Business Review

(including Summary Financial Statement)

Year ended 31 March 2018

the West Brom

Key highlights of the 2017/18 financial year

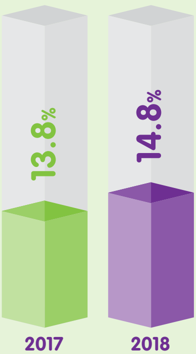
Statutory and underlying profit

£8.8m

Statutory and underlying profit before tax of **£8.8m** (2016/17: statutory loss of £19.8m, underlying profit of £7.7m), a 14% improvement in underlying performance.

18% increase in new mortgage lending

Gross residential mortgage advances up 18% to **£837m** (2016/17: £712m). At £265m (2016/17: £167m), new lending to first time buyers was the highest in the Society's history.



Strengthened capital position

14.8%

Strengthened capital position, with a Common Equity Tier 1 (CET 1) capital ratio of **14.8%** (2016/17: 13.8%). Successful modernisation of the capital structure after the year-end date through the issue of Core Capital Deferred Shares, qualifying CET 1 capital instruments.

17% reduction in commercial loans

17% reduction in non-core commercial loan book, falling to under £0.5bn at 31 March 2018 (2016/17: £0.6bn).

Recognition for our ongoing commitment to members and local communities being Highly Commended in the **Community Services** and Best Regional Building Society categories in the **Mortgage Finance Gazette Awards** for the second year running.

INVESTORS IN PEOPLE | Gold

Achievement of the Gold accreditation standard from Investors in People for our approach to people management.

Chief Executive's Business Review

Dear fellow members,

The Society has again performed well against its mutual purpose. At £837m residential lending was 18% higher than in the previous period, with lending to first time buyers the highest in the Society's history. For savers we were able to reverse the long-term decline in interest rates by passing on benefits from the first increase in Bank Rate for over 10 years. Although we took the opportunity to raise some long-term funding from institutional investors, which did result in overall retail balances reducing, our lending remains predominantly funded by retail savers. This mutual model of using members' deposits to promote residential lending to those who wish to own their own home has stood the test of time, nearly 170 years in fact for the West Brom and its generations of members.

Performance against our mutual purpose

Although the return to a statutory profit of £8.8m (2016/17: statutory loss of £19.8m) shows a dramatic swing in profitability, this is of course a distorted view given the one-off adjustment required in 2016/17. The prior year results included £27.5m of one-off costs related to reimbursing the interest charged on certain buy to let mortgages. It is therefore more appropriate to measure our progress in terms of the underlying position, whereby profits improved by 14% to £8.8m.

14% increase
in underlying profit before tax
(2016/17: £7.7m), to £8.8m

£8.8m
Statutory profit before tax
(2016/17: loss of £19.8m)

However, what truly reflects the success of the Society's strategy over the last decade has been returning its activities to those that best reflect our purpose. At 31 March 2008, the mortgage portfolio comprised only 36% lending for the purpose of home ownership, with the remainder being made up of 41% buy to let and 23% commercial loans. Moving forward 10 years, the Board's focus on the back to basics principles of the traditional building society model has fundamentally changed the composition of the loan book, which is now over 56% for home ownership, 34% buy to let and just 10% commercial lending. New residential lending for prime owner occupation has increased for the fifth consecutive year, by 18% to £837m (2016/17: £712m), with balances net of redemptions increasing to £2.7bn (2016/17: £2.3bn). These increased volumes have been achieved despite a fiercely competitive marketplace with historically low mortgage pricing being driven by the very low costs of funding provided under the Term Funding Scheme.

18% increase

in new residential lending (2016/17: £712m), to £837m

Clearly our support for home ownership also means we need to ensure we are able to help those wishing to buy their first house. It is pleasing to see that the Society has again supported an increasing number of first time buyers (nearly 2,000) through a range of products designed to keep initial setup costs to a minimum by offering up to 95% loan to value products with both free valuations and cashback options.

A number of demographic factors have continued to contribute to a decline in mortgage backed home ownership which has been particularly stark amongst younger generations. The Society recognises the importance of the role of the UK's housing market in supporting broader economic prosperity and in turn our own members' financial wellbeing. As a building society operating within the mutual sector our role is to ensure the availability of mortgage finance not only to first time buyers, but also those looking to build their own home and those looking to secure affordable borrowing options in retirement. Therefore, over the next year, we plan to expand our product offering to accommodate the changing needs of our borrowers.

The trust shown by our loyal saving members to hold their funds in safe and secure accounts in exchange for a good return underpins the success of our sustainable mutual model. Retail deposits of £4.1bn (2016/17: £4.4bn) represent a healthy 93% (2016/17: 104%) of residential mortgage balances. For savers, the long awaited decision of the Monetary Policy Committee to increase Bank Rate to 0.5% will have provided some good news for those reliant on interest receipts to support living costs or those who wish to grow their capital for a planned purpose or a rainy day. The weighted average savings rate paid by the Society across retail deposits continues to remain above the rate paid across the cash savings market as a whole with a number of competitively priced fixed and variable products launched through online, direct and branch channels. Last year in particular the launch of the Society's competitively priced Help to Buy ISA specifically through our branches illustrates our continued support for those looking to save for their first home in our heartland.

A modernised capital base

In January last year the Society received a challenge from a new minority shareholder of the Society's issued capital as to the eligibility of the Profit Participating Deferred Shares (PPDS) as Common Equity Tier 1 (CET 1) capital. While the Board remained of the unequivocal view that the PPDS met CET 1 requirements in all respects confirmation of this position was sought from the European Banking Authority (EBA). In the meantime the Board continued to act in the interests of members and pursued opportunities to assure the Society's regulatory capital position irrespective of any response from the EBA. To this end constructive engagement was held with a different group of holders, representing a majority of the PPDS and nearly half of the Permanent Interest Bearing Shares (PIBS). Following these discussions, it became clear that a modernisation of the Society's capital base would be appropriate regardless of any EBA decision.

Consequently, the Society announced a Liability Management Exercise (LME), which introduced two new capital instruments, Core Capital Deferred Shares (CCDS) and Subordinated Tier 2 Notes. This restructuring was completed in April, just after the financial year end, and resulted in an increase in member reserves of circa £50m. There was no material change in the Society's Common Equity Tier 1 or total capital ratios.

Our Common Equity Tier 1 ratio ended the year at 14.8% (2016/17: 13.8%) and our total capital ratio at 16.7% (2016/17: 16.0%). This is a strong position, enabling the Society to continue the success of recent years.

14.8%

Common Equity Tier 1 capital ratio (2016/17: 13.8%), up 1.0%.

The main factors underlying the financial performance and position of the Society are described in more detail below.

Net interest margin

There was a slight upwards movement in the net interest margin from 0.95% in 2016/17 to 0.96% at the current year end date.

It is not a strategic aim to maximise interest margin, rather to maintain it at a level adequate to cover the operational and capital costs of running a modern, customer focused and sufficiently capitalised organisation. Margin management involves balancing the needs of borrowing and saving members and making investments to support their long-term financial wellbeing.

A number of counterbalancing factors impacted the reported net interest margin. Residential mortgage yields were driven down by increased competition in the mortgage market despite an increase in Bank Rate by 0.25% to 0.50% in November 2017. The reduction in the buy to let book and commercial lending balances also reduced interest income. This was more than offset by lower overall funding costs, including the benefits from utilising the Bank of England's Term Funding Scheme (TFS) during the year, and growth in owner occupied residential lending. The highly competitive mortgage market is, however, expected to exert pressure on margins for some time to come.

0.96%

Net interest margin maintained (2016/17: 0.95%). We do not seek to maximise margin but deliver long-term value to members

Other income

Other income of £6.5m (2016/17: £6.8m) comprised insurance, investment and protection commissions, together with rental income earned by West Bromwich Homes Limited in its capacity as a responsible landlord.

Management expenses

Management expenses of £50.7m (2016/17: £50.1m) included a £1.5m increase in depreciation due to continued investment in our IT systems and infrastructure, as required to operate in a rapidly changing environment. Excluding depreciation charges, management expenses reduced by 2% (circa 4% in real terms, after taking inflation into account).

Management expenses include £0.3m of legal costs relating to the need for the Society to obtain external advice in response to the challenge to its PPDS qualifying as CET 1 capital explained previously. The costs of £2.7m associated with the Liability Management Exercise, a post balance sheet event, will be recognised through adjustments to the Society's capital.

The management expenses ratio increased slightly to 0.87%, in comparison with 0.86% in the previous year.

Continued spending on IT capability and security means the Society is well placed to deliver against the expectations of its current and future membership. Operational efficiency will remain a strategic priority, being fundamental to the enhancement of long-term member value.

0.87%

Management expenses ratio (2016/17: 0.86%) reflecting continued investment in infrastructure

Gains on investment properties

Via subsidiary company, West Bromwich Homes Limited, the Society provides access to residential housing predominantly in the West Midlands, the South West and South Wales.

The Property division's profits were generated by net rental income from the residential properties held and an increase in the market value of these properties. The latter resulted in a revaluation gain of £3.8m compared with £5.4m in the previous year.

Impairment provisions on loans and advances

Residential impairment credits of £0.1m (2016/17: £3.5m) were as expected, given the overall high credit quality of the residential prime owner occupied and buy to let portfolios. Residential loss allowances held on the balance sheet at 31 March 2018 were £13.2m (2016/17: £16.3m).

During the year, the Group incurred commercial impairment costs of £8.0m (2016/17: 11.1m), with provisions of £42.1m (2016/17: £39.4m) now set aside for losses on commercial mortgages. The ratio of provisions to commercial exposures was 8.6%, compared with 6.7% in the prior year. The level of coverage is considered appropriate for this portfolio, which has historically proved itself susceptible to any downturn in the economic environment. At 31 March 2018, 55% (2016/17: 56%) of commercial balances were being managed by a Law of Property Act Receiver (LPAR), with a view to achieving the best possible outcome in exiting the exposures.

Responsible lending, responsible funding

With significant growth in residential lending it is also pleasing to report that residential mortgage arrears have fallen for the fifth consecutive year. This performance is testament to the Society's capability to assess borrowers' creditworthiness supported by robust affordability models, scorecard processes and individual underwriting methods. Furthermore, the more seasoned residential loans that remain from the period leading up to the financial crisis are now performing well following a period of careful management. Core residential arrears ended the year at 0.38% (2016/17: 0.63%), below the UK Finance average of 0.81%.

I have already referred to the benefit of the Bank Rate increase for the Society's saving members although, of course, a number of borrowers will have seen an increase in their mortgage interest payments. However, with the vast majority, some 87%, of new lending on a fixed rate very few new borrowers are exposed to any immediate impact of Bank Rate increases. When ultimately borrowers do face the potential of paying a higher rate at the end of their initial fixed rate deal, we ensure that at the point of agreeing the loan that the mortgage is still affordable should there be a need to pay a considerably higher interest rate – currently more than three times the level of interest initially being paid.

Most new borrowers prefer the security of knowing what their monthly repayments will be by fixing their mortgage rate.

As a mutual, the Society remains committed to funding the majority of new residential lending growth with members' retail deposits; however the quality of the lending portfolio also provides opportunities to source long-term wholesale funding through the issuance of Residential Mortgage Backed Securities (RMBS) where it is economically sensible to do so. To this end I am pleased to report that in January the Society successfully raised £350m of low cost securitisation funding - the first time the Society has transacted in the market in five years, illustrating the confidence external investors have in the Society's ability to originate mortgage lending responsibly from good quality borrowers.

Non-core progress

Our determination to offer high quality products and services tailored to the needs of members has underpinned the commitment we made in 2009 to exit those areas that did not fit with this fundamental principle. Coming into the financial crisis of 2008/9 the Society's exposure to the commercial real estate sector stood in the region of £1.7bn. We have been conducting a carefully managed exit from this high risk exposure such that at the year end this exposure had reduced to £488m, 17% lower than the previous year and over 70% lower than the peak position. Furthermore, of the outstanding exposure some £53m is held in securitisation vehicles which, in effect, transfers the risk out of the Society. Of the remaining balance sheet exposure £254m is being managed by a Law of Property Act Receiver or Administrator, in order to achieve the best possible outcome, with £34m set aside by way of provision.

Our members' financial wellbeing

The Society strives to offer high quality products, in a responsible way, to support the financial wellbeing of our circa 434,000 members. The product range offered by the Society allows members to build financial resilience by maintaining a personal savings buffer against unexpected events and/or by continuing to build equity in their home funded through a mortgage. In addition to these core offerings the Society continues to offer a wide selection of auxiliary products from household insurance helping customers protect their homes to later life planning and the financial advice offering supported by our partners Wren Sterling.

Our communities

We take our role as a regional building society seriously and continue to make a conscious effort to assist local communities, especially in our heartland area where our branches operate. This year the Society has partnered with The Kaleidoscope Plus Group who work tirelessly throughout the region to help people achieve better mental and emotional health. Through numerous fundraising events, the Society raised an impressive £30,000 for Kaleidoscope Plus. I would like to take this opportunity to thank Kaleidoscope Plus as our charity of the year for 2017/18 with funds raised by the Society going towards the charity's Safe Spaces initiative, which supports people affected by suicide. As part of our year-long partnership, Kaleidoscope Plus also worked with a number of our people on mental health awareness training.

The West Brom's support does not end with financial donations. This year, some 115 of the Society's people actively engaged in our popular volunteering programme where various teams from the Society supported a variety of local community projects. Our financial awareness programme 'The Money-Go-Round' continues to go from strength to strength, promoting the importance of financial awareness for the next generation. I am proud to report that these awareness sessions have now been delivered to 20 schools all within the Midlands Region.

Branch managers have spent time with local school children to talk about the value of money and raise awareness of good money management.

Along that same theme, earlier this year the Society announced plans to bring our regional heritage to life through a unique partnership with the Black Country Living Museum. This new project, due for completion in 2022, will see construction of a replica West Brom 1940s branch as part of a new museum development. This educational facility will enable visitors to gain a contextual understanding of how the principles of mutuality supported the home ownership aspirations of local communities – the same premise from which the Society functions today.

Promoting engagement

Over recent years I have frequently talked about the importance of maximising the feedback we get in order to ensure we understand what will best support our members, and we are clear on what best enables my colleagues to deliver the best service we can. We have decided to make a further significant step and move beyond the initiatives we have launched in recent years by introducing two new important groups: a Member Council and an Employee Council.

Understanding what matters to both members and colleagues will help with decision making and setting our future strategy.

Both of these will be asked to consider issues that directly affect the Society, its members and how we deliver our products, services and community responsibilities, to contribute thoughts and provide perspectives that will be taken into account by the Executive and the Board when making key decisions. Recruitment for these two important groups is expected to be before the end of 2018. Continuing the theme of ensuring we, as a modern mutual, retain the vital participation of members in decision making, we are the first building society to move to a binding vote on the Directors' Remuneration Policy; this vote will take place at the forthcoming Annual General Meeting.

A vibrant future based on a traditional approach

Over what is now nearly 170 years the Society has existed through times of immense upheaval and changing thoughts on how core financial products and services can be delivered. Thriving through these times means that the Society has remained constantly modern and relevant. Perhaps we are now facing as much change and uncertainty as has existed for many periods throughout our history, not just in relation to the economy and how we come through Brexit, but also technology and the drive to digitalisation. These are all challenges we are set to take on and ensure we remain relevant for our members, present and future.

This will involve considerable change, principally in our core technologies, but we have started on this journey. We have ensured we have the capital strength, have reshaped the Society's business mix to be very clear as to who we are here to serve and have resourced ourselves to progress the next phase of technology change.

Of course, all the achievements I have detailed above are a consequence of the people who make it all happen, my colleagues. I would like to take the opportunity to thank them all for their commitment, skills and desire to deliver their best at all times on your behalf.

Jonathan Westhoff
Chief Executive
30 May 2018

Summary Financial Statement

Year ended 31 March 2018

This Financial Statement is a summary of the information in the audited Annual Accounts, the Directors' Report and the Annual Business Statement, all of which will be available to members and depositors free of charge on request at every office of West Bromwich Building Society from 5 June 2018.

Summary Directors' Report

The information contained in the Chief Executive's Business Review on pages 3 to 8 of this document addresses the requirements of the Summary Directors' Report.

Summary Financial Statement

Group results for the year	**2018 £m**	2017 £m
Net interest receivable	**55.5**	55.3
Other income and charges	**6.5**	6.8
Fair value gains/(losses)	**2.5**	(0.2)
Net realised profits	**-**	0.5
Administrative expenses	**(50.7)**	(50.1)
Operating profit before revaluation gains, impairment and provisions	**13.8**	12.3
Gains on investment properties	**3.8**	5.4
Impairment losses	**(7.9)**	(7.6)
Provisions for liabilities	**(0.9)**	(29.9)
Profit/(Loss) before tax	**8.8**	(19.8)
Taxation	**(0.9)**	(6.0)
Profit/(Loss) for the financial year	**7.9**	(25.8)

Group financial position at end of year	**2018 £m**	2017 £m
Assets		
Liquid assets	**757.2**	853.8
Mortgages	**4,805.4**	4,776.5
Derivative financial instruments	**19.5**	6.3
Fixed and other assets	**199.4**	194.2
Total assets	**5,781.5**	5,830.8
Liabilities		
Shares	**4,051.4**	4,427.3
Borrowings	**1,197.7**	846.2
Derivative financial instruments	**38.7**	69.0
Other liabilities	**23.7**	24.8
Profit participating deferred shares	**175.0**	173.0
Subscribed capital	**75.0**	75.0
Reserves	**216.6**	212.0
Revaluation reserve	**3.4**	3.5
Total liabilities	**5,781.5**	5,830.8

Summary Financial Statement (continued)

Year ended 31 March 2018

Summary of key financial ratios	2018 %	2017 %
Gross capital As a percentage of shares and borrowings	**8.95**	8.79
Liquid assets As a percentage of shares and borrowings	**14.43**	16.19
Profit/(Loss) for the year As a percentage of mean total assets	**0.14**	(0.44)
Management expenses As a percentage of mean total assets	**0.87**	0.86

'Gross capital' represents the aggregate of reserves, revaluation reserve, subscribed capital and profit participating deferred shares.

'Shares and borrowings' represent the total of shares and borrowings (including non-recourse finance).

'Management expenses' represent administrative expenses.

This Summary Financial Statement was approved by the Board of Directors on 30 May 2018.

Mark Nicholls
Chairman

Jonathan Westhoff
Chief Executive

Ashraf Piranie
Group Finance &
Operations Director

Independent Auditor’s Statement to the Members and Depositors of West Bromwich Building Society

Opinion

We have examined the Summary Financial Statement of West Bromwich Building Society (the Society) for the year ended 31 March 2018 set out on pages 9 to 10.

On the basis of the work performed, as described below, in our opinion the summary financial statement is consistent with the full financial statements, the Annual Business Statement and Directors’ Report of the Society for the year ended 31 March 2018 and conforms with the applicable requirements of section 76 of the Building Societies Act 1986 and regulations made under it.

Basis for opinion

Our examination of the summary financial statement consisted primarily of:

- Agreeing the amounts and disclosures included in the summary financial statement to the corresponding items within the full annual accounts, Annual Business Statement and Directors’ Report of the Society for the year ended 31 March 2018, including consideration of whether, in our opinion, the information in the summary financial statement has been summarised in a manner which is not consistent with the full annual accounts, the Annual Business Statement and Directors’ Report of the Society for that year;
- Checking that the format and content of the summary financial statement is consistent with the requirements of section 76 of the Building Societies Act 1986 and regulations made under it; and
- Considering whether, in our opinion, information has been omitted which although not required to be included under the relevant requirements of section 76 of the Building Societies Act 1986 and regulations made under it, is nevertheless necessary to include to ensure consistency with the full annual accounts, the Annual Business Statement and Directors’ Report of the Society for the year ended 31 March 2018.

We also read the other information contained in the Business Review and consider the implications for our statement if we become aware of any apparent misstatements or material inconsistencies with the summary financial statement.

Our report on the Society’s full annual accounts describes the basis of our opinions on those annual accounts, the Annual Business Statement and Directors’ Report.

Directors’ responsibilities

The directors are responsible for preparing the summary financial statement within the Business Review, in accordance with applicable United Kingdom law.

Auditor’s responsibilities

Our responsibility is to report to you our opinion on the consistency of the summary financial statement within the Business Review with the full annual accounts, Annual Business Statement and Directors’ Report and its conformity with the relevant requirements of section 76 of the Building Societies Act 1986 and regulations made under it.

The purpose of our work and to whom we owe our responsibilities

This auditor’s statement is made solely to the society’s members, as a body, and to the society’s depositors, as a body, in accordance with section 76 of the Building Societies Act 1986. Our work has been undertaken so that we might state to the society’s members and depositors those matters we are required to state to them in such a statement and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the society and the society’s members as a body and the society’s depositors as a body, for our work, for this statement, or for the opinions we have formed.

Andrew Walker
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
One Snowhill
Snow Hill Queensway
Birmingham
B4 6GH
30 May 2018

Braille, audio and large print versions of this leaflet are available upon request. Please contact us on 0345 241 3784.

Head Office: 2 Providence Place, West Bromwich B70 8AF
www.westbrom.co.uk

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