

# MATRIX

**Matrix Group Limited**

**Pillar 3 disclosures**

**As at February 2011**

## 1. BACKGROUND

Matrix Group Limited and its subsidiary undertakings (the “Group”) operate under the Basel II capital adequacy framework. This consists of three “pillars”:

- Pillar 1 is a formal set of rules for calculating the minimum capital required by the Group to cover potential losses arising from credit, market and operational risks.
- Pillar 2 focuses on the Group’s internal capital adequacy assessment and this covers other risks (such as business risk) as well as the three risk types covered by Pillar 1.
- Pillar 3 aims to encourage market discipline through the public disclosure of the Group’s risk and capital profile. The information disclosed includes qualitative information (about the Group’s risk governance and risk and capital management processes) and quantitative information (about its risk exposures and capital). The quantitative disclosures provide data on the calculation of risk and capital resources and requirements as set out in Pillar 1.

The UK Financial Services Authority (“FSA”) supervises the Group on a consolidated basis and has set out its Pillar 3 regulations within its “Prudential Sourcebook for Banks, Building Societies and Investment Firms” (“BIPRU” Chapter 11). These disclosures are made in conformity with those requirements.

## 2. SCOPE

The Group’s business is conducted through three divisions: Asset Management, Investment Banking, and Property. The Asset Management division’s activities include alternative funds, cash funds, investment management, private equity, VCTs and specialised finance. The Investment Banking division’s services include advice, capital raising, securities sales trading and research. The Property division raises equity and debt finance for commercial property and syndicates and manages commercial property investments. Senior management considers that this diversified business model is sound and capable of withstanding economic stresses and downturns.

The Pillar 3 disclosures herein are made at Group level and take into account the following subsidiaries of the Group, each of which is authorised and regulated by the FSA:

	Firm	Division/Principal Activity
1.	Matrix Corporate Capital LLP	Investment Banking Division: Advice, capital raising, securities sales trading and research.
2.	Matrix Alternative Asset Management LLP	Asset Management Division: Provision of investment management services for single manager hedge funds.
3.	Matrix Money Management Limited	Asset Management Division: Promotion of off-shore funds and the provision of investment management services for funds of funds, hedge funds, UCITS funds and structured products for private clients and institutions, distributed through intermediaries.

4.	Matrix Private Equity Partners LLP	Asset Management Division: Manages funds, primarily through a range of venture capital trusts (VCTs) raised from private investors.
5.	Matrix-Securities Limited	Service company and marketing of financial products.
6.	Prime Rate Capital Management LLP	Asset Management Division: Specialist provider of AAA-rated liquidity funds, enhanced cash funds and bond funds to institutional and other investors.
7.	Vine Street Capital LLP	Asset Management Division: Investor of private capital into UK businesses.
8.	Matrix Property Fund Management LLP	Property Division: Raises equity and debt finance to acquire commercial property as well as syndicating and managing commercial property investments.

The quantitative disclosures are being made in conjunction with the publication of the Matrix Group Limited Annual Report for the year ended 30 June 2010. Disclosures under Pillar 3 are made at least annually.

Due consideration has been given to the materiality of all required disclosures and to the question as to whether to withhold any of the required disclosures on the basis that they contain proprietary or confidential information.

It should be noted that these disclosures do not constitute financial statements of the Group and should not be relied on in making investment decisions in relation to the Group. The Group has not and is not required to have the Pillar 3 disclosures audited by external auditors.

### 3. RISK MANAGEMENT OVERVIEW

The main categories of risk which require consideration are the following:

- Market & Credit risk;
- Capital & Liquidity risk;
- Operational risk;
- Regulatory & Legal risk; and
- Reputational risk.

The Group places considerable weight on the management of exposures to risk. Its risk management policies are designed to identify, monitor, mitigate and control such exposures to ensure that the activities of the Group's operating divisions are managed within the risk tolerances of the Group Board.

Risk exposures are identified, monitored and controlled by the heads of each division. This is performed in conjunction with senior management from Finance, Risk, Legal and Compliance & Assurance, along with the relevant committees that form part of the governance structure. Responsibility for the approval of all risk management policies and for setting the overall risk appetite and tolerance levels rests with the Group Board. The Group Board has appointed a Group Risk Committee to review and ensure the Matrix Group entities operate appropriate risk identification and mitigation procedures. The core responsibilities are to:

1. Assess and report on the effectiveness of the Company's internal control systems in managing risks; and
2. Provide an appropriate level of reporting of the status of risk within the Matrix Group; and
3. Act on issues as and when they arise.

The committee meets on a regular basis and receives reports concerning the overall risk exposure of the Group covering areas such as exposures to market risk, credit risk, liquidity risk and operational risk. The Group has also established divisional risk and executive committees which are in turn responsible for the oversight of risk management within their areas.

The Group has a programme of insurances designed to reduce its exposure to liability and to protect its assets. These are provided by third party insurers and financially mitigate the economic consequences of risks. Any significant changes in the risk profile of the Group are taken into account by tailoring the insurance programmes to the Group's risk exposures. This approach is designed to maximise breadth of cover and certainty of response in respect of key third party liabilities, loss of assets, business interruption and people-related exposures.

#### **4. THE RISK MANAGEMENT FRAMEWORK**

Matrix Group's Board of Directors takes ultimate responsibility for managing the risks undertaken in all the businesses and for the risk management framework and policies. For each business, we:

- Identify the risks to which the capital of the business is exposed;
- Establish and operate policies which are appropriate to the size, nature and complexity of the business activities;
- Monitor and assess the risks, processes and controls designed to mitigate the exposure;
- Enhance the processes and controls based on the results from monitoring and assessment, including relevant changes in activities and the business environment.

The Risk Management Framework governance structure includes the following committees that meet on a regular basis:

- Group Board
- Group Executive Committee
- Divisional/Entity Executive and Management Committees
- Group Risk Committee
- Divisional Risk Committees
- Divisional, entity and functional business review meetings

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## 5. MARKET RISK

This is the risk of loss as a result of adverse market movements affecting the value of investments held by a firm.

The Group engages in a diversified range of activities within the financial services industry, with the majority of transactions undertaken within the UK. The Group also has a seeding arrangement in the Matrix Asia Fund, which for accounting purposes was classified as a subsidiary in the June 2010 accounts and which invests in Asian equities. As such the Group has an exposure to global economic conditions generally and to economic conditions in the UK and Asia in particular.

The Group has reduced its investment in the Fund since the year end, which has reduced the Group's overall market risk and foreign exchange requirement.

The impact of poor economic conditions on the markets the Group operates in have the potential to adversely impact the Group's financial performance and prospects, as well as increasing other risks. The Group's exposure to market risk is mainly in its trading book and the long term investments it holds, for example the Asia Hedge Fund. The Group distinguishes between day-to-day business conducted in the market and own balance sheet investments.

Where relevant, currency is generally bought or sold at the time of trading in order to meet the funds due or receivable on settlement.

## 6. CREDIT RISK

This is the risk of loss as a result of the non-payment of a debtor. The Group has adopted the 'Standardised Approach' in respect of credit risk.

The main credit risk in the Group is the non-payment of fees and cash holdings at banks. The Group seeks to deal only with creditworthy counterparties.

Within the Investment Banking division the credit risk associated with securities transactions is limited by the fact that counterparty receivable balances are settled on a delivery versus payment basis.

Outstanding corporate finance fees are monitored closely. Strict payment terms are written into engagement letters. Transactional fees are normally required to be paid prior to deal completion/deal announcement or, in the case of fund raisings, are netted off the funds raised thereby mitigating credit risk. In the case of retained clients, fees are billed quarterly.

The Group's cash and cash equivalents are held with a range of banks, most of which are major UK clearing banks currently supported by a government guarantee.

## 7. LIQUIDITY RISK

This is the risk that a business will be unable to meet its financial obligations as they fall due. Each operating company in the Group has its own cash resources which are available to Group when required. Some also have banking facilities structured to meet their obligations at all times.

Ultimate responsibility for liquidity management rests with the Group Board. The Group manages liquidity risk by maintaining cash reserves, banking facilities and borrowing facilities to meet its forecast and actual cash flows and matching maturity profiles of financial assets and liabilities.

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## 8. OPERATIONAL RISK

This is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk. The Group has adopted the Basic Indicator Approach in respect of operational risk.

The Group seeks to avoid, mitigate, manage or transfer operational risk in order to attain acceptable residual levels. This objective is implemented largely through the maintenance of appropriate systems, processes and controls. The Group employs experienced staff, maintains clear segregation of duties and clear lines of escalation. Relevant operational procedures are documented and staff are provided with appropriate training. Outsourced relationships are monitored to ensure adherence to contractual obligations. Business continuity plans are in place and are subject to regular review and testing. Operational risk is further mitigated by professional indemnity insurance.

## 9. REPUTATION RISK

This is the risk of an event occurring which could adversely affect a Group or an individual entity's reputation. The effect could be for instance a loss of confidence by clients, which could in turn affect the ability to generate income.

The Group considers a loss of reputation to be a significant risk to a business operating in the financial services sector. The Group believes that the risk to its reputation would arise as a result of a failure to manage the Group's other risks and therefore always endeavours to always act with integrity and places the highest importance on risk management at all levels of the organisation. It strives to demonstrate this commitment to maintaining the highest level of integrity through its culture, the dedication of senior management time and resources to ensure all employees are aware of the need to display the highest ethical standards in their day to day work and interaction with its clients, regulators and other stakeholders.

## 10. RISK APPETITE

The establishment of Group's risk appetite and tolerance is the responsibility of the Group Board. In addition to the implementation of the policy set by the Group Board, significant new business developments and changes are subject to Board approval. The Group Board, through its appointment of the Group Risk Committee and Divisional Risk and Executive Committees is provided with the relevant management information to enable it to conduct its oversight and governance responsibilities appropriately. Through the composition of the Group's Board it has a comprehensive understanding of the risks throughout the business.

Matrix is a privately owned company in which a majority of the shareholders are employees of the Group. In addition, Group Board members hold a majority of the shares, and all Group Board members, along with other key management, are either shareholders or have share options. Consequently, the interests of the shareholders are aligned with the interests of the management and employees of the Group.

Matrix Group uses its short lines of communication to agree new policies, procedures or business developments quickly and if necessary at short notice. Any new developments will always be made in the context of the current and future risks, cash and profits projection.

Reviews of financial cover required for potential risk are undertaken periodically.

## 11. CAPITAL ADEQUACY

Capital Resources are defined under a number of different tests including regulatory, accounting and internal economic capital criteria. Each of the different tests permits or requires certain additions or deductions, and these are summarised below:

- Goodwill is deducted 100% from regulatory capital;
- The employee benefit trust is derecognised and is therefore deducted 100% from capital;
- Losses in respect of entities outside the scope of consolidated supervision are excluded from reserves.

As at 30 June 2010 the Group had £18.049 million of regulatory capital in place after deductions compared with a requirement of £9.571 million. This resulted in a £8.478 million surplus. Details are set out below.

	<b>£'000</b>
<b>Capital Resources</b>	
Tier 1 capital	19,749
Deductions from tier 1 capital	<u>(1,700)</u>
Tier 1 capital after deductions	18,049
Tier 2 capital	-
Tier 3 capital	-
<b>Total capital after deductions</b>	<u>18,049</u>
<b>Capital requirement</b>	
Credit risk requirement	4,647
Operational risk requirement	4,415
Market / position risk requirement	509
<b>Total capital requirement</b>	<u>9,571</u>
<b>Surplus capital resources</b>	<u><b>8,478</b></u>

Note: The capital resources figures are updated on an annual basis, in conjunction with the issue of the Group statutory accounts.