RAVEN PROPERTY GROUP LIMITED

Raven Property Group Limited
Risk Report

Extracted from the 2018 Annual Report

RISK REPORT

Risk Appetite

As explained in last year's annual report, the Group is adapting its balance sheet to deal with the heightened foreign exchange risk that followed the depreciation of the Rouble in late 2014:

- We reduced existing US Dollar gearing to dampen the effects of Rouble exchange rate volatility on secured debt covenant requirements;
- We have completed a number of acquisitions to enhance our Rouble income streams; and
- We are now converting all of our US Dollar secured debt into a Rouble/Euro mix of facilities.

We are well into the last stage of this transition and expect to completely eliminate any exposure to US Dollar facilities in the current year. As well as re-balancing our currency risk we believe that this will also reduce our exposure to future sanctions risks.

The fundamentals of our market have stabilised and there is a distinct possibility of a continued tightening in supply putting pressure on ERVs and property yields. We intend to continue with our acquisition and growth strategy to take advantage of the opportunities that will arise.

Risk Management and Internal Controls

Risk assessment is built into the Group's operating model and performed throughout the organisation as part of day to day operations. The Board is ultimately responsible for the management of risk and regularly carries out a robust assessment of the principal risks and uncertainties affecting the business, discusses how these may impact on operations, performance and solvency and what mitigating actions, if any, can be taken. The Audit Committee is responsible for ensuring that the internal control procedures are robust and that risk management processes are appropriate. A fuller explanation of the process is given in the Audit Committee Report. The Cypriot holding company is an important part of the day to day management of the Group's operational risks through its authorisation procedures and management oversight duties. It has also recently engaged an outsourced, internal audit function to assist with its responsibilities in managing and monitoring the effectiveness of the internal control systems in place between Cyprus and Russia. The weekly operational committee meetings for each department within the Group allow operational and management information to flow through the Group's risk matrix in a timely manner.

The risk management process is designed to identify, evaluate and mitigate any significant risk the Group faces. The process aims to manage rather than eliminate risks and can only provide reasonable and not absolute assurance.

No significant failings or weaknesses in the internal control and risk assessment procedures have been identified during the year.

Principal Risks and Uncertainties

We have set out in the following tables the principal risks and uncertainties that face our business, our view on how those risks have changed during the year and a description of how we mitigate or manage those risks. We have also annotated those risks that have been considered as part of the viability assessment.

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Political and Economic Risk

Risk	Impact	Mitigation	Change in 2018
Oil and Gas dependent economy V Oil price volatility returns leading to a weakening Rouble.	Reduced consumer demand has an impact on our customer base, reducing appetite for new lettings, the renewal of existing leases and restricting rental growth. This also leads to impaired asset values. The weak Rouble increases the cost of servicing foreign currency debt.	With little or no speculative development in the market, research continues to forecast a drop in vacancy and a tightening of rental levels. We are reducing the balance sheet reliance on foreign currency debt and this will continue in the current year.	⇨
Sanctions The use of economic sanctions by the US and EU continues for the foreseeable future.	Continued isolation of Russia from international markets and a return to a declining Russian economy.	The local market has accepted the inevitability of long term economic sanctions and this has played its part in the fundamental changes to the Russian economy. We have adapted our business model to secure our position in the market. However, the risk of increased sanctions remains.	⇨

Financial Risk

Risk	Impact	Mitigation	Change in 2018
Foreign Exchange V At the year end, 26% of warehouse GLA and 69% of secured debt had foreign currency exposure.	A weakening of the Rouble against those foreign currencies reduces our ability to service debt and reduces our profitability. US Dollar pegged leases contribute above market rental income. As those leases mature, rental income will drop.	We have significantly reduced our exposure to foreign currency secured debt facilities and will continue to do so in the current year. Our acquisition strategy and higher occupancy support our rental income levels with market level Rouble income.	⇩
Interest rates V Increases in Central Bank Rates and financing benchmarks.	The cost of debt increases and Group profitability and debt service cover reduce.	The majority of our variable cost of debt is hedged with the use of caps with terms matching the debt maturity profile.	⇨

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Property Investment

Risk	Impact	Mitigation	Change in 2018
Acquisitions V Our acquisition activity has increased significantly and we operate in an immature investment market where legacy issues are common with Russian acquisitions.	Legacy issues may erode earnings enhancement and integration into our existing systems may involve excessive management resource.	We have a strong senior management team in both our Cyprus and Moscow offices with international and Russian experience in real estate acquisitions. External advisers undertake full detailed due diligence on any acquisition projects.	⇨
Leases V Market practice increasingly incorporates lease break requirements and landlord fit-out obligations.	This can lead to uncertainty of on going annualised income due to lease break clauses. There is additional landlord risk attached to the delivery of tenant fit-out requirements.	We have a proactive property management team and continued open dialogue with tenants. We have a dedicated project management resource assigned to construction and fit-out obligations under leases. Market conditions are improving with rents increasing and vacancy dropping. Lease breaks are less likely to be exercised in this market and tenants are signing longer leases on new lettings.	⇨
Capital Expenditure V As 75% of our warehouse portfolio was built between 2007 and 2009 some elements of the buildings require replacement or modernisation.	Properties become less attractive to prospective tenants or lower rental values are achieved.	We have put in place a capital expenditure programme to maintain our properties at a Grade A level. These works should protect or even enhance levels of rent achievable.	**NEW**

Russian Domestic Risk

Risk	Impact	Mitigation	Change in 2018
Legal Framework The legal framework in Russia continues to develop with a number of new and proposed laws expected to come into force in the near future.	The large volume of new legislation from various state bodies is open to interpretation, puts strain on the judicial system and can be open to abuse.	We have an experienced in house legal team including a litigation specialist. We use a variety of external legal advisors when appropriate. Our lease agreements have been challenged and have proven to be robust in both ICAC arbitration and in Russian Courts.	⇨
Russian Taxation Russian tax code is changing in line with global taxation trends in areas such as transfer pricing, beneficial ownership of cross border cash flows and capital gains tax.	Tax treaties may be renegotiated and new legislation or clarification of existing practice may increase the Group's tax expense.	Our business is a significant contributor to inward investment in the Russian logistics sector. Our structure has developed to deal with the commercial risks of operating in Russia rather than to take advantage of tax benefits. Management and control is exerted as appropriate in each jurisdiction and the skills and experience of staff in each office reflect that commercial requirement. Ultimately, Russia remains a relatively low tax jurisdiction with 20% Corporation tax.	⇨

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Personnel Risks

Risk	Impact	Mitigation	Change in 2018
Key Personnel Failing to retain key personnel.	Strategy becomes more difficult to flex or implement.	The Remuneration Committee and Executives review remuneration packages against comparable market information; Employees have regular appraisals and documented development plans and targets; and We are continually addressing succession issues where they arise.	

Change Key

V Viability statement risk

Increased risk in the period

Stable risk in the period

Decreased risk in the period

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