Announcement of half-year results for the six months ended 30 June 2018

Key Highlights
• Operating profit increased by 16% to £7.2m (2017: £6.2m) • Profit before tax was £6.9m. Profit before tax in the comparable period ended 30 June 2017 of £7.2m included a credit of £2.1m on the purchase of our Cobalt offices. Excluding the gain on purchase, profit increased by £1.8m (35%) • Gross lending of £229m in the first half of 2018 was in line with plan (2017: £303m) • Mortgage arrears reduced and remain at very low levels at 0.36% (2017: 0.39%), well below industry averages • Capital ratios remain robust with Total Capital Ratio (Solvency) at 18.9%, Tier 1 Ratio at 16.7%, Common Equity Tier 1 Ratio at 15.7% and Leverage Ratio at 5.3% • Liquidity as a percentage of shares, deposits and liabilities (excluding encumbered assets) was 17.3% • We have supported over 500 first time buyers and seen Self Employed mortgage volumes double • Newcastle Building Society Community Fund at the Community Foundation continues to grow and increased levels of grants have been made • 26 new jobs created • Colleagues have doubled their volunteering contribution so far this year. Over 117 organisations have been able to count on willing support in 2017/18

Chief Executive's Review

For over 150 years Newcastle Building Society has been connecting communities in the North East with a better financial future. This is our purpose as a building society and our Members can rely on us to help them save and plan their finances, buy their own home, make positive changes to our local communities and of course be a great place for colleagues to work and develop.

In the first half of 2018 we have made great progress, with growth in lending, more new savers and increased levels of financial advice business. In terms of financial performance we are reporting increased profits from ongoing operations, strong capital ratios, a robust liquidity position and low levels of arrears, reflecting the excellent credit quality of our residential mortgage book.

I am delighted that we have been able to improve operating profitability at a time when we continue to invest in our branch network, our community and our people. We have also continued to upgrade and invest in our systems. The difference this makes to our customers has been seen in growth in Members in the North East and industry awards which have included Legal and General Mortgage Club Award - Best Small Lender and Excellence in Resource and Talent Management from the Chartered Institute of Personnel Development. Put simply making sufficient and sustainable profits allows us to serve all of our stakeholders effectively.

Profitability

Profit before tax was £6.9m for the six months ended 30 June 2018 compared to £7.2m for the first half of 2017. Although we have seen a slight headline profit reduction from the prior comparable period, 2017 profit before tax included a one off credit of over £2m in relation to the purchase of our Cobalt offices.

Operating profit before provisions and the Financial Services Compensation Scheme levy increased by 16% to £7.2m from £6.2m.

Net interest income increased by £2.4m to £16.0m reflecting increased income from mortgage lending, the impact of rises in LIBOR coupled with the ongoing benefit of reduced funding costs from participation in the Bank of England Term Funding Scheme. Our net interest margin improved to 86bp at 30 June 2018. (30 June 2017: 75bps and 31 December 2017: 79bps).

Other income and charges increased by £0.5m to £14.8m (2017: £14.3m). Income from Newcastle Strategic Solutions Limited, our Savings Management outsourcing business continues to grow as balances under management rise. Income from Newcastle Financial Advisers Limited, our financial advice subsidiary was up by £0.2m when compared to the period ended 30 June 2017.

Our cost to income ratio improved by 1.5% to 76.5% (2017: 78.0%). Management expenses (comprising administration expenses and depreciation) increased by £1.9m from £21.7m to £23.6m. This primarily reflects the investment in our People through our Pay and Grading project which has seen the Society increase pension provision and benchmark the level of salary it offers. We have also created new posts which are supporting the Society's growth, delivering effective management of risk and reflect the continuing investment being made in the Society and its branch network.

Capital

The Total Capital Ratio (Solvency) increased to 18.9% from 18.3% at the prior comparable period. The ratio was the same as 31 December 2017 (18.9%) with profit generated through the first half of 2018 offset by lending growth coupled with the amortisation of Tier 2 capital as it approaches maturity in 2019. From 30 June 2017 to 30 June 2018, the Tier 1 ratio improved from 15.8% to 16.7% and Common Equity Tier 1 ratio improved from 14.5% to 15.7%. The Society's Basel III leverage ratio (transitional basis) was 5.3% at 30 June 2018 (5.0% at 30 June 2017). Capital ratios disclosed include half year retained profits.

Liquidity

Liquid assets as a percentage of Shares, Deposits and Liabilities at 30 June 2018 were 23.9% (2017: 25.4%). Excluding encumbered liquid assets the ratio decreased from 18.3% at 30 June 2017 to 17.3% at 30 June 2018. The quality of liquidity continues to be excellent, comprising assets held in cash or that can easily be converted to cash through treasury markets (repo) or via the various Bank of England liquidity schemes. We expect to carefully manage liquidity to lower levels over the second half of the year.

Credit Risk

The percentage of mortgages in arrears by 3 months or more continued at a level lower than the UK average, at 0.36% compared to 0.39% at 30 June 2017, and 0.34% at 31 December 2017. Possession cases remain at very low levels. Gross lending for the first half of the year was in line with plan. Net lending was lower than the prior comparable period as continuing growth in mortgages was offset by higher than forecast redemptions from our closed commercial and residential social landlord books. The Society's prime residential mortgage book grew by £61m during the first half of 2018 (£155m first half 2017).

Supporting our Customers

We recognise the power of communities and the role of the high street as a focus for community life. 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 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 format branch launched in Durham earlier this year. It will be followed by Carlisle and Gosforth, and is part of an ambitious plan that will see all our branches updated by early 2020.

We continue to provide some of the best buy savings rates on the high street and earlier this year supplemented this with the launch of a new regular saver product at 2.25% (including bonus) to encourage a savings habit across the region.

In the first six months of this year, we have supported over 500 first time buyers in their quest to own their own home. Our gross lending exceeded £220m, with prime net lending increasing by over £50m.

We've seen our Self Employed mortgage volumes double and we have also introduced Help to Buy and Buy to Let mortgages for this growing market reflecting the continuing change in employment trends.

We were very pleased to be recognised by the Legal and General Mortgage Club Awards as best smaller lender for 2018.

The Society currently offers customers access to Co-op's market leading funeral plans. Following a recent agreement, customers will now be able to access broader later-life planning services provided by Co-op.

In May the Society's subsidiaries, Newcastle Strategic Solutions Limited and Newcastle Systems Management Limited 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.

Investing in our Colleagues
We have continued to build on our Gold Investors in People recognition which we were awarded last year. To be able to better understand and respond to our colleagues' views, we have introduced a new online engagement tool which gives us the opportunity to regularly check feedback and opinions. It has already helped guide some of our developments and improvements.

We have 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 have made a significant investment in our new leadership programmes for senior managers, and continue to build our apprentice programme. We offer great apprenticeship opportunities across a range of business areas, supporting our apprentices with a Living Wage salary, a structured learning programme with both a nationally recognised qualification and a career at the end. This complements the graduate recruitment and undergraduate placement programmes we have been running for many years.

Our commitment to growing the financial adviser talent of the future through a bespoke training programme between Openwork and our Newcastle Financial Adviser subsidiary continues. The programme provides an opportunity 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.

We have created 26 new roles so far this year to support our Society's growth and investment plans. Our Human Resources Team are central to how we work to develop the region's talent and potential and we were proud to see them recognised by the North East HR&D CIPD Awards in June when they won the award for Excellence in Resourcing & Talent Management.

Working with our Communities
We aim to help our communities make positive changes.

There are around 35,000 people living with dementia in the North East a statistic that is expected to increase. Our response is a commitment to ensuring that every colleague will become a Dementia Friend by 2019. We are also making Dementia Friends sessions available to customers in our branches, and even welcoming staff from other banks to learn more about improving the lives of those living with dementia in our region.

Our branch community connections continue to grow, providing us with unique opportunities to help out in ways that make a real difference to those involved. Whether that's restoration work on the Durham Teapot undertaken by the City of Durham Trust, or NE Youth's 'Projects With Pride' Awards, 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 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. Our grant programme is expanding year on year and now includes larger grants of up to £50,000 to support community building improvements.

The Community Fund will also maintain support for the Sir Bobby Robson Foundation, with an ongoing and significant level of funding support for at least the next five years. We 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.

Our community grants are supplemented by a very active colleague volunteering programme. Colleagues have doubled their volunteering contribution so far this year. Over 117 organisations have been able to count on willing support in 2017/18.

Our commitment to improving access to financial education across our region continues. Our regular financial 'Big Talks' which are open to members and non-members alike are ideal for those who want to learn more about how to manage their finances and plan for the future. Investments, retirement planning, inheritance tax planning and estate planning are all covered in our informal but informative, myth busting sessions that take place across the North East and at no cost or obligation to those who wish to participate.

Across our region we continue to work with school children as part of our primary school education programme, the Boardroom Charity Challenge. Our branch led financial education sessions culminate with a presentation to a Chief Executive-led panel. This year's winner was Rainbird Primary School.

Summary

I am pleased with the Society's improved progress and performance in the first half of the year. We will continue to invest in the business and focus on our purpose and why we are here as a building society. Whilst our Society, colleagues and communities look set to face continued economic uncertainty from Brexit and wider global issues, we will continue to do what we do best; helping people save and plan their finances and own their own home, being a great place to work and supporting our communities in making positive changes.

Andrew Haigh
Chief Executive
30th July 2018

Forward-looking statements

Certain statements in this half-yearly information are forward-looking. These statements are made in good faith based on the information available up to the time of approval of this report and such statements should be treated with caution due to the inherent uncertainties, including both economic and business risk factors, underlying any such forward-looking information. Therefore actual results may differ materially from those expressed or implied by these forward-looking statements. The Directors undertake no obligation to update any forward-looking statements whether as a result of new information, future events or otherwise.

Summary Consolidated Income Statement

	Unaudited 6 months 30 Jun 18 £m	**Unaudited 6 months 30 Jun 17 £m**	**Audited 12 months 31 Dec 17 £m**
Interest receivable and similar income	36.0	31.9	65.6
Interest payable and similar charges	(20.0)	(18.3)	(36.5)
Net interest income	**16.0**	**13.6**	**29.1**
Other income and charges	14.8	14.3	28.8
Total operating income	**30.8**	**27.9**	**57.9**
Administrative expenses	(22.1)	(20.5)	(43.0)
Depreciation	(1.5)	(1.2)	(2.8)
Operating profit before impairments, provisions and exceptional items	**7.2**	**6.2**	**12.1**
Impairment charges on loans and advances to customers	(0.2)	(0.2)	(0.2)
Provisions for liabilities and charges	(0.1)	(0.9)	(1.0)
Exceptional gain on purchase of Cobalt Offices	-	2.1	2.2
Profit before taxation	**6.9**	**7.2**	**13.1**
Taxation expense	(1.3)	(1.4)	(2.2)
Profit after taxation for the financial period	**5.6**	**5.8**	**10.9**

The Notes on pages 10 to 21 form an integral part of this condensed consolidated half-yearly financial information.

Summary Consolidated Statement of Comprehensive Income

	Unaudited 6 months 30 Jun 18 £m	Unaudited 6 months 30 Jun 17 £m	Audited 12 months 31 Dec 17 £m
Profit for the period	5.6	5.8	10.9
Other comprehensive (expense)/income:			
Items that may be reclassified to income statement			
Movement on available for sale reserve	(0.1)	1.8	1.8
Income tax on items that may be reclassified to income statement	-	(0.4)	(0.3)
Total items that may be reclassified to income statement	(0.1)	1.4	1.5
Items that will not be reclassified to income statement			
Derecognition of pension surplus	-	-	(1.7)
Total items that will not be reclassified to the income statement	-	-	(1.7)
Total other comprehensive (expense)/income	(0.1)	1.4	(0.2)
Total comprehensive income for the financial period	5.5	7.2	10.7

The Notes on pages 10 to 21 form an integral part of this condensed consolidated half-yearly financial information.

Summary Consolidated Balance Sheet

	Unaudited 30 Jun 18 £m	Restated Unaudited 30 Jun 17 £m	Audited 31 Dec 17 £m
ASSETS			
Liquid assets	791.5	843.6	789.8
Derivative financial instruments	5.0	5.0	4.9
Loans and advances to customers	2,721.5	2,702.4	2,707.3
Fair value adjustments for hedged risk	183.0	207.7	206.2
Property, plant and equipment and other assets	53.2	54.8	53.9
TOTAL ASSETS	**3,754.2**	**3,813.5**	**3,762.1**

	Unaudited 30 Jun 18 £m	Restated Unaudited 30 Jun 17 £m	Audited 31 Dec 17 £m
LIABILITIES			
Shares	2,775.1	2,830.2	2,788.5
Fair value adjustments for hedged risk	0.8	2.8	1.6
Deposits and debt securities	529.9	490.0	504.6
Derivative financial instruments	186.6	209.3	210.2
Other liabilities	14.5	17.9	15.4
Subordinated liabilities	25.0	50.0	25.0
Subscribed capital	30.0	30.0	30.0
Reserves	192.3	183.3	186.8
TOTAL LIABILITIES	**3,754.2**	**3,813.5**	**3,762.1**

The Notes on pages 10 to 21 form an integral part of this condensed consolidated half-yearly financial information.

Summary Consolidated Statement of Movement in Members' Interests

For the 6 months ended 30 June 2018 (unaudited)

	General reserve	Fair Value through Other Comprehensive Income	Total
	£m	£m	£m
At 1 January 2018	185.0	1.8	186.8
Movement in the period	5.6	(0.1)	5.5
At 30 June 2018	190.6	1.7	192.3

For the 6 months ended 30 June 2017 (unaudited)

	General reserve	Available for sale reserve	Total
	£m	£m	£m
At 1 January 2017 (Restated)	175.8	0.3	176.1
Movement in the period	5.8	1.4	7.2
At 30 June 2017 (Restated)	181.6	1.7	183.3

For the year ended 31 December 2017 (audited)

	General reserve	Available for sale reserve	Total
	£m	£m	£m
At 1 January 2017	175.8	0.3	176.1
Movement in the year	9.2	1.5	10.7
At 31 December 2017	185.0	1.8	186.8

The Notes on pages 10 to 21 form an integral part of this condensed consolidated half-yearly financial information.

Summary Consolidated Cash Flow Statement

	Unaudited 6 months to 30 Jun 18 £m	Unaudited 6 months to 30 Jun 17 £m	Audited 12 months 31 Dec 17 £m
Net cash flows from operating activities	26.0	87.8	66.9
Payment into defined benefit pension scheme	(0.6)	(0.9)	(2.0)
Net cash flows from investing activities	52.7	(47.9)	(49.0)
Net cash flows from financing activities	(2.2)	(3.0)	(30.7)
Net increase in cash and cash equivalents	**75.9**	**36.0**	**(14.8)**
Cash and cash equivalents at the start of period	183.6	198.4	198.4
Cash and cash equivalents at the end of the period	**259.5**	**234.4**	**183.6**

Other percentages

	6 months 30 Jun 18 %	Restated 6 months 30 Jun 17 %	12 months 31 Dec 17 %
Gross capital as a % of shares and borrowings	7.5	8.0	7.4
Liquid assets as a % of shares and borrowings	23.9	25.4	23.9
Wholesale deposits as a % of shares and borrowings	16.0	14.8	15.3
Liquid assets as a % of shares and borrowings excluding encumbered assets	17.3	18.3	17.0
Net interest receivable as a % of mean total assets (“NIM”)	0.86	0.75	0.79
Cost to income ratio	76.5	78.0	79.0
Profit after tax as a % of mean total assets	0.30	0.31	0.29
Management expenses as a % of mean total assets*	1.26	1.18	1.24
Common Equity Tier 1 Ratio	15.7	14.5	15.3
Tier 1 Ratio	16.7	15.8	16.6
Total Capital Ratio (Solvency)	18.9	18.3	18.9
Leverage Ratio (Basel III - end point)	5.0	4.6	4.7
Leverage Ratio (Basel III - transitional)	5.3	5.0	5.2

** Expressed on an annualised basis*

The above percentages are unaudited. Capital ratios disclosed include half year retained profits. The figures for the 12 months ended 31 December 2017 are extracted from the audited 2017 accounts. The Notes on pages 10 to 21 form an integral part of this condensed consolidated half-yearly financial information.

Notes

1. General information

1.1. The half-yearly financial information set out above, which was approved by the Board of Directors, does not constitute accounts within the meaning of the Building Societies Act 1986.

1.2. The financial information for the 12 months to 31 December 2017 has been extracted from the financial statements for that year, and on which the auditors gave an unqualified opinion, and which have been filed with the Financial Conduct Authority and Prudential Regulation Authority.

1.3. The half-yearly financial information for the 6 months to 30 June 2018 and the 6 months to 30 June 2017 is unaudited.

1.4. The announcement will be sent to holders of the Society's permanent interest bearing shares. Copies are available from the Society's Principal Office at Portland House, Newcastle upon Tyne NE1 8AL.

2. Basis of preparation

The condensed consolidated financial information for the half-year ended 30 June 2018 has been prepared in accordance with the Disclosure and Transparency Rules of the Financial Conduct Authority and with IAS 34, 'Interim financial reporting' as adopted by the European Union. The half-yearly financial information should be read in conjunction with the annual financial statements for the year ended 31 December 2017, which have been prepared in accordance with IFRSs as adopted by the European Union.

The Board has reviewed medium and long term plans over a 5 year horizon with particular emphasis on examining forecast capital, profitability and liquidity of the Group and the risks to those forecasts through a variety of stress testing scenarios. In reviewing the Group capital plans the Board has also considered the impact of recent pronouncements from the Financial Policy Committee which increase the capital requirements for Banks and Building Societies through a higher countercyclical capital buffer. This horizon is considered appropriate through alignment to the Group's usual forecasting and management reporting allowing robust and continuous assessment of the Group's expected position and principal risks over the time-frame. Active risk management is undertaken to mitigate the Group's principal risks as detailed in note 4 of this half-yearly financial information.

The outcome of this review is that the Directors are satisfied that the Society and the Group have adequate resources to continue in business and meet their liabilities throughout the period of assessment. Accordingly the financial statements of the Group have been prepared on a going concern basis with no material uncertainties that the going concern basis of accounting is appropriate.

Restatement

As disclosed in the Group's Annual Report and Accounts 2017, the Group no longer recognises any net defined benefit asset with respect to pensions on its balance sheet. The 30 June 2017 balance sheet presented in this interim report is therefore restated to reflect retrospective derecognition of the pensions surplus of £2.2m net of any associated deferred tax.

3. Accounting policies

The half-yearly financial information has been prepared on the basis of the accounting policies adopted for the year ended 31 December 2017, as described in those financial statements, except for the following key developments:

IFRS 15 Revenue from contracts with customers superseded IAS 18 Revenue from 1 January 2018 and established principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. The standard moved focus from risks and rewards, to the transfer of control of goods or services at either a point in time or over time. IFRS 15's core principle is that revenue should be recognised in relation to the transfer of goods or services to customers in an amount that reflects the consideration that is expected in exchange for those goods or services.

The primary impact of IFRS 15 is to the Group's Solutions business and has not had a significant impact on the Society or Group's pattern of income recognition. IFRS 15 does introduce expanded disclosure requirements, first applicable to these financial statements. Accordingly, the Group presents its interim IFRS 15 disclosures in the notes to this half year announcement. IFRS 9, in precedence to IFRS 15, dictates the accounting for revenue linked to most financial instruments, including the Group's mortgages and shares.

IFRS 9 Financial instruments superseded IAS 39 Financial Instruments from 1 January 2018, impacting the Group's classification and measurement, impairment and hedge accounting for financial instruments. While the Group was broadly unaffected by IFRS 9's classification and unaffected by IFRS 9's measurement requirements as the previous IAS 39 and current IFRS 9 accounting requirements are similar across similar classifications, the Group's accounting policies for financial instruments have been updated to reflect the specific requirements of IFRS 9 as follows:

Classification of financial assets is based on the cash flow characteristics of the assets and the business model under which the assets are held. Assets may be classified at amortised cost, fair value through other comprehensive income and fair value through profit or loss.

Amortised cost
Where the contractual cash flow characteristics of an asset reflect "solely payments of principal and interest on the principal amount outstanding" (SPPI), an asset may be classified at 'amortised cost', with income recognised under the effective interest rate method, where the asset's objective business model is 'held to collect contractual cash flows'. Cash flows are typically deemed to be SPPI in nature where there is a pre-determined date of repayment and where interest on the underlying financial assets is analogous to interest on 'simple debt instruments'- dominated by compensation for credit risk, the time value of money and a profit margin.

In assessing the business model applicable to its financial assets, the Society has considered how financial asset performance is evaluated and reported to senior management, the key risks affecting this performance and how these are managed, and how managers of the business are compensated in respect of asset performance. This analysis was undertaken at a more granular level than is presented in the Group's Balance Sheet or Notes to the Accounts.

The Society operates under a simple and straightforward building society model and does not trade in financial instruments. This allows for a more objective assessment of the business model under which financial assets are managed as typically there is no history, appetite or expectation that the Society will 'sell' its financial assets. Similarly, there is no compensation paid to staff with respect to fair value gains and no risk reporting geared at the speculative realisation of profit.

• The Society's core business of mortgage lending is undertaken with a view to long term recovery of contractual cash flows. Interest charged on mortgage lending and subsequent mortgage cash flows are agreed by the Society's Mortgages and Savings Committee and calculated to ensure that the 'time-value of money' and the credit risk that lending exposes the Society to is adequately compensated via the interest rates agreed.
• The Society's non-mortgage lending, typically loans and advances to banks, is similarly undertaken with a view to recovery of contractual cash flows and with interest charged that meets the SPPI requirements.
• The Society's cash balances, where interest generative, are held to collect contractual interest flows (and to ensure appropriate liquidity is on hand to meet the Society's liabilities as they fall due).
• The Society's trade receivables, whether due from third parties or intra-group companies, are held to collect the contractual cash balances as they fall due. The Society does not engage in debt factoring activities.

Fair value through other comprehensive income
Where the contractual cash flow characteristics of an asset reflect SPPI, an asset may be classified at 'fair value through comprehensive income' with fair value movements recognised through other comprehensive income, where the asset's objective business model is 'held to collect contractual cash flows, or for sale'.

While the Group does not trade in financial instruments, it is required to demonstrate the liquidity through regular sales of instruments in its debt security portfolio (held for liquidity purposes and to generate an interest income return that typically exceeds the interest return on cash or Bank of England reserve account holdings). This requirement, while regulatory in nature, is sufficient to indicate a business model conclusion that the assets are held to collect contractual cash flows, 'or for sale'. The Group's primary debt security holdings are in covered bonds, residential mortgage backed securities (RMBS) and government gilts. Each attract a rate of interest analogous with a simplified debt instrument (the Society assessing that the interest rate receivable is sufficiently compensating for the time value of money and perceived credit risk inherent in each investment). The Group's current treasury policy ensures that investment in RMBS is at a sufficiently 'senior secured' level to conclude that RMBS cashflows continue to meet the SPPI requirements.

Fair value through profit or loss
Where the contractual cash flow characteristics of an asset do not reflect SPPI, or where neither of the above business models suitably reflect management of the asset, an asset is to be classified at 'fair value through profit or loss', with fair value movements recognised through the Income Statement. The Group's derivative

financial instruments are classified at fair value through profit or loss. The Group has not otherwise elected to hold at fair value through profit or loss financial assets it could otherwise have held at amortised cost or fair value through comprehensive income.

A small number of cash-based financial assets previously held at amortised cost are held at fair value through profit or loss under IFRS 9 due to either the indeterminate timing of cash flows or failing the SPPI requirements.

The Group's IFRS9 impairment policy is discussed in detail on pages 17 to 19 of this half yearly financial information.

4. Principal Risks and Uncertainties

The Group's activities expose it to a variety of risks: market risk (predominantly interest rate risk), credit risk, liquidity risk and operational risk. There have been no changes in the principal risks and uncertainties facing the Group and no significant changes to these risks are currently expected in the second half of the year.

The interim condensed consolidated financial information does not include all risk management information and disclosures required in the annual financial statements, and should be read in conjunction with the Group's Annual Report and Accounts for December 2017.

There have been no material changes to the Group's risk appetite.

5. Taxation

The effective tax rate is 19.0% (2017: 19.25%). The tax charge has been calculated as far as possible to approximate to the expected full year tax rate and includes an adjustment to deferred tax assets, and to current tax for changes in the enacted corporation tax rate.

6. Related Party Transactions

During the 6 months to 30 June 2018 the Society purchased £8.3m (2017: £7.0m) of Business Support Services from Newcastle Strategic Solutions Limited (NSSL) and £2.0m (2017: £2.2m) Managed IT and Property Services from Newcastle Systems Management Limited (NSML), both wholly owned subsidiary companies. The Society received £11.8m (2017: £6.3m) from NSSL and £0.5m (2017: £0.5m) from NSML for the provision of financial and administrative services during the same period. For further detail see Note 29 of the Newcastle Building Society Annual Report and Accounts 2017.

7. Revenue from Contracts with Customers

	Unaudited 6 months to 30 Jun 18 £m	Unaudited 6 months to 30 Jun 17 £m	Audited 12 months 31 Dec 17 £m
Interest and similar income	36.0	31.9	65.6
Revenue from contracts with customers			
Solutions business:			
Savings - management services	11.4	10.9	21.8
Savings Management - project and change services	0.7	0.5	1.1
IT services	0.3	0.4	1.0
Member Business:			
Regulated advice services	2.0	1.9	3.8
Third party services	0.4	0.5	0.9
Total revenue from contracts with customers	**14.8**	**14.2**	**28.6**
Other income (non IFRS15)	1.3	1.6	3.1
Total Revenue	**52.1**	**47.7**	**97.3**

In accordance with IFRS 8, 'Operating Segments', the Group reports the following segments; Member business and Solutions business. When the Group prepares financial information for management, it disaggregates revenue by segment and service type.

The table above illustrates the disaggregation of revenue in scope of IFRS 15, 'Revenue from Contracts with Customers'. Revenue from customers with contracts generated by the Solutions business and the Member business can be seen in “Other income and charges” within the Segment information note. During the 6 months to 30 June 2018 other charges included in “Other income and charges” were £1.3m (30 June 2017: £1.5m, 31 December 2017: £2.9m).

8. Segment information

The chief operating decision maker has been identified as the Board of Directors. The Board reviews the Group’s internal reporting in order to assess performance and allocate resources. Management has determined the operating segments based on these reports. Following the management approach of IFRS 8, operating segments are reported in accordance with the internal reporting provided to the Board of Directors. The operating segments used by the Group meet the definition of a reportable segment under IFRS 8.

The ‘Member business’ segment provides mortgage, savings, investment and insurance products to Members and customers. The ‘Solutions business’ segment (that includes subsidiaries Newcastle Strategic Solutions Limited and Newcastle Systems Management Limited) provides business to business services through people, processes and technology. The Board assesses performance based on profit before tax after the allocation of all central costs. Operating profit before impairments, provisions and exceptional items is also assessed as this provides information on underlying business performance.

Income and directly attributable costs are allocated to each segment and support costs are apportioned, based on direct salary costs and detailed allocations by budget holders.

6 months to 30 June 2018	Member Business £m	Solutions Business £m	Total £m
Net interest receivable	16.0	-	16.0
Other income and charges	2.3	12.5	14.8
Administrative expenses	(13.1)	(9.0)	(22.1)
Depreciation	(0.9)	(0.6)	(1.5)
Operating profit before impairments, provisions and exceptional items	**4.3**	**2.9**	**7.2**
Impairment charges on loans and advances to customers	(0.2)	-	(0.2)
Provisions for liabilities and charges	(0.1)	-	(0.1)
Profit for the period before taxation	**4.0**	**2.9**	**6.9**
Taxation expense			(1.3)
Profit after taxation for the financial period			**5.6**

6 months to 30 June 2017	Member Business £m	Solutions Business £m	Total £m
Net interest receivable	13.6	-	13.6
Other income and charges	2.4	11.9	14.3
Administrative expenses	(12.1)	(8.4)	(20.5)
Depreciation	(0.6)	(0.6)	(1.2)
Operating profit before impairments, provisions and exceptional items	**3.3**	**2.9**	**6.2**
Impairment charges on loans and advances to customers	(0.2)	-	(0.2)
Provisions for liabilities and charges	(0.9)	-	(0.9)
Exceptional gain on purchase of Cobalt Offices	2.1	-	2.1
Profit for the period before taxation	**4.3**	**2.9**	**7.2**
Taxation expense			(1.4)
Profit after taxation for the financial period			**5.8**

Year to 31 December 2017	Member Business £m	Solutions Business £m	Total £m
Net interest receivable	29.1	-	29.1
Other income and charges	5.6	23.2	28.8
Administrative expenses	(26.4)	(16.6)	(43.0)
Depreciation	(1.7)	(1.1)	(2.8)
Operating profit before impairments, provisions and exceptional items	**6.6**	**5.5**	**12.1**
Impairment charges on loans and advances to customers	(0.2)	-	(0.2)
Provisions for liabilities and charges	(1.0)	-	(1.0)
Exceptional gain on purchase of Cobalt Offices	2.2	-	2.2
Profit for the period before taxation	**7.6**	**5.5**	**13.1**
Taxation expense			(2.2)
Profit after taxation for the financial period			**10.9**
Total Assets	**3,745.3**	**16.8**	**3,762.1**

9. Fair value measurement

The following table summarises the fair value measurement basis used for assets and liabilities held on the Balance Sheet at fair value at 30 June 2018.

	Level 1	Level 2	Level 3	Total
	£m	£m	£m	£m
Financial assets				
Debt securities – Fair value through other Comprehensive income	326.4	-	-	326.4
Derivative financial instruments	-	5.0	-	5.0
Fair value adjustments for hedged risk on underlying instruments	-	183.0	-	183.0
Financial liabilities				
Derivative financial instruments	-	186.6	-	186.6
Fair value adjustments for hedged risk on underlying instruments	-	0.8	-	0.8

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability either directly (i.e. as price) or indirectly (i.e. derived from prices).

Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

These definitions have been taken from the March 2009 amendment to IFRS 13 'Improving Disclosures: Financial Instruments'.

There were no transfers between levels in the period.

Debt securities issued by the Society held on balance sheet at their amortised cost of £1.0m at 31 December 2017 were repaid in full during the 6 months to 30 June 2018.

10. IFRS 9 Financial Instruments

The Group first applied the accounting requirements of IFRS 9 on 1 January 2018. Under IFRS 7, Financial Instruments: Disclosures, the Group is required to disclose quantified and qualitative information in this half-year report to detail the impact that transition to IFRS 9 has had between 31 December 2017 and 1 January 2018. As disclosed in the 2017 Annual Report and Accounts, the Group's closing IAS 39 balance sheet on 31 December 2017 and its opening balance sheet at the start of 1 January 2018 under IFRS 9 was as follows:

Balance sheet Assets	**Balance at 31 December 2017* £m**	**In scope for IFRS 9?**	**In scope for IFRS 9 impairment?**	**Current IAS 39 accounting classification**	**Agreed IFRS 9 accounting classification**	**Classification and measurement impact**
Cash and balances with the Bank of England						
Balances with the Bank of England	176.9	**Yes**	**Yes**	AC	AC	None
Bank of England cash ratio deposit	3.4	**Yes**	**No**	AC	FVTPL	Limited. Fair value and amortised cost equivalent in value.
Physical cash	1.7	**Yes**	**No**	AC	AC	None
Loans and advances to banks						
Loans and advances to banks (collateral pledged)	226.1	**Yes**	**No**	AC	FVTPL	Limited. Fair value and amortised cost equivalent in value.
Loans and advances to banks (non-collateral pledged)	1.6	**Yes**	**Yes**	AC	AC	None
Debt securities						
Gilts	84.8	**Yes**	**No**	AFS	FVOCI	Limited: Fair value through other comprehensive income is the equivalent of Available for sale
Residential mortgage backed securities	157.2	**Yes**	**Yes**	AFS	FVOCI	
Covered bonds	138.1	**Yes**	**Yes**	AFS	FVOCI	
Derivative financial instruments						
Interest rate swaps	4.9	**Yes**	**No**	FVTPL	FVTPL	None
Loans and advances to customers						
Prime residential	1,723.2	**Yes**	**Yes**	AC	AC	None
Buy-to-let	186.5	**Yes**	**Yes**	AC	AC	None
Equity release	209.9	**No**	**No**	n/a IFRS 4 insurance contract	n/a IFRS 4 insurance contract	Equity release mortgages are not in IFRS 9 scope. IFRS 4 accounting approximates IAS 39 accounting and provisioning methodology.
Policy loans	4.4	**Yes**	**Yes**	AC	AC	None
Housing association	498.0	**Yes**	**Yes**	AC	AC	None
Commercial (including commercial residential)	64.2	**Yes**	**Yes**	AC	AC	None
Serviced apartments	21.1	**Yes**	**Yes**	AC	AC	None
Fair value adjustments for hedged risk						
Fair value adjustments for hedged risk	206.2	**Yes**	**No**	FVTPL	FVTPL	None
Investment in subsidiaries						
Investment in subsidiaries	(nil on a group basis)	**No**	**No**	n/a	n/a	n/a, out of scope
Property, plant and equipment						
Property, plant and equipment	38.8	**No**	**No**	n/a	n/a	n/a, out of scope
Deferred tax assets						
Deferred tax assets	3.2	**No**	**No**	n/a	n/a	n/a, out of scope
Retirement benefit asset						
Retirement benefit asset	-	**No**	**No**	n/a	n/a	n/a, out of scope
Other assets						
Trade and other receivables	11.9	**Yes**	**Yes**	AC	AC	None

Balances as at 31st December 2017 are net of IAS39 provisions. The quantified impact of classification and measurement at 31st December 2017 is £nil.
*No measurement changes would have arisen between 31 December 2017 and 1 January 2018 if IAS 39 had been applied to both periods.
* No balances were reclassified into the amortised cost category as a result of transition to IFRS 9.
* No balances were reclassified out of the fair value through profit and loss category as a result of transition to IFRS 9.
In the table above the following abbreviations are relevant: AC – amortised cost, FVTPL – fair value through profit or loss and FVOCI – fair value through other comprehensive income.

Impairment

IFRS 9 replaced the IAS 39 ‘incurred losses’ provisioning model with a forward looking assessment of impairment. Expected credit losses are recognised across applicable financial assets (as detailed in the table above) based on whether there has been a significant increase in credit risk since the asset’s origination.

Loss allowances for expected credit losses are recognised on all financial assets held at either amortised cost, in which case loss allowances impact the Income Statement, or at fair value through other comprehensive income, in which case loss allowances impact other comprehensive income and become reserves reductions. A simplified approach has been adopted for trade receivables and contract assets.

Loss allowances against in-scope assets are recognised differently depending upon the initial credit risk of the assets at their origination, and the movement in said credit risk up to the current reporting date.

Assets can be assessed on an individual or collective basis and assessment should consider forward looking information.

When assessing movement in credit risk it is the change in the risk of default occurring that is key, not the change in the amount of any expected credit loss.

Scenarios are modelled to determine 12 month and lifetime expected credit losses against assets. Multiple scenarios to allow a probability weighted outcome are expected and while it is not necessary to identify every scenario, and it is advised not to select unlikely scenarios, the International Accounting Standards Board still expect at least one scenario to be included that is ‘expecting to default’, even if historically or presently there is no indication that a default will occur.

Where an asset has not seen a significant increase in credit risk since its origination (‘Stage 1 assets’), 12 month expected credit losses are recognised as a loss allowance. These are the portion of lifetime expected credit losses that result from default events on the asset that are possible within the 12 months after the reporting date.

Where an asset has seen a significant increase in credit risk since origination, but there is no objective evidence of impairment at the reporting date (‘Stage 2 assets’), lifetime expected credit losses are recognised. Where an asset has seen significant increase in credit risk since origination and there is objective evidence of impairment at the reporting date (‘Stage 3 assets’), lifetime expected credit losses are recognised and interest income is to be calculated against the net carrying amount of the financial asset, rather than the typical gross amount.

Forward looking assessments of financial assets are undertaken to support the loss allowances recognised against assets expected to default at any point in their lifetime (or within 12 months for stage 1 assets). IFRS 9’s multiple, forward looking scenarios have brought forward to ‘now’ the recognition of future potential losses.

Implementation of high quality IFRS 9 impairment models requires significant management experience and judgement, both in assessing historic performance trends and factors and in projecting these into uncertain future economic environments. External professional modelling assistance has been coupled with the Society’s extensive internal expertise to facilitate a robust and compliant implementation. Best practice guidance issued by consolidated professional audit and accountancy firms, IFRS implementation guidance, and banking centric governance and modelling guidance from European and domestic authorities form the foundation of the Society’s IFRS 9 impairment response.

IFRS 9 Qualitative Impairment Impact

Residential and new Buy to Let Mortgages

IFRS 9 has had minimal impact on the Group’s mortgage provisions. The Group’s core lending, to prime residential and high quality buy to let customers is considered to be of low risk and securely collateralised. The Group continues to experience historic low levels of arrears and does not lend in excess of 95% LTV (75% LTV for Buy to Let). With the Group holding the first legal charge over the mortgaged property against which it lends, this protects the Group from borrower default as proceeds from the sale of any property are first used to extinguish the Group’s exposure to its borrowers.

Historically, the Group has provided prudently against its overdue residential lending: providing for the full amount of expected loss, as assessed at a provisioning Committee level, against mortgages falling into arrears of three months or more.

Under IFRS 9, the Group's residential and new buy to let provisioning is informed by tailored IFRS 9 provisioning models. The models allow a consistent assessment of mortgage assets, operating as follows:

Staging

• At the application stage, a prospective borrower's credit risk is assessed. The Society does not lend to high risk customers but will lend to 'prime customers' who can fall under a range of 'application scores'- based on a wide variety of factors including affordability, credit history, committed monthly spend, etc. A borrower's application score gives a quantified assessment of borrower risk- a 'risk score'.
• On a quarterly basis, the Group receives borrower credit scores from Experian, an industry leader in the provisioning of consolidated credit scoring information. This data is mapped internally to a new borrower risk score– allowing continuous assessment of the movement in borrower risk since origination.
• Where a borrower's risk score is suitably consistent between origination and the reporting date, a borrower is categorised as a 'stage 1' borrower.
• Where a borrower's risk score increases past pre-defined internal thresholds, but a borrower has not otherwise 'defaulted', the borrower is categorised as a 'stage 2' borrower. A borrower who has fallen into >1 month's arrears is automatically considered to be a stage 2 borrower.
• A borrower who has defaulted, (assessed against a range of internal qualitative and quantitative criteria) is categorised as a 'stage 3' borrower. A borrower who has fallen into >3 month's arrears is automatically considered to be a stage 3 borrower.

Default indicators and Probability of default (PD)

The Society calculates, for each mortgage exposure, a forward view as to how likely that mortgage is to default at some point over its expected life. The probability that a mortgage will default is not 'point in time'- the Society has to calculate a continuous and forward looking assessment of the probability of default as IFRS 9's base expectation is that 'lifetime' expected credit losses will be provided for (or 12 month expected losses for stage 1 assets).

Lifetime expected credit losses are calculated by the Society as the discrete losses that would likely be incurred (considering mortgage exposure vs. the expected sale value of the mortgaged property) if a mortgage defaulted on any of a large range of future dates. Each discrete provision needs to be assigned a probability of default weighting in order to calculate one overall 'lifetime' expected credit loss. As such, a continuous forward view to the probability of default must be calculated.

The Society calculates its probability of default as follows:
• The Society has undertaken a detailed assessment of more than 12 years of its internal credit risk data to determine the core factors that lead to borrower default.
• Default indicators identified included granting of forbearance, evidence of mortgage fraud, borrowers falling into > 3 months arrears, borrower insolvency or bankruptcy and voluntary repossession of property. These are used in the staging assessment above to assist in the classification of borrowers as stage 1, stage 2 or stage 3.
• The Society's assessment also considered 'wider' patterns of default, analysing historic borrower defaults by their maturity (how long a mortgage had been held by the Society), vintage (during which original time period the Society lent to a borrower) and considering 'exogenous' (external factors including the interest rate environment, unemployment rates, UK (nominal) GDP, House Price Index, etc.) factors in play at the time of default.
• The exogenous, maturity and vintage (EMV) factors are used to derive point in time and forward looking probability of default curves: projecting historical information about defaults suffered under known 'EMV conditions' forward in combination with the Society forward views on the wider macroeconomic environment (as this will influence the forward view on how exogenous factors may develop over time). In combination, these curves form the Society's forward looking probability of default curve, as calculated under the 'EMV' model.

Exposure at default (EAD)

• The Group projects mortgage balances forward to give an estimate of each borrower's mortgage balance over time. This factors in forecast interest additions and expected borrower payments alongside an estimate of the value of each borrower's property collateral throughout a long term forecast. An adjustment is made to uplift the Group's exposure to borrowers to simulate a typical borrower default of 3 missed monthly payments plus typical fees associated with arrears.
• The output is a per-mortgage forward projection of mortgage balances.

Loss given default (LGD)

• The Group calculates a per-mortgage 'loss given default' (LGD), an estimate of the proportion of each mortgage loan exposure that is believed to be at risk if the borrower defaults on their obligation to repay the outstanding capital and interest and the property is subsequently possessed and sold.

• LGD is calculated as the probability of possession given the default of a borrower (PPD) which estimates the likelihood of possession following default multiplied by the expected shortfall on each mortgage: an estimation of the difference between the exposure at default (as discussed above) and the sale price of the property, net of relevant sales costs.

*Provisions: PD * EAD * LGD*
The Group then calculates a final provision for each mortgage: the probability of default multiplied by the amount the Group expects to lose in the event of a default. As discussed above, this is not 'static' or a 'point in time' loss: the Group calculates PD, EAD and LGD across a continuous forward planning horizon. The final provision number is not a singular PD*EAD*LGD, it reflects the discounted overall expected loss that could be incurred over the life of each mortgage: a weighted average of multiple possible future loss events.

Multiple economic scenarios
IFRS 9 expects more than one scenario to be considered when calculating expected credit losses. The Society applies this principle by assessing the provisions required under three separate macroeconomic forecasts. These macroeconomic forecasts feed into the exogenous component of the Society's EMV models.

The Society runs:
• Base scenario: calculated with reference to the Bank of England's quarterly forecasts, and in line with budgets;
• Upside scenario: a positively stressed variant to the base scenario; and
• Downside scenario: a negatively stressed variant to the base scenario.

The Society's final expected credit losses are the losses calculated under each discrete scenario multiplied by a 'likelihood factor': currently set to 80% for the base scenario and 10% for each of the upside and downside scenarios.

Legacy mortgages
Specialist internal departments assess the risk of loss against the Group's legacy mortgage books on a case by case basis. Across the Society's historically highest risk exposures, commercial real estate, this includes the annual completion of tailored risk grade scorecard designed to encompass the key characteristics contributing to underlying risk.

Each of the scorecard risks are weighted to provide a final 'weighted risk score' for the loan, which categorises the loan in terms of likelihood of failure in a moderate or severe recessionary scenario. The risks that carry the highest weightings relate to tenant failure and serviceability.

Exposures receiving the highest overall risk scores are placed onto the Society's 'borrower watchlists' prompting enhanced and more frequent internal scrutiny.

All payments due are monitored on a real-time basis. In the event of a late payment the position is reviewed immediately and appropriate action taken. The facility is then closely monitored.

IFRS 9 Quantitative Impairment Impact
The impact of IFRS 9's staging and consequent loss provisioning to the Society's closing 31 December 2017 balance sheet was as follows:

	IFRS 9 Gross Exposure									
	Stage 1			**Stage 2**			**Stage 3**			**Total**
	Of which Months in Arrears			Of which Months in Arrears			Of which Months in Arrears			
	< 1	1-3	> 3	< 1	1-3	> 3	< 1	1-3	> 3	
	£m	£m	£m	£m	£m	£m	£m	£m	£m	**£m**
Prime residential	1,564.8	-	-	155.8	15.0		3.9	1.1	6.8	**1,747.4**
Buy to Let	175.8	-	-	10.6	-	-	0.2	-	-	**186.6**
Commercial	32.6	-	-	-	0.1	-	15.0	-	-	**47.7**
Housing Association	498.0	-	-	-	-	-	-	-	-	**498.0**
Serviced Apartments	21.1	-	-	-	-	-	-	-	-	**21.1**
Policy loans	4.2	-	-	0.6	-	-	-	-	-	**4.8**
Total	**2,296.5**	**-**	**-**	**167.0**	**15.1**	**-**	**19.1**	**1.1**	**6.8**	**2,505.6**

	Expected Credit Losses									
	Stage 1			**Stage 2**			**Stage 3**			**Total**
	Of which Months in Arrears			Of which Months in Arrears			Of which Months in Arrears			
	< 1	1-3	> 3	< 1	1-3	> 3	< 1	1-3	> 3	
	£000	£000	£000	£000	£000	£000	£000	£000	£000	**£000**
Prime residential	83.7	-	-	101.7	29.4		103.2	9.5	237.7	**565.2**
Buy to Let	0.7	-	-	2.7	-	-	0.4	-	-	**3.8**
Commercial	1,322.0	-	-	-	-	-	7,598.0	-	-	**8,920.0**
Housing Association	-	-	-	-	-	-	-	-	-	**-**
Serviced Apartments	-	-	-	-	-	-	-	-	-	**-**
Policy loans	-	-	-	360.6	-	-	-	-	21.8	**382.4**
Total	**1,406.4**	**-**	**-**	**465.0**	**29.4**	**-**	**7,701.6**	**9.5**	**259.5**	**9,871.4**

The impact of IFRS 9’s staging and consequent loss provisioning to the Society’s closing 30 June 2018 balance sheet was as follows:

	IFRS 9 Gross Exposure									
	Stage 1			**Stage 2**			**Stage 3**			**Total**
	Of which Months in Arrears			Of which Months in Arrears			Of which Months in Arrears			
	< 1	1-3	> 3	< 1	1-3	> 3	< 1	1-3	> 3	
	£m	£m	£m	£m	£m	£m	£m	£m	£m	**£m**
Prime residential	1,614.5	-	-	142.6	15.5	-	3.6	1.7	6.7	**1,784.6**
Buy to Let	193.3	-	-	11.5	0.4	-	0.2	-	-	**205.4**
Commercial	29.3	-	-	-	-	-	13.0	-	0.1	**42.4**
Housing Association	466.6	-	-	-	-	-	-	-	-	**466.6**
Serviced Apartments	19.8	-	-	-	-	-	-	-	-	**19.8**
Policy loans	3.6	-	-	0.3	0.2	-	-	-	-	**4.1**
Total	**2,327.1**	**-**	**-**	**154.4**	**16.1**	**-**	**16.8**	**1.7**	**6.8**	**2,522.9**

	Expected Credit Losses									
	Stage 1			**Stage 2**			**Stage 3**			**Total**
	Of which Months in Arrears			Of which Months in Arrears			Of which Months in Arrears			
	< 1	1-3	> 3	< 1	1-3	> 3	< 1	1-3	> 3	
	£000	£000	£000	£000	£000	£000	£000	£000	£000	**£000**
Prime residential	43.1	-	-	139.8	42.4	-	29.1	18.9	278.4	551.7
Buy to Let	1.4	-	-	3.8	0.6	-	0.4	-	-	6.2
Commercial	1,322.0	-	-	-	-	-	7,532.1	-	-	8,854.1
Housing Association	-	-	-	-	-	-	-	-	-	-
Serviced Apartments	-	-	-	-	-	-	-	-	-	-
Policy loans	-	-	-	189.2	-	-	-	-	-	189.2
Total	**1,366.5**	**-**	**-**	**332.8**	**43.0**	**-**	**7,561.6**	**18.9**	**278.4**	**9,601.2**

Debt securities

The Society’s debt security holdings are all of ‘investment grade’ or higher. The Society has therefore assessed that the credit risk on its debt security exposures has not increased significantly since initial recognition.

The Society’s treasury risk department runs very severe annual stressed scenarios over the Society’s residential mortgage backed securities (RMBS). The Society’s policy to allow only investment grade and senior secured exposures leaves the Society highly insensitive to stressed scenarios as the ‘waterfall structure’ of RMBS payments ensures continued Society receipt of contractual cash flows even through significantly stressed scenarios.

The Society's covered bond exposures are similarly resilient: the Society is only exposed to regulated UK covered bonds with the regulations providing for the full segregation of covered bond asset pools from the bond issuer. The regulations introduce numerous investor protections including mandatory over-collateralisation, an extensive initial application process and regular regulatory stress testing and supervisory monitoring.

As a result, the Society was not significantly impacted by the IFRS 9 impairment requirements with respect to its debt security exposures. No provisioning was required at 31 December 2017, 1 January 2018 or 30 June 2018.

Trade and other receivables

The company has elected to take advantage of IFRS 9's practical expedient when assessing the accounting impairment applied to its trade receivables. Lifetime expected credit losses are therefore provided against all trade receivables. A provisions matrix approach, where provisions against receivables are calculated as an increasing percentage of the receivable balance, rising as receivables fall further overdue, has been adopted.

Assessment of the appropriate provision percentages has been made in line with the company's historic trade receivable recovery. Where appropriate, forward looking views to recovery will also be incorporated.

The Society was not significantly impacted by the IFRS 9 impairment requirements with respect to its trade and other receivables. £30,000 was provided at 31 December 2017 and 1 January 2018. At 30 June 2018 £28,934 was provided.

Impairment Conclusion

The overall quantified impact of IFRS 9 to the Group's provisions compared to the existing IAS 39 provisions at 31 December 2017 was not material.

Hedge Accounting

IFRS 9's hedging requirements did not have significant impact to the Society's hedging activities, serving broadly to relax a number of the IAS 39 hedging criteria.

The Society has elected to adopt IFRS 9's hedging requirements for its non-macro hedges at 1 January 2018 and continues to apply the IAS 39 hedging requirements to its macro hedge portfolio.

Statement of Directors' responsibilities

The Directors confirm that this condensed consolidated half-yearly financial information has been prepared in accordance with IAS 34 as adopted by the European Union, and that the half-yearly management report herein includes a true and fair review of the information required by the Disclosure and Transparency Rules (DTR 4.2.4, DTR 4.2.7 and DTR 4.2.8).

The Society's Home Member State is the United Kingdom.

The Directors of Newcastle Building Society are listed in the Annual Report for 2017. Angela Russell, Deputy CEO and Finance Director, retired at the conclusion of the Annual General Meeting on 25 April 2018. There were no other changes to the Board in the period.

On behalf of the Board

Andrew Haigh
Chief Executive
30th July 2018

Independent review report to the Directors of Newcastle Building Society

Report on the condensed consolidated interim financial statements

Our conclusion
We have reviewed Newcastle Building Society's condensed consolidated interim financial statements (the "interim financial statements") for the 6 month period ended 30 June 2018. Based on our review, nothing has come to our attention that causes us to believe that the interim financial statements are not prepared, in all material respects, in accordance with International Accounting Standard 34, 'Interim Financial Reporting', as adopted by the European Union.

What we have reviewed
The interim financial statements comprise:

- the summary consolidated balance sheet position as at 30 June 2018;
- the summary consolidated income statement and summary consolidated statement of comprehensive income for the period then ended;
- the summary consolidated cash flow statement for the period then ended;
- the summary consolidated statement of movement in members' interests for the period then ended; and
- the explanatory notes to the interim financial statements.

The interim financial statements included in the announcement of half year results have been prepared in accordance with International Accounting Standard 34, 'Interim Financial Reporting', as adopted by the European Union.

As disclosed in note 2 to the interim financial statements, the financial reporting framework that has been applied in the preparation of the full annual financial statements of the Group is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Responsibilities for the interim financial statements and the review

Our responsibilities and those of the directors
The announcement of half year results, including the interim financial statements, is the responsibility of, and has been approved by, the directors.

Our responsibility is to express a conclusion on the interim financial statements based on our review. This report, including the conclusion, has been prepared for and only for the directors of the Society as a body, for management purposes, in connection with interim review and for no other purpose. Our report may not be made available to any other party without our prior written consent. We do not, in giving this conclusion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What a review of interim financial statements involves
We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 and 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.

A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK) and, consequently, does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.
We have read the other information contained in the announcement of half year results and considered whether it contains any apparent misstatements or material inconsistencies with the information in the interim financial statements.

PricewaterhouseCoopers LLP
Chartered Accountants
Newcastle upon Tyne
30 July 2018