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The Royal Bank of Scotland Group

Report and Accounts 1989

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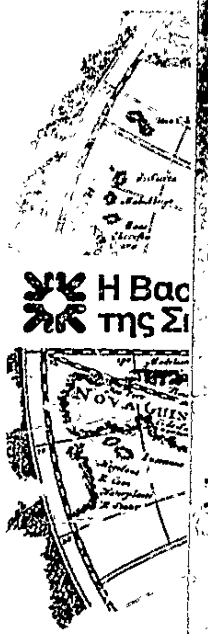
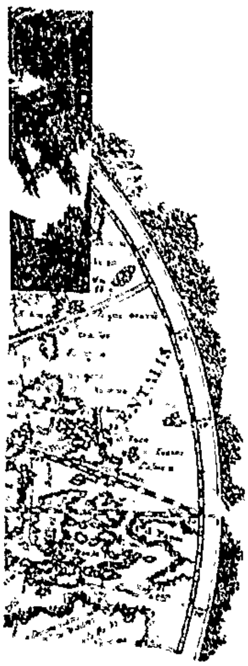


Corporate Statement



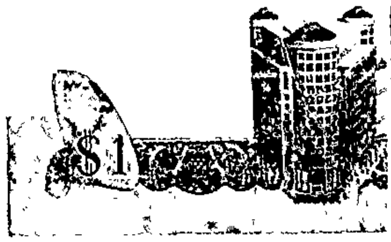
The Royal Bank of Scotland Group is an independent financial services group, with its headquarters in Edinburgh, operating throughout Great Britain and in certain overseas markets. We regard our reputation for integrity and financial stability earned from over two hundred and fifty years of serving our customers as the foundation upon which we will build our future. Our overall objective is, through the excellence of our service, to satisfy the needs of our customers, the requirements of our shareholders and the aspirations of our staff. We will seek to use our skills and capital in markets where we can give special value to our customers through superior service thus achieving higher returns for our shareholders while expanding the Group. We recognise that our most important resource is our people, their skills and their commitment to our customers. Communication is a priority as is personal development. Our people will participate in success through a system which rewards initiative, effort and performance and which accords with the practice prevailing within their particular business area. We will maintain our commitment to innovation and technology in order that our customers will benefit from new services and lower costs. We are fully aware of our social responsibility to the communities in which we live and work, national and local. At each level we will play our part in creating a good business environment and in participating in the wider aspects of the fabric of community life. The achievement of these objectives, year on year, will contribute to our Group retaining the independent status which we firmly believe is in the best long term interests of our customers, shareholders and staff.

Financial Highlights

for the year ended 30th September 1989

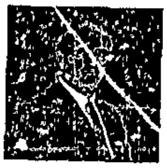
	£m	1988 £m
Profit before exceptional item	**336·5**	309·2
Profit before taxation	**228.2**	309·2
Profit attributable to ordinary shareholders	**147·1**	192·5
Ordinary dividends	**54·7**	43·2
Retained profit	**92·4**	149·3
Total assets	**27,435·7**	21,659·9
Total shareholders' funds	**1,410·7**	1,269·7
Earnings per 25p ordinary share		
before exceptional item	**29·4p**	26.8p*
er exceptional item	**19·9p**	26.8p*
Dividends per 25p ordinary share	**7·2p**	6.0p*
Dividend cover (times)		
before exceptional item	**4·1**	4·5
after exceptional item	**2.8**	4·5

*Earnings and dividends per 25p ordinary share have been adjusted to show the effects of the capitalisation issue in September 1989.



Corporate Structure

The Royal Bank of Scotland Group plc
Group holding company



The Royal Bank of Scotland plc
Bob Maiden *managing director*
Clearing banking and financial services from over 870 branches throughout the United Kingdom and in several overseas locations

Charterhouse plc
Victor Blank *chief executive*
Merchant banking, development capital, stockbroking and securities

Citizens Financial Group, Inc.
George Graboys *president and chief executive officer*
Banking and financial services in New England, U.S.A.

RoyScot Finance Group plc
Bob Riding *chief executive*
Leasing, factoring, contract hire, hire purchase and instalment finance; and review of the activities of the A. T. Mays Group

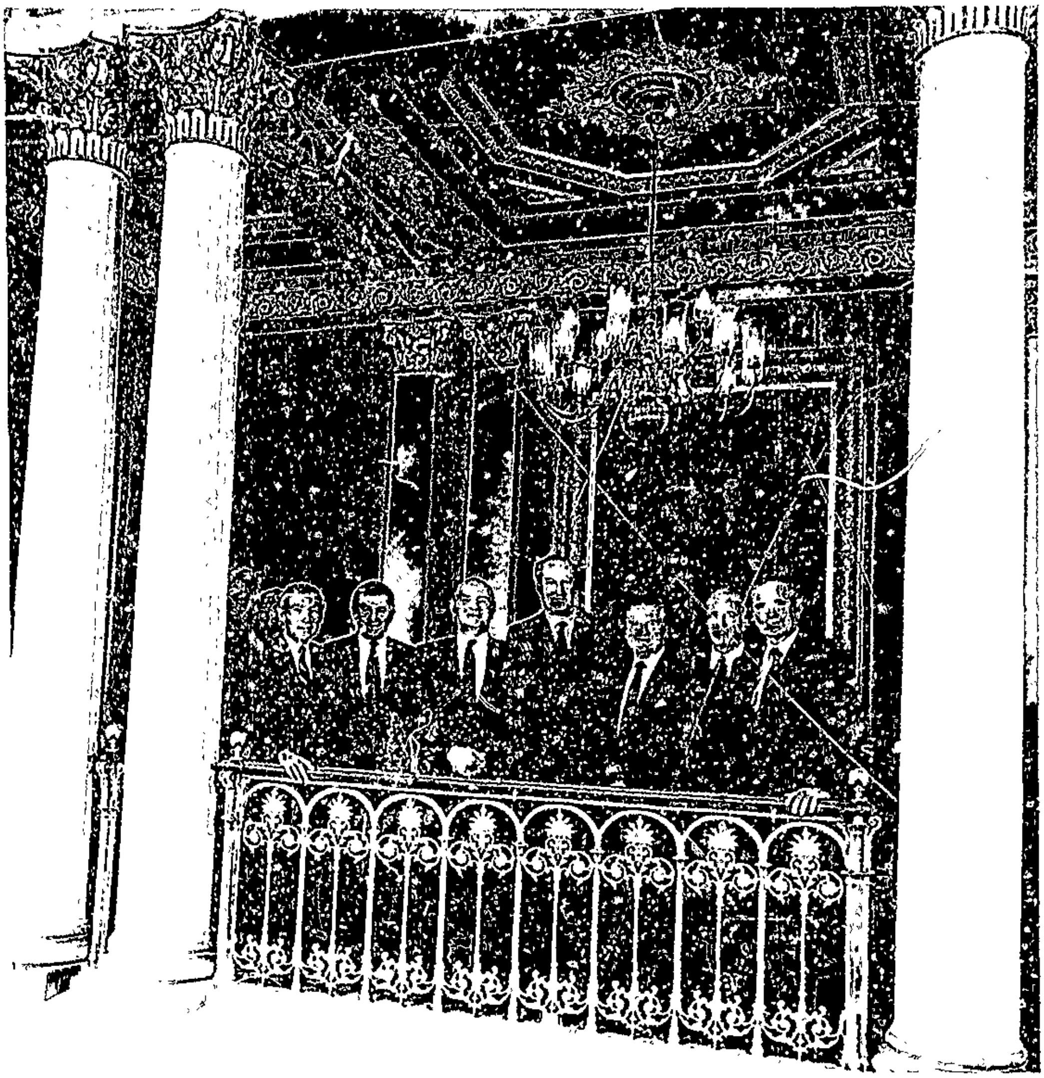
Direct Line Insurance plc
Peter Wood *chief executive*
Insurance underwriting covering motor, home and credit insurance

Capital House Investment Management Limited
Norman Riddell *chief executive*
Investment management

Royal Bank Group Services Limited
James Rafferty *managing director*
Technological development of the Group with responsibility for property, equipment and all related resources

Corporate Structure

Continued



The Group executive (from left to right): George Graboys, president and chief executive officer of Citizens Financial Group, Kenneth Thompson, group finance director, Charles Winter, group chief executive, Victor Blank, chief executive of Charterhouse, Rob Farley, deputy group chief executive, Bob Malden, managing director of The Royal Bank of Scotland and George Mathewson, director of strategic planning and development.

Distinctive operating structure

Our unique operating structure strengthens our position as a widely-based financial services group. It allows us to draw on the experience of each business, to expand the range of financial services in the United Kingdom and overseas and to operate more effectively in each of our chosen markets.

Each of our operating divisions enjoys a high degree of autonomy. This allows individual "brands" to flourish in their individual marketplaces, benefiting from membership of the Group and adding to it through shared activities and skill transfers.

Central role of the group executive

The Group executive is a full-time compact team of senior personnel, reporting directly to the board of directors. It has responsibility for setting fundamental objectives and performance targets, analysing and defining individual strategies identifying growth markets, allocating resources and controlling expansion worldwide.

This structure fosters the development of distinct independent cultures within the operating divisions while enhancing cohesive Group spirit in the attainment of a common purpose. In this way, the Group executive endeavours to ensure that the Group always meets its customers' needs and maximises the returns for its shareholders.

Statement by the Chairman

The year to 30th September 1989 has once again been a successful one for our company despite the slowdown in the U.K. economy which I predicted in my interim statement. This has continued and indeed intensified. Against this background, we have considered it prudent to make a number of provisions in respect of customers who are experiencing problems. Following these, we have recorded an increase in profit of £27.3 million to £336.5 million which, in the circumstances, is highly satisfactory. From this figure we are deducting an exceptional specific provision in respect of lending to countries in payment difficulties. This represents the culmination of a programme commenced in 1986 and we do not consider that any further exceptional provision for this class of lending should be required. A profit of £147.5 million remains after taxation which enables us to recommend a final dividend of 4.8p per share to give a worthwhile increase of 20 per cent. for the year.

PERFORMANCE AND DEVELOPMENTS

During the last year we have continued to implement key strategic initiatives and have also increased cross-selling opportunities among our subsidiaries. Earnings per share before the exceptional provision have again increased and, at 29.4p per share, maintains the favourable trend firmly established over recent years. Net interest income for the Group was up by 21 per cent., offset to an extent by the introduction of interest paying current accounts. Other operating income increased strongly by 29 per cent. Although expenses for the enlarged Group rose by 28 per cent., the underlying cost: income ratio continues to bear favourable comparison with that of our main competitors. Increased central financing costs were incurred in respect of the overseas acquisitions and the application of a new accounting standard led to the re-introduction of a pension fund charge in The Royal Bank of Scotland. Since my last annual statement, much has been done to build on the achievements of 1988 in the U.S.A. and Europe. In December 1988, the acquisition of Citizens Financial Group, based in Rhode Island, U.S.A., was completed. This purchase was a significant step in the Group's declared intention to reduce its reliance on purely sterling income and also leaves us well placed for future controlled expansion into the retail banking market in the U.S.A. Citizens has already demonstrated that it will serve as an ideal flagship for this growth. In Europe, our alliance with Banco Santander Group of Spain was cemented further when it became our largest shareholder by increasing its shareholding in the Group from 2.5 per cent. to almost 10 per cent. in December 1988. In addition, I was pleased to accept an invitation to join Santander's board of directors and to welcome Don Emilio Botin to our board. Progress of the alliance is reviewed regularly by senior executives from both groups who are responsible for agreeing and developing new projects. The benefits of the alliance are evident at many levels such as the establishment in July of a jointly owned bank in Gibraltar, managed

Statement by the Chairman

Continued

by The Royal Bank of Scotland. In addition to developing our interests overseas, we have capitalised upon opportunities in our home markets. Life assurance had been identified as a gap in the range of financial services which we offer and to be a market which offered potential for profitable expansion and cross-selling opportunities. We were therefore delighted to announce in September the establishment of a new joint venture life assurance company with one of Scotland's major life offices, the Scottish Equitable Life Assurance Society. Our balance sheet has been strengthened by the issue of U.S.$200 million non-cumulative preference shares and the capitalisation of revaluation reserves, together with loan capital issues of U.S.$650 million. As a result our capital ratios comfortably exceed the requirements of both the Bank of England and the Bank for International Settlements in Basle.

DIVIDENDS

The directors have recommended a final dividend on the ordinary shares of 4.8p, which, together with an interim dividend of 2.4p, will give a total for the year of 7.2p (1988—6.0p), an increase of 20 per cent. on the previous year. Over the past five years the ordinary dividend has grown at a compound annual rate of 17.3 per cent. compared with a compound annual inflation rate of 5.1 per cent., reflecting the sustained strong performance of the Group and the board's policy that shareholders should continue to benefit from the Group's achievements. Once again, at the annual general meeting, we intend to seek approval to offer new shares in lieu of the cash dividend.

ECONOMIC DEVELOPMENTS

The last twelve months have seen a robust performance by the world's industrial economies and a marked upturn in world trade. A number of the highly indebted countries have benefited, but to an insufficient extent to resolve their difficult long term problems. This buoyancy of the world economy has brought with it inflationary pressures which have resulted in a global tightening of monetary policy. There has also been a perceptible improvement in the U.S. current account deficit in the last year, an encouraging trend which, it is hoped, will continue. The United Kingdom, however, has performed less well with output failing to keep pace with the rise in domestic consumer and investment expenditure. There has also been a marked increase in bank lending and a rapid rise in inflation which peaked at around 8.5 per cent. during the summer. This has been accompanied by a widening of the current account deficit which may approach £20 billion this year. This deficit cannot be sustained for long, and a substantial contraction in domestic expenditure will be necessary to reduce it. The increase in bank base rates is part of this process although a protracted period of such rates will produce a marked slowdown in economic activity and a reversal of the decrease in unemployment. Consumer spending has been slowing down while the housing market has eased, producing a similar trend in new personal borrowing. High interest rates are also affecting the corporate sector, which now has a significant financial deficit and there is likely to be a reduction in investment over the short term. Several segments of this sector have nevertheless performed well to date, in particular the mechanical and electrical engineering industries. The oil industry has demonstrated a willingness to invest following the stabilisation of the oil price. The outlook for this industry looks encouraging and this is important for the well-being of the Scottish economy which generally has had a reasonably satisfactory year. As we move into a new decade, it is reassuring to see much of U.K. industry preparing itself for the advent of the single European market. The current priority for domestic policy is to come to grips with the immediate problems of inflation and the balance of payments deficit.

BOARD AND EXECUTIVE

Since my last annual statement three new directors have joined the board. In early February, following our alliance with Banco Santander Group, Don Emilio Botin, their chairman, joined our board as did Mr George Graboys, the president and chief executive officer of Citizens Financial Group, following our acquisition of that company. Their contributions to our deliberations have already been of great value. On 1st October 1989, The Rt. Hon. George Younger was appointed a director, after a long and distinguished career in politics and government culminating in more than six years as Secretary of State for Scotland and, latterly, three years as Secretary of State for Defence. We are delighted to welcome him to our board and his contribution in the years ahead will, I am sure, be invaluable. At the annual general meeting three of our long serving non-executive directors will be retiring, Mr J. C. Roger Inglis, Mr Norman Quick and The Rt. Hon. Lord Thomson of Monifieth. Roger Inglis is currently our longest serving director, having joined the board of the former Royal Bank of Scotland in 1967. He joined the Group board in 1985. As one of Edinburgh's most distinguished lawyers he has served us well on a number of board committees and is presently chairman of the property committee and a member of the audit committee. Norman Quick joined the board of Williams & Glyn's Bank in 1978 and the Group board in 1985, following the merger of our two clearing banks. He has served as chairman of the audit committee since the merger in 1985 and he has guided this important committee with skill and understanding over an important period in the Group's development. We are delighted that despite his other commitments, he will be remaining on the board of The Royal Bank of Scotland for the present. George Thomson joined the board of the former Royal Bank of Scotland in 1977 after a distinguished career in journalism, politics and government, and, latterly, as an EEC commissioner in Brussels. This appointment to our board was

Statement by the Chairman

Continued

his first on returning to this country, an event of which we are proud. His help and advice to the board, particularly as our political adviser, has been considerable and to me personally as a wise counsellor and friend over the years. To all three of these retiring directors who have carried out their duties on the board in an exemplary and dedicated way, we extend our warmest thanks for all they have done. They will be greatly missed.

STAFF

Our ability to continue to broaden the Group's geographic base and expand the range of financial services which it offers, can only be achieved with the commitment of our staff. Similarly, in today's increasingly competitive environment, the need for companies to provide a friendly and efficient service is of paramount importance. Here again, our staff have a vital role to play. The success of the Group over the past year has been achieved through the sterling efforts of all our staff and in recognition of this your directors have decided that all participants in the Group's profit sharing schemes should receive a special cash payment equivalent to 2·1 per cent. of their salaries. I would like to offer my sincere thanks and those of my board colleagues to all of them for their efforts.

FUTURE OUTLOOK

In an ever-changing environment we must be prepared constantly to change not only in response to the needs of our customers but also to manage change in anticipation of their needs in the future. During the coming years, we intend to broaden our horizons by building on our existing international operations. In Europe, 1990 will see a further strengthening of our alliance with Banco Santander Group and, with 1992 firmly in mind, we intend to extend our European operations should the right opportunities arise. As mentioned earlier, Citizens Financial Group will be used as the base for the expansion of our presence in the U.S. retail banking market, especially in New England. Whilst the slowdown in the U.K. economy will make trading conditions difficult in the coming year, I am confident that the exciting developments planned for the Group, will provide a sound basis for future growth and that we will continue to consolidate our position as one of the leading U.K. financial services groups with our unique asset of having our headquarters firmly established in Scotland.

Michael Herries

29th November 1989

Report by the Group Chief Executive

GROUP RESULTS

In the year to 30th September 1989, the Group's operating profit reached the record level of £336.5 million. This satisfactory operating performance together with a 26.7 per cent. increase in total assets to £27.4 billion reflects the achievement, this year, of our aim to assure our shareholders of steadily growing returns into the future.

Additional exceptional provisions of £108.3 million in respect of lending to nine rescheduling countries have been charged to the profit and loss account as an exceptional item. The Group's medium and long term exposure to these countries totals £191.8 million and there is an additional £57.0 million of interbank and trade facilities. The exceptional additional provisions result in total specific provisions of £186.2 million in respect of these commitments and we believe that there should be no need for further exceptional provisions in the future.

Profit contributions from the Group's six main operating subsidiaries were as follows:

	1989 £m	1988 £m
The Royal Bank of Scotland	289.4	272.0
Charterhouse	53.4	35.1
Citizens Financial Group	22.1	—
RoyScot Finance Group*	24.1	27.8
Direct Line Insurance	8.1	4.0
Capital House	1.2	(2.1)

* includes A. T. Mays

The level of operating profit achieved by The Royal Bank of Scotland represented an increase of 6.4 per cent. over the previous year. Net interest income increased by 17.8 per cent. reflecting continued growth in lending volumes and the impact of higher base interest rates throughout the year. Term loans grew significantly and overdrafts have also shown good growth in recent months. Average mortgage balances were 37·1 per cent. higher than last year although latterly, growth has slowed following the downturn in demand. The deposit mix continued to change to more expensive deposits following the introduction of interest paying current accounts. It is pleasing to report that these accounts have been a marked success with balances now in excess of £300 million. Gold Deposit Account average balances grew by 66.1 per cent. over the past year to almost £1.3 billion. Commission and fee income increased by 11.8 per cent., with good growth in service charges and facility fees. Operating expenses increased by 18.1 per cent., notably as a result of the re-introduction of a pension fund charge arising from the application of a new accounting standard. The "normal" bad and doubtful debt charge was £13.3 million higher than the charge for the previous year.

At Charterhouse, an excellent performance saw profits for the year increase by £18.3 million. Most areas of the business contributed to an underlying 22.0 per cent. improvement. These included the capital markets division and corporate finance department of Charterhouse Bank where healthy performances produced higher fees and other income. Additionally, Charterhouse Development Capital maintained its impressive record of profitable investment activity and Charterhouse Tilney has returned to profitability having substantially increased its research capability. Other operating income benefited from the receipt of profits, deferred from an earlier year, from the Charterhouse shareholding in Distillers.

The acquisition of Citizens Financial Group was completed on 16th December 1988 and its performance in the period to 30th September 1989 bears very favourable comparison with its competitors in the New England area of the U.S.A., given the impact of reduced interest margins arising from the prevailing high interest rate environment. Profits in the post-acquisition period amounted to U.S.$35.8 million, which translates to £22.1 million, and this provides encouragement for the future.

In a year of difficult trading conditions, RoyScot Finance Group contributed £21.5 million to our operating profits. Although business levels remained strong throughout the year, the effect of higher interest rates had an unfavourable impact on most of the subsidiaries in this division. The recent considerable investment programme to consolidate various functions and subsidiaries, however, leaves RoyScot well placed in its highly competitive marketplace. A. T. Mays continued to expand its branch network and, in a poor year for the travel industry, achieved an operating profit of £2.6 million.

Direct Line Insurance had an outstanding year with a 102 per cent. improvement in profits. Both motor and creditor insurance recorded good increases compared to last year, the former benefiting from a mild winter. The household insurance business continued to develop and, while not yet profitable, we are confident of its long term prospects. A higher level of investment income was earned on funds deployed in the money markets as a result of the higher level of interest rates.

The confidence in the prospects of Capital House we expressed last year was rewarded with the expected return to profitability. There was healthy growth in fee income with a rising level of funds under management during the year which now stand at £2.6 billion.

IMPLEMENTATION OF GROUP STRATEGY

Our purpose as a Group is to create shareholder value by actively managing a complementary set of financial businesses to meet customer needs in both personal and corporate markets. The core elements of our strategy are: the development of cross-selling opportunities between different elements within the existing Group and the broadening of our horizons by targeted expansion of our financial services base and geographical spread into new markets and businesses through which we can build significant inter-relationships.

We have chosen this strategy for two reasons. First, the needs of our customers are increasingly complex and can best be met by drawing on the resources of the Group as a whole, rather than simply on the resources of one company. Secondly, by building inter-relationships between new and existing parts of the Group, we can broaden our income base and increase the contribution from fee income. We can also reduce hitherto near total dependence on the U.K. economy through profitable expansion of overseas operations and thus increase our return to shareholders during a period when our markets are becoming increasingly competitive. We believe that this strategy is the best way for the Group to add value to its subsidiaries and so enhance the return to shareholders and the service to customers.

During the past year we have implemented a number of major initiatives in support of this strategy. Internationally, through the development of our alliance with Banco Santander Group and the completion of the acquisition of Citizens Financial Group, we are now positioned to serve a wider clientele and are actively investigating further opportunities in both Europe and the U.S.A. We have continued to expand The Royal Bank of Scotland's branch coverage in England, while simultaneously developing our tele-marketing capabilities through Direct Line Insurance and the consumer banking division of the Bank.

Our alliance with Banco Santander Group and our life assurance joint venture with Scottish Equitable Life Assurance Society are major advances in the development of our strategy. Both offer the prospect of combining services and methods of delivery to meet customer needs more effectively. As a result, we will shortly be in a position to offer an integrated home finance package to our personal customers by drawing on the resources of The Royal Bank of Scotland for funding, of Direct Line Insurance for home and contents insurance, and of the new joint venture life company for life assurance cover. Similarly, by using Banco Santander's A.T.M. network and the newly-created link between our data processing systems, The Royal Bank of Scotland is unique amongst U.K. banks in offering our customers access from Spain to their accounts in the United Kingdom. In forging our alliance with Santander and our insurance joint venture we have diversified into new markets which offer the prospect of significant complementary relationships with our core businesses.

BALANCE SHEET STRENGTH

The continuing expansion of the Group's business both at home and overseas is dependent on the size and strength of its capital base. With this in mind, therefore, we obtained approval at an extraordinary general meeting in August 1989 to issue non-cumulative preference shares denominated in both sterling and U.S. dollars. We have already taken advantage of the more favourable conditions in the U.S.A. to raise $200 million in dollar preference shares and in so doing we became the first company registered in Scotland to obtain a listing on the New York Stock Exchange. We have the flexibility to make further preference share issues either in the U.S.A. or the United Kingdom. Our balance sheet was further strengthened by virtue of the three for two share issue in September 1989 following the capitalisation of certain of the Group's revaluation reserves. These steps, together with the loan capital issues totalling U.S.$650 million which we made during the year, have enabled us to increase our capital without seeking to raise additional funds from shareholders; and this continues to be our policy.

FUTURE AIMS

While remaining firmly committed to our home market in the United Kingdom, we shall continue to explore international opportunities arising in the major developed markets of the world. Particular emphasis will be placed on the development of our alliance with Banco Santander Group in Europe and on the expansion of our retail banking activities in the New England States of the U.S.A. through Citizens Financial Group. The development of new and shared technologies will continue to be a priority with a view to increasing profitability, providing new marketing systems and facilitating new product development.

Our ultimate aim is to maximise the quality of service to our customers, the returns for our shareholders and the job satisfaction of our employees.

OPERATIONAL REVIEW

PERSONAL FINANCIAL SERVICES IN THE UNITED KINGDOM

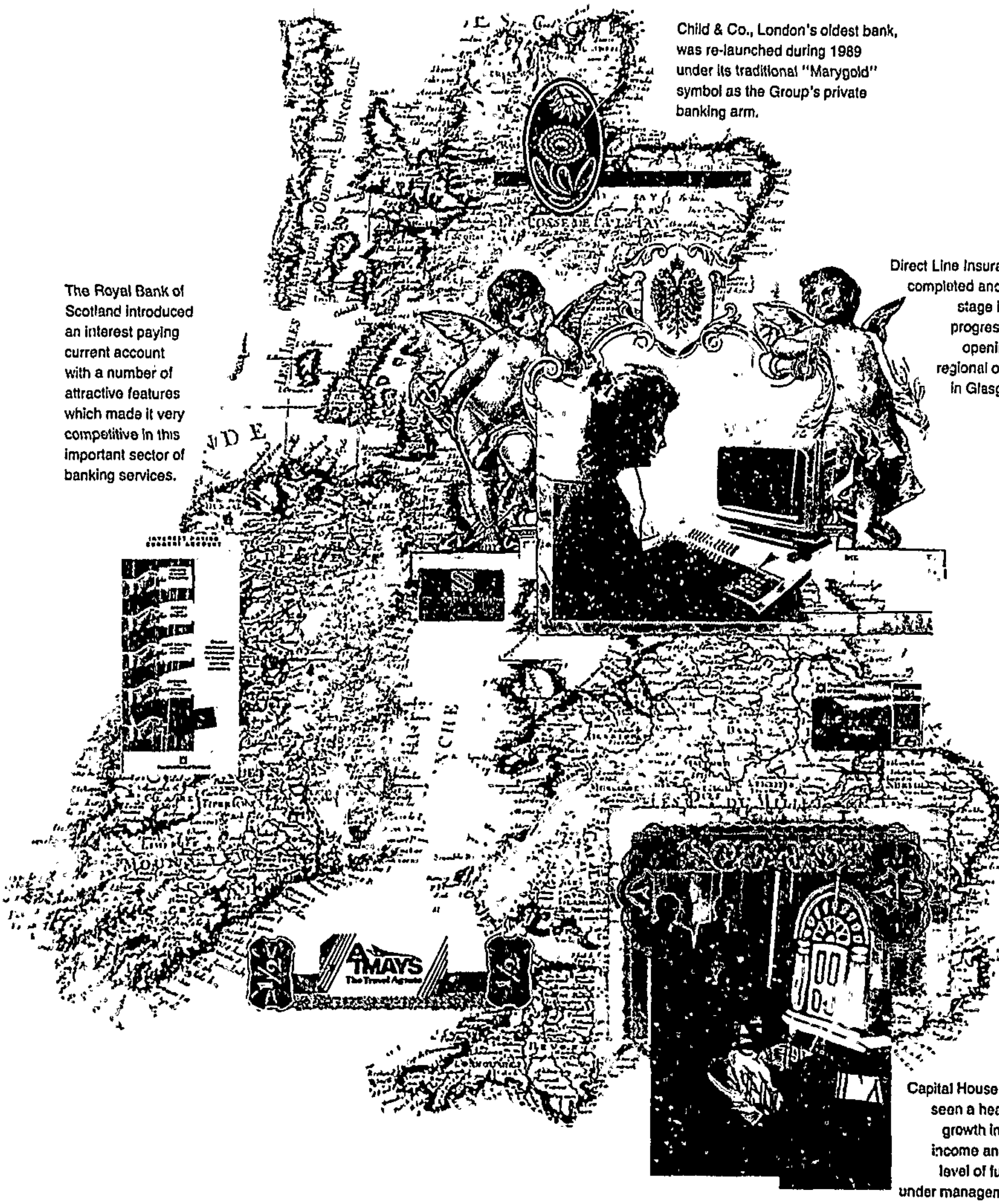
The core business of The Royal Bank of Scotland continued to prosper during the year despite the more difficult trading conditions. An important development was the launch on 1st March 1989 of an interest paying current account, backed by a major press and television advertising campaign. This new account has been instrumental in attracting a significant number of new customers and has also been well received by existing customers. The Bank's branch network in the United Kingdom has continued to expand in England into areas identified as offering profitable opportunities. New branches have been opened at Loughborough, Milton Keynes, Truro, Hanley, Maidenhead, Stoneleigh and Clifton, Bristol. Work is progressing on a further 15 branches with most of these anticipated to open by the end of September 1990. An additional significant property development in the Bank was the purchase of 18.3 acres of land at South Gyle, Edinburgh in January of this year. Planning permission has been granted for developing this site as a new administrative building and work on the first phase, which will extend to around 300,000 square feet, commenced in July. It is expected that this building will be ready for occupation by July 1992 and will accommodate over 1,300 staff to be relocated from other less suitable premises in Edinburgh.

The Bank's mortgage book continued to grow over the year as a whole, despite the high mortgage rate and the decline during the latter part of the year in the demand for mortgages. The Gold Deposit Account has continued to be popular with customers, and the enhancements made last year to that account and the Premium Account have ensured that the Bank's high-interest savings accounts continue to compete effectively in the marketplace.

Child & Co., London's oldest bank, was re-launched during 1989 under its traditional "Marygold" symbol as the Group's private banking arm.

The Royal Bank of Scotland introduced an interest paying current account with a number of attractive features which made it very competitive in this important sector of banking services.

Direct Line Insurance completed another stage in its progress by opening a regional office in Glasgow.



Capital House has seen a healthy growth in fee income and its level of funds under management has increased.

Report by the Group Chief Executive

Continued

During the year, Child & Co., Bankers was re-launched as the Bank's private banking arm. Based at No. 1 Fleet Street, London, Child & Co. has a tradition stretching back over 400 years of providing a high quality personal banking service to discerning clients. Child & Co. will continue to develop and refine its individual style of private banking to look after a wider selection of personal, professional and corporate clients.

Direct Line Insurance, which provides motor, household and creditor insurance products, has progressed to become the largest exclusively direct insurer for motor and home insurance in the United Kingdom. The volume of insurance underwritten continues to grow rapidly and, for the second successive year, not only was an underwriting profit made on the motor account but with yet a further reduction in the operating ratio. The company, which has a significant customer database of its own, broadens the overall Group customer database and provides additional opportunities for the cross-selling of financial services and products among other companies in the Group.

The year under review has been one of rapid change in the provision of plastic card services. In responding to these changes, The Royal Bank of Scotland has launched its own Visa credit card to give customers a further choice in the methods available to them of payment for goods and services. The Bank, in conjunction with other banks, continued to develop the Switch debit card scheme, which is now a major payment system within the United Kingdom. In addition, the launch of its new multi-function card, Highline, which provides cash dispenser, cheque guarantee and electronic payment facilities by use of a single card, has been well received. The Bank also played an active role in the inaugural service of national EftPos (electronic funds transfer at point of sale) which was launched in three separate locations during September 1989. The Style credit card operation, managed by RoyScot Financial Services, continued to expand into northern England and it is planned to continue the phased expansion of this business to give eventual national coverage. As a Group, we shall continue to develop our range of plastic card products, to seize new opportunities and to meet the needs and demands of our customers.

In what has been a difficult trading year for the provision of travel services, A. T. Mays has continued to expand its network to almost 300 branches, consolidating its position as the fourth largest of the high street travel agents. With the assistance of our Group services company, Royal Bank Group Services, A. T. Mays is now carrying out an upgrading of back office systems which will further increase efficiency.

A number of technological developments are in hand and these are aimed primarily at enhancing the opportunities for the cross-selling of services among the operating divisions of the Group. An example of this is the exciting new customer-operated information unit, with an interactive video-screen, which is based on computer programs developed by a team within the Group services company. These units, which have been installed at a number of locations within the Group, provide customers with accurate, up-to-date information on a wide range of Group products such as personal loans, mortgages, motor and household insurance and travel offers. Following the success of a pilot Phoneline scheme, which utilises speech recognition techniques, a nationwide scheme is now being developed to enable personal customers of The Royal Bank of Scotland to deal directly with their banking business through ordinary telephone handsets.

Many additional facilities have been provided to branches of the Bank to enable them to handle the increasing workload resulting from the introduction of new products and services. This work has included the introduction of database technology to provide the branches and head office functions with the information required to assist them in serving customers efficiently.

A further technological development was the availability from 1st July 1989 of a facility for Royal Bank of Scotland customers to withdraw cash from their accounts through a number of Banco Santander's cash dispensers in Spain. In addition, Banco Santander issued Cashline-style cards to its student customers for use in our Cashline network on visits to the United Kingdom.

While uncertain stock market conditions and persistent adverse investor sentiment were in evidence throughout the year, Capital House Investment Management continued to develop its high quality investment management services. In particular, two new products, PEP Capitaliser and the Smaller Companies Trust, were launched during the year. The new Capital House Asset Management Portfolio service for investors of £10,000 to £100,000, has been very successful, attracting nearly £6 million.

Our stockbroking service, provided by Charterhouse Tilney, has continued to increase its regional coverage both organically, through the opening of a new office in Aberdeen and the recruitment of an additional sales team in London, and by the acquisition of the Peterborough office of Buckmaster & Moore. As a result of this expansion, Charterhouse Tilney has gained new clients with an aggregate portfolio value of approximately £250 million. Charterhouse Tilney also provides a share dealing service for customers of The Royal Bank of Scotland.

The Royal Bank of Scotland continues to provide a successful executor and trustee service and will be introducing a computerised personal taxation advisory service in advance of the introduction of independent taxation in April 1990. Our new life assurance joint venture with Scottish Equitable Life Assurance Society will result in the Bank becoming an appointed representative of the joint venture company for the purposes of the Financial Services Act. It is expected that this change in our polarisation stance will also enable us to market the investment products of Capital House direct to customers of The Royal Bank of Scotland. This has not been possible hitherto because of the Bank's status as an independent intermediary. Independent advice will, however, still be available to those of our customers who require it through a separate company, Royal Bank Insurance Services, which will continue to operate largely as before.

Financial services for corporate customers in the United Kingdom

All of the divisions in the Group involved in the corporate sector have placed emphasis on the broadening of their client bases to ensure growth in profits and increased fee-based income.

The Royal Bank of Scotland has a long tradition of serving the banking needs of corporate customers in all sectors of the market. In particular, the Bank is committed to helping small businesses become established, to expand when and where appropriate and to survive temporary difficulties. To emphasise its commitment to small businesses, the Bank has produced a 20-minute business information video titled "Planning for Profit" which complements its range of business information booklets.

Royline, The Royal Bank of Scotland's desk top banking system for the business customer, continues to increase its client base at a steady rate and a significant feature has been the number and quality of new business customers attracted to the Bank in order to take advantage of this service. A number of enhancements and new facilities are planned for Royline over the coming years. These developments are aimed at strengthening the Bank's relationship with the business community and providing the service required by business customers direct to their own offices, where it is of most use to them.

The Bank has also introduced a new credit card transaction handling service called Roynet. Roynet will allow retailers to deal with the Bank for all Visa, Access, Mastercard, Eurocard and Switch transactions which will be of great benefit to the many retail customers who accept credit cards and at no extra cost to them. Roynet will be particularly useful for handling the new Switch electronic debit card. It is anticipated that some ten million Switch cards will be in use by the end of 1989 and they will be accepted through over 30,000 retailer terminals.

Charterhouse Bank's corporate finance department was very active during the year in support of existing and new clients including News International and Ladbroke Group. The department also assisted its clients in a number of rights issues including two by Queens Moat Houses for a total of £204 million. In all, the department

Royline, The Royal Bank of Scotland's desktop banking system, has continued to increase its client base. Further enhancements to the system are planned for the future

Charterhouse Bank advised Plaxton Group plc on its successful acquisition of Hanly's and on treasury management, and provided subordinated capital for its asset finance company.

Report by the Group Chief Executive

Continued

was involved in 89 transactions totalling £2.9 billion.

Charterhouse's range of services to the corporate customer has also been enhanced by the setting up of a new syndications unit within the corporate banking division. This division provides a highly sophisticated debt financing service, specialising in property and acquisition financing. In a growing number of transactions it has assisted corporate finance and development capital clients by arranging, structuring and syndicating senior and mezzanine debt.

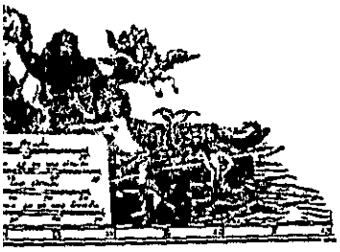
The Group's capital markets division in Charterhouse Bank has completed its first full year of trading at a profit, trading actively in the capital markets and advising a wide range of corporate and institutional customers, of both Charterhouse and The Royal Bank of Scotland, on exchange rate and interest rate hedging, capital structuring, cash flow and treasury management. The division has developed sophisticated techniques for eliminating risks involved in domestic and cross border acquisitions and financial structures designed to maximise value to shareholders. Corporate customers have welcomed the manner in which the division has worked closely with other divisions of Charterhouse and the Group. Its approach has been particularly effective in bringing together the mix of services and resources available from the Group in addressing customers' requirements. The care taken in identifying the tax, accounting, legal and regulatory implications of services provided for corporate finance directors and treasurers has proved important in building stronger relationships with customers.

Charterhouse Development Capital has successfully raised a second £200 million buy-out fund and has now closed its original £100 million buy-out fund. Investors in the new fund comprise leading institutions from around the world including Japan, the United Kingdom and the U.S.A.

In the year under review Charterhouse led the buy-outs of ABI Caravans, Oyez Stationery, Tyzack and the refinancing of MFI. Tyzack was a listed company, and Charterhouse Development Capital worked closely with the corporate finance department within Charterhouse on this transaction. It is the combination of financial advisory skills, provided by the various divisions of Charterhouse Bank, and the investment skills and capacity of Charterhouse Development Capital, which has enabled Charterhouse to maintain its position as one of the market leaders advising and investing in management buy-outs.

Charterhouse Development Capital also continued to invest in a large number of smaller management buy-outs and buy-ins and other unlisted companies including Addison Design Consultants and Fountain Forestry. During the year, some 50 investments were made, totalling over £65 million.

Within RoyScot Finance Group, RoyScot Corporate Leasing provides specialist funding for major U.K. companies in the finance of fixed assets. The value of assets financed increased significantly during the year with continued success being seen in the aircraft industry, an example being the investment in a consortium company with other major lessors and British Airways, to finance British Airways' replacement 747 fleet. Support was also provided to industry in manufacturing and distribution and to the leisure industry through the Aonach Mor ski development near Fort William. Commercial instalment finance for vehicles, plant and equipment is provided by RoyScot Trust, which wrote record levels of business again, and opened new branches during the year in Cardiff, Hull, Hickley and Kilmarnock, reinforcing the company's emphasis on the speed of service to local business communities. RoyScot Drive provides fleet vehicle management services, including vehicle funding, location and acquisition, maintenance, administration and disposal. A substantial restructuring of the company took place during the year to match its heightened market share and profile. RoyScot Factors, providing a full range of cash flow management services, continued to attract new customers and market share and against a background of sluggish retail spending, RoyScot Financial Services entered into agreements with major retailers for the development of its



Report by the Group Chief Executive

Continued

Style credit card and continued the growth of its own-brand card business.

In serving the corporate community, Charterhouse Tilney has increased its corporate brokerships from 23 to 36 during the past 12 months, all in business sectors in which Charterhouse Tilney has a specialist research capability. Corporate broking activity was at a record level during the year and included the successful completion of Charterhouse Tilney's first contested takeover bid as sole broker acting for Anglo United in its £478 million acquisition of Coalite. Service to institutional clients was enhanced by the recruitment of seven new teams of high quality analysts, extending coverage to around 60 per cent. by value of the FT All Share Index. Charterhouse Tilney's international department provides a high quality research service on medium sized French stocks, and has also recently strengthened its U.K. equities team serving European institutions.

Capital House provides quality pension fund management expertise for institutional clients and The Royal Bank of Scotland continues to have a major presence in the market as company registrars and as unit trust trustees. Although volumes of work in the registrar's department have not returned to pre-1987 levels, there has been high activity in the field of capital operations work with a heavy involvement in company mergers, rights issues, employee share schemes and scrip dividends.

International business

Our international business has developed during the past year in line with our strategy of targeting opportunities in Europe and north-eastern America. This will enable us to maximise the benefits of the single unified European market planned for 1992 and to secure a foothold in the important U.S. financial marketplace, the world's largest banking market, thereby broadening our sources of profit and geographic capability.

The acquisition of Citizens Financial Group, completed in December 1988, was an important step towards achieving growth and long term profit ambitions in what is a major world economy. It has a strong deposit base, a high quality loan portfolio, earnings growth potential, good management and no exposure to rescheduling countries or to energy-related loan business. It is well placed for expansion and we are committed to developing Citizens as a flagship to lead the expansion of our U.S. banking services for personal and corporate customers. Citizens prides itself on the quality of service provided to its customers and continues to develop and enhance its full range of services which include deposit products, trust services, retail lending, a comprehensive range of mortgage products, credit cards, automated banking and corporate banking. A priority has been the maximisation of technology transfer opportunities between Citizens and other Group subsidiaries and arrangements are in hand for The Royal Bank of Scotland to supply international services to Citizens' customers. This will provide Citizens with an international edge. In addition, tangible benefits have already been seen for Citizens' funding operations as a result of its becoming a subsidiary of the Group. The Royal Bank of Scotland's operations in the U.S.A. once again produced excellent results and the executive vice-president of the Bank's northern American operations was elected to the board of Citizens with a view to cementing closer relations between the Bank and Citizens.

It is now just over one year since we announced our alliance with Banco Santander Group with a view to meeting our objective of providing a service in Europe to our U.K. customers with interests abroad and generating profit from indigenous customer bases there. The alliance has made considerable progress during the year and has provided us with the capacity to be in the financial markets in Spain, Germany and Belgium. As a result, a range of attractive opportunities, in which we would otherwise have had no opportunity to participate, have come our way. To meet our aims for development of the alliance we are in the process of establishing a jointly-owned subsidiary, Royal-Santander Financial Services SA, to provide assistance for either British customers looking for opportunities in Spain or

Report by the Group Chief Executive

Continued

Spanish customers looking for opportunities in the United Kingdom. This company will have offices in Madrid and the Costa del Sol which can provide valuable practical advice on business and financial matters, acting as the initial point of contact in the co-ordination of the full range of services offered by both banking groups.

In Germany, the jointly-owned CC-Bank's strategy has been to concentrate on the consumer credit market in which it is already well established. This strategy has been further refined to target specific niche markets in conjunction with other, complementary, local organisations. During the year, our other joint investment with Banco Santander Group, Credit du Nord Belge was renamed CC-Banque Belgique. A number of additions have been made to the senior management of this bank and a strategic review has been undertaken to ensure effective use of resources and identification of target markets.

On 31st July 1989, The Royal Bank of Scotland (Gibraltar) opened for business. Jointly owned by both banks and managed by The Royal Bank of Scotland, the new bank provides a wide range of offshore financial products and services to the expatriate community in southern Spain, Portugal and Gibraltar. It is also able to meet the needs of local residents and the prospect of a new bank with the strength of two major banks in their respective countries behind it has attracted many approaches from both customers and potential customers and much valuable business is already being transacted.

A further feature of the development of the alliance has been co-operation between the development capital arm of Charterhouse and Banco Santander de Negocios, the merchant banking subsidiary of Banco Santander Group, in raising funds for Vista, an investment company, for which it is intended that £25 million be raised. In addition, Charterhouse and Banco Santander de Negocios have also jointly invested in the £14.5 million management buy-in of Cuallado SA, the Madrid-based parcels-delivery service.

Charterhouse has expanded significantly its network of international relationships by closely linking its investment expertise and capacity with a customer needs driven advisory service. Access to new markets and to the corporate finance opportunities which will arise from them is given by Charterhouse's association with a number of respected financial groups.

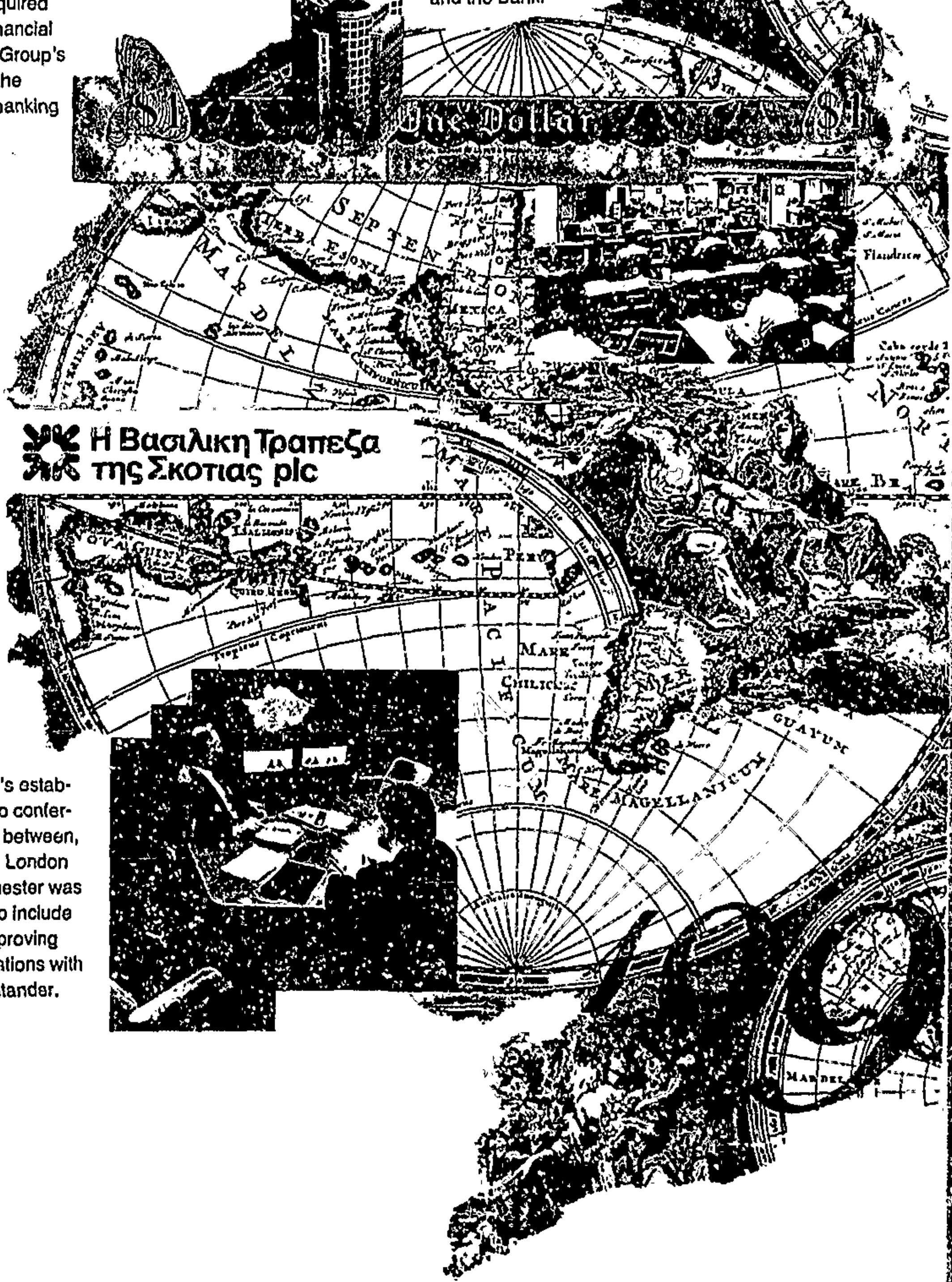
In Germany, Charterhouse, along with Nomura, GE Capital and a number of other major institutions, has taken a minority stake in Matuschka Gruppe, a leading independent non-bank financial services group whose activities include corporate finance, development capital and investment management. In Italy, Charterhouse has formed an alliance with Basinvest SpA, a merchant bank formed by Banco de Sicilia, the eighth largest bank in Italy. Basinvest's activities include direct investment, mergers and acquisitions and capital markets' finance.

These new alliances, together with the close relationship which Charterhouse enjoys with Banco Santander de Negocios, continue the expansion started in 1988 when Charterhouse formed development capital joint ventures in Sweden and France. Charterhouse has been active in the development capital industry in France for some 15 years, through Charterhouse Associates which manages FF700 million of funds and has invested in some 80 companies, and DEFI, a FF400 million investment company in which Credit National, Elf Aquitaine, Parfinance and a number of other leading French institutions are investors. Basinvest, Matuschka, Banco Santander de Negocios, Credit National and Alven, the joint venture Swedish investment company, are all founder limited partners with Charterhouse in Charterhouse European Partners (CEP), a £100 million fund, which will be managed by Charterhouse, for investment in corporate restructuring throughout Europe. All the founder limited partners have themselves committed capital and will provide CEP with vital links into Europe's national markets.

In the U.S.A., Charterhouse's recently expanded corporate finance office continues to work closely and profitably with Charterhouse Group

The Royal Bank of Scotland's operations in the U.S.A. produced excellent results. Closer relations are being cemented between Citizens and the Bank.

A new headquarters is being built at Providence for the recently acquired Citizens Financial Group, the Group's flagship in the U.S. retail banking market.



The Group's established video conferencing link between, Edinburgh, London and Manchester was extended to include Madrid, improving communications with Banco Santander.

The official opening of The Royal Bank of Scotland (Gibraltar) in September was a significant step in the alliance with Banco Santander

The Group's traditional support for the Edinburgh International Festival was particularly appropriate in 1989 as it joined with Banco Santander to bring the Festival its first traditional Spanish 'zarzuela'.

In the summer of 1989, Royal Bank of Scotland's customers were able to withdraw cash from their accounts by using Banco Santander cash dispensers in Spain.

Report by the Group Chief Executive

Continued

International (CHUSA), its associate company, which has been making equity-related investments, primarily in leveraged buy-outs, since 1973. CHUSA has to date acquired 27 companies with a total aggregate purchase price of U.S.$850 million. During the year, it has also successfully raised a new equity fund of U.S.$265 million in which Charterhouse is a major participant.

The Royal Bank of Scotland, in addition to its other international operations, has traditionally been highly regarded in the field of global correspondent banking and, in order to build on its excellent reputation in this area of activity, a new branch, dedicated solely to providing a high quality service to foreign correspondent banks, was opened in London in the early spring of this year. This fully co-ordinated service, which was previously provided from a number of locations in the United Kingdom, has proved to be successful in attracting new accounts from a variety of banks in a highly competitive market.

The shipping industry has recovered well from recent depression and this has enabled The Royal Bank of Scotland to capitalise on its long history of uninterrupted involvement in this market by expanding business in terms of both lending and deposits. A high level of profitability was achieved in this sector during the financial year.

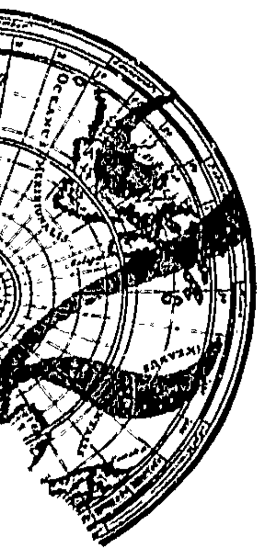
During 1989 we have also placed additional importance on the development of our services for the expatriate community as the need increases for international private banking products provided from an offshore location. International private banking services are now available from locations in Jersey, Guernsey, Isle of Man, Switzerland, Hong Kong, Singapore, the Bahamas and Gibraltar. An international private banking office, headquartered in London, has been established by The Royal Bank of Scotland and this will be responsible for developing high quality personal banking and financial counselling services for offshore customers. Development of the international private banking business will be undertaken in close co-operation with Capital House whose discretionary investment management service will be an integral part of the full range of services on offer.

BROADENING HORIZONS

We shall continue to develop our existing successful markets and to target new areas for future growth, both within the United Kingdom and overseas.

Above all, we aim to be different from our competitors by providing a service which is seen by our customers to be better, friendlier and more competitive and which also produces a maximum return for our shareholders.

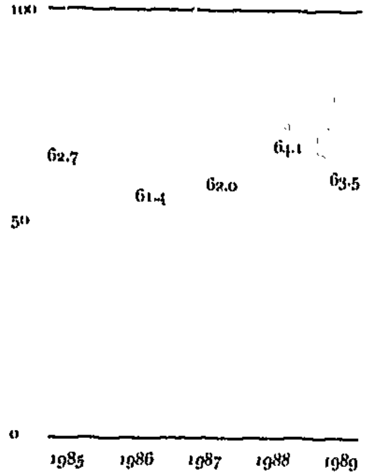
29th November 1989



Financial Review

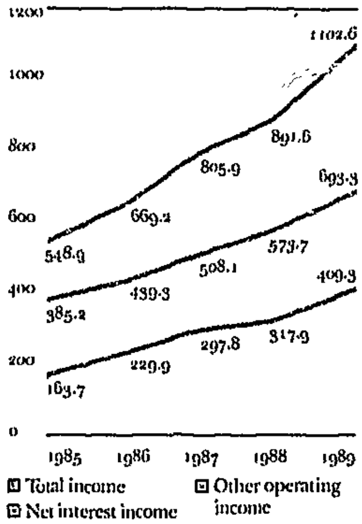
PERFORMANCE RATIOS

Cost to income ratio
PERCENTAGE POINTS



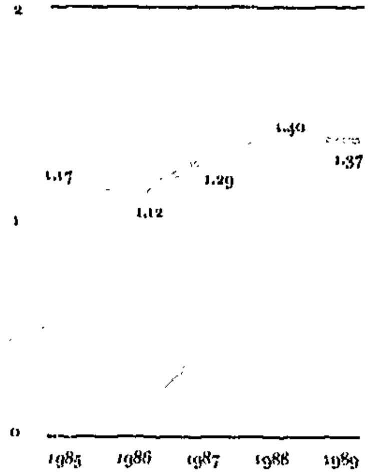
This ratio is constantly monitored, both on a Group and a divisional basis. Costs and income have been affected by a number of factors in recent years. However, the above graph depicts what we believe to be the true underlying trend in this important ratio. Profits arising from property sales, which were significant in 1986 and 1987, have been excluded while expenses in 1987 and 1988 have been adjusted to incorporate a pension fund charge. Finally, figures for A. T. Mays have been excluded as, in common with all travel agencies, it has a very high cost to income ratio and this distorts the overall Group position.

Analysis of income
£ MILLION



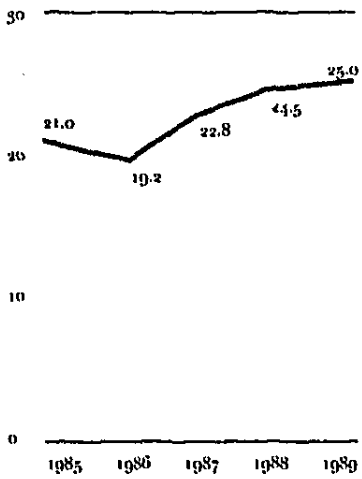
Total income showed a very encouraging 23.7 per cent. growth in 1989, increasing to £1,102.6 million. Volume growth was the major factor in a 20.9 per cent. increase in net interest income with average interest earning assets growing by 20.4 per cent. This arose in all areas of the Group with about 7 per cent. attributable to the acquisition of Citizens Financial Group. Higher interest rates were also a significant factor with average base rate 3.9 per cent. higher than in 1988.
An impressive 28.8 per cent. increase was achieved in other operating income. Good growth was evident in: banking fees, particularly service charges and facility fees—foreign exchange and arbitrage income—corporate finance fees and brokerage commission within Charterhouse—a first time contribution from Citizens Financial Group—insurance underwriting profits at Direct Line Insurance—travel commission in A. T. Mays.

Underlying pre-tax return on average total assets
PERCENTAGE POINTS



Adjusting for the distorting factors identified in the cost to income ratio, the underlying return on total assets shows a modest downturn this year from 1.40 per cent. to 1.37 per cent. The acquisition of Citizens Financial Group had an effect on the return. Although £1.9 billion was added to the Group's balance sheet, the acquisition was funded by borrowing and as a result there was little impact on the Group's profits.

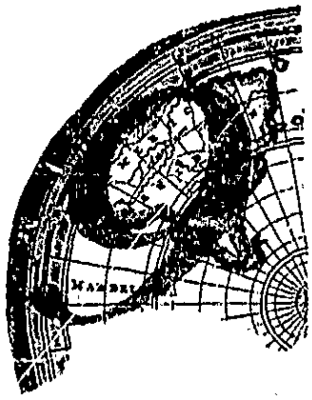
Underlying pre-tax return on average equity
PERCENTAGE POINTS



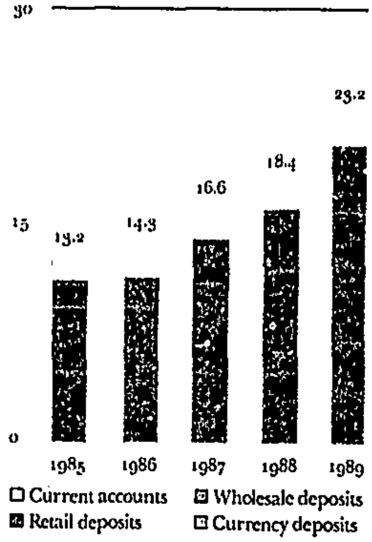
The above figures are again based on underlying profit figures. This ratio is regarded as one of the key profit measures and, accordingly, considerable importance is placed on the improving trend evident since 1986.

Financial Review

BALANCE SHEET ANALYSIS



Analysis of deposits by type
£ BILLION



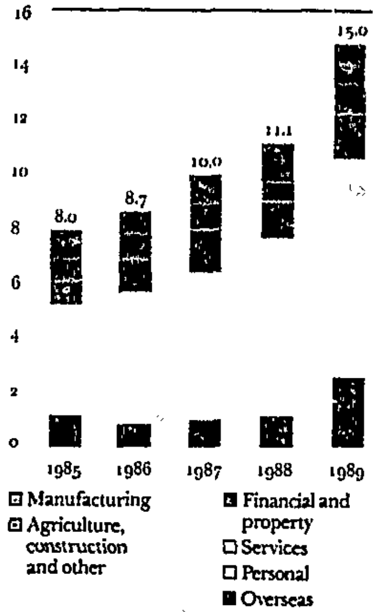
Total deposits increased by 25.9 per cent., from £18,439 million to £23,219 million. Interest-free current accounts were £209 million lower than last year. This was due to the introduction of interest paying current accounts in The Royal Bank of Scotland. The new account, balances on which are included in retail deposits, has proved extremely popular and over £300 million had been taken by 30th September 1989, a significant proportion of which represents 'new' money to the Group.

In addition to benefiting from interest paying current accounts, retail deposits reflect strong growth from the competitive Gold Deposit Account, giving overall growth of 33.7 per cent.

Wholesale deposits include customer bid deposits which have also shown good growth in the year. As a result, the increase in market funding has been modest.

Of the £2,426 million increase in foreign currency deposits, £1,653 million was attributable to the acquisition of Citizens Financial Group.

Analysis of advances
£ BILLION



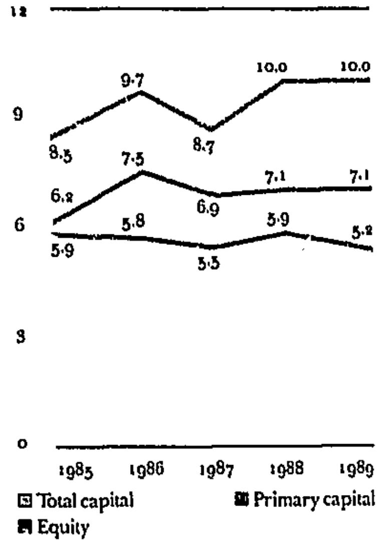
Good growth was achieved in all categories of advances to customers. Lending to corporate customers increased by 24.8 per cent. with demand for both overdraft and term loan facilities being particularly strong. House purchase lending at 30th September 1989 was 19.7 per cent. higher than at the same date last year although growth has slowed following the downturn in demand. Other personal lending continued to be strong.

Overseas lending more than doubled due to the Group's expansion in the U.S.A. and it now constitutes 17.6 per cent. of total advances to customers.

Financial Review

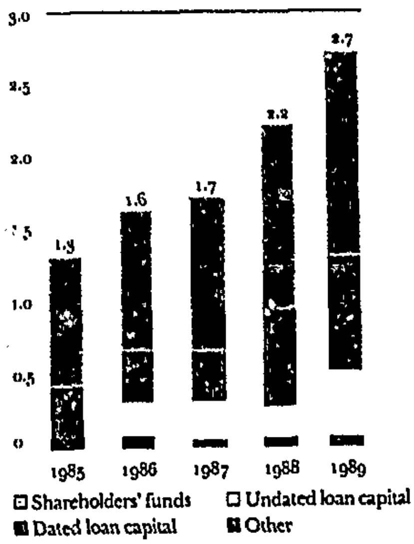
CAPITAL ADEQUACY

Capital ratios
PERCENTAGE POINTS



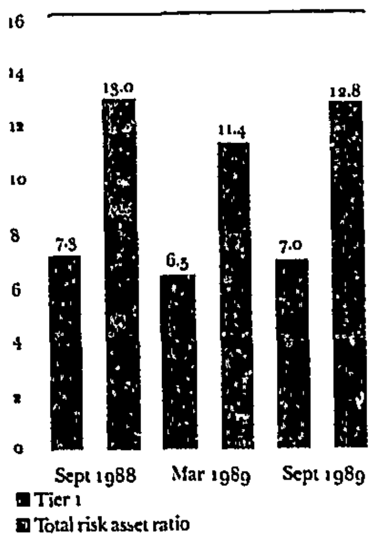
(1) Equity: total assets, where equity is share capital+reserves+minority interests.
(2) Primary capital: total assets, where primary capital is equity+the general provision for bad and doubtful debts+undated loan capital.
(3) Total capital base: total assets, where total capital base is primary capital+dated loan capital.
The risk asset and capital ratios on this page are also used to measure the adequacy of the Group's capital base and are closely monitored by management. Since 1st October 1988, the Group's equity increased by £141.0 million despite the additional exceptional provisions for rescheduling country debt. However, total assets increased by £5.7 billion causing a fall in the equity to total assets ratio to 5.2 per cent. Nevertheless, the ratio is at a very comfortable level.

Capital base
£ BILLION



During the year, we have significantly strengthened our capital base, which now stands at £2.7 billion. We have raised U.S.$200 million of preference share capital, U.S.$400 million of undated loan capital, and U.S $250 million of dated loan capital (see pages 31 and 32).
Thus, despite the additional exceptional provisions for rescheduling country debt, the capital base shows considerable strength, leaving us well placed for the future.

Risk asset ratio
PERCENTAGE POINTS

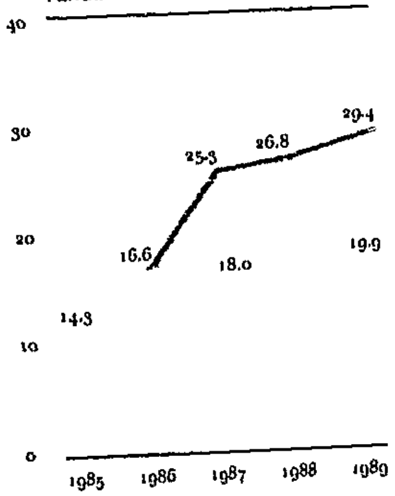


The strength of the Group's capital base is highlighted by the risk asset ratio. At 7.0 per cent. for the tier 1 ratio and 12.8 per cent. for the total risk asset ratio, the ratios compare very favourably, both with other U.K. banks and with the acceptable minimum ratios of 4.0 per cent. and 8.0 per cent. respectively.

Financial Review

SHAREHOLDERS' RETURNS

Earnings per share
PENCE

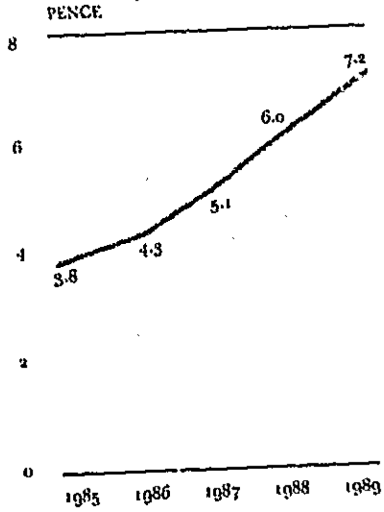


Adjusted for capitalisation issue.

⊡ Before exceptional items
☐ After exceptional items

Excluding the additional exceptional provisions for rescheduling country debt, earnings per share showed a steady growth with an improvement of 9.7 per cent. It is also noteworthy that the earnings per share figure for 1989, after the exceptional item, is nevertheless higher than that reported for each year with the exception of 1988.

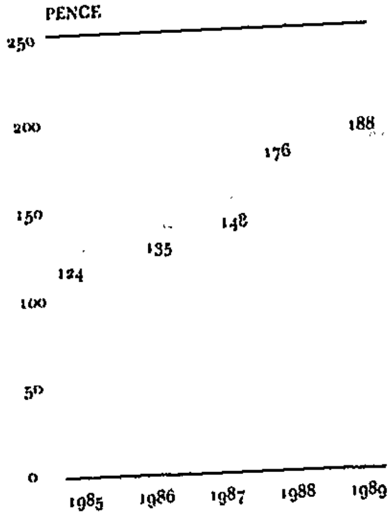
Dividends per share
PENCE



Adjusted for capitalisation issue.

The board of directors is recommending a final dividend of 4.8p per share, bringing total dividends to 7.2p per share for the year. The proposed 20 per cent. increase gives a compound growth rate of 17.3 per cent. since 1985 and continues the growth pattern of recent years. In the same period, annual inflation has grown at the compound rate of 5.1 per cent. Underlying dividend cover is a comfortable 4.1 times. Even allowing for the exceptional provision, dividend cover is a respectable 2.8 times.

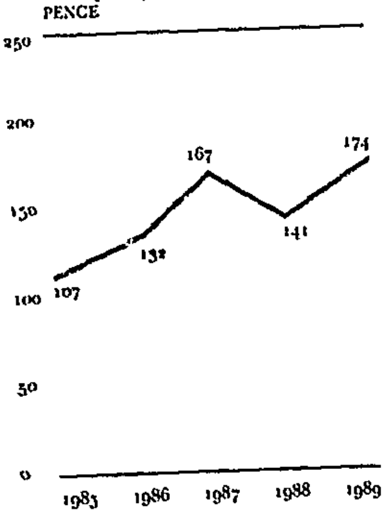
Net asset value per ordinary share
PENCE



Adjusted for capitalisation issue.

Since 1985, there has been a steady increase in the net asset value per share, reflecting the policy of making sufficient retentions to support future balance sheet growth.

Share price per ordinary share
PENCE



Adjusted for capitalisation issue.

The share price of the company's 25p ordinary shares has more than regained the high levels reached prior to the stock market collapse in October 1987.

Five-Year Financial Summary

	1985 £m	1986 £m	1987 £m	1988 £m	1989 £m
Profit before exceptional items	166.3	184.5	274.2	309.2	336.5
Exceptional items	—	—	77.0	—	108.3
Profit before taxation	166.3	184.5	197.2	309.2	228.2
Taxation	71.6	65.3	68.1	115.1	80.7
Profit after taxation	94.7	119.2	129.1	194.1	147.5
Earnings per 25p ordinary share*					
before exceptional items	14.3p	16.6p	25.3p	26.8p	29.4p
after exceptional items	14.3p	16.6p	18.0p	26.8p	19.9p
Dividends per 25p ordinary share*	3.8p	4.3p	5.1p	6.0p	7.2p
Dividend cover (times)	3.7	3.9	3.5	4.5	2.8

	£m	£m	£m	£m	£m
Issued share capital	72	72	72	73	189
Reserves	810	886	979	1,197	1,222
Shareholders' funds	882	958	1,051	1,270	1,411
Minority interests	3	5	5	8	8
Dated loan capital	338	357	345	637	786
Undated loan capital	—	242	215	207	462
Capital resources	1,223	1,562	1,616	2,122	2,667

	£bn	£bn	£bn	£bn	£bn
Deposits and customers' current accounts	13.2	14.3	16.6	18.4	23.2
Advances to customers and other accounts	10.7	11.0	12.6	13.7	19.1
Total assets	15.0	16.6	19.1	21.7	27.4
Bank branches	878	864	856	857	905
Other branches	49	51	61	342	394
Average number of employees	17,718	18,609	19,557	23,174	26,530
Average base rate	11.8%	11.1%	10.2%	9.3%	13.2%

*Earnings and dividends per 25p ordinary share have been adjusted to show the effects of the capitalisation issue in September 1989.

Directors and Officers

Chairman
*Sir Michael Young-Herries, OBE, MC, JP, LLD, DLitt

Vice-chairmen
Peter Edward Gerald Balfour, CBE
Sir Austin Pearce, CBE, DSc

Directors
The Rt. Hon. The Earl of Airlie, KT, GCVO, PC, JP
*Maurice Victor Blank
Emilio Botin-Sanz Sautuola y Garcia de los Rios
†Sir Robin Duthie, CBE, LLD
*Henry Edward Farley
*George Graboys
Ian Faulconer Heathcoat Grant, JP, DL
Henry Louis Carron Greig, CVO, CBE
†Angus McFarlane McLeod Grossart, LLD
Alexander Macdonald Hamilton, CBE, JP
†James Craufuird Roger Inglis
John Nigel Courtenay James, FRICS
*Robert Mitchell Maiden
*Dr George Ross Mathewson, CBE, LLD, FRSE
†Norman Quick, CBE, DL, LLD, MA
†Charles Frederick Eardley Shakerley
*Kenneth Thompson
Sir Adam Thomson, CBE, LLD
The Rt. Hon. Lord Thomson of Monifieth, KT, PC, LLD, DLitt, DSc, FEIS
*Charles Milne Winter
The Rt. Hon. George Kenneth Hotson Younger, TD, PC, DL, MP

*Executive †Member of the audit committee

Group chief executive
Charles Milne Winter

Deputy group chief executive
Henry Edward Farley

Secretary
Miller Roy McLean

Registrars
The Royal Bank of Scotland plc
PO Box 435 Owen House 8 Bankhead Crossway North
Edinburgh EH11 4BR

Auditors
Deloitte Haskins & Sells, Chartered Accountants
Edinburgh and London

Registered office
36 St Andrew Square Edinburgh EH2 2YB
Telephone: 031-556 8555

The Royal Bank of Scotland Group plc is registered in Scotland No. 45551

Non-Executive Directors

Peter Balfour (age 68) vice-chairman, is also chairman of Charterhouse plc. He is president of the Scottish Council Development and Industry and has a number of other directorships including British Assets Trust PLC.

Sir Austin Pearce (age 68) vice-chairman, is chairman of Oxford Instruments Group plc and a director of Jaguar PLC, Pearl Group PLC and Smiths Industries plc. He was formerly chairman and chief executive of Esso Petroleum Company Limited and was chairman of British Aerospace PLC until his retiral in 1987. He is also a member of the Panel on Take-overs and Mergers.

Lord Airlie (age 63) is Lord Chamberlain of The Queen's Household. He is chairman of General Accident Fire and Life Assurance Corporation plc and, until 1984, was chairman of Schroders plc, the London merchant banking group.

Don Emilio Botin (age 55) is chairman of Banco de Santander, S.A. He is a director of a number of Spanish companies.

Sir Robin Duthie (age 61), a chartered accountant, is chairman of Britoil plc and a former chairman of the Scottish Development Agency and is a director of a number of public and private companies. He is also chairman of Capital House Investment Management Limited.
(Member of the audit committee.)

Ian Grant (age 50) is managing director of Glenmoriston Estates Limited and is chairman of Pacific Assets Trust plc. He is a director of a number of public and private companies.

Carron Greig (age 64) is chairman of Horace Clarkson PLC and a former chairman of the Baltic Exchange in London.

Angus Grossart (age 52) is chairman and managing director of Noble Grossart Limited. He is chairman of Edinburgh Fund Managers PLC and Scottish Investment Trust PLC and his other public directorships include Alexander and Alexander Services Inc. (U.S.A.), Globe Investment Trust plc, Hewden-Stuart plc and Scottish Television plc.
(Member of the audit committee.)

Alistair Hamilton (age 64) is joint senior partner in the Glasgow firm of solicitors, McGrigor Donald, and is a past president of the Law Society of Scotland.

Roger Inglis (age 64) recently retired as a senior partner of Shepherd & Wedderburn W.S., solicitors, Edinburgh. He is chairman of British Assets Trust PLC and has a number of other directorships.
(Member of the audit committee.)

Jimmy James (age 54) is a trustee of the Grosvenor Estate, London. He is a director of Sun Alliance Insurance Group plc and is a past president of the Royal Institution of Chartered Surveyors.

Norman Quick (age 67) is chairman of Quicks Group plc and he is a member of the Court and Council of the University of Manchester.
(Chairman of the audit committee.)

Tim Shakerley (age 55) is chairman of Provincial Group PLC. A former partner in Sheppards & Chase, stockbrokers, he has a number of other directorships.
(Member of the audit committee.)

Sir Adam Thomson (age 63) is chairman and chief executive of Gold Stag Limited and was formerly chairman and chief executive of British Caledonian Group plc. He is chairman of the Institute of Directors and also deputy chairman of Martin Currie Pacific Trust PLC.

Lord Thomson (age 68) is a former chairman of The Independent Broadcasting Authority. He was an MP, a government minister and a European commissioner. His other directorships include Imperial Chemical Industries plc and the Woolwich Equitable Building Society.

George Younger (age 58) is a Member of Parliament and Privy Councillor. He was a government minister having held the offices of Secretary of State for Defence and Secretary of State for Scotland.

Report of the Directors

The directors have pleasure in presenting their report together with the audited accounts for the year ended 30th September 1989.

Profit and dividends

The profit attributable to the ordinary shareholders of the company amounted to £147.1 million as set out in the consolidated profit and loss account on page 37.

Half-yearly dividends on the cumulative preference shares and an interim dividend of 2.4p* per ordinary share were paid on 31st May and 19th July 1989, respectively, totalling £18.6 million.

The directors have declared the dividends for the half-year ended 30th September 1989 on the cumulative preference shares, which will cost £27,000, and now recommend that a final dividend of 4.8p per ordinary share be paid, absorbing £36.1 million. If this recommendation is approved by the shareholders at the annual general meeting, the retained profit for the year will amount to £92.4 million.

*Adjusted for the effects of the capitalisation issue in September 1989.

Scrip dividend alternative

Over 13,500 shareholders and more than 4,300 members of staff participating in the staff profit sharing scheme elected to receive a total of 1.2 million ordinary shares in lieu of cash in respect of the final dividend for the year ended 30th September 1988 and the interim dividend paid on 19th July 1989. Shareholders are to be offered a similar choice in respect of the final dividend for the financial year ended 30th September 1989 and details are contained in the separate letter to shareholders concerning the additional business to be transacted at the annual general meeting.

Activities and business review

The company is a holding company co-ordinating the activities of its subsidiary companies which are engaged principally in providing a comprehensive range of banking and other financial services. The statement by the chairman and the report by the group chief executive on pages 6 to 22 inclusive contain a review of the business of the Group for the year ended 30th September 1989, of recent events, and of likely future developments.

Annual report on Form 20-F

An annual report on Form 20-F is being filed with the Securities and Exchange Commission in the U.S.A. and copies will be available on request to the Secretary. Much of the detailed financial information therein is shown in the accounts and subsequent financial analyses.

Corporate structure

Details of the principal subsidiary companies of the company are shown on page 46.

On 16th December 1988, the company acquired the entire issued common stock of Citizens Financial Group, Inc., a United States regional bank holding company, based in Rhode Island, for a purchase price of U.S.$30.50 per common share, valuing the whole of the issued common stock at U.S.$440 million.

Ordinary share capital

During the year, in addition to the shares issued in lieu of cash dividends mentioned above, the ordinary share capital of the company was increased as follows:

(a) by the issue to Banco de Santander, S.A. of 7,574,944 fully paid ordinary shares on 29th November 1988 at 355.8p per share in connection with certain agreements entered into with Banco Santander Group;

(b) by the issue to the trustees of the staff profit sharing (share ownership) scheme of 703,222 fully paid ordinary shares on 19th January 1989 at 339.87p per share;

Report of the Directors

Continued

(c) by the issue of 689,044 fully paid ordinary shares on 31st May 1989 at 385.0p per share in connection with the purchase of a further tranche of shares in A. T. Mays Group PLC, whereby the company's interest in A. T. Mays Group was increased to 75 per cent.;

(d) by the issue of 2,328,574 fully paid ordinary shares on 30th June 1989 at 379.0p per share in connection with the purchase of the remaining shares in A. T. Mays Group PLC following the exercise by the vendors of the put option granted to them in the relative sale and purchase agreement; and

(e) by the issue of 450,990,273 fully paid new ordinary shares on 1st September 1989 to the holders of ordinary shares in the proportion of three new ordinary shares for every two ordinary shares held at 31st August 1989 in consequence of the capitalisation of £112,747,568.25 standing to the credit of the company's revaluation reserves. Approval of the capitalisation of reserves and the increase in the company's authorised ordinary share capital to £260 million was given by shareholders at the extraordinary general meeting of the company held on 30th August 1989.

Details of the current authorised and issued ordinary share capital are shown on page 50.

Non-cumulative preference share capital

At the extraordinary general meeting of the company held on 30th August 1989, shareholders gave approval to the creation by the company and issue in appropriate market conditions of up to:

(a) 200 million non-cumulative sterling preference shares of £1; and

(b) 16 million non-cumulative dollar preference shares of U.S.$0.01.

On 14th September 1989, 8.0 million Series A non-cumulative dollar preference shares of U.S.$0.01 were issued by the directors at U.S.$25.00 per share. Details of the current authorised and issued non-cumulative preference share capital of the company are shown on page 50.

Allotment of share capital

At the extraordinary general meeting of the company held on 30th August 1989, resolutions were passed which gave the directors power to allot the unissued shares of the company and which superseded the resolutions passed at the annual general meeting held on 12th January 1989. That power will expire at the date of the forthcoming annual general meeting and accordingly similar resolutions will be proposed to renew that power for a further year at the annual general meeting: the resolutions are contained in the separate letter to shareholders in respect of the additional business to be transacted at the annual general meeting.

Shareholdings

The company has been notified of the following interests in its shares as at 30th November 1989.

	% *held*
Ordinary shares:	
Banco de Santander, S.A.	9.90
Kuwait Investment Office	6.19

	% *held*
Preference shares:	
11 per cent. cumulative:	
Guardian Royal Exchange plc	25.97
Prolific Group plc	6.28
5½ per cent. cumulative:	
Bassett-Patrick Securities Limited	10.55
Guardian Royal Exchange plc	20.25
Provincial Insurance PLC	22.83

Notification has been received on behalf of Mr A. W. R. Medlock and Mrs H. M. Medlock that they each have an interest in the holding of 5½ per cent. cumulative preference shares registered in name of Bassett-Patrick Securities Limited noted above and that there are further holdings of 3,050 and 2,500 shares, respectively, of that class registered in each of their names.

Loan capital

On 23rd February 1989, RBSG Capital Corporation, a wholly-owned subsidiary of the company, issued and sold in the U.S.A., U.S.$250 million 10⅛ per cent. guaranteed capital notes due 2004 at a price of 99.25 per cent. of the principal amount of the notes, raising a total of U.S.$245.2 million. Payment of principal and interest is guaranteed on a subordinated basis by the company. The net proceeds of the sale of the notes were on-lent to the company on a subordinated basis and were used to repay a portion of short-term borrowing from The Royal Bank of Scotland plc incurred to finance the acquisition of Citizens Financial Group, Inc.

On 24th August 1989, the company issued and sold U.S.$400 million undated floating rate primary capital notes at a price of 100 per cent. of the principal amount of the notes, raising a total of U.S.$381.5 million. The notes have no final maturity date. The net proceeds of the sale of the notes were used to repay a portion of short-term borrowing from The Royal Bank of Scotland plc incurred to finance the acquisition of Citizens Financial Group, Inc. The remainder of the net proceeds were on-lent to The Royal Bank of Scotland plc on a subordinated basis.

Details of outstanding issues of loan capital are shown on page 49.

Directors

The present members of the board of directors are named on page 28.

Mr G. Graboys was appointed a director of the company on 3rd February 1989, Don Emilio Botin was appointed a director of the company on 4th February 1989 and Mr G. Younger was appointed a director of the company on 1st October 1989. In accordance with the articles of association, they will retire at the annual general meeting and, being eligible, they offer themselves for reappointment.

The directors retiring by rotation are Mr P. E. G. Balfour, Sir Austin Pearce, Lord Airlie, Mr J. C. R. Inglis, Mr N. Quick and Lord Thomson. Mr J. C. R. Inglis, Mr N. Quick and Lord Thomson do not seek reappointment, but Mr P. E. G. Balfour, Sir Austin Pearce and Lord Airlie, being eligible, offer themselves for reappointment.

Remuneration of directors

An ordinary resolution will be proposed at the annual general meeting to increase the ordinary remuneration of each director from £7,500 to £10,000 per annum with effect from 11th January 1990.

Directors' interests

The interests of the directors at 30th September 1989 in the shares of the company are shown on page 34.

None of the directors held a beneficial interest in the loan capital of the company or its subsidiaries, or in the shares of any of the subsidiaries of the company, during the period between 1st October 1988, or date of appointment if later, and 30th November 1989.

Audit committee

The audit committee comprises Mr N. Quick (chairman), Sir Robin Duthie, Mr A. M. M. Grossart, Mr J. C. R. Inglis and Mr C. F. E. Shakerley, all of whom are non-executive directors of the company.

Employee involvement

The company and its subsidiaries encourage employee involvement by a process of communication and consultation. This takes the form of frequent written communication with all members of staff by means of internal circulars and letters and the regular distribution of a staff newspaper. By these means, staff are advised of major developments affecting the Group as a whole and are able to improve their awareness of the range of services available from the Group through its various operating divisions. In addition, a number of video films have been produced by the Group and the operating divisions for the information and education of its staff.

Profit sharing schemes have existed since 1980 which have included the opportunity to acquire shares in the company. Share option schemes were introduced in 1986.

Share option schemes

On 2nd June 1989, options were granted over 658,750* ordinary shares at a price of 150.0p* per share under the company's executive share option scheme.

On 2nd June 1989, options were granted over 2,711,490* ordinary shares at a price of 135.2p* per share under the company's savings-related share option scheme.

At the annual general meeting on 12th January 1989, the directors were empowered to make minor changes to the rules of the savings-related share option scheme provided that no amendment affects the basic structure of the scheme. Certain amendments to the rules have been made in consequence of the Finance Act 1989 by the directors in exercise of this authority.

*Adjusted for the effects of the capitalisation issue in September 1989.

Staff

The weekly average number of persons employed by the company and its subsidiaries in the United Kingdom was 24,378 and their aggregate remuneration for the year amounted to £301.8 million.

Charitable and other contributions

The total amount given for charitable purposes by the company and its subsidiaries during the year was £1,008,900. Additionally, contributions amounting to £305,683 were made by the company's Community Fund to support organisations which improve the quality of life for individuals within the community, enhance or conserve the environment, or preserve the national heritage.

Close company provisions

The close company provisions of the Income and Corporation Taxes Act 1970, as amended, do not apply to the company and there has been no change in this respect since 30th September 1989.

Auditors

The auditors, Deloitte Haskins & Sells, have indicated their willingness to continue in office. Resolutions to reappoint them and to authorise the directors to fix their remuneration will be proposed at the annual general meeting.

By order of the board.

M R McLean

Secretary

Edinburgh

30th November 1989

Directors' Interests in Shares

ORDINARY SHARES	30th September 1989 Shares	Options	1st October 1988* or date of appointment if later Shares	Options
The Rt. Hon. The Earl of Airlie	3,125		1,250	
P. E. G. Balfour	3,312		1,270	
M. V. Blank	37,461	187,500	13,215	70,000
Sir Robin Duthie	6,522		2,540	
H. E. Farley	29,947	193,812	10,764	77,525
G. Graboys	20,000		—	
I. F. H. Grant	3,312		1,270	
H. L. C. Greig	3,125		1,250	
A. M. Hamilton	12,500		5,000	
J. C. R. Inglis	6,250		2,500	
J. N. C. James	500		—	
R. M. Maiden	24,604	207,507	8,716	73,003
Dr G. R. Mathewson	—	188,032	—	70,000
Sir Austin Pearce	3,312		1,270	
N. Quick	3,312		1,270	
K. Thompson	2,500	187,500	1,000	[illegible]
Sir Adam Thomson	2,567		1,000	
The Rt. Hon. Lord Thomson of Monifieth	3,125		1,250	
C. M. Winter	29,174	237,500	10,466	80,000
Sir Michael Young-Herries	15,624	225,000	6,250	90,000

The above interests in the ordinary shares were all held beneficially.

Sir Michael Young-Herries had a non-beneficial interest in 10,636 ordinary shares at 30th September 1989 and 4,255 ordinary shares at 1st October 1988*.

Mr P. E. G. Balfour and Mr M. V. Blank, as trustees of the staff profit sharing share schemes of Charterhouse Bank Limited, Charterhouse Development Capital Limited, Charterhouse Tilney and the former Charterhouse Investment Management Limited, had a non-beneficial interest in 585,554 ordinary shares at 30th September 1989 and 171,894 ordinary shares at 1st October 1988*. Sir Robin Duthie and Mr C. M. Winter, as trustees of the staff profit sharing share scheme of Capital House Investment Management Limited, had a non-beneficial interest in 14,420 ordinary shares at 30th September 1989 and 5,768 ordinary shares at 1st October 1988*.

No other director had an interest in the ordinary shares during the year.

*Interests at 1st October 1988 are stated before adjustment in respect of the capitalisation issue in September 1989.

PREFERENCE SHARES

Mr A. M. Hamilton held a beneficial interest in 180 11 per cent. cumulative preference shares of the company at 30th September 1989 and at 1st October 1988. Mr G. Graboys held a beneficial interest in 2,000 Series A non-cumulative dollar preference shares of U.S.\$0.01 each of the company at 30th September 1989. No other director had an interest in the preference shares during the year.

There has been no change in the directors' interests in the shares of the company shown above between 30th September 1989 and 30th November 1989.

Accounting Policies

The accounts on pages 37 to 53 are prepared on the basis of the principal accounting policies adopted by the company and its subsidiaries described below.

The consolidated accounts are prepared in accordance with Part VII, Chapter II of, and Schedule 9 to, the Companies Act 1985. The accounts of the company are prepared in accordance with section 228 of, and Schedule 4 to, the Companies Act 1985. As provided by section 228(7) of the Companies Act 1985, no profit and loss account is presented for the company.

1 Accounting convention

The accounts are prepared under the historical cost convention modified by the periodic valuations of premises and certain investments.

2 Bases of consolidation

The consolidated accounts deal with the accounts of the company, its subsidiaries and associates (the 'Group') made up to 30th September with the exception of certain subsidiary companies where accounts are made up to 30th June to avoid undue delay in publication of the Group's accounts. Audited management accounts are used, with the permission of the Department of Trade and Industry, for certain subsidiary companies.

Subsidiary companies are those companies in which the company owns directly or indirectly more than 50 per cent. of the voting capital. The Group accounts for subsidiaries by consolidating fully their assets, liabilities and results for the year and by showing separately the interests of minority shareholders therein. All inter-company balances and transactions are eliminated from the consolidated statements.

Investments in associated companies are accounted for by the equity method and are stated in the consolidated balance sheet at the investing company's share of their net tangible assets. The investing company's share of the results of associated companies is included in the consolidated profit and loss account. For this purpose, the latest available audited accounts are used together with unaudited interim accounts where necessary.

3 Rates of exchange

Foreign currency balances and results from overseas branches and subsidiaries are expressed in sterling at the rates of exchange ruling at the balance sheet date. Exchange differences relating to trading are dealt with in the profit and loss account; those arising from the application of closing rates of exchange to the opening net assets of overseas subsidiaries are taken to reserves.

4 Pension costs

In arriving at the operating profit, the costs of providing pensions are assessed and charged on a regular basis in accordance with the advice of independent professionally qualified actuaries.

5 Lease income receivable

Income after taxation from finance leases is recognised over the primary period of the lease in proportion to the net funds invested. It is allocated to profit before and after taxation by applying the prevailing rate of corporation tax to the net income.

Income from operating leases is credited to profit and loss account on a straight-line basis over the period of each lease.

6 Taxation

Provision is made for taxation at current rates on the taxable profits and relief for overseas taxation is taken where appropriate.

Certain items of income and expenditure are accounted for in different periods for financial reporting purposes and for taxation purpose. Deferred taxation is provided on the liability method in respect of timing differences which are expected to result in a taxation liability in the foreseeable future.

7 Provisions for bad and doubtful debts

Specific provisions are made against advances when, as a result of a detailed appraisal of the advances portfolio, it is considered that recovery is doubtful. A general provision is made against advances to cover bad and doubtful debts which have not been separately identified but are known from experience to be present in any portfolio of bank advances. The specific and general provisions are deducted from advances.

Provisions made during the year (less amounts released and recoveries of amounts written off in previous years) are charged against profits. Where interest on doubtful advances is credited to the profit and loss account, provision is made as appropriate. Advances classified as bad debts are written off in part or in whole when the extent of the loss incurred has been confirmed.

8 Trade investments

Trade and other long term investments are included in the consolidated balance sheet at cost less amounts written off and provision is made against the book value where in aggregate this exceeds current valuation. Income is recognised when dividends are received.

9 Investments (other than trade investments)

Premiums and discounts on the acquisition of dated stocks are amortized over the period from date of purchase to date of maturity and an appropriate proportion thereof is included in the profit and loss account. Such stocks are shown in the consolidated balance sheet at amortized cost.

Investments, other than dated stocks, are included in the consolidated balance sheet at the lower of cost and market value and, in the case of unlisted investments, at the lower of cost and directors' valuation. Investments held for dealing purposes are included in the consolidated balance sheet at market value.

Investments in subsidiaries and in associated companies are included in the balance sheets at the investing company's share of the net tangible assets.

Profits and losses on sales of investments are dealt with in the profit and loss account as they arise.

10 Premises and equipment

Freehold and long leasehold buildings are maintained to the highest possible standard by regular expenditure charged against operating profit, and accordingly are not depreciated.

Short leasehold premises are amortized by equal annual instalments over the unexpired term of the lease.

Full professional valuations of premises are made periodically and any increase or deficit on revaluation is reflected in fixed assets and reserves at that time. Any profit from the sale of revalued premises is calculated by deducting the revalued amount from the net proceeds.

Computers are depreciated on a straight-line basis over five years and other equipment over periods between four and fifteen years.

11 Goodwill

Goodwill arising on acquisitions of subsidiaries and associates, being the excess of cost over fair value of the Group's share of net tangible assets acquired, is charged against reserves in the year of acquisition.

Consolidated Profit and Loss Account

for the year ended 30th September 1989

	Note	£m	1988 £m
Operating profit			
The company and its subsidiaries	1	306.9	277.9
Share of profits of associated companies		29.6	31.3
Profit before exceptional item		336.5	309.2
Exceptional item	9	108.3	—
Profit before taxation		228.2	309.2
Taxation	2	80.7	115.1
Profit after taxation		147.5	194.1
Minority interests		0.3	1.5
		147.2	192.6
Preference dividends	3	0.1	0.1
Profit attributable to ordinary shareholders		147.1	192.5
Ordinary dividends	5	54.7	43.2
Retained profit	22	92.4	149.3
Earnings per 25p ordinary share	6		
before exceptional item		29.4p	26.8p*
after exceptional item		19.9p	26.8p*

*Adjusted to show the effects of the capitalisation issue in September 1989.

Consolidated Balance Sheet

at 30th September 1989

	Note	£m	1988 £m
Assets employed:			
Cash and short-term funds	7	6,322.9	6,351.1
Collections on other banks		402.1	420.4
Investments	8	781.7	481.3
Advances to customers and other accounts	9	19,093.6	13,754.3
		26,600.3	21,007.1
Trade investments	10	60.4	10.1
Investments in associated companies	11	107.3	77.1
Premises and equipment	15	667.7	565.6
		27,435.7	21,659.9
Financed by:			
Liabilities			
Deposits and customers' current accounts	16	23,219.4	18,439.3
Notes in circulation		538.1	487.0
Other liabilities	17	1,011.6	611.6
		24,769.1	19,537.9
Dated loan capital	19	785.8	637.2
Undated loan capital	20	462.3	207.4
Minority interests		7.8	7.7
Share capital and reserves			
Issued share capital	21	188.9	72.9
Reserves	22	1,221.8	1,196.8
		1,410.7	1,269.7
		27,435.7	21,659.9

Chairman

Vice-chairman

Group chief executive

Balance Sheet - the Company

at 30th September 1989

	Note	£m	1988 £m
Fixed assets			
Investments:			
Shares in subsidiaries	12, 13	1,733.2	1,470.7
Loans to subsidiaries	14	632.4	324.4
		2,365.6	1,795.1
Current assets			
Debtors:			
Due by subsidiaries		11.8	10.5
Creditors			
Amounts falling due within one year:			
Creditors		16.8	12.2
Due to subsidiaries		35.4	29.1
Current taxation		12.0	9.3
Proposed final dividends		36.1	27.9
		100.3	78.5
Net current (liabilities)		(88.5)	(68.0)
Fixed assets less net current liabilities		2,277.1	1,727.1
Amounts falling due after more than one year:			
Due to subsidiaries		154.1	—
		2,123.0	1,727.1
Dated loan capital	19	250.0	250.0
Undated loan capital	20	462.3	207.4
Capital and reserves			
Called up share capital	21	188.9	72.9
Share premium account	22	263.0	111.6
Revaluation reserve	22	934.4	1,066.0
Profit and loss account	22	24.4	19.2
		1,410.7	1,269.7
		2,123.0	1,727.1

Chairman

Vice-chairman

Group chief executive

Statement of Source and Application of Funds

for the year ended 30th September 1989

	£m	1988 £m
Source of funds		
Profit attributable to ordinary shareholders	147.1	192.5
Adjustments for items not involving movement of funds:		
Depreciation	63.6	45.6
Retentions by associated companies	(9.3)	(13.7)
Profit on sales of investments	(12.9)	(7.7)
Exchange translation adjustments on loan capital	16.9	(12.7)
Other	(5.4)	1.1
Funds generated by operations	200.0	205.1
Funds from other sources:		
Disposal of trade investments and investment in associated companies	2.9	0.2
Disposal of premises and equipment	25.3	9.7
Loan and preference share capital issued	554.4	297.3
Ordinary share capital issued	46.2	8.2
Other	3.8	1.0
	832.6	521.5
Application of funds		
Dividends paid	46.6	38.5
Purchase of trade investments and investment in associated companies	70.1	5.2
Investment in subsidiaries	103.4	15.9
Purchase of premises and equipment	145.6	108.2
Loan capital repaid	44.5	0.2
Expenses of capital issues	21.1	4.4
Other	44.0	9.5
	475.3	181.9
Increase in working capital (see below)	357.3	339.6
	832.6	521.5
Analysis of increase in working capital:		
Increase in advances to customers and other accounts	5,332.9	1,162.0
Increase in short-term funds and investments	247.4	1,208.4
	5,580.3	2,370.4
Increase in deposits and other liabilities	5,223.0	2,030.8
	357.3	339.6

Notes on the Accounts

1 Operating profit

The operating profit of the company and its subsidiaries is stated after taking account of the following:

	£m	1988 £m
Income		
Income from investments (other than trade investments) including the amortization of dated stocks:		
Listed investments	59.9	39.0
Unlisted investments	8.5	3.6
Income from trade investments:		
Listed investments	0.5	0.1
Unlisted investments	2.8	0.4
Profit on sales of investments	12.9	7.7
Charges		
Interest on deposits and other accounts	2,041.6	1,170.0
Interest on loan capital	100.8	64.7
Hire of equipment	10.0	7.4
Operating lease rentals	21.8	18.3
Staff profit sharing schemes	15.3	14.9
Auditors' remuneration [the company £45,300 (1988—£20,700)]	1.1	0.7
Depreciation:		
Short leasehold buildings	1.7	1.1
Computers and other equipment	52.0	44.5

Pension funds' costs:

The total pension charge for the Group in respect of the year to 30th September 1989 was £27.7 million (1988—£3.6 million), of which £22.9 million related to the pension scheme of The Royal Bank of Scotland plc (the 'Bank'), £4.1 million to other U.K. schemes, and £0.7 million to overseas schemes. The increase in the pension charge arises as a result of the adoption of Statement of Standard Accounting Practice No. 24—Accounting for pension costs, with effect from 1st October 1988.

The Bank's pension scheme (the 'scheme'), which covers approximately 85 per cent. of the Group's U.K. employees is of the defined benefit type. The scheme is set up under trust and the assets of the scheme are, therefore, held separately from those of the Bank. The pension cost relating to the scheme is assessed in accordance with the advice of a qualified actuary using the projected unit method. It is calculated to spread the cost of pensions over the employees' expected working service lives with the Bank and is based on the most recent actuarial valuation of the scheme which was completed as at 30th September 1988, at which date the market value of the scheme was £717 million. The principal assumptions used in the latest valuation were that the annual rate of return on investments would be 2 per cent. higher than the annual increase in salaries, and 4 per cent. higher than the annual increase in present and future pensions and the annual increase in equity dividends. During the year to 30th September 1989, a review disclosed that the actuarial value of the assets was sufficient to cover 118 per cent. of the benefits that had accrued to members, after allowing for expected future increases in earnings. The scheme is funded using the same assumptions and actuarial method as described above. The surplus disclosed is being corrected by a short-term suspension of contributions which is expected to apply until 30th September 1992.

The pension schemes operated within Charterhouse, Direct Line Insurance and A. T. Mays which cover approximately 15 per cent. of the Group's U.K. employees are similarly constituted and are fully funded. The principal overseas scheme, which is sponsored by Citizens Savings Bank, is a defined benefit plan and is funded on a current basis in compliance with the requirements of the Employee Retirement Income Security Act in the U.S.A.

Notes on the Accounts

Continued

2 Taxation

The company and its subsidiaries:

	£m	1988 £m
Based on the profit for the year:		
U.K. corporation tax at 35 per cent. (1988—35 per cent.)	73.3	105.9
Relief for overseas taxation	(1.8)	(0.9)
Deferred taxation	(10.5)	(4.7)
	61.0	100.3
Overseas taxation	13.3	3.2
	74.3	103.5
Prior year items	(4.8)	(0.7)
	69.5	102.8
Share of associated companies	11.2	12.3
	80.7	115.1

As a result of anticipated roll-over relief, no taxation has been provided in respect of profit on sales of business premises.

3 Preference dividends

	£000	1988 £000
On 11 per cent. (now 7.7 per cent. plus tax credit) cumulative preference shares	39	39
On 5½ per cent. (now 3.85 per cent. plus tax credit) cumulative preference shares	15	15
	54	54

4 Profit dealt with in the accounts of the company

Of the profit attributable to ordinary shareholders, £61·6 million (1988—£52.2 million) has been dealt with in the accounts of the company.

5 ORDINARY DIVIDENDS

	p per share	1988 p per share	£m	1988 £m
Interim	2·4*	2.1*	18·6	15.3
Proposed final	4·8	3.9*	36·1	27.9
	7·2	6.0*	54·7	43.2

*Adjusted to show the effects of the capitalisation issue in September 1989.

6 EARNINGS PER SHARE

Earnings per share have been calculated by reference to the weighted average of 740.3 million (1988—717.0 million) ordinary shares in issue during the year, profit of £217·5 million (1988—£192.5 million) before the exceptional item, net of taxation relating thereto, and profit of £147·1 million (1988—£192.5 million) after the exceptional item. Fully diluted earnings per share are not given as the dilution arising from options granted is not material. The weighted averages of ordinary shares in issue have been adjusted for the effects of the capitalisation issue in September 1989.

7 CASH AND SHORT-TERM FUNDS

	£m	1988 £m
Coin, bank notes and balances with Bank of England	736·9	721.3
Money at call and short notice	4,781·6	5,029.2
Bills discounted	584·8	384.3
Certificates of deposit	219·6	216.3
	6,322·9	6,351.1

8 INVESTMENTS

	Book value £m	Valuation £m	1988 Book value £m	1988 Valuation £m
Listed investments:				
British Government securities	189·4	181·9	224.1	221.6
Other investments listed in Great Britain	82·5	127·9	102.8	132.5
Investments listed elsewhere	378·7	376·7	87.6	93.2
	650·6	686·5	414.5	447.3
Unlisted investments	131·1	144·5	66.8	72.3
	781·7	831·0	481.3	519.6

Listed investments have been valued at market prices and unlisted investments at directors' valuation.

12 PRINCIPAL SUBSIDIARY COMPANIES

The principal subsidiary companies at 30th September 1989, all of which are wholly-owned except where otherwise indicated and the capital of which consists solely of ordinary shares, are shown below. The companies marked with an asterisk operate in the country of incorporation or registration; the others operate mainly in the United Kingdom.

	Nature of business	Country of incorporation or registration
Owned by the company:		
The Royal Bank of Scotland plc	Banking	Scotland
Charterhouse plc	Holding company	England
*Citizens Financial Group, Inc.	Bank holding company	U.S.A.
RoyScot Finance Group plc	Holding company	England
A. T. Mays Group PLC	Travel agents	Scotland
Direct Line Insurance plc	Insurance	England
Capital House Investment Management Limited	Investment portfolio and fund managers	England
Royal Bank Group Services Limited	Technology, property and related resources	Scotland
Owned by The Royal Bank of Scotland plc:		
†*Associated Merchant Bank Pte Limited (64 per cent.)	Merchant banking	Singapore
RBS Trade Services Limited	Confirming house	England
Royal Bank Insurance Services Limited	Insurance broking	Scotland
*Royscot International Finance B.V.	Finance raising company	The Netherlands
*The Royal Bank of Scotland AG	Banking	Switzerland
*The Royal Bank of Scotland (Gibraltar) Limited (51 per cent.)	Banking	Gibraltar
*The Royal Bank of Scotland (Guernsey) Limited	Banking	Guernsey
*The Royal Bank of Scotland (I.O.M.) Limited	Banking	Isle of Man
*The Royal Bank of Scotland (Jersey) Limited	Banking	Jersey
*The Royal Bank of Scotland (Nassau) Limited	Banking	Bahamas
*Williams & Glyn's (Nederland) B.V.	Finance raising company	The Netherlands
Owned by Charterhouse plc:		
Charterhouse Bank Limited	Merchant banking	England
Charterhouse Development Capital Limited	Provision of development capital	England
Charterhouse Securities Limited	Holding company	England
Owned by Charterhouse Development Capital Limited:		
Charterhouse Business Expansion Fund Management Limited	Business expansion fund managers	England
*Charterhouse S.A.	Provision of development capital	France
Owned by Charterhouse Securities Limited:		
Charterhouse Tilney	Stockbroking	England
Owned by Citizens Financial Group, Inc.:		
*Citizens Savings Bank	Banking	U.S.A.
*Citizens Trust Company	Banking	U.S.A.
*Fairhaven Savings Bank	Banking	U.S.A.
*Gulf States Mortgage Co., Inc.	Mortgage banking	U.S.A.
Owned by RoyScot Finance Group plc:		
Royal Bank Leasing Limited	Leasing and hire purchase	Scotland
RoyScot Factors Limited	Factoring and invoice discounting	England
RoyScot Financial Services Limited	Holding company	England
RoyScot Trust plc	Instalment financing and leasing	England
RoyScot Vehicle Contracts Limited	Holding company	England
Owned by RoyScot Financial Services Limited:		
Style Financial Services Limited	Credit card company	Scotland

†Accounts made up to 30th June.

Notes on the Accounts

Continued

9 ADVANCES TO CUSTOMERS AND OTHER ACCOUNTS

	£m	1988 £m
Advances to customers, less provisions	14,416·4	10,740.0
Placings with banks over one month	2,980·8	1,871.1
Amounts receivable under finance leases	1,247·7	1,006.5
Debtors and other accounts	448·7	136.7
	19,093·6	13,754.3

The cost of assets acquired during the year for the purpose of letting under finance leases and hire purchase agreements was £858·7 million (1988—£608.6 million).

Provisions for bad and doubtful debts and movements thereon in the year were:

	Specific £m	General £m	1988 Specific £m	1988 General £m
At 1st October	367·3	50·7	365.7	44.9
Additions on acquisition of subsidiary company	2·4	8·5	0.4	—
Currency translation adjustment	4·9	0·5	(4.4)	(0.3)
Amounts written off	(65·0)	—	(55.7)	—
Recoveries of amounts written off in previous years	6·5	—	8.2	—
Charge to profit and loss account	73·4	12·4	53.1	6.1
Exceptional additional provisions charged to profit and loss account	108·3	—	—	—
At 30th September	497·8	72·1	367.3	50.7
Total provisions	569·9		418.0	

Exceptional item:

Additional exceptional provisions of £108·3 million in respect of lending to nine rescheduling countries have been charged to the profit and loss account as an exceptional item. This charge includes £10·7 million in respect of realised losses on debt sales and swaps. The Group's medium and long term exposure to these countries totals £191·8 million and there is an additional £57·0 million of interbank and trade facilities. The exceptional additional provisions result in total specific provisions of £186·2 million in respect of these commitments and we believe that there should be no need for further exceptional provisions in the future.

The Group's exposure to these countries is summarised as follows:

	£m	1988 £m
Mexico	118·7	110.6
Brazil	72·8	71.3
Other Latin American countries	15·4	31.5
	206·9	213.4
Africa	38·8	54.3
Rest of the world	3·1	33.9
	248·8	301.6
Exposure in U.S. dollars	U.S.$403·7m	U.S.$509.0m

Notes on the Accounts

Continued

5 Ordinary dividends

	p per share	1988 p per share	£m	1988 £m
Interim	2·4*	2.1*	18·6	15.3
Proposed final	4·8	3.9*	36·1	27.9
	7·2	6.0*	54·7	43.2

*Adjusted to show the effects of the capitalisation issue in September 1989.

6 Earnings per share

Earnings per share have been calculated by reference to the weighted average of 740.3 million (1988—717.0 million) ordinary shares in issue during the year, profit of £217·5 million (1988—£192.5 million) before the exceptional item, net of taxation relating thereto, and profit of £147·1 million (1988—£192.5 million) after the exceptional item. Fully diluted earnings per share are not given as the dilution arising from options granted is not material. The weighted averages of ordinary shares in issue have been adjusted for the effects of the capitalisation issue in September 1989.

7 Cash and short-term funds

	£m	1988 £m
Coin, bank notes and balances with Bank of England	736·9	721.3
Money at call and short notice	4,781·6	5,029.2
Bills discounted	584·8	384.3
Certificates of deposit	219·6	216.3
	6,322·9	6,351.1

8 Investments

	Book value £m	Valuation £m	1988 Book value £m	1988 Valuation £m
Listed investments:				
British Government securities	189·4	181·9	224.1	221.6
Other investments listed in Great Britain	82·5	127·9	102.8	132.5
Investments listed elsewhere	378·7	376·7	87.6	93.2
	650·6	686·5	414.5	447.3
Unlisted investments	131·1	144·5	66.8	72.3
	781·7	831·0	481.3	519.6

Listed investments have been valued at market prices and unlisted investments at directors' valuation.

13 SHARES IN SUBSIDIARIES

Movements during the year:

	£m
At 1st October 1988	1,470·7
Additions	260·8
Net decrease in net tangible assets of subsidiaries	(18·8)
Currency translation adjustment	20·5
At 30th September 1989	1,733·2

14 LOANS TO SUBSIDIARIES

Movements during the year:

	£m
At 1st October 1988	324·4
Additions	299·7
Currency translation adjustment	8·3
At 30th September 1989	632·4

15 PREMISES AND EQUIPMENT

	Freehold premises £m	Long leasehold premises £m	Short leasehold premises £m	Computers and other equipment £m	Total £m
At 1st October 1988	318.1	53.1	26.7	333·4	731·3
Additions on acquisition of subsidiary company	25·8	—	2·9	15·3	44·0
Additions	29·2	0·6	8·2	107·6	145·6
Disposals	(3·7)	(0·2)	(0·3)	(42·5)	(46·7)
At 30th September 1989	369·4	53·5	37·5	413·8	874·2
Consisting of:					
At 1988 valuation	316·4	52·7	4·7	—	373·8
At cost	53·0	0·8	32·8	413·8	500·4
	369·4	53·5	37·5	413·8	874·2
Accumulated depreciation	—	—	9·0	197·5	206·5
Net book value at 30th September 1989	369·4	53·5	28·5	216·3	667·7
1988	318.1	53·1	20.5	173.9	565.6

Future expenditure:

	£m	1988 £m
Contracts not provided for in the accounts	20·2	14·5
Authorised by the directors but not contracted for	96·9	32·7
	117·1	47·2

Notes on the Accounts

Continued

16 Deposits and customers' current accounts

	£m	1988 £m
Sterling current accounts	2,682·8	2,891.9
Sterling retail deposits	4,404·5	3,292.5
Sterling wholesale deposits	8,866·6	7,415.4
Foreign currency deposits and other accounts	7,265·5	4,839.5
	23,219·4	18,439.3

17 Other liabilities

	£m	1988 £m
Creditors and accrued expenses	662·6	253.3
Taxation—current	162·3	177.3
—deferred (see note 18)	150·6	153.1
Proposed final dividends	36·1	27.9
	1,011·6	611.6

18 Deferred taxation

Provision has been made in the accounts for the amounts of deferred taxation shown below:

	£m	1988 £m
Short-term timing differences	(28·7)	(2.0)
Capital allowances on computers and other equipment	18·2	16.5
Capital allowances on finance lease receivables	195·8	175.9
Advance corporation tax recoverable	(34·7)	(37.3)
	150·6	153.1

Movements during the year:	
At 1st October 1988	153·1
Charge/(credit) to profit and loss account:	
current year	(10·5)
prior year	6·9
Other movements	1·1
At 30th September 1989	150·6

No provision has been made for the following potential amounts of deferred taxation:

	£m	1988 £m
Capital allowances on computers and other equipment	0·7	2.7
Capital allowances on finance lease receivables	10·9	10.9
	11·6	13.6

No provision has been made for the potential taxation liability which might arise in the event of any of the investments in subsidiaries and associated companies, or of freehold and long leasehold premises being realised at their balance sheet values, as it is intended that most of the investments and premises will be retained on a long term basis; it is also expected that tax on any chargeable gain which might arise on sales of premises will be covered by roll-over relief.

19 Dated loan capital

	£m	1988 £m
The company		
£200 million floating rate (minimum 5¼ per cent.) notes 2005	200·0	200.0
£50 million 8¼ per cent. notes 1994 with warrants to procure the subscription of 17·7 million ordinary shares of the company	50·0	50.0
The Royal Bank of Scotland plc		
£125 million 10⅝ per cent. subordinated bonds 1998*	125·0	125.0
Royscot International Finance B.V.		
U.S.$75 million 11⅞ per cent. guaranteed bonds 1993 with warrants to subscribe for up to U.S.$75 million 11½ per cent. guaranteed bonds 1993* (repaid 15th November 1988)	—	44.4
U.S.$74.2 million (1988—U.S.$62.8 million) 11½ per cent. guaranteed bonds 1993*	45·7	37.2
U.S.$200 million guaranteed floating rate notes 1994/1998*	123·3	118.5
RBSG Capital Corporation		
U.S.$250 million 10⅛ per cent. guaranteed capital notes 2004*	154·1	—
Williams & Glyn's (Nederland) B.V.		
U.S.$100 million 11 per cent. guaranteed bonds 1993*	61·6	59.3
Charterhouse plc		
10 per cent. unsecured loan notes 1987/1991	2·7	2.8
Citizens Financial Group, Inc.		
U.S.$38 million 9.4 per cent. senior notes 1995	23·4	—
	785·8	637.2

*Loans unconditionally guaranteed by the company.

Interest on loan capital wholly repayable within five years was £12·3 million (1988—£12.1 million).

20 Undated loan capital

	£m	1988 £m
The company		
U.S.$350 million undated primary capital floating rate (minimum 5 per cent.) notes	215·7	207.4
U.S.$400 million undated floating rate primary capital notes	246·6	—
	462·3	207.4

Notes on the Accounts

Continued

21 Share capital	Ordinary shares of 25p each £m	Cumulative preference shares of £1 each* £m	Non-cumulative dollar preference shares of 1 cent each £m	Non-cumulative sterling preference shares of £1 each £m	Total £m
Authorised	**260.0**	**0.9**	**0.1**	**200.0**	**461.0**
Allotted, called up and fully paid:					
At 1st October 1988	72.0	0.9	—	—	72.9
Issued under profit sharing (share ownership) scheme and share option schemes	0.3	—	—	—	0.3
Issued in connection with acquisition of investments	2.6	—	—	—	2.6
Issued in lieu of cash dividends	0.3	—	—	—	0.3
Capitalisation issue	112.7	—	—	—	112.7
Preference shares issued during the year	—	—	0.1	—	0.1
At 30th September 1989	**187.9**	**0.9**	**0.1**	—	**188.9**

*The cumulative preference shares of £1 each consist of £0.5 million 11 per cent. (now 7.7 per cent. plus tax credit) and £0.4 million 5½ per cent. (now 3.85 per cent. plus tax credit).

During the year to 30th September 1989, 891,902 ordinary shares were allotted following early exercises of options under the company's savings-related and executive share option schemes. Also, during the year to 30th September 1989, options were granted under the company's executive share option scheme. and under the company's savings-related share option scheme. At 30th September 1989, options under the schemes exercisable between 1990 and 1999 at prices ranging from 116·0p to 150·0p per share were outstanding in respect of 25,641,261 ordinary shares.

On or after 15th September 1994, the 8·0 million Series A non-cumulative dollar preference shares of U.S.\$0·01 each are redeemable, at the option of the company, in whole or in part from time to time, at the redemption prices set forth below plus an amount equal to dividends otherwise payable for the then current quarterly dividend period accrued to the date fixed for redemption.

Redemption date	*Redemption price*
15th September 1994 to 14th September 1995, inclusive	U.S.$26.41
15th September 1995 to 14th September 1996, inclusive	U.S.$26.12
15th September 1996 to 14th September 1997, inclusive	U.S.$25.84
15th September 1997 to 14th September 1998, inclusive	U.S.$25.56
15th September 1998 to 14th September 1999, inclusive	U.S.$25.28
On or after 15th September 1999	U.S.$25.00

All of the Series A non-cumulative dollar preference shares are held by Citibank, NA, 111 Wall Street, New York, New York 10043, U.S.A., as depositary and the registrar and paying agent is The Royal Bank of Scotland plc, PO Box 435, Owen House, 8 Bankhead Crossway North, Edinburgh EH11 4BR.

Notes on the Accounts

Continued

22 Reserves

	The Group £m	The company £m	Associated companies £m
At 1st October 1988	1,196.8	1,196.8	49.1
Premium arising on issues of shares	166·2	166·2	—
Elimination of goodwill—Citizens Financial Group, Inc.	(74·3)	—	—
—Other	(29·1)	—	—
Decrease in net tangible assets of subsidiaries	—	(18·8)	—
Expenses of capital issues	(21·1)	(14·8)	—
Capitalisation issue	(112·7)	(112·7)	—
Retained profit for the year	92·4	6·9	9·4
Other movements	3·6	(1·8)	0·8
At 30th September 1989	1,221·8	1,221·8	59·3

The reserves of the Group include share premium of £263·0 million (1988—£115.6 million), surplus on revaluation of premises of £62·2 million (1988—£169.5 million), and other non-distributable reserves of £4·5 million (1988—£6.8 million). The reserves of the company include share premium of £263·0 million (1988—£111.6 million) and surplus on revaluation of subsidiaries of £934·4 million (1988—£1,066.0 million).

23 Acquisition of Citizens Financial Group, Inc.

Fair values of net assets acquired, stated in accordance with U.K. accounting principles (U.K.GAAP):	£m
Cash and short-term funds	47.8
Investments	409.2
Advances to customers and other accounts	1,152.1
Other assets	60.1
Deposits and other liabilities	(1,499.4)
Net assets acquired (cost of acquisition £244.1 million including expenses)	169.8

No significant adjustments were required to the book values of the net assets.

Figures in the above table have been translated at U.S $ .8225=£1, the rate of exchange at the date of acquisition.

Notes on the Accounts

Continued

24 Contingent liabilities

Acceptances, guarantees and other obligations entered into on account of customers, for which there are corresponding liabilities of customers, are not included in the consolidated balance sheet.

These comprised:

	£m	1988 £m
Acceptances	534·3	770.2
Guarantees and other obligations	1,008·2	1,053.0
	1,542·5	1,823.2

In addition, there are outstanding contracts for the purchase and sale of foreign currencies, financial futures contracts, option contracts and various other arrangements with customers which are not reflected in the consolidated balance sheet. It is not envisaged that any material irrecoverable liability will arise from these transactions.

25 Lease commitments

At 30th September, the annual rental commitments under non-cancellable operating leases were:

	Property £m	Equipment £m	1988 Property £m	1988 Equipment £m
Expiring within one year	1·5	2·1	1.1	2.8
Expiring between one and five years	3·1	10·3	3.3	6.5
Expiring after five years	18·7	0·1	19.1	0.1
	23·3	12·5	23.5	9.4

26 Directors' and employees' emoluments

	£000	1988 £000
Fees as directors	237	186
Other emoluments including pension contributions	1,523	1,141
Total directors' emoluments	1,760	1,327

The emoluments of the chairman were £110,228 (1988—£90,205). The emoluments of the group chief executive were £183,822 (1988—£150,620) and the emoluments of the highest paid U.K. director were £446,654 (1988—£375,487).

The numbers of other U.K. directors whose emoluments, excluding pension contributions, fell into the following categories, were:

£		1988	£		1988	£		1988
10,001—15,000	8	10	40,001— 45,000	1	—	115,001—120,000	1	1
15,001—20,000	2	1	50,001— 55,000	—	1	120,001—125,000	—	1
20,001—25,000	2	2	55,001— 60,000	—	1	135,001—140,000	1	—
25,001—30,000	1	—	90,001— 95,000	—	1	140,001—145,000	1	—
35,001—40,000	—	1	110,001—115,000	1	—			

Fees amounting to £105,000 (1988—£79,437) have been waived by eight (1988—eight) directors.

The company had no employees during the year ended 30th September 1989 (1988—nil).

27 TURNOVER

Turnover attributable to the business of banking is not shown. Non-banking turnover of subsidiary companies was:

	£m	1988 £m
Capital cost of assets financed	858·7	608.6
Insurance	78·3	60.1
Credit card business	23·8	20.1
Travel agency commission	28·9	27.0
Other non-banking activities	42·0	31.4
	1,031·7	747.2

28 RATE OF EXCHANGE

At 30th September 1989, the principal rate of exchange for foreign currency translations was U.S.$1.6225=£1 (1988—U.S.$1.6875=£1).

29 TRANSACTIONS WITH DIRECTORS AND OFFICERS

(a) At 30th September 1989, the amounts outstanding in relation to transactions, arrangements and agreements entered into by authorised institutions in the Group were £2,152,905 in respect of loans to 24 persons who were directors of the company (or persons connected with them) at any time during the financial year and £211,083 to four persons who were officers of the company at any time during the financial year. As at the same date, there were in existence three guarantees totalling £50,000 in respect of certain obligations of one director.

(b) On 31st May 1988, the company's subsidiary, The Royal Bank of Scotland plc (the "Bank") purchased from Dr G. R. Mathewson, a director of the company and the Bank, and his wife, the dwellinghouse known as "Larach-Beg", Banchory for the sum of £125,000 (the "purchase price"). The purchase, which was approved prior to completion by the shareholders of both the company and the Bank in general meeting, was made subject to Dr Mathewson retaining the right to repurchase the dwellinghouse in the event of his ceasing to be an executive director of the company or its subsidiaries, or on such earlier date as the directors of the company may allow. Any repurchase is to be either at the purchase price or at a price determined by an independent professional valuation carried out at the time of repurchase, whichever figure is the higher. The right to repurchase will lapse if not exercised within one month after Dr Mathewson ceases to be an executive director of the company or its subsidiaries and, in the event that he remains an executive director after 31st May 2008 his right of repurchase will become exercisable at that time. The dwellinghouse is at present let by the Bank on a commercial basis, with the rental payments being received wholly by the Bank.

(c) There were no contracts of significance to the business of the company and its subsidiaries which subsisted during or at the end of the company's financial year to 30th September 1989 in which any director of the company had a material interest.

APPROVAL OF ACCOUNTS

The accounts were approved by the board of directors on 30th November 1989.

Report of the Auditors

TO THE MEMBERS OF THE ROYAL BANK OF SCOTLAND GROUP plc

We have audited the accounts on pages 35 to 53 in accordance with Auditing Standards.

In our opinion the accounts give a true and fair view of the state of affairs of the company and of the Group at 30th September 1989 and of the profit and source and application of funds of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Chartered Accountants

Edinburgh

30th November 1989

Financial Analyses

Analysis of operating profit for the year ended 30th September 1989

(a) DETAILED PROFIT AND LOSS ACCOUNT:

	£m	1988 £m
The company and its subsidiaries		
Interest and investment income receivable	2,835·7	1,808.4
Interest payable including interest on loan capital	2,142·4	1,234.7
Net interest income	693·3	573.7
Commissions and fees	330·6	270.7
Foreign exchange	47·6	34.6
Profit on sales of investments	12·9	7.7
Profit on sales of premises	1·4	1.8
Other income	16·8	3.1
Total income	1,102·6	891.6
Staff expenses	397·8	298.9
Premises and equipment expenses including depreciation	123·8	106.3
Other expenses	188·3	149.3
Total expenses	709·9	554.5
	392·7	337.1
Bad and doubtful debts charge	85·8	59.2
	306·9	277.9
Share of profits of associated companies	29·6	31.3
Profit before exceptional item	336·5	309.2
Exceptional item	108·3	—
Profit before taxation	228·2	309.2

(b) PROFIT BEFORE EXCEPTIONAL ITEM BY DIVISION:

	£m	1988 £m
The Royal Bank of Scotland	289·4	272.0
Charterhouse (note 1)	53·4	35.1
Citizens Financial Group (note 2)	22·1	—
RoyScot Finance Group (including A. T. Mays Group)	24·1	27.8
Direct Line Insurance	8·1	4.0
Capital House Investment Management	1·2	(2.1)
Central financing costs and holding company expenses	(61·8)	(27.6)
	336·5	309.2

Notes:

1. The Charterhouse figures are stated before any transfer to inner reserves of Charterhouse Bank Limited and after making consolidation adjustments.
2. The Citizens figure of £22·1 million (U.S $35·8 million) is for the nine and a half month post-acquisition period and is stated in accordance with U.K. accounting principles (U.K. GAAP).

Financial Analyses

Continued

AVERAGE BALANCE SHEET AND RELATED INTEREST

	Average Balance* £m	Rate %	Interest £m	1986 Average Balance* £m	1986 Rate %	1986 Interest £m
Assets						
Short-term funds						
domestic	5,189·7	11·0	572·4	4,787.3	8.8	422.6
foreign†	3,083·1	11·4	351·1	2,748.4	7.7	211.5
Investments						
domestic	283·2	12·7	36·0	351.2	10.3	36.2
foreign	426·9	7·6	32·5	164.3	6.4	10.5
Advances to customers						
domestic	9,198·0	14·7	1,353·7	7,849.5	10.9	855.0
foreign	2,331·0	12·5	290·4	1,211.2	11.3	136.7
Lease and H.P. receivables						
domestic	1,564·4	12·5	195·2	1,231.7	10.7	132.4
foreign	56·6	7·8	4·4	42.8	8.2	3.5
Interest earning assets	22,132·9	12·8	2,835·7	18,386.4	9.8	1,808.4
Non-interest earning assets	1,410·4	—	—	1,132.8	—	—
Total average assets	23,543·3	12·0	2,835·7	19,519.2	9.3	1,808.4
Liabilities						
Commercial paper						
domestic	—	—	—	—	—	—
foreign	76·3	10·0	7·6	113.3	7.3	8.3
Short-term borrowings						
domestic	4,507·7	10·9	493·4	4,204.2	8.3	348.9
foreign	1,247·2	11·4	142·1	652.1	8.3	54.0
Demand and savings deposits						
domestic	9,604·4	10·7	1,031·5	7,859.5	7.1	561.8
foreign	3,507·5	10·4	365·3	2,430.9	8.1	197.0
Loan capital	958·2	10·7	102·5	705.4	9.2	64.7
Interest bearing liabilities	19,901·3	10·8	2,142·4	15,965.4	7.7	1,234.7
Interest free liabilities						
demand deposits	1,536·5	—	—	1,641.3	—	—
other liabilities	844·2	—	—	780.5	—	—
Shareholders' funds	1,261·3	—	—	1,132.0	—	—
Total average liabilities	23,543·3	9·1	2,142·4	19,519.2	6.3	1,234.7

*Average balances have been calculated on a daily basis using customers' cleared balances, netted where interest set-off arrangements exist.

†In addition to customers' balances held at subsidiaries and branches located overseas, 'foreign' includes overseas residents' balances held at domestic offices.

CHANGES IN NET INTEREST INCOME—VOLUME AND RATE ANALYSIS

	1989 over 1988			1988 over 1987		
	Increase/(decrease) due to changes in:					
	Average volume £m	Average rate £m	Net change £m	Average volume £m	Average rate £m	Net change £m
Interest earning assets						
Short-term funds						
domestic	44.5	105.3	149.8	106.7	(46.9)	59.8
foreign	37.9	101.7	139.6	40.6	40.2	80.8
Investments						
domestic	(8.6)	8.4	(0.2)	3.9	(2.5)	1.4
foreign	20.0	2.0	22.0	(2.5)	0.8	(1.7)
Advances to customers						
domestic	200.4	298.3	498.7	102.9	(34.4)	68.5
foreign	139.2	14.5	153.7	(12.3)	2.6	(9.7)
Lease and H.P. receivables						
domestic	40.6	22.2	62.8	21.6	(8.3)	13.3
foreign	1.1	(0.2)	0.9	0.9	(0.4)	0.5
Total interest income	475.1	552.2	1,027.3	261.8	(48.9)	212.9
Interest bearing liabilities						
Commercial paper						
domestic	—	—	—	—	—	—
foreign	(3.8)	3.1	(0.7)	1.0	0.9	1.9
Short-term borrowings						
domestic	35.2	109.3	144.5	25.6	(3.9)	21.7
foreign	67.9	20.2	88.1	9.0	7.6	16.6
Demand and savings deposits						
domestic	186.8	282.9	469.7	131.0	(79.2)	51.8
foreign	112.4	55.9	168.3	16.8	26.8	43.6
Loan capital	27.2	10.6	37.8	11.1	0.6	11.7
Total interest expense	425.7	482.0	907.7	194.5	(47.2)	147.3
Changes in net interest income						
domestic	27.7	31.4	59.1	67.4	(9.6)	57.8
foreign	21.7	38.8	60.5	(0.1)	7.9	7.8
	49.4	70.2	119.6	67.3	(1.7)	65.6

The above table allocates changes in net interest income between volume and rate. Volume and rate variances have been calculated based on movements in average balances over the periods and changes in interest rates on average interest earning assets and average interest bearing liabilities.

Financial Analyses

Continued

Interest rates, yields, spreads and margins

	Average rate %	1988 Average rate %
United Kingdom		
The Royal Bank of Scotland plc base rate	13.2	9.3
The Royal Bank of Scotland plc home mortgage rate	13.5	10.6
London inter-bank offered rate		
three month sterling	13.3	9.4
three month eurodollar	9.3	7.7
United States		
Prime rate	10.8	9.0
Yields, spreads and margins:		
Gross yield[1]		
total	12.8	9.8
domestic	13.3	10.2
foreign	11.5	8.7
Interest spread[2]		
total	2.0	2.1
domestic	2.5	2.6
foreign	0.8	0.6
Interest margin[3]		
total	3.1	3.1
domestic	3.3	3.3
foreign	2.8	2.5
Average margin between base rate and standard deposit rate	5.5	4.9

[1] Gross yield is the average interest rate earned on interest earning assets.

[2] Interest spread is the difference between the average interest rate earned on interest earning assets and the average interest rate paid on interest bearing liabilities.

[3] Interest margin is net interest income as a percentage of average interest earning assets.

Cross border outstandings in excess of 1 per cent. of total assets

The following table identifies countries to which the Group's cross border outstandings exceeded 1 per cent. of total assets at 30th September 1989.

	Commercial, industrial and other private sector £m	Governments and official institutions £m	Banks and other financial institutions £m	Total £m	As % of total assets*
Canada	66.0	1.0	23[illegible].0	299.0	1.1
France	8.0	2.0	397.0	407.0	1.5
Japan	11.0	—	663.0	674.0	2.4
United States	404.0	1.0	284.0	689.0	2.5

*Assets comprise total assets employed as reported in the consolidated balance sheet and acceptances as reported in the notes on the accounts, which together totalled £27,970.0 million at 30th September 1989.

Cross border outstandings between ¾ per cent. and 1 per cent. of total assets

At 30th September 1989, cross border outstandings to borrowers in countries in which such outstandings amounted to between ¾ per cent. and 1 per cent. of total assets totalled £279 million in aggregate. The country concerned was Italy.

Financial Analyses

Continued

ANALYSIS OF ADVANCES

The following table analyses, for domestic and foreign activities, advances to customers (before provisions) and amounts receivable under finance leases by type of customer and geographical area.

	At 30th September				
	1985 £m	1986 £m	1987 £m	1988 £m	1989 £m
Domestic					
Loans guaranteed by exports credit guarantee department	240.0	371.1	321.7	255.1	213·1
Central and local government and government owned corporations	65.2	43.5	37.2	68.6	52·6
Manufacturing	954.4	1,020.5	1,035.8	1,150.0	1,447·9
Construction	300.0	331.2	374.9	428.3	521·9
Finance	550.7	705.9	1,046.8	628.3	768·5
Service industries	723.3	718.7	930.2	1,109.5	1,618·4
Agriculture, forestry and fishing	517.8	541.7	540.2	552.6	588·0
Property	458.6	566.4	621.0	706.4	880·2
Business and other services	1,102.0	1,179.7	1,148.8	1,225.3	1,620·5
Persons: home mortgages	626.6	681.7	1,282.8	1,807.5	2,163·2
other	1,114.3	1,297.2	1,253.7	1,560.3	1,991·8
Other loans	28.6	29.2	46.6	68.1	19·6
Instalment credit	207.0	304.9	357.2	425.8	452·2
Finance leases	641.4	769.6	856.7	1,009.9	1,246·7
Total domestic advances	7,529.9	8,561.3	9,853.6	10,995.7	13,584·6
Foreign					
Foreign-U.K. based*	870.6	680.5	645.3	695.2	722·2
Europe other than the U.K.	70.7	81.0	112.7	108.0	127·4
United States	93.9	91.2	157.1	194.1	1,466·3
Rest of the World	115.5	80.7	99.6	132.8	333·4
Total foreign advances	1,150.7	933.4	1,014.7	1,130.1	2,649·3
Accrued interest	106.8	87.2	63.1	38.7	235·6
Total advances	8,787.4	9,581.9	10,931.4	12,164.5	16,469·5

*The term 'Foreign–U.K. based' refers to advances by offices in the United Kingdom made to customers domiciled outside the United Kingdom.

Financial Analyses

Continued

SELECTED FIGURES IN ACCORDANCE WITH U.S. GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

The Group's consolidated financial statements are prepared in accordance with U.K. accounting principles (U.K. GAAP). These differ in certain significant respects from accounting principles followed in the U.S.A. (U.S. GAAP).

The following tables summarise the significant adjustments to profit attributable to ordinary shareholders (net income), shareholders' equity and total assets which would result from the application of U.S. GAAP instead of U.K. GAAP.

	£m	1988 £m
Net income as reported under U.K. GAAP	147·1	192.5
Property depreciation	(0·2)	(0.2)
Deferred tax	2·0	4.2
Amortisation of goodwill	(6.9)	(2.7)
Amortisation of debt issue expenses	(1·3)	(0.7)
Loan origination fees	(6·0)	(4.2)
Pension costs	2·0	(11.1)
Approximate net income under U.S. GAAP	136·7	177.8

	£m	1988 £m
Shareholders' equity as reported under U.K. GAAP	1,410·7	1,269.7
Revaluation of property less depreciation	(221·8)	(221.6)
Deferred tax	(11·6)	(13.6)
Amortisation of goodwill	156·6	60.1
Amortisation of debt issue expenses	20·0	7.3
Loan origination fees	(19·1)	(13.1)
Proposed dividend	36·1	27.9
Pension costs	(15·0)	(17.0)
Approximate shareholders' equity under U.S. GAAP	1,355·9	[illegible]

	£m	1988 £m
Total assets as reported under U.K. GAAP	27,435·7	21,659.9
Revaluation of property less depreciation	(221·8)	(221.6)
Amortisation of goodwill	156·6	60.1
Amortisation of debt issue expenses	20·0	7.3
Acceptances	534·3	770.2
Approximate total assets under U.S. GAAP	27,924·8	22,275.9

Principal Offices in Great Britain

The company

Head office

42 St Andrew Square Edinburgh EH2 2YE

London office

67 Lombard Street London EC3P 3DL

The Royal Bank of Scotland plc

Head office

42 St Andrew Square Edinburgh EH2 2YE

Regional offices

9 Rubislaw Terrace Aberdeen AB9 8YQ
36 St Andrew Square Edinburgh EH2 2YB
Dale House 21 West George Street Glasgow G2 1EW
Regent's House Islington London N1 8XL
45 Mosley Street Manchester M60 2BE

Main offices

46/48 Deansgate Bolton BL1 1BH
142/144 Princes Street Edinburgh EH2 4EQ
36 St Andrew Square Edinburgh EH2 2YB
98 Buchanan Street Glasgow G1 3BA
113 Buchanan Street Glasgow G1 2SP
1 Dale Street Liverpool L2 2PP
7 Burlington Gardens London W1A 3DD
Child & Co. 1 Fleet Street London EC4Y 1BD
Drummonds 49 Charing Cross London SW1A 2DX
5/10 Great Tower Street London EC3P 3HX
Holt's Whitehall London SW1A 2EB
67 Lombard Street London EC3P 3DL
22 St Mary Axe London EC3A 8DD
62/63 Threadneedle Street London EC2R 8LA
38 Mosley Street Manchester M60 2BE
St Ann Street Manchester M60 2SS
8 South Parade Nottingham NG1 2JS
97 Fishergate Preston PR1 2DP
5 Church Street Sheffield S1 1HF
32 Wallgate Wigan WN1 1LA

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2 Festival Square Edinburgh EH3 9SU
98 King Street Manchester M2 4WU
198 West George Street Glasgow G2 2NR

A.T. Mays Group PLC

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Direct Line Insurance plc

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Cavendish House 51/55 Southend Croydon CR0 1BF
Direct Line House 139 West Regent Street Glasgow G2 2SG

Charterhouse plc

Head office

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Charterhouse Bank Limited

1 Paternoster Row St Paul's London EC4M 7DH
26 St Andrew Square Edinburgh EH2 1AF
55 Spring Gardens Manchester M2 2BY

Charterhouse Development Capital Limited

7 Ludgate Broadway London EC4V 6DX
26 St Andrew Square Edinburgh EH2 1AF
55 Spring Gardens Manchester M2 2BY

Charterhouse Tilney

Private client and research department:
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Institutional sales and research department:
1 Paternoster Row St Paul's London EC4M 7DH
Private client department:
Warnford Court Throgmorton Street London EC2 2AT

RoyScot Finance Group plc

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RoyScot Corporate Leasing

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Birchin Court 19/25 Birchin Lane London EC3V 9DJ
Edward House 289 West Campbell Street Glasgow G2 4UG
Bridgewater House 60 Whitworth Street Manchester M1 6LT

RoyScot Factors Limited

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31 St Andrew Square Edinburgh EH2 2PS

RoyScot Financial Services Limited

Edward House 289 West Campbell Street Glasgow G2 4UG

RoyScot Trust plc

RoyScot House The Promenade Cheltenham GL50 1PL
14 Lynedoch Crescent Glasgow G3 6EQ

RoyScot Drive

286 Chase Road Southgate London N14 6HF

Overseas Offices

Citizens Financial Group, Inc.
870 Westminster Street Providence Rhode Island 02903 U.S.A.

Rhode Island subsidiaries
Citizens Savings Bank
Citizens Trust Company
Citizens Leasing Corporation
Citizens Financial Services Corporation

Out-of-state subsidiaries
Gulf States Mortgage Co., Inc.
900 Circle 75 Parkway Atlanta Georgia 30339 U.S.A.

Fairhaven Savings Bank
215 Washington Street Fairhaven Massachusetts 02719 U.S.A.

The Royal Bank of Scotland plc
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ASEAN and Australasia regional office:
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San Francisco agency:
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Representative offices
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Suite 4950 1000 Louisiana
Houston Texas 77002 U.S.A.
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The Royal Bank of Scotland AG
Talstrasse 82 8001 Zürich Switzerland

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1 Corral Road Gibraltar

The Royal Bank of Scotland (Guernsey) Limited
La Tour Gand House
Pollet St Peter Port Guernsey Channel Islands

The Royal Bank of Scotland Trust Company (Guernsey) Limited
La Tour Gand House
Pollet St Peter Port Guernsey Channel Islands

The Royal Bank of Scotland (I.O.M.) Limited
Victory House Prospect Hill Douglas Isle of Man

The Royal Bank of Scotland (Jersey) Limited
22 Hill Street St Helier Jersey Channel Islands

The Royal Bank of Scotland Trust Company (C.I.) Limited
Capital House Bath Street St Helier Jersey Channel Islands

The Royal Bank of Scotland (Nassau) Limited
50 Shirley Street Nassau Bahamas
The Royal Bank of Scotland plc is a member of the Inter-Alpha Group of Banks

The Royal Bank of Scotland plc also operates in the Far East through a subsidiary company:
Associated Merchant Bank Pte Limited
9 Battery Road 08-03 Straits Trading Building Singapore 0104
and through an affiliated non-banking financial institution:
P.T. Multinational Finance Corporation
PO Box 730KBY Wisma BCA 12th Floor Jalan Jenderal Sudirman
Kav 22-23 Jakarta 12920 Indonesia

Charterhouse Associates S.A.
47 Avenue George V 75008 Paris France

Charterhouse Inc.
535 Madison Avenue New York NY 10022 U.S.A.

Capital House International Investment Management Limited
701/704 Two Exchange Square
8 Connaught Place Central Hong Kong
Capital House Bath Street St Helier Jersey Channel Islands

Analyses of Ordinary Shareholdings

at 2nd November 1989

	Number of shareholdings	Shares of 25p each Number in millions	% of total
Female	16,677	78.0	10.4
Male	16,350	66.4	8.8
Trustee and joint accounts	1,332	7.0	0.9
Banks and nominee companies	3,137	426.1	56.7
Investment companies	85	3.3	0.5
Insurance companies	227	89.0	11.8
Other companies	705	25.1	3.3
Pension funds	37	32.1	4.3
Universities, schools and others	265	24.8	3.3
	38,815	751.8	100.0

Range of shareholdings:

1– 500	4,307	0.8	0.1
501– 1,000	3,969	3.1	0.4
1,001– 5,000	20,762	55.0	7.3
5,001– 10,000	5,989	42.2	5.6
10,001– 25,000	2,658	40.0	5.3
25,001– 50,000	493	16.8	2.2
50,001–100,000	198	14.0	1.9
100,001 and over	439	579.9	77.2
	38,815	751.8	100.0

Financial Calendar

If approved, the final dividend on the ordinary shares for the year ended 30th September 1989 will be paid on 1st March 1990 to those shareholders registered on 21st December 1989. If the necessary approval is obtained from shareholders at the annual general meeting on 11th January 1990, as an alternative to cash, a scrip dividend election is to be offered and shareholders will receive details of this by letter after that date.

The interim dividend on the ordinary shares is normally paid in July.

Dividends on the cumulative preference shares are payable on 31st May and 31st December each year.

Half-year results *Announced on 3rd May 1989*
Full year results *Announced on 30th November 1989*
Report and accounts *Posted to shareholders on 14th December 1989*
Annual general meeting *To be held in Edinburgh on 11th January 1990*

Notice of Meeting

Notice is hereby given that the twenty-second annual general meeting of the members of The Royal Bank of Scotland Group plc will be held in the Caledonian Hotel, Edinburgh, on Thursday, 11th January 1990, at 12 noon, for the following purposes:

1 To receive and consider the accounts to 30th September 1989 and the reports of the directors and auditors thereon.

2 To declare a final dividend on the ordinary shares *(resolution numbered 1 on the proxy form)*.

3 To reappoint directors *(resolutions numbered 2 to 7 inclusive on the proxy form)*.

4 To reappoint Deloitte Haskins & Sells as auditors *(resolution numbered 8 on the proxy form)*.

5 To authorise the directors to fix the remuneration of the auditors *(resolution numbered 9 on the proxy form)*.

6 To consider and, if thought fit, pass the resolutions set out in the Appendix to the circular letter to shareholders dated 5th December 1989 accompanying the report and accounts of which this notice forms a part. The resolutions are numbered 10 to 13 inclusive on the proxy form, and resolution numbered 12 will be proposed as a special resolution with the remaining resolutions being proposed as ordinary resolutions.

By order of the board.

M R M^cKee

Secretary

36 St Andrew Square, Edinburgh
5th December 1989

Note:

Every member entitled to attend and vote at the meeting is entitled to appoint a proxy or proxies to attend and, on a poll, vote instead of the member. A proxy need not be a member of the company. A pre-paid form appointing a proxy is enclosed with this notice. To be effective, it must be completed and be received at the company's transfer office not less than forty-eight hours before the time fixed for the meeting.

Copies of directors' service contracts, together with a statement of all transactions of each director of the company and, so far as he is aware or can reasonably ascertain, of his family interests in the shares of the company and of its subsidiaries and in the loan capital of the company and its subsidiaries covering the period from 6th December 1988 to 4th December 1989, will be available for inspection at the company's registered office during the usual business hours on any weekday (Saturdays and public holidays excepted) from the date of this notice until the date of the meeting and at the place of the meeting for at least fifteen minutes prior to the meeting and during the meeting.