



Helping our customers at the moments that matter most



**About this report**

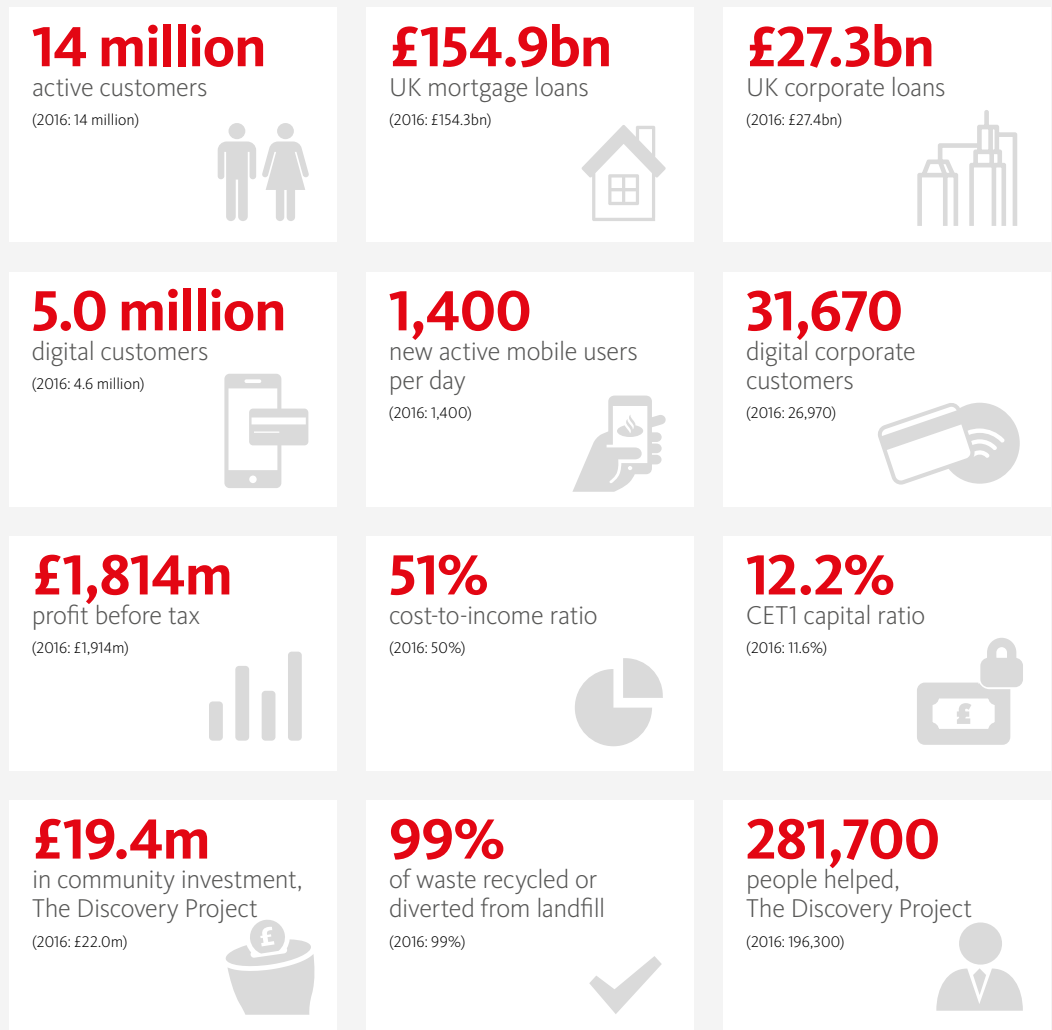
The Strategic Report outlines the key elements of the Santander UK Group Holdings plc 2017 Annual Report (2017 Annual Report). We produce it to help readers more easily assess our performance and future prospects. It also explains Santander UK today and our place in the UK banking market.

We are committed to high ethical standards in how we deal with all our stakeholders as well as our environmental responsibility. As such, the sustainability of our business is not separated from our strategic direction and we have included key information from our sustainability reporting in our Strategic Report.

By order of the Board.

**Nathan Bostock**  
Chief Executive Officer  
27 February 2018

Highlights 2017



For more information see [aboutsantander.co.uk](http://aboutsantander.co.uk)



**Important information for readers**

Santander UK Group Holdings plc and its subsidiaries (collectively Santander UK or the Santander UK group) operate primarily in the UK, and are part of Banco Santander (comprising Banco Santander SA and its subsidiaries). Santander UK plc is regulated by the UK Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) and certain other companies within the Santander UK group are regulated by the FCA.

This Strategic Report contains forward-looking statements that involve inherent risks and uncertainties. Actual results may differ materially from those contained in such forward-looking statements. See Forward-looking statements on page 259 of the 2017 Annual Report.

Santander UK Group Holdings plc (the Company) is the immediate parent company of Santander UK plc. The Company and Santander UK plc operate on the basis of a unified business strategy and have common Boards, albeit the principal business activities of the Santander UK group are currently carried on by Santander UK plc and its subsidiaries (the Santander UK plc group). The Company has adopted Santander UK plc's Corporate Governance and Risk Frameworks to ensure consistency of application. However, the Frameworks are applied from the level of Santander UK plc across the Santander UK plc group. As a result, the review of the business and principal risks and uncertainties facing the Company, and the description of the Company's Corporate Governance, including the activities of the Board and risk management arrangements, are integrated with those of Santander UK plc and are reported in this document as operating within the Company.

# Santander UK

We help our customers at the moments that matter most. We champion British businesses and help them to grow sustainably. Our customer focus helps us to develop more loyal and lasting relationships.

## What factors are affecting the banking market?

Read more on page 8



## How do we manage risk effectively?

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## Chair's statement



Santander UK delivered a strong business performance in 2017, meeting our business objectives, despite significant headwinds in the external environment.

### Strong business growth and management performance

Santander UK delivered strong business momentum in 2017, meeting our business objectives, despite significant uncertainty in the external environment. We achieved this while maintaining prudent risk management and balance sheet resilience.

I would like to thank Nathan Bostock, our CEO, the management team and all our people who have together delivered this performance. Impressively, they have at the same time continued to make good progress in the transformation of our culture, capabilities and systems critical for building a bank that is fit for the future.

### Digital transformation and cyber security

We have continued to put significant focus on our digital capability in all parts of our business and processes. Our digital transformation remains a priority, and is crucial to delivering the banking service our customers rightly expect. In 2017, we gained an average of 1,400 new mobile app users every day and reached an important landmark in providing our first end-to-end digital mortgage. Santander UK now has 1.9 million digital-only customers.

As technological progress continues, a more digital world also brings new challenges. The financial sector is experiencing ever increasing and complex risks from cyber attacks which potentially threaten our customers' data security and privacy as well as our own systems. As more of our customers interact with us online and we prepare for the positive changes that Open Banking will bring, we are

also working to combat fraud and constantly update our fraud detection capabilities. Together with large parts of the sector, we have responded to these challenges by working collaboratively with each other and closely with law enforcement and Government authorities through initiatives such as the Joint Fraud Taskforce and organisations like the National Cyber Security Centre. These efforts serve as a good example of how the public and private sector can work effectively together in the national interest. At Santander UK we are taking all reasonable steps to stay well-prepared to meet developing cyber threats, supported by global expertise from the Santander Group.

### Challenging the Big Four incumbent banks

Santander UK is uniquely placed as the leading full-service scale challenger bank in the UK. We are a challenger in every part of the banking market – apart from mortgages, a legacy from our building society heritage – and current accounts where our innovative and customer-focused 1|2|3 World offering, launched in 2012, allowed us to disrupt the dominance of the Big Four banks and change incumbent behaviour. At the same time, we have a wide geographic footprint in the UK and strong brand recognition. In addition, with long-term support from our shareholder, Banco Santander SA, we have been able to leverage the strength of the Banco Santander group to pioneer innovation and build global trade corridors and alliances to support our internationally trading SMEs. But we retain the mentality and mind set to be innovative, agile and driven to challenge the Big Four banks which is essential to improve the experience of all UK customers.

“ Santander UK is uniquely placed as the leading full-service scale challenger bank in the UK.”

The development of our commercial banking business is testament to what we have achieved as a challenger. We have been awarded *Business Moneyfacts* 'Best Business Bank' for the third year in a row. By investing in our people and operations, and relentlessly maintaining a customer-focused culture, Santander UK has grown its market share in SME banking from an almost standing start in 2009.

We are committed to continuing to innovate and to challenge the incumbent banks, providing a better and more customer-focused service for UK households and businesses. However, it is clear that the incumbency of the Big Four banks in the SME and corporate banking segments will only change to achieve a well-functioning market for these businesses through structural changes that remove barriers for credible scale challengers like Santander UK. The RBS Alternative Remedies represent an important opportunity for challengers like Santander UK to provide real competition in UK banking.

### Embedding the right culture

We have further strengthened the connection between culture, conduct and customer outcomes by establishing the Board Responsible Banking Committee. The purpose of this committee is to assist the Board in shaping the culture, reputation and customer propositions of Santander UK through overseeing and advising management on conduct, people, community, brand and compliance issues.

We launched a leadership programme to help our senior managers embed and role model more effectively the nine behaviours that our people identified in 2015 as underpinning the culture and values of Simple, Personal and Fair that we aspire to. We have also further evolved performance management measures for all our employees so that they are evaluated against both **how** they deliver their objectives as well as **what** they deliver. I am pleased that our five employee-led diversity and support networks have had 5,000 new members join in 2017, helping to build further a diverse and inclusive culture across the bank.

### Supporting our customers through the UK's withdrawal from the EU

Uncertainty about the UK's future relationship with the EU has contributed to a more cautious outlook for the economy in 2018 and 2019 relative to other major economies. This uncertainty is particularly felt by our SME customers who trade internationally and are in the supply chains of larger multinational corporations.

As Santander UK is primarily a retail and commercial bank with the overwhelming majority of our assets and of our liabilities in the UK, our business model will not be directly affected by the UK's withdrawal from the EU and we are well placed to support our customers through this changing environment. With our European shareholder we also have more options to support our corporate clients and to offer innovative business solutions for SMEs, such as our unique trade proposition for businesses importing and exporting all over the world.

### Managing the pace and volume of regulatory change

A critical part of the challenge in the external environment facing banks is the unprecedented volume of regulatory initiatives that need to be implemented simultaneously. While we continue to strongly support the substance of these changes, and a robust supervisory environment, the pace and flow of regulatory changes could potentially add to operational risks and affect customer experience. This is compounded where implementation deadlines, for example for MiFID2, GDPR, Open Banking and ring-fencing, have fallen in very close succession and coinciding with adjusting to a new relationship between the UK and the EU. We are cognisant of the need to do this while also continuing to change culture and invest to provide the service that customers in the UK expect.

“ We are on track to deliver the necessary changes required under the Banking Reform Act in advance of the legislative deadline of January 2019.”

We are on track to deliver the necessary changes required under the Banking Reform Act in advance of the legislative deadline of January 2019. All of our retail customers and an overwhelming majority of our corporate customers will not experience any change as they will remain within a 'wide' ring-fenced bank. We will continue to serve the more complex needs of our largest corporate customers through the London branch of Banco Santander SA. Subject to final regulatory approval, we do not anticipate any structural changes to our overall governance model.

### A strong and effective Board

With our ring-fencing model confirmed, we have made a number of new appointments to the Board. Antonio Roman, Chief Financial Officer, and Javier San Felix, Deputy CEO and Head of Retail Banking, joined the Board as Executive Directors on 1 August 2017. We were also pleased to announce two Non-Executive Directors nominated by Banco Santander SA to the Board in December. Gerry Byrne, Chairman of Banco Santander SA's Polish subsidiary Bank Zachodni WBK, joined the Board on 1 December 2017 and Lindsey Argalas, Banco Santander SA's new Chief Digital and Innovation Officer joined on 1 January 2018. We are very pleased to be able to draw on this wealth of international banking and technology expertise for the Board.

During 2017, three Non-Executive Directors nominated by Banco Santander SA stepped down from the Board: Peter Jackson following his departure as an executive of Banco Santander SA, Bruce Carnegie-Brown, Vice Chairman of Banco Santander SA, and Manuel Soto after 14 years of service on the Banco Santander SA Board and 4 years with us. We are very grateful for the commitment and expertise they brought to Board deliberations and I would like to thank them all for their invaluable contribution.

## Simple | Personal | Fair

Our culture is built on doing things The Santander Way

### Simple

We offer our customers products that are easy to understand and a service which is convenient, no matter when or how they want to engage with us. We make our processes better so they are easy and clear for our customers and our people.

### Personal

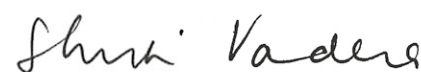
We treat our customers as valued individuals, providing a professional service they can trust. We support our colleagues to develop their skills and achieve their ambitions.

### Fair

We are open, honest and treat others as we would like to be treated. We earn our investors a sustainable return and do our part to support our communities.

I am pleased that this year we have reached our target early of one third of Board Directors being women. We will continue to strive to improve gender balance on the Board and across the business.

As we look forward to 2018, Santander UK is well placed to meet its challenge of continuing to improve the service we provide to our customers and to meet our ambition to be the best bank for our people, customers, shareholder and communities.



### Shriti Vadera

Chair  
27 February 2018

## Santander UK at a glance

We are a large customer-focused bank, and the UK's leading full-service scale challenger.

We are the only UK bank with the scale and breadth of proposition to challenge the big four UK banks. With our omni-channel approach we serve our customers through digital channels, in particular mobile, alongside a network of branches and Corporate Business Centres supported by telephone call centres.

We play an important role in the UK economy and in the communities in which we operate. We help people finance their home, save for the future and support business growth. We employ around 20,000 people and we paid £484m of corporation tax in 2017.

**3<sup>rd</sup> largest mortgage provider<sup>(1)</sup>**

**4<sup>th</sup> largest current account provider<sup>(2)</sup>**

**5<sup>th</sup> largest commercial lender<sup>(1)</sup>**

We are a straightforward bank that creates value by serving our customers with financial products and services. Most of our 14 million customers are individuals but we also serve a growing number of small, medium and large UK companies.

Most of what we do can be described as lending money to borrowers, taking deposits from savers, providing bank accounts and payment services. We also offer a wide range of investment and insurance products to households and other more specialised services and products to companies.

We are here to help our customers prosper and by doing so we create and protect sustainable value for all our stakeholders.

(1) Santander UK analysis. Mortgage provider rank based on bank annual reports. Commercial lender rank based on loans to SME and mid corporate clients by UK retail and commercial banks and building societies.

(2) CACI's CSDB Current Account Stock, Volume, December 2017.

We provide high quality, seamless service across an optimised branch network, digital and telephony channels

We use market leading tools to help our customers monitor, understand and manage their finances

**14 million**  
active UK customers



**NeoCRM**

Our customer relationship management tool allows us to more effectively engage with, and better serve, our customers by bringing together information from across different channels. We call this our omni-channel approach.

Read more in the panel on the **opposite page**.

**806**  
branches<sup>(3)</sup>



**Santander Investment Hub**

Our online service provides our c220,000 registered customers with access to more than 1,300 investment funds.

**64**  
Corporate Business Centres



**Santander Working Capital Loans**

Our online product helps our SME customers manage cash flow quickly and efficiently, so they can concentrate on running and growing their business.

**£200.3bn**  
customer loans



**Online mortgage application**

Our online mortgage application allows both new and existing customers to find a new deal with us, and to quickly and easily apply online.

**£175.9bn**  
customer deposits



(3) Branch coverage: c80% of UK financial centres. Branches include 61 university branches



## Successful roll out of NeoCRM, our customer relationship management tool

NeoCRM is a key enabler of our ambition to deliver a seamless omni-channel approach. This approach allows our customers to engage with us in the branch, on the telephone or via digital channels and to pick up the conversation where they left off, through a different channel if they choose. NeoCRM allows our people to easily view customer contact records from all channels so can they provide a more meaningful and relevant service.

During 2017 we completed the roll out of NeoCRM to our branch and contact centre people, as well as to our Santander Business Managers. This means that we now have 14,000 colleagues using NeoCRM. Colleagues from across the business collaborate to develop, improve and enhance NeoCRM on an ongoing basis. Feedback from our customer-facing people has been a key driver of innovations.

We do things  
The Santander Way:  
Simple, Personal, Fair

We manage our business  
through three customer  
business segments, supported  
by the Corporate Centre

We have a consistent  
strategy which underpins  
our business

### Our customers are at the heart of everything we do

We believe a motivated and engaged workforce provides the best customer service and embedding the right culture and behaviours is crucial to this. The nine behaviours that our people defined to embody our values are now established as a part of how we measure performance and determine reward for our people and the management team.

Read more on [page 7](#)

### We have a culture of personal responsibility

Each of us does our part to:

- Identify risks and opportunities
- Assess their probability and impact
- Manage the risks and suggest alternatives
- Report, challenge, review, learn and 'speak up'



**IDENTIFY**  
**ASSESS**  
**MANAGE**  
**REPORT**

Read more on [page 14](#)

### Retail Banking

Residential mortgage loans, savings, investments, current accounts, credit cards, personal loans and insurance for individuals and small businesses with an annual turnover of up to £6.5m.

### Commercial Banking

Products and services including loans, bank accounts, deposits, treasury services, trade and asset finance for SME and corporate customers with annual turnover above £6.5m.

### Global Corporate Banking

Tailored services and solutions for corporate clients with annual turnover above £500m and financial institutions.

### Corporate Centre

Management of capital, funding, balance sheet and strategic liquidity risk. Small non-core portfolio including aviation, shipping, infrastructure and commercial mortgages and some of our social housing loans.

### Customers

Grow customer loyalty and market share.

Deliver operational and digital excellence.



Read more on [page 22](#)

### Shareholders

Achieve consistent, growing profitability and a strong balance sheet.



Read more on [page 23](#)

### People

Live The Santander Way through our behaviours.



Read more on [page 24](#)

### Communities

Support communities through skills, knowledge and innovation.



Read more on [page 25](#)

## CEO Review



We have achieved much as a business in 2017 and are proud to have helped our customers at the moments that mattered most to them.

Q

A

### Q. What have been the highlights of 2017?

**A.** Santander UK is performing well. We have delivered on our promises to our shareholders, reporting a solid 2017 performance against the backdrop of an uncertain external environment. I am confident we will deliver on all our targets for shareholders, people and communities. Indeed on returns, we have revised our 2018 target on return on tangible equity upwards, from 8-10% to 9-10%.

I'm really pleased with the progress we are making across the business. In particular, we have continued to help our customers at the moments that matter most, delivering an excellent service and products that make a real difference to their lives and businesses. Although we will continue to grow, we will not reach our loyal retail customers target. Low interest rates for savings products resulted in consolidation of savings into our 11213 Current Account, and therefore impacted loyal customer conversion.

We have continued to make a positive impact on the communities in which we operate

through our Corporate Social Responsibility and University programmes. We are playing our part to help those who are vulnerable and in need, and giving a boost to those in education and at the start of their careers, to gain the essential skills for future success.

### Q. What are the main issues that the banking sector faces?

**A.** We have been very busy preparing for a number of important regulatory changes. Over the coming years, Open Banking will have a bearing on customer interaction and the nature of our competitors while also offering new opportunities for challengers like us. And given new ring-fencing rules come into force in January 2019 we needed to complete a significant amount of preparatory work in 2017, and into 2018.

The UK banking sector remains very competitive, resulting in falling lending margins – notably, some best buy rates in the market for unsecured lending were on par with secured mortgage lending rates in 2017. We don't feel that is sensible and understand the PRA's review of consumer credit lending prompted by the ongoing strong growth of this market. Also, we and the UK banking sector will continue to face credit events in the course of regular business.

Perhaps the biggest challenge we face is the uncertainty of the UK's future relationship with the EU. Although our business is focused on UK individuals and businesses, this uncertainty is a major concern for our customers and the wider economy.

We made some adjustments to our proposition in 2017, given the potential uncertainty ahead and tight margins in certain areas. We therefore

decided to restrict lending growth in consumer, and commercial real estate sectors.

In 2017, the UK economy followed similar trends to 2016 and there is an expectation that we'll see similar trends in 2018. The market consensus includes a wide range of key economic indicator projections though, and this adds a degree of caution to our outlook.

### Q. What opportunities do you see?

**A.** Our strategy enables us to realise opportunities and equips us for different eventualities. This is supported by proven innovation, customer-centric technology and our position in a global banking group.

We have scale in key areas, such as mortgages and current accounts. Nonetheless, we feel we can offer a real alternative to the larger banks in areas such as business banking and commercial banking, and this is where we are building our proposition.

### Q. Your purpose is to help customers prosper – what does that mean to you?

**A.** Prosperity can mean many things, it's not just about money. We want to help people to buy homes, manage their financial needs and to grow and protect their businesses. To do that our focus is to build more loyal relationships, providing innovative products with a deeper more personalised service.

This is not easy to do and we have invested heavily to ensure we can deliver the service our customers want across all channels. Importantly, we want them to be able to move seamlessly between channels – they could start a transaction online, phone us with a query and complete it in branch. We also see a real potential to apply this approach to our small



and medium sized business customers. By helping these customers to grow their business we are helping to fuel the UK economy.

**Q. How are you leveraging technology?**

**A.** I am excited by the opportunities that new technology offers us and optimistic about our future. The world is moving at a fast pace and we will move with it. We can already see today how technology can help us to develop new ways of engaging with our customers and make our back office more efficient. We have ambitious plans to continue to improve our service to our customers.

Importantly, I think we can learn from financial technology (FinTech) companies – how to be more agile and how we can create innovative, technology-driven banking services. That could be through better processes, greater use of technology, getting better at the basics or just by working together in a more collaborative way. By working with disruptive FinTech companies we think we can deploy new technologies to be a bank that doesn't just meet but anticipates customer needs.

**Q. How are you helping UK companies to grow?**

**A.** There are over five million SMEs in the UK so they are an incredibly important part of the economy. We are trying to differentiate ourselves around a number of distinct approaches. Our Breakthrough programme has a variety of features – as an example we link up with Santander Universities to fund internships into SMEs and run workshops at branches for smaller businesses. Through this scheme, we've supported over 2,200 internships, with over half the participants going on to secure further employment.

We continue to help larger corporates with their more specialist needs. We featured highly in the UK infrastructure league tables with funding for more than 25 infrastructure and energy projects in the UK in 2017. We also saw increased client demand for our Debt Capital Markets services, with €170bn of bond issuance managed.

As companies grow, the opportunity to go further, to move into markets overseas and then expand even further is something we are well-placed to help with. We are introducing a number of trade corridors to enable cross-border client relationships and transactional services. Importantly, by working with the wider Banco Santander group we are facilitating introductions to support trade and offer our customers new business opportunities.

**Q. How important is it for Santander UK to be active in the community?**

**A.** It's essential that each of us play our part in helping the wider community. We strongly encourage all our people to utilise and expand their skillsets, whilst investing in charitable, education and employability programmes. These benefit the community, which includes our future workforce and customers, but is also very much a part of building a motivated and engaged workforce.

I am proud that in 2017, our efforts benefitted over 281,000 people in our communities through The Discovery Project, our flagship community investment initiative. Our employees also raised over £1m for our Charity Partners, Age UK and Barnardo's.

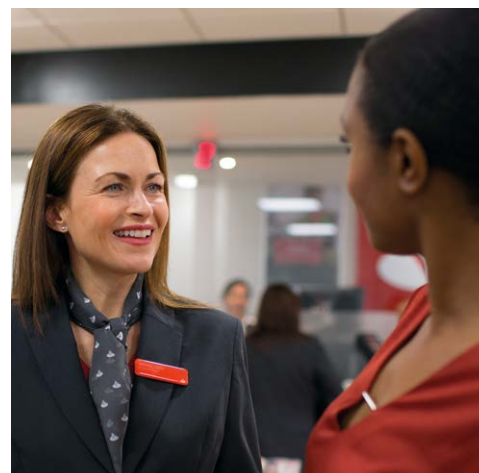
**Q. How are you changing the culture at Santander UK?**

**A.** I want Santander UK to be a bank which is Simple Personal and Fair, and two years ago I launched the Santander Behaviours to reinforce these values. Today they continue to underpin everything we do and are integral in our interactions with colleagues, customers, communities and shareholders. Every day I meet colleagues who inspire me. They show passion, they embrace change, give support and actively collaborate. They also keep their promises and aren't afraid to speak up to make things better for all stakeholders.

I am incredibly grateful for the hard work of all our people who are making our bank a true partner for our customers and our communities. A bank that our customers trust to do the right thing, a bank that people want to work for, which values its employees and where diversity is championed and speaking up encouraged. I truly believe that we can be the best bank in the UK, a bank that we can all be proud of.



**Nathan Bostock**  
Chief Executive Officer  
27 February 2018



**Our Santander Behaviours**  
Living The Santander Way

The Santander Behaviours describe how we should interact day-to-day with our colleagues, customers, shareholders and communities to bring Simple, Personal and Fair to life.



**I Bring Passion** and energy and give my best



**I Talk Straight** and think about the impact of my words



**I Embrace Change** and look for better ways to do things



**I Show Respect** including through the little things



**I Speak Up** and challenge where necessary



**I Keep Promises** and make decisions



**I Give Support** to colleagues by taking a genuine interest in them and appreciating their contribution



**I Truly Listen** for different and new opinions and am open to challenge



**I Actively Collaborate** with others to get the best outcome for the customer

## Market overview

We see five major forces affecting the UK banking market.

### Changing customer behaviour

Customer expectations and behaviours are evolving as new technologies are more widely adopted and the UK's demographic profile changes

#### The opportunity and challenge

Millennials are taking an increasingly important position in society. The UK population is ageing and this is impacting traditional customer segments and creating diverging needs. The adoption of new technology offers many benefits to customers but there is a risk that it can't fully satisfy some customers' needs.

#### What we've seen so far

Changing customer profiles and behaviour have significantly disrupted the banking sector. In a digital age, customers demand frictionless access to products and services and banks are re-evaluating their service and operating models. As a result, branch numbers across the UK are in decline.

#### Our response

We understand that our customers have different needs and serve them through the most suitable channel for them. For our retail customers this can be through branch, telephone or digital. For our small business customers we have a network of Corporate Business Centres across the UK.

We have introduced a new relationship management tool to support our omni-channel approach to allow seamless customer conversations across different channels. We have also invested in technology like our Investment Hub to help our customers manage their money flexibly for the longer term.

### Rapid technological change

Technology is at the core of changes to the way we interact with customers. It offers improved ease of access and faster service – driving a move to digital channels

#### The opportunity and challenge

The pace of technological development is increasing rapidly. This opens up opportunities for banks to re-evaluate how they engage with their customers. At the same time, it is important to maintain cyber security and resilience to protect both our customers and our operations.

#### What we've seen so far

Many customers have embraced digital platforms as part of their day-to-day banking and indeed for many this is now the norm. However, there is still a significant number of customers who prefer a traditional banking service. For banks, technology represents an important opportunity to streamline back-office processes.

#### Our response

By utilising innovative solutions allied with our customer-centric approach, we aim to deliver excellent customer experience through digitalisation and simpler, more agile processes.

We are looking to adopt new ways of working to bring applications to market with greater speed, integrating enabling technologies to accelerate the digital transformation.

Our ongoing collaboration with FinTech companies through open IT architecture will allow us to bring greater personalisation to our services, anticipating our customers' needs, and providing a frictionless experience.

### Strong market competition

The UK banking market remains highly competitive, with pressure on margins and an ongoing focus on sustainable customer relationships

#### The opportunity and challenge

The long-standing structure of the UK banking market is becoming increasingly fragmented. Large banks are competing strongly while facing threats from smaller challengers and technology-led new entrants. These trends are likely to continue with the introduction of Open Banking which aims to drive competition and innovation in UK retail banking.

#### What we've seen so far

The UK government Term Funding Scheme (TFS) has helped to keep the cost of lending low in 2017 while contributing to reduced competition for deposit acquisition. Demand for new mortgages has been below long-term averages and together with lower rates for typical fixed mortgage products led to a highly competitive environment. Competitive pressures in corporate and commercial banking have also remained high.

#### Our response

As the leading full-service scale challenger we are well-positioned to succeed in a competitive market.

During 2017, we continued to closely manage new mortgage lending. We adjusted our appetite accordingly when we felt the risk return trade-off was particularly low. Similarly we have controlled growth in commercial real estate lending and consumer credit through our prudent underwriting criteria and our proactive risk management policies.

## 1.9 million

Exclusive mobile app users

## 194 million

Digital customer transactions in 2017

## 25 bps reduction

Average 2 year fixed mortgage price in 2017

## Demanding regulatory change agenda

Regulation in the UK remains focused on encouraging greater competition, supporting positive customer outcomes, and making banks stronger

### The opportunity and challenge

The regulatory agenda continues to present both risks and opportunities for UK banks. As well as encouraging competition, new entrants and innovation, it also focuses on conduct towards customers and financial stability.

### What we've seen so far

Digital advances have opened up opportunities for both start-ups and established technology companies. This is set to continue with the launch of Open Banking which aims to increase the number of companies that can offer financial services and enable them to develop technology to manage customers' money.

We have also received confirmation of two important regulatory items: indicative MREL requirements and the final rules and guidance on Payment Protection Insurance (PPI) from the FCA.

### Our response

We expect our returns going forward will be impacted by increased regulatory compliance costs and the demanding banking regulation regime. However, we remain confident that we can continue to grow our business and plan to further develop loyal relationships with our personal and corporate customers by living up to our commitment to be Simple, Personal and Fair and behaving with high ethical standards.

>100

Regulatory initiatives

## Uncertain economic environment

Despite a relatively stable economy in 2017, the medium term outlook for the UK remains uncertain

### The opportunity and challenge

We see uncertainty ahead and with a wide range of projections for key economic indicators, such as GDP and house price growth, it's possible that outcome will be significantly different from the current consensus view.

### What we've seen so far

The UK economy experienced solid growth in 2017, with record low levels of unemployment. Despite the squeeze on real incomes from rising inflation and muted earnings growth, the Bank of England decided to raise Bank Rate for the first time since July 2007 based, in part, on this solid growth. Business investment has continued to be affected by the ongoing uncertainty in the UK economy, which has impacted corporate borrowing.

### Our response

We have a track record of consistent profitability, a resilient balance sheet and a relentless focus on customers. We believe that we are well-placed to manage any potential uncertainties and deliver our strategy.

In light of the uncertain outlook we continued to control growth in some higher margin business areas where we saw potentially higher risks. We believe that our proactive risk management policies will deliver a resilient performance in the business.

+0.5% to +2.6%

Range of HMT consensus for 2018 growth in annual GDP



## The UK's future relationship with the EU remains uncertain

The UK's uncertain future relationship with the EU is likely to impact the evolution of the macro economy and also adds complexity to the delivery of strategic development.

For the banking sector, much of the debate has centred on the position of the City of London and the potential impact of the loss of cross border access for financial services providers (often referred to as 'passporting'). Given our UK focus, we do not expect this will be a major issue for us. However, the impact on the wider economy and our customers in the medium term is unclear.

We have not yet seen any significant impact on our business although we do expect consumer spending to be affected by a squeeze on real earnings through increasing inflation.

UK businesses face ongoing uncertainty over future trade arrangements and how the transition to any new rules will be managed. This uncertainty has impacted business investment, although this is still forecasted to grow.

# Business model

**Our purpose** is to help people and businesses prosper.

**Our aim** is to be the best retail and commercial bank, earning the lasting loyalty of our stakeholders.

## Strategic priorities Business model



### Customers

Grow customer loyalty and market share

Deliver operational and digital excellence



### Shareholders

Achieve consistent, growing profitability and a strong balance sheet



### People

Live The Santander Way through our behaviours



### Communities

Support communities through skills, knowledge and innovation

### What we do

#### We provide financial products and services to individuals and businesses

- Mortgages, unsecured loans, credit cards and overdrafts
- Banking and savings accounts, investment and insurance products
- Specialised services and products to companies of all sizes

#### We generate sustainable profit

- Earn a margin on our products
- Charge fees for our services
- Efficiently manage the infrastructure of people, property and technology that support our business
- Provide for credit losses which may occur if things don't go as planned

#### We are building a resilient business

- Invest to ensure we have robust technology and systems
- Keep enough capital and liquidity to withstand times of stress

### How we do it

#### We use funding from diversified sources<sup>(1)</sup>

**£176bn**

UK retail and corporate deposits through current and savings accounts

**£63bn**

Wholesale funding through a range of debt programmes and market facilities

#### We maintain financial strength and resilience

- A predictable medium-low risk profile
- A track record of profitability
- Well capitalised

#### We have a straightforward ring-fence structure

- Majority of activities within the ring-fence after January 2019
- Single point of entry resolution entity
- Minimal disruption for most of our customers

(1) At 31 December 2017.

### We deliver great customer service

#### We aim for a seamless experience

across all channels, no matter how our customers choose to engage with us

#### We offer a differentiated proposition

with products and services tailored to be more meaningful and relevant to customer needs

### We manage risk effectively

#### We take a prudent approach to risk appetite

by making the right lending decisions and by mitigating the risks we face

#### We identify, assess, manage and report risks

that could impact our results, reputation or the sustainability of our business

### We do things The Santander Way: Simple, Personal and Fair

#### We take personal responsibility

for our actions

#### We have high ethical standards

in everything we do



## How we stand out

### We build strong customer relationships

- Driving new primary relationships with personal and corporate clients
- Leveraging a comprehensive product range

### We want to be the bank of choice for UK companies

- Helping UK companies as they expand into overseas markets
- Adapted to industry segments
- Relationship managers based near our clients businesses

### We benefit from being an important part of a well-diversified global bank

- Significant synergies and able to leverage group technology investment
- Shared management experience and stronger brand identity

### We improved customer experience

for retail and corporate customers, with further improvement at the heart of our plans

### We are the most resilient UK bank

with the lowest CET1 drawdown in the 2016 and 2017 PRA stress tests

### We live the Santander Behaviours

in our interaction with each other and our customers

## Value creation



### Customers

We help our customers prosper, by supporting our personal customers through all the stages of their lives and championing British businesses.

**24,000**

First-time home buyers helped in 2017

**>£500m**

Growth Capital Finance to SMEs since 2012



### Shareholders

We remain consistently profitable with a strong balance sheet.

**50%**

Annual dividend payout

**10 years**

Profitability and dividend paid every year



### People

We offer first-class professional development opportunities and competitive pay and benefits.

**£8.8m**

Employee training and development in 2017

**104,800 days**

Employee training in 2017



### Communities

Our people are active participants in a wide range of community volunteering and charitable activities and help to decide which we support.

**£19.4m**

Support for communities

**281,700**

People supported in 2017

See how we measure success  
**on page 12**

# Strategic review

The key to achieving our strategic goals is to embed our Simple, Personal and Fair culture.

| Key Performance Indicator <sup>(1)</sup>   |  | Why it is important  |
|--|--|--|
| <b>Customers</b><br>      | <b>Loyal retail customers</b><br>(million)                   | We believe that a loyal customer base, where a primary bank account acts as the anchor of the relationship, provides customer insight, improved risk profile and reduces customer turnover.                |
|  | <b>Loyal SME &amp; Corporate customers</b>                   | We believe that a primary banking relationship with our corporate customers allows us to increase returns through a relationship model while capitalising on our differentiated international proposition. |
|  | <b>Retail customer satisfaction<sup>(2)</sup></b><br>(FRS %) | We believe that a satisfied customer base is key to the long-term sustainability of our business and is at the heart of our plans to help people and business prosper.                                     |
|  | <b>Digital customers</b><br>(million)                        | We believe that promoting the use of digital and mobile technology builds on our track record for innovation, giving customers more choice and helping us to provide a better customer experience.         |
|  | <b>Fee income</b><br>(2015-2018, CAGR <sup>(3)</sup> %)      | We believe that growing fee income indicates that we are developing fair and transparent fee-based services as part of our drive for deeper relationships with customers.                                  |
| <b>Shareholders</b><br> | <b>Return on tangible equity<sup>(4)</sup></b><br>(%)        | We believe it is important to deliver returns above our cost of equity and return on tangible equity (RoTE) is a holistic measure of the sustainability of our business operations.                        |
|  | <b>Cost-to-income ratio</b><br>(%)                           | We believe that digital and operational innovation will help us to work more efficiently and allow us to make ongoing cost savings and balanced investment decisions.                                      |
|  | <b>CET1 capital ratio</b><br>(%)                             | We believe it is important to maintain sufficient capital above the minimum regulatory requirements and market expectations for the sustainability of our business operations.                             |
|  | <b>NPL ratio</b><br>(%)                                      | We monitor the NPL ratio as a holistic, well understood measure of credit risk, one of the most important risks we face.   |
|  | <b>Dividend payout ratio</b><br>(%)                          | We believe this ratio shows how we balance our need to organically grow our capital base with a fair return on the investment made by our parent.  |
| <b>People</b><br>       | <b>Colleague engagement<sup>(5)</sup></b><br>(%)             | We believe a highly motivated and engaged workforce provides the best customer service.  |
| <b>Communities</b><br>  | <b>People supported<sup>(6)</sup></b><br>(cumulative)        | We believe that supporting communities through skills, knowledge and innovation benefits the wider society in which we live and work, and helps us to build a better business.                             |

(1) See page 27 for KPI definitions.  
 (2) Customer satisfaction as measured by the Financial Research Survey (FRS) run by GfK.  
 (3) CAGR (Compound annual growth rate) is measured between 31 December 2015 and 31 December 2018.  
 (4) See page 27 for 'Return on ordinary shareholders' equity' which is the nearest IFRS measure.  
 (5) Colleague engagement is the percentage of colleagues that feel favourably engaged working for Santander UK. Survey conducted by Korn Ferry, October 2017.  
 (6) The target for people supported is cumulative from 2016 to 2018.

## How we are doing

**Loyal retail customers** increased in 2017 but growth was impacted by low interest rates for savings, which encouraged consolidation of deposits into more competitive products. While we continued to grow, we will not reach this target in 2018.

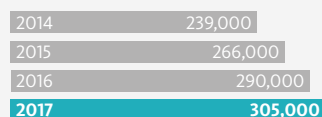
## Results



## 2018 target

**4.7 million**  
More to do

**Loyal SME and corporate customers** increased as we further improved our customer experience and business banking offering. We also developed our international proposition as we began to introduce UK trade corridors with Spain, Poland, Brazil and India to enable cross-border client referrals.



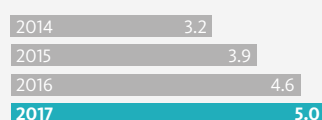
**308,000**  
On track

**Retail customer satisfaction** was broadly in line with the average of our three highest performing peers on a rolling 12-month basis at 31 December 2017. Ongoing improvement remains at the heart of our plans.



**Top 3**  
On track

**Digital customers** continued to grow, gaining an average of 1,400 new active mobile users per day, of which 1.9 million exclusively use our mobile app in their transactions with us. In 2017, 47% of mortgages were retained online and 38% of current account openings were made through digital channels.



**6.5 million**  
More to do

**Net fee and commission income** increased due to higher current account and wealth management fees in Retail Banking, and international, digital and payment fees in Commercial Banking.



**5% – 10%**  
On track

**RoTE** was impacted by higher impairment charges, primarily due to exposures on Carillion plc, and increased operating expenses, partially offset by steady income growth.



**9% – 10%**  
On track

**Cost-to-income** increased slightly in 2017 as higher income from retail liability margin improvement was more than offset by higher costs. The impact of higher regulatory, risk and compliance costs was partially offset by embedded cost savings.



**50% – 52%**  
On track

**CET1 capital ratio** improved as capital increased from retained profit and continued build of CET1 capital, alongside lower risk weighted assets.



**c12%**  
On track

**NPL ratio** improved, supported by our predictable medium-low risk profile, proactive management actions and the ongoing resilience of the UK economy.



**< 2.00%**  
On track

**Dividend payout ratio** of 50% was maintained and we declared £553m of ordinary dividends for the year, in line with our dividend policy.



**50%**  
On track

**Colleague engagement** was broadly stable and above the average of other UK financial sector companies. We have also made improvements in key areas such as leadership; Simple, Personal and Fair; processes and resources; respect and recognition.



**Top 3 UK Bank**  
On track

**People supported** through employee participation in a range of programmes designed to build skills, knowledge and experience, as well as encourage innovation.



**600,000 2016-18**  
On track

Note chart shows cumulative progress to target.

## Risk overview

Sound risk management is at the centre of our day-to-day activities. It benefits our business and our customers by helping to ensure balanced and responsible growth.

### Top risks

We regularly review the top risks that could impact our customers and shareholders. Risks actively monitored over 2017 include the following.

#### UK's future relationship with the EU

Article 50 was triggered in March 2017 and the UK's exit negotiations commenced with the EU in June. In May, political uncertainty increased following the General Election, and this has the potential to further complicate negotiations. We regularly update contingency plans we have in place for a range of possible economic political and regulatory scenarios.

#### Mitigating the impact of a low rate environment

In November 2017, the Bank of England increased the Base Rate to 50bps, reversing the 25bps cut made in August 2016, following the EU referendum in June 2016. The path of any future rate increases, according to the Bank of England is currently expected to be gradual, given uncertainties over future trading arrangements with the EU. However in comparison to 2016, the prospects for further rate increases in the future means this risk has reduced. We assess the potential impacts of future rate increases on our customers to help ensure their borrowing remains affordable.

#### Ring-fencing

We continue to execute our ring-fence plans, in order to meet the 1 January 2019 legislative deadline. The majority of customer assets and liabilities will remain within the ring-fenced bank, providing longer-term flexibility with minimal disruption for our customers. Santander UK plc and Abbey National Treasury Services plc (ANTS) have entered into an agreement with Banco Santander for the transfer of the corporate and wholesale markets business which is prohibited from inclusion in the ring-fenced bank. There are regulatory risks to our plans, which could be compounded by the final outcome of the EU exit negotiations. However, we maintain close communications with the relevant authorities and continue to refine our contingency plans to mitigate these risks as they evolve.

#### Building and maintaining capital strength

The CET1 capital ratio was 12.2% at 31 December 2017, above the current regulatory minimum. Steady profits growth increased the ratio combined with lower risk-weighted assets. The Bank of England stress test results showed that we exceeded the regulatory hurdle rate set by the PRA for our projected CET1 and UK leverage ratios.

Our plans for 2018 include a number of refinements to our regulatory capital models in response to supervisory recommendations and consultations. The Financial Policy Committee (FPC) announced an increase in the Countercyclical buffer from 0% to 1%. IFRS 9 was implemented from 1 January 2018, changing the way in which we recognise loan loss provisions, and has the potential to make regulatory stress testing results far more pro-cyclical than the current approach.

#### Pension scheme

Our pension risk profile has grown over the last few years, mainly driven by the deterioration of long-term gilt yields. During 2017, however, risk levels have fallen due to mitigating strategies employed during the year. The 2016 triennial valuation was completed in March 2017, and following this the CF Trustee began an extensive investment and hedging strategy review. As a consequence, the CF Trustee has implemented a number of actions, which have already reduced the risk profile of the scheme. We are also taking actions to improve risk management and control, along with the associated governance.

#### Financial Crime

Aligned with the evolving regulatory environment in the UK, our Financial Crime control framework continues to be upgraded. A centralised bank-wide programme with direct oversight and governance has been established, including review by the Board Responsible Banking Committee. Systems and controls have been enhanced to aid compliance with our legal and regulatory obligations.

#### Managing a complex change agenda

As part of our business planning strategy we have continued to invest in important risk mitigation projects in order to keep pace with changes in the regulatory environment and technological advances. We have established robust processes and controls that allow us to track any potential issues and mitigate any execution risk.

#### Cyber-attacks

In 2017 we have seen an increase in observed cyber-attacks against global institutions. We have continued our investment in our detection capabilities against malicious activity and building a Cyber Defence Centre, to protect both our customers and our shareholders. We also help our customers stay safe online with a range of internal and industry-wide initiatives.

#### Conduct risks

Conduct risk can result from activities that we engage in, that could lead to unfair outcomes for customers or negatively impact market stability. We have regular contact with the FCA with respect to industry reviews, competition studies and other requests. Our Compliance unit supports a wide range of regulatory deliverables, provides oversight across key operational areas, and undertakes additional assurance testing. We encourage all our people to take personal responsibility for managing risk through our I AM Risk programme.

#### Third Party Risks

We rely on a number of major suppliers, in order to continue to deliver products and services to our customers. The complexity and criticality of services provided by third-parties to the industry is a key operational risk that has been recognised by ourselves, our peers, and the regulators.

We place emphasis on a carefully controlled and managed Third Party Supplier Risk Framework, and are enhancing our resources in this area in order to manage this risk. This framework ensures that those with whom we intend to conduct business meet our risk and control standards throughout the life of our relationship with them. We monitor and manage our ongoing supplier relationships to ensure our standards and contracted service performance continue to be met.



## Emerging risks in 2017

We regularly review the emerging risks that could impact our customers and shareholders. Risks actively monitored over 2017 include the following.

### Changing customer behaviour

Customer expectations are shifting as population demographics evolve and the adoption of digital technologies drives changes in how people interact with their banking services provider. This has potential to provide disruption to the banking sector with higher demands for customer-centricity, accessibility, simplicity and automation. In response we are working to enhance digitalisation and to ensure that our bank is appropriately designed to meet the increased expectations of our customers.

### Rapid technological change

Technological change offers choice and convenience to our customers. It also supports our omni-channel approach, aids operational and cost efficiency and sustainable profitability. However it means that we need to continue to maintain appropriate levels of investment in organisational transformation. We also need to rapidly integrate new technologies and place a high priority on technology risk management, especially cyber security, in order to protect our customers and our reputation.

## I AM RISK – our Risk Culture



At Santander UK every one of us takes personal responsibility for managing risk by doing our part to:

- Identify risks and opportunities
- Assess their probability and impact
- Manage the risks and suggest alternatives
- Report, challenge, review, learn and 'speak up'.

### Strong market competition

The UK Banking market continues to be highly competitive. At present, our main competition comes from incumbent banks who have simplified their operations and refocused their activity. Areas of particular competitive focus include mortgages, a significant driver of profits in the UK retail banking industry, and costs, as a key strategic lever in protecting or improving financial returns. During 2017, we began preparing for the second Payment Services Directive (PSDII) and Open Banking as well as the additional competition these initiatives will bring to the market. In the longer term, there is also potential for new types of competitors, such as scale digital players, to gain market presence by leveraging their large customer bases and digital customer interfaces.

### Demanding regulatory agenda

We continue to face a complex regulatory change agenda, with key projects due for delivery across 2018 and 2019 including PSDII, Markets in Financial Instruments Directive (MiFID II) and General Data Protection Regulation (GDPR).

### Uncertain macro environment

The UK economy has performed better in 2017 than many initial expectations following the EU referendum. However, momentum has slowed relative to 2016 and forward looking growth forecasts have trended downwards throughout the year. Exit negotiations between the UK and the EU are complex and challenging, and as a result, uncertainty has been increasing with respect to the future trade and services relationship. This uncertainty is reflected in cautious levels of business investment and subdued confidence.

Arrears remain at historically low levels, with good credit quality being maintained across our lending portfolios, supported by our prudent approach to lending. Some normalisation from these cyclically low levels could arise over the medium term. In the Corporate credit market there are several signs, including narrowing profit margins, pointing towards the end of the current cycle following the continued expansion of credit in the last three years.

# 8bps

estimated transitional impact of IFRS 9 on CET1 ratio



## Minimal initial impact of IFRS 9 on the capital position

From 1 January 2018, IFRS 9 replaced IAS 39 standard which will change the way we raise loan loss provisions. This will also have an initial impact on capital reserves. The most fundamental change is to the measurement of impairment losses, which will follow expected credit losses (ECL) approach.

We have completed the implementation of the systems and processes needed to comply with IFRS 9. The estimated transitional impact on the CET1 capital ratio is a decrease of 8bps before any transitional arrangements, which are expected to reduce the amount recognised in 2018. As a result, the adoption of IFRS 9 is not expected to have material impact on our capital position.

Further details about our transition to IFRS 9 can be found in a separate document, 'Transition to IFRS 9' available on our website at: [santander.co.uk/uk/about-santander-uk/investor-relations/santander-uk-group-holdings-plc](http://santander.co.uk/uk/about-santander-uk/investor-relations/santander-uk-group-holdings-plc)

## Risk overview continued

### Risk types

All our activities involve identifying, assessing, managing and reporting risks. A top risk is a current risk within our business that could have a material impact on our financial results, reputation and the sustainability of our business model. Our current top risks are set out on page 14.

### Credit

1 3

#### What is credit risk

Credit risk is the risk of loss that could arise if our customers or counterparties default on their obligation. Defaults reduce the value of our assets, and increase our write-downs and allowances for impairment losses.

The main drivers of defaults and of increased credit risk include increased unemployment, falling house prices, increased corporate insolvency levels, reduced corporate profits, increased personal insolvency levels, increased interest rates and/or higher tenant defaults.

#### What have we seen so far

Our NPL ratio fell to 1.42% in 2017 (2016: 1.50%) while the cost of credit was 0.10% compared to the medium-term average of 0.20% to 0.30%. The benign credit environment has supported our customers and helped to reduce credit risk. In particular, unemployment, one of the most important factors in mortgage defaults, has been below 5% for two years. Whilst the UK market continues to show resilience, we are cautious on the outlook in light of recent increases in corporate profit warnings and economic uncertainty.

#### How do we mitigate the risk

We manage our exposures carefully to ensure we stay within our risk appetite and agreed concentration limits. We have thorough credit checking and approval processes to understand the risk we take on when we lend. We closely monitor the economy and where we see areas of stress we take action to reduce our exposure or to adapt our pricing to adequately reflect the risk.

#### NPL ratio (%)

|      |      |
|------|------|
| 2014 | 1.80 |
| 2015 | 1.54 |
| 2016 | 1.50 |
| 2017 | 1.42 |

### Market (Banking market)

3

#### What is banking market risk

Banking market risk is the risk of loss of income or economic value due to changes to interest rates in the banking book, or to changes in exchange rates.

Changes in interest rates are the largest driver of our exposure to banking market risk. This is because we are a significant mortgage provider and deposit taker focused on the UK. A large proportion of our interest income is based on an interest rate which is either contractually or effectively fixed.

#### What have we seen so far

The interest rate environment in the UK has been low and stable for a prolonged period. Bank rate rose for the first time in ten years in November 2017 from 0.25% to 0.50%. Market expectations are for future rate increases to be gradual in nature. Our balance sheet is positioned to benefit from a rising interest rate environment, although the pace and scale of expected change will moderate any impact on income.

#### How do we mitigate the risk

We use a variety of approaches to protect the bank from interest rate risk. These include using financial instruments or by matching fixed rate deposits with fixed rate loans of a similar term.

#### NIM sensitivity +50 bps (£m)

|      |     |
|------|-----|
| 2014 | 15  |
| 2015 | 131 |
| 2016 | 240 |
| 2017 | 212 |

### Capital

3

#### What is capital risk

Capital risk is the risk that we do not have an adequate amount or quality of capital to meet our internal business objectives, regulatory requirements, market expectations and dividend payments, including AT1 coupons.

Capital resources can be depleted by losses and requirements can be increased by changing regulations or by deterioration in the creditworthiness of our customers.

#### What have we seen so far

Regulatory capital requirements have increased significantly since the financial crisis as regulators have attempted to strengthen banks' balance sheets. Santander UK continued to generate capital from profits throughout the financial crisis and continued to pay dividends of 50% of recurring profit every year, in line with our policy.

#### How do we mitigate the risk

We utilise a capital risk framework that informs and monitors our capital risk appetite. Capital and leverage ratios are monitored to ensure we meet current and future regulatory requirements. We also undertake wide-ranging stress testing analyses to confirm our capital adequacy under various adverse scenarios.

#### Total capital ratio (%)

|      |      |
|------|------|
| 2014 | 17.3 |
| 2015 | 17.4 |
| 2016 | 17.3 |
| 2017 | 17.8 |

### Strategic priority key:

- 1 Grow customer loyalty and market share
- 2 Deliver operational and digital excellence
- 3 Achieve consistent, growing profitability and a strong balance sheet

## Pension

3

### What is pension risk

Pension risk is the risk of making additional contributions to our defined benefit pension schemes to meet our obligations as a sponsor. Additional contributions can be required when the funding position of the schemes is worse than planned. The key drivers of pension risk are primarily long-term interest rates and inflation which affect the value of the pension liabilities, as well as the risks of assets not delivering sufficient returns. Increases in pension risk can also increase our capital requirements.

### What have we seen so far

In recent years, UK pension funds have experienced headwinds as a result of falling long-term gilt yields driving an increase in the value of pension liabilities. In many cases these increases in liability values have only been partially offset by increases in the value of hedging assets and return-seeking assets. Where funding positions have deteriorated, additional contributions or extensions to funding plans may be required. Across 2017, the pension fund surplus, measured on an accounting basis, improved by £29m to £204m.

### How do we mitigate the risk

We monitor pension risk monthly against the overall risk appetite set by the Board. A range of investment strategies are used to generate income and capital growth to contribute to the cost of the scheme benefits. Hedging strategies are used to mitigate the impact of inflation and changing interest rates.

### Funded defined benefit pension scheme accounting surplus (£m)

|      |     |
|------|-----|
| 2014 | 156 |
| 2015 | 483 |
| 2016 | 175 |
| 2017 | 204 |

## Conduct

1 2 3

### What is conduct risk

Conduct risk is the risk that our decisions and behaviours lead to poor outcomes for our customers, and that we fail to maintain high standards of market behaviour and integrity. This could happen through product design, sales practices, post-sale servicing, complaint handling and the risk that our people do not conduct themselves in the manner we expect them to.

### What have we seen so far

In recent years, a significant conduct issue faced by banks relates to PPI, with significant provisions set aside by the industry for redress. Following confirmation by the FCA of the deadline for customer complaints relating to PPI, banks are now funding advertising campaigns to inform customers who may be eligible for redress.

As a result we made further provisions this year for PPI. We also made a provision relating to the sale of interest rate derivatives, following an ongoing review of certain customers potentially eligible for redress.

### How do we mitigate the risk

Our culture of Simple, Personal and Fair, underpinned by our nine behaviours, enables us to embed a conduct strategy within the business where we place the fair treatment of customers at the heart of what we do. We always look to improve our processes and training to ensure this, integrating fair treatment into our product and service design reviews.

### Remaining conduct provision (£m)

|      |     |
|------|-----|
| 2014 | 291 |
| 2015 | 637 |
| 2016 | 493 |
| 2017 | 403 |

## Operational

1 2 3

### What is operational risk

Operational risk is the risk of loss due to inadequate or failed internal processes and systems, or external events. It occurs where unexpected or unplanned events prevent us from achieving our business objectives. We consider our top three operational risks (excluding conduct) to be cyber security, third party supplier management, and process and change management.

### What have we seen so far

Cyber risk has become an increasingly prominent issue, with various well-known companies targeted with sophisticated cyber-attacks, including Distributed Denial of Service (DDoS) attacks, malware and phishing attacks.

### How do we mitigate the risk

To mitigate the three main operational risks we face, we utilise separate but complementary approaches. We operate a layered defence approach to cyber risk, focused on identifying, detecting, preventing, responding to and recovering from cyber-attacks, including simulation tests. We carefully select our suppliers and manage our ongoing relationships diligently. Before we engage in new activities, develop new products, enter unfamiliar markets or utilise new technology, we conduct operational risk assessments before we proceed.

## 9% decline

in total operational risk losses (excluding PPI) compared to previous 3 year average

## Financial crime

2 3

### What is financial crime risk

Financial crime risk is the risk that we or third parties facilitate money laundering that finances terrorism, bribery and corruption or evasion of financial sanctions. If we fail to meet our obligations to address these risks, it could impact our business negatively as well as affecting the safety and security of our customers and the communities we support.

### What have we seen so far

We have made a number of enhancements to our systems and controls in recent years. We enhanced our partnerships with public authorities and strengthened our reporting to senior management. This included implementing our Financial Crime Transformation Program, which has enhanced our risk assessment, screening and transaction monitoring.

### How do we mitigate the risk

We are committed to the strongest possible response to financial crime risks. We carry out risk assessments for customer, product, business, sector and geographic risk and also perform due diligence to understand our customers' activities and banking requirements. This targeted approach allows us to predict, detect, prevent and, where possible, disrupt financial crime.

## £54m

incremental investment in financial crime enhancements planned for 2018

## CFO review



I am pleased to report solid 2017 financial results with continued progress towards our strategic and operational goals.

### Solid business performance in 2017

We delivered solid and sustainable business performance in 2017, while progressing on our strategic and operational goals. Profit before tax was £1,814m, down 5% from £1,914m in 2016. Our 2017 financial results were impacted by a credit impairment charge for Carillion plc, which offset otherwise good profit growth.

Total operating income was up 2%, through retail liability margin improvement and good income momentum in Retail Banking and Global Corporate Banking. These were partially offset by continued pressure on new lending margins and Standard Variable Rate (SVR) mortgage attrition. Income also benefited from a gain of £48m following the sale of our shareholding in Vocalink Holdings Limited and £39m of accrued interest release on a foreign tax liability.

Operating expenses before impairment losses, provisions and charges were up 4%. Strategic investment, regulatory compliance costs and inflationary pressures outweighed the benefit of operational and digital efficiencies.

Total operating impairment losses, provisions and charges increased to £203m (2016: £67m). This was primarily due to the Carillion plc credit impairment charge, as well as PPI and other conduct provision charges of £109m and £35m respectively. Overall, the loan book continues to perform well with an improved NPL ratio of 1.42%, down 8bps.

Return on ordinary shareholders' equity of 8.9% was down (2016: 9.6%), while return on tangible equity was lower at 10.2% from 10.9%, impacted by higher impairments and higher costs.

### Controlled growth in customer balances

Customer loans of £200.3bn were broadly stable (2016: £200.2bn). Mortgage lending increased £0.6bn as we focused on retention and management pricing actions in a competitive environment. Corporate customer loans fell by £0.1bn due to active management of our commercial real estate (CRE) portfolio which decreased by £0.9bn, this was largely offset by strong growth in other areas of corporate lending.

Customer deposits increased £3.5bn to £175.9bn and the loan-to-deposit ratio improved to 113%. This growth was largely a result of higher retail current account balances, which were up £2.5bn. Corporate customer deposits also grew, increasing by £3.0bn in 2017. Growth in these areas was partially offset by outflows in Retail Banking savings products of £3.9bn.

### 2017 Performance highlights

# 1.90%

Banking NIM  
(2016: 1.79%)

# £1,814m

Profit before tax  
(2016: £1,914m)

# £27.3bn

Lending to UK companies  
(2016: £27.4bn)

# £67.3bn

Retail Banking current account balances  
(2016: £64.8bn)

# £6.2bn

MREL eligible senior unsecured debt issued  
(2016: £4.4bn)

# £87.0bn

Risk-weighted assets (RWAs)  
(2016: £87.6bn)



### Maintaining balance sheet strength

The Common Equity Tier 1 (CET1) capital ratio increased to 12.2% (2016: 11.6%). This reflected steady profit growth and lower risk weighted assets which fell by £0.6bn to £87.0bn. The UK leverage ratio improved 30bps to 4.4%.

Wholesale funding with a residual maturity of less than one year decreased to £14.9bn, mainly as the result of maturing medium-term funding. The liquidity coverage ratio (LCR) decreased 19 percentage points to 120%, reflecting the increased requirements due to EU adoption of Regulatory Technical Standards for assessing additional collateral outflows and efficient liquidity planning. The LCR eligible liquidity pool significantly exceeded wholesale funding of less than one year, with a 326% coverage ratio.

### Robust funding plan executed in 2017

Our overall requirement for medium-term funding issuance was lower in 2017 due to the availability of the Term Funding Scheme (TFS), which served as a replacement of some of our secured funding. TFS total outstanding was £8.5bn.

We also issued £7.3bn of medium-term funding, of which £2.1bn (sterling equivalent) was senior unsecured notes from our holding company, £1.2bn from our operating company, £2.3bn were covered bonds and £1.7bn were securitisations. We are well placed to meet minimum requirement for eligible liabilities, with £6.2bn of senior unsecured funding from our holding company issued to date.

### Conduct remediation

The final FCA rules and guidance for Payment Protection Insurance (PPI), including Plevin, set a deadline of 29 August 2019 for customer complaints to be registered. This was followed by an FCA advertising campaign to raise awareness.

As a result, we made additional provisions in 2017, amounting to net £109m. The remaining provision for PPI redress and related costs amounted to £356m. We continue to monitor our provision levels in respect of recent claims experience.

The remaining non-PPI related conduct provisions amounted to £47m, including a provision of £35m relating to the sale of interest rate derivatives. This charge followed an ongoing review regarding regulatory classification of certain customers potentially eligible for redress.

### 2018 outlook remains uncertain

We anticipate that the UK economy will continue to grow in 2018, although at a slightly subdued pace. Stronger global growth is likely, coming in particular from emerging markets. Nonetheless, for the UK economy, some downside risks could materialise, as a result of higher inflation and low wage growth reducing households' real earnings. This may restrict consumer spending which, when combined with a potentially more challenging macro environment, adds a degree of caution to our outlook.

We expect Banking NIM will be lower than in 2017, with continued competitive pressures on new asset margins as well as SVR attrition. Cost management remains a key area of focus, as we work to comply with the demanding regulatory agenda and inflationary pressures. We will continue to invest in strategic projects, including global group initiatives, which over time will further improve our customer experience and operational efficiency.

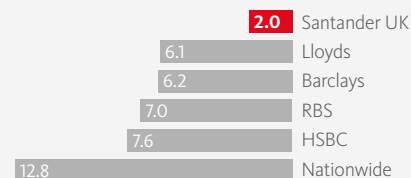
We anticipate gross mortgage lending growth in line with the market, with continued focus on customer service and retention while delivering operational and digital excellence. Our lending to UK companies is likely to grow in line with the market. Our lending growth to trading business customers will remain strong, partially offset by modest growth in CRE exposures. This will result in slower overall growth than in recent years.

We will continue to purposefully control growth in line with our proactive risk management policies and prudent approach to risk appetite. These actions will help deliver sustainable results while supporting our customers in an uncertain environment.



**Antonio Roman**  
Chief Financial Officer  
27 February 2018

### Bank of England 2017 stress tests CET1 drawdown (percentage points)



Source: Bank of England, Stress testing the UK banking system: 2017 results

### 2017 PRA stress test: Santander UK most resilient of UK banks

The latest PRA stress test results were released in November 2017.

With a stressed CET1 ratio of 9.7% after allowed management actions, we significantly exceeded the PRA threshold requirement of 7.6%. Additionally, with a stressed leverage ratio of 3.3% we exceeded the PRA threshold requirement of 3.25%.

As in 2016, we were the most resilient of the UK banks with the lowest drawdown of 2% on our CET1 ratio<sup>(1)</sup>.

The outcome of the stress test underlines the quality and strength of our UK-based balance sheet as well as our strong risk management practices.

(1) CET1 drawdown is defined as CET1 ratio at December 2017 less minimum stressed ratio (after the impact of 'strategic' management actions and conversion of AT1).

## Corporate Governance review

Strong governance is an essential component in delivering our purpose to help people and business prosper.

We make continuous progress in striving to be the best governed bank in the UK, improving both our effectiveness and efficiency.

### UK Group Framework

The UK Group Framework sets out the relationship between the Company and its shareholder, Banco Santander SA. This provides us with clarity about how we discharge our responsibilities in the UK as an independent Board, while ensuring that Banco Santander SA is able to exert the oversight and control of its subsidiary that its regulators expect.

The UK Group Framework was updated in 2017, principally to bring it in line with a newly codified appointments policy to be adopted across the Banco Santander group.

### Board composition and skills

Our current Board comprises 14 members with diverse and complementary experience spanning retail and corporate banking, financial markets, wealth management, technology, governance, financial reporting, economics, public policy and government. In line with our UK Group Framework, 50% including the Chair are Independent<sup>(1)</sup> Non-Executive Directors (INEDs) with the other 50% being a combination of Executive Directors (EDs) and Banco Santander nominated Non-Executive Directors (Group NEDs).

There have been a number of changes to Group NEDs and EDs during the year. In February 2017, Peter Jackson stepped down following his departure as an executive of Banco Santander SA. In June 2017, Bruce Carnegie-Brown, Vice Chairman of Banco Santander SA, stepped down following his appointment as Chairman of Lloyds of London. In December 2017, Manuel Soto also stepped down after a period of four years serving on the Board of Santander UK.

On 1 August 2017, Antonio Roman and Javier San Felix were appointed to the Board as EDs.

Antonio is Chief Financial Officer and Javier is Head of Retail & Business Banking and Deputy CEO. These appointments increased the number of EDs on the Board from one to three.

Gerry Byrne and Lindsey Argalas joined the Board as Group NEDs on respectively 1 December 2017 and 1 January 2018. Gerry is the Chairman of Bank Zachodni WBK SA, Banco Santander SA's Polish subsidiary, and brings with him a wealth of banking experience gained over 40 years. Lindsey is Banco Santander SA's Chief Digital and Innovation Officer, replacing Peter Jackson, and is responsible for developing digital strategy and supporting innovation throughout the Banco Santander group. We operate one year rolling terms for all NEDs in line with best practice.

### Board Committees

All Board Committees are chaired by INEDs and have only INEDs as members, other than the Board Risk Committee and Board Nomination Committee. Following Manuel Soto's retirement from the Board in December 2017, the Board Audit Committee is also comprised of INEDs only and our policy is for it to remain that way.

During the second half of the year we established the Board Responsible Banking Committee to assist the Board in shaping the culture, reputation and customer propositions of Santander UK through overseeing and advising management on conduct, people, community, brand and compliance issues. A full report on the activities of the committee will be included in the 2018 Annual Report.

We undertook a comprehensive review in April 2017 of the composition of the Board Committees. Previously, all INEDs served on all of the Board's Committees except the Board Nomination Committee, largely to accelerate their understanding of the key issues facing Santander UK given the number of changes to the population of INEDs three years ago.

### Board composition at December 2017<sup>(1)</sup>

#### Shriti Vadera

Independent Board Chair  
Chair of Nomination Committee

### Independent Non-Executive Directors

#### Alain Dromer

#### Annemarie Durbin

Chair of Remuneration Committee

#### Ed Giera

Chair of Risk Committee

#### Chris Jones

Chair of Audit Committee

#### Genevieve Shore

Chair of Customer & Innovation Forum<sup>(2)</sup>

#### Scott Wheway

Senior Independent Director  
Chair of Responsible Banking Committee

### Banco Santander nominated Non-Executive Directors

#### Lindsey Argalas

(with effect from 1 January 2018)

#### Ana Botín

#### Gerry Byrne

#### Juan Rodríguez Inciarte

### Executive Directors

#### Nathan Bostock

Chief Executive Officer

#### Antonio Roman

Chief Financial Officer

#### Javier San Felix

Head of Retail & Business Banking  
and Deputy CEO

(1) The terms 'independence' and 'Independent' are, unless otherwise stated, defined in accordance with our UK Group Framework.

(2) The Customer & Innovation Forum is a management committee.

# 31%

Female Board members

31 December 2016



Following a planned review, the membership of the Board Audit, Remuneration and Nomination Committees has been reduced to improve efficiency and effectiveness. It was decided that all INEDs would remain on the Board Risk Committee given the nature of the issues considered by that Committee. Committee readouts at Board meetings by Committee Chairs have been enhanced to ensure the Board as a whole is kept well-informed of the discussions at all the Committees. The membership of the Committees is set out on page 60 of the 2017 Annual Report.

We have undertaken an annual review of all the Terms of Reference of the Board Committees in line with best practice, with minor changes required. Additionally, Terms of Reference for the Board Responsible Banking Committee were approved in June 2017 and we agreed consequential changes for the Terms of Reference for the Board Risk Committee to effect the allocation of tasks between both Committees. All Terms of Reference are available on our website at [www.santander.co.uk](http://www.santander.co.uk).

### Diversity

Following the appointment of Lindsey Argalas in 2018, we achieved a ratio of 36% female directors, three years ahead of our target of 33% by 2020. We will continue to strive toward gender balance and improving our broader diversity.

### Culture

In 2017, we further strengthened the connection between culture, conduct and customer outcomes by establishing the Board Responsible Banking Committee.

# 36%

Female Board members

1 January 2018



**How we spent our time (%)**

|                        | 2017 | 2016 |
|------------------------|------|------|
| Business and customer  | 45   | 54   |
| People                 | 15   | 10   |
| Risk and control       | 20   | 12   |
| Regulation and capital | 10   | 15   |
| Governance             | 10   | 9    |



### How we spent our time

As in previous years, the nature of Board discussions means the categorisation of how we spent our time is somewhat artificial, given that many topics such as commercial business issues, people, regulation and risk management are inseparable in nature. Nevertheless we have maintained the discipline of recording the allocation of time through a consistent methodology so that we can monitor changes in the way we allocate time to our strategic priorities even if, in absolute terms, the definitions are less illuminating.

During 2017, the Board spent 45% of its meeting time on business and customer priorities, down from 54% in 2016. Some of this reduction resulted from the establishment during the year of the Board Responsible Banking Committee which spent time, for instance, assessing our overdraft strategy and recommending changes to the Board. The reduction also reflects the additional amount of time that was devoted to our people (2017: 15%; 2016: 10%) to develop further our plans for succession, talent management and to equip Santander UK with the necessary skills to deliver our medium and long-term vision in the face of market change. The Board also spent additional time during the year on risk and control matters and assessing our readiness for new regulatory requirements, such as ring-fencing, MiFID II and GDPR.

As was the case in 2016, we held our annual two-day strategy offsite in June 2017 focusing on the importance of innovation and digital transformation for our future business. The Board and management discussed the opportunities and risks facing Santander UK and approved a number of initiatives to improve the customer experience and help deliver future growth. The output from the strategy day helped inform the Board's forward agenda for the remainder of 2017 and for 2018.

### Board effectiveness

We reviewed the progress made on the actions arising from last year's in depth external evaluation of Board effectiveness, which in addition to discussion at the Board Nomination Committee and the Board, have also been discussed at the meetings of the Board Committee Chairs held quarterly. Due to the extensive nature of the external review carried out over a number of months in the prior year, the Board on the recommendation of the Board Nomination Committee decided not to carry out an external evaluation in 2017. The internal review has concluded that the Board, the Chair and each of its Directors remain effective.

### Future Board priorities

In 2018, we expect to spend more time moving to a new customer-centric operating model, on innovation and technology, the implementation of an efficiency plan, delivering our people strategy and talent management planning, conduct and culture, and ring-fencing. This focus underpins everything we do to be Simple, Personal and Fair, and is directed towards being the best bank for our people, customers, shareholders and communities.

# Stakeholder review



## Customers

We aim to build lasting relationships with our customers by being a bank that is Simple, Personal and Fair in everything we do.

### Helping our customers prosper

Our focus is to help our customers at the moments that matter most, delivering an excellent service and products that make a real difference to their lives.

Our investment in technology has given our customers the choice of how, when and where they can access and manage their money. Be that through our branch network, telephone or digital channels. Our customers can apply for our full range of core products online, with an option to save a part-completed application.

In 2017, we continued to improve our business banking services for smaller SME customers. We streamlined our portfolio to increase capacity and improve client support. We also introduced a fast-track asset finance process and a simplified credit application to facilitate quicker lending decisions for smaller exposures.

In June 2017, we launched the new World Elite MasterCard for Santander Select and Santander Private customers offering a world of travel benefits. This formed part of the launch of Santander Private, a service to provide banking and wealth management services to private clients, business owners and entrepreneurs. This was followed by the launch of new current accounts for our Select and Private customers in November 2017.

We were also the first bank to launch Talking ATMs across our entire UK branch network. This gives audible guidance to customers to help them use our ATMs, either with or without the use of the screen. In addition, we launched a new branch locator tool with an enhanced mobile experience to give our customers easy access to branch information.

### Optimising our branch network

We continued to invest in our network of 806 branches, with almost 500 refurbished so far. This included new layouts, services and technology to serve our customers better.

Ongoing reviews aim to ensure our resources are targeted efficiently by removing duplication due to close proximity and closing branches which are under utilised. We are a signatory to the Access to Banking Standard which ensures open and fair communication where banks decide to close branches. In 2017, we closed 36 branches in line with this standard.

### Supporting our vulnerable customers

We are committed to supporting our vulnerable customers. All customer-facing colleagues are trained to help recognise vulnerable customers and to understand the issues which affect them.

Colleagues now have access to a support tool providing guidance and solutions for vulnerable customers. A dedicated team provides intensive support to customers facing financial difficulty by helping them regain control of their finances, with solutions tailored to their individual circumstances.

The consideration of vulnerable customers has been part of our product approval process for over a year and we have an approved vulnerable customer policy which applies across all areas of the bank. Specific social insights research is used to better understand the needs of older customers, and we will continue to build on this into 2018.

### We are championing British businesses

Santander Breakthrough helps ambitious businesses grow and prosper through a range of activities focused on talent, networking, knowledge, finance and international growth. In 2017, over 6,270 businesses engaged in Breakthrough activities including more than 3,290 attendees at 160 Breakthrough in Branch events, which continue to connect business owners to their local business community.

We also organised a wide range of masterclasses and workshops with some of the UK's most innovative companies – 400 businesses have benefited from practical



## Innovative digital tools

A new Mortgage Video Service allows customers to access mortgage advice via video from either 60 video-enabled branches or from their home using their own device. The service has received extremely positive feedback, with an overall customer recommendation rating of 9 out of 10.

Another important innovation is our Mortgage Chatbot which we launched in October 2017. This tool for existing mortgage customers who are choosing a new deal provides immediate answers to generic, non-case specific questions. From launch to the end of 2017, more than 6,000 users asked over 10,000 questions.

solutions to grow their business. In addition, more than 1,600 SMEs benefited from the Santander Universities Internship Programme with access to subsidised internships from one of more than 80 partner universities.

Beyond everyday banking, we helped businesses achieve their global ambitions with 246 companies benefiting from 28 overseas and virtual trade missions. Our Liverpool City Incubator is an initiative that helps steer start-up founders in the right direction. During 2017 this provided tailored support to 34 businesses.

Some of our customers have the potential for significant growth and require capital as well as non-financial support. In 2017, our Growth Capital Team provided £31.2m of growth capital and £152.7m of senior debt to 50 companies.



## Shareholders

We aim to deliver a long-term, sustainable return for our shareholders while helping people and businesses prosper.

### Being an important part of a global bank

We are a subsidiary of Banco Santander and part of the Banco Santander group. Our parent is a leading retail and commercial bank, founded in 1857, head-quartered in Spain and among the world's top banks by market capitalisation. Banco Santander has meaningful market share in 10 countries in Europe and the Americas.

At the end of 2017, Banco Santander had 133 million customers, 13,697 branches and 202,000 employees. In 2017, Banco Santander reported €6,619m attributable profit. Santander UK is an important part of the global business and contributed 16% of underlying attributable profit (excluding the Corporate Centre and Spanish Real Estate).

Our ordinary shares are all held by Banco Santander group companies and are not listed. Our preference shares, however, are listed on the London Stock Exchange. We also have other equity instruments, in the form of four AT1 securities issued in 2014, 2015 and 2017.

**£1,254m**

profit after tax  
(2016: £1,317m)



### Consistent shareholder returns

We remained consistently profitable throughout the financial crisis. Our profitability has been built on the strength of our proposition, cost discipline and our prudent approach to risk appetite.

Our track record of profitability enabled us to pay a dividend every year since 2008. Our policy is to declare a dividend of 50% of earnings attributable to ordinary shareholders.

### Benefiting from being an independent subsidiary

Banco Santander operates a subsidiary model to minimise the risk of problems in one part of the organisation spreading to another. This means that autonomous subsidiaries, like us, are responsible for their own liquidity, funding and capital management.

The subsidiary model gives us considerable financial and operational flexibility while also allowing us to take advantage of the significant synergies and strengths that come from being part of a major, well-diversified banking group.

Importantly we benefit from Banco Santander's strong brand, products and platforms as well as their systems development capacity – we utilise common technology platforms. Taken together, these constitute a major competitive advantage for us.

### Effective investor engagement

Banco Santander has a large retail shareholder base in the UK, a legacy of our former building society heritage. The Banco Santander Shareholder Relations team provides help and support for these shareholders, and manage all engagement with them.

Our UK Investor Relations team actively engages with institutional investors across the globe. In 2017, we held over 200 meetings with existing and prospective debt and equity investors, and presented our strategic update at the Banco Santander Group Strategy Day in New York. Our investors continued to focus on the UK macro environment, including competition and regulation, business momentum and business growth as well as our debt issuance plans.

Our well-executed capital and debt issuance programmes and good credit ratings are, in part, due to our successful investor engagement programme. It also reflects the investor support and interest in our proposition as an independent entity and a core geography in the Banco Santander group.



## A straightforward ring-fence structure

UK legislation establishes new requirements for certain UK banks to ring-fence their retail activities, such as current accounts, savings accounts and payments. The largest UK banking groups, including Santander UK, have to comply with these requirements by 1 January 2019.

Santander UK plc will become the main ring-fenced bank of the Santander UK group. It will serve all our personal customers in the UK and the vast majority of our business customers.

To the extent allowed by the legislation, the ring-fenced bank will also broadly continue to hold and serve our corporate banking business in the UK. There will be some instances where products cannot be offered, or customers cannot be served from within the ring-fence bank. In most of these instances, these products will be provided, or these customers served, by Banco Santander through its London branch. This will include some Global Corporate Banking business and Corporate Banking customers.

Abbey National Treasury Services plc will transfer all of its business to either Santander UK or Banco Santander's London Branch, save for a small portfolio of specific assets that will remain in Abbey National Treasury Services plc and be held until their maturity.



## Stakeholder review continued



### People

We aim to attract, retain and reward the most talented and committed people. We offer first-class development schemes and a workplace that empowers people, encourages individuality and promotes collaboration.

#### Helping our people prosper

We provide a full range of skills, development, training and career support for our people to develop their potential. During 2017, our people undertook over 104,800 training days and we invested over £8.8m in employee learning and development.

Our approach is to provide our people with a competitive package of pay and benefits, and to reward them for their contribution to the business and our sustainable performance. We act in accordance with all relevant and applicable legislative and regulatory rules and guidance, regularly benchmarking our package and policies to ensure we remain aligned to the market. We are a Living Wage and London Living Wage employer. We have a successful ongoing partnership with Advance and the Communication Workers Union (CWU), our recognised trade unions. In 2017, we continued consultation on significant proposals and business change initiatives.

We offer a range of personalised benefits, and focus on financial wellbeing for our people. We encourage our people to participate in our pension and share ownership schemes. In 2017, 36% of colleagues participated in one or both of our two HMRC-approved share save schemes.

#### Prioritising diversity

We seek to create a culture where every employee and customer is treated with respect. Through our workplace policies we continue to recognise the potential that all people bring to the workplace regardless of age, disability, gender, gender identity, marital or civil partnership status, maternity, pregnancy, race, sexual orientation, religion or belief (or absence of).

We embed diversity and inclusion across our business through a number of initiatives, programmes and training. These include our employee-led diversity networks, Women in Business, Embrace, Parents&Carers, Ethnicity@Work, Enable! and unconscious bias training. We also ensure that all internal communications reflect the diversity of our employees and customers in the language and images we use.

In June 2016, we signed the HM Treasury Women in Finance Charter – setting a 50% (+/-10%) gender target for our senior female population over the next five years. Women made up 31% of our Board, 40% of executive committee and over 28% of senior managers at 31 December 2017.

#### Protecting the wellbeing of our people

A safe and healthy workplace is fundamental to help our people prosper. We provide practical advice, emergency support and training for both employees and managers. Our managers are also given training and support to foster psychological well-being within their teams, and to recognise where support may be needed.

We offer free and confidential telephone advice 24/7, face-to-face counselling and critical incident support, with a special focus on assisting employees facing difficult circumstances. Santander Personal Support Services provides practical, emotional and, in some cases, financial support for a broad range of lifestyle issues.

In 2017, we launched a digital version of our quarterly staff magazine, Health and Lifestyle Update. We also updated the magazine and launched a 'cover star' campaign to celebrate inspirational employee stories. One of these featured a young man from our Retail division and the challenges he faces working with severe autism. Another featured a transgender woman, and the journey she went through to be true to who she is in the workplace.

**£8.8m**

Investment in employee training and development in 2017 equivalent to 4.6 days training per FTE



### Gender pay gap report

We are committed to creating a culture that values and champions diversity, and creates equality of opportunity for all. This is a commitment that starts at the very top of our organisation and flows throughout it.

The gender pay gap takes into account all roles at all levels of the organisation, rather than comparing pay received by women and men performing the same roles. We regularly review and analyse our employee pay to ensure men and women are treated equally when performing the same role. We are, therefore, confident that we do not have an equal pay issue at Santander UK.

Instead, our gender pay and bonus gaps reflect our organisational structure. Santander UK has proportionally more women than men in our branch and customer service centre roles, and proportionately more men in our senior leadership team.

We are committed to overcoming this through transparency, understanding the root causes of issues and finding solutions that are both practical and beneficial to employees.

We are realistic about the challenges we face, and the historical composition of financial services that we are seeking to evolve. We know there is more to do and we are committed to improving diversity and inclusion at all levels in the bank.

For our 2017 Gender Pay Gap Report see [www.santanderjobs.co.uk/diversity](http://www.santanderjobs.co.uk/diversity).



## Communities

We support communities around the UK by providing skills, knowledge and innovation.

### Helping our communities prosper

We are passionate about creating value for the communities that we serve. The Discovery Project is our flagship community investment initiative that aims to help one million people by 2020. The programme supports skills, knowledge and innovation projects through:

- Explorer: to help people learn about the world and prepare them for the future
- Transformer: to guide people through work-focused support and training
- Changemaker: to fund innovations that help society.

We rely on the support of a number of partners who help us to deliver our aims. These include, Young Enterprise, Career Ready, National Citizen Service, Money Advice Trust and Crowdfunder.

As well as providing funds and promoting initiatives that support the aims of The Discovery Project, we also encourage our people to share their skills and time by volunteering in their communities.

# 281,700

People helped through our Discovery Project

### Crowdfunding

In 2017, we partnered with Crowdfunder to explore new ways to fund community groups, charities and social entrepreneurs to build skills, grow knowledge and support innovation. Selected projects that received the backing of the 'crowd' received matched funding of up to £10,000. During 2017, 42 projects were supported providing over £303,000 in funding and helping over 2,000 beneficiaries.

### Santander Foundation

In 2017, the Santander Foundation provided over £3.1m in grants to over 700 organisations for projects that help disadvantaged people. Discovery Grants are available to registered UK charities, community interest companies or

credit unions to support activities that improve skills, knowledge or support social innovation. The Santander Foundation also contributed over £2.3m through the Staff Matched Donation Scheme to support our employees' fund raising activities for charities of their choice.

### Our charity partners

Our commitment to our 3 year partnership with Age UK and Barnardo's continued in 2017, with the aim of supporting older and young people through fund raising and volunteering. In 2017, our people raised over £1m taking the total funds raised since 2016 to over £2.2m.

### Celebrating our support for Higher Education

Since 2002, Banco Santander has donated over €1.5bn to universities across the globe. This made it one of the largest global corporate contributors to education, according to a 2015 report by the Varkey Foundation and UNESCO.

In the UK we have donated over £60m to 83 UK partner universities over the last ten years. In 2017, we directly supported over 13,000 students, graduates and university staff through initiatives focusing on education, employability and entrepreneurship.

With our partner universities we also fund internships for students and graduates in SMEs across the UK. In the 2016/2017 scheme we supported over 2,200 internships in over 1,600 businesses from which 55% of participants secured further employment<sup>(1)</sup>.

As part of our strategy we also promote the Entrepreneurship Awards, one of the UK's largest student and graduate business pitching competitions. In 2017, we included a three day programme to provide 18 of the best start-ups with over 20 masterclasses.

Our £1m Enterprise and Entrepreneurship Fund supports university-led projects across the UK. This helps students start, run or scale a business, or champion the development of entrepreneurial skills, cultures and mind-set.

In 2017, we launched an innovative cycle hire scheme competition for twenty three partner universities for the chance to win funding from Santander to implement their own cycle schemes on campus.



## Santander Cycles

The Santander Cycle scheme continues to be a great success, helping people get around London and Milton Keynes while keeping fit and saving money. Revenue raised by the London scheme increased by £400,00 in 2017. This reduced the subsidy needed from public funds to run the scheme. During 2017, almost 10.5m bike hires were made, the second record breaking year in a row.

In a partnership with our customer Blaze, we completed installing Laserlights on all 12,000 Santander Cycles. We also launched a new generation of bikes with in-built smart technology, including GPS and bluetooth. Trials of new beacons and wireless technology at Santander Cycle docking stations helped keep the public up to date.

We celebrated the first anniversary of the Santander Cycles scheme in Milton Keynes alongside the town's 50th year celebration. We reached over 70,000 bike hires and almost 17,000 registrations in 2017, and opened our 50th docking station. We also supported a number of community initiatives including the National Youth Circuit Championships, the HerdaboutMK initiative (alongside our charity partner Barnardo's) and co-funding of the Discover MK app.

(1) Based on the total number of responses from our survey

## Stakeholder review continued

### Corporate Social Responsibility and Sustainability

We want to help people and businesses prosper now and in the future. We'll do this by leading the bank in the right way and doing the right thing for all of our customers, shareholders, people, and communities.

#### Managing our environmental impact efficiently

Our Environmental & Energy Management Systems (EMS & EnMS) provide a framework for defining responsibilities and processes in relation to waste, energy, water, travel and supply chain management at our 15 main offices and data centres in the UK. In 2017, we successfully recertified the ISO 14001 & ISO 50001 accreditation across all of these properties.

Smart meter technology allows us to track the energy performance of our properties, helping us to reduce energy wastage. This contributed to an annual reduction of 10% in electricity and 5% in gas usage. Our electricity is sourced from green suppliers and has zero carbon emissions.

Business travel represents 52.2% of our total CO<sub>2</sub> emissions which fell from 6,650 tonnes in 2016 to 5,997 tonnes in 2017, representing a 9% reduction per employee. We encourage our people to use travel-free meeting methods wherever possible.

Over 99% of the waste generated through our operations is either recycled or diverted from landfill. In the past two years, we have cut our paper usage by 37%, although in 2017 this was 12% higher than 2016. Our online banking customers receive paperless statements (with an opt-out option), and our print suppliers have ISO 14001 certification and maintain full Forest Stewardship Council chain of custody.

#### Managing our supply chain responsibly

We buy goods and services from over 1,600 external suppliers and intra-group companies accounting for £1.7bn of costs in 2017, governed by our Cost Management and Procurement Policy, Third Party Risk Management Policy and Conduct in Supplier Relationships Manual.

We meet the Living Wage requirement for employees of suppliers who work at Santander UK sites, and our supplier contracts include specific requirements to respect human rights and ethical labour practice based on the principles of the UN Global Compact.

We are a signatory to the Business in the Community Access Pledge, a public commitment to a fair and open procurement process for SMEs. In 2017, 80% of our new supplier contracts, worth over £7m, were with businesses with less than £10m annual turnover or 250 employees.

#### We are committed to high ethical standards

We adhere to laws and regulations, conduct business in a responsible way and treat our stakeholders with honesty and integrity. We review each investment and lending proposal case-by-case, taking account of the potential impact on human rights, public health and the environment. We also consider the ethics of supporting or partnering with particular organisations, governments and projects.

Our Code of Ethical Conduct sets out the standards we expect of our people. It supports our commitment to being Simple, Personal and Fair and also helps to protect our reputation by building a culture free from corruption, risk of compromise or conflicts of interest.

See page 63 of the 2017 Annual Report for more on our Code of Ethical Conduct and Anti-Bribery and Corruption Policy.

#### Developing how we report our corporate social responsibility

We believe that the performance of our business cannot be considered separately from the sustainability of the wider environment and the prosperity of our stakeholders. We regularly engage with our stakeholders, including our regulators, the government, the media and consumer groups to ensure we listen to their views to define issues that are important to the society as a whole as well as our business.

### Modern Slavery Act 2015

We actively seek to prevent slavery and human trafficking in our workforce and supply chain. We have put in place a number of measures across the business to help drive this outcome. As an example, we now require our suppliers to comply with explicit requirements to respect human rights and adhere to ethical labour practice.

We have also reviewed our pension arrangements to ensure that, where relevant, the fund managers comply with the Act. We will review this annually to ensure continued compliance.

We will continue to assess the impact and effectiveness of these measures and will continue to work with our stakeholders to prevent slavery and human trafficking in our workforce and supply chain.

Our Sustainability Report will provide further details of our community projects, our contribution to the prosperity of the economy and our impact on the environment. This is the first step in the development of how we manage, monitor and report on our corporate social responsibility. We plan to share further insight on the subsequent steps in that development during 2018.

In 2017 we changed the reporting of Discovery Project grants to include committed spend and associated donations for the year rather than on the timing of payments. This change better reflects activity during the period and aligns to how beneficiaries report donations and grants.

Colleague engagement is measured by a survey conducted by Korn Ferry. One of the survey questions changed in 2017 and so, to remove the effect of this, the 2017 result incorporates some 2016 data.

#### Assurance statement of non-financial reporting

We commissioned SGS United Kingdom Ltd to provide assurance at moderate level on the veracity of non-financial 2017 data and claims on pages 22 and 24 to 27 of this Stakeholder review. The full assurance statement is available at: [santander.co.uk/uk/about-santander-uk/csr](http://santander.co.uk/uk/about-santander-uk/csr).

## Other information

| At 31 December                             |     | 2017        | 2016        | 2015        | Notes  |
|--|-----|-------------|-------------|-------------|--|
| <b>Customers</b>                           |     |             |             |             |  |
| Loyal retail customers                     | KPI | 3.9 million | 3.7 million | 3.7 million |  |
| Loyal SME and corporate customers          | KPI | 305,000     | 290,000     | 266,000     |  |
| Retail customer satisfaction               | KPI | 63.0%       | 62.9%       | 62.9%       | Financial Research Survey by GfK, December 2017  |
| Digital customers                          | KPI | 5.0 million | 4.6 million | 3.9 million |  |
| Fee income CAGR                            | KPI | 6%          | 8%          | (3)%        | 2016 and 2017 CAGR measured from 31.12.15  |
| FCA reportable customer complaints         |     | 363,340     | 250,463     | 223,235     | 2017 increase largely due to PPI, following complaints deadline confirmation by the FCA and customer information campaign                                |
| <b>Shareholders</b>                        |     |             |             |             |  |
| RoTE                                       | KPI | 10.2%       | 10.9%       | 8.2%        |  |
| Return on ordinary shareholders' equity    |     | 8.9%        | 9.6%        | 7.2%        | Restated per accounting policy change outlined in on page 28   |
| CIR  | KPI | 51%         | 50%         | 53%         |  |
| CET1 capital ratio                         | KPI | 12.2%       | 11.6%       | 11.6%       |  |
| NPL ratio                                  | KPI | 1.42%       | 1.50%       | 1.54%       |  |
| Dividend payout ratio                      | KPI | 50%         | 51%         | 50%         |  |
| Water usage (m <sup>3</sup> )              |     | 278,699     | 301,565     | 293,598     |  |
| Waste collected (tonnes)                   |     | 5,288       | 4,506       | 4,517       |  |
| CO <sub>2</sub> per employee (tonnes)      |     | 0.47        | 0.52        | 0.66        |  |
| <b>People</b>                              |     |             |             |             |  |
| Colleague engagement                       | KPI | 71%         | 72%         | 71%         | See note on changes to our reporting on page 26  |
| Full-time equivalent employees             |     | 19,432      | 19,220      | 19,992      | Santander UK employees at 31 December  |
| Employee turnover                          |     | 15%         | 13%         | 14%         |  |
| <b>Communities</b>                         |     |             |             |             |  |
| People supported                           | KPI | 281,700     | 196,300     | N/A         |  |
| Support to communities                     |     | £19.4m      | £22.0m      | £23.4m      | See note on changes to our reporting on page 26  |
| Corporation tax paid                       |     | £484m       | £507m       | £419m       | See <a href="http://www.santander.co.uk/uk/about-santander-uk/csr/taxation-strategy">www.santander.co.uk/uk/about-santander-uk/csr/taxation-strategy</a> |
| % of contracts awarded to small businesses |     | 80%         | 61%         | 58%         | Businesses with <£10m turnover or <250 employees   |

## KPI definitions

**Loyal retail customers:** Primary banking current account customers who hold an additional product.

**Loyal SME and corporate customers:** Santander Business Banking customers, managed under Retail Banking, who have three month average credit turnover of at least £1,000 across their Banking accounts. Corporate customers, who have at least three products and, for those in the trade business, must also have a current account with a minimum activity threshold specific to their customer segment.

**Retail customer satisfaction:** Measured by the Financial Research Survey (FRS) run by GfK for 12 months ended 31 December 2017.

**Digital customers:** Customers who have logged onto Retail or Business online banking or mobile app at least once in the month.

**Fee income CAGR:** Net fee and commission income compound annual growth rate is measured between end 2015 and end 2018.

**Return on tangible equity:** The profit after tax attributable to equity holders of the parent, divided by average shareholders' equity less non-controlling interests, other equity instruments and average goodwill and other intangible assets.

**Cost-to-income ratio:** Total operating expenses as a percentage of total income.

**NPL ratio:** Non-performing loans as a percentage of loans and advances to customers.

**CET1 capital ratio:** CET1 capital as a percentage of risk-weighted assets.

**Dividend payout ratio:** Equity dividend declared as a percentage of earnings attributable to ordinary shareholders (profit after tax less payment of dividend on equity accounted instruments and non-controlling interests).

**Colleague engagement:** Measured by the Group Engagement Survey (GES), conducted by Korn Ferry for Banco Santander during September and October 2017. Results are benchmarked against other firms in the UK financial sector and other high-performing firms.

**People supported:** People supported through our charity partnerships, the Santander Foundation, Santander Universities and by employee volunteer activities through our Discovery Project programme.

For our KPIs, read more on **page 13**

For our glossary see: [santander.co.uk/uk/about-santander-uk/investor-relations-glossary](http://santander.co.uk/uk/about-santander-uk/investor-relations-glossary)

### The Directors, in preparing this Strategic Report, have complied with s414C of the Companies Act 2006.

Under the UK Companies Act 2006, a safe harbour limits the liability of Directors in respect of statements in and omissions from the Strategic Report. Under English law the Directors would be liable to the Company, but not to any third party, if this report contained errors as a result of recklessness or knowing misstatement or dishonest concealment of a material fact, but would otherwise not be liable. The Strategic Report has been drawn up and presented in accordance with and in reliance upon English company law and the liabilities of the Directors in connection with these reports shall be subject to the limitations and restrictions provided by such law.

## Summarised consolidated income statement

| For the years ended 31 December  | 2017<br>£m     | 2016<br>£m     |
|--|----------------|----------------|
| Net interest income  | 3,803          | 3,582          |
| Non-interest income <sup>(1)</sup>   | 1,109          | 1,213          |
| <b>Total operating income</b>  | <b>4,912</b>   | <b>4,795</b>   |
| <b>Operating expenses before impairment losses, provisions and charges</b> | <b>(2,502)</b> | <b>(2,417)</b> |
| Impairment losses on loans and advances                                    | (203)          | (67)           |
| Provisions for other liabilities and charges                               | (393)          | (397)          |
| <b>Total operating impairment losses, provisions and charges</b>           | <b>(596)</b>   | <b>(464)</b>   |
| <b>Profit before tax</b>   | <b>1,814</b>   | <b>1,914</b>   |
| Tax on profit  | (560)          | (597)          |
| <b>Profit after tax for the year</b>                                       | <b>1,254</b>   | <b>1,317</b>   |

(1) Comprised of 'Net fee and commission income' and 'Net trading and other income'.

## Summary of segmental balance sheet assets and liabilities

| At 31 December                          | 2017<br>£bn  | 2016 <sup>(2)</sup><br>£bn |
|---|--------------|----------------------------|
| <b>Customer loans</b>                   |              |                            |
| Retail Banking                          | 169.0        | 168.6                      |
| Commercial Banking                      | 19.4         | 19.4                       |
| Global Corporate Banking                | 6.0          | 5.7                        |
| Corporate Centre                        | 5.9          | 6.5                        |
| <b>Total customer loans</b>             | <b>200.3</b> | <b>200.2</b>               |
| Other assets                            | 114.5        | 102.3                      |
| <b>Total assets</b>                     | <b>314.8</b> | <b>302.5</b>               |
| <b>Customer deposits</b>                |              |                            |
| Retail Banking                          | 149.3        | 148.1                      |
| Commercial Banking                      | 18.7         | 17.2                       |
| Global Corporate Banking                | 4.5          | 4.1                        |
| Corporate Centre                        | 3.4          | 3.0                        |
| <b>Total customer deposits</b>          | <b>175.9</b> | <b>172.4</b>               |
| Medium-Term Funding                     | 40.6         | 46.1                       |
| Other liabilities                       | 82.1         | 68.5                       |
| <b>Total liabilities</b>                | <b>298.6</b> | <b>287.0</b>               |
| Shareholders' equity                    | 15.8         | 15.1                       |
| Non-controlling interest <sup>(3)</sup> | 0.4          | 0.4                        |
| <b>Total liabilities and equity</b>     | <b>314.8</b> | <b>302.5</b>               |

(2) In 2017 we changed the accounting policy for acquisitions where the business is ultimately controlled by the same entity both before and after the purchase. These acquisitions are now accounted for at book value. This change reduced retained earnings and goodwill of previous acquisitions by £631m. This amount largely represents the difference between the purchase price and the aggregate book value of the assets and liabilities acquired from Banco Santander S.A. in 2010. The comparative period has been restated to reflect this change in accounting policy.

(3) Non-controlling interests refers to other equity instruments issued by Santander UK plc and PSA Finance UK Limited (PSA cooperation), a cooperation between Santander Consumer (UK) plc and Banque PSA Finance SA (accounted for as a subsidiary).




## Further Information

### Contact us

#### Customer services

For further information about products and services, please visit our website:

 [santander.co.uk](http://santander.co.uk)  
[customerservices@santander.co.uk](mailto:customerservices@santander.co.uk)

 +44 (0)870 6076000



#### Shareholders

Information for UK shareholders of Banco Santander can be found at our website:

 [santandershareholder.co.uk](http://santandershareholder.co.uk)  
[santandershareholders@equiniti.com](mailto:santandershareholders@equiniti.com)

By post, please write to:

Santander Nominee Service  
Aspect House  
Spencer Road  
Lancing BN99 6DA

 +44 (0)371 3842000  
 +44 (0)121 4157188 (From outside the UK)

#### Community involvement

To find out more about applying for donations and the Santander UK Foundation, please visit our website:

 [santanderfoundation.org.uk](http://santanderfoundation.org.uk)

#### Media centre

Contacts for the media relations team are available at our website via the media section:

 [aboutsantander.co.uk](http://aboutsantander.co.uk)  
[mediarelations@santander.co.uk](mailto:mediarelations@santander.co.uk)

#### Investor relations

For financial results and presentations, stock exchange announcements, credit ratings and information for debt investors, please visit the investor relations section of our website:

 [aboutsantander.co.uk](http://aboutsantander.co.uk)  
[ir@santander.co.uk](mailto:ir@santander.co.uk)

### Key Dates

24 April 2018  
25 July 2018  
31 October 2018

Q1 2018 results  
Q2 2018 results  
Q3 2018 results

### Glossary

#### Retail customer satisfaction

The Financial Research Survey (FRS) is a monthly personal finance survey of around 5,000 consumers prepared by the independent market research agency, GfK.

The 'retail customer satisfaction' score refers to the proportion of extremely and very satisfied customers across mortgages, savings, main current accounts, home insurance, UPLs and credit cards, based on a weighting of those products calculated to reflect the average product distribution across Santander UK and competitor brands.

The competitor set used to calculate the product weights is Barclays, Halifax, HSBC, Lloyds Bank, Nationwide and NatWest. The competitor set included for the ranking and highest performing peers is Barclays, Halifax, HSBC, Lloyds Bank and NatWest.

#### 2016-2018 KPIs and targets

KPIs are presented at 31 December in the periods indicated. Reported KPIs are based on spot balances at these dates with the exception of the CIR, RoTE, and retail customer satisfaction, which are based on performance in the relevant period or year.

KPI targets for 2018 were set at the 2015 Banco Santander Investor Day based on the forecast and outlook then in place. Three targets were revised in 2016. At the 2017 Group Strategy Update we revised our RoTE 2018 target to 9%-10% from 8%-10%. We plan to provide a strategic update for the period beyond our current 2016-2018 target horizon during 2018.

#### For a glossary of terms used in this report:

[www.santander.co.uk/uk/about-santander-uk/investor-relations-glossary](http://www.santander.co.uk/uk/about-santander-uk/investor-relations-glossary)



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