# Key risks and mitigations

### Our approach to risk management supports our strategic priorities

We are exposed to a variety of risks as a result of our global business activities. Effective risk management is a core competence and we actively monitor the potential impact of current and emerging risks. This was particularly important in 2020 given the market turbulence caused by Covid-19. We place significant focus on the integrity and good conduct of employees and doing the right thing for our stakeholders. Our risk management framework is underpinned by a strong control culture with clear oversight responsibilities.

## Managing risk

The Board is accountable for risk and oversight of the risk management process. It assesses the most significant risks facing the business and also uses quantitative exposure measures, such as stress tests, where appropriate, to understand the potential impact on the business. Non-executive oversight of the risk management framework process with respect to standards of integrity, risk management and internal control is exercised through the Audit and Risk Committee. We embed risk management within all areas of the business at a Group and legal entity level. The Group Chief Executive and Group Management Committee (GMC), as the principal advisory committee to the Group Chief Executive, have responsibility for regularly reviewing the key risks we face. This includes their respective business areas identifying, monitoring and reporting in all legal entities on relevant risks and controls. They are also responsible for monitoring that individual behaviours reflect the culture and core values of the business. It is the responsibility of all employees to uphold the control culture of Schroders.

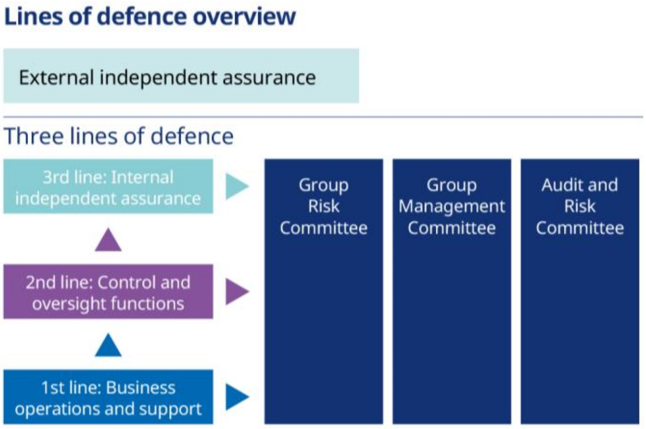
The executive oversight of risk is delegated by the Group Chief Executive to the Chief Financial Officer. The Chief Financial Officer has responsibility for the risk and control framework of the Group. Independent monitoring and reporting of risks and controls across the Group and at a legal entity level is undertaken by the second line. The Chief Financial Officer chairs the Group Risk Committee (GRC), which normally meets ten times a year. The GRC supports the Chief Financial Officer and GMC in discharging their risk management responsibilities. The committee is attended by the heads of Group Risk, Compliance, Legal and Internal Audit, chief operating officers and chief administrative officers from across the business, and senior management from Distribution, Investment, 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 is supported by a number of sub-committees, including the Conflicts of Interest committee and the Group Regulatory Oversight committee, which review and challenge risks and report significant risk matters to the GRC.

## Lines of defence

The first line of defence against undesirable outcomes is the business functions themselves and the line managers across the Group. 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, including through the Risk and Control Assessment process.

Line management is supplemented by oversight functions, including Group Risk, Compliance, Legal, Governance, Finance, Tax and HR, which constitute the second line of defence. The compliance assurance 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.

We maintain comprehensive insurance cover with a broad range of policies covering a number of insurable events.




## Risk appetite

Risk appetite statements are set by the Board and cover all our key risks (excluding strategic risk as this risk type mainly comprises factors that are external to our operating model). They apply to Asset Management, Wealth Management and the Group itself. Tailored versions of the risk appetite statements have been created for some of our legal entities.

Each risk appetite statement is supported by a number of metrics and tolerances to quantify risk appetite and to enable us to provide an assessment of risk position against risk appetite. Risk position versus appetite is formally assessed on an annual basis and is reviewed and challenged by the GRC, GMC and Audit and Risk Committee prior to the Board.

The risk appetite statements and their supporting metrics and tolerances were reviewed in 2020 and a number of improvements were made. New metrics were added to reflect the changing business environment and to allow a more quantified assessment of risk.

## Covid-19 response

Our response to the pandemic demonstrated the resilience of our employees and the strength of the infrastructure supporting our business processes. Our people worked extremely hard to meet our clients' needs and our systems coped well. There was no significant impact on business operations despite a significant number of staff working remotely at various times over the year. Prior to 2020, we had already started to evolve our Business Continuity Strategy primarily to a work from home model, with an initial focus on our London office. As changes to our infrastructure had already been made, we were very well positioned to switch to working from home with minimal disruption.

**Key highlights from our Covid-19 response**

Our response was governed by the Crisis Management Team (CMT) which met regularly from January to May. A key focus of the CMT was protecting the welfare of our employees and ensuring we could continue to deliver the standard of service our clients expect. The central co-ordination of the response by the CMT, combined with the response of regional Incident Management Teams and a level of office autonomy, meant we were able to flex our approach at a regional and office level dependent on government guidance and level of infection.

Our systems performed well and our IT environment remained stable throughout the pandemic. In order to further support colleagues who were working from home, we increased our internet capacity from 2GB to 10GB. We also enhanced our remote working capabilities through upgrading our virtual conferencing capabilities and rolling out a collaboration platform.

The delivery of the annual business continuity programme is reliant on a framework of business continuity co-ordinators and plan owners across the business. They played a key role in our response by ensuring effective co-ordination of activities across the business, which included capturing any additional technology requirements for home working and delivering our minimum viable presence approach (i.e. ensuring those staff who performed critical activities which could not be undertaken from home were in the office).

We quickly identified key suppliers who, if impacted by Covid-19, could potentially have the most significant impact upon our own operations. For a six-week period, we implemented daily reporting from key suppliers. Once it was established that service performance was being maintained and any potential significant risks had been mitigated, the reporting moved to weekly and then monthly.

Our Risk and Control Assessments, already a core part of our operational risk framework, were key in enabling us to quickly assess the extent to which business processes and controls were impacted by the need to work from home, and therefore required additional or amended controls.

We supported our employees by sending approximately 900 laptops, monitors and other hardware to their homes, allowing them to maintain productivity.

Elevated liquidity risks, particularly during March 2020, highlighted the importance of our robust fund liquidity risk management framework. We were able to promptly identify, report and escalate areas where liquidity risk was heightened. We operated a cross-functional Liquidity Management Oversight meeting for information sharing, escalation of concerns and resolution of issues.

In consideration of the heightened market volatility we moved to more frequent monitoring of certain investment risk metrics and held more regular oversight meetings to review the risk and performance of portfolios. In addition, our Group Pricing Committee met regularly to consider pricing and valuation issues caused by the volatility.

We strengthened our communications to employees to help them feel supported and engaged. Our internal communications and employee interactions remained a key focus throughout 2020.

Our global offices were reconfigured to meet local government guidelines thereby allowing staff to safely return when and where this was permitted and appropriate.

## Group Policies

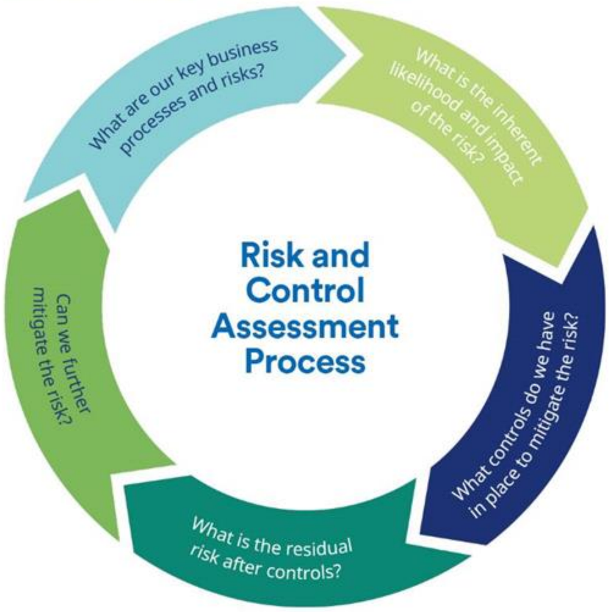
Our control framework is underpinned by a set of Group policies, which are reviewed annually to ensure they remain relevant. Our approach is to have simple, principles-based policies that are adopted across the Group. This means our employees are supported with clear guidance on what they should and should not do, while similarly our service providers are briefed on the standards we expect them to adhere to. The Group policy framework helps our newly acquired businesses understand the culture of the Group and the parameters within which we expect them to operate.

## 2020 Developments

Whilst Covid-19 dominated much of the year, a number of other initiatives were undertaken during 2020 by Group Risk. Some of these are summarised below:

- A formal Operational Resilience Programme was established to build on our existing resilience capabilities. As part of this our key business processes are reassessed and stress tested to ensure we can continue to operate during extreme events.
- Alongside Information Security, we enhanced our data loss prevention approach through improvements to controls and data surveillance capabilities.
- The Risk and Control Assessment Process (summarised in the diagram below) continues to be a key part of our operational risk framework and assisted with our response to Covid-19. We improved the alignment of the Risk Event process and our Risk and Control Assessment Process to update the documentation of controls with the goal of minimising the re-occurrence of Risk Events.
- The Asset Class Risk & Performance Committees were enhanced by improving processes to review performance and by applying a broader range of methods for overseeing exposure concentrations. These committees are the primary venue for the first and second line functions to review and challenge risk and performance.
- We developed ESG risk toolkits for the investment risk assessment of portfolios. These are used for day-to-day risk oversight and formal review and challenge at the Asset Class Risk & Performance Committees.
- We conducted thematic investment risk reviews including active risk taking in portfolios and liquidity risk management.
- Our credit risk monitoring processes were enhanced with the addition of a new external provider that aggregates internal credit ratings from large banks and produces consensus ratings.
- A portal for identifying and monitoring negative news relating to counterparties was implemented to strengthen our credit risk management processes.
- We developed a dashboard for monitoring the governance arrangements associated with User Defined Tools. A User Defined Tool is a technology application created or modified outside the core Technology function.

Risk and Control Assessment Process



## Key risks

### Assessment of key risks

We periodically assess the risks faced by our business and update the detail of the Group's key risks. This provides us with a good understanding of the risk profile of the Group, enabling our risks to be managed effectively. We have 19 key risks across Strategic, Business and Operational risk categories.

These risks have been assessed in light of the current environment (including Covid-19), geopolitical factors, market conditions, changing client demand and regulatory sentiment. We have taken into consideration the views of subject matter experts and risk owners within the business, and the working environments faced by our employees around the world. We monitor internal and external environments to identify new and emerging risks. We then analyse each risk and assess how this can be managed and mitigated.

The Group determines which key risks it considers to be heightened, for example those that are more costly if they materialised, and we then undertake further work to manage these actively. When considering these risks, we take into account the objectives of regulators to ensure market integrity, good conduct, appropriate consumer protection and the promotion of competition within the industry.

The following Key Risks are ranked within each category based on our combined assessment of the impact and likelihood of each occurring after our controls are applied.

### Strategic risks

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

| Risk | Description | How we manage risk |
|---|---|---|
| 1. Changing investor requirements | Client requirements are evolving rapidly. Failing to adapt or evolve our business model and product range to reflect these changes could lead to a drop in AUM.<br>This is notable in the Solvency II driven investment requirements of clients and the move from Defined Benefit to Defined Contribution pensions for example.<br>ESG is a material part of our client considerations and we expect climate change risks to feature more heavily in future investment requirements and offerings. | We have intensified our focus on ESG by ensuring our investment criteria includes integration of ESG into the decision process, subject to local requirements, and we have launched thematic products related to Climate and Energy Transition. We continue to expand our capabilities in Private Assets & Alternatives, including a majority interest in an Asian-based Real Estate business, Pamfleet. Seed capital has been deployed in 22 new funds during 2020. We carefully manage our cost base to reflect our clients' changing asset allocation requirements investing in new products where client demand exists. |
| 2. Fee attrition | Fee attrition caused by clients allocating more of their assets to passive products and a lower allocation to public markets, and a smaller pool of capital allocated to active fund managers resulting in increased competition on price.<br>A move towards vertical integration can also impact revenues of investment managers as the pricing power may reside with the organisations that have the end client relationship. | We have continued to focus on Solutions and outcome-oriented strategies, and Private Assets & Alternatives, which diversify our fee income, increasing our AUM by £51 billion in these areas over the year. We are also increasingly diversifying our product offering, supporting long-term profitability. |

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| Risk | Description | How we manage risk |
|---|---|---|
| 3. Market returns | Our income is derived from the value of assets we manage. Falling markets reduce our AUM and therefore impact revenues. Market falls may be exacerbated by geopolitical risks and the currency in which the AUM is denominated.<br>Current economic uncertainty with slowing global economies may also impact markets. The response of central banks may have a dependency on fiscal measures which could impact market returns. Greater co-operation across central banks may be required, at a time when economies are becoming more inward looking. Capital investment may be targeted at domestic growth rather than being allocated to cross border initiatives. | We have diversified income streams across a range of markets to mitigate falling markets in any one area. We now have 54% of AUM from Solutions, Private Assets & Alternatives and Wealth Management up from 51% in 2019.<br>Our focus on growing our Private Assets & Alternatives product range allows us to have a broader range of income streams which are less directly linked to markets. We have made key hires and management appointments in this part of the business to strengthen our leadership and drive growth in our product offering. The further development of our Wealth Management business, including the acquisition of Sandaire, a London-based family office, enables us to leverage the greater longevity and higher more sustainable margins that come with this business. |
| 4. Business model disruption | Our business model could be disrupted by a range of external factors including technology advancements, product evolution and market participants.<br>We see mass customisation of products coupled with changes in regulation such as the value assessment, requiring a response from asset managers, in addition to an increasing move to private markets. | We continue to deliver efficiencies and insights through technology. Digital initiatives are in progress to improve client experience, engagement and servicing. We are investing in our technology platform to support scalability, agility in our product offering and our expanding Private Assets & Alternatives business. A key focus on leveraging data by our Data Insights Unit has supported this. |

## Business risks

**Impact for Schroders**: 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.

| Risk | Description | How we manage risk |
|---|---|---|
| 5. Reputational risk | This may arise from poor conduct, judgement or risk events due to weaknesses in systems or controls. The reputation of Schroders can be impacted by any of our key risks. | We consider reputational risks when initiating changes to our strategy or operating model and maintain high standards of conduct. |
| 6. Investment performance risk | There is a risk that portfolios may not meet their investment objectives or that there is a failure to deliver consistent performance. | We have clearly defined investment processes designed to meet investment targets within stated parameters, which are subject to independent review and challenge.<br>Oversight of both risk and performance is embedded in our business processes and governance. |

| Risk | Description | How we manage risk |
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| 7. Climate change risk | A failure to understand the pricing of assets affected by climate change due to declining cash flows from industries or a lower demand for impacted assets. This may lead to poor investment decisions, more volatile pricing as asset prices adjust to reflect the increasing regulation of carbon emissions and a failure to offer climate positive products impacting our performance, brand and reputation. | We have developed a range of proprietary tools to better understand the impacts of climate change on the portfolios we manage including a physical risk model and a transition risk model.<br>We assess our corporate exposure to physical climate change risks and that of our supply chain and we actively monitor our emissions and have adopted targets to reduce our carbon footprint. |
| 8. Financial instrument risk | We face market, credit, liquidity and capital risks from the instruments we use when managing AUM, as well as those arising from holding investments where we act as principal. The impact of financial instrument risks on our business may negatively affect our earnings (due to market, credit or liquidity risk) or ability to invest in our business (due to insufficient capital). | We manage capital, liquidity and the Group's own investments through Board-set limits and in the Group Capital Committee. Equity market risk in seed capital is hedged where it is economic and practicable to do so and foreign currency Group investments are hedged back to sterling.<br>We monitor our credit and counterparty exposure in the Group balance sheet, bank lending portfolios and in our client assets. |
| 9. Product risk | There is a risk that our product offering is not suitably diversified, or does not provide access to strategies that will help investors to meet their objectives. There is also the risk that products are not accurately described, or that they do not perform in alignment with their investment objective(s) for a sustained period.<br>There is also the risk that product liquidity is not consistent with the product description, or the redemption requirements of investors. | Our dedicated Product and Solutions function focuses on strategy, innovation and changing investor requirements.<br>In the first instance, identified risks are managed within the formal Product Governance Framework, which includes the Product Strategy Committee, Product Development Committee, Product Governance Committee and Capacity Committee.<br>We have a liquidity risk management framework and monitor the liquidity of our products on an ongoing basis. |
| 10. Business concentration risk | Insufficient diversification in distribution channels, products, clients, markets, or income streams could pose a risk to our business. | We have a broad range and scale of products, distribution and investment channels and our development of strategic relationships and acquisitions enables further diversification of income streams. |

### Operational risks

**Impact for Schroders:** 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.

| Risk | Description | How we manage risk |
|---|---|---|
| 11. Conduct and regulatory risk | The risk of inappropriate conduct, conflicts management practices or behaviours negatively impacting on client outcomes or markets and participants, or of failing to comply with existing or new regulations. This includes financial crime requirements. | We promote a strong compliance culture and seek to maintain good relationships with our regulators. We also encourage appropriate conduct and regulatory compliance via our conduct risk framework supported by compliance assurance programmes. |
| 12. Process risk | The risk of failure of significant business processes, such as mandate compliance, trade execution for investment portfolios, client suitability checks, financial crime risk management and asset pricing. | Our key business processes are regularly reviewed and the risks assessed through the Risk and Control Assessment Process. When we undertake change, such as acquisitions, we assess new processes that may arise. |
| 13. Business services resilience risk | The risk that we are unable to operate critical business services. | Our crisis management, business continuity and disaster recovery processes are tested regularly to ensure that we can respond and recover from extreme events. |
| 14. Information security risk | The risk that our technology is compromised or inadequate, resulting in the confidentiality, integrity or availability of our data or Schroders' services being negatively impacted. | We have a dedicated Information Security function responsible for the design and operation of our information security risk framework. Information security risk is overseen by specialists within both the second and third line of defence and is monitored by the Information Security Risk Oversight Committee. |
| 15. Fraud risk | Fraud could arise from any attempt to defraud the firm or our clients by circumventing our processes and controls. | Controls are in place, which are assessed as part of the Risk and Control Assessment Process. We continue to apply particular focus to our payment processes. |
| 16. Legal risk | The risk that we, our clients, suppliers or other third parties fail to meet or record legal or regulatory obligations. | Our policies and procedures consider legal risk as part of their design. We have an escalation process for areas of material risk and our Legal function supports our employees and the business. |
| 17. Technology risk | A change or failure in technology could pose a risk to the integrity or availability of the services we offer. | Policies and technical standards are deployed, together with robust project and change management processes, which cover the assessment of business requirements, risk and scalability. |

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| 18. Tax risk | We and the funds we manage are exposed to tax compliance, reporting and transactional risks, which include the submission of late or inaccurate tax returns. | Our tax strategy sets out our approach to managing our tax affairs, underpinned by a governance framework and supported by the Tax function, which works with management and advisers to monitor our position and relevant tax changes. |
| 19. People and employment practices risk | The inability to attract, retain or develop key employees to support our business or maintain high standards in employment practices. | We have competitive remuneration and retention plans and build depth and strength in our workforce. We have sustainable succession and employee development processes and recruit selectively through our entry-level and experienced hire programmes. |