YBS GROUP

YORKSHIRE BUILDING SOCIETY INTERIM GROUP ACCOUNTS 30 JUNE 2017

Interim Management Report
for the six months ended 30 June 2017

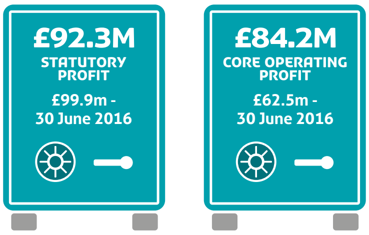
We are focused on keeping our members' interests at the heart of all that we do.

Chief Executive's summary

A STRONG START TO THE YEAR...

I am pleased to report that the Yorkshire Building Society has had another solid performance during the first half of 2017.

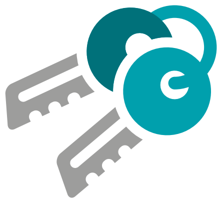
Financial highlights include:



Sustainable profits

Statutory profit before tax of £92.3m (30 June 2016: £99.9m) and core operating profit of £84.2m (30 June 2016: £62.5m). This is in line with our expectations given current market conditions and continues to represent a healthy and sustainable level of profit.

Mortgage balances

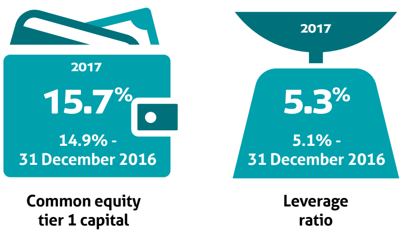


Mortgage balances of £34.0bn (31 December 2016: £34.1bn); Gross lending was £3.4bn (30 June 2016: £3.5bn). Net lending (i.e. after repayments and redemptions) was -£2m (30 June 2016: £521m).

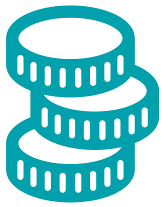
Our lending performance remains in line with our plans as we continue to take a measured approach to lending in a competitive market and an uncertain economy.

Maintained capital strength

Common equity tier 1 capital of 15.7% (31 December 2016: 14.9%) and leverage ratio of 5.3% as at 30 June 2017 (31 December 2016: 5.1%).



Savings balances

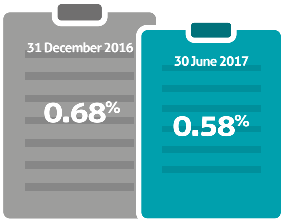


Savings balances of £28.9bn (31 December 2016: £29.1bn). Our expectation is that interest rates will remain low for some time and we need to balance our savings inflow against the amount of mortgage lending we do. Market rates have continued to fall, and we have had to manage the rates on some of our savings accounts to ensure we are not paying too much above market rates.

Chief Executive's summary continued...

Strong liquidity position

Levels remain securely above regulatory requirements. Balances increased to £5.0bn (31 December 2016: £4.7bn) representing a Liquidity ratio of 13.6% (31 December 2016: 12.8%) with a Liquidity Coverage ratio of 162% (31 December 2016: 160%).



Asset quality improvements

The value of retail mortgages three months or more in arrears (including possessions) continued to reduce to 0.58% (31 December 2016: 0.68%).

We look to make a sustainable level of profit to allow our business to grow at a sensible and healthy rate. Our current performance allows the Group to build on its financial foundation, focus on an experience for our customers in line with our vision, "to be the most trusted provider of financial services in the UK" and provide them with good-value products.

In working towards our vision, we monitor how trusted we are by both our customers and non-customers alike. We use a YouGov survey, which asks people if they agree that "Yorkshire Building Society is an organisation that you can trust". We have been ranked consistently in the top five, and as high as 2nd, during the first six months of 2017.

We measure customer experience through Net Promoter Score®[1]. This is a universally recognised metric that allows us to measure customer advocacy and loyalty. Our performance in the first six months of this year has been strong with our current score of +42 up from +34[2] at the end of 2016. This compares favourably to the industry average of +6[3].

[1] Net Promoter®, Net Promoter Score®, and NPS® are trademarks of Satmetrix Systems, Inc., Bain &Company, Inc., and Fred Reichheld.

[2] Restated to reflect revised weightings for different channels - 31 December 2016 score on previous basis was +33. +34 (12 month average score, January to December 2016, based on interviews with 30,250 customers), +42 (six month average score, January to June 2017, based on interviews with 14,039 customers).

[3] KPMG Nunwood Customer Experience Excellence Annual Study for the UK financial services sector.

Chief Executive's summary continued...

Strategic update:

- Delivering the changes announced earlier in the year which include the withdrawal of our N&P brand for our retail customers, closure of the N&P current account, integration of N&P systems with other Group systems and closure and subsequent disposal of 48 branches across our network. These changes are being delivered through 2017 and 2018 and are intended to simplify and improve the efficiency of our business whilst aligning our engagement with our customers to their changing preferences. We are on track to deliver the changes as expected.
- Ongoing simplification of our savings product range whilst delivering an average interest rate on our savings products of 1.03% compared to the rest of the market at 0.75%[4].
- Our operational excellence programme continues to deliver improvements in our customer experience and efficiency. For example, improvements to our ISA transfer processes allowing for faster and more efficient transfers.
- Changes to our mortgage affordability criteria, making it easier for people to buy a home.
- Continued work towards achieving IRB advanced capital management status which, when implemented, will allow the Group to manage our credit risk and capital requirements more effectively.

> "Changes to our mortgage affordability criteria, making it easier for people to buy a home."

[4] Based upon CACI savings market data as at April 2017

Chief Executive's summary continued...

We are delighted that our customers and industry professionals continue to recognise our hard work as underlined by the number and calibre of awards that we have already won this year:

Award	Accolade
Moneynet Personal Finance Awards 2017	Best First Time Buyer Mortgage Provider
Moneynet Personal Finance Awards 2017	Best Offset Mortgage Provider
Moneynet Personal Finance Awards 2017	Best Fixed Rate Mortgage Provider
Moneyfacts Consumer Awards 2017	First-Time Mortgage Buyers' Choice
Process Network Excellence Awards 2017	Best Process Improvement Project Under 90 Days
Process Network Excellence Awards 2017	Best Start-up Business Process Improvement Programme Under 2 Years
PR Moment Awards 2017	Low budget campaign of the year - in-house
Mortgage Advice Bureau Awards 2017	The Relationship Award
Moneywise Mortgage Awards	Best lender for discounts
Moneywise Mortgage Awards	Best lender for first time buyers
2017 Moneyfacts Awards	Best Building Society Mortgage Provider
Recognising Excellence	Most Improved Lender

Our colleagues continue to play a key part in providing a great customer experience for our members and we are focused on creating an environment where our people are engaged, happy and committed.
I would like to thank all the people working for the Group for their ongoing support and commitment in helping us meet our goals.

Mike Regnier,
Chief Executive

Business Highlights

The focus of the Board for the first half of 2017 has been on:

Managing our mortgage and savings business and ensuring that volumes remain balanced and sustainable despite the continuing highly competitive environment and economic uncertainty.

Maintaining and refining our risk management framework to protect our customers and ensure our ongoing operational and financial sustainability.

Overseeing the progress of our project portfolio, in particular the elements of the portfolio that relate to regulatory requirements and to the changes in our branding, products and distribution.

Ensuring the ongoing development of our commercial strategy.

Delivering and continually enhancing exceptional customer service.

Ensuring that we maintain our capital and liquidity ratios above the regulatory minimums and at a level that is efficient and sustainable.

Continual management of our mortgage arrears performance and ensuring that we maintain appropriate levels of provisions.

Business Highlights continued...

Profit before tax was £92.3m for the six months to 30 June 2017 compared to £99.9m for the equivalent period in 2016.

In addition to monitoring profit before tax (a statutory measure) the Board uses core operating profit as a measure of underlying performance. This adjusts the pre-tax profit for non-core items, both positive and negative, that are considered one-off in nature or reflect a difference that will reverse over time.

Our core operating profit for the six months to 30 June 2017 was £84.2m against £62.5m in the same period in 2016. The table below explains the adjustments made to statutory profit to arrive at the core operating figure.

		Half-year ended 30 June 2017			Half-year ended 30 June 2016			Year ended 31 December 2016		
	NOTES	Statutory	Non-core items	Core	Statutory	Non-core items	Core	Statutory	Non-core items	Core
		£m	£m	£m	£m	£m	£m	£m	£m	£m
Net interest income	i)	**238.7**	**-**	**238.7**	235.5	(2.8)	232.7	475.6	(2.8)	472.8
Non-interest income (net)	ii)	**11.1**	**(5.3)**	**5.8**	26.1	(17.9)	8.2	36.3	(24.4)	11.9
Volatility on assets held at fair value	iii)	**5.7**	**(5.7)**	**-**	-	-	-	0.6	(0.6)	-
Fair value volatility on derivatives and hedging	iv)	**8.1**	**(8.1)**	**-**	25.0	(25.0)	-	0.3	(0.3)	-
Net realised profits		**9.7**	**-**	**9.7**	-	-	-	1.8	-	1.8
Total income		**273.3**	**(19.1)**	**254.2**	286.6	(45.7)	240.9	514.6	(28.1)	486.5
Management expenses		**(159.3)**	**-**	**(159.3)**	(172.3)	-	(172.3)	(346.0)	-	(346.0)
Operating profits before provisions		**114.0**	**(19.1)**	**94.9**	**114.3**	**(45.7)**	**68.6**	**168.6**	**(28.1)**	**140.5**
Impairment of loans and advances to customers		**3.0**	**-**	**3.0**	(1.5)	-	(1.5)	(0.1)	-	(0.1)
Other provisions	v)	**(24.7)**	**11.0**	**(13.7)**	(12.9)	8.3	(4.6)	(17.0)	4.6	(12.4)
Profit before tax		**92.3**	**(8.1)**	**84.2**	**99.9**	**(37.4)**	**62.5**	**151.5**	**(23.5)**	**128.0**

Notes - significant exclusions made in calculation of Core Operating Profit.

i) Release of fair value adjustments made against assets taken on during mergers.

ii) Proceeds from the sale of Vocalink shares (£3.2m) and profit on the sale of properties (£2.1m).

iii) Non-core investments.

iv) Fair value timing differences.

v) Financial Services Compensation Scheme levy (£2.5m) and restructuring costs (£8.5m) - see Note 6.

Business Highlights continued...

The main items in the income statement that contribute to profit:

- Net interest income of £238.7m (30 June 2016: £235.5m) representing a Net interest margin of 1.20% (30 June 2016: 1.21%). This is broadly in line with 2016 and is in line with our plans.
- Non-interest income decreased to £11.1m (30 June 2016: £26.1m). 2016 included £9.6m profit from property disposals and £8.3m in relation to the Group's shares in Visa Europe. 2017 is more reflective of the underlying run rate for non-interest income but does include £2.1m of profits from property disposals and £3.2m of income from Vocalink shares sold to Mastercard in H1.
- Fair value volatility of £13.8m (30 June 2016: £25.0m) is lower than 2016 when we saw significant Brexit impacts on some of our Euro denominated transactions. 2017 has seen a more stable position, with positive movements in the year largely reflecting the unwind of adverse movements in the past as the underlying transactions mature.
- Net realised profits of £9.7m (30 June 2016: Nil) reflect profits made on disposal of liquid asset investments in H1. These sales are largely made to prove the liquidity of assets held, and volatility in the gilt market through 2017 to date has resulted in profits being made.
- Management expenses reduced to £159.3m (30 June 2016: £172.3m) with a cost:income ratio of 58% (30 June 2016: 60%). The drivers for this are the timing of spend against our project portfolio in 2017, full year impacts of 2016 branch closure activities and a range of activities focused on managing cost and efficiency more closely in the organisation.
- Impairment provisions reflect a release of £3.0m (30 June 2016: charge of £1.5m), a reflection of the general quality of our mortgage books and positive house price inflation.
- The charge for provisions of £24.7m is higher than the equivalent period (30 June 2016: £12.9m); the key components being:
    - a reduction in the Financial Services Compensation Scheme (FSCS) charge level following announcements from the scheme over future expectations of charges;
    - increases in provisions for Payment Protection Insurance (PPI) to reflect higher levels of payouts in H1 extrapolated out to cover the remaining period;
    - an additional provision for Mortgage Payment Protection Insurance (MPPI) following announcements earlier in the year from the Financial Conduct Authority (FCA); and
    - a provision for restructuring costs as we reshape our business to a simpler, more efficient structure.

As a mutual we do not pay dividends to external shareholders so our profit requirements are driven solely by our need for ongoing capital. Our overall profit level remains sustainable and this interim result is in line with our growth given our commitment to remaining healthy and sustainable.

The Group's business activities are focused in the UK and relate predominantly to mortgage lending which is funded primarily through domestic deposits. We continue to have a cautious approach to liquidity management and as at 30 June 2017 our liquidity portfolio consisted almost entirely of exposures to the Bank of England and the UK Government.

Business Highlights continued...

The principal risks and uncertainties affecting the Group were reported on page 38 of the Annual Report and Accounts as at 31 December 2016 and are listed below. They continue to be the principal risks that affect the Group as at 30 June 2017.

Our approach to managing these risks is set out in the Risk Management Report on page 75 of our 2016 Annual Report and Accounts. In our planning for the rest of the year and beyond we will continue to regularly monitor the situation but, with the exception of the impacts deriving from the UK's decision to exit from the EU (which is discussed in our outlook section), we don't expect to see significant changes.

The main risks are:

Prudential – Credit Risk

- Retail credit risk
- Commercial credit risk
- Wholesale credit risk

Prudential – Financial Risk

- Balance sheet management risk
- Collateral and encumbrance risk
- Fair value volatility risk
- Liquidity and funding risk
- Market risk
- Model risk
- Pension risk
- Provisioning risk

Operational Risk

- Operational resilience
- Change risk
- Financial management, reporting and tax risk
- Fraud risk
- Information management risk
- Information security risk
- IT risk
- Payments risk
- People risk
- Premises risk
- Third party risk

Compliance and Conduct Risk

- Complaints and redress risk
- Customer treatment risk
- Financial crime risk
- Reward and remuneration risk
- Product governance risk
- Sales suitability risk

Business Risk

- Capital risk
- Also includes a broader set of risk measurements already included elsewhere in this list.

Business Highlights continued...

Outlook for 2017

We are in a period of political and economic uncertainty arising from the UK's decision to exit from the EU. This has created and will continue to create volatility in our markets, but managing volatility is a core part of what we do every day. The Group is well positioned with strong capital and liquidity positions and we are confident that we can continue to manage these risks as we run and build our business.

There is a level of uncertainty over the timing of the next rate increase in the UK with the market assumption moving regularly. Our approach to any future changes will continue to focus on managing changes as sympathetically as possible for our customers, whilst maintaining clear focus on safeguarding our financial strength and sustainability.

We will ensure that we monitor any further risks that emerge.

Changes to the Board

A complete list of the Board of Directors can be found in the 2016 Annual Report and Accounts which signposted the retirement of Dame Kate Barker and David Paige from the Board at the 2017 Annual General Meeting on 25 April 2017.

Following the AGM, Neeta Atkar was appointed as a non-executive director and Chair of the Risk Committee, replacing David Paige. A highly experienced risk professional, Neeta has almost 30 years' experience in financial services, having held a series of senior positions at both banks and insurance companies, starting her career at the Bank of England and then moving to the newly formed financial services regulator. Neeta has worked across all aspects of risk through her career, covering credit, operational, financial crime and regulatory risks. Most recently, she was the Chief Risk Officer at TSB. She is currently a non-executive director at the British Business Bank and Chair of its risk committee.

Signed on behalf of the Board by:

John Heaps, Chairman

Mike Regnier, Chief Executive

28 July 2017

Forward-looking statements

This Interim Management Report has been prepared solely to provide additional information to members to assess the Group's performance and strategies, and should not be relied on by any other party or for any other purpose. It contains certain forward-looking statements, which are made by the directors in good faith based on the information available to them up to the time of their approval of this report. Such statements should be treated with caution due to the inherent uncertainties, including both economic and business risk factors, underlying any such forward-looking information.

CONDENSED GROUP INCOME STATEMENT

	Notes	Half-year to 30 June 2017 (Unaudited) £m	Half-year to 30 June 2016 (Unaudited) £m	Year to 31 December 2016 (Audited) £m
Interest receivable and similar income		**533.9**	601.3	1,178.8
Interest payable and similar charges		**(295.2)**	(365.8)	(703.2)
Net interest income		**238.7**	235.5	475.6
Fees and commissions receivable		**16.5**	18.5	32.3
Fees and commissions payable		**(12.1)**	(11.8)	(23.4)
Net fee and commission income		**4.4**	6.7	8.9
Net gains from fair value volatility on financial instruments	2	**13.8**	25.0	0.9
Net realised profits	3	**9.7**	-	1.8
Other operating income	4	**6.7**	19.4	27.4
Total income		**273.3**	286.6	514.6
Administrative expenses		**(146.6)**	(161.2)	(323.3)
Depreciation and amortisation		**(12.7)**	(11.1)	(22.7)
Operating profit before provisions		**114.0**	114.3	168.6
Impairment of loans and advances to customers	5	**3.0**	(1.5)	(0.1)
Provisions	6	**(24.7)**	(12.9)	(17.0)
Profit before tax		**92.3**	99.9	151.5
Tax expense	7	**(23.3)**	(24.2)	(37.3)
Net profit		**69.0**	**75.7**	**114.2**

CONDENSED GROUP STATEMENT OF COMPREHENSIVE INCOME

	Notes	Half-year to 30 June 2017 (Unaudited) £m	Half-year to 30 June 2016 (Unaudited) £m	Year to 31 December 2016 (Audited) £m
Net profit		**69.0**	75.7	114.2
Items that will subsequently be reclassified to profit and loss: Available for sale investments:				
Valuation gains taken to equity		**12.1**	8.7	9.0
Amounts transferred to income statement		**(13.6)**	-	(0.7)
Tax on available for sale securities	7	**0.4**	(2.2)	(2.3)
Effect of change in corporation tax rate	7	**-**	-	0.3
Cash flow hedges:				
Gains/(losses) taken to equity		**3.9**	(31.1)	(25.7)
Amounts transferred to income statement		**(0.5)**	7.0	46.0
Tax on cash flow hedge reserve	7	**(0.9)**	6.4	(5.7)
Effect of change in corporation tax rate	7	**-**	-	0.3
Items that will not subsequently be reclassified to profit and loss:				
Remeasurement of net retirement benefit obligations	8	**(32.1)**	25.3	(27.0)
Tax relating to retirement benefit obligations	7	**8.1**	(6.7)	7.6
Total comprehensive income for the period		**46.4**	**83.1**	**116.0**

CONDENSED GROUP STATEMENT OF FINANCIAL POSITION

	Notes	30 June 2017 (Unaudited) £m	30 June 2016 (Unaudited) £m	31 December 2016 (Audited) £m
ASSETS				
Liquid Assets				
Cash in hand and balances with the Bank of England		**4,111.1**	3,550.4	3,525.0
Loans and advances to credit institutions		**432.2**	661.6	542.8
Debt securities		**454.9**	505.5	608.1
Loans and advances to customers		**34,038.5**	33,996.8	34,103.3
Derivative financial instruments		**573.2**	525.3	540.5
Investments		**5.1**	5.9	10.3
Intangible assets		**30.2**	34.8	34.1
Investment properties		**12.2**	15.2	15.0
Property, plant and equipment		**120.1**	132.6	129.3
Deferred tax assets	7	**10.5**	34.0	16.3
Retirement benefit surplus	8	**13.7**	92.7	42.0
Other assets		**35.0**	35.0	28.8
Total assets		**39,836.7**	**39,589.8**	**39,595.5**
LIABILITIES				
Shares		**28,440.0**	28,979.9	28,693.2
Amounts owed to credit institutions		**3,334.0**	2,925.9	3,120.8
Other deposits		**419.3**	463.6	434.7
Debt securities in issue		**4,695.8**	4,078.8	4,361.4
Derivative financial instruments		**261.7**	509.8	348.0
Current tax liabilities	7	**15.4**	21.0	12.8
Deferred tax liabilities	7	**8.5**	28.8	16.2
Other liabilities		**41.8**	45.7	54.7
Provisions		**45.9**	36.6	29.1
Subordinated liabilities		**300.4**	304.9	297.0
Subscribed capital		**6.6**	6.8	6.7
Total liabilities		**37,569.4**	**37,401.8**	**37,374.6**
Total equity attributable to members		**2,267.3**	2,188.0	2,220.9
Total liabilities and equity		**39,836.7**	**39,589.8**	**39,595.5**

CONDENSED GROUP STATEMENT OF CHANGES IN MEMBERS' INTEREST

	General reserve	Hedging reserve	Available for sale reserve	Total reserves
	£m	£m	£m	£m
HALF-YEAR TO 30 JUNE 2017				
At 1 January 2017 (Audited)	2,220.9	(8.1)	8.1	2,220.9
Current period movement net of tax	45.0	2.5	(1.1)	46.4
At 30 June 2017 (Unaudited)	2,265.9	(5.6)	7.0	2,267.3
HALF-YEAR TO 30 JUNE 2016				
At 1 January 2016 (Audited)	2,123.0	(23.0)	4.9	2,104.9
Current period movement net of tax	94.5	(17.9)	6.5	83.1
At 30 June 2016 (Unaudited)	2,217.5	(40.9)	11.4	2,188.0
YEAR TO 31 DECEMBER 2016				
At 1 January 2016 (Audited)	2,123.0	(23.0)	4.9	2,104.9
Reallocation of tax	3.0	–	(3.0)	–
Current period movement net of tax	94.9	14.9	6.2	116.0
At 31 December 2016 (Audited)	2,220.9	(8.1)	8.1	2,220.9

CONDENSED GROUP STATEMENT OF CASH FLOWS

	Notes	Half-year to 30 June 2017 (Unaudited) £m	Half-year to 30 June 2016 (Unaudited) £m	Year to 31 December 2016 (Audited) £m
CASH FLOWS FROM OPERATING ACTIVITIES:				
Profit before tax		92.3	99.9	151.5
Working capital adjustments	10	3.3	(3.3)	7.0
Net increase in operating assets	10	(34.3)	(567.2)	(766.8)
Net (decrease)/increase in operating liabilities	10	(55.4)	1,126.3	1,005.6
Taxation paid		(15.1)	(7.1)	(20.7)
Net cash flows (used in)/from operating activities		**(9.2)**	**648.6**	**376.6**
CASH FLOWS FROM INVESTING ACTIVITIES:				
Purchase of property, plant and equipment and intangible assets		(1.5)	(7.4)	(17.8)
Proceeds from sale of property, plant and equipment		6.8	15.0	20.4
Purchase of debt securities		(474.4)	(206.5)	(502.4)
Proceeds from sale and redemption of debt securities		635.9	(20.8)	173.9
Net cash flows from/(used in) investing activities		**166.8**	**(219.7)**	**(325.9)**
CASH FLOWS FROM FINANCING ACTIVITIES:				
Redemption of securities		(100.7)	(744.3)	(804.3)
Issue of securities	10	426.7	400.0	700.0
Interest paid on subordinated liabilities and subscribed capital		(8.0)	(8.0)	(16.0)
Net cash flows from/(used in) financing activities		**318.0**	**(352.3)**	**(120.3)**
Net increase/ (decrease) in cash and cash equivalents		**475.6**	**76.6**	**(69.6)**
Opening balance		4,016.2	4,085.8	4,085.8
Total closing cash and cash equivalents		**4,491.8**	**4,162.4**	**4,016.2**
CASH AND CASH EQUIVALENTS:				
Cash and balances with central banks		4,059.6	3,500.8	3,473.4
Loans and advances to credit institutions		432.2	661.6	542.8
		4,491.8	4,162.4	4,016.2

Notes to the accounts

1. Introduction

Reporting period

The financial statements show the financial performance of the Group for the half-year ended 30 June 2017.

Basis of preparation

These Interim Group Accounts have been prepared in accordance with International Accounting Standard (IAS) 34 'Interim Financial Reporting'. The accounting policies, presentation and methods of computation are consistent with those applied by the Group in its latest audited annual financial statements, which were prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU.

Going concern

The Board undertakes regular rigorous assessments of whether the Group is a going concern in light of current economic and market conditions and all available information about future risks and uncertainties. Details of the review undertaken in February 2017 are given on page 45 of the 2016 Annual Report and Accounts.

The directors confirm, based on the latest formal review undertaken in July 2017, that they consider the Group has adequate resources to continue in existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing these financial statements.

Accounting developments

The information on future accounting developments and their potential effect on the financial statements are provided on pages 108 and 109 of the 2016 Annual Report and Accounts. The Group's implementation project for IFRS 9 has continued development of the necessary impairment models and processes with the first parallel run completed for the retail mortgage portfolios during June 2017. Until the models have been sufficiently tested for multiple dates and input assumptions to enable a reliable understanding of the calculated IFRS 9 impairment provision, the Group is not able to disclose a potential impact on the financial statements and any consequential effects of regulatory capital requirements.

2. Net gains from fair value volatility on financial instruments

	Half-year to 30 June 2017 (Unaudited)	Half-year to 30 June 2016 (Unaudited)	Year to 31 December 2016 (Audited)
	£m	£m	£m
Derivatives and hedging	**8.1**	25.0	0.3
Other items	**5.7**	-	0.6
	13.8	25.0	0.9

Derivatives and hedging

Fair value volatility on derivatives and hedging relates to changes in the fair value of derivatives that provide effective economic hedges but where the Group has either not achieved hedge accounting or the nature of the hedge relationship has given rise to ineffectiveness. The £8.1m profit in the current period is predominantly due to adverse movements on interest rate swaps in the past that have unwound as the underlying transactions mature.

Embedded derivatives

The £5.7m profit for the current period relates to the realised gain on the maturity of a structured credit investment.

Notes to the accounts continued...

3. Net realised profits

These relate to the disposal of available for sale assets. Profits or losses of this nature are variable as they primarily arise from the Group's objective to regularly transact in the market in order to prove the liquidity of its portfolio of buffer liquid assets.

4. Other operating income

Other income for the period to 30 June 2017 includes £3.2m received in respect of the Group's interest in Vocalink, which was purchased by Mastercard on 2 May 2017.
In addition, the Group realised profits of £2.1m on the disposal of property.

5. Impairment of loans and advances to customers

There have been no significant changes to our approach to provisioning since 31 December 2016.

The Group continues to use forbearance to assist borrowers facing difficulties, balancing the best interests of the Group with those of the individual, where there is a realistic prospect of a borrower's circumstances improving within the foreseeable future. There has been no material change to the extent and makeup of forbearance which is described on page 169 of the 2016 Annual Report and Accounts.

6. Provisions

The provisions charge for the period is outlined below:

	Half-year to 30 June 2017 (Unaudited)	Half-year to 30 June 2016 (Unaudited)	Year to 31 December 2016 (Audited)
	£m	£m	£m
FSCS levy	**2.5**	8.3	4.5
Customer redress and conduct issues	**12.2**	8.8	15.6
Other	**10.0**	(4.2)	(3.1)
	24.7	12.9	17.0

Financial Services Compensation Scheme (FSCS) levy

The FSCS reimburses depositors when institutions fail using loans from HM Treasury, which are subsequently recovered from the failed institutions. Any shortfall in this recovery is levied on member firms, along with the interest costs on the loans.

The £2.5m provision charge for the current period relates predominantly to interest for the scheme year 2017/18. The charge is lower than prior years as a result of the announced sale by Bradford & Bingley of certain mortgage assets leading to a significant reduction in the amount borrowed by FSCS from HM Treasury.

Customer redress and conduct issues

Provisions are held in respect of various potential customer claims and represent management's best estimate of the likely costs. A charge of £12.6m was made for PPI claims, based on estimated future claims volumes, uphold rates and average cost and reflects the expected impact of the FCA's recent policy statement highlighting a communication campaign to consumers and a longer time period in which claims can be submitted.

Other provisions

The £10.0m provision charge for the current period predominantly relates to £8.5m of restructuring costs expected to be paid as a result of business and organisational changes announced during the first six months of 2017.

Notes to the accounts continued...

7. Taxation

An effective tax rate of 21.65% has been applied to the Group's profit. This is higher than the standard corporation tax rate in the year of 19.25% due to non tax-deductible expenses.

A surcharge of 8% on the profits of banking companies (including building societies) was introduced on 1 January 2016. This has increased the tax charge and is reflected in the tax balances.

The main rate of corporation tax will reduce from 19% to 17% from 1 April 2020. These rate changes are reflected in the deferred tax balances in these accounts.

8. Retirement benefit obligations

	At 1 January 2017 (Audited)	Movements	At 30 June 2017 (Unaudited)
	£m	£m	£m
Present value of defined benefit obligation	(949.3)	(6.9)	(956.2)
Assets at fair value	991.3	(21.4)	969.9
Funded status/defined benefit asset	**42.0**	**(28.3)**	**13.7**

The present value of the defined benefit obligation as at 30 June 2017 has been derived using assumptions that are consistent with those used for the 31 December 2016.

Corporate bond yields have remained low over the first half of 2017; this has led to a lower discount rate assumption and increasing liabilities. This has been partially offset by a decrease in future expectations of long term inflation. In addition, a significant amount of benefits have been transferred out of the Scheme over the first half of the year, decreasing both liabilities and net assets (cash).

The fall in the value of the pension fund in the first six months of 2017 contrasts with the increase in its value in the corresponding period in 2016. The latter, as stated in the 2016 Interim Accounts, was driven by material falls in bond and gilts yields following the result of the EU referendum in June 2016 which led to lower discount rates and consequently significantly higher valuations of both assets and liabilities.

9. Related parties

The Society has an investment in Arkose Funding Limited. In 2014, a loan of £4.0m to Arkose Funding Limited was fully impaired.

The Group has a related party relationship with Sesame Bankhall Group Limited (SBG) as Alison Hutchinson is a non-executive director of an indirect parent company of SBG, Aviva Life Holdings UK Limited. SBG is a lending partner of Accord Mortgages Limited, a subsidiary of the Society and a Lead Panel Valuer for the Group. During the period Accord Mortgages Limited paid commission of £1.5m to SBG, in relation to lending completed via their network of independent financial advisers.

As at 30 June 2017 an amount of £1.4m is outstanding between the two companies relating to fees for property valuation reports in respect of mortgage applications. Transactions are made on an arm's length basis.

The Group also has a related party relationship with Aviva Insurance Limited, as Mark Pain, Vice Chairman, is a non-executive director of this company. The Group historically sold insurance products provided by Aviva Insurance Limited, the income from these sales during the period was £0.3m.

Transactions for this period are similar to those for the year to 31 December 2016, details of which can be found in the 2016 Annual Report and Accounts.

Notes to the accounts continued...

10. Notes to the condensed group statement of cash flows

	Half-year to 30 June 2017 (Unaudited)	Half-year to 30 June 2016 (Unaudited)	Year to 31 December 2016 (Audited)
	£m	£m	£m
WORKING CAPITAL ADJUSTMENTS:			
Depreciation and amortisation	12.7	11.1	22.7
Profit on sale of assets	(2.1)	(9.6)	(11.8)
Interest on subordinated liabilities and subscribed capital	8.0	8.0	16.0
Provisions	21.7	14.4	17.1
Fair value of subordinated liabilities and subscribed capital	3.3	18.9	10.9
Net realised profits	(9.7)	-	(1.8)
Increase in other assets	(9.8)	(12.1)	(9.5)
Decrease in other liabilities	(20.8)	(34.0)	(36.6)
Working capital adjustments	**3.3**	**(3.3)**	**7.0**
(INCREASE)/DECREASE IN OPERATING ASSETS:			
Loans and advances to customers	67.8	(676.6)	(781.7)
Investments	5.2	(4.5)	(8.9)
Derivative financial instruments	(107.3)	113.9	23.8
Net increase in operating assets	**(34.3)**	**(567.2)**	**(766.8)**
INCREASE/(DECREASE) IN OPERATING LIABILITIES:			
Shares	(253.2)	1,583.5	1,296.8
Amounts owed to credit institutions	213.2	(376.5)	(181.6)
Other deposits	(15.4)	(80.7)	(109.6)
Net (decrease)/increase in operating liabilities	**(55.4)**	**1,126.3**	**1,005.6**

Issue of securities

During the period, the Group issued €500m (£426.7m) of six year covered bonds.

Cash and balances with central banks

Cash and balances with central banks excludes cash ratio deposits of £51.5m held with the Bank of England, which are not available for use in the Group's day-to-day operations.

Notes to the accounts continued...

11. Segmental reporting

This section analyses the Group's performance by business segment.

The chief operating decision maker has been identified as the Board, which reviews the Group's internal reporting and is responsible for all significant decisions. The Group's reportable segments under IFRS 8 'Operating Segments', based on the information reviewed by the Board, have been determined according to similar economic characteristics and the nature of the products and services. Details of the reportable segments are listed below:

Segment	Description	Basis of aggregation
Retail	Prime residential owner occupied lending, prime intermediary lending and non-owner occupied lending. Traditional member savings, non-traditional savings and sale of general insurance, protection and investment products provided by third parties.	These are the core activities and focus of the Group.
Non-retail	Prime commercial lending portfolio (including social housing).	These ongoing parts of the business support the Group's financial stability and primary businesses but are not considered core and have a non-retail customer base.
Secondary	Non-prime residential owner occupied lending, consumer banking, personal lending, non-prime commercial lending and non-owner occupied lending acquired through mergers.	These elements, originated and acquired through merger, are closed to new business and are historic areas in which the Group no longer operates.
Central	Supporting business units, the Treasury function and other head office group functions which have not been apportioned across the aforementioned segments.	These operations are not directly customer related.

No segmental information is presented on geographical lines, because substantially all of the Group's activities are in the United Kingdom.

The majority of the Group's revenues are in the form of interest and the Board monitors the Group's net interest income, to assess performance and direct the Group. Therefore, interest receivable and similar income has been shown net of interest payable and similar expense.

Recharging of funding across the Group has been included using the Group's internal funds transfer pricing methodology, which includes the cost of raising external funds.

Income and directly attributable costs have been allocated to each segment as applicable, with support costs being apportioned based on levels of employees.

The accounting policies for the reported segments are consistent with the Group's accounting policies outlined in Note 1 of the 2016 Annual Report and Accounts.

Notes to the accounts continued...

11. Segmental reporting continued...

HALF-YEAR TO 30 JUNE 2017 (UNAUDITED)		Retail	Non-retail	Secondary	Central	Total
	Notes	£m	£m	£m	£m	£m
Net interest income		168.4	10.3	11.7	48.3	238.7
Non-interest income (net)	a	10.7	-	-	0.4	11.1
Net realised profits and fair value		-	-	-	23.5	23.5
Management expenses	b	(101.0)	(1.3)	(0.9)	(56.1)	(159.3)
Operating profit before provisions		78.1	9.0	10.8	16.1	114.0
Impairment and other provisions		(0.7)	-	0.1	(21.1)	(21.7)
Profit before tax		77.4	9.0	10.9	(5.0)	92.3
Total assets		32,189.3	1,047.6	769.3	5,830.5	39,836.7
Total liabilities		29,041.6	-	-	8,527.8	37,569.4
Total equity attributable to members		-	-	-	2,267.3	2,267.3

Notes

a) Non-interest income (net) includes fees and commissions receivable, fees and commissions payable and other operating income.

b) Management expenses include administrative expenses, depreciation and amortisation.

Notes to the accounts continued...

11. Segmental reporting continued...

HALF YEAR TO 30 JUNE 2016 (UNAUDITED)	Notes	Retail	Non-retail	Secondary	Central	Total
		£m	£m	£m	£m	£m
Net interest income		146.5	8.3	13.5	67.2	235.5
Non-interest income (net)	a	13.2	-	-	12.9	26.1
Net realised profits and fair value		-	-	-	25.0	25.0
Management expenses	b	(103.7)	(1.1)	(1.0)	(66.5)	(172.3)
Operating profit before provisions		**56.0**	**7.2**	**12.5**	**38.6**	**114.3**
Impairment and other provisions		(9.7)	-	0.1	(4.8)	(14.4)
Profit before tax		**46.3**	**7.2**	**12.6**	**33.8**	**99.9**
Total assets		**31,944.5**	**960.9**	**876.8**	**5,807.6**	**39,589.8**
Total liabilities		**29.681.8**	**-**	**-**	**7,720.0**	**37,401.8**
Total equity attributable to members		**-**	**-**	**-**	**2,188.0**	**2,188.0**

YEAR TO 31 DECEMBER 2016 (AUDITED)	Notes	Retail	Non-retail	Secondary	Central	Total
		£m	£m	£m	£m	£m
Net interest income		301.1	18.9	28.8	126.8	475.6
Non-interest income (net)	a	22.4	-	-	13.9	36.3
Net realised profits and fair value		-	-	-	2.7	2.7
Management expenses	b	(208.9)	(2.5)	(2.0)	(132.6)	(346.0)
Operating profit before provisions		**114.6**	**16.4**	**26.8**	**10.8**	**168.6**
Impairment and other provisions		(7.1)	-	1.2	(11.2)	(17.1)
Profit/(loss) before tax		**107.5**	**16.4**	**28.0**	**(0.4)**	**151.5**
Total assets		**32,139.0**	**1,025.3**	**824.2**	**5,607.0**	**39,595.5**
Total liabilities		**29,354.5**	**-**	**-**	**8,020.1**	**37,374.6**
Total equity attributable to members		**-**	**-**	**-**	**2,220.9**	**2,220.9**

Notes

a) Non-interest income (net) includes fees and commissions receivable, fees and commissions payable, and other operating income.

b) Management expenses include administrative expenses, depreciation and amortisation.

Notes to the accounts continued...

11. Segmental reporting continued...

Total income for the reportable segments can be analysed as follows:

HALF-YEAR TO 30 JUNE 2017 (UNAUDITED)	Retail	Non-retail	Secondary	Central	Total
	£m	£m	£m	£m	£m
External income	**311.0**	**17.8**	**17.5**	**(96.5)**	**249.8**
Income from other segments	**(131.9)**	**(7.5)**	**(5.8)**	**145.2**	**-**
Total income	**179.1**	**10.3**	**11.7**	**48.7**	**249.8**

HALF-YEAR TO 30 JUNE 2016 (UNAUDITED)	Retail	Non-retail	Secondary	Central	Total
	£m	£m	£m	£m	£m
External income	309.6	16.4	21.5	(85.9)	261.6
Income from other segments	(149.9)	(8.1)	(8.0)	166.0	-
Total income	**159.7**	**8.3**	**13.5**	**80.1**	**261.6**

YEAR TO 31 DECEMBER 2016 (AUDITED)	Retail	Non-retail	Secondary	Central	Total
	£m	£m	£m	£m	£m
External income	620.5	35.1	43.6	(187.3)	511.9
Income from other segments	(297.0)	(16.2)	(14.8)	328.0	-
Total income	**323.5**	**18.9**	**28.8**	**140.7**	**511.9**

Notes to the accounts continued...

12. Fair values

Fair value is the price that would be received on the sale of an asset or the price paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Where external market prices are available they have been used to determine fair value. Otherwise, internal pricing models using external market data have been used. The Group measures fair value using the following fair value hierarchy:

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

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The table below summarises the carrying value and fair value of financial assets and liabilities measured at amortised cost as at the Statement of Financial Position date.

AT 30 JUNE 2017 (UNAUDITED)	Carrying value	Level 1	Fair Values Level 2	Level 3	Total Fair Value
	£m	£m	£m	£m	£m
ASSETS:					
Cash in hand and balances with the Bank of England	4,111.1	-	4,111.1	-	4,111.1
Loans and advances to credit institutions	432.2	-	432.2	-	432.2
Loans and advances to customers	34,038.5	-	34,664.3	-	34,664.3
LIABILITIES:					
Shares	28,440.0	-	28,425.1	-	28,425.1
Amounts due to credit institutions	3,334.0	-	3,334.0	-	3,334.0
Other deposits	419.3	-	419.3	-	419.3
Debt securities in issue	4,695.8	-	4,791.0	-	4,791.0
Subordinated liabilities	300.4	-	316.0	-	316.0
Subscribed capital	6.6	-	6.2	-	6.2

Notes to the accounts continued...

12. Fair values continued...

AT 31 DECEMBER 2016 (AUDITED)	Carrying value	Level 1	Fair Values Level 2	Level 3	Total Fair Value
	£m	£m	£m	£m	£m
ASSETS:					
Cash in hand and balances with the Bank of England	3,525.0	-	3,525.0	-	3,525.0
Loans and advances to credit institutions	542.8	-	542.8	-	542.8
Loans and advances to customers	34,103.3	-	34,698.9	-	34,698.9
LIABILITIES:					
Shares	28,693.2	-	28,641.2	-	28,641.2
Amounts due to credit institutions	3,120.8	-	3,120.8	-	3,120.8
Other deposits	434.7	-	434.7	-	434.7
Debt securities in issue	4,361.4	-	4,421.8	-	4,421.8
Subordinated liabilities	297.0	-	305.1	-	305.1
Subscribed capital	6.7	-	6.0	-	6.0

The table below classifies all financial instruments held at fair value according to the method used to establish the fair value.

AS AT 30 JUNE 2017 (UNAUDITED)	Level 1	Level 2	Level 3	Total
	£m	£m	£m	£m
ASSETS:				
Debt securities – fair value	**-**	**-**	**4.2**	**4.2**
Embedded derivatives	**-**	**-**	**-**	**-**
Debt securities – available for sale	**447.3**	**3.4**	**-**	**450.7**
Derivative financial instruments	**-**	**528.0**	**45.2**	**573.2**
Investments	**-**	**-**	**5.1**	**5.1**
LIABILITIES:				
Derivative financial instruments	**-**	**250.8**	**10.9**	**261.7**

Notes to the accounts continued...

12. Fair values continued...

AS AT 31 DECEMBER 2016 (AUDITED)	Level 1	Level 2	Level 3	Total
	£m	£m	£m	£m
ASSETS:				
Debt securities – fair value	-	-	7.6	7.6
Embedded derivatives	-	-	(8.9)	(8.9)
Debt securities – available for sale	560.5	3.5	45.4	609.4
Derivative financial instruments	-	486.6	53.9	540.5
Investments	-	-	10.3	10.3
LIABILITIES:				
Derivative financial instruments	-	329.8	18.2	348.0

The following table analyses movements in the Level 3 portfolio:

	As at 1 January 2017 (Audited)	Items recognised in the income statement	Net repayments in the period	Transfers into/(out of) Level 3 portfolio	As at 30 June 2017 (Unaudited)
	£m	£m	£m	£m	£m
ASSETS:					
Debt securities – fair value	7.6	-	(3.4)	-	4.2
Embedded derivatives	(8.9)	5.7	3.2	-	-
Debt securities – available for sale	45.4	-	(45.4)	-	-
Derivative financial instruments	53.9	(0.4)	(8.3)	-	45.2
Investments	10.3	-	(5.2)	-	5.1
LIABILITIES:					
Derivative financial instruments	18.2	(3.7)	(3.6)	-	10.9

Details of valuation techniques are disclosed on page 174 of the 2016 Annual Report and Accounts.

There have been no other transfers of assets or liabilities between the levels of the fair value hierarchy during the period.

Responsibility statement

We confirm that to the best of our knowledge, the condensed set of financial statements has been prepared in accordance with International Accounting Standard 34 'Interim Financial Reporting'; the interim report includes a fair review of the information required by DTR 4.2.7R (indication of important events during the first six months and description of principal risks and uncertainties for the remaining six months of the year); and the interim report includes a fair review of the information required by DTR 4.2.8R (disclosure of related parties' transactions and changes therein).

By order of the Board

John Heaps
Chairman

Robin Churchouse
Finance Director

28 July 2017

Independent review report to Yorkshire Building Society

We have been engaged by the Society to review the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2017 which comprises the Income statement, the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Changes in Members' Interest, the Statement of Cash Flows and related notes 1 to 12. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Society in accordance with International Standard on Review Engagements (UK and Ireland) 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Auditing Practices Board. Our work has been undertaken so that we might state to the Society those matters we are required to state to it in an independent review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company, for our review work, for this report, or for the conclusions we have formed.

Directors' responsibilities

The half-yearly financial report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the half-yearly financial report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

As disclosed in note 1, the annual financial statements of the group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with International Accounting Standard 34 "Interim Financial Reporting" as adopted by the European Union.

Our responsibility

Our responsibility is to express to the Society a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2017 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Deloitte LLP

Statutory Auditor

Leeds, United Kingdom

28 July 2017

Other information

The interim management report information set out in this document is unaudited and does not constitute accounts within the meaning of section 73 of the Building Societies Act 1986. The financial information for the year ended 31 December 2016 has been extracted from the Annual Accounts for that year. The Annual Accounts for the year ended 31 December 2016 have been filed with the Financial Conduct Authority.

The Auditor's report on the Annual Accounts was unqualified and did not include any matters to which the Auditor drew attention by way of emphasis without qualifying their report.

A copy of the interim management report is placed on Yorkshire Building Society's website. The directors are responsible for the maintenance and integrity of the information on the website. Information published on the internet is accessible in many countries with different legal requirements. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

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YBS GROUP