28 March 2019

ARBUTHNOT BANKING GROUP (“Arbuthnot”, “the Group” or “ABG”)
Audited Final Results for the year to 31 December 2018

Diversification as new businesses commence

Arbuthnot Banking Group today announces an increase in profit before tax of 172%.

Arbuthnot Banking Group PLC is the holding company for Arbuthnot Latham & Co., Limited and has a 15.5% shareholding in Secure Trust Bank PLC.

FINANCIAL HIGHLIGHTS
- Profit Before Tax £6.8m (2017: £2.5m)
- Underlying profit before tax £7.4m (2017: £3.2m)
- Operating income increased by 24% to £67.9m (2017: £54.6m)
- Negative earnings per share 134.5p (2017: positive 43.9p)*
- Continuing earnings per share 38.0p (2017: 14.0p)
- Underlying earnings per share 40.3p (2017: 17.6p)
- Final dividend per share 20p (2017: 19p), an increase of 5%
- Total full year dividend per share 35p (2017: 33p)
- Bonus share issue to create new class of non-voting shares
- Net assets £196m (2017: £236m)
- Net assets per share 1283p (2017: 1547p)
- Underlying return on deployed equity 5.6% (2017: 4.2%)

OPERATIONAL HIGHLIGHTS

Arbuthnot Latham
- Profit before tax £14.6m (2017: £11m) an increase of 33%**
- Average net margin at 4.7% (2017: 4.5%)
- Customer loans increased 17% to £1,225m (2017: £1,049m)
- Written loan volume increased 1% to £469m (2017: £466m)
- Customer deposits increased 23% to £1,714m (2017: £1,391m)
- Assets under management decreased 6% to £985m (2017: £1,044m)
- Arbuthnot Asset Based Lending launched in May 2018 issuing facilities of £43m
- Arbuthnot Specialist Finance developed with first loan approved in 2019
- Arbuthnot Direct established to provide deposit products direct to the retail market

Secure Trust Bank – Investment
- Shareholding now at 15.5% (2017: 18.6%)
- De-recognised as an associated undertaking due to loss of significant influence
- Net loss following de-recognition £25.7m

Commenting on the results, Sir Henry Angest, Chairman and Chief Executive of Arbuthnot, said: “The Group has had another good year with further deployment of capital. Diversity of earnings increased with good progress being made by the Commercial Bank, along with the launch of our new ventures, Asset Based Lending, Arbuthnot Direct and Specialist Finance. These new businesses should give the Group a strong basis from which to develop in the future.”

Note: * Results include £25.7m net loss on derecognition of STB associate recorded in discontinued operations.
** Includes an adjustment to RAF earn out liability giving a one off profit of £2.6m.

ENQUIRIES:

Arbuthnot Banking Group Sir Henry Angest, Chairman and Chief Executive Andrew Salmon, Chief Operating Officer James Cobb, Group Finance Director	0207 012 2400
Stifel Nicolaus Europe Ltd trading as KBW (Nomad and Joint Broker) Robin Mann Gareth Hunt Stewart Wallace	0207 710 7600
Numis Securities Ltd (Joint Broker) Stephen Westgate	0207 260 1000
Maitland (Financial PR) Neil Bennett Jais Mehaji Sam Cartwright	0207 379 5151

The 2018 Annual Report and Notice of Meeting will be posted and available on the Arbuthnot Banking Group website http://www.arbuthnotgroup.com on or before 12 April 2019. Copies may be obtained from the Company Secretary, Arbuthnot Banking Group PLC, Arbuthnot House, 7 Wilson Street, London, EC2M 2SN.

Consolidated statement of comprehensive income

	Note	Year ended 31 December 2018 £000	2017 £000
Interest income	8	65,290	47,427
Interest expense		(10,107)	(6,334)
Net interest income		**55,183**	**41,093**
Fee and commission income	9	12,956	13,805
Fee and commission expense		(234)	(282)
Net fee and commission income		**12,722**	**13,523**
Operating income		**67,905**	**54,616**
Net impairment loss on financial assets	10	(2,731)	(394)
Other income	11	6,588	3,033
Operating expenses	12	(64,982)	(54,721)
Profit before tax from continuing operations		**6,780**	**2,534**
Income tax expense	13	(1,121)	(448)
Profit after tax from continuing operations		5,659	2,086
Profit from discontinued operations after tax	14	(25,692)	4,437
(Loss) / profit for the year		**(20,033)**	**6,523**
Other comprehensive income			
Items that are or may be reclassified to profit or loss			
Available-for-sale reserve		-	128
Available-for-sale reserve - Associate		-	389
Tax on other comprehensive income		-	(104)
Items that will not be reclassified to profit or loss			
Changes in fair value of equity investments at fair value through other comprehensive income		(13,893)	-
Tax on other comprehensive income		(26)	-
Other comprehensive (loss) / income for the period, net of tax		**(13,919)**	**413**
Total comprehensive (loss) / income for the period		**(33,952)**	**6,936**
Profit attributable to:			
Equity holders of the Company		(20,033)	6,523
(Loss) / profit for the year		**(20,033)**	**6,523**
Total comprehensive income attributable to:			
Equity holders of the Company		(33,952)	6,936
Total comprehensive (loss) / income for the period		**(33,952)**	**6,936**
Earnings per share for profit attributable to the equity holders of the Company during the year (expressed in pence per share):			
Basic earnings per share - Continuing operations	16	38.0	14.0
Basic earnings per share - Discontinued operations	16	(172.5)	29.9
Basic earnings per share	16	**(134.5)**	**43.9**
Diluted earnings per share - Continuing operations	16	38.0	14.0
Diluted earnings per share - Discontinued operations	16	(172.5)	29.9
Diluted earnings per share	16	**(134.5)**	**43.9**

Consolidated statement of financial position

	Note	At 31 December 2018 £000	2017 £000
ASSETS			
Cash and balances at central banks	17	405,325	313,101
Loans and advances to banks	18	54,173	70,679
Debt securities at amortised cost / held-to-maturity	19	342,691	227,019
Assets classified as held for sale	20	8,002	2,915
Derivative financial instruments	21	1,846	2,551
Loans and advances to customers	22	1,224,656	1,049,269
Other assets	24	12,716	20,624
Financial investments	25	35,351	2,347
Deferred tax asset	26	1,490	1,527
Interests in associates	27	-	83,804
Intangible assets	28	16,538	15,995
Property, plant and equipment	30	5,304	3,962
Investment property	31	67,081	59,439
Total assets		**2,175,173**	**1,853,232**
EQUITY AND LIABILITIES			
Equity attributable to owners of the parent			
Share capital	37	153	153
Retained earnings	38	209,083	237,171
Other reserves	38	(13,280)	(949)
Total equity		**195,956**	**236,375**
LIABILITIES			
Deposits from banks	32	232,675	195,097
Derivative financial instruments	21	188	931
Deposits from customers	33	1,714,286	1,390,781
Current tax liability		236	705
Other liabilities	34	18,549	16,239
Debt securities in issue	35	13,283	13,104
Total liabilities		**1,979,217**	**1,616,857**
Total equity and liabilities		**2,175,173**	**1,853,232**

Chairman's statement

I am pleased to report that Arbuthnot Banking Group ("ABG" or "the Group") has achieved a profit before tax for 2018 of £6.8m (2017: £2.5m). It reflects our continued deployment of capital and investment in our principal banking subsidiary, Arbuthnot Latham and Co., Limited ("AL" or the "Bank"). To that end, to allow us to focus solely on managing this investment, Andrew Salmon and I resigned from the Board of Secure Trust Bank PLC in August 2018. While this was the right decision for the Group, it did result in us falling foul of the accounting rules once again. The fact that we no longer had significant influence in our associated company, meant we were required to classify our shareholding as a financial investment and recognise the resultant mark to market loss. This we have shown as discontinued operations. I always felt it was inappropriate that we were required to recognise this unrealised gain in 2016 and now feel justified as we write off a previous profit that we never should have been required to take.

As I reflect on the progress that the Group has made, I am encouraged that our strategy of diversification is gathering momentum. It must be noted that two significant market events took place in 2018. Firstly, the large systemic UK banks concluded their ring fencing process and secondly, the final requirement of the phasing in of the capital buffers was completed. Thus, almost ten years since the worst of the financial crisis, the largest banks are able to focus on growth strategies rather than internal projects or capital raising. It is not clear how they will build out their business, but already we have seen an increase in liquidity in the mortgage sector, as the ring fenced banks work to deploy this "trapped funding". However, we remain steadfast in our philosophy of not chasing lending volumes by lowering our returns or taking excessive credit risk.

I am confident that clients will still want to receive a personalised service and specialist banks will therefore continue to play a significant role in providing bespoke funding, services and advice to a market that can't be mass processed through automated credit models and algorithms. What is clear to me, is that not relying on generating income from a single market sector, will be important. This is why we have focused on diversifying our revenue streams and invested in developing new businesses.

Accordingly, I am pleased to see the progress that our new ventures have made in 2018. Renaissance Asset Finance ("RAF") has grown its lending balances by 21%. Arbuthnot Asset Based Lending ("ABL") commenced trading in May 2018 ahead of plan and has already issued facilities to the value of £43m and has drawn balances of £25m. This business has also carried its momentum into the new year. In January ABL issued a further £29m of facilities, being an increase of more than 50% on the December balance.

The Specialist Finance team joined us in August 2018 and began setting up the infrastructure and operations required to commence trading. This is largely completed now and they have begun a soft launch. Their first loan received Credit Committee approval in February 2019.

Given our philosophy of caution when it comes to funding our lending, I have taken a keen interest in the development of our new Arbuthnot Direct deposit platform. This enables us to provide deposit products directly to the retail market via our newly created internet platform, with rates advertised on the best buy tables. Although we do not need to raise deposits via this channel, it is good to have it available, should an attractive opportunity arise, and it is helpful in raising funds of longer duration.

Finally, I am satisfied with the progress that our core business has made. The Private Bank has struggled to maintain its momentum, but I hope by refocussing its strategies to concentrate on sourcing and nurturing new relationships with criteria clients, this should bring good future growth. The Commercial Bank has continued to build out both sides of the balance sheet, increasing its loan balances by 46%, while at the same time remaining self-funding, increasing deposits by £258m.

RBS Remedies Application

As we have previously announced, the Commercial Bank plans to take part in the RBS remedies process. We have already been selected as one of 11 banks accepted into the Incentivised Switching Scheme ("ISS"), where RBS customers are incentivised to join another bank. Additionally, AL will be submitting its application for a grant from the Capabilities and Innovation Fund. We are confident that as a well-established bank with a 186 year history of serving our clients, with high quality products and a tailored relationship-led service, we are a strong candidate for the grant we are seeking.

We have a proven track record of building successful businesses which meet customer needs in the sectors in which they operate. Our Commercial Bank launched in 2016 and already has customer loan balances of £443m at the year end. Success with our application for a grant from the Capability and Innovation Fund would enable us to bring our differentiated, private banking style relationship banking offer to a wider range of sectors than we are currently able to service, and to offer a more complete banking service to our clients across the country.

We are also delighted to be working closely with Oracle as part of the application process, as we recognise that to service our clients to the highest standards, complementary digital solutions are a prerequisite if we are to provide real competition to this under-served market. We have forged a strong and efficient working partnership with Oracle, who are the providers of our core banking technology. They have been helpful in identifying innovations in the global Commercial Banking industry and plan to deliver them to the UK Market via our bid.

If we are successful in this bid process, we will bring forward our plans for further developing our Commercial Banking platform, with the grant money accelerating our transformation of the Bank.

Non-voting Shares

In 2016 we asked shareholders to approve, at the AGM, a number of resolutions to enable us to start the process of creating and issuing a new class of shares in Arbuthnot Banking Group. These new shares will rank pari passu with the existing ordinary shares in every way, including their right to receive the same dividends as ordinary shares, except they will not have the right to vote in shareholder meetings. As a Board and Company we believe that the current control structure, has enabled the business to take long term investment decisions and sometimes develop contrarian strategies, like ceasing to lend in the height of the financial boom of the mid 2000s. This strategy paid off when we were able to take full advantage of the opportunities that came our way following the financial crisis, in particular, being able to buy Everyday Loans for £1 in 2012 and then selling it for a profit of £117m in 2016.

These new non-voting shares will enable us to maintain the control structure, but will provide us with the means to raise further capital, to continue to develop the business and to fund suitable inorganic deals should the opportunities arise. Thus, I am delighted to announce that we will establish these new shares following the AGM in May. To allow all of our shareholders to benefit from the new class of shares, we intend to offer them to existing shareholders by way of a bonus share issue of one new non-voting share for every 100 ordinary shares held.

Since this is an exploratory exercise, your Board is keen to keep central expenses to a minimum and therefore these new shares will be listed on the NEX Growth Market following the issue and at the same time the ordinary shares will be dual listed on the NEX exchange and also AIM. The NEX Exchange is a fully regulated Recognised Investment Exchange for shares in growth companies and its costs are significantly lower than either the main market of the London Stock Exchange or AIM. Further details are set out in the circular to shareholders enclosed with the Annual Report.

Board Changes and Personnel

Ian Henderson departed from the Board on 31 August and I would like to thank him for the valuable contributions he has made to AL. Jeremy Kaye our Company Secretary, decided to retire after having given 46 years of dedicated service to Arbuthnot. He was succeeded by Nick Jennings. We will miss his attention to detail that only a classical education can develop. I wish him well for a long and happy retirement. Furthermore on 8 August Paul Lynam left the Board. I thank him for the significant contribution he made in developing both Secure Trust Bank and Arbuthnot Banking Group.

Most importantly, I should mention that as part of our continued integration of the Group and the Bank, I was pleased to be able to appoint Andrew Salmon as CEO of Arbuthnot Latham in June 2018. Andrew has worked with me in various capacities for over 20 years. He will retain his Group responsibilities. He is supported by two deputies, James Cobb, our Group Finance Director and Stephen Fletcher, previously the Head of our Commercial Bank.

Finally, the performance of the Group also reflects the hard work and commitment of all the members of staff. On behalf of the Board I extend our thanks to all of them for their dedicated efforts in 2018.

Dividend

The Board is proposing a final dividend of 20p, an increase of 1p on last year. Together with the interim dividend of 15p it gives a total dividend of 35p (2017: 33p), which represents an increase of 2p on the ordinary dividend.

If approved, the dividend will be paid and the bonus share issue will be made on 17 May 2019 to shareholders on the register at close of business on 26 April 2019.

Outlook

The macro economic outlook has grown increasingly uncertain. Major economies have seen industrial output slow, with Germany narrowly avoiding a technical recession. At the same time trade conflicts may develop further and the impact of Brexit has yet to be reflected fully in the UK economy.

However, given our cautious approach to banking, I feel confident that our balance sheet should withstand any likely downturn in the economy. I am also optimistic that our new ventures can continue to make good progress and establish themselves as significant contributors to the future success of Arbuthnot Banking Group PLC.

Looking further ahead, the UK economy might surprise us. It has proved to be very resilient, despite all the doom and gloom, and with a strong government introducing the right economic policies to promote business, Brexit could well deliver a bright future.

Strategic Report

Business Review

Arbuthnot Latham & Co., Ltd

	2018	2017
Operating income	£68.4m	£54.9m
Other income	£6.8m	£3.9m
Operating expenses	£57.8m	£47.4m
Profit before tax (before Group recharges)	£14.6m	£11.0m
Customer loans	£1,224.7m	£1,049.3m
Customer deposits	£1,714.3m	£1,390.8m
Total assets	£2,172.5m	£1,783.7m
Assets under management	£985.1m	£1,044.3m
Average net margin	4.7%	4.5%
Loan to deposit ratio	71.4%	75.4%

Arbuthnot Latham & Co., Limited has reported a profit before tax of £14.6m (2017: £11m), which is an increase of 33%. However, the underlying profit increased by 25%, when the impact of the one off adjustment to the management earn out liability for Renaissance Asset Finance and the investment made in our new business ventures are excluded.

At the time when the acquisition of RAF was completed, the future liability for the management earn out was estimated to be the maximum permitted under the sale and purchase agreement. This liability has now been reassessed and £2.6m taken back to profit. However, RAF continues to perform well and has increased its customer loan balances by 21% in 2018, even though this is below the level the management team had anticipated at the time of agreeing the earn out contract.

Overall the Bank's leading indicators, namely customer balances, showed good growth during the year. Customer loan balances increased by 17% and deposits grew by 23%. Assets under management declined by 6%, largely as a result of the market volatility experienced in the final quarter of the year, as the global markets declined by in excess of 10%.

The other important item in the profit of the Bank is the investment made in the new business ventures. This totalled £1.6m in the year and mainly represents the set up costs incurred by ABL and the Arbuthnot Specialist Finance ("ASF") business. The ABL team commenced in January 2018 and made good progress in establishing its operational processes. As a result of this and also of growing customer demand, the business was able to start writing business in May, two months earlier than planned. At the end of the year the business had issued customer facilities of £43m and had drawn balances of £25m. This business will continue to be a drag on earnings of the bank in 2019, but is expected to break even toward the end of 2019.

ASF was established in August 2018 and has grown to be a team of seven. This team has now also set up its operating systems and has entered a soft launch in 2019, with its first customer loan being approved by Credit Committee in February 2019. It will remain in build out phase during 2019 and expects to break even in 2020.

Credit losses in the year increased to £2.7m (2017: £0.4m), which equates to 22 basis points of the year end customer loan balances. This loss rate remains within our accepted range. However, the increase in reported losses is due to several underlying factors. Firstly, the increased size of the loan book will lead to increased credit losses, even if the loss rate remains constant. Secondly, the introduction of IFRS9 has played a significant role in the higher impairments. The standard requires losses to be attributed to loans at the time of origination as a 12 month Expected Credit Loss ("ECL") in stage one, so a growing front book requires higher provision balances. Also, the definition of when loans are considered to be in default is clearly identified, where previously some element of judgement was exercised. It is therefore expected that, in some of the stage three lending cases where provisions have been required, we will recover a large proportion of the amount outstanding.

Private Banking (including Dubai)

The Private Bank customer loan balances reduced by 1% as the competitive forces within the prime lending market increased during the year. It is clear that the ring fenced banks have been active in the mortgage markets as lending metrics have taken on an all too familiar picture, namely, lowering margins and increasing loan to value ratios. As a result, the Private Bank has refused to be drawn into this competition. Instead, we prefer to extend loans that we believe meet our return criteria, with volumes of loans being the resultant output rather than an input requirement. This can be seen from the loan origination volumes of the Private Bank which fell by 9% during 2018.

Throughout 2018 customer deposits in the Private Bank increased by 9% to close the year at £1,041m (2017: £955m). The Investment Management business started the year with funds under management of £1,044m and closed at £985m. The significant movements in this business saw £90m of gross inflows of new money, which was largely offset by transfers out. The market turbulence of the final quarter saw the funds being marked down by £79m, offsetting the gains made in the early part of the year to leave the net performance a fall of £25m.

During the year the management structure in the Private Bank was reorganised. Given the competition in the lending markets the Private Bank has been realigned to focus on growing the Wealth Management sector of the Bank. This will re-emphasise the need to identify and establish banking relationships with criteria clients. Over time, this should increase the flow of customer balances into deposits, investment management and also provide wealth planning opportunities.

Commercial Bank

The Commercial Bank continued to trade well during the year. Customer loan balances increased by £140m to close the year at £445m, a growth rate of 46%. Additionally, the Commercial Bank remained self-funding and was able to increase its customer deposits by £258m, an increase of 84%, to reach a yearend balance of £567m. However, as noted in the 2017 Annual Report and Accounts, the Commercial Bank has targeted a higher return on its lending performance and has therefore accepted a lower flow of business, which resulted in lower volumes of business being completed. Lending volumes fell by 12% to £190m as compared to 2017, which generated volumes of £217m.

The Commercial Bank has continued to develop its transactional proposition and to that effect has been accepted into the RBS remedies Incentivised Switching Scheme and will be submitting a bid to the Capabilities and Innovation fund for a mid-tier grant. If successful, the Commercial Bank will continue to develop its SME offering while maintaining a personalised service. This along with technology powered by our partner Oracle, should prove to be successful in the SME banking market.

Renaissance Asset Finance

RAF continued to perform well during the year. Customer balances increased by 21% to close the year at £86m and written volumes saw growth of 59% to reach £56m.

The salesforce of the business was reinforced during the year and spent time re-engaging in some of the specialist broker markets. In particular the business wrote deals to finance drainage tankers; these are larger and long term finance deals which should help to extend the term duration of the lending book.

The business also had some success in cross selling its products to the Private Bank network. In particular, the higher value and vintage car finance has proved popular.

New Ventures

During the year the Bank began developing four new lines of business.

Firstly, we launched the Asset Based Lending Business which provides finance secured on either invoices, assets or stock of the borrower. This business is performing ahead of expectations with issued facilities of £43m at the year end and drawn loan balances of £25m. The investment made in this business totalled £0.9m net of revenues earned in the year.

Secondly, the Specialist Finance business, which provides short term secured lending solutions to professional and entrepreneurial property investors commenced in August 2018, and after having set up the business platform has now entered a soft launch phase. The business cost £0.3m during 2018.

Thirdly, the Arbuthnot Direct deposits platform was developed during the year at a cost of £0.2m. This business will enable us to provide deposit products directly to the retail market via a newly created internet platform, with rates advertised on the best buy tables.

Finally, the Arbuthnot Real Estate Fund which was established in 2017, continued its exploratory work of identifying the sector of the investment market that will be the most suitable to receive the marketing of the funds products. Progress has been slow and a decision on the future viability of this fund will be concluded in the first half of 2019. Regardless of the outcome of this review, the ongoing cost of the fund was neutral in 2018.

Strategic Report - Financial Review

Arbuthnot Banking Group adopts a pragmatic approach to risk taking and seeks to maximise long term revenues and returns. Given its relative size, it is nimble and able to remain entrepreneurial and capable to taking advantage of favourable market opportunities when they arise.

The Group provides a range of financial services to clients and customers in its chosen markets of Private and Commercial Banking and Specialist Lending. The Group's revenues are derived from a combination of net interest income from lending, deposit taking and treasury activities, fees for services provided and commission earned on the sale of financial instruments and products. The Group also earns rental income on its investment property and receive dividends from financial investments.

Highlights

Summarised Income Statement	2018 £000	2017 £000
Net interest income	55,183	41,093
Net fee and commission income	12,722	13,523
Operating income	67,905	54,616
Other income	6,588	3,033
Operating expenses	(64,982)	(54,721)
Impairment losses - loans and advances to customers	(2,731)	(394)
Profit before tax from continuing operations	6,780	2,534
Income tax expense	(1,121)	(448)
Profit after tax from continuing operations	5,659	2,086
Profit from discontinued operations after tax	(25,692)	4,437
Profit for the year	**(20,033)**	**6,523**
Basic earnings per share (pence) - Continuing operations	38.0	14.0
Basic earnings per share (pence) - Discontinuing operations	(172.5)	29.9
Basic earnings per share (pence)	**(134.5)**	**43.9**

Underlying profit reconciliation 31 December 2018	Arbuthnot Latham & Co. £000	Group Centre £000	Arbuthnot Banking Group £000
Profit before tax from continuing operations	14,574	(7,794)	6,780
AL cost of establishing new ventures	1,579	-	1,579
STB dividend income full year at current shareholding	1,000	641	1,641
RAF deferred consideration adjustment	(2,584)	-	(2,584)
Underlying profit	**14,569**	**(7,153)**	**7,416**
Underlying basic earnings per share (pence) - Continuing operations			40.3
Underlying basic earnings per share (pence)			**(132.3)**

Underlying profit reconciliation 31 December 2017	Arbuthnot Latham & Co. £000	Group Centre £000	Arbuthnot Banking Group £000
Profit before tax from continuing operations	10,959	(8,425)	2,534
AL investment in operating systems	78	-	78
AL acquisition costs	108	-	108
RAF - full year equivalent income*	466	-	466
Underlying profit	**11,611**	**(8,425)**	**3,186**
Underlying basic earnings per share (pence) - Continuing operations			17.6
Underlying basic earnings per share (pence)			**47.5**

* - RAF profit contribution adjustment as if received from 1 January 2017 and not as currently included from 28 April 2017 (pro forma basis).

The Group has reported a profit before tax on continuing operations of £6.8m (2017: £2.5m). This is an increase on the prior year of 172%. The underlying profit before tax was £7.4m (2017: £3.2m), an increase of 131%.

This reflects the progress being made in the core banking business as the surplus capital held by the Group continues to be deployed. However, once again the reported results contain certain one off items that need explanation.

Firstly, the results contain an adjustment to the predicted future liability for the amount payable to the RAF management team. At the time of the acquisition, we anticipated that the business performance of RAF would be such that the maximum amount payable of £6.5m would be achieved in the earn out period which ends in 2020. While the business continues to perform robustly, increasing its customer loan balances by 21% in the year, this will not be sufficient to attain the levels forecast in the earn out agreement. Accordingly, the liability has been reduced by £2.6m and the corresponding amount recorded as a one off profit in the Income Statement.

Secondly, during the year Sir Henry Angest and Andrew Salmon resigned their positions on the board of Secure Trust Bank PLC ("STB") and the Group has no right to appoint any directors to the STB board in the future. As a result of this the Group was deemed to no longer have significant influence over the associated company and thus the shareholding is now recognised as a financial investment. This required the investment to be marked to market. Given the decline in the share price of STB over the previous years, this assessment resulted in a mark to market loss of £28.7m. The loss was reflected as a discontinued activity, partly offset by the year to date income earned from the associate.

Given this accounting requirement, the dividend paid on this investment in the first half of the year, prior to the change in treatment, was not recorded in the profit and loss account, but will be going forward.

Finally, the Group continued its policy of diversification and further developed new businesses that have now started trading. The investment in Asset Based Lending, Specialist Finance and Arbuthnot Direct lowered the reported profits by £1.6m as the start-up costs of new staff and operating systems was absorbed by the profit of the Group. These businesses should move toward a breakeven point in 2019 or early 2020 and then reach profitability in 2021.

The Group has negative total Basic Earnings per share ("EPS") of 134.5p (2017: positive 43.9p), including the mark to market loss arising on the de-recognition of the associated company. Adjusting for this, the continuing EPS is 38.0p (2017: 14.0p), an increase of 171% or on an underlying basis the continuing EPS is 40.3p (2017: 17.6p), an increase of 129%.

Total operating income earned by the Group increased by 26%, largely due to the increased levels of customer loan balances as the capital deployment continued. The net margin of this lending was 4.7% (2017: 4.5%) as declines in the core bank margins 4.1% (2017: 4.4%) were offset by the higher margins earned by the new lending businesses, which has become proportionally more significant to the overall results. Fees and commissions declined due to the lower levels of Assets Under Management resulting from the global market volatility, particularly in the second half of 2018. Also wealth planning advisory fees were lower as the wealth management proposition was realigned.

The Group's expense base increased by 20% as the cost of the new businesses were absorbed along with natural inflationary increases and further growth in the core banking proposition. The net increase in growth of income and expenses resulted in positive operating leverage or "Jaws" of 6%.

Impairment losses increased to £2.7m (2017: £0.4m), with the previous loss rate of 4 basis points increasing to 22 basis points. The increase in the loss rate was largely as a result of the introduction of the IFRS9 accounting standard during the year. This has three changes, which will affect the results on an ongoing basis.

Firstly, the growth of the front book (Stage 1) requires provisions to be made on newly originated loans regardless of their performance, hence a growing loan book will require higher provisions.

Secondly, the standard requires future economic scenarios to be modelled and the result of these "stress tests" need to be factored into the resultant provisions.

Finally, the old accounting rules allowed for loans to be deemed "non accrual" whereby interest ceased to be accounted for on underperforming loans. Now we are required to gross up the accounting by continuing to record interest on these loans and at the same time increasing the offsetting provisions. This will result in higher impairment losses but no overall change to net income.

Overall the return on equity on a continuing basis for the Group was 3.0% (2017: 1.1%), which continues to be distorted by the surplus capital. This return when calculated on the capital required is 5.6 (2017: 4.2%).

This remains below target levels as the Group continues to develop operational scale. However, given the final increase in the capital conservation buffer on 1 January 2019, the total capital requirements (including the countercyclical buffer) now stand at levels 44% higher than 3 years ago. Thus, the ROE percentage target is now accordingly lower in the mid-teen range.

Balance Sheet Strength

Summarised Balance Sheet	2018 £000	2017 £000
Assets		
Loans and advances to customers	1,224,656	1,049,269
Liquid assets	802,189	610,799
Other assets	148,328	193,164
Total assets	**2,175,173**	**1,853,232**
Liabilities		
Customer deposits	1,714,286	1,390,781
Other liabilities	264,931	226,076
Total liabilities	1,979,217	1,616,857
Equity	195,956	236,375
Total equity and liabilities	**2,175,173**	**1,853,232**

During the year total assets increased to £2.2bn (2017: £1.9bn), which was as a result of our ongoing growth of customer loan balances, while at the same time maintaining our conservative funding policy of relying only on retail deposits and targeting a loan to deposit ratio of between 65-75%. Included in other assets are the Groups investment properties which total £67m and are held at fair value. The most significant of these properties is 20 King Street which is valued at £53.3m. The valuation methodology is based on a discounted cash flow model, with the most important inputs being expected rentals for prime west end office space and yield values for similar properties. These inputs were reviewed and verified by leading surveyors. The methodology has used 4% as the yield, which is in the range of observed yields of 3.75% to 4.15%. The yield gave the property value of £53.9m which was in fact £0.6m higher than the previous fair value of £53.3m. Given the subjective nature of the model, we have taken the conservative view that the valuation should remain unchanged. Further analysis of the methodologies and sensitivities that the inputs may have on the valuation can be found in Note 4 of the Report and Accounts.

Thus net assets of the Group now stand at £12.83 per share (2017: £15.47). The decrease is attributable to the accounting adjustments made to derecognise the associated company during the year.

Segmental Analysis

The segmental analysis is shown in more detail in Note 44. The Group is organised into six operating segments as disclosed below:

1) Private Banking – Provides traditional private banking services as well as offering financial planning and investment management services. This segment includes Dubai and the Tay mortgage portfolio.
2) Commercial Banking – Provides bespoke commercial banking services and tailored secured lending against property investments and other assets.
3) RAF – Specialist asset finance lender mainly in high value cars but also business assets.
4) All Other Divisions – All other smaller divisions and central costs in Arbuthnot Latham & Co., Ltd (Arbuthnot Commercial Asset-Based Lending, Arbuthnot Direct, Arbuthnot Specialist Finance, Investment properties and Central unallocated items)
5) Group Centre – ABG Group Centre management.

The analysis presented below, and in the business review, is before any consolidation adjustments to reverse the impact of the intergroup operating activities and also intergroup recharges and is a fair reflection of the way the Directors manage the Group.

Private Banking

Summarised Income Statement	2018 £000	2017 £000
Net interest income	33,763	31,528
Net fee and commission income	11,494	12,977
Operating income	45,257	44,505
Other income	2	-
Operating expenses - direct costs	(15,601)	(14,420)
Operating expenses - indirect costs	(21,891)	(21,848)
Impairment losses - loans and advances to customers	(1,966)	(308)
Profit before tax	**5,801**	**7,929**

Private Banking reported a profit before tax of £5.8m (2017: £7.9m). This is a decrease of £2.1m or 27%. This decrease is largely attributable to increased credit provisions, which rose by £1.7m, partially due to the introduction of IFRS 9.

Operating Income increased by 2% as increased competition in the prime loan markets caused margin compression. Also, volatility in the global markets resulted in reduced fee income from the wealth management division. Direct costs rose by nearly 10%, while allocated indirect costs were largely unchanged. The average customer yield was 4.9% (2017: 5.2%).

The customer loan balances of the Private Bank reduced by £7m or 1% during the year, as the competitive forces in the markets left the bank unwilling to give up returns on lending and thus not chase loan volumes at any price.

The deposits increased to £1,041m (2017: £955m). The average loan to value of the private banking loans was 52% (2017: 53%).

Commercial Banking

Summarised Income Statement	2018 £000	2017 £000
Net interest income	16,384	6,720
Net fee and commission income	914	471
Operating income	17,298	7,191
Operating expenses - direct costs	(5,636)	(4,584)
Operating expenses - indirect costs	(8,898)	(4,670)
Impairment losses - loans and advances to customers	(278)	-
Profit / (loss) before tax	**2,486**	**(2,063)**

The Commercial Bank generated a profit before tax of £2.5m (2017: loss of £2.1m), an increase of £4.5m. This is due to the increase in operating income as the business benefited from a full year of income from loans that were mainly generated in the second half of 2017.

The increase in income was partially offset by a higher level of allocated or indirect costs. This is a result of the increased significance of the business, but also a higher level of central costs to oversee and control the division. The average customer loan yield was 4.0% (2017: 3.2%).

The customer loan book closed at £445m (2017: £305m), an increase of 46% with deposits increasing by 84% to £567m.

The average loan to value of the Commercial Bank loan portfolio was 50% (2017: 63%).

RAF

Summarised Income Statement	2018 £000	2017 £000
Net interest income	5,344	3,154
Net fee and commission income	137	75
Operating income	5,481	3,229
Other income	73	-
Operating expenses - direct costs	(3,169)	(1,690)
Impairment losses - loans and advances	(437)	(86)
Profit before tax	**1,948**	**1,453**

Renaissance Asset Finance recorded a profit before tax of £1.9m (2017: £1.5m). This represents an increase of £0.5m or 34%.

The purchase of RAF was completed on 28 April 2017. The 2018 results therefore include a full year for both operating income and direct costs. The annualised 2017 numbers result in the comparatives being in line. An increase in customer loans were offset by a fall in customer yields, which on average for 2018 were 9.6% compared to 9.9% in 2017.

The customer loan balances increased by 21% to close the year at £86m (£71m).

Other Divisions

Summarised Income Statement	2018 £000	2017 £000
Net interest income	163	-
Net fee and commission income	177	-
Operating income	340	-
Other income	6,683	3,870
Operating expenses - direct costs	(2,634)	(230)
Impairment losses - loans and advances to customers	(50)	-
Profit before tax	**4,339**	**3,640**

The aggregated profit before tax of other divisions was £4.3m (2017: £3.6m).

Reported within the other divisions were Investment Properties £1.8m (2017: £1.9m), New Ventures cost of £1.6m (2017: £nil) and central items, which this year contains the £2.6m adjustment to the RAF management earn out liability and rental income earned on space in our Wilson Street offices.

Group Centre

Summarised Income Statement	2018 £000	2017 £000
Net interest income	(105)	51
Subordinated loan stock interest	(366)	(360)
Operating income	(471)	(309)
Other income	760	160
Operating expenses	(8,083)	(8,276)
Profit after tax	**(7,794)**	**(8,425)**

The Group costs reduced to £7.8m (2017: £8.4m) mainly due to £0.7m receipt of the interim dividend paid by STB in September.

IFRS 9

The provisions of IFRS 9 – Financial Instruments have been applied by the Group for the year ended 31 December 2018.

As a result of the implementation of IFRS 9, accounting for credit losses has fundamentally changed, moving from an “incurred” to an “expected” basis. This has required the development of credit loss models, which are used to estimate credit impairments by taking into account the composition of individual loan portfolios and the macro economic outlook at each reporting date. Also, the future economic environment has been “stressed” in varying scenarios to ensure the provisions are appropriate.

The introduction of IFRS 9 has resulted in an initial increase in impairment provisions and may increase volatility in the Group’s Income Statement in the future (see Note 2(f)).

Under new capital regulations, the impact of IFRS 9 on regulatory capital is being phased in over a period of five years. The Group has a strong capital position and the fully loaded impact of IFRS 9 is not considered significant.

Capital

The Group’s capital management policy is focused on optimising shareholder value over the long term. There is a clear focus on delivering organic growth and ensuring capital resources are sufficient to support planned levels of growth. The Board regularly reviews the capital position.

The Group's lead regulator, the Prudential Regulation Authority ("PRA"), sets and monitors capital requirements for the Group as a whole and for the individual banking operations. The lead regulator adopted the Basel III capital requirements with effect from 1 January 2014. As a result, the Group's regulatory capital requirements have been based on Basel III since 2014.

In accordance with the EU's Capital Requirements Directive ("CRD") and the required parameters set out in the PRA Handbook, the Individual Capital Adequacy Assessment Process ("ICAAP") is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. However, as a minimum, the ICAAP is updated annually as part of the business planning process. The ICAAP is a process that brings together the management framework (i.e. the policies, procedures, strategies, and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management. The Group's regulated entity is also the principal trading subsidiary as detailed in Note 43.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted a "Pillar I plus" approach to determine the level of capital the Group needs to hold. This method takes the Pillar I capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations deliver a sufficient capital sum adequate to cover management's anticipated risks. Where the Board considers that the Pillar I capital does not reflect the risk, an additional capital add-on in Pillar II is applied, as per the Individual Capital Guidance ("ICG") issued by the PRA.

The Group's regulatory capital is divided into two tiers:

- Tier 1 comprises mainly shareholders' funds and revaluation reserves, after deducting goodwill, other intangible assets and a significant investment in a financial institution (STB). The portion of the investment representing up to 10% of ABG's Tier 1 is added back to capital resources and then risk weighted at 250%, while anything above this 10% is deducted.
- Lower Tier 2 comprises qualifying subordinated loan capital. Lower Tier 2 capital cannot exceed 50% of Tier 1 capital.

The ICAAP includes a summary of the capital required to mitigate the identified risks from the Group's regulated activities and the amount of capital that the Group has available. All regulated trading entities have complied with all of the externally imposed capital requirements to which they are subject.

Capital ratios	2018 £000	2017 £000
Core Tier 1 capital	197,942	236,375
Deductions	(32,658)	(77,761)
Tier 1 capital after deductions	165,284	158,614
Tier 2 capital	13,283	13,104
Total capital	**178,567**	**171,718**
Core Tier 1 capital ratio (Net Core Tier 1 capital/Basel III Total Risk Exposure)	**15.9%**	**17.3%**
Total Capital Ratio (Capital/Basel III Total Risk Exposure)	**17.2%**	**18.8%**

Risks and Uncertainties

The Group regards the monitoring and controlling of risks and uncertainties as a fundamental part of the management process. Consequently, senior management are involved in the development of risk management policies and in monitoring their application. A detailed description of the risk management framework and associated policies is set out in note 6.

The principal risks inherent in the Group's business are strategic, credit, market, liquidity, operational, cyber, conduct, regulatory and macroeconomic.

Strategic risk

Strategic risk is the risk that may affect the Group's ability to achieve its corporate and strategic objectives. This risk is important to the Group as it continues its growth strategy. However, the Group seeks to mitigate strategic risk by focusing on a sustainable business model which is aligned to the Group's business strategy. Also, the Board of Directors meets once a year to hold a two day board meeting to ensure that the Group's strategy is appropriate for the market and economy.

Credit risk

Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. This risk exists in Arbuthnot Latham, which currently has a loan book of £1,225m. The lending portfolio in AL is extended to clients, the majority of which is secured against cash, property or other assets. Credit risk is managed through the Credit Committee of AL.

Market risk

Market risk arises in relation to movements in interest rates, currencies and equity markets. The Group's treasury function operates mainly to provide a service to clients and does not take significant unmatched positions in any market for its own account. As a result,

the Group's exposure to adverse movements in interest rates and currencies is limited to interest earnings on its free cash and interest rate re-pricing mismatches. The Group actively monitors its exposure to future interest rate rises.

The Group is exposed to changes in the market value of properties. The current carrying value of Investment Property is £67.1m. Any changes in the market value of the property will be accounted for in the Income Statement and as a result could have a significant impact on the profit or loss of the Group.

The Group has a 15.5% interest in STB. This is currently recorded in the Group's balance sheet as a Financial Investment. The carrying value is adjusted to market value at each balance sheet date, according to the share price of STB. Any gains or losses that arise are recorded in Other Comprehensive Income.

Liquidity risk
Liquidity risk is the risk that the Group cannot meet its obligations as they fall due. The Group takes a conservative approach to managing its liquidity profile. Retail client deposits and drawings from the Bank of England Term Funding Scheme fund the Group. The loan to deposit ratio is maintained at a prudent level, and consequently the Group maintains a high level of liquidity. The AL Board annually approves the Individual Liquidity Adequacy Assessment Process ("ILAAP"). The Directors model various stress scenarios and assess the resultant cash flows in order to evaluate the Group's potential liquidity requirements. The Directors firmly believe that sufficient liquid assets are held to enable the Group to meet its liabilities in a stressed environment.

Operational risk
Operational risk is the risk that the Group may be exposed to financial losses from conducting its business. The Group is exposed to operational risks from its Information Technology and Operations platforms. There are additional internal controls in these processes that are designed to protect the Group from these risks. The Group's overall approach to managing internal control and financial reporting is described in the Corporate Governance section of the Annual Report.

Cyber risk
Cyber risk is an increasing risk that the Group is subject to within its operational processes. This is the risk that the Group is subject to some form of disruption arising from an interruption to its IT and data infrastructure. The Group regularly test the infrastructure to ensure that it remains robust to a range of threats, and has continuity of business plans in place including a disaster recovery plan.

Conduct risk
As a financial services provider we face conduct risk, including selling products to customers which do not meet their needs, failing to deal with customers' complaints effectively, not meeting customers' expectations, and exhibiting behaviours which do not meet market or regulatory standards.

The Group adopts a zero risk appetite for any unfair customer outcomes. It maintains clear compliance guidelines and provides ongoing training to all staff. Periodic spot checks and internal audits are performed to ensure these guidelines are being followed. The Group also has insurance policies in place to provide some cover for any claims that may arise.

Regulatory risk
Regulatory risk is the risk that the Group will have insufficient capital resources to support the business or does not comply with regulatory requirements. The Group adopts a conservative approach to managing its capital. The Board approves an ICAAP annually, which includes the performance of stringent stress tests to ensure that capital resources are adequate over a three year horizon. Capital and liquidity ratios are regularly monitored against the Board's approved risk appetite as part of the risk management framework.

Regulatory change also exists as a risk to the Group's business. Notwithstanding the assessments carried out by the Group to manage the regulatory risk, it is not possible to predict how regulatory and legislative changes may alter and impact the business. Significant and unforeseen regulatory changes may reduce the Group's competitive situation and lower its profitability.

Macroeconomic and competitive environment
The Group is also exposed to indirect risks that may arise from the macroeconomic and competitive environment. The economic environment is relatively stable in the UK. However, the international landscape is increasingly uncertain. The uncertain performance of the economies in the EU and the increasingly protectionist stance being taken by other major economies may have an adverse affect on the UK. In particular, this may cause a further softening of central London property prices, which may spread out further to the South East.

The Group monitors its exposure to future interest rate rises and currently has minimal lending to customers in products that would be directly sensitive to interest rate rises. However, at the current levels of interest rates, the affordability enjoyed by the Group's customers is beneficial.

Brexit

Given the uncertainty that exists over Brexit with the UK due to exit from the EU, the Group has tried to anticipate the risks that it may face if an economic shock arises as a result. It has also examined how business activities may be affected if free provision of services cross borders is prohibited.

The Group's only overseas operation is in Dubai, so the vast majority of the Group's income and expenditure is based in the UK. However, after leaving the EU we may no longer be able to provide financial advisory services to EU citizens in the EU. This amounts to an insignificant value of fees within the Income Statement. We have however made plans to be able to generate uninterrupted EU payments via the SEPA network.

Analysis is ongoing with our card service provides to ensure that data transfers made from the UK to EU and visa versa are compliant with the appropriate Data Protection Rules.

Finally, there are two significant business risks that may arise in an economic shock. Firstly, increased credit risk as borrowers are unable to continue to meet their interest obligations as they fall due. This would be alongside a significant fall in the collateral values of our security held against the loans. The average loan to value of our lending book is 53.9%, so to have any material impact this fall in collateral values would have to be severe and prolonged. In our ICAAP stress test scenarios, we are able to withstand a property value fall of 40% over an 18 month period alongside a doubling of our loss rates.

The second significant asset class that would be at risk in a down turn would be the Investment Properties, in particular 20 King Street. The sensitivity analysis of how a change in yields may affect the property values is shown in note 4. Any potential reduction in confidence in the West End prime office market would manifest itself in a lower valuation.

Board of Directors

Sir Henry Angest

Appointed to the Board in December 1985. Sir Henry is the Chairman and Chief Executive and is also Chairman of Arbuthnot Latham & Co., Limited. He gained extensive national and international experience as an executive of The Dow Chemical Company and Dow Banking Corporation. He was previously Chairman of Secure Trust Bank PLC and a Director until August 2018, Chairman of the Banking Committee of the London Investment Banking Association and a Director of the Institute of Directors. He is a Past Master of the Worshipful Company of International Bankers.

James Cobb FCA

Joined the Board in 1 November 2008 as Group Finance Director. He was also appointed Deputy Chief Executive of Arbuthnot Latham & Co., Limited in May 2018. He was previously Deputy Chief Financial Officer and Controller of Citigroup's Global Consumer Group in Europe, Middle East and Africa and qualified as a Chartered Accountant with Price Waterhouse.

Andrew Salmon FCA

Appointed a Director in March 2004. He joined the Company in 1997 as Head of Business Development and is also Chief Operating Officer and since July 2018 Chief Executive of Arbuthnot Latham & Co., Limited. He was a director of Secure Trust Bank PLC until August 2018. He was previously a director of Hambros Bank Limited and qualified as a Chartered Accountant with KPMG.

Ian Dewar FCA

Appointed a Non-Executive Director in August 2015. He is Chairman of the Audit Committee. He was a Partner for 19 years in the Financial Services Practice of KPMG from which he retired in 2012 after 32 years at the firm. He is a non-executive director of Brewin Dolphin Holdings PLC.

Sir Christopher Meyer

Appointed a Non-Executive Director in October 2007. He had a distinguished diplomatic career, culminating in 1997 as Ambassador to the USA. He was previously Ambassador to Germany, Press Secretary to Prime Minister John Major and from 2003 to 2009 Chairman of the Press Complaints Commission. He is also on the International Advisory Board of British American Business Inc., Distinguished Fellow of the Royal United Services Institute and Honorary Fellow of Peterhouse, Cambridge.

Sir Alan Yarrow FCSI (Hon)

Appointed a Non-Executive Director in June 2016. Sir Alan spent 37 years with Dresdner Kleinwort until 2009, latterly as Group Vice Chairman and Chairman of the UK Bank and then served as Chairman of the Chartered Institute for Securities & Investment until October 2018. He is Chairman of Turquoise Global Holdings Ltd and a director of Institutional Protection Services Ltd. He is also Vice President of the Royal Mencap Society, Independent Partnership Advisor to James Hambro & Partners and an advisor to Zeamo. Sir Alan is an Alderman, Magistrate and HM Lieutenant of the City of London, a member of the Court of the Fishmongers' Company, and Liveryman of several other Livery Companies. He is a member of the Takeover Appeal Board, the Advisory Board of the Commonwealth Investment & Advisory Council. Sir Alan was Lord Mayor of the City of London for the year 2014-15.

Nicholas Jennings FCA

Appointed Group Company Secretary in July 2018. He was previously Company Secretary of Daily Mail and General Trust plc and of Close Brothers Group plc. He is a Chartered Accountant.

Group Directors' Report

The Directors present their report for the year ended 31 December 2018.

Business Activities

The principal activities of the Group are banking and financial services. The business review and information about future developments, key performance indicators and principal risks are contained in the Strategic Report on pages 4 to 17.

Corporate Governance

The Corporate Governance report on pages 19 to 27 contains information about the Group's corporate governance arrangements, including in relation to the Board's decision to apply the UK Corporate Governance Code, published by the Financial Reporting Council ("FRC") in July 2018, in response to a change in the AIM Rules.

Results and Dividends

The results for the year are shown on page 37 of the financial statements. The Directors recommend the payment of a final dividend of 20p (2017: 19p) on the ordinary shares which, together with the interim dividend of 15p paid (2017: 14p) on 28 September 2018, represents total dividends for the year of 35p (2017: 33p). The final dividend, if approved by members at the 2019 Annual General Meeting ("AGM"), will be paid on 17 May 2019 to shareholders on the register at close of business on 26 April 2019.

Directors

The names of the Directors of the Company at the date of this report, together with biographical details, are given on page 18 of this Annual Report. All the Directors listed on those pages were directors of the Company throughout the year. Mr. P. A. Lynam and Mr. I.A. Henderson retired from the Board on 8 August and 31 August 2018 respectively.

Under Article 78 of the Articles of Association, Sir Henry Angest and Sir Christopher Meyer retire at the AGM and, being eligible, offer themselves for re-election. Sir Henry Angest has a service agreement terminable on twelve months' notice. Sir Christopher Meyer, an independent non-executive director, has a letter of appointment terminable on three months' notice.

Company Secretary

On 17 July 2018, Nicholas Jennings was appointed Secretary on the retirement of Jeremy Kaye. He can be contacted at the Company's registered office.

Viability Statement

In accordance with the UK Corporate Governance Code, the Directors confirm that there is a reasonable expectation that the Group will continue to operate and meet its liabilities, as they fall due, for the three-year period up to 31 December 2021. A period of three years has been chosen because it is the period covered by the Group's strategic planning cycle and also incorporated in the ICAAP, which forecasts key capital requirements, expected changes in capital resources and applies stress testing over that period.

The Directors' assessment has been made with reference to:

- the Group's current position and prospects – please see the Financial Review on pages 9 to 17;
- the Group's key principles – please see Corporate Philosophy on page 1; and
- the Group's risk management framework and associated policies, as explained in Note 6.

The Group's strategy and three-year plan are evaluated and approved by the Directors annually. The plan considers the Group's future projections of profitability, cash flows, capital requirements and resources, and other key financial and regulatory ratios over the period. The ICAAP is updated at least annually as part of the business planning process.

Going Concern

After making appropriate enquiries which assessed strategy, profitability, funding, risk management (see Note 6 to the financial statements) and capital resources (see Note 7), the directors are satisfied that the Company and the Group have adequate resources to continue in operation for the foreseeable future. The financial statements are therefore prepared on the going concern basis.

Authority to Purchase Shares

Shareholders will also be asked to approve a Special Resolution renewing the authority of the Directors to make market purchases of shares not exceeding 10% of the issued share capital. The Directors will keep the position under review in order to maximise the Company's resources in the best interests of shareholders.

Financial Risk Management

Details of how the Group manages risk are set out in in the Strategic Report and in Note 6 to the financial statements.

Directors' Interests

The interests of current Directors and their families in the ordinary shares of the Company at the dates shown, together with the percentage of the current issued share capital held, were as follows:

Beneficial Interests	1 January 2018	31 December 2018	26 March 2019	%
Sir Henry Angest	8,200,901	8,351,401	8,351,401	56.1
J.R. Cobb	5,000	6,000	6,000	-
A.A. Salmon	51,699	51,699	51,699	0.3

Substantial Shareholders

The Company was aware at 11 March 2019 of the following substantial holdings in the ordinary shares of the Company, other than those held by one director shown above:

Holder	Ordinary Shares	%
Liontrust Asset Management	961,028	6.5
Miton Asset Management	662,086	4.4
Slater Investments	595,638	4.0
Mr. R Paston	529,130	3.6
M&G Investment Management	527,268	3.5

Significant Contracts

No Director, either during or at the end of the financial year, was materially interested in any contract with the Company or any of its subsidiaries or associated companies, which was significant in relation to the Group's business. At 31 December 2018, one Director had loans from Arbuthnot Latham & Co., Limited amounting to £515,000 and four directors had deposits with Arbuthnot Latham amounting to £1,884,000 all on normal commercial terms as disclosed in Note 42 to the financial statements.

At 1 January 2018, one Director had a loan from Secure Trust Bank PLC, which ceased to be an associated company on 8 August 2018, amounting to £409,000 and two Directors had deposits amounting to £403,000, all on normal commercial terms as disclosed in Note 42 to the financial statements.

Directors' Indemnities

The Company's Articles of Association provide that, subject to the provisions of the Companies Act 2006, the Company may indemnify any Director or former Director against any liability and may purchase and maintain insurance against any liability. The Company maintained directors and officers liability insurance throughout the year.

Employees

The Company gives due consideration to the employment of disabled persons and is an equal opportunities employer. It also regularly provides employees with information on matters of concern to them, consults on decisions likely to affect their interests and encourages their involvement in the performance of the Company through regular communications and in other ways.

Political Donations

The Company made political donations of £6,000 to the Conservative Party during the year (2017: £32,000).

Branches outside of the UK

During the year Arbuthnot Latham operated a branch in Dubai which is regulated by the Dubai Financial Services Authority.

Events after the Balance Sheet Date

There were no material post balance sheet events to report.

Annual General Meeting

The Company's AGM will be held on Thursday 9 May 2019. At the AGM, Shareholders will be asked to vote on a number of resolutions including the creation and bonus issue of a new class of ordinary non-voting shares and the re-appointment of KPMG LLP as the Company's auditor.

Disclosure of Information to the Auditor

Each of the persons who are Directors at the date of approval of this Annual Report confirm that:

- so far as each director is aware, there is no relevant audit information of which the Company's auditor is unaware; and
- they have taken all the steps they ought to have taken as a director to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Statement of Directors' Responsibilities in Respect of the Strategic Report and the Directors' Report and the Financial Statements

The Directors are responsible for preparing the Strategic Report, the Directors' Report and the Financial Statements in accordance with applicable law and regulations. Company law requires the Directors to prepare Group and Parent Company Financial Statements for each financial year. As required by the AIM Rules of the London Stock Exchange they are required to prepare the Group Financial Statements in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the EU and applicable law and have elected to prepare the Parent Company Financial Statements on the same basis.

Financial Statements

Under company law the Directors must not approve the Financial Statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and the Company and of the Group profit or loss for that period. In preparing each of the Group and Parent Company Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- assess the Group and Parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they intend either to liquidate the Group or the Parent Company or to cease operations, or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that its Financial Statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of Financial Statements may differ from legislation in other jurisdictions.

The Directors confirm the Annual Report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Group and Parent Company's position, performance, business model and strategy.

By order of the Board

N D Jennings
Secretary
27 March 2019

Corporate Governance

Introduction and Overview

Arbuthnot Banking Group has a strong and effective corporate governance framework. The Board endorses the principles of openness, integrity and accountability which underlie good governance and takes into account the provisions of the UK Corporate Governance Code in so far as they are considered applicable to and appropriate for it, given its size and circumstances, and the role and overall shareholding of its majority shareholder. Moreover, the Group contains two subsidiaries authorised to undertake regulated business under the Financial Services and Markets Act 2000, one of which (Arbuthnot Latham & Co., Ltd) is regulated by the Prudential Regulatory Authority and the Financial Conduct Authority and is an authorised deposit-taking business. It in turn has a subsidiary, Renaissance Asset Finance Limited, which is regulated by the Financial Conduct Authority. Arbuthnot Latham & Co., Ltd also operates a branch in Dubai, which is regulated by the Dubai Financial Services Authority. Accordingly, the Group operates to the high standards of corporate accountability and regulatory compliance appropriate for such a business.

In March 2018, the AIM Rules were amended to require AIM companies to state which corporate governance code they had decided to apply, how the AIM company complies with that code, and where it departs from its chosen code an explanation of the reasons for doing so. This information was published, as required, on the Company's website by 28 September 2018 and the Company plans to review it each year as part of its annual reporting cycle.

The Board decided to report against the UK Corporate Governance Code, published by the Financial Reporting Council ("FRC") in July 2018 ("the Code") with effect from 28 September 2018. This section of the Annual Report summarises how the Company applies the Code and in broad terms how it has complied with its provisions since that date, giving explanations where it has chosen not to do so.

The Company is led by the Board which, following changes in August 2018, comprises six members: the executive Chairman, two other executive directors, Andrew Salmon and James Cobb, and three independent non-executive directors who thereby constitute half of the Board in line with the Code. The Board sets the long term focus and customer oriented culture of the Group. The responsibilities of Sir Henry Angest as Chairman include leading the Board, ensuring its effectiveness in all aspects of its role, ensuring effective communication with shareholders, setting the Board's agenda and ensuring that all Directors are encouraged to participate fully in the activities and decision-making process of the Board.

In 2016 an independent Board Effectiveness Review was carried out by an external consultant. In October 2018 it was determined to carry out the annual Board Effectiveness Review internally. The evaluation took the form of a confidential questionnaire which assessed the performance of the Board and its Committees. The questions were set to explore the themes developed the previous year, including Board effectiveness, Board composition, Board dynamics, alignment of the Board and executive team, interaction with major shareholders, induction, performance and training, Board Committees and the Secretariat. The feedback was collated by the Company Secretary and discussed by the Board in November 2018. The responses were positive, confirming that the Board was of the view that it receives the correct level of insight into and oversight of the Company, both directly to it and in terms of management information and oral updates provided during meetings. Directors also agreed that the Arbuthnot culture set out in the Arbuthnot Principles and Values manifests itself at Board level and in the external view of the Group as a whole.

The Board

The Board met regularly throughout the year, holding six scheduled meetings as well as a two-day off-site strategy meeting. Substantive agenda items have briefing papers, which are circulated in a timely manner before each meeting. The Board ensures that it is supplied with all the information that it requires and requests in a form and of a quality to fulfil its duties.

In addition to overseeing the management of the Group, the Board has determined certain items which are reserved for decision by itself. These matters include approval of the Group's long-term objectives and commercial strategy, ensuring a sound system of internal control, risk management strategy, approval of major investments, acquisitions and disposals, any changes to capital structure and the overall review of corporate governance.

The Company Secretary is responsible for ensuring that the Board processes and procedures are appropriately followed and support effective decision making. All directors have access to the Company Secretary's advice and services. There is an agreed procedure for directors to obtain independent professional advice in the course of their duties, if necessary, at the Company's expense.

All directors receive induction training upon joining the Board, with individual AIM training provided by the Company's Nominated Adviser, regulatory and compliance training provided by the Group Head of Compliance or an external firm of lawyers, risk management training (including that in relation to the ICAAP and ILAAP) with an overview of credit and its associated risks and mitigation by the Head of Credit Risk in Arbuthnot Latham.

Overview of Compliance with the FRC Code, together with Exceptions

The Board focuses not only on the provisions of the Code but its principles, ensuring as follows:

- The Company's purpose, values and strategy as a prudently managed organisation align with its culture, with a focus on fairness and long-term shareholder returns.
- The Board has an appropriate combination of executive and non-executive directors, who have both requisite knowledge and understanding of the business and the time to commit to their specific roles.
- The Board comprises directors with the necessary combination of skills to ensure the effective discharge of its obligations, with an annual evaluation of the capability and effectiveness of each director as well as the Board as a composite whole; appropriate succession plans are also in place and reviewed annually, or more frequently if appropriate.
- The Board and Audit Committee monitor the procedures in place to ensure the independence and effectiveness of both external and internal auditors, and the risk governance framework of the Company, with all material matters highlighted to the relevant forum (Board/Committee).
- Remuneration policies and practices are designed to support strategy and promote long-term sustainable success, with a Remuneration Committee in place to oversee director and senior management pay.

In respect of the Code's specific provisions, an annual review is carried out, comparing the Company's governance arrangements and practices against them. Any divergences are noted, with relevant rationale considered carefully to determine whether it is appropriate. Consideration is also given to guidance issued, which may require a review of the relevant reasoning intra-year.
In line with the FRC's Guidance on Board Effectiveness, the Board additionally takes into account its suggestions of good practice when applying the Code focusing on the five key principles specified in the Code.

Where the Company's governance does not completely align with Code, it is generally as a result of the role of its overall majority shareholder, itself adding a level of protection to long-term shareholder interests, and it has had no negative impact on the Company.

All divergences from the Code, with an explanation of the reasons for doing so are set out below:

Provision 3 - The majority shareholder is Chairman and Chief Executive of ABG. Engagement with other major shareholders is carried out as appropriate by the Chairman, the Group Chief Operating Officer or the Group Finance Director. There has been no requirement to date to consult with them on matters delegated to Board committees, but if appropriate/when requested, this would be arranged.

Provision 5 – The Board has regard to the interests of all its key stakeholders in its decision making. The Company has fewer than 20 employees, all of whom have direct access to Board members. As such, it has not been deemed necessary to appoint an employee representative to the Board, nor a formal workforce advisory panel, nor a designated non-executive Director.

Provision 9 - Sir Henry Angest carries out the role of Chairman and Chief Executive, given his long-term interest as majority shareholder, itself aligning with the interests of other shareholders. The Group Chief Operating Officer and the Group Finance Director provide a strong, independent counterbalance, ensuring challenge and independence from a business perspective, against the stakeholder focus of the Chairman carrying out his Chairman's role. The Company follows the US model that is very successful in ensuring commercial success with strong corporate governance and stakeholder awareness, having a shared Chairman and CEO, with a separate, empowered, Chief Operating Officer.

Provision 10 ¬ The Board considers Sir Christopher Meyer to be independent, notwithstanding his serving more than nine years, since his views and any challenge to executive management remain firmly independent.

Provision 12 – The Board has not appointed a Senior Independent Director, as major shareholders talk openly with the Chairman, the Group Chief Operating Officer and the Group Finance Director on request.

Provision 14 – Attendance at meetings is not reported as, should a Director be unable to attend a meeting, that Director receives relevant papers in the normal manner and relays any comments in advance of the meeting to the Chairman. The same process applies in respect of the Board Committees.

Provision 18 – For the purposes of stability and continuity, the Company continues to offer Directors for re-election on a three-year rolling basis in accordance with the Company's Articles of Association and company law. The Directors seeking re-election at the AGM are Sir Henry Angest and Sir Christopher Meyer, who have served on the Board for 33 years and 11 years respectively. The contribution of Sir Henry Angest, who beneficially owns more than 50% of the issued share capital, has been invaluable in the successful development of the Company. Sir Christopher Meyer's wide-ranging experience including as a diplomat at the most senior level has provided an important independent measure of challenge to executive management. Accordingly, the Board fully supports the resolutions for their reappointment.

Provision 19 - Sir Henry Angest's role as Chairman has extended over nine years and is expected to continue indefinitely, given his key role as majority shareholder both in protecting the stability of his and other shareholder interests and in overseeing a balanced and risk-managed approach to growing the business with a view to the longer-term.

Provision 32 – Sir Henry Angest is Chairman of the Remuneration Committee, as is appropriate in the context of his majority shareholding.

Internal Control and Financial Reporting

The Board of directors has overall responsibility for the Group's system of internal control and for reviewing its effectiveness. Such a system is designed to manage rather than eliminate risk of failure to achieve business objectives and can only provide reasonable, but not absolute, assurance against the risk of material misstatement or loss.

The Directors and senior management of the Group review and approve the Group's Risk Appetite Statement and Risk Management Policy. Risk appetite sets out the Board's attitude to risk and internal control and includes qualitative and quantitative measures which are reported to every Board meeting; the Risk Management Policy details how risks are monitored and controlled within the Bank. Key business risks and emerging risks are continuously identified, evaluated and managed by means of limits and controls set by and managed at an operational level by AL management and governed through Arbuthnot Latham Committees.

Significant risks identified in connection with the development of new activities are subject to consideration by the Board. There are well-established budgeting procedures in place and reports are presented regularly to the Board detailing the results, in relation to Arbuthnot Latham, of each principal business unit, variances against budget and prior year, and other performance data. The Board receives regular reports on any risk matters that need to be brought to its attention, enabling it to assess the Group's emerging and principal risks.

Shareholder Communications

The Company maintains communications via one to one meetings as appropriate with its major shareholders and makes full use of the AGM to communicate with shareholders. The Company aims to present a balanced and understandable assessment in all its reports to shareholders, its regulators, other stakeholders and the wider public. Key announcements and other information can be found at www.arbuthnotgroup.com.

Board Committees

The Board has established Audit, Nomination, Remuneration and Donations Committees, each with formally delegated duties and responsibilities and with written terms of reference, which require consideration of the committee's effectiveness. The Board keeps the governance arrangements under review. Further information in relation to these committees is set out below. The Board maintains direct responsibility for issues of Risk without the need for its own Risk Committee, since responsibility for large lending proposals is a direct responsibility of its subsidiary, Arbuthnot Latham.

Audit Committee

Membership and meetings

Membership of the Audit Committee is restricted to non-executive Directors and comprises Ian Dewar (as Chairman), Sir Christopher Meyer and Sir Alan Yarrow. The Company Secretary acts as its Secretary. The Committee met four times during the year.

The Audit Committee oversees, on behalf of the Board, financial reporting, the appropriateness and effectiveness of systems and controls, the work of Internal Audit and the arrangements for and effectiveness of the external audit. The ultimate responsibility for reviewing and approving the Annual Report and Accounts and the Interim Report lies with the Board. The Audit Committee also reviews whistleblowing arrangements for employees to raise concerns in confidence.

External Audit

The Senior Statutory Auditor of the external auditors, KPMG LLP, changed in April 2018, following a five-year association with the Company. The Committee assesses the independence and objectivity, qualifications and effectiveness of the external auditors on an annual basis as well as making a recommendation on their reappointment to the Board. The Committee received a report showing the level of non-audit services provided by the external auditors during the year and members were satisfied that the extent and nature of these did not compromise auditor independence. The Committee has concluded that KPMG remain independent and that their audit is effective.

KPMG has held office since August 2009. Consequently, the Committee is required by the EU Audit Regulation 2014 to conduct a competitive audit tender in 2019. The Committee will oversee the tender process and is committed to ensure a fair and transparent process is put in place including a clearly articulated set of selection criteria agreed by the Committee in advance. The tender is not expected to occur before the AGM to be held on 9 May 2019 at which a resolution to re-appoint KPMG LLP as the Company's auditor will be proposed.

Activity in 2018

Internal Audit

On behalf of the Board, the Audit Committee monitors the effectiveness of systems and controls. To this end, Internal Audit provides the Audit Committee and the Board with detailed independent and objective assurance on the effectiveness of governance, risk management and internal controls. Since Arbuthnot Latham established its own Audit Committee, the role of the Group Audit Committee has been mainly supervisory in relation to internal audit matters, though it receives items of material note deriving from Arbuthnot Latham's internal audits, including an assessment of culture which forms part of every internal audit.

The Audit Committee approves the Internal Audit risk based programme of work and monitors progress against the annual plan. The Committee reviews Internal Audit resources and the arrangements that: ensure Internal Audit faces no restrictions or limitations to conducting its work; that it continues to have unrestricted access to all personnel and information; and that Internal Audit remains objective and independent from business management.

The Head of Internal Audit provides reports on the outcomes of Internal Audit work directly to the Committee and the Committee monitors progress against actions identified in these reports.

The Committee received a Self-Assessment report on Internal Audit in September 2018 and it is satisfied with Internal Audit arrangements during 2018.

Integrity of Financial Statements and oversight of external audit

The Committee:

- Received and agreed the Audit Plan prepared by the external auditors;
- Considered and formed a conclusion on the critical judgements underpinning the Financial Statements, as presented in papers prepared by management. In respect of all of these critical judgements, the Committee concluded that the treatment in the Financial Statements was appropriate.
- Received reports from the external auditors on the matters arising from their work, the key issues and conclusions they had reached;
- The Chairman of the Committee attended, as an observer, Audit Committee meetings of Arbuthnot Latham, the Company's operating subsidiary;
- The Committee monitored the changes to financial reporting requirements which came in effect on 1 January 2018, principally IFRS 9;
- In addition, it considered changes to financial reporting requirements that are not yet effective but that are likely to affect the reported results or financial position of the Group and Company in future. The most notable change is IFRS 16, Leases, where the Committee has reviewed Management's methodology, and is satisfied with the disclosures as set out in Note 3.27.

The reports from the external auditors include details of internal control matters that they have identified as part of the annual statutory financial statements audit. Certain aspects of the system of internal control are also subject to regulatory supervision, the results of which are monitored closely by the Committee and the Board. In addition, the Committee receives by exception reports on the ICAAP and ILAAP which are key control documents that receive detailed consideration by the board of Arbuthnot Latham.

The Committee approved the terms of engagement and made a recommendation to the Board on the remuneration to be paid to the external auditors in respect of their audit services.

Significant areas of judgement

The Audit Committee considered the following significant issues and accounting judgements in relation to the Financial Statements:

Impairment of loans and advances to customers

The Committee reviewed presentations from management detailing the provisioning methodology across the Group as part of the full year results process. The Committee considered and challenged the provisioning methodology applied by management, including timing of cash flows, valuation and recoverability of supporting collateral on impaired assets. The Committee concluded that the impairment provisions, including management's judgements, were appropriate.

The charge for impaired loans and advances totalled £2.7m for the year ended 31 December 2018. The disclosures relating to impairment provisions are set out in Note 4.1(a) to the financial statements.

Valuation of Investment Properties

The three investment properties are held at fair value. The Committee reviewed and challenged the key assumptions used in the valuation of the properties including yields, rental income and refurbishment costs.

As at 31 December 2018, the Group's property investment portfolio totalled £67.1m, as detailed in Note 31. The disclosures relating to the fair value of investment properties are set out in Note 4.1(c) to the financial statements.

Effective Interest rate

Interest earned on loans and receivables is recognised using the Effective Interest Rate ("EIR") method. The EIR is calculated on the initial recognition of a loan through a discounted cash flow model that incorporates fees, costs and other premiums or discounts. There have been no changes to the EIR accounting policies during the year.

The Committee considered and challenged the EIR methodology applied by management and specifically in relation to acquired loan portfolios. The Committee considered management assumptions including expected future customer behaviours and concluded that the EIR methodology was appropriate as at 31 December 2018.

The disclosures relating to EIR are set out in Note 4.1(b) to the financial statements.

<u>Going Concern and Viability Statement</u>

The financial statements are prepared on the basis that the Group and Company are each a going concern. The Audit Committee reviewed management's assessment and is satisfied that the going concern basis and assessment of the Group's longer-term viability is appropriate.

<u>Other Committee activities</u>

In November 2018, Committee members contributed to the review of the Committee's effectiveness as part of its evaluation by the Board. The review did not highlight any material concerns.

On behalf of the Board, the Committee reviewed the financial statements as a whole in order to assess whether they were fair, balanced and understandable. The Committee discussed and challenged the balance and fairness of the overall report with the executive directors and also considered the views of the external auditor. The Committee was satisfied that the Annual Report could be regarded as fair, balanced and understandable and proposed that the Board approve the Annual Report in that respect.

In March 2019 the Committee met separately with each of the Head of Internal Audit and the Senior Statutory Auditor without any other executives present. There were no issues or concerns raised by them in regard to discharging their responsibilities.

Nomination Committee

Membership and meetings

The Nomination Committee is chaired by Sir Henry Angest and its other members are Sir Christopher Meyer and Sir Alan Yarrow. The Head of Corporate Governance acts as its Secretary. The Committee met once during the year. It is required to meet formally at least once per year and otherwise as required.

The Nomination Committee assists the Board in discharging its responsibilities relating to the composition of the Board. The Nomination Committee is responsible for and evaluates on a regular basis the balance of skills, experience, independence and knowledge on the Board, its size, structure and composition, retirements and appointments of additional and replacement directors and will make appropriate recommendations to the Board on such matters. The Nomination Committee also considers succession planning, taking into account the skills and expertise that will be needed on and beneficial to the Board in the future.

Activity in 2018

The Committee reviewed policies on Board Diversity, Board Suitability and Board Training and Development. It also assessed and confirmed the collective and individual suitability of Board members. The contribution of Sir Henry Angest remains invaluable in the successful development of the Company. As regards the non-executive Directors' skill sets, Ian Dewar, with a wealth of experience as a partner in a major accounting firm, has successfully chaired the Audit Committee. Sir Christopher Meyer's wide-ranging experience including as a diplomat at the highest level has provided an important independent measure of challenge to executive management. The Board has benefitted from Sir Alan Yarrow's wise counsel, challenge to management and many years' experience in the City of London.

In November 2018, the Committee confirmed that the Board's current composition provides the Company with a balanced, knowledgeable, diverse and informed group of directors, bringing strategic acumen, foresight and challenge to the executive, commensurate with the size of the business. The Committee reviewed succession planning and agreed that there was a sensible and strong plan in place. In terms of any new hires, it noted that account would be taken of provisions in the Board Diversity Policy. The Committee also agreed that it continued to operate effectively and, as such, no changes to its membership, composition or activities were proposed to the Board.

Remuneration Committee

Membership and meetings
Membership is detailed in the Remuneration Report on page 28. The Committee met twice during the year. It is required to meet formally at least once per year and otherwise as required.

The Remuneration Committee assists the Board in determining its responsibilities in relation to remuneration including, inter alia, in relation to the Company's policy on executive remuneration determining, the individual remuneration and benefits package of each of the Executive Directors and the fees for Non-Executive Directors.

The Committee also deals with remuneration-related issues under the Prudential Regulation Authority's Remuneration Code applicable to the Company. The Remuneration Report on pages 28 and 29 gives further information and details of each Director's remuneration.

Donations Committee

Membership and meetings
The Donations Committee is chaired by Sir Henry Angest and its other members are Sir Christopher Meyer and Sir Alan Yarrow. The Committee met once during the year.

The Committee considers any political donation or expenditure as defined within sections 366 and 367 of the Companies Act 2006.

Remuneration Report

Remuneration Committee

Membership of the Remuneration Committee is limited to non-executive directors together with Sir Henry Angest as Chairman. The present members of the Committee are Sir Henry Angest, Sir Christopher Meyer and Sir Alan Yarrow. The Head of Corporate Governance acts as its Secretary. The Committee met twice during the year.

The Committee has responsibility for producing recommendations on the overall remuneration policy for directors for review by the Board and for setting the remuneration of individual directors. Members of the Committee do not vote on their own remuneration.

Remuneration Policy

The Remuneration Committee determines the remuneration of individual directors having regard to the size and nature of the business; the importance of attracting, retaining and motivating management of the appropriate calibre without paying more than is necessary for this purpose; remuneration data for comparable positions, in particular the rising remuneration packages at challenger banks; the need to align the interests of executives with those of shareholders; and an appropriate balance between current remuneration and longer-term performance-related rewards. The remuneration package can comprise a combination of basic annual salary and benefits (including pension), a discretionary annual bonus award related to the Committee's assessment of the contribution made by the executive during the year and longer-term incentives, including executive share options. Pension benefits take the form of annual contributions paid by the Company to individual money purchase schemes. The Remuneration Committee reviews salary levels each year based on the performance of the Group during the preceding financial period. This review does not necessarily lead to increases in salary levels. For the purposes of the FCA Remuneration Code, all the provisions of which have been implemented, the Group and its subsidiaries are all considered to be Tier 3 institutions.

Activity in 2018

The Remuneration Committee undertook its regular activities during the year including reviewing the operation of the Remuneration Policy, having regard to the performance of the Company during the year, with particular regard to the level of discretionary bonus awarded and the level of inflation impacting on salaries.

Directors' Service Contracts

Sir Henry Angest, Mr. Salmon and Mr. Cobb each have service contracts terminable at any time on 12 months' notice in writing by either party.

Long Term Incentive Schemes

Grants were made to three Directors on 14 June 2016 under Phantom Option Scheme introduced on that date, to acquire ordinary 1p shares in the Company at 1591p exercisable in respect of 50% on or after 15 June 2019 and in respect of the remaining 50% on or after 15 June 2021 when a cash payment would be made equal to any increase in market value.

Under this Scheme, Mr. Salmon was granted a phantom option to acquire 200,000 ordinary 1p shares in the Company, which remained outstanding at 31 December 2018. Mr. Cobb was granted a phantom option to acquire 100,000 ordinary 1p shares in the Company, which remained outstanding at 31 December 2018. The phantom option granted to Mr. Henderson to acquire 100,000 ordinary 1p shares in the Company lapsed on 31 August 2018 when he left the Company. The fair value of the remaining options at the grant date was £1m.

Directors' Emoluments

	2018 £000	2017 £000
Fees (including benefits in kind)	205	205
Salary payments (including benefits in kind)	4,387	4,533
Pension contributions	93	105
	4,685	**4,843**

	Salary £000	Bonus £000	Benefits £000	Pension £000	Fees £000	Total 2018 £000	Total 2017 £000
Sir Henry Angest	1,200	-	79	-	-	1,279	1,289
JR Cobb	625	300	17	35	-	977	852
IA Dewar	-	-	-	-	75	75	75
IA Henderson (to 31/08/2018)	333	-	11	23	-	367	840
Sir Christopher Meyer	-	-	-	-	60	60	60
AA Salmon	1,200	600	22	35	-	1,857	1,657
Sir Alan Yarrow	-	-	-	-	70	70	70
	3,358	**900**	**129**	**93**	**205**	**4,685**	**4,843**

Details of any shares or options held by directors are presented on page 20 and 122.

The emoluments of the Chairman were £1,279,000 (2017: £1,289,000). The emoluments of the highest paid director were £1,857,000 (2017: £1,657,000) including pension contributions of £35,000 (2017: £35,000).

Secure Trust Bank was paid a fee of £36,000 up to 8 August 2018 (2017: £60,000) for the services of Mr. Lynam rendered as a non-executive director.

Retirement benefits are accruing under money purchase schemes for three directors who served during 2018 (2017: four directors).

Independent auditor's report

to the members of Arbuthnot Banking Group PLC

1. Our opinion is unmodified

We have audited the financial statements of Arbuthnot Banking Group PLC ("the Company") for the year ended 31 December 2018 which comprise the consolidated statement of comprehensive income, consolidated statement of financial position, company statement of financial position, consolidated statement of changes in equity, company statement of changes in equity, consolidated statement of cashflows, company statement of cashflows, and the related notes, including the accounting policies in notes 2 & 3.

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 31 December 2018 and of the Group's loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- the parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We have fulfilled our ethical responsibilities under, and are independent of the Group in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to listed entities. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion.

Overview		
Materiality: group financial statements as a whole	£600,000 (2017:£570,000) 8.8% (2017: 8%) of Group profit before tax	
Coverage	100% (2017:100%) of group profit before tax	
Risks of material misstatement		**vs 2017**
Event driven	New: Brexit uncertainty	New matter
Recurring risks	Loan loss provisioning	▲
	Revenue recognition: effective interest rate	◄►
	Investment property	▲
	Recoverability of parent company's investment in subsidiaries	◄►

2. Key audit matters: including our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. The key audit matters in arriving at our audit opinion above were addressed in the context of, and solely for the purpose of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Brexit uncertainty

Refer to page 16 (strategic report)

The risk	Our response
Group and Parent **Unprecedented levels of uncertainty** All audits assess and challenge the reasonableness of estimates, in particular as described in loan loss provisioning, revenue recognition: effective interest rate and investment properties below and related disclosures and the appropriateness of the going concern basis of preparation of the annual accounts. All of these depend on assessments of the future economic environment and the Group's future prospects and performance. In addition, we are required to consider the other information presented in the Annual Report including the principal risks disclosure and to consider the directors' statement that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy. Brexit is one of the most significant economic events for the UK and at the date of this report its effects are subject to unprecedented levels of uncertainty of outcomes, with the full range of possible effects unknown.	We have developed a standardised firm-wide approach to the consideration of the uncertainties arising from Brexit in planning and performing our audits. Our procedures included: — **Our Brexit knowledge** – We considered the directors' assessment of Brexit-related sources of risk for the Group's business and financial resources compared with our own understanding of the risks. We considered the directors' plans to take action to mitigate the risks. — **Sensitivity analysis** – When addressing loan impairment, recognition of revenue: effective interest rate, investment properties and other areas that depend on forecasts, we compared the directors' sensitivity analysis to our assessment of the full range of reasonably possible scenarios resulting from Brexit uncertainty. — **Assessing transparency** – As well as assessing individual disclosures as part of our procedures on loan loss provisioning, revenue recognition: effective interest rate and investment properties we considered all the Brexit related disclosures together, including those in the strategic report, comparing the overall picture against our understanding of the risks. No audit should be expected to predict the unknowable factors or all possible future implications for a Group and this is particularly the case in relation to Brexit.

KPMG

Loan loss provisioning

Group - £6.6 million; 2017: £1.4 million

Refer to page 26 (Audit Committee Report), note 3.10 (accounting policy) and note 23 (financial disclosures).

The risk

Group

Subjective estimate

IFRS 9 was implemented by the Group on 1 January 2018. This new standard requires the Group to recognise expected credit losses (ECL) on financial instruments which involves significant judgement and estimates to be made by the Group.

The most significant areas where we identified greater levels of management judgement are:

- Significant increase in credit risk (SICR) and the Group's definition of default – the criteria selected to identify a SICR and the Group's definition of default are judgmental and can materially impact the ECL by determining whether a 12 month (stage 1) or lifetime (stage 2 or 3) provision is recorded.
- Economic scenarios – IFRS 9 requires the Group to measure ECL on a forward-looking basis, incorporating future macro-economic variables reflecting a range of future conditions.
- Complex ECL model – inherently judgemental modelling techniques are used to estimate stage 1 ECLs which involves determining Probabilities of Default (PD) and Loss Given Default (LGD).
- Data capture - the ECL model uses a combination of static (e.g. original collateral valuation) and dynamic data (e.g. current balance/interest rates) about the Group's loans. Owing to the risk of associated with transferring system data to the impairment model (e.g. due to manual process) there is a risk that the data used in the ECL model is inaccurate.
- For loans classified as stage 2 or 3, these are individually assessed, an impairment assessment is required at an individual loan level, based on the probability of default and the estimated future cash flows discounted to present value at the loans effective interest rate ('EIR'). There are a number of data inputs and assumptions including the cost of obtaining and selling collateral and, probable sale proceeds.

The effect of these matters is that, as part of our risk assessment, we determined that the impairment of loans and advances to customers has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. Note 4 of the financial statements discloses the sensitivities estimated by the Group.

Disclosure quality

The disclosures regarding the Group's application of IFRS 9 are key to understanding the change from IAS 39 as well as explaining the key judgments and material inputs to the IFRS 9 ECL results.

Our response

Our audit procedures over SICR and the Group's definition of default included:

— **Methodology implementation:** We compared the Group's SICR thresholds and definition of default with the relevant accounting standard.

— **Benchmarking assumptions:** We compared the Group's SICR thresholds and definition of default with other lenders.

Our audit procedures over the Group's economic scenarios included:

— **Sensitivity analysis**: We performed sensitivity analysis over the probability weightings attached to each economic scenario.

— **Benchmarking assumptions:** We compared the Group's probability weightings attached to each economic scenario to other lenders.

Our audit procedures over the Group's ECL model included:

— **Data comparison:** We checked a sample of the internal data used in the model back to the Group's and Bank's underlying source. We also checked the external inputs of collateral valuations to supporting documentation.

— **Methodology implementation:** We assessed whether the model, if applied as designed, would perform the impairment calculation as intended.

Our audit procedures over the Group's stage 2 and 3 loans where impairment indicators had been identified included:

— **Test of detail:** We tested the completeness of the Group's listing of loans classified as stage 2 or 3 by assessing the accuracy of arrears reporting.

— **Assessing valuers credential:** We evaluated the competence of the valuers engaged by the directors to support the valuation of collateral. This included consideration of their qualifications and expertise.

— **Sensitivity analysis:** We performed sensitivity analysis over the collateral valuation, time to sell and probability of default assumptions.

Assessing transparency: We evaluated whether the disclosures appropriately reflect and address the uncertainty which exists when determining the expected credit losses. As a part of this, we assessed the sensitivity analysis that is disclosed. In addition, we challenged whether the disclosure of the key judgments and assumptions made was sufficiently clear.

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Revenue recognition: effective interest rate

Group - *£65.3* million; 2017: £47.4 million
Refer to page 26 (Audit Committee Report), note 3.4 (accounting policy) and note 8 (financial disclosures).

The risk	Our response
Group **Subjective estimate** Using models, interest and fees earned and incurred on loans are recognised using the effective interest rate ('EIR') method that spreads directly attributable expected cash flows over the expected lives of the loans. The expected lives of loans are uncertain. The most significant areas where we identified greater levels of management judgement are: • Accounting implications - for originated loans, transaction costs are required to be spread over the EIR period. Given that transaction costs are often one-off costs, usually occurring either at the start or at the end of the contract, it is not uncommon for these to be overlooked when constructing EIR models. • Calculation error - the EIR model is complex and so open to the possibility of arithmetical errors and that modelling principles are not in accordance with accounting requirements. • Data capture - the EIR model uses data about the Group's loans that are sourced in other systems. The transfer of data from the underlying system to the EIR model is a manual process. There is a risk that the data used in the model is inaccurate. The effect of these matters is that, as part of our risk assessment, we determined that revenue recognition; effective interest rate has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole, and possibly many times that amount. Note 4 discloses the sensitivities estimated by the Group.	Our procedures included: — **Methodology implementation:** We compared the application of the EIR methodology and the cash flows included in the models with the relevant accounting standard, checking that the model included the appropriate transaction costs. — **Tests of detail:** Through sample testing we assessed whether the model performs the EIR calculation as designed. — **Control operations:** We visited the servicer for the loan book not administered by the Group to test the relevant controls over the recording of loan balances and interest at these entities. — **Data capture:** We performed sample testing to assess the accuracy and consistency of the information provided by the servicer company to the Group; and that this is appropriately captured in the models. — **Sensitivity analysis:** We assessed the models for their sensitivity to changes in the key assumptions by considering different profiles to help us assess the reasonableness of the assumptions used and identify areas of potential additional focus. — **Historical comparison:** We critically assessed the Group's cash flow forecasts by comparing them to current and past performance of the Group's portfolios, including recent cash collections. — **Assessing transparency:** We evaluated whether the disclosures appropriately reflect and address the level of subjective estimation that exists when determining revenue recognition on the Group's loan portfolios. In addition, we challenged whether the disclosure of the key estimates and assumptions made was sufficiently clear.

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Investment properties

Group - £67.1 million; 2017: £59.4 million
Refer to page 26 (Audit Committee Report), note 3.17 (accounting policy) and note 31 (financial disclosures).

The risk	Our response
Group **Subjective valuation** Investment property requires the directors to apply significant judgments and estimates to its fair value assessment. The directors have prepared models with input from professional advisors to calculate the fair value of the investment properties. As a result there is an inherent risk that the assumptions used in the calculations are not complete, accurate or appropriate. The effect of these matters is that, as part of our risk assessment, we determined that investment properties have a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole, and possibly many times that amount. Note 4 discloses the sensitivities estimated by the Group.	Our procedures included: — **Assessing valuers' credentials:** We evaluated the competence of the experts engaged by the Group to support the valuation methodologies and key assumptions. This included consideration of their qualifications and expertise. — **Our property valuation expertise:** With the assistance of our property valuation specialists, we challenged the valuation approaches and assumptions determined by the directors. — **Benchmarking assumptions:** We compared the Group's key assumptions on yields taking into account market data and asset-specific considerations. We also considered whether other key assumptions applied by the Group (i.e. estimated future rental value) were supported by available data. — **Sensitivity analysis:** We have undertaken sensitivity analysis over the key valuation assumptions (i.e. yields, renovation costs and future rental value). — **Assessing transparency:** We assessed the adequacy of the investment property disclosures by reference to the requirements in IAS 40.

Recoverability of parent company's investment in subsidiaries

Parent - *£134.6* million; 2017: *97.8* million
Refer to note 3.1a (accounting policy) and note 43 (financial disclosures).

The risk	Our response
Parent **Recoverability of investment** The carrying value of the parent Company's investment in subsidiaries represents 79% (2017: 70%) of the Company's total assets. Recoverability of the investment is not considered a high risk of significant misstatement or subject to significant judgement. However, due to the materiality of the investment in the context of the parent Company financial statements, this is considered to be the area that had the greatest focus of our overall parent Company audit.	Our procedures included: — **Tests of detail:** Compared the carrying amount of a sample of the highest value investments, representing 98% (2017: 98%) of the total investment balance with the relevant subsidiaries' balance sheet to identify whether their net assets, being an approximation of their minimum recoverable amount, were in excess of their carrying amount and assessing whether those subsidiaries have historically been profit-making. — **Assessing subsidiary audits:** Assessing the work performed during the subsidiary audits on that sample of those subsidiaries and considering the results of that work, on those subsidiaries' profits and net assets.

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3. Our application of materiality and an overview of the scope of our audit

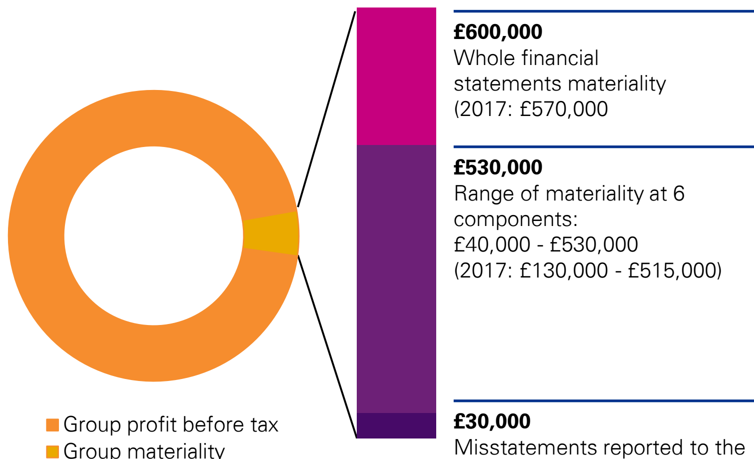
Materiality for the Group financial statements as a whole was set at £600,000 (2017: £570,000). This was determined with reference to the performance of the individual components within the Group, representing 8.8% (2017: 8%) of Group profit before tax.

Materiality for the parent Company financial statements as a whole was set at £386,000 (2017: £406,000), determined with reference to a benchmark of parent company profit before tax, of which it represents 4.5% (2017: 4.5% of parent Company profit before tax).

We reported to the Audit Committee any corrected or uncorrected identified misstatements exceeding £30,000 (2017: £28,500), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Group profit before tax
£6,780,000 (2017: £6,971,000)

Group Materiality
£600,000 (2017: £570,000)



How we scoped our audit:

Of the Group's 6 (2017: 3) components, we subjected 6 (2017: 3) to full scope audits for group purposes. The components within the scope of our work accounted for the 100% (2017: 100%) of Group revenue, 100% (2017: 100%) of Group profit before tax and 100% of Group total assets (2017: 100%).

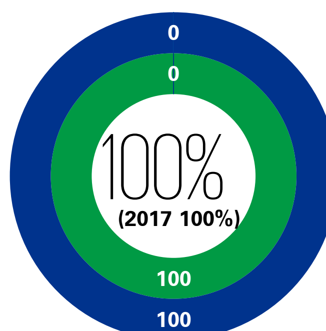
The Group team approved the component materialities which ranged from £40,000 to £530,000 (2017: £130,000 to £515,000), having regard to the mix of size and risk profile of the Group and components.

The audit of one (2017: one) component was performed by a UK component audit team. The audit of the remainder of the Group was performed by the Group audit team.

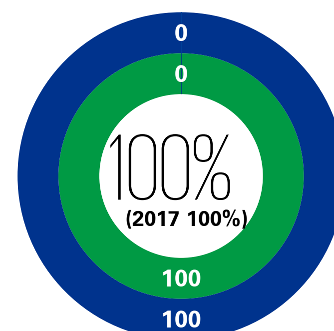
The Group team instructed the component auditor as to the significant areas to be covered, including the relevant risks detailed above and the information to be reported back.

Telephone conference meetings were held with the component auditor. At these meetings, the findings reported to the Group team were discussed in more detail, and any further work required by the Group team was then performed by the component auditor.

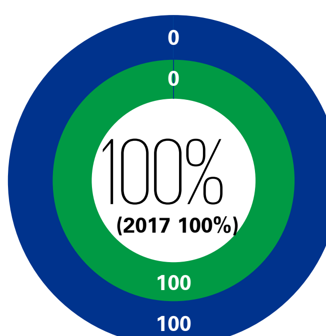
Group revenue



Group profit before tax



Group total assets



Full scope for group audit purposes 2018

Full scope for group audit purposes 2017

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4. We have nothing to report on going concern

The Directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the Company or the Group or to cease their operations, and as they have concluded that the Company's and the Group's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over their ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

Our responsibility is to conclude on the appropriateness of the Directors' conclusions and, had there been a material uncertainty related to going concern, to make reference to that in this audit report. However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgments that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the group or the company will continue in operation.

In our evaluation of the Directors' conclusions, we considered the inherent risks to the Group's and Company's business model and analysed how those risks might affect the Group's and Company's financial resources or ability to continue operations over the going concern period. The risks that we considered most likely to adversely affect the Group's and Company's available financial resources over this period was the impact of Brexit on the Group and Company's liquidity and capital resources, in particular:

- availability of funding and liquidity in the event of a market wide stress scenario including the impact of Brexit, and
- impact on regulatory capital requirements and resources in the event of an economic slowdown or recession.

As these were risks that could potentially cast significant doubt on the Group's and the Company's ability to continue as a going concern, we considered sensitivities over the level of available financial resources indicated by the Group's financial forecasts taking account of reasonably possible (but not unrealistic) adverse effects that could arise from these risks individually and collectively and evaluated the achievability of the actions the Directors consider they would take to improve the position should the risks materialise.

Based on this work, we are required to report to you if:

— we have anything material to add or draw attention to in relation to the directors' statement in Note 2e to the financial statements on the use of the going concern basis of accounting with no material uncertainties that may cast significant doubt over the Group and Company's use of that basis for a period of at least a year from the date of approval of the financial statements

We have nothing to report in these respects, and we did not identify going concern as a key audit matter.

5. We have nothing to report on the other information in the Annual Report

The directors are responsible for the other information presented in the Annual Report together with the financial statements. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except as explicitly stated below, any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work we have not identified material misstatements in the other information.

Strategic report and directors' report

Based solely on our work on the other information:

— we have not identified material misstatements in the strategic report and the directors' report;

— in our opinion the information given in those reports for the financial year is consistent with the financial statements; and

— in our opinion those reports have been prepared in accordance with the Companies Act 2006.

Disclosures of principal risks and longer-term viability

Based on the knowledge we acquired during our financial statements audit, we have nothing material to add or draw attention to in relation to:

— the directors' confirmation within the director's report on page 19 that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency and liquidity;

— the Risks and Uncertainties disclosures describing these risks and explaining how they are being managed and mitigated; and

— the directors' explanation in the Group Director's Report – Viability Statement of how they have assessed the prospects of the Group, over what period they have done so and why they considered that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Our work is limited to assessing these matters in the context of only the knowledge acquired during our financial statements audit. As we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgments that were reasonable at the time they were made, the absence of anything to report on these statements is not a guarantee as to the Group's and Company's longer-term viability.

Corporate governance disclosures

We are required to report to you if:

— we have identified material inconsistencies between the knowledge we acquired during our financial statements audit and the directors' statement that they consider that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy; or

— the section of the annual report describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.

We have nothing to report in these respects.

6. We have nothing to report on the other matters on which we are required to report by exception

Under the Companies Act 2006, we are required to report to you if, in our opinion:

— adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or

— the parent Company financial statements are not in agreement with the accounting records and returns; or

— certain disclosures of directors' remuneration specified by law are not made; or

— we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 21, the directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

Irregularities – ability to detect

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the annual accounts from our general commercial and sector experience, through discussion with the directors (as required by auditing standards), and from inspection of the Group's regulatory correspondence and discussed with the directors the policies and procedures regarding compliance with laws and regulations. We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit. The potential effect of these laws and regulations on the annual accounts varies considerably.

Firstly, the Group is subject to laws and regulations that directly affect the annual accounts including financial reporting legislation (including related companies legislation, distributable profits legislation and taxation legislation), and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the Group is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the annual accounts, for instance through the imposition of fines or litigation or the loss of the Group's licence to operate. We identified the following areas as those most likely to have such an effect: regulatory capital and liquidity, conduct, financial crime including money laundering and certain aspects of company legislation recognising the financial and regulated nature of the Group's activities.

Through these procedures we became aware of actual or suspected non-compliance and considered the effect as part of our procedures on the related financial statement items The actual or suspected non-compliance was not sufficiently significant to our audit to result in our response being identified as a key audit matter.

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the annual accounts, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations (irregularities) is from the events and transactions reflected in the financial statement , the less likely the inherently limited procedures required by auditing standards would identify it. In addition, as with any audit, there remained a higher risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. We are not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

8. The purpose of our audit work and to whom we owe our responsibilities

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Pamela McIntyre
(Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
March 2019

Company statement of financial position

	Note	At 31 December 2018 £000	2017 £000
ASSETS			
Loans and advances to banks	18	17,008	36,103
Financial investments	25	19,313	140
Current tax asset		52	-
Deferred tax asset	26	113	641
Intangible assets	28	6	-
Property, plant and equipment	30	208	157
Other assets	24	42	199
Interests in associates	27	-	5,056
Interests in subsidiaries	43	134,614	97,802
Total assets		**171,356**	**140,098**
EQUITY AND LIABILITIES			
Equity			
Share capital	37	153	153
Other reserves	38	(8,133)	(1,111)
Retained earnings	38	162,729	124,659
Total equity		**154,749**	**123,701**
LIABILITIES			
Current tax liability		-	152
Other liabilities	34	3,324	3,141
Debt securities in issue	35	13,283	13,104
Total liabilities		**16,607**	**16,397**
Total equity and liabilities		**171,356**	**140,098**

The Company has elected to take the exemption under section 408 of the Companies Act 2006 not to present the Parent Company profit and loss account. The profit for the Parent Company for the year is presented in the Statement of Changes in Equity.

Consolidated statement of changes in equity

	Attributable to equity holders of the Group					
	Share capital	Capital redemption reserve	Fair value reserve*	Treasury shares	Retained earnings	Total
	£000	£000	£000	£000	£000	£000
Balance at 31 December 2017	**153**	**20**	**162**	**(1,131)**	**237,171**	**236,375**
IFRS 9 adjustment net of tax	-	-	-	-	(2,090)	(2,090)
Balance at 1 January 2018	**153**	**20**	**162**	**(1,131)**	**235,081**	**234,285**
Total comprehensive income for the period						
Loss for 2018	-	-	-	-	(20,033)	(20,033)
Other comprehensive income, net of tax						
Changes in fair value of equity investments at fair value through other comprehensive income**	-	-	(13,893)	-	-	(13,893)
Tax on other comprehensive income	-	-	(26)	-	-	(26)
Total other comprehensive income	**-**	**-**	**(13,919)**	**-**	**-**	**(13,919)**
Total comprehensive income for the period	**-**	**-**	**(13,919)**	**-**	**(20,033)**	**(33,952)**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Unwind Employee Trust	-	-	-	-	685	685
Sale of Secure Trust Bank shares	-	-	1,588	-	(1,588)	-
Final dividend relating to 2017	-	-	-	-	(2,829)	(2,829)
Interim dividend relating to 2018	-	-	-	-	(2,233)	(2,233)
Total contributions by and distributions to owners	**-**	**-**	**1,588**	**-**	**(5,965)**	**(4,377)**
Balance at 31 December 2018	**153**	**20**	**(12,169)**	**(1,131)**	**209,083**	**195,956**

* The Available-for-sale reserve in 2017 was reclassified to the Fair value reserve as from 1 January 2018 with the introduction of IFRS 9.

** Mainly relate to movement in STB share price. There is currently no tax implications to the movement as the shareholding still qualifies for significant shareholding exemption.

	Attributable to equity holders of the Group					
	Share capital	Capital redemption reserve	Available-for-sale reserve	Treasury shares	Retained earnings	Total
	£000	£000	£000	£000	£000	£000
Balance at 1 January 2017	**153**	**20**	**(251)**	**(1,131)**	**235,567**	**234,358**
Total comprehensive income for the period						
Profit for 2017	-	-	-	-	6,523	6,523
Other comprehensive income, net of tax						
Available-for-sale reserve - net change in fair value	-	-	128	-	-	128
Available-for-sale reserve - Associate - net change in fair value	-	-	389	-	-	389
Tax on other comprehensive income	-	-	(104)	-	-	(104)
Total other comprehensive income	**-**	**-**	**413**	**-**	**-**	**413**
Total comprehensive income for the period	**-**	**-**	**413**	**-**	**6,523**	**6,936**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Equity settled share based payment transactions	-	-	-	-	(155)	(155)
Final dividend relating to 2016	-	-	-	-	(2,680)	(2,680)
Interim dividend relating to 2017	-	-	-	-	(2,084)	(2,084)
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**(4,919)**	**(4,919)**
Balance at 31 December 2017	**153**	**20**	**162**	**(1,131)**	**237,171**	**236,375**

Company statement of changes in equity

	Attributable to equity holders of the Company					
	Share capital	Capital redemption reserve	Fair value/ available-for-sale reserve*	Treasury shares	Retained earnings	Total
	£000	£000	£000	£000	£000	£000
Balance at 1 January 2017	**153**	**20**	**-**	**(1,131)**	**133,847**	**132,889**
Total comprehensive income for the period						
Loss for 2017	-	-	-	-	(4,269)	(4,269)
Other comprehensive income, net of income tax	-	-	-	-	-	-
Total comprehensive income for the period	**-**	**-**	**-**	**-**	**(4,269)**	**(4,269)**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Equity settled share based payment transactions	-	-	-	-	(155)	(155)
Final dividend relating to 2016	-	-	-	-	(2,680)	(2,680)
Interim dividend relating to 2017	-	-	-	-	(2,084)	(2,084)
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**(4,919)**	**(4,919)**
Balance at 31 December 2017	**153**	**20**	**-**	**(1,131)**	**124,659**	**123,701**
Total comprehensive income for the period						
Profit for 2018	-	-	-	-	46,049	46,049
Other comprehensive income, net of income tax	-	-	-	-	-	-
Changes in fair value of equity investments at fair value through other comprehensive income**	-	-	(10,624)	-	-	(10,624)
Total other comprehensive income	**-**	**-**	**(10,624)**	**-**	**-**	**(10,624)**
Total comprehensive income for the period	**-**	**-**	**(10,624)**	**-**	**46,049**	**35,425**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Unwind Employee Trust	-	-	-	-	685	685
Sale of Secure Trust Bank shares	-	-	1,588	-	(1,588)	-
Transfer of Secure Trust Bank shares to AL	-	-	2,014	-	(2,014)	-
Final dividend relating to 2017	-	-	-	-	(2,829)	(2,829)
Interim dividend relating to 2018	-	-	-	-	(2,233)	(2,233)
Total contributions by and distributions to owners	**-**	**-**	**3,602**	**-**	**(7,979)**	**(4,377)**
Balance at 31 December 2018	**153**	**20**	**(7,022)**	**(1,131)**	**162,729**	**154,749**

* The Available-for-sale reserve in 2017 was reclassified to the Fair value reserve as from 1 January 2018 with the introduction of IFRS 9.

** Mainly relate to movement in STB share price. There is currently no tax implications to the movement as the shareholding still qualifies for significant shareholding exemption.

Consolidated statement of cash flows

	Note	Year ended 31 December 2018 £000	Year ended 31 December 2017 £000
Cash flows from operating activities			
Interest received		73,879	43,389
Interest paid		(8,290)	(6,093)
Fees and commissions received		13,669	8,682
Other income		6,588	3,033
Cash payments to employees and suppliers		(84,216)	(47,600)
Taxation paid		(1,217)	(379)
Cash flows from operating profits before changes in operating assets and liabilities		413	1,032
Changes in operating assets and liabilities:			
- net increase in derivative financial instruments		(38)	(331)
- net increase in loans and advances to customers		(180,600)	(233,175)
- net decrease/(increase) in other assets		4,758	(7,952)
- net increase in amounts due to customers		323,505	392,937
- net increase/(decrease) in other liabilities		2,310	(843)
Net cash inflow from operating activities		**150,348**	**151,668**
Cash flows from investing activities			
Disposal of financial investments		9,301	-
Purchase of computer software	28	(2,294)	(2,641)
Purchase of property, plant and equipment	30	(2,482)	(666)
Proceeds from sale of property, plant and equipment	30	97	-
Purchase of investment property	31	(879)	(6,421)
Disposal of Tarn Crag (Holdings) Limited	27	-	900
Purchase of Renaissance Asset Finance Limited	29	-	(2,072)
Cash balance acquired through Renaissance Asset Finance Limited acquisition	29	-	2,815
Purchase of debt securities		(467,772)	(211,080)
Proceeds from redemption of debt securities		356,883	90,410
Net cash outflow from investing activities		**(107,146)**	**(128,755)**
Cash flows from financing activities			
Increase/(decrease) in borrowings		37,578	132,928
Dividends paid		(5,062)	(4,764)
Net cash inflow/(outflow) from financing activities		**32,516**	**128,164**
Net increase in cash and cash equivalents		75,718	151,077
Cash and cash equivalents at 1 January		383,780	232,703
Cash and cash equivalents at 31 December	41	**459,498**	**383,780**

Company statement of cash flows

	Note	Year ended 31 December 2018 £000	Year ended 31 December 2017 £000
Cash flows from operating activities			
Dividends received from subsidiaries		3,056	2,618
Interest received		84	202
Interest paid		(559)	(513)
Other income		52,260	1,643
Cash payments to employees and suppliers		(50,316)	(7,977)
Taxation paid		(402)	-
Cash flows from operating profit/(loss) before changes in operating assets and liabilities		4,123	(4,027)
Changes in operating assets and liabilities:			
- net decrease/(increase) in group company balances		155	(1,788)
- net (increase)/decrease in other assets		(1)	690
- net increase in other liabilities		187	120
Net cash inflow/(outflow) from operating activities		**4,464**	**(5,005)**
Cash flows from investing activities			
Increase investment in subsidiary	43	(18,500)	(43,200)
Disposal of property, plant and equipment		97	-
Purchase of property, plant and equipment	30	(94)	-
Net cash (outflow)/inflow from investing activities		**(18,497)**	**(43,200)**
Cash flows from financing activities			
Dividends paid		(5,062)	(4,764)
Net cash used in financing activities		**(5,062)**	**(4,764)**
Net decrease in cash and cash equivalents		(19,095)	(52,969)
Cash and cash equivalents at 1 January		36,103	89,072
Cash and cash equivalents at 31 December	41	**17,008**	**36,103**

Notes to the Consolidated Financial Statements

1. Reporting entity

Arbuthnot Banking Group PLC is a company domiciled in the United Kingdom. The registered address of Arbuthnot Banking Group PLC is 7 Wilson Street, London, EC2M 2SN. The consolidated financial statements of Arbuthnot Banking Group PLC as at and for the year ended 31 December 2018 comprise Arbuthnot Banking Group PLC and its subsidiaries (together referred to as the "Group" and individually as "subsidiaries"). The Company is the holding company of a group primarily involved in banking and financial services.

2. Basis of preparation

(a) Statement of compliance

The Group's consolidated financial statements and the Company's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs as adopted and endorsed by the EU) and the Companies Act 2006 applicable to companies reporting under IFRS.

The consolidated financial statements were authorised for issue by the Board of Directors on 27 March 2019.

(b) Basis of measurement

The consolidated and company financial statements have been prepared under the historical cost convention, as modified by investment property and derivatives, financial assets and financial liabilities at fair value through profit or loss or other comprehensive income.

(c) Functional and presentational currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Pounds Sterling, which is the Company's functional and the Group's presentational currency.

(d) Use of estimates and judgements

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

(e) Going concern

After making appropriate enquiries which assessed strategy, profitability, funding, risk management (see Note 6) and capital resources (see Note 7), the directors are satisfied that the Company and the Group have adequate resources to continue in operation for the foreseeable future. The financial statements are therefore prepared on the going concern basis.

(f) Accounting developments

The accounting policies adopted are consistent with those of the previous financial year, except for the following:

IFRS 9 'Financial Instruments'

IFRS 9 Financial Instruments is effective for annual periods beginning on or after 1 January 2018. It replaces IAS 39 Financial Instruments: Recognition and Measurement. The Group has adopted IFRS 9 on 1 January 2018. This results in changes in accounting policies previously recognised in the financial statements.

In accordance with the transitional arrangements of IFRS 9 comparative figures have not been restated. However, as required by the transitional arrangements if prior periods are not restated, any difference arising between IAS 39 carrying amounts and IFRS 9 carrying amounts at 1 January 2018 are recognised in opening retained earnings (or in other comprehensive income, as applicable) at 1 January 2018.

IFRS 9 introduces key changes in the following areas:

- Classification and measurement, that is based on the business model and contractual cash flow characteristics of the financial instruments.
- Impairment, introducing an expected credit loss model using forward looking information which replaces the incurred loss model. The expected loss model introduces a three stage approach to impairment.

a) Classification and measurement

The Group classifies financial assets into one of the three following categories:

- Amortised cost, financial assets held in a business model in order to collect contractual cash flows, where the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest ("SPPI") on the principal amount outstanding.
- Fair value through other comprehensive income ("FVOCI"), financial assets held in a business model which collects contractual cash flows and sells financial assets where the contractual terms of the financial assets give rise on specified dates to cash flows that are solely payments of principal and interest ("SPPI") on the principal amount outstanding. The Group currently has no financial assets within this business model.
- Fair value through profit or loss ("FVPL), assets not measured at amortised cost or FVOCI. There is an option to make an irrevocable election on initial recognition for non-traded equity investments to be measured at FVOCI, in which case dividends are recognised in profit or loss, but gains or losses are not reclassified to profit or loss upon de-recognition, and impairment is not recognised in the income statement. The election can be made on an instrument by instrument basis.

IFRS 9 has not changed the classification or measurement of the Groups financial liabilities.

(b) Impairment
IFRS 9 replaced the IAS 39 "incurred loss" impairment recognition framework with a three stage expected credit loss approach ("ECL"). The three stages under IFRS 9 are as follows:
- Stage 1 – entities are required to recognise a 12 month ECL allowance on initial recognition.
- Stage 2 – a lifetime loss allowance is held for assets where a significant increase in credit risk has been identified since initial recognition for financial assets that are not credit impaired. The assessment of whether credit risk has increased significantly since initial recognition is performed for each reporting period for the life of the loan.
- Stage 3 – a lifetime ECL allowance is required for financial assets that are credit impaired at the reporting date.

Measurement of ECL
The assessment of credit risk and the estimation of ECL are unbiased and probability weighted. ECL is measured on either a 12 month (Stage 1) or lifetime (Stage 2) basis depending on whether a significant increase in credit risk has occurred since initial recognition or where an account meets the Group's definition of default (Stage 3).

The ECL calculation is a product of an individual loan's probability of default ('PD'), exposure at default ('EAD') and loss given default ('LGD') discounted at the effective interest rate ('EIR').

Significant increase in credit risk ("SICR") (movement to Stage 2)
The Group's transfer criteria determines what constitutes a significant increase in credit risk, which results in a financial asset being moved from Stage 1 to Stage 2. The Group has determined that a significant increase in credit risk arises when an individual borrower is more than 30 days past due or if forbearance measures have been put in place.

The Group monitors the ongoing appropriateness of the transfer criteria, where any proposed amendments will be reviewed and approved by the Groups Credit Committees at least annually and more frequently if required.

A borrower will move back into stage 1 conditional upon both a minimum of 6 months' good account conduct and the improvement of the Client's situation to the extent that the probability of default has receded sufficiently and a full repayment of the loan, without recourse to the collateral, is likely.

Definition of default (movement to Stage 3)
The Group uses a number of qualitative and quantitative criteria to determine whether an account meets the definition of default and as a result moves into Stage 3. The criteria are as follows:
- The rebuttable assumption that more than 90 days past due is an indicator of default. The Group therefore deems more than 90 days past due as an indicator of default, except for cases where the customer is already within forbearance. This will ensure that the policy is aligned with the Basel/Regulatory definition of default.
- The Group has also deemed it appropriate to classify accounts where there has been a breach in agreed forbearance arrangements, recovery action is in hand or Bankruptcy proceedings or similar insolvency process of a client, or director of a company.

A borrower will move out of Stage 3 when their credit risk improves such that they are no longer past due and remain up to date for an internally approved period.

Forward looking macroeconomic scenarios
IFRS 9 requires the entity to consider the risk of default and impairment loss taking into account expectations of economic changes that are reasonable.

The Group uses a bespoke macroeconomic model to determine the most significant factors which may influence the likelihood of an exposure defaulting in the future. At present, the most significant macroeconomic factor relates to property prices. The Group

currently consider five probability weighted scenarios. The model adopts five probability weighted scenarios no change, severe, moderate, growth and decline. The Group has derived an approach for factoring probability weighted macroeconomic forecasts into ECL calculations, adjusting PD and LGD estimates.

Expected life
IFRS 9 requires lifetime expected credit losses to be measured over the expected life. Currently the Group considers the loan's behavioural life is equal to the contractual loan term. This approach will continue to be monitored and enhanced if and when deemed appropriate.

Transition disclosures
The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Group's financial assets and financial liabilities as at 1 January 2018:

Financial assets	Original classification under IAS 39	Carrying amount under IAS 39 on 31 December 2017 £000	New classification under IFRS 9	Carrying amount under IFRS 9 on 1 January 2018 £000
Cash and balances at central banks	Loans and receivables	313,101	Amortised cost	313,101
Loans and advances to banks	Loans and receivables	70,679	Amortised cost	70,679
Debt securities	Held-to-maturity	227,019	Amortised cost	227,019
Derivative financial instruments	FVPL	2,551	Mandatorily at FVPL	2,551
Loans and advances to customers	Loans and receivables	1,049,269	Amortised cost	1,046,689
Financial investments - Equity	Available-for-sale	1,635	Designated FVOCI	1,635
Financial investments - Debt	Available-for-sale	712	FVPL	712
Total financial assets		**1,664,966**		**1,662,386**
Financial liabilities				
Deposits from banks	Amortised cost	195,097	Amortised cost	195,097
Deposits from customers	Amortised cost	1,390,781	Amortised cost	1,390,781
Derivative financial instruments	FVPL	931	Mandatorily at FVPL	931
Total financial liabilities		**1,586,809**		**1,586,809**

The following table sets out the impact of adopting IFRS 9 on the statement of financial position carrying amounts and retained earnings as at 1 January 2018. Only balances impacted by the transition to IFRS 9 are included in the table; all other balances are unchanged.

Group Impact of adoption of IFRS 9 on retained earnings	£000
Recognition of expected credit losses under IFRS 9	2,580
Related tax	(490)
Impact at 1 January 2018	**2,090**

Impact of adopting IFRS 9 on the impairment of the financial assets
The most significant impact on the Group's financial statements from the adoption of IFRS 9 results from the new impairment requirements. On the adoption of IFRS 9 on 1 January 2018, the increase in loss allowances (before tax) was £2.6m.

The following table reconciles the closing impairment for financial assets in accordance with IAS 39 as at 31 December 2017, to the opening ECL allowance determined in accordance with IFRS 9 as at 1 January 2018:

	IAS 39 carrying amount on 31 December 2017	Re-measurement	IFRS 9 opening balance on 1 January 2019	Of which		
Group	£000	£000	£000	Stage 1 £000	Stage 2 £000	Stage 3 £000
Loans and advances to customers (gross)	1,050,631	-	**1,050,631**	992,252	29,502	28,877
Less allowances for impairment	(1,362)	(2,580)	**(3,942)**	(1,244)	(1,178)	(1,520)
Loans and advances to customers	**1,049,269**	**(2,580)**	**1,046,689**	**991,008**	**28,324**	**27,357**

The ECL coverage as a percentage of gross loans and advances at 1 January 2018 was 0.38% and by Stage as follows: Stage 1 - 0.13%, Stage 2 - 3.99% and Stage 3 - 5.26%.

Forward looking information
The Group incorporates forward looking information (FLI) into the assessment of whether there has been a significant increase in credit risk and the calculation of ECLs.

IFRS 9 requires an unbiased and probability weighted estimate of credit losses by evaluating a range of possible outcomes that incorporates forecasts of future economic conditions. FLI is required to be incorporated into the measurement of ECL as well as the determination of whether there has been a significant increase in credit risk since origination. Measurement of ECLs at each reporting period should reflect reasonable and supportable information at the reporting date about past events, current conditions and forecasts of future economic conditions. Forecasts for key macroeconomic variables that most closely correlate with the Bank's portfolio are used to produce five economic scenarios, comprising of no change, upside case, downside case, moderate stress and severe stress, and the impacts of these scenarios are then probability weighted. The estimation and application of this forward looking information will require significant judgement. External information is used to produce the forecast information.

Transition impact including impact on capital
The Group recorded an adjustment to its opening retained earnings as at 1 January 2018 to reflect the application of the new requirements at the adoption date, and has not restated comparative periods. The total adjustment to capital was £2.8m.

Under IFRS 9, the Group's CET1 ratio has reduced by approximately 1 basis points after transitional relief (23 basis points before transitional relief). This is mainly driven by the increase in IFRS 9 ECL for standardised portfolios that directly impacts CET1 as there is no regulatory deduction to absorb the increase.

CET 1 ratio
- 17.32% under IAS 39 at 31 December 2017;
- 17.09% under IFRS 9 at 1 January 2018 before transitional relief;
- 17.31% under IFRS 9 at 1 January 2018 after transitional relief.

Transitional relief relates to the phasing of the impact of the initial adoption of ECL as permitted by Regulation (EU) 2017/2395 of the European Parliament and Council. The Group has adopted the transitional relief. Under this approach, the balance of ECL allowances in excess of the regulatory excess EL and standardised portfolios are phased into the CET1 capital base over 5 years. The proportion phased in for the balance at each reporting period is 2018: 5%; 2019 15%; 2020 30%; 2021 50%; 2022 75%. From 2023 onwards, there is no transitional relief.

v) Impact on Governance and Controls
The Group plans to apply its existing governance framework to ensure that appropriate controls and validations are in place over key processes and judgments to determine the ECL. As part of the implementation, the Group has refined existing internal controls and implemented new controls where required in areas that are impacted by IFRS 9, including controls over the development and probability weighting of macroeconomic scenarios, credit risk data and systems, and the determination of a significant increase in credit risk.

IFRS 15 Revenue from Contracts with customers
On 1 January 2018, the Group adopted the requirements of IFRS 15. IFRS 15 established a comprehensive framework for revenue recognition. It replaces existing revenue recognition guidance, including IAS 18 Revenue.

IFRS 15 establishes the principles to apply when reporting information about the nature, amount, timing and uncertainty of revenue and cash flows from a contract with a customer. The standard introduces a five step revenue recognition model to be applied to all contracts with customers to determine whether, how much, and when revenue is recognised.

The new standard replaces IAS 18 'Revenue', IAS 11 'Construction Contracts' and related interpretations. It applies to all revenue arising from contracts with customers but does not apply to insurance contracts, financial instruments or lease contracts, which fall under the scope of other IFRS standards. It also does not apply if two companies in the same line of business exchange non-monetary assets to facilitate sales to other parties. Of particular note, interest income, the main source of revenue for the Group, falls outside the scope of IFRS 15.

The Group also generates fees from banking services, primarily management fees and commissions. Fees in respect of banking services are recognised in line with the satisfaction of performance obligations. This can be either at a point in time or over time, in

line with the provision of the service to the customer. The majority of banking services are performed at a point in time and payment is due from a customer at the time a transaction takes place. For services performed over time, payment is generally due in line with the satisfaction of performance obligations. The costs of providing these banking services are incurred as the services are rendered. The price is usually fixed and always determinable.

The Group has adopted IFRS 15 using the cumulative effect method (without practical expedients), as such the standard is applied as of 1 January 2018 and comparative information is not restated. The cumulative effect of initially applying IFRS 15 is recognised as an adjustment to the opening balance of retained earnings. IFRS 15 is only applied retrospectively to contracts that are not completed contracts at 1 January 2018.

The Group assessed its non-interest revenue streams that fall under the scope of IFRS 15 and determined that there was no material impact on the amount or timing of revenue to be recognised as a result of the adoption of IFRS 15. As such there is no adjustment to the opening balance of retained earnings or related tax balances. Furthermore, there is no impact to the consolidated statement of financial position or the consolidated statements of profit and loss and other comprehensive income. Revenue is disaggregated by reportable segment as detailed in Note 9.

3. Significant accounting policies

The accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

3.1. Consolidation

(a) Subsidiaries

Subsidiaries are all investees (including special purpose entities) controlled by the Group. The Group controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The acquisition method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Identifiable assets acquired, liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the cost of acquisition over the fair value of the Group's shares of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the Statement of Comprehensive Income as a gain on bargain purchase. Contingent consideration related to an acquisition is initially recognised at the date of acquisition as part of the consideration transferred, measured at its acquisition date fair value and recognised as a liability. The fair value of a contingent consideration liability recognised on acquisition is remeasured at key reporting dates until it is settled, changes in fair value are recognised in the profit or loss.

The Company's investments in subsidiaries are recorded at cost less, where appropriate, provisions for impairment in value.

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

(b) Changes in ownership and non-controlling interests

Changes in ownership interest in a subsidiary that do not result in the loss of control are accounted for as equity transactions and no gain or loss is recognised. Adjustments to non-controlling interests are based on a proportionate amount of the net assets of the subsidiary.

When control of a subsidiary is lost, the Group derecognises the assets, liabilities, non-controlling interest and all other components of equity relating to the former subsidiary from the consolidated statement of financial position. Any resulting gain or loss is recognised in profit or loss. Any investment retained in the former subsidiary is recognised at its fair value at the date when control is lost.

(c) Special purpose entities

Special purpose entities ("SPEs") are entities that are created to accomplish a narrow and well-defined objective such as the securitisation of particular assets or the execution of a specific borrowing or lending transaction. SPEs are consolidated when the investor controls the investee. The investor would only control the investee if it had all of the following:

- power over the investee;
- exposure, or rights, to variable returns from its involvement with the investee; and
- the ability to use its power over the investee to affect the amount of the investor's returns.

The assessment of whether the Group has control over an SPE is carried out at inception and the initial assessment is only reconsidered at a later date if there were any changes to the structure or terms of the SPE, or there were additional transactions between the Group and the SPE.

(d) Associates
Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20 and 50 percent of the voting power of another entity. Associates are accounted for using the equity method and are initially recognised at cost. The Group's investment includes goodwill identified on acquisition, net of any accumulated impairment losses. The consolidated financial statements include the Group's share of the total comprehensive income and equity movements of equity accounted investees, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds its interest in an equity accounted investee, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the investee.

3.2. Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Group Board. The Group Board, which is responsible for allocating resources and assessing performance of the operating segments, has been identified as the chief operating decision maker. All transactions between segments are conducted on an arm's length basis. Income and expenses directly associated with each segment are included in determining segment performance. There are six operating segments:

- Private Banking – Provides traditional private banking services as well as offering financial planning and investment management services.
- Commercial Banking – Provides bespoke commercial banking services and tailored secured lending against property investments and other assets.
- Renaissance Asset Finance – Specialist asset finance lender mainly in high value cars but also business assets.
- All other divisions – All other smaller divisions and central costs in Arbuthnot Latham & Co., Ltd (Arbuthnot Commercial Asset-Based Lending, Arbuthnot Direct, Arbuthnot Specialist Finance, Dubai, Tay mortgage portfolio, Investment properties and Central costs)
- Group Centre – ABG Group Centre management

3.3. Foreign currency translation

Foreign currency transactions are translated into the functional currency using the spot exchange rates prevailing at the dates of the transactions or valuation where items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Statement of Comprehensive Income. Foreign exchange differences arising from translation of equity instruments, where an election has been made to present subsequent fair value changes in Other Comprehensive Income ("OCI"), will also be recognised in OCI.

3.4. Interest income and expense

Interest income and expense are recognised in the Statement of Comprehensive Income for all instruments measured at amortised cost using the effective interest rate ("EIR") method.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:
- the gross carrying amount of the financial asset; or
- the amortised cost of the financial liability.

The 'gross carrying amount of a financial asset' is the amortised cost of a financial asset before adjusting for any expected credit loss allowance. When calculating the effective interest rate, the Group takes into account all contractual terms of the financial instrument but does not consider expected credit losses.

The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

For financial assets that have become credit impaired following initial recognition, interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset. If the asset is no longer credit impaired, then the calculation of interest income reverts to the gross basis.

The Group monitors the actual cash flows for each acquired book and where they diverge significantly from expectation, the future cash flows are reset. Expectation may diverge due to factors such as one-off payments or expected credit losses. In assessing whether

to adjust future cash flows on an acquired portfolio, the Group considers the cash variance on an absolute and percentage basis. The Group also considers the total variance across all acquired portfolios. Where cash flows for an acquired portfolio are reset, they are discounted at the EIR to derive a new carrying value, with changes taken to profit or loss as interest income. The EIR rate is adjusted for events where there is a change to the reference interest rate (Bank of England base rate) affecting portfolios with a variable interest rate which will impact future cash flows. The revised EIR is the rate which exactly discounts the revised cash flows to the net carrying value of the loan portfolio.

3.5. Fee and commission income

Fee and commission income which is integral to the EIR on a financial asset are included in the effective interest rate (see note 3.4).

All other fee and commission income is recognised as the related services are performed, under IFRS 15. Fee and commission income is reported in the below segments.

Types of fee	Description
Banking commissions	- Banking Tariffs are charged monthly for services provided.
Investment management fees	- Annual asset management fees relate to a single performance obligation that is continuously provided over an extended period of time.
Wealth planning fees	- Provision of bespoke, independent Wealth Planning solutions to Arbuthnot Latham's clients to help them achieve their long-term financial goals.
Foreign exchange fees	- Provides foreign currencies for our clients to purchase/sell.

The principles in applying IFRS 15 to fee and commission use the following 5 step model:

- identify the contract(s) with a customer;
- identify the performance obligations in the contract;
- determine the transaction price;
- allocate the transaction price to the performance obligations in the contract; and
- recognise revenue when or as the Group satisfies its performance obligations.

Asset and other management, advisory and service fees are recognised, under IFRS 15, as the related services are performed. The same principle is applied for financial planning services that are continuously provided over an extended period of time.

The Group includes the transaction price, some or all of an amount of, variable consideration estimated only to the extent that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty associated with the variable consideration is subsequently resolved.

Policy applicable before 1 January 2018

Fees and commissions which are not considered integral to the effective interest rate are recognised on an accrual basis when the service has been provided.

Asset and other management, advisory and service fees are recognised on an accruals basis as the related services are performed. The same principle is applied for financial planning services that are continuously provided over an extended period of time.

3.6. Rental income

Rental income is recognised on a straight line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income over the term of the lease.

3.7. Discontinued operations

A discontinued operation is a component of the Group's business, the operations and cash flows of which can be clearly distinguished from the rest of the Group and which:

- represents a separate major line of business or geographical area of operations;
- is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or
- is a subsidiary acquired exclusively with a view to re-sale.

Classification as a discontinued operation occurs on disposal or when the operation meets the criteria to be classified as held for sale (see note 3.14), if earlier. When an operation is classified as a discontinued operation, the comparative Statement of Comprehensive Income is re-presented as if the operation had been discontinued from the start of the comparative year.

3.8. Financial assets and financial liabilities

3.8.1 Financial assets and financial liabilities (Policy applicable from 1 January 2018)

IFRS 9 requires financial assets and liabilities to be measured at amortised cost, fair value through other comprehensive income ("FVOCI") or fair value through the profit and loss ("FVPL"). Liabilities are measured at amortised cost or FVPL. The Group classifies financial assets and financial liabilities in the following categories: financial assets and financial liabilities at FVPL; FVOCI, financial assets and liabilities at amortised cost and other financial liabilities. Management determines the classification of its financial instruments at initial recognition.

A financial asset or financial liability is measured initially at fair value plus, transaction costs that are directly attributable to its acquisition or issue with the exception of financial assets at FVPL where these costs are debited to the income statement.

(a) Financial instruments measured at amortised cost

Financial assets that are held to collect contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortised cost. A basic lending arrangement results in contractual cash flows that are solely payments of principal and interest on the principal amount outstanding. Financial assets measured at amortised cost are predominantly loans and advances and debt securities.

Loans and advances

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable and the SPPI criteria are met. Loans are recognised when cash is advanced to the borrowers inclusive of transaction costs. Loans and advances, other than those relating to assets leased to customers, are carried at amortised cost using the effective interest rate method. The accounting for assets leased to customers is set out under note 3.18(a).

Debt securities at amortised cost

Debt securities at amortised cost are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has determined meets the SPPI criteria. Debt security investments are carried at amortised cost using the effective interest rate method, less any impairment loss.

(b) Financial assets and financial liabilities at FVPL

Financial assets and liabilities are classified at FVPL where they do not meet the criteria to be measured at amortised cost or FVOCI or where financial assets are designated at FVPL to reduce an accounting mismatch. They are measured at fair value in the statement of financial position, with fair value gains/losses recognised in the income statement.

Financial assets that are held for trading or managed within a business model that is evaluated on a fair value basis are measured at FVPL, because the business objective is neither hold-to-collect contractual cash flows nor hold-to-collect-and-sell contractual cash flows.

This category comprises derivative financial instruments and financial investments. Derivative financial instruments utilised by the Group include structured notes and derivatives used for hedging purposes.

Financial assets and liabilities at FVPL are initially recognised on the date from which the Group becomes a party to the contractual provisions of the instrument, including any acquisition costs. Subsequent measurement of financial assets and financial liabilities held in this category are carried at FVPL until the investment is sold.

(c) Financial instruments at FVOCI

Financial instruments at FVOCI are those not classified as another category of financial assets. These include investments in special purpose vehicles and equity investments in unquoted vehicles. They may be sold in response to liquidity requirements, interest rate, exchange rate or equity price movements. Financial investments are initially recognised at cost, which is considered as the fair value of the investment including any acquisition costs. The securities are subsequently measured at fair value in the statement of financial position.

Fair value changes in the securities are recognised directly in equity (OCI).

A debt instrument is measured at fair value through other comprehensive income if it meets both of the following conditions:

- the asset is held within a business model whose objective is achieved by collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset meet the SPPI criterion.

There is a rebuttable presumption that all equity investments are FVPL, however on initial recognition the Group may make an irrevocable election to present the fair value movement of equity investments that are not held for trading within OCI. The election can be made on an instrument by instrument basis.

For debt instruments, changes in fair value are recognised in OCI.
For equity instruments, there are no reclassifications of gains and losses to the profit or loss statement on derecognition and no impairment recognised in the profit or loss. Equity fair value movements are not reclassified from OCI under any circumstances.

(d) Financial guarantees and loan commitments
Financial guarantees represent undertakings that the Group will meet a customer's obligation to third parties if the customer fails to do so. Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. The Group is theoretically exposed to loss in an amount equal to the total guarantees or unused commitments; however, the likely amount of loss is expected to be significantly less; most commitments to extend credit are contingent upon customers maintaining specific credit standards. Liabilities under financial guarantee contracts are initially recorded at their fair value, and the initial fair value is amortised over the life of the financial guarantee. Subsequently, the financial guarantee liabilities are measured at the higher of the initial fair value, less cumulative amortisation, and the best estimate of the expenditure to settle obligations.

(e) Other financial liabilities
Other financial liabilities are non-derivative financial liabilities with fixed or determinable payments. Other financial liabilities are recognised when cash is received from the depositors. Other financial liabilities are carried at amortised cost using the effective interest rate method. The fair value of other liabilities repayable on demand is assumed to be the amount payable on demand at the Statement of Financial Position date.

Basis of measurement for financial assets and liabilities
Amortised cost measurement
The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at initial recognition, minus principal payments, plus or minus the cumulative amortisation using the effective interest rate method of any difference between the initial amount recognised and the maturity amount, less any reduction for impairment.

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

When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same for which market observable prices exist, net present value and discounted cash flow analysis.

For measuring derivatives that might change classification from being an asset to a liability or vice versa such as interest rate swaps, fair values take into account both credit valuation adjustment (CVA) and debit valuation adjustment (DVA) when market participants take this into consideration in pricing the derivatives.

Derecognition
Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or when the Group has transferred substantially all risks and rewards of ownership. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Group is recognised as a separate asset or liability in the Statement of Financial Position. In transactions in which the Group neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset and it retains control over the asset, the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset. There have not been any instances where assets have only been partially derecognised.

The Group derecognises a financial liability when its contractual obligations are discharged, cancelled, expire, are modified or exchanged.

Offsetting
Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group currently has a legally enforceable right to set off the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions such as the Group's trading activity.

3.8.2 Financial assets and financial liabilities (Policy applicable before 1 January 2018)
The Group classifies financial assets and financial liabilities in the following categories: financial assets and financial liabilities at FVTPL; loans and receivables; held-to-maturity investments; available-for-sale financial assets and other financial liabilities. Management determines the classification of its investments at acquisition. A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

(a) Financial assets and financial liabilities at FVTPL (policy applicable before 1 January 2018)
This category comprises listed securities and derivative financial instruments. Derivative financial instruments utilised by the Group include embedded derivatives and derivatives used for hedging purposes. Financial assets and liabilities at fair value through profit or loss are initially recognised on the date from which the Group becomes a party to the contractual provisions of the instrument. Subsequent measurement of financial assets and financial liabilities held in this category are carried at fair value through profit or loss.

(b) Loans and receivables (policy applicable before 1 January 2018)
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. Loans are recognised when cash is advanced to the borrowers. Loans and receivables, other than those relating to assets leased to customers, are carried at amortised cost using the effective interest rate method.

(c) Held-to-maturity (policy applicable before 1 January 2018)
Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has the positive intent and ability to hold to maturity and that have not been designated at FVTPL or as available-for-sale investments. Held-to-maturity investments are carried at amortised cost using the effective interest rate method, less any impairment loss.

(d) Available-for-sale (policy applicable before 1 January 2018)
Available-for-sale ("AFS") investments are those not classified as another category of financial assets. These include investments in special purpose vehicles and equity investments in unquoted vehicles. They may be sold in response to liquidity requirements, interest rate, exchange rate or equity price movements. AFS investments are initially recognised at cost, which is considered as the fair value of the investment including any acquisition costs. AFS securities are subsequently measured at fair value in the statement of financial position.

Fair value changes in the AFS securities are recognised directly in equity (AFS reserve) until the investment is sold or impaired. Once sold or impaired, the cumulative gains or losses previously recognised in the AFS reserve are recycled to the profit or loss.

(f) Other financial liabilities
Other financial liabilities are non-derivative financial liabilities with fixed or determinable payments. Other financial liabilities are recognised when cash is received from the depositors. Other financial liabilities are carried at amortised cost using the effective interest rate method. The fair value of other liabilities repayable on demand is assumed to be the amount payable on demand at the Statement of Financial Position date.

3.9. Derivative financial instruments

All derivatives are recognised at their fair value. Fair values are obtained using recent arm's length transactions or calculated using valuation techniques such as discounted cash flow models at the prevailing interest rates, and for structured notes classified as financial instruments fair values are obtained from quoted market prices in active markets. Derivatives are shown in the Statement of Financial Position as assets when their fair value is positive and as liabilities when their fair value is negative.

Embedded derivatives (policy before 1 January 2018)
Embedded derivatives arise from contracts ('hybrid contracts') containing both a derivative (the 'embedded derivative') and a non-derivative (the 'host contract'). Where the economic characteristics and risks of the embedded derivatives are not closely related to those of the host contract, and the host contract is not at fair value through profit or loss, the embedded derivative is bifurcated and reported at fair value and gains or losses are recognised in the Statement of Comprehensive Income.

3.10. Impairment of financial assets

(a) Assets carried at amortised cost
The Group recognises loss allowances on an expected credit loss basis for all financial assets measured at amortised cost, including loans and advances, debt securities and loan commitments.

Credit loss allowances are measured as an amount equal to lifetime ECL, except for the following assets, for which they are measured as 12 month ECL:
- Financial assets determined to have a low credit risk at the reporting date
- Financial assets which have not experienced a significant increase in credit risk since their initial recognition.

Impairment model
The IFRS 9 impairment model adopts a three stage approach based on the extent of credit deterioration since origination:

- Stage 1: 12-month ECL applies to all financial assets that have not experienced a significant increase in credit risk ("SICR") since origination and are not credit impaired. The ECL will be computed based on the probability of default events occurring over the next 12 months. This Stage 1 approach is different from the historic approach which estimates a collective allowance to recognise losses that have been incurred but not reported on performing loans. Stage 1 includes the current performing loans (up to date and in arrears of less than 10 days) and those within Heightened Business Monitoring ("HBM"). Accounts requiring HBM are classified as a short-term deterioration in financial circumstances and are tightly monitored with additional proactive client engagement, but not deemed SICR.

A financial asset is within HBM where:
- A loan is in arrears between 10 and 30 days;
- Bankers become aware of signs of potential future difficulties, such as
  - cash flow difficulties
  - unexpected hard core borrowing
  - regular requests for excesses
  - returned cheques
  - lack of engagement/failure to respond to information requests
  - breach of covenants/conditions
  - count court judgements

- Stage 2: When a financial asset experiences a SICR subsequent to origination, but is not in default, it is considered to be in Stage 2. This requires the computation of ECL based on the probability of all possible default events occurring over the remaining life of the financial asset. Provisions are higher in this stage (except where the value of charge against the financial asset is sufficient to enable recovery in full) because of an increase in credit risk and the impact of a longer time horizon being considered (compared to 12 months in Stage 1).

Evidence that a financial asset has experienced a SICR includes the following considerations:
- A loan is in arrears between 31 and 90 days;
- Forbearance action has been undertaken;

- Stage 3: Financial assets that are credit impaired are included in this stage. Similar to Stage 2, the allowance for credit losses will continue to capture the lifetime expected credit losses. At each reporting date, the Group will assess whether financial assets carried at amortised cost are in default. A financial asset will be considered to be in default when an event(s) that has a detrimental impact on estimated future cash flows have occurred.

Evidence that a financial asset is within Stage 3 includes the following data:
- A loan is in arrears in excess of 90 days;
- Breach of terms of forbearance;
- Recovery action is in hand; or
- Bankruptcy proceedings or similar insolvency process of a client, or director of a company.

The credit risk of financial assets that become credit impaired are not expected to improve such that they are no longer considered credit impaired.

Presentation of allowance for ECL in the statement of financial position
For financial assets measured at amortised cost, these are presented as the gross carrying amount of the assets minus a deduction for the ECL.

Write-off
Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. This is the case when the Group determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the outstanding amount due.

(b) Renegotiated loans
Loans that are neither subject to ECLs nor individually significant, and whose terms have been renegotiated, are no longer considered to be past due but are treated as new loans.

(c) Forbearance
Under certain circumstances, the Group may use forbearance measures to assist borrowers who are experiencing significant financial hardship. Any forbearance support is assessed on a case by case basis in line with best practice and subject to regular monitoring and review. The Group seeks to ensure that any forbearance results in a fair outcome for both the customer and the Group.

(d) Assets classified as financial investments
Equity instruments at fair value through other comprehensive income
Equity investments are not subject to impairment charges recognised in the income statement. Any fair value gains and losses are recognised in OCI whch are not subject to reclassification to the income statement on derecognition.

Debt instruments at FVOCI
Changes in fair value are recognised in OCI, the loss allowance will be recognised in OCI and shall not reduce the carrying amount of the financial asset in the statement of financial position. Impairment costs will be recognised in the profit or loss with a corresponding entry to OCI. On derecognition, cumulative gains and losses in OCI are reclassified to the profit or loss.

Impairments to financial assets carried at FVOCI are recognised in the Statement of Comprehensive Income.

Impairment of assets carried at amortised cost (Policy applicable before 1 January 2018)
On an ongoing basis the Group assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. Objective evidence is the occurrence of a loss event, after the initial recognition of the asset, that impacts on the estimated contractual future cash flows of the financial asset or group of financial assets, and can be reliably estimated.
The criteria that the Group uses to determine whether there is objective evidence of an impairment loss include, but are not limited to the following:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower;
- Initiation of bankruptcy proceedings;
- Deterioration in the value of collateral;
- Deterioration of the borrower’s competitive position.

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset’s carrying amount and the present value of estimated future cash flows discounted at the financial asset’s original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the Statement of Comprehensive Income.

If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

The Group considers evidence of impairment for loans and advances at both a specific asset and collective level. All individually significant loans and advances are assessed for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. In assessing collective impairment, the Group uses historical trends of the probability of default, emergence period, the timing of recoveries and the amount of loss incurred, adjusted for management’s judgement as to whether current economic and credit conditions are such that the actual losses are likely to be significantly different to historic trends.

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the Statement of Comprehensive Income.
A customer’s account may be modified to assist customers who are in or have recently overcome financial difficulties and have demonstrated both the ability and willingness to meet the current or modified loan contractual payments. Loans that have renegotiated or deferred terms, resulting in a substantial modification to the cash flows, are no longer considered to be past due but are treated as new loans recognised at fair value, provided the customers comply with the renegotiated or deferred terms.

3.11. Impairment of non-financial assets
The carrying amounts of the Group’s non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset’s recoverable amount is estimated. Impairment for goodwill is discussed in more detail under note 3.15(a).

3.12. Term Funding Scheme
The Term Funding Scheme (“TFS”) was announced by the Bank of England on 4 August 2016 and became effective from 19 September 2016. The scheme is now closed. The TFS allows participants to borrow central bank reserves in exchange for eligible collateral. Amounts drawn from the TFS are included within “Deposits from banks” on the Statement of Financial Position as detailed in Note 32.

3.13. Inventory

Land acquired through repossession of collateral which is subsequently held in the ordinary course of business with a view to develop and sell is accounted for as inventory.

Inventory is measured at the lower of cost or net realisable value. The cost of inventories comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

3.14. Assets classified as held for sale

Assets, or disposal groups comprising assets and liabilities, that are expected to be recovered primarily through sale rather than through continuing use, are classified as held for sale.

The criteria that the Group uses to determine whether an asset is held for sale under IFRS 5 include, but are not limited to the following:

- Management is committed to a plan to sell
- The asset is available for immediate sale
- An active programme to locate a buyer is initiated
- The sale is highly probable, within 12 months of classification as held for sale
- The asset is being actively marketed for sale at a sales price reasonable in relation to its fair value

Current assets held for sale are measured at the lower of their carrying amount and fair value less costs to sell except where measurement and remeasurement is outside the scope of IFRS 5. Where investments that have initially been recognised as current assets held for sale, because the Group has been deemed to hold a controlling stake, are subsequently disposed of or diluted such that the Group’s holding is no longer deemed a controlling stake, the investment will subsequently be classified as fair value through profit or loss or fair value through other comprehensive income investments in accordance with IFRS 9. Subsequent movements will be recognised in accordance with the Group’s accounting policy for the newly adopted classification.

Once classified as held for sale, intangible assets and property, plant and equipment are no longer amortised or depreciated.

3.15. Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group’s share of the net identifiable assets of the acquired subsidiary or associate at the date of acquisition. Goodwill on acquisitions of subsidiaries or associates is included in ‘intangible assets’. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

The Group reviews the goodwill for impairment at least annually or more frequently when events or changes in economic circumstances indicate that impairment may have taken place and carries goodwill at cost less accumulated impairment losses. Assets are grouped together in the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit" or "CGU"). For impairment testing purposes goodwill cannot be allocated to a CGU that is greater than a reported operating segment. CGUs to which goodwill has been allocated are aggregated so that the level at which impairment is tested reflects the lowest level at which goodwill is monitored for internal reporting purposes. Goodwill acquired in a business combination is allocated to groups of CGUs that are expected to benefit from the synergies of the combination. The test for impairment involves comparing the carrying value of goodwill with the present value of pre-tax cash flows, discounted at a rate of interest that reflects the inherent risks of the CGU to which the goodwill relates, or the CGU’s fair value if this is higher.

(b) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the basis of the expected useful lives (three to ten years).

Costs associated with maintaining computer software programs are recognised as an expense as incurred.

Costs associated with developing computer software which are assets in the course of construction, which management has assessed to not be available for use, are not amortised.

(c) Other intangibles

Other intangibles include trademarks, customer relationships, broker relationships, technology and banking licences acquired. These costs are amortised on the basis of the expected useful lives (three to fourteen years).

3.16. Property, plant and equipment

Land and buildings comprise mainly branches and offices and are stated at the latest valuation with subsequent additions at cost less depreciation. Plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, applying the following annual rates, which are subject to regular review:

Leasehold improvements	3 to 20 years
Office equipment	3 to 10 years
Computer equipment	3 to 5 years
Motor vehicles	4 years

Leasehold improvements are depreciated over the term of the lease (until the first break clause). Gains and losses on disposals are determined by deducting carrying amount from proceeds. These are included in the Statement of Comprehensive Income.

3.17. Investment property

Investment property is initially measured at cost. Transaction costs are included in the initial measurement. Subsequently, investment property is measured at fair value, with any change therein recognised in profit and loss within other income.

If a change in use occurs and investment property is transferred to owner-occupied property, the property's deemed cost for subsequent reporting is its fair value at the date of change in use.

3.18. Leases

(a) As a lessor

Assets leased to customers under agreements which transfer substantially all the risks and rewards of ownership, with or without ultimate legal title, are classified as finance leases. When assets are held subject to finance leases, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

Assets leased to customers under agreements which do not transfer substantially all the risks and rewards of ownership are classified as operating leases. When assets are held subject to operating leases, the underlying assets are held at cost less accumulated depreciation. The assets are depreciated down to their estimated residual values on a straight-line basis over the lease term. Lease rental income is recognised on a straight line basis over the lease term.

(b) As a lessee

Rentals made under operating leases are recognised in the Statement of Comprehensive Income on a straight-line basis over the term of the lease.

Leases in which the Group assumes substantially all the risks and rewards of ownership of the leased asset are classified as finance leases. Leased assets by way of finance leases are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation. Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

3.19. Cash and cash equivalents

For the purposes of the Statement of Cash Flows, cash and cash equivalents comprises cash on hand and demand deposits, and cash equivalents are deemed highly liquid investments that are convertible into cash with an insignificant risk of changes in value with a maturity of three months or less at the date of acquisition.

3.20. Employee benefits

(a) Post-retirement obligations

The Group contributes to a defined contribution scheme and to individual defined contribution schemes for the benefit of certain employees. The schemes are funded through payments to insurance companies or trustee-administered funds at the contribution rates agreed with individual employees.

The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

There are no post-retirement benefits other than pensions.

(b) Share-based compensation – cash settled
The Group adopts a Black-Scholes valuation model in calculating the fair value of the share options as adjusted for an attrition rate for members of the scheme and a probability of pay-out reflecting the risk of not meeting the terms of the scheme over the vesting period. The number of share options that are expected to vest are reviewed at least annually.

The fair value of cash settled share-based payments is recognised as personnel expenses in the profit or loss with a corresponding increase in liabilities over the vesting period. The liability is remeasured at each reporting date and at settlement date based on the fair value of the options granted, with a corresponding adjustment to personnel expenses.

(c) Deferred cash bonus scheme
The Bank has a deferred cash bonus scheme for senior employees. The cost of the award is recognised to the income statement over the period to which the performance relates.

(d) Short-term incentive plan
The Group has a short-term incentive plan payable to employees of one of its subsidiary companies. The award of a profit share is based on a percentage of the net profit of a Group subsidiary.

3.21. Taxation

Current income tax which is payable on taxable profits is recognised as an expense in the period in which the profits arise. Income tax recoverable on tax allowable losses is recognised as an asset only to the extent that it is regarded as recoverable by offset against current or future taxable profits.

Deferred tax is provided in full on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax is not accounted for if it arises from the initial recognition of goodwill, the initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future. Deferred tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the Statement of Financial Position date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax entities, when they intend to settle current tax liabilities and assets on a net basis or the tax assets and liabilities will be realised simultaneously.

Deferred tax assets are recognised where it is probable that future taxable profits will be available against which the temporary differences can be utilised.

3.22. Issued debt and equity securities

Issued financial instruments or their components are classified as liabilities where the contractual arrangement results in the Group having a present obligation to either deliver cash or another financial asset to the holder, to exchange financial instruments on terms that are potentially unfavourable. Issued financial instruments, or their components, are classified as equity where they meet the definition of equity and confer on the holder a residual interest in the assets of the Company. The components of issued financial instruments that contain both liability and equity elements are accounted for separately with the equity component being assigned the residual amount after deducting from the instrument as a whole the amount separately determined as the fair value of the liability component.

Financial liabilities, other than trading liabilities at fair value, are carried at amortised cost using the effective interest rate method as set out in policy 3.4. Equity instruments, including share capital, are initially recognised as net proceeds, after deducting transaction costs and any related income tax. Dividend and other payments to equity holders are deducted from equity, net of any related tax.

3.23. Share capital

(a) Share issue costs
Incremental costs directly attributable to the issue of new shares or options by Arbuthnot Banking Group, are shown in equity as a deduction, net of tax, from the proceeds.

(b) Dividends on ordinary shares
Dividends on ordinary shares are recognised in equity in the period in which they are approved.

(c) Share buybacks
Where any Group company purchases the Company’s equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company’s equity holders until the shares are cancelled or reissued.

3.24. Financial guarantees and loan commitments

Financial guarantees represent undertakings that the Group will meet a customer's obligation to third parties if the customer fails to do so. Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. The Group is theoretically exposed to loss in an amount equal to the total guarantees or unused commitments. However, the likely amount of loss is expected to be significantly less; most commitments to extend credit are contingent upon customers maintaining specific credit standards. Liabilities under financial guarantee contracts are initially recorded at their fair value, and the initial fair value is amortised over the life of the financial guarantee. Subsequently, the financial guarantee liabilities are measured at the higher of the initial fair value, less cumulative amortisation, and the best estimate of the expenditure to settle obligations.

3.25. Fiduciary activities

The Group commonly acts as trustee and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. These assets and income arising thereon are excluded from these financial statements, as they are not assets of the Group.

3.26. Provisions and contingent liabilities

Provisions are recognised when the Group has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of economic resources will be required from the Group and amounts can be reliably measured.

Onerous contract provisions are recognised for losses on contracts where the forecast costs of fulfilling the contract throughout the contract period exceed the forecast income receivable. In assessing the amount of the loss to provide on any contract, account is taken of the Group's forecast results which the contract is servicing. The provision is calculated based on discounted cash flows to the end of the contract.

Contingent liabilities are disclosed when the Group has a present obligation as a result of a past event, but the probability that it will be required to settle that obligation is more than remote, but not probable.

3.27. New standards and interpretations not yet adopted

The following standards, interpretations and amendments to existing standards have been published and are mandatory for the Group's accounting periods beginning on or after 1 January 2019 or later periods, but the Group has not early adopted them:

IFRS 16, 'Leases' (effective from 1 January 2019).

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. IFRS 16 replaces existing leases guidance, including IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases – Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. IFRS 16 removes the distinction between finance and operating leases and instead provides a single lessee accounting model. The Group, as a lessee, will be required to recognise lease liabilities and corresponding right-of-use assets for all applicable leases. The new standard also provides the option not to recognise 'short-term' leases and leases of 'low-value' assets. Where this exemption is taken, such leases will continue to be expensed to the income statement over the term of the lease.

The income statement recognition pattern for the Group's leases will differ from the current pattern for operating leases, with interest on the liabilities and depreciation expense on the right-of-use assets recognised separately. In the cash flow statement, lease payments will be categorised within financing activities rather than operating activities.

The Group will reassess the classification of sub-leases in which the Group is a lessor. Based on the information currently available the implementation of IFRS 16 is not expected to have a material impact on the financial statements.

IFRS 16 does not significantly change the accounting for finance leases or leases by lessors.

Management are currently reviewing all long-term contractual agreements to ensure all leases are correctly transitioned.

The Group continues to evaluate the full impact of IFRS 16, but expects to recognise right-of-use assets on its balance sheet at the adoption date in respect of property assets currently accounted for as operating leases. A corresponding lease liability will also be recognised, representing the future payments to be made under these leases, discounted at the rate implicitly defined in the lease or, where no rate is defined in the lease, the Group's incremental borrowing rate at lease inception.

Transition

The standard is effective for annual periods beginning on or after 1 January 2019. The Group plans to apply IFRS 16 initially on 1 January 2019, using the modified retrospective approach (option 2). As a result there will be no impact to retained earnings on adoption of IFRS 16, with no restatement of comparative information.

Additionally, on transition, the Group will apply the practical expedient to grandfather the definition of a lease on transition

This means that it will apply IFRS 16 to all contracts entered into before 1 January 2019 and identified as leases in accordance with IAS 17 and IFRIC 4

The Bank has assessed the impact that the initial application will have on its business and will adopt the standard for the year ending 31 December 2019.
It estimates that the IFRS 16 transition amount will:

- increase assets and liabilities by approximately £21m as at 1 January 2019;
- reduce the Group's CETI ratio by 32bps; and
- increase operating expenditure by £0.4m in 2019.

All financial metrics as at 31 December 2018

4. Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

4.1 Estimation uncertainty

(a) Expected credit losses ("ECL") on financial assets

The Group reviews its loan portfolios and debt security investments to assess impairment at least on a quarterly basis. The basis for evaluating impairment losses is described in accounting policy 3.10. The measurement of ECL required by the implementation of IFRS 9, from 1 January 2018, necessitates a number of significant judgements. Specifically judgements and estimation uncertainties relate to assessment of whether credit risk on the financial asset has increased significantly since initial recognition, incorporation of forward-looking information ("FLI") in the measurement of ECLs and key assumptions used in estimating recoverable cash flows. These estimates are driven by a number of factors that are subject to change which may result in different levels of ECL allowances.

The Group incorporates FLI into the assessment of whether there has been a significant increase in credit risk. Forecasts for key macroeconomic variables that most closely correlate with the Bank's portfolio are used to produce five economic scenarios, comprising of a no change, upside case, downside case, moderate stress and severe stress, and the impacts of these scenarios are then probability weighted. The estimation and application of this FLI will require significant judgement supported by the use of external information.

12 month ECLs on loans and advances (loans within Stage 1) are calculated using a statistical model. The key assumptions are the probability of default and the economic scenarios. Life time ECLs on loans and advances (loans within Stage 2 and 3) are calculated based on an individual valuation of the underlying asset and other expected cash flows.

For individually significant financial assets in Stage 2 and 3, ECL is calculated on an individual basis and all relevant factors that have a bearing on the expected future cash flows are taken into account. These factors can be subjective and can include the individual circumstances of the borrower, the realisable value of collateral, the Group's position relative to other claimants, and the likely cost to sell and duration of the time to collect. The level of ECL is the difference between the value of the recoverable amount (which is equal to the expected future cash flows discounted at the loan's original effective interest rate), and its carrying amount.

Management considered a range of variables in determining the level of future ECL. The two of the key judgements were in relation to "time to collect" and "collateral valuations". Sensitivity analysis was carried out based on what was considered reasonably possible in the current market conditions.

If time to collect increased by six months across all Stage 2 and 3 client exposures, this would lead to a negative £0.4m impact through the Profit or Loss. A six month reduction in time to collect would lead to a £0.3m favourable impact on the Profit or Loss.

If the collateral valuations increased by 10% across all Stage 3 client exposures, this would lead to a positive £1.3m impact through the Profit or Loss. If the collateral valuations decreased by 10% across all Stage 3 client exposures, this would lead to a £1.9m adverse impact on the Profit or Loss.

Another of the key judgements concerns the probability of the economic scenarios to the measurement of the ECL. The probability weighting and forward looking economic scenarios as at 31 December 2018 are as follows:

	Probability weighted forward looking economic scenarios				
	Highest Stress	Moderate Stress	No Change	Growth	Decline
Probability of scenario	**1.0%**	**3.0%**	**21.0%**	**25.0%**	**50.0%**
Impact of scenario					
- Change in collateral values					
London	(40.0%)	(20.0%)	-	0.5%	(2.0%)
Rest of UK	(40.0%)	(20.0%)	-	0.5%	(1.5%)
Overseas	(40.0%)	(20.0%)	-	2.3%	(1.0%)
- Movement in share prices*	-	-	-	4.0%	(4.0%)

* - for loans secured against equity portfolios

Management assess a range of scenarios and in the current economic climate it is reasonably possible that the moderate scenario could increase to 9% probability, the decline scenario increase to 60% probability and the growth scenario reduce to 10% probability this would lead to a negative £0.2m impact through Profit or Loss.

(b) Effective Interest Rate

Acquired loan books are initially recognised at fair value. Subsequently, they are measured under the effective interest rate method, based on cash flow models which require significant judgement assumptions on prepayment rates, late payments, the probability and timing of defaults and the amount of incurred losses. Management review the expected cash flows against actual cash flows to ensure future assumptions on customer behaviour and future cash flows remain valid. If the estimates of future cash flows are revised, the gross carrying value of the financial asset is recalculated as the present value of the estimated future contractual cash flows discounted at the original effective interest rate, or in the case of the acquired books the credit-adjusted effective interest rate. The adjustment to the carrying value of the loan book is recognised in the Statement of Comprehensive Income.

Under both IFRS 9 and IAS 39, for the originated loan portfolio interest income is recorded using the effective interest rate method. The key assumptions applied by Management in the EIR methodology remain materially unchanged from the 2017 financial statements.

Management must therefore use judgement to estimate the expected life of each instrument. The accuracy of the effective interest rate would therefore be affected by unexpected market movements resulting in altered customer behaviour, inaccuracies in the models used compared to actual outcomes and incorrect assumptions.

If customer loans repaid 6 months earlier than anticipated on the originated loan book, interest income would increase by £0.8m (2017: £0.3m), due to acceleration of fee income.

In 2018 the Group recognised £0.9m (2017: £64k) of additional interest income to reflect actual cash flows received on the acquired mortgage books being in excess of forecast cash flows.

The key judgements in relation to calculating the net present value of the acquired mortgage books relate to the timing of future cash flows and loss rates on principal repayments. Management have considered an early and delayed 6 month sensitivity on the timing of repayment and a 10% increase and decrease of principal repayments to be to be reasonably possible.

If the acquired loan books were modelled to accelerate cash flows by 6 months, it would increase interest income in 2018 by £0.3m (2017: £0.4m) while a 10% increase in principal repayments will increase interest income in 2018 by £0.3m (2017: £0.2m) through a cash flow reset adjustment. Additionally a 10% increase in credit losses would reduce interest income in 2018 by £0.3m (2017: £0.2m) through a cash flow reset adjustment.

Management must therefore use judgement to estimate the expected life of each instrument. The accuracy of the effective interest rate would therefore be affected by unexpected market movements resulting in altered customer behaviour, inaccuracies in the models used compared to actual outcomes and incorrect assumptions.

Due to acceleration of fee income, if customer loans repaid 6 months earlier than anticipated, interest income would increase by £0.8m (2017: £0.3m).

(c) Investment property

The valuations that the Group places on its investment properties are subject to a degree of uncertainty and are calculated on the basis of assumptions in relation to prevailing market rents and effective yields. These assumptions may not prove to be accurate, particularly in periods of market volatility. The current uncertainty due to Brexit has had the effect of reducing the activity in the property market, which, has in turn resulted in less market evidence being available for Management in making its judgement on the key assumptions of property yield and market rent. The Group currently owns three investment properties, as outlined in note 29.

The Group's in-house surveyors have valued all three investment properties utilising externally sourced market information and property specific knowledge.

King Street in London with value of £53.3m (2017: £53.3m)

The King Street property is currently fully tenanted, with the main lease ending in 2019 at which point the offices will be refurbished and re-let at prevailing market rents. The valuation assessment considers the net present value of net cash flows to be generated from the property, taking into account expected rental growth rate, void periods, occupancy rate, lease incentive costs such as rent-free periods and other costs not paid by tenants. The expected net cash flows are discounted using risk-adjusted discount rates. Among other factors, the discount rate estimation considers the quality of a building and its location, tenant quality and lease terms. Management judgement is required for the inputs used in the discounted cash flow model, which have been assessed as follows:

- yield: 4%
- future rent forecast (per square ft.) £102.50
- refurbishment period of 6 months and rent to be increased by 5% (every 5 years)
- estimated refurbishment costs: £2.2m

		Revised fair value gain / (loss)	
	Variable	£'m	%
Forecast yield	**4.00%**		
- Yield 0.25% lower	3.75%	5.2	9.72%
- Yield 0.15% lower	3.85%	3.3	6.15%
- Yield 0.15% higher	4.15%	(1.9)	(3.50%)
- Yield 0.25% higher	4.25%	(3.4)	(6.40%)
Future forecast rent (Per Square Foot)	**102.5**		
- Positive +5%	107.6	3.0	5.56%
- Negative -5%	97.4	(1.8)	(3.29%)
Forecast periodic Rent Increases (Every 5 years)	**5%**		
- Positive +25%	6%	3.6	6.75%
- Negative -25%	4%	(2.1)	(4.00%)
Forecast refurbishment Costs	**2.2**		
Cost of refurbishment doubles	4.5		
- 5% increase to rental value per square foot (p.s.f.)		0.9	1.78%
- No impact to rental value		(1.4)	(2.65%)
No refurbishment undertaken	-		
- Existing tenants rent p.s.f maintained and periodic rent increase 5%		0.8	1.52%
- Existing tenants rent p.s.f maintained and periodic rent increase 4%		(2.6)	(4.90%)

4 St Philips Place in Birmingham with value of £7m (2017: £6.1m)

The St Philips Place property was acquired on 24 November 2017. The property is currently undergoing comprehensive refurbishment and is therefore unoccupied at the end of the financial year. A development appraisal has been undertaken by estimating the gross development value and deducting the estimated costs to complete the refurbishment, arm's length financing costs and development profit margin.

The gross development has the following key inputs:

- forecast yield: 6.25%

- forecast annual rent: £0.77m
- refurbishment costs: £3.2m

	Variable	Revised fair value gain / (loss) £'m	%
Forecast yield	**6.25%**		
Yield 0.25% lower	6.00%	0.3	3.89%
Yield 0.25% higher	6.50%	(0.5)	(7.13%)
Forecast net rental value (Total Annual £'m)	**0.77**		
Positive +5%	0.81	0.4	5.42%
Negative -5%	0.73	(0.6)	(9.61%)
Forecast development costs	**(3.2)**		
Costs increase +10%	(3.5)	(0.4)	(6.15%)
Costs decrease -10%	(2.9)	0.2	2.68%

Crescent Office Park in Bath with value of £6.8m (2017: £6.8m)
In December 2017, the office building was acquired with the intention to be included within a new property fund initiative that the Group had planned to start-up. The property had tenants in situ with the Fund recognising rental income.

It was recognised as held for sale under IFRS 5 and therefore not consolidated in the financial statements in 2017. In 2018 the launch of the property fund was placed on hold and as a result it was reclassified as an investment property as the property no longer met the IFRS 5 criteria. The property remained occupied as at 31 December 2018 with the Group receiving rental income.

In accordance with IAS 40, the property is recognised at fair value, with its carrying value at year end of £6.8m equal to its fair value.

The valuation of the property has the following key inputs:
- yield: 6.50%
- future rent increases (every five years): 4.00%

	Variable	Revised fair value gain / (loss) £'m	%
Model Yield	**6.50%**		
- Yield 0.25% lower	6.25%	0.2	2.25%
- Yield 0.25% higher	6.75%	(0.4)	(6.10%)
Model Future Rent Increases (Every 5 Years)	**4.00%**		
- Positive +25%	5.00%	0.2	3.11%
- Negative -25%	3.00%	(0.1)	(2.10%)

(e) IFRS 9 'Financial Instruments'
On 1 January 2018, the Group adopted the requirements of IFRS 9. IFRS 9 introduces new requirements for the classification and measurement, impairment and hedge accounting of financial assets and liabilities. The new standard replaces IAS 39 'Financial Instruments: Recognition and Measurement'.

The Group has adjusted its opening 1 January 2018 retained earnings to reflect the application of the new requirements of IFRS 9. In accordance with the transition requirements, comparative periods are not restated. As such, the comparative periods in 2017 are reported under the requirements of IAS 39 and are not comparable to the information presented for 2018.

5. Maturity analysis of assets and liabilities

The table below shows the maturity analysis of assets and liabilities of the Group as at 31 December 2018:

At 31 December 2018	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Cash and balances at central banks	405,325	-	405,325
Loans and advances to banks	54,173	-	54,173
Debt securities at amortised cost	203,211	139,480	342,691
Assets classified as held for sale	8,002	-	8,002
Derivative financial instruments	192	1,654	1,846
Loans and advances to customers	388,603	836,053	1,224,656
Other assets	8,257	4,459	12,716
Financial investments	14,976	20,375	35,351
Deferred tax asset	-	1,490	1,490
Intangible assets	-	16,538	16,538
Property, plant and equipment	-	5,304	5,304
Investment property	-	67,081	67,081
	1,082,739	**1,092,434**	**2,175,173**
LIABILITIES			
Deposits from banks	7,675	225,000	232,675
Derivative financial instruments	188	-	188
Deposits from customers	1,624,978	89,308	1,714,286
Current tax liability	236	-	236
Other liabilities	18,549	-	18,549
Debt securities in issue	-	13,283	13,283
	1,651,626	**327,591**	**1,979,217**

The table below shows the maturity analysis of assets and liabilities of the Group as at 31 December 2017:

At 31 December 2017	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Cash and balances at central banks	313,101	-	313,101
Loans and advances to banks	70,679	-	70,679
Debt securities held-to-maturity	122,236	104,783	227,019
Assets classified as held for sale	2,915	-	2,915
Derivative financial instruments	950	1,601	2,551
Loans and advances to customers	224,954	824,315	1,049,269
Other assets	16,188	4,436	20,624
Financial investments	128	2,219	2,347
Deferred tax asset	-	1,527	1,527
Investment in associate	-	83,804	83,804
Intangible assets	-	15,995	15,995
Property, plant and equipment	-	3,962	3,962
Investment property	-	59,439	59,439
	751,151	**1,102,081**	**1,853,232**
LIABILITIES			
Deposits from banks	195,097	-	195,097
Derivative financial instruments	931	-	931
Deposits from customers	1,333,423	57,358	1,390,781
Current tax liability	705	-	705
Other liabilities	16,239	-	16,239
Debt securities in issue	-	13,104	13,104
	1,546,395	**70,462**	**1,616,857**

The table below shows the maturity analysis of assets and liabilities of the Company as at 31 December 2018:

At 31 December 2018	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Loans and advances to banks	6	-	6
Loans and advances to banks - due from subsidiary undertakings	17,002	-	17,002
Financial investments	-	19,313	19,313
Current tax asset	52	-	52
Deferred tax asset	-	113	113
Intangible assets	-	6	6
Property, plant and equipment	-	208	208
Other assets	42	-	42
Interests in subsidiaries		134,614	134,614
	17,102	**154,254**	**171,356**
LIABILITIES			
Other liabilities	3,324	-	3,324
Debt securities in issue	-	13,283	13,283
	3,324	**13,283**	**16,607**

The table below shows the maturity analysis of assets and liabilities of the Company as at 31 December 2017:

At 31 December 2017	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Loans and advances to banks	6	-	6
Loans and advances to banks - due from subsidiary undertakings	36,097	-	36,097
Financial investments	128	12	140
Deferred tax asset	-	641	641
Property, plant and equipment	-	157	157
Other assets	199	-	199
Interests in associates	-	5,056	5,056
Interests in subsidiaries	-	97,802	97,802
	36,430	**103,668**	**140,098**
LIABILITIES			
Current tax liability	152	-	152
Other liabilities	3,141	-	3,141
Debt securities in issue	-	13,104	13,104
	3,293	**13,104**	**16,397**

6. Financial risk management

Strategy

By their nature, the Group's activities are principally related to the use of financial instruments. The Directors and senior management of the Group have formally adopted a Group Risk and Controls Policy which sets out the Board's attitude to risk and internal controls. Key risks identified by the Directors are formally reviewed and assessed at least once a year by the Board, in addition to which key business risks are identified, evaluated and managed by operating management on an ongoing basis by means of procedures such as physical controls, credit and other authorisation limits and segregation of duties. The Board also receives regular reports on any risk matters that need to be brought to its attention. Significant risks identified in connection with the development of new activities are subject to consideration by the Board. There are budgeting procedures in place and reports are presented regularly to the Board detailing the results of each principal business unit, variances against budget and prior year, and other performance data.

The principal non-operational risks inherent in the Group's business are credit, market, liquidity and capital.

(a) Credit risk

The Company and Group take on exposure to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Significant changes in the economy, or in the health of a particular industry segment that represents a concentration in the Company and Group's portfolio, could result in losses that are different from those provided for at the balance sheet date. Credit risk is managed through the Credit Committee of the banking subsidiary.

The Company and Group structure the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to products, and one borrower or groups of borrowers. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. The limits are approved periodically by the Board of Directors and actual exposures against limits are monitored daily.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral, and corporate and personal guarantees.

The Group employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of collateral to secure advances, which is common practice. The principal collateral types for loans and advances include, but are not limited to:

- Charges over residential and commercial properties;
- Charges over business assets such as premises, inventory and accounts receivable;
- Charges over financial instruments such as debt securities and equities;
- Charges over other chattels; and
- Personal guarantees

Upon initial recognition of loans and advances, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In order to minimise any potential credit loss the Group will seek additional collateral from the counterparty as

soon as impairment indicators are noticed for the relevant individual loans and advances. Repossessed collateral, not readily convertible into cash, is made available for sale in an orderly fashion, with the proceeds used to reduce or repay the outstanding indebtedness, or held as inventory where the Group intends to develop and sell in the future. Where excess funds are available after the debt has been repaid, they are available either for other secured lenders with lower priority or are returned to the customer.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards.

The Group incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and its measurement of ECL. The key inputs into the measurement of the ECL are:

- future economic scenarios
- probability of default
- loss given default
- exposure at default

The Group's maximum exposure to credit risk before collateral held or other credit enhancements is as follows:

Group	2018				
Credit risk exposures (all stage 1, unless otherwise stated)	Private Banking £000	Commercial Banking £000	RAF £000	All Other Divisions £000	Total £000
On-balance sheet:					
Cash and balances at central banks	-	-	-	405,325	405,325
Loans and advances to banks	-	-	354	53,819	54,173
Debt securities at amortised cost	-	-	-	342,691	342,691
Derivative financial instruments	-	-	-	1,846	1,846
Loans and advances to customers (net of ECL)	670,464	443,108	85,957	25,127	1,224,656
Stage 1	618,487	431,630	84,275	25,127	1,159,519
Stage 2	20,033	11,478	1,180	-	32,691
Stage 3	31,944	-	502	-	32,446
Other assets	-	-	443	2,533	2,976
Financial investments	-	-	-	35,351	35,351
Off-balance sheet:					
Guarantees	435	1,309	-	-	1,744
Loan commitments and other credit related liabilities	51,950	15,930	-	-	67,880
At 31 December	**722,849**	**460,347**	**86,754**	**866,692**	**2,136,642**

Group	2017				
Credit risk exposures (under IAS 39)	Private Banking £000	Commercial Banking £000	RAF £000	All Other Divisions £000	Total £000
On-balance sheet:					
Cash and balances at central banks	-	-	-	313,101	313,101
Loans and advances to banks	-	-	1,087	69,592	70,679
Debt securities held-to-maturity	-	-	-	227,019	227,019
Derivative financial instruments	-	-	-	2,551	2,551
Loans and advances to customers (net of impairment)	650,245	305,055	71,265	22,704	1,049,269
Other assets	-	-	137	11,827	11,964
Financial investments	-	-	-	2,347	2,347
Off-balance sheet:					
Guarantees	443	2,533	-	-	2,976
Loan commitments and other credit related liabilities	85,303	46,660	-	-	131,963
At 31 December	**735,991**	**354,248**	**72,489**	**649,141**	**1,811,869**

The Company's maximum exposure to credit risk (all stage 1) before collateral held or other credit enhancements is as follows:

	2018 £000	2017 £000
Credit risk exposures relating to on-balance sheet assets are as follows:		
Loans and advances to banks	17,008	36,103
Financial investments	19,313	140
Other assets	-	162
At 31 December	**36,321**	**36,405**

The above tables represent the maximum credit risk exposure (net of impairment) to the Group and Company at 31 December 2018 and 2017 without taking account of any collateral held or other credit enhancements attached. For financial assets, the balances are based on gross carrying amounts as reported in the Statement of Financial Position. For guarantees and loan commitments, the amounts in the table represent the amounts for which the group is contractually committed.

The table below represents an analysis of the loan to values of the exposures secured by property for the Group:

	2018					
	Private Banking		Commercial Banking		Total	
	Loan Balance	Collateral	Loan Balance	Collateral	Loan Balance	Collateral
Group	£000	£000	£000	£000	£000	£000
Less than 60%	312,478	698,621	249,446	559,271	561,924	1,257,892
Stage 1	297,674	659,650	238,071	532,671	535,745	1,192,321
Stage 2	8,701	25,830	11,375	26,600	20,076	52,430
Stage 3	6,103	13,141	-	-	6,103	13,141
60%-80%	224,782	309,329	165,954	259,917	390,736	569,246
Stage 1	211,737	288,994	165,954	259,917	377,691	548,911
Stage 2	9,458	14,535	-	-	9,458	14,535
Stage 3	3,587	5,800	-	-	-	-
80%-100%	64,649	49,740	6,540	9,400	71,189	59,140
Stage 1	52,968	37,161	6,540	9,400	59,508	46,561
Stage 2	531	550	-	-	531	550
Stage 3	11,150	12,029	-	-	11,150	12,029
Greater than 100%*	28,528	16,860	8,918	7,614	37,446	24,474
Stage 1	16,654	8,245	8,918	7,614	25,572	15,859
Stage 2	-	-	-	-	-	-
Stage 3	11,874	8,615	-	-	11,874	8,615
Total	**630,437**	**1,074,550**	**430,858**	**836,202**	**1,061,295**	**1,910,752**

*In addition to property, other security is taken, including charges over Arbuthnot Latham Investment Management portfolios, other chattels and personal guarantees. The increase in loan to values greater than 100% is due to an increase in exposures collateralised by other assets.

£19.3m of balances with a loan to value of greater than 100% are within Stage 3. Property valuations used are those from the loan origination date or updated 3rd party valuations where applicable.

	2017					
	Private Banking		Commercial Banking		Total	
	Loan Balance	Collateral	Loan Balance	Collateral	Loan Balance	Collateral
Group	£000	£000	£000	£000	£000	£000
Less than 60%	288,734	740,812	166,666	367,550	455,400	1,108,362
60%-80%	238,760	356,242	108,996	168,015	347,756	524,257
80%-100%	64,288	75,298	5,538	5,700	69,826	80,998
Greater than 100%	32,206	26,124	9,142	8,230	41,348	34,354
Total	**623,988**	**1,198,476**	**290,342**	**549,495**	**914,330**	**1,747,971**

Prior year numbers are presented under IAS 39 and therefore has no Staging.

The table below represents an analysis of loan commitments compared to the values of properties for the Group (all Stage 1):

	2018					
	Private Banking		Commercial Banking		Total	
	Loan Balance	Collateral	Loan Balance	Collateral	Loan Balance	Collateral
Group	£000	£000	£000	£000	£000	£000
Less than 60%	30,289	83,603	14,880	32,097	45,169	115,700
60%-80%	15,467	23,295	1,050	1,615	16,517	24,910
Total	**45,756**	**106,898**	**15,930**	**33,712**	**61,686**	**140,610**

	2017					
	Private Banking		Commercial Banking		Total	
	Loan Balance	Collateral	Loan Balance	Collateral	Loan Balance	Collateral
Group	£000	£000	£000	£000	£000	£000
Less than 60%	62,294	218,643	481	56,000	62,775	274,643
60%-80%	20,471	29,935	5,869	8,861	26,340	38,796
80%-100%	28,825	31,982	754	754	29,579	32,736
Greater than 100%	3,590	3,253	1,500	852	5,090	4,105
Total	**115,180**	**283,813**	**8,604**	**66,467**	**123,784**	**350,280**

Renegotiated loans and forbearance

The contractual terms of a loan may be modified due to factors that are not related to the current or potential credit deterioration of the customer (changing market conditions, customer retention, etc.). In such cases, the modified loan may be derecognised and the renegotiated loan recognised as a new loan at fair value.

When the terms of a financial asset are modified and the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly reflects the comparison of:

- its remaining lifetime PD at the reporting date based on the modified terms; with
- the remaining lifetime PD estimated based on data on initial recognition and the original contractual terms.

When modification results in derecognition, a new loan is recognised and allocated to Stage 1 (assuming it is not credit-impaired at that time).

The Group renegotiates loans to customers in financial difficulties (referred to as 'forbearance') to maximise collection opportunities and minimise the risk of default. Under the Group's forbearance policy, loan forbearance is granted on a selective basis if the debtors is currently in default on its debt, or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The revised terms can include changing the timing of interest payments, extending the date of repayment of the loan, transferring a loan to interest only payments and a payment holiday. Both retail and corporate loans are subject to the forbearance policy. The Group Credit Committee regularly reviews reports on forbearance.

For financial assets modified as part of the Group's forbearance policy, the estimate of PD reflects whether the modification has improved or restored the Group's ability to collect interest and principal and the Group's previous experience of similar forbearance action. As part of this process, the Group evaluates the borrower's payment performance against the modified contractual terms and considers various behavioural indicators.

Generally, the forbearance is a qualitative indicator of a SICR (see note 3.10)

As at 31 December 2018, loans for which forbearance measures were in place totalled 2.22% (2017: 2.94%) of total value of loans to customers for the Group. 2017 forbearance has been reclassified to align to current forbearance policy. These are set out in the following table:

	2018		2017	
	Number	Loan Balance	Number	Loan Balance
		£000		£000
Transfer to interest only	1	175	-	-
Term extension	15	25,814	15	29,586
Payment holiday	16	1,189	5	1,237
Total forbearance	**32**	**27,178**	**20**	**30,823**

Concentration risk

The tables below show the concentration in the loan book based on the most significant type of collateral held for each loan.

	Loans and advances to customers		Loan Commitments	
	2018	2017	2018	2017
	£000	£000	£000	£000
Concentration by product				
Asset based lending*	25,128	-	18,122	-
Asset finance	85,958	71,425	-	-
Cash collateralised	5,379	17,747	-	-
Commercial lending	248,042	202,912	4,806	24,371
Investment portfolio secured	45,182	49,667	3,136	4,222
Mixed collateral**	91,167	70,954	4,867	3,957
Residential mortgages	713,095	633,003	54,346	99,413
Unsecured	10,705	3,561	725	-
At 31 December	**1,224,656**	**1,049,269**	**86,002**	**131,963**
Concentration by location				
East Anglia	32,960	18,438	294	-
London	455,567	407,805	28,096	56,777
Midlands	69,686	42,484	3,538	800
North East	18,448	25,741	1,050	-
North West	59,045	44,630	1,275	825
Northern Ireland	2,813	2,903	-	-
Scotland	10,793	10,988	-	-
South East	219,890	203,305	15,522	23,462
South West	140,560	116,692	9,201	15,236
Wales	7,521	8,002	426	-
Overseas	30,486	21,556	1,400	-
Non-property collateral	176,887	146,725	25,200	34,863
At 31 December	**1,224,656**	**1,049,269**	**86,002**	**131,963**

* In 2018 Q1, the Group began its asset-based lending business including invoice discounting, supported by stock, plant & machinery, property and cash flow lending.

** Mixed collateral is where there is no single, overall, majority collateral type.

(b) Operational risk (unaudited)

The Group's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Group's reputation with overall cost effectiveness and to avoid control procedures that restrict initiatives and creativity. The Group is exposed to operational risks from its Information Technology and Operations platforms. There are additional internal controls in these processes that are designed to protect the Group from these risks. The Group's overall approach to managing internal control and financial reporting is described in the Corporate Governance section of the Annual Report.

Compliance with Group standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of the Internal Audit reviews are discussed with senior management, with summaries submitted to the Arbuthnot Banking Group Audit Committee.

Cyber risk

Cyber risk is an increasing risk that the Group is subject to within its operational processes. This is the risk that the Group is subject to some form of disruption arising from an interruption to its IT and data infrastructure. The Group regularly test the infrastructure to ensure that it remains robust to a range of threats, and has continuity of business plans in place including a disaster recovery provision.

Conduct risk

As a financial services provider we face conduct risk, including selling products to customers which do not meet their needs; failing to deal with customers' complaints effectively; not meeting customers' expectations; and exhibiting behaviours which do not meet market or regulatory standards.

The Group adopts a zero risk appetite for any unfair customer outcomes. It maintains clear compliance guidelines and provides ongoing training to all staff. Periodic spot checks and internal audits are performed to ensure these guidelines are being followed. The Group also has insurance policies in place to provide some cover for any claims that may arise.

(c) Market risk

Price risk

The Company and Group are exposed to price risk from equity investments and derivatives held by the Group. The Group is not exposed to commodity price risk.

Based upon the financial investment exposure in Note 25, a stress test scenario of a 10% (2017: 10%) decline in market prices, would result in a £17,000 (2017: £32,000) decrease in the Group's income and a decrease of £3.5m (2017: £231,000) in the Group's equity. The Group considers a 10% stress test scenario appropriate after taking the current values and historic data into account.

Based upon the financial investment exposure given in Note 25, a stress test scenario of a 10% (2017: 10%) decline in market prices, would result in a £nil (2017: £13,000) decrease in the Company's income and a decrease of £1.9m (2017: £11,000) in the Company's equity.

Currency risk

The Company and Group take on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. This is managed through the Group entering into forward foreign exchange contracts. The Board sets limits on the level of exposure for both overnight and intra-day positions, which are monitored daily. The table below summarises the Group's exposure to foreign currency exchange rate risk at 31 December 2018. Included in the table below are the Group's assets and liabilities at carrying amounts, categorised by currency.

	GBP (£)	USD ($)	Euro (€)	Other	Total
At 31 December 2018	£000	£000	£000	£000	£000
ASSETS					
Cash and balances at central banks	405,244	30	47	4	405,325
Loans and advances to banks	8,856	13,794	19,714	11,809	54,173
Debt securities at amortised cost	243,680	99,011	-	-	342,691
Derivative financial instruments	1,655	4	3	184	1,846
Loans and advances to customers	1,169,157	16,122	39,377	-	1,224,656
Other assets	2,861	-	115	-	2,976
Financial investments	34,219	954	178	-	35,351
	1,865,672	**129,915**	**59,434**	**11,997**	**2,067,018**
LIABILITIES					
Deposits from banks	232,675	-	-	-	232,675
Derivative financial instruments	3	4	1	180	188
Deposits from customers	1,526,623	130,061	46,068	11,534	1,714,286
Other liabilities	1,782	-	-	-	1,782
Debt securities in issue	-	-	13,283	-	13,283
	1,761,083	**130,065**	**59,352**	**11,714**	**1,962,214**
Net on-balance sheet position	**104,589**	**(150)**	**82**	**283**	**104,804**
Credit commitments	67,880	-	-	-	67,880

The table below summarises the Group's exposure to foreign currency exchange risk at 31 December 2017:

At 31 December 2017	GBP (£) £000	USD ($) £000	Euro (€) £000	Other £000	Total £000
ASSETS					
Cash and balances at central banks	313,101	-	-	-	313,101
Loans and advances to banks	6,027	40,870	16,944	6,838	70,679
Debt securities held-to-maturity	170,723	56,296	-	-	227,019
Derivative financial instruments	2,525	1	25	-	2,551
Loans and advances to customers	997,025	14,912	37,332	-	1,049,269
Other assets	11,964	-	-	-	11,964
Financial investments	140	706	1,501	-	2,347
	1,501,505	**112,785**	**55,802**	**6,838**	**1,676,930**
LIABILITIES					
Deposits from banks	195,067	-	-	30	195,097
Derivative financial instruments	914	1	-	16	931
Deposits from customers	1,228,878	112,731	42,733	6,439	1,390,781
Other liabilities	1,207	-	-	-	1,207
Debt securities in issue	-	-	13,104	-	13,104
	1,426,066	**112,732**	**55,837**	**6,485**	**1,601,120**
Net on-balance sheet position	**75,439**	**53**	**(35)**	**353**	**75,810**
Credit commitments	131,963	-	-	-	131,963

Derivative financial instruments (see note 21) are in place to mitigate foreign currency risk on net exposures for each currency. A 10% strengthening of the pound against the US dollar would lead to a £5,000 increase (2017: £5,000 increase) in Group profits and equity, while a 10% weakening of the pound against the US dollar would lead to the same decrease in Group profits and equity. Similarly, a 10% strengthening of the pound against the Euro would lead to a £4,000 increase (2017: £4,000 increase) in Group profits and equity, while a 10% weakening of the pound against the Euro would lead to the same increase in Group profits and equity..

The table below summarises the Company’s exposure to foreign currency exchange rate risk at 31 December 2018:

At 31 December 2018	GBP (£) £000	Euro (€) £000	Total £000
ASSETS			
Loans and advances to banks	3,437	13,571	17,008
Financial investments	19,313	-	19,313
	22,750	**13,571**	**36,321**
LIABILITIES			
Other liabilities	1,838	-	1,838
Debt securities in issue	-	13,283	13,283
	1,838	**13,283**	**15,121**
Net on-balance sheet position	**20,912**	**288**	**21,200**

The table below summarises the Company's exposure to foreign currency exchange rate risk at 31 December 2017:

At 31 December 2017	GBP (£) £000	Euro (€) £000	Total £000
ASSETS			
Loans and advances to banks	22,734	13,369	36,103
Financial investments	140	-	140
Other assets	162	-	162
	23,036	**13,369**	**36,405**
LIABILITIES			
Other liabilities	1,840	-	1,840
Debt securities in issue	-	13,104	13,104
	1,840	**13,104**	**14,944**
Net on-balance sheet position	**21,196**	**265**	**21,461**

A 10% strengthening of the pound against the Euro would lead to £3,000 (2017: £3,000) decrease in the Company profits and equity, conversely a 10% weakening of the pound against the Euro would lead to the same increase in the Company profits and equity.

Interest rate risk

Interest rate risk is the potential adverse impact on the Company and Group's future cash flows from changes in interest rates, and arises from the differing interest rate risk characteristics of the Company and Group's assets and liabilities. In particular, fixed rate savings and borrowing products expose the Group to the risk that a change in interest rates could cause either a reduction in interest income or an increase in interest expense relative to variable rate interest flows. The Group seeks to "match" interest rate risk on either side of the Statement of Financial Position. However, this is not a perfect match and interest rate risk is present in: Money market transactions of a fixed rate nature, fixed rate loans, fixed rate savings accounts and floating rate products dependent on when they re-price at a future date.

Interest rate risk is measured throughout the maturity bandings of the book on a parallel shift scenario for a 200 basis points movement. Interest rate risk is managed to limit value at risk to be less than £1.5m. The current position of the balance sheet is such that it results in a favourable impact on the economic value of equity of £1.3m (2017: £0.8m) for a positive 200bps shift and an adverse impact of £1.4m (2017: £0.8m) for a negative 200bps movement. The negative movement is capped at the Bank of England base rate of 75bps (2017: 50bps), which result in a negative impact of £0.5m (2017: £0.3m). The Company has no fixed rate exposures, but an upward change of 50bps on variable rates would increase pre-tax profits and equity by £10,000 (2017: increase pre-tax profits and equity by £10,000).

The following tables summarise the re-pricing periods for the assets and liabilities in the Company and Group, including derivative financial instruments which are principally used to reduce exposure to interest rate risk. Items are allocated to time bands by reference to the earlier of the next contractual interest rate re-price and the maturity date.

Group **As at 31 December 2018**	Within 3 months £000	More than 3 months but less than 6 months £000	More than 6 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000	Non interest bearing £000	Total £000
ASSETS							
Cash and balances at central banks	405,325	-	-	-	-	-	405,325
Loans and advances to banks	54,115	-	58	-	-	-	54,173
Debt securities at amortised cost	269,026	27,846	41,896	3,923	-	-	342,691
Derivative financial instruments	304	-	-	1,542	-	-	1,846
Loans and advances to customers	1,030,316	6,107	17,502	170,525	206	-	1,224,656
Other assets*	-	-	-	-	-	111,131	111,131
Financial investments	-	-	-	-	-	35,351	35,351
	1,759,086	**33,953**	**59,456**	**175,990**	**206**	**146,482**	**2,175,173**
LIABILITIES							
Deposits from banks	232,675	-	-	-	-	-	232,675
Derivative financial instruments	188	-	-	-	-	-	188
Deposits from customers	1,255,488	197,785	95,868	165,145	-	-	1,714,286
Other liabilities**	-	-	-	-	-	18,785	18,785
Debt securities in issue	13,283	-	-	-	-	-	13,283
Equity	-	-	-	-	-	195,956	195,956
	1,501,634	**197,785**	**95,868**	**165,145**	**-**	**214,741**	**2,175,173**
Impact of derivative instruments	25,762	-	-	(25,762)	-	-	
Interest rate sensitivity gap	**283,214**	**(163,832)**	**(36,412)**	**(14,917)**	**206**	**(68,259)**	
Cumulative gap	**283,214**	**119,382**	**82,970**	**68,053**	**68,259**	**-**	

* Other assets include all remaining assets in the Statement of Financial Position, which are not shown separately above.

** Other liabilities include all remaining liabilities in the Statement of Financial Position, which are not shown separately above.

Group **As at 31 December 2017**	Within 3 months £000	More than 3 months but less than 6 months £000	More than 6 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000	Non interest bearing £000	Total £000
ASSETS							
Cash and balances at central banks	313,101	-	-	-	-	-	313,101
Loans and advances to banks	61,211	579	8,889	-	-	-	70,679
Debt securities held-to-maturity	185,926	35,093	6,000	-	-	-	227,019
Derivative financial instruments	950	-	-	1,601	-	-	2,551
Loans and advances to customers	880,822	6,938	10,774	143,979	-	6,756	1,049,269
Other assets	-	-	-	-	-	188,266	188,266
Financial investments	-	-	-	-	-	2,347	2,347
	1,442,010	**42,610**	**25,663**	**145,580**	**-**	**197,369**	**1,853,232**
LIABILITIES							
Deposits from banks	195,097	-	-	-	-	-	195,097
Derivative financial instruments	931	-	-	-	-	-	931
Deposits from customers	1,061,442	162,503	109,478	57,358	-	-	1,390,781
Other liabilities	-	-	-	-	-	16,944	16,944
Debt securities in issue	13,104	-	-	-	-	-	13,104
Equity	-	-	-	-	-	236,375	236,375
	1,270,574	**162,503**	**109,478**	**57,358**	**-**	**253,319**	**1,853,232**
Impact of derivative instruments	17,824	-	-	(17,824)	-	-	
Interest rate sensitivity gap	**189,260**	**(119,893)**	**(83,815)**	**70,398**	**-**	**(55,950)**	
Cumulative gap	**189,260**	**69,367**	**(14,448)**	**55,950**	**55,950**	**-**	

* Other assets include all remaining assets in the Statement of Financial Position, which are not shown separately above.

** Other liabilities include all remaining liabilities in the Statement of Financial Position, which are not shown separately above.

Company As at 31 December 2018	Within 3 months £000	More than 3 months but less than 6 months £000	More than 6 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000	Non interest bearing £000	Total £000
ASSETS							
Loans and advances to banks	16,977	-	-	-	-	31	17,008
Other assets*	-	-	-	-	-	135,035	135,035
Financial investments	-	-	-	-	-	19,313	19,313
	16,977	**-**	**-**	**-**	**-**	**154,379**	**171,356**
LIABILITIES							
Other liabilities**	-	-	-	-	-	3,324	3,324
Debt securities in issue	13,283	-	-	-	-	-	13,283
Equity	-	-	-	-	-	154,749	154,749
	13,283	**-**	**-**	**-**	**-**	**158,073**	**171,356**
Interest rate sensitivity gap	**3,694**	**-**	**-**	**-**	**-**	**(3,694)**	
Cumulative gap	**3,694**	**3,694**	**3,694**	**3,694**	**3,694**	**-**	

* Other assets include all remaining assets in the Statement of Financial Position, which are not shown separately above.

** Other liabilities include all remaining liabilities in the Statement of Financial Position, which are not shown separately above.

Company As at 31 December 2017	Within 3 months £000	More than 3 months but less than 6 months £000	More than 6 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000	Non interest bearing £000	Total £000
ASSETS							
Loans and advances to banks	35,944	-	-	-	-	159	36,103
Other assets*	-	-	-	-	-	103,855	103,855
Financial investments	-	-	-	-	-	140	140
	35,944	**-**	**-**	**-**	**-**	**104,154**	**140,098**
LIABILITIES							
Other liabilities**	-	-	-	-	-	3,293	3,293
Debt securities in issue	13,104	-	-	-	-	-	13,104
Equity	-	-	-	-	-	123,701	123,701
	13,104	**-**	**-**	**-**	**-**	**126,994**	**140,098**
Interest rate sensitivity gap	**22,840**	**-**	**-**	**-**	**-**	**(22,840)**	
Cumulative gap	**22,840**	**22,840**	**22,840**	**22,840**	**22,840**	**-**	

* Other assets include all remaining assets in the Statement of Financial Position, which are not shown separately above.

** Other liabilities include all remaining liabilities in the Statement of Financial Position, which are not shown separately above.

(d) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. The liquidity requirements of the Group are met through withdrawing funds from its Bank of England Reserve Account to cover any short-term fluctuations and longer term funding to address any structural liquidity requirements.

The Group has formal governance structures in place to manage and mitigate liquidity risk on a day to day basis. The Board of AL sets and approves the liquidity risk management strategy. The Assets and Liabilities Committee ("ALCO"), comprising senior executives of the Group, monitors liquidity risk. Key liquidity risk management information is reported by the finance teams and monitored by the Chief Executive Officer and Finance Director on a daily basis. The ALCO meets monthly to review liquidity risk against set thresholds and risk indicators including early warning indicators, liquidity risk tolerance levels and Individual Liquidity Adequacy Assessment Process ("ILAAP") metrics.

The PRA requires the Board to ensure that the Group has adequate levels of liquidity resources and a prudent funding profile, and that it comprehensively manages and controls liquidity and funding risks. The Group maintains deposits placed at the Bank of England, and highly liquid unencumbered assets that can be called upon to create sufficient liquidity to meet liabilities on demand, particularly in a period of liquidity stress.

Arbuthnot Latham & Co., Limited ("AL") has a Board approved ILAAP, and maintains liquidity buffers in excess of the minimum requirements. The ILAAP is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. At a minimum, the ILAAP is undated annually. The Liquidity Coverage Ratio ("LCR") regime has applied to the Group from 1 October 2015, requiring management of net 30 day cash outflows as a proportion of high quality liquid assets. The actual LCR at 282% (2017: 222%) has significantly exceeded the regulatory minimum of 90% (2017: 80%) throughout the year.

The Group is exposed to daily calls on its available cash resources from current accounts, maturing deposits and loan draw-downs. The Group maintains significant cash resources to meet all of these needs as they fall due. The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Group. It is unusual for banks to be completely matched, as transacted business is often of uncertain term and of different types.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest bearing liabilities as they mature are important factors in assessing the liquidity of the Group and its exposure to changes in interest rates.

The tables below show the undiscounted contractual cash flows of the Group's financial liabilities and assets as at 31 December 2018:

At 31 December 2018	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial liability by type						
Non-derivative liabilities						
Deposits from banks	232,675	(232,675)	(232,675)	-	-	-
Deposits from customers	1,714,286	(1,719,600)	(1,274,190)	(355,512)	(89,898)	-
Other liabilities	1,782	(1,782)	(1,775)	-	-	(7)
Debt securities in issue	13,283	(19,431)	(90)	(271)	(1,447)	(17,623)
Issued financial guarantee contracts	-	(1,744)	(1,744)	-	-	-
Unrecognised loan commitments	-	(86,002)	(86,002)	-	-	-
	1,962,026	**(2,061,234)**	**(1,596,476)**	**(355,783)**	**(91,345)**	**(17,630)**
Derivative liabilities						
Risk management:	188					
- Outflows	-	(188)	(188)	-	-	-
	188	**(188)**	**(188)**	**-**	**-**	**-**

At 31 December 2018	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial asset by type						
Non-derivative assets						
Cash and balances at central banks	405,325	405,325	405,325	-	-	-
Loans and advances to banks	54,173	54,173	54,115	58	-	-
Debt securities at amortised cost	342,691	346,694	129,604	101,449	115,641	-
Loans and advances to customers	1,224,656	1,382,857	46,646	173,077	1,038,465	124,669
Other assets	2,976	2,976	2,976	-	-	-
Financial investments	35,351	35,351	16,038	-	19,313	-
	2,065,172	**2,227,376**	**654,704**	**274,584**	**1,173,419**	**124,669**
Derivative assets						
Risk management:	1,846					
- Inflows	-	1,846	-	-	-	1,846
	1,846	**1,846**	**-**	**-**	**-**	**1,846**

The tables below show the undiscounted contractual cash flows of the Group's financial liabilities and assets as at 31 December 2017:

At 31 December 2017	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial liability by type						
Non-derivative liabilities						
Deposits from banks	195,097	(195,097)	(195,097)	-	-	-
Deposits from customers	1,390,781	(1,395,770)	(1,040,893)	(293,425)	(61,452)	-
Other liabilities	1,207	(1,207)	(1,207)	-	-	-
Debt securities in issue	13,104	(19,381)	(87)	(262)	(1,395)	(17,637)
Issued financial guarantee contracts	-	(2,976)	(2,976)	-	-	-
Unrecognised loan commitments	-	(131,963)	(131,963)	-	-	-
	1,600,189	**(1,746,394)**	**(1,372,223)**	**(293,687)**	**(62,847)**	**(17,637)**
Derivative liabilities						
Risk management:	931					
- Outflows	-	(931)	(931)	-	-	-
	931	**(931)**	**(931)**	**-**	**-**	**-**

At 31 December 2017	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial asset by type						
Non-derivative assets						
Cash and balances at central banks	313,101	313,101	313,101	-	-	-
Loans and advances to banks	70,679	70,679	61,211	579	8,889	-
Debt securities held-to-maturity	227,019	227,166	22,886	101,277	103,003	-
Loans and advances to customers	1,049,269	1,187,665	126,689	121,493	800,091	139,392
Other assets	11,964	11,964	11,964	-	-	-
Financial investments	2,347	2,347	2,335	-	12	-
	1,674,379	**1,812,922**	**538,186**	**223,349**	**911,995**	**139,392**
Derivative assets						
Risk management:	2,551					
- Inflows	-	2,551	-	-	-	2,551
	2,551	**2,551**	**-**	**-**	**-**	**2,551**

The table below sets out the components of the Group's liquidity reserves:

Liquidity reserves	31 December 2018 Amount £000	31 December 2018 Fair value £000	31 December 2017 Amount £000	31 December 2017 Fair value £000
Cash and balances at central banks	405,325	405,325	313,101	313,101
Loans and advances to banks	54,173	54,173	70,679	70,679
Debt securities at amortised cost / held-to-maturity	342,691	344,001	227,019	227,951
Undrawn credit lines	10,000	10,000	10,000	10,000
	812,189	**813,499**	**620,799**	**621,731**

Assets pledged as collateral or encumbered

The total financial assets recognised in the statement of financial position that had been pledged as collateral for liabilities at 31 December 2018 were £308.9m (2017: £208.7m).

Financial assets are pledged as collateral as part of sales and repurchases, securities borrowing and securitisation transactions under terms that are usual and customary for such activities. In addition, as part of these transactions, the Group has received collateral that it is permitted to sell or repledge in the absence of default.

The table below analyses the contractual cash flows of the Company's financial liabilities and assets as at 31 December 2018:

At 31 December 2018	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial liability by type						
Non-derivative liabilities						
Other liabilities	1,838	(1,838)	(248)	-	-	(1,590)
Issued financial guarantee contracts	13,283	(19,431)	(90)	(271)	(1,447)	(17,623)
	15,121	**(21,269)**	**(338)**	**(271)**	**(1,447)**	**(19,213)**

At 31 December 2018	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial asset by type						
Non-derivative assets						
Loans and advances to banks	17,008	17,008	17,008	-	-	-
Financial investments	19,313	19,313	-	-	19,313	-
	36,321	**36,321**	**17,008**	**-**	**19,313**	**-**

The table below analyses the contractual cash flows of the Company's financial liabilities and assets as at 31 December 2017:

At 31 December 2017	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial liability by type						
Non-derivative liabilities						
Other liabilities	1,840	(1,840)	(251)	-	-	(1,589)
Debt securities in issue	13,104	(19,381)	(87)	(262)	(1,395)	(17,637)
	14,944	**(21,221)**	**(338)**	**(262)**	**(1,395)**	**(19,226)**

At 31 December 2017	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial asset by type						
Non-derivative assets						
Loans and advances to banks	36,103	36,103	36,103	-	-	-
Financial investments	140	140	128	-	12	-
Other assets	162	162	162	-	-	-
	36,405	**36,405**	**36,393**	**-**	**12**	**-**

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature are important factors in assessing the liquidity of the Group and its exposure to changes in interest rates and exchange rates.

Fiduciary activities

The Group provides investment management and advisory services to third parties, which involve the Group making allocation and purchase and sale decisions in relation to a wide range of financial instruments. Those assets that are held in a fiduciary capacity are not included in these financial statements. These services give rise to the risk that the Group may be accused of maladministration or underperformance. At the balance sheet date, the Group had investment management accounts amounting to approximately £985m (2017: £1,044m). Additionally, the Group provides investment advisory services.

(e) Financial assets and liabilities

The tables below set out the Group's financial assets and financial liabilities into their respective classifications:

At 31 December 2018	FVPL £000	FVOCI £000	Amortised cost £000	Total carrying amount £000	Fair value £000
ASSETS					
Cash and balances at central banks	-	-	405,325	405,325	405,325
Loans and advances to banks	-	-	54,173	54,173	54,173
Debt securities at amortised cost	-	-	342,691	342,691	344,001
Derivative financial instruments	1,846	-	-	1,846	1,846
Loans and advances to customers	-	-	1,224,656	1,224,656	1,187,408
Other assets	2,976	-	-	2,976	2,976
Financial investments	165	35,186	-	35,351	35,351
	4,987	**35,186**	**2,026,845**	**2,067,018**	**2,031,080**
LIABILITIES					
Deposits from banks	-	-	232,675	232,675	232,675
Derivative financial instruments	188	-	-	188	188
Deposits from customers	-	-	1,714,286	1,714,286	1,714,286
Other liabilities	1,782	-	-	1,782	1,782
Debt securities in issue	-	-	13,283	13,283	13,283
	1,970	**-**	**1,960,244**	**1,962,214**	**1,962,214**

At 31 December 2017	Fair value through profit or loss £000	Held-to-maturity £000	Loans and receivables £000	Available-for-sale £000	Liabilities at amortised cost £000	Total carrying amount £000	Fair value £000
ASSETS							
Cash and balances at central banks	-	-	313,101	-	-	313,101	313,101
Loans and advances to banks	-	-	70,679	-	-	70,679	70,679
Debt securities held-to-maturity	-	227,019	-	-	-	227,019	227,951
Derivative financial instruments	2,551	-	-	-	-	2,551	2,551
Loans and advances to customers	-	-	1,049,269	-	-	1,049,269	1,022,816
Other assets	-	-	11,964	-	-	11,964	11,964
Financial investments	-	-	-	2,347	-	2,347	2,347
	2,551	**227,019**	**1,445,013**	**2,347**	**-**	**1,676,930**	**1,651,409**
LIABILITIES							
Deposits from banks	-	-	-	-	195,097	195,097	195,097
Derivative financial instruments	931	-	-	-	-	931	931
Deposits from customers	-	-	-	-	1,390,781	1,390,781	1,390,781
Other liabilities	-	-	1,207	-	-	1,207	1,207
Debt securities in issue	-	-	-	-	13,104	13,104	13,104
	931	**-**	**1,207**	**-**	**1,598,982**	**1,601,120**	**1,601,120**

The Group's accounting policies on the classification of financial instruments under IFRS 9 are set out in Note 3.8. The application of these policies resulted in reclassifications set out in Note 2(f).

Valuation of financial instruments
The Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions. If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same for which market observable prices exist, net present value and discounted cash flow analysis. The objective of valuation techniques is to determine the fair value of the financial instrument at the reporting date as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. In the event that fair values of assets and liabilities cannot be reliably measured, they are carried at cost.

The Group measures fair value using the following fair value hierarchy that reflects the significance of the inputs used in making measurements:

- Level 1: Quoted prices in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.
- Level 3: Inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads assists in the judgement as to whether a market is active. If, in the opinion of management, a significant proportion of the instrument's carrying amount is driven by unobservable inputs, the instrument in its entirety is classified as valued using significant unobservable inputs. 'Unobservable' in this context means that there is little or no current market data available from which to determine the level at which an arm's length transaction would be likely to occur. It generally does not mean that there is no market data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used).

The tables below analyse financial instruments measured at fair value by the level in the fair value hierarchy into which the measurement is categorised:

At 31 December 2018	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Derivative financial instruments	-	1,846	-	1,846
Financial investments	34,223	-	1,128	35,351
	34,223	**1,846**	**1,128**	**37,197**
LIABILITIES				
Derivative financial instruments	-	188	-	188
	-	**188**	**-**	**188**

At 31 December 2017	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Derivative financial instruments	-	2,551	-	2,551
Financial investments	144	-	2,203	2,347
	144	**2,551**	**2,203**	**4,898**
LIABILITIES				
Derivative financial instruments	-	931	-	931
	-	**931**	**-**	**931**

There were no transfers between level 1 and level 2 during the year.

The following table reconciles the movement in level 3 financial instruments measured at fair value (financial investments) during the year:

Movement in level 3	2018 £000	2017 £000
At 1 January	2,203	2,012
Consideration received	163	-
Disposals	(1,403)	-
Movements recognised in Other Comprehensive Income	135	136
Movements recognised in the Income Statement	30	55
At 31 December	**1,128**	**2,203**

Secure Trust bank investment
The Group currently holds equity shares in Secure Trust Bank plc, valued at £34.2m (2017: £nil). The shares are recognised at fair value using quoted prices on the London Stock Exchange.

Visa Inc. investment
Arbuthnot Latham currently holds preference shares in Visa Inc., valued at £863k (2017: £706k) as at 31 December 2018. These shares have been valued at their future conversion value into Visa Inc. common stock. The valuation includes a 31% haircut, comprising 25% due to a contingent liability disclosed in Visa Europe's accounts in relation to litigation and 6% based on a liquidity discount.

Investment in overseas property company
Arbuthnot Latham currently holds a debt and equity investment classified as FVPL in a property company which owns an office building through its 100% owned subsidiary. During 2018 the subsidiary company was sold under the terms of the sale agreement the buyer agreed to purchase 100% of the share capital and reimburse all outstanding loans. The proceeds of the sale have been distributed to the investors, except for the amount withheld for the general and specific warranties (which will be released in three instalments at 18 month intervals) included as a condition of the sale agreement. A distribution of £1.6m has been received and a gain of £75k has

been recognised in profit or loss during the year. The investment has been valued at £165k as at 31 December 2018. The investment has been valued as the discounted consideration outstanding less 11% hair cut for the warranties.

Hetz Ventures, L.P.
Arbuthnot Latham currently holds an equity investment in Hetz Ventures, L.P. which was a launched in January 2018 with the primary objective to generate attractive risk-adjusted returns for its Partners, principally through long-term capital appreciation, by making, holding and disposing of equity and equity-related investments in early stage revenue generating Israeli technology companies, primarily in cyber, fin-tech and the disruptive software sectors. The company has committed to a capital contribution of USD $1.0m of the total closing fund capital of USD$55.0m. At 31 December 2018 the company had made capital contributions into the Fund of $168k.

The investment is classified as FVOCI and is valued at fair value by Hetz Ventures, L.P. at £0.1m as at 31 December 2018. As at year end the fair value is deemed to be cost less management fees due to the immature stage of investments that have been made by the Fund.

The tables below analyse financial instruments not measured at fair value by the level in the fair value hierarchy:

At 31 December 2018	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Cash and balances at central banks	-	405,325	-	405,325
Loans and advances to banks	-	54,173	-	54,173
Debt securities at amortised cost	-	342,691	-	342,691
Loans and advances to customers*	-	996,198	228,458	1,224,656
Other assets	-	-	2,976	2,976
	-	**1,798,387**	**231,434**	**2,029,821**
LIABILITIES				
Deposits from banks	-	232,675	-	232,675
Deposits from customers	-	1,714,286	-	1,714,286
Other liabilities	-	-	1,782	1,782
Debt securities in issue	-	-	13,283	13,283
	-	**1,946,961**	**15,065**	**1,962,026**

* On transition to IFRS 9 on 1 January 2018, all loans on a variable rate are now recognised as Level 2 financial instruments.

At 31 December 2017	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Cash and balances at central banks	-	313,101	-	313,101
Loans and advances to banks	-	70,679	-	70,679
Debt securities held-to-maturity	-	227,019	-	227,019
Loans and advances to customers	-	-	1,049,269	1,049,269
Other assets	-	-	11,964	11,964
	-	**610,799**	**1,061,233**	**1,672,032**
LIABILITIES				
Deposits from banks	-	195,097	-	195,097
Deposits from customers	-	1,390,781	-	1,390,781
Other liabilities	-	-	1,207	1,207
Debt securities in issue	-	-	13,104	13,104
	-	**1,585,878**	**14,311**	**1,600,189**

7. Capital management

The Group's capital management policy is focused on optimising shareholder value. There is a clear focus on delivering organic growth and ensuring capital resources are sufficient to support planned levels of growth. The Board regularly reviews the capital position.

The Group's lead regulator, the Prudential Regulatory Authority ("PRA"), sets and monitors capital requirements for the Group

In accordance with the EU's Capital Requirements Directive ("CRD") and the required parameters set out in the PRA Handbook (BIPRU 2.2), the Individual Capital Adequacy Assessment Process ("ICAAP") is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. However, at a minimum, the ICAAP is updated annually as part of the business planning process. The ICAAP is a process that brings together the management framework (i.e. the policies, procedures, strategies, and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted a "Pillar I plus" approach to determine the level of capital the Group needs to hold. This method takes the Pillar I capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations delivers a sufficient capital sum adequately to cover management's anticipated risks. Where the Board considered that the Pillar I calculations did not reflect the risk, an additional capital add-on in Pillar II is applied, as per the Total Capital Requirement ("TCR") issued by the PRA. The current TCR of the Group is 9.00%.

The Group's regulatory capital is divided into two tiers:

- Tier 1 comprises mainly shareholders' funds and revaluation reserves, after deducting goodwill, other intangible assets and the deduction for a significant investment in a financial institution (STB). The portion of the investment representing up to 10% of ABG's Tier 1 is added back to capital resources and then risk weighted at 250%, while anything above the 10% is therefore deducted.
- Lower Tier 2 comprises qualifying subordinated loan capital. Lower Tier 2 capital cannot exceed 50% of Tier 1 capital.

The following table shows the regulatory capital resources as managed by the Group:

	2018 £000	2017 £000
Tier 1		
Share capital	153	153
Retained earnings*	209,083	237,171
Deduction for significant investment*	(34,219)	(83,804)
Add back 10% of CET1 (risk weighted at 250%)	18,137	22,038
Capital redemption reserve	20	20
IFRS 9 - Transitional add back	1,986	-
Treasury shares	(1,131)	(1,131)
Deduction for goodwill	(5,202)	(5,202)
Deduction for other intangibles	(11,336)	(10,793)
Fair value/Available-for-sale reserve*	(12,169)	162
Prudent valuation deduction	(38)	-
Total tier 1 capital resources	**165,284**	**158,614**
Tier 2		
Debt securities in issue	13,283	13,104
Total tier 2 capital resources	**13,283**	**13,104**
Total tier 1 & tier 2 capital resources	**178,567**	**171,718**
Core Tier 1 capital ratio (Net Core Tier 1 capital/Basel III Total Risk Exposure)	**15.9%**	**17.3%**
Total Capital Ratio (Capital/Basel III Total Risk Exposure)	**17.2%**	**18.8%**

*The reduced deduction for significant investment is due to the fall in the fair value of the investment in STB, which is now accounted for as a financial asset at fair value through OCI. The initial fair value adjustment went through retained earnings as part of the net current year loss recorded and fair value losses since then are reflected in the fair value reserve.

The ICAAP includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. The PRA sets TCR for each UK bank calibrated by reference to its Capital Resources Requirement, broadly equivalent to 8 percent of risk weighted assets and thus representing the capital required under Pillar I of the Basel III framework. The ICAAP is a key input into the PRA's TCR setting process, which addresses the requirements of Pillar II of the Basel III framework. The PRA's approach is to monitor the available capital resources in relation to the TCR requirement. The Group maintains an extra internal buffer and capital ratios are reviewed on a monthly basis to ensure that external requirements are adhered to. All regulated entities have complied with all of the externally imposed capital requirements to which they are subject.

Pillar III complements the minimum capital requirements (Pillar I) and the supervisory review process (Pillar II). Its aim is to encourage market discipline by developing a set of disclosure requirements which will allow market participants to assess key pieces of information on a firm's capital, risk exposures and risk assessment processes. Our Pillar III disclosures for the year ended 31 December 2018 are published as a separate document on the Group website under Investor Relations (Announcements & Shareholder Info).

8. Net interest income

	2018	2017
	£000	£000
Cash and balances at central banks	2,264	801
Loans and advances to banks	2,703	258
Debt securities at amortised cost / held-to-maturity	3,303	1,353
Loans and advances to customers	57,020	45,015
	65,290	**47,427**
Deposits from banks	(1,517)	(35)
Deposits from customers	(8,224)	(5,939)
Debt securities in issue	(366)	(360)
Interest expense	**(10,107)**	**(6,334)**
Net interest income	**55,183**	**41,093**

9. Fee and commission income

Fee and commission income is disaggregated below and includes a total for fees in scope of IFRS 15, Revenues from Contracts with Customers:

Group At 31 December 2018	Private Banking	Commercial Banking	RAF	All other divisions	Total
	£000	£000	£000	£000	£000
Banking commissions	747	617	151	220	1,735
Foreign exchange fees	558	232	-	537	1,327
Investment management fees	8,177	-	-	1	8,178
Wealth planning fees	1,404	-	-	312	1,716
Total fee and commission income	**10,886**	**849**	**151**	**1,070**	**12,956**

Group At 31 December 2017	Private Banking	Commercial Banking	RAF	All other divisions	Total
	£000	£000	£000	£000	£000
Banking and services fees	1,487	374	-	402	2,263
Foreign exchange fees	545	161	-	356	1,062
Investment management fees	7,870	-	-	17	7,887
Wealth planning fees	2,593	-	-	-	2,593
Total fee and commission income	**12,495**	**535**	**-**	**775**	**13,805**

10. Net impairment loss on financial assets

	2018 £000	2017 £000
Net Impairment losses on loans and advances to customers	2,731	394
Of which:		
Stage 1	821	-
Stage 3	1,910	-
	2,731	**394**

The provision charge in 2018 has increased largely due to the transition to IFRS 9, if 2017 was restated on an IFRS 9 basis the charge would have been £3.0m.

During the year, the Group recovered £41k (2017: £116k) of loans which had previously been written off.

11. Other income

Other income includes a fair value adjustment of £2.6m (2017: £nil), to the contingent consideration for the acquisition of Renaissance Asset Finance Ltd. The fair value adjustment is based on management's assessment of the underlying performance of the business and reflects a reduction in the estimated future liability payable under the sale and purchase agreement.

Other items reflected in other income include rental income from the investment properties (see Note 31) of £2.6m (2017: £2.1m), premises recharges of £0.7m (2017: £0.7m) to STB for office space occupied and dividends received on the shares held in STB of £0.7m, since de-recognition as an associate undertaking.

12. Operating expenses

Operating expenses comprise:	2018 £000	2017 £000
Staff costs, including Directors:		
Wages, salaries and bonuses	37,051	30,937
Social security costs	4,176	3,576
Pension costs	1,842	1,558
Share based payment transactions (note 39)	(318)	189
Amortisation of intangibles (note 28)	1,752	1,036
Depreciation (note 30)	1,122	1,508
Financial Services Compensation Scheme Levy	113	190
Operating lease rentals	3,143	3,087
Operating expenses for investment property	282	230
Acquisitions costs	378	108
Other administrative expenses	15,441	12,302
Total operating expenses from continuing operations	**64,982**	**54,721**

Details on Directors remuneration are disclosed in the Remuneration Report on page ##RREP.

Remuneration of the auditor and its associates, excluding VAT, was as follows:	2018 £000	2017 £000
Fees payable to the Company's auditor for the audit of the Company's annual accounts	112	105
Fees payable to the Company's auditor and its associates for other services:		
Audit of the accounts of subsidiaries	323	221
Audit related assurance services	160	85
Other assurance services	10	17
Other non-audit services	10	-
Total fees payable	**615**	**428**

13. Income tax expense

	2018 £000	2017 £000
United Kingdom corporation tax at 19% (2017: 19.25%)		

Current taxation		
Corporation tax charge - current year	620	472
Corporation tax charge - adjustments in respect of prior years	132	(141)
	752	**331**
Deferred taxation		
Origination and reversal of temporary differences	350	(135)
Adjustments in respect of prior years	19	252
	369	**117**
Income tax expense	**1,121**	**448**
Tax reconciliation		
Profit before tax	6,780	2,534
Tax at 19% (2017: 19.25%)	1,288	488
Permanent difference - Tax on associate income	(854)	(429)
Other permanent differences	536	277
Tax rate change	-	1
Prior period adjustments	151	111
Corporation tax charge for the year	**1,121**	**448**

Permanent differences mainly relate to associate income which is reflected after tax.

The tax charge on discontinuing operations is disclosed in note 14.

On 26 October 2015 the Government substantively enacted a reduction in the UK corporation tax rate from 20% to 19% (effective from 1 April 2017). An additional reduction to 17% (effective from 1 April 2020) was substantively enacted on 6 September 2016. This will reduce the Bank's future current tax charge accordingly.

14. Discontinued operations

The profit after tax from discontinued operations is made up as follows:

Discontinued operations	Year ended 31 December 2018 £000	Year ended 31 December 2017 £000
Profit after tax from discontinued operations - STB associate income (up to 8 August 2018)	2,971	4,437
Loss after tax on de-recognition of STB	(28,663)	-
Loss after tax from discontinued operations	**(25,692)**	**4,437**

15. Average number of employees

	2018	2017
Private Banking	135	136
Commercial Banking	46	38
RAF	26	13
All Other Divisions	182	161
Group Centre	17	17
	406	**365**

16. Earnings per ordinary share

Basic

Basic earnings per ordinary share are calculated by dividing the profit after tax attributable to equity holders of the Company by the weighted average number of ordinary shares 14,889,048 (2017: 14,852,763) in issue during the year.

Diluted

Diluted earnings per ordinary share are calculated by dividing the dilutive profit after tax attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year, as well as the number of dilutive share options in issue during the year. The number of dilutive share options in issue at the year end was nil (2017: nil).

Profit & dilutive profit attributable	2018 £000	2017 £000
Total (loss) / profit after tax attributable to equity holders of the Company	(20,033)	6,523
Profit after tax from continuing operations attributable to equity holders of the Company	5,659	2,086
(Loss) / profit after tax from discontinued operations attributable to equity holders of the Company	(25,692)	4,437

Basic & Diluted Earnings per share	2018 p	2017 p
Total Basic Earnings per share	(134.5)	43.9
Basic Earnings per share from continuing operations	38.0	14.0
Basic Earnings per share from discontinued operations	(172.5)	29.9

17. Cash and balances at central banks

Group	2018 £000	2017 £000
Cash and balances at central banks	**405,325**	**313,101**

All assets have been assessed as Stage 1 at 1 January and 31 December 2018, with immaterial ECL.

Surplus funds are mainly held in the Bank of England reserve account, with the remainder held in certificates of deposit, fixed rate notes and money market deposits in highly rated banks (the majority held in UK clearing banks).

18. Loans and advances to banks

Group	2018 £000	2017 £000
Placements with banks included in cash and cash equivalents (note 41)	**54,173**	**70,679**

The table below presents an analysis of loans and advances to banks by rating agency designation as at 31 December, based on Moody's long term ratings:

Group	2018 £000	2017 £000
Aaa	709	-
Aa3	42,230	39,871
A1	8,880	20,553
A2	1,906	10,012
A3	10	-
Baa1	430	235
Unrated	8	8
	54,173	**70,679**

None of the loans and advances to banks are past due (2017: £nil). ECL has been assessed as immaterial.

Company	2018 £000	2017 £000
Placements with banks included in cash and cash equivalents (note 41)	**17,008**	**36,103**

Loans and advances to banks include bank balances of £17.0m (2017: £36.1m) with Arbuthnot Latham & Co., Ltd.

19. Debt securities at amortised cost / held-to-maturity

Debt securities represent certificates of deposit.

The movement in debt securities may be summarised as follows:

Group	2018 £000	2017 £000
At 1 January	227,019	107,300
Exchange difference	4,783	(951)
Additions	467,772	211,080
Redemptions	(356,883)	(90,410)
At 31 December	**342,691**	**227,019**

The table below presents an analysis of debt securities by rating agency designation at 31 December, based on Moody's long term ratings:

Group	2018 £000	2017 £000
Aaa	76,281	100,106
Aa1	84,218	51,389
Aa2	32,325	5,946
Aa3	56,046	18,384
A1	75,657	18,187
A2	18,164	-
A3	-	33,007
	342,691	**227,019**

None of the debt securities are past due (2017: £nil). ECL has been assessed as immaterial.

20. Assets classified as held for sale

	Group	
	2018 £000	2017 £000
Seed capital investments held for sale	-	-
Repossessed property held for sale	8,002	2,915
	8,002	**2,915**

Seed capital investments held for sale

The Group considers itself a sponsor of an investment fund when it facilitates the establishment of a fund in which the Group is the investment manager. The Group ordinarily provides seed capital in order to provide initial scale and facilitate marketing of the funds to third-party investors. The fund is then financed through the issue of units to investors. Aggregate interests held by the Group include seed capital, management fees and performance fees. The Group generates management and performance fee income from managing the assets on behalf of third-party investors.

The Group has an investment of £nil (2017: £1) in the share capital of the SPV created to administer the fund. At 31 December 2018, the Group has a receivable of £nil (2017: £6.8m) from the SPV, which is reflected in Note 24.

In 2017, the Fund was classified as held for sale, the criteria required for this classification have not been met in 2018 and therefore has been consolidated in 2018.

Repossessed property held for sale

In the prior year, a property in Spain held as collateral on a loan was repossessed. As at the time of repossession, it was expected that the property would be sold in 12 months, it was recognised as held for sale. A sale was not possible within during the year, due to factors outside of the Group’s control, however as a sale is assessed to be probable within 12 months, it has been recognised as held for sale with a carrying value of £3.1m (2017: £2.9m)

During the year, a further property in Spain held as collateral on a loan, valued at £4.9m at year end was repossessed. The Group's policy is to pursue timely realisation of the collateral in an orderly manner. The property is recognised as an asset held for sale.

All repossessed property is expected to be sold within 12 months.

21. Derivative financial instruments

	2018			2017		
	Contract/ notional amount	Fair value assets	Fair value liabilities	Contract/ notional amount	Fair value assets	Fair value liabilities
Group	£000	£000	£000	£000	£000	£000
Currency swaps	4,929	192	188	9,614	950	931
Interest rate swaps	25,762	112	-	17,824	-	-
Structured notes	1,607	1,542	-	1,607	1,601	-
	32,298	**1,846**	**188**	**29,045**	**2,551**	**931**

All assets have been assessed as Stage 1 as at 1 January and 31 December 2018, with immaterial ECL.

The principal derivatives used by the Group are over the counter exchange rate contracts. Exchange rate related contracts include currency swaps and interest rate swaps.

A forward foreign exchange contract is an agreement to buy or sell a specified amount of foreign currency on a specified future date at an agreed rate. Currency swaps generally involve the exchange of interest payment obligations denominated in different currencies; exchange of principal can be notional or actual. The currency swaps are settled net and therefore the fair value is small in comparison to the contract/notional amount. Interest rate swaps are used to hedge against the Profit or Loss impact resulting from the movement in interest rates, due to some exposures having fixed rate terms.

Also included in derivative financial instruments are structured notes. The Group invested in the structured notes, which are maturing in 2021.

The Group only uses investment graded banks as counterparties for derivative financial instruments. None of the contracts are collateralised.

The table below presents an analysis of derivative financial instruments contract/notional amounts by rating agency designation of counterparty bank at 31 December, based on Moody's long term ratings:

	2018	2017
Group	£000	£000
A1	29,601	26,521
A2	2,635	2,524
Baa1	62	-
	32,298	**29,045**

22. Loans and advances to customers

Analyses of loans and advances to customers:

	2018				
	IAS 39	Stage 1	Stage 2	Stage 3	Total
Group	£000	£000	£000	£000	£000
At 31 December 2017	1,050,631	-	-	-	1,050,631
IFRS 9 reclassification into Stages	(1,050,631)	992,252	29,502	28,877	-
Gross loans and advances at 1 January 2018	**-**	**992,252**	**29,502**	**28,877**	**1,050,631**
Originations		458,825	-	-	458,825
Repayments and write-offs		(266,890)	(8,809)	(2,526)	(278,225)
Transfer to Stage 1		7,975	(7,975)		-
Transfer to Stage 2		(27,929)	28,975	(1,046)	-
Transfer to Stage 3		(3,109)	(8,993)	12,102	-
Gross loans and advances at 31 December 2018	**-**	**1,161,124**	**32,700**	**37,407**	**1,231,231**
Less allowances for ECLs (see Note 23)	-	(1,606)	(8)	(4,961)	(6,575)
Net loans and advances at 31 December 2018	**-**	**1,159,518**	**32,692**	**32,446**	**1,224,656**

	2017				
	IAS 39	Stage 1	Stage 2	Stage 3	Total
Group	£000	£000	£000	£000	£000
Gross loans and advances at 31 December 2017	**1,050,631**	**-**	**-**	**-**	**1,050,631**
Less allowances for impairments (see Note 23)	(1,362)	-	-	-	(1,362)
Net loans and advances at 31 December 2017	**1,049,269**	**-**	**-**	**-**	**1,049,269**

Comparative data for 2017 has been prepared under IAS 39. For a maturity profile of loans and advances to customers, refer to note 6.

Loans and advances to customers by division (net of ECL / impairments):

	2018				
	Private Banking	Commercial Banking	RAF	All Other Divisions	Total
Group	£000	£000	£000	£000	£000
Stage 1	618,486	431,630	84,276	25,126	1,159,518
Stage 2	20,034	11,478	1,180	-	32,692
Stage 3	31,944	-	502	-	32,446
At 31 December 2018	**670,464**	**443,108**	**85,958**	**25,126**	**1,224,656**

	2017				
	Private Banking	Commercial Banking	RAF	All Other Divisions	Total
Group	£000	£000	£000	£000	£000
At 31 December 2017	**650,245**	**305,055**	**71,265**	**22,704**	**1,049,269**

Analyses of past due loans and advances to customers by division:

	2018				
	Private Banking	Commercial Banking	RAF	All Other Divisions	Total
Group	£000	£000	£000	£000	£000
Up to 30 days	47,766	20,784	2,519	-	71,069
Stage 1	47,766	20,784	2,078	-	70,628
Stage 2	-	-	154	-	154
Stage 3	-	-	287	-	287
30 - 60 days	662	2,300	775	-	3,737
Stage 2	662	2,300	565	-	3,527
Stage 3	-	-	210	-	210
60 - 90 days	385	4,177	297	-	4,859
Stage 2	385	4,177	175	-	4,737
Stage 3	-	-	122	-	122
Over 90 days	49,415	-	546	-	49,961
Stage 2	12,901	-	272	-	13,173
Stage 3	36,514	-	274	-	36,788
At 31 December	**98,228**	**27,261**	**4,137**	**-**	**129,626**

	2017				
	Private Banking	Commercial Banking	RAF	All Other Divisions	Total
Group	£000	£000	£000	£000	£000
Up to 30 days	90,527	24,599	-	-	115,126
30 - 60 days	11,043	-	-	-	11,043
60 - 90 days	5,078	-	-	-	5,078
At 31 December	**106,648**	**24,599**	**-**	**-**	**131,247**

Prior year numbers are presented under IAS 39 and therefore has no Staging.

Loans and advances to customers include finance lease receivables as follows:

Group	2018 £000	2017 £000
Gross investment in finance lease receivables:		
- No later than 1 year	36,609	28,911
- Later than 1 year and no later than 5 years	62,541	53,766
- Later than 5 years	214	-
	99,364	82,677
Unearned future finance income on finance leases	(13,406)	(11,412)
Net investment in finance leases	**85,958**	**71,265**
The net investment in finance leases may be analysed as follows:		
- No later than 1 year	30,657	23,170
- Later than 1 year and no later than 5 years	55,095	48,095
- Later than 5 years	206	-
	85,958	**71,265**

(b) Loans and advances renegotiated

Restructuring activities include external payment arrangements, modification and deferral of payments. Following restructuring, a previously overdue customer account is reset to a normal status and managed together with other similar accounts. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue. These policies are kept under continuous review. Renegotiated loans that would otherwise be past due or impaired totalled £nil (2017: £nil).

(c) Collateral held

Collateral is measured at fair value less costs to sell. Most of the loans are secured by property. The fair value of the collateral held against loans and advances in Stage 3 is £51.3m (2017: £59.4m – collateral of loans and advances recognised as impaired under IAS 39) against loans (net of ECL) of £37.4m (2017: £29.7m – loans and advances recognised as impaired under IAS 39). The weighted average loan-to-value is 72.9% (2017: 50%).

23. Allowances for impairment of loans and advances

An analysis of movements in the allowance for ECLs:

Group	IAS 39 £000	Stage 1 £000	Stage 2 £000	Stage 3 £000	Total £000
At 31 December 2017	1,362				1,362
IFRS 9 transition adjustment	2,580				2,580
Reclassification into IFRS 9 Stages	(3,942)	1,244	1,178	1,520	-
At 1 January 2018	**-**	**1,244**	**1,178**	**1,520**	**3,942**
Transfer to Stage 1		-	-	-	-
Transfer to Stage 2		(378)	378	-	-
Transfer to Stage 3		(81)	(1,548)	1,629	-
Current year charge		821	-	1,871	2,692
Adjustment due to variation in expected future cash flows		-	-	78	78
Repayments and write-offs		-	-	(137)	(137)
At 31 December 2018	**-**	**1,606**	**8**	**4,961**	**6,575**

Allowances for impairments of loans and advances - IAS 39 comparatives

Reconciliation of specific allowance for impairments:

Group	2017 £000
At 1 January	973
Impairment losses	329
On acquisition of RAF (see note 29)	51
Loans written off during the year as uncollectible	(15)
Amounts recovered during the year	(116)
At 31 December	**1,222**

Reconciliation of collective allowance for impairments:

Group	2017 £000
On acquisition of RAF (see note 29)	75
Impairment losses	65
At 31 December	**140**
Total allowance for impairments as at 31 December 2017	**1,362**

24. Other assets

Group	2018 £000	2017 £000
Trade receivables	2,976	5,208
Inventory	4,058	4,436
Receivable from investment fund held for sale	-	6,756
Prepayments and accrued income	5,682	4,224
	12,716	**20,624**

As allowed by IFRS 9, the Group utilises the practical expedient for the stage allocation of particular financial instruments which are deemed ‘low credit risk’. This practical expedient permits the Group to assume, without more detailed analysis, that the credit risk on

a financial instrument has not increased significantly since initial recognition if the financial instrument is determined to have 'low credit' at the reporting date. The Group allocates such assets to Stage 1. The low credit risk exemption is applied to Trade receivables. ECL has been assessed as immaterial.

Inventory
Land acquired through repossession of collateral which is subsequently held in the ordinary course of business with a view to develop and sell is accounted for as inventory. The land is currently in the process of being redeveloped and will ultimately be sold off as individual residential plots. The proceeds from the sale of these plots will be used to repay the outstanding loans. Pinnacle Universal is a special purpose vehicle, 100% owned by the Group, which owns this land.

Company	2018 £000	2017 £000
Trade receivables	-	3
Due from subsidiary undertakings	-	159
Prepayments and accrued income	42	37
	42	**199**

25. Financial investments

Group	2018 £000	2017 £000
Designated at fair value through profit and loss		
- Listed securities	-	128
- Debt securities	165	-
Designated at fair value through other comprehensive income		
- Listed securities	34,222	4
- Debt securities	-	1,497
- Unlisted securities	964	718
Total financial investments	**35,351**	**2,347**

Listed securities
The Group holds investments in listed securities which are valued based on quoted prices.

On 8 August 2018, ABG lost significant influence over STB. At this date the interest in associate was de-recognised and the shares held in STB were marked to market and disclosed as a financial investment. The shares were designated as FVOCI for strategic purposes. In November 2018 ABG sold 575,000 shares held in STB, reducing the shareholding from 18.64% to 15.53%. The carrying value at year end is £34.2m and £0.7m of dividends were received in the year.

Debt securities
The Group has made an investment in an unlisted special purpose vehicle, set up to acquire and enhance the value of a commercial property through its 100% owned subsidiary. During 2018 the subsidiary company was sold under the terms of the sale agreement the buyer agreed to purchase 100% of the share capital and reimburse all outstanding loans. The proceeds of the sale have been distributed o the investors, except for the amount withheld for the general and specific warranties (which will be released in three instalments at 18 month intervals included as a condition of the sale agreement. A distribution of £1.6m has been received and a gain of £0.1m has been recognised in profit or loss during the year. The investment has been valued at £0.2m as at 31 December 2018 (see note 6. (e)).

Unlisted securities
All unlisted securities have been designated as FVOCI as they are held for strategic reasons.

On 23 June 2016 Arbuthnot Latham received €1.3m cash consideration following Visa Inc.'s completion of the acquisition of Visa Europe. As part of the deal Arbuthnot Latham also received preference shares in Visa Inc., these have been valued at their future conversion value into Visa Inc. common stock. Management has assessed the fair value of the Group's investment as £863k (2017: £706k). This valuation includes a 31% haircut.

On adoption of IFRS 9 at 1 January 2018, the Group designated its investment in the security as FVOCI. Previously, this investment was classified as available for sale and measured at fair value through other comprehensive income. Dividends received during the year amounted to £7k (2017: £2k).

A further investment in an unlisted investment vehicle was a made in the year. The carrying value at year end is £100k and no dividends were received in the year.

Company	2018 £000	2017 £000
Financial investments comprise:		
- Listed securities (at fair value through OCI)	19,312	128
- Unlisted securities (at fair value through OCI)	1	12
Total financial investments	**19,313**	**140**

26. Deferred taxation

The deferred tax asset comprises:

Group	2018 £000	2017 £000
Accelerated capital allowances and other short-term timing differences	(68)	372
Movement in fair value of financial investments FVOCI / available-for-sale	(66)	(40)
Unutilised tax losses	1,134	1,195
IFRS 9 adjustment	490	-
Deferred tax asset	**1,490**	**1,527**
At 1 January	1,527	1,665
On acquisition of RAF	-	5
Other Comprehensive Income - FVOCI / available-for-sale	(26)	(26)
Profit and loss account - accelerated capital allowances and other short-term timing differences	(96)	(576)
Profit and loss account - tax losses	(405)	459
IFRS 9 adjustment	490	-
Deferred tax asset at 31 December	**1,490**	**1,527**

Company	2018 £000	2017 £000
Accelerated capital allowances and other short-term timing differences	2	346
Tax losses	111	295
Deferred tax asset	**113**	**641**
At 1 January	641	397
Profit and loss account - accelerated capital allowances and other short-term timing differences	-	(51)
Profit and loss account - tax losses	(528)	295
Deferred tax asset at 31 December	**113**	**641**

Deferred tax assets are recognised for tax losses to the extent that the realisation of the related tax benefit through future taxable profits is probable.

27. Interests in associates

Group	2018 £000	2017 £000
Secure Trust Bank PLC	-	83,804
Interests in associates	**-**	**83,804**

Secure Trust Bank ("STB")

At 31 December 2017, ABG had an 18.64% shareholding in STB. On 8 August 2018, ABG lost significant influence over STB and as such the interest in associate was de-recognised. This resulted in a loss on de-recognition of £28.7m, as the shares were marked to market at that date. The profit from associate up to 8 August 2018 was £3m. Going forward the shareholding in STB is reflected as a financial investment as disclosed in Note 25.

Interest in associate for the Company is set out below:

Company	2018 £000	2017 £000
Secure Trust Bank PLC	-	5,056
Interests in associates	**-**	**5,056**

28. Intangible assets

Group	Goodwill £000	Computer software £000	Other intangibles £000	Total £000
Cost				
At 1 January 2017	1,682	8,507	214	10,403
Additions	-	2,641	-	2,641
On Acquisition - RAF (see note 29)	3,520	-	2,348	5,868
At 31 December 2017	**5,202**	**11,148**	**2,562**	**18,912**
Additions	-	2,294	-	2,294
At 31 December 2018	**5,202**	**13,442**	**2,562**	**21,206**
Accumulated amortisation				
At 1 January 2017	-	(1,732)	(149)	(1,881)
Amortisation charge	-	(830)	(206)	(1,036)
At 31 December 2017	**-**	**(2,562)**	**(355)**	**(2,917)**
Amortisation charge	-	(1,483)	(268)	(1,751)
At 31 December 2018	**-**	**(4,045)**	**(623)**	**(4,668)**
Net book amount				
At 31 December 2017	5,202	8,586	2,207	15,995
At 31 December 2018	5,202	9,397	1,939	16,538

The accounting policy for goodwill is described in note 3.15 (a). The Group reviews the goodwill for impairment at least annually or when events or changes in economic circumstances indicate that impairment may have taken place. Significant management judgements are made in estimations, to evaluate whether an impairment of goodwill is necessary. Impairment testing is performed at CGU level and the following two items, with judgements surrounding them, have a significant impact on the estimations used in determining the necessity of an impairment charge:

• Future cash flows - Cash flow forecasts reflect management's view of future business forecasts at the time of the assessment. A detailed three year budget is done every year and management also uses judgement in applying a growth rate. The accuracy of future cash flows is subject to a high degree of uncertainty in volatile market conditions. During such conditions, management would perform impairment testing more frequently than annually to ensure that the assumptions applied are still valid in the current market conditions.

• Discount rate - Management also apply judgement in determining the discount rate used to discount future expected cash flows. The discount rate is derived from the cost of capital for each CGU.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. There are currently two CGUs (2017: two) with goodwill attached; the core Arbuthnot Latham CGU (£1.7m) and RAF CGU (£3.5m).

Management considers the value in use for both CGUs to be the discounted cash flows over 5 years with a terminal value (2017: 5 years with a terminal value). The 5 year discounted cash flows with a terminal value are considered to be appropriate as the goodwill relates to an ongoing well established business and not underlying assets with finite lives. The terminal value is calculated by applying a discounted perpetual growth model to the profit expected in 2020 as per the approved 3 year plan. A growth rate of 8.9% (2017: 12.5%) was used for income and 6.9% (2017: 18%) for expenditure from 2018 to 2020 (these rates were the best estimate of future forecasted performance), while a 3% (2017: 3%) percent growth rate for income and expenditure (a more conservative approach was taken for latter years as these were not budgeted for in detail as per the three year plan approved by the Board of Directors) was used for cash flows after the approved three year plan.

Management considers the value in use for the RAF CGU to be the discounted cash flows over 5 years with a terminal value. The 5 year discounted cash flows with a terminal value are considered to be appropriate as the goodwill relates to an ongoing, well established, business and not underlying assets with finite lives. The terminal value is calculated by applying a discounted perpetual growth model to the profit expected in 2022 as per the approved budget. A growth rate of 3% (2017: 5%) was used (this rate was the best estimate of future forecasted performance).

The growth rates used are above the forecast UK growth rate of 1.3% to reflect the Bank's current growth strategy enabled by capital available at parent level.

Cash flows were discounted at a pre-tax rate of 12% (2017: 12%) to their net present value. The discount rate of 12% is considered to be appropriate after evaluating current market assessments of the time value of money and the risks specific to the assets or CGUs.

Currently, the value in use and fair value less costs to sell of both CGUs exceed the carrying values of the associated goodwill and as a result no sensitivity analysis was performed.

29. Acquisition of Renaissance Asset Finance Ltd

On 28 April 2017, Arbuthnot Latham & Co. Ltd completed the acquisition of 100% of the share capital of Renaissance Asset Finance Limited ("RAF") from its founders following receipt of regulatory approval.

RAF is a provider of finance for a range of specialist assets which includes vintage and expensive cars and SME business assets. The acquisition supported ALs strategy to diversify its proposition within the specialist financial services sector.

The consideration will be paid in four staged amounts, all of which will be in cash. The first payment was equal to the net assets at completion of £2.1m. The remaining three payments are performance related and will be based on the profits of RAF in each of the three calendar years 2018 to 2020. The maximum amount payable for the performance based payments is limited to £6.5m. AL has also provided an intercompany loan to RAF at completion of £57m to re-finance RAF's existing finance liabilities. The consideration and the refinancing of RAF's funding liabilities have been satisfied from the Group's current cash resources.

The assets acquired and resulting goodwill on acquisition are set out in the table below. The fair value of intangibles acquired include £0.4m relating to customer relationships, £1.5m relating to broker relationships and £0.4m for the brand. The resultant goodwill represented the assembled specialist workforce, established process and control environment, cross selling opportunities between the two companies and the opportunity cost of a fully operational company within the sector.

	Acquired assets / liabilities £000	Fair value adjustments £000	Recognised values on acquisition £000
Loans and advances to banks	2,815	-	2,815
Loans and advances to customers	57,684	-	57,684
Other asset	1,341	-	1,341
Deferred tax assets	5	-	5
Intangible assets	-	2,348	2,348
Property, plant and equipment	23	-	23
Total assets	61,868	2,348	64,216
Deposits from banks	58,969	-	58,969
Current tax liability	195	-	195
Other liabilities	632	-	632
Total liabilities	**59,796**	**-**	**59,796**
Net identifiable assets	**2,072**	**2,348**	**4,420**
Consideration			7,940
Goodwill			**3,520**

30. Property, plant and equipment

Group	Freehold land and buildings £000	Leasehold improvements £000	Computer and other equipment £000	Motor Vehicles	Total £000
Cost or valuation					
At 1 January 2017	-	4,587	2,741	97	7,425
Additions	-	408	258	-	666
On acquisition - RAF (see note 29)	-	20	52	-	72
Disposals	-	-	(10)	-	(10)
At 31 December 2017	**-**	**5,015**	**3,041**	**97**	**8,153**
Additions	-	1,764	627	91	2,482
Disposals	-	-	-	(97)	(97)
At 31 December 2018	**-**	**6,779**	**3,668**	**91**	**10,538**
At 1 January 2017	-	(1,217)	(1,380)	(46)	(2,643)
Depreciation charge	-	(944)	(540)	(25)	(1,509)
On acquisition - RAF (see note 29)	-	(16)	(33)	-	(49)
Disposals	-	-	10	-	10
At 31 December 2017	**-**	**(2,177)**	**(1,943)**	**(71)**	**(4,191)**
Depreciation charge	-	(823)	(276)	(23)	(1,122)
Disposals	-	-	-	79	79
At 31 December 2018	**-**	**(3,000)**	**(2,219)**	**(15)**	**(5,234)**
Net book amount					
At 31 December 2017	**-**	**2,838**	**1,098**	**26**	**3,962**
At 31 December 2018	**-**	**3,779**	**1,449**	**76**	**5,304**

Included within the depreciation charge for the year is £nil (2017: £78k) of additional depreciation in relation to the early termination of a property lease.

Company	Computer and other equipment £000	Motor Vehicles £000	Total £000
Cost or valuation			
At 1 January 2017	214	97	311
At 31 December 2017	**214**	**97**	**311**
Additions	3	91	94
Disposals	-	(97)	(97)
At 31 December 2018	**217**	**91**	**308**
Accumulated depreciation			
At 1 January 2017	(82)	(46)	(128)
Depreciation charge	(2)	(24)	(26)
At 31 December 2017	**(84)**	**(70)**	**(154)**
Depreciation charge	(1)	(24)	(25)
Disposals	-	79	79
At 31 December 2018	**(85)**	**(15)**	**(100)**
Net book amount			
At 31 December 2017	**130**	**27**	**157**
At 31 December 2018	**132**	**76**	**208**

31. Investment property

Group	2018 £000	2017 £000
Opening balance	59,439	53,339
Additions	879	6,421
Transfer	6,763	-
Fair value adjustment	-	(321)
At 31 December 2018	**67,081**	**59,439**

£0.9m of additions in 2018 relate to development costs of the St Philips Place property. No property interests are held under operating leases and accounted for as investment property.

King Street London

Arbuthnot Latham & Co., Limited acquired premises in the West End of London (namely 20 King Street/10 St James's Street) on 23 June 2016. The property comprises 22,450 square feet of office space and approximately 7,000 square feet of retail space. The property is held by way of leasehold from The Crown Estate Commissioners that expires in 2136 and with a rent review every five years.

The property is currently fully tenanted, with the main lease ending in 2019. It is accounted for as investment property and the Group has elected to apply the fair value model. It was therefore initially recognised at cost and then subsequently at fair value. The fair value is determined using the rental income on the property and the associated effective yield of similar properties in the surrounding area (see note 4.1(d)). At 31 December 2018 there was no material difference between the cost of the property and the fair value. Independent market commentary of the prime London property market was undertaken at year end to support the valuation.

The Group received £2.1m (2017: £2.1m) rental income during the year and incurred £0.2m (2017: £0.2m) of direct operating expenses.

St Philips Place Birmingham

On 24 November 2017, Arbuthnot Latham & Co., Limited acquired leasehold premises in Birmingham (St Philips House, 4 St Philips Place). The property comprises 24,286 square feet of office space.

The property is unoccupied and is currently undergoing comprehensive refurbishment at an estimated cost of £3.2m. After refurbishment the property will be let out. It is accounted for as investment property and the Group has elected to apply the fair value model. It was therefore initially recognised at cost and then subsequently at fair value (see note 4.1(c)).

A development appraisal has been completed by estimating the gross development value and deducting the estimated costs to complete the refurbishment, arm's length financing costs and development profit margin.

Crescent Office Park, Bath

In November 2017, a Property Fund, based in Jersey and owned by the Group, acquired a freehold office building in Bath. The property comprises 25,526 square ft. over ground and two upper floors with parking spaces. The property was acquired for £6.35m. On the date of acquisition, the property was being multi-let to tenants and was at full capacity.

In 2017, the Fund was recognised as an asset held for sale under IFRS 5 and therefore not consolidated in the financial statements. At 31 December 2018 it was consolidated into the Group as it no longer met the IFRS 5 criteria and is recognised as an investment property. The Group has elected to apply the fair value model (see note 4.1(c)).

The Group recognised £0.5m rental income during the year and incurred £0.5m of operating expenses.

32. Deposits from banks

Group	2018 £000	2017 £000
Deposits from other banks	**232,675**	**195,097**

Deposits from banks include £225m (2017: £188m) obtained through the Bank of England Term Funding Scheme ("TFS"). For a maturity profile of deposits from banks, refer to Note 6.

33. Deposits from customers

Group	2018 £000	2017 £000
Current/demand accounts	944,564	868,855
Notice accounts	75,879	101,909
Term deposits	693,843	420,017
	1,714,286	**1,390,781**

Included in customer accounts are deposits of £24.5m (2017: £29.2m) held as collateral for loans and advances. The fair value of these deposits approximates their carrying value.

For a maturity profile of deposits from customers, refer to Note 6.

34. Other liabilities

Group	2018 £000	2017 £000
Trade payables	1,782	1,207
Accruals and deferred income	16,767	15,032
	18,549	**16,239**

Financial Services Compensation Scheme Levy

In common with all regulated UK deposit takers, AL pays levies to the Financial Services Compensation Scheme (“FSCS”) to enable the FSCS to meet claims against the Scheme. The FSCS levy consists of two parts: a management expenses levy and a more significant compensation levy. The management expenses levy covers the costs of running the scheme and the compensation levy covers the amount of compensation and associated interest the Scheme pays, net of any recoveries it makes using the rights that have been assigned to it.

The Group’s FSCS provision reflects market participation up to the reporting date and the accrual of £nil (2017: £0.2m) relates to the interest levy for the Scheme year 2019/20 which was paid in 2018. This amount was calculated on the basis of the Group’s share of protected deposits and the FSCS’s estimate of total interest levies payable for each Scheme year.

Company	2018 £000	2017 £000
Due to subsidiary undertakings	1,838	1,840
Accruals and deferred income	1,486	1,301
	3,324	**3,141**

35. Debt securities in issue

Group and Company	2018 £000	2017 £000
Subordinated loan notes	**13,283**	**13,104**

The subordinated loan notes were issued on 7 November 2005 and are denominated in Euros. The principal amount outstanding at 31 December 2018 was €15,000,000 (2017: €15,000,000). The notes carry interest at 3% over the interbank rate for three month deposits in euros and are repayable at par in August 2035 unless redeemed or repurchased earlier by the Company.

The contractual undiscounted amount that will be required to be paid at maturity of the above debt securities is €15,000,000.

Given the fact that the Group has never been subject to a published credit rating by any of the relevant agencies and the notes in issue are not quoted, it is not considered possible to estimate a fair value for these notes.

36. Contingent liabilities and commitments

Contingent liabilities

The Group is subject to extensive regulation in the conduct of its business. A failure to comply with applicable regulations could result in regulatory investigations, fines and restrictions on some of the Group's business activities or other sanctions. The Group seeks to minimise this risk through the adoption and compliance with policies and procedures, continuing to refine controls over business practices and behaviour, employee training, the use of appropriate documentation, and the involvement of outside legal counsel where appropriate.

Capital commitments

At 31 December 2018, the Group had capital commitments of US$0.7m (2017: £nil) in respect of a contribution in an equity investment.

Credit commitments

The contractual amounts of the Group’s off-balance sheet financial instruments that commit it to extend credit to customers are as follows:

Group	2018 £000	2017 £000
Guarantees and other contingent liabilities	1,744	2,976
Commitments to extend credit:		
- Original term to maturity of one year or less	67,880	131,963
	69,624	**134,939**

Operating lease commitments

Where a Group company is the lessee, the future aggregate lease payments under non-cancellable operating leases are as follows:

Group	2018 £000	2017 £000
Expiring:		
Within 1 year	2,129	2,330
Later than 1 year and no later than 5 years	10,787	10,943
Later than 5 years	2,661	5,384
	15,577	**18,657**

In 2013, Arbuthnot Latham & Co., Ltd entered into a 16 year lease on 7 Wilson Street, London (the head office for Arbuthnot Banking Group PLC and the principal location for Arbuthnot Latham & Co., Ltd), with a break at 11 years and rent reviews after 5, 10 and 15 years. The initial rent is £1.75m per annum. This lease forms the most significant part of the operating leases disclosed in the table above.

In 2015, the Bank entered into a 10 year lease to occupy part of the ground floor of The Senate, Southernhay Gardens, Exeter, with a break clause and rent review after 5 years. The initial rent is £0.1m per annum.

In 2017, the Bank entered into a 10 year lease to occupy part of the eighth floor of 82 King Street, Manchester, with a break clause and rent review after 5 years. The initial rent is £0.1m per annum.

On 3 January 2018, Arbuthnot Latham entered into a 12 year lease (up to 16 October 2029) to occupy the first, second and third floor of 10 Dominion Street London, with a break clause on 16 October 2024. The initial rent is £0.7m per annum.

In addition to the above commitments, ground rent of £0.2m per annum is payable for the remaining term of 118 years of the King Street investment property.

37. Share capital

Group and Company	Number of shares	Ordinary share capital £000	Share premium £000
At 1 January 2017	15,279,322	153	-
At 31 December 2017 & December 2018	**15,279,322**	**153**	**-**

The Ordinary shares have a par value of 1p per share (2017: 1p per share). At 31 December 2018 the Company held 390,274 shares (2017: 390,274) in treasury.

38. Reserves and retained earnings

Group	2018 £000	2017 £000
Capital redemption reserve	20	20
Fair value reserve / Available-for-sale reserve	(12,169)	162
Treasury shares	(1,131)	(1,131)
Retained earnings	209,083	237,171
Total reserves at 31 December	**195,803**	**236,222**

The capital redemption reserve represents a reserve created after the Company purchased its own shares which resulted in a reduction of share capital.

Company	2018 £000	2017 £000
Capital redemption reserve	20	20
Fair value reserve	(7,022)	-
Treasury shares	(1,131)	(1,131)
Retained earnings	162,729	124,659
Total reserves as 31 December	**154,596**	**123,548**

39. Share-based payment options

Company – cash settled
On 14 June 2016 Mr. Salmon was granted phantom options pursuant to the Phantom Option Scheme to acquire 200,000 ordinary 1p shares in the Company at 1591p exercisable in respect of 50% on or after 15 June 2019 and in respect of the remaining 50% on or after 15 June 2021 when a cash payment would be made equal to any increase in value. On 14 June 2016 Mr. Cobb and Mr. Henderson were each granted phantom options pursuant to the Phantom Option Scheme to acquire 100,000 ordinary 1p shares in the Company at 1591p exercisable in respect of 50% on or after 15 June 2019 and in respect of the remaining 50% on or after 15 June 2021 when a cash payment would be made equal to any increase in market value. The fair value of the options at grant date was £1.3m. At 31 December 2018, the fair value of the options was £0.1m (2017: £0.8m).

The performance conditions of the Scheme are that for the duration of the vesting period, the dividends paid by ABG must have increased in percentage terms when compared to an assumed dividend of 29p per share in respect of the financial year ending 31 December 2016, by a minimum of the increase in the Retail Prices Index during that period.

Also from the grant date to the date the Option is exercised, there must be no public criticism by any regulatory authority on the operation of ABG or any of its subsidiaries which has a material impact on the business of ABG.

Options are forfeited if they remain unexercised after a period of more than 7 years from the date of grant. If the participant ceases to be employed by the Group by reason of injury, disability, ill-health or redundancy; or because his employing company ceases to be a shareholder of the Group; or because his employing business is being transferred out of the Group, his option may be exercised within 6 months after such cessation. In the event of the death of a participant, the personal representatives of a participant may exercise an option, to the extent exercisable at the date of death, within 6 months after the death of the participant.

On cessation of employment for any other reason (or when a participant serves, or has been served with, notice of termination of such employment), the option will lapse although the Remuneration Committee has discretion to allow the exercise of the option for a period not exceeding 6 months from the date of such cessation.

In such circumstances, the performance conditions may be modified or waived as the Remuneration Committee, acting fairly and reasonably and taking due consideration of the circumstances, thinks fit. The number of Ordinary Shares which can be acquired on exercise will be pro-rated on a time elapsed basis, unless the Remuneration Committee, acting fairly and reasonably and taking due consideration of the circumstances, decides otherwise. In determining whether to exercise its discretion in these respects, the Remuneration Committee must satisfy itself that the early exercise of an option does not constitute a reward for failure.

The probability of payout has been assigned based on the likelihood of meeting the performance criteria, which is 100%. The Directors consider that there is some uncertainty surrounding whether the participants will all still be in situ and eligible at the vesting date. Therefore the directors have assumed a 9% attrition rate for the share options vesting in June 2019 and 15% attrition rate for the share options vesting in June 2021. The attrition rate will increase by 3% per year until the vesting date. ABG had a write back of £0.3m in relation to share based payments during 2018 (2017: £0.2m expense), as disclosed in Note 12.

Measurement inputs and assumptions used in the Black-Scholes model are as follows:

	2018	2017
Expected Stock Price Volatility	19.8%	27.0%
Expected Dividend Yield	3.6%	2.5%
Risk Free Interest Rate	0.8%	0.5%
Average Expected Life (in years)	1.46	2.46

40. Dividends per share

Final dividends are not accounted for until they have been approved at the Annual General Meeting. At the meeting on 9 May 2019, a dividend in respect of 2018 of 20p per share (2017: actual dividend 19p per share) amounting to a total of £2.98m (2017: actual £2.83m) is to be proposed. The financial statements for the year ended 31 December 2018 do not reflect the final dividend which will be accounted for in shareholders' equity as an appropriation of retained profits in the year ending 31 December 2019.

41. Cash and cash equivalents

For the purposes of the Statement of Cash Flows, cash and cash equivalents are comprised of the following balances with less than three months' maturity from the date of acquisition.

Group	2018 £000	2017 £000
Cash and balances at central banks (Note 17)	405,325	313,101
Loans and advances to banks (Note 18)	54,173	70,679
	459,498	**383,780**

Company	2018 £000	2017 £000
Loans and advances to banks	**17,008**	**36,103**

42. Related party transactions

Related parties of the Company and Group include subsidiaries, directors, Key Management Personnel, close family members of Key Management Personnel and entities which are controlled, jointly controlled or significantly influenced, or for which significant voting power is held, by Key Management Personnel or their close family members.

Other than the directors' remuneration (see Remuneration Report pages 27 to 28), payment of dividends and transactions with subsidiaries and associates, there were no related party transactions within the Parent Company. A number of banking transactions are entered into with related parties in the normal course of business on normal commercial terms. These include loans and deposits. Except for the directors' disclosures, there were no other Key Management Personnel disclosures; therefore the tables below relate to directors and their close family members.

Group - subsidiaries	2018 £000	2017 £000
Loans		
Loans outstanding at 1 January	508	1,361
Loans advanced during the year	126	150
Loan repayments during the year	(2)	(3)
Transfer to deposits during the year	(117)	-
Transferred to loans with associates	-	(1,000)
Loans outstanding at 31 December	**515**	**508**
Interest income earned	**15**	**23**

Group - associates	2018 £000	2017 £000
Loans		
Loans outstanding at 1 January	1,409	404
Loans advanced during the year	-	5
Loan repayments during the year	(1,409)	-
Transferred from loans with subsidiaries	-	1,000
Loans outstanding at 31 December	**-**	**1,409**
Interest income earned	**-**	**5**

The loans to directors are mainly secured on property, shares or cash and bear interest at rates linked to base rate. No provisions have been recognised in respect of loans given to related parties (2017: £nil).

Group - subsidiaries	2018 £000	2017 £000
Deposits		
Deposits at 1 January	3,233	3,398
Deposits placed during the year	3,390	3,563
Deposits repaid during the year	(4,622)	(2,728)
Transfer to loans during the year	(117)	-
Transferred to deposits with associates	-	(1,000)
Deposits at 31 December	**1,884**	**3,233**
Interest expense on deposits	**7**	**46**

Group - associates	2018 £000	2017 £000
Deposits		
Deposits at 1 January	1,403	318
Deposits placed during the year	-	85
Deposits repaid during the year	(1,403)	-
Transferred from deposits with subsidiaries	-	1,000
Deposits at 31 December	**-**	**1,403**
Interest expense on deposits	**-**	**5**

Details of directors' remuneration are given in the Remuneration Report. The Directors do not believe that there were any other transactions with key management or their close family members that require disclosure.

Details of principal subsidiaries are given in Note 43. Transactions and balances with subsidiaries are shown below:

	2018		2017	
	Highest balance during the year	Balance at 31 December	Highest balance during the year	Balance at 31 December
	£000	£000	£000	£000
ASSETS				
Due from subsidiary undertakings	35,483	17,002	89,150	36,256
Shares in subsidiary undertakings	134,614	134,614	97,802	97,802
	170,097	**151,616**	**186,952**	**134,058**
LIABILITIES				
Due to subsidiary undertakings	2,097	1,566	4,011	1,570
	2,097	**1,566**	**4,011**	**1,570**

The disclosure of the year end balance and the highest balance during the year is considered the most meaningful information to represent the transactions during the year. The above transactions arose during the normal course of business and are on substantially the same terms as for comparable transactions with third parties.

The Company undertook the following transactions with other companies in the Group during the year:

	2018	2017
	£000	£000
Arbuthnot Latham & Co., Ltd - Recharge of property and IT costs	930	1,087
Arbuthnot Latham & Co., Ltd - Recharge for costs paid on the Company's behalf	1,520	1,501
Arbuthnot Latham & Co., Ltd - Group recharges for shared services	(1,200)	(1,483)
Secure Trust Bank PLC (from 16 June 2016 to 8 August 2018 as associate) - Group recharges for shared services	(751)	(813)
Secure Trust Bank PLC (from 16 June 2016 to 8 August 2018 as associate) - Dividends received	(2,101)	(2,618)
Total	**(1,602)**	**(2,326)**

43. Interests in subsidiaries

Company	Investment at cost £000	Impairment provisions £000	Net £000
At 1 January 2017	57,166	(2,564)	54,602
Capital contributions to Arbuthnot Latham & Co., Limited	43,200	-	43,200
At 31 December 2017	**100,366**	**(2,564)**	**97,802**
Capital contributions to Arbuthnot Latham & Co., Limited	36,812	-	36,812
At 31 December 2018	**137,178**	**(2,564)**	**134,614**

Company	2018 £000	2017 £000
Subsidiary undertakings:		
Bank	132,314	95,502
Other	2,300	2,300
Total	**134,614**	**97,802**

(a) List of subsidiaries

Arbuthnot Latham & Co., Limited is the only significant subsidiary of Arbuthnot Banking Group. Arbuthnot Latham is incorporated in the United Kingdom, has a principal activity of Private and Commercial Banking and is 100% owned by the Group.

The table below provides details of other subsidiaries of Arbuthnot Banking Group PLC at 31 December:

	% shareholding	Country of incorporation	Principal activity
Direct shareholding			
Arbuthnot Fund Managers Limited	100.0%	UK	Dormant
Arbuthnot Investments Limited	100.0%	UK	Dormant
Arbuthnot Limited	100.0%	UK	Dormant
Arbuthnot Properties Limited	100.0%	UK	Dormant
Arbuthnot Unit Trust Management Limited	100.0%	UK	Dormant
Gilliat Financial Solutions Limited	100.0%	UK	Dormant
Peoples Trust and Savings Plc	100.0%	UK	Dormant
West Yorkshire Insurance Company Limited	100.0%	UK	Non-trading
Windward Insurance Company PCC Limited	100.0%	Guernsey	Insurance
Indirect shareholding via intermediate holding companies			
Arbuthnot Commercial Asset Based Lending Limited	100.0%	UK	Asset Finance
Arbuthnot Latham (Nominees) Limited	100.0%	UK	Dormant
Arbuthnot Latham Real Estate Holdco Limited	100.0%	Jersey	Property Investment
Arbuthnot Latham Real Estate Holdings Limited	100.0%	UK	Property Investment
Arbuthnot Latham Real Estate PropCo Limited	100.0%	Jersey	Property Investment
Arbuthnot Real Estate Capital Limited	100.0%	Jersey	Property Investment
Arbuthnot Real Estate Capital GP 1 Limited	100.0%	Jersey	Property Investment
Arbuthnot Real Estate Capital Fund 1 Limited	100.0%	Jersey	Property Investment
Arbuthnot Securities Limited	100.0%	UK	Dormant
Arbuthnot Specialist Finance Limited	100.0%	UK	Dormant
Artillery Nominees Limited (dissolved 16 January 2018)	100.0%	UK	Dormant
John K Gilliat & Co., Limited	100.0%	UK	Dormant
Pinnacle Universal Limited	100.0%	BVI	Property development
Pinnacle Universal Limited	100.0%	UK	Dormant
Renaissance Asset Finance Limited	100.0%	UK	Asset Finance

All the subsidiary and related undertakings above are unlisted and none are banking institutions. All entities are included in the consolidated financial statements and have an accounting reference date of 31 December. On 16 January 2018, Artillery Nominees Limited was dissolved.

All Jersey entities have their registered office as 26 New Street, St Helier, Jersey, JE2 3RA. Pinnacle Universal Limited's (BVI) registered office is 9 Columbus Centre, Pelican Drive, Road Town, Tortola, BVI. All other entities listed above have their registered office as 7 Wilson Street, London, EC2M 2SN.

(b) Non-controlling interests in subsidiaries

There were no non-controlling interests at the end of 2017 or 2018.

(c) Significant restrictions

The Group does not have significant restrictions on its ability to access or use its assets and settle its liabilities other than those resulting from the supervisory frameworks within which banking subsidiaries operate. The supervisory frameworks require banking subsidiaries to keep certain levels of regulatory capital and liquid assets, limit their exposure to other parts of the Group and comply with other ratios. The carrying amounts of the banking subsidiary's assets and liabilities are £2,171m and £1,994m respectively (2017: £1,784m and £1,651m respectively).

(d) Risks associated with interests

During the year Arbuthnot Banking Group PLC made £36.8m (2017: £43.2m) capital contributions to Arbuthnot Latham & Co., Ltd. The contributions were made to assist the Bank during a period of growth to ensure that all regulatory capital requirements were met.

44. Operating segments

The Group is organised into six operating segments as disclosed below:

1) Private Banking – Provides traditional private banking services as well as offering financial planning and investment management services. This segment includes Dubai and the Tay mortgage portfolio.
2) Commercial Banking – Provides bespoke commercial banking services and tailored secured lending against property investments and other assets.
3) RAF – Specialist asset finance lender mainly in high value cars but also business assets.
4) All Other Divisions – All other smaller divisions and central costs in Arbuthnot Latham & Co., Ltd (Arbuthnot Commercial Asset-Based Lending, Arbuthnot Direct, Arbuthnot Specialist Finance, Investment properties and Central unallocated items)
5) Group Centre – ABG Group Centre management.

Transactions between the operating segments are on normal commercial terms. Centrally incurred expenses are charged to operating segments on an appropriate pro-rata basis. Segment assets and liabilities comprise loans and advances to customers and customer deposits, being the majority of the balance sheet.

	Continuing operations						Discontinued Operations	
Year ended 31 December 2018	Private banking £000	Commercial Banking £000	RAF £000	All Other Divisions £000	Group Centre £000	**Total £000**	**Retail Bank Associate Income £000**	**Group Total £000**
Interest revenue	38,185	18,889	7,536	680	88	**65,378**	**-**	**65,378**
Inter-segment revenue	-	-	-	-	(88)	**(88)**	**-**	**(88)**
Interest revenue from external customers	38,185	18,889	7,536	680	-	**65,290**	**-**	**65,290**
Fee and commission income	11,550	1,036	151	219	-	**12,956**	**-**	**12,956**
Revenue from external customers	**49,735**	**19,925**	**7,687**	**899**	**-**	**78,246**	**-**	**78,246**
Interest expense	(4,422)	(2,505)	(2,192)	(517)	(199)	**(9,835)**	**-**	**(9,835)**
Add back inter-segment revenue	-	-	-	-	88	**88**	**-**	**88**
Subordinated loan note interest	-				(360)	**(360)**	**-**	**(360)**
Fee and commission expense	(56)	(122)	(14)	(42)	-	**(234)**	**-**	**(234)**
Segment operating income	45,257	17,298	5,481	340	(471)	**67,905**	**-**	**67,905**
Impairment losses	(1,966)	(278)	(437)	(50)	-	**(2,731)**	**-**	**(2,731)**
Other income	2	-	73	6,683	(170)	**6,588**	**-**	**6,588**
Operating expenses	(37,492)	(14,534)	(3,169)	(2,634)	(7,153)	**(64,982)**	**-**	**(64,982)**
Segment profit / (loss) before tax	5,801	2,486	1,948	4,339	(7,794)	**6,780**	**-**	**6,780**
Income tax (expense) / income	-	-	(431)	35	(725)	**(1,121)**	**-**	**(1,121)**
Segment profit / (loss) after tax	**5,801**	**2,486**	**1,517**	**4,374**	**(8,519)**	**5,659**	**-**	**5,659**
Loss from discontinued operations	**-**	**-**	**-**	**-**	**-**	**-**	**(25,692)**	**(25,692)**
Segment profit / (loss) after tax	**5,801**	**2,486**	**1,517**	**4,374**	**(8,519)**	**5,659**	**(25,692)**	**(20,033)**
Loans and advances to customers	670,464	443,108	85,958	36,626	(11,500)	**1,224,656**	**-**	**1,224,656**
Other assets	-	-	-	936,370	14,147	**950,517**	**-**	**950,517**
Segment total assets	**670,464**	**443,108**	**85,958**	**972,996**	**2,647**	**2,175,173**	**-**	**2,175,173**
Customer deposits	1,041,208	566,748	-	136,092	(29,762)	**1,714,286**	**-**	**1,714,286**
Other liabilities	-	-	-	251,437	13,494	**264,931**	**-**	**264,931**
Segment total liabilities	**1,041,208**	**566,748**	**-**	**387,529**	**(16,268)**	**1,979,217**	**-**	**1,979,217**
Other segment items:								

The "Group Centre" segment above includes the parent entity and all intercompany eliminations.

Year ended 31 December 2017	Continuing operations Private Banking £000	Commercial Banking £000	RAF £000	All Other Divisions £000	Group Centre £000	Total £000	Discontinued operations Retail Bank Associate Income £000	Group Total £000
Interest revenue	36,179	7,228	4,194	-	204	**47,805**	**-**	**47,805**
Inter-segment revenue	(174)	-	-	-	(204)	**(378)**	**-**	**(378)**
Interest revenue from external customers	36,005	7,228	4,194	-	-	**47,427**	**-**	**47,427**
Fee and commission income	13,104	621	80	-	-	**13,805**	**-**	**13,805**
Revenue from external customers	**49,109**	**7,849**	**4,274**	**-**	**-**	**61,232**	**-**	**61,232**
Interest expense	(4,651)	(508)	(1,040)	-	(153)	**(6,352)**	**-**	**(6,352)**
Add back inter-segment revenue	174	-	-	-	204	**378**	**-**	**378**
Subordinated loan note interest	-	-	-	-	(360)	**(360)**	**-**	**(360)**
Fee and commission expense	(127)	(150)	(5)	-	-	**(282)**	**-**	**(282)**
Segment operating income	44,505	7,191	3,229	-	(309)	**54,616**	**-**	**54,616**
Impairment losses	(308)	-	(86)	-	-	**(394)**	**-**	**(394)**
Other income	-	-	-	3,870	(837)	**3,033**	**-**	**3,033**
Operating expenses	(36,268)	(9,254)	(1,690)	(230)	(7,279)	**(54,721)**	**-**	**(54,721)**
Segment profit / (loss) before tax	7,929	(2,063)	1,453	3,640	(8,425)	**2,534**	**-**	**2,534**
Income tax (expense) / income	-	-	(303)	(237)	92	**(448)**	**-**	**(448)**
Segment profit / (loss) after tax	**7,929**	**(2,063)**	**1,150**	**3,403**	**(8,333)**	**2,086**	**-**	**2,086**
Profit from discontinued operations	-	-	-	-	-	**-**	**4,437**	**4,437**
Segment profit / (loss) after tax	**7,929**	**(2,063)**	**1,150**	**3,403**	**(8,333)**	**2,086**	**4,437**	**6,523**
Loans and advances to customers	650,245	305,055	71,265	34,204	(11,500)	**1,049,269**	**-**	**1,049,269**
Other assets	-	-	-	721,502	82,461	**803,963**	**-**	**803,963**
Segment total assets	**650,245**	**305,055**	**71,265**	**755,706**	**70,961**	**1,853,232**	**-**	**1,853,232**
Customer deposits	954,577	308,341	-	176,886	(49,023)	**1,390,781**	**-**	**1,390,781**
Other liabilities	-	-	-	210,680	15,396	**226,076**	**-**	**226,076**
Segment total liabilities	**954,577**	**308,341**	**-**	**387,566**	**(33,627)**	**1,616,857**	**-**	**1,616,857**
Other segment items:								
Capital expenditure	-	-	-	(3,307)	-	**(3,307)**	**-**	**(3,307)**
Depreciation and amortisation	-	-	-	(2,354)	(26)	**(2,380)**	**-**	**(2,380)**

Segment profit is shown prior to any intra-group eliminations.

Prior year numbers have been represented according to the 2018 operating segments reported to management. The UK private bank has a branch in Dubai, which generated £4.4m (2017: £4.5m) of income and had direct operating costs of £2.9m (2017: £2.7m). All Dubai branch income is booked in the UK. Other than the Dubai branch, all operations of the Group are conducted wholly within the United Kingdom and geographical information is therefore not presented.

45. Country by Country Reporting

Article 89 of the EU Directive 2013/36/EU otherwise known as the Capital Requirements Directive IV ('CRD IV') was implemented into UK domestic legislation through statutory instrument 2013 No. 3118, the Capital Requirements (Country-by-Country Reporting) Regulations 2013 (the Regulations), which were laid before the UK Parliament on 10 December 2013 and which came into force on 1 January 2014.

Article 89 requires credit institutions and investment firms in the EU to disclose annually, specifying, by Member State and by third country in which it has an establishment, the following information on a consolidated basis for the financial year: name, nature of activities, geographical location, turnover, number of employees, profit or loss before tax, tax on profit or loss and public subsidies received.

31 December 2018 Location	Turnover (£m)	Number FTE employees	Profit/(loss) before tax (£m)	Tax paid (£m)
UK	67.9	423	9.7	1.2
Dubai	-	14	(2.9)	-

31 December 2017 Location	Turnover (£m)	Number FTE employees	Profit/(loss) before tax (£m)	Tax paid (£m)
UK	54.6	350	9.8	-
Dubai	-	16	(2.7)	-

The Dubai branch income is booked through the UK, hence the turnover is nil in the above analysis. Offsetting this income against Dubai branch costs would result in a £1.6m profit (2017: £1.8m). After indirect cost allocation it results in a loss of £0.8m (2017: loss of £0.5m). No public subsidies were received during 2018

46. Ultimate controlling party

The Company regards Sir Henry Angest, the Group Chairman and Chief Executive Officer, who has a beneficial interest in 56.1% of the issued share capital of the Company, as the ultimate controlling party. Details of his remuneration are given in the Remuneration Report and Note 42 of the consolidated financial statements includes related party transactions with Sir Henry Angest.

47. Events after the balance sheet date

There were no material post balance sheet events to report.

Five Year Summary

		2014	2015	2016	2017	2018
		£000	£000	£000	£000	£000
Profit \ (loss) for the year after tax		17,016	26,524	227,569	6,523	(20,033)
(Loss) / profit before tax from continuing operations*		(3,824)	(2,606)	(1,966)	2,534	6,780
Total Earnings per share						
Basic (p)		58.6	86.3	1,127.2	43.9	(134.5)
Earnings per share from continuing operations*						
Basic (p)		(24.8)	(16.9)	(18.2)	14.0	38.0
Dividends per share (p)	- ordinary	27.0	29.0	31.0	33.0	35.0
	- special	-	-	325.0	-	-

Other KPI:

	2014	2015	2016	2017	2018
	£000	£000	£000	£000	£000
Net asset value per share (p)	1,136.0	1,252.7	1,533.8	1,547.0	1,282.5

* - Prior year numbers have been restated for continuing operations.