

Operational risk management

Alliance UniChem applies effective risk management in identifying opportunities and preparing strategies for the efficient operation and continued development of the Group against a background of complex, regulated and competitive markets.

Our risk management strategy aims to provide sound assurance for management on the effectiveness of our control framework. The Group's approach to this comes from the active management, rather than elimination, of risk. Our aim is to ensure that we understand risks before taking decisions to enable balanced choices and to allow opportunities to be pursued and objectives met with confidence.

Business risk factors

In the day to day operation of our businesses and the development of the Group, both in existing and new markets, we face risks and uncertainties, a number of which are unique to the business sectors in which we operate. The risk factors addressed below are those which we believe could adversely affect us, potentially impacting the operations, revenue, profits, cash flow or assets of the Group. Additional risks and uncertainties currently unknown to us, or which we currently deem to be immaterial, may also have an adverse effect on the Group. We use our risk management process to identify, monitor, evaluate and escalate such issues as they emerge, enabling the Board to take appropriate action wherever possible in order to control them.

The factors listed below should be considered in connection with any forward looking statements in this report.

The Group operates in regulated environments and therefore may be adversely impacted by regulatory reviews aimed at reducing government's costs

As a pharmaceutical wholesaler and operator of retail pharmacies, we are subject to legislation in our markets covering: certain minimum service levels and product ranges; the conditions under which these products must be stored, distributed and dispensed; the safeguards we must operate to ensure integrity of the supply chain and to protect patients receiving prescriptions; and the reimbursement permissible or provided for our wholesale and retail businesses. Changes to existing legislation or other regulations and the introduction of new legislation or other regulations may affect our operations. Regulatory changes driven by political or economic pressures, particularly those relating to the sourcing of medicines or pricing, have the potential to impact our performance through pressures on revenue, gross margins or costs. Any changes in current approaches to licensing either through enhanced restrictions on wholesalers or a reduction in service levels required within the industry which may lead to enhanced competition, may affect our operations. In addition, changes to the licensing regimes for pharmacies, or restrictions on reimbursement controls for state funded pharmacies, may affect the operations and profitability of our pharmacies and, through their impact on the wider community of pharmacies, have a consequent impact on our wholesale businesses.

As a leading industry player in many of the countries in which we operate, we are able to contribute constructively and effectively to consultation on the development of regulation in those markets. We are fully cognizant that

regulation is a constant feature of the markets within which we operate. When regulatory changes take place we react swiftly. This can mean varying our market propositions (such as adjusting prices and discounts) where necessary in order to mitigate the adverse effects of any such changes. We also seek to take advantage of any opportunities that regulatory changes may afford.

The markets within which the Group operates are highly competitive and are subject to change

The Group operates in highly competitive markets which, notwithstanding their regulated nature, are subject to competition from direct competition and alternative supply sources, including importers (parallel trade), domestic opportunistic traders and manufacturers who supply product direct to pharmacies or patients. These can result in adverse pressure on pricing or discounts to customers and, within a regulated commercial environment, can sometimes produce unexpected consequences and subject us to changes in market structure, such as the potential risk of disintermediation. It is possible that suppliers, customers and payors could change their operational models in a way that could adversely affect the Group's operations. The Group monitors service offerings and counters these risks by ensuring that its offering to its customers is competitive and backed by excellent customer service. The broad portfolio of businesses with their geographic and commercial diversity, coupled with high service and efficiency levels across the Group, provide both a defence from new market entrants and a sound platform from which to benefit from any opportunities that developments in our markets may offer.

Acquisitions in existing and new geographical markets and related business areas have inherent risk

The Group's strategy for continued growth includes acquiring businesses and associate interests to complement our existing business portfolio. Failure to identify, conduct appropriate due diligence and appropriately integrate acquisitions, particularly in new geographical markets, could have an adverse impact on the Group's competitive position, growth prospects and business operational financial performance. Exploitation of our particular in-house corporate development expertise in this area enables the Group to make acquisitions which consistently create shareholder value while avoiding unsuitable markets and businesses.

The Group has a potential exposure to the consequences of the supply of defective products or negligence and breach of contract claims arising from failure to provide services properly

Whilst the Group does not undertake any product manufacturing (all its own brand products being manufactured by third party manufacturers), potential financial or reputational consequences could result from risks regarding the infiltration of counterfeit products into the supply chain, the re-labelling of certain products or by contamination or mishandling issues. The Group maintains a robust framework of operational and professional pharmacy controls to prevent such product-related incidents. In addition, pharmacy product risk exposure is limited as the Group only maintains relationships with licensed manufacturers of medicines who would legally carry primary responsibility for any product defect.

The Group is also exposed to risks arising through professional or process error in its pharmacies and in the professional services it provides. Robust operational and pharmaceutical controls are managed by a team of senior pharmacists and supported by ongoing training for every pharmacist or dispenser. These processes are subject to proactive review and assurance activity and are designed to mitigate the likelihood of material damage to the Group from product and service risks.

The occurrence of major operational problems could have an adverse effect on the performance of the Group

In common with other businesses, Alliance UniChem depends on its process and control framework to mitigate the possibility of a major failure in operations, information technology, finance, human resources or other key business processes capable of having an impact on its performance. These failures may be caused by internal factors, such as a major information technology systems failure, a stock handling procedure breakdown or failure to retain key personnel. They could also be driven by external events, such as the failure of third party suppliers, terrorism or natural disasters such as epidemics, pandemics and other major events which impact us as well as the communities we serve. The Group continues to develop and strengthen its coordinated risk management and assurance mechanisms to manage these risks in a manner which it believes ensures an appropriate and effective control framework for its businesses at a local, national and corporate level.

A major health, safety or environmental incident could harm our employees or people in the communities we serve and expose the Group to reputational damage, litigation and adversely impact our operational and financial performance

The Group takes its corporate responsibilities in the field of health, safety and the environment very seriously and fully recognises the potential human, reputational and financial consequences of these risks. In managing risks relating to the health and safety of its employees, protection of the public and the environment and the storage and handling of hazardous substances and waste products, the Group relies for control on group-wide environmental, health and safety standards, which meet or exceed the regulatory requirements in all the countries in which we operate. Compliance with these standards and with changes to the regulatory environment are monitored and reviewed to give assurance that our controls continue to protect our people and the communities that we serve and to ensure that the Group can demonstrate to appropriate authorities responsible management and compliance with regulation in these areas.

Other risk factors

The Board considers that Alliance UniChem is also subject to other conventional commercial and financial risks which are common to most international groups. These include the management of customer credit and trade receivables and those risks specified in the Financial Review section of the Operational and Financial Review, including interest rate and currency risk management. These risks are reviewed and managed through the Group's business performance and risk management processes.