



## Agenda

### **David Anderson, Chief Executive, CFS**

- Balanced Scorecard

### **John Reizenstein, Chief Financial Officer, CFS**

- Performance

### **Paul Hemingway,**

### **Director of Financing & Risk, the Co-operative Group**

- tCG and United Merger

### **David Anderson, Chief Executive, CFS**

- Progress in the year
- What next

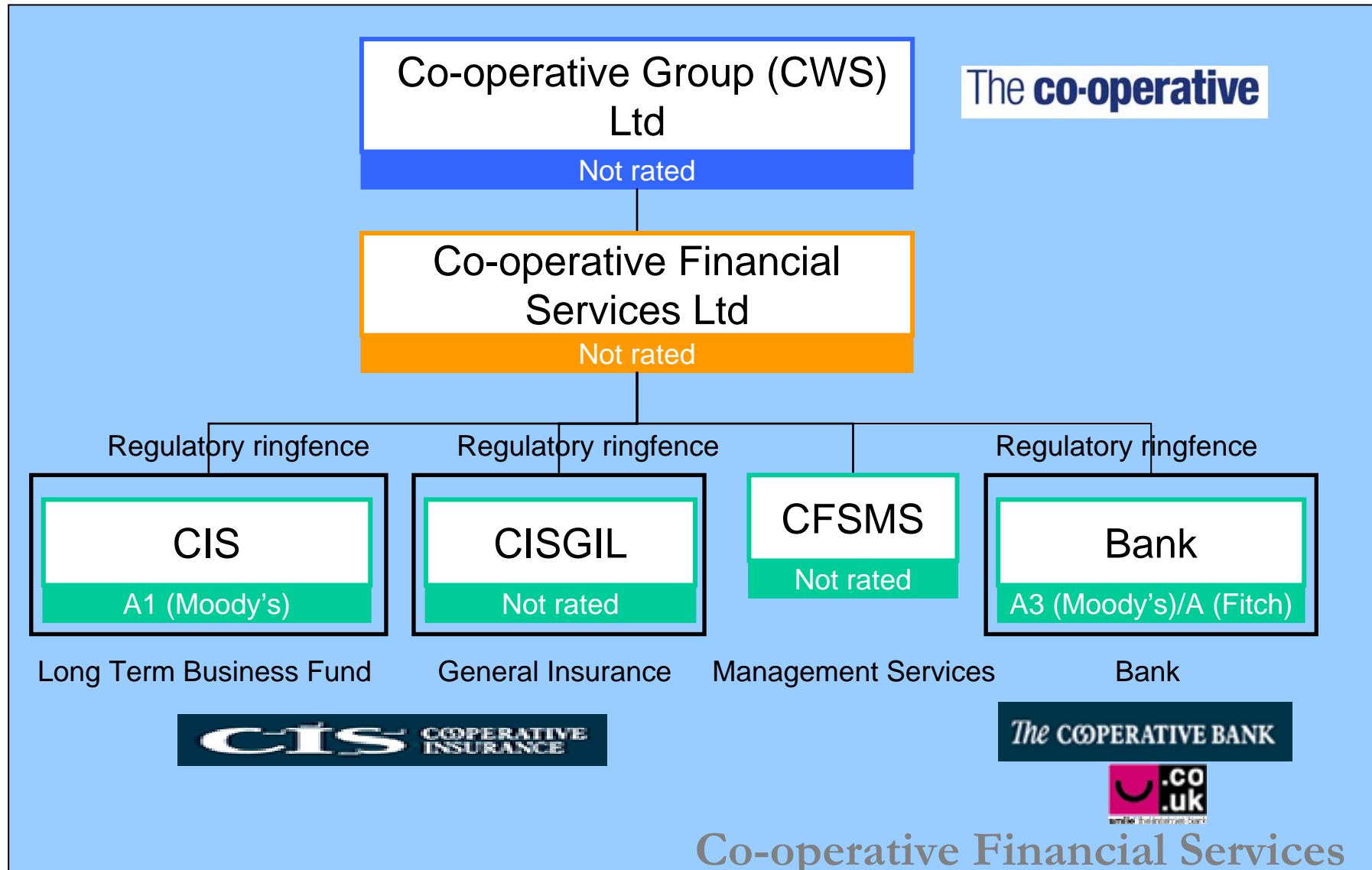
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# David Anderson

Chief Executive, CFS

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# Structure



## Balanced Scorecard

- **Key Performance Indicators**
  - Profit generation to create a sustainable model
  - Market leading customer satisfaction
  - Market leading colleague satisfaction
  - Market leading social responsibility approach
  - Membership growth

## Balanced Scorecard

### Profit generation to create a sustainable model

- CFS operating profit, before significant items, decreased £13.1m from £159.3m to £146.2m
  - General Insurance claims ratio down to 74% from 76% (2004 86%) leading to a technical result of £43.2m (2005:£40.6m, loss in 2004)
  - Bank profit before tax fell from £97.8m to £76.3m, with increased impairment charges and higher costs

Adjusted Shareholder profit £152m v target £162m

New business profit for L&S to breakeven - achieved

L&S maintenance expenses - £83m v target £95m

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## Balanced Scorecard

### Market leading customer satisfaction

From GFK NOP's Financial Research Survey:

Retail Bank 73.0% v 62.6% (top 5 by market share)

General Insurance 71.2% v 67.7% (top 5 by market share)

Life & Savings 44.0% v 42.0% (rest of market)

### Market leading colleague satisfaction

Response rate improved, now 86%

Colleague engagement and satisfaction level v 2006 target

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## Key Performance Indicators

### **Market leading social responsibility approach**

Unprompted awareness of social responsibility

Performance in BitC Corporate Responsibility Index

Bank – first (2005 4<sup>th</sup>) CIS – tenth (2005 22<sup>nd</sup>)

### **Membership growth**

Relaunched in September 2006.

1.5m members at launch, 2.0m by year end

Targeting 600,000 new members in 2007

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# John Reizenstein

Chief Financial Officer, CFS

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## Bank – Profit & Loss

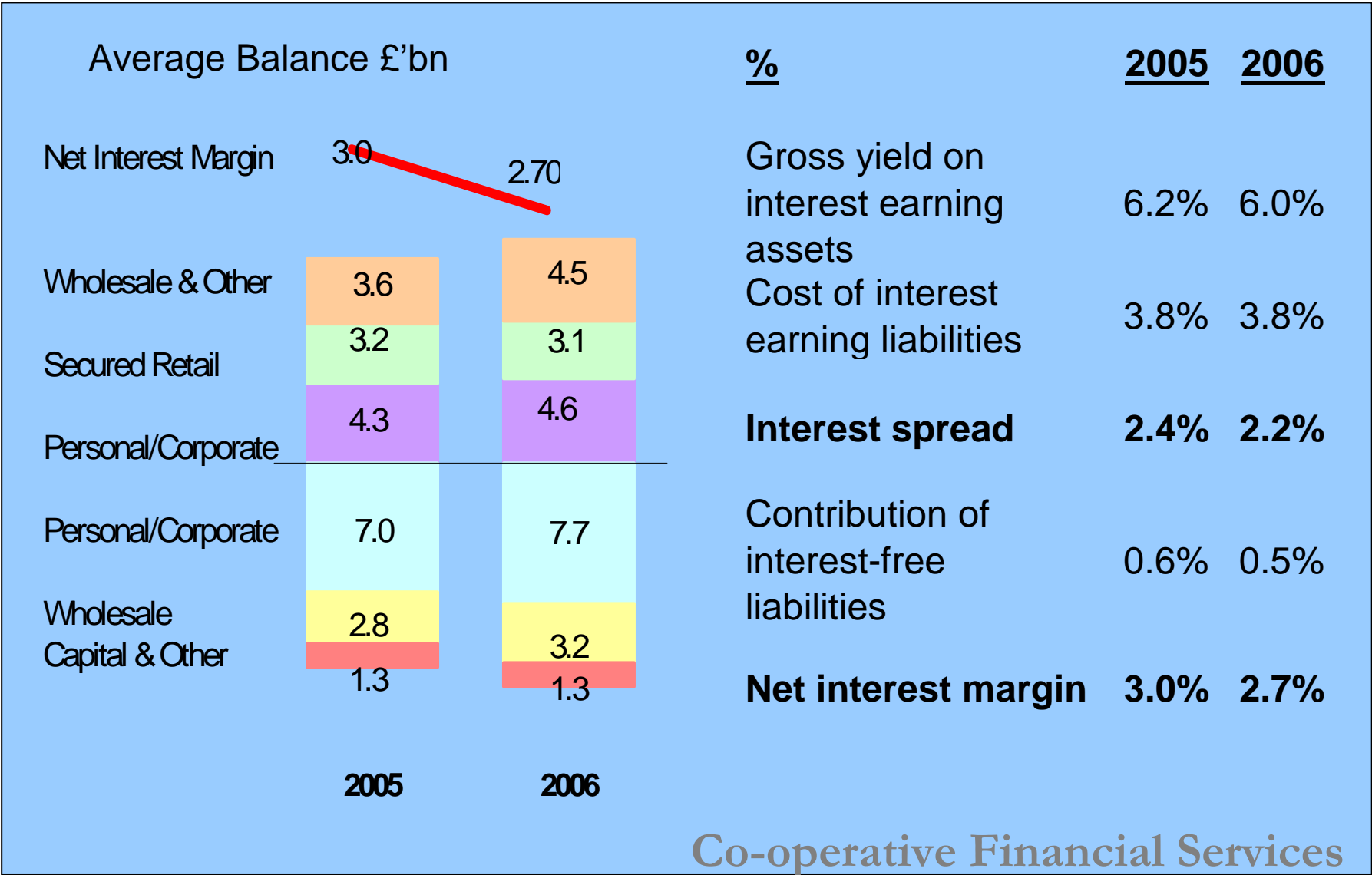
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<u>£m</u>	<u>2005</u>	<u>2006</u>	<u>Change</u>
Net Interest Income	320.5	320.3	(0.2)
Non Interest Income	205.9	201.2	(4.7)
<b>Operating Income</b>	<b>526.4</b>	<b>521.5</b>	<b>(4.9)</b>
Operating Expenses	(328.8)	(339.9)	(11.1)
<b>Operating Profit</b>	<b>197.6</b>	<b>181.6</b>	<b>(16.0)</b>
Impairment Losses	(99.8)	(105.3)	(5.5)
<b>Operating profit before Significant Items</b>	<b>97.8</b>	<b>76.3</b>	<b>(21.5)</b>
<b>Cost Income Ratio</b>	<b>62.5%</b>	<b>65.2%</b>	<b>2.7%</b>

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# Income Drivers



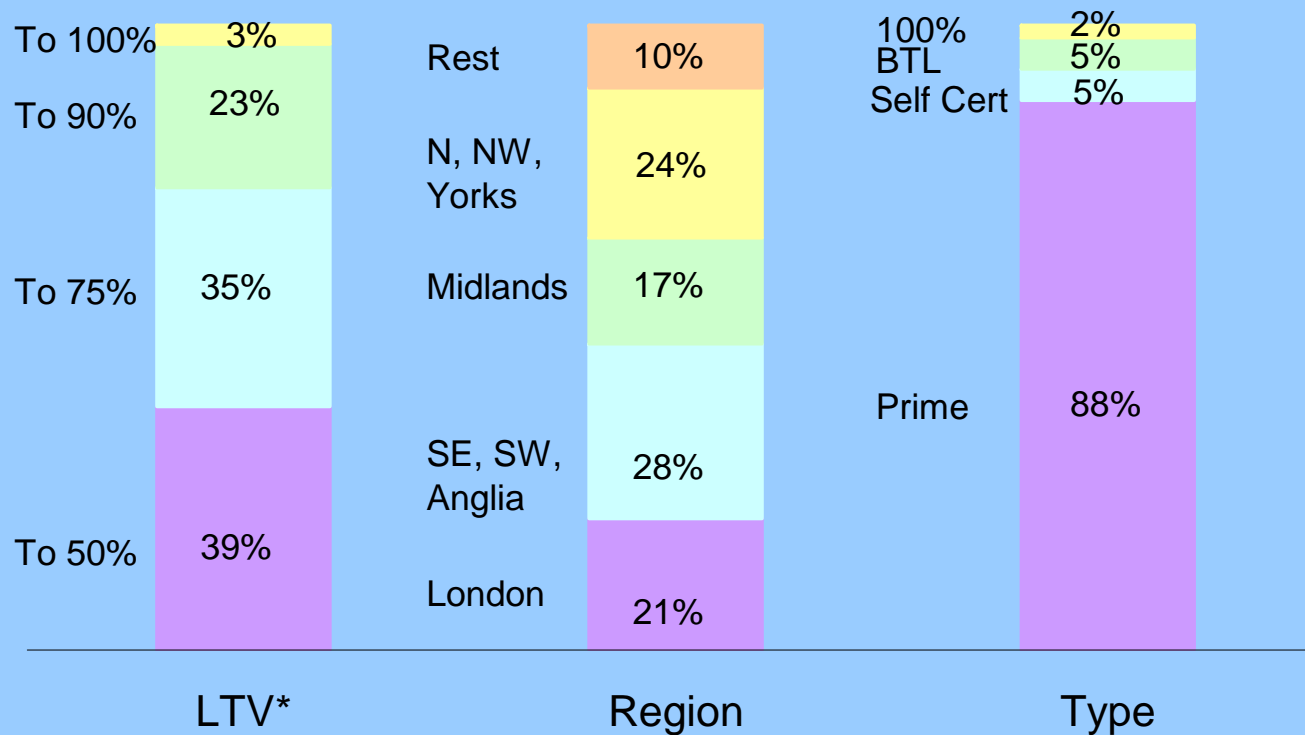
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# Stable Mortgage Portfolio

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£3.1bn mortgage book



\* LTV at last valuation, not indexed

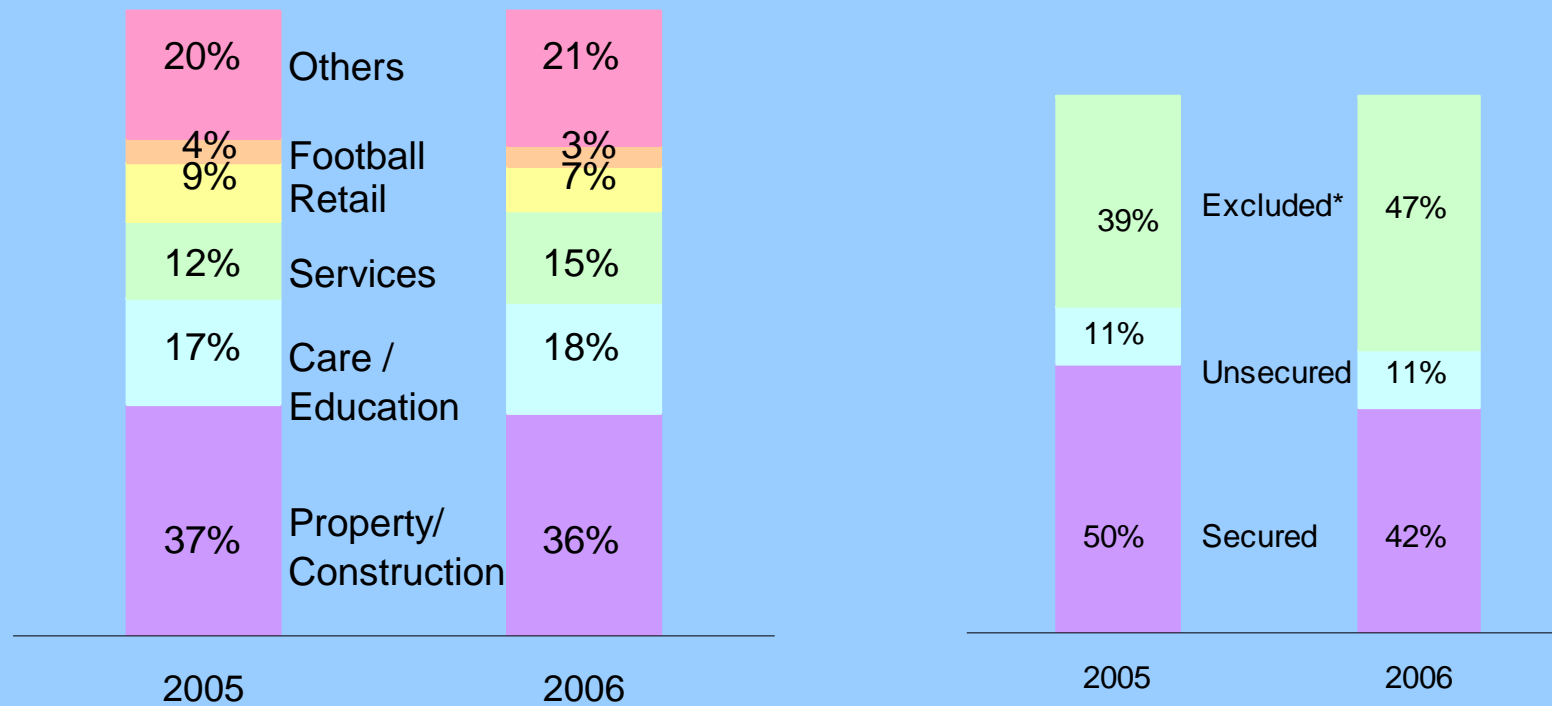
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# Corporate lending

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## 2006 £2.8bn corporate lending (2005 : £2.3bn)



\*Excluded is 80% Structured Finance Unit incl Asset Finance.

Lending includes PFI

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## Non Interest Income

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<u>£m</u>	<u>2005</u>	<u>2006</u>	<u>Change</u>
Fees and commission receivable	193.9	193.6	(0.3)
Insurance commission income	45.6	38.8	(6.8)
Fees and commission payable	(39.1)	(33.8)	5.3
Other income, including dealing	5.5	2.6	(2.9)
<b>Non-interest income</b>	<b>205.9</b>	<b>201.2</b>	<b>(4.7)</b>

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## Operating Expenses

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<u>£m</u>	<u>2005</u>	<u>2006</u>	<u>Change</u>
Staff Costs - wages & salaries	101.9	109.6	7.7
- Pensions & social security costs	29.2	23.4	(5.8)
Other staff costs	8.7	9.3	0.6
	<b>139.8</b>	<b>142.3</b>	<b>2.5</b>
Other administration expenses	164.3	173.2	8.9
Depreciation & amortisation	24.7	24.4	(0.3)
<b>Operating expenses</b>	<b>328.8</b>	<b>339.9</b>	<b>11.1</b>
<b>Staff numbers</b>	<b>4,226</b>	<b>4,163</b>	

Investment in product, regulatory and other systems

Development of customer relationship initiatives eg branch network trials

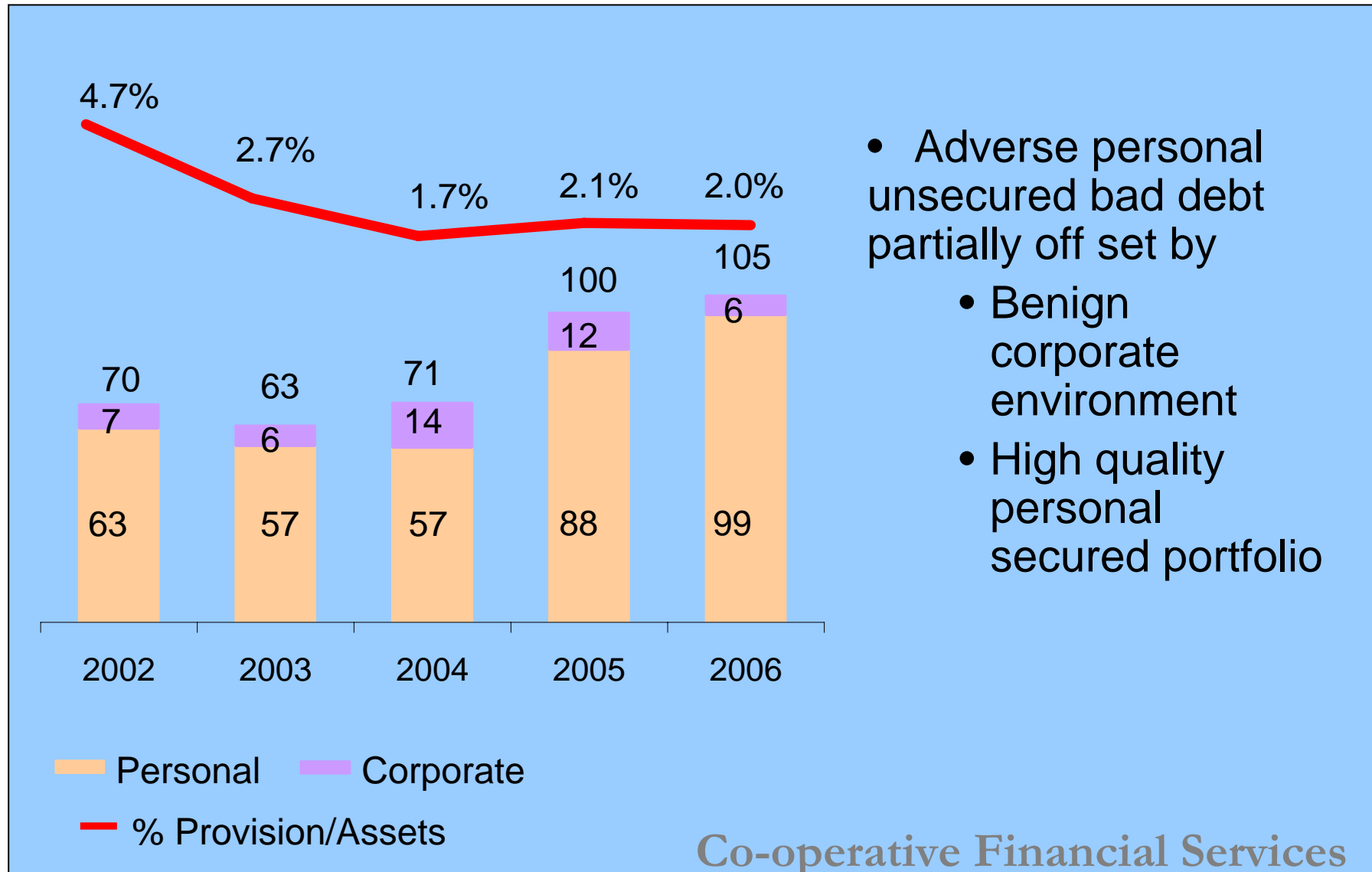
Staff costs: £7.7m increase due to inflation and harmonisation

£5.8m decrease in pensions contributions due to PACE

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# Bad Debts

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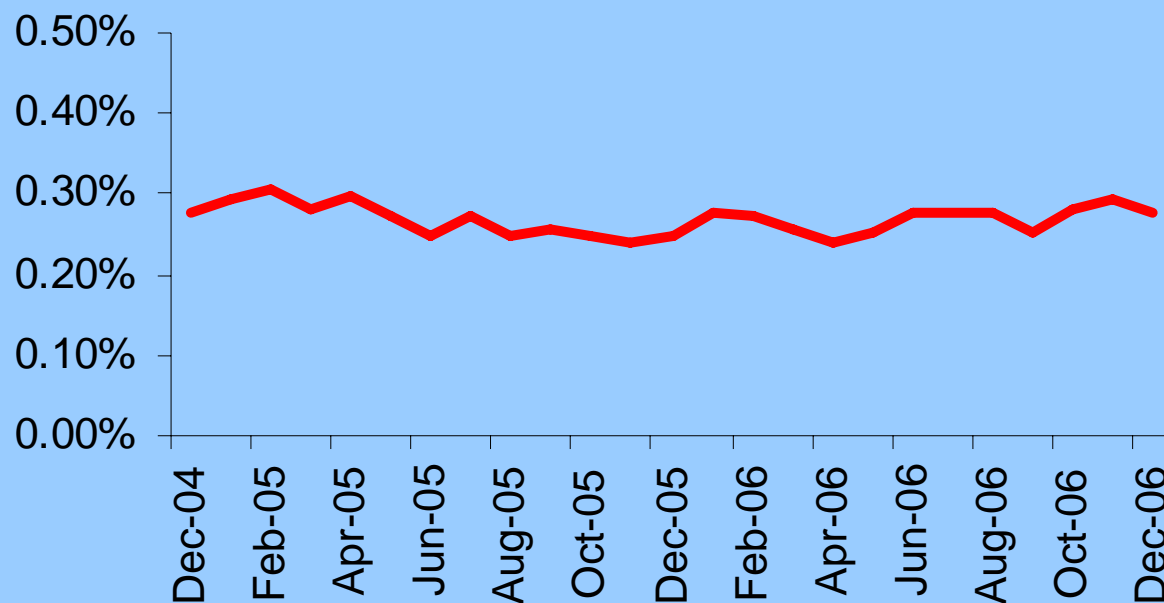


## Strong Credit Characteristics

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### Mortgages >3m Arrears (% of balance)



### Statistics

78% new to Bank

Avg Loan £66k

Book LTV\* 48%

New business  
LTV 53%

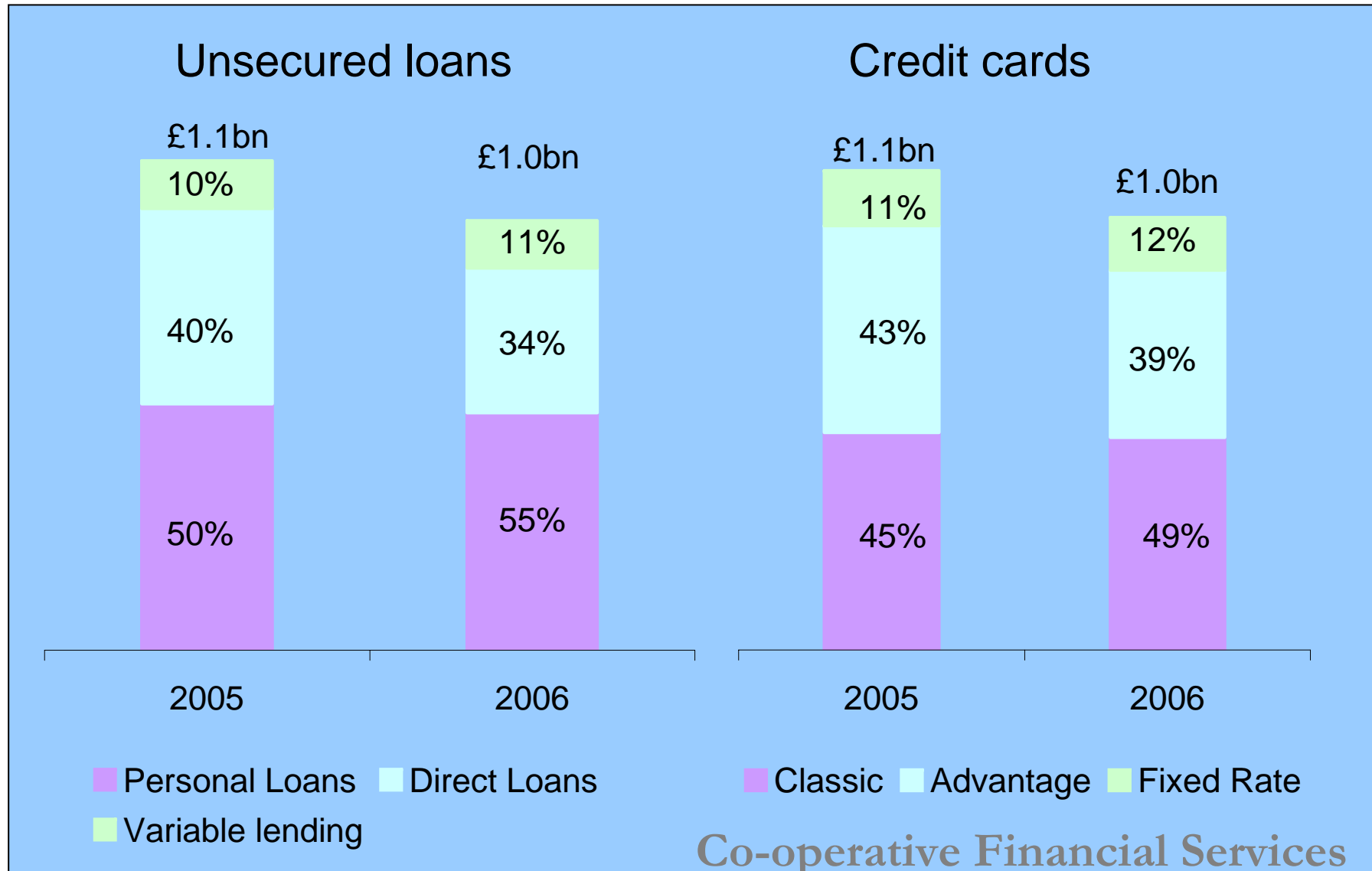
- Very low arrears levels, £8.7m >3mth arrears
- Book now seasoned, started in 2000

\* LTV at last valuation, not indexed

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# Unsecured Personal Lending

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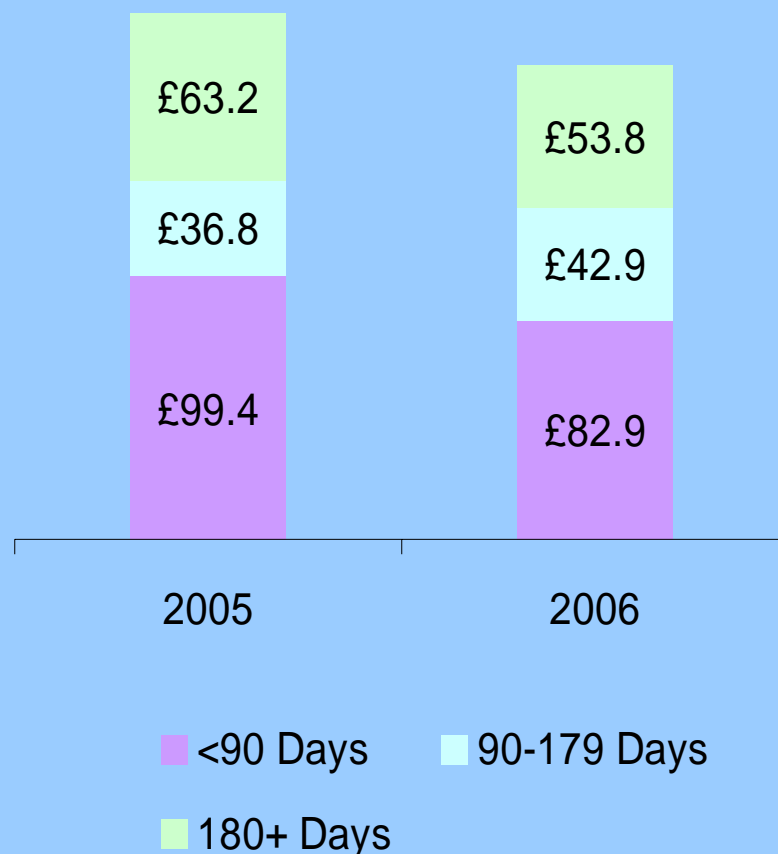


## Personal lending - arrears

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### Arrears Balance



- Bad debt charge for Personal increased from 1.6% of book balance to 1.9%, due in part to attrition

- Mortgage bad debt charge £179k

### Provisioning rates

	<u>2005</u>	<u>2006</u>
Visa	4.80%	5.50%
Other unsecured	2.99%	3.49%
Mortgages	0.01%	0.01%

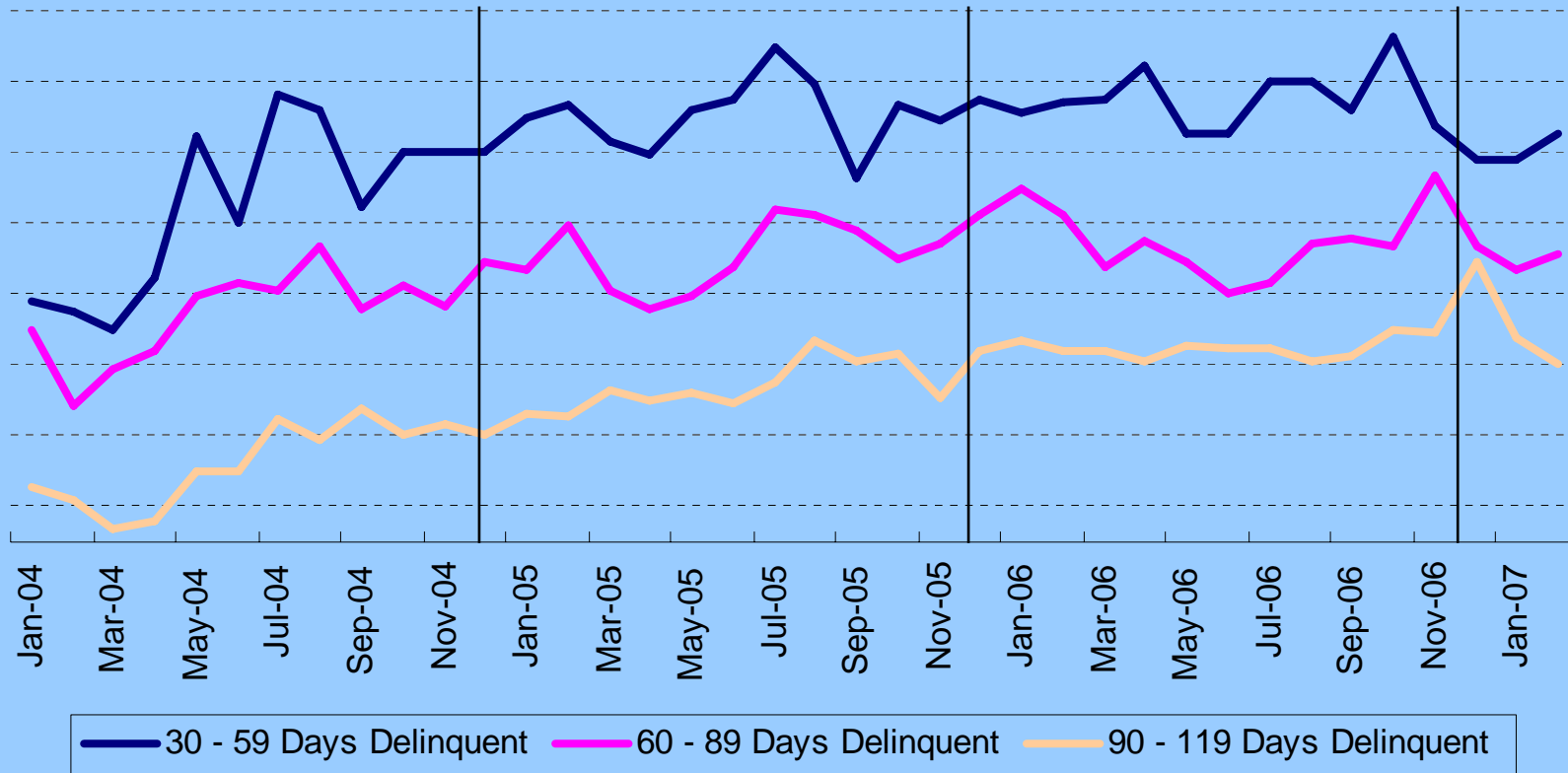
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# Personal lending - arrears

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**Retail Banking Unsecured Lending. Balances Rolling to Worse State From 30-59, 60-89 and 90 - 119 Days Delinquent.**



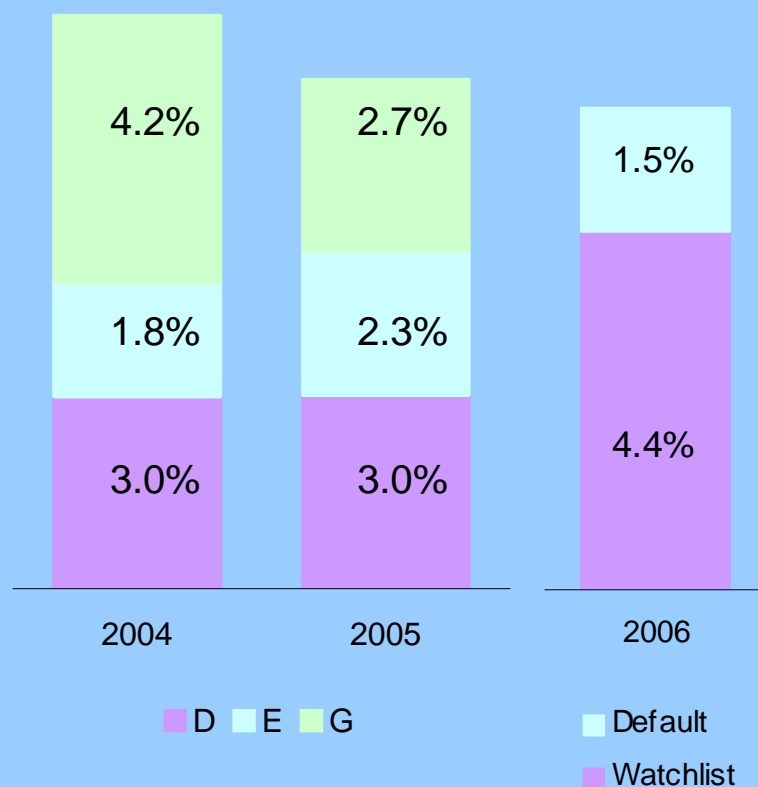
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## Corporate Credit Quality

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### Arrears % of book



- Impairment charge down by £5.5m to £6m (0.21% of debit balances)
- Rating System: Migrated to Basel 2 compliant models in 2006
  - Watchlist (Previously Grade D): Performing, close control
  - Default (Previously Grade E&G): Recovery action
- Property & Construction
  - 39% Balances; 36% Total Committed Exposure
  - 77% investment property
  - Maximum LTV 70%
- Corporate Syndications
  - 23% Balances; 18.8% Total Committed Exposure

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## Segmental Analysis

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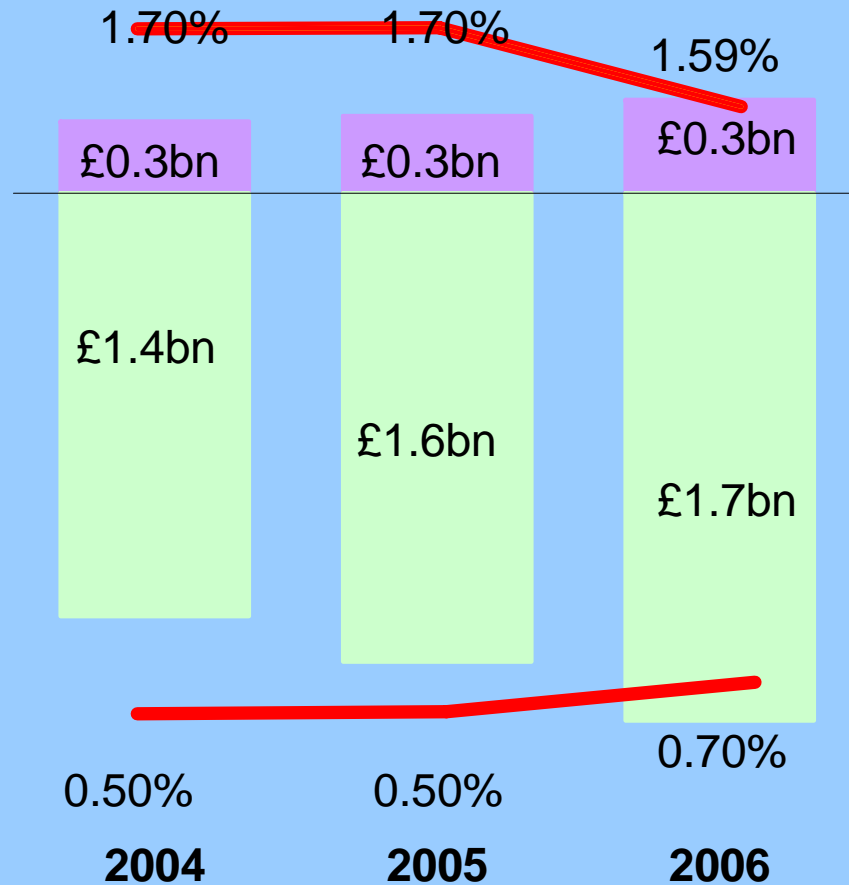


### Operating profit by segment

<u>£m</u>	<u>2005</u>	<u>2006</u>	<u>Change</u>
Retail	50.1	34.2	(15.9)
Corporate	49.3	55.1	5.8
Wholesale	14.8	3.9	(10.9)
Central Costs	(16.4)	(16.9)	(0.5)
<b>Operating profit</b>	<b>97.8</b>	<b>76.3</b>	<b>(21.5)</b>

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smile



- Smile profitable on a stand alone basis
- Continuing liability balance growth, despite widening margins
- Attracts high net worth customers

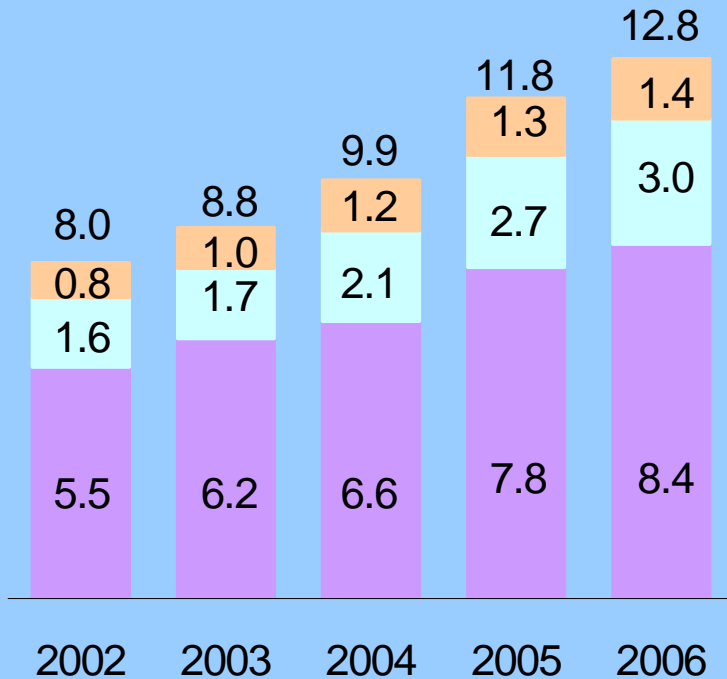
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# Funding

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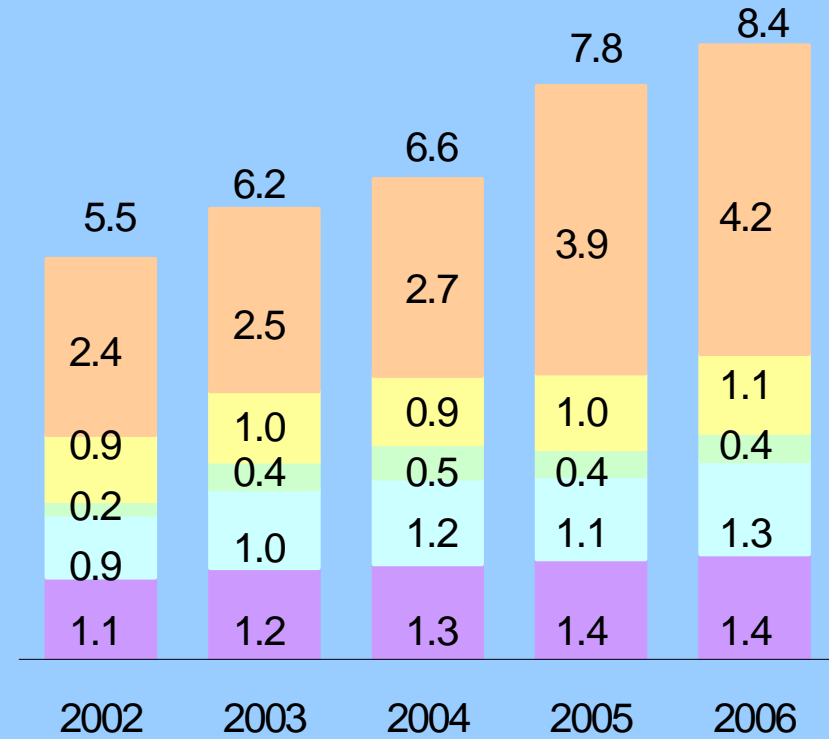


## Total Liabilities & Capital (£bn)



■ Retail 
 ■ Wholesale 
 ■ Capital & Other

## Retail Balances (£bn)



■ Non-interest bearing C/A 
 ■ Current account 
 ■ Term deposits 
 ■ ISA's 
 ■ Savings

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## Strong Capital Base

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### Capital Ratios (%)



### Strong capital ratios

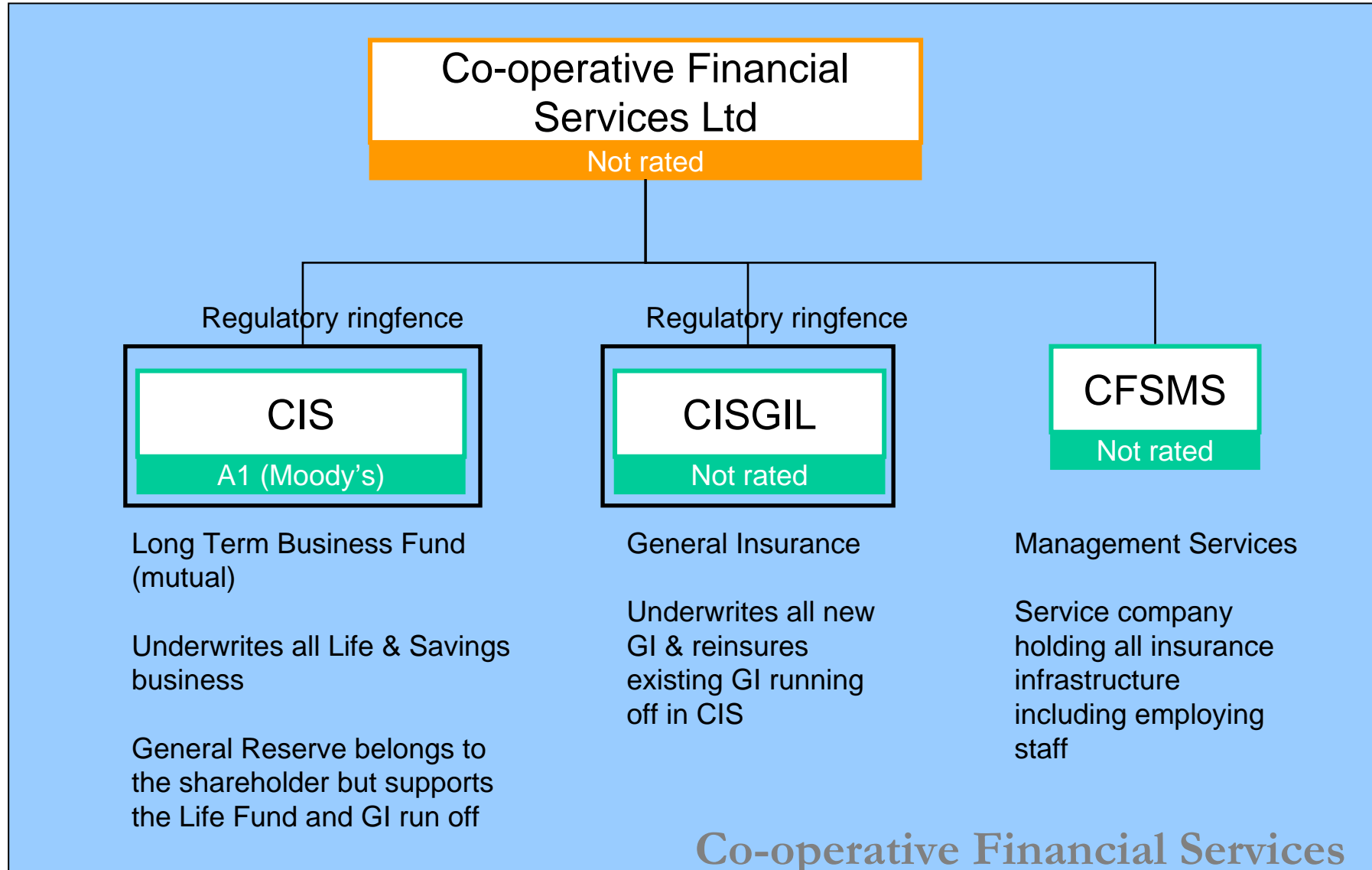
- More secured asset base
- Pensions addressed
- Low risk Treasury operation

### Relatively low gearing of capital base

Basel – PAP submitted, parallel running being undertaken whilst awaiting decisions committee

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# Co-operative Insurance



## General Insurance



<u>£m</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Gross written premiums	663.2	583.9	471.3
Earned premiums	648.9	592.1	496.0
Claims ratio	85.8%	76.2%	74.2%
Expense ratio	28.5%	28.5%	31.8%
Combined ratio	114.3%	104.7%	106.0%

- Lower earned premiums – repricing portfolio and moving to new direct channels
- New motor pricing engine – loss ratio fallen by 10.6 points
- Property high weather related claims – claim ratio 14 points worse

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## General Insurance



<u>£m</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Technical Result	(19.9)	40.6	43.2
Restructuring costs	(25.1)	(25.5)	(13.0)
Gain on implementation of PACE			4.0
Internal debt interest on capital			(4.3)
Rebates to Co-operative members	(3.0)	(3.2)	(1.9)
Operating profit before tax	(48.0)	11.9	28.0

- Reduced claims ratio - Claims transformation programme
- Launch of Eco Motor Insurance

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## CFS P&L



<u>£m</u>	<u>2005</u>	<u>2006</u>	<u>Change</u>
Banking profit	97.8	76.3	(21.5)
General Insurance technical profit	40.6	43.2	2.6
Other shareholder (excluding STIF)	24.1	28.6	4.5
Profit based discounts & rebates to members	(3.2)	(1.9)	1.3
<b>Results pre-investment fluctuations</b>	<b>159.3</b>	<b>146.2</b>	<b>(13.1)</b>
Membership dividend	(2.7)	(2.0)	0.7
Short Term Investment Fluctuations	16.6	(11.5)	(28.1)
<b>Profit before Significant Items</b>	<b>173.2</b>	<b>132.7</b>	<b>(40.5)</b>

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## Pension Scheme

### Pensions (PACE)

- Implemented new Co-operative Group Pension (Average Career Earnings) scheme on 6 April 2006
- Pension assets & liabilities transferred from CFS balance sheets, with P&L charges solely on contributions made.
- Scheme deficits of £116.8m transferred to Co-operative Group
  - Bank £109.2m
  - CISGIL £4.0m
  - Long term business £3.6m

## LTBF



Mutual, all profits retained for the benefit of policyholders

- New business met breakeven target in 2006 after cost of capital
- Maintenance expense target beaten

<u>Long Term Business Fund (£bn)</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Available assets (excluding gilt repos)	16.3	17.9	17.6
Realistic value of liabilities (excluding gilt repos)	15.6	17.1	16.4
Net surplus	0.7	0.8	1.2
Working capital ratio	4.50%	4.50%	6.40%
Risk capital margin (RCM) cover	3.1	10.6	11.2
RCM cover, incl. £200m General Reserve	3.9	13.2	13.2
Maintenance costs	£122.6m	£98.7m	£84.7m

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# Paul Hemingway

Director of Financing & Risk,  
The Co-operative Group (tCG)



## tCG Merger

## The **co-operative**

- December 2006 the Boards of the Co-operative Group and United Co-operatives announced their intention to merge
- Strategically and economically compelling case for merger via transfer of assets & liabilities. Net Trading Assets of £406m contributed to consolidated group.

	<b>tCG</b>	<b>United</b>	<b>Combined</b>
Sales	£7.3bn	£2.2bn	£9.5bn
Profit	£318m	£62m	£380m
Net Assets	£3,272m	£406m	£3,678m
Outlets	3,433	1,171	4,604
Members	1.5m	1.0m	2.5m

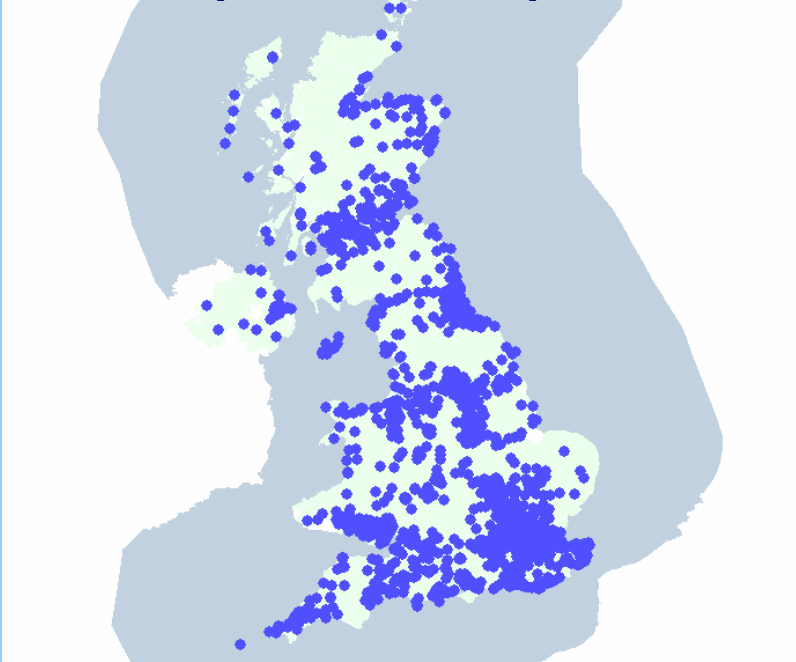
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## tCG Merger

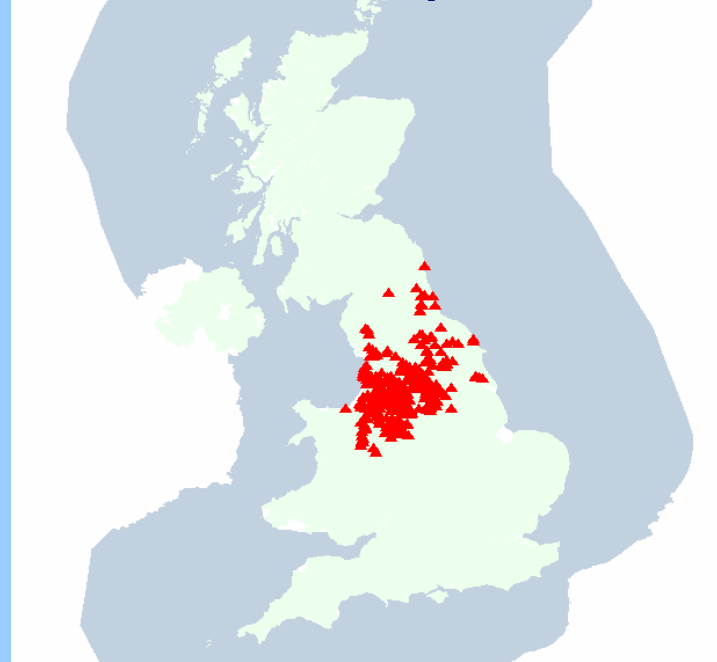
## The **co-operative**

- The Co-operative Group and United Co-op bring together geographical strengths.
- Head Offices at Manchester and Rochdale are geographically close

**Co-operative Group Food**



**United Co-op Food**



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## tCG Merger

## The **co-operative**

- Both Societies strong in core consumer facing trading businesses
- Combining businesses will provide a stronger platform to compete in their respective markets
- Both Societies have complementary specialist retail activity

<b>Outlets</b>	<b>tCG</b>	<b>United</b>	<b>Combined</b>
Food	1,700	621	2,321
Pharmacy	430	230	660
Travel	330	121	451
Funerals	626	178	804
Other businesses	347	21	368

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## tCG Merger

## The **co-operative**

- Increased levels of co-operative in recent years e.g. CRTG, CTTG. Merger is next step and will create 83% of co-operative retail trade in the UK
- Board structure of tCG post merger would become 34 members
  - 17 from Group's current regions, 9 from Group's current corporate members and 8 from United current regions
  - Commitment to reduce to no more than 25 within 18 months of merger
- Combined operating cost base significant savings will be targeted
- Net debt / EBITDAP ratio increases from 0.8 in the Group to 1.2 combined but still comfortably within group target.

### **Pension Position 2006**

	<b>tCG</b>	<b>United</b>	<b>Combined</b>
IAS 19 Surplus / (deficit)	£287.1m	£(106.7)m	£180.4m
Deferred Tax	£(86.1)m	£32.0m	£(54.1)m
Surplus / (deficit), post tax	£201.0m	£(74.7)m	£126.3m

**Co-operative Financial Services**

## tCG Merger

## The **co-operative**

- 16 – 25 April – first round United Co-operatives meetings
- 28 April – Special General Meeting of the Co-operative Group
- 14 – 22 May – second round of United Co-operatives meetings
- 18 May – the Co-operative Group Board meet to agree merger
- 23 May – Members, Colleagues and Investors told of the outcome of the United vote
- 29 July – Creation of the world's largest co-operative society

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# David Anderson

Chief Executive, CFS

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## Progress in last year

### New customer propositions

- Trials of high interest current account
- First Time Buyer Mortgage
- Eco motor insurance
- Flexible personal pension
- New branch trials
- Unit linked bond
- New GI rating engine

### Organisational design

- Single set of terms & conditions
- Integrated pension schemes
- New organisational design implemented
- Delivered CIS Modernisation programme (2004-2006) with annualised savings of over £115m at a lifetime cost of £164m

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## Progress in last year

### Awards

- Bank topped the BitC Corporate Social Responsibility Index  
CIS was best in sector, coming 10<sup>th</sup> overall
- smile 'Best Online Banking Provider' & 'Best Student Account'  
Your Money Direct Awards 2006
- Mortgages 'Best Specialist Mortgage' – Mortgage Magazine Awards  
'Best Direct Mortgage Lender' – Your Mortgage Awards
- Bank's 'Stand Up' brand campaign won 'Best TV Advert' in the first  
Green Awards
- Flagship Socially Responsible Investment (SRI) fund, the Co-  
operative Insurance Sustainable Leaders Trust, was best  
performing of 324 unit trusts in UK All Companies sector

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## What next

- **CFS Change Plan – investment in strategic & operational capability**
  - Customer facing systems & processes
  - Integrate customer management & data
  - Operational effectiveness (including cost reduction)
- **Increase Corporate Banking Centres from 11 to 22 over next 3 years**
- **Continued focus on consumer bad debt reduction**
- **Testing alternative distribution options**
- **Focus on mortgage sales through Financial Advisers**
- **Brand rollout in 2008**

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# Co-operative Financial Services

Capital Markets Presentation

23 April 2007