

20 March 2007

For immediate release



ARBUTHNOT BANKING GROUP PLC

Preliminary results for the year to 31 December 2006

Arbuthnot Banking Group PLC (“Arbuthnot”) today announces final results for the year ended 31 December 2006. Arbuthnot is the holding company for Arbuthnot Securities Limited, Arbuthnot Latham & Co Limited and Secure Trust Bank PLC.

Financial Highlights

	2006	2005	Increase
Operating income	£57.8m	£56.3m	+3%
Profit before income tax	£14.7m	£7.7m	+92%
Profit before tax and exceptional items	£8.2m	£7.4m	+12%
Basic earnings per share	63.8p	45.8p	+39%
Total dividends	32.5p	32.0p	+2%
Net assets	£43.3m	£33.1m	+31%
Tier 1 & 2 Capital	£48.2m	£37.0m	+30%

Commenting on the results, Henry Angest, Chairman and Chief Executive of Arbuthnot, said:

“Arbuthnot Banking Group made good progress in 2006. We are particularly pleased that Arbuthnot Securities again substantially raised its profits. This together with the £12.6 million profit realised on the sale of Ropemaker Street demonstrates the Group’s ability to create significant value through taking an independent and long term view.”

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Operational Highlights

Investment Banking - Arbuthnot Securities

- Total income of £21.7m (2005: £19.5m)
- Profit before tax and exceptional items up 77% to £5.0m (2005: £2.8m)
- 35 transactions including six IPO's in 2006
- Corporate client list increased from 60 to 71 (now 75)

Private Banking – Arbuthnot Latham

- 18% deposit growth, 11% loan book growth and 11% client growth
- Strong investment management performance with average absolute returns of 12.7%, being 3.3% ahead of the benchmark
- Net investment of £1.1m in developing business
- Profit before tax and exceptional items broadly unchanged at £0.3m (2005: £0.4m)

Retail Banking – Secure Trust Bank

- Appointment of new management team bringing expertise from Barclays, GE and HSBC
- Key aspects of new strategy include:
 - Enhancement of the core “OneBill” product
 - Focus on building customer base of “OneBill”
 - Move away from taking risk in unsecured lending
- Profit before tax and exceptional items reduced by 11% to £6.8m (2005: £7.5m)
- Investment of £1.5m in 2007 and a further £1.5m in 2008

Switzerland

- Appointment of Chief Executive
- Swiss Bank to be operational in 2007 (subject to regulatory approval)

Sale and Leaseback – 20 Ropemaker Street

- £12.6m exceptional profit achieved
- Lease agreed on favourable terms including a five year and nine year option to break the lease

CHAIRMAN'S STATEMENT

Profits before tax for 2006 were £14.7 million (2005: £7.7 million). A better reflection of underlying performance is pre-tax profit before exceptional items, which amounted to £8.2 million (2005: £7.4 million). This is a particularly satisfying result since it was achieved in a year when two of the group's three businesses operated in a phase of transition. Secure Trust Bank started its turnaround under a new management team, while the phase of long term investment in Arbuthnot Latham continued in 2006. That the Group was able to improve profitability against such a challenging background reflects a continued strong performance at Arbuthnot Securities, and also the benefits of our strategy of diversifying our income across the financial services sector.

Arbuthnot Securities

Since recording losses in the first two years in which it was owned by the Group (2003 and 2004), the performance of Arbuthnot Securities has improved significantly. Pre-tax pre-exceptional profits for 2006 rose to £5.0 million (2005: £2.8 million), on total income of £21.7 million (2005: £19.5 million). Income was well balanced with primary income and secondary income/corporate retainers each representing 50%, which provides some reassurance that the business is not overexposed to any downturn in the rate of new issuance on the AIM market. Costs remained well under control, with headcount at the year end of 74, (2005: 74). The corporate client list recorded very pleasing growth, from 60 at the start of the year to 71 at the year end, which has produced a sharp improvement in retainer income.

Arbuthnot Securities completed 35 transactions during the year, including six IPOs. Features of the year include fund raisings for four listed investment funds (for which a total of approximately £250 million was raised), the IPO of Nationwide Accident Repair Services (by the end of 2006 its share price had risen by approximately 50%) and the IPO of Matchtech (a recruitment business with an £85 million market capitalisation).

Arbuthnot Latham

Arbuthnot Latham continued its transition into a full service private banking business growing client numbers by 11%. This involves investment in growing a wealth management business, principally by recruiting more client relationship managers and asset management expertise and has a negative impact on profits. There is typically a lead-time of 12 to 18 months before client relationship managers make a positive profit contribution. As a result, pre-tax pre-exceptional profits in Arbuthnot Latham were broadly unchanged at £0.3m after taking account of a net £1.1m investment in people and infrastructure (2005: £0.4 million).

CHAIRMAN'S STATEMENT (continued)

A key component in the development of this business is achieving growth in assets under management. The performance of the discretionary funds has been most encouraging, with average returns of 3.3% above the benchmark, and an average return of 12.7% in 2006.

Another important factor for the growth of Arbuthnot Latham's franchise is the development of its own offshore capability through the establishment of a bank in Switzerland. Good progress was made here in 2006: we have announced the appointment of Hans-Rudolf Strasser as Chief Executive, progressed outsourcing arrangements and held satisfactory discussions with regulators in Switzerland and the UK. Applications are due to be made to the relevant regulatory bodies shortly and it is anticipated that trading will commence in the second half of 2007. The cost of this investment in 2007 is expected to be £0.7 million.

Secure Trust Bank

During 2006, Secure Trust Bank continued to experience a decline in customer numbers for its "OneBill" account, and disappointing trading in other products and services offered by the bank, including insurance, estate agency and personal lending. Taken together, these factors produced a decline in this division's profit before tax and exceptional items to £6.8 million (2005: £7.6 million). In addition, as previously announced, a provision of £2.9 million was deemed to be appropriate against outstanding debts on the affinity insurance arrangement terminated in 2005. To address the continued decline at Secure Trust Bank, the Board decided to effect senior management changes. Gary Jennison, formerly Managing Director of Barclays Bank branch network was hired as the new Chief Executive. He joined in September 2006, and swiftly brought in a new management team, including a new Chief Operating Officer, a Sales and Marketing Director and a Finance Director.

The new management team has undertaken a comprehensive review of the business and produced a strategy to arrest the decline and restore growth. This strategy involves the strengthening of the core "OneBill" product through the addition of ancillary benefits for the customer and the extension of the offering. The relaunch of "OneBill" is scheduled to take place in the second half of 2007. The implementation of this strategy requires a significant investment in upgrading systems and operational processes, as well as in sales and marketing. This investment, most of which will be expensed rather than capitalised, is expected to affect the income statement for Secure Trust Bank by approximately £1.5 million in 2007, with a further £1.5 million expected to impact the 2008 result. Despite the effect of this programme on short term results, the Board is confident that the implementation of this strategy will restore this business to growth and that the prospects for the business are promising.

CHAIRMAN'S STATEMENT (continued)

Sale and Leaseback of 20 Ropemaker Street

In 2003, the Group bought the freehold building of 20 Ropemaker Street for £18.0 million including fit out costs with the intention of owning the building for the long term. In 2006, we were urged by our property advisers, who have an outstanding track record, to review our position. As a result of the strong property market and very favourable lease terms, including the ability to terminate the lease in 2011 and 2015, the Board felt a sale and leaseback of the building was an opportunity too good to miss. A profit of £12.6 million was generated as a result of this transaction.

The exceptional profit from the sale and leaseback of the building allowed some well deserved bonuses to be awarded for sustained and outstanding performance. It is the Group's longstanding philosophy to reward outstanding performance with cash awards when the business generates significant profits for shareholders and we intend to continue this practice. As Chairman of the Remuneration Committee, I decided not to accept any reward myself.

Board Changes and Personnel

There were a number of changes to the Group Board during 2006. Gary Jennison was appointed Chief Executive of Secure Trust Bank and joined the Board in September 2006 and Paul Sheriff was appointed Group Finance Director and joined the Board in October 2006. I welcome both of these colleagues to the Board.

Colin Wakelin retired from the Board in December 2006 and David Lascelles will be retiring in May 2007 and I am grateful to both for their contribution over eight and four years respectively. As announced in last year's Annual Report, Stephen Lockley left the Group in September. Additionally, Keith Deakin and Derek Pearson left the Board in February 2007.

These results once again reflect the continuing hard work and dedication of our employees. On behalf of the Board I extend our thanks to all staff for their commitment which contributed to the Group's success in 2006.

Dividend

The Board is proposing an increased final dividend of 22p, from 21.5p last year, bringing the total dividend for the year to 32.5p (2005: 32p). If approved, the final dividend will be paid on 24 May 2007 to shareholders on the register at 27 April 2007.

CHAIRMAN'S STATEMENT (continued)

Outlook

2007 will be a year of investment as the strategy takes effect at Secure Trust Bank and the bank in Zurich is established. Arbuthnot Latham will aim to achieve payback for the significant investment in people made over the last three years. Arbuthnot Securities will seek to build on the strong performance of 2006.

All three divisions have made a satisfactory start to 2007. As ever with our business, Corporate Finance fees are unpredictable and can be individually significant. However, our corporate pipeline is encouraging and the year has begun well with two important corporate transactions completed: a 50 million euro placing for Camper & Nicholsons Marina Fund and a £30 million placing for Aurum Mining plc.

Recognising that 2007, like 2006, is an important year of transition for the Group, the Board remains cautiously optimistic about the outlook.

ARBUTHNOT BANKING GROUP PLC – FINALS 7/30

CONSOLIDATED INCOME STATEMENT

	Profit before exceptional items 2006 £000	Exceptional items 2006 £000	Year to 31.12.06 £000	Profit before exceptional items 2005 £000	Exceptional items 2005 £000	Year to 31.12.05 £000
Interest and similar income	19,168	-	19,168	18,070	-	18,070
Interest expense and similar charges	(9,042)	-	(9,042)	(8,573)	-	(8,573)
Net interest income	10,126	-	10,126	9,497	-	9,497
Fee and commission income	47,787	-	47,787	45,685	-	45,685
Fee and commission expense	(4,241)	-	(4,241)	(1,904)	-	(1,904)
Net fee and commission income	43,546	-	43,546	43,781	-	43,781
Net trading income	4,102	-	4,102	3,069	-	3,069
Operating income	57,774	-	57,774	56,347	-	56,347
Gain on sale of Arbuthnot House	-	12,623	12,623	-	-	-
Gain on sale of minority interest in subsidiary	-	-	-	-	850	850
Impairment losses on loans and advances	(1,986)	(2,900)	(4,886)	(1,641)	-	(1,641)
Operating expenses	(47,559)	(3,212)	(50,771)	(47,339)	(541)	(47,880)
Profit before income tax	8,229	6,511	14,740	7,367	309	7,676
Income tax expense	(2,092)	(1,953)	(4,045)	(2,359)	162	(2,197)
Profit on discontinued activity after taxation	-	-	-	-	1,405	1,405
Profit for the year	6,137	4,558	10,695	5,008	1,876	6,884
Attributable to:						
Equity holders of the Company	4,833	4,558	9,391	4,613	1,876	6,489
Minority interest	1,304	-	1,304	395	-	395
	6,137	4,558	10,695	5,008	1,876	6,884
Earnings per share for profit attributable to the equity holders of the Company during the year (expressed in pence per share):						
- basic and fully diluted	32.8p	31.0p	63.8p	32.6p	13.2p	45.8p

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CONSOLIDATED BALANCE SHEET

	31.12.06	31.12.05
	£000	£000
ASSETS		
Cash	181	188
Loans and advances to banks and building societies	54,214	28,587
Trading securities – long positions	9,095	5,383
Loans and advances to customers	155,594	140,151
Debt securities held-to-maturity	105,961	88,389
Intangible assets	3,025	3,000
Property, plant and equipment	10,638	31,458
Investment Securities	5,856	2,477
Other assets	22,730	26,471
Total assets	367,294	326,104
LIABILITIES		
Deposits from banks	7,729	9,190
Trading securities – short positions	2,303	2,785
Deposits from customers	270,448	239,433
Debt securities in issue	10,106	12,716
Other liabilities	29,886	26,998
Current tax liabilities	3,486	790
Deferred tax liabilities	35	1,116
Total liabilities	323,993	293,028
EQUITY		
Share capital	150	143
Share premium account	21,085	17,115
Retained earnings	17,866	11,111
Other reserves	1,402	3,395
Capital and reserves attributable to the Company's equity holders	40,503	31,764
Minority interest	2,798	1,312
Total equity	43,301	33,076
Total equity and liabilities	367,294	326,104

ARBUTHNOT BANKING GROUP PLC – FINALS 9/30

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Attributable to equity holders of the Company				Minority interest	Total
	Share capital	Share premium account	Other reserves	Retained earnings		
	£000	£000	£000	£000		
Balance at 1 January 2005	130	13,370	3,395	9,106	89	26,090
Issue of shares	13	3,745	-	-	-	3,758
Sale of minority interest in Arbuthnot Securities Limited	-	-	-	-	832	832
Profit for 2005	-	-	-	6,489	395	6,884
Final dividend relating to 2004	-	-	-	(2,989)	(4)	(2,993)
Interim dividend relating to 2005	-	-	-	(1,495)	-	(1,495)
At 31 December 2005/1 January 2006	143	17,115	3,395	11,111	1,312	33,076
Issue of shares	7	3,970	-	-	-	3,977
Sale of minority interest in Arbuthnot Securities Limited	-	-	-	-	187	187
Transfer on sale of properties	-	-	(1,993)	1,993	-	-
Profit for 2006	-	-	-	9,391	1,304	10,695
Final dividend relating to 2005	-	-	-	(3,060)	(5)	(3,065)
Interim dividend relating to 2006	-	-	-	(1,569)	-	(1,569)
At 31 December 2006	150	21,085	1,402	17,866	2,798	43,301

ARBUTHNOT BANKING GROUP PLC – FINALS 10/30

CONSOLIDATED CASH FLOW STATEMENT

	Year to 31.12.06 £000	Year to 31.12.05 £000
Cash flows from operating activities		
Interest received	19,168	18,099
Interest paid	(9,042)	(8,573)
Fees and commissions received	43,546	45,193
Net trading and other income	4,102	3,069
Recoveries on loans previously written off	10	178
Cash payments to employees and suppliers	(51,816)	(47,062)
Taxation paid	(2,470)	(226)
Cash flows from operating profits before changes in operating assets and liabilities	<u>3,498</u>	<u>10,678</u>
Changes in operating assets and liabilities:		
- net increase in trading securities	(4,194)	2,142
- net increase in loans and advances to customers	(17,439)	(11,917)
- net decrease in other assets	3,797	(14,704)
- net decrease in deposits from other banks	(1,461)	(21,640)
- net increase in amounts due to customers	31,015	36,437
- net increase in other liabilities	2,927	10,269
Net cash from operating activities:		
Continuing activities	18,143	10,397
Discontinued activity	-	868
	<u>18,143</u>	<u>11,265</u>
Cash flows from investing activities		
Purchase of investments	(3,435)	(1,311)
Investment in subsidiaries	-	(1,093)
Disposal of subsidiary, net of cash disposed	-	926
Disposal of minority interest	187	1,682
Purchase of property, plant and equipment	(2,253)	(1,273)
Purchase of computer software	(428)	(310)
Proceeds from sale of property, plant and equipment	34,244	209
Net purchases of debt securities	(16,833)	(25,058)
Net cash used in investing activities	<u>11,482</u>	<u>(26,228)</u>
Cash flows used in financing activities		
Issue of shares	3,977	3,758
Issue of debt securities	-	10,149
Repayment of debt securities	(2,610)	(5,356)
Dividends paid	(4,633)	(4,488)
Net cash from financing activities	<u>(3,266)</u>	<u>4,063</u>
Net increase in cash and cash equivalents:		
Continuing activities	26,359	(12,694)
Discontinued activity	-	1,794
	<u>26,359</u>	<u>(10,900)</u>
Cash and cash equivalents at beginning of year (Note (1))	57,359	68,259
Cash and cash equivalents at end of year	<u>83,718</u>	<u>57,359</u>

Note (1): The cash and cash equivalents at beginning of year have been restated to include certificates of deposit with an original maturity of less than three months. They previously included certificates of deposit with remaining maturity of less than three months.

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SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - see pages 24 to 30

NOTES

1. Segmental Analysis of Profits

	Year to 31.12.06					
	Retail banking	Private banking	Investment banking	Subordinated loan notes	Group costs	Group total
	£000	£000	£000	£000	£000	£000
Segment profit	6,759	341	4,959	-	(3,182)	8,877
Subordinated loan notes interest	-	-	-	(648)	-	(648)
Profit before exceptional items	6,759	341	4,959	(648)	(3,182)	8,229
Exceptional items	(3,358)	12,366	(274)	-	(2,223)	6,511
Profit before tax	3,401	12,707	4,685	(648)	(5,405)	14,740
Discontinued activity						

	Year to 31.12.05					
	Retail banking	Private banking	Investment banking	Subordinated loan notes	Group costs	Group total
	£000	£000	£000	£000	£000	£000
Segment profit	7,576	449	2,801	-	(2,841)	7,985
Subordinated loan notes interest	-	-	-	(618)	-	(618)
Profit before exceptional items	7,576	449	2,801	(618)	(2,841)	7,367
Exceptional items	(163)	(171)	698	-	(55)	309
Profit before tax	7,413	278	3,499	(618)	(2,896)	7,676
Discontinued activity	-	1,405	-	-	-	1,405

The profit before tax figures exclude the results of Arbutnot Insurance Brokers Limited (“AIB”) which was sold in October 2005 and the profits of which (up to the date of sale) are shown as a discontinued activity in the income statement. AIB was previously included within the private banking division.

2. Earnings per ordinary share

Basic and fully diluted

Earnings per ordinary share are calculated on the net basis by dividing the profit attributable to shareholders of £9,391,000 (31.12.05: £6,489,000) by the weighted average number of ordinary shares 14,716,433 (31.12.05: 14,167,472) in issue during the period.

Adjusted

Earnings per ordinary share before exceptional items are calculated on the net basis by dividing the profit before exceptional items attributable to shareholders of £4,833,000 (31.12.05: £4,937,000) by the weighted average number of ordinary shares 14,716,433 (31.12.05: 14,167,472) in issue during the period.

3. These preliminary results, which were approved by the Board of Directors on 19 March 2007, are unaudited. Under IFRS, only a complete set of financial statements comprising a balance sheet, income statement, statement of changes in equity, cash flow statement, together with comparative financial information and financial notes, can provide a fair presentation of the company's financial position, results of operations and cash flow.

The figures for the year ended 31 December 2005 are derived from the Group Accounts for the year. A copy of the Group Accounts for that year, on which the auditors gave an unqualified opinion, has been delivered to the Registrar of Companies.

BUSINESS REVIEW

The business review considers each of the Group's businesses and the key performance measures.

Investment Banking - Arbuthnot Securities

	2006	2005	Increase
Total income	£21.7m	£19.5m	+11%
Corporate clients	71	60	+18%
Gross trading & commission income	£9.6m	£9.0m	+7%
Corporate finance fees	£12.1m	£10.5m	+15%

The turnaround in Arbuthnot Securities continued to progress broadly as planned in 2006, despite more difficult conditions for new issues on the AIM market during the second half of the year. Profit before tax and exceptional items rose by 77% to £5.0 million compared to a £2.8 million profit in 2005 and a £1.6 million loss in 2004.

Corporate fee income amounted to £12.1 million (2005: £10.5 million). Arbuthnot Securities completed 35 transactions during the year, including six IPOs. Features of the year include the fund raisings for four listed investment funds (for which a total of approximately £250 million was raised), the IPO of Nationwide Accident Repair Services (by the end of 2006 its share price had risen by approximately 50%) and the IPO of Matchtech (a recruitment business with an £85 million market capitalisation, which is also trading at a healthy premium).

The corporate client list also grew significantly from 60 at the start of the year to 71 at the year end. The Hemscott 'Corporate Advisers Rankings Guide' shows the Arbuthnot corporate clients list to be the fastest growing in the market.

Secondary commission and trading income amounted to £9.6 million (2005: £9.0 million). Highlights include the £35 million secondary placing of shares in Delta, a corporate client, in May 2006. Secondary revenues and brokership retainers represent 50% of the Company's total income. It is a positive feature of Arbuthnot Securities' earnings profile that it is less dependent on revenue from AIM issuance than many of its competitors. The satisfactory contribution from secondary income and trading partly reflects the benefit of the research hiring programme undertaken over the last two years during which the research team has been largely rebuilt.

This growth in income has been achieved against a background of stable pre-bonus costs. Total headcount ended 2006 where it started the year at 74. However, this picture masked 12 changes of individuals which reflect the on-going process of upgrading the quality of the firm's personnel.

ARBUTHNOT BANKING GROUP PLC – FINALS 14/30

Following the appointment of a new Chief Executive in September 2004, actions taken towards the end of that year put the business on a sustainable footing in 2005. In 2006 the business made further progress in more difficult market conditions. It now has significant momentum, with the structure and positioning to deliver strong growth into the future. Earlier this year Arbuthnot Securities became a member of the Dubai International Financial Exchange and a team of four analysts has also been recruited to be based in a new office in Glasgow. The corporate pipeline is encouraging and 2007 has started well with two substantial fundraisings and a net four new corporate clients in the first two months.

Private Banking – Arbuthnot Latham

	2006	2005	Increase
Operating income	£13.6m	£12.4m	+10%
Customer deposits	£244.0m	£206.9m	+18%
Customer loans	£120.0m	£107.1m	+12%
Total assets	£286.0m	£246.2m	+16%

The past year has marked a period of continued progress for Arbuthnot Latham. Business volumes have risen strongly with client growth of 11% and further investment has been made in both people and services. This investment has resulted in customer deposits growing by 18% to £244 million and the loan book grew by 12% to £120 million.

Arbuthnot Latham continues to improve its service delivery. At the end of the first quarter the new investment management product was launched. Integral to this product is a bespoke risk profiling tool which ensures that each client's portfolio reflects the level of risk they are willing to take. As a result of the introduction of this new product, the rate of growth in assets under management increased steadily throughout the year. The new product was underpinned by excellent performance of the discretionary portfolios, which recorded an average relative return of 3.3% above the benchmark, and an average absolute return of 12.7% for 2006. At the end of 2006 internet banking was introduced and take-up of this service during early 2007 has been encouraging.

Arbuthnot Latham continued to invest in quality staff to provide our clients with the level of service that they have come to expect across the increased product range and was pleased to attract a number of senior private bankers, pensions consultants and specialists in the finance of 'super yachts' and high-end overseas property. Changes to the pensions legislation in April 2006, known as 'A Day', have created opportunities particularly for our self-invested personal pension (SIPP) product.

During 2006 an investment of £1.1 million was made in more client relationship managers and asset management expertise that has had a negative impact on profits in the short-run. There is typically a lead-time of 12-18 months before client relationship managers make a positive contribution. It is anticipated that this investment will ensure that the bank is well placed to deliver an improved return in 2007.

ARBUTHNOT BANKING GROUP PLC – FINALS 15/30

Looking to 2007, continued investment will be made to expand and improve the services to our clients. In particular, in the second quarter of 2007 a credit card will be introduced and improvements to our back office systems will be implemented.

Plans for Arbuthnot Banking Group to open a banking business in Switzerland are well advanced. The Chief Executive Officer has been recruited and the process of obtaining a regulatory licence is proceeding. It is anticipated that the services we will be able to offer in Switzerland will also be attractive to many of Arbuthnot Latham's clients.

Retail Banking – Secure Trust Bank

	2006	2005	Increase
Operating income	£24.2m	£25.9m	-7%
Unsecured lending	£29.9m	£32.3m	-7%
Expenses	£16.1m	£16.9m	-5%
Customer numbers ('000)	46	49	-5%

Despite the increasingly competitive environment and the continuing reduction in customer numbers, the Retail Banking Division delivered a reasonably robust operating income of £24.2 million and profits before tax and exceptional items of £6.8 million.

In 2005, the business entered into an arrangement to write motor insurance business through an affinity arrangement. Higher transaction volumes and a very high level of customer cancellations led to the business being terminated in late 2005. In 2006, a bad debt provision of £2.9 million has been made reflecting the difficulty in recovering the outstanding amounts.

As a result of the changing landscape for unsecured personal lending in the UK, Secure Trust Bank has cut back on new lending outside of the "OneBill" account. This has resulted in a 7% reduction in unsecured loans during 2006. The impairment charge (excluding the £2.9 million provision above) rose £0.3 million to £1.9 million. The decision was also taken to close the loss making Estate Agency business at the end of 2006 and this has already been implemented.

In 2006, the senior management team has been replaced at Secure Trust Bank. In September, Gary Jennison joined as Chief Executive Officer, having previously been responsible for UK branch operations for Barclays. In addition to this appointment, a new Chief Operating Officer, Sales and Marketing Director and Finance Director have been appointed to the business bringing in expertise from GE, Barclays and HSBC respectively.

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The new management team has undertaken a comprehensive review of the business and has produced a strategy to arrest the decline and restore growth. Key themes include the enhancement of the core “OneBill” product, a focus on building the customer base of “OneBill” and a move away from taking risk in unsecured lending outside of the “OneBill” account. Additionally, the “OneBill” product will be enhanced through the addition of ancillary benefits for the customer. The product is scheduled to be re-launched in the second half of 2007.

The investment of approximately £4 million over the next 18 months, most of which will be expensed, will affect the profitability of Secure Trust Bank by approximately £1.5 million in 2007 and a further £1.5 million in 2008. Profits should start improving in 2008 as a result of this investment.

The business currently trades under a number of different brands including “OneBill”, Secure Trust Bank, Secure Homes and SecureDirect. This leads to confusion within the customer base and it is anticipated that the business will be rebranded in the second half of 2007 to coincide with the re-launch of the “OneBill” product.

2007 will be a transition year for Secure Trust Bank with a number of initiatives being planned and developed in the first half for implementation in the second half of the year.

FINANCIAL REVIEW

Highlights

Summarised Profit & Loss Account

£'000	2006	2005
Net interest income	10,126	9,497
Net fee and commission income	43,546	43,781
Net trading income	4,102	3,069
Operating income	57,774	56,347
Operating expenses	(47,559)	(47,880)
Impairment losses	(1,986)	(1,641)
Other items	6,511	850
Profit before income tax	14,740	7,676
Basic earnings per share	63.8p	45.8p

Summarised Balance Sheet

£'000	2006	2005
Assets		
Loans and advances to customers	155,594	140,151
Liquid assets	160,356	117,164
Other assets	51,344	68,789
Total assets	367,294	326,104
Liabilities		
Customer deposits	270,448	239,433
Other liabilities	53,545	53,595
Total liabilities	323,993	293,028
Equity	43,301	33,076
Total equity and liabilities	367,294	326,104

The aim of Arbutnot Banking Group is to maximise revenues and profits through providing a range of financial services to customers and clients in its three chosen niche markets of private banking (Arbutnot Latham), investment banking (Arbutnot Securities) and retail banking (Secure Trust Bank/OBC Insurance Consultants). The Group's revenues are derived from a combination of net interest income from its lending, deposit-taking and money market activities; fees for services provided to customers and clients; commissions earned on the sale of financial instruments and products; and equity market-making profits.

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Background market conditions were generally favourable in 2006. The FTSE 100 index rose by 11% and the IPO market was strong in the first six months though it weakened in the second half. Base rates increased from 4.5% to 5.0% giving limited opportunity for the Group to increase net interest margins. At the same time, the well-publicised pressures on the consumer, particularly in relation to unsecured debt, have led to tighter credit control and a reduction in new unsecured lending. Against this mixed background, an improved operating performance from the Group's businesses enabled total operating income to increase by 3% to £57.8 million, profit before tax to rise by 92% to £14.7 million and earnings per share to increase by 39% to 63.8p.

The statutory operating profit for the Group is shown above. The Board believes a truer reflection of the Group's on-going business is afforded by the measure of 'Adjusted profit before tax' and 'Adjusted earnings per share' that excludes items that are one-off or non-recurring and not part of the on-going business profitability.

£'000	2006	2005
Operating income	57,774	56,347
Operating expenses	(47,559)	(47,339)
Impairment losses	(1,986)	(1,641)
Adjusted profit before tax	8,229	7,367
Adjusted earnings per share	32.8p	32.6p

Adjusted profit before tax rose by 12% to £8.2 million resulting in an adjusted earnings per share of 32.8p. This is principally due to the increased profitability of Arbuthnot Securities resulting in a higher minority interest.

Sale and Leaseback of Arbuthnot House

In 2003, the Group bought the vacant freehold building of 20 Ropemaker Street for £18.0 million including fit out costs. In 2006, as a result of a strong property market and very favourable lease terms, the Group entered into a sale and leaseback of the building. A profit of £12.6 million was generated as a result of this transaction. The lease on the building is a 15 year lease with break clauses at five and nine years for an annual rent of £1.7 million per annum.

Rights Issue

In April 2006, £4 million net of expenses was raised via a placing and open offer which has been earmarked to fund development of the private banking operation in Switzerland.

Balance Sheet Strength and Cash flow

Total assets of the Group increased to £367.3 million (2005: £326.1 million) as a result of the ability to attract customer deposits in the private bank. Net assets of the Group increased to £43.3 million (2005: £33.1 million), due to the cash arising from operating performance combined with the profit on the sale and leaseback transaction and the proceeds from the rights issue.

The Group's total liquid resources (including longer duration certificates of deposit) rose by £43.2 million to £160.4 million (2005: £117.2 million). Cash and cash equivalent rose by £26.3 million to £83.7 million (2005: £57.4 million) principally as a result of the cash received on the sale of Arbuthnot House.

Segmental Analysis

The primary business segments are Investment Banking (Arbuthnot Securities), Private Banking (Arbuthnot Latham), Retail Banking (Secure Trust Bank) and Group costs.

Arbuthnot Securities

£'000	2006	2005
Net interest income	338	119
Net fee and commission income	16,191	15,462
Net trading income	4,102	3,069
Operating income	20,631	18,650
Operating expenses	(15,946)	(15,151)
Profit before tax	4,685	3,499
Gain on sale of shares to minority	-	(850)
Restructuring costs	274	152
Adjusted profit before tax	4,959	2,801

Operating income rose 11% to £20.6 million with expenses rising 5% to £16.0 million. Adjusted profit before tax rose 77% to £5.0 million in 2006.

Under the terms of the Arbuthnot Securities Long Term Incentive Plan, the Group has sold 40% of the issued ordinary share capital in Arbuthnot Securities Limited to its staff via the Arbuthnot No. 2 ESOP Trust.

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Arbuthnot Latham (including Arbuthnot Commercial Finance)

£'000	2006	2005
Net interest income	5,910	5,328
Net fee and commission income	7,645	7,049
Operating income	13,555	12,377
Operating expenses	(13,417)	(12,113)
Bad debt provision	(54)	14
Profit on disposal of Arbuthnot House	12,623	-
Profit before tax	12,707	278
Profit on disposal of Arbuthnot House	(12,623)	-
Restructuring costs	257	171
Adjusted profit before tax	341	449
£'000	2006	2005
Assets		
Advances (including Group companies)	120,082	107,079
Liquid assets	149,442	106,821
Other assets	16,465	32,292
Total assets	285,989	246,192
Liabilities		
Customer deposits (including Group companies)	243,975	206,911
Other liabilities	13,988	14,207
Total liabilities	257,963	221,118
Capital	28,026	25,074
	285,989	246,192

Note: The above balance sheet is for Arbuthnot Latham only

Operating income rose by 10% but continued investment in new staff led to an 11% rise in expenses. Adjusted profit before tax in 2006 was similar to 2005 with adjusted operating profit of £0.3 million compared to £0.4 million in 2005. The 2006 figure includes an investment in people and infrastructure of £1.1 million relating to the wealth management and asset management businesses.

Total assets increased by 16% to £286.0 million (2005: £246.2 million) with loans increasing by 12% and customer deposits by 18%.

Secure Trust Bank (including OBC Insurance Consultants)

£'000	2006	2005
Net interest income	4,526	4,668
Net fee and commission income	19,710	21,270
Operating income	24,236	25,938
Operating expenses	(16,003)	(16,870)
Impairment losses	(4,832)	(1,655)
Profit before tax	3,401	7,413
Restructuring costs	458	163
Bad debt provision ('Yes Car Credit')	2,900	-
Adjusted profit before tax	6,759	7,576

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Operating income fell by 7% to £24.2 million with operating expenses (before restructuring costs) falling by 5%.

Adjusted profit before tax fell 11% to £6.8 million. The impairment charge (before affinity bad debt) rose 17% to £1.9 million as a result of arrears on the unsecured loan book.

Group & Other Costs

£'000	2006	2005
Group costs (including head office property)	(3,182)	(2,841)
Subordinated loan stock	(648)	(618)
Total Group & other costs	(3,830)	(3,459)

Group and other costs increased from £3.5 million in 2005 to £3.8 million in 2006. In addition to the above items, £1.9 million relates to long term bonuses made possible by the sale and leaseback of Arbutnot House and there is a further £0.3 million relating to restructuring costs.

Exceptional Items

In addition to the £12.6 million profit on the sale and leaseback of the building, there was the bad debt provision of £2.9 million, restructuring costs in the three divisions of £1.0 million and Group restructuring costs of £0.3 million. Bonuses totalling £1.9 million were granted to a number of key individuals to recognise their outstanding contribution to the Group.

The total exceptional items resulted in an exceptional profit of £6.5 million in 2006.

Capital

The international measure for capital adequacy is the risk asset ratio which relates regulatory capital to on and off balance sheet assets.

The Group's regulatory capital is divided into two tiers defined by the European Community Banking Consolidation Directive as implemented in the UK by the FSA's Interim Prudential Sourcebook for Banks. Tier 1 comprises mainly shareholders' funds, minority interest, after deducting goodwill and other intangible assets. Tier 2 comprises qualifying subordinated loan capital and revaluation reserves. Tier 2 capital cannot exceed 50% of tier 1 capital. Total capital is reduced by deducting investments in subsidiaries that are not consolidated for regulatory purposes.

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Risk weighted assets are determined according to a broad categorisation of the nature of each asset or exposure and counterparty.

£'000	2006	2005
Tier 1	37,543	23,213
Tier 2	11,456	14,620
Less deductions	(828)	(803)
Total capital	48,171	37,030
Total risk weighted assets	211,423	200,640
Risk asset ratio	22.8%	18.5%

The Group's capital position has significantly improved during 2006, largely due to the sale and leaseback transaction. The Group has capacity to raise further Tier 2 capital should this be required.

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

Risk Management

The Group regards the monitoring and controlling of risks as a fundamental part of the management process. Consequently, senior management are involved in the development of risk management policies and in monitoring their application

The principal non-operational risks inherent in the Group's business are credit, counterparty, liquidity and market risks. Credit risk is managed through the Credit Committees of Secure Trust Bank and Arbuthnot Latham & Co, with significant exposures also being approved by the Group Risk Committee. Of the total gross loan book of £159.0 million at 31 December 2006, some £29.9 million represents largely unsecured loans to customers of Secure Trust Bank and £129.1 million represents the commercial lending portfolio, most of which is well secured against cash, property, factored debts or other assets. A provision of £3.5 million (2.2% of total outstandings) is carried against the loan book.

Market risk arises in relation to movements in interest rates, currencies and equity markets. The Group's treasury function operates mainly to provide a service to clients and does not take significant unmatched positions in any markets for its own account. Hence, the Group's exposure to adverse movements in interest rates and currencies is limited to the interest earnings on its free cash and interest rate repricing mismatches.

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Through Arbuthnot Securities the Group is also involved in market-making and underwriting in UK equities. The market-making book is well controlled and is relatively modest in relation to the Group's overall financial resources (net long positions outstanding at 31 December 2006 were £6.8 million). The market-making book is subject to Group-approved limits, both in aggregate and in relation to individual stocks. Outstanding positions are monitored against these limits both intraday and overnight. All significant underwriting transactions are individually approved by the Group Risk Committee.

A conservative approach is also taken to managing the liquidity profile and capital of the Group. Both of the banking subsidiaries operate with liquidity margins and risk asset ratios in excess of the minimum levels set by the regulators.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

1. Basis of presentation

The Group's consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Commission. This means those International Accounting Standards, International Financial Reporting Standards and related Interpretations (SIC-IFRIC interpretations), subsequent amendments to those standards and related interpretations, future standards and related interpretations issued or adopted by the International Accounting Standards Board (IASB) that have been endorsed by the European Union. The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of certain fixed assets and financial assets and financial liabilities held at fair value through profit or loss.

These consolidated financial statements are the second full financial statements prepared by the Group in accordance with IFRS.

2. Consolidation

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

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

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

3. Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments.

4. Foreign currency translation

(a) Functional and presentation currency

All Group entities operate primarily in the United Kingdom and items included in their financial statements are measured using pounds sterling ('the functional currency'). The consolidated financial statements are presented in pounds sterling, which is the Company's functional and presentation currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

5. Interest income and expense

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

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

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

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

6. Fee and commission income

Fees and commissions which are not considered integral to the effective interest rate, are generally recognised on an accrual basis when the service has been provided. Loan commitment fees are deferred and recognised as an adjustment to the effective interest rate on the loan. Commission and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party – such as the issue or the acquisition of shares or other securities or the purchase or sale of businesses – are recognised on completion of the underlying transaction. Asset and other management, advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportioned basis. The same principle is applied for financial planning and insurance services that are continuously provided over an extended period of time.

7. Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale financial assets. Management determines the classification of its investments at initial recognition.

(a) *Financial assets at fair value and through profit or loss*

This category comprises financial assets held for trading.

(b) *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable.

(c) *Held-to-maturity*

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(d) *Available-for-sale*

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Included in available-for-sale are equity investments in special purpose vehicles set up to acquire and enhance the value of commercial properties. These investments are of a medium term nature. There is no open market for these securities and due to the nature of the underlying assets any valuation would contain significant estimation. Consequently, the Directors believe that it is appropriate to hold the investments at cost.

Purchases and sales of financial assets at fair value through profit or loss are recognised on trade-date – the date on which the Group commits to purchase or sell the asset. Loans are recognised when cash is advanced to the borrowers. Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership.

Financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method. Gains and losses arising from changes in the fair value of the ‘financial assets at fair value through profit or loss’ category are included in the income statement in the period in which they arise.

The fair values of quoted investments in active markets are based on current bid prices for long positions and offer prices for short positions (taking into account the size and liquidity of the holding).

8. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

9. Impairment of financial assets

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

after the initial recognition of the asset (a ‘loss event’) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

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

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

10. Intangible assets

(a) *Goodwill*

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group’s share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in ‘intangible assets’. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

(b) *Computer software*

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the basis of the expected useful lives (three to five years).

Costs associated with developing or maintaining computer software programs are recognised as an expense as incurred.

11. Property, plant and equipment

Land and buildings comprise mainly branches and offices and are stated at latest valuation with subsequent additions at cost less depreciation. Plant and equipment is

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, applying the following annual rates, which are subject to regular review:

Freehold buildings	2%
Office equipment	5% to 15%
Computer equipment	20% to 33%
Motor vehicles	25%

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

12. Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash, loans and advances to banks and building societies and short-term highly liquid debt securities.

13. Post-retirement benefits

The Group contributes to a defined contribution scheme and to individual defined contribution schemes for the benefit of certain employees. The schemes are funded through payments to insurance companies or trustee-administered funds at the contribution rates agreed with individual employees.

The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

There are no post-retirement benefits other than pensions.

14. Deferred tax

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

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

15. Borrowings

Borrowings are recognised initially at fair value, being their issue proceeds (fair value of consideration received) net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

16. Share capital

(a) *Share issue costs*

Incremental costs directly attributable to the issue of new shares or options or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds.

(b) *Dividends on ordinary shares*

Dividends on ordinary shares are recognised in equity in the period in which they are approved.

17. Fiduciary activities

The Group commonly acts as trustees and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. These assets and income arising thereon are excluded from these financial statements, as they are not assets of the Group.

The 2006 Annual Report will be posted to shareholders and copies may be obtained from the Company Secretary, Arbuthnot Banking Group PLC, Arbuthnot House, 20 Ropemaker Street, London EC2Y 9AR.