OUTCOMES BEYOND PERFORMANCE

ANNUAL REPORT AND FINANCIAL STATEMENTS
31 DECEMBER 2016

www.hermes-investment.com

Registered No: 1661776

HERMES
INVESTMENT MANAGEMENT

Our commitment to holistic returns aims to deliver excellent investment performance and stewardship while helping to improve the lives of many

CONTENTS

} OUTCOME #12

Our work with the Institutional Investors Group on Climate Change is helping pension funds and asset managers take a proactive approach to managing carbon risk.

ABOUT US

We are an asset manager with a difference. We believe that, while our primary purpose is helping beneficiaries retire better by providing world class active investment management and stewardship services, our role goes further. We believe we have a duty to deliver holistic returns – outcomes for our clients that go far beyond the financial and consider the impact our decisions have on society, the environment and the wider world.

Our goal is to help people invest better, retire better and create a better society for all.

KEY FACTS

£28.5BN

We manage £28.5bn on behalf of institutional and retail investors around the world. Our investment capabilities span public and private equity and debt, infrastructure, real estate and multi asset solutions.

£261BN

We help asset owners and asset managers actively engage on their investments totalling over £261bn. These companies collectively support more than 25m current and future pensioners and savers.

351

We employ 351 talented individuals and are owned by the BT Pension Scheme, the largest corporate pension scheme in the United Kingdom.

OUR YEAR IN BRIEF

2016 Financial and Business Highlights

Our mission is to help beneficiaries retire better. To achieve this, we aim 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	2016	2015	Variance
DELIVERING HOLISTIC RETURNS	Percentage of investment strategies with a three-year track record to beat their benchmark[1]	**74%**	100%	↓
	Assets under management and advice[2]	**£28.5bn**	£23.0bn	↑
	Assets under stewardship[3]	**£261.3bn**	£154.7bn	↑
	Number of companies engaged	**562**	466	↑
	Number of company and policy interactions	**1,691**	1,823	↓
EMPLOYEE ALIGNMENT	Employee turnover	**10.1%**	11.3%	↓
DELIVERING A SUSTAINABLE AND PROFITABLE FIRM	Statutory revenue[4]	**£104.0m**	£105.5m	↓
	Statutory profit (pre-tax)	**£10.5m profit**	£14.6m profit	↓
	Underlying revenue[5]	**£111.8m**	£105.6m	↑
	Underlying profit[5]	**£15.5m**	£11.7m	↑
	Third-party revenue (as a % of total revenue)	**59%**	52%	↑

1 Performance is calculated using published benchmarks for strategies. If a strategy does not have an official benchmark a performance target is used. A representative portfolio for each strategy has been used and not all portfolios are included in these calculations. It excludes private equity and infrastructure and strategies that do not have the required track record.
2 The movement in Assets under Management and Advice is explained in more detail on page 22.
3 Assets under Stewardship relate to Hermes Equity Ownership Services Limited (Hermes EOS).
4 Statutory revenue represents the result as calculated in accordance with United Kingdom Generally Accepted Accounting Practice. Statutory revenue throughout the report relates to net group turnover as shown in the profit and loss account.
5 Underlying profit and underlying revenue represents the result regularly provided to the Board as this is considered the most useful basis on which to manage the activities of the Group. The reconciliation for this is provided on page 11. Underlying revenue differs from statutory revenue due to the timing of the recognition of non-recurring performance fees and the treatment of recharges to related entities.

CHAIRMAN'S STATEMENT

Review of 2016

Introduction

In 2011, our owners agreed a growth plan for Hermes that would transform it from the internal manager of the BT Pension Scheme (BTPS) into an internationally recognised third-party asset manager that would create a new model for the investment industry by considering the wider impact of its decisions on the environment and society, not just financial returns.

This required a long-term vision to create a sustainable firm focused on creating long-term holistic returns for all its stakeholders, measured by a range of financial and non-financial metrics. We will discuss underlying business performance throughout this report in this context, whilst also giving prominence to relevant statutory measures.

£10.5M

statutory profits (£14.6m in 2015)

£15.5M

underlying profits

↓

32%

higher than in 2015

59%
of our revenues now come from third parties

£111.8M
underlying revenues (£105.6m in 2015)

£98.6M
underlying costs (£98.4m in 2015)

With more uncertainty ahead, we will continue to focus on providing our clients and their underlying beneficiaries and savers with holistic returns. By that, we mean investment and stewardship outcomes that meet their long-term needs and which have a positive impact on society.

Overview

2016 was a successful year for Hermes, with long-term investment performance maintained, increasing sales and growth in both third-party assets under management and assets for which we provide stewardship services. Underlying profits of £15.5m were 32% higher than in 2015 (£11.7m), due to continued strong inflows of third-party assets, rising equity markets and the weakness in sterling, which benefited our non-sterling denominated earnings. Statutory profits of £10.5m were lower than in 2015 (£14.6m) due mainly to non-recurring performance fees recognised in 2015 from the BTPS portfolio.

Our business mix continues to evolve, with almost 60% of our revenues now generated from third parties. Overall revenues were £111.8m on an underlying basis (2015: £105.6m) and £104.0m on a statutory basis while underlying costs have remained broadly flat at £98.6m (2015: £98.4m). The difference to underlying revenue has been primarily driven by non-recurring performance fees.

Outlook

2016 may well come to be viewed as a pivotal year for global politics and the world economy, although the results may not be felt for some time. The impact of Brexit has, so far, been negligible for the firm, but we continue to monitor developments and plan for a range of possible outcomes. If the campaigning rhetoric becomes reality, the result of the US election could significantly affect global trade and the progress made on carbon reduction at the Paris Climate Summit. Elections in various European countries during 2017 could create further tensions within the European Union.

With more uncertainty ahead, we will continue to focus on providing our clients and their underlying beneficiaries and savers with holistic returns. By that, we mean investment and stewardship outcomes that meet their long-term standard of living needs and which have a positive impact on society. We have a team of investment professionals with great experience of navigating their way through many market environments and the associated volatility.

We will continue to focus on delivering excellent long-term investment performance, supported by our sophisticated Environmental, Social and Governance (ESG) integration and world-leading stewardship services. Due to our increasing market share of UK and European markets, coupled with the growth potential in Asia that is starting to become reality, the Board has every confidence that the business will continue to grow, despite the headwinds the industry may face.

Culture

At the heart of Hermes is a deeply held belief that we have a duty to generate outcomes for savers and beneficiaries that go beyond investment performance to include the impact on companies, individuals and society as a whole. This belief permeates everything that we do as a business and is reflected in the Hermes Pledge, which you will find at the end of the annual report and financial statements. The Pledge, which is voluntary, has been signed by 98% of our employees.

The remuneration of senior executives and their long-term incentives, the parameters of which have been set by our owners based on clear metrics, are laid out in the remuneration section of this report, which we have expanded considerably to further demonstrate our commitment to transparency. Our Board reports regularly to our owners, who are represented by two Non-Executive Directors who are also trustees of the pension scheme.

We continue to lead the debate and contribute to the transformation of the investment industry, and it was pleasing to see this recognised by *Financial News*, as the leader in ESG investing at their 20th Anniversary Awards for Excellence in European Finance.

I was also very pleased to announce Saker Nusseibeh's appointment to the Banking Standards Board during the course of the year.

At the heart of Hermes is a deeply held belief that we have a duty to generate outcomes for savers and beneficiaries that go beyond investment performance to include the impact on companies, individuals and society as a whole. This belief permeates everything that we do as a business and is reflected in the Hermes Pledge, which you will find at the end of the annual report and financial statements. The Pledge, which is voluntary, has been signed by 98% of our employees.

The Board

Paul Spencer CBE stepped down as Chairman of the Board on 31 March 2016. Under his leadership, Hermes has evolved into a highly regarded third-party asset manager that goes beyond investment performance to consider the needs of its clients, their beneficiaries and the society in which they live. As Chairman, I will lead the Board with the same objectives. Kathryn Matthews and Catherine Claydon stepped down from their roles as Non-Executive Directors before the date of this report, and I would like to thank them for their important contributions over their periods of service.

Lastly, on behalf of the Board I would like to thank everyone at Hermes for their hard work and dedication over the last 12 months, without which we would not have had such success, nor be so well placed for the future.

David Stewart
Chairman
31 March 2017

OUTCOME #14

A pupil from King's Cross Primary School, London N1. Benefiting from being part of the £550m King's Cross Redevelopment Programme.

KING'S CROSS URBAN REGENERATION

- A joint venture with UK and international partners
- 50 new environmentally friendly buildings
- 9,000 metres of green roofs
- 2 new schools
- 250 local people recruited
- 4,000 students at Central St Martin's
- 26 acres of new parks and open spaces
- Generating an annualised return of over 25% for investors

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.

I have been Chief Executive for five years and during that time, thanks to the hard work and skill of so many talented colleagues, we have transformed our business. Not only that, but we have seen the concept of stewardship and integrated ESG moving from the fringe to the mainstream.

It is particularly encouraging to see asset owners and asset managers alike increasingly accept what we have been saying for more than 30 years – that they have responsibilities that extend far beyond short-term financial gain. We believe that there is an unstoppable momentum behind this concept, which we refer to as "holistic returns", and that we are ideally positioned to lead its evolution and generate significant growth as a result.

At a financial level, several key metrics are linked to the underlying performance of the business, as reflected in our management accounts.

Five years of sustained growth

We have:

Beaten our performance benchmarks in **100%** of our investment strategies over five years to the end of December 2016[1]

Consolidated **13** boutiques into **ONE** global, award-winning, brand

Outperformed peer group medians[2] for **100%** of our strategies over five years, **93.3%** over three years + **88.9%** over one year

Established **389** new client relationships in **ELEVEN** new markets

Engaged with companies valued at more than **US$15 TRILLION** on behalf of more than **25 MILLION** beneficiaries worldwide

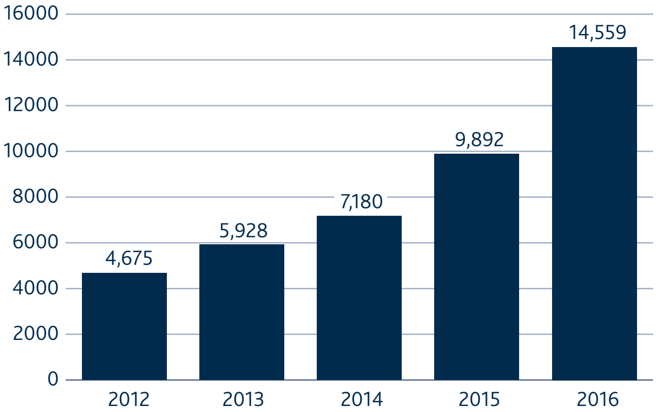
Grown assets by more than **300%**

and increased third-party revenues to almost **60%**

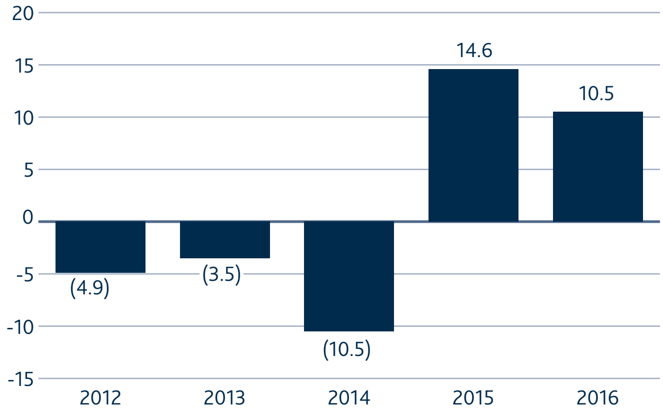
Increased stewardship assets by **£107BN** to **£261BN**

1 Excludes private equity and infrastructure.
2 Strategies that do not have a peer group are excluded from this calculation.

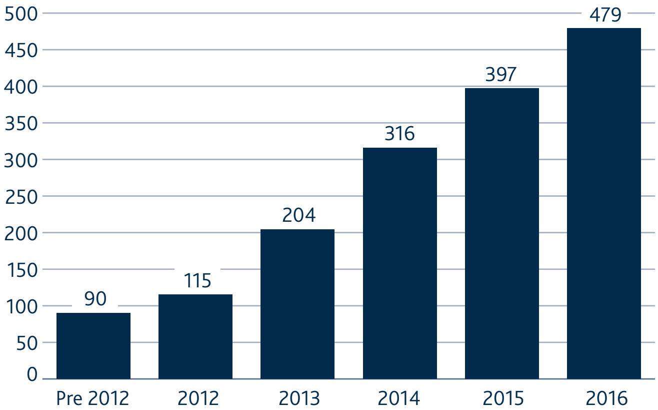
Third-party assets under management £m



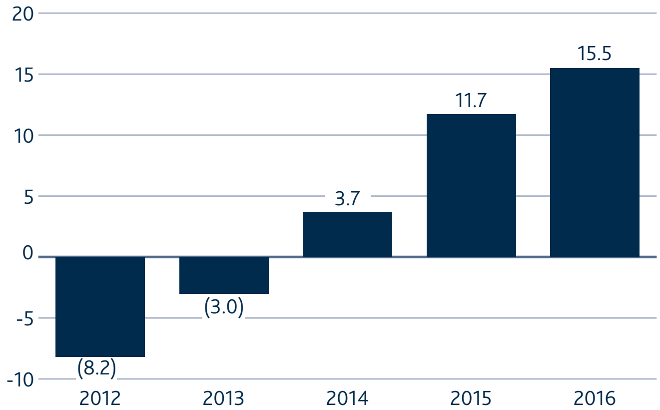
Statutory profit and (loss) £m



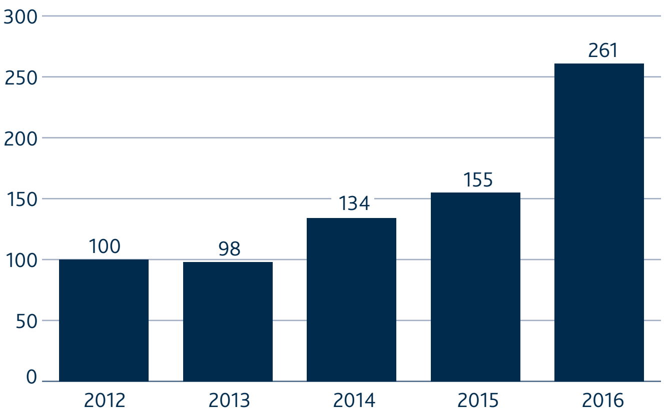
Number of third-party clients



Underlying profit and (loss) £m



Stewardship assets under advice £bn



	2012 £m	2013 £m	2014 £m	2015 £m	2016 £m
Statutory accounts pre-tax profit/(loss)	(4.9)	(3.5)	(10.5)	14.6	10.5
Add back goodwill amortisation	1.2	1.3	1.3	1.3	1.3
Restructuring	–	–	12.1	–	–
Bonus deferral	(1.1)	(0.5)	0.5	(1.3)	(2.0)
Regulatory change costs	–	–	–	(3.0)	–
Non-recurring performance fee crystalisation	–	–	–	(3.6)	3.6
Other	(3.4)	(0.3)	0.3	0.6	(1.5)
Long-term incentive plan	–	–	–	3.1	3.6
Underlying pre-tax profit/(loss)	(8.2)	(3.0)	3.7	11.7	15.5

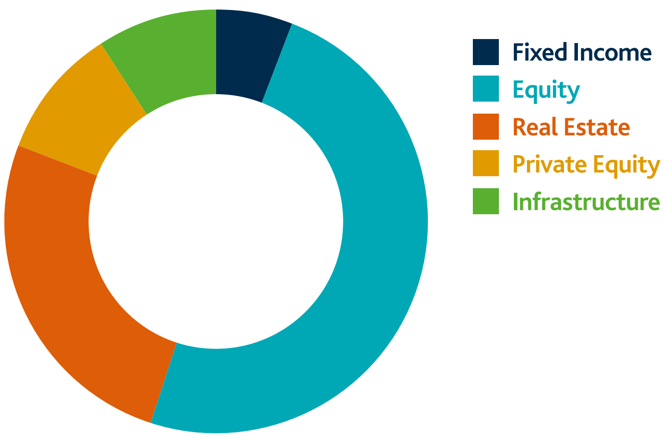
Information provided to the Board is prepared on an underlying basis, as this is the most useful basis on which to manage the activities of the Group. This result excludes a number of items that are not fully within the control of management. These items include goodwill amortisation, bonus deferral adjustments, defined benefit pension charges and foreign exchange retranslation of non-sterling denominated subsidiaries.

Further information is included on page 21.

Assets

We invest across a broad range of asset classes, with equity and real estate making up the largest proportion of the Group's investments. Between all the asset classes, we currently manage

£28.5BN



ALIGNED WITH THE NEEDS OF OUR CLIENTS

Underpinning our growth strategy is an intense focus on providing high value-add, sustainable, investment returns, delivered holistically and at an appropriate price.

We focus our resources on areas where:

There is long-term appeal from long-term investors

We can offer access to co-investment opportunities alongside our owner, BTPS, and other sophisticated global institutions

We have a differentiated approach through our active management and active ownership proposition

Within this framework, we have developed an optimised growth strategy based on four distinct pillars:

1. High conviction, high active share and liquid benchmarked capabilities integrating ESG factors

2. Unconstrained liquid credit and multi asset strategies

3. Access to private markets opportunities in infrastructure, private equity, private debt and real estate

4. Providing active ownership services to asset owners and asset managers, spanning stewardship, active engagement, intelligent voting, sustainable development and advocacy

BUSINESS REVIEW

At the end of 2016, 74% of our strategies had outperformed their benchmarks over three years. 2016 was a volatile year for public equity and credit markets, with some extreme short-term swings such as those experienced in the aftermath of the Brexit vote. Our median active share* was 87% and our asset-weighted information ratio** was 0.74. Over one year, only 44% of our strategies have outperformed their benchmarks. This was disappointing and below the standards to which we aspire. Over the same time period, however, 89% of our strategies outperformed their peer group medians, with 93% outperforming over three years and 100% over five years.

In our private markets strategies, our commercial real estate fund has outperformed its benchmark by an average of 2.5% over 10 years. Our flagship infrastructure vehicle has generated an internal rate of return of 12% with a cash yield of 8%. Our private equity co-investment program has generated an internal rate of return of 26%.*** All these strategies continue to deliver excellent long-term returns to their investors.

Revenues rose to £112m (£104m on a statutory basis) as our client base grew strongly in the year. Statutory profits before tax declined to £10.5m (2015: £14.6m), while the underlying profits rose 32% to £15.5m (2015: £11.7m).

Net sales from third parties were £3bn for the period, including assets raised in our joint venture, Hermes GPE LLP. Net new third-party revenues continued to grow and now equate to 59% of our total revenues, compared with 52% at the end of 2015 and less than 20% over five years ago.

We generated strong inflows across our investment strategies, led by our global equities capabilities, which raised more than £1bn. This was driven by the strong long-term performance generated since inception eight years ago, coupled with a growing interest in the team's sophisticated approach to explicitly integrating ESG factors as a means of enhancing returns. Academic evidence of the correlation between better governance and better returns continues to build.

74%
of our strategies outperformed their benchmarks over 3 years

12%
internal rate of return in our flagship infrastructure vehicle

£3BN
net third-party sales for the period, including assets raised in our joint venture, Hermes GPE

Despite the concerns caused by the Brexit vote, our greatest level of sales came from the UK and Europe, where the Nordic, Swiss and German markets generated the highest revenues.

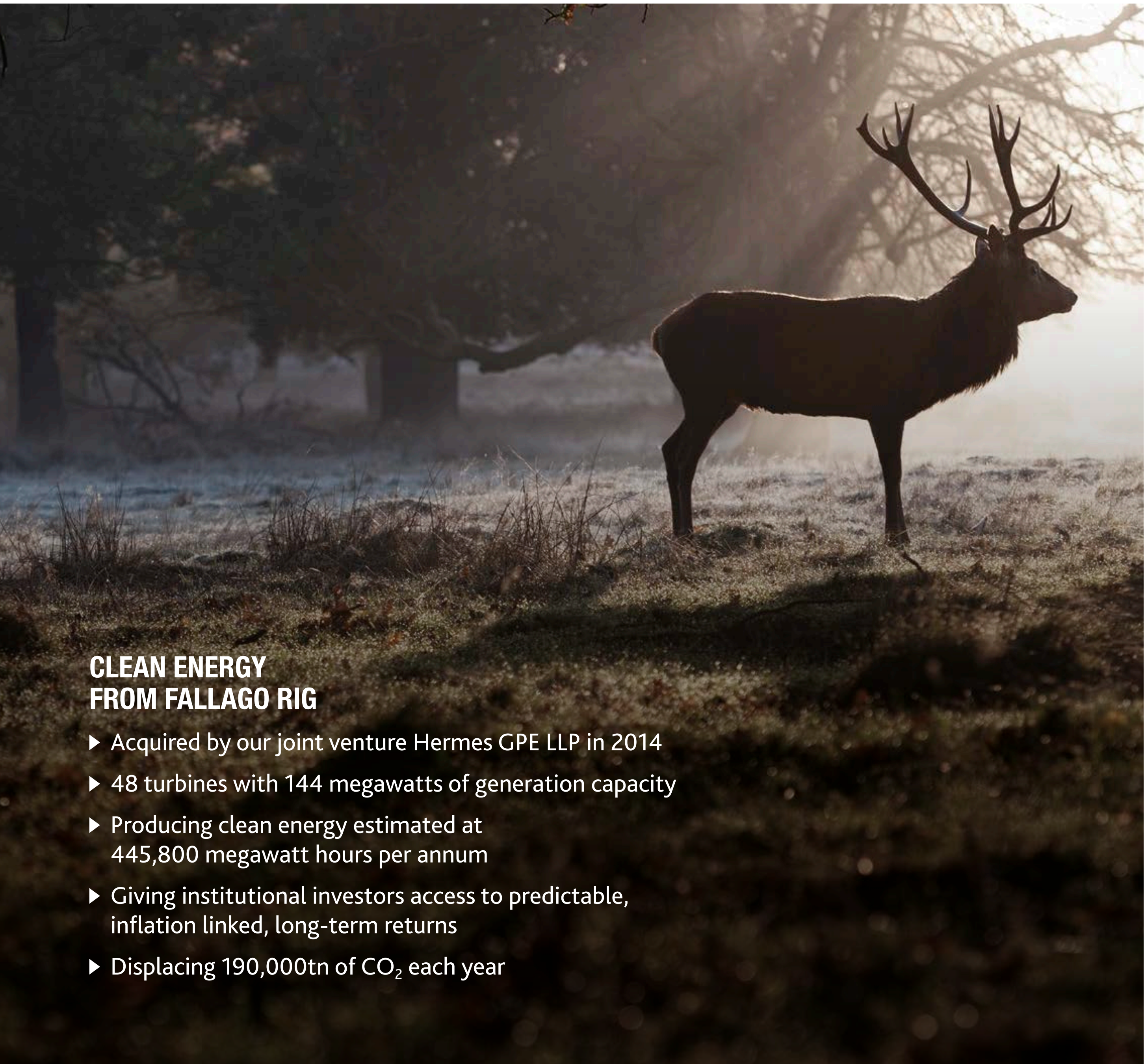
* Active share – measure of the percentage of stock holdings in a manager's portfolio that differ from the benchmark index.
** Information ratio – ratio of portfolio returns above the returns of the benchmark to the volatility of those returns. The IR measures a portfolio manager's ability to generate excess returns relative to a benchmark.
*** 2016 return for private equity is up to June 2016 and for infrastructure is up to September 2016.

Our global and regional emerging markets strategies generated the highest level of new revenues during the year, with most asset classes contributing positively. The exception was our European equity strategy, which saw outflows following two years of strong inflows. The prospects for this strategy are likely to remain challenging in 2017, given the political and economic challenges across Europe. Our credit strategies continue to grow in popularity as do our private markets capabilities, with infrastructure in particular seeing strong flows in the first half of the year.

Our new direct lending strategy was established toward the end of 2016 and is generating interest from investors. It is an excellent example of a strategy that delivers an outcome beyond performance, offering long-term investors access to a stream of relatively low risk but attractive yield, whilst providing a new source of finance to British companies. We intend to add a European version in 2017.

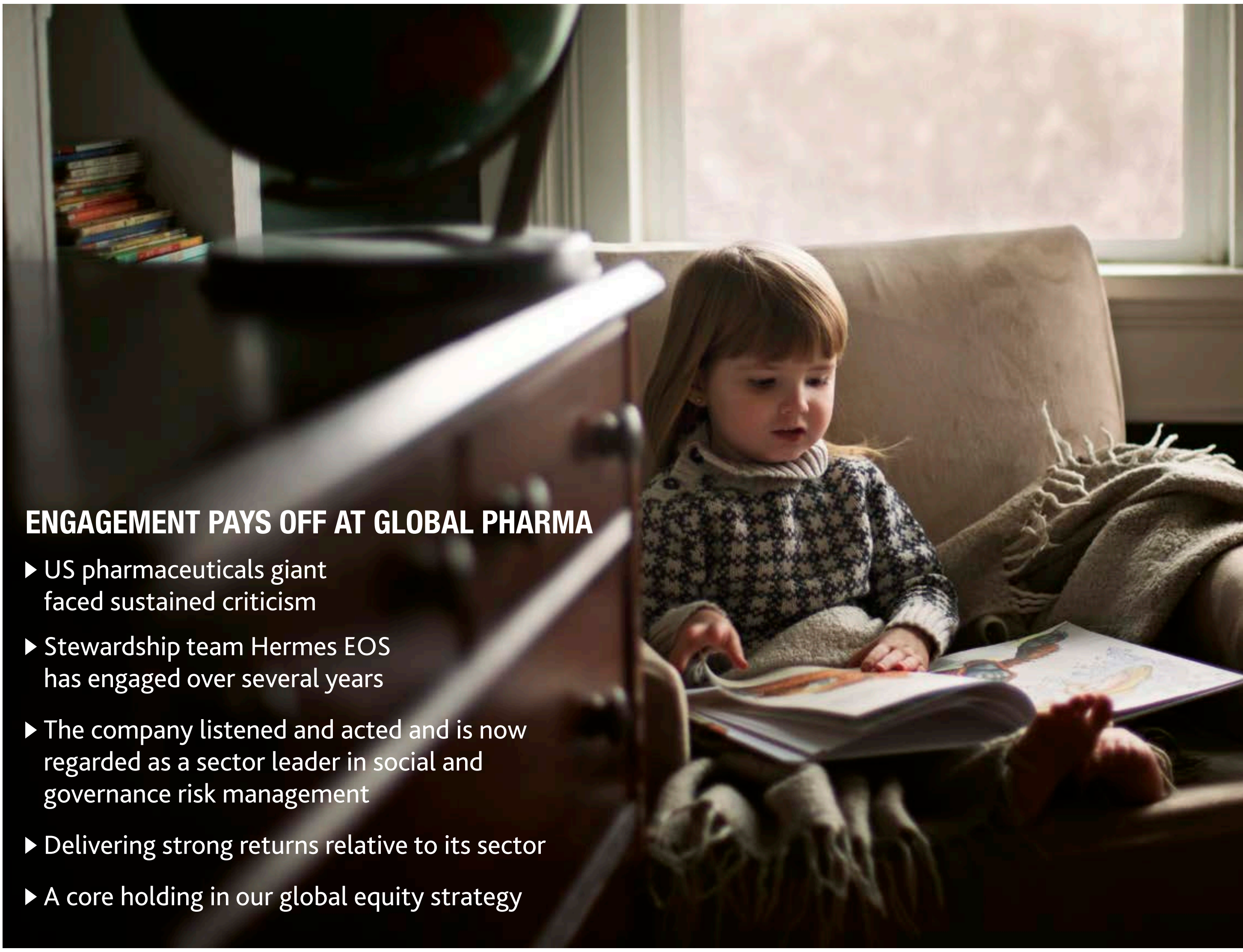
Despite the concerns caused by the Brexit vote, our greatest level of sales came from the UK and Europe, where the Nordic, Swiss and German markets generated the highest revenues. We won our first Italian client, having entered that market at the end of 2015. The UK remains our largest single market in terms of clients and revenues, with high growth potential in both institutional and wholesale channels.

Our global and regional emerging markets strategies generated the highest level of new revenues during the year, with most asset classes contributing positively.



CLEAN ENERGY FROM FALLAGO RIG

- Acquired by our joint venture Hermes GPE LLP in 2014
- 48 turbines with 144 megawatts of generation capacity
- Producing clean energy estimated at 445,800 megawatt hours per annum
- Giving institutional investors access to predictable, inflation linked, long-term returns
- Displacing 190,000tn of CO_2 each year



ENGAGEMENT PAYS OFF AT GLOBAL PHARMA

- US pharmaceuticals giant faced sustained criticism
- Stewardship team Hermes EOS has engaged over several years
- The company listened and acted and is now regarded as a sector leader in social and governance risk management
- Delivering strong returns relative to its sector
- A core holding in our global equity strategy

We are pursuing a two-pronged growth strategy in Asia, selling directly in Singapore, Hong Kong, Korea and Australia, while developing strategic partnerships in Japan and Taiwan.

One of the most sophisticated pension fund markets in the world is Australia, where we are seeing strong demand for mandates that combine active management with active ownership. This is a combination we are uniquely placed to offer thanks to the investment we have long made in our dedicated stewardship team, Hermes EOS.

Demand for stewardship services is growing rapidly elsewhere in Asia, and we were awarded our first stewardship mandate in Japan from PFA, one of the world's largest pension funds. There is increasing interest from asset managers globally for our stewardship services, and we believe this is a significant growth opportunity.

BRAND RECOGNITION

Hermes was little known outside a small group of specialist investors five years ago, when we set out to build a thriving next generation asset manager and disrupt the traditional approach of the investment industry for the benefit of all. It has been highly encouraging, therefore, to receive the recognition of our peers, generate strong media interest and have our views sought by policy makers and regulators around the world. In 2016 alone, we have aided the development of new stewardship codes in Japan and Malaysia, had our views on executive pay referenced by the British Government, been asked to appear on the BBC, Sky, and Bloomberg, and quoted in more than 7,000 individual news articles.

A selection of the awards we were honoured to receive in 2016

OUTLOOK

We see considerable growth potential in 2017, despite the high levels of uncertainty that we expect to persist throughout the year. We will prudently invest, with the following priorities:

1. Increasing our global leadership in active ownership and stewardship
2. Expanding our credit, private markets and ESG capabilities
3. Deepening distribution networks in our core markets of the UK and Europe
4. Building our presence in Asia directly and by forging partnerships with strong regional firms
5. Broadening relationships with our strategic global partners

At all times we will adhere to our principles of seeking holistic returns for our clients, the pensioners and savers who rely on them and the societies in which they and we all live. We will continue to focus on delivering excellent investment performance, while strongly advocating for a financial industry that better serves the needs of society and for companies to improve their environmental, social and governance behaviours. We will continue to strive to help people invest better, retire better and create a better society for all.

Page 18 outlines how the Group delivers value to all stakeholders of the business.

IMPROVING WORKERS' RIGHTS IN BANGLADESH

- Long-running engagement with producers and retailers
- Helping some of the world's largest retailers better understand their supply chains
- Encouraging greater engagement with their suppliers
- Resulting in longer-term contracts, improving working conditions and better pay for workers
- The improvements we seek are not finished and engagement continues

DELIVERING VALUE

Stakeholder constituency	Business activities	Our differentiators
Beneficiaries	Our public markets capabilities include high active share equities, specialist credit and multi asset. Our private markets expertise includes real estate, infrastructure, private equity and private debt. We offer pioneering stewardship services enabling institutional investors to become active owners of public companies through a highly effective group of skilled, multinational professionals. Broad public policy engagement agenda directed towards promoting responsible investment and ownership practices and advocating for a global financial system that operates in the interests of all.	Since our establishment in 1983, we have believed that we have a duty that extends beyond the purely financial. We have been actively engaging with companies for over 20 years.
Clients		The Hermes Pledge of Responsibility expresses the commitment of each of us individually to always put the interests of our clients and their beneficiaries at the heart of what we do.
Environment		Our ownership by the UK's largest corporate pension schemes provides us deep insight into the long-term needs of clients and their beneficiaries.
		In addition to our ISO 14001 accreditation, comprehensive engagement programme with companies and carbon risk-aware investments, we offset our carbon output. We aim for our carbon footprint to be certified as net zero.
Financial system		We look 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. This includes supporting the independent 300 Club, which was established by our Chief Executive Saker Nusseibeh.
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.	We believe that how we behave is as important as how we perform. Both behaviours and performance are set as explicit objectives and our performance review process treats both equally.
Community	We have a strong corporate citizenship programme that is focused on helping the communities in which we live and work.	Our volunteer programmes, which include lunchtime reading sessions with young people or supporting those more vulnerable within the London Borough of Tower Hamlets, keep us connected to our purpose.

Shareholder value

Talented and motivated employees
+
Strong investment returns
+
Extensive stewardship
=
A sustainable and profitable firm

BUSINESS REVIEW

	Business activity		Principal risk arising from activity
Income generation	Management fees are charged based on assets under management multiplied by the fee rate. Our management fees for the year increased as a result of asset inflows, market growth and favourable currency movements. Asset inflows from third-party investors remain in line with targets.	Management fees	Loss of key client risk; Investment performance risk; Investment risk including market risk and geopolitical risk; Business and reputational risk; Credit risk; Operational risk including operating model, change risk, regulatory risk, material error risk, outsourcing and cyber risk
	Performance fees decreased, due to managing fewer mandates with performance fees attached to them.	Performance fees	Loss of key client risk; Investment performance risk; Investment risk including market risk and geopolitical risk; Business and reputational risk; Credit risk; Operational risk including operating model, change risk, regulatory risk, material error risk, outsourcing and cyber risk
	Hermes Investment Management provides sophisticated stewardship services through its specialist team, Hermes EOS, to some of the world's leading asset owners on over £261bn of assets.	Other revenue	Investment risk including market risk and geopolitical risk; Business and reputational risk; Credit risk; Operational risk including operating model, change risk, regulatory risk, material error risk, outsourcing and cyber risk
	Hermes GPE LLP has been a successful joint venture since its inception in 2010. For 2016, the share of profit arising from Hermes GPE LLP was £2.3m.	Share of joint venture profits	Investment risk including market risk and geopolitical risk; Business and reputational risk; Credit risk; Operational risk including operating model, change risk, regulatory risk, material error risk, outsourcing and cyber risk
–			
Expenses	We aim to recruit, train and retain talent in house, as we believe in the importance of people contributing to the success of all aspects of the business. We provide a competitive benefits package to attract and retain the best people.	Staff costs	Employee risk and culture risk; Credit risk; Operational risk including operating model, change risk, regulatory risk, material error risk, outsourcing and cyber risk
	Our wide range of operational functions provides support to all areas of our business and are essential to our success. We have invested in best-in-class systems and people, while ensuring costs are tightly monitored and controlled.	Other expenses	Employee risk and culture risk; Credit risk; Operational risk including operating model, change risk, regulatory risk, material error risk, outsourcing and cyber risk
=			

Profits – Dividends paid out / Taxes to government = **Retained equity re-invested in line with strategic and business objectives of Hermes.**

EMPLOYEES – ATTRACTING AND DEVELOPING TALENT

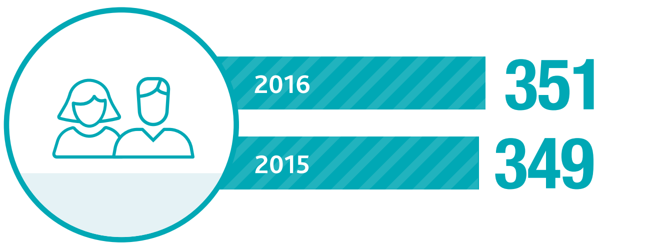
Hermes' success is built on strong values and the contributions of its employees. We aim to build a firm populated by excellent, motivated people, encouraging a culture of positive challenge across the business, for the benefit of our clients.

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 our people can perform at the highest level, feel valued and be able to build upon their knowledge and skills.

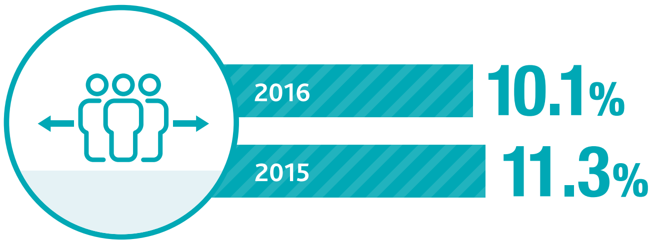
To develop future talent within the business, our Learning & Development team has created a suite of management programmes that span induction, skills and technical development, management development and professional studies.

A workplace that embraces diversity is important to ensuring that we are maximising the potential of our workforce. We recognise that diversity offers real benefits. We employ high-calibre people from many different backgrounds, combining talents and experience to deliver exceptional performance. As a forward-thinking organisation we have been active members of the 30% Club in the UK, supporting the goal of achieving a minimum of 30% women on FTSE 100 Boards through our engagements with investee companies and more than meeting that level ourselves. We recognise the need to maintain the positive momentum and to that end we were pleased to sign up to the Women in Finance Charter in 2016. As part of our commitment to the Charter we have publicly set out gender diversity targets at multiple levels for the Group as well as outlining a range of steps we are taking to support attainment of these targets. Importantly, we believe that diversity encompasses not only gender but also nationality, ethnicity, religion, cultural background, education, sexual orientation, personality differences, experience and skill sets.

No. of employees



(Voluntary) Employee Turnover



Gender Diversity

	2018 target range	% female at 31 Dec 2016
Firm-wide	35-50%	38%
Board (including executive committee members)	30-50%	33%
Senior management level	25-40%	22%

FINANCIAL REVIEW

Statutory Accounts Pre-Tax Profit/(Loss)	2016 £'000	2015 £'000
Turnover	**103,996**	105,477
Administrative expenses	**(99,275)**	(95,489)
Non-operating items	**5,753**	4,583
Statutory Group profit	**10,474**	14,571
Non-recurring performance fee adjustment	**3,600**	(3,600)
Goodwill amortisation	**1,335**	1,335
Regulatory change costs	**–**	(2,950)
Foreign exchange retranslation	**(1,529)**	(630)
Bonus deferral	**(2,026)**	(1,329)
Other	**56**	1,207
Long-term incentive plan	**3,634**	3,123
Underlying profit	**15,544**	11,727
Underlying profit margin	**15%**	11%

Underlying performance

Information provided to the Board is prepared on an underlying basis as this is the way in which to best manage the activities of the Group and measure the performance of the Executive leadership of the business. This result excludes a number of items that are not fully within the control of management. These include goodwill amortisation, bonus deferral adjustments, defined benefit pension charges and foreign exchange retranslation of non-sterling denominated subsidiaries.

Other reconciling items in 2016 include performance fee revenues recognised upon the closure of investment management activities in Singapore in 2015. These fees were recognised on the basis that they would have accrued if the closure of activities in Singapore had not occurred. These fees were recognised in full in the 2015 statutory profit and loss. Regulatory change costs relating to the implementation of MiFID II were recognised in full in 2015 in the management accounts, although these costs will be recognised in the statutory financial statements in 2017.

The Group has achieved a statutory £10.5m profit in 2016 in comparison to £14.6m in 2015. On an underlying basis the Group achieved an increase in profit to £15.5m due to the underlying revenue increase to £111.8m (2015: £105.6m). This is primarily due to greater management fees as a result of inflows, foreign exchange movements and market movements offset by a decrease in performance fees in the year. The Group is now less reliant on performance fees and there are fewer mandates where such fees are earned. Assets under management and advice have increased to £28.5bn from £23.0bn in 2015. The increase is driven by the increase in third-party AUM of £4.7bn, demonstrating the ability of the Group to deliver growth of the third-party business in line with the strategy agreed by the Board and our owner. This reconciliation is shown on page 22. The proportion of revenue from third parties has increased significantly to 59% compared to 52% in the prior year.

Operating costs increased by an inflationary amount of 4% in 2016 while the underlying profit margin has increased from 11% in 2015 to 15% in 2016.

The Group has recognised a total tax charge of £0.8m in 2016 in comparison to a net credit of £5.5m in 2015. The prior year credit is impacted by significant one-off items, such as a tax deduction in relation to the Group's recovery payments to the Group's defined benefit pension plan and implementation of a revised transfer pricing policy.

Financial position

Consolidated net assets as at 31 December 2016 were £54.8m (31 December 2015: £54.5m). The small decrease is mainly due to the actuarial loss on the defined benefit pension scheme offsetting the statutory profit after tax in the year. Cash balances at 31 December 2016 increased to £69.9m (2015: £53.4m) mainly due to the issue of share capital (+£10m), statutory profit for the year (+£9.7m) and pension contributions (-£8.3m).

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 worsened during 2016, principally due to a decrease in the discount rate assumptions that increase the pension liabilities, and is now £10.4m in deficit compared to a £1.6m surplus in 2015 (see note 17 for further information on the pension scheme).

During the second half of 2016 our owners, BTPS, injected £10m ordinary share capital into the Company to offset the negative actuarial movement in HGPS. This reaffirmed the clear commitment from our owners to support Hermes.

The Group has both the financial strength and capital resources to support and execute its strategic plans. The Board and executive leadership remain focused on growing and developing our core business and continuing to increase third-party assets and revenues.

Regulatory capital

The Group continues to maintain a regulatory capital surplus above the 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

Tax Governance

We comply fully with all relevant tax laws and regulations in all relevant jurisdictions in which the Group operates. We seek only to organise our operations, wherever they may be located, within the confines of all relevant local and international tax laws and regulations applicable. We have a transparent working relationship with HMRC and inform them of key transactions prior to implementation to gain certainty or clearance where the position may be uncertain.

The Group complies fully with all current international exchange of information regulations, namely the US's Foreign Account Tax Compliance Act (FATCA), the UK's Crown Dependencies and Overseas Territories (CDOT) regime and the Common Reporting Standard (CRS). We will comply with any amendments to these regulations and the introduction of any new ones.

We monitor tax changes that may affect the Group and plan and prepare for changes, once full operating details have been announced, to ensure a smooth transition and continued compliance. In particular we are monitoring the OECD's Base Erosion Profit Sharing (BEPS) Action Plan and upon implementation of any of the Actions, by way of introduction into domestic legislation (in the UK or where ever the Group operates), we will comply fully with any new tax provisions that may result therefrom.

Assets Under Management and Sub-Advice (in £bn)		
At 1 January 2016		23.0
New funds raised	6.3	
Other redemptions, realisations and withdrawals	(4.3)	
	2.0	
Net new funds		2.0
Market movement		3.5
At 31 December 2016		28.5
% increase in assets under management and sub-advice		24%

Please note the total assets under management figure above for Hermes includes assets under sub-advice of £1.5bn (2015: £1.0bn) and includes £5.4bn of assets that are managed by Hermes GPE LLP, which is a joint venture between Hermes and GPE Partner Limited (2015: £3.7bn).

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 pages 28 and 29; and
- Setting clearly defined risk appetites monitored with specific metrics within set limits.

The most significant risks facing the business are a downturn in 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 that may impact the Group's ability to deliver its strategy and how we seek to mitigate these risks is set out on pages 29 to 31. 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.

INVESTMENT REVIEW

Economic and market review

Despite China's slowdown, political surprises, and the US's second interest rate rise in a decade, global growth in 2016 was not derailed, though it was clipped to about 3.0%. This was the lowest rate since 2009, when China was growing over 9% year-on-year. These factors, however, tempered optimism about whether economic recoveries could continue in 2017, putting pressure on central banks to keep their monetary policies accommodative.

Continued low inflation made this task easier. With wage pressure subdued, key interest rates in the advanced economies were maintained close to record lows – even as oil prices recovered ground as demand proved resilient and oil-exporting countries agreed on production cuts. (Brent crude more than doubled in 2016 from a low of \$26 per barrel to \$56 per barrel.)

This supported the US and UK economies, which pulled themselves further away from the economic downturn of 2008-09. In the US, real GDP stands about 13% higher than pre-crisis and in the UK about 10% higher. Yet, with the euro-zone and Japan barely back to square one since the crisis, there is still only a two-speed recovery. This prompted the European Central Bank and the Bank of Japan to set negative policy interest rates and run extra quantitative easing.

The main surprises in 2016 were undoubtedly political, adding to policy uncertainty. Last June's UK referendum vote to leave the EU will initiate a period of negotiation that could extend beyond the two years assumed under Article 50 of the Lisbon Treaty. Yet, other than sterling's sharp depreciation, the initial market and economic effects proved to be muted.

Moreover, November's election of Donald Trump as US President was taken positively by most growth assets, as speculation that major economies will loosen their fiscal policies took US equity markets to new highs, raised global inflation expectations, and made the near three-decade bull-run in government bonds look strained. Meanwhile, December's rejection by referendum of Italy's Constitutional reforms was another anti-establishment vote.

2017 Outlook

These political surprises could herald significant shifts in economic policy. Growth should still be supported by expansionary measures, but could face an additional challenge. Rather than the financial distrust of 2008-09, financial markets may need to brace for political distrust, with the threat of beggar-thy-neighbour policies – from the US to Europe – rising.

Amid these conflicting growth forces, our economic outlook is based on six core beliefs.

1 First, governments will offer fiscal solutions to add stimulus, try to appease electorates, and take the policy 'baton' back from the central banks. President Trump is looking to reflate the US economy, and austerity in the UK is being deferred again. It makes sense, too, for slower-growth Japan and the eurozone to loosen fiscally using their aggressive QE to cap any offsetting rise in bond yields. Europe's highly-charged political year adds urgency for this.

2 Second, this will come in addition to further monetary expansion. We are nine years beyond the first traces of crisis, yet the central banks still dare not lower the tide of liquidity hiding the sharp rocks beneath. Real policy rates should stay negative, with peak rates lower than before, and central banks unable to turn off their liquidity taps without unintended consequences.

3 Third, should protectionist forces build, inflation will reappear. A risk is that President Trump invokes 'Super 301' to impose trade tariffs without Congressional approval. But, the inflation it encourages could be the 'wrong sort' – cost push, led by tariffs, goods and labour shortages, rather than demand-pull. In which case, central banks could 'turn a blind eye' if their economies stagflate. Under these conditions, the inflationary flame should snuff itself out without an aggressive rise in interest rates.

4 Fourth, China has the policy tools to soften its landing. Its main macro dilemma is supporting growth, yet minimising a boost to the housing market. There, affordability in the main cities has deteriorated faster than in other world financial centres. The deflationary and leveraging risks need watching, and the People's Bank of China would have to delve into its massive $3trn reserves to cushion any indirect blow of a 'trade war' on China's balance sheets.

5 But, fifth, for those non commodity-exporting emerging markets with high exposure to short-term US dollar debt and/or foreign saving needs, the outlook would appear less rosy. For these countries, vulnerabilities exist such as via a stronger US dollar. But, for others, external debt-ratios are lower, with fewer currency pegs to have to protect, and, where domestic debt climbs, they too could run QE.

6 Finally, without convincing recoveries, any contagion, unlike 2008, may be political rather than financial. With elections coming in France, Germany, The Netherlands, and probably Italy, there may be little sympathy for a quick, condition-free UK Brexit deal. The UK's exit negotiations could take longer than the three years needed in 1982-1985 by Greenland.

In which case, for financial assets, reflation trades have been justified. Yet the potential for further political disruption, protectionism, cost inflation, and thus dissipating growth suggest that 'lower for longer' on interest rates and the search for yield will probably persist.

INVESTMENT PERFORMANCE AND STEWARDSHIP

Over the longer term Hermes has continued to demonstrate its ability to deliver strong investment performance relative to both benchmark and peers.

For 2016, 44% of strategies outperformed their benchmarks. For those strategies that have a three-year track record, 74% outperformed their benchmarks as of 31 December 2016. In turn, Hermes' three-year asset weighted information ratio was 0.74.

For 2016, 50% of measurable strategies were first quartile and 89% above median. Over three years 60% were first quartile and 93% above median.

Portfolio analysis

As part of our commitment to engagement with investee companies as a means of supporting the delivery of holistic returns, we engaged with a percentage of the assets under management in the strategies listed below. This is shown in brackets after each strategy.

Asia ex-Japan

In 2016, the performance of the strategy exceeded its benchmark by 3.9%, with the since inception annualised relative return also 10% above benchmark. The overweight position and stock selection in South Korea was the main contributor to relative performance. The main detractors to performance were the underweight position in Taiwan and negative currency effect from China. Relative to peers, the strategy has been first quartile in each year since inception. (42% AUM engaged).

Global Emerging Markets

In 2016, the main strategy underperformed its benchmark by 1.8%. The annualised relative return since team inception is 5.2% above benchmark. Relative to peers the strategy remains first quartile over three years, five years and since inception. Currency effect was one of the main detractors to relative performance, notably in the Emerging Asia region. Stock selection in Brazil and Russia also contributed to the relative underperformance. On a positive note, stock selection in China and Taiwan was strong, therefore reducing the negative currency effect attributed to China. (43% AUM engaged).

Global Equities

In 2016, the core Global Equity and Screened ESG strategies both exceeded their benchmarks by 1.8%, with the since inception annualised relative returns also remaining strong at 1.4% and 2% above benchmark respectively. The Global Equity ESG strategy underperformed its benchmark by 1.3% in 2016, however the since inception annualised relative return remains 3% above benchmark. In the main Global Equity strategy, key drivers of performance came from the US, with additional contributions from Europe, driven by stock selection in all cases. The main detractors to relative performance came from stock selection in the UK and Italy. The main Global Equity strategy remains first quartile over one, three, five year and since inception periods. (56% AUM engaged).

Multi Asset

In 2016, the strategy outperformed the UK RPI by 2.8%, with the since inception annualised relative return 0.2% above benchmark. The matching portfolio was the main contributor to performance for the year, whereas the enhancing portfolio detracted slightly. In terms of assets, the top contributors for the year were Global Bonds and Inflation Breakeven, whereas the main detractors were Equity Indices and Risk Factors. Relative to peers, the strategy ranked in the second quartile on a one-year basis.

European Equities

In 2016, all three European Equity strategies underperformed their respective benchmarks after a challenging fourth quarter that saw a sharp rotation from growth towards value. European Alpha underperformed by 2.8%, Europe ex-UK, 1.6% and Eurozone 2.1%. Even with the underperformance in 2016, since inception annualised relative performance remains positive with European Alpha 2.7%, Europe ex-UK 2.9% and Eurozone 0.8% above their respective benchmarks. Relative to peers all three strategies are above median on a since inception basis. In the main Alpha strategy, stock selection was the main detractor to relative performance, notably in Industrials and Materials. The main positive contributors came from stock selection in the Financials and Consumer Goods sectors. (55% AUM engaged).

US SMID & Global Small Cap

In 2016, all three strategies exceeded their respective benchmarks, with US SMID 3.2%, US All Cap 0.7% and Global Small Cap 0.6% ahead. With the positive performance in 2016, the since inception annualised relative performance for all three strategies remains strong, with US SMID 1.9%, US All Cap 2.2% and Global Small Cap 2.3% once again ahead of their benchmarks. Relative to peers all three strategies are first quartile on a since inception basis. For the US SMID and Global Small Cap strategies, stock selection accounted for the majority of the outperformance, notably Health Care and Technology. Financial Services and Consumer Staples were the main detractors of relative performance. The US All Cap strategy main drivers of performance came from Technology and Materials & Processing, whilst the main detractors of performance were the Health Care and Financial Services sectors. (11%-13% AUM engaged).

Credit

Overall, 2016 was another strong year for credit markets globally and this was evident in the strong absolute performance of our credit strategies, with High Yield returning 11.6%, Investment Grade 5.9%, Multi Strategy 10% and Absolute Return 3.4%. Even though the main Global High Yield strategy underperformed its benchmark by 3.4%, the strategy is still positive on a since inception annualised basis 0.9% above benchmark. Global High Yield also continued to deliver top-quartile performance relative to its peers over three year, five year and since inception periods. Key drivers of the returns across the range were our quality bias, whilst avoiding distressed energy (this was the primary detractor in the Global High Yield strategy). Our favouring of US and emerging markets over Europe aided returns, as did our pro-cyclical sector positioning. (36% AUM engaged).

562 companies engaged on a range of ESG issues in 2016

↓

20% increase on 2015

Real Estate

For Real Estate UK Core and International strategies, 2016 relative performance was 2.0% and -0.5% respectively. The Hermes Property Unit Trust for the full year 2016 outperformed its benchmark by 2.6%, placing it top quartile within the Other Balanced Property Funds Index and over the five and ten-year periods achieved top spot.

The Real Estate Debt strategy has outperformed its target, three-month Libor +2%, by 1% in 2016 and 0.8% on a since inception annualised gross internal rate of return basis. The strong performance of the strategy can be attributed to all loans achieving interest rates in excess of the target.

RESPONSIBILITY

During 2016, we engaged with 562 companies on a range of ESG issues – a 20% increase on 2015. Encouragingly, of the 336 companies where we had set explicit objectives, we were pleased to have made progress on just under half during the year (45%). In total, we had 1,408 interactions (including meetings, calls and letters) with companies and voted at 9,286 company meetings, voting against management at 47.7% of meetings (up slightly from 2015). In addition to engaging directly with companies, we also carried out nearly 283 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 founded by our Chief Executive.

During the 2016 voting season there were a number of high profile companies that were on the receiving end of shareholder opposition to their pay policies or practices. Reflecting on the lack of meaningful change over recent years, we published a new paper clarifying our expectations around the issue and setting out a series of proposals for improvements in order to bring about greater simplicity and alignment and ultimately enhance public confidence. We also continued to build on our intensive engagement efforts with relevant companies on climate change, which this year culminated in the presenting of shareholder resolutions at the AGMs of Anglo American, Glencore and Rio Tinto. We also co-filed a shareholder resolution at Chevron and supported a similar resolution at ExxonMobil, requesting disclosure of its asset portfolio resilience under low-carbon scenarios. Pleasingly, the momentum for stewardship continues to grow globally, as evidenced by the launch this year of stewardship codes in Brazil, Taiwan and Singapore. Hermes actively supported the development of each of these new Codes and

Pleasingly, the momentum for stewardship continues to grow globally, as evidenced by the launch this year of stewardship codes in Brazil, Taiwan and Singapore.

believe such initiatives will make an important contribution to the development of the stewardship activities of institutional investors around the world and in turn enhance the corporate governance of companies in which they invest. The positive change being generated by the 2014 introduction of such a Code in Japan is encouraging, and we were pleased this year to be appointed by the Pension Fund Association (PFA) of Japan to develop and implement its stewardship activities.

Internally, we continued to embed the awareness and consideration of ESG issues alongside the insights gleaned from engagement activity within our investment processes and fund performance monitoring. In July we published a report, "Delivering Holistic Returns", which outlines our approach of how we put it into practice. Pleasingly, this year saw significant increases to the engagement coverage of some of our funds as well as enhancements made to the measurement of ESG risk and the carbon footprints of each fund. As a result, the interaction between our engagers, analysts and portfolio managers continues to increase to the benefit of our clients and their beneficiaries. This positive momentum on further embedding commitment to responsibility was mirrored across our various capabilities, including infrastructure and private equity. In real estate we expanded the reporting within our annual Responsible Property Investment report to provide more specific qualitative and quantitative details on the positive social, economic and environmental impacts of some of our investments. We achieved a further 11% year-on-year reduction in CO_2 emissions on a like-for-like basis – the ninth straight year that such a reduction has been achieved.

Corporate Citizenship

At Hermes, we are particularly conscious that we should as a company strive to meet the expectations that we have of others. In addition to our behaviours as individual employees and the delivery of strong investment performance for our clients, we also believe we should lead by example as a firm and strive therefore to make a difference, not only through our investment solutions, but in how we contribute to both the financial system and wider community.

In evidence of our commitment, we were proud to achieve the revised ISO 14001 requirement this year. Similarly, during 2016, in recognition of the value of a diverse workforce and in particular the benefits of having a diversity of experience amongst senior management, we became a founding signatory to the Women in Finance Charter and have set ourselves firm-wide, board level and senior management level gender diversity targets.

Our activities in the local community continued to be supported by our staff. These projects include lunchtime reading and numeracy sessions with young people, renovating local schools and gardens, and 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. In addition, this year a new Hermes diversity and inclusion group (Unity) successfully implemented a timetable of events and workshops covering a wide range of diversity, inclusion and wellbeing topics, which included unconscious bias awareness training for staff and an inaugural men's health and wellbeing day.

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 the Community
Hermes is an active member of Business in the 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.

RISK MANAGEMENT

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:

1 Risk and Compliance Executive

2 Business Development Forum

3 Hermes Strategy Group

4 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 that 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.

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

Hermes' key risk exposures are grouped according to:

- Business risk
- Operational risk
- Market and financial risk (includes capital, credit risk, liquidity risk)

The following table summarises the key business risks and mitigating actions. The listing is for illustrative purposes only and is not a ranking of materiality.

Risk	Mitigants
1 – Strategy and culture (business risk)	
The risk that Hermes does not meet its long-term strategic objectives or operates in a negative cultural environment.	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. 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. 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 the back of the report for the Hermes Pledge.
2 – Loss of key client/stakeholder support (operational risk)	
This risk relates to the loss of a key client or support from a key stakeholder (BTPS) and, therefore, having a detrimental impact on the Firm.	This risk is mitigated by the Firm growing its third-party offering (as demonstrated on pages 9 and 10) and diversifying its client base, whilst continuing to meet the requirements of its clients and stakeholders.
3 – The operating model (operational risk)	
The risk that the operating infrastructure is not fit for purpose, is inefficient or not scalable, failing to support strategic plans. The risks that technology systems and support are inadequate or fail to adapt to changing requirements.	Operational support to the business is based on middle office processes and controls that are performed in-house and back office processes undertaken by third-party service providers. The Operations department oversees that back office operations perform in accordance with expectations and to defined tolerances. Hermes relies on technology and qualified professionals to maintain its infrastructure and invests in IT accordingly. A robust governance structure exists with Board-level committees, e.g. Risk & Compliance Committee, Audit Committee, to review priorities, progress against plans, risks/issues etc. Operational policies and procedures are reviewed and updated periodically and available to all staff.

Risk	Mitigants
4 – Change/M&A risk (operational risk)	
The risk that Hermes fails to deliver a major change initiative in a controlled manner or the risk that the initiative does not deliver expected benefits. Failure for new ventures to align with the culture and vision of Hermes.	There is in place a comprehensive Change Governance process including policies, procedures and Senior Management oversight directly and/or via applicable Board/ Management committees.
5 – Employee risk (operational risk)	
The risk that key staff across the business leave or are not adequately motivated in their role as well as excess reliance on a small number of key staff members (key man risk).	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.
6 – Regulatory & legal risk (operational risk)	
The risk of regulatory or legal 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. This includes the risk that new regulations, or changes to the interpretation or implementation of existing regulations, affect the Firm. This risk includes the risk that tax requirements are not understood, implemented and complied with.	Hermes relies on its employees, with support from the Compliance, Risk, Finance, Tax and Legal functions, to consider carefully the obligations the Group assumes and compliance with them. Hermes maintains compliance procedures across the Group and compliance with relevant regulatory requirements is monitored in accordance with a risk-based programme. 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.
7 – Material error/breach risk (operational risk)	
The risk of a material error and/or investment mandate (guideline) breach.	A strong control environment exists at Hermes and 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. Formal Errors and Breaches process is in place, which includes reporting and escalation, investigations, etc to ensure that lessons are learnt/additional controls are implemented to prevent a recurrence. Root cause analysis reporting undertaken for material matters. Insurance cover is in place to cover certain specified significant errors, breaches, regulatory, legal, conduct and other types of risk issues. Internal audits and external audits provide an extra layer of assurance.
8 – Outsourcing (operational risk)	
The risk that outsourcing plans are not aligned to the wider strategy or that outsourcers fail to deliver the expected benefits/services.	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.

Risk	Mitigants
9 – Cyber risk and business continuity (operational risk)	
Internal or external misconduct potentially causing loss to the company and/or compromising Hermes' reputation. E.g. Unauthorised/fraudulent activity occurring, the risk that products are misrepresented to clients, trader operating in an inappropriate manner.	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, all teams have a Business Continuity Plan and an Incident Management Team (IMT) has been established with regular testing. Regular tests are planned in conjunction with IMT and in accordance with the policy timeframe. A register of issues is kept and appropriate actions are taken to address matters in a in a timely fashion.
10 – Investments (market and financial risks)	
The risk that portfolios will not meet their investment objectives, adversely affecting levels of new business or fee income.	Investment teams adhere to clearly-defined investment processes to seek suitable investment opportunities and manage the inherent market risks in accordance with clients' risk appetite and investment parameters. The Hermes Investment Office independently monitors risk and performance (through independent systems and processes) and ensures the rigour of team strategies. The Hermes Investment Risk Framework provides monitoring and challenge of investment risks and performance across teams.
11 – Geo-political (market and financial risks)	
Risks associated with political matters that could impact the governmental system and damage the economy and, therefore, impact Hermes negatively (e.g., reduced earnings). 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.	Hermes offers a diversified and broad product range that provides clients with solutions tailored to a variety of market conditions and serves to diversify individual market dependencies. Scenario analysis and impact is undertaken independently by the Investment Office to assess the performance of portfolios under a stressed environment. The Board has a limited appetite for market risk; therefore Hermes only holds proprietary investments for hedging purposes with the exception of nominal seed capital. These investments are only used to hedge the valuation movements on bonuses (co-invest) that are linked to the value of Hermes' funds.

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

S Nusseibeh
Chief Executive Officer
31 March 2017

DIRECTORS

The Board comprises the following Directors:

D Stewart* (Chairman)

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).

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.

I Kennedy

Ian, who was appointed as an Executive Board Director in 2015, is Hermes' Chief Operating Officer and a member of the Executive Committee.

Immediately prior to joining Hermes, in 2012 Ian established InvestMe Financial Services LLC, one of the earliest firms in the UAE to receive an investment advisory license by the Securities and Commodities Authority (SCA) in Abu Dhabi.

Having worked in the City since 1992 in various houses as an accountant, and subsequently risk and control manager and Finance Director, Ian became COO for the UK wealth management and private banking division of Fortis, ultimately acting as interim CEO. After leading the sale of the business to BNP Paribas in 2009, Ian became Chief Operating Officer and Chief Financial Officer of BNP Paribas Wealth Management UK.

Ian graduated from King's College, University of London with a BSc in Biochemistry, and qualified as a chartered accountant with Arthur Anderson & Co.

W McClory*

Billy was appointed to the BTPS Trustee Board on 1 September 1997 and joined the Board of Hermes Fund Managers as a Non-Executive Director in August 2010. He is currently the senior Non-Executive Director of Hermes Fund Managers Limited. Billy was employed by Post Office Telecommunications from 1968 to 1978. He is a former national officer of the CWU and its predecessor unions the Civil and Public Services Association and the National Communications Union (NCU). He was responsible for negotiations on pension matters in the telecommunications and financial services sector and was the lead officer for pension matters for the BT Unions. He is a Trustee of the NCU Staff Superannuation Scheme and was chair of its trustee board until 2011. He is a former trustee of the BT Retirement Plan. Billy is a member of UNITE (formerly the National Federation of Occupational Pensioners).

H Steel

Harriet is Head of Business Development, a member of the Executive Committee (ExCo) and an Executive Board Director. She joined the firm in 2011 with responsibility for Sales, Client Service, Marketing, Communications and Product Strategy. Under her leadership, Hermes has built a fast-growing and profitable third-party business in which assets under management for external clients have tripled, and revenues grown from 15% to 60% of the total. Appointed to the Board of Hermes in 2013, Harriet became the company's first female Executive Director.

Harriet's career in the City began in 1990 after graduating from Princeton University with a degree in architecture. She joined the global trading team at Bankers Trust, initially trading currency options and subsequently holding senior derivatives sales roles in Paris, London and New York before joining Morgan Stanley's fixed income group in 1996. In 2003 Harriet established Portico Advisors, an asset raising and marketing advisory firm for alternative investment managers, including hedge funds, private equity and real estate strategies, which she ran until joining Hermes.

Harriet acts as a mentor to female executives at Hermes, encouraging them to fulfil their potential and providing practical insight and guidance on how to achieve success in the City. Harriet is a regular commentator in the print and broadcast media on business, economic and diversity issues and, for the last three years, has been recognised as one of the top 100 women in European finance by *Financial News*.

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, Senior Independent Director and Chairman of the Audit Committee at TR Property Investment Trust Plc, and Non-Executive Director and Chairman of the Audit and Risk Committee of Kames Capital 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.

The following Directors were appointed to the Board during the year: **C Claydon (5 May 2016)**

The following Directors resigned from the Board during the year: **P Spencer (31 March 2016), C Claydon (31 December 2016)**

The following Directors resigned from the Board after the year: **K Matthews (31 January 2017)**

Paul Spencer (resigned during the year), Catherine Claydon (resigned during the year) and Billy McClory do not meet the definition of independence in the UK Corporate Governance Code as they serve as Trustees of the BTPS, the Group's ultimate parent company; each of the other Non-Executive members of the Board and each Committee are considered independent.

* Non-Executive

REPORT OF THE AUDIT COMMITTEE

MEMBERSHIP

The Audit Committee currently comprises two Non-Executive Directors, David Watson (Chairman) and Billy McClory. During the year the following Directors served on the Committee: Kathryn Matthews (resigned 31 January 2017), David Stewart (resigned 31 March 2016) and Catherine Claydon (appointed 5 May 2016, resigned 31 December 2016). 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.

An annual review of the Committee's Terms of Reference is undertaken to ensure that they are relevant and correct.

David Stewart and Catherine Claydon did not attend some meetings due to existing conflicts.

Committee attendance during 2016		
Member	**Number of meetings eligible to attend**	**% of meetings attended**
David Watson	6	100
Kathryn Mathews	6	100
Billy McClory	6	100
David Stewart	3	67
Catherine Claydon	3	67

WORK OF THE COMMITTEE DURING 2016

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;
- monitoring implementation of actions arising from the review of the external effectiveness of Internal Audit;
- 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;
- consideration of the audit matters for the year and approval of actions required in respect of disclosures, statutory guarantees and deed of support from BTPS;
- consideration of the remuneration report disclosures;
- active monitoring of the defined benefit pension scheme, regulatory capital and capital funding requirements; and
- review and approval of the request for further regulatory capital from BTPS.

EXTERNAL AUDITOR TENDER PROCESS

During the period the Group undertook an external audit tender, in conjunction with its parent, BTPS. Deloitte has been the auditor of BTPS and Group companies since 1 January 1993 following the amalgamation of the British Telecommunications Staff Superannuation Scheme and BT New Pension Scheme. Despite there being no specific rules for mandatory audit rotation for such entities, the Boards of the Group and BTPS concluded they would follow the rules that are applied to large PLCs (tender every 10 years and maximum term of 20 years).

The selection process was run jointly by BTPS and the Hermes Group (HFML) with a Working Group consisting of the Chairmen of both the BTPSM and HFML Audit Committees supported by a Tender Team made up of representatives from BTPSM and HFML. The Working Group made a recommendation that received approval from the BTPS and Hermes Audit Committees and the BTPS Trustees, who in turn are recommending that other independent Boards and joint ventures within the BTPS Group consider and approve the appointment.

Formal approval of the new auditor appointment will occur after the resignation of the current auditor, which is expected to take place after the sign-off of the final Annual Report and financial statements. For HFML, the resignation of Deloitte is expected after the signing date of this report.

EVALUATING PERFORMANCE OF THE COMMITTEE

Internal audit undertook work on the governance framework across the Group during 2016. This examined the governance framework of the Board and committees, whether meetings are regular, agendas are followed and actions are taken and followed up. Also considered was the "Tone at the Top" and the engagement of the Risk team in strategic decision-making information.

REPORT OF THE RISK AND COMPLIANCE COMMITTEE

MEMBERSHIP

The Risk and Compliance Committee ("the Committee" or "RCC") currently comprises three Non-Executive Directors: David Stewart (Chairman), David Watson and Billy McClory. During the year the following Directors served on the committee: Kathryn Matthews (resigned 31 January 2017) and Catherine Claydon (appointed 5 May 2016, resigned 31 December 2016). 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, Strategic Compliance Director and Head of Risk 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;

Committee attendance during 2016

Member	Number of meetings eligible to attend	% of meetings attended
Kathryn Mathews	6	100
Billy McClory	6	100
David Stewart	6	100
David Watson	6	100
Catherine Claydon	4	75
Paul Spencer	1	100

- 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 with 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 2016

Major topics considered by the Committee during the year were:

- assessment of Governance Structure and Terms of Reference;
- approval of the Risk Appetite Statement and Risk Management Framework;
- approval 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 potential Brexit risks, notably counterparty credit risk;
- consideration of IT Security – Information Security (sometimes referred to as 'cyber');
- evaluation of 2016 Risk Plan;
- review of work done to strengthen the transaction reporting process;
- review and challenge of reports received from internal audit, regulators, risk and compliance functions;
- review of the AAF (Audit and Assurance Faculty) report;
- review of reports on Conduct Risk following introduction of the Conduct Risk Framework;
- review of potential risks and regulatory capital implications associated with the Hermes Group Defined Benefit Pension Scheme; and
- review and debate of reports received from regulators and the Risk and Compliance functions.

REPORT OF THE REMUNERATION COMMITTEE

MEMBERSHIP

The Remuneration Committee is constituted as a committee of the Board of Hermes Fund Managers Limited. Membership of the Remuneration Committee is formed by the Chairman of Hermes and other Non-Executive Directors who are appointed in line with the business needs of the Group.

The Remuneration Committee currently comprises three Non-Executive Directors: Billy McClory (interim Chair), David Stewart and David Watson. During the year the following Directors served on the Committee: Kathryn Matthews (resigned 31 January 2017), Paul Spencer (resigned 31 March 2016) and Catherine Claydon (appointed 5 May 2016, resigned 31 December 2016).

The primary focus continues to be centred on advising the Board of Directors on remuneration matters. This advice takes shape through policies and plans that are designed to motivate and retain high-calibre Executive Directors, senior management and staff.

The report has placed an increased emphasis on remuneration disclosure in 2016, ensuring a continuous improvement in both the transparency and detail of the Group's remuneration reporting.

Transparency

The transparency of the disclosures mirrors public company disclosure, disclosing pay for Executive Directors and setting this in the context of the firm's performance. This aligns the principles with Hermes' recommendations for public listed companies, and this is discussed in detail in the report.

Stakeholder alignment

The Group believe that remuneration must be aligned with long-term performance, reflect strong risk management and encourage a responsible culture with regard to both investments and relationships with key stakeholders. It is important that the remuneration framework is clear, understandable and achievable in order to motivate and retain employees and ensure alignment with the strategic business targets agreed with the Shareholder. This is achieved 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 metrics used as part of the annual appraisal discussion. These have been reinforced by the introduction of The 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 employees with the purpose is set out on the following page.

Strategy

Hermes' ongoing strategy is to build a world-class investment management business that delivers outstanding holistic return outcomes for clients and their beneficiaries, attracts strong inflows of third-party assets and continues to meet and exceed the financial objectives. Hermes will continue to review remuneration policy in anticipation of this growth and with the changing shape of the Company. Individuals' remuneration will continue to be linked with the success and long-term growth of the Hermes Group.

Reward strategy principles

As a private firm with a single shareholder, the principal-agent issues present in the public listed company sector are less prominent for Hermes. Indeed, representatives from the owner sit on the Board and the Remuneration Committee and are directly involved in developing and approving executive remuneration policy and outcomes.

In 2016 Hermes published a paper on the topic of executive pay, intended to provide further clarity as to how Hermes expects remuneration to be structured and applied in practice by publicly listed companies. Within the paper it diagnoses a series of problems with the existing remuneration structures that is prevalent across the listed sector. The Hermes belief is that pay structures have become too complex, fail to adequately connect pay awards to long-term value creation and create an excessive focus on share price management. The Group argues that there is insufficient accountability along the length of the ownership chain, in particular at board level, with respect to pay outcomes.

Notwithstanding, being a privately owned company, Hermes is aligned to those principles we have communicated to listed companies. There is a key focus on strategic delivery (we do not have a share price to distort focus) and rewarding both "the how" as well as "the what" in terms of operational and financial performance, and through representation on the board there are clear lines of accountability to the owners.

Hermes remuneration philosophy and principles

The Group's philosophy is to reward individual contribution, as demonstrated by the delivery of long-term sustainable results that are aligned with the business strategy, values and behaviours and which serve the best interests of clients, their beneficiaries and the owner, while enabling the business to maximize its potential.

Through focusing on long-term awards, the incentive pay strategies encourage employees to act like long-term shareholders and support the performance of the firm and its culture in order to create a sustainable business, while discouraging excessive risk taking. The risk appetite of the Group is closely monitored, and further discussed in the Risk Management section of the Strategic Report. Individual and organisational performance is transparently and rigorously assessed against a combination of financial (multi-year) and non-financial (multi-year) KPIs in order to determine the appropriate total remuneration that will attract and retain key talent.

The following page demonstrates how the Hermes embodies these key principles.

Remuneration Principles promoted by Hermes	Specifics	How are they implemented at Hermes?
Shareholding Executives should make a material long-term investment in the company's shares	Long-term awards for senior management that encourage long-term success An approved ex-ante total cap on overall pay Commitment to not pay more than is necessary	Our Long Term Incentive Plan operates as a profit-share and is designed to encourage profit growth over a 4-year profile. It gives the recipients the right to share in the growth of the Group in the fourth year following the award grant. We do not operate a cap for individual pay, however the bonus pool is capped at 27% of revenues for 2016. Relative spend on pay is also monitored. Remuneration is reviewed annually and benchmarked to the external market. The Group will pay competitive and attractive, but not excessive, total remuneration in order to achieve outstanding performance.
Alignment Pay should be aligned to the long-term success and the desired corporate culture	Strategic performance metrics (rather than total shareholder return) to dominate incentive schemes Assessment of performance with use of relevant metrics focused towards impact on stakeholders To promote a sound and aware approach to risk management that is aligned with the firm's risk appetite, client needs and corporate objectives Tail risk built into pay structures	A proportion of key employees' deferred remuneration is delivered as fund awards, which are notional investments in funds managed by the Group, thereby aligning the short- and long-term interests of employees with our clients and stakeholders. Individuals are assessed on a combination of financial, technical and behavioural key performance indicators. Non-financial metrics include demonstration of Hermes' corporate behaviours as outlined in the Hermes Pledge. Individuals will be highly rated if they perform successfully while embodying the Hermes behaviours as conveyed in the Hermes Pledge. Further detail is discussed later in the report. The Remuneration Committee works closely with the Risk Committee, to ensure that remuneration principles are governed by a sound and risk-aware management system. During the vesting period for deferred compensation, awards are subject to the malus clause in the plan rules. After vesting, awards remain subject to clawback.
Simplicity Pay schemes should be clear and understandable for both investors	To deliver reward programs that are transparent, simple to administer and affordable to the Group	We have taken steps in recent years to simplify pay arrangements, with two complementary incentive schemes. The discretionary bonus rewards past performance and includes a deferred portion for ongoing alignment, while the LTIP provides a forward-looking motivational tool to deliver a sustainable business.
Accountability Remuneration committees should use discretion to ensure that awards properly reflect business performance	Ownership and accountability for pay outcomes, including greater use of discretion Publication of pay ratio	Our Remuneration Committee is consistently enhancing the disclosures we provide within the annual remuneration report. Total Variable Compensation is determined by the Remuneration Committee and recommended to the Board. Revenue and profit metrics are used for bonus pool funding. Profit acts as a hurdle that, unless cleared, will require the Remuneration Committee to review the bonus pool size – in light of its duties to the shareholder and the Board. The Remuneration Committee has overall discretion to adjust 100% of discretionary awards and has adjusted awards both up and down over recent years. We have this year disclosed our relative spend on pay and the ratio of total CEO pay as compared to median worker pay. Our CEO and fellow Executive committee members hold regular events in which they make themselves available to answer any questions from staff.
Stewardship Companies and investors should regularly discuss strategy, long-term performance and the link to remuneration	Greater quality of engagement along the ownership chain	Our owner is represented on our Board and the Remuneration Committee, ensuring there is clear connection between us as a firm, our owner and our owner's underlying beneficiaries.

OUTLINE OF INDIVIDUAL PAY ELEMENTS OF THE GROUP

Individual pay elements support our purpose and align interests with clients and stakeholders

Fixed pay elements – base salary, retirement and other benefits

Provides competitive fixed pay at a level that reflects market compensation for the role. Applies to all employees.

- Assists employees with retirement and provides insurance coverage and other corporate benefits
- Determined by experience, duties and scope of responsibility, as well as internal and external market factors
- Reviewed annually, Remuneration Committee considers, challenges and approves the budget requested by Executive Committee
- Proposals are approved in accordance with the Remuneration Committee Terms of Reference

Bonus

Encourages all employees to deliver high levels of performance and demonstrate behaviours that are in line with the corporate values, thus aligning the interest of shareholders, investors and stakeholders.

Structure:

- The discretionary bonus scheme is for all eligible employees. Eligibility is based on service conditions
- Individual awards are based on an assessment of an individual's performance and behaviours with reference to firm performance, team performance and market intelligence
- All bonus allocations are reviewed by the Executive Committee and the top 50 reviewed by the Remuneration Committee
- Based on the size of the bonus, an element is deferred and co-invested. Both the upfront and deferred elements of the bonus are delivered in cash, with the deferred portion co-invested in investment strategies to ensure alignment of interest. (See next section for more detail.)
- Leaver provisions: Good and bad leaver provisions apply to the awards

Performance & Adjustment:

- The company-wide bonus pool is based purely on company performance
- Performance measures are based on revenue, profitability and margin. If the performance measures are not sufficiently met, the pool size is then determined by the Remuneration Committee's approval. Furthermore, Remuneration Committee and Executive Committee are not obligated to fully distribute the bonus pool and should adjustments be required (risk or otherwise), they have the discretion to impose any relevant adjustments. 100% of the award is subject to adjustments
- The Risk Committee advises the Remuneration Committee about any considerations the Remuneration Committee should take into account

Co–investment/bonus deferral

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.

Structure:

- The deferral scheme applies to all eligible employees whose bonus is £50,000 or greater
- Awards vest over three years in equal tranches and the performance period does not restart each year
- Over the performance period, the underlying award notionally tracks fund(s) performance, and is adjusted in line with the performance of the fund(s). For the sake of clarity, it can be adjusted upward or downward
- For investment professionals at least 50% of their deferred award is notionally co-invested into the fund(s) they manage. The remaining 50% can also be notionally co-invested into the funds they manage, or the employee can choose to notionally co-invest in a basket of funds from across the Company. There is no retention period
- Non-investment professionals must notionally co-invest 100% of their deferred bonus award into a basket of funds
- During the vesting period for deferred compensation, awards are subject to malus. After the vesting, awards remain subject to clawback
- Upon vesting, the change in performance during the performance period is applied to the vesting tranche. This mechanism is applied when performance increases, as well as decreases

Individual pay elements support our purpose and align interests with clients and stakeholders

Long-term incentive plan (LTIP)

Aligns the interests of employees to those of the shareholder by encouraging employees to grow profits over the long term through sustained performance. The LTIP operates as a profit-share and is designed to encourage profit growth over the four-year grant period. It gives the recipients the right to share in the growth of the Company in the fourth year following the award grant.

Structure:

- Participants are selected at the discretion of the Executive Committee and approved by the Remuneration Committee on the basis of an employee's projected ability to influence the company over the performance period, and can be in any part of the Company. Eligibility is reviewed on annual basis
- Profitability is measured following the close of the fourth year of the award; the award is calculated on a proportional basis for all participants in that year's allocation
- The award vests as a single amount after four years and is subject to plan rules being fulfilled
- The vested award is delivered to the recipient as a cash payment
- Upon vesting, participants have no further right to the awards. There is only one annual allocation per year

Performance & Adjustment:

If a decision is taken by the Committee to restrict an award (to any degree), it will prevent an award from being paid to the employee.

Interim Profit Participation Plan (IPPP)

Transitions participants in the previous Equity Participation Plan to the LTIP and aligns the mid-term interests of employees with clients and stakeholders. This strategy gives the recipients the right to share in the growth of the Company in each year following the award grant until the LTIP plan vests.

Structure:

- Participants can work in any part of the Company
- Profitability figures are measured following the close of each performance year; then the award is calculated on a proportional basis for all participants in that year's allocation
- The awards vest annually over three years and is subject to plan rules being fulfilled
- Upon vesting, participants have no further right to the awards. There is only one allocation
- The vested award is delivered to the recipient as a cash payment

Performance & Adjustment:

If a decision is taken by the Committee to restrict an award (to any degree), it will prevent an award from being paid to the employee.

ASSESSMENT OF PERFORMANCE

Below is a description of the approach to measuring the performance of individuals including both financial and non-financial metrics, and explains how this assessment influences an individual's remuneration.

- The Company Performance Management Process requires all managers to review the performance and behaviours of their employees and to assign a rating to reflect their contribution throughout the year.
- All roles are benchmarked against the market to ensure that their remuneration is competitive without being excessive.
- A rigorous review is undertaken to ensure a strong correlation between positive assessments and positive awards; and negative assessments and negative awards.
- Non-financial metrics include demonstration of corporate behaviours, and successfully delivering agreed objectives.

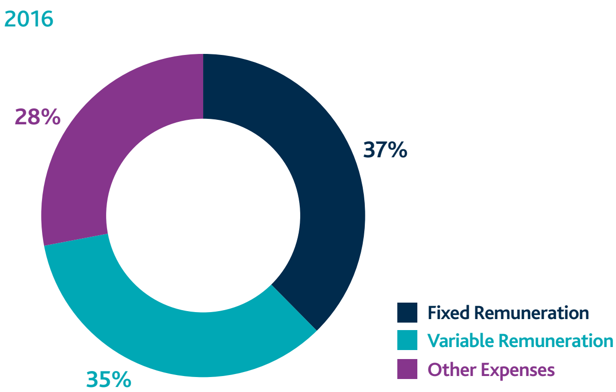
REMUNERATION RATIOS

The compensation to net revenue ratio, bonus to revenue ratio and CEO to median employee ratio form part of the key remuneration measures. These measures allow us to benchmark performance against industry peers and align compensation with the Company's financial performance. For 2016, the Board and the Shareholder approved a bonus to revenue ratio of 27%.

Relative spend on pay		
Ratio	**2016**	2015
Compensation ratio* Total compensation for employees/net underlying revenues	**53%**	55%
Bonus to revenue ratio Bonus/Underlying Revenues *100	**27%**	27%
CEO to median employee pay Total pay for CEO/Median annual compensation for UK employees (excl. executives)	**20x**	20x

*As the business continues to grow, the committee expects this ratio to decline.

The chart below shows the relative spend on remuneration (both fixed and variable) as a percentage of total costs of the business.



TREATMENT OF EXECUTIVE INCENTIVE SCHEMES, DEFERRED COMPENSATION AWARDS AND LTIPs

The main sources of variable remuneration are the discretionary annual cash bonus, the co-investment/bonus deferral scheme and the Long Term Incentive Plan. The proposed awards are presented to the Remuneration Committee by the Executive Committee, which reviews all the proposals prior to the submission to the Remuneration Committee. All the schemes are approved by the HFML Board and the Remuneration Committee, and are reviewed on an annual basis.

Any bonus pool is set as part of the strategic plan agreed between the Board and the sole shareholder, BTPS, in 2014. The Remuneration Committee and Executive Committee are charged with effectively distributing any awards across the Company on a discretionary basis. Participation in any bonus pool is limited to eligible employees only.

With regard to employees engaged in control functions, we ensure that their remuneration does not compromise their ability to objectively review the business areas they control and monitor.

GUARANTEED VARIABLE REMUNERATION

The Company will not guarantee or replace any incentive awards that would breach certain internal criteria. In limited and exceptional circumstances, the Company may agree to make an award of guaranteed variable remuneration in line with the Company policies. Replacement awards are not the Company's standard compensation practice; however, on the occasions where a replacement award is considered, the Company will take steps to determine an appropriate amount and at all times be committed to paying no more than is necessary. Retention awards are considered guaranteed variable remuneration.

REMUNERATION POLICY COVERAGE

This policy covers all permanent employees of the Company, wherever based, and across all subsidiaries. We believe the current policy to be fully compliant with the requirements of both BIPRU Investment Firms (Prudential sourcebook for Banks, Building Societies and Investment firms) and Alternative Investment Fund Managers (AIFMD).

PERFORMANCE AND KPIs

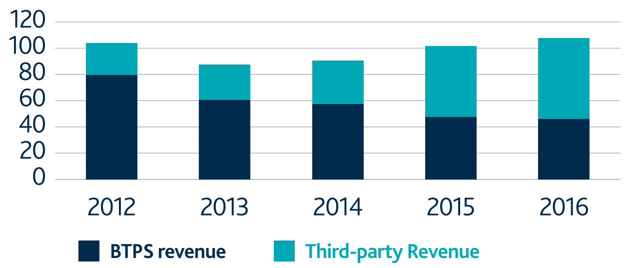
2016 Performance and Remuneration outcomes

The Committee considered the Company's results relative to key performance indicators below and progress against its strategic objectives, as well as the personal performance of each Executive Director (further information on remuneration amounts can be found in Director's Note 8.) This includes taking a balanced approach to growing the business profitably and in a sustainable way that encourages the longevity of client relationships, whilst retaining and developing the key talent critical to the long-term success of Hermes.

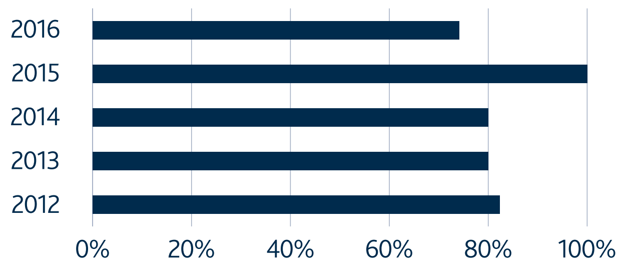
KPIs at a glance

The charts below provide an overview of the Group's performance over the last five years.

Total revenue £m

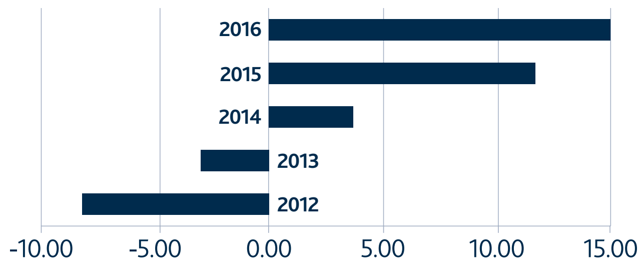


Investment performance

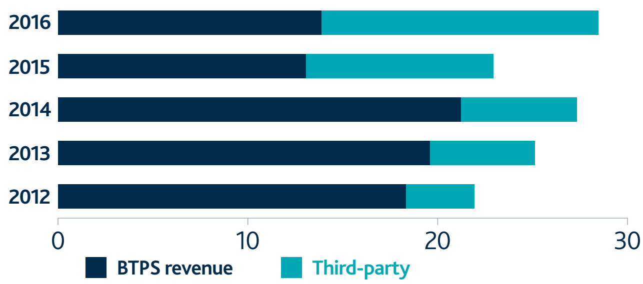


*Investment performance is against the three-year benchmark

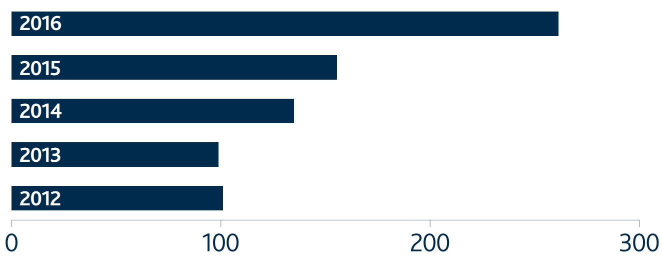
Underlying profit (loss) pre tax £m



Assets under Management £bn



Assets under Stewardship £bn



EXECUTIVE BOARD DIRECTORS REMUNERATION v KPIs

The Executive Board of Directors for this purpose are comprised of the key management personnel, two of whom are not Directors of the company. Key management personnel is a term used by FRS 102 for those persons having authority and responsibility for planning, directing and controlling the activities of a reporting entity, directly or indirectly, including any Director (whether executive or otherwise).

The total spend on remuneration is derived from a composite of the revenue and profit metrics discussed in more detail on the previous page. Further information on the total spend for Directors is detailed below.

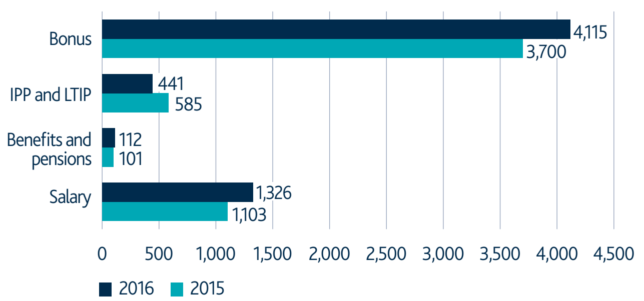
2016 £'000	2015 £'000
5,994	5,491

Total Directors' remuneration includes emoluments, amounts receivable under long-term incentive schemes and company contributions to money purchase pension schemes.

Total Directors' remuneration has increased by £503k from 2015 to 2016 due to an increase in the number of Executive Directors to five, from four. On a per capita basis, the total Directors' remuneration is consistent with 2015. When determining Directors' compensation for 2016, performance against agreed strategic objectives was considered.

The chart below shows the composition of remuneration for 2015 and 2016.

Executive Directors' pay



CHIEF EXECUTIVE'S REMUNERATION

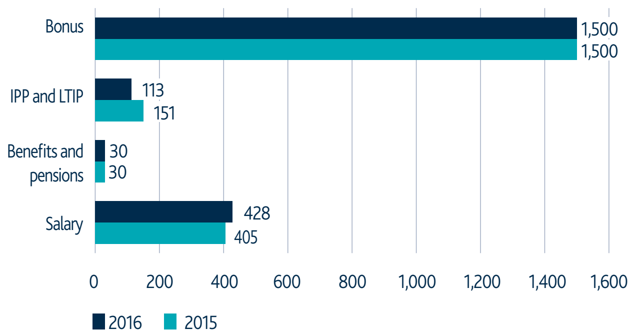
The Chief Executive's performance is formally assessed twice each year by the Chairman of the Hermes Board. Assessment is against the CEO's annual objectives and progress toward the achievement of the long-term objectives of the business.

The formal appraisal supports further discussion and deliberation by the Remuneration Committee regarding the CEO's annual cash bonus, deferred co-investment and long-term incentive pay award. This process is formally documented as part of the Committee's Terms of Reference. Hermes' performance and behaviour framework applies to all staff regardless of seniority; however, specific additional competencies are assigned to those in leadership and management positions.

2016 £'000	2015 £'000
2,071	2,086

Total Directors' remuneration includes emoluments, amounts receivable under long-term incentive schemes and company contributions to money purchase pension schemes.

Chief Executive Officer's pay



Key performance indicators	Key points in 2016 financial year – relevant to bonus award	Assessment
Financial performance		
Operating profit	Achieved continued growth in underlying profitability above target and in line with the strategic plan	✓✓✓
Third-party growth	Consistent and material increases over 5 years in third-party assets to achieve a more sustainable firm for its stakeholders	✓✓✓
Cost control	Effective cost controls in place and initiatives sensitively and successfully applied across the business	✓✓
Investment performance	3 and 5 year investment performance – 89% (3 year) above median in 2016 and net new flows of £2.0bn – demonstrates client growth	✓✓
Qualitative		
Ambassador for asset management industry through initiatives	Founder Chair and now member of the 300 Club. Successful fulfilment of all commitment and engagements including The 300 Club, CFA Future of Finance Advisory Council, IA, Mosaic, Banking Standards Board and lending support to CSR initiatives	✓✓✓
Hermes Pledge and performance and behaviour framework	Clear leadership in developing, promoting and implementing Hermes' mission to deliver holistic returns, the Hermes Pledge and Hermes' performance and behaviour framework	✓✓✓

Key	
Above target	✓✓✓
Around target	✓✓
Between threshold and target	✓
Below threshold	↓

POTENTIAL REGULATORY CHANGE

On 21 December 2015, the European Banking Authority published its final guidelines on sound remuneration policies, which came into effect on 1 January 2017. Hermes currently applies 'Proportionality' as a Level 3 firm under the PRA's and FCA's regulations on remuneration, but in the future we may be required to make changes to the remuneration policy to remain compliant with these rules.

The Committee believes that the approach of not capping variable remuneration at an individual level is in the best interests of shareholders and clients. It allows the Group to attract, retain and motivate the best talent, who know that good performance and behaviour in line with the values will be rewarded. It also allows the base salaries to remain relatively low, controlling the fixed cost base when times are challenging. This will continue to be monitored closely and will consult with shareholders if a new policy is required.

In light of the potential regulatory developments, the Board and Committee will review the remuneration policy in 2017, as the position becomes clearer. We will continue to monitor this closely and will consult with the Shareholder if a new policy is required.

RESPONSIBILITIES

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

- agreeing the broad policy and framework for the remuneration of the Chief Executive Officer, other Executive Directors of the Company, and senior managers whose compensation is over a certain threshold;
- determining the overarching principles and parameters of the remuneration policy on a Hermes Group-wide basis, excluding Hermes GPE LLP, which is a joint venture;
- establishing and maintaining a competitive remuneration package to attract, motivate and retain high calibre Executive Directors and senior management across the Group;
- aligning senior executives' remuneration with the interests of shareholders and relevant remuneration legislation;
- ensuring compliance with the FCA and other regulators' rules with regards to remuneration; and
- reviewing and approving the annual objectives for Executive Directors of the Board, in accordance with its Terms of Reference, against which their performance for remuneration purposes will be measured.

Committee attendance

Committee attendance during 2016		
Member	Number of meetings eligible to attend	% of meetings attended
Kathryn Mathews	3	100
Paul Spencer*	1	0
Billy McClory	3	100
David Stewart	3	100
David Watson	3	100
Catherine Claydon	1	100

*Paul Spencer did not attend due to an existing conflict.

WORK OF THE COMMITTEE DURING 2016

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

- recommending a remuneration policy and remuneration policy statement to the Board;
- continuing to apply regulations to compensation matters, and monitor developments of new regulations and government policies; and
- approving remuneration proposals across salary, bonus and LTIP.

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 2016 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 Hermes Pledge, provide alignment between Management and both the 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.

NON-EXECUTIVE DIRECTORS

The independent Non-Executive Directors who make up the Remuneration Committee at Hermes do not have a vested interest in the amounts being paid to any employees and do not participate in any Company-based incentive schemes.

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 at regular intervals.

INDEPENDENCY AND OBJECTIVITY OF THE REMUNERATION COMMITTEE

The Head of Risk, Head of Compliance and Head of Internal Audit have reporting lines into the Chairman of the Audit Committee in the case of internal audit, and into the Risk and Compliance Committee in the case of Risk and Compliance. The Head of HR, although reporting internally, interfaces directly with the Chair of the Remuneration Committee. The chair of each of the committees is a Non-Executive Director.

Remuneration for the Head of Risk, Head of Compliance, Head of Internal Audit, and Head of HR is proposed by Executive Management but independently approved by the Remuneration Committee. It is based on a combination of individual performance and market comparison. Objectives for control functions are set and measured independent of the business areas they support. The independence ensures the discretionary award granted is reflective of the achievement of objectives, rather than business performance.

PERSONAL SHAREHOLDING POLICY

When applicable, Hermes staff undertake not to use personal hedging strategies or remuneration or liability-related contracts of insurance to undermine the risk-alignment effects embedded in their remuneration arrangements, and the Executive Committee maintains effective arrangements designed to ensure that staff comply with their undertaking.

AVOIDING CONFLICTS OF INTEREST

To ensure remuneration policies avoid conflicts of interests, the Company developed a ‘Conflicts of Interest Policy’ in accordance with the Markets in Financial Instruments Directive (MiFID), which outlines the steps the Company has taken to identify and mitigate the types of conflict of interests that exist, or may exist.

EFFECTIVE RISK MANAGEMENT

To ensure that remuneration decisions take into account the implications for risk and risk management of the firm, the heads of Legal, Risk, Compliance and Audit provide the Remuneration Committee with regular updates on any errors or breaches that may have occurred throughout the performance period. At the end of the period, the Control Functions are re-engaged to ensure that any errors or breaches have been taken into account for making remuneration decisions.

DIRECTORS’ EMOLUMENTS

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

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.

Committee attendance during 2016

Member	Number of meetings eligible to attend	% of meetings attended
Kathryn Mathews	3	100
Billy McClory	3	100
David Stewart	3	67*
David Watson	3	100
Paul Spencer	1	100
Catherine Claydon	1	100

*David Stewart did not attend one meeting due to an existing conflict.

WORK OF THE COMMITTEE DURING 2016

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;
- appointments to the Boards of the main subsidiary companies of the Group; and
- approval of various committee changes.

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. As at 31 December 2016 our Board was made up of seven Directors of whom two (29%) 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.

DIRECTORS' REPORT

Secretary:	Sue Cane
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 2016. The Directors who served during the year are listed on pages 32 and 33.

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 21 and 22. 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 2016 (2015: £nil). During 2016 dividends have been declared and paid by subsidiaries of the Company. Dividends paid to minority shareholders are shown on page 64.

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 27 January 2017 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 HGPS. Accordingly, they continue to adopt the going concern basis in preparing the financial statements for the year ended 31 December 2016. 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.

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.

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, sexual orientation, ethnic or national origin.

SUBSEQUENT EVENTS

There were no subsequent events material to the financial statements from the balance sheet date, 31 December 2016, to the date of approval of the financial statements, 31 March 2017.

AUDITOR

The Board has performed an audit tender process in 2016 and expects to appoint a new auditor in April 2017.

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 2017

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 2016, which comprise Consolidated Profit and Loss Account, Consolidated Statement Of Comprehensive 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 29. 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 2016 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.

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 the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified any material misstatements in the Strategic Report and the Directors' Report.

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 2017

OUTCOME #26

The introduction of on-site schools has helped a large US retailer improve employee satisfaction & productivity in its South American workforce.

CONSOLIDATED PROFIT AND LOSS ACCOUNT

For the year ended 31 December 2016

	Notes	2016 £'000	2015 £'000
Group turnover	3	**107,116**	107,376
Fee and commission expenses		**(3,120)**	(1,899)
Net group turnover		**103,996**	105,477
Administrative expenses		**(99,276)**	(95,489)
Group operating profit		**4,721**	9,988
Share of results of associated undertakings	4	**2,305**	4,495
Realised currency gain		**1,591**	389
Profit/(loss) on ordinary activities before interest and taxation		**8,617**	14,872
Interest payable and similar charges	5	**(250)**	(299)
Interest receivable and similar income	5	**1,807**	198
Other finance income/(costs)	5	**300**	(200)
Profit on ordinary activities before taxation	6	**10,474**	14,571
Tax on profit on ordinary activities – Group	9	**(788)**	5,511
Profit on ordinary activities after taxation		**9,686**	20,082

All of the results are derived from continuing operations.
The notes to these financial statements on pages 66 to 98 are an integral part of these financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2016

	Notes	2016 £'000	2015 £'000
Profit for the financial year		**9,686**	20,082
Other comprehensive income			
Remeasurement of net defined benefit liability	17	**(20,000)**	4,500
Tax credit/(charge) – attributable to net actuarial (loss)/gain	9	**3,656**	(3,874)
Currency translation differences on foreign currency net investments		**(1,534)**	(489)
Other comprehensive income		**(17,878)**	137
Total comprehensive income		**(8,192)**	20,219
Profit for the year attributable to:			
Non-controlling interest		**243**	400
Equity shareholders of the Company		**9,443**	19,682
		9,686	20,082
Total comprehensive income for the period attributable to:			
Non-controlling interest		**243**	400
Equity shareholders of the Company		**(8,435)**	19,819
		(8,192)	20,219

The notes to these financial statements on pages 66 to 98 are an integral part of these financial statements.

CONSOLIDATED BALANCE SHEET

As at 31 December

	Notes	2016 £'000	2015 (restated) £'000
Fixed assets			
Intangible assets – goodwill	11	**735**	1,103
Tangible assets	12	**1,664**	1,702
Joint ventures	13	**7,932**	9,557
Investments	13	**10,049**	5,758
		20,380	18,120
Current assets			
Debtors	14	**33,838**	38,198
Cash at bank and in hand	24	**69,851**	53,360
		103,689	91,558
Current liabilities			
Creditors – amounts falling due within one year	15	**(38,045)**	(37,476)
Net current assets		**65,644**	54,082
Total assets less current liabilities		**86,024**	72,202
Creditors – amounts falling due after more than one year	15	**(17,168)**	(14,675)
Provisions for liabilities	16	**(3,640)**	(4,608)
Net assets excluding pension liabilities		**65,216**	52,919
Pension (deficit)/surplus	17	**(10,405)**	1,600
Net assets including pension liabilities		**54,811**	54,519

	Notes	2016 £'000	2015 (restated) £'000
Capital and reserves			
Called up share capital	19	**62,458**	52,458
Profit and loss account		**(7,886)**	1,661
Shareholder's funds		**54,572**	54,119
Non-controlling interest	28	**239**	400
Total capital employed		**54,811**	54,519

The restatement in 2015 relates to the reclassification of an amount between 'creditors – amounts falling due within one year' and 'provisions for liabilities' as disclosed in notes 15-16.

These financial statements were approved by the Board of Directors and authorised for issue on 31 March 2017. The notes to these financial statements on pages 66 to 98 are an integral part of these financial statements.

Signed on behalf of the Board of Directors:

S Nusseibeh – Director

COMPANY BALANCE SHEET

As at 31 December

	Notes	2016 £'000	2015 (restated) £'000
Fixed assets			
Tangible assets	12	**1,664**	1,702
Investments	13	**42,400**	36,665
		44,064	38,367
Current assets			
Debtors	14	**33,509**	37,587
Cash at bank	24	**67,556**	51,092
		101,065	88,679
Current liabilities			
Creditors – amounts falling due within one year	15	**(74,403)**	(61,754)
Net current assets		**26,662**	26,925
Total assets less current liabilities		**70,726**	65,292
Creditors – amounts falling due after more than one year	15	**(12,899)**	(10,058)
Provisions for liabilities and charges	16	**(3,640)**	(4,608)
Net assets excluding pension liabilities		**54,187**	50,626
Pension (deficit)/surplus	17	**(10,405)**	1,600
Net assets including pension liabilities		**43,782**	52,226

	Notes	2016 £'000	2015 (restated) £'000
Capital and reserves			
Called up share capital	19	**62,458**	52,458
Profit and loss account		**(18,676)**	(232)
Shareholder's funds		**43,782**	52,226

The restatement in 2015 relates to the reclassification of an amount between 'creditors – amounts falling due within one year' and 'provisions for liabilities' as disclosed in notes 15-16.

These financial statements were approved by the Board of Directors and authorised for issue on 31 March 2017. The notes to these financial statements on pages 66 to 98 are an integral part of these financial statements.

Signed on behalf of the Board of Directors:

S Nusseibeh – Director
Registered company number: 1661776

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

As at 31 December 2016

	Called up share capital £'000	Profit and loss account £'000	Non-controlling interest £'000	Total £'000
At 31 December 2015	52,458	1,661	400	54,519
Profit for the year	–	9,443	243	9,686
Remeasurement of net defined benefit liability	–	(20,000)	–	(20,000)
Deferred tax (loss)/gain on pension liabilities	–	3,656	–	3,656
Currency translation differences on foreign currency net investments	–	(1,534)	–	(1,534)
Total comprehensive income	–	(8,435)	243	(8,192)
Issue of shares	10,000	–	–	10,000
Dividend	–	–	(327)	(327)
Increase in subsidiary	–	(1,112)	–	(1,112)
Removal of minority interest	–	–	(77)	(77)
At 31 December 2016	62,458	(7,886)	239	54,811

COMPANY STATEMENT OF CHANGES IN EQUITY

As at 31 December 2016

	Called up share capital £'000	Profit and loss account £'000	Total £'000
At 31 December 2015	52,458	(232)	52,226
Loss for the year	–	(2,100)	(2,100)
Remeasurement of net defined benefit liability	–	(20,000)	(20,000)
Deferred tax gain on pension liabilities	–	3,656	3,656
Total comprehensive income	–	(18,444)	(18,444)
Issue of shares	10,000	–	10,000
At 31 December 2016	62,458	(18,676)	43,782

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December

	Notes	2016 £'000	2015 £'000
Net cash inflow from operating activities	23	**6,782**	5,680
Cash flows from investing activities			
Proceeds from sale of fixed asset investments		**808**	1,785
Purchase of fixed asset investments		**(3,493)**	(6,146)
Interest received		**201**	133
Dividends received from associates/joint ventures		**2,963**	4,451
Purchase of growth shares		**–**	(6,074)
Purchase of minority interests		**(1,192)**	–
Corporation tax received/(paid)		**1,454**	(1,612)
Purchase of tangible fixed assets		**(774)**	–
Net cash flows from investing activities		**(33)**	(7,463)
Cash flows from financing activities			
Proceeds on issue of share capital		**10,000**	–
Dividends paid		**(327)**	(202)
Net cash inflow/(outflow) from financing		**9,673**	(202)
Net increase/(decrease) in cash and cash equivalents	24	**16,422**	(1,985)
Cash and cash equivalents at beginning of year		**53,360**	55,445
Effect of foreign exchange rate changes		**69**	(100)
Cash and cash equivalents at end of year		**69,851**	53,360

COMPANY CASH FLOW STATEMENT

For the year ended 31 December

	Notes	2016 £'000	2015 £'000
Net cash (outflow)/inflow from operating activities	23	**(4,725)**	18,337
Cash flows from investing activities			
Proceeds from sale of fixed asset investments		**808**	1,743
Purchase of fixed asset investments		**(3,495)**	(4,224)
Interest received		**184**	113
Dividends received from subsidiaries		**14,385**	14,750
Purchase of growth shares		**–**	(6,074)
Corporation tax received/paid		**1,444**	–
Investment in subsidiaries		**(1,192)**	(334)
Purchase of tangible fixed assets		**(774)**	–
Net cash flows from investing activities		**11,360**	5,974
Cash flows from financing activities			
Proceeds on issue of share capital		**10,000**	–
Net cash inflow from financing		**10,000**	–
Net increase in cash and cash equivalents	24	**16,635**	24,311
Cash and cash equivalents at beginning of year		**51,092**	26,928
Effect of foreign exchange rate changes		**(171)**	(147)
Cash and cash equivalents at end of year		**67,556**	51,092

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 December 2016

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 50. The nature of the Group's operations and its principal activities are set out in the strategic report on pages 9 to 31.

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 financial statements and related notes have been reformatted to reflect the way in which revenues and costs are managed internally. Fee and commission expenses are now shown separately. The new presentation provides a more relevant basis on which to measure performance as it enhances comparability between revenues and related costs.

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.

Hermes Assured Limited and Hermes Investments (North America) Limited, two wholly-owned subsidiaries, are exempt from the requirements of the Companies Act relating to the audit of individual accounts for the year ended 31 December 2016 by virtue of section 479A of the Companies Act 2006.

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.

Fee and commission expenses are paid to third parties for ongoing services under distribution agreements and are charged to the profit and loss account over the period in which the services is expected to be provided.

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 with a full year's charge for amortisation in the year of acquisition.

If a reliable estimate of the useful life of goodwill cannot be made, the life shall not exceed five years. Provision is made for any permanent diminution in the value of goodwill.

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).

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 that are classified as payable or receivable within one year on initial recognition are measured at the undiscounted amount of the cash or other consideration expected to be paid or received, net of 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

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.

Fair value measurement

The best evidence of fair value is a quoted price for an identical asset in an active market (Level 1). 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 (Level 2). 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 (Level 3).

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

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. An impairment loss recognised for goodwill however, shall not be reversed in a subsequent period.

Where indicators exist for a decrease in impairment loss, the prior impairment loss is tested to determine reversal. For all assets other than goodwill, if and only if the reasons for the impairment loss have ceased to apply, an impairment loss shall be reversed in a subsequent period. 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.

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.

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.

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

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.

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 lease provisions are obligations arising under onerous contracts and 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 requires 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.

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 by the Group exclusive of VAT and is analysed by activity as follows:

	Group	
	2016 £'000	2015 £'000
Management fees	**95,724**	82,568
Performance fees	**6,490**	19,846
Other fee income	**4,902**	4,962
Total group turnover	**107,116**	107,376

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:

	2016 £'000	2015 £'000
Joint ventures:		
Hermes GPE LLP	**2,305**	4,495
	2,305	4,495

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

5. FINANCE COSTS (NET)

	2016 £'000	2015 £'000
Interest payable and similar charges	**250**	299
Less: Investment income	**(1,807)**	(198)
Other finance (income)/costs	**(300)**	200
	1,857	301

	2016 £'000	2015 £'000
Interest payable and similar charges in respect of:		
Financing charge on contract to re-purchase HEEL shares (see below)	**–**	49
Loan from ultimate parent	**250**	250
	250	299
Investment income		
Income on fixed asset investments (see note 13):		
Other investments	**1,606**	65
Interest receivable and similar income in respect of:		
Bank deposit balances	**201**	133
	1,807	198

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

5. FINANCE COSTS (NET) (continued)

	2016 £'000	2015 £'000
Other finance (income)/costs		
Net interest expense on defined benefit liability	**5,600**	5,400
Net interest income on defined benefit assets	**(5,900)**	(5,200)
	(300)	200

6. PROFIT/LOSS ON ORDINARY ACTIVITIES BEFORE TAXATION

	2016 £'000	2015 £'000
The profit on ordinary activities before taxation is stated after charging/(crediting):		
Depreciation on tangible fixed assets (note 12)	**812**	1,473
Amortisation of goodwill (note 11)	**1,335**	1,335
Net loss on financial liabilities at fair value through profit and loss	**157**	–
Foreign exchange gain	**(1,748)**	(389)
Profit on fair value movement of investments (note 13)	**(1,606)**	(65)
Rental charges under operating leases	**1,879**	1,868
Rental income from operating leases	**(372)**	(302)
Auditor's remuneration:		
Audit fees – Subsidiaries	**134**	132
Audit fees – Company	**81**	81
	215	213
Non-audit fees:		
Other services	**104**	108
Total fees payable to Group auditor	**319**	321

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 £16,710 (2015: £18,505). These fees were charged to and paid directly by the pension scheme.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

7. STAFF NUMBERS AND COSTS

	2016 No.	2015 No.
Average number of persons employed by the Group and Company in the year:		
Investment management	**133**	138
Administration	**218**	211
	351	349

	2016 £'000	2015 £'000
Staff costs during the year in respect of these Directors and employees were:		
Wages and salaries	**57,245**	55,333
Social security costs	**7,006**	6,655
Pension cost related to Group scheme	**4,157**	4,326
Redundancy payments	**1,335**	619
	69,743	66,933

8. DIRECTORS' REMUNERATION AND TRANSACTIONS

	2016 £'000	2015 £'000
Directors' remuneration (including Non-Executive Directors)		
Emoluments	**4,174**	4,044
Amounts receivable under long-term incentive schemes	**218**	287
Company contributions to money purchase pension schemes	**59**	66
	4,451	4,397

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 £1,292,500 (2015: £1,005,000), although they will only become payable after the Directors satisfy future service conditions. Deferred awards are included in total remuneration disclosed above.

	2016 No.	2015 No.
The number of Directors who:		
Are members of a money purchase pension scheme	**3**	3
Exercised options over shares in company	**–**	2
Had awards receivable in the form of units under a long-term incentive scheme	**3**	3

	2016 £'000	2015 £'000
Remuneration of the highest paid Director:		
Emoluments	**1,938**	1,915
Company contributions to money purchase schemes	**19**	20
Amounts receivable (other than shares and share options) under long-term incentive schemes	**114**	151
	2,071	2,086

Of this amount £785,000 (2015: £535,000) 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

9. TAX ON PROFIT ON ORDINARY ACTIVITIES

	2016 £'000	2015 £'000
a) Analysis of tax charge/(credit) for the year		
Profit and loss account:		
Current tax:		
UK corporation tax at 20.00% (2015: 20.25%)	**1,602**	1,098
Overseas tax	**(3)**	3
Share of tax charge in joint ventures and associates	**–**	9
Adjustment in respect of prior periods	**(122)**	(2,410)
Total current tax charge	**1,477**	1,300
Deferred tax:		
Timing differences, origination and reversal	**731**	(2,325)
Adjustment in respect of prior periods	**(1,757)**	(2,535)
Effect of tax rate change on opening balances	**337**	649
Total deferred tax credit	**(689)**	(4,211)
Tax charge/(credit) on profit on ordinary activities	**788**	(5,511)
Statement of comprehensive income		
Current tax:		
UK corporation tax at 20% (2015: 20.25%)	**(1,600)**	–
Deferred tax:		
Actuarial (gain)/loss on defined benefit pension scheme	**(2,056)**	3,874
Total tax on items in the statement of other comprehensive income	**(3,656)**	3,874

9. TAX ON PROFIT ON ORDINARY ACTIVITIES (continued)

	2016 £'000	2015 £'000
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 20.00% (2015: 20.25%). The differences are explained below:		
Profit on ordinary activities multiplied by the average rate of corporation tax in the UK of 20.00% (2015: 20.25%)	**2,095**	2,950
Effects of:		
Non-taxable income	**(252)**	(279)
Non-deductible expenses	**404**	391
Amounts transferred to the Statement of Comprehensive Income	**(344)**	(2,954)
Foreign tax charge	**(3)**	1
Adjustments in respect of prior periods	**(1,879)**	(4,945)
Effect of differences to deferred tax rates	**1,094**	1,564
Deferred tax recognised	**(399)**	(2,339)
Effect of overseas tax rate differences	**–**	9
Group relief not charged for	**72**	91
Current tax charge/(credit) for the year	**788**	(5,511)

The effective tax rate of 7.5% is lower than the UK corporation tax rate of 20% for the year primarily due to deferred tax balances relating to joint venture investments and the utilisation of tax assets (namely trading losses) for which deferred tax had not previously been provided.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

9. TAX ON PROFIT ON ORDINARY ACTIVITIES (continued)

	2016 Provided £'000	2016 Unprovided £'000	2015 Provided £'000	2015 Unprovided £'000
c) Deferred tax position				
The Group				
Deferred tax asset/(liability):				
Fixed asset timing difference	**(2,612)**	**(3)**	(2, 271)	(3)
Tax losses	**–**	**(8,665)**	–	(10,047)
Capital gains	**291**	**–**	–	–
Short-term timing differences	**(4,742)**	**(15)**	(2,047)	(21)
	(7,063)	**(8,683)**	(4,318)	(10,071)
The Company				
Deferred tax asset/(liability):				
Fixed asset timing differences	**(2,598)**	**–**	(2,256)	–
Tax losses	**–**	**(6,615)**	–	(7,004)
Capital gains	**291**	**–**	–	–
Short-term timing differences	**(3,557)**	**–**	(876)	–
	(5,864)	**(6,615)**	(3,132)	(7,004)

Deferred tax assets totalling £8,683,308 (2015: £10,070,939) 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. LOSS ATTRIBUTABLE TO 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 £2,100,158 (2015: loss of £9,485,257).

11. INTANGIBLE FIXED ASSETS

	Goodwill £'000
The Group	
Cost:	
At 1 January 2016	11,936
Written off	(8,614)
At 31 December 2016	3,322
Accumulated amortisation:	
At 1 January 2016	(10,833)
Written off	8,614
Amortisation	(368)
At 31 December 2016	(2,587)
Net book value:	
At 31 December 2016	735
At 31 December 2015	1,103

The remaining unamortised goodwill above relates to Hermes European Equities Limited (formerly Hermes Sourcecap Limited).

Unamortised goodwill of £3,870,022 (2015: £4,837,022) 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 (2015: £967,000) was amortised during the year relating to the Hermes GPE LLP joint venture, in addition to the amortisation charge above.

The brought forward amounts for cost and accumulated amortisation both include an amount of £8,614,000 in relation to the fully amortised goodwill for Hermes Focus Asset Management Limited. As this entity has been previously disposed of the amount has been fully written off in both the cost and accumulated amortisation.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

12. TANGIBLE FIXED ASSETS

	Leasehold Improvements £'000	Fixtures, Fittings and Equipment £'000	Total £'000
The Group			
Cost:			
At 1 January 2016	5,915	11,507	17,422
Additions	–	774	774
Disposals	–	–	–
At 31 December 2016	**5,915**	**12,281**	**18,196**
Accumulated depreciation:			
At 1 January 2016	5,139	10,581	15,720
Charge for the year	205	607	812
At 31 December 2016	**5,344**	**11,188**	**16,532**
Net book value:			
At 31 December 2016	**571**	**1,093**	**1,664**
At 31 December 2015	**776**	**926**	**1,702**

12. TANGIBLE FIXED ASSETS (continued)

	Leasehold Improvements £'000	Fixtures, Fittings and Equipment £'000	Total £'000
The Company			
Cost:			
At 1 January 2016	5,915	11,263	17,178
Additions	–	774	774
Disposals	–	–	–
At 31 December 2016	**5,915**	**12,037**	**17,952**
Accumulated depreciation:			
At 1 January 2016	5,139	10,337	15,476
Charge for the year	205	607	812
At 31 December 2016	**5,344**	**10,944**	**16,288**
Net book value:			
At 31 December 2016	**571**	**1,093**	**1,664**
At 31 December 2015	**776**	**926**	**1,702**

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

13. FIXED ASSET INVESTMENTS

	Investment in Joint Ventures £'000	Unlisted Investments £'000	Total £'000
The Group			
At 1 January 2016	9,557	5,758	15,315
Share of retained profit	2,305	–	2,305
Additions	–	3,493	3,493
Movement in fair value	–	1,606	1,606
Goodwill amortisation	(967)	–	(967)
Disposals	–	(808)	(808)
Dividends received from joint ventures	(2,963)	–	(2,963)
At 31 December 2016	**7,932**	**10,049**	**17,981**

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 £3,493,299 and £808,549 respectively. These investments are measured at fair value. A fair value gain of £1,605,567 was recognised in the profit and loss during the year (2015: £64,839).

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

	2016 £'000	2015 £'000
Hermes GPE LLP	**7,932**	9,557
TOTAL	**7,932**	9,557

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.

13. FIXED ASSET INVESTMENTS (continued)

	Investment in Subsidiaries £'000	Investment in Joint Ventures £'000	Unlisted Investments £'000	Total £'000
The Company				
Cost:				
At 1 January 2016	18,593	12,674	5,754	37,021
Additions	1,192	–	3,495	4,687
Movement in fair value	–	–	1,606	1,606
Disposal	–	–	(808)	(808)
At 31 December 2016	**19,785**	**12,674**	**10,047**	**42,506**
Provision for impairment:				
At 1 January 2016	356	–	–	356
Movement in provision	(250)	–	–	(250)
At 31 December 2016	**106**	**–**	**–**	**106**
Net book value:				
At 31 December 2016	**19,679**	**12,674**	**10,047**	**42,400**
At 31 December 2015	**18,237**	**12,674**	**5,754**	**36,665**

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 reversed the provision for impairment of £250,000 against the investment in Hermes Equity Ownership Services Limited, due to the improvement in the net assets position.

During the year the Company acquired an additional 7% in Hermes European Equities Limited, an existing majority-owned subsidiary.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

14. DEBTORS

	2016 Group £'000	2016 Company £'000	2015 Group £'000	2015 Company £'000
Due within one year:				
Owed by subsidiaries	**–**	**16,625**	–	17,476
Owed by joint ventures	**11**	**11**	11	11
Owed by parent	**9,644**	**152**	13,928	135
Trade debtors	**2,936**	**606**	5,180	107
Taxation	**7,124**	**11,568**	5,684	15,744
Other debtors	**1,570**	**1,570**	1,161	1,151
Prepaid and accrued income	**12,553**	**2,977**	12,234	2,963
	33,838	**33,509**	38,198	37,587

15. CREDITORS

	2016 Group £'000	2016 Company £'000	2015 Group (restated) £'000	2015 Company (restated) £'000
Amounts falling due within one year:				
Owed to parent	**191**	**–**	994	–
Owed to subsidiaries	**–**	**54,336**	–	44,608
Other creditors	**2,467**	**2,440**	1,249	1,206
Taxation	**–**	**–**	–	–
Deferred taxes	**–**	**–**	–	–
Accruals and deferred income	**35,387**	**17,627**	35,233	15,940
	38,045	**74,403**	37,476	61,754
Amounts falling due after more than one year:				
Owed to parent	**5,822**	**5,822**	5,572	5,572
Other creditors	**11,346**	**7,077**	9,103	4,486
	17,168	**12,899**	14,675	10,058

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.

The prior year comparative figures for accruals and deferred income in both the Group and the Company have been restated to remove a dilapidation liability of £2,866,926. The prior year amount in provisions for liabilities and charges has been restated to include this liability. See Note 16 for further details.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

16. PROVISIONS FOR LIABILITIES AND CHARGES

	Onerous Lease Provision 2016 £'000	Restructuring Provision 2016 £'000	Dilapidation Provision 2016 £'000	Total 2016 £'000
The Group and Company				
At 1 January	**1,191**	**550**	**2,867**	**4,608**
Charged to the profit and loss	**461**	–	–	**461**
Release of unused provision	–	**(188)**	**(398)**	**(586)**
Utilisation of provision	**(481)**	**(362)**	–	**(843)**
At 31 December	**1,171**	–	**2,469**	**3,640**

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. During the year the Group increased its onerous lease provision by £461,541 due to an increase in vacant space to be effected in 2017.

The restructuring provision related 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 and the residual amount in 2016.

The dilapidation provision is recognised on the leasehold property at Lloyds Chambers, 1 Portsoken Street as the terms of the lease require the Company to restore the property to its original condition following changes made to the property during the period of the lease. The brought forward amount has been restated following a reclassification between 'accruals and deferred income' and 'provisions for liabilities and charges'. See Note 15 for further details.

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. Members of HGPS are entitled to pension amounts on retirement linked to their final salary (with inflationary uplift). 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 £3,557,492 during the year (2015: £3,626,243). The contributions outstanding as at the year-end amounted to £Nil (2015: £390,733).

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.

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:

	2016 years	2015 years
Retiring today	**27.6**	27.5
Retiring in 20 years	**30.0**	29.2

17. PENSION COMMITMENTS (continued)

The actuarial valuation was updated at 31 December 2016 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 (2015: £8.3m).

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:

	2016 £m	2015 £m
Present value of funded Scheme obligation	**(190.7)**	(144.0)
Fair value of Scheme assets	**180.3**	145.6
(Deficit)/Surplus	**(10.4)**	1.6

The amounts recognised in the profit and loss account are as follows:		
Administration costs	**0.6**	0.7
Interest on Scheme obligation (included in other finance costs)	**5.6**	5.4
Past service cost	**–**	0.6
Expected return on Scheme assets (included in other finance income)	**(5.9)**	(5.2)
Total	**0.3**	**1.5**

'Interest on Scheme obligation' and 'Expected return on Scheme assets' are disclosed net as £0.3m 'Other finance costs' in the Consolidated Profit and Loss Account (2015: £0.2m).

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

	2016 £m	2015 £m
Actual return less expected return on Scheme assets, i.e. gain/(loss)	**26.7**	(0.4)
Experience gains and losses arising on Scheme liabilities, i.e. (loss)	–	(1.5)
Changes in assumptions underlying the present value of Scheme liabilities, i.e. gain/(loss)	**(46.7)**	6.4
Actuarial (loss)/gain	**(20.0)**	**4.5**

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

17. PENSION COMMITMENTS (continued)

Changes in the present value of the defined benefit obligation are as follows:

	2016 £m	2015 £m
Opening defined benefit obligation	**144.0**	148.5
Past service cost	**–**	0.6
Interest cost	**5.6**	5.4
Benefits paid	**(5.6)**	(5.6)
Experience loss on defined benefit obligation	**–**	1.5
Changes to assumptions	**46.7**	(6.4)
Closing defined benefit obligation	**190.7**	144.0

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

	2016 £m	2015 £m
Opening fair value of assets	**145.6**	138.8
Interest on assets	**5.9**	5.2
Company contribution	**8.3**	8.3
Benefits paid	**(5.6)**	(5.6)
Administrative costs	**(0.6)**	(0.7)
Return on assets less interest	**26.7**	(0.4)
Closing fair value of assets	**180.3**	145.6

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

	2016 %	2015 %
Equities	**32**	32
Bonds/Gilts	**41**	31
Real estate/Other	**27**	37

Included in the fair value of plan assets are investments in the Group's managed funds with a value of £27.3m (2015: £23.4m).

17. PENSION COMMITMENTS (continued)

Principal actuarial assumptions at the balance sheet date:

	2016 %	2015 %
Discount rate at 31 December	**2.8**	4.0
Future pensionable salary increases	**2.1**	2.0
Future increases to pensions in payment (HGPS members)	**3.1**	3.0
Future increases to pensions in payment (HPS members)	**2.1**	2.0

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.

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

	2016 £m	2015 £m	2014 £m	2013 £m	2012 £m
Present value of Scheme obligation	**(190.7)**	(144.0)	(148.5)	(140.7)	(118.4)
Fair value of Scheme assets	**180.3**	145.6	138.8	118.4	109.8
Surplus/(Deficit)	**(10.4)**	1.6	(9.7)	(22.3)	(8.6)
Experience adjustments on Scheme assets – gain/(loss)	**26.7**	(0.4)	10.5	3.4	1.7
Experience adjustments on Scheme liabilities – gain/(loss)	**–**	(1.5)	(0.1)	0.2	0.1

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

18. FINANCIAL INSTRUMENTS

The carrying value of the Group and Company's financial assets and liabilities are summarised below:

	2016 £m	2015 £m
Financial assets		
Measured at fair value through profit or loss		
Fixed asset unlisted investments (see note 13)	**9,797**	5,566
Measured at undiscounted amount receivable		
Trade and other debtors	**33,838**	38,198
Fixed asset investments in unlisted equity instruments (see note 13)	**252**	192
	43,887	43,956
Financial liabilities		
Measured at fair value through profit and loss		
Foreign exchange forward derivative contracts	**157**	–
Measured at amortised cost:		
Loans payable	**5,822**	5,572
Measured at undiscounted amount payable:		
Trade and other creditors	**52,874**	51,187
	58,853	56,759

The Group enters into forward foreign exchange contracts to hedge exposure to net revenues received in foreign currency. The liability above reflects the fair value of those derivative contracts at the balance sheet date. The below shows the contracts entered into before the year end:

	Sell		Buy		Settlement date	Fair value in £'000
Liabilities						
	USD '000	22,443	GBP '000	18,000	20 Dec 2017	18,164
	EUR '000	5,849	GBP '000	5,000	20 Dec 2017	4,993
Net change in fair value						**157**

Fair value was determined using the Level 2 measurement basis.

18. FINANCIAL INSTRUMENTS (continued)

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

	2016 £'000	2015 £'000
Interest income and expense		
Total interest expense for financial liabilities at amortised cost	**250**	250
Fair value gains and losses		
On financial assets measured at fair value through profit and loss	**1,606**	65
On financial liabilities measured at fair value through profit and loss	**157**	–

19. CALLED UP SHARE CAPITAL

	2016 £'000	2015 £'000
Called up, allotted and fully paid:		
62,458,000 (2015: 52,458,000) Ordinary shares of £1 each	**62,458**	52,458
	62,458	52,458

On 4 October 2016, the company issued capital of £10,000,000 to its owner, BTPS.

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:

	No. of shares 2016	Subscription price (£) 2016	No. of shares 2015	Subscription price (£) 2015
Outstanding at beginning of period	**–**	**–**	3,717	3,717
Granted during the period	**–**	**–**	–	–
Forfeited during the period	**–**	**–**	(3,717)	(3,717)
Outstanding at the end of the period	**–**	**–**	–	–

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

21. LONG TERM INCENTIVE PLAN

The Long Term Incentive Plan (LTIP) is an incentive plan designed 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 a particular year represents the following:

- On vesting 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 above the initial base value.

	No. of units awarded 2016	No. of units awarded 2015
At 1 January	**95.5**	–
Issued during year	**94.5**	98.5
Forfeited during year	**(15.5)**	(3.0)
At 31 December	**174.5**	95.5

The total of all awards outstanding as at the 31 December 2016 is 174.5 units.

During the year the Company issued 94.5 units. Due to the leaver provisions 15.5 of these units were forfeited during the year. The total liability recognised as at 31 December 2016 was £2,972,722 (2015: £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 2016 was £1,587,041 (2015: £1,640,319).

22. FINANCIAL COMMITMENTS

Operating Lease Commitments

The Group and Company's total future minimum lease payments on non-cancellable operating leases are as follows:

	Land and Buildings 2016 £'000	Other 2016 £'000	Land and Buildings 2015 £'000	Other 2015 £'000
Within one year	**2,134**	**168**	2,125	469
Between two – five years	**1,408**	**98**	3,439	266
After five years	**–**	**–**	–	–
	3,542	**266**	5,564	735

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

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 2016 by virtue of section 479A of the Companies Act 2006.

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

	Group 2016 £'000	Company 2016 £'000	Group 2015 £'000	Company 2015 £'000
Operating gain/(loss)	**4,721**	**(23,074)**	9,988	(21,582)
Bank charges	**(14)**	**(17)**	–	–
Reversal of impairments	**–**	**(250)**	–	–
Adjustment for pension funding	**(7,700)**	**(7,700)**	(7,034)	(7,034)
Depreciation	**812**	**812**	1,473	1,413
Amortisation	**1,335**	**–**	1,335	–
Decrease/(increase) in debtors	**5,003**	**(949)**	(1,014)	5,255
Increase in creditors	**2,625**	**26,453**	932	40,285
Net cash inflow/(outflow) from operating activities	**6,782**	**(4,725)**	5,680	18,337

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

	Group 2016 £'000	Company 2016 £'000	Group 2015 £'000	Company 2015 £'000
Net funds at beginning of year	**53,360**	**51,092**	55,445	26,928
Increase/(decrease) in cash in year	**16,491**	**16,464**	(2,085)	24,164
Net funds at end of year	**69,851**	**67,556**	53,360	51,092

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

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.

SUBSIDIARY UNDERTAKINGS	ACTIVITY	REGISTERED OFFICE
Hermes Investment Management Limited	Investment management	Lloyds Chambers, 1 Portsoken St, London (Lloyds Chambers)
Hermes Real Estate Investment Management Limited	Investment management	Lloyds Chambers
Hermes European Equities Limited	Investment management	Lloyds Chambers
Hermes BPK Limited	Investment management	Lloyds Chambers
Hermes Private Equity Limited	Investment management	Lloyds Chambers
Hermes Alternative Investment Management Limited	Investment management	Lloyds Chambers
Hermes Equity Ownership Services Limited	Stewardship and corporate governance	Lloyds Chambers
Hermes Administration Services Limited	Investment management	Lloyds Chambers
Hermes Assured Limited	Investment management	Lloyds Chambers
Hermes BPK Partners Inc	Investment management	2711 Centerville Road, Suite 400 New York NY10017, USA
Hermes Investments (North America) Limited	Investment management	Lloyds Chambers
Hermes Fund Managers (North America) GP, Inc.	Investment management	200 State Street, 7th floor, Boston MA 02109-2696, USA
Hermes Real Estate Debt GP Limited	Investment management	Lloyds Chambers
Hermes Private Debt I GP Limited	Investment management	Lloyds Chambers
Hermes Global Funds GP Limited	Inactive	c/o Walkers Corporate Services Limited, 87 Rory Street, George Town, Grand Cayman, KY1-9005, Cayman Islands
Hermes BPK Accelerator (Cayman) Limited	Inactive	Intertrust Corporate Services (Cayman) Limited, 190 Elgin Avenue, George Town, Grand Cayman, KY1-9005, Cayman Islands
Hermes BPK Coinvestment Trustees Limited	Inactive	Lloyds Chambers
Hermes Pension Fund Management Limited	Inactive	Lloyds Chambers
Hermes Secretariat Limited	Inactive	Lloyds Chambers
Hermes Sourcecap Limited	Inactive	Lloyds Chambers

JOINT VENTURES	ACTIVITY	REGISTERED OFFICE
Hermes GPE LLP	Investment management	Lloyds Chambers
Vista UK Residential 1 (GP) LLP	Investment management	Lloyds Chambers
Vista UK Residential Real Estate (GP) LLP	Investment management	Brodies LLP, 15 Atholl Crescent, Edinburgh, EH3 8HA

Subsidiary undertakings disclosed above are wholly-owned subsidiaries except for Hermes European Equities Limited (90% of ordinary share capital owned). All subsidiaries disclosed above have been consolidated in these financial statements.

HFM (Singapore) Pte. Limited which is incorporated in Singapore, was dissolved on 5 December 2016. HFM (Australia) Pty Limited which was incorporated in Australia, was dissolved on 16 December 2015. Hermes Global Equities Partners LP and Hermes Fund Managers (North America) LP were dissolved on 31 July 2015.

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.

The liquidation process of Hermes BPK Limited is still in progress and expected to take place in 2017.

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, interest rate and market 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 2016, the Group and the Company's financial assets exposed to credit risk amounted to the following:

	Group 2016 £'000	Company 2016 £'000	Group 2015 £'000	Company 2015 £'000
Financial assets				
Cash at bank	**69,851**	**67,556**	53,360	51,092
Owed by subsidiaries	**–**	**16,625**	–	17,476
Trade debtors and accrued income	**15,489**	**3,583**	17,414	3,070
Taxation	**7,124**	**11,568**	5,684	15,744
Owed by parent	**9,644**	**152**	13,928	135
Other debtors	**1,581**	**1,581**	1,172	1,162
	103,689	**101,065**	91,558	88,679

Cash at bank is held in current accounts or placed on deposit in highly-rated liquid money-market funds or 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. There were no trade debtors of the Group that were more than 90 days past due at 31 December 2016 (2015: £1,055,348).

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

26. FINANCIAL RISK MANAGEMENT OBJECTIVES AND STRATEGY (continued)

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

	Maturity	Group 2016 £'000	Company 2016 £'000	Group 2015 £'000	Company 2015 £'000
Financial liabilities					
Owed to parent	**<12 mths**	**191**	**–**	994	–
Owed to associates	**<12 mths**	**–**	**54,336**	–	44,608
Other creditors <12 mths	**<12 mths**	**1,620**	**1,593**	488	445
Unfunded pension liability	**<12 mths**	**847**	**847**	761	761
Accruals and prepaid income	**<6 mths**	**35,387**	**17,627**	35,233	15,940
Owed to parent	**>12 mths**	**5,822**	**5,822**	5,572	5,572
Other creditors > 12 mths	**>12 mths**	**11,346**	**7,077**	9,103	4,486
		55,213	**87,302**	52,151	71,812

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.

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 £1.4m interest would have been earned.

Market risk – foreign exchange

Market risk is the possibility for the Group to experience losses due to factors that affect the overall performance of the financial markets in which the Group is involved. One key factor is foreign currency exchange risk as the Group receives income and incurs expenses in foreign currencies.

Due to a net exposure to foreign currency movements the Group partially hedges this exposure through the use of foreign currency forward contracts (see note 18 for further disclosures).

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 to BT Pension Scheme Management Limited (BTPSM) in respect of services provided to the Hermes Group.

	2016 £'000	2015 £'000
P Spencer (Chairman & Non-Executive Director Fee)	**25**	88
W McClory (Non-Executive Director Fee)	**20**	25
Total	**45**	113

Central allocated costs from the Company to BTPSM totalled £3,350,035 during the year (2015: £3,511,028). An amount was due to the Company from BTPSM totalling £1,285,035 at year-end (2015: £1,092,720).

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

- Hermes European Equities Limited (HEEL) – formerly Hermes Sourcecap Limited

  Central allocated costs from the Company to HEEL totalled £2,731,482 during the year (2015: £1,763,856). HEEL provide funds to HFML to place on deposit for the Group. There is an amount due to HEEL totalling £2,168,072 at year-end (2015: £612,808 amount due to HEEL), representing the net year-end debt due to HEEL 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 (2015: £1,350,000). An amount was due to the Company from HGPE totalling £11,268 at year-end (2015: £10,833).

The amounts outstanding above for HEEL and HGPE are unsecured and will be settled in cash. No guarantees have been given or received. No provisions have been made for doubtful debts in respect of the amounts owed by related parties.

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

Directors' transactions

Loan to Director:

There were no loans to Directors in the year ended 31 December 2016. During the year ended 31 December 2015 the company advanced one of the Directors an unsecured loan totalling £120,000. Interest was charged at the HMRC beneficial loan rate. This loan was repaid in 2015

Other related party transactions

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

The total remuneration for key management personnel for the period totalled £6,352,407 (2015: £5,868,436), being remuneration disclosed in note 7 of £4,450,597 (2015: £4,397,375) and remuneration provided to other key management personnel of £1,901,810 (2015: £1,471,061).

NOTES TO THE FINANCIAL STATEMENTS (continued)

Year ended 31 December 2016

28. NON-CONTROLLING INTEREST – EQUITY

The minority interest liability of £239,000 (2015: £400,000) included within the consolidated balance sheet and a debit of £243,000 (2015: debit of £400,100) included within the consolidated profit and loss account relate to a 9.51% shareholding in Hermes European Equities Limited, which is owned by an individual Director of the entity (2015: 17% shareholding owned by an individual Director).

29. ULTIMATE PARENT UNDERTAKING AND CONTROLLING PARTY

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 financial statements into which the results of the Company are consolidated. The financial statements of the BT Pension Scheme can be obtained at Lloyds Chambers, 1 Portsoken Street, London E1 8HZ.

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, cooperative 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