15 March 2018

OneSavings Bank plc

Preliminary results for the year ended 31 December 2017

Financial highlights

- Underlying profit before tax[1] increased 21% to £167.7m (2016: restated[2] £138.2m)
- Loan book growth of 23% to £7.3bn (2016: £5.9bn) driven by 14% growth in gross originations to £2.6bn (2016: £2.3bn)
- Strong income growth alongside continued focus on cost discipline and efficiency delivered a stable cost to income ratio[3] of 27% (2016: 27%)
- Net interest margin ('NIM')[4] stable at 316bps (2016: restated[2] 316bps)
- Further improved loan loss ratio[5] of 7bps (2016:16bps)
- Return on equity ('RoE')[6] remained strong at 28% (2016: 29%), despite strengthening our Common Equity Tier 1 ('CET1') capital ratio to 13.7% (2016: 13.3%)
- Underlying basic earnings per share[7] grew 23% to 51.1 pence (2016: 41.7 pence)
- Recommended final dividend[8] of 9.3 pence per share giving a full year dividend of 12.8 pence per share, in line with our target dividend payout ratio
- Further optimisation of capital structure through the issue of £60m of Additional Tier 1 securities

Andy Golding, CEO of OneSavings Bank, said:

"I am delighted that OneSavings Bank has delivered another excellent set of results for 2017, whilst successfully negotiating significant regulatory and tax changes in our core Buy-to-Let market.

We generated a 21% increase in underlying profit before tax and a 23% increase in underlying basic earnings per share. This was underpinned by strong organic originations, up 14% to £2.6bn, maintaining attractive margins and prudent risk management alongside continued cost efficiency and discipline. We delivered a strong return on equity of 28% despite strengthening our CET1 ratio to 13.7%.

Despite market sentiment linked to political and economic uncertainty going forward, we entered 2018 with a strong pipeline of new business in our core markets and intend to deploy our proven credit risk and operational competencies to expand our residential and commercial product offerings in 2018.

We also expect to deliver net loan book growth in the mid-teens in 2018 and NIM of c. 3%, reflecting current asset pricing and an expectation of a rising cost of funds after the end of TFS. We anticipate a cost to income ratio of c. 30% for 2018, reflecting the significant increase in the cost of regulation and planned investment in the business to support our growth strategy.

OneSavings Bank is well placed to take advantage of growth opportunities in 2018 and we remain confident in our ability to generate attractive returns for our shareholders."

Key metrics

	2017	2016
Loan loss ratio[5] (bps)	**7**	16
Statutory profit before tax (£m)	**167.7**	163.1
Total assets (£bn)	**8.6**	6.6
Statutory basic EPS[9] (pence)	**51.1**	49.4
Loan to deposit ratio[10] (%)	**92**	90
3 months + arrears[11] (%)	**1.2**	1.4
Customer net promoter score	**+62**	+59

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Analyst presentation

A presentation for analysts will be held at 9:30am on Thursday 15 March at The Lincoln Centre, 18 Lincoln's Inn Fields, WC2A 3ED. The UK dial in is 0808 109 0700, standard international access is +44 (0) 20 3003 2666. For both the password is One Savings. The presentation will be webcast and available from 9.30am on the OneSavings Bank website at osb.co.uk in the Investor Relations, Report and Accounts section. Registration is open immediately.

About OneSavings Bank plc

OneSavings Bank plc began trading as a bank on 1 February 2011 and was admitted to the main market of the London Stock Exchange in June 2014 (OSB.L). OSB joined the FTSE 250 index in June 2015. OSB is a specialist lending and retail savings group authorised by the Prudential Regulation Authority, part of the Bank of England, and regulated by the Financial Conduct Authority and Prudential Regulation Authority.

OSB primarily targets market sub-sectors that offer high growth potential and attractive risk-adjusted returns in which it can take a leading position and where it has established expertise, platforms and capabilities. These include private rented sector Buy-to-Let, commercial and semi-commercial mortgages, residential development finance, bespoke and specialist residential lending and secured funding lines. OSB originates organically through specialist brokers and independent financial advisers. It is differentiated through its use of high skilled, bespoke underwriting and efficient operating model.

OSB is predominantly funded by retail savings originated through the long established Kent Reliance name, which includes online and postal channels, as well as a network of branches in the South East of England. Diversification of funding is currently provided by access to a securitisation programme and the Term Funding Scheme.

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1. Before exceptional items of £nil (2016: exceptional items of £24.9m, see Alternative performance measures and Exceptional items in the Financial review for further details).
2. Prior to 2017, OSB deducted coupons on equity Perpetual Subordinated Bonds ('PSBs') accounted for as dividends from underlying profit before and after tax, net interest margin and cost to income ratio. Following a review of market practice in advance of the Bank's AT1 issue in May 2017, OSB no longer deducts these coupons from the calculation of these key performance indicators. The comparatives have been restated accordingly (see Financial review for further details). Interest payments on AT1 securities classified as dividends are treated in the same way.
3. Administrative expenses, including depreciation and amortisation, as a percentage of total income.
4. Net interest income as a percentage of average interest bearing assets including off balance sheet Funding for Lending Scheme (FLS) drawings.
5. Impairment losses expressed as a percentage of average gross loans and advances.

6. Profit after tax excluding exceptional items after tax of £nil in 2017 (2016: after tax exceptional items of £18.5m, see Alternative performance measures and Exceptional items in the Financial review for further details), and after deducting coupons on equity PSBs, including the tax effect of £0.7m (2016: £0.9m) and coupons on AT1 securities, including the tax effect of £2.0m, as a percentage of average shareholders' equity (excluding equity PSBs of £22m and AT1 securities of £60m) of £446.6m in 2017 and £346.9m in 2016.
7. Underlying profit after taxation and after deducting coupons on equity PSBs, including tax effect of £0.7m (2016: £0.9m) and AT1 coupons, including tax effect of £2.0m, divided by the weighted average number of ordinary shares in issue.
8. Representing 25% of underlying profit after tax. To be paid on 16 May 2018, subject to approval at the Annual General Meeting on 10 May 2018, with a record date of 23 March 2018. For 2016, the dividend of 7.6p per share represented a final two-thirds dividend.
9. Statutory profit after taxation divided by the weighted average number of ordinary shares in issue.
10. Excluding the impact of FLS/TFS drawdowns. The unadjusted ratio was 109% as at 31 December 2017 (2016: 100%).
11. Portfolio arrears rate (excluding legacy problem loan book) of accounts for which there are missed or overdue payments by more than three months.

Non-IFRS performance measures

OneSavings Bank believes that the non-IFRS performance measures included in this document provide valuable information to the readers as they enable the reader to identify a more consistent basis for comparing the business' performance between financial periods, and provide more detail concerning the elements of performance which the Group is most directly able to influence or are relevant for an assessment of the Group. They also reflect an important aspect of the way in which operating targets are defined and performance is monitored by OneSavings Bank's Board. However, any non-IFRS performance measures in this document are not a substitute for IFRS measures and readers should consider the IFRS measures as well. Refer to Alternative performance measures in the Financial review for further details, reconciliations and calculations of non-IFRS performance measures included throughout this document, and the most directly comparable IFRS measures.

Important disclaimer

This document should be read in conjunction with the documents distributed by OneSavings Bank plc ('OSB') through the Regulatory News Service ('RNS'). This document contains certain forward-looking statements, beliefs or opinions, including statements with respect to the business, strategy and plans of OSB and its current goals and expectations relating to its future financial condition, performance and results. Such forward-looking statements include, without limitation, those preceded by, followed by or that include the words 'targets', 'believes', 'estimates', 'expects', 'aims', 'intends', 'will', 'may', 'anticipates', 'projects', 'plans', 'forecasts', 'outlook', 'likely', 'guidance', 'trends', 'future', 'would', 'could', 'should' or similar expressions or negatives thereof. Statements that are not historical facts, including statements about OSB's, its directors' and/or management's beliefs and expectations, are forward-looking statements. By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend upon circumstances that may or may not occur in the future. Factors that could cause actual business, strategy, plans and/or results (including but not limited to the payment of dividends) to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements made by OSB or on its behalf include, but are not limited to: general economic and business conditions in the UK and internationally; market related trends and developments; fluctuations in exchange rates, stock markets, inflation, deflation, interest rates and currencies; policies of the Bank of England, the European Central Bank and other G8 central banks; the ability to access sufficient sources of capital, liquidity and funding when required; changes to OSB's credit ratings; the ability to derive cost savings; changing demographic developments, and changing customer behaviour, including consumer spending, saving and borrowing habits; changes in customer preferences; changes to borrower or counterparty credit quality; instability in the global financial markets, including Eurozone instability, the potential for countries to exit the European Union (the "EU") or the Eurozone, and the impact of any sovereign credit rating downgrade or other sovereign financial issues; technological changes and risks to cyber security; natural and other disasters, adverse weather and similar contingencies outside OSB's control; inadequate or failed internal or external processes, people and systems; terrorist acts and other acts of war or hostility and responses to those acts; geopolitical, pandemic or other such events; changes in laws, regulations, taxation, accounting standards or practices, including as a result of an exit by the UK from the EU; regulatory capital or liquidity requirements and similar contingencies outside OSB's control; the policies and actions of governmental or regulatory authorities in the UK, the EU or elsewhere including the implementation and interpretation of key legislation and regulation; the ability to attract and retain senior management and other employees; the extent of any future impairment charges or write-downs caused by, but not limited to, depressed asset valuations, market disruptions and illiquid markets; market relating trends and developments; exposure to regulatory scrutiny, legal proceedings, regulatory investigations or complaints; changes in competition and pricing environments; the inability to hedge certain risks economically; the adequacy of loss reserves; the actions of competitors, including non-bank financial services and lending companies; and the success of OSB in managing the risks of the foregoing.

No representation or warranty is made that any of these statements or forecasts will come to pass or that any forecast results will be achieved. Any forward-looking statements made in this document speak only as of the date they are made and it should not be assumed that they have been revised or updated in the light of new information of future events. Except as required by the Prudential Regulation Authority, the Financial Conduct Authority, the London Stock Exchange PLC or applicable law, OSB expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained in this document to reflect any change in OSB's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based. The information, statements and opinions contained in this document and subsequent discussion do not constitute a public offer under any applicable law or an offer to sell any securities or financial instruments or any advice or recommendation with respect to such securities or financial instruments.

Chief Executive's Statement

I am delighted to report another excellent year for OneSavings Bank ('OSB'). The Group's clear strategy and unique business model have proven robust as we successfully navigated significant regulatory and tax changes during the year. Underlying basic earnings per share grew by 23% to 51.1 pence with underlying pre-tax profit up by 21% to £167.7m. We finished the year with a strong balance sheet, a high quality secured asset portfolio and an excellent reputation for customer service. Our strategy continues to provide the platform for us to grow and develop our business.

The Group grew its loan book by 23% to £7.3bn in 2017, whilst maintaining its strong discipline on understanding and pricing for risk, and delivering a stable net interest margin ('NIM') of 3.16% for the year.

Balance sheet growth was achieved whilst delivering a best in class return on equity of 28% and a low cost to income ratio of 27%. Our CET1 capital ratio increased to 13.7% from 13.3% in 2016, demonstrating the strength of our organic capital generation capability to support significant growth through profitability. I am very pleased that we further optimised our capital structure through the issuance of £60m of Additional Tier 1 securities ('AT1 securities') in May 2017.

The Board is recommending a final dividend of 9.3 pence per share. Together with the interim dividend of 3.5 pence this gives a total dividend per share for the year of 12.8 pence, in line with our stated dividend policy.

Best specialist lender

OneSavings Bank continued to grow its loan book through its specialist lending brands, with total organic origination up by 14% in 2017 to £2.6bn. Our core Buy-to-Let lending sub-segment grew by 39% to £5.0bn, with our target audience of professional landlords continuing to deliver strong application and completion volumes.

This performance has been achieved despite the overall Buy-to-Let market shrinking in response to tax and regulatory changes. These changes have reduced the attractiveness of the sector to amateur investors, whilst largely maintaining the interest of professional landlords, and have driven the reduction in gross advances from £40.6bn in 2016 to £35.8bn[1] in 2017. In this context, the Bank's performance demonstrates the sustainable strength of our proposition targeted at professional landlords, particularly our specialist, manual underwriting, and our deep relationships with mortgage intermediaries.

New Buy-to-Let mortgage origination increased during 2017, reflecting our specialism and expertise in lending to limited companies and large portfolio landlords. Professional/multi-property landlords accounted for 80% of completions for OSB by value during 2017, up from 75% in 2016.

We have also seen significant growth in the commercial side of our Buy-to-Let/SME segment. Organic origination grew to £176m, as we focused on innovation and building scale in our established InterBay Commercial business. In March, we successfully piloted an entry to the bespoke bridging market, again leveraging the Bank's strengths in asset risk assessment and manual underwriting.

We saw a reduction in originations in the residential segment in 2017. This contributed to the first charge gross loan book reducing to £1,241m from £1,322m in 2016, with new organic lending more than offset by redemptions in the back book and acquired mortgages in run-off. However, we see opportunities for growth in the residential market in 2018 and beyond.

I am pleased that our more cyclical commercial businesses continued to perform strongly. The Bank's Heritable Development Finance business provides development finance to smaller residential developers, with a preference for forging relationships with those active outside prime central London.

The business continued to grow in 2017, in spite of new entrants to the market, as customers sought an experienced and pragmatic lender.

In addition, we have also grown the provision of secured funding lines to other lenders that operate in certain high yielding, specialist sub-segments, such as residential bridge finance and asset finance.

Whilst we continue to carefully consider inorganic acquisition opportunities, market pricing did not meet our high return targets during the year.

Our broker net promoter score ('NPS') recovered from the short-term negative NPS of -7 in the first half of the year, the result of a surge in Buy-to-Let volumes. For the second half of the year, our NPS was +25.

We made significant investment in our sales capability and continued to gain recognition from mortgage customers and intermediaries, winning multiple awards during the year. I am particularly pleased that OSB won the Mortgage Strategy Awards Best Specialist Lender and The Mortgage Introducer Awards Specialist Lender of the Year in 2017.

To encourage greater levels of retention amongst borrowers reaching the end of their initial product term, OSB offers a mortgage product transfer scheme ('Choices'). Under this programme, borrowers are encouraged to engage with their broker to receive advice and select from a bespoke product set. Since the implementation of the scheme in mid-2016, we have seen a consistently strong proportion of our borrowers choose a new product within three months of their initial product ending, at around 60% by December 2017. This is driven by success in switching borrowers who were otherwise remaining on standard variable rate ('SVR') and who, by definition, were therefore in the market for other lenders.

Sustainable funding model with award winning savings

Our stable and award winning retail funding franchise continues to support lending growth, with retail deposits up 12% to £6.7bn during the year. Over 27,000 new savings customers joined the Bank during 2017 and our successful programme of creating long-term savings relationships by offering market competitive rates to all customers, including those with maturing fixed rate bonds and ISAs, continued to deliver a very strong 90% retention rate. The strength and fairness of our retail savings proposition, coupled with excellent customer service and high retention rates, continues to allow the Bank to raise significant funds without needing to price at the very top of the best buy tables and provides a consistent and stable source of liquidity.

I am delighted that Kent Reliance has been recognised by Moneyfacts in 2017 as the Best Cash ISA Provider for the fifth year running. The Bank also received the ISA Provider of the Year Award from Consumer Moneyfacts for the second consecutive year. These awards are a testament to our savings proposition and to the outstanding customer service delivered by our staff.

The Bank remained predominantly retail funded during 2017, with a loan to deposit ratio for the year of 92%[2] delivering on our strategy to primarily fund our loan book using retail deposits. We continued to make judicious use of the Bank of England's Funding for Lending Scheme ('FLS') and the Term Funding Scheme ('TFS'), drawing down additional net funding of £624m in the year. The Bank completed its planned transition out of the FLS into the TFS by year end. As at 31 December 2017, TFS drawdowns stood at £1.25bn.

Leveraging our unique business model

As the Group has grown, costs and efficiency have remained a key focus for the business, resulting in a stable cost to income ratio of 27% (2016: 27%[3]) despite significant investment during the year. We continued to invest in our risk management and modelling capabilities in preparation for IFRS 9 and our planned internal ratings based ('IRB') application. We also invested in technology to offer an automated solution to brokers to help the Bank meet the PRA's new specialist underwriting rules in an efficient way.

OSBIndia continues to undertake a range of primary processing services at a significantly lower cost than an equivalent UK-based operation and with very high quality levels. I am especially pleased that we achieved this whilst maintaining our focus on customers, borne out by an increase in customer NPS to an outstanding 62% (2016: 59%).

We continue to differentiate ourselves from the competition by offering well-defined propositions in high margin, underserved markets, where we have the experience, as well as the internal and intermediary infrastructure, to successfully develop and service those markets.

Building our business for the future

The Group continued to exercise strong diligence over loan and customer assessment. The loan loss ratio fell to 7bps in the year to 31 December 2017 (2016: 16bps) mainly due to assumption updates that took place in 2016. We remain particularly pleased with the performance of the front book of mortgages. From more than 38,500 loans totaling £8.3bn of new organic originations since the Bank's creation in February 2011, we have only 137 cases of arrears over three months in duration, with an aggregate balance of £18.4m and an average loan to value ('LTV') of 63%, reflecting the continued strength of the Bank's underwriting and lending criteria.

The weighted average LTV of the overall mortgage book remained low at 64% at the end of 2017, with an average LTV of 69% on new origination during the year.

In 2017 we saw the market adjusting to the new Buy-to-Let underwriting standards, including ensuring that lenders reflect the changes to personal tax on landlords within their affordability assessments. We have seen a clear trend for borrowers to seek to mitigate this by opting to borrow via a limited company during 2016 and 2017, with a continued increase in the proportion of purchase applications via limited companies for our main Buy-to-Let brand, Kent Reliance, to 69% in 2017. The Group has always specialised in lending to limited companies, and given market trends, this gives us a competitive advantage over those lenders without such a capability.

From 1 January 2017, The Prudential Regulation Authority ('PRA') required lenders to adopt more stringent affordability assessments. We have always assessed affordability for borrowers through our specialist underwriting model and applied stringent stress tests, so were well-placed to benefit from these changes. This can be seen in our weighted average interest coverage ratio ('ICR') for Buy-to-Let origination during 2017, which increased to 185%, demonstrating our cautious approach to the assessment of customer affordability.

Further market-wide measures to strengthen underwriting standards were implemented from October 2017. We already substantively met the regulatory requirements for assessment of landlords with four or more mortgaged properties, and sought to enhance this proposition through the use of technology, creating a simple and automated way of providing comprehensive portfolio information. This has been embedded within our underwriting process to create a strong proposition for brokers and borrowers alike.

These measures and an expectation of further interest rate rises also caused a shift in the demand amongst our professional landlords towards five year fixed rate products which accounted for c. 43% of our Buy-to-Let completions in 2017. Competition has increased in this area, and the market has not yet fully repriced following the Bank of England base rate rise in November 2017 or for subsequent widening of swap spreads, putting pressure on margins.

Outlook

Trading conditions in our core markets are positive and current application levels are strong. In line with UK Finance forecasts, the overall Buy-to-Let market is expected to contract further in 2018, however, we expect to continue to grow market share through the relevance of our proposition to professional landlords.

The Group's IFRS 9 models and first generation IRB models were delivered on schedule in late 2016 and we ran the models in parallel throughout 2017. We remain pleased with progress towards our IRB application and also welcomed the recalibration of risk weights in the final revisions to the Basel III reforms on standardised capital requirements published in December 2017. We believe that these new calibrations combined with the final IRB output floor will be beneficial to the Bank's capital requirements, however we remain cautious until the final rules are adopted.

The market sub-segments targeted by OSB, principally professional landlords, including limited companies, have remained strong despite the overall slowdown in the Buy-to-Let market in 2017. We remain confident in the underlying strength of the Private Rented Sector and believe that we are well-placed as the Buy-to-Let market continues to professionalise in response to tax and regulatory changes. We will continue to concentrate on what we have proven we do best; using our relationships, manual underwriting expertise and secured lending strategy to lend responsibly to our customers.

We see opportunities for growth in other segments of the lending market where we already have expertise and a platform to build from. In particular, we expect to grow commercial and bridge finance lending through our InterBay Commercial brand and see further opportunities to grow our residential lending franchise.

We will remain predominantly retail funded, aiming to fund our loan book through our Kent Reliance savings brand. In addition, we intend to invest in our online savings platform during 2018 to attract a broader customer base and grow SME and other lower cost deposits in future years. Our additional liquidity will continue to come from wholesale funding, and we intend to return to the securitisation market during 2018 following the closure of the TFS in February. We drew down an additional £250m in 2018 before the scheme closed, bringing the total balance to £1.5bn. Over time we will use these different funding sources to optimise our cost of funds.

The pipeline of regulatory change continues to grow, with GDPR and PSD 2 both going live in 2018 and work continuing on IRB and other smaller regulatory projects. We expect to expense c. £7m on regulatory projects in 2018, around double the total in 2017. In addition, we plan to continue to invest in our technology infrastructure, mortgage origination system and online savings platforms to support our future growth strategy and enable us to broaden our reach into adjacent markets, such as sub-segments of residential mortgages, where we see opportunities, particularly once we transition to IRB. All of these projects are expected to lead to a significant increase in operating costs in 2018. However, we expect to offset this in part, by delivering further efficiencies in the cost of running the Bank on a 'business as usual' basis, by continuing to focus on cost discipline and leveraging our unique operating platform in India.

We are now live with IFRS 9 after a successful parallel run throughout 2017. The day one impact of the implementation of IFRS 9 is an increase in the provisions of c. £4m, representing 9bps on the Bank's CET1 ratio as at 31 December 2017, on an end game basis, reflecting the strength of security underpinning our loan book.

Our achievements in 2017 are a testament to the management and staff of OSB and I would like to thank my colleagues for their hard work and commitment throughout the year.

Looking forward to 2018

Over the coming year, organic lending through the Buy-to-Let segment will remain the key driver of loan book growth, but we expect to grow our residential lending, and our commercial and bridge finance lending through our InterBay Commercial brand.

We expect to deliver net loan book growth in the mid teens in 2018 and NIM of c. 3%, reflecting current asset pricing, in particular for five year fixed loans and an expectation of a rising cost of retail funds after the end of TFS. We anticipate a cost to income ratio of c. 30%, reflecting the significant increase in the cost of regulation and planned additional investment in the business.

We start 2018 with a fully loaded CET1 ratio of 13.7% and a proven organic capital generation capability through profitability. We anticipate maintaining a CET1 ratio at a minimum 12% going forward. Our dividend policy for 2018 remains a payout ratio of at least 25% of underlying profit after taxation attributable to ordinary shareholders.

Our primary growth strategy remains organic origination, but we continue to look at inorganic opportunities, including portfolio purchases, where they meet the Bank's return hurdles.

I believe that OneSavings Bank is well placed to take advantage of opportunities that arise and we remain capable of generating attractive returns for our shareholders.

Andy Golding

Chief Executive Officer
15 March 2018

1. UK Finance, New and outstanding Buy-to-Let new mortgages, 2 Feb 2018.
2. Excluding the impact of TFS/FLS drawdowns. The unadjusted ratio was 109% as at 31 December 2017 (2016: 100%).
3. Prior to 2017, OSB deducted coupons on equity Perpetual Subordinated Bonds ('PSBs') accounted for as dividends from underlying profit before and after tax, net interest margin and cost to income ratio. Following a review of market practice in advance of the Bank's AT1 issue in May 2017, OSB no longer deducts these coupons from the calculation of these key performance indicators. The comparatives have been restated accordingly. Interest payments on AT1 securities classified as dividends are treated in the same way.

Operating and financial review

Business highlights

2017 was another year of exceptional performance underpinned by organic originations of £2.6bn at attractive margins, strong risk management and cost efficiency and discipline.

Net loans and advances grew by 23% in 2017 to £7.3bn. The growth was due primarily to an increase in new lending in the Buy-to-Let sub-segment, as the market became increasingly focused on our core audience of professional landlords. Regulatory change, introducing more complex underwriting standards to the Buy-to-Let industry in 2017, has driven additional business flow to specialist lenders resulting in growth in our market share. This growth was achieved whilst improving the Group's CET1 ratio to 13.7% from 13.3% in 2016, demonstrating the strength of the capital generation capability of the business through profitability. The Group's capital position was further strengthened in May 2017 by the issuance of £60m of Additional Tier 1 capital securities ('AT1 securities'), with the total capital ratio strengthening to 16.9% from 15.1% in 2016 and the leverage ratio also increasing to 6% from 5.5%. The successful issuance of AT1 securities highlights OSB's strong balance sheet and attractive investment proposition to debt investors.

The Group remains focused on organic origination as its core growth strategy and gross new organic lending of £2.6bn in 2017 was up 14% compared with £2.3bn in 2016. OSB continued to experience high demand for its products during 2017, particularly in Buy-to-Let where the Group targets professional landlords with larger portfolios. Buy-to-Let/SME is the Group's largest segment comprising 77% of the gross loan book with Residential Mortgages at 23% as at 31 December 2017. New organic originations in our residential book decreased, which, combined with redemptions in the back book and acquired mortgages in run-off, contributed to the first charge gross loan book reducing to £1,240.6m from £1,322.1m in 2016.

The Bank made no portfolio acquisitions during 2017 (2016: portfolios of first and second charge residential mortgages for £180.7m). However we continue to evaluate selective inorganic opportunities that provide long-term value and meet our strategic objectives when they arise. The Group conducts extensive due diligence when considering any portfolio acquisitions and in 2017, market pricing for deals under consideration did not meet the Group's stringent return conditions.

For all our lending segments, we manually underwrite all risks, providing us with a competitive advantage over more automated lenders, as we are able to identify and understand complex cases that others cannot. The weighted average LTV of the mortgage book remained low at 64% at the end of 2017, with an average LTV of 69% on new origination during the year, reflecting the strength of our balance sheet. Both the loan loss ratio and portfolio arrears rate improved in the year to 7bps and 1.2% respectively (2016: 16bps and 1.4% respectively) further demonstrating our disciplined underwriting and lending criteria. We also have limited exposure to high value properties, with only 4% of our total loan book secured on properties valued at greater than £2m and with an LTV above 65%.

The broker-led Choices mortgage product transfer scheme that we introduced in 2016 has encouraged greater levels of retention amongst those borrowers reaching the end of their initial product term. Since the implementation of the scheme in mid-2016, we have seen a consistently strong proportion of our borrowers choose a new product within three months of their initial product ending, at around 60% by December 2017. This is driven by success in switching borrowers who were otherwise remaining on standard variable rate ('SVR') and who, by definition, were therefore in the market for other lenders.

The Bank continued to offer secured funding lines to non-bank lenders, however kept a cautious approach in light of macroeconomic uncertainty. Total credit approved limits as at 31 December 2017 were £336.6m with total loans outstanding of £122.1m (31 December 2016: £330.2m and £122.3m respectively). During the year, two new funding lines in the Buy-to-Let/SME segment were extended.

The Group remained predominantly retail funded during the year with a loan to deposit ratio of 92%[1] as at 31 December 2017 (2016: 90%[1]).

Our customer-centric strategy of providing transparent savings products which offer long-term value for money continued to deliver high levels of customer satisfaction and loyalty during the year. Our customer net promoter score ('NPS') increased to +62 for 2017 and the maturing fixed term bond and ISA balance retention rate remained strong at 90% (2016: +59 and 87% respectively). Retail deposits were up 12% to £6.7bn as at 31 December 2017.

The business savings account which was introduced in 2016 had a successful year with total deposits constituting just over 1% of the entire savings book, or £69.5m total balance as at 31 December 2017.

Whilst remaining committed to our retail savings franchise, throughout 2017 we complemented it as a funding source by taking advantage of the government funding schemes: Term Funding Scheme ('TFS') and Funding for Lending Scheme ('FLS'). By the end of 2017, the Bank had completed its planned transition out of the FLS into the TFS and as at 31 December 2017, TFS drawdowns stood at £1,250.0m (31 December 2016: TFS at £101.0m and FLS £524.6m). Total funding through the schemes increased by £624.4m in the year.

1. Excluding the impact of TFS/FLS drawdowns. The unadjusted ratio was 109% as at 31 December 2017 (2016: 100%).

Financial overview

The Group reported strong profit growth in 2017. Statutory profit before taxation of £167.7m was 3% higher than in 2016 (2016: £163.1m) despite the £24.9m net gain on exceptional items in the prior year. On an underlying basis, profit before taxation increased by 21% to £167.7m (2016: restated £138.2m[2]). This significant improvement in underlying profitability reflects the strength of our lending and funding franchises and our efficient operating model. Statutory and underlying basic earnings per share ('EPS') strengthened to 51.1p (2016: 49.4p and 41.7p respectively).

Our focus on cost discipline and efficiency continued throughout 2017, helping to deliver a very strong cost to income ratio of 27% (2016: 27%[2]) despite increased investment in the business and in meeting the growing cost of regulation.

Return on equity remained strong at 28% (2016: 29%) despite our strengthened capital position.

The Board is recommending a final dividend of 9.3 pence per share, which together with the interim dividend of 3.5 pence per share, represents 25% of underlying profit after taxation attributable to ordinary shareholders for the year, in line with the Bank's stated dividend policy.

2. Prior to 2017, OSB deducted coupons on equity PSBs accounted for as dividends from underlying profit before and after tax, net interest margin and cost to income ratio. Following a review of market practice in advance of the Bank's AT1 issue in May 2017, OSB no longer deducts these coupons from the calculation of these key performance indicators. The comparatives have been restated accordingly. Interest payments on AT1 securities classified as dividends are treated in the same way.

Segmental review

The following tables show the Group's loans and advances, risk weighted assets and contribution to profit by segment.

31 December 2017, £m	BTL/SME[1]	Residential	Total
Gross loans to customers	5,654.1	1,673.5	7,327.6
Provision for impairment losses	(13.2)	(8.4)	(21.6)
Net loans to customers	5,640.9	1,665.1	7,306.0
Risk weighted assets	2,642.8	705.7	3,348.5
Net interest income	177.1	68.3	245.4
Other income/expense	(1.5)	(5.8)	(7.3)
Total income	175.6	62.5	238.1
Impairment losses	(0.8)	(3.6)	(4.4)
Contribution to profit	174.8	58.9	233.7

31 December 2016, £m	BTL/SME restated[1]	Residential	Total
Gross loans to customers	4,104.3	1,859.9	5,964.2
Provision for impairment losses	(17.2)	(7.8)	(25.0)
Net loans to customers	4,087.1	1,852.1	5,939.2
Risk weighted assets	1,944.3	798.7	2,743.0
Net interest income	135.2	71.4	206.6
Other income/expense	(0.5)	(4.7)	(5.2)
Total income	134.7	66.7	201.4
Impairment losses	(1.8)	(7.2)	(9.0)
Contribution to profit	132.9	59.5	192.4

1. The personal loan portfolio has largely completed its run-off and is therefore no longer considered as a separate segment by the Group. The remaining net loan book of £0.9m (31 December 2016: £9.1m) and negative contribution to profit for the period of £0.8m (2016: contribution to profit of £2.7m) have been reported in the Buy-to-Let/SME segment with comparatives restated accordingly.

Buy-to-Let/SME

Buy-to-Let/SME sub-segment: gross loans

	Group 31-Dec-2017 £m	Group 31-Dec-2016 £m
Buy-to-Let	**5,033.8**	3,613.3
Commercial	**370.8**	268.3
Residential development	**143.9**	141.6
Funding lines	**104.5**	71.7
Personal loans[1]	**1.1**	9.4
Total	**5,654.1**	4,104.3

1. The personal loan portfolio has largely completed its run-off and is therefore no longer considered as a separate segment by the Group. The remaining net loan book of £0.9m (31 December 2016: £9.1m) and negative contribution to profit for the period of £0.8m (2016: contribution to profit of £2.7m) have been reported in the Buy-to-Let/SME segment with comparatives restated accordingly.

The Buy-to-Let market contracted during the year in response to tax and regulatory changes, which led to increased withdrawal of the amateur landlord from the private rented sector. According to UK Finance, Buy-to-Let gross advances in 2017 fell by 12% to £35.8bn[2] (2016: £40.6bn) with the decrease also reflecting the spike in lending recorded in March 2016 ahead of the stamp duty land tax ('SDLT') change. Even though the overall Buy-to-Let market shrank in 2017, the demand from professional landlords with larger portfolios continued its momentum, leading to strong growth in our market share over the year from c. 4% of new Buy-to-Let mortgages in 2016 to c. 6% in 2017. Professional/multi-property landlords accounted for 80% of completions for OSB by value during 2017, up from 75% in 2016.

The Group significantly increased its volume of new organic lending in this segment in 2017 to £2.4bn, an increase of 23% on 2016 new organic lending of £1.9bn. This included a significant increase in the Buy-to-Let and Commercial sub-segments lending through the Kent Reliance and InterBay brands. We continued to see strong growth opportunities particularly in Buy-to-Let with gross loans of £5,033.8m at 31 December 2017 (2016: £3,613.3m), weighted average LTV of 69% and average loan size of c. £250,000.

A significant proportion of the Buy-to-Let market comes from refinancing. OSB's Buy-to-Let refinancing percentage was 60% during 2017, up from 58% in 2016.

From 1 October 2017, more comprehensive underwriting rules, including affordability assessment for multi-property landlords came into effect. We have always assessed affordability for borrowers through our specialist underwriting model and apply stringent stress tests. Our weighted average interest coverage ratio ('ICR') for Buy-to-Let origination during 2017 increased to 185% (2016: 171%). The new underwriting rules and an expectation of further interest rate rises also caused a shift in the demand amongst our professional landlords towards five year fixed rate products, which accounted for c. 43% of Buy-to-Let completions in 2017.

In addition, to aid brokers in complying with the new underwriting rules, OSB partnered with a technology provider to develop a bespoke tool for assessing the health of a landlord's overall property portfolio, the first of its kind in the market.

Recent tax changes also had an impact on how borrowers structure their portfolios. In 2016, we saw a clear trend for borrowers to form limited companies in order to mitigate reductions in yield resulting from changes to personal taxation, and in 2017 OSB saw an increase in applications from limited companies for our main Buy-to-Let brand Kent Reliance, from 42% in 2016 to 69% in 2017.

We invested in sales capability across all of our lending brands and attracted new talent from large lenders in the year. Through the Kent Reliance and InterBay brands, the Bank distributes via intermediaries throughout England and Wales with a bias towards properties in London and the South East, where the demand supply gap is widest and most sustainable. We have further extended the geographical coverage of our business through investment in the intermediary sales team, ensuring we are seeing appropriate opportunities in other regions.

We have grown our commercial lending with a gross value of the portfolio at £370.8m as at 31 December 2017 (2016: £268.3m), low weighted average LTV of 63% and average loan size of £330,000. In March, we successfully piloted an entry to the bespoke bridging market, again leveraging the Bank's strengths in asset risk assessment and manual underwriting.

The Bank's Heritable Development Finance business provides development finance to smaller residential developers, with a preference for forging relationships with those active outside prime central London. The business continued to grow in spite of new entrants to the market, as customers sought an experienced and cautious lender. However, in line with our prudent approach given macroeconomic uncertainty, the number of potential development schemes which have withstood the business' stringent stress testing has reduced significantly. The residential development funding gross loan book at the end of 2017 was £143.9m, with a further £78.0m committed (31 December 2016: £141.6m and £70.0m respectively). Gross advances during 2017 totalled £123.7m (31 December 2016: £98.4m). Since inception the business has written £479m of loans.

In addition, the Bank continued to grow the provision of secured funding lines it provides to non-bank lenders which operate in certain high-yielding, specialist sub-segments, such as bridging finance and asset finance. Total credit approved limits as at 31 December 2017 were £303.0m with total loans outstanding of £104.5m (31 December 2016: £244.0m and £71.7m respectively). During 2017, two new funding lines were added. The pipeline remains robust, however given the macroeconomic uncertainties, the Bank continues to adopt a cautious approach.

OSB's combined Buy-to-Let/SME net loan book grew by 38% in 2017 to £5,640.9m (2016: restated £4,087.1m[1]) due to the gross new lending in the year, partially offset by back book redemptions, and is the Group's largest segment. Buy-to-Let/SME made a contribution to profit of £174.8m in 2017, up 32% compared to £132.9m[1] in 2016, primarily due to the growth in the loan book and low impairment losses of £0.8m (2016: restated £1.8m[1]).

The Group remains highly focused on the credit quality of new lending as demonstrated by the average LTV in the Buy-to-Let/SME segment as at 31 December 2017 of 69% (31 December 2016: 69%) with only 0.7% of loans exceeding 90% LTV (31 December 2016: 0.4%). The average LTV for new Buy-to-Let/SME origination was 70% (2016: 70%).

2. UK Finance, New and outstanding buy-to-let new mortgages, UK, MM17, 2 February 2018.

Residential mortgages

Residential sub-segment: gross loans

	Group 31-Dec-2017 £m	Group 31-Dec-2016 £m
First charge	**1,240.6**	1,322.1
Second charge	**415.3**	487.2
Funding lines	**17.6**	50.6
Total	**1,673.5**	1,859.9

During the year, the Group organically originated residential lending of £243.9m (2016: £382.1m). We saw a significant reduction in originations in the residential sector in 2017. This contributed to the first charge gross loan book reducing to £1,240.6m from £1,322.1m in 2016, with new organic lending more than offset by redemptions in the back book and acquired mortgages in run-off.

Organic lending remains the Group's core strategy, however we continue to actively consider inorganic opportunities as they arise, particularly where we have in-house servicing expertise. However, in 2017, the Group made no acquisitions of portfolios due to market pricing not meeting our return hurdles (2016: portfolios of first and second charge mortgages for £180.7m).

Our Kent Reliance brand provides bespoke first charge mortgages, typically to prime credit quality borrowers with more complex circumstances, for example high net worth borrowers with multiple income sources and self-employed borrowers. These circumstances often preclude them from the mainstream market, where most lenders favour automated decision making over manual underwriting.

Kent Reliance also operates in the shared ownership market, where borrowers buy a property in conjunction with a housing association.

Our second charge mortgage brand, Prestige Finance, provides secured finance to good credit quality borrowers who are seeking a loan to raise funds rather than refinancing their first charge mortgage. Competitive pressure in the second charge market caused price reductions and we allowed our market share to fall to ensure we continue to appropriately price for risk. The second charge residential loan book had a gross value as at 31 December 2017 of £415.3m (2016: £487.2m).

OSB continued to provide secured funding lines to non-bank lenders which operate in certain high-yielding, specialist sub-segments, such as residential bridge finance. The Bank continued its cautious approach in the more cyclical businesses given macroeconomic uncertainty. Total credit approved limits at 31 December 2017 were £33.6m with total loans outstanding of £17.6m (2016: £86.2m and £50.6m respectively). During 2017, one facility of £34.4m matured.

OSB's total residential loan portfolio had a net carrying value of £1,665.1m as at 31 December 2017 (2016: £1,852.1m). The average LTV remained low at 56% (2016: 58%) with only 3% of loans by value with LTVs exceeding 90% (2016: 3%). The average LTV of new residential origination during 2017 was 65% (2016: 66%).

Residential mortgages made a contribution to Group profit of £58.9m in 2017, down 1% (2016: £59.5m), reflecting the fall in the loan book, partially offset by the benefit of lower cost of funds and impairment losses. Impairment losses in 2016 included the impact of additional prudence in collectively assessed provision assumptions following the EU referendum result.

Financial review

Summary Profit or Loss	**Group 31/12/2017 £m**	**Group 31/12/2016 £m**
Net interest income	**245.4**	206.6
Net losses on financial instruments	**(6.3)**	(4.3)
Net fees and commissions	**0.5**	1.7
External servicing fees	**(1.5)**	(2.6)
Administrative expenses[1]	**(65.1)**	(53.7)
FSCS and other regulatory provisions	**(0.9)**	(0.5)
Impairment losses	**(4.4)**	(9.0)
Exceptional items	**-**	24.9
Profit before taxation	**167.7**	163.1
Profit after taxation	**126.9**	120.9
Underlying profit before taxation[3]	**167.7**	138.2[2]
Underlying profit after taxation[3]	**126.9**	102.4[2]

Key ratios		
Net interest margin[3]	**316bps**	316bps[2]
Cost to income ratio[3]	**27%**	27%[2]
Management expense ratio[4]	**0.86%**	0.86%
Loan loss ratio[3]	**0.07%**	0.16%
Basic EPS[3], pence per share	**51.1**	49.4
Underlying basic EPS[3], pence per share	**51.1**	41.7
Return on equity[3]	**28%**	29%
Dividend per share, pence per share	**12.8**	10.5

Extracts from the Statement of Financial Position

	£m	**£m**
Loans and advances	**7,306.0**	5,939.2
Retail deposits	**6,650.3**	5,952.4
Total assets	**8,589.1**	6,580.9

Key ratios		
Liquidity ratio[5]	**15.2%**	17.9%
Common equity tier 1 ratio[6]	**13.7%**	13.3%
Total capital ratio	**16.9%**	15.1%
Leverage ratio	**6.0%**	5.5%

1. Including depreciation and amortisation.
2. Prior to 2017, OSB deducted coupons on equity Perpetual Subordinated Bonds ('PSBs') accounted for as dividends from underlying profit before and after tax, net interest margin and cost to income ratio. Following a review of market practice in advance of the Bank's AT1 issue in May 2017, OSB no longer deducts these coupons from the calculation of these key performance indicators. The comparatives have been restated accordingly. Interest payments on AT1 securities classified as dividends are treated in the same way.
3. See definition in key performance indicators table on page 1.
4. Administrative expenses including depreciation and amortisation as a percentage of average total assets.
5. Liquid assets as a percentage of funding liabilities.
6. Fully-loaded under Basel III /CRD IV.

Alternative performance measures

OSB believes that the use of alternative performance measures ('APMs') for profitability and earnings per share provides valuable information to the readers of the financial statements and presents a more consistent basis for comparing the Group's performance between financial periods, by adjusting for exceptional non-recurring items. APMs also reflect an important aspect of the way in which operating targets are defined and performance is monitored by the Board. However, any APMs in this document are not a substitute for IFRS measures and readers should consider the IFRS measures as well.

Reconciliation of statutory profit to underlying profit

	Profit before taxation		**Profit after taxation**	
	Group 31-Dec-2017 £m	**Group 31-Dec-2016 £m**	**Group 31-Dec-2017 £m**	**Group 31-Dec-2016 £m**
Statutory profit	**167.7**	163.1	**126.9**	120.9
Gain on Rochester 1 disposal	**-**	(34.7)	**-**	(25.8)
Exceptional amortisation of fair value adjustments on hedged assets	**-**	9.8	**-**	7.3
Underlying profit	**167.7**	138.2	**126.9**	102.4

Statutory basic EPS of 51.1 pence per share (2016: 49.4 pence per share) is calculated by dividing profit attributable to ordinary shareholders of £124.2m (2016: £120.0m) which is profit after taxation of £126.9m (2016: £120.9m) less coupons on equity PSBs, including the tax effect of £0.7m (2016: £0.9m) and coupons on AT1 securities, including the tax effect of £2.0m (2016: £nil) by the weighted average number of ordinary shares in issue during the year of 243.2m (2016: 243.1m).

Underlying basic EPS of 51.1 pence per share (2016: 41.7 pence per share) is calculated by dividing underlying profit attributable to ordinary shareholders of £124.2m (2016: £101.5m), which is underlying profit after taxation of £126.9m (2016: restated £102.4m) less coupons on equity PSBs, including the tax effect of £0.7m (2016: £0.9m) and coupons on AT1 securities of £2.0m (2016: £nil) by the weighted average number of ordinary shares in issue during the year of 243.2m (2016: 243.1m).

Prior to 2017, OSB deducted coupons on equity PSBs accounted for as dividends from underlying profit before and after tax. Following a review of market practice in advance of the Bank's issuance of AT1 securities in May 2017, OSB no longer deducts these coupons and underlying profit before and after taxation for 2016 have been restated throughout this document accordingly.

The table below illustrates the key ratios under previous and current methods and the impact of the change in calculation methodology.

Change in key ratio calculation

Cost to income ratio	2017 %	2016 %
Previous method	**27**	27
Add back coupons on equity PSBs	**(0)**	(0)
Current method	**27**	27

Net interest margin		
Previous method	**3.15**	3.14
Add back coupons on equity PSBs	**0.01**	0.02
Current method	**3.16**	3.16

Underlying profit before tax	2017 £m	2016 £m
Previous method	**166.7**	137.0
Add back coupons on equity PSBs	**1.0**	1.2
Current method	**167.7**	138.2

Underlying profit after tax		
Previous method	**126.2**	101.5
Add back coupons on equity PSBs	**0.7**	0.9
Current method	**126.9**	102.4

Strong profit growth

The Group reported profit growth of 3% in 2017 with profit before taxation of £167.7m (2016: £163.1m including net gain from exceptional items of £24.9m). On an underlying basis, the Bank recorded a 21% increase in underlying profit before taxation to £167.7m (2016: restated £138.2m[1]) reflecting strong balance sheet growth and a stable net interest margin combined with continued focus on cost discipline and efficiency.

Profit after taxation in 2017 increased by 5% to £126.9m (2016: £120.9m including the net gain after taxation from exceptional items of £18.5m). On an underlying basis, profit after taxation increased by 24% to £126.9m (2016: restated £102.4m[1]). The Group's effective tax rate was 24.1%[2] in 2017 (2016: 25.6%), with a lower proportion of the Group's profits subject to the Bank Corporation Tax Surcharge.

Net interest margin

The Group reported an increase in net interest income of 19% to £245.4m in 2017 (2016: £206.6m) reflecting the growth in the loan book and a stable NIM of 316bps (2016: restated 316bps[1]). The stable NIM in 2017 represents a reduction in asset yields in line with the falling cost of funds.

The average cost of retail funds fell year on year, although market rates started to rise again in 2017.

The Bank benefited from a higher average balance in the Bank of England schemes in 2017 versus the prior year and the transition from FLS into the cheaper TFS. As at December 2017, the TFS drawdowns stood at £1,250.0m (2016: £101.0m) and FLS at £nil (2016: £524.6m).

Margins on the Bank's fixed rate mortgage products, particularly five year fixed rate Buy-to-Let, declined in the fourth quarter of 2017 as the market did not reprice these products following the Bank of England base rate rise and subsequent widening of swap spreads in anticipation of future increases in interest rates.

Losses on financial instruments

Fair value loss on financial instruments in 2017 of £6.3m (2016: loss £4.9m) includes £7.3m amortisation of fair value adjustments on hedged assets relating to cancelled swaps (2016: £4.9m). The amortisation of fair value adjustments in both years includes the impact of accelerating the amortisation in line with the run-off of the underlying legacy long-term fixed rate mortgages due to faster than expected prepayments.

In 2016, the Group also made a £0.6m gain on disposal of a portion of non-performing personal loans with a gross value of £10.9m.

Net fees and commission

Net fees and commission income of £0.5m (2016: £1.7m) comprises fees and commission receivable of £1.5m (2016: £2.5m) partially offset by commission expense of £1.0m (2016: £0.8m). Fees and commissions receivable decreased in 2017 due primarily to lower arrangement fees on funding lines.

External servicing fees

External servicing fees decreased to £1.5m in 2017 (2016: £2.6m) due to the transfer of servicing for acquired first charge residential loan books to the Bank's operation in India during the year and the further run-off of the personal loans portfolio.

Efficient and scalable operating platform

Administrative expenses including depreciation were up 21% to £65.1m in 2017 (2016: £53.7m), reflecting the growth in the business and the increased demands of regulation, including projects relating to IFRS 9 and an internal ratings based approach to risk weights ('IRB').

The Group's cost to income ratio of 27% and the management expense ratio of 0.86% remained stable (2016: 27%[1] and 0.86% respectively) despite the increased cost of regulation, reflecting the Bank's focus on efficiency and use of its scalable low cost back office based in Bangalore, India.

FSCS and other regulatory provisions

Regulatory provisions expense of £0.9m (2016: £0.5m) includes levies due to the Financial Services Compensation Scheme ('FSCS') which continued to decrease and other regulatory provisions.

Impairment losses

Impairment losses decreased to £4.4m in 2017 (2016: £9.0m) representing 7bps on average gross loans and advances (2016: 16bps). The decrease was primarily due to increased prudency in assumptions introduced in 2016 following the UK referendum vote to leave the EU, as well as lower underlying loan losses on acquired residential portfolios, and the effect of increasing property values reducing potential loss.

The performance of the front book of mortgages remains strong, reflecting the continued strength of the Bank's underwriting and lending criteria. We kept tight control on credit quality, as seen in our reportable arrears statistics. From more than 38,500 loans totalling £8.3bn of new organic originations since the Bank's creation in February 2011, there were only 137 cases of arrears over three months or more as at 31 December 2017, with an aggregate value of just £18.4m and average LTV of 63%.

IFRS 9

We had a successful parallel run of the IFRS 9 models throughout 2017 and were operating live under the new standard from 1 January 2018. The day one impact of the implementation of IFRS 9 is an increase in the provisions of c. £4m, representing 9bps on the Bank's CET1 ratio as at 31 December 2017 on an end game basis, reflecting the strength of security underpinning our loan book.

The Group continues to monitor the performance of the underlying IFRS 9 models whilst assessing the ongoing appropriateness of all key judgement and estimate areas ahead of the full reporting of IFRS 9 impact later in 2018.

Exceptional items

There were no exceptional items in 2017.

Exceptional items in 2016 of £24.9m comprised the gain on disposal of the Bank's entire economic interest in Rochester 1 of £34.7m and an exceptional loss of £9.8m in respect of accelerated amortisation of fair value adjustments on hedged assets relating to legacy back book long-dated swap cancellations, in line with the underlying mortgage asset run-off, due to faster than expected prepayments. The exceptional loss represented the impact of accelerating the amortisation in prior years from 2012 to 2015.

Dividend

The Board recommends a final dividend for 2017 of 9.3 pence per share. Together with the 2017 interim dividend of 3.5 pence per share, this represents 25% of underlying profit after taxation attributable to ordinary shareholders for 2017, in line with the Bank's target dividend pay-out ratio. The proposed final dividend will be paid on 16 May 2018, subject to approval at the AGM on 10 May 2018, with an ex-dividend date of 22 March 2018 and a record date of 23 March 2018.

Balance sheet growth

Net loans and advances grew by 23% in 2017 to £7,306.0m (31 December 2016: £5,939.2m) attributable primarily to an increase in new lending in the Buy-to-Let/SME segment.

Retail deposits and total assets grew by 12% and 30%, respectively in 2017 with additional funding of £624.4m supplied by the FLS and TFS throughout the year. By the end of 2017, the Group had completed its planned transition out of the FLS scheme (31 December 2016: £524.6m) to the TFS with drawings under the scheme of £1,250.0m (31 December 2016: £101.0m).

The TFS drawdowns are offered in the form of collateralised cash loans. The scheme closed to new drawings at the end of February 2018 and the Group has four years from the date of the drawing to repay the existing loans.

Liquidity

OneSavings Bank operates under the PRA's liquidity regime. The Bank operates within a target liquidity runway in excess of the minimum regulatory requirement. In addition, the Bank maintains a strong retention track record on fixed term bond and ISA maturities. As at 31 December 2017, our liquidity coverage ratio of 250% (2016: 239%) was significantly in excess of the 2017 regulatory minimum of 90%, including drawings under the Bank of England FLS and TFS funding facilities. The Group's liquidity ratio as at 31 December 2017 was 15.2% (31 December 2016: 17.9%).

Capital

The Bank's fully-loaded CET1 capital ratio under CRD IV strengthened to 13.7% as at 31 December 2017 (31 December 2016: 13.3%), demonstrating the strong organic capital generation capability of the business to support significant growth through profitability.

We further optimised our capital structure through the issuance of £60m of AT1 securities in May 2017.

The Bank had a total capital ratio of 16.9% and a leverage ratio of 6.0% as at 31 December 2017 (31 December 2016: 15.1% and 5.5% respectively).

The Bank had a Pillar 2a requirement of 1.1% of risk weighted assets as at 31 December 2017 (31 December 2016: 1.2%).

Cash flow statement

In 2017, the Group replaced £524.6m of Bank of England FLS off balance sheet securities with cash drawn down under the TFS. This led to cash and cash equivalents increasing by £680.6m during the year to £1,165.9m as at 31 December 2017 (2016: restated £485.3m[1]).

The Group's loans and advances to customers grew by £1,371.2m during the year, partially funded by an additional £697.9m of deposits from retail customers which mainly contributed to £512.9m of cash used in operating activities. The remaining funding came primarily from additional drawdowns under the TFS, which in conjunction with replacing the FLS securities, totalled £1,149.0m during the year. Together with £59.4m of funding from the issuance of AT1 securities, this generated £1,167.5m of cash from financing activities. Cash generated from investing activities was £26.0m, primarily driven by the sale and maturity of investment securities and the purchase of additional equipment and intangible assets.

In 2016, the Group increased its loans and advances to customers by £1,031.3m. This was partially funded by an additional £588.6m of deposits from retail customers. Collectively, these were the main drivers of the £323.8m (restated[3]) of cash used in operating activities. The remaining funding came primarily from the Group replacing its maturing on balance sheet available for sale investment securities (£309.4m decrease, restated[3]) with off balance sheet securities under the FLS (£363.9m increase) in its liquidity portfolio. Together with £80.2m of cash received from the Rochester 1 disposal, this generated £381.9m (restated[3]) of cash inflows from investing activities. In addition, the Group drew down £101.0m of cash under the TFS which is reflected in the cash generated from financing activities.

1. Prior to 2017, OSB deducted coupons on equity Perpetual Subordinated Bonds ('PSBs') accounted for as dividends from underlying profit before and after tax, net interest margin and cost to income ratio. Following a review of market practice in advance of the Bank's AT1 issue in May 2017, OSB no longer deducts these coupons from the calculation of these key performance indicators. The comparatives have been restated accordingly. Interest payments on AT1 securities classified as dividends are treated in the same way.

2. Effective tax rate excludes £0.4m of adjustments relating to prior years.

Summary cash flow statement

	Group 31-Dec-2017 £m	**Restated[3] Group 31-Dec-2016 £m**
Profit before tax	**167.7**	163.1
Net cash generated/(used in):		
Operating activities	**(512.9)**	(323.8)
Investing activities	**26.0**	381.9
Financing activities	**1,167.5**	56.7
Net increase/(decrease) in cash and cash equivalents	**680.6**	114.8
Cash and cash equivalents at the beginning of the period	**485.3**	370.5
Cash and cash equivalents at the end of the period	**1,165.9**	485.3

3. The 2016 comparatives have been reclassified to include investment securities with maturity less than three months and to exclude encumbered loans and advances to credit institutions within cash and cash equivalents.

Statement of Profit or Loss

For the year ended 31 December 2017

	Group 2017 £m	Group 2016 £m
Interest receivable and similar income	**332.7**	309.5
Interest payable and similar charges	**(87.3)**	(102.9)
Net interest income	**245.4**	206.6
Fair value losses on financial instruments	**(6.3)**	(4.9)
Gains on sales of financial instruments	**-**	0.6
Fees and commissions receivable	**1.5**	2.5
Fees and commissions payable	**(1.0)**	(0.8)
External servicing fees	**(1.5)**	(2.6)
Total income	**238.1**	201.4
Administrative expenses	**(61.6)**	(51.1)
Depreciation and amortisation	**(3.5)**	(2.6)
Impairment losses	**(4.4)**	(9.0)
FSCS and other regulatory provisions	**(0.9)**	(0.5)
Exceptional gain on sale	**-**	34.7
Exceptional accelerated amortisation of fair value adjustments on hedged assets	**-**	(9.8)
Profit before taxation	**167.7**	163.1
Taxation	**(40.8)**	(42.2)
Profit for the year	**126.9**	120.9
Dividend, pence per share	**12.8**	10.5
Earnings per share, pence per share		
Basic	**51.1**	49.4
Diluted	**50.7**	49.0

The above results are derived wholly from continuing operations.

Statement of Other Comprehensive Income

For the year ended 31 December 2017

	Group 2017 £m	Group 2016 £m
Profit for the year	**126.9**	120.9
Items which may be reclassified to profit or loss:		
Fair value changes on available-for-sale securities		
Arising in the year	**0.1**	0.1
Revaluation of foreign operations	**(0.3)**	0.9
Other comprehensive income for the year	**(0.2)**	1.0
Total comprehensive income for the year	**126.7**	121.9

Statement of Financial Position

As at 31 December 2017

	Group 2017 £m	Group 2016 £m
Assets		
Cash in hand	**0.5**	0.4
Loans and advances to credit institutions	**1,187.2**	417.8
Investment securities	**19.1**	141.7
Loans and advances to customers	**7,306.0**	5,939.2
Derivative assets	**6.1**	1.8
Fair value adjustments on hedged assets	**31.9**	46.9
Deferred taxation asset	**5.1**	3.4
Intangible assets	**6.8**	4.7
Property, plant and equipment	**21.5**	13.1
Other assets	**4.9**	11.9
Total assets	**8,589.1**	6,580.9

	Group 2017 £m	Group 2016 £m
Liabilities		
Amounts owed to retail depositors	**6,650.3**	5,952.4
Amounts owed to credit institutions	**1,250.3**	101.7
Amounts owed to other customers	**25.7**	4.0
Derivative liabilities	**21.8**	24.4
Fair value adjustments on hedged liabilities	**-**	1.9
Current taxation liability	**18.3**	21.1
Other liabilities	**16.3**	18.6
FSCS and other regulatory provisions	**1.4**	1.5
Subordinated liabilities	**10.9**	21.6
Perpetual subordinated bonds	**15.3**	15.3
	8,010.3	6,162.5
Equity		
Share capital	**2.4**	2.4
Share premium	**158.4**	157.9
Retained earnings	**337.5**	240.7
Other reserves	**80.5**	17.4
	578.8	418.4
Total equity and liabilities	**8,589.1**	6,580.9

Statement of Changes in Equity

For the year ended 31 December 2017

Group	Share capital	Share premium	Capital contribution	Transfer reserve	Foreign exchange reserve	Available -for-sale reserve	Share-based payment reserve	Retained earnings	Equity bonds[1]	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Balance at 1 January 2017	**2.4**	**157.9**	**6.2**	**(12.8)**	**0.1**	**-**	**1.9**	**240.7**	**22.0**	**418.4**
Profit for the year	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**126.9**	**-**	**126.9**
Coupon paid on equity bonds[2]	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(2.7)**	**-**	**(2.7)**
Dividends paid	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(27.0)**	**-**	**(27.0)**
Other comprehensive income	**-**	**-**	**-**	**-**	**(0.3)**	**0.1**	**-**	**-**	**-**	**(0.2)**
Share-based payments	**-**	**0.5**	**0.2**	**-**	**-**	**-**	**3.1**	**0.2**	**-**	**4.0**
Additional Tier 1 securities issuance[3]	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(0.6)**	**60.0**	**59.4**
Balance at 31 December 2017	**2.4**	**158.4**	**6.4**	**(12.8)**	**(0.2)**	**0.1**	**5.0**	**337.5**	**82.0**	**578.8**

Group	Share capital	Share premium	Capital contribution	Transfer reserve	Foreign exchange reserve	Available -for-sale reserve	Share-based payment reserve	Retained earnings	Equity bonds[1]	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Balance at 1 January 2016	2.4	157.9	5.8	(12.8)	(0.8)	(0.1)	0.9	144.0	22.0	319.3
Profit for the year	-	-	-	-	-	-	-	120.9	-	120.9
Coupon paid on equity bonds[2]	-	-	-	-	-	-	-	(0.9)	-	(0.9)
Dividends paid	-	-	-	-	-	-	-	(23.3)	-	(23.3)
Other comprehensive income	-	-	-	-	0.9	0.1	-	-	-	1.0
Share based payments	-	-	`0.4	-	-	-	1.0	-	-	1.4
Balance at 31 December 2016	2.4	157.9	6.2	(12.8)	0.1	-	1.9	240.7	22.0	418.4

1. Equity bonds comprise £22.0m of Perpetual Subordinated Bonds and £60.0m of Additional Tier 1 securities ('AT1 securities').
2. Coupon paid on equity bonds is shown net of tax.
3. Additional Tier 1 securities issuance costs of £0.6m are shown net of tax.

Statement of Cash Flows

For the year ended 31 December 2017

	Group Year ended 31-Dec-17 £m	Restated[1] Group Year ended 31-Dec-16 £m
Cash flows from operating activities		
Profit before tax	**167.7**	163.1
Adjustments for non-cash items:		
Depreciation and amortisation	**3.5**	2.6
Interest on subordinated liabilities	**0.9**	1.2
Interest on perpetual subordinated bonds	**0.9**	0.9
Impairment charge on loans	**4.4**	9.0
Gain on sale of financial instruments	**-**	(0.6)
FSCS and other provisions	**0.9**	0.5
Fair value losses on financial instruments	**6.3**	4.9
Share-based payments	**2.4**	1.5
Exceptional items	**-**	(24.9)
Changes in operating assets and liabilities:		
Increase in loans and advances to credit institutions[1]	**(6.3)**	(5.9)
Increase in loans to customers	**(1,371.2)**	(1,031.3)
Increase in retail deposits	**697.9**	588.6
Increase in intercompany balances	**-**	-
Net decrease/(increase) in other assets	**7.0**	-
Net (increase)/decrease in derivatives and hedged items	**(0.1)**	0.9
Increase/(decrease) in credit institutions and other customers deposits	**21.3**	(2.7)
Net (decrease)/increase in other liabilities	**(3.3)**	(1.4)
Exchange differences on working capital	**(0.3)**	0.9
Cash used in operating activities	**(468.0)**	(292.7)
Interest paid on bonds and subordinated debt	**(1.8)**	(2.1)
Sales of financial instruments	**-**	1.9
FSCS and other provisions paid	**(1.0)**	(1.3)
Net tax paid	**(42.1)**	(29.6)
Net cash used in operating activities	**(512.9)**	(323.8)
Cash flows from investing activities		
Maturity and sales of investment securities	**40.0**	712.2
Purchases of investment securities[1]	**-**	(402.8)
Proceeds from disposal of a subsidiary[2]	**-**	80.2
Purchases of equipment and intangible assets	**(14.0)**	(7.7)
Cash generated from investing activities	**26.0**	381.9

Cash flows from financing activities		
Bank of England TFS drawdowns	**1,149.0**	101.0
Coupon paid on equity bonds	**(3.7)**	(1.2)
Dividends paid	**(27.0)**	(23.3)
AT1 securities issuance net of costs	**59.4**	-
Proceeds from issuance of shares under employee SAYE schemes	**0.5**	-
Repayment of debt[3]	**(10.7)**	(19.8)
Net cash generated from in financing activities	**1,167.5**	56.7
Net increase in cash and cash equivalents	**680.6**	114.8
Cash and cash equivalents at the beginning of the year[1]	**485.3**	370.5
Cash and cash equivalents at the end of the year[1]	**1,165.9**	485.3
Movement in cash and cash equivalents	**680.6**	114.8

1. The 2016 comparatives have been restated to include investment securities with maturity less than three months and to exclude encumbered loans and advances to credit institutions (being the cash ratio deposit and swap margin paid) within cash and cash equivalents. This has no effect on the balance sheet.
2. Proceeds from a disposal of a subsidiary relate to the Group's disposal of the entire economic interest in Rochester Financing No.1 plc during 2016.
3. Repayment of debt comprises the 2017 LIBOR linked floating rate subordinated liabilities of £5.7m and the 2017 average standard mortgage rate linked floating subordinated liabilities of £5.0m.

Extract from notes to the financial statements

1. Interest receivable and similar income

	Group 31-Dec-17 £m	Group 31-Dec-16 £m
At amortised cost:		
On BTL/SME mortgages	**247.3**	208.8
On Residential mortgages	**91.8**	107.1
On investment securities	**0.1**	1.2
On other liquid assets	**2.0**	1.6
At fair value through profit or loss		
Net expense on derivative financial instruments	**(8.5)**	(9.2)
	332.7	309.5

Included within interest receivable is £1.3m (2016: £1.3m) in respect of interest accrued on accounts with an individually assessed specific provision.

2. Interest payable and similar charges

	Group 31-Dec-17 £m	Group 31-Dec-16 £m
On retail deposits	**86.1**	101.8
On Perpetual Subordinated Bonds	**0.9**	0.9
On subordinated liabilities	**0.9**	1.2
On wholesale borrowings	**3.1**	3.2
Net income on derivative financial instruments	**(3.7)**	(4.2)
	87.3	102.9

3. Risk management

Segment and sub-segment credit risk analysis

Loan to value analysis by band for all loans:

	As at 31-Dec-17			
Band	**BTL/SME £m**	**Residential £m**	**Total £m**	**%**
0 - 50%	**747.6**	**808.3**	**1,555.9**	**21**
50% - 60%	**960.5**	**260.6**	**1,221.1**	**16**
60% - 70%	**1,606.8**	**228.3**	**1,835.1**	**25**
70% - 80%	**1,939.4**	**184.5**	**2,123.9**	**29**
80% - 90%	**359.1**	**138.2**	**497.3**	**7**
90% - 100%	**15.1**	**31.6**	**46.7**	**1**
>100%	**24.5**	**22.0**	**46.5**	**1**
Total mortgages before provisions	**5,653.0**	**1,673.5**	**7,326.5**	**100**
Personal loans	**1.1**	**-**	**1.1**	
Total loans before provisions	**5,654.1**	**1,673.5**	**7,327.6**	

	As at 31-Dec-16			
Band	**BTL/SME £m**	**Residential £m**	**Total £m**	**%**
0 - 50%	755.9	761.7	1,517.6	25
50% - 60%	859.6	278.7	1,138.3	19
60% - 70%	1,202.4	282.7	1,485.1	25
70% - 80%	1,041.2	257.1	1,298.3	22
80% - 90%	194.8	196.9	391.7	7
90% - 100%	5.0	48.0	53.0	1
>100%	36.0	34.8	70.8	1
Total mortgages before provisions	4,094.9	1,859.9	5,954.8	100
Personal loans	9.4	-	9.4	
Total loans before provisions	4,104.3	1,859.9	5,964.2	

Loan to value analysis by band for BTL/SME:

	As at 31-Dec-17				
	Buy-to-Let	**Commercial**	**Residential development**	**Funding lines**	**Total**
Band	**£m**	**£m**	**£m**	**£m**	**£m**
0 - 50%	**567.0**	**66.8**	**88.3**	**25.5**	**747.6**
50% - 60%	**841.2**	**62.3**	**42.8**	**14.2**	**960.5**
60% - 70%	**1,437.7**	**120.6**	**8.9**	**39.6**	**1,606.8**
70% - 80%	**1,811.5**	**112.8**	**3.9**	**11.2**	**1,939.4**
80% - 90%	**343.1**	**2.5**	**-**	**13.5**	**359.1**
90% - 100%	**14.2**	**0.4**	**-**	**0.5**	**15.1**
>100%	**19.1**	**5.4**	**-**	**-**	**24.5**
Total mortgages before provisions	**5,033.8**	**370.8**	**143.9**	**104.5**	**5,653.0**
Personal loans					**1.1**
Total loans before provisions					**5,654.1**

	As at 31-Dec-16				
	Buy-to-Let	**Commercial**	**Residential development**	**Funding lines**	**Total**
Band	**£m**	**£m**	**£m**	**£m**	**£m**
0 - 50%	534.1	85.2	104.7	31.9	755.9
50% - 60%	750.4	67.1	23.5	18.6	859.6
60% - 70%	1,096.8	71.0	13.4	21.2	1,202.4
70% - 80%	1,006.2	35.0	-	-	1,041.2
80% - 90%	193.0	1.8	-	-	194.8
90% - 100%	5.0	-	-	-	5.0
>100%	27.8	8.2	-	-	36.0
Total mortgages before provisions	3,613.3	268.3	141.6	71.7	4,094.9
Personal loans					9.4
Total loans before provisions					4,104.3

Loan to value analysis by band for Residential mortgages:

	As at 31-Dec-17			
Band	**First charge £m**	**Second charge £m**	**Funding lines £m**	**Total £m**
0 - 50%	**647.1**	**150.2**	**11.0**	**808.3**
50% - 60%	**163.3**	**94.2**	**3.1**	**260.6**
60% - 70%	**147.9**	**78.4**	**2.0**	**228.3**
70% - 80%	**136.1**	**47.2**	**1.2**	**184.5**
80% - 90%	**116.4**	**21.6**	**0.2**	**138.2**
90% - 100%	**22.2**	**9.3**	**0.1**	**31.6**
>100%	**7.6**	**14.4**	**-**	**22.0**
Total mortgages before provisions	**1,240.6**	**415.3**	**17.6**	**1,673.5**

	As at 31-Dec-16			
Band	**First charge £m**	**Second charge £m**	**Funding Lines £m**	**Total £m**
0 - 50%	579.6	154.5	27.6	761.7
50% - 60%	166.4	103.1	9.2	278.7
60% - 70%	173.3	102.3	7.1	282.7
70% - 80%	188.3	64.0	4.8	257.1
80% - 90%	168.3	27.2	1.4	196.9
90% - 100%	31.9	16.0	0.1	48.0
>100%	14.3	20.1	0.4	34.8
Total mortgages before provisions	1,322.1	487.2	50.6	1,859.9

Analysis of mortgage portfolio by arrears and collateral held

The tables below provide further information on collateral in the mortgage portfolio by payment due status. Capped collateral only recognises collateral to the value of each individual mortgage and does not recognise over-collateralisation. The collateral position by LTV bands is captured in the LTV analysis above.

In 2016 there was an update to the categorisation where collectively assessed provisions on loans greater than 3 months in arrears are now treated as specific provisions, in addition to those that are individually assessed.

Below is a summary of capped collateral:

	As at 31-Dec-17		As at 31-Dec-16	
	Loan balance £m	**Capped collateral £m**	**Loan balance £m**	**Capped collateral £m**
Not past due and not impaired	**6,792.9**	**6,784.8**	5,478.4	5,464.5
Past due but not impaired	**452.2**	**452.1**	395.9	395.8
Impaired	**81.4**	**76.6**	80.5	69.1
Total mortgages before provisions	**7,326.5**	**7,313.5**	5,954.8	5,929.4
Personal loans	**1.1**		9.4	
Total loans before provisions	**7,327.6**		5,964.2	

A breakdown of the table above by payment due status is as follows:

	As at 31-Dec-17		As at 31-Dec-16	
	Loan balance £m	**Capped collateral £m**	**Loan balance £m**	**Capped collateral £m**
Not impaired:				
Not past due	**6,792.9**	**6,784.8**	5,478.4	5,464.5
Past due < 1 month	**307.1**	**307.1**	183.5	183.5
Past due 1 to 3 months	**102.0**	**101.9**	168.2	168.2
Past due 3 to 6 months	**20.9**	**20.9**	24.4	24.3
Past due 6 to 12 months	**14.1**	**14.1**	12.8	12.8
Past due over 12 months	**7.6**	**7.6**	6.2	6.2
Possessions[1]	**0.5**	**0.5**	0.8	0.8
	7,245.1	**7,236.9**	5,874.3	5,860.3
Impaired[2]:				
Not past due	**12.3**	**7.7**	3.2	0.4
Past due < 1 month	**0.8**	**0.8**	1.0	1.0
Past due 1 to 3 months	**2.2**	**2.1**	1.2	1.2
Past due 3 to 6 months	**23.7**	**23.7**	14.8	14.8
Past due 6 to 12 months	**16.3**	**16.3**	16.3	16.2
Past due over 12 months	**14.5**	**14.4**	31.8	24.9
Possessions	**11.6**	**11.6**	12.2	10.6
	81.4	**76.6**	80.5	69.1
Total mortgages before provisions	**7,326.5**	**7,313.5**	5,954.8	5,929.4
Personal loans	**1.1**		9.4	
Total loans before provisions	**7,327.6**		5,964.2	

Contractual maturity:
Group

Past due but not impaired:	**As at 31-Dec-17 Loan balance £m**	**As at 31-Dec-16 Loan balance £m**
Less than three months	**9.3**	5.0
Three months to one year	**7.2**	4.3
One to five years	**27.7**	22.4
More than five years	**408.0**	364.2
	452.2	395.9
Impaired:		
Less than three months	**11.2**	17.0
Three months to one year	**0.9**	1.2
One to five years	**5.9**	2.5
More than five years	**63.4**	59.8
	81.4	80.5

1. Mortgages with properties in possession are not considered impaired if the fair value of collateral exceeds the value of debt.
2. Impaired is defined as loans with a specific provision against them.

Analysis of mortgage portfolio by arrears for BTL/SME

	As at 31-Dec-17				
	Buy-to-Let	Commercial	Residential development	Funding lines	Total
	£m	£m	£m	£m	£m
Not impaired:					
Not past due	**4,810.7**	**360.8**	**143.9**	**104.5**	**5,419.9**
Past due < 1 month	**160.4**	**2.8**	**-**	**-**	**163.2**
Past due 1 to 3 months	**31.9**	**0.6**	**-**	**-**	**32.5**
Past due 3 to 6 months	**2.7**	**-**	**-**	**-**	**2.7**
Past due 6 to 12 months	**0.7**	**-**	**-**	**-**	**0.7**
Past due over 12 months	**0.3**	**0.8**	**-**	**-**	**1.1**
Possessions	**-**	**-**	**-**	**-**	**-**
	5,006.7	**365.0**	**143.9**	**104.5**	**5,620.1**
Impaired:					
Not past due	**4.6**	**4.5**	**-**	**-**	**9.1**
Past due < 1 month	**-**	**0.1**	**-**	**-**	**0.1**
Past due 1 to 3 months	**-**	**-**	**-**	**-**	**-**
Past due 3 to 6 months	**9.1**	**-**	**-**	**-**	**9.1**
Past due 6 to 12 months	**4.0**	**0.4**	**-**	**-**	**4.4**
Past due over 12 months	**1.6**	**0.1**	**-**	**-**	**1.7**
Possessions	**7.8**	**0.7**	**-**	**-**	**8.5**
	27.1	**5.8**	**-**	**-**	**32.9**
Total mortgages before provisions	**5,033.8**	**370.8**	**143.9**	**104.5**	**5,653.0**
Personal loans					**1.1**
Total loans before provisions					**5,654.1**

Contractual maturity:
Past due but not impaired:

Less than three months	**5.8**	**-**	**-**	**-**	**5.8**
Three months to one year	**5.6**	**-**	**-**	**-**	**5.6**
One to five years	**5.1**	**0.8**	**-**	**-**	**5.9**
More than five years	**179.5**	**3.4**	**-**	**-**	**182.9**
	196.0	**4.2**	**-**	**-**	**200.2**

Impaired:

Less than three months	**6.9**	**-**	**-**	**-**	**6.9**
Three months to one year	**0.6**	**-**	**-**	**-**	**0.6**
One to five years	**1.1**	**0.1**	**-**	**-**	**1.2**
More than five years	**18.5**	**5.7**	**-**	**-**	**24.2**
	27.1	**5.8**	**-**	**-**	**32.9**

As at 31-Dec-16

	Buy-to-Let	Commercial	Residential development	Funding lines	Total
	£m	£m	£m	£m	£m
Not impaired:					
Not past due	3,468.7	252.9	141.6	71.7	3,934.9
Past due < 1 month	62.5	3.3	-	-	65.8
Past due 1 to 3 months	56.5	1.1	-	-	57.6
Past due 3 to 6 months	2.0	0.3	-	-	2.3
Past due 6 to 12 months	0.4	0.7	-	-	1.1
Past due over 12 months	-	0.3	-	-	0.3
Possessions	-	-	-	-	-
	3,590.1	258.6	141.6	71.7	4,062.0
Impaired:					
Not past due	2.5	0.1	-	-	2.6
Past due < 1 month	-	0.4	-	-	0.4
Past due 1 to 3 months	-	0.3	-	-	0.3
Past due 3 to 6 months	1.1	0.2	-	-	1.3
Past due 6 to 12 months	2.3	0.1	-	-	2.4
Past due over 12 months	9.0	6.0	-	-	15.0
Possessions	8.3	2.6	-	-	10.9
	23.2	9.7	-	-	32.9
Total mortgages before provisions	3,613.3	268.3	141.6	71.7	4,094.9
Personal loans					9.4
Total loans before provisions					4,104.3

Contractual maturity

Past due but not impaired:					
Less than three months	0.1	-	-	-	0.1
Three months to one year	0.4	-	-	-	0.4
One to five years	4.1	-	-	-	4.1
More than five years	116.8	5.7	-	-	122.5
	121.4	5.7	-	-	127.1
Impaired:					
Less than three months	15.4	-	-	-	15.4
Three months to one year	-	-	-	-	-
One to five years	-	-	-	-	-
More than five years	7.8	9.7	-	-	17.5
	23.2	9.7	-	-	32.9

Analysis of mortgage portfolio by arrears for Residential mortgages

	As at 31-Dec-17			
	First charge £m	Second charge £m	Funding lines £m	Total £m
Not impaired:				
Not past due	**1,023.6**	**331.8**	**17.6**	**1,373.0**
Past due < 1 month	**123.1**	**20.8**	**-**	**143.9**
Past due 1 to 3 months	**46.4**	**23.1**	**-**	**69.5**
Past due 3 to 6 months	**10.5**	**7.7**	**-**	**18.2**
Past due 6 to 12 months	**8.1**	**5.3**	**-**	**13.4**
Past due over 12 months	**3.2**	**3.3**	**-**	**6.5**
Possessions	**0.5**	**-**	**-**	**0.5**
	1,215.4	**392.0**	**17.6**	**1,625.0**
Impaired:				
Not past due	**2.9**	**0.3**	**-**	**3.2**
Past due < 1 month	**0.7**	**-**	**-**	**0.7**
Past due 1 to 3 months	**2.2**	**-**	**-**	**2.2**
Past due 3 to 6 months	**7.5**	**7.1**	**-**	**14.6**
Past due 6 to 12 months	**6.6**	**5.3**	**-**	**11.9**
Past due over 12 months	**2.2**	**10.6**	**-**	**12.8**
Possessions	**3.1**	**-**	**-**	**3.1**
	25.2	**23.3**	**-**	**48.5**
Total mortgages before provisions	**1,240.6**	**415.3**	**17.6**	**1,673.5**

Contractual maturity
Past due but not impaired:

Less than three months	**3.3**	**0.2**	**-**	**3.5**
Three months to one year	**1.0**	**0.6**	**-**	**1.6**
One to five years	**11.5**	**10.3**	**-**	**21.8**
More than five years	**176.0**	**49.1**	**-**	**225.1**
	191.8	**60.2**	**-**	**252.0**
Impaired:				
Less than three months	**4.2**	**0.1**	**-**	**4.3**
Three months to one year	**-**	**0.3**	**-**	**0.3**
One to five years	**0.8**	**3.9**	**-**	**4.7**
More than five years	**20.2**	**19.0**	**-**	**39.2**
	25.2	**23.3**	**-**	**48.5**

As at 31-Dec-16

	First charge £m	Second charge £m	Funding line £m	Total £m
Not impaired:				
Not past due	1,100.6	392.3	50.6	1,543.5
Past due < 1 month	99.8	17.9	-	117.7
Past due 1 to 3 months	80.2	30.4	-	110.6
Past due 3 to 6 months	12.8	9.3	-	22.1
Past due 6 to 12 months	5.0	6.7	-	11.7
Past due over 12 months	2.8	3.1	-	5.9
Possessions	0.8	-	-	0.8
	1,302.0	459.7	50.6	1,812.3
Impaired:				
Not past due	0.6	-	-	0.6
Past due < 1 month	0.6	-	-	0.6
Past due 1 to 3 months	0.9	-	-	0.9
Past due 3 to 6 months	6.0	7.5	-	13.5
Past due 6 to 12 months	5.8	8.1	-	13.9
Past due over 12 months	4.9	11.9	-	16.8
Possessions	1.3	-	-	1.3
	20.1	27.5	-	47.6
Total mortgages before provisions	1,322.1	487.2	50.6	1,859.9

Contractual maturity:
Past due but not impaired:

Less than three months	4.3	0.6	-	4.9
Three months to one year	2.8	1.1	-	3.9
One to five years	9.1	9.2	-	18.3
More than five years	185.2	56.5	-	241.7
	201.4	67.4	-	268.8
Impaired:				
Less than three months	1.3	0.3	-	1.6
Three months to one year	0.2	1.0	-	1.2
One to five years	-	2.5	-	2.5
More than five years	18.6	23.7	-	42.3
	20.1	27.5	-	47.6

Geographical analysis by region

An analysis of loans by region is provided below:

Region	As at 31-Dec-2017		As at 31-Dec-2016	
	£m	%	£m	%
East Anglia	**236.4**	**3**	182.2	3
East Midlands	**249.6**	**4**	204.5	3
Greater London	**3,173.0**	**43**	2,543.1	43
Guernsey	**73.8**	**1**	93.4	2
Jersey	**225.1**	**3**	282.0	5
North East	**103.0**	**1**	90.3	2
North West	**347.9**	**5**	273.2	5
Northern Ireland	**16.9**	**-**	16.8	-
Scotland	**51.1**	**1**	56.1	1
South East	**1,591.7**	**22**	1,278.5	21
South West	**522.3**	**7**	380.6	6
Wales	**142.9**	**2**	114.7	2
West Midlands	**425.4**	**6**	308.6	5
Yorks & Humberside	**167.4**	**2**	130.8	2
Total mortgages before provisions	**7,326.5**	**100**	5,954.8	100
Personal loans	**1.1**		9.4	
Total loans before provisions	**7,327.6**		5,964.2	

General note to the financial information

The financial information set out in the announcement does not constitute the Company's statutory accounts for the years ended 31 December 2017 or 31 December 2016, but is derived from those statutory accounts, which have been reported on by the Company's auditors. Statutory accounts for the years ended 31 December 2016 have been delivered to the Registrar of Companies and those for the year ended 31 December 2017 will be delivered to the Registrar following the Company's Annual General Meeting.

Sections of this preliminary announcement, including but not limited to the Chief Executive's Report and Operating and Financial Review, may contain forward-looking statements with respect to certain of the plans and current goals and expectations relating to the future financial condition, business performance and results of the Group. These have been made by the Directors in good faith using information available up to the date on which they approved this report. By their nature, all forward-looking statements involve risk and uncertainty because they relate to future events and circumstances that are beyond the control of the Group and depend upon circumstances that may or may not occur in the future. There are a number of factors that could cause actual future financial conditions, business performance, results or developments to differ materially from the plans, goals and expectations expressed or implied by these forward-looking statements and forecasts. Nothing in this document should be construed as a forecast.

A copy of the Annual Report and Accounts for the year ended 31 December 2017 will be posted to shareholders in due course. Copies of this announcement can be obtained from the Group Company Secretary, OneSavings Bank plc, Reliance House, Sun Pier, Chatham, Kent ME4 4ET.

Risk overview

Strategic Risk Management Framework

Ongoing risk identification, assessment, monitoring and reporting are the primary risk disciplines underpinning the Group's growth strategy and adherence to the prudential and conduct regulatory requirements. The Group's approach to risk management is outlined within the Strategic Risk Management Framework ('SRMF').

The SRMF is the overarching framework which enables the Board and senior management to actively manage and optimise the risk-reward profile within the constraints of the Group risk appetite. Specifically, the SRMF enables the Board and senior management to take informed decisions by appropriately balancing the interests and expectations of the various stakeholders and to manage potential trade-offs within the context of the risk appetite.

Risk principles and culture

The Board adopted a principle-based approach to articulating its expectations and guidance relating to how the Group should frame its risk management approach. The risk management principles are designed to set a clear 'tone from the top' with respect to the Group's risk culture and values. The risk principles also provide the background context in which to articulate the Group's risk management objectives, strategy and appetite. The risk principles are:

- **Customer outcomes:** fair treatment and good customer outcomes are core business values which cannot be put at risk
- **Proportionate and scalable:** the approach to risk management needs to be commensurate with the complexity of the underlying risk profile and appropriately agile to respond to changing business and regulatory needs
- **Actively managed:** the risk profile needs to be actively managed within the Board approved risk appetite
- **Comprehensive coverage:** all risks and their underlying drivers impacting the Group's strategic, business, operational and regulatory objectives should be actively assessed, monitored and reported
- **Segregation of duties:** risk taking, oversight and assurance responsibility to be organised in adherence to the 'three lines of defence' principle
- **Integration and usage:** risk assessment should be a critical feature of decision making processes at all levels of the organisation
- **Versatile and progressive:** the approach to managing risks should be subject to continuous review and challenge to keep pace with emerging good practice and regulatory standards.

In adherence to the risk management principles, the Group Board and senior management have cultivated a risk culture which encourages a proactive, transparent and analytical approach to risk management. Risks are assumed in a balanced and considered manner, taking into account stakeholder expectations, good customer outcomes, risk management capabilities and controls.

Risk strategy & appetite

Risk strategy

OSB's risk strategy is to create value through informed risk-based decisions and leveraging the Group's risk data and analytics in a timely and accurate manner to optimise the risk-reward profile. Risks are only to be assumed which can be effectively identified, assessed, measured and controlled across all phases of the risk life cycle.

This risk strategy is based on three key components:

• Creating value through generating returns which sufficiently exceed the cost of risk, funding costs and operating costs

• Risks are only to be assumed where they are subject to a structured and disciplined approach to risk management

• Risk management capabilities are scalable and agile enough to adequately address future evolution of the risk profile.

Risk appetite

The Group effectively aligned its strategic and business objectives with its risk appetite, ensuring that the Board and senior management are able to monitor the underlying risk profile relative to the overarching risk principles, risk strategy and financial performance objectives of the Group. The risk appetite is a critical mechanism though which the Board and senior management are able to identify adverse trends and respond to unexpected developments in a timely and considered manner.

The risk appetite is calibrated to reflect the Group's strategic objectives, business operating plans, as well as external economic, business and regulatory constraints. In particular, the risk appetite is calibrated to ensure that the Bank continues to deliver against its strategic objectives and operates with sufficient financial buffers even when subjected to plausible but extreme stress scenarios. The objective of the Board risk appetite is to ensure that the strategy and business operating model is sufficiently resilient.

The risk appetite is calibrated using statistical analysis and stress testing to inform the process by which the Board set management triggers and limits against key risk indicators. The Board and senior management actively monitor actual performance against Board approved management triggers and limits to respond in a timely manner to adverse trends and breaches.

Risk appetite statements

Overarching risk appetite statement

The Bank has a prudent and proportionate approach to risk taking and management, which is reflective of its straightforward business model. The inherent resilience of the Group's business model is underpinned by the fact that the Bank only lends on a secured basis, has established robust underwriting practices and relies on intermediary based distribution. The Group supports its lending activities by being predominantly reliant on stable retail funding, supported by strong and high quality financial buffers. The highly efficient business operating model is an important source of competitive advantage. The Group also places significant importance on its strong conduct and compliance culture as an important driver of its overall success.

Strategic and business risk appetite statement

The Group's strategic and business risk appetite states that the Group does not intend to undertake any long to medium-term strategic actions that would put at risk its vision of being a leading specialist lender, backed by a strong and dependable saving franchise. The Group adopts a long-term sustainable business model which, while focused on niche sub-sectors, is capable of adapting to growth objectives and external developments.

Reputational risk appetite statement

The Group does not knowingly conduct business or organise its operations to put its reputation and franchise value at risk.

Credit risk appetite statement

The Group seeks to maintain a high quality lending portfolio that generates adequate returns, under normal and stressed periods. The portfolio is actively managed to operate within set criteria and limits based on profit volatility, focusing on key sectors, recoverable values, and affordability and exposure levels. The Group aims to continue to generate sufficient income and control credit losses to a level such that it remains profitable even when subjected to a credit portfolio stress of a 1 in 20 intensity stress scenario.

Market risk appetite statement

The Group actively manages market risk arising from structural interest rate positions. The Group does not seek to take a significant interest rate position or a directional view on rates and it limits its mismatched and basis risk exposures.

Liquidity and funding risk appetite statement

The Group actively maintains stable and efficient access to funding and liquidity to support its ongoing operations. It also maintains an appropriate level and quality of liquid asset buffer so as to withstand market and idiosyncratic liquidity related stresses.

Solvency risk appetite statement

OSB seeks to ensure that it is able to meet its Board Level Capital buffer requirements under a 1 in 20 stress scenario. The Group's solvency risk appetite is constrained within the leverage ratio related requirements. We manage our capital resources in a manner which avoids excessive leverage and allows us flexibility in raising capital.

Operational risk appetite statement

The Group's operational processes, systems and controls are designed to minimise disruption to customers, damage to the Bank's reputation and any detrimental impact on financial performance. The Bank actively promotes the continual evolution of its operating environment through the identification, evaluation and mitigation of risks, whilst recognising that the complete elimination of operational risk is not possible.

Conduct risk appetite statement

The Bank considers its culture and behaviours in ensuring the fair treatment of customers and in maintaining the integrity of the markets in which it operates a fundamental part of its strategy and a key driver to sustainable profitability and growth. OSB does not tolerate any systemic failure to deliver fair customer outcomes. On an isolated basis incidents can result in detriment owing to human and / or operational failures. Where such incidents occur they are thoroughly investigated, and the appropriate remedial actions are taken to address any customer detriment and to prevent recurrence.

Compliance and regulatory risk appetite statement

The Group views ongoing conformance with regulatory rules and standards across all the jurisdictions in which it operates as a critical facet of its risk culture. The Group does not knowingly accept compliance risk which could result in regulatory sanctions, financial loss or damage to its reputation. The Group will not tolerate any systemic failure to comply with applicable laws, regulations or codes of conduct relevant given its business operating model.

Risk Governance and organisational structure

Risk governance refers to the processes and structures established by the Board to ensure that risks are assumed and managed within the Board approved risk appetite, with clear delineation between risk taking, oversight and assurance responsibilities. The Group's risk governance framework is structured to adhere to the 'three lines of defence' model. All risk taking, oversight and assurance functions are allocated to accountable Executives.

The Group Board has the ultimate responsibility for the oversight of the Group's risk profile and management framework and where it deems it appropriate, it delegates its authority to its nominated committees. The Board and its committees are provided with appropriate and timely information relating to the nature and level of the risks to which the Group is exposed and the adequacy of the risk controls and mitigants. The Internal Audit function provides independent assurance to the Board and its committees as to the effectiveness of the systems and controls and the level of adherence with internal policies and regulatory requirements.

2017 highlights

IFRS 9

The Board has identified transition towards IRB based capital treatment as an important strategic objective and the Group has made significant progress in the development of its IFRS 9 and Internal Ratings Based ('IRB') frameworks. The Group's IFRS 9 programme progressed to plan, moving into the parallel run phase for 2017. We are well placed to implement IFRS 9 in 2018.

Credit risk

The Group's credit profile performed strongly in 2017, driven by deep market knowledge of the specialist markets in which it operates, prudent lending policies and sound credit risk management.

During the year, the Group's portfolio composition mix continued to evolve with pre-2011 lending (prior to OneSavings Bank PLC being established) continuing to run off. Legacy problem loans reduced further in 2017 from £13.8m to £8.6m, following careful management by our experienced collections team. The Group's acquired portfolios also continued to perform in line with expectations in terms of run-off rates and credit profile performance.

The Group's funding lines and development finance businesses delivered a strong performance in 2017, with no impairment recognised across either segment.

Strong Group originations performance was observed in 2017, driven by performance across the Buy-to-Let/SME segment. Importantly, this lending was underwritten at sensible LTV levels, where underwriting policy, tightened post the United Kingdom's decision to leave the European Union, resulted in a greater clustering of LTV levels against the portfolio average. Post-2011 lending, incorporating enhanced lending criteria, continued to make up an increasing proportion of the Group's total loans and advances to customers, where 38,500 loans have been underwritten with only 137 loans being greater than three months arrears with aggregate loans totalling £18.4m with aggregate weighted average LTV of 63%.

This portfolio mix shift coupled with strong credit risk management and continuing favourable economic conditions supported the portfolio arrears rate reducing to 1.2% as at 31 December 2017 excluding legacy problem loans (31 December 2016: 1.4%).

Credit profile performance

Segment	Measure	31-Dec-2017	31-Dec-2016	Variance	Commentary
BTL/SME	New origination average LTV	70%	70%	0%	New lending average LTV remained stable
	Weighted average ICR for new lending	185%	171%	+14%	Resulting from a tightening of affordability rules
Residential	New origination average LTV	65%	66%	-1%	New lending average LTV reduced
	Percentage of new residential lending with a loan to income (LTI) greater than 4.5	3.2%	2.6%	+0.6%	Increase in cases with LTI>4.5

Other key risk measures also performed strongly within the period:

• gross exposure to semi-commercial/commercial lending remains low at £370.8m with weighted average LTV of 63%

• gross exposure to residential development finance remains low at £143.8m with a further £78.0m committed with a weighted average LTV of 37.7%

• the Group has limited exposure to high LTV loans on properties worth more than £2m. In total only 4% of the Group's loan portfolio is secured on properties valued at greater than £2m with a LTV greater than 65%.

Forbearance

Where borrowers experience financial difficulties which impacts their ability to service their financial commitments under the loan agreement, forbearance may be used to achieve an outcome which is mutually beneficial to both the borrower and the Bank.

By identifying borrowers who are experiencing financial difficulties pre-arrears or in arrears a consultative process is initiated to ascertain the underlying reasons and to establish the best course of action to enable the borrower to develop credible repayment plans and to see them through the period of financial stress.

Forbearance type	2017 number of accounts	2017 year-end balance £m	2016 number of accounts	restated[1] 2016 year- end balance £m	’17 vs ’16 variance number of accounts	’17 vs ’16 variance of balance £m
Interest only switch	**35**	**3.8**	60	6.3	-25	-2.5
Interest rate reduction	**-**	**-**	3	2.2	-3	-2.2
Term extension	**29**	**4.9**	31	5.9	-2	-1.0
Payment holiday	**50**	**1.5**	37	1.6	13	-0.1
Voluntary assisted sale	**2**	**0.7**	-	-	2	0.7
Payment concession (reduced monthly payments)	**42**	**0.8**	58	3.5	-16	-2.7
Capitalisation	**-**	**-**	3	0.1	-3	-0.1
Total	**158**	**11.7**	192	19.6	-34	-7.9

Loan type	2017 number of accounts	2017 year-end balance £m	2016 number of accounts	restated[1] 2016 year- end balance £m	’17 vs ’16 variance number of accounts	’17 vs ’16 variance of balance £m
First charge owner occupier	**55**	**4.5**	117	12.4	-62	-7.9
Second charge owner occupier	**77**	**1.6**	60	1.3	17	0.3
Buy-to-Let	**26**	**5.6**	14	5.5	12	0.1
Commercial	**-**	**-**	1	0.4	-1	-0.4
Total	**158**	**11.7**	192	19.6	-34	-7.9

1. The 2016 year end forbearance balances have been restated for second charge owner occupier to remove the related first charge balance, to align to the enhanced approach adopted for 2017.

Solvency risk

The Bank has maintained an appropriate level and quality of capital to support its prudential requirements with sufficient contingency to withstand a severe but plausible stress scenario. The solvency risk appetite is based on a stacking approach, whereby the various capital requirements (Pillar 1, ICG, CRD IV buffers and Board and management buffers) are incrementally aggregated as a percentage of available capital (CET1 and total capital).

Solvency risk is a function of balance sheet growth, profitability, access to capital markets and regulatory changes. The Bank actively monitors all key drivers of solvency risk and takes prompt action to maintain its solvency ratios at acceptable levels. The Board and management also assess solvency when reviewing the Bank's business plans and inorganic growth opportunities.

In 2017, the Bank strengthened its CET1 ratio by 0.4% to 13.7% and total capital ratio by 1.8% to 16.9% despite strong organic growth, demonstrating both the strength of internal capital generation capabilities through profitability and the ability to raise additional capital in the market.

Liquidity and funding risk

The Bank has a prudent approach to liquidity management through maintaining sufficient liquidity resources to cover cash flow imbalances and fluctuations in funding under both normal and stressed conditions arising from market wide and Bank specific events. The Bank's liquidity risk appetite has been calibrated to ensure that the Bank always operates above the minimum prudential requirements with sufficient contingency for unexpected stresses whilst actively minimising the risk of holding excessive liquidity which would adversely impact the financial efficiency of the business model.

The Bank has successfully utilised the Bank of England FLS and TFS secured funding facilities to manage its liquidity throughout 2017, and continues to attract new retail savers and retain existing customers through loyalty-based product offerings.

In 2017 the Bank actively managed its liquidity and funding profile within the confines of its risk appetite as set out in the ILAAP. Its liquidity ratio at 15.2% and liquidity coverage ratio ('LCR') at 250% remain well above risk appetite and regulatory minimums.

Market risk

The Bank proactively manages its risk profile in respect of adverse movements in interest rates, foreign exchange rates and counterparty exposures. The Bank accepts interest rate risk and basis risk as a consequence of structural mismatches between fixed rate mortgage lending, sight and fixed term savings and the maintenance of a portfolio of high quality liquid assets. Interest rate exposure is mitigated on a continuous basis through portfolio diversification, reserve allocation and the use of financial derivatives within limits set by ALCO and approved by the Board.

Interest rate risk

The Bank does not actively assume interest rate risk, does not execute client or speculative securities transactions for its own account, and does not seek to take a significant directional interest rate position. Limits have been set to allow management to run occasional unhedged positions in response to balance sheet dynamics and capital has been allocated for this. Exposure limits are calibrated in accordance with a statistically-derived risk appetite, and are calibrated in proportion to available CET1 capital in order to accommodate balance sheet growth.

The Group sets limits on the tenor and rate reset mismatches between fixed-rate assets and liabilities, including derivatives hedges, with exposure and risk appetite assessed with reference to historic and potential stress scenarios cast at consistent levels of modelled severity.

Throughout 2017 the Bank managed its interest rate risk exposure within its risk appetite limits. The Bank has also made significant progress in a project to replace its current interest rate risk management system with a new system allowing greater functionality which will enhance the management of interest rate risk. Implementation of the new system is scheduled to be completed during the first half of 2018.

Basis risk

Basis risk arises from assets and liabilities repricing with reference to different interest rate indices, including positions which reference variable market, policy and managed rates. As with structural interest rate risk, the Bank does not seek to take a significant basis risk position, but maintains defined limits to allow operational flexibility.

As with structural interest rate risk, capital allocation has been set in proportion to common equity tier 1 capital, with exposure assessed and monitored monthly across a range of ‘business as usual’ and stressed scenarios.

Throughout 2017 the Bank managed its basis risk exposure within its risk appetite limits.

Operational risk

OSB continues to adopt a proactive approach to the management of operational risks. The Operational Risk Management Framework has been designed to ensure a robust approach to the identification, measurement and mitigation of operational risks, utilising a combination of both qualitative and quantitative evaluations in order to promote an environment of progressive operational risk management. The Group’s operational processes, systems and controls are designed to minimise disruption to customers, damage to the Bank’s reputation and any detrimental impact on financial performance. The Bank actively promotes the continual evolution of its operating environment through the identification, evaluation and mitigation of risks, whilst recognising that the complete elimination of operational risk is not possible.

Where risks continue to exist, there are established processes to provide the appropriate levels of governance and oversight, together with an alignment to the level of risk appetite stated by the OSB Board.

A strong culture of transparency and escalation has been cultivated throughout the organisation, with the operational risk function having a Group wide remit, ensuring a risk management model that is well embedded and consistently applied. In addition, a community of Risk Champions representing each business line and location have been identified. Operational Risk Champions ensure that the operational risk identification and assessment processes are established across the Group in a consistent manner. Risk Champions are provided with appropriate support and training by the operational risk function.

Regulatory and compliance risk

The Bank is committed to the highest standards of regulatory conduct and aims to minimise breaches, financial costs and reputational damage associated with non-compliance. However, given the growing scale and complexity of regulatory changes, it is acknowledged that there may be isolated instances whereby the Bank’s interpretation and response to new regulatory requirements reflects the Bank’s specific circumstances and its desire to give the best customer outcomes.

The Bank has an established compliance function which actively identifies, assesses and monitors adherence with current regulation and the impact of emerging regulation.

Principal risks and uncertainties

Strategic and business risk

The risk to the Bank's earnings and profitability arising from its strategic decisions, change in the business conditions, improper implementation of decisions or lack of responsiveness to industry changes.

Arising from

Performance against strategic and business targets does not meet stakeholder expectations. This has the potential to damage the Group's franchise value and reputation.

Mitigation and control

Regular monitoring by the Board and the Executive Committee of monitoring of strategic and business performance against market commitments, the balanced business scorecard and risk appetite. Use of stress testing to flex core business planning assumptions to assess potential performance under stressed operating conditions.

Reputational risk

The potential risk of adverse effects that can arise from the Bank's reputation being sullied due to factors such as unethical practices, adverse regulatory actions, customer dissatisfaction and complaints or negative/adverse publicity. Reputational risk can arise from a variety of sources and is a second order risk – the crystallisation of a credit risk or operational risk can lead to a reputational risk impact.

Arising from

Potential loss of trust and confidence that our stakeholders and customers place in us as a responsible and fair provider of financial services.

Mitigation and control

Culture and commitment to treating customers fairly and being open and transparent in communication with key stakeholders. Established processes to proactively identify and manage potential sources of reputational risk.

Credit risk

The potential for loss due to the failure of a counterparty to meet its contractual obligation to repay a debt in accordance with the agreed terms.

Individual borrower defaults

Borrowers may encounter idiosyncratic problems in repaying their loans, for example loss of a job or execution problems with a development project. While most of the Bank's lending is secured, some borrowers may fail to maintain the value of the security.

Mitigation and controls

All loans are extended only after thorough bespoke and expert underwriting to ensure ability and propensity of borrowers to repay and sufficient security in case of default.

Should there be problems with a loan, the collections and recoveries team works with customers unable to meet their loan service obligations to reach a satisfactory conclusion while adhering to the principle of treating customers fairly.

Our strategic focus on lending to professional landlords means that properties are likely to be well managed, with income from a diversified portfolio mitigating the impact of rental voids or maintenance costs. Lending to owner-occupiers is subject to a detailed affordability assessment, including the borrower's ability to continue payments if interest rates increase. Lending on commercial property is more based on security, and is scrutinised by the Group's independent Real Estate team as well as by external valuers.

Development lending is extended only after a deep investigation of the borrower's track record and stress testing the economics of the specific project.

The Group's Transactional Credit Committee actively reviews and approves larger or more complex mortgage applications.

Macroeconomic downturn

A broad deterioration in the economy would adversely impact both the ability of borrowers to repay loans and the value of the Group's security. Credit losses would impact across the lending portfolio, so even if individual impacts were to be small, the aggregate impact on the Group could be significant.

Mitigation and controls

The Group works within portfolio limits on LTV, affordability, name, sector and geographic concentration that are approved by Risk Committee and the Board. These are reviewed on a semi-annually basis. In addition, stress testing is performed to ensure that the Group maintains sufficient capital to absorb losses in an economic downturn and continue to meet its regulatory requirements.

Wholesale credit risk

The Bank has wholesale exposures both through call accounts used for transactional and liquidity purposes and through derivative exposures used for hedging.

Mitigation and controls

The Group transacts only with high quality wholesale counterparties. Derivative exposures include collateral agreements to mitigate credit exposures.

Market risk

Potential loss due to changes in market prices or values.

Interest rate risk

An adverse movement in the overall level of interest rates could lead to a loss in value due to mismatches in the duration of assets and liabilities.

Mitigation and controls

The Group's Treasury department actively hedges to match the timing of cash flows from assets and liabilities.

Basis risk

A divergence in market rates could lead to a loss in value, as assets and liabilities are linked to different rates.

Mitigation and controls

The Group strategically focuses on products linked to administered rates to keep control of yield.

Liquidity and funding risk

The risk that the Group will be unable to meet its financial obligations as they fall due.

Retail funding stress

As the Group is primarily funded by retail deposits, a retail run could put it in a position where it could not meet its financial obligations.

Increased competition for retail savings driving up funding costs, adversely impacting retention levels and wider damage to OSB franchise.

Mitigation and controls

The Group's funding strategy is focused on a highly stable retail deposit franchise. The large number of depositors provides diversification and a high proportion of balances are covered by the FSCS and so there is no material risk of a retail run.

In addition, the Group performs in-depth liquidity stress testing and maintains a liquid asset portfolio sufficient to meet obligations under stress. The Group holds prudential liquidity buffers to manage funding requirements under normal and stressed conditions.

The Group proactively manages its savings proposition through both the Liquidity Working Group and the ALCO.

Finally, the Group has prepositioned mortgage collateral with the Bank of England which allows it to consider other alternative funding sources to ensure it is not solely reliant on retail savings.

The Group's funding plan ensures a diverse funding profile and initiatives have been put in place to replace TFS with a comprehensive Retail Mortgage Backed Securities ('RMBS') programme.

Term funding scheme withdrawal

The potential impact of the withdrawal of the TFS programme is uncertain.

Mitigation and controls

The Group's funding plan ensures a diverse funding profile and initiatives have been put in place to replace TFS with a comprehensive Retail Mortgage Backed Securities ('RMBS') programme.

Solvency risk

The potential inability of the Bank to ensure that it maintains sufficient capital levels for its business strategy and risk profile under both the base and stress case financial forecasts.

Arising from

Key risks to solvency arise from balance sheet growth and unexpected losses which can result in the Bank's capital requirements increasing or capital resources being depleted such that it no longer meets the solvency ratios as mandated by the PRA and Board risk appetite.

The regulatory capital regime is subject to change and could lead to increases in the level and quality of capital that the Group needs to hold to meet regulatory requirements.

Mitigation and controls

Currently the Bank operates from a strong capital position and has a consistent record of strong profitability.

The Bank actively monitors its capital requirements and resources against financial forecasts and plans and undertakes stress testing analysis to subject its solvency ratios to extreme but plausible scenarios.

The Bank also holds prudent levels of capital buffers based on CRD IV requirements and expected balance sheet growth.

The Group engages actively with regulators, industry bodies, and advisers to keep abreast of potential changes and provide feedback through the consultation process.

Operational risk

The risk of loss or negative impact to the Group resulting from inadequate or failed internal processes, people or systems, or from external events.

Cyber/data security risk

The risk of a loss of customer or proprietary data as a result of theft or through ineffective data management.

Mitigation and controls

A series of tools designed to identify and prevent network / system intrusions are deployed across the Group.

The effectiveness of the controls is overseen by a dedicated IT Security Governance Committee, with specialist IT Security staff employed by the Bank.

Data risk

The use of inaccurate, incomplete or outdated data may result in a range of risks impacting risk management and reporting services.

Mitigation and controls

The Bank continues to invest in and enhance its data management architecture, systems, governance and controls.

Regulatory risk

The operational risks arising from the management of a significant volume of regulatory change.

Mitigation and controls

The Bank operates a series of controls to identify any relevant regulatory change at an early stage.

Regulatory related changes are appropriately prioritised and resourced in order to ensure the timely implementation of any operational changes required.

Operational and IT Resilience

Banks should have business resiliency, continuity monitoring and plans in place to ensure an ability to operate on an ongoing basis and limit losses in the event of severe business disruption.

Technical failures (including bugs, network or data) resulting in critical system outage. These would include OSB's primary mortgage origination and servicing systems, saving processing system and core reporting and data management systems leading to loss of service, revenue, business performance and potential customer detriment.

Mitigation and controls

The Bank has established an Operational Resilience Programme that is delivering a Group wide approach in respect to planning and testing. In addition the Programme is designed to highlight any areas of specific vulnerability.

A range of back-up technologies employed to provide real-time replication on various critical systems while disaster recovery capabilities are tested annually.

Real-time system performance monitoring established and a dedicated testing team in place.

Operational execution and scalability

The inability of the Bank to automate current operational processes at the speed the business requires in order to successfully meet future growth.

Mitigation and controls

In order to mitigate incidents materialising from manual processes an established two tier (dependent and independent within the first line) risk based quality control program is in place.

Conduct risk

The risk that the Group's behaviours or actions result in customer detriment or negative impact on the integrity of the markets in which it operates.

Product suitability

Whilst the Group originates relatively simple products, there remains a risk that (primarily legacy) products may be deemed to be unfit for their original purpose in line with the current regulatory definitions.

Mitigation and controls

The Group has a strategic commitment to provide simple, customer-focused products. In addition, a Product Governance framework is established to oversee both the origination of new products and to revisit the ongoing suitability of the existing product suite.

A dedicated Product Governance team which is part of an independent Conduct Risk team serves to effectively manage this risk.

Data protection

The risk that customer data is accessed inappropriately, either as a consequence of network / system intrusion or through operational errors in the management of the data.

Mitigation and controls

In addition to a series of network / system controls (documented within as part of the operational risks), the Bank performs extensive root cause analysis of any data leaks in order to ensure that the appropriate mitigating actions are taken.

Compliance and regulatory risk

The risk that a change in legislation or regulation or an interpretation that differs from the Group's will adversely impact the Group.

Arising from

Key compliance regulatory changes that impacted the Bank included PRA's Buy-to-let underwriting standards, certification regime under the SM&CR, PSD2, GDPR, Criminal Finances Act, European Fourth Money Laundering Directive, FCA guidance on automatic capitalisation for residential mortgage customers.

Mitigation and controls

The Bank has an effective horizon scanning process to identify regulatory change.

All significant regulatory initiatives are managed by structured programmes overseen by the change management team and sponsored at Executive management level.

The Bank has proactively sought external expert opinions to support interpretation of the requirements and validation of its response.

Conduct regulation

Regulatory changes focused on the conduct of business could force changes in the way the Group carries out business and impose substantial compliance costs. For example, the Financial Policy Committee's increased focus on Buy-to-Let lending or tax changes such as the Bank profits surcharge must be considered.

Mitigation and controls

The Group has a programme of regulatory horizon scanning linking into a formal regulatory change management programme. In addition, the focus on simple products and customer oriented culture means that current practice may not have to change significantly to meet new conduct regulations.

Emerging risks

The Group proactively scans for emerging risks which may have an impact on its ongoing operations and strategy. The Group considers its top emerging risks to be:

Political and macroeconomic uncertainty

As a result of the UK government triggering Article 50 and subsequent general election result, there is an increased likelihood of a period of macroeconomic uncertainty. The Group's lending activity is solely focused in the United Kingdom and as such, will be impacted by any risks emerging from changes in the macroeconomic environment.

Mitigation and controls

The Group has implemented robust monitoring processes and via various stress testing activity (i.e. ad hoc, risk appetite and ICAAP) understands how the Group performs over a variety of macroeconomic stress scenarios and has subsequently developed a suite of early warning indicators which are closely monitored to identify changes in the economic environment.

General data usage

From the 25 May 2018, the Group will comply with GDPR. This will result in increased regulatory requirements with respect to processing customer and employee personal and other data in the course of day-to-day business activities.

Mitigation and controls

The Group has mobilised a project (with dedicated resources) to implement the GDPR as required.

Viability Statement

In accordance with provision C.2.2 of the UK Corporate Governance Code, the Board of Directors have assessed the prospects and viability of the Group over a three-year period by comprehensively assessing the principal risks and uncertainties to which it is exposed and have concluded that they have a reasonable expectation that the Group will be able to continue to operate and meet its liabilities as they fall due over that period.

The three-year time period was selected for the following reasons:

- The Group's operating and financial plan covers a three-year period.
- The three-year operating and financial plan considers, among other matters: the Board's risk appetite; macroeconomic outlook; market opportunity; the competitive landscape; and sensitivity of the financial plan to volumes, margin pressures and capital requirements.
- The Board believes that there is sufficient visibility over the economic and regulatory landscape and the market outlook offered by the three-year time horizon to make a reasonable assessment of viability, and
- Uncertainty in the UK economic outlook over the medium to long-term following the EU referendum outcome.

The Company is authorised by the PRA, and regulated by the FCA and PRA, and undertakes regular analysis of its risk profile and assumptions. It has a robust set of policies, procedures and systems to undertake a comprehensive assessment of all the principal risks and uncertainties to which it is exposed on a current and forward-looking basis (as described in Principal Risks and uncertainties above).

The Group manages and monitors its risk profile through its strategic risk management framework, in particular through its risk appetite statement and risk limits. Potential changes in its risk profile are assessed across the business planning horizon by subjecting the operating and financial plan to severe but plausible macroeconomic and idiosyncratic scenarios.

Stress testing is a vital discipline, which underpins the Company's Individual Capital Adequacy Assessment Process ('ICAAP') and Individual Liquidity Adequacy Assessment Process ('ILAAP'). The Group has developed a bespoke macroeconomic model which identifies the most predictive macroeconomic variables and their relative relationship to arrears, collateral valuations and loan losses. As a secured mortgage lender the Group is most sensitive to changes in house price movements, unemployment and Bank of England base rate changes. The Group's stress testing capability then leverages the developed macroeconomic variable relationships to conduct detailed scenario analysis over a range of stress scenarios which feed key risk processes such as the setting of risk appetite, loan loss forecasts and ICAAP and ILAAP stress testing activity.

In addition, the Company identified a suite of credible management actions that would mitigate the impact of stress scenarios. The Board and executive management use the outcome of the stress test analysis to evaluate the Company's management options and adequacy of the Company's capital and liquidity resources to withstand an extreme but plausible stress scenario. The Company holds sufficient capital to withstand such a stress scenario.

In addition, the Group identifies a range of catastrophic stress scenarios, which could result in the failure of its current business model. Business model failure scenarios (reverse stress tests) are primarily used to inform the Board and executive management of the outer limits of the Group's risk profile. Reverse stress tests play an important role in helping the Board and its executives to identify potential recovery options under a business model failure scenario, and form an important aspect of the Company's recovery and resolution plans prescribed by the regulator. During the year, a number of reverse stress tests were analysed including an extreme macroeconomic downturn (1 in 200 severity), a cyber-attack leading to a loss of customer data which is used for fraudulent activities, extreme regulatory and taxation changes impacting Buy-to-Let lending volumes and a liquidity crisis caused by severe market conditions combined with idiosyncratic consequences.

The ongoing monitoring of all principal risks and uncertainties that could impact the operating and financial plan, together with the use of stress testing to ensure that the Group could survive a severe but plausible stress, enables the Board to reasonably assess the viability of the business model over a three-year period.

Directors' responsibility statement

The responsibility statement below has been prepared in connection with the full Annual Report of the Company for the year ended 31 December 2017. Certain parts of these accounts are not presented within this announcement.

The Directors are responsible for preparing the Annual Report and the Group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors are required to prepare the Group financial statements in accordance with International Financial Reporting Standards ('IFRS') as adopted by the European Union and applicable law and have elected to prepare the parent company financial statements on the same basis.

Under company law the Directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Group and parent company and of the profit or loss of the Company for that period.

In preparing each of the Group and parent company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently
- make judgements and estimates that are reasonable, relevant and reliable
- state whether they have been prepared in accordance with IFRSs as adopted by the EU
- assess the Group and parents Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy at any time the financial position of the parent company, and enable them to ensure that the financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Strategic Report, Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that complies with that law and those regulations. The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole; and
- the Strategic Report includes a fair review of the development and performance of the business and the position of the issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

We consider the Annual Report and accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Group's position and performance, business model and strategy.

Each of the persons who is a Director at the date of the approval of this report confirms that:

- so far as the Director is aware, there is no relevant audit information of which the Company's auditor is unaware;
- the Director has taken all the steps that he/she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Approved by the Board and signed on its behalf by:

Jason Elphick
Group General Counsel and Company Secretary
15 March 2018