London Stock Exchange

RNS Final Results

Final Results

COVENTRY BUILDING SOCIETY

Released 07:00:09 04 March 2021

RNS Number : 1073R
Coventry Building Society
04 March 2021

4 March 2021

Coventry Building Society delivers a resilient performance, providing outstanding service to members and investing for the future.

Commenting on these results, Steve Hughes, Chief Executive Coventry Building Society, said:

I was immensely proud to join the Society in April. 2020 was an unprecedented year as a result of the Covid-19 pandemic but we remained open for business, continuing to meet the needs of our members and customers and providing great service. We have continued to invest for the future while delivering a robust financial performance and we balanced the differing needs of borrowers, savers and those in financial difficulty. I am proud of my colleagues who have lived our values and our belief in putting members first.

Financial results for the 12 months ended 31 December 2020 include:

- **Mortgages:** Mortgage balances have increased by £1.2bn to £43.5bn.
- **Savings:** Savings balances increased by £1.9bn to £38.2bn.
- **Member value:** The average weighted savings rate paid to members was 1.18%, 0.55% higher than the average paid in the market and equivalent to an additional £197m in interest to savers[1].
- **Member outcomes:** The Society delivered outstanding service with a Net Promoter Score of +73[2] and supported 39,000 borrowers with payment holidays.
- **Profit:** Profit before tax was resilient at £124m (2019: £147m) after booking £36m of incremental provisions for potential future credit losses.
- **Capital and liquidity strength:** Common Equity Tier 1 (CET 1) ratio remains well above statutory requirements at 33.0% whilst the Society's Leverage Ratio on a UK modified basis increased to 4.6%. The Liquidity Coverage Ratio of 179% is also considerably above the regulatory minimum requirement.
- **Leading cost efficiency:** At 0.49%[4] the Society continues to report amongst the lowest cost to mean assets ratio of any UK building society, whilst continuing to invest significantly in its technology infrastructure and digital capability.
- **Outstanding employee engagement:** The Society has a 3 star rating for colleague engagement and was recognised for being 2nd in the Sunday Times Best Big Companies to Work For list.
- **Supporting communities:** Whilst face to face activity has been limited due to lockdown, we have increased emergency support for our community partners, tackling immediate needs and the longer term consequences of the pandemic. 43% of colleagues have been engaged in charitable activity over the last 12 months (2019: 82%).

AN UNPRECEDENTED YEAR

When I joined the Society at the end of April, the impacts of the Covid-19 pandemic were still emerging. Since then, the ongoing health crisis, combined with the economic and social impacts of ongoing lockdown restrictions have had a major impact on all our lives. I would like to thank all key workers across the country for all they have done during this time and my thoughts go out to everyone who has been impacted by the pandemic.

I am very proud of the way that my colleagues responded to the unprecedented disruption and their focus and dedication supporting our members and each other. I would like to thank them for their hard work during this time and for the warm welcome I have received in my first eight months.

The pandemic required us to change the way we worked and delivered our services. We kept our branches open, making them Covid-secure for our employees and customers. We increased resources in our customer service centres allowing more calls to be answered and invested in technology to allow the majority of our colleagues to work from home. We made improvements to our website to provide information and support for members who access their accounts online.

We helped 39,000 mortgage customers with payment holidays and we have worked with them so that they understand the impacts of the holiday on their future mortgage payments. We will continue to support those in financial difficulty once the payment holiday period ends.

The reduction in the Bank of England Base Rate reduced the income we earn from our mortgages and our liquidity investments. This required us to make some difficult short term decisions on savings and mortgage rates to protect the financial resilience of the Society which is in members' long term interest.

DELIVERING A RESILIENT PERFORMANCE

Despite the challenging environment, we maintained our industry leading service levels, grew our mortgage and savings balances and made good progress delivering our technology programmes. Our profit before tax, while lower year on year at £124 million (2019: £147 million), underpins our strong capital ratios, a key measure of our long term resilience.

Our mortgage growth of 3.0% (2019: 7.6%) was in line with the market growth rate[3]. This rate of growth is lower than previous years which reflects the effective closure of the housing market during the first lockdown, lower remortgaging activity and our concious decision to manage mortgage volumes at points in the year. Market activity picked up significantly in the second half of the year and we selectively increased our participation. We remain focused on lower risk, high quality secured mortgage lending with an average loan to value on loans originated in the year of 63.7% (2019: 63.7%).

Our savings balances increased by 5% (2019: 8.9%), compared with market household deposit growth of over 10%[3]. Our savings growth was ahead of the growth in mortgages but below the market where households held more of their balances in current accounts as the level of consumer spending fell. Our average savings rate fell to 1.18% (2019: 1.49%) following a 0.65% reduction in Bank of England Base Rate to 0.10% and compares favourably to a UK average savings rate of 0.63%[3]. This means that we paid additional interest of £197 million[1] to our savings members in 2020 (2019: £228 million) when compared to the market average. We cannot operate in isolation from the market but we are committed to providing value to our members.

The uncertain economic outlook, particularly in those industries most impacted by Covid-19, has led us to set aside an additional £36 million of provisions for potential future credit losses in our mortgage book, notwithstanding the fact that the book is low risk and continues to perform well with no significant losses to date.

Spending our members' money wisely and maintaining our relative cost efficiency is a key priority for us. In 2020 our cost to mean asset ratio remained broadly stable at 0.49%[4] (2019: 0.48%). Our total management expenses increased to £246 million (2019: £229 million) and the increase included additional spend on our technology and change programmes.

Our profit in the year has resulted in us maintaining our strong capital ratios. Our Common Equity Tier 1 ratio was 33.0% (2019: 32.0%), well above the regulatory minimum requirement. Our Leverage Ratio increased to 4.6% (2019: 4.4%[5]) and our Liquidity Coverage Ratio was 179% (2019: 214%). These metrics demonstrate the strength and stability of the organisation and underpin our desire to be a safe and secure home for our members' money.

INVESTING FOR THE FUTURE

The Society has a significant investment agenda and we have continued to make good progress on our change projects throughout the year. The pandemic has reinforced our understanding that consumers value choice, flexibility and simplicity in how they manage their financial needs.

Building strong technology infrastructure and operational resilience is a core element of our investment programme including new data centres, upgrading our databases and establishing a testing capability that will allow more agile and cost-effective change. Digitising our mortgage and savings business is a key strategic focus, allowing customers to self-serve, reducing our paper and other resource use and unlocking the potential for future partnerships. We delivered technology to support stronger online authentication in the first half of 2020. We have also started work on the foundations for future digital functionality for all of our channels. We aim to bring the best of our personal touch to a digital world and continue to offer customers choice around how they access our products and services.

Our members value the fantastic personal service we provide through branches and over the phone and we are continuing to invest in these channels. Our branch redesign programme was paused during the first lockdown, but we restarted this activity while ensuring that Covid-secure measures were in place and we redesigned four branches in 2020, with the considerable investment in our branches due to be completed by 2022. This coupled with investment in our brand will see us continue to build on our aim of being locally loved in our communities and also result in a brand that is also better recognised across the UK.

A FOCUSED STRATEGY WITH PURPOSE, MEMBERS AND OUR PEOPLE AT ITS CORE

It has been fantastic to engage with the Board and all 2,700 colleagues of setting the long term direction of the Society.

We have spent time focused on our purpose and the positive role we can play in society. It will drive our decision making, inform our strategy and will be the focus of our efforts for members, our communities and our environment. Our purpose of giving people the power to be better off through life means all our stakeholders will be better off because of the contribution of the Society.

We won't get everything right first time, but our purpose will be the standard to which we will hold ourselves. Unless we can demonstrate through our actions that people are better off trusting us with their savings and borrowing needs, better off working with us, and that we are contributing to a fairer and more sustainable wider society, then we will not be delivering our full potential and will not be acting in the long term interests of our membership or our society.

As a mutually owned building society we will always believe in putting our Members First. Providing a safe home for people's savings and enabling others to buy homes is what we have done throughout our long history and will continue to be at the core of what we do. In 2020 we have re-shaped our strategy and all of our colleagues have been engaged in this process. We have a clear ambition and have defined the priorities that we need to deliver on to achieve it.

This ambition is focused on being the best in our core markets of mortgages and savings with a clear focus on brilliant propositions meeting the needs of consumers, providing industry leading service, investing in our brand, our colleagues and providing members and customers choice through human or digital channels. Our values are built around the acronym CARES - Caring, Ambitious, Responsible, Empowering and Straightforward. These values recognise what has made the Society great but also look to the future - I see these values being lived by my colleagues every day and I know this is what our members and customers experience.

We look forward to sharing our progress on our strategic priorities as we move forward.

SUPPORTING OUR COLLEAGUES

We did not furlough any of our colleagues and we have worked to help our people impacted by the pandemic. Measures included extending our Carers Flex scheme to allow additional flexibility for those colleagues who have caring and childcare responsibilities and launching a service to allow all colleagues to access an online GP through video consultations. We have also launched an Employee Assistance Programme which provides a wellbeing hub and telephone counselling.

We responded quickly to new ways of working to enable our colleagues to serve members and run the Society safely. This included setting up equipment and technology to allow 75% of our office-based colleagues to work from home. We also transformed our branch and head office sites to ensure that these locations are Covid-secure. It was an incredible time to join a business having to try and build relationships and trust remotely but technology has been our friend and I have been able to virtually meet most of my 2,700 colleagues and have virtually visited all of our branches and operations. Engagement has been excellent and I have been able to get a real sense of the fantastic culture of the organisation and deep rooted belief of putting Members First.

Our colleagues continued to deliver excellent services to members throughout the year as measured by our Net Promoter Score[2] of +73 (2019: +74). We have also maintained high levels of colleague engagement as a 3* employer in the Sunday Times Best Large Companies to Work For list, achieving second place in the rankings in February 2020 as previously reported. It is also great to get external recognition for the fantastic service we provide and the quality of our products. To receive continued recognition from Fairer Finance for the simplicity and transparency of our products and from Which? for the quality of our service is testament to what we are about. I am immensely proud of these achievements.

We are committed to creating the right environment at the Society, one where everyone feels that they can belong. We have pledged to sign up to the Race at Work Charter in 2021 which is an important next step for us. The Society employs more women than men, but this mix reverses in senior leadership roles - we want to see that change. Likewise, our ambition is to see more ethnic diversity in our managerial population. I look forward to reporting our progress to you.

We continue to create employment opportunities with our apprenticeship and graduate offers, providing great development opportunities for our colleagues and adding to our capability across the organisation. It has been fantastic to meet all new joiners this year and see the talent and dynamism they will bring to our future.

The voice of our colleagues is important in supporting our decision making. My Society is a forum of 30 colleagues from around the business and is attended by Peter Ayliffe our Deputy Chair. They meet quarterly and have had the opportunity to engage in strategy development, engagement and remuneration matters and play an important part in informing Board decisions.

MAKING A DIFFERENCE IN OUR COMMUNITIES

Making a real difference to our communities and to wider society is really important to everyone at the Society. We have programmes that focus on financial education and employment skills, creating opportunity for young people, addressing food poverty and homelessness in our home city of Coventry and reducing loneliness and isolation in our communities.

The opportunities for our colleagues to be directly involved in community activity in 2020 were limited by the pandemic so we supported our communities in new and different ways. Supporting education and creating opportunity for young people is critical. We worked with schools to provide stationery to children studying at home. We launched a £50,000 grant scheme to help Coventry primary school pupils deliver additional maths support to help pupils after time out of traditional education during the year. We also moved our employability programme online so that we can offer this to pupils without face to face sessions.

The pandemic has heightened the social challenges our communities face. We increased funding to a number of charities across Coventry that provide food and shelter to those most in need. We also provided support to University Hospital Coventry & Warwickshire Charity, so it could increase support to its own employees and their patient's families. Our branches continue to support local causes as well as providing financial services to members and in doing so reduce loneliness and isolation for those who were unable to meet up with friends and family.

Our members continued to save in our Poppy Bonds savings product which resulted in a further £0.8 million donation to The Royal British Legion, bringing our support for the charity to almost £19 million. These donations make a real difference to current and former members of the armed forces and their families including benefit, debt and financial support and housing and employment support for those most in need.

We have focused and exciting plans for 2021 as we bring our purpose to life in our heartland and communities.

LOOKING AHEAD

2020 was an unprecedented year, impacting the health and lives of millions of people and also impacting the livelihoods of many others and the performance of the wider UK economy.

We expect the outlook to be uncertain for some time to come and we will continue to run the Society prudently. We aim to continue to provide brilliant service and good value to our members and customers with a strong focus on the wellbeing of our colleagues as well.

Our capital strength allows us to invest for the long term giving current and future generations flexible mortgage and savings propositions and genuine choice around how they access our products and services supported by great teams across our branches, contact centres and head offices. Capital is also needed to fund growth. Our resilience through previous periods of economic uncertainty gives us confidence we will continue to grow in the years ahead, supporting people who want to save and who want to buy their own homes and giving them the power to be better off through life.

I would like to thank our members, colleagues, customers and partners for their support and loyalty. I am delighted to have joined the Society and look forward to working with my colleagues to see the Society achieve its potential and fulfil its ambition.

---

1. The Society's average month end savings rate compared with the Bank of England average rate for household interest-bearing deposits on the Society's mix of products.
2. Net Promoter Score (NPS) is a measure of customer advocacy that ranges between -100 and +100 which represents how likely a customer is to recommend our products and services
3. Source: Bank of England
4. Administrative expenses, depreciation and amortisation/Average total assets.
5. During the year the Society has refined its calculation of this measure. Had this applied in 2019 the comparative would be 4.6%.

FINANCIAL REVIEW

INCOME STATEMENT

OVERVIEW

In 2020, the Society has faced significant challenges resulting from the pandemic and our focus has been on supporting members, customers and colleagues through these unprecedented times. Our results for the year are impacted by the following factors which relate to the pandemic:

- We have increased our provisions for future expected credit losses (ECLs) in the light of the continued uncertainty surrounding the future economic outlook.
- While our net interest income increased in the year, the 0.65% reduction in the Bank of England Base Rate in March had a negative impact on our net interest income.
- Mortgage growth, while in line with the market, has been moderated from previous years due to the significant economic uncertainty.

As a result, profits for the year have reduced to £124 million (2019: £147 million). This reflects a strong recovery in the second half of the year following profits reported in our Interim Financial Report to 30 June 2020 of £22 million.

The Society remains committed to providing long term sustainable value to members through competitively priced savings and mortgage products while ensuring we continue to invest to improve services and the long term resilience of your Society.

In running the Society we seek to balance the needs of our mortgage and savings members. As reported in our Interim Financial Report, the impact of the 0.65% reduction in the Bank of England Base Rate in March had the effect of reducing net interest income.

In order to mitigate the impact of this, we took the difficult decision to reduce the rates of interest paid to our savings members. The time lag between the Bank of England Base Rate changes and repricing savings rates reduced net interest income in the year by £18 million.

In overall terms, our net interest margin for the year reduced by 0.02% to 0.81% (2019: 0.83%). Of this reduction, 0.04% was due to the impact of the repricing following the Base Rate fall. This was offset by an increase of 0.02% relating to improving returns on our mortgage book. At 0.81%, our net interest margin has improved significantly from the 0.72% reported at the half year in line with our expectation that net interest margin would return towards 2019 levels.

Despite the reductions in savings rates, the Society has continued to pay favourable savings rates compared with the market average, balancing distribution of member value and the long term health and resilience of the Society. £197 million (2019: £228 million) of additional interest was paid to savings members as compared with average market rates[1].

Costs have increased £17 million to £246 million (2019: £229 million). Day-to-day operating costs increased by £11 million to £160 million (2019: £149 million) and spending on our strategic investment programme increased by £5 million to £57 million (2019: £52 million) with a further £1 million increase in the depreciation of previous investment.

The economic environment remains very uncertain and our expectations are for a rise in unemployment and house price falls in the period ahead. Notwithstanding the very strong asset quality and overall low risk nature of our balance sheet we recognised £36 million of additional provisions in the year for ECLs on the Society's mortgage portfolio. Significant judgement and estimation has been applied in calculating expected credit losses given the uncertain environment. More information on the ECL provision is set out below.

	2020 £m	2019 £m
Interest receivable	859.9	1,010.5
Interest payable	(451.4)	(613.8)
Net interest income	408.5	396.7
Other income	(0.1)	0.1
Losses on derivatives and hedge accounting	(0.7)	(17.2)
Total income	407.7	379.6
Management expenses	(245.6)	(229.1)
Impairment charge	(36.4)	(2.1)
Provisions	(0.5)	-
Charitable donation to Poppy Appeal	(0.8)	(1.2)

Profit before tax	124.4	147.2
Tax	(23.0)	(25.5)
Profit for the year	101.4	121.7

NET INTEREST INCOME

Net interest income has increased to £409 million (2019: £397 million) despite the Bank of England Base Rate reductions in March which reduced income by £18 million. This reduction was offset by an increase of £30 million due to growth and higher margins on our mortgage assets. There has also been a small reduction in future expected income recognised due to changes in customer behaviour. We will continue to assess the impact of changes in customer behaviour that occurs as a result of product and market developments.

NET INTEREST MARGIN

Net interest margin has decreased by 0.02% to 0.81%. This is the result of a reduction of 0.04% relating to the impact of the reduction in Bank of England Base Rate, partly offset by an increase of 0.02% reflecting an improvement in the margin on our mortgage book.

	2020 £m	2019 £m
Net interest income	409	397
Average total assets	50,515	47,801
	%	%
Net interest margin	0.81	0.83

DERIVATIVES AND HEDGE ACCOUNTING

The Society uses derivative financial instruments solely for risk management purposes to manage interest rate and currency risk arising from its mortgage and savings activity and from non-sterling, fixed rate wholesale funding. Over the last 12 months, the Society has continued to enhance its hedge accounting processes, in part to improve hedge effectiveness. The loss of £1 million for the year represents hedge ineffectiveness and fair value movements on derivatives where hedge accounting has not been obtained (2019: £17 million loss). These fair value movements represent timing differences and include adjustments to fair values as a result of Covid-19 related mortgage payment holidays.

MANAGEMENT EXPENSES

Overall management expenses have increased by £17 million or 7%. Of the £17 million increase in management expenses, day-to-day operating costs increased by £11 million to £160 million (2019: £149 million). The increase was due to salary and cost inflation, higher IT costs as investment programmes deliver and £4 million of costs incurred in response to the pandemic, including costs to facilitate remote working, personal protective equipment for colleagues and modifications to our branch and head office buildings.

Spending on our strategic investment programmes increased by 10%, or £5 million, to £57 million (2019: £52 million) with a further £1 million increase in depreciation of previous investment spend referenced in day-to-day operating costs above. Investment in the year has focused on a new mortgage platform, improving the resilience and security of our technology and some early investment in digital capabilities.

Running the Society efficiently remains at the heart of the Society's strategy enabling us to provide better value to members. The cost to mean total assets ratio of 0.49%[2] (2019: 0.48%) is expected to remain among the lowest in the UK building society sector and we will continue to invest in the Society for the benefit of members and to ensure the long term health and sustainability of the Society.

IMPAIRMENT CHARGE

The full economic impacts of the pandemic are uncertain and it is expected that government support such as payment holidays and the furlough scheme have obscured potential credit deterioration in the mortgage book. Notwithstanding very strong asset quality and the overall low risk nature of our balance sheet, it is against this backdrop we have made provisions for ECLs of £36 million (2019: £2 million). We have undertaken a significant amount of work over an extended period in order to seek to identify and properly consider a range of potential risks in a range of different scenarios including a scenario where house prices fall by a third and unemployment doubles. We have sought to estimate the impact of all of these risks in assessing ECLs.

By 31 December 2020, 39,000 members had taken Covid-19 related mortgage payment holidays, representing just under 15% by value of the mortgage loan book. There were 2,600 active payment holidays at the year end and 98% of the accounts with expired payment holidays had resumed mortgage payments. A further 2% of payment holiday customers are continuing to experience financial difficulties and we remain committed to supporting them through these challenging times.

The unprecedented nature of Covid-19 and the availability of payment holidays means that the calculation of expected credit losses has required significant judgement and estimation techniques. Of the total charge for the period, £33 million relates to a post model adjustment (PMA) where existing models do not fully reflect the ECLs arising from Covid-19 implications. The PMA has principally been calculated using the following techniques:

- By segmenting the book to identify higher risk segments and uplifting probability of default (PDs) accordingly. Higher risk segments include loans with a Covid-19 related payment holiday and those loans which have not taken a payment holiday but where external credit data indicates a deterioration in credit quality. The PDs applied in calculating the PMA have been uplifted by an average of 7.5%, weighted by value.
- We have reversed the benefit from the positive house price inflation we have seen since the start of the pandemic. HPI growth has been particularly strong in the second half of 2020 driven by temporary government support to keep the housing market strong such as stamp duty holiday which is expected to end on 31 March 2021. We believe this has only delayed the potential for house price falls in the near term and as such we have removed the impact of these increases when calculating ECLs.
- We have begun an assessment of more granular house price information on our mortgage book and this provides a more accurate view of indexed LTVs and risks associated with pockets of negative equity.

The remaining £3 million of ECL increase relates to worsening forward-looking macroeconomic scenarios and increases in the modelled ECL provision. The alternative scenarios reflect a range of possible outcomes as the economy emerges from the pandemic.

IFRS 9 requires loans to be assessed as 'stage 2' where there has been a significant increase in credit risk. During 2020 we have extended the criteria for stage 2 to include accounts which have taken a mortgage payment holiday of greater than three months and accounts with mortgage payment holidays where there are indications of a deterioration in credit quality. The remaining payment holiday cases have been left in stage 1. This change in criteria has resulted in 6.0% of loans being transferred into stage 2 (2019: nil) but despite this 91.3% of the book remains in stage 1 (2019: 97.0%).

As a result of these changes the ECL provision now equates to 0.11% of the overall mortgage book (2019: 0.03%). The materially higher level of ECL provision coverage is reflective of both the unprecedented nature of the environment and the potential risks in the period ahead.

PROVISIONS

There is a small charge of £0.5 million (2019: £nil) for provisions for liabilities. This relates to legal and redress cases.

CHARITABLE DONATION TO THE POPPY APPEAL

The Society continued to support The Royal British Legion's Poppy Appeal with £0.8 million donated during the year (2019: £1.2 million), bringing the total donated over the Society's relationship with the Legion to almost £19 million.

TAXATION

In 2020, the corporation tax charge was £23 million (2019: £26 million), an effective tax rate of 18.5% (2019: 17.3%).

BALANCE SHEET

OVERVIEW

In line with the underlying strategy the overall shape of the Balance Sheet has remained consistent during the year. Mortgage balances and liquidity have grown during the year by £1.2 billion and £0.4 billion respectively, with mortgage growth funded by growth in retail savings.

A summarised Balance Sheet is set out below:

	2020 £m	2019 £m
Assets		
Loans and advances to customers	43,482.8	42,234.7
Liquidity	7,314.5	6,854.7
Other	701.0	441.4
Total assets	51,498.3	49,530.8
Liabilities		
Retail funding	38,151.1	36,238.1
Wholesale funding	10,367.9	10,605.4
Subordinated liabilities and subscribed capital	67.2	67.1
Other	706.0	417.4
Total liabilities	49,292.2	47,328.0
Equity		
General reserve	1,835.1	1,773.3
Other equity instruments	415.0	415.0
Other	(44.0)	14.5
Total equity	2,206.1	2,202.8
Total liabilities and equity	51,498.3	49,530.8

LOANS AND ADVANCES TO CUSTOMERS

Our lending strategy remains unchanged and is focused on high quality, low loan to value loans within the prime residential market. These loans are primarily distributed through third party intermediaries, giving the Society a regionally diverse mortgage portfolio in a cost-effective manner.

In 2020, we advanced £6.7 billion of mortgages (2019: £8.6 billion) and mortgage balances grew by £1.2 billion (2019: £3.0 billion). The year on year growth in mortgages of 3.0% is in line with mortgage market growth of 3.0%[3] resulting in our market share remaining the same as 2019 at 2.9%.

This year, our approach to lending was more cautious in light of the pandemic, market disruption and the significant uncertainty we faced. As a result, our growth was lower than 2019 but still in line with the market.

New lending of owner-occupier mortgages accounted for 60% of total new lending in 2020 (2019: 67%) at an average loan to value (LTV) of 65.5% (2019: 64.8%). Total mortgage assets at 31 December 2020 stood at £43.4 billion (2019: £42.2 billion) which comprises £25.7 billion of owner-occupier loans (2019: £25.5 billion) and £17.7 billion buy to let loans (2019: £16.7 billion).

The balance weighted indexed loan to value of the mortgage book at 31 December 2020 decreased to 52.8%[4] (2019: 55.4%). Arrears have been impacted by borrowers' ability to meet payments against the economic backdrop of Covid-19 and increased slightly in 2020, but remain significantly better than the industry as a whole. As at 31 December 2020, 0.09% of mortgage balances were 2.5% or more in arrears (2019: 0.08%) compared with the latest available industry average of 0.69%[5].

Possessions and forbearance have been supported by mortgage payment holidays and have remained low with 22 cases in possession at the year end (2019: 33) and forbearance levels down by 17.1% year on year in value terms and 21.3% in number of cases.

LIQUIDITY

On-balance sheet liquid assets have increased to £7.3 billion (2019: £6.9 billion) as we maintained a prudent liquidity buffer given the uncertain economic environment. While the Liquidity Coverage Ratio (LCR) reduced from elevated levels in 2019, it continued to be very strong at 179% (2019: 214%), significantly above the minimum regulatory requirement.

Liquid assets are principally held in deposits at the Bank of England and UK Government investment securities. This means that asset quality remains very high with 93% of the portfolio rated Aaa-Aa3 (2019: 96%). 98% of liquid assets are held in UK sovereign or UK financial institutions (2019: 99%).

Included in liquid assets are £1.0 billion of assets held at fair value through other comprehensive income (FVOCI). As at 31 December 2020, the balance on the FVOCI reserve was a £2 million gain, net of tax (2019: £4 million gain, net of tax).

RETAIL FUNDING

Retail savings increased in the year by £2.0 billion to £38.2 billion (2019: £36.2 billion), representing growth of 5.3%, compared with market growth of 10.2%[3]. The Society's savings market share reduced slightly to 2.5%[3] (2019: 2.6%).

The Society continued to support the cash ISA market, maintaining our market share at 6.3%[3] (2019: 6.3%). Our growth was supported through our partnership with Hargreaves Lansdown where we expanded our product range through its Active Savings platform to include a restricted access savings account. Our performance in the year reflects both our mortgage performance and our position of being predominantly funded by retail savings with 88% of mortgage loans funded by retail savings (2019: 86%).

WHOLESALE FUNDING

We use wholesale funding to make our funding more diverse, enabling growth and lowering risk, both of which benefit members.

We materially increased our funding capabilities in 2020, with issuances from two new funding vehicles. In July 2020, we accessed the RMBS market through our Economic Master Issuer programme (£0.35 billion), our first issuance of this type through a Master Trust RMBS. In October 2020, we retained issuance from our newly created Godiva Covered Bonds LLP which utilises buy to let loans and enables us to further collateralise government funding schemes. In addition, in January we completed a £0.5 billion covered bond issuance and in the second half of the year issued £0.35 billion of unsecured debt. These were offset by £1.5 billion of maturities in the year.

In March 2020 the Bank of England launched the Term Funding Scheme with additional incentives for SMEs (TFSME) to enable lenders to support new lending into the wider economy. To date, we have drawn £2.3 billion of funding under the Scheme, replacing some of the planned wholesale funding and we have repaid £2.0 billion of the previous Term Funding Scheme leaving £4.55 billion of Central Bank Term Funding outstanding as at 31 December 2020 (2019: £4.25 billion).

EQUITY

The Society's equity is predominantly made up of its general reserve and Additional Tier 1 (AT 1) capital. While the Society made post-tax profits of £101 million in the year, total equity remained in line with last year at £2.2 billion, reflecting £29 million distribution to AT 1 capital holders and negative movements in the cash flow hedge and pension reserves which largely offset the post-tax profits.

PENSION FUND

The pension scheme assets and liabilities are recorded in the Society's accounts and the overall position was a surplus of £10 million at the end of 2020 (2019: £24 million). These assets and liabilities are impacted by market movements and the reduction in the year is driven by the fall in UK corporate bond yields in the second half of 2020. The Society continues to monitor the pension scheme to ensure that there is no scheme deficit over the medium term.

REGULATORY CAPITAL

We hold capital to protect members against future losses. As we grow our mortgage book the amount of capital we need to hold to meet the Capital Requirements Directive (CRD) IV increases.

The Society's CRD IV capital position[6] as at 31 December 2020 is summarised below. During the year, capital available for CET 1 or 'capital resources' increased by £92 million, primarily driven by profit after tax of £101 million.

The increase in capital, partly offset by a 2% increase in risk weighted assets (RWAs), has increased our CET 1 ratio to 33% (2019: 32%). We expect this to continue to be among the highest reported in the UK.

Our new IRB models have been approved by the PRA in the year which accounted for a 2% increase in RWAs. The new models have a much wider distribution of risk grades meaning that accounts are likely to move between grades more frequently and are more sensitive to factors such as HPI in the risk grade allocation.

However, prior to the implementation of the new IRB models, the underlying RWAs had decreased by less than 1% which was driven by offsetting factors relating to mortgage growth of 3%, improvements in the loan to value of mortgages largely as a result of increases in HPI and a reduction in RWAs for derivatives.

The PRA has recently released a consultation paper (CP14/20): "Internal Ratings Based UK mortgage risk weights: Managing deficiencies", which recommends flooring both average and individual IRB UK mortgage risk weights. If this were to be implemented as proposed, our CET 1 ratio would reduce by approximately 6%. From 2023, Basel IV RWA floors are being phased in and will reduce the Society's reported CET 1 ratio further, as they do not give full credit for our very low risk mortgage book. Applying the Basel IV RWA floors to the year end figures on a full transition basis would result in a CET 1 ratio of 17%.

The Society's Total Capital Requirement (TCR) has been updated to reflect changes in the regulatory setting of buffers, and the update of the Pillar 2 requirement to an absolute amount. As a result, our TCR at December 2020 was £574 million, equating to 10.6% of RWAs (2019: £590 million; 11.2%). We comfortably meet this requirement using CET 1 capital alone.

We are not currently bound by regulatory leverage ratios but we monitor leverage ratios on both a CRR[7] and UK basis. The UK ratio differs from the CRR basis in that it includes a restriction on the amount of AT 1 capital that can be included in leverage capital and excludes central bank claims with a maturity less than three months from leverage exposure.

The CRR and UK leverage ratios have increased slightly to 4.3% and 4.6%[8] respectively (2019: 4.1% and 4.4% respectively) driven by the increase in capital resources in the year.

	End-point 31 Dec 2020 £m	End-point 31 Dec 2019 £m
Capital resources:		
Common Equity Tier 1 (CET 1) capital	1,783.3	1,691.0
Total Tier 1 capital	2,198.3	2,106.0
Total capital	2,198.3	2,106.0
Risk weighted assets	5,410.6	5,283.6
Capital and leverage ratios:	%	%
Common Equity Tier 1 (CET 1) ratio	33.0	32.0
CRR leverage ratio[6]	4.3	4.1
UK leverage ratio[8,10]	4.6	4.4

1. The Society's average month end savings rate compared with the Bank of England average rate for household interest-bearing deposits on the Society's mix of products.
2. Administrative expenses, depreciation and amortisation/Average total assets.
3. Source: Bank of England
4. LTV is calculated using the Nationwide Building Society quarterly regional House Price Index (HPI).
5. Source: Prudential Regulation Authority - latest available information at 30 September 2020.
6. Excluding any IFRS 9 transitional provisions which were negligible.
7. Capital Requirements Regulation.
8. During the year the Society has refined its calculation of this measure. Had this applied in 2019 the comparative would be 4.6%.
9. The CRR leverage ratio is calculated in accordance with the definitions of CRD IV as amended by the European Commission delegated regulation.
10. The UK leverage ratio includes a restriction on the amount of Additional Tier 1 capital and excludes central bank reserves from the calculation of leverage exposures.

END

FR SSFSSLEFSEED