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 69. 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. 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.

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.

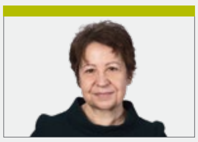
De La Rue's risk management framework

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

PRINCIPAL RISKS AND UNCERTAINTIES RANKED BY NET PREDICTED IMPACT

Key for strategic focus

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

Key for risk outlook

Increasing
Decreasing
No change

Exposure	Impact	Mitigation	Impact on strategy	Outlook
Bribery and corruption				
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. There is zero tolerance to non-compliance and it is dealt with through disciplinary procedures. We have a particular focus on raising awareness through local Ethics Champions as well as training on anti-bribery and corruption, and competition law. Our policies and processes are independently audited. Our rigorous 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. This is further enhanced by external due diligence checks. 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, which is complemented by a whistleblowing hotline.	4	No change
Failure to integrate and execute M&A activity				
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. This process is led by a skilled in-house M&A team which is supported by each function within the Company and experienced legal and financial advisers. The Board has to approve all such transactions before they can proceed.	2	No change
Failure to innovate and modernise to be competitive				
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 e-commerce, 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 R&D to ensure a steady flow of ideas into our innovation pipeline. Our product roadmaps are designed to meet our customers' needs and to ensure a clear and tested product roadmaps and lifecycle methodology. We continue to invest in modern and cost effective techniques and emerging 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 operate an active digital scouting for technology and digital companies, and collaboration with universities to ensure that we remain aware of new technologies.	2	Decreasing
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 end to end quality management system with defined standards and acceptable limits for all products across all production sites. The process is run by dedicated quality professionals. 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 2018/19, we introduced further capital and operational investment to prioritise on automated detection technologies to enhance quality across all product lines and ensure customer focused delivery.	1	Decreasing

Risk and risk management continued

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Failure of a key supplier				
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 strengthened procedures for identifying possible risks for each supplier as part of the Procurement Transformation Programme, launched in November 2017. Key suppliers are monitored and managed through supplier analytics and contract management programmes. This ensures that all key supplier contracts have been reviewed on their financial strength and their ability to deliver to our quality standards and security, as well as their business continuity arrangements as a part of the onboarding process. Key suppliers are audited on a rotational basis and have a recovery plan in case of failure. As a contingency, alternative suppliers are pre-qualified wherever possible and where necessary we retain higher levels of stocks.	1	No change
Inability to accurately forecast financial information				
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 as part of a data driven customer relationship management programme 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. This has included a core focus on improving month end close procedures. We also actively monitor and track actions or 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.	3	No change
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 have continued engagement with national and international governments to enable expansion of new markets. We employ complex sales methodologies to identify and qualify opportunities. These measures, along with our strong focus on customer service and improving our 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 continued acquisition of 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.	3	No change
Management lack of bandwidth and clear prioritisation to execute the strategy and run the business				
Our business has seen a considerable level of organisational 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 of Transform, Fix and Run are incorporated into the annual objectives each year and cascade via each functional area to provide line of sight to strategy 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	No change

Exposure	Impact	Mitigation	Impact on strategy	Outlook
Pension fund liability				
The Group's UK defined benefit pension scheme (the 'Scheme') is in deficit. As at 30 March 2019 the deficit as accounted for under IAS 19 was £76.8m (31 March 2018: £87.6m).	We have created a joint working group with the pension trustees to proactively manage our pension obligations. The next triennial valuation is near to completion.	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. We have also appointed external advisers to the Company, who are advising on how to reduce the risk to the Company balance sheet.	3	
Loss of a key site or process				
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 accredited to the ISO22301:2012 Business Continuity standard. This is supported by site based business continuity coordinators who ensure that all other sites are aligned to ISO22301:2012 standards. 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. These controls are monitored via internal auditing and through monthly business continuity forums, quarterly business continuity management steering committee meetings and annual ELT/audit committee. Risk outlook has increased due to number of reported site risks and escalations.	1	
Failure in health, safety and environment controls				
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 HSE resources and a robust 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, which are being updated to meet ISO45001:2018 requirements. 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 4	
Breach of information security				
A breakdown in the control environment including collusion, non-compliance or an external attack could lead to a cyber security breach resulting in the loss of critical data.	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. This is supported by an independent information security team which is focused on ensuring that all hardware and software deployed has compliant and secure security built in. 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, behaviour analytics, quality reviews, regular testing, network segregation, access restrictions, system monitoring, security reviews and vulnerability assessments of infrastructure and applications. We also conduct supplier reviews on a risk basis and ensure all of our employees undertake mandatory information security e-learning. Our processes and policies are monitored and audited internally and externally.	1 4	

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Breach of 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 dedicated security personnel, robust standardised physical security and materials control policies and procedures at our production sites, which reduce the risk of inadvertent loss or theft during manufacturing. This is overseen and monitored by Group Security, HSE and Risk to ensure compliance. Vetting of personnel, training and auditing is conducted in line with the Group Baseline Security Manual. We apply risk assessed stringent operational procedures – and use vetted and approved carriers and personnel – to handle movements of security materials between our sites and onward delivery to customers. All movements are monitored, risk managed and conducted in line with TAPA standards. We also maintain a comprehensive global insurance programme. We also ensure that product security verification and reconciliation are embedded and monitored throughout all sites to ensure that product is stored, shipped, reconciled and destroyed securely and safely.	4	No change
Breach of sanctions				
Entering a contract or other commitment with a customer, supplier or partner which is subject to a sanction or trade embargo could lead De La Rue to be in breach of sanctions. This is a new risk in FY19. Following review by the Audit Committee and in light of continuing developments in this area, the Board considers being in breach of sanctions to be a key risk in achieving the Group's objectives.	Breach could result in imprisonment and substantial fines for individuals, the leadership team, the Board and the Company. In addition it may lead to a withdrawal of our banking facilities, as well as disbarment from future tenders.	We utilise strong policies and processes to ensure national and international sanction compliance. This will be overseen by the newly created Sanctions Board and external auditing of the programme. Commercial opportunities are considered against the sanction risk as standard within the RFA process and we utilise customer relationship management systems to identify medium and high sanction risk opportunities. If identified these are investigated by legal, treasury and commercial teams to ensure compliance.	3	

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.

Whilst the Group has a five year strategic planning horizon, the financial performance of the Group 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 and mitigations as set out in pages 37 to 40 and considered plausible scenarios of one or more of the principal risks crystallising in the same time period in the context of its strategic plan.

The two risks identified as having the largest impact on the viability of the Group were:

- Failure to innovate and modernise
- Failure to win or renew a material contract

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 to materially differ from current expectations, including the ability to maintain a dividend, meet current investment plans and comply with Banking covenants. The Board has focused on the impact of these risk scenarios on Group EBITDA, as the limiting factor is the Net Debt/EBITDA covenant, not the absolute value of net debt.

Scenarios that the Directors see as implausible (or outside of the Group's control eg 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 2023. The current facility expires in December 2021, however the Directors are comfortable that the facility will be renewed with the same covenant requirements as the Company enjoys continued strong support from its relationship banks.

Based on the forecasts, net of mitigations for the three years modelled, the maximum reduction in EBITDA that could be supported by the Group before the net debt/EBITDA covenant is breached is 35-40%.

The Directors have reviewed a detailed report of four scenarios over the three year timeframe and the impact that the materialisation of the risks has on the Group's EBITDA and net debt, in order to assess the ability of the Group to maintain its operations within the facility and covenant headroom of its current banking facilities.

Based on the review of these scenarios over the three year period, the Directors are comfortable that there are no recurring breaches of the Group's net debt/EBITDA covenant and therefore have a reasonable expectation that the Group is viable and will be able to meet its obligations as they fall due up to March 2022.

This conclusion is based on the current strategic plan approved by the Board and we acknowledge that we operate in a changing commercial environment which may cause this plan to adapt. In responding to changing conditions, we will continue to evaluate any additional risks involved which may impact the business model and future viability.