

'keeping in touch'



Financial Highlights
(adopted IFRS basis)¹

	Half-year to 30 June 2005 £m	Half-year to 30 June 2004 (Restated) ² £m	Full year 2004 (Restated) ² £m
Operating income	251.8	242.3	498.0
Profit/(loss) on ordinary activities before tax	15.0	(1.7)	(115.0)
Retained profit/(loss) for the financial period	10.7	(0.3)	(101.0)
Basic and diluted profit/(loss) per share (pence)	1.3p	–	(11.3p)
Total assets	11,421.4	12,225.5	12,048.1
Share capital, share premium, capital reserve and other reserves	587.7	883.1	882.4
Accumulated losses	(251.3)	(442.9)	(541.2)
Total equity attributable to the equity holders of the parent	336.4	440.2	341.1

¹ Including Continuing and Discontinued operations

² See note 1 on page 06

Chief Executive's review

Introduction

Operating profit in the second quarter was £13 million for the core UK business on the new IFRS basis of reporting leading to a half year profit of £23 million. The overall Group profit before tax, including discontinued activities, was £15 million for the six months ended 30 June 2005.

Egg's UK credit card business has performed well, with balance growth of 5% in the first half compared with 2% for the industry. MasterCard continues to perform well and contribute to the good growth rates seen over the past year since its launch.

As planned, following our tightening of lending criteria, personal loan sales have reduced in the first half from the record levels seen in 2004 and we expect a similar trend for the remainder of the year.

Revenues in the UK in the first half at £251 million were up 5% compared with the same period last year. This reflected good growth in card income offset by less up front income in terms of the commission earned from selling associated insurances on loans due to the tactical reduction in sales.

Costs are falling, reducing by £10 million (8%) when compared with the first half of 2004 and our cost/income ratio has improved to 44% in the first six months this year from 51% for the same period last year. This is in part due to the restructuring exercise completed this quarter which has aligned our cost base to our strategy which is refocused on our core business and the needs of the UK consumer. We intend to launch a number of innovative propositions aimed at helping customers to benefit from managing, using and understanding their money more effectively.

Credit quality remains strong and as expected the impairment charge reduced slightly in the second quarter. Also, as we noted in April, we expect a lower charge in the second half of the year as the benefits from the changes we made to our loans scorecard and in our collections function continue to emerge.

Our exit from non-core businesses continues and we are confident existing provisions are adequate.

Overall the result for the first half was in line with our expectations and we remain confident about the remainder of the year.

Contents

01	Chief Executive's review
05	Financial information
06	Consolidated income statement
07	Consolidated balance sheet
08	Consolidated statement of changes in equity
10	Consolidated cash flow statement
12	Notes to the financial information
21	Independent review report by KPMG Audit plc to Egg plc
22	Average balance sheet (UK business only)
22	Average yields (UK business only)
23	Appendix 1
BC	How to contact us

Summary income statement by quarter (adopted IFRS basis) (unaudited)

	Q2 2005 £m	Q1 2005 £m	Q4 2004 £m	Q3 2004 £m	Q2 2004 £m
UK					
Net interest income	75.3	70.8	73.3	70.4	70.1
Other operating income	51.1	53.8	66.3	48.3	49.9
Egg UK operating income	126.4	124.6	139.6	118.7	120.0
Operational and administrative expenses	(36.9)	(37.1)	(40.7)	(39.2)	(37.7)
Brand and marketing costs	(8.4)	(8.1)	(12.4)	(9.0)	(10.6)
Development costs	(2.8)	(3.7)	(6.2)	(5.2)	(4.7)
Depreciation and amortisation	(6.9)	(6.9)	(7.1)	(4.3)	(5.6)
Impairment losses on loans and advances to customers	(58.3)	(58.9)	(52.8)	(47.1)	(41.3)
Egg UK operating profit	13.1	9.9	20.4	13.9	20.1
France					
Net interest income/(expense)	0.1	(0.3)	0.8	1.8	2.1
Other operating (expense)/income	(0.4)	1.3	(7.0)	0.9	(0.1)
Egg France operating (expense)/income	(0.3)	1.0	(6.2)	2.7	2.0
Operational and administrative expenses	(3.5)	(9.0)	(10.1)	(8.5)	(9.9)
Brand and marketing costs	-	-	-	-	(0.9)
Development costs	-	-	-	-	(0.2)
Depreciation and amortisation	1.0	-	(0.4)	(3.1)	(1.7)
Impairment losses on loans and advances to customers	-	(0.3)	(5.8)	(3.9)	(5.5)
Utilisation of exit cost provision	3.0	9.6	15.8	10.1	-
Egg France operating profit/(loss)	0.2	1.3	(6.7)	(2.7)	(16.2)
Subsidiaries/associates/JV's	0.3	(3.4)	(17.6)	(1.0)	(0.6)
Transaction costs	-	-	(2.7)	(1.1)	(1.3)
Provision for France exit costs	-	3.5	-	(112.8)	-
Restructuring costs	(3.6)	(6.3)	(3.0)	-	0.2
Group profit/(loss) before tax (including discontinued activities)	10.0	5.0	(9.6)	(103.7)	2.2

Note: All comparatives for 2004 have been restated to adopted IFRS basis (excluding the impact of IAS 32 and IAS 39, which the Group has elected to adopt only from 1 January 2005).

Financial Review**Egg UK****Revenues**

Net interest income in Q2 2005 was £75.3 million (Q1 2005: £70.8 million). The increase has resulted from the growth in standard rate balances on cards this quarter. Moving forward we expect stronger growth in net interest income in the second half following our decision to re-price the card book from August.

Non-interest income in Q2 2005 was slightly reduced at £51.1 million (Q1 2005: £53.8 million). Commission income earned from sales of associated insurances on our loan book continued to decline this quarter as penetration rates fell again to 48% (Q1 2005: 51%). This was offset by £2.2 million of unrealised gains on derivatives arising from the adoption of fair value accounting under IAS 39 (Q1 2005: £0.6 million unrealised loss) which is purely a timing difference given no gain or loss is expected over the life of the derivatives as they are economic hedges and will not be traded.

Costs

Operational and administrative costs at £36.9 million for the quarter (Q1 2005: £37.1 million) continued their recent downward trend reflecting again some immediate benefit from the restructuring completed this quarter, which has been targeted principally at the overhead base. We are on track to deliver at least the £12 million of annual savings initially envisaged from the restructuring.

Brand and marketing costs were £8.4 million (Q1 2005: £8.1 million). The marketing mix this quarter was different with less TV advertising on Visa Card which resulted in lower acquisition at 94,000 new accounts (Q1 2005: 139,000). Additional campaigns were run to increase cross sales of personal loans which were up 5% over the first quarter.

Development costs were £2.8 million for the quarter, a decrease from Q1 2005 (£3.7 million). This reduction primarily reflects the fact £0.4 million of internal software development costs which had been expensed in Q1 were identified as eligible for capitalisation this quarter.

Depreciation and amortisation at £6.9 million was unchanged on the first quarter.

This strong overall cost performance has contributed to a further small improvement in the cost/income ratio this quarter to 44% (Q1 2005: 45%). Moving forward we expect costs to rise in H2 compared to H1 reflecting the fact that the annual pay rise is effective from July each year and we continue to make investments in our credit function to deliver the reducing bad debt charge. However we expect income growth to enable us to drive the cost/income ratio down further over time.

Impairment for losses on loans and advances to customers

The Q2 charge for impairment of £58.3 million was in line with our expectations and reduced slightly on the first quarter (£58.9 million). The impairment charge as a percentage of 12 month lagged assets in the overall unsecured portfolio remained consistent at 4.0% (Q1 2005: 3.9%). Moving forward we expect the impact of our decision to tighten lending criteria, allied to the maturing of the personal loan book, should see both the absolute charge and the charge as a percentage of lagged assets start to reduce over the second half of the year.

At the period end, impairment provisions on the balance sheet represented 3.5% of assets compared to 3.2% at 31 December 2004 and 3.1% at 30 June 2004. The increase reflects the greater level of maturity in the portfolio and the higher percentage of unsecured assets within it.

Egg France and provision for exit costs

As noted in April we now expect the final costs of exiting our French business to be lower than the £113 million (€170 million) provision made in July 2004 and we therefore released £3.5 million (€5 million) of the provision in the first quarter. The only net movement in the French profit and loss account in Q2 was a small exchange gain of £0.2 million.

Subsidiaries/associates/JV's

There was no net profit or loss this quarter. The £3.1 million net loss year to date primarily reflects the exit costs provision in respect of Funds Direct raised in Q1 2005.

Restructuring costs

We completed our review of our total cost base, and in particular the overhead functions and a final £3.6 million of costs were incurred or accrued in respect of people who have exited the business taking the total to £9.9 million. The estimated annual savings resulting from this reorganisation are £12 million.

International Financial Reporting Standards

The six month results to June 2004 were originally prepared under UK GAAP. These results have been restated for the adoption of International Financial Reporting Standards excluding IAS 32 and IAS 39. The basis of preparation of the 2005 Interim Financial Statements is shown in full on page 05, supported by our adopted accounting policies as shown in Note 1. The adjustments made to the 30 June 2004 UK GAAP Income Statement, Balance Sheet and Cash Flow Statement to bring them in line with IFRS (excluding IAS 32 and IAS 39) are shown in Appendix 1.

Business Review**Egg UK – Product information**

	30 June 2005 £m	30 June 2004 £m	31 December 2004 £m
Product balances			
Egg Card	3,769	3,091	3,578
Egg personal loans	2,753	2,256	2,618
Total unsecured lending	6,522	5,347	6,196
Egg mortgages	1,128	1,154	1,102
Prudential mortgages	529	684	591
Total secured lending	1,657	1,838	1,693
Egg savings	6,222	6,402	6,215
Prudential savings	123	144	121
Total retail liabilities	6,345	6,546	6,336

Unsecured lending

Credit card balance growth was a £191 million (5.3%) net increase in the first half, a strong result when compared with the same period last year when balances increased by just £76 million. It is also encouraging against the background of industry balances increasing by just 2.2%. Within the portfolio we have seen strong acquisition in the first quarter followed by an outflow of incentive balances in the second quarter reflecting the fact that a number of six month and eight month incentive offers from last year came to an end this period. Interest bearing balance growth has been encouraging in the first half and this is reflected in the improving card yields up to 9.9% from 9.6% at 31 December 2004.

The Visa Card is predominantly a borrowing card with high levels of balance transfers driving the growth. This has resulted in above industry average balance per card and revolving percentages. We intend to further boost sales of our MasterCard in the second half with a new improved proposition which will aim to focus on spend, an area where Egg currently has below industry average penetration.

Personal loan disbursements were £895 million for H1 leading to net balance growth of £135 million. This is a solid performance, but as expected, is a reduction on the record loan volumes achieved last year (H1 2004: Disbursements – £1,137 million and Net balance growth – £484 million) and reflects our decision, indicated in our preliminary results announcement to tighten lending criteria.

Savings

H1 2005 saw a net inflow on Egg deposits of £7 million (H1 2004: £238 million inflow). Retail liabilities are primarily an element within Egg's overall funding strategy rather than an acquisition product. Given our strong liquidity position in the second quarter we withdrew our bonus account offering and have seen outflows in line with previous experience. We expect the margin on our savings business to continue to improve in H2.

Other products

The Prudential branded mortgage book continues in run-off and the Egg book grew by just 2% in the first half reflecting the fact that we are not currently promoting this product.

The Egg Insure business acquired 90,000 new policies in H1 putting it on track for a record year of acquisition.

Egg Money Manager sales have also been on the increase with 69,000 new registered users in the first half of 2005 compared to 36,000 in the same period last year.

Capital

Capital ratios for Egg Banking plc at 30 June 2005 were 9.1% (tier 1) and 15.0% (total) (30 June 2004: 9.6% (tier 1) and 16.8% (total)). On a consolidated basis the total capital ratio was 13.3% (30 June 2004: 16.5%). The reduction in capital ratios predominantly reflects the provision for exit costs in France and impairment of Funds Direct.

As announced in February we have undertaken a restructuring of share capital and reserves with a view to eliminating the Company's profit and loss deficit against other reserves including the share premium account. This restructuring will allow the payment of dividends as and when sufficient distributable reserves have been generated and the Board considers it to be in the best interests of the Company.

This process required the approval of a Special Resolution at the Annual General Meeting and, following that a series of approvals by the High Court. As at 30 June 2005 only one remaining approval of the Court was outstanding and this was received on 6 July 2005 after which the accumulated losses of Egg plc have been reduced to £72 million from £541 million at 31 December 2004.



Paul Gratton
Chief Executive
27 July 2005

Financial information

Financial results prepared in accordance with International Financial Reporting Standards adopted for use in the European Union for the six months ended 30 June 2005.

Basis of preparation

EU law (IAS Regulation EC 1606/2002) requires that the next annual consolidated financial statements of the Group for the year ended 31 December 2005 be prepared in accordance with IFRS adopted by the EU (adopted IFRS).

The financial information has been prepared on the basis of recognition and measurement requirements of IFRS in issue that are either endorsed by the EU and effective, or are expected to be endorsed and effective at 31 December 2005, the Group's first annual reporting date at which they are required to use adopted IFRS. Based on these adopted and unadopted IFRSs, the directors have made assumptions about the accounting policies to be applied, as detailed in the description of accounting policies set out below.

In particular the directors have assumed that the amendment to IAS 19 "Employee Benefits – Actuarial Gains and Losses" issued by the IASB will be fully adopted by the EU and therefore available for use in the annual IFRS Financial Statements for the year ended 31 December 2005.

In respect of financial instruments, the Group's policy has been to adopt IAS 32 "Financial Instruments: Disclosure and Presentation" and IAS 39 "Financial Instruments: Recognition and Measurement" from 1 January 2005, except as restricted by the European Commissions Accounting Regulatory Committee. Comparatives for 2004 have not been restated to reflect the requirements of IAS 32 and IAS 39 and, as permitted by IFRS 1, are accounted for under UK GAAP in accordance with the accounting policies set out in the annual financial statements for the year ended 31 December 2004.

In addition, the adopted IFRSs that will be effective or available for voluntary early adoption in the annual financial statements for the year ended 31 December 2005 are still subject to change and to the issue of additional interpretations and therefore cannot be determined with certainty. Accordingly, the accounting policies for the annual period that are relevant to this interim financial information will be determined only when the annual financial statements are prepared for the year ended 31 December 2005.

The comparative figures for the financial year ended 31 December 2004 are not the Group's statutory accounts for that financial year. Those accounts, which were prepared under UK GAAP in accordance with the Companies Act 1985, have been reported on by the Company's auditors and delivered to the registrar of companies. The report of the auditors was unqualified and did not contain statements under Section 237(2) or (3) of the Companies Act 1985.

Transitional arrangements

On transition to IFRS, an entity is generally required to apply IFRS retrospectively, except where an exemption is available under IFRS 1 "First-time Adoption of International Financial Reporting Standards". The following is a summary of the key elections from IFRS 1 that were made by the Group:

- The Group has elected to adopt the IFRS 1 exemption in relation to business combinations and will only apply IFRS 3 "Business Combinations" prospectively from 1 January 2004. As a result, the balance of goodwill under UK GAAP at 31 December 2003 will be deemed the cost of goodwill at 1 January 2004.
- The Group has elected to adopt the IFRS 1 option to reset foreign currency cumulative translation reserves to zero on transition to IFRS.

Furthermore, the Group has adopted the exemption in IFRS 1 to not prepare comparative information in accordance with IAS 32 "Financial Instruments: Disclosure and Presentation" and IAS 39 "Financial Instruments: Recognition and Measurement". These standards will therefore only apply from 1 January 2005 and in the comparative figures for the year ended 31 December 2004, financial instruments will continue to be accounted for on a UK GAAP basis. The Group has also elected to adopt IFRS 5 "Non-current Assets Held for Sale and Discontinued Operations" from 1 January 2005.

Consolidated income statement

(unaudited)

	Notes	Six months ended 30 June 2005 £m	Three months ended 30 June 2005 £m	Six months ended 30 June 2004 (Restated) ¹ £m	Three months ended 30 June 2004 (Restated) ¹ £m	Year ended 31 December 2004 (Restated) ¹ £m
Continuing operations:						
Interest income		494.4	242.2	433.1	221.3	902.8
Interest expense		(348.3)	(166.9)	(288.6)	(150.8)	(615.4)
Net interest income		146.1	75.3	144.5	70.5	287.4
Fee and commission income		104.0	49.6	105.8	53.7	220.7
Fee and commission expense		(9.4)	(5.2)	(14.8)	(4.9)	(25.2)
Net fee and commission income		94.6	44.4	91.0	48.8	195.5
Net trading income		9.3	6.4	–	–	–
Other operating income		1.0	0.3	3.4	0.9	14.7
Operating income		251.0	126.4	238.9	120.2	497.6
Administrative expenses						
– personnel expenses		(46.4)	(22.1)	(44.2)	(21.8)	(92.7)
– depreciation and amortisation		(13.8)	(6.9)	(11.9)	(6.0)	(22.2)
– other administrative expenses		(60.6)	(29.7)	(67.6)	(31.9)	(139.3)
		(120.8)	(58.7)	(123.7)	(59.7)	(254.2)
Impairment losses on loans and advances to customers	2	(17.2)	(58.3)	(82.4)	(41.4)	(182.4)
Operating profit		13.0	9.4	32.8	19.1	61.0
Share of operating (loss)/profit of joint venture		(0.1)	–	0.3	–	0.3
Share of associate losses		–	–	(0.2)	(0.1)	(0.4)
Profit on continuing ordinary activities before tax		12.9	9.4	32.9	19.0	60.9
Tax charge on profit on continuing ordinary activities	3	(3.7)	(3.4)	(11.5)	(5.8)	(24.7)
Profit on continuing ordinary activities after tax		9.2	6.0	21.4	13.2	36.2
Discontinued operations:						
Profit/(loss) on discontinued ordinary activities after tax	4	1.5	(3.5)	(21.7)	(8.8)	(137.2)
Retained profit/(loss) for the period		10.7	2.5	(0.3)	4.4	(101.0)
Attributable to:						
Equity holders of the parent		11.4	2.4	(0.1)	4.7	(99.7)
Minority interests		(0.7)	0.1	(0.2)	(0.3)	(1.3)

		Pence per share	Pence per share	Pence per share	Pence per share	Pence per share
Consolidated earnings/(loss) per share						
Basic	5	1.3	0.2	–	0.5	(11.3)
Diluted	5	1.3	0.2	–	0.5	(11.3)
Continuing earnings per share						
Basic	5	1.1	0.7	2.6	1.5	4.6
Diluted	5	1.1	0.7	2.6	1.5	4.6

¹ The comparative results for the six months ended 30 June 2004, the three months ended 30 June 2004 and the year ended 31 December 2004 have been restated to reflect the adoption of International Financial Reporting Standards, as explained on page 05. A reconciliation of the income statement, balance sheet and cash flow statement for the period ended 30 June 2004 with UK GAAP, in accordance with which the comparatives were previously prepared, is shown in Appendix 1. A reconciliation of the income statement, balance sheet and cash flow statement for the year ended 31 December 2004 was shown in Appendix 1 of our Press Release on the results for the three months ended 31 March 2005 issued on 27 April 2005.

Consolidated balance sheet

(unaudited)

	Notes	30 June 2005 £m	30 June 2004 (Restated)* £m	31 December 2004 (Restated)* £m
Assets				
Cash and balances with central banks		7.3	13.1	14.0
Loans and advances to banks		747.2	294.7	615.9
Securities purchased under agreement to resell		251.2	–	319.4
Investment securities		2,264.6	4,145.8	3,119.7
Derivative financial instruments		71.4	12.8	16.0
Loans and advances to customers		7,915.6	7,105.5	7,642.0
Prepayments and accrued income		9.1	77.5	58.3
Investments in joint venture and associate		10.1	6.5	6.3
Property, plant and equipment		46.9	53.9	48.0
Intangible assets		44.1	53.5	49.0
Deferred tax		35.8	25.6	28.9
Other assets		18.1	436.6	130.6
Total assets		11,421.4	12,225.5	12,048.1
Liabilities				
Deposits by banks		2,483.7	2,016.0	2,352.0
Securities sold under agreements to repurchase		–	816.8	130.5
Customer accounts		6,451.2	6,698.6	6,607.4
Investment securities in issue		1,404.6	1,339.2	1,806.5
Derivative financial instruments		78.7	13.0	17.5
Other liabilities		119.6	279.9	110.5
Accruals and deferred income		78.2	170.0	215.0
Provisions for liabilities and charges		1.9	–	16.8
Subordinated liabilities				
– Dated loan capital		468.0	450.8	450.8
Total liabilities		11,085.9	11,784.3	11,707.0
Shareholders' equity				
Called up share capital	6	412.2	412.2	412.2
Share premium account	6	–	110.9	111.0
Capital reserve	6	179.1	359.7	359.7
Other reserves	6	(3.6)	0.3	(0.5)
Accumulated losses	6	(251.3)	(442.9)	(541.2)
Total equity attributable to the equity holders of the parent		336.4	440.2	341.2
Minority interests (equity)		(0.9)	1.0	(0.1)
Total equity		335.5	441.2	341.1
Total equity and liabilities		11,421.4	12,225.5	12,048.1

* See note 1 on page 06.

Consolidated statement of changes in equity

(unaudited)

	Attributable to equity holders of the Group						Total £m
	Called up share capital £m	Share premium account £m	Capital reserve £m	Other reserves £m	Accumulated losses £m	Minority interest £m	
Changes in equity for the six months ended 30 June 2004:							
Balance at 1 January 2004 as previously reported under UK GAAP	410.3	107.5	359.7	–	(445.1)	1.2	433.6
Changes upon transition to IFRS	–	–	–	–	0.5 ¹	–	0.5
Restated balance under IFRS	410.3	107.5	359.7	–	(444.6)	1.2	434.1
Exchange differences on foreign currency translations	–	–	–	0.3	–	–	0.3
Net gain recognised directly in equity	–	–	–	0.3	–	–	0.3
Loss for the period	–	–	–	–	(0.1)	(0.2)	(0.3)
Total recognised income and expense for the period	–	–	–	0.3	(0.1)	(0.2)	–
Increase in share capital	1.9	–	–	–	–	–	1.9
Increase in share premium	–	3.4	–	–	–	–	3.4
Share-based payment adjustment to reserves	–	–	–	–	0.9	–	0.9
Awards under incentive schemes	–	–	–	–	0.9	–	0.9
Balance at 30 June 2004	412.2	110.9	359.7	0.3	(442.9)	1.0	441.2
Changes in equity for the year ended 31 December 2004:							
Balance at 1 January 2004 as restated under IFRS	410.3	107.5	359.7	–	(444.6)	1.2	434.1
Exchange differences on foreign currency translations	–	–	–	(0.5)	–	–	(0.5)
Net loss recognised directly in equity	–	–	–	(0.5)	–	–	(0.5)
Loss for the year	–	–	–	–	(99.7)	(1.3)	(101.0)
Total recognised expense for the year	–	–	–	(0.5)	(99.7)	(1.3)	(101.5)
Increase in share capital	1.9	–	–	–	–	–	1.9
Increase in share premium	–	3.5	–	–	–	–	3.5
Share-based payment adjustment to reserves	–	–	–	–	2.3	–	2.3
Awards under incentive schemes	–	–	–	–	0.8	–	0.8
Balance at 31 December 2004	412.2	111.0	359.7	(0.5)	(541.2)	(0.1)	341.1

¹ The adjustment relates to deferred tax on share-based payments.

	Attributable to equity holders of the Group						Total £m
	Called up share capital £m	Share premium account £m	Capital reserve £m	Other reserves £m	Accumulated losses £m	Minority interest £m	
Changes in equity for the six months ended 30 June 2005:							
Balance at 31 December 2004	412.2	111.0	359.7	(0.5)	(541.2)	(0.1)	341.1
Changes in accounting policy (adoption of IAS 32 and IAS 39)	–	–	–	(0.9)	(14.4)	–	(15.3)
Restated balance	412.2	111.0	359.7	(1.4)	(555.6)	(0.1)	325.8
Available-for-sale investments:							
Valuation gains taken to equity	–	–	–	4.6	–	–	4.6
Cash flow hedges:							
Losses taken to equity	–	–	–	(8.3)	–	–	(8.3)
Exchange differences on foreign currency translations	–	–	–	1.5	–	–	1.5
Net loss recognised directly in equity	–	–	–	(2.2)	–	–	(2.2)
Profit/(loss) for the period	–	–	–	–	10.7	(0.8)	9.9
Total recognised income and expense for the period	–	–	–	(2.2)	10.7	(0.8)	7.7
Adjustments to share premium and capital reserve due to capital reconstruction	–	(111.0)	(180.6)	–	291.6	–	–
Share-based payment adjustment to reserves	–	–	–	–	2.0	–	2.0
Balance at 30 June 2005	412.2	–	179.1	(3.6)	(251.3)	(0.9)	335.5

Consolidated cash flow statement

(unaudited)

	Note	Six months ended 30 June 2005 £m	Six months ended 30 June 2004 (Restated)* £m	Year ended 31 December 2004 (Restated)* £m
Cash flows from operating activities				
Continuing operations:				
Operating profit before taxation		13.0	32.8	61.0
Adjusted for:				
Depreciation, impairment and amortisation		13.8	20.9	28.4
Impairment losses on loans and advances to customers		34.3	30.4	70.1
Gain on sale of investment securities		-	(1.9)	(7.5)
Share schemes adjustment in reserves		2.0	-	-
Net (increase)/decrease in operating assets:				
Loans and advances to banks		24.6	38.2	54.8
Derivative financial instruments		(60.9)	-	-
Loans and advances to customers		(283.9)	(399.0)	(1,115.6)
Securities purchased under agreement to resell		68.9	-	(319.4)
Accrued income and prepayments		(0.8)	(1.9)	16.9
Other assets		251.9	(174.1)	99.4
Net increase/(decrease) in operating liabilities:				
Deposits by banks		(50.4)	303.4	772.3
Securities sold under agreements to repurchase		(131.0)	(12.3)	(698.7)
Customer accounts		30.5	256.8	(53.0)
Investment securities in issue		(410.5)	(83.7)	383.6
Accruals and deferred income		(9.2)	13.0	29.6
Derivative financial instruments		28.7	-	-
Other liabilities		(271.7)	(26.9)	(133.6)
Subordinated liabilities		14.8	-	-
Tax refund received/(taxation paid)		5.4	(0.2)	14.1
Net cash outflow from continuing operating activities		(730.5)	(4.5)	(797.6)
Discontinued operations:				
Net cash (outflow)/inflow from discontinued operating activities		(5.9)	19.3	76.2
Total net cash (outflow)/inflow from operating activities		(736.4)	14.8	(721.4)

* See note 1 on page 06.

	Note	Six months ended 30 June 2005 £m	Six months ended 30 June 2004 (Restated)* £m	Year ended 31 December 2004 (Restated)* £m
Cash flows from investing activities				
Continuing operations:				
Purchase of property, plant and equipment		(5.7)	(3.6)	(13.1)
Disposal of property, plant and equipment		1.3	–	–
Purchase of software intangibles		(13.7)	(14.2)	(37.7)
Disposal of software intangibles		7.5	–	–
Purchase of investment securities		(3,986.4)	(2,924.4)	(6,447.5)
Disposal of investment securities		4,858.7	2,904.2	7,435.3
Net cash inflow/(outflow) from continuing investing activities		861.7	(38.0)	937.0
Discontinued operations:				
Net cash (outflow)/inflow from discontinued investing activities		–	(2.2)	90.6
Total net cash inflow/(outflow) from investing activities		861.7	(40.2)	1,027.6
Cash flows from financing activities				
Continuing operations:				
Proceeds from issue of share capital		–	5.3	5.4
Net cash inflow from continuing financing activities		–	5.3	5.4
Discontinued operations:				
Net cash inflow from discontinued financing activities		–	–	–
Total net cash inflow from financing activities		–	5.3	5.4
Increase/(decrease) in cash and cash equivalents in the period		125.3	(20.1)	311.6
Cash and cash equivalents at the beginning of the period	7	627.6	322.9	322.9
Exchange adjustments		1.5	–	(6.9)
Cash and cash equivalents at the end of the period	7	754.4	302.8	627.6

* See note 1 on page 06.

Notes to the financial information

1. Significant accounting policies

The following is a list of the Group's key accounting policies under IFRS. As a result of the Group's decision to adopt the IFRS 1 exemption and not restate comparatives for IAS 32 and IAS 39, certain accounting policies will only apply from 1 January 2005 and not to the 2004 comparatives. These policies have been denoted with an asterisk.

Basis of consolidation

The financial information of the Group incorporates the assets, liabilities, and results of the Company and its subsidiary undertakings (including Special Purpose Entities) to 30 June 2005. Subsidiary undertakings are all entities over which the Group has the power to govern its financial and operating policies so as to obtain benefits from their activities. Inter-company transactions and balances are eliminated upon consolidation.

Associated undertakings and joint ventures

An associate is an entity that is neither a subsidiary nor a joint venture, in which the Group has the power to exercise significant influence regarding the financial and operating policy decisions of the investee. A joint venture is a long-term contractual arrangement between the Group and one or more other parties to undertake an economic activity in which the investing parties exercise joint control.

The Group's share of the profits net of losses of associates and of joint ventures are included in the consolidated income statement on an equity accounting basis and its interest in their net assets is included in investments in the consolidated balance sheet by reference to its equity holdings. When the Group's share of losses exceeds its interest in an associate or joint venture, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued.

Financial instruments*

The Group classifies its financial assets (excluding derivatives) as either loans and receivables or available-for-sale. Other than derivatives, the Group does not classify any of its financial assets as fair value through profit or loss or held-to-maturity.

The Group measures all of its financial liabilities at amortised cost, other than those derivative financial instruments which have been designated as part of a hedging relationship (see below).

a) Loans and receivables and financial liabilities at amortised cost

The Group's loans and advances to customers are classified as loans and receivables. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, and whose recoverability is based solely on the credit risk of the issuer. The Group measures both its loans and receivables and financial liabilities (other than derivatives designated as part of a hedging relationship) at amortised cost, whereby the principal balance is the amount at initial recognition, less any principal repayments and impairment and adjusted for the cumulative amortisation calculated using the effective interest method. The effective interest method is a method whereby estimated future cash payments or receipts are discounted through the expected life of the financial instrument.

b) Available-for-sale financial assets

Available-for-sale financial assets are non-derivative assets, principally but not exclusively investment securities, intended to be held for an indefinite period of time. The Group measures these assets at fair value, with subsequent changes in fair value being recognised in equity except for interest income, impairment losses and foreign exchange gains and losses which are recognised in the income statement. Upon derecognition of the asset, or where there is objective evidence that the investment security is impaired, the cumulative gains and losses recognised in equity are removed from equity and recycled to the income statement.

Impairment losses on loans and advances to customers*

The Group assesses its financial assets or groups of financial assets for objective evidence of impairment at each balance sheet date. An impairment loss is recognised if, and only if, there is a loss event (or events) that has occurred after initial recognition and has a reliably measurable impact on the estimated future cash flows of the financial assets or groups of financial assets.

a) Assets held at amortised cost

Where the financial asset(s) is carried at amortised cost, the Group measures the amount of the impairment loss by comparing the carrying amount of the asset with the present value of its estimated future cash flows.

In estimating the future cash flows, the Group looks at the expected cash flows of the assets and applies historical loss experience of assets with similar credit risks which have been adjusted for conditions in the historical loss experience which no longer exist. The estimated future cash flows are discounted using the financial asset's original or variable effective interest rate and exclude credit losses that have not yet been incurred.

1. Significant accounting policies continued

Impairment losses on loans and advances to customers* continued

a) Assets held at amortised cost continued

The amount of the impairment loss is recognised immediately through the income statement and a corresponding reduction in the value of the financial asset is recognised through the use of an allowance account.

b) Available-for-sale financial assets

For available-for-sale financial assets, the Group assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets are impaired. The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows. The rate used to discount the cash flows is the original effective interest rate on the available-for-sale financial asset(s). The amount of the impairment loss is recognised in the income statement. This includes cumulative gains and losses previously recognised in equity which are now recycled from equity to the income statement.

Derivative financial instruments and hedge accounting*

a) Derivative financial instruments

The Group undertakes transactions in derivative financial instruments, which include currency swaps, interest rate swaps, interest rate caps, forward rate agreements, options, credit derivatives and similar instruments, for non-trading purposes.

The Group's derivative activities are entered into for the purpose of matching or eliminating risk from potential movements in interest rates inherent in the Group's assets, liabilities and positions or for the purpose of reducing credit risk inherent in the Group's balance sheet. All derivative transactions (including foreign exchange and credit) are for economic hedging purposes and so it is therefore decided at the outset which position the derivative will be hedging. Derivatives are reviewed regularly for their effectiveness as hedges and corrective action taken, if appropriate.

Where the derivative has not been designated as a hedge or does not qualify for a hedging relationship in accordance with IAS 39, the derivative is initially measured at fair value, and remeasured at fair value at each balance sheet date, with the changes in the fair value of the derivative being recognised through the income statement. Fair values are based on quoted market prices in active markets, and where these are not available, using valuation techniques such as discounted cash flow models.

Where the fair value of the derivative is positive, the derivative is recognised on balance sheet as a financial asset. Conversely, where its fair value is negative, the derivative is recognised on balance sheet as a financial liability.

b) Cash flow hedges

Where relevant, the Group has elected to designate its derivatives as hedges against the exposure to variability in cash flows of its recognised assets and liabilities, with the effective part of any gain or loss on the derivative financial instrument recognised directly in equity. At inception, the Group formally designates the hedge, documenting the nature of the hedging relationship, the risk management objective and the strategy for undertaking the hedge.

Derivatives designated as hedges are tested for effectiveness on inception of the hedge relationship and on an ongoing basis. The ineffective part of any gain or loss is recognised in the income statement immediately. Any gain or loss arising from changes in the time value of the derivative is excluded from the measurement of the hedge effectiveness and is recognised in the income statement.

Cumulative amounts recognised through equity are taken to the income statement in the period in which the underlying hedged item matures and its associated gain or loss affects the income statement. Cumulative amounts recognised through equity are also taken to the income statement in the period in which the hedging relationship is broken or the hedge becomes ineffective.

The Group has not designated its derivatives as any other type of hedge in accordance with IAS 39.

c) Embedded derivatives

Certain derivatives are embedded within other non-derivative host financial instruments to create a hybrid instrument. Where the economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risk of the host instrument, and where the hybrid instrument is not measured at fair value, the Group separates the embedded derivative from the host instrument and measures it at fair value with the changes in fair value recognised in the income statement. Depending on the classification of the host instrument, the host is then measured in accordance with the relevant requirements of IAS 39.

Offsetting financial instruments*

Financial assets and their related liabilities are presented gross within the relevant headings in the Group balance sheet, unless there is a legally enforceable right to offset and there is an intention to settle net in which case the assets and liabilities are presented net.

1. Significant accounting policies continued

Derecognition of financial assets and liabilities*

The Group's policy is to derecognise financial assets only when the contractual right to the cash flows from the financial asset expire. The Group also derecognises financial assets that it transfers to another party provided the transfer of the asset also transfers the right to receive the cash flows of the financial asset. Where the transfer does not result in the Group transferring the right to receive the cash flows of the financial assets, but it does result in the Group assuming a corresponding obligation to pay the cash flows to another recipient, the financial assets are also accordingly derecognised. Based on an analysis of risks, rewards and where necessary, consideration of control of the assets, such assets would either be derecognised or retained.

The Group derecognises financial liabilities only when the obligation specified in the contract is discharged, cancelled or has expired.

Investment securities*

On initial recognition, debt issued is measured at its fair value net of transaction costs directly attributable to the debt issued, in accordance with IAS 39. Subsequent measurement is at amortised cost using the effective interest rate method to amortise incremental attributable issue and transaction costs over the life of the instrument.

Interest income and expense recognition*

Interest income and interest expense on loans and receivables and liabilities held at amortised cost are recognised on an effective yield basis, inclusive of transactions costs and fees, and discounts and premiums where appropriate. As previously described, the effective interest method is a method whereby estimated future cash payments or receipts are discounted over the expected life of the financial instrument.

Share-based payments

Share-based payments are accounted for on a fair value basis. The Group measures the fair values of the Save-As-You-Earn schemes using the Black-Scholes model and the fair value of all other share-based payment schemes including the Restricted Share Plans (RSPs) using a Present Economic Value (binomial) model. The fair value is then recognised in the income statement over the relevant vesting period and adjusted for lapses, with the number of shares expected to lapse estimated at each balance sheet prior to the vesting date, with the corresponding increase recognised in equity. The only exception is where the share-based payment has vesting outcomes attached to market based performance conditions such as in the case of some of the RSPs. Under these circumstances, additional modelling is required to take into account these market based performance conditions which effectively estimate the number of shares expected to vest. No subsequent adjustment is then made to the fair value charge for shares that do not vest in the event that these performance conditions are not met.

In accordance with the transitional provisions of IFRS 2 "Share-based Payments", the Group has only applied the requirements of the standard to share-based payments granted after 7 November 2002, and had not yet vested as at 1 January 2004.

Property, plant and equipment

Buildings, leasehold improvements, fixtures and fittings, plant and equipment, computer equipment and other tangible assets are stated at cost, less any accumulated depreciation. The Group recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other costs are recognised in the income statement as an expense as incurred.

Costs capitalised are depreciated to their estimated residual values in equal annual instalments over their estimated useful lives, as follows:

Buildings	25 to 50 years
Leasehold improvements	10 years
Fixtures and fittings	10 years
Plant and equipment	3 to 10 years
Computer equipment	3 to 5 years

Land is stated at cost and is not depreciated. Assets under construction are not depreciated until they are brought into commercial use.

Intangible assets

a) Goodwill

Goodwill is stated at cost less any accumulated impairment losses. On acquisition of a business, goodwill arises where the consideration given exceeds the fair values attributed to the net assets acquired. The goodwill is capitalised and is subject to an annual impairment review and also when there are indications of impairment.

1. Significant accounting policies continued

Intangible assets continued

a) Goodwill continued

Prior to 31 December 2003, purchased goodwill was capitalised and amortised on a straight-line basis, over the investment's estimated useful life, assessed on an individual basis. Impairment reviews were carried out only as was appropriate. Amortisation of goodwill ceased from 1 January 2004.

b) Computer software

Costs incurred in the development of computer software for internal use are capitalised as intangible assets where the software leads to the creation of an identifiable non-monetary asset and it is probable that the expected future economic benefits that are attributable to the asset will flow to the Group. The software is classified as an intangible asset where it is not an integral part of the related hardware and amortised over its estimated useful life which is generally three to five years.

Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash and non-restricted balances with central banks.

Provisions

The Group recognises a provision when there is a present legal or constructive obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and the amount has been reliably estimated.

Taxation

Income tax payable is charged on all taxable profits arising in the accounting period.

Deferred tax is calculated on all taxable temporary differences arising on the differences between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred tax assets and liabilities are recognised at gross on the balance sheet and deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised. Deferred taxes are determined using the rates enacted or substantively enacted at the balance sheet date.

The deferred tax charge or credit is recognised in the income statement unless the deferred tax relates to fair value adjustments for available-for-sale investments, effective elements of cash flow hedges and other amounts taken directly to equity. In these circumstances the deferred tax charge or credit will also be recognised in equity and recycled to the income statement at the same time as when the originating entry is recycled from equity to the income statement. Group relief receivable from the parent company is included in other assets.

Foreign currency translation

Foreign currency monetary assets and liabilities are translated at the rates of exchange ruling on the balance sheet date and foreign currency non-monetary items measured in terms of historical cost are translated using the exchange rate at the date of the transaction. Exchange differences on monetary items are dealt with in the income statement. Exchange differences on non-monetary items are recognised in line with whether the gain or loss on the non-monetary item itself is recognised in the income statement or in equity.

The balance sheets of overseas branches are translated into sterling at the rates of exchange ruling at the balance sheet date and their income statements are translated at the average rates of exchange for the period from 1 January to the balance sheet date. All exchange differences relating to the translation of an overseas branch are recognised through a separate component of other reserves.

Upon the disposal of a foreign operation, the cumulative foreign currency translation reserves which relate to the operation being disposed of is taken to the income statement when the gain or loss on disposal is recognised.

From 1 January 2005, foreign exchange gains or losses on available-for-sale debt securities will be recognised in the income statement.

Employee benefits

The Group accounts for its pension schemes and other non share-based employee benefits under IAS 19 "Employee Benefits".

The Group's main pension scheme, which covers 81% of the Group's employees who have taken up their right to contribute to a pension scheme, is a defined contribution scheme. For this scheme the cost is charged to the income statement as contributions become due. The assets of the Scheme are held in a separately administered fund.

1. Significant accounting policies continued

Employee benefits continued

Certain employees are members of the Prudential plc's defined benefit scheme ("Prudential Scheme"). In line with paragraph 34A of the amendment to IAS 19 "Employee Benefits – Actuarial Gains and Losses, Group Plans and Disclosures", even though the Prudential Scheme is a defined benefit scheme, as there is no contractual agreement or stated policy for charging the net defined benefit cost of the plan as a whole measured in accordance with IAS 19 to individual group entities, the net defined benefit cost of the plan has only been recognised in the financial statements of Prudential plc as it is the legal sponsor employer of the plan. Therefore, in accordance with IAS 19, the Group recognises a cost on the basis of its contributions payable to the plan for the period.

Further details of the Prudential Scheme are shown in the group financial statements of Prudential plc.

Other employee benefits are recognised in the income statement as incurred.

Leased assets

Leases are classified as operating leases where the risks and rewards of ownership are retained by the lessor. Operating lease rentals are expensed to the income statement on a straight line basis.

The Group does not undertake any material financing leases as either lessee or lessor.

Profit share from creditor insurance policies

Profit share from creditor insurance policies are recognised on an accruals basis.

Brand development costs

Brand development costs are written off as incurred.

Treasury shares

Share capital in the Company purchased by the Group is recognised as a reduction in shareholders' equity.

2. Impairment losses on loans and advances to customers

Group operating profit is stated after charging impairment losses on loans and advances to customers of £117.5 million (30 June 2004 on a UK GAAP basis: £92.9 million). The impairment losses on loans and advances to customers at 30 June 2005 have been calculated on the basis of IAS 39, in accordance with the accounting policy in note 1. The balances at 30 June 2004 and 31 December 2004 were calculated on the basis of UK GAAP as explained in the principal accounting policies in the 2004 annual report.

	Continuing £m	Discontinued £m	Total £m
Balance at 31 December 2004 under UK GAAP	249.4	0.9	250.3
IAS 39 transition adjustments	(3.3)	–	(3.3)
IFRS reclassification	7.7	–	7.7
Revised balance at 1 January 2005 under IFRS	253.8	0.9	254.7
Amounts written off	(82.9)	(1.2)	(84.1)
New and additional allowances	117.2	0.3	117.5
Net charge against allowances	34.3	(0.9)	33.4
Balance at 30 June 2005	288.1	–	288.1

Allowances at 30 June 2005 were 3.5% of advances to customers (30 June 2004: 3.1%).

3. Tax

The taxation charge assumes a UK corporation tax rate of 30% (2004: 30%) and comprises:

	Six months ended 30 June 2005 £m	Six months ended 30 June 2004 (Restated)* £m	Year ended 31 December 2004 (Restated)* £m
Tax charge on profit on continuing ordinary activities	3.7	11.5	24.7

* See note 1 on page 06.

4. Discontinued operations

The following is an analysis of the profit/(loss) on ordinary activities after tax for discontinued operations (represented by Egg France and Funds Direct).

	Six months ended 30 June 2005 £m	Three months ended 30 June 2005 £m	Six months ended 30 June 2004 (Restated)* £m	Three months ended 30 June 2004 (Restated)* £m	Year ended 31 December 2004 (Restated)* £m
Net interest (expense)/income	(0.2)	0.3	3.3	1.7	6.4
Other operating income/(expense)	1.0	(0.4)	0.1	0.1	(6.0)
Operating income	0.8	(0.1)	3.4	1.8	0.4
Administrative expenses	(12.6)	(3.7)	(25.3)	(12.0)	(45.6)
Depreciation and amortisation	1.0	1.0	(2.2)	(1.2)	(7.1)
Impairment of goodwill and fixed assets re Funds Direct	–	–	–	–	(16.6)
Impairment losses on loans and advances to customers	(0.3)	–	(10.5)	(5.4)	(20.1)
Utilisation of provision for loss on termination of discontinued operations	13.0	3.4	–	–	25.9
Operating profit/(loss)	1.9	0.6	(34.6)	(16.8)	(63.1)
Release/(provision) for loss on termination of discontinued operations	0.2	–	–	–	(112.8)
Profit/(loss) on discontinued ordinary activities before tax	2.1	0.6	(34.6)	(16.8)	(175.9)
Tax (charge)/credit on profit/(loss) on ordinary activities	(0.6)	(4.1)	12.9	8.0	38.7
Retained profit/(loss) attributable to discontinued operations	1.5	(3.5)	(21.7)	(8.8)	(137.2)

* See note 1 on page 06.

5. Earnings per share

The consolidated earnings/(loss) per share is calculated by dividing the retained profit/(loss) attributable to the Group for the financial period by the weighted average of ordinary shares in issue during the period. The continuing earnings per share was calculated by dividing the profit after tax attributable to continuing operations for the financial period by the weighted average of ordinary shares in issue during the period.

The discontinued earnings/(loss) per share for the six months and three months ended 30 June 2005 is as follows:

	Six months ended 30 June 2005 £m	Three months ended 30 June 2005 £m	Six months ended 30 June 2004 (Restated)* £m	Three months ended 30 June 2004 (Restated)* £m	Year ended 31 December 2004 (Restated)* £m
Discontinued operations:					
Basic earnings/(loss) per share (pence)	0.2	(0.5)	(2.6)	(1.0)	(15.9)
Diluted earnings/(loss) per share (pence)	0.2	(0.5)	(2.6)	(1.0)	(15.9)

* See note 1 on page 06.

The discontinued earnings/(loss) per share was calculated by dividing the retained profit or loss attributable to discontinued operations for the financial period by the weighted average of ordinary shares in issue during the period.

6. Capital reconstruction

In accordance with the resolution agreed by the Annual General Meeting on 16 May 2005, Egg plc has applied to the High Court to undertake a capital reconstruction eliminating the Share Premium account and Capital Reserve to reduce accumulated losses. As at 30 June 2005, two of the three Court hearings required to complete this capital reconstruction had taken place. Accordingly the capital situation of the Group as at 31 December 2004 and as at 30 June 2005 is as follows:

	30 June 2005 £m	31 December 2004 (Restated)* £m
Shareholders' equity		
Called up share capital	412.2	412.2
Share premium account	–	111.0
Capital reserve	179.1	359.7
Other reserves	(3.6)	(0.5)
Accumulated losses	(251.3)	(541.2)
Shareholders' equity	336.4	341.2

* See note 1 on page 06.

Subsequent to the above on 6 July 2005, the final Court hearing was held which further reduced the Capital Reserve to nil and correspondingly decreased accumulated losses on a Group basis to £72.2 million.

7. Cash and cash equivalents

	As at 1 January 2005 (Restated)* £m	Cash flow' £m	As at 30 June 2005 £m
Cash	14.0	(6.7)	7.3
Loans and advances to other banks payable on demand	344.2	296.9	641.1
Cash equivalents	269.4	(163.4)	106.0
	627.6	126.8	754.4

	As at 1 January 2004 (Restated)* £m	Cash flow (Restated)* £m	As at 30 June 2004 (Restated)* £m
Cash	13.3	(0.2)	13.1
Loans and advances to other banks payable on demand	146.6	82.1	228.7
Cash equivalents	163.0	(102.0)	61.0
	322.9	(20.1)	302.8

	As at 1 January 2004 (Restated)* £m	Cash flow (Restated)* £m	As at 31 December 2004 (Restated)* £m
Cash	13.3	0.7	14.0
Loans and advances to other banks payable on demand	146.6	197.6	344.2
Cash equivalents	163.0	106.4	269.4
	322.9	304.7	627.6

* See note 1 on page 06.

1 The movement in cash flow includes FX movements.

The cash balance at 30 June 2005, 31 December 2004 and 30 June 2004 relates solely to a cash ratio deposit, held with the Bank of England.

8. Segmental information

The Group is organised into two main business segments:

(i) Retail Financial Services ("Retail") – is responsible for all customer focused products and services. It includes credit cards, consumer loans, mortgages, savings and insurance products.

(ii) Treasury and Balance Sheet Management ("Wholesale") – is responsible for asset and liability management across the Group's overall balance sheet. In particular it manages the Group's capital and liquidity positions as well as managing market and currency risks.

In determining how to allocate income and costs between these two segments, the Group uses a transfer pricing methodology.

Given its responsibility for management of the overall balance sheet, capital and liquidity the Wholesale segment effectively charges or pays a net transfer price depending on whether it is funding or investing the net balance transferred from the Retail balance sheet each day. This net transfer price is market based and adjusted firstly to take account of liquidity requirements and secondly for derivatives used to manage the interest rate risk within the Retail balance sheet.

The cost of the debt capital held by the Group is split between Retail and Wholesale according to the proportion of risk weighted assets held within each segment. The balance of the risk weighted assets is currently calculated according to the Basel 1 definitions.

8. Segmental information continued

The net return on investing the equity capital, including the costs of the various capital management techniques currently in use by the Group including credit card securitisation and credit default swaps, is earned by Treasury and for segmental reporting purposes is also split between Retail and Wholesale according to the proportion of risk weighted assets held within each segment.

All external customer revenues and expenses are allocated to Retail as are the majority of the Group's operating costs and the investment in brand and marketing. The costs allocated to the Wholesale segment are directly attributable to its lines of business.

As the Group has disposed of its French business, it no longer considers disclosure along geographical segmentation lines to be appropriate. The results, cash flows, assets and liabilities relating to the French business are included within discontinued operations.

	Retail £m	Wholesale £m	Total £m
Six months ended 30 June 2005			
Continuing operations:			
Net interest income	143.8	2.3	146.1
Operating profit	10.3	2.7	13.0
Discontinued operations:			
Net interest expense	(0.2)	-	(0.2)
Operating profit	1.9	-	1.9
Three months ended 30 June 2005			
Continuing operations:			
Net interest income	74.5	0.8	75.3
Operating profit	8.3	1.1	9.4
Discontinued operations:			
Net interest income	0.3	-	0.3
Operating profit	0.6	-	0.6
Year ended 31 December 2004			
Continuing operations:			
Net interest income	280.3	7.1	287.4
Operating profit	55.6	5.4	61.0
Discontinued operations:			
Net interest income	6.4	-	6.4
Operating loss	(63.1)	-	(63.1)
Six months ended 30 June 2004			
Continuing operations:			
Net interest income	141.0	3.5	144.5
Operating profit	30.8	2.0	32.8
Discontinued operations:			
Net interest income	3.3	-	3.3
Operating loss	(34.6)	-	(34.6)
Three months ended 30 June 2004			
Continuing operations:			
Net interest income	68.9	1.6	70.5
Operating profit	18.3	0.8	19.1
Discontinued operations:			
Net interest income	1.7	-	1.7
Operating loss	(16.8)	-	(16.8)

Independent review report by KPMG Audit plc to Egg plc

Introduction

We have been engaged by the Company to review the financial information set out on pages 05 to 20 and we have read the other information contained in the interim report and considered whether it contains any apparent misstatements or material inconsistencies with the financial information.

This report is made solely to the Company in accordance with the terms of our engagement to assist the Company in meeting the requirements of the Listing Rules of the Financial Services Authority. Our review has been undertaken so that we might state to the Company those matters we are required to state to it in this report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company for our review work, for this report, or for the conclusions we have reached.

Directors' responsibilities

The interim report, including the financial information contained therein, is the responsibility of and has been approved by the directors. The directors are responsible for preparing the interim report in accordance with the Listing Rules which require that the accounting policies and presentation applied to the interim figures should be consistent with those applied in preparing the preceding annual financial statements except where any changes, and the reasons for them, are disclosed.

As disclosed on page 05 to the financial information, the next annual financial statements of the Group will be prepared in accordance with IFRSs adopted for use in the European Union.

The accounting policies that have been adopted in preparing the financial information are consistent with those that the directors currently intend to use in the next annual financial statements. There is, however, a possibility that the directors may determine that some changes to these policies are necessary when preparing the full annual financial statements for the first time in accordance with those IFRSs adopted for use by the European Union. This is because, as disclosed on page 05, the directors have anticipated that certain Standards, which have yet to be formally adopted for use in the European Union, will be so adopted in time to be applicable to the next annual financial statements.

Review work performed

We conducted our review in accordance with guidance contained in Bulletin 1999/4 "Review of interim financial information" issued by the Auditing Practices Board for use in the United Kingdom. A review consists principally of making enquiries of Group management and applying analytical procedures to the financial information and underlying financial data and, based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review is substantially less in scope than an audit performed in accordance with Auditing Standards and therefore provides a lower level of assurance than an audit. Accordingly, we do not express an audit opinion on the financial information.

Review conclusion

On the basis of our review we are not aware of any material modifications that should be made to the financial information as presented for the six months ended 30 June 2005.

KPMG Audit Plc

Chartered Accountants
27 July 2005

Average balance sheet (UK business only)

	30 June 2005		30 June 2004		31 December 2004	
	Average balance £m	Average rate %	Average balance £m	Average rate %	Average balance £m	Average rate %
Assets						
Wholesale assets	3,965	4.50	4,219	4.28	4,212	4.51
Mortgages	1,720	5.37	2,014	4.74	1,835	5.09
Personal loans	2,564	7.07	1,779	7.48	2,228	7.25
Credit cards	3,535	9.86	2,940	9.45	3,175	9.61
Total average interest-earning assets	11,784	6.79	10,952	6.27	11,450	6.55
Fixed and other assets	247	–	94	–	339	–
Total assets	12,031	–	11,046	–	11,789	–
Liabilities						
Customer accounts	6,388	4.36	6,494	3.36	6,280	3.90
Wholesale liabilities and subordinated debt	4,687	4.67	3,923	4.30	4,540	4.67
Total average interest-bearing liabilities	11,075	4.51	10,417	3.71	10,820	4.22
Other liabilities	459	–	208	–	450	–
Total liabilities	11,534	–	10,625	–	11,270	–
Total equity	497	–	421	–	519	–
Total equity and liabilities	12,031	–	11,046	–	11,789	–

Note:

The above analysis represents interest earned or borne on on-balance sheet assets and liabilities only. In each case the average balances and yields have been calculated on a 12-month rolling basis.

The figures for Q2 2005 are compiled on a full IFRS basis including the effect of IAS 32 and IAS 39 and as such are no longer strictly comparable to the prior period and prior year figures.

Average yields (UK business only)

	30 June 2005	30 June 2004	31 December 2004
	Average rate %	Average rate %	Average rate %
Interest income as a percentage of average interest-earning assets	6.79	6.27	6.55
Interest expense as a percentage of average interest-bearing liabilities	4.51	3.71	4.22
Interest spread	2.28	2.56	2.33
Net interest margin (includes interest on off-balance sheet items)	2.45	2.56	2.51

1. UK GAAP to IFRS reconciliations – income statement

Reconciliation of the income statement – for the six months ended 30 June 2004

	UK GAAP on an IFRS format £m	Reclassifications £m	IFRS 2 Share-based Payments £m	IFRS 3 Business Combinations £m	IAS 12 Income Taxes £m	Total effect of transition to IFRS £m	Restated under IFRS (unaudited) £m
Continuing operations:							
Interest income	433.1	–	–	–	–	–	433.1
Interest expense	(288.6)	–	–	–	–	–	(288.6)
Net interest income	144.5	–	–	–	–	–	144.5
Fee and commission income	105.8	–	–	–	–	–	105.8
Fee and commission expense	(14.8)	–	–	–	–	–	(14.8)
Net fee and commission income	91.0	–	–	–	–	–	91.0
Other operating income	3.4	–	–	–	–	–	3.4
Operating income	238.9	–	–	–	–	–	238.9
Administrative expenses							
personnel expenses	–	(45.6)	1.4	–	–	(44.2)	(44.2)
depreciation and amortisation	(11.9)	–	–	–	–	–	(11.9)
other administrative expenses	(113.2)	45.6	–	–	–	45.6	(67.6)
	(125.1)	–	1.4	–	–	1.4	(123.7)
Impairment losses on loans and advances to customers	(82.4)	–	–	–	–	–	(82.4)
Operating profit	31.4	–	1.4	–	–	1.4	32.8
Share of operating profit of joint venture	0.3	–	–	–	–	–	0.3
Share of associate losses	(0.8)	–	–	0.6	–	0.6	(0.2)
Profit on continuing ordinary activities before tax	30.9	–	1.4	0.6	–	2.0	32.9
Tax charge on profit on continuing ordinary activities	(11.7)	–	–	–	0.2	0.2	(11.5)
Profit on continuing ordinary activities after tax	19.2	–	1.4	0.6	0.2	2.2	21.4
Discontinued operations:							
Loss on discontinued ordinary activities after tax	(22.1)	–	–	–	0.4	0.4	(21.7)
Retained loss for the period	(2.9)	–	1.4	0.6	0.6	2.6	(0.3)

2. UK GAAP to IFRS reconciliations – balance sheet

Reconciliation of the balance sheet as at 30 June 2004

	UK GAAP on an IFRS format £m	IFRS adjustments £m	Restated under IFRS (unaudited) £m
Assets			
Cash and balances with central banks	13.1	–	13.1
Loans and advances to banks	294.7	–	294.7
Investment securities	4,145.8	–	4,145.8
Derivative financial instruments	–	12.8	12.8
Loans and advances to customers	7,105.5	–	7,105.5
Prepayments and accrued income	77.5	–	77.5
Investments in joint venture and associates	5.9	0.6	6.5
Property, plant and equipment	100.9	(47.0)	53.9
Intangible assets	6.1	47.4	53.5
Deferred tax	24.9	0.7	25.6
Other assets	449.4	(12.8)	436.6
Total assets	12,223.8	1.7	12,225.5
Liabilities			
Deposits by banks	2,016.0	–	2,016.0
Securities sold under agreements to repurchase	816.8	–	816.8
Customer accounts	6,698.6	–	6,698.6
Investment securities in issue	1,339.2	–	1,339.2
Derivative financial instruments	–	13.0	13.0
Other liabilities	292.9	(13.0)	279.9
Accruals and deferred income	170.0	–	170.0
Subordinated liabilities			
Dated loan capital	450.8	–	450.8
Total liabilities	11,784.3	–	11,784.3
Shareholders' equity			
Called up share capital	412.2	–	412.2
Share premium account	110.9	–	110.9
Capital reserve	359.7	–	359.7
Other reserves	–	0.3	0.3
Accumulated losses	(444.3)	1.4	(442.9)
Total equity attributable to the equity holders of the parent	438.5	1.7	440.2
Minority interests (equity)	1.0	–	1.0
Total equity	439.5	1.7	441.2
Total equity and liabilities	12,223.8	1.7	12,225.5

3. UK GAAP to IFRS reconciliations – cash flow statement

The most significant adjustment to the cash flow statement under IFRS is an adjustment to reclassify certain amounts from loans and advances to cash and cash equivalents. Presentation of a cash flow statement on an IFRS basis does not affect the underlying cash flows of the business.

Reconciliation of the cash flow statement – for the six months ended 30 June 2004

	UK GAAP on an IFRS format £m	IFRS adjustments £m	Restated under IFRS (unaudited) £m
Cash flows from operating activities			
Continuing operations:			
Operating profit before taxation	31.4	1.4	32.8
Adjusted for:			
Depreciation, impairment and amortisation	22.3	(1.4)	20.9
Impairment losses on loans and advances to customers	30.4	–	30.4
Gain on sale of investment securities	(1.9)	–	(1.9)
Net (increase)/decrease in operating assets:			
Loans and advances to banks	118.5	(80.3)	38.2
Loans and advances to customers	(399.0)	–	(399.0)
Securities purchased under agreement to resell	–	–	–
Accrued income and prepayments	(1.9)	–	(1.9)
Other assets	(174.1)	–	(174.1)
Net increase/(decrease) in operating liabilities:			
Deposits by banks	303.4	–	303.4
Securities sold under agreements to repurchase	(12.3)	–	(12.3)
Customer accounts	256.8	–	256.8
Investment securities in issue	(83.7)	–	(83.7)
Accruals and deferred income	13.0	–	13.0
Other liabilities	(26.9)	–	(26.9)
Taxation paid	(0.2)	–	(0.2)
Net cash inflow/(outflow) from continuing operating activities	75.8	(80.3)	(4.5)
Discontinued operations:			
Net cash inflow from discontinued operating activities	41.0	(21.7)	19.3
Total net cash inflow from operating activities	116.8	(102.0)	14.8
Cash flows from investing activities			
Continuing operations:			
Purchase of property, plant and equipment	(3.6)	–	(3.6)
Disposal of property, plant and equipment	–	–	–
Purchase of software intangibles	(14.2)	–	(14.2)
Purchase of investment securities	(2,924.4)	–	(2,924.4)
Disposal of investment securities	2,904.2	–	2,904.2
Net cash outflow from continuing investing activities	(38.0)	–	(38.0)
Discontinued operations:			
Net cash outflow from discontinued investing activities	(2.2)	–	(2.2)
Total net cash outflow from investing activities	(40.2)	–	(40.2)
Cash flows from financing activities			
Continuing operations:			
Proceeds from issue of share capital	5.3	–	5.3
Total net cash inflow from financing activities	5.3	–	5.3
Increase/(decrease) in cash and cash equivalents in the period	81.9	(102.0)	(20.1)
Cash and cash equivalents at the beginning of the period	159.9	163.0	322.9
Cash and cash equivalents at the end of the period	241.8	61.0	302.8

see you next year

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How to contact us

Shareholder enquiries:

Lloyds TSB Registrars
The Causeway
Worthing
West Sussex BN99 6DA
Tel: 0845 6060252

Registered Office:

1 Waterhouse Square
138-142 Holborn
London EC1N 2NA

Registered Number:

Registered in England and Wales
Number 2448340

Company Secretary:

Sue Windridge
1 Waterhouse Square
138-142 Holborn
London EC1N 2NA

Investor relations:

Kieran Coleman
1 Waterhouse Square
138-142 Holborn
London EC1N 2NA
Tel: 020 7526 2648

Media enquiries:

Tel: 020 7526 2600

Website address:

www.egg.com

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