Nick Slape (CEO) and Louise Britnell (CFO) will host an audio conference on 28 February 2024 at 9am (UK time) to present the full year 2023 results followed by a Q&A session.

To access the call please visit https://www.co-operativebank.co.uk/about-us/investor-relations/

Additional materials are also available at this address.

BASIS OF PRESENTATION

The Co-operative Bank Holdings Limited is the immediate parent company of The Co-operative Bank Finance p.l.c. and the ultimate parent company of The Co-operative Bank p.l.c. In the following pages the term 'Group' refers to The Co-operative Bank Holdings Limited and its subsidiaries. The term 'Finance Group' refers to The Co-operative Bank Finance p.l.c. and its subsidiaries. The term 'Bank' refers to The Co-operative Bank p.l.c. and its subsidiaries which are consolidated within the Finance Group and then ultimately the Group. Unless otherwise stated, information presented for the Group equally applies to the Bank and the Finance Group.

Underlying basis: The statutory results are adjusted to remove certain items that do not promote an understanding of historical or future trends of earnings or cash flows, which therefore allows a more meaningful comparison of the Group's underlying performance.
Alternative performance measures: The Group uses a number of alternative performance measures, including underlying profit or loss, in the discussion of its business performance and financial position.

2023 Annual Report and Accounts

28 February 2024

The Co-operative Bank ('the Bank') is pleased to provide an update on its performance in the twelve months ended 31 December 2023.

- **Underlying profit of £120.9m;** NIM of 180bps increased 14bps year on year
- **Statutory profit of £71.4m;** reflects exceptional redress of £28.9m in respect of the legacy business, alongside strategic transformation and advisory costs of £22.5m
- **Strong liquidity position;** pillar 1 LCR spot position 195.4%, 12 month rolling average LCR 211.4%
- **Robust customer credit quality;** accounts greater than three months in arrears remain low
- **Resilient capital position;** supports intention to commence dividend distributions
- **Delivering the Bank's ESG agenda;** UK's best ESG rated high street bank by Morningstar Sustainalytics for the third consecutive year
- **Delivering our strategic priorities;** new mortgage platform delivered and transformation programme set to be completed in H1 2024

Nick Slape, Chief Executive Officer, said:

"2023 has been a year of transformation and I am extremely proud of what we have achieved. The underlying profit before tax of £120.9m reflects our strong, sustainable and low risk business model, while statutory profit before tax of £71.4m was impacted by exceptional redress on legacy mortgage business, strategic transformation and advisor costs.

We have made significant progress on our IT Simplification programme, including successfully in-housing our mortgage servicing capabilities, going live with our new cloud based mortgage platform and completing 67% of our savings migration. We remain on track to complete the programme in 2024.

We received a further ratings increase, upgraded three notches in twelve months from Fitch, moving us to BB+. Both Moody's and Fitch now have the Bank on a 'positive outlook'. Over time, improvements in our credit rating will enable us to further reduce our funding costs and grow our SME customer franchise.

As a result of our increased capital strength and sustainable profitability, the Board has recommended an inaugural ordinary dividend of 0.13p per share for 2023, rewarding our shareholders for their support while we have undertaken the transformation of the Bank. Our objective is to continue distributions to shareholders through a progressive and sustainable ordinary dividend policy, whilst maintaining the flexibility to undertake returns of surplus capital, when appropriate.

We remain committed to our core ethical values. In 2023, we were again rated as the UK's best ESG rated high street bank by Morningstar Sustainalytics and we issued our third green bond.

The Bank has made an excellent start to 2024. We received over 12,500 new current account applications in January, representing an increase of over 300% versus the same period last year. New mortgage origination has also been strong with £1.2bn applications in January. Looking to the future, whilst the economic outlook remains uncertain, the Bank is well positioned with a low risk balance sheet and strong capital and liquidity positions. We remain focused on delivering attractive and sustainable returns to our shareholders through growing our core mortgage and current account business, supported by diversification of our mortgage offering and evolving our SME lending proposition. We are ever

mindful of the financial challenges that the current economic climate poses for a number of customers and we will continue to support them where needed.

We announced in December 2023 that the Bank is in exclusive discussions with Coventry Building Society regarding a possible acquisition of the Bank. These discussions remain ongoing as we continue to evaluate the merits of the combination.

I would like to thank our valued customers for their continued loyalty as well as all colleagues for their tireless commitment. Without them, our achievements over the past year would not have been possible."

FINANCIAL PERFORMANCE UPDATE

INCOME STATEMENT (£m)

	Twelve months ended 31 December	
	2023	**2022**
Net interest income	**477.0**	458.3
Other operating income	**38.2**	41.1
Total income	**515.2**	499.4
Operating expenditure	**(445.5)**	(372.7)
Impairment charge	**(0.6)**	(6.4)
Non-operating income	**2.3**	12.3
Profit before tax	**71.4**	132.6
Taxation credit / (charge)	**58.3**	(110.5)
Profit after tax	**129.7**	22.1

Adjustments to profit before tax	**2023**	2022 Re-presented [1]
Exceptional redress	**28.9**	0.0
Exceptional project expenditure	**22.5**	15.6
Other exceptional (gains) / losses	**(1.9)**	(12.2)
Underlying profit before tax	**120.9**	136.0

Key ratios:		
Net interest margin (bps) [2]	**180**	166
RoTE (%) [3]	**10.1**	1.3
Cost:income ratio (%) [4]	**86.1**	72.8
Asset quality ratio (bps) [5]	**0.3**	3.1

1. Certain advisory and transformation related costs have been reclassified into exceptional project expenditure from other exceptional (gains)/losses
2. Net interest income over average interest earning assets
3. Profit after tax over average equity less intangibles
4. Total statutory expenditure over total statutory income (excludes impairment)
5. Impairment charge over average customer assets

PERFORMANCE HIGHLIGHTS

Profit before tax of £71.4m and underlying profit of £120.9m

Total income of £515.2m; including net interest income and other operating income which has increased by 3% in comparison to the twelve months ended 31 December 2022 (FY 22: £499.4m).

Net interest income increased by 4% to £477.0m (FY 22: £458.3m) and net interest margin (NIM) has risen by 14 basis points (bps) from 166bps to 180bps, with both benefitting from increases in the base rate.

Total operating expenditure including exceptional costs increased by 20% to £445.5m (FY 22: £372.7m), whereas underlying operating expenses excluding exceptional expenditure increased by 10% to £393.7m (FY 22: £357.0m). Exceptional project spend relates to strategic investment in our mortgage and savings transformation programme of £14.7m (FY 22: £15.0m), alongside advisory costs relating to the review of strategic options announced last year of £7.8m (FY 22: £0.6m). An exceptional provision has been recognised of £28.9m (FY 22: £nil) in respect of a legacy customer redress matter and more information is provided in the Annual Report and Accounts which is available on our website.

Excluding those exceptional items described above, underlying non-staff costs were held to £219.0m after absorbing inflationary pressures and an increase in continuous improvement project costs to £29.1m (FY 22: £22.1m). Staff costs rose by 21% to £145.6m due to planned insourcing

and investment in contact centres, along with inflationary pay rises. Overall, our statutory cost:income ratio increased in the year to 86.1% from 72.8% and our underlying cost:income ratio increased in the year from 71.5% to 76.4%.

Net impairment charge of £0.6m (FY 22: £6.4m); driven by updated economics outlook earlier in the year related to base rate increases and a decline in forward looking Commercial Real Estate property values offset by a £1.6m release relating to one specific legacy connection.

We have recognised a £2.3m non-operating exceptional gain (FY 22: £12.3m), predominantly relating to Visa shareholdings. 2022 includes the sale of a small loan portfolio and partial sale of our Visa shareholding.

Income tax credit of £58.3m

The income statement tax credit for FY23 of £58.3m is predominantly driven by deferred tax asset recognition of additional historical tax losses, partially offset by the tax charge on profits in the period. The tax charge in 2022 of £110.5m was affected by the pension "buy-in" resulting in a decrease in deferred tax assets, the impact of the decrease of the banking surcharge rate on deferred tax balances, and the tax charge on the profits in the period.

Strong liquidity position

Total assets reduced by 7% compared with 31 December 2022 with legacy assets reducing by 7% to £0.6bn. Retail secured balances have reduced to £19.1bn (FY 22: £19.6bn) which includes an increase of £0.3bn in respect of the acquisition of the Sainsbury's Bank mortgage portfolio. Secured balances have reduced by £0.5bn as we have actively managed new business volumes to preserve Bank margins.

Total liabilities reduced by 8% to £24.7bn over the period (FY 22: £26.8bn). SME deposit balances have remained broadly stable at £3.3bn (FY 22: £3.4bn) whilst retail deposit balances decreased by 6% to £15.7bn (FY 22: £16.6bn) driven by a reduction in retail current account balances to £5.1bn (FY 22: £5.8bn). This is driven by a decrease in customer average balances, primarily attributed to the cost of living crisis. 80.8% of our core customer deposits are insured through FSCS, and have remained stable throughout the year. The Bank maintains a very strong 12 month average LCR position of 211.4%. Total blended cost of funds has increased, due to base rate rises, to 240bps but still remains cost efficient (FY 22: 73bps). During the year we have repaid c.£1.2bn of TFSME.

Robust customer credit quality

The asset quality ratio (AQR) in total across retail, SME and legacy customer lending remains strong, reflecting the Bank's low-risk lending profile. AQR as at 31 December 2023 is 0.3bps (FY 22: 3.1bps). The average core mortgage book loan-to-value (LTV) has increased slightly this year, but remains low at 55.7% (FY 22: 53.5%). Secured accounts over three months in arrears represented only 0.21% of total accounts as at 31 December 2023 (FY 22: 0.13%).

Resilient capital position

CET1 ratio has increased from 19.8% to 20.4%, prior to the proposed dividend, and remains well above the regulatory minimum of 14.3%, including CRD IV buffers. The increase is attributed to an increase in retained earnings with risk-weighted assets (RWAs) remaining stable at £4.8bn (FY 22: £4.8bn).

Following the Bank's £200m Green MREL Senior transaction in May, plus profits in the period, total MREL-qualifying resources, prior to proposed dividend, have grown by £264.5m. We have £402.4m surplus MREL resources compared with a requirement of £1,461.4m (30.6%), including CRD IV buffers of 4.5%.

Delivering the Bank's ESG agenda

We are pleased to be rated as the UK's best Environmental, Social and Governance (ESG) rated high street bank by Morningstar Sustainalytics for the third consecutive year, with a score of 8.5 as of 9 October 2023 – the lower the score, the better the rating. We have also maintained our ratings across other ESG risk rating agencies, receiving an AAA rating from MSCI, and a Prime Rating of C with ISS. We were delighted to be recognised by consumer champion Which? as an 'Eco Provider', further reinforcing our leadership in ESG.

We increased our volunteering impact during 2023, achieving a significant uplift in colleague volunteering days from 594 to 2,335. This highlights our dedication to directly contribute to the communities we serve.

In collaboration with homeless charity, Shelter, we've actively campaigned for a fairer renting system, driving meaningful conversations and pushing for positive transformations in the private rented sector. By leveraging our influence, we're working towards bringing an end to all-too-common unfair evictions and unsafe housing, and to secure stronger rights for all renters.

Our long-term commitment to our planet and protecting the environment remains a key priority. In line with our ambitious decarbonisation plans, we have committed to aligning our Scope 1 & 2 direct emissions to net zero by 2030 and have made steps to report our Scope 3 emissions data for the first time. In addition, we continue our long-held stance to refuse banking services to any business which exploits the world's natural resources and we are embarking on a project to restore greenery and wildlife to over 1,000 nature-deprived spaces across the country alongside our partners, Friends of the Earth.

Delivering our strategic priorities

Our focus over the year has been attracting and retaining customers whose values and purpose are aligned with our ethical brand and co-operative heritage. We took key steps to diversify our mortgage lending including the launch of the new mortgage platform, allowing brokers quick and easy access to our mortgage products and developed additional capabilities paving the way for a more flexible product offering. We also identified opportunities to inorganically grow our mortgage book with the acquisition of the Sainsbury's Bank portfolio in August, comprising c.3,500 customers and c.£0.5bn of balances.

Our mortgage and savings transformation programme remains a crucial part of our strategy, focussing on technology transformation and reducing the Bank's legacy IT estates. 2023 was a landmark year in which we delivered significant progress. We've successfully insourced mortgage operations from Capita, resulting in a significant cost reduction in future years. We have also made significant progress in enabling the migration of customers from the legacy savings platform onto our enhanced Bank branded product system, supporting the delivery of a number of new savings products to the market.

We improved our customer journeys in SME by launching a new application process for community customers, who are now able to apply for a business account digitally, significantly reducing friction within the customer journey and replacing the traditional paper-based application process. Our SME digital proposition was improved as we redesigned and rebuilt our public website to help customers find the information they need when researching our Business Current Accounts and also completed a proof of concept on tracking customer journeys end-to-end, enabling us to understand which marketing channels work best for customers and the Bank.

As we enter the second phase of our strategy, 'Embed & Expand', we will continue to build on the significant progress made over the last 12 months. The Bank has refreshed its strategic focus for 2024, built around our three growth pillars; current accounts and deposits, mortgages and SME lending. These growth pillars will be underpinned by two growth enablers; operating model transformation and ESG and ethical banking propositions.

You can read more on how we are delivering on our strategic priorities in our 2023 Annual Report and Accounts which is made available on our website.

Outlook

Our financial outlook for 2024 is as follows:

- Net interest margin of approximately 185bps; reflecting a prudent approach to interest rate risk management through an effective structural hedging strategy, offset by mortgage margin and deposit mix/margin pressures.
- Total statutory costs of approximately £410m; inflationary pressures, offset by efficiencies.
- Asset quality ratio of less than 5bps; arrears remain low and stable across all portfolios.
- Customer assets of £20-21bn; stable balance sheet remaining conscious of Bank margins.
- Return on tangible equity of approximately 10%; sustainable profitability maintains double digit returns on shareholder investment.

SEGMENTAL PROFIT / (LOSS) (£m)

Twelve months ended 31 December 2023	Core			Legacy &	Group
	Retail	SME	Total	unallocated	
Net interest income	377.3	97.7	**475.0**	2.0	**477.0**
Other operating income	21.8	15.8	**37.6**	0.6	**38.2**
Operating income	**399.1**	**113.5**	**512.6**	**2.6**	**515.2**
Operating expenses	(320.3)	(67.7)	**(388.0)**	(57.5)	**(445.5)**
Net credit impairment (losses)/gains	(0.7)	(1.3)	**(2.0)**	1.4	**(0.6)**
Non-operating income	-	-	**-**	2.3	**2.3**
Profit before tax	**78.1**	**44.5**	**122.6**	**(51.2)**	**71.4**

Twelve months ended 31 December 2022	Core			Legacy &	Group
	Retail	SME	Total	unallocated	
Net interest income	397.0	69.3	**466.3**	(8.0)	**458.3**
Other operating income	22.7	18.7	**41.4**	(0.3)	**41.1**
Operating income/(expense)	**419.7**	**88.0**	**507.7**	**(8.3)**	**499.4**
Operating expenses	(288.6)	(63.6)	**(352.2)**	(20.5)	**(372.7)**
Net credit impairment (losses)/gains	(5.2)	(1.6)	**(6.8)**	0.4	**(6.4)**
Non-operating income	-	-	**-**	12.3	**12.3**
Profit before tax	**125.9**	**22.8**	**148.7**	**(16.1)**	**132.6**

SME performance has improved during the year with profit before tax increasing to £44.5m (FY 22: £22.8m) whereas retail profit has reduced to £78.1m (FY 22: £125.9m). The significant increase in SME income is due to a high proportion of the SME balance sheet consisting of deposits which have benefited from the rising rate environment. The SME segment remains a key strategic focus for its growth potential.

Retail operating expenditure increased from £288.6m to £320.3m. This is predominantly driven by the insourcing of Capita colleagues and recruitment in the second half of 2022. SME operating expenditure is fairly stable at £67.7m (FY 22: £63.6m). Legacy & unallocated operating expenditure has increased from £20.5m to £57.5m due to increased strategic project spend and exceptional legacy redress that have not been allocated to any segment.

SEGMENTAL BALANCE SHEET (£m)

31 December 2023	Core			Legacy &	Group
	Retail	SME	Total	unallocated	
Segment assets	19,302.9	378.4	19,681.3	6,390.0	26,071.3
Segment liabilities	15,690.4	3,320.7	19,011.1	5,651.2	24,662.3

31 December 2022	Core			Legacy &	Group
	Retail	SME	Total	unallocated	
Segment assets	19,841.3	388.2	20,229.5	7,903.3	28,132.8
Segment liabilities	16,607.8	3,396.8	20,004.6	6,829.2	26,833.8

SELECTED KEY PERFORMANCE INDICATORS

% (unless otherwise stated)	2023	2022	Change
CET1 ratio [1]	**20.4**	19.8	0.6
Total capital ratio [1]	**25.3**	23.8	1.5
Risk-weighted assets (£m)	**4,781**	4,816	(35)
Leverage ratio (PRA) [2]	**4.1**	4.0	0.1
Liquidity coverage ratio (spot)	**195.4**	242.9	(47.5)
Liquidity coverage ratio (12 month rolling average) [3]	**211.4**	265.3	(53.9)
Loan to deposit ratio	**106.4**	104.1	2.3
Average core mortgage LTV	**55.7**	53.5	2.2
Volume of core mortgage accounts > 3 months in arrears	**0.21**	0.13	0.08
NPL as a % of total exposures	**0.5**	0.4	0.1

1. Prior to proposed dividend
2. Calculated as per PRA definition, excluding Bank of England reserves
3. Calculated in line with Pillar 3 requirements

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The person responsible for arranging the release of this announcement on behalf of The Co-operative Bank Holdings Limited and The Co-operative Bank p.l.c. is Catherine Green, Company Secretary.

About The Co-operative Bank
The Co-operative Bank p.l.c. provides a range of banking products and services to about 2.5m retail customers and c.94k small and medium sized enterprises ('SME'). The Bank is committed to values and ethics in line with the principles of the co-operative movement. The Co-operative Bank is the only high street bank with a customer-led ethical policy, which gives customers a say in how their money is used. Launched in 1992, the policy has been updated on six occasions, with new commitments added in June 2022 to cover what we do for our planet, people and the community.

The Co-operative Bank p.l.c. is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. The Co-operative Bank p.l.c. eligible customers are protected by the Financial Services Compensation Scheme in the UK, in accordance with its terms.

Note: This announcement contains inside information.
The Co-operative Bank p.l.c. LEI: 213800TLZ6PCLYPSR448
The Co-operative Bank Finance p.l.c. LEI: 213800KNE8ER4N9BLF11
The Co-operative Bank Holdings Limited LEI: 213800MY2BSP459O8A22

PRIMARY FINANCIAL STATEMENTS

CONSOLIDATED INCOME STATEMENT

£million

	Year ended 31 December	
	2023	**2022**
Interest income calculated using the effective interest rate method	**883.8**	581.2
Other interest and similar income	**263.4**	88.7
Interest income and similar income	**1,147.2**	669.9
Interest expense and similar charges	**(670.2)**	(211.6)
Net interest income	**477.0**	458.3
Fee and commission income	**67.4**	64.4
Fee and commission expense	**(31.0)**	(32.6)
Net fee and commission income	**36.4**	31.8
Other operating income (net)	**4.1**	21.6
Operating income	**517.5**	511.7
Operating expenses	**(445.5)**	(372.7)
Operating profit before net credit impairment losses	**72.0**	139.0
Net credit impairment losses	**(0.6)**	(6.4)
Profit before tax	**71.4**	132.6
Income tax	**58.3**	(110.5)
Profit for the financial year	**129.7**	22.1

The results above are for the consolidated Group and Bank and wholly relate to continuing activities. More information regarding the basis of preparation can be found in the Annual Report and Accounts, which have been made available on our website.

The profit for the financial year is wholly attributable to equity shareholders.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

£million

	Year ended 31 December	
	2023	**2022**
Profit for the year	**129.7**	22.1
Items that may be recycled to profit or loss:		
Changes in cash flow hedges:		
Transfers from equity to income or expense	**(7.2)**	(6.9)
Income tax	**2.0**	2.8
Changes in fair value through other comprehensive income:		
Net changes in fair value recognised directly in equity	**(30.2)**	121.6
Transfers from equity to income or expense	**27.5**	(131.3)
Income tax	**-**	1.5
Items that may not subsequently be recycled to profit or loss:		
Changes in net retirement benefit asset:		
Defined benefit plans losses for the year	**(16.4)**	(693.8)
Income tax	**4.6**	231.1
Other comprehensive expense for the year, net of income tax	**(19.7)**	(475.0)
Total comprehensive income/(expense) for the year	**110.0**	(452.9)

The results above are for the consolidated Group and Bank. More information regarding the basis of preparation can be found in the Annual Report and Accounts, which have been made available on our website.

CONSOLIDATED BALANCE SHEET

£million

	31 December 2023	31 December 2022
Assets		
Cash and balances at central banks	**2,708.3**	5,270.4
Loans and advances to banks	**212.6**	387.1
Loans and advances to customers	**20,149.4**	20,491.2
Investment securities	**2,088.3**	942.7
Derivative financial instruments	**309.1**	520.1
Other assets	**47.9**	46.6
Property, plant and equipment	**23.6**	22.8
Intangible assets	**114.0**	90.0
Right-of-use assets	**31.4**	33.0
Current tax assets	**4.3**	1.8
Deferred tax assets	**233.9**	167.4
Net retirement benefit asset	**148.5**	159.7
Total assets	**26,071.3**	28,132.8
Liabilities		
Deposits by banks	**4,288.9**	5,683.4
Customer accounts	**19,215.1**	20,072.7
Debt securities in issue	**-**	181.9
Derivative financial instruments	**110.3**	103.5
Other liabilities	**37.4**	42.8
Accruals and deferred income	**22.8**	32.5
Provisions	**60.6**	33.2
Other borrowed funds	**891.2**	646.9
Lease liabilities	**30.1**	31.0
Net retirement benefit liability	**5.9**	5.9
Total liabilities	**24,662.3**	26,833.8
Capital and reserves attributable to the Group's equity holders		
Ordinary share capital	**0.9**	0.9
Share premium account	**313.8**	313.8
Retained earnings	**2,097.8**	1,968.1
Other reserves	**(1,003.5)**	(983.8)
Total equity	**1,409.0**	1,299.0
Total liabilities and equity	**26,071.3**	28,132.8

The financial positions above are for the consolidated Group and Bank. More information regarding the basis of preparation can be found in the Annual Report and Accounts, which have been made available on our website.

CONSOLIDATED STATEMENT OF CASH FLOWS

£million

	Year ended 31 December	
	2023	**2022**
Cash flows from/(used in) operating activities:		
Profit before tax	**71.4**	132.6
Adjustments for non cash movements:		
Pension scheme adjustments	**(3.4)**	(12.7)
Net credit impairment losses	**0.6**	6.4
Depreciation, amortisation and impairment	**34.8**	35.3
Other non-cash movements	**90.3**	143.8
Changes in operating assets and liabilities:		
(Decrease)/increase in deposits by banks	**(1,394.5)**	155.8
Increase in prepayments	**(2.7)**	(1.1)
Decrease in accruals and deferred income	**(9.7)**	(4.5)
Decrease in customer accounts	**(874.0)**	(1,028.8)
Decrease in debt securities in issue	**(181.9)**	(21.4)
Decrease/(increase) in loans and advances to banks	**30.3**	(28.5)
Decrease in loans and advances to customers	**590.4**	32.5
Net movement of other assets and other liabilities	**(52.7)**	(28.6)
Income tax paid	**(2.7)**	(6.8)
Net cash flows used in operating activities	**(1,703.8)**	(626.0)
Cash flows from/(used in) investing activities:		
Purchase and construction of tangible and intangible assets	**(55.0)**	(48.0)
Purchase of investment securities	**(1,542.7)**	(465.7)
Proceeds from sale of property and equipment	**-**	0.4
Proceeds from sale of shares and other interests	**0.2**	20.4
Proceeds from sale and maturity of investment securities	**434.9**	679.0
Purchase of equity shares	**-**	(0.8)
Proceeds from sale of investment properties	**0.3**	-
Dividends received	**0.1**	0.2
Net cash flows (used in)/from investing activities	**(1,162.2)**	185.5
Cash flows from/(used in) financing activities:		
Proceeds from issuance of Tier 2 notes and senior unsecured debt	**397.9**	248.4
Redemption of Tier 2 notes	**(163.5)**	-
Interest paid on Tier 2 notes and senior unsecured debt	**(62.7)**	(44.5)
Lease liability principal payments	**(6.6)**	(14.6)
Net cash flows from financing activities	**165.1**	189.3
Effect of exchange rate changes on cash and cash equivalents	**(5.4)**	(8.2)
Net decrease in cash and cash equivalents	**(2,706.3)**	(259.4)
Cash and cash equivalents at the beginning of the year	**5,458.1**	5,717.5
Cash and cash equivalents at the end of the year	**2,751.8**	5,458.1
Comprising of:		
Cash and balances with central banks	**2,631.7**	5,183.8
Loans and advances to banks	**120.1**	274.3
	2,751.8	5,458.1

RECONCILIATION OF MOVEMENTS OF LIABILITIES TO CASHFLOWS ARISING FROM FINANCING ACTIVITIES

£million

	2023			2022		
	Lease liabilities	Other borrowed funds	Total	Lease liabilities	Other borrowed funds	Total
Balance at the beginning of the year	31.0	646.9	**677.9**	44.1	402.1	446.2
Changes from financing cashflows						
Proceeds from issuance of Tier 2 notes and senior unsecured debt	-	397.9	**397.9**	-	248.4	248.4
Redemption of Tier 2 notes	-	(163.5)	**(163.5)**	-	-	-
Interest paid on Tier 2 notes and senior unsecured debt	-	(62.7)	**(62.7)**	-	(44.5)	(44.5)
Lease liability principal payments	(6.6)	-	**(6.6)**	(14.6)	-	(14.6)
Total changes from financing cash flows	24.4	818.6	**843.0**	29.5	606.0	635.5
Other changes						
Interest payable on lease liabilities and Tier 2 notes	1.0	63.2	**64.2**	1.2	48.1	49.3
Other non cash movement	-	9.4	**9.4**	-	(7.2)	(7.2)
Remeasurements of lease liabilities	4.7	-	**4.7**	0.3	-	0.3
Balance at the end of the year	30.1	891.2	**921.3**	31.0	646.9	677.9

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

£million

2023	Share capital	Share premium	FVOCI reserve	Cash flow hedging reserve	Capital re-organisation reserve	Defined benefit pension reserve	Retained earnings	Total equity
At 1 January 2023	0.9	313.8	(5.3)	10.6	(1,011.4)	22.3	1,968.1	**1,299.0**
Total comprehensive (expense)/income for the year	-	-	(2.7)	(5.2)	-	(11.8)	129.7	**110.0**
At 31 December 2023	**0.9**	**313.8**	**(8.0)**	**5.4**	**(1,011.4)**	**10.5**	**2,097.8**	**1,409.0**

2022	Share capital	Share premium	FVOCI reserve	Cash flow hedging reserve	Capital re-organisation reserve	Defined benefit pension reserve	Retained earnings	Total equity
At 1 January 2022	0.9	313.8	2.9	14.7	(1,011.4)	485.0	1,946.0	1,751.9
Total comprehensive (expense)/income for the year	-	-	(8.2)	(4.1)	-	(462.7)	22.1	(452.9)
At 31 December 2022	0.9	313.8	(5.3)	10.6	(1,011.4)	22.3	1,968.1	1,299.0

SELECTED NOTES TO THE FINANCIAL STATEMENTS

All amounts are stated in £m unless otherwise indicated.

NOTE 1: SEGMENTAL INFORMATION

The Group provides a wide range of banking services within the UK. The Executive Committee (ExCo) has been determined to be the chief operating decision-maker of the Group. The Group's operating segments reflect its organisational and management structures in place at the reporting date. ExCo reviews information from internal reporting based on these segments in order to assess performance and allocate resources. The segments are differentiated by whether the customers are individuals or business entities. The operating costs of all business functions are allocated to the income-generating businesses. Treasury balances have not been allocated to segments to maintain clarity on underlying customer product balances.

2023	**Core**			**Legacy &**	**Group**
	Retail	**SME**	**Total**	**unallocated**	
Net interest income	377.3	97.7	475.0	2.0	477.0
Other operating income	21.8	15.8	37.6	0.6	38.2
Operating income	**399.1**	**113.5**	**512.6**	**2.6**	**515.2**
Operating expenses	(320.3)	(67.7)	(388.0)	(57.5)	(445.5)
Net credit impairment (losses)/gains	(0.7)	(1.3)	(2.0)	1.4	(0.6)
Non-operating income	-	-	-	2.3	2.3
Profit before tax	**78.1**	**44.5**	**122.6**	**(51.2)**	**71.4**

2022	**Core**			**Legacy &**	**Group**
	Retail	**SME**	**Total**	**unallocated**	
Net interest income	397.0	69.3	466.3	(8.0)	458.3
Other operating income	22.7	18.7	41.4	(0.3)	41.1
Operating income/(expense)	419.7	88.0	507.7	(8.3)	499.4
Operating expenses	(288.6)	(63.6)	(352.2)	(20.5)	(372.7)
Net credit impairment (losses)/gains	(5.2)	(1.6)	(6.8)	0.4	(6.4)
Non-operating income	-	-	-	12.3	12.3
Profit before tax	125.9	22.8	148.7	(16.1)	132.6

The table below represents the reconciliation of the underlying basis and the segmental note to the consolidated income statement. The underlying basis is the basis on which information is presented to the chief operating decision maker and excludes the items below which are included in the statutory results.

		Removal of:			
2023	**IFRS statutory**	**Volatile items[1]**	**Strategic projects**	**Non recurring[2]**	**Underlying basis**
Net interest income	477.0	-	-	-	**477.0**
Other operating income	40.5	(2.3)	-	-	**38.2**
Operating income	**517.5**	**(2.3)**	**-**	**-**	**515.2**
Operating expenses	(445.5)	-	12.2	39.6	**(393.7)**
Net credit impairment losses	(0.6)	-	-	-	**(0.6)**
Profit before tax	**71.4**	**(2.3)**	**12.2**	**39.6**	**120.9**
Cost:income ratio[3]	**86%**				**76%**

1. In the period ended 31 December 2023, this mainly comprises gain on shares revaluation.
2. In the period ended 31 December 2023, this comprises customer redress costs and other exceptional costs.
3. Cost:income ratio is calculated as (operating expenses plus net customer redress release)/(operating income).

2022	IFRS statutory	Removal of: Volatile items[1]	Strategic projects	Non recurring[2]	Underlying basis
Net interest income	458.3	-	-	-	458.3
Other operating income	53.4	(8.2)	-	(4.1)	41.1
Operating income	511.7	(8.2)	-	(4.1)	499.4
Operating expenses	(372.7)	-	12.4	3.3	(357.0)
Net credit impairment losses	(6.4)	-	-	-	(6.4)
Profit before tax	132.6	(8.2)	12.4	(0.8)	136.0
Cost:income ratio[3]	73%				71%

1. In the period ended 31 December 2022, this comprises gain on shares revaluation.
2. In the period ended 31 December 2022, this comprises gains on the sale of a small legacy loan book, release of PPI provision and other exceptional costs.
3. Cost:income ratio is calculated as (operating expenses plus net customer redress release)/(operating income).

The table below represents the segmental analysis of assets and liabilities.

2023	Core			Legacy & unallocated	Group
	Retail	SME	Total		
Segment assets	19,302.9	378.4	19,681.3	6,390.0	26,071.3
Segment liabilities	15,690.4	3,320.7	19,011.1	5,651.2	24,662.3

2022	Core			Legacy & unallocated	Group
	Retail	SME	Total		
Segment assets	19,841.3	388.2	20,229.5	7,903.3	28,132.8
Segment liabilities	16,607.8	3,396.8	20,004.6	6,829.2	26,833.8

NOTE 2: RELATED PARTY TRANSACTIONS

Parent, subsidiary and ultimate controlling party

As at 31 December 2023, the Group had one significant shareholder, SP Coop Investments Ltd, holding over 20% of the B shares of the Holding Company, and therefore a related party.

In 2023 and the comparative year, SP Coop Investments Ltd did not have any holdings in the Tier 2 and senior unsecured debt issued by The Co-operative Bank Holding Ltd/The Co-operative Bank Finance p.l.c. and hence did not receive any interest payments in this respect.

A loan is recognised by Holding Company and Bank Company to achieve structural subordination of the MREL-qualifying debt (the "internal MREL"). The terms of the internal MREL are the same as those of the external MREL-qualifying debt. The total amount due from Bank Company to Holding Company at 31 December 2023 in this regard was £891.2m (2022: £646.9m to Finance Company) including accrued interest. The interest paid by Bank Company to Holding Company/Finance Company on the internal MREL instrument was £62.7m (2022: £44.5m). Other intercompany funding arrangements with Bank Company comprise £46.4m (2022: £nil) owed by Finance Company and £46.4m (2022: £nil) owed to Holding Company.

Transactions with other related parties

Key management personnel are defined as the Board of Directors and Executive Committee members. The related party transactions with key management are disclosed below:

	2023	2022
Deposits and investments at the beginning of the year	**2.5**	1.6
Net movement	**(2.0)**	0.9
Deposits and investments at the end of the year	**0.5**	2.5

In addition, there were £0.4m (2022: £0.4m) relating to loans to key management personnel, arising in the normal course of business.

Key management personnel

	2023	2022
Total remuneration receivable by key management personnel	**8.7**	9.3

In 2023, the total number of key management personnel was 20 (2022: 19). Further information about the remuneration of senior management personnel and Material Risk Takers is included in the Directors' Report on remuneration.

NOTE 3: EVENTS AFTER THE BALANCE SHEET DATE

There are no post balance sheet events to report.

RISK MANAGEMENT

1. RISK MANAGEMENT OBJECTIVES AND POLICIES

1.1 Our approach to risk management

Responsibility for risk management resides at all levels within the Group and is supported by both Board and management level committees. A three lines of defence ("3LOD") model is deployed on the following basis:

- First line – responsible for owning and managing all risks within defined appetites, complying with risk policies and control standards, ensuring supporting procedures are documented and maintained using the risk and control self-assessment ("RCSA"), and are responsible for reporting the performance, losses, near-misses and status of risks through governance.
- Second line - the risk function acts as the second line of defence ("2LOD"). The risk framework owners ("RFOs") are responsible for setting risk policies, control standards, Group-wide procedures and risk appetite. RFOs sit within the second line with the exception of some specialist areas where the RFO sits within first line (for example legal, financial reporting and people risk); the second line risk function will provide oversight over the RFO activities in such cases.
- Third line - the internal audit function assesses the adequacy and effectiveness of the control environment and independently challenges the overall management of the risk management framework ("RMF").

1.2 Chief Risk Officer Update

I am pleased to report that in 2023 the Group has made improvements across a range of key risks. Of particular note is the work done to reduce the Group's technology risk thanks to the ongoing progress made on our transformation journey, particularly with regards to the Simplification programme. Further, the work done to effectively control the Group's credit risk profile and support the Bank's customers who are in financial difficulties amidst a turbulent external operating environment has been essential throughout the year.

Significant risks

We continue to have end-of-life IT systems which require remediation, known as technical debt. These systems pose a risk to operations and service reliability for customers. To mitigate this, we have made significant progress throughout 2023 with our flagship mortgage and savings Simplification programme, which includes the delivery of a new mortgage origination platform. Work will continue to mitigate the potential risk of service interruption for our customers, and the financial risk of losses arising from technical debt.

The ongoing cost of living crisis has resulted in financial loss for banks across the industry. The Monetary Policy Committee's decision on 1 February 2024 to maintain current base rate level continues to put pressure on customers with respect to their credit obligations, something we remain highly vigilant of. As a result of this, we have worked throughout the year to identify what the right type of forbearance treatments are in limiting customers falling into arrears. We are well positioned to continue supporting customers in this way and will continue to monitor customer segments for potential signs of financial difficulty.

Further to losses, financial organisations have also experienced cost pressures as a result of the record levels of inflation seen throughout 2023. With our ongoing business transformation programmes underway, higher operational costs incurred have had an adverse impact on our overall profitability. We understand the importance of tight cost control, and seek wherever possible to operate in the most efficient way possible. Through 2024, we will remain vigilant of these cost pressures and look to limit overall impact to profitability they cause.

In November 2023, the Group received two final decisions from the Financial Ombudsman Service ("FOS") which in part upheld complaints related to historical increases in the Standard Variable Rate applied to a closed book of mortgage customers between 2011 and 2012. In order to limit potential further harm, the Group's Board concluded that proactive steps should be taken to compensate eligible customers with similar characteristics regardless of whether they had complained.

Key 2023 achievements and looking ahead

We have achieved some significant milestones through 2023. In the year, we successfully completed the acquisition of the Sainsbury's Bank mortgage portfolio, adding to our strong existing mortgage business. We have obtained permission to risk weight these mortgages using our existing internal ratings based ("IRB") model as part of this transaction.

We were also able to refinance our existing Tier 2 capital issuance, with a large order book reflecting the market's view of performance. This supports future profitability and ensures that we maintain a strong capital position to preserve resilience and enable future growth.

We have delivered the requirements of Consumer Duty by the regulatory implementation date of 31 July 2023. This included prioritisation of high priority open book products which were then subject to a full assessment against the Consumer Duty requirements. An assessment of price and fair value was undertaken against all remaining open book products along with in-depth reviews of key customer journeys. Critical repairs of customer communications were completed. Our governance framework and management information capabilities have been enhanced to continually evidence good customer outcomes. To support the implementation, we have delivered mandatory e-learning to all colleagues, regular Q&A sessions and face to face training to support embedding of the Consumer Duty for all colleagues.

This year, we rebranded our mortgage origination services from 'Platform' to 'The Co-operative Bank for Intermediaries', a move partnered with the launch of our new mortgage platform. This is another step forward in our Simplification programme, aiming to simplify our product brands and systems, ultimately making our operations leaner and more dynamic when change is needed. Having a unified platform for mortgage origination reduces operational risks associated with managing multiple origination platforms.

We have worked effectively with regulatory bodies over the year to deliver new retail secured IRB exposure at default ("EAD"), loss given default ("LGD") and hybrid probably of default ("PD") models in line with the requirements set out in policy statement PS11/20. We have now submitted our EAD, LGD and PD models and await Prudential Regulation Authority ("PRA") approval whilst holding post model adjustments in respect of the anticipated impact of the model change.

1.3 Governance Overview

The Board oversees and approves the RMF and is supported by the Risk Committee ("RC"). The RC's purpose is to review principal risk categories and risk appetite, report conclusions to the Board for approval and oversee the implementation of the RMF, whilst anticipating changes in business conditions. The purpose of the RC is to review and challenge risk appetite and the RMF.

There is a formal structure for identifying, reporting, monitoring and managing risks. This comprises, at its highest level, risk appetite statements and appetite metrics which are set and approved by the Board and are supported by granular risk appetite measures across each of the principal risk categories within the RMF. This is underpinned by an RMF which sets out the high level policy, control standards, roles, responsibilities, governance and oversight for the management of all principal risks as part of the RMF.

Material risks and issues, whether realised or emerging, inclusive of those documented in relation to the RMF itself are described along the lines of principal risks within section 1.8.

1.4 Our Risk Management Framework (RMF)

Further information can be found in the full Annual Report and Accounts, which has been made available on our website.

1.5 Risk management strategy and appetite

The Board has primary responsibility for identifying the key business risks faced and approving the risk management strategy through the setting of risk appetite, which defines the type and amount of risk the Group is prepared to take both qualitatively and quantitatively in pursuit of our strategic objectives. In addition, the Board approves key regulatory submissions including the Internal Liquidity Adequacy Assessment Process ("ILAAP") and the Internal Capital Adequacy Assessment Process ("ICAAP").

Risk appetite is translated into specific key risk appetite metrics ("KRAMs") which are tracked, monitored and reported to the appropriate risk committees (refer to section 1.7). Our refreshed risk appetite framework has been embedded through 2023, with KRAMs and key risk indicators ("KRIs") being reported into the appropriate governance committees highlighting where we are outside appetite and the achievement of the strategy is at risk.

1.6 Our risk culture

A critical supporting factor of the RMF is risk culture; this is a shared set of values and behaviours that defines how all colleagues approach the management of risk. This culture begins at the top of the organisation with the Board and the executive team who lead by example with consistent and clear communication of their commitment to managing risk at all levels of the business. Risk management is included in every colleague's objectives each year and is embedded within the Group scorecard against which performance is measured.

We have committed to embedding a strong culture of risk management and provide mandatory annual training and additional opportunities for colleagues to refresh knowledge on the RMF. In addition, there are opportunities for leaders to share knowledge and experience in respect of risk management in their roles. Culture is measured through continued monitoring of the risk section of the scorecard, the RMF dashboard, which includes metrics on risk process adherence through RMF-focussed second line of defence assurance reviews, and through second line of defence oversight and feedback.

1.7 Our risk governance

The Board is the key governance body and is responsible for strategy, performance and ensuring appropriate and effective risk management. It has delegated the responsibility for the day-to-day running of the business to the Chief Executive Officer ("CEO"). The CEO has established the Executive Committee to assist in the management of the business and deliver the approved strategy and Plan in an effective and controlled manner. The Board has established Board committees and senior management committees to oversee the RMF, including identifying the key risks faced and assessing the effectiveness of any risk management actions.

Committee	Risk focus
Board Chair: Bob Dench	The Board has collective responsibility for the long-term success of the business. Its role is to provide leadership within a framework of prudent and effective controls which enable risk to be assessed and managed. It sets the values and standards and ensures the obligations to its shareholders, customers and other stakeholders are understood and met. The Board sets strategy and approves plans presented by management for the achievement of strategic objectives it has set. It determines the nature and extent of the significant risks it is willing to take in achieving strategic objectives and is responsible for ensuring maintenance of sound risk management and internal control systems.
Risk Committee (RC) Chair: Raj Singh	RC is responsible for reviewing and reporting its conclusions to the Board on the Bank's risk appetite and propose for approval by the Board and oversee the implementation of an RMF, taking a forward-looking perspective and anticipating changes in business conditions.
Executive Risk Oversight Committee (EROC)	EROC is responsible for oversight of the risk profile of the Group (within the agreed Board risk appetite). EROC reviews and challenges the risks associated with business strategy, plans and overall management of risks. EROC achieves some of its objectives through delegating responsibility to sub-committees: OCROC, MROC, PROC and CROC. EROC

Chair: CRO	will escalate, where appropriate, to the Board via the RC.
Executive Committee (ExCo) Chair: CEO	ExCo is responsible for defining and implementing the Board-approved strategy successfully by monitoring and managing delivery against plan and applying appropriate risk management actions to emerging risks.
Asset and Liability Committee (ALCo) Chair: CFO	ALCo is primarily responsible for overseeing the management of capital, market, earnings, liquidity and funding risks. Its responsibilities include identifying, managing and controlling the balance sheet risks in executing its chosen business strategy, ensuring the capital and liquidity position is managed in line with appropriate policies and that adequate capital is maintained at all times. In order to align the function of key committees more closely, ALCo started to report directly to the Risk Committee. This change will further reinforce the mitigation of financial risks through embedding a structure whereby key asset and liability management decisions are set within a risk governance setting.
Model Risk Oversight Committee (MROC) Chair: Director of Capital, Impairment and Model Development	MROC ensures, on an ongoing basis, that the model rating systems and material models are operating effectively. This includes providing executive level review and challenge of the model risk and the impact of model risks on business model and strategy. MROC also provides oversight of IRB permissions, including the exemptions where the standardised approach to calculate Pillar 1 capital requirements is applied.
Credit Risk Oversight Committee (CROC) Chair: Director of Credit Risk	CROC is responsible for monitoring significant credit risks and issues within the entire credit lifecycle, the controls and management actions being taken to mitigate them and to hold to account the executives responsible for actions. CROC reviews the credit risk strategy on an ongoing basis, making recommendations to EROC as appropriate.
Operational, Compliance & Financial Crime Risk Oversight Committee (OCROC) Chair: Director of Compliance, Director of Operational Risk	OCROC is responsible for monitoring significant operational risks and issues including significant conduct, regulatory, product, reputational, fraud and anti-money laundering ("AML") risks and issues, the controls and management actions being taken to mitigate them and to hold to account the executives responsible for actions. OCROC oversees the current and emerging operational risk profile, ensuring key risk exposures are managed within risk appetite and reported to EROC as appropriate, including the monitoring of adherence to the RMF alongside a process for continuous improvement.
Pension Risk Oversight Committee (PROC) Chair: Director of Capital, Impairment and Model Development	PROC is responsible for oversight of all aspects of pension arrangements which the Group either sponsors or participates in, to ensure cost, risk, capital, investment and employee requirements are met.

1.8 Principal risk categories

Sections 1.8.1 – 1.8.6 provide an overview of the key themes, risk mitigation activity, and future focus of each of our principal risks categories as laid out within our RMF. Where applicable we will make reference to our thematic risks of climate risk and operational resilience.

1.8.1 CREDIT RISK

Definition:

Credit risk is the risk to profits and capital that arises from a customer's failure to meet their legal and contractual payment obligations. Credit risk applies to retail, small and medium-sized enterprises ("SME") and treasury.

Retail secured and unsecured credit risk

Key themes:

Managing lending profiles to new and existing customers is key to the ongoing management of exposure to credit risk. This involves the continual optimisation of our strategies across all portfolios, using both internal and external customer performance data, as well as ensuring the appropriate oversight of their performance.

Strategy continues to focus on growth in new mortgage business volumes, principally through mortgage intermediaries. Nevertheless, we recognise that we remain reliant on interest income from our mortgage portfolio and are therefore still committed to seeking opportunities to diversify our income streams and yield whilst remaining cognisant of the credit implications of this approach. The progress of Simplification with regards to mortgage re-platforming in 2023 further facilities our ability to leverage diversification opportunities in future.

Key risks across 2023 and into 2024 relate to the cost of living crisis impacts on our customer base due to the impact of macroeconomic factors including inflation and interest rates. With unemployment also likely to increase in 2024, the culmination of these factors could lead to an increased number of customers facing financial difficulty or falling into arrears.

Mitigation:

Credit risk is managed within an agreed set of risk appetite measures for each portfolio, which are monitored through a clearly defined RMF. All credit exposure mandates are approved within a clearly defined credit approval authority framework.

To support customers facing financial difficulty, we operate a pre-arrears contact strategy to unsecured and secured customers. 95% loan-to-value ("LTV") lending has been managed through higher score cut-offs and restricting flats/maisonettes as acceptable collateral. A significant proportion of 95% LTV applications are also reviewed by the underwriting team.

Whilst the mortgage portfolio is low risk and underpinned by robust credit strategies, the cost of living crisis is impacting everyone across the UK. We have undertaken an updated affordability assessment of our residential secured portfolio to understand the impact of rising cost of living alongside rate increases for customers, in particular the impact on disposable household income for customers holding products maturating in 2024 and 2025. This has enabled us to identify those customers most at risk of falling into a negative disposable income position and therefore needing support. Positively, the average level of disposable income for the current portfolio is £1,463 per month and 92% of these customers have a monthly disposable income estimated to be more than £250, based on their current mortgage rate. Applying a rate shock to customers with products maturing in the next 2 years, average disposable income reduces to £1,300 per month. Customers considered "at risk" based on their refreshed net disposable income (less than minus £100) have been profiled compared to those not at risk. Additionally, this analysis is used to inform our expected credit loss ("ECL") judgements and has incorporated customers who may be showing potential signs of stress into our stage 2 population thereby appropriately capturing the expected financial impact of the affordability shock.

As at year end, the weighted average LTV on the Sainsbury's Bank portfolio is 51.6% (vs. 55.7% for Bank). The proportion of Sainsbury's balances with an LTV of 60% or less stood at 69.9% (vs. 55.5% for Bank). The proportion of interest only balances is also comparable, standing at 10.5% for Sainsbury's Bank (vs. 9.1% for Bank). There are 16 cases in arrears on the Sainsbury's Bank mortgage book.

The monitoring of the unsecured portfolio is a key risk focus, especially given prevailing macroeconomic conditions. In response to this, we created an unsecured cost of living task force at the start of 2023 to review key components of customer management, arrears strategies and processes to ensure they remain fit for purpose. In addition to this, a suite of new unsecured stress early warning indicators ("EWIs") were developed in order to more closely monitor potential changes to asset quality. Furthermore, our annual affordability calculator refresh has incorporated rising costs into the affordability calculation for new secured and unsecured credit applications.

In relation to climate change risk, the secured portfolio is slightly less exposed to both river/sea and surface flood risk when compared to the UK property market as a whole. In addition, the risk to the secured portfolio from subsidence is also slightly lower than the UK as a whole.

Future focus:
The housing market has slowed in 2023, however there are signs house prices will fall as we go into 2024 and this will be closely monitored. Further, there is a risk that base rate will remain high for longer than forecast, prolonging interest rate strain on customers resulting in them being unable to meet their credit obligations. To date, secured and unsecured assets remain high quality, with the secured portfolio being resilient to higher interest rates as noted above.

SME credit risk

Key themes:
SME customers continue to grapple with persistently high (although falling) inflation rates, elevated interest rates and the need to increase wages. Throughout 2023 a key risk relates to visible tightening on affordability assessments which has been driven by the impacts of COVID-19 and now subsequently the macroeconomic environment. Due to the current climate, there is an increased risk of rising numbers of those entering into financial difficulty and subsequently recoveries.

Throughout 2023 the focus has been on establishing growth within the SME portfolio for new and existing customers, with new money applications coming primarily through broker introductions into the relationship management team.

Mitigation:
Credit risk is managed within an agreed set of risk indicator and appetite measures for each portfolio, monitored through a clearly defined, well embedded RMF, with enhanced and effective controls. All credit delegated lending authorities are approved within a clearly defined credit approval authority framework.

Throughout 2023, we focussed on affordability assessments throughout the loan lifecycle, conducting robust sensitivity analysis at origination to account for high costs and interest rates, and implement customer strategies for those facing financial difficulty. We have enhanced the use of EWIs and pre-arrears strategies to identify and contact 'at risk' customers, making adjustments identified as vulnerable to support the best outcomes.

For SMEs facing financial challenges, we provide tailored forbearance and collections solutions where appropriate, as they navigate the management of their businesses. Our approach to proactive engagement, particularly for recipients of Bounce-Back Loan ("BBLs") scheme and Coronavirus Business Interruption Loan Scheme ("CBILS") facilities has minimised the need for recovery actions. This remains a closely monitored area, given the rising insolvency rates in the UK and potential for stagnant growth, leading to ongoing uncertainty around the longer term viability of SMEs.

Through corporate lending, we consider climate risk qualitatively within our relationship managed portfolio. Climate risk analysis is carried out on a case by case basis at the point of acquisition and upon annual review. Additionally, ethical business screening is undertaken upon origination, and we do not lend to businesses involved in fossil fuels or activity which contradicts our Ethical Policy.

We have identified substantial growth opportunities in the SME portfolio within selected sectors. In 2023, our primary focus has been enhancing the RMF and processes to bolster efficiency and support this future growth strategy. Simultaneously, we maintain vigilant oversight of the existing portfolio aiding customers in rebuilding their businesses post pandemic and addressing challenges associated with the cost of living.

Future focus:
Looking ahead to 2024, our focus will be on closely monitoring SMEs unable to pass on rising costs to their customers and the expanding cohort of government loan scheme customers that have exhausted Pay as You Grow solutions. Early interventions persist to allow flexibility for viable businesses. The resourcing levels of the business support teams are continuously under review to ensure our capacity to meet the escalating challenges in the upcoming year.

Key indicators:
Impairment losses: £0.6m (2022: £6.4m)
Core mortgage accounts >3 months in arrears (by balance): 0.18% (2022: 0.09%)

1.8.2 OPERATIONAL RISK

Definition:
Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or external events.

Operational resilience
Key themes:
Operational resilience is a thematic risk within the RMF and is defined as the risk of the Group suffering operational disruptions arising from the inability to prevent, adapt, respond to, recover and learn from previous events.

Operational resilience events are expected to occur, however our appetite is to have plans in place that mitigate and/or minimise disruptions, ensuring reduced harm to customers, maintaining the safety and soundness of the business and limiting impacts to the wider financial sector. We have no appetite for any breach of regulation in relation to operational resilience and will, at all times, seek to achieve and maintain compliance with all relevant legal and regulatory requirements.

Mitigation:
We have completed a programme of work to identify our important business services (“IBS”), set impact tolerance thresholds for the maximum tolerable levels of disruption to each IBS, map the IBS, complete scenario testing and identify operational resilience vulnerabilities. In 2023 we have made improvements in IBS mapping, enabling easier identification of vulnerabilities requiring remediation. Our approach to scenario testing has also matured in 2023, with testing now considering severe but plausible scenarios which could impact multiple pillars of resilience and multiple IBS at once.

Future focus:
Between now and 31 March 2025 we will focus on remediation of vulnerabilities and continue to manage operational resilience as business-as-usual (“BAU”) through completing the aforementioned activity annually. In 2024 it is expected that identified vulnerabilities are remediated and that operational resilience processes are further developed in line with recently updated industry guidance.

We will continue to monitor the effectiveness of operational resilience risk management through RMF activity, dedicated operational resilience reporting in governance, dedicated assurance reviews completed as part of the three lines of defence risk management model and a multi-year scenario testing plan.

Change risk
Key themes:
2023 has seen the continuation of enhanced governance and oversight of business change, namely the Simplification programme to re-platform our mortgages and savings. Failure to deliver these key change projects in a safe and timely manner limit the agility with which we can adapt our products and pricing, alongside requiring us to hold heightened capital requirements as a result of technical debt.

Mitigation:
The 2023 transformation portfolio has delivered a set of initiatives in support of the overall strategy, with a focus on risk remediation, improved customer experience and regulatory compliance.

Through the Simplification programme, we have now seen the successful delivery of our new, in-house mortgage system providing origination and variation capabilities, alongside the insourcing of servicing teams from Capita. This implementation is a step change in our mortgage offering to customers as we can now directly service our own customers and have control over mortgage products, pricing with flexibility and tailoring our offerings to current and potential customers.

As part of the same programme of work, the majority of our savings customers have now been migrated away from legacy IT systems to newly developed Group-owned systems. This initiative has led to the introduction of multiple new savings products since the beginning of the year.

Contributing to the successful delivery of the programme was the significant time and effort invested in oversight and assurance across all three lines of defence. This included executive and Board sub-committee focus applied to the programme, with clear accountability for ownership and delivery. Throughout the year we have continually improved our business change methodology, and the operating financial control framework is demonstrating its effectiveness through a dedicated committee.

Finally, the progress made in the Simplification programme has allowed us to take significant steps to reduce our dependency and exposure to legacy IT systems. This work will continue into 2024, aligning with objectives to meet our risk appetite targets related to technical debt levels (for more information, refer to technical debt below).

Future focus:
In 2024, robust programme monitoring and oversight of key developments will continue across all three lines of defence. Frequent updates on the Group's transformation progress will continue to be provided to the regulators. The completion of Simplification, the mortgage and savings re-platforming and transformation programme, will lead to a significant reduction to the Group's operational risk profile and technical debt exposure. Robust programme monitoring and oversight of key developments has been and will continue to be in place through 2024.

Technical debt

Key themes:
As with many other financial institutions, we are grappling with end-of-life IT systems that provide key services. To reduce the associated risks and minimise the impact of any disruptions, we have devised a strategy to eliminate the highest risk legacy systems and have implemented additional resilience arrangements to safeguard IT services until replacement.

Mitigation:
Various programmes and projects, most notably the Simplification programme will further reduce the level of technical debt. Ongoing investment and monitoring for 2024 is in place to continuously modernise our environment and minimise future technical debt as technologies continue to age.

Future focus:
We anticipate that a significant volume of technical debt will be decommissioned by the end of 2024 through application and server remediation. This will result in a reduction of the associated residual risk to an acceptable level.

Financial crime

Key themes:
We have a zero tolerance for money laundering, terrorism financing or the circumvention of financial sanctions, and will not knowingly do business with or facilitate the activities, individuals or entities that we believe to be engaged in financial crime. We consciously act to reduce the risk that we are exposed to uncontrolled levels of financial crime causing unplanned fraud losses, reduced customer confidence or reputational damage.

Fraud losses continue to be a significant contributing factor to operational losses in 2023 with case volumes for both account takeover ("ATO") and authorised push payments ("APP") increasing.

Mitigation:
Our risk appetite framework sets out a list of high risk activities and customer types with which we will not enter into a relationship with, and action will be taken to terminate any existing relationships, which fall into a prohibited category.

Our financial crime risk policies and standards set out the minimum requirements for mitigating money laundering and fraud risks. We conduct regular financial crime risk assessments to ensure that adequate identification, assessment, mitigation, management and monitoring of all financial crime risks is undertaken across all business activities.

We have delivered various change projects throughout 2023 to enhance our financial crime framework; these included strengthening our AML and sanctions controls, payment-filtering screening and additional fraud controls to ensure we continue protecting customers from fraud throughout 2024.

Future focus:
We continue to invest in improvements to our financial crime systems and controls and this will continue through 2024, with improved monitoring and integration of behavioural biometrics that will improve detection against both APP and ATO fraud. Further to this, we are currently undergoing a proof of concept to implement machine-learning capabilities to augment our existing money laundering transactional monitoring solution.

Finally, our dedicated regulatory risk team monitors industry developments via a fully embedded horizon scanning process, and attends industry-led working groups to ensure a consistent approach to regulatory change is fully understood and aligned to our peers.

Cybercrime

Key themes:
Over the last year, the cyber security threat to the UK has evolved significantly. The National Cyber Security Centre has identified the UK as the third most targeted country for cyberattacks, behind Ukraine and the United States. This has resulted in an increase in the number of firms falling victim to cyber-attacks, with ransomware continuing as a popular attack vector for cyber criminals – causing significant operational, financial and data impacts for targeted organisations. In addition, geo-political cyber threats have emerged as a more significant threat than our previous cyber strategies have considered, and this landscape is evolving at pace following the Russian invasion of Ukraine and concerns around China.

Mitigation:
The Board-approved 2022 cyber security strategy has delivered an intelligence-led approach to managing cyber risk that is aligned to industry standards and independent assessment. Through this, we have been awarded ISO27001 accreditation, one of the industry's most recognised information security standards.

Our 2023 cyber security programme has ensured that we respond effectively to the evolving threat landscape, support the adoption of new technologies. Through the programme, we have significantly developed our cyber maturity, capability and resilience, using industry-recognised frameworks and independent assessment to validate control enhancements and strategic investments.

Additionally, progress in our Simplification programme continues to provide material reductions in our technical debt, in turn reducing our exposures to cyber risks as a result of legacy IT systems.

Future focus:
With the embedding of the new Chief Information Officer, we will refresh our cyber strategy in 2024 to build on its successes of protecting customers and operations from the ever-evolving cyber threats. The strategy will be informed by external key threats and intelligence, and focus on necessary improvements, identified by internal and independent external assessments, to ensure we keep pace with industry peers.

<u>Third party supplier risk</u>
Key themes:
We continue to be dependent on suppliers to support or provide key banking services.

Mitigation:
Following the engagement of an external third party, support has been provided in assessing supplier risk management, alignment of our framework to industry best practise and providing guidance on how to deliver further improvements. As a result, a new operating model and associated controls have been implemented with enhancements in place for the risk management of all suppliers. Risk policies and controls standards as part of the RMF have been updated to reflect the new requirements, and any identified gaps will be managed through established monitoring and reporting.

2023 has seen the successful integration of Capita colleagues who now provide mortgage servicing operations in-house. This change ensures that resourcing levels are appropriate to support our customers.

Future focus:
Our focus for 2024 will be on our strategic IT suppliers and reviewing existing contracts and service provision. This will utilise enhancements made to the procurement lifecycle and upskilling of internal capabilities to achieve better outcomes through our commercial partnerships.

<u>Compliance risk</u>
Key themes:
We aim for continuous compliance with all relevant regulatory requirements, promptly remedying any unintentional breaches. Recognising the substantial execution risks associated with regulatory changes, we acknowledge the significant resource demand across the business.

Mitigation:
This year, we demonstrated regulatory compliance with the Financial Conduct Authority's ("FCA") Consumer Duty for open products and services by the implementation date of 31 July 2023. We are on track to implement the duty for closed products and services by 31 July 2024. We assessed policies, procedures and processes of our key customer journeys and have taken steps where necessary to ensure they are in line with the new duty, embedding changes into business-as-usual activities for consistent good customer outcomes.

Future focus:
We are dedicated to regulatory compliance, prioritising the delivery of significant regulatory changes in 2024 and beyond to enhance customer protection and outcomes, and strong financial resilience.

Key changes from the PRA, FCA, His Majesty's Treasury and the Bank of England include:

- regulatory reform – with the 'Edinburgh Reforms' and the Financial Services and Markets Bill, this potentially represents significant change across the regulated financial services industry. We will engage in consultations and discussions with regulators.
- PRA implementation of the Basel 3.1 standards – we are on track to deliver these substantial reforms which will provide a consistent approach and are aligned to international and EU standards. We are engaged on this topic and are working through the capital requirements and implications.
- Payment Systems Regulator – new reimbursement requirements for victims of APP fraud (including Faster Payments and CHAPS). This will provide consistency for consumers as the industry moves from a voluntary code to mandatory regulations. It will increase consumer protection for authorised transactions which consumers currently receive for unauthorised transactions today.

<u>Conduct and reputational risk</u>
Key themes:
We are committed to delivering good customer outcomes and to avoiding causing material customer harm. We support our customers to make effective, timely and properly informed decisions, acting in good faith, avoiding foreseeable harm and supporting customers to pursue their financial objectives. If harm arises we will take appropriate remedial action where necessary.

As an ethical bank, we welcome higher expectations for customer outcomes set through Consumer Duty. We view Consumer Duty as an opportunity to strengthen and sharpen our conduct frameworks to evidence that we deliver good outcomes for our customers.

Mitigation:
We have continued to react and support our customers' need for forbearance in light of increased cost of living. We proactively signed up and implemented the FCA's Mortgage Charter, and we provide our customers with an appropriate level of care and support through reviewing policies, procedures, lending criteria and oversight through our cost of living working groups. This ensures our customers receive appropriate tailored forbearance that is in their interests and takes account of their individual circumstances. We continue to offer support through an emergency hardship fund in severe circumstances.

We have supported vulnerable customers by becoming one of the founding members of the Experian Support Hub. This is an online platform that allows our customers to share their support needs once to multiple organisations. Further, we have partnered with InterpretersLive! to offer customers access to sign language facilities to communicate with us so we can adequately support those who wish to communicate using British Sign Language.

We continue to invest in digital channels to ensure we treat all customers fairly and allow all customers to access Bank services through their preferred channel. An example of our investment was the award we received by the expert independent organisation Digital Accessibility Centre - AA Web Content Accessibility Guidelines ("WCAG") accreditation. This is an internationally recognised standard for web accessibility. This will support our vulnerable customers and provide information in ways that they can understand and use it. We also recognise the diverse needs of our customers and have maintained commitment to our other channels through our investment into new branches.

We also keep informing and educating our customers to the ever-changing tactics of fraudsters and continue to support the industry-recognised 'Take Five' national campaign.

During a period of increased interest rates, we have adopted a pricing policy where all our savings customers have benefitted from rate rises and ensuring fairness for all customers with a similar product holding. We have actively participated in the FCA Cash Savings Market Review and are in line with industry commitments, and will implement enhancements to our approach to ensure products meet the fair price and value outcome.

In November 2023, the Group received two final decisions from the FOS that partially upheld complaints brought by customers regarding historical changes to the Standard Variable Rate ("SVR") within a closed book of mortgages acquired by the Group as part of its merger with the Britannia Building Society in 2009. In light of these decisions, the Group's Board approved proposals from management to take proactive steps concerning other closed-book SVR mortgage customers, regardless of whether or not they had complained. It was concluded that eligible closed-book SVR customers impacted by the decisions will be partially refunded interest charged historically in line with the Bank's obligations under the FCA's complaint handling rules.

Future focus:
As we achieved the key 31 July 2023 milestone for Consumer Duty (Open Book), investing time in embedding knowledge and processes across the business will ultimately ensure that we remain regulatory compliant. We need to utilise data and management information to ensure we make fully informed decisions to ensure our customers receive good outcomes.

The Cash Savings Market review is the first indication of a change in approach by the regulator following the implementation of Consumer Duty. The review focusses on consumer understanding and price and fair value outcomes.

There is a requirement for banks to act and engage differently, using data and management information to identify customers and communicate with customers in low and lower paying savings accounts and non-interest bearing accounts. This is a more targeted approach by the regulator for banks to take action and act differently to address potential harm where customers are at risk by their inaction.

Key indicators:
Net operational losses: £18.1m (2022: £16.8m)

1.8.3 CAPITAL RISK

Definition:
The risk that regulatory capital resources are inadequate to cover regulatory capital requirements.

Key themes:
Risk-weighted assets ("RWAs") at 31 December 2023 total £4.8bn. RWAs reflect risk adjusted assets factoring in PD, LGD and EAD. This calculation is used to derive the Group's capital requirement. Increases in RWAs are driven either by increases in underlying assets or increases in the risk weighting (or density) assigned to these assets. Significant changes in RWAs are typically driven by changes in modelling requirements, for banks that have permission to use the IRB approach. We, alongside other IRB institutions, have faced challenges with respect to the development of our secured IRB models to ensure compliance with PS11/20.

From 1 January 2022, we raised a post model adjustment ("PMA") to reflect the expected impact of PS11/20 on our secured RWAs and expected losses ("EL"), whilst model development remained ongoing. This PMA was revised in December 2022 to reflect progress in the development of

compliant models, and has been continuously monitored throughout the year. In 2023, the Group submitted our new secured IRB EAD, LGD, and hybrid PD models to the PRA, with full implementation expected in 2024.

Our capital position is influenced by changes in the wider UK and global economy, with capital risks arising from changes in unemployment, interest rates, inflation, house prices, economic growth and other variables. 2023 has been a year of macroeconomic uncertainty, with the Bank of England continuing to take monetary policy action to return to its mandated inflation target 2% (+/- 1%). Higher interest rates and quantitative tightening have increased funding costs and therefore placed downward pressure on net interest margin, profitability and capital. This action is expected to put pressure on consumer and business affordability, which also drives additional credit risk, with a concurrent impact on RWAs, EL and expected credit loss provisions under IFRS 9. These impacts are being closely monitored across all of our credit portfolios.

Mitigation:
Effective capital risk management is a key priority of the Board and executive team. We closely monitor current and future capital positions across all regulatory frameworks (total capital ratio ("TCR"), MREL and leverage ratio), including capital buffers. Capital management is a key activity across all three lines of defence, with oversight of the strategy and resulting capital impacts being a key priority, alongside regulatory activities. We engage closely with our regulators to ensure they are well informed of actual and expected changes in capital position.

We are well-positioned for the risk of a material deterioration in the macroeconomic environment, with capital available to absorb losses and increases in capital requirements based on the results of our annual stress testing exercise. Capital resources continue to grow organically through ongoing profitability, and we have evidenced our ability to complete capital transactions in recent years, including the issuance of senior Minimum Requirements for Eligible Liabilities ("MREL") qualifying notes in May 2023, and refinancing of our 2019 Tier 2 subordinated notes issuance in November 2023.

Future focus:
In November 2022, the PRA published Consultation Paper 16/22 ("CP16/22"): Implementation of the Basel 3.1 Standards, outlining the PRA's proposed rules and expectations. On 27 September 2023, the PRA announced that it intends to delay implementation of the final Basel 3.1 policies by six months, to 1 July 2025. Basel 3.1 represents the most significant change to the regulatory capital framework since Basel 3 implementation, and a significant amount of activity is required to meet the proposed requirements. On 12 December 2023, the PRA published Policy Statement 17/23 ("PS17/23"), outlining part 1 of its near-final Basel 3.1 standards.

The key changes proposed in CP16/22 and PS17/23 include:

- the transitional implementation of a standardised RWA output floor;
- changes to the standardised approaches to credit risk and operational risk; and
- amendments to IRB approaches, credit risk mitigation ("CRM"), credit valuation adjustment ("CVA") risk, as well as further requirements for disclosures and reporting.

We have completed a full interpretation of the proposed changes outlined in CP16/22, alongside an initial impact assessment, with Board and executive engagement also conducted. An initial comparison of CP16/22 and PS17/23 has been conducted and there are no material changes anticipated between the papers. As at 31 December 2023, we anticipate end-state (1 January 2030) Basel 3.1 requirements to reduce CET1 ratio by 3.7% on a pro-forma basis. We also note that the PRA is yet to publish further guidance on how it intends to adjust the Pillar 2 capital frameworks in the context of Basel 3.1. We intend to explore strategic actions to optimise our balance sheet with respect to the proposed changes under Basel 3.1.

We are cognisant of our dependency on net interest income, particularly generated through mortgage lending. We are exposed to volatility in the mortgage trading environment, with risks to capital arising from the potential income volatility and impacts on profitability and capital resource accrual. Throughout 2024, and with further pressures arising from Basel 3.1, we will continue to explore options available to drive balance sheet and income stream diversification. Alongside Basel 3.1 implementation, we continue to monitor the regulatory environment and understand potential future impact of changes to regulatory capital frameworks. Regulatory changes can have a material impact on our capital position and as such the Bank closely monitors for these changes.

Key indicators:
CET1 Ratio (prior to proposed dividend): 20.4% (2022: 19.8%)
Total Capital Ratio (prior to proposed dividend): 25.3% (2022: 23.8%)
Leverage ratio: 4.1% (2022: 4.0%)

1.8.4 MODEL RISK

Definition:
Model risk is the potential for adverse consequences caused by models. Model risk can lead to financial loss, regulatory penalties or fines, poor business or strategic decision-making, incorrect financial reporting, damage to a bank's reputation or adverse customer outcomes.

Key themes:
As we have permission to adopt an IRB approach, providing a significant capital benefit to the organisation relative to the standardised approach, we acknowledge an exposure to capital risk implications from regulatory change. In 2023, all secured IRB models have been submitted for PRA review and we are currently awaiting feedback.

The development of second generation IFRS 9 models for unsecured retail assets remains an important priority with notable progress being made for retail credit cards. However, uncertainty in the UK economy has continued to complicate ongoing model assessments.

Multiple work streams have been established to align with the requirements outlined in Supervisory Statement SS1/23 for model risk management ("MRM"), primarily focusing on extending the model framework to incorporate deterministic quantitative methods.

Mitigation:
Throughout 2023, we have maintained an active dialogue with the PRA, adapting our secured models in line with regulatory expectations of PS11/20, leading to the regulatory submissions noted above. Additionally, we maintain an independent second line function to review both new and existing models in a timely manner, with recommendations submitted through model governance as part of approval for model use. A robust IRB attestation is completed annually to ensure our permission is retained.

Assessment of continued suitability of capital requirements for all models, including the paused developments for unsecured retail assets, is performed biannually, to consider any reasons that would suggest a change in position, with PMAs approved as required through model governance committees.

We continue to focus on PMAs for IFRS 9 provisioning to mitigate risks deriving from the economic environment, reflecting concerns to specific sectors and to address model limitations.

Future focus:
In 2024, our focus will be on the implementation of secured hybrid models post PRA approval. Should further remediation be necessary following regulatory feedback, a reassessment to timelines and expected capital requirements will be conducted. Furthermore, the development of our second generation IFRS 9 models will continue, alongside the planned implementation of MRM requirements for Q2 2024.

Key indicators:
N/a

1.8.5 LIQUIDITY AND FUNDING RISK

Definition:
Liquidity and funding risk is the risk that we are unable to meet obligations as they fall due or can only do so at excessive cost.

Key themes:
We maintained a strong level of liquidity through 2023. Whilst liquidity coverage ratio ("LCR") reduced, primarily due to Term Funding for Small to Medium-sized Enterprises ("TFSME") repayments of £1.2bn, significant headroom continued to be held against regulatory minimum. We have repaid TFSME funding whilst managing our funding and refinancing position, and remaining funding continues to provide support for our lending activities, funding profile and liquidity resources as we recognise the potential impact of the economic environment and market conditions on customer funds.

We are predominantly customer-funded, with strong retail and SME deposit franchises. Customer behaviour and balances have reflected both cost of living pressures and the higher rate environment, but this has been offset in funding position where we have not been required to compete for more expensive funding.

We have responded to base rate rises by increasing customer rates across deposits (both on sale and closed products), ensuring all customers receive higher interest on their balances.

Wholesale funding comprises secured and unsecured debt programmes as well as participation in the Bank of England TFSME. Wholesale funding activity in 2023 has continued to be limited to MREL and Tier 2 transactions to support our capital resources.

Mitigation:
Liquidity and funding risk is managed primarily with respect to liquidity risk appetite and liquidity coverage ratio. We prepare an annual Internal Liquidity Adequacy Assessment Process ("ILAAP") to ensure that our liquidity risk framework remains appropriate and that we hold sufficient liquidity resources.

We also hold a portfolio of high-quality liquid assets ("HQLA"), alongside contingency funding actions which enable us to raise or preserve liquidity in adverse conditions, and assets available for Bank of England facilities.

Future focus:
Whilst liquidity and funding position continues to be strong, we recognise that cost of living challenges, a higher rate environment and market volatility relating to broader economic, domestic and geopolitical factors may impact the level and cost of liquidity and funding risk in the future. The impact of wholesale market conditions on our liquidity and funding position is limited as we maintain surplus funding, though we recognise the need to refinance TFSME in coming years as well as supporting broader balance sheet strategy. We recognise the potential for uncertainty in customer behaviour as the economic situation evolves, considering such risks in our management of liquidity resources.

Key indicators:
Loan to deposit ratio: 106.4% (2022: 104.1%)
High quality liquid assets ("HQLA"): £4.5bn (2022: £5.9bn)
Liquidity coverage ratio: 211.4% (2022: 265.3%)

1.8.6 MARKET RISK

Definition:
Market risk is the risk of loss as a result of the value of assets or liabilities being adversely affected by movements in market prices, interest rates or exchange rates.

Key themes:
The business model and market risk framework mean that our main exposure to market risk is through potential mismatches in the profiles of customer assets and deposit liabilities. Underlying economic uncertainties and market volatilities have continued to present challenging conditions in which to manage market risk exposures. Market risks associated with fixed term mortgages are a continued area of focus, including pipeline risk and prepayment behaviour. Our acquisition of Sainsbury's Bank's mortgage book has not resulted in a material change to net interest rate risk exposure, and was managed within existing risk appetite. We continue to maintain a structural hedge for current account, non-maturing deposits and other non-interest bearing balances, seeking to provide a natural hedge to mortgage origination and a smoother income profile, while acknowledging the lag effect of investment in a higher rate environment.

Mitigation:
We operate a clear market risk framework, with risk limits in place to monitor and manage exposures and impacts of market movements. We seek to hedge market risks where appropriate, including matching of assets and liabilities, as well as use of derivative instruments (interest rate swaps) to manage remaining exposures. The framework has continued to provide a robust structure, adapted to changing conditions and continued to appropriately manage overall exposure to market risk.

Future focus:
We recognise the potential for further volatility in market conditions, in response to economic, domestic and geopolitical conditions. Customer behaviours in response to economic and market conditions are expected to materialise through prepayment and pipeline risks, deposit levels and mix, as well as potential impacts of the Mortgage Charter. Following a period of rising rates, market risk will likely be influenced by the risk of reducing rates and volatility as the rate environment responds to economic conditions and central bank actions.

The impact of severe events due to changing climate patterns or rapid shifts in climate change-related regulation around the world has the potential to cause sharp adjustments to market prices as well as interest rates and exchange rates. Increased market risk as well as operational risk could also arise as a result of disruption to business services, supply chains and transport links.

Key indicators:
PV01: measures the sensitivity of future cash flows to a one basis point shift in interest rates.

END

FORWARD-LOOKING STATEMENTS

This document contains certain forward-looking statements with respect to the business, strategy and plans of the Group and its current targets, goals and expectations relating to its future financial condition and performance, developments and/or prospects. Forward-looking statements sometimes can be identified by the use of words such as ‘may’, ‘will’, ‘seek’, ‘continue’, ‘aim’, ‘anticipate’, ‘target’, ‘projected’, ‘expect’, ‘estimate’, ‘intend’, ‘plan’, ‘goal’, ‘believe’, ‘achieve’, ‘predict’, ‘should’ or in each case, by their negative or other variations or comparable terminology, or by discussion of strategy, plans, objectives, goals, future events or intentions.

Examples of such forward-looking statements include, without limitation, statements regarding the future financial position of the Group and its commitment to its plan and other statements that are not historical facts, including statements about the Group or its Directors’ and/or management’s beliefs and expectations. Any such forward-looking statements are not a reliable indicator of future performance, as they may involve significant stated or implied assumptions and subjective judgements, which may or may not prove to be correct. There can be no assurance that any of the matters set out in forward-looking statements are attainable, will actually occur, will be realised, or are complete or accurate. Past performance is not necessarily indicative of future results. Differences between past performance and actual results may be material and adverse.

For these reasons, recipients should not place reliance on, and are cautioned about relying on, forward–looking statements as actual achievements, financial condition, results or performance measures could differ materially from those contained in the forward-looking statement. By their nature, forward-looking statements involve known and unknown risks, uncertainties and contingencies because they are based on current plans, estimates, targets, projections, views and assumptions and are subject to inherent risks, uncertainties and other factors both external and internal relating to the Group’s plan, strategy or operations, many of which are beyond the control of the Group, which may result in it not being able to achieve the current targets, predictions, expectations and other anticipated outcomes expressed or implied by these forward-looking statements. In addition, certain of these disclosures are dependent on choices relying on key model characteristics and assumptions and are subject to various limitations, including assumptions and estimates made by management. No representations or warranties, expressed or implied, are given by or on behalf of the Group as to the achievement or reasonableness of any projections, estimates, forecasts, targets, prospects or returns contained herein. Accordingly, undue reliance should not be placed on forward-looking statements.

Any forward-looking statements made in this document speak only as of the date of this document and it should not be assumed that these statements have been or will be revised or updated in the light of new information or future events and circumstances arising after today. The Group expressly disclaims any obligation or undertaking to provide or release publicly any updates or revisions to any forward-looking statements contained in this document as a result of new information or to reflect any change in the expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based, except as required under applicable law or regulation.

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