Risk management process and key risk categories

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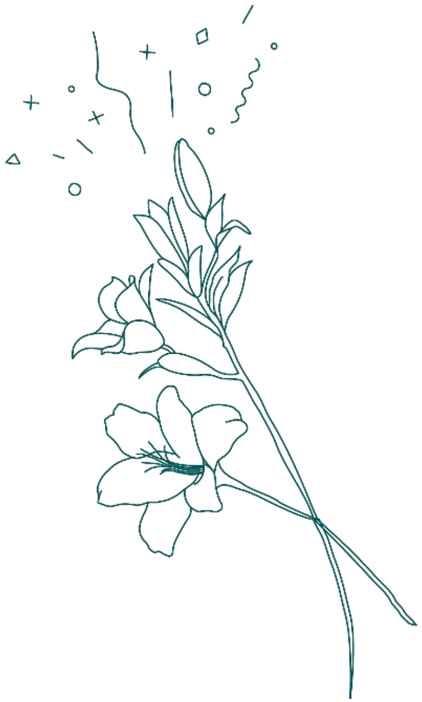

Risk management process and key risk categories

CapMan faces many different risks and uncertainties, which could if realised affect its strategic direction, financial position, earnings, operations and reputation. Assessment and management of risks is an integral part of CapMan's ability to conduct its operations in a successful manner. CapMan classifies risks in various risk categories and identifies principal risks for each category. CapMan performs an annual review of the risk environment and reports on any material developments quarterly.

Risk management strategy and process

Risk management constitutes a significant part of CapMan's corporate governance. Risk needs to be managed rather than avoided and consideration of risk should not stifle innovation. Rather, consideration of risk should enable CapMan to make better decisions.
As the risk definition includes both positive and negative effects of uncertainty on company objectives, harnessing opportunities, as compared to only managing threats, should be considered as part of risk management. The Board of Directors decides on the risk appetite and risk tolerance with the target to ensure continuity of operations and to optimise CapMan's ability to meet its objectives The Chief Operating Officer, supported by the independent Risk & Valuation team, has day-to-day responsibility for the implementation and continuous development of the risk management process.

Risk management objectives

Risk management at CapMan aims to

- Set the risk appetite and tolerance in accordance with CapMan's strategy;
- identify and assess key risk factors in CapMan's operations and business environment; and
- manage these risk factors to allow CapMan to achieve its strategic and financial objectives.

Further risk management objectives

- Ensure the safety and wellbeing of employees;
- ensure the continuity of business operations;
- increase risk awareness throughout the organisation;
- protect the reputation of CapMan, its personnel and investors;
- effectively allocate resources for risk treatment; and
- identify opportunities.

Key risk categories

CapMan categorises its risks and identifies the following principal risks for each category:

Risk category	Principal risks
1. Strategic risk	• Failure to achieve strategic or performance targets • Failure to select the correct strategy in a competitive environment • Failure to recruit and retain key personnel • Failure to scale the business
2. Financial risk	• Poor financial performance • Insufficient liquidity position • Failure to obtain financing
3. Market risks	• Interest and foreign exchange rate, inflation and asset price volatility • Changes in customer preferences • Fluctuations of the transaction market • Failure in fundraising
4. Operational risks	• Cyber threats and system errors • Inadequate or failed processes or controls • Corruption, fraud or criminal behaviour • Mistakes
5. Regulatory risks	• Adverse changes in the regulatory environment
6. Sustainability risk	• Failure to invest in sustainable assets and ESG related incidents or lack of appropriate ESG approach in portfolio companies • Unreasonable increase in costs to comply with sustainability and reporting requirements
7. Reputational risk	• Negative public perception

The drivers of principal risks under each risk category are further described below.

1. Strategic risk

Strategic risks occur when, for internal or external reasons, the company is unable to achieve its strategic targets, or the chosen strategy proves incorrect or ineffective. Strategic risk management at CapMan is a part of the overall Group strategy development. For example, strategic risks are considered when evaluating which businesses, investment Strategies or funds are pursued, what kinds of investors or clients are targeted with different products and services, how concentrated the customer base is, or how to ensure business continuity. Moreover, as CapMan's success is based on skilled and motivated personnel, who may be difficult to replace or recruit, a people strategy together with continuous succession planning are a key part of strategic risk management. CapMan aims to have a diversified portfolio of businesses with entrepreneurial teams and a diversified customer base. Strategic risks and targets are continuously monitored by senior management and Board of Directors.

2. Financial risk

Financial risk refers to risks impacting the financial position and/or performance of the company. CapMan's turnover is to a large extent based on long-term agreements and therefore risk levels are relatively low in the short term. Similarly, the majority of the cost base is fixed in the short term. Therefore, the biggest drivers for financial risk for CapMan are returns of fund investments as well as the timing and magnitude of carried interest, both of which have significant exposure to market risk as well as the performance of individual funds and portfolio assets. Monitoring and managing these underlying risks is a key activity of all investment teams. The risks are also monitored by the Risk & Valuations team on a continuous basis. Another key financial risk for CapMan is Group liquidity and financing, as CapMan typically has sizeable off-balance sheet liabilities relating to the commitments made to funds.

Financial risks are actively managed by continuous follow-up of the liquidity position and cash flow forecasts and by maintaining sufficient liquidity buffers relative to open commitments.

CapMan has long term financial objectives, including targets for growth, return on equity and equity ratio, which are continuously monitored and regularly reported to senior management and Board of Directors. CapMan also has a revolving credit facility to ensure its ability to cover unexpected cash requirements. The company targets a long maturity profile for debts by actively managing its credit portfolio in order to secure long-term debt financing at attractive terms also in the future.

3. Market risk

Market risk refers to the risk of losses arising from movements in market prices, or the risk that the market or customer behaviour changes in a way that makes CapMan's business model or product/service offering sub-optimal. CapMan is exposed to significant market risk both due to its significant investments in funds, as well as due to its reliance on the international fundraising market in raising capital for its funds under management. Market risk may also impact the timing and magnitude of carried interest by causing delay or value impairment of exits from the funds. Market risk is part of operating in the finance industry and can be only partially mitigated.

CapMan aims to have a diversified portfolio of businesses and investment strategies, covering multiple asset classes and geographies. CapMan has also strategically improved its earnings mix by launching different types of funds and also services less dependent on the financial markets. Investments to funds and the diversification as well as income from different business areas are monitored as part of executing CapMan's strategy and each time new investments are decided.

4. Operational risk

Operational risk refers to the risk of loss resulting from inadequate or failed internal processes or systems, human error or from external events. For CapMan, the most important operational risks relate to cyber and IT systems, compliance with often complex regulations and agreements, fraud, corruption or other criminal behaviour, and mistakes or human error. CapMan has continuous process to monitor and manage operational incidents and risks. Issues are actively managed and there are controls in place to mitigate risk for the most critical functions. CapMan implements Anti-Money Laundering (AML) policies and procedures designed to prevent and detect money laundering, bribery and corruption and related activities. The activities involve KYC (Know Your Customer) procedures on fund investors and portfolio companies. These topics are covered by regular trainings for employees. CapMan works together with reputable insurance brokers to ensure reasonable insurance coverage for potential liability that might result from any material conventional operative incidents.

5. Regulatory risk

Regulatory risk refers to the risk of adverse changes in the regulatory environment including unexpected changes in legal practice and changes made by the government or a regulatory body in international or local taxation and tax conventions between countries in which CapMan has operations. This may increase the costs of operating a business or reduce the attractiveness of operating in each country or tax regime.

Fund and wealth management are regulated industries and CapMan has subsidiaries that are regulated under AIFMD or MiFID regimes. There are also several other laws and regulations that may impact CapMan's operations or strategy. CapMan has a dedicated Compliance function, supported by Risk & Valuation, Legal & Compliance and Sustainability teams, to monitor regulatory changes and changes in political environment as well as market environment and societal discussion in co-operation with external advisors. In fund and investment structuring, CapMan also uses advisors to ensure up-to-date understanding of the latest regulations, including concerning taxation. Decisions relating to tax matters are driven by business considerations, and CapMan considers stakeholder opinion, reputational risk, commercial, financial, legal, and regulatory factors alongside tax legislation. CapMan does not practice aggressive tax planning.

The most significant ongoing regulatory developments that impact the finance industry in Europe are related to sustainability. CapMan continues to monitor and adapt to sustainability-related and other regulation that impacts the industry.

6. Sustainability risk

Sustainability risk refers to environmental, social or governance events or conditions that, if they occur, could cause a material negative financial impact or reputational harm, or negatively impact the environment or the people involved in CapMan's operations or portfolio companies, and/or other stakeholders.

CapMan own direct sustainability risk is limited, and mainly related to its own operations such as the use of renewable energy, employees' travel habits, being an attractive, diverse, and equitable workplace, and maintaining high business ethics and integrity by complying with laws and regulations and acting in a responsible manner in line with CapMan's values.

The most significant sustainability risk for CapMan is, however, indirect through the investment activities in the Real Estate, Infrastructure and Private Equity funds managed by CapMan, and through the investments made from CapMan's own balance sheet. To manage investment-related sustainability risk, CapMan works to ensure that each of its investment strategies operates in a sustainable way and makes investments that are in themselves sustainable, can be transitioned towards more sustainable practices and are not at risk of becoming obsolete or stranded. Moreover, it is important to ensure that the investment process always follows CapMan's Sustainable Investment Policy, that relevant pre-investment checks are completed properly and that ESG Due Diligence guidelines are followed for each investment. CapMan has implemented a restriction list to restrict or exclude certain investment activities or industries from the investment scope. CapMan guides its portfolio companies' sustainability work through Active Ownership. All our eligible Private Equity and Infrastructure assets will establish SBT validated emission reduction targets by 2032, and we have set a target to achieve emission reductions in our real-estate portfolio compared to 2021.

CapMan is also committed to multiple sustainability reporting initiatives and internal guidelines and processes in place, for example a Codes of Conduct both for CapMan and our suppliers and internal Sustainability and Diversity, Equity and Inclusion working groups as well as a Sustainability Academy to educate CapMan's employees and other stakeholders about sustainability issues, to make its sustainability actions more transparent and to mitigate sustainability risks. CapMan educates its portfolio companies' management and personnel about ESG matters and has onboarding process where ESG related processes and principles are implemented on Portfolio Company level.

7. Reputational risk

Reputational risk is the risk of negative publicity, poor public perception or uncontrollable events to have an adverse impact on CapMan's reputation, thereby affecting its ability to meet strategic or financial objectives or reducing shareholder value. Reputational risk is a core risk for CapMan, since the business mainly relies on mutual trust between business parties. Realisation of reputational risk could impact fundraising and deal flow as well as the ability to attract and retain key employees, all of which have substantial impact on CapMan's performance. CapMan aims to build an ethical culture and has identified high ethics as one of its values. CapMan has a Code of Conduct and other policies in place to guide its employees beyond being compliant with laws and regulations. CapMan also has controls, such as a Whistleblowing Channel, in place and aims to maintain a continuous dialogue with relevant stakeholders.