# Barclays PLC

# IFRS 9 Transition Note

March 2018

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### Forward-looking statements

This document contains certain forward-looking statements within the meaning of Section 21E of the US Securities Exchange Act of 1934, as amended, and Section 27A of the US Securities Act of 1933, as amended, particularly estimates with respect to the effect of the implementation of IFRS 9 on Barclays Group. Barclays cautions readers that no forward-looking statement is a guarantee of future performance and that actual results or other financial condition or performance measures could differ materially from those contained in the forward-looking statements. These forward-looking statements can be identified by the fact that they do not relate only to historical or current facts. Forward-looking statements use words such as 'may', 'will', 'seek', 'continue', 'aim', 'anticipate', 'target', 'projected', 'expect', 'estimate', 'intend', 'plan', 'goal', 'believe', 'achieve', or other words of similar meaning. Examples of forward-looking statements include, amongst others, statements or guidance relating to the Group's future financial position, income growth, assets, impairment charges, provisions, capital, leverage and other regulatory ratios, payments of dividends, IFRS 9 impacts and other statements that are not historical fact. These statements and estimates are based on the current assumptions, beliefs and expectations of Barclays' management. By their nature, forward-looking statements involve risk and uncertainty because they relate to future events and circumstances. These may be affected by changes in legislation, the development of standards and interpretations under the International Financial Reporting Standards including implementation of IFRS 9, evolving practices with regard to the interpretation and application of accounting and regulatory standards. For further information, see "Overview of key impacts on transition to IFRS 9" and "Measurement uncertainty."

Subject to our obligations under applicable law and regulation, we undertake no obligations to update publicly or review any forward-looking statements, whether as a result of new information or otherwise.

The reader should, however, consult any additional disclosures that Barclays has made or may make in documents it has published or may publish via the Regulatory News Service of the LSE and/or has filed or may file with the US Securities and Exchange Commission.

# Overview of key impacts on transition to IFRS 9

This document is designed to assist the reader in understanding the impact on Barclays Group of the adoption of IFRS 9 *Financial Instruments,* which replaces IAS 39 *Financial Instruments: Recognition and Measurement*, and is effective from 1 January 2018. The document provides a movement analysis from IAS 39 reported numbers as included in the Barclays PLC Annual Report 2017 to IFRS 9 numbers adopted from 1 January 2018.

The impact assessments included in this document have been estimated under an interim control environment with models that continue to undergo validation. The implementation of the comprehensive end state control environment will continue as Barclays introduces business-as-usual controls throughout 2018. The impacts below are point in time estimates and should not be considered to be forecasts.

The key impacts arising from the implementation of IFRS 9 on 1 January 2018 are as follows:

### Significant and material impacts

- Total impairment allowance and provisions increased by approximately £2.76bn from £4.8bn as at 31 December 2017 to £7.5bn as at 1 January 2018, a 58% increase.
- The impact of the 'Classification and measurement' changes introduced by IFRS 9 is not material to Barclays, with an overall decrease in shareholders' equity of £17m.
- Shareholders' equity decreased by approximately £2.2bn post tax, reducing TNAV by 13 pence per share.
- The estimated impact on CET1 capital is a reduction of £1.0bn, driven by the decrease in shareholders' equity of £2.2bn, offset by a reduction in the regulatory deduction where expected loss is greater than impairment of £1.2bn.
- The impact on the Barclays PLC CET1 ratio is a reduction of approximately 34bps from 13.3% as at 31 December 2017 to 12.9% as at 1 January 2018 on a fully loaded basis.
- After applying the transitional arrangements outlined in Capital Requirements Regulation Article 473a, the ratio is unchanged at 13.3% as at 1 January 2018.

# Background

### Introduction

From 1 January 2018, a new accounting standard, IFRS 9, is effective which prescribes the rules for measuring impairment allowances for financial assets, the classification and measurement of financial assets, and hedge accounting. This transition note supplements information provided in the Barclays PLC Annual Report 2017 and provides initial disclosures to assist the reader in understanding the impact of implementing the new requirements as at 1 January 2018. Whilst there are no mandatory, prescriptive guidelines on the disclosure requirements for this transition note, the requirements in the following documents have been considered and incorporated where appropriate prior to more extensive disclosures in the Barclays PLC Annual Report 2018:

- IFRS 9, including the narrow scope amendment issued by the International Accounting Standards Board (IASB) in October 2017;
- IFRS 7 *Financial instruments: Disclosures* requirements relating to the initial application of IFRS 9;
- Enhanced Disclosure Task Force guidance issued in November 2015; and
- PRA guidance issued in January 2018.

### International Financial Reporting Standards (IFRS)

In July 2014, the IASB published the final version of IFRS 9 *Financial Instruments* replacing IAS 39, *Financial Instruments: Recognition and measurement*. IFRS 9 was endorsed by the European Union (EU) in November 2016, and is effective for accounting periods beginning on or after 1 January 2018. A narrow-scope amendment to IFRS 9 was issued by the IASB in October 2017. As Barclays expects the EU to endorse the amendment by 31 December 2018, the amendment has been applied in relation to the impacts included within this transition note.

IFRS 9 introduces key changes in the following areas:

1. Classification and measurement - requiring asset classification and measurement based upon both business model and product characteristics.
2. Impairment – introducing an expected credit loss model using forward looking information which replaces an incurred loss model.
3. Hedge accounting – introducing changes to, and wider eligibility criteria to hedging of financial instruments.

### 1. Classification and measurement

IFRS 9 requires the classification of financial assets to be determined by a contractual cash flows test referred to as "Solely payment of principal and interest" (SPPI) and a business model test.

Financial assets that fail the SPPI test will be measured at Fair value through the income statement.

For assets passing the SPPI test, a business model test assesses the objective of holding the asset. The business model test for financial assets can be summarised as follows:

- Financial assets will be measured at amortised cost if they are held within a business model where the objective is to hold financial assets in order to collect contractual cash flows ("Hold to collect" business model).

- Financial assets will be measured at fair value through other comprehensive income if they are held within a business model where the objective is achieved by both collecting contractual cash flows and selling financial assets ("Hold to collect and sell" business model).

- Financial assets will be measured at fair value through the income statement if they do not meet the business model criteria of either "Hold to collect" or "Hold to collect and sell".

- Entities also have the option to designate a financial asset as measured at fair value through the income statement if doing so eliminates or significantly reduces a measurement or recognition inconsistency (accounting mismatch).

### 2. Impairment

IFRS 9 introduces a new impairment model that requires the recognition of expected credit losses on all financial assets at amortised cost or at fair value through other comprehensive income (other than equity instruments), lease receivables and certain loan commitments and financial guarantee contracts. The expected credit loss must also consider forward looking information to recognise impairment allowances earlier in the lifecycle of a product. IFRS 9 consequently is likely to increase the volatility of impairment allowances as the economic outlook changes, although cash flows and cash losses are expected to remain unchanged.

IFRS 9 introduces a three-stage approach to impairment as follows:

- Stage 1 - the recognition of 12 month expected credit losses (ECL), that is the portion of lifetime expected credit losses from default events that are expected within 12 months of the reporting date, if credit risk has not increased significantly since initial recognition;
- Stage 2 - lifetime expected credit losses for financial instruments for which credit risk has increased significantly since initial recognition; and
- Stage 3 - lifetime expected credit losses for financial instruments which are credit impaired.

In contrast, the IAS 39 impairment allowance assessment was based on an incurred loss model, and measured on assets where there was objective evidence that loss had been incurred, using information as at the balance sheet date.

Please see "Impairment allowance reconciliations" on pages 6-7 for further information on the increase in impairment upon adoption of IFRS 9 and "Expected Credit Losses" on page 8 for detail of exposures and impairment allowances by stage.

## 3. Hedge accounting

IFRS 9 revises the requirements on hedge accounting, adoption of which is optional. In addition, certain aspects of IAS 39, being the portfolio fair value hedge accounting model for interest rate risk, continues to be available for entities (while applying IFRS 9 to the remainder of the entity's hedge accounting relationships) until the IASB completes its accounting for dynamic risk management project.

Barclays will continue to apply the relevant IAS 39 hedge accounting requirements, and will implement the amended IFRS 7 hedge accounting disclosure requirements.

### Early adoption of own credit recognition in Other Comprehensive Income

From 1 January 2017, Barclays had applied the option in IFRS 9 to recognise changes in own credit for financial liabilities designated at fair value through profit and loss under the fair value option in other comprehensive income.

### Presentation of comparatives

As permitted by IFRS 9, Barclays is not restating comparatives on initial application. This transition note provides a reconciliation of the closing balance sheet as at 31 December 2017 to the opening balance sheet at 1 January 2018, together with a summary of the impact on the financial statements, risk reporting, key performance indicators and regulatory capital ratios.

### Balance sheet presentation

Whilst not required by IFRS 9, Barclays has introduced changes to balance sheet presentation. These changes are introduced within this transition note and will be used going forward. Please see "Balance sheet movement" on page 14 for further information.

# Impairment allowance reconciliations

### Reconciliation from IAS 39 to IFRS 9 - financial assets under IFRS 9 subject to an increase in impairment allowance

The table below, reconciles the closing impairment allowances for financial assets in accordance with IAS 39 and provisions for loan commitments and financial guarantee contracts in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* as at 31 December 2017 and the opening impairment allowances determined in accordance with IFRS 9 as at 1 January 2018.

| Reconciliation of impairment allowance and provisions | Impairment allowance under IAS 39 or provision under IAS 37 | Reclassification impact | Additional IFRS 9 impairment allowance | Impairment allowance under IFRS 9 |
|---|---|---|---|---|
| | £m | £m | £m | £m |
| Loans and advances at amortised cost | 4,652 | (52) | 2,508 | 7,108 |
| Available for sale investments / Financial assets at fair value through other comprehensive income | 38 | (38) | 3 | 3 |
| **Total on-balance sheet** | **4,690** | **(90)** | **2,511** | **7,111** |
| Provision for undrawn contractually committed facilities and guarantee contracts | 79 | - | 341 | 420 |
| **Total impairment and provision** | **4,769** | **(90)** | **2,852** | **7,531** |

- The introduction of IFRS 9 has increased the total impairment allowance held by Barclays by approximately £2.76bn, from £4.8bn as at 31 December 2017 to £7.5bn as at 1 January 2018, as a result of earlier recognition of impairment allowances.
- The Reclassification impact is due to the reclassification of assets to Fair Value through the Income Statement treatment that do not have an impairment allowance under IFRS 9.

## Reconciliation from IAS 39 to IFRS 9 – impairment allowance and provisions

The table below presents a reconciliation of the IAS 39 impairment allowances for incurred credit losses to IFRS 9 impairment allowances for expected credit losses by major product.

| Impairment allowance | Total<br>£m | Of which: Credit cards, unsecured and other retail lending<br>£m |
|---|---|---|
| **Total IAS 39 impairment allowance and IAS 37 Provision** | **4,769** | **3,073** |
| Less: available for sale investments | (38) | - |
| Less: Identified impairment on fair value assets no longer in scope under IFRS 9 | (52) | - |
| Less: Management adjustments to IAS 39 impairment allowance incorporated in modelling | (306) | (54) |
| IFRS 9 incremental impact of 12 month impairment allowance | 291 | 151 |
| IFRS 9 incremental impact of lifetime impairment allowance | 2,553 | 2,097 |
| IFRS 9 additional impairment allowance on assets impaired under IAS 39 | 314 | 258 |
| **Total impact of IFRS 9 on impairment allowances and provisions** | **2,852** | **2,452** |
| **Total impairment allowance under IFRS 9** | **7,531** | **5,525** |

The concepts and methodology under the two bases are different and therefore, assumptions have been made to derive the incremental impact under the three categories in the table for illustration purposes.

The impact on impairment allowance generated by multiple economic scenario modelling is embedded in the individual categories above.

*Incremental impact of 12 month impairment allowance*

This compares Stage 1 balances, which have not had a significant increase in credit risk under IFRS 9, against IAS 39 exposures that may have been subject to an impairment allowance. For Retail this includes allowances for unidentified impairment for accounts that do not trigger PD deterioration criteria for stage 2 and identified impairment for accounts less than 30 days past due; and for Wholesale this includes allowances for unidentified impairment for live accounts and accounts in watch list 1 (see Glossary for definition of watch list items).

*Incremental impact of lifetime impairment allowance*

This compares Stage 2 balances, which have had a significant increase in credit risk or require additional allowance against IAS 39 exposures that may have been subject to an impairment allowance. For Retail this includes allowances for unidentified impairment for accounts that trigger PD deterioration criteria for stage 2, High Risk Account Management assets, assets in rehabilitation (i.e. accounts curing out of stage 3) and accounts more than 30 days but less than 90 days past due; for Wholesale this includes allowances for unidentified impairment for accounts in watch list 2 and watch list 3.

The majority of this increase was due to PD deterioration notably from the unsecured portfolios now being assessed with a Lifetime PD, most significantly UK Cards and US Cards. The remaining increase in allowance was due to the difference in the way ECL and incurred loss provisions are calculated for delinquent accounts, classified as collectively impaired under IAS 39, and yet to reach the trigger for Stage 3.

*Additional impairment allowance on assets impaired under IAS 39*

This relates to Stage 3 balances and is due to the differences in the way ECL and incurred loss provisions are calculated, including the use of probability weighted economic scenarios as opposed to an expected outcome. For Retail this includes allowances for identified impairment for accounts greater than 90 days past due, accounts in forbearance and assets in recovery; for Wholesale this includes allowances for identified impairment for accounts in watch list 4.

Stage 3 accounts are assigned a PD of 1. In Retail portfolios, the increase was mainly attributed to new models under IFRS 9 together with a 90 days past due (dpd) trigger into Stage 3 for unsecured portfolios (180 dpd for mortgages) compared to previously where, under IAS 39, the collective models default definition would have been based on 180 days past due.

# Expected Credit Losses

IFRS 9 impairment requirements apply to all financial assets classified at amortised cost, lease receivables, debt financial assets at fair value through other comprehensive income, loan commitments and financial guarantee contracts. This contrasts to the IAS 39 impairment requirements applicable to the above, with the exception of loan commitments and financial guarantee contracts covered by IAS 37. In addition, IAS 39 required impairment assessment for available for sale equity instruments based on significant and prolonged decline in fair value which is out of scope under IFRS 9.

IFRS 9 requires the recognition of 12 month expected credit losses (the portion of lifetime expected credit losses from default events that are expected within 12 months of the reporting date) if credit risk has not significantly increased since initial recognition (stage 1), and lifetime expected credit losses for financial instruments for which the credit risk has increased significantly since initial recognition (stage 2) or which are credit impaired (stage 3).

### Financial Instruments with impairment, by stage

The table below presents a breakdown of gross financial assets in scope of IFRS 9 where there has been an increase in impairment allowance with stage allocation by asset classification, including off balance sheet exposures.

| | Gross exposure | | | | Impairment allowance | | | |
|---|---|---|---|---|---|---|---|---|
| | Stage 1 | Stage 2 | Stage 3 | Total | Stage 1 | Stage 2 | Stage 3 | Total |
| As at 01.01.18 | £m | £m | £m | £m | £m | £m | £m | £m |
| Loans and advances at amortised cost | 265,617 | 49,592 | 9,081 | 324,290 | 613 | 3,112 | 3,383 | 7,108 |
| Financial assets at FVOCI[1] | 51,846 | 2 | - | 51,848 | 3 | - | - | 3 |
| Off balance sheet loan commitments and financial guarantee contracts | 294,264 | 38,867 | 1,442 | 334,573 | 133 | 259 | 28 | 420 |
| **Total** | **611,727** | **88,461** | **10,523** | **710,711** | **749** | **3,371** | **3,411** | **7,531** |

| | Net exposure | | | |
|---|---|---|---|---|
| | Stage 1 | Stage 2 | Stage 3 | Total |
| As at 01.01.18 | £m | £m | £m | £m |
| Loans and advances at amortised cost | 265,004 | 46,480 | 5,698 | 317,182 |
| Financial assets at FVOCI[1] | 51,843 | 2 | - | 51,845 |
| Off balance sheet loan commitments and financial guarantee contracts | 294,131 | 38,608 | 1,414 | 334,153 |
| **Total** | **610,978** | **85,090** | **7,112** | **703,180** |

[1] Excluding equities not held for trading of £1.4bn (not covered by IFRS 9).

- Stage 1: 86.1% of gross exposure in scope for IFRS 9 is in Stage 1 and has not experienced a significant increase in credit risk since origination.
- Stage 2: 12.4% of gross exposure is in Stage 2 and has seen an increase in credit risk since origination. These assets are the key driver of the increase in impairment allowances under IFRS 9.
- Stage 3: 1.5% of gross exposure is in Stage 3 which is credit impaired including defaulted assets and some forbearance assets.

# Loans and advances at amortised cost

The sections below include the analysis of loans and advances at amortised cost by business, product and credit quality excluding provisions for off-balance sheet loan commitments and financial guarantee contracts.

## Analysis of loans and advances at amortised cost

The table below presents Gross exposure, Impairment allowance and Coverage ratio by stage allocation and business segment. The net exposure is provided in order to reconcile to the balance sheet.

| | Gross exposure | | | | Impairment allowance | | | | Coverage ratio (Impairment allowance / Gross exposure) | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Stage 1 | Stage 2 | Stage 3 | Total | Stage 1 | Stage 2 | Stage 3 | Total | Stage 1 | Stage 2 | Stage 3 | Total |
| As at 01.01.18 | £m | £m | £m | £m | £m | £m | £m | £m | % | % | % | % |
| Barclays UK | 129,837 | 25,798 | 3,152 | 158,787 | 142 | 1,310 | 1,142 | 2,594 | 0.1 | 5.1 | 36.2 | 1.6 |
| Barclays International | 22,427 | 7,051 | 1,466 | 30,944 | 297 | 1,298 | 1,081 | 2,676 | 1.3 | 18.4 | 73.7 | 8.6 |
| Head Office | 6,498 | 1,596 | 952 | 9,046 | 8 | 62 | 294 | 364 | 0.1 | 3.9 | 30.9 | 4.0 |
| **Total Group retail** | 158,762 | 34,445 | 5,570 | 198,777 | 447 | 2,670 | 2,517 | 5,634 | 0.3 | 7.8 | 45.2 | 2.8 |
| Barclays UK | 22,835 | 3,880 | 1,092 | 27,807 | 25 | 88 | 114 | 227 | 0.1 | 2.3 | 10.4 | 0.8 |
| Barclays International | 75,331 | 11,128 | 2,345 | 88,804 | 139 | 349 | 694 | 1,182 | 0.2 | 3.1 | 29.6 | 1.3 |
| Head Office | 8,689 | 139 | 74 | 8,902 | 2 | 5 | 58 | 65 | - | 3.6 | 78.4 | 0.7 |
| **Total Group wholesale** | 106,855 | 15,147 | 3,511 | 125,513 | 166 | 442 | 866 | 1,474 | 0.2 | 2.9 | 24.7 | 1.2 |
| **Total loans and advances at amortised cost** | 265,617 | 49,592 | 9,081 | 324,290 | 613 | 3,112 | 3,383 | 7,108 | 0.2 | 6.3 | 37.3 | 2.2 |
| Less: Impairment allowance | | | | 7,108 | | | | | | | | |
| **Total net exposure** | | | | 317,182 | | | | | | | | |

- Stage 1 assets - impairment is calculated based on a 12 month expected loss. Coverage for these performing, non-deteriorated assets is 0.2%.
- Stage 2 assets - have seen a significant increase in credit risk but are not defaulted and are largely performing. Under IFRS 9, these assets require a lifetime expected loss to be held, driving an increase in coverage to 6.3%.
- Stage 3 assets - coverage ratio increases to 37.3%. Stage 3 includes defaulted exposures and assets under forbearance arrangements. Some of these assets remain subject to collections activities and this, along with collateral holdings, reduces expected loss levels for these assets.
- Retail coverage ratios are higher than wholesale coverage ratios, primarily driven by the nature of risk inherent in the Credit Card portfolios, partially offset by lower coverage levels in Home Loans due to the collateralised nature of the portfolio.
- Barclays International retail portfolio coverage levels are higher than those in Barclays UK reflecting the mix of assets, notably the Home Loan portfolio in Barclays UK.
- Barclays UK Stage 3 wholesale coverage ratio reflects the level of collateral held against recovery and forbearance assets in the business banking portfolio.

## Loans and advances at amortised cost by product

The table below presents an analysis of Gross exposure, Impairment allowance and Coverage ratio by product for loans and advances at amortised cost.

| | | Stage 2 | | | | | |
|---|---|---|---|---|---|---|---|
| | Stage 1 | Not past due | <30 dpd | >30 dpd | Total | Stage 3 | Total |
| As at 01.01.18 | £m | £m | £m | £m | £m | £m | £m |
| **Gross exposure** | | | | | | | |
| Home Loans[1] | 125,224 | 17,108 | 1,612 | 604 | 19,324 | 2,425 | 146,973 |
| Credit cards, unsecured and other retail lending[1] | 40,482 | 13,562 | 702 | 502 | 14,766 | 3,544 | 58,792 |
| Corporate loans | 99,911 | 14,534 | 407 | 561 | 15,502 | 3,112 | 118,525 |
| **Total** | **265,617** | **45,204** | **2,721** | **1,667** | **49,592** | **9,081** | **324,290** |
| **Impairment allowance** | | | | | | | |
| Home Loans[1] | 38 | 77 | 10 | 13 | 100 | 326 | 464 |
| Credit cards, unsecured and other retail lending[1] | 441 | 2,086 | 203 | 245 | 2,534 | 2,291 | 5,266 |
| Corporate loans | 134 | 444 | 22 | 12 | 478 | 766 | 1,378 |
| **Total** | **613** | **2,607** | **235** | **270** | **3,112** | **3,383** | **7,108** |
| **Coverage ratio** | | | | | | | |
| Home Loans[1] | - | 0.5 | 0.6 | 2.2 | 0.5 | 13.4 | 0.3 |
| Credit cards, unsecured and other retail lending[1] | 1.1 | 15.4 | 28.9 | 48.8 | 17.2 | 64.6 | 9.0 |
| Corporate loans | 0.1 | 3.1 | 5.4 | 2.1 | 3.1 | 24.6 | 1.2 |
| **Total** | **0.2** | **5.8** | **8.6** | **16.2** | **6.3** | **37.3** | **2.2** |

[1] Included in the above analysis are Wealth and Private Banking exposures measured on an individual customer exposure basis and reported as Wholesale.

- Credit cards typically have higher coverage ratios due to their unsecured nature and resulting high levels of loss given default.
- Coverage levels for Stage 3 Corporate Loans reflect a small number of idiosyncratic positions and therefore can be variable over time.
- Stage 2 includes an element of past due exposures. Coverage for these assets is materially higher than the remainder of Stage 2 assets, particularly in Credit Cards.

## Credit quality of loans and advances at amortised cost

The table below presents the credit quality by stage for loans and advances at amortised cost.

| | Strong (including investment grade) | | | | Satisfactory (BB+ to B) | | | | Higher risk (B- and below) | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Stage 1 | Stage 2 | Stage 3 | Total | Stage 1 | Stage 2 | Stage 3 | Total | Stage 1 | Stage 2 | Stage 3 | Total | Total |
| As at 01.01.18 | £m | £m | £m | £m | £m | £m | £m | £m | £m | £m | £m | £m | £m |
| **Gross exposure** | | | | | | | | | | | | | |
| Home Loans | 122,090 | 12,870 | - | 134,960 | 3,098 | 5,311 | - | 8,409 | 36 | 1,143 | 2,425 | 3,604 | 146,973 |
| Credit cards, unsecured and other retail lending | 26,992 | 3,225 | - | 30,217 | 13,383 | 9,270 | - | 22,653 | 107 | 2,271 | 3,544 | 5,922 | 58,792 |
| Corporate loans | 83,452 | 6,184 | - | 89,636 | 16,010 | 7,358 | - | 23,368 | 449 | 1,960 | 3,112 | 5,521 | 118,525 |
| **Total** | **232,534** | **22,279** | **-** | **254,813** | **32,491** | **21,939** | **-** | **54,430** | **592** | **5,374** | **9,081** | **15,047** | **324,290** |
| **Impairment allowance** | | | | | | | | | | | | | |
| Home Loans | 37 | 40 | - | 77 | 1 | 34 | - | 35 | - | 26 | 326 | 352 | 464 |
| Credit cards, unsecured and other retail lending | 221 | 329 | - | 550 | 211 | 1,458 | - | 1,669 | 9 | 747 | 2,291 | 3,047 | 5,266 |
| Corporate loans | 55 | 99 | - | 154 | 73 | 238 | - | 311 | 6 | 141 | 766 | 913 | 1,378 |
| **Total** | **313** | **468** | **-** | **781** | **285** | **1,730** | **-** | **2,015** | **15** | **914** | **3,383** | **4,312** | **7,108** |
| **Net exposure** | | | | | | | | | | | | | |
| Home Loans | 122,053 | 12,830 | - | 134,883 | 3,097 | 5,277 | - | 8,374 | 36 | 1,117 | 2,099 | 3,252 | 146,509 |
| Credit cards, unsecured and other retail lending | 26,771 | 2,896 | - | 29,667 | 13,172 | 7,812 | - | 20,984 | 98 | 1,524 | 1,253 | 2,875 | 53,526 |
| Corporate loans | 83,397 | 6,085 | - | 89,482 | 15,937 | 7,120 | - | 23,057 | 443 | 1,819 | 2,346 | 4,608 | 117,147 |
| **Total** | **232,221** | **21,811** | **-** | **254,032** | **32,206** | **20,209** | **-** | **52,415** | **577** | **4,460** | **5,698** | **10,735** | **317,182** |

- The credit quality distribution is based on IFRS 9 12 month probability of default at the reporting date.
- Stage 1 Higher risk assets, presented gross of associated collateral held, are of weaker credit quality and have not significantly deteriorated since origination. Examples would include leveraged corporate loans or non-prime credit cards.

The Group uses the following internal measures to determine credit quality for loans that are performing:

| Default Grade | Retail lending Probability of default | Wholesale lending Probability of default | Credit Quality Description |
|---|---|---|---|
| 1-3 | 0.0-0.60% | 0.0-0.05% | Strong |
| 4-5 | | 0.05-0.15% | |
| 6-8 | | 0.15-0.30% | |
| 9-11 | | 0.30-0.60% | |
| 12-14 | 0.60-10.00% | 0.60-2.15% | Satisfactory |
| 15-19 | | 2.15-11.35% | |
| 20 - 21 | 10.00%+ | 11.35%+ | Higher Risk |

For loans that are performing, these descriptions can be summarised as follows:

**Strong:** there is a very high likelihood of the asset being recovered in full.

**Satisfactory:** while there is a high likelihood that the asset will be recovered and therefore of no cause for concern to the Group, the asset may not be collateralised, or may relate to retail facilities. At the lower end of this grade there are customers that are being more carefully monitored, for example, corporate customers which are indicating some evidence of deterioration, mortgages with a high loan to value, and unsecured retail loans operating outside normal product guidelines.

**Higher risk:** there is concern over the obligor's ability to make payments when due. However, these have not yet converted to actual delinquency. However, the borrower or counterparty is continuing to make payments when due and is expected to settle all outstanding amounts of principal and interest.

Loans that are past due are monitored closely, with impairment allowances raised as appropriate and in line with the Group's impairment policies. These loans are all considered higher risk for the purpose of this analysis of credit quality.

# Regulatory capital

The Group's capital plan is set in consideration of the Group's risk profile and appetite, strategic and performance objectives, regulatory requirements, and market and internal factors, including the results of stress testing. The plan is managed through both short and long term planning cycles. Conducting stress tests ensures that the capital plan provides sufficient resilience to withstand the impact of a severe financial stress and includes an assessment of capital management actions, such as reducing dividends, which could be undertaken to improve the financial position. The most recent capital plan, stress test and capital management actions have been prepared on an IFRS 9 basis to ensure the bank remains sufficiently capitalised for both normal and stressed market conditions including the more volatile and larger range of impacts from IFRS 9.

The accounting change arising from the implementation of IFRS 9 has an impact on regulatory capital and leverage ratios with the following effects:

### Common Equity Tier 1 (CET1) capital and risk weighted assets (RWA) on a fully loaded basis

- The increase in impairment reduces CET1 capital through total equity upon first time adoption of IFRS 9;
- The increase in IRB impairment causes a reduction in the excess of expected losses over impairment deduction; and
- RWAs increase due to additional deferred tax assets (DTAs) risk weighted at 250%, offset by a reduction in standardised RWAs from the increase in the impairment allowance.

### Transitional arrangements for capital

The IFRS 9 transitional capital regime was implemented by Regulation (EU) 2017/2395, with an effective date of 1 January 2018. Barclays wrote to the PRA in Q4 2017 informing them of the intention to apply the transitional arrangement for IFRS 9, at both consolidated and individual entity levels. EU legislative bodies agreed on the transitional arrangement on 14 November 2017 and that agreement was adopted and published in the Official Journal in December 2017.

A modified static approach for the IFRS 9 transitional capital regime was implemented by Regulation (EU) 2017/2395, with an effective date of 1 January 2018 with the following key features:

- Transitional relief for the "day 1" impact on adoption of IFRS 9 (static) and for the net changes between day 1 and the reporting date (modified), subject to eligibility;
- Separate calculations for Standardised and IRB portfolios, reflecting the different ways the framework takes account of impairment; and
- Tapering of the transitional benefit over a 5 year period as follows:

  - 2018 95%
  - 2019 85%
  - 2020 70%
  - 2021 50%
  - 2022 25%
  - Thereafter 0%

## Capital impact

The table below presents the impact of the transition from IAS 39 to IFRS 9 on the regulatory capital and leverage ratios with the application of transitional provisions as per Article 473a of the Capital Requirements Regulation (CRR).

| Capital ratios - impact of transition to IFRS 9 | IAS 39 As at 31.12.17 | Impact Fully Loaded | Fully Loaded IFRS 9 As at 01.01.18 | Net impact after Transitional relief | Transitional IFRS 9 As at 01.01.18 |
|---|---|---|---|---|---|
| CET1 capital ratios | 13.3% | (0.34%) | 12.9% | 0.04% | 13.3% |
| **Capital resources** | £m | £m | £m | £m | £m |
| Shareholders' equity (excluding non-controlling interests) per the balance sheet[1] | 63,905 | (2,217) | 61,688 | (1,005) | 62,900 |
| Excess of expected losses over impairment[2] | (1,239) | 1,239 | - | 1,239 | - |
| Other regulatory adjustments and deductions | (21,101) | - | (21,101) | - | (21,101) |
| **CET1 Capital** | **41,565** | **(978)** | **40,587** | **234** | **41,799** |
| Additional tier 1 capital | 8,811 | - | 8,811 | - | 8,811 |
| **Total tier 1 capital** | **50,376** | **(978)** | **49,398** | **234** | **50,610** |
| Excess of impairment over expected losses[2] | - | 70 | 70 | 3 | 3 |
| Other tier 2 capital | 14,270 | - | 14,270 | - | 14,270 |
| **Total tier 2 capital** | **14,270** | **70** | **14,340** | **3** | **14,273** |
| **Total capital** | **64,646** | **(908)** | **63,738** | **237** | **64,883** |
| **Risk Weighted Assets (RWAs)[3]** | **313,033** | **573** | **313,606** | **840** | **313,873** |
| **Leverage Ratios[4]** | | | | | |
| UK Leverage ratio total exposure measure | **984,710** | (635) | **984,075** | 577 | **985,287** |
| CRR Leverage ratio total exposure measure | **1,124,521** | (635) | **1,123,886** | 577 | **1,125,098** |
| UK Leverage tier 1 capital | **50,376** | (978) | **49,398** | 234 | **50,610** |
| CRR Leverage tier 1 capital | **50,376** | (978) | **49,398** | 234 | **50,610** |
| UK Leverage ratio | **5.1%** | (0.10%) | **5.0%** | 0.02% | **5.1%** |
| CRR Leverage ratio | **4.5%** | (0.08%) | **4.4%** | 0.02% | **4.5%** |

The implementation of IFRS 9 results in a reduction in the fully loaded CET1 ratio of 34bps. With the application of CRR Article 473a transitional provisions, the impact is an increase of 4bps as at 1 January 2018.

[1]*Impact to Shareholders' equity*
Total increase in impairment allowances as a result of IFRS 9, net of tax, decreases shareholders equity through retained earnings by £2.2bn.

[2]*Impact to excess of expected losses over impairment allowances deduction*
For regulatory Internal Ratings Based (IRB) exposures, the calculation of capital takes account of the expected loss via a comparison with the impairment allowances. Under IAS 39, this resulted in an excess of expected loss that was deducted from CET1 capital. Under IFRS 9, the impairment allowances change to an expected credit loss model and therefore the regulatory shortfall has been eliminated. Where the impairment allowance is higher than expected loss, the excess is added back to tier 2 capital and capped at an amount of 0.6% of IRB RWAs.

[3]*Impact to RWAs*
The DTAs created from the increase of impairment have been risk weighted at 250%, thereby increasing RWAs. When DTAs arising from temporary differences are above the 10% CET1 capital threshold, any excess above the threshold is deducted and those below the threshold are risk weighted at 250% up to the point they reach threshold. Standardised RWAs have decreased due to the increase in impairment being offset against the Standardised Credit Risk exposures.

[4]*Impact to Leverage*
UK and CRR leverage ratios on a fully loaded basis decrease by approximately 10bps and 8bps respectively. This is largely due to the decrease in Tier 1 capital. With the application of CRR Article 473a transitional provisions, the impact is immaterial as at 1 January 2018.

# Balance sheet movement

The table below presents an indicative impact of the changes to balance sheet presentation and of the transition to IFRS 9 on Barclays PLC's consolidated balance sheet showing separately the changes arising from reclassification and any associated remeasurement, and the impact of increased impairment.

| | 31.12.2017 | Balance sheet presentation | IFRS 9 Classification and measurement | IFRS 9 Impairment change | 01.01.2018 |
|---|---|---|---|---|---|
| | £m | £m | £m | £m | £m |
| **Assets** | | | | | |
| Cash and balances at central banks | 171,082 | - | - | - | **171,082** |
| Items in the course of collection from other banks | 2,153 | (2,153) | - | - | **-** |
| Loans and advances to banks | 35,663 | (35,663) | - | - | **-** |
| Loans and advances to customers | 365,552 | (365,552) | - | - | **-** |
| Cash collateral and settlement balances | - | 77,168 | (2,389) | - | **74,779** |
| Loans and advances at amortised cost | - | 329,157 | (9,467) | (2,508) | **317,182** |
| Reverse repurchase agreements and other similar secured lending | 12,546 | - | (11,949) | - | **597** |
| Trading portfolio assets | 113,760 | - | 413 | - | **114,173** |
| Financial assets designated at fair value | 116,281 | (116,281) | - | - | **-** |
| Financial assets at fair value through the income statement[1] | - | 116,281 | 23,930 | - | **140,211** |
| Derivative financial instruments | 237,669 | - | - | - | **237,669** |
| Financial investments | 58,916 | (57,415) | (1,501) | - | **-** |
| Financial assets at fair value through other comprehensive income | - | 52,305 | 936 | - | **53,241** |
| Investments in associates and joint ventures[2] | 718 | - | (19) | - | **699** |
| Goodwill and intangible assets | 7,849 | - | - | - | **7,849** |
| Property, plant and equipment | 2,572 | - | - | - | **2,572** |
| Current tax assets | 482 | - | - | - | **482** |
| Deferred tax assets | 3,457 | - | - | 649 | **4,106** |
| Retirement benefit assets | 966 | - | - | - | **966** |
| Prepayments, accrued income and other assets | 2,389 | (2,389) | - | - | **-** |
| Other assets | - | 4,542 | 31 | - | **4,573** |
| Assets included in disposal groups classified as held for sale | 1,193 | - | - | - | **1,193** |
| **Total assets** | **1,133,248** | **-** | **(15)** | **(1,859)** | **1,131,374** |
| **Liabilities** | | | | | |
| Deposits from banks | 37,723 | (37,723) | - | - | **-** |
| Deposits at amortised cost | - | 398,701 | (18,860) | - | **379,841** |
| Items in the course of collection due to other banks | 446 | (446) | - | - | **-** |
| Customer accounts | 429,121 | (429,121) | - | - | **-** |
| Cash collateral and settlement balances | - | 68,143 | (2,218) | - | **65,925** |
| Repurchase agreements and other similar secured borrowing | 40,338 | - | (25,285) | - | **15,053** |
| Debt securities in issue | 73,314 | - | - | - | **73,314** |
| Subordinated liabilities | 23,826 | - | - | - | **23,826** |
| Trading portfolio liabilities | 37,351 | - | - | - | **37,351** |
| Financial liabilities designated at fair value | 173,718 | - | 46,365 | - | **220,083** |
| Derivative financial instruments | 238,345 | - | - | - | **238,345** |
| Current tax liabilities | 586 | - | - | - | **586** |
| Deferred tax liabilities | 44 | - | - | - | **44** |
| Retirement benefit liabilities | 312 | - | - | - | **312** |
| Accruals, deferred income and other liabilities | 8,565 | (8,565) | - | - | **-** |
| Other liabilities | - | 9,011 | - | - | **9,011** |
| Provisions | 3,543 | - | - | 341 | **3,884** |
| **Total liabilities** | **1,067,232** | **-** | **2** | **341** | **1,067,575** |
| **Equity** | | | | | |
| Called up share capital and share premium | 22,045 | - | - | - | **22,045** |
| Other equity instruments | 8,941 | - | - | - | **8,941** |
| Other reserves | 5,383 | - | (139) | 3 | **5,247** |
| Retained earnings | 27,536 | - | 122 | (2,203) | **25,455** |
| Total equity excluding non-controlling interests | 63,905 | - | (17) | (2,200) | **61,688** |
| Non-controlling interests | 2,111 | - | - | - | **2,111** |
| **Total equity** | **66,016** | **-** | **(17)** | **(2,200)** | **63,799** |
| **Total liabilities and equity** | **1,133,248** | **-** | **(15)** | **(1,859)** | **1,131,374** |

[1] 'Financial assets at fair value through the income statement' includes both designated and mandatory fair value assets.
[2] The impact of IFRS 9 on Group's share of profit and loss from joint ventures is shown in the classification and measurement column.

# Balance sheet commentary

The balance sheet table includes movements due to the following:

### Balance sheet presentation

Whilst not all related to IFRS 9, the following changes to the balance sheet have been introduced:

- Items in the course of collection from other banks and Prepayments, accrued income and other assets are reported in Other assets. Equally, Items in the course of collection due to other banks and Accruals, deferred income and other liabilities are reported in Other liabilities.
- Loans and advances to banks and Loans and advances to customers have been disaggregated to Loans and advances at amortised cost and Cash collateral and settlement balances. Equally, Deposits from banks and Customer accounts have been disaggregated to Deposits at amortised cost and Cash collateral and settlement balances.
- Financial assets designated at fair value have moved to Financial assets at fair value through the income statement on adoption of IFRS 9.
- The majority of available for sale assets have moved to Financial assets at fair value through other comprehensive income from Financial investments on adoption of IFRS 9. In addition, held to maturity assets have moved to Loans and advances at amortised cost.

These changes are introduced within this transition note and will be used going forward.

### Classification and measurement

This column represents the changes to the balance sheet from classification and measurement – the net effect is a decrease in shareholders' equity of £17m, with no significant offsetting movements. The classification changes include the transfer of certain Barclays International Prime Services and Equities positions from an amortised cost to a fair value approach.

Please see the Classification and Measurement section of Accounting policies, key concepts and management judgements on page 18 for further detail on the approach followed.

### Impairment

Additional impairment from the adoption of IFRS 9 is shown in the Impairment change column. The increase in impairment results in the recognition of a deferred tax asset that will amortise to current tax over time. The post tax impact is a reduction in shareholders' equity of £2.2bn. Impairment allowance under IFRS 9 considers both the drawn and the undrawn counterparty exposure. For Retail portfolios, the total impairment allowance is allocated to the drawn exposure to the extent that the allowance does not exceed the exposure. Any excess is reported on the liability side of the balance sheet as a provision. For Wholesale portfolios the impairment allowance on the undrawn exposure is reported on the liability side of the balance sheet as a provision.

# Accounting policies, key concepts and management judgements

## IFRS 9 – Financial instruments

This section focuses on key accounting policies specific to the transition to IFRS 9.

The transition document has been prepared based on IFRS 9's transition requirements, which require retrospective application by recognising the impact in the opening retained earnings of the current period. As permitted by IFRS 9, Barclays is not restating comparatives on initial application of IFRS 9 but is providing initial transitional disclosures. These disclosures compare the closing balance sheet at 31 December 2017 (under IAS 39) to the opening balance sheet at 1 January 2018 (under IFRS 9). These disclosures provide granularity and permit reconciliation between:

- the balance sheet line items under IAS 39 and IFRS 9;
- the measurement category under IAS 39 and IFRS 9; and
- the class of financial instrument as required by IFRS 7 (defined as a grouping that is appropriate for the nature of the information and takes into account the characteristics of the instruments).

Certain key transitional provisions used to calculate the transitional impact, are summarised below:

- IFRS 9 is not applied to financial instruments that have been derecognised as of 1 January 2018; and
- The classification and measurement requirements are applied considering facts and circumstances in existence as of 1 January 2018 for the business model and fair value option elections, and facts and circumstances at the date of initial recognition for the contractual cash flow characteristics of financial assets.

The impairment requirements are applied by reference to the credit quality at initial recognition i.e. the PD at transition date is compared to the PD at the date of initial recognition. Where actual information on credit quality at initial recognition is not available without undue cost or effort, an approximation may be applied using internal or external information, information about similar products, or peer group experience. In addition, the low credit risk exemption may be applied as at the transition date. Otherwise, where information on initial credit quality is not available lifetime expected credit losses must be recognised until the financial assets have been derecognised.

### (i) Impairment

IFRS 9 introduces a revised impairment model which requires entities to recognise expected credit losses based on unbiased forward-looking information. This replaces the IAS 39 incurred loss model which only recognised impairment if there is objective evidence that a loss has already been incurred and would measure the loss at the most probable outcome. The IFRS 9 impairment model is applicable to all financial assets at amortised cost, lease receivables, debt financial assets at fair value through other comprehensive income, loan commitments and financial guarantee contracts. This contrasts to the IAS 39 impairment model which was not applicable to loan commitments and financial guarantee contracts, which were covered by IAS 37. In addition, IAS 39 required the impairment of available for sale debt to be based on the fair value loss rather than estimated future cash flows as for amortised cost assets. Intercompany exposures, including loan commitments and financial guarantee contracts, are also in scope under IFRS 9 in the standalone reporting entity accounts.

### Key concepts and management judgements

The impairment requirements are complex and require management judgements, estimates and assumptions. Key concepts and management judgements include:

- Determining a significant increase in credit risk since initial recognition

IFRS 9 requires the recognition of 12 month expected credit losses (the portion of lifetime expected credit losses from default events that are expected within 12 months of the reporting date) if credit risk has not significantly increased since initial recognition (stage 1), and lifetime expected credit losses for financial instruments for which the credit risk has increased significantly since initial recognition (stage 2) or which are credit impaired (stage 3). Barclays assesses when a significant increase in credit risk has occurred based on quantitative and qualitative assessments. Exposures are considered to have resulted in a significant increase in credit risk and are moved to stage 2 when:

- **Quantitative Test**

  The annualised cumulative weighted average lifetime PD has increased by more than the agreed threshold relative to the equivalent at origination. The relative thresholds are defined as percentage increases and set at an origination score band and segment level.

- **Qualitative Test**

  Accounts that meet the portfolio's 'high risk' criteria and are subject to closer credit monitoring.

- **Backstop Criteria**

  Accounts that are 30 calendar days or more past due. The 30 days past due criteria is a backstop rather than a primary driver of moving exposures into stage 2.

Exposures move back to stage 1 once they no longer meet the criteria for a significant increase in credit risk and when any cure criteria used for credit risk management are met. This is subject to all payments being up to date and the customer evidencing ability and willingness to maintain future payments.

Barclays does not rely on the low credit risk exemption which would assume facilities of investment grade are not significantly deteriorated.

Determining the probability of default at initial recognition requires management estimates, in particular for exposures issued before the effective date of IFRS 9. For certain revolving facilities such as credit cards and overdrafts, this is when the facility was first entered into which could be a long time in the past.

Management overlays and other exceptions to model outputs are applied only if consistent with the objective of identifying significant increases in credit risk.

- Forward-looking information

Credit losses are expected cash shortfalls from what is contractually due over the expected life of the financial instrument, discounted at the original effective interest rate. Expected credit losses are the unbiased probability-weighted credit losses determined by evaluating a range of possible outcomes and considering future economic conditions. When there is a non-linear relationship between forward looking economic scenarios and their associated credit losses, five scenarios are modelled to ensure an unbiased representative sample of the complete distribution when determining the expected loss. Stress testing methodologies are leveraged within forecasting economic scenarios for IFRS 9 purposes.

- Definition of default, credit impaired assets, write-offs and interest income recognition

The definition of default for the purpose of determining expected credit losses has been aligned to the Regulatory Capital CRR Article 178 definition of default, which considers indicators that the debtor is unlikely to pay, includes exposures in forbearance and is no later than when the exposure is more than 90 days past due or 180 days past due in the case of UK mortgages. When exposures are identified as credit impaired or purchased or originated as such, IFRS 9 requires separate disclosure and interest income is required to be calculated on the carrying value net of the impairment allowance.

Credit impaired is when the exposure has defaulted which is also anticipated to align to when an exposure is identified as individually impaired under the incurred loss model under IAS 39. Write-off polices have not changed from IAS 39.

- Expected life

Lifetime expected credit losses must be measured over the expected life. This is restricted to the maximum contractual life and takes into account expected prepayment, extension, call and similar options. The exceptions are certain revolver financial instruments, such as credit cards and bank overdrafts, that include both a drawn and an undrawn component where the entity's contractual ability to demand repayment and cancel the undrawn commitment does not limit the entity's exposure to credit losses to the contractual notice period. The expected life for these revolver facilities is their behavioural life. Where data is insufficient or analysis inconclusive, an additional 'maturity factor' may be incorporated to reflect the full estimated life of the exposures, based upon experienced judgement and/or peer analysis. Potential future modifications of contracts are not taken into account when determining the expected life or exposure at default until they occur.

- Discounting

Expected credit losses are discounted at the effective interest rate (EIR) at initial recognition or an approximation thereof and consistent with income recognition. For loan commitments, the EIR is that rate that is expected to apply when the loan is drawn down and a financial asset is recognised. Issued financial guarantee contracts are discounted at the risk free rate. Lease receivables are discounted at the rate implicit in the lease as prescribed in IAS 17. For variable/floating rate financial assets, the spot rate at the reporting date is used and projections of changes in the variable rate over the expected life are not made to estimate future interest cash flows or for discounting.

- Modelling techniques

Expected credit losses are calculated by multiplying three main components, being the probability of default (PD), loss given default (LGD) and the exposure at default (EAD), discounted at the original effective interest rate. The regulatory Basel Committee of Banking Supervisors (BCBS) ECL calculations are leveraged for IFRS 9 modelling but adjusted for key differences which include:

- BCBS requires 12 month through the economic cycle losses whereas IFRS 9 requires 12 months or lifetime point-in-time losses based on conditions at the reporting date and multiple forecasts of the future economic conditions over the expected lives; and
- IFRS 9 models do not include certain conservative BCBS model floors and downturn assessments and require discounting to the reporting date at the original effective interest rate rather than using the cost of capital to the date of default.

Management adjustments are made to modelled output to account for situations where known or expected risk factors and information have not been considered in the modelling process, for example forecast economic scenarios for uncertain political events.

ECL is measured at the individual financial instrument level, however a collective approach where financial instruments with similar risk characteristics are grouped together, with apportionment to individual financial instruments, is used where effects can only be seen at a collective level for example for forward looking information.

For the IFRS 9 impairment assessment, Barclays Risk Models are used to determine the PD, LGD and EAD. For stage 2 and 3, Barclays applies lifetime PDs but uses 12 month PDs for stage 1. The ECL drivers of PD, EAD and LGD are modelled at an account level which considers vintage, among other credit factors. Also, the assessment of significant increase in credit risk is based on the initial lifetime PD curve, which accounts for the different credit risk underwritten over time.

### (ii) Forbearance

Both performing and non-performing forbearance assets are classified as stage 3 except where it is established that the concession granted has not resulted in diminished financial obligation and that no other regulatory definitions of default criteria has been triggered, in which case the asset is classified as stage 2. The minimum probationary period for non-performing forbearance is 12 months and for performing forbearance, 24 months. Hence, a minimum of 36 months is required for non-performing forbearance to move out of a forborne state.

### (iii) Classification and measurement

IFRS 9 requires financial assets to be classified on the basis of two criteria:

1) the business model within which financial assets are managed, and
2) their contractual cash flow characteristics (whether the cash flows represent 'solely payments of principal and interest').

Financial assets will be measured at amortised cost if they are held within a business model whose objective is to hold financial assets in order to collect contractual cash flows, and their contractual cash flows represent solely payments of principal and interest.

Financial assets will be measured at fair value through other comprehensive income if they are held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets, and their contractual cash flows represent solely payments of principal and interest.

Business models are determined on initial application and this may differ from the model before 1 January 2018 for certain portfolios. Barclays assesses the business model at a portfolio level. Information that is considered in determining the business model includes (i) policies and objectives for the relevant portfolio, (ii) how the performance and risks of the portfolio are managed, evaluated and reported to management, and (iii) the frequency, volume and timing of sales in prior periods, sales expectation for future periods, and the reasons for such sales. Financial assets managed on a fair value basis and those that are held for trading are held at fair value through profit and loss.

In assessing whether contractual cash flows are solely payments of principal and interest, terms that could change the contractual cash flows so that it would not meet the condition for solely payments of principal and interest are considered, including: (i) contingent and leverage features, (ii) non-recourse arrangements and (iii) features that could modify the time value of money.

Other financial assets are measured at fair value through profit and loss. There is an option to make an irrevocable election for non-traded equity investments to be measured at fair value through other comprehensive income, in which case dividends are recognised in profit or loss, but gains or losses are not reclassified to profit or loss upon derecognition, and impairment is not recognised in the income statement.

On 12 October 2017, the IASB published an amendment to IFRS 9, relating to prepayment features with negative compensation; this amendment is effective from 1 January 2019 with early application permitted. Barclays expects the EU to endorse the amendment by 31 December 2018, and will early adopt the amendment as soon as it has been endorsed. This amendment allows financial assets with such features to be measured at amortised cost or fair value through other comprehensive income provided the SPPI (solely payments of principal and interest) criteria in IFRS 9 are otherwise met. In addition the amendment to IFRS 9 clarifies that a financial asset passes the SPPI criterion regardless of the event or circumstance that cause the early termination of the contract, and irrespective of which party pays or receives reasonable compensation for the early termination of the contract. Such prepayment features are present in some fixed rate corporate and investment bank loans, and are considered to meet the criteria for amortised cost under IFRS 9. Prepayment features are consistent with the solely payments of principal and interest criteria if the prepayment feature substantially represents unpaid amounts of principal and interest and reasonable compensation for early termination of the contract.

While there are some classification changes, these are not significant from a Group perspective.

### (iv) Hedge accounting

IFRS 9 contains revised requirements on hedge accounting, adoption of which is optional. In addition certain aspects of IAS 39, being the portfolio fair value hedge for interest rate risk, continues to be available for entities (while applying IFRS 9 to the remainder of the entity's hedge accounting relationships) until the IASB completes its accounting for dynamic risk management project.

Based on analysis performed, Barclays has continued to apply the relevant IAS 39 hedge accounting requirements, although it will implement the amended IFRS 7 hedge accounting disclosure requirements.

### (v) Own credit

From 1 January 2017, Barclays had applied the option in IFRS 9 to recognise changes in own credit for financial liabilities designated at fair value through profit and loss under the fair value option in other comprehensive income. This has no effect on net assets, and any changes due to own credit in prior periods have not been restated. Any realised and unrealised amounts recognised in other comprehensive income will not be reclassified to the income statement in future periods.

## Measurement uncertainty

The measurement of expected credit loss involves increased complexity and judgement, including estimation of probabilities of default, loss given default, a range of unbiased future economic scenarios, estimation of expected lives, and estimation of exposures at default and assessing significant increases in credit risk. Impairment charges will tend to be more volatile, will be recognised earlier and the amounts will be higher. Unsecured products with longer expected lives, such as revolving credit cards, are the most impacted.

The ECL assessment is undertaken with forward looking information that captures baseline, adverse and favourable scenarios, all of which are probability weighted. The Scenario Expansion Team utilises the most recent external consensus forecast as the baseline scenario. In addition, two adverse and two favourable scenarios are derived, with associated probability weightings. The adverse scenarios are calibrated to a similar severity to internal stress tests, whilst also incorporating IFRS 9 specific sensitivities and non-linearity. The most adverse scenarios are benchmarked to the Bank of England's annual cyclical scenarios and to the most severe scenarios from Moody's inventory, but are not designed to be the same. The favourable scenarios are calibrated to be symmetric to the adverse scenarios, subject to a ceiling calibrated to relevant recent favourable benchmark scenarios. The scenarios include six core variables, (UK/US: GDP, unemployment and House Price Index), and expanded variables using statistical models based on historical correlations. The probability weights of the scenarios are estimated such that the baseline (reflecting current consensus outlook) has the highest weight and the weights of adverse and favourable scenarios depend on the difference versus the baseline; the further from the baseline, the smaller the weight. A single set of five scenarios is used across all portfolios and all five weights are normalised to equate to 100%. The impacts across the portfolios are different because of the sensitivities of each of the portfolios to specific macro-economic variables. For example, mortgages are highly sensitive to house prices and base rates, credit cards and unsecured consumer loans are highly sensitive to unemployment.

The table below provides a summary of the average, minimum and maximum values of the six key economic variables, for the baseline scenario between 2018 to 2022.

| Baseline economic variables | Average (%) | Minimum (%) | Maximum (%) |
|---|---|---|---|
| UK GDP | 1.8 | 1.5 | 2.0 |
| UK Unemployment | 4.6 | 4.6 | 4.6 |
| UK HPI | 2.8 | 2.0 | 3.2 |
| US GDP | 2.1 | 2.0 | 2.2 |
| US Unemployment | 4.1 | 4.1 | 4.2 |
| US HPI | 3.4 | 3.2 | 4.1 |

GDP and HPI are annualised growth rates. Unemployment rate is a simple average.

## Project governance and credit risk management

Barclays has a jointly accountable Risk and Finance implementation and governance programme with representation from all impacted departments. The current impairment committee structures were initiated and tested from H1 2017, providing oversight for both IAS 39 and IFRS 9 impairment results.

The impairment reporting process commences with the production of economic scenarios. The Senior Scenario Review Committee (SSRC), comprised of senior management within Risk, reviews and approves the scenario narratives, the core set of macroeconomic variables, probability weightings, and any scenario specific management overlays which are used in all ECL models. The SSRC attests that the scenarios adequately account for the non-linearity and asymmetry of the loss distribution.

The Group Impairment Committee, formed of members from both Finance and Risk and attended by both the Group Finance Director and the Chief Risk Officer, is responsible for overseeing impairment policy and practice across Barclays Group and will approve impairment results.

Reported results and key messages are communicated to the Board Audit Committee, which has an oversight role and provides challenge of key assumptions, including the basis of the scenarios adopted.

# Comparison of concepts and methodology from IAS 39 to IFRS 9

IFRS 9 methodologies do not in general build directly on existing IAS 39 methodology or concepts. The following section explains some of the key concepts under IAS 39 and broad comparison to the approach under IFRS 9.

### Individually assessed impairment

Under IAS 39, impairment allowances were measured individually for assets that were individually significant and for where there was evidence that an account was exhibiting significant financial difficulties, and where any further deterioration was likely to lead to failure. Two key inputs to the cash flow calculation were the valuation of all security and collateral, as well as the timing of all asset realisations, after allowing for all attendant costs. This method was applied mainly in the wholesale portfolios.

Under IFRS 9, whilst individual assessment remains for individually significant assets, the assessment is of expected rather than incurred loss. The expected loss calculation is a present value calculation of the credit losses expected from default events that may occur during a specified time period. The required time period being determined by risk at the reporting date relative to that at origination. Collateral valuation and timing and costs of recovery will form a part of the assessment.

### Collectively assessed impairment

For collective assessment under IAS 39, the principal trigger point for impairment was the missing of a contractual payment, which was the policy adopted across all credit cards, unsecured loans, mortgages and most other retail lending. The calculation methodology relied on the historical experience of pools of similar assets; hence the impairment allowance was collective. The impairment calculation was typically based on a roll-rate approach, where the percentage of assets that move from the initial delinquency to default was derived from statistical probabilities based on historical experience. Recovery amounts were calculated using a weighted average for the relevant portfolio. This method applied mainly to the retail portfolios and was consistent with the Group's policy of raising an allowance as soon as impairment was identified. Unidentified impairment was also included in collective impairment.

ECL assessments under IFRS 9 are based upon forward looking modelled PD, EAD and LGD parameters which are run at account level (at minimum for material portfolios), and applied across all assets from the point of origination/booking. Where account level modelling is not feasible (e.g. due to data constraints) or justifiable (immaterial/run down portfolios), segment level models or pooled assessments are applied. In such cases, segments are defined on the basis of similar risk characteristics. Where segment/pooled assessments are not feasible, benchmark parameters from relevant peer portfolios are applied in the short term.

### Impairment allowance for unidentified losses

Unidentified impairment allowances under IAS 39 were also raised to cover losses which were judged to be incurred but not yet specifically identified in customer exposures at the balance sheet date, and which, therefore, have not been specifically reported. The incurred but not yet reported calculation was based on the asset's probability of moving from the performing portfolio to being specifically identified as impaired within the given emergence period and then on to default within a specified period, termed as the outcome period. This was calculated on the present value of estimated future cash flows discounted at the financial asset's effective interest rate. The emergence and outcome periods varied across products.

Under IFRS 9, for exposures that have not had a significant increase in credit risk, a 12 month expected credit loss (the portion of lifetime expected credit losses from default events that are expected within 12 months of reporting date) is provided. Hence, IAS 39 captured incurred losses from events that have already happened but not yet displayed in the performance whilst IFRS 9 captures default events in the next 12 months with forward looking information.

### Emergence and 12 month default period

Under IAS 39, Incurred but not reported (IBNR) emergence periods were assessed at portfolio level, based on historic data, to ensure they captured materially all impairment events that have occurred but were not visible at reporting date. Typical emergence periods applied were 3-6 months. This compares to 12 month ECL for all assets under IFRS 9 rather than just the proportion where a loss event has occurred under IAS 39.

### Identifying potential credit risk loans

The Group has previously disclosed potentially and actually impaired loans as Potential Credit Risk Loans (PCRLs). PCRLs comprise two categories of loans: Potential Problem Loans (PPLs) and Credit Risk Loans (CRLs).

PPLs were loans that complied with repayment terms but where serious doubt exists as to the ability of the borrower to continue to comply with such terms in the near future. If the credit quality of a wholesale loan on a watch list deteriorates to the highest category, or a retail loan deteriorates to delinquency cycle 2, consideration was given to include it within the PPL category. Should further evidence of deterioration be observed, a loan may move to the CRL category. Events that would trigger the transfer of a loan from the PPL to the CRL category included a missed payment or a breach of covenant.

CRLs and any associated ECLs are mapped to stages 2 or 3 and PPLs and associated ECLs are included in stage 2 under IFRS 9.

# Glossary of terms

This glossary provides definitions of additional terms arising as a result of IFRS 9 that are not included in Barclays PLC Annual Report 2017. For all other definitions, please refer to the Glossary for Barclays PLC Annual Report 2017.

'90 days past due' Past due 90 days or more comprises loans that are 90 days or more past due with respect to principal or interest. An impairment allowance will be raised against these loans if the expected cash flows discounted at the effective interest rate are less than the carrying value.

'Annualised cumulative weighted average lifetime PD' The probability of default over the remaining life of the asset, expressed as an annual rate, reflecting a range of possible economic scenarios.

'Coverage ratio' This represents the percentage of impairment allowance reserve against the gross exposure.

'Discounting' Discounting is the process of determining the present value of a payment or a stream of payments that is to be received in the future.

'Effective Interest Rate (EIR)' This represents the interest rate on the financial asset after accounting for any fees applicable and compounding effect over time.

'Enhanced Disclosure Task Force (EDTF)' A group, comprising of banks, analysts, investors and auditors, established to drive reporting consistency across peer groups and enhance the disclosures in the annual report and accounts.

'Expected Credit Losses (ECL)' A present value measure of the credit losses expected to result from default events that may occur during a specified period of time. ECLs must reflect the present value of cash shortfalls. ECLs must reflect the unbiased and probability weighted assessment of a range of outcomes. ECLs are a provision held on the balance sheet as a result of the raising of a charge against profit for the expected loss inherent in the lending book.

'Expected lives' This is restricted to the maximum contractual life and takes into account expected prepayment, extension, call and similar options. The exceptions are certain revolver financial instruments, such as credit cards and bank overdrafts, that include both a drawn and an undrawn component where the entity's contractual ability to demand repayment and cancel the undrawn commitment does not limit the entity's exposure to credit losses to the contractual notice period. The expected life for these revolver facilities is their behavioural life. Where data is insufficient or analysis inconclusive, an additional 'maturity factor' may be incorporated to reflect the full estimated life of the exposures, based upon experienced judgement and/or peer analysis. Potential future modifications of contracts are not taken into account when determining the expected life or exposure at default until they occur.

'High Risk Account Management (HRAM)' High Risk is defined as the subset of up-to-date customers who, either through an event or observed behaviour exhibit potential financial difficulty. Where appropriate, these customers are proactively contacted to assess whether assistance is required.

'Identified Impairment (II)' Specific impairment allowances for financial assets, individually estimated.

'Impairment allowance' A provision held on the balance sheet as a result of the raising of a charge against profit for the expected loss inherent in the lending book.

'Initial recognition' Initial recognition is when a financial instrument is recognised for the first time in the statement of financial position.

'International Accounting Standards Board (IASB)' The IASB is the independent standard setting body of the IFRS Foundation. The IASB develops and issues International Financial Reporting Standards (IFRS).

'Lifetime expected credit losses' An assessment of expected losses associated with default events that may occur during the life of an exposure, reflecting the present value of cash shortfalls over the remaining expected life of the asset.

'Lifetime Probability' The likelihood of accounts entering default during the expected remaining life of the asset.

'Significant Increase in Credit Risk (SICR)' Barclays assesses when a significant increase in credit risk has occurred based on quantitative and qualitative assessments. Exposures are considered to have had a significant increase in credit risk as follows:

- The annualised cumulative weighted average lifetime PD increases beyond the agreed threshold relative to the equivalent at origination. Other measures of PD deterioration can also be used. The relative thresholds are defined as percentage increases and set at a score band and segment level.
- Exposures are determined to be higher credit risk and subject to closer credit risk monitoring.
- Exposures are more than 30 days past due, used as a backstop rather than a primary driver.

'Stage 1' This represents financial instruments where the credit risk of the financial instrument has not increased significantly since initial recognition. Stage 1 financial instruments are required to recognise a 12 month expected credit loss allowance.

'Stage 2' This represents financial instruments where the credit risk of the financial instrument has increased significantly since initial recognition. Stage 2 financial instruments are required to recognise a lifetime expected credit loss allowance.

'Stage3' This represents financial instruments where the financial instrument is considered impaired. Stage 3 financial instruments are required to recognise a lifetime expected credit loss allowance.

'Twelve month expected credit losses' The portion of the lifetime ECL arising if default occurs within 12 months of the reporting date (or shorter period if the expected life is less than 12 months), weighted by the probability of said default occurring.

'Twelve month PD' The likelihood of accounts entering default within 12 months of the reporting date.

'Unidentified Impairment (UI)' Impairment for losses which are judged to be incurred but not yet specifically identified in customer exposures at the balance sheet date, and which, therefore, have not been specifically reported. The incurred but not yet reported calculation is based on the asset's probability of moving from the performing portfolio to being specifically identified as impaired within the given emergence period and then on to default within a specified period, termed as the outcome period. This is calculated on the present value of estimated future cash flows discounted at the financial asset's effective interest rate. The emergence and outcome periods vary across products.

'Watch List 1' Performing: A temporary classification for obligors exhibiting some unsatisfactory features which merit closer review but are not currently indicative of significant deterioration.

'Watch List 2' Performing: Some doubt exists as to the viability of the obligor, but believe the obligor can meet obligations over the short term (next 12 months).

'Watch List 3' Definite concern exists with well-defined weaknesses. If the position deteriorates, obligor failure could occur in the very short term (< 6 months) irrespective of whether collateral is held.

'Watch List 4' Non-performing/ insolvent, regulatory default and high risk of loss.