

Risk Management

Kardan's business strategy inherently comprises risks

Kardan is inherently exposed to a relatively high degree of entrepreneurial, geopolitical, financial and legal risks in the markets in which its subsidiaries operate. The Kardan Group operates primarily in emerging and developing countries, such as China and Angola, which, by nature, have a different risk profile than developed markets. Kardan has two outstanding series of Debentures – which were issued in 2007 and 2008 by Kardan and are listed on the Tel Aviv Stock Exchange. In the past years, the repayment of these Debentures puts a heavy burden on the financial position of the Company, and as of February 2018 the Company is unable to meet the repayment obligations. Kardan is therefore in discussions with the debenture holders on concluding a debt settlement and repaying its liabilities. This entails generating cash by means of selling assets or attracting partners in projects whilst simultaneously continuing to focus on further improving our subsidiaries' results and therefore value. The Company sold its holdings in AVIS Ukraine in the first quarter of 2019. Furthermore, the Company is working hard to strengthen the financial position of Tahal through a capital increase. For more details, including on the progress of the negotiations with the debenture holders regarding a debt settlement, please refer to the Kardan Group's Business Strategy chapter.

Our risk management approach

Taking risks is an integral part of doing business and can create opportunities which in turn can lead to positive results. We therefore deem it important to have a proper 'risk culture' throughout the Kardan Group, entailing that all employees share a joint responsibility in being risk aware and acting accordingly. Likewise, we believe that management should lead the way through example.

Risk management is, clearly, an integral part of our daily management responsibility. In order to ensure

adequate knowledge and understanding of our local business environments, and thus to minimize risks, our management teams in all the markets in which we are active consist of local and international members.

We have a transparent and structured management information system in place, based on periodic management reports submitted and presented by the subsidiaries to enable sound analysis and decisions. Kardan is listed on both Euronext Amsterdam and the Tel Aviv Stock Exchange. Our governance structures are therefore solid and, given our dual listing, we are obliged to publicly report on the quarterly results of the Group. As a result, Executive Management discusses strategic, operational and budgetary issues with the management and boards of our subsidiaries at least on a quarterly basis.

Our risk management framework and processes

Our risk management framework was originally based on the principles of the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and has since been updated to incorporate the updates to the COSO frameworks, lastly the COSO ERM Framework (2017). Our risk management process incorporates the principles of the Dutch Corporate Governance Code to secure alignment with best practices while remaining fit for purpose for Kardan. The Code links 'long-term focus on value creation' and 'risk management reinforcement' and emphasizes the importance of reporting thereof. This also echoes closely what the update of the COSO ERM framework is highlighting around a more strategic approach to risk management.

We consider our risk management framework and approach to constitute a link between strategy, policy-making and operational execution and to be instrumental in obtaining a clear view on our business environment and the challenges we face, and accordingly to provide us with reasonable assurance

that we have sufficient and appropriate control measures in place to support the Group in achieving its objectives.

The Board holds at least one formal budget meeting per year, when the objectives of Kardan, and consequently the strategy and business development of its subsidiaries, are discussed at length. Furthermore, this topic is a recurring item on the agenda of Board meetings during the year. Given the debt situation of Kardan, the Board has emphasized that the repayment of its Debentures is Kardan's prime objective. This has accordingly been discussed by the Executive Management with the managers of the subsidiaries in order for them to take this into consideration in their budgets and strategic plans. Furthermore, the Board and the Executive Management require the subsidiaries to identify business and operational risk factors and the relating control measures they have taken and implemented. After approval of the subsidiaries' budgets and strategic plans, the Executive Management prepares the final budget and strategic plan for the Board. This includes Kardan's main risk categories and the relating control measures as determined during an annual risk assessment session which is conducted by the Executive Management. Afterwards, the Executive Management may decide to integrate some of the identified risk categories and controls in ongoing management information systems. Furthermore, after the first half of the year, the Executive Management provides the Board with an update on risks throughout the Group in general and on certain identified risks and their controls specifically.

Kardan has engaged an external advisory firm to provide internal audit services. In 2017 this advisor prepared an internal audit plan for a period of three years. In 2018 two internal audits were performed. The main one relates to fraud risk assessment; no significant shortcomings were detected. The second audit relates to Kardan's Internal Enforcement Plan (an internal compliance program according to Israeli Securities Authority guidelines), which provided useful

insights. In 2019 we have started implementing the internal enforcement plan. This plan entails a review of existing policies and adopting revised/new policies, in relation to reporting to security authorities, insider trading policy etc., and providing training to employees. In addition, in 2019, an internal audit on the functioning of the holding's legal department was performed resulting in a satisfactory outcome.

Besides complying with Dutch Securities Law regulations, Kardan also complies with Israel's Securities Law regulations relating to the effectiveness of internal control over financial reporting and disclosure (Israeli SOX). During 2019 all steps have been taken to be able to provide a declaration regarding the effectiveness of the internal control as referred to previously. Based upon the work performed, the CEO and the CFO of Kardan N.V. have made a statement in the Israeli Annual Report that as per December 31, 2019 the control over financial reporting and disclosure is effective (the Control Statement) and the Group's external auditors in Israel audit the effectiveness of the above mentioned internal controls over financial reporting and disclosure. On top of this, Kardan's (main) subsidiaries provide Kardan with a representation letter on a yearly basis.

The In-Control Statement by the Board of Kardan, as required by Dutch Securities Law can be found at the end of this chapter.

Main risk categories and measures

During the Executive Management's annual risk management assessment all Kardan's risk categories are assessed on the likelihood of a certain risk occurring, the impact this risk could have on the objectives and results of Kardan and possible additional measures to be taken. As a result of a combination of factors, including risk control measures taken by the Group's management, the changed circumstances in the markets in which we operate and the financial situation of Kardan, the main risk categories are

determined. The composition of the main risks may therefore vary year by year. Overall, Management concluded that the composition of the main risks the Company faces had not changed significantly in 2019. The risk of capital availability, and more specifically the risk of not being able to timely repay the debt, materialized in February 2018. This has been a key priority for Executive Management and the Board of Kardan throughout the year. Also, the risks in subsidiaries have been discussed during the risk assessment: on the one hand the improved financial performance of Galleria Dalian, which relieves some risk categories such as financial markets and capital availability of Kardan Land China, and on the other hand the deteriorated financial situation of Tahal which significantly increased the risk of insufficient capital availability for Tahal.

The ten most important risk categories (per type of risk and in alphabetical order) that Kardan currently faces are presented below, as well as the risk appetite, and the related measures in place to control these risks. Also, the impact and likelihood of each risk category is presented. Reference is also made to the financial risks, as described in the 2019 Statutory Financial Statements. We note that there are other risks that were assessed as having a less significant potential impact on the business. In this respect, the Board has decided to put special attention to the Human Resources risk, in particular, in relation to succession plan for key managers in the Group. The Board is of the opinion that given the downsizing of the operations of the Group, there is increased level of dependency on only a few key managers. The Board will continue monitoring this risk closely and will follow-up on its likelihood to materialize while taking necessary steps to mitigate.

Any significant new or changed risk exposure identified during the year is brought to the Executive Board's attention and the risk profile and corresponding control measures are revised as necessary.

Please note that in our view, the risk categories listed below should be seen as general guidance for considering the main risks related to our businesses and strategy. We deem all risk categories, as discussed during our annual risk assessments, to be relevant for our business performance and hence conscientiously monitor all of them.

Strategic Risks

Capital availability

Kardan has a substantial debenture debt at present. In order to finance the interest and capital repayments, the required funds need to be provided by our subsidiaries by means of dividend, as well as through the sale of assets by the subsidiaries or by Kardan. As a result, capital availability – both in terms of equity and debt – is challenging for the Kardan Group as a whole. We are therefore exposed to the risk that insufficient access to capital may threaten our capacity to achieve our objectives, as well as to grow and generate future financial returns. In 2018 this risk has materialized and Kardan was not able to repay its debenture holders as of February 2018. Furthermore, in August 2019, as a consequence of delays in the startup of new projects, provisions on a number of projects and the consequent pressure on liquidity, the need to strengthen the financial position of Tahal through a capital increase became apparent.

Risk Appetite:

Given our debenture debt, cash management is critical to our continuity, meaning that our tolerance in this respect is very low.

Impact: Critical

Likelihood: Certain

Measures:

In order to bring down debt at the level of Kardan, the Company aims to generate cash by, among other things, selling selected assets from our portfolio, taking

into account the maturity of assets and the market conditions. Accordingly, in the past years, Kardan sold some significant assets by which the Company secured its obligations until February 2018. Due to various circumstances, not entirely under the control of the Company, Kardan was unable to complete a sale transaction of Tahal in a manner that enabled Kardan to timely repay its debt in February 2018. Executive Management and the Board are focused on managing the potential impact by negotiating a new debt settlement. In parallel, Executive Management and the Board continue in their efforts to sell assets. In March 2019, the Company sold its investment in AVIS Ukraine. The proceeds from the sale were used for a partial repayment of the debentures in June 2019. In September 2019, the Company approached the debenture holders with a proposal to negotiate new terms of agreement which entail conversion of debt into equity. In parallel, Kardan has been working on advancing a sale transaction of its subsidiary Tahal. In 2019, the financial situation of Tahal has become challenging, which led the Board to conclude that it is important to strengthen the financial position of Tahal through a capital increase. Such capital increase, most likely by bringing a partner into Tahal, will not result in cash inflow to Kardan in order to serve its debt.

.....
This risk is segmented as 'Unique Risk' in the Israeli annual report

Concentration

Our real estate activities are concentrated in China. Our water project activities are spread more globally; mainly in emerging and frontier markets, with some large projects in CEE, India and Africa. At the end of 2016 and during 2017, our water infrastructure company Tahal signed several large-scale projects in Africa, mainly in Angola and Zambia, specifically one large 7-year contract in Angola which doubled Tahal's backlog. During 2018 and 2019 Tahal expanded its activities in India which became the second largest market of Tahal, after Africa. Consequently, the Kardan Group is specifically exposed to these regions and markets, their economic developments and, in some

instances, the extent to which government policy affects the operations of local subsidiaries. The fact that the Kardan Group – in line with our strategy – has business activities across different sectors in different (locations in) emerging markets mitigates the above-mentioned risks to a certain extent. We do note, however, that our real estate activities are characterized by long-term investments and commitments, and as such make us less flexible in adapting our profile at short notice to changing market conditions.

Risk Appetite:

Our portfolio is consciously diversified, both in terms of type of business and geography. We have a medium to high tolerance to concentration risk.

Impact: High

Likelihood: Almost Certain

Measures:

Our real estate activities in China are spread over various Tier 2 cities, all carefully selected and reflecting their growth potential which is generally higher than the country average. Moreover, we are active in both the residential and the commercial retail real estate sector which diversifies our risk further. Our water infrastructure company Tahal aims to attract additional projects worldwide in its identified emerging growth markets, which include EPC projects in the fields of water, agriculture, solid waste, environment and natural gas. The activities are spread over multiple continents. All large projects in Africa are setup with a 50% partnership. In the past few years the company expanded to India, Russia and Ukraine and in 2019 Tahal started operations in Kazakhstan. We closely monitor risks related to the specific markets and segments we operate in and discuss these risks at length in the Board meetings in order to be able to make solidly based decisions.

.....
This risk is segmented as 'Sector Risk' in the Israeli annual report

Customer needs and Competition

The needs of customers are changing as markets and technologies develop. Moreover, a logical consequence of the economic development of emerging markets, is that competition will increase. Given that the sectors in which we are active are characterized by long-term efforts and investments, the flexibility to change our strategic focus or move to other markets is limited.

Risk Appetite:

Our business is characterized by long-term efforts and investments. We have a medium tolerance for impact on our results by changes in customer needs and competition.

Impact: High

Likelihood: Probable

Measures:

Kardan has a communication process in place that ensures that crucial developments are discussed during all Board meetings and between management of the subsidiaries and the Executive Management. Based on regular customer and market surveys and the insights of management of the various subsidiaries (consisting of local and international managers) the choice of location, pace of development, geographical and product diversification and the need for possible strategic changes are discussed and decided upon.

This risk is segmented as 'Sector Risk' in the Israeli annual report

Partnering

In many of its activities the Kardan Group operates with external partners, such as joint venture partners, subcontractors, funding partners etc. Accordingly, we run the risk that ineffective alliance, joint venture, affiliate or other external relationships affect our reputation and our capability to achieve our goals due to for instance choosing the wrong partner, poor

execution of agreements or failing to capitalize on partnering opportunities.

Risk Appetite:

Successful partnerships are key to realizing our strategy. We have low tolerance for any weaknesses in the partner engagement process.

Impact: Medium

Likelihood: Probable

Measures:

Before entering into a partnership extensive groundwork is undertaken to select an appropriate partner and to check references. In many cases Kardan's extensive business network is contacted to identify potential partner candidates. Subsequently, roles and responsibilities are clearly defined and agreed upon and accordingly laid down in legal agreements which are made by our in-house and legal counsels. Moreover, being partners entails frequent sharing of communication which is addressed by regular update meetings.

This risk is segmented as 'Unique Risk' in the Israeli annual report

Sovereign/political

As we operate in emerging markets, we can be confronted with unstable and unpredictable political situations. Such instabilities might adversely affect our operations and their results. In particular, Kardan monitors the developments in the countries where it operates, even if such development may not have immediate and direct impact (for example, US-China trade war, political instability in certain African countries). In addition, the geopolitical situation of Israel in the global political universe could lead to certain countries refraining from doing business with Kardan.

Risk Appetite:

We have a conscious strategy to operate in emerging markets and correspondingly have a medium tolerance for adverse political developments.

Impact: High

Likelihood: Highly Probable

Measures:

The Executive Management and the management of our subsidiaries closely monitor the political situation of the countries in which we are located and adjust our positioning where necessary, desirable and possible. In order to enhance the understanding of the local political environments and the resulting consequences on our businesses, we carefully select local partners and appoint management teams consisting of local and international qualified managers.

This risk is segmented as 'Macro Risk' in the Israeli annual report

Operational Risks**Budget and Planning**

Budgeting and planning are crucial to all companies. The reliability of budgets depends on the ability of management to plan and control, combined with their best assessment of the situation of the (geographic) market(s) and the sector in which they operate. Kardan, with its real estate and water infrastructure activities in emerging markets, faces a number of elements in budgeting – such as periodic valuation of property assets which are affected by macroeconomic developments and consumer sentiment, as well as tendering for projects which may be delayed – creating uncertainties that are almost impossible to manage or foresee. In its assessment, management noted that the impact of uncertainties in the water infrastructure activities proved to be bigger than expected, therefore increasing the likelihood of this risk to materialize.

Risk Appetite:

The nature of the markets that we operate in inherently brings uncertainty and volatility. Consequently, we have high tolerance to adverse impacts on our financial results as a consequence of macroeconomic and other market effects on our budgets beyond our control.

Impact: High

Likelihood: Probable

Measures:

The budgets and strategic plans of all the subsidiaries of Kardan are presented to our Board and focus primarily on all those income statement line items that management can directly influence and control. Factors which are not under our control – such as foreign exchange rate impacts, macro-economic development and the resulting consumer and business sentiment, etc. – are usually not taken into account in the budgets. Monthly highlights, per subsidiary, ensure a proper understanding of the development within the subsidiaries and their operations. At the end of each quarter, a 'latest' result estimate is made compared to the budget, taking into consideration operational, market and economic realities and insights, according to which measures can and will be taken if considered necessary. As a result of the increased likelihood of this risk to materialize, the Board is now reviewing, in coordination with Tahal, additional measures to be implemented.

This risk is segmented as 'Sector Risk' in the Israeli annual report

Project Management

Project management is inherent to our business, in both our real estate and water infrastructure activities. Inadequate project management may negatively affect the achievement of the Company's objectives, its resources and future cash flows or may result in

financial and/or reputational damage. Unfortunately, in 2019 we experienced the impact by way of heavy project losses in the infrastructure activities. In its assessment, management noted that the impact of uncertainties in the water infrastructure activities proved to be bigger than expected, therefore increasing the likelihood of this risk to materialize.

Risk Appetite:

Effective project management is a key value enabler for our business. We have low tolerance for weaknesses in project execution.

Impact: High

Likelihood: Probable

Measures:

Kardan's operating companies are involved in many projects, of varying sizes and complexity, and in many different markets and each operates according to a specific growth strategy. In order to achieve their objectives and goals, it is considered essential to provide the relevant staff with appropriate project management training, including modules on management, operations, commerce and budget control among others. In addition, project reporting, on financial and non-financial aspects, has been implemented in the management information systems of the relevant Group companies. As a result of the increased likelihood of this risk to materialize, the Board is now reviewing, in coordination with Tahal, additional measures to be implemented.

This risk is segmented as 'Sector Risk' in the Israeli annual report

Financial Risks

Financial markets

Kardan is a listed company with operations in emerging and frontier markets and is strongly dependent on external financing. As such, we are

exposed to fluctuations in currencies, prices, interest rates and indices which may affect the value of our financial assets, the size of our financial liabilities and the prices of our listed securities (equity and debt). Although we are not able to estimate the impact of this, developments in the financial markets could adversely affect our results, the equity base of Kardan, the value of our assets, our ability to comply with the covenants, repay our debt and the ability within the Group to raise financing as well as the terms of such financing. It is specifically noted that Kardan is exposed to fluctuations in the exchange rates of the various currencies in which the business affairs of Kardan are managed. These fluctuations may materially affect the financial status of Kardan as the Company reports in Euro, whereas it has NIS denominated debts and most of its assets are denominated in Chinese RMB. During the past 3 years Kardan's equity was heavily negatively impacted by the foreign currency exchange rates which resulted in a deficit in our equity.

Risk Appetite:

We operate in different markets, different currencies and have a strong dependency on external financing. Correspondingly we have a high tolerance to the effects that developments in the financial markets may have outside of our influence of monitoring and hedging risks.

Impact: Critical

Likelihood: Certain

Measures:

Kardan monitors the financial positions within its businesses intensely and hedges these risks if and when deemed feasible given the specific relevant circumstances. We focus on improving our capital position and further decreasing Kardan's debt, taking into consideration the undertakings towards the Debenture Holders, and on enhancing the direct financing of our operating activities within the

subsidiaries. As described under 'capital availability' risk, Kardan is negotiating a new debt settlement with its debenture holders. In this respect, specific discussions are held in relation to equity ratio covenants and the impact of foreign currency fluctuations. Also, Kardan's proposal to convert part of its debt into equity, will strengthen the equity position which was severely hurt due to foreign exchange fluctuations, and will reduce the exposure to future fluctuations.

This risk is segmented as 'Sector Risk' in the Israeli annual report

Compliance Risks

Fraud and illegal acts

Kardan is a decentralized organization with a large number of separate entities spread over different geographic areas primarily in emerging markets. We run the risk that fraudulent activities or illegal acts perpetrated by managers, employees, customers, suppliers or third parties may expose our organization to fines, sanctions, and loss of customers, profits and reputation, etc., and may adversely impact our ability to achieve our objectives.

Risk Appetite:

Having a decentral organization in emerging markets we are exposed to the risk of fraud and illegal acts but have a low tolerance to any deviations from our Code of Conduct.

Impact: Medium

Likelihood: Probable

Measures:

Our Code of Conduct provides guidance to all employees on ethical behavior with the aim of preventing fraud and illegal acts and is circulated throughout the Kardan Group annually. We have also embedded relevant policies and procedures, such as authorization schemes and segregation of duties, as

much as possible in the daily operations in order to provide checks and balances for our activities, as well as a whistleblower policy. Moreover, in some of our operations we have additional measures which enable us, at an early stage, to identify possible operational irregularities. As Kardan needs to comply with many regulations, entity level controls were implemented (also as part of the Israeli SOX) in order to prevent and detect fraud and illegal acts. Further, as described above, in 2018 an internal audit was performed on fraud risk assessment. Although no significant deficiencies were detected, Kardan continues to address fraud risk as a recurring item, also for internal audits.

This risk is segmented as 'Unique Risk' in the Israeli annual report

Legal and Regulatory

Kardan operates in many diversely regulated markets and market segments and is consequently exposed to the risk that changing laws and regulations may threaten its capacity to consummate important transactions, enforce contractual agreements or implement specific strategies and activities.

Risk Appetite:

Adherence to laws, regulations and agreements secures our license to operate. We have a low tolerance to breaches and/or lagging adoption of changed/new regulations.

Impact: Critical

Likelihood: Highly Probable

Measures:

With the assistance of its internal and external legal counsels, Kardan continuously monitors its exposure and the regulatory environments in which it operates, aiming to both anticipate and respond to a changing context or changing regulations and the related consequences on its businesses. Moreover, the governance structure of Kardan and the compliance

policies and procedures provide a structured framework within which all of the group companies operate. In 2018 Kardan put focus on the new GDPR requirements in order to ensure compliance to the extent possible, acknowledging the fact that there is always a certain level of exposure. In 2019, an internal audit was performed on the functioning legal department, and although the result was satisfactory, Kardan continues to review and assess the exposure.

This risk is segmented as 'Macro Risk' in the Israeli annual report

Specific actual risk: spread of the coronavirus

The outbreak of the coronavirus in China and the virus's subsequent global spread adds an additional and actual risk, which is not reflected in our main risk categories. Given its unique nature and the fact that it is actually materializing, it is presented as a separate risk.

The outbreak of the coronavirus constitutes a global macroeconomic risk, causing uncertainty about future economic activity around the world and turmoil on financial markets, and is expected to impact inflation. The potential damage to the global economy depends on the speed and ability to contain the spread of the disease across the entire world. At this stage, given the uncertainty in the duration and magnitude of the crisis, the Company is unable to estimate or the full implications for the Company's operations and financial performance. It should be noted that, as of the Report Date, the spread of the coronavirus and the resulting restrictions placed in China, might adversely affect the financial performance of Kardan Land China in Q1 2020. The continuation of the crisis might cause further deterioration in the financial performance of Kardan Land China and Tahal.

In-Control Statement of the Board (2019)

Kardan's risk management and internal control systems, as described above, have been regularly discussed with the Audit Committee, the Board and the internal and external auditors. During 2019 the Board evaluated the various risk categories as described above. In particular, attention was given to capital availability, financial markets and concentration risks and the possible impact on the going concern of the company should one (or more) of these risks materialize. During 2018 one of the risk materialized when it became clear that the Company was unable to repay its obligations due in February 2018. The Company started negotiations with its debenture holders to come to a settlement. As of the date of this report, these negotiations are still on going, however a final settlement has not been signed yet. The Board realizes that it is dependent on external parties to manage various risks, currently in particular in relation to the sale of assets and to reaching a debt settlement.

Based on its review of the risk management and internal control systems, and recognizing the inherent limitations as described earlier, the Board is of the opinion that

- i. the report provides sufficient insights into any failings in the effectiveness of the internal risk management and control systems;
- ii. the aforementioned systems provide reasonable assurance that the financial reporting does not contain any material inaccuracies;
- iii. based on the state of affairs as per 31 December 2019, it is justified that the financial reporting is prepared on a going concern basis. Reference is made to note 1B of the statutory financial statements regarding the Company's financial position and going concern; and
- iv. the report states those material risks and uncertainties that are relevant to the expectation of the Company's continuity for the period of twelve months after the preparation of the report.