ROYAL LONDON ASSET MANAGEMENT

Pillar 3 Disclosure

Prudential Consolidation Group incorporating:

Royal London Asset Management Ltd

and

Royal London Unit Trust Managers Ltd

31 December 2019

Contents

1. Introduction

Background

The Capital Requirements Directive (‘CRD’) and Capital Requirements Regulation (‘CRR’) - usually referred to together as CRD IV - formalised the regulations for investment firms to disclose additional information relating to their risk management approach and capital adequacy. The aim of the CRD IV is to promote the market standards for information disclosures which ensure clarity, meaningfulness, consistency over time and comparability across different institutions.

The disclosure of this information is known as Pillar 3 and is designed to complement the two other pillars of the CRD, namely the minimum capital requirements (Pillar 1) and the supervisory review process (Pillar 2). The disclosure has been prepared in accordance with the requirements laid out in Section 8 of the CRR.

- Pillar 1 – Sets out the minimum capital requirements, through the application of measurement rules, of firms to cover credit, market and operational risk;
- Pillar 2 – Requires firms and supervisors to undertake an internal capital adequacy assessment process to determine whether the financial institution needs to hold additional capital against risks not adequately covered in Pillar 1;
- Pillar 3 – Complements the other two pillars and effects market discipline through public disclosure showing an institution’s risk management policies, approach to capital management, capital resources and an analysis of its credit risk exposures.

Scope of Application

The Pillar 3 disclosures set out in this document are done at the level of the prudential consolidation group comprising Royal London Asset Management Limited (‘RLAM Ltd’) and Royal London Unit Trust Managers Limited (‘RLUTM’), further referred to as ‘the RLAM Estate’. The document describes the risk management objectives and policies, processes for managing material risks, structure and organisation of the risk management functions, the scope and nature of risk reporting and measurement systems and the policies for mitigating risk.

Frequency of Disclosure

This Disclosure is based on the RLAM Estate’s Internal Capital Adequacy Assessment Process (‘ICAAP’) review dated 29/06/2020 and is subject to review and update at least annually. The RLAM Estate will reassess the need to publish some or all of the disclosures more frequently than annually in light of any significant change to the relevant characteristics of its business including disclosure about capital resources and adequacy, and information about risk exposure and other items prone to rapid change.

Disclosure is published on the RLAM's website: http://www.rlam.co.uk/Home/Footer/Pillar-3-/

Board Approval

These disclosures were approved for publication by Board of Directors of RLAM Ltd on 29/06/2020. The Board has verified that the disclosures are consistent with formal policies and are satisfied with the adequacy and effectiveness of the risk management arrangements.

Company Description

The firms forming the RLAM Estate prudential consolidation group - RLAM Ltd and RLUTM - are wholly owned subsidiaries of The Royal London Mutual Insurance Society Limited ("RLMIS").

RLAM Ltd is a key firm within the Royal London Group, managing most of the Group's assets, in addition to providing active investment management solutions to a wide range of third party institutional and wholesale clients. The firm has a diverse range of third party institutional clients including company pension funds, universities and other educational establishments, insurance companies, local authorities, medical organisations, religious bodies and charities. Our wholesale clients include wealth managers, multi-managers and discretionary fund managers, with an increasing amount of intermediary business transacted through platforms. RLAM Ltd provides asset management products and services across fixed income, equity, multi-asset, property and sustainable investments. RLAM Ltd is a limited licence IFPRU firm authorised and regulated by the FCA.

RLUTM is an Authorised Corporate Director (ACD) and an Alternative Investment Fund Manager (AIFM) of a number of investment companies and funds. RLUTM is authorised and regulated by the FCA and the Central Bank of Ireland and is authorised to carry out designated investment business and the marketing of authorised funds in the United Kingdom and in Ireland.

The RLAM Estate's organisational structure is designed to ensure strict segregation between the investment management function, client reporting and the monitoring of compliance with clients' guidelines and regulatory requirements.

2. Governance Arrangements

As part of RLMIS, the RLAM Estate is subject to the formal governance hierarchy that is in place across the Royal London Group to ensure effective escalation of issues through different business lines.

While RLAM Ltd and RLUTM are both RLMIS subsidiaries they are – strategically and operationally – managed independently from RLMIS. The governance of both legal entities is carried out through regular meetings of their respective Boards of Directors (BoD). The BoD of each legal entity within the consolidation group have the ultimate responsibility for risk management, compliance and regulatory matters and have oversight of the effective implementation of the Risk Management System ('RMS') and are responsible for effective and prudent management and periodically assess governance arrangements with a view to correcting deficiencies. Members of the BoD are selected based on relevant industry knowledge, skills and expertise to achieve this aim. The RLAM Estate recognises the need for diversity in its recruitment policy.

Whilst the RLAM Estate's strategy is formally set annually by the Boards, the strategic and business risks arising from the plan are reviewed by the the RLAM Executive Committee on a monthly basis. Additionally, various line Committees were established to assist the responsible persons in the proper performance of their duties. Individuals identified as chairs of the respective line committees have responsibility for reporting on their areas of accountability to the Board of RLAM Ltd as set out in the Matters Reserved for the Board.

The Directors who serve on the Board are:

Name	Function in RLAM Ltd	Function in RLUTM
John Brett	-	Independent Non-Executive Director
Nora O'Mahony	-	Independent Non-Executive Director
Andrew Carter	Chief Executive	Executive Director (Chairman)
Piers Hillier	Executive Director	-
Andrew Hunt	Executive Director	Executive Director
Rakesh Kumar	-	Executive Director
Steven Murray	Non-Executive Director[1]	-
Kevin Parry	Non-Executive Director[1] (Chairman)	-
Catherine Read	Executive Director	Executive Director
Ewan Smith	Non-Executive Director[1]	-
Susan Spiller	-	Executive Director
Robert Williams	Executive Director	Executive Director

The RLAM Ltd Board Risk Committee ('BRC') was formed in 2016 and meets quarterly, or more frequently if required. The BRC comprises of Executive and Non-executive Directors and is chaired by a Non - Executive Director. The main role of the BRC is to monitor and review the effectiveness of risk management and internal control system; in this capacity it approves the elements of risk management framework, receives regular reports from the Chief Risk Officer and considers issues escalated by the Business Risk Committee.

3. Risk Management Objectives and Policies

The RLAM Estate adheres to the risk management objectives and policies set out for companies within the Royal London Group. The RLAM Estate maintains a comprehensive risk management

[1] Non-Executive Directors are members of the board of directors who are not part of the executive team of RLAM and RLUTM; they may have executive roles in Royal London Group entities other than RLAM or RLUTM.

framework, referred to as the Risk Management System ('RMS'). It has clearly defined procedures for identifying and escalating risk concerns throughout the organisation. These processes help to safeguard client assets, protect the interests of all stakeholders and meet our responsibilities as a UK regulated entity.

The ultimate responsibility for risk management lies with the Board of the relevant legal entity within the prudential consolidation group. There are also a number of management committees chaired by, and consisting of, Senior Managers that have responsibility for specific areas of risk.

Senior management intend to manage the the RLAM Estate capital base so that a prudent amount of excess capital is retained above the amounts calculated for the assessed risks. The capital retained will allow the RLAM Estate to maintain and grow its business without further capital injection.

The framework is governed and structured through a variety of mechanisms that assist in ensuring employees are aware and understand their responsibilities:

- Risk is a core consideration when setting strategy, formulating business plans and managing performance;
- Implementation of a risk and control self-assessment process that facilitates the identification and assessment of risks across all business units and provides a systematic means of identifying risk and control gaps that threaten the achievement of business or process objectives;
- Establishment of an effective risk management governance structure distinguishing between management and oversight activity and accountability;
- Risk appetite is clearly articulated reflecting the level of risk that the RLAM Estate is willing to accept (or not accept) while pursuing its business objectives whilst being consistent, where relevant, with appetite set out at Group level;
- Development and implementation of risk policies and procedures.

Three Lines of Defence

The RLAM Estate's governance structure for risk management is based on the 'three lines of defence' model. Primary responsibility for risk management lies with the business. A second line of defence is provided by the Group's independent Risk and Compliance function, which reports to the Board Risk Committee. The third line of defence is provided by Internal Audit, which reports to the Board Risk Committee and provides process assurance, supported by external audit.

The RLAM Estate's governance structure is consistent with the Royal London Group 3 lines of defence model that clearly defines the ownership and responsibilities of risks:

Risk Management System

The RLAM Estate has adopted the RLMIS Risk Management System (RMS) as its framework for managing risks. The RMS is a cohesive set of components that is designed to sustain and uphold high standards of risk management throughout the Royal London Group. Components of the RMS such as the risk strategy, risk appetite and policies set out the objectives, direction, limits and tolerances within which the Directors expect the business to operate.

The key elements of the RMS are:

- Risk Appetite Framework
  The Risk Appetite Framework 'RAF' defines what is considered an acceptable risk profile and sets limits on the level and nature of risks the firm is willing to assume in achieving its strategic objectives and Medium Term Plan. The Risk Appetite Statements which precisely refer to the RLAM Estate's key risks serve this purpose and guide the decision-making process with regard to pursuing the business strategy, methods of risk management and determining whether the risk position is within our risk appetite. The RAF is subject to a periodic review performed at least annually, the purpose of which is to reassess the tolerance for material risks inherent in the business.

- Risk Metrics
  Risk metrics are defined and monitored as part of the RAF to track the nature, complexity and scale of the business activities. All risk metrics are logged on the risk system (Archer)

and reported to the relevant governance bodies on a regular basis. Any areas of concern identified through the risk metrics are escalated to the Board and an assessment is made with regard to the impact on internal capital requirement. The risk metrics are subject to a periodic review performed at least annually to reassess the main risks and tolerances.

- RCSA
  Each function within the RLAM Estate owns a risk register. The risk register owner (usually the Head of Function) is responsible for identifying all key risks inherent in the key processes operated. Each risk identified is logged on the risk system (Archer) and scored on an inherent risk basis using a 5x5 impact and likelihood matrix. The controls in place to mitigate the risks are then identified, logged and assessed for design effectiveness and performance effectiveness. The risk is then scored on a residual basis using the same 5x5 matrix. If any controls are identified as not being fully effective or any risks are not mitigated to within risk appetite, a finding is recorded and an action plan is put in place to address the situation. All action plans are tracked via the Archer risk system to ensure timely completion.

- Top Risks
  Top down risks are identified via a monthly meeting with the RLAM Estate senior management. These may include risks to achieving the RLAM Estate's medium term business plan, risks that are managed at an overall the RLAM Estate level and any key regulatory, change, and economic risks owned at the Executive level.

- Operational Risk Events
  All identified risk events are logged on the Archer risk system with the impact established and documented. All risk events are independently reviewed to ensure the accuracy and completeness of the data captured, that the action plans are robust and each event is closed in a timely manner. Data from the risk events logged is used to support the development of the Operational Risk Scenarios within ICAAP.

- Operational Risk Scenario Analysis
  Operational Risk Scenario Analysis is used by the RLAM Estate to identify and assess plausible operational risk events using a combination of the internal and external operational risk data and expert management judgement. Operational Risk Scenario Analysis looks at the risks faced by the business and potential financial impact of any of these risks materialising. Operational Risk Scenario Analysis is used to support the calculation of capital held for operational risk within Pillar 2 requirement.

Stress-testing

Stress-testing is undertaken within the RLAM Estate, as part of the ICAAP, to monitor and quantify risk and capital and ascertain whether sufficient capital resources are held against risks on a forward-looking basis. The process reflects stressed scenarios that identify an appropriate range of adverse circumstances of varying nature, severity and duration relevant to the RLAM Estate's risk profile. The conclusion of the stress testing process is the identification of the potential risks the business faces and, where appropriate, a recommendation for capital to be held against each scenario. Scenarios are derived by analysing current and emerging risks impacting the RLAM Estate as well as known external examples of stresses that are relevant to the RLAM Estate's business model.

4. Key Risks to the RLAM Estate

The RLAM Estate is required to complete a consolidated ICAAP at least on an annual basis. The ICAAP document sets out the key risks to the business and demonstrates how the RLAM Estate satisfies itself that it has sufficient capital.

The ICAAP process ensures the executive management of the RLAM Estate regularly oversee and assess:

- The company's processes, strategies, and systems;
- The major sources of risk to the company's ability to meet its liabilities;
- The results of internal stress testing of these risks; and
- The amount and types of financial and capital resources and whether they are adequate to cover the nature and level of the risks to which the RLAM Estate is exposed.

The ICAAP is used within the business to support the decision-making process, identify potential risk exposures and implement appropriate mitigants. The ICAAP is formally reviewed by the RLAM Ltd Board and is further considered as part of the annual business planning cycle. Should business plans / significant re-positioning dictate, interim reviews will be undertaken. Management information allows the Board to regularly monitor the RLAM Estate's business against the risk framework and use it to make adjustments throughout the year and whenever else this may prove necessary.

The RLAM Estate has identified and assessed the following key risks within the ICAAP:

Credit Risk

Credit risk is the loss resulting from a counterparty's failure to repay amounts in full when due. Three material sources of credit risk for the consolidation group have been identified as:

- The placement of cash deposits with banks and surplus liquidity in funds;
- Clients who owe fees for the investment management services provided;
- Fund debtor balances, held on RLUTM's balance sheet.

The RLAM Estate adopts the standardised approach to credit risk and uses Fitch ratings. These ratings are used to assess the exposure classes for cash balances held with banks. Other exposures, such as trade debtors and accrued income, are treated as unrated.

The RLAM Estate has cash balances held in 4 UK banks or invested in a Royal London UCITS fund - Cash Plus. There is explicit management oversight of the credit quality of deposit institutions and monthly review of credit worthiness of deposit institutions.

The RLAM Estate manages the risk resulting from fund debtor balances through regular monitoring and evaluating potential impact on P&L.

Concentration Risk

Concentration risk is any single or group of exposures that may have the potential to produce losses large enough to threaten firm's health or ability to maintain its core business or a material change in an institution's risk profile. This includes large (connected) individual exposures or significant exposures to groups of counterparts, whose likelihood of default is driven by common underlying factors, e.g. sector, economy, geographical location and instrument type.

The main sources of concentration risk for RLAM Estate are linked to:

- Credit concentration relating to deposits held at bank. This risk is managed by allocating deposits between 4 different banks with strong credit ratings. This reduces the risk significantly and provides assurance that the firm will maintain access to its cash balances and capital resources;
- Receiving majority of income from a limited number of clients. This risk was analysed as part of stress testing and it has been concluded that the diversification of revenue is sufficient; in particular removing any specific single stream of income (even the largest one) does not threaten the financial position of the RLAM Estate over the 5 year horizon.

Market Risk

Market risk is a risk to a firm's financial condition arising as a result of adverse movements in the markets, such as foreign currency exchange rates, interest rates, security and commodity prices.

None of the firms comprising the consolidation group trade on its own account, underwrite issues of financial instruments on a firm commitment basis, nor run proprietary trading positions. Both firms hold all their assets in bank deposits or in funds and have no material foreign exchange exposures.

Although it is common for asset management firms to invest 'seed capital' in newly launched funds, in the Royal London Group the 'seed capital' is normally provided by the parent entity – RLMIS. Market risk on the RLAM Estate's balance sheet is therefore limited to short term exposures arising from the receipt of income or payment of invoices in foreign currency which are de minimis.

Operational Risk

Operational risk is the risk of loss resulting from people, systems, inadequate or failed internal processes or from internal events (excluding strategic and reputational risk).

Operational risk may arise from errors in transaction processing, breaches of internal control systems and compliance requirements, internal or external fraud, damage to physical assets, and/or business disruption due to system failures, execution, delivery and process management or other events. Operational risk can also arise from potential legal or regulatory actions as a consequence of non-compliance with regulatory requirements, ethical or market standards or contractual obligations.

Sources of operational risk are monitored through the RMS. Components of the RMS such as the risk strategy, risk appetite and policies set out the objectives, direction, limits and tolerances within which the Directors expect the business to operate.

Liquidity Risk

Liquidity risk is the risk that adequate liquid funds are not available to settle liabilities as they fall due. The RLAM Estate's funding sources are client fees paid in arrears while its main costs are general expenses and salaries. There is a process for debtors' monitoring and clients' funding concentration has been considered in the liquidity stress testing within the ICAAP.

In line with the FCA Policy Statement 09/16 on Liquidity, the RLAM Estate has satisfied itself with the capital requirements set aside in the liquidity test projection and has considered the costs in winding down its business in the context of a liquidity problem. The firm operates within a liquidity policy which is measured and reported each month to the Chief Finance Officer. Should a liquidity crisis arise, the Board has approved a contingency funding plan which does not rely on parental support for capital or liquidity.

Interest rate risk arising from non-trading activities

Interest rate risk is the risk that fair value of future cashflows will fluctuate because of changes in market interest rate.

The main sources of interest rate risk for the RLAM Estate are risks to earnings and capital arising from:

- adverse movements in interest rates relating to cash deposits and investments in funds;
- adverse changes to market value of assets the RLAM Estate manages which may impact the levels of management fees earned.

Interest rate movements have been included within the stress-testing and assessed through scenario analysis alongside market movements.

Pension obligation risk

Pension risk is the risk resulting from the firm's contractual or other liabilities with respect to a pension scheme.

RLAM Estate previously participated in the Royal London Group Pension Scheme (RLGPS). The scheme closed to future accruals on 1 April 2016. The responsibility for cash injections arising as a result of the Trustees' funding decisions, Section 75 employer debt provisions or any other reasons has been with the RLMIS. In any event, the RLAM Estate might be allocated a proportion of costs in respect to its employees who have participated in RLGPS. At the end of 2019, the scheme had a funding surplus therefore no capital injections were required. The RLMIS ICA assessment continues to set aside capital against pension obligation risk therefore there is no additional capital provision held for this risk in the RLAM Estate.

Contagion risk

Contagion risk is the risk that the financial position of the firm could be adversely affected by its relationship with other entities in the same group or by risks which may affect the financial position of the whole group.

Royal London Group offers diverse product ranges and operates across a number of market sectors. Different legal entities forming the Royal London Group do not reflect a uniform front that would be materially impacted by contagion. As a result of the Royal London rebranding campaign, legal entities within the group operate under the same brand. It is recognised that in case of a reputational event and subsequent negative publicity relating to the Royal London brand, there could be some impact on the RLAM Estate and its business, mostly in a commercial sense. The RLAM Estate has built a strong position as an investment manager, supported by a good performance history, is not reliant on the Royal London Group for financing and has adequate risk management processes in place to ensure mitigation of such risk.

All of the Companies within the Group set aside appropriate risk capital within their individual ICAAP submissions, or within the RL Group Solvency II submission.

Reputation risk

Reputation risk is defined as the risk of damage to the firm's reputation that could lead to negative publicity, costly litigation, a decline in the customer base or the exit of key employees and therefore directly or indirectly leading to a loss of revenue. The RLAM Estate's reputation is a fundamental tenet of its business and success.

Potential exposure to reputation risk is reduced by having a well-established control environment which ensures compliance and adherence to the regulatory, market and ethical obligations, both imposed on the firm and required by the Board. The RLAM Estate's aim is to ensure that the services it carries out are of the highest standard at all times and also ensuring the risk of reputation damage is significantly reduced by the effectiveness of the controls it has in place. To this end the RLAM Estate has considered a number of scenarios regarding behaviour, communications, marketing and client reporting where an action (or inaction) could precipitate the loss of goodwill in clients and/or market reputation.

Regulatory Risk

Regulatory risk is related to the effect a change in regulations or legislation may have on a firm or the way it is carrying out its business, as well as the risk of a regulatory fine as a result of being non-complaint with the regulatory requirements.

Within the consolidation group a Regulatory Change Steering Group has been set up to ensure that new legislation and regulatory requirements applicable to the RLAM Estate are identified and their impact on the business is assessed. Monitoring of change regulatory projects takes place in various governance forums across the consolidation group and relevant Management Information are reported to the Board periodically. The RAF includes metrics relating to change and regulatory projects which are reported quarterly to the RLAM Ltd Board Risk Committee and monthly to the Business Risk Committee.

5. Capital Requirements

Calculating Capital requirements

The minimum capital requirement for the RLAM Estate prudential consolidation group is determined as the higher of Pillar 1, Pillar 2 and the net cost of the wind-down:

- The Pillar 1 requirement is calculated as the higher of the fixed overhead requirement (FOR) and Credit and Market risk. For the RLAM Estate consolidation group, the Pillar 1 has been set by the FOR of £25.6 million.
- Pillar 2 capital requirement is estimated as part of the annual ICAAP. The minimum Pillar 2 capital requirement has been determined to be £113.5 million; the ICG-adjusted requirement is £114.2 million.
- The RLAM Estate has defined a wind-down plan covering the prudential consolidation group. The net cost has been calculated as part of the annual ICAAP to be £46.1 million.

		Pillar 1 (in £m)	Pillar 2 (in £m)	Wind-down
Consolidated requirement	Credit Risk	10.3	12.8	-
	Market Risk	0.2	0.2	-
	FOR	25.6	n/a	-
	Operational Risk	n/a	100.5	-
	The RLAM Estate Total	**25.6**	**113.5**	**46.1**

Capital Resources

At 31 December 2019 and throughout the year, all legal entities within the RLAM Estate prudential consolidation group complied with their individual capital requirements as set out by the FCA. The table below summarises the total capital at a Group level as at 31 December 2019.

Capital resources[2]	Group £m
Tier 1	
Permanent share capital	2.6
Profit and loss account and other reserves	189.4
Interim net losses	-
Deductions from Tier 1 Capital	-
Total Tier 1 after deductions	**192.0**
Tier 2	-
Total Capital before deductions	192.0
Deductions from total capital	-
Total own funds	**192.0**

The Board has concluded that the RLAM Estate has sufficient financial resources in terms of both capital and liquidity to ensure that there is no significant risk that its liabilities cannot be met as they fall due. The Directors firmly believe that capital charges do not represent an effective substitute for adequate and effective risk management processes. In this context senior management have reviewed the existing business control environment to make sure it is continuously improving and that risks are managed in a comprehensive and robust manner.

6. Remuneration Disclosure

The remuneration policy of the RLAM Estate is under the oversight of the Group's Remuneration Committee. Information on the remuneration policy, the link between pay and performance, and quantitative information can be found on the Royal London website:
http://www.royallondon.com/about/corporategovernance/remuneration/

Contact:
Mr. John Nicol
Chief Risk Officer
Phone: 020 7506 6500

[2] Tier 1 capital comprises of share capital, share premium, profit and loss and other reserves. Tier 2 capital includes revaluation reserves; RLAM Estate does not utilise any Tier 2 capital or debt funding.