

Risk Overview

Enterprise Risk Management

The Group operates in the food industry and is exposed to a variety of risks and uncertainties. The Group's Enterprise Risk Management framework is designed to identify, assess and mitigate key risks by taking appropriate measures to ensure the achievement of the Group's strategic objectives.

Overall responsibility for establishing, reviewing and adapting the company-wide governance, risk management, compliance and control processes lies with the Board of Directors (the Board). The Board has delegated responsibility for evaluating the Group's governance, risk and control environment to the Audit, Finance, Risk, Quality & Compliance Committee (the AFRQCC).

Implementation and execution of the risk management processes are delegated by the Board to the Executive Committee (the ExCo) and further cascaded to regional and functional management.

The Group Risk Management function facilitates the enterprise risk assessment process for identifying and understanding the Group's key risks, allocating ownership

to drive specific actions and taking the relevant measures to address them. Group Risk Management presents the key risks to the ExCo and the AFRQCC on an annual basis. Regional and functional management ensures that risks are managed appropriately, that measures and controls are operating effectively and that the additional mitigation actions are implemented as deemed appropriate. Ongoing monitoring of the Group's key risks and its respective risk management activities are embedded in regular management review meetings or in dedicated committees. The AFRQCC meets as often as the business requires, at least three times per fiscal year, in order to deal with any significant issues reported by Management, Assurance functions (including Group Risk Management, Compliance and Internal Audit) or external authorities and regulators.

While it is acknowledged that the Group faces many risks, the Board has identified the key risks that could potentially impact the achievement of the Group's strategic objectives. These are outlined in the table below.

Key Risks

Environmental, Social and Governance (ESG)

Risk Description

The Group's strategic and operational business objectives and associated performance frameworks are linked to a complex, highly interconnected and continuously evolving global ESG landscape. Factors such as the effects of climate change, carbon emissions, deforestation, human rights abuse, business ethics, diversity and inclusion, equality and stakeholder impact represent a wide source of drivers that can lead to opportunity and risk in the pursuit of business objectives and the creation of stakeholder value. Further ESG-related transition risk factors include uncertainties in relation to stakeholder expectations (civil society, customers, investors, NGOs, regulators and suppliers) associated with social and environmental accountability towards governance, strategy, opportunity & risk management, metrics and reporting. Furthermore this encompasses continued uncertainty over the adequate operational implementation of various recent and emerging ESG regulations such as end to end supply chain traceability and due diligence. Uncertainty on enforcement practices by relevant competent authorities could expose the Group to supply chain disruptions and litigation and negatively impact the Group's commercial position and reputation.

Mitigation/Measures

The Group has a long-standing commitment to sustainability. The Group identifies material ESG topics according to the double materiality assessment principles and outlines in detail its plan to make sustainable chocolate the norm in its Forever Chocolate Progress Report, which is published on an annual basis. Key elements of the Group's sustainability strategy and performance are described in more detail in the Sustainability section of the Annual Report and the annual Forever Chocolate Progress Report. The Group is committed to continuously improve and implement ESG specific oversight structures, agile resilience and adaptation measures, robust supply chain traceability and due diligence processes and effective reporting frameworks. A dedicated ESG task force is employed to oversee, coordinate and align all relevant ESG activities in order to achieve those objectives. The aforementioned principles are also actively promoted in the Group's dealings with suppliers and customers and are as far as possible, imposed through the Group's contractual relationships with these stakeholders. Further stakeholder assurance is obtained through external ratings and audits. The Group publicly discloses sustainability performance, policies, programs, actions, and metrics to the needs of its stakeholders. The Group's progress is reflected in several renowned ESG performance benchmarks and assessments. Dedicated teams are proactively monitoring the evolving regulatory landscape to ensure the Group complies with emerging regulatory requirements as they develop.

Risk Overview

Key Risks

Long-term sustainable supply of cocoa and other agricultural raw materials

Risk Description

The Group is dependent on a sustainable supply of quality cocoa beans and other agricultural raw materials so that it can produce high-quality cocoa and chocolate products. ESG risk factors such as declining productivity attributable to poor agricultural practices, nutrient-depleted soils and aging cocoa trees, waning interest from the next generation in becoming cocoa farmers, child labor in supply chains, a shift in the cultivation preferences of farmers from cocoa and other raw material cultivations to alternative, more attractive crops, and the long-term impacts of deforestation and climate change could lead to a shortfall in high-quality cocoa beans and other essential agricultural raw materials in the mid- to long-term.

Mitigation/Measures

Under the umbrella of its overall sustainability strategy Forever Chocolate, the Group focuses and reports on four pillars to make sustainable chocolate the norm: Prospering farmers, human rights, thriving nature and sustainable ingredients. Long-term measures also include the continuous evaluation and diversification of supply sources in origin countries, developing improved agricultural practices for cocoa farms and maintaining an industry dialogue with key stakeholders in origin and consumer countries. The Group's sustainability strategy and framework is described in more detail in the Sustainability section of the Annual Report and the annual Forever Chocolate Progress Report.

Rapidly shifting consumer trends

Rapidly shifting consumer trends may disrupt market and industry dynamics, which could impact the future growth of the Group's business.

Trend analysis by the Group's marketing and customer insight teams, together with cross-functional commercial and operational teams working closely with customers, aim to identify trends in the marketplace, both positive and negative, at an early stage. The Group constantly invests in data analytics, R&D and operational capabilities as part of a well-structured process, enabling the Group to develop new products, capabilities and distribution channels which proactively address evolving trends and changing demand patterns.

Business transformation

Timely initiation and successful execution of business transformation initiatives are critical to pursue strategic objectives, avoid disruption, improve agility and adapt to changing market conditions. Ineffective project portfolio management and implementation, insufficient due diligence, inaccurate business plan assumptions or inadequate post-merger integration processes can all have negative consequences. Investing in technology that is no longer competitive or becomes obsolete soon may further impact the successful execution of business transformation. These factors can result in an underperforming business, reduced synergies, or higher costs than expected.

All major business transformation projects are prioritized and monitored by the Business Transformation and Strategy Team which is handpicked by the Group's ExCo. The Group deploys dedicated teams with significant experience and capability for their respective business transformation projects. These teams proactively follow market, technology and other trends and work in close collaboration with functional and regional experts, external advisors, and the Group's ExCo. A clearly defined process for the evaluation, execution and integration of major business transformations is employed. The performance of major transformational projects and acquisitions are periodically reviewed against their goals. A similar process is employed for the execution of major acquisitions and divestitures.

External political and economic environment

Uncertain political and economic conditions (including spillover effects induced by epidemics or pandemics, geopolitical or geoeconomic conflicts or climate change related events or conditions) could result in reduced demand for chocolate and cocoa products or affect the Group's operations, supply chain and cost structure. This may affect the Group's expansion plans, profitability and financial position.

The Group has a presence in both developed and emerging markets with a well-diversified business and operations portfolio in different market, product and customer segments. Through its global operation and innovation networks, the Group is able to rapidly respond to customer requests and provide flexible, optimized recipes to adapt to changing market conditions. The Group regularly monitors the political and economic situation and developments globally and specifically in regions with higher uncertainty in order to prepare for various scenarios which may arise. The Group's capability to respond to temporary supply and demand shocks as well as structural shifts associated with a changing political or economic environment is assured by an agile organization and a well-governed issue management and strategy execution process.

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Mitigation/Measures

Long-term outsourcing agreements

The Group has entered into a number of important long-term outsourcing agreements with customers. Failure to renew, early termination of existing long-term outsourcing agreements, failure to enter into new agreements or failure to negotiate terms that are attractive could have a material impact on the result of operations.

The Group has a highly diversified global customer base representing a healthy mix of small, medium and large customers. For global strategic customers, the Group has established long-term outsourcing agreements governing mutual cooperation, addressing standards for quality, quantity commitments, pricing, service levels, innovation and ethics. For these customers, the Group has appointed dedicated teams that develop and maintain a close relationship in order to respond to customer needs professionally and promptly and to provide high-quality services that are mutually beneficial for all stakeholders concerned. These teams have expertise in customer relationships, service and innovation, as well as in commercial and pricing matters.

Talent and workforce management

Failure to attract, retain and develop a talented workforce with the right capabilities and skills could impact the Group's ability to achieve its strategic objectives. Tight and competitive labor markets (accelerated by shifting skill requirements, new ways of working and demographic shifts or other factors) could lead to a shortage of skilled labor or talent in selected regions and functions. Sustained shortages and increased turnover rates could further impact the Group's costs and operational reliability.

Every effort is made to nurture a diverse and inclusive work environment that is supported with optimal processes and policies to attract, select, develop, reward and retain talent with the right capabilities and skills needed to achieve the Group's strategic objectives. The Group employs succession planning, talent reviews, remuneration benchmarking, long- and short-term incentive plans, training and leadership development programs, as well as the tools to support and measure the success of all these processes. The Group's strategy for Diversity & Inclusion is described in more detail in the "Our People" section of this Annual Report. Further, the Group continuously invests in business process technology and automation to make work more productive, collaborative and rewarding for its employees.

Quality & food safety

Products not meeting quality and food safety standards expose the Group to business interruption, litigation, product liability and recall claims. This could also negatively impact the Group's reputation and may lead to a loss of revenue and market share. There is also a risk that raw materials are accidentally or maliciously contaminated throughout the supply chain. Furthermore, other product defects may occur due to human error, equipment failure or other factors.

The Group's quality management programs and systems consist of clear cross functional accountabilities, robust standards, guidelines and procedures. The Group's comprehensive quality program is being improved continuously and comprises areas such as supplier strategy & requirements, factory design, testing processes. In addition, a quality and food safety culture program, embraced by the Group's Executive Committee, is in effect across the entire Group to ensure all employees of the Group maintain a zero-defect mindset. A well-governed issue management process is regularly reviewed, updated and simulated to ensure adequate and timely reaction in the event of a food safety incident.

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Mitigation/Measures

Operations and supply chain

The Group's operations and supply chain network could be disrupted by incidents at manufacturing sites, adverse weather conditions, climate change, disease (human or crop), natural disasters, political instability, sabotage and other factors which could impact the ability to produce and deliver products to customers.

The Group's operations and supply chain department operates a well-diversified and flexible manufacturing network that is governed by a well structured and coordinated global, regional and local sales and operations planning process. Furthermore, a well-structured issue management process is in place to manage recovery and business continuity of operations should the situation require it in times of distress. The global sourcing departments are continuously monitoring weather, harvest, political risk and other indicators to proactively anticipate potential supply shortages or interruptions of raw materials, machinery, equipment, indirect materials, logistics or other services. Short-term mitigation measures include adequate levels of safety stocks and a diversified regional supply network. Long-term adaptation and resilience measures include strategic reviews of the Group's operation and supply chain footprint.

Information and operations technology

The Group's business processes and its interaction with customers, suppliers and employees working remotely are highly dependent on reliable and secure information and operations systems. Cyberattacks on our business-critical information and operations technology assets, environmental or physical damage to global data centers, a global wide area network breakdown or any other significant security incident could lead to a loss of availability or integrity of business critical technology assets resulting in a business interruption, loss of confidential data, direct losses of financial resources and non-compliance with data protection laws or other regulatory frameworks. Major cyber incidents may also negatively impact the Group's reputation and lead to loss of revenue and market share.

The Group's information management and technology department and the Group's operations and supply chain department have implemented robust end to end cyber security risk management frameworks. To ensure a holistic approach to cybersecurity, those frameworks establish a clear cyber risk management governance and strategy including the involvement of senior management and business stakeholders. Various preventive structures for the Group's business-critical applications and locations including various technical solutions and regular internal awareness campaigns as well as training on cybersecurity for all employees and selected contractors are in place and being improved continuously. In the event of a major event, incident response and disaster recovery solutions, plans and procedures are in place and continuously enhanced. A mid-term plan to enhance information and operations technology security is regularly defined, and improvements are being implemented continuously.

Risk Overview

Key Risks

Price volatility of raw materials and other input factors

Risk Description

Market prices for raw materials, energy and other input factors, as well as the structure of the terminal markets could have an influence on the Group's liquidity and operational results. To manage its exposure to these factors, the Group uses derivative financial instruments and forward physical commitments. Liquidity and operating results may be affected by ineffective hedging strategies or by positions taken. Furthermore, the Group's profitability can be affected by its exposure to the volatility of the combined cocoa ratio, which expresses the combined sales prices for cocoa butter and cocoa powder in relation to the cocoa bean price.

Mitigation/Measures

The Group's commodity risk management policies require that all risk exposures are hedged back-to-back in accordance with the related limit framework from the moment such exposures are entered into. For its contract business, namely the Food Manufacturers Product Group, which accounts for the majority of the business, the Group mitigates the impact of volatility in prices of raw material and other input factors through a cost-plus pricing model. Raw material price exposures arising at contract signing are hedged in accordance with the commodity risk management limit framework, price exposures to other input cost factors are managed through index based pricing mechanisms. In the Gourmet & Specialties Product Group, the Group applies a price list model whereby forecasted sales are hedged and price lists are adapted on a regular basis. Adherence to the limit framework is regularly monitored by experts on local, regional as well as on group level. In the Cocoa Product Group, the Group attempts to mitigate the effects of the volatility of the combined ratio by means of a central management system which monitors the positions and exposures related to cocoa products globally, taking into account both internal and external demand. The Group's financial risk management framework related to commodities, foreign currencies, interest rates and liquidity is described in more detail in note 3.7 to the Consolidated Financial Statements.

Treasury

The Group's operations are exposed to foreign currency, interest rate, liquidity and credit risks. Volatility in raw material prices and supply chain requirements affect the Group's working capital requirements and cash flows and could result in liquidity issues. Failure to deliver on key parameters including cash flow could result in a downgrade of the Group's credit rating and restrict its access to financial markets.

The Group has established a robust financial risk management framework and governance structure. The Group's treasury policy requires that all foreign currency exposures in a floating currency regime as well as interest rate risk exposures are hedged in accordance with the related limit framework from the moment such exposures are entered into. The Group's liquidity is ensured by means of regular Group-wide monitoring and planning of liquidity coordinated by the Group's centralized treasury department. Financing needs are covered through a combination of adequate credit lines with reputable financial institutions and short- and long-term debt capital market products. The Group's financial risk management framework related to financing and liquidity is described in more detail in note 3.7 to the Consolidated Financial Statements.

Legal, regulatory and compliance

The Group is subject to both international and national laws, regulations and standards in such diverse areas as product safety, product labeling, environment, health and safety, employment and human rights, supply chain traceability & supplier due diligence, intellectual property rights, antitrust, anti-bribery and corruption, employment and human rights, trade sanctions, data privacy, supply chain traceability & supplier due diligence, corporate transactions and taxes in the countries in which it operates, as well as stock-exchange-listing and disclosure regulations in a constantly changing regulatory environment. Failure to comply with applicable laws and regulations could expose the Group to investigations, litigation, administrative and/or criminal proceedings potentially leading to significant costs, fines and/or criminal sanctions against the Group and/or its directors, officers and employees with possible reputational damage.

Dedicated regional and local functional managers, supported by specialized corporate functions and external advisors, ensure compliance with applicable laws and regulations. The Group has robust policies, processes and controls in place in the relevant areas. The Group's legal & compliance department oversees the Group's compliance program, which ensures awareness of the compliance risks and the Group's compliance standards. The Code of Conduct, the Supplier Code and other Group policies set out the legal and ethical standards of behavior expected from all employees and selected stakeholders.