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GOOD PROGRESS AND IMPROVING PERFORMANCE: BUILDING A STRONG STANDALONE FUTURE

- National Australia Bank (NAB), owner of Clydesdale and Yorkshire Banks, today released half year results for its UK Banking¹ operations
- NAB also announced its intention to pursue a demerger and Initial Public Offering (IPO) of the holding company of Clydesdale Bank (National Australia Group Europe Ltd) and its subsidiaries, referred to in this document as “Listco”. Clydesdale Bank PLC operates the Clydesdale Bank and Yorkshire Bank brands
- Discussions with regulators and other key stakeholders, whilst significant to date, remain ongoing. There is no certainty that a transaction will occur. Any transaction is subject to approval by regulators, the boards of NAB and Listco and NAB shareholders. Completion is targeted for the end of calendar year 2015
- The UK Banking results below are for the six months to 31 March 2015. Unless otherwise stated, figures are comparisons with the six months to 31 March 2014:
 - Pre-tax cash earnings² £118 million, up 33%; cash earnings £99 million, up 36%
 - Charge for bad and doubtful debts down £31 million (56%) to £24 million
 - £2.4 billion mortgage growth (14.5%)
 - Listco Common Equity Tier 1 ratio of 11.9%, up from 9.4% in September 2014
- A reconciliation between the UK Banking results and Listco’s results is attached

Debbie Crosbie, Acting Chief Executive, said:

“Today’s announcement marks the beginning of an exciting new opportunity for Clydesdale and Yorkshire Banks. Our performance is improving and we’re providing real customer choice in the UK which is driving encouraging growth across our target retail and SME markets.

“We believe the foundations of a strong standalone future have been laid in the progress made restructuring and refocusing our business and this is clear in our half year results. Pre-tax cash earnings are up a third to £118 million, charges to provide for bad and doubtful debts more than halved and mortgage lending is up £2.4 billion.

“There’s more work to be done as we move the business forward and build a better bank for our customers. Oversight and governance of historical PPI complaints have been completely overhauled and comprehensive programmes are underway to put this right to ensure we are doing the right thing by our customers.

“The strong start we’ve made since the beginning of 2015 means we’re well placed to build on our organic growth plans. In particular, we’ve seen encouraging growth in current account switchers supported by a market leading offer. Our ISA rates have headed the field, we’ve offered a market leading credit card and we continue to punch above our weight in the mortgage market. Support for customers will continue to be at the heart of our business. More efficient distribution channels, significant investment in technology, digital banking, brand awareness and innovative products will ensure this positive momentum continues.”

¹ Unless otherwise stated, the results are for NAB UK Banking and not those of Clydesdale Bank PLC or Listco. UK Banking consists of banking and wealth management activities in the UK operating under the Clydesdale Bank and Yorkshire Bank brands. It does not include NAB’s wholesale banking operations in the UK.

NAB Exit

- Significant work has been undertaken on a range of exit options, in particular those provided by public markets.
- The preferred public market exit option is a demerger of 70-80% of National Australia Group Europe Ltd and its subsidiaries (Listco) to NAB shareholders and a sale of shares in an IPO of the balance of approximately 20-30% to institutional investors, targeting an exit by end of 2015 subject to market conditions.
- Demerger would accelerate a full exit, delivering greater certainty than a full IPO alternative and NAB shareholders can retain potential upside from Listco.
- Listco is well positioned to be demerged to NAB shareholders and sold to investors as a standalone retail and business bank with strong market shares across its core regional markets in the UK.
- This is a substantial and complex undertaking, subject to risk and addressing a number of issues of which the most substantive is conduct mitigation.
- Listco is proposed to have CET1 ratio of approximately 13% (from 11.9%) with an expected equity injection by NAB prior to separation.
- There is no certainty that a transaction will occur and discussions with regulators and other key stakeholders, whilst significant to date, remain ongoing.
- Any transaction will also be subject to a number of matters, including:
 - approvals from UK and Australian regulators and listing authorities;
 - approval of the transaction by the boards of Listco and NAB; and,
 - approval of the transaction by NAB shareholders.
- Preliminary standalone credit ratings of Listco are expected to be senior investment grade post separation.
- The UK Prudential Regulation Authority (PRA) has advised that in order to demerge Listco, NAB will be required to provide capital support for Listco against potential losses related to legacy conduct costs. These are centred on payment protection insurance, interest rate hedging products and fixed rate tailored business loan conduct issues not covered by existing provisions, to a total cap of £1.7bn, provided that the demerger occurs within the intended timeframe.
- Form, duration and final regulatory capital treatment of the conduct support remain subject to ongoing discussion with regulators.

Business Performance

Reflecting material reductions in bad and doubtful debts and improved economic conditions, pre-tax cash earnings² increased 33% to £118 million compared to £89 million in the prior corresponding period. Cash earnings were £99 million compared to £73 million. Underlying profits at £142 million were up by 2.2% on the September half and down 1.4% on the prior corresponding period.

The charge to provide for bad and doubtful debts fell by 56% or £31 million to £24 million, primarily driven by the improved UK economy and the reduced size of the business portfolio as well as management actions to improve asset quality.

Operating expenses decreased by £4 million (1.2%) due to a one-off pension scheme gain in the half, combined with charges of £13 million for conduct issues that were incurred only in the March 2014 half. These favourable impacts were partially offset by restructuring charges of £11 million combined with marketing costs to

² Unless otherwise stated, information in this document is presented on a cash earnings basis. "Cash earnings" is a key non-GAAP financial performance measure used by NAB. "Cash earnings" are calculated by excluding certain items which are otherwise included within the calculation of net profit attributable to owners of the company, in order to better reflect what NAB considers to be the underlying performance of the Group. UK Banking cash earnings exclude fair value and hedge ineffectiveness income/expense and significant items including PPI redress. A full definition is set out in the NAB Profit Announcement under Glossary of Terms.

support customer acquisition. More work is required to improve the cost to income ratio from 70.4%. This is compared with 71.3% at September 2014 and 70.3% at March 2014.

Average gross loans and acceptances increased by £1.3 billion (4.9%) to £28 billion. Driven by continued support for first-time buyers and re-mortgaging customers, mortgage growth of 14.5% was achieved. Despite significant mortgage portfolio growth, retail asset quality remains strong with low levels of housing impaired loans. Retail lending growth was partially offset by a £1.1 billion reduction in business lending balances due to subdued demand for credit, competitive pressures and includes significant reductions in areas we have chosen not to compete in as we reshape our business book. Our strategic focus on SME customers in key sectors and local communities is progressing well with around £500 million of new business lending in the half.

Strongly customer deposit funded, average deposit volumes were up £900 million in the half to £24.2 billion. An improved deposit mix was achieved with growth in current and savings accounts, partially offset by a reduction in higher cost term deposits. Net interest margins in the half were 2.18% (from 2.25%) driven by an increase in low yielding liquid assets and lower lending margins due to competitive pressures. This was partially offset by an improved retail deposit mix and lower funding costs.

With an improved capital and funding base, at 31 March 2015, Listco's Common Equity Tier 1 ratio was 11.9% up from 9.4% at 30 September 2014.

Customer Support

Significant investment to support customer improvements has continued in the half. This included new products for personal customers and more competitive products for SME customers combined with more effective distribution. This summer we will launch a new, innovative digital banking service marking a significant change in how customers can choose to bank with us. Drawing on extensive customer feedback, this exciting new approach to banking is currently being tested by customers.

We're building a bank better able to meet our customers' changing needs and ensuring that we have the right premises and people in the right locations to serve all of our customers' needs is fundamental to that. Over the next year we will continue to change the shape of our branch and business centre network, bringing more services for more customers under one roof in better, more central locations. Aberdeen will be the first location where we will fully bring together all of our services to improve the way we serve retail and business customers.

Significant investment continues to be made in our branch network. By the end of the year we will deliver 18 branch facelifts, three relocations to better sites in Bolton, Chesterfield and Newcastle-Upon Tyne and a new flagship branch in Leeds. A total of 19 branches will close and four branches and business centres are expected to co-locate this year.³

Historical Conduct

An income statement charge of £21 million was recognised by Listco to reflect the outcome of the FCA's enforcement action announced on 14 April 2015. In line with the UK banking industry, the level of Payment Protection Insurance (PPI) claims

³ The 19 closing branches are Blackpool Central Dr, Colne, Driffield, Stalybridge, Featherstone, Glasgow Springburn, Denny, Kettering, Kilwinning, South Bank, Dundee Downfield, Elland, Helensburgh, Barnsley New Street, Forres, Altrincham, Dollar, Hamilton Cadzow Street and Leeds York Road. The co-locations will be in Gloucester, Lincoln, York and Leicester.

continues to be monitored and the provision is subject to significant risks and uncertainties.

Significant progress has been made towards completion of the in-scope interest rate hedging product review. The extent of future complaints on out-of-scope products remains more uncertain. The total costs associated with conduct related matters remain subject to a wide range of uncertain factors.

Media Contacts
Investor Relations

Barry Gardner / Jason Clarke
Miles Storey / Lee Kelly

0845 603 5447
0207 710 2977

UK Banking⁴

	Half Year to			Mar 15 ⁽¹⁾ v Sep 14 %	Mar 15 ⁽¹⁾ v Mar 14 %
	Mar 15 ⁽¹⁾	Sep 14	Mar 14		
	£m	£m	£m		
Net interest income	386	379	380	1.8	1.6
Other operating income	93	105	105	(11.4)	(11.4)
Net operating income	479	484	485	(1.0)	(1.2)
Operating expenses	(337)	(345)	(341)	2.3	1.2
Underlying profit	142	139	144	2.2	(1.4)
Charge to provide for bad and doubtful debts	(24)	(25)	(55)	4.0	56.4
Cash earnings before tax	118	114	89	3.5	32.6
Income tax expense	(19)	(29)	(16)	34.5	(18.8)
Cash earnings	99	85	73	16.5	35.6

Average Volumes (£bn)

Gross loans and acceptances	28.0	27.1	26.7	3.3	4.9
Interest earning assets	35.5	34.6	33.9	2.6	4.7
Total assets	38.5	37.8	36.3	1.9	6.1
Customer deposits	24.2	23.7	23.3	2.1	3.9

Risk Weighted Assets (£bn)

Risk-weighted assets - credit risk (spot)	18.4	18.7	19.2	(1.6)	(4.2)
Total risk-weighted assets (spot)	24.1	23.5	24.1	2.6	-

Performance Measures

Cash earnings on average assets	0.52%	0.45%	0.40%	7 bps	12 bps
Cash earnings on average risk-weighted assets	0.84%	0.71%	0.60%	13 bps	24 bps
Net interest margin	2.18%	2.18%	2.25%	-	(7 bps)
Cost to income ratio	70.4%	71.3%	70.3%	90bps	(10 bps)
Cash earnings per average FTE (£k)	27	23	21	17.4	28.6
FTEs (spot)	7,249	7,278	7,103	0.4	(2.1)

⁽¹⁾ March 2015 results have been prepared in accordance with AASB9; prior periods have not been restated.

Distribution	As at		
	Mar 15	Sep 14	Mar 14
Number of retail branches	294	296	322
Number of ATMs	888	859	859
Number of internet banking customers (no. '000s) ⁽¹⁾	659	623	599

⁽¹⁾ Prior period numbers have been restated due to changes in methodology.

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Reconciliation of UK Banking to Listco results

Half year ended Mar 15 £m	UK Banking ¹	Non UK Banking ²	Statutory Reclass	Listco
Net interest income	386	4	-	390
Other operating income	93	57	6	156
Net operating income	479	61	6	546
Operating expenses	(337)	(24)	(2)	(363)
Impairment losses on credit exposures	(24)	-	(4)	(28)
Cash earnings (pre-tax)	118	37	-	155
Tax expense	(19)	1	-	(18)
Cash earnings (post-tax)	99	38	-	137

⁽¹⁾ Represents the UK Banking segment as reported in NAB Group'

⁽²⁾ Represents certain Listco items recognised outside of the UK Banking segment including the gains on capital restructure

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