

Nationwide Building Society

**Preliminary Results Announcement
For the year ended
4 April 2009**



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Underlying Results

These results have been prepared in line with International Financial Reporting Standards accounting policies (‘IFRS’). Where appropriate, certain aspects of the results are presented to reflect management’s view of the underlying results in order to provide a clearer representation of the performance of the Group.

Profit before tax shown on a reported and underlying basis are set out on page 10. Reported profit before tax of £212 million (2008: £686 million) has been adjusted for Financial Services Compensation Scheme (FSCS) costs of £241 million; transformation costs of £107 million, in connection with the restructuring and resizing of the business including the integration of Portman, Cheshire and Derbyshire into the Group; gains arising on business combinations of £157 million, and the movement in the value of derivatives and hedge accounting of £10 million to derive an underlying profit before tax of £393 million (2008: £781 million).

Impact of mergers and acquisitions on Financial Results

Results relating to the mergers with Derbyshire and Cheshire building societies and the acquisition of core parts of the Dunfermline building society are included with effect from the date of completion of the mergers and acquisition, 1 December 2008, 15 December 2008 and 30 March 2009 respectively. Results relating to the merger with Portman Building Society were included with effect from the date of completion, 28 August 2007.

Forward Looking Statements

Certain statements in the Preliminary Announcement are forward looking. Although Nationwide believes that the expectations reflected in these forward looking statements are reasonable, we can give no assurance that these expectations will prove to be an accurate reflection of actual results. Because these statements involve risks and uncertainties, actual results may differ materially from those expressed or implied by these forward looking statements.

We undertake no obligation to update any forward looking statements whether as a result of new information, future events or otherwise.

HIGHLIGHTS

Nationwide Building Society today announced its results for the year ended 4 April 2009. This set of results demonstrates a resilient performance in an exceptionally difficult market place.

Nationwide has performed well in unprecedented and challenging market conditions:

- Underlying profit before tax of £393 million (2008: £781 million). The reduction of 50% reflects the cost of carrying additional liquidity and margin compression in a low interest rate environment, together with an increase in impairment provisions in the current recessionary conditions.
- Reported profit before tax for the year of £212 million (2008: £686 million).
- Reported profit is after an exceptional charge of £241 million in respect of FSCS levies covering the Group's share of interest for the full three year period of the HM Treasury loan to FSCS. These levies account for more than half of the fall in reported profit.
- Despite the challenging environment an estimated £680 million benefit has been provided to members in the year through competitive interest rates and lower fees and charges.
- Total assets, including the impact of the mergers with The Derbyshire and The Cheshire building societies and acquisition of certain assets and liabilities of Dunfermline Building Society, increased by 13% to £202.4 billion (4 April 2008: £179.0 billion).

Prudent and robust balance sheet:

- Strong capital ratios with a Tier 1 ratio of 15.1% and Core Tier 1 ratio of 12.1% (Basel II, IRB basis). Nationwide is the largest UK banking institution not to have raised capital during the year.
- Balance sheet funded predominantly by retail savings, with our wholesale funding ratio of 28.6% (4 April 2008: 31.0%) being one of the lowest levels within UK banking institutions.
- Loans originated by Nationwide continue to perform strongly, with the proportion of residential mortgage accounts more than 3 months in arrears of 0.60%, compared with the CML industry average of 2.39% as at 31 March 2009. The CML industry average has deteriorated at twice the rate of Nationwide's arrears on originated loans in the year to 31 March 2009.
- Mortgage assets acquired through mergers with Derbyshire and Cheshire and the purchase of Dunfermline's prime residential assets have been fair valued on a basis which makes allowance for anticipated losses over the remaining life of the loans. As a result of this fair valuation exercise, Group profits are protected from future losses.
- The recession has impacted the commercial property market particularly in the second half of the year and has resulted in a significant increase in the number and value of commercial arrears cases, albeit from a very low base. The number of Nationwide originated commercial cases 3 or more months in arrears is 179 (4 April 2008: 66).
- The proportion of unsecured personal loan balances over 30 days in arrears increased to 7.15% (2008: 5.88%), but remains significantly less than the industry average of 17.0%.
- The Society's core liquidity ratio at 4 April 2009 was 12.8% (4 April 2008: 8.9%).
- The Available for Sale (AFS) reserve has increased to £2.0 billion negative, net of tax (4 April 2008: £0.4 billion negative). The AFS assets have been carefully reviewed based upon latest performance data and no significant additional impairment has been booked in the second half of the year. The majority of these assets were purchased with the intention of holding them to maturity and we continue to expect to recover full value for substantially all of them over their residual life.

Proactive response to market conditions:

- Merger transactions with The Derbyshire and The Cheshire Building Societies were successfully completed in December 2008, three months after announcement.
- Acquisition of prime residential loans, retail liabilities and other selected assets and liabilities of Dunfermline Building Society completed in March 2009.
- Portman integration was completed ahead of schedule, with total merger synergies of £90 million to be delivered by the end of 2009/10.
- Retail savings franchise expanded into the Republic of Ireland with the opening of a branch in Dublin.

Nationwide’s chief executive, Graham Beale, said,

“History will record 2008 as a year of fundamental change to banks and financial institutions across the world. Nationwide has remained strong in the midst of all this turbulence and has been the only major UK banking institution not to raise capital or seek access to Government sponsored capital enhancing schemes. This reflects a combination of our naturally high capital and prudent lending practices which are the hallmark features of a strong building society.

“Profitability has been adversely affected by the low interest rate environment and increased provisions as a result of the current recession. Our reported profit is 53% lower than it would otherwise have been because there is an exceptional charge of £241 million relating to the levies payable to the FSCS.

“We regard the fact that the FSCS charge is not linked to the level of risk posed to the financial system by individual institutions, but instead is allocated by share of the retail savings market, as illogical and unfair, producing a disproportionate outcome for the low risk retail funded institutions, particularly building societies. This view is shared by 173 cross party MPs. We have also lobbied for an increase in the FSCS limit from £50,000 to at least £100,000 which would reassure savers with independent institutions that they have similar protection as those with Government owned, nationalised and part-nationalised banks.

“During the year we played our part in promoting financial stability by merging with the Derbyshire and Cheshire building societies in December 2008 and by acquiring selected assets and liabilities of Dunfermline Building Society in March 2009. In addition, the Group also expanded its retail savings franchise by opening a branch in Ireland in March 2009.

“The size of the mortgage and savings market has contracted significantly in the year as a result of the extreme economic conditions. In addition aggressive deposit taking by state owned institutions such as NS&I and Northern Rock took in excess of 70% of the savings market in the second half of 2008. Against this background we maintained our competitive position with healthy market shares of over 8% for mortgages and 10% for savings deposit growth.

“Market conditions will remain challenging throughout 2009 and beyond. In particular, the low interest rate environment will continue to depress margin and higher levels of unemployment and business failures will inevitably lead to increased loan loss provisions. However, we remain confident that Nationwide’s high quality balance sheet and robust capital ratios will continue to underpin our financial strength and place us in a strong position to trade through these conditions and remain a real and attractive alternative to the banks.”

FINANCIAL SUMMARY

	2009	2008
Financial Performance	£m	£m
Underlying profit before tax	393	781
Reported profit before tax	212	686
Lending Volumes	£bn	£bn
Group residential – gross	18.9	27.1
Group residential – net	1.6	6.7
Commercial – gross	2.2	6.1
Commercial – net	0.6	2.4
Consumer finance – net unsecured lending	(0.1)	(0.2)
Savings Volumes	£bn	£bn
Retail savings deposits growth	4.5	13.3
Net receipts	1.7	9.7
Market Shares	%	%
Group residential – gross	9.0	7.8
Group residential – net	8.2	7.1
Retail savings deposit growth	10.1	17.1
Key Ratios	%	%
Cost to income ratio – underlying basis	60.0	55.7
Cost to income ratio – reported basis	60.3	59.4
Net interest margin	0.93	1.12
Balance Sheet	£m	£m
Total assets	202,361	179,027
Loans and advances to customers	155,482	142,804
Member savings balances	128,284	113,816
Total shares, deposits and loans (SDLs)	186,405	167,365
Total regulatory capital	9,706	9,474
Asset Quality	%	%
Proportion of residential mortgage accounts 3 months+ in arrears:		
Nationwide originated	0.60	0.40
Nationwide originated plus acquired*	0.76	0.40
Average indexed loan to value of residential mortgage book	52	43
Average indexed loan to value of new residential lending	58	61
Commercial accounts 3 months+ in arrears:		
Nationwide originated	1.62	0.56
Nationwide originated plus acquired*	1.87	0.56
Percentage of unsecured personal loan accounts 30 days+ in arrears	7.15	5.88
Key Ratios	%	%
Solvency ratio (Basel II)**	19.5	12.4
Tier 1 ratio**	15.1	9.7
Core Tier 1 ratio**	12.1	8.1
Wholesale funding ratio	28.6	31.0
Core liquidity ratio	12.8	8.9
Loan to deposit ratio ***	112.4	117.2

* 'Acquired' relates to assets acquired from Derbyshire, Cheshire and Dunfermline building societies

** Capital ratios are reported on an Internal Ratings Based basis for 2009 and a Standardised basis for 2008

*** The loan to deposit ratio represents loans and advances to customers divided by (shares + other deposits + amounts due to customers).

CHIEF EXECUTIVE'S REVIEW

Nationwide has performed well in unprecedented and challenging market conditions:

The past financial year has been marked by unprecedented and exceptional market conditions, with problems initially arising in the financial services industry spreading to the broader economy. We are in the middle of a global downturn with the UK economy officially in the deepest recession since the second world war. During the year a number of banks have required Government support, with some becoming nationalised or part-nationalised in the process. Nationwide has not been required to raise additional capital and, despite the market conditions, has delivered an estimated £680 million of benefits to members through competitive interest rates and lower fees and charges.

Whilst we have not been immune to the impact of the recession, we have delivered a resilient performance with an underlying profit performance for the year of £393 million (2008: £781 million). The reduction in our underlying profit performance reflects the impact of carrying higher levels of liquidity and operating within an environment of higher retail funding costs and significant margin compression and, despite our prudent lending policies, an increase in impairment charges reflecting the current recessionary conditions.

Statutory profit before tax was £212 million (2008: £686 million). Our reported profit is 53% lower than it would otherwise have been because there is an exceptional charge of £241 million relating to levies payable to the Financial Services Compensation Scheme (FSCS) following the failure of a number of banking institutions. Without this charge, our reported profit before tax would have been £453 million which, in the context of the current recessionary conditions and low interest rate environment, demonstrates the ability of our business model to withstand extremely challenging market conditions.

Reported profit also includes transformation costs of £107 million principally associated with costs in connection with restructuring and resizing the business including the integration of Portman, Cheshire and Derbyshire building societies into the Group, gains on business combinations of £157 million from Cheshire and Dunfermline, and a positive movement in the value of derivatives and hedge accounting of £10 million.

Prudent and secure business model:

Nationwide, as a building society, has remained true to its core values. We have a strong and diversified funding base, with over 70% of our funding through retail deposits, which means that we are less reliant on the wholesale markets than many of our listed competitors.

We have continued to manage our business in a prudent manner throughout the year. Competition for retail funds has been strong and economic conditions, combined with the low interest rate environment, have seen a reduction in the overall size of the market. Our approach has been to offer fair and consistent pricing to our savers. Our net receipts, including offshore deposits, were £1.7 billion and our retail savings deposit growth was £4.5 billion. Lending activities have been managed to match broadly with the levels of deposit taking. Total net lending for the year was £2.1 billion (2008: £8.9 billion). Of this, Group net residential lending was £1.6 billion representing a market share of 8.2% (2008: 7.1%).

We have maintained a consistent focus on the quality of our lending, with the average indexed loan to value of new residential lending reducing from 61% to 58%. Whilst the recession has had an impact upon the level of our arrears, our increase has been less than the average increase for the Council of Mortgage Lenders (CML). For Nationwide originated loans, the proportion of mortgage accounts three months or more in arrears was 0.60% (2008: 0.40%), compared to a CML industry average of 2.39% as at 31 March 2009.

Mortgage assets acquired through mergers with Derbyshire and Cheshire and the purchase of Dunfermline's prime residential assets have been fair valued on a basis which makes allowance for anticipated losses over the remaining life of the loans. As a result of the fair valuation exercise, we have provided £203 million against total residential mortgage assets of £8.6 billion to cover our expectation of future credit losses.

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The quality of the prime residential mortgage book, which accounts for approximately 86% of our residential mortgage loans, remains strong with the proportion of Nationwide originated mortgage accounts three months or more in arrears of 0.44% (4 April 2008: 0.34%). As anticipated, arrears in the specialist lending portfolios have shown a marked increase in the year and, for Nationwide originated loans, the proportion of specialist accounts in arrears increased to 2.45%, compared with 1.11% the previous year.

The current market conditions have had a significant impact upon commercial property values and we have seen a substantial increase in the level of commercial arrears and provisions through reduced tenant demand and business failures. Excluding low risk lending to social housing and Private Finance Initiatives (PFI), the commercial loan portfolio is well diversified by property type, industry sector and geography with only limited exposure to subordinated or non senior loans or speculative development.

We have experienced increases in levels of arrears and defaults, particularly over the second half of the year. There are 179 Nationwide originated commercial accounts three months or more in arrears at 4 April 2009 (4 April 2008: 66 accounts, 30 September 2008: 75 accounts) all of which have been individually assessed for impairment. Over the year, the level of balance sheet provision has increased to £194 million (4 April 2008: £30 million) bringing provision as a percentage of assets to 0.92% (4 April 2008: 0.15%).

The commercial portfolios acquired from the Derbyshire and Cheshire include £80 million of subordinated loans and £160 million of residential property development. The quality of these portfolios is not equivalent to our own originated book and they have been subject to rigorous evaluation as part of our accounting fair value exercise on acquisition. As a result, in bringing these assets onto our balance sheet, we have written them down by £179 million out of a total gross exposure of £1.2 billion to cover our expectation of future credit losses. Our current assessment of the risk inherent in these portfolios is not materially different to the view taken during our pre completion due diligence for the merger transactions.

Nationwide has always maintained a strong and robust capital position. The FSA has confirmed that Nationwide has cleared the conditions required to use its Internal Ratings Based (IRB) models to calculate capital requirements. At 4 April 2009, the Group's Core Tier 1 capital ratio, on an IRB basis, was 12.1% and Tier 1 ratio was 15.1%. These ratios are significantly higher than the ratios reported in our Half Year results announcement for the six months to 30 September 2008, which were reported on a Standardised basis and excluded the Cheshire and Derbyshire mergers and Dunfermline acquisition. The ratios are also substantially in excess of those reported by the major banks in their 2008 year end results announcements. In view of our strong capital position, the Tripartite authorities agreed in March 2009 that Nationwide was not required to raise any additional capital.

Nationwide responded positively to market conditions:

Nationwide has taken steps to support the building society sector and promote financial stability during this exceptional period. This year, Nationwide has merged with the Cheshire and the Derbyshire and acquired the prime residential mortgage book, retail liabilities and other selected assets and liabilities of Dunfermline Building Society. The mergers with the Cheshire and Derbyshire were legally completed in December 2008, within three months of announcement, whilst the acquisition of Dunfermline's assets and liabilities took place on 30 March 2009. The relatively short timescales to completion demonstrates Nationwide's ability to react quickly and positively in the interests of all stakeholders.

The transactions have provided an opportunity for Nationwide to deepen its national franchise at a local level. Derbyshire, Cheshire and Dunfermline will all retain their regional identities and operate as three new trading brands for Nationwide. Despite their separate financial difficulties, which have been prudently provided for through the fair valuation of assets as at the date of acquisition, we believe these transactions are in the long term interests of our members and will generate value over the medium term. The fair valuation exercise also ensures that Nationwide is protected from any further losses from the acquired assets provided that they perform in line with assumptions at take on.

In March 2009 we further extended our retail savings franchise by expanding into the Republic of Ireland, adding to the offshore presence the Society already has on the Isle of Man. Nationwide UK (Ireland) will not only provide

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the Society with an extra outlet for attracting retail savings but it will also offer the Society access for the first time to funding from the European Central Bank should it be required.

The FSCS scheme is inequitable and we have been lobbying hard for positive change:

The transfer of Bradford & Bingley's retail deposit business to Abbey and the subsequent failure of other banks and deposit-taking institutions during the year triggered claims against the FSCS. Nationwide, along with other building societies, will be required to pay levies to the FSCS, primarily to fund interest payments on treasury loans to the Scheme, based upon our share of protected deposits.

We have been actively lobbying the Tripartite authorities to review the way in which FSCS levies are allocated across the industry. We believe the current allocation is unfair and has a disproportionate effect on building societies, who are required to hold a greater proportion of funding in the form of retail deposits.

Based upon the current FSCS allocation, we have recognised a charge of £241 million in our year end financial statements. This provision covers the full cost of the Group's estimated share of the levies in respect of the initial three year loan facility from HM Treasury.

Nationwide has always adopted a prudent and responsible approach to lending. We firmly believe that the allocation of levies should reflect the risk profile of the organisation and to require building society members to bear a disproportionate cost of the failures of high risk banking businesses is both unfair and wholly contrary to this principle. This view is endorsed by 173 cross party MPs supporting a need for a review of the way it is allocated.

We have also lobbied for the FSCS limit to be increased from £50,000 to at least £100,000 per individual – which would cover 99% of our members' savings. This would reassure savers of independent institutions that they have similar protection as those with Government owned, nationalised and part-nationalised banks.

The economic outlook remains challenging:

The UK economy contracted very sharply at the end of 2008 and the beginning of 2009, following the intensification of the global financial crisis in September. Although there have been some encouraging indications that the rate of decline is beginning to slow, we expect the economy to remain in recession until at least the end of 2009. Any recovery in 2010 is likely to be sluggish as consumers work off excess debt and fiscal policy is tightened in order to control the public sector deficit. The labour market is expected to lag developments in the overall economy, meaning that the unemployment rate may continue rising well into 2010.

The financial crisis and the recession have already had a significant impact on the housing market, where prices have fallen considerably from their 2007 peak. In recent months, the rate of price declines has slowed somewhat, although it is too early to say that this marks a definitive turning point. Lower prices and lower interest rates could start to attract more buyers into the market as the year progresses. However, high levels of unemployment and low wage growth are likely to limit the pace of any recovery.

The savings market also faces another challenging year, as deteriorating employment conditions make it difficult for households to save, and the very low level of interest rates currently prevailing is leading many households to prioritise debt reduction over deposit accumulation. Consequently we expect both the UK Household savings market and UK mortgage market to contract in 2009/10, taking the net mortgage market into negative growth.

Nationwide remains well positioned:

Current economic, market and interest rate conditions are leading to a reduction in the Group's profitability and it is clear that 2009 and 2010 will continue to present a very difficult trading environment. We remain committed to mutuality and will continue to run our business in a manner which responds to market conditions but maintains long term good value for our members.

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We expect both the mortgage and savings market to contract in 2009 which will lead to intensive competition for high quality mortgages and retail deposits. The cost of retail and wholesale funding and our prudent approach to liquidity management will continue to exert downward pressure on margins and this trend will be compounded by the full year impact of the low interest rate environment. We expect the level of impairments to increase during 2009 as an inevitable consequence of prevailing economic conditions. As a result, we expect the significantly reduced level of underlying profit in the second half of 2008/09 to continue throughout 2009/10 with scope for further reduction dependent upon the level of competition for retail funds and the performance of the wider economy.

As a sector, mutuals are well placed to tolerate lower levels of profitability without the burden of having to pay a dividend to shareholders. We do expect further consolidation in the financial services sector and Nationwide will continue to act in a responsible manner to support the mutual sector and provide market stability. However, we will not be a lender of last resort and will only consider transactions that will enhance and not destroy value to our members.

Nationwide's balance sheet is well capitalised with a high level of liquidity and a strong retail funding base. The outlook is challenging, but we remain well positioned to trade through these difficult conditions and remain a real and attractive alternative to the banks.

Graham Beale
Chief Executive

26 May 2009

BUSINESS REVIEW

INCOME STATEMENT OVERVIEW

Profit before tax on a reported and underlying basis are set out below. Certain aspects of the profit before tax are presented to reflect management's view of underlying results, to provide a clearer representation of the performance of the Group.

Profit before tax on a reported basis was £212 million (2008: £686 million). Underlying profit before tax equates to reported profit before tax adjusted for the add back of FSCS cost; movements in the value of derivatives and hedge accounting; transformation costs and gains on business combinations. Underlying profit before tax was £393 million (2008: £781 million). The comparative year additionally includes an adjustment for policyholder tax and the net impact of disposal of our investment and protection subsidiaries to Legal and General.

Year to 4 April 2009	As reported	FSCS costs	Reported profit pre FSCS costs	Movements on derivatives and hedge accounting	Policyholder tax	Transformation costs	Gains on business combinations*	Underlying
	£m	£m	£m	£m	£m	£m	£m	£m
Net interest income	1,758	-	1,758	-	-	-	-	1,758
Other income	516	-	516	-	-	-	(157)	359
Fair value adjustments	10	-	10	(10)	-	-	-	-
Total income	2,284	-	2,284	(10)	-	-	(157)	2,117
Administrative expenses	1,252	-	1,252	-	-	(107)	-	1,145
Depreciation and amortisation	126	-	126	-	-	-	-	126
Impairment losses on loans and advances to customers	394	-	394	-	-	-	-	394
Provisions for liabilities and charges	249	(241)	8	-	-	-	-	8
Impairment losses on investment securities	51	-	51	-	-	-	-	51
Profit before tax	212	241	453	(10)	-	107	(157)	393

* Gains on business combinations represent the net identifiable assets of The Cheshire and the Dunfermline at the dates of the respective merger and acquisition, minus the consideration in respect of those transactions. Further detail is given in notes 19 and 20.

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Year to 4 April 2008	As reported	FSCS costs	Reported profit pre FSCS costs	Movements on derivatives and hedge accounting	Policyholder tax	Transformation costs	Gains on business combinations/disposal**	Underlying
	£m	£m	£m	£m	£m	£m	£m	£m
Net interest income	1,796	-	1,796	-	-	-	-	1,796
Other income	411	-	411	-	15	-	(10)	416
Fair value adjustments	(31)	-	(31)	31	-	-	-	-
Total income	2,176	-	2,176	31	15	-	(10)	2,212
Administrative expenses	1,168	-	1,168	-	-	(59)	-	1,109
Depreciation and amortisation	124	-	124	-	-	-	-	124
Impairment losses on loans and advances to customers	106	-	106	-	-	-	-	106
Provisions for liabilities and charges	(10)	-	(10)	-	-	-	-	(10)
Impairment losses on investment securities	102	-	102	-	-	-	-	102
Profit before tax	686	-	686	31	15	59	(10)	781

** Amounts reported in respect of gains on business combinations/disposals in 2008 related exclusively to the disposal of our investment and protection subsidiaries to Legal and General.

Underlying Profit

A Summary Income Statement on an underlying basis is as follows:

	Year to 4 April 2009 £m	Year to 4 April 2008 £m
Net interest income	1,758	1,796
Other income	359	416
Total income	2,117	2,212
Expenses	1,271	1,233
Impairment losses on loans and advances	394	106
Impairment losses on investment securities and other provisions	59	92
Underlying profit before tax	393	781

Underlying profit for the year was £393 million (2008: £781 million), demonstrating a resilient performance under difficult market conditions. The key drivers of this performance are set out below.

PERFORMANCE BY INCOME STATEMENT CATEGORY

Net interest income, at £1,758 million was marginally lower than the previous year.

	Year to 4 April 2009 £m	Year to 4 April 2008 £m
Net interest income	1,758	1,796
Weighted average total assets	189,624	160,265
	%	%
Net interest margin	0.93	1.12

We responded prudently to the exceptional market conditions during the year by significantly increasing our levels of liquidity and by ensuring that this increased liquidity was concentrated in highly liquid securities such as Gilts and our Bank of England reserve account.

The Society's core liquidity ratio at 4 April 2009 was 12.8% (4 April 2008: 8.9%). This increase in liquidity combined with a switch into higher grade instruments has reduced our net interest margin by around 4 bps. In addition our net exposure to Libor linked assets has reduced significantly in the year as borrowers have moved onto variable rates and savers onto fixed rates. As a result, despite an increase in the average bank base rate:Libor differential in the year, our benefit from this has reduced year on year resulting in an approximate 5 bps decline in the net interest margin.

The remaining decline (c10bps) in net interest margin is attributable to increased costs of funding, including Government sponsored funding schemes, and declining retail spread. Margins on new lending in both the retail and commercial sector have widened considerably but with lower levels of new business origination have not fully offset the progressive impact of repricing of both wholesale and retail liabilities. The increased propensity of retail mortgage borrowers to migrate onto our BMR (our standard variable rate) product, which is capped at 200 basis points over base, at the end of their deal period has contributed to this imbalance in the rate at which assets and liabilities are repricing.

Looking forward we anticipate that our margin will continue to trend downwards, albeit at a reduced rate, due to the impact of the low base rate environment and continuing wholesale market disruption. Competition for retail funds remains intense, and the cost of various Government sponsored funding schemes will have an increasing impact on our margin.

Other income

Other income represents income earned from the sale of insurance and investment products together with administration and transaction fees not included within interest margin. Other income also includes dividends on equities held within the Treasury investment portfolio.

Underlying other income at £359 million was £57 million lower than the comparative year (2008: £416 million). The sale of our life insurance and unit trust businesses in January 2008 combined with our new distribution agreement with Legal & General has had the effect of reducing both income and costs by about £22 million as gross income and costs have been replaced with a net commission income stream.

Income from equity shares, which arises from a relatively small portfolio and naturally exhibits an uneven profile of recognition, was £9 million lower than the previous year and as a result of current market conditions, a loss of £25 million has been recognised in the income statement in respect of the revaluation and sale of the Group's properties.

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The remaining fall in other income reflects reduced income from banking in relation to unauthorised overdrafts and returned items, and reduced fees in respect of unsecured personal loans.

Expenses

	Year to 4 April 2009 £m	Year to 4 April 2008 £m
Employee costs:		
• Wages and salaries	465	431
• Social security costs	40	34
• Pension costs	94	100
	599	565
Other administrative expenses	546	544
Depreciation and amortisation	126	124
	1,271	1,233

Total underlying expenses as reported amounted to £1,271 million, representing an increase of 3% over the prior year. However, adjusting for the additional Portman, Cheshire and Derbyshire costs and the effect of the sale of our life insurance and unit trust businesses referred to above, underlying expenses have increased by just 1% in the year reflecting the continued focus on our cost base.

The Portman merger increased the underlying cost base since its completion in August 2007 and we estimate these additional costs to be around £26 million relative to last year. In addition the recent mergers with the Cheshire and Derbyshire have added an extra £22 million to the underlying cost base in the current year.

We have completed the integration of Portman ahead of schedule and will deliver by the end of 2009/10 the £78 million of cost savings per annum which were planned as part of the overall synergies from the Portman transaction.

Our underlying cost income ratio for the year was 60.0% (4 April 2008: 55.7%). The pressures on income arising from the low interest rate environment and the additional costs arising from the mergers, before achieving cost synergies which we expect to deliver by 2011/12, have impacted our ratio. In light of current market conditions we are continuing to seek ways to contain costs and are taking steps to restructure and re-size certain areas of the business.

Impairment losses on loans and advances

	Year to 4 April 2009 £m	Year to 4 April 2008 £m
Secured lending	280	(16)
Unsecured lending	114	122
	394	106

The charge for impairment losses on loans and advances was significantly more than for 2008, driven by increased provisions on the secured books. The underlying quality of both secured and unsecured lending remains strong. Of the £280 million charge on secured lending £91 million (2008: release of £12 million) relates to residential mortgages and £189 million, (2008: release of £4 million) relates to commercial lending.

The charge on residential primarily relates to specialist lending (£87 million) as increases in arrears, combined with reductions in property valuations, have resulted in a requirement for increased impairment provisions. The charge

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on the prime book was just £4 million as modest arrears and lower average LTV's have acted as a buffer against the impact of falling house prices. Deterioration on the books has been contained as increases in unemployment in the second half of the year coincided with the substantial falls in interest rates that made repayments more affordable and so tended to offset the rate of growth in arrears. In addition, levels of write off of £8 million (specialist £5 million, prime £3 million) have remained relatively low. The impairment provision has increased by 223% to £123 million over the year and residential provision as a percentage of total residential assets increased to 0.10% (4 April 2008: 0.03%). Impairment provisions as a percentage of originated mortgage balances on cases 3 or more months in arrears increased to 12.10% (4 April 2008: 7.77%).

In our commercial lending division, difficult market conditions resulted in an increase in commercial loan defaults, particularly over the second half of the year where the individual impairment charge was £139 million compared with £25 million in the first half. The principal drivers of the increased provisions in the commercial portfolio are covenant breaches on LTV's as a result of substantial falls in capital values; reduced tenant demand either as a result of tenant failure or reduced ability to cure void periods at the end of lease terms, and business failures on owner occupied properties.

The number of commercial property cases in arrears increased significantly in the second half of the year from 75 cases at 30 September 2008 to 179 at 4 April 2009. Increases in arrears have also impacted the collective provision resulting in an additional impairment charge of £7 million. The overall level of provision for Commercial as a percentage of assets at 4 April 2009 has increased significantly to 0.92% (4 April 2008: 0.15%).

The remaining £18 million impairment charge relates to a portfolio of European commercial loans which are classified as "other" loans in note 8 on page 39.

The reduction in the charge for unsecured lending relates to lower levels of write off and delinquent accounts combined with a reduction in the provision required against the up to date book. Asset quality of our unsecured books remains strong reflecting our cautious approach and prudence in our underwriting.

Impairment losses on investment securities and other provisions

	Year to 4 April 2009 £m	Year to 4 April 2008 £m
Treasury investments	51	102
Other provisions	8	(10)
	59	92

The extremely difficult market conditions led to the well publicised collapse of a number of global financial institutions in the year. As a result of these failures the Treasury investments impairment charge is £51 million (4 April 2008: £102 million, relating exclusively to SIV investments) including £34 million in respect of Washington Mutual, £3 million in respect of Lehman Brothers and £12 million in respect of our exposure to the Icelandic banks.

Other provisions have been made in respect of various customer claims. It is expected that the liability will predominantly crystallise over the next 12-24 months.

Derivatives and hedge accounting

All derivatives entered into by Nationwide are recorded on the balance sheet at fair value with any valuation movements being taken to the income statement. Derivatives are only used to limit the extent to which the Group will be affected by changes in interest rates, exchange rates or other market indices. Derivatives are therefore used exclusively to hedge risk exposures and are not used for speculative purposes.

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The £10 million gain (4 April 2008: £31 million charge) relating to fair value adjustments on derivatives and hedge accounting represents the net fair value adjustment (after matching it with offsetting adjustments in the fair valuation of the related hedged items) on derivative instruments that are matching risk exposures on an economic basis. Some income statement volatility arises on these items due to accounting ineffectiveness of designated hedges, or because hedge accounting has not been adopted or is not achievable on certain items. The gain, in so far as it relates to ineffectiveness, is primarily due to timing differences in cashflows and interest rate reset dates between the derivative instruments and the hedged assets and liabilities. The impact can be volatile, and has been markedly so at various points during the financial year before stabilising at the year end date. However, over time the impact will trend to zero and has been excluded in reporting the Group's underlying performance.

Policyholder Tax

Prior to the disposal of Nationwide Life and as a consequence of the requirement to consolidate the Group's life business on a line by line basis, the comparative income statement includes amounts attributable to policyholders which affect profit before tax, the most significant of which is policyholder tax. Tax on policyholder investment returns was included in the Group's tax charge rather than being offset against the related income. In order to provide a clearer representation of the performance of the Group, the net impact of amounts attributable to policyholders have been removed from underlying results for the comparative period.

Taxation

The statutory reported tax charge for the year is £50 million (2008: £191 million). This represents an effective tax rate of 23.6% (2008: 27.8%), which is lower than the statutory rate in the UK of 28%. The lower rate is due principally to adjustments to amounts provided in respect of prior periods.

BALANCE SHEET

Loans and advances to customers

Lending remains predominantly concentrated on high quality secured products with residential mortgages accounting for 83.9% of our total loans and advances to customers, commercial lending 14.4%, and consumer finance 1.7%. The mix of lending has remained broadly consistent with that reported at 4 April 2008, with the slightly increased proportion of specialist residential balances attributable largely to the acquisition of assets from the Derbyshire and Cheshire mergers.

Loans and advances to customers	4 April 2009		4 April 2008	
	£bn	%	£bn	%
Prime residential mortgages	111.9	72.1	105.5	73.7
Specialist residential mortgages	18.2	11.8	14.1	9.9
Total residential mortgages	130.1	83.9	119.6	83.6
Commercial lending	22.4	14.4	20.6	14.4
Consumer finance	2.7	1.7	2.8	2.0
Gross balances	155.2	100.0	143.0	100.0
Less: Impairment provisions	(0.4)		(0.2)	
Add: Micro hedge adjustment	0.7		-	
Total	155.5		142.8	

Residential

Retail residential mortgages are primarily Nationwide branded advances made through our branch network and intermediary channels. In addition, our balance sheet includes prime mortgages totalling £5.2 billion which were brought onto our balance sheet following our acquisitions of the Cheshire, Derbyshire and Dunfermline portfolios.

Specialist residential mortgages of £14.8 billion are advances made through our Specialist Lending brands, The Mortgage Works UK plc (TMW) and UCB Home Loans Ltd (UCB), and £3.4 billion arising from the acquisitions of the Cheshire, Derbyshire and Dunfermline brands. Loans were advanced primarily in the Buy to Let and self-certification markets. Buy to Let mortgages make up 62% of total specialist lending, 28% relates to self-certification mortgages, 7% relates to near prime and just 3%, amounting to approximately £0.5 billion relates to sub prime, of which £0.4 billion was acquired as part of the mergers with Derbyshire and Cheshire and have been subject to rigorous fair value assessment.

As advised at the half year, we expected the economic environment to result in continued increases in residential arrears but we predicted that Nationwide's arrears would be markedly better than industry averages. Actual experience has confirmed this expectation and we anticipate that our favourable trend relative to industry average will be maintained.

Cases 3 months or more in arrears as % of total book		4 April 2009	4 April 2008
Nationwide self originated mortgages:	Year on Year movement		
Prime		0.44	0.34
Specialist		2.45	1.11
Nationwide self originated mortgages	50%	0.60	0.40
Including effect of acquired societies:			
Prime		0.46	0.34
Specialist		3.72	1.11
Group – including acquired loans	90%	0.76	0.40
Industry average	103%	2.39	1.18

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Mortgage assets acquired through mergers with Cheshire and Derbyshire and the purchase of Dunfermline’s prime residential assets have been fair valued on a basis which includes an allowance of £203 million for anticipated losses over the remaining life of the loans. These valuations fully reflect market conditions at the date of acquisition and it is therefore unlikely that these loans will contribute any significant further losses to the Group. Accordingly in evaluating the Group’s exposure to losses, as well as the quality of its underwriting process, it is relevant to focus on arrears levels excluding rather than including the effect of acquired assets.

The Nationwide arrears figures above include buy to let cases where a “receiver of rent” has been appointed under the Law of Property Act 1925 (as amended) whereas the CML industry average excludes these cases. For comparison, Nationwide’s figures with LPA receiver cases excluded are as follows:

Cases 3 months or more in arrears as % of total book (excluding LPA)

		4 April 2009	4 April 2008
Nationwide self-originated:	Year on Year movement		
Prime		0.44	0.34
Specialist		2.15	1.11
Group	43%	0.57	0.40
Industry average	103%	2.39	1.18

An alternative measurement of arrears, which is less sensitive to the effect of the significant fall in interest rates experienced in recent months, which reduce monthly payments due and hence increase the number of months in arrears for a constant £ value of arrears, is to show the number of accounts where arrears exceed more than 2.5% of the balance outstanding. Figures based on this measure are given in the following table:

Cases with more than 2.5% of balance outstanding as % of total

		4 April 2009	4 April 2008
Nationwide self-originated:	Year on Year movement		
Prime		0.42	0.40
Specialist		1.28	0.64
Group	17%	0.49	0.42
Industry average	71%	1.85	1.08

The above measures show that the arrears on Nationwide’s overall portfolio are significantly lower than industry average and that the rate of increase in Nationwide’s arrears excluding the impact of fair valued regional brands assets is also much lower.

Possessions of Nationwide originated properties during the year totalled 941 cases (2008: 400 cases) and represented only 2.12% of cases taken in by the industry as a whole compared to our par share of all cases of 11.90%. The closing stock of Group possessions, including acquired societies, of 1,248 cases represents 0.087% of the total portfolio (31 March 08: 0.017%), compared with the industry measure of 0.226% (31 March 2008: 0.132%).

For Specialist, the rate of increase in possessions taken in (excluding mergers) has been more than the average for the industry. However, on our specialist owner occupied lending, the rate of increase is broadly in line with our prime book.

Possessions as % of total book (cases)		4 April 2009	4 April 2008
Nationwide self-originated:	Year on Year movement		
Prime		0.021	0.011
Specialist		0.500	0.092
Group	241%	0.058	0.017
Industry average	71%	0.226	0.132

Possessions taken in during the year as % of total book (cases)		4 April 2009	4 April 2008
Nationwide self-originated:	Year on Year movement		
Prime		0.04	0.02
Specialist		0.50	0.15
Group	133%	0.07	0.03
Industry average	67%	0.40	0.24

We have continued to focus on affordability and loan to value (LTV) ratios in underwriting loans during the year. The average indexed LTV ratio of the Group's residential loan portfolio is estimated at 52% (4 April 2008: 43%) whilst the average LTV of new residential mortgage lending was 58% (4 April 2008: 61%).

Loan to value analysis:	4 April 2009			4 April 2008		
	Prime %	Specialist %	Group %	Prime %	Specialist %	Group %
Total book						
<70%	72	35	69	84	55	82
70% - 80%	8	16	9	7	22	8
80% - 90%	7	20	8	6	20	7
90% - 100%	7	20	8	3	2	3
> 100%	6	9	6	0	1	0
Average LTV of stock (indexed)	50	71	52	41	63	43
Average LTV of new business	57	67	58	59	74	61

Of the balances shown above with LTV in excess of 100%, only 2% of cases were in arrears at 4 April 2009, amounting to balances of approximately £49 million.

Commercial

Excluding assets acquired via the mergers with Derbyshire and Cheshire, our commercial lending portfolio of £21.4 billion comprises £13.3 billion secured on commercial property ("Property Finance"), £6.9 billion advanced to Registered Social Landlords and £1.2 billion under the Private Finance Initiative (PFI). There are currently no arrears of three months or more on the Registered Social Landlord or PFI portfolios. Our Property Finance portfolio is well diversified by industry type and by borrower and we have only modest exposure to development finance with total balances of £99.6 million to 3 high quality office developments.

Challenging market conditions have resulted in sharp declines in capital values on commercial property combined with increases in levels of arrears and defaults, particularly over the second half of the year. There are 179 accounts three months or more in arrears at 4 April 2009 (4 April 2008: 66 accounts, 30 September 2008: 75 accounts) all of which have been individually assessed for impairment. Robust arrears management is carried out by dedicated teams who, supported by daily arrears reporting, maintain a focus on early intervention to maximise

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economic value and mitigate losses. Over the year, the level of provision has increased to £194 million (4 April 2008: £30 million) bringing provision as a percentage of assets to 0.92% (4 April 2008: 0.15%).

Commercial mortgage assets totalling £1.0 billion acquired through mergers with Cheshire and Derbyshire have been fair valued in the same way as described for residential assets above, including an allowance of £179 million for anticipated losses over the remaining life of the loans. As with residential, these loans should not contribute any significant losses to the Group for the foreseeable future.

We expect difficult market conditions to continue into 2009/10 and this will inevitably lead to further provisions. However, we remain confident that our book, which is primarily focused on low risk areas, will perform better than most and this, combined with proactive management, will ensure Commercial continues to make a positive long term contribution to the Group.

Consumer Finance

In consumer finance, the balance of accounts more than 30 days in arrears has remained broadly static and our performance compared to the industry remains favourable. For Personal Loans and Credit Cards, the table below shows our arrears levels are significantly better than averages for the industry (FLA and APACS):

Percentage of accounts more than 30 days in arrears	31 March 2009		31 March 2008	
	NBS %	Industry %	NBS %	Industry %
Personal Loans	7.15	17.00	5.88	11.20
Credit Card	5.70	8.28	4.50	7.99

Funding

The Society has well diversified sources of funding. Over 70% of funding is provided by retail savings, and we attracted a total of £1.7 billion of net retail deposits in the year, including £0.7 billion from our offshore subsidiary, Nationwide International Limited. These retail deposits provided the majority of the funding required for our total residential, commercial and consumer finance net lending in the year of £2.1 billion.

Our strong retail funding base is supported by a well diversified wholesale funding portfolio. Wholesale funding increased to £53.7 billion at 4 April 2009 (4 April 2008: £50.1 billion) but overall the wholesale funding ratio has decreased from 31.0% at 4 April 2008 to 28.6%. Similarly our loan to deposit ratio has improved to 112.4% (4 April 2008: 117.2%). The additional funding has primarily been used to strengthen the liquidity portfolio.

The following table analyses the change in the makeup of wholesale funding and reflects the changes in the marketplace, where secured funding (other than for very short terms) has become commonplace:

Wholesale Funding portfolio mix	4 April 2009 %	4 April 2008 %
Repo & Other Secured Agreements	25.8	17.8
Deposits	12.4	13.2
Certificates of Deposit	16.6	17.6
Commercial Paper	9.9	8.2
Covered Bonds	17.9	18.7
Medium Term Notes	16.1	22.4
Other non-retail	1.3	2.1
Total	100.0	100.0

Nationwide continued its strategic aim of diversifying its funding sources with the completion of the Silverstone Master Trust securitisation structure. Notes have been issued by the Silverstone Master Issuer plc (2008-1 and

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2008-2) to the Society, either to create collateral for funding or for subsequent sale to investors outside the Group once fixed income markets create opportunities for appropriately priced transactions. This capability, combined with our Covered Bond Programme, which successfully achieved Regulated Covered Bond status from the FSA during the year, enables the Society to use its mortgage portfolios as security in support of funding opportunities. The Society has been successful in expanding its secured funding with a variety of market counterparties for periods from 3 months to 5 years. In November we issued £1.5 billion under the UK Government's Credit Guarantee Scheme, assisting us to maintain the ratio of short to long term funding at a consistent level of approximately 67%:33%.

The Society is a Bank of England (BoE) reserve account holder and benefits from the liquidity provided by the BoE's market operations including through the Special Liquidity Scheme (SLS).

Our short and long term credit ratings from the major rating agencies at 26 May 2009 are as follows:

	Long Term	Short Term	Subordinated	Outlook
Standard and Poors	A+	A-1	A	Negative
Moody's	Aa3	P-1	Baa3	Stable
Fitch	AA-	F1+	A+	Stable

More information on our management of funding and liquidity risk will be included in the Principal Risks section within the Annual Report & Accounts 2009.

Treasury Portfolios

Group treasury assets at 4 April 2009 were £34.5 billion (4 April 2008: £31.6 billion). These assets are held in two separate portfolios; the liquidity portfolio and the investment portfolio. At 4 April 2009 the liquidity portfolio totalled £31.1 billion (4 April 2008: £27.3 billion) with the investment portfolio totalling £3.4 billion (4 April 2008: £4.3 billion).

Treasury assets, in the majority of cases, are valued using market prices or prices obtained from counterparties. In cases where market prices are not available, discounted cash flow valuation models are used. 100% of treasury assets are categorised as Level 1 or 2 using the IFRS 7 fair value hierarchy.

Out of a total £34.5 billion of treasury assets held in the liquidity and investment portfolios, £21.2 billion are held as AFS and under IFRS they are marked-to-market through reserves. The non-AFS balances are predominately short term loans to financial institutions or deposits with the Bank of England. The fair value movements of AFS assets, that are not impaired, have no effect on the Group's profit for the year or its regulatory capital. As at 4 April 2009 the balance on the AFS reserve was £2,009 million negative, net of tax (4 April 2008: £418 million negative). The adjustment in the price of these assets is a reflection of the turbulence in worldwide markets and deteriorating economic conditions and the consequent repricing of the cost of credit. The assets have been carefully reviewed based upon latest performance data and no significant additional impairment has been booked in the second half of the year. We continue to believe that we will recover full value for substantially all of them on maturity.

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	Cumulative AFS Reserve 4 April 2009 £bn	Fair Value on balance sheet 4 April 2009 £bn	Cumulative AFS Reserve 4 April 2008 £bn	Fair Value on balance sheet 4 April 2008 £bn
Gilts and Supranational bonds	(0.4)	6.6	-	3.8
Residential mortgage backed securities (RMBS)	0.7	2.7	0.2	3.5
Covered bonds and floating rate notes	0.4	7.5	0.1	6.3
Certificates of deposit and commercial paper	-	1.0	-	7.6
Liquidity portfolio	0.7	17.8	0.3	21.2
Collateralised debt obligations (CDO)	0.1	0.1	-	0.1
Collateralised loan obligations (CLO)	0.2	0.5	-	0.5
Commercial mortgage backed securities	0.3	0.6	0.1	0.9
Corporate bond portfolio	-	0.2	-	0.2
Credit card backed securities	0.1	0.3	-	0.3
Financial institutions including sub debt	0.2	0.6	-	0.6
Residential mortgage backed securities (RMBS)	0.3	0.2	0.1	0.3
US student loan	0.3	0.7	0.1	0.7
Other investments	0.1	0.2	-	0.7
Investment Portfolio	1.6	3.4	0.3	4.3
Negative AFS reserve before hedge accounting and taxation	2.3		0.6	
AFS Assets		21.2		25.5
Hedge accounting adjustment for interest rate risk	0.5		-	
Taxation	(0.8)		(0.2)	
Negative AFS reserve	2.0		0.4	

In October 2008 the IASB issued an amendment to IAS39 allowing assets to be reclassified from AFS to loans and receivables. At this time, we have elected not to make use of this reclassification option.

The Group holds bonds, with a fair value of £63 million, wrapped with additional credit enhancement provided by monoline insurers and these are included within the appropriate portfolios in the following tables. As the bonds are traded explicitly with the benefit of this enhancement, any deterioration in the credit profile of the monoline insurer is reflected in the market prices and therefore in the carrying amount of these securities. £58 million of this exposure is to Ambac and the remainder to MBIA. Only one bond totalling £2 million would need to be considered for immediate impairment if either MBIA or Ambac were to default.

Impairment losses on investment securities

An impairment loss of £51 million has been recognised in the income statement as a result of liquidity issues faced by a number of counterparties. A loss of £34 million has been recognised on a senior unsecured exposure to Washington Mutual Bank which went into FDIC Receivership in September 2008 and a loss of £3 million was recognised in respect of our exposure to Lehman Brothers which filed for bankruptcy protection in September 2008.

We also had exposure to two Icelandic banks which went into receivership during October 2008 and have raised a provision for £12 million. In addition we have also raised a full provision against the remaining £2 million of our original investment in SIVs.

It is important to place these provisions in context. The Group has total assets of £202.4 billion and the total Treasury portfolio is spread across over 500 institutions and investments. The impairment charge of £51 million represents only 0.15% of the total Treasury portfolio of £34.5 billion.

Treasury Liquidity Portfolio

Balance sheet assets held in the Liquidity Portfolio totalled £31.1 billion as at 4 April 2009 (4 April 2008: £27.3 billion). We have continued to increase the quality and liquidity of the assets held, with 48% of the portfolio held in sovereign exposure and over 99% of our liquidity portfolio rated A or better with 78% rated AA or above.

The following table shows an analysis of the on balance sheet liquidity portfolio at 4 April 2009:

Liquidity Portfolio	4 April 2009 £bn	AAA %	AA %	A %	BBB %	UK %	US %	Europe %	Other %	4 April 2008 £bn
Bank of England	8.2	100	-	-	-	100	-	-	-	3.3
Loans to financial institutions	4.7	-	48	52	-	89	-	1	10	2.3
Other (including items in transit and clearing accounts)	0.4	-	-	-	-	100	-	-	-	0.5
Non AFS Assets	13.3									6.1
Gilts	4.7	100	-	-	-	100	-	-	-	3.3
Supranational bonds	1.9	100	-	-	-	-	5	95	-	0.5
Residential mortgage backed securities (RMBS)	2.7	99	1	-	-	40	-	53	7	3.5
Covered bonds	0.9	86	14	-	-	-	3	91	6	0.8
Floating rate notes	6.6	23	23	52	2	34	2	54	10	5.5
Certificates of deposit and commercial paper	1.0	-	25	75	-	100	-	-	-	7.6
AFS Assets	17.8									21.2
Total liquidity portfolio	31.1	64	14	22	-	70	1	25	4	27.3

Ratings are obtained from Standard and Poors in the majority of cases, from Moody's if there is no Standard and Poors rating available, and internal ratings are used if neither is available.

The residual weighted average life of the loans to financial institutions, floating rate notes and certificates of deposit and commercial paper referred to above are 9 days, 30 months and 15 days respectively.

Treasury investment portfolio

The treasury investment portfolio was established to generate additional income for the Group. At 4 April 2009, the investment portfolio totalled £3.4 billion (4 April 2008: £4.3 billion). Over 97% of the investment portfolio is rated A or better with over 76% rated AA or better. In light of current market conditions we have not sought to expand the portfolio and we manage the existing portfolio to minimise potential risk.

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The following table shows an analysis of the investment portfolio at 4 April 2009:

	Investment Portfolio (All AFS Assets)	4 April 2009 £bn	AAA %	AA %	A %	Other %	UK %	US %	Europe %	Other %	4 April 2008 £bn
(i)	Collateralised debt obligations (CDO)	0.1	5	-	-	95	-	100	-	-	0.1
(ii)	Collateralised loan obligations (CLO)	0.5	100	-	-	-	26	70	4	-	0.5
(iii)	Commercial mortgage backed securities	0.6	93	6	1	-	50	11	39	-	0.9
(iv)	Corporate bond portfolio	0.2	13	7	80	-	17	16	67	-	0.2
(v)	Credit card backed securities	0.3	97	3	-	-	47	53	-	-	0.3
(vi)	Financial institutions including subordinated debt	0.6	-	26	69	5	22	35	36	7	0.6
(vii)	Other corporate bonds	-	-	46	54	-	100	-	-	-	0.4
(viii)	Residential mortgage backed securities (RMBS)	0.2	54	22	17	7	55	39	6	-	0.3
(ix)	US student loan	0.7	98	1	1	-	-	100	-	-	0.7
(x)	Other investments	0.2	30	30	37	3	17	45	35	3	0.3
	Total	3.4	65	11	21	3	27	52	19	2	4.3

Ratings are obtained from Standard and Poors in the majority of cases, from Moody's if there is no Standard and Poors rating available, and internal ratings are used if neither is available.

The main reasons for the reduction in the investment portfolio during the period were the maturity in April 2008 of a deep discounted corporate bond with a notional value of £380 million, reduction in asset values and paydowns in Asset Backed Securities. This was partially offset with the assets acquired from the mergers with Derbyshire and Cheshire building societies.

An independent monthly review is undertaken by Risk Management Division on the current and expected future performance of all treasury assets. A governance structure exists to identify and review under performing assets and highlight the likelihood of future losses. In accordance with accounting standards, assets are impaired where there is objective evidence that current events and/or performance trends will result in a loss.

- (i) The CDO exposure of £61 million is made up of four investments. Two are backed by US Prime RMBS (80%), one CDO of US ABS was purchased as part of a SIV restructure (4%) and we own one US Trust Preferred CDO (16%). There is no direct exposure to commercial real estate CDOs or synthetic CDOs.
- (ii) CLOs comprise £472 million of AAA rated assets. Although corporate default rates continue to rise, our senior positions in these structures and our focus on selection of strong managers is anticipated to provide some protection from future downward rating migration.
- (iii) 93% of the CMBS portfolio is AAA and is exposed to established commercial real estate markets with the bulk of our holdings in the UK and Germany. Underlying collateral consists of office, retail, industrial and warehouse exposures with experienced sponsors supporting the underlying loans. The CMBS portfolio includes limited exposure to leisure markets.
- (iv) The £188 million corporate bond portfolio includes £149 million of assets where the credit risk has been fully hedged by entering into credit default swaps (CDS) with a European financial institution (rated by S&P, Moody's and Fitch as A+, Aa1 and AA- respectively).

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- (v) The credit card portfolio is 97% AAA rated and is performing in line with expectations.
- (vi) Of the £553 million held from financial institutions, £352 million is classified as subordinated debt, of which approximately 84% is from UK or European issuers.
- (vii) The other corporate bonds of £19 million are whole business securitisations. Although these benefit from monoline insurance wraps from either Ambac or MBIA, we anticipate full repayment without any assistance from the wrap providers.
- (viii) Our total investment holdings in RMBS are £229 million. Our total US exposure within this portfolio is £89 million of which £66 million is rated AAA. The US exposure is made up of £35 million Prime First Lien and £54 million Alt A. The combined average FICO score at origination was 717 and the average LTV was 76%. There are two US Alt-A holdings totaling £17 million which due to deteriorating economic conditions have migrated from AAA to BB (£6 million) and B (£11 million). The remaining exposure below AAA is to well established UK and European issuers.
- (ix) The US student loan portfolio comprises 71% FFELP (Federal Family Education Loan Programme) originated loans which are 98% guaranteed by the US Government, and 29% Alternative Student Loans. 98% of the Student Loan exposure is AAA rated and there has been only one holding downgraded since initial purchase.
- (x) Included within other investments category are £66 million of unrated coupon strips, underpinned by A or above rated financial institutions, £51 million of lease receivables of which 92% are AAA rated, £28 million of AAA rated other European consumer finance loans, £25 million of auto finance ABS of which 92% is AAA rated, and £32 million structured notes issued by funding vehicles, of which 79% are AA rated insurance companies and 21% A.

CAPITAL STRUCTURE

Capital is held by the Group to protect its depositors, to cover its inherent risks, to provide a cushion for unexpected losses, and to support the development of the business. In assessing the adequacy of its capital resources, the Group considers its risk appetite, the material risks to which the Group is exposed and the appropriate management strategies required to manage those risks. Additional information on our capital management processes will be included in the Risk Management and Control section of the Business Review in the Annual Report & Accounts 2009.

The Group is required to manage its capital in accordance with prudential rules issued by its regulator, the Financial Services Authority (FSA). Since 1 January 2008, and throughout the financial year, the Group has complied with these rules which implement the EU Capital Requirements Directive (Basel II).

As at 4 April 2008 the Group calculated its capital requirement on a Standardised basis. The Group's Internal Ratings Based (IRB) Waiver Application was approved by the FSA in May 2008, with subsequent confirmation from the FSA that Nationwide has cleared the conditions required to use its IRB models to calculate capital requirements. As at 4 April 2009 capital requirements are calculated on this IRB basis. The Group has also received Individual Capital Guidance (ICG) based on the IRB approach.

The following table shows the Group capital position as at 4 April 2009 on the IRB basis. Figures for 2009 are for the enlarged Group which includes the acquisitions of Derbyshire and Cheshire building societies and core parts of the Dunfermline building society. The acquisitions and transition to IRB have resulted in some changes to the capital composition for the enlarged Group. Figures for 2008 show the Nationwide Group prior to the mergers and acquisition and are on a Standardised basis only.

As at 4 April 2009, regulatory capital stood at £9.7 billion (2008: £9.5 billion) with the Group's total solvency ratio remaining strong at 19.5% (2008: 12.4%). The Core Tier 1 solvency ratio stood at 12.1% (2008: 8.1%).

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	4 April 2009 Basel II IRB £m	4 April 2008 Basel II Standardised £m
Tier 1		
General reserve	6,234	6,303
Permanent interest bearing shares (Note 1)	1,526	1,245
Pension fund net deficit add back (Note 2)	167	19
Intangible assets (Note 3)	(211)	(137)
Deductions from Tier 1 capital (Note 4)	(186)	(6)
	7,530	7,424
Tier 2		
Revaluation reserve	69	121
Subordinated debt (Note 1)	2,233	1,743
Collective impairment allowance	60	192
Deductions from Tier 2 capital (Note 4)	(186)	(6)
	2,176	2,050
Total capital	9,706	9,474
Risk weighted assets – Pillar 1 (Note 5)		
Retail mortgages	13,559	43,836
Commercial loans	18,751	17,306
Treasury	9,065	7,891
Other	4,702	3,604
Market Risk	37	39
Operational Risk	3,704	3,962
	49,818	76,638
Key capital ratios:		
Total capital	9,706	9,474
Core Tier 1 (%) (Note 6)	12.1	8.1
Tier 1 ratio (%) (Note 6)	15.1	9.7
Total capital (%) (Note 6)	19.5	12.4
Tier 2 to Tier 1 ratio (%)	28.9	27.6

Notes

- (1) Permanent interest bearing shares and subordinated debt include any fair value adjustments arising from micro hedging and adjustments for unamortised premiums and discounts that are included in the consolidated balance sheet.
- (2) The regulatory capital rules allow the pension fund deficit to be added back to regulatory capital and a deduction taken instead for an estimate of the additional contributions to be made in the next 5 years, less associated deferred tax.
- (3) Intangible assets do not qualify as capital for regulatory purposes.
- (4) Certain deductions from capital are required to be allocated, 50% to Tier 1 and 50% to Tier 2 capital. Deductions are subject to different treatment under IRB in respect of net expected loss over accounting provisions and certain securitisation positions. These are calculated in accordance with FSA guidance.
- (5) The measurement of Risk Weighted Assets differs significantly under IRB and so the stated figures for 4 April 2008 are not directly comparable with those for 4 April 2009. The Basel II Pillar 1 capital requirements are calculated using the Retail IRB approach for prime mortgages and unsecured lending; Foundation IRB for treasury portfolios (excluding corporates); and the Standardised approach for all other credit risk exposures.
- (6) Calculated as relevant capital divided by Risk Weighted Assets. Core Tier 1 relates to Tier 1 capital excluding permanent interest bearing shares.

PENSION FUND (RETIREMENT BENEFIT OBLIGATIONS)

The Group operates Final Salary, Career Average Revalued Earnings (CARE) defined benefit and defined contribution pension arrangements.

The total net retirement benefit liability measured under IAS 19, including the Nationwide Pension Fund, the former Portman Building Society arrangements and the Derbyshire and Cheshire schemes is £331 million (4 April 2008: £40 million). The increase reflects falls in the values of the funds' assets, partly offset by reductions in the IAS 19 liabilities. The Group has not taken over the defined benefit arrangements of the Dunfermline Building Society.

We have been actively managing the retirement benefit liability and have taken a number of steps to contain and reduce the deficit over the last few years:

- Final Salary arrangements closed to new members in 2001 and CARE arrangements closed in 2007;
- Employee contributions (for Nationwide final salary arrangements) increased from 5% to 7%;
- Special contributions of £200 million paid in the period 2005/06 - 2007/08; and
- All the Trustee boards continue to work closely with their advisors to optimise the investment strategy for the schemes' assets.

We will continue to review our options to manage the pension schemes in a responsible way. Following the full triennial valuation of the Nationwide Pension Fund as at 31 March 2007 a plan has been developed to clear the deficit by 2013.

PERFORMANCE BY BUSINESS STREAM

Nationwide classifies its business streams as follows:

Retail

- Prime residential mortgage lending;
- Consumer Finance;
- Retail funding;
- Insurance and Investments;
- Distribution channels supporting these product divisions.

Commercial and Specialist lending

- Commercial lending;
- Specialist residential mortgage lending.

Group

- Treasury group operations and income generation activities;
- Capital;
- Items classified as being non-attributable to our core business areas.

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The contribution to underlying profit before tax against underlying comparatives by each of these business streams is set out in the table below.

	Year to 4 April 2009 Underlying £m	Year to 4 April 2008 Underlying £m
Retail	189	264
Commercial and Specialist lending	18	269
Group	186	248
Total contribution before tax	393	781

RETAIL BUSINESS STREAM

	Year to 4 April 2009 Underlying £m	Year to 4 April 2008 Underlying £m
Total income	1,453	1,462
Expenses	1,138	1,098
Impairment and other provisions	126	100
Contribution from Retail	189	264

The overall contribution from the Retail business stream decreased by 28% to £189 million in the year (2008: £264 million).

Total income was broadly flat with growth in the business following the mergers with Portman, Derbyshire and Cheshire, being offset by a reduction in the net interest margin arising from the low interest rate environment and increased retail funding costs. Over the same period expenses have grown by 4% reflecting the growth in the business.

Impairment and other provisions increased by 26% to £126 million as a result of an increase in the secured provision charge.

Prime residential mortgage lending

The difficult economic conditions combined with falling house prices and lack of consumer confidence have led to a significant reduction in the size of the UK housing and mortgage market in the year. Total UK net mortgage lending fell by almost 80% to £19.4 billion compared to £94.1 billion a year ago. In spite of the significant contraction, we have continued to trade in a manner that demonstrates our commitment to the market and the strength of our mortgage franchise, whilst at the same time giving added support to our members. During the year we launched our Nationwide Homeowner Mortgage Charter, which sets out our promise to work with our customers experiencing temporary financial difficulties to ensure all options are explored to keep them in their homes. Our gross mortgage lending was £16.7 billion (2008: £23.1 billion), whilst net lending was £0.9 billion (2008: £4.9 billion).

During the year we widened our product range to allow more customers the flexibility to build up overpayment reserves and those on tracker products to switch to a fixed rate product at any time. We introduced a new on-line facility enabling customers at the end of their deal to switch to a new product and are on schedule to deliver the first phase of our new flexible mortgage platform which will improve product functionality and operational efficiency.

Consumer Finance

Whilst Consumer Finance products are an important source of income, our market shares have historically been low. This provides us with an opportunity going forward to increase our sales and market share and generate further income for the Group.

The Society's current account, FlexAccount, is the key product in developing and retaining lasting customer relationships and we have been promoting our Account Transfer service to customers in order for them to realise the full benefits of the account. The low base rate environment has provided a challenge and measures have been taken during the year to ensure the sustainability of the product. Credit and debit interest rates have been amended to maintain the margin and some costs charged by VISA for foreign transactions have been passed on to customers as appropriate. We opened 486,000 new current accounts in the year and the total number of accounts is now just under 4.8 million.

Total UK credit card gross lending was down 1% in the year. Against this background, we have seen a growth in lending, with gross lending up 10% to £3.3 billion, representing a market share of just over 2.5%. Card activation rates have remained strong and in February 2009 the Society retained the award for 'Most Responsible Credit Card Lending Practices' at the Card Awards 2009. The Society has reaffirmed its commitment to, and encourages the adoption of a positive order of payments by the credit card industry, especially in the current financial climate.

We continue to adopt a prudent approach to unsecured lending with credit scoring, affordability and indebtedness rules used as part of our assessment of whether to lend or not. Lending criteria has been further tightened during the year and in December 2008 we adopted risk based pricing along with a highly competitive rate. This has resulted in us attracting incremental high credit quality business.

Retail funding

Whilst the current economic conditions have created uncertainty for savers seeking a safe haven for their capital, the low interest rate environment has prompted consumers to become more active in seeking the best return for their money. Overall the savings market has experienced a marked slowdown in the year. The total change in UK Household savings balances, including interest capitalised and accrued, was an increase of £45 billion, compared to £78 billion in the previous year.

Retail savings continue to represent our primary source of funding and new products to enhance our savings range have been launched throughout the year. All ex-Portman savings accounts have now been successfully migrated to Nationwide systems which will improve efficiency and functionality for those members.

Insurance & Investments

Our General Insurance performance has been driven by continued strong sales of buildings and contents cover to our new and existing mortgage customers as well as growth of our standalone home insurance sales through our direct channels.

The primary general insurance products offered by the Group are buildings and contents, payment protection, motor and travel insurances. This year we linked with Liverpool Victoria to provide our customers with access to leading car, travel, commercial and Buy to Let insurance products. We use leading insurers as third-party underwriters to carry the risks involved in insurance. The commissions and profit shares we receive from these insurers are an important source of non-margin income for the Group.

Our Life and Investment products are predominately produced by Legal and General and we are now into our second year of working with them. This is proving very productive and reinforces the decision we took to sell our Life and Unit Trust Companies to them in early 2008. Total Protection and Investment sales in the year were on a par with 2008 volumes and the second half of the year saw 10% growth.

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The Investment market has proved challenging with significant falls and volatility in the FTSE. However, sales of Guaranteed Equity Bonds (GEBs) have performed strongly, with sales increasing by 74% on 2008. Since September 2008, monies invested in GEBs have been held by our Treasury team and this has become a valuable source of medium-term funding for the Society.

Pricing benefit

Pricing benefit is the value that Nationwide estimates that it distributes to its members in the form of favourable product pricing (including interest rates, fees and charges) compared with our competitors. During the year ended 4 April 2009 we estimate that we generated pricing benefit of approximately £680 million by offering better rates and by charging lower fees and charges than our competitors.

Distribution channels

Performance across all distribution channels has held up well during the year, with sales activity up 12% in comparison with last year and against a more challenging economic back drop. Customer satisfaction across all channels remains broadly stable.

Significant investment continues in all channels, underpinning Nationwide's commitment to its retail customers. New premises have been acquired in Leeds, Bristol, Portsmouth and Cheltenham along with work on 115 branches to enhance capacity or maintain the quality of our brand on the high street since April 2008. The Society continually assesses its network to ensure its shape reflects the needs of its members. As a result eight branches were closed this year where local member usage failed to justify and warrant the ongoing cost of maintaining a branch presence.

During the year we moved our Swindon call centre to a purpose built office in west Swindon to expand our telephone service capacity. We have also invested heavily in upgrading our telephone system to deliver improved service levels for our members.

The Internet Bank has performed particularly strongly with sales up 29% over the previous year, whilst internet banking activity is up 36%. Nationwide continues to develop its internet offering launching a new on-line Mortgage Switcher process in August. This allowed 3,861 customers to transfer into a new mortgage deal quickly and simply. Security of customers' on-line transactions has also been increased through the deployment of industry leading remote card authentication to prevent internet fraud, resulting in a reduction of 84%. Nationwide was also awarded 'Best Overall Online Provider' from the Your Money Direct Awards for 2008.

COMMERCIAL AND SPECIALIST LENDING

	Year to 4 April 2009 Underlying £m	Year to 4 April 2008 Underlying £m
Total income	364	338
Expenses	70	74
Impairment and other provisions	276	(5)
Contribution from Non-Retail	18	269

Contribution from the Commercial and Specialist business stream reduced by 93% to £18 million as a result of a significant rise in impairment charges, and represents 5% of the Group's total underlying profit.

Nationwide Building Society – Preliminary Results Announcement

Income rose by 8% in the year reflecting the growth in the specialist lending business following the mergers with Portman, Derbyshire and Cheshire.

Despite the growth in the business, expenses fell 5% in the year as a result of cost focused restructure programmes. Impairment and other provisions increased significantly in the year to £276 million reflecting the difficult market conditions.

Commercial lending

UK commercial property values have been falling since June 2007 and are now approximately 40% below their peak. This market has traditionally relied on debt-financing but the banking crisis has led to reduced flows to the sector, limiting activity and depressing capital values. The collapse of Lehman Brothers in September 2008 was a further blow to confidence and the onset of the global economic downturn has increased the likelihood of tenant failure, depressing rental growth and borrower income.

Having begun the year with tightened lending criteria and reduced volume targets, further lending restrictions were introduced as the downturn in commercial property gathered pace. In addition to a cautious approach to lending the Division undertook a cost focused restructure programme and strengthened arrears management teams. All new lending has been in lower risk sectors on a very selective basis to take advantage of widening margins.

The commercial loan book grew to £22.4 billion (4 April 2008: £20.6 billion) mainly due to the inclusion of balances of £0.6 billion from the Cheshire Building Society and £0.4 billion from the Derbyshire Building Society. Loans to social housing providers increased to £7.2 billion (4 April 2008: £6.3 billion), government sponsored Private Finance Initiatives to £1.2 billion (4 April 2008: £1.1 billion) and exposure to investment property increased to £13.7 billion (4 April 2008: £12.9 billion). The remaining £0.3 billion (4 April 2008: £0.3 billion) relates to a portfolio of European leveraged loans managed by a leading European CLO manager.

Specialist residential mortgage lending

The specialist lending market has contracted significantly in the year with the CML highlighting both a reluctance in landlords to expand their existing portfolios and a reduction in new landlords entering the market. For our specialist lending division, the decline of the specialist lending market has been more than offset by the reduction in competitor activity, caused by the substantial withdrawals and closures of major lenders within the sector.

During the year we have concentrated on delivering value to our members rather than seeking to expand market share. Changes to our lending policy and underwriting criteria have ensured a selective presence in our chosen markets and new business margins have significantly increased.

At 4 April 2009, the total specialist mortgage book was £18.2 billion (2008: £14.1 billion). Of the £4.1 billion increase in balance, £3.4 billion is due to the mergers with Cheshire and Derbyshire and the acquisition of Dunfermline. The Mortgage Works (TMW) is the only active specialist lending brand for Nationwide, following the closure to new lending of UCB in October 2008, and the closure of Cheshire, Derbyshire and Dunfermline at the date of acquisition. There are no proposals to reopen these portfolios.

As anticipated, specialist lending arrears have increased, as explained on pages 16 and 17. Our focus continues to be on the management of arrears and respective losses and product level comparison to industry arrears benchmarks shows that all portfolios exhibit favourable performance.

GROUP BUSINESS STREAM

	Year to 4 April 2009 Underlying £m	Year to 4 April 2008 Underlying £m
Total income	300	412
Expenses	63	61
Impairment and other provisions	51	103
Contribution from Group	186	248

Contribution from the Group business stream fell 25% to £186 million. The majority of this fall was due to the increased cost of holding higher grade liquidity combined with a reduction in the benefit accruing from the base:Libor differential. This has been partly offset by a reduction in treasury provisions.

The current year impairment charge of £51 million relates to impairment losses on investment securities. More information is provided on page 21. The £103 million charge in the prior year primarily relates to an impairment provision on Structured Investment Vehicles.

RESPONSIBILITY STATEMENT

The directors confirm that the financial statements, prepared in accordance with International Financial Reporting Standards as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and income and expenditure of the Group as required by the Disclosure and Transparency rules (DTR 4.1.12). The management report includes a fair review of the development and performance of the business and the Group together with a description of the principal risks and uncertainties faced.

A full list of the Board of Directors will be disclosed in the Annual Report and Accounts 2009. Nationwide's principal inherent risks are described in the Risk Management and Control section of the Business Review in the Annual Report and Accounts.

Signed on behalf of the Board by

Mark Rennison
Group Finance Director
26 May 2009

CONSOLIDATED INCOME STATEMENT
For the year ended 4 April 2009

	Notes	2009 £m	2008 £m
Interest receivable and similar income	3	9,250	9,701
Interest expense and similar charges	4	7,492	7,905
Net interest income		1,758	1,796
Fee and commissions income		359	334
Fee and commissions expense		(4)	(2)
Premiums on insurance contracts and fair value gains on insurance assets	5	-	142
Income from investments		16	25
Other operating income	6	145	3
Gains/(losses) from derivatives and hedge accounting		10	(31)
Profit on sale of a subsidiary		-	10
Total income		2,284	2,277
Insurance claims and change in liabilities	5	-	101
Total income net of claims on insurance contracts		2,284	2,176
Administrative expenses	7	1,252	1,168
Depreciation and amortisation		126	124
Impairment losses on loans and advances to customers	8	394	106
Provisions for liabilities and charges	9	249	(10)
Impairment losses on investment securities		51	102
Profit before tax		212	686
Analysed as:			
• Profit before tax, FSCS levies, transformation costs and gains on business combinations		403	745
• FSCS levies		(241)	-
• Transformation costs and gains on business combinations		50	(59)
Profit before tax		212	686
Taxation		50	191
Profit after tax		162	495

Results relating to the acquisitions of The Derbyshire, The Cheshire and the Dunfermline building societies are included with effect from the date of completion of the acquisitions, 1 December 2008, 15 December 2008 and 30 March 2009 respectively. Results relating to the merger with Portman Building Society were included with effect from the date of completion on 28 August 2007.

Transformation costs totalling £107 million relate to the acquisition of The Derbyshire and The Cheshire building societies, core parts of the Dunfermline Building Society and other costs relating to the restructuring of parts of our business.

Gains on business combinations totalling £157 million relate to the acquisition of The Cheshire Building Society and the acquisition of core parts of the Dunfermline Building Society. Further details are provided in notes 19 and 20.

CONSOLIDATED BALANCE SHEET

As at 4 April 2009

	Notes	2009 £m	2008 £m <i>Reclassified (Note 2)</i>
ASSETS			
Cash and balances with the Bank of England		8,201	3,353
Loans and advances to banks		5,040	2,837
Investment securities - available for sale		21,223	25,486
Derivative financial instruments		5,861	2,408
Fair value adjustment for portfolio hedged risk		3,408	247
Loans and advances to customers	10	155,482	142,804
Investments in equity shares		81	61
Intangible fixed assets		211	137
Property, plant and equipment		886	811
Investment properties		9	15
Accrued income and expenses prepaid		743	555
Deferred tax assets		859	116
Other assets		357	197
Total assets		202,361	179,027
LIABILITIES			
Shares		128,284	113,816
Deposits from banks		13,283	11,777
Other deposits		5,673	4,567
Due to customers		4,371	3,433
Debt securities in issue		34,794	33,772
Fair value adjustment for portfolio hedged risk		239	-
Derivative financial instruments		5,986	1,201
Other liabilities		671	751
Provisions for liabilities and charges	9	271	16
Accruals and deferred income		354	355
Subordinated liabilities	11	2,233	2,058
Subscribed capital	11	1,526	1,245
Current tax liabilities		51	(12)
Retirement benefit obligations		331	40
Total liabilities		198,067	173,019
General reserve	12	6,234	6,303
Revaluation reserve	13	69	121
Available for sale reserve	14	(2,009)	(418)
Cash flow hedge reserve	15	-	2
Total reserves & liabilities		202,361	179,027

CONSOLIDATED STATEMENT OF RECOGNISED INCOME AND EXPENSE

For the year ended 4 April 2009

	Notes	2009 £m	2008 £m
Available for sale investments - net fair value movement	14	(2,212)	(633)
Property revaluation	13	(72)	(19)
Cash flow hedge amortisation	15	(2)	-
Actuarial (loss)/gain on retirement benefit obligations	12	(321)	61
Taxation on items through reserves		731	166
Net income recognised directly in reserves		(1,876)	(425)
Net profit for the year		162	495
Total recognised income and expense for the year		(1,714)	70

CONSOLIDATED STATEMENT OF MOVEMENTS IN RESERVES

For the year ended 4 April 2009

	General reserve £m	AFS reserve £m	Revaluation reserve £m	Cashflow reserve £m	Total £m
At 5 April 2008	6,303	(418)	121	2	6,008
Total recognised income and expense	(69)	(1,591)	(52)	(2)	(1,714)
At 4 April 2009	6,234	(2,009)	69	-	4,294
At 5 April 2007	5,296	41	128	-	5,465
Total recognised income and expense	534	(456)	(8)	-	70
Acquired on transfer of Portman Building Society	697	(3)	8	2	704
Merger related bonus to Portman Building Society members - net of tax	(231)	-	-	-	(231)
Transfers between reserves	7	-	(7)	-	-
At 4 April 2008	6,303	(418)	121	2	6,008

CONSOLIDATED CASH FLOW STATEMENT
For the year ended 4 April 2009

	Notes	2009 £m	2008 £m
Cash flows from operating activities			
Profit before tax		212	686
Adjustments for:			
- Non-cash items included in profit before tax	16	471	400
- Changes in operating assets	16	(11,416)	(31,432)
- Changes in operating liabilities	16	9,425	40,990
- Interest paid on subordinated liabilities		(102)	(87)
- Interest paid on subscribed capital		(127)	(75)
- Taxation		69	(67)
Cash flow from operating activities		(1,468)	10,415
Cash flow from investing activities			
Purchase of investment securities		(14,681)	(23,571)
Sale and maturity of investment securities		18,159	16,260
Purchase of property, plant and equipment		(205)	(179)
Sale of property, plant and equipment		4	21
Sale of investment properties		2	1
Purchase of intangible fixed assets		(61)	(39)
Sale of subsidiary undertaking		-	289
Cash and cash equivalents acquired on transfer of engagements		2,757	392
Cash flow from investing activities		5,975	(6,826)
Cash flows from financing activities			
Maturity of subordinated liabilities		(325)	-
Cash flows from financing activities		(325)	-
Net increase in cash		4,182	3,589
Cash and cash equivalents at start of year		9,212	5,623
Cash and cash equivalents at end of year	16	13,394	9,212

Cash balances transferred into the Group and Society include £1,202 million of cash and cash equivalents acquired on the transfer of business from the Derbyshire, the Cheshire and the Dunfermline Building Societies during the year.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

1 Reporting period

These results have been prepared as at 4 April 2009 and show the financial performance for the year from, and including, 5 April 2008 to this date.

2 Basis of preparation

The 2009 preliminary results have been prepared in line with International Financial Reporting Standards accounting policies ('IFRS') as adopted by the European Union and in effect for the year ending 4 April 2009. The accounting policies adopted for use in the preparation of this Preliminary Results Announcement and which will be used in preparing the Annual Report and Accounts for the year ending 4 April 2009 were included in the 'Annual Report & Accounts 2008' document. Copies of this document are available at www.nationwide.co.uk/about_nationwide/results_and_accounts/.

Business combinations

On 1 December 2008 and 15 December 2008, the Society merged with The Derbyshire Building Society and The Cheshire Building Society respectively, with The Derbyshire and The Cheshire transferring their engagements to the Society. Furthermore on 30 March 2009 the Society acquired core parts of the Dunfermline Building Society.

These business combinations have been accounted for following the requirements of IFRS 3 (2008 Revised): Business Combinations. The revised standard, while approved by the IASB and available for early adoption globally, is yet to be endorsed by the EU. In the absence of any other directly applicable GAAP IFRS 3 (2008 Revised) has been applied in accordance with the principles applicable to selection of accounting policies laid out in IAS 8. The revised standard extends its scope to mutual organisations and applies the acquisition method to business combinations which has resulted in some significant prospective changes to the Group's accounting policies. For example, all assets and liabilities acquired, including intangible assets which may not have been recognised by the acquiree, have been measured at fair value at the acquisition date.

The consideration transferred is valued by reference to the members' interests acquired, and additionally for Dunfermline, the consideration receivable from HM Treasury. Assets and liabilities which, following the Group's accounting policies, would be carried at amortised cost, are bought on to the balance sheet at their fair value at acquisition and are subsequently carried at amortised cost using the effective interest rate method. The income statement includes the results of the engagements transferred from The Derbyshire, The Cheshire and the Dunfermline since 1 December 2008, 15 December 2008 and 30 March 2009 respectively. Further information is provided in notes 19 and 20.

On 28 August 2007, the Society merged with Portman Building Society, with Portman transferring its engagements to the Society. The transfer of engagements was not accounted for in accordance with IFRS 3 'Business Combinations' as the standard at that time specifically excluded business combinations involving two mutual entities. IFRS 3 (2008 Revised) was not available at the time of the Portman merger. The assets and liabilities acquired on transfer of engagements from Portman Building Society were incorporated at their carrying values in the Portman cessation accounts, adjusted to reflect the Group's accounting policies. Details of the transfer are given in note 51 of the 2008 Annual Report and Accounts.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT**2 Basis of preparation (continued)****Prior year reclassification**

A short term deposit of £2,947 million at 4 April 2008 has been re-classified from loans and advances to banks to be included in cash and balances with the Bank of England on the balance sheet date. This change does not affect total assets or total cash and cash equivalents. The consequential change is to the cash and cash equivalents analysis in the notes to the cash flow statement (note 16).

This change has been made to give greater clarity, as under the new treatment all short term cash balances with the Bank of England are identified as such, which management believe is more relevant than the previous treatment of splitting those deposits for regulatory and other such requirements and those deposited solely for operational reasons.

3 Interest receivable and similar income

	2009 £m	2008 £m
On loans fully secured on residential property	6,916	6,547
On other loans	1,083	1,045
On investment securities	1,249	1,111
On other liquid assets	261	247
Net (expense)/income on financial instruments hedging assets	(410)	609
Expected return on pension assets	151	142
	9,250	9,701

4 Interest expense and similar charges

	2009 £m	2008 £m
On shares	4,724	4,964
On subscribed capital	85	76
On deposits and other borrowings		
– Subordinated liabilities	93	90
– Other	1,130	829
Debt securities in issue	1,376	1,565
Foreign exchange differences	4	1
Net (income)/expense on financial instruments hedging liabilities	(61)	266
Pension interest cost	141	114
	7,492	7,905

5 Premiums on insurance contracts and fair value gains on insurance assets and insurance claims and changes in liabilities

These items relate to the Group's life insurance subsidiary, Nationwide Life, which was sold on 31 January 2008 to Legal and General. Since the sale, Nationwide has received commission income on the sale and renewal of Legal and General insurance products sold by Nationwide. This income is included in fees and commission income.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

6 Other operating income

	2009 £m	2008 £m
Gains on business combinations	157	-
Rental income	7	5
Loss on revaluation and sale of fixed assets	(25)	-
Change in value of in force life insurance contract business	-	(8)
Other	6	6
	145	3

More information on the gains on business combinations is provided in notes 19 and 20.

7 Administrative expenses

	2009 £m	2008 £m
Employee costs		
– Wages and salaries	465	431
– Social security costs	40	34
– Pension costs	94	100
	599	565
Other administrative expenses	653	603
	1,252	1,168

Administrative expenses include £107 million of transformation costs, including £32 million directly relating to business combinations (2008: £52 million in respect of the Portman merger), and £2 million relating to the setting up of the new distribution agreement with Legal & General (2008: £7 million). Further details are provided in notes 19 and 20. The remaining £73 million of transformation cost relate to the restructuring of parts of our business.

8 Impairment losses on loans and advances to customers

	2009 £m	2008 £m
Impairment charge/(credit) for the year		
Loans fully secured on residential property	93	(12)
Loans fully secured on land	169	(4)
Other loans	132	122
	394	106
Impairment provision at the end of the year		
Loans fully secured on residential property	123	38
Loans fully secured on land	192	30
Other loans	155	144
	470	212

These provisions have been deducted from the appropriate asset values in the balance sheet.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT**9 Provisions for liabilities and charges**

	FSCS £m	Other Provisions £m	Total £m
At 5 April 2008	-	16	16
Acquired on acquisitions:			
Derbyshire	7	-	7
Cheshire	6	-	6
Dunfermline	4	-	4
Provisions utilised	-	(11)	(11)
Charge for the year	241	8	249
At 4 April 2009	258	13	271
At 5 April 2007	-	50	50
Provisions utilised	-	(24)	(24)
Release for the year	-	(10)	(10)
At 4 April 2008	-	16	16

Financial Services Compensation Scheme

Based on its share of protected deposits, the Group pays levies to the Financial Services Compensation Scheme (FSCS) to enable the FSCS to meet claims against it. In September 2008 a claim was triggered against the FSCS by the transfer of Bradford and Bingley plc's retail deposit business to Abbey National plc. Further claims have been triggered by the failures of various Icelandic Banks, London Scottish plc and the transfer of the core parts of Dunfermline Building Society to the Group.

The FSCS has met, or will meet, the claims by way of loans received from HM Treasury. The terms of these loans are interest only for the first three years and the FSCS will seek to recover the interest cost, together with ongoing management expenses, by way of annual levies on member firms over this period. The FSCS has, in turn, acquired the rights to the realisation of the assets of these financial institutions. The FSCS may have a further liability if there are insufficient funds available from the realisation of the assets of the financial institutions to fully repay the HM Treasury loans.

The Group has recognised a charge in the year for levies of £241 million. This charge is in addition to provisions totalling £17 million acquired on the transfers of business of The Derbyshire, The Cheshire and acquisition of core parts of the Dunfermline Building Societies. The resulting total provision of £258 million is the Group's estimated share of the levies which it will incur in respect of the period of the initial three year loan facility from HM Treasury. The provision has been calculated based on the Group's estimated share of protected deposits, the FSCS's latest estimates for the industry's levies for scheme years 2008/09 and 2009/10, estimated capital amounts outstanding on the HM Treasury loans and future Libor rates in respect of levies of subsequent scheme years. The amounts do not take account of any levies which may be payable from any refinancing after the maturity of the initial 3 year loan facility or which may be payable should the FSCS fail to recover sufficient funds to repay its loans, as any such amounts cannot currently be reliably estimated.

Other provisions

Other provisions have been made in respect of various customer claims. It is expected that the liability will predominantly crystallise over the next 12 – 24 months.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

10 Loans and advances to customers

	2009 £m	2008 £m
Loans fully secured on residential property	138,794	127,078
Loans fully secured on land	11,750	11,476
Other loans	4,219	4,225
	154,763	142,779
Fair value adjustment for micro hedged risk	719	25
	155,482	142,804

Loans fully secured on land include £374 million (2008: £294 million) of loans which are fully secured on residential property but are classified as ‘loans fully secured on land’ in accordance with the Building Societies Act 1997.

A detailed analysis of loans and advances to customers is given below:

	2009 £m	2008 £m
Retail - Prime residential mortgages	111,893	105,538
Non-retail - Specialist residential mortgages	18,160	14,045
Total residential mortgages	130,053	119,583
Commercial lending	22,506	20,633
Unsecured personal lending	1,503	1,696
Credit card	885	801
Overdrawn current accounts	286	278
	155,233	142,991
Impairment provisions	(470)	(212)
Fair value adjustment for micro hedged risk	719	25
	155,482	142,804

Certain loans and advances to customers are used to secure debt securities in issue (funding) as follows:

	2009		2008	
	Assets pledged £m	Secured funding £m	Assets pledged £m	Secured funding £m
Covered bonds	38,130	9,408	18,680	9,356
Securitisations and other secured lending	29,401	1,498	-	-
	67,531	10,906	18,680	9,356

Pledged assets include those available to Nationwide Covered Bonds LLP, Silverstone Master Trust and other funding vehicles, even where they have not yet been used to provide collateral to support external funding transactions. Secured funding disclosed above, however, is that obtained from issuance to external counterparties and does not include self issuances that may be used in the future as collateral for repo and other similar type operations. As a result, the relationship between pledged assets and secured funding above is not representative of the haircut applied to collateral values in determining the available level of funding.

The Society established the Silverstone Master Trust securitisation structure on 16 July 2008. Notes are issued by Silverstone Master Issuer plc (Securities 2008 -1 and 2008 - 2) to the Society, either for the

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

10 Loans and advances to customers (continued)

purposes of creating collateral to be used for funding or for subsequent sale of notes to investors outside the Group.

The Society established Nationwide Covered Bonds LLP in 2005. The LLP provides security to issues of covered bonds made by the Society to external counterparties and also for the purposes of creating collateral.

11 Subordinated liabilities and subscribed capital

	2009 £m	2008 £m
Subordinated liabilities		
Subordinated notes	2,116	2,035
Fair value adjustment for micro hedged risk	127	29
Unamortised premiums and issue costs	(10)	(6)
	2,233	2,058
Subscribed capital		
Permanent interest bearing shares	1,415	1,235
Fair value adjustment for micro hedged risk	161	20
Unamortised premiums and issue costs	(50)	(10)
	1,526	1,245

All of the Society's subordinated notes and permanent interest bearing shares (PIBS) are unsecured. The Society may, with the prior consent of the FSA, redeem some of the subordinated notes and PIBS early.

On 7 May 2009, the Group, with the consent of the FSA, redeemed early £15 million of subordinated notes due 2014 at a cost of £15 million.

On 11 April 2008 the Group, with the consent of the FSA, redeemed early Euro 400 million of subordinated floating rate notes due 2013 at a cost of £325 million.

The subordinated notes rank pari passu with each other and behind claims against the Society of all depositors, creditors and investing members. The PIBS rank pari passu with each other and behind claims of the subordinated notes. The claims of the PIBS holders in a winding-up or dissolution of the Society would be restricted to the principal amount of the PIBS together with the interest accrued.

12 General reserve

Movements in general reserve were as follows:	2009 £m	2008 £m
At 5 April 2008	6,303	5,296
Acquired on transfer of engagements of Portman	-	697
Merger related bonus to Portman members	-	(329)
Tax on merger related bonus to Portman members	-	98
Profit for the year	162	495
Actuarial (loss)/gain on retirement benefit obligations	(321)	61
Tax on actuarial (loss)/gain on retirement benefit obligations	90	(18)
Change in the rate of deferred taxation	-	(4)
Transfer from the revaluation reserve	-	7
At 4 April 2009	6,234	6,303

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

13 Revaluation reserve

Movements in the revaluation reserve were as follows:	2009	2008
	£m	£m
At 5 April 2008	121	128
Acquired on transfer of engagements - Portman	-	8
Revaluation decrease on land and buildings	(72)	(19)
Decrease in deferred tax liability on revaluation of land and buildings	20	11
Transfer to the general reserve	-	(7)
At 4 April 2009	69	121

14 Available for sale reserve

Movements in the available for sale reserve were as follows:	2009	2008
	£m	£m
At 5 April 2008	(418)	41
Acquired on transfer of engagements – Portman	-	(3)
Net loss from changes in fair value	(2,216)	(726)
Amounts transferred to income statement on disposal and impairment	4	93
Decrease in tax liability	621	177
At 4 April 2009	(2,009)	(418)

15 Cash flow hedge reserve

Movements in the cash flow hedge reserve were as follows:	2009	2008
	£m	£m
At 5 April 2008	2	-
Acquired on transfer of engagements	-	2
Amortisation	(2)	-
At 4 April 2009	-	2

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

16 Notes to the cash flow statement

	2009 £m	2008 £m
Non-cash items included in profit before tax		
Net increase/(decrease) in impairment provisions	258	(14)
Impairment loss on investment securities	51	102
Depreciation and amortisation	126	124
Loss on sale of property, plant and equipment	3	1
Loss on revaluation and sale of investment property	6	-
Interest on subordinated liabilities	93	90
Interest on subscribed capital	85	76
Loss on the revaluation of land and buildings	16	-
(Gain)/loss from derivatives and hedge accounting	(10)	31
Gains on business combinations	(157)	-
Profit on sale of subsidiary undertaking	-	(10)
	471	400
Changes in operating assets		
Loans and advances to banks	(325)	(35)
Investment securities	(543)	(3,126)
Derivative financial instruments and fair value adjustment for portfolio hedged risk	(7,085)	(2,359)
Other financial assets at fair value	-	(537)
Deferred tax assets	(659)	(62)
Loans and advances to customers	(2,483)	(26,726)
Other operating assets	(321)	1,413
	(11,416)	(31,432)
Changes in operating liabilities		
Shares	4,490	27,020
Deposits from banks, customers and others	856	9,343
Derivative financial liabilities and fair value adjustment for portfolio hedged risk	4,769	529
Debt securities in issue	356	4,900
Insurance contracts liabilities	-	(1,228)
Retirement benefit obligations	298	(133)
Other operating liabilities	(1,344)	559
	9,425	40,990
Cash and cash equivalents		
Cash and balances with the Bank of England	8,201	3,353
Loans and advances to other banks repayable in 3 months or less	4,262	2,636
Investment securities with a maturity period of 3 months or less	931	3,223
	13,394	9,212

The group is required to maintain balances with the Bank of England which, at 4 April 2009, amounted to £173 million (2008: £197 million). These balances are included within loans and advances to banks on the balance sheet and are not included in the cash and cash equivalents in the cash flow statement as they are not liquid in nature.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

17 Segmental reporting

2009	Retail £m	Commercial and Specialist Lending £m	Group £m	Total £m
Net interest income	921	2,179	(1,342)	1,758
Transfers between segments in respect of funding	185	(1,829)	1,644	-
	1,106	350	302	1,758
Other income (note i)	347	14	155	516
Total revenue	1,453	364	457	2,274
Expenses (note i)	1,264	346	221	1,831
Segment results (note ii)	189	18	236	443
FSCS levies				(241)
Gains from derivatives and hedge accounting				10
Profit before tax				212
Taxation				50
Profit after tax				162

2008	Retail £m	Commercial and Specialist Lending £m	Group £m	Total £m
Net interest income	451	1,830	(485)	1,796
Transfers between segments in respect of funding	637	(1,504)	867	-
	1,088	326	382	1,796
Other income	360	11	40	411
Total revenue	1,448	337	422	2,207
Expenses (note i)	1,199	68	223	1,490
Segment results (note ii)	249	269	199	717
(Losses) from derivatives and hedge accounting				(31)
Profit before tax				686
Taxation				191
Profit after tax				495

Notes

- (i) Expenses includes impairment losses on loans and advances to customers, provisions for liabilities and charges (excluding FSCS levies) and impairment losses/gains on investments but excludes gains from derivatives and hedge accounting. Other income in 2009 includes gains on business combinations.
- (ii) The Group segment for 2009 differs from the corresponding underlying result in the Business Review (see page 31) as the latter excludes transformation costs and gains on business combinations. The Retail segment for 2008 differs from the corresponding underlying result in the Business Review (see page 27) as the latter excludes the tax attributable to policyholder earnings. The Group segment for 2008 differs from the corresponding underlying result in the Business Review (see page 31) as the latter excludes costs relating to the merger and the disposal of Nationwide's life, investment and pensions subsidiaries.

The Group operates predominantly in the UK, the Isle of Man and the Republic of Ireland and accordingly no geographical analysis has been presented.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

18 Debt securities in issue

Nationwide continued its strategic aim of diversifying its funding sources with the completion of the Silverstone Master Trust securitisation structure. Notes have been issued by Silverstone Master Issuer plc (Securities 2008-1 and 2008-2) to the Society, either to create collateral for funding or for subsequent sale to investors outside the Group once fixed income markets create opportunities for appropriately priced transactions. In November we issued £1.5 billion under the UK Government's Credit Guarantee Scheme, assisting us to maintain the ratio of short to long term funding at a consistent level of approximately 67%:33%.

19 Transfer of engagements

On 1 December 2008 and 15 December 2008, the Society acquired all of The Derbyshire Building Society (The Derbyshire) and all of The Cheshire Building Society (The Cheshire) respectively. The primary reason for the acquisitions was to enhance the strength and stability of the Building Society sector. The Boards of The Derbyshire and The Cheshire independently reached a conclusion that merging with Nationwide was in the best interests of their members, given the current uncertain economic environment and following the identification of financial issues faced by both Societies. From the Nationwide perspective, the acquisitions provided an opportunity to build on its strong position within the financial services sector by adding two attractive customer franchises to its existing operations.

The Consolidated Income Statement of the Group includes acquisition related administrative expenses for The Derbyshire and The Cheshire of £12 million. As the merger programmes for both The Derbyshire and The Cheshire were run jointly it is impractical to split these costs between the two acquisitions.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

19 Transfer of engagements (continued)

The Derbyshire Building Society

The assets and liabilities acquired and associated fair value adjustments required to conform with IFRS 3 (2008 Revised) 'Business Combinations' are set out below:

Balance Sheet		Cessation Accounts UK GAAP Format £m	IFRS Re-class £m	Fair Value Adjustments £m	Acquisition Fair Values £m
	Notes				
ASSETS					
Cash and balances with the Bank of England		5	-	-	5
Loans and advances to banks		671	-	-	671
Investment securities - available for sale	ii	423	-	(96)	327
Derivative financial instruments	i/iii	-	41	79	120
Loans and advances to customers	iv	5,073	-	(75)	4,998
Investments in equity shares		-	-	1	1
Intangible assets	v	-	2	21	23
Property, plant and equipment	v	22	(2)	(1)	19
Current tax assets		2	-	-	2
Deferred tax assets	vi	20	-	43	63
Other assets	vii	26	-	(25)	1
Accrued income and expenses prepaid	i	43	(41)	1	3
Total assets		6,285	-	(52)	6,233
LIABILITIES					
Shares	viii	4,365	(2)	54	4,417
Deposits from banks		347	-	-	347
Due to customers		743	-	5	748
Debt securities in issue	ix	377	-	32	409
Derivative financial instruments	iii	-	2	72	74
Provisions for liabilities and charges	x	-	-	7	7
Other liabilities		13	-	-	13
Accruals and deferred income		7	-	-	7
Subordinated liabilities	ix	105	-	(1)	104
Subscribed capital	ix	143	-	(36)	107
Total liabilities		6,100	-	133	6,233
Net identifiable assets		185	-	(185)	-
Imputed consideration	xi				-
Gain on acquisition					-

Explanation of material adjustments to take on balances

- i. The cessation accounts of The Derbyshire have been prepared in accordance with UK Generally Accepted Accounting Principles (UK GAAP) and some balance sheet reclassifications have therefore been made to conform with IFRS formats. The most material of these has been to reclassify accrued interest on derivative financial instruments from Accrued Income and Expenses Prepaid to Derivative Financial Instruments.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

19 Transfer of engagements (continued)

- ii. Investment securities were previously carried at amortised cost subject to impairment. These are now included at fair value using market prices or prices obtained from counterparties.
- iii. Derivative financial instruments were previously carried at amortised cost and these are now included at fair value based on discounted future cash flow models with market inputs valued consistently with the Group.
- iv. Loans and advances to customers were previously carried at amortised cost subject to impairment and have been recognised at fair value at the acquisition date. The acquisition fair value adjustment reflects both credit and interest rate risk associated with these assets. This fair value acquisition becomes the new amortised cost for acquired loans and receivables.
- v. Identifiable intangible assets are in respect of core deposits, £16 million (recognising the intrinsic value of the retail savings book), customer relationships (income streams from renewable contracts – primarily insurance) and brand, £1 million, and goodwill, £4 million (recognising the benefit to the Group of The Derbyshire savings book). The core deposit and customer relationships and brand intangibles will be amortised over their useful lives of between 5 and 10 years. The goodwill will be subject to an annual impairment review. In addition, £2 million of computer software has been reclassified from Property, Plant and Equipment to Intangible Assets. We have classified the former head office of the acquired Society as a specialised administration building.
- vi. The deferred tax adjustment reflects the tax consequences of the other fair value adjustments made.
- vii. The other asset fair value adjustment primarily reflects the write off of premiums paid by The Derbyshire to acquire mortgage books.
- viii. The fair value adjustment for shares reflects interest rate risk associated with these liabilities. Under UK GAAP these liabilities were carried at amortised cost.
- ix. The fair value adjustments for debt securities in issue, subscribed capital and subordinated liabilities reflect both credit and interest rate risk associated with these liabilities. Under UK GAAP these liabilities were carried at cost.
- x. This represents recognition of the FSCS liability relating to The Derbyshire savings balances transferred to the Group.
- xi. Consideration represents the fair value of members' interests transferred. The combination of the two societies did not involve the transfer of any cash consideration. The value of the consideration has been calculated by measuring the fair value of The Derbyshire business. The calculation has been made with reference to quoted financial services organisations with publicly available valuations, adjusted to take account of such items as the relative size, financial status, economic diversification and the unquoted nature of the business. This has resulted in a value of £nil attributed to the consideration.

The cessation accounts of The Derbyshire for the period 1 January 2008 to 30 November 2008, audited by KPMG, reported net interest income of £40 million and a post tax loss of £70 million. To calculate an estimate of the results of the business combination from the beginning of the year, we estimate that net interest income of £27 million and a post tax loss of £69 million relating to The Derbyshire would be added to the figures as reported in the Group income statement.

Following the merger, The Derbyshire ceased to exist, being subsumed by Nationwide Building Society. It is thus not possible to separate its results post the transfer of engagements.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

19 Transfer of engagements (continued)**The Cheshire Building Society**

The assets and liabilities acquired and associated fair value adjustments required to conform with IFRS 3 (2008 Revised) 'Business Combinations' are set out below:

Balance sheet	Notes	Cessation Accounts £m	Fair value Adjustments £m	Acquisition Fair Value £m
ASSETS				
Cash and balances with the Bank of England		57	-	57
Loans and advances to banks		139	(1)	138
Investment securities – available for sale	i	639	(8)	631
Derivative financial instruments	ii	35	5	40
Loans and advances to customers	iii	3,755	(26)	3,729
Intangible assets	iv	2	10	12
Property, plant and equipment	iv	15	1	16
Investment properties		3	(1)	2
Current tax asset		1	-	1
Deferred tax asset		4	2	6
Other assets		1	-	1
Accrued income and expenses prepaid		2	-	2
Retirement benefit asset		7	-	7
Total assets		4,660	(18)	4,642
LIABILITIES				
Shares	v	3,236	19	3,255
Deposits from banks	v	291	1	292
Due to customers	v	521	5	526
Debt securities in issue	vi	262	(5)	257
Derivative financial instruments	ii	93	12	105
Deferred tax liabilities		4	-	4
Provisions for liabilities and charges	vii	-	6	6
Accruals and deferred income		8	-	8
Subordinated liabilities	vi	65	(2)	63
Subscribed capital	vi	41	(4)	37
Total liabilities		4,521	32	4,553
Net identifiable assets		139	(50)	89
Imputed consideration	viii			-
Gain on acquisition	ix			89

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

19 Transfer of engagements (continued)

Explanation of material adjustments to take on balances

- i. The fair value adjustment in respect of investment securities reflects the adoption of more prudent counterparty risk valuations. The methodology used is fully consistent with that used by the Group.
- ii. The fair value adjustment in respect of derivative financial instruments arises from the adoption of Nationwide's discounted cash flow models.
- iii. Loans and advances to customers were previously carried at amortised cost subject to impairment and have been recognised at fair value at the acquisition date. The acquisition fair value adjustment reflects both credit and interest rate risk associated with these assets. This fair value acquisition becomes the new amortised cost for acquired loans and receivables. Furthermore, the fair value hedge adjustment of £72 million recognised in The Cheshire cessation accounts has been written off.
- iv. The intangible assets are in respect of core deposits, £9 million (recognising the intrinsic value of the retail savings book) and customer relationships (income streams from renewable contracts – primarily insurance) and brand, £1 million. These intangibles will be amortised over their useful lives of between 5 and 10 years. We have classified the former head office of the acquired Society as a specialised administration building.
- v. The fair value adjustments for shares, deposits from banks and due to customers reflect interest rate risk associated with these liabilities. Under IFRS these liabilities were previously carried at amortised cost.
- vi. The fair value adjustments for debt securities in issue, subscribed capital and subordinated liabilities reflect both credit and interest rate risk associated with these liabilities. Under IFRS these liabilities were carried at amortised cost.
- vii. The fair value adjustment for provisions for liabilities and charges represents the FSCS liability relating to The Cheshire savings balances transferred to the Group.
- viii. Imputed consideration represents the fair value of members' interests transferred. The combination of the two societies did not involve the transfer of any cash consideration. The value of the consideration has been calculated by measuring the fair value of The Cheshire business. The calculation has been made with reference to quoted financial services organisations with publicly available valuations, adjusted to take account of such items as the relative size, financial status, economic diversification and the unquoted nature of the business. This has resulted in a value of £nil attributed to the consideration.
- ix. Net identifiable assets in excess of consideration transferred results in a gain on acquisition. IFRS 3 (Revised 2008) requires that, where the fair value of the acquired assets exceeds the consideration transferred, the acquirer should reassess the identification and measurement of the assets, liabilities and contingent liabilities and the measurement of the consideration. After completing this additional review, in accordance with the requirements of IFRS 3 (Revised 2008), this gain has been recognised in the income statement. The gain represents the fact that, in the distressed market conditions at the acquisition date, the value of net assets acquired was greater than the value of the ongoing business on a standalone basis, represented by imputed consideration.

The cessation accounts of The Cheshire for the period 1 January 2008 to 14 December 2008, audited by KPMG, reported net interest income of £31 million and a post tax loss of £34 million. To calculate an estimate of the result of the business combination from the beginning of the year, we estimate that net interest income of £23 million and a post tax loss of £36 million relating to The Cheshire would be added to the figures as reported in the Group income statement.

Following the merger, The Cheshire ceased to exist, being subsumed by Nationwide Building Society. It is thus not possible to separate its results post the transfer of engagements.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT**20 Acquisition**

On 30 March 2009 the Society acquired the retail and wholesale deposits, branches, head office and originated residential mortgages (other than social housing loans and related deposits) of Dunfermline Building Society (Dunfermline). This acquisition follows a sale process conducted by the Bank of England under the Special Resolution Regime provisions of the Banking Act 2009. The acquisition was designed to protect Dunfermline's members and depositors who became Nationwide members and depositors on the acquisition date.

On acquisition H M Treasury made a payment to the Society of £1.5 billion to cover the net liabilities that are not covered by the acquired assets.

As the acquisition took place immediately prior to year end, at the date of preparing the Group financial statements the information required to value the acquisition was incomplete. The initial accounting for the Dunfermline acquisition has thus been determined provisionally. Any revisions to fair values will be recognised as adjustments to the initial accounting in the following period. The Dunfermline will not be preparing any cessation accounts.

The provisional fair values of assets and liabilities acquired are set out below:

	Notes	Provisional Fair Values £m
ASSETS		
Cash and balances with the Bank of England		2
Loans and advances to banks		578
Investment securities – available for sale		9
Derivative financial instruments		53
Loans and advances to customers	i	1,032
Intangible assets	ii	15
Property, plant and equipment	ii	10
Accrued income and expenses prepaid		2
Other assets		35
Total assets		1,736
LIABILITIES		
Shares	iii	2,306
Deposits from banks	iii	50
Derivative financial instruments		76
Other deposits	iii	731
Provisions for liabilities and charges	iv	4
Accruals and deferred income		2
Total liabilities		3,169
Net identifiable liabilities		1,433
Cash consideration		1,501
Imputed consideration		-
Total Consideration		1,501
Gain on acquisition	v	68

The Consolidated Income Statement of the Group includes acquisition related administrative expenses for the Dunfermline of £2 million.

NOTES TO THE PRELIMINARY RESULTS ANNOUNCEMENT

20 Acquisition (continued)

Explanation of material provisional fair value adjustments

- i Loans and advances to customers have been adjusted to reflect both credit and interest rate risk associated with these assets. Note only originated residential mortgages (other than social housing loans) were acquired.
- ii Identifiable intangible assets recognised under IFRS 3 (2008 Revised) is in respect of core deposits (recognising the intrinsic value of the retail savings book), customer relationships (income streams from renewable contracts – primarily insurance) and brand. These intangibles will be amortised over their useful lives of between 5 and 10 years. We have classified the former head office of the acquired Society as a specialised administration building
- iii Shares, deposits from banks and other deposits have been adjusted to reflect interest rate risk associated with these liabilities.
- iv This represents recognition of the FSCS liability relating to The Dunfermline savings balances transferred to the Group.
- v The gain on acquisition primarily represents the discount given as part of commercial negotiations prior to the purchase of the identified assets and liabilities by the Society.
- vi The Group did not acquire any rights, obligations or liabilities in respect of The Dunfermline Building Society pension scheme.

The results for the five day period post acquisition are deemed immaterial to the Group. As only part of the Dunfermline Building Society was acquired it is not possible to disclose the revenue and profit/loss of the combined entity as though the acquisition had taken place at the beginning of the year.

ADDITIONAL INFORMATION

a) Total Residential mortgages

The average LTV of Residential mortgages is 52% (4 April 2008: 43%) whilst the average LTV of new lending was 58% (4 April 2008: 61%). The value of residential property is updated on a quarterly basis to reflect changes in the house price index. Further LTV information is set out as follows:

	2009	2008
	%	%
Loan to value analysis:		
Total book		
<50%	51	63
50% - 60%	9	10
60% - 70%	9	9
70% - 80%	9	8
80% - 90%	8	7
90% - 100%	8	3
>100%	6	0
Average loan to value of stock (indexed)	52	43
Average loan to value of new business	58	61
New business profile:		
First-time buyers	16	19
Home movers	22	39
Remortgagers	54	37
Buy to let	8	5

b) Retail business stream

The table below provides further information on our prime residential loans and advances by payment due status:

	2009				2008			
	Residential Mortgages £bn	Consumer Finance £bn	Balance Outstanding £bn	%	Residential Mortgages £bn	Consumer Finance £bn	Balance outstanding £bn	%
Not impaired:								
Neither past due nor impaired	109.6	2.4	112.0	98	102.8	2.6	105.4	97
Past due up to 3 months but not impaired	1.9	0.1	2.0	2	2.4	0.1	2.5	3
Impaired	0.4	0.2	0.6	-	0.3	0.1	0.4	-
	111.9	2.7	114.6	100	105.5	2.8	108.3	100

The status “neither past due not impaired” includes any asset where a payment due under strict contractual terms is received late or missed. The amount included is the entire financial assets rather than just the payment overdue.

Loans in the analysis above which are less than 3 months past due have collective impairment allowances set aside to cover credit losses on loans which are in the early stages of arrears, apart from loans acquired from the Cheshire, the Derbyshire and the Dunfermline. These have had allowances set aside to cover anticipated losses as part of the fair value assessment.

Impaired Retail assets are further analysed as follows:

ADDITIONAL INFORMATION (continued)

	2009				2008			
	Residential Mortgages £m	Consumer Finance £m	Balance Outstanding £m	%	Residential Mortgages £m	Consumer Finance £m	Balance outstanding £m	%
Impaired status:								
Past due 3 to 6 months	217	63	280	51	190	61	251	58
Past due 6 to 12 months	100	70	170	31	60	71	131	30
Past due over 12 months	26	37	63	12	14	30	44	10
Possessions	33	0	33	6	10	-	10	2
	376	170	546	100	274	162	436	100

£50 million (2008: £23 million) of loans that would be past due or impaired have had their terms renegotiated in the last 12 months.

Collateral held against Retail residential mortgages	2009 £m	2009 %	2008 £m	2008 %
Past due but not impaired	1,937	99	2,381	100
Impaired	340	99	263	100
Possessions	31	94	10	100
	2,308	99	2,654	100

Collateral held in relation to secured loans that are either past due or impaired is capped to the amount outstanding on an individual loan basis. The percentage in the table above is the cover over the impaired asset.

Negative Equity on Retail residential mortgages	2009 £m	2008 £m
Past due but not impaired	8	3
Impaired	3	1
Possessions	2	0
	13	4

c) *Commercial and Specialist Lending business streams*

The table below provides further information on Commercial and Specialist Lending loans and advances by payment due status:

	2009				2008			
	Specialist Lending £bn	Commercial Lending £bn	Total £bn	%	Specialist Lending £bn	Commercial Lending £bn	Total £bn	%
Not impaired:								
Neither past due nor impaired	15.7	21.5	37.2	92	13.2	20.4	33.6	96
Past due up to 3 months but not impaired	1.4	0.5	1.9	4	0.7	0.2	0.9	3
Impaired	1.1	0.4	1.5	4	0.2	-	0.2	1
	18.2	22.4	40.6	100	14.1	20.6	34.7	100

The status “neither past due not impaired” includes any asset where a payment due under strict contractual terms is received late or missed. The amount included is the entire financial assets rather than just the payment overdue.

Loans in the analysis above which are less than 3 months past due have collective impairment allowances set aside to cover credit losses on loans which are in the early stages of arrears, apart from loans acquired from the Cheshire, the Derbyshire, and the Dunfermline. These have had allowances set aside to cover anticipated losses as part of the fair value assessment.

ADDITIONAL INFORMATION (continued)

Impaired Commercial and Specialist Lending assets are further analysed as follows:

	2009				2008			
	Specialist Lending £m	Commercial Lending £m	Total £m	%	Specialist Lending £m	Commercial Lending £m	Total £m	%
Impaired status:								
Past due 3 to 6 months	443	122	565	38	107	20	127	53
Past due 6 to 12 months	320	229	549	37	51	9	60	25
Past due over 12 months	117	21	138	10	28	9	37	15
Possessions	215	12	227	15	17	-	17	7
	1,095	384	1,479	100	203	38	241	100

£45 million (2008: £28 million) of loans that would be past due or impaired have had their terms renegotiated in the last 12 months.

Collateral held against Commercial and Specialist lending	2009 £m	2009 %	2008 £m	2008 %
Past due but not impaired	1,844	97	819	95
Impaired	1,204	96	222	99
Possessions	218	96	16	94
	3,266	97	1,057	96

Collateral held in relation to secured loans that are either past due or impaired is capped to the amount outstanding on an individual loan basis. The percentage in the table above is the cover over the impaired asset.

Negative Equity on Commercial and Specialist lending	2009 £m	2008 £m
Past due but not impaired	53	42
Impaired	48	2
Possessions	9	1
	110	45

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OTHER INFORMATION

The financial information set out in this announcement which was approved by the Board on 26 May 2009, does not constitute accounts within the meaning of section 73 of the Building Societies Act 1986.

The Annual Accounts for the year ended 4 April 2008 have been filed with the Financial Services Authority and Registry of Friendly Societies in England and Wales. The Auditors' Report on these Annual Accounts was unqualified. The Annual Accounts for the year ended 4 April 2009 will be lodged with the Financial Services Authority and the Registry of Friendly Societies following publication.

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

This announcement will also be available on the Nationwide Building Society website, www.nationwide.co.uk, from 27 May 2009.

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