United Kingdom

The new platform will provide numerous benefits to TSB and its customers.

Highlights

- TSB achieved the goals announced in September and is gearing up for a new era.
- Improvements in customer acquisition processes and an increase in the number of managers.

Business overview

TSB has a multi-channel distribution model nationwide, comprising 550 branches in England, Wales and Scotland. At the end of the year, it had 5 million customers and 8,353 employees. The TSB franchise (TSB Banking Group PLC), conducts a high-street banking business in the UK which includes current and savings accounts, personal loans, mortgages and credit/debit cards.
Its business was previously divided in three segments:
- The franchise: comprising the multichannel banking business.
- Mortgage enhancement: a set of mortgages assigned to TSB in 2014 in the context of the restructuring of Lloyds Banking Group.
- The Whistletree portfolio: a set of loans, primarily mortgages, acquired from Cerberus in 2015.

Following the early return of the mortgage enhancement portfolio to Lloyds Banking Group in June 2017, TSB has operated as a single business within the franchise segment, including the *Whistletree* loan portfolio.

Management priorities in 2018

TSB, a unique and credible proposition to swiftly increase competitiveness in the SME business.

In April 2018, TSB completed its phased migration to a new IT platform (G2). The new platform covers all customer systems and channels, as well as all back office systems, and is critical to TSB's long-term ability to deliver for customers.

When TSB was initially established, it used the platform of Lloyds Banking Group (LBG), one of its competitors, operating on legacy banking systems. This meant that making changes to TSB's products and services was slow, and the cost, timing, design and pace of executing changes were set by a competitor. In June 2015, the acquisition of TSB provided the opportunity to leverage Sabadell's experience with migrating the Bank to a new system, which would enable TSB to provide better products and services more suited to its customers' needs.

Whilst the migration of all customer records took place as planned, customers experienced problems in the initial period after migration in accessing their accounts online, with long wait times on the phone and slower transaction times in branches.

The immediate priority in the period following the migration was to resolve the service issues impacting customers, and move swiftly to identify and fix the causes of these issues. Internal analysis indicated that the design of the platform itself was sound, and that most of the issues were attributable to deployment onto the technical infrastructure. The underlying problems were linked mainly to three key areas: the initial configuration, the infrastructure capacity and some aspects of the code.

The TSB Board also commissioned an independent review, from Slaughter and May, a firm of UK lawyers, to understand why these problems occurred, and the FCA and PRA conducted their own joint investigation.

At the beginning of September, the TSB Board announced that Paul Pester was stepping down from his position as Chief Executive and leaving the Company. TSB set three immediate priorities and very significant progress has been, at a good pace.

— Incident resolution process: at 30 January 2019, circa 181,000 complaints from customers since migration have been resolved, i.e. around 90% of the 204,000 complaints, ensuring that no customer is left out of pocket. New complaints now being received are significantly lower in volume, closer to pre-migration levels, with the majority no longer connected to migration issues.

— Full functionality for customers: all critical and urgent IT incidents have been resolved and the most significant customer-facing issues have been dealt with. Although occasional IT issues and interruptions occur, the number of these incidents has been reduced significantly since the immediate post-migration period and IT services are now stable and in line with industry performance.

  Customers have started to see the benefits of the new IT system, with a single platform and faster processing times for some of our services. As a result, in December TSB received the largest number of mortgage applications of any week in its history.

  Towards the end of 2018, customers also started to benefit from an increased number of products available through online channels for the first time since migration. Online current account sales have now returned to levels consistent with the most recent comparable pre-migration period and calls from customers needing help with their online applications are down 90% due to the significantly improved application process. Customers can also open a current account in branches in almost half the time compared with before migration.

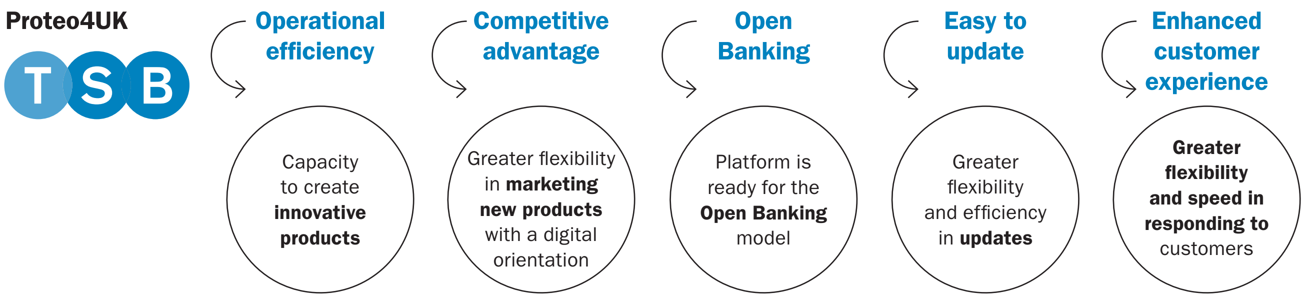
— New CEO for TSB: in November, it was announced that Debbie Crosbie would join the TSB Board as CEO, subject to regulatory approval. Debbie joins from CYBG PLC, bringing over two decades of experience in retail and SME banking, and an open and engaging leadership style. Debbie brings a clear innovative mindset to TSB and shares the vision of making banking better for all UK customers. She will join TSB in the Spring.

TSB remains one of the most strongly capitalised banks in the UK and, with an ample liquidity reserve, is well positioned both to weather economic uncertainty and shocks but also to deploy its financial reserves in further growth. While TSB remains confident in the relative strength of the UK economy, it is mindful of the challenges ahead, as economic and market conditions remain uncertain for a range of reasons, including Brexit.

Whilst the migration to the new platform caused considerable frustration and difficulties, looking forward, TSB remains confident that the platform is now delivering real benefits to customers and, importantly, also enables TSB to support more local businesses right across the UK.

TSB ushers in a new era.

G2 Benefits of the new platform



Key business data

Net income in December 2018 amounted to -€240 million, due mainly to the -€460 million in additional migration and post-migration expenses (T4).

Net interest income totalled €1,000 million, down 3.3% year-on-year due to the commercial drives at TSB following the IT migration.

Net fees and commissions fell 10.9% in year-on-year terms due mainly to lower services fees and to customer management actions at TSB following the IT migration. Income from financial transactions includes the results of fixed-income sales.

Administrative expenses and depreciation and amortisation charges increased by 14.6% year-on-year to -€1,148 million, including -€195 million in non-recurrent migration and post-migration expenses.

Provisions and impairments came to -€231 million, including a provision of -€142.1 million for total estimated compensation to customers, including extraordinary expenses for handling complaints linked to migration.

Net loans and advances to customers (excl. repos) amounted to €33,929 million, down 4.4% year-on-year. A constant exchange rates, the reduction on the previous year would have been 2.7% .

Customer funds on the balance sheet fell by 5.6% y/y to €32,484 million (down 4.7% at constant exchange rates). In 2018, they fell mainly because the maturity of time deposits (FRISA), while demand deposits (PCA) increased.

Financial performance was significantly affected by the IT migration, with costs incurred in preparing for migration and charges and waived income associated with the post-migration service disruption, partially offset by a provisional recovery of losses from Sabis under the MSA and OSA contracts.

Net interest income declined, due mainly to the impact on overdraft interest of the post-migration service disruption and the absence of earnings in 2018 from the Mortgage Enhancement portfolio. The decrease in net interest income in 2018 broadly reflects competitive pressures and interest waivers.

In 2018, the cost of customer deposits remained stable and included interest costs on savings that held steady in year-on-year terms, along with an increase in interest costs on bank accounts, following the rise in rates applicable to Classic Plus account balances.

Other revenues increased significantly, driven by the recognition of revenues from LBG as a result of exiting the outsourced services agreement upon migration to the new IT platform.

Payments deriving from service disruptions during migration including compensation to customers and additional operating costs: customer rectification costs, reimbursements and associated expenses, additional funding costs, consultancy costs to support the TSB reparations programme and anti-fraud and operating expenses.

Impairments decreased, reflecting an improvement in UK unemployment, a revised outlook for house prices relative to 2017 and a downward revision to unsecured recovery valuations.

TSB's capital position remained strong, with a Common Equity Tier 1 (CET1) ratio of 19.5% and a leverage ratio of 4.4% on a fully-loaded basis.

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T4 Key figures — UK business

	2017	2018	% 18/17
Net interest income	**1,034**	**1,000**	**(3.3)**
Equity-accounted affiliates and dividends	—	—	—
Fees and commissions (net)	96	85	(10.9)
Net income from financial transactions, and exchange differences	110	18	(83.8)
Other operating income/expense	(16)	(60)	283.2
Gross income	**1,223**	**1,042**	**(14.8)**
Administrative expenses and depreciation and amortisation	(1,002)	(1,148)	14.6
Operating profit/(loss)	**221**	**(106)**	**(147.8)**
Provisions and impairments	(89)	(231)	—
Gain/(loss) on derecognition of assets, etc.	7	1	—
Profit/(loss) before tax	**139**	**(335)**	**(341.5)**
Income tax	(49)	95	(295.2)
Profit/(loss) after tax	**90**	**(240)**	**(366.5)**
Non-controlling interest	—	—	—
Net attributable profit	**90**	**(240)**	**(366.5)**
Ratios (%)			
ROE (profit / average shareholders' equity)	5.8%	—	—
Cost: income (general administrative expenses / gross income)	79.5%	101.6%	—
NPL ratio (%)	0.4%	1.3%	—
Stage 3 exposure coverage ratio (%)	55.9%	50.4%	—
Assets	**48,145**	**46,182**	**(4.1)**
Loans and advances to customers (net), excluding repos	35,501	33,929	(4.4)
Liabilities	**46,597**	**44,596**	**(4.3)**
On-balance sheet customer funds	34,410	32,484	(5.6)
Wholesale funding in the capital markets	1,920	1,688	(12.1)
Assigned capital	**1,548**	**1,586**	**—**
Off-balance sheet customer funds	**—**	**—**	**—**
Other indicators			
Employees	8,287	8,353	0.8
Branches	551	550	(0.2)

The exchange rate applied for 2018 was GBP 0.8873 for the balance sheet and GBP 0.8945 (year average) for the income statement.
The exchange rate applied for 2017 was GBP 0.887 for the balance sheet and GBP 0.875 (year average) for the income statement.