Interim Financial Report

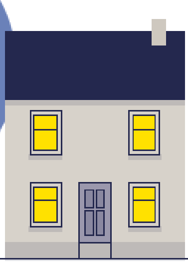
30 June 2019

Leeds Building Society

2019: our performance so far

Gross residential lending exceeded
£1.9bn
(H1 2018: £1.8bn)

We helped **20,000** more people have the home they want.



Total assets up 7% to
£20.7bn
(Dec 2018: £19.4bn)

Record savings balances up 5% to
£14.6bn
(Dec 2018: £13.9bn)

We helped **32,000** more people save for their future.

We paid an average of
1.35%
to our savers compared to the rest of market average of 0.73%

An annual benefit to all our savers of **£84m**.

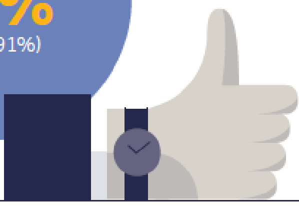
Profit before tax
£49.4m
(H1 2018: £60.1m)

Common Equity Tier 1 Capital is
30.3%
(Dec 2018: 31.3%)

Reserves available to protect us from future problems.

Customer Satisfaction
92%
(2018: 91%)

We have an ongoing commitment to be customer focused in everything we do.



Colleague engagement score up 1% to
82%
(2018: 81%)

We're committed to being a great place to work.

Chief Executive Officer's Review

Leeds Building Society has delivered a robust financial performance for the first half of 2019, with mortgage lending and savings balances up, in our first mid-year results since I became Chief Executive Officer.

In the first half of the year the Society increased residential mortgage balances by 4.4% to £16.5bn (December 2018: £15.8bn), supported by new lending of £1.9bn (six months to June 2018: £1.8bn), and attracted 5.2% more savings balances (£14.6bn; December 2018: £13.9bn), taking total assets above £20bn for the first time, up 6.9% to £20.7bn from £19.4bn at 31 December 2018.

During that period we helped 32,000 more people to save, as well as 20,000 more to have the home they want, including 6,000 who moved into their very first home.

The Society has demonstrated continued support of our members by offering competitive products and services despite economic uncertainty. Sustained pressure on mortgage pricing and high levels of refinancing have translated into lower mortgage income and, without an equivalent reduction in funding costs, have suppressed net interest income.

The underlying strength of the mortgage book remains high with a low level of arrears and continued high quality security; albeit a worsening view of forecast economic conditions has negatively impacted expectations of credit losses and resulted in increased charges for impairment loss provisions.

Notwithstanding these pressures, we have reported a robust profit of £49.4m (six months to June 2018: £60.1m) that has added to our established financial security and strong capital position.

The Society's resilience was further enhanced a year ago when the Prudential Regulation Authority granted Internal Ratings Based (IRB) permission, enabling us to assess our own capital requirements for credit risk using internal models. CET1 and total capital ratios of 30.3% and 37.0% respectively are among the strongest risk based measures of any UK bank or building society and the UK leverage ratio of 5.4% is well above the regulatory requirement.

Our ambitious investment plans are progressing well. So far in 2019 work has begun to fit out our new Leeds headquarters and the phased upgrading to future-proof lending systems is underway. Both projects are major commitments to future service improvements which also will boost efficiency and save money.

The building society model of focusing on long term value for the benefit of our membership as a whole continues to be a guiding principle which enables us to remain secure and stable. We stay true to the purpose for which we were founded, to help people save and have the home they want, and we continue to lend responsibly and grow in a prudent and carefully managed way. This is despite the challenging headwinds in the UK economy and the impact of cooling consumer confidence.

As expected, increased competition and the effects of slowing economic growth have had an impact on our profit levels. Similarly, our ongoing investment in member value and our digital capabilities will affect profits. While profits have reduced this year they remain at a healthy level.

Our cost to income and cost to mean asset ratios of 49.4% and 0.50% respectively are among the best in the sector, and we retain our keen cost focus.

Following planned high levels of growth over several years, we have made a conscious choice to moderate increases in mortgages and savings balances to focus on protecting our interest margin.

Chief Executive Officer's Review

We'll continue to pursue our strategy of supporting borrowers who are not well served by the wider market, such as through Shared Ownership, Interest Only and Buy to Let, as we keep looking for new ways to respond to the evolving needs of our members. Our approach was recognised when What Mortgage magazine awarded us the accolade of 'Best Shared Ownership Lender' for the fourth consecutive year. We've also built on last year's launch of our Retirement Interest Only proposition and seen rising demand in this new segment of later life lending.

Customer satisfaction levels remain high at 92% (2018: 91%). As a mutual, we need to balance the needs of our whole membership, whether borrowers or savers, and whilst we cannot ignore the impact of continued low interest rates in the market, we work hard to keep savings rates as high as possible for as long as possible in what has been a historically low rate environment. We will carry on paying above the market average to our savers. On the latest data available, we paid 0.62% above the market average on our savings rates, equating to an annual benefit to our savers of £84 million[1].

Fairer Finance also awarded the Society its 'Gold Ribbon' for savings accounts based on customer happiness and trust, along with our ability to explain things clearly.

The Society is committed to being a great place to work and continues to support and develop its people. As a result colleague engagement increased to 82% (2018: 81%). The significant support from colleagues for our first national charity partner, Samaritans, means fundraising is nearing our £250,000 target, seven months ahead of schedule.

As we progress towards our corporate responsibility goals, we'll keep on setting ourselves stretching targets. Last month we celebrated Fair Tax Mark accreditation for a second year, offering independent proof of our tax transparency, which is something that matters greatly to members.

Our direction is always shaped by our members. Talking, and listening, to them informs how we develop our products and services, and also how we conduct ourselves as a responsible business.

All executive directors voluntarily opted to move to the existing colleague pension scheme, effective from 1 September, without any compensation for the loss in benefits, thus reducing the cost to the Society.

Doing the right thing for colleagues, members and communities continues to shape our business strategy and practice, as it has done throughout our long history. Our commitment to long term stability for the benefit of our membership as a whole means we are well placed to withstand economic shocks and market uncertainty.

Richard Fearon

Chief Executive Officer

[1] The Society paid an average of 1.35% to its savers compared to the market average of 0.73% - CACI's CSDB, Stock, June 2018 – May 2019, latest data available. CACI is an independent company that provides financial benchmarking data and covers 87% of the high street cash savings market.

2019 First Half Key Performance Indicators

The 2019 first half key performance indicators are shown below. Comparative figures are shown for the full year unless otherwise stated. The only change from the measures reported in the 2018 Interim Financial Report is the UK leverage ratio is used instead of the CRR leverage ratio, in line with internal reporting.

Customer focused

To support the aspirations of a targeted range of borrowers and savers focused on where our expertise adds significant value.

New (gross) residential lending APM	Net residential lending APM	Savings balances	Society membership
£1.9 billion	**£0.7 billion**	**£14.6 billion**	**811,000 members**
H1 2018: £1.8 billion	H1 2018: £0.5 billion	Dec 2018: £13.9 billion	Dec 2018: 804,000 members

Secure

To generate strong levels of profit through optimising our lending to continue to build a sound capital base.

Profit before tax	Net interest margin APM	Liquidity Coverage Ratio (LCR)	Common Equity Tier 1 (CET1) ratio	UK leverage ratio	Credit ratings (Long term)
£49.4 million	**0.98%**	**226%**	**30.3%**	**5.4%**	**Fitch A- Moody's A3**
H1 2018: £60.1 million	2018: 1.15%	Dec 2018: 214%	Dec 2018: 31.3%	Dec 2018: 5.5%	Dec 2018: Fitch A- Moody's A3

Service driven

To deliver outstanding personal service across all channels supported by access to colleagues when desired.

Number of days from mortgage application to offer	% of customer administration processing completed within service standards	Customer satisfaction	Colleague engagement score
15 days	**99%**	**92%**	**82%**
2018: 16 days	2018: 93%	2018: 91%	2018: 81%

Efficient

To adapt our operating model as markets and needs change, whilst being intolerant of waste.

Cost to income ratio APM	Cost to mean asset ratio APM	Colleague turnover
49.4%	**0.50%**	**18%**
2018: 44.8%	2018: 0.52%	2018: 19%

Alternative performance measures (indicated above by APM) and other terms used in this report are explained and reconciled to the equivalent statutory measure in the glossary of terms on pages 181 to 184 of the 2018 Annual Report and Accounts which can be found at www.leedsbuildingsociety.co.uk/press/financial-results/.

Financial performance

In the first half of 2019 the Society has continued to grow its balance sheet, with total assets increasing by 6.9% to £20.7 billion. However, in common with the rest of the financial services sector, tough competition has resulted in a contraction in margins which has had an impact on profits.

The Group's profit before tax for the first six months of 2019 was £49.4 million (six months to June 2018: £60.1 million). As expected, the reduction in profit is primarily driven by lower net interest income resulting from challenging market conditions combined with elevated charges for impairment reflecting a worsening view of forecast economic conditions and a moderated level of provision releases.

Net interest income

	Six months to June 2019 £m	Six months to June 2018 £m	Year to December 2018 £m
Net interest income	98.0	109.6	218.1
Mean total assets	20,055	18,990	18,937
	%	%	%
Net interest margin (NIM) APM	**0.98**	**1.15**	**1.15**

As anticipated, net interest income has decreased, 10.6% lower in the first half of 2019 than the same period in the prior year. This is primarily due to lower mortgage income, reflecting sustained market pressure and high levels of product switches and refinancing. The Society supports existing customers by offering competitive products when their product term ends in order to retain them. Intense competition in the mortgage market means that new products are written at lower margins than those written in previous years, diluting the overall NIM.

The Society continues to focus on lending to specific segments of the market where it has established expertise, such as buy to let and shared ownership. This focus helps to mitigate some of the impact of this margin compression.

Management expenses

	Six months to June 2019 £m	Six months to June 2018 £m	Year to December 2018 £m
Colleague costs	29.9	29.6	61.4
Other administrative expenses	16.3	17.5	33.5
Depreciation and amortisation	3.7	1.8	4.0
Total management expenses	**49.9**	**48.9**	**98.9**
	%	%	%
Cost to income ratio APM	49.4	43.4	44.8
Cost to mean asset ratio APM	0.50	0.52	0.52

The Society continues to maintain close control on costs, with management expenses increasing by 2.0% in the first half of 2019 compared to 2018. The average number of colleagues employed by the Society is approximately 3% lower in H1 2019 than H1 2018.

Depreciation and amortisation charges have increased due to capital investment in technology in recent years. The Society has a number of change initiatives in progress which will enhance its digital capabilities in order to continue to meet the needs of existing and new members. This significant investment will lead to further increases in depreciation and amortisation charges in the coming years.

Impairments and provisions

	Six months to June 2019 £m	Six months to June 2018 £m	Year to December 2018 £m
Residential loan impairment charge	3.0	0.7	2.4
Commercial loan impairment release	(0.9)	(3.2)	(3.6)
Provisions release	(0.4)	(0.6)	(0.2)
Total impairments and provisions	**1.7**	**(3.1)**	**(1.4)**

The proportion of residential mortgages in arrears[1] increased to 0.51% in the first half of 2019 (December 2018: 0.46%). The residential impairment charge of £3.0 million is primarily due to a worsening view of forecast economic conditions which impact expectations of credit losses and therefore impairment loss provisions under IFRS 9. In particular house price growth and GDP growth are expected to be lower due to continued uncertainty surrounding the nature and impact of the UK's exit from the European Union.

While the individual scenarios have been updated to reflect this worsening view, the number of scenarios used, and the weighting of the scenarios, remain unchanged from 31 December 2018. This reflects the largely unchanged economic environment at 30 June 2019 compared to the year end and the continued uncertainty surrounding the potential impact of the UK leaving the EU.

Provision coverage is unchanged compared to December 2018 at 0.18%. Actual realised losses continue to be lower than provided for.

The Society continues to manage down its legacy commercial loan portfolio. No further losses have been realised in 2019 and provisions have been released on loans which redeemed in full.

Financial position

Total assets increased by 6.9% in the first half of 2019, from £19.4 billion at 31 December 2018 to £20.7 billion.

Loans and advances to customers

	30 June 2019 £m	30 June 2018 £m	31 December 2018 £m
Residential loans	16,504	15,291	15,805
Commercial loans	21	60	31
Other loans	229	244	232
Impairment provision	(35)	(43)	(34)
Loans and advances to customers	**16,719**	**15,552**	**16,034**
	%	%	%
Proportion of mortgages in arrears[1]	0.51	0.63	0.46
Balance-weighted average indexed LTV of mortgage book	54	56	55
Balance-weighted average LTV of new lending	60	63	62

Gross new lending in the first half of 2019 was higher than in the same period in 2018 at £1.9 billion (H1 2018: £1.8 billion) despite an increasingly competitive mortgage market. The Society's share of new mortgage lending remains above its natural market share at 1.5% (2018 full year: 1.4%).

[1] Mortgages which are either in possession or with arrears of more than 1.5% of the balance

The growth in mortgage balances in recent years has led to a high volume of customers reaching the end of their initial product term. Strong performance in retaining these customers on new products has limited the level of redemptions, with net lending for the first half of the year of £0.7 billion (six months to June 2018: £0.5 billion).

The Society maintains a conservative lending policy and controls on new lending have been maintained throughout the period, which is reflected in the average LTV of new lending. The overall quality of the book remains high with a low level of arrears, well below the market average[2], and a weighted average indexed LTV of the book at 30 June 2019 of 54% (December 2018: 55%).

Liquidity

	30 June 2019 £m	30 June 2018 £m	31 December 2018 £m
Liquid assets	3,323	3,290	2,827
	%	%	%
Liquidity Coverage Ratio (LCR)	226	249	214
Liquid assets as a percentage of shares and borrowings	17.49	18.36	15.90

The level of liquid assets (including reserves with the Bank of England and other High Quality Liquid Assets) varies throughout the year depending on the timing of savings and wholesale funding inflows. At 30 June 2019, the balance of liquidity was inflated by the proceeds of a £600 million Covered Bond issuance in the first half of the year. Liquidity remained well in excess of regulatory minima throughout the period, and is subject to regular stress testing which demonstrates that appropriate levels of liquidity are maintained.

At 30 June 2019, 100% of liquid assets were rated ‘A’ or above.

Funding

	30 June 2019 £m	30 June 2018 £m	31 December 2018 £m
Shares (member deposits)	14,638	13,854	13,910
Wholesale funding	4,360	4,064	3,871
Total funding	**18,998**	**17,918**	**17,781**
	%	%	%
Wholesale funding ratio	21.7	21.3	20.3

The Society has continued to grow savings balances through its branch network and online, with balances increasing by 5.2% to £14.6 billion. The Society continues to pay above average market rates to reward savings members.

In April 2019 the Society issued a £600m Covered Bond, its largest ever Covered Bond issuance and its first with an interest rate linked to SONIA.

[2] The Society’s arrears of more than 2.5% of the balance at 30 June 2019 were 0.39% for Homeowners and 0.11% for Buy to let, compared to market averages of 0.85% for Homeowners and 0.24% for Buy to let (Source: UK Finance: Mortgage Arrears and Possessions Update Quarter 1 2019).

Capital

The Prudential Regulation Authority (PRA) granted the Society an Internal Ratings Based (IRB) permission effective from 1 July 2018. In the table below, the comparative figures for 30 June 2018 have been restated to be shown on an IRB basis in order to aid comparability with the current period.

Capital resources	30 June 2019 £m	30 June 2018 £m	31 December 2018 £m
Total equity attributable to members	1,064	985	1,026
Adjustments	(33)	(21)	(29)
Common Equity Tier 1 (CET1) capital	1,031	964	997
Additional Tier 1 capital	7	10	10
Total Tier 1 capital	1,038	974	1,007
Tier 2 capital	220	215	218
Total regulatory capital resources	**1,258**	**1,189**	**1,225**
Risk-weighted assets	3,405	3,274	3,183
	%	%	%
CET1 ratio	30.3	29.5	31.3
Total capital ratio	37.0	36.3	38.5
CRR leverage ratio	4.9	4.9	5.1
UK leverage ratio	5.4	5.4	5.5

The Society has maintained capital levels significantly in excess of regulatory minima throughout the first half of 2019. Total capital resources have increased broadly in line with retained profits for the period.

Principal risks & uncertainties

To ensure that the interests of members are adequately protected, the Society has embedded an Enterprise Risk Management Framework, which is designed to identify, manage, monitor and control the risks associated with the delivery of the Society's strategic objectives. Further details can be found on pages 66 to 70 of the 2018 Annual Report and Accounts.

The principal risks arising from the Society's strategy are credit, funding and liquidity, capital, market, operational, conduct, strategic and business risk. These are common to most retail financial services firms in the UK. The directors consider that these principal risks have not changed since the previous reporting period, with full details set out on pages 14 to 19 of the 2018 Annual Report and Accounts.

The emerging risks identified on pages 20 and 21 of the 2018 Annual Report and Accounts remain prevalent. In particular, macroeconomic and political risks remain heightened due to uncertainty surrounding the UK's departure from the EU and the wider geopolitical environment. As a UK centric business, the Society has limited exposure to the EU. However, in common with other UK lending and deposit takers, the Society could be impacted by any effects on the wider economy from leaving the EU without appropriate arrangements. The Society considers macroeconomic and political risk on a regular basis under both central and stressed conditions in order to understand and manage the impact on its business model.

Condensed Consolidated Income Statement

	Notes	**Six months to 30 June 2019 (Unaudited) £M**	Six months to 30 June 2018 (Unaudited) £M	Year to 31 December 2018 (Audited) £M
Interest receivable and similar income	3	**227.6**	224.0	457.0
Interest payable and similar charges	4	**(129.6)**	(114.4)	(238.9)
Net interest receivable		**98.0**	109.6	218.1
Fees and commissions receivable		**3.5**	4.0	8.6
Fees and commissions payable		**(0.6)**	(0.4)	(0.8)
Fair value gains less losses from financial instruments		**(0.6)**	(0.3)	(5.7)
Other operating income		**0.7**	(0.1)	0.7
Total income		**101.0**	112.8	220.9
Administrative expenses	5	**(46.2)**	(47.1)	(94.9)
Depreciation and amortisation		**(3.7)**	(1.8)	(4.0)
Impairment (losses) / gains on loans and advances to customers	6	**(2.1)**	2.5	1.2
Provisions release	7	**0.4**	0.6	0.2
Loss on sale of financial assets		**-**	(6.9)	(6.5)
Operating profit and profit before tax		**49.4**	60.1	116.9
Tax expense	8	**(12.5)**	(15.1)	(27.7)
Profit for the period		**36.9**	45.0	89.2

All amounts relate to continuing operations apart from £0.3m of interest receivable in 2018. This related to the sale of a portfolio of loans and advances to customers secured on residential property in the Republic of Ireland (see note 13 of the 2018 Annual Report and Accounts).

Condensed Consolidated Statement of Comprehensive Income

	Six months to 30 June 2019 (Unaudited) £M	Six months to 30 June 2018 (Unaudited) £M	Year to 31 December 2018 (Audited) £M
Profit for the period	**36.9**	45.0	89.2
Items that may subsequently be reclassified to profit and loss:			
Fair value gains / (losses) on investment securities measured at fair value through other comprehensive income	**2.9**	(3.0)	(5.3)
(Gains) / losses on investment securities measured through other comprehensive income reclassified to profit or loss on disposal	**(0.1)**	0.1	(0.8)
Tax relating to items that may subsequently be reclassified	**(0.7)**	0.6	1.3
Items that may not subsequently be reclassified to profit and loss:			
Actuarial (loss) / gain on retirement benefit surplus	**(2.3)**	4.3	8.6
Revaluation loss on properties revalued	**-**	-	(1.0)
Tax relating to items that may not be reclassified	**0.6**	(1.4)	(4.8)
Total comprehensive income for the period	**37.3**	45.6	87.2

Condensed Consolidated Statement of Financial Position

	Notes	**30 June 2019 (Unaudited) £M**	30 June 2018 (Unaudited) £M	31 December 2018 (Audited) £M
Assets				
Liquid assets				
Cash in hand and balances with the Bank of England		**1,879.1**	1,822.1	1,428.0
Loans and advances to credit institutions		**188.2**	163.7	169.7
Investment securities		**1,256.0**	1,304.0	1,229.1
Derivative financial instruments		**278.5**	259.1	273.4
Loans and advances to customers	9			
Loans fully secured on residential property		**16,474.9**	15,263.9	15,777.1
Other loans		**243.9**	288.5	256.3
Fair value adjustment for hedged risk on loans and advances to customers		**73.9**	28.8	18.0
Assets classified as held for sale: loans and advances to customers		**-**	133.2	-
Other assets, prepayments and accrued income		**234.1**	159.6	160.5
Deferred tax assets		**6.3**	6.4	6.4
Intangible assets		**9.0**	6.0	8.5
Property, plant and equipment		**67.7**	54.0	53.0
Retirement benefit surplus	10	**8.5**	6.2	10.1
Total assets		**20,720.1**	19,495.5	19,390.1
Liabilities				
Shares		**14,637.6**	13,854.4	13,909.5
Fair value adjustment for hedged risk on shares		**6.0**	34.7	15.7
Derivative financial instruments		**200.8**	127.3	133.2
Amounts owed to credit institutions		**1,350.4**	1,285.2	1,399.3
Amounts owed to other customers		**193.3**	260.9	211.0
Debt securities in issue		**2,816.0**	2,517.7	2,260.3
Other liabilities and accruals		**201.6**	184.8	188.7
Current tax liabilities		**11.2**	15.1	12.4
Deferred tax liabilities		**4.3**	2.1	4.3
Provisions for liabilities and charges	7	**4.0**	5.5	5.0
Subscribed capital		**231.1**	222.9	224.2
Total liabilities		**19,656.3**	18,510.6	18,363.6
Total equity attributable to members		**1,063.8**	984.9	1,026.5
Total liabilities and equity		**20,720.1**	19,495.5	19,390.1

Note: 'Deferred tax liabilities' and 'Total equity attributable to members' at 30 June 2018 have been amended to reflect the finalisation of the tax impacts of the adoption of IFRS 9 from 1 January 2018. The amended figures are consistent with the 31 December 2018 position disclosed in the 2018 Annual Report and Accounts.

Condensed Consolidated Statement of Changes in Members' Interest

Six months to 30 June 2019	General reserve £M	Fair value reserve £M	Revaluation reserve £M	Other reserve £M	Total equity attributable to members £M
At 1 January 2019 (Audited)	1,006.3	(2.3)	8.2	14.3	1,026.5
Comprehensive income for the period	35.2	2.1	-	-	37.3
Revaluation gains transferred on disposal of assets	0.2	-	(0.2)	-	-
At 30 June 2019 (Unaudited)	**1,041.7**	**(0.2)**	**8.0**	**14.3**	**1,063.8**

Six months to 30 June 2018	General reserve £M	Fair value reserve £M	Revaluation reserve £M	Other reserve £M	Total equity attributable to members £M
At 1 January 2018 (Audited)	931.3	2.3	11.1	14.3	959.0
Impact of adoption of IFRS9 at 1 January 2018	(26.4)	0.2	-	-	(26.2)
Tax relating to adoption of IFRS9 at 1 January 2018	6.5	-	-	-	6.5
At 1 January 2018 (Restated)	911.4	2.5	11.1	14.3	939.3
Comprehensive income for the period	47.9	(2.3)	-	-	45.6
Revaluation gains transferred on disposal of assets	0.8	-	(0.8)	-	-
At 30 June 2018 (Unaudited)	960.1	0.2	10.3	14.3	984.9

Year to 31 December 2018	General reserve £M	Fair value reserve £M	Revaluation reserve £M	Other reserve £M	Total equity attributable to members £M
At 1 January 2018 (Audited)	931.3	2.3	11.1	14.3	959.0
Impact of adoption of IFRS9 at 1 January 2018	(26.4)	0.2	-	-	(26.2)
Tax relating to adoption of IFRS9 at 1 January 2018	6.5	-	-	-	6.5
At 1 January 2018 (Restated)	911.4	2.5	11.1	14.3	939.3
Comprehensive income for the year	93.9	(4.8)	(1.9)	-	87.2
Revaluation gains transferred on disposal of assets	1.0	-	(1.0)	-	-
At 31 December 2018 (Audited)	1,006.3	(2.3)	8.2	14.3	1,026.5

Note: For the six months to 30 June 2018 the tax impacts of the adoption of IFRS 9 have been amended to reflect the finalised position. The amended figures are consistent with those for the year to 31 December 2018 disclosed in the 2018 Annual Report and Accounts.

Condensed Consolidated Statement of Cash Flows

	Six months to 30 June 2019 (Unaudited) £M	Six months to 30 June 2018 (Unaudited) £M	Year to 31 December 2018 (Audited) £M
Profit before tax	**49.4**	60.1	116.9
Adjusted for changes in:			
Impairment provision	**0.3**	(0.3)	(15.8)
Provisions for liabilities and charges	**(1.0)**	(0.9)	(1.4)
Depreciation and amortisation	**3.7**	1.8	4.0
Loss on sale of financial assets	**-**	6.9	6.5
Non-cash and other items	**(32.0)**	13.8	(20.5)
Cash generated from operations	**20.4**	81.4	89.7
Changes in operating assets and liabilities:			
Derivative financial instruments	**3.7**	(35.2)	(43.6)
Loans and advances to customers	**(685.6)**	(481.8)	(813.6)
Other operating assets	**(71.9)**	50.1	40.1
Shares	**728.2**	782.9	838.0
Amounts owed to credit institutions and other customers	**(66.6)**	340.2	404.4
Other operating liabilities	**25.2**	(27.8)	34.1
Taxation paid	**(13.7)**	(15.6)	(31.2)
Net cash flows from operating activities	**(60.3)**	694.2	517.9
Cash flows from investing activities			
Purchase of investment securities	**(2,559.0)**	(814.9)	(1,995.1)
Proceeds from sale and redemption of investment securities	**2,534.0**	289.4	1,539.0
Purchase of intangible assets	**(1.7)**	(1.3)	(4.5)
Purchase of property, plant and equipment	**(4.6)**	(2.7)	(4.6)
Proceeds from sale of property, plant and equipment	**0.4**	1.7	2.2
Net cash flows from investing activities	**(30.9)**	(527.8)	(463.0)
Cash flows from financing activities			
Net proceeds from issue of debt securities	**650.4**	56.5	93.0
Repayments of debt securities in issue	**(89.6)**	(386.6)	(701.0)
Net proceeds from issue of subscribed capital	**-**	197.9	199.2
Net cash flows from financing activities	**560.8**	(132.2)	(408.8)
Net increase/(decrease) in cash and cash equivalents	**469.6**	34.2	(353.9)
Cash and cash equivalents at the beginning of the period	**1,597.7**	1,951.6	1,951.6
Cash and cash equivalents at the end of the period	**2,067.3**	1,985.8	1,597.7

Note: The presentation of certain items for the six months to 30 June 2018 has been amended to align to the presentation for the year to 31 December 2018 in the 2018 Annual Report and Accounts. This resulted in a £1.9m reduction in 'Net cash flows from operating activities' and corresponding increase in 'Net cash flows from investing activities'.

Notes to the Accounts

1. General information

Reporting period

The Interim Financial Report is for the six months to 30 June 2019 and is unaudited.

Basis of preparation

This condensed consolidated set of financial statements has been prepared in accordance with the International Accounting Standard ("IAS") 34 – Interim Financial Reporting, as adopted by the European Union. It does not include all the information required by International Financial Reporting Standards ("IFRS") in full annual financial statements and should be read in conjunction with the Annual Report and Accounts for the year ended 31 December 2018 which was prepared in accordance with IFRS as adopted by the EU.

These financial statements are presented in sterling and, except where otherwise indicated, have been rounded to the nearest one hundred thousand pounds.

The following IFRS pronouncements, relevant to the Group, were adopted with effect from 1 January 2019:

IFRS 16 – Leases
IFRIC 23 – Uncertainty over Income Tax Treatments

The adoption of IFRS 16 has impacted the Statement of Financial Position of the Group and this is disclosed further in note 2.

The adoption of IFRIC 23 has not resulted in any material changes to the accounting policies or financial statements of the Group. Other amendments to IFRS which are effective from 1 January 2019 have not had a material impact on the financial statements of the Group.

At the date of authorisation of these financial statements, the following standards and interpretations (which have not been applied in these financial statements) were in issue but not yet effective:

IFRS 17 – Insurance Contracts

IFRS 17, which is effective from 1 January 2022, is not expected to have a material impact on the Group since the Group does not issue insurance contracts. The Group holds a collateral loan which represents a pool of equity release mortgages purchased from a third party and is currently accounted for under IFRS 9 – Financial Instruments. The Group expects to continue to apply IFRS 9 to this loan following the adoption of IFRS 17, as permitted by the scope exclusion proposed in ED/2019/4 – Amendments to IFRS 17.

Accounting policies and judgements

The Group's revised accounting policy for leases, following adoption of IFRS 16, is set out in note 2. The Group's remaining accounting policies, presentation and methods of computation are consistent with those applied by the Group in its latest audited annual financial statements, which can be found in note 1 to the 2018 Annual Report and Accounts.

Segmental reporting

As reported in note 1(n) of the 2018 Annual Report and Accounts, the Group has determined that it has one reportable segment under IFRS 8 and therefore no separate segmental reporting is provided.

Going concern

The directors have reviewed the Group's financial position and future plans and forecasts, considering current economic and market conditions (including the possible impact of the UK's exit from the European Union) and the potential risks to the business as set out in the 2018 Annual Report and Accounts. In this context the directors consider that the Group has a resilient business model, maintains an appropriate level of liquidity to meet both the normal demands of the business and the requirements which might arise in modelled stressed circumstances and that current capital resources and plans for future capital generation are sufficient to maintain capital in excess of regulatory requirements. Accordingly, the going concern basis has been adopted in the preparation of the Interim Financial Report.

2. Impact of adoption of IFRS 16 - Leases

a. Introduction

IFRS 16 – Leases was adopted by the Group from 1 January 2019. The standard replaces IAS 17 – Leases and specifies how an entity will recognise, measure, present and disclose leases. The objective of the new standard is to ensure that lessees and lessors provide information which fully represents the lease transactions in which the entity is involved.

The impact on the Group is to bring the majority of leases where the Group is a lessee on-balance sheet. Leased assets are recognised as 'right-of-use' assets within 'Property, plant and equipment' and a corresponding lease liability is recognised within 'Other liabilities and accruals' in the Statement of Financial Position. The right-of-use asset is depreciated while interest expense is charged on the lease liability. Previously operating lease costs were recorded within administrative expenses within the Income Statement.

The Group has chosen to apply the 'modified retrospective' approach to transition. The cumulative effect of initially applying the standard is applied to the opening balance sheet at 1 January 2019 and comparative information has not been restated. Further, for all leases, the Group has chosen to measure the right-of-use asset at an amount equal to the lease liability.

The Group has applied the practical expedient permitted to recognise all leases which end within 12 months of the date of adoption as short term leases, resulting in no right-of-use asset or lease liability being recognised for these leases.

The adoption of IFRS 16 has had no impact on how the Group accounts for leases where it is the lessor.

b. Accounting policy – leases

The new accounting policy adopted by the Group from 1 January 2019 in relation to leases is detailed below:

The Group classifies all contracts which give the right to control the use of an identified asset for a period of time in exchange for a consideration as leases. If the supplier of the asset has a substitution right then this is not classified as an asset and the contract is not classified as a lease.

Lessee

At the commencement of a lease, the Group recognises a right-of-use asset within 'Property, plant and equipment' and a lease liability within 'Other liabilities and accruals' in the Statement of Financial Position. The lease liability is initially measured at the present value of all contractual payments that are not paid at the commencement date, discounted using the Group's cost of borrowing at the date of inception of the lease. The calculation of the lease liability reflects the Group's judgement as to whether it will exercise a purchase, extension or termination option. For leases of land and buildings, the Group has elected not to separate non-lease components and account for the lease and non-lease components as a single lease component.

Interest is charged on the lease liability at the Group's cost of borrowing at the date of inception of the lease and recorded in 'Interest payable and similar charges' within the Income Statement.

The lease liability is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Group's estimate of the amount expected to be payable under a residual value guarantee, or if the Group changes its assessment of whether it will exercise a purchase, extension or termination option. When the lease liability is remeasured in this way, a corresponding adjustment is made to the right-of-use asset, or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

The right-of-use asset is initially measured at an amount equal to the lease liability. It is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term (or the end of the estimated useful life for the equivalent item of property, plant and equipment if shorter). Right-of-use assets are reviewed annually for indications of impairment. Impairment losses are recognised immediately as an expense in the Income Statement.

Notes to the Accounts (continued)

2. Impact of adoption of IFRS 16 - Leases (continued)

b. Accounting policy – leases (continued)

No right-of-use asset or lease liability is recognised for leases with a lease term of less than 12 months and leases of low value items. Lease payments associated with these leases are recognised as an expense on a straight line basis over the lease term.

Lessor

All of the Group's leases where the Group acts as a lessor are classified as operating leases. The Group recognises lease payments received under operating leases in line with receipt of payments.

c. Financial impact

The Group has a number of short leasehold properties which are used as branches and office accommodation. Right-of-use assets totalling £13.4 million have been recognised at 1 January 2019 in respect of these properties, with corresponding lease liabilities of £13.4 million. The weighted average incremental borrowing rate used as the discount rate in the calculation of lease liabilities recognised in the Statement of Financial Position at 1 January 2019 was 2.88%.

The operating lease commitments at 31 December 2018 disclosed in note 29(d) of the 2018 Annual Report and Accounts are reconciled to the lease liability recognised on 1 January 2019 below:

	£M
Operating lease and service contract commitments at 31 December 2018	43.0
Service contracts which do not meet the definition of a lease (note (i))	(34.3)
Operating leases recognised as short term leases on adoption of IFRS 16	(0.1)
Operating leases commencing after 1 January 2019 (note (ii))	(0.9)
Additional lease payments included in calculation of lease liability (note (iii))	7.0
Impact of discounting (note (iv))	(1.3)
Lease liability recognised on 1 January 2019	13.4

(i) The Group is committed to a multi-year service contract for the provision and maintenance of its IT infrastructure which was disclosed in note 29(d) of the 2018 Annual Report and Accounts. This contract does not provide the Group with the right to control the use of an identified asset and therefore does not meet the definition of a lease under IFRS 16.

(ii) Leases signed before 31 December 2018 which were therefore included in operating lease commitments disclosed at 31 December 2018 but did not commence until after 1 January 2019 are excluded from the lease liability recognised at 1 January 2019.

(iii) Operating lease commitments disclosed at 31 December 2018 represented the minimum contractual commitments, assuming that termination options were exercised where this was possible at the discretion of the lessee. Under IFRS 16, the lease liability calculation takes into account the Group's expected behaviour in respect of future termination options.

(iv) Previously, undiscounted commitments were disclosed, whereas the lease liability represents the discounted value of future lease payments.

Notes to the Accounts (continued)

3. Interest receivable and similar income

	Six months to 30 June 2019 (Unaudited) £M	Six months to 30 June 2018 (Unaudited) £M	Year to 31 December 2018 (Audited) £M
Interest receivable calculated using the effective interest rate method:			
On loans fully secured on residential property	**218.8**	218.7	442.2
On other loans and advances to customers	**0.5**	1.6	2.4
On investment securities	**6.8**	4.3	10.2
On other liquid assets	**6.5**	5.5	12.8
Total interest receivable calculated using the effective interest rate method	**232.6**	230.1	467.6
Similar income on instruments held at fair value through profit or loss:			
On other loans and advances to customers	**4.9**	6.7	13.0
On investment securities	**-**	0.1	0.2
Net expense on derivatives which hedge financial assets and are designated in accounting hedge relationships	**(7.5)**	(11.4)	(18.7)
Net expense on derivatives which hedge financial assets and are not designated in accounting hedge relationships	**(2.4)**	(2.5)	(5.1)
Total similar income on instruments held at fair value through profit or loss	**(5.0)**	(7.1)	(10.6)
Assets classified as held for sale	**-**	1.0	-
Total interest receivable and similar income	**227.6**	224.0	457.0
Included in the above is:			
Interest receivable on impaired financial assets	**1.3**	1.4	2.1

4. Interest payable and similar charges

	Six months to 30 June 2019 (Unaudited) £M	Six months to 30 June 2018 (Unaudited) £M	Year to 31 December 2018 (Audited) £M
Interest payable on instruments not held at fair value through profit or loss			
On shares held by individuals	**95.2**	85.1	175.7
On deposits and other borrowings	**31.9**	33.4	69.1
On subscribed capital	**5.4**	3.0	8.5
Total interest payable on instruments not held at fair value through profit or loss	**132.5**	121.5	253.3
Similar charges on instruments held at fair value through profit or loss			
On shares held by individuals	**-**	0.3	0.3
Net income on derivatives which hedge financial liabilities and are designated in accounting hedge relationships	**(5.2)**	(5.2)	(7.9)
Net expense/(income) on derivatives which hedge financial liabilities and are not designated in accounting hedge relationships	**2.3**	(2.2)	(6.8)
Total similar charges on instruments held at fair value through profit or loss	**(2.9)**	(7.1)	(14.4)
Total interest payable and similar charges	**129.6**	114.4	238.9

Notes to the Accounts (continued)

5. Administrative expenses

	Six months to 30 June 2019 (Unaudited) £M	Six months to 30 June 2018 (Unaudited) £M	Year to 31 December 2018 (Audited) £M
Staff costs			
Wages and salaries	**21.7**	22.6	49.0
Social security costs	**2.7**	2.3	4.9
Other pension costs	**3.3**	2.7	6.5
Other staff costs	**2.2**	2.2	1.0
Remuneration of auditor	**0.2**	0.3	0.6
Other administrative expenses			
Technology	**5.6**	5.6	10.3
Property	**2.1**	3.5	6.6
Marketing	**2.1**	2.2	3.1
Other	**6.3**	5.7	12.9
Total administrative expenses	**46.2**	**47.1**	**94.9**

6. Impairment on loans and advances to customers

	Six months to 30 June 2019 (Unaudited) £M	Six months to 30 June 2018 (Unaudited) £M	Year to 31 December 2018 (Audited) £M
Loans fully secured on residential property	**3.0**	0.7	2.4
Loans fully secured on land	**(0.9)**	(3.2)	(3.6)
Total impairment losses / (gains) for the period	**2.1**	(2.5)	(1.2)

Notes to the Accounts (continued)

7. Provisions

The provisions charge/(release) and provisions at the end of the period are shown below.

	Six months to 30 June 2019 (Unaudited) £M	Six months to 30 June 2018 (Unaudited) £M	Year to 31 December 2018 (Audited) £M
Provisions charge / (release)			
FSCS levy	**-**	(0.3)	(0.3)
Customer redress and related provisions	**-**	(0.3)	(0.2)
Property related	**(0.2)**	-	-
Other provisions	**(0.2)**	-	0.3
Total provisions release	**(0.4)**	(0.6)	(0.2)
Liabilities			
FSCS levy	**-**	0.7	0.3
Customer redress and related provisions	**3.6**	4.3	3.9
Commission clawback	**0.3**	0.3	0.3
Property related	**-**	0.2	0.2
Other provisions	**0.1**	-	0.3
Provisions at the end of the period	**4.0**	5.5	5.0

The Group has a contingent liability in respect of contributions to the Financial Services Compensation Scheme provided by the Financial Services and Markets Act 2000. At 30 June 2019 no levies were due.

8. Taxation

The standard rate of corporation tax applicable to the Group for the six months ended 30 June 2019 was 19% (six months ended 30 June 2018: 19%, full year ended 31 December 2018: 19%). A reduction in the UK corporation tax rate from 19% to 18% (effective 1 April 2020) was substantively enacted on 26 October 2015, and an additional reduction to 17% (also effective 1 April 2020) was substantively enacted on 6 September 2016. The Finance (No. 2) Act 2015 introduced an additional surcharge of 8% on banking profits (including those of building societies) above a £25m threshold from 1 January 2016.

Deferred tax balances have been calculated at a rate of 25% (inclusive of the 8% banking levy), as it is expected that these balances will mostly reverse after 1 April 2020.

Notes to the Accounts (continued)

9. Loans and advances to customers

30 June 2019 (Unaudited)	Gross balance £M	Impairment loss provision £M	Total £M
Loans fully secured on residential property	**16,503.8**	**(28.9)**	**16,474.9**
Loans fully secured on land	**20.6**	**(3.1)**	**17.5**
Other loans	**228.9**	**(2.5)**	**226.4**
Total loans and advances to customers	**16,753.3**	**(34.5)**	**16,718.8**

30 June 2018 (Unaudited)	Gross balance £M	Impairment loss provision £M	Total £M
Loans fully secured on residential property	15,291.4	(27.5)	15,263.9
Loans fully secured on land	59.9	(13.2)	46.7
Other loans	244.3	(2.5)	241.8
Total loans and advances to customers	15,595.6	(43.2)	15,552.4

31 December 2018 (Audited)	Gross balance £M	Impairment loss provision £M	Total £M
Loans fully secured on residential property	15,804.8	(27.7)	15,777.1
Loans fully secured on land	30.8	(4.0)	26.8
Other loans	232.0	(2.5)	229.5
Total loans and advances to customers	16,067.6	(34.2)	16,033.4

The Group continues to use forbearance arrangements to assist its arrears management strategies to minimise credit risk whilst ensuring that customers are treated fairly. This includes the use of arrangements to assist borrowers in arrears who are now able to meet agreed repayment strategies, including or excluding arrears balances. The Group's approach to forbearance is described on page 149 of the 2018 Annual Report and Accounts and is materially unchanged.

10. Retirement benefit surplus

	30 June 2019 (Unaudited) £M	30 June 2018 (Unaudited) £M	31 December 2018 (Audited) £M
Present value of pension scheme's liabilities	**(111.2)**	(105.8)	(102.5)
Scheme assets at fair value	**119.7**	112.0	112.6
Pension scheme surplus	**8.5**	6.2	10.1

The Group operates both defined benefit and defined contribution schemes. The defined benefit scheme provides benefits based on final salary for certain employees. It closed for future accruals on 31 December 2014. The surplus on the scheme has reduced since 31 December 2018 due to changes in the prevailing interest rate environment.

Notes to the Accounts (continued)

11. Related party transactions

The Group had no related party transactions outside the normal course of business in the six months ended 30 June 2019 (June 2018: £nil, December 2018: £nil).

12. Financial commitments

The Group has commitments of £22.1m (June 2018: £nil, December 2018: £1.5m) payable under executory contracts which relate to technology investment programmes and the refurbishment of the Society's new head office. This amount is inclusive of value added tax.

13. Credit risk on loans and advances to customers

a. Retail mortgages

A full analysis of credit risk on retail mortgages is included in note 31 of the 2018 Annual Report and Accounts.

The table below provides information on the Group's retail mortgages by payment due status, excluding impairment loss provisions. The table includes £11.6m (June 2018: £10.3m, December 2018: £11.7m) of loans and advances secured on residential property in Spain that are past due and £0.6m (June 2018: £0.7m, December 2018: £0.5m) in possession.

	30 June 2019 (Unaudited)		30 June 2018 (Unaudited)		31 December 2018 (Audited)	
	£M	**%**	£M	%	£M	%
Not past due	**16,237.9**	**98.4**	14,951.8	97.9	15,552.2	98.4
Past due up to 3 months	**192.0**	**1.2**	267.4	1.7	190.8	1.2
Past due 3 to 6 months	**37.7**	**0.2**	36.3	0.2	28.5	0.2
Past due 6 to 12 months	**18.9**	**0.1**	19.6	0.1	18.4	0.1
Past due over 12 months	**10.8**	**0.1**	10.3	0.1	9.5	0.1
Possessions	**6.5**	**-**	6.0	-	5.4	-
Total	**16,503.8**	**100.0**	15,291.4	100.0	15,804.8	100.0

The Group's policy for calculating impairment of loans and advances to customers is detailed in note 1 of the 2018 Annual Report and Accounts. The table below summarises the Group's retail mortgage balances, loan commitments and associated impairment loss provisions:

	30 June 2019 (Unaudited)			30 June 2018 (Unaudited)		
	Gross exposure	**Impairment loss provision**	**Provision coverage**	Gross exposure	Impairment loss provision	Provision coverage
	£M	**£M**	**%**	£M	£M	%
Retail mortgages						
Stage 1	**14,963.6**	**5.1**	**0.03**	13,696.5	2.4	0.02
Stage 2 and <30 days past due	**1,278.8**	**8.1**	**0.63**	1,332.2	7.2	0.54
Stage 2 and 30+ days past due	**90.9**	**1.4**	**1.55**	73.9	1.1	1.45
Stage 3	**170.5**	**14.3**	**8.37**	188.8	16.8	8.89
Total retail mortgages	**16,503.8**	**28.9**	**0.18**	15,291.4	27.5	0.18
Loan commitments						
Stage 1	**699.9**	**-**	**0.01**	670.3	-	-

Notes to the Accounts (continued)

13. Credit risk on loans and advances to customers (continued)

a. Retail mortgages (continued)

	31 December 2018 (Audited)		
	Gross exposure £M	Impairment loss provision £M	Provision coverage %
Retail mortgages			
Stage 1	14,189.0	3.9	0.03
Stage 2 and <30 days past due	1,369.0	8.4	0.62
Stage 2 and 30+ days past due	73.9	1.4	1.81
Stage 3	172.9	14.0	8.10
Total retail mortgages	15,804.8	27.7	0.18
Loan commitments			
Stage 1	675.8	-	0.01

Retail mortgages are all fully secured on residential property. The indexed loan to value analysis of the Group's retail mortgage portfolio is as follows:

	30 June 2019 (Unaudited) %	30 June 2018 (Unaudited) %	31 December 2018 (Audited) %
<70%	**78.9**	75.7	79.1
70% - 80%	**12.0**	13.3	11.7
80% - 90%	**6.7**	7.9	7.0
>90%	**2.4**	3.1	2.2
Total percentage	**100.0**	100.0	100.0

The overall weighted average indexed loan to value of the residential portfolio is 54% (June 2018: 56%, December 2018: 55%).

b. Commercial loans

A full analysis of credit risk on commercial loans is included in note 31 to the 2018 Annual Report and Accounts.

The table below provides information on the Group's commercial loans by payment due status, excluding impairment loss provisions.

	30 June 2019 (Unaudited)		30 June 2018 (Unaudited)		31 December 2018 (Audited)	
	£M	**%**	£M	%	£M	%
Not past due	**20.6**	**100.0**	59.0	98.5	30.8	100.0
Possessions	**-**	**-**	0.9	1.5	-	-
Total	**20.6**	**100.0**	59.9	100.0	30.8	100.0

Notes to the Accounts (continued)

13. Credit risk on loans and advances to customers (continued)

b. Commercial loans (continued)

The table below summarises the Group's commercial loan balances and associated impairment loss provisions:

	30 June 2019 (Unaudited)			30 June 2018 (Unaudited)		
	Gross exposure	**Impairment loss provision**	**Provision coverage**	Gross exposure	Impairment loss provision	Provision coverage
	£M	**£M**	**%**	£M	£M	%
Commercial loans						
Stage 1	**-**	**-**	**-**	-	-	-
Stage 2 and <30 days past due	**12.9**	**2.5**	**19.2**	31.8	3.8	12.0
Stage 2 and 30+ days past due	**-**	**-**	**-**	-	-	-
Stage 3	**7.8**	**0.7**	**8.3**	28.1	9.4	33.5
Total commercial loans	**20.7**	**3.2**	**15.5**	59.9	13.2	22.1

	31 December 2018 (Audited)		
	Gross exposure	Impairment loss provision	Provision coverage
	£M	£M	%
Commercial loans			
Stage 1	-	-	-
Stage 2 and <30 days past due	23.1	3.3	14.5
Stage 2 and 30+ days past due	-	-	-
Stage 3	7.7	0.7	9.4
Total commercial loans	30.8	4.0	12.9

The indexed loan to value analysis of the Group's commercial loan portfolio is as follows:

	30 June 2019 (Unaudited)	30 June 2018 (Unaudited)	31 December 2018 (Audited)
	%	%	%
<70%	**41.3**	27.5	28.7
70% - 80%	**-**	22.0	31.0
80% - 90%	**7.4**	3.5	5.0
>90%	**51.3**	47.0	35.3
Total percentage	**100.0**	100.0	100.0

The overall indexed loan to value of the commercial portfolio is 56% (June 2018: 81%, December 2018: 60%).

Notes to the Accounts (continued)

14. Fair values

a. Carrying value and fair value of financial instruments not carried at fair value

The table below compares the carrying and fair values of the Group's financial instruments not held at fair value at the reporting date. Where available, market values have been used to determine fair values. Where market values are not available, fair values have been calculated by discounting future cash flows at prevailing interest rates.

		30 June 2019 (Unaudited)		30 June 2018 (Unaudited)	
	Fair value hierarchy level	Carrying value £M	Fair value £M	Carrying value £M	Fair value £M
Financial assets					
Cash in hand and balances with the Bank of England	**Level 1**	**1,879.1**	**1,879.1**	1,822.1	1,822.1
Loans and advances to credit institutions	**Level 2**	**188.2**	**188.2**	163.7	163.7
Loans and advances to customers:					
Loans fully secured on residential property	**Level 3**	**16,474.9**	**16,948.9**	15,263.9	15,754.2
Other loans	**Level 2**	**17.5**	**17.5**	46.7	44.4
Financial liabilities					
Shares	**Level 2**	**14,637.6**	**14,656.2**	13,834.9	13,848.5
Amounts owed to credit institutions	**Level 2**	**1,350.4**	**1,350.4**	1,285.2	1,285.2
Amounts owed to other customers	**Level 2**	**193.3**	**193.3**	260.9	260.9
Debt securities in issue	**Level 1**	**2,690.8**	**2,935.9**	2,359.4	2,023.7
Debt securities in issue	**Level 2**	**125.2**	**125.3**	158.3	158.7
Subscribed capital	**Level 1**	**231.1**	**278.1**	222.9	222.9

		31 December 2018 (Audited)	
	Fair value hierarchy level	Carrying value £M	Fair value £M
Financial assets			
Cash in hand and balances with the Bank of England	Level 1	1,428.0	1,428.0
Loans and advances to credit institutions	Level 2	169.7	169.7
Loans and advances to customers:			
Loans fully secured on residential property	Level 3	15,777.1	16,251.2
Other loans	Level 2	26.8	26.8
Financial liabilities			
Shares	Level 2	13,909.5	13,922.6
Amounts owed to credit institutions	Level 2	1,399.3	1,399.3
Amounts owed to other customers	Level 2	211.0	211.0
Debt securities in issue	Level 1	2,123.5	2,318.1
Debt securities in issue	Level 2	136.8	136.9
Subscribed capital	Level 1	224.2	272.1

14. Fair values (continued)

b. Fair value measurement basis for financial instruments carried at fair value

The methodology and assumptions for determining the fair value of financial assets and liabilities are included in note 36 of the 2018 Annual Report and Accounts and remain materially unchanged since December 2018.

The tables below classify all assets and liabilities carried at fair value in the Statement of Financial Position according to the method used to establish their fair value.

As at 30 June 2019 (Unaudited)	Level 1 £M	Level 2 £M	Level 3 £M	Total £M
Assets				
Investment securities - At fair value through other comprehensive income	**319.5**	**936.5**	**-**	**1,256.0**
Derivative financial instruments	**-**	**255.4**	**23.1**	**278.5**
Loans and advances to customers	**-**	**-**	**226.4**	**226.4**
Fair value adjustment for hedged risk on loans and advances to customers	**-**	**-**	**73.9**	**73.9**
Total assets	**319.5**	**1,191.9**	**323.4**	**1,834.8**
Liabilities				
Fair value adjustment for hedged risk on shares	**-**	**-**	**6.0**	**6.0**
Derivative financial instruments	**-**	**100.3**	**100.5**	**200.8**
Total liabilities	**-**	**100.3**	**106.5**	**206.8**

As at 30 June 2018 (Unaudited)	Level 1 £M	Level 2 £M	Level 3 £M	Total £M
Assets				
Investment securities				
At fair value through other comprehensive income	610.7	690.1	-	1,300.8
At fair value through profit or loss	-	3.2	-	3.2
Derivative financial instruments	-	233.3	25.8	259.1
Loans and advances to customers	-	-	241.8	241.8
Fair value adjustment for hedged risk on loans and advances to customers	-	-	28.8	28.8
Assets classified as held for sale: loans and advances to customers	-	133.2	-	133.2
Total assets	610.7	1,059.8	296.4	1,966.9
Liabilities				
Shares	-	19.5	-	19.5
Fair value adjustment for hedged risk on shares	-	-	34.7	34.7
Derivative financial instruments	-	45.0	82.3	127.3
Total liabilities	-	64.5	117.0	181.5

14. **Fair values** (continued)

b. **Fair value measurement basis for financial instruments carried at fair value** (continued)

As at 31 December 2018 (Audited)	Level 1 £M	Level 2 £M	Level 3 £M	Total £M
Assets				
Investment securities - At fair value through other comprehensive income	457.0	772.1	-	1,229.1
Derivative financial instruments	-	248.5	24.9	273.4
Loans and advances to customers	-	-	229.5	229.5
Fair value adjustment for hedged risk on loans and advances to customers	-	-	18.0	18.0
Total assets	457.0	1,020.6	272.4	1,750.0
Liabilities				
Fair value adjustment for hedged risk on shares	-	-	15.7	15.7
Derivative financial instruments	-	35.6	97.6	133.2
Total liabilities	-	35.6	113.3	148.9

Level 1: Relates to financial instruments where fair values are derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Valuation techniques are used to value these instruments for which significant inputs are taken from observable market data for the asset and liability, either directly (market prices) or indirectly (derived prices) other than quoted prices included in Level 1. These include valuation models used to calculate the present values of expected future cash flows, using curves from published market sources and are employed when no active market exists or when no quoted prices for similar instruments can be obtained.

Level 3: The valuation of the asset or liability is not based on observable market data (unobservable inputs). Valuation techniques include net present value and discounted cash flow methods. The assumptions used in such models include risk-free benchmark interest rates, foreign currency exchange rates and expected price volatilities. The objective of the valuation techniques is to determine a fair value that reflects the price of the financial instrument that would have been used by two counterparties in an arm's length transaction.

There have been no transfers of assets or liabilities between the above levels of valuation during the period. Details of the recurring fair value measurements of assets and liabilities included in level 3 are included in the 2018 Annual Report and Accounts on page 169.

Notes to the Accounts (continued)

14. Fair values (continued)

c. Reconciliation of level 3 fair value measurements of financial instruments

Six months to 30 June 2019 (Unaudited)	**Financial assets £M**	**Financial liabilities £M**
Balance at 1 January 2019	**272.4**	**(113.3)**
Total (losses) / gains in the Income Statement	**(6.9)**	**(2.9)**
Movement in fair value adjustment for hedged risk on loans and advances to customers	**55.9**	**-**
Movement in fair value adjustment for hedged risk on shares	**-**	**9.7**
Net repayment in the period	**2.0**	**-**
Balance at 30 June 2019	**323.4**	**(106.5)**

Six months to 30 June 2018 (Unaudited)	Financial assets £M	Financial liabilities £M
Balance at 1 January 2018	291.5	(85.8)
Total (losses) / gains in the Income Statement	(11.1)	9.3
Movement in fair value adjustment for hedged risk on loans and advances to customers	16.3	-
Movement in fair value adjustment for hedged risk on shares	-	(40.5)
Net repayment in the period	(0.3)	-
Balance at 30 June 2018	296.4	(117.0)

Year to 31 December 2018 (Audited)	Financial assets £M	Financial liabilities £M
Balance at 1 January 2018	291.5	(85.8)
Total (losses) / gains in the Income Statement	(5.6)	(6.0)
Movement in fair value adjustment for hedged risk on loans and advances to customers	5.5	-
Movement in fair value adjustment for hedged risk on shares	-	(21.5)
Net repayment in the year	(19.0)	-
Balance at 31 December 2018	272.4	(113.3)

Notes to the Accounts (continued)

14. Fair values (continued)

d. Level 3 unobservable inputs

(i) Loans and advances to customers (collateral loan)

The collateral loan which represents a pool of equity release mortgages is valued using a discounted cash flow model which uses unobservable input assumptions for property price volatility, sales discount, mortality, early prepayment and the discount rate used to discount future cash flows. Wherever possible these input assumptions are calculated with reference to historic data. The variables which are considered to have the largest impact on the value of the loan are property price volatility and the discount rate. The sensitivities below reflect a range of alternative assumptions based on observed historic data and regulatory guidance.

At 30 June 2019, a 300 basis points increase in assumed property price volatility would reduce the value of the collateral loan by £5.5m and a 500 basis points decrease in assumed property price volatility would increase the value of the collateral loan by £8.2m. A 19 basis points increase in the discount rate would reduce the value of the collateral loan by £4.6m and a 41 basis points decrease in the discount rate would increase the value of the collateral loan by £10.8m.

(ii) Derivative financial instruments (securitisation swaps and equity release swaps)

The valuation of securitisation swaps is performed using models which utilise a combination of observable market interest rate data and unobservable assumptions about future mortgage prepayment. At 30 June 2019, a 20% proportionate increase in prepayments would lead to a decrease in the fair value of the swaps of less than £0.1m. A 20% proportionate reduction in prepayments would increase the fair value by less than £0.1m. These sensitivities reflect the variability in prepayment rates observed historically.

For equity release swaps, the valuation uses significant unobservable inputs which have not been developed by the Group. The Group is therefore not disclosing quantitative information regarding these inputs, in line with the permitted exemption under IFRS 13.

(iii) Fair value adjustment for hedged risk

The Group designates a portfolio of fixed rate mortgages into hedge relationships to mitigate interest rate risk and similarly for a portfolio of fixed rate savings. For the mortgage portfolio only, the calculation of the fair value uses observable market interest rate data and assumptions about projected prepayments. These prepayment assumptions are unobservable inputs that are calculated using historic data and reviewed periodically so that projections are broadly in line with actual data, with sensitivities calculated based on historic observed variability.

At 30 June 2019, a 20% proportionate increase in mortgage repayments would lead to a reduction in the fair value of the mortgages in the hedge relationship of £1.9 million. A 20% proportionate decrease in mortgage repayments would lead to an increase in the fair value of the mortgages of £2.0 million.

15. Events after the date of the Statement of Financial Position

There have been no material subsequent events between 30 June 2019 and the date of approval of this Interim Financial Report by the Board.

Notes to the Accounts (continued)

Cautionary statement

This Interim Financial Report has been prepared solely to provide additional information to members to assess the Group's financial position and the potential for its strategies to succeed. These statements should not be relied on by any other party or for any other purpose. The Interim Financial Report contains certain forward-looking statements. These statements are made by the directors in good faith based on the information available to them up to the time of their approval of this report. Such statements should be treated with caution due to the inherent uncertainties, including both economic and business risk factors, underlying any such forward-looking information.

Responsibility statement

We confirm that to the best of our knowledge:

- the condensed set of financial statements have been prepared in accordance with International Accounting Standard 34 'Interim Financial Reporting';
- the Interim Financial Report includes a fair review of the information required by DTR 4.2.7R (indication of important events during the first six months and description of principal risks and uncertainties for the remaining six months of the year); and,
- the Interim Financial Report includes a fair review of the information required by DTR 4.2.8R (disclosure of related parties' transactions and changes therein).

Signed on behalf of the Board of Directors:

Richard Fearon Chief Executive Officer	Andrew Greenwood Chief Risk Officer

1 August 2019

Independent Review Report to Leeds Building Society

We have been engaged by the Leeds Building Society (the "Society") to review the condensed set of financial statements in the Interim Financial Report for the six months ended 30 June 2019 which comprises the condensed consolidated income statement, the condensed consolidated statement of comprehensive income, the condensed consolidated statement of financial position, the condensed consolidated statement of changes in members' interest, the condensed consolidated statement of cash flows and related notes 1 to 15. We have read the other information contained in the Interim Financial Report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Society 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. Our work has been undertaken so that we might state to the Society those matters we are required to state to them in an independent review 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 Society, for our review work, for this report, or for the conclusions we have formed.

Directors' responsibilities

The Interim Financial Report is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the Interim Financial Report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

As disclosed in note 1, the annual financial statements of the group are prepared in accordance with IFRS as adopted by the European Union. The condensed set of financial statements included in this Interim Financial Report has been prepared in accordance with International Accounting Standard 34 'Interim Financial Reporting', as adopted by the European Union.

Our responsibility

Our responsibility is to express to the Society a conclusion on the condensed set of financial statements in the Interim Financial Report based on our review.

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 United Kingdom. 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. A review is substantially less in scope than an audit conducted in accordance with International Standards of 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.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the Interim Financial Report for the six months ended 30 June 2019 is not prepared, in all material respects, in accordance with the International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Deloitte LLP

Statutory Auditor

Leeds, United Kingdom

1 August 2019

Other Information

The financial information set out in the Interim Financial Report, which was approved by the Board of Directors on 1 August 2019, does not constitute statutory accounts within the meaning of the Building Societies Act 1986.

The financial information for the year ended 31 December 2018 has been extracted from the Annual Report and Accounts for that year. The Annual Report and Accounts have been filed with the Financial Conduct Authority.

The audit opinion for the 31 December 2018 annual statutory financial statements was unqualified and included no reference to any matter on which the auditor is required to report by exception.

A copy of the Interim Financial Report is placed on the Society's website. The directors are responsible for the maintenance and integrity of the information on the website. Information published on the internet is accessible in many countries with different legal requirements. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.