RAVEN PROPERTY GROUP LIMITED

Raven Property Group Limited
Risk Report

Extracted from the 2019 Annual Report

RISK REPORT

Risk Appetite

The 2019 financial year saw a marked improvement in our sector with market rents increasing, vacancy dropping and property valuations improving. We have now extinguished all of our US Dollar liabilities and asset secured debt is currently a Rouble/Euro mix, reducing our foreign exchange balance sheet risk. If favourable terms for Rouble secured facilities continue then we will further reduce our exposure to Euro financing in the current year.

As we stated in last year's Risk Report, we intended to continue with our acquisition driven growth strategy in the current year but instead have been distracted by some unforeseen developments.

The most significant risk we were presented with in 2019 was a significant overhang in our ordinary shares as firstly WIM and then latterly, IAML, two of our largest shareholders, faced liquidity issues. We diverted funds we had earmarked for property acquisitions to purchase WIM's ordinary shares in August 2019 and subsequently contracted to purchase IAML's. We have secured a credit committee approved financing line for the IAML transaction.

However, we now have the Coronavirus situation and the subsequent oil price collapse. Given the uncertainty surrounding the potential impact this may have on our business we have temporarily reduced our risk appetite. The immediate effect of this is a decision to maintain our current liquidity levels and postpone the IAML share buy back until we have a better understanding of the fall out, if any, from the crisis. Already we have seen a fall in oil prices precipitating a weakening of the Rouble. In a worst case scenario, this could lead to a suspension of investment decisions by our tenants, a disruption in supply chains impacting on the demand for new warehouse space and potential defaults by existing tenants whose businesses are affected most. However, given the experience the business had in 2015 and 2016 following the last oil price collapse we have adapted our balance sheet to reduce the impact of market shocks such as this and we believe we are in a significantly stronger position than we were during that period.

For now though, other than the Rouble weakening, we are not seeing any impact on our operations but we will proceed with caution.

The principal risk factors that follow reflect our opinion of how they have changed in 2019 and how the oil price volatility may impact on our business. The impact of Coronavirus on our local market is as yet unknown.

We are also cognisant of our responsibility for our impact on the environment and sustainability. We are looking at a number of potential projects at the moment. These range from introducing greater energy efficiency in our buildings as part of our rolling capital expenditure programme, through managing international travel with greater use of VCU technology and carbon offsets to the assessment of the impact of building a solar panel farm and the introduction of bee hives at one of our regional asset sites.

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, including new and emerging risks, 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.

Our Cypriot holding company board has been working with our other jurisdictions reviewing and codifying the group's internal control infrastructure and has overseen the first year of our internal audit function. 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. The Risk Committee has met four times during the year and reports are also reviewed by the Audit Committee. The Cypriot Board have reported to the Audit Committee on progress made with their internal control procedures with and without the internal auditors in attendance.

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 2019
Oil and Gas dependent economy V Oil price volatility leads to a weakening of the Rouble.	The weak Rouble increases the cost of servicing Euro debt and puts pressure on banking covenants. A low oil price dampens infrastructure spending which leads to a drop in consumer demand. This in turn impairs demand for warehouse space and a contraction in demand from existing tenants.	As the majority of our financing is Rouble denominated our banking covenants are less sensitive to the servicing of the Euro element of our debt. The amortisation profile of our facilities is weighted towards the Euro element of the facility to reduce the foreign exchange risk over the term of the loans. With little or no speculative development in the market and low vacancy levels research indicates that the warehouse sector should be resilient in the short to medium term.	→
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 including extinguishing all US Dollar liabilities. However, the risk of increased sanctions remains.	→

Financial Risk

Risk	Impact	Mitigation	Change in 2019
Foreign Exchange V At the year end 42% of secured debt was denominated in Euros and all of our preference shares in Sterling.	A weakening of the Rouble against those foreign currencies reduces our ability to service debt and preference share coupons and reduces our profitability.	We have significantly reduced our exposure to foreign currency secured debt facilities and will continue to do so. As noted above, bank covenants are now less sensitive to the servicing of the Euro element of facilities. The improvement in our secured debt foreign exchange risk benefits the servicing of our preference shares as the overall foreign exchange risk of subordinated debt reduces. However, the recent weakening of the Rouble does increase this risk in the current year.	↓
Interest rates V Increases in Central Bank rates and financing benchmarks.	The cost of debt increases and Group profitability and debt service cover reduce.	We are operating in a low or reducing interest rate environment for Euro and Rouble facilities. Our variable cost of debt is hedged with the use of caps with terms matching the debt maturity profile.	→
Share Buy Backs V We have purchased 16.5% of our ordinary shares in the year and contracted to purchase a further 28.5% in the current year.	We reduce our equity base and increase group gearing.	The overhang of ordinary shares has been impeding share performance and the acquisitions are NAV per share enhancing. Our gearing levels are more an indicator of low asset valuations. The increase in values over the past 12 months partly compensates for the impact of last year's buy backs on our gearing levels.	**NEW**

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Property Investment

Risk	Impact	Mitigation	Change in 2019
Acquisitions V 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 advisors 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 given the lack of available space.	
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 rolling five year capital expenditure programme to maintain our properties at a Grade A level. These works should protect and potentially enhance levels of rent achievable.	

Russian Domestic Risk

Risk	Impact	Mitigation	Change in 2019
Legal Framework The legal framework in Russia continues to develop, with new and proposed laws regularly being introduced.	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 2019
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 where available; 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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