Schroders

Pillar 3 disclosures

31 December 2019

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Overview

Purpose

This document sets out the consolidated Pillar 3 disclosures for Schroders plc (Schroders or the Group) as at 31 December 2019. It fulfils the regulatory disclosure requirements of the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD) referred to collectively as CRD IV. CRD IV has the effect of implementing the international Basel III framework in the European Union (EU) for banks, building societies and investment firms. It is supplemented by technical standards issued by the European Banking Authority (EBA).

The capital and risk disclosures required under Pillar 3 are produced annually and published alongside the Schroders plc Annual Report and Accounts (Annual Report and Accounts). These disclosures are made as at 31 December 2019, which is Schroders plc's accounting reference date. They are not subject to audit and have been produced solely for the purposes of satisfying the Pillar 3 regulatory requirements. Additional relevant information can be found in the Group's Annual Report and Accounts, which is available on the Schroders corporate website (www.schroders.com/ir).

Summary capital position and requirements

Under CRD IV, institutions are required to meet the following own funds requirements: a common equity Tier 1 (CET1) capital ratio of 4.5%, a Tier 1 (T1) capital ratio of 6% and a total capital ratio of 8%. The Group's regulatory capital consists entirely of CET1 capital. The Group's capital ratio is calculated as regulatory capital divided by the total risk exposure and the Group's key regulatory metrics are shown in table 1. As at 31 December 2019, the Group complied with all externally imposed regulatory capital requirements.

Table 1: Key regulatory metrics

	Total regulatory capital £m	Total risk exposure £m	Capital ratios[1] %
2019	2,122.3	8,485.6	25.0
2018	2,279.0	7,564.0	30.1

Risk weighted exposures	2019 £m	2018 £m
Credit risk	4,123.2	3,710.3
Market risk	455.8	169.0
Operational risk	3,895.3	3,680.0
Credit valuation adjustment	11.3	4.7
Total	**8,485.6**	**7,564.0**

Pillar 1 capital required[2]	2019 £m	2018 £m
Credit risk	329.9	296.8
Market risk	36.5	13.5
Operational risk	311.6	294.4
Credit valuation adjustment	0.9	0.4
Total	**678.9**	**605.1**

[1]The Group's Capital is made up entirely of CET1 capital. Therefore the CET1, Tier 1 and total capital ratios are all the same.
[2]The Pillar 1 capital required is 8% of the risk weighted exposure amount.

Regulatory framework

Regulatory supervision

The Group, which includes a subsidiary with a UK banking licence, is supervised in the UK on a consolidated basis. Its lead regulator is the Prudential Regulation Authority (PRA). The PRA sets the Group's Total Capital Requirement (TCR) and monitors the Group's capital adequacy on an ongoing basis. Certain subsidiaries of the Group are supervised by their local regulators who set and monitor the local capital adequacy requirements.

Basel III framework

The Group's regulatory capital is assessed under the Basel III framework, which comprises three pillars:

– Pillar 1 sets rule-based minimum capital standards;

– Pillar 2 establishes the approach to supervisory review and the setting of individual capital requirements, taking into consideration the firm's own assessment of how much capital is required to support the business; and

– Pillar 3 sets disclosure requirements.

Pillar 3 disclosures aim to promote market discipline by enabling market participants to access information relating to regulatory capital and risk exposures.

Regulatory, accounting and business developments

Significant developments with respect to relevant prudential regulatory rules are noted below, together with any business developments or changes to accounting rules that are of particular relevance to the Group's Pillar 3 disclosures.

Regulatory developments in the EU

Revisions to the Basel III framework are implemented in the EU through amendments to CRD IV. The first tranche of revisions, commonly referred to as CRD V and CRR2, passed into law during 2019. The majority of these rules will be effective from the middle of 2021.

The Investment Firm Regulation (IFR) and Directive (IFD) provide a new EU legislative package establishing a dedicated prudential framework for investment firms. This legislation passed into law during 2019 and will be effective from June 2021.

The Group is in the process of preparing for both these changes.

Regulatory buffers

The final increase in the capital conservation buffer to 2.5% was effective from 1 January 2019. On 11 March 2020 it was announced that the UK countercyclical buffer will reduce to 0% effective immediately. It is expected to remain at 0% for at least 12 months. The rate was 1.0% as at 31 December 2019, and had been due to increase to 2.0% on 16 December 2020.

Schroders Personal Wealth

On 3 October 2019, the Group acquired a 49.9% equity interest in Scottish Widows Schroder Wealth Holdings Limited, a financial planning joint venture with Lloyds Banking Group plc that trades as 'Schroders Personal Wealth'.

IFRS 16

IFRS 16 Leases (IFRS 16) replaced IAS 17 Leases and became effective on 1 January 2019. The adoption of IFRS 16 resulted in the Group recognising a right-of-use asset that represents the value of the lease and a corresponding lease liability. The impact was mainly to gross up the Group's balance sheet and resulted in an additional capital requirement of £55 million.

Brexit

The Group is well prepared for Brexit and does not currently expect it to have a significant impact on our business or operating model having already taken steps to review our corporate structure across Europe. Notwithstanding this, we continue to monitor closely the negotiations between the UK and EU regarding the future relationship for trade and services arrangements. Further details are set out in the Annual Report and Accounts on page 50.

Climate change

In 2019, the PRA published a supervisory statement setting out its expectations with respect to the management of financial risks from climate change. These risks are fully considered in the Group's risk management framework. Further details are set out in the Annual Report and Accounts on page 40.

Basis of consolidation

The Pillar 3 disclosures relate to the Group on a consolidated basis. Information about the Group's subsidiaries, including regulated entities, is provided in note 38 of the Annual Report and Accounts.

The regulatory basis of consolidation differs from the accounting basis of consolidation due to the following adjustments:

- The Group's insurance entities (Schroder Pension Management Limited and Burnaby Insurance (Guernsey) Limited) are excluded from the regulatory basis of consolidation. Insurance entities are subject to a separate regulatory framework and are outside the scope of CRD IV. The Group's insurance entities are, however, included in the Group's risk management framework and have been adequately capitalised throughout the year.
- Certain joint ventures are proportionally consolidated for the purpose of calculating the Group's regulatory capital position.
- Collective Investment Undertakings (CIUs), which are consolidated in the financial accounts, are not included within the regulatory basis of consolidation as they do not meet the definition of financial institutions. The Group's interests in such vehicles are recognised as financial assets and are included in the determination of the relevant capital requirement.

Table 2: Reconciliation of financial position – financial accounting to regulatory scope of consolidation

	31 December 2019 (audited)	Deconsolidation of insurance subsidiaries	Proportional consolidation of certain joint ventures	Deconsolidation of CIUs	Regulatory balance sheet
	£m	£m	£m	£m	£m
Assets					
Cash and cash equivalents	2,660.3	(10.6)	50.7	(81.9)	2,618.5
Trade and other receivables	806.7	(9.3)	18.5	(19.1)	796.8
Financial assets	3,016.4	(28.9)	-	(117.4)	2,870.1
Share of net assets in associates and joint ventures	356.5	-	(195.2)	-	161.3
Goodwill and intangibles relating to associates and joint ventures	41.5	-	-	-	41.5
Capital invested in insurance entities	-	32.8	-	-	32.8
Property, plant and equipment	652.3	-	4.8	-	657.1
Goodwill and intangible assets	1,133.4	-	162.9	0.2	1,296.5
Deferred tax	36.9	-	-	-	36.9
Retirement benefit scheme surplus	136.3	-	-	-	136.3
Assets backing unit-linked liabilities	12,425.9	(13,050.6)	-	624.7	-
Total assets	**21,266.2**	**(13,066.6)**	**41.7**	**406.5**	**8,647.8**
Liabilities					
Trade and other payables	921.7	(15.5)	26.6	(12.6)	920.2
Financial liabilities	3,531.1	-	4.4	(205.8)	3,329.7
Lease liabilities	425.3	-	3.4	-	428.7
Current tax	54.1	10.4	0.7	(0.1)	65.1
Provisions	32.2	-	0.2	-	32.4
Deferred tax	16.2	-	6.4	-	22.6
Retirement benefit scheme deficits	12.2	-	-	-	12.2
Unit-linked liabilities	12,425.9	(13,050.5)	-	625.0	0.4
Total liabilities	**17,418.7**	**(13,055.6)**	**41.7**	**406.5**	**4,811.3**
Net assets	**3,847.5**	**(11.0)**	**-**	**-**	**3,836.5**
Called up share capital	282.5	-	-	-	282.5
Share premium	124.2	-	-	-	124.2
Own shares	(169.1)	-	-	-	(169.1)
Other reserves[1]	3,543.3	(11.0)	-	-	3,532.3
Total shareholders' equity	**3,780.9**	**(11.0)**	**-**	**-**	**3,769.9**
Non-controlling interests[2]	66.6	-	-	-	66.6
Equity	**3,847.5**	**(11.0)**	**-**	**-**	**3,836.5**

[1]Other reserves consist of the net exchange differences reserve, associates and joint ventures reserve and profit and loss reserve. Together these reserves make up retained earnings and accumulated comprehensive income.
[2]Non-controlling interests relate to equity capital of subsidiaries held by entities that are not within the scope of consolidation.

Risk management framework and governance

Board risk management declaration

The Board is responsible for the risk management framework of the Group as detailed in the Annual Report and Accounts on page 44.

Risk management framework

The Group is exposed to a variety of risks as a result of its business activities. As such, active and effective risk management is a core competence and we actively monitor the potential impact of current and emerging risks. The Group places significant focus on the integrity and good conduct of employees and the risk management framework is underpinned by a strong ethical culture with clear oversight responsibilities.

The Board is accountable for risk and oversight of the risk management process. It assesses the most significant risks facing the Group and also uses quantitative exposure measures, such as stress tests, to understand the potential impact on the business. Non-executive Director oversight of the risk management process with respect to standards of integrity, risk management and internal control is exercised through the Board Audit and Risk Committee (BARC).

It is the responsibility of all employees to uphold the control culture of Schroders. We embed risk management within all areas of the business. The Group Chief Executive and Group Management Committee (GMC), as the principal executive committee, have responsibility for regularly reviewing the key risks facing the Group. This includes ensuring that their respective business areas are monitoring and reporting relevant risks and controls. They are also responsible for monitoring individual behaviours, ensuring that they mirror the culture and core values of the business.

Oversight of risk is delegated by the Group Chief Executive to the Chief Financial Officer (CFO). The CFO has responsibility for the risk and control framework of the Group. Independent monitoring and reporting of risks and controls at a Group and legal entity level is supported by the Group Head of Risk.

The CFO chairs the Group Risk Committee (GRC), which met ten times in 2019. The GRC supports the CFO and the GMC in discharging their risk management responsibilities. The committee is attended by the heads of the control functions (Group Risk, Compliance, Legal and Internal Audit) along with chief operating officers from across the business and senior managers from Distribution, Product and Wealth Management. Other GMC members regularly attend. The GRC reviews and monitors the adequacy and effectiveness of the Group's risk management framework, including relevant policies and limits. It also reviews trends and current exposures to our key risks and considers issues as they arise. The GRC and the Wealth Management Audit and Risk Committee receive reports relating to the risk profile of Wealth Management.

Our Business Issues and Conflicts Committee supports the GRC and GMC in identifying and managing conflicts that may arise from time to time in our diversified business. The first line of defence against undesirable outcomes is the business functions themselves and the line managers across Asset Management, Wealth Management and Infrastructure. Heads of each business area take the lead role with respect to identifying potential risks in their area and implementing and maintaining appropriate controls to manage these risks.

Line management is supplemented by the control and oversight functions, including Group Risk, Compliance, Legal, Governance, Finance, Tax and Human Resources, which constitute the second line of defence. The compliance monitoring programme reviews the effective operation of relevant key processes against regulatory requirements.

Internal Audit provides retrospective, independent assurance over the operation of controls and forms the third line of defence. The internal audit programme includes reviews of risk management processes and recommendations to improve the control environment, supplemented by external assurance from the Group's auditors. The team also carries out thematic compliance monitoring work.

All key risk types, including strategic, operational, and business risks, are in scope of the risk management framework. Risk appetite statements and associated measures and metrics are in place for each of our key risks, with the exception of Strategic risks which are managed by the Audit and Risk Committee. Capital is not held for Strategic risk as it is influenced by factors outside of our control. Further details about the Group's key risks and mitigations is provided in the Annual Report and Accounts.

Schroder plc's credit rating of A+ from Fitch reflects its strong and conservative risk culture.

Management of key risks

The key risks to which the Group is exposed are summarised below, together with an overview of the relevant capital considerations. A variety of techniques are used to quantify, measure and mitigate risks, depending on the nature of the risk. These include modelling, the use of controls, contingency planning, insurance, collateral and capital allocation.

Monitoring, stress testing tools and escalation processes are in place for key capital and liquidity metrics. Recovery planning is also completed, which details the escalation path for crisis management governance and provides senior management with a set of actions designed to improve the capital and liquidity positions in the event of a stress scenario.

Strategic risks

These risks relate to our strategy and the environment in which we operate. If these risks are not carefully managed, our Assets under Management (AUM) may be lowered and the income we therefore receive. Our business plans seek to address these risks by responding to the challenges faced and growing our assets and earnings.

Whilst capital is not specifically held for strategic risk, it is taken into consideration when assessing capital requirements in respect of business risks (including financial risks) and operational risks.

The Group's key strategic risks are: Changing investor requirements; Fee attrition; Business model disruption; and Market returns.

Business risks

In executing our strategy, a number of key risks arise that could impact our ability to attract and retain clients. By evolving our product offering and delivering investment performance, we have the best opportunity to be selected by clients when allocating assets. A failure to achieve this could lead to a decrease in AUM.

The Group's key business risks are: Reputational risk; Investment performance risk; Climate change risk; Product risk; Business concentration risk; and Financial instrument risk.

Financial instrument risks

The Group faces credit risk, market risk, liquidity risk and the risk of insufficient capital from holding investments where the Group acts as a principal. The Group's approach to management of these risks is set out in this report in the respective sections.

Operational risks

Operational risks are inherent in all activities and processes. They exist in the normal course of business and are heightened when we undertake changes to our organisation. When operational risk events occur, this may affect our clients and our ability to serve them. We may be liable for financial losses or fines, which could affect our business performance and may weaken our standing with stakeholders.

The Group's key operational risks are: Conduct and regulatory risk; Information security risk; Process risk; Fraud risk; Technology risk; Legal risk; Tax risk; People and employment practices risk; and Business services resilience risk.

The Group's approach to operational risk management is set out on page 16 of this report.

Pillar 2 and ICAAP

The Internal Capital Adequacy Assessment Process (ICAAP) is the means by which the Group assesses the level of capital (Pillar 2) that is required to support current and future risks in its business. The ICAAP focuses on the principal risks to the consolidated financial position and assesses the capital required to meet unexpected losses, calculated at a confidence level specified by the Board. It examines each key risk category to identify the exposures that could put the Group's capital at risk. Risks are then assessed using the most appropriate technique and outputs are measured as part of the risk management and oversight process.

Risk and control assessments (RCAs) are completed by each business area to identify and assess their operational risks and controls. Outputs from this process, together with other information such as internal and external risk events, support the operational risk scenario analysis that is used to determine the level of capital required.

The ICAAP also uses a range of scenarios to assess the impact of severe but plausible stress events on capital resources and regulatory capital requirements. The stress test analysis is used to inform the amount of capital that needs to be held as a buffer above minimum requirements. The next section provides further detail on the approach to stress testing.

The ICAAP is updated and formally reviewed by the Board on at least an annual basis, with more frequent reviews in the event of a fundamental or anticipated change to the business or the environment in which the Group operates.

Stress testing

Stress testing is an important element of the Group's planning and risk management processes, helping us to identify, analyse and manage risks within the business. Capital planning forms part of the ICAAP and a range of stress tests and scenario analyses are used to estimate the impact of stress events on capital resources and regulatory capital requirements.

Stress testing is performed on the Group's business plan and considers the impact of a number of the Group's key risks crystallising over the assessment period. The severe but plausible stress scenarios include the following factors which, where relevant, use assumptions more severe than the regulatory stress scenario required by the PRA:

- Outflows of AUM or deterioration in the value of AUM, as a result of, for example, a market downturn, foreign exchange movements, climate change risks or poor investment performance;
- a significant decline in net operating revenue margins reducing projected revenues, together with an increase in the ratio of total costs to net income; and
- the impact of a material operational risk event which could lead to reputational damage and outflows of the Group's AUM.

In addition, stress testing is conducted for the Group's Internal Liquidity Adequacy Assessment Process (ILAAP) and for reverse stress test scenarios. Together with the Group's business plan, capital and liquidity stress tests support the Directors' assessment of the Group's viability as detailed in the Viability Statement (see page 51 of the Annual Report and Accounts).

Board succession and diversity policy

The Board succession process is detailed on page 64 of the Annual Report and Accounts. The Board policy on diversity is detailed on page 64 of the Annual Report and Accounts.

Capital management and regulatory own funds

Capital management

The Group allocates its total assets less liabilities (total capital) between working capital, investment capital and other items. The Group aims to maintain a strong financial position to enable investment in the future of the Group. The Group's capital on an accounting basis is shown in table 3 (as detailed on page 144 of the Annual Report and Accounts):

Table 3: Capital composition

	2019 £m	2018 £m
Working capital – regulatory and other	1,216	1,341
Working capital – seed and co-investment	578	535
Investment capital – liquid	408	465
Investment capital – illiquid	148	165
Other items	1,498	1,115
Total capital	**3,848**	**3,621**

(i) Working capital

The Group's policy is for subsidiaries to hold sufficient working capital to meet their regulatory and other operating requirements. Local regulators oversee the activities of, and impose minimum capital and liquidity requirements on, the Group's operating entities.

Working capital is also deployed through certain subsidiaries to support new investment strategies and growth opportunities and to co-invest alongside the Group's clients.

(ii) Investment capital

Available capital held in excess of working capital requirements is transferred to investment capital. Investment capital is managed with the aim of achieving a low-volatility return. It is mainly held in investment grade corporate bonds and funds managed by the Group.

These liquid investments are available to support the organic development of existing and new business strategies and to respond to other investment and growth opportunities as they arise, such as acquisitions. Investment capital also includes certain commercial private equity investments and illiquid legacy investments.

(iii) Other items

Other items comprises assets that are not investible or available to meet the Group's general operating or regulatory requirements. It includes assets that are inadmissible for regulatory capital purposes such as goodwill and intangible assets.

Regulatory own funds

Regulatory capital is categorised as either Common Equity Tier 1, Additional Tier 1 or Tier 2 depending on the characteristics of the capital items. The Group's regulatory capital meets all of the conditions of CRR article 28 and consists entirely of CET1 capital.

The Group's CET1 capital consists of two classes of shares, ordinary shares and non-voting ordinary shares, as detailed on page 151 of the Annual Report and Accounts. Non-voting ordinary shares carry the same rights as ordinary shares except that they do not confer the right to attend or vote at any general meeting of Schroders plc and on a capitalisation issue they carry the right to receive non-voting ordinary shares rather than ordinary shares. Ordinary share capital accounts for 80% of the Group's total share capital with the remaining 20% represented by non-voting ordinary share capital. CET1 capital includes share premium, retained profits and certain other reserves.

A number of deductions and adjustments are made before arriving at the Group's regulatory own funds. In calculating CET1 capital as at 31 December 2019, deductions have been made for the Group's intangible assets net of deferred tax of £1,315.4 million (including £909.3 million of goodwill), the Group defined benefit pension surplus net of deferred tax of £113.1 million and its own shares held to hedge employee share schemes of £169.1 million. Regulatory adjustments for deferred tax assets and significant investments in financial sector entities are required when certain thresholds are exceeded. As at 31 December 2019, no adjustments were required for these items.

The composition of the Group's regulatory capital is shown in table 4 and the own funds disclosure template as required in Commission Implementing Regulation (EU) No 1423/2013 is presented in Appendix 1.

Table 4: Composition of regulatory capital

	2019 £m	2018 £m
Equity per the regulatory balance sheet[1]	3,836.5	3,610.1
Direct and indirect holdings by an institution of own CET1 instruments[2]	169.1	163.9
Non-qualifying minority interests	(66.6)	(2.7)
Adjustment for foreseeable dividends	(216.7)	(216.1)
Common Equity Tier 1 (CET1) capital before regulatory adjustments	**3,722.3**	**3,555.2**
Common Equity Tier 1 (CET1) capital: regulatory adjustments		
Intangible assets (net of related tax liability)	(1,315.4)	(980.7)
Direct and indirect holdings by an institution of own CET1 instruments	(169.1)	(163.9)
Defined-benefit pension fund assets (net of related tax liability)	(113.1)	(129.2)
Additional value adjustments	(2.4)	(2.4)
Total regulatory adjustments to Common Equity Tier 1 (CET1)	**(1,600.0)**	**(1,276.2)**
Total Common Equity Tier 1 Capital	**2,122.3**	**2,279.0**
Total Capital	**2,122.3**	**2,279.0**

[1]Shareholder equity per the regulatory balance sheet includes the deduction for direct holdings of own CET1 instruments.
[2]Direct holdings of own CET1 instruments are added back to equity because these are presented as a regulatory adjustment in the composition of regulatory capital requirements published by the EBA.

Capital requirements

The Group's Pillar 1 capital requirement is calculated as the total of the credit risk, market risk, operational risk and credit valuation adjustment requirements. Table 5 summarises the Group's Pillar 1 capital requirement.

Table 5: Total consolidated capital requirement of the Group under Pillar 1

	2019 £m	2018 £m
Credit risk		
Central governments or central banks	-	-
Regional governments or local authorities	-	1.9
Multilateral development banks	-	-
Institutions	28.2	34.8
Corporates	57.5	62.7
Retail	2.8	2.8
Secured by mortgages on immovable property	4.7	5.6
Exposures in default	0.1	-
Items associated with particular high risk[1]	15.4	7.2
Covered bonds	0.5	0.7
CIUs	76.4	72.7
Equity	8.2	8.5
Other items[2]	136.1	99.9
Total credit risk capital requirement	**329.9**	**296.8**
Market risk		
In respect of foreign exchange	36.5	13.5
Total market risk capital requirement	**36.5**	**13.5**
Operational risk		
Calculated in accordance with the Standardised approach	311.6	294.4
Total operational risk capital requirement	**311.6**	**294.4**
Credit valuation adjustment[3]		
Calculated in accordance with the Standardised approach	0.9	0.4
Total credit valuation capital requirement	**0.9**	**0.4**
Total Pillar 1 capital requirement	**678.9**	**605.1**

[1]High risk exposures include private equity investments.
[2]Other items as per CRR article 134 include accrued income, fee debtors, tax, prepayments and other debtors.
[3]CRD IV introduced a regulatory capital charge to cover credit valuation adjustment (CVA) risk, the risk of adverse movements in the credit valuation adjustments taken for expected credit losses on derivative transactions. The standardised approach has been applied to calculate the CVA.

The Group's Total Capital Requirement (TCR), which is its Pillar 1 requirement plus its Pillar 2A requirement, was £858 million as at 31 December 2019 (2018: £827 million).

In addition to the TCR, the Group is required to hold capital in its insurance entities, which are not consolidated in the banking group, and to maintain buffers in accordance with EU regulation. As at 31 December 2019 the Group was required to hold a capital conservation buffer of 2.5% (2018: 1.875%) of risk weighted assets and a countercyclical capital buffer of 0.64% of risk weighted assets (2018: 0.68%). The Group is not required to hold capital in relation to the globally systemically important institutions buffer. The capital conservation buffer is designed to ensure that institutions build up capital buffers outside periods of stress which can be drawn upon if required. The countercyclical capital buffer is deployed in a jurisdiction when excess credit growth is associated with an increase in system-wide risk. The institution specific countercyclical buffer that applies to the Group is the weighted average of the countercyclical capital buffers that apply in the jurisdictions where our relevant credit exposures are located.

As at 31 December 2019, the Group's overall capital requirement including these amounts was £1,127 million (2018: £1,021 million).

Leverage ratio

CRD IV requires firms to calculate a non-risk based Leverage Ratio to supplement risk-based capital requirements. The leverage ratio measures the relationship between capital resources and total assets. The purpose of monitoring and managing this metric is to enable regulators to constrain the build-up of excessive leverage.

The leverage ratio is calculated based on the Group's capital divided by exposures which are defined as the total of on and off balance sheet exposures less the deductions applied to Tier 1 capital.

As at 31 December 2019 the Group's leverage ratio was 29.1% (2018: 32.5%). The leverage disclosure templates required by Commission Implementing Regulation (EU) No 2016/200 are presented in Appendix 2.

Credit risk

Overview

Credit risk is the risk that a counterparty to a financial instrument, loan or commitment will cause the Group financial loss by failing to discharge their obligations. The Group is exposed to credit risk in relation to its loans and advances to customers, cash held on deposit with banks (including central banks), fixed income investments, trade and other receivables (including balances subject to settlement risk) and derivative positions arising from its management of interest rate risk and market risk.

Credit risk management

The Group employs a range of techniques to assess and monitor credit risk.

The Group has a credit risk management framework in place to assess and monitor the creditworthiness of the Group's counterparties using, where appropriate, External Credit Assessment Institutions (ECAI) ratings supplemented by internal assessments. Exposures are monitored against relevant thresholds including regulatory large exposure requirements. The Group seeks to diversify its exposure across different counterparties.

Credit risk is mitigated where possible through collateralisation of exposures. In Wealth Management, financial collateral such as client portfolios is used to support client lending. Financial collateral is marked to market on a daily basis and compared to the outstanding loan balance. Other assets, such as real estate property, are also used as collateral. These assets are valued less frequently but meet the requirements of the CRR Article 208(3).

The Group does not usually provide loans, overdrafts or advances to clients on an unsecured basis.

Credit risk measurement

Schroders has elected to adopt the standardised approach to credit risk. Under the standardised approach, the Group's credit risk capital requirement is calculated as 8% of total risk weighted exposures. Risk weighted exposures are calculated by applying a prescribed regulatory risk-weight to individual credit risk exposures.

As the Group's trading book is small, the Group applies the derogation allowed under article 94 of the CRR to include exposures arising from the Group's limited trading activities in the Group's credit risk exposure.

Calculating the credit risk exposure

The Group's regulatory credit risk exposure is calculated using the accounting value of the relevant instruments. Adjustments are made for the effect of funded credit protection on reverse repurchase agreements and adjustments for credit losses made in accordance with IFRS. An add-on to reflect the potential future exposure of the Group's derivative portfolio is incorporated and off-balance sheet exposures are included after applying the relevant credit conversion factor (CCF). Items deducted from regulatory capital are excluded from the credit risk exposure.

The recognition of funded credit protection is subject to a number of considerations, including ensuring the legal enforceability of the collateral arrangements, monitoring the market value of the collateral and ensuring that the value of the collateral is not materially correlated with the credit quality of the counterparty.

Table 6 shows the Group's total credit risk exposure by asset class.

Table 6: Fully adjusted credit risk exposure value

	Regulatory balance sheet[1] £m	Regulatory adjustments £m	Effect of funded credit protection on reverse repurchase agreements £m	Credit risk mitigation £m	Off-balance sheet items post CCFs £m	Derivative add-on £m	2019 Exposure value £m
Assets							
Cash and cash equivalents	2,618.5	-	(322.7)	-	-	-	2,295.8
Trade and other receivables	796.8	-	(0.3)	-	-	-	796.5
Financial assets	2,870.1	-	(250.0)	(1.1)	41.3	11.9	2,672.2
Share of net assets in associates and joint ventures	161.3	-	-	-	-	-	161.3
Goodwill and intangibles relating to associates and joint ventures	41.5	(41.5)	-	-	-	-	-
Insurance entity capital	32.8	-	-	-	-	-	32.8
Property, plant and equipment	657.1	-	-	-	-	-	657.1
Goodwill and intangible assets	1,296.5	(1,296.5)	-	-	-	-	-
Deferred tax	36.9	37.8	-	-	-	-	74.7
Retirements benefit scheme surplus	136.3	(136.3)	-	-	-	-	-
Financial liabilities	-	-	-	-	-	19.1	19.1
Total	**8,647.8**	**(1,436.5)**	**(573.0)**	**(1.1)**	**41.3**	**31.0**	**6,709.5**

[1]Approaches to assessing potential credit risk adjustments past due and impaired financial assets are detailed in Appendix 3 to this document.

Each exposure is assigned to a credit risk exposure class as defined in article 112 of the CRR. This is set out in table 7 below.

Table 7: Exposure value per table 6 analysed by exposure class

	2019 Exposure value £m	2018 Exposure value £m
Central governments or central banks	1,756.3	1,601.3
Regional governments or local authorities	-	119.3
Multilateral development banks	35.8	54.8
Institutions	1,291.6	1,530.4
Corporates	884.6	964.9
Retail	48.0	47.7
Secured by mortgages on immovable property	152.8	166.4
Exposures in default	1.8	-
Items associated with particular high risk	128.2	59.5
Covered bonds	68.6	92.8
CIUs	955.3	908.5
Equity	41.0	42.6
Other items	1,345.5	915.9
Total exposure value	**6,709.5**	**6,504.1**

Appendix 4 provides further information on the Group's on and off-balance sheet exposures subject to the credit risk framework broken down by significant country. Countries contributing to approximately 90% of the Group's total exposure have been disclosed separately and all other countries have been categorised as 'Other'.

Calculating the risk weighted exposure

The Group's risk-weighted exposure is calculated by applying the risk weights prescribed in Part 3, Title II, Chapter 2 of the CRR to the credit exposures in table 7. The allocation of risk weights by exposure class is shown in table 8.

The risk weight is based on the exposure class to which the exposure is assigned, the maturity of the exposure and the credit quality of the counterparty. The Group assesses the credit quality of its counterparties with reference to credit assessments conducted by ECAIs. The primary ECAI used by the Group is Fitch and its ratings are used to assess the credit quality of exposures wherever possible. If a Fitch rating is unavailable, a rating from an alternative ECAI is used, including Moody's or Standard & Poor's. All three ratings agencies are recognised as eligible ECAIs by the PRA. Where no credit rating can be obtained, the exposure is categorised as unrated. Unrated exposures are risk weighted based on exposure class and include loans to individuals, seed capital, equity investments, trade and other receivables, tax assets and fixed assets.

Table 8: Risk weighted assets by exposure class

	Exposure after credit risk mitigation – Risk weights									2019
£m	**0%**	**20%**	**35%**	**50%**	**75%**	**100%**	**150%**	**250%**	**Other**	**Total risk weighted assets**
Central governments or central banks	1,756.3	-	-	-	-	-	-	-	-	-
Regional governments or local authorities	-	-	-	-	-	-	-	-	-	-
Multilateral development banks	35.8	-	-	-	-	-	-	-	-	-
Institutions	-	982.6	-	309.0	-	-	-	-	-	351.0
Corporates	-	93.3	-	181.5	-	609.8	-	-	-	719.2
Retail	-	-	-	-	48.0	-	-	-	-	36.0
Secured by mortgages on immovable property	-	-	144.6	-	-	8.2	-	-	-	58.8
Exposures in default	-	-	-	-	-	1.8	-	-	-	1.8
Items associated with particular high risk	-	-	-	-	-	-	128.2	-	-	192.3
Covered bonds	-	-	-	-	-	-	-	-	68.6	6.9
CIUs	-	-	-	-	-	955.3	-	-	-	955.3
Equity	-	-	-	-	-	0.1	-	40.9	-	102.4
Other items	0.5	-	-	-	-	1,108.1	-	236.9	-	1,700.2
Total	**1,792.6**	**1,075.9**	**144.6**	**490.5**	**48.0**	**2,683.3**	**128.2**	**277.8**	**68.6**	**4,123.9**

Calculating the risk weighted exposure with small and medium-sized enterprise supporting factor

A small and medium-sized enterprise (SME) supporting factor, as defined in article 501 of the CRR, is applied to certain exposures. SME supporting factors are in place to ensure adequate flow of credit to SME's which has the effect of reducing risk weighted assets in the retail category. Table 9 shows the risk weighted exposure with the SME supporting factor applied.

Table 9: Risk weighted exposures by exposure class including SME supporting factor

	2019 Risk weighted assets (with SME factor) £m	2018 Risk weighted assets (with SME factor) £m
Central governments or central banks	-	-
Regional governments or local authorities	-	23.9
Multilateral development banks	-	-
Institutions	351.0	435.6
Corporates	719.2	783.1
Retail	35.3	35.0
Secured by mortgages on immovable property	58.8	70.3
Exposures in default	1.8	-
Items associated with particular high risk	192.3	89.3
Covered bonds	6.9	9.3
CIUs	955.3	908.5
Equity	102.4	106.5
Other items	1,700.2	1,248.8
Total risk weighted exposure amount (with SME supporting factor)	**4,123.2**	**3,710.3**
Total credit risk capital requirement	**329.9**	**296.8**

Market risk

Overview

Market risk is the risk that the value of assets will fluctuate as a result of movements in factors such as market prices, interest rates and foreign exchange rates. The Group's primary exposures to market risk arise from holdings of principal investments and foreign currency positions as a result of overseas operations. The Group has a second order exposure to market risk through its investment management activities as the income earned from this agency business will vary dependent on the value of AUM. This second order exposure does not give rise to a capital requirement, but is considered as part of the Group's market risk management activities and stress testing.

Market risk management

Our geographically diversified, broad product range helps to mitigate market risk in a variety of market conditions and serves to diversify individual market dependencies.

For its principal investments, the Group has an investment framework in place that includes a risk appetite and prescribed limits which are approved by the Board. The currency risk associated with non-sterling investments within the investment capital and seed capital portfolios is hedged, where appropriate, using short-dated forward foreign exchange contracts. The Group also aims to hedge the market risk exposure in its seed capital investments where practical. Where this is not possible the Group Capital Committee is required to approve the risk exposure.

The Group is exposed to foreign exchange risk as a result of transactional foreign exchange exposures in its operating entities. Transactional foreign exchange exposures arise as a result of a position held in a currency other than the functional currency of the transacting entity. The Group seeks to minimise its exposure to this risk by converting foreign currency positions to the functional currency of the transacting entity as soon as practical.

The Group is exposed to structural foreign exchange risk as a result of its net investment in overseas subsidiaries and branches. These investments are recorded in the functional currencies of the individual entities and subsequently translated to the Group's presentational currency (sterling). Foreign exchange differences arising on the translation of the foreign operations are recorded in the net exchange differences reserve through other comprehensive income and give rise to movements in the Group's CET1 capital. The Group manages its exposure to this risk by returning surplus capital to the ultimate parent of the Group as soon as practical.

The Wealth Management Executive Committee monitors and manages market risk, primarily interest rate risk in the banking book, in the Group's banking businesses. This process includes monitoring the sensitivity of the balance sheet to movements in yield curves and assessing any mismatch between interest rate sensitive assets and liabilities.

Market risk measurement

The Group calculates its own funds requirement for market risk in accordance with Part 3, Title IV, Chapter 2 of the CRR. In determining its Pillar 1 capital requirement, the Group is required to consider whether its exposure to market risk arises from trading or non-trading activities. The Group does not generally hold positions with trading intent. Financial instruments that make up the Group's investment capital and seed capital portfolios are considered to be non-trading as they are not managed on a short-term basis and the positions are not bought in order to benefit from actual or expected short term price differences.

Consequently, the Group's trading book is small and therefore, as noted in the credit risk section above, the Group applies the derogation allowed under article 94 of the CRR to include exposures arising from the Group's limited trading activities in the Group's credit risk exposure.

Therefore, the Group's capital requirement for market risk is calculated based on the Group's exposure to foreign exchange risk. The Group applies the standardised rules to determine the capital requirement for these exposures.

Foreign exchange position risk measurement

The Group considers article 352 of the CRR when calculating its overall net foreign exchange position. The net open positions in each currency are assessed to determine an overall net foreign exchange position, which is then multiplied by 8% to calculate the Group's capital requirement.

Table 10: Foreign exchange positions subject to capital charge

	2019 £m	2018 £m
Long position subject to capital charge	455.8	169.0
Market risk capital requirement	**36.5**	**13.5**

Operational risk

Overview

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. It includes legal, regulatory, tax, technology, information security, third party, and fraud risks, and is inherent in all activities and processes.

Operational risk is a significant risk for the Group, and makes up 46% (2018: 49%) of the total capital requirement.

Operational risk management

Line management is responsible for operational risk controls throughout the Group's business, including communicating controls through documented policies, procedures and standards, and for promoting and overseeing high standards of conduct in accordance with the Group's Guiding Principles (and Values) and Conduct framework.

RCAs are required to be completed by each business area at least annually and when significant changes occur. The RCAs set out relevant risks and the controls and supervision practices that have been implemented by management. Group Risk oversee the completion of RCAs and report to the GRC on key findings including high risk areas for which risk mitigation plans are required. Other elements of the framework include risk event management and escalation, internal control reports and third party risk assessments.

Further information on the key operational risks and how those risks are managed can be found in the Annual Report and Accounts on page 45.

Operational risk measurement

Schroders has adopted the standardised approach to calculating the Pillar 1 capital requirement for operational risk in accordance with Part 3, Title III, Chapter 3 of the CRR. Under the standardised approach, institutions calculate an average relevant indicator over the past three years. The Group's relevant indicator is based on revenues, including the sum of interest receivable and similar income, interest payable and similar charges, income from shares and other variable/fixed-yield securities, commissions/fees receivable, commissions/fees payable and other operating income. Revenues are categorised by business line, each with a relevant beta factor ranging from 12% to 15%. The operational risk capital requirement is calculated by multiplying average revenues by the relevant beta factor and summing across the business lines.

Table 11: Calculation of the relevant indicator and own fund requirement

	2019		2018	
	Risk weighted assets	Capital required	Risk weighted assets	Capital required
Relevant indicator elements	£m	£m	£m	£m
Commercial banking	19.2	1.5	11.8	0.9
Retail banking	19.5	1.6	19.4	1.6
Agency services	3.5	0.3	1.5	0.1
Asset management	3,853.1	308.2	3,647.4	291.8
At 31 December	**3,895.3**	**311.6**	**3,680.1**	**294.4**

Other risks and sensitivity analysis

Non trading book exposures in equities

An overview of the accounting techniques and valuation methodologies used, as required by article 447 of the CRR, is included in note 9, Financial Assets, within the Annual Report and Accounts.

Pension obligation risk

The risk of deficit in the defined benefit section of the Schroders Retirement Benefit Scheme (the Scheme), which was closed to future accrual on 30 April 2011, is assessed through the use of stress tests which consider the impact of possible alternative assumptions on the valuation of the Scheme liabilities as well as stresses on asset values. Stress tests are performed in line with the PRA's Supervisory Statement PS17/15, dated July 2015, and the PRA Statement of Policy 'The PRA's methodologies for setting Pillar 2 capital'. The Group was not required to hold capital for pension obligation risk as at 31 December 2019.

Liquidity risk

Liquidity risk is the risk that a firm, although having assets greater than liabilities, is unable to meet payment obligations in a timely manner; and, in relation to clients' portfolios, the inability to sell the underlying investments for full value or at all in a timely manner.

The Group carries out an ILAAP on a consolidated basis and holds liquidity resources to meet its own expected payment obligations as they fall due, both under normal conditions and severe but plausible stresses. The Group's liquidity stress tests are in addition to the stress tests that are produced by each of the Wealth Management banking subsidiaries in assessing their own individual liquidity requirements.

Interest rate risk

Interest rate risk is the exposure of the Group's balance sheet to adverse movements in interest rates, i.e. the risk that the fair value of future cash flows of financial instruments will fluctuate due to changes in market interest rates. The largest exposure to interest rate risk within the Group arises from the maturity mismatch (both contractual and repricing) between assets and liabilities on the banking subsidiaries' balance sheets.

The sensitivities to interest rate risk analysed by currency for a 0.75% (2018: 1.0%) increase in interest rates as at 31 December 2019 and as at 31 December 2018 are shown in table 12.

Table 12: Interest rate sensitivity: analysis by currency of increase in interest rates

	2019 £m	2018 £m
GBP	1.2	1.6
EUR	0.3	0.6
Others	1.5	1.8
Total	**3.0**	**4.0**

Asset encumbrance

Certain of the Group's assets are encumbered, for example as a result of collateralising margin agreements. A summary of the Group's encumbered and unencumbered assets is provided in Appendix 5.

Remuneration disclosures

The following disclosures explain how Schroders has complied with the regulatory requirements under the UK implementation of the Capital Requirements Directive (CRD), in particular Articles 92 to 95.

These disclosures should be read in conjunction with the Remuneration report on pages 72 to 108 of the Annual Report and Accounts, which provides further information on the activities of our Remuneration Committee and our remuneration principles and policies.

Details of the UK Remuneration Codes can be found at www.fca.org.uk and information on the Remuneration Part of the PRA Rulebook can be found at www.prarulebook.co.uk.

Decision-making process for determining the remuneration policy

Schroders has an established Remuneration Committee consisting of independent non-executive Directors of Schroders plc. The Committee met nine times during 2019. Their responsibilities include recommending to the Board the Group's policy on Directors' remuneration, overseeing the remuneration governance framework and ensuring that remuneration arrangements are consistent with effective risk management. The Committee determines the remuneration for the executive Directors, other members of the GMC and the Group Company Secretary, monitors and reviews remuneration for the control function heads and other MRTs, and also provides oversight of the compensation review outcomes for employees more broadly. The Committee determines Directors' remuneration in the context of remuneration across the Group, including financial performance, the total compensation ratio and the remuneration outcomes for the wider workforce. To avoid conflicts of interest, no Director or employee participates in decisions determining their own remuneration.

The Chairman of the Audit and Risk Committee serves on the Remuneration Committee, to ensure the Remuneration Committee is adequately informed of risks facing the Group and the management of those risks. The Committee's Terms of Reference was updated in July 2019 to bring it into greater alignment with the principles and provisions of the UK Corporate Governance Code. The Committee received advice from PricewaterhouseCoopers LLP and McLagan (AON) Limited during the year. The Committee assesses the performance of its external advisers annually, to ensure that the advice provided is independent of any support provided to management. The role and activities of the Committee and their use of advisers are further detailed in the Remuneration report and the Committee's Terms of Reference (both of which are available on the Group's website).

The Remuneration Committee developed the Group's remuneration policy with a number of principles in mind. The overall policy is designed to promote the long-term success of the Group. It is:

- Aligned with clients: A significant proportion of higher-earning employees' and material risk takers' variable remuneration is granted as Fund Awards, which are notional investments in funds managed by the Group, thereby aligning the interests of employees and clients.
- Aligned with shareholders: A significant proportion of variable remuneration is granted in the form of deferred awards over Schroders' shares, thereby aligning the interests of employees and shareholders. In addition, the executive Directors of Schroders plc and other members of the GMC are required, over time, to acquire and retain a holding of Schroders' shares or rights to shares equivalent in value to 300% of annual base salary, or 500% of salary for the Group Chief Executive. On stepping down, the executive Directors are required to maintain the level of shareholding required while they were an executive Director for a period of two years.
- Aligned with financial performance: Total variable compensation is managed as a percentage of pre-bonus profit before tax and exceptional items, determined by the Remuneration Committee and recommended to the Board. The total spend on remuneration is managed as a percentage of net income, the total compensation ratio. These ratios are determined by the Committee and recommended to the Board. This approach aligns remuneration with financial performance.
- Competitive: Employees receive a competitive remuneration package, which is reviewed annually and benchmarked by reference to the external market. This allows us to attract and retain the best talent, who know that good performance will be rewarded.
- Designed to encourage retention: Deferred variable remuneration does not give rise to any immediate entitlement. Awards normally require the participant to be employed continuously by the Group until at least the third anniversary of the grant date in order to vest in full.

The Remuneration Committee is satisfied that the Group's remuneration approach is in line with regulatory requirements. Schroders is a Level 3 firm under the PRA Rulebook and FCA Remuneration Code proportionality regimes for CRD.

Material risk taker criteria

The Group's Material Risk Takers (MRTs) under CRD are individuals in roles that can materially affect the risk of the Group. Subject to proportionality considerations, the list of individuals reviewed in determining those who are CRD MRTs includes:

- Directors of Schroders plc and certain key operating subsidiaries;
- Non-executive directors of Schroders plc and certain key operating subsidiaries;
- Members of the Group Management Committee;
- Employees in key control function roles;
- Other employees who the Group deems may have a material impact on the firm's risk profile through their professional activities; and
- Employees who are remunerated at the same levels as senior management and material risk takers identified above, if their role has a material risk impact.

The Schroders CRD MRT population is determined in accordance with technical standards issued by the European Banking Authority with respect to qualitative and appropriate quantitative criteria to identify categories of staff whose professional activities have a material impact on an institution's risk profile. In determining whether or not someone who meets the quantitative criteria in the technical standard should be included as a CRD MRT, the professional activities of the role were assessed for their impact on the ICAAP risks as identified by the Group. Control frameworks and relevant committee terms of reference were also taken into account. The identification framework was reviewed by the Heads of Control Functions in 2019 and their input reflected as appropriate.

Link between pay and performance

Employee remuneration, including for CRD MRTs, is comprised of fixed pay and variable performance-related pay. The Remuneration Committee reviews individual fixed pay and variable performance-related pay decisions for all employees deemed to be CRD MRTs.

Fixed pay is principally comprised of salaries or fees. All MRTs receive either a salary (for employees) or fees (for non-executive Directors) that reflects a market competitive rate of pay, taking account of the employee's role and responsibilities, skills and experience and ongoing contribution. Fixed pay also includes appropriate benefits in kind to help recruit and retain talent, reflect local market practice and support employee health and wellbeing. Cash allowances are sometimes paid, typically after a benefit was phased out so cash in lieu was offered to existing employees in exchange. Retirement benefits are also provided to help recruit and retain talent, reflect local market practice and enable and encourage provision for retirement.

Variable performance-related pay is principally comprised of annual bonus awards, which aim to motivate employees to achieve financial, non-financial and personal objectives for the financial year, which are consistent with the Group's strategy and help to reward talent for their individual contribution. Non-executive directors do not receive variable performance-related pay. The overall size of the annual pool for variable performance-related pay is a material component of the Group's total remuneration expense. It is set by the Board and the Remuneration Committee by reference to two ratios: 1) bonus charge to pre-bonus profit before tax and exceptional items; and 2) total compensation ratio, both of which are reported to shareholders. This ensures that the aggregate spend on variable performance-related pay is directly linked to the Group's performance.

MRTs who are permanent employees are eligible to be considered for an annual bonus award each year. Bonuses for all employees take account of overall Group, team and individual performance against agreed objectives. In this context, performance typically includes financial and non-financial measures. Financial metrics include trends in profit and cost-control, client investment performance, and net new business. Non-financial performance metrics, including adherence to effective risk management and behaviours aligned to Schroders' values form a significant part of the performance assessment that is considered in determining the individual's bonus award. During the annual performance appraisal, line managers assess each employee's behaviours to identify those whose behaviour exemplifies Schroders values – Excellence, Integrity, Innovation, Passion and Teamwork – as well as any employees whose behaviour falls short of the standards that the firm expects.

The Heads of Risk, Compliance, Internal Audit and Legal provide input to Senior Management and the Remuneration Committee on issues that should be taken into consideration in setting the bonus pool or reviewing individual remuneration outcomes. This provides a further opportunity to reflect attitudes to risk and compliance and behaviours in line with our values in the determination and allocation of the bonus pool and in individual employee performance appraisals and remuneration outcomes. We believe that a discretionary incentive approach is preferable to the use of formulaic arrangements, to ensure that good conduct and behaviours in line with our values are rewarded, to avoid reinforcing or creating conflicts of interest and to encourage a one-team attitude. MRTs are subject to enhanced control function oversight of their activities and direct oversight of their remuneration by the Remuneration Committee.

Deferral of incentive awards is a key mechanism to retain talent, primarily through the use of bonus deferrals.

- CRD MRTs who have also been identified as MRTs under the Undertaking for Collective Investment in Transferable Securities (UCITS) or Alternative Investment Fund Managers (AIFM) Directives are subject to the UCITS/AIF MRT remuneration policy. This sees 40%-60% of variable remuneration for each UCITS/AIF MFT being deferred. At least 50% of variable remuneration is delivered as Fund units, applying equally to both the deferred element and the upfront element (i.e. that element that is not deferred). Upfront fund awards are subject to a six month retention period and deferred fund awards to an additional six months deferral period, so they vest over a period of 3.5 years.
- Deferred annual bonus awards for UCITS/AIF MRTs are granted under the Deferred Award Plan (DAP). The DAP aligns the interests of UCITS/AIF MRTs with those of clients and shareholders, provides an incentive for the employee to stay at Schroders and makes it more expensive for competitors to recruit talent from Schroders. DAP share awards are conditional rights to acquire shares in the Group at nil cost and vest over three years. DAP fund awards are conditional rights to receive a cash sum based on the value of a notional investment in a range of Schroders investment products and vest over 3.5 years. The pay-outs from DAP fund awards are directly determined by the Group's performance in managing funds for our clients. In 2019, deferrals were generally delivered equally between share awards and fund awards, subject to a minimum fund award of £10,000.
- For employees who are not UCITS/AIF MRTs, deferred annual bonus awards are granted under the Equity Compensation Plan (ECP). The ECP works in a similar way to the DAP but is slightly simplified, as these roles are not subject to the remuneration requirements of the UCITS or AIFM Directives.
- The Equity Incentive Plan (EIP) is an additional deferred remuneration plan, used to recognise sustainable performance and potential, and to increase the alignment of employee interests with the interests of shareholders and clients. EIP awards operate in a similar way to ECP awards but vest after five years.
- In March 2019, executive Directors of Schroders plc were eligible to be considered for an award under the Long Term Incentive Plan (LTIP), which is comprised of deferred awards of Schroders' shares that vest after four years to the extent that performance conditions are achieved.

In addition to providing retention incentives, a primary purpose of our deferred awards (DAP, ECP, EIP and LTIP) is to support our performance culture where employees recognise the importance of sustainable performance, at the Group, business and individual levels and their responsibilities in delivering value for clients and shareholders over the longer-term.

Under malus terms, deferred remuneration awards granted under the DAP, ECP, EIP or LTIP may be reduced or lapsed, at the Committee's discretion. Under clawback terms, amounts paid or released from such awards may be recovered for a period of 12 months from the date of payment or release, at the Committee's discretion. These terms can be used to risk-adjust deferred remuneration awards in a range of circumstances, set out in the Group's malus and clawback policy. The potential malus and clawback triggers were designed around the requirements of the UCITS and AIFM Directives and the ESMA Guidelines on remuneration under those directives. The circumstances in which malus and clawback might be triggered include:

- Fraud, misbehaviour or misconduct by the Participant;
- Serious error by the Participant as a result of the Participant's negligent conduct or omission;
- A significant failure of risk management for which the Participant has significant responsibility;
- Corporate failure or a significant downturn in financial performance to which the participant's negligent conduct has significantly contributed;
- A material financial misstatement for which the Participant has significant responsibility or which has led to a greater portion of an award being released to the Participant than would otherwise have been the case;
- Vesting or settlement based on erroneous or misleading data; and
- A regulatory sanction where the conduct or omission of the Participant significantly contributed to the sanction.

Malus terms apply to ECP awards granted since May 2011, to EIP awards granted since July 2013 and to DAP and LTIP awards granted at any time. Clawback applies to ECP, EIP and LTIP awards granted since October 2013 and to DAP awards granted at any time. For awards granted prior to 2018 the circumstances in which malus and clawback terms could be applied were more narrowly described.

Employees including CRD MRTs are not allowed to enter into hedging arrangements that undermine the intended performance alignment of deferred awards.

Further details of our remuneration policy, our deferred remuneration arrangements and LTIP performance conditions are provided in the Remuneration report.

Quantitative remuneration disclosures

422 individuals have been identified as MRTs under the Capital Requirements Directive, of which 56 are classified as Senior Management. The increase in the number of MRTs compared to last year reflects changes in committee membership and management structure.

Table 13: Total remuneration expenditure for Material Risk Takers split by Senior Management and other Material Risk Takers

2019	Senior Management £'000	Other Material Risk Takers £'000
Fixed remuneration	12,560	74,196
Variable remuneration	46,400	128,360
Total remuneration	**58,960**	**202,556**

2018	Senior Management £'000	Other Material Risk Takers £'000
Fixed remuneration	7,225	73,957
Variable remuneration	32,513	148,597
Total remuneration	**39,738**	**222,554**

Table 14: Aggregate remuneration expenditure for Material Risk Takers by business area

	2019 £'000	2018 £'000
Asset Management	186,116	190,135
Wealth Management	22,115	21,521
Rest of Group	53,285	50,636
Total remuneration	**261,516**	**262,292**

The remuneration disclosed above includes:

– Non-executive Director fees for 2019;

– Annual base salaries as at 31 December 2019 (or at termination date for leavers);

– Cash bonus awards for the 2019 performance year;

– Deferred awards (ECP, DAP, EIP and LTIP) for 2019 based on the face value at the date of grant. LTIP awards are subject to performance conditions, which can result in the portion of the award that is ultimately released ranging from 0% to 100%. The figures above assume 50% vesting;

– The grant date value of any allocations of an entitlement to receive a share in any carried interest earned on certain investment vehicles; and

– Any other awards for new hires and any bonus payments made to leavers.

In addition, MRTs other than non-executive Directors are normally eligible to receive employee benefits, such as private health care and pension, on the same basis as other employees. One of the non-executive Directors of Schroders plc also receives private health care and medical benefits, the value of which is included in the disclosures above.

Appendix 1 Own funds disclosures

Table 15: Own funds

	Common Equity Tier 1 (CET1) capital: Instruments and reserves	2019 £m	2018 £m	Regulation (EU) No 575/2013 Article Reference
1	Capital instruments and the related share premium accounts	406.7	406.7	26(1), 27, 28, 29
2	Retained earnings	3,181.7	2,943.1	26(1)(c)
3	Accumulated other comprehensive income (and other reserves)	133.9	205.4	26(1)
6	Common Equity Tier 1 (CET1) capital before regulatory adjustments	3,722.3	3,555.2	
	Common Equity Tier 1 (CET1) capital: regulatory adjustments			
7	Additional value adjustments	(2.4)	(2.4)	34,105
8	Intangible assets (net of related tax liability)	(1,315.4)	(980.7)	36(1)(b), 37
15	Defined-benefit pension fund assets	(113.1)	(129.2)	36(1)(e), 41
16	Direct and indirect holdings by an institution of own CET1 instruments	(169.1)	(163.9)	36(1)(f), 42
28	**Total regulatory adjustments to Common Equity Tier 1 (CET1)**	**(1,600.0)**	**(1,276.2)**	
29	**Common Equity Tier 1 Capital**	**2,122.3**	**2,279.0**	
45	**Tier 1 Capital (T1 = CET1 + AT1)**	**2,122.3**	**2,279.0**	
59	**Total Capital**	**2,122.3**	**2,279.0**	
60	**Total risk weighted assets**	**8,485.6**	**7,564.0**	
	Capital ratios and buffers			
61	**Common Equity Tier 1 (as a percentage of total risk exposure)**	**25.0%**	**30.1%**	**92(2)(a)**
62	**Tier 1 (as a percentage of total risk exposure amount)**	**25.0%**	**30.1%**	**92(2)(b)**
63	**Total capital (as a percentage of total risk exposure amount)**	**25.0%**	**30.1%**	**92(2)(c)**
64	**Institution specific buffer requirement (CET1 requirement in accordance with article 92(1)(a) plus capital conservation and countercyclical buffer requirements, plus systematic risk buffer, plus systemically important institution buffer expressed as a percentage of risk exposure amount)**	**7.6%**	**7.0%**	**CRD 128, 129, 130, 131, 133**
65	**of which: capital conservation buffer requirement**	**2.50%**	**1.875%**	
66	**of which: countercyclical buffer requirement**	**0.64%**	**0.68%**	
68	**Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)**	**17.0%**	**22.1%**	**CRD 128**
	Amounts below the thresholds for deduction (before risk weighting)			
72	Direct and indirect holdings of the capital of financial sector entities where the institution does not have a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	55.7	69.2	36(1)(h), 46, 45, 56(c), 59, 60, 66(c), 69, 70
73	Direct and indirect holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	202.8	218.0	36(1)(i), 45, 48
75	Deferred tax assets arising from temporary differences (amount below 10% threshold, net of related tax liability where the conditions in article 38(3) are met)	74.7	79.6	36(1)(c), 38, 48

Appendix 2 Leverage disclosures

Table 16: Summary reconciliation of accounting assets and leverage ratio exposures

		2019 £m	2018 £m
1	Total assets as per published financial statements	21,266.2	19,634.3
2	Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation	(12,618.4)	(11,581.6)
4	Adjustments for derivative financial instruments	31.0	25.9
6	Adjustment for off-balance sheet items (i.e. conversion to credit equivalent amounts of off-balance sheet exposures)	41.3	44.2
7	Other adjustments	(1,428.5)	(1,109.9)
8	**Leverage ratio total exposure measure**	**7,291.6**	**7,012.9**

Table 17: Leverage ratio common disclosure

		2019 £m	2018 £m
	On-balance sheet exposures (excluding derivatives and SFTs)		
1	On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	7,968.8	7,535.2
2	(Asset amounts deducted in determining Tier 1 capital)	(1,428.5)	(1,109.9)
3	**Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets) (sum of lines 1 and 2)**	**6,540.3**	**6,425.3**
	Derivative exposures		
4	Replacement cost associated with all derivatives transactions (i.e. net of eligible cash variation margin)	46.7	20.5
5	Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method)	31.0	25.9
11	**Total derivatives exposures (sum of lines 4 to 10)**	**77.7**	**46.4**
	SFT exposures		
12	Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions	632.3	497.0
16	**Total securities financing transaction exposures (sum lines 12 to 15a)**	**632.3**	**497.0**
	Other off-balance sheet exposures		
17	Off-balance sheet exposures at gross notional amount	41.3	44.2
19	**Other off-balance sheet exposures (sum of lines 17 and 18)**	**41.3**	**44.2**
	Capital and total exposure measure		
20	**Tier 1 capital**	**2,122.3**	**2,279.0**
21	**Leverage ratio total exposure measure (sum of lines 3, 11, 16, 19, EU-19a and EU-19b)**	**7,291.6**	**7,012.9**
	Leverage ratio		
22	**Leverage ratio**	**29.1%**	**32.5%**

Table 18: Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures)

		2019 £m	2018 £m
EU-1	**Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:**	**6,540.3**	**6,425.3**
EU-3	Banking book exposures, of which:	6,540.3	6,425.3
EU-5	Exposures treated as sovereigns	1,792.1	1,775.4
EU-7	Institutions	1,262.6	1,488.2
EU-8	Secured by mortgages of immovable properties	149.1	162.2
EU-9	Retail exposures	41.8	43.1
EU-10	Corporate	812.6	962.4
EU-12	Other exposures (e.g. equity)	2,482.1	1,994.0

Appendix 3 Credit risk adjustments

Credit risk adjustments are amounts by which capital has been reduced in order to reflect losses exclusively related to credit risk under IFRS, resulting from impairments, value adjustments or provisions for off-balance sheet items that are recognised in the income statement.

Value adjustments

A value adjustment is a deduction from CET1 capital where the prudent value of financial assets measured at fair value is materially lower than the fair value recognised in the financial statements. The valuation adjustment is calculated based on the fair value of items having an impact on own funds. As at 31 December 2019 the value adjustment was £2.4 million (2018: £2.4 million).

Impairment

The Group applies an expected loss model for the calculation of impairment. Under the expected loss model, impairment losses are recorded if there is an expectation of credit losses, even in the absence of a default event. Expected credit losses are calculated on all debt instruments and loans that are not measured at fair value through profit or loss.

The Group has internal processes including consideration of internal, external, historic and forward-looking information about specific loans and securities as well as market data designed to assess the credit risk profile of its financial instruments. A three stage model is used for calculating expected credit losses which requires financial assets to be assessed as:

- Performing – financial assets where there has been no significant increase in credit risk since original recognition;
- Under-performing – financial assets where there has been a significant increase in credit risk since initial recognition, but no default; or
- Non-performing – financial assets that are in default.

For performing financial assets expected credit losses are calculated based on the credit losses that are expected to be incurred over the following 12 month period. For under-performing and non-performing financial assets, expected credit losses are calculated based on the expected credit losses over the life of the instrument.

Approaches and methods adopted for determining impairment

For financial assets held with rated counterparties, the Group calculates expected credit losses based on default information published by rating agencies and considers any known factors not yet reflected in this information.

For loans and advances to clients, the Group calculates expected credit losses based on historical credit loss experience and by taking into account the relevant Wealth Management approval authorities' current lending rates against the various types of collateral. A record is kept of all information that has or could have an impact on a client's servicing and repayment as well as of all loan exposures where collateral has decreased in value and/or quality. This record is used to identify under-performing and non-performing loans.

For trade and other receivables, the Group has established a provision matrix that incorporates the Group's historical credit loss experience, counterparty groupings and whether a receivable is past due or not.

A financial asset is past due when the counterparty has failed to make a payment when contractually due. Past due financial assets as at 31 December 2019 are presented in table 19.

Table 19: Non-performing exposures

	31 December 2019 £m	31 December 2018 £m
Up to and including 3 months	22.8	15.8
Over 3 months up to 1 year	3.9	4.2
Total	**26.7**	**20.0**

Appendix 4 Credit risk exposure segmentation

Table 20: Exposure value by geographical areas and exposure classes (£m)

	Net value (£m)										
	United Kingdom	Switzerland	United States	Luxembourg	Germany	Singapore	Japan	Hong Kong	Australia	Other	Total
Central governments or central banks	1,396.2	301.5	45.1	-	-	13.4	-	-	-	0.1	1,756.3
Regional governments or local authorities	-	-	-	-	-	-	-	-	-	-	-
Multilateral development banks	-	-	-	-	-	-	-	-	-	35.8	35.8
Institutions	555.4	140.3	26.4	41.7	59.9	57.6	131.0	41.6	40.8	196.9	1,291.6
Corporates	285.9	38.4	199.6	79.6	41.7	14.3	0.3	38.0	21.9	164.9	884.6
Retail	30.8	2.1	-	-	0.4	0.1	-	0.2	-	14.4	48.0
Secured by mortgages on immovable property	104.7	-	-	-	-	-	-	2.9	-	45.2	152.8
Exposures in default	1.8	-	-	-	-	-	-	-	-	-	1.8
Items associated with particular high risk	52.8	40.1	7.7	12.7	-	-	-	-	-	14.9	128.2
Covered bonds	68.6	-	-	-	-	-	-	-	-	-	68.6
CIUs	491.6	0.7	33.2	333.9	1.0	-	8.9	1.6	26.2	58.2	955.3
Equity	41.0	-	-	-	-	-	-	-	-	-	41.0
Other items	825.4	131.8	113.9	45.2	15.7	73.3	26.5	34.1	13.6	66.0	1,345.5
Total	**3,854.2**	**654.9**	**425.9**	**513.1**	**118.7**	**158.7**	**166.7**	**118.4**	**102.5**	**596.4**	**6,709.5**

Table 21: Net exposures by residual maturity and exposure classes (£m)

	Net value (£m)					
	On demand	<= 1 year	> 1 year <= 5 years	> 5 years	No stated maturity	Total
Central governments or central banks	1,488.4	267.9	-	-	-	1756.3
Regional governments or local authorities	-	-	-	-	-	-
Multilateral development banks	10.0	25.8	-	-	-	35.8
Institutions	1,217.6	63.9	10.1	-	-	1,291.6
Corporates	-	638.1	246.5	-	-	884.6
Retail	-	29.6	18.4	-	-	48.0
Secured by mortgages on immovable property	-	71.1	81.7	-	-	152.8
Exposures in default					1.8	1.8
Items associated with particular high risk	-	128.2	-	-	-	128.2
Covered bonds	-	-	68.6	-	-	68.6
CIUs	-	955.3	-	-	-	955.3
Equity	-	-	-	-	41.0	41.0
Other items	-	470.5	39.0	2.3	833.7	1,345.5
Total	**2,716.0**	**2,650.4**	**464.3**	**2.3**	**876.5**	**6,709.5**

Appendix 5 Asset encumbrance disclosures

Asset encumbrance arises from collateral pledged against secured funding and other collateralised obligations. The following tables disclose the median balance sheet value of encumbered and unencumbered assets during 2019 based on the requirement in Part Eight of the Capital Requirements Regulation and in the related Guideline issued by the EBA.

Table 22: Encumbered and unencumbered assets

2019	Carrying amount of encumbered assets £m	Fair value of encumbered assets £m	Carrying amount of unencumbered assets £m	Fair value of unencumbered assets £m
Assets of the reporting institution	**95.1**		**8,475.5**	
Equity instruments	-	-	36.2	36.2
Debt securities	68.9	68.9	1,978.2	1,978.2
Other assets	26.2		6,461.1	

2018	Carrying amount of encumbered assets £m	Fair value of encumbered assets £m	Carrying amount of unencumbered assets £m	Fair value of unencumbered assets £m
Assets of the reporting institution	**97.1**		**8,252.0**	
Equity instruments	-	-	33.5	33.5
Debt securities	66.4	66.4	2,013.5	2,013.5
Other assets	30.7		6,205.0	

Table 23: Collateral received

	2019		2018	
	Fair value of encumbered collateral received or own debt securities issued £m	Fair value of collateral received or own debt securities issued available for encumbrance £m	Fair value of encumbered collateral received or own debt securities issued £m	Fair value of collateral received or own debt securities issued available for encumbrance £m
Assets of the reporting institution	**-**	**551.6**	**-**	**496.4**
Equity instruments	-	-	-	-
Debt securities	-	541.4	-	496.4
Other collateral received	-	10.2	-	-
Own debt securities issued other than own covered bonds or ABSs	-	-	-	-

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