

## Principal Risks and Uncertainties

# Risk MANAGEMENT

**Risk management is the responsibility of the Board and is a key factor in delivering the Group's strategic objectives.**

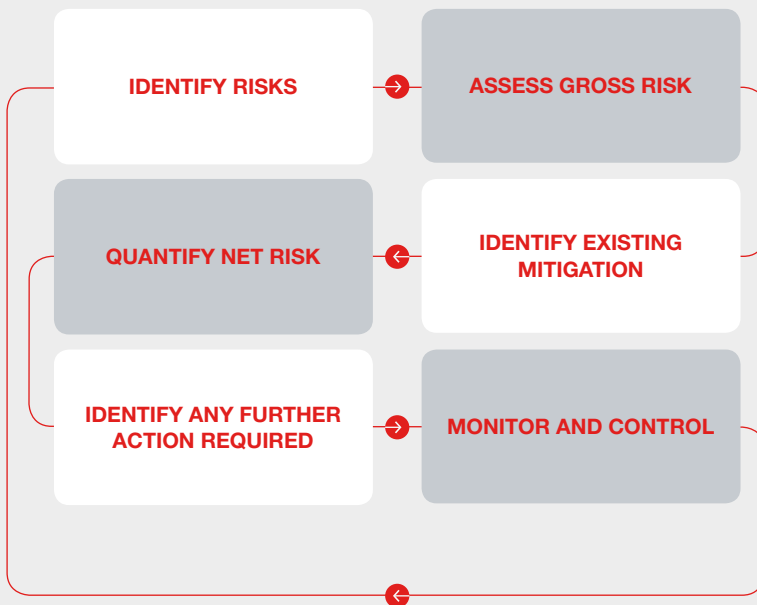
### Approach to Risk Management

The Board is responsible for setting the risk appetite, establishing a culture of effective risk management and for ensuring that effective systems and controls are in place and maintained.

Senior managers take ownership of specific risks and implement policies and procedures to mitigate exposure to those risks.

### Risk Management Process

The risk management process sits alongside our strong governance culture and effective internal controls to provide assurance to the Board that risks are being appropriately identified and managed.



### How we manage risk

Risk is managed across the Group in the following ways:

- The Board meets annually to review strategy and set the risk appetite.
- Risks faced by the Group are identified during the formulation of the annual business plan and budget process, which sets objectives and agrees initiatives to achieve the Group's goals, taking account of the risk appetite set by the Board.
- Senior management and risk owners consider the root cause of each risk and assess the impact and likelihood of it materialising. The analysis is documented in a risk register, which identifies the level of severity and probability, ownership and mitigation measures, as well as any proposed further actions (and timescale for completion) for each significant risk.
- The Group has an executive Risk Management Committee, chaired by the Chief Financial Officer. This Committee meets on a regular basis. The status of the most significant risks and mitigations are reviewed at each meeting, with other risks reviewed on a cyclical basis.
- The Executive Directors also meet with senior managers on a regular basis throughout the year. This allows the Executive Directors to ensure that they maintain visibility over the material aspects of strategic, financial and other risks.
- The Group's Audit and Risk Committee assists the Board in assessing and monitoring risk management across the Group. The role of the Committee includes ensuring the timely identification and robust management of inherent and emerging risks, by reviewing the suitability and effectiveness of risk management processes and controls. The Committee also reviews the risk register to ensure net risk and proposed further actions are together consistent with the risk appetite set by the Board.
- See also Impact of COVID-19 on page 58.



### Principal risks

Each of the principal risks set out below includes an assessment of the impact of COVID-19 where appropriate (and therefore COVID is not included as a separate risk).

- |  |   |
|--|---|
| 01 Macroeconomic conditions                    | 09 Warehousing and distribution capacity constraints                          |
| 02 Cyber security                              | 10 Unplanned plant downtime   |
| 03 Regulatory risks, including health & safety | 11 Ability to attract and retain key personnel and highly skilled individuals |
| 04 Raw material supply                         | 12 Shortages or increased costs of appropriately skilled labour               |
| 05 Raw material and traded goods pricing       | 13 Failure to develop new products  |
| 06 Customer credit risk                        | 14 Competitor activity  |
| 07 Sustainability                              | 15 Failure to identify, complete and integrate bolt-on acquisitions           |
| 08 Manufacturing capacity constraints          | 16 Digital and IT system development  |

### Internal control

The Group has well-defined systems of internal control.

The Group has a robust process of financial planning and monitoring, which incorporates Board approval of operating and capital expenditure budgets. Performance against the budget is subsequently monitored and reported to the Board on a monthly basis. The Board also monitors overall performance against operating, safety and other targets set at the start of the year.

Performance is reported formally to shareholders through the publication of results both annually and half-yearly. Operational management regularly reports on performance to the Executive Directors.

Day-to-day operations are supported by a clear schedule of authority limits that define processes and procedures for approving material decisions. This ensures that projects and transactions are approved at the appropriate level of management, with the largest and most complex projects being approved by the Board. The schedule of authority limits is reviewed on a regular basis so that it matches the needs of the business.

The Group also has processes in place for ensuring business continuity and emergency planning.

In order to further enhance the internal control and risk management processes, KPMG provides an outsourced internal audit service to the Group. KPMG work closely with the Risk Management Committee in delivering the Group's internal audit programme.

## Principal Risks and Uncertainties continued

### Impact of COVID-19

As described in the Corporate Governance Statement on page 66, in response to the COVID-19 pandemic, the Board increased its activity with respect to the Company, in order to support the Executive team and properly discharge its governance responsibilities. Since the onset of the first lockdown, more regular and frequent virtual Board update meetings have been held, on a weekly basis at certain times, to consider emerging risks, discuss financial and operational matters and monitor performance against revised targets.



In addition, with the Group's finance and administrative teams working substantially from home during the period, controls

related to the processing of cash payments and receipts were enhanced during lockdown periods (e.g. higher levels of approval required for transactions over certain limits). More generally, the Group's IT team have remained particularly vigilant and alive to cyber risks during this period and we continue to invest in our cyber security.

In conclusion, with the assistance of the Audit and Risk Committee, the Board has reviewed the effectiveness of the system of internal control, taking into account the impact of COVID-19. Following its review, the Board determined that it was not aware of any significant deficiency or material weakness in the system of internal control.

### Risk profile

The principal risks monitored by the Board are as follows:

Principal Risk and Impact	Strategic Priorities	Mitigation	Risk Change in Reporting Period	Movement
<p><b>MACROECONOMIC CONDITIONS</b> Our products are used in the residential and commercial building and construction markets, both within the RMI sector, for new residential housing developments and for new construction projects.</p> <p>Our private RMI business is strongly correlated to the level of household disposable incomes. Our new-build business is particularly influenced by the level of activity in the house-building industry.</p> <p>As such, our business and ability to fund ongoing operations is dependent on the level of activity and market demand in these sectors, itself often a function of general economic conditions (including interest rates and inflation) in the UK.</p> <p>Government economic and social policy can also have a significant impact on our business.</p>		<ul style="list-style-type: none"> <li>Notwithstanding macro conditions, we expect our strategic priorities and self-help initiatives to support sales and profit growth and drive good cash conversion.</li> <li>Initiatives include: growing market share, expanding the branch network, delivering sustained operational excellence and increasing recycling.</li> <li>Actions taken in response to the COVID-19 pandemic have secured our financial position.</li> <li>We operate comfortably within the terms of our bank facility and related financial covenants.</li> </ul>	<ul style="list-style-type: none"> <li>The UK economy is experiencing a severe downturn due to the ongoing impact of the COVID-19 pandemic.</li> <li>Now that key aspects of the UK's trading relationship with the EU have been defined, and the first two months of 2021 have passed without significant interruption to raw material imports for our business, Brexit related uncertainty has reduced. The medium-term impact of Brexit on the UK economy remains unclear.</li> <li>CPA now forecast the private housing RMI market to grow 14% in 2021 (after a 14% decline in 2020).</li> <li>The UK is also experiencing high levels of mortgage approvals.</li> <li>UK base rate is at its lowest ever level.</li> </ul>	▲
<p><b>CYBER SECURITY</b> A breach of IT security (externally or internally) could result in an inability to operate systems effectively (e.g. viruses) or the release of inappropriate information (e.g. hackers).</p>		<ul style="list-style-type: none"> <li>Ongoing investment in cyber risk detection and prevention tools.</li> <li>Physical security of servers at third-party off-site data centre, with full disaster recovery capability.</li> <li>Password and safe-use policies in place, internet usage monitored and anti-malware used.</li> <li>External cyber review and internal audit reviews conducted periodically, resulting in significant enhancements in defence.</li> <li>Cyber awareness/IT security campaign active for all employees.</li> <li>Enhanced monitoring and vigilance in response to increased remote working in 2020.</li> <li>Financial crime protection and cyber liability insurance in place.</li> </ul>	<ul style="list-style-type: none"> <li>Increased home working in response to the COVID-19 pandemic has elevated cyber risk.</li> <li>This remains a high-profile area and continues to receive considerable management attention.</li> </ul>	▲

**Movement key:****Strategic Priorities key:**

Target growth in market share



Develop innovative new products



Explore potential bolt-on acquisition opportunities



Deliver sustained operational excellence



Expand our branch network



Develop the sustainability of our business, products and operations



Develop a market-leading digital proposition

Principal Risk and Impact	Strategic Priorities	Mitigation	Risk Change in Reporting Period	Movement
<p><b>REGULATORY RISKS, INCLUDING HEALTH &amp; SAFETY</b></p> <p>We may be adversely affected by the crystallisation of unexpected corporate or regulatory risks.</p> <p>These include health &amp; safety, data, reputational and environmental risks (including regulations related to our recycling operations), or other legal, taxation and compliance matters.</p>		<ul style="list-style-type: none"> <li>Procedures and policies in place to support compliance with all relevant regulations.</li> <li>Regular communication and training on policy compliance.</li> <li>Monitoring procedures in place, including near miss and potential hazard reporting for health &amp; safety matters.</li> <li>Introduction of a range of COVID-safe protection measures, in line with recommended guidance and designed and implemented collaboratively with input from the workforce.</li> <li>Employees returning to work post H1 2020 shut-down provided with training and personal protective equipment where necessary.</li> <li>Internal and third-party site audits to test compliance with our policies.</li> </ul>	<ul style="list-style-type: none"> <li>COVID-19 has significantly increased health &amp; safety risks.</li> <li>More generally, recent developments widen the scope and increase the penalty regime for breaches in these areas. For example: Corporate Criminal Offence of Failure to Prevent the Facilitation of Tax Evasion ('CCO') legislation came into force on 30 September 2017, and General Data Protection Regulations ('GDPR') came into effect in May 2018.</li> </ul>	▲
<p><b>RAW MATERIAL SUPPLY</b></p> <p>There are only a limited number of PVC resin and certain other raw material suppliers and we operate with limited raw material storage capacity.</p> <p>The recycling feedstock supply market is fragmented and can be unpredictable.</p> <p>Failure to receive raw materials on a timely basis could impact on our ability to manufacture products and meet customer demand.</p>	 	<ul style="list-style-type: none"> <li>We generally operate with at least two suppliers for all critical raw materials, including PVC resin, to support security of supply.</li> <li>On-going raw material tests to identify potential alternative suppliers.</li> <li>A spot market exists for resin, that we are able to access at certain times.</li> <li>Contractual arrangements for certain key suppliers include liquidated damages for failure to supply.</li> <li>Regular reviews to test financial stability of key suppliers.</li> <li>Potential remains for increased resin supply originating from the US to come on line and deliver into Europe.</li> </ul>	<ul style="list-style-type: none"> <li>A number of European PVC resin suppliers issued force majeure notices on material supply in H2 2020, following plant outages and other operational issues.</li> <li>Strong demand for PVC resin exacerbated supply constraints in H2 2020.</li> <li>Knock-on effect into recycling feedstock supply market also tightening in 2020.</li> <li>The PVC resin supply market remains tight at the beginning of 2021, which is also impacting pricing (see below).</li> </ul>	▲
<p><b>RAW MATERIAL AND TRADED GOODS PRICES</b></p> <p>Our manufacturing operations depend on the supply of PVC resin, a material derivative of ethylene which in turn is a derivative of crude oil.</p> <p>The price of PVC resin can therefore be subject to fluctuations based on the markets for crude oil and ethylene, as well as the market for resin itself.</p> <p>In addition, although we pay for resin in sterling, crude oil and ethylene are priced in US dollars and euros respectively. As such, the price of resin in sterling is also impacted by international currency markets.</p> <p>Our ability to pass on resin and other raw material or traded goods price increases to our customers will depend on market conditions at the time.</p>		<ul style="list-style-type: none"> <li>We generally operate with at least two suppliers for all critical raw materials and traded goods, including PVC resin, to provide competitive pricing.</li> <li>Where possible we pass through raw material or traded goods price increases to our customers.</li> <li>Increasing the use of recycled material in our manufacturing partially mitigates exposure to resin prices, although prices for recycling feedstock can also be volatile.</li> <li>We consider fixed price supply arrangements with suppliers where it is economic to do so.</li> </ul>	<ul style="list-style-type: none"> <li>Raw material prices fluctuated throughout 2020, primarily due to the impact of COVID-19 on the relevant markets.</li> <li>Supply-side constraints resulted in increasing prices for PVC resin and recycling feedstock in H2 2020, continuing on into 2021.</li> <li>We have elected not to enter into a fixed price contract for PVC resin so far in 2021, as the premium currently required by suppliers is prohibitive.</li> </ul>	◀▶

## Principal Risks and Uncertainties continued

Principal Risk and Impact	Strategic Priorities	Mitigation	Risk Change in Reporting Period	Movement
<p><b>CUSTOMER CREDIT RISK</b> Default by a large customer or multiple smaller customers could result in a material bad debt(s). The loss of a major customer(s) could limit our ability to continue to grow the business.</p>		<ul style="list-style-type: none"> <li>Regular process for in-depth credit reviews for existing and new customer accounts.</li> <li>Following onset of COVID-19 pandemic and first lockdown, increased frequency of credit reviews and greater involvement of relevant Executive Committee members in managing position on key accounts.</li> <li>Significant increase in bad debt provisions recorded in H1. Year end provisions remain at a similar level, reflecting continued prudent assessment of bad debt risk.</li> <li>Credit insurance in place to the extent available for selected large accounts.</li> </ul>	<ul style="list-style-type: none"> <li>Increased bad debt risk due to the impact of COVID-19 on our customer base, with some business failures and a deterioration in the age profile of receivables during the first lockdown in H1.</li> <li>Some improvement in bad debt experience and age profile of receivables in H2, although significant uncertainty remains.</li> </ul>	▲
<p><b>SUSTAINABILITY</b> Demonstrating improving business sustainability is becoming increasingly important to all stakeholders.  We have a strong underlying position, driven by our expanding window recycling operation. We intend to widen this narrative into a Group-wide sustainability strategy, which will encompass all aspects of business sustainability.  Failure to do so could lead to regulatory challenges (e.g. if sustainability regulation is tightened) and potentially reduced access to capital and difficulties with recruitment and retention.</p>		<ul style="list-style-type: none"> <li>Strong underlying position driven by window recycling operation, which drives significant carbon savings compared to the use of virgin PVC resin.</li> <li>Publication of verified carbon savings data in the 2020 annual report.</li> <li>Work in progress to define and implement a Group-wide sustainability strategy, with long-term goals linked to relevant UN Sustainable Development Goals and the UK Government's transition towards a net zero carbon economy.</li> </ul>	<ul style="list-style-type: none"> <li>Continued rise in importance of sustainability for all stakeholders.</li> </ul>	▲
<p><b>MANUFACTURING CAPACITY CONSTRAINTS</b> Demand running above our manufacturing capacity may result in production related inefficiencies, as well as customer service issues if a backlog of customer orders develops.  A shortage of capacity may also prevent the acquisition of new customers, thereby limiting our ability to continue to grow the business.</p>		<ul style="list-style-type: none"> <li>Investment in 2019 to increase co-extrusion and foam capacity by 30% and 15% respectively.</li> <li>Strengthened management team in critical areas, including Chief Operating Officer (joined Q3 2019). Team ensured peak periods in H2 2020 were navigated successfully.</li> <li>COO has an improvement plan with c.100 actions targeting productivity gains in extrusion, foiling, warehousing and distribution.</li> <li>New warehouse facility (see below) is a catalyst to free up space in the existing footprint to future-proof extrusion capacity.</li> </ul>	<ul style="list-style-type: none"> <li>Customer demand in H2 2020 increased to such an extent that the business was running close to existing manufacturing capacity.</li> <li>Competitor weakness has resulted in a clear opportunity to acquire new customers.</li> <li>Investment in new extrusion capacity planned for 2021.</li> </ul>	▲
<p><b>WAREHOUSING AND DISTRIBUTION CAPACITY CONSTRAINTS</b> We exceeded the capacity of our existing warehouse in 2018/19, resulting in significant inefficiencies and additional labour and distribution costs.  A new central warehouse and distribution centre was approved early in 2020, which will deliver &gt; 50% increase in capacity, improved efficiency and a safer operation.  On-time execution of the fit-out project and successful operation from the new site are critical to unlocking future growth potential and the delivery of anticipated improvements in operating efficiencies.</p>		<ul style="list-style-type: none"> <li>Strengthened management team in critical areas, including Chief Operating Officer and Head of Supply Chain (joined Q3 2019). Team ensured peak periods in H2 2020 were navigated successfully from existing facilities.</li> <li>COO has an improvement plan with c.100 actions targeting productivity gains in extrusion, foiling, warehousing and distribution.</li> <li>Fully resourced team hired to deliver new warehouse fit-out, including project management and technical expertise, supported by third party subject matter specialists.</li> </ul>	<ul style="list-style-type: none"> <li>Despite strong customer demand in H2 2020, and existing capacity constraints, measures taken (including extra labour and temporary overflow site) to ensure safe and successful operation from the existing warehouse.</li> <li>Fit-out of the new warehouse continued safely throughout 2020, despite COVID-related constraints, with the new site becoming operational early in 2021.</li> <li>Transition to continue in 2021, with the final stages expected to complete in Q2.</li> </ul>	▲

**Movement key:**

▲ Increase    ◀ No change    ▼ Decrease

**Strategic Priorities key:**

Target growth in market share



Develop innovative new products



Explore potential bolt-on acquisition opportunities



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Principal Risk and Impact	Strategic Priorities	Mitigation	Risk Change in Reporting Period	Movement
<p><b>UNPLANNED PLANT DOWNTIME</b></p> <p>The business is dependent on the continued and uninterrupted performance of our production facilities.</p> <p>Each of the facilities is subject to operating risks, such as: industrial accidents (including fire); extended power outages; withdrawal of permits and licences (e.g. the regulated operation of the recycling facility); breakdowns in machinery; equipment or information systems; prolonged maintenance activity; strikes or other extended workforce absences; natural disasters; and other unforeseen events.</p>	 	<ul style="list-style-type: none"> <li>Regular planned maintenance to reduce the risk of plant failure, including maintenance capital investment of &gt;£5 million per annum across the Group.</li> <li>Extrusion facilities spread over three manufacturing sites.</li> <li>Recycling facilities spread over two sites.</li> <li>Group-wide disaster recovery plans in place.</li> <li>Introduction of a range of COVID-safe protection measures, in line with recommended guidance and designed and implemented collaboratively with input from the workforce.</li> <li>Employees returning to work post H1 2021 shut-down provided with training and personal protective equipment where necessary.</li> </ul>	<ul style="list-style-type: none"> <li>Potential for COVID-19 to spread amongst the workforce and result in significant and extended absence.</li> </ul>	▲
<p><b>ABILITY TO ATTRACT AND RETAIN KEY PERSONNEL AND HIGHLY SKILLED INDIVIDUALS</b></p> <p>Our success depends inter alia, on the efforts and abilities of certain key personnel and our ability to attract and retain such people, with the appropriate skills and experience.</p>	 	<ul style="list-style-type: none"> <li>Developing successful track record and clear strategic direction provides an attractive backdrop to joining the senior team at Eurocell.</li> <li>Market rate compensation for all personnel, including leadership team.</li> <li>Equity-based long-term incentive plans in place for senior team.</li> <li>People plan includes focus on improving employee engagement and communication.</li> </ul>	<ul style="list-style-type: none"> <li>Guaranteed long-term incentive plan awards issued to senior team in 2020 (excluding Executive Directors) to help mitigate impact of COVID-19 on existing in-flight schemes.</li> <li>Progressive implementation of people plan.</li> </ul>	◀
<p><b>SHORTAGES OR INCREASED COSTS OF APPROPRIATELY SKILLED LABOUR</b></p> <p>We are subject to supply risks related to the availability and cost of labour, both in our manufacturing operations and in our branch business. Our headquarters and several manufacturing and operational sites are located in areas of generally full employment.</p> <p>We may also experience labour cost increases (including those related to the Minimum Wage) or disruptions in circumstances where we have to compete for employees with the necessary skills and experience in tight labour markets.</p>	 	<ul style="list-style-type: none"> <li>Market level or better salaries and good benefits package.</li> <li>Induction and training programme.</li> <li>Annual SAYE share-save scheme available to all personnel.</li> <li>Use of fixed-term contracts to secure sufficient labour through H2 2020 without longer-term commitment, due to inherent levels of uncertainty.</li> <li>People plan includes focus on improving employee engagement and communication.</li> </ul>	<ul style="list-style-type: none"> <li>Sufficient labour secured in H2 2020 via fixed-term contract initiative.</li> <li>Fifth SAYE scheme planned for 2021.</li> <li>Progressive implementation of people plan.</li> </ul>	◀
<p><b>FAILURE TO DEVELOP NEW PRODUCTS</b></p> <p>Failure to innovate could reduce our growth potential or render existing products obsolete.</p> <p>The launch of new products and new variants of existing products is an inherently uncertain process. We cannot guarantee that we will continuously develop successful new products or new variants of existing products.</p> <p>Nor can we predict how customers and end-users will react to new products or how successful our competitors will be in developing products which are more attractive than ours.</p>	 	<ul style="list-style-type: none"> <li>We invest continuously in research and development through our in-house team.</li> <li>The team is highly focused on new ways to develop existing products and to be innovative with new ones.</li> <li>We work closely with customers and technical advisers on product development.</li> <li>We have a strong product pipeline with more than 25 projects in development.</li> </ul>	<ul style="list-style-type: none"> <li>Recent successes for Profiles include: introduction of a flush window sash for the Logik product range, a new sliding patio door system (Syncro) and development of a through-colour grey substrate profile.</li> <li>In Building Plastics, the Equinox conservatory roof system has been developed to include a skylight (Vega) and our new suite of outdoor living products, including the Kyube garden room, has been very well received.</li> </ul>	◀

## Principal Risks and Uncertainties continued

Principal Risk and Impact	Strategic Priorities	Mitigation	Risk Change in Reporting Period	Movement
<p><b>COMPETITOR ACTIVITY</b></p> <p>We have a number of existing competitors who compete on range, price, quality and service. Increased competition could reduce volumes and margins on manufactured and traded products.</p>		<ul style="list-style-type: none"> <li>• Strong market and customer awareness, with good intelligence around competitor activity.</li> <li>• Absolute focus on customer proposition and points of differentiation in product and service offering.</li> <li>• We have developed a strong new customer pipeline.</li> </ul>	<ul style="list-style-type: none"> <li>• During the first lockdown period in H1 2020, the business prepared well for re-opening, from both an operational and commercial perspective. These activities supported further gains in market share delivered in H2 2020.</li> <li>• The more uncertain market environment may have weakened some of our competitors.</li> </ul>	
<p><b>FAILURE TO IDENTIFY, COMPLETE AND INTEGRATE ACQUISITIONS</b></p> <p>We may not be able to identify and complete appropriate bolt-on acquisitions (one of our strategic priorities).</p> <p>Any future acquisition we do make poses integration risks which may affect our results or operations.</p> <p>The acquisition and integration of companies is a complex, costly and time-consuming process involving a number of possible risks. These include diversion of management attention, failure to retain personnel, failure to maintain customer service levels, disruption to relationships with various third parties, system risks and unanticipated liabilities.</p>		<ul style="list-style-type: none"> <li>• Public communication of bolt-on acquisitions being a strategic priority.</li> <li>• Good knowledge of companies operating in our sector and related sectors.</li> <li>• Six acquisitions completed since our IPO in 2015.</li> <li>• Tried and tested procedure for the integration of new acquisitions and a good track record of recent success.</li> </ul>	<ul style="list-style-type: none"> <li>• Whilst we continue to assess and consider acquisition opportunities, our focus in 2020 and 2021 is delivering operational efficiencies from recent investments in manufacturing and warehousing capacity.</li> <li>• Previously reported delays with the project to expand Eurocell Recycle North (acquired in 2018) further impacted by H1 2020 shut-down. Performance is now improving towards delivering acceptable operational and financial performance.</li> </ul>	
<p><b>DIGITAL AND IT SYSTEMS DEVELOPMENT</b></p> <p>We have introduced a new strategic priority to develop a sector-leading digital proposition.</p> <p>Stakeholders in most organisations increasingly require full end-to-end digital solutions; a trend exacerbated by the COVID pandemic.</p> <p>Failure to develop a leading digital proposition could lead to a competitive disadvantage, hinder progression of our other priorities and detract from the supplier, customer and employee experience of working with Eurocell.</p>		<ul style="list-style-type: none"> <li>• Strengthened IT function with recruitment of New Director of IT with strong sector and digital experience (joined March 2020).</li> <li>• Developed three-year IT road map, including significant investment in additional resources and application landscape to support development of business efficiency and digital proposition.</li> </ul>	<ul style="list-style-type: none"> <li>• Increasing importance of digital for stakeholders.</li> </ul>	