

Hobart Capital Markets Ltd

Pillar 3 Disclosures 2009

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1.0 EXECUTIVE SUMMARY

This Pillar 3 document covers Hobart Capital Markets Ltd – a FSA Regulated company.

1.1 Summary Financial Positions

The projected regulatory position of the company over the next four years is detailed below, showing a significant capital surplus.

	2010	2011	2012	2013
	<u>£ 000</u>	<u>£ 000</u>	<u>£ 000</u>	<u>£ 000</u>
Capital Resources	2,891	3,827	5,690	7,882
Capital Requirements				
- Pillar 1	(1,045)	(1,172)	(1,174)	(1,190)
- Pillar 2	(200)	(248)	(287)	(306)
Capital Surplus	1,646	2,407	4,229	6,386

1.2 Capital and Dividend Plan

The company is capitalised by the issue of ordinary shares and preference shares.

The capital requirements of the company are monitored on an ongoing basis to ensure that at any time there is always sufficient capital in place, this is also completed as part of the annual budgeting process. At the time of writing this report, the business is in the process of introducing an additional £1m of capital to ensure it has sufficient capital resources to cover its risks.

Dividends are paid if it is considered that there are adequate reserves in place and any payment would not jeopardise the company's ability to meet all of its regulatory requirements. As a privately owned company, there are no external expectations with respect to dividends.

1.3 Material Risks

An exercise has been completed considering the key risks that the company faces. The twelve risk headings as suggested by the FSA have been

considered and the detailed risks within those headings have also been looked at, along with any controls and mitigating factors that exist within the business to manage these risks.

From the analysis completed, risks have been described as low, medium or high. The material risks that the company faces are considered to be the following:-

Liquidity risk

The company manages its cash flow carefully at all times and prepares rolling six month cash flow forecasts at least once a month. Cash balances and expected flows are monitored on a daily basis. However, there is an inherent liquidity risk associated with the CFD business and although the CFD book is small and well margined, it could increase in the future. Accordingly there is a medium liquidity risk.

Credit risk

This has been classified as a low risk. Due to the nature of the business there is the potential for loss if clients default on margin calls. The business suffered bad debts from the Dawnay Day Groups of companies for CFD margin defaults during the year to September 2008. Hobart has not experienced any other CFD margin defaults since then. Following the recent turbulence in the market place, the business has reviewed its credit risk policy and subsequently reduced its CFD book significantly.

Concentration risk

The company has a diverse client base, accordingly there is not a reliance on any one client for a substantial portion of the company's turnover, hence this risk is considered a low risk.

Business risk

The company has no control over the wider economic environment but any economic downturn will undoubtedly have an impact on the business and its performance, this is considered a low risk.

This risk categorisation was determined as part of the ICAAP process completed in September 2009. These categories will be reviewed in April 2010 when the ICAAP is updated.

1.4 Outstanding Issues

This Pillar 3 document will be reviewed again in 2010 where input from a professional services firm that has completed Pillar 3 exercises for a number of clients may be sought. This exercise would highlight where additional refinements or analysis are considered necessary.

1.5 Preparation and Approval

This Pillar 3 document has been prepared by Finance Personnel within the company and has been circulated for review by Senior Management within the company.

2. BACKGROUND

Hobart Capital Markets Limited acts as an agency broker in equities and fixed interest securities, as well as providing equity contracts for difference ('CFDs'), for institutional clients and high net worth individuals.

The business has now completed its fourth full year of trading. Initially the business operated as a division of Dawnay, Day Brokers Ltd before, on the 1st October 2007, the entire division, then called Dawnay, Day Capital Markets, was reassigned to Hobart Capital Markets Limited the new company that was established for this purpose. The business has seen continued growth and expansion in trading turnover throughout this four year period.

Trading and client reporting are controlled by state of the art STP systems utilising systems provided by Fidessa, Oasys and Rolf and Nolan amongst others. Hobart accepts orders and reports back to institutions using Fix protocol when required.

Equity clearing and settlement is provided by Nomura International Plc and Pershing Securities Ltd under a model B arrangement, with a similar facility from Nomura for fixed interest. Hobart issue CFDs to its clients and fully hedge these with CFDs written by a number of leading CFD providers. The client side of the business uses Rolf and Nolan to prepare client related information and monitoring. The accounting system used within the business is Sage 50.

The company is regulated by the FSA and is classified as a BIPRU €125k, Limited License Firm.

The European Union Capital Requirements Directive came into effect on 1 January 2007. It introduced consistent capital adequacy standards and an associated supervisory framework in the EU based on the Basel II rules agreed by the G-10.

In the UK, the implementation of this Directive was done by the introduction of rules by the Financial Services Authority (FSA). These FSA requirements require disclosures known as Pillar 3. These Pillar 3 requirements are designed to provide market participants with key information on a firm's risk exposures and risk management processes. The Pillar 3 disclosures also aim

to complement the minimum capital requirements (Pillar 1) of a firm and the supervisory review processes of Pillar 2.

Hobart Capital Markets Ltd adopted the Pillar 1 – 3 standardised approach to risk from the company's inception. Any disclosures made in this document are on a standardised basis.

2.1 Frequency and Basis of Disclosures

This disclosure document has been prepared in accordance with the requirements of Pillar 3.

Future disclosures will be issued on an annual basis from 30 September 2010 and published as soon as practicable after the publication of the Annual Report and Accounts.

2.2 Verification and Location

These disclosures have been reviewed by the Hobart Capital Markets Ltd Risk Oversight Group (ROG) and are published on the corporate website (www.hobartcapital.com). The disclosures are not subject to audit except for when they are in line with the disclosures prepared in the company's Annual Report and Accounts. The members of The Hobart ROG include Colin Thomas (CEO), Richard O'Neill (Head of Operations), Neil Ridley (Joint Head of Trading) and Martin Lawrence (Financial Controller).

3. RISK MANAGEMENT OBJECTIVES AND POLICIES

Hobart Capital Markets Ltd is a privately owned business. Due to the fact the shareholders are also employees of the business and with the current market turmoil; the Board has been prudent in deciding on its risk appetite. As such, the Board has agreed to adopt an overall low risk appetite.

This risk appetite has been integrated into the corporate planning, capital planning and group risk management processes within the business. This allows the board to adopt some overall parameters to ensure the business operated within its chosen risk category.

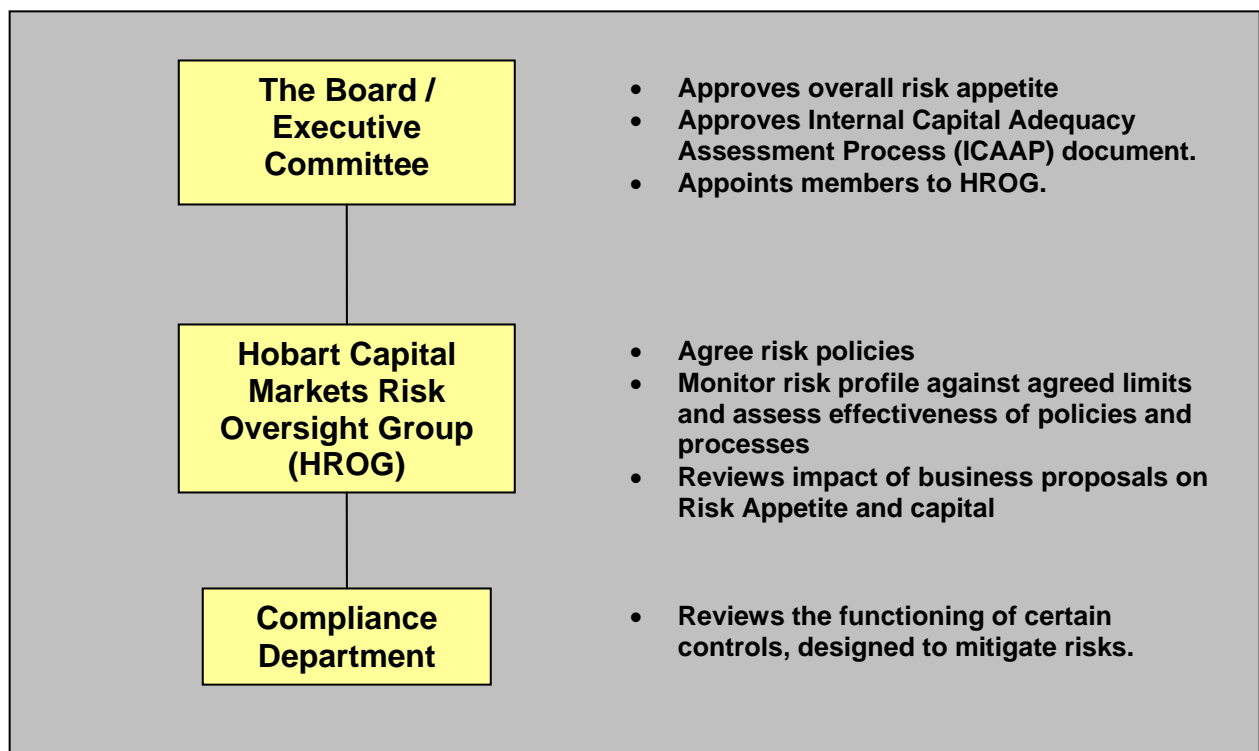
3.1 The Hobart Capital Markets Ltd approach to risk

Hobart Capital Markets tries to mitigate its risks in two ways. The primary responsibility for risk identification, monitoring and control lies with the operational areas. Oversight and guidance is provided by the Hobart Risk Oversight Committee, which meets quarterly to discuss the various risks

facing the business. Finance personnel are going to establish a quarterly risk management report from 1st January 2010. The purpose of this is to document and quantify the various risks facing the business and track how the risk exposure is managed on a monthly basis.

The compliance department also consider the impact and severity of the risks on an individual basis; which is in isolation from other risk analysis. This provides a third control to ensure the low risk appetite of the business is adhered to.

This model is applied to all risks which could have a significant negative impact on the business if they were to materialise. Such material risks represent Hobart Capital Markets 'Risk Profile' and are reviewed and reassessed at least annually as part of the Internal Capital Adequacy Assessment Process (ICAAP) – see section 5.1.



The Hobart Capital Markets Ltd committee and risk management structure is summarised above

4. CAPITAL RESOURCES

As at 30 September 2009, the business complied with the capital requirements that were in force as set out by the FSA.

The following table shows the breakdown of the total available capital for Hobart Capital Markets Ltd.

Capital Resources as at 30 September 2009		STAGE	30-Sep-09
Tier 1 Capital	Permanent share capital - ordinary shares		3,000,000
	Permanent share capital - 'A' ordinary shares		951
	Profit and loss account - audited accounts		- 5,024,674
	Interim Losses		- 401,961
	Externally verified interim profit & loss account		
	Sub-Total	A	- 2,425,684
	Irredeemable non cumulative preference shares	B	4,000,000
	TOTAL Tier 1 Capital before deductions	E	1,574,316
	TOTAL Tier 1 Capital after deductions	F	1,574,316
Tier 2 Capital	Total of upper and lower tier 2 capital	K	-
Tier 3 Capital	Total Tier 3 capital	Q	-
Total Capital	TOTAL CAPITAL AFTER DEDUCTIONS	T	1,574,316

4.1 Tier 1 Capital

Tier 1 capital comprises Ordinary Shares, A Ordinary Shares and Irredeemable Non-Cumulative Preference Shares. A deduction has been taken from Tier 1 capital in respect of the losses incurred from July 2008 onwards, which were largely caused by the write off of debts from the demise of companies associated to Hobart's former parent company.

5. CAPITAL ADEQUACY

Hobart Capital Markets Ltd measures its capital requirement at least monthly to ensure there is always sufficient regulatory capital within the business to support its activities. Regulatory capital covers all Pillar 1 risks (i.e. credit risk, market risk, exchange rate risk). Hobart Capital Markets Ltd determines its minimum Capital Resources Requirement using a detailed regulatory capital schedule which is compliant with the BIPRU rules.

Regulatory Capital is reported in the monthly Board Pack, so the Board is aware of any movements in this requirement on a monthly basis.

5.1 Internal Capital Adequacy Assessment Process (ICAAP)

Hobart Capital Markets Ltd undertakes an Internal Capital Adequacy Assessment Process (ICAAP) which is an internal assessment of its capital needs. The ICAAP is a constantly evolving document that is to be updated at least twice annually to encompass the changes in the business. The ICAAP considers the current Pillar 1 risks and predicts company performance over a four year period to forecast what the Pillar 1 risk will be each year.

The ICAAP also looks at the various risks Hobart Capital Markets Ltd faces by calculating its Pillar 2 requirement. Pillar 2 capital identifies and quantifies the risks facing the business using scenario analysis. The result is an additional capital requirement which should be sufficient to mitigate any of these risks, should they impact on the business.

5.2 Minimum Capital Requirement

Hobart Capital Markets Ltd has a minimum capital requirement which is equal to its fixed overhead requirement (FOR) as this is higher than the total of the company's combined credit and market risk requirements.

5.3 Summary Financial Position – Capital Projections

The projected regulatory position of the company over the next four years is detailed on page 3, showing a significant capital surplus in each of the four years to 2013.

6. CREDIT RISK MEASUREMENT AND MITIGATION

Credit risk can be described as the potential loss to an institution of all or part of a loan, outstanding debtor balance, security, guarantee or indemnity given by the institution.

This has been classified as a medium risk within Hobart Capital Markets. Due to the nature of the business there is the potential for loss if clients default on CFD margin calls. Hobart has had no defaults for CFD margins from any clients other than companies associated with the former Dawnay Day group. Following the recent turbulence in the market place, the business has reviewed its credit risk policy and subsequently reduced its CFD exposure significantly. Credit risk is now considered to be minimal.

7. MARKET RISK

Market risk is defined as the potential reduction in net income, or decrease in value of the balance sheet, arising from adverse market movements.

Examples of specific market risks are:

- Interest Rate Risk
- Foreign Exchange Risk

Hobart Capital Markets Ltd minimises their exposure to Interest Rate Risk, as any exposure to changes in interest rates are passed on to the client. The residual interest rate risk is minimal.

Exposure to Foreign Exchange Risk is again on behalf of the client, therefore the majority of currency gains and losses would be to the benefit or detriment of the individual clients. It is the policy of Hobart Capital Markets Ltd to reconcile all currency balances daily and where applicable sell down into the base currency at least monthly. This minimises any risk of exchange rate gains and losses. A certain amount of Euro's and US dollars are maintained to cover invoices received in non-base currency.

8. OPERATIONAL RISK

Operational risk can be described as “the risk of loss arising from inadequate or failed internal processes, people and systems or from external events” (industry standard definition). Using this definition as guidance, Hobart Capital Markets has identified the following key operational risks and who is responsible:

- Financial Control – Financial Controller
- Fraud – MLRO, compliance department and all other business areas
- Business Continuity (DR) – Head of Operations / IT Manager
- Information Security – Head of Operations / IT Manager
- Information Technology – Head of Operations / IT Manager
- Regulatory/Legal – Chief Executive Officer, Compliance department and Financial Controller
- Key Staff Retention – Chief Executive Officer

The responsibility for each of these risks falls with the relevant area. Further to this, guidance is provided through the Hobart Capital Markets Risk Oversight Group (HROG). The compliance department monitors certain key controls designed to mitigate these risks.