MANCHESTER BUILDING SOCIETY GROUP

CONDENSED CONSOLIDATED HALF YEARLY FINANCIAL INFORMATION

30 JUNE 2019

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DIRECTORS' REPORT

Introduction

The Directors present their Condensed Consolidated Half Yearly Financial Information of the Group for the 6 months ended 30 June 2019.

At 30 June 2019 the Group consisted of the Society and its two wholly owned subsidiaries: MBS (Mortgages) Limited and MBS (Property) Limited. In August 2019 MBS (Property) Limited was sold and ceased to be a member of the group.

Strategic summary

The Group's strategy since 2013 has been to reduce risks and conserve regulatory capital by moving its risk profile away from those legacy asset positions that carried higher risks and higher regulatory capital risk weightings. The disposal of the Group's head office building and its holding company, MBS (Property) Limited in August 2019 was a continuation of this strategy. The strategy was necessary because of events, fully disclosed in the Annual Report and Accounts for the year ended 31 December 2012, that led to a material write-down of the Group's reserves following a change in the accounting treatment of certain financial assets.

The Group continues to have headroom above its Pillar 1 plus Pillar 2A requirement in total capital terms but does not meet the qualitative standards for the level of Common Equity Tier 1 regulatory capital ("CET 1"). Consequently, the Society did not pay the coupons on Permanent Interest Bearing Shares ("PIBS") in April 2019 as such a distribution is prohibited under CRD IV article 141.

Following the Society's CET 1 capital falling below the required 4.5% of Risk Weighted Assets in 2018, a medium to long term strategic plan was produced which was independently reviewed and acknowledged by the PRA who agreed to monitor the Society against it. The plan was updated in July 2019.

The Group's results for the period are explained in detail in the sections that follow, along with the principal risks and uncertainties that the Group faces.

Business review

The Group recorded a profit after taxation for the 6 months ended 30 June 2019 of £454k, compared with a loss for the 6 months ended 30 June 2018 of £1,629k.

Mortgage assets reduced by 5% in the 6 months as the Group continued to make no new advances.

The Group's net interest income decreased by 14% compared with the same period in 2018. Retail balances at the end of June 2019 were £211m, £15m lower than at the end of December 2018.

Other operating income for the 6 months ended 30 June 2019 totalled £393k, compared to £612k for the comparative period in 2018 which included a one-off receipt in respect of damages awarded to the Society as part of the High Court judgment against its former external auditors, Grant Thornton UK LLP.

The Group's administrative expenditure was £3,585k (59%) lower than in the comparative period in 2018 which included £2,309k of costs awarded to Grant Thornton as part of the High Court judgment. £818k of the underlying reduction related to lower legal costs in relation to the case. There were further savings of £458k primarily on professional fees, contractor costs and audit fees.

Impairment losses of £921k were recorded in the period in respect of the Group's mortgage and loan books, compared to £245k in the first half of 2018. This increase was primarily driven by increased provisions on the Spanish lifetime portfolio.

The Group continued to minimise mortgage arrears and to help borrowers in difficulties to resolve their situations, taking a consultative approach with borrowers who experienced repayment difficulties and applying forbearance as appropriate. At 30 June 2019, excluding the second charge portfolio, there were 15 mortgage accounts where payments were 12 or more months in arrears (31 December 2018: 15). Total arrears were £1.1m (31 December 2018: £1.2m).

High levels of liquidity were maintained throughout the period with the Society having significant balances deposited with the Bank of England.

Risks and uncertainties

Given the Society does not meet the qualitative standards for the level of CET1 regulatory capital, the requirement for an increase in CET1 capital in order to return to lending, and the assessed prospects for the business and its capital position without such a return, there is a material uncertainty relating to the ability of the Group and Society to continue as a going concern due to the continued run-off of the balance sheet. A medium to long term strategic plan was produced which was independently reviewed and acknowledged by the PRA who agreed to monitor the Society against it. An update to this plan was submitted to the PRA in July 2019.

Every business faces risks as part of its day-to-day operations. The Board's risk management objectives are to seek to minimise the risks that the Group faces, by articulating that it has a low appetite for risk and by deploying a range of risk management policies and procedures within an appropriate control environment in order to achieve such an outcome.

A full explanation of the Board's assessment of the risks and uncertainties that are faced by the Group was set out in the 2018 Annual Report and Accounts on pages 5 to 6.

Summarised below are a number of the Group's key risks and uncertainties:

Credit Risk: The Group is exposed to the risk that it may not receive back in full any sum that has been loaned (in relation to loans and advances) or any sum that it has deposited with a banking counterparty (in relation to liquid assets) when such amounts fall due. The Board monitors credit risk, underlying security values and the level of impairment provisions on a regular basis. Credit risk is more of a consideration in relation to loans and advances than in relation to the Group's liquid assets; the former involve relationships with individuals or small businesses, whilst the latter are far fewer in number, being restricted to either the Bank of England or UK High Street banks, where credit risk is assessed as being very low.

The Group's management of credit risk in respect of loans and advances recognises that as the portfolio runs off it is likely that a greater part of the residual assets will have a higher credit risk profile.

The assessment of credit risk and the related impairment provisioning is a critical accounting estimate, impacted by judgments relating to customer affordability and economic circumstances, including the level of interest rates. Prior to the current strategy of no new lending, credit risk was mitigated by appropriate mortgage underwriting and by limiting the Group's exposure to particular market sectors or loans exhibiting particular attributes. Since the cessation of new lending credit risk has been mitigated through the monitoring of management information, assessment of arrears and forbearance cases, and regular loan provision reviews. The Group holds two mortgage books (the NMB MAC and CLC books), where previously it held a beneficial interest and these portfolios were administered by third parties. An assessment has been made of the estimated discounted future cash flows expected to arise from both these portfolios of loans which forms the basis for the impairment provision.

Insurance Risk: Impairment assessments incorporate the insurance risk attached to the Group's lifetime mortgage contracts, which are euro-denominated. The risk arises from a contractual term within the relevant mortgage contracts which in certain circumstances precludes the Group from pursuing the borrower or their estate for any shortfall on redemption. This risk is managed through oversight of the portfolio, including monitoring valuations, the assessment of redemptions and provisioning policy. The insurance provision is a critical accounting estimate, as its assessment is based on expected future outcomes relating to the date on which an account redeems, expected to be on the death of the borrower, a move into care or through non-health related voluntary pre-payment. It is also affected by the assumptions made in relation to house price appreciation and depreciation. This means that the insurance risk provision can move by a material amount dependent upon these assumptions and market conditions.

Liquidity Risk: The Group's strategy is to maintain sufficient funds in unencumbered liquid form at all times to ensure that its liabilities can be met as they fall due. Regular stress testing of liquidity is undertaken by separately using 20 week and 3 month time horizons. The Group operates within closely monitored Board-approved liquidity policy limits, which are reviewed on a daily basis by the Group's Finance and Treasury departments, reported to the Treasury Committee each week and considered by the Board each month. During H1 2019, the Group continued to have a significant proportion of its liquid assets deposited with the Bank of England.

Capital Risk: In order to conserve capital, the Group has continued not to undertake new lending. The Group continues to have headroom above its Pillar 1 plus Pillar 2A requirement in total capital terms, but does not meet the qualitative standards for the level of CET 1 regulatory capital. The Group has continued to explore ways in which the CET 1 regulatory capital position could be improved. A medium to long term strategic plan was produced in June 2018 which was independently reviewed and acknowledged by the PRA who agreed to monitor the Society against this plan. An update to this plan has been submitted to the PRA in July 2019.

Interest Rate Risk: The Group's mortgage and savings products have different interest rate types and differing maturity profiles. This means that the Group is exposed to movements in interest rates. A movement in an external interest rate (e.g. Bank of England Base Rate or LIBOR) does not always affect every mortgage and savings product that the Group holds. The Group has more fixed rate mortgage products (notably its lifetime mortgages) than it has fixed rate savings products. Presently, there are no interest rate swaps in place to mitigate the risk. The interest rate risk position is monitored by the Risk Committee and the Board and is managed via the setting of internal policy limits and through the holding of an ascribed level of regulatory capital to mitigate the risk of interest rate movement. The Board has considered this risk by its review of financial projections under differing interest rate scenarios over the long-term. The Group has a natural partial hedge provided by fixed coupons on capital and some savings products.

The Board does not intend to hedge its fixed rate mortgages using interest rate swaps at this time; this position is monitored regularly. A rise in interest rates gives rise to a risk of decreasing margins as a greater portion of the mortgage portfolio than the deposit portfolio is based on fixed rates. Liquidity risk can also be managed through changes in the interest rate of the deposit book.

Currency Risk: The Group faces currency movement risks on its Euro-denominated mortgage balances which represent 21% of total mortgage assets as at 30 June 2019. The exchange rate risk arising on these balances is managed and partially mitigated by transacting foreign exchange forward contracts. The exchange rate risk position is reported to the Asset and Liability Committee ('ALCO') and Board each month.

Economic Risk: The Group faces the risk that its interest margin can become subjected to the pressure that is brought to bear from being an institution that is primarily funded through retail deposits. Within this market, there is great competition for attracting retail deposits at sustainable rates of interest. Market rates offered by retail institutions reduced following the launch of the Bank of England's Funding for Lending and Term Funding Schemes; however, there is a risk that as repayments are required under these schemes there may be upward pressure on rates to prevent savings outflows.

The Group is also exposed to movements in the value of residential and commercial property in both its mortgage impairment provision requirements and those property assets held at fair value; the Group's investment property.

Political Risk: The UK referendum decision to leave the EU in June 2016 continues to create additional uncertainties for the economy, financial markets, housing and mortgage markets, government policy and financial services regulation. The impact upon borrower behaviour and collateral values within the Spanish lifetime portfolio is unknown. The Group has taken legal advice and contacted the regulatory authority in Spain and believes that operational risk is limited.

Regulatory Risk: As a regulated entity, the Group is exposed to risks arising from a failure to adhere to relevant regulation. In order to minimise this risk, the Group has deployed a number of risk management policies and procedures. The Group's Risk Management Framework ("RMF") is designed around the present needs of the Group. The RMF includes the responsibilities of the Board, the Risk Committee, the Conduct Committee and Management as to how the Group meets, monitors and reports on its regulatory requirements. Oversight of Regulatory Risk is the responsibility of the Compliance function and is led by the Compliance Manager.

The majority of the regulatory requirements that the Group faces are laid down by the PRA and the Financial Conduct Authority ("FCA"). The Group monitors developments in all relevant aspects of financial service regulation and undertakes assessments of the present and future impacts of such. Appropriate actions are taken to strengthen controls and amend the Group's strategy to meet changing regulatory requirements.

In addition to considering the impact of any non-compliance on the recoverability of loan balances and thus impairment provisioning, the Group considers the conduct risk which arises from having originated regulated loans and having acquired regulated loan portfolios. As is the case for all financial institutions there is a risk that aspects of current or historic business might be considered as not being conducted in accordance with all relevant regulation, or the fair and reasonable treatment of customers.

Certain activities of the Group, particularly the NMB MAC and CLC second charge loan portfolios carry greater levels of conduct risk. The administration of the NMB MAC and CLC portfolios was brought in-house in December 2015 and following that transfer the historic conduct of these portfolios was reviewed in detail by management and redressed where appropriate. Although a detailed review of these portfolios has been carried out, there is no judicial certainty in the legal position and there is a risk that further conduct issues or cases of non-compliance with regulations could be identified in the future.

Provision has been made where the Group is aware of a specific conduct or regulatory issue and can estimate its impact.

Other Matters

Board and staff changes

The Directors and Officers as at 30 June 2019 remain unchanged from those disclosed at 31 December 2018 on page 70 of the 2018 Annual Report and Accounts.

Going Concern

The directors consider that it is appropriate for the accounts to be prepared on a going concern basis of accounting as fully explained in Note 1.2 on page 13, which sets out the risks and uncertainties assessed as part of the preparation of the accounts.

Forward-looking statements

Within the half yearly information comments are made about future events. These statements are based on the Group's current view of the UK and Spanish economies, financial markets and regulation. The Board can give no assurances that actual outcomes will be in line with these assumptions.

The Group does not undertake to update any of the statements about future events prior to the reporting of the full year results.

Approval of interim financial statements

The Condensed Consolidated Half Yearly Financial Information was approved by the Board of Directors on 28 August 2019.

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE CONDENSED CONSOLIDATED HALF YEARLY FINANCIAL INFORMATION

The directors confirm that, to the best of their knowledge:

- The condensed set of consolidated accounts has been prepared in accordance with IAS 34 *Interim Financial Reporting*, as adopted by the European Union.
- The half yearly accounts include the information required by the Financial Conduct Authority Disclosure and Transparency Rules (DTR 4.2.7 and DTR 4.2.8)

The results for the half year ended 30 June 2019 and those comparable figures for the half year ended 30 June 2018 are unaudited. The figures for the year ended 2018 are extracted from the 2018 Annual Report and Accounts, prepared in accordance with IFRS as adopted in the EU, on which the Independent Auditors gave an unqualified opinion but did include an emphasis of matter in relation to the existence of a material uncertainty which may cast significant doubt about the Group's ability to continue as a going concern. Further details in relation to this are provided in Note 1.2 on page 13.

The Directors are responsible for the maintenance and integrity of information on the Society's website. Copies of the 2018 Annual Report & Accounts and this Half Yearly Financial Information may be found at: www.themanchester.co.uk/Main/FinancialInformation

The Board of Directors responsible for the half yearly accounts are listed below:

H.F. Baines	Vice Chairman
I.A. Dewar	Non-Executive Director
D.A. Harding	Chairman
J. Lincoln	Non-Executive Director
P.A. Lynch	Chief Executive
F.B. Smith	Non-Executive Director
M.A. Winterbottom	Finance Director

Signed on behalf of the Board of Directors

D.A. Harding
Chairman
28 August 2019

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Note	Unaudited 6 months to 30-Jun-19 £000	Unaudited 6 months to 30-Jun-18 £000	Audited 12 months to 31-Dec-18 £000
Interest receivable and similar income		5,072	5,526	10,828
Interest expense and similar charges		(1,503)	(1,359)	(2,869)
Net interest income		3,569	4,167	7,959
Other operating income		393	612	1,027
Other operating charges		(46)	(38)	(58)
Net gain on financial assets designated at fair value through profit and loss		1	1	1
Total operating income		3,917	4,742	8,929
Administrative expenses and depreciation		(2,547)	(6,132)	(10,185)
Operating profit / (loss) before impairment and provisions		1,370	(1,390)	(1,256)
Expected credit losses	7	(120)	(134)	(1)
Other impairment losses	7	(801)	(111)	(760)
Reversal of previous impairment on property, plant and equipment	7	-	-	1,074
Financial Services Compensation Scheme levy	11	5	6	6
Profit / (Loss) for the period before taxation		454	(1,629)	(937)
Income tax expense	4	-	-	-
Profit / (Loss) for the period		454	(1,629)	(937)

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Unaudited 6 months to 30 June 2019

	Retained earnings £000	Subscribed capital £000	PPDS £000	Total £000
Closing Balance at 31 December 2018	(11,259)	9,788	17,461	15,990
Loss and total comprehensive expense for the period	454	-	-	454
Balance at 30 June 2019	(10,805)	9,788	17,461	16,444

Unaudited 6 months to 30 June 2018

	Retained earnings £000	Subscribed capital £000	PPDS £000	Total £000
Closing Balance at 31 December 2017	(10,023)	9,788	17,461	17,226
Credit Loss adjustment to 1 January 2018 reserves in relation to implementation of IFRS 9	(299)	-	-	(299)
Opening Balance at 1 January 2018 under IFRS 9	(10,322)	9,788	17,461	16,927
Loss and total comprehensive expense for the period	(1,629)	-	-	(1,629)
Balance at 30 June 2018	(11,951)	9,788	17,461	15,298

Audited 12 months to 31 December 2018

	Retained earnings £000	Subscribed capital £000	PPDS £000	Total £000
Closing Balance at 31 December 2017	(10,023)	9,788	17,461	17,226
Credit Loss adjustment to 1 January 2018 reserves in relation to implementation of IFRS 9	(299)	-	-	(299)
Opening Balance at 1 January 2018 under IFRS 9	(10,322)	9,788	17,461	16,927
Loss and total comprehensive expense for the period	(937)	-	-	(937)
Balance at 31 December 2018	(11,259)	9,788	17,461	15,990

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Note	Unaudited 30-Jun-19 £000	Unaudited 30-Jun-18 £000	Audited 31-Dec-18 £000
Assets				
Liquid assets	*5*	43,495	45,055	48,072
Derivative financial instruments		104	102	30
Loans and advances to customers	*6*	208,999	235,256	219,740
Property, plant and equipment		188	6,008	6,955
Investment property		155	571	428
Current tax assets	*4*	-	-	-
Deferred tax assets	*8*	-	-	-
Other assets		2,492	2,435	2,160
Assets in disposal groups classified as held for sale	*9*	6,908	-	-
Total assets		262,341	289,427	277,385

	Note	Unaudited 30-Jun-19 £000	Unaudited 30-Jun-19 £000	Audited 31-Dec-18 £000
Liabilities				
Due to members		211,399	236,975	225,919
Deposits from banks and others	*10*	12,183	16,086	13,682
Derivative financial instruments		941	320	331
Other liabilities		1,942	1,484	2,225
Provisions for liabilities and charges	*11*	31	64	38
Subordinated liabilities	*12*	14,200	14,200	14,200
Subscribed capital	*13*	5,000	5,000	5,000
Liabilities directly associated with assets in disposal groups classified as held for sale	*9*	201	-	-
Total liabilities		245,897	274,129	261,395
Equity				
Retained earnings		(10,805)	(11,951)	(11,259)
Subscribed capital	*13*	9,788	9,788	9,788
Profit participating deferred shares	*14*	17,461	17,461	17,461
Total equity		16,444	15,298	15,990
Total equity and liabilities		262,341	289,427	277,385

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

	Unaudited 6 months to 30-Jun-19 £000	Unaudited 6 months to 30-Jun-18 £000	Audited 12 months to 31-Dec-18 £000
Net cash flows (used in) / from operating activities	(4,572)	1,089	3,882
Net cash flows from investing activities	1	28	244
Net cash flows from financing activities	3	-	3
Net (decrease) / increase in cash and cash equivalents	(4,568)	1,117	4,129
Net (decrease) / increase in cash and cash equivalents	(4,568)	1,117	4,129
Cash and cash equivalents at the start of the period	48,061	43,932	43,932
Cash and cash equivalents at the end of the period	43,493	45,049	48,061

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of preparation and significant accounting policies

1.1 Basis of preparation

This half yearly financial information for the 6 months ended 30 June 2019 has been prepared in accordance with both the Financial Conduct Authority's Disclosure and Transparency Rules and IAS 34 *Interim Financial Reporting*, as adopted by the EU. This financial information should be read in conjunction with the 2018 Annual Report and Accounts.

The half yearly financial information set out above does not constitute Accounts within the meaning of the Building Societies Act 1986.

The financial information for the 12 months to 31 December 2018 has been extracted from the 2018 Annual Report and Accounts, prepared in accordance with IFRS as adopted in the EU. In relation to these accounts, the opinion of the Independent Auditors was unqualified but did include an emphasis of matter in relation to the existence of a material uncertainty which may cast significant doubt about the Group's ability to continue as a going concern. Further details in relation to this are provided in Note 1.2 below.

The half yearly financial information for the 6 months ended 30 June 2019 and the 6 months ended 30 June 2018 are unaudited.

1.2 Basis of preparation: going concern

The Group's interim financial statements for the 6 months ended 30 June 2019 have been prepared on a going concern basis as explained below.

The Group has not been active in the Mortgage market since 2013 and at present has insufficient capital to return to lending. There is currently no plan in place to return to lending, though this is something which may be revisited should the capital position improve to a level where such activity may be appropriate. The current strategy of the Board, therefore, continues to be the management of a long-term run-off of the balance sheet.

Following the first instance judgment in the case against Grant Thornton UK LLP, and the interim costs awarded against the Society, the requirement to hold CET 1 Regulatory Capital of at least 4.5% of total Risk Weighted Assets was temporarily not met. A medium to long term strategic plan was produced which was independently reviewed and acknowledged by the PRA who agreed to monitor the Society against this plan. The plan shows that the Society remains viable in the medium-term and is able to rebuild its regulatory capital ratios in the medium-term. The plan was subject to an independent review on behalf of the regulators. It is recognised that there are a number of risks to this plan, particularly following a stress event in the economy or financial markets. Such stress events may include a downturn in the housing market either in the UK or Spain, additional provision requirements on one or more of the Group's larger mortgage exposures, significant unexpected expenses or a materially different mortgage repayment profile to that included within the plan.

The Board continues to work closely with its regulators to develop and implement its strategic plan. Implementation may involve third parties and require regulatory approval and as such may carry execution risk.

When satisfying themselves that the Group and Society have adequate resources to continue to operate for the foreseeable future as a going concern, the directors have reviewed the plan and the ability for it to be followed. The directors are reliant on the regulators' position regarding the plan remaining unchanged.

Whilst the Group continues to have a shortfall against qualitative standards for the level of CET 1 capital, the total capital position remains strong with significant headroom above its total Pillar 1 plus Pillar 2A requirements in total capital terms as set by the PRA. The liquidity position also remains strong with significant headroom above both its policy and operational limits.

Having due regard to these matters and after taking into consideration the material uncertainties above, which may cast significant doubt over the Group's ability to continue as a going concern, the Board continues to adopt the going concern basis of accounting in preparing the financial statements.

1.3 Basis of preparation: accounting policies

The half yearly financial information has been prepared consistently with the accounting policies described on pages 25 to 30 of the 2018 Annual Report and Accounts.

IFRS 16 – Leases is effective from 1 January 2019. An assessment of the impact of IFRS 16 has been performed and it does not have a material impact based on the current structure of the Society's leases with third parties.

The Group expects that the accounting policies that will be applied at the time of compiling the 2019 Annual Report and Accounts will be materially the same as for the 2018 Annual Report and Accounts.

2. Fair values of financial assets and liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between knowledgeable, willing market participants at the measurement date.

Wherever possible, fair values have been calculated using unadjusted quoted market prices in active markets for identical instruments held by the Group. Where quoted market prices are not available, or are unreliable, fair values have been determined using valuation techniques which, to the extent possible, use market observable inputs, but in some cases use non-market observable inputs.

Valuation techniques used include discounted cash flow analysis and pricing models and, where appropriate, comparison to instruments with characteristics similar to those of the instruments held by the Group.

Because a variety of estimation techniques are employed and significant estimates made, comparisons of fair values between financial institutions may not be meaningful. Readers of these financial statements are thus advised to use caution when using this data to evaluate the Group's financial position.

The fair value measurement basis used is as follows:

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

Level 2 Valuation techniques where all inputs are taken from observable market data, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3 Valuation techniques where significant inputs are not based on observable market data. None of the Group's assets or liabilities are valued using this technique.

A comparison between the carrying values and fair values of the Society's financial assets and liabilities is shown in the following table:

	30 June 2019		30 June 2018		31 December 2018	
	Carrying Value	Fair Value	Carrying Value	Fair Value	Carrying Value	Fair Value
	£000	£000	£000	£000	£000	£000
Financial assets						
Cash and balances with the Bank of England	37,676	37,676	34,989	34,989	33,123	33,123
Loans and advances to credit institutions	5,819	5,819	10,066	10,066	14,949	14,949
Loans and advances to customers	208,999	200,503	235,256	224,856	219,740	210,856
Other Assets	104	104	102	102	1,160	1,160
	252,598	244,102	280,413	270,013	268,972	260,088
Financial liabilities						
Due to members	211,399	211,423	236,975	236,968	225,919	225,826
Other deposits	12,183	12,183	16,086	16,086	13,682	13,682
Subordinated liabilities	14,200	14,200	14,200	14,200	14,200	14,200
Subscribed capital	5,000	900	5,000	1,225	5,000	1,103
Other liabilities	941	941	320	320	2,133	2,133
	243,723	239,647	272,581	268,799	260,934	256,944

(i) Market prices have been used to determine the fair value of listed investment securities

(ii) The fair value of derivatives and investment securities that are not listed are calculated by utilising internal valuation models using a discounted cash flow model based on a current yield curve appropriate for the remaining term to maturity. External market data is used within these internal valuation models. Derivatives are held for trading. Investment securities are designated at fair value through profit or loss. Movements in the valuations of derivatives and investment securities are treated as fair value through profit and loss, and these financial assets and liabilities are grouped into the fair value hierarchy under level 2.

(iii) The fair value of Investment Properties is determined by using available index data and reflects the market value at the balance sheet date and revaluations performed in the year.

3. Segmental information

The Group's results are predominantly derived from the Society's principal operations. The Group's other income streams are not sufficiently material to require segmental reporting

4. Income tax

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
Results for the period before tax	454	(1,629)	(937)
Tax rate	19.00%	19.00%	19.00%
Expected tax credit	86	(310)	(178)
Adjustments for non-deductible items	12	7	14
Income not taxable	-	-	(200)
Deferred tax movement closing rate/ average rate difference	-	-	50
Current period losses for which no deferred tax asset recognised	(14)	399	586
Decrease in deferred tax asset recognised	-	-	(167)
Fixed asset timing difference for which no deferred tax asset recognised	(84)	(96)	-
Profits of period covered by brought forward losses in respect of which no deferred tax asset recognised	-	-	(105)
Actual tax expense	-	-	-

5. Liquid assets

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
Cash and balances with the Bank of England	37,676	34,989	33,123
Loans and advances to credit institutions	5,819	10,066	14,949
	43,495	45,055	48,072

6. Loans and advances to customers

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
Gross Balances			
Fully secured on residential property	210,991	234,442	220,268
Fully secured on land	20,265	23,835	21,784
Other loans	565	813	777
	231,821	259,090	242,829
Provisions			
Fully secured on residential property	20,080	19,518	19,499
Fully secured on land	2,709	4,309	3,578
Other loans	33	7	12
	22,822	23,834	23,089
Net Balances			
Fully secured on residential property	190,911	214,924	200,769
Fully secured on land	17,556	19,526	18,206
Other loans	532	806	765
	208,999	235,256	219,740

7. Impairment losses

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
Expected credit losses			
Impairment losses on loans and advances to customers on residential property and land	132	158	44
Amounts recovered on loans and advances to customers on residential property and land, written off in prior periods	(12)	(24)	(43)
Total expected credit losses	**120**	**134**	**1**
Other impairment losses			
Impairment losses on loans and advances to customers on lifetime mortgages	801	111	760
Total other impairment losses	**801**	**111**	**760**
Reversal of previous impairment on Property, Plant and Equipment	-	-	(1,074)
Total impairment losses / (gains)	**921**	**245**	**(313)**

8. Deferred tax assets

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
Tax losses	2	1	3
Deferred tax movement on timing differences on derivative contracts	1	30	13
Accelerated tax depreciation	(3)	(31)	(16)
Other provisions	-	-	-
Total	-	-	-

9. Assets in disposal groups classified as held for sale

The group's land and buildings, being its head office, was owned by MBS (Property) Limited ("MBSP"). Heads of terms to sell MBSP were signed in March 2019 and the sale completed in August 2019. At 30 June 2019 the assets and liabilities of MBSP were classified as "held for sale" as required by *IFRS 5 – Non-current assets held for sale and discontinued operations*. The items within this disposal group are measured at carrying value, being the lower of carrying value and fair value less disposal costs.

The assets and liabilities within the disposal group were as follows:

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
Assets			
Property Plant & Equipment	6,642	-	-
Other Assets	266	-	-
	6,908	-	-
Liabilities			
Other Liabilities	201	-	-
	201	-	-

10. Deposits from banks and others

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
Other deposits	12,183	16,086	13,682
Total	12,183	16,086	13,682

11. Provisions for liabilities and charges

FSCS levy	Unaudited 30-Jun-19 £000	Unaudited 30-Jun-18 £000	Audited 31-Dec-18 £000
At start of period	11	31	31
Release for the period	(6)	(6)	(6)
Provision utilised	0	0	(14)
At end of period	5	25	11

Customer redress	Unaudited 30-Jun-19 £000	Unaudited 30-Jun-18 £000	Audited 31-Dec-18 £000
At start of period	25	111	111
Release for the period	0	(2)	(4)
Provision utilised	0	(71)	(82)
At end of period	25	38	25

Other	Unaudited 30-Jun-19 £000	Unaudited 30-Jun-18 £000	Audited 31-Dec-18 £000
At start of period	2	100	100
Release for the period	(1)	(79)	(78)
Provision utilised	0	(20)	(20)
At end of period	1	1	2
Total provisions for liabilities and charges at the end of the period	31	64	38

(i) Financial Services Compensation Scheme ("FSCS levy")

The Society's provision for FSCS charges arises from its operation as a UK deposit taker. The FSCS levy consists of two parts- a management expenses levy, which covers the interest cost of running the scheme, and a capital levy to cover the cost of the compensation paid, net of any recoveries.

The expected management expenses levy for the FSCS scheme year 2018-19 had been provided at the end of 2018. The provision release for the half year to 30 June 2019 is in respect of a reduction in the expected management expenses levy for the FSCS scheme year 2019-20. This charge represents the expected full cost of the FSCS levy for the financial year.

No provision is made for scheme years beyond these periods. The levy is paid during the third quarter each year and the Society does not expect to recover any sums paid.

(ii) Customer redress provision

The customer redress provision is held in relation to a customer redress exercise in respect of instances of non-compliance with the CCA within the NMB MAC and CLC second charge portfolios, which is detailed on page 67 of the 2018 Annual Report and Accounts. This redress exercise was completed in 2017. Attempts to contact some customers have been unsuccessful to date, and the £25k provision is retained at 30 June 2019 in relation to these customers.

(iii) Other provision

The other provision relates to the result of the BoS v Rea decision, which is detailed on page 67 of the 2018 Annual Report and Accounts. The remediation exercise in relation to this provision was completed during 2018. The £1k provision that remains relates to a small number of customers which the Society has, so far, been unable to contact.

12. Subordinated liabilities

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
Loan (repay 2022) interest: 3 month LIBOR + 1.75%	5,000	5,000	5,000
Loan (repay 2023) interest: 3 month LIBOR + 2.45%	4,200	4,200	4,200
Loan (repay 2032) interest: 6.70%	5,000	5,000	5,000
Total	14,200	14,200	14,200

13. Subscribed capital

The Society has two tranches of PIBS in issue. The first tranche was issued in 1999 and is remunerated at 8.00% and the other was issued in 2005 and is remunerated at 6.75%. The two tranches are accounted for differently as they are subject to differing legal arrangements. Both tranches of PIBS are unsecured and rank pari passu with each other. In priority terms, the PIBS holders rank behind the Society's depositing members, its wholesale counterparties and all subordinated note holders. PIBS coupons are non-cumulative.

Classified as a liability:

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
8.00% Permanent Interest Bearing Shares	5,000	5,000	5,000
Total	5,000	5,000	5,000

Classified as equity:

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
6.75% Permanent Interest Bearing Shares	9,788	9,788	9,788
Total	9,788	9,788	9,788

14. Profit Participating Deferred Shares

	Unaudited 30 Jun 19 £000	Unaudited 30 Jun 18 £000	Audited 31 Dec 18 £000
Nominal value - proceeds received	18,000	18,000	18,000
Less: issue costs	(539)	(539)	(539)
Total	17,461	17,461	17,461

The shares were issued in April 2013, are unsecured and rank pari passu with any other deferred shares comprising Common Equity Tier 1 capital issued or to be issued by the Society and rank behind any other deferred shares of the Society in issue not comprising Common Equity Tier 1 capital, including the Society's 1999 and 2005 PIBS.

The PPDS holders rank behind the Society's depositing members, its wholesale counterparties and all subordinated note holders.

The terms of the PPDS allow the Board, at its sole discretion, to declare a dividend of up to 30% of the Society's post tax profits. Dividends are non-cumulative.

15. Capital

The Board manages capital within the regulatory limits set by the PRA.

The Group calculates and reports its regulatory capital on a "Total Group" basis with the regulatory capital group being made up of the Society, MBS (Mortgages) Limited and MBS (Property) Limited.

	Unaudited 30 Jun 19 Total Group £000	Unaudited 30 Jun 18 Total Group £000	Audited 31 Dec 18 Total Group £000
Tier 1 Capital			
Common Equity Tier 1 Capital (CET1)			
Accumulated Losses	(11,259)	(11,952)	(11,259)
IFRS 9 transitional arrangements -	255	285	285
Profit Participating Deferred Shares	17,461	17,461	17,461
Total CET1 Capital	6,457	5,794	6,487
Other Tier 1 Capital			
Permanent Interest Bearing Shares			
-Nominal balance	14,788	14,788	14,788
-Amortisation	(10,352)	(8,873)	(8,873)
Net Permanent Interest Bearing Shares	4,436	5,915	5,915
Total Tier 1 Capital	10,893	11,709	12,402
Tier 2 Capital			
Subordinated Debt			
-Nominal balance	14,200	14,200	14,200
-Amortisation	(7,062)	(4,657)	(5,584)
Net Subordinated Debt	7,138	9,543	8,616
Collective Provisions	-	441	-
Permanent Interest Bearing Shares	10,352	8,873	8,873
Total Tier 2 Capital	17,490	18,857	17,489
Total Regulatory Capital	28,383	30,566	29,891

Since the start of 2019 Total Regulatory Capital under CRD IV has decreased by £1,508k from £29,891 to £28,383k.

The decrease results from ongoing operations, made up as follows:

- a reduction of £30k regarding the transitional rules covering the implementation of IFRS 9;
- the continued grandfathering of Subordinated debt out of Tier 2 capital over a 9 year period, amounting to £500k in the half year;
- amortisation out of Tier 2 capital of an additional portion of Subordinated debt which now has less than five years to its maturity date, amounting to £978k in the half year.

As at 30 June 2019 the Society met its Pillar 1 plus Pillar 2A requirement in total capital terms, but continued to have a shortfall against the qualitative standards for the level of CET1 regulatory capital. The Society as required by CRD IV article 142 submitted a Capital Conservation Plan to the PRA in October 2016 as a result of this shortfall, with a number of subsequent updates setting out proposed measures to improve the regulatory capital position. In June 2018, following the Society's CET 1 capital falling below the required 4.5% of Risk Weighted Assets, a new medium to long term strategic plan was produced which was independently reviewed and acknowledged by the PRA who agreed to monitor the Society against it. This plan was updated and resubmitted in July 2019. The PRA continue an open dialogue with the Society on future developments.

16. Related party transactions

The Group is controlled by Manchester Building Society and at 30 June 2019 consisted of the Society and its two wholly owned subsidiaries: MBS (Mortgages) Ltd and MBS (Property) Ltd. The Society continued to provide loan funding to its subsidiaries during the half year ended 30 June 2019 in a manner similar to that disclosed in the 2018 Annual Report and Accounts. Accordingly, transactions with these related parties are entered into in the normal course of business; related party transactions, for the half year to 30 June 2019 are similar in nature to those for the year ended 31 December 2018. In August 2019, MBS (Property) Ltd was sold and ceased to be a member of the group.

The Officers as at 30 June 2019 remain unaltered from those disclosed at 31 December 2018 on page 70 of the 2018 Annual Report and Accounts.

Where the services of key management personnel are provided by entities controlled by them, then transactions with these entities are approved by the Remuneration and Nominations Committee.

17. Financial commitments

There is no material change to the Group's financial commitments from the position reported in the 2018 Annual Report and Accounts

18. Contingent liabilities and assets

(i) Contingent liabilities

Given the high level of scrutiny regarding financial institutions' treatment of customers and business conduct from regulatory bodies and other sources there is a risk that certain aspects of the Group's current or historic business, including, amongst other things, CCA regulated loans, may be determined by the FCA and other regulatory bodies or the courts as, in their opinion, not being conducted in accordance with applicable laws or regulations, or fair and reasonable treatment.

As detailed in the Regulatory risk section on pages 6 and 7 and in Note 11, provision has been made where the Group is aware of a specific conduct issue and can estimate its impact reliably.

As disclosed on page 67 of the 2018 Annual Report and Accounts there is a risk that other aspects of the Group's business might be considered as not having been conducted in accordance with all relevant regulation, or the fair and reasonable treatment of customers. It is also not possible to rule out the possibility of other instances of non-compliance with CCA or other regulations which have not been identified. No provisions against these risks are included in these accounts.

As noted in the Strategic Report on page 3 of the 2018 Annual Report and Accounts, the High Court judgment resulting from the Society's legal claim against its former external auditors, Grant Thornton UK LLP ("GT"), resulted in GT being awarded £2,309k interim costs. In addition, in 2019, the Society has paid a further £266k to GT in relation to legal fees associated with the unsuccessful appeal. While the Society has been granted leave to appeal the decision to the Supreme Court, there remains the potential for a final costs determination that may require the Society to pay a further sum to Grant Thornton. An accrual for these costs was made in 2018 based upon the best estimate of the Board but the value of such an award is not known at this time and so there remains the potential for some additional costs to be incurred.

(ii) Contingent assets

The Group's claim against Grant Thornton UK LLP, as detailed in section (i) above, may result in further damages being awarded to the Society upon appeal to the Supreme Court. The likelihood and amount of any potential award are not known at this time. It is expected that the appeal will be heard no earlier than mid-2020, with the judgment known some time later.

19. Events after the end of the reporting period

There have been no events occurring after the end of the reporting period that would have a material impact upon the results reported.

20. Other Ratios

	Unaudited 6 months to 30 Jun 19 %	Unaudited 6 months to 30 Jun 18 %	Audited 12 months to 31 Dec 18 %
Gross capital as a percentage of shares and borrowings	15.9	13.6	14.7
Liquid funds as a percentage of shares and borrowings	19.5	17.8	20.1
Profit/(Loss) after tax as a percentage of mean total assets *(expressed on an annualised basis)*	0.3	(1.1)	(0.3)
Group management expenses as a percentage of mean total assets *(expressed on an annualised basis)*	1.8	4.1	3.5
Leverage ratio	3.8	3.7	4.2

The definitions for the above ratios are explained in detail on page 69 of the 2018 Annual Report and Accounts.

The Society has utilised available transitional arrangements in relation to the impact of adopting IFRS 9 on regulatory capital and the figures above reflect these arrangements. Had the transitional arrangements not been adopted, the leverage ratio would have been 3.6%.

21. Post Balance Sheet Events

On 15 August 2019 the Society sold its subsidiary MBS (Property) Limited. The assets of the subsidiary were classified as "held for sale" at 30 June 2019 and are disclosed in Note 9. The sale is a non-adjusting event under *IAS 10 – Events after the Reporting Period*. The sale of the subsidiary generated a gain for the Group of £0.3m after associated professional fees. This gain will be recognised in the 2019 Annual Report and Accounts.