The Co-operative Bank p.l.c.

11 November 2016

Q3 2016 Trading Update

Core Bank franchise

- Total Core Bank net customer loans remained stable at £15.4bn as at 30 September 2016 (£15.4bn at 30 June 2016) as an increase in mortgage balances was offset by reduced unsecured balances.
- Mortgage origination continued to improve with completions for the nine months to 30 September 2016 totalling £2.2bn (£1.8bn for the nine months to 30 September 2015) and redemptions (excluding contractual repayments) falling to £1.3bn during the same period (£1.8bn for the nine months to 30 September 2015). The pipeline also remains strong.
- New business asset spreads remained under pressure due to strong competition in the mortgage market.
- The Core Bank recorded an operating profit for the nine months to 30 September 2016, driven by the reduction in the FSCS levy and the gain from the sale of gilts, compared with an operating loss in the same period in 2015. The Core Bank recorded a small operating loss in Q3 2016.
- In the third quarter, current accounts increased to 1,433k accounts, of which 656k were prime accounts (1,422k and 646k respectively at 30 June 2016), as the £150 current account switching offer made the Bank's offering more competitive. Current account balances also increased during the same period.
- The Bank's current account Net Promoter Score was 24 at the end of the third quarter (26 at the end of the first half of 2016). The Bank is still ranked #3 vs peers which further emphasises the consistently strong service levels being delivered in contact centres and branches alongside continued improvement in digital channels.
- An upgraded mobile app was released in September 2016 and Apple Pay was launched in October 2016.

Cost reduction programme

- Total Bank operating costs for the nine months to 30 September 2016 were 10% lower than the same period last year and 3% lower quarter on quarter.
- The 5 additional branch closures announced in August will be completed by the end of November, reducing the network to 105 branches.
- The Bank continues to focus on cost challenges given the lower for longer interest rate environment.

Projects

- The Bank's migration of the majority of its mainframe-based core banking systems has been rescheduled from mid-November to Q1 2017 to allow the remediation of the results of system testing. This delay will lead to additional programme costs. The migration of some non-customer facing systems remains on schedule to take place before end-2016. The Bank expects to have substantially completed the Enterprise Services Outsourcing (ESO) programme by end-Q1 2017.
- The Bank continues to work with Capita to seek to agree a way forward for the transformation element of the mortgage outsourcing contract. The existing outsourcing of mortgage processing by Capita both for new and existing Bank customers continues to operate in a satisfactory manner.
- There remains risk to the costs of the project portfolio in 2016. The Bank has further reprioritised the rest of the project portfolio and the focus will be on projects that are essential for regulatory reasons and on those which will provide greatest value to the Bank.

Progress addressing legacy issues

- The deleveraging of the Non-core portfolio remains on track. We continue to evaluate the options available for future deleverage activity in order to facilitate further de-risking of the Bank.
- Redress for Payment Protection Insurance (PPI) for the first nine months of 2016 was marginally below forecast with lower valid complaint volumes and lower average redress. No further provisions were taken for PPI in Q3. The volume of future complaints remains the key uncertainty and, in particular, the

Bank awaits the FCA's final decision on the proposed time bar and associated consumer communications campaign.

- The Consumer Credit Act (CCA) redress and remediation programme was 98% complete at 30 September 2016 and is expected to complete by the end of the year. No further provisions were taken for CCA in Q3. Solutions to address accounts becoming non-compliant have commenced and will be completed in H1 2017.
- Mortgage remediation activities have been substantially progressed and the programme was 95% complete at 30 September 2016. The remaining work largely reflects redress and remediation in respect of auto capitalised arrears payments. In addition, the Bank continues to assess the potential conduct issues arising out of historic mortgage systems configurations.
- The Bank continues to work through a remediation plan relating to its IRB models and remains in close and continuous dialogue with the PRA in this respect.
- Discussions continue with the Co-operative Group and the Pension Trustee regarding the separation of the PACE pension scheme. The draft triennial valuation is expected to be available in Q1 2017.

Regulatory and capital update

- The Bank’s Common Equity Tier 1 (CET1) ratio stood at 12.6% at 30 September 2016 (13.4% at 30 June 2016).
- Total Bank RWAs reduced to £7.1bn at 30 September 2016 from £7.2bn at 30 June 2016.
- As noted previously, under the PRA rulebook, not meeting the Combined Buffer prevents the Bank from paying variable remuneration during the period of non-compliance. At the half year, to accommodate this, the Bank changed its remuneration structure for the majority of employees. Arrangements for more senior staff are close to being finalised.
- The PRA has notified the Bank of its new Individual Capital Guidance (ICG), which became effective as of 1 November 2016. As at 30 September 2016, the Bank’s new Pillar 2A was equivalent to 14.1% of RWAs.
- The Bank has reviewed the terms and conditions for the Term Funding Scheme (TFS) and, although the Bank believes it would be eligible access to the scheme, it would not be on commercially beneficial terms. As a result, the Bank has not currently made a formal application to access TFS. The Bank continues to maintain adequate liquidity in excess of the regulatory minimum and has only limited wholesale funding maturities in the next 18 months.
- The Bank of England‘s approach to setting a minimum requirement for own funds and eligible liabilities (MREL) was published on 8 November 2016. The Bank’s previous guidance on MREL remains unchanged at this time.

Niall Booker, Chief Executive Officer, said:

"We continue to make progress with our turnaround plan in a challenging economic environment, maintaining our focus on costs and the delivery of initiatives that are key to building a more resilient and sustainable bank. The performance of the Core Bank demonstrates the strength of our franchise, differentiated by our ethical brand and the quality service that we know is important to our customers. Our Everyday Rewards current account proposition, supported by renewed brand marketing, has led to a net increase in prime current accounts, and our new improved digital banking service and app, as well as the introduction of Apple Pay, have been rolled out for the benefit of our current account customers. Mortgage originations remain strong.

"Delivering some elements of the turnaround plan will become more challenging given that interest rates are now likely to be lower for longer and given the uncertainty surrounding the impact of the UK's decision to leave the European Union.

"A major achievement has been a successfully executed succession plan covering the three key roles of Chief Executive Officer, Chief Financial Officer and Chief Risk Officer. We have secured strong candidates in each of these roles and I wish Liam and his team all the best as they build on the work and achievements so far. There is still much work to do but the Bank is undoubtedly in much better shape than it was in mid-2013."

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Forward looking statements

This document contains certain forward-looking statements with respect to certain of the Bank's strategy, plans and its current goals and expectations relating to its future financial condition and operating performance. The Bank cautions readers that no forward-looking statement is a guarantee of future performance and that actual results could differ materially from those contained in the forward-looking statements. These forward-looking statements can be identified by the fact that they do not relate only to historical or current facts. Forward-looking statements sometimes use words such as 'may', 'will', 'seek', 'continue', 'aim', 'anticipate', 'target', 'projected', 'expect', 'estimate', 'intend', 'plan', 'goal', 'believe', 'achieve', 'predict', 'should' or in each case, their negative or other variations or comparable terminology, or by discussion of strategy, plans, objectives, goals, future events or intentions. These forward-looking statements include all matters that are not historical facts. Examples of forward-looking statements include, among others, statements regarding the Bank's future financial position, income growth, assets, impairment charges, business strategy, capital ratios, leverage, payment of dividends, the industry in which the Bank operates, projected costs, commitments in connection with the 2016-2020 Updated Plan, estimates of capital expenditures and plans and objectives for future operations and other statements that are not historical fact.

By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend on circumstances that may or may not occur in the future, for example, macroeconomic and business conditions, the effects of continued volatility in credit markets, market related risks such as changes in interest rates and foreign exchange rates, effects of changes in valuation of credit market exposures, changes in values of issued notes, the policies and actions of governmental and regulatory authorities (including requirements regarding capital and group structures and the potential for one or more countries exiting the Eurozone), changes in legislation, the further development of standards and interpretations under IFRS and prudential interpretation and application of standards under IFRS, the outcome of current and future legal competition, a number of such factors being beyond the Bank's control. As a result, the Bank's actual future results may differ materially from the plans, goals and expectations set forth in the Bank's forward-looking statements. Forward-looking statements are not guarantees of future performance. In addition, even if the Bank's results of operations, financial condition, and the development of the financial services industry are consistent with the forward-looking statements in this document, those results or developments may not be indicative of results or developments in subsequent periods.

Any forward-looking statements made in this document speak only as of the date they are made except as required by the FCA, the PRA, the LSE or applicable law. The Bank expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in the Bank's expectations with regard thereto or any change in events, conditions or circumstances on which such statement is based. The reader should, however, consult any additional disclosures that the Bank has made or may make in documents it has published or may publish via the Regulatory News Service of the LSE.

Note: all figures contained in this trading update are unaudited.