

# RISK MANAGEMENT

## ENTERPRISE-RISK MANAGEMENT PROGRAMME

The Group has an established enterprise-wide risk management programme that aims to provide a structured basis for proactively managing financial, operational, compliance, information technology and sustainability risks in all levels of the organisation.

Risk management is a regular board agenda item.

PRINCIPAL RISK	SPECIFIC RISK WE FACE	RISK MITIGATION
<b>Strategic Plan and Innovation</b>	<p>The Group's branded business in the USA, the Philippines and the Indian subcontinent through the <i>Del Monte</i> brand, and in Asia and the Middle East through the <i>S&amp;W</i> brand, is affected by evolving consumer preferences and trends towards fresh and increased shopping in perimeter of the store, convenient products, competition and consumer perception.</p> <p>Product innovation is one of the Group's strategic pillars. The success of new product launches is key to the attainment of the Group's strategic plan.</p> <p>Supply chain support and marketing plans are critical capabilities for new products to succeed and be profitable.</p>	<ul style="list-style-type: none"> <li>• Ensure new product launches and platform criteria are met to improve likelihood of new product success and breakthrough by implementing the following measures:               <ul style="list-style-type: none"> <li>– Increase resources on innovation</li> <li>– Extend our portfolio into attractive, growing and profitable adjacencies</li> <li>– Prioritise effective execution and project management to improve profitability and cash flow</li> </ul> </li> <li>• Differentiate new products from existing categories, ensure high quality standard and appealing product design</li> <li>• Leverage our brand heritage for growth and position new products that address consumer needs and preferences</li> <li>• Compete effectively in existing and adjacent categories at a price consumers are willing to pay; penetrate new channels</li> <li>• Develop communication materials to highlight the product benefits and monitor competitors' responses; create the demand for these new products</li> </ul>
<b>Branded and Non-Branded Business</b>	<p>The Group's core categories in the US – Canned Vegetables, Canned Fruits and Canned Tomato – are large categories that generate strong cash flows but are slowing down.</p> <p>Certain non-branded business of the Group (including USDA and certain private label) requires a competitive bidding process which is speculative and volatile. The profitability of such bids is a challenge.</p>	<ul style="list-style-type: none"> <li>• Increase funding on product and packaging innovation, extend our portfolio in attractive adjacencies and expand distribution reach and penetration into new channels</li> <li>• Shift to branded, value-added and packaged products, limit private label business to select strategic customers and narrow the USDA business over time to limit potential future volatility</li> <li>• Leverage the Group's joint venture with Fresh Del Monte Produce, Inc. through collaboration on new product innovations such as chilled juices, fruit snacks and avocado products</li> <li>• Focus resources to grow the core business market share by reinforcing consumption-driven marketing communication strategies</li> </ul>
<b>Trade Spending</b>	<p>In the US, a large portion of sales expense is for trade promotion activities. Management of trade promotion activity is important.</p>	<ul style="list-style-type: none"> <li>• Assess efficiency of trade spending to adjust and optimise promotion strategies</li> <li>• Explore various programmes and tools to better manage and rely less on trade promotion</li> <li>• Channel funds to marketing, product investment and innovation</li> </ul>

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<b>Supply Chain Optimisation</b>	<p>The Group's success with planned new products relies on the capabilities of its supply chain. New platforms necessitate changes in the Group's business model.</p> <p>The use of co-manufacturers will hasten the speed at which the Group develops new products. Food safety and compliance with the Food Safety Modernization Act impact brands, customer relationship and profitability.</p>	<ul style="list-style-type: none"> <li>Executed the sale of the Sager Creek business and the shutdown of the Arkansas plant and the Plymouth plant in FY2018</li> <li>Rationalise the Group's manufacturing and distribution footprint</li> <li>Implement a robust transformation programme that instills ownership and accountability across the supply chain to deliver the plans</li> <li>Institute a robust co-manufacturer evaluation system for product and process qualification, monitor quality audit results and swiftly implement corrective actions</li> </ul>
<b>Financial Leverage and Capital Structure</b>	<p>The Group has long-term acquisition financing resulting in a leveraged balance sheet.</p> <p>Risks would arise if there is a general economic or industry slowdown that may impact the Group's performance, which subsequently may affect the Group's ability to service its interest and principal obligations.</p>	<ul style="list-style-type: none"> <li>The Group successfully completed the offering and listing of about US\$300 million Preference Shares in the Philippines in April and December 2017, with a coupon rate of 6.625% p.a. and 6.5% p.a., respectively</li> <li>Net proceeds were used to partly refinance the US\$350 million loan which was extended until February 2019</li> <li>The remaining balance of US\$54 million of Preference Shares is issuable within 2 years</li> <li>DMPL purchased US\$125 million of Second Lien Term Loans (as of April 2018) at a 30% discount in the secondary market providing the Group with significant interest and principal savings</li> <li>The Group also expects to meet its financial obligation by generating more cash flows through the following: <ul style="list-style-type: none"> <li>Improved cash flows in the US which accounts for approximately 75% of Group sales</li> <li>Expected cost savings from selling, general and administrative expense reduction initiatives, managing working capital, production levels, productivity enhancements and operational efficiencies</li> <li>Expected sales and profit growth in the Asian business with the continuous expansion of the S&amp;W brand in Asia and the Middle East both in packaged and fresh products and growth of the Philippine business through its market leadership position</li> </ul> </li> <li>The Group manages its interest rate risk by swapping variables with fixed interest rates <ul style="list-style-type: none"> <li>The majority of the term acquisition loans in the USA have already been swapped to fixed rates in February 2014, which took effect beginning February 2016 until 2021</li> </ul> </li> </ul>
<b>Working Capital Management</b>	<p>There is excess inventory due to challenges in demand planning, crop tonnage, sales forecast and order fulfillment.</p>	<ul style="list-style-type: none"> <li>Improve demand planning and adjust production plan to manage inventories and reduce wastage and obsolescence</li> <li>Conduct better oversight and monitoring of inventories using warehouse management system</li> <li>Execute the Group's strategic plans to improve cash flow and profitability by strengthening the core business and introducing new product innovations and streamline operations</li> </ul>

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<b>Tax</b>	<p>In the Philippines, the government passed a new regulation, Tax Reform for Acceleration and Inclusion (TRAIN), which applies a tax on beverages with added sugar, petroleum products and coal, among others, which impact the cost of operation. Sixty percent of the Group's beverage products, namely 100% fruit and vegetable juices, are not subject to this tax.</p> <p>The Group may lose certain tax incentives should it fail to comply with the conditions for the tax incentive.</p> <p>The Group may be exposed to additional losses from write-offs of deferred tax credits should the operations in the US continue to incur losses.</p>	<ul style="list-style-type: none"> <li>• Implement plans to reduce the impact of the sugar tax by spreading the price adjustment across categories in order to temper the beverage price adjustment and protect consumption and volume</li> <li>• Optimise production of 100% juice which is exempt from the sugar tax and work on product reformulation to mitigate the impact</li> <li>• Work on cost savings from sales, general and administrative expense reduction initiatives, management of working capital, production levels, productivity enhancements and operational efficiencies</li> <li>• Implement measures to comply with conditions related to the tax incentive</li> <li>• Proper execution of the Group's strategic and annual operating plan to meet its projected income in the US</li> </ul>
<b>Operations</b>	<p>As an integrated producer of packaged and fresh fruit products for the world market, the Group's earnings are inevitably subject to certain other risk factors, which include general economic and business conditions, change in business strategy or development plans, international business operations, production efficiencies, input costs and availability, disruption of logistics and transportation facilities, litigious counterparties, insurgent activities and changes in government regulations, including, but not limited to, environmental regulations.</p>	<ul style="list-style-type: none"> <li>• Develop and execute a long-term strategic plan and annual operating plan supported by a business continuity plan, risk management and a corporate sustainability programme</li> <li>• Pursue productivity-enhancing and efficiency-generating work practices and capital projects</li> <li>• Continue to comply with new legislations on the environment, regulatory, taxation and labour that affect operations and proactively develop strategies to reduce the impact of these regulations</li> <li>• Manage security risks in its operating units in the Philippines by strengthening security measures and improve its stakeholder relations in the communities where it operates</li> </ul>
<b>Environmental Risks</b>	<p>Production output is subject to certain risk factors relating to weather conditions, catastrophes, crop yields, crop diseases, contract growers and service providers' performance and leasehold arrangements.</p> <p>There is no assurance that natural catastrophes or climate change will not materially disrupt the Group's business operations in the future or that the Group is fully capable to deal with these situations with respect to all the damages and economic losses resulting from these risks.</p> <p>Our business in the US operates and contractually grows food in the United States where water availability may be at risk due to drought and limited water supply, new regulations on fresh water use and grey water discharges and increasing cost.</p>	<ul style="list-style-type: none"> <li>• The Group develops and executes a long-term strategic plan and annual operating plan, supported by a contingency plan and risk management measures</li> <li>• The Group also has in place disaster recovery plans and business continuity plans to mitigate these incidents and has implemented programmes and initiatives to mitigate the effects of climate change</li> <li>• The Group has Good Agricultural Practices (G.A.P.) certifications and complies with proven agricultural practices</li> <li>• To manage any impact from heavy rainfall and floods, plantings are done in various locations to minimise tonnage loss, and towing units have been augmented to ensure continuity of harvest during wet conditions</li> <li>• The Group also works with insurance brokers to assess the risk exposure and secure adequate insurance coverage, if cost effective</li> </ul>

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<b>Cyber Security</b>	<p>The increasing global incidence of cyber-attacks on Company servers and websites demonstrates the need to strengthen and improve security of the Group's systems and avoid breach.</p> <p>Cyber-attacks can disrupt operations such as exploiting weaknesses in network devices and servers, corrupting information and stealing confidential data which can lead to financial losses.</p>	<ul style="list-style-type: none"> <li>The Group develops and implements the following measures to counter and eliminate cyber-attacks from outside sources: <ul style="list-style-type: none"> <li>Adopt industry best practice to strengthen network security such as updating security patches to the system and encrypting workstations</li> <li>Continue to monitor progress, emerging risks and control and prioritise improvements by the Data Protection and Privacy Security Task Force</li> <li>Design and implement security policies and control at each local site</li> <li>Deploy effective security governance to outside sites</li> </ul> </li> <li>The Group has engaged a third party to audit its systems and mitigate such risks</li> </ul>
<b>Information Technology Optimisation</b>	<p>The Group implemented an Enterprise Resource Planning system (S.A.P.) in the US and outsourced its finance and accounting functions to a reputable global service provider in the Philippines.</p> <p>Given the new systems and processes involved, there are risks on potential security issues and system outages resulting in lost data, business interruption, timely and accurate processing of documents, monitoring of expenditures, order fulfillment and receivables.</p>	<ul style="list-style-type: none"> <li>The Group has transitioned to a new global service provider which offers services that will improve IT operations, security, systems monitoring and control</li> <li>Other measures include providing capital budget to improve network and systems and IT support</li> </ul>
<b>Talent Management</b>	<p>The Group's capability to acquire and retain talent has an impact on the execution of the strategic plan.</p>	<ul style="list-style-type: none"> <li>In the US, the Group hired a new Chief Executive Officer, Chief Marketing Officer, Senior Vice President for Operations and the Vice President for Foodservice</li> <li>The change in leadership will help attract and retain talent</li> <li>Employee engagement is one of the strategies used to attract and retain talent</li> </ul>
<b>Group Assets</b>	<p>The Group assets are exposed to various risks relating to the assets of, and the possible liabilities from, its operations.</p>	<ul style="list-style-type: none"> <li>To safeguard its assets, the Group assesses its risk exposure annually with its insurance brokers and insurance companies</li> <li>Assets are generally insured at current replacement values</li> <li>Additions during the current year are automatically included with provision for inflation protection</li> <li>During the financial year in review, all major risks were adequately covered, except where the premium costs were considered excessive in relation to the probability and extent of a loss</li> </ul>