ARROW
GLOBAL

Full-Year Results
For the 12 months ended 31 December 2019

Record free cashflow generation, reduced leverage and €838.0 million fund launch

Arrow Global Group PLC (the “Company” or the “Group”), announces its full-year results for the 12 months ended 31 December 2019.

Key Highlights

- Record £303.7 million investment volumes at a consistent 17.0% net IRR
- Gross Asset Management and Servicing (AMS) income up 5.9% to £140.1 million – 36.4% of gross total income (FY 2018: 32.9%)
- Free cashflow up 13.3% to £261.4 million (FY 2018: £230.7 million)
- Profit before tax increased 28.3% to £51.3m (FY 2018: £40.0m)
- Full year dividend up 3.1% to 13.1p (2018: 12.7p)
- Leverage reduced to 3.4x (FY 2018: 3.7x) – within target range and continuing to reduce
- Underlying ROE of 29.5% (FY 2018: 34.8%) – continues to remain above mid-20s percent target
- Fund Management Business launched with €838.0 million in initial Funds Under Management (FUM) – continue to target €2.0 billion of FUM by the end of 2020

Commenting on today’s results, Lee Rochford, Group chief executive officer of Arrow Global, said:

“The business performed well against its key operating metrics in 2019, with returns in the Investment Business remaining strong and improving margins in our Asset Management and Servicing business leading to a 28.3% increase in profit before tax to £51.3 million. This helped increase free cashflow generation by 13.3% to £261.4 million, allowing us to increase the dividend for the seventh year in a row and finish 2019 within our new lower leverage range of 3.0x-3.5x.”

“We are excited by Arrow’s future prospects and continue to see enormous opportunity to generate strong returns in our chosen markets. The launch of our Fund Management business is transformational for the Group, allowing us to capture more of this opportunity while also growing our capital light earnings. Our initial fundraise of €838.0 million was a milestone in our evolution to become a fully integrated alternative asset manager. We believe we can scale this business significantly over time and are continuing to target total Funds Under Management (FUM)of €2.0 billion by the end of 2020.”

Group financial highlights	31 December 2019	31 December 2018	Change
Core cash collections (£m)	442.3	411.6	7.5%
Third party AMS income (£m)	94.4	91.7	2.9%
Underlying profit before tax (£m)	78.1	82.4	(5.2%)
Basic EPS (p)	20.0	17.0	17.6%
84-month ERC (£m)	1,817.9	1,634.8	11.2%
120-month ERC (£m)	2,035.4	1,972.1	3.2%

The scheduled presentation at the offices of JP Morgan has been cancelled.

Due to the ongoing Coronavirus situation, **Arrow Global's results will now be available remotely via webcast and audio conference call only** at 9.30am UK time. The details for these are included below. **Please note the call number has changed.**

Q&A

A Q&A function will be available via both the conference call and the webcast. If you wish to ask a question via the webcast, you will be able to **email your question directly to the company** dbrowne@arrowglobal.net. Questions asked via the conference call line will be **addressed directly to company management over the phone line.**

Webcast link: https://bit.ly/36JpMPl

Conference call details:

Dial-in details: +44 (0)330 336 9105
Meeting ID: 6314554

Notes:
A glossary of terms can be found at the end of the document. More details explaining the business can be found on the Company's website at www.arrowglobalir.net

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Forward looking statements

This document contains statements that constitute forward-looking statements relating to the business, financial performance and results of the Group and the industry in which the Group operates. These statements may be identified by words such as "expectation", "belief", "estimate", "plan", "target", or "forecast" and similar expressions or the negative thereof; or by forward-looking nature of discussions of strategy, plans or intentions; or by their context. All statements regarding the future are subject to inherent risks and uncertainties and various factors could cause actual future results, performance or events to differ materially from those described or implied in these statements. Such forward-looking statements are based on numerous assumptions regarding the Group's present and future business strategies and the environment in which the Group will operate in the future. Further, certain forward-looking statements are based upon assumptions of future events which may not prove to be accurate and neither the Company nor any other person accepts any responsibility for the accuracy of the opinions expressed in this document or the underlying assumptions. The forward-looking statements in this document speak only as at the date of this presentation and the Company assumes no obligation to update or provide any additional information in relation to such forward-looking statements.

Group chief executive officer's review

Continuing to deliver against key operating metrics

The business performed well against its key operating metrics in 2019. Collections and returns in the Investment business remained strong and investment volumes were at record levels of £303.7 million. Revenues and margins in our Asset Management and Servicing business (AMS) also grew and margins have already reached our medium-term target of mid-20s percent. This solid operational performance helped increase our free cash flow generation by 13.3% to £261.4 million, continuing to allow us to strike the right balance between allocating capital to invest for future growth, paying dividends and deleveraging. We finished the year within our new lower leverage range of 3.0x-3.5x net debt to adjusted EBITDA and continue to target the lower end of this range over time. Profit before tax increased 28.3% to £51.3 million and it is proposed that shareholders receive dividend per share growth of 3.1% to 13.1p – the seventh consecutive year of progressive dividend delivery.

Executing the strategic pivot to a more capital light model

It has been a pivotal year for Arrow as we continue to focus on the business's shift to a more capital light alternative asset management model. Our vision is to be 'The Innovative and Valued Partner in Credit and Asset Management' and to build an alternative investment business that appeals to investors looking access high yielding assets. We have a long track record of investing our own, and our clients', capital into the assets we specialise in and have consistently grown the number of assets we service. The next logical step was to build a Fund Management business where we could invest third-party capital at scale, alongside Arrow's balance sheet on a discretionary basis into our large market opportunity. In December, we announced that we had raised an initial €838.0 million of total Fund Management capital commitments from a diverse range of investors, by both geography and investment style, signalling the first significant step on this journey. We have been hugely encouraged by the amount of investor demand we have encountered and are targeting €2.0 billion of total funds under management (FUM) by the end of 2020. When viewed in the context of our five-year targets, the growth of our Fund Management business reinforces the execution of a successful capital light strategy. This will see us drive gross AMS revenues, which include internal AMS revenues, from the current 36.4% of gross total revenues to towards 50.0%, as well as sustain gross AMS EBITDA margins of at least mid-20s percent, in line with our medium-term targets.

Restructuring the Group to accommodate the integrated asset management model

The Group is already well positioned to manage third-party funds, with many of the required personnel already in place. As a result, we have performed a predominantly internal restructuring process to ensure the Group is positioned to drive the capital light Fund Management strategy. Zach Lewy, our founder, will run the Fund Management business as its chief executive officer, while also remaining chief investment officer of the Group. Oliver Stratton, our Group chief commercial officer, will ensure that we deploy the most effective collections strategies and that our client relationships are well managed. Dave Sutherland, our Group chief operating officer will continue to manage the pan-European operations of the Group. Below the Group executive committee level, we have developed a streamlined reporting structure where senior members of the business with strong industry experience, are leading their respective origination, underwriting, analytics and servicing teams on a country basis. This has been implemented alongside the development of a robust Group-wide governance structure that ensures close alignment between Arrow and the Fund Management business.

A business model built to take advantage of the significant market opportunity

We have been extremely successful in putting in place the building blocks for our Fund Management vision. In recent years, we have positioned ourselves to capture the massive market opportunity we have by building two interdependent business lines – IB and AMS. They serve our wide client franchise and provide each other with off-market deals. We have carefully created this platform by acquiring twelve servicing businesses that enable us to target, and invest in, high margin niches in attractive markets. It is a highly efficient platform that gives us relevance, pricing power and off-market deal flow and I am particularly proud that over 70.0% of our deals were off-market in 2019 – a true testament to our differentiated business model and quite unique in financial services. The 'One Arrow' investment programme ensured that we successfully integrated these businesses, instilling the right culture, oversight, capability and resourcing at the centre necessary to turn our acquisitions into a single pan-European business capable of operating at scale.

Building a differentiated Fund Management business to capture more value

We are confident that we have a unique and compelling market offering for our Fund Management business. Importantly, we do not compete head-on with the large Global and European debt funds that are the most prolific purchasers of assets in this space. Given we originate more niche assets outside of these investors' very large target deal size and concentrated approach, many of these institutions like to co-invest with us on assets that we originate and are our clients. Furthermore, few institutional fund investors have our local presence. The combination of our local, in-market origination teams and our centralised structuring and investment team, combined with regulated, specialist servicing platforms on the ground, means we can originate smaller deals away from competitive auctions at higher returns. When combined with the significant market opportunity offered by our platform, there is clear demand from alternative asset investors to commit capital to our investment strategies.

The impact of rapidly building a Fund Management business and pivoting towards a more capital light model

I'm extremely proud of the transformation the business has undergone in 2019 and the long-term value creation a more capital light model will bring is significant. Executing this pivot has not just involved raising a fund but building of an entirely new business line, at the same time as reconfiguring the rest of the business to support it. As we are still a relatively small business, we have had to prioritise building the Fund Management business over other activities that might have been more accretive to earnings in the short-term, sacrificing that short-term performance for the larger long-term prize. The demand placed on the wider Arrow team in order to achieve this in such a short time has demanded an enormous amount of dedication over and above their day-to-day roles. For this extra effort, I extend my sincere thanks to everyone at Arrow who has been involved.

Arrow's Environmental, Social and Governance (ESG) programme

We recognise that to be successful in the long-term we need to have the right approach in place that ensures that we continue to operate ethically, give back to local communities and help to safeguard the environment for future generations. In 2019, Arrow embarked formally on its ESG journey, forming a dedicated ESG working Group led by our chief operating officer, Dave Sutherland. We are committed to enhancing our ESG performance and are developing a structured roadmap defining our key areas of focus and development. While we already report a set of "Key ESG factors", our roadmap intends to build on this platform, pinpointing specific areas of focus to deliver against internal and external expectations. Arrow's operations are intertwined with stakeholders across the financial services industry. We are therefore extremely focused on ensuring best practice across the entire range of the company's activities. At the consumer level, this means placing strong emphasis on customer treatment and outcomes. We are committed to working closely with relevant

regulatory bodies, including the FCA, to ensure that we continue to deliver best practice and favourable customer outcomes.

Focus on risk management

We have built a robust business that has a strong counter-cyclical element to it and that can generate returns despite weaker economic environments. Execution is key and we are aware of the importance of delivering against our targets and building a Fund Management business that supports capital light revenue growth and deleveraging over the long-term. Regulation is clearly something we focus on and we look to maintain strong relationships with all the regulatory authorities in our countries of operation. While changes in regulation cannot be predicted with certainty, we have been careful to move into markets that we consider have more mature regulatory frameworks. We are also experts in managing our business to ensure the right customer outcomes and to deliver our goal of building better financial futures for all our stakeholders.

No impact from Coronavirus to date but active ongoing monitoring of the situation

We are closely monitoring the developing Coronavirus situation and it is currently too soon to say what impact this will have on the global economy and how long it may last. Our immediate focus is on the health and welfare of our colleagues, as well as ensuring continuity of service for our customers and clients. We have fully instituted our response plans and, at this stage, there has been no detrimental impact on our business. This includes Italy where, in February, collections were running ahead of target. Prudent management of our resources remains a priority and we are taking a cautious view of capital deployment and risk-adjusted pricing in the short term. With over 70% of our deals transacted off-market, we are in a good position to carefully evaluate the risks of any portfolio we underwrite and have flexibility around the timing of investments. Prior experience of operating during a downturn means we expect any impact on cashflows that we do see to be largely timing related rather than due to any ultimate loss. The benefit of having materially reduced our individual transaction sizes in recent years is that we are not over-exposed to any specific portfolio under-performing.

No material impact from Brexit

We continue to monitor the ongoing Brexit situation closely for any impact it may have on the Group's operations. As the majority of our revenues are in Euros and not Sterling, we remain relatively well insulated from any sudden foreign exchange impact related to the UK's departure from the European Union.

A message for the entire Arrow team

Businesses are only as good as their employees and I believe we have built a great team at Arrow. The external recognition we have received this year is testament to this. Our Portuguese servicing business, Whitestar, won 'Best Asset Management Service Provider Portugal 2019', as well as the 'Top Employer Portugal 2020' certification by the Top Employers Institute. Moreover, the Group was shortlisted for three awards at the 2019 Credit Strategy awards. A personal highlight for me has also been travelling round the business as part of our 'smart story' roadshow, celebrating the successes of local teams and outlining the exciting journey the Group is embarking on as it transforms into an alternative asset manager.

Outlook

Arrow remains well positioned to react robustly to the fast-moving macro-economic environment in 2020. Our prudence in refinancing the balance sheet in recent years means we have long liabilities with no debt maturing before 2024. When combined with nearly €1 billion of freshly raised capital committed to our Fund Management business and ready to deploy, we remain optimistic for the business's prospects. We continue to target €2.0 billion of total FUM and welcome the significant operational and funding flexibility this provides moving forward. The market we operate in is large and becoming increasingly more active as European financial institutions are encouraged to deleverage and transfer assets off their balance sheets and into the

capital markets. Our strong origination operation allows us to target the most attractive niches within this asset flow and that continues to translate into the strong returns that are attractive to both us and our fund investors. When I look further ahead over the next three years, I remain confident in our ability to continue to grow our FUM, deploy these funds at attractive IRRs and charge predictable Fund Management and AMS fees for our services. Successfully executing this will mean that the Group's transition to a more capital light business model will continue to accelerate, supporting the key elements of our five-year targets – to double AMS revenues, reduce leverage, increase cost efficiencies and grow returns to shareholders.

Lee Rochford
Group chief executive officer
12 March 2020

Group chief financial officer's review

I joined Arrow in the second half of 2019, and I am excited to be part of the business at such an interesting time as it transitions towards an increasingly capital light model. It was a key year for the Group, as we exerted significant time and resource into executing this pivot, culminating in a successful initial fund raise of third-party capital at notable scale.

Overview

On a statutory basis, profit before tax increased by 28.3% to £51.3 million (2018: £40.0 million), principally driven by the considerably lower level of refinancing charges. There were a number of adjusting items in relation to the launch of Arrow's Fund Management business and strategic simplification programmes throughout the year. It is not anticipated that any significant adjusting items will be incurred in 2020 in relation to these activities. Underlying profit before tax reduced 5.2% to £78.1 million (2018: £82.4 million), primarily driven by lower impairment gains.

As we highlighted at the Interim and Q3 results, we are executing our strategic shift much faster, and at much greater scale, than initially guided at our Capital Markets Day in November 2018, where we set out the Group's five-year strategy. This accelerated speed of execution has meant that we have delayed or cancelled smaller scale strategies in both the Investment business and Asset Management and Servicing business (AMS), which would have yielded greater near-term EPS growth. Instead, we sacrificed these more immediate earnings streams to focus our time and resource on raising discretionary funds at scale at the Group level to accelerate towards our goal to become a fully integrated asset management business. We believe that rapid delivery against this objective will create significant shareholder value. Our strong investment track record appeals to investors seeking attractive yield and in December 2019, we announced a successful inaugural fund raise of €838.0 million of total capital commitments, with a target to manage €2.0 billion of funds under management (FUM) by the end of 2020.

Strong cash generation

One of the key performance metrics for the business is free cash flow generation. Arrow has an excellent track record of generating high levels of free cash flow and 2019 saw this increase by 13.3% to a record £261.4 million (2018: £230.7 million). This was driven by a 7.5% increase in core cash collections to £442.3 million (2018: £411.6 million) from the Investment business and a 2.9% increase in capital light third-party servicing revenues from the Asset Management and Servicing business to £94.4 million (2018: £91.7 million). The increase resulted in a 12.2% improvement in adjusted EBITDA to £330.0 million (2018: £294.0 million). The reconciliation for the year of profit after tax to the cash result, including a reconciliation to adjusted EBITDA, is provided in the additional information section. Adjusted EBITDA is a key indicator for the business's cash flow and allows the Group to monitor the operating performance, cash flow generation and leverage of the Group.

Investment business

Record investment volumes at consistent returns

Throughout 2019, the pricing environment and quantum of opportunities within our markets remained attractive, resulting in higher purchase volumes than previously guided.

In 2019, Arrow committed to investing a record £303.7 million in new portfolios, with £62.9 million of this payment deferred to 2020 (2018: £263.4 million purchased, with £12.0 million deferred). This meant we were able to prudently manage annual leverage in 2019, while also ensuring a robust flow of Investment business revenue into 2020, despite likely reduced balance sheet investment volumes due to the co-invest structure with the Fund Management business. This should help to support earnings while the business transitions to a more capital light model. Despite these record volumes, our returns remained stable at a 17.0% Net IRR and the average deal size onto our own balance sheet reduced by 41.8% to £3.9 million (2018: £6.7 million), further reducing our future concentration risk. The size of our portfolio investment, combined with the co-investment we receive from institutional fund clients, allowed us to continue to grow the funds under management on our servicing platform. This provides both increased Asset Management and Servicing revenues and future purchase opportunities for Arrow's Investment business and Fund Management business as the co-investment owners of those portfolios look to sell into the secondary market. Arrow is extremely well positioned to purchase these portfolios in bilateral trades at attractive returns given our experience of servicing them. The Group continues to take a prudent approach to its underwriting, targeting Net IRRs in the mid-teens.

Core cash collections – record performance with a changing shape expected over time

Core cash collections from our purchased portfolio asset base increased to £442.3 million (2018: £411.6 million), reflecting continued strong operational performance. Core cash collections continue to cumulatively outperform our underwriting expectations. As at 31 December 2019, we have cumulatively collected 104% of our initial underwriting expectation on all portfolios, consistent with the position as at 31 December 2018 reflecting our continued underwriting discipline. The Group continues to purchase an increasing proportion of secured assets, including real estate assets – as highlighted by the move at the 2019 Interim results to independently disclose real estate assets on our balance sheet given their growing materiality. Cash collections from unsecured assets – Arrow's original asset class – tend to be recognised on a more consistent basis quarter to quarter. Increasing cash collections from secured assets – where cash collections are more frequently realised at one point in time, rather than collected gradually over time – will result in greater quarterly variability of cash collections. The advantage of the secured collections profile is that the payback on these assets is generally faster than unsecured, but the timing can move between quarters. We therefore continue to encourage the market not to look at the Group's collections profile on a quarterly basis when performance is better reflected on an annualised basis.

Income – lower levels of revaluations

While core cash collections in the Investment business increased by 7.5%, Investment business income decreased by 9.1% to £244.8 million (2018: £269.4 million). This was principally driven by a significant reduction in upwards revaluations of portfolios held on the balance sheet, along with increased amortisation as cash from secured and real estate assets was realised at a faster rate. Revaluations in 2018 had seen a positive impact from specific litigation work that was undertaken on the back book to drive cash collections from unpaying accounts. Lower levels of revaluations led to a 75.0% reduction in non-cash impairment gains to £12.7 million (2018: £50.7 million).

Arrow's Fund further evolves the purchase model and accounting

Arrow's new Fund is targeting FUM of €2.0 billion by the end of 2020. This includes a 24.9% commitment from Arrow and will form the majority of Arrow's future ordinary course of investment volume.

Moving forward, Arrow will continue to originate and underwrite assets before offering them to the Fund.

If the Fund decides to invest in the asset then Arrow will co-invest capital up to 24.9% of the transaction. This means the Group will likely invest its own balance sheet at a reduced rate in 2020 and onwards compared to recent years, depending on total Fund investment. Over time, this structure also means that an increasing proportion of our assets will be accounted for under fair value, rather than at amortised cost, simplifying our accounting.

Asset Management and Servicing business

Revenue and margins continue to improve

The Group's capital light AMS income has grown significantly in recent years and gross revenues increased by 5.9% to £140.1 million (2018: £132.3 million), constituting 36.4% of total Group revenue. Margins also improved by 3.7ppts. to 23.9%, in line with our 2023 target to grow EBITDA margins in the AMS business to the mid-twenties percent. Third-party fees (excluding internal fees for servicing the Investment business) increased 2.9% to £94.4 million (2018: £91.7 million). Our execution of the pivot to becoming more capital light by building a Fund Management business faster, and at greater scale, than originally planned had an impact on AMS revenue in 2019. Under the original strategy, smaller and faster to execute fund raises were envisaged at the local level in our Norfin and Sagitta businesses in Portugal and Italy, which would have driven AMS fees. More capital intensive strategies had also been assumed in the business plans relating to a number of the servicing businesses that also would have driven nearer term EPS accretion (but also leverage). While this has created a short-term headwind to AMS revenues, the opportunities and benefits that a scaled pan-European Fund Management business offers significantly outweigh this.

The Fund Management business will accelerate the growth and achievement of targets

The launch of Arrow's Fund Management business will continue to fuel the growth we have seen in our AMS business, providing scalable opportunities to grow capital light AMS revenues by offering AMS services to the Fund. Revenue from Fund Management activities will be incorporated in the AMS segment until it becomes large enough to be a separately reported segment. During 2020, the Group plans to present a Fund Management seminar to assist the market in modelling the impact of the Fund Management business on Arrow's performance in the coming years.

The financial benefits of raising this Fund are numerous, including:

- The accelerated achievement of five-year targets
- New capital light earnings streams from market standard management fees and performance fees payable to Arrow as manager of the Fund, resulting in further improvements in the quantum and quality of earnings in the medium-term
- A reduction in leverage due to lower absolute levels of Arrow balance sheet investment compared to recent periods as a result of the co-invest structure with the Fund
- Increased future flexibility around Arrow's capital structure
- A scalable opportunity to grow capital light AMS activities by offering AMS services to the Fund
- Continued attractive returns on capital from Arrow's co-investment alongside the Fund in portfolios

Costs

Focus on efficiency

The collection activity cost ratio improved by 4.1 ppts. to 24.8% (2018: 28.9%) as the Group continued to extract efficiencies within our servicing businesses and reduced the number of lower margin servicing contracts ahead of the expected volume relating to the Fund Management business.

Group overheads reduced from £136.0 million to £123.9 million. This reduction was primarily driven by the release of provisions held against the payment of deferred consideration against recent business acquisitions. This collectively totalled £21.1 million and the release is primarily driven by the accelerated strategic shift towards a capital light business comprising a larger Group level Fund Management offering. Under the previous strategy, management teams were incentivised on projects that no longer form part of the current strategy and their remuneration has been realigned to the Group's Fund Management strategy. Cash overheads remained broadly flat at £97.2 million (2018: £95.0 million).

Total adjusting items related to costs came in at £26.8 million, £3.8 million higher than guided. The cost of implementing the efficiency programme announced at the Interim results – representing an investment of £20.0 million to extract £20.0 million of run rate costs – was £15.2 million. Benefits for the programme have been reforecast at around £17.0 million, representing better returns on the investment than originally planned. The changes are due principally to higher than anticipated new business volumes in the UK. The UK business is already running at the improved efficiency levels we are targeting. Start-up costs relating to the launch of our Fund Management business were £10.1m as the size and scale of the launch of the business exceeded expectations. The remaining £1.5 million relates to the costs associated with the acquisition of Drydens.

All further spend on efficiency savings will be absorbed within business as usual cost, with no further adjusting items relating to this anticipated in 2020.

Finance costs and Tax

Net interest charges of £54.5 million were lower by 18.4% than 2018 as no bond refinancing costs were incurred during 2019. Underlying net interest charges of £54.5 million were up 13.2% on 2018 as a function of the unwind of the discount rate on deferred consideration, higher facility balances in the period and the impact of the adoption of IFRS 16 lease accounting.

The tax charge of £14.0 million represents an effective tax rate of 27.3% (2018: 25.1%) on profit before tax. The effective tax rate on underlying profit is 23.2% (2018: 22.2%) and has increased as we continue to generate a greater amount of the Group's profit from non-UK jurisdictions, which have outperformed our business plan, but which have tax rates in excess of the UK.

Robust balance sheet

Leverage continues to reduce

The Group continues to have significant liquidity headroom, with headroom as at 31 December 2019 of £153.0 million and no debt facilities maturing until 2024. This means that the Group's weighted average duration of its borrowing facilities is 4.8 years – longer than its weighted average asset life – representing a strong position for a financial services business.

On 30 April 2019, the Group further strengthened and diversified its funding structure by completing a securitisation of loan portfolios with a £100.0 million revolving commitment through an asset backed security funding structure at LIBOR + 3.1% per annum. Following this, Arrow's weighted average cost of debt has reduced to 3.7% (2018: 3.9%).

The Group's secured net debt position at the period end was £1,134.2 million (2018: £1,089.2 million) with the increase mainly relating to further portfolio purchases in the year. Leverage reduced to 3.4x (2018: 3.7x) as a result of the continued strong cash generation from the Investment and AMS businesses. We continue to target the lower end of the 3.0x-3.5x leverage range in the medium-term.

As part of the insourcing of litigation operations on 8 April 2019, the Group acquired Drydens Limited, a provider of legal services, broadening Arrow's UK range of servicing capabilities and skills across consumer and commercial litigation, probate and insolvency. The goodwill on acquisition of Drydens Limited amounted to £14.5 million.

Strong returns for shareholders

Statutory return on equity (ROE) was 17.9% (2018: 16.3%) and was impacted by the adjusting items in the period. Underlying ROE, one of the key performance metrics for the Group is 29.5% (2018: 34.8%) and continues to be well in excess of our mid-20s percent through-the-cycle target. Basic EPS is £0.20p (2018: £0.17p) with the increase largely relating to the lower levels of adjusting items incurred during the year.

Underlying basic EPS reduced by 10.8% to £0.33p (2018: £0.37p), impacted by the shift in operational focus referred to above, as well as higher finance costs, a higher tax rate and a one-off non-controlling interest charge.

The Group's dividend policy is to deliver a pay-out ratio of at least 35.0% of underlying profit after tax, reflecting our confidence that the shift towards a capital light business model will increase the scope to return capital to shareholders in the future. The Group proposes to pay an 8.7p final dividend, increasing the total declared and proposed dividends for the year to 13.1p (2018: 12.7p), representing an increase of 3.1% on 2018.

Summary and outlook

The Group has continued to deliver against its priorities in 2019 in what was a pivotal year for the Group's business model. Key operating metrics across the Group performed well and we achieved record free cashflow generation and record investment volumes while also maintaining returns at a consistently attractive level.

In the wider market, the geographic and asset class diversification of the Group means that we continue to find attractive investment opportunities exhibiting returns significantly in excess of our cost of capital. We remain vigilant for early signs of economic distress, particularly regarding COVID-19 and Brexit. However, economic dislocation potentially presents higher return purchasing opportunities and our back book has historically remained robust during distressed scenarios.

The launch of our Fund Management business is transformational for the Group as we continue to transition towards a more capital light integrated asset management model. While profitability was impacted by the speed of the pivot towards this model, and the time and resource that absorbed during the year, it leaves us in a very strong position moving forward. Increased cash generation will continue to enable us to deleverage, while access to such a large pool of third-party capital reduces our dependence on the bond market. While initial start-up costs mean the business will not contribute materially to the Group's profit in 2020, it will begin

to do so from 2021 onwards. We will update the market on the economics of the business and its accelerated impact on Arrow's five-year targets later in 2020.

Matt Hotson
Group chief financial officer
12 March, 2020

Financial statements

Consolidated statement of profit or loss and other comprehensive income

For the year ended 31 December 2019

	Note	2019 £000	2018 £000
Income from portfolio investments at amortised cost	12	199,094	193,932
Fair value gain on portfolio investments at FVTPL	12	32,397	24,745
Impairment gains on portfolio investments	12	12,714	50,727
Income from real estate inventories	12	561	–
Total income from portfolio investments		244,766	269,404
Income from asset management and servicing		94,360	91,661
Profit from sale of property		–	731
Other income		392	–
Total income		339,518	361,796
Operating expenses:			
Collection activity costs	5	(109,798)	(119,041)
Other operating expenses	5	(123,902)	(135,972)
Total operating expenses		(233,700)	(255,013)
Operating profit		105,818	106,783
Finance income		61	76
Finance costs	4	(54,559)	(66,868)
Profit before tax		51,320	39,991
Taxation charge on ordinary activities	6	(14,033)	(10,022)
Profit after tax		37,287	29,969
Other comprehensive income:			
Items that are or may be reclassified subsequently to profit or loss:			
FX translation difference arising on revaluation of foreign operations		(7,077)	1,370
Movement on hedging reserve		161	(241)
Total comprehensive income		30,371	31,098
Profit after tax attributable to:			
Owners of the Company		35,223	29,969
Non-controlling interest		2,064	–
		37,287	29,969
Comprehensive income attributable to:			
Owners of the Company		28,307	31,098
Non-controlling interest		2,064	–
		30,371	31,098
Basic EPS (£)	7	0.20	0.17
Diluted EPS (£)	7	0.19	0.17

Consolidated and statement of financial position

As at 31 December 2019

	Note	Group 2019 £000	Group 2018 £000
Assets			
Cash and cash equivalents		88,765	92,001
Trade and other receivables		75,094	94,206
Portfolio investments – amortised cost	12	932,199	869,056
Portfolio investments – FVTPL	12	169,799	217,974
Portfolio investments – real estate inventories	12	61,626	-
Property, plant and equipment		24,521	7,761
Intangible assets		38,159	44,264
Deferred tax asset		10,759	8,113
Investment in subsidiary undertakings		–	–
Goodwill	8	267,700	262,679
Total assets		1,668,622	1,596,054
Liabilities			
Bank overdrafts	13	1,386	2,696
Revolving credit facility	13	230,963	242,121
Derivative liability		509	502
Trade and other payables	9	223,001	197,657
Current tax liability		7,645	7,915
Other borrowings	13	3,672	11,635
Asset-backed loans	13	84,077	–
Senior secured notes	13	897,875	926,340
Deferred tax liability		17,637	14,930
Total liabilities		1,466,765	1,403,796
Equity			
Share capital		1,769	1,763
Share premium		347,436	347,436
Retained earnings		129,240	116,589
Hedging reserve		(423)	(584)
Other reserves		(280,630)	(273,547)
Total equity attributable to shareholders		197,392	191,657
Non-controlling interest		4,465	601
Total equity		201,857	192,258
Total equity and liabilities		1,668,622	1,596,054

Note – the balance sheet has been re-presented on a reducing liquidity basis and portfolio investments have been split out into their constituent parts. Prior periods have been re-presented accordingly on this basis.

Consolidated and statement of changes in equity

For the year ended 31 December 2019

Group	Ordinary shares £000	Share premium £000	Retained earnings £000	Hedging reserve £000	Own share reserve £000	Translation reserve £000	Merger reserve £000	Total £000	Non-controlling interest £000	Total £000
Balance at 1 January 2018	1,753	347,436	104,511	(343)	(3,291)	7,844	(276,961)	180,949	173	181,122
Profit after tax	–	–	29,969	–	–	–	–	29,969	–	29,969
Exchange differences	–	–	–	–	–	2,572	–	2,572	–	2,572
Recycled to profit after tax	–	–	–	–	–	(1,202)	–	(1,202)	–	(1,202)
Net fair value losses – cash flow hedges	–	–	–	(291)	–	–	–	(291)	–	(291)
Tax on hedged items	–	–	–	50	–	–	–	50	–	50
Total comprehensive income for the year	–	–	29,969	(241)	–	1,370	–	31,098	–	31,098
Share-based payments net of tax	–	–	3,267	–	–	–	–	3,267	–	3,267
Shares issued	10	–	–	–	–	–	–	10	–	10
Repurchase of own shares	–	–	–	–	(2,509)	–	–	(2,509)	–	(2,509)
Dividend paid	–	–	(21,158)	–	–	–	–	(21,158)	–	(21,158)
Dividend paid by NCI	–	–	–	–	–	–	–	–	(43)	(43)
Non-controlling interest on acquisition	–	–	–	–	–	–	–	–	471	471
Balance at 31 December 2018	1,763	347,436	116,589	(584)	(5,800)	9,214	(276,961)	191,657	601	192,258
Impact of adopting IFRS 16	–	–	(947)	–	–	–	–	(947)	–	(947)
Balance post IFRS adjustments at 1 January 2019	1,763	347,436	115,642	(584)	(5,800)	9,214	(276,961)	190,710	601	191,311
Profit after tax	–	–	35,223	–	–	–	–	35,223	2,064	37,287
Exchange differences	–	–	–	–	–	(7,077)	–	(7,077)	–	(7,077)
Recycled to income statement net of tax	–	–	–	7	–	–	–	7	–	7
Net fair value gains – cash flow hedges	–	–	–	187	–	–	–	187	–	187
Tax on hedged items	–	–	–	(33)	–	–	–	(33)	–	(33)
Total comprehensive income for the year	–	–	35,223	161	–	(7,077)	–	28,307	2,064	30,371
Shares issued	6	–	–	–	–	–	–	6	–	6
Repurchase of own shares	–	–	–	–	(6)	–	–	(6)	–	(6)
Share-based payments net of tax	–	–	1,437	–	–	–	–	1,437	–	1,437
Dividend paid	–	–	(23,062)	–	–	–	–	(23,062)	–	(23,062)
Non-controlling interest on acquisition	–	–	–	–	–	–	–	–	1,800	1,800
Balance at 31 December 2019	1,769	347,436	129,240	(423)	(5,806)	2,137	(276,961)	197,392	4,465	201,857

Consolidated and statement of cash flows

For the year ended 31 December 2019

	Note	Group 2019 £000	Group 2018 £000
Net cash generated/(used in) by operating activities	15	20,516	(19,021)
Investing activities			
Purchase of property, plant and equipment		(1,269)	(2,367)
Purchase of intangible assets		(11,830)	(11,077)
Proceeds from disposal of intangible assets and property, plant and equipment		18	3,759
Acquisition of subsidiaries, net of cash acquired		(2,850)	(57,022)
Movements in deferred consideration related to subsidiary acquisitions		(12,004)	(11,612)
Net cash used in investing activities		(27,935)	(78,319)
Financing activities			
Movements in other banking facilities		(7,499)	90,621
Proceeds from senior notes (net of fees)		–	345,847
Redemption of senior notes		–	(203,467)
Early repayment of bond		–	(13,623)
Proceeds from ABS issuing		85,604	–
Increase in non-controlling interest on acquisition		1,800	471
Repayment of interest on senior notes		(35,870)	(36,522)
Repurchase of own shares		(6)	(2,509)
Issue of share capital		6	10
Bank interest received		61	76
Bank and other similar fees paid		(8,452)	(6,248)
Finance lease payments		(5,061)	–
Payment of dividends		(23,062)	(21,201)
Payment of deferred interest		–	(257)
Net cash flow generated by/(used in) financing activities		7,521	153,198
Net increase/(decrease) in cash and cash equivalents		102	55,858
Cash and cash equivalents at beginning of year		92,001	35,943
Effect of exchange rates on cash and cash equivalents		(3,338)	200
Cash and cash equivalents at end of year		88,765	92,001

1. Statutory information

This document does not constitute the Group's statutory accounts for the years ended 31 December 2018 or 31 December 2019 but is derived from those accounts. Statutory accounts for 31 December 2018 have been delivered to the Registrar of Companies, and those for 2019 will be delivered to the Registrar of Companies following the Group's annual general meeting.

The auditor has reported on the 2018 and 2019 accounts; their reports were (i) unqualified, (ii) did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report and (iii) did not contain a statement under section 498 (2) or (3) of the Companies Act 2006.

The financial statements of the Group have been prepared under the historical cost convention. The accounting policies are the same as those that will be disclosed in the annual report and accounts for the year ended 31 December 2019. The financial information included in this preliminary announcement is based on the Group's annual report and accounts for the year ended 31 December 2019, which are prepared in accordance with International Financial Reporting Standards (IFRSs) and in accordance with IFRSs adopted by the European Union. The annual report and accounts for the year ended 31 December 2019 will be posted to shareholders in March 2020. The annual general meeting will take place on 2 June 2020.

2. General information

Arrow Global Group Plc is a company incorporated in England and Wales and is the ultimate parent company of the Group. The address of the registered office is presented on the inside back cover. The financial statements are presented in Pounds Sterling, which is the Company's functional currency. All amounts have been rounded to the nearest thousand except when otherwise indicated.

The Group's principal activity is to identify, acquire and manage secured and unsecured defaulted and non-core loan portfolios and real estate from, and on behalf of financial institutions such as banks, institutional investors and credit card companies.

The Group's financial statements for the year ended 31 December 2019 have been prepared in accordance with IFRS as adopted for use in the EU, and therefore comply with Article 4 of the EU IFRS Regulation. The accounting policies have been applied consistently in the current and prior periods, except for the impact of new accounting standards.

As permitted by section 408 of the Companies Act 2006, a separate income statement and related notes of the Company have not been presented in this annual report and accounts.

3. Segmental reporting

The Group reports under three separate reportable segments. Segmental information has been provided in line with what is reviewed on a regular basis by the chief operating decision maker (CODM), which is the board of directors collectively, as defined in IFRS 8. The principal business categories are as follows:

Investment Business	All portfolio investments that the Group owns, and the income and costs associated with them
Asset Management and Servicing Business	Income and costs associated with managing debt portfolios on behalf of the Group and external servicers. Our Fund Management business is reported under this segment.
Group functions	Costs not directly associated with either the Investment or Asset Management and Servicing Business, but relevant to overall oversight and control of the Group's activities

These segments represent how the Group manages the wider business, and the organisational structure is aligned to these segments. Therefore, this has been deemed to be the appropriate level of disaggregation to provide information to the CODM. Further granularity, such as type of AMS contract, or type of IB portfolio, is not how the business is managed or organised, and hence such further detail has not been presented to the CODM, or in the segmental disclosures.

The intra-segment elimination column below removes charges made from the Asset Management and Servicing Business segment to the Investment Business segment on behalf of the Group for servicing and collection of the Group's portfolio investments. The intra-segment charge is calculated on equivalent commercial terms to charging third parties. For further information on adjusting items, please see the additional information section.

2019	Investment Business £000	Asset Management and Servicing Business £000	Group functions £000	Intra-segment elimination £000	Adjusting items	Total year ended 31 December 2019 £000
Total income	244,766	140,054	392	(45,694)	–	339,518
Collection activity costs	(92,682)	(62,495)	(315)	45,694	–	(109,798)
Gross margin	152,084	77,559	77	–	–	229,720
Gross margin %	62.1%	55.4%				
Other operating expenses excluding depreciation, amortisation and forex	(24,339)	(44,155)	(9,166)	–	(26,789)	(104,449)
EBITDA	127,745	33,404	(9,089)	–	(26,789)	125,271
EBITDA margin %	52.2%	23.9%				
Depreciation, amortisation and forex	–	–	(19,453)	–	–	(19,453)
Operating profit	127,745	33,404	(28,542)	–	(26,789)	105,818
Net finance costs	–	–	(54,498)	–	–	(54,498)
Refinancing costs	–	–	–	–	–	–
Profit before tax	127,745	33,404	(83,040)	–	(26,789)	51,320

2018	Investment Business £000	Asset Management and Servicing Business £000	Group functions £000	Intra-segment elimination £000	Adjusting items	Total year ended 31 December 2018 £000
Total income	269,404	132,306	731	(40,645)	–	361,796
Collection activity costs	(94,617)	(63,989)	–	40,645	(1,080)	(119,041)
Gross margin	174,787	68,317	731	–	(1,080)	242,755
Gross margin %	64.9%	51.6%				
Other operating expenses excluding depreciation, amortisation and forex	(20,715)	(41,613)	(36,733)	–	(22,676)	(121,737)
EBITDA	154,072	26,704	(36,002)	–	(23,756)	121,018
EBITDA margin %	57.2%	20.2%				
Depreciation, amortisation and forex	–	–	(14,235)	–	–	(14,235)
Operating profit	154,072	26,704	(50,237)	–	(23,756)	106,783
Net finance costs	–	–	(48,134)	–	–	(48,134)
Refinancing costs	–	–	–	–	(18,658)	(18,658)
Profit before tax	154,072	26,704	(98,371)	–	(42,414)	39,991

Total income includes income from portfolio investments, asset management and servicing and other income.

2019 Geographical information	UK and Ireland £000	Portugal £000	Italy £000	Netherlands £000	Intra-Group trading £000	Total £000
Total Income	134,066	100,722	84,077	66,347	(45,694)	339,518
Income from AMS contracts with customers	35,261	34,201	34,632	35,960	(45,694)	94,360
Non-current assets	114,110	74,535	82,226	59,509	–	330,380

2018 Geographical information	UK and Ireland £000	Portugal £000	Italy £000	Netherlands £000	Intra-Group trading £000	Total £000
Total Income	139,990	117,971	64,712	79,768	(40,645)	361,796
Income from AMS contracts with customers	30,593	27,153	30,041	44,519	(40,645)	91,661
Non-current assets	82,419	69,686	77,927	84,672	–	314,704

Income from contracts with customers has been disaggregated on a geographical basis, as a similar set of services are provided to customers across the geographies, and therefore this was deemed to be the most appropriate level of disaggregation for this disclosure.

Non-current assets are assets with a useful life of more than one year with the exception of deferred tax which has been excluded.

Gross AMS income includes commission income, debt collection, due diligence, real estate management, advisory fees and intra-Group income for these services.

	2019 £000	2018 £000
Third-party AMS Business income	94,360	91,661
Intra-Group AMS income	45,694	40,645
Gross AMS income	140,054	132,306
Investment Business Income	244,766	269,404
Other income	392	731
Gross income	385,212	402,441

Gross income includes commission income, debt collection, due diligence, real estate management, advisory fees and intra-Group income for Asset Management and Servicing, total income for the Investment Business and other income.

4. Finance costs

	2019 £000	2018 £000
Interest and similar charges on bank loans	8,028	7,168
Interest and similar charges on senior secured notes	38,232	37,458
Interest and similar charges on asset backed securitisation	2,509	–
Interest rate swap and forward exchange contract hedge costs	515	1,568
Lease liability interest	1,395	–
Other interest	3,880	2,016
Bond refinancing costs	–	18,658
Total finance costs	54,559	66,868

In 2018, bond refinancing costs comprised £18,658,000 incurred on the early redemption of the €230 million notes due 2023, of which £13,623,000 was a cash cost related to the call premium. The remaining £5,035,000 was due to a non-cash write-off of related transaction fees, in connection with the 2023 Notes.

5. Collection activity costs, other operating expenses and staff costs

Collection activity costs	Note	2019 £000	2018 £000
External collection costs		31,490	40,417
Staff costs	5.b	42,789	41,100
Direct temp labour		4,807	5,347
Direct operating costs		15,057	13,876
Legal disbursements		14,416	15,348
Other collection activity costs		1,239	2,953
Total collection activity costs		109,798	119,041

Other operating expenses	Note	2019 £000	2018 £000
Staff costs	5.b	56,142	53,346
Other staff related costs		11,591	8,625
Premises		5,401	8,242
IT		13,830	11,520
Depreciation and amortisation		18,435	14,235
Write off of PPE and intangible assets		6,377	–
Net foreign exchange losses/(gains)		1,018	(2)
Acquisition related expenses		1,457	14,717
Deferred consideration release		(21,119)	–
Other operating expenses		30,770	25,289
Total other operating expenses		123,902	135,972

In 2019, £8,817,000 of the other staff-related costs relates to temporary labour, recruitment and training (2018: £7,537,000).

b. Staff costs

	2019 £000	2018 £000
Wages, bonuses and salaries	77,698	73,749
Pension costs	2,833	2,595
Social security costs	12,576	10,126
Share-based payments	1,437	3,267
Staff restructuring	4,387	4,709
	98,931	94,446

6. Taxation

The Group's activities are predominantly UK based. The analysis below therefore uses the UK rate of corporation tax.

a. Amounts recognised in profit and loss	2019 £000	2018 £000
Current tax expense		
Tax charge at standard UK corporation tax rate	14,152	13,328
Changes in estimate related to prior years	1	(849)
Total current tax expense	14,153	12,479
Deferred tax expense		
Origination and reversal of temporary differences	(1,332)	(2,373)
Adjustment in relation to prior years	2,421	(84)
Recognition of previously unrecognised tax losses	(1,209)	–
Total deferred tax expense	(120)	(2,457)
Total income tax expense	14,033	10,022

The differences in the effective tax rate for the period and the standard rate of corporation tax in the UK at 19% (2018: 19%) are as follows:

b. Reconciliation of effective tax rate	2019 £000	2018 £000
Profit before tax	51,320	39,991
Tax charge at standard UK corporation tax rate	9,751	7,598
Effect of tax rates in foreign jurisdictions	2,052	2,606
Expenses not deductible for tax purposes	(358)	768
Changes in corporate tax rates in the year	(1,209)	(17)
Movements in unrecognised deferred tax	1,376	–
Changes in estimate relating to prior years	2,421	(933)
Total income tax expense	14,033	10,022

	2019			2018		
c. Amounts recognised in OCI	Before tax £000	Tax (expense)/benefit £000	Net of tax £000	Before tax £000	Tax (expense)/benefit £000	Net of tax £000
Items that are/may be reclassified to profit or loss						
Movement in hedging reserve:						
Effective portion of changes in fair value	187	(33)	154	(291)	50	(241)
Net amount reclassified to profit or loss	7	–	7	–	–	–
	194	(33)	161	(291)	50	(241)

The rate of UK corporation tax, as enacted under previous Finance Acts, was expected to reduce to 17% from 1 April 2020. Although the UK Government has announced its intention to pass revised legislation under which the rate would remain at 19%, no legislation has been introduced at the balance sheet date and therefore deferred tax balances in relation to the UK have been calculated using a rate of 17%.

In December 2019, a new corporate tax law was enacted in the Netherlands. Consequently, as of 1 January 2020, the corporate tax rate in the Netherlands will be reduced from 25% to 21.7%. This change resulted in a gain of €1,147,000 related to the remeasurement of deferred tax assets and liabilities of the Group's Dutch subsidiaries, being recognised during the year ended 31 December 2019.

Deferred tax

The Group has not recognised a deferred tax asset in respect of £2,560,000 (2018: £859,000) of tax losses carried forward, due to uncertainties over the future utilisation of the losses, including the future profitability of the relevant subsidiaries. These losses may be available for offset against future profits and have no expiry date. There are no unrecognised deferred tax liabilities.

Tax impact of the UK giving notice to withdraw from the EU
Given that the UK has now exited the EU (at 31 January 2020), the Group has considered the impact of Brexit from a tax perspective. The UK is in a transition period until 31 December 2020, during which time all EU directives will continue to be in force. As such, no impact to the Group's tax position is expected in 2020.

It is too soon to know what the arrangements may be with the EU from 1 January 2021 onwards, however the Group does not expect there to be any significant impact from a tax perspective.

Uncertainty over income tax treatments
The current tax liability of £7,645,000 represents the amount of income taxes payable in respect of current and prior year periods, including a provision in relation to uncertain tax positions.

As for most multinationals, the current tax environment is creating increasing levels of uncertainty and the Group is potentially subject to tax audits in many jurisdictions. By their nature, these are often complex and could take a significant period of time to be agreed with the tax authorities. The Group estimates and accrues taxes that will ultimately be payable when reviews or audits by tax authorities of tax returns are completed. The levels of risk arising from tax audits may change as a result of legislative change, tax authority guidance or practice and correspondence with the tax authorities during a specific audit. It is not possible to quantify the impact that such future developments may have on the tax positions taken in the financial statements.

7. Earnings per share (EPS)

	2019 £000	2018 £000
Profit after tax attributable to shareholders	35,223	29,969
Weighted average ordinary shares	175,859	174,939
Potential exercise of share options	4,942	4,515
Weighted average ordinary shares (diluted)	180,801	179,454
Basic earnings per share (£)	0.20	0.17
Diluted earnings per share (£)	0.19	0.17

Refer to table of alternative performance measures in the 'additional information' section for details of underlying earnings per share.

8. Goodwill

	£000
Cost	
At 1 January 2018	155,088
Additions	107,984
Exchange rate differences	1,916
At 31 December 2018	264,988
Additions	14,519
Adjustment of the discounted value of deferred consideration paid for EI	462
Modification to Drydens' opening balance sheets' fair value post-acquisition	693
Exchange rate differences	(10,653)
At 31 December 2019	270,009
Amortisation and impairment	
At 31 December 2018 and 31 December 2019	2,309
Net book value	
At 31 December 2019	267,700
At 31 December 2018	262,679

The following table provides a breakdown of goodwill acquired during the current and prior year:

	£000
Goodwill on acquisition	
At 1 January 2018	155,088
Parr Credit s.r.l.	22,533
Europa Investimenti S.p.A (EI)	48,219
Norfin Investimentos S.A. (Norfin)	31,335
Bergen Capital Management Limited (Bergen)	5,164
Modification to EI opening balance sheet fair value post-acquisition	733
Exchange rate differences	1,916
At 31 December 2018	264,988
Drydens Limited (Drydens)	14,519
Exchange rate differences and goodwill adjustments	(9,498)
At 31 December 2019	270,009

Goodwill acquired in a business combination is allocated, at acquisition, to the CGUs that are expected to benefit from that business combination. The carrying amount of goodwill has been allocated to four aggregated CGUs on the basis that these represent the lowest level at which goodwill is monitored for internal management purposes and are not larger than the single operating segment defined under IFRS 8 (Operating Segments).

Goodwill CGU allocation

In relation to goodwill, the four CGUs identified are UK and Ireland, comprising all Group companies acquired in the Capquest acquisition, Arrow Global Receivables Management Limited, Mars Capital, Bergen and Drydens; Portugal, comprising of all the Group companies acquired in the Whitestar, Gesphone, Redrock and Norfin acquisitions; Benelux, comprising all the Group companies acquired in the Vesting acquisition; and Italy, comprising Zenith, Parr Credit and Europa Investimenti S.p.A. The UK and Ireland, Portugal, Benelux, and Italy CGUs, represent the cash flows generated principally from collections on acquired portfolio investments and management and servicing of third-party debt.

Given the structure and operating model of the Group, it has been deemed appropriate to combine a number of CGUs for impairment testing purposes. This is in line with the Group’s stated strategy of providing a range of services in each geographic region in which the Group operates and represents the lowest level at which the Group’s resources and assets are allocated internally.

The discount rate was a post-tax rate based on the yield of average European 10-year government bonds, adjusted for a risk premium to reflect both the increased risk of investing in equities generally and the systemic risk of the specific CGU.

Five years of cash flows were included in the discounted cash flow model. A long-term growth rate into perpetuity has been determined as the lower of the nominal GDP rates for the countries in which the CGU operates and the long-term compound annual profit before taxes, depreciation and amortisation growth rate estimated by management.

Budgeted profit before taxes, depreciation and amortisation were based on expectations of future outcomes taking into account past experience, adjusted for the anticipated revenue growth. Revenue growth was projected taking into account the average growth levels experienced over the past five years and the estimated growth for the next five years.

The key assumptions described above may change as economic and market conditions change. The Group estimates that likely possible changes in these assumptions would not cause the recoverable amount of any CGU to decline below the carrying amount.

The Group’s goodwill balance has been assessed and no part of the overall balance is deemed to be deductible for tax purposes.

For the purposes of impairment testing, goodwill is allocated to the Group's CGUs as follows:

	2019 £000	2018 £000
UK and Ireland	79,476	64,312
Portugal	69,156	73,061
Benelux	40,824	43,132
Italy	78,244	82,174
	267,700	262,679

An impairment review was carried out at 31 December 2019 that resulted in no impairment to goodwill. The goodwill was assessed to be appropriately stated. The Group tests goodwill annually for impairment, or more frequently if there are indications that goodwill might be impaired. The recoverable amount of the CGUs is determined as the higher of fair value, less cost to sell and value in use. The key assumptions for the value in use calculations were as follows:

	2019				2018			
	UK and Ireland	Portugal	Benelux	Italy	UK and Ireland	Portugal	Benelux	Italy
Discount rate %	8.6%	9.0%	8.2%	9.0%	8.5%	8.9%	8.2%	8.9%
Growth rate used to extrapolate forecasts	2.0%	2.2%	2.0%	1.7%	2.0%	2.2%	2.0%	1.7%

Discount rates

Management estimates discount rates using post-tax rates that reflect current market assessments of the time value of money and the risks specific to the CGUs. Post-tax rates are used alongside post-tax cash flows, as the post-tax discount rate is more readily derived from observable market information. Any potential differences between post-tax discount rates and cash flows and the pre-tax method under IAS 36 have been considered, and no material differences between approaches have been identified.

The starting point for determining the discount rates for each CGU was to use the Group's weighted average cost of capital (WACC) and adjust this for specific factors for each of the CGUs to derive a market participant's rate. The factors took into account the risks inherent in each of the CGUs; such as currency, regulatory, and economic risks and the different operations in the CGUs were also considered.

The Group prepares cash flow forecasts derived from the most recent financial budgets approved by management for the next five years and extrapolates cash flows into perpetuity. The forecasts assume growth rates in collection activity which in turn drive forecast collections and cost figures. These assumptions are in keeping with the directors' expectations of future growth. Appropriate tax rates are applied to the cash flow forecasts for each CGU. The analysis has been prepared using post-tax cash flows and discount rates, as post-tax discount rates can be more readily derived from observable market data. The Group is satisfied that this is materially equal to performing the analysis on pre-tax cash flows and discount rates.

The Group has conducted a sensitivity analysis on the impairment test of the CGU's carrying value. The CGUs would become impaired based on a net post-tax cash flow reduction set out below, or based on an increase in the discount rate noted below:

	A cash flow reduction of	A discount rate increase of
UK and Ireland	58%	11%
Portugal	41%	5%
Benelux	23%	2%
Italy	59%	8%

9. Trade and other payables

Current	2019 £000	2018 £000
Trade payables	15,635	24,133
Deferred consideration on acquisition of subsidiaries	11,332	11,119
Deferred consideration on portfolio investments	62,944	12,031
Taxation and social security	356	163
Due to subsidiary undertaking	–	–
Accruals	35,006	53,954
Other liabilities	19,495	43,781
Lease liability	5,312	–
	150,080	145,181
Non-current		
Trade payables	15,278	3,673
Deferred consideration on acquisition of subsidiaries	19,040	48,803
Other liabilities	20,411	–
Lease liability	18,192	–
	72,921	52,476
Total trade and other payables	223,001	197,657

Deferred consideration on acquisition of subsidiaries has reduced as amounts were repaid in the period, alongside remeasurements of deferred contingent consideration liabilities in the period which reduced their value. Deferred consideration on portfolio investments have increased in the period as significantly more portfolio acquisitions had an element of deferred consideration outstanding at 31 December 2019 than 31 December 2018.

10. Dividends

The following dividends were recognised as distributions to owners during the year ended 31 December 2019:

	2019 £000	2018 £000
Interim dividend 2019: 4.4p per ordinary share (2018: 4.0p)	7,751	7,002
Final dividend 2018: 8.7p per ordinary share (2017: 8.1p)	15,311	14,156
	23,062	21,158

The 2019 interim dividend was declared at 50% of the 2018 final dividend. A final dividend for 2019 has been proposed of 8.7p, bringing the total dividend for the year to 13.1p being 40% of underlying profit after tax. The proposed final dividend is subject to approval at the annual general meeting and has, therefore, not been included as a liability in these financial statements.

The ex-dividend date for the final dividend is 11 June 2020, with a record date of 12 June 2020 and a payment date of 17 July 2020. Shareholders will have the opportunity to elect to reinvest their cash dividend and purchase existing shares in the Company through a dividend reinvestment plan with an election date of 26 June 2020. The dividend has not been recognised as a liability and there are no tax consequences.

11. Related party transactions

Related party balances as at each year end were as follows:

	Key management personnel £000	Total £000
As at 31 December 2019 and 2018:		
Trade	–	–
	–	–

Summary of transactions

Key management, defined as permanent members of the board plus all non-executive directors, were awarded the following compensation for the financial year:

Remuneration	2019 £000	2018 £000
Salaries and performance-related bonus	1,628	2,057
Pension-related benefits	110	128
Share based payments	(306)	426
	1,432	2,611

The number of key management during the year was 6 (2018: 7).

12. Portfolio investments

Split of portfolio investments by period:

	2019 £000	2018 £000
Expected falling due after one year	916,123	841,890
Expected falling due within one year	247,501	245,140
Total	1,163,624	1,087,030

The Group recognises income from portfolios investments in accordance with IFRS 9 from 1 January 2018.

The movements in portfolio investments were as follows:

As at 31 December 2019

	Financial instruments			
	Amortised cost £000	FVTPL £000	Real estate inventories £000	Total £000
As at the year brought forward	869,056	217,974	–	1,087,030
Portfolios purchased during the year	248,470	30,052	25,165	303,687
Transfer between categories	11,483	(55,262)	43,779	–
Collections in the year	(390,734)	(48,034)	(3,543)	(442,311)
Income from portfolio investments at amortised cost	199,094	–	–	199,094
Fair value gain on portfolio investments at FVTPL	–	32,397	–	32,397
Income from portfolio investments - real estate inventories	–	–	561	561
Net impairment gain	12,720	–	(6)	12,714
Exchange and other movements	(4,729)	(7,328)	(4,330)	(16,387)
Portfolio restructure	(13,161)	–	–	(13,161)
As at the year end	932,199	169,799	61,626	1,163,624

Transfer between categories represents positions where the Group has originally held one type of instrument relating to a portfolio, and subsequently increased or changed its interest in the portfolio, leading to the requirement to consolidate the underlying structure onto the Group's balance sheet. This leads to a change in the classification of the portfolio investment held. The 'portfolio restructure' represents the restructure of a leveraged structured deal to move to a de-levered position, and hence change the nature of the holding whilst extinguishing related liabilities. Note that for real estate inventories, which are not financial instruments, the collections figure above is analogous to total sales of inventories, and the net of collections and income from portfolio investments - real estate inventories, is analogous to cost of sales of inventories. Sales of inventories are accounted for as revenue under IFRS 15, as they are not financial instruments, but are presented alongside the other portfolio investments for ease of reference.

As at 31 December 2018

	Financial instruments			
	Amortised cost £000	FVTPL £000	Real estate inventories £000	Total £000
As at the year brought forward	920,578	30,889	–	951,467
Impact of adopting IFRS 9 at 1 January 2018	(93,734)	76,734	–	(17,000)
Brought forward after impact of adopting IFRS 9 opening adjustment	826,844	107,623	–	934,467
Portfolios purchased during the year	169,514	93,836	–	263,350
Portfolio additions from acquired entities	3,339	8,514	–	11,853
Collections in the year	(387,699)	(23,889)	–	(411,588)
Income from portfolio investments at amortised cost	188,862	5,070	–	193,932
Fair value gain on portfolio investments at FVTPL	–	24,745	–	24,745
Net impairment gain	50,727	–	–	50,727
Exchange and other movements	17,469	2,075	–	19,544
As at the year end	869,056	217,974	–	1,087,030

The impact of IFRS 9 shown above is pre-tax. The post-tax impact is £14,000,000. The closing IFRS 9 position has not been shown in the table above, as post-implementation the impact of IFRS 9 is subsumed within the net impairment gain, and within income from portfolio investments at amortised cost.

The estimated future cash flows generated by portfolio investments are the key estimates/judgements in these financial statements. Flexing the expected future gross cash flows by -1/+1% would impact the closing carrying value of the portfolio investments as at 31 December 2019 by £11,020,000 (31 December 2018: £10,870,000). Note that this sensitivity applies only to 'Amortised Cost' and 'FVTPL' portfolio investments, as this is not a critical estimate for Real Estate portfolio assets.

13. Borrowings and facilities

	2019 £000	2018 £000
Senior secured notes net of transaction fees of £ 12,780,000 (2018: £14,769,000)	897,875	926,340
Revolving credit facility net of transaction fees of £3,720,000 (2018: £3,466,000)	230,963	242,121
ABS Loan net of transaction fees of £1,658,000 (2018: £nil)	84,077	–
Bank overdrafts	1,386	2,696
Other borrowings – Non-recourse facility	3,672	11,635
	1,217,973	1,182,792
Total borrowings:		
Amount due for settlement within 12 months	257,500	259,045
Amount due for settlement after 12 months	960,473	923,747

Senior secured notes
On 7 March 2018, Arrow Global Finance Plc issued €285 million floating rate senior secured notes due 2026 (the '2026 Notes') at a coupon of 3.75% over three-month EURIBOR and also issued a £100 million tap of its existing £220 million 5.125% fixed rate notes due 2024. As part of the transaction Arrow Global Finance Plc also redeemed its €230 million 4.75% over three-month EURIBOR floating rate senior secured notes.

The proceeds were used to fund the purchase price for the acquisition of Parr Credit, partially repay drawings under the revolving credit facility and to fund transaction costs and the redemption of the 2023 notes.

In 2018, bond refinancing costs comprised £18,658,000 incurred on the early redemption of the €230 million notes due 2023, of which £13,623,000 was a cash cost related to the call premium. The remaining £5,035,000 was due to a non-cash write-off of related transactions fees, relating to the 2023 notes.

The Euro senior notes and Sterling senior notes are secured by substantially all of the assets of the Group.

Revolving credit facility
On 4 January 2018 the commitments under the revolving credit facility were increased from £215 million to £255 million. The maturity of the facility was extended to 2 January 2023 and the margin reduced to 2.5%.

On 1 November 2018 the commitments under the revolving credit facility were increased from £255 million to £285 million.

On 26 February 2019, the revolving credit facility was extended to 2024, with no change in margin.

Asset backed securitisation
On 30 April 2019, the Group entered into a £100 million non-recourse committed asset backed securitisation facility with an advance rate of 55% of 84-month ERC. On the same date, the Group sold £137 million of ERC into AGL Fleetwood Limited, a wholly owned Arrow Global Group subsidiary, and borrowed an initial amount of £75 million non-recourse funding at Libor plus 3.1% under the facility.

On 31 July 2019, the Group sold a further £44 million of ERC into AGL Fleetwood Limited and subsequently borrowed an additional £25 million non-recourse funding on the same terms under the facility. The facility has a five year term comprising an initial two year revolving period followed by a three year amortising period with an option to extend by one year, subject to lender consent.

14. Acquisition of subsidiary undertaking
Current year acquisitions
a. Drydens Limited (Drydens)
On 8 April 2019, the Group acquired 100% of the share capital of Drydens. Drydens is a provider of legal services, the acquisition of which will broaden the Group's UK range of servicing capabilities and skills across consumer and commercial litigation, probate and insolvency. The total undiscounted consideration for the acquisition is £11,115,000 including deferred and contingent consideration.

Contingent consideration is payable at various times within two years from completion of the transaction upon the satisfaction of three mutually exclusive conditions which are based upon the business achieving certain targets around future volumes and the successful migration of Group accounts. The targets for contingent consideration are not linked to the post-acquisition employment status of the sellers, and is not considered to be a post-employment benefit arrangement with the former owners.

Of the £4,262,000 contingent consideration the gross undiscounted amounts are made up as follows;

Up to £2,000,000 is contingent upon the successful migration of Arrow accounts. The payment range could be anywhere between £0 and £2,000,000 with the final amount to be agreed upon in April 2020.

Up to £2,000,000 is contingent upon the performance of Arrow placed accounts against the jointly agreed business plan. The payment range could be anywhere between £0 and £2,000,000 with the final amount to be agreed upon in April 2021.

£1,000,000 is contingent upon winning Proceeds of Crime Act servicing deal from the UK Government before 8 April 2020. If the deal is not won the payment is forfeited .

Effect of the acquisition

The fair values of the identifiable assets acquired and liabilities assumed are as set out in the table below. Acquisition related costs are expensed in the profit and loss in the reporting period:

	Total £000
Property, plant and equipment	954
Customer intangible	688
Deferred tax asset	146
Cash and cash equivalents	15
Trade and other receivables	1,983
Trade and other payables	(723)
Deferred tax liability	(131)
Current tax liability	(277)
Provisions	(59)
Lease liability	(760)
Loan liability	(6,122)
Total identifiable net liabilities	(4,286)
Goodwill on acquisition	14,519
	10,233
Consideration:	
Cash	2,865
Deferred consideration	3,106
Contingent consideration	4,262
	10,233
Cash impact of acquisition in the period:	
Cash consideration	2,865
Cash and cash equivalents acquired	(15)
	2,850

An intangible asset of £688,000 has been recognised at acquisition, being the fair value after appropriate discounting, of expected cash flows arising from existing customer relationships. The gross contractual outstanding amounts of 'trade and other receivables' was materially equal to their carrying amount, with no material balances not expected to be collected upon.

Goodwill of £14,519,000 was created as a result of this acquisition. The primary reason for the acquisition was to broaden the Group's range of servicing capabilities in the UK.

In the period from acquisition to 31 December 2019, Drydens contributed income of £3,650,000 and profit after tax contribution of £1,165,000 to the consolidated results for the period. If the acquisition had occurred on 1 January 2019, Group total income would have been higher by an estimated £1,167,000 and profit after tax would have been lower by an estimated £24,000.

15. Notes to the statement of cash flows

	Group	Group	Company	Company
	2019	2018	2019	2018
	£000	£000	£000	£000
Profit after tax	37,287	29,969	11,897	154,298
Adjusted for:				
Collections in the year	442,311	411,588	–	–
Income from portfolio investments	(199,655)	(193,932)	–	–
Fair value gain on portfolios	(32,397)	(24,745)	–	–
Net impairment gain	(12,714)	(50,727)	–	–
Deferred consideration release	(21,119)	–	–	–
Depreciation and amortisation	18,435	14,235	–	–
Loss/(profit) on write off and disposal of property, plant and equipment	1,419	(731)	–	–
Loss on write off and disposal of intangible assets	5,766	508	–	–
Net interest payable	53,103	66,792	–	–
Lease liability interest	1,395	–	–	–
Foreign exchange gains	1,018	(2)	–	–
Equity settled share-based payment expenses	1,437	3,267	–	–
Tax expense	14,033	10,022	–	–
Operating cash flows before movement in working capital	310,319	266,244	11,897	154,298
Decrease/(increase) in other receivables	15,800	(28,132)	26	(91)
Decrease/(increase) in amounts due to/from subsidiary undertakings	–	–	10,858	(130,029)
Increase/(decrease) in trade and other payables	12,120	15,645	291	198
Cash generated by operations	338,239	253,757	23,072	24,376
Income taxes and overseas taxation paid	(14,036)	(9,428)	–	(720)
Net cash flow from operating activities before purchases of portfolio investments	324,203	244,329	23,072	23,656
Purchase of portfolio investments	(303,687)	(263,350)	–	–
Net cash generated/(used in) by operating activities	20,516	(19,021)	23,072	23,656

Additional information (unaudited)

'Underlying profit after tax' is considered to be a key measure in understanding the Group's ongoing financial performance.

Adjusting items are those items, as determined by management, that by virtue of their size, nature or incidence (i.e. outside the normal operating activities of the Group) are not considered to be representative of the ongoing performance of the Group and these items are excluded from underlying profit after tax. Judgement has been applied in determining which items are considered as 'adjusting' for the purpose of this metric.

	31 December 2019	31 December 2018				
	Reported £000	Adjustments £000	Underlying £000	Reported £000	Adjustments £000	Underlying £000
Continuing operations						
Income	339,518	–	339,518	361,796	–	361,796
Operating expenses						
Collection activity costs	(109,798)	–	(109,798)	(119,041)	1,080	(117,961)
Other operating expenses	(123,902)	26,789	(97,113)	(135,972)	22,676	(113,296)
Total operating expenses	(233,700)	26,789	(206,911)	(255,013)	23,756	(231,257)
Operating profit	105,818	26,789	132,607	106,783	23,756	130,539
Finance income	61	–	61	76	–	76
Finance costs	(54,559)	–	(54,559)	(66,868)	18,658	(48,210)
Share of profit in associates	–	–	–	–	–	–
Underlying profit before tax	51,320	26,789	78,109	39,991	42,414	82,405
Taxation charge on underlying activities	(14,033)	(4,056)	(18,089)	(10,022)	(8,275)	(18,297)
Underlying profit after tax before non-controlling interest	37,287	22,733	60,020	29,969	34,139	64,108
Non-controlling interest	(2,064)	–	(2,064)	–	–	–
Underlying profit after tax	35,223	22,733	57,956	29,969	34,139	64,108
Underlying Basic EPS (£)			0.33			0.37
Underlying tax rate			23.2%			22.2%

2019 adjusting items

Of the £26,789,000 adjusting items total in 2019, £15,220,000 relates to the Group's strategic simplification programmes, £10,112,000 relates to the expansion of the Group's Fund Management business, and £1,457,000 relates to costs incurred to facilitate the acquisition of Drydens Limited.

The Group's simplification programmes are considered to be adjusting items, as they comprise a series of actions which have incurred costs in the current period, which are not expected to recur in future periods. As such, they are not considered as part of the underlying performance of the Group. Of the £15,220,000 of spend related to the Group's strategic simplification programmes:

- £6,398,000 relates to the accelerated write-off and decommissioning of IT-related intangible assets
- £3,459,000 relates to the costs of exiting employees from certain functions across the Group, including staff restructuring
- £2,641,000 relates to the costs of exiting particular sites and small businesses lines across the Group
- £1,567,000 relates to employee costs (including allocations of existing employees' costs) of executing and delivering the programme
- £1,155,000 relates to third-party advisory costs and other costs of delivering the programme

The costs incurred in the expansion of the Group's Fund Management business are considered to be adjusting items, as a lot of this activity is being undertaken for the first time in the period, but is not expected to recur in future periods. As such, this expenditure is not considered representative of the underlying performance of the Group. Of the £10,112,000 of spend related to the expansion of the Group's Fund Management business:

- £6,897,000 relates to third-party advisory fees and sundry materials costs
- £3,215,000 relates to employee costs (including allocations of existing employees' costs) of working on this project

2018 adjusting items
Collection activity cost adjusting items relate to 'One Arrow' costs incurred during 2018.

Of the £42,414,000 adjusting items total in 2018, £18,658,000 related to bond refinancing costs, £14,717,000 were acquisition related costs, and £9,039,000 related to 'One Arrow' costs.

Of the £18,658,000 related to bond refinancing costs:

- £13,623,000 cost related to the call premium, and
- £5,035,000 due to a non-cash write-off of related transaction fees, in connection with the 2023 Notes.

Of the £14,717,000 acquisition related costs:

- £3,068,000 related to acquisitions in the current year, and
- £11,649,000 related to contingent consideration payments on previous periods' acquisitions.

The remaining £9,039,000 related to 'One Arrow', which was a Group-wide programme which began in 2017 and came to an end in 2018, and included the development of a revised governance structure, office consolidations and IT/change investment across the Group. Given the aggregate size and nature of this Group-wide transformation programme, these costs have been presented as profit adjusting items as they are considered to warrant separate presentation. The Group expects this will drive longer term benefits into future periods.

IFRS to cash result reconciliations
We provide two reconciliations between reported IFRS profit and cash measures. The first looks at the movement in our portfolio investments compared to the movements in the ERC – the gross cash value of the portfolio before it is discounted to present value for inclusion in the reported results. The second reconciles the reported profit for the year to the cash result. For completeness we also separate out other adjusting items. A number of the terms referred to in this section are defined in the glossary.

As part of the Group's Investment Business, we acquire portfolios and turn these into regular, predictable and long-term cash flows. This predominantly involves high volumes of low value collections from customers, and therefore we use analytical models to estimate cash flows we expect at an individual account level. The output of these account level forecasts is aggregated to a portfolio and then into the Group's total ERC.

When we purchase portfolio investments, we recognise them in the statement of financial position at the purchase price in accordance with IFRS. In terms of the equivalent cash measure, we add the portfolio ERC to the Group ERC at the point of purchase. We quote both 84-month and 120-month ERC forecasts as key performance measures for the business.

Collections from portfolios can extend beyond 15 years; however, we only include 84 months of cash flow in assessing the majority of our portfolio investments. As we progress through the months of each year, we roll forward the ERC forecast, meaning we always have 84 months of expected cash flow from our portfolios recognised on the statement of financial position.

Due to the nature of our business, actual collections on portfolio investments will not perform exactly as initially forecast and, each half year, we review performance against collections experience and update the ERC forecast where appropriate. This updated cash flow forecast, discounted at the applicable rate is the year-end carrying value of the portfolio investments. This movement of the portfolio investments is reflected as revenue in the income statement. The size of the portfolio asset, associated ERC and cash collections in the year are therefore all key drivers to the result we report.

As we collect on our portfolios, the statement of financial position value, ERC and income we receive decreases over time. Based upon our target returns that we expect to invest at, we are able to calculate a replacement rate, or maintenance capex, being the amount we need to invest to hold the Group's total portfolio value constant. During a year, if we invest higher than the replacement rate at target returns, the income from debt purchase grows. The replacement rate is a key driver to the cash result the business generates.

Movement in portfolio investments under IFRS reconciled to cash ERC

Total portfolio investments	IFRS £000	ERC 84-month £000	ERC 120-month £000	
Brought forward	1,087,030	1,634,786	1,972,130	ERC brought forward
Portfolios acquired during the year[1]	303,687	479,783	513,766	ERC acquired during the year
Collections in the year[2]	(442,311)	(442,311)	(442,311)	Collections in the year
Income from portfolio investments at amortised cost[3]	199,094	–	–	
Fair value gain on portfolio investments at FVTPL[4]	32,397	–	–	
Net impairment gain[5]	12,714	–	–	
Net income from real estate inventories	561	–	–	
Restructure	(13,161)	–	–	
Exchange and other movements	(16,387)	–	–	
		145,682	(8,164)	ERC roll forward and reforecast[6]
		1,817,940	2,035,421	ERC carried forward
Effect of discounting[7]		(654,316)		
Carried forward 31 December 2019	1,163,624	1,163,624		

1. Portfolios acquired in the year are added to the statement of financial position carrying value of portfolio investments at their initial purchase price. The undiscounted forecast of estimated remaining collections is included in the ERC.
2. Collections made in the period are deducted from both the IFRS carrying value of portfolio investments and ERC.
3. Income on portfolio investments at amortised cost is calculated with reference to the effective interest rate (EIR) of the portfolio. This income is recognised after taking account of new portfolios, collections, updated ERC forecast, disposals and any FX impacts.
4. Fair value gain on portfolio investments at FVTPL represents net increases to carrying values, discounted to calculate the market interest rate of portfolio investments held at FVTPL as a result of reassessments to their estimated future cash flows.
5. Net impairment gain represents net increases to carrying values, discounted at the credit-adjusted EIR rate, of portfolio investments held at amortised cost as a result of reassessments to their estimated future cash flows.
6. The ERC roll forward and reforecast reflects management's updated estimation of future collections. It takes account of updated information on specific portfolios, the latest exchange rate and rolls forward the 84-month and 120-month forecast collection period.
7. Under IFRS, the carrying value of portfolio investments primarily includes 84-months of discounted cash flows, however we expect to see cash flows beyond this period and report a 120-month ERC also, as is customary for the industry.

Reconciliation of profit after tax to the cash result

	Reported profit £000	Adjusting items[4] £000	Underlying profit after tax £000	Other items £000	Cash Result £000	
Income from portfolio investments	199,655	–	199,655	242,656	442,311	Collections in the period
Fair value gains portfolio investments at FVTPL	32,397	–	32,397	(32,397)	–	
Net impairment gains	12,714	–	12,714	(12,714)	–	
Income from Asset Management and Servicing	94,360	–	94,360	–	94,360	Income from Asset Management and Servicing
Other income	392	–	392	–	392	
Total income[1]	339,518	–	339,518	197,545	537,063	
Total operating expenses	(233,700)	26,789	(206,911)	(102)[2]	(207,013)	Cash operating expenses
Operating profit	105,818	26,789	132,607	197,443	330,050	Adjusted EBITDA[5]
Net financing costs	(54,498)	–	(54,498)	12,936[3]	(41,562)	
Profit before tax	51,320	26,789	78,109	210,379	288,488	
Taxation charge on ordinary activities	(14,033)	(4,056)	(18,089)	4,053	(14,036)	
Profit after tax	37,287	22,733	60,020	214,432	274,452	
					(13,099)	Capital expenditure
					261,353	Free Cash Flow[7]
					(176,064)	Replacement rate[6]
					85,289	Cash result[4]

1. Total income is largely derived from income from portfolio investments as explained in 3 above, plus income from asset management and servicing being commission on collections for third-parties and fee income received. The non-cash items add back loan portfolio amortisation to get to core collections. Amortisation reflects a reduction in the statement of financial position carrying value of the portfolio investments arising from collections, which are not allocated to income. Amortisation plus income from portfolio investments equates to core collections
2. Includes non-cash items including depreciation and amortisation, share-based payment charges and FX
3. Non-cash amortisation of fees and interest
4. The cash result is viewed on an underlying basis which excludes certain items. These items have been excluded to provide a more comparable basis for assessing the Group's performance between financial periods.
5. Adjusted EBITDA is a key driver to the cash result. This measure allows us to monitor the operating performance of the Group. See additional information provided for detailed reconciliations of adjusted EBITDA
6. Replacement rate is the rate of portfolio investments purchases, at our target portfolio returns, required during the next 12 months to maintain the 84-month ERC as at 31 December 2019
7. Free cash flow is the adjusted EBITDA after the effect of capital expenditure and working capital movements

Reconciliation of net cash flow to adjusted EBITDA	31 December 2019 £000	31 December 2018 £000
Net cash flow used in operating activities	20,516	(19,021)
Purchases of portfolio investments	303,687	263,350
Purchase price adjustment relating to prior year	–	–
Income taxes paid	14,036	9,428
Working capital adjustments	(27,920)	12,487
Amortisation of acquisition and bank facility fee	127	273
Proceeds from sale of property	–	3,759
Dividends and income from associates	–	–
Write off and disposal of intangible asset and property plant and equipment	(7,185)	–
Acquisition costs	–	14,717
'One Arrow' costs	–	9,039
Adjusting items	26,789	–
Adjusted EBITDA	330,050	294,032
Reconciliation of core collections to adjusted EBITDA		
Income from portfolio investments including fair value and impairment gains	244,766	269,404
Portfolio amortisation	197,545	142,184
Core collections (includes proceeds from disposal of portfolio investments)	442,311	411,588
Other income	94,752	91,661
Operating expenses	(233,700)	(255,013)
Depreciation and amortisation	18,435	14,235
Foreign exchange (gains)/losses	1,018	(2)
Amortisation of acquisition and bank facility fees	127	273
Proceeds from sale of property	–	3,759
Deferred consideration release	(21,119)	–
Disposal of intangible asset	–	508
Share-based payments	1,437	3,267
Acquisition costs	–	14,717
'One Arrow' costs	–	9,039
Adjusting items	26,789	–
Adjusted EBITDA	330,050	294,032
Reconciliation of operating profit to adjusted EBITDA		
Profit after tax for the year	37,287	29,969
Underlying finance income and costs	54,498	48,134
Taxation charge on ordinary activities	14,033	10,022
Share of profit on associate	–	–
Gain on sale of associate	–	–
Adjusting finance costs	–	18,658
Operating profit	105,818	106,783
Portfolio amortisation	197,545	142,184
Depreciation and amortisation	18,435	14,235
Foreign exchange gains	1,018	(2)
Profit on sale of property	–	(731)
Amortisation of acquisition and bank facility fees	127	273
Proceeds from sale of property	–	3,759
Share-based payments	1,437	3,267
Disposal of intangible asset	–	508
Deferred consideration release	(21,119)	–
Acquisition costs	–	14,717
'One Arrow' costs	–	9,039
Adjusting items	26,789	–
Adjusted EBITDA	330,050	294,032

Glossary of Key Performance Indicators (KPIs)

A description of the Group's KPIs relating to clients, financial position and performance is set out in the 'additional information' section.

The Group's KPIs are used throughout this document to help explain the performance of the business. This glossary sets out why each of these KPIs are important to the Group.

84-month ERC

The 84-month ERC means the Group's estimated remaining collections on portfolio investments (of all classifications) over the next 84-months, representing the expected future core collections on portfolio investments during this period. The expected future collections are calculated at the end of each month, based on the Group's proprietary ERC forecasting model, as amended from time to time. The 84-month ERC is particularly important for the Group as it shows the forecast cash inflows over the same period that is used to calculate the future cash flows of the Group's portfolio investments.

120-month ERC

The 120-month ERC means the Group's estimated remaining collections on portfolio investments (of all classifications) over the next 120-months, representing the expected future core collections on portfolio investments during this period. The expected future collections are calculated at the end of each month, based on the Group's proprietary ERC forecasting model, as amended from time to time. The 120-month ERC is an important metric for the Group as in some cases the collection profile of a particular portfolio can extend beyond 84-months, and as such, the 120-month ERC gives a more holistic view of potential remaining collections from the Group's portfolio investments.

Leverage ratio

The Group's leverage ratio is calculated by dividing the secured net debt outstanding at the end of the period by the LTM (12 months' rolling average) Adjusted EBITDA. The leverage ratio presented in the Annual report and Accounts is calculated on the same basis as the financial covenant stipulated within the Group's revolving credit facility provided by a syndicate of banks. As at 31 December 2019, the actual leverage was 3.4 times against the bank covenant of 4.4 times and a management target of between 3.0 to 3.5 times.

Funds under management (FUM)

The funds under management figure for the Group represents the current gross discretionary capital that the Group is responsible for managing in some capacity, including any of its own capital which it has committed to invest alongside third parties. FUM is an important metric used to understand the scale of the Group's Fund Management business and how this compares to others in the market.

Net IRR

The net Internal Rate of Return (Net IRR) is calculated by taking the cumulative expected returns from a portfolio investment (or group of portfolio investments) and discounting these at a rate that makes the net present value of such returns equal to the price paid for the investments(s). This is an important metric for the business as it is a measure of the returns which are being generated by investing the Group's own capital into new purchases in the period.

Glossary of alternative performance measures

APM	Definition	Why is the measure used?
Adjusted EBITDA	The Adjusted EBITDA figure represents the Group's earnings before interest, tax, depreciation and amortisation, adjusted for any non-cash income or expense items. Any impact on EBITDA of 'adjusting items' (see below for definition) is also removed for the purposes of calculating adjusted EBITDA.	Adjusted EBITDA is an approximate measure of the underlying cash EBITDA of the Group. In addition, the leverage ratio of the Group is calculated as the ratio of secured net debt to Adjusted EBITDA. This makes the Adjusted EBITDA figure a key component of this metric, which also features in the Group's banking covenant measures.
Adjusting items	Adjusting items are those items that by virtue of their size, nature or incidence (i.e. outside the normal operating activities of the Group) are not considered by the Board to be representative of the ongoing performance of the Group and are therefore excluded from underlying profit after tax.	Adjusting items are used to calculate various 'underlying' metrics, to provide information about the performance of the Group without the impact of such items included.
Cash result	The cash result represents current cash generation on a sustainable basis and is calculated as Adjusted EBITDA less cash interest, income taxes and overseas taxation paid, purchase of property, plant and equipment, purchase of intangible assets and average replacement rate.	The cash result provides a measure of how much cash the Group generates across the reporting period which it can utilise on a discretionary basis, whilst maintaining the size of its current investment portfolio.
Core collections/collections	Core collections or collections represent cash collections on the Group's existing portfolio investments including ordinary course portfolio sales and put-backs.	Core collections is a key metric as it represents the Group's most significant cash inflow. It is also a key component of adjusted EBITDA which is used to calculate the Group's leverage position.
Leverage	Leverage is calculated as secured net debt over Adjusted EBITDA.	The leverage metric provides an indication of the level of indebtedness of the Group, relative to its underlying cash earnings.
Underlying profit before/after tax	Underlying profit before/after tax means profit for the period after tax adjusted for the pre-tax/post-tax effect of certain adjusting items, as defined above, as well as adjustments to remove profits due to non-controlling interests.	The Group presents underlying profit before/after tax because it excludes the effect of items which are not considered representative of the Group's ongoing performance, on the Group's profit or loss for a period.
Underlying return on equity	Underlying return on equity represents the ratio of underlying profit after tax, to average shareholder equity over a 12-month period.	Underlying return on equity provides a measure of the underlying returns generated by the Group on the average shareholder capital deployed in the period.
Underlying basic EPS	Underlying basic EPS represents earnings per share based on underlying profit after tax, excluding any dilution of shares.	Underlying basic EPS provides a metric of underlying profit after tax on a per-share basis, which is a consideration in the valuation of individual shares, amongst other items.

Glossary of terms

'AMS' Income from Asset Management and Servicing (AMS) contracts. The Group recognises revenue when it satisfies a performance obligation related to a service it has undertaken to provide to a customer.

'APM' means alternative performance measure.

'Average net assets' is calculated as the average quarterly net assets from 2018 to 2019 as shown in the quarterly and half yearly statements. In comparative periods this was calculated as the average annual net assets.

'CGU' means cash-generating unit.

'Collection activity costs' represent the direct costs of collections related to the Group's portfolio investments, such as salaries, commissions paid to third-party outsourced providers, credit bureau data costs and legal costs associated with collections.

'Cost income ratio' see 'total cost-to-income ratio'.

'Cost-to-collect ratio' is collection activity costs over total income.

'Creditors' means financial institutions or other initial credit providers to consumers, certain of which entities choose to sell paying accounts or non-paying accounts receivables related to debt purchasers (such as the Group).

'CSA' means Credit Services Association.

'Customers' means consumers whose unsecured loan obligation is owed to the Group as a result of a portfolio purchase made by the Group.

'Defaulted debt' means a debt where a customer has breached the repayment terms governing that debt such that it is unlikely to be paid. Under the Consumer Credit Act 1974 there are specific legal obligations which require a customer to be sent the relevant statutory default notice(s) after which the customer's agreement may ultimately be terminated. Other types of debts may also be defined as defaulted in the event that they remain unpaid for a period of 90 days or more, if there is not an acceptable arrangement in place to bring the account back up to date, in which case the creditor or lender may reasonably believe that the relationship has broken down. Under the Data Protection Act 1990 it is a requirement that any organisation seeking to register a default with a credit reference agency must also send a notice of intention to file a default, this notice is very similar in nature to that required under the Consumer Credit Act both of which give the debtor 28 days to bring the account back up to date before action is taken.

'Diluted EPS' means the earnings per share whereby the number of shares is adjusted for the effects of potential dilutive ordinary shares, options and LTIPs.

'DSBP' means the Arrow deferred share bonus plan.

'EBITDA' means earnings before interest, taxation, depreciation and amortisation.

'EBT' means employee benefit trust.

'ECL' means expected credit losses.

'EIR' means effective interest rate (which is based on the loan portfolio's gross internal rate of return) calculated using the loan portfolio purchase price and forecast gross ERC at the date of purchase. On acquisition, there is a short period that is required to determine the EIR, due to the complexity of the portfolios acquired.

'EPS' means earnings per share.

'ERC roll forward' relates to additional cash flows from rolling the asset life on all portfolios to seven years from the date of ERC, including the impact of any foreign exchange movement and the impact of reforecast in the period.

'FCA' means the Financial Conduct Authority.

'Free cash flow' or 'FCF' means Adjusted EBITDA after the effect of capital expenditure and working capital movements.

'FVTPL' – Financial instruments designated at fair value with all gains or losses being recognised in the profit or loss.

'FUM' means funds under management.

'GFC' means global financial crisis.

'Gross money multiple' means core collections to date plus the 84-month gross ERC or 120-month gross ERC, as applicable, all divided by the purchase price for each portfolio, excluding REO purchases and purchase price adjustments relating to asset management fees.

'IB' means the Investment Business.

'IFRS' means EU adopted international financial reporting standards.

'Income from AMS' includes commission income, debt collection, due diligence, real estate management, advisory fees and intra-group income for these services.

'IPO' means initial public offering.

'Loan to value' or 'LTV ratio' represents the ratio of 84-month ERC to net debt.

'LTIP' means the Arrow long-term incentive plan.

'NCI' means non-controlling interest.

'Net debt' means the sum of the outstanding principal amount of the senior secured notes, interest thereon, amounts outstanding under the revolving credit facility and deferred consideration payable in relation to the acquisition of portfolio investments, less cash and cash equivalents. Net debt is presented because it indicates the level of debt after taking out of the Group's assets that can be used to pay down outstanding borrowings, and because it is a component of the maintenance covenants in the revolving credit facility. The breakdown of net debt for the year ended 31 December 2019 is as follows:

	2019 £000	2018 £000
Cash and cash equivalents	(88,765)	(92,001)
Senior secured notes (pre-transaction fees net off)	902,656	935,567
Revolving credit facility (pre-transaction fees net off)	234,683	245,587
Asset-backed loans (pre-transaction fees net off)	85,604	–
Secured net debt	1,134,178	1,089,153
Deferred consideration – portfolio investments	62,944	12,031
Deferred consideration – business acquisitions	30,372	59,922
Senior secured loan notes interest	7,999	5,542
Asset-backed loan interest	131	–
Bank overdrafts	1,255	2,696
Other borrowings	3,672	11,635
Net debt	1,240,551	1,180,979

'Net IRR' means the internal rate of return net of cost to collect.

'NPL' means non-performing loan.

'OCI' means other comprehensive income.

'Off market' means those loan portfolios that were not acquired through a process involving a competitive bid or an auction like process.

'Paying account' means an account that has shown at least one payment over the last three months or at least two payments over the last six months.

'Pay-out ratio' represents the total amount of dividends paid out divided by the underlying profit after tax.

'Portfolio amortisation' represents total collections plus income from portfolio investments.

'POCI' means purchased or originated credit impaired

'Portfolio investments' are on the Group's statement of financial position and represent all debt portfolios that the Group owns at the relevant point in time. A portfolio comprises a group of customer accounts purchased in a single transaction.

'RCF' means revolving credit facility.

'Replacement rate' means the level of purchases needed during the subsequent year to maintain the current level of ERC.

'ROE' means the return on equity as calculated by taking profit after tax divided by the average equity attributable to shareholders. Average equity attributable is calculated as the average quarterly equity from 2018 to 2019 as shown in the quarterly and half yearly statements. In the comparative period this is calculated as the average annual equity attributable.

'Secured net debt' see table in 'net debt' definition.

'SIP' means the Arrow all-employee share incentive plan.

'SMART' means aligning the leadership teams across the Group around our Mission, Vision and Strategy.

'SME' means small and medium-sized enterprises.

'SPPI' means solely payments of principal and interest.

'TCF' means the treating customers fairly FCA initiative.

'Total cost-to-income ratio' is total operating expenses over total income.

'Translation reserve' comprises all foreign currency differences arising from the translation of the financial statements of foreign operations.

'TSR' means total shareholder return.