

RISK & RISK MANAGEMENT

As a leading building supplies manufacturer in a highly competitive international environment, Kingspan is exposed to a variety of risks and uncertainties which are monitored and controlled by the Group's internal risk management framework.

Overall responsibility for risk management lies with the Board who ensures that risk awareness is set at an appropriate level. To ensure that risk awareness is set at an appropriate level, the Audit Committee assists the Board by taking delegated responsibility for the risk identification and assessment in addition to reviewing the Group's risk management and internal control systems and making recommendations to the Board thereon.

The chairman of the Audit Committee reports to the Board at each Board meeting on its activities, both in regard to audit matters and risk management. The activities of the

Audit Committee are set out in detail in the Report of the Audit Committee on page 73.

The Board monitors the Group's risk management systems through this consultation with the Audit Committee but also through the Group's divisional monthly management meetings, where at least two executive directors are present. The risks and trends are the focus of each division's monthly management meeting, where their performance is also assessed against budget, forecast and prior year. In addition, key performance indicators are used to benchmark operational performance for all manufacturing sites.

In addition to this ongoing assessment of risk within the divisions, the Audit Committee oversees an annual risk assessment for the Group whereby each divisional management team is formally asked to prepare a risk assessment for their businesses. This assessment involves evaluating group-wide risks, as put forward by the Board, and also presenting additional risks that are specific to their business.

While it is acknowledged that the Group faces a variety of risks, the Board, through the processes set out above, has identified the principal risks and uncertainties that could potentially impact upon the Group's short to medium term strategic goals and these are as follows:

Risk and impact	Actions to mitigate
<p>Volatility in the macro environment</p> <p>Kingspan products are targeted at both the residential and non-residential (including retail, commercial, public sector and high rise offices) construction sectors. As a result, demand is dependent on activity levels which may vary by geographic market and is subject to the usual drivers of construction activity (i.e. general economic conditions and volatility, events such as the UK's EU Referendum, political uncertainty in some regions, interest rates, business/consumer confidence levels, unemployment and population growth).</p> <p>While construction markets are inherently cyclical, changing building and environmental regulations continue to act as an underlying positive structural trend for demand for many of the Group's products.</p>	<p>The exposure to the cyclical nature of any one construction market is partially mitigated by the Group's diversification, both geographically and by product.</p> <p>As set out in the Business Model & Strategy, the Group has mitigated this risk through diversification as follows:</p> <ul style="list-style-type: none"> > Sales outside of traditional markets, predominantly the UK and Ireland, have increased from 26% in 2006 to 69% in 2016; > Launch of new products and continual improvements to existing product lines; and > Acquisitions made during the year extend the geographic reach of the Group. <p>The full details of these diversifications are set out in the Business Model & Strategy on pages 8 to 15.</p>

Risk and impact	Actions to mitigate
<p>Failure to innovate</p> <p>Failing to successfully manage and compete with new product innovations, changing market trends and consumer tastes could have an adverse effect on Kingspan's market share, the future growth of the business and the margins achieved on the existing product line.</p>	<p>Innovation is one of Kingspan's four pillars to increasing shareholder value and therefore plays a key role within the Group.</p> <p>There is a continual review of each division's product portfolios at both the executive and local management level to ensure that they target current and future opportunities for profitable growth.</p> <p>This risk is further mitigated by continuing innovation and compelling marketing programmes. Kingspan also has a deep understanding of changing consumer and industry dynamics in its key markets, enabling management to respond appropriately to issues which may impact business performance.</p>
<p>Product failure</p> <p>A key risk to Kingspan's business is the potential for functional failure of our product which could lead to health, safety and security issues for both our people and our customers.</p> <p>The Kingspan brand is well established and is a key element of the Group's overall marketing and positioning strategy. In the event of a product failure, the Kingspan brand and/or reputation could be damaged and if so, this could lead to a loss of market share.</p>	<p>Dedicated structures and processes are in place to manage and monitor product quality controls throughout the business:</p> <ul style="list-style-type: none"> > The majority of new products go through a certification process which is undertaken by a recognised and reputable authority (for example, in the UK it is the Building Research Establishment, BRE) before it is brought to market. > Our businesses employ quality control specialists and operate strict policies to ensure consistently high standards are maintained in relation to the sourcing and handling of raw materials. > Quality audits are undertaken at our manufacturing sites. > Documented and tested product recall procedures are embedded in all our businesses and regularly reviewed. > Effective training is delivered to our staff. > We proactively monitor the regulatory and legislative environment.
<p>Business interruption (including IT continuity)</p> <p>Kingspan's performance is dependent on the availability and quality of its physical infrastructure, its raw material supply chain and its information technology. The safe and continued operation of such systems and infrastructure is threatened by natural and man-made perils and is affected by the level of investment available to improve them.</p> <p>Any significant or prolonged restriction to its physical infrastructure, the necessary raw materials or its IT systems and infrastructure could have an adverse effect on Kingspan's business performance.</p>	<p>Kingspan insists on industry leading operational processes and procedures to ensure effective management of each facility. The Group invests significantly in a rigorous programme of preventative maintenance on all key manufacturing lines to mitigate the risk of production line stoppages.</p> <p>The impact of production line stoppages is also mitigated by having business continuity plans in place to allow for the transfer of significant volume from any one of our 58 plants in the Insulated Panels division or 19 plants in the Insulation Boards division to another in the event of a shutdown.</p> <p>In addition and as part of our consequential loss insurance, Kingspan is subject to regular reviews of all manufacturing sites by external risk management experts, with these reviews being aimed at improving Kingspan's risk profile.</p> <p>In an effort to reduce Kingspan's exposure to raw material supply chain issues, Kingspan builds strong relationships with a wide range of raw material suppliers to limit the reliance on any one supplier or even a small number of suppliers.</p> <p>Kingspan's IT infrastructure is constantly reviewed and updated to meet the needs of the Group. Procedures have been established for the protection of this infrastructure and all other IT related assets. These include the development of IT specific business continuity plans, IT disaster recovery plans and back-up delivery systems, to reduce business disruption in the event of a major technology failure.</p>
<p>Credit risks and credit control</p> <p>As part of the overall service package, Kingspan provides credit to customers and as a result there is an associated risk that the customer may not be able to pay outstanding balances.</p> <p>At the year-end, the Group was carrying a receivables book of €546m expressed net of provision for default in payment. This represents a net risk of 18% of sales. Of these net receivables approximately 73% were covered by credit insurance or other forms of collateral such as letter of credit and bank guarantees.</p>	<p>Each business unit has established procedures and credit control functions around managing its receivables and takes action when necessary.</p> <p>Trade receivables are primarily managed through strong credit control functions backed up by credit insurance to the extent that it is available. All major outstanding and overdue balances together with significant potential exposures are reviewed regularly and concerns are discussed at monthly meetings at which the Group's executive directors are present.</p> <p>Control systems are in place to ensure that credit authorisation requests are supported with appropriate and sufficient documentation and are approved at appropriate levels in the organisation.</p>
<p>Employee development & retention</p> <p>The success of Kingspan is built upon effective management teams committed to achieving a superior performance in each division. Failure to attract, retain or develop these teams could have an impact on business performance.</p>	<p>Kingspan, and each of its divisions, is committed to ensuring that the necessary procedures are in place to attract, develop and retain the skill levels needed to achieve the Group's strategic goals. These procedures include strong recruitment processes, succession planning, remuneration reviews, including both long and short term incentive plans, and career development plans.</p>
<p>Fraud and cybercrime</p> <p>Kingspan is potentially exposed to fraudulent activity, with particular focus on the Group's online banking systems, online payment procedures and unauthorised access to internal systems.</p>	<p>The security processes around the Group's IT and banking systems are subject to review by divisional management and internal audit. These systems are continually reviewed with updates and improvements implemented as required. Relevant IT and security policy documents and related alerts are circulated by Group management to all divisions to ensure a consistent and effective approach is taken across the Group.</p>
<p>Acquisition and integration of new businesses</p> <p>Acquisitive growth is an important element of Kingspan's development strategy. A failure to execute and properly integrate significant acquisitions and capitalise on the potential synergies they bring may adversely affect the Group.</p>	<p>All potential acquisitions are rigorously assessed and evaluated, both internally and by external advisors, to ensure any potential acquisition meets Kingspan's strategic and financial criteria.</p> <p>This process is underpinned by extensive integration procedures and the close monitoring of performance post acquisition by both divisional and Group management.</p> <p>Kingspan also has a strong track record of successfully integrating acquisitions and therefore management have extensive knowledge in this area which it utilises for each acquisition.</p>