

Key risks and mitigations

The Group is exposed to a variety of risks as a result of its business activities. 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 staff and the risk management framework is underpinned by a strong ethical culture with clear oversight responsibilities. This section explains how we control and manage the risks in our business. It outlines key risks, how we mitigate them and our assessment of their potential impact on our business in the context of the current environment.

Managing risk

The Board is accountable for risk and oversight of the risk management process. It considers the most significant risks facing the Group and also uses quantitative exposure measures, such as stress tests, where appropriate. Non-executive Director oversight of the risk management process with respect to standards of integrity, risk management and internal control is exercised through the Audit and Risk Committee.

It is the responsibility of all employees to uphold the control culture of Schroders. We embed risk management within all areas of the business. Members of the Group Management Committee (GMC) have risk management responsibility for their respective business areas and we expect individual behaviours to mirror the culture and core values of the Group.

The Group Chief Executive and the GMC, as the principal executive committee with responsibility for the monitoring and reporting of risk and controls, regularly review the key risks facing the Group.

The executive Director 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 and independent monitoring and reporting of risks and controls is supported by the Group Head of Risk.

The Chief Financial Officer chairs the Group Risk Committee (GRC) which meets ten times a year. The GRC supports the Chief Financial Officer 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.

Lines of defence

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 and 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.

Group 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.

Schroders maintains comprehensive insurance cover with a broad range of policies covering a number of insurable events.



2017 developments

Management of our key risks has remained a priority throughout 2017. In particular, we have focused on further enhancing our operational risk framework and embedding conduct risk management in our business lines.

Specific initiatives were undertaken which cover a wide range of activities across the Group and are outlined below:

- We enhanced our skills and experience in the UK, US and Asia Pacific to ensure a smooth transition to our new front office technology platform which will provide a more comprehensive risk management capability.
- As an integral part of the corporate investment process, we have worked alongside our business teams performing due diligence on inorganic opportunities to fully assess the risks.
- We expanded our risk framework to consider our growing business activities in China, including our Wholly Foreign-Owned Enterprise.
- We performed ongoing monitoring of our risk appetite measures and metrics and enhanced these in certain areas, such as information security.

- Through our Information Security Risk Oversight Committee, we have developed risk appetite metrics to ensure we remain in a good position to manage cyber threats. We commissioned an external review of our security framework, including governance, capabilities and strategy, to ensure the inventory of planned enhancements remain appropriately prioritised.
- We performed further work to consider model risk and to manage user developed tools. We have also developed an approach to assess the risks when we deploy robotics, as this is a key business initiative for us.
- The Risk and Control Assessment (RCA) process continues to be a key part of our Risk Management Framework and is summarised in the diagram below. In 2017, we broadened the range of risks that are included and assessed within RCAs to provide a more comprehensive assessment. To support this activity we are upgrading our technology to manage RCAs, which will improve our aggregation, oversight and reporting.

Risk and control assessment process



Key risks

Assessment of key risks

We have identified 21 key risks across Strategic, Business, Financial and Operational risk categories.

These risks have been assessed in light of the current environment, taking into consideration the views of subject matter experts and risk owners within the firm, market conditions, regulatory sentiment and changes within the business. Threats with uncertain impact, probability and timeframe could impact the Group. We continuously monitor internal and external environments to identify new and emerging risks. We then analyse each risk and, if needed, develop and apply mitigation and management plans.

The Group determines which key risks it considers to be heightened, for example those that are more costly if they materialise. We then undertake further work to actively manage these. When considering these risks, we also take account of the objectives of regulators to ensure market integrity, appropriate consumer protection and promotion of competition within the industry. The diagram on the following page shows the relative position of our risks and is an outcome of our assessments.

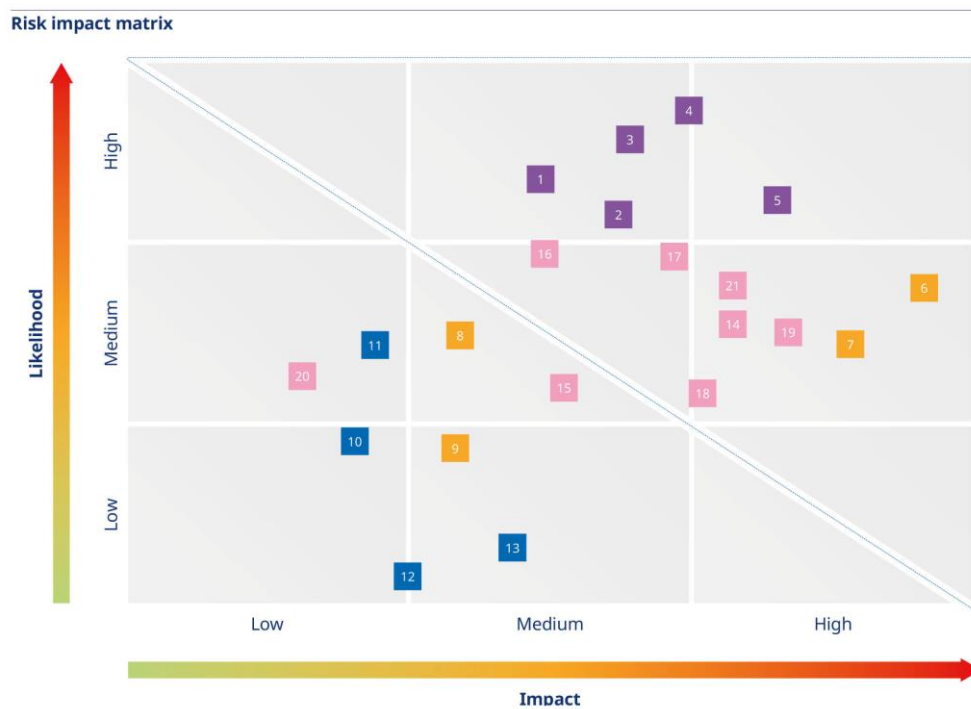
We remain vigilant in considering the impact of Brexit on our business model and have described this further at the end of this section.

Reporting on our material risks

The diagram below illustrates our key risks. The horizontal axis shows the impact of a key risk if it were to materialise and the vertical axis shows the likelihood of this occurring. The scales of each axis are set on a relative basis between each risk and are based on the residual risks.

The risks that we consider to have either a higher likelihood of impacting the organisation, or with a higher likelihood of occurring are shown above the diagonal line.

Details of these risks, and how we manage them, are described on the following pages. A summary of other key risks is set out at the end of this section.



Strategic risks

- 1 Changing investor requirements
- 2 Market returns
- 3 Fee attrition
- 4 Regulatory landscape change
- 5 Business model disruption

Business risks

- 6 Reputational risk
- 7 Investment performance risk
- 8 Product risk
- 9 Business concentration risk

Financial risks*

- 10 Market risk
- 11 Credit risk
- 12 Liquidity risk
- 13 Risk of insufficient capital

Operational risks

- 14 Conduct and regulatory risk
- 15 Legal risk
- 16 Tax risk
- 17 Process and change risk
- 18 Fraud risk
- 19 Technology and information security risk
- 20 People and employment practices risk
- 21 Third party service provider risk

* Financial risks are considered in note 19 of the financial statements.

Key risks

The table below details our heightened key risks.

Key risk	Description	How we manage risk
1. Changing investor requirements	<p>Growth in demand for investment solutions that are not currently offered by the Group. This may include index tracking strategies or certain products where Schroders does not currently offer the investment capability.</p> <p>Regulated clients derisking due to the impact of regulatory capital changes, where clients reallocate investments to capabilities that are not currently offered by the Group or at a lower margin.</p> <p>Movement from defined benefit (DB) to defined contribution (DC) pension plans in a number of countries such as the UK, Japan, South Korea and Taiwan.</p> <p>Consolidation of local authority pensions in the UK, reducing the associated fee pool.</p>	<p>Our Product and Solutions function is distinct from Investment and Distribution, in order to focus on development of new product strategies, innovation, client engagement and managing our diverse product range.</p> <p>We continue to focus on developing our investment capabilities, expanding into new investment types and specific areas of expertise, and commit seed capital to support product innovation for future growth.</p> <p>We deliver our value proposition using an approach based on our strategic capabilities, focusing attention where we believe we are able to make a significant difference for our clients or where we have current or future capabilities.</p> <p>We adapt our business structure and cost base to manage the changing asset allocation requirements of our clients and the impact on our business.</p>
2. Market returns	<p>Our income is derived from the assets we manage. A considerable and sustained decline in markets is outside our control but may contribute to a significant fall in revenues.</p>	<p>We have diversified income streams across a range of markets to mitigate a considerable fall in any one area.</p> <p>We strive to outperform our competitors with a view to attracting assets which may offset a decline or fall in any given market whilst pursuing best returns for our clients.</p>

Key risk	Description	How we manage risk
3. Fee attrition	<p>A lower fee environment and the impact on our business model of margin attrition due to:</p> <ul style="list-style-type: none"> - Changes in investor demand, driven by derisking, or a focus on lower fee margin products; - Compressed investment returns leading to greater fee sensitivity; - Moves towards vertical integration (advice, platform and investment management services, which may lead to investor and IFA risk for participants) within the industry, increasing competition and pressure on fee revenue as active managers may be disintermediated; - Rising costs within the industry, driven by changing and increasing regulatory requirements and technological advancement which impact margins; - Industry pricing pressures from competitors, forcing fee cuts in order to remain competitive; and - Consolidation of preferred distributors or partners, increasing buying power. 	<p>Our business is increasing its focus on solutions and other outcome-orientated strategies which diversifies our fee income.</p> <p>We are also increasingly diversifying our product offering, representing our strategic capabilities, to address evolving investor needs, which supports overall profitability in the long term.</p> <p>We have increased our access to private and other alternative investment assets and strategies through acquisitions and strategic relationships (e.g. infrastructure debt, securitised credit and private equity).</p> <p>We made a strategic investment into Benchmark Capital which provides the opportunity to engage in business in different parts of the value chain in the UK.</p>
4. Regulatory landscape change	<p>Regulators have moved their focus from the prudential and misconduct issues affecting investment and retail banks, to other parts of the financial system, particularly asset managers.</p> <p>There is an increased regulatory focus on transparency of objectives, pricing, fees and other indirect costs borne by end investors and clients.</p> <p>The associated operating costs of compliance reduce net profits (e.g. MiFID II, PRIIPs, the potential introduction of minimum levels of fund liquidity and the outcomes of other regulatory reviews, such as the UK FCA's Asset Management Market Study, the CMA's market investigation into investment consultancy and fiduciary management services and the FCA's market study of investment platforms).</p> <p>The implications of Brexit, especially with respect to any changes to the ability to delegate activities outside the EU, remain uncertain, although a transitional period is now more likely.</p> <p>Changes to intermediary commission and incentive structures and obligations are affecting intermediaries' product selection processes. Regulation of distribution through digital channels and robo-advice may also change.</p>	<p>Regulatory and legal change is monitored by the Compliance, Legal and Public Policy teams and our Regulatory Change Committee. We engage with our regulators in relation to potential and planned changes in regulation.</p> <p>We are actively considering all implications that may arise from Brexit and are planning accordingly. We engage in debates when the opportunity arises. More information as to how we will be positioned with respect of our EU activities after Brexit is provided at the end of this section.</p> <p>Our increasingly diverse product offering enables us to meet the changing needs of clients driven by evolving regulation.</p>

Key risk	Description	How we manage risk
<p>5. Business model disruption</p>	<p>The rise of technology solutions from competitors that disrupt our value chain including competition from quantitative investment technologies that have the potential to assimilate more data and make investment decisions, and that may be perceived to realise alpha more efficiently than active managers.</p> <p>Competitors are consolidating through merger and acquisition activities. They are increasing scale, broadening investment capabilities and expanding distribution channels resulting in stronger relative market positions.</p> <p>Increased investment and asset allocation through robo-advice services, providing automated investment capabilities and potentially displacing active management.</p> <p>Inability to meet demand for products and solution-based offerings due to our capabilities being inadequate relative to requirements.</p> <p>Concentration of risks associated with consolidation of key counterparties that support our business operations where alternative providers are not easily identifiable or where there are significant transition challenges.</p>	<p>We are driving increased efficiencies and insights through technology, including investment in data science to obtain investment insights from non-traditional data sources and upgrading our front office systems.</p> <p>Digital initiatives are in progress to improve client experience, engagement and servicing through our web and mobile platforms, e.g. single web platforms and client behaviour analytics.</p> <p>We are undertaking significant investment in our technology platform to support scalability, agility in product offerings, and our expanding private assets and alternatives business offerings.</p> <p>We monitor the performance of our key counterparties on a regular basis, as well as establishing processes for regularly assessing alternatives.</p>
<p>6.Reputational risk</p>	<p>The reputation of Schroders is of paramount importance and can be impacted by any of our key risks and by our relationships with clients, regulators and shareholders.</p> <p>This may arise from poor conduct or judgements or risk events due to weaknesses in systems or controls.</p> <p>Ineffective branding and marketing may impact our ability to grow our business.</p> <p>Reputational risk may also arise from inappropriate client relationships or mandates which have adverse implications for the Group.</p>	<p>High standards of conduct and a principled approach to regulatory compliance are integral to our culture and values. We consider key reputational risks when initiating changes in strategy or our operating model.</p> <p>We have a number of controls and frameworks to address other risks that could affect our reputation including: financial crime, investment risk, client take-on and product development.</p> <p>We have rebranded to ensure our marketing remains relevant and effective and supports our strategic objectives and product offerings.</p>

Key risk	Description	How we manage risk
7. Investment performance risk	<p>The management of investment performance risk is a core skill of the Group. This is the risk that portfolios will not meet their investment objectives or that there is a failure to deliver consistent and above-average performance.</p> <p>The risk that clients move their assets elsewhere if we are unable to outperform competitors or our investment objectives.</p>	<p>We have clearly defined investment processes designed to meet investment targets within stated risk parameters. The Group's Investment Risk Framework provides review and challenge of investment risks, independent of our fund managers, across all asset classes. Investment monitoring is performed by fund managers and asset class heads on a regular basis, as well as by asset class risk committees, the GMC and legal entity boards.</p> <p>Recognising that products may not outperform all of the time, we offer clients a diversified product set. Key to investment performance is our ability to attract and retain talented people.</p>
14. Conduct and regulatory risk	<p>The risks of client detriment arising from inappropriate conduct, conflicts, management practice or behaviour, or failing to meet client needs, interests or expected outcomes.</p> <p>The risk of money laundering, bribery or market abuse shortcomings on the part of fund investors, clients, suppliers or our employees.</p> <p>The risk of fines, penalties, censure or other sanctions arising from failure to identify or meet regulatory requirements.</p> <p>The risk that new regulations, or changes to existing interpretations of them, have a material effect on the Group's operations, risk profile or cost base and are complex to implement and difficult to manage.</p>	<p>We promote a strong compliance culture and we promote good relationships with our regulators. Our Compliance function supports management in identifying our regulatory obligations and enabling these to be met through relevant training and procedures. Compliance with relevant regulatory requirements is monitored in accordance with a risk-based programme.</p> <p>Our approach to encouraging appropriate conduct and minimising the risk of client detriment is set out in our conduct risk framework, and is built on our culture and values, supported by appropriate governance and reporting.</p> <p>Risk-based client take-on and review processes are among our key controls to address the risks of money laundering. Financial crime oversight is provided by the Financial Crime Committee.</p> <p>Regulatory and legal change is monitored by the Compliance, Legal and Public Policy teams and our Regulatory Change Committee. We engage with our regulators where appropriate in relation to potential and planned changes.</p>

Key risk	Description	How we manage risk
16. Tax risk	<p>The Group and its managed funds are exposed to:</p> <ul style="list-style-type: none"> - compliance and reporting risks, which include the submission of late or inaccurate tax returns; - transactional risks, which include actions being taken without appropriate consideration of the potential tax consequences; and - reputational risks, which cover the wider impact that our conduct in relation to our tax affairs can have on our relationships with our stakeholders. 	<p>Our approach to managing tax risk is set out in our tax strategy. This is reviewed by the Audit and Risk Committee annually. It is supported by a tax governance framework, which aligns to the Group's wider risk and control framework. Key risks and issues are escalated to the GRC and the Audit and Risk Committee.</p> <p>The Tax function works with management and advisers to monitor the tax position of the Group. Local management, with oversight from our Tax function, is generally responsible for identifying and managing the tax position of our managed funds, with the assistance of third party service providers. Developments in taxation are monitored by the Tax function and local management. We engage with industry organisations and advisers to keep abreast of relevant tax changes.</p>
17. Process and change risk	<p>The risk of failure of significant business processes, such as mandate compliance, client suitability checks and asset pricing.</p> <p>Poor execution of acquisitions or management of strategic relationships which fail to deliver intended benefits in terms of revenue or costs.</p>	<p>Our key business processes have been identified and the risks assessed by first line of defence owners through the RCA process.</p> <p>This process is used to determine the adequacy and effectiveness of key controls; with second line providing oversight and challenge. Associated controls are assessed with regard to their design and performance. Output from the RCA process is presented to the GRC.</p> <p>As part of our due diligence process when we consider an acquisition or strategic partnership, we identify areas to be remediated after a transaction is completed. Subject matter experts will be involved throughout the transition.</p>
18. Fraud risk	<p>Fraud could arise from either internal or external parties who attempt to defraud the firm or our clients by circumventing either our processes and controls or the controls operated by our third party providers (e.g. within our outsourced transfer agency activities).</p>	<p>Policies and procedures are in place to manage fraud risk. Controls in place to manage fraud risk are assessed as part of the RCA process. Attempted or any successful frauds are investigated by the Financial Crime team, with oversight from Group Risk.</p> <p>The Financial Crime Committee provides oversight of the management of Fraud risk and is a sub-committee of the Group Risk Committee.</p>

Key risk	Description	How we manage risk
19. Technology risk and information security	<p>Technology and information security risk relates to the risk that:</p> <ul style="list-style-type: none"> - our technology systems and support are inadequate or fail to adapt to changing requirements; - our systems are penetrated by third parties; or - our data is held insecurely. 	<p>Formal governance over information risks has been established across the three lines of defence through the Information Security Risk Oversight Committee. The Group holds insurance to cover cyber risks.</p> <p>Policies and technical standards, including security awareness training, have been deployed across the Group.</p> <p>Robust project management, assessment of business requirements and management of implementation risks are utilised.</p>
21. Third party service provider risk	<p>Third party service provider risk relates to the risk that suppliers may not meet their agreed service level terms.</p> <p>We have a number of outsourced supplier relationships as part of our business model, particularly in respect of information technology, fund administration, custody and transfer agency services.</p>	<p>The Audit and Risk Committee reviews all material outsourced relationships, focusing on significant aspects such as service quality and risk management.</p> <p>Policies are in place that govern our approach to appointing, managing and performing relevant due diligence of third party service providers including regular reviews of performance against agreed service levels. Minimum requirements are established for overseeing service provider risk and performance, and we perform risk assessments on service providers deemed critical to business operations.</p>

Lower rated key risks

The key risks that appear below the diagonal line in the risk impact matrix are summarised in the following table.

Key risk	Description
8. Product risk	The risk that our product or service range is not suitably diversified or viable or does not provide access to strategies sought by investors or meet their objectives.
9. Business concentration risk	The risk of insufficiently diversified distribution channels, products, clients, markets, or income streams resulting in a decline in fee revenue if investor demands change.
10. Market risk	Market movements may cause a fall in the value of principal investments and a decline in the value of our proprietary assets.
11. Credit risk	Counterparty capital exposure arising from client transactions and lending activities, principal cash and investment holdings.
12. Liquidity risk	Counterparty liquidity exposure arising from client transactions and lending activities, principal cash and investment holdings.
13. Risk of insufficient capital	The risk that the Group is unable to support its strategic business objectives due to its minimum regulatory capital restrictions.
15. Legal risk	Legal risk may arise from Schroders, clients or suppliers and other third parties failing to meet their legal obligations; Schroders taking on unintended obligations; or legal claims.
20. People and employment	People and employment practices risk may arise from an inability to attract or retain key employees to support business activities or strategic initiatives: non-compliance with legislation; or failure to manage employee performance.

Our business model and Brexit

On 29 March 2017, the British government invoked Article 50, beginning the two year countdown to the United Kingdom withdrawing from the European Union. Negotiations continue but uncertainty remains and there is a range of possible outcomes and timeframes for many aspects of the UK's exit.

Schroders is well positioned to manage the challenges that may arise as a result of Brexit. Whilst all the legal and regulatory changes of Brexit are not yet clear, our diversified business model means that we are well placed in deciding how best to respond and to continue to service our clients and grow our business. Over 80% of our net operating revenue comes from clients who are based outside the EU27.

We have a long standing commitment to continental Europe, with a substantial presence involving more than 700 employees across nine offices. In Luxembourg, our European operations centre, we have around 250 employees in Product, Risk, Compliance and other Infrastructure functions, and from there we distribute funds not just across borders within the EU, but also more widely across the world, delegating portfolio management to a number of jurisdictions.

Globally, our two largest fund ranges are in the UK and Luxembourg. The UK range is not actively marketed outside the UK. The Luxembourg range is predominantly comprised of EU27 and other non-UK investors. The UK government has said that they will, if necessary, introduce a regime to allow EU27-based funds to continue to be offered to clients based in the UK in the period immediately after Brexit.

We have obtained additional permissions in order to ensure that we can continue to offer our full range of services to European Institutional clients.