

# RISK MANAGEMENT

The aim of risk management within HKScan Group is to enable uninterrupted business operations and to safeguard conditions for achieving its business objectives.

Risk management is embedded in the HKScan management system and is based on the consistent identification, assessment and reporting of risks throughout the Group. The company's ERM process aims to promote risk awareness and effective, proactive risk management throughout the Group, and to ensure that management and the Board of Directors are in possession of sufficient information on risks to support their decision-making. The risk policy approved by the Board is applied in all operative HKScan Group companies.

The Board of Directors and CEO have responsibility for the strategy and principles of risk management within the Group and for managing risks that threaten the Group's strategic intents. Operative risks are the responsibility of the managers of the respective Business and Group functions. The CFO is responsible for managing financial risks and Group insurance policies.

At HKScan, risks are divided into four main categories: strategic risks, operative risks, economic risks and risks of damage. At Group level, the company strives to identify and regularly assess all significant risks inherent in the material balance sheet and income statement items and to determine key controls for risk prevention.

Strategic risks are assessed as a part of the annual strategy process and also in connection with major business decisions.

Operative risks are assessed not only in connection with the annual plans, but also as part of day-to-day business operations.

Economic risks and risks of damage are minimized as far as possible by applying policies and guidelines drafted for this purpose.

## HKSCAN'S MOST SIGNIFICANT RISKS

### STRATEGIC RISKS

#### FLUCTUATION IN THE AVAILABILITY AND PRICES OF RAW MATERIALS

There is variability in the prices and availability of raw materials needed for the production of HKScan products, such as feed, pork, poultry and beef. Global overproduction of feed and raw materials decreases the prices of raw materials and increases their availability, while underproduction leads to lower availability and rising raw material prices. Economic cycles, the EU's Common Agricultural Policy, trade barriers and subsidy changes affect the balance of supply and demand in the long term.

Factors rapidly affecting supply, such as animal disease epidemics, may occasionally distort the balance of supply and demand. The prices of products sold to retail are agreed months in advance in Finland, Sweden, Denmark and the Baltics, and under these circumstances, unforeseen increases in raw material prices cannot be carried over into product prices quickly enough. This may also be difficult even in situations where prices have not been agreed in advance.

HKScan has delivered a promise of 100 per cent domestic meat content in its main brands, HK<sup>®</sup>, Kariniemen<sup>®</sup> and Scan<sup>®</sup>. Although this gives HKScan a competitive edge over imported brands, it also makes HKScan vulnerable if domestic meat production declines.

HKScan has established a special procedure for monitoring key cost drivers of raw material prices, such as oil, electricity and grain. Based on the data it collects, HKScan makes module projections of the future price and availability of raw materials.

HKScan is facing growing competition in all market areas not only from other industrial producers, but also from retail chains, which are increasingly competing on the food market with their own products and brands. This local competition is intensified by multinational operators and competitors based in lower-cost countries.

The company is responding to this increased competition by strengthening its brands and innovation, improving the efficiency of its core processes, investing in high-quality products and supply reliability, forming closer ties with its producers, and more efficiently leveraging Group synergies.

## **ADAPTATION OF OPERATIONS TO POSSIBLE CHANGES IN LEGISLATION OR REGULATION AND DEPENDENCE ON THE AUTHORITIES**

HKScan's operations are regulated by the legislation of the respective countries in which the company operates. Regional and supranational regulation, such as EU legislation, also affects the company. The management affirms that HKScan operates in full compliance with all relevant legislation and other regulations. Legislation and other regulations and the interpretations thereof may change, however, and the company cannot guarantee compliance with altered requirements unless the required material actions are taken. The company is also dependent on the authorities in the countries in which it operates. Official procedures may also vary considerably in the company's various sectors of business. In addition, various unexpected actions potentially taken by pressure groups may cause restrictions to the business or volatility in demand.

## **ACQUISITIONS AND INTEGRATION OF ACQUIRED BUSINESSES**

HKScan may acquire, either in its current market areas or in new geographical areas, companies that enhance its competitive position. Risks relating to acquisitions include potentially unknown liabilities, potential inability to integrate and manage the business and personnel of an acquired company, and the risk of benefits or synergies not materializing as planned. In addition, exclusion from industry consolidation might have an adverse effect on HKScan's strategic competitive position. Expansion into new geographical areas might also cause problems relating to exchange rate fluctuations, unexpected changes in statutory requirements, changes in and compliance with local legislation and regulations, as well as political risks.

## **OPERATIVE RISKS**

### **ANIMAL DISEASES**

An outbreak of animal disease such as African swine fever, avian influenza, Newcastle disease or foot-and-mouth disease may affect the company's business and demand for its products. Animal diseases may have a long-term impact on consumer behaviour, although HKScan's management believes that consumption usually normalizes within a reasonable period of time after the discovery of an outbreak. The animal disease risk is evened out to some extent by consumption shifting to the company's other meat product groups. In a fully integrated value chain, such as is the case with most of the company's Baltic operations, the discovery of an animal disease may in the worst case scenario temporarily sever the supply of raw materials if no substitute raw material source exists.

### **DEPENDENCE ON PRODUCTION PLANTS AND THE UNINTERRUPTED OPERATION OF DISTRIBUTION CHAIN**

HKScan is dependent on the uninterrupted operation of its production plants and distribution centres. If a key production plant is destroyed or closed for any reason, if equipment is damaged in a significant manner, or other disruptions occur in production, this is likely to cause delays in HKScan's ability to produce and distribute its products as scheduled. Depending on the product, it may be possible for HKScan to transfer production to other locations, thus avoiding any significant interruptions to its operations. Changes in production of this kind may, however, be more difficult to implement in some product groups and may lead to significant delays in the deliveries of products and to lost sales, giving rise to additional expenditure before insurance coverage.

Very short lead times on delivery of orders are characteristic of the meat industry. Short lead times double the importance of an effective and dependable supply chain, underscoring the need to be able to anticipate consumer behaviour. Likewise, the reliability of logistics systems and other technological systems is extremely important. If distribution centres are damaged, destroyed or decommissioned for any reason, or if the products held in the distribution centres suffer significant damage, HKScan must come up with an alternative method of delivering products to customers until such time as the damaged distribution centre is made available again.

## **POSSIBLE PRODUCT QUALITY ISSUES**

Food safety risks concern the purity of raw materials (residues, foreign substances), the healthiness of products, packaging materials that come into contact with food, and microbiological safety. Particular attention is paid to the prevention and control of bacteria that cause food poisoning. HKScan runs rigorous in-house controls, and the facilities of all operators in the value chain are subject to strict scrutiny by the authorities as well as certified food safety management systems.

HKScan's high standard of requirements and rigorous internal control notwithstanding, the company cannot have absolute assurance of the risk-free management of the entire value chain. The realization of a risk relating to product safety or product liability may have an adverse material effect on the demand for the company's products among customers and consumers.

## **RELIANCE ON SKILLED MANAGEMENT AND EMPLOYEES**

HKScan's success is materially dependent on the professional expertise of the company's management and other personnel, as well as on the company's ability to foster the commitment of current management and other personnel and recruit new, skilled employees in the future.

HKScan is also vulnerable to potential legal or illegal strikes in the value chain or in its own operations. The risks are mitigated by developing wellbeing at work and alternative supply structures and processes.

## **ECONOMIC RISKS**

### **FINANCIAL RISKS**

Financial risks refer to unfavourable movements taking place in financial markets that may erode accrual of the company's result or reduce cash flows. The company's financial risk management aims to harness financial means to hedge the company's intended earnings performance and equity and to safeguard the Group's liquidity in all circumstances.

Financial risk management, including external and internal funding of the Group, is centralized in the Group Treasury function. HKScan's funding is obtained through the parent company, while funding to subsidiaries is arranged by the Group Treasury through intra-Group loans in the local currency of each subsidiary. Part of the Group's profits and costs are denominated in foreign currencies. Additionally, some investments and earnings are denominated in foreign currencies. The most significant exchange risks in the company's business arise from the euro, Swedish krona, US dollar and Japanese yen. The largest equities of HKScan companies are in euros, Swedish krona, and Danish krone. The Group's financial risks are presented in more detail in Note 25 to the financial statement.

## **RISKS OF DAMAGE**

### **UNFORESEEABLE FACTORS**

Natural disasters, fires, bioterrorism, sabotage, pandemics, exceptional weather conditions or other factors beyond the company's control may have an adverse effect on the health and growth of production animals or hamper the company's operations due to power outages, damage to production and property, disruptions in distribution chains, or other reasons.