MUFG Securities EMEA plc

Pillar 3 Disclosures

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MUFG Securities EMEA plc
A member of MUFG, a global financial group

Contents

1. About MUS(EMEA)

MUFG Securities EMEA plc (“MUS(EMEA)”) is a wholly-owned investment banking subsidiary of Mitsubishi UFJ Securities Holdings Co. Ltd. (“MUSHD”), which is wholly owned by Mitsubishi UFJ Financial Group (“MUFG”) and was established in 1983. MUS(EMEA)’s Tier 1 capital at 30 June 2019 was £1,530 million.

MUFG was formed in October 2005 through the merger of Mitsubishi Tokyo Financial Group and UFJ Holdings and is one of the world’s largest and most diversified financial groups. MUFG’s services include commercial banking, trust banking, investment banking, credit cards, consumer finance, asset management, leasing and other financial service activities.

MUS(EMEA) actively trades in fixed income, equity and structured finance products, providing client solutions across primary and secondary markets. The client group includes financial institutions, corporations and central banks. MUS(EMEA) primarily supports this client group from its base in London and additionally operates a branch in the Dubai International Financial Centre.

Following the UK Referendum on EU Membership (“Brexit”), MUS(EMEA) has initiated its contingency plan, including the establishment of a wholly owned subsidiary in The Netherlands. The subsidiary, namely MUFG Securities (Europe) N.V. (“MUS(EU)”), as well as a branch of that entity in Paris, are central to our strategy to support the continued servicing of clients across Europe. Note, the metrics presented within the document are prepared on a solo entity basis (i.e. not consolidated), this is in line with the IFRS financial reporting prepared by MUS(EMEA).

MUS(EMEA) works in close partnership with MUFG and its corporate bank, MUFG Bank, Ltd. (“MUFG Bank”), to ensure its clients experience seamless product delivery that meets all of their objectives.

2. Introduction

The Basel II Framework was implemented in the European Union via the Capital Requirements Directive ("CRD") in June 2006. The framework is made up of three pillars:

- Pillar 1 (Minimum capital requirements)
  Pillar 1 sets out 'minimum capital requirements'. It covers the calculation of risk weighted assets ("RWA") and the capital resources requirements for credit risk, market risk and operational risk. Credit risk includes counterparty credit risk and concentration risk.

- Pillar 2 (Supervisory review process)
  Pillar 2 capital framework is intended to ensure that firms have adequate capital to support the relevant risks in their business, and that they have appropriate processes to ensure compliance with CRD IV. It considers whether additional capital is required over and above the Pillar 1 capital requirements. A firm's internal capital adequacy assessment process ("ICAAP") supports this process.

- Pillar 3 (Market discipline)
  Pillar 3 of the Basel framework aims to promote market discipline through regulatory disclosure requirements. It covers external disclosures of capital and risk exposures to increase transparency and improve comparability and consistency of disclosures.

The Basel Committee agreed updates to the Basel framework in July 2009, commonly referred to as Basel 2.5. These seek to better capture risk from securitisation and trading book exposures and were incorporated into European law via amendments to the CRD known as the "Third Capital Requirements Directive" or "CRD III".

Basel III, released in December 2010, builds on Basel 2.5. It sets higher capital and liquidity requirements to be phased in over the coming years. In the EU, Basel III was implemented through the Capital Requirement Regulation ("CRR") and Fourth Capital Requirements Directive ("CRD IV") in January 2014. The UK Prudential Regulation Authority ("PRA") published final rules for implementing CRD IV in its Policy Statement 7/13. Reporting and Disclosure requirements are covered in the Policy Statement.

In November 2016, the European Commission proposed a number of amendments to the existing CRR and CRD IV (collectively referred to as "CRR II"). These amendments cover some of the proposals already completed or under development by the Basel Committee.

In June 2019, the EU enacted the final rules amending the Capital Requirements Regulation, known as the CRR II. The CRR II will follow a phased implementation with significant elements entering into force in 2021. These final rules will be considered alongside the implications arising from the UK's negotiations over its exit from the European Union. MUS(EMEA) is monitoring and preparing for these changes to ensure any upcoming regulatory requirements are met.

The Pillar 3 disclosures are prepared in accordance with the CRR and CRD IV as well as the European Banking Authority ("EBA") guidelines (EBA/GL/2016/11) on disclosure requirements issued in December 2016. The Pillar 3 disclosures are available on the corporate website of MUS(EMEA) (www.mufgsecurities.com).

The Pillar 3 disclosures were verified and approved internally, including a review by the Board of Directors. There is no requirement for external auditing of these disclosures.

3. Regulatory Approach

MUS(EMEA) is regulated by the UK PRA and Financial Conduct Authority ("FCA") and is subject to minimum capital adequacy standards. MUS(EMEA) calculates appropriate capital requirements for each of its material risks.

METHODOLOGIES FOR MUS(EMEA)'S CAPITAL CALCULATIONS

Pillar 1 Credit Risk

MUS(EMEA)'s credit risk requirement is measured under the Standardised Approach in accordance with Title 2 of Part Three within CRR.

Pillar 1 Market Risk

The calculation of MUS(EMEA)'s market risk capital requirements is primarily based on its internal Value at Risk ("VaR") model which has been approved by the PRA. Market risk capital requirements for a small number of positions are calculated using the Standardised Approach.

Pillar 1 Operational Risk

MUS(EMEA) calculates its operational risk using the Standardised Approach in accordance with Title 3 of Part Three within CRR.

BASIS OF CONSOLIDATION

In this disclosure, MUS(EMEA) is presented on a solo basis and there is no difference between the financial accounting consolidation and the regulatory consolidation.

4. Capital Resources

MUS(EMEA)'s regulatory capital resources are assessed under the CRR and CRD IV. MUS(EMEA)'s capital consists of Tier 1 – share capital, retained earnings and Additional Tier 1, and Tier 2 – subordinated debt which is fixed term and denominated in Japanese yen.

MUS(EMEA) manages its risk profile and its capital resources with the objective of maintaining a capital ratio in excess of the Capital Resources Requirement for its risk profile at all times. The management of MUS(EMEA)'s capital is carried out under the principle that it should not unexpectedly need to raise new capital or significantly reduce its risk taking in order to meet its capital management objectives.

MUSHD and MUS(EMEA)'s affiliate MUFG Bank provide support arrangements to MUS(EMEA), including a 'Keep Well Agreement'. MUS(EMEA) is not aware of any material impediments to the transfer of capital resources from its parent or affiliate.

The breakdown of own funds and capital ratios is shown below.

Table 1: Own Funds Disclosure

	30 Jun 2019 £m	31 Dec 2018 £m
Own Funds		
Common Equity Tier 1 ("CET1") capital before regulatory adjustments	1,421	1,260
Total regulatory adjustments to CET1	(198)	(146)
CET1 capital	**1,223**	**1,114**
Additional Tier 1 ("AT1") capital before regulatory adjustments	307	307
Total regulatory adjustments to AT1 capital	0	0
AT1 capital	**307**	**307**
Tier 1 capital	**1,530**	**1,421**
Tier 2 ("T2") capital before regulatory adjustments	321	314
Total regulatory adjustments to T2 capital	0	0
T2 capital	**321**	**314**
Total capital	**1,851**	**1,735**
Capital Ratios		
CET1 (as a percentage of total risk exposure amount)	14.4%	14.0%
Tier 1 (as a percentage of total risk exposure amount)	18.0%	17.9%
Total capital (as a percentage of total risk exposure amount)	21.8%	21.8%
Total Risk Weighted Assets ("RWA")	**8,506**	**7,946**

5. Capital Requirements

The Pillar 1 framework provides the basis for capital requirements arising from credit, market and operational risk. It covers the calculation of risk weighted assets ("RWA") and the capital requirements. The Pillar 2 framework requires firms to hold capital for all risks not sufficiently covered in the Pillar 1 framework and ensures that firms have adequate capital to support the relevant risks in their business.

In the table below, MUS(EMEA)'s Total Capital Requirements set out the minimum capital required.

Table 2: Total Capital Requirements

	30 Jun 2019 Capital required £m	31 Dec 2018 Capital required £m
Pillar 1		
Credit Risk (Including Concentration Risk)	376	327
Market Risk	252	261
Operational Risk	53	47
Total	**681**	**635**
Pillar 2	**393**	**303**
Total Capital Requirements[1]	**1,074**	**938**

1 The term 'Total Capital Requirements' is defined in the Policy Statement 30/17 issued by the PRA

6. Credit Risk

Credit risk is the risk of loss resulting from client, issuer or counterparty default and arises on credit exposure in all forms, including settlement risk. MUS(EMEA) measures credit risk capital requirements using the Standardised Approach.

METHODOLOGY

MUS(EMEA) takes counterparty and/or issuer credit risk through most of its business activities. Counterparty credit risk arises from derivatives and securities financing transactions ("SFT"). It is calculated in both the trading and non-trading books. Under CRD IV, four methods may be used to calculate exposure values for counterparty credit risk. These four methods are Mark-to-Market, Original Exposure, Standardised and Internal Models Method. MUS(EMEA) uses the mark-to-market method to determine the exposure value which is the sum of current replacement cost and potential future credit exposure.

Per Article 113 of CRR, MUS(EMEA) is required to use rating agencies' credit assessments for the determination of risk weights under the standardised approach to credit risk. The credit assessment should be produced by an eligible External Credit Assessment Institution ("ECAI") and used in a consistent manner over time. For regulatory purposes, MUS(EMEA) has selected Moody's Rating Agency as its nominated ECAI, with the exception of securitisation exposures where DBRS, a global credit rating agency, has been selected. ECAI ratings are used to determine risk weightings for all the relevant exposure classes.

Tables below shows details of MUS(EMEA)'s credit risk exposures, RWAs and capital requirements.

Table 3: Credit Risk Capital Requirements and RWAs[1]

	30 Jun 2019		31 Dec 2018	
	RWAs £m	Capital required £m	RWAs £m	Capital required £m
Counterparty Credit Risk	3,166	254	2,698	216
Credit Valuation Adjustment risk("CVA")[2]	856	68	914	73
Non-Trading Book Credit Risk[3]	674	54	474	38
Concentration Risk	-	-	-	-
Total	**4,696**	**376**	**4,086**	**327**

1 Derivatives, SFTs, and exposures to central counterparties ("CCP") are included.
2 The CVA is the capital charge accounting for potential mark to market losses due to credit quality deterioration of counterparty. MUS(EMEA) uses Standardised Approach to calculate the CVA.
3 Non-trading book credit risk includes both on and off balance sheet items including fixed assets and non-trading book issuer exposures, and banking book securitisation.

Table 4: Counterparty Credit Risk Summary[1]

	30 Jun 2019			31 Dec 2018		
	Exposure value £m	RWAs £m	Capital required £m	Exposure value £m	RWAs £m	Capital required £m
Central Government and Central Banks	324	7	1	529	7	1
Institutions (Excluding CCPs)	2,738	753	60	2,622	725	58
Institutions (CCPs)	8,109	286	23	7,558	397	32
Corporates	2,589	1,936	155	2,085	1,559	125
Multilateral Development Banks	9	-	-	38	-	-
Regional Government and Local Authority	90	18	1	17	3	0
International Organisations	51	-	-	43	-	-
Public Sector Entity	52	44	4	25	7	1
Total	**13,962**	**3,044**	**244**	**12,916**	**2,698**	**216**

1 Derivatives, SFTs, and exposures to CCPs are included

7. Market Risk

Market risk is the risk of losses from movements in market prices in the trading portfolio. MUS(EMEA) uses a variety of risk measures to quantify and control this risk, with the overall objective of ensuring that potential losses arising from market risk remain within the appetite set by the Board:

- Value at Risk ("VaR"), Stressed Value at Risk ("SVaR"), and Incremental Risk Charge ("IRC") measures provide aggregate indicators of potential losses, subject to stated confidence levels and holding periods
- Risk factor sensitivities measure the impact of moves in each risk factor, allowing concentrations of risk to be identified and controlled
- Stress testing is used to monitor and control the exposure of the portfolio to extreme moves in market rates and prices. A range of stress tests is run, covering exposures to relevant market factors and scenarios in various market conditions
- Stop loss and drawdown limits monitor actual losses at MUS(EMEA), business unit, department, and trader level.

Day–to-day responsibility for the management of market risk resides with the Market Risk Management department, which is organisationally independent from the front office departments. The Risk Analytics Group is responsible for the design of new market risk management models. Daily market risk reports are prepared for senior management and trading departments using MUS(EMEA)'s in house and vendor systems.

The market risk capital requirement is measured using internal market risk models, where approved by the PRA, or under the Standardised Approach. MUS(EMEA)'s internal market risk models comprise VaR, SVaR, IRC, and Risks Not In VaR ("RNIV") which covers all major asset classes traded by MUS(EMEA).

The table below shows the market risk capital requirements.

Table 5: Market Risk Capital Requirements and RWAs

	30 Jun 2019		31 Dec 2018	
	Capital required £m	RWAs £m	Capital required £m	RWAs £m
VaR	31	393	34	424
Stressed VaR	109	1,359	108	1,344
Incremental Risk Charge	67	839	73	917
Risks Not In VaR	39	485	40	497
Other Market Risk	6	78	7	87
Total	**252**	**3,153**	**261**	**3,268**

8. Operational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk.

MUS(EMEA) manages and controls its exposure to operational risk through its policies and procedures, which are designed to ensure that it:

- Mitigates the risk of exposure to fraud
- Processes transactions correctly, accurately and on a timely basis
- Protects the integrity and availability of information processing facilities, infrastructure and data
- Maintains the confidentiality of its client information
- Employs appropriate numbers of skilled staff and complies with relevant employment laws and regulations
- Establishes workplace environments that are safe for both employees and visitors
- Reduces both the likelihood of an incident occurring and the impact should an incident occur.

MUS(EMEA) employs The Standardised Approach ("TSA") for calculating its Pillar 1 operational risk capital requirement. MUS(EMEA) is committed to adopting leading industry practices for managing and measuring operational risk, and has also developed a primarily scenario based capital model to determine whether it should hold any additional capital for operational risk.

The table below shows the operational risk capital requirements and RWAs.

Table 6: Operational Risk Capital Requirements and RWAs

	30 Jun 2019		31 Dec 2018	
	Capital required £m	RWAs £m	Capital required £m	RWAs £m
The Standardised Approach	**53**	**657**	**47**	**593**

9. Leverage Ratio

MUS(EMEA) assesses the leverage ratio to mitigate the risk of excessive leverage. MUS(EMEA) performs regular analysis of the leverage ratio to understand drivers and sensitivities. MUS(EMEA)'s leverage ratio exposure measure is mainly driven by securities financing transactions, derivatives and inventory. In addition, Tier 1 capital resources and any applicable deductions impact on the leverage ratio. Leverage ratio is reported to the Asset and Liability Committee ("ALCO") and the Board Risk Committee ("BRC").

The disclosure of the leverage ratio below is based on the end point CRR definition of Tier 1 capital and the CRR definition of leverage exposure. MUS(EMEA)'s leverage ratio is not affected by the exemption of qualifying central bank claims. Hence, there is no difference between the UK leverage ratio and the CRR leverage ratio.

The table below shows the leverage ratios.

Table 7: Leverage Ratio

	30 Jun 2019 £m	31 Dec 2018 £m
Tier 1 capital	1,530	1,421
Total leverage ratio exposures	63,934	55,891
Leverage ratio	**2.39%**	**2.54%**
Choice on transitional arrangements for the definition of the capital measure	Fully phased in	Fully phased in