Nationwide Building Society

Interim Management Statement
Q1 2016/17

Underlying profit
Statutory profit before tax has been adjusted for a number of items, consistent with prior periods, to derive an underlying profit before tax figure. The purpose of this measure is to reflect management's view of the Group's underlying performance and to assist with like for like comparisons of performance across periods. Underlying profit is not designed to measure sustainable levels of profitability as that potentially requires exclusion of non-recurring items even though they are closely related to (or even a direct consequence of) the Group's core business activities.

12 August 2016

Nationwide Building Society today publishes its Interim Management Statement covering the quarter from 5 April 2016 to 30 June 2016 ("Q1 2016/17").

Joe Garner, Nationwide Chief Executive, said:

"As the world's largest building society, we are in the fortunate position to be able to take a long term view and focus on providing great service, security and stability for our members. This will be particularly important in a time of increased uncertainty and market volatility following the EU referendum.

"The contribution that our Society continues to make in support of the housing market and by offering long term value to savers, even in the current low interest rate environment, is evident in our trading results for the first quarter which represent a strong start to the year.

"Following the decision by the Bank of England to cut the Bank Rate to 0.25%, the Society will pass on the decrease in full to existing Base Mortgage Rate (BMR), Standard Mortgage Rate (SMR) and tracker mortgage customers. In addition we will protect members who save regularly and who are building up a deposit to buy their first home; as a result, the Flexclusive Regular Saver at 5%, the FlexOne Regular Saver at 3.5% and the Help to Buy ISA at 2% are being maintained at their current rates.

"We continue to deliver market leading customer service amongst our high street peer group with a lead of 4.8%[1], reflecting the primary focus on members which is the essence of the building society difference. A recent example of our continuing investment in service is the launch of our new Banking app with improved navigation and a range of new features.

"Looking forward, we remain focused entirely on the needs of our members, particularly during times of uncertainty. It is for this reason that we announced at our AGM last month our five-point plan for how we will support our borrowers and savers post Brexit and help them realise their ambitions. This includes a number of commitments to help people onto the housing ladder, or to move up through the housing market, while supporting those who want to save and plan for the future."

Mark Rennison, Nationwide Finance Director, said:

"Nationwide's strong trading performance provides the backdrop to a satisfactory financial performance for our first quarter of the new financial year. As we indicated when announcing our last year end results, margins have trended lower as a result of competition in the mortgage market. We are reporting a statutory profit of £401 million and an underlying profit of £368 million for the quarter, both of which are after recognising a gain of £100 million on the disposal of our stake in Visa Europe, consistent with our established accounting practice. Our capital and liquidity ratios remain strong, underpinning the security we provide to all our members.

"We have seen an increase in gross mortgage lending of 26% to £8.6 billion, equating to a market share of 15%, helping people buy homes for themselves and their families. Our range of mortgage products is very competitive and we reserve the best rates for our existing customers as a demonstration of the value we place on their loyalty.

"Looking after our savings members in uncertain and challenging times is at the heart of what we do. Our range of long term loyalty products has led to an increase in member deposits in the first quarter of £2.6 billion.

"New current account openings have increased by 21% to over 139,000 as more people choose to manage their money every day with us. Our Recommend a Friend proposition which values members for their loyalty and advocacy has helped Nationwide continue to be a net gainer of the current account switching service, taking a 15% market share."

[1] © GfK 2016, Financial Research Survey (FRS), 3 months ending 30 June 2016, proportion of extremely/very satisfied customers minus proportion of extremely/very/fairly dissatisfied customers summed across current account, mortgage and savings, high street peer group defined as providers with main current account market share >6% (Barclays, Halifax, HSBC, Lloyds Bank (inc C&G), NatWest and Santander).

Trading performance

	Quarter ended 30 June 2016 £bn	**%**	Quarter ended 30 June 2015 £bn	%
Gross residential mortgage lending/market share	**8.6**	***15.0***	6.8	*13.1*
Net residential mortgage lending/market share	**3.5**	***52.8***	2.1	*27.5*
Member deposits balance movement[2]/market share	**2.6**	***11.1***	0.1	*0.8*
Number of new current accounts opened	**139,000**		115,000	

	At 30 June 2016 £bn	**%**	At 4 April 2016 £bn	%
Residential lending balances	**165.8**		162.2	
Member deposit balances[2]	**141.3**		138.7	
Current account stock market share[3]		**7.1**		7.1

We have continued to provide support to the UK housing market with gross mortgage lending for the quarter ended 30 June 2016 of £8.6 billion, up 26% on the comparative period and representing a market share of 15.0%. The average LTV of new lending was broadly in line with the same period last year at 70% (Q1 2015/16: 69%). Net lending of £3.5 billion increased 67% and represented a market share of 52.8%. Our strong performance reflects competitive products and propositions, with no fees for standard valuations on all our mortgages, and we continue to provide our best rates exclusively to our existing mortgage members.

Gross and net mortgage lending included buy to let (BTL) lending of £1.7 billion and £0.9 billion respectively. Following the announcement of tax changes relating to BTL income, the Group has made changes to its affordability assessment to ensure borrowing for customers remains affordable. An expected contraction in the BTL market, combined with our underwriting changes, is likely to lead to lower levels of BTL new lending for the remainder of the year.

Our strategy of offering a range of long term good value products and rewarding loyal savers has resulted in member deposits[2] increasing by £2.6 billion, reflecting our strong position relative to our major high street banking competitors and represents a market share of 11.1%. This is significantly ahead of the same period last year which was affected by the popular National Savings and Investments' Pensioner Bonds.

During the period we opened over 139,000 new current accounts, 21% more than the same period last year. We continue to be a net beneficiary of the current account switching service, with 14.9% market share. Our stock market share of main and standard packaged accounts was 7.1%[3].

[2] Member deposits include current account credit balances.
[3] Based on market data as at May 2016 (comparative based on market data as at February 2016).

Financial performance

	Quarter ended 30 June 2016 £m	**%**	Quarter ended 30 June 2015 £m	%
Underlying profit before tax[4]	**368**		391	
Statutory profit before tax	**401**		379	
Net interest margin[4]		**1.35**		1.61
Underlying cost income ratio[4]		**53.6**		51.6
Statutory cost income ratio		**51.7**		52.5

	At 30 June 2016 £bn	**%**	At 4 April 2016 £bn	%
Total assets	**220.3**		208.9	
Loans and advances to customers	**182.7**		178.8	
Common Equity Tier 1 (CET1) ratio[5]		**23.4**		23.2
Leverage ratio[5]		**4.1**		4.2
Liquidity coverage ratio		**150.7**		142.6
Wholesale funding ratio		**27.1**		24.8

Underlying profit before tax for the quarter ended 30 June 2016 was down 6% at £368 million, predominantly due to a reduction in net interest income, growth in underlying costs and a modest increase in impairment provisions. This has been partially offset by a gain of £100 million from the disposal of the Group's investment in Visa Europe during the period.

Statutory profit before tax was up 6% at £401 million. This includes £31 million of derivative and hedge accounting gains which are excluded from underlying profit (Q1 2015/16: £3 million loss).

Net interest margin in the quarter of 1.35% was lower than the full year to 4 April 2016 of 1.52%, and the same period last year, due to the impact of sustained levels of competition in the mortgage market. The margin of 1.35% in the quarter is only modestly lower than the level for the last quarter of the previous year. However, expectations that the low interest rate environment will persist or that rates may decrease further in the wake of the EU referendum decision may exert further pressure on margins.

The underlying cost income ratio has increased from 51.6%[4] to 53.6% and further growth is expected in the remainder of the year. This is primarily driven from our ongoing investment programme to improve product propositions and services for members.

Our credit performance continues to be strong with low levels of impairment provisions required. The provisions recognised in the quarter were modestly higher than those in the same period in the prior year, as the level of net recoveries observed in the commercial real estate portfolio in the previous year has not been repeated. Overall, the level of arrears and delinquencies in our core lending portfolios remains broadly consistent with the position reported at 4 April 2016.

We continue to review compliance with ongoing and emerging regulatory matters, including consumer credit legislation, and have recognised a net provision charge of £13 million in the quarter in respect of potential customer redress. Current provisions reflect latest experience and the estimated impact of industry consultation.

Our capital position has remained strong, with consolidated CET1 and leverage ratios as at 30 June 2016 of 23.4% and 4.1% respectively (4 April 2016: 23.2% and 4.2% respectively)[5]. The decrease in the leverage ratio reflects both balance sheet growth and a higher pension deficit. Further information on our capital position can be found in Appendix 1.

[4] Comparatives have been restated to exclude foreign currency retranslation amounts from net interest margin within underlying profit, in line with presentational changes made in the Group's Interim Results at 30 September 2015.
[5] The capital ratios provided have been calculated under CRD IV on an end point basis. The leverage ratio is calculated using the CRR definition of Tier 1 for the capital amount and the delegated act definition of the exposure measure.

On 4 August the PRA announced a modification to the calculation of leverage exposure for the purposes of the UK leverage ratio framework by excluding central bank reserves. Under the modified basis of measurement we estimate that the Group's leverage ratio at 30 June 2016 would have been 4.4%. The permission to modify the basis of measurement for the purposes of the UK regulatory regime does not affect the requirement to calculate and report leverage in accordance with the CRR as disclosed in the table above.

Outlook

Based upon latest available data the UK economy appeared to expand at a respectable pace in the first half of 2016. However, whilst it is too early to make clear impact assessments about the EU referendum outcome, the uncertainty generated could adversely impact investment decisions and consumer spending with a consequent impact on broader growth in the near term. The longer term impact will depend on a range of factors, not least the time it takes to reach an agreement with EU and non-EU economies, the nature of those agreements and the broader political situation.

In addition to cutting Bank Rate to 0.25%, the Bank of England also announced a new Term Funding Scheme and £70 billion of additional asset purchases, to help stimulate the economy. The Monetary Policy Committee has indicated that further monetary stimulus may be required in the quarters ahead.

Our capital position and the quality of our balance sheet means Nationwide is well placed to continue to help our members and customers whatever the prevailing economic conditions. The sustained low interest rate environment and competition in core markets will maintain pressure on margins and we anticipate profits are likely to moderate in the period ahead. Nevertheless our mutual model combined with our financial strength means we are able to focus on taking a long-term view for the benefit of members, rather than actions to drive short-term profitability. We will continue to focus on supporting members and investing in new propositions and service enhancements, whilst maintaining our capital strength.

Additional information

The financial information on which this Interim Management Statement is based is unaudited and has been prepared in accordance with Nationwide's previously stated accounting policies described in the Annual Report and Accounts 2016.

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Appendix 1 – Capital position

Capital structure and ratios

Common Equity Tier 1 (CET1) capital resources have increased over the period by approximately £0.1 billion. This is the result of a strong trading performance (which was partly offset by a reduction in reserves due to an increase in the pension deficit) and lower regulatory adjustments resulting from reduced expected losses. Risk weighted assets (RWAs) increased over the period by approximately £0.2 billion. These movements have resulted in a CET1 ratio of 23.4% (4 April 2016: 23.2%).

	30 June 2016 £m	4 April 2016 £m
Common Equity Tier 1 capital before regulatory adjustments	**9,560**	9,508
Total regulatory adjustments to Common Equity Tier 1	**(1,443)**	(1,495)
Common Equity Tier 1 capital	**8,117**	8,013
Additional Tier 1 capital before regulatory adjustments	**992**	992
Total regulatory adjustments to Additional Tier 1 capital	**-**	-
Additional Tier 1 capital	**992**	992
Total Tier 1 capital	**9,109**	9,005
Tier 2 capital before regulatory adjustments	**1,659**	1,649
Total regulatory adjustments to Tier 2 capital	**-**	-
Tier 2 capital	**1,659**	1,649
Total capital	**10,768**	10,654
Ratios:	**%**	%
Common Equity Tier 1	**23.4**	23.2
Tier 1	**26.3**	26.1
Total capital	**31.1**	30.9

Note: Data in the table is reported under CRD IV on an end point basis, being full implementation of Capital Requirements Directive IV with no transitional provisions.

Capital requirements

	30 June 2016		4 April 2016	
	RWAs £m	**Pillar 1 Capital requirements* £m**	RWAs £m	Pillar 1 Capital requirements* £m
Credit risk	**28,680**	**2,294**	28,575	2,286
Counterparty credit risk	**636**	**51**	598	48
Market risk**	**-**	**-**	-	-
Operational risk	**4,604**	**368**	4,604	368
Credit valuation adjustment	**732**	**59**	698	56
Total	**34,652**	**2,772**	34,475	2,758

* The Group also holds capital to meet Pillar 2 and capital buffer requirements. Details of Pillar 2 requirements as at 4 April 2016 are set out in the Group's Pillar 3 disclosures at **nationwide.co.uk**
** Market risk has been set to zero as permitted by the CRR as exposure is below the threshold of 2% of own funds.

Leverage ratio

The Group holds capital to meet a leverage ratio requirement, with the current regulatory threshold set at 3%. The leverage ratio has decreased to 4.1% (4 April 2016: 4.2%) as a result of the balance sheet growth and a higher pension deficit.

	30 June 2016 £m	4 April 2016 £m
Tier 1 capital	**9,109**	9,005
Leverage exposure	**223,435**	213,181
	%	%
Leverage ratio*	**4.1**	4.2

* The leverage ratio is calculated using the CRR definition of Tier 1 for the capital amount and the delegated act definition of the exposure measure.