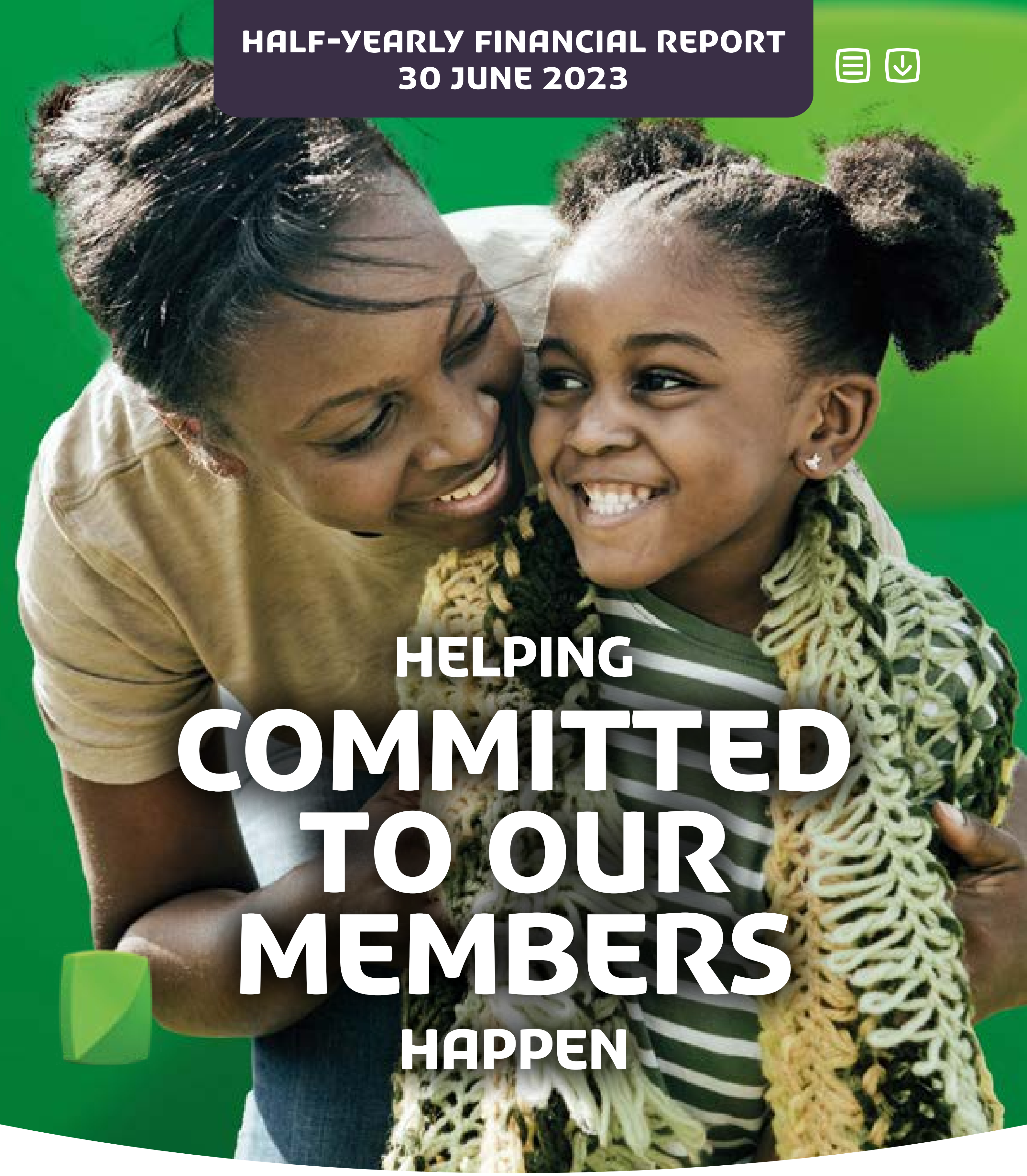
HALF-YEARLY FINANCIAL REPORT
30 JUNE 2023



HELPING COMMITTED TO OUR MEMBERS HAPPEN

YORKSHIRE BUILDING SOCIETY

Helping real life happen

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Interim Management Report

Introduction from the Chief Executive

I am pleased to introduce Yorkshire Building Society's financial report for the six months to June 2023. Having joined the Society as Chief Executive in March this year, I feel privileged to be leading an organisation so clearly aligned to delivering against its purpose: to provide *Real Help with Real Life*. Even though my time at the Society so far has been relatively brief, I have already been able to draw inspiration from the culture I have experienced – one that constantly reaches for better for our members and customers.

Our purpose is at the heart of all that we do, and the first half of 2023 has been no different. We embrace the fact that the products and services we offer can make a genuine difference as people pursue their financial goals, whether saving for a life event or looking to secure a mortgage for a home. It is not difficult to see how essential, everyday goals like these could have been undermined in recent times. The cost-of-living and the rate of inflation, both of which climbed sharply in the last few years, remain prominent concerns for people, for markets, and for governments, despite the series of monetary policy interventions made.

Within this context, the issue of resilience in personal finances has become more critical. This has long been an area of focus for us at the Society, with *Financial Wellbeing* standing beside *Place to Call Home* and *Member Value* as our three core purpose priorities. We recognise the difficulties some people are facing, and we have established new processes to make sure our customers receive the level of support appropriate to their circumstances. In June, the Society became a signatory to a government charter to support mortgage borrowers which aims to provide a range of proactive options for managing their monthly obligations without detriment to borrowers' credit records.

At YBS, we want to see the benefits of financial resilience extend to an audience wider than our membership alone. This is reflected in the community outreach and charitable activities we undertake. Our *Money Minds* and *Career Minds* sessions continue to help young people of school age equip themselves with the financial and workplace skills to succeed. After seeing the positive impact that our partnership with Citizens Advice has brought to local communities, we are expanding the programme to reach more people. Another example is our two-and-a-half-year partnership with Age UK, the leading charity for older people, which comes to an end in November this year.

I am delighted to be able to say that, through donations and the fundraising efforts of our colleagues, we successfully exceeded our target to raise £1 million for Age UK's *Building Better Lives* programme. In the first six months of the year we have supported over 148,000 people (2022 H1: 104,000) toward building their financial resilience through our instant access savings accounts and community activities.

Our ambitions under our *Place to Call Home* priority are met through lending to our mortgage customers. Our strategy in this area is unchanged, with our core lending business supporting our more targeted products which seek to address

Interim Management Report (continued)

Introduction from the Chief Executive (continued)

real problems including helping people take their first step on the property ladder. The mortgage market in the first half of 2023 has been impacted by a number of factors, including affordability pressures, which led to periods of market volatility and an overall reduction in the level of activity compared to last year. Against the backdrop of this downward trend in market activity, the Society achieved gross lending of £4.2 billion in the six months to June 2023 (2022 H1: £5.3 billion), and supported 23,000 people to have a place they can call home (2022 H1: 28,000). We expect conditions in our core markets, particularly that for mortgages, to remain challenging for the foreseeable future. This is set in the context of a likely reduction in market size compared to recent years as well as the broader economic impacts of the rising interest rate environment.

The principal reason that we exist as an organisation is to deliver long-term value to our membership. The Society's members continue to benefit from rewarding rates, as shown by the marked increase in the differential between the savings rates we offer and the average rate offered by the rest of the market. Over 2023 so far, we delivered rates that were on average 1.04 percentage points higher than the market average[1] (0.56 percentage points higher over 2022). We continue to develop our member loyalty programme, releasing a Loyalty ISA in March which saw members who have been with us for 12 months or longer be rewarded with a preferential rate. All of this purposeful activity in our savings business has supported the £3.6 billion in balance growth since the close of 2022 (2022 H1: 2.2 billion).

Our prioritisation of *Member Value* also encompasses the steps we are taking to ensure that we are in a position to meet the evolving needs and expectations of our customers over the long term. We have experienced some challenges this year in the servicing of our customers, in particular some of our complaints handling outcomes have fallen short of our internal expectations. To address this, we have invested in improved monitoring and oversight, and systems enhancements are planned later this year to further improve customer outcomes.

Our *Strategic Blueprint* and *Transformation Roadmap* set out our ambitious journey to transform the products and services we offer and the ways in which we offer them. It has now been three years since the launch of the Blueprint, and we can be proud of what has been achieved to date. We successfully reinvigorated our savings business; made considerable advancements in our digital and online capabilities; and invested in our operational security and resilience. Alongside this, progress is being made in our Environmental, Social, and Governance (ESG) strategy, including how we can support the management of climate change risks and the path to net zero. Our 2022 ESG report is available on our website, and progress on all of our *Responsible Business Priorities* and the future of our Blueprint continues to be made. A detailed update on our progress will be provided as part of our annual report.

Given the fast-changing landscape in which we operate, there will always be more change ahead. The remainder of 2023 and beyond will see us build upon our accomplishments as we continue transforming our business to give our customers even greater choice and control, and make our service as simple, swift, and supportive as we can.

Our chosen measure of customer advocacy is Net Promoter Score (NPS) – a measure of how likely customers would be to recommend us based on their experience. Our investment in transforming our online capabilities continues to be reflected in our improving digital NPS results, and supports our overall score. Our latest overall NPS for 2023 stands at +62, which is an increase of +8 this year, and is currently tracking ahead of our year-end target. Alongside the feedback relating to our products, the high standard of service delivered by our colleagues is a consistent source of praise. I am firm in my belief that our colleagues are absolutely integral to our success, and we are unwavering in our commitment to investing in our people and to fostering a working environment where everyone can thrive. All that we have achieved so far, and all that we aspire to in the years that come, would not be possible were it not for the enthusiasm, talent, and dedication of our colleagues.

All of this has translated into the Society delivering another strong set of financial results in the first half of 2023. Despite having significantly widened our savings differential, and increased our costs to accommodate both inflationary pressures and our investment in transformation, we have continued to drive improved income and profitability. Statutory profit before tax for the period was £180.6 million (2022 H1: £243.4 million) and core operating profit was £246.4 million (2022 H1: £192.5 million). Our profits are reinvested into the Society and, combined with the robust levels of capital and liquidity held, will improve our resilience and flexibility as we navigate the periods of uncertainty that lie ahead.

Whilst I have no doubt that the months and years that follow will bring new and different challenges, we can be secure in the knowledge that our business model is resilient, our risk management capabilities are robust, and our strategic direction is clear. The Yorkshire Building Society stands for something worthwhile, and I greatly look forward to working together with the executive team, our colleagues, and partners in the service of our membership.

Susan Allen, OBE

Chief Executive Officer

1 YBS Group average savings rate compared to rest of market average rates. Data source: CACI's Current Account and Savings Database (CSDB), Stock. Data period: January – May 2023 (latest data available). Comparative period: January – December 2022.

Interim Management Report (continued)

Performance at a glance

Place to call home

Gross lending
£4.2bn
£5.3bn 30 June 2022
This represents the amount we have provided to customers to help finance properties over the period.

Gross mortgage lending market share[1]
3.5%
3.1% 31 December 2022
This represents our share of all mortgage lending in the UK housing market.

Growth in mortgage balances[2]
1.5%
4.9% 30 June 2022
This represents the growth in our overall mortgage balance over the period.

New residential mortgages provided
21,000
25,000 30 June 2022
The number of new residential mortgage advances in the period, helping our customers to have a place to call home.

Financial wellbeing

Savings accounts opened
320,000
171,000 30 June 2022
The number of accounts opened by new and existing members over the period, helping them save for the future.

Savings market share[3]
2.3%
2.2% 31 December 2022
This reflects our share of the UK savings market.

Growth in shares balances
8.6%
6.3% 30 June 2022
This shows the total deposits we use to fund the mortgages we offer to our customers.

Average savings rate paid
2.96%
1.20% over 2022
This shows the benefit we are giving back to our members.

Member value

Statutory profit before tax
£180.6m
£243.4m 30 June 2022
This is the profit we earned from our ongoing business operations, excluding taxes.

Core operating profit[4]
£246.4m
£192.5m 30 June 2022
This is the profit we earned, excluding taxes, fair value volatility and one-time charges.

Cost to core income ratio
39.0%
42.3% 30 June 2022
This ratio measures how efficiently we run our Society by showing how much we are spending to generate every pound of our income.

Average savings differential to the market[5]
1.04pp higher than the market
0.56pp higher over 2022
This shows how much higher the rates we paid our customers were compared to the rest of market average.

Common Equity Tier 1 ratio
16.6%
16.8% 31 December 2022
Maintaining this ratio above a certain minimum helps to protect ourselves against unexpected losses.

Liquidity ratio
26.4%
23.3% 31 December 2022
This ratio measures our ability to lend to borrowers, give money back to savers when they want it, and pay our bills.

UK Leverage ratio
6.3%
6.2% 31 December 2022
This ratio highlights the capital we hold compared to our assets, showing our ability to cope with unexpected events.

Net Promoter Score (NPS®)[6]
+62
+54 in 2022
This measures how willing our customers are to recommend us to others.

More detail on business performance can be found in the *Business highlights* below.

1 Based on Bank of England total industry gross lending. Data period: January – May 2023.
2 Growth in mortgage balances excludes fair value adjustments for hedged risk on loans and advances to customers. Prior year comparative restated on a consistent basis.
3 Based on analysis of BSA deposits Held by Households. Data period: May 2023.
4 Definitions of alternative performance measures are provided on pages 237 to 239 of the 2022 Annual Report and Accounts.
5 YBS Group average savings rate compared to rest of market average rates. Data source: CACI's Current Account and Savings Database (CSDB), Stock. Data period: January – May 2023 (latest data available). Comparative period: January – December 2022.
6 *Net Promoter Score* and *NPS* are trademarks of Bain & Company, Inc., Fred Reichheld and Satmetrix Systems, Inc.

Interim Management Report (continued)

Business highlights

This section provides an overview of the environments within which YBS operates, as well as summarising the key activities in the first half of 2023.

Our community programmes and partnerships

The strong sense of social purpose we hold at YBS means that we seek to positively contribute to the communities within which we operate. Our programmes and partnerships reflect our commitment to supporting financial wellbeing across society, through a range of different initiatives targeted toward people at different stages of their lives.

As a financial services organisation we feel we have an opportunity to support young people as they equip themselves with the skills and education necessary to prosper in the future. The Society has continued to invest in and expand our *Money Minds* and *Career Minds* programmes, delivering over 650 so far this year, and our *Money Minds* online resources provide access to interactive, flexible learning.

We have also built upon our successful initiative in collaboration with Citizens Advice. Funding from the Society allows Citizens Advice to provide free, face-to-face, independent advice and support across a wide range of issues, including *Financial Wellbeing*. The service operates from a number of our branch locations, and in March this year we increased the number of appointments available. In the second half of 2023 we plan to expand the number of participating locations across the UK to 46 from the 18 which offer the service at present.

Since 2020, the Society has been in proud partnership with Age UK. Age UK's services and advisers are there for older people when they need it the most, and the money the Society raises helps the charity to support financial resilience across the country. Over the course of this partnership, our colleagues and members have raised £1,013,577, which includes £634,143 in donations from the Society, exceeding our £1 million target.

The process for selecting our next official charity partner is underway, with the partnership due to commence in November of this year.

Mortgages

Changes in the external environment continue to have a significant bearing on the UK mortgages market. New business mortgage customer rates began the year on a downward trend as the impacts of the market-wide disruption in the latter months of 2022 eased. However further periods of volatility meant this trajectory was not sustained. The most significant shift in the rate environment came in the second quarter of the year, where inflationary pressures demonstrated more persistence than forecasts had anticipated, and the expectations for the future path of Bank Rate elevated sharply.

This continual volatility in interest rate expectations led to a dynamic competitive landscape, with tightening margins and mortgage product ranges being withdrawn, repriced, and relaunched frequently. Steeper borrowing costs also served to constrain the level of activity in the market. The interest rate at which new mortgages can be taken out directly influences the appetite to move or buy as many find themselves less able to raise housing deposits or meet affordability criteria. Responding to the lessening demand, growth in house price indices has slowed over 2023; data released by the Office of National Statistics shows the 12-month growth rate has declined from 5.7% growth in January, to 1.9% growth in May.

Within this context, the volume of applications the Society received has remained high in H1, though not as high as the same period in 2022. This demonstrates the strength of our product propositions – including the buy-to-let (BTL) arm of our intermediary lender, Accord Mortgages Limited, which achieved a greater than typical share of the market. The Society entered 2023 with lower net lending expectations than the two preceding years, owing to the disruption to the wider lending market in Q4 2022, combined with a higher volume of maturities from our lending book. In the first six months of the year total gross lending was £4.2 billion (2022 H1: £5.3 billion), and net lending was at £0.7 billion (2022 H1: £2.1 billion).

We continue to seek to add purpose-aligned products to our range of mortgages, just as we did last year with our *Cascade Score* and *Boost LTI* (loan to income) products, which continue to provide us greater flexibility in our lending decisions. This development work is ongoing by nature, and earlier this year we launched our first mortgage-related loyalty proposition. This allows existing YBS members to claim extra cashback when they take a qualifying mortgage product with us, and if they do not need it themselves, they can pass this offer on to family or friends.

Interim Management Report (continued)

Business highlights (continued)

Savings

Greater returns on savings balances can go some way toward supporting consumers in an environment where financial challenges are so prevalent. Rising interest rates have continued to influence the returns available to savers this year, though the degree to which banks and building societies have increased variable customer rates differs institution by institution. Since the start of the year, the Society's strategy has seen our variable back book rates increase three times to the end of June, and our instant access rates were on average 1.48 percentage points higher than the market average[1] (0.77 percentage points higher over 2022).

Within the savings market, the level of competition for acquiring savings balances intensified as 2023 progressed, with the market for fixed-rate products in particular driving more attractive customer rates. Individual Savings Accounts (ISAs) also increased in popularity this year, owing both to pricing as well as to their tax advantages as Personal Savings Allowances are exhausted at a faster rate than before.

The Society achieved strong levels of growth in the first six months of 2023; shares balances increased by £3.6 billion to £45.6 billion in the period. The market disruption precipitated by the failure of a number of non-UK banking institutions had a minimal effect on our monthly savings flows. Our balance growth was supported by the performance of our ISA range, including the latest in our member loyalty programme: a Loyalty ISA, which offered a premium rate for our longer standing members. Our transformation investment also delivered behind-the-scenes efficiency improvements to customer journeys for ISA applications and transfers in the year.

Back in 2020 when we launched our Blueprint, one of our four key strategic priorities was *Savings Rebooted*. In the two years that followed, the progress we made in this area led to a higher NPS and a higher rate of growth. Our new priority, *Savings Supercharged*, represents how we will take our savings business to the next level as we continue to focus on enhancing what we offer to our members.

Outlook

The economic and political environments continue to exhibit heightened levels of uncertainty. Growth in UK Gross Domestic Product (GDP), though limited in 2023, has so far avoided entering a technical recession – which was viewed as a potential threat as 2022 ended. Pay growth has provided some compensation for consumers, however, after adjusting for inflation, real pay is still falling. The rate of unemployment has remained relatively stable for the past year; the latest official estimate (as at May 2023) was 4.0%, though there remain risks of this worsening should the economy slow from its current state.

Facing stubborn inflationary pressures, the Bank of England has increased the benchmark interest rate four times since December 2022, with Bank Rate standing at 5.0% in June 2023. Much depends on the speed and efficacy of the monetary policy tightening in returning the rate of inflation back toward the Bank of England's target of 2.0%. Broader downside risks also exist in the geopolitical environment, including any developments in the ongoing military conflict in Ukraine.

With regard to the savings market, it appears that the increased level of competition for retail savings balances which characterised the recent months of this year is likely to be sustained. A factor contributing to this will be the need for many financial institutions to refinance drawings from Bank of England funding schemes as its contractual maturity draws closer. Outside of the competitive environment, some savings providers may face pressure from government or regulators as to whether the interest rate rises are benefitting variable rate savers to an appropriate degree.

The current outlook for the mortgages market appears particularly challenging, with some of the headwinds facing this market having already made themselves known to an extent. A range of potential difficulties are faced by both existing and prospective borrowers, stemming from the cost-of-living pressures and inflationary environment.

How much of a constraint issues like affordability criteria pose to the size of the mortgage market remains to be seen, but their impacts have the potential to be material. Different segments of the lending market may also experience more acute impacts, for example increases in borrowing costs may have a greater bearing on the BTL market. Factors like these can cause shifts in the supply and demand dynamics and carry ramifications for house price growth.

The consequences of higher interest rates for existing mortgage customers are a concern for the Government and for regulators. With many borrowers facing a significant increase in their monthly payment obligations at the end of their current fixed terms, in June 2023 the Chancellor met with the UK's principal mortgage lenders and the Financial Conduct Authority (FCA) to agree support measures to protect customers. YBS is a signatory to this charter, which offers a range of options for mortgage holders that aim to alleviate some of the pressures they currently face.

Emerging challenges and threats, of natures both economic and operational, are and will continue to be monitored on a regular basis, to ensure that the Society takes appropriate action where necessary to remain in a position of strength to continue to serve our members.

1 YBS Group average instant access savings rate compared to rest of market average instant access rates. Data source: CACI's Current Account and Savings Database (CSDB), Stock. Data period: January – May 2023 (latest data available). Comparative period: January – December 2022.

Interim Management Report (continued)

Business highlights (continued)

Our financial performance

The following summary sets out the key drivers of our financial results over the first half of the year, and the impact they have on the condensed interim financial statements.

The table below presents the results of Yorkshire Building Society ('YBS' or 'the Society') and its controlled entities (collectively 'the Group' or 'YBS Group') for the half-year ended 30 June 2023. See note 1 to the condensed interim financial statements for more information on the basis of preparation.

Income Statement

Income performance and profitability for the first six months of 2023 remain strong, supported by the rising interest rate environment and continued growth of our balance sheet, particularly within our savings book. A year-on-year increase in our costs reflects the impact of inflationary pressures, but also additional purposeful investment in our Transformation programme.

Our financial performance is monitored by our Board who, in addition to looking at statutory profit before tax, look at core operating profit. Core operating profit excludes items such as fair value volatility and one-time charges that are either temporary in nature or reverse over time and so do not reflect the Group's day-to-day activities. In this reporting period, core operating profit for the period was £246.4 million, an increase of £53.9 million on the equivalent period last year (30 June 2022: £192.5 million).

The following table shows the items removed from statutory profit before tax to arrive at core operating profit.

		Half-year ended 30 June 2023			Half-year ended 30 June 2022			Year ended 31 December 2022		
		Statutory	**Remove non-core items**	**Core**	Statutory	Remove non-core items	Core	Statutory	Remove non-core items	Core
	Notes	**£m**	**£m**	**£m**	£m	£m	£m	£m	£m	£m
Net interest income	i	**417.2**	**(1.4)**	**415.8**	334.2	(1.3)	332.9	724.1	(2.4)	721.7
Other income		**1.8**	**–**	**1.8**	3.6	–	3.6	8.8	0.3	9.1
Fair value gains and losses	ii	**(71.3)**	**67.4**	**(3.9)**	50.2	(49.8)	0.4	75.6	(74.9)	0.7
Net realised gains		**1.5**	**–**	**1.5**	2.4	–	2.4	2.9	–	2.9
Total income/core income		**349.2**	**66.0**	**415.2**	390.4	(51.1)	339.3	811.4	(77.0)	734.4
Management expenses		**(161.9)**	**–**	**(161.9)**	(143.6)	–	(143.6)	(298.7)	–	(298.7)
Impairment of financial assets		**(7.5)**	**–**	**(7.5)**	(0.7)	–	(0.7)	(6.0)	–	(6.0)
Movement in provisions	iii	**0.8**	**(0.2)**	**0.6**	(2.7)	0.2	(2.5)	(4.2)	0.1	(4.1)
Profit before tax/ core operating profit		**180.6**	**65.8**	**246.4**	243.4	(50.9)	192.5	502.5	(76.9)	425.6

The notes below explain the adjustments made to statutory profit to arrive at the core operating profit figure:

i. Historical fair value credit adjustments on acquired loans.

ii. Removed fair value volatility i.e. gains and losses on derivatives not qualifying for hedge accounting, and on non-core equity investments. See note 5 to the condensed interim financial statements for more information.

iii. Non-core elements of the restructuring provision – see note 7 to the condensed interim financial statements for more information.

The following are the main items in the income statement that contribute to core operating profit:

- Net interest income for the year to June is £417.2 million (2022 H1: £334.2 million), representing a net interest margin of 1.38%, an increase of 0.16 percentage points compared to the equivalent period last year.
- Other income of £1.8 million relates to fees, commissions, and other operating income (2022 H1: £3.6 million).
- Net realised profits of £1.5 million relate to profits from the sale of liquid asset investments (2022 H1: £2.4 million).
- Management expenses were £161.9 million, an increase of £18.3 million against the same period in 2022. A significant proportion of this increase relates to a rise in people costs, reflecting a pay award that was significantly higher than the historical average. We have also accelerated investment in our Transformation programme, with the aim of delivering customer benefits earlier than previously anticipated.
- An impairment charge of £7.5 million has been recorded in the period (2022 H1: £0.7 million). This reflects changes to year-to-date changes in HPI as well as broader updates to the economic scenarios used in the modelling. See note 9 to the condensed interim financial statements for more information on expected credit losses, including the economic scenarios used.

Interim Management Report (continued)

Business highlights (continued)

Our financial performance (continued)

As a mutual we do not pay dividends to external shareholders; our profit requirements are driven solely by our need for ongoing capital to support our activities. Profit remains sufficient to provide capital for our growth aspirations and ensure we are resilient to severe economic stresses.

The Group's business activities are focused within the UK and predominantly relate 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 2023, the majority of our liquidity portfolio consisted of exposures to the Bank of England and the UK Government.

Balance Sheet

	Half-year ended 30 June 2023 £bn	Half-year ended 30 June 2022 £bn	Year ended 31 December 2022 £bn
Liquid assets	**14.9**	11.4	12.5
Loan and advances to customers	**45.9**	44.2	45.2
Fair value adjustment for hedged risk on loans and advances to customers	**(1.8)**	(0.9)	(1.5)
Other assets	**3.2**	1.7	2.6
Total assets	**62.2**	56.4	58.8
Shares – retail savings	**45.6**	37.7	42.0
Wholesale funding and other deposits	**10.8**	13.7	11.6
Subordinated liabilities	**1.2**	1.1	1.0
Other liabilities	**1.1**	0.6	0.8
Total liabilities	**58.7**	53.1	55.4
Members' interest and equity	**3.5**	3.3	3.4
Total members' interest, equity and liabilities	**62.2**	56.4	58.8

Overall balance sheet growth achieved in the year to June stands at 5.8% (2022 H1: 7.0%), with more asymmetric growth across mortgages and savings having been achieved than the previous year.

Net lending performance was lower in the first half of this year at £0.7 billion (2022 H1: £2.1 billion). Disruption to the mortgage market in the Autumn of last year resulted in a smaller pipeline of new lending being carried forward into the current year. As a result, lower volumes of new mortgages completed in January and February than we would typically expect. Completion volumes increased markedly over the period of March to June.

Net savings flows continued to perform strongly; balance growth was £3.6 billion in the period (2022 H1: £2.2 billion). This growth has been supported by the strength of our propositions, further increases to our back-book rates, and the widening of our rate differential to the market. In line with this, our overall liquidity position has further improved, standing at 26.4% (2022: 23.3%). Sufficient headroom to regulatory requirements has been maintained and we continue to diversify our high-quality liquid asset portfolio.

Our key capital ratios continue to demonstrate stability in our capital position. Our Common Equity Tier 1 ratio, which represents the relationship between the strongest form of capital (predominantly retained profits) and risk-weighted assets, is 16.6% (2022: 16.8%). And our UK leverage ratio, which compares Tier 1 capital with total assets, stands at 6.3% (2022: 6.2%).

In the first half of 2023, the Society successfully issued a Residential Mortgage Backed Security, a Sterling denominated Covered Bond, and a Senior Non-Preferred (SNP) Note, with the latter also accompanied by a liability management exercise to repurchase a proportion of an existing issuance. Additionally, in June we made a further repayment, of £1.0 billion, in respect of our drawings from the Bank of England's TFSME scheme, significantly ahead of its contractual maturity.

The asset quality of our loan book remains high. The value of loans more than three months in arrears represents 0.32% of our mortgage book at 30 June 2023 (31 December 2022: 0.31%). The number of accounts which are more than three months in arrears (including possessions) is 0.44% at 30 June 2023 (31 December 2022: 0.44%), which remains significantly better than the industry average[1], the latest data for which is 0.74% (31 December 2022: 0.73%). A number of indicators are used in assessing the credit quality of our loan book, which are continually monitored. We also continue to consider our lending criteria carefully.

1 Industry average sourced from UK Finance: Retail, 3m+ in arrears. Latest data available is as at March 2023.

Interim Management Report (continued)

Principal risks and uncertainties

The environment within which we operate and the nature of the threats that we face are continually evolving. The sources of uncertainty, both nationally and internationally, are many; they include the inflationary macroeconomic environment, the consequent cost-of-living challenges and geopolitical instability.

A description of the principal risks and uncertainties to which we are exposed is included in the table below, followed by further commentary on how these risks have evolved. We have performed stress tests to assess the impact of a range of risk scenarios and it is our assessment that, while each of the scenarios bring their individual challenges, we are well placed to manage them.

We continue to invest in our risk management capability to ensure that emerging and evolving risks are closely monitored, and that timely and appropriate action is taken to protect the interests of Yorkshire Building Society and its controlled entities (the Group), and its members and customers. Significant emerging risks are regularly reviewed through the senior Risk Committees and are considered as part of our planning process.

We have a robust risk management framework, strong capital position, diverse funding sources and high liquidity levels; and we remain confident in the financial resilience, operational resilience, and the sustainability of the Group.

Risk	Description	Principal mitigation
Strategic risk	The risk to the Society's earnings or sustainability which arises from changes in the business environment (Political, Economic, Social and Technological), or from the effectiveness of decisions and actions relating to our strategic response to those changes.	We mitigate risks relating to the business environment and our strategic choices through horizon scanning, corporate planning, scenario analysis and stress testing, and ongoing monitoring and reporting activity.
Retail and commercial credit risk	The risk to the Group of credit losses as a result of failure to design, implement and monitor an appropriate credit risk appetite.	We set a stress-tested risk appetite for retail and commercial lending activities which manages exposure to higher risk lending areas, and monitors adherence to this.
Treasury risk	The risk of losses following default on exposures arising from balances with other financial institutions, liquid asset holdings and from derivative instruments used to manage interest rate and foreign exchange risk.	We set a stress-tested risk appetite for treasury risk and monitor adherence to this. We adopt a low-risk approach to our treasury activities, investing most of its liquidity in the highest quality assets.
Funding and liquidity risk	The risk of the Group having inadequate cash flow to meet current or future requirements and expectations.	We set a stress-tested risk appetite and monitor our positions against this. We operate a diversified funding base, primarily through retail savings, supported by a strong wholesale funding franchise.
Market risk	The risk to the Group's earnings or the value of its assets and liabilities due to changes in external market rates.	We adopt a low-risk approach to market risk, and stress test all positions against a range of scenarios.
Capital risk	The risk that the Group is not able to meet regulatory capital requirements or deliver on its strategic plans due to insufficient capital resources.	We maintain a stress-tested capital risk appetite and regularly stress test its positions against severe scenarios.
Model risk	The risk that the Group's models used to manage the business are inaccurate, perform inadequately or are incorrectly used.	We operate a Model Risk Management Maturity framework which includes monitoring of model suitability and performance within agreed risk appetite.
Operational risk	The risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems, or from external events. Operational risk includes cyber, people and third-party risk.	We operate an internal control framework in line with the Board risk appetite and monitor adherence through our three lines of defence model.
Compliance and conduct risk	The risk of direct or indirect loss as a result of a failure to comply with regulations (such as money laundering) or to ensure fair customer outcomes. Compliance and conduct risk includes financial crime risk.	We operate an internal control framework in line with the Board risk appetite and monitor adherence through our three lines of defence model.

Interim Management Report (continued)

Principal risks and uncertainties (continued)

Evolution of Principal Risk Exposures

The principal risks and uncertainties continue to evolve. The key areas of focus during the first half of 2023 were rising inflation and interest rates, creating greater cost-of-living concerns for our customers, members and colleagues; a slow-down in the housing market; periods of turbulence in financial markets; and labour shortages, arising from increased demand for skills such as digital.

Economic, social, and political uncertainties (retail and commercial credit and market risks)

Pressure on mortgage affordability remains prevalent, with a range of contributing economic, social, and political factors. Inflation has continued to rise during the first half of this year, and in response, interest rates have risen further. Together, these place affordability stresses on mortgage borrowers, as well as tenants of buy-to-let and commercial landlords.

These affordability stresses are likely to continue for the foreseeable future. Affordability for new lending or where there is a material change in circumstances is assessed using a sophisticated model, which currently incorporates a stressed interest rate, and is reviewed every six months (as a minimum) to ensure it remains an appropriate level of stress. Changes have been made to this model to ensure that various cost-of-living factors are accounted for, including the impact of inflation on monthly expenditure. Equally, comprehensive activity has taken place to understand the impact of, and mitigate where appropriate, the higher cost-of-living on our new and existing portfolio.

The consequent market volatility has also continued during the first half of the year. This has required disciplined hedging and ensuring our products are carefully priced so that our risk appetites are not exceeded.

We continue to consider lending criteria carefully using an approach that is intended to balance the level of risk we take against our purpose of providing *Real Help with Real Life*. At all times we focus on our lending being responsible to protect customers and to minimise arrears.

Attracting and retaining skills and talent in high demand areas (operational risk)

We increasingly recognise that social changes brought about by the COVID-19 pandemic, such as removal of geographical barriers, have accelerated changes in employee expectations. These are resulting in increased competition in the recruitment and retention of colleagues across all areas of the business, but particularly those areas with high demand skills such as change, digital, technology and data and analytical functions.

We continue to review our value proposition in relation to talent acquisition and retention and undertake continual monitoring of the recruitment market. We do not expect candidate expectations around flexible working to return to pre-pandemic norms and so we continually review how we attract, retain and support new and existing colleagues to work flexibly. We expect the recruitment market to remain candidate-driven over the rest of the year and will therefore continue to leverage our refreshed Employee Value Proposition and proactively source talent to fulfil business requirements. Effective resource planning and forecasting is a priority, and our resourcing practices are regularly reviewed to ensure we proactively manage associated risks to deliver our *Strategic Blueprint*.

Model risk

We continue to monitor and address, via the Society's Model Risk Committee, the risks associated with the use of models and, specifically, the use of models that rely on historical data being applied to future scenarios. We continue to adapt and develop our approach to model risk management and the underlying models themselves in line with industry good practice and regulatory guidance.

Regulation and fair outcome (compliance and conduct risk)

Compliance and conduct are central to our values and behaviours, with an internal control framework that operates in line with the Board risk appetite, and which monitors adherence. However, ongoing focus and robust challenge is required to keep pace with the rapidly changing legal and regulatory environment. This is also vitally important as we continue with our ambitious transformation programme which explores new initiatives, customer journeys and ways of working.

Dialogue with our regulators continues to be open and constructive, and we continue to work with regulators and industry bodies to contribute to the developing regulatory agenda. This includes matters such as the FCA's introduction of new Consumer Duty regulation which sets higher expectations for the standard of care that firms provide to consumers. As a mutual organisation, fair customer treatment is intrinsic to everything we do and is aligned to our purpose to provide *Real Help with Real Life*.

Climate change risk (credit and operational risk)

We recognise that climate change is one of the most critical issues facing the UK and global economy. The main climate-change risks impacting us are how physical risks such as flooding, subsidence and coastal erosion affect our customers' homes. Additionally, we recognise the risks posed by the transition to a low-carbon economy such as energy efficiency regulation and any exposure to sectors most affected by this change.

We continue to develop our environmental and climate change risk management capabilities to integrate these within our risk management framework, ensure that we align with best practice, and can meet reporting and disclosure requirements.

Interim Management Report (continued)

Principal risks and uncertainties (continued)

Evolution of Principal Risk Exposures (continued)

Increased competition and new technology (operational risk)

Our digitalisation programme continues to develop wider access to our products and services through expanded digital channels. Challenger banks, FinTech firms and the digital transformation of direct competitors continue to heighten the need to remain competitive in these areas.

We continue to successfully deliver the first phase of our programme and have maintained strong governance and extensive oversight of the management of associated risks. There is, however, a residual risk that securing the resource to deliver the change necessary for some customer groups to keep pace with rapidly changing technology may also prove unsustainable, and require investment choices which may not fully meet customer expectations.

We are also modernising our IT infrastructure to improve resilience and reduce risk. As IT components age, their fit and value often deteriorate, while cost and risk often conversely grow. We have embedded an approach to managing and mitigating our legacy IT risks, including those relating to third parties, and progress is reported to the Board at least annually.

Further phases of our digitalisation and technology modernisation programmes will create additional risks, and we will continue to identify, assess, and manage these as appropriate.

Financial crime threats (compliance and conduct risk)

We operate in a hostile and constantly evolving financial crime environment, including phishing and spam attempts that seek to take advantage of customers.

We have noticed an uptick in financial crime incidents during the first half of the year and therefore remain on high alert. Our continued focus on our financial crime capability remains paramount to keep these evolving financial crime exposures within our risk appetite. The Society continues to invest to deliver and implement proportionate and effective monitoring, enhance our ability to identify threats and invest in financial crime controls.

New and evolving cyber security threats (operational risk)

The increasing use of technology, and the pace of technological change, exposes the UK financial services sector to ever-increasing and evolving cyber security risks. Geopolitical threats such as the war in Ukraine have elevated the threat landscape, with ransomware a continued threat. Resilience to such threats and an ability to effectively respond in the event of an attack remains essential to protect the Society, maintain the trust of customers and the confidence of regulators. Good progress has been made in improving the Society's security monitoring capabilities.

Continued risk management effectiveness

We continue to invest in this area to ensure that our key controls are appropriately maintained. Good progress has been made during the first half of 2023 with the continued embedding of our risk management framework across the business, evidenced by our ability to continue to adapt and respond to rapid change in our operating environment.

To further support our *Strategic Blueprint*, we defined a set of risk management priorities. These priorities set out the role that risk management plays to deliver the *Strategic Blueprint* and, in turn, long-term sustainability for the benefit of our customers and colleagues. Priorities include, but are not limited to: ensuring operational resilience vulnerabilities are identified and evaluated; improving our cyber security capabilities; building on existing capabilities to enhance understanding of risks arising from climate change; and delivering robust financial crime identification, prevention, mitigation, and reporting that will protect the Society and its customers.

Interim Management Report (continued)

Regulatory environment

Relevant updates with respect to the regulatory environment include:

Consumer Duty

The FCA's Consumer Duty comes into force for open-book products on 31 July 2023. This new fundamental principle sets higher standards, moving beyond consumer protection to require firms to 'deliver good outcomes for retail customers'.

The impact of the Duty is being seen not only in the new rules and principles specifically drafted for the Duty, but also in other work the FCA is delivering such as their consultation into *Strengthening Protections for Borrowers in Financial Difficulty*. We expect to see this kind of focus to continue.

The FCA expect Boards of Directors to take the Duty to their heart. A Consumer Duty champion has been appointed, and the Board has been regularly engaged as to YBS's progress towards meeting the requirements. YBS is assessing it's final position of readiness ahead of 31 July 2023, with the expectation that the majority of requirements will be met, with only modest gaps remaining which are captured within a post 31 July delivery plan. The FCA have already been using industry insight to provide guidance on the Duty and it is likely that they will use these Board-level assessments to identify areas of potential harm to retail customers.

The Edinburgh Reforms

In a statement on 9 December 2022, the UK Government announced a package of over 30 measures to reform UK financial services regulation. Collectively known as the 'Edinburgh Reforms', these are intended to deliver the next chapter of the Government's vision for UK financial services and are divided into four categories: a competitive marketplace promoting effective use of capital; sustainable finance; technology and innovation; and consumers and business. The Government explained that it will deliver the reforms through two tranches, and they expect to make significant progress on both by the end of 2023.

UK Fraud Strategy

On 3 May 2023, the Government published its updated Fraud Strategy. The strategy sets out the Government's plans to deliver a ten-percent reduction in fraud by the end of December 2024.

Historically the main form of fraud was 'unauthorised fraud', which is predominantly bank and credit card related, where money is taken without authorisation or without the victim's knowledge. Technology and processes have since become more effective in preventing this type of fraud, which has unfortunately given rise to an increase in 'authorised fraud', where victims are persuaded to authorise a payment themselves. This can take many forms, but common examples include retail scams, romance, and investment fraud. The key objectives of the strategy are:

- To pursue fraudsters, disrupting their activities and bringing them to justice more often and quicker.
- To block frauds at source by dramatically reducing the number of fraud and scam communications getting through to the public.
- To empower the British people to recognise, avoid, and report frauds and equip them to easily and appropriately deal with those frauds that do get through.

Separately, the Payment Systems Regulator (PSR) issued a policy statement relating to Authorised Push Payment (APP) fraud. The PSR is introducing a reimbursement requirement which will establish consistent minimum standards to reimburse victims of APP fraud. Essentially it will:

- Require payment firms to reimburse all in-scope customers who fall victim to APP fraud in most cases. The reimbursement requirement will not apply to civil disputes, where payments have been made for unlawful purposes or where the customer has acted with gross negligence.
- Share the cost of reimbursing victims 50:50 between sending and receiving payment firms.
- Provide additional protections for vulnerable customers.

The new reimbursement requirement, which is expected to come into force in 2024, will apply to all payment services providers, including building societies.

Confirmation of Payee (CoP)

This is a service that allows the customer to check the name of a destination bank account matches the name they have entered. In August 2019 the Payment Services Regulator (PSR) required the UK's six largest banking groups to introduce CoP, which resulted in 33 firms adopting the service. Subsequently, in October 2022 the PSR directed around 400 Payment Services Providers to implement a system that provided the CoP service that will increase the transaction coverage to around 99%. This implementation date for YBS will be October 2023.

Environmental, Social, and Governance Strategy (ESG)

The FCA's Environmental, Social, and Governance (ESG) Strategy sets out their target outcomes and the actions expected in order to deliver them. The aim is to support the financial sector in driving positive change, including the transition to net zero.

Financial services providers have become increasingly reliant on third-party ESG data services, as well as ratings, as they integrate ESG into their activities. It is therefore increasingly important that these services are delivered in a fair, effective, and transparent way. Further to this, in December 2022 the Government announced that it would consult on bringing ESG data and ratings providers into the FCA's regulatory perimeter.

Interim Management Report (continued)

Changes to the Board

A complete list of the board of directors can be found in the 2022 Annual Report and Accounts and on our website at www.ybs.co.uk.

As reported in the 2022 Annual Report and Accounts, we were pleased to announce in August 2022 that the Society had appointed Susan Allen OBE as our new Chief Executive Officer. Susan officially joined the Society on 2 March 2023 bringing more than 25 years of experience in financial services.

Following the recruitment processes commenced in 2022 as part of our succession plans, which were set out in the Annual Report and Accounts 2022, we announced in July 2023 that after nine years as Chair, John Heaps will be succeeded by Annemarie Durbin who will join the Board as Chair Designate by the end of the year. We were also pleased to welcome Debra Davies to our Board from 26 July 2023 as a Non-Executive Director and future Chair of the Remuneration Committee, subject to regulatory approval.

Signed on behalf of the Board by

Susan Allen, OBE

Chief Executive Officer

Alasdair Lenman

Chief Finance Officer

Condensed Interim Financial Statements

Consolidated Income Statement

	Notes	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Interest revenue calculated using the effective interest method	3	**874.3**	534.5	1,202.6
Other interest revenue	3	**467.8**	39.1	234.4
Interest revenue	3	**1,342.1**	573.6	1,437.0
Interest expense	4	**(924.9)**	(239.4)	(712.9)
Net interest income		**417.2**	334.2	724.1
Fee and commission revenue		**9.6**	11.5	21.6
Fee and commission expense		**(8.1)**	(8.5)	(16.3)
Net fee and commission income		**1.5**	3.0	5.3
(Losses)/gains from financial instruments held at fair value	5	**(71.3)**	50.2	75.6
Income from investments		**–**	–	0.1
Net realised gains on disposal of financial instruments		**1.5**	2.4	2.9
Other operating income		**0.3**	0.6	3.4
Total income		**349.2**	390.4	811.4
Administrative expenses		**(152.2)**	(132.7)	(276.9)
Depreciation and amortisation		**(9.7)**	(10.9)	(21.8)
Impairment of financial assets	6	**(7.5)**	(0.7)	(6.0)
Movement in provisions	7	**0.8**	(2.7)	(4.2)
Profit before tax		**180.6**	243.4	502.5
Tax expense	8	**(47.7)**	(57.2)	(123.2)
Profit for the period		**132.9**	186.2	379.3

Condensed Interim Financial Statements (continued)

Consolidated Statement of Comprehensive Income

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Profit for the period	**132.9**	186.2	379.3
Items that may be subsequently reclassified through profit or loss			
Cash flow hedges:			
Fair value movements taken to equity	**(6.5)**	18.6	26.1
Amounts transferred to the income statement	**(7.5)**	(3.9)	(28.1)
Tax on amounts recognised in equity	**3.9**	(4.2)	0.5
Effect of change in corporation tax rate	**–**	0.8	0.8
Financial assets measured through other comprehensive income:			
Fair value movements taken to equity	**1.8**	(3.3)	(27.0)
Amounts transferred to the income statement	**–**	0.8	(1.9)
Tax on amounts recognised in equity	**(0.5)**	0.6	7.8
Effect of change in corporation tax rate	**–**	1.6	1.9
Items that will not be reclassified through profit or loss			
Remeasurement of retirement benefit obligations	**(12.1)**	(30.5)	(80.0)
Tax on remeasurement of retirement benefit obligations	**3.4**	8.4	21.6
Effect of change in corporation tax rate	**–**	6.0	6.9
Total other comprehensive income	**(17.5)**	(5.1)	(71.4)
Total comprehensive income for the period	**115.4**	181.1	307.9

Condensed Interim Financial Statements (continued)

Consolidated Balance Sheet

		As at 30 June 2023 (unaudited) £m	As at 30 June 2022 (unaudited) £m	As at 31 December 2022 (audited) £m
Assets				
Cash and balances with the Bank of England		**7,563.7**	5,526.9	5,982.8
Loans and advances to credit institutions		**450.5**	617.8	814.7
Debt securities		**6,887.0**	5,210.4	5,684.8
Loans and advances to customers	9	**45,868.1**	44,218.3	45,203.7
Fair value adjustment for hedged risk on loans and advances to customers		**(1,792.1)**	(906.0)	(1,508.3)
Derivative financial instruments		**2,983.9**	1,461.9	2,356.5
Investments		**3.0**	5.2	2.8
Intangible assets		**16.5**	20.7	20.2
Investment properties		**15.9**	14.4	16.0
Property held for sale		**0.9**	0.3	0.9
Property, plant and equipment		**97.7**	119.0	101.1
Current tax assets		**22.7**	–	–
Retirement benefit surplus	10	**36.5**	90.9	48.8
Other assets		**27.0**	30.5	30.1
Total assets		**62,181.3**	56,410.3	58,754.1
Liabilities				
Shares		**45,632.8**	37,739.0	42,008.2
Amounts owed to credit institutions		**4,375.8**	6,569.6	5,160.9
Other deposits		**1,027.3**	1,123.3	1,138.1
Debt securities in issue		**5,409.8**	6,008.9	5,259.3
Derivative financial instruments		**908.6**	467.3	666.3
Current tax liabilities		**–**	9.4	0.7
Deferred tax liabilities		**17.7**	37.7	11.9
Other liabilities		**64.4**	75.9	64.0
Pension liability	10	**7.2**	–	7.4
Provisions		**4.0**	6.6	5.7
Subordinated liabilities		**1,221.8**	1,102.9	1,035.1
Total liabilities		**58,669.4**	53,140.6	55,357.6
Members' interests and equity		**3,511.9**	3,269.7	3,396.5
Total members' interest, equity and liabilities		**62,181.3**	56,410.3	58,754.1

Condensed Interim Financial Statements (continued)

Consolidated Statement of Changes in Members' Interest and Equity

	General reserve £m	Cash flow hedge reserve £m	Fair value through other comprehensive income £m	Total £m
Half-year to 30 June 2023				
At 1 January 2023 (audited)	**3,384.7**	**9.9**	**1.9**	**3,396.5**
Profit for the period	**132.9**	**–**	**–**	**132.9**
Net remeasurement of defined benefit obligations	**(8.7)**	**–**	**–**	**(8.7)**
Net movement in cash flow hedges	**–**	**(10.1)**	**–**	**(10.1)**
Net movement in fair value through other comprehensive income	**–**	**–**	**1.3**	**1.3**
Total comprehensive income	**124.2**	**(10.1)**	**1.3**	**115.4**
At 30 June 2023 (unaudited)	**3,508.9**	**(0.2)**	**3.2**	**3,511.9**
Half-year to 30 June 2022				
At 1 January 2022 (audited)	3,056.9	10.6	21.1	3,088.6
Profit for the period	186.2	–	–	186.2
Net remeasurement of defined benefit obligations	(16.1)	–	–	(16.1)
Net movement in cash flow hedges	–	11.3	–	11.3
Net movement in fair value through other comprehensive income	–	–	(0.3)	(0.3)
Total comprehensive income	170.1	11.3	(0.3)	181.1
At 30 June 2022 (unaudited)	3,227.0	21.9	20.8	3,269.7
Year to 31 December 2022				
At 1 January 2022 (audited)	3,056.9	10.6	21.1	3,088.6
Profit for the period	379.3	–	–	379.3
Net remeasurement of defined benefit obligations	(51.5)	–	–	(51.5)
Net movement in cash flow hedges	–	(0.7)	–	(0.7)
Net movement in fair value through other comprehensive income	–	–	(19.2)	(19.2)
Total comprehensive income	327.8	(0.7)	(19.2)	307.9
At 31 December 2022 (audited)	3,384.7	9.9	1.9	3,396.5

Condensed Interim Financial Statements (continued)

Consolidated Statement of Cash Flows

	Notes	**Half-year to 30 June 2023 (unaudited) £m**	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Cash flows from operating activities				
Profit before tax		**180.6**	243.4	502.5
Non-cash items included in profit before tax	12	**282.4**	621.3	1,186.2
Net change in operating assets	12	**(1,313.5)**	(3,014.5)	(4,914.1)
Net change in operating liabilities	12	**2,912.5**	3,057.3	6,113.2
Tax paid		**(58.5)**	(51.3)	(125.5)
Net cash flow from operating activities		**2,003.5**	856.2	2,762.3
Cash flows from investing activities				
Purchase of property, plant and equipment, and intangible assets		**(2.4)**	(5.2)	(12.8)
Proceeds from sale of property, plant and equipment		**–**	0.2	0.8
Purchase of debt securities		**(2,035.1)**	(1,737.7)	(2,952.2)
Redemption and other movements of debt securities		**836.2**	602.7	1,316.9
Net cash flow from investing activities		**(1,201.3)**	(1,140.0)	(1,647.3)
Cash flows from financing activities				
Redemption of debt securities in issue	12	**(796.3)**	(417.5)	(1,225.2)
Issue of debt securities	12	**1,005.3**	635.0	711.5
Redemption of subordinated liabilities	12	**(136.4)**	–	–
Issue of subordinated liabilities	12	**350.0**	300.0	300.0
Interest paid on subordinated liabilities		**(17.2)**	(15.3)	(33.7)
Interest paid on lease liabilities		**(0.3)**	(0.4)	(0.7)
Capital repayments on lease liabilities		**(1.6)**	(2.8)	(2.3)
Net cash flow from financing activities		**403.5**	499.0	(250.4)
Net change in cash and cash equivalents		**1,205.7**	215.2	864.6
Opening balance		**6,630.3**	5,765.7	5,765.7
Closing cash and liquid cash equivalents		**7,836.0**	5,980.9	6,630.3
Cash and liquid cash equivalents				
Cash and cash equivalents		**7,563.7**	5,526.9	5,982.8
Less Bank of England cash ratio deposit		**(178.2)**	(163.8)	(167.2)
Loans and advances to credit institutions		**450.5**	617.8	814.7
Closing cash and liquid cash equivalents		**7,836.0**	5,980.9	6,630.3

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements

1. Basis of preparation

These condensed interim financial statements present the results of Yorkshire Building Society ('YBS') and its controlled entities (collectively 'the Group' or 'YBS Group') for the half-year ended 30 June 2023.

The accounting policies, presentation and measurement applied during the period are consistent with those applied by the Group in the 31 December 2022 audited annual financial statements being International Accounting Standards (IAS), International Financial Reporting Standards (IFRS) and interpretations (IFRICs) issued by the International Accounting Standards Board (IASB) endorsed by the UK Endorsement Board (UKEB) and effective as at 1 January 2023. The presentation applied in the period is consistent with the presentation applied in the 31 December audited annual financial statements with an exception for a change in presentation as discussed below.

The Group is required under the *Building Societies Act 1986* to apply 'UK-adopted international accounting standards' as endorsed by the UKEB. The condensed interim financial statements have therefore been prepared in accordance with UK-adopted IAS 34 Interim Financial Reporting and the Disclosure Guidance and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Pounds sterling is both the functional currency of the YBS Group and the presentation currency applied to these financial statements. Except where otherwise stated, all figures in the financial statements are presented in round hundreds of thousands of pounds sterling (£0.0 million).

During the half-year to 30 June 2023 there have been no changes to the composition of the Group. The condensed interim financial statements have been subject to a review and have not been audited.

Accounting developments

The information on future accounting developments and their potential effect on the financial statements are provided on page 147 of the 2022 Annual Report and Accounts.

Going concern

The YBS Board of Directors undertake regular assessments of whether the Group is a going concern in light of changing economic and market conditions, using all available information about future risks and uncertainties. Details of the review undertaken to support the 31 December 2022 financial statements are given on page 129 of the 2022 Annual Report and Accounts.

The directors confirm that, based on the latest formal review undertaken in July 2023, and stress tests performed throughout the period, 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 condensed interim financial statements.

Change in presentation

A balance sheet line item has been created in these financial statements to present *Fair value adjustment for hedged risk on loans and advances to customers* as a separate item on the balance sheet. The balance of *Fair value adjustment for hedged risk on loans and advances to customers* was previously reported within the *loans and advances to customers* balance. Notes to the financial statements have been updated to reflect this change in presentation (note 9, note 12 and note 13).

2. Critical accounting judgements and key sources of estimation uncertainty

In applying its accounting policies, the Group makes judgements that have a significant impact on the amounts recognised in the condensed interim financial statements.

In addition, estimates and assumptions are used which could affect the reported amounts of assets and liabilities. The estimates and underlying assumptions are reviewed on an ongoing basis.

Other than the specific changes highlighted below, the key sources of estimation uncertainty remain unchanged since those disclosed on pages 153 to 154 of the 2022 Annual Report and Accounts.

Impairment of loans and advances to customers

The impairment calculation of expected credit losses (ECL) for a portfolio of mortgage loans is inherently uncertain. ECL are calculated using historical default and loss experience but require judgement to be applied in predicting future economic conditions (e.g. interest rates and house prices) and customer behaviour (e.g. default rates). The most critical judgements that lead to estimation uncertainty are as follows.

Economic scenario and weightings

The UK Economy is expected to avoid a recession, which was widely predicted throughout 2022, as a result of reducing energy prices, a more resilient global environment and continued tightness in the labour market. Growth will likely remain weak by historical standards and there remains more downside risk than upside.

Household spending is the greatest headwind in 2023 with higher prices continuing to drag on real incomes as well as the persistent increase in interest rates reducing disposable income and raising the risk of borrowers failing to meet their contractual repayments.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

2. Critical accounting judgements and key sources of estimation uncertainty (continued)

Economic scenario and weightings (continued)

Management evaluated these uncertainties, with the economic assumptions applied to the ECL model adjusted to reflect any material changes in view of the macro-economic environment. A post model adjustment was raised in 2022 and has been updated to reflect the risks relating to affordability and the impact of cost-of-living increases on our mortgage customers (see note 9 for more details).

The provision is calculated by applying a range of economic scenarios that are probability-weighted.

The Society continue to apply four economic scenarios, all of which have become less pessimistic in 2023. There is now closer alignment between the core and downturn scenarios than there was previously and it has been concluded that amending the combined weighting of the downside scenarios from 45% to 55% was appropriate.

UK CPI remained much stronger than expected with domestic price pressure easing slower than anticipated. This has led to changes in market expectations of Bank Rate peak, as rates are expected to rise further in an attempt to return inflation back towards its 2% target. As mortgages payments rise as a consequence of the increasing rate environment the likelihood of customers entering into financial difficulties grows, this could also lead to declining house prices and more adverse economic conditions than those set out in the Society's core scenario.

The Group considered alternative sets of weightings. The most severe shifted a further 5% from core and downside to severe downturn resulting in a £4.1 million increase in ECL. The least severe applied weightings as at year end whereby 5% from downside and severe downturn was shifted back to core resulting in a £3.9 million decrease in ECL. These changes in weightings have been fully modelled and been allowed to impact staging.

The key in-year impact of changes to economic variables came from applying quarterly Office of National Statistics (ONS) HPI updates, which accounted for £3.2 million of impairment charge in the first half of 2023 (2022: £12.5 million release).

In terms of sensitivity to key changes in economic variables within the model, the HPI forecast within the core scenario was replaced with the respective forecast from the downturn scenario, increasing ECL by £1.5m. Below is the percentage change in HPI forecast for the downturn scenario for the next 5 years in relation to the core scenario.

			2023 Scenario (% change)		
	2023	**2024**	**2025**	**2026**	**2027**
HPI					
Downturn	**(4.2)**	**(2.1)**	**–**	**(0.3)**	**(0.1)**

3. Interest revenue

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Calculated using the effective interest rate method:			
Loans secured on residential property	**616.8**	482.3	1,027.3
Other loans	**20.8**	11.1	26.7
Liquid assets	**142.3**	19.3	77.5
On debt securities	**94.4**	21.8	71.1
Interest revenue calculated using the effective interest rate method	**874.3**	534.5	1,202.6
Other:			
Derivatives in hedge relationships	**434.8**	34.6	212.2
Derivatives not included in hedge relationships	**32.2**	4.5	20.4
Investments held at fair value	**0.8**	–	1.8
Other interest revenue	**467.8**	39.1	234.4
Total interest revenue	**1,342.1**	573.6	1,437.0

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

4. Interest expense

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Shares held by individuals	**627.5**	135.7	442.7
Deposits from banks	**72.2**	19.9	76.1
Other deposits	**11.8**	2.1	9.3
Debt securities in issue	**71.0**	29.9	75.5
Subordinated liabilities	**17.2**	15.3	33.7
Other interest payable	**0.1**	–	0.1
Derivatives in hedge relationships	**62.0**	31.5	38.7
Derivatives not included in hedge relationships	**62.8**	4.6	36.1
Interest expense for leasing arrangements	**0.3**	0.4	0.7
Total interest expense	**924.9**	239.4	712.9

5. (Losses)/gains from financial instruments held at fair value

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Derivatives and debt securities not included in hedge relationships	**(55.5)**	60.3	106.6
Hedge accounting ineffectiveness	**(16.0)**	(9.9)	(32.4)
Equity investments held at fair value	**0.2**	(0.2)	1.4
Total net (losses)/gains from financial instruments held at fair value	**(71.3)**	50.2	75.6

Derivatives and hedging

The Society transacts interest rate swaps to hedge their exposure to movements in interest rates. Whilst all interest rate swaps have been entered into for hedging purposes, only certain arrangements meet the conditions necessary to be designated as such for accounting purposes. Where the conditions have not been met for hedge accounting to be applied the changes in the fair value of those derivatives is recognised directly in the income statement and included within derivatives and debt securities not included in hedge relationships. This portfolio of derivatives is made up of a split of swaps that receive a fixed interest cash flow ('receive fix') and swaps that pay a fixed interest cash flow ('pay fix'). In 2022, as a result of the rising rate environment, the pay fix swaps generated fair value gains which were partially offset by fair value losses from the receive fix swaps. However, in the past year the volume of receive fix swaps has grown significantly due to the increase in retail deposits generating an overall fair value loss year to date as a result of the rising rate environment we are still experiencing.

Hedge accounting ineffectiveness includes the portion of fair value offset between the derivatives and corresponding hedge items which is meeting the effectiveness test but is not fully effective, amortisation of initial fair value adjustments recognised for the hedged items. Termination of ineffective hedges are also included here.

Investments held at fair value include the fair value gains and losses on equity shares investment.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

6. Impairment of financial assets

The following table splits the income statement impairment of financial assets into those elements impacting the ECL and other items.

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Impairment charge on loans and advances to customers	**7.6**	0.5	7.0
Recoveries relating to loans and advances previously written off	**(0.4)**	0.2	(0.9)
Impairment of other financial assets	**0.3**	–	(0.1)
Impairment charge	**7.5**	0.7	6.0

7. Movement in provisions

The provisions (release)/charge for the period is outlined below:

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Restructuring	**(0.2)**	0.5	0.9
Property related provision	**(0.6)**	2.2	3.3
Total provisions (release)/charge	**(0.8)**	2.7	4.2

During the course of its business, the Society receives complaints in relation to past sales or ongoing administration, as well as being subject to enquiries from and discussions with its regulators and governmental and other public bodies, on a range of matters. The Society may also identify compliance matters through the course of business operation and monitoring. No provision is made where it is concluded that it is not probable that a reliably quantifiable payment will be made; this will include circumstances where the facts are unclear or further time or information is required to reasonably quantify the expected payment.

A contingent liability exists relating to a potential regulatory conduct matter. It is too early to determine the extent of any customer, financial and/or regulatory impact, if any.

8. Tax expense

On 1 April 2023 the UK corporation tax rate increased from 19% to 25%. This measure was substantively enacted on 24 May 2021 and deferred tax assets and liabilities at 30 June 2023, at 31 December 2022 and at 30 June 2022 have all been calculated based on the 25% rate.

On 1 April 2023 the banking surcharge decreased from 8% (on taxable profits in excess of £25 million) to 3% (on taxable profits in excess of £100 million). This change was substantively enacted on 2 February 2022. Deferred tax assets and liabilities at 30 June 2023, at 31 December 2022 and at 30 June 2022 have all been calculated based on the 3% rate.

The Group has an effective tax rate of 26.4%, which is higher than the average UK statutory corporation tax rate of 23.5% for the year. This is mainly due to the effects of the banking surcharge on the taxable profits of the Society.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers

Gross contractual exposure

The table below splits the loans and advances to customers balance per the consolidated balance sheet into its constituent parts and reconciles to the gross exposures used in the Expected Credit Losses (ECL) model. Effective Interest Rate (EIR) adjustments have been excluded from the ECL model as these do not form part of the contractual cash flows from the assets.

EIR is the measurement method used for financial assets held at amortised cost, including loans and advances to customers, which spreads income and fees over the life of the asset. See note 1 for more details. The fair value rate adjustment reflects the market value adjustment on acquired portfolios of mortgage assets in respect of interest rates on the underlying products. This is amortised over the expected life of the acquired portfolio. The fair value credit adjustment is the fair value discount applied on purchased or originated credit impaired (POCI) mortgage assets acquired as part of the Norwich & Peterborough Building Society (N&P) and Chelsea Building Society (CBS) acquisitions. Impairment represents the difference between the total ECL and the fair value credit adjustment.

ECL are calculated using models that take historical default and loss experience and apply predictions of future economic conditions (e.g. unemployment and house prices) and customer behaviour (e.g. default rates). In certain circumstances, the core models may not accurately reflect factors that are considered to result in a change in credit risk. When this happens, post model adjustments ('PMA') are overlaid to reflect the impact on ECL. The economic scenarios and the PMAs applied at 30 June 2023 are described below.

	30 June 2023 (unaudited) £m	30 June 2022 (unaudited) £m	31 December 2022 (audited) £m
Gross contractual exposures	**45,923.8**	44,265.9	45,252.1
EIR and other adjustments	**43.7**	49.9	49.7
Fair value rate adjustment	**(35.0)**	(43.8)	(39.7)
Gross loans and advances to customers	**45,932.5**	44,272.0	45,262.1
Impairment	**(40.7)**	(26.7)	(33.1)
Fair value credit adjustment	**(23.7)**	(27.0)	(25.3)
ECL	**(64.4)**	(53.7)	(58.4)
Loans and advances to customers	**45,868.1**	44,218.3	45,203.7

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

Analysis of changes in ECL

The following tables analyse the changes in ECL, split by impairment and fair value credit adjustments.

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Opening impairment	**33.1**	26.1	26.1
Amounts written off in the period	**(0.7)**	(0.4)	(1.0)
Discounting recognised in net interest income	**0.7**	0.5	1.0
Charge for the period recognised in the income statement	**7.6**	0.5	7.0
Impairment	**40.7**	26.7	33.1

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Opening fair value credit adjustment	**25.3**	28.4	28.4
Release recognised in the income statement through net interest	**(1.5)**	(1.3)	(2.4)
Write-offs	**(0.1)**	(0.1)	(0.7)
Fair value credit adjustment	**23.7**	27.0	25.3

ECL

Economic Scenarios

Accounting standards require ECL to be calculated by applying multiple economic scenarios. Each economic scenario is provided a weighting, and these are combined to arrive at the total ECL.

These scenarios are generated internally using external data, statistical methodologies, and management judgement, to span a range of plausible economic conditions. The Group continues to use four scenarios: an upside scenario that assumes more benign economic conditions; our core or central best estimate scenario; a downturn scenario that assumes more adverse economic conditions; and a more severe downturn scenario. The downturn scenario replaced the stagflation downturn scenario from 2022 year end.

Scenarios are projected over a 5 year window, reverting to long-term averages past that point. The Group allows all macro-economic scenarios to impact staging.

Current Macroeconomic Conditions

The UK Economy is expected to avoid a recession, which was widely predicted throughout 2022, as a result of reducing energy prices, a more resilient global environment and continued tightness in the labour market. Growth will likely remain weak by historical standards and there remains more downside risk than upside.

Inflation is falling from its peak, albeit slower than anticipated given movements in energy prices. Services pricing and pay growth signals continued underlying price pressure elevating core inflation.

The Bank of England responded to rising inflation with a succession of rate rises, with the last one in June taking the interest rate to 5.0%. Further increases are anticipated before the end of the year.

Upside

This assumes measures to reduce inflation succeed sooner than anticipated and GDP reverts to pre-pandemic levels during 2023. Unemployment remains lows and house prices grow at a moderate rate.

Core

The core scenario is the Group's best estimate of how the UK economy will evolve and is aligned with the central scenario used in the Group's financial planning processes.

It assumes a reduction in consumer spending, falling energy prices and base rate effects will lower inflation to 4.3% by the end of 2023. Continued Bank Rate rises during 2023 result in a peak of 5.8%.

GDP retracts by 0.7% in 2023 with this slowdown being driven by the fall in real household disposable income and rising interest rates exacerbated by the sustained rise in Consumer Price Inflation (CPI). Unemployment increases as a result and house prices reduce further. This downturn is short lived as lower borrowing costs bring back activity with price growth returning to 3.0% by 2027.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

ECL (continued)

Economic Scenarios (continued)

Downturn

The consecutive Bank of England base rate increases work to bring inflation under control by the end of 2023 and below 2.0% by 2027. Bank rates reduce to 2.0% by the end of 2024 and decrease to 1.5% in 2027.

Although inflation and bank rates start to ease up, house prices continue to fall, unemployment rises and real earnings growth remains negative.

Severe Downturn

The recession in the UK deepens as the economy contracts by over 4.0% in 2023. This is driven by the current monetary tightening cycle becoming more severe, low consumer confidence, sharp fall in business investment, government austerity measures and a global economic downturn.

Without government support measures unemployment peaks at 8.8% in 2024 which in turn drives house prices down by 34.0% (peak to trough).

Macroeconomic variables

The following table shows the values of the key variables used by each economic scenario for the period until December 2027. The table includes the three key parameters used to predict probability of default (PD) – unemployment, HPI and Bank of England base rate. GDP is also presented as it is the key input for determining the economic parameters used and provides context to the nature of the overall scenario.

Household disposable income is forecast to decrease in our economic scenarios as a result of sharply rising inflation and increases in the cost-of-living, combined with higher interest rates and the downward movement in house prices in the short term. This is assumed to lead to affordability pressures which are expected to impact on customers' ability to meet mortgage repayments. This risk is not directly captured in our models.
See the Affordability post model adjustment below for details on how this risk has been assessed and incorporated into ECL.

	June 2023 Scenario (unaudited)					December 2022 Scenario (audited)				
	2023	**2024**	**2025**	**2026**	**2027**	2023	2024	2025	2026	2027
HPI										
Upside	**1.3**	**2.2**	**3.2**	**3.2**	**3.2**	–	1.5	2.2	3.2	3.2
Core	**(6.0)**	**(2.0)**	**1.5**	**2.5**	**3.0**	(6.0)	(2.0)	1.3	2.0	2.0
Downturn	**(10.2)**	**(4.1)**	**1.5**	**2.2**	**2.9**	(12.7)	(5.0)	–	1.5	1.7
Severe downturn	**(14.5)**	**(11.8)**	**(6.8)**	**–**	**0.5**	(13.5)	(11.8)	(6.8)	–	0.5
GDP										
Upside	**0.5**	**2.0**	**2.1**	**2.0**	**2.0**	1.5	2.0	2.1	2.0	2.0
Core	**(0.7)**	**1.1**	**1.6**	**1.8**	**1.7**	(1.5)	0.8	1.6	1.8	1.8
Downturn	**(2.5)**	**0.3**	**0.4**	**1.2**	**1.8**	(6.3)	(5.3)	0.4	0.6	1.0
Severe downturn	**(4.2)**	**(3.0)**	**(1.1)**	**0.1**	**0.5**	(7.4)	(5.3)	(1.2)	–	0.2
Unemployment										
Upside	**3.9**	**4.0**	**4.0**	**4.1**	**4.1**	3.5	3.6	3.6	3.8	3.8
Core	**4.4**	**4.6**	**4.6**	**4.6**	**4.7**	4.9	5.5	5.2	4.8	4.5
Downturn	**5.5**	**6.5**	**6.5**	**6.0**	**5.5**	6.5	7.0	6.7	6.5	6.0
Severe downturn	**7.1**	**8.8**	**8.4**	**6.5**	**5.7**	7.1	8.8	8.4	8.0	7.5
Bank Rate										
Upside	**4.0**	**3.8**	**3.5**	**3.3**	**3.0**	2.0	2.0	1.5	1.5	1.5
Core	**5.8**	**5.3**	**4.8**	**4.3**	**4.0**	4.8	4.3	4.0	3.8	3.5
Downturn	**2.0**	**1.5**	**1.5**	**1.5**	**1.5**	6.3	5.5	5.0	4.8	4.5
Severe downturn	**2.0**	**–**	**–**	**–**	**–**	2.0	–	–	–	–

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

ECL (continued)

Weightings

The following table shows the expected credit loss under each of our four economic scenarios along with the weightings that have been applied to arrive at the weighted average ECL. PMAs are calculated using the weighted scenario results and so their sensitivity in each of the individual scenarios cannot be accurately determined. For completeness they have been included as a uniform adjustment across each scenario.

	30 June 2023 (unaudited)		31 December 2022 (audited)	
Scenario	**Weighted %**	**ECL £m**	Weighted %	ECL £m
Upside scenario	**5**	**36.8**	5	37.6
Core scenario	**40**	**41.1**	50	40.7
Downturn scenario	**35**	**66.6**	30	73.5
Severe downturn Scenario	**20**	**114.0**	15	94.2
Probability weighted ECL	**100**	**64.4**	100	58.4

Probability weightings have been reviewed during the period and updated to reflect economic conditions.

The core scenario weighting has decreased and the downturn and severe downturn scenario weightings have increased to reflect increased risks associated with inflation remaining higher for longer, mortgage affordability pressure due to the increases in Bank Rate to date and the ongoing economic consequences of the conflict in Ukraine.

SME judgment is applied in the final assessment of weights, informed both by an assessment of external data and statistical model results.

Post Model Adjustments

Post model adjustments ('PMA') are applied when a change in credit risk is identified that is not effectively captured in the core expected credit loss models.

PMAs are reviewed throughout the year to determine whether the identified risks are still applicable.

The PMAs applied at 30 June 2023 are as follows:

	30 June 2023 (unaudited) £m	31 December 2022 (audited) £m
Affordability	**16.9**	10.8
Uncertainty	**2.8**	7.1
Methodology changes	**–**	5.5
Model recalibration	**–**	1.1
Total PMA	**19.7**	24.5

Affordability

The affordability PMA reflects the risks of rising inflation, and its impact on customers' ability to meet repayments on their mortgage, not captured in the underlying ECL models.

Inflation is not a direct input into the models and, as such, does not have a direct influence on the output. Secondary impacts on other measures such as house prices will eventually feed into the model but there is an element of short-term insensitivity, particularly in a period of high inflation.

Although the lending undertaken by the Society is risk-averse, with a significant amount of affordability assessment undertaken as part of the decision to advance mortgage loans, there are several segments of the mortgage book that are likely to be at greater risk of affordability stresses due to the cost-of-living pressures.

The PMA applies a stress to the monthly expenditure amounts in the mortgage book affordability calculation. With affordability only measured at application stage, additional considerations were applied to earnings indexed using UK wage growth since completion. Further stress is applied to the book to reflect external pressures such as increase in outgoings, interest rate changes, cost-of-living challenges

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

ECL (continued)

Post Model Adjustments (continued)

Affordability (continued)

and income decreases. To estimate this impact, external credit data was sourced for a sample of the book using a series of affordability scenarios and this was then extrapolated for the remainder of the book.

The PMA has moved significantly since year end as a result of an increased exposure at default (EAD), largely as a result of HPI decreases and an update to the expenditure assumptions within the Society's affordability model, resulting in a greater proportion of accounts being identified as higher risk.

Further consideration has been given to the BTL book where the Society has assessed whether the coverage is sufficient to cover the increased risk to the book given the current macro-economic climate. Relative insensitivity to the stresses provided above was found and so an additional provision has been raised to cover this underestimation by applying an appropriate uplift factor based on the behaviour of a similar cohort of mortgages.

Uncertainty

Whilst we incorporate a range of economic assumptions in the scenarios and probability weightings used to calculate ECL, this approach still has certain limitations, particularly given the current volatility in market conditions. The resulting unusual and largely unforeseen impacts on the credit risks faced by the Society have given rise to several assumption uncertainties and a PMA has been established to aim to correct for these.

The key risks that this PMA provides an estimate for are provided below.

House Price Volatility

This PMA had been developed in response to extraordinary growth in house prices since the easing of the first COVID-19 lockdown and at year-end formed a significant proportion of the total uncertainty PMA (£5.7 million).

The initial part of this PMA aims to correct for the changes in HPI at a regional level that are not evenly distributed and the ECL impact of changes in collateral values are therefore not linear. This PMA is to correct for the standard deviation from the regional type mean, it is not an attempt to correct for any perceived current market wide over-valuation. A third party analysed the YBS portfolio using automated valuation models (AVM) for risk of over or under indexation, with a specific focus on geographical location, management have used this evaluation as support for this £1.0 million PMA recognised in relation to this risk.

The latter part of the PMA relates to the risk that the ONS (Office for National Statistics) indexation data that is incorporated into the ECL model on a quarterly basis is not a true representative of the market conditions as at 30 June 2023. The latest indexation from ONS was for data collected in Q1 of 2023. This PMA aims to correct for the update in market conditions by using an average of Nationwide and Halifax more recent indexations for Q2 of 2023. At year-end there were sizeable reductions observed in Q4 within Halifax and Nationwide's HPI outputs which generated more risk to ECLs and a charge was recognised as a result. However the results for Q2 2023 have been marginally positive leading to a release of £0.1 million. The total House Price Volatility PMA for half year is £0.9 million (December 2022: £5.7 million).

Climate risk

We have assessed the risks associated with climate change, both physical and transitional, in the context of ECL and concluded that the majority of these risks do not meet the requirements for recognition as:

- There have been no observed climate related defaults and therefore no identifiable significant increase in credit risk (SICR); and
- The material transition risks identified are expected to occur over a timescale in excess of the current behavioural life of our portfolio (i.e. the average term before a customer either moves onto an alternative deal or transfers to another provider) and, as such, any potential impact would be against loans yet to be underwritten.

A PMA of £1.0 million had previously been established due to the potential impact on our current loan book from properties subject to significant flood risk. The society have reviewed the PMA and given greater consideration to the impact of transitional risks rather than physical risks of the type previously considered.

The most immediate transitional risk is considered to relate to BTL accounts where the UK Government has proposed that all rental properties will need an Energy Performance Certificate (EPC) rating of 'C' or above by 2028.

Each residential property on the portfolio has a current and potential EPC grade and different treatments have been established based on these levels to either reduce the valuation of the property to land value in line with the treatment within the Society's Climate Risk models or to incorporate the costs associated with upgrading the property to these minimum levels. A PMA of £1.5 million has been recognised to reflect this.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

ECL (continued)

Post Model Adjustments (continued)

Uncertainty (continued)

Climate risk (continued)

The regulation will come into force in December 2028, meaning that any required improvements to properties can be phased in between now and then. Given this, it was not believed to be appropriate to realise the full impacts of the improvement costs/ reductions to land value immediately and a means of phasing the impacts based on the proximity to the regulations being adopted has been incorporated for specific EPC grades.

Standard Variable Rate (SVR)

The Bank of England has continued to increase the bank base rate during the first half of 2023 to help bring inflation under control with the base rate increasing from 3.5% at the beginning of the year to 5.0% as of June. The latest BoE Base Rate increase has not been incorporated into the Society's variable rates yet and so this PMA aims to estimate this impact on ECL. The payment amount at account level is recalculated annually to reflect the change in SVR rate, therefore it is not reflected in the ECL model until the annual recalculation takes place. This PMA was originally raised at year end to estimate the impact of the December bank base rate increase which has since been applied at account level. This PMA has been maintained at £0.4 million (December 2022: £0.4 million) and will be released when the updated SVR rate is applied.

Methodology Changes and Model Recalibration

All iterations of IFRS 9 models developed and implemented within the Society have sought to align to the IRB models within the business where appropriate with the definition of default (DoD) / definition of impairment a key area of focus. A PMA was established at 30 June 2021 to provide a high-level overlay to reflect the impacts of moving to the Society's fourth generation IRB models with this primarily covering:

- Additional accounts that would be classified as being Stage 3 due to meeting the additional default criteria.
- Accounts that would more likely be classified as Stage 2 due to an increase in risk, either by their transition to a higher rating grade, or to a higher risk PD model.
- Reflected changes to the eligibility of accounts meeting the definition of a significant increase in credit risk (SICR). The changes use initial recognition PD as a comparison point for SICR rather than lifetime PD.

In addition to this a PMA was also held in relation to impacts from a recalibration to the third generation IRB PD rating scale model.

There was a known misalignment between the initial recognition PDs and the current PDs compared within staging transfer criteria for accounts that originated prior to the implementation of the third generation model recalibration. The enhancements that have been made within the fourth generation development to correct this resulted in considerable reductions to stage 2 volumes. Establishing transfer criteria on a consistent basis for the full core population has resulted in more intuitive movements in the risk profile of the different stages.

Fourth generation IFRS 9 models and impacts were presented to the Society's Model Risk Committee in 2023 and approved for use. These have been used as the basis for generating Core model ECLs for this reporting period. Both the Methodology Changes and Model Recalibration PMAs have been released as they are no longer required and the reduction in ECL associated with the stage 2 movement noted above has outweighed other aspects of the migration to the fourth generation models that would have increased ECLs, leading to an overall release on initial implementation.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

ECL (continued)

Staging and POCI

The tables below shows the staging of loans and advances plus assets considered to be purchased or originated credit impaired ('POCI') recognised as part of the acquisitions of Norwich & Peterborough Building Society ('N&P') and Chelsea Building Society ('CBS'). The discount on acquisition is recognised as the fair value credit adjustment.

Details of the movements in staging are explained in the *movement analysis* section of this note.

	30 June 2023 (unaudited)		31 December 2022 (audited)	
	£m	**%**	£m	%
Gross exposures by stage				
Stage 1	**42,962.8**	**93.5**	40,251.1	88.9
Stage 2	**2,230.1**	**4.9**	4,277.3	9.5
Stage 3	**363.5**	**0.8**	338.3	0.7
POCI	**367.4**	**0.8**	385.4	0.9
Total gross exposures	**45,923.8**	**100.0**	45,252.1	100.0
Problem loans (stage 3 plus non-performing POCI)	**406.5**	**0.9**	384.7	0.9
ECL and coverage ratio by stage				
Stage 1	**23.5**	**0.1**	7.5	–
Stage 2	**15.3**	**0.7**	26.3	0.6
Stage 3	**11.7**	**3.2**	11.3	3.3
POCI	**13.9**	**3.8**	13.3	3.5
Total ECL	**64.4**	**0.1**	58.4	0.1

The Group has £367.4 million of POCI loans. Of these, 88% are now considered performing loans but are not permitted to be reclassified to stage 1 or 2. Problem loans represent the total of the Group's stage 3 balances and the non-performing portion of our POCI loans.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

ECL (continued)

Staging and POCI (continued)

The following table shows the staging split by days overdue.

	Gross exposure		ECL	
	30 June 2023 (unaudited) £m	31 December 2022 (audited) £m	**30 June 2023 (unaudited) £m**	31 December 2022 (audited) £m
Stage 1	**42,962.8**	40,251.1	**23.5**	7.5
Stage 2:	**2,230.1**	4,277.3	**15.3**	26.3
Less than 30 days past due	**2,100.8**	4,156.1	**12.7**	24.7
More than 30 days past due	**129.3**	121.2	**2.6**	1.6
Stage 3:	**363.5**	338.3	**11.7**	11.3
Less than 30 days past due	**166.7**	155.6	**3.3**	3.7
30-90 days past due	**74.0**	64.9	**1.4**	1.4
More than 90 days past due	**122.8**	117.8	**7.0**	6.2
POCI:	**367.4**	385.4	**13.9**	13.3
Less than 30 days past due	**327.7**	346.7	**11.4**	10.9
30-90 days past due	**28.1**	20.8	**1.6**	0.8
More than 90 days past due	**11.6**	17.9	**0.9**	1.6
Total	**45,923.8**	45,252.1	**64.4**	58.4

All accounts in stage 1 are less than 30 days past due.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

Risk assessment

The following tables are included to give an overview of the Group's credit risk.

Lending by Risk Grade

The risk models cover the majority of loans underwritten by the Group, with exceptions for portfolios subject to bespoke modelling requirements including Accord buy-to-let, commercial lending and POCI accounts. The Accord BTL population currently has very strict underwriting criteria and limited behavioural history, with only a single possession to date. Commercial lending has significantly different behavioural characteristics to the retail mortgages.

Gross exposures in the table below are presented pre PMAs being applied.

	30 June 2023 (unaudited)						31 December 2022 (audited)	
	Gross exposure					ECL	Gross exposure	ECL
	Stage 1	Stage 2	Stage 3	POCI	Total			
Probability of default range	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	£m	£m
0.00%–<0.15%	**31,109.1**	**619.1**	**–**	**–**	**31,728.2**	**1.7**	32,792.6	1.7
0.15%–<0.25%	**2,278.0**	**265.1**	**–**	**–**	**2,543.1**	**1.3**	1,888.6	0.7
0.25%–<0.50%	**613.0**	**135.3**	**–**	**–**	**748.3**	**0.8**	484.6	0.3
0.50%–<0.75%	**389.6**	**204.2**	**–**	**–**	**593.8**	**0.6**	583.6	0.7
0.75%–<1.00%	**215.2**	**152.2**	**–**	**–**	**367.4**	**0.6**	334.1	0.8
1.00%–<2.50%	**302.6**	**414.6**	**–**	**–**	**717.2**	**2.5**	698.2	3.4
2.50%–<10.0%	**62.8**	**168.3**	**–**	**–**	**231.1**	**2.2**	205.1	2.5
10.0%–<100%	**7.6**	**134.8**	**–**	**–**	**142.4**	**2.4**	116.4	2.3
Default	**–**	**–**	**355.7**	**31.4**	**387.1**	**12.4**	366.6	11.8
Accord buy-to-let	**6,204.0**	**71.8**	**5.6**	**–**	**6,281.4**	**2.1**	5,905.6	6.3
Commercial	**1,593.5**	**38.1**	**2.2**	**11.6**	**1,645.4**	**7.1**	1,510.6	3.7
Other*	**187.4**	**26.6**	**–**	**324.4**	**538.4**	**11.0**	366.1	24.9
PMAs	**–**	**–**	**–**	**–**	**–**	**19.7**	–	–
Total	**42,962.8**	**2,230.1**	**363.5**	**367.4**	**45,923.8**	**64.4**	45,252.1	58.4

* Other includes Registered Social Landlords and POCI accounts.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

Risk assessment (continued)

Lending by origination year

	30 June 2023 (unaudited)						31 December 2022 (audited)	
	Gross exposure					ECL	Gross exposure	ECL
Origination year	Stage 1 £m	Stage 2 £m	Stage 3 £m	POCI £m	Total £m	£m	£m	£m
2023	**3,645.1**	**38.3**	**3.9**	**–**	**3,687.3**	**3.4**	–	–
2022	**9,671.1**	**151.9**	**25.0**	**–**	**9,848.0**	**8.6**	10,184.5	7.6
2021	**8,315.5**	**251.5**	**31.4**	**–**	**8,598.4**	**7.3**	9,260.3	6.3
2020	**4,391.3**	**208.3**	**22.9**	**–**	**4,622.5**	**3.6**	4,914.3	3.6
2019	**4,257.3**	**194.4**	**29.7**	**–**	**4,481.4**	**3.3**	4,720.2	3.3
2013 – 2018	**10,057.0**	**430.4**	**74.2**	**–**	**10,561.6**	**10.4**	11,732.6	8.6
2009 – 2012	**907.5**	**57.2**	**7.4**	**–**	**972.1**	**0.6**	1,056.3	0.6
Pre-2009	**771.0**	**593.9**	**106.2**	**–**	**1,471.1**	**6.6**	1,560.7	6.4
Acquired loans	**947.0**	**304.2**	**62.8**	**367.4**	**1,681.4**	**20.6**	1,823.2	22.0
Total	**42,962.8**	**2,230.1**	**363.5**	**367.4**	**45,923.8**	**64.4**	45,252.1	58.4

Lending by Loan to value

	30 June 2023 (unaudited)					31 December 2022 (audited)
	Gross exposure					Gross exposure
Loan to value	Stage 1 £m	Stage 2 £m	Stage 3 £m	POCI £m	Total £m	£m
Less than 60%	**21,109.3**	**1,535.2**	**237.4**	**312.6**	**23,194.5**	24,364.8
60% to 75%	**14,252.3**	**474.6**	**101.3**	**43.8**	**14,872.0**	15,198.8
75% to 90%	**6,935.8**	**205.3**	**22.2**	**6.3**	**7,169.6**	5,550.6
90% or greater	**665.4**	**15.0**	**2.6**	**4.7**	**687.7**	137.9
Total	**42,962.8**	**2,230.1**	**363.5**	**367.4**	**45,923.8**	45,252.1
Average LTV (%)	**49.7**	**35.1**	**41.6**	**41.0**	**48.4**	46.8

Movement analysis

The table on page 33 details the movement in the gross exposures and ECL from the beginning to the end of the reporting period split by stage.

The Society has updated the definition of default and the probability of default rating scale on the back of a comprehensive review as part of the transition to the fourth generation internal ratings based (Gen 4 IRB) method of calculating regulatory capital. These model updates were approved for use in the core underlying models in the first half of this year and all ECL outputs have been updated to reflect these changes.

There was a known misalignment between the initial recognition PDs and the current PDs compared within staging transfer criteria for accounts that originated prior to the implementation of the third generation model recalibration which took place in 2018. Enhancements have been made within the fourth generation developments to correct this, resulting in a large reduction of stage 2 volumes and associated ECLs. This can be seen on the Transfers from stage 2 to 1 line of the gross exposures movement table.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

Movement analysis (continued)

Separate to the fourth generation model update, we have reconsidered the affordability PMA disclosure. All balances in relation to the affordability PMA are recognised in stage 1 and have been recognised here due to the accounts identified through the PMA not moving into arrears or meeting any of the quantitative (i.e. SICR thresholds) or qualitative criteria for being assigned to stage 2. Of the £43.0 billion balances in stage 1, £15.3 billion are captured by this PMA representing 35.6% of stage 1 balances that are deemed to be at risk of an increase in credit risk as a result of affordability pressures. The PMA movement from stage 2 to stage 1 can be seen on the PMA line of the ECL movement table below. We continue to monitor the risks in ECL and the stage criteria.

	Stage 1 £m	Stage 2 £m	Stage 3 £m	POCI £m	Total £m
Gross exposure at 31 December 2022	**40,251.1**	**4,277.3**	**338.3**	**385.4**	**45,252.1**
Transfers from stage 1 to 2	**(823.9)**	**823.9**	**–**	**–**	**–**
Transfers from stage 1 to 3	**(25.2)**	**–**	**25.2**	**–**	**–**
Transfers from stage 2 to 1	**2,615.4**	**(2,615.4)**	**–**	**–**	**–**
Transfers from stage 2 to 3	**–**	**(51.2)**	**51.2**	**–**	**–**
Transfers from stage 3 to 1	**8.1**	**–**	**(8.1)**	**–**	**–**
Transfers from stage 3 to 2	**–**	**23.0**	**(23.0)**	**–**	**–**
Changes to carrying value	**(652.8)**	**(43.9)**	**(0.6)**	**(4.2)**	**(701.5)**
New financial assets originated or purchased	**3,499.3**	**–**	**–**	**–**	**3,499.3**
Financial assets derecognised during the period	**(1,909.2)**	**(183.6)**	**(17.8)**	**(13.0)**	**(2,123.6)**
Write-offs	**–**	**–**	**(1.7)**	**(0.8)**	**(2.5)**
Gross exposure at 30 June 2023	**42,962.8**	**2,230.1**	**363.5**	**367.4**	**45,923.8**
ECL at 31 December 2022	**7.5**	**26.3**	**11.3**	**13.3**	**58.4**
Transfers from stage 1 to 2	**(0.1)**	**5.1**	**–**	**–**	**5.0**
Transfers from stage 1 to 3	**–**	**–**	**1.0**	**–**	**1.0**
Transfers from stage 2 to 1	**0.4**	**(4.6)**	**–**	**–**	**(4.2)**
Transfers from stage 2 to 3	**–**	**(0.7)**	**1.9**	**–**	**1.2**
Transfers from stage 3 to 1	**–**	**–**	**(0.2)**	**–**	**(0.2)**
Transfers from stage 3 to 2	**–**	**0.3**	**(0.4)**	**–**	**(0.1)**
Changes in PDs/LGDs/EADs	**(2.0)**	**6.1**	**0.2**	**1.1**	**5.4**
New financial assets originated or purchased	**2.0**	**–**	**–**	**–**	**2.0**
Changes to model assumptions and methodologies	**0.5**	**1.0**	**1.6**	**0.3**	**3.4**
Unwind of discount	**–**	**–**	**0.3**	**0.4**	**0.7**
Financial assets derecognised during the period	**(0.1)**	**(0.8)**	**(0.6)**	**(0.7)**	**(2.2)**
Write-offs	**–**	**–**	**(0.8)**	**(0.5)**	**(1.3)**
PMA	**15.3**	**(17.4)**	**(2.6)**	**–**	**(4.7)**
ECL at 30 June 2023	**23.5**	**15.3**	**11.7**	**13.9**	**64.4**

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

9. Credit risk on loans and advances to customers (continued)

Loans Purchased or Originated Credit Impaired (POCI)

The table below shows the status of the Group's POCI loans. A substantial proportion of POCI balances, were they not required to be classified as stage 3 by accounting standards, would transfer to other stages. The table below shows that 71.0% (Dec 2022: 71.9%) of balances have been fully up to date for the last 24 months and only 11.7% (Dec 2022: 12.0%) of balances would be classified as in default.

	Up to date for the last 24 months £m	Some arrears in the last 24 months £m	Meets definition of default £m	Total £m
At 30 June 2023 (unaudited)				
Gross exposure	**260.9**	**63.5**	**43.0**	**367.4**
ECL	**8.1**	**3.4**	**2.4**	**13.9**
At 31 December 2022 (audited)				
Gross exposure	277.1	61.9	46.4	385.4
ECL	7.6	3.3	2.4	13.3

10. Retirement benefit obligations

Reconciliation of funded status

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Present value of defined benefit retirement obligation	**(574.0)**	(696.4)	(593.4)
Assets at fair value	**610.5**	787.3	642.2
Funded status/defined benefit asset	**36.5**	90.9	48.8

Unfunded defined benefit scheme

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Present value of unfunded defined benefit scheme	**(7.2)**	n/a*	(7.4)

* As at 30 June 2022, the unfunded DB scheme liabilities were reported within the funded DB scheme liabilities balance.

The present value at 30 June 2023 of the unfunded defined benefit scheme was £7.2 million (30 June 2022: £8.9 million) and the relevant disclosures have been separated from those of the main employee benefits scheme where appropriate.

The present value of the defined benefit obligation as at 30 June 2023 has been calculated using assumptions that are derived consistently with those used for the 31 December 2022 year end, allowing for updated market conditions.

Liabilities have reduced overall, mainly driven by the increase in the discount rate given high Government Bond yields as a result of the rising interest rate environment. This has been partially offset by actual inflation being higher than that expected per the pension accounting assumptions. Future long-term expectations of inflation have also increased slightly.

Asset returns over the first half of the year have been less than the discount rate. While this has been partially offset by the decrease in liabilities over the half year, the overall result is a reduction of the Surplus by £12.1 million.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

11. Related parties

There have been no material changes to related parties and the associated related party transactions since the year end. For further information on these see pages 222 to 224 of the 2022 Annual Report and Accounts.

12. Notes to the consolidated statement of cash flows

	Half-year to 30 June 2023 (unaudited) £m	Half-year to 30 June 2022 (unaudited) £m	Year to 31 December 2022 (audited) £m
Depreciation and amortisation	**9.7**	10.9	21.8
Loss/(profit) on sale of assets	**–**	–	(2.4)
Interest on subordinated liabilities	**17.2**	15.3	33.7
Impairment charge/(release) for the year	**7.5**	0.7	6.0
Provisions (release)/charge	**(0.8)**	2.7	4.2
Non-cash movement in subordinated liabilities	**(26.9)**	(54.8)	(122.6)
(Gain)/loss on realisation of debt securities	**(1.5)**	(2.4)	(2.9)
(Increase)/decrease in cash ratio deposit, other assets and non-OCI element of retirement benefit surplus	**(8.1)**	(12.2)	(3.2)
Cash movements in other liabilities and provisions	**1.5**	(6.7)	(18.5)
Movement in fair value adjustment for hedged risk on loans and advances to customers	**283.8**	667.8	1,270.1
Non-cash items included in profit before tax	**282.4**	621.3	1,186.2
(Increase)/decrease in operating assets			
Non-impairment change in loans and advances to customers	**(671.9)**	(2,058.4)	(3,049.1)
Investments	**(0.2)**	0.2	2.6
Non-OCI elements of derivative financial assets	**(641.4)**	(956.3)	(1,867.6)
Net change in operating assets	**(1,313.5)**	(3,014.5)	(4,914.1)
Increase/(decrease) in operating liabilities			
Shares	**3,624.6**	2,232.6	6,501.8
Amounts owed to credit institutions	**(785.1)**	479.8	(928.9)
Non-cash movements on debt securities in issue	**(58.5)**	(99.5)	(117.9)
Other deposits	**(110.8)**	249.8	264.6
Derivative financial liabilities	**242.3**	194.6	393.6
Net change in operating liabilities	**2,912.5**	3,057.3	6,113.2

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

12. Notes to the consolidated statement of cash flows (continued)

The following tables reconcile liabilities arising from financing activities.

Liabilities from financing activities	Brought forward (audited)	Cash flows Redemption	Cash flows Issue	Non-cash changes caused by: Foreign exchange	Non-cash changes caused by: Accrued interest	Non-cash changes caused by: Fair value and other movements	Carried forward (unaudited)
	£m	£m	£m	£m	£m	£m	£m
Period to 30 June 2023							
Debt securities in issue	5,259.3	**(796.3)**	**1,005.3**	**(86.0)**	**–**	**27.5**	**5,409.8**
Subordinated liabilities	1,035.1	**(136.4)**	**350.0**	**–**	**9.8**	**(36.7)**	**1,221.8**
Total	6,294.4	**(932.7)**	**1,355.3**	**(86.0)**	**9.8**	**(9.2)**	**6,631.6**
Period to 30 June 2022							
Debt securities in issue	5,890.9	(417.5)	635.0	102.9	(3.1)	(199.3)	6,008.9
Subordinated liabilities	857.7	–	300.0	–	4.8	(59.6)	1,102.9
Total	6,748.6	(417.5)	935.0	102.9	1.7	(258.9)	7,111.8
Year to 31 December 2022							
Debt securities in issue	5,890.9	(1,225.2)	711.5	198.6	6.9	(323.4)	5,259.3
Subordinated liabilities	857.7	–	300.0	–	2.3	(124.9)	1,035.1
Total	6,748.6	(1,225.2)	1,011.5	198.6	9.2	(448.3)	6,294.4

Cash and balances with central banks

Cash and cash equivalents excludes cash ratio deposits of £178.2 million (30 June 2022: £163.8 million) held with the Bank of England, which are not available for use in the Group's day-to-day operations.

13. Fair values

Fair value is the price that would be received to sell 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).

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

13. Fair values (continued)

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

Held at amortised cost	Carrying value £m	Level 1 £m	Fair values Level 2 £m	Level 3 £m	Total fair value £m
30 June 2023 (unaudited)					
Assets					
Loans and advances to credit institutions	**450.5**	**–**	**450.5**	**–**	**450.5**
Loans and advances to customers	**45,868.1**	**–**	**–**	**43,031.2**	**43,031.2**
Debt securities – amortised cost	**2,119.9**	**2,103.7**	**–**	**–**	**2,103.7**
Liabilities					
Shares	**45,632.8**	**–**	**45,341.2**	**–**	**45,341.2**
Amounts owed to credit institutions	**4,375.8**	**–**	**4,375.8**	**–**	**4,375.8**
Other deposits	**1,027.3**	**–**	**1,027.3**	**–**	**1,027.3**
Debt securities in issue	**5,409.8**	**5,810.0**	**817.8**	**–**	**6,627.8**
Subordinated liabilities	**1,221.8**	**1,169.2**	**33.8**	**–**	**1,203.0**
30 June 2022 (unaudited)					
Assets					
Loans and advances to credit institutions	617.8	–	617.8	–	617.8
Loans and advances to customers	44,218.3	–	–	43,891.9	43,891.9
Debt securities – amortised cost	980.0	949.8	–	–	949.8
Liabilities					
Shares	37,739.0	–	37,662.4	–	37,662.4
Amounts owed to credit institutions	6,569.6	–	6,569.6	–	6,569.6
Other deposits	1,123.3	–	1,123.3	–	1,123.3
Debt securities in issue	6,008.9	6,428.7	783.8	–	7,212.5
Subordinated liabilities	1,102.9	1,029.8	35.9	–	1,065.7
31 December 2022 (audited)					
Assets					
Loans and advances to credit institutions	814.7	–	814.7	–	814.7
Loans and advances to customers	45,203.7	–	–	43,002.8	43,002.8
Debt securities – amortised cost	1,366.6	1,352.3	–	–	1,352.3
Liabilities					
Shares	42,008.2	–	41,835.3	–	41,835.3
Amounts owed to credit institutions	5,160.9	–	5,160.9	–	5,160.9
Other deposits	1,138.1	–	1,138.1	–	1,138.1
Debt securities in issue	5,259.3	4,807.9	453.8	–	5,261.7
Subordinated liabilities	1,035.1	975.7	34.0	–	1,009.7

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

13. Fair values (continued)

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

Held at fair value	Fair values Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
30 June 2023 (unaudited)				
Debt securities – fair value through income statement	**25.6**	**–**	**–**	**25.6**
Debt securities – fair value through other comprehensive income	**4,741.5**	**–**	**–**	**4,741.5**
Derivative financial assets	**–**	**2,980.5**	**3.4**	**2,983.9**
Investments	**–**	**–**	**3.0**	**3.0**
Derivative financial liabilities	**–**	**908.2**	**0.4**	**908.6**
30 June 2022 (unaudited)				
Debt securities – fair value through income statement	26.3	–	–	26.3
Debt securities – fair value through other comprehensive income	4,204.1	–	–	4,204.1
Derivative financial assets	–	1,444.6	17.3	1,461.9
Investments	–	–	5.2	5.2
Derivative financial liabilities	–	467.0	0.3	467.3
31 December 2022 (audited)				
Debt securities – fair value through income statement	25.5	–	–	25.5
Debt securities – fair value through other comprehensive income	4,292.7	–	–	4,292.7
Derivative financial assets	–	2,344.0	12.5	2,356.5
Investments	–	–	2.8	2.8
Derivative financial liabilities	–	666.3	–	666.3

The Group's Level 1 portfolio of available for sale debt securities comprises liquid securities for which traded prices are readily available.

Some derivative financial instruments are also included within Level 2 as fair values are derived from discounted cash flow models using yield curves based on observable market data.

Level 3 instruments

Derivative financial instruments within Level 3 are interest rate swaps held in the SPVs. These are valued using similar valuation technique as Level 2 derivatives, namely present value calculations using interest rate curves, but these are not based on market observable data.

The interest rate swaps are balance tracking and the swap notional is projected, and changes over time to match the balance of the underlying mortgage portfolio. The changes in the fair value of these instruments from movements in Level 3 parameters related to prepayment risk will largely offset across the interest rate swaps as the Group is hedged across these positions. Sensitivity analysis to the individual Level 3 parameters has not been disclosed on the basis that the Group does not have a significant exposure to these.

Investments classified in Level 3 relate to the Group's holding in equity preference shares. These shares are convertible into common equity shares at various intervals during the life of the instrument, based on a conversion factor set by the issuer. The valuation method therefore uses the quoted share price of the unrestricted stock as a base, applies the current estimated conversion factor as advised by the issuer and applies a discount.

This discount reflects the current illiquidity of the instrument and the risks to changes in the conversion factor between the balance sheet date and the next conversion date. Whilst the valuation is primarily based on an observable market price, the level and significance of the unobservable input relating to the calculation of the discount moves this asset into Level 3.

Condensed Interim Financial Statements (continued)

Notes to the Interim Financial Statements (continued)

13. Fair values (continued)

Level 3 instruments (continued)

Changes in the carrying value of Level 3 financial instruments in the period all relate to changes in fair value. There have been no changes in methodology, redemption, additions or transfers in or out of Level 3 in the year.

Details of valuation techniques are disclosed on pages 220 to 221 of the 2022 Annual Report and Accounts.

14. Events occurring after the end the reporting period

There have been no material post balance sheet events between 30 June 2023 and the approval of the condensed interim financial statements.

Responsibility Statements

We confirm that to the best of our knowledge:

- the condensed set of financial statements has been prepared in accordance with UK-adopted International Accounting Standard 34 *Interim Financial Reporting*; and
- the interim management 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).

By order of the Board

Susan Allen, OBE
Chief Executive Officer
26 July 2023

Alasdair Lenman
Chief Finance Officer

Independent review report to Yorkshire Building Society

Report on the condensed consolidated interim financial statements

Our conclusion

We have reviewed Yorkshire Building Society's condensed consolidated interim financial statements (the "interim financial statements") in the Half-Yearly Financial Report of Yorkshire Building Society for the 6 month period ended 30 June 2023 (the "period").

Based on our review, nothing has come to our attention that causes us to believe that the interim financial statements are not prepared, in all material respects, in accordance with UK adopted International Accounting Standard 34, 'Interim Financial Reporting' and the Disclosure Guidance and Transparency Rules sourcebook of the United Kingdom's Financial Conduct Authority.

The interim financial statements comprise:

- the Consolidated Balance Sheet as at 30 June 2023;
- the Consolidated Income Statement and Consolidated Statement of Comprehensive Income for the period then ended;
- the Consolidated Statement of Cash Flows for the period then ended;
- the Consolidated Statement of Changes in Members' Interest and Equity for the period then ended; and
- the explanatory notes to the interim financial statements.

The interim financial statements included in the Half-Yearly Financial Report of Yorkshire Building Society have been prepared in accordance with UK adopted International Accounting Standard 34, 'Interim Financial Reporting' and the Disclosure Guidance and Transparency Rules sourcebook of the United Kingdom's Financial Conduct Authority.

Basis for conclusion

We conducted our review in accordance with International Standard on Review Engagements (UK) 2410, 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Financial Reporting Council for use in the United Kingdom ("ISRE (UK) 2410"). A review of interim financial information consists of making enquiries, 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, 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.

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 interim financial statements.

Conclusions relating to going concern

Based on our review procedures, which are less extensive than those performed in an audit as described in the Basis for conclusion section of this report, nothing has come to our attention to suggest that the directors have inappropriately adopted the going concern basis of accounting or that the directors have identified material uncertainties relating to going concern that are not appropriately disclosed. This conclusion is based on the review procedures performed in accordance with ISRE (UK) 2410. However, future events or conditions may cause the group to cease to continue as a going concern.

Independent review report to Yorkshire Building Society (continued)

Responsibilities for the interim financial statements and the review

Our responsibilities and those of the directors

The Half-Yearly Financial Report, including the interim financial statements, 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 Guidance and Transparency Rules sourcebook of the United Kingdom's Financial Conduct Authority. In preparing the Half-Yearly Financial Report, including the interim financial statements, the directors are responsible for assessing the group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or to cease operations, or have no realistic alternative but to do so.

Our responsibility is to express a conclusion on the interim financial statements in the Half-Yearly Financial Report based on our review. Our conclusion, including our Conclusions relating to going concern, is based on procedures that are less extensive than audit procedures, as described in the Basis for conclusion paragraph of this report. This report, including the conclusion, has been prepared for and only for the company for the purpose of complying with the Disclosure Guidance and Transparency Rules sourcebook of the United Kingdom's Financial Conduct Authority and for no other purpose. We do not, in giving this conclusion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

PricewaterhouseCoopers LLP
Chartered Accountants
Leeds

26 July 2023

Other information

The 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 2022 has been extracted from the Annual Accounts for that year. The Annual Accounts for the year ended 31 December 2022 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 Half-Yearly Financial 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.