PRESS RELEASE
Thursday 28 March 2019
For immediate release

SECURE TRUST BANK PLC

Audited Final Results for the year to 31 December 2018

Strategic Repositioning Yielding Significant Benefits

Secure Trust Bank PLC ("STB", the "Bank" or the "Group") is pleased to announce a 38.8% increase in Group profit before tax to £34.7m for the year to 31 December 2018.

Repositioning of the business model towards lower risk lending in attractive market segments, and continued growth in both Business Finance and Consumer Finance, has driven earnings and reduced impairment losses.

The Group has entered 2019 with positive business momentum, healthy capital positions and strong liquidity and remains well placed to pursue its strategic objectives. The successful repositioning of the balance sheet will also enable the Group to navigate the current heightened levels of political and economic uncertainty.

FINANCIAL HIGHLIGHTS

- Adjusted profit before tax up 35.9% to £36.7m (2017*: £27.0m) and is in line with market expectations
- Reported profit before tax is up 38.8% to £34.7m (2017*: £25.0m)
- Higher quality book has significantly reduced cost of risk
- Healthy common equity tier 1 ratio of 13.8% (2017: 16.5%) supporting the strong growth in the loan portfolios
- Total capital ratio of 16.3% (2017: 16.8%)
- £50m of Tier 2 capital was raised at an annual coupon of 6.75%
- Operating income £151.6m (2017*: £129.5m) up 17.1%
- Basic earnings per share 153.2p (2017*: 107.7p) up 42.2%
- Adjusted earnings per share 161.8p (2017*: 116.4p) up 39.0%
- Adjusted return on average equity of 13.1% (2017*: 8.9%)
- Proposed final dividend of 64p per share (2017: 61p per share), to be paid in May 2019, representing a total dividend of 83p per share (2017: 79p per share)
- Total assets £2.44bn (2017*: £1.89bn) up 29.1%

Note: Adjusted profit and adjusted earnings per share relates to the Group's normal recurring business activities

* 2017 is reported on a continuing operations basis, which excludes the Personal Lending Division that was sold during that year, and on an IAS 39 basis

OPERATIONAL HIGHLIGHTS

- Total customer numbers increased by 29.3% to 1,279,783
- Customer deposits increased to £1,847.7m (2017: £1,483.2m) up 24.6%
- New digital deposits platform successfully operational with new products to be launched in 2019
- Overall loan book increased to £2,028.9m (2017*: £1,598.3m) up 26.9%
- Total annual new business lending volumes grew 17.2% to £1,261.9m (2017*: £1,077.1m)
- Real Estate Finance lending balances up 33%** year-on-year to £769.8m
- Invoice Finance expanded its regional footprint, opening offices in Birmingham, Leeds and London, resulting in lending balances up more than 50%** year-on-year to £194.7m
- Retail Finance lending balances up 35%** year-on-year to £597.0m

- Significant progress made in Motor Finance. Legacy sub-prime loans have been successfully replaced with higher quality lending and plans underway to expand into Prime Credit market and dealer stocking finance
- Continuing high levels of customer satisfaction as measured by FEEFO

* 2017 is reported on a continuing operations basis, which excludes the Personal Lending Division that was sold during that year
** 31 December 2017 loan book balances adjusted for the transition impact of adopting IFRS 9 as at 1 January 2018

Lord Forsyth, Chairman, said:

"2018 has been a successful year for the Group in unsettling economic circumstances. Reducing our exposure to higher risk, higher margin consumer lending activities whilst focusing on lower risk lending has delivered a good set of financial results. Despite the uncertain economic environment that the Group continues to monitor carefully, the Group enters 2019 well positioned to deliver further substantial progress in the periods ahead."

Paul Lynam, Chief Executive, said:

"2018 has seen strong Group performance when viewed across a broad range of customer, staff and financial metrics. Secure Trust Bank increased its profit before tax by 38.8%, its customer lending by 26.9% and its customer numbers by 29.3%. With the benefits of the repositioning of the business model now apparent, the Group entered 2019 with positive business momentum, healthy capital positions and very strong liquidity. Our lending portfolio is appropriately positioned for current economic conditions and the short duration nature of the asset portfolio means we can react quickly to both market opportunities and threats."

This announcement together with the associated investors' presentation are available on:
www.securetrustbank.com/results-reports/results-reports-presentations

Enquiries:

Secure Trust Bank PLC
Paul Lynam, Chief Executive Officer
Neeraj Kapur, Chief Financial Officer
Tel: 0121 693 9100

Stifel Nicolaus Europe Limited (Joint Broker)
Robin Mann
Gareth Hunt
Stewart Wallace
Tel: 020 7710 7600

Canaccord Genuity Limited (Joint Broker)
Sunil Duggal
David Tyrrell
Tel: 020 7523 8000

Tulchan Communications
Tom Murray
David Ison
Tel: 020 7353 4200

Forward looking statements

This document contains forward looking statements with respect to the business, strategy and plans of Secure Trust Bank PLC and its current goals and expectations relating to its future financial condition and performance. Statements that are not historical facts, including statements about Secure Trust Bank PLC's or management's beliefs

and expectations, are forward looking statements. By their nature, forward looking statements involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. Secure Trust Bank PLC's actual future results may differ materially from the results expressed or implied in these forward looking statements as a result of a variety of factors. These include UK domestic and global economic and business conditions, risks concerning borrower credit quality, market related risks including interest rate risk, inherent risks regarding market conditions and similar contingencies outside Secure Trust Bank PLC's control, any adverse experience in inherent operational risks, any unexpected developments in regulation or regulatory and other factors. The forward looking statements contained in this document are made as of the date hereof, and Secure Trust Bank PLC undertakes no obligation to update any of its forward looking statements.

Strategic report

Chairman's statement

2018 has been a successful year for the Group in unsettling economic circumstances. Reducing our exposure to higher risk, higher margin consumer lending activities whilst focusing on lower risk lending has delivered a good set of financial results.

Notable highlights include exceeding more than one million customers; lending balances over £2 billion; growth in statutory profit of 38.8%; growth in basic earnings per share of 42.2%; and the strengthening of our capital base. Our Real Estate Finance, Commercial Finance and Retail Finance businesses have shown strong growth. The Group is now benefiting from the digital savings platform launched in 2017 and won a number of awards including Best Savings Provider, Best Fixed Rate Bond and Best Notice Account Provider from Savings Champion.

An uncertain economic environment creates risks that require careful navigation and this has influenced our risk appetite throughout 2018 and into 2019. We continue to monitor economic indicators and assess the potential impact on our business.

During the year there were a number of changes to the Board. In August Sir Henry Angest and Andrew Salmon stepped down as directors, having contributed significantly to the business over many years including steering the business from wholly owned subsidiary to the Main Market of the London Stock Exchange. On behalf of all my colleagues I would like to record our appreciation and thanks to them. In November I was delighted to welcome Lucy Neville-Rolfe and Paul Myers to the Board following a rigorous search in which the Board was assisted by headhunters Korn Ferry. They bring significant relevant experience to our Board. The introduction of the latest version of the Corporate Governance Code with effect from 1 January 2019 also caused us to review the composition of our Board and Committees and in January I stepped down as a member of the Audit Committee and Paul Lynam stepped down from the Risk Committee. We are now fully compliant with the requirements of the new Corporate Governance Code and intend to continue to be so. The Board comprises two Executive Directors, five independent Non-Executive Directors and myself as Chairman. I am immensely grateful to Ann Berresford, Paul Marrow and Victoria Stewart for the work they have done during the year in chairing the Audit, Risk and Remuneration Committees in what has been a very busy year.

We fully recognise the importance of engaging with all our stakeholders. A new Group-wide Employee Council was established during 2018. We have established direct lines of communication from the Employee Council to the Executive Committee (via the Chief Executive Officer) and to the Board (via the Senior Independent Director and the Chief Executive Officer) both of whom sit on the Employee Council. The results of our employee survey conducted in 2018 were encouraging.

Once again I want to highlight and commend the fantastic charitable and community work being carried out by our employees. I had the opportunity during the year to visit the Birmingham St Mary's Hospice and see first-hand the impact of what our team can do. This year we were able to enhance our matched giving scheme to support our employees' fundraising activities. This forms part of our commitment to be a responsible business and make a positive contribution to the community in which we operate.

The Board is proposing a final dividend for 2018 of 64 pence per share. This, when added to the interim dividend for 2018 of 19 pence, would mean a full year dividend for 2018 of 83 pence per share. The full year dividend paid in 2017 was 79 pence per share, being made up of an interim dividend of 18 pence plus a final dividend of 61 pence. If approved at the AGM, the 2018 final dividend will be paid on 24 May 2019 to shareholders on the register as at 26 April 2019.

Finally, on behalf of the Board I would like to express my thanks to our CEO, Paul Lynam, and all of our colleagues across the Group for another year of progress and for their continued dedication and commitment. Given the resources at our disposal, the talents of our people, the flexibility of our business model and our clear strategy we can face the future, however uncertain, with optimism and confidence.

Lord Forsyth
Chairman

27 March 2019

Chief Executive' statement
I am delighted to report a strong year's performance for 2018 when viewed across a broad range of customer, staff and financial metrics. I would like to thank the entire STB team for their commitment and professionalism last year and for the way they have continued delivering good outcomes for our all-important customers. As expected, the repositioning of the business model towards lower risk lending, and continued growth in both Business Finance and Consumer Finance, has seen income grow and impairment losses reduce. These factors have driven the strong growth in reported and adjusted earnings.

The financial results for 2018 show the Group statutory profit before tax increasing by 38.8% to £34.7 million compared to the £25.0 million of profit before tax generated from continuing operations during 2017. Adjusted profit before tax on the same basis has increased by 35.9% to £36.7 million. Adjusted earnings per share increased by 39.0% over the same period with basic earnings per share increasing by 42.2%. As shown on page 21, the Group's adjusted return metrics have also improved.

With the benefits of the repositioning of the business model now apparent, the Group entered 2019 with healthy capital and liquidity positions. We have positioned the balance sheet to enable us to navigate the heightened levels of political and economic uncertainty arising from Brexit. The fundamentals of the UK economy are sound and we have seen no discernible change in the behaviour of our consumer customers. The financial sector is resilient. Corporate balance sheets are strong, and the labour market is tight as evidenced by record levels of employment.

Assuming an orderly exit from the EU we expect the UK economic outlook to improve which the Group will seek to leverage as it continues to execute its clearly defined growth strategy. We are well placed to support an increase in demand for working capital funding from businesses and residential development finance from house builders. The latter is aided by a regulatory capital efficient Enable Guarantee we have agreed with the British Business Bank. We are developing new products in our Retail Finance business and are progressing significant investment in our Motor Finance business which will see this portfolio grow considerably over the next 5 years via the provision of dealer stocking finance and a prime motor proposition for consumers. In overall terms we are well positioned in a number of attractive lending classes and have started 2019 strongly. We therefore expect good progress to be made in meeting our goals over the coming period.

Further growth in customer base and satisfaction levels remain very positive
Across our consumer and SME business products we are serving well over 1 million customers. This is a key milestone achievement in 2018. Total customer numbers are a record 1,279,783 customers which is an increase of 29.3% on the total customer base of 989,528 as at 31 December 2017.

We continue to focus on consistently delivering good outcomes for customers and ensuring that the design of our products is appropriate for their needs. From a conduct and behaviour perspective we do not cross subsidise losses or low profits on some products with super profits on others. Nor do we discriminate between customers by, for example, paying very low deposit interest rates to existing loyal customers whilst offering much higher rates to new ones. We believe that our approach is the appropriate way to interact with our customers for the long term benefit of all parties.

Customer satisfaction is measured in a number of ways. It is reassuring that 2018 has once again seen us consistently achieve customer satisfaction ratings in excess of 90% across all of our products as measured by FEEFO. We also use Net Promoter Scores to assess our customer service and these scores exhibit similar positive trends to those derived from FEEFO.

I am delighted to confirm that for the sixth year running we have retained the Customer Service Excellence standard. This standard was introduced by the Cabinet Office in 2010 to replace the Kite Mark. This indicates our customer service has been judged to meet Government standards of excellence which are benchmarked against high-performing organisations.

Whilst being pleased with external accolades and ongoing high customer satisfaction scores we are in no way complacent. We are focused on improving our existing service and products and diversifying our customer proposition via targeted investment in people, systems, processes and products.

Healthy Capital position

Our ongoing priority is to safeguard the reputation and sustainability of the Group through prudent balance sheet management, investment for long-term sustainable growth and robust risk and operational controls.

Our year end CET1 capital levels are healthy with a CET1 ratio of 13.8% compared to the 2017 year end position of 16.5%. The Total Capital Ratio was 16.3% (2017: 16.8%) and STB's leverage ratio was 10.0% (2017: 12.3%) as at 31 December 2018. The year on year movement in CET1 is a function of the investment of capital to support the strong growth in the loan portfolios. The Total Capital Requirement ratio includes the impact of the issuance of Tier 2 capital, discussed below. The ratios are comfortably ahead of minimum requirements and demonstrate capacity to continue growing customer lending balances in 2019.

As previously disclosed, the Board reviewed the Group's capital structure during the first half of 2018 and determined that an issuance of Tier 2 capital, at the rates available at the time, was advantageous. As a result an issuance of £25 million was made in July and a further issuance of £25 million in October. The annual coupon is 6.75% per annum. This is an annual post-tax cost of 5.4% and represents attractively priced funding which helps the group to reduce its overall weighted average cost of capital.

We will continue to seek to optimise the composition and cost of the Group's capital base particularly given our ongoing growth and ambition albeit barring major developments there are no plans to issue further capital in the forthcoming period.

Prudent liquidity management

Our year end loan to deposit ratio was 109.8% (2017: 107.8%). Customer demand for our deposit products remains very strong, and I am pleased to continue to note that the majority of customers with maturing medium term savings bonds chose to reinvest their funds into deposit products with us. The retention rate reached a new high of 80% for the December 2018 maturities.

The Bank has continued broadly to match-fund its customer lending with customer deposits. This strategy seeks to mitigate maturity transformation and interest basis risks. As the balance sheet grows we have continued to invest in our Treasury function which includes developing the capabilities to utilise hedging instruments should we determine that would be advantageous.

The new deposit platform which went live in the final quarter of 2017 performed well during its first full year of operation in 2018. This is now beginning to deliver benefits for the Group, enhancing the offering, providing internet banking, and improving efficiency and risk controls while providing flexibility to introduce new products. The new technology is also enhancing our customer service proposition whilst providing much greater scalability than the previous platform. This will allow us to fund our very short term lending activities, such as Invoice Finance and some Retail Finance, with lower cost shorter duration deposit products. This year we also plan to launch cash ISA products which typically offer lower rates than non ISA savings. The planned product diversification will enhance our competitive positioning and continue to support our approach of broadly matching assets and liabilities.

Usage of the Term Funding Scheme ('TFS') was increased prior to the closure of the scheme in February 2018 in order to lock in some of the unutilised capacity. This remains a modest part of the Bank's funding. I flagged in my equivalent statement last year that I expected the closure of the schemes to alter competitive dynamics in the deposit market and this has been the case. Deposit costs have risen modestly and this has been a factor in the compression of Net Interest Margins particularly in the mortgage market. STB's matched funding strategy and short duration loan book has allowed us to protect NIMs by passing through increases in our funding costs to new

borrowers and those whose loans are priced on a variable basis. This key area will require ongoing proactive management whilst TFS continues to unwind.

Income grew and cost of risk reduced

The Group's operating income grew by 17.1% to a record level of £151.6 million compared to the £129.5 million from continuing operations during 2017. Operating costs rose 18.5% to £84.5 million from £71.3 million in 2017, reflecting continued investment in the business. The cost to income ratio has remained stable at 55.7% (2017: 55.1%).

During 2017 the Group reduced its risk appetite and evolved the business model away from higher risk unsecured consumer credit and towards lower risk secured lending across a focused group of attractive asset classes. This repositioning has driven the expected substantial reduction in cost of risk.

On 1 January 2018, IFRS 9 became effective. IFRS 9 is a more volatile methodology compared to the previous IAS 39. Changes in the performance of underlying loan balances are more immediately reflected in the required IFRS 9 impairment charge as this operates on a forward looking basis whereas under IAS 39 provisions are raised as losses are incurred. The impairment requirement differential is most pronounced in rapidly growing or shrinking and rapidly improving or deteriorating portfolios. The improvement in the quality of the Motor Finance book over 2018, as described in more detail below, has consequently led to a much improved impairment charge for the year using IFRS 9 when compared to the previous year's result using IAS 39. A future deterioration in performance or economic factors could lead to the reverse impact. Ultimately the profit arising from a particular loan and the associated cash flows are unchanged.

The introduction of IFRS 9 serves to complicate prior year comparisons. On a continuing basis the IAS 39 impairments for 2017 were £33.5 million representing a cost of risk of 2.4% based on average customer lending balances. On a reported basis the IFRS 9 impairment charge for 2018 is £32.4 million representing a cost of risk of 1.8% based on average customer lending balances.

We have carefully monitored lending markets throughout 2018 and note that lenders operating in the sub prime market reported a trend of increasing impairments. These trends would appear to vindicate our decisions to exit sub prime motor finance and near prime medium term personal loans after we identified warning signs in this part of the market in late 2016.

Customer lending activities

Once again strong double digit percentage growth was achieved across the Group's loan portfolio in 2018 notwithstanding the run off of the legacy subprime motor portfolio. Total annual new business lending volumes grew 17.2% to £1,261.9 million (2017: £1,077.1 million) which translated to an increase of 26.9% in overall balance sheet customer lending assets to £2,028.9 million (2017: £1,598.3 million for continuing operations).

Consumer Finance

In 2018 total consumer lending, excluding mortgages, increased 22.0% to £905.7 million (2017: £742.5 million). Our Consumer Finance lending strategy during 2018 centred on running off the sub prime motor portfolio and allocating capital to support the continued growth in Retail Finance, which is shorter term in duration and prime in nature, and higher quality new business in Motor Finance.

The Retail Finance point of sale business, net of provisions, grew strongly as intended, with customer lending balances at 31 December 2018 increasing 32.1% to £597.0 million (2017: £452.3 million). Our Retail Finance business has continued to evolve as we have grown into one of the largest participants in this market. We are writing a broader spectrum of business including increased levels of interest bearing lending. This lending has higher levels of impairments compared to interest free finance and this is factored into our pricing to ensure we achieve our targeted risk adjusted return. The impairments and risk adjusted returns in 2018 have been in line with our expectations. However, the volatility of the IFRS 9 methodology compared to IAS 39, coupled with the rapid balance sheet growth has an impact on the V12 reported results.

During the year we made significant progress in repositioning the motor book. The legacy sub prime loans have been run down to an immaterial level and we have successfully replaced these assets with new originations of a much higher quality. As a result customer lending balances, net of provisions, have been held flat year on year with £276.4

million at 31 December 2018 compared to £274.6 million in the prior year. As expected the repositioning has driven lower like-for-like impairments in the motor portfolio and profitability margins improved as the drag effect of the run off of the sub prime part of the book abated.

The markets for those debt collection agencies fully authorised by the Financial Conduct Authority improved as more operators exited the market or were consolidated within larger entities. These attributes translated into more opportunities for Debt Managers (Services) Limited ('DMS') in the third party debt collection and portfolio acquisition spaces during 2018. The Group has taken advantage of these opportunities, with DMS generating an excellent financial result. Overall, the profit before tax of £1.6 million in 2018 for this business was well above the £0.6 million recorded for the prior year.

Consumer Mortgage lending balances have increased from £16.5 million as at 31 December 2017 to £84.7 million as at 31 December 2018 being growth of 413%. During 2018 the residential mortgage market showed increasingly aggressive competitive pressures, with lenders increasingly competing on price and risk appetite to drive new business volumes. It is no surprise that in the early part of 2019 lenders including Metro Bank, Santander UK and Nationwide Building Society have all reported Net Interest Margin contraction. My expectation is that the trend of increasing loan-to-value metrics and lower new net lending margin is likely to be sustained throughout 2019 before subsequently being tempered or reversed by factors detailed below under the 'evolving regulatory and competitive environment' heading. Given we have the options to profitably deploy capital elsewhere that would otherwise be used to support residential mortgage lending, as previously disclosed we have decided to cease origination of new residential mortgage business until conditions become more favourable. This change is not expected to have a material impact on 2019 earnings.

Business Finance

The Group's SME lending operations have grown strongly, as targeted, and I expect further positive progress in 2019 given we started the year with a strong new business pipeline. Total business customer lending balances in 2018 increased 24.7% to £1,027.3 million (2017: £824.0 million). Real Estate Finance lending balances increased by 32.5% to £769.8 million as at 31 December 2018 (2017: £580.8 million).The loan book is performing well and remains biased in favour of modestly leveraged residential investment lending. This is reflected in the portfolio composition, which in round terms is split 70% / 30% in favour of investment lending versus development lending. We have continued to adopt a cautious stance towards Central London house building finance. Outside of Central London demand for property development finance has remained robust and the units we have financed have continued to sell well, in a number of cases faster and for higher values than originally expected. The average LTV across the whole Real Estate Finance portfolio remains less than 60%.

In previous statements I noted that some lenders were offering loans up to or exceeding 100% of open market value on asset finance at extremely low margins, by historical standards. 2018 saw a 10% increase in company insolvencies in England and Wales to the highest level since 2014. As such it is not surprising to note that the Asset Finance market has seen an increase in customer defaults and in impairments during the year. We are not prepared to compromise on risk or price simply to achieve short term net balance sheet growth, and as matters stand expect this part of the lending portfolio to continue to contract as we are not writing new business. Asset Finance lending balances contracted to £62.8 million as at 31 December 2018 compared to £116.7 million a year ago. We will revisit our appetite for recommencing new lending in light of market developments in this scale part of the UK SME lending market.

Secure Trust Bank Commercial Finance, the invoice finance division of the Bank, had another excellent year and has now funded over £2.5 billion of customers' invoices since launch. Excluding the systemic banks, based on customer lending balances we are now the 5th largest operator in the invoice finance market but given the fragmented nature of the market we have substantial opportunities to continue to grow very strongly in this sector. This is evidenced by customer lending balances, which net of provisions grew 53.9% to £194.7 million at 31 December 2018 (2017: £126.5 million). I continue to believe we have one of the most capable teams of invoice financiers in the UK, supported by a scalable modern IT platform. This, coupled with Group management's experience in SME and corporate lending, gives STB a distinct advantage when it comes to structuring transactions and responding rapidly to opportunities. Impairments levels here have been immaterial reflecting very robust credit management disciplines.

Fee based accounts

As expected, the legacy OneBill product, which closed for new business in 2009, continues to see customer numbers decline over time. Customer numbers fell to 18,032 by 31 December 2018 compared to 18,963 a year earlier.

Evolving regulatory and competitive environment

From a Prudential Regulation perspective it is apparent that the regulatory direction of travel with the introduction of the MREL regime and the reforms to the Basel Capital requirements is to reduce the capital differentials between the systemic and non-systemic firms which should ultimately bode well for smaller banks.

I have noticed a change in regulatory tone particularly by the Financial Conduct Authority ('FCA') during 2018. In my opinion the FCA increasingly acknowledges that when it comes to many financial products, not just in banking, loyalty does not pay, it costs. On average, long term savers are paid considerably lower interest rates than newer customers and mortgage borrowers moving from initial fixed rates to standard variable rates ('SVR') typically pay the highest interest rates. This is the thrust of the Super Complaint lodged by the Citizens Advice Bureau in 2018 which I believe is intended to tap into the changing public and political mood, especially with the ongoing drive by regulators and politicians to be seen to protect what they describe as vulnerable customers. In late December 2018 the FCA provided the following update: 'The treatment of long-standing customers remains a priority for the FCA. We have worked closely with the CMA since they received the super-complaint. We will continue to do this. It is important that this issue is tackled and harmful practices are stopped. We expect firms to look after the interests of all customers and treat them fairly, whether they are new or longstanding. Where we have concerns about conduct by firms, we will explore all options to address this using the full range of our powers'.

In banking, millions of inert savers are paid extremely low interest rates with this extremely cheap funding helping those banks concerned to use price to dominate large parts of the lending market. This is especially so in mortgages where the additional profit subsidisation effects of high SVRs on back books allows the biggest banks and building societies to charge extremely low margins on front books. These dynamics and the current capital differentials (the latter being addressed over time by the incoming Basel capital floors) are key reasons why the 10 biggest firms control 90% of that market.

The FCA has thus far followed a 'sunlight' strategy in the hope that by raising consumer awareness of the costs of inertia they would drive changes in behaviours which would give better outcomes for consumers. This has not been as successful as desired which I believe is a key reason why the FCA is now seriously considering more direct intervention. One manifestation of this is their proposed Basic Variable Minimum Savings Rate which would greatly benefit inert long term savers. This will impact the cost of the deposit back book for the larger banks and some building societies and means they would need to accept lower profits or more likely seek to maintain NIM by increasing lending margins and / or pay less for front book deposits. By definition the challenger banks do not attract inert savings customers. So if the dominant banks need to increase lending margins it should logically increase the proportion of the market that can be economically served by the smaller challengers and specialist banks.

It is worth noting that the last Competition and Markets Authority banking market investigation highlighted that residential mortgage lending was by far the most profitable thing banks do and that the systemic firms were more profitable than the smaller ones. It is entirely possible that the FCA will consider intervention in the SVR market (the huge differences between new lending margins and SVR cannot be objectively justified in my view). This has a range of ramifications not least of which is the impact on Effective Interest Rate ('EIR') accounting. EIR allows lenders to recognise mortgage profits now based on assumed customer behaviours in the future. If SVR intervention arises then there will likely be EIR and profit ramifications. Should such a situation come to pass then the likely winners will be those who do not rely on inert savers and those who do not rely on high cost SVR customers providing super profit margins on the mortgage side.

During 2018 a number of stakeholders have recognised that post Brexit HM Government could choose to adopt a much more proportionate approach to the regulation of smaller non-internationally active banks than is possible today. Certainly one of the implications of the UK's exit from the European Union is that it can address the shortcomings of the 'one size fits all' Capital Requirements Regulation implementing the Capital Requirements Directive IV, if the appetite exists.

In summary whilst the situations above remain somewhat fluid, I am increasingly optimistic that cumulative actual and potential action by regulators could help to materially improve the competitive positioning of smaller banks in the UK.

Strategic priorities

The Group's three strategic priorities of: (i) organic growth, (ii) diversification and (iii) M&A activity are unchanged.

The benefits of a diversified business model have been evident during 2018 when we have been able to reallocate capital from higher risk higher margin to lower risk lower margin lending activities whilst continuing to scale the Group's balance sheet and grow our profitability.

The focus for 2019 is on:

(i) Organic growth in responsible lending across a diverse portfolio of attractive segments.
(ii) Continued investment in broadening our product offerings to customers.
(iii) Pursuing M&A activity on an opportunistic basis.
(iv) Optimising our capital and liquidity strategies.
(v) Continuing to target delivering profit growth in the medium term to create shareholder value.

Our long-term ambition remains to grow a broad based portfolio, balanced across consumer finance, SME finance and residential mortgage lending.

We will continue to grow our Retail Point of Sale (V12) and Motor propositions in the Consumer Finance sector. V12 has delivered six years of balance sheet and profit growth since being acquired in January 2013. Whilst now a top five player it has a modest market share and considerable potential to continue growing our lending balances which are relatively short term in duration and prime in nature.

The market for Motor Finance in the UK is nearly £60 billion. This is a highly fragmented and competitive space where we have a £0.25 billion share predominantly in non-prime lending. This is an important and profitable line of business for us. We see opportunities to continue to grow our near-prime lending and have now initiated a transformation programme which will see us offering a whole of market solution to dealers and brokers. This will include dealer stocking and prime / near-prime consumer lending products. The existing lenders in this space enjoy attractive returns on equity and we believe that the combination of the competitive funding costs provided via our banking licence and brand new technology will allow us to gain market share and grow a sizable business in this space over the next 3-5 years.

Economic and political related uncertainties have influenced UK residential house prices during 2018 with these having barely appreciated in value over the period. This has informed our risk appetite for new lending to house builders in the year with our Loan to Gross Development Value limits remaining modest to ensure that the borrower has hard equity in any deal and to provide a buffer lest market values fall. Strategically we remain committed to supporting the Government policy of building more new homes and believe an orderly exit from the EU will be positive for the UK housing market. With this in mind the Group has entered into, but not yet triggered, an ENABLE Guarantee with the British Business Bank. This is designed to enable banks to increase their lending to SMEs by reducing the amount of capital required to be held against such lending. Under an ENABLE Guarantee, the UK Government takes on a portion of the counterparty's risk on a portfolio of loans to smaller businesses in return for a fee. Assuming an orderly Brexit and positive reaction in the UK housing market the Group will allocate this additional capital to increase its funding to new build and redevelopment projects undertaken by SME housebuilders and developers.

The UK Invoice Finance and Asset Finance markets are large, fragmented and growing markets of around £20 billion each. We are very pleased with the progress made by STB Commercial Finance. We see significant future growth potential and would be interested in acquiring businesses in these spaces if the risk profile and economics of any transaction are attractive.

Residential mortgage lending is the biggest single part of the UK lending market. As previously disclosed the Group has ceased originating new residential mortgage loans due to concerns about current market practices in respect of risk and price. The capital that would otherwise have been used to support mortgages lending growth is being deployed for more optimal short-term returns. We remain interested in inorganic opportunities that would get us to the critical mass necessary to be profitable, if the economics of such a transaction were compelling. I believe the factors that will serve to make market conditions more attractive over time will be the introduction of the MREL regime, the significant Basel capital reforms, the unwinding of the Term Funding Scheme, a tightening in the

securitisation market which is already impacting some non-bank lenders and the potential for FCA price intervention in the inert savings market. We will closely monitor these evolving situations which will inform our strategic thinking.

In support of our strategy, we have engaged in a number of discussions relating to inorganic business opportunities during 2018 but none progressed to a conclusion that was acceptable to us. Our previous M&A activities have generated considerable shareholder value due in part to the discipline that we apply. We will continue to be disciplined in our approach to opportunities, prioritising the creation of sustainable, long-term shareholder value. We are continuing to work on a diverse pipeline of external business opportunities.

Current trading and outlook

Notwithstanding the slowing in UK economic activity in the latter part of 2018 and into the New Year we are pleased with our performance in the early part of 2019 which is in line with management expectations.

Management and the Board are very carefully monitoring the highly fluid political situation. We have a range of early warning indicators and contingency plans in place in the event a no deal Brexit leads to an economic downturn. We have seen no discernible change in our consumer businesses. We have deliberately repositioned the Group’s balance sheet away from higher risk consumer lending to mitigate the potential of a disorderly Brexit and ensured the overall loan book is of a short duration. To provide some context the Group’s Retail Finance lending balances now exceed £600 million. On average we are lending over £50 million per month in this area. It follows that in a stressed economy we could reduce these credit exposures in a rapid and orderly fashion. This sort of option does not exist in the medium term unsecured personal loan or credit card market. This was a factor in us exiting the former in December 2017.

Economic and political related uncertainties are weighing on the UK economy albeit this has impacted businesses much more than consumers. Concerns about the potential for a no deal exit from the EU to cause a change in consumer behaviour and an increase in loan impairments due to a squeeze on the cost of living caused by a weaker pound have negatively impacted the values of UK financial assets and bank share prices. Our SME businesses have performed well and have substantial new business pipelines, some of which is due to planned transactions being delayed whilst business owners wait to see on what basis and over what timescale the UK exits the EU. Given this, the fact that current UK economic fundamentals are solid with record employment levels, the lowest unemployment since 1975 and real take home pay rising provides grounds for optimism. My belief is that an orderly Brexit will trigger an increase in business investment which will be good for employment and pay. An abating of political and economic uncertainty should be positive for the value of financial assets and business and consumer confidence generally.

In summary, the Group's lending portfolio is appropriately positioned for the current conditions and the short duration nature of the asset portfolio means the Group can react quickly to both opportunities and threats.

The Group entered 2019 with positive business momentum, healthy capital positions and very strong liquidity and remains well placed to pursue its strategic priorities.

Paul Lynam
Chief Executive Officer

27 March 2019

Financial review

Adjusted profit reconciliation	2018 Total £million	2017 Continuing operations £million	2017 Discontinued operations £million	2017 Total £million
Interest, fee and commission income	188.6	157.3	8.0	165.3
Interest, fee and commission expense	(37.0)	(27.8)	-	(27.8)
Operating income	151.6	129.5	8.0	137.5
Impairment losses	(32.4)	(33.5)	(3.4)	(36.9)
Operating expenses	(84.5)	(71.3)	(0.3)	(71.6)

Profit on sale of Non-Standard Finance plc shares	-	0.3	-	0.3
Profit before tax	**34.7**	**25.0**	**4.3**	**29.3**
Adjustments to profit before tax (see below)	2.0	2.0	(4.3)	(2.3)
Adjusted profit before tax	**36.7**	**27.0**	-	**27.0**
Adjusted tax	(6.8)	(5.5)	-	(5.5)
Adjusted profit after tax	**29.9**	**21.5**	-	**21.5**
Adjusted basic earnings per share (pence)	**161.8**	**116.4**	-	**116.4**
Statutory results				
Profit before tax	34.7	25.0	4.3	29.3
Tax	(6.4)	(5.1)	(0.8)	(5.9)
Profit after tax	**28.3**	**19.9**	**3.5**	**23.4**
Gain recognised on disposal after tax	-	-	0.4	0.4
Profit for the year	**28.3**	**19.9**	**3.9**	**23.8**
Basic earnings per share (pence)	**153.2**	**107.7**	**21.1**	**128.8**
Adjustments to profit before tax				
Fair value amortisation	0.3	0.9	-	0.9
Transformation costs	0.4	0.8	-	0.8
Bonus payments	1.3	0.6	-	0.6
Profit on sale of Non-Standard Finance plc shares	-	(0.3)	-	(0.3)
Discontinued operations	-	-	(4.3)	(4.3)
Adjustments to profit before tax	**2.0**	**2.0**	**(4.3)**	**(2.3)**

Key performance indicators

The following key performance indicators, stated for continuing operations, are the primary measures used by management to assess the performance of the Group:

Financial KPIs

Adjusted profit	Earnings per share	Return ratios
Adjusted profit before tax **£36.7 million** 2017: £27.0 million	**Basic earnings per share** **153.2 pence** 2017: 107.7 pence	**Adjusted return on average assets** **1.4%** 2017: 1.3%
Adjusted profit after tax **£29.9 million** 2017: £21.5 million	**Adjusted basic earnings per share** **161.8 pence** 2017: 116.4 pence	**Adjusted return on average equity** **13.1%** 2017: 8.9%
		Adjusted return on required equity **14.8%** 2017: 13.5%

Growth	Margin ratios	Cost ratios	Funding ratios
Loans and advances to customers **£2,028.9 million** 2017: £1,598.3 million	**Net interest margin** **7.4%** 2017: 8.1%	**Cost of risk** **1.8% on an IFRS 9 basis** 2017: 2.4% (on an IAS 39 basis)	**Loan to deposit ratio** **109.8%** 2017: 107.8%
	Net revenue margin **8.3%** 2017: 9.1%	**Cost of funds** **2.0%** 2017: 1.9%	**Total funding ratio** **118.2%** 2017: 115.5%
	Gross revenue margin **10.4%** 2017: 11.1%	**Cost to income ratio** **55.7%** 2017: 55.1%	

Non - financial KPIs

Customer FEEFO ratings	Employee survey trust index score	Environmental intensity indicator
4.7 stars 2017: 4.7 stars (mark out of 5 based on star rating from 1,175 reviews (2017: 608 reviews))	**77%** (new measure, based on 2018 all staff survey 2018 engagement score 76% 2017: 78%)	**3.5** 2017: 4.2 (tonnes carbon dioxide per £1 million Group income)

The Remuneration Report, starting on page 97, sets out how executive pay is linked to the assessment of key financial and non-financial performance metrics.

These KPIs represent alternative performance measures that are not defined or specified under IFRS. Definitions of the financial KPIs, their calculation and an explanation of the reasons for their use can be found in the Appendix to the Annual Report on page 218. In the narrative of this financial review, KPIs are identified by being in bold font. Further explanation of the non-financial KPIs is provided in the corporate responsibility section on page 54.

Unless otherwise stated, the analyses within the Strategic Report relate to continuing operations, which represents all of the Group's divisions, excluding PLD.

Interest, fee and commission income

Interest, fee and commission income is made up of interest income, which is predominantly earned on loans and advances to customers, and fee and commission income, which consists principally of fees from the OneBill, Commercial Finance, Retail Finance and Motor Finance products and commissions earned on debt collection activities in DMS.

Interest income was £169.2 million for 2018, increasing by £27.9 million (19.7%) on 2017, which was driven by the growth of the Group’s loan books over the year. **Loans and advances to customers** increased from £1,598.3 million to £2,028.9 million over the year.

Fee and commission income was £19.4 million for 2018, increasing by £3.4 million (21.3%) on 2017. The growth relates to increasing levels of fees earned on Commercial Finance and Retail Finance lending, with fee income relating to OneBill continuing to decrease year on year, as this product is closed to new business.

The **gross revenue margin** reduced from 11.1% to 10.4%. This reflects the continued repositioning of the balance sheet to lower risk lower return lending. In particular, growth in Motor Finance lending which yields relatively high margins was modest in 2018, compared with more significant growth in Retail Finance and the low risk Business Finance portfolios.

Interest, fee and commission expense

Interest, fee and commission expenses is made up of interest expense, which is incurred in respect of deposits from customers, subordinated liabilities and TFS borrowings, and fee and commission expense, comprising mainly fees and commissions on the Motor product, and commissions paid on debt collection activities in DMS.

Interest expense was £35.5 million for 2018, increasing by £8.8 million (33.0%) on 2017. The **cost of funds** increased from 1.9% for 2017 to 2.0% for 2018. The impact on the Group of the rise in the Bank of England base rate during the year was limited in 2018, given the predominantly fixed rate deposit funding. The interest expense for 2018 includes the cost of subordinated debt raised during the year, as explained further in Note 24.

The Group’s **net interest margin** reduced from 8.1% in 2017 to 7.4% in 2018, primarily due to the mix of business referred to above.

Fee and commission expense has increased by £0.4 million (36.4%), mainly arising from the increase in activity in DMS, as set out in the business review on page 36.

Operating income

Operating income increased by 17.1% to £151.6 million (2017: £129.5 million).

The **net revenue margin** for 2018 was 8.3% compared with 9.1% for 2017. The reduction in this margin is due to the factors referred to above.

Impairment losses

Impairment losses during the year were £32.4 million (2017: £33.5 million). The impairment losses for 2018 are calculated using the expected credit loss methodology required by IFRS 9, whereas the comparative impairment losses for 2017 were calculated using the incurred loss methodology set out in IAS 39. The expected increase in charge brought about by the change in methodology to IFRS 9, which accelerates the recognition of losses particularly for growing books, has been offset by improvement in performance, particularly in respect of Motor Finance lending.

The provision charge includes the impact of applying expert credit judgement, resulting in overlays being added to provision levels estimated using the Group's models. A breakdown of the charge by product is shown in Note 3.

The **cost of risk** for 2018 on an IFRS 9 basis was 1.8%. The cost of risk on an IAS 39 basis was 2.4% for 2017. Further analysis of the Group's loan book and its credit risk exposures is provided in Notes 11, 12, 13 and 30.

Operating expenses

Operating expenses have increased, reflecting the investments made in the infrastructure and staff resources of the Group to achieve growth targets, from £71.3 million in 2017 to £84.5 million in 2018. The Group's **cost to income ratio** increased to 55.7% from 55.1% for 2017. The infrastructure growth has been focused on motor transformation, Treasury and risk management enhancements.

Taxation

The effective adjusted tax rate has fallen to 18.5%:

	2018 Effective adjusted tax rate £million	2018 Effective statutory tax rate £million	2017 Effective adjusted tax rate £million	2017 Effective statutory tax rate £million
Tax	6.8	6.4	5.5	5.1
Profit before tax	36.7	34.7	27.0	25.0
Effective rate (%)	**18.5%**	**18.4%**	**20.4%**	**20.4%**

The effective rate in the year was reduced by a deferred tax credit of £0.5 million arising from a reassessment of the rates that the deferred tax asset on the IFRS 9 transition adjustment will reverse out at over the next nine years. The tax charge reflects Bank Corporation Tax Surcharge of 8% on taxable profits of Secure Trust Bank PLC in excess of £25.0 million. Future effective tax rates for the Group will be sensitive to the quantum of projected profits in the Bank and other Group companies as well as the level of corporation tax which is due to reduce to 17% with effect from 1 April 2020. Current forecasts show that the effective tax rate is expected to increase by up to 4% over the forecast period, as the effect of the banking surcharge becomes more significant.

Distributions to shareholders

The directors recommend the payment of a final dividend of 64 pence per share which, together with the interim dividend of 19 pence per share paid on 28 September 2018, represents a total dividend for the year of 83 pence per share (2017: 79 pence per share).

Earnings per share

Detailed disclosures of earnings per ordinary share are shown in Note 8 to the Annual Report. Basic earnings per share increased by 42.2% to 153.2 pence per share (2017: 107.7 pence), as a result of the increase in profit after tax. The **adjusted basic earnings per share** increased by 39.0% to 161.8 pence per share (2017: 116.4 pence per share).

Adjusted returns

The Group measures **adjusted returns on average assets, average equity and required equity** as set out in the KPIs table on page 18. Return on average assets demonstrates how profitable the Group's assets are in generating

revenue. Return on average equity is a measure of the Group's ability to generate profit from the equity available to it. Return on required equity relates profitability to the capital that the Group is required to hold.

These ratios have all improved in comparison to 2017, driven by a combination of the improving profitability and the impact of the IFRS 9 transition adjustment reducing assets and equity at 1 January 2018.

Summarised balance sheet

	2018 £million	2017 £million
Assets		
Cash and balances at central banks	169.7	226.1
Debt securities	149.7	5.0
Loans and advances to banks	44.8	34.3
Loans and advances to customers	2,028.9	1,598.3
Other assets	51.2	27.9
	2,444.3	**1,891.6**
Liabilities		
Due to banks	263.5	113.0
Deposits from customers	1,847.7	1,483.2
Tier 2 subordinated liabilities	50.4	-
Other liabilities	45.6	46.3
	2,207.2	**1,642.5**

The assets of the Group increased by 29.2% to £2,444.3 million, primarily driven by the growth in the Group's loan portfolios.

The liabilities of the Group increased by 34.4% to £2,207.2 million, primarily driven by the increase in deposits from customers, providing funding for the Group's lending activities, the use of the Term Funding Scheme as shown in amounts due to banks, and the issue of £50 million of Tier 2 regulatory capital.

Loans and advances to customers

Loans and advances to customers include secured and unsecured loans and finance lease receivables. The composition of the loan book remains broadly consistent with 2017, with the Consumer Finance book being approximately 45% of total lending, and the Business Finance book being approximately 51%. The Consumer Mortgage business currently accounts for 4% of total lending.

Loan originations in the year, being the total of new loans and advances to customers entered into during the year, increased by 17.2% to £1,261.9 million (2017: £1,077.1 million). Over half of the new business volume (£651.5 million) was generated by the Retail Finance business.

Further analysis of loans and advances to customers, including a breakdown of the arrears profile of the Group's loan books, is provided in Notes 11, 13 and 30.

Debt Securities

Debt Securities consist solely of sterling UK Government treasury bills. The increase in the year to £149.7 million from £5 million in 2017 was for the purpose of providing collateral against Term Funding Scheme drawings with the Bank of England.

Due to Banks

The amount due to banks consists solely of drawings from the Bank of England Term Funding Scheme. The Group has drawn modest levels of this low cost source of funding to supplement customer deposit funding.

Deposits from customers

Customer deposits include term, notice and sight deposits, as well as the Group's current account and OneBill products. Customer deposits grew by 24.6% during the year to close at £1,847.7 million, to fund the increased lending balances.

Tier 2 subordinated liabilities

Tier 2 subordinated liabilities represent two £25 million tranches of 6.75% Fixed Rate Callable Subordinated Notes, including interest accrued. Further details of the note issuances are provided in Note 24. The notes qualify as Tier 2 capital. In the previous year, the Group's Tier 2 capital consisted solely of the collective impairment allowance.

New accounting standards

IFRS 9 'Financial Instruments', effective for the period beginning on 1 January 2018, has replaced IAS 39 'Financial Instruments: Recognition and Measurement'. Adoption of the standard has resulted in new accounting policies for interest income and expense, the classification and measurement of financial instruments and the impairment of financial assets and loan commitments which are set out in Note 1. Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except that comparatives for the year ended 31 December 2017 are stated on an IAS 39 basis, and therefore have not been restated.

IFRS 15 'Revenue from contracts with customers', which is also effective for the period beginning on 1 January 2018, replaces a number of existing standards and interpretations. Following consideration of the Group's operating model, it has been concluded that this standard does not have a material impact on the Group.

Discontinued operations

On 21 December 2017 the Group sold a portfolio of legacy unsecured personal loans ('PLD') to Alpha Credit Solutions 8 S.à.r.l., a company owned by AnaCap Credit Opportunities III LP. Results relating to the portfolio of unsecured personal loans have therefore been classified as discontinued operations for the year ended 31 December 2017 throughout this Annual Report. The profit before tax relating to the unsecured personal loan portfolio announced shortly after its sale for the year ended 31 December 2017 has been adjusted for statutory purposes as follows:

	Profit before tax as announced	Internal cost of funds added back	Internal attributable costs added back	Statutory profit before tax	Tax	Statutory profit after tax
	£million	£million	£million	£million	£million	£million
Year ended 31 December 2017	2.4	1.5	0.4	4.3	(0.8)	3.5

Capital' leverage and liquidity

Capital

The Group's capital management policy is focused on optimising shareholder value over the long-term. Capital is allocated to achieve targeted risk adjusted returns whilst ensuring appropriate surpluses are held above the minimum regulatory requirements. The Board reviews the capital position at every Board meeting.

The Group's regulatory capital is divided into:

- CET1 which comprises shareholders' funds, after adding back the IFRS 9 transition adjustment and deducting intangible assets, both of which are net of attributable deferred tax
- Tier 2 capital, which is solely subordinated debt issued during the year net of unamortised issue costs, capped at 25% of the capital requirement. At 31 December 2017, Tier 2 capital represented the collective allowance for impairment. Under IFRS 9, there is no longer a collective allowance.

In July 2018 the Group issued £25.0 million of Tier 2 capital and a further £25.0 million was issued in October 2018. Further information on these issuances is contained in Note 24.

The Group has elected to adopt the IFRS 9 transitional rules. For 2018 this allowed 95% of the initial IFRS 9 transition adjustment, net of attributable deferred tax, to be added back to eligible capital. Further information is provided in the Group's Pillar 3 report available at www.securetrustbank.com/investor-information.

Strategic and capital allocation decisions are therefore made with reference to estimated credit losses calculated using IFRS 9 methodology.

The Group's Individual Capital Adequacy Assessment Process ('ICAAP') includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. All regulated entities within the Group have complied during the year with all of the externally imposed capital requirements to which they are subject.

The Group operates the standardised approach to credit risk, whereby risk weightings are applied to the Group's on and off balance sheet exposures. The weightings applied are those stipulated in the Capital Requirements Regulation.

	2018 (IFRS 9 transitional rules basis) £million	2017 £million
Capital		
CET1 capital	251.8	238.9
Total Tier 2 capital	45.7	4.4
Total capital	**297.5**	**243.3**
Total Risk Exposure	**1,824.6**	**1,446.1**

	2018 (IFRS 9 transitional rules basis %	2017 %
CRD IV ratios		
CET1 capital ratio	13.8	16.5
Total capital ratio	16.3	16.8
Leverage ratio	10.0	12.3

The CET1 capital ratio is the ratio of CET1 capital divided by the Total Risk Exposure. The total capital ratio is total capital divided by Total Risk Exposure. The Group has maintained a healthy CET1 capital ratio and total capital ratio and these provide a capital buffer for continued growth.

Leverage

The Basel III framework introduced a relatively simple, transparent, non-risk based leverage ratio to act as a supplementary measure to the risk-based capital requirements. The leverage ratio is intended to restrict the build-up of leverage in the banking sector to avoid destabilising deleveraging processes that can damage the broader financial system and the economy, whilst reinforcing the risk-based requirements with a complementary simple, non-risk based 'backstop' measure.

The Basel III leverage ratio is defined by the Capital Requirements Regulation as Tier 1 capital divided by on and off balance sheet asset exposure values, expressed as a percentage. The UK leverage ratio framework sets a minimum ratio of 3.0%, which increased to 3.25% on 1 January 2018. As shown in the table above, the Group's leverage ratio remains comfortably ahead of the minimum requirement.

Liquidity

The Group continues to manage its liquidity on a conservative basis by holding High Quality Liquid Assets and utilising predominantly retail funding from customer deposits. Secure Trust Bank is a participant in the Bank of England's Sterling Money Market Operations under the Sterling Monetary Framework. As such, from July 2013, the Group was permitted to draw down facilities under the Funding for Lending Scheme and subsequently its replacement, the Term Funding Scheme.

At the year end and throughout the year, the Group had significant surplus liquidity over the minimum requirements due to its stock of High Quality Liquid Assets ('HQLA'), in the form of the Bank of England Reserve Account and UK Treasury Bills. As shown in the table below, total liquid assets increased by 37.2% from £265.4 million to £364.2 million, with the High Quality Liquid Assets balance being £319.4 million.

	2018 £million	2017 £million
Liquid assets		
Aaa – Aa3	319.4	231.1
A1 – A3	39.7	29.3
Unrated	5.1	5.0
Liquidity exposures	**364.2**	**265.4**

For Liquidity Coverage Ratio ('LCR') purposes the HQLA excludes UK Treasury Bills which are encumbered to provide collateral as part of the Group's Term Funding Scheme with the Bank of England. The total of unencumbered HQLA for LCR purposes is £240.8 million (2017: £231.1 million).

The Group has no liquid asset exposures outside of the United Kingdom and no amounts that are either past due or impaired.

The Group's LCR, and other measures used by management to manage liquidity risk, are described in the Principal Risks and Uncertainties section of the Strategic Report.

Business review – Business Finance

Real Estate Finance

Real Estate Finance was formed as a division within the Group in 2013. The division supports SMEs in providing finance principally for residential development and residential investment.

What we do

Residential Development

The Group lends to enable the development of new build property, commercial to residential conversions (including those with permitted development rights) and refurbishment projects.

Residential Investment

The Group lends on portfolios of residential property where the rental income will repay the underlying borrowing over a fixed term period. This excludes the regulated buy-to-let mortgage sector.

Other lending

The Group has limited appetite for other commercial lending (either development or investment) and has limited exposure to mixed development schemes.

How we do it

Financing is typically provided over a term of up to five years with prudent loan-to-value criteria, with a 60% Loan to Gross Development Value to residential house builders. More restrictive policies are implemented from time to time as required: for instance the Group reduced its financing of residential developments in Central London in 2015. The Group's Loan to Gross Development Value / loan-to-value ratios continue to average below 60% across all lending areas. The Group has no significant exposure to any one property scheme or developer.

The Real Estate Finance team is staffed by experienced bankers with proven property lending expertise. The team provides full support to customers and introducers over the life of the products.

Revenue and lending performance vs prior years

	2018 £million	2017 £million	2016 £million
Revenue	41.2	32.3	28.4
Lending balance	769.8	580.8 (£581.0 million on an IFRS 9 basis*)	451.0
Impairment charge/(credit)	0.5	(0.2)	0.1

*See Appendix for reconciliation

2018 performance

The business has continued to grow its Real Estate Finance business, with balances up 33% in 2018, which generated a 28% increase in revenue. The rate of growth in the first half of 2018 slowed due to an increase in repayments. The mix of the book between development and investment has remained stable, with development lending representing 30% of the book at end of 2018.

The credit quality of the book has remained strong, with no crystallised impairments and a low level of watch list cases. The impairment charge reflects an increase to loss given default due to the estimated impact of a change in the level of property sales in the event of repossession.

Looking forward

The business further added to its origination team in 2018 and expects to continue to grow balances, with an intent to focus on diversifying the mix of business, both in terms of introduction source and geographic location. The business does however continue to remain cautious around credit policy in the light of more uncertain market conditions, and can react quickly to any threats which may emerge. Growth will be managed carefully to ensure that returns are maximised whilst maintaining credit quality.

"We wanted to express our appreciation of the way Secure Trust Bank have assisted us and joined us in progressing this complicated and exciting project. From the outset the bank has shown real enthusiasm and have committed a lot of time to absorb and assist with the best way forward. You have readjusted the facility to ensure that our progress is both enjoyable and comfortable. We are impressed by the way you are very approachable which has ensured that any complications that have arisen have been resolved without holding up progress.

We are very pleased that we made the decision to go with Secure Trust Bank on this venture and a big thank you from our team to the bank."
Neobrand No. 2 Limited

Asset Finance

Asset Finance was formed as a division within the Group in December 2014.

What we do

The Asset Finance business provides funding to support SME businesses in acquiring commercial assets, such as building equipment, commercial vehicles and manufacturing equipment.

How we do it

The Asset Finance business is operated via a joint venture with Haydock, a well-established asset finance company operating across the UK. Following the change in ownership of Haydock in January 2018, the Group has ceased writing new business through the joint venture, although Haydock continues to provide a full business process outsourcing service to the Group in relation to the portfolio funded by the Group.

The current portfolio reflects hire purchase and finance lease arrangements with terms of up to five years.

Revenue and lending performance vs prior years

	2018 £million	2017 £million	2016 £million
Revenue	6.6	8.5	7.8
Lending balance	62.8	116.7 (£116.5 million on an IFRS 9 basis*)	117.2
Impairment charge	2.2	1.0	0.6

*See Appendix for reconciliation

2018 performance

Following the decision to cease writing new business in February 2018, the portfolio is in run-off. The lending balances and income have reduced during 2018, with balances reducing by £54 million (46%) in 2018. As a consequence of this run-off, lending revenue has also reduced in 2018.

Impairment losses have increased in 2018 by £1.2 million compared to 2017, reflecting an increase in the value of cases taken into collections.

Looking forward

The Asset Finance division has operated through a joint venture with Haydock Finance to date. With the change in ownership of Haydock in January 2018, the business has ceased originating new business, and continues to assess options within the Asset Finance market. The portfolio is expected to reduce in line with contractual repayments from customers.

Commercial Finance

Commercial Finance was formed as a division within the Group in 2014.

What we do

The division specialises in providing a full range of invoice financing solutions to UK businesses including invoice discounting and factoring.

Invoice discounting services provide access to funding and release typically up to 90% of the value of qualifying invoices, in confidence and allowing clients to stay in control of sales ledger management.

Factoring services, where the sales ledger management is passed on to the Group, may also provide access to funding of typically up to 90% of the value of qualifying invoices and often results in the Group managing credit control, cash allocation, statement and reminder letter distribution.

Other assets can also be funded either long or short term and for a range of loan-to-value ratios alongside these facilities.

How we do it

Commercial Finance complements the broader SME lending proposition which has been developed by the Group. The business also provides SME commercial owner occupiers with finance to buy the property they trade from in conjunction with other financing facilities.

The division has built a strong team of proven business development, credit and operational professionals who have delivered a robust and compliant operational model.

Revenue and lending performance vs prior years

	2018 £million	2017 £million	2016 £million
Revenue	13.4	7.2	4.6
Lending balance	194.7	126.5 (£126.3 million on an IFRS 9 basis*)	62.8
Impairment charge	-	0.1	0.2

*See Appendix for reconciliation

2018 performance

The Commercial Finance business saw further strong growth in 2018, with lending balances increasing by more than 50%. Income consequently saw strong growth while the cost base increase was marginal. Impairment losses continue to be minimal. In the year Commercial Finance opened offices in Birmingham, Leeds and London and recruited high calibre people from the industry, building on its focus on growth from a strong platform.

Looking forward

The team has built a reputation for high quality service, particularly within its chosen markets, and as a result the prospects for future growth are encouraging. Further national expansion through development of its regional footprint will provide the Group with a more scalable business model on which to achieve this growth.

Secure Trust Bank Commercial Finance provided a £15 million asset based lending facility to Carpet & Flooring (Trading) Limited, one of the UK's leading distributors of floor covering products. The company supplies to a wide

range of sectors, including healthcare, leisure and education. With turnover of £100 million, Carpet & Flooring employs more than 380 people across the country.

"We are delighted to have secured this additional funding from Secure Trust Bank which will support us as we deliver organic growth and pursue targeted acquisitions. The business is now in an excellent position and we're pleased to be working with Secure Trust Bank on the next phase of our plan."
Lisa Tomlin, Chief Executive Officer at Carpet & Flooring

Secure Trust Bank Commercial Finance provided a £2.3 million finance facility to Twisted Automotive to support its purchase of 240 vehicles from the iconic Land Rover Defender's last ever production run.
"With time running out on production, in 2015 we spotted a unique opportunity to increase our inventory and introduce pre-built versions of our vehicles, which helped us tackle the long waiting list and boost our revenues. With this new financial strength, we can look at expanding overseas and ready ourselves for a potential launch of a new Defender model in 2020."
Charles Fawcett, Founder of Twisted Automotive

Business review – Consumer Finance

Retail Finance

Retail Finance includes lending products for in-store and online retailers to enable consumer purchases.

What we do

The Retail Finance business, branded as "V12", provides unsecured, prime lending products to the UK customers of its retail partners to facilitate the purchase of a wide range of consumer products across in-store, mail order and online channels. This business is driven by V12 Retail Finance, which was acquired in 2013 and has provided finance in cooperation with its retail partners for more than 20 years. The V12 point of sale system is used by the Group's retail partners and Retail Finance is administered from the V12 offices in Cardiff.

Retail Finance products are unsecured, fixed rate and fixed term loans of up to 84 months in duration with a standard maximum loan size of £25,000. The average new loan is for £1,000 over a 24 month term. Lending is restricted to UK residents who have a good credit history and can demonstrate that they can afford to repay the loan.

The finance products are either interest bearing or have promotional credit subsidised by retailers, allowing customers to spread the cost of purchases into more affordable monthly payments.

How we do it

The Group operates an online e-commerce service to retailers, providing finance to customers of those retailers. The online processing system allows customers to digitally sign their credit agreements, thereby speeding up the pay-out process, and removing the need to handle and copy sensitive personal documents through electronic identity verification.

The Group serves retailers across a broad range of retail sectors including cycle, music, furniture, outdoor/leisure, electronics, dental, jewellery, home improvements and football season tickets.

The Group provides finance to customers of a large number of retailers including household names such as Jessops, Halfords, DFS, Sofology and Watchfinder.

Revenue and lending performance vs prior years

	2018 £million	2017 £million	2016 £million
Revenue	62.8	50.7	36.7
Lending balance	597.0	452.3 (£442.1 million on an IFRS 9 basis*)	325.9
Impairment charge	19.3	13.8	9.5

*See Appendix for reconciliation

2018 performance

The Retail Finance business has continued to grow strongly, with new gross lending volumes increasing to £651.5 million (an increase of 25% on the previous year). This has driven a further significant increase in lending assets, which during the year rose to £597.0 million (December 2017: £452.3 million). Market share increased from 5.6% in 2017 to 6.8% in 2018 (based on Finance & Leasing Association new business values within retail store and online credit).

Each of the three largest sub-markets for the business (sports and leisure, furniture and jewellery) have contributed to this growth, which as in previous years has been achieved through a combination of gaining increased market share and sector growth.

Revenue increased by 24% to £62.8 million (2017: £50.7 million). Impairment losses were well controlled at £19.3 million (2017: £13.8 million) and reflect accelerated provisioning under IRFS 9 aligned to a growing book.

Customer feedback, measured by FEEFO, provided the business with a score of 4.8 out of 5 for the year based on 400 reviews.

Looking forward

The Group plans further growth in Retail Finance during 2019 with the focus on acquiring increased market share across its target markets.

To underpin the continued growth, the Group continues to invest in initiatives to further enhance its systems capabilities, to ensure that quality of service to both retailers and customers is maintained or improved. This includes the online account management service, which allows customers to view their statement online and make routine self-serve changes to their account such as change of payment date and settlement.

"Great service, reasonable interest rates and fast service, thanks."
"The service we received was brilliant, was really quick to do everything on my phone with no complicated steps. I would absolutely recommend."
"Very good service with quick application and reliable credit check. Have used V12 three times and it's always been quick and easy process."
"Service was efficient and quick. Would highly recommend and currently have other accounts in place - therefore I would use the service again."
"Easy to apply all information required supplied quickly and easily. Would recommend as a hassle free route to fund your purchase at a great rate."

Motor Finance

Finance is arranged through motor dealerships, brokers and internet introducers and involves fixed rate, fixed term hire purchase arrangements, predominantly on used cars.

What we do

The Group's Motor Finance business began lending in 2008 under the Moneyway brand and provides hire purchase lending products to a wide range of customers including those who might otherwise be declined by other finance companies. This helps the Group's customers to gain the freedom and flexibility that motoring gives to their lives as well as helping introducers to sell more cars.

Motor Finance agreements are secured against the vehicle being financed.

The Group has ceased writing new business in the sub prime market and is predominantly lending to finance the purchase of volume franchise used cars in the near-prime market.

How we do it

The Bank distributes its Motor Finance products via UK motor dealers, brokers and internet introducers. New dealer relationships are established and managed by the Group's UK-wide Motor Finance sales team with all introducers subject to a strict vetting policy, which is reviewed on a regular basis.

The technology platform used allows Moneyway to: receive applications online from its introducers; provide an automated decision; facilitate document production through to pay-out to dealer; and manage in-life loan accounts.

Motor lending is administered in Solihull; however the UK motor dealers and brokers are UK-wide.

Lending performance v prior years

	2018 £million	2017 £million	2016 £million
Revenue	48.5	47.1	40.5
Lending balance	276.4	274.6 (£253.0 million on an IFRS 9 basis*)	236.2
Impairment charge	11.3	20.8	14.6

*See Appendix for reconciliation

2018 performance

The Motor Finance business narrowed its credit parameters during 2017 in order to reduce potential future impairment losses. New business volumes in 2018 reflect a higher credit quality. There was a consequent decrease in new business volumes from £142.8 million in 2017 to £141.3 million for 2018.

Impairment losses for the period have improved from £20.8 million to £11.3 million. The improvement in the quality of the book, reflecting both the shift away from sub prime motor lending discontinued during 2017, and improved collections performance have driven the reduction in losses. These improvements are amplified by the change to IFRS 9, because the expected credit loss approach required by that standard accelerates the recognition of improved performance. The improvement has been supported by the Motor Finance leadership increasing levels of resource and delivering process improvement within the Collections and Recoveries teams.

Revenue improved modestly, by 3.0%, reflecting the reduction in margin for higher credit quality business. This shift in business alongside improved collections performance has driven the improvement in impairments.

Looking Forward

The Motor Finance business plans to expand operations into the prime credit market, to drive long-term receivables growth and sustainable return outcomes. A clear opportunity exists to deliver prime and near-prime products and services in the Motor lending market for an innovative and technology led funding provider.

A programme of work is underway to deliver a new platform and business transformation through 2019/2020 with £1.4 million already invested in 2018. As part of this programme the Motor Finance business is aiming to enhance system capabilities and to deliver a broader range of products.

This is expected to improve the credit quality of the portfolio, drive business growth and deliver stable earnings. Alongside these initiatives, the business will continue to focus on the near-prime market sector through its existing introducer channel.

Over the year the business has made some key appointments to support the transformation of the business and drive growth in the prime and near-prime motor business with the new Motor leadership team all now on board.

“Moneyway have been great to deal with in 2018. The Regional support team have been very helpful and we get lots of good feedback from the sites. The improvements made in pay-out times and ease of use have certainly helped lift their reputation."
Evans Halshaw

“Since UK Car Finance began its working relationship with Moneyway, we have seen many changes, innovations and improvements. The entire culture of the business seems geared up to making everything easy, straightforward and above all else, sensible. From the systems, account management team to their processes, Moneyway are without doubt a business we enjoy working with and look forward to working in partnership with them for many years to come.”
UK Car Finance Limited

Debt Managers (Services) Limited

Debt Managers (Services) Limited (‘DMS’) was purchased by the Group in January 2013.

What we do

DMS is the Group's debt collection business. DMS collects debt on behalf of a range of clients as well as for Group companies. It also selectively invests in purchased debt portfolios from fellow subsidiary undertakings and external third parties.

How we do it

Debt Managers (Services) offers three services across credit management and in order to meet the needs of its clients:

- Business process outsourcing allows DMS to assist in the performance of early arrears accounts on behalf of clients
- Contingent collection allows a client to place accounts with Debt Managers (Services) for DMS to manage those accounts in its own name
- Debt purchase allows DMS to acquire accounts and choose how to liquidate those accounts over a period of 10 years.

DMS aims to provide all customers with the best possible customer service by recognising every customer is different. All customer facing staff receive training on how to effectively use models such as TEXAS and IDEA to help identify signs of vulnerability and on how to use tailored signposting relevant to customers' circumstances. Customers that need additional support are managed by a specialist Customer Care Team. DMS works closely with debt charities such as StepChange, Payplan and Christians Against Poverty and a range of other third parties including the Samaritans, MIND and Marie Curie to ensure that customers receive an appropriate service.

Lending performance v prior years

	2018 £million	2017 £million	2016 £million
Revenue	7.0	4.9	3.7
Lending balance	32.3	15.6 (£15.6 million on an IFRS 9 basis*)	13.5
Impairment charge	N/A	N/A	N/A

*See Appendix for reconciliation

As DMS purchases assets which are credit impaired, impairment charges are unlikely to materialise.

2018 performance

In 2018 DMS performed well with revenue increasing by 43% from £4.9 million to £7.0 million and profit before tax increasing significantly from £0.6 million to £1.6 million. This was achieved through the development of relationships with new and existing clients and a broadening of service offerings.

Looking forward

The positive momentum in the year is expected to continue into 2019 having established strong relationships and forward flow contracts with existing clients. This is expected to result in continued growth of both revenue and profit. Leveraging new technologies will enhance customer engagement and will facilitate penetration of new sectors. The ownership of DMS by the Bank means it is well placed to identify and take advantage of growth opportunities in the coming year.

Business review – Consumer Mortgages

Consumer Mortgages was launched on 20 March 2017. The division supports residential customers who are underserved by the traditional high street lenders.

What we do

The division lends to individuals who wish to purchase a property or remortgage their current property.

How we do it

Consumer Mortgages provides, through intermediaries, competitive fixed rate mortgage products to people whose personal circumstances do not fit the norm but are still credit worthy individuals with good affordability.

Financing is typically provided over a term of up to 35 years with fixed interest rate periods of 2, 3 and 5 years. The Group's purchase and remortgage products have a maximum loan to value of 90% and a maximum loan size of £2 million.

The Consumer Mortgage team is staffed by experienced mortgage and banking individuals with proven property lending expertise and underwriting skills. The team provides full support to customers and introducers over the life of the products.

Revenue and lending performance vs prior years

	2018 £million	2017 £million	2016 £million
Revenue	1.5	0.1	-
Lending balance	84.7	16.5 (£16.5 on an IFRS 9 basis*)	-
Impairment charge	0.2	-	-

*See Appendix for reconciliation

2018 performance

The Mortgage business has steadily grown since its launch. In 2018 Mortgages originated £70 million of lending and finished the year with a book of £84.7 million. As a result of market conditions, with lenders competing aggressively on price and loan-to-value metrics across the sector increasing alongside falling margins, the Group tempered its mortgage lending.

Looking forward

In the first quarter of 2019 due to the difficult economic climate, increased competition and the continued uncertain outlook, the Group announced the decision to cease new mortgage originations until market conditions improve.

Business review – Savings

The Group attracts funding primarily via retail savings, offering individuals competitive, simple products, applied for online and serviced through a highly commended online proposition, backed by UK based customer service.

What we do

The Group offers simple, straightforward notice and fixed term accounts, promoted via best buy tables and with the endorsement of national press and market commentators, available to UK based individuals saving from £1,000. Historically, the Bank has also offered business accounts priced to reflect the different associated costs and risks.

Covered by the UK Financial Services Compensation Scheme up to the specified limits, the Group offers accounts in line with its ongoing funding needs, including 14 to 180 day notice and 1 to 7 year fixed terms with a maximum balance of £1 million for sole account holders and £2 million for business and joint accounts.

Customers can choose to capitalise or pay away their interest, with annual interest on bonds and quarterly on notice accounts. The Group this year also introduced the option on limited bond products to receive a monthly income.

Alongside Savings, the Group continues to service OneBill, in operation for many years and closed in 2009 to new customers, designed to aid with household budgeting. Customers provide details of their annual bills which are aggregated and calculated into a fixed weekly or monthly schedule so customers can spread the cost of their bills through the year, receiving direct debit discounts and support liaising with providers. A monthly fee is charged.

How we do it

By virtue of the absence of a branch network, a policy of not cross-subsidising loss making products with profitable ones, a stable funding base and an operational model based on digital self-service, the Group is able to offer competitive rates and has been successful in attracting high volumes of deposits in short timescales from a wide range of customers. This provides a funding profile which gives additional financial security to the business.

The Group enters the market for deposits as and when it is necessary and maintains a funding strategy of broadly matching the term and tenor of its customer savings to the desired maturity profiles of the Group which are primarily determined by the interest rates and terms offered on loans and advances to customers. This strategy seeks to help mitigate maturity transformation and interest basis risks.

The Group is able to adjust the mix of interest rate offered and term or notice period in a manner that allows it to raise funding quickly. As part of this funding strategy, the Group may only offer savings accounts for limited periods

of time and, from time to time, may not offer new products to customers at all. The Group will cease offering products when the need for funding at that time has been satisfied.

The marketing methods employed include providing information about the savings accounts offered on price comparison websites, newspaper best buy tables and articles and via online endorsement (for example Money Saving Expert). In addition to attraction based on interest rate, customers choose Secure Trust Bank based on its financial standing, UK based operation and high standards of cyber and operational security.

Savings balances vs prior years

	2018 £million	2017 £million	2016 £million
Notice deposits	516.4	455.3	373.8
Fixed Term Savings	1,316.8	1,013.4	762.8
Sight/Instant Access	14.5	14.5	15.2
Total Balances	**1,847.7**	**1,483.2**	**1,151.8**

2018 performance

2018 represented the first year the Group operated on a new digital platform following on from a successful migration in late 2017. In the year, the Bank grew its retail savings by £364.5 million, an increase of 24.6% - equivalent to almost £12 every second. This represents nearly 26,000 new accounts and 17,000 new savings customers joining the Group this year.

In the year the Bank won a number of awards, including Best Savings Provider from Savings Champion, as well as Best Fixed Rate Bond and Best Notice Account Provider. The Group was also highly commended by The Money Pages as Best Online Savings Provider, with all of these awards independently judged and customer focused.

Throughout the year the Group has offered competitive savings products featuring in a best buy table every week. At the last point of reporting in October 2018, the Group achieved 7.5% of fixed rate bond sales online according to eBenchmarkers – a considerable achievement of many times its natural market share of non-ISA savings balances.

The introduction and adoption of online servicing has been a focus in 2018. At the start of the year, the Group had a handful of trial customers registered. At the end of December, over 30,000 customers are now registered, 70% of the overall deposit customer base, with 58% having signed in at least once. For new customers, 99.9% register and over 74% sign in at least once.

It is worth noting that 2018 marks a number of considerable milestones for the Group's savings business over the past five years, having grown balances by 323% or £1.4 billion from the start of 2014, increased the number of accounts by 115% or 26,000 and opened almost 70,000 new accounts and attracting over 37,000 customers. The Group now has customers across the majority of counties in England, Wales and Scotland, and from Shetland to Cornwall and from Norfolk to Belfast.

Looking forward

The Group plans continued savings growth through 2019 and to underpin this is investing in product diversification to attract a broader pool of customers. Development is underway to launch a Fixed Rate Cash ISA as well as shorter-dated notice and instant access products, the latter being the largest savings market in the UK by value. These new markets represent a clear opportunity to bring material benefit to the Group in its cost of retail funds.

Furthermore, the Group intends to start to invest in significant enhancements to its digital proposition and take advantage of the opportunities arising from a growing customer base. It will also consider the potential to offer savings accounts to businesses in the UK.

Principal risks and uncertainties

Risk overview

On an ongoing basis, the Directors carry out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity. The following are considered to be the principal risks facing the Group:

Risk	Description

Credit Risk	The risk that a counterparty will be unable to pay amounts in full when due.
Liquidity Risk	The risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.
Operational Risk	The risk of direct or indirect loss arising from a wide variety of causes associated with the Group's processes, personnel, technology and infrastructure, and from external factors other than the risks identified above.
Capital Risk	The risk that the Group will have insufficient capital resources to support the business.
Market Risk	The risk that the value of, or revenue generated from, the Group's assets and liabilities is impacted as a result of market movements, predominantly interest rates.
Conduct Risk	The potential for customers (and the business) to suffer financial loss or other detriment through the actions and decisions made by the business and its staff.
Regulatory Risk	The risk that the Group fails to be compliant with all relevant regulatory requirements.

Notes 30 to 33 to the financial statements provide further analysis of certain financial risks.

Further details of the principal risks, the changes in risk profile during the 2018 financial year and the Group's risk management framework are set out in the following section. There is also analysis of the key strategic and emerging risks which impact the Group. These include the UK's withdrawal from the European Union, the direct impacts of which are considered to be limited given the Group's UK operation and focus. The main indirect impact of the withdrawal on the Group, if disorderly, is most likely to be to credit risk and on demand for the Group's products.

Credit risk

Description

Credit risk is the risk that a counterparty will be unable to satisfy their debt servicing commitments when due. Counterparties include the consumers to whom the Group lends on a secured and unsecured basis and the small and medium size enterprises ('SME') to whom the Group lends on a secured basis as well as the market counterparties with whom the Group deals.

Mitigation

The Group manages credit risk through internal controls and through a three lines of defence model. The first line is the business operation team with the credit risk team being second line and internal audit being the third line. The Consumer Credit Risk Committee and SME Credit Committees, which are the monitoring committees for credit risk, report to the Board Risk Committee. The Board Risk Committee also approves lending authorities in respect of SME lending. Each consumer lending product has a credit risk committee which reviews business performance from new application metrics through to loss performance by business type and introducer. Policy and scorecard changes are approved at this committee.

For Real Estate Finance and Commercial Finance, lending decisions are made on an individual transaction basis, using expert judgement and assessment against criteria set out in the lending policies. Asset Finance lending is managed via a joint venture with Haydock, who operate in line with the Group's credit policies and risk appetite. Since the change in ownership of Haydock in January 2018, the Group has allowed the Asset Finance portfolio to reduce in line with contractual repayments from customers.

Exposure to credit risk is also managed in part by obtaining security. Motor Finance loans are secured against motor vehicles. Mortgages are secured against land/property and Real Estate Finance and Asset Finance loans are secured against property and tangible assets respectively. Commercial Finance advances are secured against a debtor book, inventory or property if a commercial mortgage is provided.

Management monitors the ratings of the counterparties in relation to the Group's loans and advances to banks. There is no direct exposure to the Eurozone and peripheral Eurozone countries.

Implementation of IFRS 9 on 1 January 2018 has resulted in changes to the timing of reporting credit losses. These changes have been built into Group forecasts and are considered in setting the Group's appetite for volume by sector.

Forbearance

The Group does not routinely reschedule contractual arrangements where customers default on their repayments. It may offer the customer the option to reduce or defer payments for a short period, in which cases the loan will retain the normal contractual payment due dates and will be treated the same as any other defaulting cases for impairment purposes. Forbearance arrangements in respect of Consumer Mortgages customers are described in Note 30.2.

Change – IMPROVED

Consumer Finance credit risk

Application trends, arrears and loss trends for the Retail Finance Portfolio are monitored monthly by the Credit Risk Team. Losses remain within risk appetite.

The Group's Motor Finance business has continued to grow despite a very competitive landscape. The Group has repositioned the motor finance business away from those customers that are most susceptible to an economic downturn. During the course of 2018 the "rate for risk" proposition was extended. The Group has embarked on a motor transformation plan which will see the implementation of a new application and servicing system. Linked to this, it is looking to expand the product range to include a unit stocking product, to provide short term finance to motor dealers so that they can buy stock together with a prime Hire Purchase ('HP') and Personal Contract Purchase ('PCP') product offering. The PCP offering will introduce a new risk for the Group, with potential for losses should the residual value of the vehicles at the end of the agreement be less than expected at inception of the contract.

Secure Trust Bank entered the Consumer Mortgage market in 2017, offering basic fixed term mortgage and re-mortgage products for those good quality customers with non-straightforward circumstances that struggle to meet the requirements of high street lenders. All loans are secured on the applicant's property. The Bank extended the range of products in 2018 to include interest only and part and part mortgages. In the first quarter of 2019 due to the difficult economic climate, increased competition and continued uncertainties the Group announced the decision to cease new mortgage originations until market conditions improve.

The move to IFRS 9 has enabled the core components of the Expected Credit Loss ('ECL') to be regularly reviewed and used to allow deeper analysis of credit loss drivers. ECL is a function of the Probability of Default ('PD') x Exposure at Default x Loss Given Default and has enabled the Bank to understand more granularly the elements that contribute to ECL. The Group monitors the average PD by product each month both looking at the back book and new business, as well as analysing any reasons for increases and decreases in PD (such as significant increase in credit risk). The recovery rates from debt sales and repossessions are also validated on a regular basis and presented to the Assumptions Committee. Furthermore, the ECL has been used for the stress testing that was used in the ICAAP in 2018.

Business Finance credit risk

Lending balances within the Real Estate Finance and Commercial Finance portfolios have continued to grow, with both portfolios remaining well within all risk appetite parameters. The continued focus on high quality, secured lending with strong counterparties has served the Group well to date. This has been particularly evident in the high value central London residential real estate market, where risk appetite remains substantially reduced and lending has been pared back.

Following the change in ownership of Haydock, in January 2018, the Asset Finance portfolio has continued to run-off over the course of the year. The Group continues to assess its options with regards to future opportunities within the Asset Finance market.

Thanks to the Group's continued adherence to its robust lending policies and credit appetite, alongside the significant experience within the lending teams, impairments and arrears within the Business Finance portfolios have remained minimal to date. Management continues to closely monitor the portfolios and the external events and environment that could impact on each of them.

Concentration risk

Management assesses the potential concentration risk from geographic, product and individual loan concentration. Due to the well diversified nature of its lending operations, the Group does not consider there to be a material exposure arising from concentration risk.

Liquidity risk

Description

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Group manages its liquidity in line with internal and regulatory requirements, and at least annually assesses the robustness of the liquidity requirements as part of the Group's Internal Liquidity Adequacy Assessment Process ('ILAAP').

The Group is required to meet daily cash flow requirements arising from maturing deposits and loan draw-downs, and maintains significant cash resources to meet all of these needs as they fall due. The liquidity requirements of the Group are mainly met by maintaining funds in liquid assets including the Bank of England reserve account to cover any short-term net outflow requirements. Longer term funding is also in place for structural liquidity and funding requirements.

The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, and can fund its assets at reasonable cost and without incurring unacceptable losses or risking damage to the Group's reputation through a failure to meet its obligations.

Mitigation

Risk tolerance

The Group maintains at all times liquidity resources which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due. The Group maintains a buffer of unencumbered High Quality Liquid Assets ('HQLA') that is available to meet its liquidity requirements.

The Group's Board has agreed a liquidity risk appetite to ensure that adequate liquidity resources are held to meet its Overall Liquidity Adequacy Rule ('OLAR') and the minimum Liquidity Coverage Ratio ('LCR'). This appetite ensures that adequate liquidity resources are held to withstand all known reasonable combinations of idiosyncratic and market risks for up to 90 days.

The Group assesses and formally demonstrates the adequacy of its liquidity through the ILAAP. As part of the ILAAP, the Group conducts regular and comprehensive liquidity stress testing to ensure compliance with its internal and regulatory requirements.

Structure and responsibilities for liquidity risk management

The Group has a formal governance structure in place to manage and mitigate liquidity risk on a day to day basis. The Board sets and approves the Group's liquidity risk management strategy. The Assets and Liabilities Committee ('ALCO'), comprising senior management and executives of the Group, meets monthly to review liquidity risk against set thresholds and risk indicators including early warning indicators, liquidity risk tolerance levels and ILAAP metrics. These metrics are managed on a day-to-day basis by the Group's Treasury function. The Risk Function is responsible for ensuring that appropriate risk management processes and controls are in place, and that they are sufficiently robust, so as to ensure that key risks are identified, assessed, monitored and mitigated.

Internal liquidity reporting

Liquidity metrics are monitored daily through daily liquidity reporting and on an ongoing basis through monthly ALCO meetings. Metrics are also included in the Monthly Information pack tabled at the Group's Executive Committee ('Exco'), Board Risk Committee and the Board. The aim is not to measure liquidity with a single metric but rather a range of principles and metrics which, when taken together, helps ensure that the Group's liquidity risk is maintained at an acceptable level.

The primary measure used by management to assess the adequacy of liquidity is the OLAR, which is the Board's own view of the Group's liquidity needs as set out in the Board approved ILAAP.

Communication of liquidity risk strategy, policies and practices across business lines and with the Board

The Group's ALCO is responsible for implementing and controlling the liquidity risk appetite established by the Board. ALCO monitors compliance with the Group's policies and oversees the overall strategy, guidelines and limits so that the Group's future plans and strategy can be achieved within risk appetite.

Funding strategy

The Group's funding risk appetite is to ensure that the Group has access to stable funding markets and is not reliant on any single source of funding. The Group is mainly funded by stable customer deposits and capital (including Tier 2 capital issued in 2018 that is non-callable for five years). The Group also has limited borrowings under Bank of England funding schemes but does not have other direct exposures to wholesale markets. Funding strategy is managed centrally.

Liquidity risk mitigation techniques

The Group seeks to mitigate liquidity risk through a number of strategies and processes:

- The diversification of its deposit and loan products
- Offering depositors competitive interest rates
- A stable funding profile
- Acquiring funding primarily through depositors subject to Financial Services Compensation Scheme protection
- Regular forecasting of liquidity and funding metrics
- Regular ALCO meetings reviewing risk metrics and upcoming risks
- Access to Bank of England liquidity schemes
- Holding adequate levels of High Quality Liquid Assets with a high proportion of cash in the Group's Bank of England Reserve Account.

Stress testing

An integral component of the approach to liquidity risk management is stress testing, some of which is prescriptive using detailed rules and guidance issued within prudential regulations and reported within regulatory returns. In addition to the regulatory prescribed stress testing, the Group undertakes its own stress tests. The Group uses various short and medium term forecasts to monitor future liquidity requirements and these include stress testing assumptions to identify the required levels of liquidity. Stress testing is typically performed on a daily basis and levels of liquidity under stress are forecast regularly and monitored by ALCO and management. The Board approves limits against both regulatory and internal stress testing requirements.

Contingency funding plans

If for reasons which may be beyond the business' control, the Group was to encounter a significant and sustained outflow of deposits or other stress on liquidity resource, the Recovery Plan incorporates the Group's plans to ensure that it remains sufficiently liquid to remain a viable independent financial institution during a severe liquidity stress event. Recovery Plan Early Warning Indicators and Invocation Trigger Points ('ITP') are regularly monitored and reported against.

The Recovery Plan is applied consistently with the Group's ILAAP as part of the overall liquidity risk management framework dealing with contingent funding requirements as they arise. The Group also retains access to the Bank of England liquidity insurance schemes, including the Discount Window Facility.

Change – IMPROVED

The Group has maintained its liquidity ratios in excess of regulatory requirements throughout the year and continues to hold significant levels of high quality liquid assets.

A number of enhancements were made to the liquidity management framework in 2018. These include approval of a revised standards and policy framework by ALCO, additional analysis of liquidity requirements and increased MI reporting frequencies, and the locking-in of an appropriate level of Term Funding Scheme funding. An experienced Liquidity Manager joined the Treasury team in July 2018 and towards the end of 2018, Risk appointed a Senior Manager, Prudential Risk. This role will provide additional scrutiny and oversight in respect of prudential matters including liquidity.

The stress tests performed as part of the ILAAP confirmed that the Group has sufficient funds to satisfy the OLAR requirement and there is no significant risk that liabilities cannot be met as they fall due. The Group's LCR at 31 December 2018 was significantly higher than the regulatory requirement.

Operational risk

Description
Operational Risk is the risk that the Group may be exposed to direct or indirect loss arising from inadequate or failed internal processes, personnel and succession, technology/ infrastructure, or from external factors.

The scope of Operational Risk is broad and includes Business Process, Business Continuity, Third Party, Financial Crime, Change, Human Resources, Information Security and IT Risk, including Cyber Risk.

Mitigation
The Group has adopted an Operational Risk Policy and Framework designed in accordance with the 'Principles for the Sound Management of Operational Risk' issued by the Basel Committee on Banking Supervision.

The approach ensures appropriate governance is in place to provide adequate and effective oversight of the Group's operational risk. The governance framework includes the Board Risk Committee and Group Operational Risk Committee.

The Group has a defined set of qualitative and quantitative operational risk appetite measures. Quantitative measures cover operational losses, complaints, key operational risks, systems availability and information security. The appetite measures are reported and monitored on a monthly basis.

Change – IMPROVED
The improvement of the status of this risk is driven by the Group's continued investment in resource, expertise and systems to support the Operational Risk Framework and Policy. This Framework defines and facilitates the following activities:

- A biannual Risk and Control Self Assessment process to identify, assess and mitigate risks across all business units through improvements to the control environment
- The Governance arrangements for managing and reporting these risks
- All risk appetite measures and associated thresholds and metrics
- An incident management process that defines how incidents should be managed and associated remediation, reporting and root-cause analysis.

In 2018 the Group successfully transitioned to 'The Standardised Approach' for assessing its Operational Risk capital, in recognition of the enhancements made to its framework and embedding this across the Group.

Key Risk themes of Operational Risk focus in 2018 include:

- **Supplier management** – The Group uses a number of third parties to support its IT and operational processes. The Group recognises that it is important to effectively manage these suppliers and has throughout 2018 embedded a suite of standard controls for all its material suppliers to reduce the risk of operational impacts on these critical services. This will continue to be an area of focus for 2019, particularly in relation to the Operational Resilience of the service provided by the most critical suppliers.
- **Operational and IT resilience** – Many elements of the operational risk framework support the ongoing resilience of the Group's operational and IT services, including Business Continuity Management, Disaster Recovery, Incident Management, Process Management and the Cyber strategy. However this will continue to be a key area of focus for 2019 as the Group continues to enhance its defences to any disruption to its most critical services.
- **Information security and cyber risk** – The Group has paid considerable attention to ensuring the effective management of risks arising from a failure or breach of its information technology systems that could result in customer exposure, business disruption, financial losses, or reputational damage.
- **Change Management** – The effective delivery of Change Management programmes plays an important role in meeting the Group's regulatory requirements, improving services and implementing strategic decisions. Ineffective change management processes could lead to poor customer outcomes, business disruption, financial loss and regulatory breaches. Change Management processes and governance are defined and embedded within the Group. Significant changes are planned in 2019, particularly in respect of the Motor Finance transformation, and these will be a key area of focus to ensure the Group maintains its customer and operational service standards and delivers its strategic objectives.

Capital risk

Description
Capital risk is the risk that the Group will have insufficient capital resources to meet minimum regulatory requirements and to support the business. The Group adopts a conservative approach to managing its capital and at least annually assesses the robustness of the capital requirements as part of the Group's Internal Capital Adequacy Assessment Process '(ICAAP').

Mitigation
The Group's capital management policy is focused on delivering shareholder value, in a safe and sustainable manner. The Board regularly reviews the current and forecast capital position to ensure capital resources are sufficient to support planned levels of growth.

In accordance with the EU's Capital Requirements Directive IV ('CRD IV') and the required parameters set out in the EU's Capital Requirement Regulation, the Group maintains an ICAAP which is updated at least annually. The ICAAP is a process that brings together the management framework (i.e. the policies, procedures, strategies and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted an approach to determine the level of capital the Group needs to hold. This method takes the Pillar 1 capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations delivers a sufficient capital sum adequate to cover management's assessment of anticipated risks. Where it is considered that the Pillar 1 calculations do not reflect the risk, an additional capital add-on in Pillar 2 is applied, as per the Total Capital Requirement issued by the PRA.

A complete assessment of the Group's capital requirement is contained in its Pillar 3 disclosures. Pillar 3 disclosures for the Group for the year ended 31 December 2018 are published as a separate document on the Group's website.

Change – STABLE

The Group maintained its capital ratios in excess of regulatory requirements throughout the year. At 31 December 2018, the CET1 ratio was 13.8% (2017: 16.5%), the total capital ratio was 16.3% (2017: 16.8%) and the leverage ratio was 10.0% (2017: 12.3%) on a Group consolidated basis. The CET 1 ratio has decreased due to the investment of capital to support strong lending growth.

The 2018 ICAAP incorporated IFRS 9 provisioning methodology, which accelerates the impact of losses in adverse economic conditions. The ICAAP demonstrated the Group's continued ability to meet its minimum capital requirements, even in severe stress scenarios. The Group's forecasting capability has been enhanced to cover a five year time horizon, with modelling of capital resources and requirements provided over that period, and future ICAAPs will also cover a five year period. Additional early warning indicators have been developed as part of the Recovery Plan process.

In July 2018 the Group raised its first Tier 2 capital: £25 million at 6.75%. A further £25 million was raised in October 2018 at the same price and the mechanisms have been developed to allow raising of Alternative Tier 1 capital, should such be needed. This provides the Group with additional flexibility in terms of capital options, and demonstrates the Group's ability to raise capital to fund planned growth. Capital resources increased during the year to £297.5 million as at 31 December 2018 (31 December 2017: £243.3 million) on a Group consolidated basis.

The improvements in the Group's range and size of capital resources, and to its capital management processes, leave it well positioned to continue to fund balance sheet growth while meeting increasing levels of regulatory capital buffers.

The Group has elected to adopt transitional provisions in respect of the implementation of IFRS 9, as set out by the European Banking Authority. These provisions allow the capital impact of the standard to be phased in over a five year period. Further details are provided in Note 33.

Market risk

Description

For the Group, market risk is primarily limited to interest rate risk, being the potential adverse impact on the Group's future cash flows from changes in interest rates arising from the differing interest rate risk characteristics of the Group's assets and liabilities. When interest rates change, the present value and timing of future cash flows change. This in turn changes the underlying value of the Group's assets, liabilities and off-balance sheet instruments and hence its economic value. Changes in interest rates also affect the Group's earnings by altering interest-sensitive income and expenses, affecting its net interest income.

The principal currency in which the Group operates is Sterling, although a small number of transactions are completed in US dollars, Euros and other currencies in the Commercial Finance business. The Group has no significant exposures to foreign currencies and hedges any significant currency risks to Sterling.

Mitigation

Market risk is managed by the Company's Treasury function and is overseen by the ALCO. The Group does not take significant unmatched positions and does not operate a trading book.

The Group's risk management framework, policies and procedures are regularly reviewed and updated to ensure that they accurately identify the risks that the Group faces in its business activities and are appropriate for the nature, scale and complexity of the Group's business.

The key measure the Group uses to monitor the risk is an Interest Rate Sensitivity Gap analysis which informs the Group of mismatched interest rate risk positions. The Group reports the interest rate mismatch on a monthly basis to ALCO, considering market value sensitivity as a proportion of the overall capital position of the Group, and earnings at risk as a proportion of forecast net interest income. These are assessed against 200bps and 100bps parallel shifts in rates respectively. The Group also measures exposure to basis risk and the economic value of equity. All such exposures are maintained within the risk appetite set by the Board and are monitored by ALCO.

Change – STABLE

The Group's exposure to market risk continues to be limited primarily to interest rate risk, with only modest exposures to foreign exchange risk. The Group remained within risk appetite in respect of interest rate risk throughout the year.

The increasing size of the Group's balance sheet increases the inherent level of interest rate risk, and the Group has responded by enhancing its Treasury capabilities and risk framework, with a wider range of risk measures developed and monitored by ALCO. The Group has developed its capability to use interest rate swaps to further mitigate this risk, if required, in 2019.

Conduct risk

Description
The Group defines conduct risk as the risk that the Group's products and services, and the way they are delivered, result in poor outcomes for customers, or harm to the Group. This could be as a direct result of poor or inappropriate execution of the Group's business activities or staff behaviour.
Mitigation
The Group takes a principles based approach and includes retail and commercial customers in its definition of 'customer', which covers all business units and both regulated and unregulated activities. Across the Group, conduct risk exposure is managed via monthly review and challenge of key risk indicators ('KRIs') at the Customer Focus Committee, which oversees complaints, FEEFO and Customer Service Excellence as well as conduct risk. Conduct risk management information is also reviewed at product level executive committee meetings. The Key Risk Indicators vary across the business units to reflect the relevant conduct risks; the business units' key risk indicators are aggregated for measurement against the Group's risk appetite, which is reported to the Group Executive Committee, Risk Committee and the Board.
Change – STABLE
Review of conduct risk and controls within the business units is managed through the regular cycle of risk and control self-assessments, in line with other operational risk categories. Members of the Customer Focus Committee review monthly key risk indicators across all business units, and meet on a quarterly basis for oversight and challenge of the first line activities to assure senior management that the first line is identifying conduct risks when they arise and taking appropriate actions to mitigate them. Training on conduct risk continues to be delivered to new starters, with an eLearning module completed by all staff during the year.

Regulatory risk

Description
Regulatory risk is the risk that the Group fails to be compliant with all relevant regulatory requirements. This could occur if the Group failed to interpret, implement and embed processes and systems to address regulatory requirements, emerging risks, key focus areas and initiatives or deal properly with new laws and regulations.
Mitigation
The Group seeks to manage regulatory risks through the Group-wide risk management framework. The Group Compliance and Regulatory Risk Committee is responsible for reviewing and monitoring regulatory changes, and ensuring that appropriate actions are taken, and also reviewing and approving the compliance risk management framework. Further details can be found on the Group's website: www.securetrustbank.com/our-corporate-information/risk-management
Change – STABLE
In the year ended 31 December 2018, the Group has delivered changes to address new and revised regulations and legislation that have come into force, including: Payment Services Directive 2 ('PSD2'), which impacts the Deposits business and came into force on 13 January 2018; changes to the Senior Managers and Certification Regime framework; the General Data Protection Regulation; rules on staff incentives, remuneration and performance management in consumer credit; rules relating to the assessment of creditworthiness and affordability in consumer credit; and the enhanced product disclosures required in the Insurance Distribution Directive. A number of formal projects and initiatives are in place to address forthcoming regulatory changes in 2019 including extending the Senior Managers and Certification Regime to the Group's regulated subsidiaries; European Banking Authority guidelines on security measures for operational and security risks and fraud reporting under PSD2; and improvements to operational resilience.

Strategic and emerging risks

In addition to the principal risks disclosed above, the Board considers strategic and emerging risks, including key factors, trends and uncertainties which can influence the results of the Group. These risks include the following:

Macroeconomic environment and market conditions

The Group operates exclusively within the UK and its performance is influenced by the macroeconomic environment in the UK. The economy affects demand for the Group's products, margins that can be earned on lending assets and the levels of loan impairment.

Although political and economic uncertainty has been prevalent throughout the year, the fundamental elements of the UK economy remain strong. Employment rates are at a record high and real take home pay is rising. Once current levels of uncertainty have abated, the Group expects levels of business investment, which have been held back, to increase and provide a boost to the economy.

UK withdrawal from European Union

The UK economy continued to grow in 2018. However, this growth was tempered by the uncertainty regarding the nature of the UK's exit from the European Union. Political developments led to a position where, at the end of 2018,

it was unclear whether the UK would be leaving the EU with a deal in place regarding the terms of its withdrawal, leaving with no deal in place, leaving at a later date or potentially, if a second referendum were called, not leaving in March 2019 or at all. The decision to extend the deadline and the scheduled indicative votes in the House of Commons on the preferred outcome leaves all of these options open.

The direct impact to the Group of the UK leaving the EU is limited, even in a no deal scenario. The “Partnership Pack” published by the government in December 2018 provides information in respect of cross border processes and procedures, including customs, excise and taxation arrangements, in the event of no deal. This document, and further publications issued in 2019, have not highlighted any additional direct risks to the Group. All continuing trade is within the UK, and the lending sectors that the Group operates in are not significantly reliant on cross border arrangements.

However, the indirect consequences of a no deal scenario could be more significant. If a customs border were established between the UK and the EU, then this could present a significant cost for many UK businesses. A knock on impact to consumer confidence and economic growth could dampen demand for the Group’s products, and/or result in deteriorating bad debt performance and hence higher impairment charges.

In particular, for the Group’s most significant business units:

Business Unit	Potential indirect impact of no deal exit
Real Estate Finance	Direct consequences on the procedures for the transfer, renting and mortgaging of property are considered unlikely. If there is a reduction in UK Finance providers, then contraction of supply could affect the choice and terms of funding available for investment or development projects. The timing or cost of development projects could be affected by price increases and/or shipping delays. Developers on some, particularly larger projects, may be more cautious about committing to dates and costs without scope for adjustment for the effect of a no deal withdrawal. These factors could reduce demand for the Group’s products.
Business Unit	Potential indirect impact of no deal exit
Commercial Finance	No direct consequence is expected due to this division’s UK customer base. Invoice financing has some countercyclical characteristics, though its medium term performance is directly linked to macroeconomic conditions, given lending balances are secured against the customer’s sales ledger.
Retail Finance	The key market sectors funded by Retail Finance could be impacted by rising raw material or finished goods input prices. Retailers would need to decide whether to pass on costs or absorb them into margins. Rising consumer prices would likely lead to reduced consumer confidence and demand and reduced retailer margins would likely lead to retailers halting or slowing UK expansion. These factors could reduce demand for the Group’s products. Consumer affordability issues could also impact on the Group’s profitability through increased impairment provisions.
Motor Finance	This division serves the UK used car market, which unlike the supply of new vehicles (often originating from other EU markets and attracting increased tariffs), is largely self-contained. However, subdued economic conditions and lower consumer confidence or spending power may have a potential adverse impact on used car demand, and associated demand for the Group’s financing. Affordability issues may also adversely impact the Group’s profitability through increased bad debts.

The Group considers the most significant potential impact of a no deal exit to be that on credit risk. In response to the uncertainty regarding the exit from the EU, the Group worked with external consultants to assess the likely impact of a no deal scenario on its Consumer Finance portfolios.

This assessment included stress test modelling of a no deal departure, using the Group’s ICAAP models. Assumptions used in the models were based on seven published economic models, developed by: Organisation for Economic Co-operation and Development (‘OECD’), London School of Economics (‘LSE’), Economists for Brexit (‘EfB’), HM Treasury (‘HMT’), National Institute for Economic and Social Research (‘NIESR’), Oxford Economics (‘OE’) and PwC. Review of these assumptions led to four summary scenarios: long, sharp recession; long, shallow recession; short, shallow recession; no recession. Each of these four scenarios was modelled to identify the expected impact on impairment provisions in respect of the Group’s consumer lending portfolios.

A range of outcomes was provided and reviewed by management. While the outcomes derived from the recession scenarios resulted in higher impairment provisions than those set out in the Group’s central plan, these were not at

a level that were considered to compromise the Group's viability. It was concluded that the Group did not need to change strategy in the anticipation of a potential no deal exit from the EU.

Following this work, the Group has developed additional early warning indicators that could indicate the need to change strategy, and the activities required in this eventuality to bring impairment losses back to base level. As well as existing measures relating to loan book performance, economic variables were selected which would act as lead indicators of potential issues. These include the Sterling to Euro exchange rate, movements in the FTSE 250 and government bond yields.

Model Risk and the impact of IFRS 9

As reported last year, the Group's modelling capability was significantly enhanced with the introduction of IFRS 9. The suite of models used to derive the probability of default ('PD'), loss given default ('LGD') and exposure at default ('EAD') of the Group's lending portfolios, and therefore impairment provisions, has been monitored throughout the year and found to be working effectively. Modest enhancements have been made which have reduced the need for expert credit judgement overlays to be used in addition to model output.

The Model Governance Committee was established in 2018 and now reports to Risk Committee. In addition to the IFRS 9 models, this committee has also reviewed and approved the models used to derive the effective interest rate and drive income release in respect of the Group's consumer lending portfolios, the IFRS 9 forecasting model and the models used in the Group's ICAAP.

The use of expected loss models for IFRS 9 accelerates impairment provisions and also accelerates the impact of changes, arising from loan performance or macroeconomic factors. This can introduce more volatility into reported earnings, albeit over time the underlying profit on a loan is unchanged. The improvement in the quality of the Group's Motor Finance lending and collections performance delivered a reduction in impairment losses for this portfolio in this accounting period, greater than would have been reported under the previous IAS 39 standard. A future deterioration in performance or in the UK economy more generally could have the opposite effect.

Risk management

Details of the Group's risk management framework, including risk appetite, governance arrangements and key committees, can be found on the Group's website:
www.securetrustbank.com/our-corporate-information/risk-management

Going concern and viability

Going concern

In assessing the Group as a going concern, the directors have given consideration to the factors likely to affect its future performance and development, the Group's financial position and the principal risks and uncertainties facing the Group, as set out in the Strategic Report. The Group uses various short and medium term forecasts to monitor future capital and liquidity requirements and these include stress testing assumptions to identify the headroom on regulatory compliance measures.

The directors are satisfied that the Company and the Group have adequate resources to continue to operate for the foreseeable future as going concerns. For this reason they continue to adopt the going concern basis in preparing this preliminary announcement.

Business viability

In accordance with provision C2.2 of the UK Corporate Governance Code, the directors confirm that there is a reasonable expectation that the Company and the Group will be able to continue in operation and meet their liabilities as they fall due, for the period up to 31 December 2021. The assessment of ongoing viability covers this period as it falls within the Group's five year planning horizon and is the period covered by the Group's stress testing.

Given the Group's healthy capital and liquidity position, reduction in exposure to higher risk lending, continuing growth in profit and positive trading outlook, the directors are confident of the Group's viability over the longer term. However, the inherent uncertainties regarding the economic, regulatory and market environment that the Group operates in may compromise the reliability of longer range forecasts. Given current economic uncertainties, and this being the first year in which the Group has extended its planning horizon to five years, the Board has

decided to continue to use a three year period for its assessment of viability rather than extending this over the full planning horizon.

The directors have based the assessment on:

- The latest annual budget, which contains information on the expected financial position and performance for the period to 31 December 2023 and by considering the potential impact of the principal risks facing the Group, as set out on pages 40 to 51.
- The analysis of key sensitivities, undertaken as part of the budget process, which could impact on profitability over the period covered by the budget. Assumptions made to calculate risk weighted assets and capital requirements are clearly stated and additional scenarios are modelled to demonstrate the potential impact of risks and uncertainties on capital.
- The Group's ILAAP, which uses stress scenarios to assess the adequacy of liquidity resources. The results of this scenario analysis are used to set the Group's OLAR and are also the basis of the liquidity requirements set by the PRA. The Group has maintained liquidity levels in excess of regulatory requirements throughout the year and is forecast to continue to do so.
- The Group's ICAAP, which considers a macroeconomic stress and a severe shock scenario in order to assess the adequacy of capital resources. The results of the scenario analysis are used to set the Group's internal and regulatory capital requirements. The Group has maintained capital levels in excess of regulatory requirements throughout the year and is forecast to continue to do so.
- Consideration of the other principal risks as set out on pages 40 to 51, to identify any other severe but plausible scenarios that could threaten the Group's business model, future performance, solvency or liquidity.
- Analysis of further scenarios related to the UK's withdrawal from the European Union. Further details of this analysis are provided on page 49.

In making this statement, the Board has sought input from the Audit Committee and the Risk Committee.

Directors' responsibility statement

The responsibility statement below has been prepared in connection with the full annual accounts of the Company for the year ended 31 December 2018. Certain parts of these accounts are not presented within this announcement.

The Directors are responsible for preparing the Annual Report and the Group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and parent company financial statements for each financial year. As required by the Listing Rules they are required to prepare the Group financial statements in accordance with IFRS as adopted by the EU and applicable law and have elected to prepare the parent company financial statements on the same basis.

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

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- state whether they have been prepared in accordance with IFRS as adopted by the EU;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group and parent company's financial position and financial performance;
- assess the Group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Group or the parent company or to cease operations, or have no realistic alternative but to do so.

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

Under applicable law and regulations, the Directors are also responsible for preparing a Strategic Report, Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that complies with that law and those regulations.

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

We confirm that to the best of our knowledge:

- The financial statements, prepared in accordance with IFRS as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and parent company and the undertakings included in the consolidation taken as a whole;
- The strategic report includes a fair review of the development and performance of the business and the position of the Group and parent company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- The annual report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Group and parent company's performance, business model and strategy.

This responsibility statement was approved by the Board of Directors on 27 March 2019 and is signed on their behalf by:

Paul Lynam
Chief Executive Officer

Neeraj Kapur
Chief Financial Officer

Consolidated statement of comprehensive income

	Note	2018 Total £million	2017 Continuing £million	2017 Discontinued £million	2017 Total £million
Income statement					
Interest income and similar income	4.1	169.2	141.3	8.0	149.3
Interest expense and similar charges	4.1	(35.5)	(26.7)	-	(26.7)
Net interest income	4.1	**133.7**	**114.6**	**8.0**	**122.6**
Fee and commission income	4.2	19.4	16.0	-	16.0
Fee and commission expense	4.2	(1.5)	(1.1)	-	(1.1)
Net fee and commission income	4.2	**17.9**	**14.9**	**-**	**14.9**
Operating income		**151.6**	**129.5**	**8.0**	**137.5**
Net impairment losses on loans and advances to customers		(32.4)	(33.5)	(3.4)	(36.9)
Operating expenses	5	(84.5)	(71.3)	(0.3)	(71.6)
Profit on sale of equity instruments available-for-sale		-	0.3	-	0.3
Profit before income tax		**34.7**	**25.0**	**4.3**	**29.3**
Income tax expense	7	(6.4)	(5.1)	(0.8)	(5.9)
Profit after income tax		**28.3**	**19.9**	**3.5**	**23.4**
Gain recognised on disposal after tax		-	-	0.4	0.4
Profit for the period		**28.3**	**19.9**	**3.9**	**23.8**
Other comprehensive income					
Items that will not be reclassified to the income statement					
Revaluation reserve		(0.3)	0.1	-	0.1
Taxation		0.1	-	-	-

		(0.2)	0.1	-	0.1
Items that may subsequently be reclassified to the income statement					
Available-for-sale reserve		-	2.8	-	2.8
Taxation		-	-	-	-
		-	2.8	-	2.8
Other comprehensive income for the period, net of income tax		**(0.2)**	**2.9**	**-**	**2.9**
Total comprehensive income for the period		**28.1**	**22.8**	**3.9**	**26.7**
Profit attributable to:					
Equity holders of the Company		**28.3**	**19.9**	**3.9**	**23.8**
Total comprehensive income attributable to:					
Equity holders of the Company		**28.1**	**22.8**	**3.9**	**26.7**
Earnings per share for profit attributable to the equity holders of the Company during the period (pence per share)					
Basic earnings per share	8.1	**153.2**	**107.7**	**21.1**	**128.8**
Diluted earnings per share	8.2	**150.9**	**106.4**	**20.9**	**127.3**

Consolidated statement of financial position

		At 31 December	
		2018	2017
	Note	£million	£million
ASSETS			
Cash and balances at central banks		169.7	226.1
Loans and advances to banks	10	44.8	34.3
Loans and advances to customers	11	2,028.9	1,598.3
Debt securities	14	149.7	5.0
Property, plant and equipment	15	11.0	11.5
Intangible assets	16	9.9	10.4
Deferred tax assets	18	7.9	0.6
Other assets	19	22.4	5.4
Total assets		**2,444.3**	**1,891.6**
LIABILITIES AND EQUITY			
Liabilities			
Due to banks	20	263.5	113.0
Deposits from customers	21	1,847.7	1,483.2
Current tax liabilities		4.2	3.0
Other liabilities	22	40.1	41.9
Provisions for liabilities and charges	23	1.3	1.4
Subordinated liabilities	24	50.4	-
Total liabilities		**2,207.2**	**1,642.5**
Equity attributable to owners of the parent			
Share capital	26	7.4	7.4
Share premium		81.2	81.2
Revaluation reserve		1.1	1.3
Retained earnings		147.4	159.2
Total equity		**237.1**	**249.1**
Total liabilities and equity		**2,444.3**	**1,891.6**

The financial statements on pages 134 to 216 were approved by the Board of Directors on 27 March 2019 and were signed on its behalf by:

Paul Lynam
Chief Executive Officer

Neeraj Kapur
Chief Financial Officer

Company statement of financial position

	Note	At 31 December 2018 £million	2017 £million
ASSETS			
Cash and balances at central banks		169.7	226.1
Loans and advances to banks	10	41.9	32.3
Loans and advances to customers	11	1,980.3	1,565.5
Debt securities	14	149.7	5.0
Property, plant and equipment	15	6.0	6.1
Intangible assets	16	8.1	8.5
Investments	17	3.9	3.7
Deferred tax assets	18	7.8	0.6
Other assets	19	65.6	33.2
Total assets		**2,433.0**	**1,881.0**
LIABILITIES AND EQUITY			
Liabilities			
Due to banks	20	263.5	113.0
Deposits from customers	21	1,847.7	1,483.2
Current tax liabilities		3.6	1.9
Other liabilities	22	49.1	44.4
Provisions for liabilities and charges	23	1.3	1.4
Subordinated liabilities	24	50.4	-
Total liabilities		**2,215.6**	**1,643.9**
Equity attributable to owners of the parent			
Share capital	26	7.4	7.4
Share premium		81.2	81.2
Revaluation reserve		0.6	0.5
Retained earnings		128.2	148.0
Total equity		**217.4**	**237.1**
Total liabilities and equity		**2,433.0**	**1,881.0**

The Company has elected to take the exemption under section 408 of the Companies Act 2006 not to present the parent company income statement. The profit for the parent company for the year of £20.8 million is presented in the Company statement of changes in equity.

The financial statements on pages 134 to 216 were approved by the Board of Directors on 27 March 2019 and were signed on its behalf by:

Paul Lynam
Chief Executive Officer

Neeraj Kapur
Chief Financial Officer

Registered number: 00541132

Consolidated statement of changes in equity

	Share capital	Share premium	Revaluation reserve	Available-for-sale reserve	Retained earnings	Total
	£million	£million	£million	£million	£million	£million
Balance at 1 January 2017	**7.4**	**81.2**	**1.2**	**(2.8)**	**149.0**	**236.0**
Total comprehensive income for the period						
Profit for 2017	-	-	-	-	23.8	23.8
Other comprehensive income, net of income tax						
Revaluation reserve	-	-	0.1	-	-	0.1
Available-for-sale reserve	-	-	-	2.8	-	2.8
Total other comprehensive income	-	-	**0.1**	**2.8**	-	**2.9**
Total comprehensive income for the period	-	-	**0.1**	**2.8**	**23.8**	**26.7**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Dividends	-	-	-	-	(14.0)	(14.0)
Tax on share-based payments	-	-	-	-	0.4	0.4
Total contributions by and distributions to owners	-	-	-	-	**(13.6)**	**(13.6)**
Balance at 31 December 2017 (as previously stated)	**7.4**	**81.2**	**1.3**	-	**159.2**	**249.1**
IFRS 9 transition adjustment	-	-	-	-	(25.8)	(25.8)
Balance at 1 January 2018	**7.4**	**81.2**	**1.3**	-	**133.4**	**223.3**
Total comprehensive income for the period						
Profit for 2018	-	-	-	-	28.3	28.3
Other comprehensive income, net of income tax						
Revaluation reserve	-	-	(0.3)	-	-	(0.3)
Tax on revaluation reserve	-	-	0.1	-	-	0.1
Total other comprehensive income	-	-	**(0.2)**	-	-	**(0.2)**
Total comprehensive income for the period	-	-	**(0.2)**	-	**28.3**	**28.1**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Dividends	-	-	-	-	(14.8)	(14.8)
Share-based payments	-	-	-	-	0.8	0.8
Tax on share-based payments	-	-	-	-	(0.3)	(0.3)
Total contributions by and distributions to owners	-	-	-	-	**(14.3)**	**(14.3)**
Balance at 31 December 2018	**7.4**	**81.2**	**1.1**	-	**147.4**	**237.1**

Company statement of changes in equity

	Share capital	Share premium	Revaluation reserve	Available-for-sale reserve	Retained earnings	Total
	£million	£million	£million	£million	£million	£million
Balance at 1 January 2017	**7.4**	**81.2**	**0.5**	**(2.8)**	**135.5**	**221.8**
Total comprehensive income for the period						
Profit for 2017	-	-	-	-	26.1	26.1
Other comprehensive income, net of income tax						
Available-for-sale reserve	-	-	-	2.8	-	2.8
Total other comprehensive income	-	-	-	**2.8**	-	**2.8**
Total comprehensive income for the period	-	-	-	**2.8**	**26.1**	**28.9**

Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Dividends	-	-	-	-	(14.0)	(14.0)
Tax on share-based payments	-	-	-	-	0.4	0.4
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**(13.6)**	**(13.6)**
Balance at 31 December 2017 (as previously stated)	**7.4**	**81.2**	**0.5**	**-**	**148.0**	**237.1**
IFRS 9 transition adjustment	-	-	-	-	(26.3)	(26.3)
Balance at 1 January 2018	**7.4**	**81.2**	**0.5**	**-**	**121.7**	**210.8**
Total comprehensive income for the period						
Profit for 2018	-	-	-	-	20.8	20.8
Other comprehensive income, net of income tax						
Revaluation reserve	-	-	0.1	-	-	0.1
Total other comprehensive income	-	-	**0.1**	-	-	**0.1**
Total comprehensive income for the period	-	-	**0.1**	-	**20.8**	**20.9**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Dividends	-	-	-	-	(14.8)	(14.8)
Share-based payments	-	-	-	-	0.8	0.8
Tax on share-based payments	-	-	-	-	(0.3)	(0.3)
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**(14.3)**	**(14.3)**
Balance at 31 December 2018	**7.4**	**81.2**	**0.6**	**-**	**128.2**	**217.4**

Consolidated statement of cash flows

	Note	Year ended 31 December 2018 £million	Year ended 31 December 2017 £million
Cash flows from operating activities – Continuing operations			
Profit for the year		28.3	19.9
Adjustments for:			
Income tax expense	7	6.4	5.1
Depreciation of property, plant and equipment	15	1.3	0.8
Loss on disposal of computer software		0.1	-
Amortisation of intangible assets	16	1.8	2.0
Impairment losses on loans and advances to customers		32.4	33.5
Share based compensation	27	0.8	-
Profit on sale of equity instruments available-for-sale		-	(0.3)
Cash flows from operating profits before changes in operating assets and liabilities		71.1	61.0
Changes in operating assets and liabilities:			
- net (increase)/decrease in debt securities		(144.7)	15.0
- net increase in loans and advances to customers		(494.8)	(378.3)
- net increase in other assets		(17.0)	(1.0)
- net increase in deposits from customers		364.5	331.4
- net decrease in other liabilities		(0.5)	(7.0)
Income tax paid		(6.4)	(5.1)
Net cash (outflow)/inflow from operating activities – Continuing operations		**(227.8)**	**16.0**
Cash flows from investing activities			
Sale of discontinued operation		-	37.1
Proceeds from sale of equity instruments available-for-sale		-	16.6
Purchase of property, plant and equipment	15	(1.1)	(0.8)
Purchase of computer software	16	(1.4)	(3.4)

Net cash (outflow)/inflow from investing activities – Continuing operations		**(2.5)**	**49.5**
Cash flows from financing activities			
Increase in amounts due to banks		150.0	43.0
Issue of subordinated liabilities	24	50.0	-
Subordinated liabilities issue costs	24	(0.8)	-
Dividends paid	9	(14.8)	(14.0)
Net cash inflow from financing activities – Continuing operations		**184.4**	**29.0**
Net (decrease)/increase in cash and cash equivalents – Continuing operations		**(45.9)**	**94.5**
Net increase in cash and cash equivalents – Discontinued operations		-	35.7
Cash and cash equivalents at 1 January		260.4	130.2
Cash and cash equivalents at 31 December		**214.5**	**260.4**

Proceeds from sale of equity instruments available-for-sale and net increase in amounts due to banks have been moved from operating activities to investing activities and financing activities respectively, as this better represents the nature of the underlying activity.

Company statement of cash flows

	Note	Year ended 31 December 2018 £million	Year ended 31 December 2017 £million
Cash flows from operating activities – Continuing operations			
Profit for the year		20.8	22.2
Adjustments for:			
Income tax expense		4.9	2.7
Depreciation of property, plant and equipment	15	0.7	0.4
Loss on disposal of computer software		0.1	-
Amortisation of intangible assets	16	1.6	1.0
Impairment losses on loans and advances to customers		33.1	35.1
Share based compensation	27	0.6	-
Profit on sale of equity instruments available-for-sale		-	(0.3)
Cash flows from operating profits before changes in operating assets and liabilities		61.8	61.1
Changes in operating assets and liabilities:			
- net (increase)/decrease in debt securities		(144.7)	15.0
- net increase in loans and advances to customers		(480.3)	(378.9)
- net (increase)/decrease in other assets		(32.4)	0.6
- net increase in deposits from customers		364.5	331.4
- net increase/(decrease) in other liabilities		6.0	(11.5)
Income tax paid		(4.3)	(2.6)
Net cash (outflow)/inflow from operating activities – Continuing operations		**(229.4)**	**58.1**
Cash flows from investing activities			
Sale of discontinued operation		-	37.1
Proceeds from sale of equity instruments available-for-sale		-	16.6
Purchase of property, plant and equipment	15	(0.5)	(0.3)
Purchase of computer software	16	(1.3)	(3.3)
Net cash (outflow)/inflow from investing activities – Continuing operations		**(1.8)**	**50.1**
Cash flows from financing activities			
Increase in amounts due to banks		150.0	43.0
Issue of subordinated liabilities	24	50.0	-
Subordinated liabilities issue costs	24	(0.8)	-
Dividends paid	9	(14.8)	(14.0)
Net cash inflow/(outflow) from financing activities – Continuing operations		**184.4**	**(14.0)**
Net (decrease)/increase in cash and cash equivalents		**(46.8)**	**94.2**
Net increase in cash and cash equivalents – Discontinued operations		-	35.7
Cash and cash equivalents at 1 January		258.4	128.5
Cash and cash equivalents at 31 December		**211.6**	**258.4**

Proceeds from sale of equity instruments available-for-sale and net increase in amounts due to banks have been moved from operating activities to investing activities and financing activities respectively, as this better represents the nature of the underlying activity.

Notes to the preliminary statements

1. Accounting policies

The principal accounting policies applied in the preparation of this preliminary announcement are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

1.1. Reporting entity

Secure Trust Bank PLC is a public limited company incorporated in England and Wales in the United Kingdom (referred to as 'the Company') and is limited by shares. The Company is registered in England and Wales and has the registered number 00541132. The registered address of the Company is One Arleston Way, Solihull, West Midlands, B90 4LH. The consolidated financial statements of the Company as at and for the year ended 31 December 2018 comprise Secure Trust Bank PLC and its subsidiaries (together referred to as 'the Group' and individually as 'subsidiaries'). The Group is primarily involved in banking and financial services.

1.2. Basis of presentation

The figures shown for the year ended 31 December 2018 are not statutory accounts within the meaning of section 435 of the Companies Act 2006. The statutory accounts for the year ended 31 December 2018 on which the auditors have given an unqualified audit report and did not contain an adverse statement under section 498(2) or 498(3) of the Companies Act 2006 will be delivered to the Registrar of Companies after the Annual General Meeting. The figures shown for the year ended 31 December 2017 are not statutory accounts. A copy of the statutory accounts has been delivered to the Registrar of Companies, contained an unqualified audit report and did not contain an adverse statement under section 498(2) or 498(3) of the Companies Act 2006. This announcement has been agreed with the Company's auditors for release.

The directors have assessed, in the light of current and anticipated economic conditions, the Group's ability to continue as a going concern. The directors confirm they are satisfied that the Company and the Group have adequate resources to continue in business for the foreseeable future. For this reason, they continue to adopt the 'going concern' basis for preparing accounts, as set out in the going concern and viability section of the Strategic Report starting on page 2.

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

1.3. IFRS 16 'Leases'

IFRS 16 'Leases' has been issued, and endorsed by the EU, but is not yet effective. It is effective for annual periods beginning on or after 1 January 2019, and has not been adopted early.

The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract i.e. the customer ('lessee') and the supplier ('lessor'). It replaces the previous leases standard, IAS 17 'Leases', and related interpretations.

IFRS 16 uses a new single model that applies to all leases, thus eliminating the classification of leases as either operating leases or finance leases for a lessee. Applying that model, on commencement of a lease, the lessee recognises a liability to make lease payments ('the lease liability'), an asset representing the right to use the underlying asset during the lease term ('the right-of-use asset'), and depreciation of right-of-use assets is shown separately from interest on lease liabilities in the income statement.

The lease liability is initially measured based on the net present value of the lease payments to be made over the remaining lease term, using the lessee's incremental borrowing rate as the discount rate. After commencement of the lease, the lease liability is measured on an amortised cost basis, with interest being calculated on an effective interest rate basis on the remaining balance of the liability, and lease payments reducing the lease liability when paid.

The right-of-use asset is initially measured at cost, being the amount of the initial measurement of the lease liability, adjusted for any prepaid rentals less any lease incentives plus any initial direct costs incurred by the lessee and

dismantling or restoration costs. Subsequently, the right-of-use asset is amortised on a straight-line basis over the remaining term of the lease.

Transition choices

The Group has elected to recognise the cumulative effect of implementing IFRS 16 as an adjustment to the opening balance of retained earnings at 1 January 2019. Accordingly, prior year comparatives shall not be restated. As a practical expedient, the Group will apply the new standard only to contracts that had previously been identified as leases. Therefore, the new standard will not be applied to contracts that had not previously been identified as leases.

The Group has also elected not to apply IFRS 16 to the following:

- Short term leases of 12 months or less.
- Leases for which the underlying asset is of low value.

This has resulted in the new standard only being applicable to a number of property leases and motor vehicle leases.

The Group has chosen to measure the initial right of use asset for property leases at its carrying amount as if the standard has been applied since the commencement date, but discounted using the incremental borrowing rate as at 1 January 2019. The initial right of use asset for all other leases is measured at an amount equal to the lease liability.

The Group's IFRS 16 implementation project is substantially complete, and based on assessments undertaken to date, the estimated adjustments (net of tax) arising from the adoption of IFRS 16 on 1 January 2019 are expected to be an increase in assets and liabilities of approximately £6 million, and there will be no material impact on shareholders' equity at 1 January 2019. Additionally, it is not expected that implementation of IFRS 16 will have any material impact on profit before tax for the year ended 31 December 2019.

Lessor accounting

Lessor accounting remains unchanged from IAS 17.

1.4. Consolidation

Subsidiaries

Subsidiaries are all investees controlled by the Group. The Group controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Subsidiaries are fully consolidated from the date on which control is transferred to the Group.

The acquisition method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

The parent company's investments in subsidiaries are recorded at cost less, where appropriate, provision for impairment in value.

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

Discontinued operations

Subsidiaries are de-consolidated from the date that control ceases. Discontinued operations are a component of an entity that has been disposed of, and represents a major line of business and is part of a single co-ordinated disposal plan.

1.5. IFRS 9 'Financial instruments'

The new standard, effective for the period beginning 1 January 2018, has replaced IAS 39 'Financial Instruments: Recognition and Measurement'. Adoption of the standard has resulted in new accounting policies for interest income and expense, the classification and measurement of financial instruments and the impairment of financial assets and loan commitments which are presented below.

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as noted below:

- The comparatives for the year ended 31 December 2017 have not been restated. Information presented for 2017 will not therefore be comparable. Differences in the carrying amounts of financial instruments resulting from adoption of IFRS 9 are recognised in retained earnings at 1 January 2018
- The determination of the business model within which a financial asset is held has been assessed based on facts that existed at the date of initial application and
- If a debt security had low credit risk at the date of initial application of IFRS 9, then the Group has assumed that the credit risk of the asset had not increased significantly since initial recognition. A financial asset is considered to have low credit risk when its credit risk rating is equivalent to the widely understood definition of investment grade.

Additionally, the Group has adopted the consequential amendments to IFRS 7 'Financial Instruments: Disclosures'. These disclosures have been applied to information presented for the year ended 31 December 2018 and have not been applied to comparative information.

Implementation of IFRS 9 resulted in a £25.8 million reduction in the Group's opening equity at 1 January 2018, being £32.1 million net of £6.3 million related to associated deferred tax impacts. There has been no change in the carrying amount of financial instruments on the basis of their measurement categories. All adjustments have arisen solely due to a replacement of the IAS 39 incurred loss impairment approach with an expected credit loss ('ECL') approach. Further details are provided in Note 38.

1.6. Interest income and expense

Applicable from 1 January 2018 – IFRS 9 basis

For all financial instruments measured at amortised cost, the effective interest rate method is used to measure the carrying value and allocate interest income or expense. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:

- the gross carrying amount of the financial asset or
- the amortised cost of the financial liability.

In calculating the effective interest rate for financial instruments, other than assets that were credit impaired on initial recognition, the Group estimates cash flows considering all contractual terms of the financial instrument (for example, early redemption penalty charges and broker commissions) and anticipated customer behaviour but does not consider future credit losses. For financial assets that were impaired on initial recognition (also referred to as purchased or originated credit impaired assets – 'POCI'), a credit adjusted effective interest rate is calculated using estimated future cash flows, including expected credit losses.

The calculation of the effective interest rate includes all fees received and paid that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial instrument.

For financial assets that are not considered to be credit impaired ('stage 1' and 'stage 2' assets), interest income is recognised by applying the effective interest rate to the gross carrying amount of the financial asset. For financial assets that become credit impaired subsequent to initial recognition ('stage 3' assets), interest income is recognised by applying the effective interest rate to the amortised cost of the financial asset. The credit risk of financial assets that become credit impaired are not expected to improve such that they are no longer considered credit impaired, however, if this were to occur the calculation of interest income would revert back to the gross basis. The Group's definition of stage 1, stage 2 and stage 3 assets is set out in Note 1.10.

For financial assets that were credit impaired on initial recognition (POCI assets), income is calculated by applying the credit adjusted effective interest rate to the amortised cost of the asset. For such financial assets the calculation of interest income will never revert to a gross basis, even if the credit risk of the asset improves.

Further details regarding when an asset becomes credit impaired subsequent to initial recognition is provided within Note 1.10.

Applicable prior to 1 January 2018 – IAS 39 basis

Interest income and expense was recognised in the income statement for all instruments measured at amortised cost using the effective interest method.

The effective interest method calculates the amortised cost of a financial asset or a financial liability and allocates the interest income or interest expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group takes into account all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

1.7. Net fee and commission income

Fees and commission income and expenses that are an integral part of the effective interest rate of a financial instrument are included in the effective interest rate and presented in the Statement of Comprehensive Income as interest income or expense.

Fees and commission income that are not considered an integral part of the effective interest rate of a financial instrument are recognised when the Group satisfies performance obligations by transferring promised services to customers.

1.8. Financial assets and financial liabilities

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all of the risks and rewards of ownership. There have not been any instances where assets have only been partially derecognised. The Group derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

Amortised cost measurement

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

Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of assets and liabilities traded in active markets are based on current bid and offer prices respectively. If the market for a financial instrument is not active the Group establishes a fair value by using an appropriate 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.

Applicable from 1 January 2018 – IFRS 9 basis

Financial Assets

The Group classifies its financial assets at inception into three measurement categories; 'amortised cost', 'fair value through other comprehensive income' ('FVOCI') and 'fair value through profit and loss' ('FVTPL'). A financial asset is measured at amortised cost if both the following conditions are met and it has not been designated as at FVTPL:

- the asset is held within a business model whose objective is to hold the asset to collect its contractual cash flows; and
- the contractual terms of the financial asset give rise to cash flows on specified dates that represent payments of solely principal and interest on the outstanding principal amount.

The Group's current business model for all financial assets is to hold to collect contractual cash flows and all assets held give rise to cash flows on specified dates that represent solely payments of principal and interest on the outstanding principal amount. All the Group's assets are therefore currently classified as amortised cost. Loans are recognised when funds are advanced to customers and are carried at amortised cost using the effective interest method.

The amortised cost of an instrument is the amount at which it is measured at initial recognition, less principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, less any expected credit loss allowance. The gross carrying amount of a financial asset is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

A debt instrument would be measured at FVOCI only if both the below conditions are met and it has not been designated as FVTPL:

- the asset is held within a business model whose objective is achieved by both collecting its contractual cash flows and selling the financial asset; and
- the contractual terms of the financial asset give rise to cash flows on specified dates that represent payments of solely principal and interest on the outstanding principal amount.

The Group currently has no financial instruments classified as FVOCI.

On initial recognition of an equity investment that is not held for trading, the Group may irrevocably elect to present subsequent changes in fair value in OCI. This election would be made on an investment by investment basis. The Group currently holds no such investments.

All other assets are classified as FVTPL. The Group currently has no financial assets classified as FVTPL.

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Group changes its business model for managing financial assets. The Group has not reclassified any financial assets during the reporting period.

Deposits from customers

The Group classifies its financial liabilities as measured at amortised cost. Such financial liabilities are recognised when cash is received from depositors and carried at amortised cost using the effective interest method.

Other financial liabilities

The subordinated liabilities comprise of 6.75% Fixed Rate Reset Callable Subordinated Notes due 2028 (the 'Notes'):

- The notes are redeemable for cash at their principal amount on a fixed date.
- The Company has a call option to redeem the securities early in the event of a 'tax event' or a 'capital disqualification event', which is at the full discretion of the Company.
- Interest payments are paid at six monthly intervals and are mandatory.
- The notes give the holders rights to the principal amount on the notes, plus any unpaid interest, on liquidation. Any such claims are subordinated to senior creditors, but rank pari passu with holders of other subordinated obligation and in priority to holders of share capital.

The above features provide the issuer with a contractual obligation to deliver cash or another financial asset to the holders, and therefore the notes are classified as financial liabilities. Further information in respect of the Notes is provided in Note 24.

Transactions costs that are directly attributable to the issue of the notes and are incremental costs that would not have been incurred if the notes had not been issued are deducted from the financial liability, and expensed to the income statement on an effective interest rate basis over the expected life of the notes.

The fair value of other liabilities repayable on demand is assumed to be the amount payable on demand at the statement of financial position date.

The Group has not elected to measure any financial liabilities at fair value.

Applicable prior to 1 January 2018 – IAS 39 basis

The Group classified its financial assets as fair value through profit or loss, loans and receivables, held-to-maturity or available-for-sale and classifies its financial liabilities as other financial liabilities. Management determines the classification of its investments at initial recognition. A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

(a) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. Loans are recognised when the funds are advanced to customers. Loans and receivables are carried at amortised cost using the effective interest method (see below).

(b) Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. Held-to-maturity investments are carried at amortised cost using the effective interest method.

(c) Available-for-sale

Available-for-sale ('AFS') investments are those not classified as another category of financial assets. These comprised equity investments in a quoted company. They may be sold in response to liquidity requirements or equity price movements. AFS investments are initially recognised at cost, which is considered as the fair value of the investment including any acquisition costs. AFS investments are subsequently measured at fair value in the statement of financial position. Fair value changes on the AFS securities are recognised in the statement of other comprehensive income and in equity (AFS reserve), until the investment is sold or impaired. Once sold or impaired, the cumulative gains or losses previously recognised in the AFS reserve are recycled to the income statement.

(d) Other financial liabilities

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

1.9. Foreign currencies

Transactions in foreign currencies are initially recorded at the rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated into the Company's functional currency at the rates prevailing on the balance sheet date. Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are included in the income statement for the period.

1.10. Impairment of financial assets and loan commitments

Applicable from 1 January 2018 – IFRS 9 basis

The Group recognises loss allowances for ECLs on all financial assets carried at amortised cost, including lease receivables and loan commitments.

Credit loss allowances are measured as an amount equal to lifetime ECL, except for the following assets, for which they are measured as 12 month ECL:

- Financial assets determined to have low credit risk at the reporting date

- Financial assets which have not experienced a significant increase in credit risk since their initial recognition; and
- Financial assets which have experienced a significant increase in credit risk since their initial recognition but have subsequently met the Group's cure policy, as set out below.

Such assets are classified as stage 1 assets.

Assets which have experienced a significant increase in credit risk since their initial recognition and have not subsequently met the Group's cure policy are classified as stage 2 assets. The Group's definitions of a significant increase in credit risk and default are set out below.

A financial asset is considered to have low credit risk when its credit risk rating is equivalent to the widely understood definition of 'investment grade' assets. The Group has assessed all its debt securities, which represents UK Treasury bills, and loans held in STB Leasing Limited, for which credit risk is retained by its partner RentSmart, to be low credit risk.

Definition of default/credit impaired financial assets (Stage 3 loans)

At each reporting date, the Group assesses whether financial assets carried at amortised cost are credit impaired (stage 3). A financial asset is considered to be credit impaired when an event or events that have a detrimental impact on estimated future cash flows have occurred. Evidence that a financial asset is credit impaired includes the following observable data:

- Initiation of bankruptcy proceedings
- Notification of bereavement
- Identification of loan meeting debt sale criteria or
- Initiation of repossession proceedings.

In addition, a loan that is 90 days or more past due is considered credit impaired for all portfolios. The credit risk of financial assets that become credit impaired are not expected to improve such that they are no longer considered credit impaired.

For Commercial Finance facilities that do not have a fixed term or repayment structure, evidence that a financial asset is credit impaired includes:

- The client ceasing to trade; and
- Unpaid debtor balances that are dated at least 6 months past their normal recourse period.

Significant increase in credit risk (Stage 2 loans)

For Consumer Finance, the credit risk of a financial asset is considered to have experienced a significant increase in credit risk since initial recognition where there has been a significant increase in the remaining lifetime probability of default of the asset. The Group may also use its expert credit judgement and where possible relevant historical and current performance data, including bureau data, to determine that an exposure has undergone a significant increase in credit risk.

For Business Finance, the credit risk of a financial asset is considered to have experienced a significant increase in credit risk where certain early warning indicators apply. These indicators may include notification of county court judgements or, specifically for the Real Estate Finance portfolio, cost over-runs and timing delays experienced by borrowers.

As a backstop, the Group considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due for all portfolios.

Performing assets which have experienced a significant increase in credit risk since initial recognition are reclassified from stage 1, for which loss allowances are measured at an amount equal to 12 month ECL, to stage 2, for which ECL is measured as lifetime ECL.

Cure policy

The credit risk of a financial asset may improve such that it is no longer considered to have experienced a significant increase in credit risk if it meets the Group's cure policy. The Group's cure policy for all portfolios requires sufficient payments to be made to bring an account back within less than 30 days past due and for such payments to be maintained for six consecutive months.

The Group has determined stage 3 to be an absorbing state. Once a loan is in default it is not therefore expected to cure back to stage 1 or 2.

Calculation of expected credit loss

ECLs are probability weighted estimates of credit losses which are measured as the present value of all cash shortfalls. Specifically, this is the difference between the contractual cash flows due and the cash flows expected to be received, discounted at the original effective interest rate or, for portfolios purchased outside of the Group by Debt Managers (Services) Limited, the credit adjusted effective interest rate. For undrawn loan commitments ECL is measured as the difference between the contractual cash flows due if the commitment is drawn and the cash flows expected to be received.

Lifetime ECL is the ECL that results from all possible default events over the expected life of a financial asset.

12 month ECL is the portion of lifetime ECL that results from default events on a financial asset that are possible within 12 months after the reporting date.

ECLs are calculated by multiplying three main components; the probability of default ('PD'), exposure at default ('EAD') and loss given default ('LGD') discounted at the original effective interest rate of an asset. These variables are derived from internally developed statistical models and historical data, adjusted to reflect forward looking information and are discussed in turn further below. Management adjustments are made to modelled output to account for situations where known or expected risk factors have not been considered in the modelling process.

Probability of default (PD) and credit risk grades

Credit risk grades are a primary input into the determination of the PD for exposures. The Group allocates each exposure to a credit risk grade at origination and at each reporting period to predict the risk of default. Credit risk grades are determined using qualitative and quantitative factors that are indicative of the risk of default e.g. arrears status and loan applications scores. These factors vary for each loan portfolio. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade. In monitoring exposures information such as payment records, request for forbearance strategies and forecast changes in economic conditions are considered for Consumer Finance. Additionally, for Business Finance information obtained during periodic client reviews, for example audited financial statements, management accounts, budgets and projections are considered, with particular focus on key ratios, compliance with covenants and changes in senior management teams.

Exogenous, Maturity, Vintage ('EMV') modelling is used in the production of forward looking lifetime PDs. This method entails modelling the effects of external (exogenous) factors against cohorts of lending and their time on the books creating a clean relationship to best demonstrate the movement in default rates as macroeconomic variables are changed. These models are extrapolated to provide PD estimates for the future, based on forecasted economic scenarios.

Exposure at default (EAD)

EAD represents the expected exposure in the event of a default. EAD is derived from the current exposure and potential changes to the current amount allowed under the terms of the contract, including amortisation overpayments and early terminations. The EAD of a financial asset is its gross carrying amount. For loan commitments the EAD includes the amount drawn as well as potential future amounts that may be drawn under the terms of the contract, estimated based on historical observations and forward looking forecasts.

For Commercial Finance facilities that have no specific term, an assumption is made that accounts close 36 months after the reporting date for the purposes of measuring lifetime ECL. This assumption is based on industry experience of average client life. These facilities do not have a fixed term or repayment structure but are revolving and increase or decrease to reflect the value of the collateral i.e. receivables or inventory. The Group can cancel the facilities with immediate effect, although this contractual right is not enforced in the normal day to day management of the

facility. Typically, demand would only be made on failure of a client business or in the event of a material event of default, such as a fraud. In the normal course of events, the Group's exposure is recovered through receipt of remittances from the client's debtors rather than from the client itself.

The ECL for such facilities is estimated taking into account the credit risk management actions that the Group expects to take to mitigate against losses. These include a reduction in advance rate and facility limits or application of reserves against a facility so as to improve the likelihood of full recovery of exposure from the debtors. Alternative recovery routes mitigating ECL would include refinance by another funding provider, taking security over other asset classes or secured personal guarantees from the client's principals.

Loss given default (LGD)

LGD is the magnitude of the likely loss in the event of default. This takes into account recoveries either through curing or, where applicable, through auction sale of repossessed collateral and debt sale of the residual shortfall amount. For loans secured by retail property, loan-to-value ratios are key parameters in determining LGD. LGDs are calculated on a discounted cash flow basis using the financial instrument's origination effective interest rate as the discount factor.

Incorporation of forward looking data

The Group incorporates forward looking information into both its assessment of whether the credit risk of a financial asset has increased significantly since initial recognition and its measurement of expected credit loss. This is achieved by developing a number of potential economic scenarios and modelling expected credit losses for each scenario. To ensure material non-linear relationships between economic factors and credit losses are reflected in the calculation of ECL a deeper stress scenario is used as one of these scenarios. The outputs from each scenario are combined using the estimated likelihood of each scenario occurring to derive a probability weighted expected credit loss. The four scenarios adopted and probability weighting applied are approved by the Assumptions Committee and are set out in Note 2.

The Group has considered which economic variables impact credit risk and credit losses. The key drivers of credit risk and credit losses included in the macroeconomic scenarios for all portfolios, with the exception of Real Estate Finance, have been identified as annual unemployment rate growth and annual house price index growth. In addition, for Asset Finance and Commercial Finance, changes to the consumer price index are also included in the macro economic scenarios. For the Real Estate Finance portfolio the key drivers have been identified as unemployment rate growth and Bank of England base rates. Base case assumptions applied for each of these variables, with the exception of the annual house price index growth, have been sourced from external consensus forecasts. The annual house price index is assumed to increase 2% per annum until December 2021 and 4% thereafter. Further details of the assumptions applied to other scenarios is presented in Note 2.

Presentation of loss allowance

Loss allowances for ECL are presented in the statement of financial position as follows with the loss recognised in the statement of comprehensive income:

- Financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets.
- Other loan commitments: generally, as a provision.

For the Real Estate Finance and Commercial Finance portfolios, where a loan facility is agreed that includes both drawn and undrawn elements and the Group cannot identify the ECL on the loan commitment separately, a combined loss allowance for both drawn and undrawn components of the loan is presented as a deduction from the gross carrying amount of the drawn component, with any excess of the loss allowance over the gross drawn amount presented as a provision.

A customer's account may be modified to assist customers who are in or have recently overcome financial difficulties and have demonstrated both the ability and willingness to meet the current or modified loan contractual payments. Where the terms of a financial asset have been modified and the modification has not resulted in derecognition, the expected cash flows arising from the modified financial asset are included in calculating any cash shortfalls from the existing asset. Any change in the carrying value of the modified asset would be recognised immediately in the income statement.

When a loan is uncollectible, it is written off against the related ECL allowance. Such loans are written off after all necessary procedures have been completed and the amount of the loss has been determined.

Motor voluntary termination provision

In addition to recognising allowances for ECLs the Group holds a provision for voluntary terminations ('VT') for all Motor Finance financial assets. VT is a legal right provided to customers who take out hire purchase agreements. The provision is calculated by multiplying the probability of VT of an asset by the expected shortfall on VT discounted back at the original effective interest rate of the asset. VT allowances are not held against loans in default (stage 3 loans).

The VT provision is presented in the statement of financial position as a deduction from the gross carrying amount of Motor Finance assets with the loss recognised in the statement of comprehensive income.

Applicable prior to 1 January 2018 – IAS 39 basis

Assets carried at amortised cost

On an ongoing basis the Group assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. Objective evidence is the occurrence of a loss event, after the initial recognition of the asset, that impacts on the estimated future cash flows of the financial asset or group of financial assets, and can be reliably estimated.

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include, but are not limited to, the following:

- Delinquency in contractual payments of principal or interest;
- Breach of financial covenants or contractual obligations;
- Cash flow difficulties experienced by the borrower; and
- Initiation of bankruptcy proceedings.

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

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

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the income statement.

Business Finance

In assessing objective evidence of a loss event for business loans, the following factors are considered:

- If any contractual repayment date has been missed;
- Covenant breaches; and
- In Commercial Finance, a loan may be considered for potential impairment if the financial prospects of the borrower's customers deteriorates.

Consumer Finance

For Consumer loans, cash flows are estimated based on past experience combined with the Group's view of the future considering the following factors:

- The Group's exposure to the customer;
- Based on the number of days in arrears at the statement of financial position date, the likelihood that a loan will progress through the various stages of delinquency and ultimately be written off; and
- The amount and timing of expected receipts and recoveries.

Modification of loans

A customer's account may be modified to assist customers who are in or have recently overcome financial difficulties and have demonstrated both the ability and willingness to meet the current or modified loan contractual payments. Loans that have renegotiated or deferred terms, resulting in a substantial modification to the cash flows, are no longer considered to be past due but are treated as new loans recognised at fair value, provided the customers comply with the renegotiated or deferred terms.

1.11. Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of the acquisition over the fair value of the Group's share of the net identifiable assets acquired at the date of acquisition. Goodwill is held at cost less accumulated impairment losses and is deemed to have an infinite life.

The Group reviews the goodwill for impairment at least annually or when events or changes in economic circumstances indicate that impairment may have taken place. Impairment losses are recognised in the income statement if the carrying amount exceeds the recoverable amounts.

(b) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software.

Costs associated with developing or maintaining computer software programs are recognised as an expense as incurred unless the technical feasibility of the development has been demonstrated, and it is probable that the expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance, in which case they are capitalised.

These costs are amortised on the basis of the expected useful lives, which are between three to ten years.

(c) Other intangibles

The acquisition of subsidiaries was accounted for in accordance with IFRS 3 'Business Combinations', which requires the recognition of the identifiable assets acquired and liabilities assumed at their acquisition date fair values. As part of this process, it was necessary to recognise certain intangible assets which are separately identifiable and which are not included on the acquiree's balance sheet, which are amortised over their expected useful lives, as set out in Note 16.

1.12. Property, plant and equipment

Property is held at its revalued amount, being its fair value at the date of valuation less any subsequent accumulated depreciation. Revaluations are carried out annually at the reporting date, and movements are recognised in Other Comprehensive Income, net of any applicable deferred tax.

Plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Pre-installed computer software licences are capitalised as part of the computer hardware it is installed on. Depreciation is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, which are subject to regular review:

Land	not depreciated
Freehold buildings	50 years
Leasehold improvements	shorter of life of lease or 7 years
Computer equipment	3 to 5 years
Other equipment	5 to 10 years

Gains and losses on disposals are determined by comparing proceeds with carrying amounts. These are included in the income statement.

1.13. Leases

(a) As a lessor

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

(b) As a lessee

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

1.14. Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise cash in hand and demand deposits, and cash equivalents comprise highly liquid investments which are convertible into cash with an insignificant risk of changes in value with a maturity of three months or less at the date of acquisition, including certain loans and advances to banks and short-term highly liquid debt securities.

1.15. Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issuance costs. Any amounts received over nominal value are recorded in the share premium account, net of direct issuance costs. Costs associated with the listing of shares are expensed immediately.

1.16. Employee benefits

(a) Post-retirement obligations

The Group contributes to defined contribution schemes for the benefit of certain employees. The schemes are funded through payments to insurance companies or trustee-administered funds at the contribution rates agreed with individual employees. The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense when they are due. There are no post-retirement benefits other than pensions.

(b) Share-based compensation

The fair value of equity settled share-based payment awards are calculated at grant date and recognised over the period in which the employees become unconditionally entitled to the awards (the vesting period). The amount is recognised as personnel expenses in the income statement, with a corresponding increase in equity. Further details of the valuation methodology is set out in Note 27.

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

1.17. Taxation

Current income tax which is payable on taxable profits is recognised as an expense in the period in which the profits arise.

Deferred tax is provided in full on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the statement of financial position date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax

entities, when they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

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

1.18. Dividends

Final dividends on ordinary shares are recognised in equity in the period in which they are approved by Shareholders. Interim dividends on ordinary shares are recognised in equity in the period in which they are paid.

2. Critical accounting judgements and key sources of estimation uncertainty

2.1 Judgements

No critical judgements have been identified.

2.2 Key sources of estimation uncertainty

Estimations which could have a material impact on the Group's financial results and are therefore considered to be key sources of estimation uncertainty are outlined below.

2.2.1 Impairment losses on loans and advances to customers

As discussed in Note 1.10 ECLs are calculated by multiplying three main components: the PD, EAD and LGD. These variables are derived from internally developed statistical models and historical data, adjusted to reflect forward looking information. The determination of both the PD and LGD require estimation which is discussed further below.

2.2.2. Probability of default (PD)

As set out in Note 1.10 Exogenous, Maturity, Vintage (EMV) modelling is used in the production of forward looking lifetime PDs in the calculation of ECLs. As the Group's performance data does not go back far enough to capture a full economic cycle, the proxy series of the quarterly rates of write offs for UK unsecured lending data is used to build an economic response model ('ERM') to incorporate the effects of recession.

The portfolios for which external benchmark information represents a significant input into the measurement of ECL are Real Estate Finance, Asset Finance and Commercial Finance. The benchmarks used for all three portfolios are Standard & Poor's Ratings and Bank of England UK Possessions as proxy data for ERM.

With the exception of the Motor Finance portfolio, sensitivity to reasonably possible changes in PD is not considered to result in material changes in the ECL allowance. The Motor Finance portfolio has seen improvements in PD since implementation of IFRS 9 due to the Group's move away from writing subprime Motor loans in January 2017 and improvements in the collections process. During the year the Motor Finance PD reduced by 9.6% resulting in an £2.3 million reduction in ECL. A 10% change in the PD for Motor Finance would impact the ECL allowance by £1.8 million.

The composition of the Retail Finance portfolio remains stable with minimal movement in PDs and the ECL allowance held for the Business Finance, Consumer Mortgages and Other portfolios remains low. Reasonably possible changes in the PD for these portfolios are not considered to result in a material change in the ECL allowance.

2.2.3 Loss given default (LGD)

The Group's policy for the determination of LGD is outlined in Note 1.10.

With the exception of the Motor Finance portfolio, the sensitivity of the ECL allowance to reasonably possible changes in the LGD is not considered material. For the Motor Finance portfolio a 10% change in the LGD is considered reasonably possible due to historic data showing movements in vehicle collection rates once a loan is in repossession stage. A 10% change in the vehicle recovery rate assumption element of the LGD for Motor Finance would impact the ECL allowance by £1.6 million. Vehicle collection rates and proceeds received on sale of vehicles at auction remained broadly stable over 2018, and therefore there was no material change to ECL as a result of LGD changes.

2.2.4 Incorporation of forward looking data

The Group incorporates forward looking information into both its assessment of whether the credit risk of a financial asset has increased significantly since initial recognition and its measurement of expected credit loss by developing a

number of potential economic scenarios and modelling expected credit losses for each scenario. Further detail on this process is provided in Note 1.10. Whilst not material and therefore not required by IAS 1, the Group has included the disclosure below as it is considered useful to readers of the Annual Report and Accounts.

The macro economic scenarios and weightings applied on adoption of IFRS 9 on 1 January 2018 and at 31 December 2018 are summarised below:

Scenario	Derivation	Weighting 31 December 2018	Weighting 1 January 2018
Base case	Derived from external consensus forecasts and used in the Group's strategic planning and budgeting processes.	65%	80%
Benign case	Assumes macroeconomic variables will move with a more positive trajectory than the base case.	10%	5%
Stressed case	Management's assessment, based on historic data, of an adverse scenario that could occur once every 7 to 8 years.	20%	10%
Deeper stress	Based on the scenario used by the PRA for the H1 2018 ICAAP. This can be found on the Bank of England's website: www.bankofengland.co.uk	5%	5%

Weightings applied to the macro economic scenarios were reviewed at the October 2018 Assumptions Committee and reconfirmed at the January 2019 Assumptions Committee. After taking into consideration current economic conditions and emerging industry practice it was agreed to revise the weightings applied. The impact of this change was £0.4 million increase to the Group's ECL.

The sensitivity of the ECL allowance to reasonably possible changes in macro-economic scenario weighting is presented below:

	Increase in stressed case weighting by 5% and reduction in base case £million	Increase in deeper stress case weighting by 5% and reduction in base case £million
Motor Finance	0.1	0.3
Retail Finance	0.1	0.8

The sensitivity of other portfolios to reasonably possible changes in macro-economic scenario weightings is not considered material.

3. Operating segments

The Group is organised into seven operating segments, which consist of the different products available, disclosed below:

Business Finance

1) Real Estate Finance: residential and commercial investment and development loans secured by UK real estate.
2) Asset Finance: loans to small and medium sized enterprises to acquire commercial assets.
3) Commercial Finance: invoice discounting and invoice factoring.

Consumer Finance

4) Motor Finance: hire purchase agreements secured against the vehicle being financed.
5) Retail Finance: point of sale unsecured finance for in-store and online retailers.
6) Debt Management: debt collection.

Consumer Mortgages

7) Residential mortgages for the self-employed, contract workers, those with complex income and those with a recently restored credit history, sold via select mortgage intermediaries.

Other

Other includes principally OneBill and RentSmart. OneBill has been closed to new customers since 2009.

Discontinued operations

Personal Lending: Unsecured consumer loans sold to customers via broker aggregators and business partners.

Currently, the Debt Management and Consumer Mortgages segments both fall below the quantitative threshold for separate disclosure, but the directors consider that they represent sufficiently distinct types of business to merit

separate disclosure. The prior year figures have been restated accordingly, in order to separately disclose Debt Management.

Management review these segments by looking at the income, size and growth rate of the loan books, impairments and customer numbers. Except for these items no costs or balance sheet items are allocated to the segments.

	Interest income and similar income £million	Fee and commission income £million	Revenue from external customers £million	Net impairment losses on loans and advances to customers £million	Loans and advances to customers £million
31 December 2018					
Business Finance					
Real Estate Finance	41.1	0.1	**41.2**	0.5	**769.8**
Asset Finance	6.6	-	**6.6**	2.2	**62.8**
Commercial Finance	5.5	7.9	**13.4**	-	**194.7**
Consumer Finance					
Retail Finance	58.7	4.1	**62.8**	19.3	**597.0**
Motor Finance	47.4	1.1	**48.5**	11.3	**276.4**
Debt Management	6.1	0.9	**7.0**	-	**32.3**
Consumer Mortgages	1.5	-	**1.5**	0.2	**84.7**
Other	2.3	5.3	**7.6**	(1.1)	**11.2**
	169.2	**19.4**	**188.6**	**32.4**	**2,028.9**

	Interest income and similar income £million	Fee and commission income £million	Revenue from external customers £million	Net impairment losses on loans and advances to customers £million	Loans and advances to customers £million
31 December 2017					
Business Finance					
Real Estate Finance	32.1	0.2	**32.3**	(0.2)	**580.8**
Asset Finance	8.5	-	**8.5**	1.0	**116.7**
Commercial Finance	2.5	4.7	**7.2**	0.1	**126.5**
Consumer Finance					
Retail Finance	47.5	3.2	**50.7**	13.8	**452.3**
Motor Finance	46.2	0.9	**47.1**	20.8	**274.6**
Debt Management	3.3	1.6	**4.9**	-	**15.6**
Consumer Mortgages	0.1	-	**0.1**	-	**16.5**
Other	1.1	5.4	**6.5**	(2.0)	**15.3**
Continuing operations	141.3	16.0	**157.3**	33.5	**1,598.3**
Discontinued operations					
Personal Lending	8.0	-	**8.0**	3.4	-
	149.3	**16.0**	**165.3**	**36.9**	**1,598.3**

The 'other' segment above includes products which are individually below the quantitative threshold for separate disclosure and fulfils the requirement of IFRS 8.28 by reconciling operating segments to the amounts reported in the financial statements.

Funding costs and operating expenses are not aligned to operating segments for day to day management of the business, so they cannot be allocated on a reliable basis. Accordingly, profit by operating segment has not been disclosed.

All of the Group's operations are conducted wholly within the United Kingdom and geographical information is therefore not presented.

4. Operating income

4.1 Net interest income

	2018 £million	2017 £million
Loans and advances to customers	167.4	140.7
Cash and balances at central banks	1.0	0.4
Debt securities	0.8	-
Loans and advances to banks	-	0.2
Interest income and similar income	**169.2**	**141.3**
Deposits from customers	(32.8)	(26.7)
Due to banks	(1.5)	-
Subordinated liabilities	(1.2)	-
Interest expense and similar charges	**(35.5)**	**(26.7)**
Net interest income	**133.7**	**114.6**

The net interest income shown above excludes £8.0 million in 2017 of interest on loans and advances to customers in respect of discontinued operations, as shown in the income statement as set out on page 134.

4.2 Net fee and commission income

	2018 £million	2017 £million
Fee and disbursement income	16.3	12.4
Commission income	2.0	2.7
Other income	1.1	0.9
Fee and commission income	**19.4**	**16.0**
Other expenses	(1.5)	(1.1)
Fee and commission expense	**(1.5)**	**(1.1)**
Net fee and commission income	**17.9**	**14.9**

Fees and commissions income consists principally of the following:

- weekly and monthly fees from the OneBill product
- associated insurance commissions and commissions earned on debt collection activities in DMS
- discounting, service and arrangement fees in Commercial Finance, and
- account management and administration fees from retailers in Retail Finance.

Fee and commission expenses consist primarily of fees payable in respect of Motor Finance.

5. Operating expenses

	Total 2018 £million	Continuing 2017 £million	Discontinued 2017 £million	Total 2017 £million
Staff costs, including those of directors:				
Wages and salaries	39.1	33.8	0.3	34.1
Social security costs	6.0	4.2	-	4.2
Pension costs	1.4	1.2	-	1.2
Share based payment transactions	0.8	(0.2)	-	(0.2)
Depreciation of property, plant and equipment (Note 15)	1.3	0.8	-	0.8
Amortisation of intangible assets (Note 16)	1.8	2.0	-	2.0
Operating lease rentals	1.7	1.5	-	1.5
Other administrative expenses	32.4	28.0	-	28.0
Total operating expenses	**84.5**	**71.3**	**0.3**	**71.6**

As described in Note 3, operating expenses are not aligned to operating segments for day-to-day management of the business, so they cannot be allocated on a reliable basis. Accordingly, discontinued operating expenses above relates only to those costs that are directly attributable to the discontinued business.

Remuneration of the auditor and its associates, excluding VAT, was as follows:

	2018	2017
	£'000	£'000
Fees payable to the Company's auditor for the audit of the Company's annual accounts	233	270
Fees payable to the Company's auditor for other services:		
The audit of the Company's subsidiaries, pursuant to legislation	37	68
Audit related assurance services	-	100
Other assurance services	95	62
All other non-audit services	140	39
	505	**539**

Other assurance services related to the half year review.

All other non-audit services related to profit certification, accounting opinion relating to the issue of the subordinated liabilities, recovery plan support, review of share scheme documentation and Financial Services Compensation Scheme reporting health check (2017: profit certification, work relating to entry into the Term Funding Scheme and advice on a potential corporate acquisition).

6. Average number of employees

	2018	2017
	Number	Number
Directors	7	8
Management	88	116
Administration	766	610
	861	**734**

During the year, the Group updated its grading and pay structure. The analysis above is therefore not directly comparable between 2017 and 2018.

7. Income tax expense

	Total	Continuing operations	Discontinued operations	Total
	2018	2017	2017	2017
	£million	£million	£million	£million
Current taxation				
Corporation tax charge - current year	7.3	5.5	0.8	6.3
Corporation tax charge - adjustments in respect of prior years	0.3	-	-	-
	7.6	**5.5**	**0.8**	**6.3**
Deferred taxation				
Deferred tax charge - current year	(1.0)	(0.5)	-	(0.5)
Deferred tax charge - adjustments in respect of prior years	(0.2)	0.1	-	0.1
	(1.2)	**(0.4)**	**-**	**(0.4)**
Income tax expense	**6.4**	**5.1**	**0.8**	**5.9**
Tax reconciliation				
Profit before tax	34.7	25.0	4.3	29.3
Tax at 19.00% (2017: 19.25%)	6.6	4.8	0.8	5.6
Permanent differences	-	0.2	-	0.2
Banking surcharge	0.3	-	-	-
Rate change on deferred tax assets	(0.6)	-	-	-
Prior period adjustments	0.1	0.1	-	0.1
Income tax expense for the year	**6.4**	**5.1**	**0.8**	**5.9**

The Government substantively enacted a reduction in the main rate of UK corporation tax from 20% to 19% (effective from 1 April 2017) and a further reduction to 17% (effective 1 April 2020). The Government also

introduced an 8% surcharge on the profits of banking companies in excess of £25 million effective from 1 January 2016 that is reflected in the 2018 tax charge and reconciliation.

8. Earnings per ordinary share

8.1 Basic

Basic earnings per ordinary share are calculated by dividing the profit attributable to equity holders of the parent by the weighted average number of ordinary shares as follows:

	2018	2017
Profit attributable to equity holders of the parent (£ millions)		
Continuing operations	28.3	19.9
Discontinued operations	-	3.9
	28.3	**23.8**
Weighted average number of ordinary shares (number)	**18,475,229**	**18,475,229**
Earnings per share (pence)		
Continuing operations	153.2	107.7
Discontinued operations	-	21.1
	153.2	**128.8**

8.2 Diluted

Diluted earnings per ordinary share are calculated by dividing the profit attributable to equity holders of the parent by the weighted average number of ordinary shares in issue during the year, as noted above, as well as the number of dilutive share options in issue during the year, as follows:

	2018	2017
Weighted average number of ordinary shares	18,475,229	18,475,229
Number of dilutive shares in issue at the year end	277,234	219,007
Fully diluted weighted average number of ordinary shares	18,752,463	18,694,236
Dilutive shares being based on:		
Number of options outstanding at the year end	511,706	368,063
Weighted average exercise price (pence)	678	799
Average share price during the period (pence)	1,489	1,974
Diluted earnings per share (pence)		
Continuing operations	150.9	106.4
Discontinued operations	-	20.9
	150.9	**127.3**

9. Dividends

	2018	2017
	£'000	£'000
2016 final dividend - 58 pence per share (paid May 2017)	-	10.7
2017 interim dividend – 18 pence per share (paid September 2017)	-	3.3
2017 final dividend – 61 pence per share (paid May 2018)	11.3	-
2018 interim dividend – 19 pence per share (paid September 2018)	3.5	-
	14.8	**14.0**

The directors recommend the payment of a final dividend of 64 pence per share which, together with the interim dividend of 19 pence per share paid on 28 September 2018, represents total dividends for the year of 83 pence per share (2017: 79 pence per share). The final dividend, if approved by members at the Annual General Meeting, will be paid on 24 May 2019 to shareholders on the register at the close of business on 26 April 2019.

10. Loans and advances to banks

	Group	Group	Company	Company
	2018	2017	2018	2017
	£million	£million	£million	£million

Placements with banks included in cash and cash equivalents (Note 28)	44.8	34.3	41.9	32.3

Moody's long-term ratings are as follows:

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
A1	11.2	6.1	11.1	6.0
A1*/A2	28.6	-	25.8	-
A3	-	23.2	-	21.3
Arbuthnot Latham & Co., Limited - No rating	5.0	5.0	5.0	5.0
	44.8	**34.3**	**41.9**	**32.3**

None of the loans and advances to banks are either past due or impaired.

11. Loans and advances to customers

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Gross loans and advances	2,096.0	1,638.2	2,048.9	1,605.4
Less: allowances for impairment on loans and advances (Note 13)	(67.1)	(39.9)	(68.6)	(39.9)
	2,028.9	**1,598.3**	**1,980.3**	**1,565.5**

The fair value of loans and advances to customers is shown in Note 35. For a maturity profile of loans and advances to customers, refer to Note 34.

Group and Company

At 31 December 2018 loans and advances to customers of £326.5 million (2017: £200.7 million) were pre-positioned under the Bank of England's Term Funding Scheme, and were available for use as collateral within the scheme.

The following loans are secured upon real estate:

	2018 Loan balance £million	2018 Loan-to-value %	2017 Loan balance £million	2017 Loan-to-value %
Real Estate Finance	769.8	57%	580.8	57%
Consumer Mortgages	84.7	59%	16.5	59%
	854.5		**597.3**	

Under its credit policy, the Real Estate Finance business lends to a maximum loan-to-value of 70% for investment loans and 60% for residential development loans and up to 65% for pre-let commercial development loans (based on gross development value), and the Consumer Mortgages business lends to a maximum of 90%.

None of these loans are impaired. All property valuations at loan inception, and the majority of development stage valuations, are performed by independent Chartered Surveyors, who perform their work in accordance with the Royal Institution of Chartered Surveyors Valuation – Professional Standards.

Group

£1.9 million (2017: £2.5 million) of collateral is held from RentSmart, against loans of £10.8 million (2017: £14.9 million). This collateral is included in trade payables at 31 December 2018. This is based upon the balance of customer receivables and expected new agreements during the following month.

12. Finance lease receivables

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

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million

Gross investment in finance lease receivables:				
- No later than 1 year	175.3	189.9	168.7	180.7
- Later than 1 year and no later than 5 years	326.9	374.2	322.0	367.7
- Later than 5 years	0.2	1.2	0.2	1.2
	502.4	565.3	490.9	549.6
Unearned future finance income on finance leases	(135.8)	(162.5)	(132.8)	(158.4)
Net investment in finance leases	**366.6**	**402.8**	**358.1**	**391.2**
The net investment in finance leases may be analysed as follows:				
- No later than 1 year	112.0	117.5	107.6	111.3
- Later than 1 year and no later than 5 years	254.4	284.2	250.3	278.8
- Later than 5 years	0.2	1.1	0.2	1.1
	366.6	**402.8**	**358.1**	**391.2**

13. Allowances for impairment of loans and advances

Group

	Not credit impaired Stage 1: Subject to 12 month ECL £million	Stage 2: Subject to lifetime ECL £million	Credit impaired Stage 3: Subject to lifetime ECL £million	Total provision £million	Gross loans and receivables £million	Provision cover %
31 December 2018						
Business Finance:						
Real Estate Finance	0.6	-	-	0.6	770.4	0.1%
Asset Finance	0.2	0.1	2.7	3.0	65.8	4.6%
Commercial Finance	0.2	0.2	0.4	0.8	195.5	0.4%
Consumer Finance:						
Retail Finance	8.9	9.8	4.3	23.0	620.0	3.7%
Motor Finance:						
Voluntary termination provision	6.0	-	-	6.0		
Other impairment	4.2	13.8	15.4	33.4		
	10.2	13.8	15.4	39.4	315.8	12.5%
Debt Management	-	-	-	-	32.3	0.0%
Consumer Mortgages	0.2	-	-	0.2	84.9	0.2%
Other	-	-	0.1	0.1	11.3	0.9%
	20.3	**23.9**	**22.9**	**67.1**	**2,096.0**	**3.2%**

Total provisions above include expert credit judgements over the Group's IFRS 9 model results of £2.0 million, of which £1.4 million are specific overlays held against credit impaired secured assets held within the Business Finance portfolio. These specific overlays have been estimated on an individual basis by assessing the recoverability and condition of the secured asset, along with any other recoveries that may be made. The remaining £0.6 million primarily relates to the estimated impact of planned enhancements to LGD elements of the models of £0.8 million, offset by a net decrease in the ECL due to management judgements in respect of the PD elements of the models.

Within this Note, provision charges and balances in respect of 2018 are prepared on an IFRS 9 basis. In accordance with the transitional provisions of the standard comparatives set out in the tables below have not been restated. Refer to Notes 1 and 38 for further information.

	Individual provision £million	Collective provision £million	Total provision £million	Gross loans and receivables £million	Provision cover %
31 December 2017 (IAS 39 basis)					
Business Finance					
Real Estate Finance	-	0.3	0.3	581.1	0.1%
Asset Finance	1.0	0.2	1.2	117.9	1.0%
Commercial Finance	0.4	0.2	0.6	127.1	0.5%
Consumer finance					
Retail Finance	6.5	1.1	7.6	459.9	1.7%
Motor Finance					

Voluntary termination provision	1.0	-	1.0		
Other impairment	23.3	2.6	25.9		
	24.3	2.6	26.9	301.5	8.9%
Debt Management	-	-	-	15.6	0.0%
Consumer Mortgages	-	-	-	16.5	0.0%
Other	3.3	-	3.3	18.6	17.7%
	35.5	**4.4**	**39.9**	**1,638.2**	**2.4%**

Provisions included in 'Other' are in respect of various legacy products. This segment also includes loans of £10.8 million (2017: £14.9 million) held in STB Leasing Limited. The credit risk associated with those loans is retained by its partner, RentSmart. Accordingly, no provision is held against the RentSmart loans.

The impairment losses disclosed in the income statement, for continuing operations, can be analysed as follows:

	2018 (IFRS 9) £million	2017 (IAS 39) £million
IFRS 9 ECL/ IAS 39 incurred loss individual provision: charge for impairment losses	30.4	36.4
IAS 39 incurred loss collective provision: charge for impairment losses	-	(0.4)
Loans written off, net of amounts utilised	4.3	1.4
Recoveries of loans written off	(2.3)	(0.5)
	32.4	36.9
Less Personal Lending	-	(3.4)
	32.4	**33.5**

Reconciliations of the opening to closing impairment allowance for losses on loans and advances are presented below:

	Not credit impaired		Credit impaired	
	Stage 1: Subject to 12 month ECL £million	Stage 2: Subject to lifetime ECL £million	Stage 3: Subject to lifetime ECL £million	Total £million
At 1 January 2018	18.9	24.9	27.9	71.7
Increase/(decrease)due to change in credit risk				
- Transfer to stage 2	(6.3)	33.0	-	26.7
- Transfer to stage 3	(0.1)	(23.4)	30.8	7.3
- Transfer to stage 1	1.5	(3.2)	-	(1.7)
Passage of time	(6.7)	(1.7)	(3.9)	(12.3)
New loans originated	17.4	-	-	17.4
Derecognised loans	(1.8)	(4.0)	-	(5.8)
Changes to model methodology	(1.3)	(0.2)	-	(1.5)
Changes to credit risk parameters	(1.2)	(1.5)	0.6	(2.1)
Other adjustments	2.4	-	-	2.4
Charge to income statement	3.9	(1.0)	27.5	30.4
Allowance utilised in respect of write offs	(2.5)	-	(32.5)	(35.0)
31 December 2018	**20.3**	**23.9**	**22.9**	**67.1**

Passage of time represents the impact of accounts maturing through their contractual life and the associated reduction in PDs. For stage 3 assets it represents the unwind of the discount applied in calculating the ECL.
Changes to model methodology represents movements that have occurred due to enhancements made to the models during the year.
Changes to credit risk parameters represents movements that have occurred due to the Group updating model inputs. This would include the impact of, for example, updating the macro economic scenarios applied to the models.
Other adjustments represents the movement in the Motor voluntary termination provision.

The table above has been prepared based on monthly movements in the ECL. Stage 1 write offs arise on Motor accounts that have exercised their right to voluntarily terminate their agreements.

	£million
31 December 2017 (IAS 39 basis)	

Individual allowances for impairment	
At 1 January	23.1
Charge for impairment losses	36.4
Amounts utilised	(13.5)
Changes to presentation in respect of debt sales	(3.6)
Sale of personal lending	(6.9)
At 31 December	**35.5**

Collective allowances for impairment	
At 1 January	5.3
Charge for impairment losses	(0.4)
Sale of personal lending	(0.5)
At 31 December	**4.4**

Total allowances for impairment	**39.9**

Interest income on loans classified as impaired totalled £2.0 million (2017: £2.6 million).

Company

	Not credit impaired Stage 1: Subject to 12 month ECL	Stage 2: Subject to lifetime ECL	Credit impaired Stage 3: Subject to lifetime ECL	Total provision	Gross loans and receivables	Provision cover
	£million	£million	£million	£million	£million	%
31 December 2018						
Business Finance:						
Real Estate Finance	0.6	-	-	0.6	770.4	0.1%
Asset Finance	0.2	0.1	2.7	3.0	65.8	4.6%
Commercial Finance	0.2	0.2	0.4	0.8	191.4	0.4%
Consumer Finance:						
Retail Finance	9.2	9.8	4.4	23.4	620.0	3.8%
Motor Finance:						
Voluntary termination provision	6.0	-	-	6.0		
Other impairment	4.3	14.2	16.0	34.5		
	10.3	14.2	16.0	40.5	315.8	12.8%
Consumer Mortgages	0.2	-	-	0.2	84.9	0.2%
Other	-	-	0.1	0.1	0.6	16.7%
	20.7	**24.3**	**23.6**	**68.6**	**2,048.9**	**3.3%**

Total provisions above include expert credit judgements over the Group's IFRS 9 model results of £2.0 million, of which £1.4 million are specific overlays held against credit impaired secured assets held within the Business Finance portfolio. These specific overlays have been estimated on an individual basis by assessing the recoverability and condition of the secured asset, along with any other recoveries that may be made. The remaining £0.6 million primarily relates to the estimated impact of planned enhancements to LGD elements of the models of £0.8 million, offset by a net decrease in the ECL due to management judgements in respect of the PD elements of the models.

	Individual provision	Collective provision	Total provision	Gross loans and receivables	Provision cover
	£million	£million	£million	£million	%
31 December 2017 (IAS 39 basis)					
Business Finance					
Real Estate Finance	-	0.3	0.3	581.1	0.1%
Asset Finance	1.0	0.2	1.2	117.9	1.0%
Commercial Finance	0.4	0.2	0.6	124.8	0.5%
Consumer Finance					
Retail Finance	6.5	1.1	7.6	459.9	1.7%
Motor Finance					
Voluntary termination provision	1.0	-	1.0		

Other impairment	23.3	2.6	25.9		
	24.3	2.6	26.9	301.5	8.9%
Consumer Mortgages	-	-	-	16.5	0.0%
Other	3.3	-	3.3	3.7	89.2%
	35.5	**4.4**	**39.9**	**1,605.4**	**2.5%**

The impairment losses disclosed in the income statement, for continuing operations, can be analysed as follows:

	2018 (IFRS 9) £million	2017 (IAS 39) £million
IFRS 9 ECL/ IAS 39 incurred loss individual provision: charge for impairment losses	33.9	38.8
IFRS 9 impairment losses in respect of off balance sheet loan commitments	0.1	-
IAS 39 incurred loss collective provision: charge for impairment losses	-	(0.4)
Loans written off, net of amounts utilised	1.7	1.4
Recoveries of loans written off	(2.4)	(0.5)
Profit on sale of debt	(0.2)	(0.3)
	33.1	39.0
Less Personal Lending	-	(3.4)
	33.1	**35.6**

Reconciliations of the opening to closing impairment allowance for losses on loans and advances are presented below:

	Not credit impaired		Credit impaired	
	Stage 1: Subject to 12 month ECL £million	Stage 2: Subject to lifetime ECL £million	Stage 3: Subject to lifetime ECL £million	Total £million
At 1 January 2018	19.0	25.1	28.2	72.3
Increase/(decrease)due to change in credit risk				
- Transfer to stage 2	(6.5)	33.9	-	27.4
- Transfer to stage 3	(0.1)	(24.0)	31.6	7.5
- Transfer to stage 1	1.5	(3.2)	-	(1.7)
Passage of time	(6.7)	(1.6)	(4.6)	(12.9)
New loans originated	17.9	-	-	17.9
Derecognised loans	(1.8)	(4.1)	2.8	(3.1)
Changes to model methodology	(1.3)	(0.2)	-	(1.5)
Changes to credit risk parameters	(1.2)	(1.5)	0.6	(2.1)
Other adjustments	2.4	-	-	2.4
Charge to income statement	4.2	(0.7)	30.4	33.9
Allowance utilised in respect of write offs	(2.5)	(0.1)	(35.0)	(37.6)
31 December 2018	**20.7**	**24.3**	**23.6**	**68.6**

Passage of time represents the impact of accounts maturing through their contractual life and the associated reduction in PDs. For stage 3 assets it represents the unwind of the discount applied in calculating the ECL.
Changes to model methodology represents movements that have occurred due to enhancements made to the models during the year.
Changes to credit risk parameters represents movements that have occurred due to the Group updating model inputs. This would include the impact of, for example, updating the macro economic scenarios applied to the models.
Other adjustments represents the movement in the Motor voluntary termination provision.

The table above has been prepared based on monthly movements in the ECL. Stage 1 write offs arise on Motor accounts that have exercised their right to voluntarily terminate their agreements.

	£million
31 December 2017 (IAS 39 basis)	
Individual allowances for impairment	
At 1 January	22.4
Charge for impairment losses	38.8
Utilised	(13.5)

Release of allowance for impairment on the sale of debt	(5.3)
Sale of personal lending	(6.9)
At 31 December	**35.5**

Collective allowances for impairment	
At 1 January	5.3
Charge for impairment losses	(0.4)
Sale of personal lending	(0.5)
At 31 December	**4.4**

Total allowances for impairment	**39.9**

Interest income on loans classified as impaired totalled £1.1 million (2017: £2.6 million).

14. Debt securities

Debt securities of £149.7 million (2017: £5.0 million) represent UK Treasury Bills. The Company's intention is to hold them to maturity and, therefore, they are stated in the statement of financial position at amortised cost.

All of the debt securities had a rating agency designation at 31 December 2018, based on Moody's long-term ratings of Aa2 (2017: Aa2). None of the debt securities are either past due or impaired.

15. Property, plant and equipment

Group

	Freehold land and buildings £million	Leasehold property	Computer and other equipment £million	Total £million
Cost or valuation				
At 1 January 2017	9.0	-	10.9	19.9
Additions	-	-	0.8	0.8
At 31 December 2017	**9.0**	**-**	**11.7**	**20.7**
Additions	-	0.1	1.0	1.1
Disposals	-	-	(2.0)	(2.0)
Revaluation	(0.8)	-	-	(0.8)
At 31 December 2018	**8.2**	**0.1**	**10.7**	**19.0**
Accumulated depreciation				
At 1 January 2017	-	-	**(8.5)**	**(8.5)**
Depreciation charge	(0.1)	-	(0.7)	(0.8)
Revaluation	0.1	-	-	0.1
At 31 December 2017	-	-	**(9.2)**	**(9.2)**
Depreciation charge	(0.5)	-	(0.8)	(1.3)
Disposals	-	-	2.0	2.0
Revaluation	0.5	-	-	0.5
At 31 December 2018	-	-	**(8.0)**	**(8.0)**
Net book amount				
At 31 December 2017	9.0	-	**2.5**	**11.5**
At 31 December 2018	**8.2**	**0.1**	**2.7**	**11.0**

Company

	Freehold property £million	Computer and other equipment £million	Total £million
Cost or valuation			
At 31 December 2017	4.6	9.8	14.4
Additions	-	0.3	0.3
At 31 December 2017	**4.6**	**10.1**	**14.7**
Additions	-	0.5	0.5

Disposals	-	(2.0)	(2.0)
At 31 December 2018	**4.6**	**8.6**	**13.2**
Accumulated depreciation			
At 1 January 2017	-	(8.2)	(8.2)
Depreciation charge	-	(0.4)	(0.4)
At 31 December 2017	-	**(8.6)**	**(8.6)**
Depreciation charge	(0.4)	(0.3)	(0.7)
Disposals	-	2.0	2.0
Revaluation	0.1	-	0.1
At 31 December 2018	(0.3)	**(6.9)**	**(7.2)**
Net book amount			
At 31 December 2017	**4.6**	**1.5**	**6.1**
At 31 December 2018	**4.3**	**1.7**	**6.0**

The Group's freehold properties comprise:

- the Registered Office of the Company, which is fully utilised for the Group's own purposes.
- Secure Trust House, Boston Drive, Bourne End, SL8 5YS, which is only partially used for the Group's own purposes.
- 25 and 26 Neptune Court, Vanguard Way, Cardiff, CF24 5PJ, which is fully utilised for the Group's own purposes.

Freehold properties are stated at fair value as at 31 December 2018 based on external valuations performed by professionally qualified valuers Knight Frank LLP. These valuations have been undertaken in accordance with International Valuations Standards, and were arrived at by reference to market evidence of the transaction prices paid for similar properties. In estimating the fair value of the properties, the valuers consider the highest and best use of the properties. Knight Frank LLP were paid a fixed fee for the valuations. Knight Frank LLP also undertakes some professional work in respect of the Group's Real Estate Finance business, although this is limited in relation to the activities of the Group as a whole. A decrease in the fair value of freehold property has been recognised and its carrying value has been adjusted accordingly. Movements in the fair value of freehold property are recognized in other comprehensive income, to the extent that any reductions do not exceed the initial increase.

The carrying value of freehold land which is included in the total carrying value of freehold land and buildings and which is not depreciated is £1.9 million (2017: £1.9 million).

The historical cost of freehold property included at valuation is as follows:

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Cost	7.9	7.9	4.1	4.1
Accumulated depreciation	(1.6)	(1.5)	(0.2)	(0.1)
	6.3	**6.4**	**3.9**	**4.0**

16. Intangible assets

Group

	Goodwill £million	Computer software £million	Other intangible assets £million	Total £million
Cost or valuation				
At 1 January 2017	1.0	12.9	2.2	16.1
Additions	-	3.3	0.1	3.4
At 31 December 2017	**1.0**	**16.2**	**2.3**	**19.5**
Additions	-	1.4	-	1.4
Disposals	-	(0.6)	(0.1)	(0.7)
At 31 December 2018	**1.0**	**17.0**	**2.2**	**20.2**

Accumulated amortisation				
At 1 January 2017	-	(6.1)	(1.0)	(7.1)
Amortisation charge	-	(1.8)	(0.2)	(2.0)
At 31 December 2017	-	**(7.9)**	**(1.2)**	**(9.1)**
Amortisation charge	-	(1.6)	(0.2)	(1.8)
Disposals	-	0.6	-	0.6
At 31 December 2018	-	**(8.9)**	**(1.4)**	**(10.3)**
Net book amount				
At 31 December 2017	**1.0**	**8.3**	**1.1**	**10.4**
At 31 December 2018	**1.0**	**8.1**	**0.8**	**9.9**

Goodwill above relates to the following cash generating units, which are part of the Retail Finance operating segment:

	2018 £million	2017 £million
Music business	0.3	0.3
V12	0.7	0.7
Total	**1.0**	**1.0**

The recoverable amount of these cash generating units are determined on a value in use calculation which uses cash flow projections based on financial forecasts covering a three year period, and a discount rate of 8%. Cash flow projections during the forecast period are based on the expected rate of new business. A zero growth based scenario is also considered. The directors believe that any reasonably possible change in the key assumptions on which recoverable amount is based would not cause the aggregate carrying amount to exceed the aggregate recoverable amount of the cash-generating unit.

Other intangible assets were recognised as part of the V12 Finance Group acquisition. These were recorded at fair value, and are being amortised on a straight line basis as follows:

	Years
IT system	5
Distribution channel	10
Brand name	5

Company

	Goodwill £million	Computer software £million	Total £million
Cost or valuation			
At 1 January 2017	0.3	9.0	9.3
Additions	-	3.3	3.3
At 31 December 2017	**0.3**	**12.3**	**12.6**
Additions	-	1.3	1.3
Disposals	-	(0.7)	(0.7)
At 31 December 2018	**0.3**	**12.9**	**13.2**
Accumulated amortisation			
At 1 January 2017	-	(3.1)	(3.1)
Amortisation charge	-	(1.0)	(1.0)
At 31 December 2017	-	**(4.1)**	**(4.1)**
Amortisation charge	-	(1.6)	(1.6)
Disposals	-	0.6	0.6
At 31 December 2018	-	**(5.1)**	**(5.1)**
Net book amount			

At 31 December 2017	**0.3**	**8.2**	**8.5**
At 31 December 2018	**0.3**	**7.8**	**8.1**

Goodwill above relates to the music business cash generating unit, which is part of the Retail Finance operating segment. The recoverable amount is determined on the same basis as for the Group.

17. Investments

Company

	£million
Cost and net book value	
At 31 December 2017 and 1 January 2018	3.7
Equity contributions to subsidiaries in respect of share options	0.2
At 31 December 2018	**3.9**

Shares in subsidiary undertakings of Secure Trust Bank PLC at 31 December 2018 are stated at cost less any provision for impairment. All subsidiary undertakings are unlisted and none are banking institutions. All are 100% owned by the Company. The subsidiary undertakings were all incorporated in the UK and wholly owned via ordinary shares. All subsidiary undertakings are included in the consolidated financial statements and have an accounting reference date of 31 December.

Details are as follows:

	Principal activity
Owned directly	
Debt Managers (Services) Limited	Debt collection company
Secure Homes Services Limited	Property rental
STB Leasing Limited	Leasing
V12 Finance Group Limited	Holding company
Owned indirectly via intermediate holding companies	
V12 Personal Finance Limited	Dormant
V12 Retail Finance Limited	Sourcing and servicing of unsecured loans

The registered office of the Company, and all subsidiary undertakings, is One Arleston Way, Shirley, Solihull, West Midlands, B90 4LH.

18. Deferred taxation

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Deferred tax liabilities:				
Unrealised surplus on revaluation of freehold property	-	(0.2)	-	-
Other short term timing differences	-	0.2	-	-
Deferred tax liabilities	-	-	-	-
Deferred tax assets:				
Other short term timing differences	7.9	0.6	7.8	0.6
Deferred tax assets	**7.9**	**0.6**	**7.8**	**0.6**
Deferred tax liabilities:				
At 1 January	-	(0.2)	-	-
Income statement	-	0.2	-	-
Other comprehensive income	-	-	-	-
At 31 December	-	-	-	-
Deferred tax assets:				
Prior period closing (IAS 39 basis)	0.6	-	0.6	0.1
Tax on IFRS 9 transition adjustment	6.3	-	6.4	-

At 1 January	6.9	-	7.0	0.1
Income statement	1.2	0.2	1.1	0.1
Other comprehensive income	(0.2)	0.4	(0.3)	0.4
At 31 December	**7.9**	**0.6**	**7.8**	**0.6**

The Government substantively enacted a reduction in the main rate of UK corporation tax from 20% to 19% (effective from 1 April 2017) and a further reduction to 17% (effective 1 April 2020). The Government also introduced an 8% surcharge on the profits of banking companies in excess of £25 million effective from 1 January 2016. Deferred tax has been calculated based on the enacted rates to the extent that the related temporary differences are expected to reverse in future periods. A deferred tax asset was recognised on the IFRS 9 transition adjustment on 1 January 2018 and the current year credit includes a reassessment of the rates at which it is projected to reverse over the period to 31 December 2027.

19. Other assets

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Other receivables	16.2	1.2	16.1	1.0
Amounts due from related companies	-	-	44.5	29.7
Prepayments and accrued income	6.2	4.2	5.0	2.5
	22.4	**5.4**	**65.6**	**33.2**

20. Due to banks

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Amounts due to other credit institutions	263.0	113.0	263.0	113.0
Accrued interest	0.5	-	0.5	-
	263.5	113.0	263.5	113.0

Amounts due to banks for the current year represent monies arising from drawings under the Term Funding Scheme. These are due for repayment between May 2021 and February 2022 (2017: May 2021 and November 2021).

21. Deposits from customers
Group and Company

	2018 £million	2017 £million
Current/demand accounts	14.5	14.5
Term deposits	1,833.2	1,468.7
	1,847.7	**1,483.2**

For a maturity profile of deposits from customers, refer to Notes 31, 32 and 34.

22. Other liabilities

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Other payables	25.8	29.5	22.8	24.5
Amounts due to related companies	-	-	14.1	9.7
Accruals and deferred income	14.3	12.4	12.2	10.2
	40.1	**41.9**	**49.1**	**44.4**

Financial Services Compensation Scheme Levy

The Financial Services Compensation Scheme has confirmed that it has repaid the remaining £4.68 billion it owed to HM Treasury relating to the Bradford and Bingley failure in 2008. Accordingly, no accrual was held for this item as at 31 December 2018.

In the prior year, the liability for the Financial Services Compensation Scheme levy was included in accruals and deferred income of both Group and Company.

In common with all regulated UK deposit takers, the Company paid a levy to the Financial Services Compensation Scheme to enable it to meet claims against it. The levy consists of a compensation levy which covers the amount of compensation and a management expenses levy, which covers the costs of running the scheme and interest associated with compensation which the scheme pays.

The Company's Financial Services Compensation Scheme accrual at 31 December 2017 of £0.2 million reflected market participation up to the date of the last payment to the scheme in September 2018. This amount was calculated on the basis of the Company's share of protected deposits and the Financial Services Compensation Scheme's estimate of total interest levies payable for the last scheme year.

23. Provisions for liabilities and charges

Group and Company

	Customer redress	ECL allowance on loan commitments	Fraud	Total
	£million	£million	£million	£million
Balance at 1 January 2017	1.3	-	-	1.3
Charged to income statement	0.4	-	0.2	0.6
Utilised	(0.5)	-	-	(0.5)
Balance at 31 December 2017	1.2	-	0.2	1.4
IFRS 9 transition adjustment	-	0.3	-	0.3
Balance at 1 January 2018	1.2	0.3	0.2	1.7
(Credited)/charged to income statement	(0.4)	0.1	(0.1)	(0.4)
Balance at 31 December 2018	**0.8**	**0.4**	**0.1**	**1.3**

Customer redress provision

The Group provides for its best estimate of redress payable in respect of historical sales of accident, sickness and unemployment insurance, by considering the likely future uphold rate for claims, in the context of confirmed issues and historical experience. The likelihood of potential new claims is projected forward to 2019, as management believe this to be an appropriate time horizon, recognising the significant decline in recent claims experience and the increasing subjectivity beyond that. The accuracy of these estimates would be affected, were there to be a significant change in either the number of future claims or the incidence of claims upheld by the Financial Ombudsman Service.

The Financial Conduct Authority has announced a deadline for making these customer redress claims, which would give consumers until 29 August 2019 to make a claim.

Fraud

The fraud provision relates to cases where the Bank has reasonable evidence of suspected fraud, but further investigation is required before the cases can be dealt with appropriately.

ECL allowance on loan commitments

In accordance with the requirements of IFRS 9 the Group holds an ECL allowance against loans it has committed to lend but have not yet been drawn. For the Real Estate Finance and Commercial Finance portfolios, where a loan facility is agreed that includes both drawn and undrawn elements and the Group cannot identify the ECL on the loan commitment separately, a combined loss allowance for both drawn and undrawn components of the loan is presented as a deduction from the gross carrying amount of the drawn component, with any excess of the loss allowance over the gross drawn amount presented as a provision. At 31 December 2018 no provision was held for losses in excess of drawn amounts.

24. Subordinated liabilities

	£million
At 1 January 2018	-
Issued during the year	50.0
Unamortised issue costs	(0.8)

Accrued interest	1.2
At 31 December 2018	**50.4**

During the year, Secure Trust Bank PLC issued two tranches of 6.75% Fixed Rate Reset Callable Subordinated Notes due 2028 (the Notes):

- £25 million on 17 July 2018
- £25 million on 2 October 2018.

The Notes mature in 2028 but the issuer may at its discretion redeem the Notes in 2023. The Notes are listed on the Global Exchange Market of the Irish Stock Exchange plc trading as Euronext Dublin.

The Notes are treated as Tier 2 regulatory capital which is used to support the continuing growth of the business taking into account increases in regulatory capital buffers. The issue of the Notes is part of an on-going programme to diversify and expand the capital base of the Bank.

25. Contingent liabilities and commitments

25.1 Contingent liabilities

As a financial services business, the Group must comply with numerous laws and regulations, which significantly affect the way it does business. Whilst the Group believes there are no material unidentified areas of failure to comply with these laws and regulations, there can be no guarantee that all issues have been identified.

25.2 Capital commitments

At 31 December 2018, the Group had no capital commitments (2017: £nil).

The Company had no capital commitments (2017: £nil).

25.3 Credit commitments

Commitments to extend credit to customers were as follows:

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Business Finance				
Real Estate Finance	173.4	98.6	173.4	98.6
Asset Finance	-	15.5	-	15.5
Commercial Finance	45.6	35.5	45.6	35.5
Consumer Finance				
Retail Finance	28.3	20.1	28.3	20.1
Motor Finance	0.5	0.6	0.5	0.6
Consumer Mortgages	15.3	7.7	15.3	7.7
Other	-	0.6	-	0.5
	263.1	**178.6**	**263.1**	**178.5**

25.4 Operating lease commitments

The future aggregate lease payments for non-cancellable operating leases are as follows:

	2018		2017	
Group	Land and buildings £million	Other £million	Land and buildings £million	Other £million
Within 1 year	1.1	0.2	0.3	0.1
Between 1 year and 5 years	3.9	0.2	0.8	0.1
Over 5 years	2.0	-	-	-
	7.0	**0.4**	**1.1**	**0.2**

	2018		2017	
Company	Land and buildings £million	Other £million	Land and buildings £million	Other £million

Within 1 year	0.8	0.1	0.1	0.1
Between 1 year and 5 years	3.0	0.1	0.4	-
Over 5 years	1.4	-	-	-
	5.2	**0.2**	**0.5**	**0.1**

There are seven leases classified as land and buildings in the Group (2017: 3). Other leases include motor vehicles and computer hardware.

26. Share capital

	2018 Number	2018 £ million	2017 Number	2017 £ million
At start and end of year	**18,475,229**	**7.4**	**18,475,229**	**7.4**

Share capital comprises ordinary shares with a par value of 40 pence each.

27. Share based payments

At 31 December 2018, the Group had five share based payment schemes in operation:

- Share option Scheme
- 2017 long term incentive plan
- 2017 sharesave plan
- 2017 deferred bonus plan
- 'Phantom' share option scheme.

A summary of the key details of each scheme is set out below:

	Outstanding at the start of the year Number	Granted during the year Number	Leavers during the year Number	Outstanding at the end of the year Number	Vested and exercisable Number	Vesting Date	Exercise price £
Equity settled							
Share option scheme	177,084	-	-	177,084	177,084	2 November 2016	7.20
						1 June 2020	0.40
2017 long term incentive plan	67,992	94,504	(899)	161,597	-	20 April 2021	0.40
						1 November 2020	13.19
2017 sharesave plan	125,947	34,449	(15,387)	145,009	-	1 November 2021	14.03
						20 April 2019	0.40
						20 April 2020	0.40
2017 deferred bonus plan	-	14,690	-	14,690	-	20 April 2021	0.40
	371,023	143,643	(16,286)	498,380	177,084		
Cash settled							
'Phantom' share option scheme	312,917	-	-	312,917	-	16 March 2019	25.00

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Expense incurred in relation to share-based payments	**0.8**	**-**	**0.6**	**-**

27.1 Share option scheme

The share option scheme was established on 17 October 2011.

On 2 November 2011, 934,998 share options were granted at an exercise price of £7.20 per share, entitling three directors and certain senior employees to purchase shares in the Company. Approximately half of the share options

vested and were exercised on 2 November 2014, with the remainder vesting and becoming exercisable on 2 November 2016. The bulk of the remainder were exercised on 7 November 2016, leaving 177,084 share options of 2 directors unexercised. Vested options are exercisable for a period of 10 years from the date of grant.

The intrinsic value of unexercised options is £0.8 million (2017: £1.8 million).

27.2 Long term incentive plan

The long term incentive plan was established on 3 May 2017.

Awards under this plan are subject to three performance conditions, which are based on:

- Annual compound growth in earnings per share ('EPS') over the performance period
- Rank of the total shareholder return ('TSR') over the performance period against the TSR of the comparator group of peer group companies
- Maintaining appropriate risk practices over the performance period reflecting the longer term strategic risk management of the Group.

The awards will vest on the date on which the board determines that these conditions have been met.

The awards have a performance term of 3 years. Those awards granted to the Executive Directors are subject to a holding period of 2 years following the vesting date. Those awards not subject to a holding period will be released to the participants on the vesting date. Vested options are exercisable for a period of 10 years from the date of grant.

The following awards have been granted under the plan, entitling two Executive Directors and certain other key senior employees to purchase shares in the Company. The exercise price is £0.40 per share. The original grant date valuation was determined using a Black-Scholes model for the EPS and risk management tranches, and a Monte Carlo model for the TSR tranche:

	Subject to a holding period of two years Awards granted	Subject to a holding period of two years Grant date valuation	Subject to no holding period Awards granted	Subject to no holding period Grant date valuation	Total Awards granted
	Number	£	Number	£	Number
Granted on 1 June 2017	33,467	12.19	34,525	14.82	67,992
At 31 December 2017	33,467		34,525		67,992
Granted on 20 April 2018	30,429	14.26	64,075	15.47	94,504
Leavers	-		(899)		(899)
At 31 December 2018	**63,896**		**97,701**		**161,597**

Measurement inputs and assumptions used for the grant date valuation were as follows:

	Awards granted on 20 April 2018	Awards granted on 1 June 2017
Share price at grant date	£20.85	£22.45
Expected dividend yield	4.05%	3.80%
Awards subject to a holding period		
Expected stock price volatility	25.2%	24.6%
Risk free interest rate	1.15%	0.42%
Average expected life (years)	5.00	5.00
Discount for lack of marketability during holding period	nil	10.00%
Awards not subject to a holding period		
Expected stock price volatility	26.9%	25.1%
Risk free interest rate	0.89%	0.19%
Average expected life (years)	3.00	3.00
Assumptions applicable to TSR tranche only		
Expected stock price volatility	27.1%	25.50%

Grant date TSR performance of the Company compared to comparator group	Upper quartile	Below median
Correlation	22%	37%

In calculating the charge to the income statement, an expected leaver rate has been assumed of nil% for the Executive Directors and 10% for other employees.

27.3 Sharesave plan

The sharesave plan was established on 3 May 2017.

This plan allows all employees with more than 12 months service to save for three years, subject to a maximum monthly amount of £500, with the option to buy shares in Secure Trust Bank PLC when the plan matures. Participants cannot change the amount that they have agreed to save each month but they can suspend payments for up to six months. Participants can withdraw their savings at any time but, if they do this before the completion date, they lose the option to buy shares at the Option Price, and if participants cease to hold plan-related employment before the third anniversary of the grant date, then the options are also lost. The options ordinarily vest approximately three years after grant date, and are exercisable for a period of six months following vesting.

The following awards have been granted under the plan, entitling all eligible employees to purchase shares in the Company. The original grant date valuation was determined using a Black-Scholes model:

	Awards granted	Grant date valuation	Exercise price
	Number	£	£
Granted on 20 September 2017	125,987	3.53	13.19
Leavers	(40)		
At 31 December 2017	125,947		
Granted on 18 September 2018	34,449	3.67	14.03
Leavers	(15,387)		
At 31 December 2018	**145,009**		

Measurement inputs and assumptions used were as follows:

	Awards granted on 18 September 2018	Awards granted on 20 September 2017
Share price at grant date	£17.53	£17.51
Expected stock price volatility	28.14%	25.55%
Expected dividend yield	4.57%	4.34%
Risk free interest rate	0.89%	0.58%
Average expected life (years)	3.36	3.36

In calculating the charge to the income statement, an expected leaver rate of 10% has been assumed.

27.4 Deferred bonus plan

The deferred bonus plan was established on 3 May 2017.

As disclosed in the 2017 annual report and accounts, 50% of the bonus earned by two Executive Directors, amounting to £280,000, was deferred into shares under the deferred bonus plan. The award will vest in three equal tranches after one, two and three years following deferral.

Accordingly, the following awards have been granted under the plan, entitling the two Executive Directors to purchase shares in the Company. The exercise price is £0.40 per share. The original grant date valuation was determined using a Black-Scholes model:

	Awards granted	Grant date valuation	Awards granted	Grant date valuation	Awards granted	Grant date valuation	Awards granted

	Vesting after 1 year	Vesting after 1 year	Vesting after 2 years	Vesting after 2 years	Vesting after 3 year	Vesting after 3 years	Total
	Number	£	Number	£	Number	£	
Granted on 20 April 2018	4,896	19.64	4,896	18.87	4,898	18.12	14,690
At 31 December 2018	**4,896**		**4,896**		**4,898**		**14,690**

Measurement inputs and assumptions used were as follows:

	Awards vesting after one year	Awards vesting after two years	Awards vesting after three years
Share price at grant date	£20.85	£20.85	£20.85
Expected dividend yield	3.96%	3.96%	3.96%
Expected stock price volatility	25.25%	30.90%	27.68%
Risk free interest rate	0.69%	0.77%	0.82%
Average expected life (years)	1.00	2.00	3.00

27.5 Cash settled share based payments

On 16 March 2015, a four year 'phantom' share option scheme was established in order to provide effective long-term incentive to senior management of the Group. Under the scheme, no actual shares would be issued by the Company, but those granted awards under the scheme would be entitled to a cash payment. The amount of the award is calculated by reference to the increase in the value of an ordinary share in the Company over an initial value set at £25 per ordinary share, being the price at which the shares resulting from the exercise of the first tranche of share options under the share option scheme were sold in November 2014.

As at 31 December 2018, 312,917 (2017: 312,917) share options remained outstanding. The options will vest on 16 March 2019, and be exercisable for a period of 10 years after grant date.

As at 31 December 2018, the estimated fair value has been prepared using the Black-Scholes model. Measurement inputs and assumptions used were as follows:

	2018	2017
Share price at reporting date	£11.80	£17.97
Expected stock price volatility	24.76%	24.49%
Expected dividend yield	7.12%	4.45%
Risk free interest rate	0.76%	0.59%
Average expected life (years)	3.71	4.03
Fair value	**£0.05**	**£0.79**

As the options can be exercised at any point during the seven years after vesting, and given high levels of share price volatility, management has concluded that it is appropriate to hold the accrual at the same level as 2017. This resulted in the following being recognised in the financial statements:

	2018 £million	2017 £million
Liability at 1 January	0.2	0.6
Credit for the year	-	(0.4)
Liability at 31 December	**0.2**	**0.2**

28. Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise the following balances with less than three months' maturity from the date of acquisition.

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Cash and balances at central banks	169.7	226.1	169.7	226.1
Loans and advances to banks (Note 10)	44.8	34.3	41.9	32.3

	214.5	**260.4**	**211.6**	**258.4**

29. 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 appetite statement 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.

A more detailed description of the risk governance structure is contained in the Strategic Report beginning on page 40.

The principal financial risks inherent in the Group's business are credit risk (Note 30), market risk (Note 31), liquidity risk (Note 32), and capital risk (Note 33).

30. 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. A formal Credit Risk Policy has been agreed by the Board whilst credit risk is monitored on a monthly basis by the Credit Risk Committees which review performance of key portfolios including new business volumes, collections performance, provisioning levels and provisioning methodology. A credit risk department within the Group monitors adherence to the Credit Risk Policy, implements risk tools to manage credit risk and evaluates business opportunities and the risks and opportunities they present to the Group whilst ensuring the performance of the Group's existing portfolios is in line with expectations.

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

Impairment provisions are provided for expected credit losses at the statement of financial position date. Significant changes in the economy could result in losses that are different from those provided for at the statement of financial position date. Management therefore carefully manages the Group's exposures to credit risk as it considers this to be the most significant risk to the business.

Exposure to Consumer Finance and Consumer Mortgages 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 lending limits where appropriate. Exposure to credit risk for these portfolios is also managed in part by obtaining collateral, principally motor vehicles on Motor Finance loans, residential property on Consumer Mortgages and a credit support balance provided by RentSmart. The assets undergo a scoring process to mitigate risk and are monitored by the Board.

For Real Estate Finance and Commercial Finance, lending decisions are made on an individual transaction basis, using expert judgement and assessment against criteria set out in the lending policies. Asset Finance lending is outsourced to Haydock, who operate in line with the Group's credit policies and risk appetite, and is currently closed to new business. The loans are secured against the assets lent against (real estate, trade receivables and commercial plant and equipment, respectively). Disclosures relating to collateral and arrears on loans and advances to customers are disclosed in Notes 11 and 13 respectively.

The Board monitors the ratings of the counterparties in relation to the Group's loans and advances to banks. Disclosures of these at the year end are contained in Note 10. There is no direct exposure to the Eurozone and peripheral Eurozone countries.

Group

With the exception of loans and advances to customers, the carrying amount of financial assets represents the Group's maximum exposure to credit risk. The Group's maximum exposure to credit risk for loans and advances to customers by portfolio and IFRS 9 stage without taking account of any collateral held or other credit enhancements attached was as follows:

	Stage 1	Stage 2			Stage 3			Total
		<= 30 days past due	> 30 days past due	Total	Excl. purchased credit impaired	Purchased credit impaired	Total	
	£million	£million	£million	£million	£million	£million	£million	£million
31 December 2018								
Business Finance								
Real Estate Finance	723.3	47.1	-	47.1	-	-	-	770.4
Asset Finance	55.6	6.5	0.5	7.0	3.2	-	3.2	65.8
Commercial Finance	186.1	8.8	-	8.8	0.6	-	0.6	195.5
Consumer Finance								
Retail	537.1	74.1	3.9	78.0	4.9	-	4.9	620.0
Motor	200.2	92.7	2.4	95.1	20.5	-	20.5	315.8
Debt Management	-	-	-	-	9.3	23.0	32.3	32.3
Consumer Mortgages	84.9	-	-	-	-	-	-	84.9
Other	11.3	-	-	-	-	-	-	11.3
Total drawn exposure	1,798.5	229.2	6.8	236.0	38.5	23.0	61.5	2,096.0
Off balance sheet								
Loan commitments	263.1	-	-	-	-	-	-	263.1
Total gross exposure	2,061.6	229.2	6.8	236.0	38.5	23.0	61.5	2,359.1
Less:								
Impairment allowance	(20.3)	(19.9)	(4.0)	(23.9)	(22.9)	-	(22.9)	(67.1)
Provision for loan commitments	(0.4)	-	-	-	-	-	-	(0.4)
Total net exposure	**2,040.9**	**209.3**	**2.8**	**212.1**	**15.6**	**23.0**	**38.6**	**2,291.6**

The above table is prepared on an IFRS 9 basis. In accordance with the transitional provisions of the standard comparatives have not been restated. Refer to Notes 1 and 13 for further information. An analysis of the Group's opening loans and advances to customers by IFRS 9 stage and portfolio is presented in Note 38. The Group has not disclosed exposures and impairment allowance split by risk rating as this split is not used internally by the Group to monitor loan book performance.

A reconciliation of opening to closing impairment allowance for losses on loans and advances to customers is presented in Note 13.

The tables below summarise the December 2017 loans and advances to customers on an IAS 39 basis:

	£million	%
31 December 2017 (IAS 39 basis)		
Neither past due nor impaired	1,545.6	94.3%
Not past due but impaired	5.4	0.3%
Past due but not impaired	0.3	0.0%
Past due up to 90 days and impaired	37.8	2.3%
Past due after 90 days and impaired	49.1	3.0%
Gross	1,638.2	100.0%
Less: allowance for impairment	(39.9)	
Net	**1,598.3**	

Gross amounts of loans and advances to customers that were past due up to 90 days and impaired were as follows:

	£million
31 December 2017 (IAS 39 basis)	
Past due up to 30 days	24.5

Past due 30 - 60 days	8.6
Past due 60 - 90 days	4.7
Total	**37.8**

Gross amounts of loans and advances to customers that were past due but not impaired were as follows:

	£million
31 December 2017 (IAS 39 basis)	
Past due up to 30 days	0.2
Past due 30 - 60 days	0.1
Total	**0.3**

Company

The Group's maximum exposure to credit risk for loans and advances to customers by portfolio and IFRS 9 stage without taking account of any collateral held or other credit enhancements attached was as follows:

	Stage 1	Stage 2			Stage 3			Total
		<= 30 days past due	> 30 days past due	Total	Excl. purchased credit impaired	Purchased credit impaired	Total	
	£million	£million	£million	£million	£million	£million	£million	£million
31 December 2018								
Business Finance								
Real Estate Finance	723.3	47.1	-	47.1	-	-	-	770.4
Asset Finance	55.6	6.5	0.5	7.0	3.2	-	3.2	65.8
Commercial Finance	182.0	8.8	-	8.8	0.6	-	0.6	191.4
Consumer Finance								
Retail	537.1	74.1	3.9	78.0	4.9	-	4.9	620.0
Motor	200.2	92.7	2.4	95.1	20.5	-	20.5	315.8
Consumer Mortgages	84.9	-	-	-	-	-	-	84.9
Other	0.6	-	-	-	-	-	-	0.6
Total drawn exposure	1,783.7	229.2	6.8	236.0	29.2	-	29.2	2,048.9
Off balance sheet								
Loan commitments	263.1	-	-	-	-	-	-	263.1
Total gross exposure	2,046.8	229.2	6.8	236.0	29.2	-	29.2	2,312.0
Less:								
Impairment allowance	(20.7)	(20.2)	(4.1)	(24.3)	(23.6)	-	(23.6)	(68.6)
Provision for loan commitments	(0.4)	-	-	-	-	-	-	(0.4)
Total net exposure	**2,025.7**	**209.0**	**2.7**	**211.7**	**5.6**	**-**	**5.6**	**2,243.0**

The above table is prepared on an IFRS 9 basis. In accordance with the transitional provisions of the standard comparatives have not been restated. Refer to Notes 1 and 13 for further information. The average IFRS 9 probability of default (PD) is based on 12 month PDs at the reporting date.

The tables below summarise the December 2017 loans and advances to customers on an IAS 39 basis:

	£million	%
31 December 2017 (IAS 39 basis)		
Neither past due nor impaired	1,529.0	95.3%
Not past due but impaired	5.4	0.3%
Past due but not impaired	-	0.0%
Past due up to 90 days and impaired	37.5	2.3%
Past due after 90 days and impaired	33.5	2.1%
Gross	1,605.4	100.0%
Less: allowance for impairment	(39.9)	
Net	**1,565.5**	

Gross amounts of loans and advances to customers that were past due up to 90 days and impaired were as follows:

	£million
31 December 2017 (IAS 39 basis)	
Past due up to 30 days	24.4
Past due 30 - 60 days	8.5
Past due 60 - 90 days	4.6
Total	**37.5**

Gross amounts of loans and advances to customers that were past due but not impaired were as follows:

	£million
31 December 2017 (IAS 39 basis)	
Past due up to 30 days	-
Past due 30 - 60 days	-
Total	-

30.1 Concentration risk

Management assesses the potential concentration risk from geographic, product and individual loan concentration. Due to the nature of the Group's lending operations the directors consider the lending operations of the Group as a whole to be well diversified. Details of the Group's loan and advances to customers and loan commitments by product is provided in Note 3.

Geographical concentration

The Group's Real Estate Finance and Consumer Mortgages are secured against UK property only. The Directors consider that the key risk is the location of the security, rather than location of the borrower. Accordingly, the geographical concentration of these business loans and advances to customer, for 2018, has been presented by location of the security as follows:

Group and Company

	Real Estate Finance £million	Consumer Mortgages £million
31 December 2018		
Central England	35.1	16.2
Greater London	451.5	12.2
Northern England	37.6	16.6
South East England (excl. Greater London)	209.0	26.3
South West England	9.6	9.3
Scotland, Wales and Northern Ireland	27.6	4.3
Gross loans and receivables	770.4	84.9
Allowance for impairment	(0.1)	(0.2)
Total	**770.3**	**84.7**

The geographical concentration of these business loans and advances to customer at 31 December 2017, by location of the borrower, is set out below:

	Real Estate Finance £million	Consumer Mortgages £million
31 December 2017		
Central England	6.8	2.1
Greater London	384.2	4.1
Northern England	12.1	2.1
Scotland	-	-
South East England (excl. Greater London)	154.9	5.2
South West England	3.3	1.9
Wales and Northern Ireland	-	1.1
Other	19.8	-
Gross loans and receivables	581.1	16.5

Allowance for impairment	(0.3)	-
Total	**580.8**	**16.5**

30.2 Forbearance

At year end, all customers within the Group's Consumer Mortgage business were up to date with their monthly payments. Should customers face financial difficulties, the Group may, depending on individual circumstances, offer customers one of a number of forbearance options. The types of forbearance the Group may be prepared to offer include the following:

- Temporary interest only concessions are offered to customers in financial difficulty on a temporary basis with formal periodic review. The concession allows the customer to reduce monthly payments to cover interest only, and if made, the arrears status will not increase.
- Arrangement payment plans are agreed to enable customers to reduce their arrears balances by an agreed amount per month which is paid in addition to their standard monthly repayment.
- Payment concessions can be agreed on a temporary basis whereby the customer may pay less than the contractual monthly payment, in line with their individual affordability. If a customer is within this type of concession, their arrears position will increase.
- In exceptional circumstances, capitalisations of arrears may occur or an interest rate adjustment may be applied. These are used under strict controls, explicitly where the customer circumstances offer no other option.

All forbearance arrangements are formally discussed and agreed with the customer. By offering customers in financial difficulty the option of forbearance the Group potentially exposes itself to an increased level of risk through prolonging the period of non-contractual payment and/or potentially placing the customer into a detrimental position at the end of the forbearance period.

All forbearance arrangements are reviewed and monitored regularly to assess the ongoing potential risk, suitability and sustainability to the Group.

Where forbearance measures are not possible or are considered not to be in the customer's best interests, or where such measures have been tried and the customer has not adhered to the forbearance terms that have been agreed, the Bank will consider realising its security and taking possession of the property in order to sell it and clear the outstanding debt.

Other than Consumer Mortgages, the Group does not routinely reschedule contractual arrangements where customers default on their repayments. It may offer the customer the option to reduce or defer payments for a short period, in which cases the loan will retain the normal contractual payment due dates and will be treated the same as any other defaulting cases for impairment purposes. Arrears tracking will continue on the account with any impairment charge being based on the original contractual due dates for all products.

31. Market risk

Market risks arise from open positions in interest rate and currency products, all of which are exposed to general and specific market movements. There are no significant exposures to foreign currencies and therefore there is no significant currency risk. The Group does not operate a trading book.

31.1 Interest rate risk

Group and Company

Interest rate risk is the risk of potential loss through unhedged or mismatched asset and liability positions, which are sensitive to changes in interest rates. When interest rates change, the present value and timing of future cash flows change. This in turn changes the underlying value of the Group's assets, liabilities and off-balance sheet instruments and hence its economic value. Changes in interest rates also affect the Group's earnings by altering interest sensitive income and expenses, affecting its net interest income.

The Group seeks to 'match' interest rate risk on either side of the statement of financial position. However, this is not a perfect match and interest rate risk is present on the mismatch between fixed rate loans and savings products and variable rate assets and liabilities.

The Group monitors the interest rate mismatch on at least a monthly basis. The main test employed is a 200bps interest rate shock across all interest indices on a parallel basis. The Group maintained such exposures within the risk appetite set by the Board throughout the year.

The Group measures primarily Earnings at Risk, Market Rate Sensitivity and Economic Value of Equity, through monitoring an interest rate sensitivity gap. Interest rate risks inherent in new products or through changes to the terms and conditions of existing products were assessed over the course of the year.

This potential exposure is managed by the Group Treasury function and overseen by ALCO. The policy is not to take significant unmatched positions.

31.2 Interest rate sensitivity gap

The following tables summarise the re-pricing periods for the assets and liabilities in the Company and Group. Items are allocated to time bands by reference to the earlier of the next contractual interest rate re-price and the maturity date.

Group

	Within 3 months	More than 3 months but less than 6 months	More than 6 months but less than 1 year	More than 1 year but less than 5 years	More than 5 years	Non interest bearing	Total
	£million	£million	£million	£million	£million	£million	£million
As at 31 December 2018							
ASSETS							
Cash and balances at central banks	169.7	-	-	-	-	-	169.7
Loans and advances to banks	44.8	-	-	-	-	-	44.8
Debt securities	-	149.7	-	-	-	-	149.7
Loans and advances to customers	719.6	119.4	196.1	954.8	5.4	33.6	2,028.9
Other assets	-	-	-	-	-	51.2	51.2
Total assets	**934.1**	**269.1**	**196.1**	**954.8**	**5.4**	**84.8**	**2,444.3**
LIABILITIES AND EQUITY							
Due to banks	263.0	-	-	-	-	0.5	263.5
Deposits from customers	640.2	94.9	281.5	820.1	11.0	-	1,847.7
Subordinated liabilities	-	-	-	50.0	-	0.4	50.4
Other liabilities	-	-	-	-	-	45.6	45.6
Equity	-	-	-	-	-	237.1	237.1
Total liabilities and equity	**903.2**	**94.9**	**281.5**	**870.1**	**11.0**	**283.6**	**2,444.3**
Interest rate sensitivity gap	**30.9**	**174.2**	**(85.4)**	**84.7**	**(5.6)**	**(198.8)**	
Cumulative gap	**30.9**	**205.1**	**119.7**	**204.4**	**198.8**	**-**	

	Within 3 months	More than 3 months but less than 6 months	More than 6 months but less than 1 year	More than 1 year but less than 5 years	More than 5 years	Non interest bearing	Total
	£million	£million	£million	£million	£million	£million	£million
As at 31 December 2017							
ASSETS							
Cash and balances at central banks	226.1	-	-	-	-	-	226.1
Loans and advances to banks	34.3	-	-	-	-	-	34.3
Debt securities	5.0	-	-	-	-	-	5.0
Loans and advances to customers	581.2	121.3	181.9	696.0	2.3	15.6	1,598.3
Other assets	-	-	-	-	-	27.9	27.9
Total assets	**846.6**	**121.3**	**181.9**	**696.0**	**2.3**	**43.5**	**1,891.6**
LIABILITIES AND EQUITY							
Due to banks	113.0	-	-	-	-	-	113.0
Deposits from customers	577.2	28.2	269.9	581.4	6.5	20.0	1,483.2

Other liabilities	-	-	-	-	-	46.3	46.3
Equity	-	-	-	-	-	249.1	249.1
Total liabilities and equity	**690.2**	**28.2**	**269.9**	**581.4**	**6.5**	**315.4**	**1,891.6**
Interest rate sensitivity gap	**156.4**	**93.1**	**(88.0)**	**114.6**	**(4.2)**	**(271.9)**	
Cumulative gap	**156.4**	**249.5**	**161.5**	**276.1**	**271.9**	**-**	

Company

	Within 3 months £million	More than 3 months but less than 6 months £million	More than 6 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million	Non interest bearing £million	Total £million
As at 31 December 2018							
ASSETS							
Cash and balances at central banks	169.7	-	-	-	-	-	169.7
Loans and advances to banks	41.9	-	-	-	-	-	41.9
Debt securities	-	149.7	-	-	-	-	149.7
Loans and advances to customers	714.1	118.3	194.1	948.4	5.4	-	1,980.3
Other assets	-	-	-	-	-	91.4	91.4
Total assets	**925.7**	**268.0**	**194.1**	**948.4**	**5.4**	**91.4**	**2,433.0**
LIABILITIES AND EQUITY							
Due to banks	263.0	-	-	-	-	0.5	263.5
Deposits from customers	640.2	94.9	281.5	820.1	11.0	-	1,847.7
Subordinated liabilities	-	-	-	50.0	-	0.4	50.4
Other liabilities	-	-	-	-	-	54.0	54.0
Equity	-	-	-	-	-	217.4	217.4
Total liabilities and equity	**903.2**	**94.9**	**281.5**	**870.1**	**11.0**	**272.3**	**2,433.0**
Interest rate sensitivity gap	**22.5**	**173.1**	**(87.4)**	**178.3**	**(5.6)**	**(180.9)**	
Cumulative gap	**22.5**	**195.6**	**108.2**	**186.5**	**180.9**	**-**	

	Within 3 months £million	More than 3 months but less than 6 months £million	More than 6 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million	Non interest bearing £million	Total £million
As at 31 December 2017							
ASSETS							
Cash and balances at central banks	226.1	-	-	-	-	-	226.1
Loans and advances to banks	32.3	-	-	-	-	-	32.3
Debt securities	5.0	-	-	-	-	-	5.0
Loans and advances to customers	576.6	119.2	178.3	689.1	2.3	-	1,565.5
Other assets	-	-	-	-	-	52.1	52.1
Total assets	**840.0**	**119.2**	**178.3**	**689.1**	**2.3**	**52.1**	**1,881.0**
LIABILITIES AND EQUITY							
Due to banks	113.0	-	-	-	-	-	113.0
Deposits from customers	577.2	28.2	269.9	581.4	6.5	20.0	1,483.2
Other liabilities	-	-	-	-	-	47.7	47.7
Equity	-	-	-	-	-	237.1	237.1
Total liabilities and equity	**690.2**	**28.2**	**269.9**	**581.4**	**6.5**	**304.8**	**1,881.0**
Interest rate sensitivity gap	**149.8**	**91.0**	**(91.6)**	**107.7**	**(4.2)**	**(252.7)**	
Cumulative gap	**149.8**	**240.8**	**149.2**	**256.9**	**252.7**	**-**	

32. Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

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

The Company has a formal governance structure in place to manage and mitigate liquidity risk on a day to day basis. The Board sets and approves the Company's liquidity risk management strategy. The ALCO, comprising senior executives of the Company, monitors liquidity risk. Key liquidity risk management information is reported by the Treasury function and monitored by the Chief Executive Officer and Chief Financial Officer on a daily basis. The ALCO meets monthly to review liquidity risk against set thresholds and risk indicators including early warning indicators, liquidity risk tolerance levels and ILAAP metrics.

The Company raised fixed rate deposit bonds during the year as set out below:

	2018	2017
Amount	£448.4 million	£347.9 million
Term	1 to 7 years	1 to 5 years

These were issued to broadly match the term lending by the Company.

The PRA requires a firm to maintain at all times liquidity resources which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due. There is also a requirement that a firm ensures its liquidity resources contain an adequate buffer of high quality, unencumbered assets (i.e. Government Securities in the liquidity asset buffer); and it maintains a prudent funding profile. The liquidity assets buffer is a pool of highly liquid assets that can be called upon to create sufficient liquidity to meet liabilities on demand, particularly in a period of liquidity stress. The liquidity resources outside the buffer must either be marketable assets with a demonstrable secondary market that the firm can access, or a credit facility that can be activated in times of stress.

The Group has a Board approved ILAAP. The ILAAP rules require the Group to identify, measure, manage and monitor liquidity and funding risks across different time horizons and stress scenarios, consistent with the Group's risk appetite as established by the Board. The ILAAP seeks to document the Group's approach to liquidity and funding, and demonstrate that it complies with the Overall Liquidity Adequacy Rule. The PRA's approach to liquidity supervision is based on the principle that a firm must have adequate levels of liquidity resources and a prudent funding profile, and that it comprehensively manages and controls liquidity and funding risks. The liquidity buffer required by the ILAAP has been put in place and maintained since that time. Liquidity resources outside of the buffer are made up of deposits placed at the Bank of England. The ILAAP is updated annually.

The primary measures used by management to assess the adequacy of liquidity is the Overall Liquidity Adequacy Rule, which is the Board's own view of the Group's liquidity needs as set out in the Board approved ILAAP. The Group maintained liquidity in excess of the Overall Liquidity Adequacy Rule throughout the year ended 31 December 2018.

The LCR regime has applied to the Group from 1 October 2016, requiring management of net 30 day cash outflows as a proportion of High Quality Liquid Assets. The Group has set a more prudent internal limit. The actual LCR has significantly exceeded both limits throughout the year.

The Group is exposed to daily calls on its available cash resources from maturing deposits and loan draw-downs. The Group maintains significant cash resources to meet all of these needs as they fall due.

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Group. It is unusual for banks to be completely matched, as transacted business is often of uncertain term and of different types.

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

The tables below analyse the contractual undiscounted cash flows for the financial liabilities and assets into relevant maturity groupings:

Group

	Carrying amount £million	Gross nominal inflow/ (outflow) £million	Not more than 3 months £million	More than 3 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million
At 31 December 2018						
Non-derivative financial liabilities						
Due to banks	(263.5)	(263.5)	(263.5)	-	-	-
Deposits from customers	(1,847.7)	(1,916.3)	(644.3)	(404.7)	(855.8)	(11.5)
Other financial liabilities	(26.3)	(26.3)	(26.3)	-	-	-
Subordinated liabilities	(50.4)	(66.9)	(0.8)	(2.5)	(63.6)	-
	(2,187.9)	**(2,273.0)**	**(934.9)**	**(407.2)**	**(919.4)**	**(11.5)**
Non-derivative financial assets						
Cash and balances at central banks	169.7	169.7	169.7	-	-	-
Loans and advances to banks	44.8	44.8	44.8	-	-	-
Debt securities	149.7	149.7	149.7	-	-	-
Loans and advances to customers	2,028.9	2,476.4	841.1	523.8	1,110.1	1.4
Other financial assets	16.1	16.1	16.1	-	-	-
	2,409.2	**2,856.7**	**1,221.4**	**523.8**	**1,110.1**	**1.4**
Liquidity mismatch	**221.3**	**583.7**	**286.5**	**116.6**	**190.7**	**(10.1)**

	Carrying amount £million	Gross nominal inflow/ (outflow) £million	Not more than 3 months £million	More than 3 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million
At 31 December 2017						
Non-derivative financial liabilities						
Due to banks	(113.0)	(115.1)	(0.1)	(0.4)	(114.6)	-
Deposits from customers	(1,483.2)	(1,517.2)	(580.8)	(318.6)	(611.1)	(6.7)
Other financial liabilities	(29.5)	(29.5)	(29.5)	-	-	-
	(1,625.7)	**(1,661.8)**	**(610.4)**	**(319.0)**	**(725.7)**	**(6.7)**
Non-derivative financial assets						
Cash and balances at central banks	226.1	226.1	226.1	-	-	-
Loans and advances to banks	34.3	34.3	34.3	-	-	-
Debt securities	5.0	5.0	5.0	-	-	-
Loans and advances to customers	1,598.3	2,054.4	667.8	420.8	965.3	0.5
Other financial assets	1.2	1.2	1.2	-	-	-
	1,864.9	**2,321.0**	**934.4**	**420.8**	**965.3**	**0.5**
Liquidity mismatch	**239.2**	**659.2**	**324.0**	**101.8**	**239.6**	**(6.2)**

Company

	Carrying amount £million	Gross nominal inflow/ (outflow) £million	Not more than 3 months £million	More than 3 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million
At 31 December 2018						
Non-derivative financial liabilities						
Due to banks	(263.5)	(263.5)	(263.5)	-	-	-
Deposits from customers	(1,847.7)	(1,916.3)	(644.3)	(404.7)	(855.8)	(11.5)
Other financial liabilities	(37.4)	(37.4)	(37.4)	-	-	-
Subordinated liabilities	(50.4)	(66.9)	(0.8)	(2.5)	(63.6)	-

	(2,199.0)	**(2,284.1)**	**(946.0)**	**(407.2)**	**(919.4)**	**(11.5)**
Non-derivative financial assets						
Cash and balances at central banks	169.7	169.7	169.7	-	-	-
Loans and advances to banks	41.9	41.9	41.9	-	-	-
Debt securities	149.7	149.7	149.7	-	-	-
Loans and advances to customers	1,980.3	2,427.1	801.3	519.2	1,105.2	1.4
Other financial assets	60.6	16.1	16.1	-	-	-
	2,402.2	**2,804.5**	**1,178.7**	**519.2**	**1,105.2**	**1.4**
Liquidity mismatch	**203.2**	**520.4**	**232.7**	**112.0**	**185.8**	**(10.1)**

	Carrying amount £million	Gross nominal inflow/ (outflow) £million	Not more than 3 months £million	More than 3 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million
At 31 December 2017						
Non-derivative financial liabilities						
Due to banks	(113.0)	(115.1)	(0.1)	(0.4)	(114.6)	-
Deposits from customers	(1,483.2)	(1,517.2)	(580.8)	(318.6)	(611.1)	(6.7)
Other financial liabilities	(34.2)	(34.2)	(34.2)	-	-	-
	(1,630.4)	**(1,666.5)**	**(615.1)**	**(319.0)**	**(725.7)**	**(6.7)**
Non-derivative financial assets						
Cash and balances at central banks	226.1	226.1	226.1	-	-	-
Loans and advances to banks	32.3	32.3	32.3	-	-	-
Debt securities	5.0	5.0	5.0	-	-	-
Loans and advances to customers	1,565.5	2,017.5	646.6	413.1	957.3	0.5
Other financial assets	30.7	30.7	30.7	-	-	-
	1,859.6	**2,311.6**	**940.7**	**413.1**	**957.3**	**0.5**
Liquidity mismatch	**229.2**	**645.1**	**325.6**	**94.1**	**231.6**	**(6.2)**

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

Other financial liabilities, as shown above, do not include non-interest accruals as these are not classed as financial liabilities.

33. Capital risk

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

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

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted a 'Pillar 1 plus' approach to determine the level of capital the Group needs to hold. This method takes the Pillar 1 capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations delivers a sufficient capital sum adequate to cover management's view of anticipated risks. Where it is considered that the Pillar 1 calculations do not reflect the risk, an additional capital add-on in Pillar 2 should be applied, in line with the Total Capital Requirement issued by the PRA.

Pillar 3 complements the minimum capital requirements (Pillar 1) and the supervisory review process (Pillar 2). Its aim is to encourage market discipline by developing a set of disclosure requirements which would allow market

participants to assess key pieces of information on a firm's capital, risk exposures and risk assessment processes. Pillar 3 disclosures for the Group for the year ended 31 December 2018 are published as a separate document on the Group's website.

The following table, which is unaudited, shows the regulatory capital resources for the Group. The Group has elected to adopt the IFRS 9 transitional rules. For 2018 this allowed 95% of the initial IFRS 9 transition adjustment, net of attributable deferred tax, to be added back to eligible Tier 1 capital. Tier 2 capital comprises solely subordinated debt issued during the year net of unamortised issue costs and excluding accrued interest, capped at 25% of the capital requirement. At 31 December 2017, Tier 2 capital comprised the collective allowance for loan impairment. Under IFRS 9, there is no longer a collective allowance.

	2018 £million (unaudited)	2017 £million (unaudited)
Tier 1		
Share capital	7.4	7.4
Share premium	81.2	81.2
Retained earnings	147.4	159.2
Revaluation reserve	1.1	1.3
IFRS 9 transition adjustment	24.5	-
Goodwill	(1.0)	(1.0)
Intangible assets net of attributable deferred tax	(8.8)	(9.2)
CET1 capital	**251.8**	**238.9**
Tier 2		
Subordinated liabilities	50.4	-
Less ineligible portion	(4.7)	-
Collective allowance for impairment of loans and advances	-	4.4
Total Tier 2 capital	**45.7**	**4.4**
Own Funds	**297.5**	**243.3**
Reconciliation to total equity:		
IFRS 9 transition adjustment	(24.5)	-
Eligible subordinated liabilities	(45.7)	-
Goodwill and other intangible assets net of attributable deferred tax	9.8	10.2
Collective allowance for impairment of loans and advances	-	(4.4)
Total equity	**237.1**	**249.1**

The Group ICAAP includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. The PRA sets a Total Capital Requirement ('TCR') for each UK bank calibrated by reference to its Capital Resources Requirement, which is broadly equivalent to 8% of risk weighted assets and thus representing the capital required under Pillar 1 of the Basel III framework. The ICAAP is a key input into the PRA's TCR setting process, which addresses the requirements of Pillar 2 of the Basel II framework. The PRA's approach is to monitor the available capital resources in relation to the TCR. The Group maintains an extra internal buffer and capital ratios are reviewed on a monthly basis to ensure that external and internal requirements are adhered to. The PRA reviewed the Group's ICAAP in 2017 and issued its updated TCR in March 2018.
The Group is also subject to further capital requirements imposed by the PRA on all financial services firms. During the periods, the Group complied with these requirements.

The Group raised Tier 2 capital in 2018. Further details of the capital issuance are given in Note 24.

34. Maturity analysis of consolidated assets and liabilities

Group

	Due within one year £million	Due after more than one year £million	No contractual maturity £million	Total £million
Contractual maturity analysis at 31 December 2018				

ASSETS				
Cash and balances at central banks	169.7	-	-	169.7
Loans and advances to banks	44.8	-	-	44.8
Loans and advances to customers	1,035.1	960.2	33.6	2,028.9
Debt securities	149.7	-	-	149.7
Property, plant and equipment	-	-	11.0	11.0
Intangible assets	-	-	9.9	9.9
Deferred tax assets	-	-	7.9	7.9
Other assets	-	-	22.4	22.4
Total assets	**1,399.3**	**960.2**	**84.8**	**2,444.3**
LIABILITIES				
Due to banks	263.5	-	-	263.5
Deposits from customers	1,016.6	831.1	-	1,847.7
Current tax liabilities	4.2	-	-	4.2
Other liabilities	-	-	40.1	40.1
Provisions for liabilities and charges	-	-	1.3	1.3
Subordinated liabilities	1.2	50.0	(0.8)	50.4
Total liabilities	**1,285.5**	**881.1**	**40.6**	**2,207.2**

	Due within one year £million	Due after more than one year £million	No contractual maturity £million	Total £million
Contractual maturity analysis at 31 December 2017				
ASSETS				
Cash and balances at central banks	226.1	-	-	226.1
Loans and advances to banks	34.3	-	-	34.3
Loans and advances to customers	884.4	698.3	15.6	1,598.3
Debt securities	5.0	-	-	5.0
Property, plant and equipment	-	-	11.5	11.5
Intangible assets	-	-	10.4	10.4
Deferred tax assets	-	-	0.6	0.6
Other assets	-	-	5.4	5.4
Total assets	**1,149.8**	**698.3**	**43.5**	**1,891.6**
LIABILITIES				
Due to banks	113.0	-	-	113.0
Deposits from customers	875.3	587.9	20.0	1,483.2
Current tax liabilities	3.0	-	-	3.0
Other liabilities	-	-	41.9	41.9
Provisions for liabilities and charges	-	-	1.4	1.4
Total liabilities	**991.3**	**587.9**	**63.3**	**1,642.5**

The directors have reviewed behavioural maturity of the loan book and have concluded that it would not significantly affect the analysis above.

Company

	Due within one year £million	Due after more than one year £million	No contractual maturity £million	Total £million
Contractual maturity analysis at 31 December 2018				
ASSETS				
Cash and balances at central banks	169.7	-	-	169.7
Loans and advances to banks	41.9	-	-	41.9
Loans and advances to customers	1,026.5	953.8	-	1,980.3
Debt securities	149.7	-	-	149.7
Property, plant and equipment	-	-	6.0	6.0
Intangible assets	-	-	8.1	8.1
Investments	-	-	3.9	3.9
Deferred tax assets	-	-	7.8	7.8

Other assets	-	-	65.6	65.6
Total assets	**1,387.8**	**953.8**	**91.4**	**2,433.0**
LIABILITIES				
Due to banks	263.5	-	-	263.5
Deposits from customers	1,016.6	831.1	-	1,847.7
Current tax liabilities	3.6	-	-	3.6
Other liabilities	-	-	49.1	49.1
Provisions for liabilities and charges	-	-	1.3	1.3
Subordinated liabilities	1.2	50.0	(0.8)	50.4
Total liabilities	**1,284.9**	**881.1**	**49.6**	**2,215.6**

	Due within one year £million	Due after more than one year £million	No contractual maturity £million	Total £million
Contractual maturity analysis at 31 December 2017				
ASSETS				
Cash and balances at central banks	226.1	-	-	226.1
Loans and advances to banks	32.3	-	-	32.3
Loans and advances to customers	874.1	691.4	-	1,565.5
Debt securities	5.0	-	-	5.0
Property, plant and equipment	-	-	6.1	6.1
Intangible assets	-	-	8.5	8.5
Investments	-	-	3.7	3.7
Deferred tax assets	-	-	0.6	0.6
Other assets	-	-	33.2	33.2
Total assets	**1,137.5**	**691.4**	**52.1**	**1,881.0**
LIABILITIES				
Due to banks	113.0	-	-	113.0
Deposits from customers	875.3	587.9	20.0	1,483.2
Current tax liabilities	1.9	-	-	1.9
Other liabilities	-	-	44.4	44.4
Provisions for liabilities and charges	-	-	1.4	1.4
Total liabilities	**990.2**	**587.9**	**65.8**	**1,643.9**

The directors have reviewed behavioural maturity of the loan book and have concluded that it would not significantly affect the analysis above.

35. Classification of financial assets and liabilities

Group

	Total carrying amount £million	Fair value £million	Fair value hierarchy level
At 31 December 2018 (IFRS 9 basis)			
Cash and balances at central banks	169.7	169.7	Level 1
Loans and advances to banks	44.8	44.8	Level 2
Loans and advances to customers	2,028.9	2,032.5	Level 3
Debt securities	149.7	149.7	Level 1
Other financial assets	16.2	16.2	Level 3
	2,409.3	**2,412.9**	
Due to banks	263.5	263.5	Level 2
Deposits from customers	1,847.7	1,859.7	Level 3
Other financial liabilities	26.3	26.3	Level 3
Subordinated liabilities	50.4	50.4	Level 2
	2,187.9	**2,199.9**	

	Debt securities	Loans and receivables	Other financial assets and liabilities	Total carrying amount	Fair value	Fair value hierarchy level

	£million	£million	£million	£million	£million	
At 31 December 2017 (IAS 39 basis)						
Cash and balances at central banks	-	226.1	-	226.1	226.1	Level 1
Loans and advances to banks	-	34.3	-	34.3	34.3	Level 2
Loans and advances to customers	-	1,598.3	-	1,598.3	1,641.1	Level 3
Debt securities	5.0	-	-	5.0	5.0	Level 1
Other financial assets	-	-	1.2	1.2	1.2	Level 3
	5.0	**1,858.7**	**1.2**	**1,864.9**	**1,907.7**	
Due to banks	-	-	113.0	113.0	113.0	Level 2
Deposits from customers	-	-	1,483.2	1,483.2	1,481.6	Level 3
Other financial liabilities	-	-	29.5	29.5	29.5	Level 3
	-	**-**	**1,625.7**	**1,625.7**	**1,624.1**	

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

Company

	Total carrying amount £million	Fair value £million	Fair value hierarchy level
At 31 December 2018 (IFRS 9 basis)			
Cash and balances at central banks	169.7	169.7	Level 1
Loans and advances to banks	41.9	41.9	Level 2
Loans and advances to customers	1,980.3	1,983.9	Level 3
Debt securities	149.7	149.7	Level 1
Other financial assets	60.6	60.6	Level 3
	2,402.2	**2,405.8**	
Due to banks	263.5	263.5	Level 2
Deposits from customers	1,847.7	1,859.7	Level 3
Other financial liabilities	37.4	37.4	Level 3
Subordinated liabilities	50.4	50.4	Level 2
	2,199.0	**2,211.0**	

	Debt securities £million	Loans and receivables £million	Other financial assets and liabilities £million	Total carrying amount £million	Fair value £million	Fair value hierarchy level
At 31 December 2017 (IAS 39 basis)						
Cash and balances at central banks	-	226.1	-	226.1	226.1	Level 1
Loans and advances to banks	-	32.3	-	32.3	32.3	Level 2
Loans and advances to customers	-	1,565.5	-	1,565.5	1,608.3	Level 3
Debt securities	5.0	-	-	5.0	5.0	Level 1
Other financial assets	-	-	30.7	30.7	30.7	Level 3
	5.0	**1,823.9**	**30.7**	**1,859.6**	**1,902.4**	
Due to banks	-	-	113.0	113.0	113.0	Level 2
Deposits from customers	-	-	1,483.2	1,483.2	1,481.6	Level 3
Other financial liabilities	-	-	34.2	34.2	34.2	Level 3
	-	-	**1,630.4**	**1,630.4**	**1,628.8**	

All 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.

Fair value classification

The tables above include the fair values and fair value hierarchies of the Group and Company's financial assets and liabilities. 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).
- Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

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.

Debt securities

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

At the end of December 2018 the fair value of debt securities was calculated to be equivalent to their carrying value.

Due to 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.

Dividends and other financial liabilities

The fair value of dividends and 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 dividends and 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.

36. Related party transactions

Related parties of the Company and Group include subsidiaries, Key Management Personnel, close family members of Key Management Personnel and entities which are controlled, jointly controlled or significantly influenced, or for which significant voting power is held, by Key Management Personnel or their close family members.

A number of banking transactions are entered into with related parties in the normal course of business on normal commercial terms. These include loans and deposits as set out below. Except for the directors' disclosures, there were no other Key Management Personnel disclosures, therefore the tables below relate to directors and close members of their family only.

	Directors	
	2018	2017
	£million	£million
Loans		
Loans outstanding at 1 January	3.7	3.2
Loans advanced	0.4	0.4
Interest applied	0.1	0.1
Loans outstanding at 31 December	**4.2**	**3.7**
Deposits		
Deposits outstanding at 1 January	0.4	0.3
Additional deposits made during the year	-	0.1
Deposits outstanding at 31 December	**0.4**	**0.4**

The loans outstanding above comprise the following:

- A £0.4 million advance (2017: £0.4 million) as part of a £2.5 million facility agreed with a company in which a director holds 50% of the voting shares, which is secured by property and personal guarantees.
- A £3.8 million advance (2017: £3.3 million) as part of a revised £4.4 million facility agreed with a director, which is secured by property and certain other undertakings.

Both of these transactions were agreed by the Group’s Real Estate Finance business and arose during the normal course of business. Both loans were subject to the usual Board governance and Credit Committee approval procedures and are on substantially the same terms as for comparable transactions with third parties.

The Company undertook the following transactions with other companies in the Secure Trust Bank Group:

	2018	2017
	£million	£million
Debt Managers (Services) Limited - income from sale of debt portfolio	(0.2)	(0.3)
Debt Managers (Services) Limited - debt collection services	1.0	0.2
Secure Homes Services Limited - building rental paid	0.4	0.4
V12 Finance Group Limited - dividend received	-	(13.9)
V12 Retail Finance Limited - fees and commission	21.4	20.8
	22.6	**7.2**

During the year, the basis of the fees and commission charged by V12 Retail Finance Limited was changed. A breakdown of the charges is set out below:

	2018	2017
	£million	£million
Fees and commission		
Loan management services	14.9	-
Sales commission	6.5	-
Financial intermediary charges		
Applications proposed	-	5.1
Applications accepted	-	2.3
Loan set-up and processing	-	4.5
Loan book management and servicing fees	-	8.9
	21.4	**20.8**

The loans and advances with, and amounts receivable and payable to, related companies are noted below:

	Company 2018 £million	Company 2017 £million
Amounts receivable from subsidiary undertakings	44.5	29.7
Amounts due to subsidiary undertakings	(14.1)	(9.7)
	30.4	**20.0**

Directors' remuneration

The directors' emoluments (including pension contributions and benefits in kind) for the year are disclosed in the Directors' Remuneration Report beginning on page 97.

At the year end the ordinary shares held by the directors are disclosed in the Directors' Report beginning on page 114. Details of the directors' holdings of share options, as well as details of those share options exercised during the year, are also disclosed in the Directors' Report.

37. Immediate parent company and ultimate controlling party

The Company has had no immediate parent company or ultimate controlling party.

38. Implementation of IFRS 9

Group

The table below summarises the adjustments arising on adoption of IFRS 9 on the Group's balance sheet at 1 January 2018. There has been no change in the carrying amount of financial instruments on the basis of their measurement categories. All adjustments have arisen solely due to a replacement of the IAS 39 incurred loss impairment approach with an expected credit loss approach. The Group's classification and measurement and loss impairment accounting policies are provided in Note 1.

	IAS 39 measurement category	IFRS 9 measurement category	IAS 39 carrying amount £million	ECL adjustment £million	IFRS 9 carrying amount £million
At 1 January 2018					
ASSETS					
Cash and balances at central banks	Loans and receivables	Amortised cost	226.1	-	226.1
Loans and advances to banks	Loans and receivables	Amortised cost	34.3	-	34.3
Loans and advances to customers	Loans and receivables	Amortised cost	1,598.3	(31.8)	1,566.5
Debt securities	Held to maturity	Amortised cost	5.0	-	5.0
Property, plant and equipment	N/A	N/A	11.5	-	11.5
Intangible assets	N/A	N/A	10.4	-	10.4
Deferred tax asset	N/A	N/A	0.6	6.3	6.9
Other assets	N/A	N/A	5.4	-	5.4
Total assets			**1,891.6**	**(25.5)**	**1,866.1**
LIABILITIES AND EQUITY					
Due to banks	Other financial assets and liabilities	Amortised cost	113.0	-	113.0
Deposits from customers	Other financial assets and liabilities	Amortised cost	1,483.2	-	1,483.2
Current tax liabilities	N/A	N/A	3.0	-	3.0
Other liabilities	N/A	N/A	41.9	-	41.9
Provisions for liabilities and charges	N/A	N/A	1.4	0.3	1.7
Total liabilities			**1,642.5**	**0.3**	**1,642.8**
Equity attributable to owners of the parent					
Share capital	N/A	N/A	7.4	-	7.4
Share premium	N/A	N/A	81.2	-	81.2
Revaluation Reserve	N/A	N/A	1.3	-	1.3
Retained earnings	N/A	N/A	159.2	(25.8)	133.4

Total equity	**249.1**	**(25.8)**	**223.3**
Total liabilities and equity	**1,891.6**	**(25.5)**	**1,866.1**

The following table reconciles the Group's closing IAS 39 impairment allowance to the opening IFRS 9 allowance as at 1 January 2018:

	Closing IAS 39 balance at 31 December 2017	ECL adjustment	Opening IFRS 9 balance at 1 January 2018
	£million	£million	£million
Specific allowances for impairment	35.5	36.2	71.7
Collective allowances for impairment	4.4	(4.4)	-
Impairment against on balance sheet assets	**39.9**	**31.8**	**71.7**
Provision for loan commitments	-	0.3	0.3
Total impairment and provision	**39.9**	**32.1**	**72.0**

Total provisions above include expert credit judgements over the Group's IFRS 9 model results of £2.5 million, of which £1.2 million are specific overlays for the Business Finance portfolio.

An analysis of the Group's opening gross loans and advances to customers and ECL impairment allowance by IFRS 9 stage is provided below:

	Not credit impaired		Credit impaired			
	Stage 1: Subject to 12 month ECL	Stage 2: Subject to lifetime ECL	Stage 3: Excl. purchased credit impaired	Stage 3: Purchased credit impaired	Total	Provision cover
	£million	£million	£million	£million	£million	%
1 January 2018						
Gross loans and advances						
Business Finance						
Real Estate Finance	516.5	64.6	-	-	581.1	
Asset Finance	103.1	11.3	3.5	-	117.9	
Commercial Finance	125.4	1.2	0.5	-	127.1	
Consumer Finance						
Retail Finance	398.4	57.4	3.6	-	459.4	
Motor Finance	182.0	94.0	25.5	-	301.5	
Debt Management	-	-	7.8	7.8	15.6	
Consumer Mortgages	16.5	-	-	-	16.5	
Other	15.8	0.2	3.1	-	19.1	
Total on balance sheet	**1,357.7**	**228.7**	**44.0**	**7.8**	**1,638.2**	
Loan commitments	**178.6**	**-**	**-**	**-**	**178.6**	
ECL Impairment allowance						
Business Finance						
Real Estate Finance	0.1	-	-	-	0.1	0.0%
Asset Finance	0.3	0.1	1.0	-	1.4	1.2%
Commercial Finance	0.2	0.2	0.4	-	0.8	0.6%
Consumer Finance						
Retail Finance	6.8	7.4	3.1	-	17.3	3.8%
Motor Finance:						
ECL allowance	5.9	16.9	20.1	-	42.9	
Voluntary termination provision	5.6	-	-	-	5.6	
	11.5	16.9	20.1	-	48.5	16.1%
Debt Management	-	-	-	-	-	0.0%
Consumer Mortgages	-	-	-	-	-	0.0%
Other	-	0.3	3.3	-	3.6	18.8%
Impairment allowance against on balance sheet assets	**18.9**	**24.9**	**27.9**	**-**	**71.7**	**4.4%**
Provision for loan commitments	**0.3**	**-**	**-**	**-**	**0.3**	**0.2%**

Company

The table below summarises the adjustments arising on adoption of IFRS 9 on the Company's balance sheet at 1 January 2018. There has been no change in the carrying amount of financial instruments on the basis of their measurement categories. All adjustments have arisen solely due to a replacement of the IAS 39 incurred loss impairment approach with an expected credit loss approach.

	IAS 39 measurement category	IFRS 9 measurement category	IAS 39 carrying amount £million	ECL adjustment £million	IFRS 9 carrying amount £million
At 1 January 2018					
ASSETS					
Cash and balances at central banks	Loans and receivables	Amortised cost	226.1	-	226.1
Loans and advances to banks	Loans and receivables	Amortised cost	32.3	-	32.3
Loans and advances to customers	Loans and receivables	Amortised cost	1,565.5	(32.4)	1,533.1
Debt securities	Held to maturity	Amortised cost	5.0	-	5.0
Property, plant and equipment	N/A	N/A	6.1	-	6.1
Intangible assets	N/A	N/A	8.5	-	8.5
Investments	N/A	N/A	3.7	-	3.7
Deferred tax asset	N/A	N/A	0.6	6.4	7.0
Other assets	N/A	N/A	33.2	-	33.2
Total assets			**1,881.0**	**(26.0)**	**1,855.0**
LIABILITIES AND EQUITY					
Due to banks	Other financial assets and liabilities	Amortised cost	113.0	-	113.0
Deposits from customers	Other financial assets and liabilities	Amortised cost	1,483.2	-	1,483.2
Current tax liabilities	N/A	N/A	1.9	-	1.9
Other liabilities	N/A	N/A	44.4	-	44.4
Provisions for liabilities and charges	N/A	N/A	1.4	0.3	1.7
Total liabilities			**1,643.9**	**0.3**	**1,644.2**
Equity attributable to owners of the parent					
Share capital	N/A	N/A	7.4	-	7.4
Share premium	N/A	N/A	81.2	-	81.2
Revaluation Reserve	N/A	N/A	0.5	-	0.5
Retained earnings	N/A	N/A	148.0	(26.3)	121.7
Total equity			**237.1**	**(26.3)**	**210.8**
Total liabilities and equity			**1,881.0**	**(26.0)**	**1,855.0**

The following table reconciles the Company's closing IAS 39 impairment allowance to the opening IFRS 9 allowance as at 1 January 2018:

	Closing IAS 39 balance at 31 December 2017 £million	ECL adjustment £million	Opening IFRS 9 balance at 1 January 2018 £million
Specific allowances for impairment	35.5	36.8	72.3
Collective allowances for impairment	4.4	(4.4)	-
Impairment against on balance sheet assets	**39.9**	**32.4**	**72.3**
Provision for loan commitments	-	0.3	0.3
Total impairment and provision	**39.9**	**32.7**	**72.6**

Total provisions above include expert credit judgements over the Company's IFRS 9 model results of £2.5 million, of which £1.2 million are specific overlays for the Business Finance portfolio.

An analysis of the Company's opening gross loans and advances to customers and ECL impairment allowance by IFRS 9 stage is provided below:

	Not credit impaired		Credit impaired			
	Stage 1: Subject to 12 month ECL	Stage 2: Subject to lifetime ECL	Stage 3: Excl. purchased credit impaired	Stage 3: Purchased credit impaired	Total	Provision cover
	£million	£million	£million	£million	£million	%
1 January 2018						
Gross loans and advances						
Business Finance						
Real Estate Finance	516.5	64.6	-	-	581.1	
Asset Finance	103.1	11.3	3.5	-	117.9	
Commercial Finance	123.1	1.2	0.5	-	124.8	
Consumer Finance						
Retail Finance	398.4	57.4	3.6	-	459.4	
Motor Finance	182.0	94.0	25.5	-	301.5	
Consumer Mortgages	16.5	-	-	-	16.5	
Other	0.8	0.2	3.2	-	4.2	
Total on balance sheet	**1,340.4**	**228.7**	**36.3**		**1,605.4**	
Loan commitments	**178.5**	**-**	**-**	**-**	**178.5**	
ECL Impairment allowance						
Business Finance						
Real Estate Finance	0.1	-	-	-	0.1	0.0%
Asset Finance	0.3	0.1	1.0	-	1.4	1.2%
Commercial Finance	0.2	0.2	0.4	-	0.8	0.6%
Consumer Finance						
Retail Finance	6.8	7.5	3.2	-	17.5	3.8%
Motor Finance:						
ECL allowance	6.0	17.0	20.3	-	43.3	
Voluntary termination provision	5.6	-	-	-	5.6	
	11.6	17.0	20.3	-	48.9	16.2%
Consumer Mortgages	-	-	-	-	-	0.0%
Other	-	0.3	3.3	-	3.6	85.7%
Impairment allowance against on balance sheet assets	**19.0**	**25.1**	**28.2**	**-**	**72.3**	**4.5%**
Provision for loan commitments	**0.3**	**-**	**-**	**-**	**0.3**	**0.2%**

Group and Company

As set out in Note 1 for the Real Estate Finance and Commercial Finance portfolios, where a loan facility is agreed that includes both a drawn and undrawn element and the Group cannot identify the ECL on the loan commitment separately, a combined loss allowance for both the drawn and undrawn component of the loan is recognised as an impairment allowance and deducted from the gross carrying amount of the drawn component. At 1 January 2018 loan commitments held for the Real Estate Finance and Commercial Finance portfolios were £98.6 million and £35.5 million respectively.

39. Discontinued operations

On 21 December 2017, the Bank agreed to sell its remaining portfolio of unsecured personal loans to Alpha Credit Solutions 8 S.à.r.l., a company owned by AnaCap Credit Opportunities III LP. As previously highlighted, the Group made the decision to withdraw from the unsecured personal loan market in 2016, and the sale of this portfolio represents a full exit by the Group from this market.

The net proceeds of sale, after transaction costs, amounted to £36.6 million, which was used for general corporate purposes including other forms of lending. The cash purchase consideration for the portfolio was calculated based

on an agreed price for the portfolio as at 30 June 2017, adjusted for cash receipts the Group had already received from the portfolio during the period up to the date of completion.

The effect of the transaction is to accelerate capital realisation to reinvest into the Group's core business while removing any future credit risk associated with the portfolio. The profit arising on sale of the portfolio was £0.5 million before tax. The Group continued to administer the portfolio until the completion of a migration of the portfolio to a third party administrator appointed by the purchaser, which was completed in the first half of 2018.

Details of the income statement, net assets disposed of and consequential gain recognised on disposal, and cash flow of the discontinued operation are set out below:

Income statement	2017 £million
Interest income and similar income	8.0
Interest expense and similar charges	-
Net interest income	**8.0**
Fee and commission income	-
Fee and commission expense	-
Net fee and commission income	**-**
Operating income	**8.0**
Net impairment losses on loans and advances to customers	(3.4)
Operating expenses	(0.3)
Profit before income tax	**4.3**
Income tax expense	(0.8)
Profit after income tax	**3.5**
Gain recognized on disposal after tax (see below)	0.4
Profit for the period	**3.9**

As described in Note 3, funding costs and operating expenses are not aligned to operating segments for day to day management of the business, so they cannot be allocated on a reliable basis. Accordingly, funding costs are not included above, and operating expenses above relates only to those costs that are directly attributable to the discontinued business.

	Assets sold on 21 December 2017 £million
Net assets disposed of:	
Loans and advances to customers	36.1
Consideration	
Cash	37.1
Less selling costs	(0.5)
	36.6
Gain recognised on disposal before tax	**0.5**
Tax	(0.1)
Gain recognised on disposal after tax	**0.4**

Cash flow statement	Year ended 31 December 2017 £million
Cash flows from discontinued operations	
Cash flows from operating activities	
Profit for the year	3.5
Adjustments for:	
Income tax expense	0.8

Impairment losses on loans and advances to customers	3.4
Cash flows from operating profits before changes in operating assets and liabilities	7.7
Changes in operating assets and liabilities:	
- net decrease in loans and advances to customers	28.0
Net cash inflow from operating activities and net increase in cash and cash equivalents	**35.7**

Five year summary

	2018 £million	2017 £million	2016 £million	2015 £million	2014 £million
Profit for the year					
Interest and similar income	169.2	149.3	141.1	139.7	93.6
Interest expense and similar charges	(35.5)	(26.7)	(26.3)	(21.6)	(14.2)
Net interest income	**133.7**	**122.6**	**114.8**	**118.1**	**79.4**
Net fee and commission income	17.9	14.9	14.5	14.4	18.5
Operating income	**151.6**	**137.5**	**129.3**	**132.5**	**97.9**
Impairment losses on loans and advances	(32.4)	(36.9)	(30.3)	(24.3)	(15.3)
Arbuthnot Banking Group recharges	-	-	-	(0.8)	(0.2)
Operating expenses	(84.5)	(71.6)	(71.5)	(70.9)	(56.3)
Profit on sale of equity instruments available-for-sale	-	0.3	-	-	-
Profit before income tax	**34.7**	**29.3**	**27.5**	**36.5**	**26.1**

	2018 £million	2017 £million	2016 £million	2015 £million	2014 £million
Earnings per share for profit attributable to the equity holders of the Group during the year					
(expressed in pence per share)					
- basic	153.2	128.8	754.1	157.8	122.3

	2018 £million	2017 £million	2016 £million	2015 £million	2014 £million
Financial position					
Cash and balances at central banks	169.7	226.1	112.0	131.8	81.2
Loans and advances to banks	44.8	34.3	18.2	11.5	39.8
Loans and advances to customers	2,028.9	1,598.3	1,321.0	1,074.9	622.5
Debt securities	149.7	5.0	20.0	3.8	16.3
Other assets	51.2	27.9	38.8	25.4	22.5
Total assets	**2,444.3**	**1,891.6**	**1,510.0**	**1,247.4**	**782.3**
Due to banks	263.5	113.0	70.0	35.0	15.9
Deposits from customers	1,847.7	1,483.2	1,151.8	1,033.1	608.4
Subordinated liabilities	50.4	-	-	-	-
Other liabilities	45.6	46.3	52.2	38.1	33.1
Total shareholders' equity	237.1	249.1	236.0	141.2	124.9
Total liabilities and shareholders' equity	**2,444.3**	**1,891.6**	**1,510.0**	**1,247.4**	**782.3**

Appendix (unaudited)

Key performance indicators

All revenue, income, impairments, and expenses used in the calculations below are stated on a continuing operations basis.

(i) Margin ratios

Net interest margin is calculated as interest income and similar income less interest expense and similar charges for the financial period as a percentage of the average loan book, net revenue margin is calculated as operating income for the financial period as a percentage of the average loan book and gross revenue margin is calculated as interest income and similar income plus fee and commission income for the financial period as a percentage of the average loan book. The calculation of the average loan book is the average of the monthly balance of loans and advances to customers, net of provisions and discontinued operations, over thirteen months:

	2018	2017

	£million	£million
Net interest margin		
Interest income and similar income	169.2	141.3
Interest expense and similar charges	(35.5)	(26.7)
Net interest income	133.7	114.6
Net revenue margin		
Net interest income	133.7	114.6
Net fee and commission income	17.9	14.9
Operating income	151.6	129.5
Gross revenue margin		
Interest income and similar income	169.2	141.3
Fee and commission income	19.4	16.0
Gross revenue	188.6	157.3
Opening loan book (after IFRS 9 transition adjustment see Note (vi))	1,566.5	1,255.5
Closing loan book	2,028.9	1,598.3
Average loan book	1,818.2	1,418.1
Net interest margin	**7.4%**	**8.1%**
Net revenue margin	**8.3%**	**9.1%**
Gross revenue margin	**10.4%**	**11.1%**

A reconciliation of the loan book figures used above to the statement of financial position is as follows:

	2016 £million
Balance sheet loan book	1,321.0
PLD loans	(65.5)
	1,255.5

The margin ratios all measure the yield of the loan book.

(ii) Cost ratios

Cost of risk is calculated as impairment losses on loans and advances to customers for the financial period as a percentage of the average loan book, cost of funds is calculated at interest expense for the financial period as a percentage of average loan book and cost to income ratio is calculated as operating expenses for the financial period as a percentage of operating income for the financial period:

	2018 £million	2017 £million
Net impairment losses on loans and advances to customers	32.4	33.5
Average loan book	1,818.2	1,418.2
Cost of risk	**1.8%**	**2.4%**
Interest expense	35.5	26.7
Average loan book	1,818.2	1,418.2
Cost of funds	**2.0%**	**1.9%**
Operating expenses	84.5	71.3
Operating income	151.6	129.5
Cost to income ratio	**55.7%**	**55.1%**

The cost of risk measures how effective the Group has been in managing its impairment losses. The cost of funds measures the cost of money being lent to customers. The cost to income ratio measures how efficiently the Group is utilising its cost base in producing income.

(iii) Return ratios

Annualised adjusted return on average assets is calculated as the adjusted profit after tax for the previous 12 months as a percentage of average assets, annualised adjusted return on average equity is calculated as the adjusted profit after tax for the previous 12 months as a percentage of average equity and annualised adjusted

return on required equity is calculated as the adjusted profit after tax for the previous 12 months as a percentage of average required equity.

Adjusted profit after tax is profit after tax attributable to continuing operations, adjusted for items that are non-controllable items or other items that fall outside of the Group's core business activities. A reconciliation of adjusted profit after tax to statutory profit after tax is provided on page 17.

Average assets is calculated as the average of the monthly assets balances, net of discontinued operations, average equity is calculated as the average of the monthly equity balances and average required equity is calculated as the average of the monthly balances of total required equity. Total required equity is calculated as the equity required to achieve a CET1 ratio of 12%, excluding equity required against discontinued operations:

	2018 £million	2017 £million
Adjusted profit after tax	29.9	21.5
Opening assets (after IFRS 9 transition adjustment – see below)	1,866.1	1,444.5
Closing assets	2,444.3	1,891.6
Average assets	2,182.4	1,639.9
Opening equity	223.3	236.0
Closing equity	237.1	249.1
Average equity	228.9	242.0
Opening required equity	173.3	146.1
Closing required equity	220.9	173.3
Average required equity	201.7	159.8
Annualised adjusted return on average assets	**1.4%**	**1.3%**
Annualised adjusted return on average equity	**13.1%**	**8.9%**
Annualised adjusted return on required equity	**14.8%**	**13.5%**

A reconciliation of assets to the balance sheet is as follows:

	2018 (opening balance) £million	2016 £million
Balance sheet assets	1,891.6	1,510.0
PLD assets	-	(65.5)
IFRS 9 transition adjustment	(25.5)	-
	1,866.1	**1,444.5**

A reconciliation of equity to the balance sheet is as follows:

	2018 (opening balance) £million
Equity	249.1
IFRS 9 transition adjustment	(25.8)
	223.3

Return on average assets demonstrates how profitable the Group's assets are in generating revenue. Return on average equity is a measure of the Group's ability to generate profit from the equity available to it. Return on required equity relates profitability to the capital that the Group is required to hold.

(iv) Funding ratios

The loan to deposit ratio is calculated as the loan book, net of discontinued operations, at the year end, divided by deposits from customers at the year end, and the total funding ratio is calculated as the total funding at the year end, being the sum of deposits from customers, borrowings under the Term Funding Scheme, and equity, divided by the loan book, net of discontinued operations, at the year end:

	2018 £million	2017 £million
Loan book	2,028.9	1,598.3
Deposits from customers	1,847.7	1,483.2
Borrowings under the Term Funding Scheme	263.5	113.0
Tier 2 capital (including accrued interest)	50.4	-
Equity	237.1	249.1
Total funding	2,398.7	1,845.3
Loan to deposit ratio	**109.8%**	**107.8%**
Total funding ratio	**118.2%**	**115.5%**

The funding ratios measure the Group's liquidity.

(v) Adjusted earnings per share

Adjusted earnings per ordinary share are calculated by dividing the adjusted profit attributable to equity holders of the parent by the weighted average number of ordinary shares as follows:

	2018	2017
Adjusted profit attributable to equity holders of the parent (£ millions)	29.9	21.5
Weighted average number of ordinary shares (number)	18,475,229	18,475,229
Adjusted earnings per share (pence)	**161.8**	**116.4**

(vi) Loans to customers

The impact of the IFRS 9 transition adjustments on the opening balances by segment are set out in the table below:

	31 December 2017 (on an IAS 39 basis)	IFRS 9 transition adjustment	1 January 2018 (on an IFRS 9 basis)
	£million	£million	£million
Business Finance			
Real Estate Finance	580.8	0.2	581.0
Asset Finance	116.7	(0.2)	116.5
Commercial Finance	126.5	(0.2)	126.3
Consumer Finance			
Retail Finance	452.3	(9.7)	442.6
Motor Finance	274.6	(21.6)	253.0
Debt Management	15.6	-	15.6
Consumer Mortgages	16.5	-	16.5
Other	15.3	(0.3)	15.0
	1,598.3	**(31.8)**	**1,566.5**

(vii) Adjusted profit and effective adjusted tax rate

Adjusted profit before tax was £36.7 million (2017: £27.0 million). **Adjusted profit after tax** was £29.9 million (2017: £21.5 million).

The Group uses adjusted profit for planning and reporting purposes, as it improves the comparability of information between reporting periods. The adjustments to profit relate to non-controllable items or other items that fall outside of the Group's core business activities.

Fair value amortisation relates to the acquisition of V12 Finance Group. The acquisition accounting required identifiable assets and liabilities to be adjusted to their fair value, and these adjustments are subject to amortisation.

Transformation costs comprise principally costs of closing the unsecured personal lending product, the cost of potential corporate acquisition work and treasury development (31 December 2017: comprised the costs of setting up the Group's Consumer Mortgage operation and of closing the current account and unsecured personal lending products).

Bonus payments of £1.3 million (2017: £0.6 million) relate to a long term incentive plan that was set up for a small number of employees on the creation of the Commercial Finance business. The scheme is based on profits earned by that business up to the end of 2019, and is payable in 2020.

Profit on sale of Non-Standard Finance plc shares and discontinued activities represented non-core activities.