Best in class specialist lending

2017 Results

15 March 2018

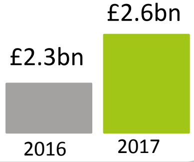
Another strong set of results for 2017

Unique business model...

...delivering yet another strong set of results

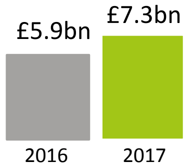
Gross organic lending

+ 14%



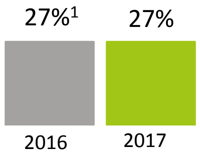
Net loan book

+ 23%



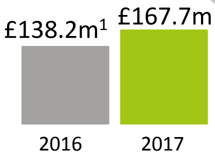
Cost to income ratio

Remaining strong



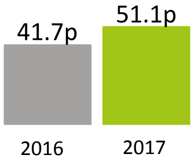
Underlying PBT

+ 21%



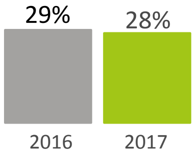
Underlying basic EPS

+ 23%



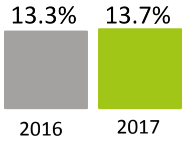
Return on equity

Best in class



Fully-loaded CET1 ratio

+ 0.4% points



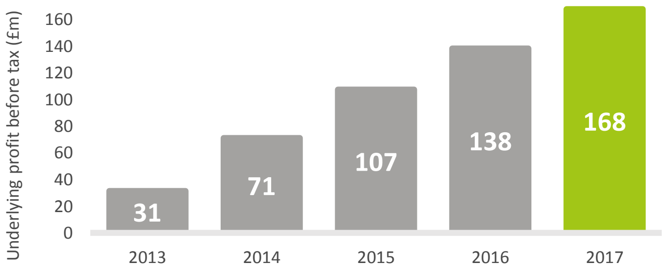
Dividend per share

12.8 pence per share (2016: 10.5p)

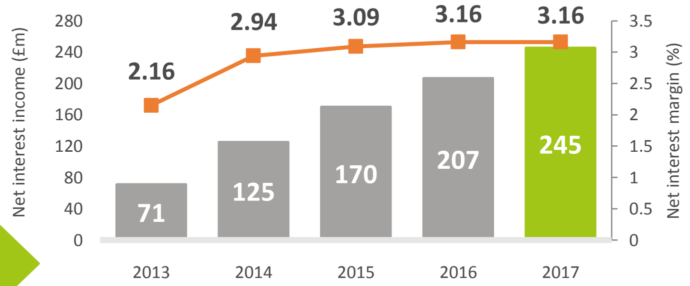
[1] Prior to 2017, OSB deducted coupons on equity Perpetual Subordinated Bonds ('PSBs') accounted for as dividends from underlying profit before and after tax, net interest margin and cost to income ratio. Following a review of market practice in advance of the Bank's AT1 issue, OSB no longer deducts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

Strong growth in profitability

1 Continued growth in underlying earnings[1]…

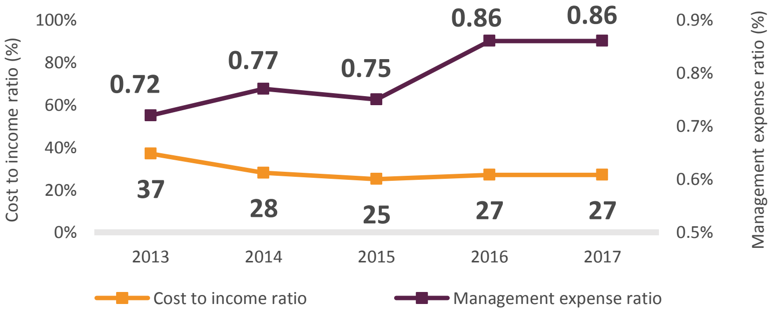


2 …with stable NIM & robust loan book growth[1]…

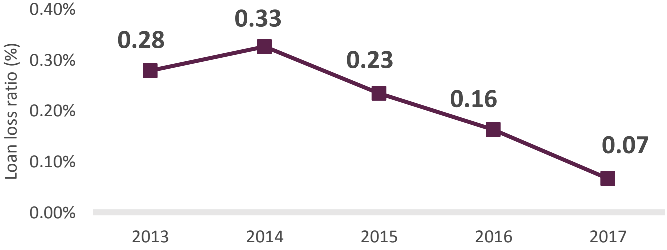


2017 RoE of 28%

3 …ongoing investment with well-controlled costs[1] …



4 …and strong credit quality

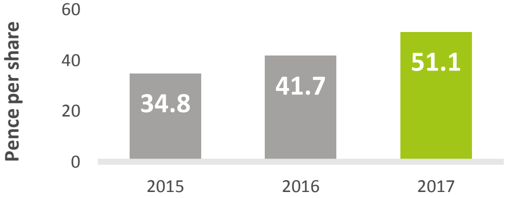


[1] Underlying profit before tax, net interest margin and cost to income ratio have been restated, see footnote on slide 2

Strong profitability drives growth in shareholder returns

	2017 £m	2016 £m	Change £m	Change %
Net interest income	245.4	206.6	38.8	*19*
Other expenses	(7.3)	(5.2)	(2.1)	*(40)*
Total income	**238.1**	**201.4**	**36.7**	***18***
Operating expenses	(65.1)	(53.7)	(11.4)	*(21)*
FSCS and other regulatory provisions	(0.9)	(0.5)	(0.4)	*(80)*
Impairment losses	(4.4)	(9.0)	4.6	*51*
Exceptional items	-	24.9[1]	(24.9)	*(100)*
Statutory PBT	**167.7**	**163.1**	**4.6**	***3***
Taxation	(40.8)	(42.2)	1.4	*3*
Statutory PAT	**126.9**	**120.9**	**6.0**	***5***
Effective tax rate	24.1%	25.6%	(1.5%)	
Underlying PBT	**167.7**	**138.2[2]**	**29.5**	***21***
Underlying PAT	**126.9**	**102.4[2]**	**24.5**	***24***

Underlying basic EPS



- Other expenses include £7.3m (2016: £4.9m) amortisation of fair value adjustments on cancelled swaps
- Impairment - improved loan loss ratio primarily due to increased prudency in assumptions taken in 2016 as well as lower underlying loan losses on acquired residential portfolios, and the effect of increasing property values reducing potential loss
- Underlying PBT up 21% reflecting strong balance sheet and net interest income growth
- Effective tax rate at 24.1% due to lower proportion of the Group's profits subject to the Bank Corporation Tax Surcharge
- Underlying basic EPS up 23% demonstrating the Group's robust business model

[1] In 2016 net gain from exceptional items included £34.7m gain on Rochester 1 disposal and £9.8m loss on amortisation of fair value adjustments on hedged assets
[2] Underlying profit before tax and underlying profit after tax have been restated, see footnote on slide 2

Strong growth whilst improving credit quality

	2017 £m	2016 £m	Change £m	Change %
Lending				
Net customer loans	7,306	5,939	1,367	*23*
o/w provisions	(22)	(25)	3	*12*
Funding and liquidity				
Customer deposits	6,650	5,952	698	*12*
Wholesale funding	26	5	21	*420*
Liquid assets	1,207	560	647	*115*
Funding for Lending Scheme	-	525	(525)	*(100)*
Term Funding Scheme	1,250	101	1,149	
Liquidity ratio	15.2%	17.9%		*(2.7)pts*

		2017	2016
Loan loss ratio (bps)		7	16
3 months in arrears (%)[1]		1.2	1.4
Legacy problem loans (£m)		8.6	13.8
Average LTV (%):	• mortgage book	64	63
	• Buy-to-Let/SME	69	69
	• Residential	56	58
Average LTV of new origination (%):			
	• mortgage book	69	69
	• Buy-to-Let/SME	70	70
	• Residential	65	66

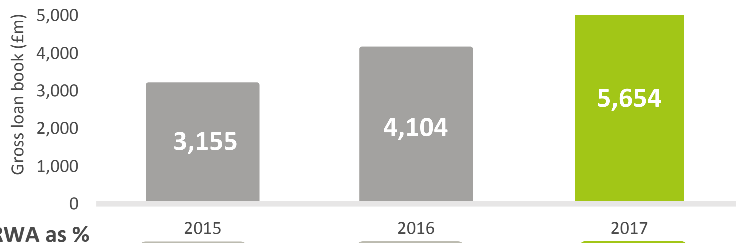
- Net loan book growth of 23% supported by 14% growth in organic origination to £2.6bn
- BoE funding schemes – transitioned out of FLS to the TFS, with TFS of £1.25bn as at 31 Dec 2017
- Liquidity coverage ratio of 250% significantly ahead of the 2017 regulatory minimum requirement of 90%
- Average LTV of new origination stable at 69% (2016: 69%)
- Weighted average interest coverage ratio ('ICR') for Buy-to-Let origination increased to 185% demonstrating prudent approach to assessment of customer affordability
- Only 4% of the Group's loan portfolio is secured on properties valued at greater than £2m with a LTV greater than 65%

1 Excluding legacy problem loan book

Segmental results – BTL/SME[1]

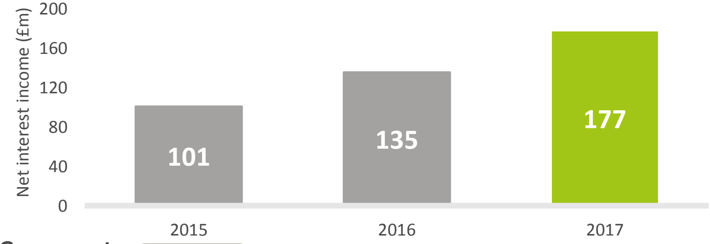
- LTVs remain low at 69% (2016: 69%) with only 0.7% of loans by value with LTVs exceeding 90% (2016: 0.4%)

1. Gross loan book[1]



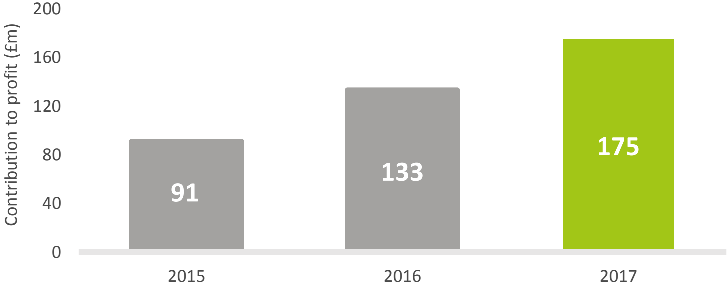
	2015	2016	2017
RWA as % of net loans	47%	48%	47%

2. Net interest income[1]

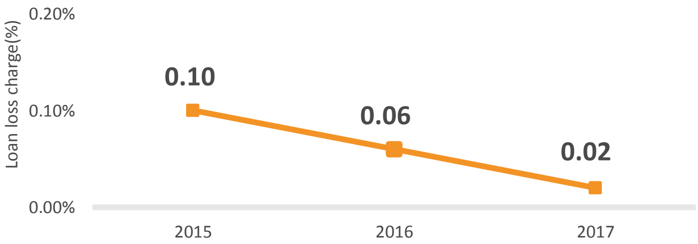


	2015	2016	2017
Gross asset yield	5.9%	5.8%	5.1%

3. Contribution to profit[1, 2]



4. Loan loss charge as a % of average gross loans[1]

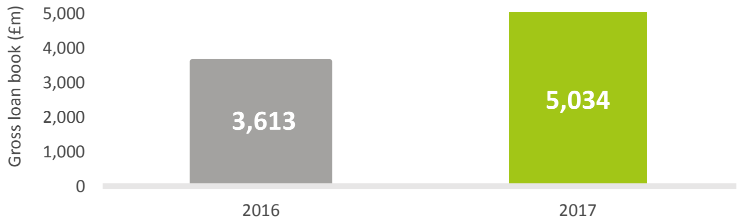


[1] The personal loan portfolio has largely completed its run-off and is therefore no longer considered as a separate segment by the Group. The remaining net loan book of £0.9m (31 December 2016: £9.1m) and negative contribution to profit for the period of £0.8m (2016: contribution to profit of £2.7m) have been reported in the Buy-to-Let/SME segment with comparatives restated accordingly. However, personal loans were excluded from the loan loss ratio in graph 4 above.

[2] Total income less impairment losses.

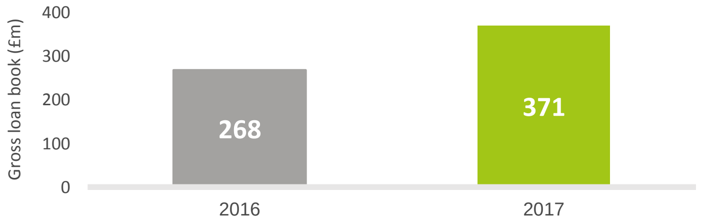
Segmental results – BTL/SME sub-segments

1. Buy-to-Let



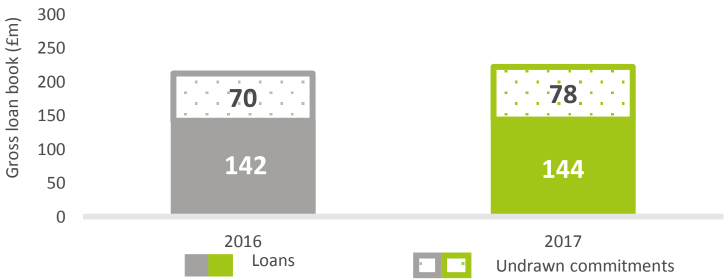
- Average interest rate coverage (ICR) was 185% during 2017 (2016: 171%)

2. Semi-commercial/Commercial



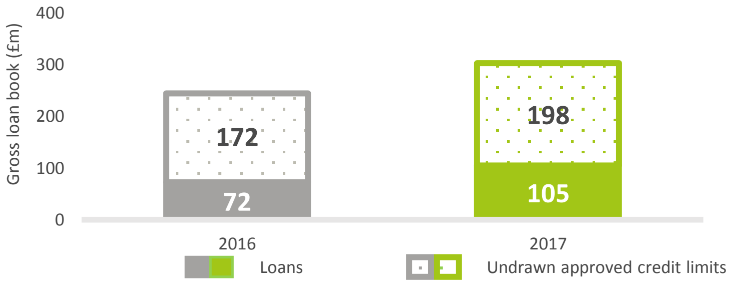
- Weighted average LTV: 63%
- Average loan size: £330,000

3. Residential development



- Target small to medium sized developers, active outside London
- Experienced and cautious team

4. Funding lines

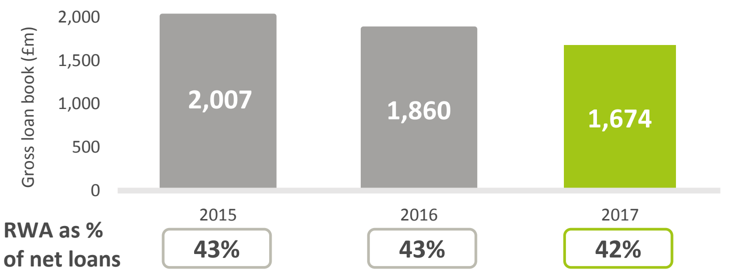


- Secured funding lines to non-bank lenders
- High yielding, secured, specialist sub-segments such as bridging finance and asset finance

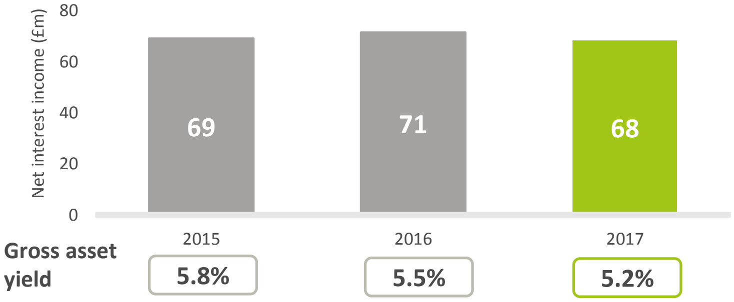
Segmental results – Residential

- Average LTV remains low at 56% (2016: 58%) with only 3% of loans by value with LTVs exceeding 90% (2016: 3%)

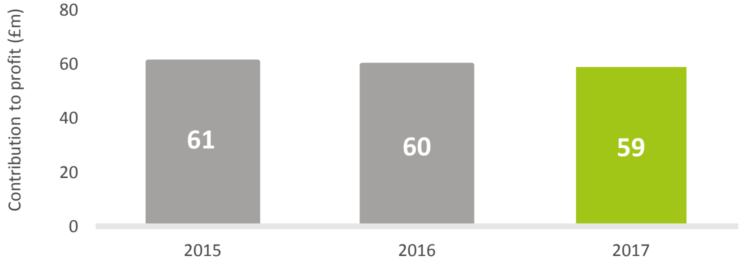
1. Gross loan book



2. Net interest income

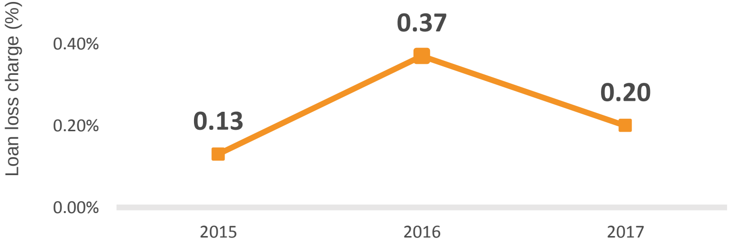


3. Contribution to profit[1]



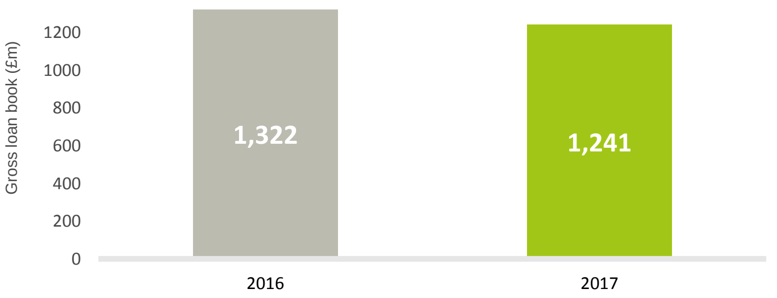
[1] Total income less impairment losses

4. Loan loss charge as a % of average gross loans

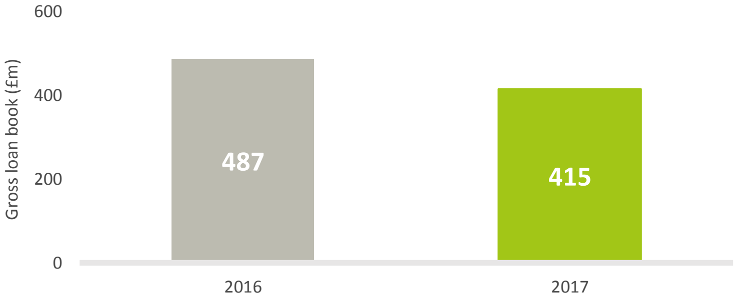


Segmental results – Residential sub-segments

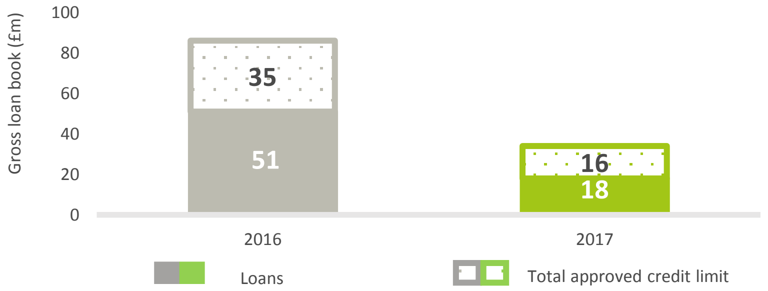
1. First charge mortgages



2. Second charge mortgages



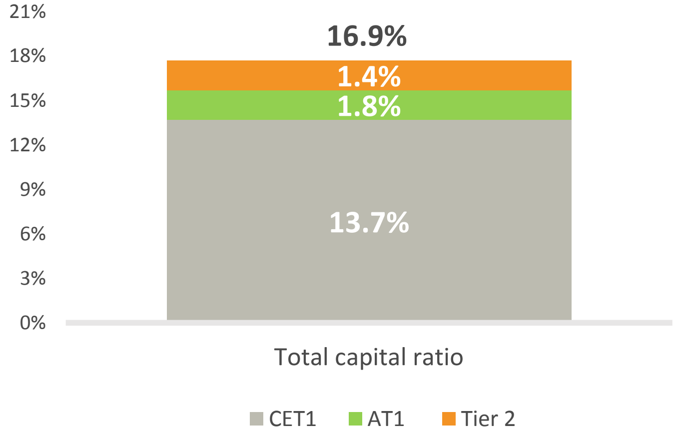
3. Funding lines



4. Summary

- First charge new organic lending in 2017 was more than offset by redemptions on the back book and acquired mortgage portfolios in run-off
- Second charge gross loan book reduced by c. 15% due to pricing in that market as we continued to exercise diligence in pricing for risk
- Reduction in funding lines loans outstanding due to the anticipated maturity of a £34m funding line at the start of the year

Stronger capital base, enhanced by AT1



	2017	2016	Change
Capital			
Risk-weighted assets (RWAs) £m	3,349	2,743	606
RWAs as % of total assets	39	42	(3%)
Common equity tier 1 ratio %	13.7	13.3	0.4
Total capital ratio %	16.9	15.1	1.8
Leverage ratio %	6.0	5.5	0.5

- Strong capital generation through profitability
- Successful issuance of £60m AT1 securities in May 2017 to optimise the capital stack and support general expenses and growth of the business
- Pillar 2a requirement of 1.1% of risk weighted assets
- We anticipate maintaining a CET1 ratio at a minimum of 12% going forward
- Successful parallel run of first generation IRB models throughout 2017

Forward guidance

Full year net loan book growth of mid-teens through organic lending

NIM for full year of c.3% reflecting current asset pricing and an expectation of rising cost of retail funds after the end of TFS

Full year cost to income of c.30% reflecting the increasing cost of regulation and planned additional investment

CET1 to remain at a minimum of 12% going forward

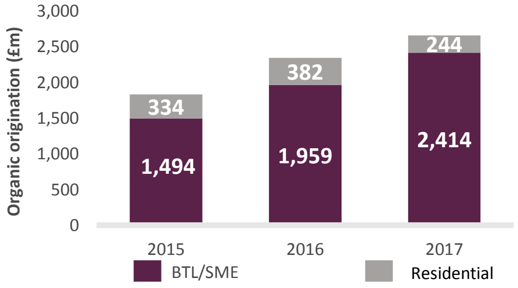
Dividend policy remains a payout ratio of at least 25%

IFRS 9 day one increase in loan loss provisions of c.£4m reflecting strength of security underpinning the loan book

Our award winning lending franchise performed strongly

Growth

Organic lending up 14%



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Retention

Significant increase in borrowers choosing new products with our 'Choices' retention scheme

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Net loan book growth of 23%

23%

Performance

Loan performance

Only 137 loans in 3m+ arrears (£18.4m), out of >38,500 loans (£8.3bn) originated since the Bank's creation in 2011

Well-positioned

- Five year fixed rate mortgages c.43% of Buy-to-Let completions
- Broker NPS recovered by year end to +25 for H2
- Limited companies account for 69% of purchase applications for Kent Reliance

Award winning

lending — mortgage strategy AWARDS '17 Best Specialist Lender WINNER

mortgage strategy AWARDS '17 Best BDM Team WINNER — distribution

Established brands

KentReliance

InterBay Commercial

Prestige Finance

Heritable Development Finance

Stable funding and award winning savings franchise

One Savings Bank

Growth

Retail deposits up

Retail deposits up 12% in the period

£6.7bn

\+

Recruiting new customers

We continue to attract new savings customers

27,000

\+

Diversification

We continued to draw funding from the TFS

£1.25bn

Performance

Strong customer retention

Retention rates on maturing Bonds and ISAs remain exceptionally strong

90%

Liquidity coverage ratio

Liquidity coverage ratio significantly ahead of the regulatory 90% minimum

250%

Award winning feedback

- Outstanding customer NPS +62
- Winning awards consistently over multiple years

WINNER
TWO TIMES
Moneyfacts Consumer Award 2016 & 2017
ISA Provider of the Year

Summary and outlook

2017 was yet another year of strong growth: 14% increase in organic origination to £2.6bn

Strong credit profile: low arrears and strong LTV coverage, and high interest cover on Buy-to-Let

Excellent customer results: customer NPS at +62, retail savings bond retention at 90%

Trading conditions in our core Buy-to-Let market remain positive and application levels for the first quarter to date are strong

Our loan book will remain predominantly retail funded, and for additional liquidity we intend to return to the securitisation market during 2018

Well capitalised to take advantage of further growth opportunities that provide long-term value and meet our strategic objectives

We see opportunities to broaden reach into adjacent markets and will invest further in growing our residential and commercial segments

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