# Summary financial statement

**This financial statement is a summary of information in the audited Annual Accounts, the Directors' Report and the Annual Business Statement, all of which will be available to members and depositors on demand at every office of Yorkshire Building Society from 12 March 2009.**

Approved by the board of directors on 2 March 2009.

Ed Anderson, Chairman

Richard Davey, Vice Chairman

Iain Cornish, Chief Executive

## Summary Directors' Report

**2008 has been a difficult year for all financial institutions, with a combination of worsening economic conditions, a falling housing market and the credit crunch. Some institutions have fallen, and many others have stumbled. The Yorkshire, whilst not unscathed by the conditions, continues to be a strong, independent mutual organisation**.

There are a number of factors behind the issues facing the UK during 2008 and into 2009:

- there has been a continuation of the disruption to the world's financial markets that started in 2007. The situation became markedly worse with the collapse, or near collapse and government rescue, of a significant number of household names across the world including in the UK the Icelandic banking groups, Bradford & Bingley, Halifax Bank of Scotland and Royal Bank of Scotland. The second half of 2008 also saw the merger or proposed merger of a number of UK building societies who found themselves the victim of these uncertain times – and indeed we helped out through our merger with the Barnsley Building Society, an otherwise well run local society that unfortunately had significant exposures to failed Icelandic banks;
- allied to these issues, the second half of 2008 saw the UK economy enter a recession. The outlook remains gloomy, with almost universal forecasts of rising unemployment and negative growth throughout 2009; and
- at the same time the UK housing market continues to see activity levels at historic lows and rapidly falling house prices. We anticipate that this will continue throughout 2009, with low lending volumes and a further significant fall in house prices.

Although these market conditions have led to material reductions in the value of a small proportion of our assets, the Society has weathered these events in good shape, principally because of a combination of:

- an exceptionally strong capital position;
- a legacy of prudent mortgage lending;
- a broad based, sustainable and well regarded funding strategy;
- a balanced approach to risk management; and
- excellent and committed staff across all areas of the business.

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"...we have reduced our rates by less than the full amount of cuts made by the Bank of England."

In the UK, this combination of a credit crunch, recession and housing downturn are all exaggerating and amplifying each other.

Throughout this period of upheaval, we have continued to manage the Society in its members' interests seeking at all times to balance the interests of our savers and our borrowers whilst, above all, protecting the financial position of the Group, which is in the interests of all members. With this in mind, for savers we have:

- continued to offer attractive savings rates and, despite staying out of certain products at times when we believed pricing was unsustainable, we have achieved over 369 best buy mentions in the year; and
- sought to protect savers as far as we are able from the financial impact of the low interest rates brought in by the Bank of England in the second half of 2008. Overall, we have reduced our rates by less than the full amount of cuts made by the Bank of England and will continue to do so wherever possible.

  We estimate that by not passing on all of the rate cuts announced in late 2008 our savers are better off than they would otherwise have been by over £50m a year.

Whilst for our borrowers:

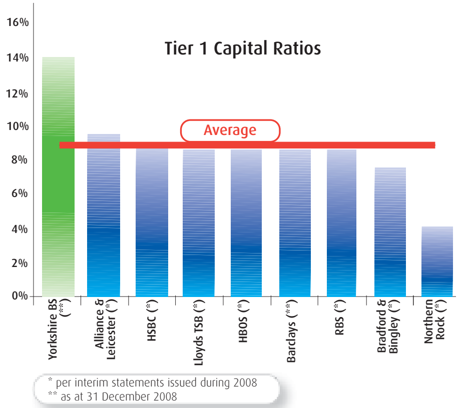
- all existing borrowers are offered an alternative to the Society's standard variable rate when their mortgage deal comes to an end;
- we contact borrowers up to 18 months before the end of their mortgage deal letting them know what their new payments might be so that they have the maximum time to adjust their finances; and
- we offer all borrowers free financial counselling where needed, and are proactive in working constructively with any borrower who is experiencing payment difficulties.

The Yorkshire is not unaffected by the wider market conditions, but we have emerged in good shape:

- the Yorkshire continues to be a strong institution in which its members can have confidence

## Core operating profit vs Statutory profit

| | 2008 £m | 2007 £m |
|---|---|---|
| **Core operating profit** | **53.0** | **91.1** |
| Treasury investments | | |
| losses from fair value volatility | (67.1) | (32.5) |
| losses realised/impairment | (7.0) | (6.9) |
| | (74.1) | (39.4) |
| Other fair value volatility | 38.3 | (11.1) |
| Other non-recurring items | 5.8 | 14.0 |
| | **23.0** | **54.6** |
| Financial Services Compensation Scheme levy | (14.7) | - |
| **Statutory profit before tax** | **8.3** | **54.6** |




– we have one of the strongest capital positions of any major UK lender (see graph above right), one of the lowest levels of wholesale funding of any major UK lender, high levels of good quality liquid assets and no exposure to many of the higher risk areas of lending such as commercial and buy-to-let; and

- our core operating profit, whilst reduced, remains healthy at £53m, and much of the reduction reflects our goal of maximising member benefit rather than profits. We have taken a number of steps to safeguard our members' interests, including:
  - early withdrawal from the few higher risk areas of lending in which we were active;
  - minimising as far as possible the impact of recent rate cuts on our savers; and
  - taking a sensible view of potential mortgage losses driven by the worsening economic conditions.

We can act in this way, despite the impact on our profits, because we are not driven by a short-term need to pay dividends to shareholders. Instead we are motivated only by the need to ensure our business is sustainable and able to deliver value to members over the long-term;

- our assets remain of a high quality. Because we are focused by our very nature on UK residential mortgage lending, we are impacted by falling house prices and rising unemployment. However our arrears remain below industry averages with the number of cases more than three months in arrears standing at 1.59% against an industry average of 1.88%. At the same time we hold high levels of good quality liquid assets; and
- our continued drive for efficiency and effectiveness in all we do continues to bear fruit. Our costs as a proportion of our assets (a key measure of efficiency) have now improved by 23% in three years. This is now worth around £35m a year to the Society. Our focus in this area will continue as long as this is not at the expense of

**"...we have one of the strongest capital positions of any major UK lender..."**

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the service we provide to our members.

Unlike many other UK lenders we did not need to raise additional capital in 2008 either from government or market sources. This in itself speaks volumes about our core strengths, especially since the authorities performed their own analyses and concluded that not only did we not require help, but that we were strong enough to provide help to other less well-placed institutions. An example of this is our merger with the Barnsley Building Society whose members and staff we are pleased to welcome to the Yorkshire Group.

Our statutory profits have fallen, to £8m against £55m in 2007, driven principally by two elements:

- a £15m charge through the Financial Services Compensation Scheme for the failures of the Icelandic banks and Bradford & Bingley, without which the Group would have been reporting a statutory profit of £23m. We have lobbied very hard to protect our members from what is undoubtedly an inequitable and disproportionate charge against those who followed the safer funding model. Building societies are by their very nature more focused on retail savings yet are paying a disproportionate share of the cost of the failure of a largely wholesale funded institution and a number of extremely aggressive overseas entrants into the UK savings markets; and
- material changes in the market value of our relatively small treasury investment portfolio. These have resulted in a real loss of £7m on sale of some of these assets, and a "book" loss of £67m on others. Total assets remaining are valued at £68m. The vast majority of these investments continue to perform and to yield a good return.

In view of this fall in statutory profits, and in the light of the general economic climate, the executive directors and General Managers have voluntarily waived their right to a bonus for 2008.

As referred to above, we have not lost sight of our key purpose – to deliver value to our members through providing

**"Unlike many other UK lenders we did not need to raise additional capital in 2008..."**

products that are good value over the long-term, and through outstanding customer service. We have continued to invest in our infrastructure and service delivery in 2008, examples of which include:

- continued commitment to our branch network with the opening of new branches in Solihull and Wolverhampton (as well as retaining all eight of the Barnsley's branches), bringing our total branch network to 143 ranging from Newquay to Inverness;
- growth in sales of our Guaranteed Investment Account, offered through Credit Suisse, up 80% against 2007, which was itself a record year for this product;
- the launch of a paperless internet savings application process, a market-leading process that won a 2008 Award for Innovation from the ifs School of Finance;
- the appointment of our Corporate Business team by 23 new Sharesave clients, including Abbey National and Stagecoach;
- a range of "behind the scenes" investments in our underlying processes and infrastructure. Areas in which we invested were as diverse as product pricing and product development systems, member enquiry and complaint handling systems, and call centre telephony; and
- a continued commitment to fighting financial crime as it impacts our members and the Group, resulting in over £2.5m being saved.

Our success in delivering customer service is reflected in two ways:

- another outstanding set of industry awards in 2008 including the Mortgage Finance Gazette "Best Debt and Arrears Management Strategy", the ifs School of Finance Financial Innovation Award for "Most Promising Initiative" and a Financial Advisor 5 star award for service; and
- most importantly, continued high ratings from our

**"...more than 9 out of 10 customers who responded ... said they would recommend us to their friends or family..."***

*Yorkshire Building Society 2008 Customer Satisfaction Survey results.

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members in our various feedback forums. Yet again more than 9 out of 10 customers who responded have said they are satisfied with our service and that they would recommend us to their friends or family.

The Yorkshire remains very well placed to continue its strategy of delivering value to our members through providing long-term products that are good value and so building sustainable relationships with them.

This requires a balanced approach across all areas of the business, including:

- growing only insofar as it does not involve taking unsustainable risks or impact on the service we offer members. In 2008 we focused particularly on ensuring that our funding is sustainable over the long-term;
- controlling our costs as far as possible, whilst ensuring that the quality and accessibility of our services are maintained at their high levels; and
- ensuring that we have in place adequate capital and liquidity to withstand the most severely stressed environment, even at the expense of short-term growth and profit.

On your behalf the board would like to thank the management and staff of your society for their continued diligence and commitment. They have seen the Yorkshire through very difficult times with a combination of professionalism and dedication and we know that they will continue to do so in 2009 and beyond.

**Whilst 2008 has been an extremely difficult year, and for some organisations a terminal one, the Yorkshire has emerged, as it entered the year, a strong independent mutual that remains committed to serving its members for many years to come.**

**"...the Yorkshire has emerged, as it entered the year, a strong independent mutual..."**

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| group results for the year | 2008 £m | 2007 £m |
|---|---|---|
| Net interest income | 164.5 | 188.2 |
| Net losses from fair value volatility | (28.8) | (43.6) |
| Net realised losses | (1.0) | (1.8) |
| Other income and charges | 31.5 | 40.9 |
| | 166.2 | 183.7 |
| Administrative expenses | (122.4) | (120.2) |
| Provisions* | (24.0) | (8.9) |
| | 19.8 | 54.6 |
| Financial Services Compensation Scheme levy | (14.7) | - |
| Operating profit | 5.1 | 54.6 |
| Negative goodwill | 3.2 | - |
| Profit before taxation | 8.3 | 54.6 |
| Taxation | 0.5 | (15.4) |
| Profit for the year | 8.8 | 39.2 |

* "Provisions" encompasses provisions for impairment of loans and advances and debt securities and provisions for liabilities.

## group financial position at end of year

| | 2008 £m | 2007 £m |
|---|---|---|
| **Assets** | | |
| Liquid assets | 5,327.7 | 4,721.9 |
| Mortgages | 16,291.8 | 15,362.0 |
| Derivative financial instruments | 1,226.7 | 294.9 |
| Fixed and other assets | 185.6 | 119.5 |
| Total assets | 23,031.8 | 20,498.3 |
| **Liabilities** | | |
| Shares | 13,683.1 | 12,448.2 |
| Borrowings | 7,329.6 | 6,640.3 |
| Derivative financial instruments | 672.2 | 94.0 |
| Other liabilities | 157.5 | 111.1 |
| Subordinated liabilities | 112.9 | 105.0 |
| Subscribed capital | 167.2 | 146.0 |
| Reserves | 909.3 | 953.7 |
| Total liabilities | 23,031.8 | 20,498.3 |

## summary of key financial ratios

| | 2008 | 2007 |
|---|---|---|
| **Gross capital as a percentage of shares and borrowings**<br>The gross capital ratio is the relationship between the Group's capital and its liabilities to investors. Capital comprises general reserves (i.e. accumulated profits), hedging and revaluation reserves, subordinated liabilities and subscribed capital (Permanent Interest Bearing Shares). | 5.66% | 6.31% |
| **Liquid assets as a percentage of shares and borrowings**<br>The liquid asset ratio measures those assets available to meet requests by investors to withdraw their money, to fund mortgage advances and to fund general business activities. It expresses cash and assets easily converted into cash as a percentage of the Group's liabilities to investors. | 25.35% | 24.74% |
| **Profit for the year as a percentage of mean total assets**<br>This ratio expresses profit, after tax, as a percentage of average total assets. | 0.04% | 0.21% |
| **Management expenses as a percentage of mean total assets**<br>The management expense ratio measures how cost-effective the Group is. It is calculated by comparing the management expenses for the year with average total assets. | 0.56% | 0.63% |

### Statement of the independent auditors to the members and depositors of Yorkshire Building Society

Pursuant to Section 76 of the Building Societies Act 1986, we have examined the Summary Financial Statement set out on pages 17-23. This auditors' statement is made solely to the Society's members, as a body, and to the Society's depositors, as a body, in accordance with Section 76 of the Building Societies Act 1986. Our work has been undertaken so that we might state to the Society's members and depositors those matters we are required to state to them in such a statement and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the Society's members as a body, and the Society's depositors, as a body, for our work, for this statement, or for the opinions we have formed.

### Respective responsibilities of directors and auditors

The directors are responsible for preparing the AGM booklet, including the Summary Financial Statement, in accordance with applicable United Kingdom law. Our responsibility is to report to you our opinion on the consistency of the Summary Financial Statement with the full Annual Accounts, Annual Business Statement and Directors' Report and its conformity with the relevant requirements of Section 76 of the Building Societies Act 1986 and regulations made under it. We also read the other information contained in the AGM booklet and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Summary Financial Statement.

### Basis of Opinion

We conducted our work in accordance with Bulletin 1999/6 'The auditors' statement on the Summary Financial Statement' issued by the Auditing Practices Board for use in the United Kingdom. Our report on the Group's full Annual Accounts describes the basis of our audit opinion on those Annual Accounts.

### Opinion

In our opinion the Summary Financial Statement is consistent with the full Annual Accounts, the Annual Business Statement and Directors' Report of Yorkshire Building Society for the year ended 31 December 2008 and conforms with the applicable requirements of Section 76 of the Building Societies Act 1986 and regulations made under it.

KPMG Audit Plc, Chartered Accountants, Registered Auditor, Leeds - 2 March 2009.