MANCHESTER BUILDING SOCIETY GROUP

CONDENSED CONSOLIDATED HALF YEARLY FINANCIAL INFORMATION

30 JUNE 2022

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DIRECTORS' REPORT

Introduction

The Directors present their Condensed Consolidated Half Yearly Financial Information of the Group for the 6 months ended 30 June 2022.

At 30 June 2022 the Group consisted of the Society and its wholly owned subsidiary, MBS (Mortgages) Limited.

Strategic summary

The Society is owned by its members. The means by which its value is preserved is by providing products that meet the financial needs of members.

The Group's strategy since 2013 has been to reduce its risks and conserve its regulatory capital and no new lending has been written in this period. This strategy was necessary because of events, fully disclosed in the Annual Report and Accounts for the year ended 31 December 2012, that led to a material write-down of the Group's reserves following a change in the accounting treatment of certain financial assets.

Following the judgment of the Supreme Court in June 2021 in relation to the legal action that the Society took against its former auditors, Grant Thornton (UK) LLP ("GT"), where the Society was awarded £13.4m in damages and subsequently received an additional £10.8m in relation to costs and interest, the Society has continued to reduce risks by reducing the size of the balance sheet by abstaining from new lending.

During this period since the judgment, the Board has continued to investigate strategic options available to the Society. One such option would be to merge the with another, larger, Building Society and preliminary merger talks are taking place with Newcastle Building Society ("NBS"). Whilst this remains just one potential strategic option for the Society, it is felt by the Board, that in principle, such a merger would be in the best interest of the Manchester's members. The Society will work with NBS, advisers and regulators to fully investigate the opportunities that this may bring to both societies and the Building Society sector.

Until an alternative strategy is agreed, regulatory capital conservation continues to be a priority and the Society will continue to follow the medium to long term strategic plan that has been shared with the Prudential Regulation Authority ("PRA"). The Group continues to have headroom above its Total Capital Requirements in total capital terms and meets the qualitative standards for the level of Common Equity Tier 1 ("CET 1") regulatory capital. Payments on both its issuances of Permanent Interest Bearing Shares ("PIBS") resumed in October 2021 and continue to be paid. Whilst the Society continues to manage down the size of the balance sheet, there remains some uncertainty over the Society's ability to make PIBS coupon payments in the long-term.

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

Business review

The Group recorded a profit after taxation for the 6 months ended 30 June 2022 of £2.0m, compared with a profit after taxation for the 6 months ended 30 June 2021 of £20.4m.

The recorded profit includes £2.4m in relation to costs recovered following the Supreme Court judgment in June 2021. The profit recorded in the 6 months to 30 June 2021 included £21.8m in relation to this judgment.

The UK economy continues to be impacted by external events. Whilst the direct impacts from the Covid-19 pandemic have largely passed, the economic impacts remain. These, coupled with the effects of Brexit and the war in Ukraine have led to higher than forecast inflation and an increasing base rate environment. This directly impacts upon the Society's underlying performance.

Mortgage assets reduced by 7% in the 6 months ended 30 June 2022 as the Group continued to make no new advances.

The Group's net interest income was £2.5m, compared with £3.1m for the comparative period in 2021. Interest receivable reduced from £3.8m to £3.6m whilst interest payable increased from £0.7m to £1.1m.

Interest received on mortgages reduced by 6% compared with the comparable period in 2021. Balances in June 2022 were 15% lower than in June 2021. Bank base rate linked mortgages have seen an increase in rates in the period, offsetting some of the income lost through balance reductions. Interest received on liquid funds was £0.1m higher than in the comparable period.

Interest payable included £0.2m in relation to interest paid on PIBS and £0.6m of interest recognised on redemption of the subordinated debt. No PIBS interest was recognised in the 6 months to 30 June 2021 as such payments were prohibited under the applicable regulatory capital conservation rules. The underlying reduction of £0.1m related to savings account balance reductions, partially offset by higher rates paid.

Other operating income for the 6 months ended 30 June 2022 was £0.4m, compared to £nil for the comparative period in 2021. This income related to movements in the Sterling: Euro exchange rate. No losses were recognised in the period. Exchange rate losses in the 6 months to 30 June 2021 were £0.5m. Exchange gains and losses are largely offset within impairment in each period.

The Group's administrative expenditure of £2.5m was £0.2m higher than in the comparative period in 2021 with £0.2m (6 months ended 31 June 2021: £0.2m) of costs being recognized in relation to the migration of the Society's core banking system. Staff costs have increased by £0.1m.

An Expected Credit Loss release of £0.1m was recorded in the period in respect of the Group's UK mortgage and loan books, in line with a release of £0.1m in the first half of 2021.

An Other Impairment Losses charge of £0.8m was recorded in the period in respect of the Group's Spanish mortgage and loan books, compared to a charge of £0.2m in the first half of 2021. The charge included a £0.3m charge (June 2021: £0.5m release) relating to the Sterling: Euro exchange rate (largely offset in other operating charges).

The Group continues to offer support to customers in financial difficulties to help resolve their situations, taking a consultative approach with borrowers who experienced repayment difficulties and applying forbearance as appropriate. At 30 June 2022, excluding the second charge portfolio, there were 17 mortgage accounts where payments were 12 or more months in arrears (31 December 2021: 17). Total arrears were £0.7m (31 December 2021: £0.8m).

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

Risks and uncertainties

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

The last two and a half years have seen uncertainty in the economy because of the Covid pandemic, the UK leaving the European Union ("EU") and war in Ukraine. The medium to long-term impact of both on UK government policy, the financial markets and the wider UK economy remains unclear. The Group's Spanish lifetime portfolio introduces additional uncertainty and risk as a result of Brexit which the Board is monitoring; in particular there is added risk and uncertainty in relation to foreign exchange volatility, property values for the Spanish lifetime portfolio and the behavioural impact on Spanish lifetime mortgage borrowers. The legal advice taken by the Group remains that operational risk in relation to the servicing of the loan book is limited.

Under IFRS 9 – Financial instruments impairment is based on expected credit losses ("ECL"). An ECL provision is required for default events in the next 12 months, whilst a lifetime ECL is required when a significant increase in credit risk is identified. The review of credit risk and the calculation of ECL are required to be unbiased and probability weighted, and should include all available relevant information, with assessments of current conditions and forecasts of future economic conditions. As a result the recognition and measurement of impairment is forward looking. Forecasts of economic conditions are uncertain and adverse movements in the forecasts create additional risks for the Group.

At the end of 2021, the London Inter-Bank Offered Rate ("LIBOR") ceased to be considered as an appropriate rate for setting interest rates meaning that loans and savings accounts linked to LIBOR need to be transitioned to an alternative benchmark rate. In response, the Society has redeemed its LIBOR linked subordinated debt and has contacted affected mortgage customers to offer an alternative. A small number of mortgage customers have not yet accepted the proposed rate and remain on "synthetic LIBOR" in line with FCA guidelines

A full explanation of the Board's assessment of the risks and uncertainties that are faced by the Group was set out in the 2021 Annual Report and Accounts on pages 5 to 6. The key risks remain similar to those identified last year.

Summarised below are the Group's other key risks and uncertainties:

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

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

The assessment of credit risk and the related impairment provisioning is a critical accounting estimate, impacted by judgments relating to customer affordability and economic circumstances, including the level of interest rates. Prior to the current strategy of abstaining from new lending, credit risk was mitigated by appropriate mortgage underwriting and by limiting the Group's exposure to particular market sectors or loans exhibiting particular attributes. Since the cessation of new lending, credit risk has been mitigated through the monitoring of management information, assessment of arrears and forbearance cases, and regular loan provision reviews. The Society continues to work with customers to ensure that appropriate levels of forbearance are provided where necessary. The Group holds two mortgage books (the NMB MAC and CLC books), where previously it held a beneficial interest and these portfolios were administered by third parties. The Group assumed ownership of the CLC portfolio in 2015 and the NMB MAC portfolio in 2018. An assessment has been made of the estimated discounted future cash flows expected to arise from both these portfolios of loans which forms the basis for the impairment provision.

The current high levels of inflation and the Bank of England base rate increases that have followed increase the likelihood of defaults on loans with borrowers having lower levels of disposable income. The Society is monitoring this closely and will work with customers in financial difficulty. No increase in defaults has been experienced to date.

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

Insurance risk is currently accounted for under IFRS 4 – Insurance Contracts. IFRS 4 will be superseded by IFRS 17 – Insurance Contracts for accounting periods beginning on 1 January 2023. The Group will need to change its accounting methodology to one that is either appropriate under IFRS 17 or under IFRS 9 – Financial Instruments.

Liquidity Risk: The Group's strategy is to always maintain sufficient funds in unencumbered liquid form to ensure that its liabilities can be met as they fall due. Regular stress testing of liquidity is undertaken by separately using 20 week and 3-month time horizons. The Group operates within closely monitored Board-approved liquidity policy limits, which are reviewed daily by the Group's Finance and Treasury departments, reported to the Treasury Committee and considered by the Board each month. During the first half of 2022, the Group continued to have a significant proportion of its liquid assets deposited with the Bank of England.

Capital Risk: In order to conserve capital, the Group has not undertaken new lending since 2013. Following the profit generated in 2021, the Group now meets all of the quantitative and qualitative requirements regarding the level of regulatory capital it must hold. PIBS coupon payments were made on both issuances of PIBS in April 2022. These payments resumed in October 2021 following a period when the Group was not permitted to make such payments. The risk of an external stress event such as a severe downturn in the housing market in either the UK or Spain, a regulatory requirement to hold additional capital or a change in accounting standards means that there remains some uncertainty over the Group's ability to make coupon payments in the long-term.

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

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

Currency Risk: The Group faces currency movement risks on its Euro-denominated mortgage balances which represent 23% of total mortgage assets as at 30 June 2022 (22% at 30 June 2021 and 21% at 31 December 2021). The exchange rate risk arising on these balances is managed and partially mitigated by transacting foreign exchange forward contracts. The exchange rate risk position is reported to the Asset and Liability Committee ('ALCO') and Board each month.

Economic Risk: The Group faces the risk that its interest margin can become subjected to the pressure that is brought to bear from being an institution that is primarily funded through retail deposits. Within this market, there is great competition for attracting retail deposits at sustainable rates of interest. The increasing base rate environment and the end of the Bank of England's Funding for Lending and Term Funding Schemes may lead to upward pressure on rates to prevent savings outflows.

The Group is also exposed to movements in the value of residential and commercial property in both its mortgage impairment provision requirements and the Group's "held for sale" property which is held at fair value.

Political Risk: The UK's exit from the EU in January 2020 continues to create additional uncertainties for the economy, financial markets, housing and mortgage markets, government policy and financial services regulation. The impact upon borrower behaviour and collateral values within the Spanish lifetime portfolio remains uncertain. The Group has taken legal advice and contacted the regulatory authority in Spain and believes that operational risk in relation to the servicing of the loan book is limited.

The Government's response to the Covid-19 pandemic resulted in an unprecedented economic downturn, with significant support offered to people affected. Recovery from the impacts of the pandemic are being affected by increases in costs of living, particularly driven by fuel and utility costs, exacerbated by the conflict in Ukraine and international sanctions placed on Russia. The impact in both the short-term and the medium-to-long-term remain uncertain. Unemployment levels and house prices have particular impacts upon the Group's credit risk.

Climate Change Risk: The Society continues to assess how climate change may impact its business. This includes the impact of increased incidents of flooding on the value of some properties within its mortgage portfolio and impacts on borrowers of requirements for minimum efficiency standards for their homes or rental properties. The Society's Finance Director is responsible for incorporating the financial risks from climate change into existing risk management practices.

Cyber Risk: The Group faces the risks of inappropriate disclosure of personal or sensitive information and inappropriate access to internal data sources, particularly cyber security threats to the Society and its Members as a result of attacks using computer systems. The Society has appropriate controls in place and uses third party expertise to mitigate this risk. The group holds cyber insurance to further mitigate any potential financial loss or disruption.

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

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

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

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

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

Other Matters

Board and staff changes

The Directors and Officers as at 30 June 2022 remain unchanged from those disclosed at 31 December 2021 on page 66 of the 2021 Annual Report and Accounts.

Going Concern

The directors consider that it is appropriate for the accounts to be prepared on a going concern basis of accounting as fully explained in Note 1.2 on pages 14 and 15, which sets out the risks and uncertainties assessed as part of the preparation of the accounts.

Forward-looking statements

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

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

Approval of interim financial statements

The Condensed Consolidated Half Yearly Financial Information was approved by the Board of Directors on 11 August 2022.

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

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

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

The results for the half year ended 30 June 2022 and those comparable figures for the half year ended 30 June 2021 are unaudited. The figures for the year ended 2021 are extracted from the 2021 Annual Report and Accounts, prepared in accordance with IFRS as adopted in the EU, on which the Independent Auditors gave an unqualified opinion.

The Directors are responsible for the maintenance and integrity of information on the Society's website. Copies of the 2021 Annual Report & Accounts and this Half Yearly Financial Information may be found at: www.themanchester.co.uk/Main/FinancialInformation

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

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

Signed on behalf of the Board of Directors

D.A. Harding
Chairman
11 August 2022

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Note	Unaudited 6 months to 30-Jun-22 £000	Unaudited 6 months to 30-Jun-21 £000	Audited 12 months to 31-Dec-21 £000
Interest receivable and similar income		3,579	3,802	7,544
Interest expense and similar charges		(1,111)	(691)	(1,371)
Net interest income		2,468	3,111	6,173
Legal damages and interest		-	14,272	14,272
Net loss on assets classified as held for sale		-	-	(194)
Other operating income		385	18	-
Other operating charges		(22)	(528)	(811)
Total operating income		2,831	16,873	19,440
Legal costs recovered		2,400	7,540	7,540
Administrative expenses and depreciation		(2,453)	(2,292)	(4,854)
Operating profit before impairment and provisions		2,778	22,121	22,126
Expected credit losses	*6*	81	106	151
Other impairment losses	*6*	(838)	(218)	(1,440)
Profit for the period before taxation		2,021	22,009	20,837
Income tax expense	*10*	-	(1,563)	(1,467)
Profit for the period		2,021	20,446	19,370

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Unaudited 6 months to 30 June 2022

	Retained earnings	Subscribed capital	PPDS	Total
	£000	£000	£000	£000
Closing Balance at 31 December 2021	8,085	9,788	17,461	35,334
Transactions with equity holders - interest on PIBS	(338)	-	-	(338)
Profit and total comprehensive income for the period	2,021	-	-	2,021
Balance at 30 June 2022	9,768	9,788	17,461	37,017

Unaudited 6 months to 30 June 2021

	Retained earnings	Subscribed capital	PPDS	Total
	£000	£000	£000	£000
Closing Balance at 31 December 2020	(11,011)	9,788	17,461	16,238
Profit and total comprehensive income for the period	20,446	-	-	20,446
Balance at 30 June 2021	9,435	9,788	17,461	36,684

Audited 12 months to 31 December 2021

	Retained earnings	Subscribed capital	PPDS	Total
	£000	£000	£000	£000
Closing Balance at 31 December 2020	(11,011)	9,788	17,461	16,238
Transactions with equity holders - interest on PIBS	(338)	-	-	(338)
Tax credit relating to interest on PIBS	64	-	-	64
Profit and total comprehensive income for the period	19,370	-	-	19,370
Balance at 31 December 2021	8,085	9,788	17,461	35,334

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Note	Unaudited 30-Jun-22 £000	Unaudited 30-Jun-21 £000	Audited 31-Dec-21 £000
Assets				
Liquid assets	4	43,422	41,813	48,293
Derivative financial instruments		29	711	712
Loans and advances to customers	5	142,240	166,381	153,300
Intangible Fixed Assets		38	49	44
Property, plant and equipment		187	277	229
Non-current assets classified as held for sale	7	447	-	491
Deferred tax assets	8	-	-	-
Other assets		2,641	23,470	1,537
Total assets		189,004	232,701	204,606

	Note	Unaudited 30-Jun-22 £000	Unaudited 30-Jun-21 £000	Audited 31-Dec-21 £000
Liabilities				
Due to members		138,832	166,270	150,254
Deposits from banks and others	9	6,549	7,588	7,036
Derivative financial instruments		774	38	9
Other liabilities		832	1,358	1,287
Current tax liability	10	-	1,563	686
Subordinated liabilities	11	-	14,200	5,000
Subscribed capital	12	5,000	5,000	5,000
Total liabilities		151,987	196,017	169,272
Equity				
Retained earnings		9,768	9,435	8,085
Subscribed capital	12	9,788	9,788	9,788
Profit participating deferred shares	13	17,461	17,461	17,461
Total equity		37,017	36,684	35,334
Total equity and liabilities		189,004	232,701	204,606

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

	Unaudited 6 months to 30 Jun 22 £000	Unaudited 6 months to 30 Jun 21 £000	Audited 12 months to 31 Dec 21 £000
Net cash flows generated from operating activities	1,422	2,936	19,712
Net cash flows (used in) investing activities	(5)	-	(2)
Net cash flows (used in) / from financing activities	(6,306)	1	(10,293)
Net (decrease) / increase in cash and cash equivalents	(4,889)	2,937	9,417
Net (decrease) / increase in cash and cash equivalents	(4,889)	2,937	9,417
Cash and cash equivalents at the start of the period	48,293	38,876	38,876
Cash and cash equivalents at the end of the period	43,404	41,813	48,293

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of preparation and significant accounting policies

1.1 Basis of preparation

The half yearly financial information for the 6 months ended 30 June 2022 has been prepared in accordance with both the Financial Conduct Authority's Disclosure and Transparency Rules and IAS 34 *Interim Financial Reporting*, as adopted by the EU. This financial information should be read in conjunction with the 2021 Annual Report and Accounts.

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

The financial information for the 12 months to 31 December 2021 has been extracted from the 2021 Annual Report and Accounts, prepared in accordance with IFRS as adopted in the EU. In relation to these accounts, the opinion of the Independent Auditors was unqualified.

The half yearly financial information for the 6 months ended 30 June 2022 and the 6 months ended 30 June 2021 are unaudited.

1.2 Basis of preparation: going concern

The Group's interim financial statements for the 6 months to 30 June 2022 have been prepared on a going concern basis as explained below.

The Group has not been active in the Mortgage market since 2013 and there is currently no plan in place to return to lending. The current strategy of the Board, therefore, continues to be the management of a long-term run-off of the balance sheet. No change in strategy has been agreed as a result of the improvement of the capital position following the Supreme Court's judgment in the Society's legal case with Grant Thornton, though the Board keep this under review and is working with advisers and the regulators to establish what the Supreme Court judgment will mean for the Manchester's ongoing strategy. Preliminary conversations are taking place with Newcastle Building Society regarding a potential merger of the two societies and the Society continues to work closely with its advisers and the regulators on this strategic option.

The Group continues to follow a medium to long-term strategic plan, against which it is monitored by the PRA. The plan shows that the Society remains viable in the medium-term and the Society has significant headroom against this plan. Although largely mitigated by the profits generated in 2021, it is recognised that there are long-term risks to this plan, particularly following a stress event in the economy or financial markets. Such stress events may include a downturn in the housing market either in the UK or Spain, additional provision requirements on some of the Group's larger mortgage exposures, or a materially different mortgage repayment profile to that included within the plan.

The stresses that have been considered by the directors when assessing the Group's ability to continue as a going concern recognise the economic uncertainty caused by the Covid-19 pandemic, Brexit and increased levels of inflation.

When satisfying themselves that the Group and Society have adequate resources to continue to operate for the foreseeable future as a going concern, the directors have reviewed the latest forecasts and the ability for the plan to be followed. Having due regard to these matters, the Board continues to adopt the going concern basis of accounting in preparing the financial statements.

The Board considers the preparation of the financial statements as a going concern to be a critical accounting judgment.

1.3 Basis of preparation: accounting policies

The half yearly financial information has been prepared consistently with the accounting policies described on pages 26 to 29 of the 2021 Annual Report and Accounts.

The Group expects that the accounting policies that will be applied at the time of compiling the 2022 Annual Report and Accounts will be materially the same as for the 2021 Annual Report and Accounts.

2. Fair values of financial assets and liabilities

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

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

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

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

The fair value measurement basis used is as follows:

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

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

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

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

	30 June 2022		30 June 2021		31 December 2021	
	Carrying Value	Fair Value	Carrying Value	Fair Value	Carrying Value	Fair Value
	£000	£000	£000	£000	£000	£000
Financial assets						
Cash and balances with the Bank of England	31,817	31,817	32,679	32,679	37,704	37,704
Loans and advances to credit institutions	11,605	11,605	9,134	9,134	10,589	10,589
Loans and advances to customers	142,240	133,534	166,381	157,751	153,300	145,618
Other assets	1,314	1,314	21,885	21,885	324	324
	186,976	178,270	230,079	221,449	201,917	194,235
Financial liabilities						
Due to members	138,832	138,759	166,270	166,308	150,254	150,248
Other deposits	6,549	6,549	7,588	7,588	7,036	7,036
Subordinated liabilities	-	-	14,200	14,200	5,000	5,000
Subscribed capital	5,000	5,044	5,000	4,282	5,000	5,238
Other liabilities	774	774	1,601	1,601	1,195	1,195
	151,155	151,126	194,659	193,979	168,485	168,717

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

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

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

3. Segmental information

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

4. Liquid assets

	Unaudited 30 Jun 22 £000	Unaudited 30 Jun 21 £000	Audited 31 Dec 21 £000
Cash and balances with the Bank of England	31,817	32,679	37,704
Loans and advances to credit institutions	11,605	9,134	10,589
	43,422	41,813	48,293

5. Loans and advances to customers

	Unaudited 30 Jun 22 £000	Unaudited 30 Jun 21 £000	Audited 31 Dec 21 £000
Gross Balances			
Fully secured on residential property	152,271	174,693	162,680
Fully secured on land	13,225	14,922	13,675
Other loans	135	219	200
	165,631	189,834	176,555
Provisions			
Fully secured on residential property	21,586	21,709	21,471
Fully secured on land	1,803	1,742	1,784
Other loans	2	2	0
	23,391	23,453	23,255
Net Balances			
Fully secured on residential property	130,685	152,984	141,209
Fully secured on land	11,422	13,180	11,891
Other loans	133	217	200
	142,240	166,381	153,300

6. Impairment losses

	Unaudited 30 Jun 22 £000	Unaudited 30 Jun 21 £000	Audited 31 Dec 21 £000
Expected credit losses			
Impairment (gains) / losses on loans and advances to customers on residential property and land	(80)	(102)	(146)
Amounts recovered on loans and advances to customers on residential property and land, written off in prior periods	(1)	(4)	(5)
Total expected credit losses	**(81)**	**(106)**	**(151)**
Other impairment losses			
Impairment losses on loans and advances to customers on lifetime mortgages	838	218	1,440
Total other impairment losses	**838**	**218**	**1,440**
Total impairment losses	**757**	**112**	**1,289**

Expected Credit losses relate to the Group's UK mortgage portfolios. The calculation methodology remains unchanged from that disclosed on pages 34 to 36 of the 2021 Annual Report and Accounts. The release in the 6 months to June 2022 is driven by a more optimistic economic outlook with downside scenario HPI assumptions, in particular, less pessimistic than the equivalent outlook in December 2021. The key assumptions used in calculating the provisions are:

	Unaudited 30-Jun-22				**Unaudited 30-Jun-21**				**Audited 31-Dec-21**			
Scenario weighting	30%	39%	30%	1%	30%	39%	30%	1%	30%	39%	30%	1%
Assumptions (5 year average)	**Upturn**	**Base**	**Mild Downturn**	**Severe Downturn**	**Upturn**	**Base**	**Mild Downturn**	**Severe Downturn**	**Upturn**	**Base**	**Mild Downturn**	**Severe Downturn**
House price index	2.6%	1.4%	(2.1%)	(6.1%)	5.2%	2.7%	(2.2%)	(8.7%)	4.0%	1.4%	(3.2%)	(9.4%)
Consumer price index	2.2%	1.8%	1.2%	0.6%	2.1%	1.9%	1.4%	0.8%	2.3%	2.0%	1.5%	1.0%
Uk Unemployment rat	3.7%	3.8%	6.1%	6.8%	3.9%	4.3%	6.2%	7.0%	3.6%	3.9%	6.0%	6.6%
LIBOR (3 month)	2.5%	2.1%	1.6%	0.7%	1.2%	0.3%	(0.0%)	(0.4%)	1.6%	0.9%	0.3%	(0.2%)
Bank base rate	2.1%	1.7%	1.2%	0.2%	1.1%	0.3%	(0.1%)	(0.6%)	1.5%	0.8%	0.3%	(0.4%)

Other impairment losses relate to the Group's Spanish lifetime portfolio. The charge of £0.8m constitutes a £0.5m charge for provision movements and a £0.3m charge related to exchange rate movements. The June 2021 charge of £0.2m constitutes a charge of £0.7m for provision movements and a £0.5m release relating to exchange rate movements. In both periods, the exchange rate movements included within impairment losses were largely offset by exchange rate movements included within Other Operating Income.

7. Non-current assets classified as held for sale

	Unaudited 30 Jun 22 £000	Unaudited 30 Jun 21 £000	Audited 31 Dec 21 £000
Non-current assets classified as held for sale			
Properties under Society control, previously used as collateral for loans fully secured on residential property	447	-	491
	447	-	491
Net loss on non-current assets classified as held for sale			
Net loss from fair value movements on properties under Society control, previously used as collateral for loans fully secured on residential property	-	-	194
	-	-	194

During 2021, two properties over which the Group had obtained full ownership rights that previously acted as collateral for two Spanish lifetime mortgage contracts were reclassified from loans and advances to customers to non-current assets classified as held for sale.

These properties were available for immediate sale and management had assessed that a sale within 12 months was highly probable. One property was sold during the first half of 2022, with the one remaining property continuing to be actively marketed for sale at a sales price judged to be reasonable in relation to the property's fair value. The asset is held at the lower of its carrying amount and fair value less costs to sell.

8. Deferred tax assets

Deferred taxes are calculated on all temporary differences under the liability method using an effectively tax rate of 19.00%. There were no movements on the deferred tax account in the period. The carrying value of the deferred tax asset ("DTA") is £nil.

DTAs are recognised for tax loss carry-forwards to the extent that the realisation of the related tax benefits through future taxable profits is probable.

The main rate of corporation tax is 19% and is due to remain at this rate at least until 31 March 2023.

The Group's long-term financial projections, based on a managed run-off of the balance sheet without a return to lending, indicate that the net interest margin will be insufficient to cover operating costs and loan impairment charges, resulting in operating losses.

It should be noted that the DTA de-recognised in prior years is still available for tax relief purposes, as tax losses can be carried forward indefinitely under UK tax rules and can be used subject to the availability of future taxable profits. Deferred tax assets have not been recognised.

At 30 June 2022 for the Group, these were:
- £1,587k arising from timing differences on derivative contracts (December 2021: £1,691k)
- £4,534k arising from losses (December 2021: £4,844k)
- £74k arising from accelerated tax depreciation and short-term temporarily deferred (December 2021: £81k)

9. Deposits from banks and others

	Unaudited 30 Jun 22 £000	Unaudited 30 Jun 21 £000	Audited 31 Dec 21 £000
Other deposits	6,549	7,588	7,036
Total	6,549	7,588	7,036

10. Income tax

	Unaudited 30 Jun 22 £000	Unaudited 30 Jun 21 £000	Audited 31 Dec 21 £000
Profit for period before tax	2,021	22,009	20,837
Tax rate	19.00%	19.00%	19.00%
Expected tax expense	384	4,182	3,959
Fair value movement on assets held for sale	-	-	37
Decrease in deferred tax asset recognised	-	-	(177)
Fixed asset timing difference for which no deferred tax asset recognised	(85)	(85)	-
Profits of period covered by brought forward losses in respect of which no deferred tax asset recognised	(299)	(2,534)	(2,352)
Actual tax expense	-	1,563	1,467

11. Subordinated liabilities

	Unaudited 30 Jun 22 £000	Unaudited 30 Jun 21 £000	Audited 31 Dec 21 £000
Loan (repay 2022) interest: 3 month LIBOR + 1.75%	-	5,000	-
Loan (repay 2023) interest: 3 month LIBOR + 2.45%	-	4,200	-
Loan (repay 2032) interest: 6.70%	-	5,000	5,000
Total	-	14,200	5,000

12. Subscribed capital

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

Classified as a liability:

	Unaudited 30 Jun 22 £000	Unaudited 30 Jun 21 £000	Audited 31 Dec 21 £000
8.00% Permanent Interest Bearing Shares	5,000	5,000	5,000
Total	5,000	5,000	5,000

Classified as equity:

	Unaudited 30 Jun 22 £000	Unaudited 30 Jun 21 £000	Audited 31 Dec 21 £000
6.75% Permanent Interest Bearing Shares	9,788	9,788	9,788
Total	9,788	9,788	9,788

13. Profit Participating Deferred Shares

	Unaudited 30 Jun 22 £000	Unaudited 30 Jun 21 £000	Audited 31 Dec 21 £000
Nominal value - proceeds received	18,000	18,000	18,000
Less: issue costs	(539)	(539)	(539)
Total	17,461	17,461	17,461

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

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

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

14. Capital

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

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

	Unaudited 30 Jun 22 Total Group £000	Unaudited 30 Jun 21 Total Group £000	Audited 31 Dec 21 Total Group £000
Tier 1 Capital			
Common Equity Tier 1 Capital (CET1)			
Accumulated Profits (after applying IFRS 9 transitional arrangements)	8,150	9,105	8,229
Profit Participating Deferred Shares	17,461	17,461	17,461
Total CET1 Capital	25,611	26,566	25,690
Other Tier 1 Capital			
Permanent Interest Bearing Shares			
-Nominal balance	14,788	14,788	14,788
-Amortisation	(14,788)	(13,309)	(13,309)
Net Permanent Interest Bearing Shares	-	1,479	1,479
Total Tier 1 Capital	25,611	28,045	27,169
Tier 2 Capital			
Subordinated Debt			
-Nominal balance	-	14,200	5,000
-Amortisation	-	(11,746)	(4,500)
Net Subordinated Debt	-	2,454	500
Permanent Interest Bearing Shares	14,788	13,309	13,309
Total Tier 2 Capital	14,788	15,763	13,809
Total Regulatory Capital	40,399	43,808	40,978

Since the start of 2022 Total Regulatory Capital has decreased by £579k from £40,978k to £40,399k.

The decrease results from the following:

- a reduction of £75k regarding the transitional rules covering the implementation of IFRS 9;
- a reduction of £4k relating to difference in amortisation period of intangible fixed assets in accounting policy and regulatory capital treatment;
- redemption of all outstanding subordinated debt, of which £500k was unamortised at 31 December 2021.

Following the profit generated in 2021, the Group now meets all of the quantitative and qualitative requirements regarding the level of regulatory capital it must hold. PIBS coupon payments were made on both issuances of PIBS in April 2022. These payments resumed in October 2021 following a period when the Group was not permitted to make such payments.

A review of the strategic direction to be taken by the Group following the Supreme Court judgment is being undertaken by the Directors alongside its regulators and advisers. Whilst the Capital position has improved to a level that all capital requirements are now satisfied, the Society remains at risk that a stress event or other significant loss could result in a future breach.

15. Related party transactions

The Group is controlled by Manchester Building Society and at 30 June 2022 consisted of the Society and its wholly owned subsidiary, MBS (Mortgages) Ltd. The Society continued to provide loan funding to its subsidiary during the half year ended 30 June 2022 in a manner similar to that disclosed in the 2021 Annual Report and Accounts. Accordingly, transactions with this related party are entered into in the normal course of business; related party transactions, for the half year to 30 June 2022, are similar in nature to those for the year ended 31 December 2021.

The Officers as at 30 June 2022 remain unaltered from those disclosed at 31 December 2021 on page 66 of the 2021 Annual Report and Accounts.

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

16. Financial commitments

There is no material change to the Group's financial commitments from the position reported in the 2021 Annual Report and Accounts.

17. Contingent liabilities and assets

(i) Contingent liabilities

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

As detailed in the Regulatory risk section on pages 7 and 8, provision has previously been made where the Group is aware of a specific conduct issue and can estimate its impact reliably. No such provision is deemed necessary at 30 June 2022.

As disclosed on page 64 of the 2021 Annual Report and Accounts there is a risk that other aspects of the Group's business might be considered as not having been conducted in accordance with all relevant regulation, or the fair and reasonable treatment of customers. It is also not possible to rule out the possibility of other instances of non-compliance with CCA or other regulations which have not been identified. No provisions against these risks are included in these accounts.

(ii) Contingent assets

Both the 2021 half year financial statements and Annual Report and Accounts included contingent assets in relation to costs and interest receivable resulting from the Supreme Court's judgment in the Society's legal case against its former auditors. Further payments totalling £2.4m were received in the period. These constituted a final settlement and no contingent assets remain at 30 June 2022.

18. Events after the end of the reporting period

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

19. Other Ratios

	Unaudited 6 months to 30 Jun 22 %	Unaudited 6 months to 30 Jun 21 %	Audited 12 months to 31 Dec 21 %
Gross capital as a percentage of shares and borrowings	28.9	32.1	28.8
Liquid funds as a percentage of shares and borrowings	29.9	24.1	30.7
Profit after tax as a percentage of mean total assets *(expressed on an annualised basis)*	2.1	17.5	9.1
Group management expenses as a percentage of mean total assets, including legal costs recovered *(expressed on an annualised basis)*	1.3	2.0	(1.3)
Group management expenses as a percentage of mean total assets, excluding legal costs recovered *(expressed on an annualised basis)*	2.5	2.0	2.3
Leverage ratio	11.8	10.9	11.8

The definitions for the above ratios are explained in detail on page 65 of the 2021 Annual Report and Accounts.