loan facilities with the Government are set out in note 14 above. Interest and guarantee fees payable on the loan in the six months ended 30 June 2009 are £309.2m (from 22 February 2008 to 30 June 2008: £587.6m, from 22 February 2008 to 31 December 2008: £1,212.6m).

In addition to these loans and guarantees the Group has transactions with numerous Government bodies on an arm's length basis in relation to the payment of corporation tax, value added tax and employee taxes and the payment of regulatory fees and levies. Transactions with these entities are not disclosed owing to the volume of transactions conducted.

There have been no other material transactions with related parties in the period.

#### **20. Capital Structure**

	<b>30 June 2009 £m</b>	<b>30 June 2008 £m</b>	<b>31 December 2008 £m</b>
Core Tier 1 capital	(794.0)	767.8	(17.1)
Perpetual non-cumulative preference shares	621.3	596.5	648.3
Innovative Tier 1 capital	299.3	299.3	299.3
Deductions from and restrictions to Tier 1 capital	(126.1)	(236.9)	(146.4)
Tier 1 capital after deductions	<u>0.5</u>	<u>1,426.7</u>	<u>784.1</u>
Upper Tier 2 capital	1,203.0	1,032.5	1,313.5
Lower Tier 2 capital	933.6	899.5	940.5
Deductions from and restrictions to Tier 2 capital	(61.1)	(162.8)	(76.3)
Tier 2 capital after deductions	<u>2,075.5</u>	<u>1,769.2</u>	<u>2,177.7</u>
Deductions from totals of Tier 1 and Tier 2	(5.1)	(5.1)	(5.1)
Total available capital resources	<u>2,070.9</u>	<u>3,190.8</u>	<u>2,956.7</u>
Risk weighted assets	26,216.3	26,726.1	27,471.4

Northern Rock's total available capital resources are shown in the table above. The FSA's capital resources gearing rules require core tier 1 capital to account for at least 50% of total tier 1 capital and limit total tier 2 capital to 100% of tier 1 capital and lower tier 2 capital to 50% of tier 1 capital. Certain elements of the total available capital resources shown above are therefore restricted for regulatory purposes. Northern Rock was granted a waiver from the restriction that total tier 2 capital must not exceed total tier 1 capital during the period 31 July 2008 to 30 June 2009.

As set out in note 1 to the Half Year results, Northern Rock's capital base has reduced to a level below its minimum regulatory capital requirement. The FSA has confirmed that it does not currently intend to restrict the activities of the Company while the legal and capital restructuring is completed.

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### NOTES TO THE RESULTS (CONTINUED)

#### **21. Other Information**

The information in this announcement is unaudited and does not constitute statutory accounts within the meaning of section 434 of the Companies Act 2006. The statutory accounts of Northern Rock plc for the year ended 31 December 2008 have been filed with the Registrar of Companies in England and Wales. The auditors' report on these accounts was unqualified and did not include a statement under section 498 of the Companies Act 2006, although the auditors' report contained an emphasis of matter in relation to the Company's ability to continue as a going concern, reflecting the need for continued support from HM Treasury.

The report will be available on the Northern Rock website [www.northernrock.co.uk](http://www.northernrock.co.uk) from 8.30am on 4 August 2009.

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### **Statement of Directors' Responsibilities**

The Directors confirm that the Group half year results have been prepared in accordance with IAS 34 as adopted by the European Union and that the management commentary and supporting notes to the half year results includes a fair review of the information required by DTR 4.2.7, namely, an indication of important events that have occurred in the first six months and their impact on the condensed set of financial statements and a description of the principle risks and uncertainties for the remaining six months of the financial year.

The Directors of Northern Rock plc at the date of this report are:

RA Sandler  
LP Adams  
MK Atkinson  
JR Coates  
RJ Davies  
JF Devaney  
GA Hoffman  
PJ Remnant  
TW Scholar

By order of the Board

RA Sandler  
4 August 2009  
Non-Executive Chairman

GA Hoffman  
4 August 2009  
Chief Executive Officer

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### Independent review report to Northern Rock plc

#### Introduction

We have been engaged by the Company to review the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2009, which comprises the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated Balance Sheet, the Consolidated Statement of Cash Flows, the Consolidated Statement of Changes in Equity and related notes. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

#### Directors' responsibilities

The half-yearly financial report is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the half-yearly financial report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority, as applicable to the issuers of debt securities.

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

#### Our responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review. This report, including the conclusion, has been prepared for and only for the Company for the purpose of the Disclosure and Transparency Rules of the Financial Services Authority, as applicable to the issuers of debt securities, and for no other purpose. We do not, in producing this report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

#### Scope of review

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

#### Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2009 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority, as applicable to the issuers of listed debt securities.

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### Independent review report to Northern Rock plc (continued)

#### Emphasis of Matter - Going Concern

In forming our review conclusion on the condensed financial statements, which is not qualified, we have considered the adequacy of the disclosure made in note 1 to the condensed financial statements concerning the Company's ability to continue as a going concern. The going concern assumption is dependent on the European Commission approving financing facilities provided by HM Treasury. The outstanding approval from the European Commission indicates the existence of a material uncertainty which may cast significant doubt about the Company's ability to continue as a going concern. The condensed financial statements do not include the adjustments that would result if the Company was unable to continue as a going concern.

PricewaterhouseCoopers LLP  
Chartered Accountants  
4 August 2009  
Newcastle

## NORTHERN ROCK GROUP HALF YEAR RESULTS

### Contacts

#### **Press Contacts**

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This document contains certain forward-looking statements with respect to certain of the plans of Northern Rock, its current goals and expectations relating to its future financial condition and performance. By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. Northern Rock's actual future results may differ materially from the results expressed or implied in these forward-looking statements as a result of a variety of factors, including UK domestic and global economic and business conditions, market related risk such as interest rates and exchange rates, delays in implementing proposals, unexpected difficulties with computer systems, unexpected changes to regulation, changes in customer preferences, competition and other factors.