SUMMARY FINANCIAL REPORT

2012

Manchester BUILDING SOCIETY

Manchester Building Society

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DIRECTORS

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R.W. Dyson MSc FRICS
A. Finch FCII FSRA MCIArb
C.W. Gee BEng FCA
D. A. Harding JP BA MPhil FCMA
P.A. Lynch
S.M. Molloy
M.J. Prior FCA (retired 17 April 2013)
I.M. Richardson BSc ACIB
J. Smith FCCA

CHAIRMAN D. A. Harding JP BA MPhil FCMA (appointed 17 April 2013)

CHIEF EXECUTIVE D.E. Cowie BSc FCA

SECRETARY I.M. Richardson BSc ACIB

SUMMARY CHAIRMAN'S STATEMENT

The financial statements for 2012 have seen a material write-down in the Society's opening reserves resulting from a change in the accounting treatment for certain financial instruments. Whilst the underlying business and profitability of the Society has remained unaltered, the accounting treatment was revised in order for the Society to comply with the latest interpretation of the requirements of International Financial Reporting Standards ("IFRS").

The accounting principles involved are complex. Included within the Society's range of mortgage products are a number where the borrower pays a fixed rate of interest. By offering fixed rate products, the Society is exposed to the risk that future movements in interest rates will see its interest margin eroded or otherwise adversely affected. The Society has entered into interest rate swap arrangements which, where terms match, lock in an interest rate, thereby gaining economic certainty as to the margin that it will earn on these products.

At each year end, the Society has calculated the "fair value" of both the swaps and the mortgages and historically reported the fair value of both in its balance sheet under the hedge accounting provisions of IFRS. The Society has now identified that this accounting treatment does not comply with IFRS hedge accounting requirements and the mortgages should be reported at their amortised cost.

The resulting accounting adjustments have been back-dated across a number of years in line with accounting conventions and the Society's opening reserves have been adjusted to take account of the pre-2012 effect of these adjustments. Prior to these adjustments, a pre-tax profit of £1.86 million was achieved in 2012; after adjustment this figure becomes a post-tax loss of £2.72 million. Remedial action has already been taken, in consultation with the Society's regulators, to rebuild the Society's capital by issuing, in April 2013, £18 million of new equity in the form of Profit Participating Deferred Shares.

In line with the Board's risk appetite, the size of the balance sheet was reduced during 2012. £4.8million of mortgages were sold at a small premium to book value. In addition, three key initiatives were taken during 2012: an application to participate in the Bank of England's Funding for Lending Scheme, a diversification of the Society's retail deposit base (via our North West Air Ambulance Affinity Account and a range of competitive SME Business Deposit Accounts) and the development of Introducer deposit accounts.

As already announced, Michael Prior, Chairman of the Board, retired on 17 April 2013 after 8 years and I should like to thank him for his contribution over this period.

D. A. Harding
Chairman
30 April 2013

SUMMARY FINANCIAL STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2012

This financial statement is a summary of information which is contained in the audited Annual Accounts, the Directors' Report and Annual Business Statement for the year ended 31 December 2012, prepared using International Financial Reporting Standards, all of which will be available to members and depositors free of charge on demand at every office and agent of Manchester Building Society from 30 May 2013 and at www.themanchester.co.uk.

Approved by the Board of Directors of the Society on 30 April 2013 and signed on its behalf by:

A.J. Finch	D.E. Cowie	C.W. Gee
Audit Committee Chairman	Chief Executive	Finance Director

SUMMARY DIRECTORS' REPORT

Business objectives and activities

The principal business objective of the Society and its subsidiary undertakings ("the Group") remains the provision of competitive facilities for both personal and business savings accounts and for mortgage finance primarily to support owner occupation of residential property.

The Board is committed to the Society's status as a mutual and independent Building Society and considers that it is in the long-term interest of members for that status to be maintained.

Corporate governance

The Group maintains a code of practice that complies with the principles in UK Corporate Governance Code ("the Code") issued by the Financial Reporting Council.

Full details of our compliance with the Code may be found in the 2012 Annual Report and Accounts.

Business review

Restatement of prior years financial positions

Our Accounts for 2012 contain two sets of restatement adjustments: one arose from the re-assessment of previous years' accounting policy and the other has seen the Society's Permanent Interest Bearing Shares ("PIBS") being shown within a different heading within the Accounts. The former had a material impact on the results for the current and previous years, whilst the latter did not.

Neither of these restatements has a detrimental impact on any of the savings or mortgage products that are held by our members.

- **Interest rate swaps.** Included within our range of mortgage products are a number where the borrower pays a fixed rate of interest. By offering fixed rate products, we are exposed to the risk that future movements in interest rates will see our interest margin adversely affected. We entered into interest rate swaps which, where terms match, lock in an interest rate; this gives us some economic certainty regarding our interest margin on these mortgage assets. IFRS requires us to calculate a "fair value" for our swaps and to record this on our balance sheet. Under certain circumstances, IFRS allows a "fair value" to be calculated for the associated fixed rate mortgages; this can have the effect of offsetting movements in the fair value of the swaps, thereby reducing the volatility in the profit and loss account. We have now identified that the swap arrangements in place did not meet the specific requirements for this accounting treatment under IFRS. As a result, the full fair value movement in the swaps continues to be recognised whilst there is no offsetting fair value movement in the mortgage assets.
- **PIBS.** During 2012 we undertook a review of the detailed terms of our PIBS and compared these to the requirements of another International Financial Reporting Standard (IAS 32). We now believe that the PIBS, which had previously been shown as a Liability, should more appropriately be classified as Equity. This restatement does not change our total assets or our retained earnings.

SUMMARY FINANCIAL STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2012

Capital

The accounting re-statement had a detrimental impact on the Society's capital during 2012. We saw a timely improvement in the capital position during April 2013, when an additional £18m of Core Equity Tier 1 capital was issued.

Other balance sheet matters

- **Total assets**. We saw a decrease in the Group's total assets by 8.2% to £780m. This was in line with the Board's plans and expectations as it sought to reduce its overall size and conserve its capital.
- **Savings products.** During 2012 we widened the range of savings products that we offered. In September 2012 we entered into our first affinity account relationship; this was with the North West Air Ambulance and we are proud to be associated with this charity. Based on the level of member deposits in this account, the Society pays a proportional sum to the Charity. Further enhancements to our product range have seen a set of competitive Business Deposit Accounts being launched with Small and Medium Sized Enterprises in mind. We intend to widen this range of products during 2013, with the first enhancement targeted to be a range of Introducer deposit accounts.
- **Mortgage products**. Our lending during 2012 was fairly muted – we made advances of £12.3m to 86 borrowers. Throughout the year, we took a cautious approach to all underwriting in order to ensure that we maintained our low risk approach to all new mortgage lending.

Results for the year

- Group loss before tax on continuing operations is £2.33m; when the effect of the change in accounting treatment is removed, the Group's profit before tax improved from £1.67m to £1.86m.

Administrative expenses

- Tight cost control saw the level of the Society's management expenses increase by only £26k during 2012.
- A charge of £693k was recorded during the year for the Society's share of the levy from the Financial Services Compensation scheme. Since it first levied charges in 2008, the Society's contributions have totalled £1.91m.

Charitable Donations

During the year, the Society made £5,000 of donations in support of a local charity (2011: £5,000).

Outlook

The Board's immediate focus for 2013 is on the improvement of both its capital position and its regulatory capital ratios. The means by which the Board can improve its capital position is by ensuring that there is a suitable sustained level of profitability reported each year. Both the pre-tax profit and the net interest margin have shown some volatility over the past 5 years, with the historic low position of Bank Base Rate squeezing our margins. During 2013, we expect our margins to improve. Additionally, we control our overheads closely to ensure that the level of operating expense is commensurate with the size and complexity of our business. Further, our capital ratios should improve through our low risk profile approach for all new mortgage lending.

We expect the retail savings sector to remain competitive during 2013, but with rates paid across the whole market further softening as a result of the Bank of England's Funding for Lending Scheme. We intend to maintain our conservative approach to the development of new savings and mortgage products so that we can show that we have a low risk approach whilst continuing to deliver appropriate outcomes for all of our members.

Continued prudent management of our liquidity is a focus for the Society. We shall continue to hold material amounts with the Bank of England and with other UK banking counterparties.

SUMMARY FINANCIAL STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2012

RESULTS FOR THE YEAR	Group		Society	
	2012	2011*	2012	2011*
Continuing Operations	£000	£000	£000	£000
Net interest income	11,754	15,328	10,598	14,122
Other income and charges	(441)	151	363	918
Fair value losses	(8,278)	(28,748)	(8,278)	(28,748)
Administrative expenses	(4,862)	(4,711)	(4,479)	(4,453)
Impairment losses	(503)	(3,882)	214	(3,882)
Loss for the year before taxation	(2,330)	(21,862)	(1,582)	(22,043)
Taxation	(393)	4,458	(535)	4,532
Loss from continuing operations for the financial period	**(2,723)**	**(17,404)**	**(2,117)**	**(17,511)**
Profit on disposal of subsidiary	-	5,964	-	5,233
Total recognised income and expense relating to the financial period	**(2,723)**	**(11,440)**	**(2,117)**	**(12,278)**
Payment to Equity Holders	(1,075)	(1,075)	(1,075)	(1,075)
Tax credit on payment to Equity Holders (See page 5 for narrative)	263	285	263	285
Transfer to Retained Earnings	**(3,535)**	**(12,230)**	**(2,929)**	**(13,068)**

FINANCIAL POSITION AT THE END OF THE YEAR	Group		Society	
	2012	2011*	2012	2011*
	£000	£000	£000	£000
Assets				
Liquid assets	142,930	185,110	142,880	185,060
Mortgages	571,662	609,618	557,125	593,641
Other loans	2,721	3,807	2,721	3,807
Derivative financial instruments	1,097	1,953	1,097	1,953
Fixed and other assets	61,668	49,204	77,256	65,641
Total assets	**780,078**	**849,692**	**781,079**	**850,102**
Liabilities				
Shares	617,009	693,522	617,009	693,522
Borrowings	81,577	74,458	81,577	74,458
Other liabilities	2,732	3,643	2,594	3,520
Derivative financial instruments	42,101	37,875	42,101	37,875
Subordinated capital	15,700	15,700	15,700	15,700
Subscribed capital##	14,788	14,788	14,788	14,788
Reserves##	6,171	9,706	7,310	10,239
Total liabilities	**780,078**	**849,692**	**781,079**	**850,102**

Classified as equity

SUMMARY OF KEY FINANCIAL RATIOS	Group		Society	
	2012	2011*	2012	2011*
	%	%	%	%
Gross capital as a percentage of shares and borrowings	5.25	5.23	5.41	5.30
Liquid assets as a percentage of shares and borrowings	20.46	24.10	20.45	24.10
Loss for the year as a percentage of mean total assets	(0.33)	(1.32)	(0.26)	(1.44)
Management expenses as a percentage of mean total assets	0.60	0.54	0.55	0.52

* Restated

SUMMARY FINANCIAL STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2012
NOTES TO THE SUMMARY FINANCIAL STATEMENT

1. Summary Financial Statement is prepared on both a Group and Society basis.
2. The gross capital ratio measures the proportion by which capital bears to shares and borrowings. Gross capital consists of retained profits, accumulated over many years in the form of reserves, Permanent Interest Bearing Shares and qualifying subordinated liabilities.
3. The liquid assets ratio measures the proportion that assets held in the form of cash and short-term deposits bears to shares and borrowings. By their nature, liquid assets are readily realisable into cash and thereby enable the Group and Society to meet requests by its investors for withdrawals on their accounts, to make new mortgage loans to borrowers and to fund its business activities generally.
4. The loss for the year as a percentage of mean total assets measures the proportion that the loss after taxation for the year represents in relation to the average of total assets for the year.

   The Group and Society need to make a reasonable level of profit each year in order to fund the continued development of its business whilst maintaining its capital ratio at a suitable level to protect investors.
5. The management expense ratio measures the proportion that administration expenses bears to the average of total assets during the year.

STATEMENT OF THE AUDITORS TO THE MEMBERS AND DEPOSITORS OF MANCHESTER BUILDING SOCIETY

Pursuant to Section 76 of the Building Societies Act 1986, we have examined the Summary Financial Statement of Manchester Building Society for the year ended 31 December 2012 set out on pages 5 to 8 and the directors' remuneration disclosure on pages 9 and 10.

The report is made solely to the members and depositors of the Manchester Building Society, both as a body, in accordance with Section 76 of the Building Society Act 1986. Our examination has been undertaken so that we might state to the Society's members and depositors those matters we are required to state in an auditors' statement and for no other purpose. To the fullest extent permitted by law, we do not accept responsibility to anyone other than the Society and the Society's members and depositors, both as a body, for our examination, for this statement, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the Summary Financial Statement in accordance with applicable United Kingdom law.

Our responsibility is to report to you our opinion on the consistency of the Summary Financial Statement with the full Annual Report and Accounts, the Directors' Remuneration Report and the Directors' Report, and its compliance with the relevant requirements of Section 76 of the Building Societies Act 1986 and the regulations made there under.

We also read the other information contained in the Summary Financial Statement and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Summary Financial Statement. The other information comprises the Summary Chairman's Statement.

Basis of opinion

We conducted our work in accordance with Bulletin 2008/3 "The Auditors' Statement on the Summary Financial Statements" issued by the Auditing Practices Board. Our report on the Groups' full Annual Report and Accounts describes the basis of our audit opinion on those Annual Accounts.

Opinion

In our opinion the Summary Financial Statement is consistent with the full Annual Report and Accounts, the Annual Business Statement and the Directors' Report of Manchester Building Society for the year ended 31 December 2012 and complies with the applicable requirements of Section 76 of the Building Societies Act 1986 and regulations made there under.

Grant Thornton UK LLP
Chartered Accountants
Registered Auditors
London

30 April 2013

SUMMARY DIRECTORS' REMUNERATION REPORT

Introduction

The purpose of this report is to provide details of the Society's policy on the remuneration of its executive and non-executive directors and explain the process for setting the level of directors' remuneration.

Remuneration Committee

The Remuneration Committee is responsible for the remuneration policy for all directors and senior managers; it does not set the remuneration of other staff. All recommendations made by the Remuneration Committee are considered by the full Board. The Committee is committed to compliance with best practise as set out in the Code.

No director is involved in any decision regarding their own level of remuneration.

Executive directors

Remuneration levels are set for executive directors at such a level to reward and retain the skills and commitment necessary to manage the development of the Group within a competitive and challenging business sector. In accordance with best practice, the Remuneration Committee reviews the remuneration arrangements for the executive directors on a periodic basis and compares their range of benefits to those available within similar organisations.

Their remuneration arrangements include:

- salaries, reviewed by the Committee on an annual basis
- membership of the Group personal pension scheme, on the same terms as other eligible employees of the Group, save for the Chief Executive, whose membership of the scheme attracts an increased level of employer pension contributions
- taxable benefits which include a car allowance and private health care

Bonus scheme arrangements that were in place historically for executive directors ceased to exist from 1 January 2011.

No executive director holds a contract with a notice period of more than 12 months.

DIRECTORS' REMUNERATION

Executive directors	**Salary**	**Pension Contributions**	**Bonus**	**Benefits**	**Total**
2012	£000	£000	£000	£000	£000
D.E. Cowie	194	33	-	17	244
C.W. Gee	117	14	-	11	142
P.A. Lynch	117	14	-	11	142
I.M. Richardson	117	14	-	10	141
	545	75	-	49	669

	Salary	**Pension Contributions**	**Bonus***	**Benefits**	**Total**
2011	£000	£000	£000	£000	£000
D.E. Cowie	192	30	16	17	255
C.W. Gee	115	13	-	11	139
P.A. Lynch	115	13	-	11	139
I.M. Richardson	115	13	-	10	138
	537	69	16	49	671

** represents final payment made in relation to historic bonus scheme arrangements; entitlement to future bonuses ceased with effect from 1 January 2011.*

Non-executive directors

Non-executive directors are remunerated by way of fees, which are recommended by the Committee to the Board on an annual basis. The level of fees is assessed on the basis of responsibility, experience, skill and time commitment and by comparison with other building societies and regional financial institutions.

Non-executive directors do not receive any other benefits and they do not have any pension arrangements through the Group.

A summary of the non executive directors' remuneration is shown below:

	Fees 2012	**Fees 2011**
	£000	£000
J.P. Allen	29	28
R.W. Dyson	29	28
A. Finch	29	28
S.M. Molloy	29	28
M.J. Prior	50	49
J. Smith	35	35
	201	196

All directors	**2012**	**2011**
	£000	£000
Total remuneration	870	867

The Group does not make mortgage loans available to any director.

Full details of directors' remuneration and other business interests are shown within the Annual Report and Accounts.

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Agencies

Please see our website at: www.themanchester.co.uk for the most up to date list of our agencies.

Savings Customer Services

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Post Manchester Building Society
Savings
PO Box 4256
Manchester M60 3AX

Mortgage Customer Services

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