Risk and risk management
How we manage our principal risks and uncertainties

How we manage risk

Risk management is the responsibility of the Board, supported by the Risk Committee which comprises members of our Executive Leadership Team (ELT). The Risk Committee is accountable for identifying, mitigating and managing risk. Further details about the Committee can be found on page 70. Our formal risk identification process evaluates and manages our significant risks in accordance with the requirements of the UK Corporate Governance Code. Our Group risk register identifies the risks, their potential impact and likelihood of occurrence, the key controls and management processes we have established to mitigate these risks, and the investment and timescales agreed to reduce the risk to an acceptable level within the Board's risk appetite.

The Risk Committee meets twice a year to review risk management and monitor the status of key risks as well as the actions we have taken to address these at both Group and functional level. Any material changes to risk are highlighted at the monthly ELT meetings, while the Audit Committee also reviews the Group's risk report. The ELT undertakes a risk workshop each year to challenge whether it has identified the principal risks that could impact the business in the context of the environment in which we operate.

Management is responsible for implementing and maintaining controls, which have been designed to manage rather than eliminate risk. These controls can only provide reasonable but not absolute assurance against material misstatement or loss. See page 68 for further information regarding internal controls.

Principal risks and uncertainties

The following pages set out the principal risks and uncertainties that could crystallise over the next three years. The Board has undertaken a robust risk assessment to identify these risks, which are listed in order of potential impact. There may be other risks that we currently believe to be less material. These could become material, either individually or simultaneously, and significantly affect our business and financial results. We have modelled potential scenarios of these risks crystallising to support the disclosures in the Viability Statement and assess the Group's risk capacity. See page 41 for further details. Due to the nature of risk, the mitigating factors stated cannot be viewed as assurance that the actions taken or planned will be wholly effective.

De La Rue's risk management framework

Board of Directors and Company Secretary

- Responsible for risk management and internal controls
- Defines risk appetite and tolerance
- Approves the risk profile

Audit Committee
- Reviews the effectiveness of internal controls
- Approves the annual internal and external audit plans
- Reviews findings from selected assurance providers

Risk Committee
- Reviews and proposes the business risk profile
- Monitors the management of key risks
- Tracks implementation of actions to mitigate risks

Ethics Committee
- Reviews ethical risks, policies and standards

Health, Safety and Environment (HSE) Committee
- Sets HSE standards
- Agrees and monitors implementation of HSE strategy
- Monitors HSE performance

Executive Leadership Team
- Accountable for the design and implementation of the risk management process and the operation of the control environment

Group policies
- Policies for highlighting and managing risks
- Procedures and internal controls

Functional management
- Ensures that risk management is embedded into business culture, practice and operations

Risk appetite

The Board has reviewed our principal risks and considered whether they reflect an acceptable level of risk. Where this is not the case, the Board has also considered what further investment is being made to reduce the likelihood and potential impact of the risk. The Board either approves the level of risk being taken, or requires management to reduce the risk exposure.

For core areas of the business, the Board uses a number of methods to ensure that management operates within an accepted risk appetite. These include delegated authority levels, the approval of specific policies and procedures and the approval of the annual insurance programme. The Board receives regular feedback on the degree to which management is operating within acceptable risk tolerances.

This feedback includes regular operational and financial management reports, internal audit reports, external audit reporting and any reports to the whistleblowing hotline. All members of the ELT have individual ownership for one or more of the principal risks. Management of those risks forms part of their personal objectives.

Key for strategic focus

1. Deliver operational excellence
2. Invest for growth
3. Strengthen balance sheet
4. Drive culture change

Key for risk outlook

- Increasing
- No change
- Decreasing

Principal risks and uncertainties ranked by net predicted impact

Risk	Exposure	Impact	Mitigation	Impact on strategy	Outlook
Breach of legal and regulatory requirements	It is possible that our employees or overseas representatives, either individually or in collusion with others, could act in contravention of our stringent requirements in relation to bribery and corruption, anti-competitive behaviours and management of third party partners (TPPs).	Major reputational and financial damage. A successful prosecution under Anti-Bribery legislation could see the Company barred from participating in major tenders.	We are accredited to the Banknote Ethics Initiative, which provides governments and central banks with assurance regarding our ethical standards and business practices. Our commitment to ethical standards is articulated in the Code of Business Principles. This is supported by underlying policies which are reviewed regularly and enforced robustly. Where necessary, non-compliance is dealt with through disciplinary procedures. We have a particular focus on raising awareness as well as training on anti-bribery and corruption, and competition law. Our policies and processes are independently audited. Our process for the appointment, management and remuneration of TPPs operates independently of the sales function. The behaviours of TPPs are strictly monitored and the TPP process is overseen by the General Counsel and Company Secretary, who reports directly to the Board on these matters. To reduce the exposure of TPPs, we are working on migrating them to employee relationships. Our whistleblowing policy and associated procedures are integral aspects of the compliance framework.	4	–
Mergers and Acquisitions	We are seeking to grow our business both organically and through appropriate partnerships and acquisitions.	Acquiring or partnering with third parties carries a level of inherent risk that the transaction may not achieve the expected business benefits over the medium to long term.	We have a controlled process for reviewing all opportunities that have to meet certain criteria before being able to progress to full due diligence and offer stage. The Board has to approve all such transactions before they can proceed.	2	↑

Risk and risk management continued

Principal risks and uncertainties ranked by net predicted impact

Risk	Exposure	Impact	Mitigation	Impact on strategy	Outlook
Failure to maintain and exploit competitive and technologically advanced products, services and manufacturing processes	We operate in competitive markets. Our products and services are characterised by continually evolving industry standards and changing technology, driven by the demands of our customers. Longer term threats could include the growth of eCommerce, the emergence of cashless societies and lower barriers to manufacturing.	Failure to maintain and exploit technical innovation and intellectual property may result in lower demand, loss of market share and lower margins.	We maintain sustained levels of investment in research and development to ensure a steady flow of ideas into our innovation pipeline. Our product roadmaps are designed to meet our customers' needs. Our materials science expertise and software science team are centralised in the UK. These teams follow defined technology management processes, which include regular pipeline and portfolio reviews. We continue to invest in new technologies to enable us to advance our R&D and manufacturing capabilities, and have increased our focus on digital technologies since the strategy review in 2015. We aim to double our R&D investment in the five years to 2020.	2	–
Quality management failure	Each of our contracts has a unique specification on product quality and delivery. Some of these contracts demand a high degree of technical specification.	A shortfall in quality management may expose us to additional cost to remake as well as to any associated fines or warranty costs.	We operate an established quality management system across all production sites. All major sites are certified to ISO9001 quality management standards. In 2012, we introduced an Operational Excellence programme to further drive continuous improvement across our manufacturing sites. In 2017-18, we introduced further capital and operational investment to increase quality management in response to increasing quality standards demanded by our customers.	1	–
Supply chain failure	We have close trading relationships with a number of key suppliers, including unique producers of specialised components that we incorporate into our finished products. With the sale of Portals De La Rue Limited, our paper supplier now moves to become a third party supplier.	Failure of a key supplier, the inability to source critical materials or poor supplier performance in terms of quality or delivery could disrupt our supply and ability to deliver on time and in full.	Where we rely on external supply, we have established procedures for identifying possible risks for each supplier. Key suppliers are managed through a supplier relationship management programme. This incorporates checks on their financial strength and their ability to deliver to our quality standards and security, as well as their business continuity arrangements. Key suppliers are audited on a rotational basis. As a contingency, alternative suppliers are pre-qualified wherever possible and where necessary we retain higher levels of stocks.	1	↑
Unpredictability in the timing and size of substantial contract awards	Political and other factors can delay government procurement decisions for sensitive products such as banknotes and passports.	The timing and size of contract awards is often uncertain. Delays lead to volatility in our order book and variance against our predicted financial performance.	We maintain close and regular contact with customers so that any changes in timing and requirements are recognised promptly. We monitor our sales activity, order pipeline and forward order book to optimise production planning and ensure that delivery to customers is on time and in full. We also monitor any delays in order confirmation on a weekly basis. This enables us to maintain flexibility in the supply chain as far as possible, and to accommodate any changes to production planning. To minimise future unpredictability, we proactively pursue longer term commitments from customers. We also aim to grow recurring revenues by expanding our digital and service offerings.	1 3	–

Principal risks and uncertainties ranked by net predicted impact

Risk	Exposure	Impact	Mitigation	Impact on strategy	Outlook
Failure to win or renew a material contract	While we operate globally and have a diversified geographic, product and customer profile, we rely heavily on a small number of medium and longer term material contracts.	Failure to win or renew a key contract could restrict growth opportunities and have a material impact on our financial performance and reputation.	Our business involves tendering for long term contracts on a constant basis. We have dedicated bid specialists and where necessary contract in additional resources for the largest strategic bids. We employ complex sales methodologies to identify and qualify opportunities. These measures, along with our focus on customer service and quality mean that we are well positioned to win or renew strategic or significant contracts. We are focused on retaining key contracts, as and when they fall due for renewal, and on winning new opportunities as they arise. However, as the UK Passport contract award announced in March 2018 shows, there can be no certainty that we will win all major contract tenders. Our order book as at March 2018 was 6% above that of March 2017.	1 2	–
Capacity for change	Our business has seen a considerable level of organisation change over the last three years. The Board expects there to be a similar level of change over the next two to three year period.	All grades of staff may become demoralised by the level of constant change in the organisation. Processes, procedures, and control environments may suffer as the ELT continues to implement change.	Our change goals are incorporated into the annual objectives each year, so that all staff understand and are familiar with our priorities. All change initiatives are reviewed and approved by the ELT following risk analysis. All change initiatives are managed through programme managers with progress monitored and reported to the ELT and Board.	4	↑
Pension fund deficit	The Group's UK defined benefit pension scheme (the Scheme) is in deficit. As at 31 March 2018 the deficit as accounted for under IAS 19 was £87.6m (25 March 2017: £237.0m).	We have created a joint working group with the pension trustees to proactively manage our pension obligations. If at the next triennial valuation in 2018 the deficit increases further under actuarial valuation, the future cash flow commitments may put future capital investment and dividends at risk.	We continue to work with the pension trustees to explore methods of improving the return of the Scheme's assets and reducing the Scheme's liabilities. As announced in November 2017, the trustees changed the primary index for increased Scheme benefits to the Consumer Prices Index. The movements in the assets and liabilities as measured under IAS 19 are in note 24 of the financial statements.	3	↓
Loss of a key site	All our manufacturing sites are exposed to business interruption risks.	The total loss of any one of these sites could have a major financial impact, particularly where the site represents a single source of supply.	Our head office and the banknote production operations in Debden and Gateshead UK are both accredited to the ISO22301:2012 Business Continuity standard. We maintain a degree of interoperability across our banknote production and security printing sites. We aim to minimise risk by adopting the highest standards of risk engineering in our production processes. In recognition of our customers' increasingly high requirements regarding business continuity, we continue to enhance the resilience of our major facilities in line with the ISO standard.	1 2 3	–

Risk and risk management continued

Principal risks and uncertainties ranked by net predicted impact

Risk	Exposure	Impact	Mitigation	Impact on strategy	Outlook
Health, safety or environmental failure	All of our activities are subject to extensive internal health, safety and environmental (HSE) procedures, processes and controls. Nevertheless, there is a risk that any failure of an HSE management process could result in a serious incident.	Failure of an HSE management process could lead to a serious injury or an environmental breach.	At all major facilities, we have a robust HSE management system which is internally audited and certified to the OHSAS18001 and ISO14001 standards. All of our activities are subject to extensive internal HSE procedures, processes and controls. The Group HSE Committee regularly reviews HSE performance. This is also monitored by the Chief Operating Officer's leadership team and reported to the Board monthly. Each manufacturing facility has clear HSE action plans which are prioritised, monitored and subject to review by local senior management to ensure that health and safety standards are maintained.	1 2 3	–
Functionality and information security risk	Increasingly, our business involves providing software to customers. Poor quality of the functionality and information security built into the software and associated hardware could affect the confidentiality and integrity of our customer, employee and business data. Factors that could potentially impact functionality and information security include human error, ineffective design or operation of key data security controls, or the breakdown of IT control processes.	Any compromise in the software functionality or confidentiality of information could impact our reputation with current and potential customers.	Our corporate information systems are accredited to the ISO27001 Information Security standard. We strengthened governance processes in 2017 with the introduction of an Information Security Steering Group. We maintain a strict control environment to enforce disciplined software development and information security practices and behaviours. A number of key technical controls are in place to manage this risk, including agile software development techniques, quality reviews, regular testing, network segregation, access restrictions, system monitoring, security reviews and vulnerability assessments of infrastructure and applications. We regularly review all aspects of information security arrangements, and our employees undertake mandatory information security e-learning.	1 2	–
Product security	Loss of product or high security components from a manufacturing site could occur as a result of negligence or theft. Loss of product while in transit, particularly during transhipment, through the failure of freight companies or through the loss of an aircraft or vessel as a result of an accident or natural disaster, is also possible.	Any loss of product or high security components has the potential to cause reputational and financial damage. In certain circumstances, customer contracts may mean that we are liable for those losses.	We have robust physical security and materials control procedures at our production sites, which reduce the risk of inadvertent loss or theft during manufacturing. We apply stringent operational procedures – and use carefully selected carriers and personnel – to handle movements of security materials between our sites and onward delivery to customers. All movements are risk managed and monitored globally on a 24/7 basis. We also maintain a comprehensive global insurance programme.	1 2	–

Risks and uncertainties where the net impact has reduced since prior year, and which are no longer regarded as principal risks and uncertainties

Risk	Exposure	Impact	Mitigation
Cultural change	In order to ensure our continued success and growth, an internal organisational redesign took place in 2015/16. The focus is on achieving sustained cultural change in our organisation to be able to adapt to a rapidly changing market environment.	Without the culture change we seek to achieve, we may not be able to execute the strategy laid out in May 2015.	As reported in 2017, our 2016/17 leadership training built on the 2015/16 strategic leadership skills with a focus on cross functional working, especially in the areas of influencing and managing competing interests. The strategic plan envisaged a three year programme of training, communication and recruitment to fill capability gaps. The outcome is expected to be a change in behaviours and skills that will allow De La Rue to be a more dynamic, agile and high performing organisation. The plan remains on track and has delivered substantial cultural change. The Executive Leadership Team now considers change fatigue to be a greater risk to the business. Consequently this risk is no longer seen as a principal risk, although it continues to be monitored at a functional level.
Failure to secure a partner for the banknote paper business, or a strategic print partner for the Banknote print business	Our ability to address the material issues of volatile demand in banknotes and over capacity in the banknote paper business will not be achieved without third party agreements.	Predictability of future revenue streams and the ability to increase the ROCE may be compromised.	The sale of Portals De La Rue Limited to Epiris has mitigated this risk such that it is no longer a principal risk.

Viability statement

The Directors have considered the longer-term viability of De La Rue plc in line with the recommendations under the UK Corporate Governance code.

While the Group has a five-year strategic planning horizon, our financial performance is inherently less predictable in years four and five because good visibility of the order book is over a shorter-term horizon. Therefore, the Directors believe that an appropriate period to consider the Group's viability is over three years.

In assessing the viability of the Group, the Directors have reviewed the principal risks as set out in pages 37 to 40 and considered foreseeable scenarios of one or more of the principal risks crystallising in the same time period in the context of our strategic plan. The scenarios have been modelled on year end net debt as well as forecast average net debt over the next three fiscal years.

The forward looking financial information upon which the impact of the risks was modelled, accounted for the loss of the UK Passport contract and the sale of Portals De La Rue paper business announced in March 2018.

The Directors have focused on principal risks that could plausibly occur and result in the Group's future operational results, financial condition and future prospects differing materially from current expectations, including the ability to maintain a dividend, meet current investment plans and comply with liquidity ratios.

Scenarios that the Directors see as implausible (or outside of the Group's control e.g. a terrorist attack or an event of nature) have not been modelled, nor have all potential mitigating responses. The Directors have assumed that the current revolving credit facility remains in place with the same covenant requirements through to December 2021.

The outcome of modelling the principal risks crystallising in a plausible combination showed that the Group's credit facilities were not exhausted. The Board also considered a reverse stress test; the extent of EBITDA the Group would have to lose against its strategic plan forecast in order to breach its credit facilities.

The result of reviewing plausible scenarios and the reverse stress test is that the Directors have a reasonable expectation that the Group is viable and will be able to meet its obligations as they fall due up to March 2021.