Banking as it should be

aldermore

Aldermore Group PLC

Annual report and accounts 2014

Strategic report

Highlights of the year

Increased support for UK SMEs and homeowners

- Net loans to customers up by 42% to £4.8 billion (2013: £3.4 billion)
- Record level of annual organic origination of £2.4 billion (2013: £1.7 billion)
- Lending to SMEs up by 32% to £2.2 billion (2013: £1.7 billion)
- Residential Mortgages grew by 53% to £2.6 billion (2013: £1.7 billion)

Dynamic online savings franchise

- Customer deposits up by 29% to £4.5 billion (2013: £3.5 billion)
- Excellent growth in SME deposits, up by 97% to £1.0 billion (2013: £0.5 billion)

Record levels of profitability

- Profit before tax up by 96% to £50.3 million (2013: £25.7 million)
- Excluding IPO costs, underlying profit before tax more than doubled to £56.3 million
- Return on equity[1] increased to 15.1% (2013: 11.6%)

Diversified funding and strong capital base

- Issued £333 million of RMBS to further diversify funding base
- Successfully issued £75 million of Additional Tier 1 capital
- Total capital ratio of 14.8% (2013: 14.2%) and leverage ratio of 6.3% (2013: 5.3%)

Building a Bank to be proud of

- Delivering exceptional service, rated 4.6 out of 5 by our customers
- Number of customers up by 23%
- Received accreditation as 'One to Watch' in The Sunday Times 'Best Companies to Work For' annual survey
- Investing for the future, number of staff increased by 28% to 876

[1] Excluding IPO costs of £6.0 million.

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For more information on our business visit
www.aldermore.co.uk

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Facebook: AldermoreBank

LinkedIn: company/aldermore-bank-plc

YouTube: AldermoreBank

The consolidated financial statements of Aldermore Group PLC ('the Group') comprise of Aldermore Group PLC ('the Company') and its subsidiary undertakings, including Aldermore Bank PLC ('the Bank').

Strategic report

Aldermore at a glance

Established in 2009, Aldermore is a SME-focused bank with a legacy-free, modern and scalable digital infrastructure.

Vision – "Banking as it should be"

- To be the strategically important bank for UK SMEs and homeowners
- DNA: Reliable, Expert, Dynamic, Straightforward

Targeted product offering

- Asset-backed lending for underserved customer segments
- Large, growing markets with attractive risk-adjusted returns
- Dynamic online deposit franchise forms funding core

Intermediary-led distribution complemented by direct

- 12 regional offices provide operational support

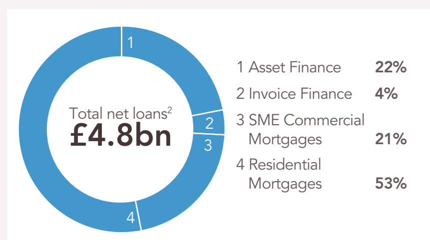
Consistent, robust credit risk management

- Modern IT systems allows focused use of expert underwriters
- Granular loan portfolio with strong credit KPIs

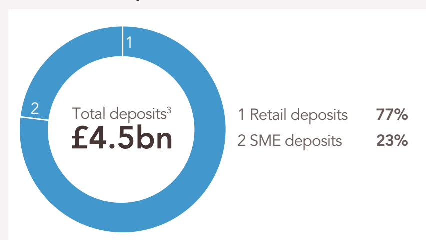
Proven track record of growth and profitability

- 98% of origination organically generated[2]
- Profit before tax almost doubled in 2014 to £50.3 million

Net loans[3]



Customer deposits[4]

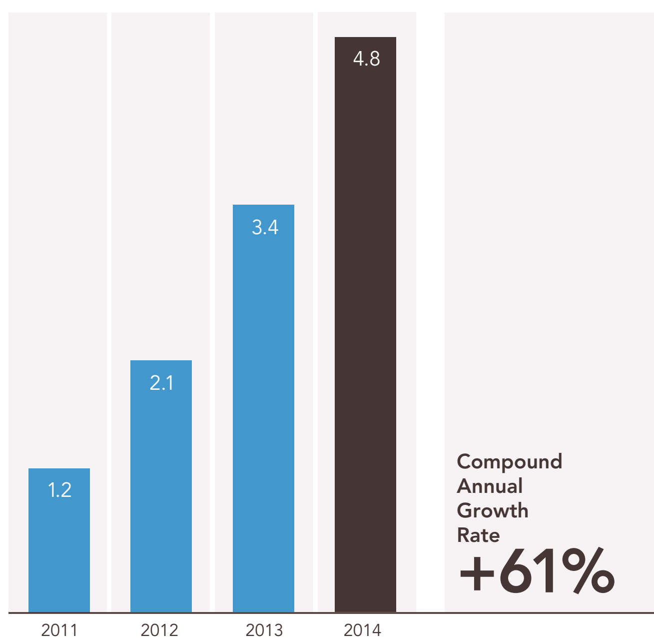


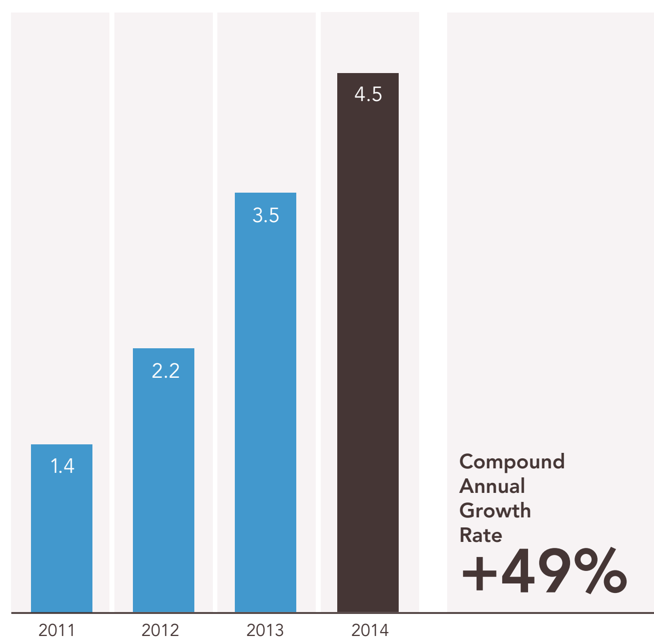
[2] From 2012 to 2014.

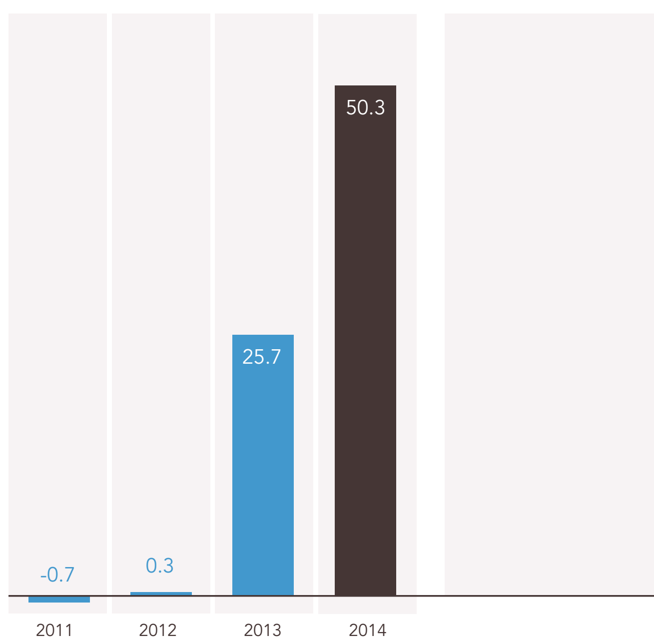
[3] Loans and advances to customers as at 31 December 2014.

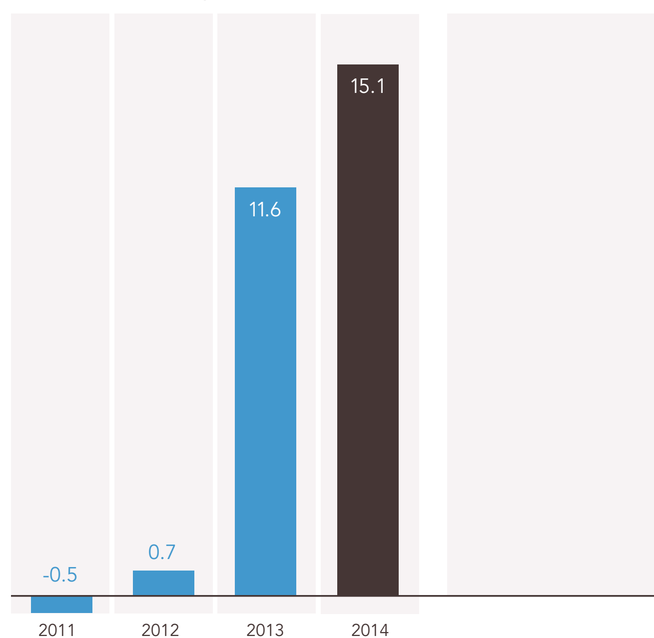
[4] Customers' accounts as at 31 December 2014. SME deposits includes corporate deposits.

Proven track record of delivery









[5] Return on equity is calculated as profit after tax (excluding post tax IPO related costs) as a percentage of average shareholders' funds.

Chairman's statement

"Aldermore has the corporate governance, risk management and culture to operate a profitable and sustainable business in public markets over the long term."

Glyn Jones
Chairman

2014 highlights

- Further strengthening of the Board with the appointment of four new independent Non-Executive Directors
- A Corporate Governance Policy Framework in line with best practice standards set out in UK Corporate Governance Code
- Continued development of our customer-centric culture founded on a clearly defined approach to risk management

Another record year

When appointed to the Board in March 2014, it was evident I was joining an energised business which had a refreshingly different approach to banking. It really is quite remarkable that a bank which started in the midst of the financial crisis has grown so significantly and is now an established business delivering long-term sustainable growth and strong shareholder returns. By offering our customers exceptional service, underpinned by strong values, Aldermore is performing strongly, with excellent organic growth and a proven track record of delivery. The Group generated profit before tax excluding IPO costs of £56.3 million, more than double the amount achieved in 2013.

The Group ended 2014 with a fully loaded CRD IV Common Equity Tier 1 capital ratio of 10.4 per cent, underlining our strong capital base and positioning the Group for long-term growth. Our liquidity position is also robust and in excess of regulatory requirements.

Governance

One of my primary goals since joining has been to further enhance the Group's corporate governance as we prepare for life as a public entity.

In September, we announced Aldermore's intention to float on the London Stock Exchange, however, the significant deterioration in global equity markets persuaded the Board to postpone the initial public offering (IPO). The number of IPOs that did not proceed during this period reinforces just how difficult the global markets were at the time. It is impossible to call the markets, but I am very proud of the management team for what was achieved, and the positive feedback that we received, against a backdrop of market turmoil. The excitement generated amongst a broad range of investors was clearly evident and so we remain confident that a listing on the London Stock Exchange is the natural next step in Aldermore's evolution.

Further strengthening our Board

This year saw a number of changes to our Board composition. When I joined, I began recruiting further Directors to build a Board capable of supporting the Group's ambitions. During the course of the year four independent Non-Executive Directors joined the Board, Danuta Gray as the Senior Independent Director, John Hitchins as Chair of the Audit Committee, Cathy Turner as Chair of the Remuneration Committee and Peter Shaw, who will now take over as Chair of the Risk Committee with effect from 1 March 2015. Neil Cochrane also joined the Board as a Non-Executive Director representing our principal shareholder.

I am delighted that we were able to attract such high calibre and experienced individuals who bring a wealth of business and public company experience.

In December, John Callender decided to step down from his position on the Board with effect from 27 February 2015, having served as an independent Non-Executive Director since the Group was established. John has played a critical role at Aldermore, making invaluable contributions both as a member of the Board, as Chairman of the Audit and Risk Committee and latterly the Risk Committee and as Acting Chairman prior to my appointment. I would like to thank John for all of his hard work and wish him the very best for the future.

I would also like to thank Mark Stephens, Deputy CEO and Group Commercial Director, Paul Myers, Chief Operating Officer, and Steve Barry, Chief Risk Officer, who in line with best practice for listed entities stepped down from the Board in 2014. Mark, Paul and Steve have been with Aldermore since the beginning and have made an enormous contribution to the effectiveness of the Board. They all remain key members of our Executive team.

A clearly defined approach to risk management

As well as making changes to the Board composition we restructured our committees by splitting the Audit and Risk Committee into two separate entities.

This was done to support the evolution of our Risk Management Framework. The development, implementation and maintenance of this framework is now overseen by the Risk Committee to ensure that its strategy, principles, policies and resources are aligned to the Group's risk appetite and to regulatory and industry best practices. The Risk Committee also reviews the Group's performance against risk appetites and the effectiveness of the Group's risk management processes.

Underpinned by our culture

We continue to foster a culture centred on the customer which is informed by a keen awareness of risk. We encourage staff to take personal responsibility and ask managers to empower their teams. We have developed a management framework which supports a balanced and fair approach towards risk and reward.

What does this mean in practical terms? It means that we clearly communicate our risk appetite to all staff including measurable risk tolerances and the appropriate escalation procedures. It means that our people are assessed not only on what they achieve, but more importantly on how they achieve it. It means that incentives we offer to senior management are aligned with long-term outcomes. Crucially, it means that we deliver products and services to our customers which are transparent and meet their needs.

I am confident Aldermore has the corporate governance, risk management and culture to operate a profitable and sustainable business in public markets over the long term.

2015 and beyond

2015 will be an important year for the Group. The challenges facing the global economy look set to continue, particularly in the eurozone. Meanwhile the general election in May looks likely to be one of the most unpredictable in living memory. Yet amid this economic and political uncertainty, SMEs, homeowners and savers will continue to require financial services which meet their needs and we are committed to playing our part.

On behalf of the Board, I would like to thank our customers for their continued support and to extend my gratitude to our fantastic team for their hard work, dedication and loyalty to Aldermore.

Glyn Jones
Chairman

Strategic report

Chief Executive Officer's statement

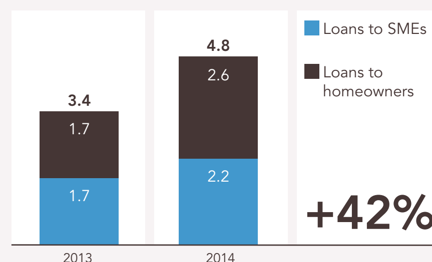
"Our financial results for 2014 demonstrate our approach is working. During the year, we lent more than ever before to UK SMEs and homeowners."

Phillip Monks
Chief Executive Officer

2014 highlights

- Profit before tax excluding IPO costs more than doubled to £56.3 million
- Net loans to customers up by 42% to £4.8 billion
- Loans to SMEs up by 32% to £2.2 billion
- Loans to homeowners up by 53% to £2.6 billion
- Record loan origination of £2.4 billion, up 39%
- Customer deposits up by 29% to £4.5 billion

Net loans (£bn)



A different kind of bank

From the beginning, nearly six years ago, Aldermore set out to be different to Britain's traditional high street lenders. Unconstrained by legacy systems and processes, our approach to serving our customers is modern, streamlined and designed to take the hassle out of banking. We understand that people are free to choose who they bank with and that their custom must be earned – not taken for granted. We are transparent about how we operate, our business model is straightforward and we have nothing to hide. We are agile, expert and entrepreneurial in our approach which allows us to empathise with our customers: Britain's underserved Small and Medium-sized Enterprises (SMEs), homeowners and savers.

An approach that works

Our financial results for 2014 demonstrate our approach is working. During the year, we lent more than ever before to UK SMEs and homeowners with total loans up by 42 per cent to £4.8 billion. Record levels of organic origination of £2.4 billion, up 39 per cent on the previous year of £1.7 billion, drove this excellent growth in net lending. To support our lending businesses our online retail and SME deposits franchise continues to go from strength to strength. Customer deposits grew by 29 per cent to £4.5 billion with SME deposits up by 97 per cent to £1 billion. We continued to diversify our funding in 2014 with our inaugural Residential Mortgage-Backed Securitisation (RMBS) in April, which was oversubscribed.

We maintained our focus on managing costs and leveraging our operating model which saw our cost to income ratio fall by six per cent[6] to 60 per cent and we continue on plan towards our target of less than 40 per cent by the end of 2017.

The growth we have seen in our business has delivered strong and sustainable returns for our shareholders. Profit before tax excluding IPO costs of £6.0 million more than doubled to £56.3 million driving a return on equity of 15.1 per cent.

To support our medium-term growth plans and to adopt a capital structure appropriate for a mature bank, we raised £75.1 million of additional capital through the issuance of Additional Tier 1 (AT1) securities in December 2014.

Our customers' success is our success

Every day we see examples of how our support is helping to fuel the success of Britain's SMEs, whether this is by enabling them to purchase equipment to fulfil new contracts, providing expertise to manage their cash flow or advancing them funds to expand their property portfolios.

Our customers like what we are doing. We are one of the only banks to ask customers to rate and review our services online. In 2014, our average score was 4.6 out of 5 and 96 per cent of customers who left us a review said they would recommend us. We often read reviews which describe our service as "banking as it should be".

Building a long-term, sustainable business

In May 2015, we will celebrate the Group's sixth anniversary. We have achieved a great deal since we were founded in 2009. When I think back to those early days, our focus was on building sound and sustainable infrastructure, smart and efficient processes and customer-focused propositions. We simply wanted to lay the foundations of a profitable business while being reliable, expert, dynamic and straightforward in everything we do. That, in essence, is our DNA.

Since then we have demonstrated that we have a profitable and straightforward business model that provides great service for our customers. In 2014, we made further significant investment in the Group's controls and infrastructure, including configuring our digital platform so it is fully scalable to support future growth with moderate ongoing investment.

We also have a great team dedicated to executing our strategy, which was further bolstered in June 2014 with the appointment of Vicki Harris who joined as Group Strategy and Marketing Director. Our Board of Directors has been further strengthened in 2014 and I am grateful for their support in ensuring we build a sustainable business for the long term.

A year of highlights

In 2014, we restructured our mortgages businesses to better serve customers, expanded our customer Ratings & Reviews service, launched the Aldermore Community Team (ACT) and received accreditation as 'One to Watch' in the Sunday Times 'Best Companies to Work For' annual survey. We also continued to improve the services we provide to customers, with the launch of products including our unique Customised Fixed Rate Account which allows SMEs to decide – to the day – how long they want to deposit their money for. We also introduced 'APP+', a mobile application which enables Asset Finance introducers to price a deal or complete an application on the go, wherever they are and whenever is convenient. The Group won more industry awards than ever before – 24 across our business lines and some for the fourth consecutive year.

A strong track record set to continue

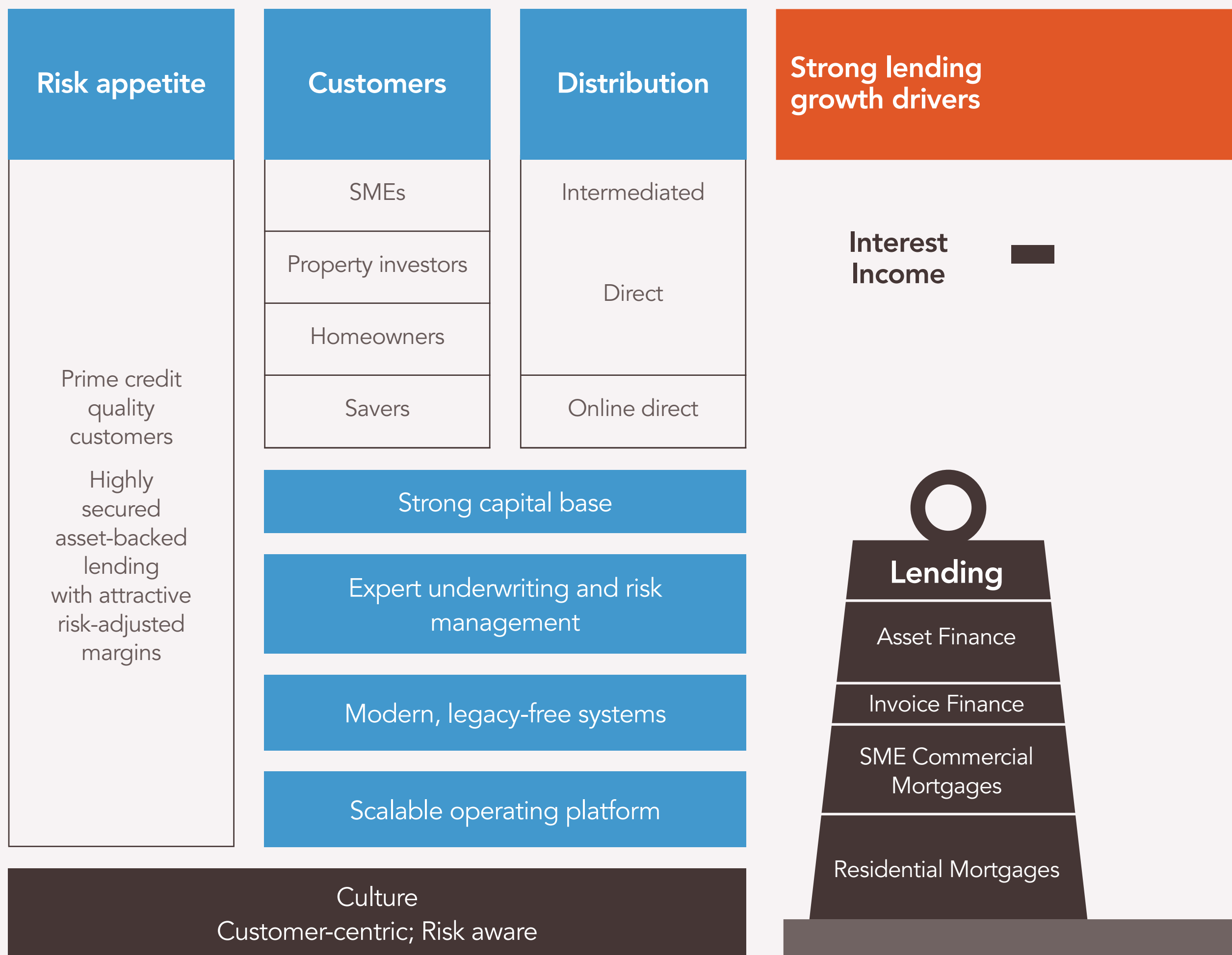
I am very proud of our achievements during 2014. It was another busy year for the Group which saw us achieve record results. I would like to thank all of our employees not only for their dedication but for the shared excitement and pride in what we are building at Aldermore. We measure our success by how we have helped customers grow their business, buy a property and save for the future. This is why people join us and it is what sets us apart from the competition and I am confident this strategy will continue to serve us well in 2015 and beyond.

Phillip Monks
Chief Executive Officer

6 Excluding IPO related costs of £6.0 million.

Strategic report

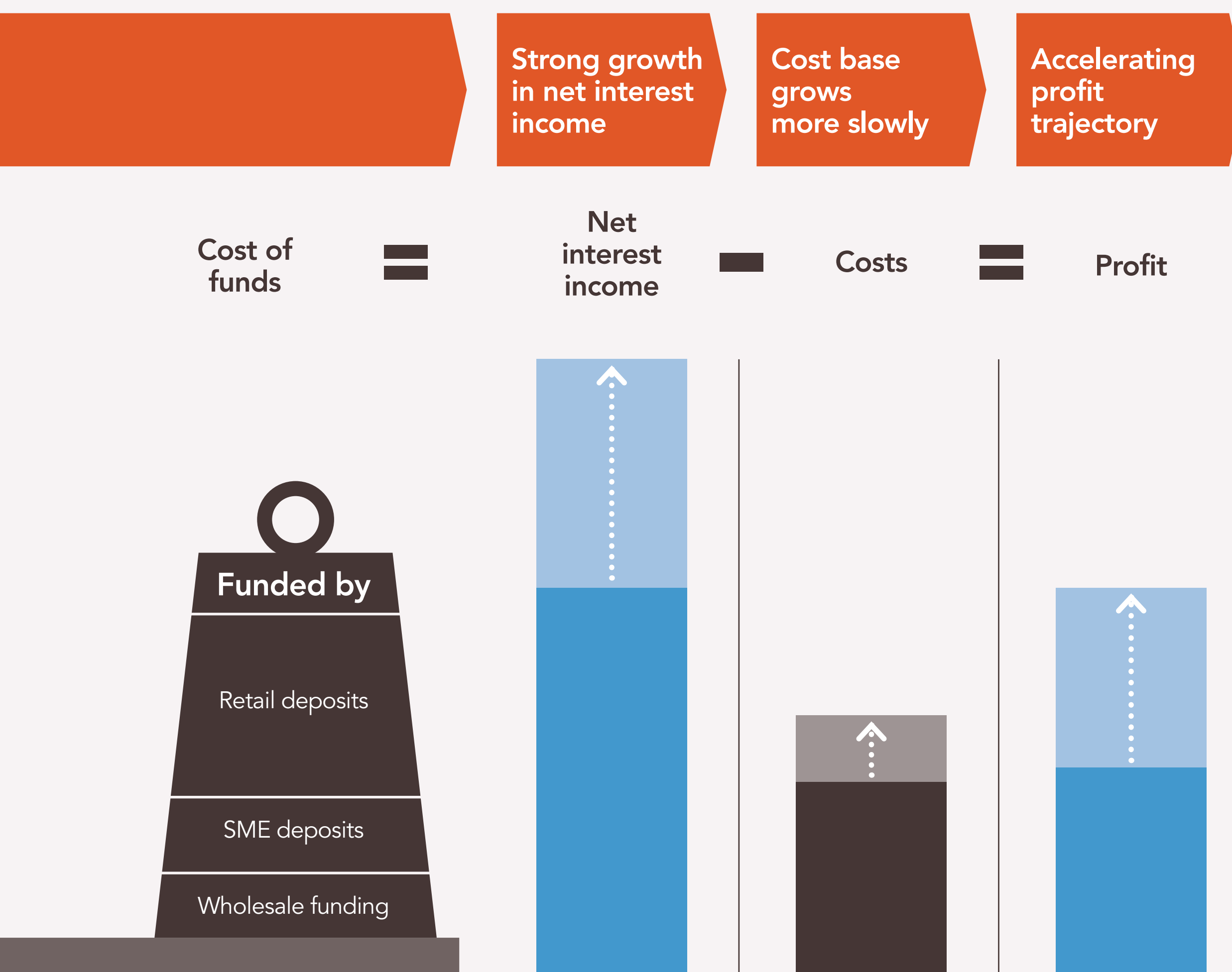
Leveraging the business model



Our DNA is to be Reliable, Expert, Dynamic and Straightforward – these values inform everything we do forming the basis of our culture and brand.

We focus on prime credit quality customers across four lending lines chosen for their size, attractive risk adjusted returns and tangible asset security. We engage with our customers through intermediaries and directly.

We enjoy the advantage of modern, legacy-free systems which we use to support, where appropriate, our expert underwriters in making considered



decisions rather than a "computer says no" approach. Our operating platform is scalable to allow for future growth.

We advance loans on which we earn income; these loans are funded via a mix of deposits and wholesale funding on which we pay interest. The difference is net interest income which grows with our loan book. Having invested upfront in our operating platform, our cost base grows more slowly than our net interest income driving an accelerating profit trajectory. This is what we refer to as "leveraging our business model".

Our strategy

To deliver long-term sustainable growth and strong shareholder returns through offering simple financial products and solutions that are within our risk appetite and meet the needs of disenfranchised and underserved SMEs, homeowners and savers across both their business and personal lives.

Strategic objectives

1 Build strong market positions with distinctive customer propositions in chosen segments, while maintaining excellent asset quality

Aldermore focuses on specialist lending to SMEs and homeowners across four large lending segments which were deliberately targeted for their strong collateral characteristics, attractive risk-adjusted returns and growth potential.

2 Deliver long-term sustainable and efficient growth and generate strong shareholder returns

The Group aims to leverage its scalable, efficient and legacy-free operating model to grow revenues more quickly than its cost base and deliver long-term, sustainable profitability.

3 Maintain prudent capital, funding and liquidity positions

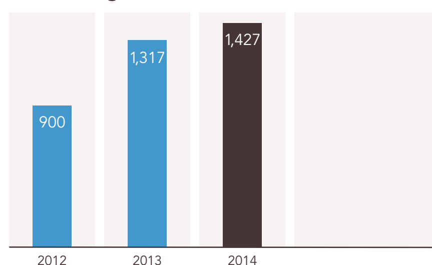
Our aim is to take a prudent approach towards maintaining a capital base that supports the Group's growth aspirations and exceeds regulatory requirements. Our funding is expected to remain predominantly deposit-led. However, in addition we utilise wholesale sources such as the Bank of England's Funding for Lending Scheme, our Residential Mortgage Backed Securitisation and a small amount of Tier II funding.

4 Continue to build an engaged and productive workforce aligned with the Aldermore culture

We recognise that for us to be successful in what we do, it is important to attract and retain a talented workforce. The Group aims to hire people who fit culturally and have the right competencies. We then empower managers with the tools and support needed to increase employee engagement.

Our Key Performance Indicators

Net loans growth (£m)

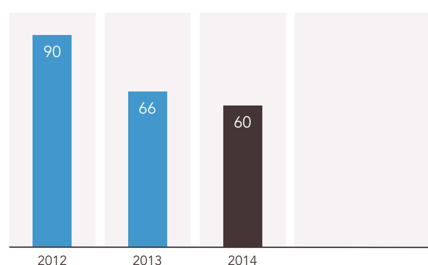


Definition
Absolute increase in loans and advances to customers net of impairment provisions.

We aim to grow net loans whilst remaining within our clearly defined risk appetite.

We aim to maintain net loan growth in line with current run rates.

Cost/income ratio (%)

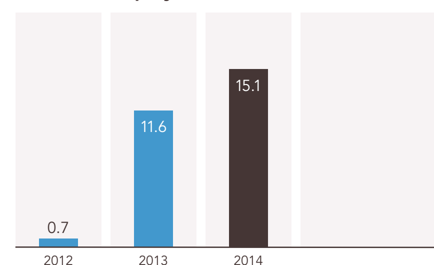


Definition
Cost/income ratio is calculated as administrative expenses (excluding IPO related costs), depreciation and amortisation, as a percentage of operating income.

As a Group, we are successfully leveraging our operating model. Between 2012 and 2014, whilst our loan book grew at a compound annual rate of 53 per cent, the compound rate of increase in our cost base over the same period was only 33 per cent. As a result, cost/income ratio at the end of 2014, excluding IPO related costs, was 60 per cent compared to 90 per cent in 2012 and 66 per cent in 2013.

The Group is targeting a cost/income ratio of less than 40 per cent by the end of 2017.

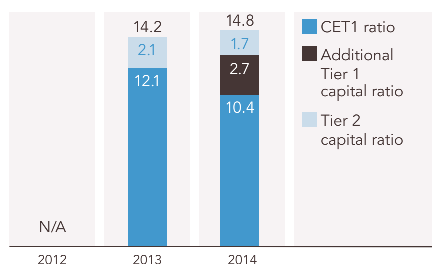
Return on equity (%)



Definition
Calculated as profit after tax (excluding post tax IPO related costs) as a percentage of average equity.

Our return on equity increased from 11.6 per cent in 2013 to 15.1 per cent (excluding costs associated with the IPO) primarily as a result of increased profitability.

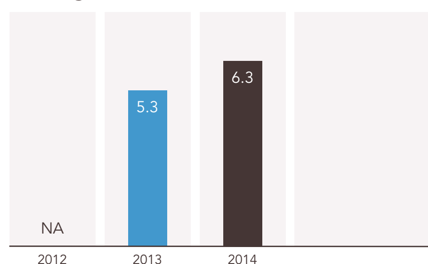
Total capital ratio (%)



Definition
Fully loaded CRD IV Common Equity Tier 1 (CET1) capital ratio is calculated as risk weighted assets as a percentage of CET1 capital. Fully loaded represents the adoption of all requirements of CRD IV once the transitional phase has elapsed. In Aldermore's case, there is no difference between current CET1 ratio and fully loaded CET1 ratio.

Aldermore has levels of capital which are in excess of the requirements set by the Prudential Regulation Authority (PRA). As at 31 December 2014 Aldermore's fully loaded CRD IV CET1 Ratio was 10.4 per cent and total capital ratio of 14.8 per cent.

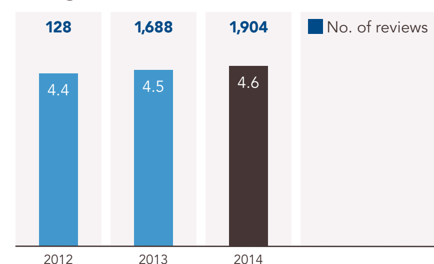
Leverage ratio (%)



Definition
A ratio of Tier 1 Capital to total exposures, calculated in accordance with the requirements of CRD IV.

Aldermore's leverage ratio as at 31 December 2014 was 6.3 per cent and exceeds the minimum requirement as proposed by the PRA.

Ratings and reviews



Definition
Our online Ratings & Reviews service enables customers to provide honest reviews of our products and services. When customers submit a review, we ask them to give us a rating out of 5 based on their experience with us.

Our Ratings & Reviews service was launched in 2012 for our personal savings, business savings and Invoice Finance customers. In 2014, we also extended the service to our Residential Mortgage customers. The feedback we receive is published unedited on our website and is used by us to help improve our services to customers.

Strategic report

Chief Financial Officer's review

Another record year for the Group

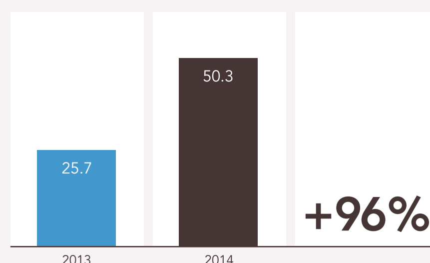
"2014 was another record year for Aldermore. As expected, as the business matures we are seeing our significant balance sheet growth driving an accelerating profit trajectory. We delivered record loan origination of £2.4 billion, net new lending in excess of £1.4 billion and almost doubled profit before tax to £50.3 million."

James Mack
Chief Financial Officer

2014 highlights

- Net loans to customers up by 42% to £4.8 billion
- Customer deposits up by 29% to £4.5 billion
- Cost to income ratio[7] down 6pts to 60% (2013: 66%)
- Excluding IPO costs, profit before tax of £56.3 million is more than double 2013
- Return on equity[7] increased to 15.1% (2013: 11.6%)
- Issued £333 million of RMBS to further diversify funding base
- Successfully issued £75 million of AT1 capital
- Strongly capitalised with total capital ratio of 14.8% and leverage ratio of 6.3%

Profit before tax (£m)



[7] Excludes costs related to IPO of £6.0 million.

Balance sheet – key items	2014 £m	2013 £m	% change
Loans and advances	4,801.1	3,373.8	42
Cash and near cash equivalents[8]	197.0	430.4	(54)
Investments	509.7	355.7	43
Other assets	57.5	43.1	33
Total assets	**5,565.2**	**4,203.0**	**32**
Customer deposits	4,459.0	3,464.0	29
RMBS	279.1	–	–
FLS	304.2	383.1	(21)
Tier 2 capital	36.8	35.6	3
Other liabilities	107.3	55.0	95
Total liabilities	**5,186.4**	**3,937.6**	**32**
Total equity	**378.9**	**265.4**	**43**
Key ratios			
Net loan growth	1,427	1,317	
Loans to deposits ratio	108%	97%	
Liquid assets/deposits	16%	23%	
Total capital ratio	14.8%	14.2%	

Assets exceed £5 billion

In 2014, we increased our support to British SMEs and homeowners with a 42 per cent increase in net loans to £4.8 billion (2013: £3.4 billion). Net new lending of £1.4 billion was above both our guidance of around £1.3 billion and the prior year and was supported by record organic origination of £2.4 billion.

We hold a liquid assets buffer in the form of cash and investments to mitigate liquidity risk. As at 31 December 2014, the ratio of liquid assets to deposits was 16 per cent compared to 23 per cent for the prior year when the Group was holding additional liquidity in advance of issuing our inaugural RMBS.

Total assets exceeded £5 billion for the first time and were up by 32 per cent on the prior year driven by increased lending volumes.

Diversified funding base

Our lending activity is matched by a diversified funding base which is predominantly deposit-led with wholesale funding from RMBS, the UK Government's Funding for Lending Scheme (FLS) and a small amount of Tier 2 debt securities.

We continued to attract savers with our 'good returns effortlessly' proposition and deposits increased by 29 per cent over 2013 to £4.5 billion at the end of 2014. We have driven very strong growth in SME deposits, up 97 per cent in 2014 to over £1 billion. We've also recently launched corporate deposits to further diversify our future funding sources.

Our loans to deposits ratio has moved from 97 per cent at the end of 2013 to 108 per cent at 31 December 2014 as we have continued to diversify the wholesale element of our funding base. Looking forward, we expect to see this ratio to remain above 100 per cent reflecting the increased proportion of wholesale funding now used.

In April 2014, we completed our inaugural RMBS issuing c.£333 million of securities priced at LIBOR +67bps. We were delighted at the level of investor interest in this transaction.

We continue to use the FLS and Aldermore was the third biggest lender to UK SMEs under this scheme during the year. As at 31 December 2014, we had drawn £485 million of treasury bills under the FLS creating £304 million of on-balance sheet funding via repurchase transactions.

The Tier 2 instrument is a historic instrument with a nominal value of £40 million issued in May 2012 and a first call date in May 2017.

As a result of the above, total liabilities grew at 32 per cent to £5.2 billion (2013: £3.9 billion).

[8] Includes 'Cash and balances at central banks' and 'Loans and advances to banks'.

Chief Financial Officer's review continued

Record profitability

Income statement – key items	2014 £m	2013 £m	% change
Interest income	227.8	156.4	46
Interest expense	(87.6)	(75.8)	16
Net interest income	**140.2**	**80.6**	**74**
Net fee income	18.6	16.0	16
Other income	6.2	11.7	(47)
Total operating income	**165.0**	**108.3**	**52**
Operating expenses	(105.1)	(71.2)	48
of which IPO related costs	*(6.0)*	–	–
Impairment losses on loans and advances to customers	(9.6)	(11.5)	(17)
Profit before tax	**50.3**	**25.7**	**96**
Tax	(11.9)	–	–
Profit after tax	**38.4**	**25.7**	**50**
Key ratios			
Net interest margin	3.4%	3.0%	0.4%
Cost/income ratio[9]	60%	66%	(6)%
Cost of risk[10]	23bps	42bps	(19)bps
Return on equity[9] (post tax)	15.1%	11.6%	3.5%

Total equity

As at 31 December 2014, total equity was £378.9 million an increase of 43 per cent on the prior year due to the issue of £73.7 million of AT1 capital, net of costs, in December 2014 and an increase in retained earnings driven by the profit for the year.

Lending growth drives interest income

The 42 per cent growth in net lending delivered during the year has driven 46 per cent growth in interest income to £227.8 million (2013: £156.4 million) with the gross interest margin remaining broadly constant at 5.57 per cent (2013: 5.76 per cent). We continued to diversify our funding mix with a higher proportion of SME deposits and the RMBS issuance in April. Both of these funding sources are cheaper than our average cost of funding and helped drive our cost of funding down to 2.14 per cent (2013: 2.79 per cent). As the RMBS was issued in April 2014, we have only experienced nine months of benefit and expect to accrue further benefits in 2015.

As a result, we delivered an increase in net interest income of 74 per cent to £140.2 million (2013: £80.6 million) whilst also driving a 0.4 per cent improvement in the net interest margin from 2.97 per cent in 2013 to 3.43 per cent for 2014.

Net fees and other income

Net fee income is predominantly driven by the Invoice Finance business which was stable in the year. The growth of 16 per cent during the year to £18.6 million (2013: £16.0 million) predominantly relates to other fee income. Other fee income contains commitment, arrangement, valuation and early redemption fees related to our mortgages business as well as fees associated with the Asset Finance business and the increase during the year was driven by growth in lending in these portfolios.

Other income includes other operating income and derivative income and was down over prior year at £6.2 million (2013: £11.7 million) due to adverse mark to market movements on hedging derivatives caused by financial markets volatility in the fourth quarter.

[9] Excludes costs related to IPO of £6.0 million.

[10] Cost of risk is calculated as impairment losses as a percentage of average net loans.

Leveraging our scalable operating platform

Operating expenses were £105.1 million, an increase of 48 per cent on 2013 expenses of £71.2 million. Excluding costs related to the IPO of £6.0 million, underlying operating expenses were £99.1 million, an increase of 37 per cent over 2013.

Operating expenses	2014 £m	2013 £m	% change
Other administrative expenses	91.6	65.3	40
Provisions	3.6	2.1	71
IPO related costs	6.0	–	–
Depreciation and amortisation	3.9	3.8	2
Total operating expenses	**105.1**	**71.2**	**48**
Operating expenses excluding IPO related costs	99.1	71.2	39

Other administrative expenses have grown by 40 per cent during the year to £91.6 million (2013: £65.3 million). The rise was mainly due to an increase in staff costs, up by 29 per cent to £49.4 million (2013: £38.4 million). The number of employees and contractors increased by 28 per cent to 876 in 2014. The increase in costs represent a 'step-change' from the previous year as we invested further to build a sustainable and prudently managed business.

We particularly focused on the strengthening of central functions including risk, compliance and finance to ensure we retain the appropriate levels of oversight as the business continues to grow and mature, and to prepare for a potential listing.

We have increased investment in information technology systems by 77 per cent to £8.3 million (2013: £4.7 million). Despite the increase, our ongoing investment needs in IT remains moderate. Included within administrative expenses was a charge of £1.6 million as we wrote off the investment in development of systems, related to Asset Finance, following a review of requirements.

Provisions predominantly reflect the levy for the UK Government's Financial Services Compensation Scheme (FSCS) which offers protection to individual deposit holders on amounts up to £85,000. The levy is linked to size of the Group's savings business and has grown by 57 per cent in 2014 to £2.6 million (2013: £1.7 million).

During 2014, the Group undertook significant preparations for a listing on the London Stock Exchange and the related costs charged to the income statement in the year were £6.0 million (2013: £nil). Due to adverse stock market conditions following the announcement of our Intention to Float (ITF), the Group withdrew the offer on 15 October 2014.

Depreciation and amortisation remained broadly consistent with the prior year at £3.9 million (2013: £3.8 million).

Reduced cost/income ratio

We continued to make good progress towards our target cost/income ratio of less than 40 per cent by the end of 2017 with a 6 percentage point reduction over the year to 60 per cent (2013: 66 per cent) excluding IPO costs.

Improved cost of risk

We continue to rigorously manage the credit portfolio. In addition to the actions taken in Invoice Finance, we also benefitted from a large recovery in the Asset Finance division and two large recoveries in our SME Commercial Mortgages business. As a result, impairment losses in 2014 were reduced to £9.6 million (2013: £11.5 million) equating to a cost of risk of 23bps (2013: 42bps). Excluding these three recoveries, the cost of risk for 2014 was 33bps.

Underlying profit doubled

In 2014 we have generated profit before tax of £50.3 million, up by 96 per cent over 2013. Excluding IPO related costs, underlying profit before tax of £56.3 million is more than double that achieved in 2013.

Strategic report

Chief Financial Officer's review continued

Strong performance across all divisions

Segmental result[11]	2014 £m	2013 £m	% change
Asset Finance	25.5	12.9	97
Invoice Finance	5.4	3.3	64
SME Commercial Mortgages	34.0	18.7	82
Residential Mortgages	56.8	26.4	115
Central Functions	(71.3)	(35.6)	100
Profit before tax	**50.3**	**25.7**	**96**
Tax	(11.9)	–	–
Profit after tax	**38.4**	**25.7**	**50**

During 2014, we delivered improvements in profit before tax in each of our lending divisions. Our Asset Finance division almost doubled its segmental result to £25.5 million, while SME Commercial Mortgages division was up by 82 per cent to £34.0 million (2013: £18.7 million). The segmental result for Residential Mortgages more than doubled to £56.8 million (2013: £26.4 million). I am pleased to see the positive impact of actions that we took in our Invoice Finance division, with the segmental result up by 64 per cent at £5.4 million. Further details on financial performance of each business can be found on page 18 to page 37 of this report.

2014 costs related to central functions were £71.3 million (2013: £35.6 million). These costs are mainly related to staff costs and office costs, as we invested in further strengthening risk, finance and compliance. Central functions include costs associated with our Savings and Treasury divisions which are responsible for raising finance on behalf of lending divisions and are managed centrally. Included within these central functions costs are staff related costs of £26.7 million, information technology related costs of £6.7 million, office costs of £3.8 million, depreciation and amortisation costs of £3.4 million, Financial Services Compensation Scheme costs of £2.6 million as well as £1.6 million relating to the write down of an intangible asset. As previously discussed, we also incurred £6.0 million costs related to the IPO.

The tax charge for 2014 was £11.9 million (2013: £nil) as the Group became a taxpayer for the first time during the year and represents an effective tax rate of 23.6 per cent (2013: 0 per cent). Profit after tax was £38.4 million (2013: £25.7 million), an increase of 50 per cent over 2013.

Driving strong returns

The record profit performance of the Group resulted in strongly improved returns with a return on equity, excluding IPO costs, of 15.1 per cent compared with 11.6 per cent for 2013. On a like for like basis, the improvement over 2013 is closer to 6 per cent as, had 2013 not benefitted from brought forward tax losses and been taxed at 2014 rates, the 2013 return would have be closer to 9 per cent.

[11] Segmental result = Divisional profit before allocation of central costs and tax. Numbers may not exactly sum due to rounding.

Capital position

Capital	2014 £m	2013 £m	% change
Common Equity Tier 1 capital	281.2	242.1	16
Additional Tier 1 capital	73.7	–	–
Tier 2 capital	45.3	41.9	8
Total capital	**400.2**	**284.0**	**41**
Risk Weighted Assets (RWA)	**2,702.0**	**1,993.0**	**36**
Key ratios			
Fully loaded CRD IV CET1 ratio (%)	10.4%	12.1%	(1.7)%
Total capital ratio	14.8%	14.2%	0.6%
Leverage ratio[12]	6.3%	5.3%	1.0%

The Group's fully loaded CRD IV total capital ratio as at 31 December 2014 was 14.8 per cent up from the prior year of 14.2 per cent driven by retained earnings and AT1 capital.

In December 2014, Aldermore issued £73.7 million, net of costs, of AT1 perpetual notes with an associated coupon of 11.875 per cent and a first call date of April 2020. This is an important step in developing a CRD IV compliant capital structure appropriate for a mature bank and strengthens our overall capital position.

The Group's proforma leverage ratio was comfortably above the required minimum of 3 per cent at 6.3 per cent, up from 5.3 per cent at the end of 2013 due to the issuance of AT1 securities.

Outlook

We are confident of continuing to build upon these excellent results. In 2015, we expect to again grow net loans in line with current run rates and make further progress towards our target of a cost/income ratio of less than 40 per cent by the end of 2017.

[12] A ratio of Tier 1 Capital to total exposures, as calculated by the Group in accordance with the requirements of Capital Requirements Directive (CRD IV).

Strategic report

Asset Finance

2014 highlights

- Net lending exceeded £1 billion, up by 45% on 2013
- Advanced over £2 billion in asset finance funding since 2009
- Record origination of £739.5 million, up 21% over 2013
- Net interest income up by 60% to £36.9 million
- Cost of risk remains low at 30bps
- Segmental result up 97% to £25.5 million
- New stocking finance and operating lease products
- Launched smartphone and tablet pricing application

Aldermore supports capital investment in business-critical assets via hire purchase and lease agreements. Leveraging our depth and breadth of expertise, we finance a wide array of assets encompassing plant and machinery, transportation, printing equipment, digital technologies and specialist large ticket items. This flexibility enables us to meet the needs of customers ranging in size from micro clients to plcs across key industries.

In addition, we offer wholesale and block discounting facilities to smaller leasing companies and brokerages enabling them to extend credit directly to SMEs.

Market

Asset Finance loans originated in the UK were approximately £25 billion[13] in 2014. Around 80 per cent of market origination relates to 'hard' assets such as vehicles and plant and machinery for which there are strong secondary markets. A significant proportion of the remainder consists of 'soft' assets such as telephony, IT and printing equipment, which tend to have low or no secondary values. Our estimated market share based on loan originations for 2014 was 3.0 per cent.

There are three distinct distribution channels within the Asset Finance market[13]: Direct, which is mostly dominated by large banks, accounted for around 50 per cent of the market, Vendor i.e. equipment manufacturers represented around 33 per cent, with the remainder being distributed by specialist commercial finance brokers.

Strategy

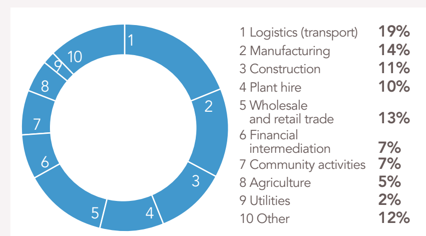
We aim to be our partners' 'funder of first choice' by being easy to do business with, quick to respond and consistent in our credit decisions, giving direct access to our underwriters when required.

We employ specialists across key industries including logistics, manufacturing, construction and agriculture with an in-depth understanding of our clients' businesses and the assets they require. In addition, we have a dedicated structured products team who can consider larger ticket, more complex transactions and receivables financing.

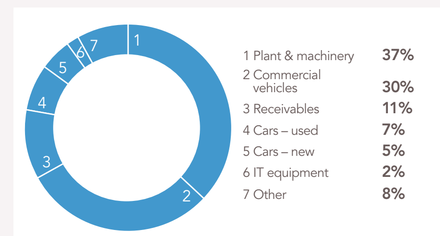
Our modern digital technology allows us to use expert human underwriting in a targeted and cost-effective way. Where we are unable to auto-accept a proposal, our credit experts will work with our introducers to better understand the transaction enabling us to consider every transaction on its own merit.

Since inception, our focus had been predominantly on hard assets distributed via brokers. During 2014, we expanded the range of assets we finance to include printing equipment, digital technologies, renewables and a wide array of soft assets. Building on our strong track record with our introducers, we also extended our distribution focus to Vendors.

Portfolio by sector (%)



Portfolio by product type



[13] Source: Finance & Leasing Association (Asset Finance).

Distribution

Aldermore currently works with a network of around 600 introducers who are supported by a national network of Aldermore business development managers and our central service team. These introducers accounted for around 75 per cent of loans originated during the year. The remaining 25 per cent of origination was generated via vendors, dealers and, through our wholesale channel.

Financial performance

2014 was another excellent year for our Asset Finance business with our portfolio exceeding £1 billion for the first time. Net loans grew by 45 per cent, and at the end of 2014 were £1,044.3 million (2013: £720.2 million) with customer numbers[14] up by 60 per cent to around 33,000. Our Asset Finance division has now advanced over £2 billion to UK businesses since its inception in 2009.

We grew organic origination to £739.5 million, up 21 per cent over prior year of £609.8 million. In the fourth quarter we launched our stocking finance product, to finance equipment dealers' inventory, which we expect to support growth of our vendor business in the future.

As expected, the enlarged portfolio generated significant growth in gross interest income, up 52 per cent to £56.7 million (2013: £37.4 million). Along with all of our lending lines, Asset Finance benefitted from a reduced cost of funding as we continue to diversify our funding sources. Net interest income grew by 60 per cent to £36.9 million (2013: £23.0 million) while net interest margin remained constant at 4.2 per cent.

The cost of risk improved by 17bps to 30bps (2013: 47bps) as it benefitted from a significant recovery.

Administrative expenses increased by 25 per cent to £11.9 million (2013: £9.5 million) as we continued to invest in the business. The segmental result almost doubled, growing at 97 per cent to £25.5 million (2013: £12.9 million).

Continued investment

We continued to invest in our digital capability and in the second half of 2014, launched our Asset Finance application for pricing and proposals, called APP+, making it easier for our introducers to get a quote for their clients anytime, anywhere and speeding up the credit approval process. Using a mobile or tablet, registered introducers can obtain a price, even on complicated quotes, within around 60 seconds.

Recently, we wrote off an investment in development of a system following a review of requirements. The related costs were included within central expenses.

Our Asset Finance team increased from 128 at the end of 2013 to 146 with a focus on front end sales-force to support our customers and introducers, and our credit team. We're pleased to see a lot of interest from people within the industry who are attracted by our approach to improve the customers' experience via human interaction rather than the credit scoring approach of some competitors.

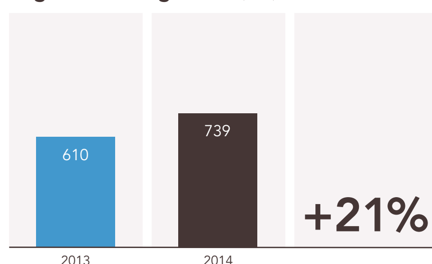
Around 100 of our employees completed our 'exceptional customer service training programme' which we implemented during the year.

We've also extended a new internal technical training programme to our key introducers' teams – free of charge – as we look to help develop the next generation of Asset Finance professionals across the industry. We received over 100 external applications and excellent feedback for what we believe is a unique initiative within the industry.

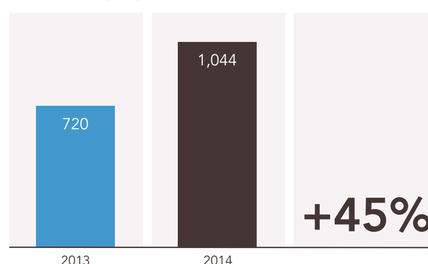
Outlook

As business confidence increases and SMEs look to catch up on investment delayed since the financial crisis, we expect the asset finance market as a whole to grow. We look to build on our strong foundations to continue to diversify the distribution and asset mix of our growing business.

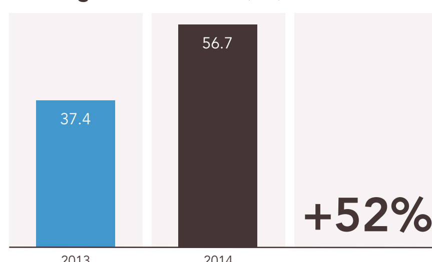
Organic loan origination (£m)



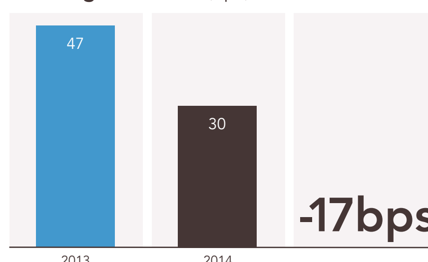
Net loans (£m)



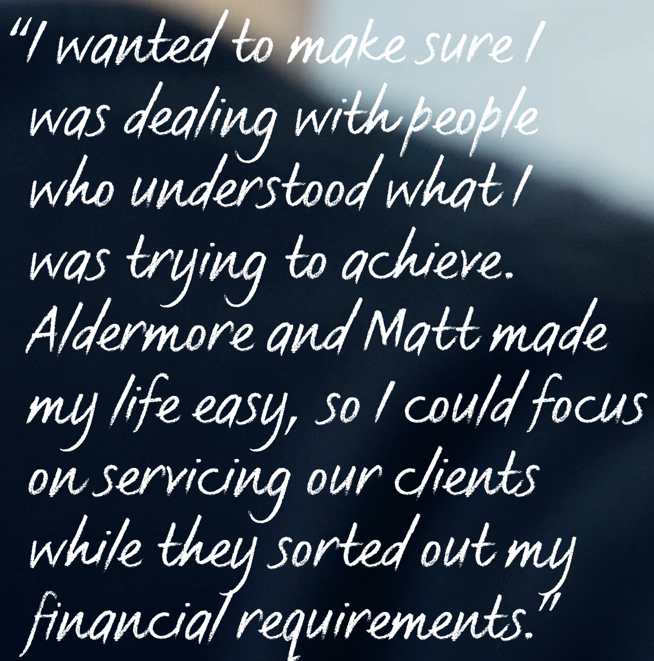
Growing interest income (£m)



Declining cost of risk (bps)



[14] As measured by customer accounts



Steve Knee
Managing Director
Cloudbass

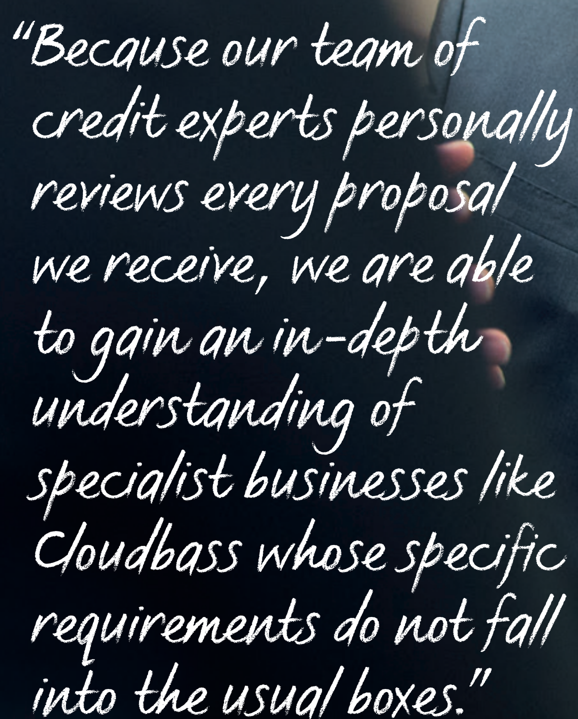
Cloudbass – Investing for growth

The challenge…

With clients including Sky, BT, ITV Sport, the BBC and Manchester United, Cloudbass is one of Britain's leading suppliers of outside broadcasting facilities and specialist crew. Recently, the company took advantage of the opportunity to expand its business when a key competitor exited the industry.

Cloudbass was able to buy out its competitor's contracts, which included the BBC's Question Time programmes and Premier League commitments. In order to fulfil these new contracts, the company needed to purchase additional specialist broadcast kit, including outside broadcasting vehicles and cameras.

Steve Knee, Managing Director at Cloudbass, required funding for these purchases and called in the help of Matt Vaughan at Asset Finance Solutions. Matt, who is one of our brokers, understood our strong commitment to helping companies like Cloudbass fulfil their potential and knew that we had the expertise and appetite to consider a deal of this complexity and find the right solution.



"Because our team of credit experts personally reviews every proposal we receive, we are able to gain an in-depth understanding of specialist businesses like Cloudbass whose specific requirements do not fall into the usual boxes."

David Ray
Business Development Manager
Aldermore

The solution...

When we initially reviewed the Cloudbass proposal, the rationale for the purchase was clear. Nevertheless the company required a large advance in relation to the size of the business for what are considered to be specialist assets.

Working in collaboration with Matt Vaughan, our underwriters took the time to get to know and fully understand the business along with the wider sector in which Cloudbass operates. We also took comfort in the strong management team and their industry experience.

In order to complement the Asset Finance solution provided, a facility through our Invoice Finance team was also included. The fact that Cloudbass needed to secure funding within a matter of weeks from winning the new contracts was not a problem for us. Due to working in close partnership with our introducer, we were able to deliver a solution within the required timescale.

Strategic report

Invoice Finance

2014 highlights

- Supporting UK SMEs with c.£1.4 billion of financing in 2014
- Segmental result up by 64% to £5.4 million
- Driven significant operational and process improvements
- Cost of risk improved to 174bps (2013: 290bps)
- Specialist Finance team created
- Construction Finance proposition launched

Awards

- Winner – Factor and Invoice Discounter of the Year (National Association of Commercial Finance Brokers (NACFB) Awards 2014)
- Winner – Alternative Funder of the Year (South West Dealmakers Awards 2014)
- Winner – Alternative Funder of the Year (Central and East of England Dealmakers Awards 2014)

Invoice Finance is an important working capital tool for SMEs. Aldermore will usually lend up to 85 per cent of the value of approved outstanding invoices issued by the borrower to its customers. There are two main products, Factoring and Discounting; with the difference being that with the former, Aldermore often takes control of the borrower's debt collection.

Our customers are typically owner-managed SMEs and we focus on key sectors including Manufacturing, Wholesale, Recruitment and Logistics.

Market

According to the Asset Based Finance Association (ABFA), gross advances for the first nine months of 2014 were around £19 billion and up by 12 per cent over the same period in 2013. However, the majority of this growth in pound terms was generated by companies with turnover greater than £50 million rather than our target customers who are at the smaller end of the turnover scale.

We estimate our market share to be around one per cent based on advances at the end of the third quarter of 2014.

Strategy

Invoice Finance currently represents around four per cent of our total lending portfolio and we expect it to continue to constitute a small part of our loan book.

Given the short-term nature of this product, with the underlying invoices translated into cash within 60 days, our average gross lending is equivalent to providing around £1.4 billion of working capital finance to UK SMEs in 2014.

We employ specialist service teams in our target sectors that spend time understanding our clients' business and design appropriate financing solutions. We offer simple and transparent solutions such as our ABC fixed fee Factoring product and look to provide a fast response with around 98 per cent of credit decisions made within 48 hours.

Following a small number of fraud cases in 2013, we have improved the controls across risk, operations and sales to build a sustainable platform for the future.

We are growing and upskilling our sales force and creating a trainee development plan to build the next generation of talent. From a product perspective, we will continue to innovate to meet our customers' needs and will expand our Specialist Finance team, who focus on construction, trade and export finance initiatives.

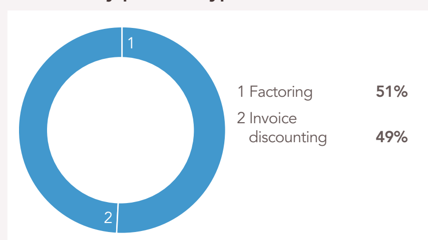
To date, we have generated strong growth in direct distribution and we plan ongoing investment in technology to enhance the customer experience and drive further growth from this channel.

Distribution

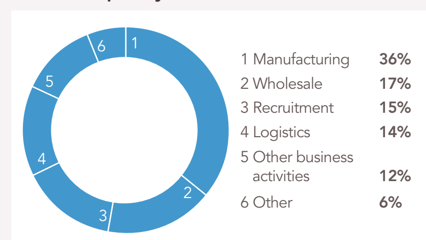
Our intermediated and direct distribution channels are supported by local relationship managers based in our 12 regional offices. We work with more than 500 intermediary groups at a local and national level who originated around 71 per cent of loans in 2014.

Direct distribution has grown rapidly in recent years and now represents around 29 per cent of origination.

Portfolio by product type



Portfolio split by sector



Financial performance

Our key focus for 2014 was to build a stable platform for the future. Following a small number of fraud cases, more than would normally be expected in 2013, we have substantially enhanced credit and operational procedures, centralised operations, refocused the portfolio towards customers with smaller turnover and exited a number of accounts. As a result of these actions, we reduced the overall size of the portfolio by £31.4 million or 15 per cent to £180.6 million (2013: £212.0 million).

Origination at £45.2 million (2013: £67.9 million) was also impacted by our focus on smaller clients.

Gross interest income remained consistent with the prior year at £9.3 million (2013: £9.4 million) and net interest income increased by 18 per cent to £5.9 million (2013: £5.1 million) as we benefitted from the reduced cost of funds associated with our ongoing funding diversification strategy. The mix between Factoring, which attracts higher fees for running a client's debtor ledger, and Discounting has stabilised, and as a result, fee income is also stable at £17.5 million (2013: £17.9 million).

Administration expenses of £14.7 million (2013: £14.0 million) reflect the ongoing investment to improve the operating platform.

We were pleased to see the result of our actions with cost of risk declining by 116bps to 174bps (2013: 290bps) in line with management expectations.

As a result, the segmental result improved by 64 per cent to £5.4 million.

Initiatives

In 2014, we set up a Specialist Finance team who launched a new Bad Debt Protection proposition, Construction Finance and Trade Finance solutions. We are also working with the Institute of Recruiters to continue to drive our proposition in this sector forward.

As well as working with existing intermediaries, we introduced a scheme to work with accounting firms to distribute Invoice Finance products to SMEs which has been well received.

Continued investment

During 2014, we upgraded our core systems and are piloting mobile technology via the launch of a pricing app with a quick quote calculator.

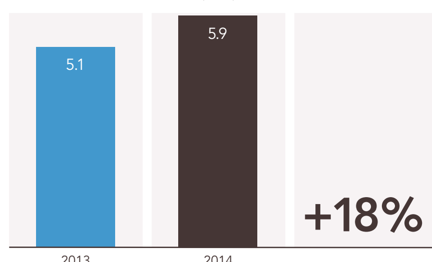
We have also focused on recruitment and training as a key element of building a sustainable platform for the future. We have appointed new Directors of Risk, Operations and Sales, invested in a Sales Excellence programme targeted at employees with the potential to be a regional sales manager within twelve months and launched an online Career Academy.

We were delighted to win 'Factor and Invoice Discounter of the Year – 2014' from the National Association of Commercial Finance Brokers (NACFB). Even more pleasing are the unedited comments provided by our customers on our online ratings and review service where our service is rated 4.7 out of 5.

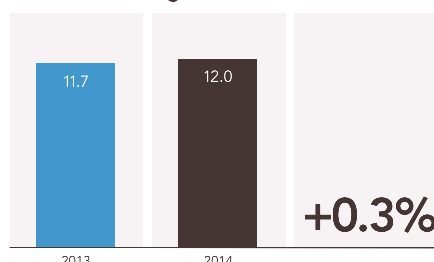
Outlook

Having stabilised the platform, we look forward to continuing to develop our Invoice Finance business and providing ongoing working capital support to UK SMEs.

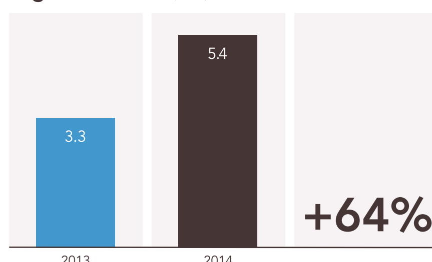
Net interest income (£m)



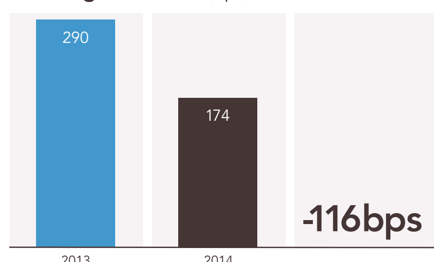
Net revenue margin (%)



Segmental result (£m)



Declining cost of risk (bps)



Invoice Finance Case Study

Richard Haines
Managing Director
Mainstream Direct

Mainstream Direct – Taking time to understand the business

The challenge…

Mainstream Direct, a family-run direct mail production business based in Northampton, did not feel that it was getting the support it required from its existing invoice finance provider. Richard Haines, the Managing Director of the company, wanted a funder who would take the time to understand his business and work closely with the company to help it continue its growth.

Richard mentioned this to his accountant, Gavin Parsons at Haines Watts, leading Gavin to direct him to Aldermore through our Accountancy Advice Scheme. The scheme, which was launched in 2014, sees us reward customers that come to us via an accountant with a voucher to redeem against further accountancy services.

Explaining his decision to refer Mainstream Direct to us, Gavin at Haines Watts said "Aldermore has developed a reputation for making the extra effort to understand their customers' needs and offer bespoke deals which fulfil their businesses' requirements. Recommending Aldermore to Mainstream Direct was an easy decision."

Jacques Alard
Relationship Manager
Aldermore

The solution…

Early on in the relationship, our Invoice Finance team visited Richard and his team at their premises to discuss their requirements and to walk them through the interfactor transfer process from their existing provider to Aldermore. We also explained the dedicated support that was on offer throughout the term of the facility.

Given the company's experience with its previous provider, it was important that we demonstrated that we would provide consistent support and always be on hand to assist. For instance, we were able to support the company with its credit control when it lost a member of staff responsible for processing invoices by providing guidance on managing the ledger and working through outstanding invoices.

As a result of our support, Mainstream Direct has been able to unlock cash to support its ambitious growth plans. The facility we provided has supported the company to expand its current services and diversify into new areas such as packaging for the printing industry.

SME Commercial Mortgages

2014 highlights

- Net lending up by 33% to £1.0 billion
- Organic origination of £421.9 million; up 45% over 2013
- Net interest income up by 64% to £41.6 million
- Record segmental result of £34.0 million

Awards

- Winner – Development Lender of the Year (Bridging & Commercial Awards 2014)
- Highly Commended – Commercial Lender of the Year (Bridging & Commercial Awards 2014)

Integrated approach

We offer a full range of mortgage products and whether a customer accesses us directly or via an intermediary, we aim to be easy to do business with and respond quickly.

During 2014, we brought our two mortgage businesses together under a single management team, supported by a single IT platform, to provide an integrated approach to our customers. We have a private rental sector proposition across the whole spectrum of property investment, supported by expert teams.

SME Commercial Mortgages

Aldermore offers mortgages to cover the full lifecycle from property development through to purchase and refinancing as well as bridging loans.

Our SME Commercial Mortgages business focuses on mortgages for shops, warehouses, industrial units, offices and professional buy-to-let, where the customer has more than five properties or is a corporate entity.

Our maximum loan size is £2 million on a single property or £5 million over multiple properties. The majority of the underlying assets are residential properties.

The portfolio is very granular, with the average loan size being £320,000. It is well secured with a maximum Loan to Value (LTV) of 75 per cent and an average indexed LTV ratio of 52 per cent.

Market

We estimate[15] that gross annual commercial mortgage origination is currently around £44 billion. Based on our 2014 origination of £421.9 million we estimate our market share to be around 1.0 per cent.

Strategy

We look to build on our ability as one of the few lenders who can offer a full spectrum of products from vanilla buy-to-let mortgages to complex Houses of Multiple Occupancy (HMO), commercial investments and commercial owner occupied. Having created a centre of excellence to support the private rental sector, we will continue to leverage our integrated approach to grow this part of the portfolio.

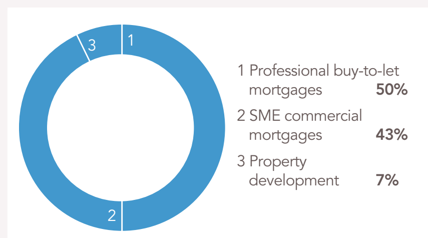
We work closely with our brokers to ensure we are easy to do business with and responsive, for more complex cases. We will continue to invest in our online portal technology to support this important channel.

Looking forward, we also seek to actively develop our direct business which to date has grown as a result of repeat business and referrals.

Distribution

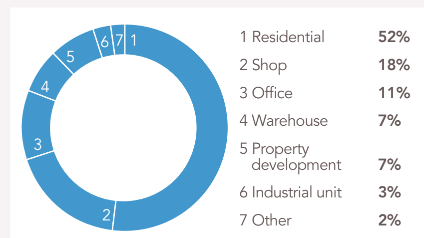
91 per cent of SME Commercial Mortgages originated during 2014 were distributed through our broker panel of around 1,000 brokers. The remaining 9 per cent were distributed directly.

Portfolio by product type



1 Professional buy-to-let mortgages	50%
2 SME commercial mortgages	43%
3 Property development	7%

Portfolio by asset type



1 Residential	52%
2 Shop	18%
3 Office	11%
4 Warehouse	7%
5 Property development	7%
6 Industrial unit	3%
7 Other	2%

[15] Estimates based on De Montfort University mid-year 2014 Commercial Property Lending Report.

Financial performance

We drove significant growth in 2014, with the SME Commercial Mortgages portfolio exceeding £1 billion for the first time.

Driven by an increase in customers[16] from 2,400 to 3,200, we delivered growth in net lending of 33 per cent to £1,011.3 million (2013: £762.0 million). We saw the success of our private rental sector initiative with professional buy-to-let growing by 24 per cent and now forming 50 per cent of the overall portfolio.

Organic origination of £421.9 million, increased by 45 per cent on the prior year (2013: £291.9 million). We have expanded our reach into the broker market with originations in 2014 up by 45 per cent through this channel.

Strong growth in net lending positively impacts our gross interest income, which is up by 41 per cent to £56.2 million while we have maintained our gross interest margin at 6.3 per cent (2013: 6.1 per cent). Funding costs across the Group have continued to decline with net interest margin improving to 4.7 per cent (2013: 3.9 per cent). Net interest income has grown by 64 per cent to £41.6 million (2013: £25.3 million).

We have retained our focus on credit quality as average loan size remains relatively small with a high proportion of tangible asset security. In addition, we benefitted from two large recoveries and this is reflected in the reduced cost of risk which at the end of 2014 was at 25bps (2013: 30bps).

The continued investment in the business is reflected in a 43 per cent increase in administrative expenses to £6.9 million (2013: £4.8 million).

Finally, the segmental result was £34.0 million (2013: £18.7 million), a record for this business.

Continued investment

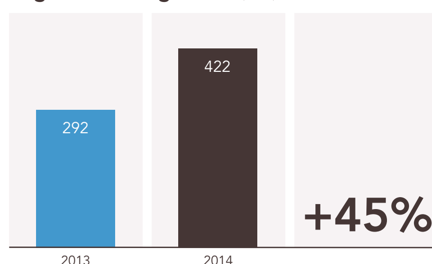
In 2014, we recruited a specialist team to focus on residential property development, developing a new IT platform to support our proposition. We also launched a new Bridging Finance product for brokers. Unlike many bridging lenders we look to offer a long term mortgage at the same time as bridging finance.

To support continued growth of the business, we have increased our sales force and also our back office operations. As a result our team has grown from 61 to 84 during 2014.

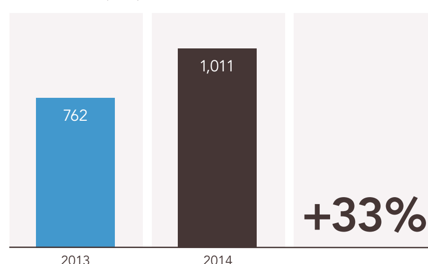
Outlook

Improving business confidence and an increasing need for rental properties are expected to boost demand for commercial mortgages in the medium term. We will continue to support our customers' financing needs, leveraging our modern technology to deliver excellent service.

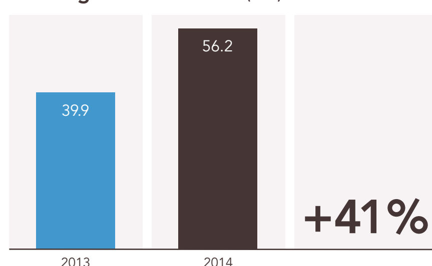
Organic loan origination (£m)



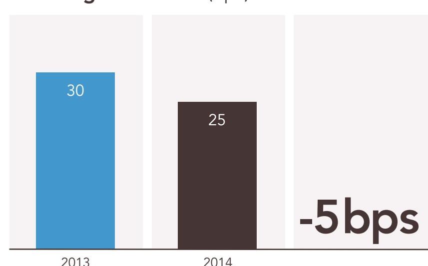
Net loans (£m)



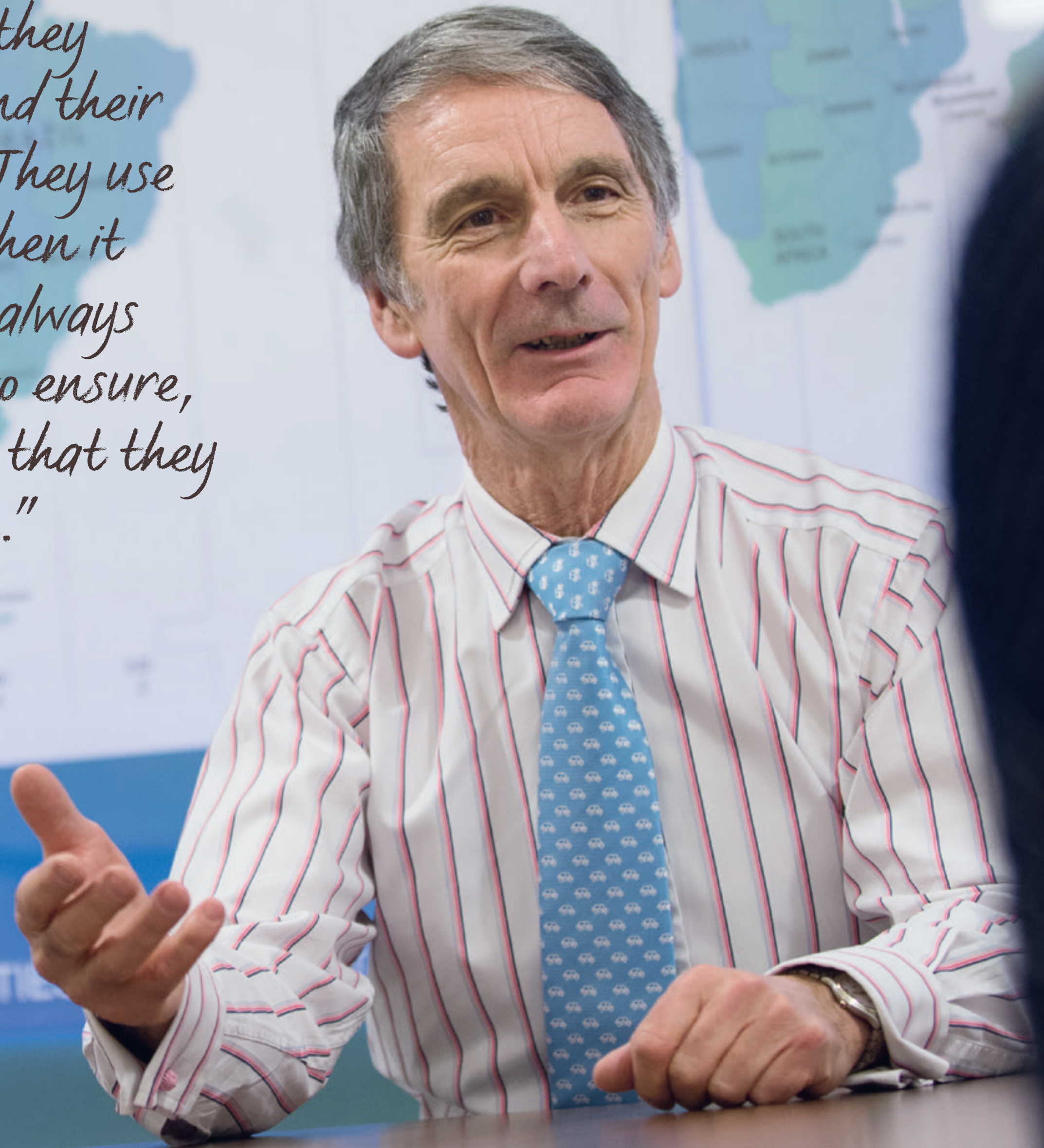
Growing interest income (£m)



Declining cost of risk (bps)



[16] As measured by customer accounts



"Aldermore are different from many other lenders in the way that they view the client and their circumstances. They use common sense when it matters and are always looking at ways to ensure, where they can, that they get the deal done."

Howard Thomas
Director
Howard Thomas Ltd

Howard Thomas – Getting the deal done at pace

The challenge…

When Howard Thomas's clients approached him to find them a commercial mortgage for the purchase of a ground floor retail unit with upstairs residential accommodation in Derby, he knew that Aldermore would be able to help.

Mr Thomas's clients are seasoned property owners with commercial and residential properties as part of their portfolios. The husband of the investment duo already held commercial property under his name, and on this occasion the couple wanted to extend the wife's residential portfolio to include a commercial property. The property in Derby represented the perfect opportunity.

The challenge with this application was the property had already been purchased at auction so needed a very quick completion. In fact, the timeline was so tight that the deal needed to be paid out within 13 working days from the date of the application in order to meet the auction house deadline.

"A deal like this would normally take between eight and twelve weeks from application to completion. To turn it around in thirteen days was a remarkable achievement by all involved and is the quickest I've ever seen a case go through for a commercial property purchase."

Lisa Baker
Commercial Mortgage Manager
Aldermore

The solution...

To meet the purchase deadline, everything about the deal had to be prioritised. As soon as Mr Thomas submitted his clients' application, we assessed it on the same day and sent back confirmation to Mr Thomas to proceed to valuation. The survey was booked for the following day.

We contacted the surveyor as soon as the valuation had taken place to ensure the case could be passed to our underwriters for approval as quickly as possible. Following our call to the surveyor, some reports were required which were needed as a condition of approval. Mr Thomas worked extremely quickly to obtain these reports which were satisfactory to clear the conditions by the time we received the valuation report.

Ultimately it was down to the great communication and speed of response from all parties, including Mr Thomas and his client, which enabled us to make an offer within four working days of the valuation instruction. Mr Thomas's clients were able to complete their purchase a mere eight working days after the initial offer was accepted, meeting their deadline.

Strategic report

Residential Mortgages

2014 Highlights

- Net lending up by 53% to £2.6 billion
- Organic loan origination exceeds £1.1 billion
- Net interest income doubled to £63.5 million
- Segmental result more than doubled to £56.8 million
- Cost of risk remains low at 6bps

Awards

- Winner – Best Specialist Lender (Financial Reporter Industry Awards 2014)
- Winner – Best Specialist Lender (Legal & General Mortgage Club Awards 2014)
- Winner – Best Specialist Lender (Mortgage Strategy Awards 2014) – third consecutive year
- Winner – Best Specialist Lender (Mortgage Force Awards)
- Winner – Best Specialist Lender (Pink Service Awards 2014)
- Winner – Best Lender Customer Service (What Mortgage Awards 2014)

Our Residential Mortgages business provides residential buy-to-let and owner-occupied mortgages with around 62 per cent of the portfolio currently being buy-to-let. In the owner-occupied sector we target underserved prime customers including the self-employed, professionals and first time buyers.

We offer a full product range with fixed, variable and discounted rates and although our maximum loan size is £1 million, the average loan size is much smaller at around £137,000.

Market

The UK residential mortgage market is large, with 2014 gross originations including buy-to-let, of £206 billion[17], giving Aldermore an estimated market share[18] of 0.6 per cent. Market originations are expected to grow[17] as the demand for housing continues.

Distribution through intermediaries remains a significant market feature[19] accounting for in excess of 50 per cent of total originations.

Strategy

We aim to get new customers into new homes and support small businesses including first time landlords. Our private rental sector team works across both residential and commercial segments providing a full suite of buy-to-let products and are able to deal with everything from an amateur landlord with one property to a professional investor with hundreds of properties. Within Residential Mortgages we focus on individuals where we can finance up to five properties.

Our owner-occupied business targets underserved prime customers who may fall outside the automated decisioning processes of some of our competitors, e.g. self-employed and first time buyers. We were also an early adopter of Government schemes such as the Help to Buy: mortgage guarantee scheme.

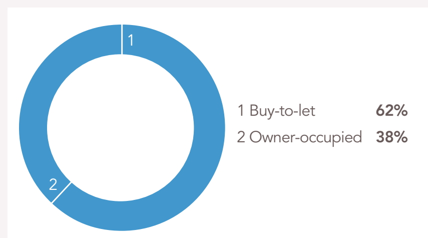
As in our other divisions, we aim to be easy to do business with, transparent and quick to respond. We benefit from our modern technology. In Residential Mortgages, our brokers are able to apply via an online portal and obtain a decision in principle within 90 seconds. This portal takes the application and links to external systems automatically completing basic identity, fraud and credit checks and builds an underwriting file highlighting any specific issues to our underwriters. This technology allows us to use targeted human underwriting in a cost-effective manner to make considered and consistent credit decisions.

Distribution

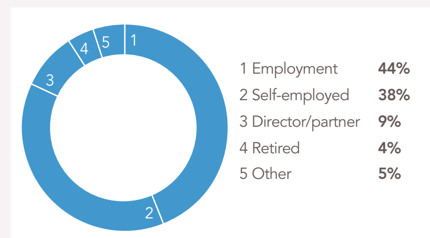
We enjoy strategic relationships with major UK distributors and in total work with around 12,000 brokers via our paperless bespoke broker portal. Around 88 per cent of 2014 originations were generated by brokers.

We have had a tremendous response to our direct to customer proposition and it now accounts for 12 per cent of all originations. Over time, we would expect the distribution mix between intermediated and direct to move towards market average levels.

Portfolio split by product type



Portfolio by customer type



17 Source: Council of Mortgage Lenders (CML) – December 2014.

18 Market share calculation based on loan originations in 2014.

19 Source: FSA – Mortgage Market Review: Distribution and Disclosure.

Financial performance

2014 was a record year for our Residential Mortgages business with net loans up by 53 per cent to £2.6 billion (2013: £1.7 billion) driven by an increase in number of customers[20] to 19,000 (2013: 13,000). The buy-to-let portfolio grew by 45 per cent during the year, while the owner occupied portfolio grew by 106 per cent thereby becoming a larger proportion of the overall portfolio at the end of 2014.

Originations exceeded £1.1 billion per annum for the first time, with Help to Buy mortgage guarantee scheme generating £189 million of loans in the year. Origination via brokers grew as we saw increased levels of repeat business from existing brokers. Direct originations were supported by the launch of our direct loyalty and retention programmes.

This significant growth resulted in an increase in interest income of 60 per cent to £106.9 million with our gross interest margin remaining stable at 5.0 per cent (2013: 5.1 per cent). Net interest income after funding costs doubled to £63.5 million (2013: £31.8 million) mainly driven by lower cost of funding, a feature across all our lending divisions.

We manage the credit quality of the portfolio carefully, with the average loan size remaining small at £139,000 and high asset security with indexed loan to value of 67 per cent. This control is reflected in the low cost of risk of 6bps (2013: 10bps).

Administrative expenses at £9.6 million grew at a much lower rate than growth in operating income. The segmental result more than doubled to £56.8 million (2013: £26.4 million).

Continued investment

We continue to invest in our systems to ensure they allow our customers and brokers to access us easily and support our underwriters. During 2014, we invested in a Bridging portal for intermediary applications which will be fully deployed in 2015.

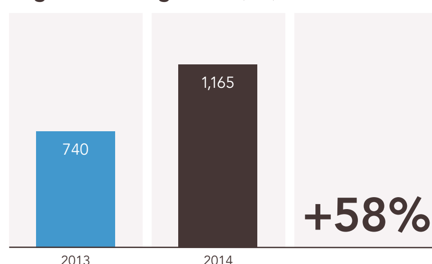
Our team grew from 97 at the end of 2013 to 132 by the end of 2014 as we invested in increasing our operations and risk functions.

We're delighted with the positive feedback we've had from customers via our online rating and reviews service where we scored 4.7 out of 5.

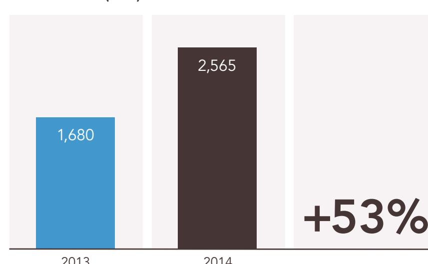
Outlook

There remains a fundamental shortage of new housing in the UK and we look to support efforts to alleviate this issue. We see significant growth opportunities in the underserved market segments we target and buy-to-let, which should continue to drive growth in our Residential Mortgages portfolio in 2015.

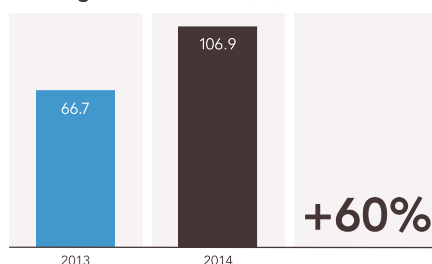
Organic loan origination (£m)



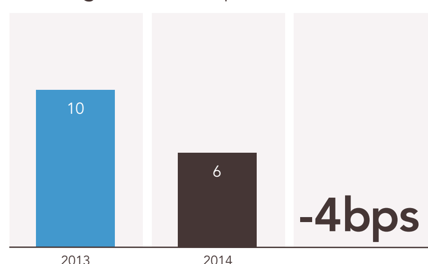
Net loans (£m)



Growing interest income (£m)



Declining cost of risk (bps)



[20] As measured by customer accounts

Malcolm and Julia Wiggins
Homeowners

The challenge…

Mr and Mrs Wiggins, a married couple who are both self-employed, were looking for their 'forever home' ahead of the birth of their first grandchild. They wanted somewhere with space for their growing family and soon found the perfect property – a lovely country house surrounded by fields and wildlife in Wales.

In order to purchase the property, the couple submitted a joint mortgage application to a major high street lender. Despite having significant equity in their existing property, they were not offered the terms they had requested, a decision that the lender only informed them of after 14 weeks had passed. Mr and Mrs Wiggins then approached their existing mortgage lender who declined their application to port their current mortgage.

After their second mortgage application was turned down, Mr and Mrs Wiggins became extremely worried that they were in danger of losing the house. Given the time that had elapsed since their original offer on the property had been accepted, there was extreme pressure on the chain and the vendor was threatening to pull out of the sale.

"I've spoken to Mr and Mrs Wiggins since they moved and they are extremely happy in their new home – in fact they said moving there is the best thing they've ever done. I'm really pleased that we were able to step in at the last minute to help them complete their purchase."

Gemma Donnelly
Mortgage Advisor
Aldermore

The solution…

Anxious to find a lender that would support them, Mr and Mrs Wiggins undertook an internet search and came across Aldermore. Fortunately we were able to quickly step in and do all within our power to help them meet their tight and demanding timeframe.

To better understand Mr and Mrs Wiggins's needs, we spoke to them on the phone before they submitted their application. Although they were both self-employed, their requirements seemed straightforward. However, to ensure that we gave the best advice, we needed to discuss their repayment plans as they had applied for an interest only mortgage on a residential property.

Due to these initial discussions, we were able to make an offer extremely quickly upon receiving the full application – within less than a week and a half. Throughout the process, we stayed in regular phone contact with the couple, remaining especially conscious of their prior experiences with other lenders. Mr and Mrs Wiggins were able to successfully complete their purchase and have since written to thank us for our support.

Strategic report

Savings

2014 highlights

- Total deposits grew by 29% to £4.5 billion
- SME deposits now exceed £1 billion
- SME Customised Fixed Rate Account (CFRA) launched
- Rated 4.6 out of 5 by our customers

Awards

- Four Time Winner – ISA Provider of the Year (Consumer Moneyfacts Awards 2011-14)
- Winner – Best Business Fixed Account Provider (Business Moneyfacts Awards 2014)
- Winner – Best Bank Savings Provider (Moneyfacts Awards 2014)
- Winner – Best Cash NISA (Online Personal Wealth Awards 2014 and 2013)
- Winner – Best Business Savings Account Provider (Savings Champion Awards 2014)
- Winner – Best Bank Savings Provider (Your Money Awards 2014)
- Winner – Best Online Savings Account Provider (Your Money Awards 2014)
- Winner – Best Online Cash ISA Provider (Your Money Awards 2014)
- Winner – Innovation in the SME Finance Sector (Business Moneyfacts Awards 2014)

Aldermore's dynamic online savings franchise anchors our funding base enabling us to support the financing needs of UK SMEs and homeowners.

We offer a range of award-winning, straightforward saving products to both Retail and SME customers and have recently expanded into the corporate savings market. Products include retail fixed term, notice, easy access and cash ISAs as well as SME fixed term and easy access accounts.

Market

The UK savings market is large at around £1.7 trillion[22] across both retail and SME/Corporate deposits and is steadily expanding. Aldermore has estimated market shares[23] of around 0.3 per cent in retail deposits and 0.2 per cent in SME/ Corporate deposits leaving substantial scope for future expansion without the need to target large market shares.

Strategy

We believe that saving should be as straightforward and as rewarding as possible for our customers.

For both retail and SME depositors, we aim to deliver exceptional service. Accounts can be opened and funded online within fifteen minutes as our modern IT systems and processes are able to link to external systems to complete key identity checks. We also offer phone and postal access for retail customers.

A key pillar of our brand is total transparency. We publish unedited reviews on our website which allows us to react to customer feedback, improving our offering, and allows potential customers to see what other savers think of our products and services. In this, we believe we are unique in the UK banking sector. We don't believe in products with gimmicks, teaser rates or introductory offers which the customer then has to keep an eye on.

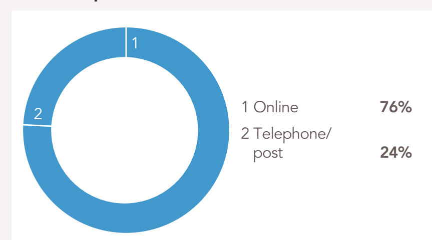
Having identified that SMEs' savings needs were as underserved as their lending needs, we launched our SME offering in 2012. We see strong opportunities for growth in both the SME and Corporate deposit market which we recently entered.

Distribution

Our distribution strategy is predominantly online with around 76 per cent of retail and almost all SME accounts opened via our website.

Deposits by customer type[21]

Retail deposits – distribution[24]



[21] SME deposits include corporate deposits

[22] Source: Bank of England. UK deposit pool comprises outstanding sterling deposits and repos for individuals (retail) and non-financial businesses (SME/Corporate)

[23] Based on deposits as at 31 December 2014

[24] Based on accounts opened in 2014

Growth

Our deposit business delivered another strong year of growth, with total deposits growing by 29 per cent to £4.5 billion (2013: £3.5 billion) and forming around 88 per cent of the Group's total funding base (2013: 90 per cent).

We now have almost 94,000 retail savers holding around 114,000 accounts (2013: 86,000 customers with 100,000 accounts) with total retail deposits growing by 16 per cent to £3.4 billion (2013: £2.9 billion).

Within three years, SME deposits have surpassed £1 billion and are nearly double the balance at the end of 2013 (£0.5 billion). SME customers increased to 11,000 (2013: 7,000) while number of accounts more than doubled to 14,500 (2013: 7,000).

Product innovation

At the start of 2014, we launched our Customised Fixed Rate Account (CFRA) for SMEs, with our modern, flexible systems enabling us to develop and launch this product within three months. This innovative account allows SMEs to decide the exact term of their deposit ranging from 60 days to five years and a maturity date dial will provide the corresponding interest rate. Alternatively, a customer can select the interest rate they want to earn and our system will calculate the maturity required. We believe this is the only account of its kind in the SME market and in less than a year represents around 11 per cent of our SME deposit base.

Ratings and reviews

We believe that reviews are an excellent way of providing a great customer experience for both existing and future customers and we are delighted that our customers currently rate us at 4.6 out of 5.

We take feedback seriously and take action to improve our services and products:

- during 2014 we changed our 0845 telephone number to a 0345 number so that calls would be free from mobile phones as well as landlines;
- we simplified our payments processes to make faster payment options more obvious; and
- a customer can now open a subsequent account in two clicks as we link automatically to data from the original account rather than making the customer repeat the full process.

Outlook

We will continue to provide transparent, straightforward and innovative products which meet the needs of both our Retail and SME depositors supported by exceptional customer service. During 2015, we also look to extend further into the corporate savings market.

Customer deposits[25] (£bn)

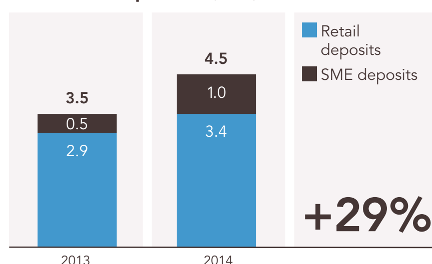
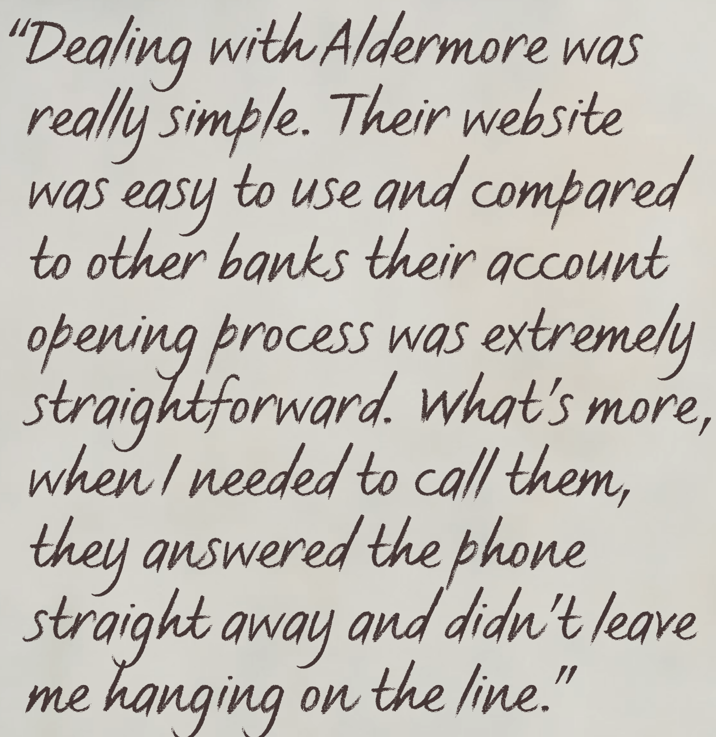


Illustration purposes only.
For more information on the Customised Fixed Rate Account please visit http://www.aldermore.co.uk

[25] SME deposits include corporate deposits. Numbers may not exactly sum due to rounding.



Steve Edwards
Managing Director
Silvertel

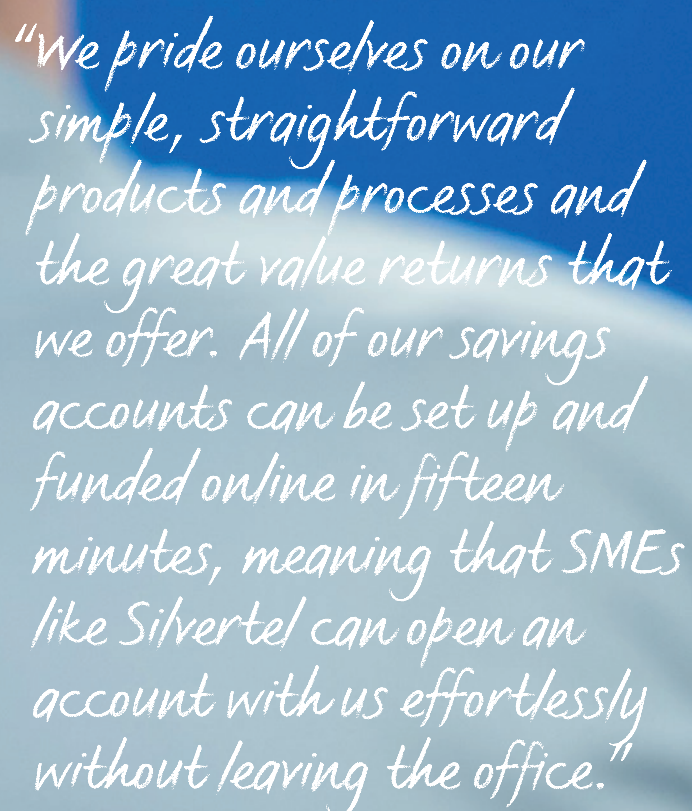
Silvertel – Allowing customers to choose their own terms

The challenge...

Silvertel, which is based in Newport in Wales, specialises in developing and supplying electronic components to an extensive customer base including many leading technology, telecoms and security companies around the world. The business was founded by electronics graduate Steve Edwards in 1997.

Steve keeps spare cash in reserve in case of an emergency. He cannot lock this money away for long periods of time since he never knows when the company may need to access it at short notice, however there is the flexibility to lock it away for a few months at a time. Steve was disappointed with the rate he was getting from the company's main high street bank so began looking at other options.

Steve had not previously heard of Aldermore and came across us through a search on a price comparison website. He also read a number of independent reviews of Aldermore online which talked positively about us. Intrigued by what he had seen, Steve was persuaded to come to us for his company's savings needs.



"We pride ourselves on our simple, straightforward products and processes and the great value returns that we offer. All of our savings accounts can be set up and funded online in fifteen minutes, meaning that SMEs like Silvertel can open an account with us effortlessly without leaving the office."

Richard Taylor
Head of Products, Savings
Aldermore

The solution…

Steve decided that our Customised Fixed Rate Account (CFRA) was right for Silvertel. With the account, customers do not have to adhere to a maturity date chosen by us; instead they can select any date between 60 days to five years, with the interest rate increasing the longer they leave their money with us. We believe it is the only account of its kind for SMEs.

The ability to select a maturity date has proved useful for Silvertel. It allows Steve to fix the term for a few months at a time before rolling the funds over for another fixed term – something he has done several times since opening the account. In fact, he was so impressed with his experience of Aldermore that he has since opened a personal savings account with us too.

We developed the CFRA after speaking to hundreds of SMEs who told us that, as well as good returns and straightforward processes, they require flexibility from their savings accounts. The account is one example of how we put customers at the heart of what we do.

Principal risks and uncertainties

This section describes the principal risks and uncertainties to which the Group is exposed along with the Group's approach to mitigating these risks.

All of the risks described within this section are classified as principal risks within the Group's Risk Management Framework and are considered to be important to the future development, performance and position of the Group. However, there is a sub set of these principal risks which are deemed to be more pertinent given the Group's current circumstances. These particular risks reflect the Group's development and growth strategy:

- credit risk: in particular, given the unseasoned nature of the book, there is a future risk that the underlying credit impairment loss trends differ from the Group's current expectations;
- capital risk: as the Group continues to follow a growth strategy, there is a risk that the Group has insufficient capital to cover regulatory requirements;
- operational risk: given the growth strategy, there is a risk that the operational infrastructure is inadequate to support the Group. The Group currently has a significant transformation and change agenda which includes the concurrent running of numerous projects. These projects include IT based projects designed to ensure that the Group's infrastructure remains modern and scalable, to support the Group's growth strategy. Therefore the Group is exposed to execution risk on these projects. During 2014, an element of this risk crystallised resulting in a £1.6 million write off of an intangible asset.

Each of these risks, along with how the Group mitigates them, is discussed in detail below.

The Group's Risk Management Framework is designed to ensure that risks are identified, assessed, managed and monitored effectively. Group Risk provides oversight of the risk profile. Each risk has a defined risk appetite which is controlled through documented policies and regular reporting, and is monitored and overseen by one or more committees as part of the Group's governance process.

Further detail regarding the Risk Management Framework is provided in Note 40 and specific detail on capital management is provided in Note 41. Further details regarding the management of strategic risk, operational risk and conduct risk are presented below.

Current risks

Economy

The economic environment is relatively stable within the UK, with growth across most sectors and contained inflationary risks. However, international geopolitical risks are increasing in the EU, Russia and China which may adversely affect the UK and these developments are being closely monitored. Deflation and contraction, especially in the EU economies, could act as a drag on the UK, and central London property price softening could broaden out. The Group is not exposed to any direct risks of a possible Greek exit from the eurozone.

Recent deflationary pressures, exacerbated by reducing oil prices have reduced and flattened the yield curve and have extended the timing for near-term interest rate increases.

The Group has a material proportion of mortgage assets which are sensitive to interest rate rises, therefore the reduced interest rates in the near term will lower the risk on affordability pressures linked to rising interest rates.

Oil & gas sector

Falling oil prices over a prolonged period are likely to affect property and asset values for companies involved in the oil industry, especially for property values in Aberdeen, Scotland. The Group has a very modest exposure to this risk and there are no immediate signs of stress apparent, but the position is being closely monitored.

Cyber risk

As the Group continues to grow, with a number of projects running, operational risk will continue to remain an area of focus. Operational risks such as cyber risk and IT security are reviewed at Board level as well as at management level committees. Cyber risk is a high profile issue for banks and cyber risk threats are expected to increase over time for the industry. The Group's current position in managing cyber risks has been reviewed during 2014 and control enhancements made. Further investment and actions are planned for 2015 to increase protection against IT security and IT resilience risks.

The following table details all of the risks classified as principal risks within the Group's Risk Management Framework.

Strategic risk

Definition	Mitigation of risk
The risk which can affect the Group's ability to achieve its corporate and strategic objectives.	Strategic risk is particularly important as the Group continues its growth strategy. The Group seeks to mitigate strategic risk by focusing on a sustainable business model which is aligned to the Group's business strategy. Strategic risk can arise as a result of both internal and external factors. The Group seeks to identify and mitigate the individual components of strategic risk through the application of the Risk Management Framework. Further details of strategic risk are provided below.

Credit risk

Definition
The risk of financial loss arising from a borrower failing to meet their financial obligations to the Group in accordance with agreed terms.

Mitigation of risk
The Group seeks to mitigate credit risk by focusing on business sectors where it has specific expertise and through limiting concentration of exposures of larger loans and or geographical and business sectors, especially where there are higher levels of risk. The Group also seeks to obtain security cover, and where appropriate, personal guarantees from borrowers.

The Group uses detailed lending policies tailored to each business area which outline the approach to lending, underwriting criteria, credit mandates, concentration limits and product terms. The Group maintains a dynamic approach to credit management. Its lending policies and performance against risk appetites are regularly reviewed and the Group will take necessary steps if specific issues are identified or expected to deteriorate, due to economic, sector or borrower specific weaknesses.

External rating agency ratings for borrowers are not typically available in the specialist segments in the retail and SME markets in which the Group operates. Credit risk is, instead, assessed through a combination of due diligence, reviewing credit reference agency reports, reviewing financial information, credit scores and the use of underwriting expertise.

As a growing business with a relatively unseasoned loan book, there remains a risk that the level of credit risk incurred to date is not reflective of the future credit risk which may be incurred as the loan book matures.

The Group actively manages credit risk as described above and is cognisant of the relatively unseasoned nature of the book as it reviews credit performance. See page 104 for further analysis.

Capital risk

Definition
The risk that the Group has insufficient capital to cover regulatory requirements and growth plans.

Mitigation of risk
The Group undertakes certain activities to manage and mitigate capital risk. The primary mechanism to ensure that sufficient capital is held is through regulating the volume of asset origination. In addition, capital risk management activities include monthly capital forecasting over a period of 12-18 months designed to provide a forward view on capital allocation and excess regulatory capital. Furthermore, stress testing and sensitivity analysis is performed to provide information on the Group's capital position. Capital requirements under stressed conditions are considered as part of the Group's Internal Capital Adequacy Assessment Process.

In December 2014, the Group has raised further capital in the form of Additional Tier 1 securities to enable it to continue its growth strategy. There will continue to be a keen focus on capital management to ensure that the Group has a capital structure which is both compliant with the relevant regulatory requirements and also supports the Group's growth strategy. See page 119 for further analysis.

Liquidity risk

Definition
The risk that the Group is not able to meet its financial obligations as they fall due, or can do so only at excessive cost.

Mitigation of risk
To protect the Group and its depositors, the Group maintains a liquidity buffer, which is based on its liquidity needs under stressed conditions. The liquidity buffer is monitored on a daily basis to ensure there are sufficient liquid assets at all times to cover cash flow movements and fluctuations in funding and to enable the Group to meet all financial obligations and to support anticipated asset growth. Liquidity requirements under stressed conditions are considered as part of the ILAA process. Through the ILAA process, the Group has assessed the level of liquidity necessary to prudently cover systemic and idiosyncratic risks and the ILAA process determines the appropriate liquidity buffer, taking into account the specific nature of the deposit base. See page 115 for further analysis.

Interest rate risk

Definition
The risk of financial loss through un-hedged or mismatched asset and liability positions sensitive to changes in interest rates.

Mitigation of risk
Where possible the Group seeks to match the interest rate structure of assets with liabilities or deposits creating a natural hedge. Where this is not possible the Group will enter into swap agreements to convert fixed interest rate liabilities into variable rate liabilities, which are then matched with variable interest rate assets. See page 117 for further analysis.

Principal risks and uncertainties continued

Market risk

Definition	Mitigation of risk
The financial impact from movements in market prices on the value of assets and liabilities.	The Group does not seek to take or expose itself to market risk, and does not carry out proprietary trading, although certain liquid asset investments which form part of the liquid asset buffer may carry a limited amount of mark-to-market risk which is regularly monitored. It is accordingly considered that there is minimal exposure to market risk. See page 117 for further analysis.

Operational risk

Definition	Mitigation of risk
The risk of financial loss and/or reputational damage resulting from inadequate or failed internal processes, people and systems or from external events including financial crime.	The Group aims to minimise operational failures through the establishment and subsequent investment in sound systems, controls and audit functions. Further details are provided below.

Conduct risk

Definition	Mitigation of risk
The risk of detriment to the Group's customers due to the inappropriate execution of its business activities and processes.	The Group has a zero appetite for systemic unfair outcomes that may result in significant detriment to the Group's customers. However, occasional failures in operational processes may occur, for example administration and processing errors or interruptions to IT systems. These occasional events may have an impact on customers leading to customer detriment. The Group has set a tolerance around the detriment caused through such non-systemic process failings. The Group has reviewed its conduct risk framework and is rolling out further improvements in 2015. The Group mitigates conduct risk by monitoring various operational metrics and by tracking activities which affect customers, monitoring customer complaints, implementing process improvements and adhering to service standards. Further details are provided below.

Strategic risk

As described above, the Group seeks to mitigate strategic risk through the application of the Risk Management Framework. The section below provides further details of how strategic risk can arise.

The Group's strategic direction and performance is impacted by external factors (that are similar to those impacting other financial institutions) and internal operational factors.

External factors

External factors include uncertainty around future interest rate movements and increased competition, especially from new entrants to the market, which may challenge product and pricing margins. The Group closely monitors competitor activity, pricing, and customer behaviour and feedback and reflects this in pricing and marketing plans.

As with other financial institutions, the Group is also affected by the level of litigation activity environment. However, the Group has not sold any PPI products and only provides advice to retail mortgage customers on a limited basis. The Group does not currently operate in the retail lending space of unsecured personal loans, credit cards or current accounts.

As a regulated business, the Group must also comply with the complex and changing regulatory environment. Prudential and conduct regulation continues to evolve and the Group maintains regulatory monitoring activity to understand future requirements and how this may affect the Group. To comply with current prudential regulatory requirements, the Group maintains adequate capital and liquidity resources to satisfy these requirements at all times. Notwithstanding, the Group's borrowing costs and capital requirements could be affected by future prudential regulatory developments.

There remains a keen focus on capital management to ensure that the Group has an appropriate capital structure in place to support the Group's growth strategy.

The Group has a zero risk appetite for material regulatory breaches. To ensure compliance with regulatory requirements, the Group has policies, processes and standards which provide the framework for business activities and staff to operate to which are in accordance with the laws, regulations and voluntary codes which apply to the Group and its activities. Compliance with regulation incurs significant costs which are factored into the operational cost and are considered in relation to the specific products and services that the Group offers.

Internal factors
Internal factors which impact strategic risk include the adequacy of IT systems, data security, project management, supplier and outsourcing arrangements and from internal and third party fraud and compliance failings. As the Group grows it continues to monitor the adequacy and ability of its third party suppliers to support the Group, now and in the future and where necessary will seek alternative arrangements.

The Group distribution strategy involves the use of intermediaries based in the UK. As a result of this strategy, the Group is exposed to the risk inherent in relying on third parties to sell and promote products. There is a risk that intermediaries act inappropriately or fail to adhere to applicable conduct regulations or standards in the sale of the Group's loan products, which could harm the Group's brand and/or reputation. Other risks include that the Group may fail to develop products that are attractive to intermediaries or otherwise not succeed in developing relationships with intermediaries and could therefore lose the service of intermediaries.

Operational risk

A key internal factor is operational risk, which is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This risk includes IT, information security, project, outsourcing, tax, legal, fraud and compliance risks.

The Group aims to maintain robust operational systems and controls and seeks to operate within the defined level of operational risk. The operational risk appetite considers risk events, the assessment of internal controls as well as holding additional capital for certain operational risks.

As part of the operational risk management process, the Group has an Operational Risk Policy, and undertakes a Risk & Control Self-Assessment process across the Group, and has business continuity plans in place. The Group uses an Enterprise Risk Management system to support the recording of risks and controls as well as monitoring operational risks and risk events.

Through the establishment of, and investment in, sound systems, controls and audit functions, the Group aims to minimise's operational failures. Operational risk is reviewed by the Business Risk Committee, which meets monthly to ensure that a quality and robust IT, operations and compliance service is delivered at all times and is capable of supporting the changing business requirements of the Group. It has responsibility for monitoring all the key operational risks facing the organisation, including compliance and operational risks. The Business Risk Committee provides a monthly report to the Executive Risk Committee on operational risk matters.

The Group has placed emphasis on ensuring that the IT infrastructure, performance, resilience, and security meet the on-going needs of the business. In particular significant investment in cyber risk controls to ensure that the Group maintains appropriate levels of controls to counter the increasing threat of cyber-crime across the banking and financial services industries.

The Group currently has a significant change agenda which includes the concurrent running of numerous projects. These projects include IT based projects designed to ensure that the Group's infrastructure remains modern and scalable, to support the Group's growth strategy. Therefore the Group is exposed to execution risk on these projects.

Conduct risk

Conduct risk is the risk of detriment caused to the Group's customers due to the inappropriate execution of its business activities and processes. The Group extends the definition of 'customer' to include both retail and SME commercial customers (but excludes intermediaries and/other third parties) across all business segments, including both regulated and non-regulated activities, thereby applying its conduct risk policies to all lending and deposit-taking activities.

The Group has a zero appetite for systemic unfair outcomes, which may result in significant detriment to the Group's customers. Systemic unfair outcomes may arise from poor product design, poor sale processes or unacceptable operational practices which risk repeated or continual outcomes which are detrimental to customers.

However, occasional failures in operational processes may occur, for example administration and processing errors or interruptions to IT systems. These occasional events may have an impact on customers, leading to customer detriment. The Group has set a tolerance around the detriment caused through such non-systemic process failings.

The risk is that customers can suffer detriment due to actions, processes or products which originate from within the Group. Conduct risk can arise through the design of products that do not meet customers' needs, mishandling complaints where the Group has behaved inappropriately towards its customers, inappropriate sale processes and exhibiting behaviour that does not meet market or regulatory standards.

Customer detriment could affect the Group's reputation, lead to loss of market share due to damage to Aldermore's brand, may lead to customer redress payments and could lead to regulatory action and censure.

The Group mitigates conduct risk by monitoring various operational metrics and by tracking activities which affect customers, monitoring customer complaints, implementing process improvements and adhering to service standards. The conduct risk metrics (which include among others, staff performance levels, training, customer feedback and complaints, product retention rates and cancellations, arrears levels and customer service standards) vary across the business lines and consist of individual business line conduct risk KPIs, the sum of which is measured against the risk appetite.

Conduct risk metrics and KPIs are in place to evidence fair outcomes, identify any emerging issues and document remedial actions. Each customer-facing area is responsible for implementing controls designed to manage and report on conduct risk, which includes understanding how customer detriment may occur, how it is identified and how it is prevented going forward. Conduct risk is monitored by the Business Risk Committee.

Strategic report

Our customers, people and communities

By acting in a socially beneficial and ethical manner, we are both contributing to the communities where we operate and also supporting our strategy, long-term performance and the sustainability of our business.

Our brand pillars – total transparency, exceptional service and community – shape everything we do and inform our approach to our customers, our people and our communities.

Businesses that last have a purpose beyond simply making money. This is why we are committed to fulfilling the responsibilities that come with being a British bank supporting SMEs, homeowners and savers.

Our customers

Our aim is to deliver exceptional service. By exceeding customers' expectations, we are differentiating Aldermore from its competitors, helping to attract and retain customers.

We continue to focus on our digital infrastructure to ensure that our customers can interact with us whenever is most convenient for them. Visits to our website exceeded 1.85 million in 2014, up 19 per cent. Over 76 per cent of retail savings applications and all of our SME savings applications are now taken online.

At the end of 2014, we relaunched our website to simplify the customer journey and improve usability. Navigation is now customer-led, meaning visitors can select who they are, to help them find suitable products and services. The website is tablet and mobile friendly to enable visitors to access the information they need wherever they are.

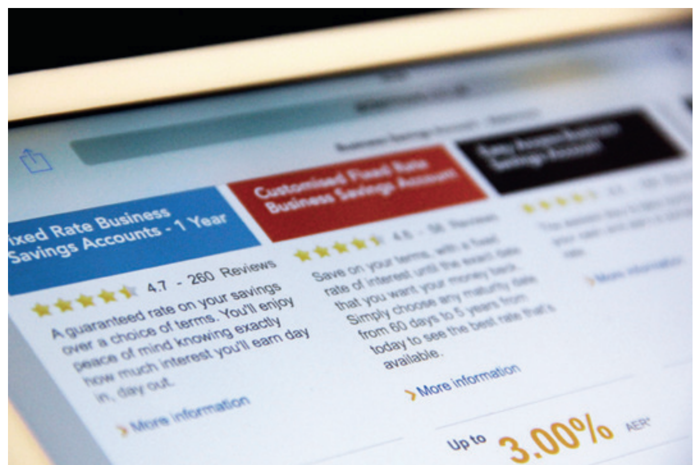
We are dedicated to transparency in everything we do. In 2012, we launched unedited ratings and reviews on our website, giving every customer the opportunity to comment on our products and services online. Initially launched for Retail Deposits, SME Deposits and Invoice Finance, we extended the service to Residential Mortgage customers in 2014. We received 1,904 reviews across our Ratings & Reviews service during 2014 and achieved an average rating of 4.6 out of 5, something we are very proud of and an endorsement of our approach.

Not all of the feedback we receive is positive and there are times we fall short. If we receive a complaint, it is investigated by the relevant business line and reported to our Executive Team.

We actively use feedback from our customers to improve our products and processes.

In 2014, improvements included changing our 0845 telephone number to a 0345 number so that calls are free from mobile phones as well as landlines; simplifying our payments processes to make faster payment options more obvious; and streamlining the process for opening multiple accounts by linking automatically to data from the original account instead of making the customer repeat the full process.

Ratings & Reviews
We read every comment that we receive through our online Ratings & Reviews service. Customers regularly suggest improvements to our products and services and we always consider these suggestions when developing our offering.



Our people

In 2014, the number of people we employ increased by 28 per cent taking the total number of employees to 876. To support this growth, we focused on our recruitment and induction processes. Recognising the importance of social media for reaching key talent, we have increased our use of channels such as LinkedIn for recruitment.

In the second half of 2014, we centralised our induction programme to ensure a consistent introduction to the Group for all new starters. Each new starter is invited to a full day workshop in which they learn about our brand, values, approach to risk management and our products and services.

We are committed to employee engagement at Aldermore. To reward and recognise the contribution our people make, we relaunched our REDStar recognition scheme which rewards our people for going above and beyond. The scheme now sees us rewarding weekly nominees and quarterly overall winners. Throughout the year we received 358 REDStar nominations.

We also understand that clear career progression has a positive impact on employee motivation. During 2014, 137 of our people were promoted or moved into new roles and 27 per cent of positions were filled internally. To encourage career development, we launched a 'Building Your Career' toolkit which is now widely used and accessible to all.

We place a great deal of importance on ensuring that the lines of communication between our people and the Group's leaders are two-way and transparent. We have continued our programme of Executive visits to our regional offices during which our people are able to meet and hear from senior members of the Aldermore team.

We hold an annual employee roadshow in which we bring our people together to update them on the Group's vision and strategy. The roadshow also provides a forum for our people to pose questions to the Executive Team and to network with their colleagues. Roadshow events were held in Manchester, Leicester and Reading to enable all of our people to attend regardless of their geographical location. Following the roadshow, 84 per cent of respondents felt they had a good understanding of our vision and strategy.

At the end of 2014, we took part in the Sunday Times 'Best Companies to Work For' survey and were accredited as 'One to Watch'. We are very proud of this recognition and our people are clearly proud to work for Aldermore.

Our communities

We make a real effort to give back to our communities, whether it is supporting the country's vital SME community, making a positive contribution to the local communities in which we operate or behaving as a responsible member of the UK's financial services community.

Our commitment to Britain's SME community extends beyond simply providing lending to businesses. In September, we piloted our first 'Helping You Grow Your Business' event, inviting our customers and introducers to a topical discussion on industry trends which included representation from the Bank of England. It also provided individuals the opportunity to network with like-minded businesses.

We realise the importance of sharing our industry insight as widely as possible, which is why we produce regular industry research. In 2014, this included our quarterly 'SME Monitor' report produced in conjunction with the Centre for Economics and Business Research (Cebr) which looked at cost inflation amongst Britain's SMEs. Our 'Saving SMEs' report provided a measure of the business savings market by analysing SMEs' attitudes towards saving.

Best Companies 'One to Watch' accreditation
We have been awarded 'One to Watch' status by Best Companies to Work For, acknowledging our progress towards making Aldermore a great place to work. The Best Companies Index is recognised as a leading measure of workplace excellence.

Executive roadshow
We are committed to giving our people regular updates on the Group's strategic vision and direction. Our annual Executive roadshow ensures that all employees hear directly from our Executives and can ask any questions they may have.

Our customers, people and communities continued

Aldermore Community Team
The Aldermore Community Team (ACT) was established in October 2014 to enhance our 'Community' brand pillar and is responsible for our community and fundraising initiatives. We have ACT champions based in each of our 12 offices.

Our communities continued

We also recognise our duty to help our intermediary partners deliver exceptional service to their SME clients. To support the commercial finance broker community, we launched our 'Next Generation Training Academy' which sees us provide training to junior staff at our Asset Finance broker partners. This initiative has reinforced our broker relationships and is another way we are helping SMEs to access the expertise they need.

Recognising the important contribution made by entrepreneurs to the British economy, we support the SKILL! Programme which promotes business skills and entrepreneurialism amongst young people. This year our staff acted as corporate mentors to budding entrepreneurs at schools in Manchester, Reading and Peterborough.

We regularly run community and fundraising activities. In October 2014, we launched the Aldermore Community Team (ACT), a group of volunteers spanning our offices who are responsible for managing these initiatives. The team has already staged several fundraising events coordinated across the Group.

Our £ for £ Matching Scheme sees us top up charitable contributions made by our employees. Through the scheme we donated £11,360 to non-profit and community organisations during 2014. Causes supported included the Royal British Legion, Macmillan Cancer Support and Help the Hospices.

Through our support for Government schemes encouraging lending to businesses and homeowners, we aim to play our part in Britain's banking community. Aldermore has been an enthusiastic participant in the Funding for Lending Scheme, providing much-needed credit to Britain's SMEs, and was an early adopter of the Help to Buy scheme.

As a bank supporting over 160,000 customers, it is vital that we contribute our views to industry discussions and respond to Government consultations on the banking needs of SMEs and individuals. The evidence we gave to the Business, Innovation and Skills Select Committee on the Government's support for SMEs in December is just one instance where we have been able to share our experiences.

Our communities are extremely important to us and we are committed to making a positive contribution to them. In this way, we are not only giving something back but also supporting the long-term performance and sustainability of Aldermore.

Approved by the Board and signed on its behalf by:

Phillip Monks
Director

16 February 2015

Corporate governance report

Introduction

This aim of this Corporate governance report is to provide shareholders with a clear view of the Group's corporate governance approach.

The Group is committed to the highest standards of corporate governance. The corporate governance of the Group has evolved during the year in order to strengthen further the robust framework by which the Group is governed. This report represents the position as at 2014 year-end unless stated otherwise. The following sections provide details of the role and composition of the Board, its Committees and other key individuals and committees.

Aldermore Bank PLC is owned 100 per cent by Aldermore Group PLC. During the year, changes were made to conform the respective Boards so that the same Directors served on both Boards.

This Corporate governance report includes the following sections:

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b. Roles and responsibilities of the Board
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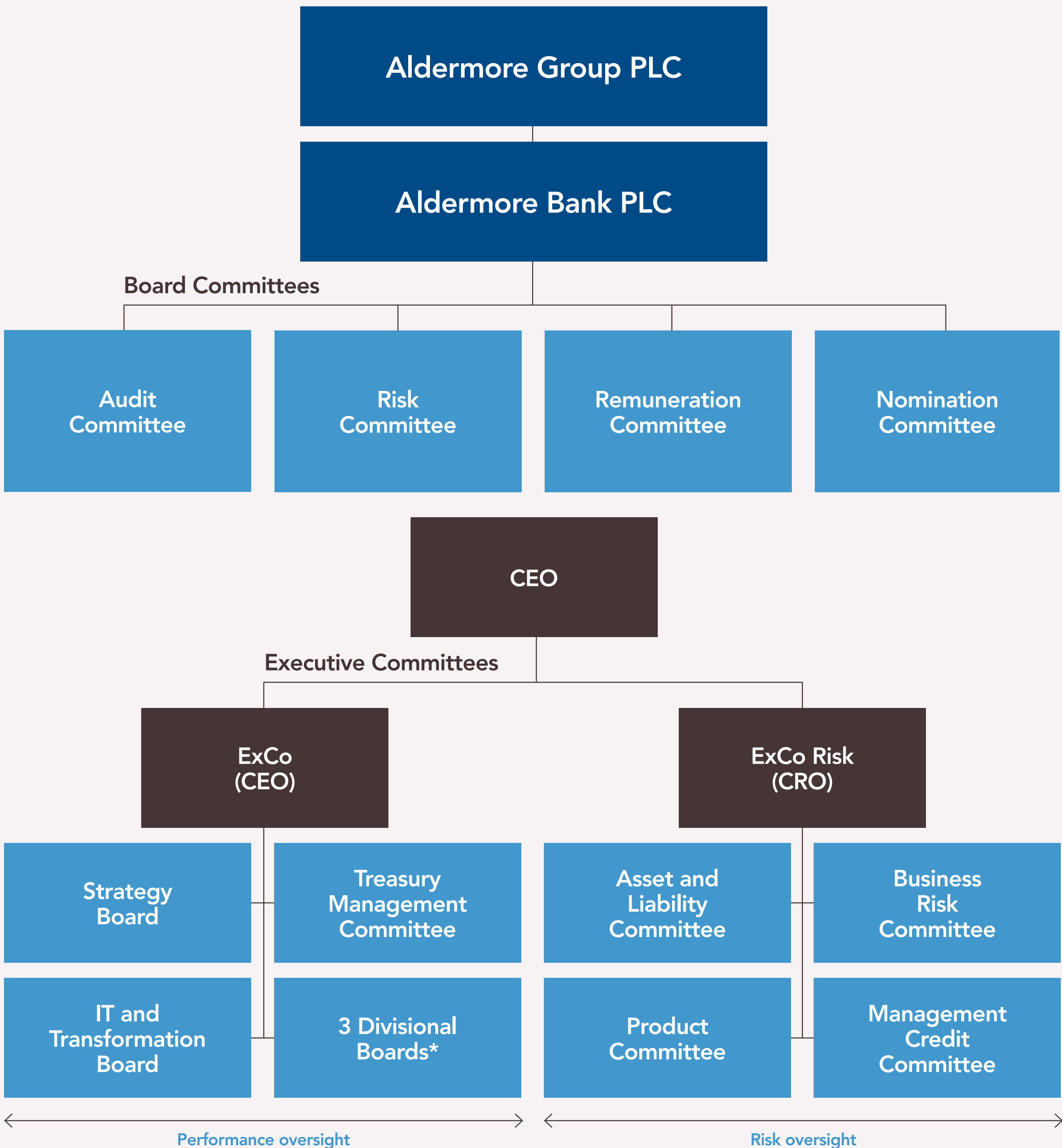
Governance

Corporate governance report continued

1. Overview of the Corporate Governance Structure as at 1 January 2015



* Divisional Boards comprise of: Mortgages Board, Commercial Finance Board (Asset Finance and Invoice Finance) and Savings Board

2. The Board

a. Board composition as at 31 December 2014

The Board

Non-Executive Directors:

Glyn Jones (Chairman)
Peter Cartwright (Non-Executive Director)
Neil Cochrane (Non-Executive Director)
Danuta Gray (Senior Independent Director)
John Callender[26] (Independent Non-Executive Director)
John Hitchins (Independent Non-Executive Director)
Christopher Stamper (Independent Non-Executive Director)
Cathy Turner (Independent Non-Executive Director)
Peter Shaw (Independent Non-Executive Director)

Executive Directors:

Phillip Monks (Chief Executive Officer)
James Mack (Chief Financial Officer)

As at 31 December 2014 the Board consisted of nine Non-Executive Directors (including the Chairman) and two Executive Directors. During 2014 there were a number of changes to the composition of the Board as detailed on page 48. The Board regards all of the Non-Executive Directors, other than Peter Cartwright and Neil Cochrane (appointed as shareholder Directors by the Group's principal shareholders, AnaCap Financial Partners and AnaCap Financial Partners II ('AnaCap')) and Glyn Jones (as Chairman), as 'independent Non-Executive Directors' (within the meaning of the UK Corporate Governance Code) and free from any business or other relationship that could materially interfere with the exercise of their independent judgement. The Board regarded Glyn Jones as independent upon his appointment as Chairman (within the meaning of the UK Corporate Governance Code).

The Board currently includes two female members, 18 per cent of its total composition.

b. Roles and responsibilities of the Board

The Board is collectively responsible to the shareholders and its other stakeholders for the long term success of the Group. The Board is committed to implementing and maintaining a well-defined and well-structured corporate governance framework to achieve long term sustainable success. The Board has responsibility for determining the business strategy and related risk appetite of the Group and to monitor performance against the plan, objectives and performance indicators for each area. The Board also has responsibility to maintain a system of internal controls, which provide assurance of effective and efficient operations, internal financial controls and compliance with all applicable laws and regulations. Additionally, the Board is responsible for ensuring that the executive maintain an effective risk management and oversight process across the Group to enable delivery of the strategy and business performance within the approved risk appetite and risk control framework.

Fundamentally, the Board is the main decision making forum for the Group. Therefore, all matters of significance because of their strategic, risk, financial, key person, regulatory or reputation implications or consequences are addressed by the Board. However, certain matters are reserved for the Group's principal shareholders, AnaCap, and the Board actively engages AnaCap on all such matters through the shareholder Directors.

In addition, the Board sets annual objectives for each year in addition to setting the Group's strategic direction. These are implemented through approval and regular assessment of the business plan and strategy process. At each Board meeting the Directors discuss strategic and business matters, financial, operational, risk and governance issues and other relevant business items that arise. Following Board Committee meetings the Board receives oral reports from the Chairs of each Committee at the next Board meeting.

[26] John Callender resigned with effect from 27 February 2015.

Corporate governance report continued

2. The Board continued

c. Role of the Chairman

Glyn Jones was appointed as Chairman in March 2014.

As Chairman, Glyn's primary objective is the governance of the Board. He leads the Board and is primarily responsible for setting the Board's agenda and ensuring that adequate time is available for discussion of all key agenda items, in particular strategic issues. The Chairman promotes a culture of openness and debate by facilitating the effective contribution of Non-Executive Directors and ensuring constructive relations between Executive and Non-Executive Directors. He also ensures Directors receive accurate, timely and clear information and that there is effective communication with shareholders. The Chairman is not responsible for the running of the day-to-day business of the Group, such duty being delegated to the Chief Executive Officer by the Board.

Details of Glyn's other business commitments are included in his biography and the Board is satisfied that these commitments do not interfere with the performance of his duties for the Group.

There is a clear division of responsibilities between the Chairman and the Chief Executive Officer.

Prior to Glyn's appointment, John Callender acted as Interim Chairman.

d. The role of the Senior Independent Director

Danuta Gray joined the Board as the Senior Independent Director in September 2014.

The Senior Independent Director is available to shareholders if they have concerns that the normal channels of communication to shareholders via the Chairman, Chief Executive Officer or other Executive Directors have failed to resolve any issues, or for which such channels of communication are inappropriate.

The Senior Independent Director will meet with the other Non-Executive Directors without the Chairman present once a year and on other occasions, as appropriate, to appraise the Chairman's performance.

Details of Danuta's other business commitments are included in her biography on page 52 and the Board is satisfied that these commitments do not interfere with the performance of her duties for the Group.

e. Changes to the Board[27]

Name	Position	Relevant Date
David Soskin	Non-Executive Director	Appointed to the Board on 06/02/2014 Resigned from the Board on 02/06/2014
Christopher Stamper	Non-Executive Director	Appointed to the Board on 06/02/2014
Glyn Jones	Non-Executive Director	Appointed to the Board on 21/03/2014
Cathy Turner	Non-Executive Director	Appointed to the Board on 28/05/2014
John Hitchins	Non-Executive Director	Appointed to the Board on 28/05/2014
Peter Shaw	Non-Executive Director	Appointed to the Board on 04/09/2014
Neil Cochrane	Non-Executive Director	Appointed to the Board on 04/09/2014
Danuta Gray	Non-Executive Director	Appointed to the Board on 29/09/2014
Steve Barry	Executive Director	Resigned from the Board on 21/09/2014
Paul Myers	Executive Director	Resigned from the Board on 21/09/2014
Mark Stephens	Executive Director	Resigned from the Board on 21/09/2014

[27] The Executive Directors above who resigned from the Board on 21 September 2014 did so in order to ensure the Group could meet UK Corporate Governance Code requirements for the Board to have a majority of independent Non-Executive Directors; all three executives continue to work for the Group in their executive roles.

f. Directors' induction and ongoing professional development

All Directors receive a comprehensive tailored induction programme. The induction programme includes an introduction to the Board and the business, including strategy, key risks and topical issues in order to enhance their understanding and knowledge of the Group's business and operations.

The Board also receives regular training and briefing sessions for on-going professional development both internally and externally in order to update and refresh their skills and knowledge.

g. Directors' conflicts of interest

The Companies Act 2006 provides that a Director must avoid situations where he/she can have a direct or indirect interest that conflicts or might conflict with the interests of the Group. The Company's Articles of Association contain provisions that allow the Board to consider and, if it sees fit, authorise such conflicts in certain situations. The Board confirms that such powers have been operated effectively and that a formal system for Directors to declare their interests and for the non-conflicted Directors to authorise conflicts continues to be in place.

3. Board Committees

The Board is supported by four key Committees:

- Audit Committee
- Risk Committee
- Remuneration Committee
- Nomination Committee

a. Composition of Board Committees at 31 December 2014

Details of the respective responsibilities of each Committee are provided below.

Audit Committee	Risk Committee	Remuneration Committee	Nomination Committee
John Hitchins (Chair)	John Callender (Chair)[28]	Cathy Turner (Chair)	Glyn Jones (Chair)
Peter Cartwright	Peter Cartwright	Danuta Gray	Peter Cartwright
Peter Shaw	John Hitchins	Peter Shaw	Danuta Gray
Christopher Stamper	Christopher Stamper	Glyn Jones	John Callender[28]
John Callender[28]	Peter Shaw[29]	Peter Cartwright	Cathy Turner

b. Audit Committee

The Audit Committee is made up of five members, four of whom are independent Non-Executive Directors. The Audit Committee is chaired by John Hitchins, who is considered by the Board to have recent and relevant financial experience. Further details of John's experience are provided in his biography on page 53.

The Audit Committee[30] met eight times in 2014 – three times as the Audit and Risk Committee and five times as the Audit Committee.

The Audit Committee's responsibilities include the monitoring of the integrity of the Group's financial statements and the involvement of the External Auditors in that process as well as reviewing the Group's internal control and risk management systems. It focuses in particular on compliance with accounting policies and accounting estimates and ensuring that an effective system of internal financial control is maintained. The ultimate responsibility for reviewing and approving the annual report and accounts and the half-yearly reports, remains with the Board.

The Audit Committee also receives regular updates from Internal Audit. The Committee reviews and assesses the annual Internal Audit work plan and receives reports on the results of the Internal Auditors' work.

[28] John Callender resigned from the Board and its committees with effect from 27 February 2015.

[29] Peter Shaw has been appointed Chair of the Risk Committee and a member of the Nomination Committee, replacing John Callender with effect from 1 March 2015.

[30] Until June 2014 part of a joint Audit and Risk Committee.

Governance

Corporate governance report continued

3. Board Committees continued

The Audit Committee formally reports to the Board on its proceedings after each meeting on matters within its duties and responsibilities, including how these duties and responsibilities have been discharged. In addition, the Audit Committee makes recommendations to the Board on any area within its remit where action is required.

c. Risk Committee

The Risk Committee is made up of five members, four of whom are independent Non-Executive Directors. During 2014, the Risk Committee was chaired by John Callender[31]. Further details of John's experience are provided in his biography on page 53.

The Risk Committee[32] met six times in 2014 – three times as the Audit and Risk Committee and three times as the Risk Committee.

The Risk Committee's responsibilities include the development and maintenance of the Group's Risk Management Framework, ensuring that its strategy, principles, policies and resources are aligned to the Group's risk appetite, as well as to regulatory and industry best practices. The Risk Committee also monitors and reviews the formal arrangements established by the Board in respect of internal controls and the Risk Management Framework and reviews the effectiveness of the Group's systems for risk management and compliance with financial services legislation and regulatory requirements.

The Risk Committee formally reports to the Board on its proceedings after each meeting on matters within its duties and responsibilities, including how these duties and responsibilities have been discharged. In addition, the Risk Committee makes recommendations to the Board on any area within its remit where action is required and makes recommendations to the Remuneration Committee on issues that should be taken into account in remuneration decisions.

d. Remuneration Committee

The Remuneration Committee is made of five members, three of whom are independent Non-Executive Directors. The Remuneration Committee is chaired by Cathy Turner. Further details of Cathy's experience are provided in her biography on page 53. Prior to Cathy, the post was held by John Callender.

The Remuneration Committee met four times in 2014.

The Remuneration Committee's responsibilities include assisting the Board in relation to the Group's remuneration framework, including making recommendations to the Board on the Group's policy on executive remuneration, setting the over-arching principles and parameters of the Group's remuneration policy and determining the individual remuneration and benefits package of each of the Group's Executive Directors and certain senior Executives. The remuneration of Non-Executive Directors is a matter for the Chairman and Executive Directors of the Board. No Director or senior manager shall be involved in any decisions as to their own remuneration.

The Remuneration Committee is also responsible for recommending and monitoring the structure and level of remuneration for senior management, including pension rights and any compensation payments.

The Remuneration Committee formally reports to the Board on its proceedings after each meeting on matters within its duties and responsibilities, including how these duties and responsibilities have been discharged. In addition, the Remuneration Committee makes recommendations to the Board on any area within its remit where action is required.

e. Nomination Committee

The Nomination Committee is made up of five members, three of whom are independent Non-Executive Directors. The Nomination Committee is chaired by Glyn Jones. Further, details of Glyn's experience are provided in his biography on page 52. Prior to Glyn's appointment, the post was held by John Callender.

The Nomination Committee met formally once in 2014. On other occasions, the full Board discharged the responsibilities of the Committee.

The Nomination Committee's responsibilities include considering and making recommendations to the Board in respect of appointments to the Board, the Board Committees and the chairmanship of the Board Committees. It is also responsible for keeping the structure, size and composition of the Board under regular review, and for making recommendations to the Board with regard to any changes necessary. This Committee also considers succession planning, taking into account the skills and expertise that will be needed on the Board in the future.

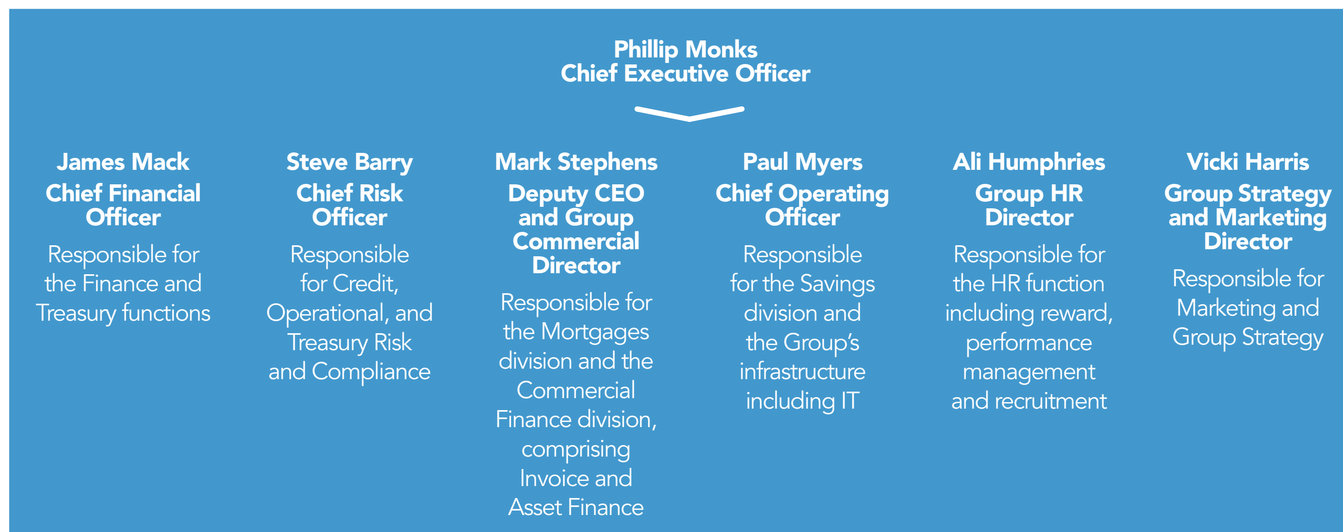
The Nomination Committee formally reports to the Board on its proceedings after each meeting on matters within its duties and responsibilities, including how these duties and responsibilities have been discharged. In addition, the Nomination Committee makes recommendations to the Board on any area within its remit where action is required.

[31] Peter Shaw has been appointed Chair of the Risk Committee with effect from 1 March 2015.

[32] Until June 2014 part of a joint Audit and Risk Committee. In addition, the Board Credit Committee met twice during 2014 before being amalgamated with the Risk Committee.

4. Executive Team

a. Details of the Executive Team



b. The role of the Chief Executive Officer and Executive Committees

Phillip Monks has direct charge of the Group on a day-to-day basis and is accountable to the Board for the financial and operational performance of the Group. Phillip was part of the team that founded the Bank in 2009 and has over 30 year's industry experience. Further details of Phillip's experience are provided in his biography on page 52.

He is supported by the Executive Team, who make up the two Executive Committees (ExCo) whose responsibility it is to implement the strategic objectives as agreed by the Board. ExCo, under the leadership of the CEO, is responsible for the management of the Group.

As set out on page 46, the ExCo is split into two committees:

- Executive Committee (Performance)
- Executive Risk Committee

c. Executive Committees

A number of sub-committees report into ExCo and assist with monitoring and oversight of the running of the business.

The following sub-committees report to the Executive Committee (Performance):

- Strategy Board
- Divisional Boards (Mortgages, Commercial Finance, Savings)
- IT and Transformation Board
- Treasury Management Committee

The following sub-committees report to Executive Risk Committee:

- Asset and Liability Committee
- Business Risk Committee
- Management Credit Committee
- Product Committee

5. Company Secretary

The Company Secretary is responsible for advising the Board through the Chairman on all governance related matters. All Directors have access to the advice and services of the Company Secretary.

Governance

Board of Directors

Executive Directors

Phillip Monks

Chief Executive Officer, Age 54

Phillip was part of the team which founded Aldermore in 2009 and has over 30 years' industry experience.

Most recently he established, and obtained a banking licence for, Europe Arab Bank where he was CEO until 2008.

Prior to this, Phillip held senior roles within Barclays Bank plc, including Branch Director of Barclays Private Bank in Geneva, Director of Business and Corporate Banking in North West England, Managing Director of Barclays Corporate Banking in London, the Midlands and South East and, finally, CEO of Gerrard Investment Management from 2003 upon its acquisition by Barclays from Old Mutual plc.

James Mack

Chief Financial Officer, Age 43

James joined Aldermore in June 2013 and is responsible for the Finance and Treasury functions.

From 2010, he held a number of senior finance roles within the Co-operative Banking Group including Acting CFO, Director of Financial Control and Head of Financial Planning and Analysis.

Prior to this, James spent six years with the Skipton Building Society and was instrumental in leading the merger with the Scarborough Building Society. James joined KPMG in 1993 and spent 11 years in their financial services practice.

Non-Executive Directors

Glyn Jones

Chairman, Age 62

Glyn joined the Board as Chairman in March 2014. He is currently the Senior Independent Director on the Board of Direct Line Insurance Group plc and, since May 2007, has been the Chairman of Aspen Insurance Holdings Limited, a New York listed specialty lines insurance and re-insurance business.

Glyn was formerly the Chairman of Towry Holdings Limited between 2006 and 2011. He also served as Chairman of Hermes Fund Managers from 2008 to 2011 and was Chairman of the sister company BT Pension Scheme Management for a part of this period.

Glyn was Chief Executive Officer of the independent investment group, Thames River Capital, from 2005 to 2006. From 2000, he served as Chief Executive Officer of Gartmore Investment Management in the UK for four years. Prior to this, Glyn was Chief Executive Officer of Coutts NatWest Group and Coutts Group, having joined in 1997.

In 1991, Glyn joined Standard Chartered in Hong Kong where he became the general manager of Global Private Banking. He was a consulting partner with Coopers & Lybrand/Deloitte Haskins & Sells Management Consultants from 1981 to 1990. Glyn is a graduate of Cambridge University and a Fellow of the Institute of Chartered Accountants in England & Wales.

Danuta Gray

Senior Independent Director, Age 55

Danuta joined the Board as the Senior Independent Director in September 2014.

Danuta has extensive business experience having spent 26 years in the telecommunications sector. Starting her career at BT in 1984, Danuta held numerous senior roles becoming Senior Vice President, BT Europe in 1999.

During her time at BT she gained experience in marketing, customer service, communications, technology and sales, and in leading and implementing change.

Danuta was Chairman of Telefonica O2 in Ireland until December 2012, having previously been its Chief Executive from 2001 to 2010.

Previously Danuta served for seven years on the Board of Irish Life & Permanent PLC as Chairman of the Remuneration Committee and was a Non-Executive Director of Aer Lingus PLC from 2006 – 2013. Danuta is currently also a Non-Executive Director at Old Mutual PLC, Michael Page International PLC and Paddy Power PLC.

Peter Cartwright

Non-Executive Director, Age 49

Peter's involvement with the Board dates back to the launch of Aldermore in May 2009.

He is one of the founding partners of AnaCap Financial Partners LLP where he is also the Co-Managing Principal responsible for developing AnaCap's portfolio company investments.

Prior to AnaCap, Peter was Commercial Director within a speciality insurance services provider backed by a UK-based private equity firm, and between 1999 and 2003 was Sales & Marketing Director and Operations Director for GMAC UK and On:line Finance, respectively, having previously worked for GE Capital.

Peter is an experienced business builder and operational specialist and holds various Non-Executive and supervisory Board roles within banks and financial services companies across Europe.

Neil Cochrane

Non-Executive Director, Age 30

Neil joined the Board in September 2014. Neil's involvement with Aldermore dates back to May 2010, when he joined AnaCap Financial Partners LLP's Business Services team.

This role saw Neil take responsibility for day-to-day interaction with senior management of the AnaCap's portfolio companies on strategic and operational development.

Neil is currently an Investment Director within the team. Neil brings eight years strategic financial services experience to this role. He started his career as a consultant at Oliver Wyman Financial Services in 2006 where he was involved in a broad range of projects for banking and insurance clients. His assignments covered clients in the UK, Europe and the U.S. and were predominately focused on new business launches, strategy development, M&A and risk management.

Neil graduated from the University of Nottingham in 2006 with a BA (Hons) in Economics.

John Hitchins

Independent Non-Executive Director, Age 60

John is an independent Non-Executive Director and chairs the Audit Committee. He was appointed to Board in May 2014. He brings 36 years of experience in the audit arena, having spent his whole career at PricewaterhouseCoopers ('PwC'), including as an audit partner.

John was formerly Chairman of the Banking Committee of the Institute of Chartered Accountants in England & Wales and a Board member of the Institute's Financial Services Faculty. He has also served as a member of the Institute's Business Law Committee. During his career with PwC, John specialised in bank auditing and financial advisory services and his clients have included institutions such as Euroclear, Lloyds Banking Group, The Bank of England, Bank of Ireland, Britannia Building Society, Barclays, JP Morgan Chase and Nomura.

Until recently, John was a member of the UK FCA Practitioner and Markets Practitioner Panels. He is currently a member of the Governing Council of the Centre for the Study of Financial Innovation, a not-for-profit City-based think tank. John is a graduate of Oxford University and a Fellow of the Institute of Chartered Accountants in England & Wales.

John Callender

Independent Non-Executive Director, Age 64

John joined the Board in May 2009 and chairs the Risk Committee. John resigned from the Board and its committees with effect from 27 February 2015.

He is currently Non-Executive chair of ANZ Bank Europe Ltd and holds Non-Executive Directorship at Ford Credit Europe Plc (where he chairs the Risk Committee and is a member of the Audit Committee), and at Motability Operations Plc (Where he chairs the Remuneration Committee and is a member of the Audit Committee).

John is also a member of the Financial Conduct Authority Regulatory Decisions Committee which he was invited to join in 2013. Until recently John served for a number of years as Governor of Reading Blue-Coat School in Sonning, Berkshire.

Previously he was a senior executive in Barclays plc with considerable experience of operating in Europe, India and the USA, running a number of Businesses including the asset finance, leasing, invoice finance and contract hire operations. He served on the Board of the Finance and Leasing Trade Association for six years and was elected Chair for 1996/1997.

Peter Shaw

Independent Non-Executive Director, Age 55

Peter joined the Board as an independent Non-Executive Director in September 2014 and will chair the Risk Committee with effect from 1 March 2015.

Peter brings over 30 years financial services experience to his new role, having spent most of his career at RBS NatWest. Joining NatWest as a graduate trainee in 1981, Peter worked across a number of business areas during his career with the group including retail, SME, private banking, corporate banking, HR and risk.

Between 1994 and 2002, Peter was Managing Director of various group businesses offshore, based in Jersey. In 2002, Peter returned to the UK to become COO of the Risk Function at Group Head Office and between 2004 and 2010 Peter was Chief Risk Officer for various group businesses including RBS UK Retail, Wealth & Ulster Bank. Between May 2012 and January 2013, Peter acted as interim Chief Risk Officer for the Co-operative Banking Group.

Peter is currently also a Non-Executive Director at Bank of Ireland UK PLC, where he is chair of the bank's Risk Committee and a member of the Audit Committee.

Peter graduated from London South Bank University in 1981 with a BA in Modern Languages. Peter holds an ACIB and DipFS. He is also a Fellow of the Chartered Institute of Bankers in Scotland.

Chris Stamper

Independent Non-Executive Director, Age 59

Chris is an independent Non-Executive Director and was appointed to the Board in February 2014.

He brings 35 years of experience in the asset finance industry, most recently as Director and CEO of ING Lease (UK) Ltd. He is a founding governor of The Leasing Foundation and was a Director of Finance and Leasing Association Ltd. from 2003 to 2012 and a former Chairman of their Asset Finance Division.

Previously, Chris was Head of Abbey Business responsible for five business units focused on the SME market. Prior to this, Chris was the Managing Director of Lombard Sales Finance where he spent 21 years.

Cathy Turner

Independent Non-Executive Director, Age 51

Cathy is an independent Non-Executive Director and chairs the Remuneration Committee.

She was appointed to the Board in May 2014. She is currently Non-Executive Director and Chair of the Remuneration Committee of Countrywide plc. She is also a Vice President of UNICEF UK and a member of the Board of the Royal College of Art. She is also an Associate of the advisory group Manchester Square Partners.

Cathy has extensive industry experience working with Deloitte & Touche, Ernst & Young and Watson Wyatt as a compensation and benefits consultant in her early career. She subsequently joined Barclays PLC, where she was a member of the Group Executive Committee with responsibility for Human Resources, Corporate Affairs, Strategy and Brand and Marketing.

During her time with Barclays she was also Director, Investor Relations for four years and had extensive experience in remuneration in her many roles.

Most recently, she was Chief Administrative Officer of Lloyds Banking Group PLC. Cathy is a graduate of the University of Lancaster.

Consolidated Directors' report

The Directors present their consolidated Directors' Report and the financial statements of the Group for the year ended 31 December 2014.

Strategic Report

The Group has chosen, in accordance with section 414c(11) of the Companies Act 2006, as noted in this Directors' Report, to include certain additional matters in its Strategic Report that would otherwise be required to be disclosed in this Directors' Report.

Principal activity

The Group is authorised to accept deposits under the Financial Services & Markets Act 2000. The Group's principal activities during 2014 were the provision of banking and related services in the United Kingdom. See page 10 for a description of the Group's business model and strategy.

Corporate Governance

The Corporate Governance section set out on pages 45 to 53 forms part of this Directors' Report.

Results and dividends

The results for the year are set out in the Income Statement on page 59. The profit before taxation for the year ended 31 December 2014 was £50.3 million (2013: £25.7 million). A full review of the financial performance of the Group is included within the Strategic report starting on page 6.

The Directors do not recommend the payment of a dividend (2013: £nil).

Business review and future developments

The required information regarding the business review and future developments, key performance indicators and principal risks and uncertainties are contained within the Strategic Report.

	Page
Business review and future developments	6
Key performance indicators	11
Principal risks and uncertainties	38

Financial instruments

The Group uses financial instruments to manage certain types of risk, including liquidity and interest rate risk. Details of the objectives and management of these instruments are contained in the risk management section. Details of exposures to these risks, as well as credit risk are also provided in Note 41 to the consolidated financial statements.

Post balance sheet events

Details of significant events after 31 December 2014 are included in Note 44 to the consolidated financial statements and form part of this Report.

Capital management

The Board is required to consider all material risks which the Group faces and determines whether additional capital is required in order to provide further protection to depositors and borrowers and to ensure the Group is sufficiently well capitalised to withstand a severe economic downturn. Full details of the Group's approach to capital management, including an analysis of the Group's regulatory capital position, are provided in Note 42 to the consolidated financial statements.

On 9 December 2014, Aldermore Group PLC issued £75 million Fixed Rate Reset Additional Tier 1 Perpetual Subordinated Contingent Convertible Securities (the 'Securities'). The Securities are perpetual and have no fixed redemption date. Redemption of the Securities is at the option of the Company on 30 April 2020 and annually thereafter. The Securities bear interest at an initial rate of 11.875 per cent p.a. until 30 April 2020 and thereafter at the relevant Reset Interest Rate as provided in the terms and conditions governing the securities. Interest is payable on the loan annually in arrears on each interest payment date commencing 30 April 2015 and is non-cumulative. The Borrower has the full discretion to cancel any interest scheduled to be paid on the Securities. The Securities are convertible into ordinary shares of the Company in the event of the Group's Common Equity Tier 1 ratio falling below 7 per cent.

The issuance of the above securities raised proceeds of £75.1 million, which after deducting issuance costs, resulted in net proceeds of £73.7 million. Further details are provided in Note 36 to the consolidated financial statements.

Share capital

Details of the Company's share capital at 31 December 2014 is provided in Note 35 to the consolidated financial statements.

Going concern

The financial statements are prepared on a going concern basis, as the Directors are satisfied that the Group has the resources to continue in business for the foreseeable future. In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including the current state of the balance sheet, future projections of profitability, cash flows and capital resources and the longer term strategy of the business. The Group's capital and liquidity plans, including stress tests, have been reviewed by the Directors. The Group's forecasts and projections show that it will be able to operate at adequate levels of both liquidity and capital for the foreseeable future, including a range of stressed scenarios, taking management actions into account as appropriate if the additional capital needed to continue the forecast growth strategy is not forthcoming. After making due enquiries, the Directors believe that the Group has sufficient resources to continue its activities for the foreseeable future and to continue its expansion, and the Group has sufficient capital to enable it to continue to meet its regulatory capital requirements as set out by the Prudential Regulation Authority ('PRA').

Employees

Our people are proud of the Bank we are building.

All new starters attend a centralised induction programme to ensure a consistent introduction to the Group. Each new starter is invited to a full day workshop in which they learn about our brand, values, approach to risk management, products and services.

We run a full communications programme targeted at all of our people, as well as bespoke programmes for managers and our senior leadership team. These programmes are orchestrated by an employee communications manager who reports into the central Corporate Affairs team and has direct access to the Executive Team.

Regular central communications are issued to all of our people, covering topics including our financial performance at key points throughout the year, as well as other strategic and HR-related updates. Channels include, although are not limited to, all employee emails, our intranet and Yammer.

In 2014, we refreshed our intranet to make it more user-friendly and bring it in line with our brand identity. As part of our commitment to transparency, key information has also been made more visible. For example, the intranet homepage now carries our Twitter feed, so that our people can follow external conversations we are involved in; recent examples of customer reviews from our Ratings & Reviews service, so that we can see what our customers are saying about us; and a feed from Yammer, to keep our people abreast of internal conversations.

We place a great deal of importance on ensuring that the lines of communication between our people and the Group's leaders are two-way and transparent. We have continued our programme of Executive visits to our regional offices during which our people are able to meet and hear from senior members of the Aldermore team.

We hold an annual employee roadshow in which we bring our people together to update them on the Group's vision. The roadshow also provides a forum for our people to pose questions to the Executive Team and to network with their colleagues. Roadshow events were held in Manchester, Leicester and Reading to enable all of our people to attend regardless of their geographical location. Following the roadshow, 88 per cent of people surveyed said that our Executive Team answered all of the questions put to them.

In early 2014, we conducted a pulse survey amongst employees which revealed that 84 per cent of respondents agreed that they received regular information from Aldermore that keeps them informed. We continue to make every effort to ensure that all of our people are aware of our strategy and understand the Group's performance objectives as this drives our success.

We are committed to ensuring that disabled people are afforded equality of opportunity in respect to entering and continuing employment within the Group. This includes all stages from recruitment and selection, terms and conditions of employment, access to training and career development.

Consolidated Directors' report continued

The Group is committed to diversity and we work hard to ensure that all of our people are offered equal opportunities throughout their career with us. We are determined that nobody is discriminated against, directly or indirectly, on the basis of age, ethnic or national origin, religion or beliefs, sexual orientation, gender, marital status or disability.

Directors

Details of the Directors, including appointments and resignations during the financial year, and changes since the end of the financial year are provided on page 48 of the Corporate Governance section of the report.

Directors' indemnities

Certain Directors benefited from qualifying third party indemnity provisions in place during the year ended 31 December 2014 and at the date of this report.

The Group also purchased Directors, and officers, liabilities insurance during the year, which provides appropriate cover for legal actions brought against its Directors.

Significant contracts

Details of related party transactions are set out in Note 39.

Corporate responsibility

The Group's corporate responsibilities activities are outlined on page 42.

Substantial shareholding

Aldermore Group PLC (the Parent Company) is controlled by AnaCap Financial Partners II, LP (52.3 per cent. of voting rights) and AnaCap Financial Partners, L.P. (47.7 per cent. of voting rights).

Political contributions

The Group made no political donations during the year (2013: £nil).

Research and development

The Group has a comprehensive product approval process and develops new products and services in each of its business divisions in the ordinary course of business. All new products, campaigns and business initiatives are reviewed and approved by the Group's Product Committee.

Disclosure of information to Auditors

The Directors who held office at the date of approval of this Directors' report confirm that, so far as they are aware, there is no relevant audit information of which the Group's auditors are unaware; and each Director has taken all steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the Group's auditor is aware of that information.

Auditor

KPMG LLP have expressed their willingness to continue in office as auditors.

By order of the Board

Phillip Monks
Director

16 February 2015

Statement of Directors' responsibilities in respect of the Strategic report, the Directors' report and the financial statements

The Directors are responsible for preparing the Strategic report, the Directors' report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and Parent Company financial statements for each financial year. Under that law they have elected to prepare both the Group and the Parent Company financial statements in accordance with IFRSs as adopted by the EU and applicable law.

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;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the Parent Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Parent Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

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

Financial statements

Independent auditor's report to the members of Aldermore Group PLC

We have audited the financial statements of Aldermore Group PLC for the year ended 31 December 2014 set out on pages 59 to 126. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU and, as regards the Parent Company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

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

Respective responsibilities of Directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 57, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2014 and of the Group's profit for the year then ended; the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the EU;
- the Parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Mike Peck

Michael Peck (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
Canary Wharf
London
E14 5GL

16 February 2015

Consolidated income statement

For the year ended 31 December 2014

	Note	**Year ended 31 December 2014 £'000**	Year ended 31 December 2013 £'000
Interest income	5	227,833	156,441
Interest expense	6	(87,618)	(75,799)
Net interest income		**140,215**	**80,642**
Fee and commission income	7	26,386	23,555
Fee and commission expense	8	(7,819)	(7,529)
Net (expense)/income from derivatives and other financial instruments at fair value through profit or loss	9	(4,066)	3,277
Gains on disposal of debt securities		2,944	1,869
Other operating income	10	7,357	6,531
Total operating income		**165,017**	**108,345**
Provisions	32	(3,605)	(2,111)
Costs in preparation for an initial public offering		(6,014)	–
Other administrative expenses		(91,622)	(65,252)
Administrative expenses	14	**(101,241)**	**(67,363)**
Depreciation and amortisation	15	(3,901)	(3,822)
Operating profit before impairment losses		**59,875**	**37,160**
Impairment losses on loans and advances to customers	20	(9,570)	(11,468)
Profit before taxation		**50,305**	**25,692**
Taxation (charge)/credit	17	(11,871)	14
Profit after taxation – attributable to equity holders of the Group		**38,434**	**25,706**
Basic earnings per share	18	16.4	12.7
Diluted earnings per share	18	16.3	12.6

The notes and information on pages 63 to 120 form part of these financial statements.
The result for the year is derived entirely from continuing activities.

Consolidated statement of comprehensive income

For the year ended 31 December 2014

	Year ended 31 December 2014 £'000	Year ended 31 December 2013 £'000
Profit after taxation	**38,434**	**25,706**
Other comprehensive income/(expense):		
Items that may subsequently be transferred to the income statement:		
Available for sale debt securities:	793	(2,566)
Fair value movements	3,456	(1,490)
Amounts transferred to the income statement	(2,465)	(1,869)
Taxation	(198)	793
Total other comprehensive income/(expense)	**793**	**(2,566)**
Total comprehensive income attributable to equity holders of the Group	**39,227**	**23,140**

Financial statements

Consolidated statement of financial position

As at 31 December 2014

	Note	**31 December 2014 £'000**	31 December 2013 £'000
Assets			
Cash and balances at central banks		79,567	192,844
Loans and advances to banks	19	117,401	237,544
Debt securities	21	509,684	355,653
Derivatives held for risk management	22	8,168	8,872
Loans and advances to customers	20	4,801,064	3,373,844
Fair value adjustment for portfolio hedged risk	5	7,175	–
Other assets	26	3,344	312
Prepayments and accrued income	27	6,856	5,109
Deferred taxation	17	6,598	3,299
Property, plant and equipment	25	2,815	2,858
Intangible assets	24	22,571	22,657
Total assets		**5,565,243**	**4,202,992**
Liabilities			
Amounts due to banks	28	305,907	385,951
Customers' accounts	29	4,458,962	3,464,018
Derivatives held for risk management	22	54,198	17,867
Fair value adjustment for portfolio hedged risk	6	1,528	–
Other liabilities	30	18,634	14,343
Accruals and deferred income	31	21,107	16,236
Current taxation		8,148	2,492
Provisions	32	2,008	1,157
Debt securities in issue	33	279,143	–
Subordinated notes	34	36,758	35,571
Total liabilities		**5,186,393**	**3,937,635**
Share capital	35	23,737	23,737
Share premium account	35	–	237,305
Contingent convertible securities	36	73,657	–
Capital contribution reserve		2	2
Warrant reserve		2,200	2,200
Available for sale reserve		1,375	582
Retained earnings		277,879	1,531
Equity		**378,850**	**265,357**
Total liabilities and equity		**5,565,243**	**4,202,992**

These financial statements were approved by the Board and were signed on its behalf by:

Phillip Monks
Director

16 February 2015
Registered number: 06764335

The notes and information on pages 63 to 120 form part of these financial statements.

Consolidated statement of cash flows

For the year ended 31 December 2014

	Note	**Year ended 31 December 2014 £'000**	Year ended 31 December 2013 £'000
Cash flows from operating activities			
Profit before taxation		50,305	25,692
Adjustments for non-cash items and other adjustments included within the income statement	37	(9,422)	18,002
(Increase) in operating assets	37	(1,487,787)	(1,320,852)
Increase in operating liabilities	37	962,772	1,571,927
Income tax paid		(9,712)	–
Net cash flows (used in)/generated from operating activities		**(493,844)**	**294,769**
Cash flows from investing activities			
Purchase of debt securities		(531,953)	(89,071)
Proceeds from sale and maturity of debt securities		346,183	41,265
Capital repayments of debt securities		48,226	23,893
Interest received on debt securities		11,229	7,948
Purchase of property, plant and equipment and intangible assets		(5,400)	(5,298)
Net cash used in investing activities		**(131,715)**	**(21,263)**
Cash flows from financing activities			
Proceeds from issue of shares		–	63,165
Capital repayments on debt securities issued		(52,840)	–
Debt securities issuance costs		(2,086)	–
Proceeds from issue of debt securities		333,300	–
Issuance costs of contingent convertible securities		(1,454)	–
Proceeds from issue of contingent convertible securities		75,111	–
Interest paid on debt securities		(2,513)	–
Interest paid on subordinated notes		(5,150)	(5,150)
Net cash from financing activities		**344,368**	**58,015**
Net (decrease)/increase in cash and cash equivalents		**(281,191)**	**331,521**
Cash and cash equivalents at start of the year	37	415,210	83,689
Movement during the year		(281,191)	331,521
Cash and cash equivalents at end of the year	37	**134,019**	**415,210**

Financial statements

Consolidated statement of changes in equity

	Share capital £'000	Share premium account £'000	Contingent convertible securities £'000	Capital contribution reserve £'000	Warrant reserve £'000	Available for sale reserve £'000	Retained earnings £'000	Total £'000
Year ended 31 December 2014								
As at 1 January	23,737	237,305	–	2	2,200	582	1,531	265,357
Total comprehensive income	–	–	–	–	–	793	38,434	39,227
Transactions with equity holders:								
– Reduction in share premium (Note 35)	–	(237,305)	–	–	–	–	237,305	–
– Issuance of contingent convertible securities (Note 36)[1]	–	–	75,111	–	–	–	–	75,111
– Issuance costs	–	–	(1,454)	–	–	–	–	(1,454)
– Share based payments (Note 35)	–	–	–	–	–	–	609	609
As at 31 December	**23,737**	**–**	**73,657**	**2**	**2,200**	**1,375**	**277,879**	**378,850**
Year ended 31 December 2013								
As at 1 January	19,918	177,959	–	2	2,200	3,148	(24,337)	178,890
Total comprehensive income	–	–	–	–	–	(2,566)	25,706	23,140
Transactions with equity holders:								
– Shares issued, net of expenses	3,819	59,346	–	–	–	–	–	63,165
– Share based payments (Note 35)	–	–	–	–	–	–	162	162
As at 31 December	**23,737**	**237,305**	**–**	**2**	**2,200**	**582**	**1,531**	**265,357**

[1] On 9 December 2014, Aldermore Group PLC ('the Company') raised £75.1 million of Fixed Rate Reset Additional Tier 1 Perpetual Subordinated Contingent Convertible Securities. Further detail is provided in Note 36.

Notes to the financial statements

1. Basis of preparation

(a) Accounting basis

The consolidated financial statements of Aldermore Group PLC (the 'Company') and its subsidiary undertakings (together, the 'Group'), including its principal subsidiary, Aldermore Bank PLC (the 'Bank').

Both the Group consolidated financial statements and the Company financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards ('IFRSs') as issued by the International Accounting Standards Board ('IASB'), and as adopted by the European Union.

The Group prepared its annual consolidated financial statements under United Kingdom Generally Accepted Accounting Practice ('UK GAAP') until 31 December 2013. UK GAAP differs in certain respects from IFRSs, hence when preparing these financial statements, management has amended certain accounting and valuation methods and accounts disclosures to comply with IFRSs. The significant accounting policies adopted are set out in Note 2.

The Group's first set of IFRS financial statements for the six months ended 30 June 2014 was included in the information memorandum for the contingent convertible securities issued in December 2014 (see Note 36). The Group's date of transition to IFRSs was 1 January 2011. The Group's first set of IFRS financial statements, including the reconciliations required by IFRS 1, are available on the Group's website www.investors.aldermore.co.uk.

By including the Company financial statements here together with the Group consolidated financial statements, the Company is taking advantage of the exemption in Section 408 of the Companies Act 2006 not to present its individual income statement and related notes that form a part of these approved financial statements.

The principal activity of the Company is that of an investment holding company.

(b) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries which are entities controlled by the Company (jointly referred to as the Group) made up to 31 December each year.

Control is achieved when the Company:

- has power over the investee;
- is exposed, or has rights, to variable returns from its involvement with the investee; and
- has the ability to use its power to affect its returns.

The Company reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

Subsidiaries are consolidated from the date on which control is transferred to the Group and are deconsolidated from the date that control ceases. Uniform accounting policies are applied consistently across the Group. Intercompany transactions and balances are eliminated upon consolidation.

Securitisation vehicles

The Group has securitised certain loans and advances to customers by the transfer of the beneficial interest in such loans to securitisation vehicles (see Note 20). The securitisation enabled the subsequent issue of debt securities by a securitisation vehicle to investors who have the security of the underlying assets as collateral. The securitisation vehicles are fully consolidated into the Group's accounts as the Group has control as defined above.

The transfer of the beneficial interest in these loans to the securitisation are not treated as sales by the Group. The Group continues to recognise these assets within its own Statement of Financial Position after the transfer as it continues to retain substantially all the risks and rewards from the assets.

(c) Going concern

The financial statements are prepared on a going concern basis, as the Directors are satisfied that the Group has the resources to continue in business for the foreseeable future (which has been taken as 12 months from the date of approval of the financial statements). In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including the current state of the balance sheet, future projections of profitability, cash flows and capital resources and the longer term strategy of the business. The Group's capital and liquidity plans, including stress tests, have been reviewed by the Directors. The Group's forecasts and projections show that it will be able to operate at adequate levels of both liquidity and capital for the foreseeable future, including a range of stressed scenarios, taking management actions into account as appropriate if the additional capital needed to continue the forecast growth strategy is not forthcoming. After making due enquiries, the Directors believe that the Group has sufficient resources to continue its activities for the foreseeable future and to continue its expansion, and the Group has sufficient capital to enable it to continue to meet its regulatory capital requirements as set out by the Prudential Regulation Authority ('PRA').

Notes to the financial statements continued

1. Basis of preparation continued

(d) Basis of measurement

The financial statements have been prepared on the historical cost basis except for the following material items in the financial statements:

- derivative financial instruments are measured at fair value through profit or loss;
- debt securities designated at fair value through profit or loss;
- available for sale debt securities are valued at fair value through other comprehensive income; and
- fair value adjustments for portfolios of financial assets and financial liabilities designated as hedged items in qualifying fair value hedge relationships, which reflect changes in fair value attributable to the risk being hedged.

(e) Use of estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about areas of estimation, uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are included in Note 3.

(f) Future accounting developments

All standards or amendments to existing standards which have been endorsed by the European Union ('EU') and which are available for early adoption for annual periods commencing on or after 1 January 2014 have been adopted by the Group.

There are also a number of standards, amendments and interpretations which have been issued by the IASB but which have not yet been endorsed by the EU. The most significant of these is IFRS 9: '*Financial Instruments*', the planned replacement for IAS 39: '*Financial Instruments: Recognition and Measurement*.'

IFRS 9 introduces new requirements for the classification and measurement of financial assets, hedge accounting and the impairment of financial assets. Under IFRS 9 financial assets are classified and measured based on the business model under which they are held and the characteristic of their contractual cash flows. In addition, IFRS 9 is replacing the incurred loss approach to impairment of IAS 39 with one based on expected losses, and is replacing the rules based hedging requirements of IAS 39 with new requirements that align hedge accounting more closely with risk management activities.

IFRS 9, including the final version of the requirements in respect of impairment, was issued on 24 July 2014. The IASB has decided to apply IFRS 9 for annual periods beginning on or after 1 January 2018. IFRS 9 is required to be applied retrospectively, but prior periods need not be restated. IFRS 9, including its commencement date, will be subject to endorsement by the EU.

In addition, the IASB has commenced a separate project for macro hedging, which is exploring a new way to account for the dynamic risk management of open portfolios and is likely to be of future relevance to the Group. That project is still at the Discussion Paper stage and as yet the likely final form of any amendments to IFRS 9, or their required implementation date, is not clear. The adoption of IFRS 9 is expected to have a material impact on the Group's financial statements. Work is ongoing to quantify the impact.

The changes in the approach to impairment would not be likely to have a significant impact on the Group's impairment provisions in respect of specifically impaired loans or those loans where there has been a credit deterioration although the loans are not considered to be yet impaired, as the current impairment provisions on such loans are based on estimates of expected losses. In respect of other loans against which collective provisions are raised our current approach as explained in Note 3 is to estimate probabilities of defaults, and hence expected losses, for the next 12 months. This approach is similar to that which will be required under IFRS 9 except that in order to measure incurred losses, as required by IAS 39, we then adjust the calculated 12 month expected loss for an emergence period reflective of the underlying asset so as to reflect only the impairment which is considered to have been incurred at the reporting date.

The IASB has also issued IFRS 15: '*Revenue from contracts with customers.*' The impact for the Group is currently being assessed. The Standard will be effective for annual reporting periods beginning on or after 1 January 2017 with retrospective application subject to EU endorsement.

2. Significant accounting policies

(a) Interest income and expense

Interest income and expense are recognised in the income statement on an effective interest rate ('EIR') basis. The EIR is the rate that, at the inception of the financial asset or liability, exactly discounts expected future cash payments and receipts over the expected life of the instrument back to the initial carrying amount. When calculating the EIR, the Group estimates cash flows considering all contractual terms of the instrument (for example, prepayment options) but does not consider the assets' future credit losses.

At each reporting date, management makes an assessment of the expected remaining life of its financial assets, including any acquired loan portfolios, and where there is a change in those assessments the remaining amount of any unamortised discount or premiums is adjusted so that the interest income continues to be recognised prospectively on the amortised cost of the financial asset at the original EIR. The adjustment arising is recognised within interest income in the income statement for the current period.

The calculation of the EIR includes all transaction costs and fees paid or received that are an integral part of the interest rate, together with the discounts or premium arising on the acquisition of loan portfolios. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Interest income and expense presented in the income statement include:

- interest on financial assets and financial liabilities measured at amortised cost calculated on an EIR basis;
- interest on available for sale debt securities calculated on an EIR basis;
- interest income recognised on finance leases where the Group acts as the lessor (see Note 2(o));
- the effective portion of fair value changes in qualifying hedging derivatives designated in fair value hedges of interest rate risk, together with changes in the fair value of the hedged item attributable to the hedged risk; and
- interest income on financial assets designated at fair value so as to avoid an accounting mismatch with derivatives held as an 'economic' hedge and the matching interest component of the derivative.

Interest income includes amounts the Group charges its Invoice Finance clients as interest each day on the balance of their outstanding loans. This interest income is recognised in the income statement on an EIR basis.

(b) Fee and commissions and other operating income

Fee and commission income

Fee and commission income includes fees relating to services provided to customers which do not meet the criteria for inclusion within interest income.

Within the Invoice Finance division of the Group, customers are charged a factoring fee for managing their sales ledgers. This fee is recognised within fee and commissions income over the period in which the ledger management service is provided. Other fee and commission income includes fees charged for valuations, documentation, mortgage services and arrears, and are recognised as the related services are performed.

Arrangement fees and others fees relating to loans and advances to customers are included within interest income as part of the EIR calculation.

Fee and commission expense

Fee and commission expense predominantly consists of introducer commissions, legal and valuation fees and company search fees. Where these fee and commissions are incremental costs that are directly attributable to the issue of a financial instrument, they are included in interest income as part of the EIR calculation. Where they are not incremental costs that are directly attributable they are recognised within fee and commission expense as the services are received.

Other operating income

Other operating income predominantly arises from the provision of Invoice Finance services and includes disbursements and collect out income. This income is recognised within other operating income when the service is provided.

(c) Net income from derivatives and other financial instruments at fair value through profit or loss

Net income from derivatives and other financial instruments at fair value through profit or loss relates to non-trading derivatives held for risk management purposes that do not form part of a qualifying hedging arrangement and financial assets designated at fair value through profit or loss. It includes all realised and unrealised fair value changes, interest and foreign exchange differences, with the exception of interest income on financial assets designated at fair value and the matching interest component of the hedging derivatives. The assets designated at fair value are treated in this manner so as to avoid an accounting mismatch with derivatives held as an 'economic' hedge.

Notes to the financial statements continued

2. Significant accounting policies continued

(d) Financial instruments – recognition and derecognition

(i) Recognition

The Group initially recognises loans and advances, amounts due to banks, customer accounts and subordinated notes issued on the date that they are originated.

Regular way purchases and sales of debt securities and derivatives are recognised on the trade date at which the Group commits to purchase or sell the asset. All other financial assets and liabilities are initially recognised on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

(ii) Derecognition

Financial assets are derecognised when they are qualifying transfers and:

- the rights to receive cash flows from the assets have ceased; or
- the Group has transferred substantially all the risks and rewards of ownership of the assets.

When a financial asset is derecognised in its entirety, the difference between the carrying amount and the sum of the consideration received (including any new asset obtained less any new liability assumed) and any cumulative gain or loss that had been recognised in other comprehensive income is recognised in the income statement.

When available for sale financial assets are derecognised, the cumulative gain or loss, including that previously recognised in reserves, is recognised in the income statement.

A financial liability is derecognised when the obligation is discharged, cancelled or expires. Any difference between the carrying amount of a financial liability derecognised and the consideration paid is recognised through the income statement.

(iii) Funding for Lending Scheme ('FLS')

Loans and advances over which the Group transfers its rights to the collateral thereon to the Bank of England under the FLS are not derecognised from the statement of financial position, as the Group retains substantially all the risks and rewards of ownership, including all cash flows arising from the loans and advances and exposure to credit risk. The treasury bills that the Group borrows against the transferred assets are not recognised in the statement of financial position, but where they are sold to third parties by the Group under agreements to repurchase, the cash received is recognised as an asset within the statement of financial position together with the corresponding obligation to return it which is recognised as a liability at amortised cost within 'Due to banks'. Interest is accrued over the life of the agreement on an EIR basis.

(e) Financial assets

(i) Overview

The Group classifies its financial assets (excluding derivatives) as either:

- loans and receivables;
- available for sale; or
- financial assets designated at fair value through profit or loss

(ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Group does not intend to sell immediately or in the near term. These are initially measured at fair value plus transaction costs that are directly attributable to the financial asset. Subsequently, these are measured at amortised cost using the EIR method. The amortised cost is the amount advanced less principal repayments, plus or minus the cumulative amortisation using the EIR method of any difference between the amount advanced and the maturity amount less impairment provisions for incurred losses. Loans and receivables mainly comprise loans and advances to banks and customers.

(iii) Available for sale

Available for sale financial assets are debt securities that are not held for trading and are intended to be held for an indefinite period of time. These are initially measured at fair value plus transaction costs that are directly attributable to the financial asset. Subsequently, they are measured at fair value based on current quoted bid prices in active markets for identical assets that the Group can access at the reporting date. Where there is no active market or the debt securities are unlisted the fair values are based on valuation techniques including discounted cash flow analysis, with reference to relevant market rates, and other commonly used valuation techniques. Interest income is recognised in the income statement using the EIR method. Impairment losses are recognised in the income statement. Other fair value changes are recognised in other comprehensive income and presented in the available for sale reserve in equity. On disposal, the gain or loss accumulated in equity is reclassified to the income statement.

(iv) Fair value assets designated at fair value through profit or loss

Financial assets designated at fair value through profit or loss are assets which have been designated as such to eliminate or significantly reduce a measurement and recognition inconsistency or where management specifically manages an asset or liability on that basis. These assets are measured at fair value based on current quoted bid prices in active markets for identical assets that the

Group can access at the reporting date. Gains and losses arising from changes in the fair value are brought into the income statement within 'Net income/(expense) from derivatives and other financial instruments at fair value through profit or loss' as they arise.

(f) Financial liabilities

(i) Overview

Financial liabilities are contractual obligations to deliver cash or another financial asset. Financial liabilities are recognised initially at fair value, net of directly attributable transaction costs for financial liabilities other than derivatives. Financial liabilities, other than derivatives, are subsequently measured at amortised cost.

(ii) Financial liabilities at amortised cost

Financial liabilities at amortised cost are recognised initially at fair value, which equates to issue proceeds net of transaction costs incurred. They are subsequently stated at amortised cost. Any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

(iii) Subordinated notes

Subordinated notes issued by the Group are assessed as to whether they should be treated as equity or financial liabilities. Where there is a contractual obligation to deliver cash or other financial assets, they are treated as a financial liability and measured at amortised cost using the EIR after taking account of any discount or premium on the issue and directly attributable costs that are an integral part of the EIR. The amount of any discount or premium is amortised over the period to the expected call date of the instrument. All subordinated notes issued by the Group are classified as financial liabilities; however, the warrants attached to the subordinated notes, which give the holders the right to subscribe for shares in Aldermore Group PLC (the 'Parent Company'), have been included in equity as a warrant reserve at the residual value attributable to the warrants after deducting from the face value of the instrument as a whole the amounts determined separately as the fair value of the subordinated notes at the date of issue.

(g) Impairment – financial assets

(i) Assessment

At each reporting date the Group assesses its financial assets not at fair value through profit or loss as to whether there is objective evidence that the assets are impaired. Objective evidence that financial assets are impaired can include:

- significant financial difficulty of the borrower;
- a breach of contract such as default or delinquency in interest or principal repayments;
- the granting of a concession for economic or legal reasons relating to the borrower's financial condition that the Group would not otherwise grant;
- indications that a borrower or issuer will enter bankruptcy or other financial reorganisation;
- the disappearance of an active market for a debt security because of the issuer's financial difficulties; or
- national or local economic conditions that correlate with defaults within groups of financial assets e.g. increases in unemployment rates or decreases in property prices relating to the collateral held.

The Group considers evidence for the impairment of loans and advances at both the individual asset and collective level. In certain cases where a borrower is experiencing significant financial distress, the Group may use forbearance measures to assist them and militate against default. Any forbearance measures agreed are assessed on a case by case basis.

(ii) Scope

The Group considers evidence of impairment of financial assets at both an individual asset and collective level.

Individual impairment

All individually significant financial assets are assessed for individual impairment using a range of risk criteria. Those found not to be individually impaired are then collectively assessed for any impairment that has been incurred but not yet identified.

Assets are considered to be individually impaired where they meet one or more of the following criteria:

- a default position equivalent to three or more missed monthly repayments (or a quarterly payment which is over 30 days past due);
- litigation proceedings have commenced;
- act of insolvency, e.g. bankruptcy, administration or liquidation, or appointment of an LPA Receiver;
- invoice finance accounts are classified as in default when there is cessation of additional advances and/or when the facility is in collect out; or
- where there is evidence of fraud.

Notes to the financial statements continued

2. Significant accounting policies continued

Collective impairment
All financial assets that are not found to be individually impaired are collectively assessed for impairment by grouping together financial assets with similar risk characteristics.

(iii) Measurement
Impairment provisions on financial assets individually identified as impaired are calculated as the difference between the carrying amount and the present value of estimated future cash flows discounted at the asset's original EIR.

When assessing collective impairment, the Group estimates incurred losses using a statistical model which multiplies the probability of default ('PD') for each class of customer (using external credit rating information) by the loss given default ('LGD') multiplied by the estimated exposure at default ('EaD') to arrive at the projected expected loss. An emergence period is subsequently applied to the projected expected loss to determine the estimated level of incurred losses at each reporting date. In addition an adjustment is made to discount the imputed cash flows from the model at the assets' original EIR to arrive at the recorded collective provisions. The model's results are adjusted for management's judgement as to whether current economic and credit conditions are such that actual losses are likely to differ from those suggested by historical modelling.

In assessing the level of collective impairment provisions, the Group uses statistical modelling of historical trends of probability of default, 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 actual losses are likely to be greater or less than suggested by historical trends. Default rates, loss rates and the expected timing of future recoveries are benchmarked against actual outcomes to ensure they remain appropriate.

Impairment losses are recognised immediately in the income statement and a corresponding reduction in the value of the financial asset is recognised through the use of an allowance account.

A write-off is made when all or part of a financial asset is deemed uncollectible or forgiven after all collection procedures have been completed and the amount of the loss has been determined. Write-offs are charged against amounts previously reflected in the allowance account or directly to the income statement. Any additional amounts recovered after a financial asset has been previously written off are offset against the write-off charge in the income statement once they are received. Allowances for impairment losses are released at the point when it is deemed that, following a subsequent event, the risk has reduced such that an allowance is no longer required.

Interest on impaired financial assets is recognised at the same EIR as applied at the initial recognition of the financial asset but applied to the book value of the financial asset net of any individual impairment allowances that have been raised.

(iv) Impairment of financial assets classified as available for sale
Impairment losses on available for sale debt securities are recognised by reclassifying the losses accumulated in the available for sale reserve in equity to the income statement. The cumulative loss that is reclassified from equity to the income statement is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss recognised previously in the income statement. Changes in impairment provisions attributable to the effective interest method are reflected as a component of interest income.

If in a subsequent period the fair value of an impaired available for sale debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognised, then the impairment loss is reversed.

(h) Financial instruments – 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 in the principal, or in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk.

When applicable, the Group measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing on an ongoing basis.

When there is no quoted price in an active market, the Group uses valuation techniques that maximise the use of relevant observable inputs and minimises the use of unobservable inputs. The chosen valuation techniques incorporate all the factors that market participants would take into account in pricing a transaction.

The best evidence of fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration received or given.

If an asset measured at fair value has a bid and an offer price, the Group measures assets and long positions at a bid price and liabilities at an offer price.

(i) Derivative financial instruments

The Group enters into derivative transactions only for the purpose of reducing exposures to fluctuations in interest rates, exchange rates and market indices; they are not used for proprietary trading purposes.

Derivatives are carried at fair value with movements in fair values recorded in the income statement. Derivative financial instruments are principally valued by discounted cash flow models using yield curves that are based on observable market data or are based on valuations obtained from counterparties. As the Group's derivatives are covered by master netting agreements with the Group's counterparties, with any net exposures then being further covered by the payment or receipt of periodic cash margins, the Group has used a risk free discount rate for the determination of their fair values.

All derivatives are classified as assets where their fair value is positive and liabilities where their fair value is negative. Where there is the current legal ability and intention to settle net, then the derivative is classified as a net asset or liability, as appropriate. Where cash collateral is received, to mitigate the risk inherent in amounts due to the Group, it is included as a liability within 'Amounts due to banks'. Where cash collateral is given, to mitigate the risk inherent in amounts due from the Group, it is included as an asset in 'Loans and advances to banks'.

(j) Hedge accounting

The Group designates certain derivatives held for risk management as hedging instruments in qualifying hedging relationships. On initial designation of the hedge, the Group formally documents the relationship between the hedging instruments and hedged items, including the risk management objective, the strategy in undertaking the hedge and the method that will be used to assess the effectiveness of the hedging relationship. The Group makes an assessment both at the inception of the hedge relationship as well as on an ongoing basis, as to whether the hedging instruments are expected to be highly effective in offsetting the changes in the fair value of the respective hedged items during the period for which the hedge is designated.

Fair value hedge accounting for a portfolio hedge of interest rate risk

The Group has applied fair value hedge accounting for a portfolio hedge of interest rate risk for the first time, starting on 1 January 2014. As part of its risk management process the Group identifies portfolios whose interest rate risk it wishes to hedge. The portfolios comprise either only assets or only liabilities. The Group analyses each portfolio into repricing time periods based on expected repricing dates, by scheduling cash flows into the periods in which they are expected to occur. Using this analysis, the Group designates as the hedged item an amount of assets or liabilities from each portfolio that it wishes to hedge.

The Group measures monthly the change in fair value of the portfolio relating to the interest rate risk that is being hedged. Provided that the hedge has been highly effective, the Group recognises the change in fair value of each hedged item in the income statement with the cumulative movement in their value being shown on the statement of financial position as a separate item, 'Fair value adjustment for portfolio hedged risk', either within assets or liabilities as appropriate. This amount is amortised on a straight line basis to the income statement over the remaining average useful life of the original hedge relationship, from the month in which it is first recognised.

The Group measures the fair value of each hedging instrument monthly. The value is included in derivative financial instruments in either assets or liabilities as appropriate, with the change in value recorded in the income statement. Any hedge ineffectiveness is recognised in the income statement as the difference between the change in fair value of the hedged item and the change in fair value of the hedging instrument.

(k) Embedded derivatives

A derivative may be embedded in another instrument, known as the host contract. Where the economic characteristics and risks of an embedded derivative are not closely related to those of the host contract (and the host contract is not carried at fair value through profit or loss), the embedded derivative is separated from the host and held on the statement of financial position with derivatives held for risk management at fair value. Movements in fair value are posted to the income statement, whilst the host contract is accounted for according to the relevant accounting policy for that particular asset or liability.

Embedded derivatives contained within equity instruments are considered separately. The embedded derivative on the contingent convertible securities is not separated as the Group has an accounting policy not to separate a feature that has already been considered in determining that the entire issue is a non-derivative equity instrument.

Notes to the financial statements continued

2. Significant accounting policies continued

(l) Property, plant and equipment

Items of property, plant and equipment are stated at cost or deemed cost at transition to IFRSs, less accumulated depreciation and any provision for impairment. Cost includes expenditure that is directly attributable to the acquisition of the asset or costs incurred in bringing the asset to use. Depreciation is provided on all property, plant and equipment, at rates calculated to write off the cost of each asset to realisable values on a straight line basis over its expected useful life, as follows:

- fixtures, fittings and equipment — five years
- computer hardware — one to five years

Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment. Equipment held for use in operating leases is written down to its estimated residual value on a straight line basis over the period of the underlying lease agreement.

(m) Intangible assets

Goodwill

Goodwill is stated at cost or deemed cost at transition to IFRSs, less any accumulated impairment losses. Goodwill is not amortised but is tested for impairment on an annual basis. Where impairment is required, the amount is recognised in the income statement and cannot be subsequently reversed.

Computer systems

Software acquired by the Group is measured at cost less accumulated amortisation and any accumulated impairment losses.

Expenditure on internally developed software is recognised as an asset when the Group is able to demonstrate its intention and ability to complete the development and use the software in a manner that will generate future economic benefits, and can reliably measure the costs to complete the development. The capitalised costs of internally developed software include all costs directly attributable to developing the software, and are amortised over its useful life. Internally developed software is stated at capitalised cost less accumulated amortisation and impairment.

Software is amortised on a straight line basis in the income statement over its useful life, from the date that it is available for use. The estimated useful life of software is one to five years.

(n) Impairment of non-financial assets

The carrying amounts of the Group's non-financial assets are reviewed at least annually to determine whether there is any indication of impairment. If any such indication exists, then the assets recoverable amount is estimated.

Goodwill

Goodwill is tested for impairment at least annually. For the purpose of impairment testing, goodwill is allocated to divisions. An impairment loss is recognised if the carrying amount of a division exceeds its recoverable amount. The recoverable amount of a division is the greater of its value in use and its fair value less costs to sell. The estimation of recoverable value is based on value in use calculations incorporating forecasts by management of post-tax profits for the subsequent five years, and a residual value, discounted at a risk-adjusted interest rate appropriate to the cash generating unit.

Where impairment is required, the amount is recognised in the income statement and cannot be subsequently reversed.

Intangible assets

If impairment is indicated, the asset's recoverable amount (being the greater of fair value less costs to sell and value in use) is estimated. Value in use is calculated by discounting the future cash flows from continuing use of the asset. If the carrying value of the asset is less than the greater of the value in use and the fair value less costs to sell, an impairment loss is recognised in the income statement.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(o) Assets leased to customers

All leases of assets to customers are finance leases as defined by IAS 17. When assets are leased to customers under 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, within interest income in the income statement, over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return ignoring tax cash flows.

(p) Assets leased from third parties

Leases where the lessor retains substantially all the risks and rewards of ownership are classified as operating leases. Payments made under operating leases, net of any incentives received from the lessor, are charged to the income statement, within administrative expenses or staff costs (in the case of company cars), on a straight line basis over the period of the lease. The Group holds no assets under finance leases.

(q) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

The Group has an obligation to contribute to the Financial Services Compensation Scheme ('FSCS') to enable the FSCS to meet compensation claims from, in particular, retail depositors of failed banks. A provision is recognised to the extent it can be reliably estimated and when the Group has an obligation in accordance with IAS 37. The amount provided is based on information received from the FSCS, forecast future interest rates and the Group's historic share of industry protected deposits.

(r) Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities held at the balance sheet date are translated into sterling at the exchange rates ruling at the balance sheet date. Exchange differences are charged or credited to the income statement.

(s) Taxation

Taxation comprises current and deferred tax, which is recognised in the income statement except to the extent that it relates to items recognised directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on taxable income or loss for the period, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for:

- temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss;
- temporary differences related to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future; and
- taxable temporary differences arising on the initial recognition of goodwill.

The measurement of deferred tax reflects the tax consequences that would follow the manner in which the Group expects at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. Deferred tax is measured using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(t) Pension costs

The cost of providing retirement benefits is charged to the income statement at the amount of the defined contributions payable for each year. Differences between contributions payable and those actually paid are shown as accruals or prepayments. The Group has no defined benefit pension scheme.

(u) Shareholders' funds

(i) Capital instruments

The Company classifies capital instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instruments. Where an instrument contains no obligation on the Company to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the Group, or where the instrument will or may be settled in the Company's own equity instruments but includes no obligation to deliver a variable number of the Company's own equity instruments then it is treated as an equity instrument. Accordingly, the Company's share capital, contingent convertible securities and warrants represented by the warrant reserve are presented as components of equity within shareholders' funds. Any dividends, interest or other distributions on capital instruments are recognised in equity. Related income tax is accounted for in accordance with IAS 12.

(ii) Share premium

Share premium is the amount by which the fair value of the consideration received exceeds the nominal value of the shares issued.

(v) Capital raising costs

Costs directly incremental to the raising of share capital are netted against the share premium account. Costs directly incremental to the raising of convertible securities included in equity are offset against the proceeds from the issue within equity.

Financial statements

Notes to the financial statements continued

2. Significant accounting policies continued

(w) Cash and cash equivalents
Cash and cash equivalents comprises cash balances and balances with a maturity of three months or less from the acquisition date, which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

(x) Investment in Group undertakings
Investments in Group undertakings are initially recognised at cost. At each reporting date, an assessment is made as to whether there is any indication that the investment may be impaired. If such an indication exists, the Company estimates the investment's recoverable amount. The investment is written down to the recoverable amount if this is lower than its carrying value. The impairment loss is recognised in the income statement.

(y) Warrants
The Company's subsidiary, Aldermore Bank PLC, has issued subordinated notes with an attached warrant. The warrant gives the holders the right to subscribe for shares in the Company. The value attributable to these warrants has been reflected in an increase in the investment in Group undertakings and has been included in equity as a warrant reserve.

(z) Share based payment transactions
Employees (including senior Executives) of the Group may receive remuneration in the form of share based payment transactions, whereby employees can purchase equity instruments in Aldermore Group PLC, the Group's Parent Company ('equity-settled transactions'). The consideration paid for the equity instruments was in some cases below the fair value at the transaction date. The fair value of these transactions is determined at the transaction date and is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award.

The expense recognised in the income statement for the period represents the movement in cumulative expense recognised at the beginning and end of that period. Where the Group's Parent grants equity instruments to the Group's employees, which are accounted for as equity settled in the consolidated accounts of the parent, the Group accounts for these share based payments as equity settled. Further details of share based payments are provided in Note 35.

The share based payment transactions are recognised as an investment in Group undertakings with an associated credit to the share based payment reserve within the Parent Company standalone financial statements.

3. Use of estimates and judgements

The preparation of financial information requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected. The judgements and assumptions that are considered to be the most important to the portrayal of the Group's financial condition are those relating to loan impairment provisions, EIRs, contingent liabilities, the classification of contingent convertible securities and intangible assets.

(a) Loan impairment provisions
Loan portfolios across all divisions of the Group are reviewed on at least a monthly basis to assess for impairment. In determining whether an impairment provision should be recorded, judgements are made as to whether there is objective evidence that a financial asset or portfolio of financial assets is impaired as a result of loss events that occurred after recognition of the asset and by the reporting date. The calculation of impairment loss is management's best estimate of losses incurred in the portfolio at the balance sheet date and reflects expected future cash flows based on both the likelihood of a loan or advance being written off and the estimated loss on such a write-off.

At 31 December 2014 gross loans and advances to customers totalled £4,824 million (31 December 2013: £3,395 million) against which impairment allowances of £23 million (31 December 2013: £21 million) had been made (see Note 20). The Group's accounting policy for loan impairment provisions on financial assets classified as loans and receivables is described in Note 2(g). Impairment allowances are made up of two components, those determined individually against specific assets and those determined collectively. Of the impairment allowance of £23 million at 31 December 2014, £14 million relates to individual provisions and £9 million relates to collective provisions. The section below provides details of the critical elements of judgement within the loan impairment calculations. Less significant judgements are not disclosed.

Individual
Individual impairment allowances are established against the Group's individually significant financial assets that are deemed by management to be impaired. The determination of individual impairment allowances requires the exercise of considerable judgement by management involving matters such as local economic conditions, the financial status of the customer and the realisable value of the security held. The actual amount of the future cash flows and their timing may differ significantly from the assumptions made for the purposes of determining the impairment allowances and consequently these allowances can be subject to variation as time progresses and the circumstances of the customer become clearer.

Collective
The collective impairment allowance is also subject to estimation uncertainty and in particular is sensitive to changes in economic and credit conditions, including the interdependency of house prices, unemployment rates, interest rates, borrowers' behaviour and consumer bankruptcy trends. All of these factors can influence the key assumptions detailed below. It is, however, inherently difficult to estimate how changes in one or more of these factors might impact the collective impairment allowance.

The key assumptions used in the collective model are: probability of default ('PD'), the loss given default ('LGD') and the loss emergence period ('EP') (the time between a trigger event occurring and the loans being identified as individually impaired). An additional element is included within the collective provision to reflect fraud losses that are incurred as at the reporting date but are yet to be individually impaired. Further details in respect of assumptions and details of the sensitivity of the estimate of the impairment allowance to changes in significant assumptions are as follows:

Probability of default:
The PD is based on external individual customer credit rating information updated for each reporting date. This external credit rating information gives a PD in the next 12 months where 'default' is defined as loans which are 2 months or more in arrears '2 MIA' and incorporates credit information from a broad range of financial services products for each customer.

Management make an estimate so as to adjust the external data to reflect both the individual nature of the Group's lending and the Group's policy of classifying loans which are 3 months or more in arrears ('3 MIA') as 'impaired'. This adjustment is achieved by using two management assumptions: firstly a 'roll rate' that reflects how many of the loans which fall into 2 MIA will also fall into 3 MIA; and secondly a scalar that adjusts the external PDs to reflect the individual nature of the Group's lending.

- A 10 per cent absolute increase in the 'roll rate' assumed by management between 2 MIA and 3 MIA (e.g. a PD increasing from 50 per cent. to 60 per cent.), when the loans are considered to be individually impaired would increase the impairment allowance by £0.4 million.
- A 10 per cent relative reduction in the scaling factors applied to external data in order to arise at PDs appropriate to the individual nature of lending being undertaken would increase the impairment allowance by £0.5 million.

Loss given default
The model calculates the LGD from the point of repossession. Not all cases that are 3 MIA will reach repossession. Management therefore adjust the model by applying an assumption of the percentage of accounts 3 MIA that will reach repossession.

- A 10 per cent absolute reduction in this assumption would decrease the impairment allowance by £0.8 million.

The LGD is also sensitive to the application of the House Price Index ('HPI') and Forced Sale Discount ('FSD') which affect the underlying value of the collateral which is expected to be received.

- A 10 per cent relative reduction in the HPI would increase the overall impairment allowance by £1.2 million.
- A five per cent absolute increase in the FSD would increase the overall impairment provision by £0.9 million.

Emergence period
Management make a judgement, according to the line of business for the underlying loans, on the length of emergence period to apply to the estimated losses expected to be recognised in the next 12 months in order to determine those which are considered as incurred as at the reporting date.

- A three month increase in all emergence periods would increase the overall impairment allowance by £3.3 million.

(b) Effective interest rate
IAS 39 requires interest earned from mortgages to be measured under the EIR method, as described in Note 2(a). Management must therefore use judgement to estimate the expected life of each type of instrument and hence the expected cash flows relating to it. The accuracy of the EIR would therefore be affected by unexpected market movements resulting in altered customer behaviour, inaccuracies in the models used compared to actual outcomes and incorrect assumptions.

A critical estimate in determining EIRs is the expected lives to maturity of the Group's commercial and residential mortgage portfolios, as a change in the estimates will have an impact on the period over which the directly attributable costs and fees, and any discount received on the acquisition of the mortgage loan portfolios, are recognised. An extension of the estimated expected lives for a period of six months would have the effect of reducing the cumulative profit before tax recognised as at 31 December 2014 by £2.4 million (31 December 2013: £2.4 million).

Notes to the financial statements continued

3. Use of estimates and judgements continued

(c) Contingent liabilities

As outlined in Note 32 and 38, the Group has made certain judgements and estimates about the extent of any customer redress for aspects of non-compliance with certain areas of detailed laws and regulations including the Customer Credit Act. The judgements and estimates made represent the best estimate of the Directors based on information available including legal advice. Further details are outlined in Note 32 and 38.

(d) Classification of contingent convertible securities

The Group issued £75 million of Fixed Rate Reset Additional Tier 1 Perpetual Subordinated Contingent Convertible Securities ('the Securities') during the year (see Note 36 for further detail).

The Securities (net of the associated issuance costs) have been classified as equity within the statement of financial position. The decision to classify the Securities as equity (as opposed to debt) required management to consider the individual terms attached to the Securities, including the conversion clauses. This involved obtaining external legal and professional advice.

The Group is not required to make payments under any circumstances, other than on a winding up. The Securities are convertible into ordinary shares of the Company in the event of the Group's Common Equity Tier 1 ratio falling below 7 per cent. Subject to circumstances which are within the Company's control, conversion can only be for a fixed number of the Company's ordinary shares. The Securities impose no obligation on the Group to deliver cash or other financial benefit to security holders because they are perpetual, with no fixed redemption or maturity date and interest is due and payable only at the sole and absolute discretion of the Company. Furthermore, interest is non-cumulative.

After consideration of all of the terms and the external advice received, management concluded that the Securities should be classified as equity in accordance with IAS 32: *Financial instruments.*

(e) Intangible assets

The Group assesses its intangible assets at least annually for evidence of impairment. Where the asset is under development, the Group considers whether it is reasonably likely to complete the asset and bring it into use. The Group also considers if the asset will generate sufficient economic benefit over and above the current carrying value of the asset. These considerations have resulted in a write-off of £1.6 million during the year.

4. Segmental information

The Group has four reportable operating segments as described below which are based on the Group's four lending divisions plus Central Functions. Each segment offers groups of similar products and services and are managed separately based on the Group's internal reporting structure. Residential and SME Commercial Mortgages are operated under a single management team and supported by a single IT platform. However, the characteristics of the two businesses are sufficiently different and accordingly the segments are reported separately to the Board. Therefore, the two businesses represent separate operating segments in accordance with IFRS 8.

For each of the reportable segments the Board, which is the Group's Chief Operating Decision Maker, reviews internal management reports on a monthly basis. The following summary describes the operations in each of the Group's reportable segments:

- Residential Mortgages – Prime residential mortgages targeting underserved segments of creditworthy borrowers that provide attractive and sustainable margins and residential buy-to-let mortgages.
- SME Commercial Mortgages – Property finance needs of professional, residential/commercial property investors, and owner-occupier SMEs. Targets prime and specialist prime segments with loan sizes below £5 million.
- Asset Finance – Lease and hire purchase financing for SMEs, focusing on sectors with strong returns and liquid secondary asset markets.
- Invoice Finance – Simple factoring/discounting facility and credit control for SMEs, targeting owner managed businesses.

Central Functions represent the reconciling items between the total of the four reportable operating segments and the consolidated income statement. As well as common costs, Central Functions includes the Group's Treasury and Savings functions which are responsible for raising finance on behalf of the operating segments. The costs of raising finance are all recharged by Central Functions to operating segments, apart from those costs relating to the subordinated notes (Note 6) and net expense/income from derivatives held at fair value.

Common costs are incurred on behalf of the operating segments and typically represent savings administration costs, back office costs and support function costs such as Finance, Risk and Human Resources. The costs are not directly attributable to the operating segments.

Information regarding the results of each reportable segment and their reconciliation to the total results of the Group are included below. Performance is measured based on the segmental result as included in the internal management reports.

Segmental information for the year ended 31 December 2014

	Residential Mortgages £'000	SME Commercial Mortgages £'000	Asset Finance[1] £'000	Invoice Finance £'000	Central Functions[1] £'000	Total £'000
Interest income – external customers	106,924	56,215	56,684	9,276	(1,266)	227,833
Interest expense – external customers	–	–	–	–	(87,618)	(87,618)
Interest (expense)/income – internal	(43,427)	(14,663)	(19,749)	(3,327)	81,166	–
Net fees and other income – external customers	4,109	1,518	3,064	17,543	(1,432)	24,802
Total operating income	**67,606**	**43,070**	**39,999**	**23,492**	**(9,150)**	**165,017**
Administrative expenses including depreciation and amortisation	(9,551)	(6,865)	(11,878)	(14,712)	(62,136)	(105,142)
Impairment losses on loans and advances to customers	(1,252)	(2,246)	(2,661)	(3,411)	–	(9,570)
Segmental result	**56,803**	**33,959**	**25,460**	**5,369**	**(71,286)**	**50,305**
Tax						(11,871)
Profit after tax						**38,434**
Assets	2,564,899	1,011,291	1,044,298	180,576	764,179	5,565,243
Liabilities	–	–	–	–	(5,186,393)	(5,186,393)
Net assets/(liabilities)	**2,564,899**	**1,011,291**	**1,044,298**	**180,576**	**(4,422,214)**	**378,850**

[1] A £1,628,000 write-off in relation to an Asset Finance intangible asset has been recorded within Central Functions as the asset was under construction at the time of write-off.

Segmental information for the year ended 31 December 2013

	Residential Mortgages £'000	SME Commercial Mortgages £'000	Asset Finance £'000	Invoice Finance £'000	Central Functions £'000	Total £'000
Interest income – external customers	66,670	39,910	37,375	9,379	3,107	156,441
Interest expense – external customers	–	–	–	–	(75,799)	(75,799)
Interest (expense)/income – internal	(34,920)	(14,562)	(14,360)	(4,318)	68,160	–
Net fees and other income – external customers	2,875	89	1,992	17,861	4,886	27,703
Total operating income	**34,625**	**25,437**	**25,007**	**22,922**	**354**	**108,345**
Administrative expenses including depreciation and amortisation	(6,944)	(4,792)	(9,501)	(13,993)	(35,955)	(71,185)
Impairment losses on loans and advances to customers	(1,261)	(1,965)	(2,585)	(5,657)	–	(11,468)
Segmental result	**26,420**	**18,680**	**12,921**	**3,272**	**(35,601)**	**25,692**
Tax						14
Profit after tax						**25,706**
Assets	1,679,686	761,998	720,198	211,962	829,148	4,202,992
Liabilities	–	–	–	–	(3,937,635)	(3,937,635)
Net assets/(liabilities)	**1,679,686**	**761,998**	**720,198**	**211,962**	**(3,108,487)**	**265,357**

Financial statements

Notes to the financial statements continued

5. Interest income

	2014 £'000	2013 £'000
On financial assets not at fair value through profit or loss:		
On loans and advances to customers	227,758	153,676
On loans and advances to banks	1,548	1,206
On debt securities	5,105	3,818
	234,411	**158,700**
On financial assets at fair value through profit or loss:		
Net interest expense on financial instruments hedging assets	(12,128)	(7,970)
Net interest income on debt securities designated at fair value	5,550	5,711
	227,833	**156,441**

Included within interest income on loans and advances to customers for the year ended 31 December 2014 is a total of £2,029,000 (31 December 2013: £957,000) relating to impaired financial advances.

Included within net interest income on financial instruments hedging assets are fair value losses of £8,758,000 (31 December 2013: £nil) on derivatives held in qualifying fair value hedging arrangements, together with gains of £7,175,000 (31 December 2013: £nil) representing changes in the fair value of the hedged item attributable to the hedged interest rate risk on loans and advances to customers.

6. Interest expense

	2014 £'000	2013 £'000
On financial liabilities not at fair value through profit or loss:		
On customers' accounts	80,035	70,411
On amounts due to banks	1,522	1,822
On debt securities in issue	3,281	–
On subordinated notes	6,338	6,121
	91,176	**78,354**
On financial liabilities at fair value through profit or loss:		
Net interest income on financial instruments hedging liabilities	(4,785)	**(3,678)**
Other	1,227	**1,123**
	87,618	**75,799**

Included within net interest expense on financial instruments hedging assets are fair value gains of £1,649,000 (31 December 2013: £nil) on derivatives held in qualifying fair value hedging arrangements together with losses of £1,528,000 (31 December 2013: £nil) representing changes in the fair value of the hedged item attributable to the hedged interest rate risk on customers' accounts.

7. Fee and commission income

	2014 £'000	2013 £'000
Invoice finance fees	14,546	14,949
Insurance commissions receivable	601	1,221
Other	11,239	7,385
	26,386	**23,555**

Details of 'other' fee and commission income are provided in Note 2 (b).

8. Fee and commission expense

	2014 £'000	2013 £'000
Introducer commissions	1,932	1,962
Legal and valuation fees	2,467	1,688
Company searches and other fees	1,815	2,296
Credit protection and insurance charges	1,154	762
Insurance commissions payable	451	821
	7,819	**7,529**

9. Net (expense)/income from derivatives and other financial instruments at fair values through profit or loss

	2014 £'000	2013 £'000
Net (losses)/gains on derivatives	(17,278)	13,993
Net gains/(losses) on assets designated at fair value through profit or loss	9,537	(10,716)
Net gains on available for sale assets held in fair value hedges	4,068	–
Less: realised gains transferred to gains on disposal of debt securities	(393)	–
	(4,066)	**3,277**

10. Other operating income

	2014 £'000	2013 £'000
Disbursements, collect out and other invoice finance income	7,066	6,344
Other	291	187
	7,357	**6,531**

11. Staff costs

	2014 £'000	2013 £'000
Wages and salaries	43,248	33,684
Social security costs	5,009	3,905
Other pension costs	1,157	835
	49,414	**38,424**

The average number of persons employed by the Group during the year, including Non-Executive Directors, was 764 (31 December 2013: 621).

12. Remuneration of Directors

	2014 £'000	2013 £'000
Directors' emoluments	2,797	2,747
Compensation for loss of office	20	195
Contributions to money purchase scheme	61	60
	2,878	**3,002**

Compensation for loss of office in 2014 of £20,000 (2013: £195,000) relates to two Directors (2013: two Directors) and includes £nil (2013: £nil) pension plan contribution. In addition, in the prior year, the Group's controlling party repurchased those Directors' shares in the Company for an amount which was £94,000 in excess of the initial purchase price.

The Group made payments of £24,000 to two Directors' individual personal pension plans during the year (2013: £25,000, two Directors).

Notes to the financial statements continued

12. Remuneration of Directors continued

During 2014 one Director was given the option to purchase B ordinary shares of £0.10 and two Directors were given the option to purchase C ordinary shares of £0.0001 in the ultimate Parent Company, Aldermore Group PLC, at a discount to market value. 455,021 discounted B ordinary shares were purchased and 17,985,919 discounted C ordinary shares were purchased (2013: one Director, 303,347 B ordinary shares). The shares issued in the year give rise to a benefit of £408,000 (2013: £61,000). A charge of £555,000 has been recognised in the year in relation to the total share based payments amount.

Highest paid Director

The above amounts include the following in respect of the highest paid Director:

	2014 £'000	2013 £'000
Emoluments	703	653
Contributions to money purchase scheme	20	10
Share based payments	4	61
	727	**724**

13. Pension and other post-retirement benefit commitments

The Group operates two defined contribution pension schemes. The assets of the schemes are held separately from those of the Group in independently administered funds. Pension contributions of £1,157,000 (31 December 2013: £835,000) were charged to the income statement during the year in respect of these schemes. The Group made payments amounting to £24,000 (31 December 2013: £25,000) in aggregate in respect of certain employees' individual personal pension plans during the year. There were outstanding contributions of £209,000 at the year end (31 December 2013: £128,000).

14. Administrative expenses

	Note	**2014 £'000**	2013 £'000
Staff costs	11	49,414	38,424
Legal and professional and other services		23,527	12,095
Information technology costs		8,289	4,683
Office costs		4,017	3,191
Provisions	32	3,605	2,111
Other		12,389	6,859
		101,241	**67,363**

Included in administrative expenses are £6,014,000 of costs incurred in preparation for an initial public offering.

Information technology costs include £1,628,000 (31 December 2013: £nil) in relation to a write-off of intangible assets.

Included in other administrative expenses are costs relating to temporary staff of £4,534,000 (31 December 2013: £2,322,000), travel and subsistence of £2,825,000 (31 December 2013: £2,382,000) and staff recruitment of £2,050,000 (31 December 2013: £1,197,000).

15. Depreciation and amortisation

	Note	**2014 £'000**	2013 £'000
Depreciation	25	950	697
Amortisation of intangible assets	24	2,951	3,125
		3,901	**3,822**

16. Profit on ordinary activities before taxation

The profit on ordinary activities is arrived after charging:

	2014 £'000	2013 £'000
Operating lease rentals (including service charges)		
– land and buildings	1,898	1,174
– plant and equipment	522	436
Foreign exchange loss	29	33
The remuneration of the Group's external auditors, KPMG LLP, and their associates is as follows:		
Fees payable to the Group's auditor for the audit of the annual accounts (excluding VAT)	50	–
Fees payable to the Group's auditor for the audit of the accounts of subsidiaries (excluding VAT)	347	245
Audit fees	397	245
Fees payable to the Group's auditor and its associates for other services (excluding VAT):		
Audit related assurance services[1]	568	43
Taxation compliance services	14	29
Other taxation advisory services[2]	232	94
Corporate finance services[3]	827	–
Other assurance services[4]	582	94
All other services	21	58
Non-audit fees	2,244	318
	2,641	**563**

1 Audit related assurance services comprise services provided in relation to the IFRS conversion audit and interim profit verifications during the year. Also included is work in relation to the Group's issuance of Additional Tier 1 contingent convertible securities.

2 Other taxation advisory services relate to advice provided on a number of specific tax areas arising in the normal course of business. The advice provided also included tax advice relating to the Group's initial public offering.

3 Fees payable for corporate finance services for year ended 31 December 2014 include £827,000 for the Reporting Accountants' reports in relation to the Group's intended initial public offering.

4 Other assurance services relate to services provided in relation to the audit of the Group's results in preparation for its intended initial public offering.

17. Taxation

a) Tax charge/(credit)

	2014 £'000	2013 £'000
Current tax on profits for the year	15,510	2,492
Over provision in previous periods	(157)	–
Total current tax charge	**15,353**	**2,492**
Deferred tax	(3,731)	(2,506)
Under provision in previous periods	249	–
	11,871	**(14)**

A current tax charge of £16,000 and a deferred tax charge of £182,000 was recognised in other comprehensive income during the year ended 31 December 2014 (31 December 2013: £793,000 deferred tax credit) in respect of available for sale debt securities.

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Notes to the financial statements continued

17. Taxation continued

b) Factors affecting tax charge/(credit) for the year

The tax assessed for the year is different to that resulting from applying the standard rate of corporation tax in the UK of 21.5 per cent (31 December 2013: 23.25 per cent). The differences are explained below:

	2014 £'000	2013 £'000
Profit before tax	**50,305**	**25,692**
Tax at 21.5% (2013: 23.25%) thereon	10,816	5,973
Effects of:		
Expenses not deductible for tax purposes	689	(26)
Prior year deductible temporary differences utilised in the year	–	(3,455)
Recognition/(release) of deferred tax asset	–	(2,506)
Over provision in previous period	92	–
Deferred tax rate adjustment	274	–
	11,871	**(14)**

c) Deferred tax asset

A net deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as probable that there will be suitable future taxable profits against which the unwinding of the asset can be offset.

Analysis of recognised deferred tax asset:

Year ended 31 December 2014	**Balance at start of the year £'000**	**Recognised in income statement £'000**	**Recognised in other comprehensive income £'000**	**Balance at end of the year £'000**
Capital allowances less than depreciation	3,392	3,163	–	6,555
Gains on available for sale debt securities recognised through other comprehensive income	(148)	–	(182)	(330)
Other temporary differences	55	318	–	373
	3,299	**3,481**	**(182)**	**6,598**

Year ended 31 December 2013	Balance at start of the year £'000	Recognised in income statement £'000	Recognised in other comprehensive income £'000	Balance at end of the year £'000
Tax losses carried forward	941	(941)	–	–
Capital allowances less than depreciation	–	3,392	–	3,392
Gains on available for sale debt securities recognised through other comprehensive income	(941)	–	793	(148)
Other temporary differences	–	55	–	55
	–	**2,506**	**793**	**3,299**

Reductions in the UK corporation tax rate from 24 per cent to 23 per cent (effective 1 April 2013) and to 21 per cent (effective from 1 April 2014) were substantively enacted on 3 July 2012 and 2 July 2013 respectively. A further reduction to 20 per cent (effective from 1 April 2015) was also substantively enacted on 2 July 2013. This will reduce the Group's future current tax charge accordingly. The deferred tax assets at 31 December 2014 and 31 December 2013 have been calculated based on the rate of 20 per cent substantively enacted at those balance sheet dates.

There were £nil unrecognised deferred tax balances at 31 December 2014 (31 December 2013: £nil).

18. Earnings per share

Basic earnings per share is calculated by dividing the net profit/(loss) attributable to equity shareholders of the Group by the weighted average number of ordinary shares in issue during the year.

	2014	2013
Profit attributable to equity shareholders of the Group (£'000)	38,434	25,706
Weighted average number of ordinary shares in issue (thousand)	233,658	203,019
Basic earnings per share (p)	16.4	12.7

The ordinary shares in issue used in the denominator in the calculation of basic earnings per share are the A1, A2, D and E ordinary shares. The B and C ordinary shares are excluded from the calculation on the basis that prior to any initial public offering they have no entitlement to dividends or other distributions of the Parent Company.

The calculation of diluted earnings per share has been based on the same profit attributable to equity shareholders of the Group as for basic earnings and the weighted average number of ordinary shares outstanding after the potential dilutive effect of outstanding share warrants. The share warrants give the holders the right to subscribe for 2,905,779 E ordinary shares at a price of £1.12 per share and a further 1,452,889 E ordinary shares at a price of £1.55 per ordinary share, and are exercisable until 31 May 2022.

	2014	2013
Weighted average number of ordinary shares in issue (thousand) (basic)	233,658	203,019
Effect of share warrants in issue	1,967	357
Weighted average number of ordinary shares in issue (thousand) (diluted)	235,625	203,376
Diluted earnings per share (p)	16.3	12.6

19. Loans and advances to banks

	2014 £'000	2013 £'000
Included in cash and cash equivalents: balances with less than three months to maturity at inception	60,371	226,194
Cash collateral on derivatives placed with banks	46,162	11,350
Other loans and advances to banks	10,868	–
	117,401	**237,544**

There were no individual or collective provisions for impairment held against loans and advances to banks. £10,868,000 is recoverable more than 12 months after the reporting date (2013: £nil) and relates to cash held by the Group's securitisation vehicle, Oak No.1 PLC.

20. Loans and advances to customers

	2014 £'000	2013 £'000
Gross loans and advances	4,823,638	3,394,872
less: allowance for impairment losses	(22,574)	(21,028)
	4,801,064	**3,373,844**
Amounts include:		
Expected to be recovered more than 12 months after the reporting date	4,205,825	2,880,879

At 31 December 2014, loans and advances to customers of £719.9 million (31 December 2013: £822.9 million) were pre-positioned with the Bank of England and HM Treasury Funding for Lending Scheme. These loans and advances were available for use as collateral with the Scheme, against which £485.0 million of UK Treasury Bills had been drawn as at the reporting date (31 December 2013: £485.0 million).

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Notes to the financial statements continued

20. Loans and advances to customers continued

At 31 December 2014, loans and advances to customers include £293.1 million (31 December 2013: £nil) which have been used in secured funding arrangements, resulting in the beneficial interest in these loans being transferred to Oak No. 1 PLC which is a securitisation vehicle consolidated into these financial statements. The carrying value of these loans on 10 April 2014 when the beneficial interest was transferred was £362.3 million. These loans secured £333.3 million (2013: £nil) of funding for the Group (see Note 33). All the assets pledged are retained within the statement of financial position as the Group retains substantially all the risks and rewards relating to the loans.

Allowance for impairment losses

Year ended 31 December 2014	Individual £'000	Collective £'000	Total £'000
Balance as at 1 January	14,714	6,314	21,028
Impairment loss for the year:			
Charge to the income statement	6,373	3,197	9,570
Unwind of discounting	(1,025)	(984)	(2,009)
Write-offs net of recoveries	(6,015)	–	(6,015)
Balance as at 31 December	**14,047**	**8,527**	**22,574**

Year ended 31 December 2013	Individual £'000	Collective £'000	Total £'000
Balance as at 1 January	9,318	3,131	12,449
Impairment loss for the year			
Charge to the income statement	7,689	3,779	11,468
Unwind of discounting	(361)	(596)	(957)
Write-offs net of recoveries	(1,932)	–	(1,932)
Balance as at 31 December	**14,714**	**6,314**	**21,028**

The charge to the Group's income statement shown in the table above is presented net of releases of provisions previously recorded against individual customers. The following table provides a further breakdown of impairment losses:

	2014 £'000	2013 £'000
Provisions established	12,758	12,262
Less:		
Significant provision releases prior to write-off[1]	(2,091)	(793)
Recoveries of amounts previously written off	(1,097)	(1)
Charge to the income statement	**9,570**	**11,468**

1 Significant provision releases comprise individual cases where a change in circumstances has resulted in a release of an individually assessed impairment provision in excess of £300,000.

Finance lease receivables

Loans and advances to customers include the following finance leases of equipment where the Group is the lessor:

	2014 £'000	2013 £'000
Gross investment in finance leases, receivable:		
Less than one year	469,841	279,078
Between one and five years	690,359	512,398
More than five years	16,672	19,574
	1,176,872	**811,050**
Unearned finance income	(130,686)	(90,852)
Net investment in finance leases	**1,046,186**	**720,198**
Net investment in finance leases, receivable:		
Less than one year	376,079	235,781
Between one and five years	653,902	465,403
More than five years	16,205	19,014
	1,046,186	**720,198**

The Group enters into finance lease and hire purchase arrangements with customers in a wide range of sectors including plant and machinery, cars and commercial vehicles. The accumulated allowance for uncollectible minimum lease payments receivable is £2,213,000 (31 December 2013: £2,328,000).

Due to the nature of the business undertaken, there are no material unguaranteed residual values for any of the finance leases at 31 December 2014 or 31 December 2013.

Included in the above disclosure is approximately £70 million in relation to block discounting facilities (31 December 2013: approximately £52 million) and approximately £17 million in relation to unsecured lending at 31 December 2014 (31 December 2013: approximately £17 million).

21. Debt securities

	2014 £'000	2013 £'000
Debt securities designated at fair value through profit or loss:		
UK Government Gilts	116,405	108,399
Supranational Bonds	37,951	54,499
	154,356	**162,898**
Available for sale debt securities:		
UK Government Gilts and Treasury Bills	21,519	24,647
Supranational Bonds	292,965	90,264
Corporate Bonds	24,516	–
Asset-backed securities	16,328	77,844
	355,328	**192,755**
	509,684	**355,653**

At 31 December 2014, £459.1 million (31 December 2013: £301.6 million) of debt securities are expected to be recovered more than 12 months after the reporting date. There were no impairment losses in respect of available for sale debt securities.

22. Derivatives held for risk management

Amounts included in the statement of financial position are analysed as follows:

	2014		2013	
Instrument type	**Assets £'000**	**Liabilities £'000**	Assets £'000	Liabilities £'000
Interest rate (not in hedging relationships)	1,075	23,218	8,484	17,511
Interest rate (fair value hedges)	6,632	30,546	–	–
Equity	408	408	354	354
Foreign exchange	53	26	34	2
	8,168	**54,198**	**8,872**	**17,867**

All derivatives are held either as fair value hedges qualifying for hedge accounting (from January 2014) or are held for the purpose of managing risk exposures arising on the Group's other financial instruments (all periods).

Fair value hedges of interest rate risk

From January 2014, the Group has used interest rate swaps within qualifying hedge accounting relationships to manage its exposure to changes in the fair values of certain fixed rate lending and savings products and debt securities held, attributable to changes in market interest rates.

Further details regarding the Group's approach to hedge accounting, including a description of the Group's exposure to volatility are provided in Note 41.

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Notes to the financial statements continued

22. Derivatives held for risk management continued

Other derivatives held for risk management

The Group uses other derivatives, not designated in qualifying hedge relationships, to manage its exposure to the following:

- Interest rate risk on certain debt securities held which are designated at fair value through profit or loss;
- Interest rate basis risk on certain mortgage loans;
- Equity market risk on equity linked products offered to depositors; and
- Foreign exchange risk on currency loans provided to invoice finance customers.

23. Investment in subsidiaries

On 25 September 2014, the 99.9 per cent majority interest in Aldermore Holdings Limited was transferred to Aldermore Group PLC, leaving the Bank as a wholly owned subsidiary of Aldermore Group PLC. Subsidiary undertakings, all of which are registered in England and operate in the UK, are listed below. All subsidiaries are included in the consolidated financial statements.

	Principal activity	Shareholding %
Subsidiary undertakings		
Aldermore Bank PLC	Banking and related services	100%
Securitisation vehicles		
Oak No.1 Mortgage Holdings Limited	Holding company for securitisation vehicle	*
Oak No.1 PLC	Securitisation vehicle	*
Dormant subsidiary undertakings		
Aldermore Invoice Finance (Holdings) Limited	Dormant	100%
Aldermore Invoice Finance Limited	Dormant	100%
Aldermore Invoice Finance (Oxford) Limited	Dormant	100%
Subdsidiary undertakings struck-off		
Aldermore Holdings Limited	Holding company	100%
Aldermore Bank Nominees Limited	Dormant	100%
Base Commercial Mortgages Holdings Limited	Dormant	100%
Base Commercial Mortgages Limited	Dormant	100%
Base Commercial Mortgages Funding Limited	Dormant	100%
Lynchwood Commercial Funding No.1 Limited	Dormant	100%
Lynchwood Commercial Funding No.2 Limited	Dormant	100%

* The share capital of these securitisation vehicles is not owned by the Group, but these vehicles are included in the consolidated financial statements as they are controlled by the Group.

An application to strike companies from the register of companies was filed with Companies House on 29 September 2014. Formal strike-off was completed on 3 February 2015.

24. Intangible assets

	Computer systems £'000	Goodwill £'000	Total £'000
Cost/deemed cost at transition to IFRS			
1 January 2014	16,253	12,653	28,906
Additions	4,493	–	4,493
Write-off	(1,628)	–	(1,628)
31 December 2014	**19,118**	**12,653**	**31,771**
1 January 2013	12,898	12,653	25,551
Additions	3,355	–	3,355
31 December 2013	**16,253**	**12,653**	**28,906**
Amortisation			
1 January 2014	6,249	–	6,249
Charge for the year	2,951	–	2,951
31 December 2014	**9,200**	**–**	**9,200**
1 January 2013	3,124	–	3,124
Charge for the year	3,125	–	3,125
31 December 2013	**6,249**	**–**	**6,249**
Net book value			
31 December 2014	**9,918**	**12,653**	**22,571**
31 December 2013	**10,004**	**12,653**	**22,657**

Goodwill arose on the acquisitions of Base Commercial Mortgages Holdings Limited and Absolute Invoice Finance Holdings Limited. For the purpose of impairment testing, goodwill is allocated to the Group's operating divisions. The aggregate amount allocated to each division is as follows:

	2014 £'000	2013 £'000
SME Commercial Mortgages	8,547	8,547
Invoice Finance	4,106	4,106
	12,653	**12,653**

No impairment losses on goodwill were recognised during the year ended 31 December 2014 (31 December 2013: £nil).

The recoverable amounts for SME Commercial Mortgages and Invoice Finance divisions have been calculated based on their value in use, determined by discounting the future cash flows to be generated from the continuing use of the division. Value in use at 31 December 2014 has been determined in a similar manner as at 31 December 2013.

- Key assumptions used in the calculation of value in use were the following: Cash flows were projected based on past experience, actual operating results and the five year business plan (31 December 2013: the four year business plan). Cash flows for a further 10 year period were extrapolated using a constant growth rate of 3 per cent (31 December 2013: 3 per cent). The forecast period is based on the Group's long term perspective with respect to the operation of these divisions.
- Pre-tax discount rates of 13 per cent and 15 per cent (31 December 2013: 13 per cent and 15 per cent) respectively were applied in determining the recoverable amounts for the SME Commercial Mortgages and Invoice Finance operating divisions. These discount rates were based on the weighted average cost of funding for the divisions based on the Group's regulatory capital requirement and expected market returns for debt and equity funding, adjusted for risk premiums to reflect the systemic risk of the individual divisions.

The key assumptions described above may change as economic and market conditions change. The Group estimates that reasonably possible changes in these assumptions are not expected to cause the recoverable amount of either division to reduce below the carrying amount.

Notes to the financial statements continued

25. Property, plant and equipment

	Fixtures, fittings and equipment £'000	Computer hardware £'000	Total £'000
Cost/deemed cost at transition to IFRS			
1 January 2014	2,661	3,078	5,739
Additions	568	339	907
31 December 2014	**3,229**	**3,417**	**6,646**
1 January 2013	1,888	1,908	3,796
Additions	773	1,170	1,943
31 December 2013	**2,661**	**3,078**	**5,739**
Depreciation			
1 January 2014	1,357	1,524	2,881
Charge for the year	396	554	950
31 December 2014	**1,753**	**2,078**	**3,831**
1 January 2013	1,040	1,144	2,184
Charge for the year	317	380	697
31 December 2013	**1,357**	**1,524**	**2,881**
Net book value			
31 December 2014	**1,476**	**1,339**	**2,815**
31 December 2013	**1,304**	**1,554**	**2,858**

26. Other assets

	2014 £'000	2013 £'000
Amounts recoverable within one year	3,124	197
Amounts recoverable after one year	220	115
	3,344	**312**

27. Prepayments and accrued income

Amounts recoverable within 12 months:	2014 £'000	2013 £'000
Accrued income	2,683	1,810
Other prepayments	4,173	3,299
	6,856	**5,109**

28. Amounts due to banks

Amounts repayable within 12 months:	2014 £'000	2013 £'000
Due to banks – repurchase agreements	304,207	383,071
Due to banks – deposits	600	1,205
Cash collateral received on derivatives	1,100	1,675
	305,907	**385,951**

Collateral given under repurchase agreements

The face value of securities sold under agreements to repurchase at 31 December 2014 was £305 million (31 December 2013: £385 million) all of which were drawn down from the Bank of England under the terms of the Funding for Lending Scheme. The Group conducts these repurchase transactions under the terms of applicable General Master Repurchase Agreement guidelines. Consideration received in return for the collateral is recorded as 'Amounts due to banks' and is accounted for as a financial liability at amortised cost.

29. Customers' accounts

	2014 £'000	2013 £'000
Amounts repayable within one year	3,438,472	2,728,364
Amounts repayable after one year	1,020,490	735,654
	4,458,962	**3,464,018**

30. Other liabilities

Amounts payable within 12 months:	2014 £'000	2013 £'000
Other taxation and social security costs	3,813	3,967
Amounts payable to Invoice Finance customers	10,091	7,146
Trade creditors	2,870	848
Other payables	1,860	2,382
	18,634	**14,343**

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Notes to the financial statements continued

31. Accruals and deferred income

Amounts payable within 12 months:	2014 £'000	2013 £'000
Accruals	18,424	13,787
Deferred income	1,971	1,805
Fee accruals	712	644
	21,107	**16,236**

32. Provisions

	Financial Services Compensation Scheme £'000	Customer redress £'000	Total £'000
1 January 2014	707	450	1,157
Utilised during the year	(2,083)	(671)	(2,754)
Provided during the year	2,606	999	3,605
31 December 2014	**1,230**	**778**	**2,008**
1 January 2013	576	–	576
Utilised during the year	(1,530)	–	(1,530)
Provided during the year	1,661	450	2,111
31 December 2013	**707**	**450**	**1,157**

Financial Services Compensation Scheme ('FSCS')
In common with all regulated UK deposit takers, the Group's principal subsidiary, Aldermore Bank PLC, pays levies to the FSCS to enable the FSCS to meet claims against it. The FSCS levy consists of two parts: a management expenses levy and a compensation levy, which includes capital and interest levies. The management expenses levy covers the costs of running the scheme and the compensation levy covers the amount of compensation the scheme pays, net of any recoveries it makes using the rights that have been assigned to it. During 2008 and 2009 claims were triggered against the FSCS in relation to Bradford & Bingley plc., Kaupthing Singer & Friedlander Ltd, Heritable Bank plc., Landsbanki Islands hf, London Scottish Bank plc. and Dunfermline Building Society. In order to fund the compensation costs of the defaults, the FSCS borrowed £20.4 billion from HM Treasury which is repayable by 31 March 2016.

The FSCS provision at 31 December 2014 of £1,230,000 represents interest levies for scheme years 2014/2015. The interest levy provisions represent the interest costs on the loans borrowed for HM Treasury for the 12 months ending 31 March 2015. The funding rate used is the higher of the 12 month LIBOR plus 100 basis points, and the relevant gilt rate published by the Debt Management Office.

The capital levy provision of £nil (31 December 2013: £nil) includes the Group's estimate of its share of the capital shortfalls on loans made to failed institutions by the FSCS. The shortfalls are expected to be recovered by 31 March 2016 when the loans from HM Treasury are due for repayment. The capital levy is paid in the same financial year in which it is levied.

Customer redress
A provision of £999,000 (31 December 2013: £450,000) in relation to Consumer Credit Act ('CCA') non-compliance has been reflected in the financial statements. The Group has a small number of loans which are regulated under the CCA and has identified that, following changes to the CCA in 2008, certain letters and statements have been sent to customers that do not fully comply with the requirements prescribed by the CCA. Accordingly, these customers are entitled to redress for interest and fees charged on the relevant loans as a result of this technical non-compliance, notwithstanding there is unlikely to have been any customer detriment.

33. Debt securities in issue

Debt securities in issue are repayable from the reporting date in the ordinary course of business as follows:

	2014 £'000	2013 £'000
In more than one year	**279,143**	–

Debt securities in issue with a principal value of £280.5 million are secured on certain portfolios of variable and fixed rate mortgages through the Group's securitisation vehicle, Oak No. 1 PLC. These notes are redeemable in part from time to time, such redemptions being limited to the net capital received from mortgage customers in respect of the underlying assets. There is no obligation for the Group to make good any shortfall. Further disclosure relating to the underlying assets is contained in Note 20.

34. Subordinated notes

	2014 £'000	2013 £'000
Subordinated notes	**36,758**	**35,571**

During 2012 the Group issued £40 million subordinated 12.875 per cent loan notes, repayable in 2022, with an option for the Group to redeem early after five years. The interest rate is fixed until May 2017. The loan notes were issued at a discount, and are carried in the balance sheet at amortised cost using the EIR of 18.597 per cent. In addition to the loan notes, a warrant was issued by the Group's Parent Company, Aldermore Group PLC. The warrant was valued at £2,200,000, and this was treated as a warrant reserve within equity in accordance with the accounting policy in Note 2 f(iii).

35. Share capital

Type	2014 £	2013 £
A1 ordinary shares of £0.10 each	3,569,400	3,569,400
A2 ordinary shares of £0.10 each	5,870,427	5,870,427
B ordinary shares of £0.10 each	385,463	385,463
C ordinary shares of £0.0001 each	13,200	12,845
D ordinary shares of £0.10 each	5,440,522	5,440,522
E ordinary shares of £0.10 each	8,458,428	8,458,428
	23,737,440	**23,737,085**

Rights of class of share:

Type	Full voting rights	Dividend rights	Distribution rights in the event of a sale or wind-up
A1 ordinary shares of £0.10 each	✓	✓	✓
A2 ordinary shares of £0.10 each	✓	✓	✓
B ordinary shares of £0.10 each	✗	✗	✓
C ordinary shares of £0.0001 each	✗	✗	✓
D ordinary shares of £0.10 each	✗	✓	✓
E ordinary shares of £0.10 each	✗	✓	✓

During the year ended 31 December 2014, 7,815,867 C ordinary shares with a total nominal value of £781 were issued for £781.

During the year ended 31 December 2014, 4,260,960 (31 December 2013: 1,361,031) C ordinary shares with a nominal value of £426 (31 December 2013: £136) were repurchased. These shares were subsequently cancelled creating a capital contribution reserve.

During the year ended 31 December 2013, 38,196,551 E ordinary shares with a nominal value of £3,819,656 were issued for £64,138,380. A total of £59,344,711 share premium was recognised on these issues, net of capital raising costs.

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Notes to the financial statements continued

35. Share capital continued

Share premium
On 21 September 2014 AC Acquisitions Limited reduced its share premium by special resolution from £237,305,000 to £nil. This amount has been transferred to retained earnings. AC Acquisitions Limited was re-registered on 30 September 2014 as Aldermore Group PLC.

Share based payments
The Employee Share Programme allows employees (including senior executives) of the Group to receive remuneration in the form of share based payment transactions, whereby employees can purchase equity instruments in Aldermore Group PLC. The consideration paid for the equity instruments was in some cases below the fair value at the transaction date. The grant date fair value of share based payment awards granted is recognised as an employee expense in the Group with a corresponding increase in equity over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the employees become fully entitled to the award.

The amount recognised as an expense is adjusted to reflect the actual number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of awards that meet the related service and non-market performance conditions at the vesting date. For share based payment awards with non-vesting conditions, the grant date fair value of the share based payment is measured to reflect such conditions and there is no true up for differences between expected and actual outcomes.

The consolidated charge reflects that recognised at a subsidiary level with the corresponding credit going to equity.

The following classes of shares have been granted to employees and Directors of the Group. For shares issued below fair value, the difference between fair value and price paid is charged to the income statement by the employing entity over the relevant service period over which the benefits of the awards are received.

Year ended 31 December 2014	**Number of shares granted**	**Weighted average fair value at grant date**
B ordinary shares of £0.10 each	455,021	£1.21
C ordinary shares of £0.0001 each	36,182,667	£0.0018

Year ended 31 December 2013	Number of shares granted	Weighted average fair value at grant date
B ordinary shares of £0.10 each	303,347	£0.52
C ordinary shares of £0.0001 each	–	–
E ordinary shares of £0.10 each	171,027	£1.31

The value from the shares is expected to be derived on a form of exit. However, the Articles of Association stipulate that in the event of an employee leaving the Group, the shares are immediately transferred back to the Company's custody with an amount paid back to the leaver depending on the conditions of leaving.

The fair value of services received in return for shares granted is measured by reference to the fair value of shares granted. The fair value of the shares granted during 2014 and 2013 was based on contemporaneous transactions between unconnected parties in the same, or similar, shares, with adjustments made to take account of the different rights, including dividend rights. The charge in the Group's income statement for the year ended 31 December 2014 in relation to all share based payment transactions was £609,000 (31 December 2013: £162,000).

36. Contingent convertible securities

On 9 December 2014, the Company issued £75 million Fixed Rate Reset Additional Tier 1 Perpetual Subordinated Contingent Convertible Securities (the 'Securities'). Net proceeds arising from the issuance, after deducting issuance costs totalled £73,657,000.

The Securities are perpetual and have no fixed redemption date. Redemption of the Securities is at the option of the Company on 30 April 2020 and annually thereafter. The Securities bear interest at an initial rate of 11.875 per cent p.a. until 30 April 2020 and thereafter at the relevant Reset Interest Rate as provided in the Information Memorandum. Interest is payable on the securities annually in arrears on each interest payment date commencing 30 April 2015 and is non-cumulative. The Borrower has the full discretion to cancel any interest scheduled to be paid on the Securities.

The Securities are convertible into ordinary shares of the Company in the event of the Group's Common Equity Tier 1 ratio falling below 7 per cent.

As the Securities contain no obligation on the Company to make payments of principal or interest they have been classified as equity instruments as required by IAS 32. Accordingly the Securities have been included in equity at the fair value of the proceeds received less any direct costs attributable to the issue of the Securities. Any interest paid on the Securities will be a distribution to holders of equity instruments and shall be recognised directly in equity on the payment date. Although there are number of additional terms relating to events such as acquisition and wind up, there are no circumstances in which the Group has an unavoidable obligation to issue a variable number of its own shares.

The Group has not separated any embedded derivative features because the Group has an accounting policy not to separate a feature that has already been considered in determining that the entire issue is a non-derivative equity instrument.

The classification of the Securities is considered a critical judgement. See Note 3 (d).

37. Statement of cash flows

a) Adjustments for non-cash items and other adjustments included within the income statement

	2014 £'000	2013 £'000
Depreciation and amortisation	3,901	3,822
Write-off of intangible assets	1,628	–
Amortisation of securitisation issuance cost	431	–
Discount accretion on subordinated notes	1,158	971
Impairment losses on loans and advances	9,570	11,468
Unwind of discounting	(2,009)	(957)
Write-off net of recoveries	(6,015)	(1,932)
Net (gain)/loss on debt securities designated at fair value through profit or loss	(9,537)	10,716
Gains on hedged available for sale debt securities recognised in profit or loss	(4,068)	–
Net (gain) on disposal of available for sale debt securities	(2,465)	(1,869)
Interest expense on subordinated notes	5,179	5,150
Interest income on debt securities	(10,655)	(9,529)
Interest expense on debt securities in issue	2,851	–
Equity settled share based payment charge	609	162
	(9,422)	**18,002**

b) (Increase)/decrease in operating assets

	2014 £'000	2013 £'000
Loans and advances to customers	(1,428,766)	(1,325,863)
Loans and advances to banks	(45,680)	10,480
Derivative financial instruments	704	1,390
Fair value adjustments for portfolio hedged risk	(7,175)	–
Other operating assets	(6,870)	(6,859)
	(1,487,787)	**(1,320,852)**

c) Increase in operating liabilities

	2014 £'000	2013 £'000
Amounts due to banks	(80,044)	270,872
Customers' accounts	994,944	1,302,369
Derivative financial instruments	36,331	(13,745)
Fair value adjustments for portfolio hedged risk	1,528	–
Other operating liabilities	10,013	12,431
	962,772	**1,571,927**

Notes to the financial statements continued

37. Statement of cash flows continued

d) Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents comprise cash on demand and overnight deposits classified as cash and balances at central banks (unless restricted) and balances within loans and advances to banks. The following balances have been identified as being cash and cash equivalents.

Excluded balances comprise minimum balances required to be held at the Bank of England as they are not readily convertible to cash in hand or demand deposits. Cash and cash equivalents as at 31 December 2014 exclude £10.9 million held by the securitisation vehicle, Oak No.1 PLC, which is not available to the other members of the Group (31 December 2013: £nil).

	2014 £'000	2013 £'000
Cash and balances at central banks	79,567	192,844
Less excluded balances	(5,919)	(3,828)
Loans and advances to banks	60,371	226,194
	134,019	**415,210**

38. Commitments and contingencies

At 31 December 2014 the Group had undrawn commitments to lend of £404.6 million (31 December 2013: £343.7 million). These relate mostly to irrevocable lines of credit granted to customers.

At the end of the reporting period, the future minimum lease payments under non-cancellable operating leases are payable as follows:

Land and buildings	2014 £'000	2013 £'000
In less than one year	1,545	1,201
Between one and five years	2,942	3,319
More than five years	544	1,123
	5,031	**5,643**

Equipment	2014 £'000	2013 £'000
In less than one year	180	140
Between one and five years	267	14
	447	**154**

At 31 December 2014 the majority of operating leases for equipment related to 49 cars that the Group held under lease (31 December 2013: 64). The majority of these leases are due to expire in 2017.

Legislation

As a financial services Group, Aldermore Group PLC is subject to extensive and comprehensive regulation. The Group must comply with numerous laws and regulations, including the Consumer Credit Act, which significantly affect the way it does business. Whilst the Group believes there are no unidentified areas of failure to comply with these laws and regulations which would have a material impact on the financial statements, there can be no guarantee that all issues have been identified.

Working Time Directive

A recent ruling by the European Court of Justice indicated that under the European Working Time Directive, 'normal pay' for the purposes of calculating statutory holiday pay, includes contractual commission rather than being limited to basic salary. A UK Employment Tribunal is now considering the implications for UK employers under the Working Time Regulations 1998.

Meanwhile, the UK Employment Tribunal has ruled that non-guaranteed overtime payments should be included for the purposes of calculating how much holiday pay a worker should receive. It is therefore expected that the UK Employment Tribunal will conclude on a similar basis for certain commissions.

Based on information and advice to date, the Group does not expect the impact of either the non-guaranteed overtime payments or commissions to be material; however, in the event that analysis, judgements and/or appeals are determined to ultimately be different, the Group expects the likely impact to be immaterial.

39. Related parties

a) Controlling parties

The Group is controlled by AnaCap Financial Partners, II L.P. (52.3 per cent. of voting rights) and AnaCap Financial Partners, L.P. (47.7 per cent. of voting rights) who are the sole voting shareholders of Aldermore Group PLC. The following agreements are in place with a company under their control:

- The Group provides £5 million of block discounting facilities to Syscap Limited, a provider of business finance solutions. The facilities are secured by underlying receivables of short term loans, primarily to solicitors' practices which are funded at a discount to the face value of the loans. The facilities contain appropriate conditions relating to performance, non-performing deal substitution rights and default provisions in line with the Group's standard commercial policies. Pricing on the facilities is subject to normal commercial terms.
- During the year ended 31 December 2014, Syscap Limited introduced business of £21.9 million (31 December 2013: £27.7 million) and received commission of £0.4 million (31 December 2013: £0.3 million) of which £nil is outstanding as at 31 December 2014 (31 December 2013: £nil).
- In addition, the Group has been charged investment monitoring fees and capital raising costs by funds related to AnaCap Financial Partners L.P. of £150,000 for the year ended 31 December 2014 (31 December 2013: £150,000). The balance outstanding at 31 December 2014 is £93,000 (31 December 2013: £195,000).

b) Key management personnel compensation

Until 21 September 2014, key management personnel comprised the Directors of the Group. From 21 September 2014, following changes to the Group's governance structure, key management personnel also comprise the members of the Executive Committee. Prior year comparatives consist of Directors of the Group. Details of the compensation paid to key management personnel are:

	2014 £'000	2013 £'000
Emoluments	3,366	2,747
Compensation for loss of office	20	195
Group contributions to money purchase scheme	72	60
	3,458	**3,002**

Compensation for loss of office for the year ended 31 December 2014 of £20,000 (31 December 2013: £195,000) relates to two key persons (31 December 2013: two key persons) and includes a £nil (31 December 2013: £nil) pension plan contribution.

In addition, in the prior year, the Group's controlling party repurchased key persons shares in the Company for an amount which was £94,000 in excess of the initial purchase price.

The Group made payments of £24,000 in aggregate in respect of two key persons personal pension plans during the year ended 31 December 2014 (31 December 2013: £25,000, two key persons).

During the year ended 31 December 2014, one key person was given the option to purchase B ordinary shares of £0.10 and three key persons were given the option to purchase C ordinary shares of £0.0001 in Aldermore Group PLC, at a discount to market value. 455,021 discounted B ordinary shares were purchased and 26,250,206 discounted C ordinary shares were purchased (31 December 2013: one key person, 303,347 B ordinary shares).

Key persons' emoluments includes £nil of deferred bonus (31 December 2013: £nil).

Notes to the financial statements continued

39. Related parties continued

c) Transactions with key management personnel

The aggregate value of transactions and outstanding balances related to key management personnel (as defined by IAS 24 Related Party Disclosure) were as follows:

	Transaction values for the year ended	
	31 December 2014 £'000	31 December 2013 £'000
Loans	33	2
Deposits	2,015	1,570

	Maximum balance for the year ended	
	31 December 2014 £'000	31 December 2013 £'000
Loans	162	115
Deposits	1,565	1,862

	Balance outstanding as at	
	31 December 2014 £'000	31 December 2013 £'000
Loans	162	115
Deposits	1,565	1,067

The table above includes transactions and balances relating to key management personnel in post at the end of the year. Interest rates charged on loan balances outstanding from related parties are lower than the rates that would be charged in arm's length transactions. During the year ended 31 December 2014 interest was charged on these loans at an annual rate of 0.8 per cent above one month LIBOR. These loan balances are not secured. All deposit arrangements have been operated by the Group on commercial terms and conditions.

40. Financial instruments and fair values

The following tables summarise the classification and carrying amounts of the Group's financial assets and liabilities:

31 December 2014	Loans and receivables £'000	Available for sale £'000	Designated at fair value through profit or loss £'000	Fair value through profit or loss (required) £'000	Fair value hedges £'000	Liabilities at amortised cost £'000	Total £'000
Cash and balances at central banks	79,567	–	–	–	–	–	79,567
Loans and advances to banks	117,401	–	–	–	–	–	117,401
Debt securities	–	355,328	154,356	–	–	–	509,684
Derivatives held for risk management	–	–	–	8,168	–	–	8,168
Fair value adjustment for portfolio hedged risk	–	–	–	–	7,175	–	7,175
Loans and advances to customers	4,801,064	–	–	–	–	–	4,801,064
Other assets	1,298	–	–	–	–	–	1,298
Total financial assets	**4,999,330**	**355,328**	**154,356**	**8,168**	**7,175**	**–**	**5,524,357**
Amounts due to banks	–	–	–	–	–	305,907	305,907
Customers' accounts	–	–	–	–	–	4,458,962	4,458,962
Derivatives held for risk management	–	–	–	54,198	–	–	54,198
Fair value adjustment for portfolio hedged risk	–	–	–	–	1,528	–	1,528
Other liabilities	–	–	–	–	–	14,778	14,778
Debt securities in issue	–	–	–	–	–	279,143	279,143
Subordinated notes	–	–	–	–	–	36,758	36,758
Total financial liabilities	**–**	**–**	**–**	**54,198**	**1,528**	**5,095,548**	**5,151,274**

31 December 2013	Loans and receivables £'000	Available for sale £'000	Designated at fair value through profit or loss £'000	Fair value through profit or loss (required) £'000	Fair value hedges £'000	Liabilities at amortised cost £'000	Total £'000
Cash and balances at central banks	192,844	–	–	–	–	–	192,844
Loans and advances to banks	237,544	–	–	–	–	–	237,544
Debt securities	–	192,755	162,898	–	–	–	355,653
Derivatives held for risk management	–	–	–	8,872	–	–	8,872
Loans and advances to customers	3,373,844	–	–	–	–	–	3,373,844
Other assets	159	–	–	–	–	–	159
Total financial assets	**3,804,391**	**192,755**	**162,898**	**8,872**	**–**	**–**	**4,168,916**
Amounts due to banks	–	–	–	–	–	385,951	385,951
Customers' accounts	–	–	–	–	–	3,464,018	3,464,018
Derivatives held for risk management	–	–	–	17,867	–	–	17,867
Other liabilities	–	–	–	–	–	10,304	10,304
Subordinated notes	–	–	–	–	–	35,571	35,571
Total financial liabilities	**–**	**–**	**–**	**17,867**	**–**	**3,895,844**	**3,913,711**

The following table summarises the carrying amounts and fair values of those financial assets and liabilities not presented in the statement of financial position at fair value:

	2014		2013	
	Carrying value £'000	**Fair value £'000**	Carrying value £'000	Fair value £'000
Cash and balances at central banks	79,567	79,567	192,844	192,844
Loans and advances to banks	117,401	117,401	237,544	237,544
Loans and advances to customers	4,801,064	4,807,766	3,373,844	3,351,249
Other assets	1,298	1,298	159	159
Total financial assets	**4,999,330**	**5,006,032**	**3,804,391**	**3,781,796**
Amounts due to banks	305,907	305,907	385,951	385,951
Customers' accounts	4,458,962	4,469,413	3,464,018	3,473,176
Other liabilities	14,778	14,778	10,304	10,304
Debt securities in issue	279,143	281,281	–	–
Subordinated notes	36,758	47,930	35,571	44,219
Total financial liabilities	**5,095,548**	**5,119,309**	**3,895,844**	**3,913,650**

Key considerations in the calculation of the disclosed fair values for those financial assets carried at amortised cost include the following:

Cash and balances at central banks
These represent amounts with an initial maturity of less than three months and as such their carrying value is considered a reasonable approximation of their fair value.

Loans and advances to banks
These represent either amounts with an initial maturity of less than three months or longer term variable rate deposits placed with banks, where adjustments to fair value in respect of the credit risk of the counterparty are not considered necessary. Accordingly the carrying value of the assets is considered to be not materially different from their fair value.

Loans and advances to customers
For fixed rate lending products the Group has estimated the fair value of the fixed rate interest cash flows by discounting those cash flows by the current appropriate market reference rate used for pricing equivalent product plus the credit spread attributable to the borrower. For standard variable rate lending products, and fixed rate products when they revert to the Group's standard variable rate, the interest rate on such products is considered equivalent to a current market product rate and as such the Group considers the discounted future cash flows of these mortgages to be equal to their carrying value. The fair value estimations do not incorporate adjustments for future credit risk, however, incurred loss provisions are deducted from the fair value amounts.

Notes to the financial statements continued

40. Financial instruments and fair values continued

Other assets and liabilities
These represent short term receivables and payables and as such their carrying value is not considered to be materially different from their fair value.

Amounts due to banks
These mainly represent securities sold under agreements to repurchase which were drawn down from the Bank of England under the terms of the Funding for Lending Scheme. These transactions are collateralised by UK Government Treasury Bills, which have a low susceptibility to credit risk, so adjustments to fair value in respect of the credit risk of the counterparty are not considered necessary. Accordingly the carrying value of the liabilities are considered to be not materially different from their fair value.

Customers' accounts
The fair value of fixed rate customers' accounts have been determined by discounting estimated future cash flows based on market interest rates on equivalent deposits. Customers' accounts at variable rates are at current market rates and therefore the Group regards the fair value to be equal to the carrying value. The estimated fair value of deposits with no stated maturity is the amount repayable on demand.

Debt securities in issue
Where securities are actively traded in a recognised market, with readily available and quoted prices, these have been used to value the securities. These securities are therefore regarded as having Level 1 fair values.

Subordinated notes
The estimated fair value of the subordinated notes is based on discounted cash flows using interest rates for similar liabilities with the same remaining maturity, credit ranking and rating. The calculated fair value takes no account of the warrants issued separately to the holders of the subordinated notes, which have been separately accounted for as a capital contribution within equity (see Note 34).

The following table provides an analysis of financial assets and liabilities held on the consolidated statement of financial position at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

31 December 2014	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
Financial assets:				
Derivatives held for risk management	–	8,168	–	8,168
Debt securities:				
Asset backed securities	–	16,328	–	16,328
UK Gilts and Supranational bonds	468,840	–	–	468,840
Corporate bonds	24,516	–	–	24,516
	493,356	**24,496**	**–**	**517,852**
Financial liabilities:				
Derivatives held for risk management	–	54,198	–	54,198
	–	**54,198**	**–**	**54,198**

Level 1: Fair value determined using quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Fair value determined using directly or indirectly observable inputs other than unadjusted quoted prices included within Level 1 that are observable.

Level 3: Fair value determined using one or more significant inputs that are not based on observable market data.

31 December 2013	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
Financial assets:				
Derivatives held for risk management	–	8,872	–	8,872
Debt securities:				
Asset backed securities	–	77,844	–	77,844
UK Gilts and Supranational bonds	277,809	–	–	277,809
	277,809	**86,716**	**–**	**364,525**
Financial liabilities:				
Derivatives held for risk management	–	17,867	–	17,867
	–	**17,867**	**–**	**17,867**

The fair values of UK Gilts and Supranational bonds are based on quoted bid prices in active markets.

The fair values of asset backed securities are based on prices provided by third party pricing services, but before relying on these prices, the Group has obtained an understanding of how the prices were obtained to ensure that each investment is assigned an appropriate classification within the fair value hierarchy.

The fair values of derivative assets and liabilities are determined using widely recognised valuation models for determining the fair values of common derivative financial instruments such as interest rate swaps that use only observable market data that require little management judgement and estimation. Credit value and debt value adjustments have not been applied as the derivative assets and liabilities are largely collateralised.

Fair value measurement – financial assets and liabilities held at amortised cost

All the fair values of financial assets and liabilities carried at amortised cost are considered to be Level 2 valuations which are determined using directly or indirectly observable inputs other than unadjusted quoted prices, except for debt securities in issue which are Level 1 and Loans and advances to customers which are Level 3.

Fair value of transferred assets and associated liabilities

Securitisation vehicle

The beneficial ownership of the loans and advances to customers sold to the securitisation vehicle by the Bank fail the derecognition criteria, and consequently, these loans remain on the balance sheet of the seller. The seller therefore recognises a deemed loan financial liability on its balance sheet and an equivalent deemed loan asset is held on the securitisation vehicle's balance sheet. The deemed loans are repaid as and when principal repayments are made by customers against these transferred loans and advances.

The securitisation vehicle has issued fixed and floating rate notes which are secured on loans and advances to customers. The notes are redeemable in part from time to time, such redemptions being limited to the net capital received from mortgagors in respect of the underlying assets.

The Group retains substantially all of the risks and rewards of ownership. The Group benefits to the extent to which surplus income generated by the transferred mortgage portfolios exceeds the administration costs of these mortgages. The Group continues to bear the credit risk of these mortgage assets.

The results of the securitisation vehicle listed in Note 23 is consolidated into the results of the Group. The table below shows the carrying value and fair value of the assets transferred to the securitisation vehicle and its associated liabilities. The carrying value presented below is the carrying amount recorded in the books of the subsidiary company, some of these notes are held internally by the Group and as such are not shown in the consolidated statement of financial position of the Group.

31 December 2014	Carrying amount of transferred assets not derecognised £'000	Carrying amount of associated liabilities £'000	Fair value of transferred assets not derecognised £'000	Fair value of associated liabilities £'000	Net position £'000
Oak No. 1 PLC	293,110	279,143	295,526	281,281	14,245

In addition to the transferred assets not derecognised, the Group held within Oak No. 1 PLC Loans and advances to banks amounting to £18.4 million. This represents amounts of interest and principal already collected from the transferred mortgage portfolios which will be required to be distributed to the note holders of Oak No. 1 PLC on the next quarterly repayment date in 2015.

41. Risk management

A key component of the Group's business strategy is the effective management of risk in order to ensure that the Group maintains sufficient capital, liquidity and controls at all times, and acts in a reputable way, taking into account the interests of customers, regulators and shareholders.

Given the nature of the activities undertaken, the principal risks that the Group faces are strategic risk, credit risk, capital risk, liquidity risk, interest rate risk, market risk, operational risk and conduct risk. The Group has not defined regulatory risk as a single category of risk, owing to the broad nature of regulation. Prudential regulatory risks are covered as part of capital risk, liquidity risk and operational risk. Conduct regulatory risks are covered under conduct risk.

The Group's Risk Management Framework, policies and procedures are subject to ongoing improvement, and are regularly reviewed and updated to ensure that they accurately identify the risks that the Group faces in its business activities. In addition, the Group continues to invest in and develop its risk management systems and resources to ensure that the risk management function, governance and infrastructure are appropriate for the nature, scale and complexity of the business, which has and continues to experience growth.

All these risks arise as a result of the Group's normal operations. The Group does not enter into transactions for speculative purposes. The Group uses derivatives such as interest rate swaps to manage interest rate and other market risks.

Notes to the financial statements continued

41. Risk management continued

The risk management structure has developed over the current and comparative period presented. In prior periods, the governance structure operated primarily at an Aldermore Bank PLC level. Whilst it has continued to operate at the Aldermore Bank PLC level during the year ended 31 December 2014, the intention is for the structure to operate equally at the Aldermore Group PLC and Aldermore Bank PLC level. The following sections describe the Risk Management Framework and committee structure in operation at 31 December 2014.

A review of the governance structure at an Executive Committee level was performed in December 2014. A number of changes were made which became effective from 1 January 2015. Details of the revised structure are provided within the Corporate Governance section on page 45.

Further details regarding the Group's capital management are provided in Note 42.

a) Risk Management Framework

A core objective for the Group is the effective management of risk. The responsibility for identifying and managing the principal risks ultimately rests with the Group's Board of Directors. The Board has ultimate responsibility for setting the Group's strategy, risk appetite and control framework. The Risk Management Framework is outlined below, indicating the relevant governance and control structure for each principal risk.

i) Principal risks

The principal risks faced by the Group are listed below:

- strategic risk – the risks which can affect the Group's ability to achieve its corporate and strategic objectives;
- credit risk – the risk of financial loss arising from a borrower or counterparty failing to meet their financial obligations to the Group in accordance with agreed terms;
- capital risk – the risk that the Group has insufficient capital to cover regulatory requirements and growth plans;
- liquidity risk – the risk that the Group is not able to meet its financial obligations as they fall due, or can do so only at excessive cost;
- interest rate risk – the risk of financial loss through un-hedged or mismatched asset and liability positions sensitive to changes in interest rates;
- market risk – the financial impact from movements in market prices on the value of assets and liabilities;
- operational risk – the risk of financial loss and/or reputation damage resulting from inadequate or failed internal processes, people and systems or from external events including financial crime; and
- conduct risk – the risk of detriment caused to the Groups' customers due to the inappropriate execution of its business activities and processes.

The Risk Management Framework is designed to ensure that each risk is managed, monitored and overseen through a dedicated risk-individual committee. Each risk has a defined risk appetite which is controlled through documented policies and frequent reporting, and is overseen by a governance process.

The Group's Risk Management Framework is outlined below, indicating the relevant governance and control structure for each principal risk.

The Risk Management Framework includes the following components:

- policy and control documents – the overarching document which sets out the overall appetite and how each principal risk is managed;
- risk reporting – the primary reporting document relating to the risk;
- stress testing – the primary means to understand how the risk area behaves under stressed conditions, and the implication for capital and liquidity resources; and
- monitoring committees – the principal committee responsible for monitoring risk is the Risk Committee. This is supported by further oversight by the Group Risk function, executive committees, other Board level governance committees and internal audit.

To support the Risk Management Framework, the Group operates a 'three lines of defence' model:

- the first line of defence comes through operational management, who manage risk by operating within approved policies and implementing and maintaining appropriate systems and controls that are effective on a daily basis.
- the second line of defence comprises governance and oversight. Governance and oversight include the monitoring committees and the Group Risk function. These functions cover all principal risk areas, such as credit risk, interest rate risk, operational risk and liquidity risk. The committee structure is covered in more detail below.
- the third line of defence is independent assurance checking. This is provided by the Internal Audit function. Assurance reporting is provided to the Audit Committee.

ii) Control framework
The control framework operates over each principal risk as described below:

'ALCO' is the Asset and Liability Committee.

Escalation procedures exist which seek to ensure that issues are reported and addressed at the right level.

	Group risk oversight						
	Business model risk	Prudential risks					Conduct risks
Principal risk	Strategic risk	Credit risk	Capital risk	Liquidity risk	Market & interest rate risk	Operational risk	Conduct risk
Control documents	Business plan (strategic objectives/ financial forecast)	Credit policy	ICAAP	ILAA & liquidity policy	Interest rate policy	Operational risk policy and key risk registers	Conduct risk policy
Risk reporting	Strategic risk register & financial reporting	Credit pack	ALCO & capital forecast	ALCO & treasury forecast	ALCO & treasury forecast	OPCO & operational risk reporting	Conduct risk reporting
Stress testing	Strategic risk stress-testing pack (also ICAAP)	ICAAP	ICAAP	ILAA	ICAAP	ICAAP	ICAAP
Second line monitoring committee	ExCo (report to Board)	Management Credit Committee (report to ExCo)	ALCO (report to ExCo)	ALCO (report to ExCo)	ALCO (report to ExCo)	Operating Committee (report to ExCo)	Product Committees (report to ALCO/ ExCo)
Additional oversight	Board / ExCo / Internal audit oversight						

A detailed analysis of all key risks has been considered as part of the capital adequacy assessment and is documented in the Internal Capital Adequacy Assessment Process ('ICAAP') report, which is approved by the Board. Liquidity risk is individually assessed through the Individual Liquidity Adequacy Assessment ('ILAA'), also approved by the Board. Operational risk is managed through the Operational Risk Policy and Key Risks Registers.

Notes to the financial statements continued

41. Risk management continued

a) Risk Management Framework continued

iii) Risk oversight, monitoring and reporting
The Group has a Chief Risk Officer ('CRO') who is responsible for ensuring each risk is adequately monitored, managed and mitigated. Through the Group Risk function, the CRO is responsible for providing assurance to the Board and the Directors that the principal risks are adequately managed and that the Group is operating within its risk appetites.

The below diagram presents the functional focus of the risk department:

Prudential risk management covers liquidity, market and capital risk. Strategic risk is managed collectively by the Board and the Executive Committee.

Group Risk is an independent risk management function, and is separate from the operational and sales side of the Group. Group Risk is responsible for ensuring that appropriate risk management processes, techniques and controls are in place, and that they are sufficiently robust.

The Group Risk function provides periodic independent reports on risk positions, risk management and performance against the risk appetite statements for all principal risks faced by the Group. Risk reports are provided to the Operating Committee, Executive Committee, Risk Committee, Audit Committee and Board.

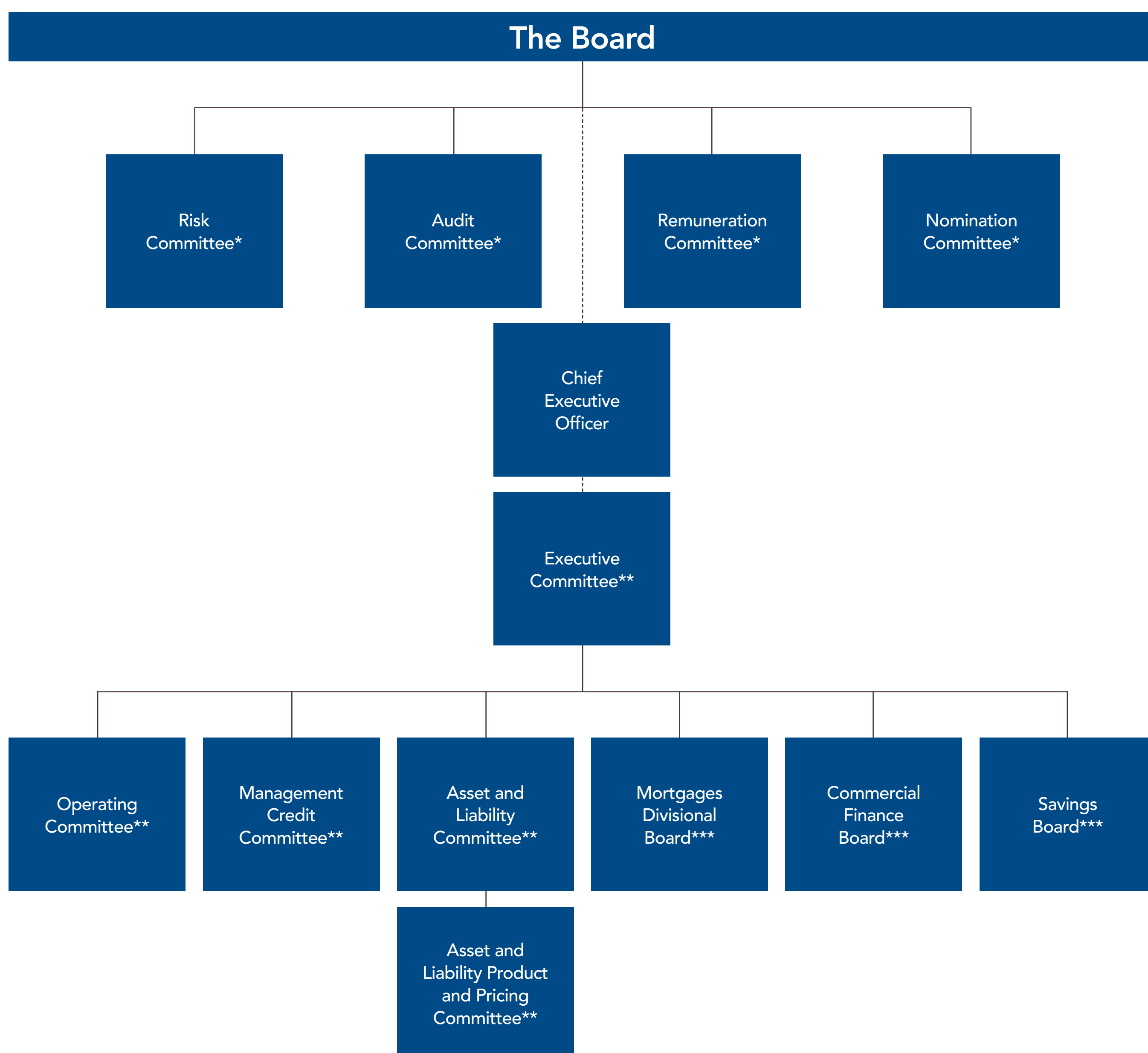
The reporting and oversight process is designed to ensure the committees which form the governance structure are informed and aware of the principal risks and that there are adequate controls in place for these risks. Reports are produced on each principal risk and the frequency ranges from daily to monthly, according to what is appropriate for the risk.

iv) Committee structure

The responsibility for managing the principal risks ultimately rests with the Group's Board of Directors.

The Group's committee structure with regard to risk management is outlined below. This structure was in existence as at 31 December 2014.

A review of the governance structure at an Executive Committee level was performed in December 2014. A number of changes were made which became effective from 1 January 2015. Details of the revised structure are provided within the Corporate Governance section on page 45.



* Non-Executive oversight

** Executive/Second line oversight

*** First Line

Financial statements

Notes to the financial statements continued

41. Risk management continued

a) Risk Management Framework continued

Set out below are the details of the Board and principal committees which enable high level controls to be exercised over the Group's activities. The frequency of meetings is detailed below, although these committees will meet more frequently as circumstances require. The details provided below represent the operation of each committee as at 31 December 2014.

In the prior period, the risk management structure operated primarily at an Aldermore Bank PLC level. Whilst it has continued to operate at the Aldermore Bank PLC level during the year ended 31 December 2014, the intention is for the structure to operate equally at the Aldermore Group PLC and Aldermore Bank PLC level.

Committee	Risk focus
The Board	The Board is the primary governing body and has ultimate responsibility for setting the Group's strategy, corporate objectives and risk appetite. The strategy and risk appetites take into consideration the interests of depositors, borrowers and shareholders. The Board defines and approves the level of risk which the Group is willing to accept and is responsible for maintaining a sufficient control environment to manage the principal risks. The Board is also responsible for ensuring the capital and liquidity resources are adequate to achieve the Group's objectives without taking undue risk. The Board also maintains a close oversight of current and future activities, through a combination of monthly board reports including financial results, operational reports, budgets and forecasts and reviews of the main risks set out in the ICAAP and ILAA reports.
Audit Committee	During 2014, the Audit and Risk Committee separated into two separate committees. The Audit Committee is responsible for reviewing the Group's internal control environment and monitors the financial integrity of the financial statements, and involves internal and external auditors in that process. It focuses in particular on compliance with accounting policies and ensuring that an effective system of internal financial control is maintained.
Risk Committee	During 2014, the Audit and Risk Committee separated into two separate committees. The Board has delegated responsibility for oversight of the Group's principal risks to the Risk Committee, which includes reviewing the performance against risk appetites and the effectiveness of the Group's internal controls and risk management processes. This committee oversees the development, implementation and maintenance of the Group's Risk Management Framework, ensuring that its strategy, principles, policies and resources are aligned to the Group's risk appetite, as well as to regulatory and industry best practices.
Remuneration Committee	The Remuneration Committee reviews remuneration matters, employee benefits and performance related pay structures for the Group. It is also responsible for considering and determining the Group's remuneration policy and reviewing its adequacy and effectiveness.
Nomination Committee	The Nomination Committee reviews the structure and composition of the Board, succession planning and material appointments, in particular Board appointments.
Executive Committee	The Executive Committee takes day-to-day responsibility for the running of the business. The Executive Committee implements the strategy and financial plan which is approved at the Board and ensures the performance of the business is conducted in accordance with the Board's instructions. The Executive Committee interacts with the Board via the CEO.
Management Credit Committee	This committee meets monthly and is responsible for monitoring portfolio performance to ensure it remains within the Bank's credit risk appetite and reviewing and maintaining credit and lending policies. Detailed credit reports are produced covering each specific business line. These reports are reviewed by the Management Credit Committee and Group Risk. The credit packs report on the quality of new lending, credit performance, arrears and non-performing loans and also provides detail on the composition of the credit portfolios.
Asset & Liability Committee ('ALCO')	The Executive Committee has delegated responsibility for managing the Group's exposure to capital, liquidity, interest rate and market risk to the ALCO. The ALCO meets monthly and ensures that the firm adheres to the market risk, interest rate risk and liquidity policies and objectives set down by the Board. It also has responsibility for ensuring that the policies that are implemented are adequate to meet prudential and regulatory targets. The committee is also responsible for the effective management of the Group's assets and liabilities and the impact on capital and liquidity of future business activity and management actions.

Operating Committee ('OPCO')	The Operating Committee reviews IT, operational and compliance matters to ensure appropriate systems and controls exist which are able to support the needs of the Group including any projects and change programmes. The committee monitors operational risk, including regulatory, compliance and conduct risk, implements the operational risk management policy and reviews operational performance, including key risk indicator reports.
Asset and Liability: Product and Pricing Committee	The committee meets monthly to review, approve and set the pricing for new products proposals, and reviews product performance as well as on-going pricing initiatives and strategic directions on product launch. The committee is also responsible for the effective oversight of the Group's conduct risk processes for new products.
Divisional Boards (Mortgages, Commercial Finance and Savings)	The Divisional Boards meet on a monthly basis and provide a forum for open discussion and decisions on key issues affecting the relevant business segment. Specific responsibilities include the delivery of strategic objectives, budget formulation and financial delivery, recruitment, training, implementing and maintaining effective controls, product review and performance and management of conduct risk.

v) Risk appetite

The Risk Management Framework is the means through which risks are identified, assessed, reported and monitored. The Group has set a defined risk appetite for each of the principal risks and performance against the risk appetite statements is monitored and reported on a regular basis. The risk appetites are set by the Board and implemented by the Executive Committee. The Group Risk function is responsible for ensuring the Group operates within the stated risk appetites.

The risk appetite framework has the following components:

- risk appetite statement: the articulation of the level and types of risk that the Group is willing to accept in order to achieve its business objectives;
- risk capacity: the maximum level of risk the Group can assume before breaching constraints determined by regulatory capital and liquidity needs;
- risk limits: quantitative measures that allocate the Group's aggregate risk appetite statement to individual activities. Where possible this includes forward looking measures; and
- risk profile: the point in time assessment of the Group's net risk exposure.

The following section provides details of the Group's risk appetite for each of the principal risks:

Strategic risk appetite

The strategic risk appetite is measured in terms of the deviation against key performance indicators which form part of the Group's business plan. Performance against the strategic risk appetite is measured every quarter and reported to the Risk Committee.

Credit risk appetite

The Group operates a business line individual credit risk appetite, as well as an overall credit risk appetite for its lending activities. Expected losses are factored into the budgeting and forecast process and reflect the Group's expected view of lending performance, taking into account recent performance data and the prevailing economic environment.

The Group recognises that actual losses may differ from forecasted or budgeted values. The credit risk appetites are set as an upper limit on losses from credit and credit related fraud and so this limit is set above the budgeted value for each business.

Capital risk appetite

Capital Risk is the risk that the Group has insufficient capital to cover regulatory requirements and/or growth plans. The Group maintains sufficient capital to cover regulatory requirements, including any capital planning buffers, and maintains a management capital buffer.

Liquidity risk appetite

The Board has set a liquidity risk appetite which aims to ensure that a prudent level of liquidity is held to cover an unexpected liquidity outflow such that the Group will be able to meet its financial commitments during an extended period of stress. Additionally, reputational risks are kept low through honouring pipeline commitments expected to complete during a three month period.

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Notes to the financial statements continued

41. Risk management continued

a) Risk Management Framework continued

Market and interest rate risk appetite
The Group aims to minimise interest rate risk and has a policy of matching fixed or variable rate assets with liabilities of a comparable interest rate basis, supplemented by derivatives such as interest rate swaps.

The Group does not seek to take or expose itself to market risk, and does not carry out proprietary trading, although certain liquid asset investments which form part of the liquid asset buffer carry mark to market risk which is regularly monitored.

Operational risk appetite
The Group aims to maintain operational systems and controls and seeks to operate within a defined level of operational risk. The operational risk appetite considers risk events, the assessment of internal controls, as well as holding additional capital for certain operational risks.

Conduct risk appetite
The Group has a zero appetite for systemic unfair outcomes, which may result in significant detriment to the Group's customers. Systemic unfair outcomes may arise from poor product design, poor sales processes or unacceptable operational practices which risk repeated or continual outcomes which are detrimental to customers.

b) Credit risk

i) Overview
Credit risk is the risk of financial loss arising from a borrower or counterparty failing to meet their financial obligations to the Group in accordance with agreed terms. This risk arises from the Group's lending activities as a result of defaulting mortgage, lease and loan contracts and is the most significant risk faced by the Group.

Although credit risk arises from the Group's loan book it can also arise from off balance sheet activities. The Group does not actively trade in financial instruments, other than for liquidity management purposes.

Credit risks associated with lending are managed through the use of detailed lending policies which outline the approach to lending, underwriting criteria, credit mandates, concentration limits and product terms. The Group maintains a dynamic approach to credit management and aims to take necessary steps if individual issues are identified or if credit performance deteriorates, or is expected to deteriorate, due to borrower, economic or sector-specific weaknesses.

The Group seeks to mitigate credit risk by focusing on business sectors where it has specific expertise and through limiting concentrated exposures on larger loans, certain sectors and other factors which can represent higher risk. The Group also seeks to obtain security cover, and where appropriate, personal guarantees from borrowers.

Due to the retail and SME markets the Group operates in, external rating agency ratings for borrowers are not typically available. However, credit risk is assessed through applying a combination of due diligence, reviewing credit reference agency reports, reviewing financial information, credit scores and the use of underwriters.

Group Risk, the Management Credit Committee and Risk Committee have oversight responsibility for credit risk.

ii) Credit exposure
Maximum exposure to credit risk
The following table presents the Group's maximum exposure to credit risk of financial instruments on the balance sheet and commitments to lend before taking into account any collateral held or other credit. The maximum exposure to credit risk for loans, debt securities, derivatives and other on balance sheet financial instruments is the carrying amount and for loan commitments the full amount of any commitment to lend that is irrevocable or is revocable only in response to material adverse change.

Included in the statement of financial position:	Note	**2014 £'000**	2013 £'000
Cash and balances at central banks		79,567	192,844
Loans and advances to banks		117,401	237,544
Debt securities		509,684	355,653
Derivatives held for risk management		8,168	8,872
Loans and advances to customers		4,823,638	3,394,872
Other assets		1,298	159
		5,539,756	4,189,944
Commitments to lend	38	404,593	343,652
Gross credit risk exposure		**5,944,349**	**4,533,596**
Less: allowance for impairment losses	20	(22,574)	(21,028)
Net credit risk exposure		**5,921,775**	**4,512,568**

iii) Credit risk management

Credit risk – lending

The Group targets SME and mortgage customers. Credit risk is managed in accordance with lending policies, the risk appetite and the Risk Management Framework. Lending policies and performance against risk appetites are reviewed regularly. This section provides further detail on the specific areas where the Group is exposed to credit risk.

Residential Mortgages

The Group's residential mortgage lending focuses on owner occupied residential and buy-to-let mortgage loans.

All applications are reviewed by an experienced team of underwriters who assess each application. Applications are underwritten in accordance with a residential mortgage lending policy and each loan has to undergo an affordability assessment, which takes into account the specific circumstances of each borrower. Information is obtained on all loan applications from credit reference agencies which provide a detailed insight on the applicant's credit history and indebtedness, which is reviewed by the underwriters.

The Group aims to take a conservative approach to lending, lending up to a maximum of 85 per cent loan-to-value ('LTV') on a single dwelling without further guarantees and undertakes a full valuation on all properties which act as security. Valuation reports are produced by an experienced panel of qualified external valuers. The Group also offers mortgages with a LTV between 85 per cent and 95 per cent via the Help to Buy scheme. This lending has an associated government guarantee which reduces the credit risk to the Group.

The Group does offer limited advice to mortgage borrowers but does not sell payment protection insurance policies.

SME Commercial Mortgages

The Group provides commercial mortgages to businesses who own their own property and to commercial and residential property investors. Loans are typically to SMEs and secured on smaller properties, with limits in place for loans over £1.5 million. A team of experienced underwriters review all applications.

Properties are individually valued and a detailed report produced to ensure the property represents suitable security. Consideration is given to whether the property has an alternate use and/or can be disposed of within a reasonable period in the event of default, where the asset acting as security has to be recovered and sold. Valuations are performed by qualified external surveyors. The valuation reports also provide commentary on the tenancy/letting of properties where the commercial mortgages are connected to an investment property transaction. In-house valuation experts approve the panel of qualified external valuers and perform ongoing quality monitoring.

Affordability assessments are performed on all loans and other forms of security are often obtained, such as a personal guarantee.

Loans to commercial mortgage customers are secured on properties solely located in the UK, although there are various sectors within the UK to which the Group is not currently lending. Concentration risks are monitored and credit exposures are diversified by sector and geography. Regular reviews are performed on loans in the portfolio, with particular attention paid to larger exposures.

Property Development

The Group has a small portfolio of property development loans, which are predominantly for the purpose of building and developing residential property.

Although the UK property sector has shown signs of recovery, the Group continues to be cautious about property development financing. The Group has maintained a conservative approach to development lending and developments are regularly inspected by the Group and external quantity surveyors.

Invoice Finance

The invoice financing activity provides working capital finance for SME clients. This activity may also include credit control and collection services for clients.

The approval process includes a review of the management, financial and operational strength of the client's business and careful consideration is given to the quality and contractual collectability of the underlying receivables which act as security. Information on the business and the individuals behind the business are reviewed and financial and credit information is obtained from external credit reference agencies.

During the term of the facility, in-life monitoring, audits and reconciliations are performed to ensure the risk of fraud and default risks associated with client failure are carefully managed. There is significant diversification at the invoice level which heavily mitigates concentration risk.

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Notes to the financial statements continued

41. Risk management continued

b) Credit risk continued

Asset Finance

The asset finance business line originates loan and lease contracts to a diversified range of end users and finances a range of assets. Exposures range from public sector organisations to corporates, SMEs and sole traders. Asset finance and leasing to smaller businesses can represent a higher risk, although the majority of contracts will have tangible assets acting as security which can be recovered and sold in the event of default.

Expert manual underwriting, supported by data driven by risk management systems and automated decision making is used to underwrite credit proposals. Information on the business and the individuals behind the business are carefully reviewed and financial and credit information is obtained from external credit reference agencies. Assets which act as security are valued and the future resale value of assets is also considered where appropriate. Audits and site visits are used to ensure the Group maintains an awareness of the location, use and condition of assets being financed where considered necessary.

At the balance sheet date the Group has nominal direct residual value risk.

Impaired and past due loans

The table below provides information on the payment due status of loans and advances to customers:

Details of the methodologies and estimates used to determine the allowances for loan impairments are provided in Note 3.

	Residential Mortgages £'000	SME Commercial Mortgages £'000	Asset Finance £'000	Invoice Finance £'000	Total £'000
2014					
Neither past due nor individually impaired	2,542,738	994,410	1,039,692	183,324	4,760,164
Past due but not individually impaired	19,405	16,061	7,167	–	42,633
Individually impaired	6,003	6,292	2,614	5,932	20,841
	2,568,146	**1,016,763**	**1,049,473**	**189,256**	**4,823,638**
2013					
Neither past due nor individually impaired	1,654,324	752,387	715,971	213,749	3,336,431
Past due but not individually impaired	23,715	4,733	5,228	–	33,676
Individually impaired	3,634	9,979	3,238	7,914	24,765
	1,681,673	**767,099**	**724,437**	**221,663**	**3,394,872**

Past due but not individually impaired loans are further analysed as follows:

Past due but not individually impaired	2014 £'000	2013 £'000
– Up to 2 months past due	29,989	27,318
– 2 to 3 months past due	12,644	6,358
Total	**42,633**	**33,676**

Impairment coverage is analysed as follows:

Coverage ratio	2014 £'000	2013 £'000
Gross Loans and advances	4,823,638	3,394,872
Of which individually impaired	20,841	24,765
Impaired as a % of gross loans and advances	0.43%	0.73%
Allowance for losses – individual provisions	14,047	14,714
Coverage	**67.40%**	**59.41%**

The credit quality of assets that are neither past due nor individually impaired are internally analysed as follows:

2014	Residential Mortgages Residential £'000	 Buy-to-Let £'000	 Total £'000	SME Commercial Mortgages Commercial £'000	 Buy-to-Let £'000	 Total £'000	Asset Finance Total £'000	Invoice Finance Total £'000
Low risk	585,826	1,380,644	1,966,470	257,375	369,693	627,068	59,262	–
Medium risk	341,771	172,479	514,250	113,865	105,938	219,803	839,553	6,502
High risk	38,040	23,978	62,018	103,308	44,231	147,539	140,877	176,822
Total	**965,637**	**1,577,101**	**2,542,738**	**474,548**	**519,862**	**994,410**	**1,039,692**	**183,324**
Fair value of collateral held	**965,559**	**1,576,914**	**2,542,473**	**474,548**	**519,862**	**994,410**	**738,390**	**181,752**

2013	Residential Mortgages Residential £'000	 Buy-to-Let £'000	 Total £'000	SME Commercial Mortgages Commercial £'000	 Buy-to-Let £'000	 Total £'000	Asset Finance Total £'000	Invoice Finance Total £'000
Low risk	392,637	965,253	1,357,890	171,859	268,893	440,752	32,160	–
Medium risk	115,445	151,279	266,724	86,927	87,856	174,783	579,290	7,388
High risk	12,400	17,310	29,710	80,199	56,653	136,852	104,521	206,361
Total	**520,482**	**1,133,842**	**1,654,324**	**338,985**	**413,402**	**752,387**	**715,971**	**213,749**
Fair value of collateral held	**520,127**	**1,132,891**	**1,653,018**	**338,985**	**413,402**	**752,387**	**509,456**	**206,342**

The above categorisation is based on internal grading models.

Low medium high grading methodology:

The grading models are used to generate a consistent Group-wide approach for the grading of customer credit risk exposures for all lending businesses, and provide a relative internal ranking of risk. Drivers for the grade mapping include external credit reference agency risk scores, property valuations and qualitative factors. The relative measure of risk reflects a combined assessment of the Probability of Default ('PD') by the customer and an assessment of the expected loss in the event of default.

The probability of default refers to the probability of a customer or counterparty defaulting, which is typically taken as three payments past due, within the next 12 months. A default probability model predicts this probability by using credit scores along with financial, behavioural and qualitative inputs.

The main drivers of loss in the event of default i.e. Loss Given Default ('LGD') are the propensity to 'cure', that is for an account to be restored to a performing status, and the level of security held in relation to the credit exposure. The level of security varies, ranging from a small number of very short term unsecured loans in the Asset Finance business, to highly secured loans on residential property within the Residential Mortgage business. The valuation method for assets is specific to the nature of the collateral and includes indexation for property valuations.

The resulting classification of balances between Low, Medium and High is consequently driven by a combination of the probability of default and loss given default grades explained above. A matrix of fifteen PD and ten LGD grades determine the category within which each loan is categorised.

Fair value of collateral methodology:

For Residential and Commercial Mortgages agreements, the fair value of underlying collateral is calculated based on the indexed valuation of the property on which the mortgage is secured. Where the balance outstanding is greater than the indexed valuation, the fair value of the collateral is capped to the value of the outstanding balance.

For Asset Finance agreements, the estimated fair value of the collateral is calculated by applying LGDs on a case by case basis. The LGD against each loan is deducted from the balance outstanding to derive a proxy for fair value. As the fair value is derived using LGDs, the fair value calculated includes an element of prudence as the LGD is based on non-performing loan data. Only a small proportion of neither past due nor impaired assets will ultimately default.

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Notes to the financial statements continued

41. Risk management continued

b) Credit risk continued

Individually impaired balances are further analysed as follows:

2014	Residential Mortgages			SME Commercial Mortgages			Asset Finance	Invoice Finance
	Residential £'000	Buy-to-Let £'000	Total £'000	Commercial £'000	Buy-to-Let £'000	Total £'000	Total £'000	Total £'000
Impaired status:								
Past due 3 – 6 months	1,709	1,688	3,397	436	74	510	1,837	–
Past due 6 – 12 months	186	737	923	2,891	–	2,891	370	3,225
Past due over 12 months	1,407	276	1,683	2,543	348	2,891	407	2,707
	3,302	**2,701**	**6,003**	**5,870**	**422**	**6,292**	**2,614**	**5,932**
Of which: Possessions	1,376	–	1,376	–	–	–	1,363	–

2013	Residential Mortgages			SME Commercial Mortgages			Asset Finance	Invoice Finance
	Residential £'000	Buy-to-Let £'000	Total £'000	Commercial £'000	Buy-to-Let £'000	Total £'000	Total £'000	Total £'000
Impaired status:								
Past due 3 – 6 months	2,479	279	2,758	122	2,295	2,417	1,424	–
Past due 6 – 12 months	482	284	766	1,104	153	1,257	654	4,727
Past due over 12 months	–	110	110	3,382	2,923	6,305	1,160	3,187
	2,961	**673**	**3,634**	**4,608**	**5,371**	**9,979**	**3,238**	**7,914**
Of which: Possessions	–	–	–	2,176	–	2,176	280	–

Movement in impaired loans is analysed as follows:

2014	Residential Mortgages £'000	SME Commercial Mortgages £'000	Asset Finance £'000	Invoice Finance £'000
At 1 January	3,634	9,979	3,238	7,914
Classified as impaired during the year	4,090	1,828	3,517	4,171
Transferred from impaired to unimpaired	(1,147)	(581)	(630)	–
Amounts written off	(59)	(336)	(2,190)	(4,246)
Repayments	(515)	(4,598)	(1,321)	(1,907)
At 31 December	**6,003**	**6,292**	**2,614**	**5,932**

2013	Residential Mortgages £'000	SME Commercial Mortgages £'000	Asset Finance £'000	Invoice Finance £'000
At 1 January	1,398	9,184	3,992	3,591
Classified as impaired during the year	3,370	7,098	1,226	4,505
Transferred from impaired to unimpaired	(597)	(2,828)	(441)	–
Amounts written off	(94)	(925)	(767)	(65)
Repayments	(443)	(2,550)	(772)	(117)
At 31 December	**3,634**	**9,979**	**3,238**	**7,914**

Collateral held and other enhancements
The principal indicators used to assess the credit security of performing loans are loan-to-value ratios for commercial and retail mortgages. Loan-to-collateral value on indexed origination information on the Group's residential mortgage portfolio is set out below:

Residential Mortgages

	2014 £'000	2013 £'000
100%+	9,167	39,122
95 – 100%	82,454	26,378
90 – 95%	151,447	23,775
85 – 90%	82,427	20,103
80 – 85%	117,888	62,875
75 – 80%	219,839	225,890
70 – 75%	370,024	421,991
60 – 70%	770,682	486,067
50 – 60%	450,194	211,533
0 – 50%	310,777	161,952
	2,564,899	**1,679,686**
Capital repayment	898,008	425,316
Interest only	1,666,891	1,254,370
	2,564,899	**1,679,686**
Average Loan to Value percentage – all residential mortgages	66.84%	66.80%
Average Loan to Value percentage – buy-to-let residential mortgages	64.18%	68.19%

Residential Mortgages at a Loan to Value of 90% and above have increased as a result of the Group's participation in the Help to Buy Scheme.

SME Commercial Mortgages
Loan-to-collateral value on indexed origination information on the Group's commercial mortgage portfolio is set out below:

	2014 £'000	2013 £'000
100%+	–	–
95 – 100%	–	–
90 – 95%	–	–
85 – 90%	209	566
80 – 85%	2,113	812
75 – 80%	26,522	21,515
70 – 75%	73,065	42,474
60 – 70%	204,627	215,914
50 – 60%	252,420	264,764
0 – 50%	452,335	215,953
	1,011,291	**761,998**
Capital repayment	478,760	380,760
Interest only	532,531	381,238
	1,011,291	**761,998**
Average Loan to Value percentage – all commercial mortgages	52.23%	56.82%
Average Loan to Value percentage – buy-to-let	55.73%	60.72%

2013 comparatives have been re-presented with a revised split between the LTV bandings.

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Notes to the financial statements continued

41. Risk management continued

b) Credit risk continued

Invoice Finance
In respect of invoice finance, collateral is provided by the underlying receivables (e.g. trade invoices). As at 31 December 2014, the average advance rate against the fair value of sales ledger balances which have been assigned to the Group, net of amounts considered to be irrecoverable, is 68.04 per cent (31 December 2013: 69.34 per cent).

In addition to the value of the underlying sales ledger balances, the Group will, wherever possible, obtain additional security before offering invoice finance facilities to a client. These include limited personal guarantees from major shareholders, charges over personal and other business property, cross guarantees from associated companies and unlimited warranties in the case of frauds. These additional forms of security are impracticable to value given their nature.

Asset Finance
In respect of asset finance, collateral is provided by the Group's rights and/or title to the underlying leased assets, which the Group is able to repossess in the event of default. Where appropriate, the Group will also obtain additional security, such as parent company or personal guarantees. Asset finance also undertakes a small volume of unsecured lending where it has obtained an understanding of the ability of the borrower's business to generate cash flows to service and repay the facilities provided. As at 31 December 2014 the total amount of such unsecured lending was £17.4 million.

Concentration of credit risk
The Group monitors concentration of credit risk by product type, geographic location and sector. Analyses of concentrations are shown below. Details of the Group's lending by product type are as follows:

	2014 £'000	2013 £'000
Finance lease receivables	1,044,298	720,198
Invoice financing	180,576	211,962
SME Commercial Mortgage loans	1,011,291	761,998
Residential Mortgage loans	2,564,899	1,679,686
	4,801,064	**3,373,844**
Including:		
Value of buy-to-let residential mortgages	1,597,255	1,172,213
Value of buy-to-let commercial mortgages	401,090	411,262

Credit concentration of assets by size analysed as follows:

	2014			2013		
	Residential Mortgages £'000	**SME Commercial Mortgages £'000**	**Asset Finance £'000**	Residential Mortgages £'000	SME Commercial Mortgages £'000	Asset Finance £'000
£0 – £50k	32,485	7,117	460,409	24,011	5,857	291,794
£50 – £100k	548,053	64,933	224,912	390,316	46,889	155,957
£100 – £150k	608,382	69,861	108,361	404,716	52,634	72,116
£150 – £200k	424,686	71,650	59,135	271,954	48,419	44,609
£200 – £300k	479,799	114,550	73,556	283,193	83,997	55,074
£300 – £400k	233,269	80,233	36,274	135,404	56,632	32,528
£400 – £500k	93,509	62,991	21,644	66,570	45,989	18,112
£500k – £1m	132,502	190,714	39,988	98,180	156,023	37,122
£1m – £2m	12,214	181,727	12,208	5,342	157,566	10,459
£2m+	–	167,515	7,811	–	107,992	2,427
Total	**2,564,899**	**1,011,291**	**1,044,298**	**1,679,686**	**761,998**	**720,198**

An analysis of the Group's geographical concentration is shown in the table below:

	2014 %	2013 %
East Anglia	9.5	8.8
East Midlands	6.3	6.2
Greater London	20.9	19.2
North East	1.6	1.9
North West	11.9	13.2
Northern Ireland	0.1	0.1
Scotland	4.6	4.3
South East	19.5	18.7
South West	9.9	9.9
Wales	3.2	3.3
West Midlands	8.2	8.3
Yorkshire and Humberside	4.3	6.1
	100.0	**100.0**

An analysis of the Group's loans and advances to customers by sector is shown in the table below:

	2014 %	2013 %
Agriculture, hunting and forestry	1.3	0.9
Construction	3.2	3.2
Education	0.1	–
Electricity, gas and water supply	0.6	0.6
Financial intermediation	1.4	1.2
Health and social work	0.2	0.3
Hotels and restaurants	0.3	0.4
Manufacturing	4.8	5.9
Mining and quarrying	0.2	0.2
Private households with employed persons	0.8	1.0
Public administration and defence; compulsory social security	0.1	0.2
Real estate, renting and business activities	18.7	18.5
Residential	61.4	59.1
Transport, storage and communication	3.9	4.4
Wholesale and retail trade; repair of motor vehicles, motorcycles and personal household goods	3.0	4.1
	100.0	**100.0**

Forbearance

On occasion, borrowers experience financial difficulties which impact their ability to meet mortgage or SME finance obligations. Management seeks to identify borrowers who are experiencing financial difficulties as well as contacting borrowers whose loans have gone into arrears, consulting with them in order to ascertain the reason for the difficulties, and to establish the best course of action that can be taken to bring the account up to date. In certain circumstances where the borrower is experiencing significant financial distress, management may use forbearance measures to assist them. These are all considered on a case-by-case basis and must be in the best interest of the customer. The forbearance measures are undertaken in order to achieve the best outcome for both the customer and the Group by dealing with financial difficulties and arrears at an early stage.

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Notes to the financial statements continued

41. Risk management continued

b) Credit risk continued

The most widely used methods of forbearance are reduced monthly payments, loan term extension, deferral of payment and a temporary or permanent transfer to interest only payments to reduce the borrower's financial pressures. Where the arrangement is temporary, borrowers are expected to resume normal payments within six months. Temporary concessions are counted as forborne for three months following the end of the concession. Permanent concessions are counted as forborne for 24 months following the concession. As at 31 December 2014 and as at 31 December 2013, the Group had undertaken forbearance measures as follows in each of its lending divisions:

	2014 £'000	2013 £'000
Asset Finance		
Capitalisation	21	953
Reduced monthly payments	68	–
Loan-term extension	162	482
Deferred payment	1,152	1,601
Total Asset Finance	**1,403**	**3,036**
Total forborne as a percentage of the total divisional gross lending book (%)	0.13%	0.42%
SME Commercial Mortgages		
Temporary or permanent switch to interest only	3,741	7,152
Total SME Commercial Mortgages	**3,741**	**7,152**
Total forborne as a percentage of the total divisional gross lending book (%)	0.37%	0.93%
Residential Mortgages		
Temporary or permanent switch to interest only	1,661	1,842
Reduced monthly payments	1,076	–
Loan-term extension	11	11
Deferred payment	624	90
Total Residential Mortgages	**3,372**	**1,943**
Total forborne as a percentage of the total divisional gross lending book (%)	0.13%	0.12%
Total forborne		
Total capitalisation	21	953
Temporary or permanent switch to interest only	5,402	8,994
Total reduced monthly payments	1,144	-
Total loan-term extension	173	493
Total deferred payment	1,776	1,691
Total forborne	**8,516**	**12,131**
Total forborne as a percentage of the total gross lending book (%)	0.18%	0.36%

The Group's total loan balances in forbearance decreased by 30 per cent from £12.1 million as at 31 December 2013 to £8.5 million as at 31 December 2014.

Analysis of forborne accounts is shown in the tables below:

2014	**Residential Mortgages £'000**	**SME Commercial Mortgages £'000**	**Asset Finance £'000**	**Total £'000**
Neither past due nor impaired	1,438	2,259	1,152	4,849
Past due but not impaired	1,225	1,482	175	2,882
Impaired	709	–	76	785
	3,372	**3,741**	**1,403**	**8,516**

2013	Residential Mortgages £'000	SME Commercial Mortgages £'000	Asset Finance £'000	Total £'000
Neither past due nor impaired	1,481	7,152	2,076	10,709
Past due but not impaired	111	–	960	1,071
Impaired	351	–	–	351
	1,943	**7,152**	**3,036**	**12,131**

Credit risk – treasury

Credit risk exists with treasury assets where the Group has acquired securities or placed cash deposits with other financial institutions. The credit risk of treasury assets is considered to be relatively low. No assets are held for speculative purposes or actively traded. Certain liquid assets are held as part of the Group's liquidity buffer.

The table below sets out information about the credit quality of financial assets held by treasury:

	2014 £'000	2013 £'000
Cash and balances at central banks and Loans and advances to banks		
– Rated AAA	–	–
– Rated AA+ to AA-	79,555	192,844
– Rated A+ to A-	100,043	237,544
– Rated BBB+	17,370	–
	196,968	**430,388**
Debt securities: UK Government Gilts and Treasury Bills and Supranational Bonds		
– Rated AAA	334,927	144,794
– Rated AA+ to AA-	158,429	133,015
– Rated A+ to A-	–	–
– Rated BBB+	–	–
Debt securities: Asset backed securities		
– Rated AAA	16,328	68,837
– Rated AA+ to AA-	–	8,609
– Rated A+ to A-	–	398
– Rated BBB+	–	–
	509,684	**355,653**
Derivatives held for risk management purposes		
– Rated AAA	–	–
– Rated AA+ to AA-	689	651
– Rated A+ to A-	4,182	8,221
– Rated BBB+	3,297	–
	8,168	**8,872**
	714,820	**794,913**

As at 31 December 2014 and at 31 December 2013 none of the treasury assets were past due or impaired.

Notes to the financial statements continued

41. Risk management continued

b) Credit risk continued

Cash placements
Credit risk of Group and treasury counterparties is controlled through the counterparty placements policy which limits the maximum exposure by entity where the Group can place cash deposits. All institutions need a sufficiently high long term and short term rating at inception.

Gilts and Supranational Bonds
As part of the liquidity buffer, the Group holds a portfolio of Gilts and Supranational Bonds. These instruments are AAA or AA+ to AA- rated, and typically carry sovereign risk.

Asset backed securities
The Group has a portfolio of asset backed securities. The majority of these investments are in AAA or AA+ to AA- rated bonds secured on UK originated assets. All investments are in Sterling; no foreign currency bonds were bought. The portfolio has credit enhancement, providing principal protection against losses.

Derivatives
Credit risk on derivatives is controlled through a policy of only entering into contracts with a small number of UK credit institutions, with a credit rating of at least AA- at inception. Most derivative contracts are collateralised through the receipt/payment of daily cash margin calls to cover the mark to market asset/liability.

iv) Offsetting financial assets and liabilities
It is the Group's policy to enter into master netting and margining agreements with all derivative counterparties. In general, under master netting agreements the amounts owed by each counterparty that are due on a single day in respect of all transactions outstanding in the same currency under the agreement are aggregated into a single net amount being payable by one party to the other. In certain circumstances, for example when a credit event such as a default occurs, all outstanding transactions under the agreement are aggregated into a single net amount being payable by one party to the other. In certain circumstances, for example when a credit event such as a default occurs, all outstanding transactions under the agreement are terminated.

Under the margining agreements where the Group has a net asset position valued at current market values, in respect of its derivatives with a counterparty, then that counterparty will place collateral, usually cash, with the Group in order to cover the position. Similarly, the Group will place collateral, usually cash, with the counterparty where it has a net liability position.

As the Group's derivatives are under master netting and margining agreements as described above, they do not meet the criteria for offsetting in the statement of financial position.

The following tables detail amounts of financial assets and liabilities subject to offsetting, enforceable master netting agreements and similar arrangements including the Funding for Lending Scheme as detailed in Notes 20 and 28.

				Related amounts not offset in the statement of financial position		
2014 **Type of financial instrument**	**Gross amount of recognised financial instruments £'000**	**Gross amount of recognised financial instrument offset in the statement of financial position £'000**	**Net amount of financial instruments presented in the statement of financial position £'000**	**Financial instruments £'000**	**Cash collateral paid /(received) £'000**	**Net amount £'000**
Assets						
Loans and advances to customers (amounts pre-positioned as collateral under the FLS)	719,900	–	719,900	(304,207)	–	415,693
Derivatives held for risk management	8,168	–	8,168	(7,068)	(1,100)	–
	728,068	**–**	**728,068**	**(311,275)**	**(1,100)**	**415,693**
Liabilities						
Amount due to banks – repurchase agreements	(304,207)	–	(304,207)	304,207	–	–
Derivatives held for risk management	(54,198)	–	(54,198)	7,068	46,162	(968)
	(358,405)	**–**	**(358,405)**	**311,275**	**46,162**	**(968)**

2013 Type of financial instrument	Gross amount of recognised financial instruments £'000	Gross amount of recognised financial instrument offset in the statement of financial position £'000	Net amount of financial instruments presented in the statement of financial position £'000	Related amounts not offset in the statement of financial position Financial instruments £'000	Cash collateral paid /(received) £'000	Net amount £'000
Assets						
Loans and advances to customers (amounts pre-positioned as collateral under the FLS)	822,900	–	822,900	(383,071)	–	439,829
Derivatives held for risk management	8,872	–	8,872	(6,163)	(1,675)	1,034
	831,772	**–**	**831,772**	**(389,234)**	**(1,675)**	**440,863**
Liabilities						
Amounts due to banks – repurchase agreements	(383,071)	–	(383,071)	383,071	–	–
Derivatives held for risk management	(17,867)	–	(17,867)	6,163	11,350	(354)
	(400,938)	**–**	**(400,938)**	**389,234**	**11,350**	**(354)**

c) Liquidity risk

Liquidity risk is the risk that the Group is not able to meet its financial obligations as they fall due, or can do so only at excessive cost.

To protect the Group and its depositors against liquidity risks, the Group maintains a liquidity buffer which is based on the Group's liquidity needs under stressed conditions. The liquidity buffer is monitored on a weekly basis to ensure there are sufficient liquid assets at all times to cover cash flow movements and fluctuations in funding and to enable the Group to meet all financial obligations and to support anticipated asset growth.

Through the ILAA process, the Group has assessed the level of liquidity necessary to prudently cover systemic and idiosyncratic risks and the ILAA process determines the appropriate liquidity buffer, taking into account the specific nature of the deposit base.

The ILAA requires the Group to consider all material liquidity risks in detail and the ILAA has documented the Group's analysis of each key liquidity risk driver and set a liquidity risk appetite against each of these drivers. Liquidity risks are specifically considered by the ALCO each month.

Based on the business model of funding primarily via retail and SME deposits, the Board has set a liquidity risk appetite which it considers to be appropriate to provide it with the assurance that the relevant liquidity risk drivers should be considered and appropriately stressed and that the Group is able to meet liabilities beyond the targeted survival period.

The components of the Group's liquidity buffer were as follows:

	2014 £'000	2013 £'000
Bank of England reserve account and unencumbered cash and bank balances	104,216	390,369
UK Gilts and Treasury Bills and Supranational Bonds	486,225	275,817
Treasury Bills held under the FLS scheme	179,608	99,784
Covered Bonds	4,005	–
Total liquidity buffer	**774,054**	**765,970**
As a % of funding liabilities	14.87%	19.56%

Notes to the financial statements continued

41. Risk management continued

c) Liquidity risk continued

Encumbered assets
The Group holds encumbered assets in the form of a reserve bank account with the Bank of England (see Note 37), loans and advances to customers secured within the securitisation vehicle and prepositioned under the FLS scheme (see Note 20) and cash collateral received from derivative transactions. These balances have been disclosed in the relevant note disclosures. Further details of assets encumbered within the Group's securitisation vehicle are provided in Note 40.

An overview of the Group's key liquidity risk drivers is provided below:

Deposit funding risk
The deposit funding risk is the primary liquidity risk driver for the Group and this could occur if there was a concern by depositors over the current or future creditworthiness of the Group. Although the Group seeks to operate in such a way as to protect depositors, an extremely high proportion of deposits are also protected by the government's Financial Services Compensation Scheme ('FSCS'). The FSCS provides £85,000 of protection to depositors.

Wholesale funding
The Group mainly finances its operations through retail and SME deposit taking. It does not have long term wholesale funding lines in place with the exception of drawings under the Funding for Lending Scheme, repo facilities to help manage liquid assets, and debt securities issued by the Group securitisation vehicle in April 2014. The Group does have relationship banking facilities in place which are used to hedge against currency and interest rate exposures as well as repo facilities for short term liquidity management.

A summary of the Group's wholesale funding sources is shown below:

	Note	**2014 £'000**	2013 £'000
Repurchase agreements on drawings under FLS Scheme	28	304,207	383,071
Debt securities in issue	33	279,143	–
Deposits by banks	28	600	1,205
		583,950	**384,276**

Payments systems
The Group does not form part of the UK payment system. However, in the event there are problems with one of the payment systems, the Group has access to other facilities with which to make payments if needed.

Pipeline loan commitments
The Group needs to maintain liquidity to cover for the outstanding pipeline of loan offers. Although certain pipeline offers may not be legally binding, the failure to adhere to an expression of intent to finance a loan contract brings reputation risk, therefore liquidity is held for such pipeline offers.

Cash collateral requirements
The swap Credit Support Annex ('CSA') agreement requires the Group or a swap counterparty to hold cash in a deposit account, depending on whether the swap is in or out of the money. As the Group is unrated, the swap agreements are not credit rating sensitive in relation to the Group, which removes the impact from a downgrade risk.

Contingency funding plan
As a regulated firm, the Group is required to maintain a Contingency Funding Plan ('CFP'). The plan (which is now part of the Group's Recovery and Resolution Plan ('RRP')) involves a two stage process, covering preventative measures and corrective measures to be invoked when there is a potential or actual risk to the Group's liquidity or capital position. The CFP/RRP provides a plan for managing a liquidity or capital situation or crisis within the Group, caused by internal events, external events or a combination thereof. The plan outlines what actions the Group could take to ensure it complies with the liquidity adequacy rules, maintains sufficient capital and operates within its risk appetite and limits, as set and approved by the Board.

The following is an analysis of gross undiscounted contractual cash flows payable under financial liabilities:

Gross contractual cash flows

	Payable on demand £'000	Up to 3 months £'000	3 to 12 months £'000	1 to 5 years £'000	More than 5 years £'000	Total £'000
2014						
Non-derivative liabilities						
Amounts due to banks	1,142	234,785	69,910	–	–	305,837
Customers' accounts	1,190,398	809,826	1,434,729	1,090,600	–	4,525,553
Other liabilities	4,200	9,479	–	–	–	13,679
Debt securities in issue	–	14,770	40,651	240,033	–	295,454
Subordinated notes	–	–	5,150	47,725	–	52,875
Unrecognised loan commitments	404,593	–	–	–	–	404,593
	1,600,333	**1,068,860**	**1,550,440**	**1,378,358**	**–**	**5,597,991**
Derivative liabilities						
Derivatives held for risk management – settled net	542	1,200	10,597	25,029	18,022	55,390
Derivatives held for risk management settled gross:						
Amounts received	(2,349)	(4,544)	–	–	–	(6,893)
Amounts paid	2,349	4,545	–	–	–	6,894
	542	**1,201**	**10,597**	**25,029**	**18,022**	**55,391**
2013						
Non-derivative liabilities						
Amounts due to banks	1,685	174,938	109,934	99,806	–	386,363
Customers' accounts	944,724	668,323	1,138,897	775,581	–	3,527,525
Other liabilities	3,583	6,793	–	–	–	10,376
Subordinated notes	–	–	5,150	52,875	–	58,025
Unrecognised loan commitments	343,652	–	–	–	–	343,652
	1,293,644	**850,054**	**1,253,981**	**928,262**	**–**	**4,325,941**
Derivative liabilities						
Derivatives held for risk management – settled net	–	978	3,179	11,158	3,118	18,433
Derivatives held for risk management settled gross:						
Amounts received	(13,849)	–	–	–	–	(13,849)
Amounts paid	13,849	–	–	–	–	13,849
	–	**978**	**3,179**	**11,158**	**3,118**	**18,433**

d) Market and interest rate risk

The main market risk faced by the Group is interest rate risk which primarily arises from retail and commercial assets and liabilities, liquidity holdings, funding through FLS, debt securities issued by the Group securitisation vehicle and subordinated notes. Interest rate risk is the risk of loss through mismatched asset and liability positions sensitive to changes in interest rates. Oversight of interest rate risk is covered by ALCO on a monthly basis. Interest rate risk consists of asset-liability gap risk and basis risk.

Asset-liability gap risk

Where possible the Group seeks to match the interest rate structure of assets with liabilities, creating a natural hedge. Where this is not possible the Group will enter into interest rate swap transactions to convert the fixed rate exposures on loans and advances, customer deposits and available for sale securities into variable three month LIBOR liabilities.

Given timing differences and the price of hedging small gaps, it is not cost effective to have an absolute match of variable rate assets and liabilities. The risk exposure of the overall asset-liability interest rate profile is monitored against approved limits using two main measures:

- Changes to economic value of the balance sheet as a result of 2 per cent shift in the interest yield curve; and
- Simulated Value at Risk ('VaR').

Financial statements

Notes to the financial statements continued

41. Risk management continued

d) Market and interest rate risk continued

For each period the risk measures reported were as follows (note: potential losses are shown as negative numbers):

	2014 £'000	2013 £'000
2% shift up of the yield curve:		
As at period ended	(323)	(1,459)
Average of month end positions reported to ALCO	(2,274)	(1,463)
2% shift down of the yield curve:		
As at period ended	(1,086)	3,206
Average of month end positions reported to ALCO	2,490	1,722
Simulated VaR:		
As at period ended	(3,687)	1,106
Average of month end positions reported to ALCO	(1,966)	1,652

Simulated VaR measures the monthly maximum potential gain or loss in the net fair value of interest bearing assets and liabilities due to market volatility within a statistical confidence level of 99 per cent. The VaR methodology employed is a Monte Carlo simulation based on 30 day average movements in LIBOR. The VaR methodology has inherent limitations in that market volatility in the past may not be a reliable predictor of the future, and may not reflect the time required to hedge or dispose of the position, hence VaR is not used as the sole measure of risk. The risk measures above are based on the Group's interest bearing assets and liabilities, including the Contingent convertible securities.

Basis risk
Basis risk is where there is a mismatch in the interest rate reference base for assets and liabilities. When the Group enters into derivative contracts to swap fixed rate assets and liabilities into variable rate liabilities, the reference base is usually three month LIBOR. Certain lending products have interest rates which are based on the prevailing Bank of England Base Rate ('BBR') and this different basis reference leads to basis risk.

The Group has a basis risk policy in place which places limits on the net mismatch between base rate linked assets and liabilities; and seeks to manage the overall level of basis risk exposure by entering into basis swap agreements. As at 31 December 2014 the amount of the basis risk sensitivity measure, as described above, was £480,000 (31 December 2013: £260,000).

Other market risks
The Group does not carry out proprietary trading or hold any positions in assets or equity which are actively traded.

The Group does, however, hold a portfolio of asset backed securities and a portfolio of liquid assets (primary Gilts, Treasury Bills and Supranational Bonds) which are used for liquidity buffer purposes. The interest rate risk on these liquid assets is considered as part of the asset – liability gap risk described above. The instruments are also exposed to other forms of market risk e.g. credit spread risk. Prices are monitored on a day-to-day basis to ensure that the Group is aware of any material diminution in value. Formal monthly prices are subject to independent review and are reported to ALCO. The Group has repo facilities in place which will be used in the first instance to obtain liquidity when necessary, which will avoid the need to sell the liquidity buffer assets and so crystallise any price gain or loss due to market price movements.

Hedge accounting
As detailed above, the Group only uses derivative contracts in order to hedge existing exposures on loans and advances to customers, customer deposits and available for sale securities, principally with regard to following the Group's policies in respect of the management of asset-liability gap and basis rate risks. Wherever possible the Group seeks to include the derivatives used within hedges which meet the qualification requirements of IAS 39 to be accounted for as fair value portfolio hedges (see accounting policy (j) and Note 22). There are however times where, in order to meet IAS 39 requirements for prospective testing of hedge effectiveness for new derivatives to be included in hedging portfolios, there is a time lag before IAS 39 hedge accounting may commence.

Similarly, there are also certain derivative contracts, e.g. those hedging basis risk exposures (see above) which do not meet the criteria for hedge accounting under IAS 39. The gains and losses arising on contracts which do not meet the IAS 39 hedge accounting criteria are included within 'Net (expense)/income from derivatives and other financial instruments at fair value through profit or loss', but as they are not matched by similar adjustments to the economically hedged hedged assets and liabilities they give rise to volatility in the income statement which will reverse over the life of the instrument.

There is also a portfolio of fixed rate UK Gilts and Supranational Bonds where the pre-existing hedges using interest rate swaps did not meet the requirements for hedge accounting on transition to IFRSs and as a consequence the Group used the option available within IFRS to designate the bonds at fair value through profit and loss in order to reduce the accounting mismatch with the derivatives used to hedge the bonds. Changes in the fair value of the bonds and the hedging derivatives, and any differences between them, which are largely attributable to changes in the fair value of the bonds due to changes in their credit risk, are both reflected within the income statement as part of 'Net (expense)/income from derivatives and other financial instruments at fair value through profit or loss'.

42. Capital management

The European Union Capital Requirements Directive came into effect on 1 January 2007. This introduced consistent capital adequacy standards and an associated supervisory framework in the EU based on the Basel II Accord. This was replaced by Capital Requirements Regulation ('CRR') and Capital Requirements Directive (together referred to as CRD IV) which came into force on 1 January 2014 and is enforced in the UK, together with local implementing rules and guidance, by the Prudential Regulation Authority ('PRA').

The Group operated under CRD III framework for periods up to 31 December 2013 and under the CRD IV framework from 1 January 2014.

As part of the Internal Capital Adequacy Assessment Process ('ICAAP') applicable to CRD IV firms, the Board is required to consider all material risks which the Group faces and determine whether additional capital is required in order to provide additional protection to depositors and borrowers and to ensure the Group is sufficiently well capitalised to withstand a severe economic downturn.

The Board manages its internal capital levels for both current and future activities and documents its risk appetite and capital requirements during stress scenarios as part of the ICAAP.

The ICAAP represents the aggregated view on risk for the Group and is used by the Board, management and shareholders to understand the levels of capital required to be held over the near and medium term and to assess the resilience of the Group against failure. The Group submitted its last ICAAP to the PRA in February 2014 and is currently in the process of revising the current year ICAAP. It was subject to a Supervisory Review Evaluation Process ('SREP') by the PRA.

The Group is required to maintain a certain level of capital to meet several requirements:

- to meet minimum regulatory capital requirements;
- to ensure the Group can meet its objectives, including growth objectives;
- to ensure the Group can withstand future uncertainty, such as a severe economic downturn; and
- to provide assurance to depositors, customers, shareholders and other third parties.

The Group presents regular reports on the current and forecasted level of capital, as well as the results of stress scenarios, to the ALCO, Board and to the Risk Committee.

The key assumptions and risk drivers used to create the ICAAP are regularly monitored and reported and any material deviation from the forecast and risk profile of the Group would mean the ICAAP would need to be reviewed.

The Group complied with all externally imposed capital requirements throughout the years ended 31 December 2014 and 2013, when its reporting to regulators was based on its books and records maintained under UK GAAP.

As at 31 December 2014, the Group's capital base was made up of £354.9 million of Tier 1 capital and £45.3 million of Tier 2 capital. Tier 1 capital consisted of fully issued ordinary shares, satisfying all the criteria for a Tier 1 instrument as outlined in the CRR, audited/verified reserves, and qualifying Additional Tier 1 capital issued by the Group in December 2014. Tier 2 capital relates to issued subordinated loan notes and collective impairment allowances.

Financial statements

Notes to the financial statements continued

42. Capital management continued

The Group's regulatory capital position as at the period end was as follows:

	2014 £'000	2013 £'000
Tier 1		
Share capital	23,737	23,737
Share premium account	–	237,305
Capital contribution reserve	2	2
Warrant reserve	2,200	2,200
Retained earnings	277,879	1,531
Less: Intangible assets	(22,571)	(22,657)
Total common equity Tier 1 capital (CET1)	**281,247**	**242,118**
Additional Tier 1 (AT1)		
Additional Tier 1 – contingent convertible securities	73,657	–
Total Tier 1 capital	**354,904**	**242,118**
Tier 2		
Subordinated notes	36,758	35,571
Collective impairment allowance	8,527	6,314
Total Tier 2 capital	**45,285**	**41,885**
Total regulatory capital	**400,189**	**284,003**

Both years above are presented on an IFRS basis. The 2013 comparatives were previously reported to the Prudential Regulation Authority ('PRA') and its predecessor, the Financial Services Authority, based on the Group's UK GAAP accounts. Regulatory capital has increased during 2014 as a result of the issuance of Additional Tier 1 capital in December 2014 and the inclusion of the profit for the year in retained earnings.

The Group has elected to use the standardised approach for credit risk. Under CRD III and CRD IV, the Group must set aside capital equal to 8 per cent of its total risk weighted assets to cover its 'Pillar 1' capital requirements. The Group must also set aside additional 'Pillar 2' capital to provide for additional risks. This is calculated by multiplying the Pillar 1 capital by the Individual Capital Guidance ('ICG') ratio.

The ICG ratio is based on the various risks which the Group faces and is agreed by the PRA. The Group's capital base was in excess of the minimum required under the ICG.

Further details of the Group's management of capital are provided in the Pillar III disclosures which are available on the Group's investor relations website: www.investors.aldermore.co.uk.

Reconciliation of equity per statement of financial position to capital resources

	2014 £'000	2013 £'000
Equity per statement of financial position	378,850	265,357
Regulatory adjustments:		
Add: subordinated notes	36,758	35,571
Add: collective impairment allowance	8,527	6,314
Less: available for sale reserve	(1,375)	(582)
Less: intangible assets	(22,571)	(22,657)
Total regulatory capital	**400,189**	**284,003**

With effect from 1 January 2015, the available for sale reserve will be included in the Group's Common Equity Tier 1 capital.

43. Controlling party information

Aldermore Group PLC (the Parent Company) is controlled by AnaCap Financial Partners II, L.P. (52.3 per cent. of voting rights) and AnaCap Financial Partners, L.P. (47.7 per cent. of voting rights).

44. Post balance sheet events

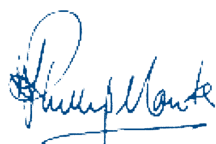
There have been no material post balance sheet events.

The Company statement of financial position

As at 31 December 2014

	Note	As at 31 December 2014 £'000	As at 31 December 2013 £'000	As at 1 January 2013 £'000
Assets				
Loans and advances to banks	3	1,368	2,330	102
Investment in Group undertakings	4	333,975	259,116	197,394
Other assets	6	265	115	2
Total assets		**335,608**	**261,561**	**197,498**
Liabilities				
Accruals and deferred income	7	843	744	–
Total liabilities		**843**	**744**	**–**
Share capital	8	23,737	23,737	19,918
Share premium account	8	–	237,305	177,960
Contingent convertible securities	9	73,657	–	–
Other reserves		914	305	141
Warrant reserve		2,200	2,200	2,200
Retained earnings		234,257	(2,730)	(2,721)
Equity		**334,765**	**260,817**	**197,498**
Total liabilities and equity		**335,608**	**261,561**	**197,498**

These financial statements were approved by the Board and were signed on its behalf by:



Phillip Monks
Director

16 February 2015

Registered number: 06764335
The notes and information on pages 124 to 126 form part of these financial statements.

Financial statements

The Company statement of cash flows

For the year ended 31 December 2014

	Note	As at 31 December 2014 £'000	As at 31 December 2013 £'000	As at 1 January 2013 £'000
Cash flows from operating activities				
(Loss) before taxation	2	(318)	(9)	–
(Increase)/decrease in operating assets	6	(150)	(113)	586
Increase/(decrease) in operating liabilities	7	99	744	(608)
Net cash flows (used in)/generated from operating activities		**(369)**	**622**	**(22)**
Cash flows from investing activities				
Investment in Group undertakings	4	(74,250)	(61,558)	(689)
Net cash used in investing activities		**(74,250)**	**(61,558)**	**(689)**
Cash flows from financing activities				
Proceeds from issue of shares	8	–	63,164	182
Net cash flows from contingent convertible securities	9	73,657	–	–
Net cash from financing activities		**73,657**	**63,164**	**182**
Net increase/(decrease) in cash and cash equivalents		**(962)**	**2,228**	**(529)**
Cash and cash equivalents at start of the year	3	2,330	102	631
Movement during the year		(962)	2,228	(529)
Cash and cash equivalents at end of the year	3	**1,368**	**2,330**	**102**

The Company statement of changes in equity

For the year ended 31 December 2014

	Share capital £'000	Share premium account £'000	Contingent convertible securities £'000	Share based payment reserve £'000	Capital contribution reserve £'000	Warrant reserve £'000	Retained earnings £'000	Total £'000
Year ended 31 December 2014								
As at 1 January	23,737	237,305	–	303	2	2,200	(2,730)	260,817
Loss for the year	–	–	–	–	–	–	(318)	(318)
Transactions with equity holders:								
– Reduction in share premium	–	(237,305)	–	–	–	–	237,305	–
– Issue of contingent convertible securities	–	–	75,111	–	–	–	–	75,111
– Issue costs	–	–	(1,454)	–	–	–	–	(1,454)
– Share based payments	–	–	–	609	–	–	–	609
As at 31 December	**23,737**	**–**	**73,657**	**912**	**2**	**2,200**	**234,257**	**334,765**
Year ended 31 December 2013								
As at 1 January	19,918	177,960	–	139	2	2,200	(2,721)	197,498
Total comprehensive income	–	–	–	–	–	–	(9)	(9)
Transactions with equity holders:								
– Shares issued during the year	3,819	–	–	–	–	–	–	3,819
– Premium on share issued during the year	–	60,319	–	–	–	–	–	60,319
– Issue costs	–	(974)	–	–	–	–	–	(974)
– Share based payments	–	–	–	164	–	–	–	164
As at 31 December	**23,737**	**237,305**	**–**	**303**	**2**	**2,200**	**(2,730)**	**260,817**

In 2014 and in previous years, certain Directors have been given the option to purchase 'B' ordinary shares of £0.10 at a discount to market value. This gives rise to a reserve of £912,000 (2013: £303,000; 2012: £139,000) which is distributable.

Notes to the Company financial statements

1 Basis of preparation

a) Accounting basis

These standalone financial statements for Aldermore Group PLC ('the Company') are the first to be prepared in accordance with International Financial Reporting Standards as adopted by the European Union ('IFRSs'). The Company prepared its financial statements under United Kingdom Generally Accepted Accounting Practice ('UK GAAP') until 31 December 2013. The date of transition to IFRS is 1 January 2013. No amendments to accounting and valuation methods were required to transition from UK GAAP to IFRS. When preparing these financial statements, management made a number of presentational changes to comply with IFRSs. The significant accounting policies adopted are set out in Note 2 to the consolidated financial statements.

b) Going concern

The Directors consider that it is appropriate to continue to adopt the going concern basis in preparing the financial statements.

c) Income statement

Under Section 408 of the Companies Act 2006 the Company is exempt from the requirement to present its own income statement.

2. Net loss attributable to equity shareholders of the Company

On including the standalone Company financial statements here together with the Group consolidated financial statements, the Company is taking advantage of the exemption in Section 408 of the Companies Act 2006 not to present its individual income statement and related notes that form a part of these financial statements.

	Year ended 31 December 2014 £'000	Year ended 31 December 2013 £'000	As at 1 January 2013 £'000
Net loss attributable to equity shareholders of the Company	**(318)**	**(9)**	**–**

3. Loans and advances to banks

	Year ended 31 December 2014 £'000	Year ended 31 December 2013 £'000	As at 1 January 2013 £'000
Repayable on demand	**1,368**	**2,330**	**102**

There were no collective or individual provisions for impairment against loans and advances to banks.
All amounts are considered to be cash and cash equivalents.

4. Investment in group undertakings

	Year ended 31 December 2014 £'000	Year ended 31 December 2013 £'000	As at 1 January 2013 £'000
As at 1 January	259,116	197,394	194,366
Capital injections – share capital	–	61,558	700
Equity warrants issued	–	–	2,200
Capital contributions – share based payments	609	164	139
Capital raising costs	–	–	(11)
Additional Tier 1 perpetual loan	74,250	–	–
As at 31 December	**333,975**	**259,116**	**197,394**

As at 31 December 2014, £nil worth of investments (31 December 2013: £nil; 1 January 2013: £nil) were classed as impaired.

Investment in subsidiaries

The Company owns 100 per cent of the issued share capital of Aldermore Bank PLC, which is a registered bank. Details of subsidiary undertakings of the Bank are provided in Note 23 to the consolidated financial statements.

During the year ended 31 December 2012 a non-returnable capital contribution of £2,200,000 was paid on the issue of share warrants. In addition, certain Directors were given the option to purchase 'B' ordinary shares of £0.10, at a discount to market value. This gave rise to a movement of £139,000.

All the companies listed in Note 23 to the consolidated financial statements are related parties to the Company. See Note 5 for the related party disclosures.

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Additional Tier 1 Perpetual Loan

On 9 December 2014, the Company issued £75 million Fixed Rate Reset Additional Tier 1 Perpetual Subordinated Contingent Convertible Securities (the 'Securities') as described in Note 36 to the consolidated financial statements.

Also on 9 December 2014, the Company entered into an agreement with Aldermore Bank PLC (the 'Bank') for an Additional Tier 1 Perpetual Loan. The Company agreed a loan to the Bank of £75 million less the sum of £750,000 in respect of certain costs borne by the Company in connection with its issue of the Securities.

The loan is perpetual and has an indefinite duration, is repayable at the option of the Bank, and bears interest at an initial rate of 11.875 per cent p.a. until 30 April 2020 and thereafter at the relevant Reset Interest Rate as provided in the loan agreement. Interest is payable on the loan annually in arrears on each interest payment date commencing 30 April 2015 and is non-cumulative. The Borrower has the full discretion to cancel any interest scheduled to be paid on the loan.

The loan balance is written down to zero and all accrued but unpaid interest and any other amounts payable on the loan are cancelled in the event of either the Bank's or the Group's Common Equity Tier 1 ratios falling below 7 per cent or if the Securities are converted or written down at the request of the Supervisory Authority.

Given its nature the loan has been classified as an investment in a subsidiary undertaking and is carried at cost in accordance with IAS 27. Interest on the loan is recognised on payment as that is the point at which the unconditional receipt by the Company is established.

5. Related party transactions

The aggregate value of loans and balances relating to Directors of the Company were as follows:

	Year ended 31 December 2014 £'000	Year ended 31 December 2013 £'000	As at 1 January 2013 £'000
Transaction value for the year ended	33	2	n/a
Maximum balance during the period ended	162	115	n/a
Balance outstanding as at year ended	162	115	113

Interest rates charged on loan balances outstanding from related parties are lower than the rates that would be charged in arm's length transactions. During the year ended 31 December 2014, interest was charged on these loans at a rate of 0.8 per cent above one month LIBOR. These loan balances are not secured.

In addition to the above transactions, the Company entered in to an Additional Tier 1 perpetual loan with Aldermore Bank PLC as described in Note 4.

6. Other assets

	Year ended 31 December 2014 £'000	Year ended 31 December 2013 £'000	As at 1 January 2013 £'000
Amounts recoverable within 1 year:	65	–	2
Amounts recoverable after 1 year:	200	115	–
Total other assets	**265**	**115**	**2**

Other assets includes £200,000 (31 December 2013: £115,000; 1 January 2013: £ nil) of loans to Group employees.

During the year ended 31 December 2014, Group employees received loans totalling £33,000 (year ended 31 December 2013: £nil). Interest was charged on these loans at an annual rate of 0.8 per cent above 1 month LIBOR. The loans are made for the purpose of enabling the employees to satisfy their personal liabilities in respect of shares issued, and are repayable in 2018.

7. Accruals and deferred income

	Year ended 31 December 2014 £'000	Year ended 31 December 2013 £'000	As at 1 January 2013 £'000
Amounts payable within 12 months:			
Accruals	843	744	–
	843	**744**	**–**

Notes to the Company financial statements continued

8. Share capital

Details of share capital of the Company are provided in Note 35 to the consolidated financial statements.

9. Contingent convertible securities

Details of the contingent convertible securities issued by the Company are provided in Note 36 to the consolidated financial statements.

10. Risk management

Through its Risk Management Framework, the Group is responsible for determining its principal risks, and the level of acceptable risks, as stipulated in the Group's risk appetite statement, thus ensuring that there is an adequate system of risk management so that the levels of capital and liquidity held are consistent with the risk profile of the business.

The risk management disclosures of the Group on pages 97 to 119 apply to the Company where relevant and therefore no additional disclosures are included in this note.

11. Fair values of financial assets and liabilities

The Directors consider that the fair value of its financial assets and liabilities are approximately equal to their carrying value. Accordingly no further disclosures in respect of fair values are provided.

12. Controlling party information

Aldermore Group PLC is controlled by AnaCap Financial Partners, II L.P. (52.3 per cent. of voting rights) and AnaCap Financial Partners, L.P. (47.7 per cent of voting rights).

13. Post balance sheet events

There are no material post balance sheet events.

14. IFRS reconciliations

The Company previously prepared its primary financial statements under UK GAAP, which differs in certain significant respects from IFRSs. There were no amendments to accounting and valuation methods required to transition from UK GAAP to IFRS. When preparing these financial statements, management made a number of presentational changes to comply with IFRSs.

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