

NEWCASTLE BUILDING SOCIETY ANNOUNCES 2018 FINANCIAL RESULTS

Key Highlights

- Operating profit of £14.7m compared to £12.1m for 2017
- Total operating income of £64.5m compared to £57.9m for 2017
- Strong Capital ratios - Common Equity Tier 1 ratio of 15.7% and Leverage ratio of 5.4%
- Robust liquidity ratio of 14.6%
- Gross mortgage lending of £520m
- The number of mortgages in 3 months arrears or more at a record low of 0.30
- Our multi-million pound branch refurbishment programme with newly refurbished branches in Durham, Gosforth and Carlisle
- £797,000 or 6% of our pre-tax profits made in charitable donations
- Newcastle Building Society Community Fund awarded over £179,000 in grants to 76 charities across our heartland
- Partnership with The Prince's Trust
- Industry awards including for the second year "What Mortgage Awards 2018" Winner for Best Regional Building Society
- 1,500 Dementia friends trained by the Society's Dementia Friends champion

Chief Executive's Statement

I am very pleased to report that 2018 was a year of continued positive progress for the Society, with growth in residential lending, more new savers resulting in an increase in Members and increased levels of financial advice business.

This progress is underpinned with a robust financial performance, including increased operating profit, strong capital and liquidity ratios and very low levels of arrears.

Financial performance

It is only possible for the Society to thrive and continue to serve the region if our underlying business model is sustainable in the long term and our financial performance is robust. Profitability is one of the key financial performance measures.

Profit before tax improved to £13.3m for the year ended 31 December 2018 compared to £13.1m for 2017. Our 2017 profit before tax was positively impacted by a one-off credit of over £2m relating to the purchase of our Cobalt office and it is pleasing to report that in 2018 we saw that one-off credit replaced by an overall improvement in Operating Profit before provisions and exceptional items, which increased by £2.6m to £14.7m.

Overall growth in income of £6.6m, was offset by an increase in costs of £3.9m associated with the significant ongoing investment into the business, including our branch refurbishment programme and pay and grading project. The cost to income ratio improved from 79% to 77%. Net interest margin improved from 0.79% to 0.92% reflecting increased income.

Mortgage impairment charges have increased, from £0.2m to £1.5m, the majority of which reflects a small number of legacy non-performing commercial loans.

Provisions for liabilities and charges decreased by £1.1m from £1.0 debit to £0.1m credit. The credit relates to the reduction in the provisions required for the Financial Services Compensation Scheme levy and consumer redress.

The Group's capital ratios remain robust with Common Equity Tier 1 ratio improving from 15.3% to 15.7% and Tier 1 capital ratio reducing slightly from 16.6% to 16.3%. The Group's overall capital ratio (Solvency ratio) also reduced to 17.7% compared to 18.9% at the end of 2017. Both reductions were as a result of a planned repayment of one of the Group's Permanent Interest Bearing Shares during 2018. The leverage ratio (on a transitional basis) was 5.4%.

Despite the weak growth in the mortgage market during 2018 and strong competition, as noted above, our gross residential mortgage lending was £520m and net residential lending was £160m. The percentage of mortgage loans in arrears of 3 months or more, across our whole mortgage portfolio based on the number of loans, reduced again from 0.34% to 0.30%; lower than the industry average. Possession cases also continued at very low levels reflecting the excellent credit quality of the Society's residential lending.

The Group's liquidity, excluding encumbered assets, ended the year as 14.6%, compared to 17.0% in 2017. This had been actively managed down over the second half of the year to improve efficiency but remains well within in our planned operating guidelines and above our minimum operating requirements.

The Society's liquidity coverage ratio was 179% against a regulatory minimum required level of 100%. This significant headroom reflects the quality of the Society's liquidity with the majority of it invested in AAA/AA rated assets, in the UK.

Connecting with our Purpose

At the heart of Newcastle Building Society lies our Purpose, which states that we 'connect communities in the North East with a better financial future' and leads us to put our customers and the communities we serve foremost in our plans and ambitions for the future.

In what proved to be a very busy and productive year for the Society, we achieved a number of positive outcomes in delivering our Purpose and making a genuine difference for the communities we serve. Just some of the highlights from the year include:

- The launch of our new branch concept for Durham, Gosforth and Carlisle branches as part of our multi-million pound branch refurbishment programme;
- Our continued support for the Newcastle Building Society Community Fund at the Community Foundation, which has enabled the launch of Building Improvement Grants, designed to help maintain and improve community buildings in the region, with the first £50,000 grant awarded to Springfield Community Association;
- The Newcastle Building Society Community Fund was also pleased to announce a four-year partnership, committing donations of more than £100,000 to The Prince's Trust, supporting programmes which seek to invest in young talent and improve employability in the region. The Prince's Trust also provides significant leadership development opportunities for colleagues across the Society;
- Our ongoing commitment to Dementia Friends, which has to date involved over 1,500 colleagues, customers and staff from the local high street in receiving awareness training from the Society's Dementia Friend champion; and
- By no means least welcoming new colleagues to the Society in particular those who have joined us as part of our early talent community.

Building authentic and lasting customer relationships

We were pleased to see our customer satisfaction score improve from 96% to 98% in 2018. Helping people own their homes is a key pillar of our Purpose and is at the heart of our building society.

Our gross lending for 2018 exceeded £520m, slightly reduced from £535m in 2017, in a fiercely competitive market. Our prime net lending was over £160m leading to an overall increase in our residential mortgage book.

Despite the broader UK economic challenges, we supported over 1,100 first time buyers in their quest to own their own home. Our Self Employed mortgage volumes have doubled and we have also introduced 'Help to Buy' and 'Buy to Let' mortgages for this growing self-employed market reflecting the continuing change in employment trends.

Once again it was great to be recognised in a number of industry awards. For the second year in a row we have been awarded 'What Mortgage's' Best Regional Building Society. We were also named Best Self Build Lender by 'Build IT' and we were also recognised by the Legal and General Mortgage Club Awards as best smaller lender for 2018. When combined with service quality awards received by clients of our Newcastle Strategic Solutions Limited subsidiary, we were involved in winning 24 industry awards in 2018.

As well as helping customers own their home, we also believe that it is important that we encourage people to save and help them plan their finances.

Despite the backdrop of extensive bank branch closures across our region, our commitment to being present in the towns and cities across the North East remains firm. We recognise the power of communities and the role of the high street as a focus for community life. That is why we are improving the branch experience we provide to our customers, as part of a wider investment programme, delivering modern, bright and open spaces, with private meeting areas, friendly and knowledgeable colleagues, and a financial adviser in every branch.

Our latest new branch format was launched in 2018 in Durham, Gosforth and Carlisle and we continue with our programme to update all of our branch network by the end of 2019.

Our savings accounts offer some of the best buy savings rates on the high street and during 2018 we were featured in national press best buy tables. We added to our savings portfolio a new regular saver product and a one or two year fixed rate bond. We also increased the rate on the current issue of The Newcastle Community Saver easy access account.

In the second half of the year we introduced our Newcastle Cash Lifetime ISA, which enables customers to save for a deposit for their first home or for their retirement, attracting a 25% UK Government bonus on amounts saved each tax year.

Our growing range of savings accounts has been well received and I am delighted that as a result, 2018 saw an increase in the number of Members of the Society. We have offered our new Members a warm welcome to Newcastle Building Society, committing that we will remain on the high street now and in the future.

Our financial advice subsidiary, Newcastle Financial Advisers Limited, gives customers financial advice regardless of how much they have to invest. Newcastle Financial Advisers Limited has a significant and growing level of funds under management for people in the region.

Our Pension Clinics were very successful, offering free 30 minute chats with a financial adviser to help people get answers to their pension questions and see what they may need to do next.

Newcastle Financial Advisers increased income and profits in 2018 and scores highly for customer satisfaction.

Helping our colleagues realise their potential

Our colleagues are the driving force of our Society and in return we aim to be a great place for them to work, where they can realise their potential. It is also important to us as a significant employer, that where appropriate, we continue to offer and grow the employment opportunities we offer across the region, adding 68 new jobs in 2018.

Our Human Resources team are central to how we work to develop the region's talent and potential and it was great to see their work recognised by the North East HR&D CIPD Awards in June when they won the award for Excellence in Resourcing & Talent Management.

We have made a significant investment in our new leadership programmes for senior managers, and continue to build our early talent programme as we build our contribution to nurturing regional talent, which can come from all walks of life and irrespective of background and personal circumstances.

Our early talent programme has been running for a number of years for graduate recruitment and undergraduate placement, but has been further developed to include apprenticeships. Our growing apprenticeship opportunities are across a range of business areas, with all apprenticeships attracting a Living Wage salary (paying above the Government recommended wage), a structured learning programme with both a nationally recognised qualification and a career at the end. Our partnership with The Prince's Trust also plays a key role in our developing talent and supporting employability in the region.

An important part of our customer offering is the provision of face to face financial advice. We understand that this service is highly valued by our customers and we are one of the few financial services companies still offering financial advice on the high street.

Fundamental to this is our financial adviser colleagues and our commitment to growing the financial adviser talent of the future. Our bespoke training programme between Openwork and Newcastle Financial Advisers Limited provides opportunities for growth and development and colleague applications are invited from across the business. The programme leads to a professional status and a role as a qualified financial adviser. We are delighted that two more graduates from the programme have recently taken up full time financial adviser positions in the branch network after completing their professional training.

In 2018 we improved employer pension contributions for more than half our colleagues to help them build a bigger pension pot, and following a review of pay and grading, more than a third of our colleagues have enjoyed a salary uplift over and above the cost of living increase also provided. We are proud to be a Real Living Wage employer, which goes further than the Government's national minimum wage.

Connecting with our communities

Our branches continue to play a key role in their local communities. Where possible, we are introducing community spaces into our refurbished branches which are available to community groups and have already been used in a host of different ways.

We have also tried to be sympathetic to local tradition when we have restored older buildings – for example the restoration work on the iconic Durham Teapot that sits above our Durham branch, undertaken by the City of Durham Trust and the stained glass windows and chandeliers in our new location in Carlisle have both preserved features which are valued by local residents. We consider it a privilege to support those in our towns and cities who are actively working to improve the potential, history and culture of our region.

We donated £797,000 or 6% of our pre-tax profits to charity during 2018. We have continued to build the Newcastle Building Society Community Fund at the Community Foundation, through donations made by the Society in proportion to balances held in our Community Saver accounts and our colleague fundraising activities.

The Community Fund is building a legacy for future Members, with increasing capacity to make grants which support local charities and community groups. Our grant programme is expanding year on year and now includes larger grants of up to £50,000 to support community building improvements. In addition, a total of £179,000 was awarded in 63 smaller grants during 2018.

We have a long-standing relationship with the Sir Bobby Robson Foundation. The Newcastle Building Society Community Fund at the Community Foundation is continuing that relationship with an ongoing and significant level of funding support for at least the next five years. The combined contributions of the Society and The Newcastle Building Society Community Fund have just passed the £2.8m mark in cumulative donations to this worthy cause, which funds leading cancer research, diagnosis and treatment for people across our region.

There are around 35,000 people living with dementia in the North East, a statistic that is expected to increase. We have committed to ensuring that every colleague will become a Dementia Friend and have also been offering Dementia Friends sessions to customers in our branches, and extended an open invitation for others on the high street to join us. I am proud that we have over 1,500 Dementia Friends who received training and learnt about improving the lives of those living with dementia in our region.

Our colleagues have continued to embrace our volunteering programme in 2018, more than doubling their volunteering contribution this year with 55% of colleagues volunteering. They have spent over 4,750 hours in the community supporting 137 groups and local charities.

Helping our clients and partners succeed

Newcastle Strategic Solutions Limited and Newcastle Systems Management Limited, two of the Society's subsidiaries received ISO 27001 Certification for their Information Security Management System. Meeting this international standard benchmark evidences our ongoing investment in having the right controls to respond to the threats to data and IT service provision. We were also pleased to renew our Cyber Essentials Plus accreditation during the year.

Newcastle Strategic Solutions continues to be the UK's leading provider of outsourced savings management services and we were delighted to see strong growth in scale of savings balances under administration throughout 2018 and a number of clients win industry awards for the quality of service provided to their customers.

Summary

2018 has been a significant year of change and progress for Newcastle Building Society. We have seen our highest growth in income compared to recent years with increasing profitability year on year and our Member base has started to grow again. We have seen good levels of lending and are particular pleased to be able to support new homeowners in taking their first steps onto the property ladder.

Our connection to our communities is even more evident and embedded in the day to day operations of the Society. Our contributions to the Newcastle Building Society Community Fund at the Community Foundation are both enabling a positive impact to be made immediately through community grants and building a legacy for future generations as the fund continues to grow. Finally, our Newcastle Strategic Solutions Limited and Newcastle Systems Management Limited subsidiaries continue to offer market leading services and make a positive contribution to our financial performance.

Whilst economic uncertainties continue from Brexit and other global issues, we passionately believe in our Purpose of "Connecting Communities in the North East with a better Financial Future." and continue to invest in our business, colleagues and communities to build a strong regional brand that is recognised for making a genuine difference for the communities we serve.

We have no doubt that the year ahead will bring many unique challenges but we believe we are well placed to address them and continue in our long term aspiration to live out our Purpose and make a genuine, positive contribution in supporting our Members by helping them save, plan their finances and own their home, and in our support for their communities across the region.

Andrew Haigh
Chief Executive
27th February 2019

NEWCASTLE BUILDING SOCIETY
PRELIMINARY ANNOUNCEMENT
for the year ended 31 December 2018

SUMMARY CONSOLIDATED INCOME STATEMENTS

	2018	2017
	£m	£m
Interest receivable and similar income	75.2	65.6
Interest payable and similar charges	(41.0)	(36.5)
Net interest income	34.2	29.1
Other income and charges	30.2	28.7
Gains less losses on financial instruments and hedge accounting	0.1	0.1
Administrative expenses	(46.9)	(43.0)
Depreciation	(2.9)	(2.8)
Operating profit before impairments, provisions and exceptional items	14.7	12.1
Impairment charges on loans and advances to customers	(1.5)	(0.2)
Provisions for liabilities and charges	0.1	(1.0)
Exceptional gain on purchase of Cobalt Offices	-	2.2
Profit for the year before taxation	13.3	13.1
Taxation expense	(2.5)	(2.2)
Profit after taxation for the financial year	10.8	10.9

SUMMARY CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	2018	2017
	£m	£m
Profit for the financial year	10.8	10.9
Other comprehensive income/(expense):		
<i>Items that may be reclassified to income statement</i>		
Movement on fair value through other comprehensive income/available for sale reserve	(1.7)	1.8
Income tax on items that may be reclassified to income statement	0.3	(0.3)
Total items that may be reclassified to income statement	<u>(1.4)</u>	<u>1.5</u>
<i>Items that will not be reclassified to income statement</i>		
Actuarial remeasurements on retirement benefit obligations	-	-
Income tax on items that will not be reclassified to income statement	-	-
De-recognition of pensions surplus	(1.1)	(1.7)
Total items that will not be reclassified to income statement	<u>(1.1)</u>	<u>(1.7)</u>
Total comprehensive income for the financial year	<u>8.3</u>	<u>10.7</u>

SUMMARY CONSOLIDATED BALANCE SHEETS

	2018	2017
	£m	£m
ASSETS		
Liquid assets	692.4	789.8
Derivative financial instruments	3.5	4.9
Loans and advances to customers	2,772.2	2,707.3
Fair value adjustments for hedged risk	175.9	206.2
Property, plant and equipment	38.8	38.8
Other assets	15.0	15.1
TOTAL ASSETS	3,697.8	3,762.1
LIABILITIES		
Shares	2,713.7	2,788.5
Fair value adjustments for hedged risk	0.4	1.6
Deposits and debt securities	552.4	504.6
Derivative financial instruments	178.3	210.2
Other liabilities	12.9	15.4
Subordinated liabilities	25.0	25.0
Subscribed capital	20.0	30.0
Reserves	195.1	186.8
TOTAL LIABILITIES	3,697.8	3,762.1

SUMMARY CONSOLIDATED CASH FLOW STATEMENTS

	2018	2017
	£m	£m
Cash (outflows) / inflows from operating activities	(50.6)	66.9
Payment into defined benefit pension scheme	(1.5)	(2.0)
Net cash (outflows) / inflows from operating activities	(52.1)	64.9
Cash (outflows)/inflows from investing activities		
Purchase of property, plant and equipment	(2.9)	(18.8)
Sale of property, plant and equipment	-	-
Purchase of investment securities	(72.5)	(185.1)
Sale and maturity of investment securities	121.2	154.9
Net cash (outflows)/inflows from investing activities	45.8	(49.0)
Cash outflows from financing activities		
Interest paid on subordinated liabilities	(0.8)	(2.1)
Interest paid on subscribed capital	(3.5)	(3.5)
Repayment of subordinated liabilities	-	(25.0)
Repayment of subscribed capital	(10.0)	-
Repayments under finance lease agreements	-	(0.1)
Net cash outflows from financing activities	(14.3)	(30.7)
Net (decrease) in cash	(20.6)	(14.8)
Cash and cash equivalents at start of year	183.6	198.4
Cash and cash equivalents at end of year	163.0	183.6

Summary of key financial ratios	2018	2017
	%	%
Gross capital as a percentage of shares and borrowings	7.37	7.36
Liquid assets as a percentage of shares and borrowings	21.20	23.94
Profit for the year as a percentage of mean total assets	0.29	0.29
Management expenses for the year as a percentage of mean total assets	1.33	1.24

Notes

- The financial information set out above, which was approved by the Board of Directors on 26 February 2019, does not constitute accounts within the meaning of the Building Societies Act 1986.
- The financial information for the years ended 31 December 2018 and 31 December 2017 has been extracted from the Accounts for those years and on which the auditors have given an unqualified opinion.