RISK MANAGEMENT REPORT

Office - Cascades Building, Port-Louis

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RISK GOVERNANCE AND MANAGEMENT

The Board believes that risk management must be a seamless part of the Group's culture, with every employee having a demonstrable commitment to risk. It thus recognises its responsibility to oversee the Group's internal control and risk management programme.

The Risk Management and Audit Committee (RMAC), as a subcommittee of the Board, has been established to assist the Board in fulfilling its oversight role. The RMAC, guided by a formally approved charter, reviews the financial statements, risk philosophy, strategy and policies recommended by management, and monitors the internal and external audit activities.

RMAC focus areas during the year under review

Audited Financial statements	Quarterly Management Accounts
Risk Management Reports	Internal Audit Reports
External Audit Reports	Updated RMAC Terms of Reference
Internal Audit charter	Corporate Governance Reports

Internal Audit

Internal auditing services have been outsourced to SmarTree Consulting Ltd (hereafter referred to as the internal auditor). The latter reports functionally to the Chairman of the RMAC.

The roles and responsibilities of the internal audit function are documented in an internal audit charter, as approved by the RMAC. The internal auditor attends all RMAC meetings where the annual audit plan is approved; the findings of the internal audit reports are regularly reviewed.

The internal audit activities are separate and distinct from those of the external auditor. They are designed in accordance with international standards on auditing. The audit scope attempts to cover the significant risk areas, as captured in the business risk register. In discussion with management, the audit scope was extended to non-financial areas like project tendering and procure to pay. The internal auditor has unrestricted access to employees and records.

Audit reports are circulated to senior management and RMAC members. High risks issues are regularly reported and reviewed during RMAC meetings, and a follow-up mechanism is available to facilitate the monitoring of progress on remedial actions. The Chairman of the RMAC is allocated a dedicated portion of time during each Board meeting to report on all aspects relating to internal audit and risk management.

Internal audit services are not limited to providing assurance and satisfying regulatory compliance requirements, although these remain the function's core expectations. During the period under review, the focus for the internal auditor was to have a more collaborative approach, thus shifting the balance between assurance and advisory to achieve greater business insights.

Going forward, the internal audit approach will evolve towards a "trusted advisory service" and actively engage with the external auditor to ensure that combined assurance is provided to address all the significant risks faced by the Group.

Internal Control

The internal control system is primarily designed to manage business risks and provide reasonable assurance against material misstatement or loss. During the year under review, management has been actively involved in reviewing and upgrading its control procedures to mitigate risks more effectively. The internal auditor provides the RMAC and management independent assurance as to the effectiveness of internal control processes.

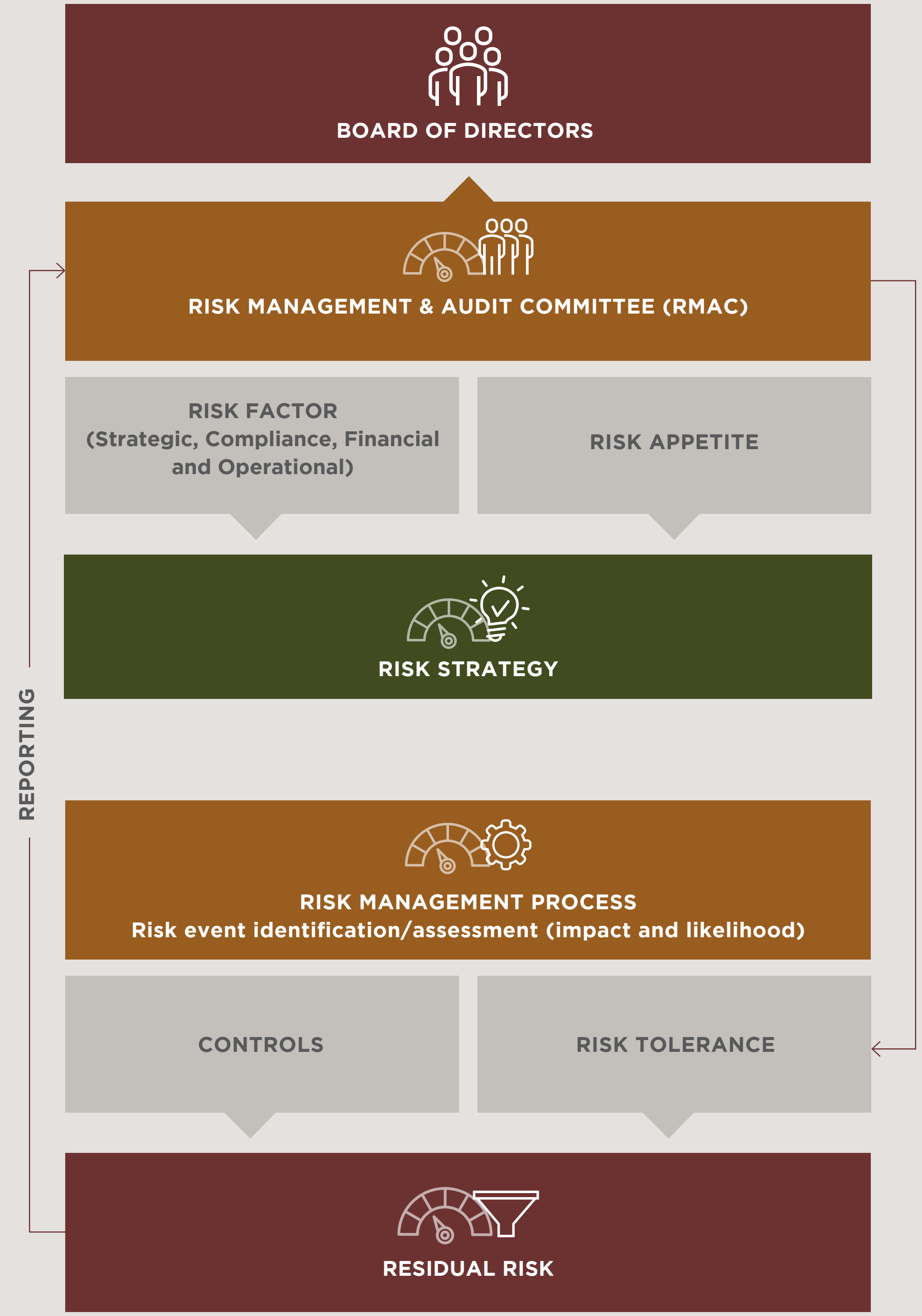
The Enterprise Risk Management Journey

Effective Risk Management is key to achieving Lavastone Properties' strategic and operational objectives.

The Group's focus on managing risks ensures the long-term sustainability of its business. Management is accountable to the Board for the design, implementation and detailed monitoring of the risk management process, and has the responsibility to maintain risk reports, mainly in the form of a risk register and risk chart, which are treated as living documents.

The Risk Governance Structure

The Risk Governance Structure is shown below:



Risk Identification

The Group has in place an identification and risk assessment process, overseen by the RMAC and created for the early detection and assessment of risk events, based on their probability of occurrence and potential impact on strategic objectives. This ensures early risk recognition and evaluation of any immediate or future impact and provides for relevant corrective action to be taken accordingly. The identified risk events are assessed using common metrics: one inherent, before the specific control measures put in place to mitigate the risk, and one residual, considering the specific control measures in place.

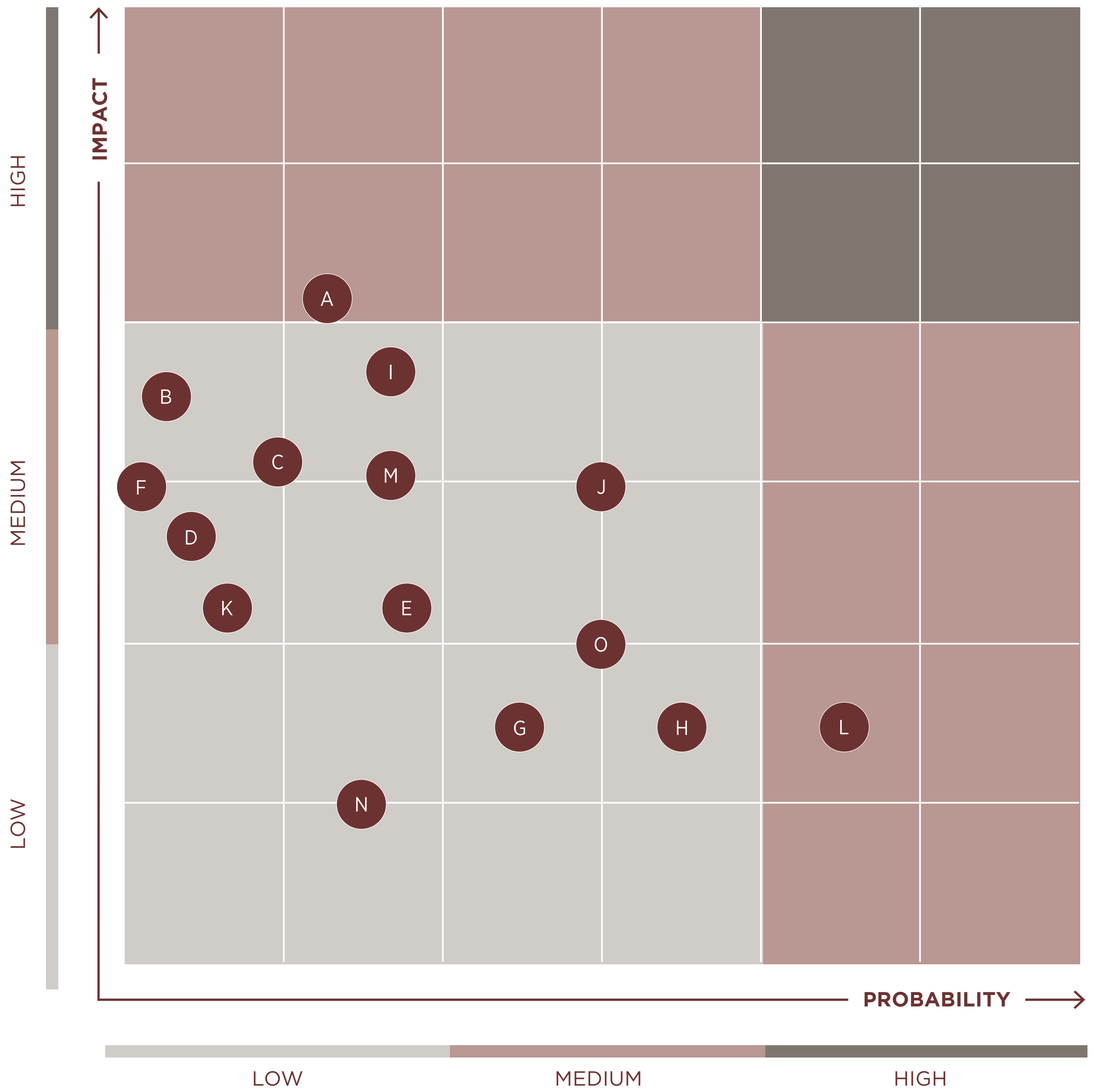
In view of Lavastone's listing on the DEM in December 2018, a risk assessment was conducted during the financial year ended September 2018. During the financial year ended September 2019, the risks mentioned below were regularly reviewed and monitored at RMAC level:

Sector specific risks	FY 17/18	FY 18/19	Trend
Macroeconomic - A	√	√	⇔
Liquidity - B	√	√	⇔
Valuation - C	√	√	⇔

Company specific risks	FY 17/18	FY 18/19	Trend
Regulatory - D	√	√	⇔
Financing - E	√	√	⇔
Credit - F	√	√	⇔
Tenant concentration - G	√	√	⇓
Geographical concentration - H	√	√	⇓
Contracting - I	√	√	⇔
Competition - J	√	√	⇔
Operational - K	√	√	⇓
Business interruption - L	-	New	⇔
Health and Safety - M	-	New	⇔
Environmental development - N	-	New	⇔
Project - O	-	New	⇔

Risk evaluation and treatment

The Risk Chart below shows the most relevant risk events, according to their residual assessment (after controls), that threaten the fulfilment of the Group's corporate strategy:



KEY RISKS AND MITIGATION

The most relevant risk events and main control measures implemented to mitigate their potential impact and/or probability of occurrence are documented in the table below.

	RISK EVENT	DESCRIPTION	MITIGATING CONTROLS
STRATEGIC	**Macroeconomic -** A	Changes in economic conditions may adversely affect the demand for premises (particularly offices and commercial buildings) and, indirectly, the rental potential of buildings and market value of properties. Though these conditions are out of the Company's control, they may adversely affect its NAV or ability to make distributions to shareholders.	Segmental diversification and quality of its existing long-term tenants.
STRATEGIC	**Liquidity -** B	The Group's large land bank and other non-yielding properties may be especially illiquid due to their location, age, quality and specification. Such illiquidity may affect the Group's ability to: • vary its portfolio; • dispose, or liquidate part, of its portfolio in a timely fashion and at satisfactory prices, in response to changes in economic, real estate market or other conditions, or the exercise by tenants of their contractual rights – such as those that enable them to vacate properties occupied by themselves prior to, or at, the expiry of the originally agreed term.	Constant monitoring of its debt cover ratios, while maintaining a conservative gearing ratio. Furthermore, the Group has already put in place an action plan to actively convert its non-yielding assets to yielding status.
STRATEGIC	**Valuation -** C	Property assets are inherently difficult to value as there are no liquid market or standard pricing mechanisms. As a result, valuations are subject to substantial uncertainty – there is no assurance that estimates resulting from a valuation process will reflect the actual sales price, even when such sales occur shortly after the date of the valuation.	Carrying independent property valuations on a yearly basis and ensuring that the Group's reported NAVs reflect the value the Group would receive if it had to sell all of its underlying assets immediately.
COMPLIANCE	**Regulatory -** D	The Group may be adversely affected should there be any changes in accounting standards or regulations in relation to real estate, including those governing permitted and planning usage, taxes and government charges. These can increase business operation costs, reduce the attractiveness of investment and/or change the competitive landscape.	Lobby with authorities and keep abreast of new policies and legislation.

	RISK EVENT	DESCRIPTION	MITIGATING CONTROLS
FINANCIAL	**Financing -** E	The Group has historically been fully funded by Cim. Eventually, it shall stand on its own to negotiate its funding facilities. The Group may use its existing cash resources and incur additional borrowings to finance additions to its portfolio. In the event that rental income of the property portfolio falls, the use of borrowings will increase, which will have an adverse effect on the Group's profits.	Manage the Group's exposure to funding requirements and interest rate fluctuations, through adequate monitoring of credit metrics and debt cover ratios.
FINANCIAL	**Credit -** F	Given the business's tenant concentration, the Group may be subject to one or more tenants being unable to pay their contractual debt obligations.	Conduct regular Service Level Agreement reviews with all tenants and closely monitor debtors.
OPERATIONAL	**Tenant concentration -** G	Over 50% of the rental revenue is contributed by 4 tenants. As a result, the Group's financial performance may be impacted should any of these key tenants decide not to renew their contract. This may be aggravated if the Group is unable to quickly find replacement tenants on the same rental terms.	Build and maintain long-standing relationships with key tenants and ensure they sign long-term rental contracts with the Group. New tenants have been on boarded with long-term contracts.
OPERATIONAL	**Geographical concentration -** H	Over 50% of the Group's rental revenue is generated by its 6 Port Louis properties. Considering the trend over the last few years, which saw businesses relocating to Ébène and other newly created business hubs outside of Port Louis, there is definitely a risk that the Group's financial performance be impacted should existing and prospective tenants decide to relocate outside of Port Louis.	Pursue the Group's expansion strategy to mitigate the risk.
OPERATIONAL	**Contracting -** I	The Group engages in contractual relationships with both related and third parties in the ordinary course of its business. Failure of such parties to fulfil their contractual responsibilities could place the business at risk.	Perform yearly reviews of main suppliers and identify prospective suppliers to replace current ones should these not be able to honour their contractual obligations. For tenant lease contracts, employ strict advance rental collection policies, effected via standing orders.

	RISK EVENT	DESCRIPTION	MITIGATING CONTROLS
OPERATIONAL	**Competition -** J	Competition in the local real estate market may lead prices for properties identified by the Group for acquisition to be driven up through competing bids. Accordingly, the existence and extent of such competition may have a material adverse effect on the Group's ability to acquire properties at satisfactory prices. On satisfactory terms, this may lead to loss of market shares and, possibly, key tenants.	Keep abreast of developments in the real estate market and assess any new opportunity on its merits and on the Group's ability to generate an appropriate return. Ongoing market intelligence and strategic alliances. Continuous improvement of services to clients, including prompt response to resolve issues.
	Operational - K	The Group's operational and financial performance may be impacted by a number of inherent risks, including: • Changes in rental rates and/or occupancy due to competition; • Terms for the renewal of rental contracts, which are less favourable than existing terms; • Ability to collect rent and service charges on a timely basis; • Defaults by tenants and legal costs associated with the recovery thereof; • Renovation costs that are required to preserve or enhance building value; • Repairs and maintenance costs; • Increases in fees paid to third party contractors, particularly facilities management fees; and • Unforeseen capital expenditures.	Pro-actively manage the Group's operations to address the above risks and mitigate issues, by focusing on quality tenants and quality of service delivery.
	Business Interruption - L	The Group may experience unexpected events resulting in damage or injury to individuals or property, caused by natural disasters like fire, lightning, cyclone, tsunami..., or other factors including explosion, terrorism, security breach etc.	Enhance guarding services. Implement emergency procedures including fire drills and bomb threats. Insurance policy with coverage and compensation limits for accident liability, including environmental risks, events triggered by terrorist attacks, or sabotage against company-managed facilities and infrastructure.

	RISK EVENT	DESCRIPTION	MITIGATING CONTROLS
OPERATIONAL	**Health and Safety -** M	The nature of the business exposes the Group to accidents, which can impact both people and property.	Preventive maintenance on plant and equipment. Insurance cover - Public liability/ Contractors, All Risks. Training/drill as per plan with tenants. Implement adequate health and safety systems to safeguard Group activities under a "zero accidents" vision. Continuous training in occupational risk prevention, in line with plan with tenants. Permanent internal and outsourced monitoring of management systems.
	Environmental Development - N	Group activities, including the development of certain projects, can have a significant impact on the environment and the local area within which the Group operates.	Insurance policy with sufficient cover and compensation limits to meet possible liability arising from environmental risks. Measures to ensure compliance with, and awareness of, all applicable technical legislation and regulations. For instance, environmental and social impact assessment, energy efficient building, proximity to flood prone areas, supervision of construction areas and regular inspection of drains/rivers.
	Project - O	The Group has a strong pipeline of projects, already initiated since 2018. Delays in project delivery and/or poor delivery from service providers may have an adverse impact on the Group's reputation and growth. Obtaining permit approvals from local authority may take far longer than expected, leading to increases in construction costs and possible loss of tenants.	High service level specification embodied in agreement with contractors through project management contracts. Close supervision of project with service providers, to produce required project deliverables (scope, time and quality).

Our challenges and way forward for financial year 2019/20

- The Group will continue to pay close attention to any emerging risks that might impair its ability to meet its strategic targets. This also extends to risks which, despite having a low probability of occurrence, could have negative effects on its business targets. Some of the more prominent risks here include natural disasters or risks caused by human action, thereby causing technological disruption and/or obsolescence.
- Aligning the Group's Risk Management processes to ISO 31000:2018 Risk management Guideline. This guideline aims to provide all employees with a general framework on how to control and manage the different sorts of risks they encounter when working towards the achievement of the Group's business objectives. The updated policy will establish how much risk is acceptable by risk factor and set an acceptable level of tolerance.
- Review and update the Group's risk appetite.
- Form and embed a sound risk culture, whereby all employees see themselves as risk managers and consider the risks in their everyday decision-making. This will be achieved through awareness and coaching sessions.