HALF YEAR
FINANCIAL REPORT

2022

Building your future

Principality
Building Society
Cymdeithas Adeiladu

Where home matters
principality.co.uk

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Forward Looking Statements

This interim 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. Therefore, actual results may differ materially from those expressed or implied by these forward-looking statements.

The Directors undertake no obligation to update any forward-looking statements whether as a result of new information, future events or otherwise.

Chief Executive's review

Interim Report

It has been a challenging first half of the year with the cost of living crisis, and the political upheaval, both at home and abroad, continuing to bite. I'm pleased to say that as a result of our strong first half financial results, we have been able to focus our efforts on supporting our colleagues, members, and communities where possible, to try and reduce their worries about the current challenges.

Supporting our members through difficult times

We have supported our members with their savings and mortgages during this turbulent economic period. Back in February we made a promise to keep open our branches in all the towns and cities we currently operate in Wales and England until at least 2025, giving our members, colleagues, and communities' confidence that we will retain a presence on the high street.

As inflation has increased, the Bank of England base rate has increased by 1% and we have worked to balance the differing needs of our mortgage and savings customers. We have only passed on a quarter of that rise to our SVR and discount mortgage members, whilst 99% of members who save with us have benefited from at least three rate increases ensuring we are offering competitive returns for our savers as interest rates rise. As a result, on average Principality are paying savers 0.70% for savings versus the market average of 0.29% over the last 12 months[1].

Our award-winning customer service has helped us support our members, as reflected in our Net Promoter Score of almost 81, which means this percentage of customers who spoke to us say they would recommend Principality to their family and friends.

Helping our colleagues

Colleagues were initially given an average wage increase of 3% earlier this year, however, as inflation exceeded 9% during May, Principality responded by providing colleagues with an additional £1,000 to help them with the increasing cost of living, as food, fuel and energy prices increase significantly. We have also recently updated our colleague financial support policy to give a short-term interest-free loan to prevent colleagues' financial situation from drastically declining.

Listening to the ways our colleagues want to work means they can choose to work in our newly refurbished office, or at home. We believe in a fully hybrid model that gives them choice to shape how, when and where they work best in a way that balances the needs of members, Principality, their teams, and their personal circumstances.

There are clear benefits of hybrid working, especially for the wellbeing of our colleagues, cutting down on the cost of commuting as well as lessening the impact on the climate. Our colleagues clearly enjoy this decision as reflected in Principality being ranked 9th in the UK as a Great Place to Work® in the super large business category, and number one in the UK as a Great Place to Work® for women.

Helping more people find a place to call home

Principality's Commercial team once again contributed in creating communities, funding an extra 157 homes for the final phase of the Mill housing project in Cardiff – now totalling, a mix of 800 affordable and private homes all supported by our loans. A £16.0m loan to Caredig housing association, serving South West Wales, sees further progress in the Society's ambitions to create more affordable homes for people in areas that need them most. There was also high demand from housing developers for the £20.0m green fund, with further plans to create more products to help the building industry create a greener, more sustainable Wales.

Greater social impact for communities

Our Board and executive team took a decision to provide greater financial resource to support areas of our communities that most need it across Wales. Each year we plan to set aside up to three per cent of our profit for social purpose activities, and in the first half of this year, we have invested £117,000 towards community grants via our Future Generations Fund. This is on top of the business donating £100,000 to kickstart our brilliant charity partnerships with Ty Hafan and Ty Gobaith Hope House children's hospices.

[1] Source: CACI's CSDB, Stock, June 2021 to May 2022, latest data available.

Chief Executive's review (continued)

Greater social impact for communities (continued)

Our financial education projects have also gone from strength to strength as we sponsored Young Enterprise's Fiver Challenge in primary schools in Wales and for the first time across England also. Earlier this year we committed £100,000 to the London Institute of Banking and Finance who are educating secondary school children towards GCSE equivalent qualifications in finance, which means we have now helped to educate 18,000 school children and young people in the past six months.

The awful events in Ukraine saw our colleagues and members ask us to get involved. Earlier this year Principality donated £20,000 to the Disasters Emergency Committee (DEC) with a further £6,000 donated to the Ukraine Humanitarian Appeal by generous colleagues and members. As a mutual building society with a purpose of making a difference to the lives of people and communities, we decided to also offer up to five homes to accommodate and support Ukrainian refugees who have been displaced. The building society has already successfully housed one family and is in discussions with other councils across Wales to hand more families keys to a safe place they can call home.

A path to net zero

I'm delighted our journey to become a more sustainable and environmentally sound business continues to progress. This year we received carbon neutral status and our newly refurbished head office has a sustainable design with recycled materials, as well as using existing furniture so we minimised waste and our carbon footprint. It is a healthy start but there is more work to be done before we can become net zero in our operations which we hope to achieve by 2030.

Strong performance

As a building society owned by our members, our aim is to focus on the long-term and invest to support the future growth of the Society and support our members, not meet short term shareholder needs.

Our financial performance was strong in the first six months, with £99.3m growth in our mortgage book (£24.7m June 2021), as we helped 1,936 first-time buyers get a home. More than £2.5bn in applications were processed through the new mortgage platform since it was launched. This means that mortgage applications could be processed faster than before, and we can continue to grow and launch new services in the future knowing we are building on strong foundations.

Underlying profit[2] reached £26.1m (£28.6m June 2021), whilst statutory profit before tax for the period is £31.0m (£33.1m June 2021), so members can be assured that our capital position is strong enough to withstand any potential difficulties facing the wider economy with our capital ratio standing at 30.79% (30.85% at 31 December 2021[3]) . We will use our profitability to reinvest in the business for the benefit of our members and support our purpose of making a difference in our communities.

Outlook

The future remains uncertain as the cost of living and political upheaval looks set to continue, with higher interest rates and inflation and slow economic growth. We will remain focused on our purpose; to create better homes for members, help members to financially secure their futures, as well as trying to create a fairer society for our communities. Principality continues to be a strong and secure Society, and we will continue to seek innovative ways to create affordable solutions for homeowners, first-time buyers, as well supporting savers and our colleagues for the rest of the year.

Julie-Ann Haines
Chief Executive Officer
9 August 2022

[2] Underlying profit before tax is further explained in the Income Statement on page 4.

[3] From the 1 January 2022 the Society applied a new calculation methodology in order to comply with new regulatory changes. The reported capital ratio as at 31 December 2021 was 33.99%.

Business review
for the six months ended 30 June 2022

Key Performance Indicators

Performance against our strategy is measured through a number of key performance indicators that are aligned to our strategic pillars.

	Six months to 30 June 2022	Six months to 30 June 2021	Year ended 31 December 2021
Purpose Led Organisation			
Net Retail Mortgage Growth	£99.3m	£24.7m	£(142.4)m
Net Retail Savings Growth	£(5.8)m	£(21.2)m	£(238.4)m
Brand Consideration[1]	26.0%	28.0%	24.0%
Cost Income Ratio[2]	63.2%	69.0%	70.5%
Stand-Out Experience			
Net Promoter Score[3]	80.9	80.8	80.5
Statutory Profit Before Tax	£31.0m	£33.1m	£64.0m
Underlying Profit Before Tax[4]	£26.1m	£28.6m	£54.4m
Net Interest Margin	1.32%	1.14%	1.17%
Common Equity Tier 1 Ratio[5]	30.79%	30.70%	33.99%

[1] Brand consideration measures whether a respondent would actively consider Principality the next time they take out a financial product or service. (Source: Beaufort Wales Omnibus)
[2] The cost income ratio measures management expenses (administration expenses, depreciation and amortisation) as a proportion of total income.
[3] Source: Internal survey data for the six months ended 30 June 2022.
[4] Underlying profit before tax is further explained in the Income Statement section below.
[5] Excluding unaudited interim profits/losses. The equivalent ratio including unaudited interim profits at 30 June 2022 would be 32.01%.

The above key performance indicators, apart from profit/loss before tax, are alternative performance measures (APMs) which are used internally to inform key management decisions. Further information on these APMs can be found within the 2021 Annual Report and Accounts within the strategic report and glossary sections.

Financial performance

Income statement

As detailed in the Chief Executive's review, the underlying profit before tax for the six months to 30 June 2022 was £26.1m (30 June 2021: £28.6m). Statutory profit before tax was £31.0m (30 June 2021: £33.1m). Both measures reflect the ongoing strong performance of the Society, and support the ability to invest in the long-term.

In the prior periods presented, profit has been impacted by large releases of impairment provisions for loan losses, however in the current period group provisions have remained relatively consistent with the 31 December 2021 position resulting in a modest release of £0.2m (30 June 2021: release of £9.1m).

	30 June 2022 £m	30 June 2021 £m	31 December 2021 £m
Statutory Profit Before Tax	**31.0**	**33.1**	**64.0**
Adjusted for:			
Fair value gains	(4.9)	(4.5)	(9.6)
Underlying profit before tax	26.1	28.6	54.4

The purpose of the underlying measure is to reflect management’s view of the group’s underlying performance, presented to aid comparability across reporting periods by adjusting for items which affect statutory measures but are deemed to be either non-recurring or fair value movements which are predominantly driven by swap prices that are outside of management's control. This aligns to measures used by management to monitor the performance of the business.

Business review (continued)
for the six months ended 30 June 2022

Net interest margin

Net interest margin for the period was 1.32% (30 June 2021: 1.14%). The Bank of England Base Rate increases created a favourable variance on interest rate hedging instruments and liquid asset interest. This was partially offset by an increase in wholesale funding costs, higher interest payable on customer deposits, marginally lower commercial lending balances and the continued planned reduction in loan assets held in the secured personal lending portfolio to £93.5m (31 December 2021: £108.4m). This has resulted in a £15.0m increase in interest receivable and a £7.2m increase in interest payable.

Fair value movements

Fair value movements represent the change in value of certain assets and liabilities to reflect underlying market rates. These movements are primarily timing differences, which will reverse as the asset or liability approaches maturity. During the period, the group recognised a gain of £4.9m in the income statement (30 June 2021: £4.5m gain) in relation to these movements in fair value.

Operating expenses

Operating expenses increased when compared with the same period last year at £45.3m (30 June 2021: £44.0m). These were expected to increase following increased IT costs as we move to a hybrid working model and costs associated with a new change delivery structure. The reduction in the cost income ratio is due primarily to an increase in net interest income. Focus on managing the core cost base of the business as a proportion of assets remains a priority. The management expense ratio has increased marginally at the half year due to the slightly higher cost base and a lower level of assets.

Total operating expenses are set out in the table below:

	30 June 2022 £m	30 June 2021 £m	31 December 2021 £m
Retail financial services	43.7	42.4	89.8
Commercial lending	1.3	1.3	2.6
Secured personal lending	0.3	0.3	0.7
Total operating expenses	45.3	44.0	93.1
Management expense ratio[1]	0.85%	0.81%	0.84%
Cost income ratio	63.2%	69.0%	70.5%

[1] The management expense ratio measures cost as a proportion of mean assets.

Impairment provisions for losses on loans and advances

The impairment provision movement over the first half of the year was a release of £0.2m to £17.6m (30 June 2021: release of £9.1m to £25.0m). The group takes a conservative approach to lending and has robust affordability, credit quality and underwriting standards. The performance of the group's loan portfolios continues to be strong with low levels of arrears, while rising house prices have led to lower potential losses. However, management are required to incorporate forward-looking information into their calculation of expected credit losses, and the economic outlook has worsened given the cost of living crisis and the war in Ukraine. The net effect of these factors is that provisions have remained relatively consistent with the position at 31 December 2021 (£17.8m).

While the group position has remained consistent, there have been movements within the group's individual loan portfolios, as disclosed in the table overleaf. Each portfolio uses a different model to calculate provisions, which have different sensitivities to changes in the current and forecasted economic environment.

Impairment provisions for losses on loans and advances (continued)

Total impairment provisions held are as follows:

	30 June 2022 £m	30 June 2021 £m	31 December 2021 £m
Retail mortgages	7.5	8.9	8.3
Secured personal lending	3.2	4.4	3.1
Commercial lending	6.9	11.7	6.4
Total	17.6	25.0	17.8

Statement of financial position

Total assets have reduced to £10,539.2m (31 December 2021: £10,907.9m). A reduction was anticipated, as wholesale funds raised through the TFS have begun to be repaid, and one of the group's residential mortgage backed security (RMBS) issuances was also repaid during the period. This offset the increase in derivative financial instruments caused by rising interest rates in the first half of the year.

Loans and advances to customers

The retail mortgage portfolio increased to £8,132.6m (31 December 2021: £8,033.3m), and the quality of the loans remains strong with an average balance to value of 52.9% (31 December 2021: 55.7%). The commercial lending portfolio also increased to £782.4m (31 December 2021: £776.3m), and the secured personal lending portfolio continued to run off, decreasing to £93.5m (31 December 2021: £108.4m).

Funding

Funding levels are closely monitored to maintain a diverse and balanced funding base. The majority of funding comes from retail savings, which has remained flat at £7,934.6m (31 December 2021: £7,943.8m) as a result of a more competitive retail savings market due to rising interest rates.

Capital and liquidity

The group's Common Equity Tier 1 ratio, which measures qualifying capital reserves as a proportion of risk weighted assets, is 30.79% as at 30 June 2022 (31 December 2021: 30.85%). The Common Equity Tier 1 ratio presented in the 2021 financial statements was 33.99%, however this included the Capital Requirements Regulation Quick Fix Package for intangible assets which no longer applies and has been removed in the above comparative. The reduction has also been caused by the requirement to apply a post model adjustment to reflect the expected eventual uplift in risk weights and associated pillar 1 capital requirements brought about by new regulations. This adjustment remains under review.

The PRA leverage ratio, which measures Tier 1 capital as a proportion of total on and off balance sheet assets, is 6.43% at the end of the period (31 December 2021: 6.38%). The ratio disclosed in the 31 December 2021 financial statements was the EBA leverage ratio which was 5.56%.

The capital position remains robust and both ratios are well above the minimum regulatory requirements.

The business continues to hold a conservative buffer of high quality liquid assets, with a liquidity ratio of 14.3% (31 December 2021: 16.6%). The Liquidity Coverage Ratio (LCR) is 196.2% at 30 June 2022 (31 December 2021: 242.3%), which remains well above the current regulatory minimum of 100%.

Business review (continued)
for the six months ended 30 June 2022

Principal risks and uncertainties

The principal risks and uncertainties affecting the group were set out in the Risk Overview section of the Strategic Report in the Annual Report and Accounts for the year ended 31 December 2021. These risks are categorised as: credit, market, liquidity and funding, conduct, operational, business, solvency and legal and regulatory risk, and are common to most financial services firms in the UK.

These remain the principal risks to the group at 30 June 2022.

The group is monitoring the impact of the Russia-Ukraine conflict and rising levels of inflation on the macroeconomic environment, the performance of the group's lending portfolios and the availability of funding. The impact on the group in relation to the Russia-Ukraine conflict is currently expected to be immaterial and the potential impact of rising inflation is considered as part of impairment provisioning on page 24. This will be closely monitored going forward.

Although the business is exposed to a number of potential risks and uncertainties, it is well placed to meet these challenges, with a diversified and flexible funding base, and strong levels of capital and liquidity.

Iain Mansfield
Chief Financial Officer
9 August 2022

Condensed consolidated income statement
Group interim results for six months to 30 June 2022

	Notes	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
Interest receivable and similar income	3	114.0	99.0	198.7
Interest payable and similar charges	4	(43.9)	(36.7)	(69.5)
Net interest income		70.1	62.3	129.2
Fees and commission receivable	5	1.7	2.1	3.9
Fees and commission payable		(1.0)	(0.9)	(1.8)
Net fee and commission income		0.7	1.2	2.1
Other operating income		0.5	0.3	0.8
Other fair value gains	6	4.9	4.5	9.6
Net operating income		76.2	68.3	141.7
Administrative expenses	7	(40.2)	(38.5)	(79.8)
Depreciation and amortisation		(5.1)	(5.5)	(10.8)
Other impairment losses		-	-	(2.5)
Operating expenses		(45.3)	(44.0)	(93.1)
Impairment credit for losses on loans and advances	14	0.2	9.1	15.4
Provisions for liabilities and charges	11	(0.1)	(0.3)	-
Operating profit and profit before taxation		31.0	33.1	64.0
Taxation expense	9	(6.8)	(7.2)	(15.2)
Profit for the period/year		24.2	25.9	48.8

Condensed consolidated statement of other comprehensive income
Group interim results for six months to 30 June 2022

	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
Profit for the period/year	24.2	25.9	48.8
Items that will not be reclassified subsequently to profit and loss:			
Actuarial gain on retirement benefit obligations	2.9	1.0	4.3
Tax on retirement benefit obligations	(0.7)	-	(1.0)
Items that may be reclassified subsequently to profit and loss:			
Loss on assets at fair value through other comprehensive income	(1.7)	(0.1)	(0.4)
Tax on assets at fair value through other comprehensive income	0.4	-	-
Total comprehensive income for the period/year	25.1	26.8	51.7

Condensed consolidated statement of financial position
Group interim results as at 30 June 2022

	Notes	30 June 2022 £m (Unaudited)	30 June 2021 £m (Unaudited)	31 December 2021 £m (Audited)
Assets				
Liquid assets:				
Cash in hand and balances with the Bank of England		1,121.2	1,409.9	1,645.8
Loans and advances to credit institutions		153.3	209.4	165.8
Debt securities		134.3	79.8	76.3
		1,408.8	1,699.1	1,887.9
Derivative financial instruments		189.8	26.1	52.8
Loans and advances to customers:				
Loans fully secured on residential property		8,569.3	8,833.9	8,598.2
Other loans		276.2	287.3	285.1
	10	8,845.5	9,121.2	8,883.3
Intangible fixed assets		25.5	26.4	26.0
Property, plant and equipment		39.3	36.5	36.6
Investment properties		6.1	6.6	6.2
Current tax assets		-	-	-
Deferred tax assets		2.3	1.3	2.3
Other assets		5.9	0.5	-
Retirement benefit obligations	8	6.1	-	3.2
Prepayments and accrued income		9.9	8.7	9.6
Total assets		10,539.2	10,926.4	10,907.9
Liabilities				
Shares		7,934.6	8,163.9	7,943.8
Deposits and debt securities:				
Amounts owed to credit institutions		1,163.8	1,069.0	1,296.2
Amounts owed to other customers		207.5	228.8	270.1
Debt securities in issue		502.3	755.2	696.0
		1,873.6	2,053.0	2,262.3
Derivative financial instruments		29.2	60.0	24.7
Current tax liabilities		0.1	1.0	0.8
Other liabilities		11.6	13.5	11.3
Provisions for liabilities	11	2.7	3.1	2.7
Accruals and deferred income		7.7	8.0	10.6
Deferred tax liabilities		8.3	2.6	5.4
Retirement benefit obligations	8	-	-	-
Total liabilities		9,867.8	10,305.1	10,261.6
General reserve		671.9	620.2	645.5
Other reserves		(0.5)	1.1	0.8
Total equity and liabilities		10,539.2	10,926.4	10,907.9

Condensed consolidated statement of changes in Members' interests
Group interim results for six months to 30 June 2022

	Six months to 30 June 2022 (Unaudited)		
	General Reserve £m	Fair Value through OCI reserve £m	Total equity attributable to Members £m
Balance at 1 January 2022	645.5	0.8	646.3
Comprehensive income/(expense) for the period	26.4	(1.3)	25.1
At 30 June 2022	671.9	(0.5)	671.4

	Six months to 30 June 2021 (Unaudited)		
	General Reserve £m	Fair Value through OCI reserve £m	Total equity attributable to Members £m
At 1 January 2021	593.4	1.2	594.6
Comprehensive income/(expense) for the period	26.8	(0.1)	26.7
At 30 June 2021	620.2	1.1	621.3

All items dealt with in arriving at the profit for the period, and the preceding financial periods, relate to continuing operations. The accounting policies and notes on pages 12 to 25 form part of these accounts.

Condensed consolidated statement of cash flows
Group interim results for six months to 30 June 2022

	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
Net cash flows from operating activities	(277.4)	117.8	372.8
Cash flows from investing activities			
Purchase of intangible assets	(1.6)	-	(5.7)
Purchase of property, plant and equipment	(5.6)	(6.6)	(7.7)
Purchase of investment securities	(62.3)	(9.0)	(8.7)
Proceeds from sale and maturity of investment securities	2.6	7.8	10.7
Net cash flows from investing activities	**(66.9)**	**(7.8)**	**(11.4)**
Cash flows from financing activities			
Interest paid on debt securities in issue	(5.5)	(5.5)	(11.1)
Proceeds from issuance of debt securities in issue	0.6	-	1.1
Redemption of debt securities in issue	(187.4)	(213.8)	(268.0)
Repayments of lease liabilities	(0.5)	(0.6)	(1.0)
Net cash flows from financing activities	**(192.8)**	**(219.9)**	**(279.0)**
(Decrease)/increase in cash and cash equivalents	(537.1)	(109.9)	82.4
Cash and cash equivalents at beginning of period/year	1,811.6	1,729.2	1,729.2
Cash and cash equivalents at end of period/year	**1,274.5**	**1,619.3**	**1,811.6**
Represented by:			
Cash and balances with the Bank of England	1,121.2	1,409.9	1,645.8
Loans and advances to credit institutions repayable on demand	153.3	209.4	165.8
	1,274.5	1,619.3	1,811.6
Operating activities			
Profit before taxation	31.0	33.1	64.0
Adjusted for:			
Depreciation and amortisation	5.1	5.7	10.8
Charge on defined benefit pension scheme	-	-	-
Impairment on loans and advances to customers	(0.2)	(9.1)	(15.4)
Imparirment on fixed assets	-	-	1.5
Impairment on intangible assets	-	-	1.0
Change in fair values	118.4	40.8	99.8
Change in other provisions	0.1	0.4	-
Interest on debt securities in issue	5.5	5.2	10.8
Non-cash items included in profit before tax	(0.2)	0.4	(0.4)
Changes in net operating assets			
Loans and advances to customers	(90.3)	46.1	223.1
Other operating assets	(4.6)	3.5	0.9
Derivative financial instruments	(132.6)	(48.6)	(110.6)
Shares	(5.8)	(21.2)	(238.4)
Deposits	(195.1)	70.3	338.8
Other operating liabilities	(2.1)	(2.6)	(2.1)
Contributions paid into defined benefit scheme	-	(1.7)	(1.7)
Taxation paid	(6.6)	(4.5)	(9.3)
Net cash flows from operating activities	**(277.4)**	**117.8**	**372.8**

Notes to the accounts
for the six months ended 30 June 2022

1. Basis of preparation

The condensed consolidated set of financial statements of the group for the half-year ended 30 June 2022 have been prepared in accordance with the Disclosure and Transparency Rules of the Financial Conduct Authority and with International Accounting Standard (IAS) 34 Interim Financial Reporting. The annual financial statements of the group are prepared in accordance with International Financial Reporting Standards (IFRS) and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) as adopted for use within the UK. The accounting policies adopted are consistent with those of the previous financial year.

Going concern

The Directors have assessed the viability of the group, taking into account business strategy, principal risks and current economic conditions. The approach taken is consistent with that undertaken at the 2021 year-end.

The Directors have considered the resilience of the group, taking account of its current position, the risks facing the business in severe but plausible scenarios and the effectiveness of any mitigating actions. The assessment has considered the potential impacts on the business model, future performance, capital adequacy and liquidity. The group's financial forecasts have been refreshed and take consideration of the expected impact of the COVID-19 pandemic, rising inflation and the Russia-Ukraine conflict on the macroeconomic environment, the performance of the group's lending portfolios and the availability of funding.

The group's most recent Internal Liquidity Adequacy Assessment Process (ILAAP) has recently been finalised and the Internal Capital Adequacy Assessment Process (ICAAP) is due to be approved imminently. Both are completed annually and use internal scenarios aligned to the Bank of England severity benchmarks and reflect the specific nature of the group's business. Included within these scenarios are substantial falls in residential and commercial property prices, increases in unemployment, changes to interest rates and reduced funding availability within wholesale and retail markets.

Having considered the plans and forecasts for the group, the Directors remain satisfied that the group has adequate resources and no material uncertainties that lead to significant doubt about the group's ability to continue in business for the foreseeable future. Accordingly, the financial statements continue to be prepared on a going concern basis.

New and amended standards adopted by the group

There were no new standards adopted in the current year.

Notes to the accounts
for the six months ended 30 June 2022

1. Basis of preparation (continued)

Impact of standards issued but not yet applied

There are no material impacts expected from issued standards and amendments to existing standards that are not yet applicable.

Judgements in applying accounting policies and critical accounting estimates

The critical judgements and areas of critical accounting estimates remain consistent with those disclosed in the 2021 Annual Report and Accounts, being impairment provisions on loans and advances (note 14), retirement benefit obligations (note 8) and provisions for customer and regulatory complaints (note 11).

2. Business segments

The group operates three main business segments: retail financial services, commercial lending and secured personal lending.

Transactions between the business segments are on normal commercial terms and conditions.

	Six months to 30 June 2022 (Unaudited)			
	Retail financial services £m	Commercial lending £m	Secured personal lending £m	Total £m
Net interest income	58.5	7.7	3.9	70.1
Other income and charges	5.5	0.6	-	6.1
Net operating income	64.0	8.3	3.9	76.2
Operating expenses	(43.7)	(1.3)	(0.3)	(45.3)
Impairment provision for losses on loans and advances	0.9	(0.4)	(0.3)	0.2
Provision for other liabilities and charges	-	-	(0.1)	(0.1)
Operating profit and profit before taxation	21.2	6.6	3.2	31.0
Taxation expense				(6.8)
Profit after taxation				24.2

	Six months to 30 June 2021 (Unaudited)			
	Retail financial services £m	Commercial lending £m	Secured personal lending £m	Total £m
Net interest income	51.4	7.2	3.7	62.3
Other income and charges	5.2	0.8	-	6.0
Net operating income	56.6	8.0	3.7	68.3
Operating expenses	(42.4)	(1.3)	(0.3)	(44.0)
Impairment provision for losses on loans and advances	3.9	4.1	1.1	9.1
Provision for other liabilities and charges	-	-	(0.3)	(0.3)
Operating (loss)/profit and loss before taxation	18.1	10.8	4.2	33.1
Taxation credit				(7.2)
Profit after taxation				25.9

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for the six months ended 30 June 2022

2. Business segments (continued)

	Year ended 31 December 2021 (Audited)			
	Retail financial services £m	Commercial lending £m	Secured personal lending £m	Total £m
Net interest income	106.6	14.4	8.2	129.2
Other income and charges	11.1	1.4	-	12.5
Net operating income	117.7	15.8	8.2	141.7
Operating expenses	(89.8)	(2.6)	(0.7)	(93.1)
Impairment provision for losses on loans and advances	3.8	9.2	2.4	15.4
Provision for liabilities	0.6	-	(0.6)	-
Operating profit and profit before taxation	32.3	22.4	9.3	64.0
Taxation expense				(15.2)
Profit after taxation				48.8

The group operates entirely within the UK, and therefore a geographical segment analysis is not presented.

	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
Total assets by business segments			
Retail financial services	9,643.3	10,029.7	10,008.5
Secured personal lending	127.0	124.3	124.5
Commercial lending	768.9	772.4	774.9
Total assets	10,539.2	10,926.4	10,907.9
Total liabilities and equity by business segment			
Retail financial services and Commercial lending	10,412.2	10,802.1	10,783.4
Secured personal lending	127.0	124.3	124.5
Total liabilities and equity	10,539.2	10,926.4	10,907.9

3. Interest receivable and similar income

	Group		
	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
On loans fully secured on residential property	103.9	106.9	213.1
On other loans	5.2	5.0	9.9
On debt securities	0.5	0.4	0.8
On other liquid assets	4.6	0.6	1.5
On derivative financial instruments	(0.2)	(13.9)	(26.6)
	114.0	99.0	198.7

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4. Interest payable and similar charges

	Group		
	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
On shares held by individuals	31.7	31.3	58.7
On deposits and debt securities	11.1	7.5	14.6
On subscribed capital	-	-	-
On lease liabilities	0.2	0.2	0.3
On derivative financial instruments	0.9	(2.3)	(4.1)
	43.9	36.7	69.5

5. Fees and commission receivable

	Group		
	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
Insurance and related financial service products	0.4	0.5	0.9
Mortgage related fees	1.3	1.6	3.0
	1.7	2.1	3.9

6. Other fair value gains and losses

	Group		
	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
Gains on derivatives in hedging relationships	124.9	44.0	107.0
(Losses)/Gains on derivatives not in hedging relationships	(1.6)	1.1	2.3
Gains on derivatives	123.3	45.1	109.3
(Losses)/Gains on economic hedged items	(1.2)	3.2	5.9
(Losses) on hedged items attributable to hedged risk	(117.2)	(43.8)	(105.6)
(Losses) on hedged items	(118.4)	(40.6)	(99.7)
	4.9	4.5	9.6

Other fair value gains and losses represent the difference between changes in the fair values excluding interest flows of the hedging derivatives and the changes in the fair values excluding interest flows of the underlying hedged items.

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for the six months ended 30 June 2022

7. Administrative expenses

	Group		
	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
Wages and salaries	21.1	20.3	41.4
Social security costs	2.0	1.8	3.7
Other pension costs	1.2	1.3	2.5
	24.3	23.4	47.6
Other administrative expenses	15.9	15.1	32.2
	40.2	38.5	79.8

8. Retirement benefit obligations

	Group		
	30 June 2022 £m (Unaudited)	30 June 2021 £m (Unaudited)	31 December 2021 £m (Audited)
Fair value of plan assets	64.7	82.0	84.7
Present value of funded and unfunded obligations	(58.6)	(82.0)	(81.5)
Pension scheme surplus	6.1	-	3.2

The pension scheme surplus has increased from £3.2m at December 2021 to £6.1m at 30 June 2022, as a result of actuarial gains of £2.9m during the period. The surplus is recognised as an asset of the Society, as the pension trust allows any surplus on winding up of the scheme to be repaid to the Society.

Significant actuarial assumptions in the determination of the defined benefit obligation are the discount rate, inflation rate and life expectancy. The sensitivity analysis below represents the net impact on the scheme liabilities of a 0.5% increase or decrease in each assumption.

	Group	
	Increase 0.5% £m	Decrease 0.5% £m
Discount rate	(4.2)	4.2
Inflation	4.2	(4.2)
Life expectancy (+1 year/ -1 year)	2.2	(2.2)

Notes to the accounts
for the six months ended 30 June 2022

9. Taxation

Taxation for the group for the 6 months to 30 June 2022 is charged at 21.9% (30 June 2021: 21.8%), representing the best estimate of the annual effective tax rate expected for the full year, applied to the forecast pre-tax income for the year and pro-rated for the six-month period. The effective statutory rate of corporation tax for the year ending December 2021 was 23.7%. The June 2022 and December 2021 tax charges/(credits) included the banking surcharge due to annual and estimated annual profits being above £25.0m.

The actual tax charge for the period differs from that calculated using the statutory rate of corporation tax in the UK as follows:

	Group		
	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
Profit before tax	31.0	33.1	64.0
Profit multiplied by the standard rate of corporation tax at 19.00% (2021: 19.00%)	5.9	6.3	12.2
Effects of:			
Expenses not deductible for tax purposes	(0.2)	0.1	-
Adjustments to prior years	-	-	0.6
Impact of banking surcharge	0.5	0.6	1.5
Impact of rate change	-	-	0.9
Timing differences	0.6	0.2	-
Tax charge	6.8	7.2	15.2

10. Loans and advances to customers

	Group		
	30 June 2022 £m (Unaudited)	30 June 2021 £m (Unaudited)	31 December 2021 £m (Audited)
Fully secured on residential property	8,736.1	8,810.5	8,637.2
Fully secured on land	276.2	287.3	285.1
	9,012.3	9,097.8	8,922.3
Provision for impairment losses	(17.6)	(25.0)	(17.8)
Unamortised loan origination fees	13.8	15.9	13.5
Fair value adjustment for hedged risk	(163.0)	32.5	(34.7)
	8,845.5	9,121.2	8,883.3

Notes to the accounts
for the six months ended 30 June 2022

11. Provisions for liabilities

	Group		
	30 June 2022 £m (Unaudited)	30 June 2021 £m (Unaudited)	31 December 2021 £m (Audited)
At beginning of the period/year	2.7	2.8	2.8
Charge for the period/year	0.1	0.3	-
Release during the period/year	(0.1)	-	(0.1)
At end of the period/year	2.7	3.1	2.7

The group continues to hold provisions in respect of various customer claims. The provision reflects management's best estimate of the costs required to settle its remaining obligations and takes account of expected customer behaviour, costs incurred with associated legal claims and an updated assessment of the remaining exposure population. The majority of the provision is expected to be utilised over the next three to five years.

Although a significant degree of uncertainty remains with regard to the ultimate cost of settling customer claims, the provision balance is expected to be sufficient to meet any remaining obligations. The provision will continue to be monitored and customer trends and behaviours analysed to ensure the provision remains appropriate.

12. Related party transactions

The group had no related party transactions outside the normal course of the business during the six months to 30 June 2022. Transactions for this period are similar to those for the year to 31 December 2021, details of which can be found in note 33 of the 2021 Annual Report and Accounts.

13. Financial instruments

Carrying values and fair values

The table below compares carrying values and fair values of the group’s financial instruments by category.

	30 June 2022		31 December 2021	
	Carrying Value £m (Unaudited)	Fair Value £m (Unaudited)	Carrying Value £m (Audited)	Fair Value £m (Audited)
Total assets				
Cash in hand and balances with Bank of England	1,121.2	1,121.2	1,645.8	1,645.8
Loans and advances to credit institutions	153.3	160.7	165.8	173.2
Debt securities	134.3	134.3	76.3	76.3
Derivative financial instruments	189.8	189.8	52.8	52.8
Loans and advances to customers	8,845.5	8,976.1	8,883.3	9,019.1
	10,444.1	10,582.1	10,824.0	10,967.2
Total liabilities				
Shares	7,934.6	7,955.5	7,943.8	7,961.5
Amounts owed to credit institutions	1,163.8	1,163.8	1,296.2	1,296.2
Amounts owed to other customers	207.5	207.5	270.1	270.1
Debt securities in issue	502.3	494.2	696.0	702.3
Derivative financial instruments	29.2	29.2	24.7	24.7
	9,837.4	9,850.2	10,230.8	10,254.8

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13. Financial instruments (continued)

Further details on the methods and assumptions which have been applied in determining fair value are set out in note 30 of the 2021 Annual Report and Accounts.

Assets and liabilities measured at fair value

	30 June 2022 (Unaudited)			
	£m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets at fair value through profit or loss:				
Derivative financial instruments	189.8	-	177.4	12.4
Financial assets at fair value through other comprehensive income:				
Debt securities	134.3	134.3	-	-
Total	324.1	134.3	177.4	12.4
Financial liabilities at fair value through profit or loss:				
Amounts owed to credit institutions	1.9	-	1.9	-
Debt securities in issue	(8.4)	(8.4)	-	-
Derivative financial instruments	29.2	-	16.8	12.4
Total	22.7	(8.4)	18.7	12.4

	30 June 2021 (Unaudited)			
	£m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets at fair value through profit or loss:				
Derivative financial instruments	26.1	-	21.8	4.3
Financial assets at fair value through other comprehensive income:				
Debt securities	79.8	79.8	-	-
Total	105.9	79.8	21.8	4.3
Financial liabilities at fair value through profit or loss:				
Amounts owed to credit institutions	1.9	-	1.9	-
Debt securities in issue	3.4	3.4	-	-
Derivative financial instruments	60.0	-	55.7	4.3
Total	65.3	3.4	57.6	4.3

	31 December 2021 (Audited)			
	£m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets at fair value through profit or loss:				
Derivative financial instruments	52.8	-	49.2	3.6
Financial assets at fair value through other comprehensive income:				
Debt securities	76.3	76.3	-	-
Total	129.1	76.3	49.2	3.6
Financial liabilities at fair value through profit or loss:				
Amounts owed to credit institutions	1.9	-	1.9	-
Debt securities in issue	(1.9)	(1.9)	-	-
Derivative financial instruments	24.7	-	21.1	3.6
Total	24.7	(1.9)	23.0	3.6

The tables above provide an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into levels 1 to 3 based on the degree to which the fair value is observable. This is detailed on the following page.

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13. Financial instruments (continued)

Hierarchy for fair value disclosures

Level	
1.	Quoted prices (unadjusted) in active markets for identical assets or liabilities.
2.	Inputs other than quoted prices included within level 1 that are observable for the asset or liability either directly or indirectly (i.e derived from prices).
3.	Inputs for the asset or liability that are not based on observable market data.

The items included within level 3 are interest rate swaps, the notional amounts for which track the amortisation profile of the mortgage assets within the Retail Mortgage Backed Securities (RMBS) structures. The valuations are calculated using present value calculations based on market interest rate curves and projected mortgage prepayment amounts. The unobservable inputs relate to the projection of the notional amounts of the swaps, which change over time to match the balance of the underlying mortgage portfolio. There were no significant inter-relationships between unobservable inputs that materially affect fair values.

The fair value of the level 3 derivatives is shown in the table below.

	Group		
	30 June 2022 £m (Unaudited)	30 June 2021 £m (Unaudited)	31 December 2021 £m (Audited)
Financial assets at fair value through profit or loss:			
At beginning of the period/year	3.6	9.0	9.0
Fair value gains/(losses)	9.1	(4.8)	(5.5)
Interest (paid)/received	(0.3)	0.1	0.1
At end of the period/year	12.4	4.3	3.6
Financial liabilities at fair value through profit or loss:			
At beginning of the period/year	3.6	9.0	9.0
Fair value losses/(gains)	9.1	(4.8)	(5.5)
Interest (received)/paid	(0.3)	0.1	0.1
At end of the period/year	12.4	4.3	3.6

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14. Credit risk

The table below shows the group's estimated maximum exposure to credit risk for all financial assets.

i) Loans and advances to customers

The group's exposure to credit risk relating to loans and advances to customers can be broken down by security as follows:

	Group		
	30 June 2022 £m (Unaudited)	30 June 2021 £m (Unaudited)	31 December 2021 £m (Audited)
In respect of loans and advances to customers:			
Secured by a first charge on residential property	8,641.1	8,684.8	8,528.0
Secured by a first charge on land	276.3	287.3	285.1
Secured by a second charge on residential property	94.9	125.7	109.2
	9,012.3	9,097.8	8,922.3
Provisions for impairment losses	(17.6)	(25.0)	(17.8)
Effective interest rate adjustments	13.8	15.9	13.5
Fair value adjustments	(163.0)	32.5	(34.7)
	8,845.5	9,121.2	8,883.3

The group's exposure to credit risk relating to loans and advances to customers by business segment split by stage in accordance with IFRS 9 is as follows:

	Retail Financial Services		Commercial Lending		Secured Personal Lending	
Stage	30 June 2022 £m (Unaudited)	31 December 2021 £m (Audited)	30 June 2022 £m (Unaudited)	31 December 2021 £m (Audited)	30 June 2022 £m (Unaudited)	31 December 2021 £m (Audited)
1	7,039.1	7,208.9	844.8	797.4	42.4	56.9
2	1,417.9	1,062.8	76.4	88.4	39.0	37.8
3	48.1	45.3	9.4	7.7	13.1	14.1
	8,505.1	8,317.0	930.6	893.5	94.5	108.8

The group's expected credit losses split by stage in accordance with IFRS 9 and by business segment is as follows:

	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
Retail financial services	7.5	8.9	8.3
Secured personal lending	3.2	4.4	3.1
Commercial lending	6.9	11.7	6.4
	17.6	25.0	17.8

14. Credit risk (continued)

The group's split of loans by stage in accordance with IFRS 9 and by business segment is as follows:

Retail Financial Services and Secured Personal Lending

Stage	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
1	82.4%	85.7%	86.2%
2	16.9%	13.6%	13.1%
3	0.7%	0.7%	0.7%
	100.0%	100.0%	100.0%

In determining ECLs at 30 June 2022, a change has been made to the Retail IFRS 9 model, removing the absolute long-run probability of default (LRPD) threshold, which prevented any customer with an LRPD of less than 10% from migrating to stage 2 unless the customer is in arrears. The removal of this threshold has increased the number of loans in stage 2 by approximately 5,600 resulting in an increase to ECLs of £0.2m.

Commercial Lending

Stage	6 months to 30 June 2022 £m (Unaudited)	6 months to 30 June 2021 £m (Unaudited)	Year ended 31 December 2021 £m (Audited)
1	90.8%	88.2%	89.2%
2	8.2%	10.5%	9.9%
3	1.0%	1.3%	0.9%
	100.0%	100.0%	100.0%

The average index-linked loan balance to value (BTV), in respect of the group's loans secured by a first or second charge on residential property, is 52.9% (31 December 2021: 55.7%).

The percentage of retail lending cases fully secured by a first charge, currently with arrears greater than three months, is 0.51% (31 December 2021: 0.50%).

Residential lending cases fully secured by a first charge which were six months or more in arrears had arrears balances of £1.2m (31 December 2021: £1.2m) with 215 (31 December 2021: 228) cases.

The percentage of secured personal loans currently in arrears by two months or more by number is 9.6% (31 December 2021: 9.19%), which by value is 11.16% (31 December 2021: 8.35%).

The critical accounting estimates applied in determining expected credit loss provisions are:

- determining criteria for identifying a significant increase in credit risk;
- choosing appropriate models and assumptions for the measurement of expected credit losses; and
- establishing the number and relative weightings of forward-looking economic scenarios.

14. Credit risk (continued)

Sensitivity analysis has been performed on the staging criteria. A 10% variance has been selected as this is deemed to be a reasonable variation which could occur over a 12 month period in the current economic environment. The impact of a 10% increase or reduction in the volume of loans in stage 2 is as follows:

Stage	Retail financial services £m	Secured personal lending £m	Commercial lending £m
Stage 1 to Stage 2	0.9	0.1	2.1
Stage 2 to Stage 1	(0.1)	(0.0)	(0.2)

Forward looking economic scenarios

Forecasts of economic variables together with probability weightings are supplied by an external provider. Economic scenarios have been selected which take account of a range of possible economic outcomes. Due to the levels of inflation currently experienced by the UK economy, and the worsening economic outlook in light of the war in Ukraine, the incumbent downside scenario has been replaced with a stagflation scenario. This new scenario assumes that interest rates will rise swiftly to stem inflation in the short-term, while the economy will underperform against its potential in the long-term.

House prices are a key variable in calculating expected losses, and they have experienced strong growth during the pandemic and to date. The base scenario forecast has worsened since December 2021, largely due to the higher interest rate environment, as borrowing costs are expected to increase. However, the severe downside outlook on house prices supplied by our external provider has improved, due to a shift in assumptions away from the epidemiological to the geopolitical. Management feel there is still a severe downside risk comparable with the position in December 2021, and in order to address this concern have restated the severe downside HPI forecast to reach the same house price trough as the December 2021 forecast, which is presented below.

Scenario	Weighting at 30 June 2022 %	2022 Scenario 2022 %	2023 %	2024 %	2025 %		Weighting at 31 Dec 2021 %	2021 Scenario 2022 %	2023 %	2024 %	2025 %
HPI (Growth)											
Base	50	4.1	2.9	4.8	2.2		50	3.4	6.0	5.2	3.7
Upside	20	10.7	13.1	4.6	(1.8)		20	14.2	8.5	4.8	2.1
Downside	23	0.2	(12.3)	(4.5)	3.4		23	(9.8)	(8.1)	(1.9)	4.4
Severe Downside	7	(6.7)	(16.8)	(5.4)	2.5		7	(13.4)	(10.3)	(2.5)	4.3

Scenario	Weighting at 30 June 2022 %	2022 Scenario 2022 %	2023 %	2024 %	2025 %		Weighting at 31 Dec 2021 %	2021 Scenario 2022 %	2023 %	2024 %	2025 %
Unemployment (Absolute)											
Base	50	3.9	4.4	4.6	4.7		50	4.7	4.4	4.4	4.5
Upside	20	3.5	3.7	3.8	4.0		20	3.9	3.3	3.5	3.8
Downside	23	4.3	6.6	7.1	7.1		23	6.2	6.6	6.5	6.3
Severe Downside	7	5.1	8.4	8.1	8.2		7	7.2	7.5	7.2	7.1

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14. Credit risk (continued)

Scenario	Weighting at 30 June 2022 %	2022 Scenario				Weighting at 31 Dec 2021 %	2021 Scenario			
		2022 %	2023 %	2024 %	2025 %		2022 %	2023 %	2024 %	2025 %
GDP (Growth)										
Base	50	9.9	3.7	2.9	2.5	50	6.8	4.6	2.5	1.7
Upside	20	11.6	4.8	2.6	2.3	20	11.3	3.7	2.9	2.3
Downside	23	9.2	3.8	(3.6)	1.7	23	(1.5)	5.3	2.9	2.2
Severe Downside	7	9.0	(6.7)	2.4	3.6	7	(3.8)	4.1	2.1	2.1

Post model adjustment - ERM sensitivity

There is a risk that the default volumes predicted by the ERM are not sensitive enough to the macroeconomic forecasts, particularly given the increased level of uncertainty since December 2021. This PMA effectively assumes that forecasted downturn PDs will increase in line with unemployment forecasts and restricts the impact of any other economic variables that reduce the downturn PDs, with unemployment chosen given the strong correlation between increased unemployment and defaults during the last major recession. The PMA impacts Significant Increase in Credit Risk (SICR) thresholds, resulting in an additional 2,600 loans in stage 2 and an increase to ECLs of £1.3m.

Post model adjustment - cost of living

This PMA captures the risk of the cost of living crisis impacting the ability of customers to repay their mortgages. Inflation is at a 40 year high and expected to climb higher before the end of 2022, while a further increase in the Ofgem price cap is due in October. Currently, the two largest drivers of the inflation are energy and food prices, which both form a larger proportion of expenditure for lower income individuals; as such the PMA has identified customers susceptible to rising prices by using both loan to income (LTI) and total income at origination. Customers in stage 1 with LTI of 4.45 or above or income below the National Living Wage have been given an average stage 2 ECL, uplifting ECLs by £1.6m. Decreasing the LTI threshold to 4.35 would increase the uplift by £0.4m, while increasing the income threshold to £25,000 would increase the uplift by £0.8m.

The IFRS 9 models calculate expected credit losses for each scenario and then apply the weightings to generate the weighted output for each model. Sensitivity analysis has been performed on the impact of each economic scenario. The table below shows the range of ECL impact between the most optimistic and the most severe scenario. The ECL range is the difference between applying a 100% weighting to the most severe downturn scenario and the upside scenario.

Portfolio	Upside £m	Severe Downside £m	ECL Range £m
Retail financial services	(2.0)	9.5	7.5
Secured personal lending	(1.9)	4.3	2.4
Commercial lending	(2.6)	5.7	3.1
Total	**(6.5)**	**19.5**	**13.0**

14. Credit risk (continued)

The tables below set out information on movements in impairment loss provisions on loans and advances to customers:

	Group			
	Stage 1 12 month ECL £m	Stage 2 Lifetime ECL £m	Stage 3 Lifetime ECL £m	Total £m
At 1 January 2022	3.1	8.9	5.8	17.8
Transfers:				
Stage 1 transfers	(1.2)	-	-	(1.2)
Stage 2 transfers	-	0.5	-	0.5
Stage 3 transfers	-	-	0.7	0.7
New loans	0.8	0.2	-	1.0
Settled loans	(0.2)	(1.2)	(0.4)	(1.8)
Changes in credit quality	3.5	(2.2)	(0.9)	0.4
Changes in loan model assumptions	(0.4)	0.1	0.5	0.2
Loss allowance at 30 June 2022	5.6	6.3	5.7	17.6

	Group			
	Stage 1 12 month ECL £m	Stage 2 Lifetime ECL £m	Stage 3 Lifetime ECL £m	Total £m
At 1 January 2021	5.1	18.7	10.5	34.3
Transfers:				
Stage 1 transfers	(2.7)	-	-	(2.7)
Stage 2 transfers	-	1.1	-	1.1
Stage 3 transfers	-	-	1.7	1.7
New loans	0.6	1.5	0.1	2.2
Settled loans	(0.8)	(2.2)	(3.1)	(6.1)
Changes in credit quality	2.4	(9.9)	(3.4)	(10.9)
Changes in loan model assumptions	(1.5)	(0.3)	-	(1.8)
Loss allowance at 31 December 2021	3.1	8.9	5.8	17.8

ii) Commercial

Loans secured on commercial property are diversified by industry type with the largest exposure to one counterparty amounting to £25.6m (31 December 2021: £26.3m) or 3.2% (31 December 2021: 3.3%) of gross balances.

Asset quality remains strong with impaired balances of £11.9m (31 December 2021: £7.2m), or 1.5% of gross balances (31 December 2021: 0.9%).

iii) Treasury

The treasury risk function monitors exposure concentrations against a variety of criteria including counterparty and country limits, and all exposures are well spread across this risk assessment framework.

Provisions for expected credit losses in relation to treasury instruments of £1.0m were held at 30 June 2022 (31 December 2021: £1.1m).

Responsibility statement

We confirm that to the best of our knowledge:

(a) the condensed set of financial statements has been prepared in accordance with IAS 34 *Interim Financial Reporting* as adopted by the UK;

(b) the interim management report includes a fair review of the information required by DTR 4.2.7 (indication of important events during the first six months and the description of principal risks and uncertainties for the remaining six months of the year); and

(c) the interim management report includes information required by DTR 4.2.8 (indication of any related party transactions that have taken place or any changes in the related party transactions described in the last annual report).

By order of the Board,

Julie-Ann Haines
Chief Executive Officer
9 August 2022

Independent review report to Principality Building Society

We have been engaged by the Principality Building Society (the "Society") to review the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2022 which comprises the condensed consolidated income statement, condensed consolidated statement of other comprehensive income, condensed consolidated statement of financial position, condensed statement of changes in Member's interests, condensed consolidated statement of cash flows and related notes 1 to 14.

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2022 is not prepared, in all material respects, in accordance with United Kingdom adopted International Accounting Standard 34 and the Disclosure Guidance and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Basis for Conclusion

We conducted our review in accordance with International Standard on Review Engagements (UK) 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.

As disclosed in note 1, the annual financial statements of the Society will be prepared in accordance with United Kingdom adopted international accounting standards . The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with United Kingdom adopted International Accounting Standard 34, "Interim Financial Reporting" and the Disclosure Guidance and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Conclusion Relating to Going Concern

Based on our review procedures, which are less extensive than those performed in an audit as described in the Basis for Conclusion section of this report, nothing has come to our attention to suggest that the directors have inappropriately adopted the going concern basis of accounting or that the directors have identified material uncertainties relating to going concern that are not appropriately disclosed.

This conclusion is based on the review procedures performed in accordance with this ISRE (UK), however future events or conditions may cause the entity to cease to continue as a going concern.

Responsibilities of the directors

The directors are responsible for preparing the half-yearly financial report in accordance with United Kingdom adopted International Accounting Standard 34, "Interim Financial Reporting" and the Disclosure Guidance and Transparency Rules of the United Kingdom's Financial Conduct Authority.

In preparing the half-yearly financial report, the directors are responsible for assessing the Society's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Society or to cease operations, or have no realistic alternative but to do so.

Auditor's Responsibilities for the review of the financial information

In reviewing the half-yearly financial report, we are responsible for expressing to the Society a conclusion on the condensed set of financial statement in the half-yearly financial report. Our conclusion, including our Conclusions Relating to Going Concern, are based on procedures that are less extensive than audit procedures, as described in the Basis for Conclusion paragraph of this report.

Independent review report to Principality Building Society (continued)

Use of our report

This report is made solely to the Society in accordance with International Standard on Review Engagements (UK) 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Financial Reporting Council. Our work has been undertaken so that we might state to the Society those matters we are required to state to it 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
Cardiff, UK
9 August 2022

Other information

The information for the period ended 30 June 2022 is unaudited and does not constitute accounts within the meaning of section 73 of the Building Societies Act 1986. The financial information for the year ended 31 December 2021 has been extracted from the Annual Report and Accounts for that year. The annual accounts for the year ended 31 December 2021 have been filed with the Financial Conduct Authority.

The auditor's report on the 2021 Annual Report and Accounts was not qualified and did not include a reference to any matters to which the auditor drew attention by way of emphasis without qualifying the report.

A copy of the this Half Year Financial Report is placed on Principality Building 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.

Glossary

Arrears	A customer is in arrears when they are behind in fulfilling their obligations with the result that an outstanding loan payment is overdue. Such a customer can also be said to be in a state of delinquency.
Brand consideration	Brand consideration measures whether a respondent would actively consider Principality the next time they take out a financial product or service.
Carbon Net Zero	Net zero means that we will reduce all of our scope 1 and 2 emissions to as little as possible by 2030 as well as the following elements of our scope 3 emissions: paper, water, external data centres, waste disposal, business travel, colleague commuting and home working. We will neutralise residual emissions with net zero aligned carbon removals. Scope 1 emissions - generated by directly owned or controlled sources i.e. fuel combustion and company-owned vehicles. Scope 2 emissions - purchased electricity. Scope 3 emissions - other indirect operational emissions that occur in the supply chain, both upstream and downstream.
Commercial lending	Secured loans to a commercial borrower.
Contractual maturity	The final payment date of a loan or other financial instrument, at which point the entire remaining outstanding principal and interest is due to be repaid.
Common Equity Tier 1 capital	The highest quality form of capital as defined in the Capital Requirements Directive IV, comprising accumulated reserves and qualifying instruments after regulatory deductions.
Common Equity Tier 1 capital ratio	Common Equity Tier 1 capital as a proportion of risk-weighted assets.
Cost income ratio	A ratio that represents the proportion of management expenses (i.e. administrative expenses, depreciation and amortisation) to total income.
Credit risk	The risk of financial loss arising from a failure of a customer or counterparty to settle their financial and contractual obligations as they fall due.
Debt securities in issue	Transferable certificates of indebtedness including certificates of deposits, and fixed and floating rate notes.
Defined benefit pension scheme	A scheme that defines the benefit an employee will receive on retirement, depending on such factors as age, length of service and salary.
Financial Conduct Authority (FCA)	The statutory body responsible for conduct of business regulation and supervision of UK authorised firms from 1 April 2013. The FCA also has responsibility for protecting consumers and promoting healthy competition.
Internal Capital Adequacy Assessment Process (ICAAP)	The group's internal assessment of the levels of capital that need to be held by the Society to meet its regulatory capital requirements.
Internal Liquidity Adequacy Assessment Process (ILAAP)	The group's internal assessment of the levels of liquidity that need to be held by the Society to meet its regulatory liquidity requirements.
Leverage ratio	A ratio which measures Tier 1 capital against total on and off balance sheet assets.
Liquid assets	Cash or other assets that can be readily converted to cash without loss of value.

Glossary (continued)

Liquidity Coverage Ratio (LCR)	A liquidity metric which aims to ensure that a firm maintains an adequate level of liquidity to meet its needs for a 30 calendar day time horizon under a severe stress scenario.
Loan To Value ratio (LTV)	A ratio showing outstanding loan balance as a percentage of the value of the security.
Management expense ratio	A ratio that measures cost as a proportion of mean assets.
Member	A person who has a share investment or a mortgage loan with the Society.
Net interest income	The difference between the interest received on assets and the interest paid on liabilities.
Net interest margin	This ratio calculates the net interest income as a percentage of mean total assets.
Net retail mortgage lending	Total movements in the retail mortgage book; includes all inflows and outflows in respect of retail lending.
Net retail savings growth	Total movements in the retail savings portfolio; includes all inflows and outflows in relation to retail savings.
Permanent Interest-Bearing Shares (PIBS)	Unsecured, Sterling denominated Additional Common Equity Tier 1 capital instruments repayable at the option of the Society.
Regulatory capital	Capital allowable under regulatory rules, less certain required regulatory adjustments and deductions.
Residential Mortgage Backed Securities (RMBS)	A category of asset backed security that represents interests in a group of residential mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and/or principal).
Retail loans	Loans to individuals rather than institutions, including residential mortgage lending.
Shares	Money deposited by Members in a retail savings account with the Society and held as a liability in the statement of financial position.
Subscribed capital	See Permanent Interest-Bearing Shares (PIBS).

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This leaflet is available in large print, Braille and audio tape on request by calling 0330 333 4000•

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