ARBUTHNOT BANKING GROUP PLC

19 July 2022

ARBUTHNOT BANKING GROUP PLC (“Arbuthnot”, “the Company”, “the Group” or “ABG”)
Unaudited results for the six months to 30 June 2022

Arbuthnot Banking Group PLC is pleased to announce a half yearly profit before tax of £3.4m.

Arbuthnot Banking Group PLC is the holding company for Arbuthnot Latham & Co., Limited.

FINANCIAL HIGHLIGHTS

- Profit before tax increased 11% to £3.4m (30 June 2021: £3.0m)
- Underlying profit before tax of £10.7m (30 June 2021: £6.5m)*
- Agreed terms for the sale of King Street property with exchange expected shortly
- Interim dividend declared of 17p per share (30 June 2021: 16p per share for the normal interim dividend, 21p for a special dividend)
- CET1 capital ratio of 11.4% (31 December 2021: 12.3%) and total capital ratio of 14.0% (31 December 2021: 14.9%)
- Earnings per share of 17.8p (30 June 2021: 27.2p)
- Net assets per share of £13.00 (30 June 2021: £12.92; 31 December 2021: £13.15)

OPERATIONAL HIGHLIGHTS

- Customer loans of £2.1bn (30 June 2021: £1.9bn; 31 December 2021: £2.0bn)** increased by 5% in the first half of the year
- Customer deposits of £2.8bn (30 June 2021: £2.6bn; 31 December 2021: £2.8bn) remained stable from the end of 2021
- Assets under management of £1.30bn (30 June 2021: £1.22bn; 31 December 2021: £1.36bn) – a decrease of 4% in the first half of the year as investment markets declined

*Details of the calculation of underlying profit before tax can be found in note 6
**Customer loans also includes Leased Asset balances

Commenting on the results, Sir Henry Angest, Chairman and Chief Executive of Arbuthnot, said: **“During the first half of 2022 the Group has seen a marked improvement in underlying profitability as a result of the rising interest rate environment. Given our low cost and stable relationship-based deposits, the Group is well positioned to continue to fund the diverse lending businesses and maintain good margins as it builds towards delivering our “future state” plan.”**

Interim Dividend
The interim dividend of 17p per share will be paid on 23 September 2022 to shareholders on the register at the close of business on 26 August 2022.

The full set of interim results are available at http://www.arbuthnotgroup.com.

The Directors of the Company accept responsibility for the contents of this announcement.

The information contained within this announcement is deemed to constitute inside information as stipulated under the retained EU law version of the Market Abuse Regulation (EU) No. 596/2014 (the "UK MAR") which is part of UK law by virtue of the European Union (Withdrawal) Act 2018. The information is disclosed in accordance with the Company's obligations under Article 17 of the UK MAR. Upon the publication of this announcement, this inside information is now considered to be in the public domain.

ENQUIRIES:

Arbuthnot Banking Group 020 7012 2400
Sir Henry Angest, Chairman and Chief Executive
Andrew Salmon, Group Chief Operating Officer
James Cobb, Group Finance Director

Grant Thornton UK LLP (Nominated Adviser and AQSE Corporate Adviser) 020 7383 5100
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Daniel Bush
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Maitland/AMO (Financial PR) 020 7379 5151
Neil Bennett
Sam Cartwright

Chairman's Statement

I am pleased to be able to report that the Group has made a good start to the year. The profit before tax for the first six months is recorded as £3.4m compared to £3.0m in the comparable period in the prior year.

The underlying profit before tax for the period is £10.7m, after adjusting for the change in net realisable value of the property in King Street (£4.0m) resulting from the agreement to sell the property. Terms for sale have been agreed and exchange of contracts is expected shortly. Additionally, the profit needs to be adjusted for the forgone profit on the sale of trucks generated by Asset Alliance (£3.3m), which is required from the acquisition accounting in the prior year.

The improvement in the profitability comes from continued growth and diversification of our lending balances and now also significantly from the increase in base rates. In the months of May and June the Group achieved underlying profitability of more than £2.0m per month.

It should be noted that given the delay in the repricing of deposits compared to the immediate impact of the base rate increases on lending rates, the Group is enjoying abnormally wide interest margins. These may narrow as the fixed rate deposit balances reprice when they mature and are renewed at higher rates.

The business model of funding our specialist lending divisions by attracting cheaper but sticky balances from our relationship driven deposit account clients was always dependant on a "normal" interest rate environment. The average cost of deposits in 2021 was 39 bps and it is currently running at 37 bps. The upward pressure on this rate has been reduced, as we took a strategic decision not to compete for deposits on the non-relationship aggregator platforms. In fact, we have allowed £100m of deposits to mature without competing to retain them in our book. These have been replaced by direct relationship balances as the deposit book remained flat at £2.8bn from the end of 2021.

Overall demand for lending products has continued across our divisions with balances (including lease assets) growing to £2.1bn, an increase of £112m from the year end 2021.

As the business model has benefitted from improved conditions given the base rate increases, the major headwind on the horizon will be the upward pressure on our cost base. Competition in the employment market is starting to result in accelerating increases in salaries in the market, as the cost-of-living crisis starts to interact with full employment. To this end, the Board decided at its recent meeting in July to award a one-off payment to all employees of £1,500 payable in September. This will total approximately £1m.

The Board has also noted the recent decision by the Financial Policy Committee ("FPC") of the Bank of England to press on with its plans to introduce the second increase of 1% in the countercyclical capital buffer, effective in July 2023. Confusingly, at the same time the committee encouraged banks to continue to lend into a possible recessionary economy.

As previously noted, the Board has a number of options available to manage the capital resources of the Group, without slowing our lending plans as the divisions build towards the "future state" strategy that was set out in the Investor presentation associated with the Annual Report and Accounts for 2021.

One of these options is to allocate capital away from non-core assets and accordingly we have agreed terms to sell our grade A, long leasehold property situated in the West End, at 20 King Street. The property had been recently fully refurbished and the agreed headline price is £60m or a yield of 3.75%. The adjustments for letting incentives and voids will reduce the total receipts to an estimated £56.6m compared to the carrying value of the asset at £60.6m. Once exchange has taken place, completion of the sale will be dependent on receiving approval from the owner of the freehold, the Crown Estate.

Given the removal of restrictions on the ability of banks to pay dividends, the Board intends to return to its progressive dividend policy. Accordingly, an interim dividend of 17p per share will be paid on 23 September 2022 to shareholders on the register at the close of business on 26 August 2022. This is an increase of 1p per share from the normal interim dividend paid in 2021.

Banking

The Banking division has reported a profit before tax of £6.6m (30 June 2021: profit of £0.1m), with lending balances totalling £1.46bn and deposits of £2.61bn (30 June 2021: lending of £1.28bn; deposits of £2.43bn). The increase in profitability is primarily due to increased interest income from lending balances repricing up as a result of successive increases in the Bank of England base rate, with the average cost of deposits remaining stable over the period.

The Bank continues to maintain strong levels of liquidity reserves without competing for higher priced "best buy table" deposits, which have experienced a material uplift in interest rates following the successive base rate rises. Where deposits have matured and not been retained, a significant portion have been from aggregator and platform channels where the Bank does not have a direct relationship with the underlying client. There was continued focus on targeting clients who value the Bank's quality service led proposition.

Going into 2022, the Bank had a strong lending pipeline that has resulted in drawdowns being broadly on plan. Net loan growth has been tempered by repayments ahead of expectations as the result of a number of watchlist lending cases being resolved. Despite this, the Banking loan book has grown by 3% in the 6 months to June 2022 and 14% since the end of June 2021.

The Bank of England base rate rises had a positive effect on the Bank's revenue for the year. There has been a strong preference from clients for fixed rate lending outside the Bank's targeted return on capital. This had presented a barrier to growth with an adverse impact on the pipeline, however, enquiries have started to return to expected levels towards the end of the period.

During 2021, the Bank announced a three-year strategic "originate to sell" agreement with a third party to build a Commercial Real Estate Loan portfolio. Transactions totalling £20.4m have been completed to date with a strong pipeline in development. Additionally, there is a large volume of capital intensive Commercial Real Estate loans maturing in the second half 2022, outside of the Bank's current appetite, to which it will be able to provide support via this agreement.

Wealth Management

In the first half of 2022, Assets under Management ("AuM") fell 4% to £1,303m as a result of turbulence across most markets. This was despite gross client inflows of £128.1m, which were 32% higher than the prior year. AUM however showed 6.5% growth year on year.

Account closures were 33% lower year on year and client attrition associated with last year's closure of the Dubai office has remained within expectations.

Mortgage Portfolios

The Group's acquired mortgage portfolio is currently operating in line with expectations with balances of £171.2m compared to £191.1m as at 30 June 2021 and £178.1m at the year end.

Renaissance Asset Finance ("RAF")

RAF has reported a profit before tax of £0.2m (30 June 2021: £1.0m), with customer loan balances of £102.6m (30 June 2021: £93.0m). The reduced profit is due to the increase in the intercompany funding charge, which is linked to the BoE base rate.

The RAF loan book has grown 11% year on year, and 5% in the first half of the year. The business continues to experience strong demand for its asset finance facilities with the current pipeline of new business proposals and acceptances above pre-pandemic levels. RAF however continues to experience delays in deal originations as a result of supply chain challenges.

Loans under forbearance measures following the pandemic continue to be confined to the London purpose-built taxi market but have shown significant recovery as London and the economy returns to normality.

Arbuthnot Commercial Asset Based Lending ("ACABL")

ACABL has reported a profit before tax of £2.9m (30 June 2021: £1.8m), with a loan book of £238.8m (30 June 2021: £147.9m).

Despite the challenging markets, the business has been presented with a number of transactions suiting ACABL's lending approach. The business completed its largest deal to date in January with facilities written in excess of £20m, comprising both traditional asset-based lending as well as a Recovery Loan Scheme ("RLS") facility.

The ACABL loan book has continued to increase at a good rate with 32% growth in the 6 months to 30 June 2022 and a 61% increase year on year. The loan book growth was marginally offset by the repayment of some of the business's earlier written facilities where ACABL has supported the client successfully through their growth phase.

Where appropriate, RLS products have continued to be utilised in deal structuring over the period. This government backed scheme has now closed. As at 30 June 2022 ACABL had an RLS exposure totalling £39.6m across 23 loans.

Arbuthnot Specialist Finance Limited ("ASFL")

ASFL has made a loss before tax of £0.6m (30 June 2021: loss of £0.6m). Customer loan balances were £9.6m at the half year (30 June 2021: £7.5m).

ASFL continues to make progress on implementing its new business plan. The loan book remains in line with the prior year end with a steady pipeline.

Asset Alliance Group ("AAG")

AAG reported a loss of £1.1m for the six months to 30 June 2022 (excluding the bargain purchase of £8.7m, AAG reported a loss of £0.8m for the three months ended 30 June 2021), with assets available to lease of £115.1m compared to £132.3m for the same period in the prior year and £121.6m at the year end. This loss is after paying intercompany interest of £1.8m (30 June 2021: £0.7m).

The global supply chain issues previously affecting AAG's ability to source new trucks has started to show signs of improvement with orders placed prior to the COVID pandemic starting to be fulfilled. The business has continued to maintain a steady order book with forward orders of new trucks increasing in term and volume. The business remains behind the original lending growth plan due to delays experienced in prior periods. However, the business is well positioned for possible economic headwinds with a significant portfolio of assets leased to essential service sectors.

Used truck sales continue to be supported by an ongoing strong demand in the second-hand market, achieving higher than budgeted margins which is supporting underlying profitability. The business continues to develop its Bus and Coach lending business and focus on the stronger urban markets which remain robust with regular asset replacement cycles in place.

Owned Properties

As mentioned above, the Group has agreed, subject to contract, to sell its King Street property. Furthermore, after the completion of the sale process for two of the Bank's overseas properties acquired as a result of bad debts, the Bank now only holds one overseas property.

Operations

The Bank continues to observe increased client banking activity as economic activity continues to gain pace after the previous year's lockdowns, with a 40% increase of outbound payments against the prior year, including outward Faster Payments increasing 54%. Digital wallet transactions (Apple and Google Pay), launched during the prior year, are trending up with a steady increase in client usage month on month.

Outlook

The macro-economic environment appears increasingly uncertain with inflation predicted to reach double figures and interest rates set to rise further. However, the bank is positively positioned for the upward trend in interest rates whilst remaining alert to the risks that may arise to borrowers if the economy worsens.

Consolidated Statement of Comprehensive Income

	Note	Six months ended 30 June 2022 £000	Six months ended 30 June 2021 £000
Income from banking activities			
Interest income		49,088	36,723
Interest expense		(6,552)	(6,784)
Net interest income		**42,536**	**29,939**
Fee and commission income		10,099	8,782
Fee and commission expense		(59)	(177)
Net fee and commission income		**10,040**	**8,605**
Operating income from banking activities		**52,576**	**38,544**
Income from leasing activities			
Revenue		48,851	22,533
Cost of goods sold		(40,538)	(19,689)
Gross profit from leasing activities		**8,313**	**2,844**
Total group operating income		**60,889**	**41,388**
Net impairment loss on financial assets		(1,201)	(865)
Other income	7	610	2,889
Profit from bargain purchase	9	-	8,656
Operating expenses		(56,923)	(49,030)
Profit before income tax		**3,375**	**3,038**
Income tax (expense) / credit		(705)	1,054
Profit for the period		**2,670**	**4,092**
Other comprehensive income			
Items that will not be reclassified to profit or loss			
Changes in fair value of equity investments at fair value through other comprehensive income		462	9,096
Tax on other comprehensive income		(88)	(17)
Other comprehensive income for the period, net of tax		**374**	**9,079**
Total comprehensive income for the period		**3,044**	**13,171**
Earnings per share for profit attributable to the equity holders of the Company during the period (expressed in pence per share):			
Basic earnings per share	8	17.8	27.2
Diluted earnings per share	8	17.8	27.2

Consolidated Statement of Financial Position

	At 30 June	At 30 June	At 31 December
	2022	2021	2021
	£000	£000	£000
ASSETS			
Cash and balances at central banks	512,837	616,004	814,692
Loans and advances to banks	125,839	104,904	73,444
Debt securities at amortised cost	386,880	391,987	301,052
Assets classified as held for sale	3,220	3,183	3,136
Derivative financial instruments	4,165	850	1,753
Loans and advances to customers	1,989,867	1,726,471	1,870,962
Current tax asset	-	17	-
Other assets	110,188	110,044	110,119
Financial investments	2,970	11,407	3,169
Deferred tax asset	3,233	420	2,562
Intangible assets	30,853	27,794	29,864
Property, plant and equipment	118,551	140,465	125,890
Right-of-use assets	14,663	16,306	15,674
Investment properties	6,550	6,550	6,550
Total assets	**3,309,816**	**3,156,402**	**3,358,867**
EQUITY AND LIABILITIES			
Equity attributable to owners of the parent			
Share capital	154	154	154
Retained earnings	200,785	204,165	201,026
Other reserves	(321)	(4,891)	(301)
Total equity	**200,618**	**199,428**	**200,879**
LIABILITIES			
Deposits from banks	230,110	230,106	240,333
Derivative financial instruments	162	286	171
Deposits from customers	2,801,530	2,642,761	2,837,869
Current tax liability	1,877	-	413
Other liabilities	23,092	29,820	26,216
Lease liabilities	15,269	16,912	16,214
Debt securities in issue	37,158	37,089	36,772
Total liabilities	**3,109,198**	**2,956,974**	**3,157,988**
Total equity and liabilities	**3,309,816**	**3,156,402**	**3,358,867**

Consolidated Statement of Changes in Equity

	Attributable to equity holders of the Group						
	Share capital	Revaluation reserve	Capital redemption reserve	Fair value reserve	Treasury shares	Retained earnings	Total
	£000	£000	£000	£000	£000	£000	£000
Balance at 1 January 2022	**154**	**-**	**19**	**979**	**(1,299)**	**201,026**	**200,879**
Total comprehensive income for the period							
Profit for the six months ended 30 June 2022	-	-	-	-	-	2,670	2,670
Other comprehensive income, net of income tax							
Changes in the fair value of financial assets at FVOCI	-	-	-	462	-	-	462
Tax on other comprehensive income	-	-	-	(88)	-	-	(88)
Total other comprehensive income	**-**	**-**	**-**	**374**	**-**	**-**	**374**
Total comprehensive income for the period	**-**	**-**	**-**	**374**	**-**	**2,670**	**3,044**
Transactions with owners, recorded directly in equity							
Contributions by and distributions to owners							
Sale of financial assets carried at FVOCI	-	-	-	(394)	-	394	-
Final dividend relating to 2021	-	-	-	-	-	(3,305)	(3,305)
Total contributions by and distributions to owners	**-**	**-**	**-**	**(394)**	**-**	**(2,911)**	**(3,305)**
Balance at 30 June 2022	**154**	**-**	**19**	**959**	**(1,299)**	**200,785**	**200,618**

	Attributable to equity holders of the Group						
	Share capital	Revaluation reserve	Capital redemption reserve	Fair value reserve	Treasury shares	Retained earnings	Total
	£000	£000	£000	£000	£000	£000	£000
Balance at 1 January 2021	**154**	**-**	**19**	**(12,690)**	**(1,299)**	**207,839**	**194,023**
Total comprehensive income for the period							
Profit for the six months ended 30 June 2021	-	-	-	-	-	4,092	4,092
Other comprehensive income, net of income tax							
Changes in the fair value of financial assets at FVOCI*	-	-	-	4,485	-	-	4,485
Tax on other comprehensive income	-	-	-	(17)	-	-	(17)
Total other comprehensive income	**-**	**-**	**-**	**4,468**	**-**	**-**	**4,468**
Total comprehensive income for the period	**-**	**-**	**-**	**4,468**	**-**	**4,092**	**8,560**
Transactions with owners, recorded directly in equity							
Contributions by and distributions to owners							
Sale of Secure Trust Bank Shares	-	-	-	4,611	-	(4,611)	-
Special dividend relating to 2019**	-	-	-	-	-	(3,155)	(3,155)
Total contributions by and distributions to owners	**-**	**-**	**-**	**4,611**	**-**	**(7,766)**	**(3,155)**
Balance at 30 June 2021	**154**	**-**	**19**	**(3,611)**	**(1,299)**	**204,165**	**199,428**

* The change in fair value of financial investments of £4.5m is due to the movement in the value of the investment in Secure Trust Bank, as the share price increased from £8.75 at 31 December 2020 to £10.58 at 30 June 2021.
**On 19 March 2021 the Group paid a special dividend of 21p per share to replace the dividend that was withdrawn at the request of the regulators at the outset of the pandemic.

Consolidated Statement of Cash Flows

	Six months ended 30 June 2022 £000	Six months ended 30 June 2021 £000
Cash flows from operating activities		
Interest received	47,590	37,476
Interest paid	(6,669)	(7,162)
Fees and commissions received	10,680	6,397
Net trading and other income	610	2,889
Cash payments to employees and suppliers	(44,754)	(33,949)
Cash flows from operating profits before changes in operating assets and liabilities	7,457	5,651
Changes in operating assets and liabilities:		
- net decrease in derivative financial instruments	(2,421)	630
- net increase in loans and advances to customers	(115,156)	(134,441)
- net decrease in other assets	858	179
- net increase/increase in deposits from banks	-	16
- net (decrease)/increase in amounts due to customers	(36,339)	277,554
- net increase / (decrease) in other liabilities	(10,076)	6,815
Net cash (outflow)/inflow from operating activities	**(155,677)**	**156,404**
Cash flows from investing activities		
Purchase of financial investments	(4)	(94)
Disposal of financial investments	536	11,650
Purchase of computer software	(2,840)	(2,227)
Purchase of property, plant and equipment	(35,822)	(13,575)
Proceeds from sale of property, plant and equipment	23,668	7,219
Purchase of Asset Alliance Group Holdings Limited	-	(9,998)
Cash balance acquired through Asset Alliance Group Holdings Limited acquisition	-	3,883
Purchases of debt securities	(286,424)	(343,137)
Proceeds from redemption of debt securities	210,408	294,790
Net cash outflow from investing activities	**(90,478)**	**(51,489)**
Cash flows from financing activities		
Decrease in borrowings	-	(127,918)
Dividends paid	(3,305)	(3,155)
Net cash used in financing activities	**(3,305)**	**(131,073)**
Net (decrease)/increase in cash and cash equivalents	(249,460)	(26,158)
Cash and cash equivalents at 1 January	888,136	747,066
Cash and cash equivalents at 30 June	**638,676**	**720,908**

Notes to the Consolidated Financial Statements

1. Basis of preparation

The interim financial statements have been prepared on the basis of accounting policies set out in the Group's 2021 statutory accounts as amended by UK-adopted standards and interpretations effective during 2022 as set out below and in accordance with IAS 34 "Interim Financial Reporting" as adopted for use in the UK. The directors do not consider the fair value of the assets and liabilities presented in these financial statements to be materially different from their carrying value.

The statements were approved by the Board of Directors on 18 July 2022 and are unaudited. The interim financial statements will be available on the Group website (www.arbuthnotgroup.com) from 20 July 2022.

2. 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 4.

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

Reputational risk

Reputational risk is the risk to the Group from a failure to meet reasonable stakeholder expectations as a result of any event, behaviour, action or inaction by ABG itself, its employees or those with whom it is associated. This includes the associated risk to earnings, capital or liquidity.

ABG seeks to ensure that all of it businesses act consistently with the seven corporate principles as laid out on page 1 of the Annual Report and Accounts. This is achieved through a central Risk Management framework and supporting policies, the application of a three-lines of defence model across the Group and oversight by various committees. Employees are supported in training, studies and other ways and encouraged to live out the cultural values within the Group of integrity, energy and drive, respect, collaboration and empowerment. In applying the seven corporate principles, the risk of reputational damage is minimised as the Group serves its shareholders, customers and employees with integrity and high ethical standards.

Macroeconomic and competitive environment

The Group is exposed to indirect risks that may arise from the macroeconomic and competitive environment.

Russia Ukraine Conflict

On 24 February 2022 Russia initiated an invasion of neighbouring Ukraine. The global community reacted with a series of severe sanctions against Russia. As a global supplier of commodities the effects of the sanctions and war in the region is undetermined, however, it is likely to have a knock-on effect on global economies and specifically European nations with a reliance on Russian exports. Global financial markets have reacted with falling stock markets along with significant rises in oil and gas prices. Inflation is currently forecast to be significantly higher than recent history. The situation could have significant geopolitical implications, including economic, social and political repercussions on a number of regions that may impact the Group and its customers.

Arbuthnot Latham has always had very limited appetite to have clients with high risk factors, and this includes Russian clients, whether based in or outside of Russia. Well before the invasion of Ukraine, we had classified Russia as a high risk country and we would only take on clients with any links to Russia in exceptional circumstances and where their financial activities were straightforward. We have also never operated a Russian desk. This longstanding approach means our exposure to Russian clients of any description is limited to only seven out of our total client base of six thousand.

For the avoidance of doubt, we have no clients that have been included or mentioned in any of the Government sanctions, and we do not and will not work with individuals or entities that could reasonably be seen to be controlled by, under the influence of, or connected with the Russian regime.

Coronavirus

Uncertainty remains around the impact of possible future COVID-19 variants on both domestic and global economies. The global economic impact from COVID-19 has improved, with developed economies in recovery. The strength of further recovery depends crucially on the degree to which COVID-19 vaccines and treatments allow a return to pre-pandemic levels of economic activity.

Brexit

The Brexit transition period came to an end on 31 December 2020 and the EU and UK agreed the Trade and Cooperation Agreement on 24 December 2020. There is still some uncertainty around the long term consequences of Brexit. Following the closure of the Dubai office during the year, all the Group's income and expenditure is now based in the UK.

Climate change

Climate change presents financial and reputational risks for the banking industry. The Board consider Climate change a material risk as per the Board approved risk appetite framework which provides a structured approach to risk taking within agreed boundaries. The assessment is proportional at present but will develop over time as the Group generates further resources and industry consensus

emerges. The assessment is maintained by the Chief Risk officer and has been informed by the ICAAP review and workshops for employees.

Whilst it is difficult to assess how climate change will unfold, the Group is continually assessing various risk exposures. The UK has a legally binding target to cut its greenhouse gas emissions to "net-zero" by 2050. There is growing consensus that an orderly transition to a low-carbon economy will bring substantial adjustments to the global economy which will have financial implications while bringing risks and opportunities.

The risk assessment process has been integrated into existing risk frameworks and will be governed through the various risk governance structures including review and recommendations by the Arbuthnot Latham Risk Committee. Arbuthnot Latham has been assessed against the Task Force on Climate-related Financial Disclosures' ("TCFD") recommended disclosures and where appropriate the FCA/PRA guidance as per the Supervisory Statements.

In accordance with the requirements of the PRA's Supervisory Statement 'Enhancing banks' and insurers' approaches to managing the financial risks from climate change', the Group has allocated responsibility for identifying and managing the risks from climate change to the relevant existing Senior Management Function. The Bank is continuously developing a suitable strategic approach to climate change and the unique challenges it poses.

The FCA have issued 'Climate Change and Green Finance: summary of responses and next steps'. In addition to the modelling of various scenarios and various governance reviews, the Group will continue to monitor requirements through the relationship with UK Finance.

Strategic risk
Strategic risk is the risk that the Group's ability to achieve its corporate and strategic objectives may be compromised. This risk is particularly 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 Directors normally meet once a year outside a formal Board setting to ensure that the Group's strategy is appropriate for the market and economy.

Credit risk
Credit risk is the risk that a counterparty (borrower) will be unable to pay amounts in full when due. This risk exists in Arbuthnot Latham, which currently has a loan book of £1,990m (30 June 2021: £1,726m). The lending portfolio in Arbuthnot Latham is extended to clients, the majority of which is secured against cash, property or other high quality assets. Credit risk is managed through the Credit Committee of Arbuthnot Latham.

Market risk
Market risk arises in relation to movements in interest rates, currencies, property 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 changes in interest rates.

The Group is exposed to changes in the market value of its properties. The current carrying value of Investment Property is £6.6m (31 December 2021: £6.6m) and properties classified as inventory are carried at £81.2m (31 December 2021: £87.1m). Any changes in the market value of the property will be accounted for in the Income Statement for the Investment Property and could also impact the carrying value of inventory, which is at the lower of cost and net realisable value. As a result, it could have a significant impact on the profit or loss of the Group.

Liquidity risk
Liquidity risk is the risk that the Group, although solvent, either does not have sufficient financial resources to enable it to meet its obligations as they fall due, or can only secure such resources at an excessive cost. 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 Bank. The loan to deposit ratio is maintained at a prudent level, and consequently the Group maintains a high level of liquidity. The Arbuthnot Latham Board annually approves the Internal 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's exposures to operational risk include its Information Technology ("IT") 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.

In line with further guidance issued by the Regulator, the Bank has continued to focus on ensuring that the design of systems and operational plans are robust to maintain operational resilience in the face of unexpected incidents. During 2021 and 2022 the Bank continued to review these plans and undertook tests to ensure backup and recovery processes were effective even when working in a hybrid working model.

During 2021 the FCA, PRA and BoE published their final policy papers on building operational resilience. The Group complied with the initial requirements prior to the implementation date of 31 March 2022.

Cyber risk
Cyber risk is an increasing risk for the Group within its operational processes. It 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 tests 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 clients' complaints effectively, not meeting clients' expectations, and exhibiting behaviours which do not meet market or regulatory standards.

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

Regulatory and capital risk
Regulatory and capital risk includes the risk that the Group will have insufficient capital resources to support the business and/or does not comply with regulatory requirements. The Group adopts a conservative approach to managing its capital. The Board of Arbuthnot Latham 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 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.

3. 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. For a full list of critical accounting estimates and judgements, please refer back to the Annual Report and Accounts for 2021. Assumptions surrounding credit losses are discussed in more detail below, while other critical accounting estimates and judgements have remained unchanged from what was previously reported.

Estimation uncertainty - 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 measurement of ECL required by IFRS 9, 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 Baseline, which is the central scenario, developed internally based on public consensus forecasts, and four less likely scenarios, one upside and three downside scenarios (Downside 1, Downside 2 and Extreme Downside), 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 on a collective basis, grouped together by product and geographical location. The key assumptions are the probability of default, the economic scenarios and loss given default ("LGD") having consideration for collateral. Lifetime 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 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.

The Group considered the impact of various assumptions on the calculation of ECL (changes in GDP, unemployment rates, inflation, exchange rates, equity prices, wages and collateral values/property prices) and concluded that collateral values/property prices, UK GDP and UK unemployment rate are key drivers of credit risk and credit losses for each portfolio of financial instruments.

The five macroeconomic scenarios modelled on future property prices were as follows:

- Baseline
- Upside
- Downside 1 (2021: Decline)
- Downside 2 (2021: Moderate decline)
- Extreme downside (2021: Severe decline)

The tables below therefore reflect the expected probability weightings applied for each macroeconomic scenario:

	Probability weighting	
	Jun-22	Dec-21
Economic Scenarios		
Baseline	53.0%	52.0%
Upside	18.0%	25.0%
Downside 1 (2021: Decline)	20.0%	16.0%
Downside 2 (2021: Moderate decline)	7.0%	5.0%
Extreme downside (2021: Severe decline)	2.0%	2.0%

Due to changes in the UK economic outlook the baseline (central) scenario used at 30 June 2022 is less optimistic than the baseline scenario at 31 December 2021. The tables below show the five-year forecasted average for property prices growth, UK unemployment rate and UK real GDP growth:

	30 June 2022				
	Base	Upside	Downside 1	Downside 2	Extreme downside
Five-year summary					
UK House price index - average growth	2.5%	6.0%	(0.3%)	(2.3%)	(4.4%)
UK Commercial real estate price - average growth	(0.4%)	3.5%	(2.6%)	(2.9%)	(3.2%)
UK Unemployment rate - average	4.1%	3.8%	5.5%	7.4%	9.2%
UK GDP - average growth	1.9%	3.5%	0.9%	0.2%	(0.6%)

	31 December 2021				
	Base	Upside	Decline	Moderate Decline	Severe Decline
Five-year summary					
UK House price index - average growth	2.0%	5.6%	(0.7%)	(2.8%)	(4.8%)
UK Commercial real estate price - average growth	1.4%	5.1%	(1.2%)	(1.8%)	(2.4%)
UK Unemployment rate - average	4.2%	3.8%	5.7%	7.5%	9.4%
UK GDP - average growth	2.3%	3.9%	1.3%	0.6%	(0.1%)

The tables below list the macroeconomic assumptions at 30 June 2022 used in the base, upside and downside scenarios over the five-year forecast period. The assumptions represent the absolute percentage unemployment rates and year-on-year percentage change for GDP and property prices.

UK House price index - four quarter growth

Year	Baseline	Upside	Downside 1	Downside 2	Extreme downside
2022	5.1%	8.8%	(2.8%)	(7.2%)	(11.7%)
2023	1.9%	5.6%	(4.5%)	(10.8%)	(17.2%)
2024	2.0%	5.4%	(0.9%)	(3.8%)	(6.8%)
5 year average	2.5%	6.0%	(0.3%)	(2.3%)	(4.4%)

UK Commercial real estate price - four quarter growth

Year	Baseline	Upside	Downside 1	Downside 2	Extreme downside
2022	(0.2%)	4.2%	(14.5%)	(19.1%)	(23.7%)
2023	(1.0%)	3.9%	(3.4%)	(5.9%)	(8.4%)
2024	(0.2%)	3.5%	1.9%	4.0%	6.0%
5 year average	(0.4%)	3.5%	(2.6%)	(2.9%)	(3.2%)

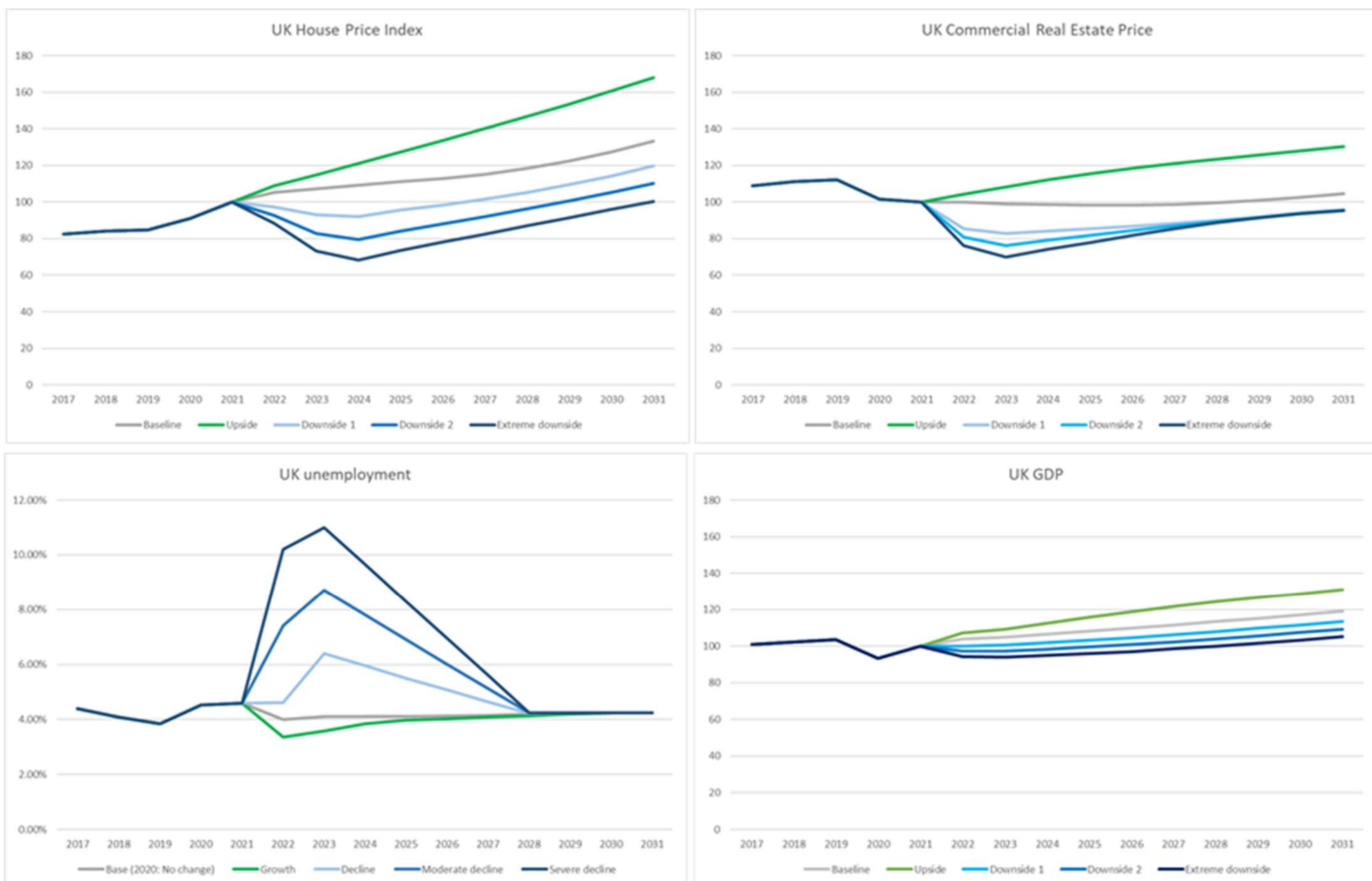
UK Unemployment rate - annual average

Year	Baseline	Upside	Downside 1	Downside 2	Extreme downside
2022	4.0%	3.4%	4.6%	7.4%	10.2%
2023	4.1%	3.6%	6.4%	8.7%	11.0%
2024	4.1%	3.8%	6.0%	7.8%	9.7%
5 year average	4.1%	3.8%	5.5%	7.4%	9.2%

UK GDP - annual growth

Year	Baseline	Upside	Downside 1	Downside 2	Extreme downside
2022	3.8%	7.2%	(0.1%)	(2.8%)	(5.6%)
2023	1.0%	1.9%	0.5%	0.0%	(0.5%)
2024	1.6%	3.0%	1.4%	1.2%	0.9%
5 year average	1.9%	3.5%	0.9%	0.2%	(0.6%)

The graphs below plot the historical data for HPI, Commercial real estate price, unemployment rate and GDP growth rate in the UK as well as the forecasted data under each of the five scenarios.



Management have assessed the impact of assigning a 100% probability to each of the economic scenarios, which would have the following impact on the Profit or Loss of the Group:

Impact of 100% scenario probability	Arbuthnot Latham Jun 2022 £m	 Dec 2021 £m
Baseline	0.2	0.1
Upside	0.3	0.1
Downside 1 (2021: Decline)	(1.0)	(0.8)
Downside 2 (2021: Moderate decline)	(6.8)	(4.0)
Extreme downside (2021: Severe decline)	(28.7)	(13.6)

4. 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, macroeconomic, market, liquidity and capital.

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 Committee regularly reviews the credit risk profile of the Group, with a clear focus on performance against risk appetite statements and risk metrics. The Committee considered credit conditions during the period.

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 has attempted to leverage stress test modelling insights to inform ECL model refinements to enable reasonable estimates. Management review of modelling approaches and outcomes continues to inform any necessary adjustments to the ECL estimates through the form of in-model adjustments, based on expert judgement including the use of available information. Management considerations included the potential severity and duration of the economic shock, including the mitigating effects of government support actions, as well the potential trajectory of the subsequent recovery.

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:

- assessment of significant increase in credit risk
- future economic scenarios
- probability of default
- loss given default
- exposure at default

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

The Group's maximum exposure to credit risk (net of impairment) before collateral held or other credit enhancements is as follows:

Group	30 June 2022							
	Banking	Mortgage Portfolios	RAF	ACABL	ASFL	AAG	All Other Divisions	Total
Credit risk exposures (all stage 1, unless otherwise stated)	£000	£000	£000	£000	£000	£000	£000	£000
On-balance sheet:								
Cash and balances at central banks	-	-	-	-	-	-	512,663	512,663
Loans and advances to banks	-	-	-	-	-	-	125,839	125,839
Debt securities at amortised cost	-	-	-	-	-	-	386,880	386,880
Derivative financial instruments	-	-	-	-	-	-	4,165	4,165
Loans and advances to customers at amortised cost	1,448,851	166,168	102,612	238,843	9,590	13,473	-	1,979,537
Stage 1 - Gross amount outstanding	1,359,839	140,170	87,420	238,980	9,053	13,473	-	1,848,935
Stage 1 - Allowance for impairment	(229)	(15)	(90)	(137)	(42)	-	-	(513)
Stage 2 - Gross amount outstanding	60,041	21,279	12,318	-	-	-	-	93,638
Stage 2 - Allowance for impairment	(4)	(10)	(114)	-	-	-	-	(128)
Stage 3 - Gross amount outstanding	30,535	4,814	3,571	-	683	-	-	39,603
Stage 3 - Allowance for impairment	(1,331)	(70)	(493)	-	(104)	-	-	(1,998)
Loans and advances to customers at fair value through profit or loss	-	-	-	-	-	-	10,330	10,330
Other assets	-	-	-	-	-	-	12,763	12,763
Financial investments	-	-	-	-	-	-	2,970	2,970
Off-balance sheet:								
Guarantees	3,427	-	-	-	-	-	-	3,427
Loan commitments	282,901	-	-	68,880	1,844	-	-	353,625
At 30 June 2022	**1,735,179**	**166,168**	**102,612**	**307,723**	**11,434**	**13,473**	**1,055,610**	**3,392,199**

Group	30 June 2021							
	Banking	Mortgage Portfolios	RAF	ACABL	ASFL	AAG	All Other Divisions	Total
Credit risk exposures (all stage 1, unless otherwise stated)	£000	£000	£000	£000	£000	£000	£000	£000
On-balance sheet:								
Cash and balances at central banks	-	-	-	-	-	-	615,832	615,832
Loans and advances to banks	-	-	-	-	-	-	104,904	104,904
Debt securities at amortised cost	-	-	-	-	-	-	391,987	391,987
Derivative financial instruments	-	-	-	-	-	-	850	850
Loans and advances to customers	1,278,305	195,108	93,032	147,913	7,530	4,583	-	1,726,471
Stage 1 - Gross amount outstanding	1,194,660	173,299	76,336	147,987	7,547	4,583	-	1,604,412
Stage 1 - Allowance for impairment	(384)	(8)	(223)	(74)	(17)	-	-	(706)
Stage 2 - Gross amount outstanding	60,472	17,576	15,921	-	-	-	-	93,969
Stage 2 - Allowance for impairment	(148)	(44)	(135)	-	-	-	-	(327)
Stage 3 - Gross amount outstanding	26,817	4,409	1,537	-	-	-	-	32,763
Stage 3 - Allowance for impairment	(3,112)	(124)	(404)	-	-	-	-	(3,640)
Other assets	-	-	-	-	-	-	15,827	15,827
Financial investments	-	-	-	-	-	-	11,407	11,407
Off-balance sheet:								
Guarantees	3,149	-	-	-	-	-	-	3,149
Loan commitments	230,876	-	-	74,331	1,729	-	-	306,936
At 30 June 2021	**1,512,330**	**195,108**	**93,032**	**222,244**	**9,259**	**4,583**	**1,140,807**	**3,177,363**

Group	Banking	Mortgage Portfolios	RAF	ACABL	ASFL	AAG	All Other Divisions	Total
	31 December 2021							
Credit risk exposures (all stage 1, unless otherwise stated)	£000	£000	£000	£000	£000	£000	£000	£000
On-balance sheet:								
Cash and balances at central banks	-	-	-	-	-	-	814,499	814,499
Loans and advances to banks	-	-	-	-	-	-	73,444	73,444
Debt securities at amortised cost	-	-	-	-	-	-	301,052	301,052
Derivative financial instruments	-	-	-	-	-	-	1,753	1,753
Loans and advances to customers	1,396,049	178,082	97,112	182,122	10,097	7,500	-	1,870,962
Stage 1 - Gross amount outstanding	1,297,782	157,566	82,952	182,213	9,896	7,500	-	1,737,909
Stage 1 - Allowance for impairment	(157)	(5)	(107)	(91)	(28)	-	-	(388)
Stage 2 - Gross amount outstanding	70,132	13,728	11,374	-	229	-	-	95,463
Stage 2 - Allowance for impairment	(32)	(9)	(36)	-	-	-	-	(77)
Stage 3 - Gross amount outstanding	31,475	6,859	5,643	-	-	-	-	43,977
Stage 3 - Allowance for impairment	(3,151)	(57)	(2,714)	-	-	-	-	(5,922)
Other assets	-	-	-	-	-	-	13,098	13,098
Financial investments	-	-	-	-	-	-	3,169	3,169
Off-balance sheet:								
Guarantees	2,931	-	-	-	-	1,629	-	4,560
Loan commitments	261,797	-	-	200,478	2,115	-	-	464,390
At 31 December 2021	**1,660,777**	**178,082**	**97,112**	**382,600**	**12,212**	**9,129**	**1,207,015**	**3,546,927**

Market risk

Market risk arises in relation to movements in interest rates, currencies, property 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 changes in interest rates.

The Group is exposed to changes in the market value of its properties. The current carrying value of Investment Property is £6.6m (31 December 2021: £6.6m) and properties classified as inventory are carried at £81.2m (31 December 2021: £87.1m). Any changes in the market value of the property will be accounted for in the Income Statement for the Investment Property and could also impact the carrying value of inventory, which is at the lower of cost and net realisable value. As a result, it could have a significant impact on the profit or loss of the Group.

Liquidity risk

Liquidity risk is the risk that the Group, although solvent, either does not have sufficient financial resources to enable it to meet its obligations as they fall due, or can only secure such resources at an excessive cost. 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 Bank. The loan to deposit ratio is maintained at a prudent level, and consequently the Group maintains a high level of liquidity. The Arbuthnot Latham Board annually approves the Internal 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.

Capital management

During the period all regulated entities have complied with all of the externally imposed capital requirements to which they are subject. The capital position of the Group remains strong. The Total Capital Requirement Ratio ("TCR") is 8.32% (31 December 2021: 8.69%), while the CET1 capital ratio is 11.4% (31 December 2021: 12.3%) and the total capital ratio is 14.0% (31 December 2021: 14.9%).

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 30 June 2022	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Derivative financial instruments	-	4,165	-	4,165
Loans and advances to customers at fair value through profit or loss	-	-	10,330	10,330
Financial investments	-	-	2,970	2,970
Investment properties	-	-	6,550	6,550
	-	**4,165**	**19,850**	**24,015**
LIABILITIES				
Derivative financial instruments	-	162	-	162
	-	**162**	**-**	**162**

At 30 June 2021	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Derivative financial instruments	-	850	-	850
Financial investments	8,671	-	2,736	11,407
Investment properties	-	-	6,550	6,550
	8,671	**850**	**9,286**	**18,807**
LIABILITIES				
Derivative financial instruments	-	286	-	286
	-	**286**	**-**	**286**

At 31 December 2021	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Derivative financial instruments	-	1,753	-	1,753
Financial investments	-	-	3,169	3,169
Investment properties	-	-	6,550	6,550
	-	**1,753**	**9,719**	**11,472**
LIABILITIES				
Derivative financial instruments	-	171	-	171
	-	**171**	**-**	**171**

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	At 30 June 2022 £000	At 30 June 2021 £000	At 31 December 2021 £000
At 1 January	9,719	9,120	9,120
Acquisitions	10,334	89	670
Disposals	(536)	-	-
Movements recognised in Other Comprehensive Income	333	89	(57)
Movements recognised in the Income Statement	-	(12)	(14)
At 30 June / 31 December	**19,850**	**9,286**	**9,719**

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

At 30 June 2022	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Cash and balances at central banks	-	512,837	-	512,837
Loans and advances to banks	-	125,839	-	125,839
Debt securities at amortised cost	-	386,880	-	386,880
Loans and advances to customers	-	-	1,989,867	1,989,867
Other assets	-	-	12,989	12,989
	-	**1,025,556**	**2,002,856**	**3,028,412**
LIABILITIES				
Deposits from banks	-	230,110	-	230,110
Deposits from customers	-	2,801,530	-	2,801,530
Other liabilities	-	-	24,634	24,634
Debt securities in issue	-	-	37,158	37,158
	-	**3,031,640**	**61,792**	**3,093,432**

At 30 June 2021	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Cash and balances at central banks	-	616,004	-	616,004
Loans and advances to banks	-	104,904	-	104,904
Debt securities at amortised cost	-	391,987	-	391,987
Loans and advances to customers	-	-	1,726,471	1,726,471
Other assets	-	-	16,058	16,058
	-	**1,112,895**	**1,742,529**	**2,855,424**
LIABILITIES				
Deposits from banks	-	230,106	-	230,106
Deposits from customers	-	2,642,761	-	2,642,761
Other liabilities	-	-	33,495	33,495
Debt securities in issue	-	-	37,089	37,089
	-	**2,872,867**	**70,584**	**2,943,451**

At 31 December 2021	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Cash and balances at central banks	-	814,692	-	814,692
Loans and advances to banks	-	73,444	-	73,444
Debt securities at amortised cost	-	301,052	-	301,052
Loans and advances to customers	-	-	1,870,962	1,870,962
Other assets	-	-	11,375	11,375
	-	**1,189,188**	**1,882,337**	**3,071,525**
LIABILITIES				
Deposits from banks	-	240,333	-	240,333
Deposits from customers	-	2,837,869	-	2,837,869
Other liabilities	-	-	7,106	7,106
Debt securities in issue	-	-	36,772	36,772
	-	**3,078,202**	**43,878**	**3,122,080**

All above assets and liabilities are carried at amortised cost. Therefore for these assets, the fair value hierarchy noted above relates to the disclosure in this note only.

Cash and balances at central banks
The fair value of cash and balances at central banks was calculated based upon the present value of the expected future principal and interest cash flows. The rate used to discount the cash flows was the market rate of interest at the balance sheet date.

At the end of each year, the fair value of cash and balances at central banks was calculated to be equivalent to their carrying value.
Loans and advances to banks
The fair value of loans and advances to banks was calculated based upon the present value of the expected future principal and interest cash flows. The rate used to discount the cash flows was the market rate of interest at the balance sheet date.

Loans and advances to customers
The fair value of loans and advances to customers was calculated based upon the present value of the expected future principal and interest cash flows. The rate used to discount the cash flows was the market rate of interest at the balance sheet date, and the same assumptions regarding the risk of default were applied as those used to derive the carrying value.

The Group provides loans and advances to commercial, corporate and personal customers at both fixed and variable rates. To determine the fair value of loans and advances to customers, loans are segregated into portfolios of similar characteristics. A number of techniques are used to estimate the fair value of fixed rate lending; these take account of expected credit losses based on historic trends and expected future cash flows.

For the acquired loan book, the discount on acquisition is used to determine the fair value in addition to the expected credit losses and expected future cash flows.

Debt securities
The fair value of debt securities is based on the quoted mid-market share price.

Derivatives
Where derivatives are traded on an exchange, the fair value is based on prices from the exchange.

Deposits from banks
The fair value of amounts due to banks was calculated based upon the present value of the expected future principal and interest cash flows. The rate used to discount the cash flows was the market rate of interest at the balance sheet date.

At the end of each year, the fair value of amounts due to banks was calculated to be equivalent to their carrying value due to the short maturity term of the amounts due.

Deposits from customers
The fair value of deposits from customers was calculated based upon the present value of the expected future principal and interest cash flows. The rate used to discount the cash flows was the market rate of interest at the balance sheet date for the notice deposits and deposit bonds. The fair value of instant access deposits is equal to book value as they are repayable on demand.

Financial liabilities
The fair value of other financial liabilities was calculated based upon the present value of the expected future principal cash flows.

At the end of each year, the fair value of other financial liabilities was calculated to be equivalent to their carrying value due to their short maturity. The other financial liabilities include all other liabilities other than non-interest accruals.

Subordinated liabilities
The fair value of subordinated liabilities was calculated based upon the present value of the expected future principal cash flows.

5. Operating segments

The Group is organised into eight operating segments as disclosed below:

1) Banking – Includes Private and Commercial Banking. Private Banking – Provides traditional private banking services. Commercial Banking – Provides bespoke commercial banking services and tailored secured lending against property investments and other assets.
2) Wealth Management – Offering financial planning and investment management services.
3) Mortgage Portfolios – Acquired mortgage portfolios.
4) RAF – Specialist asset finance lender mainly in high value cars but also business assets.
5) ACABL – Provides finance secured on either invoices, assets or stock of the borrower.
6) ASFL – Provides short term secured lending solutions to professional and entrepreneurial property investors.
7) AAG – Provides vehicle finance and related services, predominantly in the truck & trailer and bus & coach markets.
8) All Other Divisions – All other smaller divisions and central costs in Arbuthnot Latham & Co., Ltd (Investment property and Central costs).
9) Group Centre – ABG Group 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.

Six months ended 30 June 2022	Banking £000	Wealth Management £000	Mortgage Portfolios £000	RAF £000	ACABL £000	ASFL £000	AAG £000	All Other Divisions £000	Group Centre £000	**Total £000**
Interest revenue	29,635	-	3,250	4,086	5,818	463	253	5,583	2	**49,090**
Inter-segment revenue	-	-	-	-	-	-	-	-	(2)	**(2)**
Interest revenue from external customers	29,635	-	3,250	4,086	5,818	463	253	5,583	-	**49,088**
Fee and commission income	1,564	5,332	-	138	2,670	5	-	390	-	**10,099**
Revenue	-	-	-	-	-	-	48,851	-	-	**48,851**
Revenue from external customers	**31,199**	**5,332**	**3,250**	**4,224**	**8,488**	**468**	**49,104**	**5,973**	**-**	**108,038**
Interest expense	(1,613)	-	(882)	(1,547)	(2,696)	(170)	(1,994)	3,746	(1,398)	**(6,554)**
Cost of goods sold	-	-	-	-	-	-	(40,538)	-	-	**(40,538)**
Add back inter-segment revenue	-	-	-	-	-	-	-	-	2	**2**
Fee and commission expense	14	-	-	-	(73)	-	-	-	-	**(59)**
Segment operating income	29,600	5,332	2,368	2,677	5,719	298	6,572	9,719	(1,396)	**60,889**
Impairment losses	(221)	-	(49)	(465)	(46)	(117)	(303)	-	-	**(1,201)**
Other income	-	-	-	69	-	-	(182)	723	-	**610**
Operating expenses	(22,804)	(7,171)	(481)	(2,124)	(2,790)	(751)	(7,155)	(9,198)	(4,449)	**(56,923)**
Segment profit / (loss) before tax	6,575	(1,839)	1,838	157	2,883	(570)	(1,068)	1,244	(5,845)	**3,375**
Income tax (expense) / income	-	-	-	-	-	-	-	624	(1,329)	**(705)**
Segment profit / (loss) after tax	**6,575**	**(1,839)**	**1,838**	**157**	**2,883**	**(570)**	**(1,068)**	**1,868**	**(7,174)**	**2,670**
Loans and advances to customers	1,459,182	-	166,168	102,612	238,843	9,590	13,473	11,500	(11,501)	**1,989,867**
Assets available for lease	-	-	-	-	-	-	115,133	-	-	**115,133**
Other assets	-	-	-	-	-	-	-	1,206,288	(1,472)	**1,204,816**
Segment total assets	**1,459,182**	**-**	**166,168**	**102,612**	**238,843**	**9,590**	**128,606**	**1,217,788**	**(12,973)**	**3,309,816**
Customer deposits	2,611,542	-	-	-	-	-	-	207,735	(17,747)	**2,801,530**
Other liabilities	-	-	-	-	-	-	-	292,414	15,254	**307,668**
Segment total liabilities	**2,611,542**	**-**	**-**	**-**	**-**	**-**	**-**	**500,149**	**(2,493)**	**3,109,198**
Other segment items:										
Capital expenditure	-	-	-	(5)	-	-	(35,612)	(205)	-	**(35,822)**
Depreciation and amortisation	-	-	-	(3)	-	(25)	(15,015)	(2,480)	(8)	**(17,531)**

The "Group Centre" segment above includes the parent entity and all intercompany eliminations.

Six months ended 30 June 2021	Banking £000	Wealth Management £000	Mortgage Portfolios £000	RAF £000	ACABL £000	ASFL £000	AAG £000	All Other Divisions £000	Group Centre £000	**Total £000**
Interest revenue	22,634	-	3,732	4,049	3,471	293	70	2,474	9	**36,732**
Inter-segment revenue	-	-	-	-	-	-	-	-	(9)	**(9)**
Interest revenue from external customers	22,634	-	3,732	4,049	3,471	293	70	2,474	-	**36,723**
Fee and commission income	1,178	5,080	-	26	2,043	5	-	450	-	**8,782**
Revenue	-	-	-	-	-	-	23,190	-	-	**23,190**
Revenue from external customers	**23,812**	**5,080**	**3,732**	**4,075**	**5,514**	**298**	**23,260**	**2,924**	**-**	**68,695**
Interest expense	(2,086)	-	(1,104)	(1,123)	(1,148)	(94)	(891)	977	(964)	**(6,433)**
Cost of goods sold	-	-	-	-	-	-	(20,346)	-	-	**(20,346)**
Add back inter-segment revenue	-	-	-	-	-	-	-	-	9	**9**
Subordinated loan note interest	-	-	-	-	-	-	-	-	(360)	**(360)**
Fee and commission expense	(158)	-	-	-	(19)	-	-	-	-	**(177)**
Segment operating income	21,568	5,080	2,628	2,952	4,347	204	2,023	3,901	(1,315)	**41,388**
Impairment losses	(42)	-	(289)	(92)	(33)	(9)	(400)	-	-	**(865)**
Gain from a bargain purchase	-	-	-	-	-	-	8,656	-	-	**8,656**
Other income	-	-	2,239	43	-	-	-	754	(147)	**2,889**
Operating expenses	(21,433)	(6,512)	(673)	(1,923)	(2,519)	(765)	(2,393)	(8,126)	(4,686)	**(49,030)**
Segment profit / (loss) before tax	93	(1,432)	3,905	980	1,795	(570)	7,886	(3,471)	(6,148)	**3,038**
Income tax (expense) / income	-	-	-	(186)	-	-	-	1,240	-	**1,054**
Segment profit / (loss) after tax	**93**	**(1,432)**	**3,905**	**794**	**1,795**	**(570)**	**7,886**	**(2,231)**	**(6,148)**	**4,092**
Loans and advances to customers	1,279,747	-	195,108	93,033	147,913	7,530	-	11,500	(8,360)	**1,726,471**
Other assets	-	-	-	-	-	-	-	1,427,285	2,226	**1,429,511**
Segment total assets	**1,279,747**	**-**	**195,108**	**93,033**	**147,913**	**7,530**	**-**	**1,438,785**	**(6,134)**	**3,155,982**
Customer deposits	2,427,066	-	-	-	-	-	-	251,119	(35,424)	**2,642,761**
Other liabilities	-	-	-	-	-	-	-	300,310	14,296	**314,606**
Segment total liabilities	**2,427,066**	**-**	**-**	**-**	**-**	**-**	**-**	**551,429**	**(21,128)**	**2,957,367**
Other segment items:										
Capital expenditure	-	-	-	(5)	-	-	(12,557)	(131)	-	**(12,693)**
Depreciation and amortisation	-	-	-	(5)	(11)	(6)	-	(880)	(13)	**(915)**

Segment profit is shown prior to any intra-group eliminations.

6. Underlying Profit

The Group has reported a profit before tax of £3.4m (2021 H1: £3.0m). The underlying profit before tax was £10.7m (2021 H1: profit of £6.5m). There are a number of specific one-off items which are included in the results that should be noted. These are detailed in the table below.

Underlying profit reconciliation	30 June 2022 £000	30 June 2021 £000
Profit before tax and group recharges	3,375	3,038
Exceptional reduction in BoE Base Rate	-	5,746
Write down of repossessed property in Majorca	-	3,835
Gain on sale of Tay mortgage portfolio	-	(2,239)
Gain from bargain purchase	-	(8,626)
Profits earned on sale of trucks included in bargain purchase	3,328	1,547
Full year discretionary bonus accrual in first half of the year	-	3,240
Write down of King Street property	3,977	-
Underlying profit	**10,680**	**6,541**

The Bank of England Base Rate which was at 0.1% for most of 2021 was estimated to have cost the Group £5.7m of interest earnings in H1 2021, compared to when the base rate was at 75 basis points, which is where it was prior to the onset of the COVID-19 pandemic. No pro-rata adjustment was made for lost interest income in H1 2022. The base rate started to increase during the period and has now moved past the pre-pandemic level.

Included in H1 2021 was a write down of £3.8m relating to a property owned in Majorca, following an agreement to sell.

During H1 2021 the Group completed the sale of one of its residential mortgage portfolios known as Tay Mortgages to 5D Finance Limited, a subsidiary of OneSavings Bank plc. The portfolio consisted of the remaining mortgage accounts from the acquisition made in December 2014 related to the Dunfermline Building Society administration. At the time of sale customer loan balances totalled £54.9m, which were sold for £53.8m, representing 97.9% of the outstanding loans. Upon sale the Group released a credit to the profit and loss account for the remaining original discount resulting in a gain on sale of £2.2m.

During the prior year the Group acquired Asset Alliance Group Holdings Limited, which completed on 1 April 2021. The business was acquired at a discount to its fair valued net assets resulting in a bargain purchase of £8.7m in the first half of 2021.

The forgone profit on the sale of trucks generated by Asset Alliance was £3.3m in the period (30 June 2021: £1.5m), which is required from the acquisition accounting in the prior year. The fair value adjustments to individual assets at acquisition are reversed through profit or loss at the point of sale.

In 2020, as a result of the Group reporting a loss, no discretionary bonuses were awarded to staff. However, in H1 2021 with a return to profitability, the annual equivalent of £6.5m was accrued. Under normal circumstances bonuses would be accrued over a twelve-month period, thereby increasing reported profit by £3.2m.

The net realisable value of the property in King Street was reduced by £4.0m resulting from the agreement, subject to contract, to sell the property.

7. Other income

In H1 2021, other income mainly includes the profit on sale of the Tay Mortgage portfolio of £2.2m. Other income also includes rental income received from properties of £0.7m (2021: £0.2m).

8. 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 15,022,629 (2021: 15,022,629) in issue during the period.

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 period, as well as the number of dilutive share options in issue during the period. There were no dilutive share options in issue at the end of June (2021: nil).

Profit attributable	Six months ended 30 June 2022 £000	Six months ended 30 June 2021 £000
Total profit after tax attributable to equity holders of the Company	2,670	4,092

Basic Earnings per share	Six months ended 30 June 2022 p	Six months ended 30 June 2021 p
Total Basic Earnings per share	17.8	27.2

9. Acquisition of Asset Alliance Group Holdings Limited

On 31 March 2021, following receipt of regulatory approval, Arbuthnot Latham completed the acquisition of 100% of the share capital of AAG from its former owners made up of institutional investors and the key management team.

AAG provides vehicle finance and related services, predominantly in the truck & trailer and bus & coach markets. Operating from five locations, it is the UK's leading independent end-to-end specialist in commercial vehicle financing and has over 4000 vehicles under management.

The acquisition supported AL's continued strategy to diversify its proposition within the specialist financial services sector.

The consideration was paid in full in cash following completion. AL has also provided an intercompany loan to AAG at completion of £127.9m to re-finance its existing finance liabilities. The consideration and the refinancing of AAG's funding liabilities have been satisfied from the Group's current cash resources.

The share capital was acquired at a discount to the fair value of net assets resulting in a bargain purchase gain recognised in the Statement of Comprehensive Income on acquisition as set out in the table on the next page. The fair value of intangibles acquired include £3.5m for the brand.

The acquisition contributed £0.1m to interest income and £8.6m to profit before tax in the prior period.

	Acquired assets/ liabilities £000	Fair value adjustments £000	Recognised values on acquisition £000
Loans and advances to banks	3,883	-	3,883
Loans and advances to customers	4,226	-	4,226
Other assets	12,159	-	12,159
Deferred tax assets	-	2,111	2,111
Intangible assets	1,583	2,837	4,420
Property, plant and equipment	120,631	17,057	137,688
Total assets	142,482	22,005	164,487
Deposits from banks	127,918	-	127,918
Deferred tax liabilities	-	3,906	3,906
Corporation tax liability	-	2	2
Other liabilities	14,007	-	14,007
Total liabilities	**141,925**	**3,908**	**145,833**
Net identifiable (liabilities) / assets	**557**	**18,097**	**18,654**
Consideration			9,998
Negative Goodwill / Bargain Purchase			**(8,656)**

10. Events after the balance sheet date

There were no material post balance sheet events to report.