

# **NCB Group Limited**

## ***Pillar 3 Disclosures 2009***

## **Contents**

1. Introduction
2. Corporate Background
3. Risk Management Policies
4. Market Risk
5. Credit Risk
6. Operational Risk
7. Other Risks
8. Capital Adequacy & Capital Resources

# 1. Introduction

## Background

The Capital Requirements Directive (“CRD”) created a revised regulatory capital framework across Europe, based on the provisions of the Basel II Capital Accord. The Basel II Capital Accord is built around three central elements or pillars:

- *Pillar 1 – Minimum Capital Requirements:*

Pillar 1 lays down the minimum capital requirements firms are required to hold for the purposes of meeting market, credit and operational requirements.

- *Pillar 2 – Supervisory Review Process:*

Under Pillar 2 firms and regulators evaluate whether firms are holding sufficient capital to cover specific risks that are not fully captured under Pillar 1. The main principal of Pillar 2 is that firms should have a process in place for assessing their overall capital adequacy in relation to their risk profile and a strategy for maintaining their capital levels. This assessment is known as the Internal Capital Adequacy Assessment Process document.

- *Pillar 3 – Market Discipline:*

The aim of Pillar 3 is to improve market discipline by requiring firms to publish certain details of their risks, capital and risk management and thereby allowing market participants to assess the firm’s capital adequacy.

## Frequency

Disclosure will be made annually.

## Location

The disclosures are made on a fully consolidated basis for NCB Group and will be available on NCB’s website.

## Verification

This document and the disclosures made herein are not subject to external audit, and may not be based upon audited financial data, but have been reviewed by senior management.

## **2. Corporate Background**

NCB is one of Ireland's largest independent securities firms and has been a leading provider of institutional equity, wealth management and corporate finance services to our clients for over 25 years. In addition to these activities, NCB also operates in the investment funds/debt securities and venture capital areas.

### **Institutional Equities**

NCB Institutional Equities provides research and trading services to Irish and international institutional clients in Irish, UK and European stocks. The services we provide to our institutional clients include: company and sector research, economic and strategic analysis, access to company management, equity conferences and efficient trade execution and settlement.

### **Wealth Management**

NCB Wealth Management provides clients with the following services: stockbroking, investment management, retirement planning, property, private equity and alternative investment management.

### **Corporate Finance**

NCB's Corporate Finance division provides a comprehensive range of corporate advisory services to quoted companies, private firms, State-owned organizations and the Irish Government.

### **Venture Capital**

NCB's private equity arm manages investment funds which are directed at small to medium sized enterprises with significant growth potential. The funds take a significant equity position in investee companies and actively manage their investments through Board participation. NCB lists the European Investment Fund, Enterprise Ireland, Guinness Ireland and Ulster Bank among the shareholders in its funds.

### **Investment Funds & Debt Securities**

NCB's Investment Funds and Debt Securities division lists domestic and offshore funds on the Irish Stock Exchange. We provide a service to applicants seeking a listing from initial advice to the continuing requirements post-listing.

### **3. Risk Management Policies**

The Board accepts ultimate responsibility for the establishment and oversight of NCB's risk management framework. The Board determines the risk appetite and is responsible for the implementation of a risk management structure to evaluate and manage the risks faced by the firm. As part of this structure, the Board approved the formation of a Risk Management Committee to oversee and evaluate the management of risk within the firm and to report to it thereon.

It is accepted that risk exists in NCB's business and, where appropriate, NCB has policies in place to manage and mitigate risk.

To manage risk in NCB means:

- Understanding, measuring and managing the risks the firm faces
- Promoting an awareness of risk throughout the business
- Having strong independent risk and compliance functions
- Appreciating that stockbroking is about managing risk, not avoiding it

#### **Risk appetite in NCB**

The Board has determined that a low overall risk appetite is appropriate for the firm. It recognises that risk appetite may differ depending on each specific risk and prevailing market conditions, and that there is exposure to adverse movements in the stock market.

#### **Risk Management Committee**

The Risk Management Committee (RMC) maintains and reviews a Risk and Controls Assessment on a bi-annual basis. The purpose of this is to ensure that all the risks which the business faces are identified and their likely impact and means to mitigate/control them are assessed.

Specific policies have been put in place for particular risk areas: market risk, credit risk and operational risk.

The RMC meets on a quarterly basis. The RMC has the following responsibilities:-

- Review and challenge the ICAAP (on an annual basis)
- Review the firm's risk and control assessment (on a bi-annual basis)
- Review the operation of the firm's Market Risk Policy (quarterly)
- Review the operation of the firm's Credit Risk Policies (quarterly)
- Review the operation of the firm's Operational Risk Policy (quarterly)
- Consider any New Product Proposals (as required)

The RMC reports to the Board regarding all risk matters that occur during a reporting period.

#### **Risk and Control Assessment**

The purpose of this assessment process is to ensure that the directors and all senior staff in the organisation are fully aware of the risks which the firm faces, and understand the various tools and mechanisms in place to mitigate such risk.

## **4. Market Risk**

Market risk is the risk that arises from fluctuations in the value of assets held due to movements in share prices, interest rates or exchange rates.

The nature of the firm's Institutional Equity division encompasses both agency and principal transactions and where proprietary positions arise the firm is exposed to market risk.

Market risk is managed through the operation of the firm's Market Risk Policy.

In summary, the firm is exposed to market risk where the firm has a position in a financial instrument. The firm uses Value at Risk (VaR) to calculate the exposure, and uses VaR and other limits to control its exposure to market risk. The VaR is used to estimate the likely maximum monetary loss for the firm's position, based on certain assumptions. To complement the use of VaR, stress testing and back testing is also undertaken.

The key limits used intra-day to monitor the firm's exposure to market risk are the gross long, short and net limits, and individual stock limits. Stocks are categorised into one of four groups depending on liquidity and market capitalisation.

Market risk is managed through the following mechanisms:

- Existing limits in place
- Approval of new limits / changes to limits
- Intra-day monitoring of limits by the RMC
- Reporting of limit utilisation
- Approval, escalation and reporting procedures for excesses

## **5. Counterparty Credit Risk**

Counterparty credit risk is the risk that a counterparty to NCB will not fulfill their obligations (to deliver or pay for securities as required) and the collateral available is insufficient to meet any shortfall.

The nature of the firm's businesses, in which it acts as a counterparty to market and client transactions, and places its own assets with market counterparties/entities and financial institutions, means that there is continual exposure to counterparty credit risk.

Risk is managed through the firm's Counterparty Credit Risk policies.

The firm's Counterparty Credit Risk Policy (Institutional Equities) – sets out how risk is managed in relation to institutional clients and market counterparties. Institutional transactions are normally settled on a delivery versus payment basis and the exposure to NCB is the price movement between deal date and settlement date.

The following procedures are in place:

- Allocation and approval of limits (following a due diligence process)
- Monitoring of limits
- Reporting and escalation procedures for excesses / exposures
- Regular review of counterparties

The firm's Counterparty Credit Risk Policy (Wealth Management) – sets out how risk is managed in relation to Wealth Management clients.

In summary client credit risk is managed through the following mechanisms:

- Formal account opening procedures
- Credit limits
- Standard requirement for clients to have cash on account prior to trading
- Monitoring of debtors on a daily basis

Other counterparties with whom the firm places its cash and assets are subject to approval by the Risk Management Committee.

## 6. Operational Risk

Operational risk is “the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events”.

The firm’s businesses rely heavily on its staff and systems, and are supported by defined process flows and procedures, all of which expose the firm to operational risk.

The firm’s policy is to minimise operational risk as much as possible. This is done through the application of the firm’s Operational Risk Policy.

The key components of operational risk management are:

- Identification
- Measurement
- Mitigation
- Monitoring
- Reporting

Operational risks are:-

- Identified and measured through a bi-annual risk assessment process
- Mitigated primarily through the operation of internal controls and procedures
- Monitored using periodic risk assessments, loss event registers and action plans, and the review of key controls
- Reported on to the Group Risk Management Committee and the Board.

Examples of the main operational risks that the firm has identified include:

- Staffing & key persons
- Fraud
- Administrative and trading errors
- Systems/IT
- Regulatory & compliance
- Business continuity
- Reliance on suppliers

## 7. Other Risks

### **Business risk**

Business risk is the risk that the firm's position, performance or prospects are negatively impacted by changes in the macroeconomic environment and/or changes in the competitive environment.

Business risk is managed through the development of business plans, corporate strategy and management oversight. Business plans and strategy generally evolve over time though where necessary may be subject to urgent change as economic circumstances dictate.

### **Concentration risk**

Concentration risk is the risk arising from a lack of diversification within the Group's business.

The firm has three significant revenue streams: Institutional Equities, Wealth Management and Corporate Finance. There is constant focus on broadening the geographic spread of clients and the product offering.

Within Institutional Equities, the customer base is spread across Europe and the US. Historically the firm's focus has been on Irish equities, however, in recent years the firm's strategy has been to broaden its product offering to include the sale of non-Irish equities to its client base and this has been facilitated by its membership of the European Securities Network (ESN). Institutional Equities has an office in London providing an UK equity service to the UK client base, as well as the ESN.

### **Liquidity risk**

Liquidity risk is the risk that the Group is unable to meet its financial obligations as they fall due.

The Group's financial obligations primarily consist of general company operating expenses; working capital including margin, residual proprietary positions and debtors and; client and market settlements.

Liquidity risk is managed through the followings means:-

- efficient settlement processes designed to minimise late and failed settlements
- pre-approval of client/market terms which impact liquidity
- having banking facilities in place

**Insurance risk**

Insurance risk is the risk that the firm may not have adequate insurance against all eventualities and that this may result in a significant financial loss for the firm.

This risk is managed by having suitable and adequate insurance cover in place. All policies are reviewed and renewed annually. Policies currently in place:

- Professional Indemnity
- Direct Financial Loss
- Directors & Officers Liability
- Employers Liability
- Public/Products Liability
- Property Damage/Business Interruption/Computer Failure

**Legal risk**

This is the risk that legal actions may be taken against NCB.

The firm adopts internal controls, procedures and review processes already outlined in the Operational Risk section and this allied with strong management, a good compliance culture and suitable insurance cover mitigates legal risk.

## **8. Capital Adequacy & Capital Resources**

The ICAAP is a key element of the Group's implementation of the EU Capital Requirements Directive ("CRD"). It is a process that brings together the risk management framework that the Group has previously implemented to identify, manage and mitigate its risks, and the firm's budgeting and capital planning process.

The ICAAP will be reviewed and updated each year unless there are any changes in the control environment or other events that warrant a more immediate review. When performing the annual update the Board will review the stated risk appetite and compare it against actual performance and the risks identified in the Risk Register.

Not all material risks can be mitigated by capital but where capital is appropriate the Board has adopted a Pillar 2 approach. The capital requirement for the firm will be the higher of its Pillar I or Pillar 2 calculations.

As at 30<sup>th</sup> November 2008, the consolidated capital requirement of the Group was 2.74 times covered by the capital resources at that date.