Interim Financial Report

30 June 2021

Leeds Building Society

2021: Our performance so far

Gross residential lending of

£2.0bn
(H1 2020: £1.0bn)

We helped **19,000** more people have the home they want

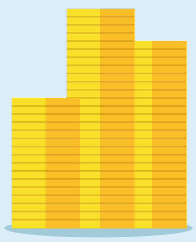
Total assets of

£21.1bn
(Dec 2020: £20.6bn)

Savings balances

£14.5bn
(Dec 2020: £14.2bn)

We helped **17,000** more people save for their future



Paid an average interest rate of

0.97%
to our savers
compared to rest of market average of **0.41%**[1]

An annual benefit to all our savers of almost **£78.5m**

Profit before tax

£70.3m
(H1 2020: £32.6m)

Common Equity Tier 1 Capital

37.6%
(Dec 2020: 36.3%)

Reserves available to protect us from future problems

Customer satisfaction[2]

93%
(2020: 93%)

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

Colleague engagement[3]

86%
(2020: 86%)

We're committed to being a great place to work

1. CACI's CSDB, Stock, June 2020 to May 2021, latest data available. **2.** Overall customer satisfaction in a survey of 1,634 customers January to June 2021. **3.** Your Voice colleague survey, 1,312 respondents in June 2021.

Chief Executive Officer's Review

Leeds Building Society has had a successful first half of 2021, providing a record level of support to the vibrant housing market.

Our strategy of supporting customers in under-served sectors has driven a successful six months as the housing market continued to trade strongly. This has included helping more than 8,600 first time buyers onto the housing ladder in 2021, a new record for any half year period and a record 37% share of the Society's new lending overall.

The rebound in home buying and remortgage activity since summer 2020 led to some of the biggest months for mortgage applications in Leeds Building Society's long history and, in 2021, our busiest ever half year.

Gross lending was up by 97% at £2.0 billion (six months to June 2020: £1.0 billion) which, together with an increase in net interest margin from 0.99% in 2020 to 1.23%[1], delivered half year profit before tax of £70.3 million (six months to June 2020: £32.6 million).

In responding to the ongoing challenges posed by the pandemic we've remained focused on our core purpose, to help people save and have the home they want, and kept our members at the heart of our long term business priorities.

We've supported the housing market at an exceptionally busy time, and supported our existing borrowers by offering mortgage payment deferrals, as well as waiving arrears fees until the end of this year.

We've supported our savers by keeping branches open for access to essential financial services and have carried on paying 0.56% above the market average rate[2], which equates to an extra £78.5 million in our savings members' pockets.

I'm immensely proud of my colleagues and their sustained efforts as the impact of the pandemic on our members has continued to evolve. Their professionalism and dedication served the Society well throughout 2020 and has been evident again during 2021, helping us to achieve an outstanding performance.

Whether it's developing new products or providing great service, our people have been integral to successes such as re-entering mainstream 95% loan to value ("LTV") lending, backing national affordable housing initiatives such as First Homes and Shared Ownership, and creating new 'green' products.

Having been able to accelerate our planned investment in 2020, we've now completed more steps to upgrade our IT systems, including introducing Lender Connect to save our intermediary partners time and effort. We're proceeding to plan with further major improvements to future-proof operations and boost resilience, such as our new data centres.

This investment programme will benefit our membership as a whole by enabling greater efficiencies, reducing costs and cutting our environmental impact.

In reporting 2020's results, we set out our strategic aim to be carbon net neutral for scope 1 and 2 emissions by the end of 2022[3] and are on target to achieve this 12 months early, as we continue to invest significant effort in progressing our responsible business strategy.

At a time when other employers have been laying off staff or placing them on furlough, I'm pleased we've done neither and instead have been able to carry on investing in skills and created more than 80 new roles.

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[1] Net interest margin is calculated as net interest income divided by mean total assets.

[2] We paid an average rate of 0.97% to our savers, compared to the rest of the market average rate of 0.41%. CACI's CSDB, Stock, June 2020 to May 2021, latest data available.

[3] Part of our Climate Change Framework, based on four pillars (Risk Management and Scenario Analysis, Reporting and Disclosure, Carbon Footprint and Products), designed to meet the requirements of TCFD on a proportionate basis. Scope 1 covers direct emissions from owned or controlled sources; scope 2 covers indirect emissions from the generation of purchased electricity, steam, heating and cooling consumed by the reporting company; and scope 3 includes all other indirect emissions that occur in a company's value chain.

These have been concentrated on strengthening important functions such as IT and data, as well as adding more underwriters and business development managers to improve service for our intermediary partners.

In addition, we're increasing our minimum full time equivalent ("FTE") salary to £18,200 per annum, a new base salary level for colleagues of £10 per hour, above and beyond our commitment as an accredited Living Wage Employer, and 50p per hour more than the Real Living Wage outside London.

It's a landmark year for us in 2021 and we're using learnings from the pandemic to ensure we keep on evolving. Having completed the move into our EPC A-rated new head office in Sovereign Street, we're experimenting with the flexible space it offers to find the right balance for hybrid working, and we're really looking forward to the imminent opening of our newest, largest branch in Leeds city centre.

While we retain our focus on efficiency, increased operating costs for 2021 were anticipated to reflect the scale of investment in future-proofing the Society and its operations for years to come. Despite that, cost to income and cost to mean asset ratios of 44.9% and 0.56% respectively (year to December 2020: 51.0% and 0.48%) remain among the best in the building society sector.

The Society maintained its cautious approach to navigating the pandemic, with tighter lending policy and criteria than before the pandemic, strong liquidity levels well above regulatory requirements and appropriate levels of provisions to reflect the fact economic conditions remain volatile and uncertain. Total arrears remain at a low level, comparing favourably against industry benchmarks[4], and we continue to retain extremely strong levels of capital.

Pleasingly, customer satisfaction and colleague engagement scores remain at record highs, at 93% and 86% respectively, and both groups have continued their enthusiastic support for our national charity partner, Dementia UK. In May the partnership launched Closer to Home, to increase access to specialist dementia clinics for communities across the UK.

The pandemic has created obstacles for all of us to overcome but for almost a century and a half the Society's strength has protected our security and independence through previous periods of economic and social upheaval.

The trust of our members and support of our intermediary partners is all the more valued in today's testing times and the faith they have placed in us, combined with our strong performance, gives me added confidence when I look to our future.

Richard Fearon

Chief Executive Officer

[4] The Society's total arrears greater than 2.5% of balance at 30 June 2021 were lower than the market average (Source: UK Finance: Mortgage Arrears and Possessions Update Quarter 1 2021).

2021 First Half Key Performance Indicators

Our vision to be Britain's most successful building society continues to be supported by our strategic pillars: Secure, Customer Centred, Simple and Future Facing, all underpinned by our People. Our corporate priorities support each of our strategic pillars and are:

- Safely keeping the Society operating for the benefit of our members;
- Keeping the Society financially resilient; and
- Informing and engaging colleagues and customers.

The Society measures its performance against its strategic pillars using key performance indicators ("KPIs"). The 2021 first half KPIs, aligned to the strategic pillars, are shown below. The KPIs are the same as those used in the 2020 Annual Report and Accounts and comparative figures are shown for the full year unless otherwise stated.

Some of the KPIs are Alternative Performance Measures ("APMs"). These are measures that are not defined in accounting standards but are useful in explaining the performance of the business. The APMs used in this report are in common use across the financial services industry. These APMs and other terms used in this report are explained and reconciled to the equivalent statutory measure in the Glossary on pages 207 to 210 of the 2020 Annual Report and Accounts.

Secure

Generate strong sustainable profit levels by meeting the needs of key segments.

Profit before tax	**£70.3 million** Six months to June 2020: £32.6 million	Profit before tax has increased from 2020 driven by significantly higher net interest income and lower impairment and fair value charges from a more positive macroeconomic outlook.
Net interest margin APM	**1.23%** Year to December 2020: 0.99%	Net interest margin has increased from 2020 due to strong lending margins and low funding costs.
Common Equity Tier 1 ("CET1") ratio	**37.6%** December 2020: 36.3%	The CET1 ratio increased as the Society continues to generate profits, while capital requirements have remained relatively static.
UK leverage ratio	**5.9%** December 2020: 5.8%	The UK leverage ratio has been increased through careful management of the Society's balance sheet and elevated profits. It remains well above the regulatory minimum of 3.25%.
New (gross) residential lending APM	**£2.0 billion** Six months to June 2020: £1.0 billion	Strong demand in the mortgage market has allowed the Society to support key segments and driven high levels of new lending whilst maintaining the credit quality criteria of the loan book.
Net residential lending APM	**£0.6 billion** Six months to June 2020: £(0.1) billion	Net lending has increased during 2021 as a result of high demand for lending products across the sector exceeding elevated redemptions, with more people looking to relocate.

2021 First Half Key Performance Indicators

Customer Centred

Deliver an outstanding member and broker experience.

Customer satisfaction	**93%** Year to December 2020: 93%	Customer satisfaction has remained high as the Society continues to focus on serving its mortgage and savings members.
Broker Net Promoter Score	**53** Year to December 2020: 46	The significant investment made in systems and processes in 2020 has continued into 2021 with further improvements to the broker experience reflected in the Net Promoter Score.
Savings balances	**£14.5 billion** December 2020: £14.2 billion	Savings balances have risen as the Society has offered good value products with excellent service in a low market rate environment. The growth in savings, as well as wholesale funding, has supported the Society by funding mortgage growth.
Society membership	**771,000 members** December 2020: 769,000 members	The number of members increased slightly as a result of the rise in mortgage lending and savings balances.
Savings rate benefit	**£78.5 million** Year to December 2020: £82.8 million	The Society is committed to its members and so consistently pays above the market average for its savings products.

Simple

Drive efficiency by removing complexity.

Cost to income ratio APM	**44.9%** Year to December 2020: 51.0%	The Society has continued to maintain tight control on costs. Although costs have increased compared to 2020, this has been at a slower rate than the growth in income, which has driven an improvement in the cost to income ratio.
Cost to mean asset ratio APM	**0.56%** Year to December 2020: 0.48%	The cost to mean asset ratio has increased reflecting investment in technological change, ahead of balance sheet growth, and increases in certain costs where spending was temporarily supressed during 2020.
Number of days from mortgage application to offer	**21 days** Year to December 2020: 24 days	The number of days from application to offer has decreased as the pressures on this metric from the pandemic have partly eased, supported by increased investment in our offering to drive efficiencies.

People

People underpin our strategy to help deliver priorities under our strategic pillars.

Colleague engagement score	**86%** Year to December 2020: 86%	Colleague engagement remains high. The Society is underpinned by our people and colleague engagement is a priority.

Financial performance

The Society has delivered strong profits and supported members with significant net lending in the first six months of 2021. Our prompt responses to the impacts of the pandemic and our robust underlying financial position have allowed us to thrive despite the continued uncertainty about the impacts of COVID-19.

The Group's profit before tax for the first six months of 2021 was £70.3 million (six months to June 2020: £32.6 million). This performance has been driven by growth in net interest income, partly from higher lending volumes, and the stabilisation of impairment charges. We have continued to support borrowers less well served by the wider market, such as shared ownership customers, as well as first time buyers and later life homeowners, and this has contributed to the increase in lending volumes in the period. We are proud of this continued support for members using our expertise throughout the pandemic, while maintaining a prudent approach to overall lending.

Net interest income

	Six months to June 2021 £m	Six months to June 2020 £m	Year to December 2020 £m
Net interest income	127.7	99.7	205.4
Mean total assets	20,864	20,670	20,724
	%	%	%
Net interest margin APM	**1.23**	**0.96**	**0.99**

Net interest income is the Society's principal form of revenue. Throughout the first half of 2021, we have continued to balance the needs of our members. We offered competitive rates to those in need of mortgages and worked hard to continue to provide an above market return to savers. We paid an average rate of 0.97% to our savers, compared to the rest of the market average rate of 0.41%[1]. We provide residential mortgages in the UK, through a network of approved mortgage brokers and directly to customers through online and telephone channels, to help members have the home they want. The Society funds the majority of mortgage lending with members' savings, through a range of channels, while the remainder is funded from other financial institutions, including through central bank schemes, on competitive terms.

Net interest margin has increased in the first half of 2021, continuing the trend seen in the second half of 2020. Higher margins earned on new loans reflect the strength of the housing market since it reopened in summer 2020, with significant demand for house moves at the same time as supply of mortgages across the market was restricted due to the pandemic. Our experience and expertise in specific segments in the market such as shared ownership and interest only allowed us to continue to lend conservatively during and after initial lockdowns.

Strong lending margins and new lending growth have been supported by significantly lower wholesale funding costs, as a result of the Bank of England's Term Funding Scheme with additional incentives for SMEs ("TFSME") which has replaced higher cost borrowing. Retail funding costs have also reduced with rates falling across the market on savings products as demand exceeds supply as a result of low consumer spending.

[1] CACI's CSDB, Stock, June 2020 to May 2021, latest data available.

Management expenses

	Six months to June 2021 £m	Six months to June 2020 £m	Year to December 2020 £m
Colleague costs	32.5	30.5	61.1
Other administrative expenses	20.4	15.0	31.8
Depreciation and amortisation	4.6	3.5	7.5
Total management expenses	**57.5**	**49.0**	**100.4**
	%	%	%
Cost to income ratio APM	44.9	52.5	51.0
Cost to mean asset ratio APM	0.56	0.47	0.48

We have continued to invest in our multi-year programme of technological change. We have strengthened key areas of the business to support this investment so that we are well positioned to deliver our future strategy. We will make use of our flexible new head office and agile technology to enhance member, broker and employee satisfaction, and position us to meet any future challenges that may arise.

This future facing investment has been one of the primary drivers for the increase in costs in the first half of 2021 compared to the same period in 2020, particularly where some of this expenditure was deferred into 2021 from 2020 due to the pandemic. This investment is significantly outweighed by higher income, meaning our cost to income ratio has improved from an already strong position. The prior period expenses also included a number of other areas of expenditure that were artificially suppressed during 2020 due to restrictions caused by the pandemic and many of our colleagues predominantly working from home.

Our colleagues are fundamental to our ability to deliver the service that our members need and we have bolstered our team to support our service and growth ambitions. The average number of colleagues (full time equivalent) employed by the Society in 2021 to date has increased to 1,345 (year to December 2020: 1,313).

Impairments and provisions

The table below summarises the impact of impairments and provision charges or (releases) on the Income Statement in the six months to 30 June 2021:

	Six months to 30 June 2021 £m	Six months to 30 June 2020 £m	Year to 31 December 2020 £m
Residential loans	(0.6)	11.7	14.7
Commercial loans	(0.1)	-	(0.1)
Impairments on loans and advances to customers	(0.7)	11.7	14.6
Other provisions	1.1	-	1.1
Total impairments and provisions	**0.4**	**11.7**	**15.7**

Residential impairment

We make provisions for expected credit losses across all loans, based on the probability of each loan defaulting and resulting in a loss, while taking into account a range of assumptions about future economic scenarios and an assessment of whether the credit risk of the loan has increased.

The provision for residential impairment increased significantly during the previous financial year due to the COVID-19 pandemic and the resulting heightened economic uncertainty. The central economic assumptions used for calculating impairment have been updated as at 30 June 2021 to reflect the improved economic performance to date and the latest view of the effects of the vaccine roll-out. However, there is continued uncertainty over the effect of the planned easing of restrictions and the end of furlough with this uncertainty reflected in the alternative modelled scenarios. The key judgements and estimates involved in the calculation of impairment loss provisions, including the use of post model adjustments, are set out in note 2 on pages 22 to 28.

Residential impairment loss provision coverage has reduced slightly during the six month period from 0.25% to 0.24% as the macroeconomic environment has stabilised, the mortgage book has grown and arrears performance has been better than expected. The number of borrowers in arrears has increased slightly since the start of the year, with the proportion in arrears by 1.5% of balance or more rising from 0.62% to 0.64%. The year-to-date impact on the Income Statement is minimal with a £0.6 million release (six months to June 2020: £11.7 million charge).

The total balance sheet impairment loss provisions against residential mortgages at 30 June 2021 were £41.2 million (31 December 2020: £42.8 million).

Other provisions

An industry wide increase in the Financial Services Compensation Scheme levy on deposit takers is expected for 2021/22 based on the latest information available so a provision has been made for the expected charge. In addition, a provision has been made for expected costs in relation to leased office properties which are due to be vacated following the move to the Society's new head office.

Financial position

Total assets increased in the first half of 2021, from £20.6 billion at 31 December 2020 to £21.1 billion. The movement is primarily due to positive net lending during the six month period. The Society has carefully managed its growth during the pandemic and continues to adjust its lending appetite based on the risk associated with the current economic environment.

Loans and advances to customers

	30 June 2021 £m	30 June 2020 £m	31 December 2020 £m
Residential loans	17,365	16,632	16,795
Commercial loans	16	17	16
Other loans	214	230	225
Impairment provision	(46)	(45)	(47)
Loans and advances to customers	**17,549**	**16,834**	**16,989**
	%	%	%
Proportion of mortgages in arrears[2]	0.64	0.57	0.62
Balance-weighted average indexed LTV of mortgage book	52	52	51
Balance-weighted average LTV of new lending	65	58	59

Our loans and advances to customers comprise mainly UK residential mortgages, which include residential owner occupied, buy to let and shared ownership. We have actively managed down our legacy commercial loan portfolio, and no new commercial loans have been issued. Other loans include a collateral loan that represents a pool of equity release mortgages purchased from a third party, where some of the risks relating to those mortgages were retained by the third party.

Gross new residential lending in the first half of 2021 was higher than in the same period in 2020 at £2.0 billion (six months to June 2020: £1.0 billion) and this positive activity is expected to continue into the second half of the year, with first half mortgage applications at record levels. The lending increase was driven by

[2] Arrears of more than 1.5% of the balance or in possession

positive demand across the market which was stimulated by Government initiatives such as the stamp duty holiday and a general desire to relocate following the lockdown. The comparative period in 2020 also includes the first COVID-19 lockdown period in which housing market activity slumped to an extremely low level.

We continue to focus on borrowers less well served by the wider market, such as shared ownership customers, as well as first time buyers and later life homeowners. We are proud that we have been able to continue to support current and new members throughout the pandemic while maintaining a prudent approach to overall lending.

The distribution of LTV ratios across the book reflects our conservative lending policy. The increased average LTV of new lending during 2021 to date of 65% (year to December 2020: 59%) relates to a change in the mix of products available, although credit criteria remain tighter than pre-pandemic.

We also continue to support existing borrowers in financial difficulty by waiving arrears fees and working with borrowers who are having difficulty returning to full payments following the expiry of their mortgage payment deferral period.

Liquid assets

	30 June 2021 £m	30 June 2020 £m	31 December 2020 £m
Liquid assets	3,063	2,997	2,975
	%	%	%
Liquidity Coverage Ratio	169	201	195
Liquid assets as a percentage of shares and borrowings	15.32	16.02	15.81

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 level of funding receipts compared to mortgage completions and other refinancing obligations. At 30 June 2021 liquidity included £2.6 billion of High Quality Liquid Assets (31 December 2020: £2.7 billion), which are either in cash or are readily realisable as cash when required. 100% of assets are rated A or above (31 December 2020: 100%).

The Prudential Regulation Authority (“PRA”) monitors liquidity under the Capital Requirements Regulation framework. Our Liquidity Coverage Ratio is 169% (31 December 2020: 195%), significantly in excess of the regulatory minimum of 100%.

Funding

	30 June 2021 £m	30 June 2020 £m	31 December 2020 £m
Shares (retail savings)	14,471	14,202	14,163
Wholesale funding	4,946	4,503	4,655
Total funding	**19,417**	**18,705**	**18,818**
	%	%	%
Wholesale funding ratio	25.4	22.4	24.6

Shares (retail savings)

The Society continues to be predominantly funded by retail savings which increased by £0.3 billion during the six month period to £14.5 billion at 30 June 2021 (31 December 2020: £14.2 billion).

As a mutual building society we remain committed to providing savers with competitive interest rates and despite the Bank of England's base rate remaining flat at 0.10%, the Society continues to pay above average market rates to its members. The Society's current minimum rate is 0.15%, above the base rate of 0.10%.

During the first half of the year, we launched a partnership which will provide access to our savings products through a third party online portal in order to increase the reach of our products.

Wholesale funding

The Society accesses the remainder of its funding requirements through complementary wholesale products. Total wholesale funding at 30 June 2021 was £4.9 billion (31 December 2020: £4.7 billion), representing 25.4% of total funding.

In March 2021, the Society issued £350 million of Senior Non-Preferred Fixed Rate Notes, repayable in March 2027. The transaction was hugely successful and had the lowest coupon to date of any similar issuance from a UK bank or building society. It helps provide term funding and future flexibility at an attractive cost for the Society in regards to its regulatory Minimum Requirement for Own Funds and Eligible Liabilities ("MREL") and rating agency requirements during an attractive issuance environment.

During the six month period the Society also drew down £800 million of TFSME funding and repaid £300 million of the original Term Funding Scheme ("TFS") drawings. At 30 June 2021, outstanding borrowing under these schemes was £0.4 billion under TFS and £1.6 billion under TFSME. We also repaid €500m of Senior Unsecured Notes which matured in early April.

In July, the Society's credit ratings with Moody's changed from negative to stable outlook reflecting our strong profitability and capital levels, together with improved economic conditions.

Capital

Capital resources	30 June 2021 £m	30 June 2020 £m	31 December 2020 £m
Total equity attributable to members	1,206	1,123	1,155
Adjustments	(40)	(36)	(39)
Common Equity Tier 1 (CET1) capital	1,166	1,087	1,116
Additional Tier 1 capital	3	5	5
Total Tier 1 capital	1,169	1,092	1,121
Tier 2 capital	229	224	227
Total regulatory capital resources	**1,398**	**1,316**	**1,348**
Tier 3 capital	350	**-**	**-**
Total MREL resources	**1,748**	**1,316**	**1,348**
Risk-weighted assets (RWAs)	**3,098**	**3,147**	**3,070**
CRD Capital Ratios	%	**%**	**%**
MREL ratio*	56.3	-	43.9
Total capital ratio	45.1	41.8	43.9
CET1 ratio	37.6	34.5	36.3
UK leverage ratio**	5.9	5.6	5.8

* Transitional MREL requirements, set by the Bank of England, are equal to 18% of risk weighted assets for the period July 2020 to 31 December 2022 plus any regulatory buffers. End state MREL requirements active from 1 Jan 2023 are two times minimum regulatory requirements plus any regulatory buffers.

** The UK regime is not currently legally binding as the Society operates below the applicable threshold set by the regulator (>£50bn).

The Society has maintained capital and leverage ratios well above regulatory requirements throughout 2021. Capital measures may fall as the full impacts of COVID-19 feed through into the economy. This is being monitored closely. However, for the Society this is from a strong position, well above any regulatory minimum due to our risk management framework and practices.

Environmental, Social and Governance

Environmental

The Society remains committed to tackling climate change, and during the first half of 2021 has made great progress in several key areas. This includes completing the refurbishment of our new head office which is net carbon neutral in operation and rated 'A' for energy efficiency. Occupancy of the new head office will progress over the second half of the year, in line with Government COVID-19 guidance.

Additionally, we have been re-accredited by the Carbon Trust, reflecting our ongoing commitment to understanding and managing our carbon footprint. As disclosed in our 2020 Annual Report and Accounts, the Society set a strategic aim to be carbon net neutral for Scope 1 and 2 emissions by the end of 2022. This work has progressed at pace, and we expect to achieve this 12 months ahead of target.

Colleagues are helping support our overall climate ambition through our 'Pledge Today, Change Tomorrow' environmental campaign, which promotes registering of individual pledges to reduce their carbon footprint. To date more than 300 individuals have signed up and pledged to save over 25,000kg of CO_2 emissions. During the first half of the year we have also announced exciting new partnerships with the Canal and Rivers Trust and the Yorkshire Dales Millennium Trust.

Social

The Society is also committed to providing support to the communities in which we operate. We are already more than half way towards our fundraising goals for our charity partner Dementia UK, raising £250,000 to date, after only 15 months of our four year partnership. Through this, we have funded the launch of Dementia UK's 'Closer to Home' programme, a unique mobile clinic which will provide support to families affected by dementia. In addition, we have organised a knowledge share workshop, which focused on fraud prevention for a number of the charity's Admiral nurses.

Through our social outreach programmes, we have reached over 7,000 students across 18 schools nationwide, providing a range of financial education materials and workshops to help improve students' understanding of financial matters and life skills. We have recently expanded this programme to cover career discussions for students, so they can connect curriculum subjects to jobs in the workplace while inspiring their future choices with regards to their careers.

The Leeds Building Society Foundation has continued to make contributions to a range of different charities through the first half of the year, providing over £82,000 in grants and donations to 89 small charities.

Governance

At the start of the year we published our "How we do business" approach, confirming the importance of our underlying values in everything we do. The Society established a Responsible Business Forum, which is chaired by our Chief Strategy and Insights Officer and is leading the delivery of the second phase of our responsible business strategy. In 2021 the Forum will define, publish and begin to monitor responsible business targets that are focused across various areas of the Society and include products, people, sustainable communities and climate. Our performance was assessed in Q2 2021 by two leading sustainability rating agencies, Sustainalytics and Vigeo Eiris and we will factor the outputs of these into our targets.

Risk Management Report

Overview

In order to ensure that the interests of members are adequately protected, the Society has embedded an Enterprise Risk Management Framework ("ERMF"), which is designed to identify, manage, monitor and control the risks associated with the delivery of the Society's strategic objectives. Further details of the framework can be found on pages 98 to 102 of the 2020 Annual Report and Accounts.

Principal risks

Principal risks arising from the Society's strategy are credit, funding and liquidity, capital, market, model, operational, conduct and strategic and business risks. These principal risk categories remain unchanged from those described on pages 39 to 46 of the 2020 Annual Report and Accounts.

During the first half of 2021, the risk profile of the Society has continued to be influenced by the effects of COVID-19 across all the principal risk categories. Key impacts and mitigating actions are set out below:

Principal risk	COVID-19 impact	Key mitigating actions
Strategic/ business risk	• During H1, the Government reimposed more stringent social restrictions to contain the spread of COVID-19, resulting in a contraction in the UK economy in Q1 2021. Since this time, and as restrictions have been eased, economic activity has started to recover steadily. • The nature of COVID-19 continues to create challenges in assessing the outlook for the external environment, with material uncertainty remaining around the longer term impacts on the economy, market competition, housing market and customer trends.	• The Society's strategic planning process establishes the business direction and investment activity in the context of the changing regulatory, competitive and technological landscape. • The Board approved corporate planning process ensures that the business environment is assessed regularly and plans adjusted accordingly. • Stress testing is regularly utilised to understand how the Society would respond and perform under a variety of severe but plausible scenarios.
Credit risk	• To date the economic impacts of COVID-19 are yet to fully flow through to the Society's mortgage portfolios, primarily due to Government intervention. However, as these schemes close, it is anticipated that increased levels of unemployment will heighten the Society's credit risk profile.	• Adapt lending policies and criteria to ensure that they remain reflective of the prevailing operating environment. • Close monitoring of lending portfolio performance. • Further investment within Customer Services to support members facing financial difficulties. • Review of the Society's IFRS 9 scenarios and weightings to ensure that they reflect the current economic climate. • Stress testing and sensitivity analysis to understand potential financial impacts and inform management responses under a variety of economic trajectories.
Funding and liquidity risk	• Ongoing uncertainty within the operating environment and changing customer behaviours continue to influence the anticipated timing of business flows. • Central bank schemes to support lending to households during the pandemic (e.g. TFSME) and the current interest rate environment continue to impact retail and wholesale funding markets.	• A strong, high quality liquidity portfolio continues to be maintained, at a level comfortably above minimum regulatory requirements. • Access to central bank funding through pre-positioned collateral. • Daily monitoring of the Society's liquidity position. • Frequent liquidity stress testing to understand the impact of severe, but plausible scenarios and to inform appropriate mitigating actions.

Risk Management Report

		• Maintenance of a Recovery Plan and Trigger Framework, including actions to restore liquidity in a stress event.
Market risk	• The Bank of England has continued to maintain a very low interest rate environment to support the economy during H1 2021. • Whilst the immediate likelihood of negative interest rates has abated, a material deterioration in the UK's economic recovery may require further central bank intervention.	• Frequent stress testing is performed to understand the potential financial impacts of movements in interest rates on the Society's balance sheet and income statement (including negative rates) and to develop appropriate management responses. • Ongoing analysis and reporting of hedge accounting considerations. • Action has been taken to ensure the Society is operationally prepared for the potential implementation of negative interest rates.
Capital risk	• COVID-19 Government support schemes have suppressed the full macroeconomic effects of the pandemic so far. Despite the ongoing uncertainty in the external environment, the Society's capital ratios are forecast to remain in excess of minimum requirements.	• As at 30 June 2021, the Society remained strongly capitalised, with significant headroom over regulatory requirements. • Stress testing is regularly performed to understand the impact on the Society's capital position under a range of severe scenarios and to inform management actions. • Maintenance of a Recovery Plan and Trigger Framework, including actions to restore and preserve capital in a stress event.
Model risk	• The Government's response to COVID-19 has resulted in a divergence between the traditional relationship of several economic variables used to calibrate financial models. • Relevant models have been subject to heightened levels of monitoring and analysis to inform adjustments and management overlays and ensure that modelled outputs remain within appropriate ranges.	• The Society continues to refine its approach to model risk management, so that models are appropriately governed and remain fit for purpose. • Additional model reviews and oversight, which consider the performance of the model suite in the context of the potential economic impacts emanating from the pandemic. • In this context, significant Board focus has centred on the appropriateness of any post model adjustments.
Operational risk	• The Society's foremost priority throughout the COVID-19 pandemic has been the health and safety of colleagues and members. • More generally COVID-19 continues to influence the Society's operational risk profile on a number of fronts, including: o Increased pressure on customer support areas; o Increased levels of remote working arrangements and associated data security risks; o An increased risk of cyber attacks as actors have sought to take advantage of prevailing conditions; o Impacts on third parties leading to temporary business disruption; and o New regulation requiring further changes to processes and systems. • The crystallisation of any of the above could result in errors, delays or losses.	• The Society continues to implement Government advice in relation to COVID-19 to ensure customer and colleague safety. As restrictions unwind the Society will develop appropriate responses accordingly. • The internal control environment is validated by risk and control self-assessments, control testing and oversight. • The Society closely monitors upstream regulation, with developments managed through an oversight framework, which allows management to respond in an efficient and proportionate manner. • Detailed resource planning has been conducted across key departments to minimise key person dependencies and prepare for changes in customer demand.

		• Heightened focus remains on mitigating potential cyber and information risks under revised working arrangements, including penetration testing and programmes of activity to improve colleague awareness. • Society suppliers identified as 'Critical' remain subject to increased oversight.
Conduct risk	• The threat remains that COVID-19 could increase the Society's conduct risk profile through a failure to recognise and appropriately manage customer circumstances, financial difficulties or vulnerabilities.	• The Society continues to monitor and apply Government and regulatory guidance. • Capacity has been increased within the operational areas supporting customers in financial difficulties to plan for an increase in expected demand as Government support schemes cease. • Risk assurance plans contain a significant focus on areas affected by COVID-19, including the impacts on customers in financial difficulties and vulnerable customers.

Emerging risks

Within the context of our principal risk categories, we continue to identify, assess and monitor emerging risks through our ERMF. These are new or evolving risks where the impact is uncertain. In assessing emerging risks, we consider the likelihood of the relevant risk materialising and the potential impact on our business strategy and stakeholders.

Our top emerging risks remain broadly consistent with those identified within the 2020 Annual Report and Accounts.

Emerging risk	Description	Strategic response
Political and macroeconomic risk	• The full economic impacts of COVID-19 are yet to fully materialise, due to Government intervention. Whilst market forecasters expect economic recovery to become entrenched during H2 2021, there remains a high level of uncertainty regarding its future trajectory. • Whilst the success of the UK vaccination program has facilitated the easing of social restrictions, the threat of further variants could require the reintroduction of such measures, which could constrain the economic recovery. • The wider impacts of the UK's new trading relationship with the European Union are starting to emerge. At present there remains a high level of uncertainty as to the longer term sectoral impacts on the wider economy. • Following the outcome of the recent Scottish election there is an increasing probability of a second Scottish referendum on independence in the medium term.	• Frequent assessment of macroeconomic and political risks under both central and stressed conditions, to understand and subsequently manage the impact on the Society's strategy and business model. • Active monitoring of credit quality within lending portfolios and thorough analysis to identify sectors that may be negatively impacted by a slowdown in the UK economy.

Cyber / financial crime	• The heightened threat of ransomware, both on the Society directly and within the supply chain, is a key risk within the Society's cyber strategy. • The wider threat of data breaches on suppliers with access to Society data continues to grow due to increased cyber-criminal activity and sophistication.	• Alignment of the Society's cyber strategy and responses to key threats in the evolving landscape. • Independent assessment of cyber controls on a periodic basis. • Industry engagement to understand the evolving threat landscape. • Colleague education and training.
Regulatory risk	• The Society's operating environment continues to be shaped by the volume, scale and complexity of regulatory change, with clarity emerging in H1 2021 on how the UK's regulatory framework will be shaped post-Brexit. • A number of regulatory instruments on the horizon will require careful consideration and implementation, such as the FCA's Consumer Duty which will further enhance rules and guidance surrounding customer outcomes. • Amendments to the rules and regulations governing the suite of measures introduced to help support the economy through COVID-19, such as the timing of scheme run-off, will necessitate careful management of potential reputational and conduct risks.	• The Society closely monitors upstream regulation, with developments managed through an oversight framework, which allows management to respond in an efficient and proportionate manner.
Climate change	• Climate change could have a significant impact on the Society's operations, members, colleagues and suppliers. This includes physical risks to the Society's housing stock and own properties, and transitional risks as the UK migrates to a net zero economy. • Reputational risks surrounding climate change could also become heightened if the Society's response does not align to increasing stakeholder and regulatory expectations.	• During H1 2021, the Society has continued to integrate climate change risks within the ERMF. This has included the further development of our Climate Change Framework, procurement of third-party data to assess the physical and transitional risks associated with our lending portfolios and defining an approach to climate change stress testing. • These climate deliverables will enable the Society to enhance its climate disclosures in the 2021 Annual Report and Accounts, in line with the recommendations from the Task Force on Climate-related Financial Disclosures.
Competition	• Following an easing of competitive pressures within the UK mortgage market during 2020 as a result of the pandemic, competition has re-emerged during H1 2021. As a result margins continue to tighten, and lenders have re-entered higher risk segments. • From a savings perspective, the availability of TFSME and the low interest rate environment has dampened retail pricing. However, as this scheme is withdrawn during H2 2021, upward pressure on pricing is anticipated. • Temporary changes in customer behaviour due to COVID-19 may become more established and result in an acceleration of the digitalisation of financial services.	• The Society closely monitors the market positioning of its products and has responded accordingly. • The Society carefully considers these risks as part of its strategic / business planning activities, which has set the future path for strategic investment and development to ensure that it is able to adapt accordingly.

Condensed Consolidated Income Statement

	Notes	**Six months to 30 June 2021 (Unaudited) £m**	Six months to 30 June 2020 (Unaudited) £m	Year to 31 December 2020 (Audited) £m
Interest receivable and similar income	3	**201.6**	219.1	402.6
Interest payable and similar charges	4	**(73.9)**	(119.4)	(197.2)
Net interest receivable		**127.7**	99.7	205.4
Fees and commissions receivable		**3.1**	2.8	5.6
Fees and commissions payable		**(0.2)**	(0.2)	(0.6)
Fair value losses from financial instruments	5	**(1.2)**	(9.3)	(16.8)
Other operating (expense) / income		**(1.2)**	0.3	3.2
Total income		**128.2**	93.3	196.8
Administrative expenses	6	**(52.9)**	(45.5)	(92.9)
Depreciation and amortisation		**(4.6)**	(3.5)	(7.5)
Impairment gains / (losses) on loans and advances to customers	7	**0.7**	(11.7)	(14.6)
Provisions charge		**(1.1)**	-	(1.1)
Operating profit and profit before tax		**70.3**	32.6	80.7
Tax expense	8	**(18.0)**	(5.8)	(18.7)
Profit for the period		**52.3**	26.8	62.0

Condensed Consolidated Statement of Comprehensive Income

	Six months to 30 June 2021 (Unaudited)	Six months to 30 June 2020 (Unaudited)	Year to 31 December 2020 (Audited)
	£m	£m	£m
Profit for the period	**52.3**	26.8	62.0
Items that may subsequently be reclassified to profit and loss:			
Fair value (losses) / gains on investment securities measured at fair value through other comprehensive income	**(1.8)**	11.7	11.1
(Gains) / losses on investment securities measured through other comprehensive income reclassified to profit or loss on disposal	**(0.1)**	0.1	(2.5)
Tax relating to items that may subsequently be reclassified	**0.6**	(3.2)	(1.6)
Effect of change in corporation tax rate	**(0.4)**	-	(0.7)
Items that may not subsequently be reclassified to profit and loss:			
Actuarial gain / (loss) on retirement benefit surplus	**1.1**	1.4	(1.9)
Revaluation gain on properties revalued	**-**	-	2.7
Tax relating to items that may not be reclassified	**(0.2)**	(0.4)	(0.5)
Effect of change in corporation tax rate	**(0.1)**	0.3	-
Total comprehensive income for the period	**51.4**	36.7	68.6

Condensed Consolidated Statement of Financial Position

	Notes	**30 June 2021 (Unaudited) £m**	30 June 2020 (Unaudited) £m	31 December 2020 (Audited) £m
Assets				
Liquid assets				
Cash in hand and balances with the Bank of England		**1,816.0**	1,382.3	1,823.2
Loans and advances to credit institutions		**368.0**	170.3	201.9
Investment securities		**879.0**	1,444.8	949.7
Derivative financial instruments		**133.0**	235.3	192.8
Loans and advances to customers	9			
Loans fully secured on residential property		**17,323.4**	16,591.7	16,752.5
Other loans		**225.6**	242.6	236.4
Fair value adjustment for hedged risk on loans and advances to customers		**(23.1)**	113.8	96.1
Other assets, prepayments and accrued income		**245.9**	247.3	270.4
Deferred tax assets		**6.8**	6.6	5.6
Intangible assets		**27.2**	23.6	28.8
Property, plant and equipment		**84.0**	69.4	81.3
Retirement benefit surplus	10	**2.1**	4.5	1.0
Total assets		**21,087.9**	20,532.2	20,639.7
Liabilities				
Shares		**14,470.8**	14,201.7	14,162.7
Fair value adjustment for hedged risk on shares		**(51.7)**	(18.9)	(13.5)
Derivative financial instruments		**162.2**	278.4	237.9
Amounts owed to credit institutions		**1,998.6**	1,211.3	1,497.3
Amounts owed to other customers		**293.6**	113.7	256.7
Debt securities in issue		**2,305.7**	3,177.6	2,900.7
Other liabilities and accruals		**110.8**	194.9	192.9
Current tax liabilities		**3.1**	1.5	2.3
Deferred tax liabilities		**4.9**	6.1	4.7
Provisions for liabilities and charges		**2.8**	1.1	1.8
Subordinated liabilities	11	**347.6**	-	-
Subscribed capital		**233.4**	242.0	241.5
Total liabilities		**19,881.8**	19,409.4	19,485.0
Total equity attributable to members		**1,206.1**	1,122.8	1,154.7
Total liabilities and equity		**21,087.9**	20,532.2	20,639.7

Condensed Consolidated Statement of Changes in Members' Interest

Six months to 30 June 2021	General reserve £m	Fair value reserve £m	Revaluation reserve £m	Other reserve £m	Total equity attributable to members £m
At 1 January 2021 (Audited)	1,125.1	5.4	9.9	14.3	1,154.7
Comprehensive income / (expense) for the period	53.9	(1.7)	(0.8)	-	51.4
Revaluation gains transferred on disposal of assets	0.2	-	(0.2)	-	-
At 30 June 2021 (Unaudited)	**1,179.2**	**3.7**	**8.9**	**14.3**	**1,206.1**

Six months to 30 June 2020	General reserve £m	Fair value reserve £m	Revaluation reserve £m	Other reserve £m	Total equity attributable to members £m
At 1 January 2020 (Audited)	1,064.6	(0.9)	8.1	14.3	1,086.1
Comprehensive income / (expense) for the period	28.3	8.6	(0.2)	-	36.7
At 30 June 2020 (Unaudited)	1,092.9	7.7	7.9	14.3	1,122.8

Year to 31 December 2020	General reserve £m	Fair value reserve £m	Revaluation reserve £m	Other reserve £m	Total equity attributable to members £m
At 1 January 2020 (Audited)	1,064.6	(0.9)	8.1	14.3	1,086.1
Comprehensive income for the year	60.5	6.3	1.8	-	68.6
At 31 December 2020 (Audited)	1,125.1	5.4	9.9	14.3	1,154.7

Condensed Consolidated Statement of Cash Flows

	Six months to 30 June 2021 (Unaudited) £m	Six months to 30 June 2020 (Unaudited) £m	Year to 31 December 2020 (Audited) £m
Profit before tax	**70.3**	32.6	80.7
Adjusted for changes in:			
Impairment provision	**(1.7)**	11.9	14.0
Provisions for liabilities and charges	**1.0**	(0.1)	0.6
Depreciation and amortisation	**4.6**	3.5	7.5
Fair value of collateral loan which represents a pool of equity release mortgages	**7.4**	(9.4)	(6.2)
Non cash and other items	**(9.5)**	1.8	3.5
Cash generated from operations	**72.1**	40.3	100.1
Changes in operating assets and liabilities			
Derivative financial instruments	**(3.8)**	22.4	20.1
Loans and advances to customers	**(569.0)**	138.0	(21.9)
Other operating assets	**26.6**	(40.9)	(61.2)
Shares	**308.1**	(315.8)	(354.8)
Amounts owed to credit institutions and other customers	**538.2**	(349.2)	79.8
Other operating liabilities	**(78.7)**	58.1	55.8
Taxation paid	**(18.5)**	(15.1)	(27.0)
Net cash flows from operating activities	**275.0**	(462.2)	(209.1)
Cash flows from investing activities			
Purchase of investment securities	**(93.9)**	(683.0)	(796.3)
Proceeds from sale and redemption of investment securities	**162.0**	957.9	1,562.4
Purchase of intangible assets	**(0.8)**	(5.1)	(11.7)
Purchase of property, plant and equipment	**(5.3)**	(7.2)	(19.1)
Proceeds from sale of property, plant and equipment	**0.2**	-	-
Net cash flows from investing activities	**62.2**	262.6	735.3
Cash flows from financing activities			
Net proceeds from issue of debt securities	**161.0**	863.5	2,427.2
Repayments of debt securities in issue	**(685.2)**	(725.6)	(2,541.4)
Net proceeds from issue of subordinated liabilities	**346.9**	-	-
Principal lease payments	**(1.0)**	(0.8)	(2.0)
Net cash flows from financing activities	**(178.3)**	137.1	(116.2)
Net increase / (decrease) in cash and cash equivalents	**158.9**	(62.5)	410.0
Cash and cash equivalents at the beginning of the period	**2,025.1**	1,615.1	1,615.1
Cash and cash equivalents at the end of the period	**2,184.0**	1,552.6	2,025.1

Notes to the Accounts

1. General information

Reporting period

The Interim Financial Report is for the six months to 30 June 2021 and is unaudited.

Basis of preparation and accounting policies

These condensed consolidated set of financial statements for the six month period ended 30 June 2021 have been prepared in accordance with International Accounting Standard 34 – Interim Financial Reporting, as adopted by the United Kingdom. They do not include all the information required by International Financial Reporting Standards ("IFRS") in full annual financial statements and should therefore be read in conjunction with the Annual Report and Accounts for the year ended 31 December 2020 which were prepared in accordance with IFRS as adopted for use in the European Union and in accordance with those parts of the Building Societies Act 1986 and the Building Societies (Accounts and Related Provisions) Regulations 1998 (as amended) applicable to societies reporting under IFRS.

The information in these interim condensed consolidated financial statements is unaudited and does not constitute annual accounts within the meaning of Section 72 of the Building Societies Act 1986 ("the Act"). Group accounts for the year ended 31 December 2020 have been filed with the Financial Conduct Authority and Prudential Regulation Authority and contained an unqualified audit report, which did not draw attention to any matters by way of emphasis and did not contain any statements under Section 78 of the Act.

The accounting policies adopted, presentation and methods of computation are consistent with those applied by the Group in its latest audited annual financial statements. At 30 June 2021 we reported a new balance sheet item "subordinated liabilities", see note 11 for details of the accounting policy adopted for these financial liabilities. These financial statements are presented in sterling and, except where otherwise indicated, have been rounded to the nearest one hundred thousand pounds.

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.

Accounting developments

The information on future accounting developments and their potential effect on the financial statements is provided on page 141 of the 2020 Annual Report and Accounts.

Segmental reporting

As reported in note 1n of the 2020 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 undertake regular rigorous assessments of whether the Group is a going concern, considering current economic and market conditions, including the ongoing impacts of the pandemic as well as the potential impact of the principal and emerging risks set out on pages 39 to 48 of the 2020 Annual Report and Accounts. An update on principal risks is provided on pages 12 to 15 of this report.

The Group has continued to operate throughout the pandemic, with the infrastructure in place to enable the majority of office based colleagues to work remotely, while adjustments have been made for colleagues working on Group premises so that they can continue to do so safely to serve our members.

The directors have concluded that:

- The Group has proven access to liquidity resources, including access to central bank funding facilities if required, sufficient to meet both the normal demands of the business and the requirements which might arise in modelled stressed circumstances. The availability and quality of liquid assets are structured so that funds are available to repay any maturing wholesale funds and cover exceptional demand from retail investors;

Notes to the Accounts (continued)

1. General information (continued)

- The Group's other assets consist primarily of mortgages secured on residential property. The recoverability of all mortgage assets is reviewed regularly and provisions are made, incorporating a forward looking view of expected losses under a range of macroeconomic scenarios, so that the Group is not exposed to losses on these assets which would impact its decision to adopt the going concern basis; and
- The Group's current capital resources are sufficient to meet regulatory requirements. Having reviewed future plans and forecasts, the directors consider plans for future capital generation are sufficient to maintain capital in excess of regulatory requirements, under both central and modelled stressed scenarios.

The directors have concluded that there is no material uncertainty in relation to the Group's continuation as a going concern and therefore it is appropriate to adopt the going concern basis in the preparation of the Interim Financial Report.

2. Critical accounting estimates and judgements

The preparation of the Interim Financial Report involves making judgements, estimates and assumptions in the application of the Group's accounting policies which affect the amounts reported in the financial statements. The critical judgements and estimates which have a significant impact on the financial statements are described in note 2 of the 2020 Annual Report and Accounts.

The critical judgements and estimates which have a significant impact on the Interim Financial Report are described below.

a. Critical judgements

Impairment of loans and advances to customers

The Group's accounting policy for the impairment of loans and advances to customers is explained in note 1e of the 2020 Annual Report and Accounts.

Post model adjustments ("PMAs") are applied to modify the level of impairment loss provisions from that calculated by the detailed models used to determine expected credit losses ("ECL") where there is a risk that is not adequately captured within modelled ECL as a result of a lack of historical data with which to model or ongoing uncertainty. Judgement is required in determining whether a PMA should be used and the appropriate quantum of the adjustment. All PMAs are subject to approval by Credit Committee and must be reviewed and reapproved at least annually.

The total of these PMAs at 30 June 2021 was £5.6m (30 June 2020: £5.8m; 31 December 2020: £9.5m). Further details of the estimates used to evaluate these PMAs are presented in note 2b below.

b. Significant accounting estimates and assumptions

Impairment of loans and advances to customers

The significant estimates required for the calculation of impairment loss provisions are forecast UK macroeconomic variables, the probability weightings of the macroeconomic scenarios used and the calculation of post model adjustments.

Macroeconomic scenarios and probability weightings

Consistent with the 2020 Annual Report and Accounts, the Group has used four macroeconomic scenarios, which are considered to represent a range of possible outcomes, in determining impairment loss provisions. The scenarios have been revised during the period to reflect the improved economic performance in the year while recognising there are still significant downside risks around the effect of the easing of restrictions and the unwind of Government support schemes.

Notes to the Accounts (continued)

2. Critical accounting estimates and judgements (continued)

b. Significant accounting estimates and assumptions (continued)

A summary of each of the four revised macroeconomic scenarios is as follows:

- Central scenario reflecting the positive effects of the vaccine rollout, balanced against the continued uncertainty around the effects of the cessation of Government support schemes. This scenario shows GDP returning to pre-pandemic levels before the end of 2022, with unemployment peaking at 7% during Q1 2022 following the end of the furlough scheme and house price growth slowing during 2022 after increases during the current financial year.
- Downside scenario as modelled in the Group's risk management process reflecting a '1 in 20' stress scenario, with higher unemployment than the central scenario and reductions in house prices as demand falls.
- Alternative downside scenario representing a more severe downturn than in the downside scenario with peak unemployment of 10.7% and a fall in demand across the housing market, causing greater reductions in house prices in the earlier years of the forecast. This scenario has been revised from that used at 31 December 2020 to reflect additional downside risk previously captured through PMAs.
- Growth scenario representing a more optimistic view of recovery from the pandemic than assumed in the central scenario, including potential upsides from the performance of the housing market.

Scenarios are developed based on the Group's analysis of third party published economic data and forecasts. Due to the unprecedented impact of the COVID-19 pandemic, historic analysis does not necessarily provide a reliable indicator of future outcomes, so the relative weighting of the macroeconomic scenarios is primarily determined by management judgement reflecting their view of the current economic and political climate, taking into account external commentary and supported by sensitivity analysis.

The scenario weightings used in the modelling of expected credit losses remain unchanged from 31 December 2020 and are detailed below:

	30 June 2021	30 June 2020	31 December 2020
Central	45%	45%	45%
Downside	30%	30%	30%
Alternative Downside	10%	10%	10%
Growth	15%	15%	15%

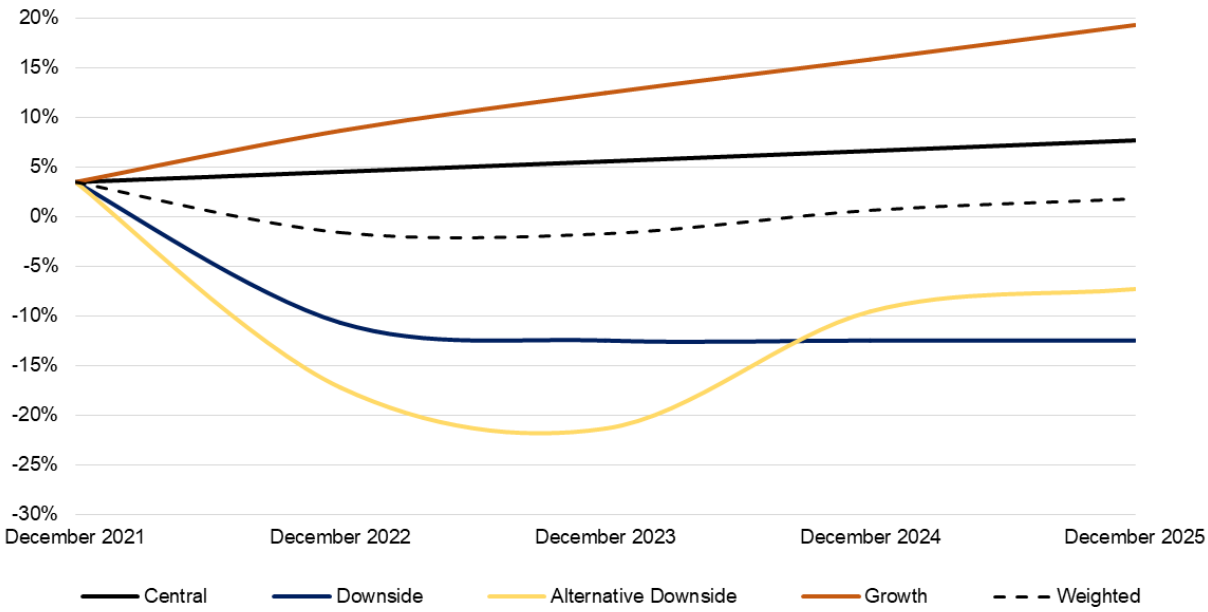
2. Critical accounting estimates and judgements (continued)

b. Significant accounting estimates and assumptions (continued)

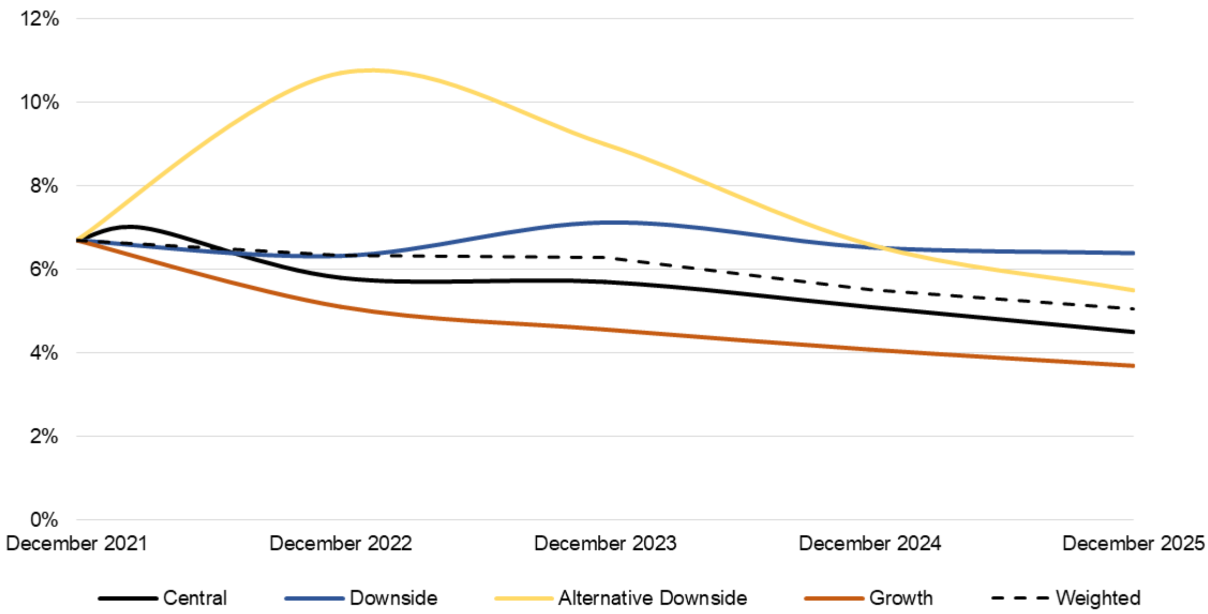
The table overleaf shows the macroeconomic assumptions used in each scenario. The variables with the most significant impact on the calculated impairment loss provisions are house price inflation and unemployment rate.

The first chart below illustrates the cumulative impact of the annual house price inflation assumptions as prices continue to rise during 2021 and then reduce during both 2022 and 2023 in the downside scenarios. The unemployment rate is forecast to peak during Q1 2022 in the central scenario before reducing to lower levels as illustrated in the second chart below.

House prices (December 2020 = 0):



Unemployment Rate (%)



Notes to the Accounts (continued)

2. Critical accounting estimates and judgements (continued)

b. Significant accounting estimates and assumptions (continued)

Macroeconomic assumptions applied by the Group in each scenario

The tables show the full year rates for house price inflation and Gross Domestic Product growth, together with the year end position for unemployment rate and Bank Base Rate. Beyond the five year period shown below, assumptions move towards historic long run averages over the following five years and then remain constant at these rates thereafter.

		30 June 2021				
		2021	**2022**	**2023**	**2024**	**2025**
House price inflation	Central	3.5%	1.0%	1.0%	1.0%	1.0%
	Downside	3.5%	(13.7%)	(2.0%)	0.0%	0.0%
	Alternative Downside	3.5%	(20.0%)	(5.0%)	15.0%	2.5%
	Growth	3.5%	5.0%	3.5%	3.0%	3.0%
	Weighted *	3.5%	(4.9%)	(0.1%)	2.4%	1.2%
Unemployment rate	Central	6.7%	5.8%	5.7%	5.1%	4.5%
(31 December)	Downside	6.7%	6.3%	7.1%	6.5%	6.4%
	Alternative Downside	6.7%	10.7%	9.0%	6.6%	5.5%
	Growth	6.7%	5.1%	4.6%	4.1%	3.7%
	Weighted *	6.7%	6.3%	6.3%	5.5%	5.1%
Gross Domestic Product growth	Central	5.0%	6.0%	2.1%	1.8%	1.7%
	Downside	5.0%	3.0%	1.7%	1.3%	1.3%
	Alternative Downside	5.0%	2.7%	5.1%	2.8%	1.2%
	Growth	5.0%	7.5%	2.2%	2.4%	2.5%
	Weighted *	5.0%	5.0%	2.3%	1.8%	1.7%
Bank Base Rate (31 December)	Central	0.10%	0.10%	0.10%	0.50%	0.50%
	Downside	0.10%	0.10%	0.10%	0.10%	0.10%
	Alternative Downside	0.10%	(0.10%)	(0.10%)	0.10%	0.10%
	Growth	0.10%	0.10%	0.10%	0.50%	0.75%
	Weighted *	0.10%	0.08%	0.08%	0.34%	0.38%

* Note that ECLs are calculated for each loan in each scenario and then probability weighted, so the weighted figure here is for illustrative purposes only.

Notes to the Accounts (continued)

2. Critical accounting estimates and judgements (continued)

b. Significant accounting estimates and assumptions (continued)

		30 June 2020				
		2020	2021	2022	2023	2024
House price inflation	Central	(2.5)%	(4.0)%	0.0%	3.5%	4.0%
	Downside	(10.6)%	(3.1)%	(2.0)%	0.0%	0.0%
	Alternative Downside	(10.8)%	(7.0)%	(4.0)%	0.0%	2.0%
	Growth	(1.0)%	(0.5)%	1.5%	5.0%	5.5%
	Weighted *	(5.5)%	(3.5)%	(0.8)%	2.3%	2.8%
Unemployment rate (31 December)	Central	7.0%	6.0%	5.0%	5.0%	4.5%
	Downside	6.5%	7.0%	7.0%	6.5%	6.5%
	Alternative Downside	7.0%	7.5%	7.5%	7.0%	6.7%
	Growth	5.3%	4.5%	3.9%	3.8%	3.8%
	Weighted *	6.6%	6.2%	5.7%	5.5%	5.2%
Gross Domestic Product growth	Central	(7.0)%	3.7%	1.7%	1.8%	2.0%
	Downside	(7.0)%	(1.0)%	2.0%	1.5%	1.5%
	Alternative Downside	(8.0)%	(1.5)%	0.5%	1.5%	2.0%
	Growth	(5.0)%	8.5%	2.7%	2.8%	3.0%
	Weighted *	(6.8)%	2.5%	1.8%	1.8%	2.0%
Bank Base Rate (31 December)	Central	0.1%	0.1%	0.3%	0.3%	0.3%
	Downside	0.1%	0.3%	0.3%	0.5%	0.5%
	Alternative Downside	1.5%	2.0%	2.0%	2.0%	2.0%
	Growth	0.1%	0.5%	1.5%	1.8%	2.0%
	Weighted *	0.2%	0.4%	0.6%	0.7%	0.8%

		31 December 2020				
		2021	2022	2023	2024	2025
House price inflation	Central	(5.0)%	(1.0)%	0.0%	2.0%	2.0%
	Downside	(13.7)%	(2.0)%	0.0%	0.0%	1.0%
	Alternative Downside	(10.0)%	(14.5)%	5.0%	3.5%	3.5%
	Growth	2.0%	3.0%	4.0%	3.5%	3.5%
	Weighted *	(7.1)%	(2.1)%	1.1%	1.8%	2.1%
Unemployment rate (31 December)	Central	7.0%	5.0%	4.8%	4.5%	4.3%
	Downside	7.0%	7.0%	6.5%	6.5%	6.1%
	Alternative Downside	10.0%	9.0%	8.5%	7.5%	7.0%
	Growth	4.5%	3.9%	3.5%	3.5%	3.5%
	Weighted *	6.9%	5.8%	5.5%	5.3%	5.0%
Gross Domestic Product growth	Central	7.0%	4.0%	2.0%	2.0%	2.0%
	Downside	2.0%	2.0%	1.5%	1.5%	1.6%
	Alternative Downside	0.0%	5.0%	3.5%	3.0%	2.0%
	Growth	14.0%	3.0%	3.0%	3.0%	2.0%
	Weighted *	5.9%	3.4%	2.2%	2.1%	1.9%
Bank Base Rate (31 December)	Central	0.1%	0.1%	0.1%	0.1%	0.1%
	Downside	0.1%	0.1%	0.1%	0.1%	0.1%
	Alternative Downside	(0.1)%	(0.1)%	0.1%	0.1%	0.1%
	Growth	0.1%	0.1%	0.3%	0.3%	0.3%
	Weighted *	0.1%	0.1%	0.1%	0.1%	0.1%

Notes to the Accounts (continued)

2. Critical accounting estimates and judgements (continued)

b. Significant accounting estimates and assumptions (continued)

The sensitivity of calculated impairment loss provisions at 30 June 2021 to changes in key individual macroeconomic variables, with all other assumptions held constant, is illustrated below. Note that due to the interaction between different economic variables within the impairment loss provision models, the impacts of such single variable sensitivities may be distorted and not representative of realistic alternative scenarios.

The impact of changing the assumption for annual house price inflation in each of the first two years of the central scenario is as follows:

	+ 2.5 percentage points	- 2.5 percentage points
(Decrease) / increase in impairment loss provisions (£m)	(0.6)	0.7

The impact of changing the assumption for unemployment in each of the first two years of the central scenario is as follows:

	+ 1.0 percentage point	- 1.0 percentage point
Increase / (decrease) in impairment loss provisions (£m)	0.4	(0.3)

In practice the above variables are unlikely to move in isolation. The combined impact of movements in a number of variables can be illustrated by the sensitivity of calculated provisions to scenario weightings. The table below shows the movement in impairment loss provisions if each of the scenarios were weighted 100%:

	Six months to 30 June 2021 (Unaudited) £m	Six months to 30 June 2020 (Unaudited) £m	Year to 31 December 2020 (Audited) £m
(Decrease) / increase in impairment loss provisions			
Central	**(16.4)**	(7.3)	(8.8)
Downside	**4.5**	2.4	10.0
Alternative Downside	**108.9**	53.1	66.5
Growth	**(18.9)**	(13.6)	(14.7)

The increased magnitude of these sensitivities in comparison to the prior year reflects the combined impact of an improved central economic position and the greater severity of the alternative downside scenario. This has increased weighted modelled ECL, meaning there has been a reduction in the overall level of PMAs required (see page 22).

Notes to the Accounts (continued)

2. Critical accounting estimates and judgements (continued)

b. Significant accounting estimates and assumptions (continued)

Economic uncertainty post model adjustment

The macroeconomic scenarios and probability weightings are considered to provide an appropriate range of forecast outcomes at the date of the Interim Financial Report. However, as there remains a significant level of economic uncertainty due to the COVID-19 pandemic it was determined that a PMA is still required.

Extensive scenario analysis was performed considering the potential impacts of certain possible events over and above those included in modelled scenarios and these were used to inform the overall level of the PMA. This included consideration of factors such as the inherent bias of reported house prices towards properties recently sold, which may not be reflective of the composition of the underlying book, particularly given the significant growth in house prices experienced over the last twelve months for certain property types and locations. This scenario analysis indicated a range of plausible values for the PMA, with the final PMA agreed at £2.0m.

Model performance post model adjustment

At 31 December 2020 it was considered that Government interventions, such as furlough, would continue to support borrowers in meeting their mortgage payments, but mask underlying increases in credit risk such that loans will have suffered a significant increase in credit risk or default event but it would not be evident in the data used in provision calculations. This view is still supported at the half year; however, reflecting credit performance of these loans in the first half of 2021, the approach for calculating the overlay is now focused on mortgage payment deferral extensions only and is based on performance by number of months since the payment deferral ended.

The second element of the PMA relates to the time from default to possession assumption, which was increased by up to 24 months at 31 December 2020 reflecting the moratorium on repossessions during the pandemic. This assumption has been retained at 30 June 2021 ahead of the recommencement of possession activity.

Thirdly, this PMA includes an adjustment to address impacts of the alternative downturn scenario for which modelled ECLs do not appropriately reflect the risk associated with the book due to the unusual nature of the scenario and lack of historic data points.

An overall model performance PMA of £0.9m is considered to be appropriate for the half year and the PMA will be reassessed ahead of the year end.

Inadequate cladding post model adjustment

Industry data on the prevalence of this issue remains very limited. The PMA was recognised at 31 December 2020 and was estimated by identifying properties at the highest risk of cladding issues using postcode data and applying a range of haircuts to property valuations and making an allowance for remediation costs. The PMA has been revised based on updated market information and guidance from the Royal Institution of Chartered Surveyors with a PMA of £2.7m considered to be appropriate as at 30 June 2021.

Fair value of the collateral loan

The Group holds a collateral loan which represents a pool of equity release mortgages purchased from a third party for which some but not all of the risks were transferred to the Group. The underlying mortgages contain a 'no negative equity guarantee' such that any shortfall that may arise on the sale of the property securing the mortgage will not be pursued. The Group therefore measures this collateral loan at fair value through profit or loss.

The fair value of this loan is calculated using a model which uses a combination of observable market data (such as interest rate curves and Retail Price Index swap prices) and unobservable inputs which require estimation, such as the discount rate, property price volatility and the haircut applied to individual sales prices. The model projects the future cash flows anticipated from the loan based on the contractual terms with the third party from which the mortgages were acquired, with the timing of those cash flows determined with reference to mortality tables (which are subject to estimation uncertainty). The model also calculates a value for the no negative equity guarantee provided to the customer using a stochastic methodology applying a variant of the Black-Scholes formula.

Notes to the Accounts (continued)

2. Critical accounting estimates and judgements (continued)

b. Significant accounting estimates and assumptions (continued)

The key estimates used in the model and the basis of estimation are summarised below:

Assumption	Basis of estimation
Discount rate	Derived from current market rates for new equity release loans adjusted for the specific profile of the Group's portfolio, also reflects liquidity term premium in current market funding costs
Property price volatility	Analysis of historic property price volatility and third party research with judgement overlay giving estimate of 10%
Sales price haircut	Average actual discounts observed on the portfolio in the previous two financial years

At 30 June 2021 the book value of the collateral loan was £211.4m (30 June 2020: £227.5m; 31 December 2020: £222.0m). The sensitivity of this value to the estimates shown above is as follows:

Assumption	Change to current assumption	(Decrease) / increase in fair value of collateral loan (£m)
Discount rate	+ / - 0.5 percentage points	(10.7) / 11.5
Property price volatility	+ / - 3 percentage points	(6.2) / 4.9
Sales price haircut	+ / - 5 percentage points	(6.4) / 5.8

The sensitivities shown reflect a range of alternative assumptions based on observed historic data and regulatory guidance.

3. Interest receivable and similar income

	Six months to 30 June 2021 (Unaudited) £m	Six months to 30 June 2020 (Unaudited) £m	Year to 31 December 2020 (Audited) £m
Interest receivable calculated using the effective interest rate method:			
On loans fully secured on residential property	**221.3**	225.4	447.1
On other loans and advances to customers	**0.3**	0.4	0.7
On investment securities	**2.4**	6.6	9.6
On other liquid assets	**0.8**	3.2	4.2
Total interest receivable calculated using the effective interest rate method	**224.8**	235.6	461.6
Similar income/(expense) on instruments held at fair value through profit or loss:			
On other loans and advances to customers	**5.2**	5.2	10.2
Net expense on derivatives which hedge financial assets and are designated in accounting hedge relationships	**(18.3)**	(11.4)	(31.4)
Net expense on derivatives which hedge financial assets and are not designated in accounting hedge relationships	**(10.1)**	(10.3)	(37.8)
Total similar income on instruments held at fair value through profit or loss	**(23.2)**	(16.5)	(59.0)
Total interest receivable and similar income	**201.6**	219.1	402.6
Included in the above is:			
Interest receivable on impaired financial assets	**3.5**	3.6	6.8

Notes to the Accounts (continued)

4. Interest payable and similar charges

	Six months to 30 June 2021 (Unaudited) £m	Six months to 30 June 2020 (Unaudited) £m	Year to 31 December 2020 (Audited) £m
Interest payable on instruments held at amortised cost			
On shares held by individuals	**58.9**	91.2	163.1
On subscribed capital	**5.4**	5.4	10.8
On deposits and other borrowings:			
Wholesale and other funding	**14.1**	31.1	50.8
Subordinated liabilities	**1.5**	-	-
Lease liabilities	**0.1**	0.2	0.3
Total interest payable on instruments held at amortised cost	**80.0**	127.9	225.0
Similar charges/(income) on instruments held at fair value through profit or loss			
Net income on derivatives which hedge financial liabilities and are designated in accounting hedge relationships	**(4.2)**	(8.0)	(12.3)
Net income on derivatives which hedge financial liabilities and are not designated in accounting hedge relationships	**(1.9)**	(0.5)	(15.5)
Total similar charges on instruments held at fair value through profit or loss	**(6.1)**	(8.5)	(27.8)
Total interest payable and similar charges	**73.9**	119.4	197.2

5. Fair value losses from financial instruments

	Six months to 30 June 2021 (Unaudited) £m	Six months to 30 June 2020 (Unaudited) £m	Year to 31 December 2020 (Audited) £m
Fair value hedge relationships			
Derivatives designated in fair value hedge relationships	**66.5**	(72.6)	(58.2)
Fair value adjustment for hedged risk of hedged items	**(65.4)**	68.5	51.1
Derivatives not designated in fair value hedge relationships			
Equity release swaps	**8.7**	(12.9)	(11.2)
Cross currency swaps net of retranslation on matched Euro liabilities	**2.2**	0.9	(0.7)
Other derivatives	**(5.8)**	(2.6)	(4.0)
Other financial instruments measured at FVTPL			
Collateral loan which represents a pool of equity release mortgages	**(7.4)**	9.4	6.2
Total fair value losses from financial instruments	**(1.2)**	(9.3)	(16.8)
The net position on the cross currency swaps and options includes:			
Movement in fair value of cross currency swaps	**(4.7)**	0.8	(2.8)
Movement in exchange rate on retranslation of cross currency swaps	**(49.6)**	59.5	44.4
Movement in exchange rate on retranslation of matched Euro liabilities	**56.5**	(59.4)	(42.3)
Net fair value gains / (losses) on cross currency swaps and matched liabilities	**2.2**	0.9	(0.7)

Notes to the Accounts (continued)

6. Administrative expenses

	Six months to 30 June 2021 £m	Six months to 30 June 2020 £m	Year to 31 December 2020 £m
Staff costs			
Wages and salaries	**24.2**	23.6	47.3
Social security costs	**2.8**	2.4	5.0
Pension costs	**3.8**	3.3	6.8
Other staff costs	**1.7**	1.2	2.0
Remuneration of auditor	**0.3**	0.3	0.6
Other administrative expenses			
Technology	**5.7**	5.0	10.4
Property	**3.3**	2.5	4.9
Development activity	**3.3**	0.6	4.1
Marketing	**1.5**	1.6	2.5
Legal and professional fees	**1.8**	1.0	2.5
Regulatory fees	**1.3**	1.1	2.5
Other	**3.2**	2.9	4.3
Total administrative expenses	**52.9**	**45.5**	**92.9**

7. Impairment on loans and advances to customers

	Six months to 30 June 2021 (Unaudited) £m	Six months to 30 June 2020 (Unaudited) £m	Year to 31 December 2020 (Audited) £m
Loans fully secured on residential property	**(0.6)**	11.7	14.7
Loans fully secured on land	**(0.1)**	-	(0.1)
Total impairment (gains) / losses for the period	**(0.7)**	11.7	14.6

The Group's policy for calculating impairment of loans and advances to customers is detailed in note 1e of the 2020 Annual Report and Accounts.

7. Impairment on loans and advances to customers (continued)

The table below summarises the Group's retail mortgage balances, loan commitments and associated impairment loss provisions.

	30 June 2021 (Unaudited)			30 June 2020 (Unaudited)		
		Impairment			Impairment	
	Gross exposure £m	**Loss provision £m**	**Provision coverage %**	Gross exposure £m	Loss provision £m	Provision coverage %
Retail mortgages						
Stage 1	**15,165.8**	**9.3**	**0.06**	13,801.0	4.3	0.03
Stage 2 and <30 days past due	**1,925.2**	**11.3**	**0.59**	2,597.5	13.8	0.53
Stage 2 and 30+ days past due	**86.9**	**1.2**	**1.37**	62.2	1.2	1.98
Stage 3	**186.7**	**19.4**	**10.39**	171.7	15.5	9.03
COVID-19 and economic PMAs*	**-**	**-**	**-**	-	5.9	-
Total retail mortgages	**17,364.6**	**41.2**	**0.24**	16,632.4	40.7	0.24
Loan commitments						
Stage 1	**1,153.9**	**-**	**0.01**	440.1	-	0.02

* COVID-19 and economic PMAs were reported at aggregated level at 30 June 2020 rather than being allocated across stages. In subsequent periods, these PMAs are included within the impairment loss provisions reported against each stage.

	31 December 2020 (Audited)		
		Impairment	
	Gross exposure £m	Loss provision £m	Provision coverage %
Retail mortgages			
Stage 1	14,287.6	7.7	0.05
Stage 2 and <30 days past due	2,243.1	15.1	0.67
Stage 2 and 30+ days past due	83.9	1.8	2.15
Stage 3	180.7	18.2	10.07
Total retail mortgages	16,795.3	42.8	0.25
Loan commitments			
Stage 1	651.8	-	0.01

7. Impairment on loans and advances to customers (continued)

The tables below provide information on movements in the gross retail mortgage exposures and associated impairment loss provisions during the year to date:

Six months to 30 June 2021

	Stage 1 12m ECL £m	Stage 2 Lifetime ECL £m	Stage 3 Lifetime ECL £m	Total £m
Gross exposure at 1 January 2021	14,287.6	2,327.0	180.7	16,795.3
Transfers resulting in increased impairment loss provision:				
From Stage 1 to Stage 2	(540.9)	540.9	-	-
From Stage 1 to Stage 3	(7.0)	-	7.0	-
From Stage 2 to Stage 3	-	(33.2)	33.2	-
Transfers resulting in reduced impairment loss provision:				
From Stage 2 to Stage 1	673.7	(673.7)	-	-
From Stage 3 to Stage 1	2.1	-	(2.1)	-
From Stage 3 to Stage 2	-	16.3	(16.3)	-
New advances	2,282.6	-	-	2,282.6
Redemptions and repayments	(1,532.3)	(165.2)	(15.8)	(1,713.3)
Gross exposure at 30 June 2021	**15,165.8**	**2,012.1**	**186.7**	**17,364.6**

	Stage 1 12m ECL £m	Stage 2 Lifetime ECL £m	Stage 3 Lifetime ECL £m	Total £m
Impairment loss provision at 1 January 2021	7.7	16.9	18.2	42.8
Transfers resulting in increased impairment loss provision:				
From Stage 1 to Stage 2	(0.5)	2.2	-	1.7
From Stage 1 to Stage 3	-	-	0.2	0.2
From Stage 2 to Stage 3	-	(0.9)	2.3	1.4
Transfers resulting in reduced impairment loss provision:				
From Stage 2 to Stage 1	0.4	(1.4)	-	(1.0)
From Stage 3 to Stage 1	-	-	-	-
From Stage 3 to Stage 2	-	0.2	(0.6)	(0.4)
Change in impairment loss provision resulting from loan modifications	-	0.2	0.1	0.3
Other remeasurement of impairment loss provision (no movement in stage)	0.4	(4.1)	0.7	(3.0)
New advances	1.5	-	-	1.5
Redemptions and repayments	(0.2)	(0.6)	(0.6)	(1.4)
Write offs	-	-	(0.9)	(0.9)
Impairment loss provision at 30 June 2021	**9.3**	**12.5**	**19.4**	**41.2**

Six months to 30 June 2020

	Stage 1 12m ECL £m	Stage 2 Lifetime ECL £m	Stage 3 Lifetime ECL £m	Total £m
Gross exposure at 1 January 2020	15,048.1	1,548.3	172.1	16,768.5
Transfers resulting in increased impairment loss provision:				
From Stage 1 to Stage 2	(1,475.9)	1,475.9	-	-
From Stage 1 to Stage 3	(7.3)	-	7.3	-
From Stage 2 to Stage 3	-	(23.4)	23.4	-
Transfers resulting in reduced impairment loss provision:				
From Stage 2 to Stage 1	291.4	(291.4)	-	-
From Stage 3 to Stage 1	3.8	-	(3.8)	-
From Stage 3 to Stage 2	-	18.0	(18.0)	-
New advances	1,103.5	-	-	1,103.5
Redemptions and repayments	(1,162.6)	(67.7)	(9.3)	(1,239.6)
Gross exposure at 30 June 2020	**13,801.0**	**2,659.7**	**171.7**	**16,632.4**

7. Impairment on loans and advances to customers (continued)

	Stage 1 12m ECL £m	Stage 2 Lifetime ECL £m	Stage 3 Lifetime ECL £m	Total £m
Impairment loss provision at 1 January 2020	3.7	9.9	15.1	28.7
Transfers resulting in increased impairment loss provision:				
From Stage 1 to Stage 2	(0.5)	4.9	-	4.4
From Stage 1 to Stage 3	-	-	0.4	0.4
From Stage 2 to Stage 3	-	(0.4)	1.6	1.2
Transfers resulting in reduced impairment loss provision:				
From Stage 2 to Stage 1	0.3	(0.8)	-	(0.5)
From Stage 3 to Stage 1	-	-	-	-
From Stage 3 to Stage 2	-	0.3	(1.1)	(0.8)
Change in impairment loss provision resulting from loan modifications	-	-	0.1	0.1
Other remeasurement of impairment loss provision (no movement in stage)	0.6	1.3	0.5	2.4
New advances	0.3	-	-	0.3
Redemptions and repayments	(0.1)	(0.2)	(0.6)	(0.9)
Write offs	-	-	(0.5)	(0.5)
Impairment loss provision at 30 June 2020 (excluding PMAs)	**4.3**	**15.0**	**15.5**	**34.8**
COVID-19 and economic PMAs*				5.9
Impairment loss provision at 30 June 2020 (including PMAs)				**40.7**

* COVID-19 and economic PMAs were reported at aggregated level at 30 June 2020 rather than being allocated across stages. In subsequent periods, these PMAs are included within the impairment loss provisions reported against each stage.

Year to 31 December 2020

	Stage 1 12m ECL £m	Stage 2 Lifetime ECL £m	Stage 3 Lifetime ECL £m	Total £m
Gross exposure at 1 January 2020	15,048.1	1,548.3	172.1	16,768.5
Transfers resulting in increased impairment loss provision:				
From Stage 1 to Stage 2	(1,338.9)	1,338.9	-	-
From Stage 1 to Stage 3	(22.9)	-	22.9	-
From Stage 2 to Stage 3	-	(40.3)	40.3	-
Transfers resulting in reduced impairment loss provision:				
From Stage 2 to Stage 1	446.9	(446.9)	-	-
From Stage 3 to Stage 1	4.5	-	(4.5)	-
From Stage 3 to Stage 2	-	28.9	(28.9)	-
New advances	2,562.2	-	-	2,562.2
Redemptions and repayments	(2,412.3)	(101.9)	(21.2)	(2,535.4)
Gross exposure at 31 December 2020	**14,287.6**	**2,327.0**	**180.7**	**16,795.3**

	Stage 1 12m ECL £m	Stage 2 Lifetime ECL £m	Stage 3 Lifetime ECL £m	Total £m
Impairment loss provision at 1 January 2020	3.7	9.9	15.1	28.7
Transfers resulting in increased impairment loss provision:				
From Stage 1 to Stage 2	(0.7)	4.4	-	3.7
From Stage 1 to Stage 3	-	-	1.5	1.5
From Stage 2 to Stage 3	-	(0.6)	3.1	2.5
Transfers resulting in reduced impairment loss provision:				
From Stage 2 to Stage 1	0.2	(1.2)	-	(1.0)
From Stage 3 to Stage 1	-	-	-	-
From Stage 3 to Stage 2	-	0.4	(1.7)	(1.3)
Change in impairment loss provision resulting from loan modifications	-	0.1	0.2	0.3
Other remeasurement of impairment loss provision (no movement in stage)	3.9	4.4	2.5	10.8
New advances	0.9	-	-	0.9
Redemptions and repayments	(0.3)	(0.5)	(1.2)	(2.0)
Write offs	-	-	(1.3)	(1.3)
Impairment loss provision at 31 December 2020	**7.7**	**16.9**	**18.2**	**42.8**

In the above tables, the impact of changes to accounting estimates and judgements, including macroeconomic scenarios and probability weightings, is included within 'other remeasurement of impairment loss provision' unless the change results in the transfer of a loan between stages in which case it is included in the relevant transfer row.

Notes to the Accounts (continued)

8. Taxation

The standard rate of corporation tax applicable to the Group for the six months ended 30 June 2021 was 19% (six months ended June 2020: 19%, year ended December 2020: 19%). An increase in the UK corporation tax rate to 25% with effect from 1 April 2023 was substantively enacted on 24 May 2021. 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 33% reflecting the increased corporation tax rate effective from 1 April 2023 and the 8% banking surcharge.

9. Loans and advances to customers

30 June 2021 (Unaudited)	**Gross exposure £m**	**Impairment loss provision £m**	**Total £m**
Loans fully secured on residential property	**17,364.6**	**(41.2)**	**17,323.4**
Loans fully secured on land	**16.0**	**(1.8)**	**14.2**
Other loans	**213.9**	**(2.5)**	**211.4**
Total loans and advances to customers	**17,594.5**	**(45.5)**	**17,549.0**

30 June 2020 (Unaudited)	Gross exposure £m	Impairment loss provision £m	Total £m
Loans fully secured on residential property	16,632.4	(40.7)	16,591.7
Loans fully secured on land	17.0	(1.9)	15.1
Other loans	230.0	(2.5)	227.5
Total loans and advances to customers	16,879.4	(45.1)	16,834.3

31 December 2020 (Audited)	Gross exposure £m	Impairment loss provision £m	Total £m
Loans fully secured on residential property	16,795.3	(42.8)	16,752.5
Loans fully secured on land	16.3	(1.9)	14.4
Other loans	224.5	(2.5)	222.0
Total loans and advances to customers	17,036.1	(47.2)	16,988.9

10. Retirement benefit surplus

	30 June 2021 (Unaudited) £m	30 June 2020 (Unaudited) £m	31 December 2020 (Audited) £m
Present value of funded obligations	**(114.3)**	(122.2)	(124.1)
Present value of unfunded obligations	**(0.8)**	(0.8)	(0.9)
Assets at fair value	**117.2**	127.5	126.0
Surplus	**2.1**	4.5	1.0

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.

Notes to the Accounts (continued)

11. Subordinated liabilities

In March 2021, the Group issued £350m of Senior Non-Preferred Fixed Rate Reset Notes under its £2bn Euro Medium Term Note Programme. The notes are denominated in sterling and have a fixed interest rate of 1.5% payable semi-annually to 16 March 2026, followed by a further year at the benchmark gilt rate plus 1.3% until maturity on 16 March 2027.

The accounting policy, presentation and method of computation adopted for subordinated liabilities are consistent with those applied by the Group for other financial liabilities that are classified as 'at amortised cost' (see note 1d of the 2020 Annual Report and Accounts for further details).

The notes rank behind the claims of all other creditors and members of the Society, other than holders of Permanent Interest Bearing Shares (PIBS) and Tier 2 capital.

12. Related party transactions

The Group had no related party transactions outside the normal course of business in the six months ended 30 June 2021 (six months ended June 2020: none, year ended December 2020: none).

13. Guarantees and other financial commitments

a. Financial Services Compensation Scheme

The Group has a contingent liability in respect of contributions to the Financial Services Compensation Scheme (FSCS) provided by the Financial Services and Markets Act 2000. The FSCS provides compensation to depositors in the event that a financial institution is unable to repay amounts due and is funded by contributions from the financial services industry.

b. Capital commitments

The Group has capital commitments contracted for but not accrued for under executory contracts of £3.9m (June 2020: £15.0m, December 2020: £5.3m) relating to technology investment programmes and other projects. This amount is inclusive of value added tax.

c. Other commitments

The Group is committed to a multi-year service contract for the provision and maintenance of its IT infrastructure. The remaining commitment at 30 June 2021 is £20.3m (June 2020: £25.9m, December 2020: £22.7m). This service contract does not meet the definition of a lease under IFRS 16 – Leases since it does not give the Group the right to control the assets used to provide the service.

Notes to the Accounts (continued)

14. Credit risk on loans and advances to customers

Retail mortgages

A full analysis of credit risk on retail mortgages is included in note 31 of the 2020 Annual Report and Accounts.

The table below provides information on the Group's retail mortgages by payment due status, excluding impairment losses. The table includes £8.2m (June 2020: £8.9m, December 2020: £8.6m) of loans and advances secured on residential property in Spain that are past due and £0.9m (June 2020: £1.3m, December 2020: £1.0m) in possession.

	30 June 2021 (Unaudited)		30 June 2020 (Unaudited)		31 December 2020 (Audited)	
	£m	**%**	£m	%	£m	%
Not past due	**16,990.5**	**97.9**	16,312.4	98.0	16,444.1	97.9
Past due up to 3 months	**260.3**	**1.6**	227.4	1.4	244.3	1.5
Past due 3 to 6 months	**42.3**	**0.2**	43.8	0.3	49.1	0.3
Past due 6 to 12 months	**42.2**	**0.2**	27.9	0.2	33.9	0.2
Past due over 12 months	**25.6**	**0.1**	12.9	0.1	19.4	0.1
Possessions	**3.7**	**-**	8.0	0.0	4.5	-
Total	**17,364.6**	**100.0**	16,632.4	100.0	16,795.3	100.0

The Group continues to use forbearance arrangements as part of its arrears management strategies to minimise credit risk, whilst ensuring customers are treated fairly. This includes the use of arrangements to assist borrowers in arrears that are now able to meet agreed repayment strategies, including or excluding arrears balances. The Group's approach to forbearance is described on page 181 of the 2020 Annual Report and Accounts and is materially unchanged.

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 2021 (Unaudited)	30 June 2020 (Unaudited)	31 December 2020 (Audited)
	%	%	%
<70%	**84.3**	82.7	85.8
70% - 80%	**9.8**	10.3	9.2
80% - 90%	**5.2**	5.4	4.4
>90%	**0.7**	1.6	0.6
Total	**100.0**	100.0	100.0

The overall weighted average indexed loan to value of the residential portfolio is 52.2% (June 2020: 52.2%, December 2020: 50.9%).

Notes to the Accounts (continued)

15. 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 2021 (Unaudited)		30 June 2020 (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**	**1,816.0**	**1,816.0**	1,382.3	1,382.3
Loans and advances to credit institutions	**Level 2**	**368.0**	**368.0**	170.3	170.3
Loans and advances to customers:					
Loans fully secured on residential property	**Level 3**	**17,323.4**	**19,045.7**	16,591.7	18,398.3
Other loans	**Level 2**	**14.2**	**14.2**	15.1	15.1
Financial liabilities					
Shares	**Level 2**	**14,470.8**	**14,532.6**	14,201.7	14,313.5
Amounts owed to credit institutions	**Level 2**	**1,998.6**	**1,998.6**	1,211.3	1,211.3
Amounts owed to other customers	**Level 2**	**293.6**	**293.6**	113.7	113.7
Debt securities in issue	**Level 1**	**2,132.7**	**2,163.8**	2,971.9	2,956.1
Debt securities in issue	**Level 2**	**173.0**	**172.6**	205.7	205.6
Subordinated liabilities	**Level 1**	**347.6**	**350.1**	-	-
Subscribed capital	**Level 1**	**233.4**	**251.1**	242.0	287.0

			31 December 2020 (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	1,823.2	1,823.2
Loans and advances to credit institutions	Level 2	201.9	201.9
Loans and advances to customers:			
Loans fully secured on residential property	Level 3	16,752.5	18,575.2
Other loans	Level 2	14.4	14.4
Financial liabilities			
Shares	Level 2	14,162.7	14,267.7
Amounts owed to credit institutions	Level 2	1,497.3	1,497.3
Amounts owed to other customers	Level 2	256.7	256.7
Debt securities in issue	Level 1	2,698.6	2,786.9
Debt securities in issue	Level 2	202.1	202.0
Subscribed capital	Level 1	241.5	251.8

Notes to the Accounts (continued)

15. 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 2020 Annual Report and Accounts and remain unchanged since December 2020.

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 2021 (Unaudited)	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
Assets				
Investment securities	**96.1**	**782.9**	**-**	**879.0**
Derivative financial instruments	**-**	**133.0**	**-**	**133.0**
Loans and advances to customers	**-**	**-**	**211.4**	**211.4**
Fair value adjustment for hedged risk on loans and advances to customers	**-**	**-**	**(23.1)**	**(23.1)**
Total assets	**96.1**	**915.9**	**188.3**	**1,200.3**
Liabilities				
Fair value adjustment for hedged risk on shares	**-**	**-**	**(51.7)**	**(51.7)**
Derivative financial instruments	**-**	**102.8**	**59.4**	**162.2**
Total liabilities	**-**	**102.8**	**7.7**	**110.5**

As at 30 June 2020 (Unaudited)	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets				
Investment securities	346.1	1,098.7	-	1,444.8
Derivative financial instruments	-	233.1	2.2	235.3
Loans and advances to customers	-	-	227.5	227.5
Fair value adjustment for hedged risk on loans and advances to customers	-	-	113.8	113.8
Total assets	346.1	1,331.8	343.5	2,021.4
Liabilities				
Fair value adjustment for hedged risk on shares	-	-	(18.9)	(18.9)
Derivative financial instruments	-	211.1	67.3	278.4
Total liabilities	-	211.1	48.4	259.5

As at 31 December 2020 (Audited)	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets				
Investment securities	57.1	892.6	-	949.7
Derivative financial instruments	-	190.9	1.9	192.8
Loans and advances to customers	-	-	222.0	222.0
Fair value adjustment for hedged risk on loans and advances to customers	-	-	96.1	96.1
Total assets	57.1	1,083.5	320.0	1,460.6
Liabilities				
Fair value adjustment for hedged risk on shares	-	-	(13.5)	(13.5)
Derivative financial instruments	-	171.8	66.1	237.9
Total liabilities	-	171.8	52.6	224.4

Notes to the Accounts (continued)

15. Fair values (continued)

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

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 or 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 and includes 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.

Details of the recurring fair value measurements of assets and liabilities are provided in the 2020 Annual Report and Accounts on page 202.

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

Six months to 30 June 2021 (Unaudited)	**Derivative financial instruments £m**	**Loans and advances to customers £m**	**Fair value adjustment for hedged risk £m**	**Total £m**
Balance at 1 January 2021	**(64.2)**	**222.0**	**109.6**	**267.4**
Total gains / (losses) in the Income Statement	**4.8**	**(7.4)**	**-**	**(2.6)**
Movement in fair value adjustment for hedged risk on loans and advances to customers	**-**	**-**	**(119.2)**	**(119.2)**
Movement in fair value adjustment for hedged risk on shares	**-**	**-**	**38.3**	**38.3**
Net repayment in the period	**-**	**(3.2)**	**-**	**(3.2)**
Balance at 30 June 2021	**(59.4)**	**211.4**	**28.7**	**180.7**

Six months to 30 June 2020 (Unaudited)	Derivative financial instruments £m	Loans and advances to customers £m	Fair value adjustment for hedged risk £m	Total £m
Balance at 1 January 2020	(54.8)	219.4	54.2	218.8
Total (losses) / gains in the Income Statement	(10.3)	9.4	-	(0.9)
Movement in fair value adjustment for hedged risk on loans and advances to customers	-	-	89.9	89.9
Movement in fair value adjustment for hedged risk on shares	-	-	(11.4)	(11.4)
Net repayment in the period	-	(1.3)	-	(1.3)
Balance at 30 June 2020	(65.1)	227.5	132.7	295.1

15. Fair values (continued)

c. Reconciliation of level 3 fair value measurements of financial instruments (continued)

Year to 31 December 2020 (Audited)	Derivative financial instruments £m	Loans and advances to customers £m	Fair value adjustment for hedged risk £m	Total £m
Balance at 1 January 2020	(54.8)	219.4	54.2	218.8
Total (losses) / gains in the Income Statement	(9.4)	6.2	-	(3.2)
Movement in fair value adjustment for hedged risk on loans and advances to customers	-	-	72.2	72.2
Movement in fair value adjustment for hedged risk on shares	-	-	(16.8)	(16.8)
Net repayment in the year	-	(3.6)	-	(3.6)
Balance at 31 December 2020	(64.2)	222.0	109.6	267.4

Total gains / (losses) for the period are included in fair value gains less losses from financial instruments in the Income Statement.

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 price haircut, mortality, early prepayment and the discount rate used to discount future cash flows. Wherever possible these input assumptions are calculated with reference to historic experience. The variables considered to have the largest impact on the value of the loan are property price volatility, sales price haircut and the discount rate. The sensitivities below reflect a range of alternative assumptions based on observed historic data and regulatory guidance.

At 30 June 2021, a 300 basis points increase in assumed property price volatility would reduce the value of the collateral loan by £6.2m and a 300 basis points decrease in assumed property price volatility would increase the value of the collateral loan by £4.9m. A 500 basis points increase in the sales price haircut would reduce the value of the collateral loan by £6.4m and a 500 basis points decrease in the sales price haircut would increase the value of the collateral loan by £5.8m. A 50 basis points increase in the discount rate would reduce the value of the collateral loan by £10.7m and a 50 basis points decrease in the discount rate would increase the value of the collateral loan by £11.5m.

(ii) Derivative financial instruments (equity release swaps)

The valuation of equity release swaps 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 2021, a 20% proportionate increase in mortgage repayments would lead to a reduction in the fair value of the mortgages in the hedge relationship of £0.1m. A 20% proportionate decrease in mortgage repayments would lead to an increase in the fair value of the mortgages of £0.1m.

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

There have been no subsequent events between 30 June 2021 and the date of approval of this Interim Financial Report by the Board which would have had a material impact on the financial position of the Group.

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, which have been prepared in accordance with International Accounting Standard 34 'Interim Financial Reporting', gives a true and fair view of the assets, liabilities, financial position and profit or loss of the Society and the undertakings included in the consolidation as a whole; and
- 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).

Signed on behalf of the Board of Directors:

Iain Cornish Chairman	Richard Fearon Chief Executive Officer	Andrew Conroy Chief Financial Officer

29 July 2021

Independent Review Report to Leeds Building Society

We have been engaged by 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 2021 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 16. 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.

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 Society will be prepared in accordance with United Kingdom adopted International Financial Reporting Standards. 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'.

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 Financial Reporting Council for use in the United Kingdom. A review of interim financial information consists of making inquiries, 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 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.

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 2021 is not prepared, in all material respects, in accordance with the International Accounting Standard 34 and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Use of our report

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.

Deloitte LLP

Statutory Auditor

Leeds, United Kingdom

29 July 2021