First State Investments (UK Holdings) Ltd

Pillar 3 disclosures

For the year ended 30 June 2018

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1. INTRODUCTION

The provisions of the Basel 2 Capital Accord as encapsulated in the Capital Requirements Directive ("CRD") issued by the European Union have been enacted in the United Kingdom through the Financial Conduct Authority's ("FCA") Handbook and particularly within the General Prudential Sourcebook ("GENPRU") and the Prudential Sourcebook for Banks, Building Societies and Investment Firms ("BIPRU").

This regulatory capital framework comprises three "pillars":

- **Pillar 1:** the minimum capital requirement that is required to cover credit, market and operational risk
- **Pillar 2:** a more company-specific internal assessment of risk to determine whether additional capital should be maintained against risks not covered by Pillar 1
    - **Pillar 3:** requirements for disclosure of capital, risks and risk management procedures and specific remuneration disclosures,

This Pillar 3 disclosure relates to the three subsidiaries of First State Investments (UK Holdings) Limited (together, "FSI") which are regulated by the Financial Conduct Authority ("FCA")[1].

Under BIPRU 11, FSI has adopted a disclosure policy which complies with the requirements taking into account that certain information of a confidential, immaterial and proprietary nature may not be disclosed. In these instances FSI has outlined the reason for non-disclosure.

[1] Two of these subsidiaries (First State Investment Management (UK) Limited and First State Investments International Limited) are BIPRU firms. The third (First State Investments (UK) Limited) is a UCITS management company and AIFM butis included in the capital resources elements of this Pillar 3 disclosure for completeness and transparency.

2. SCOPE OF APPLICATION

2.1 Group structure

As FSI is subject to consolidated supervision, the disclosures given under Pillar 3 are at a consolidated level for all the subsidiaries of First State Investments (UK) Holdings Limited.

FSI is part of the international operation of Colonial First State Global Asset Management ("CFSGAM"), the asset management business of the Commonwealth Bank of Australia ("CBA").

CFSGAM is a major division of CBA's Wealth Management business unit. Within CBA, Wealth Management is responsible for the manufacture and administration of non-banking services, including business units such as CFSGAM Australia, First State Investments and Stewart Investors in the UK and Asia. Wealth Management also provides strategic and operational support for the investment and insurance products of group companies.

Being a separate and dedicated business allows FSI to focus on its key strengths in wholesale asset management while developing a performance culture to attract and retain the key investment talent to underpin future growth and success.

2.2 FSI corporate structure

The three FSI group subsidiaries that are individually registered with the FCA and are subject to individual Pillar 1 capital requirements are as follows:

- First State Investments (UK) Limited
- First State Investment Management (UK) Limited
- First State Investments International Limited.

The Pillar 3 report will be made available on an annual basis based on the statutory accounts to 30 June each year.

3. RISK MANAGEMENT OBJECTIVES AND POLICIES

FSI has adopted the risk identification and assessment principles contained within the CBA Wealth Management Risk Management and Compliance, Business and Policy model. Both internal and external risks are recorded in a standardised risk register for the UK asset management business. Agreed risk weightings are ascribed to the specific risks that have been identified by the management team.

Findings of independent external reviews such as in ISAE 3402, internal and external audit reports, depositary reviews and Regulatory visit reports are considered when updating the risk register.

A Capital Management Policy is in place that governs the level of capital held by FSI. The policy requires FSI hold capital in excess of regulatory requirements.

FSI has an appropriately staffed Risk and Compliance department that is supported by the overall CFSGAM Risk Management and Compliance function. In addition, the Wealth Management business unit has a central Risk Management and Compliance team that provides support in a number of areas, including the consistent application of agreed standards that apply across the whole CBA group.

The UK Compliance and Risk team provides regular reports to the FSI Boards and committees as well as the CFSGAM Compliance and Risk Committee. The latter Committee meets monthly to oversee the internal controls and risk management processes, regulatory compliance and audit issues.

3.1 Credit risk

FSI is not subject to significant amounts of credit risk.

3.2 Market risk

Market risk only exists for the value of any investments held directly by FSI. Certain FSI group companies may hold seed capital positions in new funds at various points in time which, to date, have not been of a material amount

3.3 Business risk

FSI considers a prolonged and significant market downturn to be the single largest business risk as it will have an adverse impact on assets under management ('AUM') and directly impact revenue generated by the business.

As part of the Internal Capital Adequacy Assessment Process ("ICAAP")) various 'stress tests' are performed on the financial and capital forecasts of the firm to enable management to understand the effect on the business.

FSI has taken a number of measures to mitigate other business risks such as:

- Key system or infrastructure failure:. FSI has a fully tested Business Continuity Plan ("BCP") in place to ensure that all critical processes can be carried out within maximum acceptable outage levels. Cyber Security is a growing risk globally and the firm has implemented additional controls, training and system enhancements to ensure this external risk is mitigated as much as possible

Key fund manager retention: FSI has put in place appropriate remuneration schemes that promote retention of key individuals, strong succession planning is also conducted.

3.4 Concentration risk

Concentration risk is concerned with the possible lack of diversification of asset strategies, clients or distributors leading to the amplification of various other risk effects.

The largest asset strategies are the emerging market equity strategies managed by the Stewart Investors team. These are complemented by infrastructure, fixed income and a range of other equity strategies managed within the FSI group.

FSI has a wide client base across its products ranging from private investors investing directly, through those investing through fund supermarkets and other intermediaries, to large institutional clients. The client base is also geographically diverse. FSI does not believe there is any significant concentration risk associated with location or type of client.

FSI also has relationships with a large number of intermediaries and asset consultants, mitigating concentration risk within the group.

3.5 Operational risk

Operational risk is the risk of loss resulting from inadequate internal processes and/or failures in relation to the people and systems of the firm or from external events. It is this risk that is the most significant with regards to its potential impact on FSI.

To address this risk the firm has in place an Operational Risk Management Framework ('ORMF') which proactively manages operational risk in the business by the identification, assessment, management and reporting of risks on a consistent and reliable basis

Operational Risk is also assessed under the ICAAP process and appropriate capital is maintained against those risks deemed to be material to the business

3.6 Other risk

FSI takes into account the following additional risks as part of the ICAAP process - pension obligation risk, insurance risk, interest rate risk, liquidity risk, residual risk and securitisation risk. None are deemed material and/or relevant.

4. CAPITAL RESOURCES

FSI's Tier 1 capital was £97.1m at 30 June 2018.

The Pillar 1 capital requirement is calculated as the higher of (1) the sum of the credit risk and market risk capital requirements and (2) the fixed overheads requirement. Each of the credit risk, market risk and fixed overheads requirements are calculated in accordance with regulatory (GENPRU) requirements.

The Pillar 2 capital requirement involves a detailed assessment and capital modelling of all relevant risks the firm is exposed to whilst executing its business strategy and is documented in the firm's ICAAP process

The ICAAP process adopted by FSI is dynamic as the risks impacting the group and its capital resources change over time. The ICAAP is an integral part of a company's risk management process, integrating financial budgets and forecasts, capital planning as well as risk information and modelling.

The ICAAP is included in the FCA's supervisory review process.

The Pillar 1 and Pillar 2 capital calculations as at 31 December 2018 are set out in the following table.

FSI Capital at 30 June2018	Pillar 1 £'m	Pillar 2 £'m
Share capital and reserves	97.1	97.1
Tier 1 capital	97.1	97.1
Capital requirement	31.2	62.6
Surplus capital	65.9	34.5

All modelling has been undertaken using the most likely outcome based on past history and current experience of the business. FSI maintains an excess of capital above the most likely modelling scenarios.

The stress testing that was undertaken as part of the ICAAP considered various levels of market correction looking out for 3 years from the date of preparation.

5. REMUNERATION DISCLOSURES

5.1 Decision-making process for remuneration policy

First State Investments EMEA ("FSI EMEA") which includes the regulated entities First State Investments (UK) Limited, First State Investment Management (UK) Limited and First State Investments International Limited, operates a Remuneration Assurance Committee ("Committee"). The Committee has a mandate to:

- Make recommendations to the CBA Remuneration Committee in relation to FSI EMEA relevant personnel;
- Monitor adherence by FSI EMEA with applicable FCA Remuneration Codes as amended or replaced from time to time and the Group Remuneration Policy;
- Ensure that the Head of Risk & Compliance for EMEA has appropriate input into remuneration policy, and to consider any concerns raised by the risk & compliance function about the behaviours of code staff or risks in any business undertaken;
- Review performance management frameworks and processes; and
- Ensure that the bonus pool totals do not limit FSI's ability to build its capital base.

The Committee is comprised of the following:

- Regional Managing Director, FSI EMEA;
- Head of Human Resources CFSGAM; and
- Executive General Manager (EGM) Group Performance and Reward, as the delegate of the CBA Remuneration Committee (Current Chairman).

The Committee was first established during May 2011. There was one meeting of the Committee in respect of the 2017-2018 financial year.

5.2 External consultants

The Committee received independent advice on executive remuneration issues from PricewaterhouseCoopers (PwC) as part of an annual regulatory update. PwC also provided other consulting services to various parts of FSI. Other consultants are used from time to time to advise on specific issues.

5.3 Role of the relevant stakeholders

The Committee takes full account of FSI's strategic objectives in setting remuneration policy and is mindful of its duties to shareholders and other stakeholders. The Committee seeks to preserve shareholder value by ensuring the successful retention, recruitment and motivation of employees.

No individual can approve decisions relating to their own remuneration.

5.4 Code Staff criteria

When determining whether an individual meets the criteria for Code Staff, the following information is considered:

- The role the individual performs;
- The reporting lines for the role;
- The number of staff reporting to the role;
- Specific authority to carry out decisions under the role, any limits on authority and required sign off;
- Whether the employee/role is registered with the FCA as a Significant Influence Function;
- Whether the individual heads a business line that is accountable for a material portion of the annual revenue of FSI **and** they have a material impact on risk;
- Whether the individual is in a Control Function;
- Whether the individual is a Risk Taker for Code Staff purposes, including where the employee's business activities are able to create material levels of risk for the Company.

The determinants above result in all members of the Boards of Directors, Executive Committee and investment desk Heads being designated as Code Staff.

5.5 The link between pay and performance for Code Staff

Remuneration is made up of fixed pay (i.e. salary and benefits) and performance-related pay (short-term and long-term variable remuneration).

Short-term variable remuneration (STVR) is designed to reward performance in line with the business strategy, objectives, values and long term interests of FSI clients.

The annual STVR earned by an individual is dependent on the achievement of financial and non-financial objectives, including adherence to effective risk management.

FSI provides long-term variable remuneration (LTVR) which is designed to link reward with the long-term success of FSI and recognise the responsibility participants have in driving its future success and delivering value for shareholders. LTVR awards are conditional on the satisfaction of corporate performance measures.

The structure of remuneration packages is such that the fixed element is sufficiently large to enable FSI to operate a truly flexible variable remuneration policy.

5.6 Design and structure of remuneration for Code Staff

5.6.1 Salary and fees

All Code Staff receive a base salary to reflect their market value, responsibility and contribution to FSI.

5.6.2 Annual Incentives

Employees receive a mix of fixed and variable remuneration. Remuneration arrangements for these employees are designed to:

- Support the sustainable growth of revenue relative to costs;
- Contribute to aligning rewards to the interests of shareholders and our customers;
- Reflect the role remuneration can play in the overall risk management framework;
- Be market competitive, with reference to internal relativities;
- Be cost responsible and consider each component of remuneration as part of the totality of the arrangements, including non-financial rewards;
- Align the proportion of fixed versus at risk remuneration to the job family, impact and accountability of the role;
- Be simple to understand and administer;
- Be approved by an appropriate level within a framework of delegations by the Board; and
- Ensure employees do not receive excessive benefits on termination.

Employees are eligible for a STVR award based on their individual performance, and depending on their role, the performance of their business unit and/or the FSI group. These awards are managed within a strict risk framework, and the Boards of Directors of the FCA regulated entities retain ultimate discretion to reduce STVR outcomes where appropriate.

Executives receiving material STVR awards who do not receive deferred remuneration in the form of LTVR, maybe required to defer a portion of their STVR award for up to three years. Payment of this portion is subject to service conditions.

5.6.3 Long term Incentives

LTVR is awarded to key individuals within the business. These awards are deferred for three years and are subject to service conditions. The awards are aligned with either the business performance or the performance of the publicly available investment funds being managed by the relevant team.

5.6.4 Risk Adjustment

We actively manage risks associated with delivering and measuring short-term performance. All our activities are carefully managed within our risk appetite, and individual variable remuneration outcomes are reviewed and may be reduced in light of any associated risk management issues.

Risk management is also built into our remuneration framework. Risk is managed through the mandatory deferral of a substantial and meaningful portion of the STVR and/or LTVR of the employees with significant performance based remuneration. Rules for employees in Europe are set out in the UK Remuneration Policy and Variations supplement.

This deferral serves as an important retention mechanism which helps us manage the risk of losing key executive talent. It also provides a mechanism for the Board to reduce or cancel the deferred component of STVR.

The Committee reviews risk and compliance issues in relation to the vesting of deferred awards for all employees. Compliance is monitored throughout the vesting period by the Head of Risk and Compliance and their department, who reports the information to the Committee for assessment.

Any risk or performance issues that may impact the vesting of deferred awards are then highlighted to the Committee, along with any recommendations for the reduction or cancelation of any deferred awards (as appropriate).

5.7 Aggregate remuneration cost for Code Staff by business area

There were 33 employees identified as BIPRU Code Staff during the year.
Aggregate remuneration expenditure in respect of BIPRU Code Staff was as follows:

First State Investments
£22,386,481

5.8 Fixed/Variable remuneration

Fixed remuneration consists of base salaries for executives and benefits such as pension contributions. Variable remuneration consists of STVR and LTVR awards payable based on the performance of certain funds or the financial performance of the CFSGAM business unit or the CBA share price.

	Senior Management	Other BIPRU Code Staff
Number of BIPRU Code Staff	15	18
Fixed remuneration	£2,106,511	£2,184,783
Variable remuneration	£6,969,973	£11,125,213

Note: Sections 5.7 and 5.8 cover remuneration data for the two BIPRU subsidiary companies: First State Investment Management (UK) Limited and First State Investments International Limited