

**DIAM International Ltd.**

**Pillar 3 Disclosure**

**As at 31<sup>st</sup> December, 2009**

**Registered Company Number: 3472865**

**Financial Services Authorisation Registration Number: 186147**

## **Purpose of disclosures**

This document sets out the Pillar 3 market disclosures for DIAM International Ltd. (“DIAM”).

The EU Capital Requirements Directive 2006 (the “Directive”) is implemented in the U.K. by the Financial Services Authority (“FSA”) through the General Prudential sourcebook (“GENPRU”) and Prudential sourcebook for Banks, Building Societies and Investment Firms (“BIPRU”). The Directive is the common framework for implementing Basel II in the European Union. The framework consists of three pillars:

Pillar 1 sets minimum capital requirements to meet the firm’s credit, market and operational risk using standard criteria.

Pillar 2 is the Internal Capital Adequacy Assessment Process (‘ICAAP’) whereby the firm’s senior management assesses whether additional capital above Pillar 1 capital requirement is required to cover the potential risks identified by the firm.

Pillar 3 requires disclosure of specified information about a firm’s risk and capital management, including capital adequacy.

The purpose of Pillar 3 is to encourage market discipline by developing a set of disclosure requirements which will allow market participants to assess key pieces of information on a firm’s capital, risk exposures.

The rules in BIPRU 11 set out the rules for Pillar 3. The rules provide that we omit one or more of the required disclosures if we believe the information is immaterial. Materiality is based on the criterion that the omission or misstatement of any information would be likely to change or influence the decision of a reader relying on that information.

## **Background to DIAM**

DIAM is a company incorporated under the laws of England and Wales and is authorised and regulated by the Financial Service Authority (“FSA”). The firm is engaged in investment management and advisory business providing services to institutional investors.

The firm is categorised as a limited license firm by the Financial Services Authority for capital purposes. It reports on an unconsolidated basis.

DIAM is a wholly owned subsidiary of DIAM Co., Ltd., a global asset management company registered in Japan.

## **Risk governance within DIAM**

DIAM is committed to implementing a firm-wide governance and risk management framework appropriate to the size, nature and complexity of the business. The governing body for the risk framework within DIAM is the Board of Directors (the “Board”) which has the ultimate responsibility for managing and controlling risk.

## **Risk management**

DIAM’s risk management framework along with policy and objectives are reviewed at least annually and presented to the Board. During the year all senior management have a direct reporting line to the Chief Executive Officer so that communication and early discussion of the risk framework and all risk areas is strongly encouraged and appropriate action taken.

Senior management are accountable for the identification of material risks assumed in their areas of responsibility.

DIAM believes that a strong control environment is important in ensuring that the management of key risks is effective and therefore DIAM has an Internal Audit department to review processes and controls throughout the year. Internal Audit also has a responsibility to improve risk management by facilitating and challenging the management of key risks.

External reporting accountants also review controls within the 'Report on Internal Controls-AAF01/06'.

### Capital resources

The regulatory capital requirement for DIAM as at 31 December 2009 is £1, 862k. The actual capital held by DIAM as at 31st December 2009 is £12, 809k, which gives a surplus of £10, 947k.

DIAM's capital resources as at 31st December 2009 are shown in the table below:

| <b>Tier</b>    | <b>Element</b>                        | <b>(£'000)<br/>31<sup>st</sup> Dec 09</b> |
|----------------|---------------------------------------|---|
| <b>Tier 1:</b> | Permanent Share Capital               | 4,000                                     |
|                | Profit and loss and other reserves    | 8,809                                     |
|                | <b>Total Tier 1 Capital</b>           | 12,809                                    |
| <b>Tier 2:</b> | <b>Total Tier 2 Capital</b>           | 0   |
|                | <b>Deductions from total capital</b>  | 0   |
|                | <b>Total capital after deduction</b>  | 12,809                                    |
|                | <b>Regulatory capital requirement</b> | 1,862                                     |
|                | <b>Surplus</b>                        | 10,947                                    |

### DIAM's approach to assessment of capital adequacy

The firm maintains sufficient capital to meet UK regulatory requirements. In line with these requirements, the firm maintains the higher of Pillar 1 and Pillar 2 (ICAAP) capital requirements. The adequacy of the capital held by DIAM is assessed, at least annually, as part of the Individual Capital Adequacy Assessment Process (ICAAP) and is subject to formal sign off by the Board.

#### Pillar 1 capital calculation

Based upon its regulatory permissions and scope of activities, the firm is subject to the capital requirements for a limited licence firm. DIAM's pillar 1 capital is based on the Fixed Overhead Requirement (FOR), being higher than DIAM's Credit Risk plus Market Risk exposure.

|                                  | <b>Calculation Method</b>   |
|----------------------------------|---|
| Credit risk                      | The firm uses the standardised approach, under which the capital requirement is calculated as 8% of the risk weighted exposure amounts as set out by the FSA. |
| Market risk                      | The firm calculates its market risk capital requirement using the foreign currency PRR method set out in the FSA's rules.                                     |
| Fixed Overhead Requirement (FOR) | The FOR is calculated as 13 weeks' fixed expenditure based on financial statements as at 31 <sup>ST</sup> December, 2009.                                     |
| <b>Pillar 1</b>                  | Higher of the sum of the credit and market risk charges; and the FOR.   |

### *Pillar 2 (ICAAP)*

DIAM's ICAAP assesses the amount of capital required to mitigate the risks to which DIAM is exposed over a 12 month time horizon. The ICAAP consider the impacts of future business plans as well as potential adverse scenarios (such as market downturns or operational errors) on the capital resources of DIAM, to ensure regulatory capital requirements are met at all times.

The firm's exposure to risk categories as defined by the FSA and DIAM's strategies with respect to material risk categories is shown below:

| <b>Risk type</b> | <b>Treatment</b>   |
|------------------|--|
| Operational Risk | <p>Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people, systems or from external events (such as regulation) and includes legal and financial crime risks. DIAM management have reviewed operational risk scenarios to ensure that all possible impacts have been considered. The following operational risks have been considered within the review:</p> <p><i>Poor performance affects ability to generate profits</i></p> <p><i>Effect of key fund manager leaving</i></p> <p><i>Effect of not complying with customer mandates</i></p> <p><i>Effect of customer claims or legal action against firm for not providing appropriate advice</i></p> <p>Central to the management of Operational risk is the monitoring of key controls. The firm also has a programme of insurances designed to reduce its liability exposure to protect its assets.</p> |
| Market Risk      | <p>Market risk is defined as the risk of loss arising from fluctuations in values of, or income from, assets or arising from fluctuations in foreign exchange rates.</p> <p>DIAM does not trade on its own account and therefore does not create any market risk requirement in respect of its own business. The risk is the exposure to foreign exchange fluctuations due to investment management and advisory fees being denominated in currencies other than sterling. The firm enters into forward foreign exchange contracts to hedge the foreign currency risk.</p>   |
| Credit Risk      | <p>Credit risk is defined as the risk of loss caused by the failure of counterparty to perform its contractual obligations. DIAM only places its funds on short term deposit with a Group institution having a minimum credit rating of A1/P1.</p>   |

|                 |   |
|-----------------|---|
| Liquidity Risk  | <p>Liquidity risk is defined as the risk that the firm, although solvent, either does not have sufficient available resources to enable it to meet its obligations as they fall due, or can secure them only at excessive cost.</p> <p>DIAM maintains a surplus of liquid resources sufficient at all times to meet any immediate requirements it could prudently foresee. Liquidity is available in the form of cash which is invested in short-term bank deposits to ensure that it is available as required.</p>   |
| Reputation Risk | <p>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 to a loss of revenue.</p> <p>The maintenance of DIAM's reputation is a key component of its ability to achieve its strategic objectives. Some of the key events which could significantly impact the reputation of DIAM include poor performance, general adverse market conditions, high profile operational risk events such as market abuse or the loss of high profile key people.</p> <p>DIAM monitors the potential reputational impact of all risk categories and takes appropriate action to prevent and manage the kinds of events which may give rise to reputational damage. This is achieved through putting in place frameworks and controls around both performance of the funds and operational risks and monitoring of the effectiveness thereof.</p> <p>It is the responsibility of the Board to identify areas of the business or external factors which may significantly affect the reputation of DIAM and to ensure that these are adequately managed.</p> |