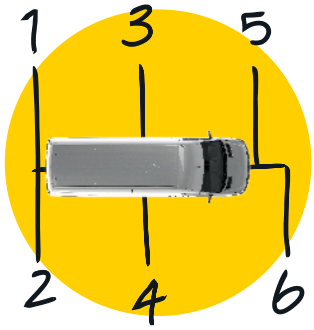
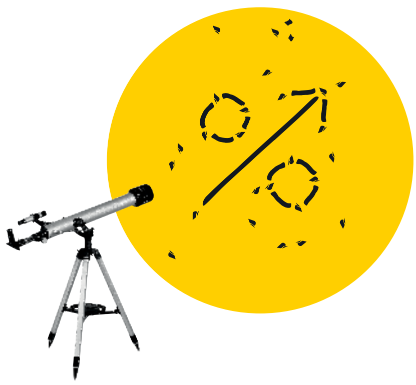
Aldermore Group PLC

Annual Report and Accounts 2016





Aldermore

Introduction

Aldermore provides specialist banking and underwriting expertise to help customers seek and seize opportunities in their professional and personal lives.

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@AldermoreBank AldermoreBank company/aldermore-bank-plc AldermoreBank

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

"Welcome to our 2016 Annual Report to Shareholders. It has been another year of remarkable achievement for Aldermore..."

Phillip Monks OBE, Chief Executive Officer

Strategic report

Making giant leaps in the banking industry

Aldermore has come a long way since launching in 2009, with a vision to provide banking as it should be. We've had some great success, but the journey has only just begun...

2009

Aldermore launches, aiming to deliver "Banking as it should be" for UK businesses and savers

2010

Aldermore establishes a residential mortgage business, providing a refreshing alternative to traditional high-street banks

2012

Aldermore now home to over £2bn of personal savings

Lending to Small and Medium Enterprises (SMEs) reaches £1bn

Aldermore extends offering by launching a business savings franchise

Aldermore makes a profit for the first time, just 3 years after launching

2013

Aldermore becomes the first UK bank to allow customers to rate and review products online

Unedited feedback continues to be published on our website today

2015

Aldermore lists on the London Stock Exchange and enters the FTSE 250 leading share index, as we exceed £6bn of lending to UK homeowners, landlords and businesses

2016

2016 was another remarkable year for Aldermore. Despite the economic uncertainty in the UK we continued to deliver value to each of our stakeholders. With a growing customer base that rate us highly, record financial performance, an employee summit and more value given back to our local communities, we are proud of our achievements and confident of much more to come.

We have also redesigned our brand purpose – to help people seek and seize opportunities – launching a new visual identity, which has been designed to capture the bold and enterprising spirit of our customers.

£7.5bn
loans to customers

£6.7bn
customer deposits

18.0%
underlying return on equity

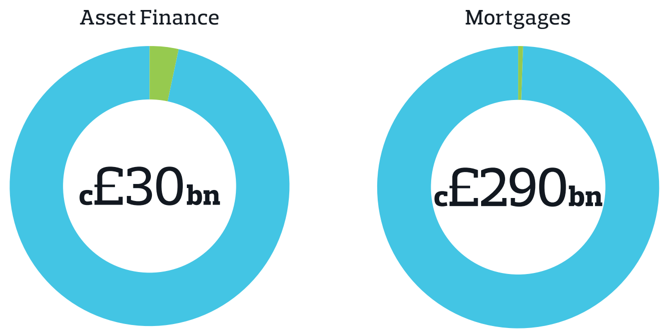
11.5%
common equity tier 1 ratio

Strategic report

Business overview

We operate as a specialist player in large markets...

Market size[1] £bn **and estimated market share** %

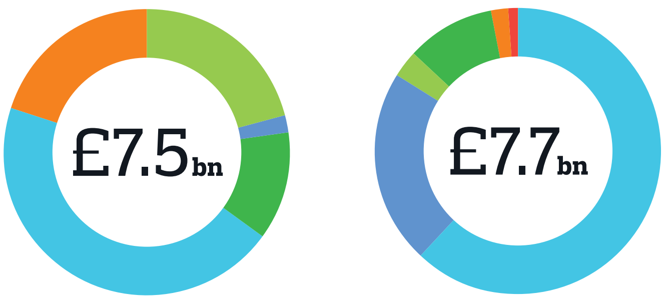


...we are diversified across both lending and funding portfolios...

	%
Asset Finance	21
Invoice Finance	2
SME Commercial Mortgages	12
Buy-to-Let	45
Residential Mortgages	20

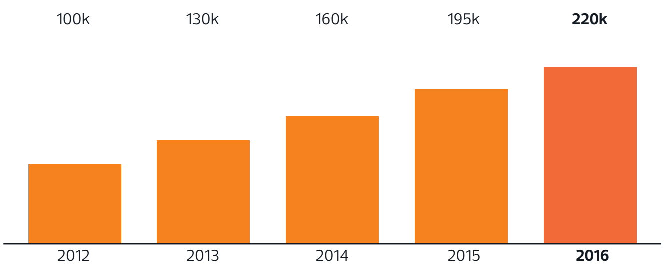
	%
Retail deposits	62
SME deposits	22
Corporate deposits	3
Government schemes	10
RMBS	2
Other wholesale	1

Lending portfolio £bn **Funding base** £bn



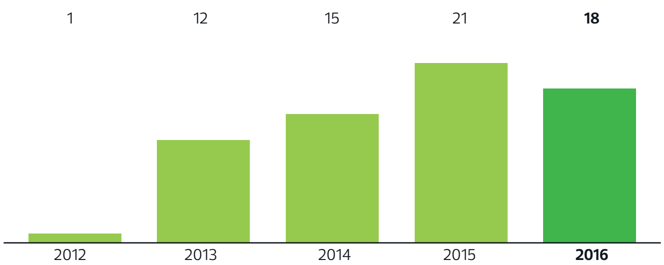
...we operate well-secured lending and savings portfolios across a broad customer base...

Customer numbers



...and generate strong risk-adjusted returns for shareholders.

Underlying[2] **return on equity** %



Strategic report

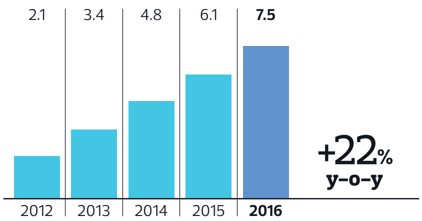
Financial highlights

> "2016 was another year of considerable financial progress for Aldermore, including record profits and an underlying[2] return on equity of 18%."

James Mack,
Chief Financial Officer

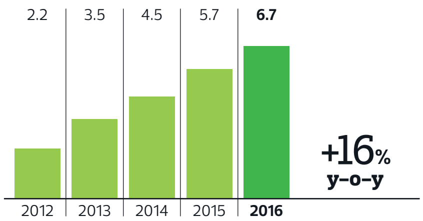
Read more about the financial performance on pages 16–30.

Net loans £bn



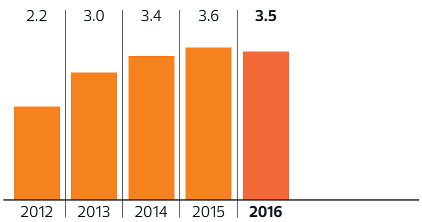
How much our customers have borrowed from us...

Customer deposits £bn



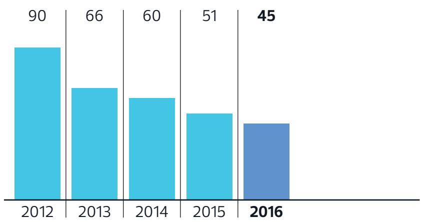
...How much our savers have deposited with us

Net interest margin %



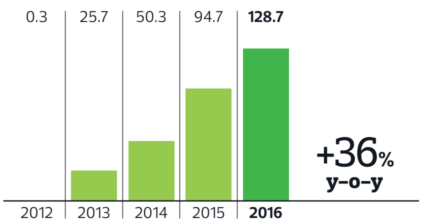
The rate of income we earn from lending less the rate we pay on savings

Underlying[2] cost/income ratio %



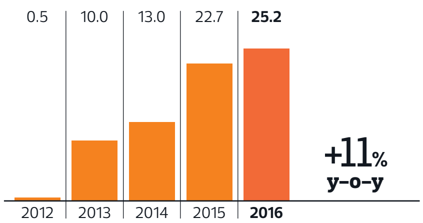
45p of operating costs are incurred to generate each £1 of income

Reported profit before tax £m



The overall profit we generated as a business, before paying tax

Reported earnings per share p



Profits after tax and AT1 payment attributable to each share in the business

1 Source: Council of Mortgage Lenders, De Montfort University, FLA, Aldermore estimates.

2 Underlying: Excluding goodwill impairment of £4.1m (pre and post tax) in 2016. Excluding IPO related costs in 2015 of £4.1m pre-tax and £3.4m post tax.

Strategic report

Chairman's statement

"As your Interim Chairman, I am honoured to be presenting our 2016 Annual Report, which highlights another year of excellent progress against our strategic objectives."

Danuta Gray,
Interim Chairman

Another year of substantial progress

During the year the Group has continued executing on its strategy to deliver 'banking as it should be' to more customers and generating strong, sustainable returns for shareholders.

Earnings per share have increased by 11% to 25.2p, generating an underlying return on average equity of 18%. These are excellent results in competitive markets and a testament to the dedication of colleagues across the Group.

Resilience in an uncertain operating environment

As well as being a year of considerable progress for Aldermore, 2016 has been a year of change and uncertainty for the banking industry as a whole, with evolving regulation, political developments and their corresponding impacts on the global economy.

In particular, the UK's referendum on EU membership and vote to leave introduced considerable volatility to financial markets, which impacted the share price of many companies, including Aldermore and other specialist lenders, as shown in the chart opposite. Following the vote, Aldermore's business model has remained resilient, demonstrated by our financial results and partly reflected in the share price performance during the second half of the year. There remains much uncertainty regarding the precise nature and timing of Britain's exit from the EU. However, the Board remains confident that the business can continue to respond to the opportunities and threats this presents and continue to successfully deliver against our strategic objectives.

Commitment to strong Governance

The Board's responsibility to provide strong and effective governance remains paramount. Throughout 2016 we were fully compliant with the Corporate Governance Code 2014 and having overseen the Board effectiveness review in my capacity as Senior Independent Director, I have every confidence in the continued strength and cumulative experience of the Board.

I would like to take this opportunity to welcome Chris Patrick to the Board and to thank Peter Cartwright and Neil Cochrane for their services as Non-Executive Directors. Both Peter and Neil made valuable contributions to the Aldermore Board, as representatives of our Principal Shareholders, AnaCap Financial Partners LLP.

On behalf of the Board I would also like to extend particular gratitude to Glyn Jones, who has served as Chairman of the Aldermore Board since March 2014. Glyn played an instrumental role in Aldermore's significant growth and transition to a listed company and leaves behind a strong, experienced and dedicated Board.

We are progressing in our search for a successor for Glyn and are confident we will secure a strong replacement to oversee Aldermore's continuing progress.

Our communities

We remain committed to investing in our communities, whether that is within Aldermore through development of the team; our local communities through volunteering and fundraising; or the broader UK economy through lending to businesses, homeowners and landlords. We are also committed to strong corporate citizenship.

We support the drive to create greater accountability and transparency throughout the banking sector and have worked to ensure compliance with the FCAs Senior Management Regime from March 2016, as well as joining the Banking Standards Board in the year. We are also proud signatories of the Women in Finance Charter and are committed to both developing greater female representation in senior positions across the Group and promoting the advantages of diversity more broadly across the business. More on our role in our communities can be found in our Corporate Responsibility Section on pages 36–38.

Outlook

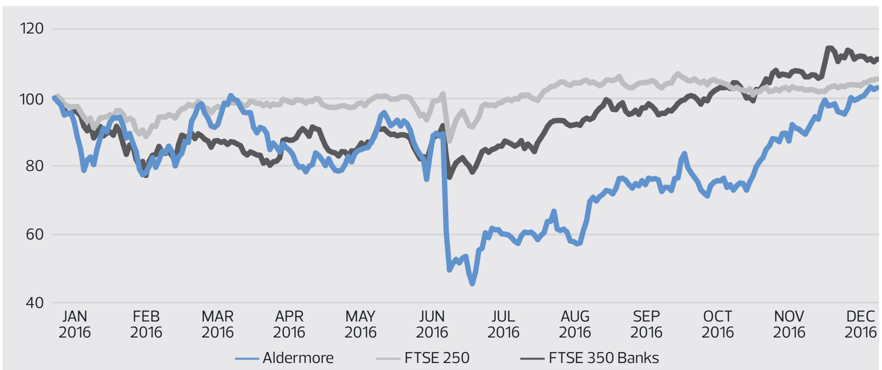
The Board is committed to supporting the substantial progress Aldermore is making in operational development and financial performance, as well as managing the challenges that this presents.

The EU referendum introduced greater uncertainty. However, the UK economy has remained resilient to date.

Your Board remains confident that Aldermore can continue to grow within existing risk appetite generating strong, sustainable returns for shareholders.

Danuta Gray,
Interim Chairman

Aldermore, FTSE 250 and FTSE 350 12 month, indexed share price performance



Share price performance from 04/1/2016 to 30/12/2016, indexed to 100.

Strategic report

Market overview

Macro-economy

Aldermore is focused solely in the UK, so what happens in the economy here matters to us. For example, the pricing of loans and savings products are often impacted by the base rate set by the Bank of England and confidence in economic growth can impact on a demand for homes or funding for business investment.

This year

2016 was an eventful year for the macro-economy, with the UK's decision to leave the EU being a significant source of volatility. This caused many economists to initially downgrade their expectations of UK GDP growth before subsequently revising them upwards as the economy proved resilient to the political uncertainty. The Bank of England also reacted to the risk to the economy from the referendum by lowering the base rate to 0.25% and extending their quantitative easing programme with the introduction of the Term Funding Scheme (TFS).

Key impact

The lowering of the Bank of England base rate was largely neutral to Aldermore as we passed on the impact through both sides of our balance sheet, while the likelihood of any material changes to Bank of England rates in the near future remains small. The TFS has provided a benefit, as we can use it to fund new lending growth into the UK economy at a lower interest expense.

Despite the volatility in financial markets, customer outlook remains broadly positive with Aldermore's SME Future Attitudes report indicating that four out of five SMEs are confident about their business performance in 2017.

Legal and regulation

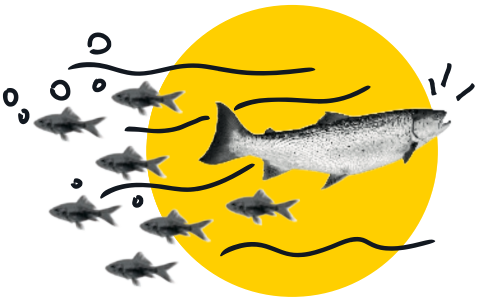
Given its importance to the economy, banking is a highly regulated market and can be affected by changes in legislation. In the UK, the PRA, and the FCA are the primary bodies which regulate the banking industry, ensuring effective prudential management and fair conduct, respectively. Together these bodies ensure that local and European law are effectively applied to the UK banking industry.

This year

A number of new laws and items of regulation, which directly impacted the banking market, were introduced or announced during 2016. The main themes of changes impacting Aldermore concerned the buy-to- let (BTL) property market, taxation and capital requirements. In the BTL market, new laws introduced by the Government included a higher rate of stamp duty payable from April 2016 and a reduction in mortgage interest tax deductibility for landlords phasing in from April 2017. The PRA announced changes to affordability testing effective from January 2017 and revised underwriting requirements for landlords with four or more properties effective from September 2017. 2016 also saw the introduction of the 8% banking tax surcharge announced in 2015 and further consultation on capital requirements and risk-weightings by the Basel Committee on Banking Standards.

Key impact

Aldermore has a comprehensive BTL offering, serving many types of customer from individual property owners through to incorporated professional landlords. Demand has remained strong throughout 2016, as reflected in the record levels of origination. In 2017, the forthcoming regulatory changes may result in a shift towards more professional investors, favouring specialist lenders, such as Aldermore. Developments in capital requirements are yet to be finalised, however Aldermore is taking steps to mitigate impacts, discussed further in our Emerging Risk Section on pages 34–35.



Competition

Since the global financial crisis in 2009 – when Aldermore was founded – ensuring healthy competition and fair customer outcomes in the UK banking market has been in sharp focus for both the regulator and the Competition and Markets Authority. In the aftermath of the crisis many banks stopped serving groups of customers, particularly certain small and medium sized businesses and first-time homebuyers, which provided an opportunity for Aldermore to grow through serving these unmet needs.

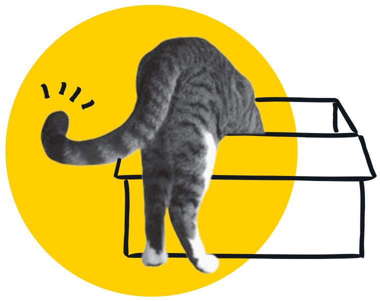
This year

Aldermore's primary markets are mortgages and business finance. Although these are competitive markets, Aldermore is recognised by brokers and customers for its 'can do' approach and occupies leading positions in several of its chosen business areas. Within the asset finance market, we continue to see consolidation in the broker channel and expect competition to increase as new lenders attempt to build a presence.

The residential mortgages market remains highly competitive and concentrated amongst the large high street banks. In this market, Aldermore serves credit-worthy niches, including the self employed and first-time buyers, where it has taken particular advantage of Government schemes. In BTL Aldermore has continued to benefit from market growth and is well positioned to benefit from the increased professionalisation of the market.

Key impact

Throughout 2016 Aldermore has continued to grow and maintain attractive margins in each of our key markets, as demonstrated by record levels of origination and robust net interest margins. We are confident that we can continue to meet the challenge presented by competitors and continue to deliver profitable and sustainable growth within our prudent risk appetite.



Customer behaviour

The traditional banking model of large branch networks and standardised single-channel service is outdated. Customers and intermediaries are increasingly demanding online or digital servicing as well as greater flexibility in savings and borrowing products. The response has been the emergence and growth of new entrants like Aldermore.

This year

Aldermore has established a track record of agility in deploying resources to serve unmet customer demand through specialist underwriting. In particular during 2016, Aldermore was able to respond with agility to a surge in BTL mortgage demand early in the year, ahead of changes to Stamp-Duty Land Tax, and again in the fourth quarter. Additionally, we have developed our brand and since the year end, launched our new visual identity which has been designed to capture the bold and enterprising spirit of our customers as we help them to seek and seize opportunities.

Key impact

By deploying specialist underwriting expertise Aldermore is able to serve the needs of customers, such as complex portfolio landlords that other traditional volume-focused banks can't. This deep expertise and operational agility has enabled us to continue growing and helping more customers to seek and seize opportunities in their professional and personal lives. We continue to invest in improving our digital propositions and servicing to customers and brokers as is reflected in the high levels of customer advocacy we received in 2016.

Strategic report

Our business model

Our foundations inform our business model

We are a specialist lender and underwriter focused in select markets

Our DNA; to be reliable, expert, dynamic and straightforward informs everything that we do

We are modern, scalable and completely focused in the UK

We differentiate across the value chain

Strong and effective Governance provides oversight and direction

Read more about our governance on page 39

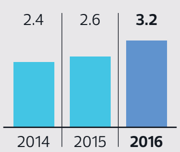
Our expertise in risk management helps secure the sustainability of our business

Read more about our risks on page 32

1

Exceptional service in distribution
We go above and beyond to add value to our broker relationships, which represent c80% of our distribution, whether through speed of service or our training academies. We also have simple direct propositions to support customers

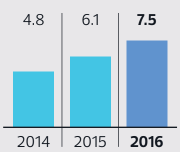
Origination £bn



2

Technology enabled specialist underwriting
Our human underwriters understand that not all customers look the same and use their experience to make safe underwriting decisions rather than adopting a "computer says yes or no" attitude

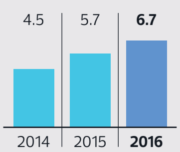
Net lending £bn



3

Award winning savings franchise
Our savings franchise is cutting-edge. Giving retail and business customers the flexibility to choose their own deposit terms and the security of knowing they will always get a competitive return without having to shop around

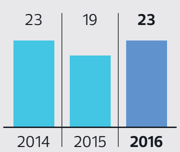
Deposits £bn



4

Excellence in credit risk and portfolio management
We are experts in understanding the risks associated with lending. We have a prudent risk appetite and have built a highly diversified business across our chosen markets and within portfolios, ensuring low levels of impairment

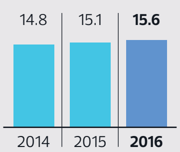
Cost of risk[1] bps



5

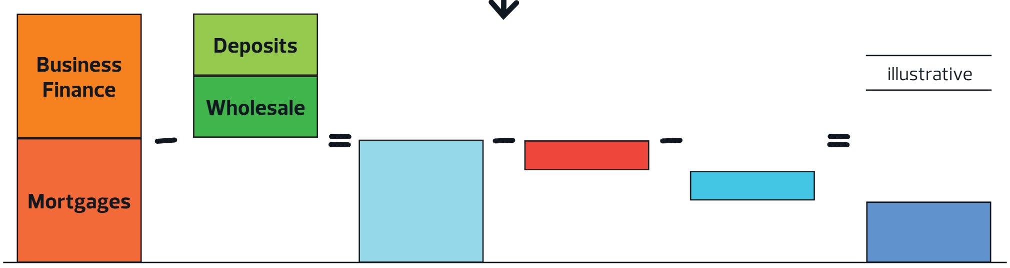
Prudent capital and liquidity management
Having built the Bank in the aftermath of the financial crisis, we understand the importance of maintaining a robust capital position and maintaining sufficient cash reserves at all times

Total capital ratio %



And generate superior returns

Financial statements start on page 140



We make loans to customers that generate interest and fee income

We pay interest on customer deposits and other sources of funding

Our income is the balance of these two

If a customer were unable to make their loan repayments, we would incur an impairment

Operating expenses are incurred in running the bank

What remains is profit – after we pay our taxes

[1] see page 15 for a definition of cost of risk

"Aldermore provides specialist banking and underwriting expertise to help customers seek and seize opportunities in their professional and personal lives.

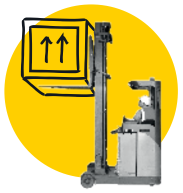
We operate in carefully selected areas of the business finance and mortgage markets, chosen for their size, attractive returns and strong collateral* characteristics.

Our DNA is built around our customers and helping them to seize opportunities. Whether serving one of our broker partners or a customer that comes to us directly, we use modern systems to support our specialist underwriting experts in making quick and informed lending decisions be it for a first home, a company car, an office, or a portfolio of rental properties.

We take our commitment to underwriting expertise and great customer service to generate strong, sustainable returns for our shareholders. To us, this is simply banking as it should be."

* Collateral is what we call the 'asset' we lend against, for example a home is used as collateral for a mortgage.

Read more about our business model in action...



Read more about Asset Finance on page 20

Read more about Residential Mortgages on page 28

Read more about Savings on page 30

Strategic report

Chief Executive Officer's review

"2016 was another great year for Aldermore, with more customers than ever choosing us to serve their needs and profitability at record highs. As we move forward on our journey, I am confident that we can continue to build on this momentum, helping more customers to seize opportunities."

Phillip Monks OBE,
Chief Executive Officer

Banking as it should be

The key drivers of our performance in 2016 are rooted in our purpose. Since the Bank was founded in 2009, we have sought to challenge the status quo and empower more people across Britain to seek and seize opportunities in their professional and personal lives by providing 'banking as it should be'. In doing so, we are addressing a market opportunity that is as real today as it was in the aftermath of the global financial crisis. In fact, as the market has matured, companies and individuals have increasingly recognised that a different kind of banking experience is both possible and available.

As a specialist bank, we don't compete head on with the traditional banks in their main markets. We go beyond their one-size fits all approach by employing specialist underwriters to understand each individual, and by making sure we offer a service that works for them. We operate in carefully selected segments where we have the necessary experience and expertise to deliver strong and sustainable risk-adjusted returns through responsible lending. We benefit from a modern infrastructure and an efficient distribution model, using an approved network of specialist intermediaries and, increasingly, direct relationships with customers online or by telephone, without the need for a costly branch network.

A record year

It is with great pride that we are reporting another record year for Aldermore, demonstrating continued progress on the journey we described at IPO. I am particularly pleased that we were able to deliver such a strong performance despite the uncertainty presented by the UK's referendum on EU membership. While the full political and economic implications of this decision are as yet unknown, the UK economy has remained resilient to date, and we continue to closely monitor our operating environment for any change.

Throughout the year, the Group has performed well and customer confidence remained high. We ended the year with strong growth, a robust credit performance and a healthy pipeline, giving us confidence that we are well positioned for further success.

Continuing commitment to UK businesses, homeowners, landlords and savers

Net loans to customers increased by £1.3bn, or 22% to £7.5bn at the end of 2016, driven by record levels of organic origination. This record performance was seen across both Business Finance and Mortgages, where, respectively, £1bn and £2bn of new customer loans were provided.

In Business Finance, we focus in both the asset finance and invoice finance markets. In Asset Finance we have leveraged our efficient broker-led distribution model to build a market leading position in this channel. Our specialist underwriting advantage in transport, plant and machinery, and other areas of expertise, enabled us to grow net lending by 7% to £1.6bn during 2016.

Across our Mortgages franchise we grew lending by 24% to £5.7bn. This was led by our broad customer offering in Buy-to-Let (BTL) which enabled us to grow BTL lending by 38% to £3.3bn. In SME Commercial Mortgages, where we have particular expertise in underwriting multi-let investment properties, lending grew by 12% to £930m. In our Residential Mortgages business we are committed to truly understanding our customers' circumstances which, with our focus on creditworthy segments of the market, enabled us to grow lending by 7% to £1.5bn.

Loan growth continues to be primarily funded by our award-winning deposit franchise. The performance of our savings business is driven by our straightforward and transparent proposition and our promise, that savers get "great returns effortlessly". Our dynamic online franchise enables customers to tailor products to their needs and our transparent approach means we don't use teaser rates. This approach drove an increase in deposits of 16% to £6.7bn in 2016. Business customers provide both c30% of this balance and a high level of advocacy, with 97% of customers surveyed saying they would recommend Aldermore to others.

Profit before tax up by over a third

Reported profit before tax rose 36% to a record high of £129m, driven by continued benefits from our growing franchises, a healthy net interest margin of 3.5% and further improvement in operational leverage with the cost to income ratio falling to below 45%. Our management of risk remains robust as demonstrated in a cost of risk of just 0.23%, and less than 0.5% of our loans by value being classed as non-performing.

Enhanced balance sheet strength and strong shareholder returns

2016 was also an important year in further strengthening our balance sheet. While our fully loaded CRD IV CET1 ratio reduced by 0.3% to 11.5% over 2016, we reached the point of capital self-sufficiency in the second half of the year when our ratio rose by 0.5%. This increase was driven by record levels of profitability and was in line with our guidance at IPO. We expect our CET1 capital ratio to continue rising in the coming years, as we deliver strong, sustainable earnings.

Overall, the Group generated underlying earnings per share of 26.4p and an underlying return on equity of 18%, or 20% prior to the impact of the 8% bank tax surcharge introduced in 2016.

Strengthening the team

The excellent progress seen in 2016 is the result of the experience and effort that everyone at Aldermore puts into supporting customers on a daily basis and for this I extend gratitude to all my colleagues across the Group.

During the year I was delighted to welcome three new members to the Executive team. Christine Palmer joined us as Chief Risk Officer, Dana Cuffe joined as Chief Operating Officer and Rob Divall joined as the Group HR Director. All of my new Executive colleagues have tremendous experience in their fields and it is a real testament to the business and the progress we have made that we can continue to attract such high calibre executives, who share our vision and can help successfully drive us forward. I also express my gratitude to our outgoing Executive team members Steve Barry, Vicki Harris, Ali Humphries and Paul Myers for all that they contributed during their time with Aldermore.

Strategic priorities

As we seek to further enhance the sustainability of returns, our strategic priorities will continue to be delivering further growth, increasing efficiency and maintaining our robust approach to risk management.

Read on for more on our strategic priorities and progress in 2016.

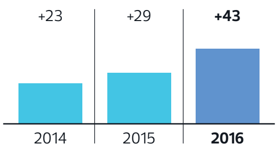
Strategic report – Chief Executive Officer's review

Our strategy – supporting strong and sustainable returns

Strategic objective	Our progress in 2016
Customer-driven: Helping more customers to seek and seize opportunities We will continue helping more customers across Britain to seek and seize opportunities, whether that's growing their business, buying their first home or securing a fair return on their savings. Our focus remains on serving diverse pools of customer demand and adjacent markets, where we can operate as an agile, service-focused specialist player in large markets, providing us with multiple levers for growth.	· 2016 was a record year for originations with over £3bn lent across Business Finance and Mortgages. Total customer numbers also reached an all-time high at over 220k, while our customer advocacy continued to improve as NPS grew from +29 to +43 · We received further recognition for our service, products and expertise in 2016, winning awards across all of our franchises, including 'Leasing and Asset Finance Provider of the Year' (NACFB), 'Best Specialist Mortgage Lender' (Your Mortgage) and 'Best Business Savings Provider' (Moneynet) · Our market-leading breadth of offering in Buy-to-Let helped us support more landlords than ever, as we grew customer numbers by 25% to c20k, originating over £1.2bn of loans, despite the increased market complexity · We continued to serve specialist segments of the residential mortgage market and invested in enhancing our propositions, including those for the self-employed and first time buyers · We also invested in developing our retention strategy in Mortgages, providing greater choice and support for customers looking for their next product
Simply delivered: Developing our scalable, effective and efficient operating model Aldermore benefits from modern, scalable systems and an efficient online broker-led distribution model, as opposed to a costly branch network. We continue to invest in key capabilities and technology, optimising our operating model to support the delivery of growth with enhanced levels of service, capability and efficiency.	· We generated greater operational leverage in the business, bringing the underlying cost to income ratio below 45% · As well as introducing new Executives we also bolstered the wider teams during 2016, strengthening expertise across the Group including, a new Head of Enterprise Risk, Chief Information Officer and Chief Data Officer · We progressed a number of improvement initiatives over the year, including enhanced digital capability, process simplification, platform upgrades and a refresh of our brand and customer segmentation
Securely managed: Maintaining a diverse and low-risk business model As specialist underwriters, our ability to understand our customers' circumstances and the value of underlying assets is a source of competitive advantage. Growth is supported and controlled by a consistent risk appetite and robust risk management framework, which drives our prudent approach across all areas of the Group.	· Our credit quality remained well within our appetite as we incurred a cost of risk of 23bps and maintained non-performing loans below 0.5% of our portfolio · We continue to originate in line with centrally controlled underwriting standards, including stress testing affordability, before going on to re-score the portfolio on a monthly basis · We made a number of enhancements to our credit risk models through our on-going work to become IFRS9 compliant ahead of the January 2018 implementation date

Key performance indicators

Customer NPS

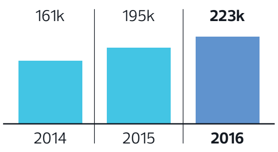


Definition
A net measure of customer advocates and detractors.

Performance
Aldermore continues to improve the NPS score enhancing the approach in 2016. 2014 is bank-wide.

Read more on page 36

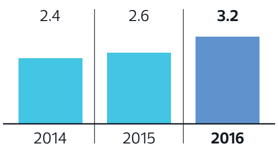
Number of customers



Definition
The number of customers selecting Aldermore for their savings or borrowing needs.

Performance
Customer numbers continue to grow, as we help more people to seek and seize opportunities.

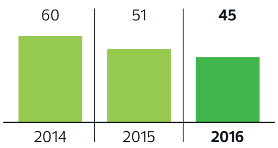
Loan origination £bn



Definition
The value of new loans we have made to customers.

Performance
Loan growth continues across both Business Finance and Mortgages, driven by organic origination.

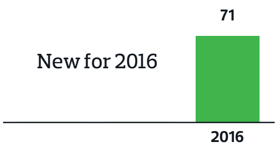
Underlying cost/income ratio %



Definition
A measure of efficiency calculated as underlying[1] expenses as a proportion of net income.

Performance
The cost income ratio continues to decline as we achieve greater operating leverage.

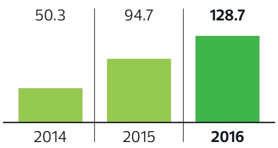
Employee engagement %



Definition
A measure of staff satisfaction and engagement with their role, leadership and business strategy.

Performance
Introduced in 2016 through our Big Conversation read more on page 37.

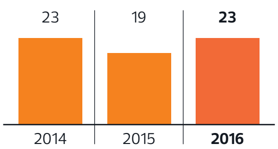
Reported profit before tax £m



Definition
Profit before tax (PBT) gives an overall measure of the performance of the business model.

Performance
PBT has increased markedly and is a record for Aldermore.

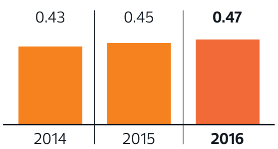
Cost of risk bps



Definition
Impairment losses as a percentage of average net loans over the period. An indicator of credit risk performance.

Performance
Impairments remained low during 2016 reflecting robust credit management and benign credit conditions.

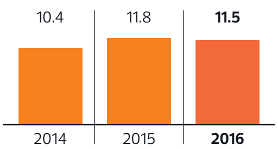
Non-performing loans %



Definition
Non-performing loans (NPL) is defined as individually impaired loans over total gross loans.

Performance
NPL remained low reflecting the positive environment for our customers and robust approach to risk management.

CET 1 ratio %



Definition
The CET1 ratio represents the core equity in the business as a proportion of risk-weighted assets and is a measure of capital strength.

Performance
CET1 remains robust, with growth in the second half of 2016.

[1] Underlying expenses includes; administrative expense, including levies but excluding one-off IPO costs and goodwill impairment expense.

Outlook for 2017 and beyond

As we deliver on the first priority of our strategy, we expect to grow our loan book by between 10% and 15% in 2017 with further growth thereafter and the portfolio mix remaining broadly stable. The exact pace of growth will be dependent on our ability to grow within our prudent risk appetite, while delivering strong and sustainable returns.

We will also continue to invest in efficiency, and enhanced operating leverage in order to deliver on our second strategic priority. This, combined with our planned growth, is consistent with the cost to income ratio declining below 40% over the medium term.

In line with our third strategic priority, we will retain a prudent approach to risk across the bank over 2017 and beyond to support the sustainability of earnings

We are delighted with the Group's performance in 2016 and remain positive on our outlook notwithstanding the economic uncertainty and potential changes to regulatory capital requirements. The Board will therefore continue to consider the payment of dividends while taking into account the growth opportunities available, anticipated changes in capital requirements, and once the Group's CET 1 ratio is above 12%.

In conclusion...

I'm delighted that our record performance in 2016 continues to demonstrate delivery against our business plan and targets and I would like to thank our customers, colleagues and shareholders for their continued support.

We have clear strategic priorities to further create and unlock value across the business, as we continue to serve and delight our customers and generate strong and sustainable returns for our shareholders.

The strategic report on pages 2 to 38 was approved by the Board and signed on its behalf by:

Phillip Monks OBE,
Chief Executive Officer

Strategic report

Chief Financial Officer's review

"I am pleased to be reporting on another strong set of financial results. I am confident that we can continue to grow and continue delivering strong, sustainable returns for shareholders."

James Mack,
Chief Financial Officer

Balance sheet – key items	2016 £m	2015 £m	% change
Net loans	7,477.3	6,144.8	22
Cash and investments	848.1	805.6	5
Other assets	55.8	58.1	(4)
Total assets	**8,381.2**	**7,008.5**	**20**
Customer deposits	6,673.7	5,742.0	16
Wholesale funding	982.2	635.8	54
Other liabilities	99.3	97.1	2
Total liabilities	**7,755.2**	**6,474.9**	**20**
Ordinary shareholders' equity	552.0	459.6	20
AT1 capital	74.0	74.0	0
Equity	**626.0**	**533.6**	**17**
Total liabilities and equity	**8,381.2**	**7,008.5**	**20**

Key metrics			
Net loan growth (£m)	1,333	1,344	0
Loan to deposit ratio (%)	112%	107%	5
Liquid assets / deposits (%)	13%	14%	(1)
Fully loaded CRD IV CET1 capital ratio (%)	11.5%	11.8%	(0.3)

Loans to customers up 22% with originations at record levels

2016 loan growth was driven by record levels of origination across both our Business Finance and Mortgages divisions at over £1bn and £2bn respectively, as we continue to build our diversified portfolio. This record level of originations was partly offset by £1.8bn of redemptions in the year. This level of redemptions represents almost a third of the loan portfolio at the start of the year, and an 83% increase on redemptions in 2015, reflecting the growing maturity of the business.

Net loans to customers reached £7.5bn (31 December 2015: £6.1bn), as the number of customers grew by 17% to over 80,000 with more UK businesses, homeowners and landlords choosing Aldermore to serve their borrowing needs.

Business Finance up 15% to £1.7bn

Asset Finance grew by 17% to £1,573m as our expertise in a broad range of asset classes allowed us to maintain our market leading position in the broker-channel and grow our wholesale proposition by 60%.

Invoice Finance continued to focus on returns, moving toward larger invoice discounting for small businesses and structured finance, and away from lower value factoring business. This was reflected in a 4% decline in loans to £154m, whilst segmental profits increased by over 50%.

Mortgages up 24% to £5.7bn

SME Commercial Mortgages saw a growing proportion of customers engaging with us directly, reflecting our reputation for expertise and service. This contributed to loan growth of 12% to £930m, despite tightening our appetite for development-based lending following the EU referendum.

In Buy-to-Let, our broad customer offering enabled us to grow lending by 38% to £3,326m. This strong growth also reflects our operational agility, as we took advantage of the market spikes in the first quarter, ahead of the introduction of an increase in stamp duty, and in the fourth quarter when we successfully took share in an active market.

In Residential Mortgages, our approach to understanding each of our customers' circumstances enabled us to grow lending by 7% to £1,494m. This growth was driven by £466m of originations which, more than offset a high level of redemptions on Help to Buy mortgages written two years ago when Aldermore was the first to market with the product.

Deposit-led funding model, with balances rising 16%

Our funding strategy remains deposit-led whilst, we actively manage wholesale sources, such as Government and central bank schemes, to provide diversification and drive an efficient cost of funds. As at 31 December 2016, our loan to deposit ratio was in line with management expectations at 112% (31 December 2015: 107%).

Our dynamic and innovative online savings franchise, which provides award-winning savings products to c140,000 customers grew by 16% to £6.7bn (31 December 2015: £5.7bn) benefitting from strong rates of retention at c70%. SME deposits of £1.6bn (31 December 2015: £1.4bn) and our Corporate deposits of £260m (31 December 2015: £156m) now represent almost a third of all deposits.

Wholesale funding increased by 54% to £982m (31 December 2015: £636m) and predominantly consists of on-balance sheet funding via repurchase agreements of Funding for Lending Scheme (FLS) Treasury Bills, drawings through the Term Funding Scheme (TFS) and our Residential Mortgage Backed Securitisation (RMBS).

As at the end of 2016, under the Bank of England's SME lending extension of FLS, the Group had on-balance sheet funding of £355m. We were also the first bank to utilise the Bank of England's newly launched TFS, with £396m of funding having been accessed by the end of 2016.

The outstanding balance on our RMBS as at 31 December 2016 stood at £131m (31 December 2015: £194m). This reduction reflects the capital repayments on the underlying mortgages.

Other wholesale funding predominantly consists of Tier 2 debt capital of £100m (31 December 2015: £38m). In October 2016, £60m subordinated loan notes were successfully issued adding to our existing Tier 2 Notes which were issued in 2012 and have an option to call in May 2017.

Profits up demonstrating continued strong returns

Profit before tax for the year increased by 36% to £128.7m (2015: £94.7m) as we maintain healthy margins across a larger loan book. Excluding £4.1m for both the goodwill impairment in 2016 and the 2015 pre-tax IPO related costs, the underlying profit before tax increased by 34% to £132.8m (2015: £98.8m).

The tax charge for the year increased by 115% to £35.2m (2015: £16.4m). This increase reflects the Group's increased profitability as well as the introduction of the 8% bank corporation tax surcharge on taxable profits above £25m from 1 January 2016. The effective tax rate of 27% in 2016 (2015: 17%) comprises the standard 20% corporate tax rate plus the 8% surcharge. Statutory profit after tax therefore increased by 19% to £93.5m (2015: £78.3m).

The return on equity generated in the period was 17.2%, or 18.0% on an underlying basis, and was in line with our commitment to delivering returns in the high teens. The 2016 basic earnings per share was 25.2p, on both a basic and fully diluted basis.

Income statement – key items	**2016 £m**	2015 £m	% change
Net interest income	**239.4**	**198.9**	**20**
Other income	28.1	25.8	9
Operating income	267.5	224.7	19
Underlying expenses	(119.2)	(115.5)	(3)
Impairments	(15.5)	(10.4)	(49)
Underlying profit before tax	132.8	98.8	34
IPO costs	0.0	(4.1)	–
Goodwill impairment	(4.1)	0.0	–
Statutory profit before tax	**128.7**	**94.7**	**36**
Tax	(35.2)	(16.4)	(115)
Profit after tax	**93.5**	**78.3**	**19**

Strategic report

Chief Financial Officer's review continued

Operating income increases 19%

During 2016 interest income grew by 19% to £358.2m driven by continuing net loan growth. The Group's average gross yield fell slightly to 5.3% (2015: 5.5%), primarily as a result of the lower rate environment and competition in Asset Finance and a change in mix with the comparatively lower yielding BTL portfolio growing at a faster pace than other portfolios.

Interest expense increased by 17% to £118.8m as we funded our lending growth. We also continued to benefit from diversified funding and access to lower cost Government schemes, reducing our average cost of funds to 1.7% (2015: 1.9%).

As a result, the Group's net interest income increased by 20% to £239.4m (2015: £198.9m) while, as expected, the net interest margin remained broadly stable at 3.5% (2015: 3.6%). Net fee and other operating income rose by 12% reflecting a higher volume of property valuations as a result of new mortgage lending.

Growth in operating expenses controlled to a 3% rise

Operating expenses were well controlled, increasing by 3% to £123.3m (2015: £119.6m), in line with management expectations. Within this, administrative expenses rose by 5% to £113.1m (2015: £107.9m), primarily reflecting the recruitment of colleagues to further support growth and enhance risk management.

Provisions of £0.8m in 2016 were 65% lower than in 2015, due to the payment of the capital element of the Financial Services Compensation Scheme (FSCS) levy having now been completed by the banking industry. Depreciation and amortisation was consistent with last year at £5.3m (2015: £5.3m).

Given their material and one-off nature, costs related to our IPO in 2015 and the impairment of goodwill related to our Invoice Finance business in 2016 are removed from our financial metrics to provide an 'underlying' view of our performance. This resulted in our cost to income ratio on an underlying basis declining by six percentage points to 45% (2015: 51%).

Capital position	2016 £m	2015 £m	% change
Common equity Tier capital	525.8	435.6	21
Additional Tier 1 capital	74.0	74.0	0
Tier 2 capital	113.1	48.6	133
Total capital	712.9	558.2	28
Risk Weighted Assets (RWAs)	**4,576.1**	**3,693.0**	**24**

Fully loaded CRD IV capital ratios (%)			
CET1 ratio (%)	11.5%	11.8%	(0.3)%
Total capital ratio (%)	15.6%	15.1%	0.5%
Leverage ratio (%)	7.0%	7.2%	(0.2)%

Loan impairments rise while cost of risk remains low at 23bps

We maintain a robust approach to risk management and this, combined with a relatively benign credit environment, has resulted in our cost of risk remaining low and below expectations at 0.23%. Impairments increased by 49% to £15.5m (2015: £10.4m), within which our collective charge grew by 31% to £4.7m (2015: £3.6m) reflecting the growth of the loan book and a further degree of caution, reflecting increased economic uncertainty following the UK's vote to leave the EU. Individual impairments of £10.8m were 58% higher than 2015 due to 2016 having seen impairments taken in relation to a relatively small number of exposures, while these had been abnormally low in 2015.

A robust capital position

The Group maintains a strong capital position and after becoming capital generative in the second half of 2016 closed the year with a fully loaded CRD IV total capital ratio of 15.6% (31 December 2015: 15.1%) and a CET1 ratio of 11.5% (31 December 2015: 11.8%). These movements reflect the profit after tax of £93.5m offset by growth in Risk Weighted Assets (RWAs) of £883m and the post-tax AT1 coupon of £6.6m, payable annually in April. The total capital ratio also benefits from the issuance of £60m Tier 2 Notes in October 2016.

RWAs increased by 24% reflecting loan growth of 22% and the increase in the Basic Indicator Approach (BIA) Operational Risk charge which is updated in the first quarter each year based on the average of the last three years' net operating income. The Group's leverage ratio at 7.0% (31 December 2015: 7.2%) remains significantly above forthcoming regulatory minimums.

As of 1 January 2017, Aldermore's total CET1 requirements under normal operating conditions, which include PRA ICG and Pillar 2B requirements as well as the phased in CRD IV buffers are higher than the 7% AT1 conversion level.

We are on track with enhancements to our credit risk models through our work to become IFRS9 compliant for January 2018 when the new accounting standard is introduced. This takes us closer to the sophistication required for an Internal Ratings-Based approach (IRB) to capital which may help to mitigate the risk of future changes in capital requirements. We will continue to monitor the cost and benefits associated to moving to IRB, as the regulatory changes and timeframes for implementation become clear.

Capital resilient under stress

We periodically test the Group's resilience to severe but plausible adverse scenarios. This process supports calibration of our stress loss buffer, ensuring we are able to withstand an economic downturn over our five year planning horizon. The outcome of this process is a key input into other Group processes, including the setting of our risk appetite, the assessment of our capital adequacy, and our assessment of risk-adjusted returns.

In 2016 , this process included the supervisory H2 2016 Annual Cyclical Scenario in addition to Aldermore's internal scenario. This scenario includes; a rapid fall in property prices, with residential property values declining by 32% and commercial by 42%; an economic downturn with a cumulative 4.3% reduction in GDP; unemployment rising to almost 10%; the BoE base rate falling to 0%; and inflation running at 3.4%.

Under this severe scenario, higher impairments including the effect of changes to IFRS9, operational risk losses and other detrimental factors would reduce our projected CET1. However, at its lowest point post Management actions, the CET1 ratio is expected to be around 8.5%, remaining above the 7% level at which our AT1 security converts to equity and significantly above our current CET1 PRA requirement and CRDIV buffers at 1 January 2017.

Outlook

The process of Britain's exit from the EU may result in economic growth deviating from current forecasts, but for 2017 there is unlikely to be any material impact. Our economic base-case upon which we set our outlook for the coming years includes the expectation that;

- house prices will continue to rise gradually,
- unemployment remains below 6%,
- the Bank of England base rate remains below 1%, and
- UK GDP growth increases to around 2%.

Returns will continue to be delivered through a combination of focused loan growth, margin stability, and robust control of expenses and impairments. Specifically we expect;

- 10 – 15% net loan growth in 2017, with a broadly stable net interest margin, around 3.5% .
- In 2017, we expect an incremental increase in costs of between £15m and £20m driven by ongoing investment, which includes mandatory projects and strengthening of our teams.
- Despite these additional costs, we expect to deliver increased efficiency and operating leverage consistent with the cost to income ratio declining below 40% over the medium term.
- We also plan to maintain the credit quality of the book such that we would expect to incur a cost of risk of between 25 and 35bps per year over the medium term. Further information on effect of changes to IFRS9 will be provided closer to the January 2018 implementation.

James Mack,
Chief Financial Officer

Strategic report

Asset Finance

2016 highlights

- Net lending to customers up by 17% to £1.6bn
- Customer numbers up 17% to c50k
- Organic origination of c£1bn, of which c30% was direct
- Broker's Leasing and Asset Finance Provider of the Year (NACFB)
- Segment result up 15% to £45.1m

	2016 £m	2015 £m	Movement %
Net interest income	59.4	51.8	15
Net fees and other income	4.2	4.3	(2)
Operating income	**63.6**	**56.1**	**13**
Administrative expenses	(12.9)	(12.0)	(8)
Impairment losses	(5.6)	(4.8)	(17)
Segmental profit	**45.1**	**39.3**	**15**
Net loans to customers	**1,573.4**	**1,346.7**	**17**
Organic origination	994.2	893.0	11
Gross interest income yield (%)	6.0	6.3	(0.3)
Net interest margin (%)	4.1	4.3	(0.2)
Cost of risk (%)	0.38	0.40	(0.02)

Asset Finance predominantly supports capital investment in business critical assets. Leveraging our depth and breadth of expertise, we finance a wide array of assets such as plant and machinery, commercial vehicles, technology, office equipment, and cars. This flexibility enables us to meet the needs of customers of all sizes across key industries. In addition, we offer wholesale and block discounting facilities to smaller finance companies and brokerages enabling them to extend credit directly to SMEs.

Performance

Net loans to customers were up by over £200m to £1.6bn, an increase of 17% driven by organic origination of £1bn; extending our Asset Finance franchise to c50k small UK businesses.

We maintain a leadership position in the competitive broker-introduced market, supporting a range of customer segments across a significant number of asset classes. We have also expanded our wholesale proposition, up c60% year-on-year. Net interest income was up 15% in the year to £59.4m, with NIM down slightly to 4.1%, driven by changes in mix and tenure, including the expansion of our wholesale channel.

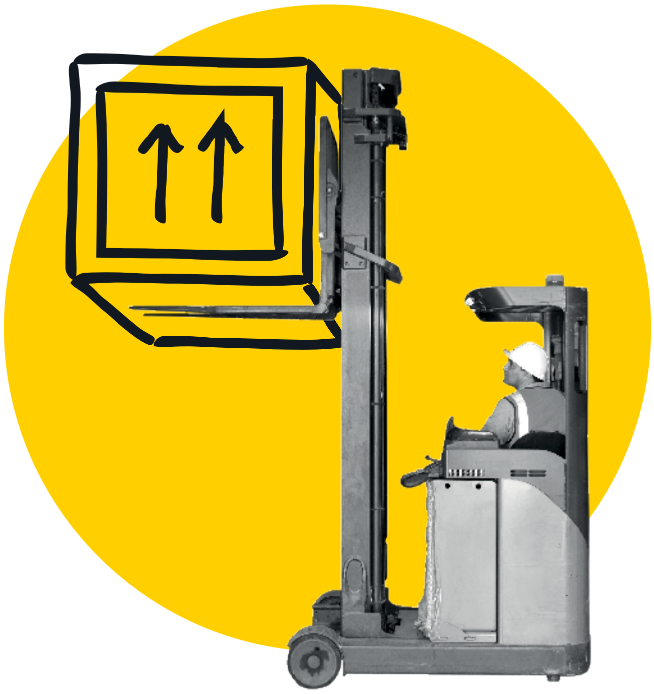
Impairments remained low at £5.6m (2015: £4.8m), with the cost of risk remaining broadly flat at 38bps, reflecting the high quality book backed by high-levels of tangible collateral. The overall segmental profit increased 15% to £45.1m (2015: £39.3m).

Market and strategy

The asset finance market was worth c£29bn of gross originations in 2016, growing by 7% year-on-year. Aldermore operates as a leader within the £5bn broker segment (which grew 9%) providing both straightforward forms of asset finance in addition to complex and structured deals which play to our specialist underwriting advantage. We are also increasing our share of smaller transactional deals and 'soft assets', which grew 15% year on year.

Consolidating our leadership in the broker market will be driven by our on-going investment programme in digital capability, aimed at enhancing our service offering by making it simpler for brokers to deal with us, especially in less complex cases. This capability can then be leveraged into new market adjacencies, including the £9bn vendor finance market.

The market is likely to remain competitive in 2017, driven by new entrants and consolidation in the broker channel, and we expect to see a continued trend toward wholesale deals. However, customer demand remains robust, with Aldermore well-positioned as market leaders to take our natural share of a growing market.



Banking for the bold

Flexible finance

ECS Engineering Services Ltd (ECS), a leading engineering company in Huthwaite near Mansfield, put in place the means to grow its business with the purchase of a new metal plate machine. The machine was funded by Aldermore and arranged by Newark-based finance broker FUNDINGROUND Ltd.

The new Peddinghaus plate machine replaced an older unit, enabling ECS to increase production capacity and provide greater efficiency and flexibility in their use of materials. This ultimately allows the company to deliver improved products to existing clients and to take on new orders.

Aldermore worked closely with the broker to understand ECS Engineering's requirements to ensure that the finance facility was structured appropriately and that the asset was delivered promptly.

"We urgently required the new plate machine to improve versatility, efficiency and quality. We were really grateful for both FUNDINGROUND's proactive approach and Aldermore's flexibility and speed of delivery."

Neil Smith, Technical Director at ECS Engineering

Strategic report

Invoice Finance

2016 highlights

- Refocused strategy delivering results
- Segmental result up 56% to £7.0m
- Administrative expenses down 29%
- Net lending down slightly to £154m

	2016 £m	2015 £m	Movement %
Net interest income	4.8	5.3	(9)
Net fees and other income	14.2	15.2	(7)
Operating income	**19.0**	**20.5**	**(7)**
Administrative expenses	(10.3)	(14.5)	29
Impairment losses	(1.7)	(1.5)	(13)
Segmental profit	**7.0**	**4.5**	**56**
Net loans to customers	**154.1**	**160.8**	**(4)**
Organic origination	41.7	35.1	19
Net revenue margin (%)	12.1	12.0	0.1
Net interest margin (%)	3.0	3.1	(0.1)
Cost of risk (%)	1.08	0.88	(0.20)

Invoice Finance provides working capital solutions for UK SMEs, ranging from vanilla invoice discounting and full-service factoring to more tailored customer solutions requiring Aldermore's in-house expertise.

Performance

Performance trends in Invoice Finance have shown significant improvement as a result of our strategy to consolidate and focus on larger discounting facilities to small businesses, demonstrated by a 56% increase in segmental profit.

Invoice Finance has a relatively short lifecycle compared to the Group's other portfolios, whilst net lending declined slightly by 4% in 2016 to end the year at £154.1m (2015: £160.8m), 19% growth in originations reflects our continuing focus toward invoice discounting and structured finance and away from lower value factoring business.

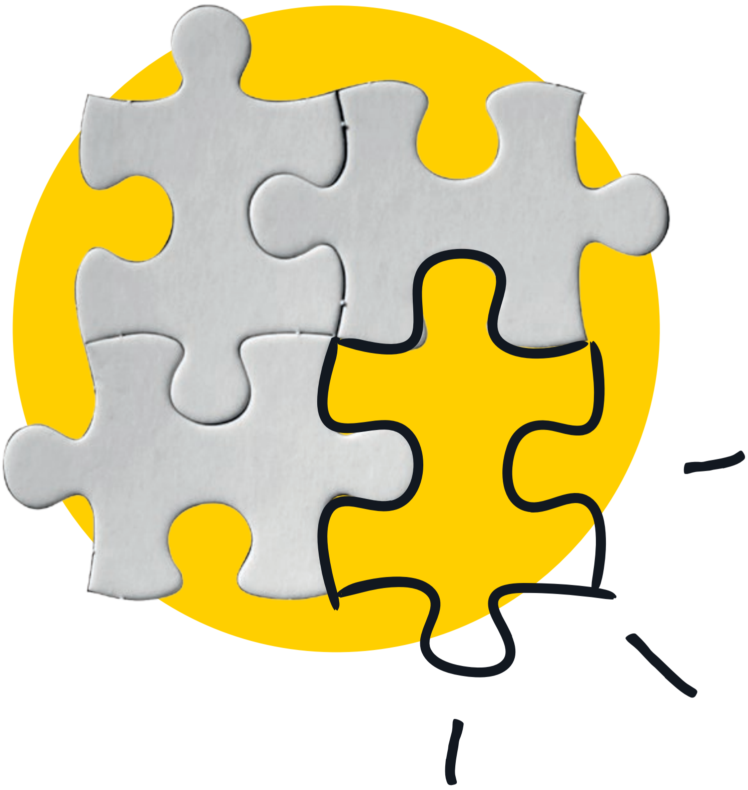
Fee income of £14.2m declined by £1.0m as we refocused and managed down customer numbers, reducing overall operating income by 7% to £19.0m. Administrative expenses were reduced by almost a third, reflecting management action to increase efficiency and focus the customer base whilst broadly maintaining overall net lending balances.

Impairments remain low, increasing by £0.2m to £1.7m, with a cost of risk at 108bps.

Market and strategy

The Invoice Finance business continues to offer a vital working capital solution for Britain's small businesses and provides a valuable contribution to the Group, as well as the potential for further opportunities for lending to small businesses. Aldermore remains a small player with less than 1% of the £21bn market.

We will continue to deploy a focused strategy, targeting key clients through enhanced sales capability, where we can develop relationships and support client growth. As we grow the client base and net lending, we will continue to drive efficiencies in the operating structure and enhance profitability.



Banking for the bold

Sitting pretty

Caldeira Limited, the UK's leading cushion manufacturer, prides itself on delivering quality combined with excellent value to its many retail clients around the world. The company has received a host of accolades, including being named among Richard Branson's Sunday Times/Virgin Atlantic Fast Track 100 companies, and since starting in Liverpool in 1991 has expanded into China and the USA.

Caldeira wanted to continue the growth and development of its three divisions and to expand its customer base. Like Caldeira, Aldermore prides itself on delivering quality service and value to businesses across the UK and was able to understand Caldeira's business and unlock valuable working capital with a £1.25m invoice finance facility, enabling the company to continue to build its reputation as a market leader in a highly-competitive global industry.

“Aldermore has a reputation as a great alternative to the high street lenders and I've been impressed by what I've seen so far, especially from the business development team. I'm looking forward to Caldeira's next stage of growth and to developing our business worldwide.”

Tony Caldeira, Founder and Managing Director, Caldeira Limited

Strategic report

SME Commercial Mortgages

2016 highlights

- Net lending to customers up by 12% to £0.9bn
- Customer numbers up 26% to c.2,000
- Organic origination of £435m
- Direct origination around 25%
- Segment result up 44% to £40.7m

	2016 £m	2015 £m	Movement %
Net interest income	45.4	34.2	33
Net fees and other income	1.3	0.8	63
Operating income	**46.7**	**35.0**	**33**
Administrative expenses	(3.1)	(4.8)	35
Impairment losses	(2.9)	(2.0)	(45)
Segmental profit	**40.7**	**28.2**	**44**
Net loans to customers	**929.9**	**829.2**	**12**
Organic origination	435.1	427.6	2
Gross interest income yield (%)	6.6	6.5	0.1
Net interest margin (%)	5.2	5.0	0.2
Cost of risk (%)	0.33	0.29	(0.04)

Our SME Commercial Mortgages business provides mortgages for investment in shops, warehouses, industrial units and offices or for residential Property Development (PD) distributed via financial intermediaries or directly to customers.

Performance

In 2016, we grew net loans to customers by 12% to £930m (2015: £829m) driven by robust organic origination partially offset by increased redemptions. Approximately 75% of originations were introduced via specialist brokers, with whom we have strong relationships. A further c25% engaged with us directly, as we continue to see a growing volume of repeat business.

The net interest margin increased slightly by 21bps to 5.2% which, combined with momentum in loan growth, has driven a 33% increase in operating income to £46.7m (2015: £35.0m). The reduction in operating expenses over the year reflects our focus on improving operating leverage as well as the greater allocation of operational resources to other Mortgages segments in 2016 to support growth.

Despite impairments in 2016 including greater prudence in collective provisioning, they remained low at £2.9m (2015: £2.0m), reflecting the low levels of arrears and continued relatively benign credit environment. The book remains backed by high quality tangible collateral with indexed loan to value, excluding PD, of 62% (2015: 63%). Our PD business had £229m of loans outstanding at the year end, with a loan to gross development of 58%. In total, the segmental profit for SME Commercial Mortgages increased by 44% to £40.7m in 2016 (2015: £28.2m).

Market and Strategy

The commercial mortgage market was worth c£43bn in originations during 2016, of which Aldermore represented less than 1%, focused on multi-let commercial investment property loans and property development to experienced regional developers.

Aldermore differentiates itself through its specialist underwriting capability and strong service proposition, enabling us to generate strong margins. Our commercial underwriters work closely with customers and our approved panel of c1k specialist brokers to understand the property use, the tenant covenant and the local market dynamics to underwrite effectively, and earn a premium.

The segments in which we operate are expected to remain competitive. However, we will continue to deploy our specialist underwriting advantage in our core niches. Specialist brokers will continue to be our priority route through which we serve our customers but we will also seek to continue to expand our direct origination capability.

Banking for the bold

Building for the future

Jamie Barnett and Nicki Cadwallander, joint owners of Worcester Properties Ltd, have a long-standing relationship with Aldermore going back five years. Specialising in student properties, Jamie and Nicki were initially introduced to Aldermore through a broker.

From starting with one house, Worcester Properties Ltd is now the largest single provider of student accommodation in Worcester and is involved in larger new builds for students.

During 2016, Aldermore assisted with two Worcester Properties loans, both units planned for further development. One was the previously disused Butlers Gym in Worcester. The gym is now being converted into a 48 bed student house of multiple occupation property. Once completed, it will be refinanced and let out to students on an annual basis.

Separately, a new development finance deal has been agreed for a 70-room facility to service Warwick University. The end value of the property is expected to be almost triple the purchase price once the development is completed.

"We regard Aldermore as a partner or colleague rather than just a lender. We have a great relationship with them, and we always have Aldermore in mind when we approach new deals."

Jamie Barnett and Nicki Cadwallader,
Worcester Properties Ltd

Strategic report

Buy-to-Let

2016 highlights

- Net lending to customers up by 38% to £3.3bn
- Customer numbers up 25% to c20k
- Organic origination of £1.3bn
- Direct origination of c20%
- Consolidation of operations in one centre of excellence
- Segment result up 26% to £83.1m

	2016 £m	2015 £m	Movement %
Net interest income	90.4	73.3	23
Net fees and other income	6.8	3.0	127
Operating income	**97.2**	**76.3**	**27**
Administrative expenses	(10.7)	(9.0)	(19)
Impairment losses	(3.4)	(1.3)	(162)
Segmental profit	**83.1**	**66.0**	**26**
Net loans to customers	**3,326.0**	**2,417.9**	**38**
Organic origination	1,289.2	673.1	92
Gross interest income yield (%)	4.7	5.0	(0.3)
Net interest margin (%)	3.1	3.3	(0.2)
Cost of risk (%)	0.12	0.06	(0.06)

Buy-to-Let (BTL) provides a comprehensive proposition catering for both individual and corporate landlords, simple to complex properties, including HMOs, and from a single property investment to large portfolios.

Performance

We significantly outperformed the market in 2016, growing net loans by 38% to £3.3bn, driven by a 92% increase in organic origination to £1.3bn. This strong growth also reflects our operational agility, as we took advantage of the market spikes in the first quarter, ahead of the introduction of an increase in stamp duty, and in the fourth quarter when we successfully took share in an active market.

Strong lending growth and a broadly stable net interest margin drove a 23% increase in net interest income to £90.4m (2015: £73.3m). Operating income was up 27% to £97.2m, with fee income benefitting from record application numbers, as we grew our customer base by 25% to c20k.

The £1.7m increase in administrative expenses is driven by an increased allocation of operational resources to support the strong loan growth delivered in the year.

A modest increase in the cost of risk to 12bps is in line with expectations and remains low. The increase is partly driven by increased prudence in collective provisioning as we extended emergence periods by three months to reflect increased economic uncertainty. The quality of the book remains robust, with average loan balances of just £170k across the portfolio and an indexed LTV of 63%. The segmental result demonstrated excellent progress, growing by 26% to £83.1m (2015: £66.0m).

Market and strategy

The BTL market was worth c£41bn in 2016, representing c14% of the overall mortgage market. Aldermore is a mainstream player in BTL and took a c3.2% market share of originations in the year but with an overall market share of c1% in this market, we have clear headroom for growth.

Our proposition offers market-leading breadth of offering for all landlords but our clear differentiation is at the specialist end of the market, with professional landlords (more than three properties) who represent c60% of our portfolio. Our distribution strategy is primarily broker-led but with a growing proportion of customers, 20% in 2016, engaging with us directly. We have a diverse geographic footprint but a bias towards the strong rental markets in Greater London and the South East.

The fundamentals supporting demand in the BTL market remain strong. There remains a shortage of housing stock and new housebuilding continues to lag Government targets. Whilst regulatory changes to personal tax relief, underwriting and affordability testing are expected to reduce the overall rate of market growth, we expect to benefit from the increased professionalisation of demand and to continue outgrowing the market, building on our small market share.

Banking for the bold

Banking on your terms

Shoaib Cheema is an experienced landlord with a buy-to-let portfolio of five properties, but a first-time Aldermore customer. He first met one of our representatives at a London property show, and decided to approach us directly for a five-year fixed rate limited-edition deal.

"I approached Aldermore primarily as I found their product range interesting and very attractive when compared to the other rates available on the market at the time."

With the uncertainty caused by the EU referendum vote, Mr Cheema was looking for a deal to provide him with longer-term security, and chose Aldermore's five-year fixed product to give him just that. Our specialist team was able to take Mr Cheema's application through to offer in just 17 working days.

"Dealing with Aldermore was very pleasant and the process was very smooth. I found Aldermore very responsive, professional and precise. They placed a much higher emphasis on providing help to the customer compared to other lenders."

Shoaib Cheema,
Buy-to-let investor and satisfied customer

Strategic report

Residential Mortgages

2016 highlights

- Net lending to customers up by 7% to £1.5bn
- Customer numbers up 8% to c11k
- Organic origination of £0.5bn
- 'Best Specialist Mortgage Lender' – Your Mortgage
- Investment in customer proposition and retention
- Segment result up 12% to £45.1m

	2016 £m	2015 £m	Movement %
Net interest income	49.6	43.8	13
Net fees and other income	1.9	2.2	(14)
Operating income	**51.5**	**46.0**	**12**
Administrative expenses	(4.5)	(5.1)	12
Impairment losses	(1.9)	(0.8)	(138)
Segmental profit	**45.1**	**40.1**	**12**
Net loans to customers	**1,493.9**	**1,390.2**	**7**
Organic origination	466.0	582.3	(20)
Gross interest income yield (%)	5.3	5.6	(0.3)
Net interest margin (%)	3.4	3.7	(0.3)
Cost of risk (%)	0.13	0.07	(0.06)

Residential Mortgages serves creditworthy first-time buyers, the self-employed and professionals, who often fall outside the automated and inflexible lending criteria of some of the mainstream providers.

Performance

The Residential Mortgages portfolio grew by 7% in 2016 to £1.5bn (2015: £1.4bn), driving net interest income up by 13%. This growth was driven by £466.0m of originations which were lower than in 2015 (2015: £582m) due to a greater focus on buy-to-let in 2016. Originations in 2016 were partly offset by redemptions increasing to £365.6m (2015: £171.8m) which was weighted to the second half of the year due to the maturity of the high yielding first cohort of Help to Buy mortgages written in mid-2014.

The net interest margin reduced by c30bps to 3.4% (2015: 3.7%), driven by a number of factors, including the reduction in the base rate and the redemption of high-yielding first cohort of Help to Buy customers.

The reduction in operating expenses over the year reflects our focus on improving operating leverage as well as the allocation of operational resources between Mortgages segments to support loan growth, which is based on origination activity and net loan balances. Despite increased prudence in collective provisioning, impairments remained low at £1.9m (2015: £0.8m), reflecting the relatively low levels of arrears and continued benign credit environment. The overall segmental profit increased 12% to £45.1m (2015: £40.1m).

Market and strategy

The residential mortgage market was worth c£205bn in originations during 2016, of which Aldermore represented just 0.2%, focused on specialist sub-segments, including first time buyers, the self-employed and professionals. We are differentiated through our use of specialist underwriting capabilities which complement modern credit rating engines. Our system-driven approach automatically completes basic checks, creates a case file, and highlights areas for further review enabling our human underwriting team to make better informed credit decisions, with greater efficiency.

The mortgages platform, operated across all three mortgage segments, underwent an upgrade during 2016, driven by requirements from the Mortgage Credit Directive but also providing an opportunity for us to enhance system functionality, including the development of a product switching portal, which will enable future growth in our target segments going forward.

Aldermore operates as a small player in specific niches and we are confident that we can continue organic origination-led growth within the large residential market. Specifically, the Mortgage Indemnity Guarantee (MIG) product that we introduced to follow-on from the Government's Help to Buy Mortgage Guarantee scheme, and a package of measures to enhance our proposition and service to the self-employed market are expected to drive increased origination activity.

Banking for the bold

Seeing the wood for the trees

Darren Herrington owns and runs his own business, Somerset Forestry, which provides tree surgery and all aspects of tree care. Somerset Forestry has posted strong profits over the past few years and Darren was looking to move from his flat into a three-bedroom terraced home with his wife and two children.

The mortgage on his flat was with a major high street lender, and as a long-time customer, he went to them first. However, during the application process Darren found that the high street bank didn't fully understand his accounts or his business.

Focusing on growing his business, Darren had been paying himself only what he needed to get by and investing the rest in new machinery and equipment, some of which he had financed with Aldermore. He approached us about taking out a mortgage for his new home and our specialist underwriters were able to review his accounts and approve his application.

"

With the high street banks, all they look at is what you earn and what you pay in tax. Aldermore was different, the team understands how a self-employed business works... Everything went very smoothly."

Darren Herrington, Business (and home) owner

Strategic report

Central functions
Savings, Treasury and Support Functions

2016 highlights

- Total deposits up by 16% to £6.7bn
- SME deposits up by 18% to £1.6bn
- Corporate deposits up by 66% to £260m
- Customer numbers up by 12% to c134k
- Highly recommended by customers (Retail 93%, Business 97%)

	2016 £m	2015 £m	Movement %
Net interest income	(10.2)	(9.5)	(7)
Net fees and other income	(0.3)	0.3	(200)
Operating income	**(10.5)**	**(9.2)**	**(14)**
Administrative expenses	(77.7)	(70.1)	(11)
IPO-related costs	–	(4.1)	–
Impairment of Invoice Finance goodwill	(4.1)	–	–
Segmental loss	**(92.3)**	**(83.4)**	**(11)**

Central Functions includes the Group's Treasury function and Savings division, as well as common costs which are not directly attributable to the operating segments. Common costs include central support function costs such as Finance, IT, Legal and Compliance, Risk and Human Resources.

Performance

Net interest income includes the interest expense relating to the Tier 2 Notes and part of the income or expense arising from derivatives held at fair value in hedging relationships, neither of which are recharged to segments.

Net fees and other income predominantly includes the net expense or income from derivatives not currently recognised as being in hedging relationships and other financial instruments at fair value through profit or loss and gains on disposals of available for sale debt securities.

Central administrative expenses, increased by 11% to £81.8m (2015: £74.2m) driven by the recruitment of colleagues as we invested to further support growth and risk management.

At the end of 2015, we held goodwill of £4.1m related to the acquisition of Absolute Invoice Finance (Holdings) Limited which was supported using a Fair Value less Cost of Disposal methodology. During 2016, as a result of the general fall in market values of financial services businesses following the EU referendum, management concluded the goodwill balance was fully impaired and a charge of £4.1m has been recognised in the income statement.

The segmental result was a charge of £92.3m (2015: charge of £83.4m).

Savings market and strategy

The market for savings in 2016 continued to be dominated by a backdrop of low and falling interest rates from a lower base rate and reduced competition for deposit funding in response to Bank of England funding schemes. In particular, the SME savings market remains highly attractive given the opportunity for non-traditional providers to offer a demonstrably better customer proposition – both in terms of rate and experience.

We continue to focus on small businesses where insight and research demonstrates a clear customer demand and market opportunity. Inflationary pressures in the economy suggest that we may have reached the bottom of the interest rate cycle and base rate movements are more likely to be upwards. This, together with increases in the annual ISA allowance (to £20k) and FSCS deposit protection limit (to £85k), means the outlook for savings customers is positive.

Risk management, internal control and viability reporting

Assessment of principal risks

As described further in the risk management section, the Board is responsible for determining the nature and extent of the principal risks it is willing to take in order to achieve its strategic objectives. The Board is also ultimately responsible for maintaining sound risk management and internal control systems. In line with requirements of the UK Corporate Governance Code, published by the Financial Reporting Council in September 2014 (the "Code"), the Directors have performed a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity.

The principal risks are further described on page 33 and the current emerging risks are described on pages 34 and 35.

Risk management and internal controls

The Board monitors the Group's risk management and internal control systems. A review of the effectiveness of the systems has been performed incorporating all material controls, including financial, operational and compliance controls.

The Group's risk management and internal control systems are designed to identify, manage, monitor and report on risks to which the Group is exposed. It can therefore only provide reasonable but not absolute assurance against the risk of material misstatement or loss. Further details of the processes and procedures for managing and mitigating these risks are provided in the risk management section from page 106.

The effectiveness of the internal controls was regularly reviewed by the Board, Audit Committee and Risk Committee during the year. This involved receiving reports from management including reports from Finance, Risk, Compliance, Group Internal Audit and the business lines. The Audit Committee also receives reports on internal controls from the Group's external auditor. Where recommendations are identified for improvements to controls these are monitored by Group Internal Audit who report the progress made in implementing them to the Audit Committee.

Based on the review performed during the year, and the monitoring and oversight activities performed, the Audit Committee, in conjunction with the Risk Committee, concluded that the Group's risk management and internal control systems were effective. The Audit Committee recommended a statement to this effect to the Board.

Based on this assessment, the Board are satisfied with the effectiveness of the Group's risk management and internal control systems.

Viability

In accordance with provision C.2.2 of the Code, the Directors have assessed the prospects of the Group over a three-year time horizon to 31 December 2019.

The Directors concluded that a three-year time horizon is an appropriate length of time to use to perform the assessment, mainly because financial forecasts have a greater level of certainty over three years. The Board monitors a longer term strategic plan which extends over the three-year horizon. This longer term strategic plan provides less certainty of outcome, but provides a robust planning tool against which strategic decisions can be made.

In the assessment of the viability of the Group, the Directors considered each of the principal risks set out on page 33 of the strategic report. In addition, the assessment has been performed with reference to the Group's current position and strategy.

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. The Directors have also considered the implications of the UK referendum on EU membership. The information considered includes a wide range of stress testing which is performed as part of both the ICAAP and ILAAP processes as further described in the Risk Management Section from page 106.

Based on the above assessment, the Directors have concluded that there is a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period to 31 December 2019.

Strategic report

Risk overview and culture

Our approach to risk

Effective risk management is a core component of the Group and is embedded throughout the organisation. The Board and senior management ensure that a strong risk culture is at the heart of everything we do, with a clearly defined risk appetite.

Risk Management Framework

The Risk Management Framework outlines the process by which we identify, manage, monitor and report risks to which the Group is exposed. The framework is supported by supplemental frameworks, policies, processes and procedures which ensure that the Group's risks are managed appropriately and within the Board sanctioned risk appetite. More detail is provided on page 108.

Principal risks:

Principal risks are the primary risks that the business faces, which could impact the delivery of our strategy. Read more about those risks and how they are managed opposite and in detail on page 112.

Emerging risks:

Emerging risks are those risks that have been identified on the horizon, which may have an impact on our future performance, compromise our existing strategy or threaten our business model. These risks are discussed on pages 34–35.

Legal and Regulatory risks:

We operate within the context of the UK legal and regulatory environment (as well as European law adopted and supported by UK regulators). The Legal and Compliance functions ensure that we are aware of both current and upcoming legal or regulatory requirements.

Risk principles and risk culture

Franchise preservation
The protection of our reputation and franchise is paramount. Everything we do is guided by the principle of putting the customer at the centre of what we do. It informs our business strategy, the way in which we do business, and the manner in which we treat our customers and other stakeholders.

Risk culture
The Board ensures that the Group actively embraces a strong risk culture, where all staff are accountable for the risks they take. The Board leads in setting the risk appetite and ensuring that the Risk Management Framework is fully embedded with a strong focus on the adherence to risk appetite in all metrics. Staff performance management and reward practices all have key risk inputs, and a focus on risk management in their design. The Group aims for employees to be risk aware, and to strike the right balance between delivering on objectives, individual accountability, and maintaining a safe and secure business adhering to risk appetite

Strong risk governance:
Risk is managed using the three lines of defence principle – separating risk origination from risk oversight and risk assurance. Governance is provided through a formal committee process, including the Board Risk and Audit Committees.

Defined risk appetite
A clearly defined Risk Appetite Framework is in place which allows the setting of detailed risk appetite and reporting metrics for principal risks.

Independent risk oversight and challenge
Risk is the risk oversight and challenge function, independent of the businesses and functions, with a reporting line to the Board Risk Committee. It is the basis of the second line of defence.

Risk management and control
Risks are identified, managed, monitored and reported against pre-determined risk appetite where appropriate. All are subject to governance and controls. Responsibility for the identification, assessment, measurement, monitoring and management of the risks rests with the first line of defence, being the business units and functions.

Principal risks

Key:

- ↑ Up
- → Stable
- ↓ Down

Principal risk	Mitigation		Commentary
Credit Risk The risk that customers are unable to make their loan repayments.	· Focus lending where we have specific expertise · Limit concentration of lending by size, geography and sector · Obtain appropriate level of security cover and perform affordability testing at origination · Embed clear lending policies in each business area · Regularly review performance against risk appetite · Stress test the portfolio to test resilience	↑	Group cost of risk remains low at 23bps (2015: 19bps) reflecting the maturation of the book and a move to less benign conditions. The heightened uncertainty for the UK economy following the referendum vote, and the implementation of the result, has increased the possibility of higher future credit losses.
Capital and Liquidity Risk The risk that we fail to hold sufficient or appropriate reserves to support growth, meet regulatory requirements, or repay obligations as they fall due.	· Monthly monitoring of capital adequacy against targets and forecasts · Maintenance of a liquidity buffer based on stressed requirements · Daily monitoring of liquidity buffer · Stress testing and sensitivity analysis of both capital and liquidity · Maintenance and annual review of the Contingency Funding Plan · Ongoing review, analysis and impact assessment of regulatory changes	→	The Group's capital remains stable and well above regulatory minimum requirements. We successfully raised additional £60m Tier 2 capital in October 2016. The Group's liquidity position remains stable.
Market Risk The risk that market movements adversely impact the Group.	· We do not seek to take or expose the Group to market risk and we do not carry out proprietary trading · We match interest rate structures of assets and liabilities to create a natural hedge where possible · Unmatched interest rate exposures are hedged with derivative 'Swap' contracts	→	The Group's approach remains prudent and underlying risks remain unchanged.
Operational Risk The risk of loss due to failure in processes, systems or human error, including outsourcing.	· Embed and ensure all staff understand and follow the Operational Risk Management Framework · Analysis of Risk Event Reporting and follow-up actions · Monitoring of the operational risk profile, and risk event reporting · Continuing to invest in information security and cyber controls following our Cyber strategy · Implementation of a Third Party Supplier Framework	→	The Group continues to invest in its IT infrastructure including Cyber controls and resilience.
Compliance, Conduct and Financial Crime Risk The risk of sanctions or financial loss as a result of a failure to comply with applicable laws, including anti-money laundering and the risk of causing unfair outcomes or detriment to customers.	· The Group provides simple and transparent products and operates solely in the UK market. · Provide and monitor against clear policy frameworks, including Conduct Risk and Product Governance · Continued investment in staff training and awareness · Horizon scanning and impact assessment of potential regulatory change	→	Whilst the financial services sector remains subject to increasing regulation and scrutiny we believe our risks remain unchanged from the prior year.
Reputational Risk Failure to meet the expectations and standards of our customers, investors, regulators or other counterparties.	· All governance committees have reputational risk considerations as a key part of their remit · Group Corporate Affairs monitors reputational risk, under the executive direction of the Group CEO · All employees are made aware of their responsibilities under the Bank's Reputational Risk Policy · Maintenance of open and transparent relationships with regulators and other key stakeholders	→	We believe the risks remain unchanged from the prior year.

Strategic report

Emerging risks

Themes	Risk
Regulatory change/intervention	
Basel Committee on Banking Supervision. December 2015 Second consultation on Revisions to the Standardised Approach for Credit Risk proposals	In December 2015 the BCBS issued a second consultative document, (Revisions to the Standardised Approach for Credit Risk) containing, amongst others, proposals to increase the capital treatment of buy-to-let and commercial real estate lending. If these proposals were implemented as outlined, the capital requirements for these market segments would increase significantly and require the execution of management actions to mitigate their impact.
IFRS 9	New reporting requirements under IFRS 9 introduce forward looking credit loss models which will lead to changes in the timing of impairment recognition. The requirement, which comes in to effect from 1 January 2018, requires the development of new risk models. The risk is that the Group is unable to deliver these before new regulation takes effect.
Buy-To-Let Mortgages Tax Changes and revised PRA Underwriting Standards	Potentially adverse impact on buy-to-let market of changes to UK tax regime and failure to comply with expectations of the regulator set out in PRA Supervisory Statement on buy-to-let Underwriting Standards issued in September 2016.
Economic and political environment	
The UK's decision to leave the European Union	Heightened economic and political risks following the UK's decision to leave the European Union. As a UK focused Group, we are sheltered from the more direct impacts of the Referendum, such as access to European markets but we are exposed to the wider economic impacts. To date we have seen no direct impact on either the lending or deposit sides of our business.
International economic and political environment	The geopolitical environment presents risks to global markets, including the impact of a new administration in the USA, deflationary concerns in the EU and continued political risks in Russia and the Middle East.
Exposure to real estate	We have a substantial lending exposure to the residential, buy-to-let, and commercial property sectors. Any property value falls, or increase in unemployment may lead to a rising number of defaults.
Interest rate environment	The low interest rate environment, introduced to stimulate growth following the financial crisis, has persisted for longer than first expected. If interest rates are increased, or growth slows, unemployment may rise and loan servicing costs may increase, which could cause an increase in credit losses.
Competitive environment	
New entrants and increased competition	The competitive landscape contains risks from new entrants, increased competition from incumbent lenders and disruptive products/software solutions potentially affecting both lending and deposit taking activities. The effect of this could result in lower volume, higher customer attrition and/or lower net interest margins.
Technology risk	
Cyber-crime	Cyber-crime is a significant threat in our increasingly interconnected world and exposes all businesses and in particular financial services companies to financial as well as reputational damage. Cyber threats continue to evolve as demonstrated by high-profile cases. The increased size of the Group, and growing customer base, increases the profile of the Group to would-be cyber attackers.
System failure/ outsourcing	The Group has a number of major outsource partners and critical supplier relationships who are key elements of the overall supply chain. The failure of one of these key partners could significantly impact the Group's operations and reputation.

Key:

- ↗ Up
- → Stable
- ↘ Down

What we did in 2016	What we expect in 2017 and Direction	Likelihood change from last year
We conducted an impact assessment of the proposed changes, followed by scenario analysis including feasible management actions. The Bank also undertook a feasibility study on transitioning from Standardised to an Internal Ratings Based (IRB) approach to capital. This included a gap analysis against current regulatory requirements and has informed our thinking into possible responses, including the possibility of applying for regulatory approval to operate in an IRB environment.	The IFRS9 work on credit models (see Emerging Risks IFRS9) takes us closer to the sophistication required for an IRB approach to capital which may help to mitigate the risk of future changes in capital requirements. We will continue to monitor the cost and benefits associated to moving to IRB, as the regulatory changes and timeframes for implementation become clear.	↗
We assessed the impact of IFRS 9 and have initiated a project plan to ensure compliance with the new standard ahead of its proposed implementation date of 1 January 2018.	We are on track with enhancements to our credit risk models and expect to be IFRS9 compliant ahead of January 2018 when the new accounting standard is introduced.	→
Continued monitoring of Buy-to-Let business levels. Amendment to Buy-to-Let affordability calculation (interest cover ratio and stress rate) in December 2016 to meet expectations in PRA's supervisory statement.	Further review of PRA's expectations in terms of portfolio landlords and use of personal income in affordability calculation, with expectation that all changes to approach considered necessary will be introduced by the 30 September 2017 deadline	→
The Group incorporated these risks in stress testing conducted during 2016.	The Group will continue to monitor the situation and will decide on an appropriate response, based on internal scenario planning, as the situation develops.	→
We have monitored these risks, and the UK economy has remained robust in the face of these domestic and global headwinds. As a UK-focused business we have not felt any adverse consequences across our trading franchise.	The medium-term outlook is unclear and there remains a possibility that material international events could adversely affect the UK, in addition to any EU exit impacts. These could act as a drag on the UK economy and affect the sectors to which we lend. We aim to manage these risks by maintaining a well-diversified product base, and remaining firmly focused on the UK.	↗
The Group continued to monitor and manage the performance of our real estate backed lending, and identified no significant change in performance in 2016. We also continued to enforce our underwriting criteria, which includes affordability testing at the point of origination.	The risks are expected to remain unchanged in 2017.	→
We conducted specific stress testing on our loan portfolio and maintained strict underwriting criteria, which includes stressing affordability rates at interest rates above those being paid today.	We will continue to monitor the external environment and respond to any interest rate rises as appropriate.	→
The risk of competition has been incorporated in our forward planning process and the external market is monitored on a consistent basis.	We will continue to monitor the external environment and adapt accordingly.	→
During 2015, and continuing into 2016, we strengthened our defences against cyber-crime. We have a cyber risk response plan, which involves working with our technology partners, and ensures that there is a practical response and appropriate escalation.	This remains a key risk area and the Group will continue to invest in ongoing security improvements.	→
The Group has controls in place in relation to sourcing and onboarding suppliers. In 2016, work was begun to further enhance the supplier management framework.	Continued focus during 2017 as the updated framework is implemented across the supplier estate.	→

Strategic report

Corporate responsibility

Our overriding principle is to support the people of Britain in their professional and personal lives. We do this by acting responsibly, giving back and taking a collaborative approach with our stakeholders. We believe that a business cannot deliver sustainable long-term returns without considering its wider impact on society.

Our customers

More customers than ever before bank with Aldermore. At the end of 2016, we served over 220k customers, an increase of 14% compared to the end of 2015.

Listening to feedback

1. We listen to our customers and take on board their feedback

- Received an average score of 4.5 out of 5 through our online Ratings & Reviews service
- 94% of customers said that they would recommend Aldermore
- Launched our Voice of the Customer programme to enable us to collect real-time customer feedback and respond to it

Putting customers first

2. We run the business in the interest of customers

- Actively manage our cash flow to ensure that we can repay our depositors
- Employ a combination of manual and automated underwriting to ensure we are lending responsibly
- Ensure that our customers understand terms and conditions, including lock-in periods

Acting responsibly

3. We are sensitive to every customer's situation

- Consider each customer as an individual rather than taking a one-size-fits all approach
- Treat vulnerable customers sensitively, providing a flexible, tailored service to meet their needs
- Ethos of treating customers fairly underpinning all of our policies and processes

What we did during the year and how our approach supported our business:

- We actively use customer feedback that we receive through our online Ratings & Reviews service to improve our offering. During 2016, we received an average rating of 4.5 out of 5 and 94% of customers who posted feedback on our website said they would recommend us.
- In 2016, we launched our Voice of the Customer programme to enable us to collect customer feedback in real-time. As part of this programme, we enhanced our methodology for measuring NPS, enabling us to gain a deeper understanding of how our customers and brokers feel about our service and providing insights to help us improve. Our overall customer NPS increased from +29 in 2015 to +43 in 2016 driven by our competitive interest rates, security and flexible lending criteria.

	2016	2015	% change
Customer numbers	**222,917**	195,061	14
Customer Net Promoter Score (NPS)	**+43**	+29	N/A
Average Ratings & Reviews score	**4.5 out of 5**	4.6 out of 5	N/A
Industry awards	**13**	25	(48)
New lending to small and medium-sized enterprises	**£1.47bn**	£1.36bn	8

Case study

Supporting first time buyers

First time buyers are critical to the effective functioning of the housing market. During 2016, we helped 1,403 first time buyers to take their first step onto the property ladder.

Aldermore has been an enthusiastic supporter of the Government's Help to Buy scheme for several years. We were one of the first lenders to take part in the scheme and the first to allow borrowers to remortgage onto Help to Buy products.

We were also one of the first organisations to offer the Help to Buy: ISA. We continue to provide this product, incentivising more people to save and enabling first time buyers to build a deposit towards their first home.

Our people

It is thanks to our people that we are able to offer a superior service to our customers. During 2016 we placed a great deal of focus on our culture, including how we encourage diversity in our workplace, engage our colleagues and drive expertise throughout Aldermore.

Promoting diversity

1. We are committed to diversity in the workplace

- Committed to equal opportunities for all our people, irrespective of gender, race, colour, age, disability, sexual orientation or marital or civil partner status
- Amongst first banks to sign up to HM Treasury's Women in Finance Charter
- Maintained our employee gender split at around 50/50

Engaging our people

2. We include our people in the future of our business

- Launched the Big Conversation, our new approach to engaging with our people
- Held our 2016 Employee Summit to allow all colleagues to hear from and interact with our Executive team
- Ran our first extended wellbeing programme, encouraging our people to look after themselves at work and at home

Building expertise

3. We support the professional development of our people

- Supported future leaders through our 'Next Generation Leaders' and 'Aspiring Managers' programmes
- First round of graduations from our Project Academy programme, which has been designed to improve project management capability across the Bank

What we did during the year and how our approach supported our business:

- We signed up to HM Treasury's Women in Finance Charter, which aims to increase female representation in senior management roles in the financial sector, committing to increasing the proportion of female senior managers at Aldermore to 30% by 2020 and to maintaining our gender split at around 50/50.
- To support our commitment to greater female representation, we launched the Women@ Aldermore network which brings in senior women from outside the business to provide advice and insight to our female employees about how to progress their careers.
- In October, we held our 2016 Employee Summit allowing all of our people to come together in one place to network, hear from our Executive team and discuss the future of the Bank. Following the event, 91% of employees said that they were proud to be part of the Aldermore journey.

Employees	2016	2015	% change
Number of employees *	**900**	816	10
Number of female employees *	**408**	383	7
Percentage of female employees	**45%**	47%	(2ppt)
Number of senior managers *	**26**	32	(19)
Number of female senior managers *	**5**	6	(17)
Percentage of female senior managers	**19%**	19%	–
Percentage of employees who say they feel proud to be a part of the Aldermore journey	**91%**	90%	1ppt
Percentage of new joiners who came through our Refer a Friend scheme	**23%**	18%	5ppt

* Employee numbers as at 31 December 2016

Case study

Facilitating a Big Conversation

Effective two-way communication is vital in engaging our people and we place a great deal of emphasis on listening to employees.

At our 2016 Employee Summit we launched 'The Big Conversation', our new approach to engaging with our people which saw us gather their views on how we can enable an improved ongoing connection to Aldermore and better deliver on our strategic objectives.

After the summit we invited over 300 employees to sessions across our offices to provide their ideas and contributions. These sessions were complemented by a business-wide pulse survey, giving every employee a chance to contribute.

The Big Conversation has been our most in-depth discussion with employees ever, giving us a deeper understanding of our culture.

Strategic report

Corporate responsibility continued

Our communities and environment

The SMEs, landlords, homeowners and savers that we support, in turn support the communities in which they live and work. We understand that we have a responsibility to give back to these communities.

Leading the industry

1. We play our part as a responsible member of the banking community

- Actively involved with industry bodies including the BBA, FLA, ABFA, CML and IMLA
- Became a member of the Banking Standards Board

Giving back

2. We give back to the communities where we operate

- Raised £26,739 for the Batten Disease Family Association (BDFA), our charity of the year
- Our people spent 525 hours volunteering for local charities and other non-profit organisations

Reducing our impact

3. We are committed to reducing our environmental impact

- Our total greenhouse gas emissions during 2016 were 525tCO_2e
- Our total greenhouse gas emissions per employee were 0.59tCO_2e

What we did during the year and how our approach supported our business:

- In November 2016, Aldermore joined the Banking Standards Board, an independently led body that promotes high standards of behaviour and competence across the UK banking industry. As a member, we are playing our part in ensuring that the industry is trusted and viewed as having a positive impact on the communities in which we operate.
- A significant part of our fundraising efforts go towards our charity of the year, which is chosen through a Bank-wide employee ballot. In 2016, our colleagues chose the Batten Disease Family Association (BDFA) as our charity of the year. Our charity of the year for 2017 is Sands, the stillbirth and neonatal death charity.
- We piloted a volunteering programme with Employee Volunteering, the non-profit organisation. This saw our employees spending over 525 hours helping charities and other non-profit organisations local to our offices.

Communities	2016	2015	% change
Amount raised for Charity of the Year	**£26,739**	£19,399	38
Amount matched by Bank through £ for £ scheme	**£10,420**	£9,488	10
Number of hours volunteered by our colleagues	**525**	Not reported	N/A

Environment*	2016	2015	% change
Total greenhouse gas (GHG) emissions (tCO_2e)	**525**	721	(27)
Total greenhouse gas (GHG) emissions per employee (tCO_2e)	**0.59**	0.85	(31)

* Further details about our greenhouse gas emissions can be found in the Directors' Report on page 105.

Case study

Supporting broker education

Much of our success is down to our broker partners so we recognise the need to support the development of the next generation. 2016 marked the third year of our asset finance broker training programme, which sees us running workshops for emerging talent at our asset finance broker partners.

Sessions are delivered at Aldermore offices by independent trainers with in-depth industry knowledge. In 2016, modules included principles of asset finance, regulation and sales skills.

During 2016, we held four separate courses attended by over 120 brokers. Since launching the programme, around 280 young brokers have benefitted from the workshops which have equipped them with the expertise they need to be successful in their chosen field.

Aldermore has come a long way. We have built a bank from scratch and delivered impressive growth. However, the journey towards truly fulfilling our responsibilities to our customers, people and wider stakeholders has only just begun.

While we are judged on our ability to meet our financial objectives, the way in which we achieve these is equally important.

We are heading in the right direction. We are involving our customers and employees in every step of the journey and building the foundations so that we can continue our strong progress over the coming years.

Corporate governance

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Corporate governance

Chairman's introduction

"2016 has been a year of consolidation and evolution as we have strived to build on a strong governance framework that we established in preparation for our listing."

Danuta Gray,
Interim Chairman

UK Corporate Governance Code 2014 ("the Code") – statement of compliance

The Board is committed to the highest standards of corporate governance and confirms that, during the year under review, the Group has complied with the requirements of the Code, which sets out principles relating to the good governance of companies. Following the resignation of Glyn Jones as Chairman with effect from 6 February 2017, and the subsequent appointment of Danuta Gray as Interim Chairman, Danuta Gray is currently not discharging her role as Senior Independent Director. These responsibilities will be resumed on appointment of a new Chairman.

The Code is available at www.frc.org.uk

This corporate governance report describes how the Board has applied the principles of the Code and provides a clear and comprehensive description of the Group's governance arrangements.

Dear Shareholder

As your Interim Chairman, I am delighted to introduce our corporate governance report for the year ended 31 December 2016.

Firstly, as I highlighted in my statement on page 7, on behalf of the Board I would like to offer our sincere thanks to Glyn Jones who decided to step down from the Board on 6 February 2017 to enable him to focus on his new role as Chairman of Old Mutual Wealth. Since joining the Group in March 2014, Glyn chaired the Board through a significant period of growth and change for the Company as it successfully completed its IPO in March 2015. Prior to the Company's listing, Glyn played a pivotal role in setting the foundations for our current governance framework, which has provided a robust environment for the Group to deliver on its strategic and financial objectives within its risk appetite. He has left a strong, experienced and dedicated Board of Directors to lead the Group through the next stage of its development, and we remain committed to building on these foundations. An external agency has been appointed to help with the process of selecting Glyn's successor which is being managed through the Corporate Governance and Nomination Committee in line with our agreed Chairman Succession Framework. We are making good progress with the search and look forward to announcing a replacement in due course. Further information about the search process is set out in the Corporate Governance and Nomination Committee Report on page 60.

In terms of other Board changes, we welcomed Chris Patrick as a Non-Executive Director in November 2016 when he replaced Neil Cochrane as the representative of our Principal Shareholders. Neil stepped down as a Director in October 2016 subsequent to him resigning from AnaCap. Peter Cartwright also resigned in April 2016 as a shareholder-representative Director due to time commitments. We would like to extend our gratitude to both of them for their significant contribution during their respective tenures. The Principal Shareholders retain the right to a second seat on the Board but currently have one representative only.

Following the IPO, 2016 has been a year of consolidation and evolution as we have strived to build on the strong governance framework that we established in preparation for our listing. The following pages describe how we comply with the main principles of the Code, how the Board operates, and the key areas of focus for both the Board and its Committees during the year. Whilst it is difficult to narrow down our activities across the year to a few highlights, the strengthening of our Risk Management Framework overseen by the Risk Committee; the broadening of the financial performance measures within the balanced scorecard for the annual bonus scheme, such that they are more aligned to our KPIs; and the comprehensive tender process for the external auditor led by the Audit Committee, are all examples of areas where our Committees have supported the Board in developing our governance arrangements.

The Board recognises that one of the keys to the Group's long-term success is the development of a healthy corporate culture. As we continue to execute on our strategy, the Group's size and complexity will continue to increase, and the Board is cognisant that the Group's culture has to evolve alongside this. Culture starts at the top, and the Board and the Executive Committee together have to drive the values and behaviours that support our brand. During the year, the Executive Committee initiated a new programme of 'Big Conversation' discussions with our employees regarding the kind of company they want Aldermore to be. A dashboard of cultural metrics has also been developed, and the Board will continue to receive regular updates on these initiatives as they progress.

The Board strongly supports the principle of diversity, of which gender is one important aspect, and we were therefore delighted to support the Group signing up to the Women in Finance Charter to promote wider female representation in senior management roles in finance. The Board has committed to a target of 30% for our female senior managers by 2020, and to maintaining our gender split at around 50/50. In respect of possible targets at Board level, we have not established a measurable target for gender representation but remain committed to increasing all aspects of diversity. As set out in our Board Diversity Policy, Director appointments are subject to a formal, rigorous and transparent procedure and are made on merit against a defined job specification and criteria. We will continue to monitor whether it is appropriate to set a Board target in the future taking into account developments arising from the Hampton – Alexander Review and seeking the views of the new Chairman when appointed.

Danuta Gray,
Interim Chairman

Corporate governance

Board of Directors

Chairman

Danuta Gray
Interim Chairman

Appointed:
September 2014

Board Committee membership:
C R

Relevant skills, strengths and experience:
Danuta brings significant leadership experience to the Board, having spent nine years as CEO of Telefónica O2 in Ireland. Her career in telecommunications spans 26 years, during which time she held numerous senior roles at BT Group PLC, gaining experience in marketing, customer service, communications, technology and sales, and leading and implementing change. She has also served as a Non-Executive Director of Irish Life & Permanent PLC and Aer Lingus Group PLC.

Principal external appointments:
- Non-Executive Director of Direct Line Insurance Group PLC
- Non-Executive Director and Chairman of the Remuneration Committee of Old Mutual PLC
- Non-Executive Director and Chairman of the Remuneration Committee of PageGroup PLC
- Member of the Defence Board of the Ministry of Defence

Executive Directors

Phillip Monks OBE
Chief Executive Officer

Appointed:
May 2009

Relevant skills, strengths and experience:
Phillip is the founding CEO of Aldermore and has a long-standing track record in championing small and medium-sized businesses and British economic growth. His banking career spans more than three decades, which includes establishing and serving as CEO of Europe Arab Bank PLC and over 20 years at Barclays PLC where he held a variety of senior corporate and private banking roles, including CEO of Gerrard Investment Management Limited, Managing Director of Barclays Corporate Banking in London, the Midlands and South East, and Head of Barclays Private Bank in Geneva. In June 2016, Phillip was awarded an OBE for his services to banking.

Principal external appointments:
- Member of the FCA Smaller Business Practitioner Panel

James Mack
Chief Financial Officer

Appointed:
September 2013[1]

Relevant skills, strengths and experience:
James brings significant financial experience to the Board, having spent six years at Skipton Building Society in capital markets, finance and audit, where he was instrumental in leading the merger with Scarborough Building Society. James began his career with KPMG LLP where he spent 11 years in the firm's financial services audit practice and he has also been Acting CFO of the Co-operative Banking Group Limited.

Principal external appointments:
- None

[1] Appointed as a Director of Aldermore Bank PLC in June 2013.

Non-Executive Directors

John Hitchins
Independent Non-Executive Director

Appointed:
May 2014

Board Committee membership:
A R

Relevant skills, strengths and experience:
John has extensive financial and audit experience having previously been a senior banking partner at PricewaterhouseCoopers LLP, specialising in bank auditing and advisory services for clients including Lloyds Banking Group PLC, the Bank of England, Bank of Ireland (UK) PLC, Barclays PLC and JP Morgan Chase. From 2001 to 2010, John was PwC's banking industry leader and from 2010 until his retirement led the PwC network's global IFRS technical group. John has also carried out a wide variety of advisory work for other banks and on behalf of the regulators covering corporate governance, high-level controls and other regulatory issues.

Principal external appointments:
- Trustee and member of the Governing Council of the Centre for the Study of Financial Innovation, a not-for-profit City-based think tank
- Deputy Chairman of the Financial Reporting Review Panel

Chris Patrick
Non-Executive Director

Appointed:
November 2016

Board Committee membership:
C R

Relevant skills, strengths and experience:
Chris brings over 25 years of financial services experience to the Board. He has been a Partner at AnaCap Financial Partners LLP since 2009 and heads the Risk and Liability Management Team, which assists the AnaCap Funds in funding, liquidity management, and monitoring key credit and market risks relating to their portfolio investments. Prior to joining AnaCap, Chris spent 10 years at Lehman Brothers International and prior to that, he held roles at Credit Suisse First Boston, Nomura International and Goldman Sachs.

Principal external appointments:
- Partner and Head of Risk and Liability Management at AnaCap Financial Partners LLP
- Member of the Supervisory Board of Credoma a.s.
- Director of Equa Holdings Limited

Robert Sharpe
Independent Non-Executive Director

Appointed:
June 2015

Board Committee membership:
A R

Relevant skills, strengths and experience:
Robert has over 35 years' experience in the banking sector, with a strong focus on mortgage lending. His previous executive roles include Group Operations Director and then CEO of Portman Building Society, where he led the merger with Nationwide Building Society, and CEO, Mortgages at Bank of Ireland (UK) PLC. In 2008, he joined West Bromwich Building Society as CEO to chart and implement its rescue plan. Robert is an experienced Non-Executive Director with previous appointments including United Arab Bank PJSC, National Bank of Oman SAOG and George Wimpey PLC.

Principal external appointments:
- Chairman of Al Rayan Bank PLC
- Chairman of Bank of Ireland (UK) PLC
- Executive Chairman of Stonehaven UK Limited
- Chairman of Honeycomb Investment Trust PLC

Non-Executive Directors continued

Peter Shaw

Independent
Non-Executive Director

Appointed:
September 2014

Board Committee membership:
A C R R*

Relevant skills, strengths and experience:
Peter brings over 30 years' financial services experience having spent most of his career at The Royal Bank of Scotland PLC and National Westminster Bank PLC where he worked across a number of business areas including retail, SME, private banking, corporate banking, HR and risk. Peter spent many years in senior risk management roles including COO of the risk function at Group Head Office in the UK and CRO for various group businesses within RBS NatWest. In addition, Peter served as Interim CRO at the Co-operative Banking Group Limited.

Principal external appointments:

- Non-Executive Director and Chairman of the Risk Committee of Bank of Ireland (UK) PLC
- Non-Executive Director of Willis Limited

Chris Stamper

Independent
Non-Executive Director

Appointed:
February 2014[2]

Board Committee membership:
A R

Relevant skills, strengths and experience:
Chris has 35 years' experience in the asset finance arena, most latterly as Director and CEO of ING Lease (UK) Limited. He is a founding Governor of the Leasing Foundation and was Director of the Finance and Leasing Association and a former Chairman of their Asset Finance Division. Prior to this, Chris held senior management roles at Abbey National PLC, where he was responsible for five business units focused on the SME market, and was the Managing Director of Lombard Sales Finance where he spent 21 years.

Principal external appointments:

- None

[2] Appointed as a Director of Aldermore Bank PLC in May 2013.

Key

- A Member of the Audit Committee
- C Member of the Corporate Governance and Nomination Committee
- R Member of the Remuneration Committee
- R Member of the Risk Committee
- * Denotes Committee Chair

Cathy Turner

Independent
Non-Executive Director

Appointed:
May 2014

Board Committee membership:
C R*

Relevant skills, strengths and experience:
Cathy has held a number of banking roles during her career, including Chief Administrative Officer at Lloyds Banking Group PLC and Group HR Director at Barclays PLC, where she was responsible for HR, strategy, corporate affairs, brand and marketing. She was also Director of Investor Relations at Barclays for four years. Formerly, Cathy worked in consultancy with Deloitte & Touche LLP, Ernst & Young LLP and Watson Wyatt Worldwide, Inc managing client relationships with a particular focus on compensation and benefits.

Principal external appointments:

- Non-Executive Director and Chairman of the Remuneration Committee of Countrywide PLC
- Non-Executive Director and Chairman of the Remuneration Committee of Old Mutual Wealth Management Limited
- Partner of Manchester Square Partners LLP
- Trustee of the Gurkha Welfare Trust
- Honorary Fellow of UNICEF UK

Company Secretary

Rachel Spencer

Company Secretary

Appointed:
February 2015

Relevant experience:
Rachel has over 25 years' listed company experience. She was the Deputy Company Secretary at Invensys PLC from 1999 until 2014 on the conclusion of its acquisition by Schneider Electric SA. She was previously with BTR PLC having joined as a trainee chartered secretary. She is a Fellow of the Institute of Chartered Secretaries and Administrators.

Responsibilities:
Rachel acts as secretary to the Board and its Committees and is accountable to the Board (through the Chairman) on all corporate governance matters.

Board membership changes during the year and to the date of this report:

- Peter Cartwright resigned as a Non-Executive Director with effect from 18 April 2016.
- Neil Cochrane resigned as a Non-Executive Director with effect from 14 October 2016.
- Chris Patrick was appointed as a Non-Executive Director on 21 November 2016.
- Glyn Jones resigned as Chairman with effect from 6 February 2017.
- Danuta Gray was appointed as Interim Chairman with effect from 7 February 2017. Danuta held the role of Senior Independent Director throughout 2016 and will resume this position on the appointment of a new Chairman.

Corporate governance

Executive Committee

Phillip Monks, Chief Executive Officer, and James Mack, Chief Financial Officer, are both members of the Group's Executive Committee. Their biographies can be found on page 42.

Dana Cuffe
Chief Operating Officer

Joined the Group:
May 2016

Relevant skills, strengths and experience:
Dana has over 30 years' experience in financial services and, prior to joining Aldermore, served as Senior Vice President and Chief Information Officer for RenaissanceRe Holdings Limited in Bermuda and was Head of Operations in Ireland. Prior to that, he spent three years as Chief Information Officer of Egg PLC, taking the organisation through an IPO and growing the customer base to over three million. Dana has also held senior IT positions in the UK, US and Australia with Credit Suisse First Boston, Global Asset Management, Citibank N.A. and Bank of America.

Responsibilities:
Dana is responsible for Technology, Group Services and Operations, Strategy, Strategic Propositions, Marketing and Digital.

Carl D'Ammassa
Group Managing Director – Business Finance

Joined the Group:
October 2013

Relevant skills, strengths and experience:
Carl has spent a number of years in the asset finance industry. Having started his financial services career at GE Capital, he held various financial, operational and general management positions in GE's Equipment Finance, Equipment Services and Restructuring divisions, including the post of CEO of the vehicle rental, plant hire and key leasing businesses. Prior to joining Aldermore, he was the Managing Director of Hitachi Capital Business Finance. Throughout his career, Carl has gained experience in challenging turnaround and transformational situations leading significant sales, operational and process improvements.

Responsibilities:
Carl is responsible for the management of the Group's lending activity through the Business Finance Division, which comprises the Asset Finance and Invoice Finance business lines.

Rob Divall
Group HR Director

Joined the Group:
September 2016

Relevant skills, strengths and experience:
Rob joined Aldermore from the Board of AdviserPlus Business Solutions Limited, a leading provider of HR managed services, where he led strategy and product development and played a key commercial role in the growth of the company through to its eventual acquisition goal. Prior to this, Rob held a variety of HR leadership positions in his eight years with Lloyds Banking Group PLC. Before Lloyds, he worked with Accenture PLC leading change programmes within the HR outsourcing division, having started the first decade of his career in retail where he held a number of senior HR and commercial roles in The Big Food Group PLC and Boots the Chemists Limited.

Responsibilities:
Rob is responsible for the Group HR function and the delivery of the people elements of the Group's strategy and performance.

Charles Haresnape[1]
Group Managing Director – Mortgages

Joined the Group:
January 2011

Relevant skills, strengths and experience:
Charles has a deep knowledge of the mortgages industry, having worked for a number of household names in the banking and building society sectors, including Nationwide Building Society and HBOS PLC. Charles was Senior Executive, Mortgage Sales and Acquisitions at Nationwide Building Society and Managing Director, Intermediary Mortgages at HBOS PLC. In addition, he has previously held roles within The Royal Bank of Scotland Group PLC where he was responsible for intermediary mortgage lending, and NatWest's branch mortgage sales force. Prior to joining Aldermore, Charles was Group Mortgage Services Director at Connells Limited, one of the UK's largest estate agency groups.

Responsibilities:
Charles is responsible for the management of the Mortgages Division, which comprises Residential Mortgages, Commercial Mortgages and Buy-to-Let business lines.

Christine Palmer
Chief Risk Officer

Joined the Group:
April 2016

Relevant skills, strengths and experience:
Christine has over 28 years' experience in risk management, corporate and commercial banking, having held roles at ING Bank N.V., where she spent eight years across London and Amsterdam, Ernst & Young LLP and The Royal Bank of Scotland Group PLC. Her career at RBS spanned almost 14 years, during which time she held a number of senior positions in the Risk function including divisional chief risk officer and senior credit risk roles. She was most recently Global Head of Operational Risk and Director of Risk, Services.

Responsibilities:
Christine is responsible for Risk across the Group which includes credit, operational, compliance, conduct and financial crime risk, as well as capital and liquidity risks.

Executive Committee responsibilities

The role of the Executive Committee is to assist the Chief Executive Officer in the performance of his duties relating to the day-to-day operation of the Group, including the:

- development and implementation of strategy, operational plans, policies, procedures and budgets
- monitoring of operating and financial performance
- prioritisation and allocation of resources
- monitoring of competitive forces in each area of operation
- design and embedding of the Risk Management Framework
- monitoring of adherence to risk appetite statements
- assessment and control of principal risks within the Group

[1] Charles is leaving the Group in 2017. A search is underway for his replacement.

Corporate governance structure

Board and Committee structure

The Board has delegated a number of its responsibilities to Board Committees, which utilise the expertise and experience of their members to examine subjects in detail and make recommendations to the Board where required. This delegation allows the Board to focus more of its time on strategic and other broader matters. The Chairs of the Board Committees provide the Board with a verbal update on matters discussed at each meeting, and Board Committee minutes are made available to the whole Board through a secure online system.

In addition to the Board Committees noted on the diagram below, the Board has established two further standing committees:

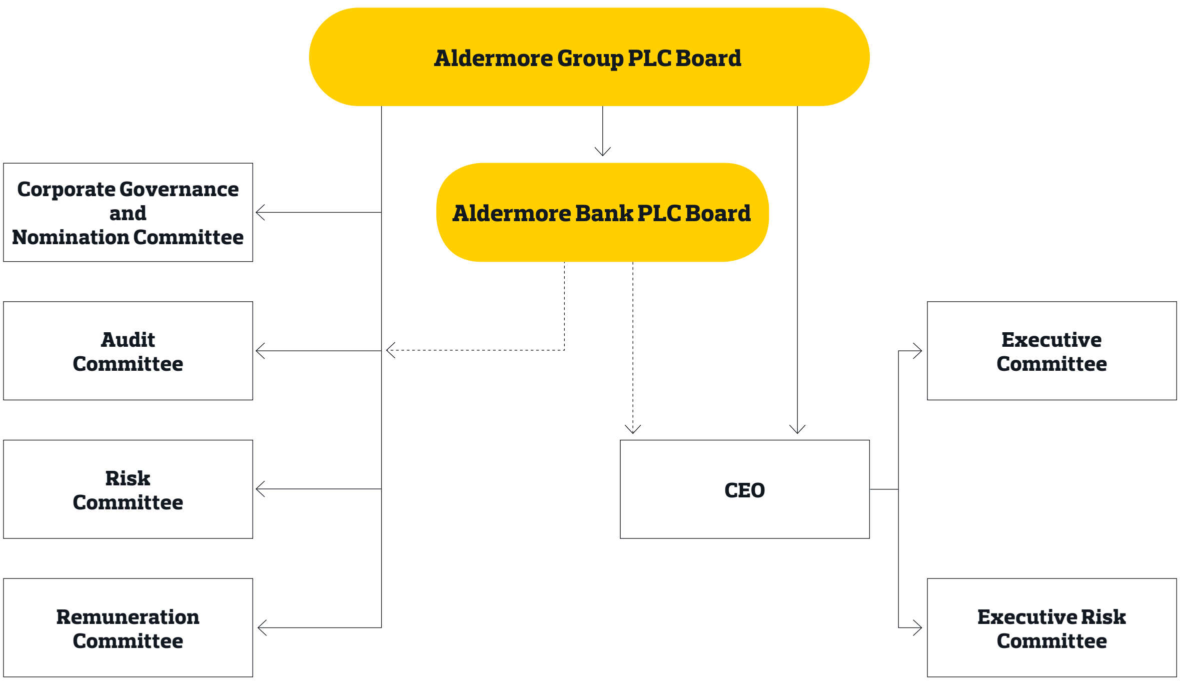
- The General Purpose Committee, comprising the two Executive Directors, for the purpose of approving routine business matters such as powers of attorney, changes to bank mandates and the execution of agreements which have already been approved in principle by the Board.
- The Disclosure Committee, comprising the two Executive Directors and the General Counsel, for the purpose of maintaining procedures, systems and controls for the identification and disclosure of market and price sensitive information.

All Board Committees have written terms of reference (available on the Company's investor website) which set out their authority, and the minutes of all meetings of these Committees are made available to the Board.

Responsibility for the day-to-day management of the Group is delegated to the CEO, who has established a structure of two executive committees, supported by a number of sub-committees, which oversee the execution of the strategy agreed by the Board, and performance and risk issues. The executive committees and their sub-committees each have their own terms of reference.

Aldermore Bank PLC ("the Bank")
The Bank is a wholly owned operating subsidiary of the Company and it transacts the Group's banking business. It is authorised by the PRA and regulated by the FCA and the PRA. The Board of the Bank mirrors that of the Company and comprises the same Directors. The Bank Board holds separate Board meetings immediately following the meetings of the Company's Board.

Governance structure and delegated authorities



Corporate governance

The Board – roles and processes

The Board

The Board is collectively responsible to shareholders for promoting the long-term success of the Group by directing and supervising the Group's affairs to create sustainable shareholder value. In setting the Group's strategy and related risk appetite, it also takes account of its obligations to other stakeholders including customers, employees, suppliers and the community in which it operates, as well as the regulatory obligations of the Bank, its principal banking subsidiary.

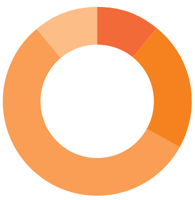
The Chairman leads the Board in its role to provide executive management with entrepreneurial direction, whilst the day-to-day management of the Group and operational matters are delegated to the CEO. The separation of duties between the Chairman and CEO is formally documented. The CEO is supported by his senior management team (the "Executive Committee"). Further details about the Executive Committee can be found on page 44, whilst further information about the role and responsibilities of each Board member can be found on the next page.

The Board's principal duties are set out in a formal schedule of matters reserved for its decision, as summarised on page 48. This schedule is reviewed annually and is available at www.investors.aldermore.co.uk

The Group Corporate Governance Framework, which is reviewed annually by the Board, sets out in detail the way the Group is governed.

[1] Danuta Gray acted as Senior Independent Director throughout 2016. She was appointed as Interim Chairman with effect from 7 February 2017 pending the appointment of a new Chairman.

Board structure
(as at 1 March 2017)

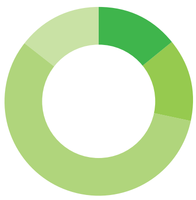


	%
Interim Chairman	11
Executive Directors	22
Independent Non-Executive Directors	56
Non-Executive Directors	11

Gender split of Directors
(as at 1 March 2017)

	%
Female	22
Male	78

Non-Executive Director tenure
(as at 1 March 2017)



	%
0–1 year	14
1–2 years	14
2–3 years	58
3–4 years	14

Chairman

- Leads the Board and ensures its effectiveness in all areas
- Sets the Board's agenda, with support from the CEO and the Company Secretary
- Promotes the highest standards of corporate governance throughout the Group
- Facilitates the effective contribution of Non-Executive Directors and a constructive relationship between Executive Directors and Non-Executive Directors
- Ensures that Directors receive timely and relevant information to support sound decision-making
- Responsible for induction, training and development of Directors
- Leads the development of the Group's culture
- Ensures effective communication with shareholders

Chief Executive Officer

- Responsible for the day-to-day management of the Group within the delegated authority and risk appetite approved by the Board
- Recommends the Group's strategy and leads the executive management team in the execution of the strategy approved by the Board
- Ensures the Group's culture is embedded in the business
- Leads the relationship with institutional shareholders and ensures that timely and accurate information is disclosed to the market as appropriate

Chief Financial Officer

- Manages the Group's financial affairs and supports the CEO in the management of the business
- Specifically manages statutory, monthly performance and regulatory reporting; and balance sheet and liquidity management

Senior Independent Director

- Acts as a sounding board for other Non-Executive Directors and the Chairman
- Chairs the Corporate Governance and Nomination Committee when it is considering succession to the role of Chairman of the Board
- Conducts the Chairman's annual performance evaluation, feeding in views from the Non-Executive Directors
- Attends meetings with major shareholders to understand their key issues and concerns, and is available to shareholders if they have concerns which contact through the normal channels has failed to resolve or is inappropriate

Non-Executive Directors[1]

- Provide independent and constructive challenge of the Executive Directors, including to help develop proposals on strategy
- Scrutinise the delivery of the strategy within the risk and control framework set by the Board
- Satisfy themselves on the integrity of financial reporting and the robustness of systems and controls
- Determine Executive Director remuneration

Company Secretary

- Provides key support and acts as a first point of contact for the Chairman and Non-Executive Directors
- Facilitates effective information flows between the Board and its Committees, and between executive management and the Board
- Keeps the Board updated on developments in corporate governance
- Facilitates induction of new Non-Executive Directors and training
- Acts as Secretary to the Board and Board Committees

[1] This includes one Non-Executive Director proposed by the Principal Shareholders under the Relationship Agreement.

Corporate governance

The Board – roles and processes continued

Board meetings

The Board held nine scheduled Board meetings, one strategy workshop and four additional ad hoc Board meetings in 2016. Two of the ad hoc meetings were called in order to analyse the Q3 forecast in greater detail in light of the uncertain economic outlook following the UK vote to leave the European Union, whilst other matters discussed at the ad hoc meetings included a substantial new contract and the appointment of the new external auditor following a tender process.

Attendance at scheduled Board and Committee meetings is set out below. There are occasions when a Director may be unable to participate in a meeting and, if this is the case, they are encouraged to provide comments to the Chairman on key items of business in advance of the relevant meeting, so that their views can be shared at the meeting and their opinions taken into account during discussions.

In addition to the meeting programme, Directors meet informally during the year enabling them to discuss sensitive and key matters in more depth.

Both the Board and its Committees have a rolling annual programme which aligns to the schedule of matters reserved for the Board and the terms of reference of each Committee. The agendas and time allocation for Board meetings are put together by the Chairman, assisted by the CEO and Company Secretary, based on the annual programme, actions arising from previous meetings and key business priorities. A similar process is followed with the Chair of each Board Committee. The Board and Committee agendas include a closed session at the end of meetings from time to time to enable the Chairman/Committee Chair to meet privately with the Non-Executive Directors without management present.

The Board monitors the performance of the Group against the approved strategy and annual business plan, and within the agreed risk appetite, through the following regular reports:

- An update from the CEO on market, customer and strategic developments.
- A business performance report which gives a holistic view of the Group's performance, and includes:
  - a report from the CFO on the financial results of the Group as a whole, as well as an investor relations update and review of various prudential regulatory matters;
  - a briefing from the Chief Risk Officer on key emerging risks, risk appetite and regulatory developments;
  - an update from the Chief Operating Officer on IT, operational and transformation matters, and strategic change projects; and
  - reports from the Managing Directors of the businesses on the business performance and related key issues, and an overview of the competitive landscape.

Key matters reserved for the Board

- Strategy
- Corporate and capital structure
- Financial reporting and controls
- Internal controls and risk management
- Material contracts
- Board membership and other appointments
- Remuneration policy
- Corporate governance matters

2016 Board and Committee attendance at scheduled meetings

Attendance	Board	Corporate Governance and Nomination Committee	Audit Committee	Risk Committee	Remuneration Committee
Danuta Gray	9/9	2/2	–	–	4/4
Glyn Jones	9/9	2/2	–	–	4/4
Phillip Monks	9/9	–	–	–	–
James Mack	8/9[4]	–	–	–	–
Peter Cartwright[1]	3/3	1/1	–	2/2[5]	–
Neil Cochrane[2]	6/7	0/0[6]	–	3/3[6]	–
John Hitchins	9/9	–	7/7	7/7	–
Chris Patrick[3]	1/1	0/0	–	0/0	–
Robert Sharpe	9/9	–	7/7	7/7	–
Peter Shaw	9/9	2/2	7/7	7/7	4/4
Chris Stamper	8/9[7]	–	7/7	6/7[7]	–
Cathy Turner	9/9	2/2	–	–	4/4

[1] Resigned on 18 April 2016. [2] Resigned on 14 October 2016. [3] Appointed on 21 November 2016. [4] Unable to attend as representing the CEO at a PRA seminar. [5] Includes meetings attended by Neil Cochrane in his capacity as alternate to Peter Cartwright. [6] Appointed as a member on 10 May 2016, and ceased to be a member on 14 October 2016. [7] Absence due to long-standing holiday arrangements.

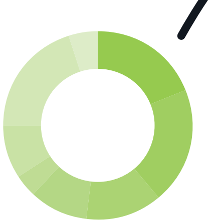
Strategy sessions

The Board is responsible for establishing the Group's strategy and plays a key role in challenging management in developing the strategic plan and objectives.

Two Board strategy workshops are generally held every year where the CEO, with members of his Executive Committee, present their views of the market and proposed plans, including new initiatives, to be probed and tested by the Non-Executive Directors. The range of experience and expertise that the Non-Executive Directors are able to bring to the debate, along with their independent oversight, is key to building a sustainable strategy. The focus of discussions is not only on how the strategy should evolve, but also on ensuring that the Group has the appropriate resources, skills and competencies to deliver the chosen strategy.

However, given the rapidly changing market and regulatory environment in which the Group operates, the strategy has to be subject to continuous review and, as such, the executive management provides the Board with regular updates on key strategic initiatives as they progress.

Time spent in 2016



	%
Business performance	19
Financial matters and investor relations	20
Governance	13
IT and operations	10
Regulatory matters	4
Risk management	9
Strategy	20
Other	5

Key topics discussed at Board and strategy meetings in 2016

Key:
- Reviewed
- Approved

Topic	Activity	Action
Business performance	Regular reports from the CEO, CFO and other members of the executive team (as detailed on page 48)	Reviewed
	Deep-dive into the Group's funding strategy	Reviewed
Financial matters and investor relations	Publicly released financial results, including going concern and viability statements and dividend policy	Approved
	Quarterly forecasts	Reviewed
	2017 annual budget	Approved
	Issuance of Tier 2 Loan Notes	Approved
Governance	Changes to the Board and composition of the Board Committees	Approved
	Annual Report and Accounts and Notice of AGM, as well as related matters such as the annual reappointment of both the Directors and the external auditor and the Directors' Remuneration Policy	Approved
	Outcome of the annual review of the effectiveness of the Board and progress against key actions	Reviewed
	Changes to the Group Corporate Governance Framework	Approved
	Annual review of disclosure controls and procedures	Approved
	Appointment of the new external auditor with effect from the 2017 AGM	Approved
	2017 annual programme	Approved
IT and operations	New contracts outside of the CEO's delegated authority	Approved
	Property strategy and an amendment to a property lease	Approved
	Key insurance renewals, including Cyber and Directors' and Officers'	Approved
Regulatory matters	Updates on the implementation of new regulatory initiatives including the Senior Managers and Certification Regime, EU Market Abuse Regulation and the Slavery Act	Reviewed
	Potential impact of future regulatory changes such as changes to credit risk weights	Reviewed
	Outcome of the processes to confirm that the Group has adequate capital and liquidity	Approved
Risk management	Regular reports from the CRO on key emerging risks, risk appetite and regulatory developments	Reviewed
	Annual review of the Reputational Risk Policy	Approved
	Changes to the Risk Appetite Framework and associated risk metrics	Approved
	2016 risk strategy	Approved
	Annual review of the effectiveness of systems of risk management and internal controls	Approved
Strategy	Quarterly presentations by the Company's joint brokers	Reviewed
	Strategic review of the Group's brand	Approved
	Updates on strategic initiatives agreed in 2015 and new strategic initiatives, including updates on digital matters	Reviewed
Other	Updates on culture and 2015 Best Companies results	Reviewed

Corporate governance

The Board – roles and processes continued

Appointments

The Corporate Governance and Nomination Committee (the "Nomination Committee") is responsible for making recommendations to the Board regarding the appointment of new Directors.

One new appointment was made to the Board in 2016 (Chris Patrick), whilst the Nomination Committee also oversaw changes to the composition of the Board Committees which arose following the resignations of Peter Cartwright and Neil Cochrane. Chris, Peter and Neil were all appointed to the Board in accordance with the Relationship Agreement between the Group and its Principal Shareholders (further information can be found on page 59). Under the Relationship Agreement, the Principal Shareholders are entitled to appoint up to two Board Directors and a member of each of the Risk Committee and the Nomination Committee. Consequently, when Peter stepped down from the Board in April 2016, the Nomination Committee considered and recommended to the Board that Neil replace Peter as a member of these Committees in line with the wishes of the Principal Shareholders. Following Neil's resignation from the Board in October 2016, the Principal Shareholders informed the Company of their intention to appoint Chris as their sole representative on the Board and as a member of the Risk and Nomination Committees. The Nomination Committee considered the proposed appointments and agreed to recommend them to the Board, subject to the completion of fitness and propriety tests. As part of this process, Chris met with each of the Committee Chairs and the Senior Independent Director to assess his competence and capability, whilst various references were sought and checks completed in order to verify his educational, employment, criminal and credit history. Regulatory approval was not required for Chris' appointment.

Induction of Directors

All Directors receive a comprehensive induction on appointment to enable their effective contribution to the Board as early as possible. Induction programmes are tailored to the needs of the new Director. The Chairman discusses requirements with the new Director, which are facilitated by the Company Secretary. The programme will typically include one-to-one meetings with business and functional heads; site visits; and access through the Board portal to past Board packs and an induction pack containing relevant Group policies and procedures. Details of Chris Patrick's

Chris Patrick's induction programme

Business Divisions

- Overview of the strategy and vision
- Understanding of the history of the businesses
- Management's views on the challenges, opportunities and competitive environment
- Understanding of the financial and cultural dynamics and the key risks
- Meeting and engaging with employees

Corporate Governance and Legal

- Introduction to the Group Corporate Governance Framework, including the matters reserved for the Board and the Committee structure
- Overview of Board processes and directors' duties
- Discussion on the Group's legal risks
- Overview of the legal and regulatory requirements for listed companies

IT and Operations

- Overview of the team structure and scope of the COO function
- Discussion on how the function supports the Group's strategic plan
- Introduction to project governance processes within the function
- Overview of major transformation projects, the refresh of the Group's brand and marketing plans for 2017

People and Culture

- Overview of the HR strategic plan and key priorities for the HR function
- Board and executive succession planning
- Overview of the Group's remuneration policy
- Discussion on setting and measuring the Group's culture

Risk and Regulatory

- Introduction to the Risk Management and Risk Appetite Frameworks
- Overview of the Senior Managers and Certification Regime and how it operates within the Group
- Understanding of the market abuse and inside information regimes

induction programme, which will be implemented during 2017, are set out at the bottom of page 50.

Diversity

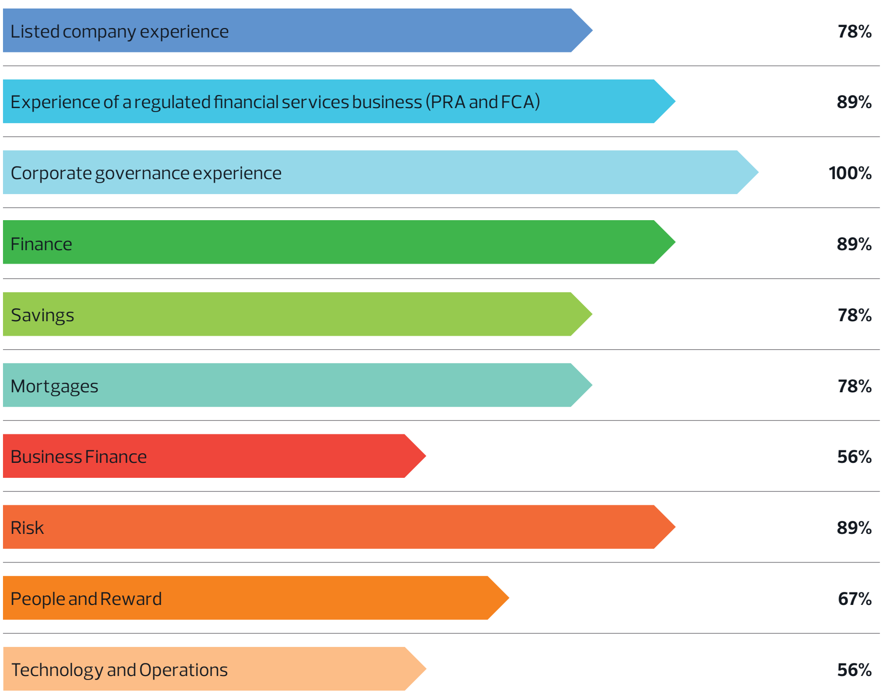
The Board embraces the benefits of diversity in the boardroom and believes that it generates effective challenge and decision-making. It strives for diversity in the broadest sense – female representation is just one of the factors that is taken into account and all Board appointments are made on merit against a defined job specification. The Company does not therefore consider it appropriate to set a measurable target for gender representation on its Board. Female membership of the Board currently stands at 22%.

The Board adopted a Board Diversity Policy in November 2015, and the Nomination Committee has since reconfirmed that no amendments to this Policy are required at the current time. However, the Policy will be revisited following the appointment of a new Chairman and taking into account developments arising from the Hampton-Alexander Review. The Policy is available at www.investors.aldermore.co.uk

Skills, knowledge and experience

As previously mentioned, the Board values all aspects of diversity and recognises the benefit of maintaining a balance of skills, experience and knowledge. During 2015, the Nomination Committee oversaw an exercise to evaluate the skills and experience on the Board. This was based on a self-assessment completed by each Director. The matrix which was compiled as a result has been kept under review in 2016. It was updated to reflect the changes to the composition of the Board during the year and, as a result, the Nomination Committee has been able to satisfy itself that the mix of skills and experience on the Board is appropriate to challenge management and support the Group's strategy. At the time of the 2015 review, some areas were identified where, in the medium term, the balance of skills, knowledge and experience could be strengthened. These remain relevant and will be taken into consideration in any future search for new Non-Executive Directors.

Self-assessment of skills and experience – % of Directors with at least a good working knowledge



Corporate governance

The Board – roles and processes continued

Election and re-election

The Code requires that all Directors retire and offer themselves for election at the first AGM following their appointment, and for re-election on an annual basis thereafter.

Ahead of the re-election of the Non-Executive Directors being recommended to shareholders, the Nomination Committee assesses the performance, time commitments and independence of each Non-Executive Director and makes a recommendation to the Board in this regard. In addition, the outcome of the appraisals of the Executive Directors (as set out on page 56) is considered. These assessments took place over January and February 2017 and, based on these factors (described further in the paragraphs that follow), as well as the balance of skills, knowledge and experience on the Board as a whole, the Board approved the recommendation that each Director should be proposed for election/re-election at the 2017 AGM. Further information about the Directors, including their experience, is set out on pages 42 and 43.

The Principal Shareholders are classed as a "controlling shareholder" of the Company under the Listing Rules. As a result, the Independent Non-Executive Directors of the Company must be elected or re-elected by both a majority of the votes cast by all of the Company's shareholders and a majority of the votes cast by the Company's independent shareholders (being all of the Company's shareholders other than the controlling shareholder). The outcome of both of these votes will be announced following the 2017 AGM.

Director performance evaluations

Details of the Director performance evaluation process are set out on page 56. The outcome of the evaluations concluded that each Director continues to be effective and to demonstrate commitment to their role.

Time commitment and independence

The Nomination Committee reviewed the time commitment to the Company demonstrated by each of the Non-Executive Directors and was satisfied that this was both in line with the requirement set out in their letters of appointment, and sufficient to discharge their duties. The external directorships and other commitments of the Non-Executive Directors were also taken into account in making this assessment.

Independence of the Non-Executive Directors is assessed by the Nomination Committee on an annual basis against the criteria set out in the Code, which require directors to be independent in character and judgement, and free from any relationships or circumstances which could affect that judgement. Factors taken into account in this assessment include length of tenure and any potential conflicts recorded in the Company's Register of Directors' Conflicts. The Nomination Committee was satisfied that there had not been any changes in circumstance which would impact on the previous assessment that all Non-Executive Directors, with the exception of the Director who represents the Principal Shareholders, were deemed to be independent.

Separately, on the basis that Danuta Gray will be acting as Chairman in an interim capacity for a limited period only, the Board continue to regard her as independent.

Shareholder-representative Director

Chris Patrick has been appointed to the Board to represent the interests of the Principal Shareholders, and is not therefore considered to be independent under the Code. Notwithstanding that he is not independent, the Nomination Committee confirmed that it was satisfied that he should be recommended for re-election at the 2017 AGM.

Conflicts of interest

The Board has procedures in place to deal with potential conflicts of interest, which are governed by both company law and the Company's Articles of Association. All Directors are required to declare any interests that could give rise to a conflict of interest with the Group, either on appointment or when they arise. Under the Company's Articles, the Board is permitted to authorise such conflicts and to impose any conditions on that authorisation that it considers to be necessary, for example to leave Board meetings when certain matters are discussed. All authorisations are recorded in the Board minutes, and entered into the Register of Directors' Conflicts.

The Nomination Committee has provided guidance to the Board on the declaration of interests which cannot reasonably be regarded as likely to give rise to a conflict of interest. In addition, the Nomination Committee undertakes an annual review of the Register of Directors' Conflicts to ensure that there have not been any changes in circumstances that would require the Board to revisit any previous authorisation that it has granted, or its view of the Directors' independence.

During the year, the Nomination Committee considered the prospective appointment of Robert Sharpe as Chairman of Bank of Ireland (UK) PLC. The proposal was considered from the perspective of any potential business conflict of interest; time commitment pressures which would prevent Robert from discharging his role with the Company; and the cross-directorship which would arise given that Peter Shaw was also a Director of Bank of Ireland (UK) PLC. Having taken into account a number of factors, including the character and judgement of both individuals, it was agreed to approve any potential conflict of interest associated with the proposed appointment.

Succession planning

Non-Executive Directors

The Nomination Committee reviewed succession planning for the Non-Executive Directors during the year. Whilst acknowledging that succession planning was key to the sustainability of the Board, the Nomination Committee was also cognisant that the majority of the Non-Executive Directors had been appointed in 2014 when a Board was formed which would be suitable to lead the Company in a public environment. The tenure of these Directors was therefore less than three years. During the year, tenure was discussed with the longest-serving Non-Executive Director (less than four years on the Board), who had confirmed that he had no specific retirement date in mind. In light of these relatively short tenures, the Nomination Committee confirmed that the previously agreed principles on which future succession planning should be based remained appropriate.

Chairman

To ensure that an effective Chairman was in place at all times to lead the Board, the Nomination Committee agreed a Chairman Succession Framework in 2015. The Framework outlined the approach that would be taken when the time came to search for a new Chairman, and confirmed that the Senior Independent Director would lead the process. As a result, following the resignation of Glyn Jones as Chairman during the year, the Nomination Committee was able to act quickly to put the Framework into action. Good progress has been made with the search, and a fuller update is provided in the Chair's introductory letter to the Nomination Committee Report on page 60.

Executive positions

Succession planning for the Executive Directors was considered by the Nomination Committee during the year, whilst the Executive Committee was strengthened through the appointment of three new members.

The Executive Committee has continued to build on work undertaken in 2015 to develop a pipeline of potential successors to executive positions below Board level. This is an iterative process which aims to assess (and regularly re-assess) the current capabilities and future potential of both the direct reports of the Executive Committee and their teams. This process is key to both the identification of employees who would benefit from or require development plans to further build on their potential, and as a way of highlighting gaps where consideration should be given to recruiting potential successors. As a result, efforts are being focused on increasing the number of employees who are moved into roles that will enable them to broaden their skills and experience, with a view to stepping up in to a more senior role in due course. The introduction of the Senior Managers and Certification Regime during 2016 has also provided additional impetus to the succession planning process as individual development plans are now required under the regulations.

Corporate governance

The Board – roles and processes continued

Board support

All Directors have access to the advice and services of the Company Secretary, who ensures that Board procedures are complied with. In addition, Directors have access to independent and professional advice at the Company's expense.

Information flow to the Board

The Board's ability to discharge its duties is dependent on the quality of the information that it receives to support decision-making. Information should be accurate and clear, and provided on a timely basis.

Board papers

The Company Secretary takes responsibility for ensuring that the Board receives high-quality information and, to the extent possible, acts as a gateway to challenge any Board papers which require additional clarity. All ad hoc Board papers include an executive summary in a standard format which ensures that key information can be easily identified by the Directors, and that important points are sign-posted.

The format of the regular business performance report to the Board is reviewed regularly in order to ensure that it continues to provide the Board with a holistic view of the business as a whole, and that insight is provided rather than data.

Resources

A library of useful information has been made accessible to Directors through an online portal. This includes corporate information such as the business plan, corporate governance material, regulatory correspondence and technical updates.

Training and development

Training sessions for Directors on topics of relevance to the Board are organised periodically throughout the year to tie in with Board and Committee meetings.

In 2016, training sessions attended by the Board included sessions on the EU Market Abuse Regulation, and Committee-specific training on IFRS9 and hedge accounting (Audit Committee) and developments in the external market (Remuneration Committee). An invite to the Committee-specific training was extended to all Directors and the sessions were well attended by non-members. The training was led by either senior management or external advisers. In addition, Directors attended relevant external training sessions.

The Board values internal development sessions as an important way of engaging with key employees and familiarising themselves with the business. In order to hear the views of the wider employees first hand, the Board has continued with the 'Meet the Board' initiative introduced in 2015. In addition, the Audit Committee held a roundtable with members of the Group Internal Audit ("GIA") function. Further information on these events can be found on the next page.

A training log is maintained by the Company Secretary for each Director as evidence of continuous development.

A longlist of potential training sessions for 2017 is being drafted by the Company Secretary based on proposals raised by Directors through the Board evaluation process. Suggestions from advisers regarding upcoming areas of regulatory change will also be sought. The Company Secretary, the Chairman and Committee Chairs will discuss the proposals, which will broadly cover business-related and technical/regulatory items. As a result, a programme of quarterly Board training sessions supplemented by Committee-specific training will be finalised for 2017. The 'Meet the Board' and GIA roundtable events will also continue.

Meeting our employees

As part of internal development, the Board appreciates the opportunity to engage directly with employees. Set out below are two examples of how this has been achieved.

'Meet the Board' – Wilmslow

In 2016, the Directors visited one of the Group's key sites in Wilmslow (where the Mortgages and Financial Reporting teams are based) as part of an initiative to enable them to engage directly with employees across the business areas and central functions. This followed two similar events held during 2015 when the Directors visited the Group's Peterborough and Reading sites. The 'Meet the Board' event was held in an informal setting and was designed to be interactive, allowing the Directors to gain a deeper understanding of the business, how it operates and the challenges that staff face on a first-hand basis, as well as providing an insight to colleagues on the role of the Board. The event also provided a valuable opportunity for employees to share their ideas and suggestions with the Directors and to put forward questions about the vision and strategy for Aldermore, in order to promote transparency and employee engagement across the Group.

The 'Meet the Board' event was well received by both the Directors and the participating employees and will continue in 2017. In particular, the Directors welcomed the informal format of the event which was conducive to stimulating an open debate with colleagues. The feedback from employees was equally positive, with many expressing their appreciation for the Directors' interest, time and engagement, and commenting on the high quality of the discussions.

"It is excellent when we have Board meetings away from London as we get the chance to meet colleagues and hear what is going on with our customers. The enthusiasm from staff was very motivating, and you could sense the energy and pride in the room. The questions asked were wide ranging and all pertinent to our future business success. I enjoyed chatting to colleagues over lunch and was pleased to learn about how, as we grow, we are creating opportunities for new and different roles and the ability to learn in current jobs." **Cathy Turner, Independent Non-Executive Director**

"It was great to see the session attended by so many people. The questions asked were really topical and the Board did a great job at answering the questions, covering both the high-level outlook on topics as well as relating the answers back to people's day jobs and the customer outlook." **Employee from Financial Reporting**

"It was great to see and hear from each of the Board members. I felt that I got more of an insight as to what is going on within the wider Group and Financial Services in general. It is unusual to get an opportunity to meet and speak with Board members when working in this industry so it was great for us to be able to ask questions and get some really useful feedback." **Employee from Residential Mortgages**

Group Internal Audit Roundtable – Reading

In June 2016, a roundtable was held between members of the Audit Committee and the GIA team in response to a recommendation from the 2015 effectiveness review of the GIA function that it would be beneficial to enable Directors to have direct dialogue with the GIA team.

The session was an informal conversation with no fixed agenda, providing the GIA team with an opportunity to introduce themselves to the Audit Committee members and ask questions, including probing Directors for their views on current and horizon risks, their individual expertise and their expectations of the GIA team. The GIA team were also keen to understand the importance of their role in supporting the Audit Committee and the interaction between the GIA Director, the Audit Committee, the other Board Committees and the CEO.

"The roundtable was useful for both the Audit Committee members, who were able to meet and learn about the skills within the GIA team, and for the GIA team who gained an insight into the Audit Committee's role and responsibilities, its members and their views on key risks within the Group. The Directors had the opportunity to ask the GIA team questions about the work they perform, the challenges faced and areas where the team would benefit from Audit Committee support. This has had a positive cultural impact on the GIA team who felt that they gained insight which they had not experienced in previous roles, as well a unique opportunity to have their views heard at Board level. Further, it provided the team with a greater understanding as to why particular audits were required and the value of the GIA reports, as well as how the Group's governance structure operates." **GIA Director**

Corporate governance

The Board – roles and processes continued

Board and Committee effectiveness

The Board recognises the benefits that reviewing the effectiveness of its own performance and that of its Committees can bring, and is conscious that the actions needed to maintain effectiveness will develop over time as the Company, the Board and best practice evolve. Effectiveness is reviewed on an annual basis, and the Nomination Committee oversees this process. In 2016, the Board decided that the annual review would be conducted internally. The last external review was undertaken by Egon Zehnder in 2014 and, in line with the Code, it is anticipated that an external review will next take place in respect of 2017.

The 2016 process was agreed by the Nomination Committee and led by the Senior Independent Director (now the Interim Chairman) with support from the Company Secretary as required. The evaluation was taken forward by way of questionnaires which were issued to all Board and Committee members, and were supplemented by one-to-one meetings between each Director and the Interim Chairman which aimed to seek more context to the responses given. The results were collated and analysed by the Company Secretary, and the draft output was discussed with the Interim Chairman and, in relation to Committees, the relevant Committee Chairs. Finalised reports and action plans were presented and agreed by the Board and Committees. The output concluded that the Board and its Committees operated effectively during 2016. A summary of the outcomes is set out on the next page, together with a summary of the areas for development for 2017 and an update on the actions arising from the last effectiveness review. Information on the Committee reviews can be found in the reports from the individual Committees on pages 60 to 73 and page 90.

The Nomination Committee will oversee the implementation of the agreed action plan for the Board and interim updates will be assessed during the year. An update on progress against these actions will be reported in the 2017 Annual Report and Accounts.

Board and Committee effectiveness process

Director performance evaluations

In tandem with the process to review Board and Committee effectiveness, a similar process is followed to evaluate the continued effectiveness of the performance of the Non-Executive Directors.

In respect of the year under review, the Interim Chairman undertook a performance evaluation for each Independent Non-Executive Director, whilst the previous Chairman led the process for evaluating the performance of the Interim Chairman (who had acted as Senior Independent Director throughout 2016). An evaluation of the Chairman's performance would ordinarily also be undertaken, but this was not completed in 2016 given that the Chairman (Glyn Jones) had already tendered his resignation when the reviews were commenced. To support the evaluations, each Director completed an anonymous questionnaire to provide an assessment of the performance and effectiveness of each of the Independent Non-Executive Directors. The Interim Chairman also solicited verbal feedback from each of the Non-Executive Directors on an individual basis. The output from the performance evaluations is being discussed in one-to-one sessions between the Interim Chairman and each Non-Executive Director, and will identify any development needs in terms of ongoing training.

The performance of the Executive Directors was appraised by the previous Chairman (in the case of the CEO) or the CEO (in the case of the CFO) with input from other Directors. The outcome of the evaluations was reviewed by the Remuneration Committee as part of the process by which changes to salary and bonus outcomes were approved.

The evaluations concluded that each Director continues to be effective, demonstrates commitment to their role, and is able to allocate sufficient time to the Company to discharge their responsibilities effectively.

Overview of Board effectiveness review

2015/16 review

Update on key development areas in 2016

Continue to embed the recently implemented new template for Board papers

- Good progress has been made with the use of an agreed Board paper template to ensure papers focus on key issues and flag decisions to be made. Management information continues to be an area for further improvement as detailed below in "Key development areas in 2017."

Implement a more structured process to review the effectiveness of past decisions, and to apply lessons learned

- A structured process for the review of the effectiveness of past decisions has been introduced which monitors on a six-monthly basis items approved by the Board, including achievement of key milestones and evaluation of successes/lessons learned.

Maintain the focus on succession planning

- The approved Chairman Succession Framework served the Company well as the search process for the new Chairman could be initiated immediately.
- The Board has overseen the changes which the CEO has made to strengthen his executive team.
- Succession planning for key executive roles continues to be an area of focus as detailed below in "Key development areas in 2017."

Review the ongoing development of the Risk Management Framework to ensure appropriate behaviour is embedded into the risk culture

- The Risk Management Framework has continued to evolve, with risk appetite statements and risk metrics being revised and refreshed as appropriate.

Develop a comprehensive training programme to meet Directors' requirements

- A bespoke training programme on key regulatory and legislative matters was developed.
- Training sessions were held at Board and Committee meetings during the year, facilitated by external advisers where appropriate (further information is detailed on page 54).
- A similar approach is being adopted in formulating a training programme for 2017.

Schedule more informal time for the Board to spend together, and extend some of the meetings to ensure there is adequate time for discussion of all agenda items, in particular strategic issues

- A number of dinners following formal meetings were scheduled to enable Directors to continue discussion of material agenda items.
- An annual round-up of remuneration-related developments was organised by the Remuneration Committee which was presented over dinner by FIT Remuneration Consultants.
- Members have spent informal time with each other and colleagues in the business through the 'Meet the Board' events (see page 55 for more information).
- These events will continue to form part of the Board calendar in 2017.

2016/17 review

Key areas of strength

- Overall, the Board is considered to work very effectively, with an open and positive culture which encourages all to contribute, as well as challenge and support the executives equally.
- It is acknowledged that there is a good mixture of subject matter experts on the Board but who all contribute on business overall to create a well-balanced team.
- The Chairs of Board Committees are all recognised for their work throughout the year.

Key development areas in 2017

Chairman

- A key focus in the next year will be the introduction of the new Chairman and ensuring his/her transition is smooth.

Agendas and management information

- Responsibilities of Committees and Board are to be reviewed to ensure duties are delegated effectively, agendas are focused on appropriate matters, and overlap is eliminated.
- In structuring meetings, continuously balance the Board agenda between strategic development, risk management and delivery assurance.
- Presentation of management information in papers to be reviewed to avoid duplication across Board and Committee meetings, and to ensure papers are amended to reflect the different areas of focus by each forum.

Succession planning and induction

- Continue to develop executive succession plans for key roles to ensure there are robust plans in place, with a dedicated strategy session to be led by the Group HR Director.
- Monitoring of talent pipeline to continue through the Nomination Committee.
- Ensure that the induction for new Non-Executive Directors is refreshed.

Board composition

- Further assessment of the skills and experience on the Board to be addressed by the new Chairman, noting there may be some further enhancement of the Board in relation to digital technology.

Corporate governance

Relations with shareholders

Shareholder engagement calendar 2016

January 2016

Preparing materials for full-year results.

February 2016

Review of materials for full-year results.

March 2016

2015 full-year results presented to the market, followed by an investor roadshow led by the CEO and CFO.

May 2016

AGM with shareholders led by the Chairman. Shareholders were invited to vote on resolutions of the Company.

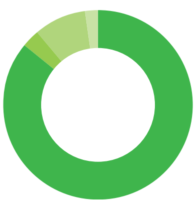
Q1 trading update was presented to the market.

Shareholder analysis

Set out below is analysis of the Company's shareholder base as at 31 December 2016. The shareholding is relatively concentrated amongst the top 10 shareholders, in particular as the Principal Shareholders hold 40.14% (discussed in more detail on page 59). Overall, the top 10 shareholders hold just under 70% of the total issued share capital.

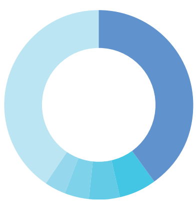
The majority of shareholders (86%) are based in the UK, particularly in the financial capital of London, with the remaining investors based primarily in the United States of America and in Europe. The primary investment style of the investor base is growth focused. This reflects the Group's growth strategy and an investor base that understands Aldermore's financial objectives.

Geographic
(% shares outstanding)



	%
UK	86
Europe	3
North America	9
Rest of World	2

Leading Shareholders
(% shares outstanding)



	%
Shareholder 1	40.1
Shareholder 2	6.3
Shareholder 3	5.5
Shareholder 4	4.0
Shareholder 5	3.7
Balance	40.4

Share register analysis as at 30 December 2016.

Investor relations

In 2016, the first full-year results as a listed company were presented to the market. A full investor engagement programme led by the CEO and CFO was carried out throughout the year with both holders and prospective holders. Additionally, a specific investor roadshow was run in relation to the £60m Tier 2 Notes issued in October 2016.

Investor meetings are normally undertaken by the CEO, CFO and the Director of Investor Relations. During the year, over 150 individual and group investor meetings were held covering topics such as business performance, competitive positioning, strategy and changes in the regulatory and political environment. The UK's vote to leave the European Union in June 2016 was one area of particular focus with investors in the year.

The Chairman and Senior Independent Director are also available to attend meetings with shareholders and address any significant concerns that shareholders may have. In particular during 2016, the Senior Independent Director (now Interim Chairman), was available to discuss the resignation of the Chairman, which was announced in November 2016.

The Group provides regular updates on its investor relations website at www.investors.aldermore.co.uk including its half-yearly financial results, reports and presentations, press releases, regulatory news, share price data and useful information for shareholders with regard to managing their shareholdings.

Information to the Board

The Chairman is responsible for ensuring effective communication with shareholders and the Board recognises the importance of constructively engaging with its shareholders. Feedback received from investors is regularly shared with Board members through the CFO's regular business performance report, which aids broader discussions on business matters and other relevant topics.

J.P. Morgan Cazenove and Royal Bank of Canada (RBC) act as joint brokers to the Company. They attend Board meetings on a quarterly basis to provide Directors with input on market conditions and investors' views. Outside of this formal

Key to activities:

- Full-year results
- Half-year results
- Trading update
- AGM
- Investor meetings

August 2016

Half-year Results were presented to the market.

September 2016

Investor roadshow of half-year results was led by the CEO and CFO, following the summer break. An investor roadshow was also undertaken ahead of the issuance of £60m Tier 2 Notes to the market in October 2016.

November 2016

Q3 trading update was presented to the market.

December 2016

Continued to engage with current and potential investors, with over 150 meetings held in the year.

programme, the views of the brokers are proactively sought on market developments including the regulatory and competitive environment.

During the year, the Board commissioned an independent perception audit of a number of the Company's leading institutional shareholders and sell-side analysts. Overall, whilst this demonstrated that the Company has a supportive investor base, there are a number of recommendations to further enhance communications and investor relations activity which will be an area of focus in 2017.

Principal Shareholders

The Principal Shareholders have an interest in the issued share capital of 40.14% and their relationship with the Company is governed by a Relationship Agreement which ensures that:

- the Company is capable of carrying out its business independently of the Principal Shareholders;
- transactions and arrangements with the Principal Shareholders (and their associates) are at arm's length and on normal commercial terms (subject to the rules on related party transactions in the Listing Rules); and
- the Principal Shareholders do not take any action that would have the effect of preventing the Company from complying with, or would circumvent the proper application of, the Listing Rules.

During the year, the Nomination Committee, in accordance with its duties, conducted a review of compliance with the terms of the Relationship Agreement and concluded that the Relationship Agreement is working effectively and that the Company is capable of carrying out its business independently of the Principal Shareholders.

The Company has adopted procedures which restrict Directors appointed by the Principal Shareholders from voting on matters where there are conflicts of interest and from using information obtained through their appointments.

Under the Relationship Agreement, as the Principal Shareholders still have an interest in more than 20% of the Company, they are entitled to appoint two Non-Executive Directors to the Board. During the year, Peter Cartwright and Neil Cochrane stepped down from the Board on 18 April 2016 and 14 October 2016 respectively. Currently, Chris Patrick, who was appointed on 21 November 2016, serves on the Board as the only Non-Executive Director appointed by the Principal Shareholders and will stand for election by shareholders at the 2017 AGM.

Annual General Meeting

The 2017 AGM will be held at 11.00am on 16 May 2017 at the offices of Linklaters LLP, 1 Silk Street, London, EC2Y 8HQ. The Notice of AGM, together with an explanation of the items of business to be discussed at the meeting, will be posted to shareholders and made available at www.investors.aldermore.co.uk. A resolution will be proposed at the 2017 AGM to amend the Company's Articles of Association so that future AGMs may be held electronically.

All members of the Board will be in attendance at the 2017 AGM which will provide an opportunity to engage with shareholders on the key issues facing the Group and respond to any questions shareholders may have. All the Directors will be available after the meeting to meet shareholders on an informal basis. Voting at the 2017 AGM will be conducted by a poll and the results will be announced to the market and made available on the Group's website as soon as practicable following the meeting.

Corporate governance

Corporate Governance and Nomination Committee Report

Nomination Committee at a glance

- The Nomination Committee is composed of a majority of Independent Non-Executive Directors in line with Code requirements and is chaired by the Company Chairman:
  - Danuta Gray (Chair), Interim Chairman[1]
  - Chris Patrick, Non-Executive Director
  - Peter Shaw, Independent Non-Executive Director
  - Cathy Turner, Independent Non-Executive Director
- Glyn Jones and Peter Cartwright were also members of the Nomination Committee until their resignations from the Board with effect from 6 February 2017 and 18 April 2016 respectively. Neil Cochrane served as a member of the Nomination Committee between 10 May 2016 and 14 October 2016.
- Regular attendees at meetings of the Nomination Committee include the CEO and Company Secretary.
- The Nomination Committee's key roles are to oversee the Board's governance arrangements and to ensure these are consistent with best practice standards; and to review the composition and effectiveness of the Board to support planning for its progressive refreshing.
- The Nomination Committee's terms of reference are reviewed annually and are available at www.investors.aldermore.co.uk

1 Meetings will be chaired by the new Company Chairman once appointed and Danuta Gray will remain a member in her capacity as Senior Independent Director.

Dear Shareholder

As a consequence of the resignation of Glyn Jones, I am now acting as Chair to the Corporate Governance and Nomination Committee (the "Nomination Committee"), and I am therefore pleased to present this report to you.

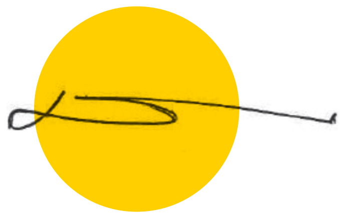
Following the resignation of Neil Cochrane as the representative of our Principal Shareholders, Chris Patrick was nominated as his replacement. With responsibility for reviewing Board vacancies, the Nomination Committee considered the appropriateness of the candidate and was pleased to recommend the appointment of Chris as a Non-Executive Director and member of the Nomination Committee and Risk Committee in November 2016.

The Nomination Committee (led by myself as the Senior Independent Director ("SID")) has dedicated considerable time to overseeing the search to identify Glyn's replacement. John Hitchins, our Audit Committee Chair, was also formally invited to join discussions and form part of the search process. We were well placed to initiate the search process quickly and effectively as, in the prior year, we had agreed a Chairman Succession Framework which outlined the agreed approach that would be adopted should a replacement ever be needed. The Framework, which was developed to ensure that the Company has in place at all times an effective Chairman to lead the Board, confirmed that, as the SID, I would assume the Chair role on an interim basis.

Perspectives on a number of external search agencies were debated by the Nomination Committee and a shortlist of agencies invited to pitch. Based on those discussions and how the respective agencies would approach our assignment, Ridgeway Partners was engaged. In conjunction with Ridgeway Partners, a detailed specification was prepared which included the most critical skills, experience and characteristics we would look for in the new Chairman. We are making good progress with the search and look forward to announcing a replacement in due course.

Further detail on the key activities that the Nomination Committee focused on in 2016 can be found on page 61. We are cognisant that governance is a dynamic area and we will continue to monitor and further embed best practice to ensure that our governance frameworks support and underpin the delivery of our strategy.

Whilst the annual effectiveness review of the Nomination Committee confirmed that we continue to operate effectively, an area highlighted for enhancement relates to succession planning. In light of this and the need to ensure that we have adequate succession planning in respect of Executive Directors and senior management, and to ensure that we have the right talent and initiatives to develop internal executives for execution of our strategy, we intend to make this a continued area of focus in 2017.

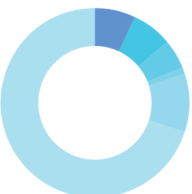


Danuta Gray,
Chair of Corporate Governance and Nomination Committee

Responsibilities of the Nomination Committee

- To review the Group's corporate governance arrangements and frameworks to ensure that they are consistent with best practice
- To review the Board's size, structure and composition, including the skills, knowledge, experience and diversity of the Directors, and that of the Board Committees
- To lead the process for nominating candidates to fill Board vacancies as they arise
- To oversee the annual effectiveness review of the Board and its Committees
- To oversee compliance with the terms of the Relationship Agreement with the Principal Shareholders
- To formulate succession plans for the Chairman, Non-Executive Directors and key senior executives

Time spent in 2016



	%
Annual effectiveness review	7
Appointment/reappointment of Directors	7
Board composition	5
Directors' conflicts	1
Governance	10
Succession planning	70

Key topics discussed at Nomination Committee meetings in 2016

Key:
- Reviewed
- Recommended to Board
- Approved

Topic	Activity	Action
Annual effectiveness review	Output of the 2015 annual effectiveness review of the Board and the Nomination Committee, including agreement of action plans	Recommended to Board
	Update on actions arising from the 2015 annual effectiveness review	Reviewed
	Process for the 2016 annual effectiveness review of the Board and its Committees, and Directors' evaluations	Recommended to Board
Appointment/reappointment of Directors	Annual re-election of Directors and review of their independence	Recommended to Board
	Appointment of a new shareholder-representative Director	Recommended to Board
Board composition	Review of Board Committee composition following the resignation of Peter Cartwright and Neil Cochrane as Directors	Recommended to Board
	Annual review of the structure, size and composition of the Board and its Committees, including the balance of skills, knowledge, experience and diversity of the Directors	Reviewed
Directors' conflicts	Potential conflicts arising from the proposed appointment of Robert Sharpe as Chairman of the Bank of Ireland (UK) PLC	Approved
	Annual review of the Directors' Conflicts Register	Approved
Governance	Nomination Committee Report to be included in the 2015 Annual Report and Accounts	Reviewed
	Gap analysis against the PRA supervisory statement – "Corporate governance: Board responsibilities"	Reviewed
	Compliance with the Relationship Agreement between the Company and its Principal Shareholders	Approved
	Annual programme of agenda items for Nomination Committee meetings in 2017	Approved
Succession planning	Succession planning for both Executive and Non-Executive Directors	Reviewed
	Succession planning for the Chairman role and initiation of the search for a new Chairman, including job specification, selection of search agency and clarification of regulatory requirements	Reviewed

Committee effectiveness

The Nomination Committee undertook a review of its own effectiveness through 2016 as part of the wider Board and Committee evaluation exercise. The review took the form of an internal evaluation and was conducted principally by way of a questionnaire that was issued to all Nomination Committee members.

The review covered various areas including the role and remit of the Nomination Committee; the effectiveness of the Chair; the appropriateness of information provided to the Nomination Committee; and the relationship with management. The Nomination Committee discussed the outcome of the review in early 2017. The Nomination Committee confirmed that it operated effectively and there were no significant areas for concern. It also noted that succession planning would remain a key area of focus in 2017. Further information about the Board and Committee effectiveness process is set out on pages 56 and 57.

Corporate governance

Audit Committee Report

Audit Committee at a glance

- The Audit Committee is composed of four Independent Non-Executive Directors, in line with Code requirements:
  - John Hitchins (Chair), Independent Non-Executive Director
  - Robert Sharpe, Independent Non-Executive Director
  - Peter Shaw, Independent Non-Executive Director
  - Chris Stamper, Independent Non-Executive Director
- Regular attendees at the Audit Committee include the CEO, CFO, CRO, Group Internal Audit Director, Group Financial Controller, representatives from KPMG and the Company Secretary.
- To comply with Code requirements that the Audit Committee has at least one member with recent and relevant financial experience, the Board is satisfied that John Hitchins meets these requirements, being a qualified chartered accountant with extensive financial and audit experience.
- The Audit Committee has also reviewed the new Code requirement that the Committee as a whole should have competence relevant to the sector in which the Company operates, and has confirmed its compliance with this statement. See pages 42 and 43 for full biographical details of Audit Committee members.
- The Audit Committee's key role is to review the integrity of the financial reporting for the Group and to oversee the effectiveness of the internal control systems and work of the internal and external auditors.
- The Audit Committee's terms of reference are reviewed annually and are available at www.investors.aldermore.co.uk

Dear Shareholder

I am pleased to present this report of the Audit Committee for the year ended 31 December 2016 and I set out below some key highlights. We continue to maintain a close relationship with the Risk Committee as there are topics of mutual interest, although with different areas of focus.

The Conduct Committee of the Financial Reporting Council ("FRC") reviews the report and accounts of public and large private companies to determine whether they comply with the Companies Act 2006 and other reporting requirements. These reviews are conducted on a "desk top" basis without access to companies' detailed records, but nonetheless the Audit Committee was delighted to receive a "no issues" letter from the FRC which confirmed that, based on their review of the Group's 2015 Annual Report and Accounts (our inaugural report as a listed company), they had no questions or queries to raise at that time.

Taking into account the framework set out in the Audit Tendering Policy (which we adopted in June 2016), the Audit Committee initiated a project in the second half of 2016 to design and execute a tender process for the external auditor. This was a significant and comprehensive exercise which concluded with the Board approving the Audit Committee's recommendation that Deloitte LLP be appointed as our external auditor for the period commencing 1 January 2017. I would like to extend my thanks to our audit partner and the wider audit team at KPMG for the support they have given to the organisation as it has transitioned into a listed company.

Given the highly regulated environment that we operate within, I am pleased to report that the outcome of the annual evaluation of the Group Internal Audit ("GIA") function demonstrates that overall the team is operating effectively and that it continues to evolve in tandem with the maturity of the organisation. In line with the Chartered Institute of Internal Audit ("CIIA") standards, the Audit Committee has agreed to commission an external quality assessment in 2017 to benchmark GIA activities against best practice and peers. Ahead of this, during 2016, the function conducted a self-assessment against the CIIA published guidance on "Effective Internal Audit in the Financial Services Sector" which provided assurance to the Audit Committee that, on a proportionate basis, the function complied with all relevant areas. Further information about GIA can be found on page 67.

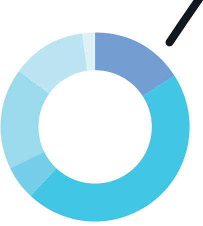
The report sets out the areas the Audit Committee focused on in 2016. Many of these will again form areas of focus for us in 2017 and, in particular, the Audit Committee will continue to provide regular oversight to the IFRS9 programme (which was mobilised during 2016) to ensure that the Company is ready for the implementation of this standard with effect from 1 January 2018.

John Hitchins,
Chair of Audit Committee

Responsibilities of the Audit Committee

- Monitor the integrity of the financial statements of the Group, including its annual reports, half-yearly reports and quarterly updates
- Challenge the consistency of, and any changes to, accounting policies and confirm whether the Group has complied with and followed appropriate accounting standards and made appropriate estimates and judgements
- Monitor and keep under review the effectiveness of the Group's internal financial controls and internal control systems
- Assess whether the Group's financial reports are fair, balanced and understandable; the appropriateness of the adoption of the going concern basis of accounting; and the statement that the Directors have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due
- Review the adequacy of the Group's whistleblowing arrangements and procedures for detecting fraud and preventing bribery and money laundering
- Monitor the remit and effectiveness of the GIA function, review all internal audit reports and monitor management's responsiveness to the findings and recommendations
- Oversee the relationship with the external auditor, including the approval of audit and non-audit fees and terms of engagement, annually assessing their independence and reviewing their findings

Time spent in 2016



	%
External audit	16
Financial reporting	46
Governance	6
Internal audit	17
Internal controls	13
Other	2

Key topics discussed at Audit Committee meetings in 2016

Key:
- Reviewed
- Recommended to Board
- Approved

Topic	Activity	Action
External audit	External audit control observations, including management's responses	Reviewed
	External auditor's assessment of their independence	Reviewed
	2016 audit strategy, terms of engagement and fee proposal	Approved
	Effectiveness review and reappointment of the external auditor	Recommended to Board
	New Audit Tendering Policy	Approved
	Audit tender process and recommendation to the Board to appoint a new external auditor with effect from the 2017 AGM	Recommended to Board
Financial reporting	Financial results, including going concern and viability statements, and the 2015 Annual Report and Accounts	Recommended to Board
	Representation letters to the external auditor	Recommended to Board
	Key judgement areas for the 2016 half-year and full-year results	Reviewed
	Pillar 3 disclosures as at 31 December 2015	Approved
	Project to implement IFRS9 (new guidelines for calculating and reporting provisions) with effect from 1 January 2018	Reviewed
	Regular review of policies, including the Loan Impairment and Provisioning Policy and Hedge Accounting Policy, and approval of a new Effective Interest Rate Stance Policy	Approved
Governance	Annual programme of agenda items for Audit Committee meetings in 2017	Approved
	Review of the Audit Committee's effectiveness	Reviewed
	Regulatory developments which impact on audit committees	Reviewed
Internal audit	Annual review of the effectiveness of the GIA function, and consideration of progress against actions from the previous review	Reviewed
	Output from the review of the GIA function against the CIIA guidance on "Effective Internal Audit in the Financial Services Sector"	Reviewed
Internal controls	Annual report from the Money Laundering Reporting Officer	Reviewed
	Annual review of whistleblowing arrangements	Reviewed
	Assessment of the effectiveness of systems of risk management and internal controls	Recommended to Board
	Annual review of disclosure controls and procedures, including the impact of the implementation of the EU Market Abuse Regulation	Recommended to Board
	Updates on data governance	Reviewed
	Processes for preventing fraudulent financial reporting	Reviewed
	Enhancement of the Business Assurance Framework	Reviewed

In addition, the Audit Committee received regular updates from the GIA function on audit reports issued and progress against audit recommendations. Non-audit services and fees were also monitored.

Corporate governance

Audit Committee Report continued

Areas of focus

Financial reporting

In respect of financial reporting, the Audit Committee considered the Company's half-year and annual financial statements and considered a number of significant issues and areas of judgement (as set out in the table below). The issues are broadly similar to those looked at in 2015 except deferred tax is no longer considered significant given the substantial reduction in the deferred tax asset.

Key issues/judgements in financial reporting	Audit Committee review and conclusions
Loan impairment provisions The calculation of loan impairment provisions is management's best estimate of losses incurred in the Group's portfolios at the balance sheet date. It involves estimates of expected future cash flows based on both the likelihood of a loan and advance being written off and the estimated loss on such a write-off. At 31 December 2016, the Group held £14.3m of specific loan impairment provisions and £13.1m of collective provisions respectively.	– The Audit Committee reviewed regular reports during the year in relation to both the collective and individual loan impairment provisions. The collective impairment model involves a number of significant assumptions. All key assumptions, including the probability of default and emergence period, have been considered, challenged and reviewed, including an analysis of the sensitivity of each key assumption. – The probability of default is assessed using information obtained from a credit bureau for comparable borrowers. These probabilities of defaults are then adjusted (usually downwards) to reflect the nature of the Group's lending. The level of adjustment is based on historic internal data. – Emergence period assumptions are necessary to estimate the time between the trigger events occurring and loans being identified as impaired. The Group has limited historical data available and therefore uses market insight to estimate the emergence period assumptions. As a result of the UK's decision to leave the EU, it is widely predicted that the UK economy will experience a sustained period of economic uncertainty. Whilst it is impossible to predict the potential impact of this economic uncertainty, a decision was made to increase the emergence period for the Mortgages segments in June 2016. This had the impact of increasing the collective impairment by £1.6m. – The Audit Committee also considered specific cases of individual provisions. The significant judgements in calculating specific provisions relate to the estimate of the value of collateral due to the specialised nature of lending in SME Commercial Mortgages and Asset Finance, coupled with the alternative exit strategies which can be adopted. – The Audit Committee agreed management's judgement was appropriate as at 31 December 2016. The disclosures relating to loan impairment provisions are set out in Note 3 and Note 22 to the financial statements on pages 166 to 167 and 177 to 178 respectively.

Key issues/judgements in financial reporting	Audit Committee review and conclusions
Effective Interest Rate ("EIR") The EIR method of accounting for income recognition requires management to make a number of assumptions. In particular, management must make a significant judgement around the estimation of the expected life of loan assets across the Group's portfolios. At 31 December 2016, the Group's balance sheet includes an EIR asset of £6.8m.	– The EIR method of accounting uses a discounted cash flow model to spread interest and fee income and expense attributable to loan assets, including costs and other premium and discounts, over the estimated life of the asset. – The Audit Committee considered and challenged the key assumptions within the EIR models. One of the key assumptions relates to the expected life of the loan asset which is underpinned by judgements made on the likely repayment profile of the Group's loan portfolios (both organic and acquired) driven by expected future customer behaviour. During the year, the Audit Committee reviewed, challenged and approved an updated governance framework related to the preparation and ongoing monitoring and enhancement of these repayment profiles. – It further reviewed the reassessment of the expected lives as at 31 December 2016, further details of which are given in Note 3 to the Financial Statements on page 168. The Audit Committee was satisfied that this reassessment had been prepared in line with the updated governance framework. After considering sensitivities of key judgements, the Audit Committee agreed that management's judgement was appropriate.
Share-based payments Share-based payments are material by nature and determination of the fair value of share-based payments awarded to Directors and employees of the Group requires management to make a number of judgements. A total charge of £3.5m in relation to share-based payments was reflected in the income statement during the year.	– During 2016, further share awards were granted under the existing schemes, including a modification. The most significant judgement remains the calculation of the expected volatility of the Company's share price. – The Audit Committee considered the accounting for the share plans, including the methodology used to calculate the fair value of the awards granted and the key inputs and assumptions used in the valuation models to calculate the charge. – The Audit Committee considered sensitivities of key assumptions and was satisfied with the judgements applied in calculating the fair value of the awards granted. The disclosures relating to share-based payments are set out in Note 3 and Note 37 to the financial statements on pages 168 and 186 to 189 respectively.
Goodwill attributable to Invoice Finance During 2016, the Group impaired goodwill balances totalling £4.1m attributable to the Invoice Finance segment. Accounting standards require an assessment of goodwill balances for impairment on at least an annual basis.	– At 1 January 2016, the Invoice Finance goodwill was carried forward using the Fair Value Less Cost of Disposal ("FVLCD") method of valuation. During 2016, following the UK's decision to leave the EU, there was a general fall in the market value of financial services businesses. As a result, at the half year a decision was taken to impair the goodwill relating to the Invoice Finance business of £4.1m. – The disclosures relating to the Invoice Finance goodwill are set out in Note 3 and Note 28 to the financial statements on pages 169 and 182 respectively.

Corporate governance

Audit Committee Report continued

Fair, balanced and understandable

In line with the Code, the overarching principle for an annual report and accounts is that the report as a whole is "fair, balanced and understandable and should provide the information necessary for shareholders to assess the company's position and performance, business model and strategy". This requirement was at the forefront of the Audit Committee's planning process for the 2016 Annual Report and Accounts to ensure that it could provide assurance to the Board about making this statement.

The process enabling the Audit Committee to reach this conclusion included:

- The production of the 2016 Annual Report and Accounts was managed by the Chief Financial Officer, with overall governance and co-ordination provided by a cross-functional team of senior management.
- This support included input from Finance, Risk, Company Secretariat, Investor Relations and the business lines (including the Managing Directors).
- There was a robust review process of inputs into the 2016 Annual Report and Accounts by all contributors to ensure disclosures were balanced, accurate and verified, and further comprehensive reviews were conducted by senior management.
- The Company Secretary reviewed all Board and Committee minutes to ensure all significant matters discussed at meetings were appropriately disclosed in the 2016 Annual Report and Accounts as required.
- A full review was undertaken by the external legal advisers to ensure all disclosure requirements were met, as well as following best practice.
- A formal review was undertaken by the Audit Committee of the draft 2016 Annual Report and Accounts in advance of final sign-off.
- A final review was performed by the Board of Directors.

In conclusion, the Audit Committee is satisfied that the 2016 Annual Report and Accounts meets the "fair, balanced and understandable" criteria.

Internal controls and risk management

The Audit Committee is responsible for reviewing the adequacy and effectiveness of the Group's systems of internal control and risk management. Details of the risk management systems in place are provided within the risk management section from page 106.

Details of the process performed to assess the effectiveness of internal controls are provided on page 31.

On the recommendation of the Audit Committee and Risk Committee, the Board concluded that the Group's systems of internal control and risk management were appropriately designed and operated effectively during 2016.

Whistleblowing

The Audit Committee reviews the adequacy and security of the Group's whistleblowing arrangements for its employees and contractors to raise concerns, in confidence, about possible wrongdoing in financial reporting or other matters. Under new regulation in 2016, the Company was required to appoint a Whistleblowing Champion to oversee the effectiveness of the whistleblowing framework, and an accountable executive for establishing policies and procedures on whistleblowing. The Chair of the Audit Committee and the Chief Risk Officer agreed to be appointed to these roles, and will carry out their responsibilities in conjunction with the Audit Committee.

During 2016, the Audit Committee reviewed the Group's whistleblowing arrangements and it was agreed that, in order to complement the processes that were already in place, an independent third-party provider would be appointed to operate a whistleblowing line. Avenues previously available to an employee for raising a concern remain in place (i.e. with their line manager in the first instance or, where not appropriate, directly with the Head of Compliance via a dedicated contact number). Once a report has been made, an initial assessment is undertaken in order to decide if an independent investigation is required.

In respect of the year under review, a report on whistleblowing was considered by the Audit Committee which concluded that there were no areas of concern which were significant or demonstrated material weaknesses in internal controls during the year.

Group Internal audit

The Group has an independent and objective GIA function which acts as the third line of defence. The GIA Director reports directly to the Audit Committee Chair and to the CEO for administrative purposes. The GIA Director meets with the Audit Committee Chair on a frequent basis and periodically with the whole Audit Committee without management present. In addition, the Audit Committee held a roundtable with members of the GIA team during the year, which allowed the Audit Committee to delve further into key areas of focus. See page 55 for more information about the roundtable event.

The Audit Committee reviews and approves the GIA Risk Assessment and Plan of Work ("GIA Plan") including the adequacy of resources and skills available. The GIA Director utilises specialist knowledge from external consultants, where appropriate, to supplement the skills of the GIA team. The GIA Director monitors changes to the business and the external environment throughout the year and considers whether any changes to the GIA Plan are needed. Any proposed changes are reviewed and approved by the Audit Committee.

The Audit Committee receives regular reports on progress against the GIA Plan including reports on individual audits as well as thematic issues identified. The Audit Committee also reviews the effectiveness of management action plans to remediate GIA findings and receives reports from GIA on the progress management has made in implementing audit recommendations.

To assess the effectiveness of GIA in respect of 2016, the Audit Committee performed an internal review which included obtaining feedback from members of the Audit Committee, as well as executive management. It also had regard to the CIIA guidance on "Effective Internal Audit in the Financial Services Sector" ("CIIA Guidance"). The internal review concluded that the function was effective overall noting that, while there were some areas for further development, these had already been identified and were being acted upon by the GIA Director. During the year, GIA also performed a self-assessment against both the CIIA Guidance and internal auditing standards. The Audit Committee reviewed the output from this review, which confirmed that GIA was operating effectively against the standards.

The Audit Committee has decided that in 2017 it will commission an external quality assessment to benchmark GIA activities against best practice and peers.

External audit

The Audit Committee is responsible for overseeing the relationship with the external auditor, including the ongoing assessment of the auditor's independence. The Audit Committee makes recommendations to the Board with regard to the appointment of the external auditor, and approves their remuneration and terms of engagement.

KPMG LLP and its predecessor firm, KPMG Audit PLC, were appointed as the Company's auditor in 2009. The current audit partner is Mike Peck who has been in place since 2014.

During 2016, the Audit Committee Chair met the external auditor on a regular basis during the year to facilitate effective and timely communication.

The Audit Committee also met the external auditor once during the year without management present in order to discuss their remit and raise any issues arising from the audit.

Independence

Processes are in place to safeguard the independence of the external auditor, including controls around the use of the external auditor for non-audit services and the operation of a Policy on the Employment of Former Employees of the External Auditor. Details of the Non-Audit Services Policy are set out on page 69. In addition, the external auditor provides the Audit Committee with further assurance as to the procedures that it maintains to preserve objectivity and confirmation that it remains independent.

Effectiveness

The Audit Committee assesses the effectiveness of the external auditor and the external audit process on an annual basis through a number of steps, including: i) agreement of their engagement letter and fees; ii) a review of the external audit plan, including the experience of the audit team assigned; iii) an evaluation of the reports issued following inspections of KPMG LLP by the Financial Reporting Council's Audit Quality Review team; iv) a review of the clarity and thoroughness of KPMG LLP's written reports and contribution to Audit Committee discussions; and v) a review of non-audit fees to confirm compliance with the Non-Audit Services Policy. Following its review of the 2016 external audit process, the Audit Committee concluded that it was effective.

Corporate governance

Audit Committee Report continued

Audit tender

During the year, the Audit Committee approved an Audit Tendering Policy which confirmed that the external audit contract would be put out to tender at least every 10 years, and where a competitive tender had not been completed in the last five years, the Company would confirm when it proposed to carry out a tender and the reasons why. This was in line with both the Code and other regulatory requirements.

The Audit Committee decided to commence a tendering process in 2016. This process culminated in a recommendation to the Board that Deloitte LLP should be appointed as the Company's auditor with effect from the 2017 AGM. This recommendation was approved by the Board in December 2016 and the proposed appointment is included in the 2017 Notice of AGM. Further detail on the tender process is provided below.

Audit Committee effectiveness

The Audit Committee undertook a review of its own effectiveness through 2016 as part of the wider Board and Committee evaluation exercise. The review took the form of an internal evaluation and was principally conducted by way of a questionnaire that was issued to all Audit Committee members.

The review covered various areas including the role and remit of the Audit Committee; the effectiveness of the Chair; the appropriateness of information provided to the Audit Committee; and the relationship with management. The Audit Committee discussed the outcome of the review in early 2017. The Audit Committee confirmed that it operated effectively and there were no significant areas for concern. Further information about the Board and Committee effectiveness process is set out on pages 56 and 57.

External audit tender process

The tender process was overseen by the Audit Committee, with support from a steering group comprising the Audit Committee Chair, the Risk Committee Chair, the CFO and the Group Financial Controller. The tender process involved five key stages, which are summarised below:

Stage 1 – Initial meetings with the audit firms

- Intention to tender was advertised on the corporate governance section of the Group's Investor Relations website.
- Five interested firms (including the incumbent firm) met with the audit tender steering group.
- These sessions enabled the steering group members to gain insight into the experience, qualification and fit of the proposed audit teams as well as to discuss any potential independence issues.

Stage 2 – Issue of formal invitation to tender

- An invitation to tender was issued to three shortlisted firms, along with a deadline to submit their intent to tender.
- The firms were also requested to submit a non-disclosure agreement, a declaration of independence from the Group and a supplier questionnaire.

Stage 3 – Provision of information to audit firms

- The Group issued all shortlisted firms with relevant information to provide them with an overview of the Group's history, business and audit requirements.
- The firms were provided with the opportunity to ask clarification questions to increase their understanding of the Group and support their tenders.

Stage 4 – Meetings with key individuals and submission of final proposals

- The shortlisted firms met with members of the executive team, the Audit Committee Chair and the GIA Director.
- These meetings were performed over two days and provided an opportunity for the Group to evaluate the firms in an informal setting, and for the firms to further enhance their understanding of the Group.
- Following these meetings, the firms had an opportunity to ask further questions before submitting their final proposals.

Stage 5 – Presentation to the Audit Committee and outcome

- All three firms were asked to present their audit proposals to the steering group.
- Based on a careful assessment against a comprehensive set of evaluation criteria, the Audit Committee recommended a preferred firm together with an alternative.
- After careful consideration, the Board accepted the recommendation from the Audit Committee to appoint Deloitte LLP as the Group's external auditor for 2017.
- The appointment of Deloitte LLP will be recommended to shareholders at the 2017 AGM.

Non-audit services

To ensure the independence of the external auditor, the Audit Committee has adopted a formal policy on the engagement of the auditor to perform non-audit services.

Under the Non-Audit Services Policy, the external auditor is prohibited from undertaking any work that is considered to threaten its independence or objectivity in its role. Prohibited work specifically includes bookkeeping services, the design and implementation of financial information systems, appraisal or valuation services, actuarial or legal services, and any other work that would involve the external auditor in preparing financial information that is included or disclosed in the audited financial statements, or in making judgements or taking decisions on behalf of management.

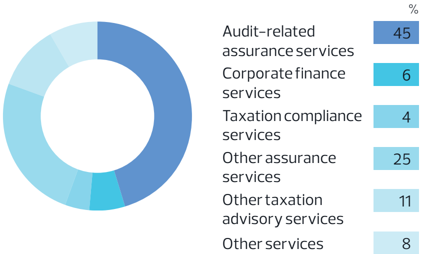
The external auditor is permitted to undertake work in other areas as long as it is the most suitable supplier of the service and the terms and conditions of the engagement, including the level of the fee, do not impair its objectivity or independence. Under the Policy, the Audit Committee pre-approves the use of the external auditor for routine non-audit services, such as profit verifications and country-by-country reporting.

Agreement to use the external auditor for non-audit services must be approved as set out below.

When determining whether the external auditor is the most suitable supplier of a particular service, management and the Audit Committee take into account the cost-effectiveness of the service and the external auditor's knowledge of the Group. KPMG LLP has policies and procedures in place to ensure that the highest standards of objectivity, independence and integrity are maintained, and these comply with the Auditing Practices Board's Ethical Standards for Auditors. The audit engagement partner must approve any non-audit services offered to the Group. This ensures that the objectives of the proposed engagement are not inconsistent with the objectives of the audit; allows the identification and assessment of any related threats to KPMG LLP's objectivity; and assesses the effectiveness of available safeguards to eliminate such threats or reduce them to an acceptable level. KPMG LLP do not carry out non-audit services where no satisfactory safeguards exist.

During the year, the external auditor was engaged to perform the following non-audit services:

Non-audit services



The above services resulted in total non-audit services being provided of £0.3m.

In 2016, the ratio of non-audit services to the external audit fee was 58%. Further information on the total fees and non-audit fees paid to the external auditor is detailed in Note 16 of the financial statements on page 174.

Service	Approval required
Service not previously pre-approved regardless of fee	Audit Committee
Any engagement greater than £100k	Audit Committee
Pre-approved services between £20k and £100k	CFO
Pre-approved services less than £20k	Direct report to the CFO

Corporate governance

Risk Committee Report

Risk Committee at a glance

- The Risk Committee is composed of a majority of Independent Non-Executive Directors, one of whom chairs the meetings, in line with the Walker Review recommendations:
  - Peter Shaw (Chair), Independent Non-Executive Director
  - John Hitchins, Independent Non-Executive Director
  - Chris Patrick, Non-Executive Director
  - Robert Sharpe, Independent Non-Executive Director
  - Chris Stamper, Independent Non-Executive Director
- Peter Cartwright was also a member of the Risk Committee until his resignation from the Board with effect from 18 April 2016. Neil Cochrane acted as Peter's alternate over this period, and served as a member in his own right between 10 May 2016 and 14 October 2016.
- Regular attendees at meetings of the Risk Committee include the CRO, CEO, CFO, business Managing Directors, Group Internal Audit Director, Company Secretary and representatives from the Group's external auditor.
- The Risk Committee's key role is to provide oversight of and advice to the Board on the current risk exposures and future risk strategy of the Group, including the development and implementation of the Group's Risk Management Framework and for ensuring compliance with the Group's approved risk appetite.
- The Risk Committee's terms of reference are reviewed annually and are available at www.investors.aldermore.co.uk

Dear Shareholder

I am pleased to present the report of the Risk Committee for 2016. The promotion of a strong risk culture is a key Board responsibility and the regular attendance at meetings of the Risk Committee by other Directors who are not members reflects the Board's desire to set this 'tone from the top'.

In November 2016, we welcomed Chris Patrick to the Risk Committee as the representative of our Principal Shareholders. Chris brings with him a wealth of financial and risk management experience. Peter Cartwright and Neil Cochrane served as shareholder-representative members during the year, and I would like to take this opportunity to thank them both for their outstanding contributions to the Risk Committee during their respective tenures. Following changes to the CEO's executive team, the Risk Committee is now supported by a new Chief Risk Officer, Christine Palmer. Joining from RBS where she held senior risk roles for the last 13 years, Christine brings strong leadership to the Risk function.

The Risk Committee has again had an active agenda in 2016. Our key priority has been to build on the substantial investment in the Risk Management Framework that we oversaw in 2015. We have continued to evolve and embed risk frameworks, policies and procedures, whilst remaining cognisant of the growth of the business, the changing economic outlook and developments in the regulatory environment.

Further detail on the enhancements that we have made to the Risk Management Framework is set out overleaf, but I would highlight in particular the progress made on embedding our Business Assurance Framework (which tests the controls within the business divisions and central functions) to reflect the growing size, scale and complexity of the Group; enhancing our stress testing capabilities; augmenting our lending policies; and reviewing our buy-to-let underwriting standards in response to regulatory changes. We have also maintained a watching brief over the impact of the UK's decision to leave the EU on our business, both at the time of the vote and as further detail on the execution of that decision has emerged. We will continue to do so as we look towards our priorities for 2017.

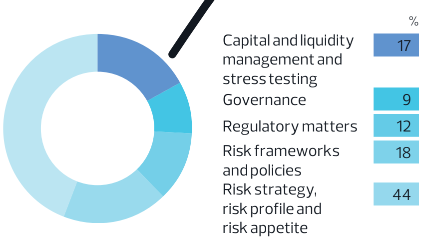
The Risk Committee keeps under review those risks on the horizon that could have a material impact on the Group in the future. These emerging risks will be an area of focus in 2017, alongside the impact on our risk appetite of changes in the external environment.

Peter Shaw,
Chair of Risk Committee

Responsibilities of the Risk Committee

- Oversee the Group's overall risk appetite, risk tolerance and risk strategy
- Monitor the risk profile against the Board-approved risk appetite
- Oversee the development, implementation and effectiveness of the overall Risk Management Framework
- Monitor the effectiveness of the Group's risk management and internal control systems
- Review the stress and scenario testing of the Group's strategic and business plans
- Ensure the adequacy of compliance with regulatory requirements (including the ICAAP and ILAAP) and recommend to the Board for approval
- Review and monitor activities, independence and effectiveness of the Risk function, including Compliance
- Review risk-related Group policies for recommendation to the Board
- Provide advice to the Remuneration Committee on principles and deliverables that will ensure that the determination of remuneration fully reflects risk performance

Time spent in 2016



Key topics discussed at Risk Committee meetings in 2016

Key:
- Reviewed (orange)
- Recommended to Board (green)
- Approved (blue)

Topic	Activity	Action
Capital and liquidity management and stress testing	Internal Capital Adequacy Assessment Process ("ICAAP") and the Internal Liquidity Adequacy Assessment Process ("ILAAP")	Recommended to Board
	Issuance of Tier 2 Loan Notes	Recommended to Board
	Base and stress scenarios for the budget and ICAAP	Approved
	Annual review of the Stress Testing Framework	Approved
Governance	Annual review of the Risk Committee's effectiveness	Reviewed
	Report from the CRO on the assessment of risk performance in relation to incentive schemes	Reviewed
	Annual programme of agenda items for Risk Committee meetings in 2017	Approved
Regulatory matters	Regular monitoring of the PSM action plan	Reviewed
	Impact on the Mortgages business of the PRA consultation paper on buy-to-let underwriting standards	Reviewed
	BCBS review of standardised credit risk weights and its impact on the Group	Reviewed
Risk frameworks and policies	Annual review of the Risk Appetite Framework	Recommended to Board
	Changes to the Operational Risk Management Framework and the annual review of its effectiveness	Approved
	Proposals to introduce a Group Policy Management Framework and a Group Models Management Framework	Approved
	Annual review of policies including the Group Concentration Risk Policy and Prudential/Treasury Policies	Approved
	Annual review of the Reputational Risk Policy	Recommended to Board
	Embedding of changes to the Business Assurance Framework	Reviewed
Risk strategy, risk profile and risk appetite	Half-yearly updates on products approved and credit policy changes	Reviewed
	Conduct risk deep-dive	Reviewed
	Annual review of risk strategy	Recommended to Board
	Adoption of a simplified approach to the monitoring of strategic risks	Approved
	Deep-dive into performance against risk appetite in the Mortgages business	Reviewed
	Review of risks associated with change activity across the Group, including post implementation reviews	Reviewed

In addition, a report is provided at each meeting from the CRO covering performance against the risk appetite metrics, escalated items from the businesses and emerging risks. The Risk Committee also receives regular updates on areas including cyber security and requests for risks to be accepted.

Corporate governance

Risk Committee Report continued

Areas of focus

Details of key matters discussed by the Risk Committee during the year are set out on page 71 and further information about discussion of these topics at meetings is described below. In addition, pages 33 to 35 provide a summary of the principal risks faced by the Group and key mitigating actions; and an overview of emerging risks, along with recent and anticipated future developments. Further information on the Group's approach to risk, including the associated governance framework for managing risk, stress testing and a full analysis of the principal risks are set out in the risk management section on pages 106 to 139.

Frameworks

During the year, the Risk Committee reviewed and updated the Risk Management Framework ("RMF") and Risk Appetite Framework ("RAF"), with risk appetite statements and risk metrics being revised and refreshed as appropriate. Proposals were approved to implement a Group Policy Management Framework (under which policies, processes and procedures will be governed) and a Models Management Framework, thereby strengthening the overarching RMF. The Stress Testing Framework was also enhanced, and the Group's ICAAP and ILAAP were challenged and recommended to Board.

Credit risk

The Risk Committee regularly reviews the credit risk profile of the Group, with a clear focus on performance against risk appetite statements and risk metrics. During the year, the Risk Committee considered in-depth reviews of a number of asset classes including the Mortgages and Buy-To-Let exposures. A number of policies were reviewed by the Risk Committee including the Group Concentration Risk Policy, changes to portfolio level policies and the impact of these on risk appetite.

The current and future impact of emerging risks on the Group's credit risk profile and risk appetite was a particular area of focus, with follow-up actions being agreed with management as required.

Capital and liquidity risk

The Risk Committee monitors capital and liquidity risk and receives regular reports on actual and forecast levels in relation to key RAF metrics.

During the year, the Risk Committee considered revisions to the Group's capital risk appetite and reviewed the impact of key regulatory developments including the BCBS proposed revisions to the standardised approach to credit risk (expected to be finalised in H1 2017) and the Bank of England's approach to minimum requirement for own funds and eligible liabilities.

The Risk Committee also reviewed changes to the approach to the management of and reporting on liquidity risks. This was strengthened by revisions to the Funds Transfer Pricing Policy (which ensures that the costs and risks of liquidity are clearly attributed to business lines) and changes to core systems and people capability which have enabled daily liquidity reporting to be enhanced.

Market risk

Although the Group does not seek to take market risk, the Risk Committee reviewed the interest rate risk that the Group carries as part of the ICAAP review process.

Operational risk

As part of the continued development of the systems and controls in place to support the control environment, the Risk Committee approved a revised Operational Risk Management Framework in early 2016, and a detailed report on the effectiveness of that framework in October 2016.

During the year, the Risk Committee received a number of updates on operational risk matters, including the operational risk profile, and on specific areas of focus including enhancements to and the implementation of business assurance (controls) testing and the risk and control self-assessment process (by which business areas maintain a view of their risks and control effectiveness).

In terms of the operational risk profile, the Risk Committee received regular updates on business continuity, disaster recovery, cyber security and cyber risk management. Cyber security remains an important area of focus for the Group with a number of improvements delivered during 2016, driven by the Security Investment Programme. This has been complemented by an independent review of the Group's security framework, and a revised cyber strategy for 2017 onwards.

In addition, the Risk Committee monitored the performance of key systems and significant projects, as well as noting material outsourced arrangements.

Compliance, conduct and financial crime risk

Conduct risk management continues to be a key area of focus for the Risk Committee. In addition to regular reports on performance against conduct risk metrics and developments regarding new and existing products, a deep-dive was presented to the Risk Committee which provided an overview of enhancements to and embedding of the conduct risk framework, and emerging themes.

In conjunction with the Audit Committee, the Risk Committee reviews the Group's arrangements for anti-money laundering on an annual basis. The effectiveness of the Financial Crime Risk Framework over 2016 was also reviewed and the Risk Committee noted the significant enhancements made to key policies and procedures during the year and the strengthening of capabilities for regular monitoring of financial crime risk metrics.

Reputational risk

The Risk Committee reviewed and recommended for Board approval the Group's Reputational Risk Policy.

Remuneration matters

The Risk Committee has a duty to advise the Remuneration Committee regarding both the design of senior executive annual and long-term incentive plans to ensure that management are not being incentivised to take undue risks; and any risk management and control issues that have arisen that it believes should be taken into account when determining executive remuneration payments under the aforementioned plans.

In 2016, the Risk Committee reviewed regular reports from the Chief Risk Officer in relation to these matters. A full assessment of the risk appetite, risk management, governance and control frameworks operating across the Group was undertaken, which took into account adherence to established risk appetite limits and triggers, risk events which have been raised, the findings from second line oversight reviews and any unsatisfactory reviews or material findings by Group Internal Audit. Consideration was also given to whether these areas revealed poor culture or a lack of risk and control awareness, and also whether actions to close risk issues were taken seriously and acted upon in a timely manner.

Risk Committee effectiveness

The Risk Committee undertook a review of its own effectiveness through 2016 as part of the wider Board and Committee evaluation exercise. The review took the form of an internal evaluation and was principally conducted by way of a questionnaire that was issued to all Risk Committee members.

The review covered various areas including the role and remit of the Risk Committee; the effectiveness of the Chair; the appropriateness of information provided to the Risk Committee; and the relationship with management. The Risk Committee discussed the outcome of the review in early 2017. The Risk Committee confirmed that it operated effectively and there were no significant areas for concern. Further information about the Board and Committee effectiveness process is set out on pages 56 and 57.

Corporate governance

Remuneration Report
Statement from the Remuneration Committee Chair

"We are satisfied that, as an overarching framework, our Remuneration Policy remains appropriate and continues to align remuneration with the long-term interests of our shareholders."

Cathy Turner
Chair of Remuneration Committee

Content

Statement from the Remuneration Committee Chair

Annual Report on Remuneration *including:*

- A report on the key details of the Remuneration Committee and its work in 2016 (pages 90 and 91)
- Appendix: Remuneration Policy (pages 92 to 99)

Dear Shareholder

On behalf of the Board, I am pleased to present our Directors' Remuneration Report (the "Remuneration Report") for the year ended 31 December 2016. In addition to this statement, the report also includes our "Annual Report on Remuneration" which covers:

- How the Directors' Remuneration Policy (the "Remuneration Policy") was implemented in 2016 and how it will be implemented in 2017
- A report on the key details of the Remuneration Committee and its activities
- An appendix which sets out an extract from our Remuneration Policy for ease of reference

The Remuneration Policy was approved by shareholders last year at the 2016 AGM. Votes of 93.68% and 93.93% were achieved in favour of the approval of the Remuneration Policy and the advisory vote on the Annual Report on Remuneration respectively, and the Board was pleased with this strong level of support.

The Remuneration Committee has kept the Remuneration Policy under review throughout the year. We are satisfied that, as an overarching framework, our Remuneration Policy remains appropriate and continues to align remuneration with the long-term interests of our shareholders. As part of our ongoing assessment of our plans, which includes consideration of market developments, we have identified some enhancements to the operation of our annual bonus plan, the Annual Incentive Plan ("AIP"), which are set out on the next page.

Performance and reward outcomes for 2016

2016 was a remarkable year. Whilst we recognise that the macroeconomic and regulatory developments globally impacted sentiment throughout the year, it was disappointing that the share price has not performed as strongly as we had hoped given the fundamentally strong financial performance that was achieved.

However, throughout 2016 we continued to focus our efforts on serving our customers, prudent growth in assets and capital accretion, such that the year finished strongly in terms of the key financial targets:

- Profit before tax of £128.7m
- Reported return on equity of 17.2%
- Reported cost/income ratio of 46.09%
- Net loan growth of £1.3bn

In determining the pay outcomes for the financial year, the Remuneration Committee has given full consideration to all aspects of performance to ensure a clear linkage to the results.

In respect of the Executive Directors, we agreed:

- a zero level of vesting for the Pre-IPO long-term awards which were subject to a TSR performance measure ending 31 December 2016. These awards have, therefore, lapsed in full; and
- an AIP award of approximately 79.7% and 80.7% of the maximum for the CEO and CFO respectively, in keeping with the strong financial results, and combined with the achievement of the non-financial and personal performance measures within the AIP balanced scorecard. Further information on the performance against relevant targets can be found on pages 79 to 81.

2017 application of Remuneration Policy

Executive Directors

Looking ahead to 2017, remuneration arrangements will remain largely unchanged from 2016. The Remuneration Committee agreed that it would be appropriate to award an increase in base salary to the Executive Directors which was consistent with the average level of increase of 2.5% awarded to employees across the Group generally. This increase will take effect from 1 April 2017. No changes are proposed to the levels of pension contributions (which we are pleased to report are in line with those paid to employees in the wider Group), taxable benefits or the market adjusted allowance.

In considering the AIP balanced scorecard for 2017, we have strived to ensure that bonus outcomes continue to be based on a framework that is both transparent and aligned with shareholder interests. We have concluded that our approach in this regard could be strengthened by:

- broadening the financial performance measures such that they are less weighted towards a single measure of profitability and are now more representative of our core financial KPIs. The weighting of the financial performance measures remains at 50%;
- further emphasising the link between risk performance and remuneration outcomes by increasing the weighting of the risk measures from 15% to 20%. This reflects input from our regulator, the PRA, for a more explicit approach to risk adjustment within scorecards across the industry as well as our own enterprise-wide objective of continuing to embed a robust risk framework; and
- removing the highly qualitative personal objectives target completely and increasing the weighting of the customer and people elements from 7.5% each to 20% and 10% respectively, reflecting the two critical enablers driving sustained performance. Individual performance will continue to be assessed through measuring the non-financial elements against both the overall achievement and personal contribution to those measures.

We believe that these modifications will enable us to provide shareholders with more transparent disclosures going forward on how we have assessed bonus outcomes.

No changes are proposed to either quantum or performance measures in respect of awards to be made under the Performance Share Plan ("PSP") in 2017, and these will be made on a similar basis to 2016.

Non-Executive Directors

Following the resignation of Glyn Jones as Chairman with effect from 6 February 2017, Danuta Gray, our Senior Independent Director, has assumed the role of Interim Chairman. We have agreed that Danuta's fee will be raised to the same level as that of the previous Chairman for the period she undertakes the interim role, recognising the increased responsibilities.

Shareholder engagement

We have followed with interest external developments over the last year regarding executive remuneration, and have monitored evolving views regarding flexible remuneration structures and the use of restricted stock. In particular, we have welcomed the increasing level of support for the tailoring of remuneration arrangements to suit each company's own culture and strategy.

We have taken the decision to widen the use of restricted stock for senior (below Board) executives from 2017 onwards as we believe that this enhances alignment of the interests of executives with the share price and, therefore, with investors, whilst also reducing overall share usage. We will review the impact of changes to our own remuneration structure and wider market developments in 2017 and beyond.

Following our listing last year, we have continued to develop our remuneration practices in line with the approved Remuneration Policy. We welcome the views of our shareholders and are committed to maintaining an open dialogue.

We hope to receive your ongoing support at our forthcoming AGM where I, along with the other members of the Remuneration Committee, look forward to answering any questions you may have on this Remuneration Report or our approach to remuneration more generally.

Cathy Turner,
Chair of Remuneration Committee

Corporate governance

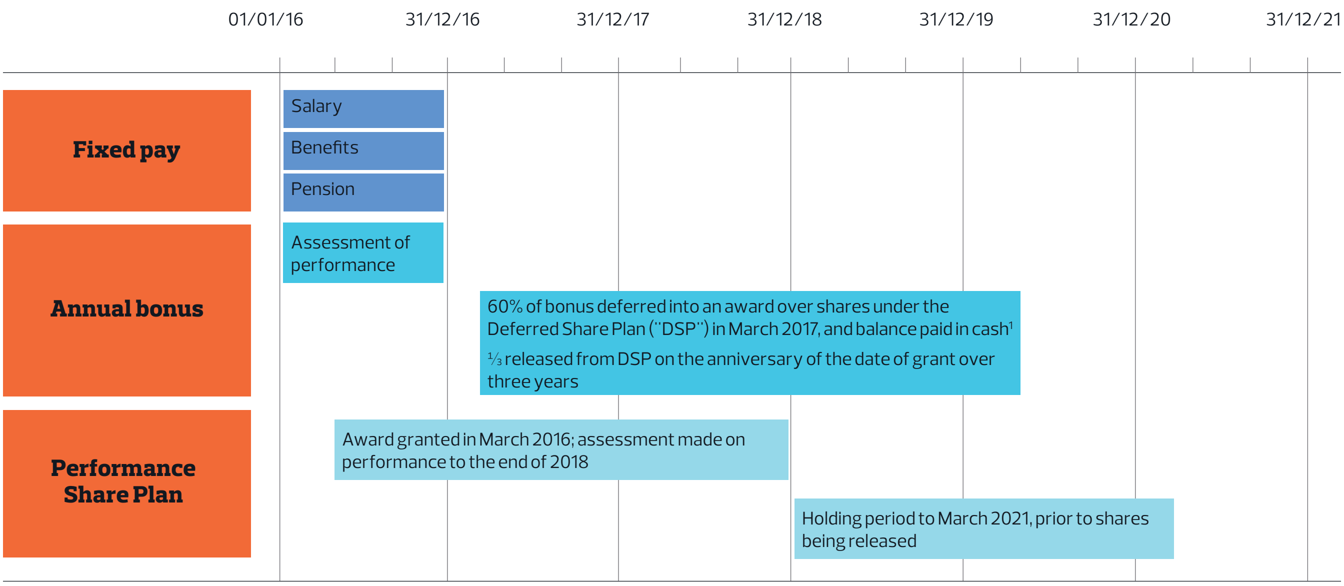
Remuneration Report
Annual Report on Remuneration

Introduction

This Annual Report on Remuneration details how the Remuneration Policy (as approved by shareholders at the 2016 AGM) was implemented in 2016, and sets out how the Remuneration Policy will be implemented in 2017.

Executive Directors

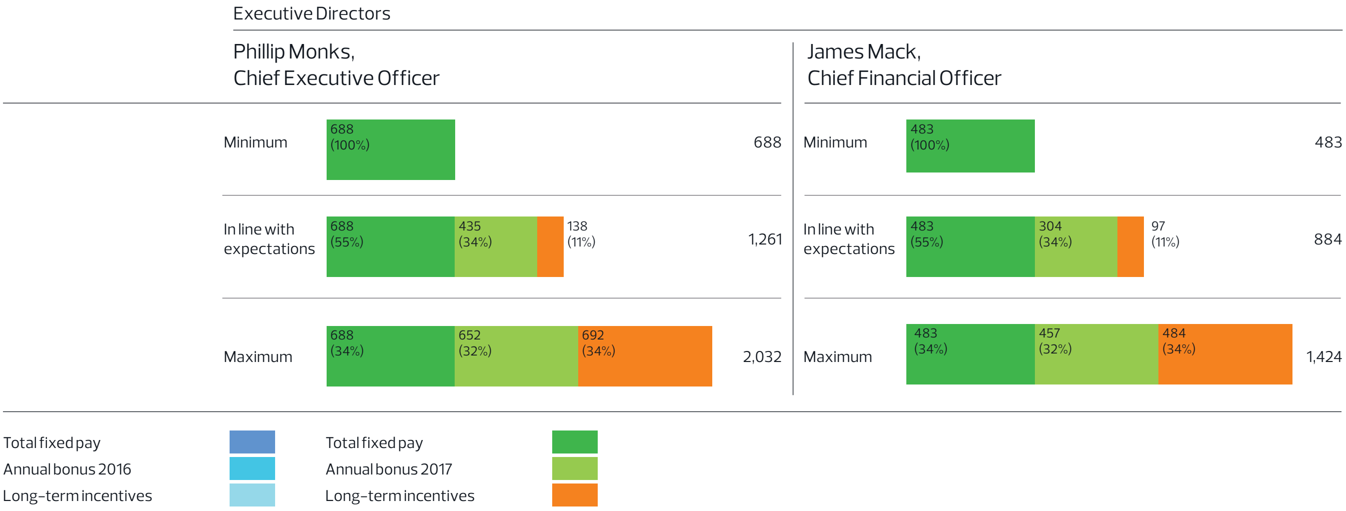
Overview of remuneration structure (2016)



[1] 60% deferred when total variable awards exceed £500k.

At a glance: 2016 total remuneration (£'000)

At a glance: Illustrations for application of the Remuneration Policy in 2017 (£'000)



At a glance: implementation of Remuneration Policy in 2017

Remuneration element	Implementation (for both CEO and CFO unless stated)		Further information on implementation
Base salary from 1 April 2017	CEO: £525,313	CFO: £367,719	See page 78
% increase from prior year	2.5%		See page 78
Benefits	Includes private medical insurance, car allowance and critical illness insurance		See page 78
Market adjusted allowance	20% of base salary		See page 79
Pension	Cash supplement of 8% of base salary		See page 79
Annual bonus – maximum opportunity as % of base salary	125%		See page 82
Annual bonus – financial metrics	Profit before tax (15%) Net interest margin (10%) Net loan growth (10%) Return on equity (5%) Cost/income ratio (5%) Cost of risk (5%)		See page 82
Annual bonus – % vesting for threshold performance	0%		See page 82
Annual bonus – non-financial metrics	Risk (20%) Customer (20%) People (10%)		See page 82
Annual bonus – deferred element	60% deferred for up to 3 years[1]		See page 82
PSP – maximum opportunity as % of base salary	135%		See page 83
PSP – performance measures	Relative TSR (50%) and EPS (50%)		See page 83
PSP – % vesting for threshold performance	20%		See page 83
Share ownership guidelines	200% of base salary		See page 88

[1] 60% deferred when total variable awards exceed £500k.

The chart to the left illustrates the potential outcomes of the Remuneration Policy for Executive Directors based on three different scenarios. The assumptions on which the scenarios are based are set out below:

Scenario	Assumptions
Minimum	Consists of base salary, benefits, market adjusted allowance and pension. A single year's maximum savings under Sharesave is also assumed.
In line with expectations	An on-target bonus under the AIP and a threshold level of vesting under the PSP are achieved.[1]
Maximum	Based on the maximum opportunity being achieved.[1]

[1] Excluding share price appreciation and dividends.

Non-Executive Directors

Fees to be paid to the Non-Executive Directors are set out on page 87. The only change to fees in 2017 (effective 1 April 2017) is an increase in the fee paid to the Chair of the Remuneration Committee (from £15k p.a. to £20k p.a.), which brings this fee into line with the fees paid to the Chairs of the Audit and Risk Committees.

Corporate governance

Remuneration Report
Annual Report on Remuneration continued

Single total figure table: Executive Directors (audited)

The following table sets out the total remuneration paid to the Executive Directors for the financial years ending 31 December 2016 and 31 December 2015.

Name	Fixed elements										Variable elements							
	Salary		Taxable benefits[1]		Pension		Market adjusted allowance[2]		Subtotal		Annual bonus[3]		Long-term incentives[4]		Subtotal		Total	
	2016 £'000	2015 £'000	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000
Phillip Monks	**509**	466	**22**	126	**35**	27	**102**	81	**668**	700	**507**	496	**0**	6,101	**507**	6,597	**1,175**	7,297
James Mack	**357**	348	**17**	44	**24**	21	**67**	43	**465**	456	**360**	351	**0**	721	**360**	1,072	**825**	1,528
Total	**866**	814	**39**	170	**59**	48	**169**	124	**1,133**	1,156	**867**	847	**0**	6,822	**867**	7,669	**2,000**	8,825

1 "Taxable benefits" comprises the gross value of any benefits paid to the Director, whether in cash or in kind, that are chargeable to UK income tax. Further detail is provided at the bottom of the page. In addition, the following items have been included under "Taxable benefits":

- Awards made under the SIP. Consistent with other employees, a one-off award was made under the SIP to both Executive Directors following IPO in recognition of their contribution to the business. This has been valued at the share price on the date of grant (£2.41) and included in the 2015 figure. These awards vested immediately on grant and are included in the share interests table on page 88.
- The write-off of loans to Phillip Monks and James Mack of £108,317 and £31,279 respectively in 2015. These loans were made originally to settle the tax payable by each of the Directors in respect of equity incentives awarded to them prior to the IPO.
- Participation by Phillip Monks and James Mack in the Sharesave Plan. Where the average share price over Q4 in the year of grant is higher than the option price, participation is included under "Taxable benefits". On this basis, participation in the 2016 invitation is included above. Further detail can be found on page 85.

2 The "Market adjusted allowance" became payable following IPO.

3 The "Annual bonus" figure represents the value of the total bonus. A proportion of the bonus will be deferred into shares under the DSP. 60% of the bonus earned in respect of 2016 will be deferred. For 2015, this was at a blended rate based on 15% being deferred into shares for the part of the bonus earned in the period up to IPO, and 60% being deferred into shares for the part of the bonus earned for the period following IPO. See page 79 for detail on the bonus outcome.

4 The Directors held certain shares pre-IPO which converted into ordinary shares on IPO. The reported gains have been calculated on the market value of shares held at IPO (£1.92) less the actual cost of any shares bought pre-IPO, regardless of whether such shares were acquired as an investment or an incentive, and included in the 2015 figure. As part of the IPO, the Directors were subject to certain lock-up arrangements in respect of their shares, as set out in the IPO Prospectus. The lock-up in respect of two-thirds of each Director's holding expired on the first anniversary of the IPO, whilst the remaining one-third expired on the second anniversary of the IPO.

Fixed pay for Executive Directors

Base salary

The Remuneration Committee considered benchmarking data in respect of the base salaries of the Executive Directors, and determined that the increases set out in the table below were appropriate. The increases, which will take effect from 1 April 2017, are in line with the Remuneration Policy and are consistent with the average level of increase of 2.5% awarded to employees in the Group generally.

	At 1 April 2017	% increase	At 1 April 2016
Phillip Monks	£525,313	2.5%	£512,500
James Mack	£367,719	2.5%	£358,750

Taxable benefits

The taxable benefits received by the Executive Directors in 2016 included private medical insurance (family cover), a car allowance and critical illness insurance.

No changes to taxable benefits are proposed to be made during 2017.

Market adjusted allowance

The market adjusted allowance is calculated as a percentage of base salary. As reported last year, with effect from 1 April 2016 the level paid to the CFO was increased from 15% to 20%, aligning it with that paid to the CEO. Further information on the market adjusted allowance can be found in the Remuneration Policy table on page 94.

No changes to the market adjusted allowance are proposed in 2017.

Pensions

Pension contributions for the Executive Directors are paid at a rate of 8%, consistent with employees in the Group generally. This may be paid into a personal pension arrangement or paid as a cash supplement (reduced for the impact of employers' NICs). Throughout 2016, the CEO chose to receive a cash supplement. Prior to 1 April 2016, a contribution of 6% was paid into a stakeholder pension for the CFO (maintained at 6% in line with the CFO's wishes). As reported last year, with effect from 1 April 2016, the CFO elected to be paid a cash supplement of 8% (less employers' NICs) and he ceased to receive contributions into a stakeholder pension.

The Company does not intend to make any changes to pension contributions in 2017.

Annual Incentive Plan ("AIP")

2016 AIP outturn

The AIP is based on a balanced scorecard of financial, non-financial and personal measures. The Remuneration Committee sets stretching performance targets at the start of the performance period. Whilst the performance of each element is assessed against the targets at the end of the performance period, the Remuneration Committee also considers total bonus outcomes within the context of both the Company's overall performance and personal performance to ensure that they are fair.

The table below sets out the performance measures and outcomes for the 2016 AIP. The maximum bonus opportunity for both the CEO and the CFO was 125% of base salary. The actual percentage of the maximum bonus awarded was 79.7% for the CEO and 80.7% for the CFO.

2016 AIP: performance assessment

	Phillip Monks		James Mack	
Measures	Weighting (%)	Actual (%)	Weighting (%)	Actual (%)
Financial	50	35.9	50	36.2
Risk	15	11.3	15	12
Customer	7.5	7.5	7.5	7.5
People	7.5	5	7.5	6
Strategic/personal	20	20	20	19
Total	**100**	**79.7**	**100**	**80.7**

Based on the assessment of the performance measures above, actual bonuses paid to the Executive Directors are set out below. 60% of the bonus awarded will be deferred into shares and held under the DSP. The deferred element of the bonus will take the form of a nil-cost option award, which will become exercisable by the Directors in equal amounts over the three years following the award, subject to continued employment and malus and clawback provisions. The number of shares to be awarded will be based on the Company's average share price over the three-day period prior to grant and will be disclosed in the 2017 Annual Report and Accounts.

Bonuses payable to Executive Directors

Name	Cash (£)	Shares (£)	Total (£)	Bonus as % of base salary (as at 31 December 2016)
Phillip Monks	202,875	304,313	507,188	99.0
James Mack	143,915	215,871	359,786	100.3

Bonuses are calculated by multiplying earnings in the financial year by the maximum bonus potential and the percentage bonus awarded.

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For financial and treasury measures, 0% and 100% of maximum opportunity was available for achievement of threshold and maximum performances respectively, with a sliding scale being applied between each point and the target level (at which point two-thirds of the maximum was payable). The financial targets are set out in the table below:

2016 AIP: financial performance measures and outcomes

Performance measures	Threshold (0% of maximum)	Target (66.6% of maximum)	Maximum (100%)	Actual	CEO weighting	CFO weighting	% of max achieved
CEO and CFO							
Profit before tax	£116.7m	£123.1m	£136.1m	£128.7m	20%	16%	81
Return on equity (reported)	15.64%	16.51%	18.25%	17.2%	20%	16%	80
Cost/income ratio (reported)	49.53%	47.28%	42.77%	46.09%	5%	4%	76
Net loan growth	£1,455m	£1,536m	£1,698m	£1,333m	5%	4%	0
CFO only							
Spread over LIBOR % – Cash	-0.21%	-0.22%	-0.24%	-0.29%	N/A	2.5%	0
Spread over LIBOR % – Liquidity Asset Buffer	0.040%	0.042%	0.047%	0.49%	N/A	2.5%	100
Wholesale stock cost of funds %	-0.92%	-0.88%	-0.80%	-0.51%	N/A	5%	100

The Remuneration Committee assesses the non-financial elements by way of both internal, quantifiable targets and a broader qualitative assessment having sought appropriate input from the Chief Risk Officer, the Group Marketing Director and the Group HR Director in respect of the risk, customer and people elements respectively. The key performance outcomes which were taken into account in agreeing the outcomes were as follows:

2016 AIP: non-financial performance measures and outcomes

Performance metric	Outcomes	% of maximum Phillip Monks	% of maximum James Mack
Risk	• A full assessment of the risk appetite, risk management, governance and control frameworks operating across the Group was undertaken by the Chief Risk Officer and discussed with the Risk Committee before formal presentation to the Remuneration Committee. This included adherence to established risk appetite limits and triggers, risk events and findings raised in the course of reviews by second-line risk teams and the Group Internal Audit function. Consideration was also given to risk culture and risk awareness. • Overall, it was recognised that the risk performance met expectations when measured against existing risk appetite and metrics, the operating environment and the current maturity of the organisation. Both the CEO and the CFO (in conjunction with the Executive team) had been strong advocates of setting the 'tone from the top', and a transparent and open culture was promoted. This had manifested itself in general trends of risk events being raised proactively and in a timely manner; management responsiveness to risk issues; and, consequently, appropriate resolution.	75%	80%
Customer	• The overarching goal for remuneration purposes was to 'put the customer at the heart of everything we do'. This objective was an assessment which included both numeric and more behavioural assessment. • NPS, or Net Promoter Score, is a customer loyalty metric which is widely used across a number of industries, and is one of the key performance indicators of the Group's strategic objective to be customer-driven (see pages 14 and 36 for more information). In 2016, the customer NPS improved by +14 which was well ahead of the target for the year. The Remuneration Committee also took into account the CFO's leadership of the Savings business, where a strong performance resulted in the increase in the Savings NPS score exceeding the target set for 2016. • The 'Voice of the Customer' programme was launched to enable the Group to collect customer feedback in real time and respond to it. The programme was championed by the Executive Directors. • Other indicators of customer views were also considered, for example customer complaints, which were maintained within accepted tolerances, and upheld rates, which remained below industry averages.	100%	100%

Performance metric	Outcomes	% of maximum Phillip Monks	% of maximum James Mack
People	• The 'Big Conversation' programme was launched, in part to replace the 'Best Companies to Work For' survey as the principal means of evaluating employee engagement and to provide more meaningful insights from people. This has enabled richer feedback to be obtained from employees, with a view to better connecting culture with strategy. • Employee engagement is a key performance indicator of the Group's strategic objective to deliver simply. Whilst the mechanism for measuring employee engagement changed in 2016 in line with the 'Big Conversation' approach and was not directly comparable to previous years, the Remuneration Committee noted that internal engagement surveys had confirmed a strong level of employee connection to Aldermore. • Senior management succession planning is continuing to evolve and the mapping of current and future talent requirements has developed further during the year. This translated into the movement of a number of employees into roles that will enable them to broaden their skills and experience, with a view to stepping up in to a more senior role in due course. In addition, development plans were formalised for the senior management team. • Internal management development programmes continue to be promoted, and strong sponsorship and support from the Executive Committee has been instrumental in the programmes resulting in internal promotions. During 2016, the CFO sponsored the Group's main internal development programme (the 'Next Generation Leaders' programme).	67%	80%

The targets for the risk customer and people measures are internal to the Group and commercially sensitive, and are likely to remain so. They are not, therefore, disclosed.

The Executive Directors' personal objectives are focused on the delivery of the Group's strategy and, in the case of the CFO, the continued evolution of the Finance functions falling within his remit. Following consideration of achievements against the objectives which were set at the beginning of 2016, the Remuneration Committee's view was that both the CEO and the CFO had performed strongly against all of their objectives and confirmed that awards of 100% and 95% of maximum respectively should be made. Examples of achievements against personal objectives are set out below:

2016 AIP: personal objectives

	Achievements
Phillip Monks	• A significant year of macroeconomic uncertainty and regulatory developments demanded a more flexible approach to planning, which has been driven by the CEO. A re-articulation of the Group's strategy has led to a renewed focus on three strategic priorities as detailed on page 14.
	• During the year, the Executive Committee was strengthened through the appointment of three new members who bring a wealth of experience in their respective fields and who will each help drive the business forward.
	• The CEO has supported the delivery of key strategic projects. This included upgrades to two of the Group's core customer platforms.
James Mack	• The CFO oversaw delivery of the project to raise £60m additional Tier 2 capital in October 2016, thereby strengthening the balance sheet.
	• A strong performance was delivered across Financial Planning, Financial Control and Capital Management with improvements made to internal structures and resources to provide improved insight and an enhanced control environment to support business decisions.
	• Under the leadership of the CFO, it has been a strong year for the Treasury function. A new asset/liability management system has been implemented with improved reporting and analysis capabilities to drive business performance in areas such as cashflow forecasting.

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2017 AIP

As set out in the statement from the Remuneration Committee Chair (on page 75), the Remuneration Committee has reviewed the balanced scorecard of performance measures to apply for the 2017 performance year. Whilst retaining the broad overall split between financial and non-financial performance measures, some changes to the underlying performance measures and weightings were agreed and, as a result, the balanced scorecard will be structured as set out below.

A key driver of the changes to the underlying performance metrics is to ensure that they are more representative of our core KPIs, thereby strengthening the link between pay and performance. The alignment of the performance metrics with our KPIs is shown below, whilst further information on the KPIs can be found on page 15.

2017 AIP: performance measures (CEO and CFO)

Financial measures	**Core KPI**	**Performance weighting**
Profit before tax	Profit before tax	15%
Net interest margin	Profit before tax	10%
Net loan growth	Net loans	10%
Return on equity	CET1 ratio	5%
Cost/income ratio	Cost/income ratio	5%
Cost of risk	Cost of risk	5%
Non-financial measures		
Risk	–	20%
Customer	–	20%
People	–	10%

The Remuneration Committee has set stretching financial targets against budget, and has agreed a suite of underlying metrics in respect of the non-financial performance measures. An evaluation of each Director's individual performance against the relevant overarching enterprise-wide objective will also be taken into account in assessing the outturn of the non-financial measures.

The targets are currently commercially sensitive but will be disclosed in the 2017 Annual Report and Accounts on a similar basis to those for 2016 in this report.

Long-term incentives

PSP: Awards made in 2016

During the year, awards were granted to the Executive Directors under the PSP (in the form of nil-cost options) with a face value at the time of the award of 135% of base salary. Full details of the awards made are included on page 84.

Half of each award is subject to a relative Total Shareholder Return ("TSR") condition whilst the other half of the award is subject to the achievement of Earnings Per Share ("EPS") targets. Both performance conditions are measured over performance periods which end on 31 December 2018. Details of the performance measures and targets are set out on the next page.

2016 PSP: performance measures

Relative TSR

Growth in TSR will be measured against a comparator group comprising the companies making up the FTSE 350 (excluding Investment Trusts and the Company itself). It is measured from 1 January 2016 (using the Company's one-month average immediately prior to 1 January 2016 as the start point) to the end of 2018 (using the Company's one-month average to 31 December 2018 as the end point). The Remuneration Committee selected relative TSR as a performance measure as it is a key indicator of returns to investors, thereby aligning interests of the Executive Directors with those of shareholders. The Remuneration Committee believes that the FTSE 350 is the most appropriate comparator group as it is more reflective of market performance than a single market grouping or a comparator group of competitors. Details of the targets for relative TSR are set out below:

Ranking	% of award which vests
Below median	0%
Median	10%
Between median and upper quartile	On a straight line basis between 10% and 50%
Upper quartile or above	50%

EPS

EPS will be measured using adjusted undiluted EPS. The Remuneration Committee selected EPS as a performance measure as it is a key internal measure of profitability. Details of the targets for EPS are set out below:

Target	% of award which vests
Below 30p	0%
30p	10%
Between 30p and 37p	On a straight line basis between 10% and 50%
37p or above	50%

In order to satisfy itself that the vesting of any awards is appropriate, the Remuneration Committee has set additional underpin performance conditions which must be met. For both performance measures, the result achieved must appropriately reflect the performance of the Company taking into account such factors as the Remuneration Committee considers appropriate; and the result achieved must be consistent with the Company's risk appetite. Additionally, in respect of TSR, the Remuneration Committee must be satisfied that the Company's achieved TSR is reflective of the Company's underlying financial performance.

PSP: Pre-IPO Awards vesting outcome

The Pre-IPO Awards granted to the Executive Directors at IPO were subject to a performance period which ended on 31 December 2016. In order to achieve a threshold level of vesting, growth of at least 20% p.a. in absolute TSR was required. At the end of the performance period, the Remuneration Committee assessed TSR performance over the performance period and determined that the minimum level of performance had not been met. The Pre-IPO Awards therefore lapsed in full.

PSP: Awards to be made in the current year (2017)

In 2017, the Remuneration Committee intends to make PSP awards to Phillip Monks and James Mack with a face value (at the time of the award) of 135% of base salary. The awards will be made on the same basis as in 2016.

On that basis, half of the award will be subject to a relative TSR condition with 20% of that part vesting at median versus the constituents of the FTSE 350 (excluding Investment Trusts and the Company itself) rising to full vesting of that part for upper quartile performance. The other half of the award will again be subject to an EPS scale with 20% of that part vesting at an EPS of 33p rising to full vesting of that part for an EPS of 41p. In both cases, the same underpins will apply as for the 2016 PSP awards.

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Scheme interests

The Directors hold the scheme interests noted below:

Executive share plan participation

Type of award	Date of grant	No of shares under award (01/01/16)[1]	Granted during 2016	Vested during 2016	Lapsed during 2016[2]	No of shares under award (31/12/16)	Face value[3]	% vesting at threshold[4,5]	Performance measures	Performance period ends	Holding period ends
Phillip Monks											
PSP Award (nil-cost option)[6]	02/03/15	351,562	–	–	–	351,562	£674,999	10%	50% based on absolute TSR 50% based on EPS	31/12/17	02/03/20
Pre-IPO Award (conditional award)	02/03/15	684,163	–	–	684,163	–	£1,313,593	20%	100% based on absolute TSR	31/12/16	N/A
DSP Award (nil-cost option)[6]	21/03/16	–	111,784	–	–	111,784	£254,566	N/A	N/A	N/A	21/03/17, 21/03/18 and 21/03/19 in relation to tranches of 1/3 of the award
PSP Award (nil-cost option)[6]	21/03/16	–	296,403	–	–	296,403	£674,999	10%	50% based on relative TSR 50% based on EPS	31/12/18	21/03/21
James Mack											
PSP Award (nil-cost option)[6]	02/03/15	218,750	–	–	–	218,750	£420,000	10%	50% based on absolute TSR 50% based on EPS	31/12/17	02/03/20
Pre-IPO Award (conditional award)	02/03/15	613,828	–	–	613,828	–	£1,178,550	20%	100% based on absolute TSR	31/12/16	N/A
DSP Award (nil-cost option)[6]	21/03/16	–	79,179	–	–	79,179	£180,314	N/A	N/A	N/A	21/03/17, 21/03/18 and 21/03/19 in relation to tranches of 1/3 of the award
PSP Award (nil-cost option)[6]	21/03/16	–	207,482	–	–	207,482	£472,499	10%	50% based on relative TSR 50% based on EPS	31/12/18	21/03/21

1 Shows the maximum number of shares that could be received, before any dividend equivalents, if the awards vested in full.

2 Performance was assessed following the end of the performance period and it was determined that the minimum level of performance had not been achieved.

3 Face value for awards made in 2015 was calculated using the final offer price of the Company's shares at IPO (192p). For awards made in 2016, the average middle market quotation over the three-day period 16–18 March 2016 (227.73p) was used to calculate face value. The relevant price was multiplied by the maximum number of shares that would vest if all performance measures and targets were met in full. Actual value at vesting will depend on actual share price at the time of vesting, and any dividend equivalents (if any) payable on vested shares.

4 Assumes that either the TSR or EPS performance measure threshold is met in respect of one half of the PSP award, and that the other half of the award lapses.

5 Vesting is also subject to underpin performance conditions. Further detail on performance conditions is provided at page 83.

6 Nil-cost options lapse ten years after the date of grant to the extent not previously exercised.

All-employee share plans

Executive Directors are invited to participate in all-employee share plans on the same basis as other Group employees. The purpose of these plans is to encourage share ownership by employees, thereby allowing them to share in the long-term success of the Group and align their interests with those of shareholders. The plans are operated within the maximum participation levels permitted under HMRC regulations from time to time. The Company has established both a Sharesave and a Share Incentive Plan ("SIP"). Details of the participation by the Executive Directors in the Sharesave Plan are set out below:

Sharesave participation

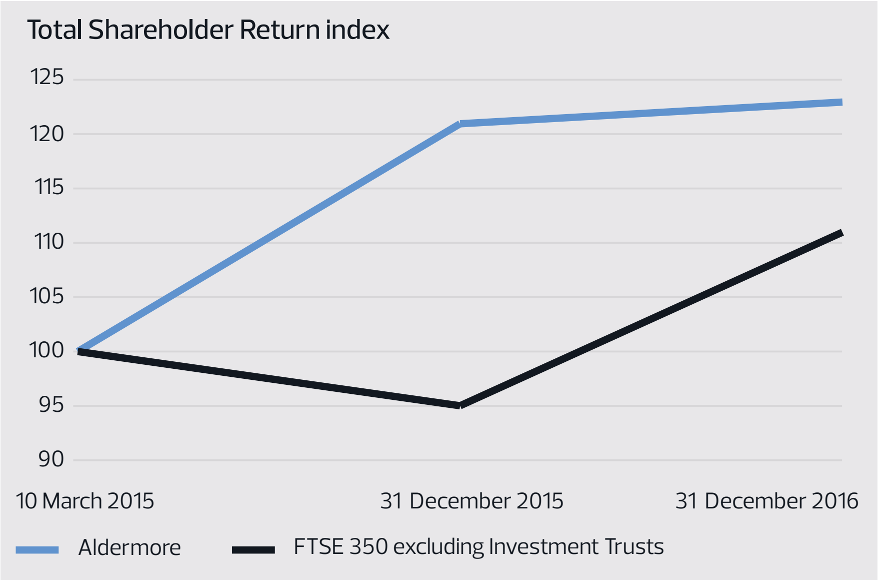
	Type of award	Date of grant	No of shares under option	Lapsed during 2016	Balance (31/12/16)	Option price (p)	Performance conditions	Normal exercise period	Market value at date of grant (£)[1]
Phillip Monks									
	Sharesave (option)	29/10/15	7,142	7,142	–	252	N/A	01/02/19–31/07/19	18,712
	Sharesave (option)	12/10/16	11,688	–	11,688	154	N/A	01/12/19–30/05/20	20,279
James Mack									
	Sharesave (option)	12/10/16	11,688	–	11,688	154	N/A	01/12/19–30/05/20	20,279

[1] Share price on the date of grant for the 2015 and 2016 invitations was 262p and 173.5p respectively.

The SIP was used as a vehicle to award free shares to employees following IPO in recognition of their contribution to the business. Awards of between £200 and £1k were made, based on length of service. The awards vested immediately on grant and are included in the share interests table on page 88.

Performance graph

This graph compares the Total Shareholder Return of £100 invested in the Company's shares and £100 invested in the FTSE 350 (excluding Investment Trusts). The comparison is made between the date of the IPO and 31 December 2016. This index was selected as the Company has been a member of the FTSE 350 since June 2015 and it provides a widely published and broad equity index.



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Total remuneration table

The table to the right shows the total remuneration figure for the CEO in 2015 and 2016. This includes any short-term and long-term incentives.

CEO remuneration

	2016	2015
Single total figure of remuneration (£'000)	**1,175**	7,297
Annual bonus (as a % of maximum)	**80.7%**	87.3%
Vested long-term incentives (as a % of maximum)[1]	**0**	N/A

[1] No PSP awards vested in 2015 or 2016. See footnote 4 to the single total figure table (page 78) for further detail on gains on shares held pre-IPO.

CEO relative pay

The table to the right shows the percentage change in the salary, taxable benefits and annual bonus of the CEO between 2015 and 2016. A comparison is provided against the average percentage change in respect of the Group's employees taken as a whole. A comparison against the median percentage change is also provided as this is more reflective of actual changes in remuneration.

CEO relative pay

	2015/16 % change		
	Salary	Taxable benefits	Annual bonus
CEO[1]	9.3%	3.3% [2]	2.4%
Average employee	4.1%	14.1%	-4.5%
Median employee	2.6%	0%	-4.8%

[1] The percentage change in the CEO's pay reflects the restructuring of the CEO's remuneration arrangements at IPO.

[2] The percentage change in the CEO's taxable benefits excludes the one-off write-off of a loan of £108,317 in 2015. The loan was made originally to settle tax payable in respect of equity incentives awarded to Phillip Monks prior to the IPO.

Relative importance of spend on pay

The table to the right compares the total remuneration paid in respect of all employees of the Group in 2015 and 2016, and distributions made to shareholders in the same years.

No dividend distributions or share buybacks were made to shareholders in 2015 or 2016 as the Company applied all its retained profits to support the growth of the business.

Relative importance of spend on pay

	2016	2015
Total employee remuneration (£m)	**64.3**	62.1
Total shareholder distributions (£m)	**0**	0

Non-Executive Directors

Non-Executive Directors' fees

The Chairman and Non-Executive Directors are paid a basic fee, whilst the Non-Executive Directors may receive further fees to reflect Board Committee or additional responsibilities.

The current fee structure was agreed at the time that the Board was put together in preparation for IPO on the basis of a benchmarking exercise against financial services companies of a similar size. The fees are reviewed by the Board (in the case of the Non-Executive Directors) and the Remuneration Committee (in the case of the Chairman) on an annual basis. The most recent review concluded that, with the exception of the fee paid to the Chair of the Remuneration Committee, the fees remained appropriate, and no increases would be made in 2017. With effect from 1 April 2017, the fee paid to the Chair of the Remuneration Committee will be brought into line with that paid to the Chairs of the Audit and Risk Committees (£20k p.a.).

Current fees are set out below:

Non-Executive Directors' Fees

Role	£ (p.a.)
Chairman	180,000
Non-Executive Director	65,000
Senior Independent Director	20,000
Chair of Audit Committee	20,000
Chair of Remuneration Committee	15,000
Chair of Risk Committee	20,000
Membership (other than chairmanship) of the Audit, Remuneration and Risk Committees	5,000

Single total figure table: Non-Executive Directors (audited)

The following table sets out the total remuneration paid to the Non-Executive Directors for the financial years ending 31 December 2016 and 31 December 2015.

			Fees[1]		Taxable benefits[2]		Long-term incentives		Total	
	Appointment date (if later than 1 January 2015)	Resignation date (if earlier than 31 December 2016)	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000	**2016 £'000**	2015 £'000
Glyn Jones			**180**	174	**–**	–	**–**	960[3]	**180**	1,134
Peter Cartwright[4]		18/04/16	**21**	57	**–**	–	**–**	–	**21**	57
Neil Cochrane[4]		14/10/16	**53**	53	**–**	–	**–**	–	**53**	53
Danuta Gray			**90**	100	**1**	2	**–**	–	**91**	102
John Hitchins			**90**	100	**–**	–	**–**	–	**90**	100
Chris Patrick[4]	21/11/16		**8**	–	**–**	–	**–**	–	**8**	–
Robert Sharpe	29/06/15		**75**	38	**–**	–	**–**	–	**75**	38
Peter Shaw			**95**	103	**3**	4	**–**	–	**98**	107
Chris Stamper			**75**	85	**1**	1	**–**	–	**76**	86
Cathy Turner			**80**	90	**–**	–	**–**	–	**80**	90
Total			**767**	800	**5**	7	**–**	960	**772**	1,767

1 The fees paid to the Non-Executive Directors relate to the period for which they held office.

2 "Taxable benefits" includes the tax liability due on travel expenses. The figures disclosed in the 2015 Annual Report and Accounts were an estimate of the amount due, and the 2015 figures above have therefore been restated to reflect actual amounts paid.

3 The gain on Glyn Jones' personal investment in certain shares prior to IPO has been included within 2015 remuneration under "Long-term incentives" (calculated at the market value of shares held at IPO (£1.92) less the original cost of his personal investment). Such shares were not part of an incentive subject to any form of performance hurdles and his only ongoing financial interest in the performance of the Company is as an ordinary shareholder.

4 Peter Cartwright, Neil Cochrane and Chris Patrick were all appointed to represent the Company's Principal Shareholders, and their fees are paid directly to these entities. Further information on the relationship with the Principal Shareholders can be found in Note 41 to the financial statements (related parties).

Corporate governance

Remuneration Report
Annual Report on Remuneration continued

Other

Shareholdings

In order to further align the interests of Executive Directors with those of shareholders, the Company has implemented share ownership guidelines. The guidelines require the Executive Directors to build up a specified level of shareholding (expressed as a percentage of base salary) within five years of the guidelines being implemented (or within five years of appointment, if later).

The required level of shareholding is 200% of base salary, using the current share price from time to time, for each of the Executive Directors. Under the guidelines, the Executive Directors are expected to retain all of the ordinary shares vesting under any of the employee share plans, after any disposals for the payment of applicable taxes and any acquisition costs, until they have achieved the required level of shareholding. Vested awards not subject to any performance condition (but subject to a holding period) count as ownership towards the guidelines after deducting the tax which would be due if the shares were released on that date. The guidelines also prohibit the Executive Directors from hedging (or offering as collateral) any shares which are unvested or unexercised under any employee share plans, and any shares which count towards meeting the guidelines.

Other shares owned by Executive Directors and their connected persons also count towards the share ownership guidelines. Both Executive Directors have met the guideline levels.

Details of the Executive Directors' beneficial interests (and their connected persons) in the Company's shares as at 31 December 2016 are set out below:

Executive Directors' shareholdings (audited)

Name	**Shareholding as at 31 December 2016**	Shareholding as at 31 December 2015	Share ownership guideline (% of base salary)	Current holding (% of base salary)[1]	Share awards/ options (subject to performance/ service conditions)[2]	Options (not subject to performance/ service conditions)[2]
Phillip Monks	**3,462,693**	3,462,693	200%	1,600%	759,749	11,688
James Mack	**436,659**	436,659	200%	288%	505,411	11,688

1 Current holding measured by reference to the middle market quotation of the Company's share price on 31 December 2016 (236.8p) and as a percentage of base salary at 31 December 2016.

2 Awards which have not yet vested do not count towards compliance with the share ownership guidelines.

3 There have not been any changes to Directors' shareholdings between the end of the financial year and the date that this Remuneration Report was signed.

The beneficial interests of the Non-Executive Directors (and their connected persons) in the Company's shares as at 31 December 2016 is set out below:

Non-Executive Directors' shareholdings (audited)

Director	**Shareholding as at 31 December 2016**	Shareholding as at 31 December 2015
Glyn Jones	**881,488**	781,488
Peter Cartwright[1, 2]	**–**	–
Neil Cochrane[1, 2]	**–**	–
Danuta Gray	**–**	–
John Hitchins	**20,000**	20,000
Chris Patrick[1]	**–**	–
Robert Sharpe	**–**	–
Peter Shaw	**–**	–
Chris Stamper	**9,500**	9,500
Cathy Turner	**42,336**	42,336

1 Appointed to act as a Director by the Principal Shareholders, whose interest in the Company's shares is set out on page 104.

2 Shareholding disclosed as at 31 December 2015 and date of resignation.

3 There have not been any changes to Directors' shareholdings between the end of the financial year and the date that this Remuneration Report was signed.

Payments to past Directors and loss of office payments (audited)

There were no payments made during the year to any person who was not a Director of the Company at the time the payment was made, but had previously been a Director. There were also no payments for loss of office made during the year.

External appointments

The Company's policy is that Executive Directors may hold one external non-executive directorship, subject to prior approval by the Company. Neither of the Executive Directors hold any external directorships at the current time.

Employee share trust

The Company has established the Aldermore Group PLC Employees' Share Trust (the "Trust"), a discretionary share trust, for the purpose of facilitating the operation of the Company's share plans. It is the Company's current intention to satisfy any vested share awards by the allotment of new shares to the Trust.

Dilution

As noted above, the Company intends to issue new shares to satisfy awards outstanding under employee share plans, and will implement these arrangements in accordance with the Investment Association Guidelines on dilution. Based on the number of awards outstanding as at 31 December 2016, the levels of dilution, which are within the dilution limits set by the Investment Association, are as set out in the table below. For the purpose of these calculations, executive awards granted prior to IPO are excluded in accordance with the relevant plan rules and as disclosed in the IPO Prospectus.

Dilution

Plan	% of the Company's issued share capital	Investment Association dilution limit (%)
All share plans	1.15%	10
Executive share plans	0.65%	5

Corporate governance

Remuneration Report
Annual Report on Remuneration continued

Remuneration Committee at a glance

- The Remuneration Committee is currently composed of three Independent Non-Executive Directors and the Company Chairman, which meets with Code requirements:
  - Cathy Turner (Chair), Independent Non-Executive Director
  - Danuta Gray, Interim Chairman[1]
  - Peter Shaw, Independent Non-Executive Director
- Glyn Jones was also a member of the Remuneration Committee throughout 2016 until his resignation as Company Chairman with effect from 6 February 2017
- Regular attendees at meetings of the Remuneration Committee include the CEO, Group HR Director, Company Secretary and FIT Remuneration Consultants LLP (who provide independent remuneration consultancy services)
- The Remuneration Committee's key role is to set the remuneration policy and individual terms for the Executive Directors, Chairman and other members of the senior management team
- Remuneration for the Non-Executive Directors is determined by the Board of Directors
- No person participates in any discussion relating to their own remuneration
- The Remuneration Committee's terms of reference are reviewed annually and are available at www.investors.aldermore.co.uk

[1] It is anticipated that, once appointed, the new Company Chairman will join the Committee as a member. Danuta Gray will remain a member in her capacity as Senior Independent Director.

Remuneration Committee

External advisers

In April 2014, the Remuneration Committee engaged FIT Remuneration Consultants LLP ("FIT") for the provision of independent remuneration advisory services following a competitive tender process. FIT does not provide any other services to the Group. FIT is a member of the Remuneration Consultants Group and adheres to its code of conduct. The Remuneration Committee reviews the effectiveness of its adviser on an annual basis, and remains satisfied that the advice that it has received from FIT during the year has been objective and independent. Total fees paid to FIT during the year amounted to £126.5k, which was charged on its normal terms.

Statement of voting at the Annual General Meeting

The results of the shareholder votes at the Company's 2016 AGM on the Remuneration Policy and the 2015 Annual Report on Remuneration are as below:

Committee effectiveness

The Remuneration Committee undertook a review of its own effectiveness through 2016 as part of the wider Board and Committee evaluation exercise. The review took the form of an internal evaluation and was conducted principally by way of a questionnaire that was issued to all Remuneration Committee members.

The review covered various areas including the role and remit of the Remuneration Committee; the effectiveness of the Chair; the appropriateness of information provided to the Remuneration Committee; and the relationship with management. The Remuneration Committee discussed the outcome of the review in 2017. The Remuneration Committee confirmed that it operated effectively and that there were no significant areas for concern. Further information about the Board and Committee effectiveness process is set out on pages 56 and 57.

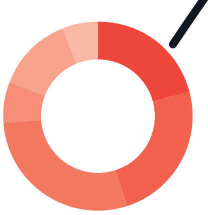
	Votes for	Votes against	Votes withheld
Directors' Remuneration Policy	93.68%	6.32%	3,567,454
Annual Report on Remuneration	93.93%	6.07%	3,604,881

The Remuneration Committee was pleased with the strong level of support in favour of these resolutions.

Responsibilities of the Remuneration Committee

- Setting remuneration policy for Executive Directors and senior management, and making recommendations to the Board on overall remuneration costs
- Determining individual remuneration arrangements for the Executive Directors, senior management and other staff falling within the remit of the FCA and PRA Remuneration Codes ("Identified Staff")
- Approving the Chairman's remuneration
- Reviewing pay and bonus allocations across the wider Group
- Reviewing the design of performance-related incentive schemes for recommendation to the Board. Once in place, agreeing targets and assessing the outcomes
- Reviewing recruitment and termination arrangements for Executive Directors, senior management and Identified Staff
- Engaging with shareholders on remuneration-related matters

Time spent in 2016



Key topics discussed at Remuneration Committee meetings in 2016

Key:
- Reviewed
- Recommended to Board
- Approved

Topic	Activity	Action
Governance	Compliance with share ownership guidelines and anti-hedging policy	Reviewed
	Annual programme of items for Remuneration Committee meetings in 2017	Approved
	Annual review of Remuneration Committee effectiveness	Approved
	Annual review of the effectiveness of the Committee's remuneration adviser	Approved
	Annual reporting, including Remuneration Report and Pillar 3 disclosures	Reviewed
Individual remuneration arrangements	Annual review of the Chairman's remuneration	Approved
	Bonus outturn, awards to be made, and fixed pay for all employees falling within the Remuneration Committee's remit	Approved
Performance-related incentive schemes	2015 AIP outturn	Approved
	Performance measures and targets in relation to awards under the 2016 AIP	Approved
	Parameters and quantum of awards to be made under the PSP and RSP in 2016	Approved
	Regular review of performance under performance-related incentive schemes, including the operation of business incentive plans within the divisions	Reviewed
	Vesting of the Pre-IPO Awards	Approved
Regulatory matters	Impact of EU Market Abuse Regulation on share plan awards and vestings	Reviewed
	Preliminary view of the outcome of reporting under gender pay gap regulations	Reviewed
Remuneration arrangements in wider Group	2016 payouts under the all-employee bonus scheme, and confirmation of 2017 budget	Approved
	2016 salary review	Approved
	2016 Sharesave invitation	Approved
	Review of benefits across the Group	Reviewed
	Renewals of health insurance policies	Approved
Setting remuneration policy	Annual review of the Directors' Remuneration Policy	Recommended to Board
	Guidelines for the application of Remuneration Policy for leavers	Approved

In addition, regular reports included updates on changes to Identified Staff, treatment of joiners and leavers (in accordance with delegated authorities), and consideration of market and regulatory updates.

The Remuneration Report was approved by the Board of Directors on 1 March 2017 and signed on its behalf by:

Cathy Turner,
Chair of Remuneration Committee

Corporate governance

Remuneration Report Appendix
Remuneration Policy

Introduction

For ease of reference, this appendix sets out an extract of our Remuneration Policy, which was approved by shareholders at the 2016 AGM held on 17 May 2016 and took effect from that date. It is intended that the Remuneration Policy will operate until the 2019 AGM unless any significant changes are proposed in the interim. No changes are proposed to the Remuneration Policy this year, and a shareholder vote on it will not therefore be required at the 2017 AGM.

The full Remuneration Policy, as approved by shareholders, can be found on pages 95 to 103 of the 2015 Annual Report and Accounts on the Company's website at www.investors.aldermore.co.uk

The Remuneration Policy is based on the following key principles:

Aligned to the long-term success of the Group

The remuneration framework is structured to align remuneration, and in particular performance-related remuneration, with the long-term interests of shareholders. Incentive plans should be designed such that they do not encourage excessive risk-taking.

Competitive but not excessive

The Group recognises that its long-term success is closely linked to its ability to attract and retain high-calibre individuals who can drive the delivery of its business strategy. However, this should be balanced with ensuring that remuneration is appropriate to the role, responsibilities, experience and performance of the individual, and is not excessive.

Appropriate and balanced proportion of variable pay

Total remuneration should balance both fixed and variable elements, whilst variable pay should be balanced between both short-term and long-term incentives with an emphasis on achieving sustainable business results.

Simplicity and transparency in the design and communication

The key to an effective remuneration structure is that the link between incentives and performance is clear, well-communicated and easily understood.

To see how the Remuneration Policy was implemented in 2016, please refer to the Annual Report on Remuneration on pages 76 to 89.

Future policy table

Executive Directors' fixed pay

Element and purpose	Policy and operation	Maximum	Performance measures	Committee flexibility
Base salary To provide a fair level of fixed pay which reflects the individual's experience and contribution To attract and retain the high-calibre individuals necessary to deliver the Group's strategy	Typically paid monthly in cash and reviewed annually The annual review takes into account various factors including: · corporate and individual performance · any change in an individual's role and responsibilities · market benchmarking · average pay increases awarded across the Group as a whole Market benchmarking primarily takes into account pan-sector companies of a similar market capitalisation rather than looking at companies solely within the financial services sector. However, the Remuneration Committee may also consider more specific data and uses all data as a reference point in considering, in its judgement, the appropriate level of salary	Although an annual review of salaries is normally undertaken, the Remuneration Committee will not automatically award an increase The Remuneration Committee may freeze salaries with consequently larger increases as and when an increase is awarded Increases will normally be in line with the average increases for staff The maximum salary increase which the Remuneration Committee may award will not result in the base salary exceeding 110% of median data for an equivalent role within a comparator group of companies (the 20 companies listed on the London Stock Exchange above and below the Company by market capitalisation)	Not applicable	Base salary increases will be awarded at the Remuneration Committee's discretion, taking into account the factors listed
Benefits To provide market-competitive benefits as part of an overall package which attracts and retains Executive Directors	A range of benefits is provided, which includes: · car allowance · private medical insurance (family cover) · life assurance · income protection · critical illness insurance Certain costs relating to Executive Director relocations will be met where appropriate	Benefits will not exceed 15% of an Executive Director's base salary on an annual basis (plus a further 100% in the case of a Director who has been relocated) As premiums are not taxable as benefits in kind, the following caps apply to life assurance and income protection: · life assurance: up to 8 times salary, although currently capped at 4 times salary · income protection: up to 75% of salary The value of such benefits is outside of the above cap The Remuneration Committee will monitor the costs in practice and ensure that the overall costs do not increase by more than it considers appropriate in all circumstances	Not applicable	The Remuneration Committee reserves the discretion to introduce new benefits as appropriate

Corporate governance

Remuneration Report Appendix
Remuneration Policy continued

Element and purpose	Policy and operation	Maximum	Performance measures	Committee flexibility
Pension To enable Executive Directors to build long-term savings for retirement, within a market-competitive package To attract and retain high-calibre individuals	Contributions may be paid into personal pension arrangements or as a cash supplement (reduced for the impact of employers' NICs)	Up to 15% of base salary p.a. This is higher than was set out in the IPO Prospectus – although there are no plans to change pension contributions currently, this higher cap allows for suitable flexibility	Not applicable	Not applicable
Market adjusted allowance To ensure appropriate weighting of fixed and variable remuneration within an overall market-competitive package The allowance ensures that the gearing of the overall package remains appropriate	A fixed monthly allowance, typically paid in cash Paid on the same basis as salary but will not be taken into account for the purposes of: · incentive pay multiples · pensions or insured benefits · shareholding guidelines · termination or redundancy payments	In order to provide a formal cap, the maximum level of market adjusted allowance will be limited to 50% of base salary p.a. for the duration of this Remuneration Policy. This level is higher than set out in the IPO Prospectus – although there is no current intention to increase the current levels, this ensures that suitable flexibility is retained	Not applicable	Increases in the market adjusted allowance will be awarded at the Remuneration Committee's discretion, but will only be increased if there is a meaningful change in the appropriate market benchmarks Market adjusted allowances may be settled in shares or other instruments

Executive Directors' variable pay

Element and purpose	Policy and operation	Maximum	Performance measures	Committee flexibility
Annual Incentive Plan ("AIP") To motivate Executive Directors and incentivise delivery of performance over a one-year operating cycle, focusing on the short- to medium-term elements of the Group's strategic aims A proportion of the annual bonus is deferred, which encourages a longer-term focus and aligns the interests of the Executive Directors with shareholders	A bonus plan which operates annually. Performance measures are set by the Remuneration Committee at the start of the financial year. Performance targets are assessed by the Remuneration Committee following the year-end and the AIP outcome is agreed At least 40% of the AIP outcome is deferred into shares under the Company's Deferred Share Plan ("DSP"), whilst at least 60% of the AIP outcome is deferred if total variable remuneration exceeds £500,000 p.a. The balance is normally paid in cash The deferred element is typically released in tranches of one-third on the first, second and third anniversaries of the award, subject to continued employment Shares within the DSP may accrue dividend equivalents which may be settled in cash or shares (and which are excluded from the limit in the next column) Both the cash and deferred elements of the bonus may be subject to malus and clawback	The maximum level of AIP outcomes is 125% of base salary p.a.	Performance measures applied may be financial or non-financial and corporate, divisional or individual, and in such proportions as the Remuneration Committee considers appropriate The AIP outcome is determined by assessing each performance measure on the following basis: · attaining the threshold level of performance produces a nil pay-out · a sliding scale (not necessarily straight-line) is applied between the threshold and maximum levels, full pay-out being achieved for this latter level · no more than two-thirds of maximum is payable for on-target performance The Remuneration Committee must be satisfied that the result was achieved consistent with the Group's risk appetite	The Remuneration Committee retains discretion to adjust performance measures and targets during the year to take account of events outside of management control which were unforeseen when the measures and targets were originally set The Remuneration Committee retains a standard power to apply its commercial judgement to adjust the outcome of the AIP for any performance measure (from zero to any cap) should it consider that to be appropriate The Remuneration Committee reserves the right to further modify the operation of the AIP to comply with developments in regulatory requirements and market practice subject to the overall cap. Operation of the AIP and DSP will not, in the Remuneration Committee's view, be made less onerous. In particular, the Remuneration Committee may vary the deferral terms and settle awards in cash, shares and other instruments

Corporate governance

Remuneration Report Appendix
Remuneration Policy continued

Element and purpose	Policy and operation	Maximum	Performance measures	Committee flexibility
Performance Share Plan ("PSP") To motivate and incentivise delivery of sustained performance over the long term, and to promote alignment with shareholders' interests	A long-term incentive plan under which awards are made annually as either nil-cost options or conditional awards Vesting is subject to performance conditions and continued employment over a period of at least three years After the performance period, awards are subject to a holding period of a further two years Shares within the PSP may accrue dividend equivalents which may be settled in cash or shares (and which are excluded from the limit in the next column) Malus and clawback may be applied to PSP awards	The PSP allows for awards over shares with an absolute maximum value of 200% of base salary per financial year Where awards are not made in a financial year due to regulatory constraints, this limit will be carried forward	Performance measures applied may be financial or non-financial and corporate, divisional or individual, and in such proportions as the Remuneration Committee considers appropriate Performance periods will not be less than (but may be longer than) three years No more than 20% of awards vest for attaining the threshold level of performance The Remuneration Committee must be satisfied that the result was achieved consistent with the Group's risk appetite	Awards may be settled in cash or other instruments Once set for an award, performance measures and targets will generally remain unaltered unless events occur which, in the Remuneration Committee's opinion, make it appropriate to substitute or vary them

Non-Executive Directors

Element and purpose	Policy and operation	Maximum	Performance measures	Committee flexibility
Chairman and Non-Executive Director fees To enable the Company to recruit and retain, at an appropriate cost, Non-Executive Directors with the necessary skills and experience to oversee the delivery of the business strategy	Fees of the Chairman and the Non-Executive Directors are set by the Remuneration Committee and the Board respectively Fees are structured as: · basic fee · additional fees for chairmanship and membership of Board Committees · additional fees for further responsibilities (e.g. Senior Independent Director) Fees are reviewed annually. Factors taken into account in the annual review include: · time commitment · equivalent benchmarks to those considered for Executive Directors with a particular emphasis on other banks/ financial services businesses	The aggregate fees (together with any shares and/or benefits including the reimbursement of travel and other expenses, and an amount to meet any tax liability arising on such expenses) of the Chairman and of Non-Executive Directors will not exceed the limit set out within the Company's Articles of Association (currently £2,000,000 p.a.)	Not applicable	Whilst there is no current intention to do so, the Company reserves the right to: · pay some or all of the Chairman's or Non-Executive Directors' fees in shares or other instruments · permit the Chairman or Non-Executive Directors to participate in any benefits in kind · change the basis of paying fees within the constraints of the cap

Recruitment Remuneration Policy

Appointment of Executive Directors

The Remuneration Policy balances the need to have appropriate remuneration levels with the ability to attract high-performing individuals to the organisation. With this in mind, the starting point for the Remuneration Committee in setting a remuneration package for a new Executive Director will be to structure a package in accordance with the Remuneration Policy, based on the individual's knowledge and experience. Consistent with the DRR Regulations, the caps contained within the Remuneration Policy for fixed pay do not apply to new recruits, although the Remuneration Committee does not currently envisage exceeding these caps in practice.

Notwithstanding the general approach set out above, the Remuneration Committee recognises that, when recruiting externally in particular, it may be necessary to compensate an individual to ensure that they are remunerated effectively. The table below sets out areas where the Remuneration Committee may exercise its discretion in order to achieve this. This may arise in particular in relation to bonus and incentive plans given that variable performance-related pay is widely used in the financial services industry to incentivise senior management.

Appointment of Non-Executive Directors

A new Non-Executive Director would be recruited on terms in accordance with the approved Remuneration Policy at that time.

Recruitment Remuneration Policy – Remuneration Committee discretion
Relocation expenses For external and internal appointments, certain relocation expenses may be provided and may be paid over more than one financial year. As set out in the Remuneration Policy, this may be up to a maximum of 100% of base salary p.a. (over and above the general policy on payment of benefits).
AIP The AIP will operate as detailed in the Remuneration Policy (including the maximum award levels). In the year of appointment, at the Remuneration Committee's discretion, the terms of that year's AIP and the performance measures will normally be varied to reflect the part year worked. For an internal appointment, any award under the AIP in respect of the individual's prior role may either continue on its original terms or be adjusted to reflect the new appointment as appropriate. No element of AIP will be guaranteed, unless in the year of joining a guaranteed element is used as part of a buy-out of awards forfeited on leaving the previous employer (see below for further detail).
PSP The PSP will operate as detailed in the Remuneration Policy (including the maximum award levels). For an internal appointment, in line with the AIP, PSP awards in respect of the individual's prior role may either continue on its original terms or be adjusted to reflect the new appointment as appropriate.
Buy-out awards For external candidates, it may be necessary to make additional awards in connection with the recruitment to buy out awards forfeited by the individual on leaving a previous employer. Although these are not subject to a formal cap, the Group will not pay more than is necessary, in the view of the Remuneration Committee, to fairly compensate for awards forfeited on leaving the previous employer to join the Group and will in all cases seek to deliver any such awards under the terms of the existing AIP and PSP. In some cases however, it may be necessary to make such buy-out awards on different terms to reflect better the structure of the awards being bought out. All buy-outs, whether under the AIP, PSP or otherwise, will take account of the service obligations and performance requirements for any remuneration relinquished by the individual when leaving their previous employer. The Remuneration Committee will seek to make buy-outs subject to what are, in its opinion, comparable requirements in respect of service and performance. However, the Remuneration Committee may choose to relax this requirement in certain cases, for example: · where the service and/or performance requirements are materially completed, or · where such factors are, in the Remuneration Committee's view, reflected in some other way, such as a significant discount to the face value of the awards forfeited, or · where necessary to retain compliance with regulatory requirements, such as CRD IV.

Corporate governance

Remuneration Report Appendix
Remuneration Policy continued

Service agreements, payments for loss of office and termination policy

Executive Directors

The terms under which the Executive Directors are appointed are set out in service agreements with the Company. In line with current market practice, the Executive Directors have rolling service agreements, which may be terminated by the Company or the individual on 12 months' notice. The date of each Executive Director's service agreement is 10 March 2015. Copies of the service agreements of the Executive Directors are available for inspection at the Company's registered office. They will also be available for inspection prior to and during the AGM.

Under the service agreements, the Company may make a payment in lieu of notice to an Executive Director. This will be limited to the amount of base salary and, potentially, other fixed benefits for the notice period and may be paid in instalments. The Director is obliged to seek alternative work during this period and the payments may cease or be reduced if the individual finds an alternative role.

Service agreements may be terminated without notice or payment in lieu of notice under a range of circumstances including gross misconduct, fraud or dishonesty, and negligence and incompetence. The agreements do not contain change of control provisions.

The Remuneration Committee is opposed to rewarding failure and, when considering a termination, takes account of all of the information available to it at the time. This policy applies both to any negotiations linked to notice periods on a termination and any treatments which the Remuneration Committee may choose to apply under the discretions available to it under the terms of the AIP, DSP and PSP. The potential treatments on termination under these plans are summarised below.

Plan	"Approved leaver" (e.g. death, injury or disability, redundancy, retirement) or otherwise at the discretion of the Remuneration Committee (including on resignation)	"Unapproved leaver" (e.g. resignation)	Termination by the Company for misconduct	Other exceptional cases (e.g. change of control, winding up of the Company)
Annual Incentive Plan ("AIP")	Payment of the award is at the discretion of the Remuneration Committee. Award usually time pro-rated for the period of service and released at the end of the performance period, subject to assessment of performance conditions.	No awards made for the year of leaving.	No awards made for the year of leaving.	Payment of the award is at the discretion of the Remuneration Committee. Award usually time pro-rated subject to satisfaction of performance conditions, which are assessed over the period to the date of the event.
Deferred Share Plan ("DSP")	Unvested awards will vest at the original vesting dates. However, the Remuneration Committee retains discretion to accelerate vesting to the date of cessation.	If leaving before the employment requirement date[1] all unvested awards will lapse. If leaving after the employment requirement date[1], unvested awards will vest at the original vesting dates. However, in this case the Remuneration Committee retains discretion to accelerate vesting to the date of cessation.	All unvested awards will lapse.	Awards will normally vest early, but may be exchanged for a new award over shares in the acquiring company in the case of an internal reorganisation.

Performance Share Plan ("PSP")	If leaving before the employment requirement date[2], awards will vest at the original vesting date on a time pro-rated basis for the period of service and subject to performance conditions. If leaving after the employment requirement date[2] but before the end of the holding period, unvested awards will vest at the original vesting dates. Under both scenarios, the Remuneration Committee retains discretion to accelerate vesting to the date of cessation. The Remuneration Committee also has discretion to reduce or disapply the time pro-rating.	If leaving before the employment requirement date[2] all unvested awards will lapse. If leaving after the employment requirement date[2] but before the end of the holding period, unvested awards will vest at the original vesting dates. However, in this case the Remuneration Committee retains discretion to accelerate vesting to the date of cessation.	All unvested awards will lapse.	Awards will normally vest early, but may be exchanged for a new award over shares in the acquiring company in the case of an internal reorganisation. The extent to which the award vests will be determined by review of performance conditions and applying time pro-rating. The Remuneration Committee has discretion to reduce or disapply the time pro-rating.

1 The first, second and third anniversaries of the date of grant (as appropriate).

2 The employment requirement date is the third anniversary of the date of grant.

The Remuneration Committee may also approve payment of amounts in settlement of statutory or contractual claims based on legal advice and may make payment of an amount in respect of legal, tax and outplacement services as it considers appropriate.

Chairman and Non-Executive Directors

The Non-Executive Directors (including the Chairman) are appointed pursuant to letters of appointment, which set out the terms of their appointment. The appointment is subject to termination by the Company at any time with three months' written notice. Directors are requested, but not obliged, to give three months' notice. The letters do not provide for compensation for loss of office. All Non-Executive Directors are subject to annual re-election by shareholders at the AGM, however should the Director not be re-elected by shareholders their appointment will cease immediately and without compensation.

Copies of the letters of appointment of the Non-Executive Directors are available for inspection at the Company's registered office. They will also be available for inspection prior to and during the AGM.

Corporate governance

Directors' Report

The Directors present their report and the financial statements of the Group for the year ended 31 December 2016. As permitted by legislation, some of the matters normally included in the Directors' Report are included by reference as detailed below.

		Where to find further information:	
Requirement	Detail	Section	Location
Business review and future developments	Information regarding the business review and future developments, key performance indicators and principal risks are contained within the strategic report.	Strategic report	Pages 16 to 30 (business review and future developments) Page 15 (key performance indicators) Page 33 (principal risks)
Corporate governance statement	The corporate governance section provides full disclosure of the Group's corporate governance arrangements. The Group has complied fully with the provisions of the UK Corporate Governance Code 2014 during the year.	Corporate governance	Pages 39 to 105
Results	The results for the year are set out in the income statement. The profit before taxation for the year ended 31 December 2016 was £128.7m (2015: £94.7m). A full review of the financial performance of the Group is included within the strategic report.	Income statement Strategic report	Page 148 Pages 1 to 38
Dividend	The Directors do not propose to recommend a final dividend in respect of the year ended 31 December 2016.	–	–
Financial instruments	The Group uses financial instruments to manage certain types of risk, including liquidity and interest rate risk. Details of the objectives and risk management of these instruments are contained in the risk management section.	Risk management	Pages 106 to 139
Post balance sheet events	There have been no material post balance sheet events.	–	–
Share capital	At 31 December 2016, the Company's share capital comprised 344,739,584 ordinary shares of £0.10 each. The Company did not repurchase any of the issued ordinary shares during the year or up to the date of this report. The powers of the Directors, including in relation to the issue or buyback of the Company's shares, are set out in the Companies Act 2006 and the Company's Articles of Association. The Directors were granted authority to issue and allot shares at the 2016 AGM. This authority expires at the end of the next AGM or, if earlier, on 30 June 2017. Shareholders will be asked to renew the authority to issue and allot shares at the 2017 AGM.	Note 36 to the consolidated financial statements	Pages 185 to 186

Requirement	Detail	Where to find further information: Section	Location
Rights and obligations attaching to shares	There are no restrictions on the transfer of the Company's ordinary shares or on the exercise of the voting rights attached to them, except for: · where the Company has exercised its right to suspend their voting rights or prohibit their transfer following the omission by their holder or any person interested in them to provide the Company with information requested by it in accordance with Part 22 of the Companies Act 2006; or · where their holder is precluded from exercising voting rights by the Financial Conduct Authority's Listing Rules or the City Code on Takeovers and Mergers. All the Company's ordinary shares are fully paid and rank equally in all respects and there are no special rights with regard to control of the Company. Under the Relationship Agreement entered into by the Principal Shareholders, AnaCap Derby Co-Investment (No.1) L.P. has agreed for so long as it holds in excess of 4.99% of the ordinary shares in the Company, that save in limited circumstances, it shall not exercise any voting rights in respect of, or sell or transfer (except for a permitted sale or transfer), any ordinary shares in the Company beneficially owned, directly or indirectly, by it.	–	–
Employees share scheme rights	Details of how rights of shares in employee share schemes are exercised when not directly exercisable by employees are provided in Note 37 to the consolidated financial statements.	Note 37 to the consolidated financial statements	Page 188
Employees	The Group is committed to employment policies, which follow best practice, based on equal opportunities for all employees, irrespective of gender, race, colour, age, disability, sexual orientation or marital or civil partner status. The Group is 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. Information on employee involvement and engagement can be found in the strategic report.	Strategic report	Pages 15 and 37
Directors	The names and biographical details of the current Directors who served on the Board and changes to the composition of the Board that have occurred during 2016 and up to the date of this report are provided in the corporate governance section and are incorporated into the Directors' Report by reference.	Corporate governance – Board of Directors	Pages 42 and 43

Corporate governance

Directors' Report
continued

Requirement	Detail	Where to find further information: Section	Location
Disclosure of information under Listing Rule 9.8.4R	Details of any long-term incentive schemes	Note 37 to the consolidated financial statements	Pages 186 to 189
	Agreement with the Principal Shareholders	Relations with shareholders	Page 59
	Contracts of significance	Note 41 to the consolidated financial statements	Page 192
	Dividend waivers	Note 36 to the consolidated financial statements	Page 185 and 186
Appointment and retirement of Directors	The appointment and retirement of the Directors is governed by the Company's Articles of Association, the UK Corporate Governance Code 2014 and the Companies Act 2006. The Company's Articles of Association may only be amended by a special resolution passed by shareholders at a general meeting. In accordance with the the UK Corporate Governance Code 2014, all of the Directors will retire and offer themselves for reappointment or appointment (in the case of Chris Patrick) at the 2017 AGM. Under the Relationship Agreement, the Principal Shareholders are entitled for such time as they have: (i) an interest of 20% or more in the Company, to appoint two Non-Executive Directors; and (ii) less than a 20% interest but an interest of 10% or more in the Company, to appoint one Non-Executive Director. Such appointments are subject to election/re-election at the AGM.	Corporate governance – election and re-election	Page 52
Directors' indemnities	The Directors who served on the Board during 2016 and up to the date of this report have benefited from qualifying third-party indemnity provisions by virtue of deeds of indemnity entered into by the Directors and the Company. The deeds indemnify the Directors to the maximum extent permitted by law and by the Articles of Association of the Company, in respect of liabilities (and associated costs and expenses) incurred in connection with the performance of their duties as a Director of the Company and any associated company, as defined by Section 256 of the Companies Act 2006. The Group also maintains Directors' and Officers' liability insurance which provides appropriate cover for legal actions brought against its Directors.	–	–

Requirement	Detail	Where to find further information: Section	Location
Significant agreements	There are no agreements between any Group company and any of its employees or any Director of any Group company which provide for compensation to be paid to an employee or a Director for termination of employment or for loss of office as a consequence of a takeover of the Company. There are no significant agreements to which the Company is a party that take effect, alter or terminate upon a change of control following a takeover bid for the Company.	–	–
Political donations	The Group made no political donations during the year.	–	–
Research and development activities	The Group does not undertake formal research and development activities. However, new products and services are developed in each of the business lines in the ordinary course of business in accordance with the Group's product and pricing governance framework. Under this framework, all new products, campaigns and business initiatives are reviewed and approved by the Group's Product and Pricing Committee. In addition to new products and services, the Group also invests in internally generated intangible assets including computer systems.	Note 28 to the consolidated financial statements	Pages 182 and 183
Emissions reporting	Details relating to required emissions reporting are set out on page 105.	Directors' Report	Page 105
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 under a range of stressed scenarios. 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.	–	–

Corporate governance

Directors' Report continued

Requirement	Detail	Where to find further information: Section	Location
Disclosure of information to auditors	Each person who is a Director at the date of this Directors' Report confirms that: · so far as the Director is aware, there is no relevant audit information of which the Group's auditors are unaware; and · he or she has taken all the steps that he or she ought to have taken as a Director to make himself or herself aware of any relevant audit information and to establish that the Group's auditor is aware of that information. This confirmation is given and should be interpreted in accordance with the provisions of the Companies Act 2006.	–	–
Auditor	Following a competitive tender process, the Board recommended that Deloitte LLP be appointed as the Group's auditor with effect from the 2017 AGM, at which resolutions concerning Deloitte's appointment and authorising the Board to set their remuneration will be proposed.	Audit Committee Report	Page 68
Annual General Meeting (AGM)	The AGM will be held at 11.00am on 16 May 2017 at the offices of Linklaters LLP, 1 Silk Street, London, EC2Y 8HQ. The Notice of AGM, together with an explanation of the items of business to be discussed at the meeting, will be posted to shareholders and made available on the Group's website. A resolution will be proposed at the 2017 AGM to amend the Company's Articles of Association so that future AGMs may be held electronically.	Group website	www.investors.aldermore.co.uk

Substantial shareholdings

In accordance with the Disclosure and Transparency Rules, the Company (as at the date of this report) has been notified of the following interests in its ordinary share capital:

	As at 31 December 2016			As at 1 March 2017		
Shareholder	Ordinary shares held	% of voting rights	Nature of holding	Ordinary shares held	% of voting rights	Nature of holding
AnaCap Financial Partners L.P.[1]	28,702,806	8.33%	Direct	28,702,806	8.33%	Direct
AnaCap Financial Partners II, L.P.[1]	37,964,311	11.01%	Direct	37,964,311	11.01%	Direct
AnaCap Derby Co-Investment (No. 1) L.P.[1]	38,821,660	11.26%	Direct	38,821,660	11.26%	Direct
AnaCap Derby Co-Investment (No. 2) L.P.[1]	32,897,211	9.54%	Direct	32,897,211	9.54%	Direct
Norges Bank	10,333,531	3.00%	Direct (2.97%) and qualifying financial instruments (0.03%)	10,358,946	3.00%	Direct
Standard Life Investments (Holdings) Limited[2]	18,656,326	5.41%	Indirect	17,696,294	5.13%	Indirect

1 These shareholdings represent the interests of the Principal Shareholders who hold 40.14% of the ordinary shares in the Company.

2 Since 31 December 2016, the Company has been notified that Standard Life Investments (Holdings) Limited decreased its shareholding on 13 January 2017 to below 5% and increased its shareholding on 27 January 2017 as set out above.

Emissions reporting

Greenhouse gas emissions

The Group's greenhouse gas ("GHG") emissions for 2016 were 525 tonnes of carbon dioxide equivalent (tCO_2e) equating to 0.59 tCO_2e per employee. In 2016, the Group established an energy baseline against which it can report in future years.

GHG emissions for the Group have been collated and calculated for all UK operations where the Group is responsible for the combustion of fuel or energy used in the operation of facilities occupied by the Group.

Reporting period

The reporting period for emissions corresponds with the Group's financial reporting period.

GHG scope of disclosure and omissions

GHG emissions disclosure will be limited to Scope 1 and Scope 2 emissions only as data was not readily available for Scope 3 emissions. Scope 1 includes fuel emissions from buildings and company vehicles and Scope 2 includes our emissions from electricity. Disclosure of Scope 3 emissions is voluntary under the regulations.

Heat and electricity supplied by landlords to premises occupied by the Group, where the heat or electricity is not separately reported or charged outside of the general building service charge, has not been included in this year's report due to lack of data. Methods to obtain this data or reliable methods for estimation will be investigated and if suitably accurate data can be obtained, this will be included in future year's reports.

GHG data integrity and calculation method

The data included in this report has been taken from multiple sources, namely: utility billed data, existing internal calculations, existing external calculations from landlords, and expense claims in relation to transport usage. It has not been possible to obtain some data for the reporting period. Where this is the case, data has been estimated either by using data from an earlier period or extrapolating existing data. Fuel consumption from vehicles for business travel was estimated from expense claim costs.

Conversion factors used in this report have been taken from the Department for Business, Energy and Industrial Strategy's "Greenhouse Gas Conversion Factor Repository" and the report has been compiled in line with the Department for Environment, Food & Rural Affairs' "Environmental Reporting Guidelines: Including mandatory greenhouse gas emissions reporting guidance".

GHG reduction plan

The Group is committed to reducing GHG emissions. The opportunities for energy savings identified through the Group's ESOS (Energy Saving Opportunity Scheme) assessment, completed in January 2016, are being progressed and implemented as appropriate.

GHG data verification

All data used for GHG emissions reporting was compiled and calculated by JRP Solutions Ltd, an independent energy specialist.

On behalf of the Board:

Rachel Spencer,
Company Secretary
1 March 2017

GHG emissions summary (tCO_2e)

Scope		2015	**2016**
Scope 1	Company transport	237	175
Scope 2	Electricity	484	350
Total GHG emissions		**721**	**525**
Average number of employees		845	887
Total per employee		**0.85**	**0.59**

Risk management

The Group's approach to risk	**107**
Risk governance and oversight	**110**
Stress testing	**111**
Principal risks	**112**

The Group's approach to risk

In this section:

The Group's approach to risk	107
Risk governance and oversight	110
Stress testing	111
Principal risks	112

All areas of the following report are covered by the external auditor's opinion on page 142, except for the leverage ratio disclosed on page 128, the risk weighted assets and associated capital ratios on page 129 and the shaded sections on pages 135 to 139.

Effective risk management plays a key role in the execution of the Group's strategy of supporting UK SMEs, homeowners, buy-to-let investors and savers. Risk taking is an inherent part of banking and, within an effective risk management framework, we aim to generate strong sustainable returns for shareholders. The Board and senior management seek to ensure that the risks the Group are taking are clearly identified, managed, monitored and reported and that the Group's resources are capable of withstanding both expected and unexpected levels of risk performance.

The Risk Overview on pages 32 to 35 provides a summary of the risk management framework within the Group. It highlights the principal risks we face, together with emerging risks and the mitigating actions we are taking to address these challenges. This detailed Risk Management Section provides additional information on our approach to risk, the associated governance framework, stress testing and provides a fuller analysis of the principal risks.

Risk Strategy

We have clearly defined our risk management objectives and have a strategy to deliver them. Our risk management strategy is to:

- Identify our principal and emerging risks
- Define our risk appetite and ensure that the business plans are consistent with it
- Ensure that the risk appetite and business plans are supported by effective risk controls, technology, and people capabilities
- Manage the risk profile to ensure that the business strategy can withstand a range of adverse conditions identified in stress testing
- Ensure a sound risk control environment and risk-aware culture
- Manage risk within the business units with effective independent oversight
- Construct our compensation practices to ensure only prudent risk taking, within our risk appetite, is rewarded.

Risk management

The Group's approach to risk
continued

Risk Management Framework

The Risk Management Framework ("RMF") refers to the process of identifying, managing, monitoring and reporting the risks to which the Group is exposed. The RMF is supported by supplemental frameworks, policies, processes and procedures. These combine to ensure that our risks are managed in a manner which is appropriate to the size and nature of the Group's operations. They are aligned to regulatory requirements and reflect industry practice, as outlined below. The Group will continue to develop and increase its range of products to better serve its customers and so grow the business sustainably in a controlled manner within the overall RMF.

What risks and regulatory requirements do we face?

Principal Risks

- Credit Risk
- Capital & Liquidity Risk
- Market Risk
- Operational Risk
- Compliance, Conduct & Financial Crime Risk
- Reputational Risk

Emerging Risks

- Regulatory Change/ Intervention
- Economic & Political Environment
- Competitive Environment
- Technology Risk

Legal & Regulatory

How do we manage risks and compliance given the business objectives?

Risk Appetite & Risk Strategy

- Risk appetite statement
- Risk appetite framework
- Risk culture
- Business strategy

Risk Infrastructure

- Governance & committee structure
- 3 lines of defence
- Risk resourcing
- Risk systems
- Reporting & escalation

Risk Life Cycle

- Frameworks
- Policies
- Processes & Procedures
- Segregation of Duties
- Risk Controls & Self Assessments
- Business Assurance
- Change Management

Data, Reporting KPIs/KRIs, Limits

Risk Metrics, Limits & Tolerances

Aggregation

Stress testing: ICAAP, ILAAP, RRP

How do we provide oversight and assurance of risk management and compliance?

Second line – risk oversight

Third line – independent assurance

Risk Appetite Framework

The Risk Appetite Framework ("RAF") is the overarching framework through which we set individual risk appetites for each principal risk. It sets out how we monitor performance against the risk appetites.

The RAF includes the following components:

- Overarching Risk Appetite Statement – this is the primary statement outlining our approach to risk taking linked to the pursuit of our business strategy. This is:

  "To run a sustainable, safe and sound business that conducts its activities in a prudent and reputable manner, taking into account the interest of its customers and also ensuring that our obligations to key stakeholders are met."

- Key risk appetite statements – the articulation of the type and level of specific risks (derived from the principal risks) that we are willing to accept or tolerate
- Risk capacity – the maximum level of risk we can assume before breaching constraints determined by regulatory capital or liquidity needs
- Risk metrics, limits and tolerances – quantitative or qualitative measures that allocate our aggregate risk appetite statements to individual business activities
- Risk profile – the point in time assessment of our risk exposures

Risk Appetite Statement

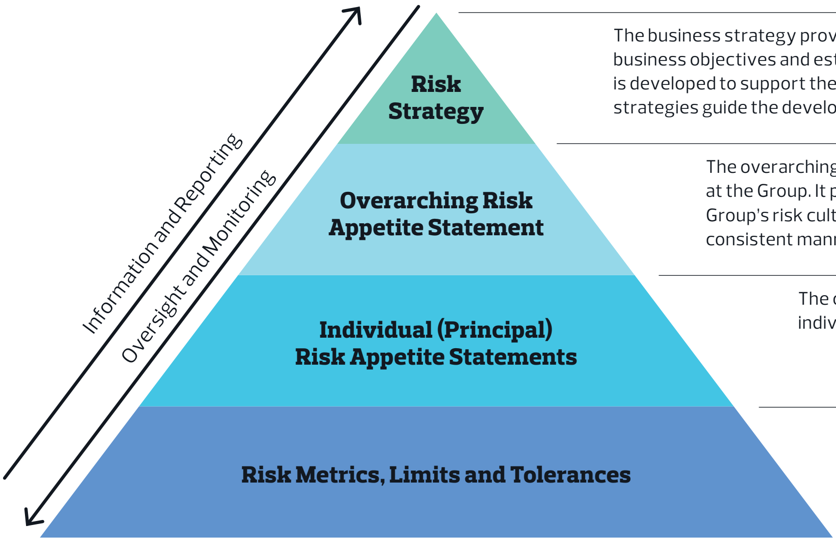
The Group's overarching Risk Appetite Statement, and detailed individual metrics define the amount and nature of risk the Group is willing to accept or tolerate in pursuit of its strategy and business objectives. The Board sets the overall risk appetite of the Group, which is expressed in detail through Principal Risk Appetite Statements, individual metrics and associated limits which are reviewed on an ongoing basis.

In articulating its risk appetite, the Group has taken into consideration the expectations of its stakeholders, the need for regulatory compliance at all times, the preservation of our franchise and reputation and our desire for controlled and sustainable profit growth.

Risk culture

The Board ensures that the Group actively embraces a strong risk culture where all staff are accountable for the risks that they take. Senior management leads in implementing the risk appetite and ensuring that the RMF is fully embedded with a strong focus on the adherence to risk appetite which is monitored through reporting metrics. Staff performance management and reward practices all have key risk inputs, and a focus on risk management in their design.

Risk Appetite Framework



The business strategy provides the context within which the Group outlines its business objectives and establishes its risk management framework. The risk strategy is developed to support the business objectives. Together, the business and risk strategies guide the development of the overarching risk appetite statement.

The overarching risk appetite statement sets the tone for risk management at the Group. It provides a framework to develop and cascade the Group's risk culture and to establish risk policies, controls, and limits in a consistent manner.

The overarching risk appetite statement is supported by individual risk appetite statements for all principal risks.

Risk appetite statements are supported by a range of meaningful and measurable metrics. These metrics can be quantitative or qualitative in nature and are subject to triggers, tolerances and limits.

Risk management

Risk governance and oversight

The Board, often via sub-committees, has responsibility for setting the overall Risk Appetite, understanding the principal risks taken by the Group and setting acceptable limits for these risks utilising the Risk Appetite Framework. As part of this responsibility, the Board reviews and approves the business strategies, principal risk statements, supporting frameworks and certain Group policies. The Board is ultimately responsible for ensuring that an adequate and effective system of internal controls is maintained and regularly reviewed. The Board Risk Committee and Board Audit Committee are the main oversight committees in this regard.

Three lines of defence

The governance framework adheres to a 'three lines of defence' model to ensure a clear delineation of responsibilities between control over day-to-day operations, risk oversight and independent assurance of our activities.

All three lines of defence are responsible for supporting and developing a culture of risk-awareness and for supporting each other to manage risk effectively for the Group. In this way, risk management responsibilities are understood at all levels, ownership and accountability are clear, and control and oversight is maintained throughout the Group.

First line of defence – Business lines and central functions

The business lines and central functions accept or tolerate risks with the aim of delivering value for the Group. The first line of defence is accountable for the controls we have in place to manage day-to-day operations. They manage risks within the business and functions to pre-agreed tolerances or limits. They identify, manage and monitor risks through regular reporting and by escalating issues as necessary.

Second line of defence – Risk functions

The second line of defence encompasses the risk management functions, which are independent of the businesses and central functions. The second line supports a structured approach to risk management by maintaining and implementing the RMF, supplemental frameworks and Group-wide risk policies. The second line monitor the execution and ongoing self-assurance testing by the first line of defence. It also provides independent oversight and guidance on risks relevant to our strategy and activities, maintains an aggregate view of risk, and monitors performance in relation to our risk appetite.

Third line of defence – Internal Audit

Internal Audit provides independent assurance to the Board via the Audit Committee that the first and second lines of defence are both effective in discharging their respective responsibilities.

The Group has continued to invest in all three lines of defence to enhance the controls around principal risks.

Risk principles and risk culture

Stress testing

Stress testing is an important risk management tool, with specific approaches documented for the Group's key annual assessments including the Internal Capital Adequacy Assessment Process ("ICAAP"), Individual Liquidity Adequacy Assessment Process ("ILAAP"), the Recovery and Resolution Plan ("RRP") and Reverse Stress Testing ("RST").

We maintain a Stress Testing Framework ("STF") which is updated on an annual basis, or more frequently if required, to assist the Board's understanding of the key risks, scenarios and sensitivities that may adversely impact our financial or operational position. These support the development of risk appetite, business and capital plans by:

- Testing our ability to withstand the emergence of risks in both 'normal' and 'stressed' conditions
- Assessing the adequacy of our financial resources (both capital and liquidity) and the potential management actions available to mitigate the effect of any adverse events
- Identifying potential gaps in our Risk Management Framework such as potential weaknesses in the operational controls maintained by the Group

The STF relies upon and supports the Capital Planning and Management policy, the Funding and Liquidity policy and the Operational and Credit Risk Frameworks, all of which provide detail of how the STF has been implemented within these specific areas.

Stress testing is an integral part of the Group's ICAAP assessment. The stress scenarios developed as part of the ICAAP are used to size and carry a stress loss buffer which ensures that the Group is able to withstand a range of adverse economic scenarios over its five year planning horizon. The ICAAP incorporates all principal risks impacting capital and is the result of active cooperation across Finance (including Treasury), Business areas and Risk functions. The Chief Financial Officer ("CFO") is accountable for the Group's ICAAP.

The ILAAP is an assessment of our liquidity position under normal and stressed conditions and is used to inform the Board of the ongoing assessment and quantification of liquidity risk and the manner in which it is managed, monitored, controlled and mitigated. The CFO is accountable for the Group's ILAAP.

The RRP provides an assessment of our ability to recover financial strength following or during a period of severe stress through a formal assessment of available recovery options. The RRP specifies the process and governance for invoking the Recovery Plan and enabling the selected options to be activated and mobilised quickly and effectively. The RRP also provides regulatory authorities with information and analysis to enable them to carry out an orderly resolution if required. The Chief Risk Officer ("CRO") is accountable for the Group's RRP.

We perform RST to identify and assess events that could cause our business model to become unviable. The outcome of failure is assumed as a starting point and we work backwards to determine the type and sequence of events and vulnerabilities that could lead to the hypothetical failure of the business. The key objective of RST is to enable the early identification of events that could cause our business plan to become unviable and to assess the likelihood of such events crystallising. Where those tests reveal a risk of business failure that is unacceptably high, when considered against our risk appetite, we will take action to prevent or mitigate that risk.

Stress testing governance

The Board is responsible for reviewing and approving the STF, scenarios for each type of stress testing and results of the stress testing analysis on at least an annual basis. The Board Risk Committee ('"BRC") is responsible for reviewing the STF annually. The scenarios for each type of stress test and results of the stress testing analysis are reviewed and recommended at the Asset and Liability Committee ("ALCO") and Executive Risk Committee ("ERC"). The BRC makes recommendations to the Board for approval of the scenarios to support the ICAAP, ILAAP and RRP. As the senior risk committee, BRC provides independent review and challenge to stress scenarios, underlying assumptions and adequacy of proposed management actions, prior to their recommendation to the Board.

The primary executive responsible for the STF is the CRO who is responsible for ensuring the development and implementation of a robust STF and overseeing its implementation. The CRO is also responsible for ensuring that the STF is fit for purpose and adheres to all regulatory requirements and industry good practices. Participants from all business units functions and second line risk are responsible for providing inputs for the development of scenarios, underlying assumptions and relevant management actions. These areas coordinate with the CRO and CFO to provide relevant data for stress testing.

Risk management

Principal risks

All areas of the following report are covered by the external auditor's opinion on page 142, except for the shaded sections on pages 135 to 139.

- Credit risk (read more below)
- Capital and Liquidity risk (read more on page 127)
- Market risk (read more on page 133)
- Operational risk (read more on page 135)
- Compliance, Conduct and Financial Crime risk (read more on page 137)
- Reputational risk (read more on page 138)

Credit risk

Credit risk is the risk of financial loss arising from the borrower or a counterparty failing to meet their financial obligations to the Group in accordance with agreed terms.

The risk arises primarily from our lending activities as a result of a defaulting mortgage, lease or loan contracts. Although credit risk arises from our loan book, it can also arise from treasury investments and off-balance sheet activities.

Credit risk appetite – loan book

The credit risk appetites are set based on expected levels of loss, credit risk concentration, portfolio composition and performance characteristics. We set an overall credit risk appetite for our lending activities, supported by specific business line level appetites. Expected losses are factored into the budgeting and forecasting process and reflect our expected view of lending performance, taking into account recent performance data and the prevailing economic environment.

We recognise that actual losses may differ from forecasted or budgeted values.

Maximum exposure to credit risk

	Note	2016 £m	2015 £m
Included in the statement of financial position:			
Cash and balances at central banks		116.4	105.3
Loans and advances to banks		67.2	94.2
Debt securities	19	664.5	606.1
Derivatives held for risk management	20	12.4	6.7
Loans and advances to customers	22	7,504.7	6,165.5
Other financial assets	42	2.9	0.4
		8,368.1	**6,978.2**
Commitments to lend	40	968.8	556.0
Gross credit risk exposure		**9,336.9**	**7,534.2**
Less: allowance for impairment losses	22	(27.4)	(20.7)
Net credit risk exposure		**9,309.5**	**7,513.5**

Exposure

The table above presents our 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 enhancements. 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.

Mitigation

We target UK SMEs, homeowners, and buy-to-let customers. Credit risk is managed in accordance with lending policies, the risk appetite and the RMF. Lending policies and performance against risk appetites are reviewed regularly. We seek to mitigate credit risk by focusing on business sectors where we have specific expertise and through limiting concentrated exposures on larger loans, certain sectors and other factors which can represent higher risk. We also seek to obtain security cover, and where appropriate, guarantees from borrowers. Affordability checks on income versus outgoings are also made where appropriate to assess a borrower's capacity to meet the servicing costs.

Credit risks associated with lending are managed through the Credit Risk Management Framework, which includes the use of detailed lending policies which outline the approach to lending, underwriting criteria, credit mandates, concentration limits and product terms. We maintain a dynamic approach to credit management and aim 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.

Credit risk is assessed through a combination of due diligence, reviewing credit reference agency reports, reviewing financial information, credit scores and the expert opinion of our underwriters. A proportionate approach is taken, ensuring that the highest risk loans and facilities are subject to detailed review by experienced senior underwriters.

This section provides further detail on the specific areas where we are exposed to credit risk.

	Asset Finance	Invoice Finance
Business description	· Originates loan and lease contracts to diversified range of end users · Exposures range from public sectors organisations to corporates, SMEs, partnerships, sole traders and directors / key staff of trading businesses	· Provides working capital for SME clients · May include credit control and collection services for clients
Management of credit risk	· Experienced manual underwriting, supported by data driven from risk systems · Information on individuals behind the business carefully considered · Financial and credit information obtained from external credit reference agencies · Assets acting as security are carefully valued, future resale values are considered · Audit and site visits used to track condition and location of certain assets	· Experienced manual underwriting · Review of management, financial and operational strength of client's business · Information on individuals behind the business carefully considered · Financial and credit information obtained from external credit reference agencies · Careful consideration of quality and contractual collectability of underlying receivables acting as security · In-life monitoring, audit and reconciliations performed to manage risk of fraud and default risk associated with client failure. · Significant diversification at invoice level heavily mitigates concentration risk

	Commercial Mortgages and Property Development	Residential Mortgages and Buy-to-Let
Business Description	**SME Commercial Mortgages** · Commercial mortgages to SME businesses either owning or acquiring business premises · Commercial mortgages to CRE property investors, typically to non/partial recourse SPVs secured on mixed retail/residential investments or smaller value CRE property investments **Property Development** · Residential development loan funding to established regional developers	**Residential Mortgages** · Residential mortgages for owner occupied properties **Buy-to-Let** · Private rental sector residential investment mortgages to individual, partnership, LLP and Limited Company landlords
Management of credit risk	**SME Commercial Mortgages** · Independent credit underwriting of all new business origination (all origination focused on UK domiciled property assets only) · Loan to Value and Debt Service capacity matrices applied on a risk based approach · All facilities supported by independent professional valuation by the Group's panel valuers · Collateral security by way of unsupported personal guarantees to tie in personal commitment, or corporate guarantees, are often taken · Financial covenant protection for CRE commercial loans >£1m secured by investment portfolio and/or multiple tenants · Enhanced in life credit risk management and stewardship for commercial mortgages, on a risk based approach, for all exposures >£1m · Early warning signs and back book surveillance, with individual counterparty cases exhibiting signs of stress/distressed escalated to Watch List for close and intensive monitoring and control **Property Development** · Loan to Cost and Loan to Gross Development Value matrices applied on a risk based approach , underpinned by independent QS verification of construction costs (including contingency) and independent professional valuation of completed units · All developments subject to independent QS monthly progress monitoring, supplemented by in house engagement and site visits	**Residential Mortgages** · Independent credit underwriting of all new business origination (all origination focused on UK domiciled residential property only) · Lending at origination restricted to max 85%LTV (except where additional scheme or insurance guarantee support is available), no adverse credit history and affordability criteria **Buy-to-Let** · Independent credit underwriting of all new business origination (UK domiciled residential investment property only) · Loan to Value and Debt Service capacity matrices applied on a risk based approach · For capital and interest repayments the underlying rental income must achieve min 1.0x on a stressed basis · Face to face interview and property visits for higher value aggregate BTL mortgages and more complex structures · Enhanced in life credit risk management and stewardship for commercial mortgages, on a risk based approach, for all exposures >£1m · Early warning signs and back book surveillance, with individual counterparty cases exhibiting signs of stress/ distressed escalated to Watch List for close and intensive monitoring and control

Risk management

Principal risks continued

Credit risk portfolio

The following Section provides analysis of our credit risk portfolio as at 31 December 2016. The analysis is segmented between credit risk on loans and advances to customers and credit risk on treasury assets. Details of the methodologies and estimates used to determine the allowances for loan impairments are provided in Note 3.

Forbearance

Forbearance is defined as any concessionary arrangement that is made for a period of three months or more where financial difficulty is present or imminent. It is inevitable that some borrowers experience financial difficulties which impact their ability to meet mortgage or SME finance obligations as per the contractual terms. We seek 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 to bring the account up to date. In certain circumstances, where the borrower is experiencing financial distress, we may use forbearance measures to assist the borrower. These are considered on a case-by-case basis and must result in a fair outcome. 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.

The most widely used methods of forbearance are temporarily 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. Both temporary and permanent concessions are reported as forborne for twenty four months following the end of the concession. In all cases, the above definitions are subject to no further concessions being made and the customers' compliance with the new terms.

See page 122 for an analysis of forbearance measures in place as at 31 December 2016.

The analysis in this Section of the report excludes the Property Development portfolio from a number of tables where it is not relevant (marked with a footnote). Gross property development exposure at 31 December 2016 was £230m (31 December 2015: £184m), and net exposure was £229m (31 December 2015: £179m).

Credit risk on loans and advances to customers

Key terms:

Neither past due nor individually impaired – Loans that are not in arrears and where there is no objective evidence of impairment.

Past due but not individually impaired – Loans that are in arrears but have not been individually assessed as impaired.

Individually impaired[1] – Loans which have been subject to specific credit risk adjustments (provisions) due to objective evidence of impairment. This heading includes cases that are past due by three months or more, but where no loss is expected.

Forborne – Any case which has had a concessionary arrangement that is made for a period of three months or more where financial difficulty is present or imminent. Cases continue to be reported as forborne for twenty four months following the end of the forbearance concession.

[1] During 2016, loans which are individually impaired and less than three months in arrears have been included within individually impaired loan disclosures. As such, 2015 comparative disclosures on pages 115 to 123 have been re-presented on this basis.

Credit quality of loans and advances to customers

The credit quality of assets measures the credit worthiness of the loan or the ability of the debtors to pay back the debt. The credit quality of lending assets is provided below and is shown gross of impairment provisions:

Analysis of loans and advances by impairment status

2016	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages £m	Buy-to-Let £m	Residential Mortgages £m	Total £m
Neither past due nor individually impaired	1,569.2	155.9	921.6	3,308.4	1,470.8	7,425.9
Past due but not individually impaired	3.3	–	6.9	13.2	19.8	43.2
Individually impaired	9.3	3.6	7.8	8.7	6.2	35.6
	1,581.8	**159.5**	**936.3**	**3,330.3**	**1,496.8**	**7,504.7**

2015	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages £m	Buy-to-Let £m	Residential Mortgages £m	Total £m
Neither past due nor individually impaired	1,344.7	163.2	819.0	2,402.8	1,373.0	6,102.7
Past due but not individually impaired	2.7	–	6.5	10.7	14.9	34.8
Individually impaired	6.7	2.9	7.9	6.4	4.1	28.0
	1,354.1	**166.1**	**833.4**	**2,419.9**	**1,392.0**	**6,165.5**

Loans and advances which are past due but not individually impaired

Past due but not individually impaired loans are further analysed according to the number of months past due as below:

Past due but not individually impaired	2016 £m	2015 £m
– Up to 2 months past due	35.6	28.4
– 2 to 3 months past due	7.6	6.4
Total	**43.2**	**34.8**
Fair value of collateral held	**42.3**	**35.2**

Loans and advances neither past due nor individually impaired

The credit quality of assets that are neither past due nor individually impaired are internally analysed as follows:

2016	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages[1] £m	Buy-to-Let £m	Residential Mortgages £m	Total £m
Low risk	–	–	368.6	2,710.7	1,083.8	4,163.1
Medium risk	1,282.4	6.9	315.8	523.4	345.4	2,473.9
High risk	286.8	149.0	7.1	74.3	41.6	558.8
Total	**1,569.2**	**155.9**	**691.5**	**3,308.4**	**1,470.8**	**7,195.8**
Fair value of collateral held	**1,102.8**	**155.8**	**691.5**	**3,308.3**	**1,470.8**	**6,729.2**

2015	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages[1] £m	Buy-to-Let £m	Residential Mortgages £m	Total £m
Low risk	49.1	–	281.7	1,864.9	907.4	3,103.1
Medium risk	1,204.6	12.9	351.4	503.0	432.2	2,504.1
High risk	91.0	150.3	7.0	34.9	33.4	316.6
Total	**1,344.7**	**163.2**	**640.1**	**2,402.8**	**1,373.0**	**5,923.8**
Fair value of collateral held	**960.6**	**160.7**	**592.7**	**2,402.8**	**1,373.0**	**5,489.8**

[1] The above analysis excludes Property Development.

Risk management

Principal risks continued

a) Risk grading methodology

The categorisation of high, medium and low risk is based on internal grading models utilised in portfolio monitoring. 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 by the customer and an assessment of the expected loss in the event of default.

The resulting classification of balances between low, medium and high is consequently driven by a combination of the Probability of Default ("PD") and Loss Given Default ("LGD") grades as further explained. A matrix of eighteen PD (fifteen of which apply to up to date accounts) and ten LGD grades determine the category within which each loan is categorised, i.e. those accounts that have a low PD and/or LGD are graded as 'low'. Those graded 'high' will be accounts that have either a high PD and/or high LGD.

- Probability of Default refers to the probability of a customer or counterparty defaulting within the next 12 months which is typically taken as three payments past due. A default probability model predicts this probability by using credit scores along with financial, behavioural and qualitative inputs.
- Key components of the Loss Given Default are the propensity to "cure", that is the likelihood/propensity for a defaulting 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.

b) Fair value of collateral methodology

For SME Commercial Mortgage, Buy-to-Let and Residential Mortgage 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 indexed valuation is greater than the balance outstanding, 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.

Impaired loan analysis

Individually impaired balances are further analysed as follows:

2016	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages[1] £m	Buy-to-Let £m	Residential Mortgages £m	Total £m
Impaired but not past due	1.0	–	2.4	0.5	0.1	4.0
Past due less than 3 months	2.5	0.6	0.2	1.5	0.6	5.4
Past due 3–6 months	3.1	0.1	–	2.8	3.8	9.8
Past due 6–12 months	2.0	1.0	1.2	3.2	1.4	8.8
Past due over 12 months	0.7	1.9	4.0	0.7	0.3	7.6
	9.3	**3.6**	**7.8**	**8.7**	**6.2**	**35.6**
Of which: Possessions	0.7	–	0.6	5.5	0.2	7.0

2015	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages[1] £m	Buy-to-Let £m	Residential Mortgages £m	Total £m
Impaired but not past due	1.4	–	0.9	1.3	–	3.6
Past due less than 3 months	1.2	0.1	–	–	0.1	1.4
Past due 3–6 months	1.2	0.2	3.4	2.8	3.3	10.9
Past due 6–12 months	1.3	0.5	–	1.6	0.5	3.9
Past due over 12 months	1.6	2.1	3.6	0.7	0.2	8.2
	6.7	**2.9**	**7.9**	**6.4**	**4.1**	**28.0**
Of which: Possessions	0.8	–	–	–	0.4	1.2

[1] The above analysis includes Property Development.

The fair value of collateral held against the above individually impaired balances at 31 December 2016 of £35.6m (31 December 2015: £28.0m) was £28.8m (31 December 2015: £23.4m). We always seek to pursue timely realisation of collateral in an orderly manner. We do not use the collateral for our own operations.

Movement in impaired loans is analysed as follows:

2016	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages[1] £m	Buy-to-Let £m	Residential Mortgages £m	Total £m
At 1 January	6.7	2.9	7.9	6.4	4.1	28.0
Classified as impaired during the period	7.3	2.1	1.0	3.5	3.1	17.0
Transferred from impaired to unimpaired	(0.3)	–	(1.0)	(1.1)	(0.7)	(3.1)
Amounts written off	(4.4)	(1.4)	(0.1)	(0.1)	(0.1)	(6.1)
Repayments	–	–	–	–	(0.2)	(0.2)
At 30 December 2016	**9.3**	**3.6**	**7.8**	**8.7**	**6.2**	**35.6**

2015	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages £m	Buy-to-Let £m	Residential Mortgages £m	Total £m
At 1 January	5.0	6.3	7.1	4.4	3.3	26.1
Classified as impaired during the period	4.3	1.3	2.8	4.9	3.5	16.8
Transferred from impaired to unimpaired	(0.7)	–	(0.1)	(0.8)	(0.7)	(2.3)
Amounts written off	(1.9)	(4.6)	(1.7)	(0.9)	(0.2)	(9.3)
Repayments	–	(0.1)	(0.2)	(1.2)	(1.8)	(3.3)
At 31 December 2015	**6.7**	**2.9**	**7.9**	**6.4**	**4.1**	**28.0**

Risk management

Principal risks continued

Impairment coverage ratio

The impairment coverage is analysed as follows:

Coverage ratio	2016 £m	2015 £m
Gross loans and advances	7,504.7	6,165.5
Of which individually impaired	35.6	28.0
Impaired as a % of gross loans and advances	0.47%	0.45%
Allowance for losses – individual provisions	14.3	10.2
Coverage	**40.17%**	**36.43%**

The coverage ratio has increased during the year as the result of a small increase in the number of loans specifically provided for (see Note 22).

Quality of collateral

The principal indicators used to assess the credit security of performing loans are Loan to Value ratios for SME Commercial, Buy-to-Let and Residential Mortgages. The following tables show loan balances net of impairment provisions.

SME Commercial Mortgages

Loan to Value on indexed origination information on our SME Commercial Mortgage portfolio is set out below:

	2016 £m	2015[1] £m
95–100%	0.4	0.4
90–95%	0.5	–
85–90%	0.7	1.1
80–85%	1.7	1.3
75–80%	12.1	8.5
70–75%	34.8	19.0
60–70%	153.2	134.7
50–60%	211.9	209.4
0–50%	285.5	275.5
	700.8	**649.9**
Capital repayment	568.4	505.8
Interest only	132.4	144.1
	700.8	**649.9**
Average Loan to Value percentage	51.74%	52.39%

1 Indexation methodology has been enhanced during 2016 hence the 2015 balances have been restated in accordance with the enhanced methodology.

The analysis excludes Property Development.

Property Development

We use 'loan to gross development value' as an indicator of the quality of credit security of performing loans for the Property Development portfolio. Loan to gross development value is a measure used to monitor the loan balance drawn compared against the expected gross development value once the development is complete. Average loan to gross development value at origination for Property Development loans at 31 December 2016 was 58.05% (31 December 2015: 56.97%).

Buy-to-Let

Loan to Value on indexed origination information on our Buy-to-Let portfolio is set out below:

	2016 £m	2015 £m
100%+	–	0.6
95–100%	0.4	5.1
90–95%	9.6	18.5
85–90%	14.8	14.5
80–85%	136.5	51.6
75–80%	461.4	219.1
70–75%	561.2	323.5
60–70%	984.3	735.1
50–60%	669.6	528.8
0–50%	488.2	521.1
	3,326.0	**2,417.9**
Capital repayment	251.1	228.4
Interest only	3,074.9	2,189.5
	3,326.0	**2,417.9**
Average Loan to Value percentage	63.21%	60.52%

Residential Mortgages

Loan to Value on indexed origination information on our Residential Mortgages portfolio is set out below:

	2016 £m	2015 £m
100%+	0.2	6.6
95–100%	17.2	55.2
90–95%	139.9	200.5
85–90%	178.4	166.2
80–85%	170.4	153.6
75–80%	166.1	138.9
70–75%	172.8	121.5
60–70%	251.4	218.3
50–60%	168.4	145.5
0–50%	229.1	183.9
	1,493.9	**1,390.2**
Capital repayment	1,303.1	1,188.0
Interest only	190.8	202.2
	1,493.9	**1,390.2**
Average Loan to Value percentage	69.48%	72.29%

Lending at higher LTV bandings is largely as a result of the Group's participation in the Help to Buy Scheme, with in excess of 90% of the portfolio having an associated government guarantee on amounts where the Loan to Value is above 85%. This reduces the Group's risk exposure. As at 31 December 2016, 96.15% of the exposures with Loan to Value in excess of 85% relate to the Help to Buy Scheme (31 December 2015: 89.16%). The Help to Buy guarantee portfolio, which makes up the majority of the Help to Buy book, had an average indexed Loan to Value of 87.47% (31 December 2015: 90.68%). As at 31 December 2016, the average indexed Loan to Value of the non-Help to Buy owner occupied book is 61.65% (31 December 2015: 64.14%).

Risk management

Principal risks continued

Invoice Finance

In respect of Invoice Finance, collateral is provided by the underlying receivables (e.g. trade invoices). As at 31 December 2016, 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 62.30% (31 December 2015: 64.99%).

In addition to the value of the underlying sales ledger balances, we will wherever possible, obtain additional collateral before offering invoice finance facilities to a client. These may 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 or certain other breaches. These additional forms of security are impractical to value given their nature.

Asset Finance

In respect of Asset Finance, collateral is provided by our rights and/or title to the underlying assets, which we are able to repossess in the event of default. Where appropriate, we will also obtain additional security, such as parent company or personal guarantees.

Asset Finance also undertakes a small volume of unsecured lending where we have 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 2016, the total amount of such unsecured lending was £40.7m (31 December 2015: £30.3m).

Concentration of credit risk

We monitor concentration of credit risk by product type, size of asset, geographic location and sector. Analysis of concentrations (presented net of impairment provisions) is shown below.

Credit concentration by segment

Details of our lending by segment are as follows:

	2016 £m	2015 £m
Asset Finance	1,573.4	1,346.7
Invoice Finance	154.1	160.8
SME Commercial Mortgages[1]	929.9	829.2
Buy-to-Let	3,326.0	2,417.9
Residential Mortgages	1,493.9	1,390.2
	7,477.3	**6,144.8**

[1] Analysis includes Property Development.

Credit concentration by quantum of exposure

An analysis of our loans and advances to customers by size of asset is shown in the table below:

	Asset Finance £m	**SME Commercial Mortgages[1] £m**	**Buy-to-Let £m**	**Residential Mortgages £m**	Asset Finance £m	SME Commercial Mortgages[1] £m	Buy-to-Let £m	Residential Mortgages £m
£0–£50k	639.7	2.9	25.4	15.9	578.8	4.0	20.7	21.1
£50–£100k	361.3	24.7	518.1	252.9	307.6	25.6	453.7	240.0
£100–£150k	145.4	31.7	480.6	414.9	136.8	29.1	410.0	396.2
£150–£200k	96.1	26.1	400.5	299.6	78.0	23.1	323.0	274.3
£200–£300k	107.4	52.3	709.1	314.1	83.9	53.3	450.5	278.7
£300–£400k	54.9	36.7	457.5	120.7	45.6	33.7	281.1	104.9
£400–£500k	40.3	40.1	219.1	21.4	31.0	36.5	145.5	24.1
£500k–£1m	79.6	119.0	306.3	51.2	52.5	117.7	209.0	45.7
£1m–£2m	34.2	140.2	116.0	3.2	27.9	140.4	79.2	5.2
£2m+	14.5	227.1	93.4	–	4.6	186.5	45.2	–
	1,573.4	**700.8**	**3,326.0**	**1,493.9**	**1,346.7**	**649.9**	**2,417.9**	**1,390.2**

[1] The analysis of the SME Commercial Mortgages segment presented above excludes the Property Development.

Credit concentration by geography

An analysis of our loans and advances to customers by geography, including Property Development, is shown in the table below:

	2016 %	2015 %
East Anglia	9.6	9.4
East Midlands	6.1	6.2
Greater London	20.7	19.3
North East	2.6	2.8
North West	10.7	11.4
Northern Ireland	0.2	0.1
Scotland	4.9	4.9
South East	19.9	19.0
South West	9.5	9.8
Wales	2.9	3.2
West Midlands	6.7	7.2
Yorkshire and Humberside	6.2	6.7
	100.0	**100.0**

Credit concentration by sector

An analysis of our loans and advances to customers by sector is shown in the table below:

	2016 %	2015 %
Agriculture, hunting and forestry	1.1	1.2
Construction	4.4	4.2
Education	0.1	0.1
Electricity, gas and water supply	0.5	0.5
Financial intermediation	1.7	1.4
Health and social work	0.3	0.2
Hotels and restaurants	0.3	0.3
Manufacturing	3.1	3.8
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	–
Real estate, renting and business activities	19.2	18.6
Residential	61.9	61.5
Transport, storage and communication	3.8	4.1
Wholesale & retail trade; repair of motor vehicles, motorcycles & personal household goods	2.5	2.9
	100.0	**100.0**

Risk management

Principal risks continued

Forbearance analysis

As at 31 December 2016, we had undertaken forbearance measures as follows in each of our segments:

	2016 £m	2015[1] £m
Asset Finance		
Capitalisation	1.3	–
Reduced monthly payments	0.2	0.3
Loan-term extension	0.3	0.1
Deferred payment	1.5	0.8
Total Asset Finance	**3.3**	**1.2**
Forborne as a percentage of the total divisional gross lending book (%)	0.21%	0.09%
Invoice Finance		
Agreement to advance funds in excess of normal contractual terms	11.1	1.8
Total Invoice Finance	**11.1**	**1.8**
Forborne as a percentage of the total divisional gross lending book (%)	6.96%	1.12%
SME Commercial Mortgages		
Temporary or permanent switch to interest only	24.3	13.3
Total SME Commercial Mortgages	**24.3**	**13.3**
Forborne as a percentage of the total divisional gross lending book (%)	2.60%	1.60%
Buy-to-Let		
Temporary or permanent switch to interest only	0.7	1.5
Reduced monthly payments	1.0	0.8
Deferred payment	0.3	0.3
Total Buy-to-Let	**2.0**	**2.6**
Forborne as a percentage of the total divisional gross lending book (%)	0.06%	0.10%
Residential Mortgages		
Temporary or permanent switch to interest only	4.5	3.5
Reduced monthly payments	2.0	0.8
Deferred payment	1.3	1.4
Total Residential Mortgages	**7.8**	**5.7**
Forborne as a percentage of the total divisional gross lending book (%)	0.52%	0.41%
Total forborne		
Total capitalisation	1.3	–
Total temporary or permanent switch to interest only	29.5	18.3
Total reduced monthly payments	3.2	1.9
Total loan-term extension	0.3	0.1
Total deferred payment	3.1	2.5
Total agreement to advance funds in excess of normal contractual terms	11.1	1.8
Total forborne	**48.5**	**24.6**
Total forborne as a percentage of the total gross lending book (%)	0.65%	0.40%

[1] 2015 SME Commercial Mortgages balance has been re-presented following a review of exposures classified as forborne.

When forbearance is granted to a borrower on a specific exposure, all exposures which are aggregated with that borrower, e.g. by reason of common ownership, are deemed as forborne for reporting purposes.

Analysis of forborne accounts by payment status is shown in the tables below:

2016	**Asset Finance £m**	**Invoice Finance £m**	**SME Commercial Mortgages £m**	**Buy-to-Let £m**	**Residential Mortgages £m**	**Total £m**
Neither past due nor individually impaired	3.2	10.4	23.8	1.4	4.9	43.7
Past due but not individually impaired	–	0.6	0.2	0.3	1.5	2.6
Individually impaired	0.1	0.1	0.3	0.3	1.4	2.2
	3.3	**11.1**	**24.3**	**2.0**	**7.8**	**48.5**

2015	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages £m	Buy-to-Let £m	Residential Mortgages £m	Total £m
Neither past due nor individually impaired	1.1	1.8	10.6	1.9	3.7	19.1
Past due but not individually impaired	–	–	1.5	0.7	1.3	3.5
Individually impaired	0.1	–	1.2	-	0.7	2.0
	1.2	**1.8**	**13.3**	**2.6**	**5.7**	**24.6**

Risk management

Principal risks continued

Credit risk – treasury assets

Credit risk exists with treasury assets where we have acquired securities or placed cash deposits with other financial institutions. The credit risk of treasury assets is considered to be relatively low. Certain treasury assets are held as part of our liquidity buffer.

Credit risk appetite – treasury assets

The Group's appetite for credit risk on treasury assets is minimal. Cash and financial assets are invested in investment grade rated entities or investment vehicles. No assets are held for speculative purposes or actively traded.

Credit quality of treasury assets

The table below sets out information about the credit quality of treasury financial assets:

	2016 £m	2015 £m
Cash and balances at central banks and loans and advances to banks		
– Rated AAA	–	105.3
– Rated AA+ to AA–	139.3	29.6
– Rated A+ to A–	35.6	48.7
– Rated BBB+	8.7	15.9
	183.6	**199.5**
High quality liquid assets included in the liquidity buffer		
– Rated AAA	430.9	396.7
– Rated AA+ to AA–	163.2	134.5
– Rated A+ to A–	–	–
– Rated BBB+	–	–
Debt securities: Asset backed securities		
– Rated AAA	70.4	71.8
– Rated AA+ to AA–	–	–
– Rated A+ to A–	–	3.1
– Rated BBB+	–	–
	664.5	**606.1**
Derivatives held for risk management purposes		
– Rated AAA	–	–
– Rated AA+ to AA–	2.6	1.4
– Rated A+ to A–	6.1	2.0
– Rated BBB+	3.7	2.3
– Rated BBB	–	1.0
	12.4	**6.7**
	860.5	**812.3**

As at 31 December 2016 and at 31 December 2015. None of the treasury assets were past due or impaired.

For these exposures the Group uses credit ratings provided by the recognised credit rating agencies Standard & Poor's[1], and Fitch.

1 "Standard and Poor's disclaimer notice in relation to the ratings information set out above: This may contain information obtained from third parties, including ratings from credit ratings agencies such as Standard & Poor's. Reproduction and distribution of third party content in any form is prohibited except with the prior written permission of the related third party. Third party content providers do not guarantee the accuracy, completeness, timeliness or availability of any information, including ratings, and are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, or for the results obtained from the use of such content. THIRD PARTY CONTENT PROVIDERS GIVE NO EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE. THIRD PARTY CONTENT PROVIDERS SHALL NOT BE LIABLE FOR ANY DIRECT, INDIRECT, INCIDENTAL, EXEMPLARY, COMPENSATORY, PUNITIVE, SPECIAL OR CONSEQUENTIAL DAMAGES, COSTS, EXPENSES, LEGAL FEES, OR LOSSES (INCLUDING LOST INCOME OR PROFITS AND OPPORTUNITY COSTS OR LOSSES CAUSED BY NEGLIGENCE) IN CONNECTION WITH ANY USE OF THEIR CONTENT, INCLUDING RATINGS. Credit ratings are statements of opinions and are not statements of fact or recommendations to purchase hold or sell securities. They do not address the suitability of securities or the suitability of securities for investment purposes, and should not be relied on as investment advice."

Management

Cash placements

Credit risk of Group and treasury counterparties is controlled through the treasury credit risk policy which limits the maximum exposure by entity with which the Group can place cash deposits. All institutions need to be rated at investment grade at the time of placement.

High quality liquid assets included in the liquidity buffer

As part of the liquidity buffer, we hold certain debt securities which qualify as high quality liquid assets included in the liquidity buffer. These instruments are AAA to AA rated. The portfolio includes UK Gilts, supranational bonds, sovereign risk bonds issued by European governments and agencies and corporate bonds.

Asset-backed securities ("ABS")

We have a portfolio of ABS. 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 an investment grade credit rating. Most derivative contracts are collateralised through the receipt/payment of daily cash margin calls to cover the mark to market value of the asset/liability.

Offsetting financial assets and liabilities

It is our 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 terminated.

Under the margining agreements where we have a net asset position with a counterparty valued at current market values, in respect of derivatives, then that counterparty will place collateral, usually cash, with us in order to cover the position. Similarly, we will place collateral, usually cash, with the counterparty where it has a net liability position.

As our derivatives are under master netting and margining agreements as described, 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, and the Term Funding Scheme as detailed in Notes 22.

Risk management

Principal risks
continued

2016 Type of financial instrument	Gross amount of recognised financial instruments £m	Gross amount of recognised financial instrument offset in the statement of financial position £m	Net amount of financial instruments presented in the statement of financial position £m	Related amounts not offset in the statement of financial position Financial instruments £m	Cash collateral paid/(received) £m	Net amount £m
Assets						
Loans and advances to customers (amounts pre-positioned as collateral under the FLS)	1,066.2	–	1,066.2	(354.8)	–	711.4
Loans and advances to customers (amounts pre-positioned as collateral under the TFS)	578.7	–	578.7	(396.1)	–	182.6
Derivatives held for risk management	12.4	–	12.4	(13.6)	(2.2)	(3.4)
	1,657.3	**–**	**1,657.3**	**(764.5)**	**(2.2)**	**890.6**
Liabilities						
Amount due to banks – repurchase agreements	(354.8)	–	(354.8)	354.8	–	–
Loans and advances to customers (amounts pre-positioned as collateral under the TFS)	(396.1)	–	(396.1)	396.1	–	–
Derivatives held for risk management	(35.8)	–	(35.8)	13.6	22.2	–
	(786.7)	**–**	**(786.7)**	**764.5**	**22.2**	**–**

2015 Type of financial instrument	Gross amount of recognised financial instruments £m	Gross amount of recognised financial instrument offset in the statement of financial position £m	Net amount of financial instruments presented in the statement of financial position £m	Related amounts not offset in the statement of financial position Financial instruments £m	Cash collateral paid/(received) £m	Net amount £m
Assets						
Loans and advances to customers (amounts pre-positioned as collateral under the FLS)	1,445.5	–	1,445.5	(398.6)	–	1,046.9
Loans and advances to customers (amounts pre-positioned as collateral under the TFS)	–	–	–	–	–	–
Derivatives held for risk management	6.7	–	6.7	(3.7)	(1.3)	1.7
	1,452.2	**–**	**1,452.2**	**(402.3)**	**(1.3)**	**1,048.6**
Liabilities						
Amount due to banks – repurchase agreements	(398.6)	–	(398.6)	398.6	–	–
Loans and advances to customers (amounts pre-positioned as collateral under the TFS)	–	–	–	–	–	–
Derivatives held for risk management	(35.4)	–	(35.4)	3.7	31.7	–
	(434.0)	**–**	**(434.0)**	**402.3**	**31.7**	**–**

Capital and Liquidity risk

Capital risk is the risk that the Group has insufficient capital to cover regulatory requirements and/or to support its growth plans.

Liquidity risk is the risk that we are not able to meet our financial obligations as they fall due, or can do so only at excessive cost.

Capital Risk

Capital risk appetite

We aim to maintain a strong capital position in line with the capital risk appetite established by the Board. Our capital risk appetite reflects the desire to optimise the capital structure of the Group and efficiently utilise its capital resources in order to generate appropriate returns for shareholders. The Group's capital risk appetite is set to ensure that the Group:

- Meets minimum regulatory capital requirements at all times;
- Is able to achieve our strategic objectives including business growth plans;
- Is able to withstand an adverse stress scenario and continue to meet our Individual Capital Guidance ("ICG"); and
- Provides assurance of the Group's resilience to depositors, customers, shareholders and other key stakeholders.

Capital Requirements

We operate under the CRD IV CRR regulatory framework which came into force on 1 January 2014 and was implemented in the UK by the Prudential Regulation Authority ("PRA").

Under CRD IV, the Group is subject to capital requirements under both Pillar 1 (minimum capital requirements) and Pillar 2 (Supervisory Review).

Pillar 1 requirements

Pillar 1 capital requirements are based on prescribed risk calculations in line with Capital Requirements Regulation ("CRR"), EBA Single Rulebook and relevant PRA regulations. Under this framework, we hold Pillar 1 capital for credit risk, operational risk, market risk and Credit Valuation Adjustments ("CVA"). We calculate our credit and market risk Pillar 1 requirements using the standardised approaches. The operational risk Pillar 1 requirement is calculated under the Basic Indicator Approach ("BIA").

Under CRD IV, we must hold total capital equal to a minimum of 8% of our total risk weighted assets to cover our Pillar 1 capital requirements. The 8% total capital minimum includes a minimum common equity tier 1 ("CET1") requirement of 4.5% of RWAs and a minimum Tier 1 requirement of 6% of RWAs.

CRD IV buffers

CRD IV introduced a number of new capital buffers to provide further capital cushions for additional risks that financial institutions may be subject to. For the Group, the combined buffer, which has to be met with CET1 capital, is comprised of the counter-cyclical capital buffer and the capital conservation buffer. The capital conservation buffer phase in commenced on 1 January 2016 when it was set at 0.625%, increasing to 1.3% on 1 January 2017. The 2.5% requirement will be fully phased in by January 2019. The countercyclical buffer in the UK is set by the Financial Policy Committee ("FPC") and reviewed on a quarterly basis. It is currently set at zero, and is expected to remain at this level at least until June 2017. The FPC has indicated that it envisages a 1% steady state countercyclical buffer for the UK in the future depending on economic conditions.

In addition to the CRD IV combined buffer, the Group is also subject to the PRA Buffer as applied as part of the Pillar 2 framework and discussed below.

Application of the Pillar 2 Framework

We have an established Internal Capital Adequacy Assessment Process ("ICAAP") which is conducted in accordance with CRD IV and PRA requirements. The ICAAP represents the aggregated view of the risks faced by the Group. It is used by the Board and management to understand the level of capital required over the planning horizon to cover these risks that are not covered or not adequately covered by the minimum regulatory capital requirement set out under Pillar 1, and also to withstand a range of adverse stress scenarios.

Key risks assessed under Pillar 2 include credit risk, credit concentration risk, operational risk and interest rate risk in the banking book.

Following a review of our ICAAP assessment, through its Supervisory Review and Evaluation Process ("SREP"), the PRA sets an ICG, which supersedes Pillar 1 requirements and establishes the minimum level of regulatory capital we must maintain at all times. The ICG has to be met with the same quality of capital as Pillar 1.

We also conduct capital stress testing and scenario analysis as part of our ICAAP assessment. We use the stress scenarios to size and carry a stress loss buffer which ensures we are able to withstand an adverse economic downturn over a five-year planning horizon. In addition, we identify management actions that could be taken to mitigate the impact of the stress on the capital position. These are aligned with our Recovery and Resolution Plan, which describes actions that can be taken to preserve capital if the stress scenario is more extreme than expected.

Risk management

Principal risks continued

The stress testing conducted in our ICAAP forms the basis for the PRA buffer assessment. Following their review, the PRA sets a PRA buffer, which in combination with the CRD IV combined buffer is held to ensure we can withstand an adverse market stress. The combination of the PRA buffer and the CRD IV combined buffer replaced the Capital Planning Buffer ("CPB") with effect from 1 January 2016. The PRA buffer has to be met fully with CET1 capital by 1 January 2019, subject to a phase-in from 1 January 2016, which is aligned with the phase in of the conservation buffer.

Throughout the year, our capital resources remained in excess of the minimum requirements determined by the ICG, CRD IV buffers and the PRA buffers.

Leverage ratio framework
Alongside the risk based capital framework, we actively monitor our leverage ratio. The leverage ratio at 31 December 2016 is 7.0%[1] (31 December 2015: 7.2%[1]), calculated in accordance with CRD IV. At present, we are not captured under the FPC's leverage ratio framework. However, leverage will become a binding requirement in 2018 as outlined in CRR, albeit the Group comfortably meets the new requirements.

Further details of our capital requirements and resources are provided in the annual Pillar III disclosures which are available on our investor relations website: www.investors.aldermore.co.uk.

Mitigation and monitoring
Our Capital Planning and Management policy establishes a framework for maintaining our current and prospective capital at an appropriate level under various scenarios. The policy describes the process for establishing the Group's capital risk appetite is approved by the Board and reviewed on an annual basis or more frequently if required.

We monitor current and forecast levels of capital against the capital risk appetite approved by the Board and report the capital position to ALCO, the Executive Risk Committee, Board Risk Committee and the Board on a regular basis. The capital forecast forms an integral component of the annual budgeting process and is updated in line with changes to our business plan. The capital forecast incorporates the impact of known forthcoming regulatory changes to ensure we are well positioned to meet them when implemented.

Analysis of capital risk
We operated in line with our capital risk appetite as set by the Board and above our regulatory capital requirements throughout the years ended 31 December 2016 and 31 December 2015.

As at 31 December 2016, our capital base was made up of £525.8m (31 December 2015: £435.6m) of Common Equity Tier 1 capital and £74.0m (31 December 2015: £74.0m) of Additional Tier 1 capital and £113.1m (31 December 2015: £48.6m) Tier 2 capital. Common Equity Tier 1 capital consisted of fully issued ordinary shares, satisfying all the criteria for a Tier 1 instrument as outlined in the CRR and audited/verified reserves. Additional Tier 1 capital was issued in December 2014. Tier 2 capital relates to issued subordinated loan notes and collective impairment allowances.

[1] Leverage ratio disclosure is not covered by the external auditor's opinion

Our capital resources as at the year-end were as follows:

	2016 £m	2015 £m
Common Equity Tier 1		
Share capital	34.5	34.5
Share premium account	73.4	73.4
Capital redemption reserve	0.1	0.1
Available for sale reserve	1.8	(1.0)
Retained earnings	442.2	352.6
Less: prudential valuation adjustment	(0.1)	–
Less: intangible assets	(26.1)	(24.0)
Total Common Equity Tier 1 capital (CET1)	**525.8**	**435.6**
Additional Tier 1		
Additional Tier 1 – contingent convertible securities	74.0	74.0
Total Tier 1 capital	**599.8**	**509.6**
Tier 2 capital		
Subordinated notes	100.0	38.1
Collective impairment allowance	13.1	10.5
Total Tier 2 capital	**113.1**	**48.6**
Total capital resources	**712.9**	**558.2**
Risk weighted assets – Pillar[1]	**4,576.1**	**3,693.0**
Capital ratios[1]		
Common Equity Tier 1 ratio	11.5%	11.8%
Tier 1 capital ratio	13.1%	13.8%
Total capital ratio	15.6%	15.1%

1 Risk weighted assets, and the capital ratios are not covered by the external auditor's opinion.

Regulatory capital has increased during 2016 due to the issuance of £60m of subordinated notes in October 2016 and the inclusion of the profit after tax for the year in retained earnings. This has been partially offset by the coupon paid on the Additional Tier 1 instrument in April 2016. Further details regarding the subordinated note issuance can be found in Note 35.

Reconciliation of equity per statement of financial position to capital resources

	2016 £m	2015 £m
Equity per statement of financial position	626.0	533.6
Regulatory adjustments		
Add: subordinated notes	100.0	38.1
Add: collective impairment allowance	13.1	10.5
Less: prudential valuation adjustment	(0.1)	–
Less: intangible assets	(26.1)	(24.0)
Total capital resources	**712.9**	**558.2**

Risk management

Principal risks continued

Liquidity Risk

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 we will be able to continue to meet our financial commitments during an extended period of stress. Additionally, reputational risks are managed through holding liquidity to meet pipeline commitments expected to complete during a three month period.

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 are considered and prudently stressed, and that we are able to meet liabilities beyond the targeted survival period.

Exposures

Liquidity risk exposure represents the amount of potential stressed outflows in any future period less expected inflows. Liquidity is considered from both an internal and a regulatory perspective.

Mitigation

To protect the Group and its depositors against liquidity risks, we maintain a liquidity buffer which is based on our 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, fluctuations in funding, enabling us to meet all financial obligations and to support anticipated asset growth.

Contingency funding plan

As a regulated firm, we are required to maintain a Contingency Funding Plan ("CFP"). The plan (which is now part of our Recovery and Resolution Plan ("RRP")) involves a two stage process, covering preventative measures and corrective measures to be invoked when there is a potential risk to our 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 we could take to ensure we comply with the liquidity adequacy rules, maintain sufficient capital and operate within our risk appetite and limits as set and approved by the Board.

Analysis of liquidity risk

Through the ILAAP process, we have assessed the level of liquidity necessary to prudently cover systemic and idiosyncratic risks. The ILAAP process determines the appropriate liquidity buffer, taking into account the specific nature of the deposit base and other liquidity risk drivers.

The ILAAP requires us to consider all material liquidity risks in detail and to document our analysis of each key liquidity risk driver and to set a liquidity risk appetite against each of these drivers. Liquidity risks are specifically considered by the ALCO each month.

An overview of our key liquidity risk drivers is provided below:

- Deposit funding risk – Deposit funding risk is the primary liquidity risk driver for the Group and this risk could crystallise if there was a concern by depositors over the current or future creditworthiness of the Group. We seek to operate in such a way as to protect depositors and in excess of 95% of deposits are also protected by the government's Financial Services Compensation Scheme ("FSCS"). The FSCS provided £75,000 of protection to each individual depositor at 31 December 2016. This protection has increased to £85,000 in 2017.
- Wholesale funding – We mainly finance our operations through retail and SME deposit taking. We also have long term wholesale funding lines in place under the Term Funding and Funding for Lending Schemes, repurchase facilities to help manage liquid assets, and debt securities issued by the Group securitisation vehicle in April 2014. We have relationship banking facilities in place, which are used to hedge against currency and interest rate exposures, as well as repurchase facilities for short term liquidity management.

A summary of our wholesale funding sources is show below:

Wholesale funding sources

	Note	2016 £m	2015 £m
Repurchase agreements on drawings under FLS Scheme	29	354.8	398.6
Central bank under TFS	29	396.1	–
Debt securities in issue	34	130.6	193.9
Deposits by banks	29	0.7	5.2
Subordinated notes	35	100.0	38.1
		982.2	**635.8**

Payment systems
We do not form part of the UK payment system however we make use of the system in our day to day business. In the event there are problems with one of the payment systems, we have access to other facilities with which to make payments if needed.

Pipeline loan commitments
We need to maintain liquidity to cover the outstanding pipeline of loan offers. Although certain pipeline offers may not be legally binding, the failure to honour an expression of intent to finance a loan contract brings reputational risk, therefore our policy is to hold liquidity for all such pipeline offers.

Cash collateral requirements
The Credit Support Annex ("CSA") agreement requires Aldermore or the derivative counterparty to hold cash in a deposit account depending on whether the swap is in or out of the money. Under a CSA, cash is passed between parties to mitigate the counterparty risk inherent in the outstanding positions which are valued daily.

Analysis of liquidity buffer
The components of the Group's liquidity buffer were as follows:

	2016 £m	2015 £m
Bank of England reserve account and unencumbered cash and bank balances	118.4	104.8
UK gilts and Treasury bills, Supranational bonds and Covered bonds (level 1 eligible)	554.0	505.9
Treasury bills held under the FLS scheme	294.8	349.0
Covered bonds (level 2 eligible)	36.8	20.8
Asset backed securities	70.4	74.8
Total liquidity buffer	**1,074.4**	**1,055.3**
As a % of funding liabilities	13.54%	15.75%

Encumbered assets
An asset is defined as encumbered if it has been pledged as collateral against an existing liability and, as a result, is no longer available to the Group to secure funding, satisfy collateral needs or be sold to reduce the funding requirement. An asset is therefore categorised as unencumbered if it has not been pledged against an existing liability. The Group monitors and manages total balance sheet encumbrance via a board-approved risk appetite framework.

Details of assets pledged through repurchase activity and collateral pledges are reported in the relevant notes to the balance sheet (Note 22 in respect of the Term Funding Scheme and Funding for Lending Scheme, and Note 42 in respect of the securitisation vehicle).

Risk management

Principal risks continued

Gross undiscounted contractual cash flows

The following is an analysis of gross undiscounted contractual cash flows payable under financial liabilities. The analysis has been prepared on the basis of the earliest date at which contractual repayments which may take place. This includes consideration of where the Group have the contractual right to call, irrespective of whether any decision to call has been made.

2016	Payable on demand £m	Up to 3 months £m	3 to 12 months £m	1 to 5 years £m	More than 5 years £m	Total £m
Non-derivative liabilities						
Amounts due to banks	312.2	45.4	0.2	396.0	–	753.8
Customers' accounts	2,041.0	1,099.9	2,264.4	1,892.1	1.0	7,298.4
Other liabilities	9.7	11.2	–	–	–	20.9
Debt securities in issue	–	10.6	29.5	118.3	–	158.4
Subordinated notes	–	5.1	47.7	75.3	–	128.1
Unrecognised loan commitments	968.8	–	–	–	–	968.8
	3,331.7	**1,172.2**	**2,341.8**	**2,481.7**	**1.0**	**9,328.4**
Derivative liabilities						
Derivatives held for risk management settled net	1.1	2.2	10.7	31.2	2.3	47.5
Derivatives held for risk management settled gross:						
Amounts received	(13.1)	–	–	–	–	(13.1)
Amount paid	13.1	–	–	–	–	13.1
	1.1	**2.2**	**10.7**	**31.2**	**2.3**	**47.5**

2015	Payable on demand £m	Up to 3 months £m	3 to 12 months £m	1 to 5 years £m	More than 5 years £m	Total £m
Non-derivative liabilities						
Amounts due to banks	1.3	308.8	95.0	–	–	405.1
Customers' accounts	1,347.8	810.5	2,122.0	1,554.6	–	5,834.9
Other liabilities	6.0	11.6	–	–	–	17.6
Debt securities in issue	–	19.8	50.0	130.5	–	200.3
Subordinated notes	–	–	5.2	42.6	–	47.8
Unrecognised loan commitments	556.0	–	–	–	–	556.0
	1,911.1	**1,150.7**	**2,272.2**	**1,727.7**	**–**	**7,061.7**
Derivative liabilities						
Derivatives held for risk management settled net	0.3	2.1	5.5	18.8	5.5	32.2
Derivatives held for risk management settled gross:						
Amounts received	(4.4)	(3.1)	–	–	–	(7.5)
Amount paid	4.4	3.1	–	–	–	7.5
	0.3	**2.1**	**5.5**	**18.8**	**5.5**	**32.2**

Market risk

> We do not seek to take or expose ourselves to market risk, and do not carry out proprietary trading, although certain liquid asset investments which form part of the liquid asset buffer carry mark to market risk which we regularly monitor.
>
> We carry interest rate risk which is the risk of loss through mismatched asset and liability positions sensitive to changes in interest rates. Interest rate risk consists of asset–liability gap risk and basis risk.

Market risk

We do not carry out proprietary trading or hold any positions in assets or equities which are actively traded.

However, we do hold a portfolio of highly rated asset backed securities and a portfolio of liquid assets (primarily 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. The instruments are also exposed to other forms of market risk e.g. credit spread risk. Prices are monitored on a daily basis to ensure that we are aware of any material diminution in value. Formal monthly prices are subject to independent review and are reported to ALCO. We have repurchase facilities in place which can 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 resulting from market price movements.

Interest rate risk

Interest rate risk appetite

We aim to minimise interest rate risk and have 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.

Mitigation

Hedge accounting

As detailed above, we use derivative contracts in order to hedge existing exposures on loans to customers, customer deposits and available for sale securities, principally with regard to following our policies in respect of the management of asset–liability gap and basis rate risks. Wherever possible we seek 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 21). However there are 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 due to operational process, 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 hedge accounting criteria are included within income as part of "Net expense from derivatives and other financial instruments at fair value through profit or loss", but, as they are not matched by similar adjustments to the hedged assets and liabilities, they give rise to volatility in the income statement on a year to year base which will reverse over the life of the hedge exposures.

Changes in the fair value of the hedged bonds and the hedging derivatives, and any differences between them, which were 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 from derivatives and other financial instruments at fair value through profit or loss".

Risk management

Principal risks continued

Analysis of interest rate risk

Asset–liability gap risk

Where possible we seek to match the interest rate structure of assets with liabilities, creating a natural hedge. Where this is not possible, we 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 exposures.

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 changes to economic value of the balance sheet as a result of a modelled 2% shift in the interest yield curve.

Basis risk

Basis risk is where there is a mismatch in the interest rate reference base for assets and liabilities. When we enter 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.

We have a market risk policy in place which places limits on the net mismatch between base rate linked assets and liabilities, and seek to manage the overall level of basis risk exposure by entering into basis swap agreements. As at 31 December 2016, the amount of the basis risk sensitivity measure was £0.0m (31 December 2015: £0.5m).

The impact of 2% shift in the interest yield curve is shown in the table below:

	2016 £m	2015 £m
2% shift up of the yield curve:		
As at year end	(7.0)	(5.5)
Average of month end positions reported to ALCO	(3.7)	(3.0)
2% shift down of the yield curve:		
As at year end	1.8	4.0
Average of month end positions reported to ALCO	0.9	1.3

The following shaded sections describe the operational risk, compliance, conduct and financial crime risk and reputational risks to which we are exposed. The sections are shaded as these areas are unaudited. All other areas of the Risk report are covered by the external auditor's opinion on page 142.

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This risk includes information technology, information security, change management, outsourcing, tax, legal, people and financial control risks.

Operational risk appetite

We aim to maintain robust operational systems and controls and seek to operate within an acceptable level of operational risk that enables execution of our business strategy, aiming for risks to be taken without unacceptable losses or reputational impacts. The operational risk appetite considers risk events and the assessment of internal controls as well as holding additional capital for certain operational risks.

Exposures

The key operational exposures that the Group is exposed to include: breakdowns in processes, controls or procedures (or their inadequacy relative to the growing size of the Group's business), systems failures and the risk of cyber threats, which impact the Group's information technology or critical infrastructure. The Group is also subject to the risk of business disruption, for example, arising from facilities/transport or utility failures, natural disasters and acts of terrorism, which may give rise to losses or reductions in service to customers and/or losses to the Group. Given the reliance on major outsource suppliers and critical suppliers, the Group is also exposed to risks in its supply chain.

The main operational risks to the Group are:

- Business continuity – risk of inadequate business recovery and disaster recovery capability to recover from any operational disruption and continue to provide product or service delivery to customers. The Group has a Business Continuity and Incident Management Framework which has been updated in 2016 and has been used to respond to internal and external events as appropriate.
- Change management – inability to execute changes effectively on a budget or to an acceptable quality. As a growing business, the Group has a significant change agenda to respond to customer and business needs, regulatory and legal developments and to deliver ongoing infrastructure and process capability to meet the Group's strategic aims.
- Financial Control and Management – The Group relies on timely, robust and accurate management information to support its financial and operational performance. The Group relies on appropriate models and, in certain cases, the use of estimates and management judgement in applying relevant accounting policies. This includes provisions for operation and conduct losses which have occurred and credit impairment charges.
- Information security – inappropriate disclosure of personal or sensitive information and/or inappropriate access to internal data sources. In particular, cyber security threats to the Group and its customers as a result of attacks through the use of computer systems exist. The growth in criminal trading of stolen data and the increasing size of the Group may increase motivation to attempt cybercrime against the Group and/or its customers. Threats continue to evolve as demonstrated by an increased increase in denial of service attacks, ransomware and increased sophistication of targeted fraud attacks by organised criminal networks. Failure to adequately manage cyber threats, and to continually review and update capabilities in response to new threats, could result in increased fraud losses, inability to perform critical economic functions, customer detriment, regulatory censure and penalty, legal liability and reputational damage. The Group continues to invest in its security infrastructure and remains aware that this is a constantly evolving threat, across the whole industry generally.
- Information technology – risks to the availability, performance and capacity of IT systems/telephony/internet. As the dependency on digital channels and other technologies grows, the impact of technology issues can become more material and immediate. The Group's technology and supplier infrastructure is critical to its operations and to the delivery of products and services to customers.

Risk management

Principal risks continued

- People – inability to attract, manage and retain competent employees to fulfil the needs of the Group. As the Group grows, it requires a diverse mix of skills and experience to deliver its strategy and its transformation and change agenda. Failure to attract and retain appropriate, qualified and skilled employees could adversely impact the Group's financial performance, control environment and compliance with evolving regulation and legislative developments.
- Process – ineffective design or execution of operational processes and payment or transaction processing failures. As the Group matures, the risks arising from existing processes may increase.
- Third party suppliers – inappropriate supplier selection and contractual arrangements, or inadequate ongoing management of critical suppliers and material outsource partners. The Group is reliant on a range of major outsource suppliers and critical suppliers for robust delivery and execution of services. The Group's Supplier Management Framework continues to evolve to ensure it is in line with regulatory expectations and industry best practice.

Mitigation and monitoring

The management of operational risk is a key area of management focus and we adopt the Basic Indicator Approach ("BIA") to operational risk. The Group has worked to understand its operational risk management framework as compared to peers and continues to align to the Basel Committee on Banking Supervision criteria for the sound management of operational risk.

The Operational Risk Management Framework has three key objectives:

- Minimise the impact of losses suffered from day-to-day operations (expected losses) and from extreme events (unexpected losses)
- Ensure awareness of the operational risks faced by the Group and the appropriate techniques to manage them in line with risk appetite
- Improve the effective management of the Group and protect its reputation and brand value

The prime responsibility for the management of operational risk and compliance within the Operational Risk Management Framework lies with business units and central functions. The Operational Risk function within Group Risk acts as a second line of defence and provides oversight and challenge of the operational risk profile, escalating issues as appropriate.

Senior management across the Group identify and assess operational risks within their respective areas and assess the effectiveness of key controls that mitigate those risks following the Risk & Control Self-Assessment process. This includes an assessment as to whether management actions are required to bring the risk within risk appetite, whether the level of risk is accepted, or escalation of the risk is required.

Operational risk event reporting is in place across the Group and corrective actions and recoveries are tracked accordingly.

We have placed emphasis on ensuring that the IT infrastructure, performance, resilience and security meet the ongoing needs of the business. Where possible the Group seeks to automate or mitigate through additional controls. In 2016 we have continued to make significant investment in cyber risk controls to ensure that we maintain appropriate levels of controls to counter the increasing threat of cyber-crime across the banking and financial services industries.

Mitigation of the risks arising from on-going changes and project activity is through a robust project governance structure and delivery framework. This approach was used to manage a series of projects during the year and ensures there are appropriate controls in place covering scoping and planning, design, initiation, monitoring and risk assessment. Following completion, post-implementation reviews are held to ensure any process or project improvements which are identified are implemented for future projects.

The Group aims to maintain an engaged and diverse workforce to ensure it can retain, develop and attract the right mix of skills and capabilities to deliver its strategy. Investment in staff training and personal development programmes, and support of both external and internal diversity projects, are key parts of ensuring we remain an employer of choice in the market.

Compliance, Conduct and Financial Crime risk

Compliance risk is the risk of legal or regulatory sanctions, material financial loss, or loss to reputation as a result of a failure to comply with applicable laws, regulations, codes of conduct and standards of good practice.

Conduct risk is the risk of legal or regulatory sanctions, material financial loss, or loss to reputation as a result of causing unfair outcomes or detriment to our customers and/or undermining market integrity as a result of our behaviour, decision making, activities or processes.

Financial crime risk is the risk of legal or regulatory sanctions, material financial loss, or loss to reputation as a result of the Group`s activities being used by criminals for the purposes of money laundering, terrorist financing, bribery and corruption and fraud.

Compliance, Conduct and Financial Crime risk appetite

We aim to minimise Compliance, Conduct and Financial Crime risk by maintaining robust systems and controls which are designed to meet existing legislative and regulatory requirements, identify new and emerging changes to the external landscape and that counter the threat of the Group's activities and products being used for the purposes of financial crime.

Exposures

The key compliance, conduct and financial crime risks that the Group is exposed to include:

Legal & Regulatory – failure to identify, interpret or respond to legal or regulatory changes or lack of contractual arrangements in place to protect the Group. The financial services industry continues to be the focus of significant regulatory change which requires the Group to both maintain compliance with existing regulations and to ensure delivery of change to achieve compliance with new and emerging regulations. The Group has a formal approach to reviewing such developments, assessing the impact on the Group and tracking our progress towards achieving compliance. Of particular current significance is the continuing embedding of the Senior Managers and Certification Regime (SMCR), the IFRS9 accounting changes, the recent BCBS capital proposals and the General Data Protection Regulations (GDPR) which are being closely managed.

Conduct – there is a risk 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 we have behaved inappropriately towards our customers, inappropriate sale processes and exhibiting behaviour that does not meet market or regulatory standards. Customer detriment could affect our reputation, lead to loss of market share due to damage to our brand and may lead to customer redress payments, regulatory action or censure.

Financial crime – failure to prevent the Group's products and services being used by criminals for the purposes of financial crime, including money laundering and terrorist financing or failure to comply with relevant financial sanctions requirements, and to prevent bribery and corruption. There is a risk the Group`s products and services could be the subject of significant fraud, either internally or externally leading to increased provisions and associated reputational damage.

Mitigation and monitoring

The primary responsibility for the management of compliance, conduct and financial crime risk lies with the business units and central functions in line with the SMCR responsibilities. The Compliance and Financial Crime functions within Group Risk act as a second line of defence and provide oversight of and challenge to the business and central functions, escalating issues as appropriate.

The Compliance and Financial Crime oversight functions are responsible for maintaining an appropriate risk framework for the management of compliance, conduct and financial crime risk, including setting the overall Group policies and minimum control requirements for the business and central functions to follow and for overseeing their compliance.

Senior management across the Group identify and assess compliance, conduct and financial crime risks (within their respective areas) and assess the effectiveness of key controls that mitigate those risks following the Risk & Control Self-Assessment process. This includes an assessment as to whether management actions are required to bring the risk within risk appetite, whether the level of risk is accepted or whether escalation of the risk is required.

Risk management

Principal risks continued

New and emerging legislative and regulatory driven changes are overseen through a defined model and standardised approach to ensure changes are both identified and assessed in terms of the impact on the Group. Any significant changes are implemented into the business units through a formal project governance approach.

We monitor and mitigate conduct risk by ensuring our products, services, business processes and procedures are designed to consistently deliver fair customer outcomes which are subject to ongoing assurance, monitoring, testing and reporting where we may be operating outside of risk appetite. Conduct risk metrics and KPIs (which include among others, staff performance levels, training, customer feedback, complaints, product retention rates, cancellations, arrears levels and customer service standards) are in place to evidence fair outcomes, identify any emerging issues and document remedial actions. Our recruitment, training and development programmes have a clear customer focus and reward mechanisms are aligned with fair customer outcomes.

The prevention of financial crime remains a key area of management focus. Money laundering checks are undertaken on all applicants to establish identity and the ultimate ownership structure for business customers. Financial sanctions and fraud checks are completed at application stage and during the customer lifecycle. Financial crime metrics and KPIs, (which include among others, fraud prevention value, frauds detected, fraud provisions and losses, suspicious activity reports and PEPs), are in place to oversee financial crime risk, identify any emerging issues and document remedial actions.

Monitoring and testing of customer processes and outcomes is undertaken within each business area and is supported by independent review and oversight through the Group Risk function.

Reputational risk

Reputational risk is defined as the potential negative consequences arising from a failure to meet the expectations and standards of our customers, investors, regulators or other counterparties during the conduct of any of our business activities. This includes not just the Group itself but all employees and other agents acting for, or otherwise associated with, the Group.

Reputational risk appetite

We aim to protect the strength of our reputation and franchise and consequently have a low appetite for reputational risk. We will seek to eliminate the potential for material risk events of this nature, or where this is not possible, mitigate them as fully and quickly as possible.

The Group will not conduct its business or engage with any stakeholders in a manner that could adversely impact its reputation or franchise value. In addition, the Group seeks to protect and enhance its reputation at all times through proactive engagement with stakeholders and on-going identification and assessment of reputational risk events with the Board and with the establishment of clear mitigating plans and actions.

Exposures

There are few reputational threats that are not intertwined with the outlined principal and emerging risks within this report. The key reputational risks the Group are exposed to include poor conduct and customer detriment, operational shortcomings, political and regulatory developments and external attacks.

Mitigation and monitoring

All employees are responsible for day-to-day identification and management of reputational risk. This is safeguarded by each employee conducting his or her business and personal activities in a manner that protects and enhances the Group's reputation.

The Board of Directors and Executive Management set the tone from the top, creating a strong culture of integrity and high ethical standards cascaded through the Group Corporate Governance Framework, Risk Management Frameworks and supporting policies and procedures.

Oversight of Reputational risk is provided by each of the committees detailed within the Risk Management Framework. In addition, the Group Corporate Affairs function supports the oversight and management of reputational risk and acts as a steward for protecting, promoting and enhancing our reputation amongst key stakeholders under the direction of the Chief Executive Officer. The principal monitoring and on-going reporting forum for Reputational Risk is the BRC. Ultimate oversight of reputational events and their resolution rests with the Board, reflecting the importance and longevity of this type of risk.

In 2016 emphasis was placed on ensuring our Crisis and Incident Management ("IMT") processes were robust and tested. Scenario based response plans were developed and further embedded communications into all crisis and IMT processes. This aims to mitigate reputational risk by ensuring a centrally coordinated response plan to prevent greater damage if a critical event occurs.

The Group follows a stakeholder–based approach in which reputational risk is identified and evaluated from a qualitative perspective depending on the stakeholder concerned.

In addition, the Group reinforces its commitment to protecting its reputation by adhering to the following principles:

- Operate in a way that is consistent with its risk appetite and the Group's values
- Conduct its business and operations with integrity and in compliance with the spirit and intent of all applicable laws and regulations in every jurisdiction in which it operates
- Undertake customer business in line with the published Terms and Conditions, and in a manner which results in fair outcomes for customers
- Will not engage in or facilitate any business activity where the purpose is to intentionally evade legal or regulatory obligations, or assist in aggressive tax avoidance schemes
- Maintain conflict of interest rules for employees, officers and Directors to protect the interest of customers and shareholders
- Recognise that the reputation, integrity and character of persons and organisations with whom we do business, such as service providers, counterparties and significantly influential clients may impact stakeholders' views of the Group and is an important consideration in establishing and maintaining relationships with them
- Maintain an open and transparent relationship with regulators and other key stakeholder groups
- Promote effective, proactive stakeholder management through ongoing engagement
- Encourage business and functions to take account of our reputation in all decision making, including dealings with customers and suppliers

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Statement of Directors' responsibilities in respect of the Annual Report and Accounts and the financial statements

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

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

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

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- 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 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.

Under applicable law and regulations, the Directors are also responsible for preparing a strategic report, Directors' Report, Remuneration Report and corporate governance statement that complies with that law and those regulations.

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

Responsibility statement of the Directors in respect of the annual financial report

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the Strategic report includes a fair review of the development and performance of the business and the position of the issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

We consider the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy.

Phillip Monks,

Chief Executive Officer

1 March 2017

Financial statements

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

Opinions and conclusions arising from our audit

1. Our opinion on the financial statements is unmodified

We have audited the financial statements of Aldermore Group PLC for the year ended 31 December 2016 set out on pages 148 to 204. 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 2016 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

2. Overview

The starting point for our audit was our experience as auditors of the Group since formation, including our assessment of the control environment and capital and liquidity positions, and we combined that with a consideration of external and internal developments and the risks they present to the Group's business model and how these risks are mitigated. These were considered in June 2016, were refreshed following the results of the EU referendum and the half year review, and have been continually reassessed through our interim and final audits. That consideration includes conversations not only with management and the Board, and ongoing knowledge gained through reading pertinent management information, but also reflected the views of the Prudential Regulatory Authority, market analysts, specialists within the firm, and peer comparisons.

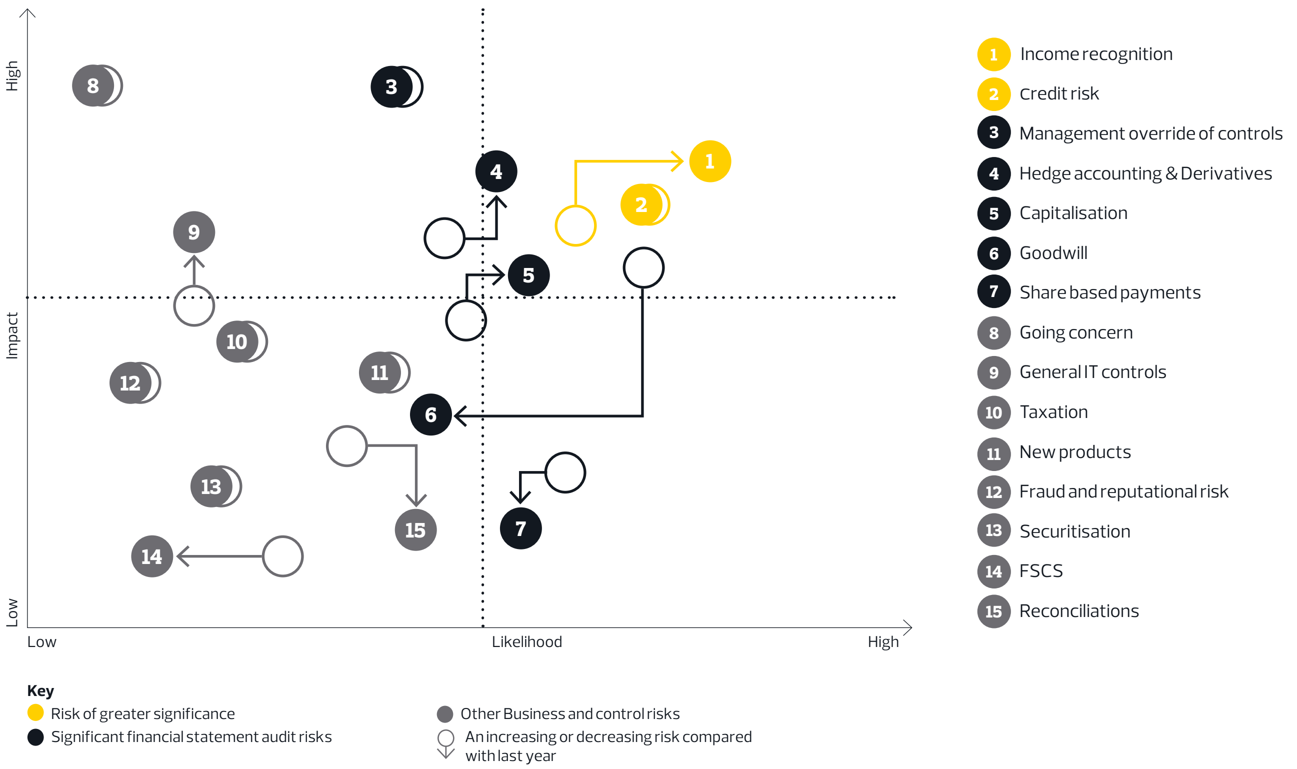
We considered that the impact of regulatory change, the greater competition within some of the Group's markets impacting redemptions, the data migrations due to core system upgrades and the challenge of meeting market expectations would increase the audit risk in the area of income recognition.

We considered that the continued strong loan growth, the challenge of meeting market expectations, the regulatory and tax challenges to the Buy-to-Let market and the impact of the result of the EU referendum could all increase the audit risk in the area of loan impairment. We note, however, that the risk continues to be mitigated through a lower interest rate environment and a relatively benign albeit uncertain credit outlook.

We considered that the audit risk in relation to goodwill has been substantially reduced, given that the Group have fully impaired the goodwill relating to the Invoice Finance Cash Generating Unit at the half year, due to a deterioration in the value of financial services companies following the result of the EU referendum.

Other factors we have considered in assessing the audit risks include the substantial project spend required in relation to systems projects, the emergence of digital and technological disrupters, increased regulation including the need to prepare for major financial reporting changes such as IFRS 9 and the Group's capital raising in October 2016.

The final result of our risk consideration is shown in the table, and we have shown those which have increased or decreased in risk. We are of the view that there are seven areas of significant risk, but two – income recognition and credit risk – represent the greatest significance.



3. Our assessment of risks of material misstatement

In arriving at our audit opinion above on the financial statements the risks of material misstatement that had the greatest effect on our audit were as follows:

Income Recognition: Effective Interest Rate asset of £34.8 million and offsetting liability of (£31.5 million) (2015: £23.9 million and (£21.5 million) respectively)

Refer to page 65 (Audit Committee Report), page 156 (accounting policy), page 168 (Use of estimates and judgements) and Note 5 (financial disclosures)

The Risk – Measuring interest income on loans and advances to customers under the effective interest rate method (Note 2(a)) requires the Directors to apply judgements, with the most critical being the expected life assumption.

The Group has a number of portfolios (including organic and acquired loans) across a variety of sectors and products which results in a large number of expected life assumptions. The sensitivity to a change in expected life can vary greatly over the portfolios depending on the underlying borrower and the other parameters also included in the effective interest rate calculation such as reversionary interest rates at the end of the fixed term, transaction costs and discounts or premium in place at inception.

The expected life assumptions utilise repayment profiles which represent how customers are expected to repay. The Group has limited historical experience to support these profiles due to the relatively unseasoned nature of its lending. Consequently, the Group makes its expected life assumptions based on its forecasting process which takes into account historical data but also, for the forecast period, the Group's expertise and experience in the sector. As such, any change in the expected life assumptions depend on the Directors' assessment of whether there is any emerging experience or market information that indicates a different repayment profile and by how much. As the forecast profiles extend significantly into the future this creates a high level of estimation uncertainty.

Financial statements

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

This has the greatest impact on the acquired loan portfolios (current balance: £113.4 million) because these were acquired at an upfront discount (unamortised balance: £7.0 million) and repayments are linked to the bank base rate with minimal incentive for the borrowers to remortgage until there is a change in interest rate expectations. This means any change in the repayment profile causes the discount received on purchase of the acquired portfolios to be adjusted and spread over the revised expected life.

In addition, repayment profiles will be affected by future changes in the market – for example, market pricing and the ability of borrowers to remortgage

The models used to measure revenue recognition rely on manual processes and controls which increase the risk associated with model stability and the completeness and accuracy of input data.

Our response – our audit procedures included:

- We tested the design, implementation and operating effectiveness of key controls over the completeness and accuracy of model inputs and the reconciliation of model outputs to the financial statements;
- We performed a reconciliation of data inputs used to measure interest income, including the loans split by product type, to reports from the Group reporting system;
- We tested application controls, with the involvement of our IT specialists, over the completeness and accuracy of the source loan input reports;
- We assessed the accuracy of the models by re-performing a sample of calculations and comparing the methodology used to our interpretation of the requirements of the relevant accounting standard;
- We tested the stability and integrity of the models with the involvement of our IT specialists;
- We challenged the appropriateness of key assumptions, including the expected lives and repayment profiles, by comparing these to the available historical customer trends within the Group, internal forecasts, and to our own expectations based on our knowledge of the Group and experience of the industry in which it operates, including the ability of customers to remortgage based on the current offerings in the market;
- For comparable lending and where available, we benchmarked the Group's expected life assumptions to peer data and/or market information; and
- We also considered the adequacy of the Group's disclosures about the changes in estimate that occurred during the period and the sensitivity disclosures across the key loan books.

Credit Risk: Impairment of loans and advances to customers £15.5 million (2015: £10.4 million)

Refer to page 64 (Audit Committee Report), page 160 (accounting policy), page 166 (Use of estimates and judgements) and Note 22 (financial disclosures)

The Risk – The impairment provision relating to the Group's loan portfolios requires the Directors to make significant judgements and assumptions over the recoverability of loan balances.

The Group performs an assessment of its loans for impairment as described in Note 2(g). The loan provision is most sensitive to assumptions made when assessing the collective provision, in particular in respect of the probability of default and the emergence period. This is because the Group has limited historical experience to support the assumptions made due to the relatively unseasoned nature of its loan portfolios underwritten during a relatively benign economic period.

To assess the probability of default, the Group uses a credit bureau to provide it with probabilities of default based on all available credit data for comparable borrowers. These probabilities are then adjusted (in almost all cases downwards) to reflect the Group's actual borrowers and the nature of its lending. The adjustments ('scalars') are based on the Group's internal data, which would not have been taken into account by the credit bureau. Management also apply overlays to the resultant modelled results to take into account both model risk and emerging risks that may not be otherwise appropriately factored in by the credit bureau.

The emergence period is assessed based on loans for which the Group is able to reliably measure the time between the trigger event occurring and the loans being identified as impaired. As the Group has limited historical data available, particularly in Asset Finance, the estimated emergence period is adjusted upwards (in the form of an overlay) and is based on market insight.

The Group's individual provisions can also require judgement, particularly in SME Commercial Mortgages and Asset Finance, where the valuation of collateral can be difficult to establish due to its specialised nature; as well as the exit strategy adopted, which can significantly impact the timing and value of the cash flows.

There continues to be regulatory focus on lending institutions factoring of forbearance arrangements adequately into their provisioning models.

The impact of the EU referendum result has also been assessed in regards to the potential impairment of collateral prices, uncertainties surrounding the House Price Index and potential increase in emergence periods as property markets have the potential of a slow down due to increased volatility in the funding markets.

Our response – our audit procedures included:

- We tested the design, implementation and operating effectiveness of key controls over the capture, monitoring and reporting of loans and advances to customers;
- We assessed the accuracy of the impairment model for collectively assessed loans, with assistance from our IT specialists, by re-performing a sample of calculations produced by the impairment model and compared the methodology used to our interpretation of the requirements of the relevant accounting standards;
- For loans assessed collectively for impairment we:
  - assessed the competency, reputation and objectivity of the credit bureau that provides the probabilities of default;
  - critically assessed the assumptions made in respect of the probabilities of default (inclusive of the scalars) and the emergence periods against our understanding of the Group as well as our knowledge of the wider market;
  - assessed the reasonableness of the methodology and accuracy of loss given default models;
  - assessed the consistency of the probabilities of default (inclusive of the scalars) and the emergence periods with the limited historic internal data available; assessed and challenged management overlays within the model for completeness and accuracy; and
  - assessed the accuracy of previous estimates of the collective provision.
- For a sample of exposures that were subject to an individual impairment assessment, and focusing on those with the most significant potential impact on the financial statements, we specifically challenged the Group's assumptions on the expected future cash flows, including the value of realisable collateral, based on our own understanding of the industry and reviewing latest correspondence on the loan and third party valuations or property indexes;
- Challenged management's assessment of identified cases of concern with material exposure;
- We assessed the performing loan book by using data analytics techniques to identify loans with characteristics that could indicate unidentified impairment;
- We benchmarked the Group's key metrics, such as arrears trends and provision coverage, to externally available data, with particular focus on similar lending; and
- We also considered compliance with the relevant accounting standards including the adequacy of the Group disclosures in relation to impairment.

Financial statements

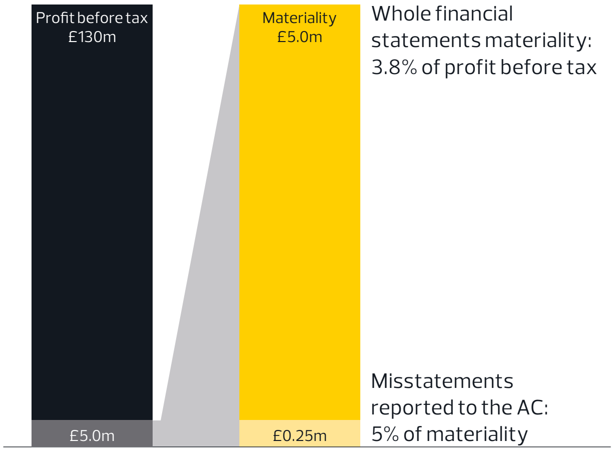
Independent auditor's report to the members of Aldermore Group PLC only continued

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

The materiality for the Group financial statements as a whole was set at £5.0 million (2015: £3.0 million), determined with reference to a benchmark of the Group profit before tax of £130.0 million (2015: £95 million), of which it represents 3.9% (2015: 3.1%).

The benchmark percentage has been increased from 3.1% to 3.9% due to an improved control environment, resulting from increased stability in controls and processes over risks as a listed entity.

We report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £0.25 million (2015: £0.15 million), in addition to other identified misstatements that warranted reporting on qualitative grounds.



The Group audit team performed the audit of the Group and its only material component as if it were a single aggregated set of financial information. The audit was performed using the materiality level set out above and covered 100% of total Group revenue, Group profit before tax, and total Group assets.

5. Our opinion on other matters prescribed by the Companies Act 2006 is unmodified

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006;
- the information given in the strategic report and the Directors' Report for the financial year is consistent with the financial statements; and
- the information given in the corporate governance statement set out on page 31 with respect to internal control and risk management systems in relation to financial reporting processes and about share capital structures ("the specified corporate governance information") is consistent with the financial statements.

Based solely on the work required to be undertaken in the course of the audit of the financial statements and from reading the strategic report, the Directors' Report and the corporate governance statement:

- we have not identified material misstatements in the strategic report, the Directors' Report, or the specified corporate governance information;
- in our opinion, the strategic report and the Directors' Report have been prepared in accordance with the Companies Act 2006; and
- in our opinion, the corporate governance statement has been prepared in accordance with rules 7.2.2, 7.2.3, 7.2.5, 7.2.6 and 7.2.7 of the Disclosure Rules and Transparency Rules of the Financial Conduct Authority.

6. We have nothing to report on the disclosures of principal risks

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

- the Directors' statement of risk management on pages 31 to 35, internal control on page 31 and viability reporting on page 31 concerning the principal risks, their management, and, based on that, the Directors' assessment and expectations of the Group's continuing in operation over the three years to 31 December 2019; or
- the disclosures in Note 1 of the financial statements concerning the use of the going concern basis of accounting.

7. We have nothing to report in respect of the matters on which we are required to report by exception

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the annual report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading.

In particular, we are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our audit and the Directors' statement that they consider that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy; or
- the Audit Committee Report does not appropriately address matters communicated by us to the Audit Committee.

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

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited 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; and
- a corporate governance statement has not been prepared by the company.

Under the Listing Rules we are required to review:

- the Directors' statements, set out on pages 103 and 31, in relation to going concern and longer-term viability; and
- the part of the corporate governance statement on page 40 relating to the company's compliance with the eleven provisions of the 2014 UK Corporate Governance Code specified for our review.

We have nothing to report in respect of the above responsibilities.

Scope and responsibilities

As explained more fully in the Directors' Responsibilities Statement set out on page 141, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. 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. This report is made solely to the company's members as a body and is subject to important explanations and disclaimers regarding our responsibilities, published on our website at www.kpmg.com/uk/auditscopeukco2014a, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

Michael Peck (Senior Statutory Auditor)

for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL

1 March 2017

Financial statements

Consolidated income statement
For the year ended 31 December 2016

	Note	**Year ended 31 December 2016 £m**	Year ended 31 December 2015 £m
Interest income	5	358.2	300.4
Interest expense	6	(118.8)	(101.5)
Net interest income		**239.4**	**198.9**
Fee and commission income	7	30.0	25.2
Fee and commission expense	8	(7.5)	(7.0)
Net expense from derivatives and other financial instruments at fair value through profit or loss	9	(4.4)	(2.1)
Gains on disposal of available for sale debt securities		3.8	2.3
Other operating income	10	6.2	7.4
Total operating income		**267.5**	**224.7**
Provisions	33	(0.8)	(2.3)
Costs in respect of initial public offering		–	(4.1)
Impairment of goodwill	11	(4.1)	–
Other administrative expenses		(113.1)	(107.9)
Administrative expenses	11	(118.0)	(114.3)
Depreciation and amortisation	15	(5.3)	(5.3)
Operating profit before impairment losses		**144.2**	**105.1**
Impairment losses on loans and advances to customers	22	(15.5)	(10.4)
Profit before taxation		**128.7**	**94.7**
Taxation	17	(35.2)	(16.4)
Profit after taxation – attributable to equity holders of the Group		**93.5**	**78.3**

Basic earnings per share (pence)	18	25.2p	22.7p
Diluted earnings per share (pence)	18	25.2p	22.6p

The notes and information on pages 153 to 198 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 2016

	Year ended 31 December 2016 £m	Year ended 31 December 2015 £m
Profit after taxation	**93.5**	**78.3**
Other comprehensive income/(expense):		
Items that may subsequently be transferred to the income statement:		
Available for sale debt securities:		
Fair value movements	7.6	(0.9)
Amounts transferred to the income statement	(3.8)	(2.1)
Taxation	(1.0)	0.6
Total other comprehensive income/(expense)	**2.8**	**(2.4)**
Total comprehensive income attributable to equity holders of the Group	**96.3**	**75.9**

The notes and information on pages 153 to 198 form part of these financial statements.

Financial statements

Consolidated statement of financial position
As at 31 December 2016

	Note	31 December 2016 £m	31 December 2015 £m
Assets			
Cash and balances at central banks		116.4	105.3
Loans and advances to banks	19	67.2	94.2
Debt securities	20	664.5	606.1
Derivatives held for risk management	21	12.4	6.7
Loans and advances to customers	22	7,477.3	6,144.8
Fair value adjustment for portfolio hedged risk		(3.5)	1.1
Other assets	24	3.1	1.4
Prepayments and accrued income	25	3.4	5.1
Deferred taxation	26	11.2	16.4
Property, plant and equipment	27	3.1	3.4
Intangible assets	28	26.1	24.0
Total assets		**8,381.2**	**7,008.5**
Liabilities			
Amounts due to banks	29	753.8	405.1
Customers' accounts	30	6,673.7	5,742.0
Derivatives held for risk management	21	35.8	35.4
Fair value adjustment for portfolio hedged risk		(1.2)	(0.8)
Other liabilities	31	25.0	21.9
Accruals and deferred income	32	27.0	25.7
Current taxation		9.7	12.5
Provisions	33	0.8	1.1
Debt securities in issue	34	130.6	193.9
Subordinated notes	35	100.0	38.1
Total liabilities		**7,755.2**	**6,474.9**
Equity			
Share capital	36	34.5	34.5
Share premium account		73.4	73.4
Contingent convertible securities	38	74.0	74.0
Capital redemption reserve		0.1	0.1
Available for sale reserve		1.8	(1.0)
Retained earnings		442.2	352.6
Total equity		**626.0**	**533.6**
Total liabilities and equity		**8,381.2**	**7,008.5**

The notes and information on pages 153 to 198 form part of these financial statements.

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

Phillip Monks
Director
1 March 2017

James Mack
Director
1 March 2017

Registered number: 06764335

Consolidated statement of cash flows
For the year ended 31 December 2016

	Note	**Year ended 31 December 2016 £m**	Year ended 31 December 2015 £m
Cash flows from operating activities			
Profit before taxation		128.7	94.7
Adjustments for non-cash items and other adjustments included within the income statement	39	11.3	9.1
Increase in operating assets	39	(1,332.8)	(1,317.9)
Increase in operating liabilities	39	1,284.5	1,368.1
Income tax paid		(31.5)	(20.2)
Net cash flows generated from operating activities		**60.2**	**133.8**
Cash flows from investing activities			
Purchase of debt securities		(298.4)	(414.0)
Proceeds from sale and maturity of debt securities		161.7	279.0
Capital repayments of debt securities		87.5	32.9
Interest received on debt securities		12.9	10.5
Purchase of property, plant and equipment and intangible assets		(11.2)	(7.3)
Net cash used in investing activities		**(47.5)**	**(98.9)**
Cash flows from financing activities			
Proceeds from issue of shares		–	75.0
Issuance costs of Initial Public Offering		–	(2.7)
Proceeds from exercise of warrants		–	5.6
Proceeds from the issue of subordinated debt		60.0	–
Issuance costs of subordinated debt		(0.6)	–
Capital repayments on debt securities issued		(63.6)	(85.7)
Purchase of own shares by Employee Benefit Trust		(0.9)	–
Coupon paid on contingent convertible securities		(8.9)	(3.5)
Interest paid on debt securities		(2.0)	(3.0)
Interest paid on subordinated notes		(5.2)	(5.2)
Net cash used in financing activities		**(21.2)**	**(19.5)**
Net (decrease)/increase in cash and cash equivalents		**(8.5)**	**15.4**
Cash and cash equivalents at start of the year	39	149.4	134.0
Movement during the year		(8.5)	15.4
Cash and cash equivalents at end of the year	39	**140.9**	**149.4**

Financial statements

Consolidated statement of changes in equity
For the year ended 31 December 2016

	Note	Share capital £m	Share premium account £m	Contingent convertible securities £m	Capital redemption reserve £m	Warrant reserve £m	Available for sale reserve £m	Retained earnings £m	Total £m
Year ended 31 December 2016									
As at 1 January		34.5	73.4	74.0	0.1	–	(1.0)	352.6	533.6
Total comprehensive income		–	–	–	–	–	2.8	93.5	96.3
Transactions with equity holders:									
– Share-based payments, including tax reflected directly in retained earnings	37	–	–	–	–	–	–	3.6	3.6
– Own shares adjustment	36	–	–	–	–	–	–	(0.9)	(0.9)
– Coupon paid on contingent convertible securities, net of tax		–	–	–	–	–	–	(6.6)	(6.6)
As at 31 December		**34.5**	**73.4**	**74.0**	**0.1**	**–**	**1.8**	**442.2**	**626.0**
Year ended 31 December 2015									
As at 1 January		23.7	–	73.7	–	2.2	1.4	277.9	378.9
Total comprehensive income		–	–	–	–	–	(2.4)	78.3	75.9
Transactions with equity holders:									
– Capital reorganisation prior to IPO		6.3	–	–	0.1	–	–	(6.4)	–
– Share issue proceeds from IPO	36	3.9	71.1	–	–	–	–	–	75.0
– Share issuance costs		–	(2.7)	–	–	–	–	–	(2.7)
– Share-based payments, including tax reflected directly in retained earnings	37	–	–	–	–	–	–	3.4	3.4
– Coupon paid on contingent convertible securities, net of tax		–	–	–	–	–	–	(2.8)	(2.8)
– Tax credit on AT1 issue costs		–	–	0.3	–	–	–	–	0.3
– Exercise of share warrants	36	0.6	5.0	–	–	(2.2)	–	2.2	5.6
As at 31 December		**34.5**	**73.4**	**74.0**	**0.1**	**–**	**(1.0)**	**352.6**	**533.6**

Notes to the consolidated 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") include 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 ("EU"). For IAS 39: "Financial Instruments: Recognition and Measurement" the exclusion regarding hedge accounting (the so called "carve out") decreed by the EU on 19 November 2014 is taken into account.

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 returns.

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

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 22). 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 vehicle 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 statement of financial position, 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, including a range of stressed scenarios, show that it will be able to operate with adequate levels of both liquidity and capital for the foreseeable future. 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 planned expansion. Additionally, 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").

Financial statements

Notes to the consolidated 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;
- certain debt securities which are 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) Presentation of risk and capital disclosures

The disclosures required under IFRS 7: "Financial instruments: disclosures" and IAS 1: "Presentation of financial statements" have been included within the audited sections of the Risk Report on page 106. Where information is marked as audited, it is incorporated into these financial statements by this cross reference and it is covered by the Independent Auditor's report on page 142.

g) Future accounting developments

All standards or amendments to existing standards which have been endorsed by the EU and which are available for early adoption for annual periods commencing on or after 1 January 2016 have been adopted by the Group apart from IFRS 9: "Financial Instruments" and IFRS 15: "Revenue from contracts with customers".

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 16: "Leases" the planned replacement for IAS 17: "Leases".

IFRS 9: "Financial Instruments" is the comprehensive standard to replace IAS 39 "Financial Instruments: Recognition and Measurement" and was endorsed by the EU on 22 November 2016. IFRS 9 is effective for annual periods beginning on or after 1 January 2018 and is required to be applied retrospectively. However, prior periods need not be restated, instead an adjustment may be reflected in opening retained earnings at the start of the period when IFRS 9 is first adopted.

The standard includes requirements for classification and measurement of financial assets and liabilities, hedge accounting and the impairment of financial assets.

Classification and measurement

The classification of financial assets will be based on the objectives of the Group's business model and the contractual cash flow characteristics of the instruments. Financial assets will then be classified as held at amortised cost, at fair value through other comprehensive income ("FVOCI"), or at fair value through profit or loss ("FVTPL"). In most instances, the measurement outcomes will be similar to those under IAS 39 and therefore, any changes from the accounting treatment currently followed by the Group under IAS 39 are not expected to be significant. The classification of financial liabilities is essentially unchanged from the treatment under IAS 39.

Impairment of financial assets

Impairment provisions in all financial assets are recognised based on either 12 month expected losses or lifetime expected losses. This will result in the acceleration of the recognition of impairment provisions and will lead to more volatile impairment charges in the income statement. However, whilst IFRS9 represents a significant change compared to IAS 39, the quantum of impairment losses recorded against any one loan over the life of the loan will not change as IFRS 9 alters only the timing of recognition of impairment losses.

IFRS 9 introduces a number of changes to approach as compared to the current methodology under IAS 39. The main changes are:

- Expected credit losses ("ECL") are based on an assessment of the probability of default, loss given default and exposure at default discounted to give a net present value. The estimation of ECL should be unbiased and probability weighted to reflect a range of possible outcomes taking into account all reasonable and supportable information including forward-looking economic assumptions.
- On initial recognition, and for financial assets where there has not been a significant increase in credit risk since the date of origination, IFRS 9 provisions will be made to reflect ECL arising from expected credit default events within the next 12 months.
- A key requirement of IFRS 9, compared with the existing impairment approach under IAS 39, relates to assets where there has been a significant increase in credit risk since the date of origination. Provisions will be made for those assets expected to default at any point over their lifetime, reflecting the asset's full expected loss.
- For assets where there is evidence of credit impairment, provisions will be made under IFRS 9 for lifetime expected credit losses, taking account of forward looking economic assumptions and a range of possible outcomes. Under IAS 39, provisions are currently based on the asset's carrying value and the present value of the estimated future cash flows.

It is not anticipated that changes in the approach to impairment will have a significant impact on the Group's provisions in respect of specifically impaired loans, as the current provisions on such loans are based on estimates of lifetime expected losses arising based on expected future cash flows, but excluding any future credit losses that have not yet been incurred.

In respect of other loans, against which collective provisions are raised, our current approach, as explained in Note 3(a), is to estimate probabilities of default 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, management currently adjust the calculated 12 month expected loss, which is based on management's current best estimates, for an emergence period based on the nature of the underlying asset enabling management to reflect only the impairment considered to have been incurred at the reporting date. Under IFRS 9, the estimated probabilities of default will need to be probability weighted, based on a range of possible economic scenarios.

While the Group's current approach to calculating collective impairment provisions (as described above) has similarities to the approach required under IFRS 9, it should be noted that IFRS 9 is a complex accounting standard and the Group's detailed credit modelling approach remains under development.

Hedge accounting

The hedge accounting requirements of IFRS 9 are designed to create a stronger link with financial risk management. At present, IFRS 9 does not address the portfolio hedging of interest rate risk currently undertaken by the Group. Pending development of the IASB's proposals for dynamic risk management (macro hedge accounting), to be considered in a separate accounting standard, IFRS 9 allows the option to continue to apply the existing hedge accounting requirements of IAS 39. The Group plans to exercise the accounting policy choice to continue IAS 39 hedge accounting (including the so called "carve out" as described in Note 2(j)).

Financial statements

Notes to the consolidated financial statements continued

1. Basis of preparation continued

Implementation

The Group has established an IFRS 9 programme. The programme is jointly sponsored by the Chief Financial Officer and Chief Risk Officer. The programme is cross-functional with representation from (but not limited to) Finance, Risk and IT. Progress is regularly reported to the IFRS 9 Steering Group and the Audit Committee.

The key features of the programme include defining the IFRS 9 methodology and accounting policies, identifying data, reconciliation and system requirements, and the development and establishment of appropriate and compliant operating models within an appropriate governance framework.

Extensive work is being carried out with regards to technical analysis, the development of the credit models and the design of the required changes to systems, data, business processes, reporting and governance relating to impairment provisions. During 2017, work will include building and testing of credit models and validating outputs, development of management information, implementation of business process changes and a parallel run phase.

The financial impact of IFRS 9 will be quantified once models and systems are further developed. Impacts are expected to be disclosed no later than in the financial statements for the year ending 31 December 2017.

The IASB has also issued IFRS 15: "Revenue from contracts with customers". IFRS 15 provides a principles-based approach to recognise revenue and the concept of recognising revenue for obligations as they are satisfied. The impact for the Group is currently being assessed but may impact our treatment of fees and commissions and other operating income, the majority of which relates to the Invoice Finance business. The Standard was endorsed on 29 October 2016 and will be effective for annual reporting periods beginning on or after 1 January 2018 with retrospective application permitted.

On 13 January 2016, the IASB issued IFRS 16: "Leases" as a replacement for IAS 17: "Leases". The Standard will be effective for annual reporting periods beginning on or after 1 January 2019, with early application being permitted for companies that also apply IFRS 15. The impact for the Group is currently being assessed. A significant change will be the inclusion of a "right of use asset" within the statement of financial position in respect of the benefit the Group receives where it leases assets under operating leases, together with a financial liability in respect of the obligation to make operating lease payments. Within the income statement, an operating charge will be reflected in respect of the use of the asset together with interest expense in relation to the financing, replacing the current operating lease charges included in administrative expenses.

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 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

i. 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 segment 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 mortgage services, arrears, and insurance commission receivable. Fee income is recognised as the related services are performed.

Arrangement fees and other fees relating to loans and advances which do meet the criteria for inclusion within interest income are included as part of the EIR.

ii. 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.

iii. 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.

(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.

Financial statements

Notes to the consolidated financial statements continued

2. Significant accounting policies continued

ii. Derecognition

Financial assets are derecognised when there 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, 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 'Amounts due to banks'. Interest is accrued over the life of the agreement on an EIR basis.

iv. Term Funding Scheme ("TFS")

Loans and advances over which the Group transfers its rights to the collateral thereon to the Bank of England under the TFS 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 cash received against the transferred assets 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 'Amounts 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. Financial 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. The Group disposed of all of its financial assets designated at fair value through profit or loss during 2015.

(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 EIR 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 method 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.

(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 may 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

Financial statements

Notes to the consolidated financial statements continued

2. Significant accounting policies continued

- 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 mitigate 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 may be 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 more than 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.

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 uncollectable 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. 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 allowance that has 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 market, 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.

Where 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.

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

Financial statements

Notes to the consolidated financial statements continued

2. Significant accounting policies continued

(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.

i. Fair value hedge accounting for portfolio hedges of interest rate risk

The Group applies fair value hedge accounting for portfolio hedges of interest rate risk. 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 the 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 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 recognised in 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.

(l) Property, plant and equipment

Items of property, plant and equipment are stated at cost, or deemed cost on 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 in 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.

(m) Intangible assets

i. Goodwill

Goodwill is stated at deemed cost upon 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.

ii. 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, i.e. goodwill and other intangible 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.

i. Goodwill

Goodwill is tested for impairment at least annually. For the purpose of impairment testing, goodwill is allocated to operating segments. An impairment loss is recognised if the carrying amount of a segment is less than its recoverable amount.
The recoverable amount of a segment is the greater of its value in use and its fair value less costs to sell. Value in use is calculated from 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. Fair value is determined through review of precedent transactions for comparable businesses.

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

ii. Other intangible assets

If impairment is indicated, the asset's recoverable amount, being the greater of value in use and fair value less costs to sell, 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

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.

Financial statements

Notes to the consolidated financial statements
continued

2. Significant accounting policies continued

(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 from the point 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. The FSCS provision is recognised at the commencement of the scheme year in line with IFRIC 21.

(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 statement of financial position date are translated into sterling using the exchange rates ruling at the statement of financial position date. Exchange differences are charged or credited to the income statement.

(s) Taxation

Taxation comprises current and deferred tax, and 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 statement of financial position 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 statement of financial position 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 and contingent convertible securities are presented as components of equity.

Any dividends, interest or other distributions on capital instruments are also recognised in equity. Any related 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.

(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 such that the recoverable amount is lower than the carrying value.

(y) Warrants

The Company's subsidiary, Aldermore Bank PLC, previously issued subordinated notes with attached warrants. The warrants gave the holders the right to subscribe for shares in the Company. These warrants were exercised during 2015 resulting in an increase in share capital and share premium. On exercise, the warrant reserve was re-classified to retained earnings.

(z) Share-based payment transactions

Employees (including Senior Executives) of the Group may receive remuneration in the form of equity settled share-based payments to incentivise and reward future strong, long-term business performance and growth.

The grant date fair value is recognised as an employee expense with a corresponding increase in equity over the period that the employees become unconditionally entitled to the awards. The grant date fair value is determined using valuation models which take into account the terms and conditions attached to the awards. Inputs into valuation models may include the risk-free interest rate, the expected volatility of the Company's share price and other factors related to performance conditions attached to the awards.

The amount recognised as an expense is adjusted to reflect differences between expected and actual outcomes, 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 market performance conditions or 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.

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

Employee Benefit Trust ("EBT")

An EBT purchased shares in the Company for the sole purpose of satisfying awards under employee share plans. These shares continue to be held within the acquiring EBT, which is consolidated in these financial statements as the EBT is deemed to be controlled by the Group.

Where an Employee Benefit Trust ('EBT') purchases the Company's share capital, the consideration paid is deducted from shareholders' equity as own shares until they are cancelled. Where such shares are subsequently sold or reissued, any consideration received is included in shareholders' equity.

Financial statements

Notes to the consolidated financial statements continued

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, EIR, and Invoice Finance goodwill.

(a) Loan impairment provisions

Loan portfolios across all segments 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 statement of financial position 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 2016, gross loans and advances to customers totalled £7,504.7 million (31 December 2015: £6,165.5 million) against which impairment allowances of £27.4 million (31 December 2015: £20.7 million) had been made (see Note 22). 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 £27.4 million at 31 December 2016, £14.3 million (31 December 2015: £10.2 million) relates to individual provisions and £13.1 million (31 December 2015: £10.5 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.

i. Individual

Individual impairment allowances are established against the Group's individual 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.

ii. Collective

The collective impairment allowance is also subject to estimation uncertainty and, in particular, is sensitive to changes in economic and credit conditions, including house prices, unemployment rates, interest rates, borrowers' behaviour and consumer bankruptcy trends. All of these factors can influence the key assumptions detailed below. However, it is 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 impairment 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 identified.

The Group uses two types of underlying models to calculate the LGD, depending on the availability of default data. For SME Commercial Mortgages, Buy-to-Let and Residential Mortgages the models use a range of key assumptions to derive an expected LGD. The key assumptions are based on management expertise and are validated against available data. For Asset Finance and Invoice Finance, the models are empirical models which use historical loss data to determine the risk drivers behind the loss.

This allows the portfolios to be segmented into homogeneous buckets to derive an LGD. Further details in respect of assumptions and details of the sensitivity of the estimate 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 'conversion 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 'conversion 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 £0.5 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 £0.7 million.

Loss given default:

The model calculates the LGD from the point of repossession of the asset. 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 £0.5 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 £2.6 million.
- A 5 per cent. absolute increase in the FSD would increase the overall impairment provision by £2.0 million.

The above assumptions are important factors when calculating the LGD to be applied for the Mortgage business.

For the Asset Finance and Invoice Finance model, the assumption with most judgment is the absolute LGD value calculated.

- A 10 per cent. relative increase in the LGD's applied in Asset Finance and Invoice Finance would increase the overall impairment allowance by £0.9 million.

Emergence period:

The Group's collective models estimate the expected losses for the next 12 months, these are then scaled back using the emergence period to reflect the level of incurred loss as at the reporting date. The emergence period is the time taken from the trigger event (such as a job loss) to the Group identifying the loan as impaired. The emergence period varies by segment and requires management to make judgements because of the limited data available. During the year, management increased the emergence period applied to the Mortgage businesses by three months in order to apply a degree of caution to reflect the potential impact of political and economic uncertainty resulting from the EU referendum. The impact of this change was to increase the collective provisions by £1.6 million.

- A further three month increase in emergence periods for Asset Finance and Invoice Finance would increase the overall impairment allowance by £4.5 million.

Financial statements

Notes to the consolidated financial statements continued

3. Use of estimates and judgements continued

(b) Effective interest rate ("EIR")

IAS 39 requires interest earned from mortgages to be measured under the EIR method. Management must therefore use judgement to estimate the expected life of each type of instrument and hence the expected related cash flows. The accuracy of the EIR would therefore be affected by unexpected market movements resulting in altered customer behaviour and inaccuracies in the models used compared to actual outcomes.

A critical estimate in determining EIR is the expected life to maturity of the Group's SME Commercial, Buy-to-Let and Residential Mortgage portfolios, as a change in these estimates will impact the period over which the directly attributable costs and fees and any discount received on the acquisition of mortgage portfolios are recognised as part of the EIR.

Included within the overall Mortgages book, are a small number of portfolios which were acquired by the Group and, as at 31 December 2016, represent approximately 2 per cent, 2 per cent and 3 per cent of SME Commercial, Buy-to-Let and Residential Mortgages net loans respectively. These portfolios were acquired at a discount which is being recognised under the EIR method. As disclosed below, these portfolios, although representing a small proportion of overall lending, are sensitive to a change in the expected repayment profiles which would impact the periods over which the discount is to be unwound.

As at 31 December 2016 and 31 December 2015 , a reassessment was made of the estimates used in respect of the expected lives of the SME Commercial, Buy-to-Let and Residential Mortgage portfolios and also of those for the Asset Finance portfolios. As a consequence, an overall adjustment of £0.5 million (2015: £0.4 million) was recorded to increase the value of the loan portfolios and the interest income recognised in the current period, so that interest can continue to be recognised at the original effective interest rate over the remaining life of the relevant lending portfolios.

The adjustment made at 31 December is analysed as follows:

	Impact on 2016 interest income £m	Impact on 2015 interest income £m
Asset Finance – organic lending	**(1.8)**	(1.6)
SME Commercial – acquired portfolios	**–**	(0.7)
SME Commercial – organic lending	**0.2**	(0.9)
Buy-to-Let – acquired portfolios	**(1.1)**	(0.6)
Buy-to-Let – organic lending	**0.1**	0.1
Residential – acquired portfolios	**(0.4)**	(1.1)
Residential – organic lending	**3.5**	5.2
	0.5	0.4

A change in the estimated expected lives, after taking account of the above adjustment, to extend the expected lives of the SME Commercial, Buy-to-Let and Residential Mortgage portfolios by six months would have the effect of reducing the cumulative profit before tax recognised as at 31 December 2016 by £1.4 million (31 December 2015: £1.5 million). Included within this sensitivity of £1.4 million, is a £3.1 million cumulative reduction in profit relating to acquired portfolios (31 December 2015: £2.8 million) due to a change in the unwind of the discount which is offset by a £1.7 million cumulative increase in profit relating to the organic portfolios (31 December 2015: £1.3 million).

A 0.5 per cent. increase in the rate of early redemptions, expressed as a percentage of the outstanding balance in respect of the Asset Finance portfolio would have the impact of reducing cumulative profit before tax recognised as at 31 December 2016 by £0.5 million (31 December 2015: £0.3 million).

(c) Share-based payments

The fair value of the share awards is calculated using statistical models. The inputs to these models require management judgement to estimate the probability and timings of events taking place in the future. The significant inputs used in the models include the exercise price, share price, expected volatility, expected life and the risk free rate. The share-based payment recognised can be materially affected by these assumptions. Further information on the key assumptions can be found in Note 37.

(d) Invoice Finance goodwill

IAS 36 requires an assessment of goodwill balances for impairment on at least an annual basis. An impairment charge should be recognised where the recoverable amount from the segment is less than the carrying value of the goodwill.

During 2016, as a result of the general fall in market values of financial services businesses that occurred following the EU referendum, there was an indication of impairment and the Invoice Finance goodwill was fully impaired. An impairment charge of £4.1 million has been recognised in the income statement.

4. Segmental information

The Group has five reportable operating segments as described below which are based on the Group's five lending segments plus Central Functions. Each segment offers groups of similar products and services and are managed separately based on the Group's internal reporting structure.

SME Commercial Mortgages, Buy-to-Let and Residential Mortgages are operated under a single management team and supported by a single IT platform. Shared administrative expenses in the mortgage business have been apportioned across these segments on the basis of business activity levels in each segment.

However, the characteristics of the three segments are sufficiently different, are reported separately to the Board and therefore, they 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:

- Asset Finance – Lease and hire purchase financing for SMEs, focusing on sectors with strong returns and liquid secondary asset markets;
- Invoice Finance – provides UK SMEs with working capital solutions through invoice discounting, factoring and asset based lending;
- SME Commercial Mortgages – Property finance needs of professional, commercial property investors, and owner-occupier SMEs. Targets prime and specialist prime segments with loan sizes generally below £5 million;
- Buy-to-Let – Offers a wide range of standard and specialist buy-to-let mortgages for residential units, multi-unit freehold or houses with multiple-occupation ("HMO") to both individuals and companies; and
- Residential Mortgages – Prime residential mortgages targeting underserved segments of creditworthy borrowers that provide attractive and sustainable margins.

Central Functions includes the reconciling items between the total of the five 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 the operating segments, apart from those costs relating to the subordinated notes and the net expense/income from derivatives held at fair value shown in Note 6.

Common costs are incurred on behalf of the operating segments and typically represent savings administration, back office 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 is shown below. Performance is measured based on the segmental result as included in the internal management reports.

Financial statements

Notes to the consolidated financial statements continued

4. Segmental information continued

Segmental information for the year ended 31 December 2016

	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages £m	Buy-to-Let £m	Residential Mortgages £m	Central Functions[1] £m	Total £m
Interest income – external customers	87.3	7.0	58.4	135.6	75.7	(5.8)	358.2
Interest expense – external customers	–	–	–	–	–	(118.8)	(118.8)
Interest (expense)/income – internal	(27.9)	(2.2)	(13.0)	(45.2)	(26.1)	114.4	–
Net fees and other income – external customers	4.2	14.2	1.3	6.8	1.9	(0.3)	28.1
Total operating income	**63.6**	**19.0**	**46.7**	**97.2**	**51.5**	**(10.5)**	**267.5**
Administrative expenses including depreciation and amortisation	(12.9)	(10.3)	(3.1)	(10.7)	(4.5)	(81.8)	(123.3)
Impairment losses on loans and advances to customers	(5.6)	(1.7)	(2.9)	(3.4)	(1.9)	–	(15.5)
Segmental result	**45.1**	**7.0**	**40.7**	**83.1**	**45.1**	**(92.3)**	**128.7**
Tax							(35.2)
Profit after tax							**93.5**
Assets	1,573.4	154.1	929.9	3,326.0	1,493.9	903.9	8,381.2
Liabilities	–	–	–	–	–	(7,755.2)	(7,755.2)
Net assets/(liabilities)	**1,573.4**	**154.1**	**929.9**	**3,326.0**	**1,493.9**	**(6,851.3)**	**626.0**

1 Central Functions administrative expenses of £81.8 million includes an impairment charge of £4.1 million in relation to Invoice Finance goodwill.

Segmental information for the year ended 31 December 2015

	Asset Finance £m	Invoice Finance £m	SME Commercial Mortgages £m	Buy-to-Let £m	Residential Mortgages £m	Central Functions[1] £m	Total £m
Interest income – external customers	75.7	7.6	44.8	111.0	66.4	(5.1)	300.4
Interest expense – external customers	–	–	–	–	–	(101.5)	(101.5)
Interest (expense)/income – internal	(23.9)	(2.3)	(10.6)	(37.7)	(22.6)	97.1	–
Net fees and other income – external customers	4.3	15.2	0.8	3.0	2.2	0.3	25.8
Total operating income	**56.1**	**20.5**	**35.0**	**76.3**	**46.0**	**(9.2)**	**224.7**
Administrative expenses including depreciation and amortisation	(12.0)	(14.5)	(4.8)	(9.0)	(5.1)	(74.2)	(119.6)
Impairment losses on loans and advances to customers	(4.8)	(1.5)	(2.0)	(1.3)	(0.8)	–	(10.4)
Segmental result	**39.3**	**4.5**	**28.2**	**66.0**	**40.1**	**(83.4)**	**94.7**
Tax							(16.4)
Profit after tax							**78.3**
Assets	1,346.7	160.8	829.2	2,417.9	1,390.2	863.7	7,008.5
Liabilities	–	–	–	–	–	(6,474.9)	(6,474.9)
Net assets/(liabilities)	**1,346.7**	**160.8**	**829.2**	**2,417.9**	**1,390.2**	**(5,611.2)**	**533.6**

1 Central Functions administrative expenses of £74.2 million includes costs in relation to the Group's Initial Public Offering of £4.1 million.

5. Interest income

	2016 £m	2015 £m
On financial assets not at fair value through profit or loss:		
On loans and advances to customers	364.0	305.4
On loans and advances to banks	0.7	0.7
On debt securities	12.4	11.1
	377.1	**317.2**
On financial assets at fair value through profit or loss:		
Net interest expense on financial instruments hedging assets	(18.9)	(18.5)
Net interest income on debt securities designated at fair value	–	1.7
	358.2	**300.4**

Included within interest income on loans and advances to customers for the year ended 31 December 2016 is a total of £3.4 million (31 December 2015: £3.2 million) relating to impaired financial advances.

Included within net interest expense on financial instruments hedging assets are fair value losses of £0.3 million (31 December 2015: gains of £2.7 million) on derivatives held in qualifying fair value hedging arrangements, together with losses of £4.4 million (31 December 2015: losses of £6.1 million) 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

	2016 £m	2015 £m
On financial liabilities not at fair value through profit or loss:		
On customers' accounts	109.8	91.6
On amounts due to banks	2.6	2.8
On debt securities in issue	2.3	3.5
On subordinated notes	7.7	6.5
	122.4	**104.4**
On financial liabilities at fair value through profit or loss:		
Net interest income on financial instruments hedging liabilities	(5.6)	(4.5)
Other	2.0	1.6
	118.8	**101.5**

Included within net interest income on financial instruments hedging liabilities are fair value gains of £2.1 million (31 December 2015: losses of £1.8 million) on derivatives held in qualifying fair value hedging arrangements, together with gains of £0.4 million (31 December 2015: gains of £2.3 million) 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

	2016 £m	2015 £m
Invoice Finance fees	11.9	12.6
Valuation fees	7.0	4.1
Documentation fees	2.8	3.2
Other fees	8.3	5.3
	30.0	**25.2**

Note 2(b) Fee and commissions and other operating income provide further details of items included within Other fees.

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8. Fee and commission expense

	2016 £m	2015 £m
Introducer commissions	1.5	1.7
Legal and valuation fees	3.4	2.7
Company searches and other fees	1.3	1.6
Credit protection and insurance charges	1.3	0.8
Other	–	0.2
	7.5	**7.0**

9. Net expense from derivatives and other financial instruments at fair value through profit or loss

	2016 £m	2015 £m
Net (losses)/gains on derivatives	(6.5)	5.0
Net (losses) on assets designated at fair value through profit or loss	–	(0.2)
Net gains/(losses) on available for sale assets held in fair value hedges	2.1	(6.9)
	(4.4)	**(2.1)**

10. Other operating income

	2016 £m	2015 £m
Disbursements, collect out and other invoice finance income	6.2	6.4
Other	–	1.0
	6.2	**7.4**

11. Administrative expenses

	Note	2016 £m	2015 £m
Staff costs	12	64.3	62.1
Legal and professional and other services		21.8	25.8
Information technology costs		10.9	7.3
Office costs		5.0	4.9
Provisions	33	0.8	2.3
Other		11.1	11.9
Impairment of goodwill		4.1	–
		118.0	**114.3**

Included in other administrative expenses are costs relating to temporary staff of £4.4 million (31 December 2015: £5.0 million), travel and subsistence of £3.0 million (31 December 2015: £3.2 million) and staff recruitment of £1.5 million (31 December 2015: £1.6 million).

Administrative expenses of £114.3 million for the year ended 31 December 2015 included £4.1 million of one-off costs associated with the Group's initial public offering.

12. Staff costs

	2016 £m	2015 £m
Wages and salaries	52.7	50.8
Social security costs	6.4	6.3
Other pension costs	1.7	1.6
Share-based payments	3.5	3.4
	64.3	**62.1**

The analysis above includes staff costs in relation to Executive and Non-Executive Directors.

The average number of persons employed by the Group during the year, including Non-Executive Directors, was 887 (31 December 2015: 845).

13. Remuneration of Directors

	2016 £'000	2015 £'000
Directors' emoluments	2,713.0	2,639.4
Payments in respect of personal pension plans	53.7	26.5
Contributions to money purchase scheme	5.3	20.9
Loan forgiveness	–	139.6
Long term incentive schemes	–	7,784.3
	2,772.0	**10,610.7**

The above disclosure is prepared in accordance with Schedule 5 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008.

Loans to Directors

At 31 December 2016, there is one loan to a Director for the value of £40,000 under normal terms of business (31 December 2015: one loan; for the value of £50,000).

Long-term incentive schemes

The Directors held certain shares pre-IPO which converted into ordinary shares on IPO. The reported gains, at IPO, have been calculated as the market value of shares held at IPO (£1.92) less the actual cost on any shares bought pre-IPO regardless of whether such shares were acquired as an investment or an incentive. The aggregate gains as at 31 December 2015 on such shares held by Directors on IPO were £7.8 million.

The Deferred Share Plan is an equity settled share-based payment and represents the portion of the Annual Incentive Plan that is deferred to align the interests of senior employees and the Executive team with shareholders. The shares granted as part of the Deferred Share Plan are detailed in Note 37.

14. 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 £1.7 million (31 December 2015: £1.6 million) were charged to the income statement during the year in respect of these schemes. The Group made payments amounting to £5,300 (31 December 2015: £26,500) in aggregate in respect of Directors' individual personal pension plans during the year. There were outstanding contributions of £0.3 million at the year end (31 December 2015: £0.3 million).

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15. Depreciation and amortisation

	Note	2016 £m	2015 £m
Depreciation	27	1.2	1.1
Amortisation of intangible assets	28	4.1	4.2
		5.3	**5.3**

16. Profit on ordinary activities before taxation

The profit on ordinary activities is after charging:

	2016 £m	2015 £m
Operating lease rentals (including service charges)		
– land and buildings	2.6	2.3
– plant and equipment	0.3	0.5
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)	0.1	0.1
Fees payable to the Group's auditor for the audit of the accounts of subsidiaries (excluding VAT)	0.6	0.4
Audit fees	**0.7**	**0.5**
Fees payable to the Group's auditor and its associates for other services (excluding VAT):		
Audit related assurance services [1]	0.2	0.1
Other taxation advisory services	–	0.2
Corporate finance services	–	0.3
Other assurance services [2]	0.1	0.1
All other services	–	0.1
Non-audit fees	**0.3**	**0.8**
	1.0	**1.3**

1 Audit related assurance services for the year ended 31 December 2016 comprise services provided in relation to interim profit verifications during the year and work in relation to the Group's issuance of subordinated loan notes.

2 Other assurance services for the year ended 31 December 2016 relate to services provided in relation to the audit of the Group's participation in the FLS scheme.

17. Taxation

a) Tax charge

	2016 £m	2015 £m
Current tax on profits for the year	33.1	25.1
(Over)/under provision in previous periods	(2.2)	1.1
Total current tax	**30.9**	**26.2**
Deferred tax	1.9	(5.2)
Under/(over) provision in previous periods	2.4	(0.9)
Effect of new tax surcharge	–	(3.7)
Total deferred tax charge/(credit)	**4.3**	**(9.8)**
Total tax charge	**35.2**	**16.4**

For 2016, the effect of the new banking surcharge is included in the current year tax charge as detailed in Note 26. A tax charge of £1.0 million in respect of the fair value movements in available for sale debt securities has been shown in other comprehensive income during the year ended 31 December 2016 (2015: £0.6 million credit). A tax credit of £2.3 million (31 December 2015: £1.0 million) has been reflected directly in equity in respect of tax relief for contingent convertible securities coupon costs.

b) Factors affecting tax charge 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 20% (31 December 2015: 20.25%). The differences are explained below:

	2016 £m	2015 £m
Profit before tax	**128.7**	**94.7**
Tax at 20% (2015: 20.25%) thereon	25.7	19.2
Effects of:		
Expenses not deductible for tax purposes	1.0	0.7
Under provision in previous period	0.2	0.2
Deferred tax rate adjustment	0.4	(3.7)
Effect of new tax surcharge	7.9	–
	35.2	**16.4**

18. Earnings per share

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

	2016	2015
Profit after taxation – attributable to equity holders of the Group (£ million)	93.5	78.3
Coupon paid on contingent convertible securities, net of tax relief (£ million)	(6.6)	(2.8)
Profit attributable to ordinary shareholders of the Group (£ million)	**86.9**	**75.5**
Weighted average number of ordinary shares in issue (million)	344.5	332.4
Basic earnings per share (p)	**25.2p**	**22.7p**

The ordinary shares in issue used in the denominator in the calculation of basic earnings per share are the ordinary shares of the Company since the share reorganisation that occurred on the Company's admission to the LSE on 13 March 2015. Further details of the share reorganisation are provided in Note 36.

The calculation of diluted earnings per share has been based on the same profit attributable to ordinary shareholders of the Group as for basic earnings and the weighted average number of ordinary shares outstanding after the potential dilutive effect of share-based payment awards to Directors and employees. The share warrants, giving rise to dilution for the first half of 2015, were exercised on 9 September 2015 and new shares were issued and listed on the London Stock Exchange.

	2016	2015
Weighted average number of ordinary shares in issue (million) (basic)	344.5	332.4
Effect of share warrants prior to their exercise	–	2.2
Effect of share-based payment awards	0.7	0.1
Weighted average number of ordinary shares in issue (million) (diluted)	345.2	334.7
Diluted earnings per share (p)	**25.2p**	**22.6p**

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19. Loans and advances to banks

	2016 £m	2015 £m
Included in cash and cash equivalents: balances with less than three months to maturity at inception	34.1	51.6
Cash collateral on derivatives placed with banks	22.2	31.7
Other loans and advances to banks	10.9	10.9
	67.2	**94.2**

There were no individual or collective provisions for impairment held against loans and advances to banks. £10.9 million is recoverable more than 12 months after the reporting date (31 December 2015: £10.9 million) and relates to cash held by the Group's securitisation vehicle, Oak No.1 PLC.

20. Debt securities

	2016 £m	2015 £m
Available for sale debt securities:		
UK Government gilts and treasury bills	32.3	94.4
Supranational bonds	359.8	267.9
Corporate bonds	29.7	29.9
Asset-backed securities	70.4	74.9
Covered bonds	172.3	139.0
	664.5	**606.1**

At 31 December 2016, £534.5 million (31 December 2015: £566.6 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.

The Group disposed of its holding of debt securities designated at fair value through profit or loss during 2015.

21. Derivatives held for risk management

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

	2016		2015	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Instrument type				
Interest rate (not in hedging relationships)	0.4	1.5	0.8	1.4
Interest rate (fair value hedges)	11.8	34.1	5.9	33.9
Equity	0.2	0.2	–	–
Foreign exchange	–	–	–	0.1
	12.4	**35.8**	**6.7**	**35.4**

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

a) Fair value hedges of interest rate risk

The Group uses interest rate swaps within qualifying hedge accounting relationships to manage its exposure to changes in market interest rates which would impact the fair values of certain fixed rate lending and savings products and debt securities held.

Further details regarding the Group's approach to hedge accounting, including a description of the Group's exposure to volatility, are provided in the risk report on page 106.

b) Other derivatives held for risk management

The Group uses other derivatives, not designated in qualifying hedge accounting 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.

22. Loans and advances to customers

	2016 £m	2015 £m
Gross loans and advances	7,504.7	6,165.5
less: allowance for impairment losses	(27.4)	(20.7)
	7,477.3	**6,144.8**

Amounts include:		
Expected to be recovered more than 12 months after the reporting date	6,466.4	5,345.5

At 31 December 2016, loans and advances to customers of £1,066.2 million (31 December 2015: £1,445.5 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 £650.0 million of UK Treasury Bills had been drawn as at the reporting date (31 December 2015: £750.0 million).

At 31 December 2016, loans and advances to customers of £578.7 million (31 December 2015: £nil) were pre-positioned with the Bank of England and HM Treasury Term Funding Scheme. These loans and advances were available for use as collateral with the Scheme. Details of amounts drawn on the facility are shown Note 29.

At 31 December 2016, loans and advances to customers include £148.7 million (31 December 2015: £206.5 million) 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 of funding for the Group. 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

	Individual £m	Collective £m	Total £m
Year ended 31 December 2016			
Balance as at 1 January	10.2	10.5	20.7
Impairment loss for the year:			
Charge to the income statement	10.8	4.7	15.5
Unwind of discounting	(1.3)	(2.1)	(3.4)
Write-offs net of recoveries	(5.4)	–	(5.4)
Balance as at 31 December	**14.3**	**13.1**	**27.4**

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22. Loans and advances to customers continued

Allowance for impairment losses

	Individual £m	Collective £m	Total £m
Year ended 31 December 2015			
Balance as at 1 January	14.0	8.5	22.5
Impairment loss for the year			
Charge to the income statement	6.8	3.6	10.4
Unwind of discounting	(1.6)	(1.6)	(3.2)
Write-offs net of recoveries	(9.0)	–	(9.0)
Balance as at 31 December	**10.2**	**10.5**	**20.7**

Finance lease receivables

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

	2016 £m	2015[1] £m
Gross investment in finance leases, receivable:		
Less than one year	521.5	465.4
Between one and five years	960.3	840.1
More than five years	20.3	20.1
	1,502.1	**1,325.6**
Unearned finance income	(162.4)	(152.7)
Net investment in finance leases	**1,339.7**	**1,172.9**
Net investment in finance leases, receivable:		
Less than one year	448.9	397.3
Between one and five years	871.2	755.8
More than five years	19.6	19.8
	1,339.7	**1,172.9**

[1] The prior year comparatives have been restated to reflect a more granular analysis of the finance lease portfolio.

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 uncollectable minimum lease payments receivable is £4.5 million (31 December 2015: £3.9 million).

Due to the nature of the business undertaken, there are no material unguaranteed residual values for any of the finance leases at 31 December 2016.

23. Investment in subsidiaries

The Company has an interest in the total ordinary share capital of the following subsidiaries (except the securitisation vehicles), all of which are registered in England and Wales and operate in the UK. All subsidiary undertakings are included in these consolidated financial statements.

Subsidiary undertakings (direct interest)	Principal activity	Shareholding per cent	Country of incorporation
Aldermore Bank PLC	Banking and related services	100	UK
Dormant subsidiary undertakings (indirect interest)			
Aldermore Invoice Finance (Holdings) Limited	Dormant	100	UK
Aldermore Invoice Finance Limited	Dormant	100	UK
Aldermore Invoice Finance (Oxford) Limited	Dormant	100	UK
AR Audit Services Limited	Dormant	100	UK
Securitisation vehicles			
Oak No.1 Mortgage Holdings Limited	Holding company for securitisation vehicle	*	UK
Oak No.1 PLC	Securitisation vehicle	*	UK

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

24. Other assets

	2016 £m	2015 £m
Amounts recoverable within one year	**3.1**	**1.4**

25. Prepayments and accrued income

	2016 £m	2015 £m
Amounts recoverable within 12 months:		
Prepayments	2.6	3.2
Accrued income	0.8	1.9
	3.4	**5.1**

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26. 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:

	Balance at start of the year £m	Recognised in income statement £m	Recognised in other comprehensive income £m	Recognised in equity £m	Balance at end of the year £m
Year ended 31 December 2016					
Capital allowances less than depreciation	16.5	(5.2)	–	–	11.3
Available for sale debt securities transition adjustment	(0.2)	–	–	–	(0.2)
(Gains)/Losses on available for sale debt securities recognised through other comprehensive income	–	–	(1.0)	–	(1.0)
Other temporary differences	(0.4)	(0.4)	–	–	(0.8)
Share-based payment timing differences	0.5	1.3	–	0.1	1.9
	16.4	**(4.3)**	**(1.0)**	**0.1**	**11.2**
Year ended 31 December 2015					
Capital allowances less than depreciation	6.5	10.0	–	–	16.5
Available for sale debt securities transition adjustment	(0.3)	0.1	–	–	(0.2)
Other temporary differences	0.4	(0.8)	–	–	(0.4)
Share-based payment timing differences	–	0.5	–	–	0.5
	6.6	**9.8**	**–**	**–**	**16.4**

Reductions have been enacted in the mainstream UK corporation tax rate from 21% to 20% (effective from 1 April 2015). Further planned reductions have been enacted to reduce the mainstream rate to 19% with effect from 1 April 2017 and to 17% with effect from 1 April 2020. The 8% corporation tax banking surcharge applicable to banking companies is effective from 1 January 2016. The surcharge is levied on the profits chargeable to corporation tax of banking companies which exceed a £25 million threshold. The net result of these changes will be to increase the Group's effective tax rate for years commencing from 1 January 2016.

Deferred tax has been provided at the revised substantively enacted rates that will apply when the deferred tax assets are realised or the deferred tax liabilities settled in line with the prior year.

There were no unrecognised deferred tax balances at 31 December 2016 (31 December 2015: £nil).

27. Property, plant and equipment

	Fixtures, fittings and equipment £m	Computer hardware £m	Total £m
Cost			
1 January 2016	3.9	4.4	8.3
Additions	0.7	0.2	0.9
31 December 2016	**4.6**	**4.6**	**9.2**
1 January 2015	3.2	3.4	6.6
Additions	0.7	1.0	1.7
31 December 2015	**3.9**	**4.4**	**8.3**
Depreciation			
1 January 2016	2.3	2.6	4.9
Charge for the year	0.5	0.7	1.2
31 December 2016	**2.8**	**3.3**	**6.1**
1 January 2015	1.8	2.0	3.8
Charge for the year	0.5	0.6	1.1
31 December 2015	**2.3**	**2.6**	**4.9**
Net book value			
31 December 2016	**1.8**	**1.3**	**3.1**
31 December 2015	1.6	1.8	3.4

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28. Intangible assets

	Computer Systems £m	Goodwill £m	Total £m
Cost			
1 January 2016	24.8	12.6	37.4
Additions	10.3	–	10.3
Write-off	–	(4.1)	(4.1)
31 December 2016	**35.1**	**8.5**	**43.6**
1 January 2015	19.2	12.6	31.8
Additions	5.6	–	5.6
31 December 2015	**24.8**	**12.6**	**37.4**
Amortisation			
1 January 2016	13.4	–	13.4
Charge for the year	4.1	–	4.1
31 December 2016	**17.5**	**–**	**17.5**
1 January 2015	9.2	–	9.2
Charge for the year	4.2	–	4.2
31 December 2015	**13.4**	**–**	**13.4**
Net book value			
31 December 2016	**17.6**	**8.5**	**26.1**
31 December 2015	11.4	12.6	24.0

Goodwill arose on the acquisitions of Ruffler Holdings Limited (subsequently renamed Aldermore Holdings Limited), 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 segments with the aggregate amount allocated to each segment as follows:

	2016 £m	2015 £m
SME Commercial Mortgages	8.5	8.5
Invoice Finance	–	4.1
	8.5	**12.6**

At 1 January 2016, the Invoice Finance goodwill was fully supported using the Fair Value less Costs of Disposal ("FVLCD") method. During 2016, as a result of the general fall in market values of financial services businesses following the EU referendum, management concluded the goodwill balance was fully impaired and a charge of £4.1 million has been recognised in the income statement.

The Value in Use ("VIU") for SME Commercial Mortgages was determined by discounting the future cash flows to be generated from the continuing use of the segment. VIU at 31 December 2016 has been determined in a similar manner as at 31 December 2015.

Key assumptions used in the calculation of VIU were the following:

- Cash flows were projected based on past experience, actual operating results and the five year business plan (31 December 2015: the five year business plan). Cash flows after the planning period were extrapolated using a constant growth rate of 2 per cent (31 December 2015: 2 per cent) into perpetuity.
- A pre-tax discount rate of 13.0 per cent (31 December 2015: 13.0 per cent) was applied in determining the recoverable amounts for the SME Commercial Mortgages operating segment. These discount rates were based on the weighted average cost of funding for the segment, taking into account the Group's regulatory capital requirement and expected market returns for debt and equity funding, then adjusted for risk premiums to reflect the systemic risk of the segment.

IAS 36 requires an assessment of goodwill balances for impairment on an annual basis, or more frequently if there is an indication of impairment. An impairment charge should be recognised where the recoverable amount from the segment is less than the carrying value of the goodwill. Under IAS 36, the recoverable amount is the greater of either the VIU of a business or its Fair Value less Costs of Disposal ("FVLCD").

The VIU of the SME Commercial Mortgages segment is significantly above the carrying value of the attributable goodwill and net assets. The Group estimates that reasonably possible changes in the above assumptions are not expected to cause the recoverable amount of SME Commercial Mortgages to reduce below the carrying amount.

29. Amounts due to banks

	2016 £m	2015 £m
Amounts repayable within 12 months:		
Due to banks – repurchase agreements	354.8	398.6
Due to banks – deposits	0.7	5.2
Cash collateral received on derivatives	2.2	1.3
	357.7	**405.1**
Amounts repayable after 12 months:		
Due to banks – central banks – Term Funding Scheme	396.1	–
	753.8	**405.1**

(a) Collateral given under repurchase agreements

The face value of securities sold under agreements to repurchase at 31 December 2016 was £355.0 million (31 December 2015: £400.0 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.

(b) Amounts repayable after 12 months

Loans received from the Bank of England against which the Group provides collateral under the Term Funding Scheme are recorded as 'Amounts due to banks' and are accounted for as a financial liability at amortised cost.

Further details of a) and b) can be found in Note 22.

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30. Customers' accounts

	2016 £m	2015 £m
Retail deposits	4,766.8	4,186.3
SME deposits	1,647.2	1,399.4
Corporate deposits	259.7	156.3
	6,673.7	**5,742.0**
Amounts repayable within one year	5,397.1	4,288.8
Amounts repayable after one year	1,276.6	1,453.2
	6,673.7	**5,742.0**

31. Other liabilities

	2016 £m	2015 £m
Amounts payable within 12 months:		
Amounts payable to Invoice Finance customers	10.5	9.4
Other taxation and social security costs	4.1	4.3
Trade creditors	3.3	3.2
Other payables	7.1	5.0
	25.0	**21.9**

32. Accruals and deferred income

	2016 £m	2015 £m
Amounts payable within 12 months:		
Accruals	26.4	24.0
Deferred income	0.6	1.7
	27.0	**25.7**

33. Provisions

	Financial Services Compensation Scheme £m	Customer redress £m	Total £m
1 January 2016	1.1	–	1.1
Utilised during the year	(1.1)	–	(1.1)
Provided during the year	0.8	–	0.8
31 December 2016	**0.8**	**–**	**0.8**
1 January 2015	1.2	0.8	2.0
Utilised during the year	(2.3)	(0.9)	(3.2)
Provided during the year	2.2	0.1	2.3
31 December 2015	**1.1**	**–**	**1.1**

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. 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.

The FSCS provision at 31 December 2016 of £0.8 million (31 December 2015: £1.1 million) represents the interest element of the compensation levy for the 2016/2017 scheme year (31 December 2015: interest levy for the 2015/2016 scheme year).

Customer redress

The Group has a small number of loans which are regulated under the Consumer Credit Act ("CCA") and had identified that, following changes to the CCA in 2008, certain letters and statements were sent to customers that did not fully comply with the requirements prescribed by the CCA. Accordingly, these customers were 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. Remediation payments to customers impacted were completed during the year ended 31 December 2015.

34. Debt securities in issue

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

	2016 £m	2015 £m
In more than one year	**130.6**	**193.9**

Debt securities in issue with a principal value of £131.2 million (31 December 2015: £194.8 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 22.

35. Subordinated notes

	2016 £m	2015 £m
Subordinated notes	**100.0**	**38.1**

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 after five years. The interest rate is fixed until May 2017. The loan notes were issued at a discount and are carried in the statement of financial position at amortised cost using an 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 warrants were valued at £2.2 million, and this was treated as a warrant reserve within equity in accordance with the accounting policy in Note 2(f). On 9 September 2015, the warrants were exercised resulting in 5.5 million ordinary £0.10 shares being issued (see Note 36).

On 28 October 2016, the Group issued £60 million subordinated 8.50 per cent loan notes, repayable in 2026, with an option for the Group to redeem after five years. The interest rate is fixed until October 2021. The loan is carried in the statement of financial position at amortised cost using an EIR of 8.9 per cent.

36. Share capital

	2016 £m	2015 £m
Type		
Ordinary shares of £0.10 each	34.5	34.5
	34.5	**34.5**

On 13 March 2015, the Company reorganised its share capital in preparation for listing on the LSE. Following the reorganisation, 117,934,783 ordinary shares of £0.10 each were issued in the IPO at a price of £1.92 per share. Of the 117,934,783 shares in the offer, 78,872,283 were sold by existing shareholders, with the remaining 39,062,500 being issued by the Company, resulting in an increase in share capital of £3,906,250 and share premium account of £71,093,750 (excluding costs).

Ordinary shares have full voting rights, dividend rights and distribution rights in the event of sale or wind up.

Following the listing, the Company made an award of free share awards under the Share Incentive Plan ("SIP"). Further details regarding the SIP are provided in Note 37. Of that original award 734 shares remain unallocated and are held in the SIP Trust, and are recorded against retained earnings within equity. The SIP Trustee waives any dividends that may be declared in respect of unallocated shares.

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36. Share capital continued

On 9 September 2015, the share warrants attached to the subordinated notes (see Note 2(f)) were exercised resulting in the following share issue:

Number of warrant shares exercised	Share capital £'000	Share premium £'000	Total £'000
5,502,164	550.2	4,970.3	5,520.5

During June 2016, an Employee Benefit Trust ("EBT") purchased 466,179 Aldermore Group PLC ordinary £0.10 shares from the market for consideration of £0.9 million. Purchases were made to enable the Group to meet a future share-based payment obligation in respect of the recruitment award detailed in Note 37. These purchases constitute Aldermore Group PLC shares held by a Group EBT and are recorded against retained earnings within equity. The EBT waives any dividends that may be declared in respect of such shares prior to their release to the participant.

At 31 December 2016, there were 344,739,584 ordinary £0.10 shares in issue resulting in share capital of £34,473,958 (31 December 2015: 344,739,584 and £34,473,958 respectively).

37. Share-based payments

The table below shows the charge to the income statement:

	2016 £m	2015 £m
Share plans issued in 2015	2.0	2.2
Share plans issued in 2016	1.5	–
Total share-based payment charge	**3.5**	**2.2**

Included within the 2015 charge disclosed in Note 12 was £1.2 million in relation to the Deferred Share Plan which was granted, as expected, during 2016.

Scheme details:

Plan	Eligible employees	Nature of award	Vesting conditions[1]	Grant dates[2]
a) Performance Share Plan	Selected senior employees	Conditional share award	Continuing employment or leaving in certain limited circumstances and achievement of Total Shareholder Return and Earnings Per Share performance conditions	2015 & 2016
b) Pre-IPO Award under the Performance Share Plan	Selected senior employees	Conditional share award	Continuing employment or leaving in certain limited circumstances and achievement of Total Shareholder Return performance condition.	2015
c) "Top Up" Pre-IPO Award under the Performance Share Plan	Selected senior employees	Conditional share award	Continuing employment or leaving in certain limited circumstances and achievement of personal and Company performance conditions	2015
d) Restricted Share Plan	Selected senior employees	Conditional share award	Continuing employment or leaving in certain limited circumstances	2015 & 2016
e) Recruitment Award	Selected senior employees	Conditional share award	Continuing employment or leaving in certain limited circumstances	2016
f) Share Incentive Plan	All employees	Non-conditional share award	Employment at date of grant	2015
g) Sharesave Plan	All employees	Qualifying SAYE plan with an option to purchase shares at the end of the saving period	Monthly contributions to the scheme and continuing employment or leavers in certain limited circumstances	2015 & 2016
h) Deferred Share Plan	Selected senior employees	Deferred conditional share award	Continuing employment or leavers in certain limited circumstances	2016[3]

1 All awards are subject to vesting conditions and therefore may or may not vest.

2 Year in which grants have been made under the relevant Plan. Further grants in future years under the Plan are possible.

3 Grants under the Deferred Share Plan are made the year following the financial year to which they relate.

The terms of the schemes are as follows:

a) Performance Share Plan

The Performance Share Plan ("PSP") is open to senior employees including the Executive team. There are currently awards outstanding for two plan years as per the table above. Individuals are required to remain in employment for three years following the grant date and the awards are subject to a two-year holding period following the required employment date.

Awards under the PSP are subject to performance conditions which are set by the Remuneration Committee and determine the extent to which awards can become available to individuals. Performance conditions for the PSP awards relate to the growth in Total Shareholder Return ("TSR") for 50% of each award and Earnings Per Share ("EPS") performance for the remaining 50% of each award. The outcome of the performance conditions, as assessed by the Remuneration Committee, will determine the vesting outcome of the awards and the shares available for exercise.

In addition, there are "*underpin*" performance conditions which must be met in relation to both elements of the award and the result achieved must both appropriately reflect the performance of the Company and be consistent with the Company's risk appetite. Furthermore, in respect of the TSR element of the grant made in 2015, the value of the TSR achieved over the performance period must be equal to or greater than the TSR of the median company of FTSE 350 companies, excluding Investment Trusts and the Company itself.

b) Pre-IPO Award under the Performance Share Plan

Pre-IPO Awards in respect of 6,920,420 shares, which were granted on 2 March 2015 to individuals as a one-off reward to recognise their contribution up to the Company's IPO, have lapsed as the principal performance condition relating to growth in TSR for the period to 31 December 2016 was not satisfied.

c) "Top Up" Pre-IPO awards under the Performance Share Plan

For the small number of employees who had been granted a "Top Up" Pre-IPO Award at the time of IPO which was intended to promote their retention and to reward them for their performance both pre-IPO and post-IPO, the Remuneration Committee amended the "Top Up" portion of those awards over 513,589 shares such that:

- The principal performance condition was a personal performance condition, as well as an underpin whereby the Remuneration Committee would determine that the performance of the Company justified the vesting. The Remuneration Committee determined that the amended performance condition and underpin had been met as at 31 December 2016.
- The awards normally become exercisable on 31 December 2018 and are contingent on employment to this date, with a leaver receiving a pro-rated proportion of the shares (for the period 31 December 2016 to 31 December 2018) except if the individual ceases employment because of misconduct in which case the whole award would lapse.

The total incremental fair value arising from the modification of the awards is £1,188,000 of which £16,000 has been reflected in the 2016 income statement charge. The fair value of the awards has been determined using the market price of Aldermore Group PLC shares as at 22 December 2016.

d) Restricted Share Plan

The Restricted Share Plan ("RSP") is open to a small number of senior employees engaged in risk and control functions. There is a requirement for individuals to remain in employment for three years following the grant date, following which the awards are subject to a two-year holding period. There are no financial performance conditions attached to the awards under the RSP.

e) Recruitment Award

The Recruitment Award was granted for the purpose of buying out awards forfeited by senior employees on resignation from their previous employment. There are no performance conditions attached to this award. The award will be released in tranches with twenty per cent vesting on each of the first, second and third anniversaries of the grant date and forty per cent on the fourth anniversary of the award, subject to continued employment.

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37. Share-based payments continued

f) Share Incentive Plan

All employees who were in employment on both 13 March 2015 and the grant date were eligible to participate in the Share Incentive Plan ("SIP"). An award of 'free shares' was granted under the SIP on 17 April 2015. Each eligible employee received shares worth £200, with an additional £200 for each year of service up to a maximum award of £1,000. There are no performance conditions associated with the share awards. Participants in the SIP are the beneficial owners of the shares granted to them, but not the registered owner. Voting rights are normally exercised by the registered owner at the direction of the participant.

g) Sharesave Plan

All employees are eligible to participate in the Group's annual invitation to join the Sharesave Plan. The grant dates of the awards are shown in the table above, with individuals in the Plan contributing a set amount each month for three years. At the end of the savings period, participants have the option to buy shares in Aldermore Group PLC at an option price which was fixed at the grant date.

There are no financial performance conditions attached to the awards but employees may only continue to participate in the Plan whilst in the employment of the Group, and subject to having made all monthly contributions. Participants have the option, but not the obligation, to buy shares at the end of the plan. There are no holding conditions in respect of shares acquired pursuant to the exercise of an option.

h) Deferred Share Plan

The Deferred Share Plan ("DSP") is open to senior employees, including the Executive team, and represents the portion of awards under the Annual Incentive Plan that is deferred to align the interests of senior employees and the Executive team with shareholders. The awards typically vest in tranches of one-third on the first, second and third anniversary of the award date, subject to continued employment. There are no market performance conditions attached to the awards made under the DSP. Share awards, representing the deferred element of the 2015 bonus payments, with a grant date fair value of £1.2 million, were granted in March 2016.

There is an anticipation that share awards for the deferred element of the 2016 bonuses, with a grant date fair value of £1.6 million, will be made in 2017.

Awards/options granted, forfeited and vested

The table below shows the changes to the options awarded during the period and the number of awards outstanding as at 31 December 2016:

Plan	Awards outstanding at 1 January 2016	Awards / options granted	Awards / options forfeited	Awards / options expired	Awards / options vested	Awards outstanding at 31 December 2016 Number	Average fair value per award granted during the year at grant date (rounded)	Total fair value to be recognised over the vesting period £m
Performance Share Plan	1,406,231	1,526,448	(292,742)	–	–	2,639,937	£1.46	3.9
Pre-IPO award under the PSP[1]	6,920,420	–	(134,274)	(6,786,146)	–	–	£0.31	–
"Top Up" Pre IPO Award under the PSP	513,589	–	–	–	–	513,589	£2.31	1.2
Restricted Share Plan	105,753	175,875	(24,635)	–	–	256,993	£2.09	0.5
Recruitment Award	–	466,179	–	–	–	466,179	£1.91	0.9
Sharesave Plan	794,966	1,379,516	(624,011)	–	–	1,550,471	£0.73	1.1
Deferred Share Plan	–	543,837	(1,850)	–	–	541,987	£2.28	1.2
Total	**9,740,959**	**4,091,855**	**(1,077,512)**	**(6,786,146)**	**–**	**5,969,156**	**–**	**8.8**

1 Average fair value includes incremental value attributable to modification for each award outstanding.

Plan	Awards / options granted	Awards / options forfeited	Awards / options expired	Awards / options vested	Awards outstanding at 31 December 2015 Number	Average fair value per award granted during the year at grant date (rounded)	Total fair value to be recognised over the vesting period £m
Performance Share Plan	1,539,629	(133,398)	–	–	1,406,231	£1.13	1.6
Pre-IPO award under the PSP	7,549,101	(115,092)	–	–	7,434,009	£0.31	2.3
Restricted Share Plan	105,753	–	–	–	105,753	£1.92	0.2
Share Incentive Plan	174,920	–	–	(174,920)	–	£2.41	0.4
Sharesave Plan	794,966	–	–	–	794,966	£0.79	0.6
Total	**10,164,369**	**(248,490)**	**–**	**(174,920)**	**9,740,959**	**–**	**5.1**

Determination of grant date fair values

Share awards are not entitled to dividends until the awards vest, but the number of shares subject to vested PSP, RSP and DSP awards may be increased to reflect the value of dividends that would have been paid up to the end of the holding period for the awards. This is designed to deliver a benefit similar to that which ordinary shareholders may receive in respect of any dividends paid during the vesting period. Accordingly, the grant date fair value of the awards with no performance conditions other than service conditions has been taken as the market value of the Company's ordinary shares at the grant date.

In respect of awards for which there are non-market performance conditions (e.g. EPS), the grant date fair value per award has been taken as the market value of an ordinary share at the grant date. A forecast is made of the number of awards expected to vest in order to determine the overall share-based payment charge to be recognised over the vesting period. In respect of awards for which there are market performance conditions (e.g. TSR), the grant date fair value of each award is required to reflect the likelihood of achieving the market conditions within the valuation.

For the awards concerned, the grant date fair values for each award were determined using stochastic simulation models with the following significant inputs:

	PSP
Ordinary share price	£2.29
Risk-free rate	0.50% p.a.
Probability distributions of TSRs for Aldermore and the median FTSE 350 (excluding Investment Trust companies)	Log normal
Annual volatility (of logarithm of TSR) for Aldermore share price (based on recently floated banks)	40%[1]
Annual volatility (of logarithm of TSR) for median of FTSE 350 (excluding Investment Trust companies) (based on five years data)	29%
Correlation between volatilities	None

1 Based on Aldermore Group PLC share price volatility annualised, from date of listing (13 March 2015) to the grant date (21 March 2016).

Share options (Sharesave Plan)

Options granted under the Sharesave Plan have no entitlement to dividends until they are exercised. The grant date fair value of the options were determined using a Black Scholes valuation model with the following significant inputs:

	Sharesave plan
Share price at grant date	£1.74
Exercise price	£1.54
Risk-free rate	0.19% p.a.
Expected volatility of Company share price	54%[1]
Expected life	3.14 years

1 Based on Aldermore Group PLC share price volatility annualised, from the date of listing (13 March 2015) to the grant date (12 October 2016).

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38. Contingent convertible securities

	2016 £m	2015 £m
Contingent convertible securities	**74.0**	**74.0**

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 and the associated tax credit, totalled £74.0 million.

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 per annum 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 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, net of tax relief thereon. Any interest paid on the Securities, net of tax relief thereon, is a distribution to holders of equity instruments and has been 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.

39. Statement of cash flows

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

	2016 £m	2015 £m
Depreciation and amortisation	5.3	5.3
Impairment of goodwill	4.1	–
Amortisation of securitisation issuance cost	0.4	0.5
Discount accretion on subordinated notes	1.6	1.4
Impairment losses on loans and advances	15.5	10.4
Unwind of discounting	(3.4)	(3.2)
Write-offs net of recoveries	(5.4)	(9.0)
Net losses on debt securities designated at fair value through profit or loss	–	0.2
(Gains)/losses on hedged available for sale debt securities recognised in profit or loss	(2.1)	6.9
Net gains on disposal of available for sale debt securities	(3.8)	(2.1)
Interest expense on subordinated notes	6.1	5.1
Interest income on debt securities	(12.4)	(12.8)
Interest expense on debt securities in issue	1.9	3.0
Equity settled share-based payment charge	3.5	3.4
	11.3	**9.1**

(b) Increase in operating assets

	2016 £m	2015 £m
Loans and advances to customers	(1,339.2)	(1,341.9)
Loans and advances to banks	9.5	14.4
Derivative financial instruments	(5.7)	1.5
Fair value adjustments for portfolio hedged risk	4.6	6.1
Other operating assets	(2.0)	2.0
	(1,332.8)	**(1,317.9)**

(c) Increase in operating liabilities

	2016 £m	2015 £m
Amounts due to banks	348.7	99.2
Customers' accounts	931.7	1,283.0
Derivative financial instruments	0.4	(18.8)
Fair value adjustments for portfolio hedged risk	(0.4)	(2.3)
Other operating liabilities	4.1	7.0
	1,284.5	**1,368.1**

(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.

	2016 £m	2015 £m
Cash and balances at central banks	116.4	105.3
Less restricted balances	(9.6)	(7.5)
Loans and advances to banks	34.1	51.6
	140.9	**149.4**

Restricted 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. Loans and advances to banks as at 31 December 2016 include £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 2015: £10.9 million).

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40. Commitments and contingencies

At 31 December 2016, the Group had undrawn commitments to lend of £968.8 million (31 December 2015: £556.0 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:

	2016 £m	2015 £m
Land and buildings		
In less than one year	1.9	1.9
Between one and five years	5.4	6.0
More than five years	1.6	2.4
	8.9	**10.3**

	2016 £m	2015 £m
Equipment		
In less than one year	0.2	0.4
Between one and five years	–	0.2
	0.2	**0.6**

At 31 December 2016, the majority of operating leases for equipment related to 64 cars that the Group held under lease (31 December 2015: 70). 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 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.

41. Related parties

(a) Controlling parties

Prior to IPO, the Group was 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 were the sole voting shareholders of Aldermore Group PLC.

On 13 March 2015, the Company was admitted to the LSE, offering 117,934,783 Ordinary shares, of which 78,872,283 shares were sold by the Selling shareholders. Upon admission, AnaCap Financial Partners L.P., AnaCap Financial Partners II L.P., AnaCap Derby Co-Investment (No.1.) L.P. and AnaCap Derby Co-Investment (No.2.) (collectively "the Principal Shareholders") and the Company entered into the 'Relationship agreement'. Details of the Relationship agreement were provided within the Prospectus issued prior to the admission to the LSE.

On 15 September 2015, the Principal Shareholders sold 40,885,613 Ordinary £0.10 shares on the open market.

At 31 December 2016, AnaCap Financial Partners L.P., AnaCap Financial Partners II L.P., AnaCap Derby Co-Investment (No.1.) L.P. and AnaCap Derby Co-Investment (No.2.) L.P held 8.33 per cent, 11.01 per cent, 11.26 per cent and 9.54 per cent of the Company's ordinary share capital respectively. Although the Principal Shareholders are no longer a controlling party for the Group they continue to have significant influence and are therefore considered to be a related party.

The Group had agreements in place with Syscap Limited which was previously under the control of Anacap Financial Partners II L.P and Anacap Financial Partners, L.P. Syscap Limited ceased to be a related party when Anacap sold their interest on 20 February 2015. Details of the previous agreements in place are listed in the Aldermore Group PLC 2015 report and accounts.

During 2016, the Group also incurred fees of £0.1 million in relation to the Directors who represent the Principal Shareholders (2015: £0.1 million).

b) Key management personnel

Key Management Personnel ("KMP") comprise Directors of the Group and members of the Executive Committee. Details of the compensation paid (in accordance with IAS 24) to KMP are:

	2016 £'000	2015 £'000
Emoluments	5,207.8	5,035.8
Payments in respect of personal pension plans	104.4	45.9
Contributions to money purchase scheme	37.3	71.3
Loan forgiveness	–	162.3
Termination benefits	1,161.9	–
Share-based payments	2,439.1	1,196.5
	8,950.5	**6,511.8**

The Group made payments of £37,300 in aggregate in respect of seven key persons' personal pension plans during the year ended 31 December 2016 (31 December 2015: £45,900, four key persons).

Key persons' emoluments includes £1.0 million of deferred bonus (31 December 2015: £0.8 million).

Share-based payments ("SBP")

As at 1 January 2015, certain KMP held a number of shares in the B, C and E classes. In preparation for the IPO, the rights to these shares were varied and the holdings re-designated.

A number of KMP were awarded shares in the Company under new share incentive plans created upon IPO. In total, KMP were granted awards over 1,822,022 shares. Further details of the share schemes, including performance conditions are provided in Note 37. In addition, a number of KMP participated in the Sharesave Plan, holding options over a total of 88,828 shares at 31 December 2016.

Transactions with KMP

The aggregate value of transactions and outstanding balances related to KMP (as defined by IAS 24: "Related Party Disclosures") were as follows:

	2016 £'000	2015 £'000
Deposits		
At 1 January	2,019.2	1,565.0
Net movement	(1,053.7)	454.2
At 31 December	**965.5**	**2,019.2**

The table above includes transactions and balances relating to KMP in post at the end of the year.

From 1 January 2015 until admission to the LSE, a number of KMP had loans with the Company. Upon admission, the Company forgave loans totalling £0.2 million. A number of KMP continue to have loans and deposits in the ordinary course of business with the Group.

At 31 December 2016, there is one loan with KMP for the value of £40,000 (31 December 2015: two loans, £126,000). All current transactions, loans and deposits, with KMP are conducted through the ordinary course of business with the Group.

During 2015 and up to admission, interest rates charged on loan balances outstanding from related parties were lower than the rates that would be charged in arm's length transactions. Interest was charged on these loans at an annual rate of 0.8 per cent above one month LIBOR.

All deposit arrangements have been operated by the Group on commercial terms and conditions.

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42. Financial instruments and fair values

The following table summarises the classification and carrying amounts of the Group's financial assets and liabilities:

31 December 2016	Loans and receivables £m	Available for sale £m	Fair value through profit or loss (required) £m	Fair value hedges £m	Liabilities at amortised cost £m	Total £m
Cash and balances at central banks	116.4	–	–	–	–	116.4
Loans and advances to banks	67.2	–	–	–	–	67.2
Debt securities	–	664.5	–	–	–	664.5
Derivatives held for risk management	–	–	12.4	–	–	12.4
Loans and advances to customers	7,477.3	–	–	–	–	7,477.3
Fair value adjustment for portfolio hedged risk	–	–	–	(3.5)	–	(3.5)
Other assets	2.9	–	–	–	–	2.9
Total financial assets	**7,663.8**	**664.5**	**12.4**	**(3.5)**	**–**	**8,337.2**
Non-financial assets						44.0
Total assets						**8,381.2**
Amounts due to banks	–	–	–	–	753.8	753.8
Customers' accounts	–	–	–	–	6,673.7	6,673.7
Derivatives held for risk management	–	–	35.8	–	–	35.8
Fair value adjustment for portfolio hedged risk	–	–	–	(1.2)	–	(1.2)
Other liabilities	–	–	–	–	20.9	20.9
Debt securities in issue	–	–	–	–	130.6	130.6
Subordinated notes					100.0	100.0
Total financial liabilities	**–**	**–**	**35.8**	**(1.2)**	**7,679.0**	**7,713.6**
Non-financial liabilities						41.6
Total liabilities						**7,755.2**

31 December 2015	Loans and receivables £m	Available for sale £m	Fair value through profit or loss (required) £m	Fair value hedges £m	Liabilities at amortised cost £m	Total £m
Cash and balances at central banks	105.3	–	–	–	–	105.3
Loans and advances to banks	94.2	–	–	–	–	94.2
Debt securities	–	606.1	–	–	–	606.1
Derivatives held for risk management	–	–	6.7	–	–	6.7
Loans and advances to customers	6,144.8	–	–	–	–	6,144.8
Fair value adjustment for portfolio hedged risk	–	–	–	1.1	–	1.1
Other assets	0.4	–	–	–	–	0.4
Total financial assets	**6,344.7**	**606.1**	**6.7**	**1.1**	**–**	**6,958.6**
Non-financial assets						49.9
Total assets						**7,008.5**
Amounts due to banks	–	–	–	–	405.1	405.1
Customers' accounts	–	–	–	–	5,742.0	5,742.0
Derivatives held for risk management	–	–	35.4	–	–	35.4
Fair value adjustment for portfolio hedged risk	–	–	–	(0.8)	–	(0.8)
Other liabilities	–	–	–	–	17.6	17.6
Debt securities in issue	–	–	–	–	193.9	193.9
Subordinated notes	–	–	–	–	38.1	38.1
Total financial liabilities	**–**	**–**	**35.4**	**(0.8)**	**6,396.7**	**6,431.3**
Non-financial liabilities						43.6
Total liabilities						**6,474.9**

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. The fair values in this note are stated at a specific date and may be significantly different from the amounts which will actually be paid on the maturity or settlement dates of the instruments. As a wide range of valuation techniques are available, it may be inappropriate to compare this fair value information to that of independent market or other financial institutions.

	2016		2015	
	Carrying value £m	**Fair value £m**	Carrying value £m	Fair value £m
Cash and balances at central banks	116.4	116.4	105.3	105.3
Loans and advances to banks	67.2	67.2	94.2	94.2
Loans and advances to customers	7,477.3	7,613.0	6,144.8	6,194.1
Other assets	2.9	2.9	0.4	0.4
Total financial assets	**7,663.8**	**7,799.5**	**6,344.7**	**6,394.0**
Amounts due to banks	753.8	753.8	405.1	405.1
Customers' accounts	6,673.7	6,705.9	5,742.0	5,752.8
Other liabilities	20.9	20.9	17.6	17.6
Debt securities in issue	130.6	131.9	193.9	194.8
Subordinated notes	100.0	101.8	38.1	48.0
Total financial liabilities	**7,679.0**	**7,714.3**	**6,396.7**	**6,418.3**

Key considerations in the calculation of the disclosed fair values for those financial assets and liabilities carried at amortised cost include the following:

(a) 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.

(b) 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.

(c) 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 products 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 changes in future credit risk, since loans were granted. However, incurred loss provisions are deducted from the fair value amounts.

(d) 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.

(e) 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 and Term Funding Schemes. 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 not considered to be materially different from their fair value.

Financial statements

Notes to the consolidated financial statements continued

42. Financial instruments and fair value continued

(f) Customers' accounts

The fair value of fixed rate customers' accounts have been determined by discounting estimated future cash flows based on rates currently offered by the Group for 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.

(g) Debt securities in issue

As the 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, see below.

(h) 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 2012 subordinated notes, which have been separately accounted for as a capital contribution within equity on issue. The warrants attached to the subordinated notes were exercised during September 2015 (see note 36).

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 2016	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
Financial assets:				
Derivatives held for risk management	–	12.4	–	12.4
Debt securities:				
Asset-backed securities	–	70.4	–	70.4
UK Gilts and Supranational bonds	392.1	–	–	392.1
Corporate bonds	29.7	–	–	29.7
Covered bonds	172.3	–	–	172.3
	594.1	**82.8**	**–**	**676.9**
Financial liabilities:				
Derivatives held for risk management	–	35.8	–	35.8
	–	**35.8**	**–**	**35.8**

31 December 2015	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets:				
Derivatives held for risk management	–	6.7	–	6.7
Debt securities:				
Asset-backed securities	–	74.9	–	74.9
UK Gilts and Supranational bonds	362.3	–	–	362.3
Corporate bonds	29.9	–	–	29.9
Covered bonds	139.0	–	–	139.0
	531.2	**81.6**	**–**	**612.8**
Financial liabilities:				
Derivatives held for risk management	–	35.4	–	35.4
	–	**35.4**	**–**	**35.4**

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.

The fair values of UK Gilts, Supranational bonds, Corporate bonds and Covered bonds are based on quoted bid prices in active markets.

The fair value of asset-backed securities are based on indicative prices provided by market counterparties, but before relying on these prices, the Group has obtained an understanding of how the prices were derived 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 methods for financial instruments such as interest rate swaps and use only observable market data that require little management judgement and estimation. Credit value and debit 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 sale of the beneficial ownership of the loans and advances to customers to the securitisation vehicle by the Bank fail the derecognition criteria, and consequently, these loans remain on the statement of financial position of the Group. The Bank, therefore, recognises a deemed loan financial liability on its statement of financial position and an equivalent deemed loan asset is held on the securitisation vehicle's statement of financial position. As the securitisation vehicle is consolidated into the Group with the Bank, the deemed loans net out in the consolidated accounts. 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.

Financial statements

Notes to the consolidated financial statements continued

42. Financial instruments and fair value continued

The results of the securitisation vehicle listed in Note 23 are 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 are the carrying amounts recorded in the Group accounts. Some of the notes issued by the securitisation vehicle are held by the Group and as such are not shown in the consolidated statement of financial position of the Group.

31 December 2016	Carrying amount of transferred assets not derecognised £m	Carrying amount of associated liabilities £m	Fair value of transferred assets not derecognised £m	Fair value of associated liabilities £m	Net position £m
Oak No. 1 PLC	**148.7**	**130.6**	**155.0**	**131.9**	**23.1**

31 December 2015	Carrying amount of transferred assets not derecognised £m	Carrying amount of associated liabilities £m	Fair value of transferred assets not derecognised £m	Fair value of associated liabilities £m	Net position £m
Oak No. 1 PLC	206.5	193.9	209.9	194.8	15.1

43. Country-by-Country reporting

The Capital Requirements (Country-by-Country reporting) Regulations came into effect on 1 January 2014 and introduce reporting obligations for institutions within the scope of the European Union's Capital Requirements Directive (CRD IV). The requirements aim to give increased transparency regarding the activities of institutions.

All companies consolidated within the Group's financial statements are registered entities in England and Wales. Note 23 to these financial statements includes an analysis of subsidiary undertakings and their principal activities. All of the subsidiary undertakings were incorporated in the UK.

The Group did not receive any public subsidies

	Jurisdiction income/ expense arose	2016 £m	2015 £m
Total operating income	UK	**267.5**	224.7
Profit before tax	UK	**128.7**	94.7
Corporation tax (paid)	UK	**(31.5)**	(20.2)
Employees (average FTE equivalent)	UK	**874**	839

44. Post balance sheet events

There have been no material post balance sheet events

The Company statement of financial position
As at 31 December 2016

	Note	**31 December 2016 £m**	31 December 2015 £m
Assets			
Loans and advances to banks	3	0.8	0.5
Investment in Group undertakings	4	415.0	411.5
Amounts receivable from Group undertakings	6	60.9	0.4
Total assets		**476.7**	**412.4**
Liabilities			
Amounts payable to Group undertakings	7	0.9	–
Subordinated notes	8	60.9	–
Total liabilities		**61.8**	**–**
Equity			
Share capital	9	34.5	34.5
Share premium account	9	73.4	73.4
Contingent convertible securities	11	74.0	74.0
Capital redemption reserve		0.1	0.1
Share-based payment reserve	10	6.9	3.4
Retained earnings		226.0	227.0
Total equity		**414.9**	**412.4**
Total liabilities and equity		**476.7**	**412.4**

The notes and information on pages 202 to 204 form part of these financial statements.

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

Phillip Monks
Director

1 March 2017

James Mack
Director

1 March 2017

Registered number: 06764335

Financial statements

The Company statement of cash flows
For the year ended 31 December 2016

	Note	**Year ended 31 December 2016 £m**	Year ended 31 December 2015 £m
Cash flows from operating activities			
Profit/(loss) before taxation	2	6.5	(1.2)
Decrease in operating assets		0.4	0.2
Decrease in operating liabilities		–	(0.9)
Net cash flows generated/(used in) from operating activities		**6.9**	**(1.9)**
Cash flows from investing activities			
Investment in Group undertakings	4	–	(74.1)
Net cash used in investing activities		**–**	**(74.1)**
Cash flows from financing activities			
Proceeds from issue of shares	9	–	75.0
Issuance costs of Initial Public Offering		–	(2.7)
Proceeds from exercise of warrants		–	5.6
Proceeds from subordinated notes	8	60.0	–
Issue of subordinated notes	8	(60.0)	–
Interest received on subordinated notes	8	0.9	–
Interest paid on subordinated notes	8	(0.9)	–
Proceeds received from Bank for the purchase of treasury shares		0.9	–
Purchase of treasury shares		(0.9)	–
Coupon paid on contingent convertible securities, net of tax		(6.6)	(2.8)
Net cash (used in)/ from financing activities		**(6.6)**	**75.1**
Net increase/(decrease) in cash and cash equivalents		0.3	(0.9)
Cash and cash equivalents at start of the year	3	0.5	1.4
Movement during the year		0.3	(0.9)
Cash and cash equivalents at end of the year		**0.8**	**0.5**

The Company statement of changes in equity
For the year ended 31 December 2016

	Share capital £m	Share premium account £m	Contingent convertible securities £m	Capital redemption reserve £m	Share-based payment reserve £m	Warrant reserve £m	Retained earnings £m	Total £m
Year ended 31 December 2016								
As at 1 January	34.5	73.4	74.0	0.1	3.4	–	227.0	412.4
Profit for the year	–	–	–	–	–	–	6.5	6.5
Transactions with equity holders:								
– Share-based payments, including tax reflected directly in retained earnings	–	–	–	–	3.5	–	–	3.5
– Coupon paid on contingent convertible securities issue costs	–	–	–	–	–	–	(6.6)	(6.6)
– Own shares adjustments	–	–	–	–	–	–	(0.9)	(0.9)
As at 31 December	**34.5**	**73.4**	**74.0**	**0.1**	**6.9**	**–**	**226.0**	**414.9**
Year ended 31 December 2015								
As at 1 January	23.7	–	73.7	–	0.9	2.2	234.3	334.8
Loss for the year	–	–	–	–	–	–	(1.2)	(1.2)
Transactions with equity holders:								
– Capital reorganisation prior to IPO	6.3	–	–	0.1	–	–	(6.4)	–
– Share issue proceeds from IPO	3.9	71.1	–	–	–	–	–	75.0
– Share issuance costs	–	(2.7)	–	–	–	–	–	(2.7)
– Share-based payments, including tax reflected directly in retained earnings	–	–	–	–	3.4	–	–	3.4
– Coupon paid on convertible securities, net of tax	–	–	–	–	–	–	(2.8)	(2.8)
– Tax credit on contingent convertible securities issue costs	–	–	0.3	–	–	–	–	0.3
– Exercise of share warrants	0.6	5.0	–	–	–	(2.2)	2.2	5.6
– Transfer of capital contribution to retained earnings	–	–	–	–	(0.9)	–	0.9	–
As at 31 December	**34.5**	**73.4**	**74.0**	**0.1**	**3.4**	**–**	**227.0**	**412.4**

Financial statements

Notes to the Company financial statements

1. Basis of preparation

a) Accounting basis

These standalone financial statements for Aldermore Group PLC (the "Company") 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 ("EU"). The significant accounting policies adopted are set out in Note 2 to the consolidated financial statements.

These results include the Employee Benefit Trust ("EBT"). Further details of the own shares purchased under the EBT can be found in Note 36 to the consolidated financial statements.

b) Going concern

As detailed in Note 1(c) to the consolidated financial statements, the Directors have performed an assessment of the appropriateness of the going concern basis. 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 profit 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.

	2016 £m	2015 £m
Net profit/(loss) attributable to equity shareholders of the Company	**6.5**	**(1.2)**

3. Loans and advances to banks

	2016 £m	2015 £m
Repayable on demand	**0.8**	**0.5**

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

	2016 £m	2015 £m
As at 1 January	411.5	334.0
Capital injections – share capital	–	74.1
Capital contributions – Share-based payments	3.5	3.4
As at 31 December	**415.0**	**411.5**

As at 31 December 2016, £nil investments (31 December 2015: £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.

All the companies listed in Note 23 to the consolidated financial statements are related parties to the Company.

Additional Tier 1 Perpetual Loan

On 9 December 2014, the Company set up a perpetual loan of indefinite duration that is repayable at the option of the Bank, and bears interest at an initial rate of 11.875 per cent per annum until 30 April 2020 and thereafter at the relevant Reset Interest Rate as provided in the loan agreement. 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

Details of related party transactions of the Company are provided in Note 41 to the consolidated financial statements.

6. Amounts receivable from Group undertakings

	2016 £m	2015 £m
Group relief on contingent convertible securities	–	0.4
Subordinated loan to Aldermore Bank PLC	60.9	–
	60.9	**0.4**

On the 28 October 2016, the Company made a £60 million subordinated 8.50 per cent loan to Aldermore Bank PLC, repayable in 2026, with an option for the Bank to redeem after five years. The interest rate is fixed until October 2021. The loan is carried in the statement of financial position at amortised cost.

7. Amounts payable to Group undertakings

	2016 £m	2015 £m
Employee Benefit Trust	**0.9**	**–**

During 2016, the Bank made an interest free loan to the Employee Benefit Trust ("EBT") in order to purchase own shares to enable the Group to meet future share-based payments awards as detailed in Note 10.

8. Subordinated notes

	2016 £m	2015 £m
Subordinated notes	**60.9**	**–**

On 28 October 2016, the Company issued £60 million subordinated 8.50 per cent notes, repayable in 2026, with an option for the Company to redeem after five years. The loan notes are carried in the statement of financial position at amortised cost.

9. Share capital

Details of share capital and share premium account of the Company are provided in Note 36 to the consolidated financial statements.

10. Share-based payments

Details of share-based payments issued by the Company are provided in Note 37 to the consolidated financial statements.

During June 2016, an Employee Benefit Trust ("EBT") purchased 466,179 of Aldermore Group PLC's ordinary £0.10 shares from the market for consideration of £0.9 million. Purchases were made to enable the Group to meet a future share-based payment obligation in respect of the recruitment award as detailed in Note 36. These purchases constitute own shares held by a Group EBT and are recorded against retained earnings within equity.

This purchase constitutes own shares held by a Group EBT and the related costs are recorded against retained earnings within equity.

Financial statements

Notes to the Company financial statements
continued

11. Contingent convertible securities
Details of the contingent convertible securities issued by the Company are provided in Note 38 to the consolidated financial statements.

12. 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 106 to 139 apply to the Company where relevant and therefore no additional disclosures are included in this note.

13. Fair value 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.

14. Controlling party information
Details of controlling party information of the Company are provided in Note 41 to the consolidated financial statements.

15. Post balance sheet events
There have been no material post balance sheet events.

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Appendices

Glossary

AIP: Annual Incentive Plan. Annual bonus scheme that is open to selected senior employees.

ALCO: Asset and Liabilities Committee. Responsible for managing the Group's exposure to capital, liquidity, interest rate and market risk.

Allowance for impairment losses: Allowances held against assets on the statement of financial position as a result of the raising of a charge against profit for the incurred losses in the lending book. The allowance represents management's best estimate of losses incurred in the loan portfolio at the reporting date.

AnaCap: See "Principal Shareholders" below.

Arrears: Customers are said to be in arrears or non-performing when they are behind in fulfilling their obligations with the result that an outstanding loan is unpaid or overdue. Corporate customers may also be considered non-performing prior to being behind in fulfilling their obligations. This can happen when a significant restructuring exercise begins.

AT1 Capital: See "Contingent Convertible Securities" below.

Bank: Aldermore Bank PLC, the principal subsidiary of Aldermore Group PLC. Bank is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority (Financial Services Register Number: 204503). It is registered in England (company number: 00947662).

Basel II: A statement of best practice issued by the Basel Committee on Banking Supervision, that defines the methods by which firms should calculate their regulatory capital requirements to retain enough capital to protect the financial system against unexpected losses. Basel II became law in the EU Capital Requirements Directive, and was implemented in the UK via the then FSA Handbook.

Basel III: A strengthening of the requirements laid out in Basel II and has been phased into the Group from 2014 ahead of full implementation by 2022. Basel III is implemented within the European Union (including the UK) through CRD IV.

Basis points (bps): One hundredth of a per cent (0.01%). 100 basis points is 1%. It is used in quoting movements in interest rates or yields on securities.

BBR: Bank of England Base Rate.

Board: The Board of Directors of Aldermore Group PLC.

Capital Requirements Directive (CRD IV): This encompasses the Capital Requirements Directive and the Capital Requirements Regulation (CRR) as well as the PRA's Policy Statement PS7/13: "Strengthening capital standards". CRD IV implements Basel III within the European Union (including the UK) and is a strengthening of the requirements laid out in Basel II.

Capital Requirements Regulation (CRR): The European Union has implemented the Basel III capital proposals through the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD), collectively known as CRD IV. CRD IV was implemented on 1 January 2014.

Capital resources: Capital held, allowable under regulatory rules, less certain regulatory adjustments and deductions that are required to be made. Capital includes retained earnings, share capital and share premium.

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

CCA: Consumer Credit Act.

CEO: Chief Executive Officer, Philip Monks.

CET1: See Fully Loaded CRD IV Common Equity Tier 1 (CET1) capital.

CFO: Chief Financial Officer, James Mack.

CFP: Contingency Funding Plan. Outlines what actions the Group could take to ensure it complies with the liquidity adequacy rules, maintains sufficient capital and operated within its risk appetite and limits, as set and approved by the Board. Forms part of the Group's Recovery and Resolution Plan (see "RRP" below).

Chairman: Danuta Gray (interim).

CML: Council of Mortgage Lenders, the main trade body representing UK mortgage lenders, of which Aldermore Bank PLC is a full member.

Collateral: A borrower's pledge, usually a property, which acts as security for repayment of the loan.

Company: Aldermore Group PLC as a standalone entity. Aldermore Group PLC is registered in England (company number: 06764335).

Conduct risk: The risk of detriment to the Group's customers due to the inappropriate execution of its business activities and processes.

Contingent Convertible Securities: Fixed Rate Reset Additional Tier 1 Perpetual Subordinated Contingent Convertible Securities also referred to as AT1 Capital. The Group issued £75 million of AT1 securities on the Irish Stock Exchange on 9 December 2014.

COO: Chief Operating Officer, Dana Cuffe.

Cost of risk: Cost of risk is defined as credit impairment losses divided by average gross loans for a given period.

Cost/income ratio: Administrative expenses including depreciation and amortisation divided by total operating income.

Coverage ratio: The proportion of individually impaired loans and advances that are covered by individual allowances for impairment losses.

CRD III: The Third Capital Requirements Directive issued by the EU. CRD III has been superseded by CRD IV.

CRD IV: The Fourth Capital Requirements Directive issued by the EU, intended to implement the Basel III agreement. Preceded by CRD III.

Credit impairment: Impairment losses on loans and advances to customers.

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

Credit Support Annex (CSA): The swap Credit Support Annex 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.

CRO: Chief Risk Officer, Christine Palmer.

Customers' accounts: Money deposited by individuals and companies that are not credit institutions. Such funds are recorded as liabilities in the Group's statement of financial position under "customers' accounts".

Debt securities in issue: Securities issued by the Group that are secured on certain portfolios of variable and fixed rate mortgages through the Group's securitisation vehicle, Oak No. 1 PLC.

Derivative: A financial instrument that has a value based on the expected future price movements of the instrument to which it is linked.

Disclosure and Transparency Rules (DTR): A set of rules implemented by the United Kingdom Listing Authority which covers matters relating to financial reporting.

DRR Regulations: Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008.

DSP: Deferred Share Plan. A share plan under which a proportion of the annual bonus earned by selected senior employees is deferred into shares.

Effective Interest Rate (EIR): The effective interest rate method calculates the amortised cost of a financial asset or financial liability, and allocates the interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset or financial liability. Calculation of the effective interest rate takes into account all contractual terms of the financial instrument but includes all amounts received or paid that are an integral part of the overall return, direct incremental transaction costs related to the acquisition or issue of a financial instrument and all other premiums and discounts.

Emergence Period (EP): The time between a trigger event occurring and the loans being identified as individually impaired.

EPS: Earnings per share.

EU: European Union.

Executive Directors: Phillip Monks (CEO) and James Mack (CFO).

Executive Committee: Comprises Phillip Monks (CEO), James Mack (CFO), Christine Palmer (CRO), Dana Cuffe (COO), Carl D'Ammassa (Group Managing Director – Business Finance), Charles Haresnape (Group Managing Director – Mortgages) and Rob Divall (Group HR Director). Charles is leaving the Group in 2017. A search is underway for his replacement. Under the leadership of the CEO, the Executive Committee is responsible for the management of the Group.

Expected loss (EL): A measure of anticipated loss for exposures captured under an internal ratings based credit risk approach. The 12 month expected loss amount is the exposure, arising from a potential default of a counterparty, over the next 12 months in respect of the amount expected to be outstanding at default.

Exposure at default (EaD): An estimate of the amount expected to be owed by a customer at the time of a customer's default.

External audit: An independent opinion, by an external firm (KPMG LLP), on the Group and Company's financial statements.

Fair Value: Fair value is defined as the amount for which an asset could be exchanged, or a liability settled, between willing parties in an arm's length transaction.

Financial Conduct Authority (FCA): The FCA is responsible for the regulation of conduct in retail, as well as wholesale, financial markets and the infrastructure that supports those markets.

Financial instruments: Any document with monetary value. Examples include cash and cash equivalents, but also securities such as bonds and stocks which have value and may be traded in exchange for money.

Financial Services Authority (FSA): An independent non-governmental body, given statutory powers by the Financial Services and Markets Act 2000, which regulated the financial services industry. It was replaced as the UK's financial regulator on 1 April 2013 by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA).

Financial Services Compensation Scheme (FSCS): The UK's compensation fund of last resort for customers of authorised financial services firms. The FSCS may pay compensation to customers, up to a specified limit, if a firm is unable, or likely to be unable, to pay claims against it, usually because it has stopped trading or has been declared in default. The FSCS is funded by the financial services industry. Every firm authorised by the PRA is obliged to pay an annual levy, which goes towards its running costs and compensation payments.

Forbearance: Forbearance takes place when a concession is made on the contractual terms of a loan in response to borrowers financial difficulties. Forbearance options are determined by assessing the customer's personal circumstances.

Forced Sale Discount (FSD): The difference in sale proceeds between a sale under normal conditions and a sale at auction.

FTSE 250: The share index consisting of the 101st to 350th largest company listed on the London Stock Exchange. Aldermore Group PLC has been a member of the FTSE 250 since June 2015.

Fully loaded CRD IV Common Equity Tier 1 (CET1) capital: A measure of capital that is predominantly common equity as defined by the Capital Requirements Regulation. CET 1 capital is the highest quality of capital and comprises share capital, share premium, capital redemption reserve, available for sale reserve, net assets and retained earnings. The book values of goodwill and intangible assets as well as other regulatory adjustments, including the full 12 month amount of expected loss over provisions, are deducted from Common Equity Tier 1 capital for the purposes of capital adequacy.

Funding for Lending Scheme (FLS): Launched by The Bank of England. Originally due to end in January 2015, the FLS was subsequently extended and will now end in January 2018.

Gap: The Bank's net exposure between fixed and variable rate elements being managed within its market risk, e.g. interest rate movements (see Market risk).

GIA: Group Internal Audit.

Group: The Aldermore Group PLC standalone entity and its subsidiary undertakings, including its principal subsidiary, Aldermore Bank PLC. Aldermore Group PLC is registered in England (company number: 06764335).

Hedging: A technique used by the Group to offset risks on one instrument by purchasing a second instrument that is expected to perform in the opposite way.

Help to Buy: "Help to Buy" was formed as part of the 2013 Budget announcement by the Government and is part of a package of measures designed to increase the availability of low-deposit mortgages for credit worthy households and to boost the supply of new housing.

HMO: Houses of multiple occupancy. A property rented out by at least 3 people who are not from 1 "household" (e.g. a family) but share facilities like the bathroom and kitchen. It is sometimes called a "house share".

HPI: House Price Index.

IASB: International Accounting Standards Board. A London-based organisation which seeks to set and enforce standards for accounting procedures. It is responsible for maintaining the International Financial Reporting Standards (IRFS).

IFRSs: International Financial Reporting Standards, the accounting standards subject to endorsement by the EU by which the Group prepared its statutory accounts commencing from 1 January 2014.

Impaired loans: Loans where the Group does not expect to collect all the contractual cash flows or expects to collect them later than they are contractually due.

Appendices

Glossary
continued

Impairment allowance: A loss allowance held on the statement of financial position as a result of the raising of a charge against profit for the incurred losses in the lending book. An impairment loss allowance may be either individual or collective.

Independent Non-Executive Directors: A Director that is free from any business or other relationship that could materially interfere with the exercise of their independent judgement.

Individual Capital Guidance (ICG): The PRA's statement as to the regulatory capital under Pillar 2a that it expects the Group to hold over the Pillar 1 requirement.

Individual Liquidity Adequacy Assessment (ILAA): The Group's assessment of its liquidity risks, controls and quantification of liquid assets required to survive severe financial shocks addressed through the use of stress tests prescribed by the PRA (see Liquidity risk).

Individually significant: Large value loans that exceed a balance threshold established by the Group, above which it is deemed appropriate to assess accounts for impairment on an individual basis.

Initial Public Offering (IPO): The act of offering ordinary equity shares of a company on a public stock exchange for the first time. The Group completed its IPO on 13 March 2015.

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

Interim Chairman: Danuta Gray.

Internal audit: The examination of the Group's records and reports by its employees. Internal audits are usually intended to prevent fraud and to ensure compliance with Board directives and management policies.

Internal Capital Adequacy Assessment Process (ICAAP): The Group's own assessment, as part of Basel II and Basel III requirements, of the levels of capital that it needs to hold in respect of its regulatory capital requirements (for credit, market and operational risks) and for other risks including stress events.

KMP: Key management personnel, namely Directors of the Group and members of the Executive Committee.

KPIs: Key performance indicators.

Leverage ratio: A CRD IV measure, calculated as the ratio of Tier 1 capital to total exposures. Total exposures include on-balance sheet items, off-balance sheet items and derivatives. The leverage ratio is a supplementary measure to the risk based capital requirements and is intended to constrain the build-up of excess leverage in the banking sector.

LIBOR (London Interbank Offered Rate): The interest rate participating banks offer to other banks for loans on the London market.

Liquid Asset Buffer: The stock of assets which the Bank has available in order to manage its liquidity risk. These assets have relatively short maturity dates.

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

Loan to value (LTV): A ratio which expresses the amount of a mortgage outstanding as a percentage of the value of the property. The Group calculates residential mortgage LTV on an indexed basis (the value of the property is updated on a quarterly basis to reflect changes in the house price index (HPI).

Loans to Deposit Ratio: The ratio of loans and advances to customers net of allowance for impairment losses divided by customer deposits.

Loss given default (LGD): An estimate of the actual loss that would occur in the event of default expressed as a percentage of the Exposure at Default.

LPA: Law of Property Act.

LSE: London Stock Exchange.

Market risk: The financial impact from movements in market prices on the value of assets and liabilities. The majority of the Bank's market risk arises from changes in interest rates.

MIA: Months in arrears.

Monte Carlo simulation: A broad class of computational algorithms that rely on repeated random sampling to obtain numerical results.

Net interest income: The difference between interest received on assets and interest paid on liabilities after taking into account the effect of hedging derivatives.

Net Interest Margin (NIM): Net interest income as a percentage of average interest-earning assets.

Net revenue margin: Total operating income as a percentage of average interest-earning assets.

NPL (non-performing loans) ratio: Individually impaired loans expressed as a percentage of gross loans.

Oak No 1 PLC: The Group's securitisation vehicle. Oak No.1 PLC is registered in England (company number: 08814635).

Operational 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.

Origination: The process of creating or acquiring a loan or mortgage.

Parent Company: Aldermore Group PLC. Aldermore Group PLC is registered in England (company number: 06764335).

Past due: When a counterparty has failed to make a payment when contractually due.

Pillar 1: Minimum capital requirement under Capital Requirements Regulation.

Pillar 2a: PRA's guidance as to regulatory capital it expects a bank to hold above Pillar 1.

Pillar 3: The part of CRD IV that sets out disclosure requirements in relation to their risks, the amount of capital required to absorb them, and their approach to risk management. The aim is to strengthen market discipline.

Principal Shareholders: Collectively AnaCap Financial Partners L.P., AnaCap Financial Partners II, L.P., AnaCap Derby Co-Investment (No.1) L.P. and AnaCap Derby Co-Investment (No.2) L.P.

Probability of default (PD): The likelihood that a loan will not be repaid and will fall into default. To calculate PD, the Group assesses the credit quality of borrowers and other counterparties and assigns them an internal risk rating.

Prudential Regulation Authority (PRA): The FSA was replaced as the UK's financial regulator on 1 April 2013 with two new regulatory bodies: the PRA and the FCA. The PRA, a subsidiary of the Bank of England, is responsible for promoting the stable and prudent operation of the financial system through regulation of all deposit-taking institutions, insurers and investment banks.

PSP: Performance Share Plan. A share plan that is open to selected senior employees.

Pts: Percentage points.

RAF: Risk Appetite Framework.

Recovery and Resolution Plan (RRP): The FSA required all UK deposit takers and large investment firms to draw up a Recovery and Resolution Plan by 31 December 2012. The Recovery Plan assesses and documents the recovery options available in situations of financial stress or negative financial shocks, either market-wide or idiosyncratic. The Resolution Plan will provide authorities with sufficient information to enable them to determine a detailed roadmap to resolve a failed financial institution, without resorting to government (effectively taxpayer) support.

Return on Equity (RoE): The ratio of profit for the year (after tax) to average shareholders' equity, expressed as a percentage.

Risk Weighted Assets (RWA): A measure of a bank's assets adjusted for their associated risks. Risk weightings are established in accordance with Basel II.

RMBS: Residential Mortgage Backed Securities. See "Securitisation" below.

RMF: Risk Management Framework. The Risk Management Framework outlines the governance, policies, procedures, systems, tools, techniques and activities by which the Board and senior management establish and monitor the Group's risk appetite and effectively manage risk.

RSP: Restricted Share Plan. A share plan that is open to selected senior employees.

SBP: Share-based payments.

Securitisation: Securitisation is a process by which a group of assets, usually loans, are aggregated into a pool, which is used to back the issuance of new securities. A company sells assets to a securitisation vehicle which then issued securities backed by the assets. This allows the credit quality of the assets to be separated from the credit rating of the original company. Assets used in the securitisations undertaken to date include mortgages to create residential mortgage backed securities (RMBS). The Group established Oak No 1 PLC as part of its funding and capital management activities.

Senior Independent Director: Danuta Gray joined the Board in September 2014 and acted as the Senior Independent Director from her appointment until 7 February 2017, when she was appointed as Interim Chairman. Danuta Gray will resume her responsibilities as Senior Independent Director on the appointment of a new Chairman.

SIP: Share Incentive Plan. A share plan that is open to all employees.

SMEs: Small and medium sized businesses engaging with the Group as customers.

SREP: Supervisory Review Evaluation Process. The SREP is a process by which the PRA will (taking into account the nature, scale and complexity of a firm's activities) review the arrangements, strategies, processes and mechanisms implemented by a firm to comply with its regulatory requirements laid down in PRA rules and the CRR, evaluate the risks to which the firm is or might be exposed, assess the risks that the firm poses to the financial system, and evaluate the further risks revealed by stress testing.

Standard Variable Rate (SVR): A variable and basic rate of interest charged on a mortgage. This may change in reaction to market conditions resulting in monthly repayments going up or down. Within Aldermore the SVR is called the Aldermore Managed Rate (AMR).

Strategic risk: The risk which can affect the Group's ability to achieve its corporate and strategic objectives.

Supervisory Authority: The UK Prudential Regulation Authority.

Term Funding Scheme (TFS): Designed to reinforce the transmission of Bank Rate cuts to those interest rates actually faced by households and businesses by providing term funding to banks at rates close to Bank Rate. The TFS also provides participants with a cost effective source of funding.

The Bank: Aldermore Bank PLC, the principal subsidiary of Aldermore Group PLC. Bank is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority (Financial Services Register Number: 204503). It is registered in England (company number: 00947662).

The Group: The Aldermore Group PLC standalone entity and its subsidiary undertakings, including its principal subsidiary, Aldermore Bank PLC. Aldermore Group PLC is registered in England (company number: 06764335).

Tier 1: A regulatory measure of financial (capital) strength. Tier 1 is divided into Common Equity Tier 1 (CET1) and Additional Tier 1 capital. CET 1 capital comprises share capital, share premium, capital redemption reserve, available for sale reserve and retained earnings. The book values of goodwill and intangible assets are deducted from CET1 capital and other regulatory adjustments may be made for the purposes of capital adequacy. Qualifying capital instruments such as Contingent Convertible Securities are included in Additional Tier 1 capital.

Tier 1 ratio: Tier 1 capital divided by Risk Weighted Assets.

Tier 2: Tier 2 capital comprises the Group's subordinated notes and collective impairment allowance (for exposures treated on a Basel II standardised basis). Certain regulatory deductions may be made for the purposes of assessing capital adequacy.

Total capital ratio: The sum of the Tier 1 capital ratio and the Tier 2 capital ratio.

TSR: Total Shareholder Return. A measure of performance that combines share price appreciation and dividends paid to show the total return to the shareholder expressed as an annualised percentage.

UK GAAP: United Kingdom Generally Accepted Accounting Practice, the accounting standards to which the Group prepared its statutory accounts until 31 December 2013.

Unsecured lending: Lending for which there is no collateral for the loan.

Appendices

Shareholder information

Annual General Meeting (AGM)

The AGM will be held on 16 May 2017 at the offices of Linklaters LLP, 1 Silk Street, London EC2Y 8HQ, commencing at 11.00am. Further details about the meeting, including the proposed resolutions, can be found in the Notice of AGM which will be posted to shareholders and made available on the Company's website at www.investors.aldermore.co.uk

Reports and communications

The Group issues regulatory announcements through the Regulatory News Service ("RNS"); shareholders can view releases via the "News and Results" section of the Company's website at www.investors.aldermore.co.uk. You will also find frequently asked questions on shareholding matters on the website.

A summary of our statutory reports and shareholder communications which can also be found in the "News and Results" section of the Company's website are listed below:

		Available format		
	Month	Online	RNS	Paper
Full-year results	Mar	Y	Y	
Annual Report and Accounts	Apr	Y		Y
Pillar 3 report	Apr	Y		
Notice of AGM and voting materials	Apr	Y		Y
Q1 trading update	May	Y	Y	
Interim results	Aug	Y	Y	
Q3 trading update	Nov	Y	Y	

Information on your shareholding

The Company's register of members is maintained by Equiniti Limited who act as our registrar. If you have any questions about your shareholding or you require any other guidance, you can contact Equiniti as follows:

Equiniti
Aspect House
Spencer Road
Lancing
West Sussex
BN99 6DA
United Kingdom
Tel: 0371 384 2030

Tel: +44 121 415 7047 (if calling from outside the UK)

Lines open 8.30am to 5.30pm (UK time), Monday to Friday (excluding public holidays in England and Wales)

Website: www.shareview.co.uk

Correspondence should refer to Aldermore Group PLC and include your full name, address and your 8 or 11 digit Shareholder Reference which can be found on your Aldermore Group PLC share certificate or proxy card.

A range of shareholder information and forms are available online at Equiniti's shareholder website, www.shareview.co.uk, including the portfolio service which gives you access to more information on your investment. By registering for this service you can also:

- Elect to view company communications online
- Research market news and data to help your investment decisions
- Update your details online, including your address or UK bank mandate
- Buy and sell shares easily through Equiniti's Shareview Dealing service
- Create your own investment portfolio showing all of your shareholdings using Shareview Portfolio
- Email queries securely

Share price information

Shareholders can access both the latest and historical share prices on our website at www.investors.aldermore.co.uk. For a real-time buying or selling price, you will need to contact a stockbroker.

Electronic shareholder communications

As an alternative to receiving documents in hard copy, shareholders can choose to receive all Company information, such as the Annual Report and Accounts and Notice of AGM, electronically. This way of receiving information has a number of advantages, including quicker delivery of documents and the ability to access reports and results on the internet wherever you are. There are also cost and environmental benefits due to the reduction in printing, packaging and postage costs.

Registering for electronic shareholder communications is very straightforward and can be done online at any time via Equiniti's shareholder website at www.shareview.co.uk

Share dealing services

The Company itself does not endorse or recommend any one service for the buying or selling of shares. The price and value of any investments and any income from them can fluctuate and may fall. Therefore, you may get back less than the amount you invested. Past performance is not a guide to future performance.

ShareGift is a charity (No.1052686) which realises the value locked up in small shareholdings. The resulting proceeds are donated to a wide range of charities based on donor suggestion. For further details please visit www.sharegift.org

Share fraud – warning to shareholders

In recent years, a number of other companies have become aware that their shareholders have received unsolicited phone calls or correspondence concerning investment matters. These are typically from overseas-based organisations who target UK shareholders, offering to sell them what often turn out to be worthless or high-risk shares in US or UK investments. These operations are commonly known as "boiler rooms". They can be very persistent and extremely persuasive, and may attempt to persuade individuals to provide email addresses or other personal information. We are not aware of any Aldermore Group investors having been targeted, but we would urge you to remain vigilant.

It is not just the novice investor that has been duped in this way; many of the victims had been successfully investing for several years. 5,000 people contact the Financial Conduct Authority ("FCA") about share fraud each year, with victims losing an average of £20,000. The FCA provides the following guidance should you be contacted in this manner:

- obtain the name of the person calling and the organisation they represent;
- check that they are properly authorised by checking the FCA register of regulated firms at www.fca.org.uk/firms/financial-services-register;
- call the organisation back to verify their identity using the telephone number listed for them on the FCA register;
- search the FCA list of unauthorised firms and individuals to avoid doing business with at www.fca.org.uk/consumers/unauthorised-firms-individuals#list. If you deal with an unauthorised firm you will not be eligible to receive payment under the Financial Services Compensation Scheme;
- report any suspicions to the FCA either by calling 0800 111 6768 or completing the online form at www.fca.org.uk/consumers/report-scam-unauthorised-firm and if the calls persist, hang up; and
- if you have already paid money to share fraudsters you should contact Action Fraud on 0300 123 2040.

Appendices

Shareholder information
continued

To reduce the risk of becoming a victim of fraud you should:

- ensure all your certificates are stored in a safe place, or hold your shares electronically in CREST (electronic settlement system for UK and Irish securities) via a nominee;
- reduce the number of cold calls you receive by registering with the Telephone Preference Service on 0345 070 0707 or by visiting **www.tpsonline.org.uk**. Alternatively you can also register by writing to Telephone Preference Service, DMA House, 70 Margaret Street, London W1W 8SS;
- keep all correspondence containing your shareholder reference in a safe place;
- shred all unwanted correspondence;
- inform Equiniti as soon as possible if you change your address. If you receive a letter from Equiniti regarding a change of address and have not recently moved house, please contact them immediately. You may be a victim of identity theft;
- know when dividends will be paid. You can request that dividends be paid direct to your bank, reducing the risk of cheques being intercepted or lost in the post. If you change your bank account, inform Equiniti of the details of your new account; and
- consider getting advice from a suitably authorised financial advisor before making any investment decision, particularly if the type of investment is unfamiliar to you.

Designed and produced by Radley Yeldar www.ry.com

Aldermore are committed to caring for the environment and looking for sustainable ways to minimise our impact on it.

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