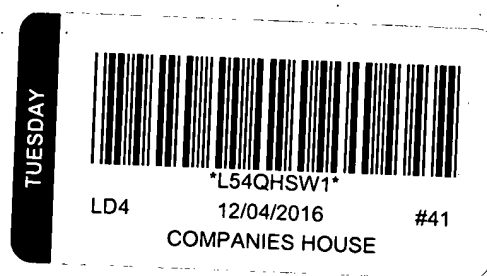


**ANNUAL REPORT AND FINANCIAL STATEMENTS**

**HERMES FUND MANAGERS LIMITED**

**31 DECEMBER 2015**



**Registered No: 1661776**

## HERMES FUND MANAGERS LIMITED

### OUR YEAR IN BRIEF

#### 2015 Financial and Business Highlights

**Hermes' Purpose: To be the world's leading provider of long-term holistic returns for savers, thus creating value for all stakeholders in the financial system**

*We understand that the way we achieve our investment objectives will have an impact that is more than purely financial – it will affect the world in which our beneficiaries live and the real value of their retirement incomes.*

OBJECTIVES	MEASURE	2015	2014	VARIANCE
DELIVERING RETURNS	Percentage of all portfolios (by number) with a 3-year track record to beat their 3 -Year benchmark	100%	80%	↑
	Assets Under Management and Advice*	£23.0bn	£28.6bn	↓ 20%
STEWARDSHIP	Assets Under Stewardship**	£154.7bn	£134.0bn	↑ 15%
	Number of Companies engaged	466	446	↑ 5%
	Number of Company and policy interactions	1,823	1,641	↑ 11%
DELIVERING A SUSTAINABLE AND PROFITABLE FIRM	Underlying Profit (pre-tax)***	£14.6m profit	£1.6m profit	↑ £13m
	Revenue	£105.5m	£90.4m	↑ 17%
	Third party revenue (total revenue)	52%	41%	↑
	Statutory Pre-Tax result	£14.6m profit	£10.5m loss	↑ £25.1m
	Consolidated Net Assets Including Pension Assets / Liabilities	£54.5m	£43.8m	↑ 24%

\* The movement in Assets and Management and Advice is explained in more detail on page 11.

\*\* Assets under Stewardship relate to Hermes Equity Ownership Services Limited.

\*\*\* Underlying 2014 profit before tax excludes the one-off costs in the prior year related to the strategic review discussed in the strategic report.

## HERMES FUND MANAGERS LIMITED

### OVERVIEW

#### Who we are

Hermes Fund Managers Limited ("Hermes" or the "Company") is a global investment management firm focused on delivering superior, sustainable, risk adjusted returns for our clients, responsibly.

#### What we do

We operate under the "Hermes Investment Management" brand and comprise 349 employees who work within or support our specialist investment teams and our leading engagement business, Hermes Equity Ownership Services Limited ("Hermes EOS"). Each investment team focuses exclusively on a particular asset class or style across equities, fixed income and private markets.

Our structure allows each investment team to focus on delivering excellent long-term risk adjusted performance to our clients, supported by a robust operating and risk control infrastructure. The teams develop their own unique investment philosophies and processes. This enables them to generate returns in the most effective ways for their asset class, without the constraints of an imposed house view or style.

Portfolios are continuously monitored by our Investment Office, which exists to ensure the investment teams are managing their portfolios in the best interests of our clients. Operating independently of the investment teams, the Investment Office plays a central role in ensuring we keep our investment promise - to deliver superior, sustainable, risk adjusted returns for our clients, responsibly.

#### Our culture

Since inception in 1983, Hermes has been owned by and acted as the principal investment manager for the BT Pension Scheme (the "Scheme") – one of the UK's largest corporate pension funds.

Our ownership by the Scheme and our duty to serve its more than 300,000 pensioners gives us a strong sense of fiduciary responsibility which is embedded throughout Hermes and which informs the decisions we make and the actions we take. It also gives us an unrivalled insight into the long-term needs of savers and helps us develop investment strategies that will enable them to meet their goals.

#### Our responsibilities

Our commitment to behaving responsibly is not limited to the way we manage money for our clients. We have a strong focus on environmental, social and governance ("ESG") issues in our investment process, throughout equities, fixed income, infrastructure and real estate. Hermes EOS engages with companies globally on such matters for many of the world's largest asset owners. We also participate extensively in industry and sector initiatives to develop best practice for both companies and investors. For example, we support the independent 300 Club, which was established by our Chief Executive Saker Nusseibeh and comprises experienced leaders from across the asset owning, managing and consulting communities. Its purpose is to challenge investment orthodoxy and improve the contribution of financial services to society; we do this because we believe that influencing companies and public policy in this way produces better and greater holistic returns for shareholders, investors and ultimately our beneficiaries.

Beyond this, we believe in acting responsibly as a company in all aspects of our business. We have a strong corporate citizenship programme that is focused on helping the communities in which we live and work. We have ISO14001 accreditation for our environmental management system and we adhere to the London living wage.

## HERMES FUND MANAGERS LIMITED

### CHAIRMAN'S STATEMENT

#### Review of 2015

##### Overview

The year ending 31 December 2015 saw considerable progress made towards delivering a sustainable and profitable business. For the first time in its history, Hermes generates more of its revenues from third parties than it does from its parent, the BT Pension Scheme. To put this into context, when I assumed the role of Chairman in 2011, less than 35% of the Company's revenues were not attributable to the scheme.

Revenues for 2015 increased to £105.5 million (2014: £90.4 million) and the firm achieved a profit before tax of £14.6 million. This compares with a loss of £10.5 million in 2014, which included restructuring costs of £12.1 million following the Company's strategic review in that year. On a like-for-like basis, the underlying profit margin increased to 13% (2014: 2%) demonstrating improving efficiencies in the business and the benefit of a consolidated "One Hermes" brand.

Strong growth continued in third party assets and associated revenues. Third party revenues, including share of profits received from Hermes GPE LLP ("Hermes GPE"), are now in excess of 50% (2014: 40%) of the total revenues earned. Most importantly, our investment teams continued to deliver strong long-term investment performance to our clients, 100% of our fund strategies outperformed their 3 year benchmarks. We also continued to build the awareness and integration of ESG issues across the firm, complementing the development of our stewardship proposition through which we are engaging across a wide range of companies, sectors and thematic issues such as carbon reduction. These are covered in more detail in the new responsibility section of the strategic report.

Towards the end of the year, we closed our active government bond capability. Our largest investor in the strategy decided to allocate their portfolio to passive managers as a cost effective way of meeting their objectives. With the withdrawal of this mandate, which formed the vast majority of the strategy, our government bond capability was no longer commercially viable.

Given the industry-wide trend towards passive management of government bond portfolios, our client's decision was one that we had included in a range of business planning scenarios. Although the loss of assets under management was significant, it has had a minimal impact on profitability due to the low fees charged on those assets. Our business is now fully aligned with our strategic growth plans and well positioned to benefit from long-term changes to the investment landscape.

##### Outlook

At the time of writing, economic and political uncertainty abounds. This looks unlikely to abate in the coming year, with presidential elections in the US, a looming referendum in the UK, the many and various problems in the Middle East and a slowing global economy.

The Board believes that we are well placed to navigate the challenges ahead and to capitalise on the opportunities that will arise. The firm is on a strong footing, with growing profitability and a product set aligned with the future needs of our clients. We have strong performance in the vast majority of our strategies, which are aligned to our clients' long-term needs. We have established a strong reputation in our core markets and have significant growth opportunities globally. Our focus continues to be on increasing profitability by growing with our clients. We will continue to invest prudently in the growth areas of our business whilst controlling costs and continuing to improve efficiency.

**HERMES FUND MANAGERS LIMITED****CHAIRMAN'S STATEMENT (continued)****Culture**

As chairman of Hermes, I view our strong culture of responsibility as fundamental to the continuing creation and delivery of value to our stakeholders. It is encouraging to see the importance of a responsible approach to investment management being more widely accepted by asset owners and asset managers, as well as those who seek to represent them in industry bodies.

The Board and the executive team recognise that the firm needs highly skilled people in order to deliver value for our clients. Equally, we recognise that we need, and indeed want, the right people. The introduction of the Hermes Pledge is a clear signal of the aspiration of what Hermes wants to embody and is reinforced by our incentive schemes which require that bonuses for all employees, without exception, are awarded based on several factors, including an assessment of how they behave and not just on what they deliver.

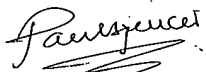
As a firm, we will continue to lead debate and contribute to the transformation of the investment industry to the benefit of our clients, their stakeholders and ultimately, society at large. In this regard, I was very pleased to announce Saker Nusseibeh's appointment to the Banking Standards Board during the course of the year.

**The Board**

After five years, I will be standing down as Chairman in April 2016. During this time, Hermes has evolved into a highly regarded company that, I believe, is setting the standard for a new type of asset management business – one that fully embeds responsible capitalism at the very heart of its business and one that truly takes a long-term holistic view of the needs of its clients and their beneficiaries.

Ian Kennedy, Chief Operating Officer of the Company, joined the Board as an executive director in December 2015. David Stewart, who joined the Board in April 2015 as a non-executive director, will assume the role of Chairman. Under David's experienced leadership, I am sure that the firm will continue its growth and I look forward to watching its development for many years to come.

Finally, I would like to thank everyone at Hermes for their hard work and dedication over the last year. It has been a privilege to work with you over the last five years and I wish you all well for the future.



Paul Spencer CBE  
Chairman

31 March 2016

## HERMES FUND MANAGERS LIMITED

### STRATEGIC REPORT

This strategic report has been prepared for the Hermes group of entities (the "Group") and therefore gives greater emphasis to those matters which are significant to the Group and its subsidiary undertakings viewed as a whole. It is intended to present a fair, balanced and understandable presentation of the Group's position and direction.

**"Since our establishment in 1983, we have believed that we have a duty that extends beyond the purely financial; that we must act as stewards of the investments we manage and advise. We do this because we believe it is right for investors and right for society. We believe better governed companies deliver better returns and create a better society in which investors live"**

#### Aligned with our clients

In 2014, we carried out a strategic review of the firm. Our goal was to ensure that we deliver investment capabilities that align with the long-term requirements of our client base, whilst taking a holistic view of their needs that extends far beyond the returns we generate. In 2015, we built on that review, with considerable success across the business.

Our focus is on areas where:

- There is long-term appeal for long-term investors.
- Our ownership structure enables us to offer clients hard-to-access co-investment opportunities alongside Scheme, one of the largest corporate pension schemes in the UK.
- We have a differentiated approach in the way we manage assets.

Our ambition is to be regarded as the leading provider of holistic returns for savers, thereby creating value for stakeholders throughout the financial system. At the heart of this ambition is an intense focus on providing high value-add, sustainable investment returns, delivered responsibly and at a competitive price.

#### Our four pillars of growth

The focus outlined above creates a framework within which we manage the business. It informs our investment, distribution and stewardship strategies. Within this framework, we have created four distinct pillars of growth.

- Raising assets in our high conviction, high active share, public markets capabilities.
- Providing access to compelling private markets opportunities in real estate, infrastructure, private equity and private debt.
- Developing "outcome" strategies in absolute return credit, multi strategy credit and multi asset.
- Expanding our stewardship and ESG integration propositions across both Hermes EOS and our various investment capabilities.

Embedded in all that we do are our core values of Excellence, Responsibility and Innovation.

## HERMES FUND MANAGERS LIMITED

### STRATEGIC REPORT (continued)

#### Our four pillars of growth (continued)

##### *Excellence*

We aspire to excellence in everything we do. This manifests itself most visibly in our investment performance, where 100% of our funds by number beat their performance benchmarks over the three years under review and 91% of strategies outperformed their benchmarks over one year.

We will only offer products to our clients where we believe there is a strong investment thesis and where we can deliver sustainable alpha through active management. For the three years to the end of December 2015, our asset weighted equity active share was 87.76%. Combining our public and private markets portfolios and using data spanning the three year period ending September to December 2015 (depending on asset class), our three year asset-weighted information ratio was 0.97 on a US Dollar basis.

Lastly, we aim to build a firm populated by excellent, motivated people across all parts of the firm, encouraging a culture of positive challenge that leads to constant improvement across the business, for the benefit of our clients.

##### *Responsibility*

We have a strong culture of responsibility, which we have continued to foster since our inception in 1983. We have always sought positive engagement with the firms in which we invest and, in our stewardship service, Hermes EOS, have the largest such resource in the industry.

We believe it is our responsibility to lead discussion and debate about the fiduciary responsibilities of fund managers to our clients, their stakeholders and ultimately, society at large. During the year we published a series of papers on responsible capitalism, spanning investment, gender diversity, sustainability and stewardship. As active members of the UN Environment Programme (UNEP FI), the UN Principles for Responsible Investment (PRI) and the Institutional Investors Group on Climate Change (IIGCC), we contributed to the publication of 'Fiduciary duty in the 21<sup>st</sup> century' report, establishing clearly that failing to consider ESG risks is a failure of investor's fiduciary duty.

During the year, we also actively participated in the 2015 UN Climate Change Conference in Paris, publishing a report entitled "Turning down the heat", which assessed the carbon risks within our investment portfolios and set out how we intend to monitor and systematically mitigate these risks. We also joined the Portfolio Decarbonisation Coalition to share best practice on how to implement carbon reduction strategies; and we co-authored the "Sustainable Responsible Investment: Implementing the Paris Climate agreement, an action framework" a tool on how to integrate carbon and ESG risks for all type of real estate investors.

Responsible behaviours to our clients, colleagues and other third parties represent a significant part of our performance management process for all employees. In October 2015 we launched the Hermes Pledge. The Pledge, which you will find at the end of this report, is an expression of our commitment to always act responsibly and transparently, keeping our clients' interests at the heart of what we do.

## **HERMES FUND MANAGERS LIMITED**

### **STRATEGIC REPORT (continued)**

#### **Our four pillars of growth (continued)**

##### ***Innovation***

We seek to create an investment management firm that is different from the norm. In doing so, we define innovation more broadly than our industry's traditional focus on new products.

##### ***Culture***

Our culture is one where we strive to ensure that the client is at the centre of our firm and responsibility embedded in all that we do. We seek to create a thoughtful environment where orthodoxies are challenged in the way that we invest, in the way that we engage and in the way that we work. One example of this innovative thinking is our Investment Office. We believe its proactive and pre-emptive engagement with our investment teams, the breadth and depth of its approach and critically its transparency benefit all of our clients.

##### ***Competence***

We actively seek talented individuals with broad expertise to add to the collective knowledge and wisdom of the firm. Recent recruits come from a wide spectrum of organisations including asset management, investment banking, alternative investments, professional services and NGOs.

##### ***Capabilities***

We believe in developing capabilities that are aligned with the long term needs of our clients and that enable them to invest in hard-to-access areas at reasonable cost. Our ownership by the Scheme gives us unrivalled insight into the needs of pension funds and their beneficiaries, which we use to inform our product development strategy.

#### **Business review**

2015 proved to be our most successful year to date across a wide range of measures. Although assets under management declined due to the closure of our government bond strategy, profits before tax grew strongly to £14.6 million, compared with £1.6 million on an underlying basis in 2014.

Third party assets grew strongly across our strategies, with significant flows into both public and private markets. Our third party assets under management increased to £9.3 billion and, as our chairman has reported, third party revenues surpassed 50% of total revenues for the first time in our history. This significant milestone was achieved three years ahead of the plan we laid out in 2014 and it is testimony to the quality of our investment proposition, the strength of our distribution capability and the increasing recognition of our brand.

New business was generated across a wide range of our strategies. Of particular note were strong inflows into our European equity capability and the infrastructure strategy managed by Hermes GPE. In line with our commitment to act in investors' interests, we "soft closed" our Asia ex Japan strategy to further investments during the first half of the year. Geographically, we received the greatest level of inflows from continental Europe, followed by the UK and North America.



## **HERMES FUND MANAGERS LIMITED**

### **STRATEGIC REPORT (continued)**

#### **Business Review (continued)**

Elsewhere, we continue to develop our distribution platform, using a combination of in-house and third-party resources as appropriate. We have registered our UCITS funds in Italy and Spain, where strong growth potential for our proposition exists. We will continue to prudently expand in 2016. Our Asian presence, which we established in Singapore at the beginning of 2014, is generating awareness of Hermes in the region and we are confident in its prospects for 2016.

From a stewardship perspective, we were appointed by more global asset owners to carry out engagement activities on their behalf. We now advise forty of the world's leading asset owners on over £150 billion of assets. We expect growth in this area to continue as demand increases for sophisticated engagement expertise.

At a brand level, we have made strong progress throughout the year. Following the consolidation into one corporate identity in 2014, we launched our new website in October 2015. The site, designed using the latest web technologies, enables us to demonstrate our capabilities and insights holistically, giving investors a clear view of the firm and the values we represent. Media coverage has been extremely strong, with more than 7,000 press articles during the year and a significant presence on TV and radio. This has helped us continue to build the Hermes brand with our target audiences.

#### **Employees – attracting and developing talent**

Hermes' success is built on strong values and the contributions of its employees. We aim to build a firm populated by excellent, motivated people, encouraging a culture of positive challenge across the business, for the benefit of our clients.

Our people make all the difference, so investing in their development is crucial to our continued success. Hermes aims to be a good employer, attracting and developing qualified and motivated people. It is the responsibility of every leader and manager throughout Hermes to create an environment where all of our people can give their best, feel valued and be able to build upon their knowledge and skills.

To develop future talent within the business, our Learning & Development team has created a suite of management programmes which span induction support, skills and technical development, management development and professional studies.

A workplace which embraces diversity is important to ensuring that we are maximising the potential of our workforce. We recognise that diversity offers real, tangible benefits. We employ high-calibre people from many different backgrounds, combining talents and experience to deliver exceptional performance.

At 31 December 2015 our main Board is 25% represented by female executive and non-executive directors. As of 1 April 2016, we expect our main Board to be 38% represented by female executive and non-executive directors. Throughout the rest of the Company 27% of our front line management staff are female; and 28% of our female staff are at Director grade. 37% of our workforce is female.

As well as gender, diversity encompasses nationality, ethnicity, religion, cultural background, education, personality differences, experience and skill-sets.

## HERMES FUND MANAGERS LIMITED

### STRATEGIC REPORT (continued)

#### Financial Review

The 2015 results reflect the positive impact of the significant investment incurred in the prior year.

	2015 £'000	2014 £'000
Turnover	105,477	90,446
Administrative expenses	(95,489)	(94,109)
Non-operating items	4,583	5,278
Underlying Group profit	<b>14,571</b>	<b>1,615</b>
Strategic implementation costs	-	(12,141)
Statutory Group profit	<b>14,571</b>	<b>(10,526)</b>

#### Financial performance

Revenue for the year increased to £105.5m (2014: £90.4m) primarily due to new funds under management of £3.3bn. Management fees increased as a result of asset inflows and performance fee revenue increased marginally to £19.7m (2014: £18.1m) demonstrating the ability of the Group to deliver investment performance against the continuing backdrop of a challenging economic environment as demonstrated in the markets review (page 12). Despite this, performance has been exceptional with 100% of funds outperforming their 3-year benchmark. The proportion of revenue from third parties has increased significantly to 52% compared to 41% in the prior year.

Operating costs have been tightly controlled during 2015 despite the increase in revenue. Operating expenses have increased by 1% to £95.5m (2014: £94.1m) while the underlying profit margin has increased from 2% in 2014 to 13% in 2015. The Group undertook a significant restructuring programme during the prior year with a cost of £12.1m associated with this shown above as strategic implementation costs.

Consolidated net assets as at 31 December 2015 were £54.5m (31 December 2014: £43.8m), representing an increase of 25% on prior year. The increase is mainly due to the statutory profit after tax in the year of £20.1m, less the repurchase of growth shares (£6.1m – see note 19), and the acquisition of shares in Hermes Sourcecap Limited, increasing the Group's shareholding in the entity (£3.2m - see note 12). Cash balances at 31 December 2015 decreased marginally to £53.4m (2014: £55.4m) mainly due to the repurchase of growth shares early in 2015. New client mandates continued to be won in 2015 and both gross and net asset inflows from continuing strategies for the year were ahead of target, with £10.0m of new gross third party annualised revenue funded and in transition.

**HERMES FUND MANAGERS LIMITED****STRATEGIC REPORT (continued)****Financial Review (continued)**Financial position

The decrease in assets under management from £28.6bn to £23.0bn as shown on page 11, is due to the closure of the government bonds strategy in the year. Although the loss of assets under management is significant, it has had a minimal impact on our profitability due to the low fees charged on those assets.

Hermes is the principal sponsor of the Hermes Group Pension Scheme ("HGPS"). HGPS is a defined benefit pension scheme that was closed to new entrants in 2008 and was closed to future accrual in 2011. The FRS 102 valuation of the pension scheme improved during 2015 principally due to the return from pension assets exceeding expectations and is now at a £1.6m surplus compared to a £9.7m deficit in 2014 (see note 16 for further information on the pension scheme).

During the second half of 2014 our owners, the Scheme, injected £20m ordinary share capital into the Company. This reaffirmed the clear commitment from our owners to support Hermes.

**Regulatory capital**

The Company continues to maintain a regulatory capital surplus above the Group capital requirement. Further details of the Group's approach to capital adequacy can be found on the Hermes website: <http://www.hermes-investment.com/en-gb/literature.aspx>

Overall, the Group has both the financial strength and capital resources to support and execute its strategic plans and the Board remains focused on growing and developing our core businesses.

**HERMES FUND MANAGERS LIMITED****STRATEGIC REPORT (continued)****Financial Review (continued)****Assets Under Management and Sub-Advice (in £billions)**

At 1 January 2015		28.6
New funds raised	3.3	
Government bonds withdrawal	(8.5)	
Other redemptions, realisations and withdrawals	(1.9)	
	<u>(10.4)</u>	
Net new funds		(7.1)
Market movement		1.5
<b>At 31 December 2015</b>		<b>23.0</b>
<i>% decrease in assets under management and sub-advice</i>		<b>19%</b>

Please note the total assets under management figure above for Hermes includes assets under sub-advice of £1.0 billion (2014: £1.0 billion) and includes £3.7 billion of assets that are managed by Hermes GPE, which is a joint venture between Hermes and GPE Partner Limited (2014: £2.9 billion).

**Principal Risks and Uncertainties**

The Group faces a number of risks in the normal course of business providing investment management and engagement services to institutional clients. These risks are managed by:

- Adhering to our established business model;
- Implementing an integrated risk management approach based on the concept of "three lines of defence" which is outlined on page 20; and
- Setting clearly defined risk appetites monitored with specific metrics within set limits.

The most significant risk facing the business is a downturn in the economic conditions which could impact the Group's performance through lower demand for its investment management products and lower investor risk appetite as a result of financial markets instability. Both would result in a decline in the value of assets under management. The majority of the Group's activities are in specialist areas where our people have significant experience and expertise. Our commitment to our proven business model and strengthening financial position allows us to support our clients in all economic conditions. This assists us in our aim of developing long term relationships with our clients. The Group carries out regular stress testing on its performance and financial positions to test resilience in the event of adverse economic conditions.

A summary of the principal risks and uncertainties which may impact the Group's ability to deliver its strategy and how we seek to mitigate these risks is set out on page 19. The risks identified remain broadly unchanged from the prior year reflecting the Group's consistent strategy and adherence to its established business model. The summary should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties faced by the Group but rather those risks which the group currently believes may have a significant impact on the Group's performance and future prospects.

**HERMES FUND MANAGERS LIMITED****STRATEGIC REPORT (continued)****Investment Review****Economics and markets review**

Despite concerns about Greece leaving the Euro, the China-inspired plunge in equities and last December's first US interest rate rise since June 2006, global growth in 2015 was not derailed, although it did slow to about 3.0%. This was the lowest rate since 2009, which was a time when China was growing over 9% year-on-year. These factors, however, tempered optimism about whether economic recoveries could continue in 2016.

With China struggling in 2015 to convincingly reach its official "close to 7%" target, financial markets and central banks were right, albeit belatedly, to reassess the world's growth prospects. Meanwhile, with record low interest rates, resilient domestic demand and lower oil prices (Brent crude fell by \$20 per barrel over 2015 to \$36 per barrel), the US and UK managed to pull themselves further away from the economic downturn of 2008-09. In the US real GDP is about 10% higher than pre-crisis and in the UK about 7% higher.

Seven years of unprecedented stimulus have led to a two-speed recovery. In the fast lane are the US, UK, Canada, Australia, and New Zealand. In the slow lane, Japan and the euro-zone are barely back to square one. In the euro-zone, it was inevitable that slow recovery, fear of Greece leaving the Euro and the proximity to deflation would trigger further quantitative easing (QE). The inability of QE, though, to fix the underlying problems of a lack of competitiveness and the need for fiscal union, meant that comparisons with Japan's asset-price deflation continued.

**2016 Outlook**

With these factors likely to persist, world growth may show only the relatively shallow uplift to 3.4% year-on-year expected by the International Monetary Fund. With 2015's growth gap between emerging and advanced economies' down to just 2.1% year-on-year (the smallest since the dot.com boom in 2000), the pressure to continue supporting world growth may tilt back from emerging to advanced economies.

Our economic outlook for 2016 is based on four core beliefs.

First, not only will US and UK real policy rates stay negative into 2017, but peak rates will be much lower than historic levels. Critical to increasing inflation will be the labour market and oil prices. Given disparate worker participation rates, wage inflation looks more imminent in the US than in the UK. Oil prices may be struggling to recover amid plentiful supply, but will need to decline significantly to prevent some increase in headline inflation later in 2016.

**HERMES FUND MANAGERS LIMITED****STRATEGIC REPORT (continued)****Investment Review (continued)**

Second, ultimately, low peak rates will be delivered by central banks starting to run down some of their assets via 'QT' (quantitative tightening). Yet, normalisation will be slow. This is partly to avoid instigating a counter-productive reaction by equities and other growth assets. Inclusion of the labour market in the US Fed's dual mandate means it has started to raise rates, but the Bank of England's single, inflation targeting mandate suggests that it will be some time yet before it decides to follow suit.

One complication is the UK's EU referendum in 2016. Logic suggests it is unlikely the UK will want to risk weaker ties with its main trading partner, foreign direct investment forgone, and a diluted relationship with the US. But, the uncertainty could weaken the pound, and, should it occur, a 'Brexit' may even need the Bank of England to reactivate its QE.

Third, China has the means to soften its economic landing. Monetary policy can be loosened, with further falls in the renminbi, more direct lending, and a range of fiscal stimuli. Any local debt strains could be addressed by QE. More troublesome might be servicing its external corporate and bank debt, but the People's Bank of China could use its massive foreign exchange reserves to avoid systemic difficulties.

In Europe, Greece may have to restructure its debt, but with about 80% of it held by official institutions, private markets should be relatively insulated. The European Central Bank, though, like the Bank of Japan, may well have to extend liquidity, and maintain negative interest rates.

Fourth, despite pockets of vulnerability, it is not inevitable that any large-scale liquidity withdrawal will herald a broad crisis in emerging markets. Unlike in previous crises, their external debt ratios are generally lower, there are fewer fixed currency pegs to protect and they too can run QE.

In summary, we expect the baton of driving global growth to be handed back to the advanced economies, leaving China to enact an avalanche of stimulus measures to arrest its decline and avert further market turmoil. If it doesn't, the US Fed's rate tightening cycle could prove to be one of the shortest yet.

## **HERMES FUND MANAGERS LIMITED**

### **STRATEGIC REPORT (continued)**

#### **Investment performance and stewardship**

Our investment teams performed well during the year, generating strong risk adjusted returns across all strategies. For strategies with a three year track record, 100% by number outperformed their relevant benchmarks. Over one year, 91% of strategies outperformed their benchmarks. As at the year end, our overall equity active share was 87.76%. At a firm-wide level, our information ratio was 0.97.

For 2015, 50% of measurable strategies were 1st quartile and 89% above median. Over three years, 71% were first quartile and 86% above median.

This represents a continuation of the excellent performance achieved in recent years and demonstrates that our business can perform at these high levels consistently and deliver sustainable, risk-adjusted alpha to our clients. We believe that our Investment Office contributes meaningfully to this ability to generate consistently strong risk-adjusted returns. Industry recognition resulted in awards for our Asia ex Japan, emerging markets, global equity and real estate investment teams. At a corporate level, we were delighted to win the Best Sustainable Investment Fund Management Group award at Investment's Week's Sustainable Investment Awards in November and be awarded a rating of A+ by the Principles for Responsible Investment (PRI) for our overall approach to responsible investing – this compares to an A rating in 2014. We also received awards for our marketing and innovation alongside a corporate "Gold Standard" award from Incisive Media.

Our stewardship team was extremely active throughout the year. While most discussions are conducted behind closed doors, the team spoke out publicly when it was appropriate to do so. In total, on behalf of both the funds in which we invest and the assets on which we advise, the team engaged with 466 companies globally, across a wide range of ESG issues. During the year we were awarded our first combined investment and stewardship mandate. We believe this will become an increasing trend in years to come.

In summary, the business is well positioned to benefit from the long-term changes in global investment management. We appreciate the trust that clients place in us when they give us their money to manage or portfolios to engage on. We will continue to strive to deliver excellence, responsibly, so that we retain that trust and meet their and their beneficiaries' needs.

#### **Portfolio analysis**

Hermes' performance was strong across the majority of asset classes in 2015.

##### **Asia ex-Japan**

The performance of the Strategy exceeded the benchmark by 10.6%, co-incidentally approximately in line with the annualised relative return of 11% since inception. In 2015 China was a strong positive contributor to relative performance. The Strategy benefited from being invested in (non-benchmark) A shares in the first half of the year and from the out performance of US-listed Chinese American Depositary Receipts in the second half of the year. The overweight position and stock selection in South Korea also contributed. The main detractor was stock selection within India. Relative to peers, the strategy has been 1<sup>st</sup> quartile in each year since inception.

## **HERMES FUND MANAGERS LIMITED**

### **STRATEGIC REPORT (continued)**

#### **Investment Review (continued)**

##### **Global Emerging Markets**

In 2015, the performance of the main Strategy exceeded the benchmark by 11.9%. Stock selection was the main contributor to relative performance in 2015, notably in China and Taiwan. In addition, the underweight position and currency effect in Brazil also contributed to relative performance whereas the main detractor of relative performance was South Africa. Relative to peers, the Strategy remains 1<sup>st</sup> quartile over all periods since inception.

##### **Global Equities**

The performance of the main Strategy exceeded the benchmark by 1%, with the annualised relative return since inception also up 1.4% above benchmark. The strategy remains 1<sup>st</sup> quartile over 3 year, 5 year and since-inception periods. The main drivers of performance came from Europe with small contributions from Japan and Asia Pacific, driven by stock selection in all cases. The US, meanwhile became gripped by an increasing nervousness ahead of the Fed rate rise which led to strong returns from a handful of stocks. This was detrimental to the strategy, which seeks to be diversified across all sectors; this was therefore the main detractor of relative performance for the year.

##### **Multi Asset**

The performance of the Strategy underperformed the UK RPI by 2.8%, with the annualised relative return since inception also down by 2%. The matching portfolio was the main drag for the year whereas the enhancing portfolio gave a positive contribution. In terms of assets, the top detractors were commodity sectors, credit and risk factors and the top contributors were government bonds, equity indices and real assets. Relative to peers the strategy is 2<sup>nd</sup> quartile on a since-inception basis.

##### **Sourcecap**

All three Sourcecap Strategies outperformed their respective benchmarks, European Alpha (8.1%), Europe ex-uk (8.6%) and Eurozone (7%). With the strong outperformance in 2015 annualised relative performance since inception remained strong (European Alpha (3.3%), Europe ex-UK (3.5%) and Eurozone (2%)). In the main, Alpha strategy stock selection was the main contributor to relative performance, which accounted for approximately 85% of the excess return notably in Spain and the UK. The main detractor of relative performance was stock specific in our Netherlands holdings. Relative to peers, all three strategies are above median since inception.

##### **US SMID & Global Small Cap**

The performance of the US SMID Strategy exceeded the benchmark by 5.2%, with the Team Inception annualised relative return up 1.7%. Stock selection accounted for the majority of the out performance, notably Financial Services and Health Care. Producer Durables was the only detractor of relative performance. The Global Small Cap strategy outperformed in 2015 1.8% relative to its index and also remains ahead of its benchmark on a 3 year and since-inception basis. Stock selection was the main driver of out-performance, notably in Industrials and Consumer Discretionary. The main detractor of relative performance was Information Technology. The US All Cap strategy which launched at the end of May 2015 also outperformed its Index by 2.8%. Relative to peers, all three strategies are 1<sup>st</sup> quartile on a since-inception basis.



**HERMES FUND MANAGERS LIMITED****STRATEGIC REPORT (continued)****Investment Review (continued)****Credit**

Three out of four Credit Strategies outperformed their respective benchmarks/targets, namely High Yield (1.8%), Multi Strategy (3.1%) and Investment Grade (0.9%). Global High Yield also continued to deliver top quartile performance relative to its peers over 3 year, 5 year and since-inception periods. The newly launched Absolute Return strategy has returned +0.02% on an absolute basis and relative to its peers is top quartile. Key drivers of the excess returns across the range were our increase in quality bias, our favouring of financials vs. corporates bias, whilst avoiding distressed energy. This was partially offset by our overly conservative interest rate exposure, and our favouring of US and Emerging Markets over Europe.

**Real Estate**

For Real Estate UK Core and International strategies, YTD to end September 2015, relative performance was 1.2% and -0.3% respectively. The Hermes Property Unit Trust out-performed its benchmark for the full year 2015 by 1.4%, placing it top quartile within the Other Balanced Property Funds Index and the top fund over the five and ten year periods. The newly launched Real Estate Debt strategy has outperformed its target 3mth Libor + 2% by 0.9% on a gross IRR basis for the period 1 April 2015 to 31 December 2015. In addition, the new Residential Real Estate strategy underperformed its target -1.9% YTD to 30 September 2015, however this was due to various acquisition costs incurred on setup.

**HERMES FUND MANAGERS LIMITED****STRATEGIC REPORT (continued)****Responsibility**

During 2015, we engaged with 466 companies on a range of ESG issues. Encouragingly, with companies where we had set explicit objectives we were pleased to have made progress on just under half during the year. In addition to the 1,450 interactions (including meetings, calls and letters) with companies we voted at 9,831 company meetings, voting against management at 46.3% of meetings. In addition to engaging directly with companies we also carried out over 300 interactions with regulators, standard setters and other third parties in the pursuit of public policy objectives and continued to provide support for the 300 Club.

Engagement highlights in 2015 include a substantive increase in our focus on climate change engagement, in particular with extractives and utilities companies, which culminated in the tabling of shareholder resolutions at a number of major companies. Proxy access – the right of shareholders to nominate candidates to be elected as board directors at annual general meetings – dominated the dialogue between shareholders and companies in the US, where encouragingly, we were pleased to see many companies responding positively. Generally, the quantity and quality of engagement with US directors is on the rise. With the introduction of the Business Supply Chain Transparency on Trafficking and Slavery Act in the US and the Modern Slavery Act in the UK there was also an increased spotlight on our engagement on human and labour rights, which we expect to continue in 2016. Emerging issues which we started to engage on during 2015 included cyber risk – estimated to be costing the global economy over \$400 billion annually - and diversity at and below the board level.

In the run up to the 2015 UN Climate Change Conference in Paris, we carried out and published for the first time carbon footprinting analysis for our equity and corporate credit funds. Together with the emissions from our real estate portfolios which we have been measuring for close to 10 years and including using our office space and travel emissions, for 2014, our emissions was just over 1,375 tons Carbon Dioxide Equivalent, equivalent to about 140 households in the UK. In 2015 we also signed up to the Portfolio Decarbonisation Coalition and a focus in 2016 will be to systematically engage with the largest emitters in our portfolios. In our real estate portfolio, where we directly manage our assets, we have reduced emissions by an average of 6.5% per annum since 2006, a trend which continued in 2015.

**HERMES FUND MANAGERS LIMITED****STRATEGIC REPORT (continued)****Corporate Citizenship**

We strive to make a difference, not only through our investment and stewardship solutions, but in how we contribute to our wider community through a diverse programme of grassroots projects. Staff volunteer through our corporate programme or with other charities that are close to their hearts, taking part in lunchtime reading sessions with young people, renovating local schools and gardens, or supporting those more vulnerable within the London Borough of Tower Hamlets, which is one of the most deprived communities in Western Europe and also right on our doorstep. Notable partnerships include:

**Mosaic**

Mosaic strives to inspire young people from poorer communities to realise their talents and potential. It also aims to rehabilitate young offenders in prison.

**Business in Community**

Hermes is an active member of Business in Community, the Prince of Wales' responsible business network and a gender diversity "champion". Members of the network tackle a wide range of issues that are essential to building a fairer society and a more sustainable future.

**East End Community Foundation**

The EECF has been dedicated to increasing opportunities for people living in London's East End for 25 years. Hermes is working with them on a number of initiatives to help raise educational achievement, enhance employability and increase social cohesion.

## **HERMES FUND MANAGERS LIMITED**

### **STRATEGIC REPORT (continued)**

#### **Risk Management**

Hermes has a strong risk culture, which emphasises the importance of rigorous controls and procedures to safeguard the interests of its clients and other key stakeholders. It is the responsibility of all employees to uphold the risk and control culture throughout all levels of the organisation.

#### **The Role of the Board**

The Board is responsible for maintaining and reviewing the effectiveness of risk management and internal controls and for determining the nature and extent of the risks it is willing to accept in achieving its strategic objectives.

For the Board to accomplish its responsibilities it has established a governance framework primarily consisting of: the Risk and Compliance Committee, the Audit Committee and the Remuneration Committee, all the members of which are Non-Executive Directors. Day-to-day management of the business has been delegated to the CEO who has established an Executive Committee, as well as a number of oversight committees to support the governance framework, namely:

- Risk and Control Executive;
- New Product and Instrument Approval Committee;
- New Business Development Forum;
- Valuations Committee;
- Liquidity, Capacity and Pricing Committee;
- Outsourcing Review Group;
- Counterparty Credit Risk Group; and
- Portfolio Review Committee.

#### **Risk Management Framework**

A Group wide risk management framework is in place to identify, measure and manage key risks and controls throughout the Group. The risk and control framework is founded on three pillars:

- Risk appetite - key parameters which set out how much risk the Group is prepared to accept;
- Corporate governance - the legal, organisational and management structure; and
- Policies and standards - the rules that determine how the business should conduct itself.

The Board regularly performs an assessment of the risks that affect the Group. Each business area is also required to perform a risk and control self assessment specific to its own function. Business areas are required to warrant that all controls have operated effectively during each quarter and to review their risk assessments semi-annually for any changes in the business, systems and processes. Risk owners assess risks in terms of impact and likelihood of the risks happening. All errors and breaches are recorded in an operational risk database which allows for any failures in controls to be linked to the risk control self assessment process. A suite of key risk indicators is in place to measure key risks against the risk appetite statement and the risk register.

## HERMES FUND MANAGERS LIMITED

### STRATEGIC REPORT (continued)

#### Risk Management (continued)

##### The Three Lines of Defence

Hermes operates a 'three lines of defence' model to risk management.

1. Business areas are responsible for the identification and management of risks;
2. The Risk, Compliance, Legal and Finance areas provide further oversight; and
3. Independent assurance is provided by Internal Audit.

Comprehensive insurance coverage provides an extra layer of assurance.

##### Capital Adequacy

The primary purpose of the Internal Capital Adequacy Assessment Process (ICAAP) is to inform the Board of the ongoing assessment of the Group's risks, how the Group intends to mitigate those risks and how much current and future capital is necessary having considered other mitigating factors. The ICAAP is formally undertaken annually, with more frequent updates when a material change occurs. Stress and scenario testing have been developed in order to test the robustness of the Group's regulatory capital against a variety of events.

Further details of the Group's approach to capital adequacy can be found on the Hermes website: <http://www.hermes-investment.com/en-gb/literature.aspx>

The following table summarises the key business risks and mitigating actions:

Risk	Mitigants
<b>1 - REPUTATIONAL RISK</b>	
Reputational risk relates to the Hermes brand, press and marketing activity as well as ethics, trust, relationships with stakeholders, conduct and the overall culture and values of the firm.	Responsibility, appropriate conduct and a principled approach to treating investors fairly, are integral to Hermes' culture. This culture is set via 'tone from the top' and is underpinned by 'Responsibility', which is explicitly stated as one of Hermes' core values and is included in the Hermes Pledge (The Pledge, issued in 2015, is the foundation of Hermes' commitment to always put its clients first, and to act responsibly and transparently). Please refer to page 89 for the Hermes Pledge.
Reputational risk can arise from any of the key risks outlined below.	Hermes engages in proactive communications with all stakeholders and monitors media coverage to understand how the Hermes reputation is perceived. Reputational risk is a key consideration in any strategic decision.

## HERMES FUND MANAGERS LIMITED

## STRATEGIC REPORT (continued)

## Risk Management (continued)

Risk	Mitigants
<b>2 - STRATEGY EXECUTION RISK</b>	
<p>The risk that Hermes does not meet its long term strategic objectives.</p>	<p>Hermes has a detailed strategic vision and plan, supported by its business operating model, which is cascaded throughout the organisation. Strategic planning includes an assessment of risks, client impact and consideration of risk appetite and capital. Indicators and financial metrics are in place to monitor progress against strategic objectives.</p> <p>A diversified range of products is offered, with regular new product launches to ensure that the offering remains in keeping with changing client requirements. A range of distribution channels mitigates against an excessive dependency on any single sales channel.</p>
<b>3 CLIENT CONCENTRATION RISK (RELIANCE ON BTPS)</b>	
<p>This risk relates to the loss of a key client or support from a key stakeholder (BTPS) and, therefore, as a result having a detrimental impact on the Firm.</p>	<p>This risk is mitigated by the Firm growing its third party offering (as demonstrated on page 9) and diversifying its client base, whilst continuing to meet the requirements of its clients and stakeholders.</p>
<b>4 - ECONOMIC / MARKET ENVIRONMENT RISK</b>	
<p>Market risk arises from market movements, which can cause a fall in the value of principal investments and a decline in the value of assets under management.</p>	<p>Hermes offers a diversified and broad product range which provides clients with solutions tailored to a variety of market conditions and serves to diversify individual market dependencies.</p> <p>The Board has a limited appetite for market risk; therefore Hermes does not trade on its own account and only holds proprietary investments for hedging purposes.</p> <p>The Firm minimises its exposure to foreign exchange risks through regular review of its foreign currency business needs.</p>
<b>5 - INVESTMENT PERFORMANCE RISK</b>	
<p>The risk that portfolios will not meet their investment objectives, adversely affecting levels of new business or fee income.</p>	<p>The Hermes Investment Risk Framework provides monitoring and challenge of investment risks and performance across teams. The Hermes Investment Office independently monitors risk and ensures the rigour of team strategies. Investment teams adhere to clearly-defined investment processes. Various management committees such as the Valuations, Liquidity Capacity and Pricing and Portfolio Review are in place, providing an extra layer of mitigation.</p>

## HERMES FUND MANAGERS LIMITED

### STRATEGIC REPORT (continued)

#### Risk Management (continued)

Risk	Mitigants
<b>6 - PEOPLE RISK</b>	
<p>The risk that key staff across the business leave or are not adequately motivated in their rôle as well as significant reliance on a small number of key staff members.</p>	<p>To mitigate people risks, the Firm has competitive remuneration and retention plans in place, with appropriate deferred benefits targeted at key employees. In line with its Principles, the Group puts in place sustainable succession and development plans. Clear objectives are set and success is measured in the annual review process, allowing the Group to identify motivational development initiatives for its staff including regular and sufficient training.</p>
<b>7- PENSION LIABILITY RISK</b>	
<p>The risk that the defined benefits pension liability increases and consequently reduces solvency levels. This could also create an obligation to increase funding into the scheme leading to cash flow difficulties.</p>	<p>To mitigate the possible detrimental effects caused by pension volatility, the Group has obtained a Deed of Support from its owner, BTPS, to inject capital into the Group if the pension deficit increases significantly to the extent that it is required for regulatory capital purposes.</p> <p>The scheme's future strategic direction is regularly reviewed and the mis-match between the scheme's assets and liabilities regularly monitored.</p>
<b>8 - REGULATORY &amp; LEGAL RISK</b>	
<p>The risk of legal or regulatory action resulting in fines, penalties, censure and/or legal action arising from failure to identify or meet regulatory and/or legislative requirements in those jurisdictions in which Hermes operates.</p> <p>The risk that new regulations or changes to the interpretation or implementation of existing regulations affect the Group's operations and cost base.</p>	<p>Hermes relies on its employees, with support from the Compliance, Risk, Finance and Legal functions, to consider carefully the obligations the Group assumes and compliance with them.</p> <p>Hermes maintains compliance procedures across the Group and compliance with relevant regulatory requirements is monitored in accordance with a risk-based programme.</p> <p>Key regulatory change risks are identified by Compliance as part of regulatory change monitoring and are also included on an Emerging Risks Assessment where appropriate.</p>

## HERMES FUND MANAGERS LIMITED

### STRATEGIC REPORT (continued)

#### Risk Management (continued)

Risk	Mitigants
<b>9 - MATERIAL ERROR / MANDATE BREACH RISK</b>	
<p>The risk of a material error, investment mandate breach or unauthorised / fraudulent activity occurring.</p>	<p>A strong control environment exists at Hermes which is supported by detailed policies and procedures. Robust internal controls are in place to mitigate and monitor client and fund limits. All pre and post trade monitoring is automated.</p> <p>Hermes has a Whistle-Blowing policy in place which encourages open communication and the highest standards of integrity and honesty.</p> <p>Hermes expects employees to behave responsibly, which is one of the Group's core values. The firm demands high ethical standards of all staff. Controls are in place to prevent and detect unauthorised activity. Insurance cover is in place to cover certain specified significant error. Internal audits, external audits and insurance coverage provide an extra layer of assurance.</p>
<b>10 – PRODUCT / INSTRUMENT RISK</b>	
<p>Product risk arises from product complexity and the risk that these products either do not meet their performance objectives or are unsuitable for certain clients.</p> <p>Product risk can also arise from capacity constraints where the size of assets under management in a particular asset class or strategy makes it more difficult to trade efficiently in the market.</p> <p>Financial instruments can take many forms, for example, equities (stocks), fixed income, debt, money market as well as more sophisticated derivative instruments, and trading, operational and other idiosyncratic instrument-related risks can result due to sophistication, etc.</p>	<p>Hermes has a dedicated Product Development team and a product approval and review procedure. The suitability of products for clients is carefully considered. Hermes monitors potential capacity constraints and mitigates them by restricting or preventing inflows into products where necessary.</p> <p>Specialist resources are used if Hermes cannot fully support products / instruments. Appropriate legal agreements are in place for all new products / instruments.</p> <p>Product Development Policy, Instrument Approval Policy and Investment Market Approval Policy are all approved and communicated.</p>
<b>11 - FINANCIAL PROMOTIONS / DISTRIBUTION RISK</b>	
<p>The risk that products are misrepresented to clients.</p>	<p>Distribution and investment teams work closely with Compliance to ensure that marketing materials are accurate and not misleading.</p> <p>A number of training sessions are run by Compliance. Financial promotions are subject to regular Compliance monitoring.</p>



# HERMES FUND MANAGERS LIMITED

## STRATEGIC REPORT (continued)

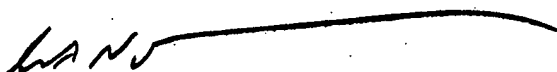
### Risk Management (continued)

Risk	Mitigants
<b>12 - OUTSOURCING RISK</b>	
The risk that an outsource provider fails to deliver the expected levels of service.	Before entering into outsourcing arrangements, the Group undertakes due diligence on outsource providers. A programme of regular oversight and assessment against agreed service levels is in place, overseen by the Outsourcing Review Group Committee.
<b>13 – TECHNOLOGY, IT SECURITY &amp; BUSINESS CONTINUITY RISKS</b>	
The risks that technology systems and support are inadequate or fail to adapt to changing requirements, that systems are vulnerable to third-party penetration or that the business cannot continue in the event of a disaster.	Hermes relies on technology and qualified professionals to maintain its infrastructure and invests in IT accordingly. Hermes has a dedicated Information Security Officer who ensures robust processes are adhered to and who is responsible for monitoring cyber crime attacks. A business continuity programme is in place, with regular testing.
<b>14 - COUNTERPARTY CREDIT RISK (HERMES OWN FUNDS)</b>	
The potential that a counterparty will fail to meet its obligations in accordance with agreed terms, thus giving rise to a risk to earnings and/or capital.	This is in respect of Hermes own balance sheet investments as clients assume the risk of counterparty default and settlement risks in accordance with the risks of investing. The Counterparty Risk area reviews and approves counterparties as well as limits on a regular basis. The Treasury desk places cash out on deposit only with approved counterparties with high ratings, within prescribed limits. Counterparties are regularly reviewed for creditworthiness. And, oversight is provided by Counterparty Credit Risk Group.
<b>15 - LIQUIDITY RISK</b>	
The risk of insufficient financial resources to enable obligations to be met as they fall due or such resources can only be secured at excessive cost.	Monthly cash forecasts are prepared based on projected revenues and approved cost budgets to ensure sufficient liquidity is available at all times. Cash held on deposit is used as a liquidity source.
<b>16 UNAUTHORISED / ROGUE TRADING RISK</b>	
The risk of unapproved activities in the Firm including a trader operating in an inappropriate manner causing loss to the company and/or compromising Hermes' reputation.	An extensive system of internal controls is in place including: segregation between front & back offices, payment controls (e.g. authorised signatories & limits, independent approval by Middle Office cash management), oversight by senior management and pre & post trade checks carried out (some automated and some manual).

**HERMES FUND MANAGERS LIMITED****STRATEGIC REPORT (continued)****Risk Management (continued)**

<b>17 – CHANGE RISK</b>	
The risk of material breakdown in normal operations, in a period of significant change, or a failure to deliver key aspects of a major change initiative; resulting in failure to deliver the expected benefits (for example; it cannot be adequately supported) as well as incurrence of significant overrun on time / cost in the change programmes / initiatives.	There is in place a comprehensive Change Governance process including policies, procedures and Senior Management oversight directly and/or via applicable Board/Management committees.

Approved by order of the Board of Directors and signed on behalf of the Board



**S Nusseibeh**  
Chief Executive Officer

31 March 2016

## HERMES FUND MANAGERS LIMITED

### DIRECTORS

The Board comprises the following Directors:

Name	Biography
P Spencer*	Paul was appointed Chairman of Hermes in June 2011. He is the Chairman of the BT Pension Scheme, the BA and Rolls Royce pension funds. He is a past President of the Association of Corporate Treasurers, a past Chairman of NS&I (National Savings), a past Chairman of the Audit Committee of WPP and was appointed CBE in the 2010 New Years Honours 'for services to financial services'.
K Matthews*	Kathryn was appointed Non-Executive Director of Hermes in August 2009. Kathryn also serves as a Non-Executive Director of Rathbone Brothers Plc. Her career has been spent entirely in the asset management industry with extensive UK and international experience managing money, leading investment management teams and building the institutional business of asset managers. She spent six years at Fidelity in various roles, most recently as CIO for the Asia Pacific region. Her career has also included senior roles at William Mercer, Axa Investment Managers, Santander Global Advisers and Baring Asset Management. Kathryn has a BSc in Economics from Bristol University.
W McClory*	Billy was appointed Non-Executive Director of Hermes in August 2010. He was employed by Post Office Telecommunications 1968-78, became a National Officer of CPSA, then National Communications Union ("NCU") in 1984 and Communication Workers Union in 1995. Responsible in the NCU for pension matters in the Post Office and BT, Billy was the lead officer on pension matters for the BT Unions 1990-97. He is a Trustee Director of the BT Pension Scheme and a member of UNITE (formerly the National Federation of Post Office & BT Pensioners).
S Nusseibeh	Saker is the Chief Executive Officer of Hermes. Saker was appointed as Chief Executive Officer in May 2012 having been interim Chief Executive Officer since November 2011. Saker joined Hermes in June 2009 as a main board director to drive, support and represent the investment capabilities of Hermes. In 2005, Saker joined Fortis Investments USA as CIO Global Equities and moved on to become Global Head of Equities, responsible for managing the company's 12 Equity centres. Previously he was CIO Global Equities and Head of Marketing of SGAM UK where he re-orientated the company offering to include high alpha UK strategies and a Global offering, following on from the sale of Trust Company of the West (TCW) to SGAM, where he was Managing Director running various Global and International strategies as well as the London office. Saker started his career at Mercury Asset Management in 1987.

\* Non-executive

# HERMES FUND MANAGERS LIMITED

## DIRECTORS (continued)

H Steel	Harriet joined Hermes as Head of Sales and Marketing in November 2011. Prior to Hermes, Harriet ran Portico Advisors from 2004. Portico raised assets globally for independent alternative asset managers across a range of strategies including Hedge Funds, Private Equity, Real Estate and Structured Products. Previously Harriet sold Fixed Income and Currency Derivatives at both Morgan Stanley and Bankers Trust Company. Harriet has a degree in Architecture from Princeton University.
D Watson*	David is an Associate of the Institute of Chartered Accountants in England and Wales and was appointed Non-Executive Director of Hermes in July 2011. Currently, David is Senior Independent Director of Countrywide Plc, a Non-Executive Director and Chairman of the Audit Committee at Charles Taylor Consulting Plc and TR Property Investment Trust Plc and Non-Executive Director of Kames Capital Plc and TR Property Investment Trust Plc. Prior to joining Hermes, David was the Chief Financial Officer (CFO) of Aviva General Insurance UK Division and between 2003 and 2007 he was the CFO of Morley Fund Management, the asset management arm of the Aviva Group. Previous to this, he spent nine years at M&G Group Plc (now M&G Investments), where he was Group Finance Director, responsible for financial management and strategic development of the group.
I Kennedy	<p>Ian is Chief Operating Officer of Hermes, a member of the Executive Committee (ExCo), and an Executive Board Director. Ian joined the firm in 2015, taking responsibility for Finance, IT, Legal, HR, Operations and Facilities.</p> <p>Ian graduated from King's College, University of London with a BSc in Biochemistry, and qualified as a chartered accountant with Arthur Andersen &amp; Co. He entered the City in 1992, joining Prudential Bache Ltd, initially as European accountant and subsequently as regional risk and control manager. In 2002, Ian joined Dryden Wealth Management as Finance Director, joining Fortis in 2005 when they acquired the firm. Ian became COO for the UK wealth management and private banking division, ultimately acting as interim CEO and leading its sale to BNP Paribas in 2009-10, where he then became Chief Operating Officer and Chief Financial Officer of BNP Paribas Wealth Management UK. In 2012, Ian established InvestMe Financial Services LLC, one of the earliest firms in the UAE to be approved for investment advisory business activities by the Securities and Commodities Authority in Abu Dhabi.</p>

\* Non-executive

**HERMES FUND MANAGERS LIMITED****DIRECTORS (continued)**

D Stewart*	David is currently Chairman of IMM Associates, a non executive director of both Caledonia Investment Trust and Hargreave Hale, and a non executive representative on the MacMillan Cancer Care Investment Committee. His prior experience includes nine years at Odey Asset Management, initially as CEO and latterly as a non executive director until standing down in December 2014. Before that, David's career encompassed Fidelity Investments (1994-2005), James Capel (1986-1994) and Swire Pacific Ltd, Hong Kong (1981-1986).
------------	---

\* Non-executive

The following Directors were appointed to the Board during the year	Ian Kennedy (1 December 2015) David Stewart (1 April 2015)
---	---

With the exception of Paul Spencer and Billy McClory, who do not meet the definition of independence in the UK Corporate Governance Code as they serve as Trustees of the BT Pension Scheme, the Group's ultimate parent company, each of the other non-executive members of the Board and each Committee are considered independent.

## **HERMES FUND MANAGERS LIMITED**

### **REPORT OF THE AUDIT COMMITTEE**

#### **MEMBERSHIP**

The Audit Committee currently comprises four Non-Executive Directors, David Watson (Chairman), Billy McClory, Kathryn Matthews and David Stewart (who was appointed to the committee on 1 April 2015). Members of the Committee are appointed by the Board following recommendations from the Nomination Committee.

Each member of the Committee brings relevant financial services experience from senior executive experience. David Watson, the Committee Chairman is considered by the Board to have significant, recent and relevant financial experience.

#### **RESPONSIBILITIES**

The Committee's primary responsibilities are to assist and advise the Board. The scope includes, but is not limited to:

- reviewing and challenging, where appropriate, the actions and judgements of management in relation to the Company's financial statements, business review and any related formal statements before submission to, and approval by, the Board;
- monitoring and reviewing the activities, processes and performance of both internal and external audit;
- monitoring compliance with internal codes of conduct and other policies;
- monitoring the quality and integrity of the financial statements of the Company; and
- reviewing and challenging, where appropriate, the risk management framework, systems, processes, procedures and controls in relation to all investment management activity and administration services that the Company has contracted to provide to its clients.

#### **WORK OF THE COMMITTEE DURING 2015**

Major topics considered or activities performed by the Committee during the financial year were:

- review of the Group's reporting, financial statements and key accounting judgements;
- review of briefings on the latest consultation papers from regulatory and professional bodies on company stewardship and corporate governance;
- approval of new Group policies and material changes to existing policies;
- approval, monitoring and resourcing of the Internal Audit Plan;
- review and debate of issues raised in Internal Audit reports including the sufficiency of management responses;
- commissioning an external effectiveness review of Internal Audit. The actions arising from the review were considered by the Committee and they are monitoring their implementation.
- active monitoring of the timely completion of agreed action points from past reports and escalation of important overruns;
- the appointment, scope of work and findings of the external auditor and consideration of any conflicts of interest;
- active monitoring of the defined benefit pension scheme, regulatory capital and capital funding requirements; and
- consideration of the accounting implications as a result of the adoption of FRS 102.

## **HERMES FUND MANAGERS LIMITED**

### **REPORT OF THE RISK AND COMPLIANCE COMMITTEE**

#### **MEMBERSHIP**

The Risk and Compliance Committee ("the Committee" or "RCC") currently comprises four Non-Executive Directors; they include: David Stewart (who was appointed to the committee on 1 April 2015), David Watson, Billy McClory and Kathryn Matthews. Mr. Stewart acts as the Chairman of the Committee. The RCC, as a committee of the Board, deals with all matters that it considers appropriate. Each member of the Committee brings relevant financial services and senior executive experience.

The Group Chief Executive Officer and/or Chief Operating Officer, Head of Risk and Head of Compliance will attend meetings at the request of the Committee. The Chairman of the Committee may also require other employees or external advisors to attend meetings as required to enable the Committee to carry out its responsibilities.

#### **RESPONSIBILITIES**

The Committee's primary responsibilities are to assist and advise the Board of Directors on the following:

- the Risk Management Framework and specifically the effectiveness of risk management, governance and compliance activity within the Group. The Committee will support the Board in its consideration of business activities that expose the business to material risk focusing on current and forward-looking aspects of risk exposure;
- the methodology and assumptions used in the Group's models for determining its regulatory capital, satisfying itself that the models are fit for purpose;
- ensuring adequate identification, measurement, monitoring and reporting on all types of risks including, but not limited to, business risk, operational risk (including regulatory risk), market/investment risk, credit risk, reputational risk and liquidity risk;
- ensuring that risk is properly considered in setting the overall remuneration policy for the Group and the remuneration of the executive directors and other senior executives;
- oversee the management of relationships and registrations regulatory authorities and to review developments and prospective changes in the regulatory environment; and
- any material or prospective legal actions involving the Group.

#### **WORK OF THE COMMITTEE DURING 2015**

Major topics considered by the Committee during the year were:

- assessment of Governance Structure and Terms of Reference;
- review of the Risk Appetite Statement and Risk Management Framework;
- analysis of the Internal Capital Adequacy Assessment Process (ICAAP) report (including risk assessment, errors & breaches, emerging risks, capital & liquidity, scenario analysis and reverse stress testing);
- approval of new Group policies and material changes to existing policies;
- consideration of major regulatory changes;
- consideration of IT Security - Information Security (sometimes referred to as 'cyber');
- evaluation of 2015 Risk Plan;
- review and challenge of reports received from internal audit, regulators, risk and compliance functions;
- evaluation and follow-up of Kinetics (independent consultants) report: 'High Level Review of Compliance and Risk Framework';
- discussion of key topics through the Risk Story Board review;
- discussion of direction in the development of the Conduct Risk Framework; and
- review and debate of reports received from regulators and the risk and compliance functions.

**HERMES FUND MANAGERS LIMITED****REPORT OF THE REMUNERATION COMMITTEE****MEMBERSHIP**

The Remuneration Committee currently comprises five Non-Executive Directors, Kathryn Matthews (Chair), Paul Spencer, David Watson, Billy McClory and David Stewart who was appointed to the committee on 1 April 2015.

**STATEMENT FROM THE CHAIR OF THE REMUNERATION COMMITTEE**

Our primary focus continues to be centred on advising the Board of Directors on remuneration matters. This advice takes shape through our policies and plans which are designed to motivate and retain high-calibre executive directors, senior management and staff. The financial services industry has continued to evolve through 2015; existing regulations are bedding in while new regulations are being discussed, and the UK government is implementing immense changes to the existing pension regimes.

We believe that compensation must be aligned with long-term performance, reflect strong risk management and encourage a responsible culture with regard to both our investments and our relationships with key stakeholders. It is important that our remuneration framework be clear, understandable and achievable in order to motivate and retain our employees and ensure alignment with the strategic business targets agreed with our Shareholder. This is done by using a combination of fixed and variable compensation tools enabling management to encourage the right behaviours and strong performance over the short, medium and long term. Management are charged with applying their discretion as they steer the Company within a clear risk management framework. Management are supported in these responsibilities by the consistent application of the Company's performance and behaviour matrix used as part of the annual appraisal discussion, introduced in 2014. This has been reinforced by the recent introduction of a Hermes Pledge which underpins the importance of putting the client first and acting responsibly and transparently. An overview of how Hermes' Remuneration Policies align the interests of senior employees with our purpose is set out on the following page.

Hermes' ongoing strategy to build a first-class asset management business which attracts strong third-party assets flows continues to deliver well ahead of the original business plan and it is therefore imperative to make sure that the remuneration strategy evolves with the business strategy. We will continue to review remuneration policy in anticipation of this growth and with the changing shape of the Company. The long term growth and success of the Hermes Group will continue to be linked to individuals' remuneration.

Kathryn Matthews



## HERMES FUND MANAGERS LIMITED

### REPORT OF THE REMUNERATION COMMITTEE (continued)

Individual pay elements support our purpose and align interests with clients and stakeholders	
<b>Bonus</b>	<p>Encourages all employees to deliver high levels of performance and demonstrate behaviours that are in line with the corporate values</p> <p>The formula driven bonus pool funding ensures the interests of the shareholders, investors and stakeholders are addressed first, followed by employee interests – who are measured on performance and behaviour.</p>
<ul style="list-style-type: none"> <li>• The discretionary bonus scheme is for all eligible employees</li> <li>• Bonus pool is based on company revenue and profit</li> <li>• Individual awards are based on an assessment of an individual's performance and behaviours with reference to firm performance, team performance and market intelligence</li> <li>• All bonus allocations are reviewed by the Executive Committee and the top 50 reviewed by the Remuneration Committee</li> <li>• The level of deferral is dependent on the quantum of the bonus</li> </ul>	
<b>Co-investment / bonus deferral scheme</b>	<p>Aligns short and long-term interests of employees with our clients and stakeholders. In particular, co-investment aligns the interests of investment professionals with those of the shareholders and investors.</p>
<ul style="list-style-type: none"> <li>• The discretionary bonus scheme is for all eligible employees whose bonus is £50,000 or greater</li> <li>• Awards vest over three years in equal tranches and the performance period does not restart each year</li> <li>• Over the performance period, the underlying award notionally tracks fund(s) performance.</li> <li>• For investment professionals at least 50% of their deferred award is notionally co-invested into the fund(s) they manage and the remaining 50% in funds from across the firm.</li> <li>• During the vesting period for deferred compensation, awards are subject to the malus clause in the plan rules. After the vesting, awards remain subject to clawback.</li> </ul>	
<b>Long-term incentive plan (LTIP)</b>	<p>Aligns the interests of employees to those of the shareholder and investors by encouraging employees to grow profits over the long term through sustained performance.</p>
<ul style="list-style-type: none"> <li>• Participants are selected at the discretion of the Executive Committee on the basis of an employee's projected ability to influence the company over the performance period</li> <li>• Performance figures are measured following the close of the fourth year of the award; the award is calculated on a proportional basis for all participants</li> <li>• The awards vest as a single amount after four years</li> <li>• The vested award is delivered to the recipient as a cash payment</li> </ul>	
<b>Discretion</b>	<p>The Remuneration Committee has the ability to apply discretion to adjust the bonus pool and any individual payments including those paid out in individual incentive schemes.</p> <p>The Remuneration Committee challenge bonus recommendations and are empowered and charged to approve or not approve recommendations put before them.</p>

### Performance

The Remuneration Committee, in accordance with its Terms of Reference, review and approve the annual objectives of the Executive Directors of the Board against which their performance for remuneration purposes is measured and aligned with the Company's performance.

### Non-Executive Directors

Non-executive director remuneration is reviewed by the Chairman and the Chief Executive and implemented, where appropriate, following approval of the ultimate parent undertaking. The fees for non-executive directors are reviewed every two years.

## **HERMES FUND MANAGERS LIMITED**

### **REPORT OF THE REMUNERATION COMMITTEE (continued)**

#### **RESPONSIBILITIES**

The Committee's primary responsibilities are to assist and advise the Board of Directors regarding, among others:

- determine the overarching principles and parameters of the remuneration policy on a Hermes group-wide basis, excluding Hermes GPE LLP which is a joint venture;
- establish and maintain a competitive remuneration package to attract, motivate and retain high calibre executive directors and senior management across the Group;
- align senior executives' remuneration with the interests of shareholders and relevant remuneration legislation;
- ensure compliance with the FCA and other regulator rules with regards to remuneration; and
- review and approve the annual objectives for Executive Directors of the Board against which their performance for remuneration purposes will be measured.

#### **WORK OF THE COMMITTEE DURING 2015**

During the year the Committee received and approved updates on the continued development of the Hermes remuneration policies and structure, including:

- introducing the Long Term Incentive Plan (LTIP) to support the evolved One Hermes strategy
- winding down the Equity Participation Plan which has been replaced by the LTIP
- continuing to apply regulations to compensation matters, and monitor developments of new regulations and government policies; and
- engaging external advisors to ensure a competitive and market-aligned future.

In line with the internal changes, the Committee received and reviewed the remuneration principles for the Group as we continue to evolve. The Committee also reviewed and endorsed salary and bonuses to be awarded during 2015 under the agreed terms of reference, and reward plans in accordance with parameters previously approved by the Committee. The Committee believes that these plans, operated within the positive culture of strong performance and behaviour that exists in the business, supported by the matrix and Hermes Pledge, provide alignment between Management and both our shareholder and clients, and are in accordance with the relevant legislative changes and best practice.

In setting these parameters and approving the awards, the Committee was aware of the market environment, peer group practice and the financial and investment performance of Hermes.

#### **DIRECTORS' EMOLUMENTS**

Directors' emoluments, all of which have been approved by the Remuneration Committee, are disclosed in Note 8 to the financial statements.

## **HERMES FUND MANAGERS LIMITED**

### **REPORT OF THE NOMINATION COMMITTEE**

#### **MEMBERSHIP**

The Nomination Committee currently comprises all Non-Executive Directors of the Company.

#### **RESPONSIBILITIES**

The Committee's primary responsibilities are to assist and advise the Board. The scope includes, but is not limited to:

- evaluating the balance of skills, knowledge and experience of members;
- regularly reviewing the structure, size and composition of the Board;
- identifying and nominating candidates for appointment to the Board
- considering the leadership needs of the Group and considering succession planning for Directors and other senior executives;
- assessing the contribution of Non-Executive Directors; and
- approving the appointment of any director to the Board of a subsidiary operating company of the Group.

#### **WORK OF THE COMMITTEE IN 2015**

Major topics considered by the Committee during the year were:

- recommendations made to the Board for the appointment of new directors;
- the appointment of one independent Non-Executive Director, an Executive Director, a new Chairman and a new Company Secretary;
- appointments to the Boards of the main subsidiary companies of the Group;
- Board evaluation; and
- noting the satisfactory operations of the committee and reviewed its terms of reference.

#### **BOARD DIVERSITY**

We are long-standing supporters of diversity in the boardroom and we are supportive of efforts to encourage diversity in all its aspects in the boardroom and, more generally, throughout the Group. Our current Board is made up of eight directors of whom two (25%) are women. Appointments to the Board are made having considered a number of different criteria, including appropriate skill sets, experience and expertise as well as all measures of diversity. We continue to expect that long lists and short lists of possible appointments to the Board reflect this position.

## HERMES FUND MANAGERS LIMITED

### DIRECTORS' REPORT

Secretary: Michelle Green (resigned 7th August 2015)  
Sue Cane (appointed 7th August 2015)

Registered Office: Lloyds Chambers, 1 Portsoken Street, London E1 8HZ.

Registered Number: 1661776

The Directors present their report on the affairs of the Group, together with the financial statements and auditor's report, for the year ended 31 December 2015. The Directors who served during the year are listed on pages 26-28.

The Chairman's statement and the Audit, Risk and Compliance, Remuneration and Nomination Committee reports form part of this Directors' report.

### RESULTS AND DIVIDEND

The results for the year are shown in the Consolidated Profit and Loss Account. A detailed business review is included in the strategic report. The Directors consider that the Company is well placed to take advantage of future opportunities. The overall performance of the Group is explained in the Financial Review section of the Strategic report on pages 9-11. Further, the Group's principal risks and uncertainties are disclosed in the Risk Management section and key performance indicators are provided in the Investment Performance section of the Strategic report.

The Directors do not recommend a dividend payment in respect of 2015 (2014: £nil). During 2015 dividends have been declared and paid by subsidiaries of the Company. Dividends paid to minority shareholders are shown on page 45.

### GOING CONCERN

Having made all reasonable enquiries and having regard to the nature of the Group and its activities, the Directors are satisfied at the time of approving the financial statements, that there is a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis in preparing the annual financial statements.

As part of their enquiries, the Directors have reviewed the adequacy of the Group's regulatory capital position under a number of scenarios. They have also considered a deed executed by BTPS on 14 January 2016 to provide additional capital to the Hermes Group should the Hermes directors deem that its capital is insufficient to meet regulatory capital requirements and that the insufficiency arises from obligations in respect of the Hermes Group Pension Scheme. Accordingly, they continue to adopt the going concern basis in preparing the financial statements for the year ended 31 December 2015. Further details regarding the adoption of the going concern basis can be found in the Statement of accounting policies in the financial statements.

### FINANCIAL INSTRUMENTS

The Group has financial instruments including debtors, creditors, investments and cash. These mostly arise from the Group's operations. The Group has a policy of identifying and controlling the risks associated with such instruments. These risks include credit risk, liquidity risk and interest rate risk. Bearing in mind the nature of the exposure to financial instruments within the Group and the limited risks associated with them, the Directors are satisfied that there is adequate control of the risks. Note 26 presents further information on the Group's financial risk management objectives and strategy.

## **HERMES FUND MANAGERS LIMITED**

### **DIRECTORS' REPORT (continued)**

#### **DIRECTORS' INDEMNITIES**

Qualifying third party indemnity provisions, which were made during the year for the benefit of directors, remain in force at the date of this report.

#### **EMPLOYEE CONSULTATION**

The Group places considerable value on the involvement of its employees and has continued to keep them informed on matters affecting them as employees and on the various factors affecting the performance of the Group and the Company.

This is achieved through formal and informal meetings, the Company magazine and a special edition for employees of the annual financial statements. Employee representatives are consulted regularly on a wide range of matters affecting their current and future interests. The Growth share scheme has been successfully replaced with a Long Term Incentive Plan ("LTIP") since the beginning of 2015. The LTIP is discussed in more detail in note 21. In addition, all employees are eligible to receive an annual bonus related to the overall profitability of the Group.

During the year meetings are held by executive management to discuss the performance of the Group with all employees. Opportunity is given at these meetings for senior executives to be questioned about matters which concern the employees.

#### **EQUAL OPPORTUNITIES POLICY**

Hermes is committed to equality and diversity. Applications for employment are always fully considered, regardless of gender, marital status, sexual orientation, age, disability, ethnic or national origin, bearing in mind the aptitudes of the applicant concerned. In the event of members of staff becoming disabled, every effort is made to ensure that their employment with the Group continues and that appropriate training is given or any other reasonable arrangements are made. The Group aims to ensure that employees are treated on the basis of their merits, abilities and potential regardless of gender, marital status, disability, ethnic or national origin.

#### **AUDITOR**

Deloitte LLP have indicated their willingness to continue in office as auditor and will be deemed to be reappointed at the end of the next period for appointing auditors as defined in section 485(2) of the Companies Act 2006. The Board expects to complete an audit tender process in 2016, the result of which will apply to the audits of all financial periods commencing after 1 January 2017.

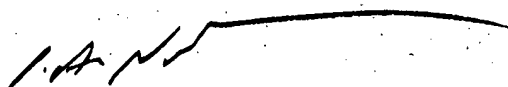
**HERMES FUND MANAGERS LIMITED****DIRECTORS' REPORT (continued)****STATEMENT ON DISCLOSURE OF INFORMATION TO THE AUDITOR**

The directors, having made enquiries to fellow directors and the Company's auditor, can state that:

- so far as they are aware, there is no relevant audit information of which the Company's auditor is unaware; and
- they have taken all reasonable steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Approved by order of the Board of Directors and signed on behalf of the Board



S Nusseibeh  
Chief Executive Officer

31 March 2016

**HERMES FUND MANAGERS LIMITED****STATEMENT OF DIRECTORS' RESPONSIBILITIES**

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland".

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

## **INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF HERMES FUND MANAGERS LIMITED**

We have audited the financial statements of Hermes Fund Managers Limited for the year ended 31 December 2015 which comprise Consolidated Profit and Loss Account, Consolidated Statement Of Income, Consolidated and Company Balance Sheets, Consolidated and Company Statement of Changes in Equity, Consolidated and Company Cash Flow Statements and the related notes 1 to 30. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland".

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

### **Respective responsibilities of directors and auditor**

As explained more fully in the Statement of Directors' Responsibilities, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### **Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### **Opinion on financial statements**

In our opinion the financial statements:

- give a true and fair view of the state of the Group's and the parent company's affairs as at 31 December 2015 and of the Group's profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.



**INDEPENDENT AUDITOR'S REPORT TO THE MEMBER OF HERMES FUND MANAGERS LIMITED (continued)****Opinion on other matter prescribed by the Companies Act 2006**

In our opinion, based on the work undertaken in the course of the audit:


- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

**Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.



Calum Thomson FCA (Senior Statutory Auditor)  
for and on behalf of Deloitte LLP  
Chartered Accountants and Statutory Auditor  
London, United Kingdom

31 March 2016

**HERMES FUND MANAGERS LIMITED****CONSOLIDATED PROFIT AND LOSS ACCOUNT  
FOR THE YEAR ENDED 31 DECEMBER 2015**

	Notes	2015 £'000	2014 (restated) £'000
GROUP TURNOVER	3	105,477	90,446
Administrative expenses		(95,489)	(106,250)
GROUP OPERATING PROFIT / (LOSS)		9,988	(15,804)
Share of results of associated undertakings	4	4,495	5,085
Realised currency gain		389	1,185
Profit on disposal of investments		-	107
PROFIT / (LOSS) ON ORDINARY ACTIVITIES BEFORE INTEREST AND TAXATION		14,872	(9,427)
Interest payable and similar charges	5	(299)	(413)
Interest receivable and similar income	5	198	114
Other finance costs	5	(200)	(800)
PROFIT / (LOSS) ON ORDINARY ACTIVITIES BEFORE TAXATION	6	14,571	(10,526)
Tax on profit / (loss) on ordinary activities - Group	9	5,511	97
PROFIT / (LOSS) ON ORDINARY ACTIVITIES AFTER TAXATION		20,082	(10,429)

All of the results are derived from continuing operations.

The restatements above relate to the transition to the accounting standard FRS 102 as disclosed in note 30.

The notes to these financial statements on pages 51 to 88 are an integral part of these financial statements.

## HERMES FUND MANAGERS LIMITED

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME  
FOR THE YEAR ENDED 31 DECEMBER

	Notes	2015 £'000	2014 (restated) £'000
Profit / (loss) for the financial year		20,082	(10,429)
Other comprehensive income			
Remeasurement of net defined benefit liability	17	4,500	6,700
Deferred tax charge— attributable to net actuarial gain	9	(3,874)	(2,588)
Currency translation differences on foreign currency net investments		(489)	(935)
OTHER COMPREHENSIVE INCOME		137	3,177
TOTAL COMPREHENSIVE INCOME		20,219	(7,252)
Profit for the year attributable to:			
Non-controlling interest		400	(595)
Equity shareholders of the Company		19,682	(9,834)
		20,082	(10,429)
Total comprehensive income for the period attributable to:			
Non-controlling interest		400	(595)
Equity shareholders of the Company		19,819	(6,657)
		20,219	(7,252)

The restatements above relate to the transition to the accounting standard FRS 102 as disclosed in note 30.

The notes to these financial statements on pages 51 to 88 are an integral part of these financial statements.

## HERMES FUND MANAGERS LIMITED

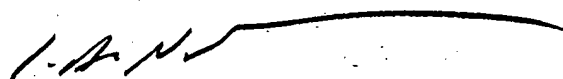
## CONSOLIDATED BALANCE SHEET AS AT 31 DECEMBER

	Notes	2015 £'000	2014 (restated) £'000
<b>FIXED ASSETS</b>			
Intangible assets – goodwill	11	1,103	1,470
Tangible assets	12	1,702	3,175
Joint ventures	13	9,557	10,480
Investments	13	5,758	3,254
		<u>18,120</u>	<u>18,379</u>
<b>CURRENT ASSETS</b>			
Debtors	14	38,198	38,494
Cash at bank and in hand	24	53,360	55,445
		<u>91,558</u>	<u>93,939</u>
<b>CURRENT LIABILITIES</b>			
Creditors - amounts falling due within one year	15	(40,343)	(44,510)
<b>NET CURRENT ASSETS</b>		<u>51,215</u>	<u>49,429</u>
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>		<u>69,335</u>	<u>67,808</u>
Creditors - amounts falling due after more than one year	15	(14,675)	(10,296)
Provisions for liabilities	16	(1,741)	(4,008)
<b>NET ASSETS EXCLUDING PENSION LIABILITIES</b>		<u>52,919</u>	<u>53,504</u>
Pension surplus / (deficit)	17	1,600	(9,700)
<b>NET ASSETS INCLUDING PENSION LIABILITIES</b>		<u>54,519</u>	<u>43,804</u>
<b>CAPITAL AND RESERVES</b>			
Called up share capital	19	52,458	58,558
Profit and loss account		1,661	(15,928)
<b>SHAREHOLDER'S FUNDS</b>		<u>54,119</u>	<u>42,630</u>
Non-controlling interest	28	400	1,174
<b>TOTAL CAPITAL EMPLOYED</b>		<u>54,519</u>	<u>43,804</u>

The restatements above relate to the transition to the accounting standard FRS 102 as disclosed in note 30.

These financial statements were approved by the Board of Directors and authorised for issue on 31 March 2016. The notes to these financial statements on pages 51 to 88 are an integral part of these financial statements.

Signed on behalf of the Board of Directors



S Nusseibeh - Director

## HERMES FUND MANAGERS LIMITED

## COMPANY BALANCE SHEET AS AT 31 DECEMBER

	Notes	2015 £'000	2014 (restated) £'000
<b>FIXED ASSETS</b>			
Tangible assets	12	1,702	3,116
Investments	13	36,665	31,040
		<u>38,367</u>	<u>34,156</u>
<b>CURRENT ASSETS</b>			
Debtors	14	37,587	29,899
Cash at bank	24	51,092	26,928
		<u>88,679</u>	<u>56,827</u>
<b>CURRENT LIABILITIES</b>			
Creditors - amounts falling due within one year	15	(64,621)	(22,539)
<b>NET CURRENT ASSETS</b>		<u>24,058</u>	<u>34,288</u>
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>		62,425	68,444
Creditors - amounts falling due after more than one year	15	(10,058)	(6,547)
Provisions for liabilities and charges	16	(1,741)	(4,008)
<b>NET ASSETS EXCLUDING PENSION LIABILITIES</b>		<u>50,626</u>	<u>57,889</u>
Pension surplus / (deficit)	17	1,600	(9,700)
<b>NET ASSETS INCLUDING PENSION LIABILITIES</b>		<u>52,226</u>	<u>48,189</u>
<b>CAPITAL AND RESERVES</b>			
Called up share capital	19	52,458	58,558
Profit and loss account		(232)	(10,369)
Revaluation reserve		-	-
<b>SHAREHOLDER'S FUNDS</b>		<u>52,226</u>	<u>48,189</u>

The restatements above relate to the transition to the accounting standard FRS 102 as disclosed in note 30.

These financial statements were approved by the Board of Directors and authorised for issue on 31 March 2016. The notes to these financial statements on pages 51 to 88 are an integral part of these financial statements.

Signed on behalf of the Board of Directors



S Nusseibeh - Director

Registered company number: 1661776

## HERMES FUND MANAGERS LIMITED

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

AS AT 31 DECEMBER 2014

Equity attributable to equity shareholders of the Group						
	Notes	Called up share capital	Profit And Loss account	Revaluation reserve	Non- Controlling Interest	Total
		£'000	£'000	£'000	£'000	£'000
At 31 December 2013 As previously stated		38,558	(8,886)	482	1,809	31,963
Changes on transition to FRS102						
Holiday pay accrual	30	-	(194)	-	-	(194)
Transfer of reserve	30	-	482	(482)	-	-
<b>At 1 January 2014 as restated</b>		<b>38,558</b>	<b>(8,598)</b>	<b>-</b>	<b>1,809</b>	<b>31,769</b>
(Loss) for the year		-	(9,834)	-	(595)	(10,429)
Remeasurement of net defined benefit liability		-	6,700	-	-	6,700
Deferred tax (loss) / gain on pension liabilities		-	(2,588)	-	-	(2,588)
Currency translation differences on foreign currency net investments		-	(935)	-	-	(935)
<b>Total comprehensive income</b>		<b>38,558</b>	<b>(15,255)</b>	<b>-</b>	<b>1,214</b>	<b>24,517</b>
Dividend paid to minority interests		-	(673)	-	-	(673)
Issue of share capital		20,000	-	-	-	20,000
Step Acquisition of subsidiary					(40)	(40)
At 31 December 2014		58,558	(15,928)	-	1,174	43,804

## HERMES FUND MANAGERS LIMITED

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

AS AT 31 DECEMBER 2015

	Called up share capital	Profit And Loss account	Revaluation reserve	Non- Controlling Interest	Total
	£'000	£'000	£'000	£'000	£'000
At 31 December 2014	58,558	(15,928)	-	1,174	43,804
Profit for the year	-	19,682	-	400	20,082
Remeasurement of net defined benefit liability	-	4,500	-	-	4,500
Deferred tax (loss) / gain on pension liabilities	-	(3,874)	-	-	(3,874)
Currency translation differences on foreign currency net investments	-	(489)	-	-	(489)
<b>Total comprehensive income</b>	<b>58,558</b>	<b>3,891</b>	<b>-</b>	<b>1,574</b>	<b>64,023</b>
Share capital reduction	(6,100)	6,100	-	-	-
Share re-purchase	-	(6,074)	-	-	(6,074)
Dividend	-	(202)	-	-	(202)
Increase in subsidiary	-	(2,054)	-	-	(2,054)
Change in minority interest accounting	-	-	-	(1,174)	(1,174)
At 31 December 2015	<b>52,458</b>	<b>1,661</b>	<b>-</b>	<b>400</b>	<b>54,519</b>

## HERMES FUND MANAGERS LIMITED

## COMPANY STATEMENT OF CHANGES IN EQUITY

AS AT 31 DECEMBER 2014

		Called up share capital	Profit And Loss Account	Revaluation reserve	Total
		£'000	£'000	£'000	£'000
At 31 December 2013 as previously stated		38,558	1,735	482	40,775
Changes on transition to FRS102	30	-	482	(482)	-
Holiday pay accrual	30	-	(57)	-	(57)
<b>As 1 January 2014 as restated</b>		<b>38,558</b>	<b>2,160</b>	<b>-</b>	<b>40,718</b>
Loss for the year		-	(16,641)	-	(16,641)
Remeasurement of net defined benefit liability		-	6,700	-	6,700
Deferred tax (loss) / gain on pension liabilities		-	(2,588)	-	(2,588)
<b>Total comprehensive income</b>		<b>38,558</b>	<b>(10,369)</b>	<b>-</b>	<b>28,189</b>
Issue of share capital		20,000	-	-	20,000
<b>At 31 December 2014</b>		<b>58,558</b>	<b>(10,369)</b>	<b>-</b>	<b>48,189</b>



## HERMES FUND MANAGERS LIMITED

## COMPANY STATEMENT OF CHANGES IN EQUITY

AS AT 31 DECEMBER 2015

	Called up share capital	Profit And Loss account	Revaluation reserve	Total
	£'000	£'000	£'000	£'000
At 31 December 2014	58,558	(10,369)	-	48,189
Profit for the year	-	9,485	-	9,485
Remeasurement of net defined benefit liability	-	4,500	-	4,500
Deferred tax (loss) / gain on pension liabilities	-	(3,874)	-	(3,874)
<b>Total comprehensive income</b>	<b>58,558</b>	<b>(258)</b>	<b>-</b>	<b>58,300</b>
Share capital reduction	(6,100)	6,100	-	-
Share re-purchase	-	(6,074)	-	(6,074)
At 31 December 2015	<b>52,458</b>	<b>(232)</b>	<b>-</b>	<b>52,226</b>

**HERMES FUND MANAGERS LIMITED****CONSOLIDATED CASH FLOW STATEMENT  
FOR THE YEAR ENDED 31 DECEMBER**

	<b>Notes</b>	<b>2015 £'000</b>	<b>2014 £'000</b>
<b>NET CASH INFLOW / (OUTFLOW) FROM OPERATING ACTIVITIES</b>	23	5,580	(6,914)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Proceeds from sale of fixed asset investments		1,785	1,330
Purchase of fixed asset investments		(6,146)	(1,347)
Interest received		133	84
Dividends received from associates/joint ventures		4,451	4,610
Purchase of growth shares		(6,074)	(40)
Corporation tax paid		(1,612)	(2,087)
Payments to acquire tangible fixed assets		-	(812)
<b>NET CASH FLOWS FROM INVESTING ACTIVITIES</b>		<b>(7,463)</b>	<b>1,738</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Issue of share capital		-	20,000
Dividends paid		(202)	(673)
<b>NET CASH INFLOW FROM FINANCING</b>		<b>(202)</b>	<b>19,327</b>
<b>NET (DECREASE) / INCREASE IN CASH AND CASH EQUIVALENTS</b>	24	<b>(2,085)</b>	<b>14,151</b>

**HERMES FUND MANAGERS LIMITED****COMPANY CASH FLOW STATEMENT  
FOR THE YEAR ENDED 31 DECEMBER**

	<b>Notes</b>	<b>2015 £'000</b>	<b>2014 £'000</b>
<b>NET CASH INFLOW / (OUTFLOW) FROM OPERATING ACTIVITIES</b>	<b>23</b>	<b>18,190</b>	<b>(11,361)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Proceeds from sale of fixed asset investments		1,743	1,330
Purchase of fixed asset investments		(4,224)	(1,347)
Interest received		113	33
Dividends received from subsidiaries		14,750	12,091
Purchase of growth shares		(6,074)	-
Investment in subsidiaries		(334)	-
Payments to acquire tangible fixed assets		-	(812)
<b>NET CASH FLOWS FROM INVESTING ACTIVITIES</b>		<b>5,974</b>	<b>11,295</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Issue of share capital		-	20,000
<b>NET CASH INFLOW FROM FINANCING</b>		<b>-</b>	<b>20,000</b>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>24</b>	<b>24,164</b>	<b>19,934</b>

**HERMES FUND MANAGERS LIMITED****NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015****1. ACCOUNTING POLICIES**

The financial statements are prepared in accordance with applicable United Kingdom law and Accounting Standards. The principal accounting policies are summarised below. They have all been applied consistently throughout the year and the preceding year.

**a) General information and basis of accounting**

The financial statements are prepared under the historical cost convention and on the going concern basis as described in the Directors' Report.

Hermes Fund Managers Limited is a company incorporated in the United Kingdom under the Companies Act. The address of the registered office is given on page 33. The nature of the group's operations and its principal activities are set out in the strategic report on pages 5 to 25.

The financial statements have been prepared under the historical cost convention, modified to include certain items at fair value, and in accordance with Financial Reporting Standard 102 (FRS 102) issued by the Financial Reporting Council.

The prior year financial statements were restated for material adjustments on adoption of FRS 102 in the current year. For more information see note 30.

The functional currency of the Company is considered to be pounds sterling because that is the currency of the primary economic environment in which the Company operates. The consolidated financial statements are also presented in pounds sterling. Foreign operations are included in accordance with the policies set out below.

**b) Basis of consolidation**

The Group financial statements consolidate the financial statements of the Company and its subsidiary undertakings drawn up to 31 December each year. Acquisitions are accounted for under the acquisition method. The results of subsidiaries acquired or sold are consolidated for the period from or to the date on which control passed.

The Group has taken exemption from preparing a Company-only profit and loss account in line with Companies Act 2006.

Business combinations are accounted for under the purchase method. Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used into line with those used by the Group. All intra-group transactions, balances, income and expenses are eliminated on consolidation. In accordance with Section 35 of FRS 102, Section 19 of FRS 102 has not been applied in these financial statements in respect of business combinations effected prior to the date of transition.

## HERMES FUND MANAGERS LIMITED

### NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

#### 1. ACCOUNTING POLICIES (continued)

##### c) Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the strategic report. The directors' report further describes the financial position of the Group; its cash flows, liquidity position and borrowing facilities; the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposure to credit risk and liquidity risk.

The directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

##### d) Turnover

Turnover is recognised on an accruals basis. To the extent that fees and commissions are recognised in advance of billing they are included as accrued income or expense. Turnover for investment management services includes performance fees based upon rolling performance periods of up to three years. These are recognised in the year the performance period ends.

Turnover is stated net of tax and is recognised when the significant risks and rewards are considered to have been transferred to the buyer. Turnover from the supply of services represents the value of services provided under contracts to the extent that there is a right to consideration and is recorded at the fair value of the consideration received or receivable. Where payments are received from customers in advance of services provided, the amounts are recorded as deferred income and included as part of creditors due within one year.

##### e) Goodwill

Goodwill represents any excess of the fair value of the consideration given over the fair value of the identifiable assets and liabilities acquired. Goodwill arising in respect of acquisitions is capitalised in the year in which it arises within intangible fixed assets and amortised over its useful life full year's charge for amortisation in the year of acquisition. The directors consider this to be a reasonable period over which to amortise goodwill. Provision is made for any permanent diminution in the value of goodwill.

In accordance with Section 35 of FRS 102, Section 19 of FRS 102 has not been applied in these financial statements in respect of business combinations effected prior to the date of transition.

## HERMES FUND MANAGERS LIMITED

### NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

#### 1. ACCOUNTING POLICIES (continued)

##### f) Financial instruments

Financial assets and financial liabilities are recognised when the Group becomes a party to the contractual provisions of the instrument. Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

All financial assets and liabilities are initially measured at transaction price (including transaction costs), except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value (which is normally the transaction price excluding transaction costs), unless the arrangement constitutes a financing transaction. If an arrangement constitutes a financing transaction, the financial asset or financial liability is measured at the present value of the future payments discounted at a market rate of interest for a similar debt instrument.

Financial assets and liabilities are only offset in the statement of financial position when, and only when there exists a legally enforceable right to set off the recognised amounts and the Group intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Debt instruments which meet the following conditions are subsequently measured at amortised cost using the effective interest method:

- The contractual return to the holder is (i) a fixed amount; (ii) a positive fixed rate or a positive variable rate; or (iii) a combination of a positive or a negative fixed rate and a positive variable rate.
- The contract may provide for repayments of the principal or the return to the holder (but not both) to be linked to a single relevant observable index of general price inflation of the currency in which the debt instrument is denominated, provided such links are not leveraged.
- The contract may provide for a determinable variation of the return to the holder during the life of the instrument, provided that (i) the new rate satisfies condition (a) and the variation is not contingent on future events other than (1) a change of a contractual variable rate; (2) to protect the holder against credit deterioration of the issuer; (3) changes in levies applied by a central bank or arising from changes in relevant taxation or law; or (ii) the new rate is a market rate of interest and satisfies condition (a).
- There is no contractual provision that could, by its terms, result in the holder losing the principal amount or any interest attributable to the current period or prior periods.
- Contractual provisions that permit the issuer to prepay a debt instrument or permit the holder to put it back to the issuer before maturity are not contingent on future events, other than to protect the holder against the credit deterioration of the issuer or a change in control of the issuer, or to protect the holder or issuer against changes in levies applied by a central bank or arising from changes in relevant taxation or law.

## HERMES FUND MANAGERS LIMITED

### NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

#### 1. ACCOUNTING POLICIES (continued)

##### (f) Financial instruments (continued)

Contractual provisions may permit the extension of the term of the debt instrument, provided that the return to the holder and any other contractual provisions applicable during the extended term satisfy the conditions of paragraphs (a) to (c).

Debt instruments that are classified as payable or receivable within one year on initial recognition and which meet the above conditions are measured at the undiscounted amount of the cash or other consideration expected to be paid or received, net of impairment.

With the exception of some hedging instruments, other debt instruments not meeting these conditions are measured at fair value through profit or loss.

Commitments to make and receive loans which meet the conditions mentioned above are measured at cost (which may be nil) less impairment.

Financial assets are derecognised when and only when (a) the contractual rights to the cash flows from the financial asset expire or are settled, (b) the Group transfers to another party substantially all of the risks and rewards of ownership of the financial asset, or (c) the Group, despite having retained some, but not all, significant risks and rewards of ownership, has transferred control of the asset to another party.

Financial liabilities are derecognised only when the obligation specified in the contract is discharged, cancelled or expires.

##### g) Investments

Investments in non-convertible preference shares and non-puttable, ordinary or preference shares (where shares are publicly traded or their fair value is reliably measurable) are measured at fair value through profit or loss. Where fair value cannot be measured reliably, investments are measured at cost less impairment.

In the Company balance sheet, investments in subsidiaries and associates are measured at cost less impairment.

Equity instruments issued by the Company are recorded at the fair value of cash or other resources received or receivable, net of direct issue costs. The Group uses derivative financial instruments to reduce exposure to foreign exchange risk. The Group does not hold or issue derivative financial instruments for speculative purposes.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each reporting date. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in profit or loss depends on the nature of the hedge relationship.

## HERMES FUND MANAGERS LIMITED

### NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

#### 1. ACCOUNTING POLICIES (continued)

##### g) Investments (continued)

###### Fair value measurement

The best evidence of fair value is a quoted price for an identical asset in an active market. When quoted prices are unavailable, the price of a recent transaction for an identical asset provides evidence of fair value as long as there has not been a significant change in economic circumstances or a significant lapse of time since the transaction took place. If the market is not active and recent transactions of an identical asset on their own are not a good estimate of fair value, the fair value is estimated by using a valuation technique.

##### h) Joint Ventures

In the Group financial statements investments in joint ventures are accounted for using the equity method. The consolidated profit and loss account includes the Group's share of joint venture profits, less losses, clearly indicated while the Group's investment in joint ventures is shown separately in the consolidated balance sheet. Goodwill arising on the acquisition of joint ventures is accounted for in accordance with the policy for associates above. Any unamortised balance of goodwill is included in the carrying value of the investment in joint ventures.

In the company financial statements investments in associates are accounted for at cost less impairment.

##### i) Impairment

Assets, other than those measured at fair value, are assessed for indicators of impairment at each balance sheet date. If there is objective evidence of impairment, an impairment loss is recognised in profit or loss as described below.

###### Non-financial assets

An asset is impaired where there is objective evidence that, as a result of one or more events that occurred after initial recognition, the estimated recoverable value of the asset has been reduced. The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use.

The recoverable amount of goodwill is derived from measurement of the present value of the future cash flows of the cash-generating units ("CGU") of which the goodwill is a part. Any impairment loss in respect of a CGU is allocated first to the goodwill attached to that CGU, and then to other assets within that CGU on a pro-rata basis.

Where indicators exist for a decrease in impairment loss, the prior impairment loss is tested to determine reversal. An impairment loss is reversed on an individual impaired asset to the extent that the revised recoverable value does not lead to a revised carrying amount higher than the carrying value had no impairment been recognised. Where a reversal of impairment occurs in respect of a CGU, the reversal is applied first to the assets (other than goodwill) of the CGU on a pro-rata basis and then to any goodwill allocated to that CGU.



## HERMES FUND MANAGERS LIMITED

### NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

#### 1. ACCOUNTING POLICIES (continued)

##### i) Impairment (continued)

###### Financial assets

For financial assets carried at amortised cost, the amount of an impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

For financial assets carried at cost less impairment, the impairment loss is the difference between the asset's carrying amount and the best estimate of the amount that would be received for the asset if it were to be sold at the reporting date.

Where indicators exist for a decrease in impairment loss, and the decrease can be related objectively to an event occurring after the impairment was recognised, the prior impairment loss is tested to determine reversal. An impairment loss is reversed on an individual impaired financial asset to the extent that the revised recoverable value does not lead to a revised carrying amount higher than the carrying value had no impairment been recognised.

##### j) Foreign exchange

Transactions denominated in foreign currencies are translated into the functional currency at the rates ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are retranslated at the rates ruling at that date. These translation differences are dealt with in the profit and loss account.

The results of overseas operations are translated at the average rates of exchange during the period and their balance sheets at the rates ruling at the balance sheet date. Exchange differences arising on translation of the opening net assets and results of overseas operations are reported in other comprehensive income and accumulated in equity (attributed to non-controlling interests as appropriate).

In the case of the consolidated financial statements, exchange differences on monetary items receivable from or payable to a foreign operation for which settlement is neither planned nor likely to occur (therefore forming part of the net investment in the foreign operation), which are recognised in other comprehensive income and reported under equity. Foreign subsidiaries are retranslated using the net investment method.

##### k) Tangible fixed assets

Tangible fixed assets are stated at cost or valuation, net of depreciation and any provision for impairment. Depreciation is provided on cost in equal annual instalments over the estimated useful economic lives of the assets. The estimated useful economic lives are as follows:

Fixtures, fittings and equipment	- One to five years
Leasehold improvements	- Period of the lease

All tangible assets are depreciated from the point of acquisition to the point of disposal.

## HERMES FUND MANAGERS LIMITED

### NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

#### 1. ACCOUNTING POLICIES (continued)

##### l) Operating leases

Rental expenses in respect of operating leases are charged to the profit and loss account on a straight line basis over the period of the lease. Rental income in respect of operating leases is recognised in the profit and loss account on a straight line basis over the period of the lease.

##### m) Pension benefits

For the Group's defined benefit scheme the amounts charged to operating profit are the current service costs and gains and losses on settlements and curtailments. They are included as part of staff costs. Past service costs are recognised immediately in the profit and loss account. The net interest cost on the net defined benefit liability is shown within finance costs. Remeasurement comprising actuarial gains and losses, and the return on scheme assets (excluding interest) are recognised immediately in other comprehensive income.

The Group's defined benefit scheme is funded, with the assets of the scheme held separately from those of the Group, in separate trustee administered funds. Pension scheme assets are measured at fair value and liabilities are measured on an actuarial basis using the projected unit credit method. The actuarial valuations are obtained at least triennially and are updated at each balance sheet date.

For defined contribution schemes, the amount charged to the profit and loss account in respect of pension costs is the contribution payable in the year. Differences between contributions payable in the year and contributions actually paid are shown either as accruals or prepayments in the balance sheet.

##### n) Investment income

Income from investments is accounted for on an accruals basis.

##### o) Current taxation

Current tax, including UK corporation tax and foreign tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Income tax is recognised in the profit and loss account for the period, except to the extent that it is attributable to a gain or loss that is recognised directly in equity. In such cases the gain or loss shown in equity is stated separately from the attributable income tax, which is also recognised directly in equity.

## HERMES FUND MANAGERS LIMITED

### NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

#### 1. ACCOUNTING POLICIES (continued)

##### p) Deferred taxation

Deferred taxation is provided in full on timing differences that result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax at a future date, at rates expected to apply when they crystallise based on current tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in financial statements. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax balances are not discounted.

Unrelieved tax losses and other deferred tax assets are recognised only to the extent that, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax liabilities are recognised for timing differences arising from investments in subsidiaries and associates, except where the Group is able to control the reversal of the timing difference and it is probable that it will not reverse in the foreseeable future. Deferred tax is measured using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date that are expected to apply to the reversal of the timing difference.

Where items recognised in other comprehensive income or equity are chargeable to or deductible for tax purposes, the resulting current or deferred tax expense or income is presented in the same component of comprehensive income or equity as the transaction or other event that resulted in the tax expense or income.

Current tax assets and liabilities are offset only when there is a legally enforceable right to set off the amounts and the Group intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Deferred tax assets and liabilities are offset only if: (a) the Group has a legally enforceable right to set off current tax assets against current tax liabilities; and (b) the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

##### q) Bonus costs

Provision is made for bonuses attributable to performance prior to the year end. Deferred bonuses subject to co-invest arrangements are accrued evenly over the period to vesting.

## HERMES FUND MANAGERS LIMITED

### NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

#### 1. ACCOUNTING POLICIES (continued)

##### r) Long-term incentive plan ("LTIP")

LTIP units awarded in the year entitle the holder to a share of pre-tax profits over a four year vesting period. The expected costs of the LTIP payment are spread over the period of vesting and recognised as a long term liability.

##### s) Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, it is probable that the Group will be required to settle that obligation and a reliable estimate can be made of the amount of the obligation.

Restructuring provisions are recognised when the Group has developed a detailed formal plan for the restructuring and has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement the plan or announcing its main features to those affected by it. The measurement of restructuring provisions includes only the direct expenditures arising from the restructuring, which are those amounts that are both necessarily entailed by the restructuring and not associated with ongoing activities of the entity.

Onerous contracts – Present obligations arising under such contracts are recognised and measured as provisions. An onerous contract is considered to exist where the Group has a contract under which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

#### 2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The reported results of the group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. UK company law require the directors, in preparing the group's financial statements, to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent. The group's estimates and assumptions are based on historical experience and expectation of future events and are reviewed periodically. The actual outcome may be materially different from that anticipated. The judgements and assumptions involved in the group's accounting policies that are considered by the board to be the most important to the portrayal of its financial condition are as follows:

##### (a) Fee and Commission income

Fee and commission income is recognised depending on the nature of service provided:

- Income earned from provision of services is recognised as the services are provided; and
- Income earned on the execution of a significant act is recognised when the act is completed.

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

## (b) Goodwill impairment

The directors review goodwill for impairment at least annually or when events or changes in economic circumstances indicate that impairment may have taken place. The recoverable amounts of relevant CGUs are based on value in use calculations using management's best estimate of future cash flows and performance, discounted at a rate which the directors estimate to be the return appropriate to the business.

## 3. TURNOVER

Turnover comprises the value of services provided in the United Kingdom and the United States of America by the Group exclusive of VAT and is analysed as follows:

	United Kingdom		United States		Group	
	2015	2014	2015	2014	2015	2014
	£'000	£'000	£'000	£'000	£'000	£'000
Investment management services	102,414	87,185	-	1,817	102,414	89,002
Other fee income	3,063	1,444	-	-	3,063	1,444
<b>TOTAL GROUP TURNOVER</b>	<b>105,477</b>	<b>88,629</b>	<b>-</b>	<b>1,817</b>	<b>105,477</b>	<b>90,446</b>

Turnover for investment management services includes performance fees based upon rolling performance periods of up to three years. These are recognised in the year the performance period ends.

## 4. JOINT VENTURES

Share of results of associated undertaking:

	2015	2014
	£'000	£'000
Joint ventures:		
Hermes GPE LLP	4,495	5,085
	<u>4,495</u>	<u>5,085</u>

Note 25 discloses additional information on principal subsidiaries and joint ventures.

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 5. FINANCE COSTS (NET)

	2015 £'000	2014 £'000
Interest payable and similar charges	299	413
Less: Investment income	(198)	(114)
Other finance costs	200	800
	<u>301</u>	<u>1,099</u>
	2015 £'000	2014 £'000
Interest payable and similar charges in respect of:		
Financing charge on contract to re-purchase HSL shares (see below)	49	163
Loan from ultimate parent	250	250
	<u>299</u>	<u>413</u>
Investment income		
Gain on fixed asset investments (see note 13):		
Other investments	65	30
Interest receivable and similar income in respect of:		
Bank deposit balances	133	84
	<u>198</u>	<u>114</u>

The financing charge on contract to re-purchase HSL shares related to the unwind of the discount and adjustments applied to the valuation of the obligation to purchase own shares in Hermes Sourcecap Limited ("HSL"). This share repurchase agreement was cancelled and in its place, on 24 December 2013 HFML agreed to acquire a further 999 ordinary shares in HSL, payable to a minority shareholder, for consideration totalling £780,036 plus contingent consideration linked to the annualised revenue of HSL. The amount in the current year reflects adjustments to the contingent consideration which was paid during the year. The consideration has now been paid in full. Interest payable to the ultimate parent relates to a loan from BTPS, as shown in Note 15.

	2015 £'000	2014 £'000
<b>Other finance costs / (income)</b>		
Net interest expense on defined benefit liability	5,400	6,100
Net interest income on defined benefit assets	(5,200)	(5,300)
	<u>200</u>	<u>800</u>

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 6. PROFIT / LOSS ON ORDINARY ACTIVITIES BEFORE TAXATION

	2015 £'000	2014 £'000
The profit / loss on ordinary activities before taxation is stated after charging / (crediting):		
Depreciation on tangible fixed assets (note 12)	1,473	1,631
Amortisation of goodwill (note 11)	1,335	1,335
Loss on disposal of fixed assets	-	2,047
Foreign exchange gain	(389)	(1,185)
Profit on fair value movement of investments (note 13)	(65)	(30)
Rental charges under operating leases	1,868	1,964
Rental income from operating leases	(302)	(118)
Auditor's remuneration:		
Audit fees - Subsidiaries	132	138
- Company	81	79
	213	217
Non-audit fees:		
Other services	108	103
Total fees payable to Group auditor	321	320

Amortisation of intangible assets is included in administrative expenses.

Fees payable to the Company's auditor and its associates in respect of associated pension schemes during the year were £18,505 (2014: £17,250). These fees were charged to and paid directly by the pension scheme.

## 7. STAFF NUMBERS AND COSTS

Average number of persons employed by the Group and Company in the year:	2015 No.	2014 No.
Investment management	138	163
Administration	211	220
	349	383
Staff costs during the year in respect of these directors and employees were:	2015 £'000	2014 £'000
Wages and salaries	55,333	55,441
Social security costs	6,655	6,629
Pension cost related to Group scheme	4,326	4,375
	66,314	66,445

**HERMES FUND MANAGERS LIMITED****NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015**  
**(continued)****8. DIRECTORS' REMUNERATION AND TRANSACTIONS**

Directors' remuneration	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Emoluments	4,044	5,550
Amounts receivable under long term incentive schemes	559	-
Company contributions to money purchase pension schemes	66	64
	<u>4,669</u>	<u>5,614</u>

The Group operates co-investment/bonus deferral schemes whereby a portion of bonuses awarded in respect of the year are deferred. The full value of deferred awards granted to executive directors in respect of the year is £1,005,000 (2014: £2,562,500), although they will only become payable after the directors satisfy future service conditions. Deferred awards are included in total remuneration disclosed above.

The number of directors who:	<b>2015</b>	<b>2014</b>
	<b>No</b>	<b>No</b>
Are members of a money purchase pension scheme	3	3
Exercised options over shares in company	2	-
Had awards receivable in the form of shares under a long term incentive scheme	3	-

Remuneration of the highest paid director:	<b>2015</b>	<b>2014</b>
	<b>£'000</b>	<b>£'000</b>
Emoluments	1,915	3,635
Company contributions to money purchase schemes	20	20
Amounts receivable under (other than shares and share options) under long-term incentive schemes	282	-
	<u>2,217</u>	<u>3,655</u>

Of this amount £535,000 (2014: £2,272,500) is deferred over a period of up to three years.

Details of transactions with directors and key management personnel during the year are disclosed in note 27.



## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 9. TAX ON PROFIT / (LOSS) ON ORDINARY ACTIVITIES

a)	Analysis of tax charge/(credit) for the year	2015 £'000	2014 £'000
	Profit and loss account:		
	<i>Current tax:</i>		
	UK corporation tax at 20.25% (2014: 21.49%)	1,098	2,035
	Overseas tax	3	107
	Share of tax charge in joint ventures and associates	9	-
	Adjustment in respect of prior periods	(2,410)	(3)
	Total current tax charge	(1,300)	2,139
	<i>Deferred tax:</i>		
	Timing differences, origination and reversal	(2,325)	(1,233)
	Adjustment in respect of prior periods	(2,535)	(1,004)
	Effect of tax rate change on opening balances	649	-
	Total deferred tax credit	(4,211)	(2,236)
	Tax charge on profit on ordinary activities	(5,511)	(97)
	Statement of total recognised gains and losses:		
	<i>Deferred tax:</i>		
	Timing differences, origination and reversal	3,874	2,588
	Total tax on items in statement of total recognised gains and losses	3,874	2,588

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 9. TAX ON LOSS ON ORDINARY ACTIVITIES (continued)

## b) Reconciliation of current tax charge

The tax charged in the year differs from that resulting from applying the average rate of corporation tax in the UK of 20.25% (2014: 21.49%). The differences are explained below:

	2015 £'000	2014 £'000
Profit / (Loss) on ordinary activities multiplied by the average rate of corporation tax in the UK of 20.25% (2014: 21.49%)	2,950	(2,262)
<i>Effects of:</i>		
Non-taxable income	(728)	(984)
Non-deductible expenses	391	807
Amounts transferred to the Consolidated Statement of Total Recognised Gains and Losses	(2,954)	639
Foreign tax charge	1	42
Chargeable gains	449	269
Adjustments in respect of prior periods	(4,945)	(1,007)
Effect of differences to deferred tax rates	1,564	99
Deferred tax (recognised) / not recognised	(2,339)	2,303
Effect of overseas tax rate differences	9	(3)
Group relief not paid for	91	-
Current tax charge for the period	<u>(5,511)</u>	<u>(97)</u>

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 9. TAX ON LOSS ON ORDINARY ACTIVITIES (continued)

## c) Deferred tax position

	2015 Provided £'000	2015 Unprovided £'000	2014 Provided £'000	2014 Unprovided £'000
<b>The Group</b>				
Deferred tax asset / (liability):				
Fixed asset timing difference	(2,271)	(3)	(22)	(3,790)
Tax losses	-	(10,047)	(23)	(12,913)
Short-term timing differences	(2,047)	(21)	(1,137)	(628)
	<u>4,318</u>	<u>(10,071)</u>	<u>(1,182)</u>	<u>17,331</u>

**The Company**

Deferred tax asset / (liability):				
Fixed asset timing differences	(2,256)	-	-	(3,785)
Tax losses	-	(7,004)	-	(12,820)
Short-term timing differences	(876)	-	-	(598)
	<u>(3,132)</u>	<u>(7,004)</u>	<u>-</u>	<u>(17,203)</u>

Deferred tax assets totalling £10,070,939 (2014: £17,286,000) have not been recognised in respect of losses, accelerated capital allowances and short-term timing differences as the Group is not sufficiently certain that it will be able to recover those assets within a relatively short period of time.

## 10. PROFIT OF THE PARENT COMPANY

As permitted by Section 408 of the Companies Act 2006, no separate profit and loss account or statement of comprehensive income is presented as part of these financial statements. The parent company's loss after tax for the year amounted to £9,485,257 (2014: loss of £16,641,101).

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 11. INTANGIBLE FIXED ASSETS

	<b>Goodwill £'000</b>
<b>The Group</b>	
Cost:	
At 1 January 2015 and 31 December 2015	<u>11,936</u>
Accumulated amortisation:	
At 1 January 2015	(10,466)
Amortisation	<u>(367)</u>
At 31 December 2015	<u>(10,833)</u>
Net book value:	
At 31 December 2015	<u>1,103</u>
At 31 December 2014	<u>1,470</u>

The remaining unamortised goodwill above relates to Hermes Sourcecap Limited.

Unamortised goodwill of £4,837,022 (2014: £5,804,426) arising on the part-acquisition of Hermes GPE LLP in 2011 is included in the carrying value of the investment in joint ventures in accordance with the policy set out in the Accounting Policies. A total of £967,000 (2014: £967,000) was amortised during the year relating to the Hermes GPE LLP joint venture, in addition to the amortisation charge above.

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 12. TANGIBLE FIXED ASSETS

<b>The Group</b>	<b>Leasehold Improvements £'000</b>	<b>Fixtures, Fittings and Equipment £'000</b>	<b>Total £'000</b>
Cost:			
At 1 January 2015 and 31 December 2015	5,915	11,507	17,422
Accumulated depreciation:			
At 1 January 2015	4,875	9,372	14,247
Charge for the year	264	1,209	1,473
At 31 December 2015	5,139	10,581	15,720
Net book value:			
At 31 December 2015	776	926	1,702
At 31 December 2014	1,040	2,135	3,175
<b>The Company</b>	<b>Leasehold Improvements £'000</b>	<b>Fixtures, Fittings and Equipment £'000</b>	<b>Total £'000</b>
Cost:			
At 1 January 2015 and 31 December 2015	5,915	11,263	17,178
Accumulated depreciation:			
At 1 January 2015	4,875	9,187	14,062
Charge for the year	264	1,150	1,414
At 31 December 2015	5,139	10,337	15,476
Net book value:			
At 31 December 2015	776	926	1,702
At 31 December 2014	1,040	2,076	3,116

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 13. INVESTMENTS HELD AS FIXED ASSETS

	Investment in Joint Ventures £'000	Unlisted Investments £'000	Total £'000
<b>The Group</b>			
At 1 January 2015	10,480	3,254	13,734
Share of retained profit	4,495	-	4,495
Additions	-	4,224	4,224
Taxation	-	-	-
Movement in fair value	-	65	65
Goodwill amortisation	(967)	-	(967)
Disposals	-	(1,785)	(1,785)
Dividends received from joint ventures	(4,451)	-	(4,451)
At 31 December 2015	<u>9,557</u>	<u>5,758</u>	<u>15,315</u>

Included within unlisted investments are investments held for the purposes of hedging liabilities on co-invest bonus arrangements which are classified as financial assets. During the year, there were additions and disposals of £4,224,522 and £1,785,241 respectively. These investments are measured at fair value. A fair value gain of £64,839 was recognised in the profit and loss during the year (2014: £29,833).

Investments in joint ventures comprise the following share of net assets:

	2015 £'000	2014 £'000
Hermes GPE LLP	<u>9,557</u>	<u>10,480</u>
TOTAL	<u>9,557</u>	<u>10,480</u>

The Group had no interests in associate undertakings at the balance sheet date.

The companies which make up the Group are analysed in note 25.

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 13. INVESTMENTS HELD AS FIXED ASSETS (continued)

	Investment in Subsidiaries £'000	Investment In Joint Ventures £'000	Unlisted Investment £'000	Total £'000
<b>The Company</b>				
Cost:				
At 1 January 2015	15,515	12,674	3,207	31,396
Additions	3,229	-	4,225	7,454
Movement in fair value	-	-	65	65
Disposal	(151)	-	(1,743)	(1,894)
At 31 December 2015	18,593	12,674	5,754	37,021
Provision for impairment:				
At 1 January 2015	356	-	-	356
Movement in provision	-	-	-	-
At 31 December 2015	356	-	-	356
Net book value:				
At 31 December 2015	18,237	12,674	5,754	36,665
At 31 December 2014	15,159	12,674	3,207	31,040

The Company recognises a provision for impairment against the investment in Hermes Investments (North America) Limited, due to the uncertain timing as to when the Company will earn a return from this investment.

The Company also recognises a provision for impairment of £250,000 against the investment in Hermes Equity Ownership Services Limited, due to its current and prior year losses and net liability position (2014: £250,000).

During the year the Company acquired an additional 18% in Hermes Sourcecap Limited, an existing majority-owned subsidiary for £3,230,514.

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 14. DEBTORS

	2015 Group £'000	2015 Company £'000	2014 Group £'000	2014 Company £'000
Due within one year:				
Owed by subsidiaries	-	17,476	-	20,706
Owed by joint ventures	11	11	32	31
Owed by parent	13,928	135	11,534	69
Trade debtors	5,180	107	1,748	24
Taxation	5,684	15,744	3,947	5,419
Other debtors	1,161	1,151	1,247	1,242
Prepaid and accrued income	12,234	2,963	19,912	2,408
	<u>38,198</u>	<u>37,587</u>	<u>38,420</u>	<u>29,899</u>
Due after one year:				
Other debtors	-	-	74	-
	<u>38,198</u>	<u>37,587</u>	<u>38,494</u>	<u>29,899</u>

## 15. CREDITORS

	2015 Group £'000	2015 Company £'000	2014 Group £'000	2014 Company £'000
Amounts falling due within one year:				
Owed to parent	994	-	4,041	-
Owed to Subsidiaries	-	44,608	-	-
Other creditors	1,249	1,206	1,543	1,518
Taxation	-	-	1,552	-
Deferred taxes	-	-	-	-
Accruals and deferred income	38,100	18,807	37,374	21,021
	<u>40,343</u>	<u>64,621</u>	<u>44,510</u>	<u>22,539</u>
Amounts falling due after more than one year:				
Owed to parent	5,572	5,572	5,322	5,322
Other creditors	9,103	4,486	4,974	1,225
	<u>14,675</u>	<u>10,058</u>	<u>10,296</u>	<u>6,547</u>

The amount owed to parent relates to a subordinated loan with an original term of five years. The loan accrues interest at 5% per annum and expires in September 2018.



## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 16. PROVISIONS FOR LIABILITIES AND CHARGES

	Onerous lease provision	Restructuring Provision	Total
	2015 £'000	2015 £'000	2015 £'000
<b>The Group and Company</b>			
At 1 January	1,478	2,530	4,008
Charged to the profit and loss			
Release unused			
Utilisation of provision	(422)	(2,480)	(2,902)
Charge for the year	135	500	635
At 31 December	1,191	550	1,741

The provision above relates to an onerous lease provision arising from vacant space on a portion of the office property. This cost includes rent, service charges and business rates apportioned to the vacant area. The principal assumptions include an aggregation of future costs discounted using a pre-tax risk-free rate based on a government bond rate of similar duration.

The restructuring provision relates to obligations arising from the strategic decision to restructure the business in 2014 including the closure of the commodities, fund of hedge fund businesses and other initiatives. The majority of the restructuring was completed in 2015.

## 17. PENSION COMMITMENTS

The Group operates a defined benefit scheme, Hermes Group Pension Scheme (the "Scheme"), funded by the payment of contributions to a separately administered trust fund. The scheme was closed to new members on 1 July 2008. The Group closed its final salary pension scheme to future accrual with effect from 31 October 2011. Thereafter, the Company made contributions to a defined contribution scheme for all employees.

Defined Contribution Scheme

Contributions to the defined contribution scheme amounted to £3,626,243 during the year (2014: £3,774,574). The contributions outstanding as at the year-end amounted to £390,733 (2014: £427,032).

Defined Benefit Pension Scheme

Contributions to the Scheme are determined with the advice of independent qualified actuaries on the basis of triennial valuations using the Projected Unit method.

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 17. PENSION COMMITMENTS (continued)

**Mortality assumptions:**

Investigations have been carried out within the past three years into the mortality experience of the Group's defined benefit schemes. These investigations concluded that the current mortality assumptions include sufficient allowance for future improvements in mortality rates. The assumed life expectations on retirement at 65 are:

	<b>2015 years</b>	<b>2014 years</b>
Retiring today	27.5	27.3
Retiring in 20 years	29.2	29.1

The actuarial valuation was updated at 31 December 2015 by a qualified actuary using assumptions that are consistent with the requirements of FRS 102. Investments have been valued, for this purpose, at fair value. Contributions of £8.3m were made during the year into the scheme (2014: £8.4m).

The amount included in the balance sheet arising from the Group's obligations in respect of its defined benefit retirement benefit scheme is as follows:

	<b>2015 £m</b>	<b>2014 £m</b>
Present value of funded Scheme obligation	(144.0)	(148.5)
Fair value of Scheme assets	145.6	138.8
Surplus / (Deficit)	1.6	(9.7)

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 17. PENSION COMMITMENTS (continued)

The amounts recognised in the profit and loss account are as follows:

	2015 £m	2014 £m
Administration costs	0.7	0.9
Interest on Scheme obligation (included in Other finance costs)	5.4	6.1
Past service cost	0.6	0.8
Expected return on Scheme assets (included in Other finance income)	(5.2)	(5.3)
Total	1.5	2.5

'Interest on Scheme obligation' and 'Expected return on Scheme assets' are disclosed net as £0.2m 'Other finance costs' in the Consolidated Profit and Loss Account (2014: £0.8m).

Analysis of the actuarial gain recognised in the consolidated statement of comprehensive income:

	2015 £m	2014 £m
Actual return less expected return on Scheme assets, i.e. (loss) / gain	(0.4)	10.5
Experience gains and losses arising on Scheme liabilities, i.e. (loss)	(1.5)	(0.1)
Changes in assumptions underlying the present value of Scheme liabilities, i.e. gain / (loss)	6.4	(3.7)
Actuarial gain	4.5	6.7

Changes in the present value of the Defined Benefit obligation are as follows:

	2015 £m	2014 £m
Opening Defined Benefit obligation	148.5	140.7
Past service cost	0.6	0.8
Interest cost	5.4	6.1
Benefits paid	(5.6)	(2.9)
Experience (gain) / loss on defined benefit obligation	1.5	0.1
Changes to assumptions	(6.4)	3.7
Closing Defined Benefit obligation	144.0	148.5

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 17. PENSION COMMITMENTS (continued)

Changes in the fair value of the assets over the period are as follows:

	2015 £m	2014 £m
Opening fair value of assets	138.8	118.4
Interest on assets	5.2	5.3
Company contribution	8.3	8.4
Benefits paid	(5.6)	(2.9)
Administrative costs	(0.7)	(0.9)
Return on assets less interest	(0.4)	10.5
Closing fair value of assets	145.6	138.8

The major categories of plan assets as a percentage of the fair value of total plan assets are as follows:

	2015 %	2014 %
Equities	32	51
Bonds / Gilts	31	17
Real estate / Other	37	32

Principal actuarial assumptions at the balance sheet date:

	2015 %	2014 %
Discount rate at 31 December	4.0	3.7
Future pensionable salary increases	2.0	1.9
Future increases to pensions in payment (HGPS members)	3.0	2.9
Future increases to pensions in payment (HPS members)	2.0	1.9

Pension increases in deferment are linked to Consumer Price Inflation (CPI) for both Hermes Pension Scheme (HPS) and Hermes Group Pension Scheme (HGPS) members. Pension increases in payment for HPS members are in line with CPI and pension increases in payment for HGPS members are in line with Retail Price Inflation (RPI).

On 17 May 1999 all assets and liabilities of the HPS were transferred to the HGPS. The rate of return has been determined on an asset class basis reflecting factors including equity market movements, future expectations, bond yields and inflation.

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 17. PENSION COMMITMENTS (continued)

Amounts for the current and previous four periods are as follows:

	2015 £m	2014 £m	2013 £m	2012 £m	2011 £m
Present value of Scheme obligation	(144.0)	(148.5)	(140.7)	(118.4)	(107.7)
Fair value of Scheme assets	145.6	138.8	118.4	109.8	92.0
Surplus / (Deficit)	1.6	(9.7)	(22.3)	(8.6)	(15.7)
Experience adjustments on Scheme assets – gain / (loss)	(0.4)	10.5	3.4	1.7	(7.0)
Experience adjustments on Scheme liabilities – loss / gain	(1.5)	(0.1)	0.2	0.1	(0.1)

## 18. FINANCIAL INSTRUMENTS

	2015 £m	2014 £m
Financial assets		
Measured at fair value through profit or loss		
Fixed asset unlisted investments (see note 13)	5,566	2,787
Measured at undiscounted amount receivable		
Trade and other debtors	38,198	38,494
Equity instruments measured at cost less impairment	-	-
Fixed asset investments in unlisted equity instruments	192	467
	<u>43,956</u>	<u>41,748</u>

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 18. FINANCIAL INSTRUMENTS (continued)

	2015 £'000	2014 £'000
<b>Financial liabilities</b>		
Measured at amortised cost:		
Loans payable	5,572	5,322
Measured at undiscounted amount payable:		
Trade and other creditors	49,446	49,484
	<u>55,018</u>	<u>54,806</u>

The Group's income, expense, gains and losses in respect of financial instruments are summarised below:

	2015 £'000	2014 £'000
<b>Interest income and expense</b>		
Total interest expense for financial liabilities at amortised cost	250	250
<b>Fair value gains and losses</b>		
On financial assets measured at fair value through profit and loss	65	30
	<u>        </u>	<u>        </u>

## 19. CALLED UP SHARE CAPITAL

	2015 £'000	2014 £'000
Called up, allotted and fully paid:		
52,458,000 (2014: 58,558,000) Ordinary shares of £1 each	52,458	58,558
	<u>52,458</u>	<u>58,558</u>

On 19 March 2015, the company undertook a share capital reduction for £6,100,000, which increased retained earnings by a corresponding amount.

## HERMES FUND MANAGERS LIMITED

### NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

#### 20. SHARE BASED PAYMENTS

Under the previous Group equity reward scheme, Group employees were invited to subscribe for 'Growth' ordinary shares in the capital of the Company. Each share provided employees with (i) a right to share in the growth in the value of third party business of the business unit in which the employee works and (ii) a right to receive dividends in respect of the growth in post-tax profits generated by third party business, but only after employees have held the shares for the vesting period. The shares vested 50% after four years and 50% after five years. Shares were held by an employee benefit trust until they vested. If an employee ceased employment before the vesting period ended, the Company could redeem the shares at par value. No exercise price was attributed to the shares issued. Details of shares issued to Group employees who provide employment services to the Group are as follows:

	2015 No. of shares	2015 Subscription price (£)	2014 No. of shares	2014 Subscription price (£)
Outstanding at beginning of period	3,717	3,717	5,685	5,685
Granted during the period	-	-	325	325
Forfeited during the period	(3,717)	(3,717)	(2,293)	(2,293)
Outstanding at the end of the period	-	-	3,717	3,717

No share awards were issued during the year (2014: 325) to employees who provided services to the Company and its subsidiaries. Equity-settled awards are valued at grant date. The fair value of the awards at grant date is recognised in the profit and loss account over the period to vesting. The fair value of the awards issued since inception of this reward scheme is not material to the financial statements of the Group or Company and therefore no more disclosure is included in these financial statements.

On 20 March 2015, the Group purchased all growth shares outstanding for cash consideration equal to the fair value of the shares totalling £6,073,867. The shares were subsequently cancelled.

#### 21. LONG TERM INCENTIVE PLAN

The Long Term Incentive Plan (LTIP) is a new incentive plan which Hermes introduced in order to align an element of certain key employees' compensation to the future success of the Group.

For each award, the shares vest after four years. Each award in 2015 represents the following:

- On vesting in 2019, and on the basis that there is no full sale of Hermes before that date a right to share in 25% of the pre-tax statutory profits of Hermes.
- Pre-vesting, a right to share in a proportion of the proceeds of any sale or partial sale of Hermes are above the initial base value.

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 21. LONG TERM INCENTIVE PLAN (continued)

	2015
	No. of units awarded
At 1 January	-
Issued during year	98.5
Forfeited during year	(3.0)
At 31 December	95.5

During the year the company issued 98.5 units. Due to the leaver provisions 3 of these units were forfeited during the year. The total liability recognised in respect of the 2015 award was £896,268.

In addition to the LTIP, an Interim Profit Participation ("IPP") plan was introduced. Each IPP unit entitles the holder to a right to share in 18.5% of the pre-tax statutory profits of Hermes for the years ending 31 December 2015, 2016 and 2017. The value of the IPP liability recognised as at 31 December 2015 was £1,640,319.

## 22. FINANCIAL COMMITMENTS

Operating Lease Commitments

The Group and Company annual commitments for the year to 31 December 2015 under operating leases are as follows:

	2015	2015	2014	2014
	Land and	Other	Land and	Other
	Buildings		Buildings	
	£'000	£'000	£'000	£'000
Operating leases which expire within:				
One year	19	-	117	-
Two - five years	2,087	938	2,131	300
Over five years	-	-	-	-
	2,106	938	2,248	300

All UK operating leases relating to land and buildings are subject to five-yearly, upward-only, rent reviews.

Other Financial Commitments

A subsidiary of the Company, Hermes Sourcecap Limited (HSL), was party to a contractual option arrangement entered into under the terms of the shareholders' agreement when the Company purchased HSL on 3 December 2009. This contract was cancelled in 2013 and in its place, the Company acquired the further shares in HSL with consideration comprising cash and contingent amounts based upon the valuation of the 999 shares purchased in future year. The value of the final contingent consideration totalled £158,384.



## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 22. FINANCIAL COMMITMENTS (continued)

Contingent Liabilities

During the year the Company gave guarantees under section 479C of the Companies Act 2006 to two wholly-owned subsidiary undertakings: Hermes Assured Limited and Hermes Investments (North America) Limited. As such, both subsidiaries are exempt from the requirements of the Companies Act relating to the audit of individual accounts for the year ended 31 December 2015 by virtue of section 479A of the Companies Act 2006.

## 23. RECONCILIATION OF OPERATING PROFIT / (LOSS) TO NET CASH OUTFLOW FROM OPERATING ACTIVITIES

	Group 2015 £'000	Company 2015 £'000	Group 2014 £'000	Company 2014 £'000
Operating gain / (loss)	9,988	(21,582)	(15,804)	(31,245)
Realised currency loss / (gain)	(100)	(147)	251	(45)
Loss on disposal of fixed assets	-	-	2,047	2,048
Difference between pension contributions and charge against operating profit	(7,034)	(7,034)	(6,803)	(6,803)
Depreciation	1,472	1,413	1,631	1,577
Amortisation	1,335	-	1,335	-
(Increase) / Decrease in debtors	(1,014)	5,255	2,097	12,281
Increase / (decrease) in creditors	933	40,285	8,332	10,826
Net cash inflow / (outflow) from operating activities	5,580	18,190	(6,914)	(11,361)

## 24. RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS

	Group 2015 £'000	Company 2015 £'000	Group 2014 £'000	Company 2014 £'000
Net funds at beginning of year	55,445	26,928	41,294	6,994
Increase / (decrease) in cash in year	(2,085)	24,164	14,151	19,934
Net funds at end of year	53,360	51,092	55,445	26,928

**HERMES FUND MANAGERS LIMITED****NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)****25. ADDITIONAL INFORMATION ON PRINCIPAL SUBSIDIARIES AND JOINT VENTURES**

The Company and the Group have investments in the following subsidiary undertakings and joint ventures which principally affect the results and net assets of the Group. All significant subsidiaries are held by the Company directly.

<b>SUBSIDIARY UNDERTAKINGS</b>	<b>ACTIVITY</b>
Hermes Investment Management Limited	Investment management
Hermes Real Estate Investment Management Limited	Investment management
Hermes Sourcecap Limited	Investment management
Hermes BPK Limited	Investment management
Hermes Private Equity Limited	Investment management
Hermes Alternative Investment Management Limited	Investment management
Hermes Equity Ownership Services Limited	Stewardship and corporate governance
HFM (Singapore) Pte. Limited	Investment management
Hermes Administration Services Limited	Investment management
Hermes Assured Limited	Investment management
HFM (Australia) Pty Limited	Investment management
Hermes Global Funds GP Limited	Investment management
Hermes BPK Partners Inc	Investment management
Hermes BPK Accelerator (Cayman) Limited	Investment management
Hermes BPK Coinvestment Trustees Limited	Investment management
Hermes Investments (North America) Limited	Investment management
Hermes Fund Managers (North America) GP, Inc.	Investment management
Hermes Global Equities Partners LP	Investment management
Hermes Fund Managers (North America) LP	Investment management
Hermes Pension Fund Management Limited	Investment management
Hermes Real Estate Senior Debt Fund GP Limited	Investment management
Hermes Private Debt I GP Limited	Investment management
Hermes Secretariat Limited	Investment management
<b>JOINT VENTURES</b>	<b>ACTIVITY</b>
Hermes GPE LLP	Investment management
Vista UK Residential 1 (GP) LLP	Investment management
Vista UK Residential Real Estate (GP)	Investment management

Subsidiary undertakings disclosed above are wholly-owned subsidiaries except for Hermes Sourcecap Limited (83% of ordinary share capital owned). All subsidiaries disclosed above have been consolidated in these financial statements. All are incorporated in Great Britain and registered and operate in England and Wales, with the exception of HFM (Singapore) Pte. Limited which is incorporated in Singapore.

Hermes GPE LLP ("HGPE") is a joint venture between Hermes Fund Managers Limited and the HGPE management team through GPE Partner Limited. It is incorporated in the United Kingdom and is registered and operates in England and Wales.

There are plans to liquidate Hermes BPK Limited during 2016 due to the closure of the business.

# HERMES FUND MANAGERS LIMITED

## NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

### 26. FINANCIAL RISK MANAGEMENT OBJECTIVES AND STRATEGY

The Group's activities expose it to a number of financial risks including credit risk, cash flow risk and liquidity risk. The use of financial derivatives is governed by the Group's policies approved by the board of directors, which provide written principles on the use of financial derivatives to manage these risks. The Group does not use derivative financial instruments for speculative purposes.

The principal financial risk exposures of the Company and the Group at the balance sheet date relate to credit, liquidity and interest rate risks. The Group has in place a system of controls and processes to mitigate the risks identified.

#### Credit Risk

Credit risk is the risk that a counterparty will be unable to meet a commitment that it has entered into with the entity. The following are credit risks relevant to the Company and the Group at the balance sheet date.

i) Fund-specific – Within a number of the funds operated by entities within the Group, investment positions are taken gaining exposure to other parties. Applicable limits are stated within the objectives and constraints of each fund. The risk is assessed by qualified and trained professionals using a range of information and tools.

ii) Transaction-related – An inevitable consequence of both investment transactions within the funds and transactions within Group entities is the involvement of counterparties, particularly brokers. A process is in place to assess the suitability of counterparties.

The carrying amounts of financial assets best represent the maximum credit risk exposure at the balance sheet date. At 31 December 2015, the Group and the Company's financial assets exposed to credit risk amounted to the following:

#### **Financial assets**

	<b>2015</b>	<b>2015</b>	<b>2014</b>	<b>2014</b>
	<b>Group</b>	<b>Company</b>	<b>Group</b>	<b>Company</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
Cash at bank	53,360	51,092	55,445	26,928
Owed by subsidiaries	-	17,476	-	20,706
Trade debtors and accrued income	17,414	3,070	21,660	2,432
Taxation	5,684	15,744	3,947	5,419
Owed by parent	13,928	135	11,534	69
Other debtors	1,172	1,162	1,353	1,273
	<b>91,558</b>	<b>88,679</b>	<b>93,939</b>	<b>56,827</b>

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 26. FINANCIAL RISK MANAGEMENT OBJECTIVES AND STRATEGY (continued)

Cash at bank is held in current accounts or put on deposit with highly-rated counterparties. Bankruptcy or insolvency of bank counterparties may cause the Company's rights with respect to the cash held by the banks to be delayed or limited. Bank credit ratings are high and are monitored by management with reference to reputable rating agencies such as Standard & Poor's, Moody's or Fitch. If the banks' financial positions were to materially deteriorate then cash holdings would be moved to other banks.

Bankruptcy or insolvency of the counterparty may also cause the Company's rights with respect to the amounts owed being delayed or limited. The Company manages its risk by dealing with reputable counterparties offering a low risk of default. The financial position of the counterparties is regularly reviewed.

At year-end, within the Company and the Group, an insignificant level of debt was substantially past due and the majority of debt outstanding at the balance sheet date has been received post year-end. Trade debtors of the Group amounting to £1,055,348 were more than 90 days past due at 31 December 2015.

Liquidity Risk

Liquidity risk arises as a result of the possibility that the Company may not have sufficient cash funds to meet its liabilities as they fall due.

Below is a maturity analysis of the Group's and the Company's undiscounted liabilities at the balance sheet date:

Financial liabilities	Maturity	2015	2015	2014	2014
		Group £'000	Company £'000	Group £'000	Company £'000
Owed to parent	< 12 mths	994	-	4,041	-
Owed to associates	< 12 mths	-	44,608	-	-
Other creditors < 12 mths	< 12 mths	488	445	2,278	701
Unfunded pension liability	< 12 mths	761	761	817	817
Accruals and prepaid income	< 6 mths	38,100	18,807	37,375	21,021
Owed to parent	> 12 mths	5,572	5,572	5,322	5,322
Other creditors > 12 mths	> 12 mths	9,103	4,486	4,974	1,225
		<u>55,018</u>	<u>74,679</u>	<u>54,806</u>	<u>29,086</u>

The Company's liquidity risk relates to its cash dealings with clients, day-to-day trading activity, the funding of operational expenses and meeting solvency requirements as determined by the regulator (Financial Conduct Authority). The maintenance of liquidity is reported and monitored by senior management on a regular basis.

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 26. FINANCIAL RISK MANAGEMENT OBJECTIVES AND STRATEGY (continued)

Interest Rate Risk

Whilst not the primary focus of the Group the nature of the business gives rise to large cash balances being held and consequently potentially significant interest receipts. The Group's Finance department aims to mitigate the interest rate risk by continually monitoring the cash position of the Group and seeks the optimal level of cash to place on deposit given the Group's liquidity requirements. The Group's Treasury department seeks to obtain the optimum return on cash deposited.

If the average rate of interest was 2% higher during the year based upon the year-end cash position, an additional £1.1m interest would have been earned.

## 27. RELATED PARTY TRANSACTIONS

## (a) General information and disclosure exemptions

Subsidiaries

The Company prepares Group accounts into which its subsidiaries are consolidated. The Company has not disclosed related party transactions with wholly-owned subsidiaries as it is taking advantage of the exemption in FRS 102.

Hermes Group Pension Scheme

Certain activities of the Scheme are carried out by the Hermes Group, all of the costs of which are borne by the Company. These costs have not been apportioned for accounting purposes between those attributable to the Scheme and those attributable to the Hermes Group as functions maintained for both entities cannot be divided meaningfully between them.

## (b) Related party transactions

During the year there were transactions with the following related parties

The following fees were paid by BT Pension Scheme Management Limited ("BTPSM") in respect of services provided to the Hermes Group.

	2015 £'000	2014 £'000
P Spencer (Chairman & Non-Executive Director Fee)	88	88
W McClory (Non-Executive Director Fee)	25	25
<b>TOTAL</b>	<b>113</b>	<b>113</b>

Central allocated costs from the Company to BTPSM totalled £3,511,028 during the year (2014: £3,796,779). An amount was due to the Company from BTPSM totalling £1,092,720 at year-end (2014: £978,923).

## HERMES FUND MANAGERS LIMITED

### NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015 (continued)

#### 27. RELATED PARTY TRANSACTIONS (continued)

The following transactions occurred during the year with subsidiaries that are / were part-owned:

- Hermes Sourcecap Limited (HSL)

Central allocated costs from the Company to HSL totalled £1,763,856.66 during the year (2014: £1,585,658). HSL provide funds to HFML to place on deposit for the Group. There is an amount due to HSL totalling £612,808 at year-end (2014: £33,734 amount due to HSL), representing the net year-end debt due to HSL for funds provided less allocation of costs.

The following transactions occurred during the year with joint ventures:

- Hermes GPE LLP (HGPE)

Central allocated costs from the Company to HGPE totalled £1,350,000 during the year (2014: £1,176,054). An amount was due to the Company from HGPE totalling £10,883 at year-end (2014: £31,210).

- Logistics Management Limited (LML)

In the prior year dividends were declared during the year totalling £29,300. HFML Group, as 50% owner of LML, received £14,650. On 20 January 2015 LML was dissolved.

The following transactions occurred during the year with other related parties:

#### Directors' transactions

Loan to director:

During the year ended 31 December 2014 the company advanced one of the directors an unsecured loan totalling £120,000. The interest was charged at the HMRC beneficial loan rate. This loan was repayable in 2015 over three instalments. During the year the entire loan was repaid.

**HERMES FUND MANAGERS LIMITED****NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)****27. RELATED PARTY TRANSACTIONS (continued)**

Other related party transactions

The key management personnel are the Directors and the Executive Committee.

The total remuneration for key management personnel for the period totalled £6,224,826 (2014: £6,651,648), being remuneration disclosed in note 7 of £4,669,340 (2014: £5,550,169) and remuneration provided to other key management personnel of £1,555,526 (2014: £1,101,481).

**28. NON-CONTROLLING INTEREST – EQUITY**

The minority interest liability of £400,000 (2014: £1,173,924) included within the consolidated balance sheet and a debit of £400,100 (2014: credit of £594,853) included within the consolidated profit and loss account relate to a 17% shareholding in Hermes Sourcecap Limited which is owned by an individual director of the entity (2014: 35% shareholding owned by individual directors and employees).

**29. ULTIMATE PARENT UNDERTAKING**

The directors regard the BT Pension Scheme as the Company's immediate and ultimate parent and controlling entity. It is also the parent of the largest and smallest Group to prepare Group accounts into which the results of the Company are consolidated. The accounts of the BT Pension Scheme can be obtained at Lloyds Chambers, 1 Portsoken Street, London E1 8HZ.

**30. EXPLANATION ON TRANSITION TO FRS 102**

This is the first year that the Company has presented its financial statements under Financial Reporting Standard 102 (FRS 102) issued by the Financial Reporting Council. The following disclosures are required in the year of transition. The last financial statements under previous UK GAAP were for the year ended 31 December 2014 and the date of transition to FRS 102 was therefore 1 January 2014. As a consequence of adopting FRS 102, a number of accounting policies have changed to comply with that standard.

## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 30. EXPLANATION ON TRANSITION TO FRS 102 (continued)

## Reconciliation of equity

	At 1 January 2014 Group £'000	At 31 December 2014 Group £'000	At 1 January 2014 Company £'000	At 31 December 2014 Company £'000
Equity reported under previous GAAP	30,154	43,033	40,775	48,378
Adjustments to equity on transition to FRS 102:				
Holiday pay accrual	(194)	(403)	(57)	(189)
Equity reported under FRS 102	29,960	42,630	40,718	48,189

Notes to the reconciliation of equity at 1 January 2014:

Reserve movements

As a result of the change in accounting policy from Alternative Valuation rules to fair value through profit and loss (FVTPL), all movements to this reserve was transferred into the profit and loss account. On the statement of comprehensive income for the Group and Company the revaluation reserve total has been transferred to the profit and loss account.

Holiday pay accrual

FRS 102 includes a requirement to provide for unutilised holiday pay entitlement at the year-end.



## HERMES FUND MANAGERS LIMITED

NOTES TO THE FINANCIAL STATEMENTS - YEAR ENDED 31 DECEMBER 2015  
(continued)

## 30. EXPLANATION OF TRANSITION TO FRS 102 (continued)

## Reconciliation of profit or loss for 2014

	Group £'000	Company £'000
Loss for the financial year under previous UK GAAP	(8,900)	(15,189)
Defined benefit pension scheme adjustment	(1,350)	(1,350)
Revaluation of fair value investments	30	30
Holiday pay accrual	(209)	(132)
Loss for the financial year under FRS 102	<u>(10,429)</u>	<u>(16,641)</u>

Notes to the reconciliation of profit or loss for 2014

These all result from changes to accounting policies as required by FRS 102.

Defined benefit pension scheme adjustment

Current GAAP requires the interest on pension assets to use the expected return on the brought forward asset. FRS 102 requires companies to use the same rate at which they discounted their pension liabilities resulting in lower income in the P&L. Ultimately, plan assets are still measured at fair value so any impact on P&L as a result of this change is compensated in other comprehensive income.

Revaluation of fair value investments

Investments held directly in fund vehicles are measured at fair value through profit and loss. Previously these movements were being recognised in the revaluation reserve.

Holiday pay accrual

FRS 102 includes a requirement to provide for unutilised holiday pay entitlement at the year-end.

## **Our pledge**

**I pledge to fulfil, to the best of my ability and judgment and in accordance with my role, this covenant:**

- I will act ethically, responsibly and with integrity
- I will put the interests of our clients and their beneficiaries first
- I will encourage responsible behaviour in the firms in which we invest and on which we engage
- I will act with consideration for society and the environment both now and in the future. I will encourage others to do the same
- I will work with industry colleagues and other key stakeholders to develop and improve our industry's contribution to society
- I will treat my clients, my colleagues and all other stakeholders with respect and as I would wish to be treated
- I will deal with our regulators in an open, co-operative and timely way
- I will communicate clearly and honestly with all parties inside and outside our firm
- I will manage conflicts of interest fairly between all parties