OneSavings Bank plc

Interim report for the six months ended 30 June 2018

LEI: 213800WTQKOQI8ELD692

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OneSavings Bank plc ('OSB' or 'the Bank' or 'the Group'), the specialist lending and retail savings group, announces today another strong set of results for the six months ended 30 June 2018.

Financial highlights

- Profit before tax[1] increased 17% to £91.8m (H1 2017: £78.4m)
- Net loan book growth of 11%, driven by 17% growth in gross organic origination to £1,444m (H1 2017: £1,229m)
- Continued focus on cost discipline and efficiency alongside strong income growth delivered a cost to income ratio[2] of 27% (H1 2017: 28%)
- Net interest margin ('NIM')[3] of 301bps (H1 2017 restated: 324bps)
- Loan loss ratio[4] of 11bps (H1 2017: 4bps), with prior period benefitting from increasing property values
- Fully-loaded Common Equity Tier 1 ('CET1') capital ratio strong at 13.3% (FY 2017: 13.7%)
- Basic earnings per share[1] 27.5p[5], up 14% (H1 2017: 24.1p)
- Return on equity[6] of 26% (H1 2017: 28%)
- Interim dividend of 4.3p per share, up 23% (H1 2017: 3.5p)[7]

Commenting on the results, Group CEO, Andy Golding said:

"I am delighted that OneSavings Bank has continued to deliver excellent shareholder returns in the first half of 2018. Volumes grew strongly with 17% growth in organic originations, driven by high demand for our professional Buy-to-Let and our commercial and semi-commercial products. This supported 17% growth in profit before tax to £91.8m and a strong return on equity of 26%.

Whilst regulatory and tax changes in the Buy-to-Let market have dampened industry-wide demand for new purchase mortgages, this has been partially offset by an increase in demand for remortgages. We focus on the professional Buy-to-Let market where trends remain positive. Demand for five year fixed rate products has risen noticeably across the market with competition continuing to increase, however we continue to see good opportunities for growth and our InterBay Commercial business continues to flourish.

Given the growth already achieved this year and considering the current pipeline and application levels for the third quarter to date, we now expect to deliver net loan book growth of high-teens in 2018, whilst maintaining an appropriate margin for the risks we are underwriting. Our continued focus on cost efficiency, whilst investing in the future, is reflected in our market-leading cost to income ratio for the first half of 27%. There will be further planned expenditure in the second half, as we invest in technology infrastructure and enhancements to our online savings and mortgage origination platforms. We continue to expect that our cost to income ratio will be c.30% for the full year, as previously guided, with all other guidance for the full year also unchanged."

Key metrics

	H1 2018	**H1 2017**
Total assets (£bn)	**9.7**	7.2

Net loan book (£bn)	**8.1**	6.5
Loan to deposit ratio[8] (%)	**90**	93
3 months+ arrears[9] (%)	**1.3**	1.4
Customer net promoter score	**+60**	+60

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Results presentation

OneSavings Bank will be holding an interim results presentation for analysts at 9:30am on Thursday 23 August at The Lincoln Centre, 18 Lincoln's Inn Fields, WC2A 3ED. The UK dial-in is 0808 109 0700 and the password is OneSavings Bank. The presentation will be webcast and available from 9.30am on the OneSavings Bank website at www.osb.co.uk/investors/results-reports-presentations. Registration is open immediately.

About OneSavings Bank plc

OneSavings Bank plc ('OSB') began trading as a bank on 1 February 2011 and was admitted to the main market of the London Stock Exchange in June 2014 (OSB.L). OSB joined the FTSE 250 index in June 2015. OSB is a specialist lending and retail savings group authorised by the Prudential Regulation Authority, part of the Bank of England, and regulated by the Financial Conduct Authority and Prudential Regulation Authority.

OSB primarily targets market sub-sectors that offer high growth potential and attractive risk-adjusted returns in which it can take a leading position and where it has established expertise, platforms and capabilities. These include private rented sector Buy-to-Let, commercial and semi-commercial mortgages, residential development finance, bespoke and specialist residential lending and secured funding lines. OSB originates organically through specialist brokers and independent financial advisers. It is differentiated through its use of highly skilled, bespoke underwriting and efficient operating model.

OSB is predominantly funded by retail savings originated through the long-established Kent Reliance name, which includes online and postal channels, as well as a network of branches in the South East of England. Diversification of funding is currently provided by access to a securitisation programme and the Term Funding Scheme.

Notes

[1] Since the Group did not record any exceptional items in the first half of 2018 or 2017, the underlying and statutory metrics are equal

[2] Administrative expenses, including depreciation and amortisation as a percentage of total income

[3] Net interest income as a percentage of average interest bearing assets including off balance sheet Funding for Lending Scheme drawings, annualised. The method of annualising NIM for the first half has been enhanced to use the actual day count instead of an assumed 182.5 days, to provide comparability with the full year NIM and the Bank's internal reporting approach. The comparative for the first half of 2017 has been restated accordingly from 322bps to 324bps.

[4] Impairment losses expressed as a percentage of average gross loans and advances, annualised, under IAS 39 provisioning approach in H1 2017 and under IFRS 9 approach in H1 2018

[5] Profit after tax attributable to ordinary shareholders (profit after tax less coupons on equity PSBs and AT1 securities, including the tax effect, of £2.4m (H1 2017: coupons on equity PSBs, including the tax effect, of £0.4m) divided by the weighted average number of ordinary shares in issue

[6] Profit after tax after deducting coupons on equity PSBs and AT1 securities, including the tax effect, of £2.4m (H1 2017: coupons on equity PSBs of £0.4m) as a percentage of average shareholders' equity (excluding equity PSBs of £22m and AT1 securities of £60m) of £518.0m in first half of 2018 and £417.0m in first half of 2017, annualised

[7] The proposed interim dividend of 4.3 pence per share for the first half of 2018 is based on one third of the total 2017 dividend of 12.8 pence per share (H1 2017: 3.5 pence per share, one third of the 2016 dividend of 10.5 pence per share)

[8] Excluding the impact of the Bank of England's Funding for Lending and Term Funding Schemes

[9] Portfolio arrears rate (excluding legacy problem loans) of accounts for which there are missing or overdue payments by more than three months as a percentage of gross loans

Alternative performance measures

OSB believes that the use of alternative performance measures ('APMs') for profitability and earnings per share provide valuable information to the readers of the financial statements and present a more consistent basis for comparing the Group's performance between financial periods, by adjusting for exceptional non-recurring items. APMs also reflect an important aspect of the way in which operating targets are defined and performance is monitored by the Board. However, any APMs in this document are not a substitute for IFRS measures and readers should consider the IFRS measures as well.

Important disclaimer

This document should be read in conjunction with the documents distributed by OneSavings Bank plc ('OSB') through the Regulatory News Service ('RNS'). This document contains certain forward-looking statements, beliefs or opinions, including statements with respect to the business, strategy and plans of OSB and its current goals and expectations relating to its future financial condition, performance and results. Statements that are not historical facts, including statements about OSB's, its directors' and/or management's beliefs and expectations, are forward-looking statements. Such forward-looking statements include, without limitation, those preceded by, followed by or that include the words 'targets', 'believes', 'estimates', 'expects', 'aims', 'intends', 'will', 'may', 'anticipates', 'projects', 'plans', 'goals', 'forecasts', 'outlook', 'likely', 'guidance', 'trends', 'future', 'would', 'could', 'should' or similar expressions or negatives thereof. By their nature, forward-looking statements involve risk and uncertainty because they are based on assumptions that may or may not be accurate, relate to events that may or may not occur in the future and depend on known and unknown risks and circumstances which may be beyond OSB's control. Factors that could cause actual business, strategy, plans and/or results (including but not limited to the payment of dividends) to differ materially from the plans, objectives, expectations, estimates and intentions expressed or implied in such forward-looking statements made by OSB or on its behalf include, but are not limited to: general political, social, economic and business conditions in the UK (such as the UK's exit from the European Union (the 'EU)) and internationally; market related trends and developments; fluctuations in exchange rates, stock markets, inflation, deflation, interest rates and currencies; policies of the Bank of England, the European Central Bank and other G8 central banks; the ability to access sufficient sources of capital, liquidity and funding when required; changes to OSB's credit ratings; the ability to derive cost savings and other benefits including, but without limitation, as a result of any acquisitions, disposals and other strategic transactions; changing demographic developments, and changing customer behaviour, including consumer spending, saving and borrowing habits; changes in customer preferences; changes to borrower or counterparty credit quality; instability in the global financial markets, including Eurozone instability, the potential for countries to exit the EU or the Eurozone, and the impact of any sovereign credit rating downgrade or other sovereign financial issues; technological changes and risks relating to IT and operational infrastructure, systems, data and cyber security; natural and other disasters, adverse weather and similar contingencies outside OSB's control; inadequate or failed internal or external processes, people and systems; terrorist acts and other acts of war or hostility and responses to those acts; geopolitical, pandemic or other such events; changes in laws, regulations, taxation, accounting standards or practices, including as a result of an exit by the UK from the EU; regulatory capital or liquidity requirements and similar contingencies outside OSB's control; the policies and actions of governmental or regulatory authorities in the UK, the EU or elsewhere including the implementation and interpretation of key legislation and regulation; the ability to attract and retain senior management and other employees; the extent of any future impairment charges or write-downs caused by, but not limited to, depressed asset valuations, market disruptions and illiquid markets; market relating trends and developments; exposure to regulatory scrutiny, legal proceedings, regulatory investigations or complaints; changes in competition and pricing environments; the inability to hedge certain risks economically; the adequacy of loss reserves; the actions of competitors, including non-bank financial services and lending companies; and the success of OSB in managing the risks of the foregoing. For additional information on possible risks to OSB's business, please see the Risk Review section of the OSB 2017 Annual Report and Accounts. Copies of this are available at www.osb.co.uk and on request from OSB.

No representation, warranty or assurance is made that any of these statements or forecasts will come to pass or that any forecast results will be achieved. Persons receiving this document should not place undue reliance on any forward-looking statements made in this document. Such forward looking statements speak only as of the date they are made and it should not be assumed that they have been revised or updated in the light of new information or future events. Except as required by the Prudential Regulation Authority, the Financial Conduct Authority, the London Stock Exchange PLC or applicable law, OSB expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained in this document to reflect any change in OSB's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

The information, statements and opinions contained in this document and subsequent discussion do not constitute a public offer, invitation or inducement under any applicable law or an offer to purchase, sell or otherwise deal in any securities or financial instruments or any advice or recommendation with respect to such securities or financial instruments. Nothing in this document shall be construed as a profit forecast. Past performance cannot be relied upon as a guide to future performance and persons needing advice should consult an independent financial adviser.

Key Performance Indicators

£1,444m **Gross new organic lending up 17%**
(H1 2017: £1,229m)

£8.1bn **Net loan book up 11%**
(FY 2017: £7.3bn)

£91.8m[1] **Statutory and underlying profit before tax up 17%**
(H1 2017: £78.4m)

27.5p[1,5] **Statutory and underlying basic EPS up 14%**
(H1 2017: 24.1p)

26%[6] **Return on equity reduced by 2ppts**
(H1 2017: 28%)

301bps[3] **Net interest margin down 23bps**
(H1 2017: restated 324bps)

27%[2] **Cost to income ratio improved by 1ppt**
(H1 2017: 28%)

13.3% **Fully-loaded common equity tier 1 ratio stable**
(H1 2017: 13.7%)

11bps[4] **Loan loss ratio up by 7bps**
(H1 2017: 4bps)

1.3%[9] **3 months+ in arrears stable**
(H1 2017: 1.4%)

+60 **Customer NPS stable**
(H1 2017: +60)

4.3p[7] **Interim dividend per share up 23%**
(H1 2017: 3.5p)

For definitions of key ratios please see footnotes above

OneSavings Bank plc

Interim report for the six months ended 30 June 2018

Chief Executive's Statement

Progress in the first half of 2018

I am delighted that OneSavings Bank delivered excellent progress and shareholder returns in the first six months of 2018. Continued strength in our core Buy-to-Let/SME segment supported strong earnings growth, with an increase in statutory and underlying basic earnings per share to 27.5p, up 14% on the first half of 2017. I am pleased to report statutory and underlying pre-tax profit of £91.8m, a 17% increase on the same period last year.

OSB continued to deliver on what we do best; providing customer-focused propositions catering for the needs of professional landlords and borrowers with more complex requirements. Our attractive market proposition supported net loan book growth of 11% to £8.1bn in the first half of 2018. This achievement highlights both our strong organic origination capability, with 17% growth in total organic origination versus the first half of 2017, and the positive impact of our Choices programme, with retention rates of c.60% within three months of borrowers' initial products ending.

OSB maintained its well-established prudent and disciplined approach to lending, continuing to focus on generating high risk-adjusted returns without making significant changes to our credit policy or attitude to risk. Net interest margin ('NIM') for the first half was 301bps, reflecting the impact of front book pricing, partially offset by the favourable cost of retail funds, as the wider savings market did not fully price in the November 2017 Bank of England Base Rate rise, and the benefit of holding a higher average balance of the Bank of England's Term Funding Scheme ('TFS').

Net loan book growth of £791m was achieved whilst delivering a 26% return on equity, and our cost to income ratio remains strong at 27% for the first half. There will be further planned expenditure in the second half as we invest in our technology infrastructure and enhancements to online savings and mortgage origination platforms.

Continued development of our strong lending franchise

We continue to differentiate ourselves from the competition by offering well-defined propositions in markets where we have the experience and distribution relationships to successfully develop and service those markets.

Net loan book growth of 11% in the period was driven by a 17% increase in gross organic origination to £1.4bn against the same period in 2017. We continued to see good opportunities with professional landlords in our core Buy-to-Let market and additional opportunities in our InterBay Commercial brand.

A high proportion of borrowers choose to take a new product with the Bank upon the end of their initial product term through Choices, OSB's mortgage product retention scheme. Under Choices, borrowers are encouraged to engage with their broker to receive advice and select from a bespoke product set.

Our coordinated distribution across all brands remains a core strategic differentiator and we have continued to gain industry recognition, winning national and broker firm awards throughout the period, including Best Specialist Mortgage Provider from Moneyfacts as well as Mortgage Strategy Awards for Best BDM Team, Best Specialist Lender and Best Buy-to-Let Lender.

The core Buy-to-Let segment, which comprises 80% of the OSB loan book, is demonstrating robust demand from professional and incorporated landlords with high levels of refinancing partially offsetting lower purchase activity and reduced demand from amateur landlords. Landlord confidence is showing modest signs of recovery as professional landlords adjust to the new tax regime.[1]

For Buy-to-Let, remortgages continue to represent c.58% of new origination for our main Kent Reliance brand. Professional/multi-property landlords accounted for 79% of Buy-to-Let completions by value during the first half of 2018, with a continued rise in the demand for five year fixed rate products for Kent Reliance from c.43% at the end of 2017 to 59% for the first six months of 2018. Limited company purchase applications for Kent Reliance were 71% of total purchase applications for the first six months of 2018, up from 69% in 2017.

Chief Executive's Statement

Our InterBay Commercial business, which provides a range of commercial, semi-commercial, bridging and more complex Buy-to-Let mortgages, has gone from strength to strength following the expansion of distribution to a wider broker audience in the first half. It has achieved a material presence with its intermediary audience, with its bridging proposition gaining good traction. This business lends at sensible loan to values ('LTVs'), and generates strong returns on a risk-adjusted basis.

We saw a reduction in originations in the residential sector in the first half of 2018 to £111m (H1 2017: £132m). Towards the end of the second quarter, we launched a new residential product range and we are seeing good levels of applications for these products in advance of the implementation of our new mortgage origination platform in early 2019. Over the medium term, we see an opportunity to deliver attractive risk-adjusted returns from this new product range, particularly once we transition to IRB.

We continue to be very pleased with the performance of our Heritable Development Finance business, which was set up as a joint venture with our Heritable team in late 2013. The quality of our development finance business pipeline remains strong, with new applications coming primarily from a mixture of repeat business from the team's extensive existing relationships and referrals. The business has written £581m of loans of which £287m have been repaid to date since its launch in 2014. Heritable is now funding over 1,000 residential units, of which 75% are located outside of London.

The Bank's secured funding line business in both its Buy-to-Let/SME and Residential segments continues to grow, with cautious risk fundamentals applied. During the first six months of 2018, gross advances to the specialty finance market, including bridging loan and asset finance businesses, totalled £94m with total loans outstanding of £158m as at 30 June 2018. During the period, one new £50m facility was approved and a number of existing facilities were increased.

Sustainable funding model with outstanding customer satisfaction

We continue to benefit from our stable and award-winning retail funding franchise, with over 23,000 new savings customers joining the Bank in the first half of 2018. The strength and fairness of our retail savings proposition continues to allow the Bank to raise significant funds without needing to price at the very top of the best buy tables. Our excellent customer service is demonstrated by our very strong customer Net Promoter Score of +60, and our exceptionally strong retention rates on maturing bonds and ISAs at 96%.

We remain committed to funding our loan book using retail savings and funding additional liquidity requirements through wholesale markets. We drew additional funds from the Term Funding Scheme in February 2018, with a total balance of £1.5bn as at 30 June 2018. Net new retail deposits were up 12% from 31 December 2017 to £7.4bn, as OSB took the opportunity to raise deposits at attractive rates, demonstrating the strength of our retail savings franchise. We expect to be in a position to return to the securitisation market in the fourth quarter of 2018.

Well-capitalised with strong risk management

The Group's total arrears balance remains low, and the portfolio arrears rate remained broadly stable at 1.3% as at 30 June 2018 (30 December 2017: 1.2%). The Group's loan loss ratio[2] for the first half was 11bps (H1 2017: 4bps), with the increase due primarily to the positive impact of indexing in the comparative period. On an underlying basis, excluding the impact of indexing, the loan loss ratio was broadly flat, as we have seen no deterioration in the credit quality across our lending portfolio.

We have maintained an appropriate level and quality of capital to support our growth objectives and to meet prudential requirements. Our CET1 ratio of 13.3% as at 30 June 2018 (31 December 2017: 13.7%) remains comfortably in excess of the regulatory requirements. The Bank's total capital ratio was 16% as at 30 June 2018 (31 December 2017: 16.9%).

Chief Executive's Statement

The weighted average LTV of the mortgage book remained low at 65% as at 30 June 2018, with an average LTV of 69% on new origination in the first half. Our average interest coverage ratio ('ICR') increased in the period to 192% (FY 2017: 185%).

Cost discipline central to our business
The low cost to income ratio of 27% reflects our efficient and scalable operating platform, and has been achieved despite additional investment in the business to meet the demands of new regulation. General Data Protection Regulation ('GDPR') and Payment Services Directive ('PSD 2') have gone live in the first half and work continues on IRB and other smaller regulatory projects. These regulatory projects, together with planned expenditure on our technology infrastructure, enhancements to our online savings and mortgage origination platforms are expected to lead to an increase in operating costs in the second half of 2018. However, we will continue to focus on delivering further efficiencies in the cost of running the Bank on a 'business as usual basis', through continued disciplined cost management, the benefits of scale and leveraging our unique operating platform in India ('OSBI') as we grow.

OSBI undertakes a range of primary processing services at a significantly lower cost than an equivalent UK-based operation, with quality of service consistently high, as reflected in an outstanding customer NPS of +60. The focus on driving improved customer experience extends to both our savings and lending franchises. Broker NPS was +33 for the first six months of 2018.

The Group successfully implemented its IFRS 9 impairment calculation approach on 1 January 2018, integrating this approach into core risk management processes such as the setting of risk appetite, business planning, stress testing and the Internal Capital Adequacy Assessment Process ('ICAAP'). We remain pleased with the progress made towards our IRB application, with the project focusing on delivering shareholder value by utilising the IRB rating system to drive enhancements to the Group's approach to risk management.

We continue to develop our business for the future
We continue to see opportunities in our core markets, and in the first half of 2018 we introduced a range of near prime products ahead of our strategic re-entry into the residential mortgage market. This initiative will be supported by the implementation of our enhanced mortgage origination system in 2019. We also extended the reach of our InterBay brand during the first half of 2018, leveraging the Group-wide distribution capability that provides us with competitive advantage in specialist markets.

We welcomed the recalibration of risk weights in the final revisions to the Basel III reforms on standardised capital requirements published in December 2017. We believe that these new calibrations, combined with the final IRB output floor, will be beneficial to the Bank's capital requirements, especially for residential lending at sensible loan to values. The Bank intends to develop and grow its bespoke residential proposition in time for the transition to IRB. Over the medium term, we see an opportunity to deliver attractive risk-adjusted returns in this segment. However, we remain cautious until the final rules are adopted.

OSB has begun to test its entry into the UK asset finance market, and we anticipate funding our first transactions later this year. This has been a long-stated goal and entry into this market is in line with OSB's strategy of targeting secured lending markets where we can bring our skills to the fore to generate strong returns on a risk-adjusted basis. As in all our lending segments, our proposition is based on providing excellent customer service to both brokers and customers, alongside strong working relationships with both. Our customers will be SMEs and small corporate businesses and we will be financing their business-critical assets which maintain an established inherent resale value. We have recruited a team of experienced high calibre asset finance professionals to execute our plans. Whilst we plan to become a meaningful funder in this market, it will not materially affect our results in the short to medium-term.

Chief Executive's Statement

Outlook

Even though we are seeing an increased level of competition, especially for five year fixed rate Buy-to-Let products, we continue to see opportunities for growth in our core markets. Given the growth already achieved this year and considering the current pipeline and application levels for the third quarter to date, we now expect to deliver net loan book growth of high-teens in 2018 driven by organic lending and strong retention. All other guidance for the full year remains unchanged.

We are mindful of the macroeconomic environment, primarily driven by uncertainties surrounding the outcome of Brexit negotiations and the potential impact on the UK economy, including pressure on house prices, particularly in London. However, we believe that our specialist underwriting capabilities across our segments are even more relevant in times of uncertainty, as they give us a greater and deeper understanding of the risks that we can actively manage and price for. We manage the business prudently with careful business planning together with strong credit risk management across the life cycle, and continue to focus on achieving high risk-adjusted returns in our chosen markets.

We continue to see opportunities to grow our business at attractive returns. We remain well-placed to take advantage of our strong relationships, our distribution reach, manual underwriting and credit risk management expertise to compete successfully in our chosen markets, lending responsibly to our customers.

Andy Golding

Chief Executive Officer

[1] BDRC Landlord Panel, July 2018
[2] Under IAS 39 provisioning approach in H1 2017 and under IFRS 9 approach in H1 2018

Interim Management Report

Financial review

Summarised financial information, including key ratios, is presented in the tables below:

Summary Profit or Loss	H1 2018 £m	H1 2017 £m
Net interest income	**135.2**	117.1
Fair value losses on financial instruments	**(1.9)**	(5.6)
Net fees and commissions	**0.2**	0.3
External servicing fees	**(0.4)**	(1.0)
Administrative expenses[1]	**(35.9)**	(30.6)
FSCS and other regulatory provisions	**(1.1)**	(0.4)
Impairment losses	**(4.3)**	(1.4)
Statutory and underlying profit before tax	**91.8**	78.4
Statutory and underlying profit after tax	**69.5**	59.0

Key ratios	H1 2018	H1 2017
Net interest margin (restated)[2]	**301bps**	324bps
Basic earnings per share, pence	**27.5**	24.1
Underlying basic earnings per share, pence	**27.5**	24.1
Return on equity	**26%**	28%
Management expense ratio[3], annualised	**79bps**	89bps
Cost to income ratio	**27%**	28%
Loan loss ratio[4]	**11bps**	4bps

Extracts from the Statement of Financial Position	30-Jun-18 £m	31-Dec-17 £m
Loans and advances	**8,096.5**	7,306.0
Retail deposits	**7,423.8**	6,650.3
Total assets	**9,669.8**	8,589.1
Key ratios		
Liquidity ratio[5]	**16.7%**	15.2%
Common equity tier 1 ratio	**13.3%**	13.7%
Total capital ratio	**16.0%**	16.9%
Total leverage ratio	**5.8%**	6.0%

[1] Including depreciation and amortisation
[2] The method of annualising NIM for the first half has been enhanced to use the actual day count instead of an assumed 182.5 days, to provide comparability with the full year NIM and the Bank's internal reporting approach. The comparative for the first half of 2017 has been restated accordingly from 322bps to 324bps
[3] Administrative expenses including depreciation and amortisation as a percentage of average total assets
[4] Under IAS 39 provisioning approach in H1 2017 and under IFRS 9 approach in H1 2018
[5] Liquid assets as a percentage of funding liabilities

For definitions of other key ratios please see footnotes above

Interim Management Report

Strong profit growth

The Group reported strong profitability in the first half of 2018 with underlying and statutory profit before tax of £91.8m, up 17% compared to £78.4m in the first half of 2017, primarily reflecting growth in the net loan book and net interest income supported by an efficient cost base.

Statutory and underlying profit after tax for the first half of 2018 was £69.5m (H1 2017: £59.0m). This represents an 18% increase compared to the first six month of 2017. The Bank's effective tax rate fell to 24.3% for the first half of 2018 (H1 2017: 24.7%) due to a reduction in the rate of corporation tax from 20% to 19% and a reduction in the proportion of Group profits subject to the Bank Corporation Tax Surcharge following continued strong performance in the InterBay Commercial business.

Net interest margin ('NIM')

The Group reported an increase in net interest income of 15% to £135.2m in the first half of 2018 (H1 2017: £117.1m) and NIM of 301bps (H1 2017 restated: 324bps[1]). The lower NIM reflects the dilutive impact of front book yields, partially offset by a relatively favourable cost of retail funds and additional benefit from the Bank of England's Term Funding Scheme ('TFS'). The favourable cost of retail funds was due primarily to the retail savings market not pricing in the full November 2017 Bank of England Base Rate rise.

Fair value losses on financial instruments

Fair value losses on financial instruments decreased in the first half of 2018 to £1.9m (H1 2017: £5.6m) due primarily to a reduction in accelerated amortisation of fair value adjustments on hedged assets relating to cancelled swaps of £2.5m compared to £6.2m in the first half of 2017. This balance also includes a £0.2m loss on disposal of the residual personal loan portfolio in June 2018.

Net fees and commissions

Net fees and commissions income of £0.2m in the first half of 2018 (H1 2017: £0.3m) comprised fees and commissions receivable of £0.7m (H1 2017: £0.8m) partially offset by fees and commissions payable of £0.5m (H1 2017: £0.5m). Fees and commissions receivable include arrangement fees on funding lines and master servicing fees. Fees and commissions payable include branch agency fees and commission paid to the Kent Reliance Provident Society for conducting member engagement activities for the Bank.

External servicing fees

External servicing fees decreased to £0.4m in the first half of 2018 (H1 2017: £1.0m) due primarily to the transfer of servicing for a number of acquired residential loan books to the Bank's operation in India in July 2017.

Efficient and scalable operating platform

Administrative expenses, including depreciation, were up 17% to £35.9m for the first half of 2018 (H1 2017: £30.6m) due to growth in the business and the increasing cost of meeting new regulation, including GDPR.

The Group's annualised management expense ratio improved by 10bps to 0.79% for the first half of 2018 (H1 2017: 0.89%) and the cost to income ratio improved to 27% (H1 2017: 28%) despite the additional investment in regulatory projects, demonstrating our ability to deliver further efficiencies in the cost of running the Bank on a 'business as usual basis', through continued focus on cost efficiency and leveraging our unique operating platform in India as we grow.

Regulatory provisions

Regulatory provisions expense, which includes the Financial Services Compensation Scheme ('FSCS') levies, increased to £1.1m for the first half of 2018 (H1 2017: £0.4m) due primarily to an increase of £0.9m in other regulatory provisions on acquired books.

Impairment losses

The continuing shift in portfolio mix and continuing positive arrears performance of originations post 2011, coupled with the relatively benign economic environment led to a strong impairment performance within the period.

Impairment losses in the first half of 2018 were £4.3m under IFRS 9 (H1 2017: £1.4m under IAS 39), which represent a loan loss ratio[2] of 11bps (H1 2017: 4bps). The increase in the loan loss ratio is due primarily to the positive impact of enhanced indexing of property values in the first half of 2017. On an underlying basis, excluding the impact of indexing in the comparative period, the loan loss ratio was broadly flat, as we have seen no deterioration in the credit quality across our lending portfolio.

The arrears performance of the front book continues to be very strong. From more than 43,500 loans totalling £9.6bn organically originated since the creation of the Bank in February 2011, only 187 were more than three months in arrears as at 30 June 2018, with a total value of £32.1m and an average loan to value of just 63%.

IFRS 9

The Group successfully implemented IFRS 9 as at 1 January 2018. The day 1 impact of implementation was an increase in impairment provisions of £3.6m. There were no significant provision transfers between impairment stages in the first half of 2018 (see note 12 to the condensed consolidated financial statements below).

Dividends

The Group's dividend policy is to declare interim dividends based on one third of the prior year's total dividend. To that end, the Board has declared an interim dividend of 4.3 pence per share for the first half of 2018, based on the 2017 full year dividend of 12.8 pence per share. The Board continues to target a full year dividend pay-out ratio of at least 25 per cent of underlying profit after tax less coupons on equity PSBs and AT1 securities classified as dividends.

Balance sheet growth

Loans and advances grew by 11% in the first half of 2018 to £8,096.5m (31 December 2017: £7,306.0m). This growth was funded by a mixture of retail deposits which increased by 12% to £7,423.8m (31 December 2017: £6,650.3m) and £250m of additional borrowings under the TFS prior to its closure to new drawings at the end of February 2018. Total borrowings under the TFS as at 30 June 2018 stood at £1,500.0m (31 December 2017: £1,250.0m).

Total assets grew by 13% to £9,669.8m (31 December 2017: £8,589.1m) due to the growth in loans and advances and liquid assets.

Interim Management Report

Liquidity

OneSavings Bank operates under the PRA's liquidity regime. The Bank operates within a target liquidity runway in excess of the minimum regulatory requirement. OSB ended the first six months of 2018 with a liquidity ratio of 16.7% (31 December 2017: 15.2%) as the Bank took the opportunity to draw down additional funding under the TFS before it closed to new borrowings at the end of February 2018 and to raise retail funds at favourable rates.

The Bank's liquidity coverage ratio of 245% as at 30 June 2018 (31 December 2017: 250%) is significantly in excess of the regulatory minimum of 100%.

The Bank's retail savings franchise continues to provide the business with long-term sustainable funding for balance sheet growth as evidenced by the retention rate for maturing deposits of 96% for the first six months of 2018 and an exceptional level of customer satisfaction with a Net Promoter Score of +60.

Capital

The Bank's capital position remained strong, with a fully-loaded CET1 ratio of 13.3% as at 30 June 2018 (31 December 2017: 13.7%) and a total capital ratio of 16.0% (31 December 2017: 16.9%), demonstrating the strong capital generation capability of the business to support significant growth through profitability. The decrease in the capital ratios was primarily due to growth in the loan book, an increase in loans classified as in default on adoption of IFRS 9 and the annual recalibration of the Pillar 1 requirement for operational risk based on higher profitability.

The Bank had a leverage ratio of 5.8% as at 30 June 2018 (31 December 2017: 6.0%) and a Pillar 2a requirement of 1.1% of risk weighted assets (31 December 2017: 1.1%).

[1] The method of annualising NIM for the first half has been enhanced to use the actual day count instead of an assumed 182.5 days, to provide comparability with the full year NIM and the Bank's internal reporting approach. The comparative for the first half of 2017 has been restated accordingly from 322bps to 324bps.
[2] Under IAS 39 provisioning approach in H1 2017 and under IFRS 9 approach in H1 2018

Interim Management Report

Segmental review

The following table shows the Group's loans and advances and contribution to profit by segment:

First half 2018, £m	Total	BTL/SME[1]	Residential mortgages
Net interest income	**135.2**	**102.3**	**32.9**
Other expense	**(2.1)**	**(0.6)**	**(1.5)**
Total income	**133.1**	**101.7**	**31.4**
Impairment losses	**(4.3)**	**(3.0)**	**(1.3)**
Contribution to profit	**128.8**	**98.7**	**30.1**
First half 2017, £m			
Net interest income	117.1	83.4	33.7
Other expense	(6.3)	(1.4)	(4.9)
Total income	110.8	82.0	28.8
Impairment (losses)/credit	(1.4)	(1.5)	0.1
Contribution to profit	109.4	80.5	28.9

As at 30 June 2018, £m	Total	BTL/SME[1]	Residential mortgages
Gross loans to customers	**8,119.4**	**6,516.3**	**1,603.1**
Provision for impairment losses	**(22.9)**	**(13.0)**	**(9.9)**
Net loans to customers	**8,096.5**	**6,503.3**	**1,593.2**
Risk weighted assets	**3,843.7**	**3,091.2**	**752.5**
As at 31 December 2017, £m			
Gross loans to customers	7,327.6	5,654.1	1,673.5
Provision for impairment losses	(21.6)	(13.2)	(8.4)
Net loans to customers	7,306.0	5,640.9	1,665.1
Risk weighted assets	3,348.5	2,642.8	705.7

[1] The personal loan portfolio was disposed of in June 2018. As at 31 December 2017, the net loan book was £0.9m with negative contribution to profit of £0.7m for six months to 30 June 2017.

Buy-to-Let/SME

Buy-to-Let/SME sub-segments: gross loans

	30-Jun-18 £m	31-Dec-17 £m
Buy-to-Let	**5,801.3**	5,033.8
Commercial	**428.6**	370.8
Residential development	**151.2**	143.9
Funding lines	**135.2**	104.5
Personal loans[1]	**-**	1.1
Total	**6,516.3**	5,654.1

[1] See footnote above

This segment comprises secured lending on property for investment and commercial purposes as well as residential development finance to small and medium-sized developers and secured funding lines to other lenders.

OSB delivered 15% net loan book growth to £6.5bn in the Buy-to-Let/SME segment in the first half of 2018, driven by a 21% increase in new organic originations to £1,332.6m for the first half of 2018, compared to £1,097.3m in the first half of 2017.

The core Buy-to-Let market continued to see robust demand from professional landlords with high levels of refinancing partially offsetting lower purchase activity and reduced demand from amateur landlords. Landlord confidence is showing modest signs of recovery as professional landlords adjust to the new tax regime.[1]

Against this backdrop, our Buy-to-Let sub-segment loan portfolio grew by £767.5m in the first half of 2018 to a gross value of £5,801.3m (31 December 2017: £5,033.8m) due to strong levels of organic origination and targeted retention through Choices, our mortgage products transfer scheme. Our weighted average interest coverage ratio increased to 192% in the first half (H1 2017: 190%).

In the Buy-to-Let sub-segment, for our main Kent Reliance brand, remortgages represented c.58% of new originations, and we also saw a continued rise in the demand for five year fixed rate products from c.43% during 2017 to 59% for the first six months of 2018. Limited company purchase applications for Kent Reliance were 71% for the first six months of 2018, up from 69% in 2017. Professional/multi-property landlords accounted for 79% of Buy-to-Let completions by value during the first half of 2018 (H1 2017: 77%).

Our InterBay Commercial business, which offers a range of commercial, semi-commercial, bridging and more complex Buy-to-Let mortgages, extended its distribution network in the first half of 2018. This helped to drive a 16% increase in our commercial and semi-commercial sub-segment with the gross loan book ending at a value of £428.6m as at 30 June 2018 (31 December 2017: £370.8m). The commercial portfolio has a low weighted average loan to value (‘LTV’) of 64% and average loan size of £340,000.

Our Heritable residential development business, which was set up as a joint venture with our Heritable team in late 2013, provides prudent development finance to small and medium-sized residential developers, with a preference for forging relationships with those active outside of the prime central London market. New applications come primarily from a mixture of repeat business from the team's extensive existing relationships and referrals. The residential development funding gross loan book at the end of June 2018 was £151.2m with a further £110.4m committed (31 December 2017: £143.9m and £78.0m, respectively). Since inception through to 30 June 2018, the business has written £580.6m of loans of which £287.2m has been repaid to date. The business is now funding over 1,000 residential units, mostly located outside of London.

In addition, the Bank continued to provide secured funding lines to non-bank lenders which operate in certain high-yielding, specialist sub-segments, such as bridging finance and asset finance. Total credit approved limits as at 30 June 2018 were £305.0m with total loans outstanding of £135.2m (31 December 2017: £303.0m and £104.5m respectively). During the period, one new £50m funding line was added and credit approved limits were increased by a further £22m across two existing funding lines. The pipeline remains robust, however, given macroeconomic uncertainties the Bank continues to adopt a cautious risk approach.

The average LTV in the Buy-to-Let/SME segment remained low at 69% (31 December 2017: 69%) with 0.3% of loans by value with an LTV exceeding 90% (31 December 2017: 0.7%). The average LTV of new Buy-to-Let/SME origination in the first half of 2018 was 70% (H1 2017: 70%).

The Buy-to-Let/SME segment made a contribution to Group profit of £98.7m in the first half of 2018, up 23% compared to £80.5m in the first half of 2017, primarily reflecting the growth in the balance sheet partially offset by lower asset yields.

Residential mortgages

Residential sub-segments: gross loans

	30-Jun-18 £m	31-Dec-17 £m
First charge	**1,190.2**	1,240.6
Second charge	**389.9**	415.3
Funding lines	**23.0**	17.6
Total	**1,603.1**	1,673.5

This segment comprises bespoke first charge mortgages, typically to prime credit quality borrowers with more complex circumstances via the Kent Reliance brand which also operates in the shared ownership market as well as second charge mortgages via the Prestige Finance brand and secured funding lines to other lenders.

During the first half of 2018, OSB's total residential loan portfolio decreased by 4% with a net carrying value of £1,593.2m as at 30 June 2018 (31 December 2017: £1,665.1m) with organic residential lending of £111.2m in the first half (H1 2017: £131.9m).

Our first charge residential book had a gross value of £1,190.2m as at 30 June 2018 (31 December 2017: £1,240.6m) with new organic lending in the first half of 2018 more than offset by redemptions on the back book and acquired mortgage portfolios in run-off.

During the first months of 2018, we focused on developing a new residential product range which launched towards the end of the second quarter.

The second charge residential loan book reduced by 6% as at 30 June 2018 with a gross value of £389.9m (31 December 2016: £415.3m) with organic origination more than offset by redemptions on the organic book and acquired books in run-off. We maintained appropriate pricing for risk in this sub-segment as competitive pressure in the second charge market caused price reductions and we allowed our market share to fall.

OSB continued to provide secured funding lines to non-bank lenders which operate in certain high-yielding, specialist sub-segments, such as residential bridge finance. The Bank continues to adopt a cautious risk approach to these more cyclical businesses given macroeconomic uncertainties. Total credit approved limits as at 30 June 2018 were £32.4m, with total loans outstanding of £23.0m (31 December 2017: £33.6m and £17.6m respectively).

The average LTV in the Residential segment remained low at 56% (31 December 2017: 56%) with only 3% of loans by value with LTV's exceeding 90% (31 December 2017: 3%). The average LTV of new residential origination in the first half of 2018 was 65% (H1 2017: 66%).

Residential mortgages made a contribution to Group profit of £30.1m in the first half of 2018, up 4% from £28.9m in the first half of 2017, primarily reflecting lower accelerated amortisation of hedged assets relating to cancelled swaps, partially offset by higher loan losses, with the comparative period benefitting from the positive impact of property value indexing.

[1] BDRC Landlord Panel, July 2018

Interim Management Report

Risk Management

Progress made during the six months to 30 June 2018

During the six months to 30 June 2018 the Group made strong progress against its strategic risk management objectives for the year.

Key highlights included the continued enhancement of the Group's strategic risk management framework, in particular:

- Continued enhancement to its integrated approach to identifying and assessing risk against Board risk appetite. Risk identification and assessment guided investment decisions in systems and controls
- Improvements to risk quantification to support strategic and business decisions and setting risk appetite to inform capital and funding plans. The Group made good progress against its strategic IRB objective of leveraging internally-developed credit risk models for determining its capital requirements
- Key initiatives relating to data governance and controls and establishing an integrated approach to operational resilience are being leveraged to enable growth in accordance with the risk appetite.

The Group successfully implemented its IFRS 9 impairment calculation approach on 1 January 2018. Within the period the Group also integrated the IFRS 9 approach into other key risk management processes such as the setting of risk appetite, business planning (including loss forecasting), stress testing and the Internal Capital Adequacy Assessment Process ('ICAAP').

The Internal Ratings-Based ('IRB') programme progressed well throughout the period, with enhancements being made to internal models along with further strengthening of the Group's model risk management arrangements.

Enhancements have been made to the Group's data management and governance capabilities in accordance with the Group's strategic data management programme.

Enhanced stress testing and scenario analysis capabilities were developed and implemented during the period, to support the Group's delivery of key regulatory submissions including the ICAAP and the Internal Liquidity Adequacy Assessment Process ('ILAAP').

The Group made significant progress in its Group wide Operational Resilience Programme which was initiated in August 2017 to deliver the appropriate framework, planning and testing of the Group's recovery capabilities. The programme is entering its final phase and is due to conclude in September 2018. The Group recognises the importance of ongoing training and testing in order to reflect the changing nature of the organisation.

The Group continued to make significant investment in people across the Risk and Compliance functions ensuring that there is sufficient capacity and capability to deliver the strategic risk enhancements planned for the second half of the year and beyond. This includes further growth in the risk reporting and analytics team in India which provides skilled resource to support the Risk and Compliance functions in the production of analysis and reporting across multiple risk types.

Principal risks and uncertainties

The Board is responsible for determining the nature and extent of the principal risks it is willing to take in order to achieve its strategic objectives.

There has not been a material change in the Group's business strategy, risk management framework or risk appetite during the six months to 30 June 2018. In the opinion of the Directors, the key principal risks have not changed materially from the overview provided in the 2017 Annual Report and Accounts.

Interim Management Report

Risk Management (continued)

The table below details the principal risks which the Board believes are the most material with respect to potential adverse movements impacting the business model, future financial performance, solvency and liquidity. A more detailed review of the Group's principal risks and uncertainties is detailed within the Risk review in the 2017 Annual Report and Accounts on pages 39 to 44, which can be accessed via our website at www.osb.co.uk.

Principal risks	Key mitigating actions
Strategic and business risk	• Regular monitoring of the Group's strategic and business performance against market commitments, the balanced business scorecard and risk appetite by the Board and the Executive Committees. • The Group also extensively uses stress tests to flex core business planning assumptions to assess potential performance under stressed operating conditions.
Reputational risk	• Established processes are in place to proactively identify and manage potential sources of reputational risk including monitoring of media coverage.
Credit risk	Individual borrower defaults • All loans are extended via bespoke and thorough expert underwriting to ensure the ability and propensity of borrowers to repay is appropriate, whilst sufficient security is in place in case an account defaults. • Should there be problems with a loan, the collections and recoveries team work with customers unable to meet their loan servicing obligations to reach a satisfactory conclusion while adhering to the principle of treating customers fairly. • Our strategic focus on lending to professional landlords means that properties are likely to be well-managed, with income from a diversified portfolio mitigating the impact of rental voids or maintenance costs. Lending to owner-occupiers is subject to a detailed affordability assessment, including the borrower's ability to continue payments if interest rates increase. • Lending on commercial property is focused on security levels, and is scrutinised by the Group's independent Real Estate team as well as by external valuers. • Development finance lending is extended only after a deep investigation of a borrower's track record and the specific project details and requires approval by a dedicated Development Finance Transactional Credit Committee. Macroeconomic downturn • The Group works within clearly defined portfolio limits approved by the Risk Committee and the Board covering loan to value (LTV), affordability, sector and geographic concentration. These are reviewed at least annually. In addition, stress testing is performed to ensure the Group maintains sufficient capital to absorb losses in an economic downturn and will continue to meet its regulatory requirements. Wholesale credit risk • The Group only transacts with high quality wholesale counterparties. Derivative exposures include collateral agreements to mitigate credit exposures.
Market risk	Interest rate risk • The Group measures exposure to interest rate risk in the banking book on a regular basis. Where mismatches exist, the Group's Treasury function actively hedges the exposures using interest rate swaps to match the repricing dates of assets and liabilities. Basis risk • The Group regularly measures exposure to basis risk. Currently the balance sheet is broadly matched for basis risk. Where there is a mismatch of market rates in the portfolio (e.g. base rate vs. LIBOR), the Treasury function hedges the exposure.

Risk Management (continued)

Principal risks	Key mitigating actions
Liquidity and funding risk	• The Group's funding strategy is focused on a highly stable retail deposit franchise. The Group's large number of depositors provides diversification, with a high proportion of balances covered by the Financial Services Compensation Scheme which mitigates the risk of a retail run. • The Group performs in-depth liquidity stress testing and maintains a liquid asset portfolio sufficient to meet obligations under stress. • The Group has prepositioned mortgage collateral with the Bank of England, so that liquidity insurance facilities can be accessed in the unlikely event that it should become necessary. • The Group's funding plan ensures a diverse funding profile and initiatives have been put in place to replace the Term Funding Scheme ('TFS') funding, including the establishment of a Retail Mortgage-Backed Securities ('RMBS') programme.
Solvency risk	• The Group actively monitors its capital requirements and resources against financial forecasts and plans and undertakes stress testing analysis to subject its solvency ratios to extreme but plausible scenarios. • The Group also holds prudent levels of capital buffers based on CRD IV requirements, its own risk appetite and expected balance sheet growth. • The Group engages actively with regulators, industry bodies and advisers to keep abreast of potential changes providing feedback through the consultation process and actively manages its capital strategy and plan.
Operational risk	Network/system intrusion • A series of tools have been designed and deployed to identify and prevent network/system intrusions. The effectiveness of implemented controls is overseen by a dedicated IT Security Governance Committee, with specialist IT security staff employed by the Group. Data risk • The Group continues to invest in its data management architecture, systems governance and controls. People risk • The Group has a series of initiatives that are intended to respond to people risk. This includes both the introduction of a range of development programmes intended to improve retention and increase the population of in-house developed talent and a dedicated talent acquisition team to meet the Group's hiring demands. Operational resilience • The Group established an Operational Resilience Programme that is delivering a Group-wide approach in respect to planning and testing. In addition, the programme is designed to highlight any areas of specific vulnerability. A range of back-up technologies is employed to provide real-time replication on various critical systems while disaster recovery capabilities are tested annually. Real-time system performance monitoring has been established and a dedicated testing team is in place to reduce the risks associated with change management. Operational execution and scalability • In order to mitigate incidents materialising from manual processes the Group maintains an independent Quality Assurance team. In addition the Group has initiated a programme to deliver improved automation across a range of processes.

Risk Management (continued)

Principal risks	Key mitigating actions
Conduct risk	Product suitability • The Group has a strategic commitment to provide simple, customer-focused products. In addition, a Product Governance framework is established to oversee both the origination of new products and to revisit the ongoing suitability of the existing product suite. • The combination of a dedicated Product Governance team and an independent Conduct Risk team serves to effectively manage this risk. Data protection • In addition to a series of network/system controls, the Group performs extensive root cause analysis of any data leaks in order to ensure that the appropriate mitigating actions are taken.
Compliance and regulatory risk	• The Group has an effective horizon scanning process to identify regulatory change. All significant regulatory initiatives are managed by structured programmes overseen by the Change Management team and sponsored at Executive management level. The Group proactively seeks external expert opinions to support its interpretation of the requirements and validation of its response. • The Group undertakes risk-based monitoring and oversight programmes to ensure it continues to meet existing regulatory requirements, has effective systems and controls and delivers fair customer outcomes.

Emerging risks

The Group proactively scans for emerging horizon risks which may have an impact on its ongoing operations and strategy. The Group considers its top emerging risks to be:

Emerging risks	Key mitigating actions
Political and macroeconomic uncertainty As the final details around the UK's withdrawal from the European Union remain unclear, there is an increased likelihood of a period of macroeconomic uncertainty. The Group's lending activity is solely focused within the United Kingdom and as such will be impacted by any risks emerging from changes in the macroeconomic environment.	• The Group has implemented robust monitoring processes and via various stress testing activity (i.e. ad hoc, risk appetite and ICAAP) understands how the Group performs over a variety of macroeconomic stress scenarios and has subsequently developed a suite of early warning indicators which are closely monitored to identify changes in the macro environment.
Competition and funding costs This risk relates to increased competition for retail and wholesale funding, driving up funding costs as firms look to replace funding raised through the FLS and TFS schemes.	• The Group carefully monitors performance against the Board-approved funding plan. • The Group holds liquidity buffers to manage funding requirements under normal and stressed conditions. • The Group has initiated a savings transformation project to deliver proposition enhancements in all channels. • The Group continues to consider alternative funding sources to ensure it is not reliant solely on retail savings. • The firm is in the process of building a securitisation capability.

Risk Management (continued)

Emerging risks	Key mitigating actions
Cyber security risks This risk relates to the Group being unable to maintain pace with the increasing threat of cybercrime.	• The Group continues to enhance its suite of preventative and detective controls to ensure that the control framework is consistent throughout the Group. • Documented response plans are established and testing performed to ensure that any breach is managed effectively. • Dedicated resources are in place and have been further increased in order to manage and coordinate cyber risk-related threats.

Credit risk portfolio performance

The Group's credit profile continues to exhibit strong performance across all key risk indicators including loan and advances positions, LTV and arrears levels.

During the six months to 30 June 2018, the Group observed strong lending growth whilst maintaining credit underwriting standards, with weighted average LTV ratios for new Buy-to-Let/SME lending remaining stable at 70% (30 June 2017: 70%) and 65% for Residential lending (30 June 2017: 66%). During the period, the average weighted interest coverage ratio for new lending increased to 192% versus 190% in the six months to 30 June 2017. Across the residential segment the percentage of new lending with a loan to income greater than 4.5 times reduced to 3.1% versus 3.7% in the comparable prior year period.

This strong lending growth across the Buy-to-Let/SME segment along with the continuing success of the Group's Choices customer retention programme facilitated 11% loan book growth in the period with loans and advances to customers growing to £8.1bn (31 December 2017 £7.3bn). The strong Buy-to-Let/SME growth more than offset a modest contraction in residential lending exposures. Residential lending acquired portfolios continue to run off in line with expectations, more than offsetting new lending in the period.

The total Group weighted average LTV ratio remained broadly stable at 65% as at 30 June 2018, increasing by one percentage point from 64% as at 31 December 2017, driven by strong BTL/SME lending within the period with a weighted average LTV of 70%. Importantly, the Group continues to observe a tighter clustering of LTVs around the weighted average.

Other key risk measures also performed strongly within the period including:

Measure	H1 2018	H1 2017	Variance	Commentary
New origination average LTV for BTL/SME lending	70%	70%	-	• Stable average weighted LTV ratio observed during H1 2018.
Weighted average Interest Coverage Ratio for new BTL/SME lending	192%	190%	+2ppts	• Marginal increase in average weighted ICR.
New origination average LTV for Residential lending	65%	66%	-1ppt	• Marginal improvement in the average weighted LTV ratio observed during H1 2018.
Percentage of new Residential lending with a loan to income (LTI) > 4.5	3.1%	3.7%	-0.6ppts	• Lower level of higher LTI originations within the period.

During the six months to 30 June 2018, the Group's portfolio composition continued to evolve favourably with pre-2011 lending continuing to run down as expected, evidenced by a further reduction in lending

Risk Management (continued)

exposures to Jersey and Guernsey. Post-2011 lending, incorporating enhanced lending criteria, continued to make up an increasing proportion of the Group's total loans and advances to customers:

- exposure to semi-commercial/commercial lending remains low at £428.6m with a weighted average LTV of 63%
- exposure to residential development finance remains low at £151.2m with a further £110.4m committed and a weighted average LTV of 34%, and
- the Group has limited exposure to high LTV loans on properties worth more than £2m. In total, only 5% of the total loan book is secured on properties valued at greater than £2m with a LTV greater than 65%.

Within the period the Group sold a small number of high exposure problem loans, which drove a reduction in the total problem loan balance from £11.9m as at 30 June 2017, to £6.0m as at 30 June 2018. These loans were highly provided for on an individually assessed basis and were managed on a case by case basis. The sale of these loans drove the higher levels of write-off balances totalling £6.3m during the six months to 30 June 2018 versus the comparable period to 30 June 2017 where write off balances totalled £3.8m (see note 13 Impairment losses).

The Group's total arrears balance remains low, and the portfolio arrears rate, excluding legacy problem loans, remained broadly stable at 1.3% as at 30 June 2018 (30 December 2017: 1.2%). An increase in the past due 3 to 6 months balance was observed during the six months to 30 June 2018 within the Buy-to-Let segment driven by two large exposure cases moving to three months in arrears with low LTV ratios. The Collections and Recoveries Team continue to carefully manage these cases (see note 15 Risk management and financial instruments BTL/SME table). The Group's residential arrears performance remained broadly stable in the period, and negligible arrears were observed across the commercial loan, funding line and development finance portfolios.

During the six months to 30 June 2018, the Group continued to experience low levels of new cases requiring forbearance arrangements, with fewer cases observed during the six months to 30 June 2018 versus first half of 2017. One large forbearance measure drove the end of period balance to be higher as at 30 June 2018 versus 30 June 2017 (see note 15 Forbearance measures undertaken).

Impairment losses increased to £4.3m in the first half of 2018 (H1 2017: £1.4m) representing a loan loss ratio[1] of 11bps on average gross loans (H1 2017: 4bps). On an underlying basis, adjusting for the positive effect of indexing of property valuations during the six months to 30 June 2017, the loan loss ratio would have been consistent with the performance in the first half of 2018 assessed under the IAS 39 approach.

[1] Under IAS 39 provisioning approach in H1 2017 and under IFRS 9 approach in H1 2018

Interim Management Report

Risk Management (continued)

The Group continues to closely monitor impairment coverage levels:

Impairment coverage review (assessed under the IFRS 9 approach)

	30-Jun-18	1-Jan-18
Gross loans and advances to customers £m	8,119.4	7,327.6
Provisions for impairment losses £m	22.9	25.2
Incurred loss remaining[1] £m	7.4	7.9
Coverage ratio versus loans and advances[2] %	0.37	0.45
Coverage ratio versus stage 3 balances (including POCI) [3] %	11.5	13.1

[1] Incurred loss is the expected loss of the portfolio at the point of acquisition and is offset against the modelled future cash flows to derive the effective interest rate for the book. The incurred loss protection is therefore recognised over the life of the book against the unwind of any purchase discount or premium through interest income. Incurred loss remaining is this protection reduced by the cumulative losses observed since acquisition.
[2] Coverage ratio versus loans and advances is the total IFRS 9 provision plus incurred losses remaining versus gross loans and advances.
[3] Coverage ratio versus stage 3 balances is the total IFRS 9 provision plus incurred losses remaining versus stage 3 balances including purchase or originated credit impaired balances, which are held in stage 3 where a lifetime loss impairment balance is held against the exposure for the life of the loan irrespective of whether it is performing and doesn't meet the Group's stage 3 definition.

The coverage ratios with respect to loans and advances and versus stage 3 balances reduced during the period to 30 June 2018 versus the 31 December 2017 predominantly driven by a reduction in total provision balances resulting from the sale of a small number of highly provisioned large problem loan cases within the period, coupled with strong growth in loans and advances to customers. The Group also observed an increase in stage 3 balances driven by two large Buy-to-Let loans moving to three months in arrears within the period, and other three months in arrears balances waiting to satisfy the Group's cure period definition prior to being migrated to stage 1.

Under the IFRS 9 approach, there are three stages which an exposure can be classified into, stage 1, where a 12 months expected credit loss provision is held, and stages 2 and 3 where a lifetime loss provision is held.

Purchased or originated credit impaired ('POCI') exposures are held in stage 3 for the lifetime of the loan, irrespective of whether they have transitioned to a performing status.

For non-POCI accounts which had previously met the Group's stage 3 criteria, a probation cure period must be satisfied prior to an exposure being migrated back to stage 1, where a twelve month loss provision is held.

These factors will result in the Group holding higher provisions than under the IAS 39 provisioning approach, and will also result in a higher level of volatility in the provision charge which is recognised in the Group's income statement.

Liquidity and funding risk management overview

OneSavings Bank's lending strategy is supported by a strong retail savings franchise, which provides the Bank with a sustainable funding platform to support long-term balance sheet growth. This strength is reflected in a high retention level on maturing fixed term products of 96% in the first half of 2018 and strong customer satisfaction scores. In addition, only 8.5% of the Bank's retail deposits as at 30 June 2018 were above the FSCS protection level of £85k. Diversification of funding is also provided by borrowing from the Bank of England under the TFS, which closed in February 2018. OSB had total TFS drawings of £1.5bn as at 30 June 2018.

Risk Management (continued)

The Group continues to operate a conservative approach to managing liquidity with a liquidity ratio of 16.7% as at 30 June 2018 (31 December 2017: 15.2%). The liquidity coverage ratio at 30 June 2018 was 245%, significantly above the regulatory minimum of 100%.

Market risk

The Group has a small amount of foreign exchange exposure, due to the Rupee denominated running costs of its OSBIndia office. Rupee denominated running costs during the period to 30 June 2018 were £2.9m (H1 2017: £2.4m).

Solvency risk management overview

The Group continued to maintain an appropriate level and quality of capital to support its growth objectives and to meet its prudential requirements. The Group maintained a strong capital position in the first half of 2018 with a CET1 ratio of 13.3% (31 December 2017: 13.7%), which remains comfortably in excess of the regulatory requirements.

OSB's capital buffers are subject to active monitoring by the Board and senior management in the context of the Bank's strategic objectives, performance commitments, economic and market conditions, regulatory changes and other risks to which the Bank is exposed.

The Basel Committee published their final Basel III framework in December 2017. A primary objective of the revisions is to reduce excessive variability of risk weighted asset values and improve the comparability of banks' capital ratios.

The Group continues to believe that these new calibrations combined with the final IRB output floor will be beneficial to the Bank's capital requirements. However, we remain cautious until the final rules are adopted in the United Kingdom.

Statement of Directors' Responsibilities

We confirm that to the best of our knowledge:

• the condensed set of financial statements has been prepared in accordance with IAS 34, Interim Financial Reporting, as adopted by the EU;

• the interim management report includes a fair review of the information required by:

(a) DTR 4.2.7R of the Disclosure Guidance and Transparency Rules, being an indication of important events that have occurred during the first six months of the financial year and their impact on the condensed set of financial statements; and a description of the principal risks and uncertainties for the remaining six months of the year; and

(b) DTR 4.2.8R of the Disclosure Guidance and Transparency Rules, being related party transactions that have taken place in the first six months of the current financial year and that have materially affected the financial position or performance of the entity during that period; and any changes in the related party transactions described in the last annual report that could do so.

The Board of Directors, as listed below, represents those individuals responsible for this interim management report:

Graham Allatt
Eric Anstee
Rod Duke
Andy Golding
Margaret Hassall
Mary McNamara
April Talintyre
David Weymouth

By order of the Board

Date: 23 August 2018

Independent Review Report to OneSavings Bank plc

Conclusion

We have been engaged by the Company to review the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2018 which comprises the Consolidated Statement of Profit or Loss, the Consolidated Statement of Other Comprehensive Income, the Consolidated Statement of Financial Position, the Consolidated Statement of Changes in Equity and the Consolidated Statement of Cash Flows and the related explanatory notes.

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2018 is not prepared, in all material respects, in accordance with IAS 34 *Interim Financial Reporting* as adopted by the EU and the Disclosure Guidance and Transparency Rules ('the DTR') of the UK's Financial Conduct Authority ('the UK FCA').

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 *Review of Interim Financial Information Performed by the Independent Auditor of the Entity* issued by the Auditing Practices Board for use in the UK. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. We read the other information contained in the half-yearly financial report and consider whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Directors' responsibilities

The half-yearly financial report is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the half-yearly financial report in accordance with the DTR of the UK FCA.

As disclosed in note 1, the annual financial statements of the Group are prepared in accordance with International Financial Reporting Standards as adopted by the EU. The Directors are responsible for preparing the condensed set of financial statements included in the half-yearly financial report in accordance with IAS 34 as adopted by the EU.

Our responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review.

The purpose of our review work and to whom we owe our responsibilities

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 DTR of the UK FCA. 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.

KPMG LLP
Chartered Accountants
15 Canada Square
London, E14 5GL
23 August 2018

Condensed Consolidated Statement of Profit or Loss

	Note	**Six months ended 30-Jun-18 (Unaudited) £m**	Six months ended 30-Jun-17 (Unaudited) £m
Interest receivable and similar income	2	**190.1**	158.5
Interest payable and similar charges	3	**(54.9)**	(41.4)
Net interest income		**135.2**	117.1
Fair value losses on financial instruments	4	**(1.7)**	(5.6)
Loss on sale of financial instruments		**(0.2)**	-
Fees and commissions receivable		**0.7**	0.8
Fees and commissions payable		**(0.5)**	(0.5)
External servicing fees		**(0.4)**	(1.0)
Total income		**133.1**	110.8
Administrative expenses	5	**(33.7)**	(29.0)
Depreciation and amortisation		**(2.2)**	(1.6)
Impairment losses	13	**(4.3)**	(1.4)
FSCS and other regulatory provisions		**(1.1)**	(0.4)
Profit before taxation		**91.8**	78.4
Taxation	7	**(22.3)**	(19.4)
Profit for the period		**69.5**	59.0
Dividend, pence per share	9	**4.3**	3.5
Earnings per share, pence per share			
Basic	8	**27.5**	24.1
Diluted	8	**27.3**	23.9

The accompanying notes on pages 33 to 62 form an integral part of these condensed financial statements.

Condensed Consolidated Statement of Other Comprehensive Income

	Six months ended 30-Jun-18 (Unaudited) £m	Six months ended 30-Jun-17 (Unaudited) £m
Profit for the period	**69.5**	59.0
Other comprehensive (expense)/income for the period		
Items which may be reclassified to profit or loss:		
Fair value changes on investment securities:		
Arising in the period	**(0.1)**	0.1
Revaluation of foreign operations	**(0.5)**	(0.1)
	(0.6)	-
Total comprehensive income for the period	**68.9**	59.0

The accompanying notes on pages 33 to 62 form an integral part of these condensed financial statements.

Condensed Consolidated Statement of Financial Position

	Note	**As at 30-Jun-18 (Unaudited) £m**	As at 31-Dec-17 (Audited) £m
Assets			
Cash in hand		**0.3**	0.5
Loans and advances to credit institutions		**1,476.7**	1,187.2
Investment securities		**19.1**	19.1
Loans and advances to customers	11	**8,096.5**	7,306.0
Derivative assets		**13.2**	6.1
Fair value adjustments on hedged assets	14	**21.1**	31.9
Deferred taxation asset		**4.4**	5.1
Intangible assets		**7.5**	6.8
Property, plant and equipment		**21.1**	21.5
Other assets		**9.9**	4.9
Total assets		**9,669.8**	8,589.1
Liabilities			
Amounts owed to retail depositors		**7,423.8**	6,650.3
Amounts owed to credit institutions		**1,508.7**	1,250.3
Amounts owed to other customers		**32.6**	25.7
Derivative liabilities		**19.9**	21.8
Current taxation liability		**18.5**	18.3
Other liabilities		**16.4**	16.3
FSCS and other regulatory provisions		**2.5**	1.4
Subordinated liabilities		**10.9**	10.9
Perpetual subordinated bonds		**15.3**	15.3
		9,048.6	8,010.3
Equity			
Share capital		**2.4**	2.4
Share premium		**158.4**	158.4
Retained earnings		**381.4**	337.5
Other reserves		**79.0**	80.5
		621.2	578.8
Total equity and liabilities		**9,669.8**	8,589.1

The accompanying notes on pages 33 to 62 form an integral part of these condensed financial statements.

Condensed Consolidated Statement of Changes in Equity

	Share capital £m	Share premium £m	Capital contribution £m	Transfer reserve £m	Foreign exchange reserve £m	Available-for-sale reserve (IAS 39) £m	FVOCI reserve (IFRS 9) £m	Share-based payment reserve £m	Retained earnings £m	Equity bonds[1] £m	Total £m
At 1 January 2018	**2.4**	**158.4**	**6.4**	**(12.8)**	**(0.2)**	**0.1**	**-**	**5.0**	**337.5**	**82.0**	**578.8**
IFRS 9 transitional adjustment	**-**	**-**	**-**	**-**	**-**	**(0.1)**	**0.1**	**-**	**(3.6)**	**-**	**(3.6)**
Tax on IFRS 9	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**0.7**	**-**	**0.7**
Restated at 1 January 2018	**2.4**	**158.4**	**6.4**	**(12.8)**	**(0.2)**	**-**	**0.1**	**5.0**	**334.6**	**82.0**	**575.9**
Profit for the period	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**69.5**	**-**	**69.5**
Coupon paid on equity bonds	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(3.3)**	**-**	**(3.3)**
Dividends paid	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(22.7)**	**-**	**(22.7)**
Other comprehensive income	**-**	**-**	**-**	**-**	**(0.5)**	**-**	**(0.1)**	**-**	**-**	**-**	**(0.6)**
Share-based payments	**-**	**-**	**0.1**	**-**	**-**	**-**	**-**	**(1.1)**	**2.4**	**-**	**1.4**
Tax recognised in equity	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**0.1**	**0.9**	**-**	**1.0**
At 30 June 2018 (Unaudited)	**2.4**	**158.4**	**6.5**	**(12.8)**	**(0.7)**	**-**	**-**	**4.0**	**381.4**	**82.0**	**621.2**
At 1 January 2017	2.4	157.9	6.2	(12.8)	0.1	-	-	1.9	240.7	22.0	418.4
Profit for the period	-	-	-	-	-	-	-	-	59.0	-	59.0
Coupon paid on equity bonds	-	-	-	-	-	-	-	-	(0.5)	-	(0.5)
Dividends paid	-	-	-	-	-	-	-	-	(18.5)	-	(18.5)
Other comprehensive income	-	-	-	-	(0.1)	0.1	-	-	-	-	-
Share-based payments	-	-	0.1	-	-	-	-	0.9	-	-	1.0
Additional Tier 1 securities issuance	-	-	-	-	-	-	-	-	(0.8)	60.0	59.2
Tax recognised in equity	-	-	-	-	-	-	-	0.6	0.3	-	0.9
At 30 June 2017 (Unaudited)	2.4	157.9	6.3	(12.8)	-	0.1	-	3.4	280.2	82.0	519.5

[1] Equity bonds comprise £22m of Perpetual Subordinated Bonds and £60m of AT1 securities.

Condensed Consolidated Statement of Cash Flows

	Note	**Six months ended 30-Jun-18 (Unaudited) £m**	Six months ended 30-Jun-17 (Unaudited) £m
Cash flows from operating activities			
Profit before tax		**91.8**	78.4
Adjustments for non-cash items	19	**11.7**	10.6
Changes in operating assets and liabilities	19	**(18.8)**	(506.1)
Cash generated from/(used in) operating activities		**84.7**	(417.1)
Interest paid on bonds and subordinated debt		**(0.8)**	(0.7)
Sales of financial instruments		**0.4**	-
Net tax paid		**(19.8)**	(21.5)
Net cash generated from/(used in) operating activities		**64.5**	(439.3)
Cash flows from investing activities			
Purchases of investment securities		**(39.9)**	**-**
Maturity and sales of investment securities		**39.9**	40.0
Purchases of equipment and intangible assets		**(2.5)**	(9.2)
Cash (used in)/generated from investing activities		**(2.5)**	30.8
Cash flows from financing activities			
Bank of England TFS drawdowns		**250.0**	450.0
Coupon paid on equity bonds		**(3.3)**	(0.5)
Dividends paid		**(22.7)**	(18.5)
AT1 securities issuance net of costs		**-**	59.2
Repayment of debt		**-**	(10.7)
Cash generated from financing activities		**224.0**	479.5
Net increase in cash and cash equivalents		**286.0**	71.0
Cash and cash equivalents at the beginning of the period	10	**1,165.9**	485.3
Cash and cash equivalents at the end of the period	10	**1,451.9**	556.3
Movement in cash and cash equivalents		**286.0**	71.0

The accompanying notes on pages 33 to 62 form an integral part of these condensed financial statements.

Notes to the Condensed Consolidated Financial Statements

1. Accounting policies

The principal accounting policies applied in the preparation of the accounts for the Group are set out below.

a) Basis of preparation

These Interim Group Financial Statements have been prepared in accordance with the Disclosure Guidance and Transparency Rules ('DTR') of the FCA and in accordance with International Accounting Standard 34 Interim Financial Reporting as adopted by the EU.

The accounting policies (apart from IFRS 9), presentation and methods of computation are consistent with those applied by the Group in its latest audited financial statements, which were prepared in accordance with International Financial Reporting Standards ('IFRS') as adopted by the EU and interpretations issued by the International Financial Reporting Interpretations Committee. They do not include all the information required for a complete set of IFRS financial statements. However, selected explanatory notes are included to explain events and transactions that are significant to an understanding of the changes in the Group's financial position and performance since the last Interim Report as at 30 June 2017 and last Annual Report for the year ended 31 December 2017.

The comparative figures for the year ended 31 December 2017 are not the Group's statutory accounts for that financial year. The statutory accounts for the year ended 31 December 2017 have been delivered to the Registrar of Companies in England and Wales in accordance with section 447 of the Companies Act 2006. The Auditor has reported on those accounts. Their report was unqualified; did not include a reference to any matters to which the Auditor drew attention by way of emphasis without qualifying their report, and did not contain a statement under section 498(2) or (3) of the Companies Act 2006.

These interim financial statements were authorised for issue by the Company's Board of Directors on 23 August 2018.

b) Accounting standards

Implementation of IFRS 9
The Group implemented IFRS 9 on 1 January 2018. The new standard has two key areas of change from the accounting policies applied in the 2017 Annual Report: classification and measurement and impairment. The Group continues to apply IAS 39 for fair value hedge accounting.

i. Classification and measurement
The Group classifies financial instruments based on the business model and the contractual cash flow characteristics of the financial instruments. The Group classifies financial assets into one of three measurement categories:

- **Amortised cost** – assets held in a business model to hold financial assets in order to collect contractual cash flows, where the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest ('SPPI') on the principal amount outstanding.
- **Fair value through other comprehensive income ('FVOCI')** – assets held in a business model which collects contractual cash flows and sells financial assets where the contractual terms of the financial assets give rise on specified dates to cash flows that are SPPI on the principal amount outstanding. The Group only measures investment securities under this category, which were previously classified as available-for-sale under IAS 39.
- **Fair value through profit or loss ('FVPL')** – assets not measured at amortised cost or FVOCI. The Group only measures derivative assets under this category.

IFRS 9 has not changed the classification or measurement of the Group's financial liabilities.

The Group has not irrevocably designated any financial assets or liabilities as FVPL in order to eliminate or significantly reduce a measurement or recognition inconsistency.

1. Accounting policies (continued)

ii. Derecognition

The Group derecognises financial assets when the contractual rights to the cash flows expire or the Group transfers substantially all the risks and rewards of ownership of the financial asset.

The forbearance measures offered by the Group are considered a modification event, as the contractual cash flows are renegotiated or otherwise modified. The Group considers the renegotiated or modified cash flows are not wholly different from the contractual cash flows, and does not consider forbearance measures to give rise to a derecognition event.

iii. Expected credit loss ('ECL')

IFRS 9 replaced the IAS 39 'incurred loss' impairment recognition framework with a three stage expected credit loss approach. The three impairment stages under IFRS 9 are as follows:

- **Stage 1** – entities are required to recognise a 12 month ECL allowance on initial recognition.
- **Stage 2** – a lifetime loss allowance is held for assets where a significant increase in credit risk has been identified since initial recognition. The assessment of whether credit risk has increased significantly since initial recognition is performed for each reporting period for the life of the loan.
- **Stage 3** – requires objective evidence that an asset is credit impaired, at which point a lifetime ECL allowance is required.

Individual assessment

The Group has retained the individual assessment provisioning process for loans over £0.5m which are more than three months in arrears, where LPA receivers are appointed, the property is taken into possession or there are any other events that suggest a high probability of credit loss, as disclosed on page 115 of the 2017 Annual Report. The Group applies its IFRS 9 models to all loans with no individually assessed provision.

Measurement of ECL

The assessment of credit risk and the estimation of ECL are unbiased and probability weighted. ECL is measured on either a 12 month (stage 1) or lifetime (stage 2) basis depending on whether a significant increase in credit risk has occurred since initial recognition or where an account meets the Group's definition of default (stage 3).

The ECL calculation is a product of an individual loan's probability of default ('PD'), exposure at default ('EAD') and loss given default ('LGD') discounted at the effective interest rate ('EIR'). The ECL drivers of PD, EAD and LGD are modelled at an account level. The assessment of whether a significant increase in credit risk has occurred is based on the lifetime PD estimate.

Significant increase in credit risk ('SICR') (movement to stage 2)

The Group's transfer criteria determines what constitutes a significant increase in credit risk, which results in an exposure being moved from stage 1 to stage 2.

At the point of recognition a loan is assigned a lifetime PD estimate. For each monthly reporting date thereafter an updated lifetime PD estimate is computed for the life of the loan. The Group's transfer criteria analyses relative changes in lifetime PD versus the origination lifetime PD, where if prescribed thresholds are met, an account will be transferred from stage 1 to stage 2.

1. Accounting policies (continued)

The Group's Risk function constantly monitors the ongoing appropriateness of the transfer criteria, where any proposed amendments will be reviewed and approved by the Group's Management Committees and the Risk and Audit Committees at least semi-annually or more frequently if required.

IFRS 9 includes a rebuttable presumption that if an account is more than 30 days past due it has experienced a significant increase in credit risk. The Group considers more than 30 days past due to be an appropriate back stop measure and therefore has not rebutted this presumption.

A borrower will move back into stage 1 where the SICR definition is no longer satisfied.

Definition of default (movement to stage 3)

The Group uses a number of quantitative and qualitative criteria to determine whether an account meets the definition of default and therefore moves to stage 3. The criteria currently include:

- The rebuttable assumption that more than 90 days past due is an indicator of default. The Group has not rebutted this assumption and therefore deems more than 90 days past due as an indicator of default. This also ensures alignment between the Group's Internal Ratings Based Models and the Basel/Regulatory definition of default.
- The Group has also deemed it appropriate to classify accounts that have moved into an unlikeliness to pay position, which includes forbearance or repossession.

A borrower will move out of stage 3 when their credit risk improves such that they roll back to zero days past due and remain there for an internally approved period. The borrower will move to stage 1 or stage 2 dependent on whether the SICR applies.

Forward looking macroeconomic scenarios

IFRS 9 requires firms to consider the risk of default and impairment loss taking into account expectations of economic changes that are reasonable.

The Group uses a bespoke macroeconomic model to determine the most significant factors which may influence the likelihood of an exposure defaulting in the future. At present, the most significant macroeconomic factors relate to the house price index ('HPI'), unemployment and the Bank of England Base Rate.

The Group has derived an approach for factoring probability weighted macroeconomic forecasts into ECL calculations, adjusting PD and LGD estimates. An account's lifetime PD is impacted by the probability weighted macroeconomic scenario and therefore impacts whether an account meets the Group's SICR transfer criteria moving the exposure between stage 1 and stage 2. The macroeconomic scenarios feed directly into the ECL calculation, as the adjusted PD, lifetime PD and LGD estimates are used within the individual account ECL allowance calculations.

The Group currently does not have an in-house economics function and therefore sources economic forecasts from an appropriately qualified third party. The Group will consider a minimum of three probability weighted scenarios, including base, upside and downside scenarios. However, the Group will constantly monitor the ongoing appropriateness of its approach referencing industry best practise.

The base case is also utilised within the Group's impairment forecasting process which in turn feeds the wider business planning processes. This economic forecast is also used within analysis to set the Group's credit risk appetite thresholds and limits.

Notes to the Condensed Consolidated Financial Statements (continued)

1. Accounting policies (continued)

Expected life

IFRS 9 requires lifetime expected credit losses to be measured over the expected life. Currently the Group considers the loan's behavioural life is equal to the full mortgage term. This approach will continue to be monitored and enhanced if and when deemed appropriate.

Purchase or originated credit impaired ('POCI')

Acquired loans that meet OSB's definition of default (90 days past due or an unlikeliness to pay position) at acquisition are treated as a POCI asset. These assets will attract a lifetime ECL allowance over the full term of the loan, even when the loan no longer meets the definition of default post acquisition. The Group does not provide for or have any own originated credit impaired loans.

All other accounting policies used are consistent with those set out on pages 112 to 122 of the 2017 Annual Report.

b) Going concern

The Board undertakes regular rigorous assessments of whether the Group is a going concern in light of current economic conditions and all available information about future risks and uncertainties.

Projections for the Group have been prepared, covering its future performance, capital and liquidity for a period in excess of 12 months from the date of approval of these financial statements including stress scenarios. These projections show that the Group has sufficient capital and liquidity to continue to meet its regulatory capital requirements as set out by the PRA.

The Board has therefore concluded that the Group has sufficient resources to continue in operational existence for a period in excess of 12 months and as a result, it is appropriate to prepare these Interim Group Financial Statements on a going concern basis.

c) Segmental reporting

The Group segments its lending by product, focusing on the customer need and reason for a loan. The Group operates under two segments: BTL/SME and Residential mortgages.

d) Judgements and estimates

The preparation of the Interim Report requires management to make estimates and assumptions that affect the reported income and expense, assets and liabilities and disclosure of contingencies at the date of the Interim Report. Although these estimates and assumptions are based on management's best judgement at that date, actual results may differ from these estimates. Estimates and assumptions are reviewed on an ongoing basis. Revisions to estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Notes to the Condensed Consolidated Financial Statements (continued)

1. Accounting policies (continued)

There have been no significant changes in the basis upon which estimates have been determined for loan book acquisition accounting and income recognition and EIR calculations compared to those applied at 31 December 2017, as described on pages 122 to 123 of the 2017 Annual Report.

The implementation of IFRS 9 on 1 January 2018 has changed the judgements and estimates used for loan book impairments, with the new ECL calculations underpinned by a suite of bespoke PD, LGD and EAD models using segmentation based on the underlying characteristics of the Group's loan portfolios.

PD models – the Group uses a number of PD models to assess the likelihood of a default event occurring within the next 12 months, utilising internal and external credit bureau information. The Group also computes a lifetime PD estimate for each loan exposure once recognised, underpinned by the 12 month PD estimate.

LGD model – the Group uses a single LGD model, which includes a number of judgement and estimate inputs, including propensity to go to possession given default ('PGD'), forced sale discount ('FSD'), time to sale ('TTS') and sale cost estimates.

EAD model – The Group uses a single EAD model to cover all applicable exposures.

2. Interest receivable and similar income

	Six months ended 30-Jun-18 (Unaudited) £m	Restated Six months ended 30-Jun-17 (Unaudited) £m
At amortised cost:		
On BTL/SME mortgages[1]	**146.9**	114.3
On Residential mortgages[1]	**43.9**	47.8
On investment securities	**0.1**	-
On other liquid assets	**3.1**	0.6
At fair value through profit or loss:		
Net expense on derivative financial instruments - financing activities	**(3.9)**	(4.2)
	190.1	158.5

[1] The comparative information for residential mortgages has been restated following a change in allocation, with an additional £2.1m of interest income disclosed compared to the previously reported balance. This has decreased the BTL/SME mortgages interest income by £2.1m.

3. Interest payable and similar charges

	Six months ended 30-Jun-18 (Unaudited) £m	Six months ended 30-Jun-17 (Unaudited) £m
On retail deposits	**50.3**	41.4
On Perpetual Subordinated Bonds	**0.4**	0.4
On subordinated liabilities	**0.4**	0.3
On wholesale borrowings	**3.4**	1.1
Net expense/(income) on derivative financial instruments - investment activities	**0.4**	(1.8)
	54.9	41.4

4. Fair value losses on financial instruments

	Six months ended 30-Jun-18 (Unaudited) £m	Six months ended 30-Jun-17 (Unaudited) £m
Fair value changes in hedged assets	**(8.3)**	(5.9)
Hedging of assets	**9.3**	6.5
Fair value changes in hedged liabilities	**-**	1.2
Hedging of liabilities	**(0.2)**	(1.1)
Ineffective portion of hedges	**0.8**	0.7
Amortisation of fair value adjustments on hedged assets	**(2.5)**	(6.2)
Net gains on unmatched swaps	**0.2**	-
Debit and credit valuation adjustment	**(0.2)**	(0.1)
	(1.7)	(5.6)

Amortisation of fair value adjustments on hedged assets relates to hedged assets and liabilities where the hedges were terminated before maturity and were effective at the point of termination.

The debit valuation adjustment ('DVA') is calculated on the Group's derivative liabilities and represents exposure of their holders to the risk of the Group's default. The credit valuation adjustment ('CVA') reflects the Group's risk of the counterparty's default.

Notes to the Condensed Consolidated Financial Statements (continued)

5. Administrative expenses

	Six months ended 30-Jun-18 (Unaudited) £m	Six months ended 30-Jun-17 (Unaudited) £m
Staff costs[1]	**20.4**	17.2
Facilities costs	**3.1**	1.2
Marketing costs	**1.0**	1.2
Support costs	**3.5**	3.1
Professional fees	**2.6**	2.5
Other costs[2]	**3.1**	3.8
	33.7	29.0

[1] Staff costs include £0.1m (2017: £0.1m) relating to the IPO share awards and £1.2m (2017: £0.9m) of share-based executive and management compensation.
[2] Other costs mainly consist of irrecoverable VAT expense.

The average number of persons employed by the Group (including executive Directors) during the first half of 2018 was 956 (first half of 2017: 775).

6. Share-based payments

The Group operates the following equity-settled share-based payment schemes, full details of which are provided on pages 126 to 128 of the 2017 Annual Report:

- IPO Share Awards
- Sharesave Scheme ('SAYE')
- Deferred Share Bonus Plan ('DSBP')
- Performance Share Plan ('PSP')

The movement in the number of share awards and their weighted average exercise prices are presented below:

	IPO share awards	**Sharesave Scheme**		**Deferred Share Bonus Plan**	**Performance Share Plan**
(Unaudited)	**Number**	**Number**	**Weighted average exercise price, (£)**	**Number**	**Number**
At 1 January 2018	**652,198**	**732,341**	**2.60**	**1,186,762**	**1,589,030**
Granted	**-**	**-**	**-**	**376,231**	**708,146**
Exercised/vested	**(577,661)**	**(6,650)**	**1.89**	**(298,631)**	**(559,179)**
Forfeited	**-**	**(26,149)**	**2.80**	**-**	**-**
At 30 June 2018	**74,537**	**699,542**	**2.60**	**1,264,362**	**1,737,997**
Exercisable at					
At 30 June 2018	**-**	**-**	**-**	**-**	**-**

Notes to the Condensed Consolidated Financial Statements (continued)

6. Share-based payments (continued)

The weighted average market price at exercise for the IPO share awards exercised during 2018 was 408 pence per share.

The weighted average market price at exercise for the SAYE options exercised during 2018 was 393 pence per share.

The market price at vesting for the DSBP and PSP awards was 372 pence per share.

7. Taxation

	Six months ended 30-Jun-18 (Unaudited) £m	Six months ended 30-Jun-17 (Unaudited) £m
Corporation tax	**(22.3)**	(18.9)
Tax in respect of prior periods	**-**	(0.5)
Total taxation	**(22.3)**	(19.4)

The taxation on the Group's profit before taxation differs from the theoretical amount that would arise using the weighted average taxation rate applicable to profits of the Group as follows:

	Six months ended 30-Jun-18 (Unaudited) £m	Six months ended 30-Jun-17 (Unaudited) £m
Profit before taxation	**91.8**	78.4
Profit multiplied by the weighted average rate of corporation tax in the UK during 2018 of 19% (2017: 19.25%)	**(17.4)**	(15.1)
Bank surcharge	**(4.6)**	(3.8)
Taxation effects of:		
Expenses not deductible for taxation purposes	**(0.2)**	-
Adjustments in respect of earlier years	**-**	(0.5)
Tax adjustments in respect of share-based payments	**0.1**	0.2
Impact of tax losses carried forward	**-**	0.1
Timing differences on capital items	**(0.2)**	(0.4)
Other	**-**	0.1
Total taxation charge	**(22.3)**	(19.4)

A reduction in the UK corporation tax rate from 20% to 19% (effective from 1 April 2017) and a further reduction to 18% (effective from 1 April 2020) were substantively enacted on 26 October 2015. An additional reduction to 17% (effective 1 April 2020) was substantively enacted on 6 September 2016. This will reduce the Group’s future tax charge accordingly.

Notes to the Condensed Consolidated Financial Statements (continued)

8. Earnings per share

Earnings per share ('EPS') are based on the profit for the period and the number of ordinary shares in issue. Basic EPS are calculated by dividing profit attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the period. Diluted earnings per share take into account share awards and options which can be converted to ordinary shares.

For the purpose of calculating earnings per share, profit attributable to ordinary shareholders is arrived at by adjusting profit for the period for the after tax amount of the coupon on the Perpetual Subordinated Bonds ('PSBs') and AT1 Securities classified as equity:

	Six months ended 30-Jun-18 (Unaudited) £m	Six months ended 30-Jun-17 (Unaudited) £m
Profit for the period	**69.5**	59.0
Adjustments:		
Coupon on equity bonds	**(3.3)**	(0.5)
Tax on coupon on equity bonds	**0.9**	0.1
Profit attributable to ordinary shareholders	**67.1**	58.6

Earnings per share are summarised in the table below:

	Six months ended 30-Jun-18 (Unaudited)	Six months ended 30-Jun-17 (Unaudited)
Weighted average number of shares, millions		
Basic	**244.0**	243.1
Diluted	**245.9**	245.1
Earnings per share, pence per share		
Basic	**27.5**	24.1
Diluted	**27.3**	23.9

9. Dividends

During the period, the Bank paid the following dividends:

	Six months ended 30-Jun-18 (Unaudited)		Six months ended 30-Jun-17 (Unaudited)	
	£m	**Pence per share**	£m	Pence per share
Final dividend for the prior year	**22.7**	**9.3**	18.5	7.6

9. Dividends (continued)

A summary of the Bank's distributable reserves from which dividends can be paid are shown below:

	Six months ended 30-Jun-18 (Unaudited) £m	Year ended 31-Dec-17 (Audited) £m
Net assets	**621.2**	475.8
Less:		
- Share capital	**(2.4)**	(2.4)
- Share premium	**(158.4)**	(158.4)
- Other non-distributable reserves [1]	**(91.8)**	(93.1)
Distributable reserves	**368.6**	221.9

[1] Other non-distributable reserves include the capital contribution, equity bonds, foreign exchange reserve, FVOCI reserve and share-based payment reserve.

The Directors propose an interim dividend for the first half of 2018 of 4.3 pence per share, based on one third of the total 2017 dividend of 12.8 pence per share, payable on 2 November 2018 with an ex-dividend date of 11 October 2018 and a record date of 12 October 2018. This dividend is not reflected in these financial statements as it was not declared as at the reporting date.

10. Cash and cash equivalents

	As at 30-Jun-18 (Unaudited) £m	As at 31-Dec-17 (Audited) £m	As at 30-Jun-17 (Unaudited) £m	As at 31-Dec-16 (Audited) £m
Cash in hand	**0.3**	0.5	0.4	0.4
Unencumbered loans and advances to credit institutions	**1,451.6**	1,165.4	555.9	402.3
Investment securities with maturity less than 3 months	**-**	-	-	82.6
	1,451.9	1,165.9	556.3	485.3

Unencumbered loans and advances to credit institutions excludes £17.3m (30 June 2017: £9.3m) held in the cash ratio deposit with the Bank of England and excludes £7.8m (30 June 2017: £14.1m) of encumbered assets in the form of cash margin collateral paid in relation to the Group's derivatives.

11. Loans and advances to customers

	As at 30-Jun-18 (Unaudited)			As at 31-Dec-17 (Audited)		
	BTL/SME £m	**Residential £m**	**Total £m**	BTL/SME £m	Residential £m	Total £m
Gross carrying amount						
Stage 1	**6,243.8**	**1,315.5**	**7,559.3**	-	-	-
Stage 2	**188.8**	**106.3**	**295.1**	-	-	-
Stage 3	**83.4**	**120.3**	**203.7**	-	-	-
Stage 3 (POCI)	**0.3**	**61.0**	**61.3**	-	-	-
IAS 39	**-**	**-**	**-**	5,654.1	1,673.5	7,327.6
	6,516.3	**1,603.1**	**8,119.4**	5,654.1	1,673.5	7,327.6
Expected credit loss						
Stage 1	**(7.9)**	**(1.8)**	**(9.7)**	-	-	-
Stage 2	**(1.0)**	**(1.1)**	**(2.1)**	-	-	-
Stage 3	**(3.9)**	**(5.1)**	**(9.0)**	-	-	-
Stage 3 (POCI)	**-**	**(1.9)**	**(1.9)**	-	-	-
Undrawn loan facilities	**(0.2)**	**-**	**(0.2)**	-	-	-
IAS 39	**-**	**-**	**-**	(13.2)	(8.4)	(21.6)
	(13.0)	**(9.9)**	**(22.9)**	(13.2)	(8.4)	(21.6)
Net carrying amount	**6,503.3**	**1,593.2**	**8,096.5**	5,640.9	1,665.1	7,306.0

Notes to the Condensed Consolidated Financial Statements (continued)

12. Expected credit losses

A reconciliation of the Group's ECLs movement during the period is shown below:

Total (Unaudited)	Stage 1 £m	Stage 2 £m	Stage 3 £m	Stage 3 (POCI) £m	IAS 39 impairments £m	Total £m
At 31 December 2017	-	-	-	-	21.6	21.6
IFRS 9 transitional adjustment	7.8	2.3	13.3	1.8	(21.6)	3.6
At 1 January 2018	7.8	2.3	13.3	1.8	-	25.2
Originations and acquisitions	0.7	0.1	-	-	-	0.8
Modifications	-	-	-	-	-	-
Disposals and write-offs	(0.1)	(0.1)	(6.6)	(0.1)	-	(6.9)
Remeasurement of loss allowance	(0.6)	0.9	2.3	0.2	-	2.8
Transfers:						
- To Stage 1	1.2	(0.8)	(0.4)	-	-	-
- To Stage 2	(0.1)	0.1	-	-	-	-
- To Stage 3	-	(0.4)	0.4	-	-	-
- To Stage 3 (POCI)	-	-	-	-	-	-
Changes in assumptions and model parameters [1]	1.0	-	-	-	-	1.0
At 30 June 2018	9.9	2.1	9.0	1.9	-	22.9

[1] The Group continues to track the predictability of all IFRS 9 models, and an enhancement was made during the six months to 30 June 2018 to ensure that model performance continued to meet internally defined performance thresholds.

BTL/SME (Unaudited)	Stage 1 £m	Stage 2 £m	Stage 3 £m	Stage 3 (POCI) £m	IAS 39 impairments £m	Total £m
At 31 December 2017	-	-	-	-	13.2	13.2
IFRS 9 transitional adjustment	6.6	1.1	8.6	-	(13.2)	3.1
At 1 January 2018	6.6	1.1	8.6	-	-	16.3
Originations and acquisitions	0.6	0.1	-	-	-	0.7
Modifications	-	-	-	-	-	-
Disposals and write-offs	-	(0.1)	(5.9)	-	-	(6.0)
Remeasurement of loss allowance	(0.5)	0.3	1.3	-	-	1.1
Transfers:						
- To Stage 1	0.5	(0.3)	(0.2)	-	-	-
- To Stage 2	-	-	-	-	-	-
- To Stage 3	-	(0.1)	0.1	-	-	-
- To Stage 3 (POCI)	-	-	-	-	-	-
Changes in assumptions and model parameters	0.9	-	-	-	-	0.9
At 30 June 2018	8.1	1.0	3.9	-	-	13.0

Notes to the Condensed Consolidated Financial Statements
(continued)

12. Expected credit losses (continued)

Residential (Unaudited)	Stage 1 £m	Stage 2 £m	Stage 3 £m	Stage 3 (POCI) £m	IAS 39 impairments £m	Total £m
At 31 December 2017	**-**	**-**	**-**	**-**	**8.4**	**8.4**
IFRS 9 transitional adjustment	**1.2**	**1.2**	**4.7**	**1.8**	**(8.4)**	**0.5**
At 1 January 2018	**1.2**	**1.2**	**4.7**	**1.8**	**-**	**8.9**
Originations and acquisitions	**0.1**	**-**	**-**	**-**	**-**	**0.1**
Modifications	**-**	**-**	**-**	**-**	**-**	**-**
Disposals and write-offs	**(0.1)**	**-**	**(0.7)**	**(0.1)**	**-**	**(0.9)**
Remeasurement of loss allowance	**(0.1)**	**0.6**	**1.0**	**0.2**	**-**	**1.7**
Transfers:						
- To Stage 1	**0.7**	**(0.5)**	**(0.2)**	**-**	**-**	**-**
- To Stage 2	**(0.1)**	**0.1**	**-**	**-**	**-**	**-**
- To Stage 3	**-**	**(0.3)**	**0.3**	**-**	**-**	**-**
- To Stage 3 (POCI)	**-**	**-**	**-**	**-**	**-**	**-**
Changes in assumptions and model parameters	**0.1**	**-**	**-**	**-**	**-**	**0.1**
At 30 June 2018	**1.8**	**1.1**	**5.1**	**1.9**	**-**	**9.9**

The movement in the 2017 provision for impairment losses under IAS 39 is shown below:

Specific	BTL/SME £m	Residential £m	Total £m
At 1 January 2017	16.8	6.6	23.4
Write-offs in period	(4.8)	(3.0)	(7.8)
Charge for the period net of recoveries	0.7	3.3	4.0
At 31 December 2017 (Audited)	12.7	6.9	19.6
Collective			
At 1 January 2017	0.4	1.2	1.6
Write-offs in period	-	-	-
Charge for the period net of recoveries	0.1	0.3	0.4
At 31 December 2017 (Audited)	0.5	1.5	2.0
Total			
At 1 January 2017	17.2	7.8	25.0
Write-offs in period	(4.8)	(3.0)	(7.8)
Charge for the period net of recoveries	0.8	3.6	4.4
At 31 December 2017 (Audited)	13.2	8.4	21.6

Notes to the Condensed Consolidated Financial Statements (continued)

13. Impairment losses

	Six months ended 30-Jun-18 (Unaudited) £m	Six months ended 30-Jun-17 (Unaudited) £m
Write-offs in period [1]	**6.3**	3.8
Decrease in provision [2]	**(2.0)**	(2.4)
	4.3	1.4

[1] The sale of properties securing a small number of high exposure problem loan cases within the period drove an increase in total write-off balances during the six months to the 30 June 2018. Additional information is disclosed in the Risk Management on page 23.
[2] The decrease in provision excludes £0.3m of provision on the personal loan portfolio which was sold in June 2018.

14. Fair value adjustments on hedged items

	As at 30-Jun-18 (Unaudited) £m	As at 31-Dec-17 (Audited) £m
Hedged assets		
Current hedge relationships	**7.6**	15.9
Cancelled hedge relationships	**13.5**	16.0
	21.1	31.9

The fair value adjustments on hedged assets in respect of cancelled hedge relationships represent the fair value adjustment for interest rate risk on legacy long-term fixed rate mortgages (c.25 years at origination) where the interest rate swap hedges were terminated before maturity and were effective at the point of termination.

15. Risk management and financial instruments

The tables below are a summary of the Group's risk management and financial instruments disclosures, of which a complete disclosure for the year ended 31 December 2017 is included in the Group's 2017 Annual Report. The tables do not represent all risks the Group is exposed to and should be read in conjunction with the Risk Management Report above.

15. Risk management and financial instruments (continued)

Credit risk

The following table shows the Group's maximum exposure to credit risk and the impact of collateral held as security, capped at the gross exposure amount, by impairment stage:

	As at 30-Jun-18 (Unaudited)		As at 31-Dec-17 (Audited)	
	Gross carrying amount £m	**Capped collateral held £m**	Gross carrying amount £m	Capped collateral held £m
Stage 1	**7,559.3**	**7,552.5**	-	-
Stage 2	**295.1**	**294.6**	-	-
Stage 3	**203.7**	**202.9**	-	-
Stage 3 (POCI)	**61.3**	**61.3**	-	-
IAS 39	**-**	**-**	7,327.6	7,313.5
	8,119.4	**8,111.3**	7,327.6	7,313.5

The Group's collateral held in relation to BTL/SME and Residential first and second charge mortgage loans is property, based in the UK and the Channel Islands. The Group's collateral held in relation to funding lines is predominantly property. The Group's personal loan portfolio, which was sold in June 2018, was unsecured.

The Group uses indexed loan-to-value ('LTV') ratios to assess the quality of the uncapped collateral held. Property values are updated to reflect changes in the house price index.

LTV analysis by band for all loans:

	As at 30-Jun-18 (Unaudited)			
	BTL/SME £m	**Residential £m**	**Total £m**	**%**
Band				
0% - 50%	**863.9**	**788.7**	**1,652.6**	**20**
50% - 60%	**999.4**	**252.1**	**1,251.5**	**15**
60% - 70%	**1,854.8**	**208.8**	**2,063.6**	**25**
70% - 80%	**2,373.8**	**176.7**	**2,550.5**	**32**
80% - 90%	**404.4**	**123.9**	**528.3**	**7**
90% - 100%	**8.4**	**33.3**	**41.7**	**1**
>100%	**11.6**	**19.6**	**31.2**	**-**
Total loans before provisions	**6,516.3**	**1,603.1**	**8,119.4**	**100**

Notes to the Condensed Consolidated Financial Statements (continued)

15. Risk management and financial instruments (continued)

	As at 31-Dec-17 (Audited)			
	BTL/SME £m	Residential £m	Total £m	%
Band				
0% - 50%	747.6	808.3	1,555.9	21
50% - 60%	960.5	260.6	1,221.1	16
60% - 70%	1,606.8	228.3	1,835.1	25
70% - 80%	1,939.4	184.5	2,123.9	29
80% - 90%	359.1	138.2	497.3	7
90% - 100%	15.1	31.6	46.7	1
>100%	24.5	22.0	46.5	1
Total mortgages before provisions	5,653.0	1,673.5	7,326.5	100
Personal loans[1]	1.1	-	1.1	-
Total loans before provisions	5,654.1	1,673.5	7,327.6	100

[1] The Group sold its personal loan portfolio in June 2018, recognising a loss on sale of £0.2m.

LTV analysis by band for BTL/SME:

	As at 30-Jun-18 (Unaudited)				
	Buy-to-Let £m	**Commercial £m**	**Residential development £m**	**Funding lines £m**	**Total £m**
Band					
0% - 50%	**634.7**	**64.8**	**120.2**	**44.2**	**863.9**
50% - 60%	**908.1**	**60.0**	**17.6**	**13.7**	**999.4**
60% - 70%	**1,648.3**	**151.4**	**8.1**	**47.0**	**1,854.8**
70% - 80%	**2,205.4**	**147.4**	**5.3**	**15.7**	**2,373.8**
80% - 90%	**387.8**	**2.0**	**-**	**14.6**	**404.4**
90% - 100%	**8.0**	**0.4**	**-**	**-**	**8.4**
>100%	**9.0**	**2.6**	**-**	**-**	**11.6**
Total loans before provisions	**5,801.3**	**428.6**	**151.2**	**135.2**	**6,516.3**

Notes to the Condensed Consolidated Financial Statements
(continued)

15. Risk management and financial instruments (continued)

	As at 31-Dec-17 (Audited)				
	Buy-to-Let £m	Commercial £m	Residential development £m	Funding lines £m	Total £m
Band					
0% - 50%	567.0	66.8	88.3	25.5	747.6
50% - 60%	841.2	62.3	42.8	14.2	960.5
60% - 70%	1,437.7	120.6	8.9	39.6	1,606.8
70% - 80%	1,811.5	112.8	3.9	11.2	1,939.4
80% - 90%	343.1	2.5	-	13.5	359.1
90% - 100%	14.2	0.4	-	0.5	15.1
>100%	19.1	5.4	-	-	24.5
Total mortgages before provisions	5,033.8	370.8	143.9	104.5	5,653.0
Personal loans					1.1
Total loans before provisions					5,654.1

LTV analysis by band for Residential:

	As at 30-Jun-18 (Unaudited)			
	First charge £m	**Second charge £m**	**Funding lines £m**	**Total £m**
Band				
0% - 50%	**642.3**	**129.2**	**17.2**	**788.7**
50% - 60%	**165.5**	**85.6**	**1.0**	**252.1**
60% - 70%	**128.8**	**79.0**	**1.0**	**208.8**
70% - 80%	**124.4**	**50.6**	**1.7**	**176.7**
80% - 90%	**98.4**	**24.4**	**1.1**	**123.9**
90% - 100%	**23.6**	**9.1**	**0.6**	**33.3**
>100%	**7.2**	**12.0**	**0.4**	**19.6**
Total loans before provisions	**1,190.2**	**389.9**	**23.0**	**1,603.1**

	As at 31-Dec-17 (Audited)			
	First charge £m	Second charge £m	Funding lines £m	Total £m
Band				
0% - 50%	647.1	150.2	11.0	808.3
50% - 60%	163.3	94.2	3.1	260.6
60% - 70%	147.9	78.4	2.0	228.3
70% - 80%	136.1	47.2	1.2	184.5
80% - 90%	116.4	21.6	0.2	138.2
90% - 100%	22.2	9.3	0.1	31.6
>100%	7.6	14.4	-	22.0
Total loans before provisions	1,240.6	415.3	17.6	1,673.5

15. Risk management and financial instruments (continued)

Analysis of mortgage portfolio by arrears and collateral held

The table below provides further information on collateral, capped at the value of each individual mortgage, over the mortgage portfolio by payment due status for each impairment stage:

	As at 30-Jun-18 (Unaudited)	
	Loan balance £m	**Capped collateral £m**
Stage 1		
Not past due	**7,445.2**	**7,438.4**
Past due < 1 month	**114.1**	**114.1**
	7,559.3	**7,552.5**
Stage 2		
Not past due	**126.0**	**125.5**
Past due < 1 month	**111.1**	**111.1**
Past due 1 to 3 months	**58.0**	**58.0**
	295.1	**294.6**
Stage 3		
Not past due	**49.4**	**49.4**
Past due < 1 month	**21.9**	**21.9**
Past due 1 to 3 months	**42.2**	**42.2**
Past due 3 to 6 months	**45.5**	**45.5**
Past due 6 to 12 months	**26.5**	**26.4**
Past due over 12 months	**9.6**	**9.5**
Possessions	**8.6**	**8.0**
	203.7	**202.9**
Stage 3 (POCI)		
Not past due	**19.9**	**19.9**
Past due < 1 month	**6.4**	**6.4**
Past due 1 to 3 months	**7.5**	**7.5**
Past due 3 to 6 months	**8.6**	**8.6**
Past due 6 to 12 months	**8.6**	**8.6**
Past due over 12 months	**10.3**	**10.3**
Possessions	**-**	**-**
	61.3	**61.3**
Total loans before provisions	**8,119.4**	**8,111.3**

15. Risk management and financial instruments (continued)

The table below provides further information on collateral, capped at the value of each individual mortgage, over the mortgage portfolio by payment due status for IAS 39 impairments, where impaired is defined as loans with a specific provision against them:

	Group As at 31-Dec-17	
	Loan balance £m	Capped collateral £m
Not impaired:		
Not past due	6,792.9	6,784.8
Past due < 1 month	307.1	307.1
Past due 1 to 3 months	102.0	101.9
Past due 3 to 6 months	20.9	20.9
Past due 6 to 12 months	14.1	14.1
Past due over 12 months	7.6	7.6
Possessions	0.5	0.5
	7,245.1	7,236.9
Impaired:		
Not past due	12.3	7.7
Past due < 1 month	0.8	0.8
Past due 1 to 3 months	2.2	2.1
Past due 3 to 6 months	23.7	23.7
Past due 6 to 12 months	16.3	16.3
Past due over 12 months	14.5	14.4
Possessions	11.6	11.6
	81.4	76.6
Total mortgages before provisions	7,326.5	7,313.5
Personal loans	1.1	
Total loans before provisions	7,327.6	

Notes to the Condensed Consolidated Financial Statements (continued)

15. Risk management and financial instruments (continued)

The tables below show the payment due status of the Group's loan portfolios by operating segment:

	As at 30-Jun-18 (Unaudited)				
BTL/SME	**Buy-to-Let £m**	**Commercial £m**	**Residential development £m**	**Funding lines £m**	**Total £m**
Stage 1					
Not past due	5,517.4	399.1	151.2	135.2	6,202.9
Past due < 1 month	39.1	1.8	-	-	40.9
	5,556.5	400.9	151.2	135.2	6,243.8
Stage 2					
Not past due	74.4	19.8	-	-	94.2
Past due < 1 month	65.1	3.7	-	-	68.8
Past due 1 to 3 months	23.9	1.9	-	-	25.8
	163.4	25.4	-	-	188.8
Stage 3					
Not past due	25.7	0.8	-	-	26.5
Past due < 1 month	8.0	-	-	-	8.0
Past due 1 to 3 months	15.6	0.6	-	-	16.2
Past due 3 to 6 months	18.0	0.5	-	-	18.5
Past due 6 to 12 months	8.3	-	-	-	8.3
Past due over 12 months	1.5	0.1	-	-	1.6
Possessions	4.3	-	-	-	4.3
	81.4	2.0	-	-	83.4
Stage 3 (POCI)					
Not past due	-	-	-	-	-
Past due < 1 month	-	0.2	-	-	0.2
Past due 1 to 3 months	-	-	-	-	-
Past due 3 to 6 months	-	-	-	-	-
Past due 6 to 12 months	-	-	-	-	-
Past due over 12 months	-	0.1	-	-	0.1
Possessions	-	-	-	-	-
	-	0.3	-	-	0.3
Total loans before provisions	5,801.3	428.6	151.2	135.2	6,516.3

Notes to the Condensed Consolidated Financial Statements (continued)

15. Risk management and financial instruments (continued)

	As at 31-Dec-17 (Audited)				
BTL/SME	Buy-to-Let £m	Commercial £m	Residential development £m	Funding lines £m	Total £m
Not impaired:					
Not past due	4,810.7	360.8	143.9	104.5	5,419.9
Past due < 1 month	160.4	2.8	-	-	163.2
Past due 1 to 3 months	31.9	0.6	-	-	32.5
Past due 3 to 6 months	2.7	-	-	-	2.7
Past due 6 to 12 months	0.7	-	-	-	0.7
Past due over 12 months	0.3	0.8	-	-	1.1
Possessions	-	-	-	-	-
	5,006.7	365.0	143.9	104.5	5,620.1
Impaired:					
Not past due	4.6	4.5	-	-	9.1
Past due < 1 month	-	0.1	-	-	0.1
Past due 1 to 3 months	-	-	-	-	-
Past due 3 to 6 months	9.1	-	-	-	9.1
Past due 6 to 12 months	4.0	0.4	-	-	4.4
Past due over 12 months	1.6	0.1	-	-	1.7
Possessions	7.8	0.7	-	-	8.5
	27.1	5.8	-	-	32.9
Total mortgages before provisions	5,033.8	370.8	143.9	104.5	5,653.0
Personal loans					1.1
Total loans before provisions					5,654.1

Notes to the Condensed Consolidated Financial Statements
(continued)

15. Risk management and financial instruments (continued)

Residential	First charge £m	Second charge £m	Funding lines £m	Total £m
	As at 30-Jun-18 (Unaudited)			
Stage 1				
Not past due	**932.5**	**286.8**	**23.0**	**1,242.3**
Past due < 1 month	**63.8**	**9.4**	**-**	**73.2**
	996.3	**296.2**	**23.0**	**1,315.5**
Stage 2				
Not past due	**11.6**	**20.2**	**-**	**31.8**
Past due < 1 month	**35.0**	**7.3**	**-**	**42.3**
Past due 1 to 3 months	**25.9**	**6.3**	**-**	**32.2**
	72.5	**33.8**	**-**	**106.3**
Stage 3				
Not past due	**19.4**	**3.5**	**-**	**22.9**
Past due < 1 month	**10.6**	**3.3**	**-**	**13.9**
Past due 1 to 3 months	**18.0**	**8.0**	**-**	**26.0**
Past due 3 to 6 months	**18.3**	**8.7**	**-**	**27.0**
Past due 6 to 12 months	**13.5**	**4.7**	**-**	**18.2**
Past due over 12 months	**5.8**	**2.2**	**-**	**8.0**
Possessions	**4.3**	**-**	**-**	**4.3**
	89.9	**30.4**	**-**	**120.3**
Stage 3 (POCI)				
Not past due	**13.6**	**6.3**	**-**	**19.9**
Past due < 1 month	**4.3**	**1.9**	**-**	**6.2**
Past due 1 to 3 months	**4.5**	**3.0**	**-**	**7.5**
Past due 3 to 6 months	**4.1**	**4.5**	**-**	**8.6**
Past due 6 to 12 months	**3.4**	**5.2**	**-**	**8.6**
Past due over 12 months	**1.6**	**8.6**	**-**	**10.2**
Possessions	**-**	**-**	**-**	**-**
	31.5	**29.5**	**-**	**61.0**
Total loans before provisions	**1,190.2**	**389.9**	**23.0**	**1,603.1**

Notes to the Condensed Consolidated Financial Statements (continued)

15. Risk management and financial instruments (continued)

	As at 31-Dec-17 (Audited)			
Residential	First charge £m	Second charge £m	Funding lines £m	Total £m
Not impaired:				
Not past due	1,023.6	331.8	17.6	1,373.0
Past due < 1 month	123.1	20.8	-	143.9
Past due 1 to 3 months	46.4	23.1	-	69.5
Past due 3 to 6 months	10.5	7.7	-	18.2
Past due 6 to 12 months	8.1	5.3	-	13.4
Past due over 12 months	3.2	3.3	-	6.5
Possessions	0.5	-	-	0.5
	1,215.4	392.0	17.6	1,625.0
Impaired:				
Not past due	2.9	0.3	-	3.2
Past due < 1 month	0.7	-	-	0.7
Past due 1 to 3 months	2.2	-	-	2.2
Past due 3 to 6 months	7.5	7.1	-	14.6
Past due 6 to 12 months	6.6	5.3	-	11.9
Past due over 12 months	2.2	10.6	-	12.8
Possessions	3.1	-	-	3.1
	25.2	23.3	-	48.5
Total loans before provisions	1,240.6	415.3	17.6	1,673.5

15. Risk management and financial instruments (continued)

Forbearance measures undertaken

The Group has a range of options available where borrowers experience financial difficulties which impact their ability to service their financial commitments under the loan agreement. These are explained on pages 45 to 46 of the 2017 Annual Report.

A summary of the forbearance measures undertaken during the period under review is below:

	H1 2018 number of accounts	**As at 30-Jun-18 £m**	Restated[1] H1 2017 number of accounts	Restated[1] As at 30-Jun-17 £m
Forbearance type:				
Interest only switch	**16**	**2.8**	27	1.5
Interest rate reduction	**3**	**0.9**	-	-
Term extension	**15**	**1.5**	21	3.7
Payment holiday	**27**	**0.8**	34	1.5
Payment concession (reduced monthly payments)	**27**	**2.5**	17	0.4
Capitalisation	**-**	**-**	-	-
Total	**88**	**8.5**	99	7.1

	H1 2018 number of accounts	**As at 30-Jun-18 £m**	Restated[1] H1 2017 number of accounts	Restated[1] As at 30-Jun-17 £m
Loan type:				
First charge owner occupier	**22**	**2.6**	43	3.5
Second charge owner occupier	**52**	**1.5**	43	1.1
Buy-to-Let	**14**	**4.4**	13	2.5
Commercial	**-**	**-**	-	-
Total	**88**	**8.5**	99	7.1

[1] Forbearance measures have been restated for second charge owner occupier mortgages to remove the first charge related balance to align to the approach adopted for the 2017 Annual Report. The 2017 comparatives also reflect changes to the data capture process.

Notes to the Condensed Consolidated Financial Statements (continued)

15. Risk management and financial instruments (continued)

Geographical analysis by region

An analysis of loans by region is provided below:

	As at 30-Jun-18 (Unaudited)		As at 31-Dec-17 (Audited)	
Region	**£m**	**%**	£m	%
East Anglia	**279.2**	**3**	236.4	3
East Midlands	**280.5**	**3**	249.6	4
Greater London	**3,561.6**	**45**	3,173.0	43
Guernsey	**67.1**	**1**	73.8	1
Jersey	**194.6**	**2**	225.1	3
North East	**113.4**	**1**	103.0	1
North West	**385.7**	**5**	347.9	5
Northern Ireland	**15.3**	**-**	16.9	-
Scotland	**47.5**	**1**	51.1	1
South East	**1,776.5**	**22**	1,591.7	22
South West	**583.3**	**7**	522.3	7
Wales	**156.3**	**2**	142.9	2
West Midlands	**480.6**	**6**	425.4	6
Yorks & Humberside	**177.8**	**2**	167.4	2
Total mortgages before provisions	**8,119.4**	**100**	7,326.5	100
Personal loans	**-**		1.1	
Total loans before provisions	**8,119.4**		7,327.6	

16. Fair values of financial assets and financial liabilities

The following tables provide an analysis of financial assets and financial liabilities measured at fair value on the Statement of Financial Position grouped into level 1 to 3 based on the degree to which the fair value is observable:

As at 30 June 2018 (Unaudited)	**Carrying amount £m**	**Principal amount £m**	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
Financial assets						
Investment securities	**19.1**	**19.0**	**19.1**	**-**	**-**	**19.1**
Derivative assets	**13.2**	**1,870.0**	**-**	**13.2**	**-**	**13.2**
	32.3	**1,889.0**	**19.1**	**13.2**	**-**	**32.3**
Financial liabilities						
Derivative liabilities	**19.9**	**2,951.9**	**-**	**19.9**	**-**	**19.9**

As at 31 December 2017 (Audited)	Carrying amount £m	Principal amount £m	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets						
Investment securities	19.1	19.0	19.1	-	-	19.1
Derivative assets	6.1	1,636.1	-	6.1	-	6.1
	25.2	1,655.1	19.1	6.1	-	25.2
Financial liabilities						
Derivative liabilities	21.8	2,493.9	-	21.8	-	21.8

Fair values are determined using the following fair value hierarchy that reflects the significance and observability of the inputs used in making the measurements:

Level 1
Fair values that are based entirely on quoted market prices (unadjusted) in an actively traded market for identical assets and liabilities that the Group has the ability to access. Valuation adjustments and block discounts are not applied to level 1 instruments. Since valuations are based on readily available observable market prices, this makes them most reliable, reduces the need for management judgement and estimation and also reduces the uncertainty associated with determining fair values.

Level 2
Fair values that are based on one or more quoted prices in markets that are not active or for which all significant inputs are taken from directly or indirectly observable market data. These include valuation models used to calculate the present value of expected future cash flows and may be employed either when no active market exists or when there are quoted prices available for similar instruments in active markets.

Level 3
Fair values for which any one or more significant input is not based on observable market data and the unobservable inputs have a significant effect on the instruments fair value. Valuation models that employ significant unobservable inputs require a higher degree of management judgement and estimation in determining the fair value. Management judgement and estimation are usually required for the selection of the appropriate valuation model to be used, determination of expected future cash flows on the financial instruments being valued, determination of the probability of counterparty default and prepayments, determination of expected volatilities and correlations and the selection of appropriate discount rates.

Notes to the Condensed Consolidated Financial Statements (continued)

16. Fair values of financial assets and financial liabilities (continued)

The following tables provide an analysis of financial assets and financial liabilities not measured at fair value on the Statement of Financial Position grouped into level 1 to 3 based on the degree to which the fair value is observable:

			Estimated fair value			
As at 30 June 2018 (Unaudited)	**Carrying amount £m**	**Principal amount £m**	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
Financial assets						
Cash in hand	**0.3**	**0.3**	**-**	**0.3**	**-**	**0.3**
Loans and advances to credit institutions	**1,476.7**	**1,476.7**	**-**	**1,476.7**	**-**	**1,476.7**
Loans and advances to customers	**8,096.5**	**8,237.6**	**-**	**2,586.3**	**5,986.3**	**8,572.6**
	9,573.5	**9,714.6**	**-**	**4,063.3**	**5,986.3**	**10,049.6**
Financial liabilities						
Amounts owed to retail depositors	**7,423.8**	**7,396.3**	**-**	**2,740.6**	**4,717.1**	**7,457.7**
Amounts owed to credit institutions	**1,508.7**	**1,508.7**	**-**	**1,508.7**	**-**	**1,508.7**
Amounts owed to other customers	**32.6**	**32.5**	**-**	**-**	**32.6**	**32.6**
Subordinated liabilities	**10.9**	**10.7**	**-**	**10.9**	**-**	**10.9**
Perpetual subordinated bonds	**15.3**	**15.0**	**15.0**	**-**	**-**	**15.0**
	8,991.3	**8,963.2**	**15.0**	**4,260.2**	**4,749.7**	**9,024.9**

			Estimated fair value			
As at 31 December 2017 (Audited)	Carrying amount £m	Principal amount £m	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets						
Cash in hand	0.5	0.5	-	0.5	-	0.5
Loans and advances to credit institutions	1,187.2	1,187.2	-	1,187.2	-	1,187.2
Loans and advances to customers	7,306.0	7,441.9	-	2,788.8	4,926.6	7,715.4
	8,493.7	8,629.6	-	3,976.5	4,926.6	8,903.1
Financial liabilities						
Amounts owed to retail depositors	6,650.3	6,610.1	-	2,474.4	4,209.6	6,684.0
Amounts owed to credit institutions	1,250.3	1,250.3	-	1,250.3	-	1,250.3
Amounts owed to other customers	25.7	25.5	-	-	25.7	25.7
Subordinated liabilities	10.9	10.7	-	11.1	-	11.1
Perpetual subordinated bonds	15.3	15.0	15.3	-	-	15.3
	7,952.5	7,911.6	15.3	3,735.8	4,235.3	7,986.4

Notes to the Condensed Consolidated Financial Statements (continued)

17. Capital management

The Group's individual regulated entities and the Group as a whole complied with all of the capital requirements which they were subject to for the periods presented.

The regulatory capital of the Group is presented below:

	As at 30-Jun-18 (Unaudited) £m	As at 31-Dec-17 (Audited) £m
Common equity tier 1 capital		
Called up share capital	**2.4**	2.4
Share premium, capital contribution and share-based payment reserve	**168.9**	169.8
Retained earnings	**381.4**	337.5
Transfer reserve	**(12.8)**	(12.8)
Other reserves	**(0.7)**	(0.1)
Total equity excluding equity bonds	**539.2**	496.8
Foreseeable dividends	**(16.8)**	(22.6)
Solo consolidation adjustments[1]	**(4.6)**	(4.8)
IFRS 9 transitional adjustment[2]	**2.7**	-
Deductions from common equity tier 1 capital		
Intangible assets	**(7.5)**	(6.8)
Deferred tax asset	**(2.2)**	(2.5)
Common equity tier 1 capital	**510.8**	460.1
Additional tier 1 capital		
AT1 Securities	**60.0**	60.0
Total tier 1 capital	**570.8**	520.1
Tier 2 capital		
Subordinated debt and PSBs	**47.6**	47.7
Collective provisions	**-**	2.0
Deductions from tier 2 capital	**(3.0)**	(2.5)
Total tier 2 capital	**44.6**	47.2
Total regulatory capital	**615.4**	567.3
Risk weighted assets (unaudited)	**3,843.7**	3,348.5

[1] The Bank has solo consolidation waivers for most of its subsidiaries. The capital contribution reserve, share-based payment reserve, foreign exchange reserve and retained earnings for unconsolidated entities have been removed from CET1.

[2] The regulatory capital has benefitted from a £2.7m add-back under IFRS 9 transitional arrangements. This represents 95% of the IFRS 9 transitional adjustment booked directly to retained earnings of £2.9m. The full impact of IFRS 9, if applied, would reduce total regulatory capital to £612.7m.

Notes to the Condensed Consolidated Financial Statements (continued)

18. Operating segments

The Group distinguishes two segments within its operations: BTL/SME mortgages and Residential mortgages.

The financial position and results of operations of the above segments are summarised below:

Six months ended 30-Jun-18 (Unaudited)	**BTL/SME £m**	**Residential mortgages £m**	**Total £m**
Balances at the reporting date			
Gross loans and advances to customers	**6,516.3**	**1,603.1**	**8,119.4**
Expected credit loss	**(13.0)**	**(9.9)**	**(22.9)**
Loans and advances to customers	**6,503.3**	**1,593.2**	**8,096.5**
Capital expenditure	**2.2**	**0.6**	**2.8**
Profit for six months ended 30-Jun-18 (Unaudited)			
Net interest income	**102.3**	**32.9**	**135.2**
Other expense	**(0.6)**	**(1.5)**	**(2.1)**
Total income	**101.7**	**31.4**	**133.1**
Impairment losses	**(3.0)**	**(1.3)**	**(4.3)**
Contribution to profit	**98.7**	**30.1**	**128.8**
Operating expenses			**(35.9)**
FSCS and other regulatory provisions			**(1.1)**
Profit before taxation			**91.8**
Taxation			**(22.3)**
Profit for the period			**69.5**

Year ended 31-Dec-17 (Audited)	BTL/SME £m	Residential mortgages £m	Total £m
Balances at the reporting date			
Gross loans and advances to customers	5,654.1	1,673.5	7,327.6
Provision for impairment losses on loans and advances	(13.2)	(8.4)	(21.6)
Loans and advances to customers	5,640.9	1,665.1	7,306.0
Capital expenditure	11.0	3.3	14.3
Profit for six months ended 30-Jun-17 (Unaudited)			
Net interest income	83.4	33.7	117.1
Other expense	(1.4)	(4.9)	(6.3)
Total income	82.0	28.8	110.8
Impairment (losses)/gains	(1.5)	0.1	(1.4)
Contribution to profit	80.5	28.9	109.4
Operating expenses			(30.6)
FSCS and other provisions			(0.4)
Profit before taxation			78.4
Taxation			(19.4)
Profit for the period			59.0

Notes to the Condensed Consolidated Financial Statements (continued)

19. Adjustments for non-cash items and changes in operating assets and liabilities

	Six months ended 30-Jun-18 (Unaudited) £m	Six months ended 30-Jun-17 (Unaudited) £m
Adjustments for non-cash items:		
Depreciation and amortisation	**2.2**	1.6
Interest on subordinated liabilities	**0.4**	0.3
Interest on perpetual subordinated bonds	**0.4**	0.4
Impairment charge on loans	**4.3**	1.4
Loss on sale of financial instruments	**0.2**	-
FSCS and other provisions	**1.1**	0.4
Fair value losses on financial instruments	**1.7**	5.6
Share-based payments	**1.4**	0.9
Total adjustments for non-cash items	**11.7**	10.6
Changes in operating assets and liabilities:		
Decrease in loans and advances to credit institutions	**(3.3)**	(7.9)
Increase in loans to customers	**(799.0)**	(608.8)
Increase in retail deposits	**773.5**	94.6
Net (increase)/decrease in other assets	**(5.0)**	3.8
Net decrease in derivatives and hedged items	**0.1**	5.5
Net increase in credit institutions and other customers deposits	**15.3**	13.9
Net increase/(decrease) in other liabilities	**0.1**	(7.1)
Exchange differences on working capital	**(0.5)**	(0.1)
Total changes in operating assets and liabilities	**(18.8)**	(506.1)

20. Related parties

The Group had no related party transactions during the six months to 30 June 2018 that would materially affect the position or performance of the Group. Details of transactions for the year ended 31 December 2017 can be found in the 2017 Annual Report on pages 137 to 139.

Transactions with Key Management Personnel

During the period, the Group granted awards under the Deferred Share Bonus Plan and Performance Share Plan as described in note 6 to these interim accounts and note 9 in the 2017 Annual Report on pages 126 to 128. The impact of these awards in the six months ended 30 June 2018 is reported within staff costs.

21. Events after the reporting date

There have been no material events after the reporting date.

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