SMBC NIKKO

SMBC NIKKO CAPITAL MARKETS LIMITED

Report and Financial Statements

31 December 2017

Company number 02418137

Company information

Registered number: 02418137
Incorporated with limited liability by shares in England and Wales

Directors

T Yazawa
A Yates
B Miura
T Imaeda
K Nakamura
J D Thomas
M Akiyama
N Okubo
P D Jackson (Independent Director)

Secretary

P Davé

Auditor

KPMG LLP
15 Canada Square
London E14 5GL

Banker

Sumitomo Mitsui Banking Corporation Europe Limited
99 Queen Victoria Street
London EC4V 4EH

Solicitor

Allen & Overy
One Bishops Square
London E1 6AO

Registered Office

One New Change
London EC4M 9AF

AUTHORISED AND REGULATED BY THE FINANCIAL CONDUCT AUTHORITY

Strategic report

The directors present the Group Strategic Report of SMBC Nikko Capital Markets Limited for the year ended 31 December 2017.

Principal activities

SMBC Nikko Capital Markets Limited Group ("the Group") is an investment business with derivatives and securities including business advisory divisions. It is part of a wider Sumitomo Mitsui Banking Corporation Group ("SMBC Group").

The Group consolidates the following legal entities:

- SMBC Nikko Capital Markets Limited ("the Company" or "CM Ltd"), company number 02418137 incorporated in England and Wales, an IFPRU investment firm authorised and regulated by the Financial Conduct Authority ("FCA"). Sumitomo Mitsui Banking Corporation ("SMBC") of Japan is the majority shareholder and controller. The Company has a representative office in Australia.
- SMBC Derivative Products Limited ("SMBC DP"), a wholly owned subsidiary of CM Ltd, which is a full scope investment firm incorporated in England and Wales, authorised and regulated by the FCA. It is structured as a bankruptcy remote derivative products company ("DPC") and has received a credit rating of Aa1 from Moody's Investors Service Inc. ("Moody's") and AA- from Standard & Poor's Ratings Group ("S&P"). SMBC DP's principal activities are the provision of interest rate and foreign exchange risk hedging products to customers seeking a highly rated counterparty and the provision, for a fee, of performance guarantees to its affiliate.
- SMBC Capital Markets (Asia) Limited ("CM Asia"), incorporated in Hong Kong and authorised and regulated by the Securities and Futures Commission. CM Asia acts as an agent and intermediary for the Company and its affiliated entities in Asian markets outside of Japan and in Australia.
- CM Ltd, SMBC DP and CM Asia together represent "the Group".

The Group's and the Company's derivatives business provides interest rate and foreign exchange hedging products to customers and the members of the wider SMBC Group. The securities activities are focussed on customer facilitation and maximising order flow in the primary and secondary debt and equity markets, with a particular focus on Japan. The repo business is primarily a customer service rather than a source of funding. The business advisory group provides advice and support to SMBC Group customers seeking new business opportunities.

The Group's and the Company's business plan for 2017 focussed on the incremental growth of existing business lines and the development of new products and services where there was an indication of client demand. The directors have considerably enhanced internal controls and governance processes to underpin sustainable business growth. Control of day-to-day business activities is exercised using appropriate measures, risk targets and limits, which define acceptable levels of risk covering all business and support activities. Monitoring of these activities is undertaken using an extensive suite of Key Risk Indicators ("KRIs") and Key Performance Indicators ("KPIs"), which have been selected for their ability to record fluctuations in individual risks. The KRIs are an important element within the management information packs presented to the Group's executive committee on a monthly basis.

KPI's

The primary KPI's monitored by management are: revenue and expenses, including comparison against budget, and capital adequacy, measured through the total capital ratio, below.

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	2017 Year on Year change	2016 Year on Year change
Net trading income increase	+ 2.8%	+ 8.2%
Operating expenses increase	+ 18.9%	+ 0.4%
Total capital ratio (Group)	42.0%	38.4%

Capital ratios are set out in Note 22, and have been maintained at levels that correspond with the Group and Company's risk appetite, as determined by the Board, throughout the year.

Corporate Governance

The Company is committed to the ongoing enhancement of its corporate governance framework to promote a culture of integrity, good conduct, ethical values and the operation of an effective internal control framework to maintain a disciplined operational environment which meets changing legal and regulatory requirements, client needs, shareholder interests and the Company's risk appetite.

In June 2017, the Board appointed an Independent Director, and a second Independent Director was appointed in January 2018.

The governance framework consists of:

- Executive Committees established by the Board comprising Board members and executive management to review and manage specific aspects of the Company's operations
- Corporate Policies to translate the corporate objectives, corporate risk appetite, legal and regulatory requirements and head office directives into the operational requirements for the various departments
- Procedures which document and define the daily and periodic processes, practices and actions that are performed to meet operational requirements, business needs and control objectives
- Internal controls - specific processes, tasks and activities performed by staff to provide reasonable assurance regarding the achievement of the objectives relating to business operations, reporting and compliance
- Regular meetings of the Board of Directors and the Executive Committees
- A 'Three Lines of Defence" model to risk management

The Board has established the following committees to facilitate the effective conduct of the business in accordance with the Company's corporate policies:

- Board Risk and Compliance Committee
- Executive Committee
- Audit Committee
- Remuneration Committee
- Nominations Committee

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The Company has also established various sub-committees to support the activities and responsibilities of the committees:

- Prudential Regulation Committee
- Risk Management Steering Committee
- Transaction Approval Committee
- New Product Committee
- Credit Committee
- Operational Risk Committee
- Liquidity Management Committee

Three Lines of Defence

The Group has adopted a "Three Lines of Defence" approach to financial risk management to ensure the adequate oversight of risks and to embed a culture of risk awareness throughout the organisation.

Each business function, and its respective head, is required to ensure that all business decisions maintain an appropriate balance between risk and return and are in accordance with the Group's and the Company's objectives and risk appetite. The business functions constitute the first line of defence ("1st LOD") and are responsible for identifying and managing risks directly and are accountable for both upside and downside outcomes. Each business function undertakes a regular risk self-assessment that is presented for executive management scrutiny.

The Risk and Compliance functions report to the Board, and make up the second line of defence ("2nd LOD") responsible for day-to-day risk identification, assessment and monitoring. This provides oversight and guidance as well as advising, facilitating and challenging the 1st LOD in their risk management activities and risk-return considerations. The Risk function ensures that the Board and senior management are duly informed and engaged.

The Internal Audit department constitutes the third line of defence ("3rd LOD") and provides independent assurance to the Board that the 1st and 2nd LODs are fit for purpose and that the risk-based information provided to the Board and management is accurate and reliable.

Principal risks and uncertainties

The Group has investment and ancillary services permissions relating to its business pursuant to the provisions of the Financial Services and Markets Act 2000 and the rules of the Financial Conduct Authority.

Risk Management

The Board has established the Board Risk and Compliance Committee (BRCC) with responsibility for providing oversight and advice to the Board on the current risk profile of the Group, its risk appetite and tolerance, the risk strategy, and the establishment and maintenance of an appropriate risk control framework. The BRCC includes independent non-executive directors as members and meets at least quarterly. It is responsible for providing oversight of:

- Adherence to the Risk Appetite,
- Implementation of Risk Strategy,
- Monitoring of Current risk exposures,
- Stress and Scenario Testing,

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- Capital Management,
- Liquidity Management, and
- Management of Large Exposures

The Group's and the Company's Risk Appetite Framework sets out the broad level of risks that are to be accepted in pursuit of its business goals and strategy. Underpinning this framework, day-to-day business activities are managed using appropriate measures, risk targets and limits, which are to be considered as defining acceptable levels of each category of risk under normal conditions and are set out within the specific policies and procedures in place across the organisation. A comprehensive risk assessment process is undertaken annually and fully documented in the Group's Internal Capital Adequacy Assessment Process ("ICAAP").

The principal risks and uncertainties facing the Group include credit and counterparty risk, liquidity risk, market risk, cash flow risk, operational risk and other risks, an overview of which is included in Note 18 to the financial statements.

Credit Risk and Counterparty Credit Risk

Credit risk is the risk of any losses to the Group arising from any credit events caused by a third party's inability or unwillingness, or a change in the market's perception of the third party's ability or willingness, to meet its obligations as they fall due.

Counterparty credit risk ("CCR") is the risk that the counterparty to a transaction could default before the final settlement of the transaction.

CCR is one of the most significant risks that the Group is exposed to.

Credit risk mitigation is a high priority for the Group's management and a variety of mitigants are employed, including:

- Collateral and netting agreements, which are actively pursued from the standpoint of both credit and liquidity risks. Collateral is predominantly in the form of cash, mainly in major currencies. Securities collateral is limited to high grade government bonds.
- Parental guarantees, which the Group and Company have purchased to cover specifically identified counterparty credit risks. Guarantee arrangements are set out in Notes 1 and 25.
- Strict credit control procedures and limits monitoring, which ensure that all front office staff incorporate a comprehensive credit assessment in their approach to pricing.

Another element of credit risk management is a rigorous quantitative valuation adjustment process based on scenario simulation and market-risk-adjusted probabilities of default. Such a system cannot by itself assure efficient pricing or monitoring of individual credit exposures but it is a strong incentive for proper trade-off of risk and return at the time of transaction, as well as providing an efficient incentive for assignment and termination of transactions later. The result of this calculation methodology is that the reserve for each name effectively reflects the market credit spread charged on the expected exposure to the counterparty at each time point. This is a good proxy for the transaction unwinding cost in the market. Management uses this reserve as a tool for credit monitoring on a portfolio basis, supplemented by reports from the Credit department, including breaking news of sharply deteriorating credits. Additionally, management reviews a series of reports on specific exposures identified as high risk.

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At each balance sheet date, the Group assesses whether financial and other assets, which are not accounted for at fair value through profit and loss, are impaired. As at 31 December 2017, no adjustments in respect of asset impairments were made (31 December 2016: $nil).

Liquidity Risk

Liquidity risk is the risk of loss or damage to the Group as a result of being unable to meet obligations when they fall due without incurring material costs in realising liquid assets. Liquidity risk arises primarily from the requirement to fund the securities balances and collateral calls on derivatives contracts.

Liquidity risk is mitigated by holding a liquid asset buffer ("LAB"), consisting of cash and highly liquid securities, to cover any unexpected cash outflows. The Group and Company measure and maintain liquidity ratios.

The Group monitors expected cash flows on its assets and liabilities to identify and address any funding gaps that may arise in the future. The funding requirements are met from its own resources, borrowing from its parent company and, occasionally, through repo market transactions. Potential funding risk is mitigated by a policy of holding significant positions in very high quality marketable securities that may be sold to cover any funding gaps. For stress testing purposes, reliance is placed only on a committed facility provided by SMBC.

Market Risk

Market risk is the risk of financial loss or damage to the Group's financial position caused by changes to market prices and other market values.

All trading instruments are subject to market risk, the potential that future changes in market conditions and other factors may create variation in the value of instruments, due to fluctuations in security prices, as well as interest and foreign exchange rates. Market risk is directly impacted by the volatility and liquidity in the markets in which the related underlying assets are traded. As the instruments are recognised at fair value, those changes directly affect reported income.

The Group has strict market risk limits for its derivative business which is predominantly undertaken on the basis that the market risk arising from customer trades is hedged either with a group company CM Inc., or a market counterparty, which substantially mitigates market risk in the derivatives business.

Market risk arises in both the primary underwriting activity and the secondary securities held for market making purposes. It is mitigated through the monitoring and enforcing of position limits and management of inventory holding periods. Market risk limits are reviewed regularly and are approved annually by the board, and are set out in an official Risk Appetite Statement.

Cash Flow Risk on Currency Expenses

Cash flow risk arises on expenses expressed in currencies other than the functional currency. The Group hedges its risk on GBP costs by entering into forward foreign exchange contracts which fix the exchange rate to US dollar, its functional and presentational currency. Accounting for cash flow hedges is described in Note 1.

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Operational Risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. Broadly, the definition excludes strategic and reputational risk, but does include risks from the wider regulatory environment including legal risk, compliance risk and, increasingly in matters of client interaction, conduct risk.

Regulatory risk, a significant factor for authorised and regulated investment firms, is the risk of non-compliance to existing regulations and that of changes to applicable regulations or laws having an adverse impact on the business.

Regulatory compliance includes a number of aspects, some of which (e.g. capital, liquidity levels) are managed together with the business risks described above and some (customer screening checks, treating customers fairly, sanctions compliance) are managed by dedicated teams. In 2017 and early 2018, regulatory compliance was enhanced through a number of measures, including the appointment of two independent non-executive directors to the Board; strengthening teams and processes in relation to regulatory reporting, risk management and compliance; and establishing an internal Prudential Regulation Committee to embed and better integrate processes such as ICAAP and Liquidity Adequacy Assessment within the firm's overall governance framework.

Conduct risk concerns potential detriment to the business, counterparties or employees caused by inappropriate judgements made in the course of business.

In applying this definition to its on-going operations, the Group monitors operational risk within its Risk Appetite and through the following core processes:

- Operational Risk Event reporting,
- Operational Risk and Control Self-Assessments, and
- Key Risk Indicator reporting.

Collectively, these processes help to identify the operational risk events that the Group is subject to and helps build a risk profile that is represented in the Group's Risk Register, as well as providing loss data and scenarios that are considered in the annual ICAAP process.

The Group seeks to minimise operational risk through clearly defined responsibilities for management and staff, comprehensive daily risk reporting and regular self-assessment of the operational framework to identify any weaknesses covering front office, credit risk management, settlements, finance, compliance, legal and systems functions.

Internal processes and controls are subject to regular verification by an independent internal audit function, reporting to the Board, which has full discretion over the particular processes and controls it chooses to review and the timing of any review.

Other Risks

Other closely monitored risks, all of which are reviewed and assessed at least annually, include the risk of additional collateral requirements in the event of SMBC's credit rating downgrade, concentration risk, wrong way risk (the risk that an exposure increases alongside the probability of the counterparty's failure), strategic risk and reputational risk.

Additionally the Group is exposed to macro-economic, geopolitical and other external business risks which include, but are not limited to, the uncertain economic environment, particularly in regards to an

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increasingly unstable geopolitical environment, and changes to the level and volatility of prices such as foreign exchange rates, credit spreads, commodity, equity prices or interest rates.

Business Environment

The Group operates in a highly regulated environment with significant additional requirements in respect of reporting, capital, liquidity, product design, customer service and other business areas, which come from multiple regulators in the countries where the Group offers its services. These regulations constantly change and evolve in response to periods of financial instability, new business practices, economic and political developments, becoming over the last few years more stringent and detailed in order to promote stability in financial markets.

The Group continues to operate in an environment of uncertainty with respect to the UK's withdrawal from the EU ("Brexit"). However, initial predictions of a major economic downturn have not materialised, though UK macro-economic indicators including economic growth, inflation, relative currency strength, interest rates, house prices and unemployment have shown mixed signals during 2017. However, this cautious and uncertain business environment has also presented opportunities which the Group has capitalised upon.

Market conditions in the wider global markets remained favourable for issuance of primary debt and equity securities and trading in the secondary markets and a number of significant mandates were secured by the Group. Furthermore, the rates environment allowed robust growth in the Derivatives business driven by client demand.

As a result, the financial performance of the Group has been steady with modest growth in net trading revenue in 2017. Operating cost increases in 2017 were largely driven by the Group's strategic plans and not directly related to the business environment.

The Group's strategic plans in response to the challenges and opportunities presented by Brexit are discussed below.

Brexit

Due to the formal notification to the EU of the UK's intention to withdraw from the EU pursuant to Article 50 of the Lisbon Treaty, the UK financial services industry may lose passporting rights granted to UK authorised financial institutions under the national transpositions of applicable EU law (in particular CRD IV as well as MiFID) which enabled them to freely provide banking business and financial services within the European Economic Area ("EEA").

The medium-term business plans of the Group have been updated to incorporate the Group's strategic response to Brexit. These plans have been developed in collaboration with the strategic plans of the Company's ultimate parent company, SMBC, to harness the combined resources of the group to meet client needs.

Using Brexit as an opportunity to further strengthen SMBC's business in the EEA, as a strategic response SMBC has established a new German based entity ("New CM") to operate as a cross-border passporting hub for securities and derivatives business with clients in all EEA jurisdictions, enabling the SMBC group as a whole to continue to provide the same level of financial services to all of its clients in the EEA.

The strategic position of the Company within the SMBC group allows the Company to both benefit from and contribute towards the business strategy of the wider group. The Company's business strategy continues to be focussed on organic growth in both its business units, which is largely driven by its UK

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customer base, and is significantly informed by SMBC Group's global strategy and the requirements of its client base.

Strategically, SMBC Group plans to continue providing the current suite of services to UK and European clients despite the impact of the UK's withdrawal from the European Union. In particular, it plans to expand its securities business services in the UK and continental Europe, with the Company and the New CM working in collaboration and with the global securities group. The Company will continue to focus upon diversifying its product offering and customer base.

By order of the Board

Antony Yates
Director
One New Change
London EC4M 9AF
Date: 19 April 2018

Directors' report

The directors present their report and the financial statements of SMBC Nikko Capital Markets Limited for the year ended 31 December 2017.

Business development and performance

The directors take into account a range of strategic, business and operational considerations when reviewing the performance of each business line. Such considerations include the efficient allocation and use of capital, earnings stability, balance sheet quality, operational robustness and the maintenance of good regulatory compliance.

Effectiveness is measured through the use of financial indicators such as budgeted revenue targets, new deal revenue and return on capital and also non-financial indicators such as conduct considerations, compliance with relevant internal and external rules and targets and the setting of measurable goals for all employees through a comprehensive assessment process. The directors pay particular attention to management information relating to regulatory capital, leverage and liquidity.

Net trading income of $227.6m for the Group in 2017 represents a 2.8% increase on the previous year and was achieved despite the uncertainties arising from Brexit, a rising interest rate environment with tapering of asset purchases by Central banks and reflects the Group's business plan to develop and diversify business revenues and profitability in a sustained manner.

During 2017, in accordance with its business plans, the Group invested in its client offering capability and also in the ongoing enhancement of its governance, control and risk management framework. This is reflected in a 21% increase in the number of Group employees in 2017 and the increase in operating costs which resulted in a reduction in operating profit for the year. Despite this, the Group reported a profit before tax of $71.8m for the year ended 31 December 2017.

Balance sheet assets and liabilities at the end of 2017 show continued balance sheet growth in securities, collateral and cash balances arising from business development in both the securities and the derivatives divisions, while the overall balance sheet showed a reduction due to lower repo levels. The financial position of the Group and the Company at the end of the year was satisfactory.

Results and dividends

The Group profit for the year, after taxation, amounted to $59.2 million (2016 - $79.1 million). No dividend was paid in the year and none has been declared (2016 - $nil).

Going Concern

Management believe that there are no material uncertainties related to events or conditions that may cast significant doubt upon the ability of the Company or the Group to continue as a going concern. The financial statements have been prepared on a going concern basis.

Directors' report

Future developments

The Company holds an important strategic position within the Sumitomo Mitsui Banking Corporation Group and despite the UK's withdrawal from the European Union the Company and Group remain committed to implementing its medium-term business plans to invest in the strengthening of its client offering to meet the diverse needs of clients, to develop and diversify revenue opportunities and sustainable profitability, and the ongoing development of its governance and control framework.

Directors

The directors who served during the year and at the date of this report were as follows:

T Yazawa

A Yates

B Miura

N Okubo (appointed 9 May 2017)

T Imaeda

K Nakamura

J D Thomas

M Akiyama

Y Tsutsumi (resigned 23 March 2017)

P D Jackson (appointed 13 June 2017)

Stephen Souchon was appointed as Independent Director on 25 January 2018, after the reporting date but before the date of signing.

The Company maintains directors' and officers' liabilities insurance cover for its directors and officers as permitted by its Articles of Association and the Companies Act 2006. Such insurance policies were reviewed during the period and remain in force.

Disclosure of information to the auditor

The Directors who held office at the date of approval of this Directors' report confirm that so far as they are each aware there is no relevant audit information of which the Company's auditor is unaware, and each Director has taken all steps that he ought to have taken as a Director to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Directors' report

Auditor

In accordance with section 487 of the Companies Act 2006, an elective resolution is in place that dispenses with the obligation to appoint an auditor annually. As a consequence, KPMG LLP continues to hold the position as the Company's auditor.

By order of the Board

Antony Yates
Director
One New Change
London EC4M 9AF
Date: 19 April 2018

Statement of directors' responsibilities

in respect of the annual report, strategic report, the directors' report and the financial statements

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

Company law requires the directors to prepare group and parent company financial statements for each financial year. Under that law they have elected to prepare both the group and the parent company financial statements in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU) and applicable law.

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 group and parent company and of their profit or loss for that period. In preparing each of the group and parent company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- assess the group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect 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 UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Independent auditor's report

to the members of SMBC Nikko Capital Markets Limited

Opinion

We have audited the financial statements of SMBC Nikko Capital Markets Limited ("the Company") for the year ended 31 December 2017 which comprise the group income statement, group statement of comprehensive income, group statement of financial position, company statement of financial position, group statement of changes in equity, company statement of changes in equity, group statement of cash flows, company statement of cash flows and related notes, including the accounting policies in note 1.

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2017 and of the group's profit for the year then ended;
- the group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We have fulfilled our ethical responsibilities under, and are independent of the group in accordance with, UK ethical requirements including the FRC Ethical Standard. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion.

Going concern

We are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least twelve months from the date of approval of the financial statements. We have nothing to report in these respects.

Strategic report and directors' report

The directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

- we have not identified material misstatements in the strategic report and the directors' report;
- in our opinion the information given in those reports for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

Matters on which we are required to report by exception

Under the Companies Act 2006, we are required 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 financial 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.

We have nothing to report in these respects.

Directors' responsibilities

As explained more fully in their statement set out on page 13, the directors are responsible for: the preparation of the financial statements and for being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

The purpose of our audit work and to whom we owe our responsibilities

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.

Simon Clark (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants

15 Canada Square
London E14 5GL
United Kingdom

Date: 19 April 2018

Group statement of profit or loss

for the year ended December 31, 2017

	Notes	*2017* *US$m*	*2016* *US$m*
Net trading income	2	227.6	221.3
Interest income	4	57.4	37.5
Interest expense	5	(52.8)	(27.6)
Total income		232.2	231.2
Staff costs	6, 7	(81.4)	(77.8)
Depreciation and amortisation	15, 16	(3.5)	(3.0)
Other operating expenses	3	(76.9)	(55.3)
Operating expenses		(161.8)	(136.1)
Operating profit		70.4	95.1
Non-trading interest income		1.4	0.5
Profit before taxation		71.8	95.6
Taxation	8	(12.6)	(16.5)
Profit for the financial year		59.2	79.1
Profit for the financial year (Company)		51.0	78.9

Group profit for the financial year is entirely attributable to the equity holders of the Parent. All results are from continuing operations.

The notes on pages 24 to 80 form an integral part of these financial statements.

Group statement of comprehensive income

for the year ended December 31, 2017

	Notes	*2017 US$m*	*2016 US$m*
Profit for the financial year		59.2	79.1
Other comprehensive income, net of tax			
Items that will never be reclassified to profit and loss:			
Actuarial (losses) arising on a defined benefit pension plan, net of tax	9	(0.1)	(0.6)
Items that are reclassified to other reserves:			
Net gains/(losses) from cash flow hedges		1.9	(1.4)
Total comprehensive income for the year attributable to equity holders of the Group		61.0	77.1

The notes on pages 24 to 80 form an integral part of these financial statements.

Group statement of financial position

for the year ended December 31, 2017

	Notes	2017 US$m	2016 US$m
Assets			
Cash at banks	10	846.0	458.6
Trading securities	11	1,376.2	704.0
Other trading assets, at fair value		76.6	30.3
Derivative assets	12	7,036.7	7,336.7
Securities purchased under agreements to resell	13	3,650.9	5,537.3
Other debtors	14	3,087.2	2,921.4
Intangible assets	15	2.0	-
Property, plant and equipment	16	10.9	11.0
Deferred tax asset	8	1.0	1.9
Total assets		16,087.5	17,001.2
Liabilities			
Derivative liabilities	12	7,005.2	7,337.5
Other trading liabilities, at fair value		176.0	112.2
Trading securities sold, not yet purchased		681.8	304.0
Securities sold under agreements to repurchase	13	2,998.0	5,199.0
Other creditors	17	3,538.2	2,421.7
Pension scheme liability	9	3.0	2.5
Total liabilities		14,402.2	15,376.9
Net assets		1,685.3	1,624.3
Equity attributable to equity holders of the parent			
Called up share capital	20	1,139.0	1,139.0
Share premium		165.0	165.0
Retained earnings		382.2	323.0
Other reserves		(0.9)	(2.7)
Total equity		1,685.3	1,624.3

The notes on pages 24 to 80 form an integral part of these financial statements.

The financial statements were approved by the Board of Directors on 19 April 2018 and were signed on its behalf by:

Antony Yates
Director
Company number 02418137

Company statement of financial position

for the year ended December 31, 2017

	Notes	2017 US$m	2016 US$m
Assets			
Cash at banks	10	702.3	330.6
Trading securities	11	1,284.3	608.4
Other trading assets, at fair value		76.6	30.3
Derivative assets	12	7,023.0	7,319.6
Securities purchased under agreements to resell	13	3,650.9	5,537.3
Other debtors	14	3,089.1	2,920.3
Investment in subsidiary undertaking	28	202.0	202.0
Intangible assets	15	2.0	-
Property, plant and equipment	16	10.8	10.9
Deferred tax asset	8	1.0	1.9
Total assets		16,042.0	16,961.3
Liabilities			
Derivative liabilities	12	6,992.5	7,321.9
Other trading liabilities, at fair value		176.0	112.2
Trading securities sold, not yet purchased		681.8	304.0
Securities sold under agreements to repurchase	13	2,998.0	5,199.0
Other creditors	17	3,535.1	2,418.9
Pension scheme liability	9	3.0	2.5
Total liabilities		14,386.4	15,358.5
Net assets		1,655.6	1,602.8
Equity attributable to equity holders of the parent			
Called up share capital	20	1,139.0	1,139.0
Share premium		165.0	165.0
Retained earnings		352.5	301.5
Other reserves		(0.9)	(2.7)
Total equity		1,655.6	1,602.8

The notes on pages 24 to 80 form an integral part of these financial statements.

Group statement of changes in equity

for the year ended December 31, 2017

	Notes	Called up share capital US$m	Share premium US$m	Retained earnings US$m	Other reserves: Pension reserve US$m	Other reserves: Cash flow hedges reserve US$m	Total equity US$m
At 1 January 2016		1,139.0	165.0	243.9	(0.7)	-	1,547.2
Profit for the year		-	-	79.1	-	-	79.1
Actuarial losses arising on a defined benefit pension plan, net of tax	9	-	-	-	(0.6)	-	(0.6)
Net losses arising on cash flow hedges		-	-	-	-	(1.4)	(1.4)
Total comprehensive income for the period		-	-	79.1	(0.6)	(1.4)	77.1
At 31 December 2016		1,139.0	165.0	323.0	(1.3)	(1.4)	1,624.3
At 1 January 2017		1,139.0	165.0	323.0	(1.3)	(1.4)	1,624.3
Profit for the year		-	-	59.2	-	-	59.2
Actuarial losses arising on a defined benefit pension plan, net of tax	9	-	-	-	(0.1)	-	(0.1)
Net gains arising on cash flow hedges		-	-	-	-	1.9	1.9
Total comprehensive income for the period		-	-	59.2	(0.1)	1.9	61.0
At 31 December 2017		1,139.0	165.0	382.2	(1.4)	0.5	1,685.3

The notes on pages 24 to 80 form an integral part of these financial statements.

Company statement of changes in equity

for the year ended December 31, 2017

	Notes	Called up share capital US$m	Share premium US$m	Retained earnings US$m	Other reserves: Pension reserve US$m	Other reserves: Cash flow hedges reserve US$m	Total equity US$m
At 1 January 2016		1,139.0	165.0	222.6	(0.7)	-	1,525.9
Profit for the year		-	-	78.9	-	-	78.9
Actuarial losses arising on a defined benefit pension plan, net of tax	9	-	-	-	(0.6)	-	(0.6)
Net losses arising on cash flow hedges		-	-	-	-	(1.4)	(1.4)
Total comprehensive income for the period		-	-	78.9	(0.6)	(1.4)	76.9
At 31 December 2016		1,139.0	165.0	301.5	(1.3)	(1.4)	1,602.8
At 1 January 2017		1,139.0	165.0	301.5	(1.3)	(1.4)	1,602.8
Profit for the year		-	-	51.0	-	-	51.0
Actuarial losses arising on a defined benefit pension plan, net of tax	9	-	-	-	(0.1)	-	(0.1)
Net gains arising on cash flow hedges		-	-	-	-	1.9	1.9
Total comprehensive income for the period		-	-	51.0	(0.1)	1.9	52.8
At 31 December 2017		1,139.0	165.0	352.5	(1.4)	0.5	1,655.6

The notes on pages 24 to 80 form an integral part of these financial statements.

Group statement of cash flows

for the year ended December 31, 2017

	Notes	2017 US$m	2016 US$m
Cash flows from operating activities			
Profit for the financial year		59.2	79.1
Adjustments to reconcile net income to net cash from operating activities:			
Depreciation and amortisation	15, 16	3.5	3.0
Tax expense	8	12.6	16.5
Change in trading securities and repurchase contracts		(608.6)	123.5
Change in trading assets, at fair value		(46.3)	(11.2)
Change in trading liabilities, at fair value		63.8	9.5
Change in other debtors		(172.8)	(687.0)
Change in derivative assets	12	300.0	(1,665.5)
Change in deferred tax assets	8	0.9	(1.0)
Change in derivative liabilities	12	(332.3)	1,628.8
Change in other creditors		1,116.5	855.2
Net gains/(losses) arising on cash flow hedges		1.9	(1.4)
Corporation tax paid	23	(5.6)	(11.3)
Net cash provided by operating activities		333.6	259.1
Cash flows from investing activities			
Purchase of intangible assets	15	(2.1)	-
Purchase of property, plant and equipment	16	(3.3)	(0.2)
Net cash outflow from investing activities		(5.4)	(0.2)
Net change in cash		387.4	338.0
Cash and cash equivalents at beginning of year	10	458.6	120.6
Cash and cash equivalents at end of year	10	846.0	458.6
Net increase in cash		387.4	338.0

The notes on pages 24 to 80 form an integral part of these financial statements.

Company statement of cash flows

for the year ended December 31, 2017

	Notes	2017 US$m	2016 US$m
Cash flows from operating activities			
Profit for the financial year		51.0	78.9
Adjustments to reconcile net income to net cash (used in) operating activities:			
Depreciation and amortisation	15, 16	3.4	3.0
Tax expense		11.1	16.2
Change in trading securities and repurchase contracts		(612.3)	108.4
Change in trading assets, at fair value		(46.3)	(11.2)
Change in trading liabilities, at fair value		63.8	9.5
Change in other debtors		(174.3)	(686.7)
Change in derivative assets	12	296.6	(1,675.8)
Change in deferred tax assets	8	0.9	(1.0)
Change in derivative liabilities	12	(329.4)	1,638.9
Change in other creditors		1,116.2	854.4
Net gains/(losses) arising on cash flow hedges		1.9	(1.4)
Corporation tax paid	23	(5.6)	(11.3)
Net cash provided by operating activities		326.0	243.0
Cash flows from investing activities			
Purchase of intangible assets	15	(2.1)	-
Purchase of property, plant and equipment	16	(3.2)	(0.1)
Net cash outflow from investing activities		(5.3)	(0.1)
Net change in cash		371.7	321.8
Cash and cash equivalents at beginning of year	10	330.6	8.8
Cash and cash equivalents at end of year	10	702.3	330.6
Net increase in cash		371.7	321.8

The notes on pages 24 to 80 form an integral part of these financial statements.

Notes to the financial statements

for the year ended December 31, 2017

1. Accounting policies

Reporting entity

These financial statements are prepared for SMBC Nikko Capital Markets Limited ("the Company") and its subsidiaries, SMBC Derivative Products Limited and SMBC Capital Markets Asia Limited (together "the Group"), under Section 399 of the Companies Act 2006. The Company is domiciled in England and Wales with the registered office as stated on page 1 and principal activities as set out in the strategic report.

Basis of consolidation

The Group consolidates all entities it controls. Control is judged to exist where the Group has the power to direct the relevant activities of an entity so as to obtain variable returns from its activities. In assessing control, the Group takes into consideration any potential voting rights that are currently exercisable.

Basis of preparation

The Group financial statements have been prepared under the historical cost convention except as set out below for the valuation of the derivative products, trading assets, trading liabilities, trading securities, and pension liabilities and in accordance with applicable accounting standards. Securities purchased under agreements to resell and securities sold under agreements to repurchase are not fair valued. The Directors have undertaken an assessment of the appropriateness of preparing the financial statements on a going concern basis and have concluded that there are no material uncertainties related to events or conditions that may cast significant doubt as to the ability of the Group to continue as a going concern.

Statement of compliance

Both the Group financial statements and the Company financial statements have been prepared and approved by the directors in accordance with International Financial Reporting Standards (IFRS) adopted by the European Union. Prior year reclassifications are recorded where applicable to conform to changes in current year presentation.

Company profit and loss account

On publishing the parent company financial statements here together with the Group financial statements, the Company is taking advantage of the exemption in s408 of the Companies Act 2006 not to present its individual income statement and related notes that form a part of these approved financial statements. The profit dealt with in the financial statements of the Company was $51.0 million in the year ended 31 December 2017 and a profit of $78.9 million in the year ended 31 December 2016.

Preparation of financial statements in US dollars

The directors consider the functional currency of the Group's activities to be US dollars since the majority of the Company's income is generated in this currency. The directors have chosen to use US dollars as the presentational currency. All financial information is presented in US$ millions and has been rounded to one decimal point unless indicated otherwise.

Foreign currency translation

Foreign currency assets and liabilities are translated into US dollar equivalents at rates of exchange ruling at the balance sheet date. Gains and losses resulting from re-measurement into US dollar equivalents are reflected in the Group income statement within net trading profit.

Notes to the financial statements

for the year ended December 31, 2017

Segmental analysis

Segmental analysis of income and net assets has not been prepared because the Group is outside of the scope of reporting per IFRS 8 - Operating Segments. The Group's own equity instruments are not traded in a public market and it is not in the process of issuing any class of instrument in a public market.

Interest income

Interest income is earned on trading securities and cash at banks. Interest income is recorded at the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset.

Fee and commission income

Fees and commissions income for services provided by the Group on securities transactions and advisory business is recognised on completion of the underlying transaction.

Intermediation fees

Where the Group receives an intermediation fee from its affiliate SMBC Capital Markets, Inc. ("CM Inc.") for a derivative transaction with an unaffiliated counterparty, the fees are recognised as the present value of estimated future cash flows on a trade date basis.

Fees charged by affiliates

The Group pays fees to SMBC and CM Inc. for support services, which include trade execution, product control, marketing, risk management, planning, system development and others. The fees are recognised as an expense when incurred.

Pension costs

The Group operates a defined benefit pension plan and a defined contribution plan, both of which require contributions to be made to separately administered funds.

Payments to the defined contribution pension scheme are recognised within staff costs in profit or loss as incurred.

Defined benefit scheme expenses recognised within staff costs consist of service costs attributable to the current and past periods, interest on plan liabilities and return on plan assets.

The obligation under the defined benefit plan at the reporting date is determined by independent actuarial valuation using the projected unit method.

The actuarial valuation involves making assumptions about discount rates, expected rates of return on assets, future salary increases, mortality rates and future pension increases. Any actuarial gains and losses are recognised net of tax in other comprehensive income.

All assumptions are reviewed at each reporting date. In determining the appropriate discount rate management considers the interest rates of high quality corporate bonds, in this case AA rated. The mortality rate is based on publicly available mortality tables in the UK. Future salary increases and pension increases are based on expected future inflation rates in the UK. Further details about the assumptions are given in note 9. Due to the long term nature of this plan, such estimates are subject to significant uncertainty.

Notes to the financial statements

for the year ended December 31, 2017

Intangible assets

Intangible assets are stated at capitalised cost less accumulated amortisation and accumulated impairment losses. The carrying values of intangible assets are reviewed for impairment at each reporting date and when events or changes in circumstances indicate that the carrying value may not be recoverable.

External expenditure on intangible assets is capitalised as incurred. Internal expenditure is recognised as an asset when the company is able to demonstrate its intention and ability to complete the development and use the software in a manner which will generate future economic benefits, and can reliably measure the costs to complete the development. At the reporting date, intangible assets consisted of external expenditure. The Group had no capitalised internal expenditure.

Intangible assets are amortised on a straight-line basis over their estimated useful lives as follows:

Computer software	3 years

Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and any losses for impairment. Cost includes the original purchase price of the asset and the costs directly attributable to bringing the asset into its working condition.

Depreciation is provided on the depreciable amount of items of property plant and equipment on a straight-line basis over their estimated useful economic lives. The depreciable amount is the gross carrying amount less the estimated residual value at the end of its useful economic life. The Group and the Company use the following annual rates in calculating depreciation:

Leasehold assets:	
Leasehold property	Over the remaining life of the lease
Costs of adaption of leasehold property	Over the remaining life of the lease
Other	
Computers and similar equipment	3 years
Fixtures, fittings and other equipment	5 years

When deciding on useful economic life the principal factors taken into consideration are the expected rate of technological change and the expected pattern of usage of the assets.

Cash and cash equivalents

Cash comprises demand deposits and short-term money market deposits of three months or fewer from the date of acquisition.

Deferred taxation

Deferred tax is provided using the liability method on temporary differences at the balance sheet date between the value of assets and liabilities for tax purposes and their carrying amounts for financial reporting purposes. Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Leasing

A lease is classified as an operating lease if it does not transfer substantially all the risk and rewards incidental to ownership. The Group classifies its office space rental as an operating lease since the risks and rewards mainly lie with the lessor. In addition, the lease term does not constitute a major part of the economic life of

Notes to the financial statements

for the year ended December 31, 2017

the building. Rentals paid under operating leases are charged to income on a straight line basis over the term of the lease.

Trading securities

Under IAS 39, an entity shall recognise a financial asset or a financial liability in its statement of financial position when, and only when, the entity becomes a party to the contractual provisions of the instrument.

IAS 39 permits a choice between trade date and settlement date accounting for recording regular way transactions. In accordance with IAS 39 when applying settlement date accounting it is still required that any movements in fair value between trade date and settlement date are reflected as they occur. The movement in fair value will be taken to profit and loss or to other comprehensive income depending upon the classification of the asset. The company uses settlement date accounting consistently.

Derivative assets and liabilities

Derivatives are initially measured at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at their fair value. Changes in the fair value are recognised immediately in the income statement except for derivatives that are used as cash flow hedges, which are recognised in other comprehensive income.

Trading assets and liabilities

Fixed income financial instruments included in trading assets and trading liabilities represent contractual agreements with counterparties that provide fixed or variable periodic payments from a stated or contingent date over a specified time period. The Group records these fixed income financial instruments at fair value. Unrealised gains and losses due to changes in fair value are included in trading profit/ (loss) in the accompanying Group income statements.

Fair Value

The Group assumes that the asset or liability is exchanged in an orderly transaction between market participants to sell the asset or transfer the liability at the measurement date under current market conditions either: (a) in the *principal market* for the asset or liability; or (b) in the absence of a principal market, in the *most advantageous market* for the asset or liability. That assumed transaction establishes a basis for determining the exit price.

The Group manages the credit and liquidity risks in their derivatives portfolio on a net basis. The Group provides fair value information on its derivative portfolio on a net basis to management. Therefore, the Group makes adjustments to the valuation of their derivatives by calculating credit and debit valuation adjustments consistent with IFRS 13 and measures the fair value of the derivative portfolio on a net basis (i.e. the unit of account is the entire portfolio).

Securities sold under agreement to repurchase and securities purchase under agreement to resell

In the ordinary course of business, the Group sells securities under agreements to repurchase them at a predetermined price ("repos"). Since substantially all of the risks and rewards (generally considered to be at least 90%) are retained by the Group, the securities remain on the consolidated statement of financial position and a liability is recorded in respect of the consideration received. On the other hand, the Group buys securities under agreements to resell them at a predetermined price ("reverse repos"). Since the Group does not obtain substantially all of the risks and rewards of ownership, these transactions are treated as collateralised loans and the securities are not included in the Group statement of financial position. These collateralised loans are carried at amortised cost.

Notes to the financial statements

for the year ended December 31, 2017

Securities borrowed or received as collateral are not recognised in the statement of financial position, unless these are sold to third parties, at which point the obligation to repurchase the securities is recorded as a trading securities sold, not yet purchased, at fair value and any subsequent gain or loss is included in "Net trading profit" in the Group statement of comprehensive income.

Credit guarantees

The Group entered into an unconditional guarantee with its parent Sumitomo Mitsui Banking Corporation ("SMBC"), acting through its Cayman and Tokyo branches (the 'Guarantor'), which guarantees the prompt and complete payment when due of any net termination payment payable to the Group under any of the ISDA Master Agreements of specific guaranteed counterparties. Having such an agreement in place means that any required credit valuation adjustment is calculated based upon the probability of the double-default of both the Counterparty and the Guarantor. A monthly fee is payable based on the average value of the guaranteed transactions. The fee has been accounted for in line with the substance of the credit guarantee. It has been computed on a fair value basis, discounted to its present value and recorded as a derivative liability on the balance sheet.

Cash flow hedges

The Company uses cash flow hedges to reduce the foreign exchange risk on the Company's forecast monthly GBP expenses during the financial year.

For cash flow hedges, any forecast transactions included must be highly probable and must present an exposure to variations in cash flows that could affect the profit and loss.

For qualifying cash flow hedges, the effective portion of the change in the fair value of the hedging derivative is recognised in other comprehensive income in the same periods during which the hedged item affects profit or loss. Any ineffective portion of the hedge is immediately recognised in profit or loss.

Significant accounting judgements and estimates

In the process of applying the Group's accounting policies, management has exercised judgement and estimates, gauged in accordance with industry best practice, when determining the amounts recognised in the financial statements in relation to the fair value of derivative assets and liabilities and credit guarantees.

Estimates use uncertain information and sometimes subjective assumptions to measure carrying values. As a result, estimates bear a risk of material adjustments to the carrying amounts in subsequent accounting periods.

Judgments do not usually directly address measurement. The management exercises judgements when accounting standards allow a range of possible measurement methods. A different judgement might lead to a materially different accounting treatment or valuation.

Estimates are used where the fair value of derivative assets and liabilities cannot be derived from active markets and is determined using a variety of valuation techniques that employ mathematical models.

The inputs to these models use observable market data where possible but, where observable market data is not available, unobservable inputs are used. The estimates include considerations of liquidity and model inputs such as volatility for longer dated derivatives. Judgement was exercised as to whether unobservable inputs constitute a significant part of the total value of derivative instruments and therefore the level at which the instruments should be classified in the fair value hierarchy.

Credit Valuation Adjustments ("CVA") and Debit Valuation Adjustments ("DVA") are incorporated into derivative valuations to reflect the value of counterparty and own credit risk. CVAs, calculated on a counterparty exposure basis across instrument type, are derived from market data and management estimates of exposure at default, probability of default and recovery rates. The DVA is an adjustment to the value of the Group's derivative liabilities that seeks to reflect the Group's own default risk, which involves similar estimates of exposure at default, probability of default and recovery rates.

Notes to the financial statements

for the year ended December 31, 2017

Judgement was exercised in respect of the methodology for valuing the Group's collateralised derivative contracts. The management has chosen to use, in line with market practice, the Overnight Indexed Swap curve ("OIS") in order to more consistently manage the associated interest rate and funding risks.

The funding fair value adjustment ("FVA") is calculated by applying future market funding spreads to the expected future funding exposure of any uncollateralised component of the OTC derivative portfolio. This includes the uncollateralised component of collateralised derivatives in addition to derivatives that are wholly uncollateralised. The expected future funding exposure is calculated by a simulation methodology, where available. The expected future funding exposure is adjusted for events that may terminate the exposure such as the default of the company or the counterparty.

The present value of future fees payable for credit guarantees that Group has purchased from SMBC, is recognised on the balance sheet and calculated with reference to the expected exposure of the derivative transactions. As the valuation involves a number of estimates, actual results may materially differ from the reported values.

Future accounting developments

The IASB has issued the following standards which have been endorsed by the EU:

IFRS 9 Financial Instruments

The new standard replaces IAS 39 Financial Instruments: Recognition and Measurement and becomes effective for annual periods beginning on or after 1 January 2018. IFRS 9 introduces new rules on classification, measurement, impairment and hedge accounting.

According to the new standard, financial assets will be classified as measured at either: i) amortised cost, ii) fair value through other comprehensive income or iii) fair value through profit or loss. The classification decision is made on the basis of cash flow characteristics and the entity's purpose for managing the specific financial asset. Debt instruments whose cash flows consist solely of payments of principal and interest are allocated to one of these categories depending whether they are held to collect contractual cash flows, both collect cash flows and sell or other purposes, such as trading or value appreciation. Equity shares and other instruments whose cash flows are not solely payments of principal and interest must be measured at fair value through profit or loss, regardless of the purpose. The entity may, at initial recognition, irrevocably designate any financial assets at fair value through profit or loss if it eliminates or significantly reduces an accounting mismatch. The entity can also make an irrevocable election to measure non-trading equity instruments at fair value through other comprehensive income.

Financial liabilities are classified at amortised cost or fair value through profit or loss when they are held for trading or designated as such on initial recognition.

IFRS 9 changes impairment testing from an incurred loss model to expected credit loss approach. It requires recognising either 12-month or lifetime expected credit losses, depending on whether the asset has low, significantly increased or high credit risk (credit-impaired). It introduces further criteria for determining significant increase and high credit risk, including rebuttable presumptions of a significant increase in credit risk for instruments over 30 days in arrears and high credit risk for instruments over 90 days in arrears. New impairment rules apply to assets measured at amortised cost, fair value through other comprehensive income, lease receivables, financial guarantees and loan commitments.

Hedge accounting remains broadly similar with the existing approach. IFRS 9 streamlines hedging with economic reasons and relaxes effectiveness criteria. It also allows to keep IAS 39 hedge accounting for either portfolio fair value hedging or all hedges.

In preparation for the new accounting regulations, the Company has assessed the impact of IFRS 9 on its financial statements and off-balance sheet guarantees as at 1 January 2018. The assessment has concluded that introduction of IFRS 9 will not produce any material changes in carrying values or measurement methods of its financial assets and liabilities. Certain debt instruments, held for liquidity purposes and currently measured at fair value, would fall under IFRS 9 into the amortised cost category. However, the Company intends to designate these instruments at fair value, as permitted by the new standard.

Notes to the financial statements

for the year ended December 31, 2017

The new impairment rules result in an additional impairment provision and reduction in reserves of $0.1 million as at 1 January 2018. As permitted by IFRS 9, the Company intends to recognise transitional adjustments directly in equity as at 1 January 2018, without restating comparative figures.

IFRS 15 Revenue from Contracts with Customers
The new standard replaces IAS 11 Construction Contracts, IAS 18 Revenue, related interpretations and becomes effective on 1 January 2018. It provides a comprehensive, principle-based model for recognising revenue from most types of contracts.

IFRS 15 introduces the definition of 'performance obligations' as a key component of a contract and five steps for revenue recognition. In order to recognise revenue, the entity should: 1) identify the contract; 2) identify the performance obligations; 3) determine the transaction price; 4) allocate the price to the performance obligations; and 5) recognise revenue as or when it satisfies its performance obligations.

The Company has assessed the accounting impact of IFRS 15 on its income from fees, commissions, intermediation and advisory services, and expects no material impact on its financial statements due to the adoption of IFRS 15.

IFRS 16 Leases
The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer (lessee) and the supplier (lessor). IFRS 16 replaces the previous lease standard, IAS 17 leases, and related interpretations. IFRS 16 is effective for annual reporting periods beginning on or after 1 January 2019. A company can choose to apply IFRS 16 before that date but only if it also applies IFRS 15 Revenue from Contracts with Customers. The Company is evaluating the effect of this new standard on its financial statements.

Notes to the financial statements

for the year ended December 31, 2017

2. Net trading income

This comprises the following items of income and expense:

	2017 *US$m*	*2016* *US$m*
Trading gain on derivative instruments	102.6	80.5
Derivatives reserves	11.3	30.0
Gains on primary and secondary trading	41.9	39.0
Underwriting and arrangement fees	72.4	73.0
Centralised activities	(0.6)	(1.2)
	227.6	221.3

Due to the global nature of the international capital markets, the directors consider that the disclosure of net trading income by geographical source would not be meaningful.

3. Other operating expenses

Other operating expenses include

	2017 *US$m*	*2016* *US$m*
Auditor remuneration		
audit fees to KPMG LLP	0.4	0.4
audit related service fees to KPMG LLP	0.2	0.2
credit rating assurance fees to KPMG LLP NY	0.3	0.3
	0.9	0.9
Operating lease rentals - land and buildings	3.7	4.6

Audit fees relate to the audit of the financial statements. Audit-related services include CASS assurance and quarterly financial reviews.

Notes to the financial statements

for the year ended December 31, 2017

4. Interest income

	2017 US$m	2016 US$m
Interest on collateral	28.6	20.4
Interest on repo transactions	21.3	15.2
Interest on securities	7.5	1.9
	57.4	37.5

5. Interest expense

	2017 US$m	2016 US$m
Interest on collateral	25.0	13.1
Interest on repo transactions	17.0	10.8
Interest on borrowings	10.8	3.7
	52.8	27.6

6. Staff costs

		Note	2017 US$m	2016 US$m
Wages and salaries			61.9	60.7
Social security costs			5.5	5.4
Pension costs:	Defined benefit scheme	9	0.2	0.2
Pension costs:	Defined contribution scheme		3.9	3.5
Other staff costs			9.9	8.0
			81.4	77.8

Notes to the financial statements

for the year ended December 31, 2017

The average monthly number of Group and Company employees during the year was 289 (2016 - 239) and 275 (2016 - 224) respectively.

7. Directors' emoluments

	2017	*2016*
	US$m	*US$m*
Emoluments	3.2	3.2
Group pension contributions	-	-
Total	3.2	3.2

	2017	*2016*
	US$m	*US$m*
Emolument of highest paid director	1.4	1.9
Group pension contributions	-	-
Total	1.4	1.9

The highest paid director belonged to the Group's defined benefit pension scheme with the Group's contribution of $30 thousand (2016 - one director with contribution of $28 thousand) in the year. These amounts are included within the directors' emoluments figures above. See note 9 for more details.

Four directors received a bonus (2016 - three directors).

Notes to the financial statements

for the year ended December 31, 2017

8. Taxation

	2017	2016
	US$m	*US$m*
Current tax		
Current year	13.8	14.7
Adjustments for prior years	(2.7)	2.3
Foreign tax suffered	2.2	-
Double tax relief	(1.0)	-
Current tax charge	12.3	17.0
Deferred tax		
Origination and reversal of temporary difference	0.2	(0.2)
Change in tax rate	-	(0.3)
Adjustment for prior years	0.1	-
Deferred tax charge / (credit)	0.3	(0.5)
Total tax charge in income statement	12.6	16.5

Disclosure of tax in other comprehensive income

	2017		2016	
	Before tax	*Net of tax*	*Before tax*	*Net of tax*
	US$m	*US$m*	*US$m*	*US$m*
Actuarial (losses) on defined benefit pension plan	(0.1)	(0.1)	(0.8)	(0.6)
Cash flow hedges	2.5	1.9	(1.9)	(1.4)
	2.4	1.8	(2.7)	(2.0)

Notes to the financial statements

for the year ended December 31, 2017

Reconciliation of effective tax rate

The tax charge on profit for the year differs from the nominal amount that would arise at the standard weighted average rate of corporation tax in the UK. The differences are explained below:

	2017 US$m	*Effective tax rate*	*2016 US$m*	*Effective tax rate*
Profit before taxation	71.8		95.6	
Tax using the UK weighted average corporation tax rate of 19.25% (2016: 20.00%)	13.8	19.2%	19.1	20.0%
Banking surcharge	3.8	5.3%	3.7	3.9%
APA adjustment	(2.1)	(2.9)%	(8.3)	(8.7)%
Adjustments for prior years	(2.7)	(3.8)%	2.4	2.5%
Other	(0.2)	(0.3)%	(0.4)	(0.4)%
	12.6	17.5%	16.5	17.3%

The Group is party to an Advance Pricing Agreement ("APA") between its affiliates CM Inc and CM Asia and Her Majesty's Revenue and Customs ("HMRC") which defines the basis on which UK tax is charged on global derivative products group profits.

Corporation tax rate

On 1 April 2017, the corporation tax rate changed from 20% to 19%, resulting in an effective rate of 19.25% for the year ended 31 December 2017. For the prior year a corporation tax rate of 20% was effective throughout the period. The government announced a further reduction to 17% effective from 1 April 2020. This reduction was substantively enacted at the reporting date.

In addition, the Finance (No. 2) Act 2015 introduced a bank surcharge of 8% on the profits of companies within banking groups, with effect from 1 January 2016. The Group has been allocated a portion of a £25m bank surcharge allowance that covers entities within the SMBC UK Group.

The deferred tax asset at 31 December 2017 has been calculated based on these rates, including the bank surcharge. The effect of the bank surcharge is reflected in this year's current tax charge.

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for the year ended December 31, 2017

Deferred tax assets (Group and Company)

	2017	*2016*
	US$m	*US$m*
Property, plant & equipment	0.5	0.9
Employee benefits	0.7	0.5
Cash flow hedges	(0.2)	0.5
Tax assets	1.0	1.9

Movement in deferred tax (Group and Company)

	January 1, 2017	*Recognised in income*	*Recognised in reserves*	*December 31, 2017*
Property, plant and equipment	0.9	(0.4)	-	0.5
Employee benefits	0.5	0.2	-	0.7
Cash flow hedges	0.5	-	(0.7)	(0.2)
Tax assets	1.9	(0.2)	(0.7)	1.0

	January 1, 2016	*Recognised in income*	*Recognised in reserves*	*December 31, 2016*
Property, plant and equipment	0.6	0.3	-	0.9
Employee benefits	0.3	-	0.2	0.5
Cash flow hedges	-	-	0.5	0.5
Tax assets	0.9	0.3	0.7	1.9

Notes to the financial statements

for the year ended December 31, 2017

9. Pension costs

The Group operates two pension schemes in the UK: a contract-based defined contribution scheme, which covers all of the Group's local employees, with the exception of one employee, and an Executive Personal Pension Plan ("EPP"), which is a trust based scheme that provides benefits on a defined benefit basis to one UK employee. The Group incurred no pension costs in respect of its Japanese expatriate employees.

The contract based scheme, The SMBC Capital Fairs Limited Group Personal Plan, is open to new entrants and future contributions. The pension cost for this scheme for the year was $3.9 million (2016 - $3.5 million). The Company recognises expenses as employees render services.

The Group currently contributes to the EPP policy at the rate of 15% of the capped salary.

The defined benefit pension has the following features:

- Payable from age 60, calculated as one-sixtieth of pensionable salary limited to the earnings cap, for each year of service;
- Guaranteed for 5 years once in payment;
- Increases at the lower of retail price index or 5% p.a.;
- Attaches a 50% spouse's pension.

The principle assumptions in valuing the Defined Benefit Obligation of the EPP are:

	2017 %	*2016* %
Rate of increase in salaries	4.8	4.8
Rate of increase in pension payment	3.3	3.3
Discount rate	2.4	2.6
Inflation assumption	3.3	3.3

Salary is set to increase at a rate of 1.5% per annum in excess of the inflation assumption. The assumption allows for both general increases in pay (due to inflation) and career progression. However, because the salary is capped, this assumption has no impact. The cap is assumed to increase in line with inflation (RPI).

The inflation assumption is set by having regard to the difference in yields between fixed-interest and index-linked investments. The difference is adjusted for an inflation risk premium of 0.2% per annum. There is no allowance for using CPI, rather than RPI.

The discount rate used to value scheme liabilities is set at the current rate of return on high quality corporate bonds, for this purpose AA rated.

Notes to the financial statements

for the year ended December 31, 2017

Values of the EPP scheme assets and liabilities were as follows:

Group and Company

	2017	*2016*
	US$m	*US$m*
Total fair value of assets	1.1	1.0
Present value of scheme liabilities	(4.1)	(3.5)
Pension scheme liability	(3.0)	(2.5)
Related deferred tax asset (Note 8)	0.7	0.6
Net pension liability	(2.3)	(1.9)

The table below lays out movements in the fair value of plan assets:

	2017	*2016*
	US$m	*US$m*
Fair value of plan assets at the beginning of the year	1.0	1.0
Expected return on plan assets	-	0.1
Employer contributions	-	-
Actuarial gain on plan assets	0.1	-
Exchange differences on opening balance	-	(0.1)
Fair value of plan assets at the end of the year	1.1	1.0

The assets of the Scheme are invested in three Aegon funds: Mixed Fund, With Profits Endowment Fund and High Equity With Profits Fund. The Mixed Fund is diversified by investing in a variety of underlying funds. The with-profits funds invest in a wide range of bonds and equities but smooth the investment returns together with the use of underlying guarantees. The table below analyses the allocation of assets by instrument type:

	2017		2016	
	%	*US$m*	*%*	*US$m*
Quoted instruments	27.6	0.3	27.6	0.3
Unquoted instruments*	69.4	0.8	70.3	0.7
Cash	3.0	-	2.1	-
	100.0	1.1	100.0	1.0

*Aegon With-Profit funds

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for the year ended December 31, 2017

Movements in the present value of the defined benefit obligation are below:

	2017 US$m	2016 US$m
Defined benefit obligations at the beginning of the year	3.5	2.9
Service cost / interest expense recognised in staff costs	0.2	0.2
Actuarial loss on scheme liabilities	0.2	1.0
Exchange differences on opening balance	0.2	(0.6)
Present value of scheme liabilities at the end of the year	4.1	3.5

Actuarial loss movements are summarised in the following table:

	2017 US$m	2016 US$m
Cumulative actuarial loss at 1 January	(2.5)	(1.5)
Actuarial loss for the year (Note 8)	(0.1)	(1.0)
Cumulative actuarial loss at 31 December	(2.6)	(2.5)
Actuarial loss for the year, net of tax (Note 8)	(0.1)	(0.6)

The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out on behalf of the Company at 31 December 2017. The present value of the defined benefit obligation, the related current service cost and the past service cost were measured using the projected unit credit method.

The expected contributions to the plan for the next annual reporting period are expected to grow by 3.3%, in line with the principal assumptions described earlier.

The maturity profile of the defined benefit obligation assumes payments increasing at the lower of RPI or 5% per annum over the weighted averaged duration of the obligation. The average duration of the obligation represents the life expectancy of a male aged 60 at the time of retirement and at the reporting date equals 30 years (2016: 30 years)

Notes to the financial statements

for the year ended December 31, 2017

Sensitivity Analysis

The approximate percentage and absolute impact on the defined benefit obligation of changes in the significant assumptions is shown below:

Assumption varied	2017 *Defined Benefit Obligation*		2016 *Defined Benefit Obligation*	
	%	*US$m*	*%*	*US$m*
Discount Rate 0.5% p.a. lower	13.0	0.5	13.0	0.4
Inflation Rate 0.5% p.a. lower	(11.0)	(0.5)	(12.0)	(0.4)
Minimum rate of improvement of mortality 0.5% p.a. lower	(3.0)	(0.1)	(2.0)	(0.1)

10. Cash at banks

	Group		*Company*	
	2017	*2016*	*2017*	*2016*
	US$m	*US$m*	*US$m*	*US$m*
Current accounts	101.0	35.1	85.2	30.1
Short-term deposits of three months or less	745.0	423.5	617.1	300.5
	846.0	458.6	702.3	330.6

At the reporting date, $19.5 million of Group (2016 - $4.3 million), and $9.1 million of Company (2016 - $3.8 million) current accounts were placed with related companies.

Short-term deposits placed with related companies amounted to $318.0 million (2016 - $1.4 million) for the Group and $316.5 million (2016 - $nil) for the Company.

A detailed analysis of the Group's and Company's credit exposure on cash at banks is included in note 18.

Notes to the financial statements

for the year ended December 31, 2017

11. Trading securities

	Listed on London Stock Exchange US$m	*Listed on non UK Exchanges US$m*	*Not Listed US$m*	*Total US$m*
Fair value as at 31 December 2017				
Group				
Floating rate notes	9.3	186.5	-	195.8
U.S. treasury securities	-	455.9	-	455.9
Foreign government securities	1.0	161.8	-	162.8
Corporate bonds	27.4	485.3	49.0	561.7
Total	37.7	1,289.5	49.0	1,376.2
Company				
Floating rate notes	9.3	144.5	-	153.8
U.S. treasury securities	-	406.0	-	406.0
Foreign government securities	1.0	161.8	-	162.8
Corporate bonds	27.4	485.3	49.0	561.7
Total	37.7	1,197.6	49.0	1,284.3

Notes to the financial statements

for the year ended December 31, 2017

	Listed on London Stock Exchange US$m	*Listed on non UK Exchanges US$m*	*Not Listed US$m*	*Total US$m*
Fair value as at 31 December 2016				
Group				
Floating rate notes	5.4	65.5	-	70.9
U.S. treasury securities	-	330.3	16.0	346.3
Foreign government securities	-	37.4	-	37.4
Corporate bonds	25.9	214.9	8.4	249.2
Equity securities	-	-	0.2	0.2
Total	31.3	648.1	24.6	704.0
Company				
Floating rate notes	5.4	20.0	-	25.4
U.S. treasury securities	-	296.3	-	296.3
Foreign government securities	-	37.4	-	37.4
Corporate bonds	25.9	214.8	8.4	249.1
Equity securities	-	-	0.2	0.2
Total	31.3	568.5	8.6	608.4

Notes to the financial statements

for the year ended December 31, 2017

12. Derivative assets and liabilities

As required by IFRS 7 and IAS 32, the Company discloses derivative assets and liabilities gross by counterparty because there is no intention to settle net.

	2017 *US\$m*	*2016* *US\$m*
Group		
Amounts due from related parties	4,779.1	4,903.6
Amounts due from external parties	2,284.3	2,477.2
Derivative reserves	(26.7)	(44.1)
Derivative assets	7,036.7	7,336.7
Amounts due to related parties	5,927.1	6,306.5
Amounts due to external parties	1,110.9	1,069.9
Derivative reserves	(32.8)	(38.9)
Derivative liabilities	7,005.2	7,337.5
Company		
Amounts due from related parties	4,766.4	4,887.4
Amounts due from external parties	2,283.3	2,476.3
Derivative reserves	(26.7)	(44.1)
Derivative assets	7,023.0	7,319.6
Amounts due to related parties	5,926.2	6,305.6
Amounts due to external parties	1,098.4	1,054.2
Derivative reserves	(32.1)	(37.9)
Derivative liabilities	6,992.5	7,321.9

In line with the requirements of IFRS 13, the Group booked a Debit Value Adjustment ("DVA"), Credit Value Adjustment ("CVA") and Funding Value Adjustment ("FVA") when calculating the fair value of its derivatives. These are all classified as derivatives reserves.

Notes to the financial statements

for the year ended December 31, 2017

The tables below provide an analysis of carrying values and principal amounts by type of contract:

	Carrying value		Notional principal	
	2017	*2016*	*2017*	*2016*
Group	*US$m*	*US$m*	*US$m*	*US$m*
Interest rate and currency swaps	6,963.3	7,196.7	141,872.6	112,863.0
Options	72.8	160.5	8,463.1	8,650.5
Forward contracts	17.5	18.8	728.5	262.7
Commodity swaps	9.8	4.8	763.6	110.9
Derivative reserves	(26.7)	(44.1)	-	-
Derivative assets	7,036.7	7,336.7	151,827.8	121,887.1
Interest rate and currency swaps	6,870.0	7,118.6	144,029.1	114,919.4
Options	72.6	160.2	8,463.1	8,650.5
Forward contracts	25.0	21.2	1,173.6	300.1
Commodity swaps	8.0	4.5	758.9	103.8
Credit guarantees (see Note 25)	62.4	71.9	-	-
Derivative reserves	(32.8)	(38.9)	-	-
Derivative liabilities	7,005.2	7,337.5	154,424.7	123,973.8

Notes to the financial statements

for the year ended December 31, 2017

	Carrying value		Notional principal	
	2017	*2016*	*2017*	*2016*
Company	*US$m*	*US$m*	*US$m*	*US$m*
Interest rate and currency swaps	6,950.8	7,181.0	141,813.1	112,760.1
Options	71.6	159.1	5,621.4	5,195.3
Forward contracts	17.5	18.8	728.5	262.7
Commodity swaps	9.8	4.8	763.6	110.9
Derivative reserves	(26.7)	(44.1)	-	-
Derivative assets	7,023.0	7,319.6	148,926.6	118,329.0
Interest rate and currency swaps	6,857.8	7,103.4	143,967.1	114,808.8
Options	71.4	158.8	5,621.4	5,195.3
Forward contracts	25.0	21.2	1,173.6	300.1
Commodity swaps	8.0	4.5	758.9	103.8
Credit guarantees (see Note 25)	62.4	71.9	-	-
Derivative reserves	(32.1)	(37.9)	-	-
Derivative liabilities	6,992.5	7,321.9	151,521.0	120,408.0

The exposure to credit or market risks is represented by carrying values. They are based on the notional amounts and other terms of the derivative instrument agreements.

The following paragraphs provide additional information on interest rate, foreign exchange, commodity, credit and equity index derivatives contracts:

Interest rate contracts

Interest rate swaps are one of the primary derivative instruments used by the Group. The two parties to an interest rate swap agree to exchange, at particular intervals, payment streams calculated on a specified notional amount with at least one stream based on a floating interest rate. Basis swaps involve two floating rates, such as prime and LIBOR. Inflation swaps are included in this category.

Forward rate agreements are settled in cash at a specified future date based on the differential between agreed upon interest rates and an index applied to a notional amount.

Interest rate caps and floors require the writer to pay the purchaser at specified future dates the amount, if any, by which a specified market interest rate exceeds the fixed cap rate or falls below the fixed floor rate, applied to a notional amount. The cap or floor writer receives a premium for bearing the risk of unfavourable interest rate changes.

Currency swaps and foreign exchange contracts

The Group is involved in a variety of currency swaps and foreign exchange contracts in its trading activities. The parties to a currency swap generally agree to the exchange of principal amounts and/or interest in two currencies, agreeing to re-exchange any principal amounts at a future date and agreed upon exchange rate. These currency swaps primarily relate to major foreign currencies such as Yen, Canadian dollars, Sterling and Euros.

Commodity derivatives

The Group has undertaken a series of commodity index swaps and options whereby it receives a fixed rate per contract and guarantees to deliver the average index price to the counterparty or, alternatively, where it guarantees a fixed payment in return for the floating average index price from the counterparty. All counterparty positions are fully hedged with a market maker.

Equity index derivatives

The Group has undertaken a number of equity index option transactions. These transactions involve the payment or receipt of amounts which are determined by reference to the movement in an equity index.

As of 31 December 2017 for most of the Group's interest rate and currency swaps, and interest rate and currency options, back to back transactions were made with CM Inc. For commodity and equity and other index trades back to back transactions were made with other market counterparties. A gain of $102.6 million before CVA, DVA and FVA adjustments, was recognised on the derivative trading portfolio in 2017 and was disclosed in the net trading income (2016 - $80.5 million). The fair value of these trades was determined using valuation techniques with significantly observable valuation inputs or internally generated models.

Note 18 describes the risks associated with derivative products.

13. Repurchase agreement assets and liabilities

	2017	*2016*
	US$m	*US$m*
Group and Company		
Amounts due from related parties	3,157.4	5,215.2
Amounts due from external parties	493.5	322.1
Securities purchased under agreements to resell	3,650.9	5,537.3
Amounts due to related parties	11.6	211.1
Amounts due to external parties	2,986.4	4,987.9
Securities sold under agreements to repurchase	2,998.0	5,199.0

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14. Other debtors

	Group		*Company*	
	2017	*2016*	*2017*	*2016*
	US$m	*US$m*	*US$m*	*US$m*
Collateral placed with related parties	2,495.6	2,342.8	2,495.6	2,342.8
Collateral placed with external parties	569.4	560.7	569.4	560.7
Prepayments	6.6	5.4	6.3	5.0
Corporation tax	-	2.8	-	2.9
Other related party debtors	4.8	0.8	7.2	0.2
Other external debtors	10.8	8.9	10.6	8.7
	3,087.2	2,921.4	3,089.1	2,920.3

Placed collateral represents cash deposits in respect of derivative and repo transactions required under Collateral Support Agreements ('CSA').

Included within collateral with related parties is a payable balance of $310.0 million (2016 - $310.0 million). This relates to an Independent Amount received from an affiliate, and is offset against collateral placed within the same CSA agreement.

15. Intangible assets

	Computer software
	US$m
Group and Company	
Cost	
Balance at 1st January 2017	-
Additions	2.1
Transfers	-
Balance at 31st December 2017	2.1
Accumulated amortisation and impairment losses	
Balance at 1st January 2017	-
Charge for the year	0.1
Balance at 31st December 2017	0.1

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for the year ended December 31, 2017

Carrying amounts	
Balance at 31st December 2016	-
Balance at 31st December 2017	2.0

No internal development costs were capitalised during the period.

16. Property, plant and equipment

The year end position of the Group and the Company comprised the following classes of assets:

	Leasehold property US$m	*Personal computers US$m*	*Furniture and fixtures US$m*	*Total US$m*
Group				
Cost				
Balance at 1st January 2016	21.9	5.8	0.3	28.0
Additions	-	0.2	-	0.2
Balance at 31st December 2016	21.9	6.0	0.3	28.2
Balance at 1st January 2017	21.9	6.0	0.3	28.2
Additions	1.1	2.1	0.1	3.3
Balance at 31st December 2017	23.0	8.1	0.4	31.5
Accumulated depreciation and impairment losses				
Balance at 1st January 2016	9.4	4.6	0.2	14.2
Depreciation for the year	2.4	0.6	-	3.0
Balance at 31st December 2016	11.8	5.2	0.2	17.2
Balance at 1st January 2017	11.8	5.2	0.2	17.2
Depreciation for the year	2.4	0.9	0.1	3.4
Balance at 31st December 2017	14.2	6.1	0.3	20.6
Carrying amounts				
Balance at 31st December 2016	10.1	0.8	0.1	11.0
Balance at 31st December 2017	8.8	2.0	0.1	10.9

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	Leasehold property US$m	*Personal computers US$m*	*Furniture and fixtures US$m*	*Total US$m*
Company				
Cost				
Balance at 1st January 2016	21.9	5.8	0.3	28.0
Additions	-	0.1	-	0.1
Balance at 31st December 2016	21.9	5.9	0.3	28.1
Balance at 1st January 2017	21.9	5.9	0.3	28.1
Additions	1.1	2.1	-	3.2
Balance at 31st December 2017	23.0	8.0	0.3	31.3
Accumulated depreciation and impairment losses				
Balance at 1st January 2016	9.4	4.6	0.2	14.2
Depreciation for the year	2.4	0.6	-	3.0
Balance at 31st December 2016	11.8	5.2	0.2	17.2
Balance at 1st January 2017	11.8	5.2	0.2	17.2
Depreciation for the year	2.4	0.8	0.1	3.3
Balance at 31st December 2017	14.2	6.0	0.3	20.5
Carrying amounts				
Balance at 31st December 2016	10.1	0.7	0.1	10.9
Balance at 31st December 2017	8.8	2.0	-	10.8

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17. Other creditors

	Group		Company	
	2017	*2016*	*2017*	*2016*
	US$m	*US$m*	*US$m*	*US$m*
Collateral received from related parties	2,804.7	1,923.4	2,804.7	1,923.4
Collateral received from external parties	139.3	197.2	139.3	197.2
Funding loans from related parties	510.3	201.5	510.3	201.5
Corporation tax	3.0	0.3	1.7	0.3
Other related party creditors	20.8	57.2	20.4	55.8
Other external creditors	60.1	42.1	58.7	40.7
	3,538.2	2,421.7	3,535.1	2,418.9

Received collateral represents cash deposits in respect of derivative and repo transactions required under Collateral Support Agreements ('CSA'). Collateral is transferred with full re-hypothecation rights.

18. Risk management

Strategy in using financial instruments

The principal activities of the Group include customer facilitation, brokering and trading in primary and secondary debt and equity securities and an extensive range of over-the-counter derivative contracts.

The Group and the Company undertake their derivative business on either an agency basis or back-to-back basis where the market risk arising from customer trades is hedged either with CM Inc, or a market counterparty.

The Group's business model is subject to a number of risks which are specific to the Group and generic to the sector.

Cash flow and fair value interest rate risk

As the Group and the Company operates a primarily hedged derivative portfolio (subject to appropriate credit adjustments) and invests in floating rate assets funded through floating rate liabilities or capital there is no significant exposure in the derivative portfolio to changes in cash flow or fair value due to interest rate risk.

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Credit risk

Credit risk represents the potential losses that the Group would incur if a counterparty failed to perform its obligations under contractual terms and collateral held was not sufficient to cover them.

Cash at banks

Credit risk of cash at banks, which corresponds to its maturity profile, is characterised by the short-term rating of the financial institutions it was held at, as analysed below:

	Group		*Company*	
	2017	*2016*	*2017*	*2016*
S&P rating	*US$m*	*US$m*	*US$m*	*US$m*
A-1+	156.6	125.6	45.0	18.8
A-1	653.0	321.3	626.2	304.2
A-2	36.4	11.7	31.1	7.6
	846.0	458.6	702.3	330.6

	Group		*Company*	
	2017	*2016*	*2017*	*2016*
Moody's rating	*US$m*	*US$m*	*US$m*	*US$m*
P-1	764.5	427.8	626.1	304.2
P-2	36.4	12.0	31.1	7.6
Not Rated	45.1	18.8	45.1	18.8
	846.0	458.6	702.3	330.6

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Trading securities

At the reporting date, trading securities had the following long-term credit rating:

	Group		*Company*	
	2017	*2016*	*2017*	*2016*
S&P rating	*US$m*	*US$m*	*US$m*	*US$m*
AAA	119.8	22.1	119.8	22.1
AA+	466.7	2.8	416.8	2.8
AA	0.6	-	0.6	-
AA-	35.8	18.3	21.8	4.3
A+	109.4	69.1	101.4	60.3
A	209.6	103.1	189.6	80.4
A-	135.7	37.0	135.7	37.0
BBB+	34.8	22.5	34.8	22.5
BBB	40.1	20.2	40.1	20.2
BBB-	35.9	2.1	35.9	2.1
BB+	0.8	-	0.8	-
Not rated	187.0	406.8	187.0	356.7
	1,376.2	704.0	1,284.3	608.4

	Group		*Company*	
	2017	*2016*	*2017*	*2016*
Moody's rating	*US$m*	*US$m*	*US$m*	*US$m*
Aaa	575.8	76.0	525.9	60.9
Aa1	21.6	2.8	21.6	2.8
Aa2	9.9	17.9	9.9	3.9
Aa3	58.7	1.1	22.0	1.1
A1	351.6	195.8	346.3	164.2
A2	28.3	12.6	28.3	12.6
A3	20.1	8.7	20.1	8.7
Baa1	69.5	11.4	69.5	11.4
Baa2	52.6	4.0	52.6	4.0
Baa3	24.0	11.4	24.0	11.4
Ba1	0.9	1.5	0.9	1.5
Not rated	163.2	360.8	163.2	325.9
	1,376.2	704.0	1,284.3	608.4

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for the year ended December 31, 2017

Reverse repos

Credit risk on securities purchased under agreements to resell (reverse repos) arises from a potential inability of customers to fully repay the amounts they received in exchange for the underlying securities. This risk is mitigated by the quality and current value of purchased securities which act as collateral.

As disclosed in Note 13, the majority of reverse repo contracts is made with related entities within SMBC group. These entities have short-term rating A-1 by S&P and P-1 by Moody's.

The table below summarises short-term credit ratings of external customers in reverse repo agreements, which corresponds to the maturity profile of these agreements:

Group and Company *S&P rating*	*2017* *US$m*	*2016* *US$m*
A-1+	28.2	-
A-1	413.1	269.6
A-2	52.2	52.5
	493.5	322.1

Group and Company *Moody's rating*	*2017* *US$m*	*2016* *US$m*
P-1	441.4	269.6
P-2	52.1	52.5
	493.5	322.1

The table below analyses the types and fair value of securities purchased under reverse repo agreements with external customers:

	2017 *US$m*	*2016* *US$m*
USD Treasury bills	242.2	127.8
European government bonds	27.3	108.1
USD corporate bonds	66.4	57.9
European corporate bonds	124.7	12.7
Japanese corporate equity	27.7	15.8
	488.3	322.3

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These underlying securities had the following long-term ratings at the reporting date:

Group and Company *S&P rating*	*2017* *US$m*	*2016* *US$m*
AAA	31.2	62.6
AA+	242.6	128.0
AA	-	47.9
AA-	6.0	-
A+	15.8	0.6
A	24.4	16.5
A-	70.5	32.8
BBB+	20.9	12.2
BBB	20.8	3.8
BBB-	9.0	2.1
Not rated	47.1	15.8
	488.3	322.3

Group and Company *Moody's rating*	*2017* *US$m*	*2016* *US$m*
Aaa	273.8	190.5
Aa2	2.2	47.9
Aa3	6.0	-
A1	80.9	38.3
A2	5.3	1.1
A3	11.2	9.9
Baa1	19.7	11.1
Baa2	16.6	-
Baa3	13.9	-
Not rated	58.7	23.5
	488.3	322.3

Derivatives

The Group's credit exposure on derivatives arises from the risk of non-performance of its counterparties in fulfilling their contractual obligations pursuant to its derivative transactions. The risk of non-performance can be directly impacted by volatile or illiquid trading markets, which may impair the counterparties' abilities to satisfy their obligations. The notional or contractual values of agreements do not represent exposure to credit risk, which is limited to the current cost of replacing the contracts with a positive market value.

As disclosed in Note 12, the majority of derivative assets is receivable from related parties. At the reporting date, the carrying value of such assets amounted for the Group to $4,779.1 million (2016 - $4,903.6 million) and for the Company - $4,766.4 million (2016 - $4,887.4 million). All related parties have long-term rating A by S&P and A1 by Moody's.

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The tables below analyse the carrying value of derivative assets with external counterparties by long-term credit rating, appropriate for the long-term nature of these instruments:

	Group		*Company*	
	2017	*2016*	*2017*	*2016*
S&P rating	*US$m*	*US$m*	*US$m*	*US$m*
AAA	73.1	102.8	73.1	102.8
AA+	1.0	-	-	-
AA-	107.0	70.9	107.0	70.9
A+	142.8	196.6	142.8	196.6
A	99.2	45.9	99.2	45.9
A-	95.4	295.6	95.4	295.6
BBB+	155.3	71.1	155.3	71.1
BBB	21.5	23.8	21.5	23.8
BBB-	0.7	0.5	0.7	0.5
BB+	4.3	-	4.3	0
BB	1.7	-	1.7	0
BB-	-	3.0	-	3.0
Unrated	1,582.3	1,667.0	1,582.3	1,666.1
	2,284.3	2,477.2	2,283.3	2,476.3

	Group		*Company*	
	2017	*2016*	*2017*	*2016*
Moody's	*US$m*	*US$m*	*US$m*	*US$m*
Aaa	73.1	102.8	73.1	102.8
Aa1	1.0	-		-
Aa2	8.9	72.9	8.9	72.9
Aa3	191.6	115.8	191.6	115.8
A1	134.3	144.4	134.3	143.5
A2	34.2	18.0	34.2	18.0
A3	211.6	258.9	211.6	258.9
Baa1	27.3	53.9	27.3	53.9
Baa2	21.1	29.4	21.1	29.4
Baa3	2.5	0.5	2.5	0.5
Ba1	6.0	-	6.0	-
Ba3	-	3.0	-	3.0
B2	-	-	-	-
Unrated	1,572.7	1,677.6	1,572.7	1,677.6
	2,284.3	2,477.2	2,283.3	2,476.3

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for the year ended December 31, 2017

Analysis of credit exposure to external derivative counterparties by maturity:

Group	*Gross replacement cost*		*Notional Principal*	
	2017	*2016*	*2017*	*2016*
	US$m	*US$m*	*US$m*	*US$m*
Term to maturity				
Up to 5 years	689.7	742.0	21,256.0	11,414.1
Greater than 5 years	1,594.6	1,735.2	14,186.3	9,143.3
	2,284.3	2,477.2	35,442.3	20,557.4

Company	*Gross replacement cost*		*Notional Principal*	
	2017	*2016*	*2017*	*2016*
	US$m	*US$m*	*US$m*	*US$m*
Term to maturity				
Up to 5 years	688.7	742.0	20,258.9	11,414.1
Greater than 5 years	1,594.6	1,734.3	14,186.3	9,093.9
	2,283.3	2,476.3	34,445.2	20,508.0

As of 31 December 2017, the Group held cash collateral from SMBC's branches amounting to $2,738.0 million (2016 - $1,921.9 million), SMBC Europe amounting to $66.0 million (2016 - $nil) and SMBC Malaysia Berhad amounting to $0.7 million (2016 - $0.4 million). Cash collateral from unaffiliated counterparties amounted to $139.3 million (2016 - $197.1 million).

Management determines concentrations of counterparty credit risk in accordance with Bank for International Settlements guidance ('BIS Rules'). Management does not believe that the Group is exposed to significant concentrations of risk identified by such factors as geographical area, currency or product.

Other trading assets

Other trading assets include an exposure to external counterparties rated BBB and lower by S&P or unrated amounting as at 31 December 2017to $53.0 million (2016: $nil).

Offsetting financial assets and financial liabilities

The disclosure set out in the following tables include financial assets and financial liabilities that are subject to an enforceable master netting arrangement or similar agreement that covers similar financial instruments.

The ISDA and similar master netting arrangements do not meet the criteria for offsetting in the statement of financial position. This is because they create for the parties to the agreement a right of set-off of recognised amounts that is enforceable only following an event of default, insolvency or bankruptcy of the Group or the counterparties or following other predetermined events. In addition, the Group and its counterparties do not intend to settle on a net basis or to realise the assets and settle the liabilities simultaneously.

The tables below provide further information on financial assets and liabilities that do not meet the offsetting criteria.

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for the year ended December 31, 2017

	Amount of recognised financial assets / liabilities US$m	*Assets / liabilities that do not meet the offsetting criteria US$m*	*Non-cash collateral US$m*	*Cash collateral US$m*	*Net amount US$m*
At 31 December 2017					
Group					
Derivative assets	7,036.7	(3,521.0)	(1,435.5)	(2,944.0)	(863.8)
Reverse repurchase agreements	3,650.9	(434.4)	(3,748.5)	-	(532.0)
	10,687.6	(3,955.4)	(5,184.0)	(2,944.0)	(1,395.8)
Group					
Derivative liabilities	7,005.2	(3,521.0)	-	(3,046.3)	437.9
Repurchase agreements	2,998.0	(434.4)	(2,971.3)	(18.7)	(426.4)
	10,003.2	(3,955.4)	(2,971.3)	(3,065.0)	11.5
Company					
Derivative assets	7,023.0	(3,508.5)	(1,435.5)	(2,944.0)	(865.0)
Reverse repurchase agreements	3,650.9	(434.4)	(3,748.5)	-	(532.0)
	10,673.9	(3,942.9)	(5,184.0)	(2,944.0)	(1,397.0)
Company					
Derivative liabilities	6,992.5	(3,508.5)	-	(3,046.3)	437.7
Repurchase agreements	2,998.0	(434.4)	(2,971.3)	(18.7)	(426.4)
	9,990.5	(3,942.9)	(2,971.3)	(3,065.0)	11.3

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for the year ended December 31, 2017

	Amount of recognised financial assets	*Assets / liabilities that do not meet the offsetting criteria*	*Non-cash collateral*	*Cash collateral*	*Net amount*
	US$m	*US$m*	*US$m*	*US$m*	*US$m*
At 31 December 2016					
Group					
Derivative assets	7,336.7	(4,070.3)	(1,130.9)	(2,119.3)	16.2
Reverse repurchase agreement	5,537.3	(5,443.5)	(10.0)	(54.5)	29.3
	12,874.0	(9,513.8)	(1,140.9)	(2,173.8)	45.5
Group					
Derivative liabilities	7,337.5	(4,070.3)	-	(2,843.2)	424.0
Repurchase agreement	5,199.0	(5,124.1)	-	(4.3)	70.6
	12,536.5	(9,194.4)	-	(2,847.5)	494.6
Company					
Derivative assets	7,319.6	(4,069.5)	(1,130.8)	(2,119.3)	-
Reverse repurchase agreement	5,537.3	(5,443.5)	(10.0)	(54.5)	29.3
	12,856.9	(9,513.0)	(1,140.8)	(2,173.8)	29.3
Company					
Derivative liabilities	7,321.9	(4,069.5)	-	(2,843.2)	409.2
Repurchase agreement	5,199.0	(5,124.1)	-	(4.3)	70.6
	12,520.9	(9,193.6)	-	(2,847.5)	479.8

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for the year ended December 31, 2017

Market risk

All trading instruments are subject to market risk, the potential that future changes in market conditions and other factors may create variation in the value of instruments, due to fluctuations in security prices, as well as interest and foreign exchange rates. Market risk is directly impacted by the volatility and liquidity in the markets in which the related underlying assets are traded. As the instruments are recognised at fair value, those changes directly affect reported income.

The Group and the Company undertake their derivative business on either an agency basis or back-to-back basis where the market risk arising from customer trades is hedged either with CM Inc, or a market counterparty. Market risk arises in both the primary and the secondary securities business. It is mitigated through the monitoring and enforcing position limits with short unwind periods. Businesses that are subject to market risk limits have these approved annually by the board and these are set out in an official risk appetite statement.

The Group invests its capital in cash deposits, treasury bills, and a portfolio of high quality floating rate notes; through the latter it seeks to earn an interest margin and, when the opportunity arises, to realise a trading profit. In addition, the Group places cash collateral with derivative trading counterparts, upon which it earns overnight interest. The Group has interest-bearing liabilities of cash collateral held on behalf of derivative trading counterparts and inter-group borrowings.

The weighted average yield on the cash deposits was 0.18% as of 31 December 2017 (2016: 0.19%). The weighted average yields as of 31 December 2017 on floating rate notes and U.S. treasury securities were 1.71% and 0.83% (2016: 1.17% and 0.24%) respectively. The Group's sensitivity to interest rates is such that a parallel shift of +/-100bp from year end rates would increase net assets by $7.1 million (2016 - $1.1 million) and decrease net assets by $ 7.1 million (2016 - $1.0 million) respectively. The increase in sensitivity is primarily driven by a substantial increase in convertible bonds and covered warrants which are not hedged against interest rate risk.

Fair value hierarchy

When available, the Group uses quoted market prices to determine fair value, and classifies such items within Level 1. Trading securities are classified in Level 1 of the fair value hierarchy since they are valued using quoted market prices.

In some cases where no market price is available the Group will make use of acceptable practical expedients such as matrix pricing to calculate fair value, in which case the items are classified within Level 2.

If quoted market prices are not available, fair value is based upon internally developed models that use current independently sourced market parameters such as interest rates, exchange rates and option volatilities, the valuation model used depends upon the specific asset or liability being valued. The determination of fair value considers various factors, including interest rate yield curves, time value and volatility factors, underlying options and derivatives and price activity for equivalent synthetic instruments.

The majority of derivative transactions entered into by the Group are executed over the counter and so are valued using internal valuation techniques as no quoted market prices exist for such instruments. The valuation technique and inputs depend on the type of derivative and the nature of the underlying reference instrument. The principal techniques used to value these instruments are discounted cash flows, Black-Scholes and Monte Carlo simulation.

The key inputs depend upon the type of derivative and the nature of the underlying instrument and include interest rate yield curves, exchange rates, the spot price of the underlying instrument and volatility. A given position is categorised as Level 2 or Level 3 depending on the observability of the significant inputs to the model. Where a valuation incorporates material inputs that are not based on observable market data, it will be classified as Level 3. Unobservable inputs are determined with reference to observable inputs, historical observations (of, for example, correlations) or the use of other analytical techniques.

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for the year ended December 31, 2017

The following table presents the fair value hierarchy of financial assets and liabilities as at 31 December 2017:

	Level 1 *US$m*	*Level 2* *US$m*	*Level 3* *US$m*	*Total* *US$m*
At 31 December 2017				
Assets - Group				
Derivative assets	-	6,971.0	65.7	7,036.7
Trading securities	1,376.2	-	-	1,376.2
Other trading assets, at fair value	-	76.6	-	76.6
	1,376.2	7,047.6	65.7	8,489.5
Liabilities - Group				
Derivative liabilities	-	7,005.2	-	7,005.2
Trading liabilities, at fair value	-	176.0	-	176.0
Trading securities sold, not yet purchased	681.8	-	-	681.8
	681.8	7,181.2	-	7,863.0
Assets - Company				
Derivative assets	-	6,957.3	65.7	7,023.0
Trading securities	1,284.3	-	-	1,284.3
Other trading assets, at fair value	-	76.6	-	76.6
	1,284.3	7,033.9	65.7	8,383.9
Liabilities - Company				
Derivative liabilities	-	6,992.5	-	6,992.5
Trading liabilities, at fair value	-	176.0	-	176.0
Trading securities sold, not yet purchased	681.8	-	-	681.8
	681.8	7,168.5	-	7,850.3

Notes to the financial statements

for the year ended December 31, 2017

The following table presents the fair value hierarchy of financial assets and liabilities as at 31 December 2016:

	Level 1 US$m	*Level 2 US$m*	*Level 3 US$m*	*Total US$m*
At 31 December 2016				
Assets - Group				
Derivative assets	-	7,258.0	78.7	7,336.7
Trading securities	702.0	2.0	-	704.0
Other trading assets, at fair value	-	30.3	-	30.3
	702.0	7,290.3	78.7	8,071.0
Liabilities - Group				
Derivative liabilities	-	7,337.5	-	7,337.5
Trading liabilities, at fair value	-	112.2	-	112.2
Trading securities sold, not yet purchased	304.0	-	-	304.0
	304.0	7,449.7	-	7,753.7
Assets - Company				
Derivative assets	-	7,240.9	78.7	7,319.6
Trading securities	606.4	2.0	-	608.4
Other trading assets, at fair value	-	30.3	-	30.3
	606.4	7,273.2	78.7	7,958.3
Liabilities - Company				
Derivative liabilities	-	7,321.9	-	7,321.9
Trading liabilities, at fair value	-	112.2	-	112.2
Trading securities sold, not yet purchased	304.0	-	-	304.0
	304.0	7,434.1	-	7,738.1

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for the year ended December 31, 2017

Transfers between levels are effective as at the end of the reporting period in which they occur. The following table provides a reconciliation of the beginning and ending balances for assets and liabilities measured at fair value using significant unobservable inputs (Level 3) for the years ended 31 December 2017 and 31 December 2016.

Year ended 31 December 2017	*January 1, 2017*	*Transfer into level 3*	*Purchases, issuances, and settlements*	*Realised losses*	*Unrealised losses*	*December 31, 2017*
	US$m	*US$m*	*US$m*	*US$m*	*US$m*	*US$m*
Assets:						
Interest rate swap	78.7	-	-	-	(13.0)	65.7
Total assets at fair value	78.7	-	-	-	(13.0)	65.7

Year ended 31 December 2016	*January 1, 2016*	*Transfer into level 3*	*Purchases, issuances, and settlements*	*Realised losses*	*Unrealised losses*	*December 31, 2016*
	US$m	*US$m*	*US$m*	*US$m*	*US$m*	*US$m*
Assets:						
Interest rate swap	92.6	-	-		(13.9)	78.7
Total assets at fair value	92.6	-	-	-	(13.9)	78.7

The table below presents the information of significant unobservable inputs used to value the Group's and Company's Level 3 financial instruments. These financial instruments are valued using information from third-party pricing sources without adjustment. The valuation techniques and inputs utilised by these third-party pricing sources are assessed by the Group to evaluate the significance of unobservable inputs inherent within these instruments' fair value.

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for the year ended December 31, 2017

The sensitivity of the fair value measurement to changes in these unobservable inputs is considered significant if a change in those inputs could result in a significantly higher or lower fair value measurement. The Group's assessment of unobservable inputs that are significant to the fair value measurement are disclosed in the table below.

The following table provides information about significant unobservable inputs for Level 3 fair value measurements:

Level 3 Financial Instruments as of December 31, 2017 and December 31, 2016

Instrument	Valuation techniques	Unobservable inputs
Interest rate swap	• Internal interest rate swap model	• Liquidity premium
	• Dealer marks	

The Company's Product Control (Market Risk) department is responsible for the valuation policies and procedures. This department is responsible for running daily valuations and risks on the Company's derivatives portfolio, and reports into the Chief Operating Officer. The Company's Risk Management department is responsible for managing model risk and its related policies and procedures, and also reports into the Chief Operating Officer. As all models are owned by the front office under supervision and reporting lines of the Head Trader, independence in the validation process is maintained. All changes in existing models are reported to the Risk Management department and approved by the Model Validation Group ("MVG"). Model use and changes to models are approved by Global Risk Management Committee ("GRMC"), to which the MVG makes its recommendations. The GRMC broader membership extends to include representatives from the Group, which also supports independence within the validation process. Pricing models are validated based on assigned tiers. Tier 1 models are validated annually, Tier 2 models are validated every 2 years and Tier 3 models are validated every 3 years. Stress tests are run on a weekly/monthly basis.

Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities, at a reasonable cost. The Group and the Company have no unfunded forward commitments in the one year period.

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Maturity of financial liabilities

As at 31 December 2017	*Carrying amount*	*0-1 year*	*1-5 years*	*More than 5 years*
Group				
Non-derivative financial liabilities				
Trading liabilities, at fair value	176.0	0.4	13.8	161.8
Trading securities sold, not yet purchased	681.8	681.8	-	-
Securities sold under agreement to repurchase	2,998.0	2,998.0	-	-
Other creditors	3,538.2	3,538.2	-	-
Derivative financial liabilities				
Derivative liabilities (excluding reserves and guarantee liabilities)	6,975.6	456.0	2,267.2	4,252.4

As at 31 December 2017	*Carrying amount*	*0-1 year*	*1-5 years*	*More than 5 years*
Company				
Non-derivative financial liabilities				
Trading liabilities, at fair value	176.0	0.4	13.8	161.8
Trading securities sold, not yet purchased	681.8	681.8	-	-
Securities sold under agreement to repurchase	2,998.0	2,998.0	-	-
Other creditors	3,535.1	3,535.1	-	-
Derivative financial liabilities				
Derivative liabilities (excluding reserves and guarantee liabilities)	6,962.2	456.0	2,265.1	4,241.1

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As at 31 December 2016	*Carrying amount*	*0-1 year*	*1-5 years*	*More than 5 years*
Group				
Non-derivative financial liabilities				
Trading liabilities, at fair value	112.2	0.3	12.0	99.9
Trading securities sold, not yet purchased	304.0	304.0		
Securities sold under agreement to repurchase	5,199.0	5,199.0		
Other creditors	2,421.7	2,421.7		
Derivate financial liabilities				
Derivative liabilities (excluding reserves and guarantee liabilities)	7,304.5	273.4	2,334.4	4,696.7

As at 31 December 2016	*Carrying amount*	*0-1 year*	*1-5 years*	*More than 5 years*
Company				
Non-derivative financial liabilities				
Trading liabilities, at fair value	112.2	0.3	12.0	99.9
Trading securities sold, not yet purchased	304.0	304.0		
Securities sold under agreement to repurchase	5,199.0	5,199.0		
Other creditors	2,418.9	2,418.9		
Derivate financial liabilities				
Derivative liabilities (excluding reserves and guarantee liabilities)	7,287.9	273.4	2,331.9	4,682.6

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for the year ended December 31, 2017

Foreign currency risk

The Group hedges its foreign exchange exposures including GBP expenses and its GBP tax position.

Operational risk

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

The primary objective of the Group's and the Company's operational risk management framework is to minimise the occurrence and impact of operational risk events, in particular avoiding extreme events, in order to support the Group's achievement of its strategic objectives.

Operational Risk encompasses areas such as transaction operations, premises and security, external suppliers, payment processes, information, data quality and records management. In accordance with market practice, the Group also recognises the importance of ramifications of the way in which the Group operates its business, which might potentially lead to conduct risk failures. Consequences could be regulatory actions including fines, public reprimands, damage to reputation, increased prudential requirements, enforced temporary or permanent suspension of operations and, in extreme cases, withdrawal of authorisation to operate.

The Group has a number of operational risk management specific processes in place, including use of KRIs. The Group recognises the benefits of using scenario analysis to assess and manage the exposure to high severity, low frequency events in order to determine the nature of operational risk losses which could potentially arise in the future.

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for the year ended December 31, 2017

19. Classification of financial assets and financial liabilities

Group	*Designated at fair value*	*Loans and receivables*	*Other financial liabilities*	*Total*
As at 31 December 2017	*US$m*	*US$m*	*US$m*	*US$m*
Financial assets measured at fair value				
Trading securities	1,376.2	-	-	1,376.2
Derivative assets	7,036.7	-	-	7,036.7
Other trading assets, at fair value	76.6	-	-	76.6
	8,489.5	-	-	8,489.5
Financial assets not measured at fair value				
Cash at banks	-	846.0	-	846.0
Securities purchased under agreements to resell	-	3,650.9	-	3,650.9
Other debtors	-	3,087.2	-	3,087.2
	-	7,584.1	-	7,584.1
Financial liabilities measured at fair value				
Derivative liabilities	7,005.2	-	-	7,005.2
Trading liabilities, at fair value	176.0	-	-	176.0
Trading securities sold, not yet purchased	681.8	-	-	681.8
	7,863.0	-	-	7,863.0
Financial liabilities not measured at fair value				
Securities sold under agreements to repurchase	-	-	2,998.0	2,998.0
Other creditors	-	-	3,538.2	3,538.2
	-	-	6,536.2	6,536.2

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Company **As at 31 December 2017**	*Designated at fair value* *US$m*	*Loans and receivables* *US$m*	*Other financial liabilities* *US$m*	*Total* *US$m*
Financial assets measured at fair value				
Trading securities	1,284.3	-	-	1,284.3
Derivative assets	7,023.0	-	-	7,023.0
Other trading assets, at fair value	76.6	-	-	76.6
	8,383.9	-	-	8,383.9
Financial assets not measured at fair value				
Cash at banks	-	702.3	-	702.3
Securities purchased under agreements to resell	-	3,650.9	-	3,650.9
Other debtors	-	3,089.1	-	3,089.1
	-	7,442.3	-	7,442.3
Financial liabilities measured at fair value				
Derivative liabilities	6,992.5	-	-	6,992.5
Trading liabilities, at fair value	176.0	-	-	176.0
Trading securities sold, not yet purchased	681.8	-	-	681.8
	7,850.3	-	-	7,850.3
Financial liabilities not measured at fair value				
Securities sold under agreements to repurchase	-	-	2,998.0	2,998.0
Other creditors	-	-	3,535.1	3,535.1
	-	-	6,533.1	6,533.1

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Group ***As at 31 December 2016***	*Designated at fair value* *US$m*	*Loans and receivables* *US$m*	*Other financial liabilities* *US$m*	*Total* *US$m*
Financial assets measured at fair value				
Trading securities	704.0	-	-	704.0
Derivative assets	7,336.7	-	-	7,336.7
Other trading assets, at fair value	30.3	-	-	30.3
	8,071.0	-	-	8,071.0
Financial assets not measured at fair value				
Cash at banks	-	458.6	-	458.6
Securities purchased under agreements to resell	-	5,537.3	-	5,537.3
Due from clients	-	3.6	-	3.6
Other debtors	-	2,917.8	-	2,917.8
	-	8,917.3	-	8,917.3
Financial liabilities measured at fair value				
Derivative liabilities	7,337.5	-	-	7,337.5
Trading liabilities, at fair value	112.2	-	-	112.2
Trading securities sold, not yet purchased	304.0	-	-	304.0
	7,753.7	-	-	7,753.7
Financial liabilities not measured at fair value				
Securities sold under agreements to repurchase	-	-	5,199.0	5,199.0
Other creditors	-	-	2,421.7	2,421.7
	-	-	7,620.7	7,620.7

Notes to the financial statements

for the year ended December 31, 2017

Company **As at 31 December 2016**	*Designated at fair value* *US$m*	*Loans and receivables* *US$m*	*Other financial liabilities* *US$m*	*Total* *US$m*
Financial assets measured at fair value				
Trading securities	608.4	-	-	608.4
Derivative assets	7,319.6	-	-	7,319.6
Other trading assets, at fair value	30.3	-	-	30.3
	7,958.3	-	-	7,958.3
Financial assets not measured at fair value				
Cash at banks	-	330.6	-	330.6
Securities purchased under agreements to resell	-	5,537.3	-	5,537.3
Due from clients	-	3.5	-	3.5
Other debtors	-	2,916.8	-	2,916.8
	-	8,788.2	-	8,788.2
Financial liabilities measured at fair value				
Derivative liabilities	7,321.9	-	-	7,321.9
Trading liabilities, at fair value	112.2	-	-	112.2
Trading securities sold, not yet purchased	304.0	-	-	304.0
	7,738.1	-	-	7,738.1
Financial liabilities not measured at fair value				
Securities sold under agreements to repurchase	-	-	5,199.0	5,199.0
Other creditors	-	-	2,418.9	2,418.9
	-	-	7,617.9	7,617.9

Notes to the financial statements

for the year ended December 31, 2017

20. Called up share capital

	Allotted, called up and fully paid 2017 US$m	*Allotted, called up and fully paid 2016 US$m*
Ordinary shares of $1 each	779.0	779.0
Preference shares of $1 each	360.0	360.0
	1,139.0	1,139.0

21. Obligations under operating leases

Annual commitments under non-cancellable operating leases at the reporting date are as follows:

Group

	Land and buildings 2017 US$m	*Other 2017 US$m*	*Land and buildings 2016 US$m*	*Other 2016 US$m*
Operating leases which expire:				
Within one year	4.8	0.1	5.4	0.1
Between two and five years	8.3	0.2	10.9	0.2
Over five years	0.5	-	0.9	-
	13.6	0.3	17.2	0.3

Company

	Land and buildings 2017 US$m	*Other 2017 US$m*	*Land and buildings 2016 US$m*	*Other 2016 US$m*
Operating leases which expire:				
Within one year	4.1	0.1	4.1	0.1
Between two and five years	6.5	0.2	9.1	0.2
Over five years	-	-	-	-
	10.6	0.3	13.2	0.3

Notes to the financial statements

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22. Regulatory capital

The primary objective of the Group's and the Company's capital management is to ensure compliance with capital requirements imposed by external regulators. Regulatory capital comprises share capital, share premium, regulator-verified profits (common equity tier 1 capital or "CET1") and perpetual non-cumulative preference shares (qualifying as additional tier 1 capital or "AT1"). Balance sheet assets and some off-balance sheet items are assigned regulatory weights to arrive at the total risk exposure. The business must maintain capital ratios, a proportion of relevant capital to total risk weighted assets ("RWA"), above minimum thresholds.

Regulatory capital, risk weighted assets and capital ratios are summarised below:

	Group		*Company*	
	2017	*2016*	*2017*	*2016*
	US$m	*US$m*	*US$m*	*US$m*
Common equity tier 1 (CET1) capital				
Called up share capital	779.0	779.0	779.0	779.0
Share premium	165.0	165.0	165.0	165.0
Retained earnings	382.2	320.2	352.5	298.9
Other reserves	(0.9)	-	(0.9)	-
	1,325.3	1,264.2	1,295.6	1,242.9
CET1 regulatory adjustments				
Intangible assets	(2.0)	-	(2.0)	-
Cash flow hedges	(0.5)	-	(0.5)	-
Other	(28.5)	(24.8)	(27.8)	(24.1)
CET1 instruments of financial sector entities where the institution has a significant investment	-	-	(38.1)	(40.9)
	(31.0)	(24.8)	(68.4)	(65.0)
Total CET1 capital	1,294.3	1,239.4	1,227.2	1,177.9
Additional tier 1 (AT1) capital				
Perpetual non-cumulative preference shares	360.0	360.0	360.0	360.0
Other adjustments	-	-	(38.1)	(40.9)
	360.0	360.0	321.9	319.1
Total regulatory capital	1,654.3	1,599.4	1,549.1	1,497.0
Risk-weighted assets (unaudited)	3,940.9	4,189.5	4,004.0	3,893.6
CET1 capital ratio (unaudited)	32.8%	29.7%	30.6%	30.3%
Total capital ratio (unaudited)	42.0%	38.4%	38.7%	38.4%

The capital adequacy is monitored daily using the rules and ratios established by the BIS rules and enacted through the European Union's Capital Requirement Regulation ("CRR").

The CRR, enacted to codify the Basel III Accord, was designed to promote safety and soundness in the European financial system. It requires authorised and regulated financial institutions to maintain appropriate levels of capital to cover the risks inherent in their business model. Basel III is a supervisory framework for risk and capital management and is structured on the basis of three pillars.

Pillar 1 specifies minimum capital requirements.

Pillar 2 describes the supervisory review process and outlines the internal capital adequacy assessment process ('ICAAP') required by firms applying Pillar 1 methodologies.

Pillar 3 requires disclosure of risk and capital information to the market. These disclosures can be found on the SMBC Capital Markets website.

Management believe that the Group and the Company have been in compliance with externally imposed capital requirements throughout the year.

In order to maintain or adjust the capital structure the Group and the Company may adjust its dividend policy or the structure and liquidity of its trading assets and liabilities.

The Group and the Company manages capital so as to ensure that the capital ratio does not fall below 25%.

23. Country-by-country reporting

The table below shows that the majority of the Groups profits are generated in the United Kingdom, and therefore a higher amount of corporation tax is paid in the United Kingdom. The Group paid $5.6 million of corporation tax (2016 - $11.3 million) and generated $71.8 million in profit for 2017 (2016 - $95.6 million), producing the global cash tax rate (corporation tax paid in the year divided by total profit before tax) of 8% (2016 - 12%). The cash tax rate is lower than the UK nominal corporation tax rate because the Advanced Pricing Agreement generates a reduction in the tax charge (see note 8 for details). In addition to that, during 2017 the Company received a corporation tax refund in respect of prior years which reduced the cash tax rate further.

The basis of preparation is as follows:

Country: The geographical location of the Group considers the country of incorporation or residence as well as the relevant tax jurisdiction. In this context, the countries applicable will be:

- United Kingdom, where the Company is a majority owned subsidiary of SMBC Tokyo. The profit of the business is generated from trading securities and derivatives and business advisory activities
- Australia, the branch acts as an agent for the Company in the Australian market.
- Hong Kong, CM Asia acts as an agent and intermediary for the Company and its affiliated entities in Asian markets outside of Japan and in Australia

Turnover: The Group defines turnover as the sum of the following consolidated income statement items:

- Net trading income
- Interest income
- Interest expense

Notes to the financial statements

for the year ended December 31, 2017

Profit before tax: The definition of profit or loss before tax is consistent with that in the Group's financial statements.

Corporation Tax Paid: The cash amount of corporation tax paid in each country in the year.

Public Subsidies Received: In the context of CBCR, this is interpreted as direct support by the government. There were no subsidies received by the Group in 2017 (2016 - nil).

Number of Employees: Employee numbers reported reflect the number of employees on a full time equivalent basis.

Accounting Framework: Amounts reported are based on local statutory financial statements, in accordance with applicable law and IFRS (International Financial Reporting Standards), unless another basis has been stated.

Country-by-Country Report 2017

Country	*Turnover*	*Profit/(Loss) before tax*	*Corporation tax paid*	*Average number of employees*
	US$m	*US$m*	*US$m*	
United Kingdom	215.5	62.9	5.6	273
Australia	2.3	1.5	-	2
Hong Kong	14.4	7.4	-	14
Global Total	232.2	71.8	5.6	289

Country-by-Country Report 2016

Country	*Turnover*	*Profit/(Loss) before tax*	*Corporation tax paid*	*Average number of employees*
	US$m	*US$m*	*US$m*	
United Kingdom	222.3	94.8	11.2	222.0
Australia	1.9	0.8	0.1	2.0
Hong Kong	7.0	-	-	15.0
Global Total	231.2	95.6	11.3	239.0

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for the year ended December 31, 2017

24. Related party transactions

	2017 *US$m*	*2016* *US$m*
SMBC - Parent		
Cash at banks	335.4	5.7
Net derivative assets	1,472.0	1,128.1
Cash collateral received	2,738.0	1,921.9
Funding loans	510.3	-
Accrued interest payable	3.0	1.1
Accrued expenses payable - credit service fee	0.5	2.0
Other liabilities	1.2	1.6
Guaranteed liabilities	372.6	432.0
Gain on derivative instruments	504.8	875.2
Interest income	2.3	-
Other income	3.5	-
Interest expense	36.3	8.4
Fees and commissions paid	12.0	14.3
Other expenses	3.6	-
SMBC Nikko Securities - Parent		
Securities purchased under resale agreements	3,157.4	5,197.2
Accrued income receivable	2.5	2.0
Net interest receivable	(4.1)	3.1
Other receivables - reimbursements	5.8	0.5
Other payables - securities trading fees	0.2	0.5
Interest on securities under resale agreements	19.8	16.6
Fees and commission on securities trading	11.2	6.1
Reimbursements	3.8	2.8
Expenses on securities trading	74.6	159.8
Other fees and commissions paid	5.5	1.3
Other expenses	1.4	-

Notes to the financial statements

for the year ended December 31, 2017

	2017 US$m	2016 US$m
SMBC Capital Markets Inc		
Collateral placed	2,802.9	2,625.3
Independent amount	(310.0)	(310.0)
Accrued interest receivable	2.7	3.5
Other assets - agency fees	6.3	0.6
Trading instruments	19.8	23.3
Net derivative instrument liabilities	2,659.8	2,490.3
Trading loans	1.3	233.7
Securities sold under repurchase agreements	11.6	-
Trading instruments liabilities	112.1	67.8
Accrued expenses payable - guarantee fees / agency fees	16.7	45.8
Securities pledged by CM Inc.*	108.9	66.5
Interest income	26.4	17.0
Fees and commissions on agency trading	3.7	3.2
Other operating income - guarantee termination / intermediation fees	39.4	18.0
Loss on derivative instruments	573.8	1,060.7
Interest expenses	2.0	5.9
Other fees and commissions paid	0.2	0.2
Other operating expenses	39.0	44.6
SMBC Nikko Securities America Inc.		
Accrued income receivable	0.8	1.2
Other assets	(0.2)	-
Securities sold under repurchase agreements	-	210.8
Accrued expenses payable - securities trading fees / agency fees	0.2	0.8
Other liabilities	1.0	0.3
Fees and commission on securities trading	0.8	4.1
Other fees and commissions paid on securities trading	0.8	2.1
Interest expense on securities sold under repurchase agreements	0.2	0.7
Other operating expenses	0.5	0.3

*In the ordinary course of business SMBC DP guarantees the performance of its affiliate, CM Inc, in relation to interest rate caps sold to third parties. To protect itself against the risk, SMBC DP has obtained an indemnity from CM Inc. To support this indemnity CM Inc pledges securities collateral in the form of US Treasury bills. At 31 December 2017 the termination value of guaranteed interest rate cap transactions, against which collateral was held, was $45.7 million (2016 - $54.5 million). The guarantees are accounted for as financial guarantees.

Notes to the financial statements

for the year ended December 31, 2017

	2017 *US$m*	*2016* *US$m*
Sumitomo Mitsui Banking Corporation of Canada		
Loss on derivative instruments	-	45.6
Sumitomo Mitsui Banking Corporation Europe Limited		
Cash at banks	2.3	-
Collateral placed	-	26.4
Net derivative instrument liabilities	(58.7)	18.8
Other liabilities	1.6	1.1
Gain on derivative instruments	118.3	128.8
Loss on derivative instruments	-	-
Other fees and commissions paid	1.2	1.2
Other operating expenses	1.8	1.1
Sumitomo Mitsui Banking Corporation (China) Limited		
Net derivative instrument assets	(0.1)	(0.1)
Gain on derivative instruments	-	0.1
Sumitomo Mitsui Banking Corporation Malaysia Berhad		
Net derivative instrument assets	0.4	0.4
Cash collateral received	0.7	0.4
Gain on derivative instruments	0.4	0.4
SMBC Nikko Securities (Hong Kong) Limited		
Other liabilities	2.4	1.2
Other non-personnel expenses	7.3	6.2
Nikko Systems Solutions, Ltd.		
Other non-personnel expenses	1.4	2.7
SMBC Friend Securities		
Expenses on securities trading	1.8	0.2
Other fees and commissions paid	0.1	-

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25. Fee in respect of credit guarantee

The Group has entered into unconditional guarantee arrangements with SMBC, acting through its Cayman and Tokyo branches, under which SMBC is obliged to make the full and prompt payment of any net termination payment payable to the Group under any of the ISDA Master Agreements with specific guaranteed counterparties.

Fees are payable monthly based on the average value of the guaranteed transactions. The fee has been computed on a fair value basis, discounted to its present value and recorded as a derivative liability on the balance sheet. The present value of these credit guarantees, and the associated fee expense in profit and loss, are set out in the table below:

	2017	*2016*	*2017*	*2016*
	US$m	*US$m*	*US$m*	*US$m*
	Credit guarantee liability	*Credit guarantee liability*	*Fees*	*Fees*
SMBC	62.4	71.9	10.6	12.9

In the case of an agreed termination of an existing guarantee the Group records a CVA reserve to ensure that the value of derivative contracts reflects counterparty credit risk. Consequently the Group will charge a termination fee equating to the CVA for any guarantees cancelled. The APA ensures that these guarantee arrangements are treated as arm's length transactions.

26. Financial and other commitments

In 2017, SMBC and the Group signed an agreement to provide the Group with a $2,000 million multi-currency revolving uncommitted facility. At 31 December 2017, $500.1 million of the facility was utilised.

In 2017, SMBC and the Group also signed an agreement to provide the Group with a JPY300.0 billion revolving uncommitted facility. At 31 December 2017, $10.2 million of the facility was utilised.

The Group has an earlier agreement with SMBC made in 2010 to provide the Group with a $250.0 million multi-currency revolving committed facility which can be terminated by either party at six months' notice. For this the Group pays a fee of 0.05% per annum on the undrawn amount of the facility.

SMBC acts as guarantor for some of the Group's transactions. For this the Group pays a fee based on the notional amount, maturity and deal type for each transaction, as detailed in note 25.

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for the year ended December 31, 2017

Under a loan agreement dated 18 April 2016, CM Inc has committed to providing SMBC DP with a $200.0 million revolving credit facility for a five year period. A commitment fee on the amount of the undrawn facility is payable to CM Inc until the maturity date of the agreement. At 31 December 2017 and 31 December 2016, the entire facility was unused.

As described in note 24, SMBC DP guarantees interest rate caps of CM Inc. In return, CM Inc. provides an indemnity to SMBC DP supported by collateral in the form of US Treasury bills.

SMBC DP, as an AA-/Aa1 derivative product company, is required by Moody's and S&P to have a Contingent Manager. Under such an agreement, an unaffiliated derivatives dealer would provide portfolio management and other general services to the firm in the event that the long term senior rating of Sumitomo Mitsui Banking Corporation ('the bank') is downgraded to Baa3 or below by Moody's, or the event that the bank's short term rating is downgraded to P-3 or below by Moody's, or the event that the long term senior rating of the bank is downgraded to BB or below by S&P, or the event that the bank's short term rating is downgraded to B or below by S&P. On 7th December 2017 the Contingent Manager Agreement with Blackrock Financial Management, Inc. rolled for twelve months as no notice to terminate was issued by SMBC DP.

27. Deferred compensation

The Company has implemented a new remuneration policy in respect of bonus deferrals, in order to prepare for a possible transition to stricter regulations. For bonus payments made in 2018, the Company will defer 20% of the bonuses for a period of two years affecting senior employees at Executive Director level and above, whose bonus exceeds 100% of the fixed pay and £100,000 in value.

28. Investment in subsidiary undertakings

The Company has invested $200.0 million in the ordinary shares of SMBC Derivative Products Limited, a 100% subsidiary, incorporated in England and Wales, registered office One New Change, London EC4M 9AF, and $2.0 million in the ordinary shares of SMBC Capital Markets Asia Limited, a 100% subsidiary, incorporated in Hong Kong, registered office 7/F, One International Finance Centre, 1 Harbour View Street, Central, Hong Kong, the results of both of which have been included in these Group financial statements. There were no changes in investments in subsidiary undertakings in the year.

29. Sponsored unconsolidated structured entities

The Group sponsors certain structured entities in which it has no interest. The Group is deemed to be a sponsor of a structured entity when it takes a leading role in determining its purpose and design and provides operational support to ensure its continued operation.

Loss from sponsored unconsolidated structured entities, where the Group did not have an interest at the end of the year, amounted to $(0.2) million (2016 - income $8.7 million).

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30. Ultimate parent undertaking and controlling party

The Company's immediate parent is Sumitomo Mitsui Banking Corporation ("SMBC"). The Company's ultimate parent is Sumitomo Mitsui Financial Group Inc ("SMFG"), incorporated in Japan. It is the largest Group of which this Company is a member and which has included this Company in its Group financial statements. Copies of these financial statements can be obtained from the following address:

1-2 Marunouchi
1-chome
Chiyoda-ku

Tokyo, Japan