Chief Executive's report

Iain Cornish

Our vision and strategy

Our vision is "to be the best organisation that our customers do business with".

We aim to achieve our vision by providing our members and customers with financial security and long-term value across a comprehensive range of mortgage, savings, investment, insurance and share plan products backed up with excellent personal service.

Our members tell us that they support us in our ambition; 9 out of 10 respondents to our regular customer surveys tell us that they would recommend us to their family or friends.

Our strategic priorities represent the areas in which the Society is investing additional resources because they are the things that will provide the most significant contribution to the achievement of our vision, and include:

- delivering an exceptional customer experience across all of our brands and distribution channels, building on our already strong position;
- maintaining a high level of financial strength and stability. This includes offering interest rates which are attractive, but crucially are also sustainable, maintaining a strong funding position and cost efficiency combined with effective risk management and corporate governance;
- ensuring our people are well trained, fairly rewarded and committed to delivering for our members;
- continually improving our administrative processes and systems; and
- looking ahead and seizing opportunities; innovating to improve delivery of benefits to members and, in the right circumstances, taking further opportunities to grow by merging with smaller societies.

For many decades the Yorkshire has been run with the interests of current and future members very clearly at its heart. The vast majority of the Society's activities have been centred on lending to people to allow them to own their own homes, funded largely by the savings of individual members. A great deal of our business continues to be delivered face to face through our expanding branch network.

The cautious approach we have adopted through the worst financial and economic crisis in a generation has left us in an extremely strong position to move ahead and meet the desire of consumers for a trusted provider who puts their interests first. This approach does not mean we are stuck in the past. We have rapidly expanded our internet and telephone-based services. We have also taken opportunities to develop the Group, for example, in the last three years we have merged with the Barnsley Building Society and the Chelsea Building Society. In both cases we have deliberately chosen to retain their brands and also their branch networks, because we believe they are valued by their members and because it enables the Group to reach the broadest possible membership and offer customers the widest range of products and services, as well as providing them with real choice in how they do business with us.

Financial strength

We are pleased to be able to report a strong set of results for 2010 which have enhanced the resilience of the Society. This was delivered against a background of continued weakness in the UK economy and the housing market; and during a year which combined significant "business as usual" challenges with the challenge of integrating Chelsea Building Society into the Yorkshire's operation.

The highlights of the Society's performance include:

- return to profitability; statutory operating profit £115m (2009: £12m loss) and core operating profit (see table below) of £128m (2009: £8m), representing a continuation of the trend reported at 30 June 2010;

Core operating profit

In addition to statutory profit before tax, the Board uses core operating profit to monitor the Group's performance. This is because the statutory figure includes a number of items that the Board believes do not reflect the longer-term, sustainable business performance either because they are pure accounting measures (e.g. negative goodwill), are one-off in nature (e.g. integration costs) or are timing differences that reverse over time (e.g. fair value adjustments).

	2010 £m	2009 £m
Statutory profit before tax	**115**	**(12)**
Reverse out the following items:		
Fair value movements	10	10
Sale of assets/Other income	1	1
Non core provisions:		
a) Structured credit	5	1
b) FSCS	4	3
c) Other liabilities	-	(2)
Negative goodwill	(17)	-
Merger costs	10	7
Core operating profit	**128**	**8**

- net interest margin restored; 1.03% (2009: 0.65%);
- increased total assets; total assets increased year on year by 32% to £30.1bn (31 December 2009: £22.7bn) as a result of the Chelsea merger;
- increased members' balances; retail savings increased by 55% to £21.4bn (31 December 2009: £13.8bn);
- capital strength; core tier 1 capital ratio 12.4% (31 December 2009: 12.2%) re-built to pre-merger levels following the reduction that initially occurred as a result of the merger. This has been delivered well ahead of plan;
- continued to hold prudent levels of liquidity; group liquidity 21.1% (31 December 2009: 31.9%), as the intentionally held pre-merger "excess" was managed down in line with the reduced requirements of the enlarged Group;
- maintained asset quality; the percentage of loans over three months in arrears by volume was stable at 1.84% (31 December 2009: 1.84%);
- wholesale funding; the issuance of a □600m five year covered bond in September supporting our balanced funding strategy;
- performance of the Chelsea brand ahead of expectations; delivery of planned merger synergies and integration well advanced;
- on a like-for-like basis achieved a management expenses ratio of 0.51% after adjusting for the impact of the merger (31 December 2009: 0.54%); and
- improved ratings position; ratings agency Standard & Poors revised its outlook on the Society from "negative" to "stable" in November in recognition of the progress made in managing our integration of Chelsea and the expected improvement in our financial position.

The financial performance and the strong delivery against our other strategic priorities combined to significantly improve the Society's position and its long-term capacity to prosper and deliver benefits to members in the future.

Chief Executive's report cont.

The Society's financial performance and position are explained in detail in the Business review which can be downloaded from our website www.ybs.co.uk/annualreport. Alternatively a full copy of the Annual Report and Accounts can be obtained from any branch, on our website www.ybs.co.uk/annualreport or by calling the AGM Helpline number quoted on the Chairman's letter.

Members

As a mutual organisation, the Yorkshire is owned by, and run for, the benefit of our current and future members and not on behalf of external shareholders. Last year was not easy for either borrowers or savers and the Society has remained very focussed on doing what it can to help its members through this difficult environment. Whilst we clearly are operating within the constraints of a fragile economy and historically low interest rates, I believe we made good progress in 2010.

Savings

In such challenging times for savers, who have seen returns fall dramatically as a result of the record-low Bank of England base rate of interest, we have offered consistent returns. For example, at the end of 2010 the Group's average interest rate on cash ISAs was 2.21%, more than five times as high as the market average rate of 0.40%[1].

The Society provided protection to our investing members by doing our best to shelter them from the full effects of the low base rate. In late 2010 independent consumer body Which? found that in the market as a whole 1 in 4 savings accounts and cash ISAs paid 0.10% or less in annual interest[2]. In contrast, fewer than 1 in 12 accounts offered by the Society paid 0.10% or less in annual interest.

Unlike a number of our competitors, during 2010 the Group did not cut the rate of interest payable on any of its variable rate savings products, including Chelsea products following the merger.

The range of structured deposits, "Protected Capital Accounts", offered in association with Credit Suisse, have been extremely popular with customers who do not wish to significantly deviate from the returns they would realise with a deposit savings account. These products offer a potential return above that possible from the traditional deposit account market, and with limited "down-side" risk. The products have been designed for customers who place importance on the capital protection and minimum return elements of a savings product but are willing to sacrifice an element of this minimum return in favour of potential additional returns.

A significant distinction between our approach and that in the wider market is that we position our savings products primarily to offer long-term value to savers. As such we do not adopt the tactic of repeatedly promoting headline-grabbing rates based on small print, or only to subsequently aggressively cut rates. Our approach once again proved attractive to members and in 2010 we opened over 270,000 new savings accounts across our Yorkshire, Barnsley and Chelsea Building Society brands. Notwithstanding this approach, our savings accounts attracted over 900 "Best Buy" mentions during the year.

Following our merger we developed and launched the Chelsea savings internet channel. This means that Chelsea customers now benefit from being able to open and manage a range of savings products online for the first time, including e-Saver Reward, e-bonds and a Fixed Rate e-ISA. We also enhanced the range of savings products available through Barnsley Building Society branches, with the addition of Monthly Reward ISA, Rollover Bond and a Fixed Rate Anniversary ISA.

In addition to offering attractive interest rates on savings products we won the Moneywise "Best Cash ISA Service Provider" award in 2010 in recognition of our excellent service.

Mortgages

We remained committed to providing people with competitive mortgage products, allowing them access to the housing market. Our approach to the mortgage market was in part illustrated by the fact that we received the highest number of "Best Buy" mentions of any mortgage provider in 2010.

Our existing borrowing members' interests were also prioritised as we ensured that all borrowers were offered fixed rate mortgage products at the end of their existing mortgage deals which provide protection against possible interest rate rises in 2011 and beyond.

The Yorkshire assisted first time buyers by offering our unique "Offset Plus" product which allows borrowers to link the savings of family or friends to their mortgage, thereby reducing mortgage interest payments while at the same time giving family or friends full control over their savings. Further support has been provided to borrowers typically on the early rungs of the housing ladder by re-introducing, in a very controlled way, lending at up to 90% loan-to-value. The higher risk inherent in this lending has been carefully managed and all such mortgages are only available through Yorkshire branch-based advised sales.

Our borrowing members who have relatively low levels of mortgage debt in relation to the value of their homes were also rewarded. We offered these members a one year fixed rate "rollover" deal with no fee to fix and no early redemption charges, meaning that they can also benefit from the certainty of a fixed rate whilst not incurring charges or being tied into their mortgage deal.

Whilst being active in uncertain mortgage and housing markets, we protected the interests of individual borrowers and the wider membership and will continue to lend on a prudent basis.

Other benefits

We improved our wider product range during the year, including the launch of "You Choose Home Insurance" which allows our customers to personalise their level of cover according to their circumstances and needs. The popularity of this product was reflected in a significant increase in demand.

YBS Share Plans

Over 170,000 members benefited from participation in Savings Related Share Option Schemes. This is an arrangement that allows employees of a company to buy company shares with money they have contributed to a savings scheme. YBS Share Plans contributed positively to the Group's performance in 2010, and acquired 24 new clients in the year including, Old Mutual plc, Friends Provident Holdings (UK) PLC, Topps Tiles PLC and Communisis plc.

Our commitment to communities

Good corporate citizenship sits at the heart of our approach to mutuality. The Group actively supports the communities in which we live and work through a number of practices including fundraising for charities and good causes, a staff volunteering programme and sound environmental policies. All of these will remain important elements of our mutual approach.

Branch network

Whilst we have invested substantially in our internet and telephone operations, our branch network remains at the heart of our operations. Many people value the personal service and high-quality advice which is best provided in a branch. Our formula is a successful one which combines the community presence and personal service of our branches with joined up and innovative on-line service.

We opened 14 more high street agencies during 2010 and kept all of our branches open. This approach contrasts starkly with the high street banks which have reduced their network by approximately 20% since 1997. Over the same period, the Yorkshire increased its branch network by 34% by a combination of merger and branch

[1]Data sourced from Bank of England Statistics Interactive Database. Cash Individual Savings Account (ISA) rates are selected for £3,000 balances. Rates for Cash ISAs are weighted by month end balances reported on balance sheet returns of institutions in the same sample.
[2]Data sourced from Which? The accounts within these statistics are easy-access, notice savings accounts and cash ISAs.

openings. At the end of 2010, our network of branches and agencies was the 9th largest in the UK and comprised:

- 135 Yorkshire branches;
- 35 Chelsea branches;
- 8 Barnsley branches; and
- 82 Yorkshire agencies.

Our commitment to our branch network hit the headlines recently when the Yorkshire became the last financial mutual to operate in Whitby. We temporarily re-branded our Whitby branch "Whitby's Building Society" and publicised the benefits of mutuality and the personal service available to customers in branch. All of these steps resulted in an influx of new business, underlining once again the fact that our branches are firmly at the heart of our business.

We have always regarded the ultimate test of value delivery as being what our members think about us, and we go to great lengths to seek feedback and give members a genuine say in how we run the Society on their behalf. Examples include the Member Forum and Member Panel. Once again I am grateful to everyone who participated in these for the valuable feedback they have given us. I would like to pay particular tribute to Martin Hawkrigg, a member of the Member Forum since its inception, who sadly died during 2010.

Regular customer satisfaction surveys provide us with reassurance that we continue to provide members with the outstanding level of service that they've come to expect. For example, in 2010, 9 out of 10 customers who responded to our surveys said they rated their satisfaction levels in dealing with us as either excellent or good.

An equally important but more technical measure of how strongly our customers recommend us is our net promoter score, which in 2010 we believe ranked at the top of the financial services industry benchmarks. Our net promoter score refers to the net percentage of customers who, when responding to the question "how likely is it that you would recommend us to a friend or colleague?", would either strongly recommend or strongly detract from the organisation. We closely monitor this measure as we feel that it provides one of the most reliable insights into how our customers perceive the products and service that they receive from us.

Just as important is how we respond when things go wrong. We do sometimes make mistakes, but when we do we take it seriously and try to respond appropriately and learn for the future. One measure of our success was when, in 2010, the Financial Ombudsman Service (FOS) published its "complaint overturn rates" on qualifying firms in the financial services sector. The Yorkshire came joint top of the table, which is an excellent achievement and one which is widely regarded as a clear indicator of the fairness of a firm's approach to complaints handling.

Merger activity

Chelsea

As we reported in our interim management report for the six months ended 30 June 2010, we successfully completed our merger with Chelsea on 1 April 2010 after it was overwhelmingly approved by the members of both societies. The merger was a transformational development for the Group and we can report that realisation of the merger benefits has progressed very well during 2010. Some of the merger highlights include:

- the integration process remained in line with our plans, with delivery of synergies on track for 2011/12;
- we extended the Yorkshire's internet savings capability to Chelsea, and attracted additional sustainably-priced retail funds offering long-term value and better service to members;
- we made substantial progress in addressing the key issues which the Chelsea had at the time of the merger, in particular we improved the funding position for the Chelsea's business as unsustainably-priced fixed rate savings product balances were managed onto more fairly priced products or moved elsewhere; and
- we retained all of the Chelsea branches.

Merger with the Chelsea has undoubtedly strengthened the Group's position giving us greater resilience for the future, broadening our reach to a greater number of members and strengthening our ability to deliver benefits to members.

Our position on merger activity

One of our strategic priorities is to look ahead and seize opportunities; this includes taking advantage of merger opportunities that may be presented to us, but we will only consider doing so where there is a clearly defined benefit to our members.

We believe mergers between building societies, where this is possible, are preferable to the alternative of combining with organisations from outside the mutual sector. We anticipate that attractive opportunities of this type will inevitably arise over the next few years and believe that the Yorkshire is well positioned to respond to them when they are in the interests of our current and future members.

Our people

I would like to thank my colleagues throughout the Society for their hard work and commitment over what has been a transformational year for the business. I have been hugely impressed by everything that my colleagues have achieved, but especially by the professionalism and resilience of our people based in Cheltenham who have dealt with the inevitable uncertainty, and in some cases, sadly, redundancies, necessitated by the Chelsea's merger with the Yorkshire.

Across the Group we achieved another good performance in our staff feedback surveys, supporting our view that our people are engaged in delivering our strategy and are committed to our future success. The surveys showed that the Yorkshire's performance against key indicators including overall satisfaction and leadership remained well above average compared to similar financial services organisations using externally benchmarked data.

Our vision for mutuality and future outlook

We believe that mutual organisations will play an increasingly important role in society, and welcome the coalition government's recognition of this.

Building societies play a critical role in the market, offering consumers real choice in retail financial services. On the one hand there is the plc model which prioritises profit, and on the other the mutual model which prioritises customers' interests.

We firmly believe that the Yorkshire's model represents one way in which successful mutual organisations will operate. The Group has demonstrated the ability to grow by successfully merging with other building societies in order to create a stronger institution delivering a broader range of benefits to a growing membership.

We continue to operate in a challenging economy which, despite no longer being in recession, includes a fragile housing market, high levels of unemployment, inflation running significantly above the Bank of England's 2% target and the base rate of interest remaining at a record-low level.

Against this environment the Group has a stable and well-balanced funding base, a robust capital position and is well placed to increase mortgage lending when the housing market recovers.

In summary, we look ahead with sensible optimism, conscious of the significant challenges the environment presents but encouraged by the opportunities we believe exist for the Yorkshire as a leading independent mutual building society.

Iain Cornish
Chief Executive
23 February 2011

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 free of charge on demand at every office of Yorkshire Building Society, including Chelsea and Barnsley branches, from 8 March 2011.

Summary directors' report

The information contained in the Chief Executive's report on pages 4 to 9 addresses the requirements of the summary directors' report.

The directors consider that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, the going concern basis has continued to be adopted in preparing the Annual Report and Accounts.

Approved by the Board of Directors on 23 February 2011.

Ed Anderson, Chairman, Richard Davey, Vice Chairman, Iain Cornish, Chief Executive.

Group results for the year

	2010 £m	2009 £m
Net interest income	272.7	147.8
Net losses from fair value volatility	(10.5)	(10.3)
Net realised profits	15.2	11.5
Other income and charges	43.4	30.7
Total Income	320.8	179.7
Administrative expenses	(162.6)	(124.3)
Chelsea Building Society merger costs	(10.4)	(6.7)
Provisions*	(45.9)	(58.5)
Operating profit/(loss) before exceptional provisions	101.9	(9.8)
Financial Services Compensation Scheme levy	(3.6)	(2.7)
Operating profit/(loss)	98.3	(12.5)
Negative goodwill	17.1	-
Profit/(loss) before taxation	115.4	(12.5)
Taxation	(23.6)	9.2
Profit/(loss) for the year	91.8	(3.3)

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

Group financial position at end of year

	2010 £m	2009 £m
Assets		
Liquid assets	5,861.8	6,700.4
Mortgages	23,370.7	14,979.4
Derivative financial instruments	579.8	904.5
Fixed and other assets	274.0	137.7
Total assets	30,086.3	22,722.0
Liabilities		
Shares	21,382.5	13,793.4
Borrowings	6,336.7	7,183.1
Derivative financial instruments	472.3	468.1
Other liabilities	175.1	106.6
Subordinated liabilities	214.9	111.7
Subscribed capital	167.3	159.3
Reserves	1,337.5	899.8
Total liabilities	30,086.3	22,722.0

Summary of key financial ratios

	%	%
Gross capital as a percentage of shares and borrowings 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).	6.20	5.58
Liquid assets as a percentage of shares and borrowings 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.	21.15	31.94
Profit/(loss) for the year as a percentage of mean total assets This ratio expresses profit or loss, after tax, as a percentage of average total assets.	0.35	(0.01)
Management expenses as a percentage of mean total assets The management expense ratio measures how cost-effective the Group is. It is calculated by comparing the management expenses (administrative expenses plus merger costs above) for the year with average total assets.	0.66	0.57
Management expenses as a percentage of mean total assets adjusted for the effects of the merger	0.51	0.54

Statement of the independent auditor 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 for the year ended 31 December 2010 which comprises the group results for the year and group financial position at end of year and summary of key financial ratios as well as the Summary directors' report.

This report is made solely to the Society's members, as a body, in accordance with section 76(5) of the Building Societies Act 1986. Our work has been undertaken so that we might state to the Society's members those matters we are required to state to them in an auditor's 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 Society and the Society's members as a body, for our audit work, for this report, for our audit report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

The directors are responsible for preparing this "Your vote, your Society" booklet, in accordance with applicable United Kingdom law.

Our responsibility is to report to you our opinion on the consistency of the Summary financial statement within this "Your vote, your Society" booklet with the full Annual Report and Accounts, Annual Business Statement and Directors' Report and its compliance 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 this "Your vote, your Society" booklet as described on the front cover and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Summary financial statement.

We conducted our work in accordance with Bulletin 2008/3 issued by the Auditing Practices Board. Our report on the Society's Annual Report and Accounts describes the basis of our audit opinion on those financial statements.

Opinion

In our opinion the Summary financial statement is consistent with the full Annual Report and Accounts, the Annual Business Statement and Directors' Report of Yorkshire Building Society for the year ended 31 December 2010 and complies with the applicable requirements of Section 76 of the Building Societies Act 1986 and regulations made thereunder.

Deloitte LLP, Chartered Accountants and Statutory Auditors, Leeds.
23 February 2011

How to vote at the AGM: attend the AGM post it www.ybs.co.uk/agm