



ARBUTHNOT BANKING GROUP PLC

20 July 2021

ARBUTHNOT BANKING GROUP PLC (“Arbuthnot”, “the Company”, “the Group” or “ABG”)

Unaudited results for the six months to 30 June 2021

and

Interim Dividend Declaration

Arbuthnot Banking Group PLC is pleased to announce a half yearly profit before tax of £3.0m compared to £0.2m in the prior year.

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

FINANCIAL HIGHLIGHTS

- Profit before tax of £3.0m (30 June 2020: £0.2m)
- Net bargain purchase from the acquisition of Asset Alliance Group Holdings Ltd (“Asset Alliance”) of £8.7m*
- Special dividend paid in March of 21p per share
- Second interim dividend declared of 16p per share
- Capital surplus of £52.8m (31 December 2020: £84.2m)
- CET1 capital ratio of 12.5% (31 December 2020: 15.4%) and total capital ratio of 15.2% (31 December 2020: 18.7%)
- Liquidity surplus of £526m in excess of the minimum regulatory requirement
- Earnings per share 27.2p (30 June 2020: 0.9p)
- Net assets per share of £12.92 (30 June 2020: £12.48; 31 December 2020: £12.70)

OPERATIONAL HIGHLIGHTS

- Customer loans of £1,726m (30 June 2020: £1,565m; 31 December 2020: £1,536m)** increased by 12% in the first half of the year
- Completed the acquisition of Asset Alliance with integration progressing well, adding £132.3m of leased assets to the balance sheet
- Customer deposits of £2,643m (30 June 2020: £2,207m; 31 December 2020: £2,365m) increased by 12% in the first half of the year
- Assets under management £1,223m (30 June 2020: £1,074m; 31 December 2020: £1,147m) increased by 7% in the first half of the year
- Accredited in March 2021 to provide Government supported Recovery Loans “RLS”

*The net bargain purchase is recorded in the Income Statement and is the difference between the £10m purchase price paid for Asset Alliance and the adjusted fair value of the assets and liabilities of the business, which totalled £18.7m. This may be subject to further review and revision in the remaining months of the year.

**Comparative results adjusted for the sale of Tay residential mortgage portfolio that was sold in February 2021

Commenting on the results, Sir Henry Angest, Chairman and Chief Executive of Arbuthnot, said: **“During the first half of 2021 the Group has returned to growth across its businesses and restored profitability despite the ongoing low interest rate environment. The acquisition of Asset Alliance is a significant step in our strategy to diversify further through the development of specialist commercial finance businesses. The declaration of an interim dividend at the same level as in 2019 is an indication of our confidence for the future prospects of the Group.”**

Interim Dividend

The interim dividend of 16p per share will be paid on 24 September 2021 to shareholders on the register at the close of business on 27 August 2021.

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 Market Abuse Regulations (EU) No. 596/2014 which is part of UK law by virtue of the European Union (Withdrawal) Act 2018. Upon the publication of this announcement, this is now considered to be in the public domain.

ENQUIRIES:

Arbuthnot Banking Group

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Sir Henry Angest, Chairman and Chief Executive
Andrew Salmon, Group Chief Operating Officer
James Cobb, Group Finance Director

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Chairman's Statement

Arbuthnot Banking Group PLC

The Group has made a good start to the year with progress being made in all of the businesses. This, despite the fact that the majority of the Group's employees have remained working remotely throughout the first six months of the year.

Following our decision in March 2020 to effectively cease lending, our balance sheet saw no growth along with reduced levels of new loan originations. This situation has reversed in 2021 with new loan originations in the first six months totalling £392.3m. This resulted in the Group's customer loan balances increasing by 9% to £1.73bn and in addition to this we now have £132.3m of leased assets following the acquisition of Asset Alliance Group Holdings Limited ("AAGH" or "Asset Alliance") on 31 March 2021. In April Arbuthnot Latham & Co., Limited ("AL" or "Arbuthnot Latham") had total assets in excess of £3.1bn for the first time in its history.

The growth trajectory of the loans together with the leased assets should see the Group end the year with customer assets at the levels we had forecasted for 2021 prior to the pandemic.

The Group's ability to continue to attract quality customer deposits remains key to the future success of our strategy. The Bank made significant progress with this key objective and ended the first half of 2021 with surplus liquidity of £526m in excess of the minimum regulatory requirement of £378m. This is despite funding both the loan book growth and the acquisition of AAGH.

During the first six months, customer deposits grew by 12% from the year-end and 20% from 30 June 2020 to close at £2.64bn. The average cost of deposits now stand at 37 basis points ("bps"), compared to 78bps prior to the reduction in base rate following the start of the pandemic.

The acquisition of AAGH is a significant addition to the Group and complements our continued diversification and a move away from consumer finance to specialist commercial finance.

The final agreed purchase price was £10m and when this is compared to the adjusted fair value of the assets and liabilities of the business, which totalled £18.7m, it results in a bargain purchase of £8.7m which is recorded in the Income Statement. These numbers may be subject to further review and revision in the remaining months of the year.

The most significant fair value adjustment arose from the valuation of the leased truck fleet. The market for second hand trucks has seen large increases in value resulting from the shortage of supply of new trucks, which has been caused by the global scarcity of computer chips used in the manufacture of vehicles. Thus, the adjustment to the asset values was an increase of 15.95% on the carrying value. This totalled approximately £19m. The fact that the truck fleet has effectively been marked to market, resulted in future profit on sale of trucks being recognised upfront and will not therefore re-emerge in the results of AAGH until the back book of trucks has been sold over the next two to three years.

Also, the truck shortage has slowed the ability of AAGH to return to growth, given the new funding supply it now enjoys. AAGH has strong purchasing power and the availability of new trucks is starting to improve, but the relative shortage will delay the business growth plans by 6-12 months.

At the outset of the pandemic we were determined to support the economy in any way we could and accordingly we applied and were accredited to the Government loan schemes; Coronavirus Business Interruption Loan Scheme ("CBILs") and Bounce Back Loan Scheme ("BBLs"). We were pleased in April to also be accredited to the new Government scheme; the Recovery Loan Scheme ("RLS").

In 2020 the Group adjusted its IFRS9 economic scenarios to measure a 5.5% fall in residential property values. This remains unaltered in 2021 despite the increased property values recorded in the first six months of the year. We prefer to remain cautious as we await the impact of the withdrawal of the Government support packages, including the reduction of stamp duty on house purchases.

The Renaissance Asset Finance ("RAF") business continues to monitor its exposure to the London Taxi market, which is showing signs of recovery but remains some way from full capacity. The value of loans under active forbearance measures, excluding re-written loans, now stands at £7.1m, which is down from £15.2m at the year ended 31 December 2020.

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. However, no dividend was paid in respect of earnings for 2020. This seemed an equitable share of the risks and rewards as the employees of the Group received no bonuses or pay rises in the same year.

In trying to restore this equilibrium now that the future prospects of the business are positive, the Group is declaring an interim dividend at the same level as paid in 2019 of 16p per share, to be paid on 24 September 2021 to shareholders on the register at the close of business on 27 August 2021. At the same time, the business has recorded a provision for bonuses at the same level as paid in 2019. It is the Bank's intention to return to fully operational offices in early September, following the relaxation in government guidelines, with measures planned over the summer to ensure a smooth and safe transition for both clients and staff.

Arbuthnot Latham & Co., Limited

Arbuthnot Latham has reported a profit before tax for the first half of the year of £3.0m (30 June 2020: £5.0m).

The Bank has now returned to growth and is restoring its profitability. However, the earnings continue to be held back by the continued low interest rate environment introduced as part of the emergency support package to protect the economy during the pandemic. This low rate has cost the Bank £8.4m in the first six months, assuming a base rate of 75bps.

Total assets of the Bank have increased to £3.16bn (30 June 2020: £2.70bn), an increase of 17%. Customer loans ended the first half at £1.73bn (30 June 2020: £1.62bn), an increase of 7% and 9% higher than the balance reported at the 2020 year-end. During the half year, the Bank originated new loans of £392.3m (30 June 2020: £193m).

The Bank grew its asset base from the year-end despite the sale of the Tay retail mortgage portfolio, which comprised balances totalling £54.9m. The portfolio was sold for a consideration of £53.8m representing 97.9% of customer balances. The portfolio was acquired at a discount in 2014. Upon sale of the portfolio the unamortised discount was realised, resulting in a net profit after professional fees of £2.1m.

Also included in the result is an accrual for staff bonuses of £6.5m. In order to conserve capital during the height of the global pandemic no discretionary bonuses were awarded for the year ending 31 December 2020. However, due to the expected return to profitability for 2021, the Bank intends to reward its staff for their hard work and dedication over the period. Bonuses will be paid after the year-end and in line with the Bank's standard remuneration and award cycle.

The Bank continued to grow its deposit base, ensuring adequate liquidity is maintained following the funding of the Asset Alliance acquisition. As at 30 June 2021, customer deposits were £2.64bn (30 June 2020: £2.21bn), an increase of 20% on the prior year and an increase of 12% from the levels at the 2020 year-end.

Despite the volatility in the markets, Assets under Management ("AuM") increased to £1.22bn (30 June 2020: £1.07bn).

Banking

The Banking division has reported a profit before tax of £0.1m (30 June 2020: profit of £4.8m), with lending balances totalling £1.28bn and deposits of £2.43bn. The reduction in profitability is largely due to bonus accruals which were not included in the prior period.

The business continued to grow in the first half of 2021, transforming prospects and pipeline into client balances whilst supporting its existing clients' aspirations as the economy tentatively emerges from the pandemic.

In the opening months of 2021, new client acquisitions were again greater than the prior year. Growth was generated by both Private and Commercial Banking, whilst at the same time the business continued to support existing clients by providing further banking and wealth planning solutions evidenced through growth across the organisation.

Deposits increased by 12% in the first six months of 2021, diversified broadly across all segments. The division continues to focus on deposit growth for the remainder of 2021, in pursuit of the Bank's client acquisition strategy. A deepening of existing relationships leveraging off the Bank's high touch relationship management approach has generated significant goodwill with clients and is considered more valued than ever.

Deposit pricing fell further compared to the 2020 rates, as pre-pandemic pricing rolled off the book to be replaced at lower rates, however, it is expected that pricing will start to stabilise for the remainder of 2021 as the majority of the higher priced back book matures.

The lending pipeline at the end of 2020 resulted in 13% loan book growth for the first half of 2021. The pipeline remains strong with growth expected to continue for the rest of 2021. The business has continued to maintain its strategy of conservative lending whilst ensuring focus remains on the risk reward profile of potential opportunities. Consequently, there has been a conscious shift towards more residential investment lending versus commercial real estate.

Lending growth has been generated from both Private and Commercial Banking relationships, with high levels of activity from the International and Real Estate teams.

The Dubai branch was closed on 31 May 2021. All existing relationships were successfully migrated to the Bank's London based teams for ongoing client servicing.

Wealth Management

AuM were £1.22bn as at 30 June 2021 (30 June 2020: £1.07bn). Wealth Management generated positive gross inflows over the first six months of 2021, with a 67% increase on the prior year, equating to a 17% annualised gross inflow rate against opening AuM. The client pipeline continues to build positively, with several larger value mandates in development.

The Sustainable Portfolio Service was launched in the second quarter, which utilises the business's central risk framework. The service leverages the underlying research and macro views of the Investment Committee, whilst seeking to maximise exposure to themes that will deliver positive social and environmental outcomes.

Mortgage Portfolios

Mortgage Portfolio balances were £195.1m as at 30 June 2021 (30 June 2020: £300.8m); this balance related entirely to the Santiago portfolio acquired in August 2019, after the Tay portfolio was sold in February 2021.

The portfolio continues to perform to expectation, with forbearance balances following the COVID payment holidays reduced to 0.2% of the total portfolio.

Renaissance Asset Finance ("RAF")

RAF has reported a profit before tax of £1.0m (30 June 2020: £1.0m), with customer loan balances of £93.0m (30 June 2020: £101.4m).

The decline in loan balances seen in 2020, as the result of the combined effects of a drop in demand by SMEs for vehicles and capital equipment, together with a tightened approach to risk, is now showing signs that it has stabilised with an indication of increased demand for asset finance facilities.

Loans under forbearance measures have recovered significantly from the peak 12 months ago. The London taxi market, making up the majority of loan balances under forbearance, is taking longer to recover and remains a key area of focus. The business is optimistic that, as restrictions ease, taxi operators will experience an improvement in activity as social distancing guidelines relax and business and leisure activity increase over the coming months.

The business recorded IFRS9 credit provisions of £0.1m (30 June 2020: £0.3m) for the six months to 30 June 2021.

Arbuthnot Commercial Asset Based Lending ("ACABL")

ACABL has reported a profit before tax of £1.8m (30 June 2020: £0.7m), with funds in use of £147.9m (30 June 2020: £66.5m).

The asset based lending business experienced a strong first half, benefitting from a significant pipeline generated at the end of 2020. The business issued 21 new facilities and had one repayment in the six months to 30 June 2021.

Revenue from servicing fees has grown in line with client activity as businesses increased their revenues following the lows of the previous 12 months. Additionally, as expected, with increased client activity, existing facilities have shown signs of amounts drawn against facility limits increasing to pre-pandemic levels.

Arbuthnot Specialist Finance Limited ("ASFL")

ASFL has made a loss before tax of £0.6m (30 June 2020: loss of £0.5m). Customer loan balances were £7.5m at the half year (30 June 2020: £8.7m).

The business continues to explore opportunities leveraging the lack of liquidity within the non-bank lending sector as the bridging finance market emerges from the lockdown period.

Asset Alliance Group Holdings Limited ("AAGH")

Following the acquisition of AAGH that completed on 31 March 2021, the business reported a profit of £7.9m, including the profit recognised from the bargain purchase. The underlying performance of the business in the three months to 30 June 2021 was £0.8m and additionally included in the results of AL was £0.7m related to the intercompany funding provided to AAGH.

As a result of the acquisition accounting requirements, which in the first case generated a gain of £8.7m via net bargain purchase, there is the requirement to adjust the cost of sales of trucks for the new base cost that will apply to the back book of trucks. This reversed £1.5m of profits. Also included was the amortisation of the brand intangible which totalled £90k in the three month period.

Beside the fair value exercise, which will be completed in the second half of the year, the integration of AAGH into the Group is progressing well.

Owned Properties

At the outset of the pandemic in 2020, the Group commissioned the refurbishment of the West End office building at 20 St Kings Street. This work has now been completed with the cost of works being £1.1m under the original budget. The property is now in the initial stage of marketing and has already generated good interest. We have also noted that yields for West End office space have firmed during 2021.

The Group has for some time had five overseas properties that it acquired as a result of bad debts arising mainly from a specialist lending team that was disbanded several years ago. In 2020 it disposed of a villa in Marbella. Last month an apartment in Ibiza was sold. The Bank has recently accepted an offer on a villa in the South of France, which is expected to complete in the second half of 2021. The offer is such that no further impairment will be required. The house in Barcelona remains subject to a legal dispute and we currently hold a forfeited deposit of one million Euros in respect of this property. The final resolution of this will be dependent on the timings of the Spanish Court that is dealing with the case. The remaining property is located in Majorca. Attempts to sell it have been difficult due to the pandemic and also due to the complexities of local planning issues. Our previous professional valuations may need to be updated following a recent change to local development rules, accordingly we have reduced the carrying value by £2.6m whilst the issues surrounding the planning permissions granted on the property are resolved.

Operations

The Bank continues to operate effectively since the move to remote working, with all services being maintained and good progress made with the Bank's transformation agenda.

As reported at the year-end, the Bank introduced 24 x 7 Faster Payments capability, having previously only transmitted payments during core business hours, improving the client experience and aligning the Arbuthnot Latham proposition with that of the larger retail banks.

The Bank continues to successfully operate remotely. Clients on-boarded during the first half of 2021, were over 10% higher than the same period last year. Levels of client attrition remained low and below the same period in previous years.

Consolidated Statement of Comprehensive Income

		Six months ended 30 June 2021 £000	Six months ended 30 June 2020 £000
	Note		
Income from banking activities			
Interest income		36,723	39,045
Interest expense		(6,784)	(9,337)
Net interest income		29,939	29,708
Fee and commission income		8,782	6,993
Fee and commission expense		(177)	(147)
Net fee and commission income		8,605	6,846
Operating income from banking activities		38,544	36,554
Income from leasing activities			
Revenue		22,533	-
Cost of goods sold		(19,689)	-
Gross profit from leasing activities		2,844	-
Total group operating income		41,388	36,554
Net impairment loss on financial assets		(865)	(1,701)
Other income	6	2,889	420
Profit from bargain purchase	8	8,656	-
Operating expenses		(49,030)	(35,072)
Profit before income tax		3,038	201
Income tax credit / (expense)		1,054	(70)
Profit for the period		4,092	131
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		9,096	(15,832)
Tax on other comprehensive income		(17)	(20)
Other comprehensive income for the period, net of tax		9,079	(15,852)
Total comprehensive income for the period		13,171	(15,721)
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	7	27.2	0.9
Diluted earnings per share	7	27.2	0.9

Consolidated Statement of Financial Position

	At 30 June 2021 £000	At 30 June 2020 £000	At 31 December 2020 £000
ASSETS			
Cash and balances at central banks	616,004	434,761	636,799
Loans and advances to banks	104,904	109,751	110,267
Debt securities at amortised cost	391,987	359,042	344,692
Assets classified as held for sale	3,183	7,617	3,285
Derivative financial instruments	850	1,749	1,843
Loans and advances to customers	1,726,471	1,620,262	1,587,849
Current tax asset	17	-	205
Other assets	110,044	90,010	96,288
Financial investments	11,407	15,310	18,495
Deferred tax asset	420	1,931	1,009
Intangible assets	27,794	22,776	23,646
Property, plant and equipment	140,465	6,849	4,905
Right-of-use assets	16,306	18,527	17,703
Investment properties	6,550	6,763	6,550
Total assets	3,156,402	2,695,348	2,853,536
EQUITY AND LIABILITIES			
Equity attributable to owners of the parent			
Share capital	154	154	154
Retained earnings	204,165	209,304	207,839
Other reserves	(4,891)	(16,929)	(13,970)
Total equity	199,428	192,529	194,023
LIABILITIES			
Deposits from banks	230,106	230,638	230,090
Derivative financial instruments	286	634	649
Deposits from customers	2,642,761	2,206,515	2,365,207
Current tax liability	-	603	-
Other liabilities	29,820	7,477	7,606
Lease liabilities	16,912	19,152	18,305
Debt securities in issue	37,089	37,800	37,656
Total liabilities	2,956,974	2,502,819	2,659,513
Total equity and liabilities	3,156,402	2,695,348	2,853,536

Consolidated Statement of Changes in Equity

	Attributable to equity holders of the Group						Total £000
	Share capital	Revaluation reserve	Capital redemption reserve	Fair value reserve	Treasury shares	Retained earnings	
	£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.

	Attributable to equity holders of the Group						Total £000
	Share capital	Revaluation reserve	Capital redemption reserve	Fair value reserve	Treasury shares	Retained earnings	
	£000	£000	£000	£000	£000	£000	
Balance at 1 January 2020	154	-	19	205	(1,214)	209,171	208,335
Total comprehensive income for the period							
Profit for the six months ended 30 June 2020	-	-	-	-	-	131	131
Other comprehensive income, net of income tax							
Changes in the fair value of financial assets at FVOCI*	-	-	-	(15,872)	-	-	(15,872)
Tax on other comprehensive income	-	-	-	20	-	-	20
Total other comprehensive income	-	-	-	(15,852)	-	-	(15,852)
Total comprehensive income for the period	-	-	-	(15,852)	-	131	(15,721)
Transactions with owners, recorded directly in equity							
Contributions by and distributions to owners							
Purchase of own shares	-	-	-	-	(85)	-	(85)
Total contributions by and distributions to owners	-	-	-	-	(85)	-	(85)
Balance at 30 June 2020	154	-	19	(15,647)	(1,299)	209,302	192,529

* The change in fair value of financial investments of £15.9m is due to the movement in the value of the investment in Secure Trust Bank, as the share price reduced from £16.00 at 31 December 2019 to £7.24 at 30 June 2020.

Consolidated Statement of Cash Flows

	Six months ended 30 June 2021 £000	Six months ended 30 June 2020 £000
Cash flows from operating activities		
Interest received	37,476	63,829
Interest paid	(7,162)	(10,892)
Fees and commissions received	6,397	6,491
Revenue received	22,726	-
Cost of goods sold paid	(22,533)	-
Net trading and other income	2,889	420
Cash payments to employees and suppliers	(34,142)	(65,645)
Cash flows from operating profits/(losses) before changes in operating assets and liabilities	5,651	(5,797)
Changes in operating assets and liabilities:		
- net decrease in derivative financial instruments	630	370
- net increase in loans and advances to customers	(134,441)	(22,646)
- net decrease/(increase) in other assets	179	(2,150)
- net increase in deposits from banks	16	217
- net increase in amounts due to customers	277,554	121,612
- net increase / (decrease) in other liabilities	6,815	(7,302)
Net cash inflow from operating activities	156,404	84,304
Cash flows from investing activities		
Purchase of financial investments	(94)	(225)
Disposal of financial investments	11,650	-
Purchase of computer software	(2,227)	(3,973)
Refurbishment cost investment property	-	(2,365)
Purchase of property, plant and equipment	(13,575)	1,064
Proceeds from sale of property, plant and equipment	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	(343,137)	(433,775)
Proceeds from redemption of debt securities	294,790	527,316
Net cash (outflow)/inflow from investing activities	(51,489)	88,042
Cash flows from financing activities		
Decrease in borrowings	(127,918)	-
Dividends paid	(3,155)	-
Net cash used in financing activities	(131,073)	-
Net (decrease)/increase in cash and cash equivalents	(26,158)	172,346
Cash and cash equivalents at 1 January	747,066	372,166
Cash and cash equivalents at 30 June	720,908	544,512

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 2020 statutory accounts as amended by standards and interpretations effective during 2021 as set out below and in accordance with IAS 34 "Interim Financial Reporting". 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 19 July 2021 and are unaudited. The interim financial statements will be available on the Group website (www.arbuthnotgroup.com) from 20 July 2021.

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 its 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.

Coronavirus

The COVID-19 pandemic has had, and continues to have, a material impact on all businesses around the world and the markets in which they operate. There are a number of factors associated with the pandemic and its impact on global economies that could have a material adverse effect on (among other things) the profitability, capital and liquidity of financial institutions.

To ensure an appropriate response to the pandemic, management scrutinised key risks emerging from the crisis and their impact on the Group's risk profile. The Board's discussions focused on operational resilience, liquidity and funding considerations, customer vulnerability, and the impact of material increases in forbearance requests on the Group's credit portfolios and on its operational capacity.

The pandemic has caused disruption to the Group's clients, suppliers and employees globally. The markets in which the Group operates have implemented severe restrictions on the movement of their respective populations, with a resultant significant impact on economic activity. These restrictions are being determined by the governments of individual jurisdictions (including through the implementation of emergency powers) and impacts (including the timing of implementation and any subsequent lifting of restrictions) may vary from jurisdiction to jurisdiction.

Schemes have been initiated by the Bank of England, national governments and regulators to provide financial support to parts of the economy most impacted by the COVID-19 pandemic. These schemes have been designed and implemented at pace, which has allowed the Group to continue meeting clients' requirements with employees monitoring operational issues which may arise in their implementation.

Furthermore, the Group relies on models to support a broad range of business and risk management activities, including informing business decisions and strategies, measuring and limiting risk, valuing exposures (including the calculation of impairment), conducting stress testing and assessing capital adequacy. Management regularly meet to discuss the impact of COVID-19 and review data to mitigate any potential negative effects.

The significant business risks that may arise from the economic shock in addition to the reduction in interest rates are:

- a) Increased credit risk as borrowers are unable to continue to meet their interest obligations as they fall due. It is also currently unclear precisely how the withdrawal of the Government's announced package of measures will affect this clear risk.
- b) The uncertainty in the economy could result in a significant fall in the collateral values of our security held against the loans. At the beginning of the pandemic the Royal Institute of Charter Surveyors ("RICS") issued a statement suggesting that any valuations they may produce in the current environment would be subject to a warning that the values vary significantly.

However, property prices have held up and transaction volumes and other relevant evidence is starting to return to levels adequate to base valuation opinions on. Also, the average loan to value of our property backed lending book is 51.5%, so to have a material impact, this fall in collateral values would have to be severe and prolonged.

- c) A prolonged reduction in business activity will affect our ability to generate new business opportunities, in which case repayments in our current lending portfolios will be greater than new originations, which will lead to an overall fall in the Group's customer lending balances and the associated revenue that this generates. At the start of the pandemic the Group significantly reduced its credit appetite due to uncertainty in the global economy, which resulted in the loan book remaining flat from 31 December 2019 to 31 December 2020. However, since re-instating credit appetite to pre-pandemic levels towards the end of 2020, the Group has generated a significant pipeline of business.
- d) The economic shock could also lead to a fall in valuations in the Groups investment properties and those properties held in inventory. As mentioned under point (b) above, transaction volumes are starting to return and property prices have held up since the start of the pandemic more than a year ago.
- e) As the revenues earned by the Group's Investment Management business are directly linked to the balances managed on behalf of our clients, any reduction in these values due to market movements will have a corresponding impact on these revenues. AUM closed the first half of 2021 7% up from 31 December 2020.

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, which was applicable from 1 January 2021. The Group has no overseas operations following the closure of its Dubai office on 31 May 2021. Consequently, the vast majority of the Group's income and expenditure is based in the UK. The Group will continue to monitor the implications of Brexit on the wider economy as the future relationship with the EU develops.

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 Board of Directors usually 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 (borrower) will be unable to pay amounts in full when due. This risk exists in Arbuthnot Latham, which currently has a loan book of £1,726m (30 June 2020: £1,620m). 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 and properties classified as inventory are carried at £86.1m. 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.

The Group has a 4.40% interest in Secure Trust Bank. 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 Secure Trust Bank. Any gains or losses that arise are recorded in Other Comprehensive Income.

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 Group. 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.

There was significant focus on the potential operational risks arising from the change in working practices due to the pandemic, particularly the continued remote working in order to protect employees and support clients through the crisis. Management attention also focused heavily on operational resilience to ensure that planning, controls and operational activities remained robust and appropriate. The Bank ensured that all employees had access to equipment to complete their work with all employees working remotely for the majority of the period.

The Group's control environment was continually monitored to ensure that the challenges posed by adapting to the impact of COVID-19 were safely addressed. There was also continued oversight of the Group's preparations for the end of the transition period, following the UK's exit from the EU, to ensure that processes and systems are appropriate to ensure continuity of service for customers.

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 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.

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 2020. 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 no change, upside case, downside case, moderate decline and severe decline, 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.

Management considered a range of variables in determining the level of future ECL. 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 client exposures, this would lead to a negative £0.7m (30 June 2020: negative £0.5m) impact through the Profit or Loss. A six-month reduction in time to collect would lead to a £0.4m favourable (30 June 2020: £0.4m favourable) impact on Profit or Loss.

If the collateral valuations increased by 10% across client exposures, this would lead to a positive £0.6m (30 June 2020: positive £1.5m) impact through Profit or Loss. If the collateral valuations decreased by 10% across all Stage 3 client exposures, this would lead to a £1.9m adverse (30 June 2020: £2.2m adverse) impact on Profit or Loss.

Five economic scenarios were modelled. A probability was assigned to each scenario to arrive at an overall weighted impact on ECL. Management judgment is required in the application of the probability weighting for each scenario.

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 only collateral values/property prices have a material impact on ECL.

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

- Severe decline
- Moderate decline
- Decline
- No change
- Growth

Other than collateral/property prices for Arbuthnot Latham and collateral/asset values for its subsidiary Renaissance Asset Finance, no other assumptions were assessed to have a material impact on ECL. The tables below therefore reflect the expected changes in collateral/property prices and collateral/asset values in each of the macroeconomic scenarios and the probability weighting applied for each scenario.

Another of the key judgements concerns the probability of the economic scenarios in the measurement of the ECL. The probability weighting and forward-looking economic scenarios are as follows for the Arbuthnot Latham and Renaissance Asset Finance:

Economic Scenarios	Arbuthnot Latham					
	Probability weighting			Change in property prices		
	Jun 2021	Jun 2020	Dec 2020	Jun 2021	Jun 2020	Dec 2020
Severe decline	2.0%	2.0%	2.0%	(40.0%)	(40.0%)	(40.0%)
Moderate decline	15.0%	20.0%	15.0%	(20.0%)	(20.0%)	(20.0%)
Decline	70.0%	70.0%	70.0%	(2.5%)	(5.0%)	(2.5%)
No Change	9.0%	4.0%	9.0%	-	-	-
Growth	4.0%	4.0%	4.0%	0.5%	0.5%	0.5%
Weighted average change in property price				(5.5%)	(8.3%)	(5.5%)

Economic Scenarios	Renaissance Asset Finance					
	Probability weighting			Change in asset values		
	Jun 2021	Jun 2020	Dec 2020	Jun 2021	Jun 2020	Dec 2020
Severe decline	6.0%	12.0%	6.0%	(15%) to (60%)	(15%) to (60%)	(15%) to (60%)
Moderate decline	20.0%	40.0%	20.0%	(7.5%) to (30%)	(7.5%) to (30%)	(7.5%) to (30%)
Decline	40.0%	40.0%	40.0%	(2.5%) to (15%)	(2.5%) to (15%)	(2.5%) to (15%)
No Change	31.0%	5.0%	31.0%	-	-	-
Growth	3.0%	3.0%	3.0%	2.0%	2.0%	2.0%
Weighted average change in asset values				(9.6%)	(14.9%)	(9.6%)

The above tables reflect the 5-year average expected change in collateral values in each economic scenario for Arbuthnot Latham and its subsidiary Renaissance Asset Finance, which were applied over the full term the Group is exposed to credit risk (also an average of 5 years). The expected change in property prices under each scenario, were weighted according to the probability of each scenario, to arrive at a probability weighted change in property prices for Arbuthnot Latham and asset values for Renaissance Asset Finance. These adjusted property and asset values are then used to assess the future expected cash flows, which are considered along with the loan exposures at default to calculate the expected credit loss. No other long-term averages are used in the calculation of ECL, as the above changes are in effect modelled over the full term of the Group's exposure to credit risk.

The change in property prices for Arbuthnot Latham and asset values for Renaissance Asset Finance were maintained at the same level as at 31 December 2020. This is to reflect the uncertainty to the property market and economy as Government support is unwound along with the removal of COVID-19 restrictions whilst the number of cases of COVID-19 are increasing.

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			Renaissance Asset Finance		
	Jun 2021	Jun 2020	Dec 2020	Jun 2021	Jun 2020	Dec 2020
	£m	£m	£m	£m	£m	£m
Severe decline	(44.4)	(31.8)	(46.4)	(3.6)	(2.9)	(4.6)
Moderate decline	(4.8)	(3.1)	(5.1)	(0.5)	(0.1)	(0.9)
Decline	0.4	0.7	0.3	0.1	0.2	0.1
No change	0.6	1.3	0.4	0.2	0.3	0.4
Growth	0.6	1.4	0.5	0.2	0.3	0.4

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 year, and in particular the impact of the COVID-19 crisis on performance against both credit risk appetite and a range of key credit risk metrics.

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 economic environment remains uncertain and future impairment charges may be subject to further volatility (including from changes to macroeconomic variable forecasts) depending on the longevity of the COVID-19 pandemic and related containment measures, as well as the longer term effectiveness of central bank, government and other support measures.

COVID-19 has created an unprecedented challenge for ECL modelling, given the severity of economic shock and associated uncertainty for the future economic path coupled with the scale of government and central bank intervention and COVID-19 relief mechanisms that have altered the relationships between economic drivers and default.

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 as the potential trajectory of the subsequent recovery. The Group also considered differential impacts on asset classes, including pronouncements from regulatory bodies regarding IFRS 9 application in the context of COVID-19, notably on significant increase in credit risk (SICR) identification.

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 2021							Total
	Banking	Mortgage Portfolios	RAF	ACABL	ASFL	AAGH	All Other Divisions	
Credit risk exposures (all stage 1, unless otherwise stated)	£000	£000	£000	£000	£000	£000	£000	£000
<u>On-balance sheet:</u>								
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
<u>Off-balance sheet:</u>								
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

30 June 2020

Group	Banking	Mortgage Portfolios	RAF	ACABL	ASFL	AAGH	All Other Divisions	Total
Credit risk exposures (all stage 1, unless otherwise stated)	£000	£000	£000	£000	£000	£000	£000	£000
<u>On-balance sheet:</u>								
Cash and balances at central banks	-	-	-	-	-	-	434,587	434,587
Loans and advances to banks	-	-	-	-	-	-	109,751	109,751
Debt securities at amortised cost	-	-	-	-	-	-	359,042	359,042
Derivative financial instruments	-	-	-	-	-	-	1,749	1,749
Loans and advances to customers	1,153,552	291,958	100,693	65,528	8,531	-	-	1,620,262
Stage 1 - Gross amount outstanding	1,054,875	279,963	98,475	65,559	8,554	-	-	1,507,426
Stage 1 - Allowance for impairment	(524)	-	(285)	(31)	(23)	-	-	(863)
Stage 2 - Gross amount outstanding	63,094	6,314	792	-	-	-	-	70,200
Stage 2 - Allowance for impairment	(24)	-	(1)	-	-	-	-	(25)
Stage 3 - Gross amount outstanding	41,023	5,681	2,158	-	-	-	-	48,862
Stage 3 - Allowance for impairment	(4,892)	-	(446)	-	-	-	-	(5,338)
Other assets	-	-	-	-	-	-	4,837	4,837
Financial investments	-	-	-	-	-	-	15,310	15,310
<u>Off-balance sheet:</u>								
Guarantees	6,401	-	-	-	-	-	-	6,401
Loan commitments	129,958	-	-	97,238	1,136	-	-	228,332
At 30 June 2020	1,289,911	291,958	100,693	162,766	9,667	-	925,276	2,780,271

31 December 2020

Group	Banking	Mortgage Portfolios	RAF	ACABL	ASFL	AAGH	All Other Divisions	Total
Credit risk exposures (all stage 1, unless otherwise stated)	£000	£000	£000	£000	£000	£000	£000	£000
<u>On-balance sheet:</u>								
Cash and balances at central banks	-	-	-	-	-	-	636,631	636,631
Loans and advances to banks	-	-	-	-	-	-	110,267	110,267
Debt securities at amortised cost	-	-	-	-	-	-	344,692	344,692
Derivative financial instruments	-	-	-	-	-	-	1,843	1,843
Loans and advances to customers	1,122,300	268,827	91,926	87,331	5,964	-	11,501	1,587,849
Stage 1 - Gross amount outstanding	1,019,896	223,803	74,790	87,372	5,971	-	11,501	1,423,333
Stage 1 - Allowance for impairment	(425)	(3)	(249)	(41)	(7)	-	-	(725)
Stage 2 - Gross amount outstanding	72,713	36,887	16,747	-	-	-	-	126,347
Stage 2 - Allowance for impairment	(87)	(93)	(353)	-	-	-	-	(533)
Stage 3 - Gross amount outstanding	33,208	8,252	1,336	-	-	-	-	42,796
Stage 3 - Allowance for impairment	(3,005)	(19)	(345)	-	-	-	-	(3,369)
Other assets	-	-	-	-	-	-	5,458	5,458
Financial investments	-	-	-	-	-	-	18,495	18,495
<u>Off-balance sheet:</u>								
Guarantees	6,248	-	-	-	-	-	-	6,248
Loan commitments	152,972	-	-	155,300	155	-	-	308,427
At 31 December 2020	1,281,520	268,827	91,926	242,631	6,119	-	1,128,887	3,019,910

Market risk

(a) Properties

The COVID-19 situation and changing market conditions are monitored closely. As at 30 June 2021, the Group has reduced the carrying value of Inventory by £1.4m due to a reduction in value of a property in Spain, while further costs were capitalised on the development of land held by Pinnacle Universal; a special purpose vehicle 100% owned by the Group. Refurbishment work on the King Street property completed in June 2021, with costs also capitalised as part of the carrying value. The Group has not changed the assumptions in valuing the properties held as Investment Property or Inventory.

(b) Financial investments

Financial investments mainly consist out of shares held in Secure Trust Bank (“STB”). The carrying value is adjusted to market value at each balance sheet date, according to the share price of STB and any gains or losses that arise are recorded in Other Comprehensive Income. The Group sold 750,000 shares on 31 March 2021 and a further 250,000 shares on 19 April 2021, reducing the shareholding from 9.75% to 4.40%. The share price increased from £8.75 at the end of December 2020 to £10.58 at 30 June 2021, with the value of the investment being £8.7m (31 December 2020: £15.9m).

Liquidity risk

The Group has managed to increase customer deposits by £278m since year-end. Liquidity buffers have been maintained in excess of minimum requirements throughout the period, with the actual Liquidity Coverage Ratio (“LCR”) at 246% (31 December 2020: 237%) significantly exceeding the regulatory minimum of 100%.

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 8.69% (31 December 2020: 8.71%), while the CET1 capital ratio is 12.5% (31 December 2020: 15.4%) and the total capital ratio is 15.2% (31 December 2020: 18.7%).

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:

	Level 1	Level 2	Level 3	Total
At 30 June 2021	£000	£000	£000	£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 30 June 2020	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Derivative financial instruments	-	1,749	-	1,749
Financial investments	13,178	-	2,132	15,310
Investment properties	-	-	6,763	6,763
	13,178	1,749	8,895	23,822
LIABILITIES				
Derivative financial instruments	-	634	-	634
Other liabilities (contingent consideration)	-	-	854	854
	-	634	854	1,488

At 31 December 2020	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Derivative financial instruments	-	1,843	-	1,843
Financial investments	15,925	-	2,570	18,495
Investment properties	-	-	6,550	6,550
	15,925	1,843	9,120	26,888
LIABILITIES				
Derivative financial instruments	-	649	-	649
	-	649	-	649

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:

	At 30 June 2021 £000	At 30 June 2020 £000	At 31 December 2020 £000
Movement in level 3			
At 1 January	9,120	8,566	8,566
Acquisitions	89	225	419
Movements recognised in Other Comprehensive Income	89	106	366
Movements recognised in the Income Statement	(12)	(2)	(231)
At 30 June / 31 December	9,286	8,895	9,120

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

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	-	1,443,667	282,804	1,726,471
Other assets	-	-	16,058	16,058
	-	2,556,562	298,862	2,855,424
LIABILITIES				
Deposits from banks	-	230,106	-	230,106
Deposits from customers	-	2,651,721	-	2,651,721
Other liabilities	-	-	33,495	33,495
Debt securities in issue	-	-	61,426	61,426
	-	2,881,827	94,921	2,976,748

At 30 June 2020	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
ASSETS				
Cash and balances at central banks	-	434,761	-	434,761
Loans and advances to banks	-	109,743	-	109,743
Debt securities at amortised cost	-	359,042	24,267	383,309
Loans and advances to customers	-	1,317,606	302,656	1,620,262
Other assets	-	-	5,225	5,225
	-	2,221,152	332,148	2,553,300
LIABILITIES				
Deposits from banks	-	230,638	-	230,638
Deposits from customers	-	2,206,515	-	2,206,515
Other liabilities	-	-	8,993	8,993
Debt securities in issue	-	-	62,067	62,067
	-	2,437,153	71,060	2,508,213

At 31 December 2020	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
ASSETS				
Cash and balances at central banks	-	636,799	-	636,799
Loans and advances to banks	-	110,267	-	110,267
Debt securities at amortised cost	-	344,692	-	344,692
Loans and advances to customers	-	1,300,824	287,025	1,587,849
Other assets	-	-	5,457	5,457
	-	2,392,582	292,482	2,685,064
LIABILITIES				
Deposits from banks	-	230,090	-	230,090
Deposits from customers	-	2,365,207	-	2,365,207
Other liabilities	-	-	1,949	1,949
Debt securities in issue	-	-	37,656	37,656
	-	2,595,297	39,605	2,634,902

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

During the second half of 2020 the Group changed the way it manages and reports the Banking sector, combining the Private Banking and Commercial Banking sector into a single Banking sector. In 2021 the Group also started to report Wealth Management separately, which was previously included as part of Banking. This is the level at which management decisions are made and how the Group will manage the overall business sectors going forward with the anticipated growth in subsidiary businesses. The comparative numbers for the divisions have been restated to reflect the new allocation method.

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 2021	Banking £000	Wealth Management £000	Mortgage Portfolios £000	RAF £000	ACABL £000	ASFL £000	AAGH £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
Turnover	-	-	-	-	-	-	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	(1,324)	(6,793)
Cost of sales	-	-	-	-	-	-	(20,346)	-	-	(20,346)
Add back inter-segment revenue	-	-	-	-	-	-	-	-	9	9
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)

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

Six months ended 30 June 2020	Banking £000	Wealth Management £000	Mortgage Portfolios £000	RAF £000	ACABL £000	ASFL £000	All Other Divisions £000	Group Centre £000	Total £000
Interest revenue	22,913	-	5,434	5,058	2,014	393	3,233	27	39,072
Inter-segment revenue	-	-	-	-	-	-	-	(27)	(27)
Interest revenue from external customers	22,913	-	5,434	5,058	2,014	393	3,233	-	39,045
Fee and commission income	1,165	4,444	-	87	1,043	1	253	-	6,993
Revenue from external customers	24,078	4,444	5,434	5,145	3,057	394	3,486	-	46,038
Interest expense	(2,396)	-	(2,213)	(1,410)	(859)	(128)	(1,009)	(989)	(9,004)
Add back inter-segment revenue	-	-	-	-	-	-	-	27	27
Subordinated loan note interest	-	-	-	-	-	-	-	(360)	(360)
Fee and commission expense	(124)	(12)	-	(1)	(9)	-	(1)	-	(147)
Segment operating income	21,558	4,432	3,221	3,734	2,189	266	2,476	(1,322)	36,554
Impairment losses	(1,087)	-	-	(603)	9	(20)	-	-	(1,701)
Other income	-	-	-	-	-	-	840	(420)	420
Operating expenses	(19,188)	(5,516)	(838)	(2,171)	(1,524)	(760)	(2,039)	(3,036)	(35,072)
Segment profit / (loss) before tax	1,283	(1,084)	2,383	960	674	(514)	1,277	(4,778)	201
Income tax (expense) / income	-	-	-	(206)	-	-	-	136	(70)
Segment profit / (loss) after tax	1,283	(1,084)	2,383	754	674	(514)	1,277	(4,642)	131
Loans and advances to customers	1,115,819	-	300,846	101,425	66,504	8,654	38,514	(11,500)	1,620,262
Other assets	-	-	-	-	-	-	1,065,270	9,816	1,075,086
Segment total assets	1,115,819	-	300,846	101,425	66,504	8,654	1,103,784	(1,684)	2,695,348
Customer deposits	1,956,153	-	-	-	-	-	276,826	(26,464)	2,206,515
Other liabilities	-	-	-	-	-	-	284,844	11,460	296,304
Segment total liabilities	1,956,153	-	-	-	-	-	561,670	(15,004)	2,502,819
Other segment items:									
Capital expenditure	-	-	-	-	(363)	-	(4,354)	-	(4,717)
Depreciation and amortisation	-	-	-	(5)	(11)	(6)	(880)	(13)	(915)

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

Prior year numbers have been represented according to the 2021 operating segments reported to management. The UK private bank had a branch in Dubai, which generated £2.0m (30 June 2020: £2.0m) of income and had direct operating costs of £1.5m (30 June 2020: £1.2m). All Dubai branch income was booked in the UK. Other than the Dubai branch, which was closed on 31 May 2021, all operations of the Group are conducted wholly within the United Kingdom and geographical information is therefore not presented.

6. Other income

Other income mainly includes the profit on sale of the Tay Mortgage portfolio of £2.2m. It also includes rental income received from the investment property of £0.2m (2020: £0.4m) and £0.4m dividend income received from STB (2020: £nil).

7. 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 (2020: 15,028,411) 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 (2020: nil).

	Six months ended 30 June 2021 £000	Six months ended 30 June 2020 £000
Profit attributable		
Total profit after tax attributable to equity holders of the Company	4,092	131

	Six months ended 30 June 2021 p	Six months ended 30 June 2020 p
Basic Earnings per share		
Total Basic Earnings per share	27.2	0.9

8. 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 AAGH from its former owners made up of institutional investors and the key management team.

AAGH 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 AAGH at completion of £127.9m to re-finance its existing finance liabilities. The consideration and the refinancing of AAGH'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.

	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)

9. Events after the balance sheet date

There were no material post balance sheet events to report.