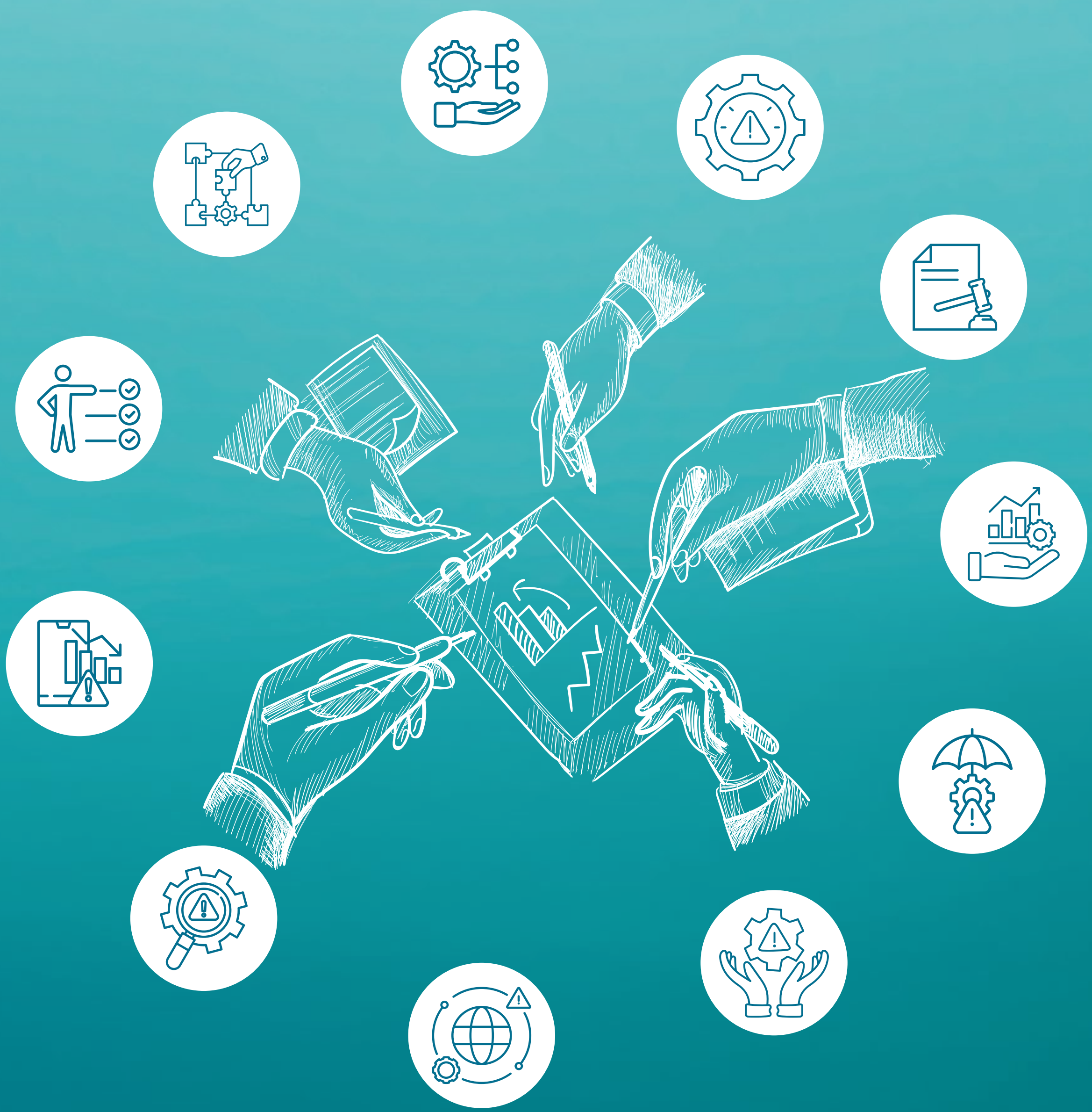
# RISK MANAGEMENT POLICY



AARTI INDUSTRIES LIMITED

## BACKGROUND:

The Policy is formulated in compliance with Regulation 17(9)(b) of the Listing Regulations and Section 134 of the Act, which requires the Company to lay down risk assessment and minimisation procedures.

Section 134(3) of the Companies Act, 2013 ('the Act') requires the Board of Directors of a Company, as part of the Board's Report, to furnish a statement indicating the development and implementation of a risk management policy for the Company including identification therein of elements of risk, if any, which in the opinion of the Board may threaten the existence of the Company.

Regulation 17 of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, as amended, requires that the Company set out procedures to inform the Board of risk assessment and minimisation procedures. The Board is responsible for framing, implementing, and monitoring the Company's risk management plan.

The Risk Management Committee is responsible for ensuring robustness of the Company's Risk Management Framework and the Board of Directors, the Audit Committee, periodically monitors its effectiveness.

## BACKGROUND:

- Aarti Industries Limited ('AIL' or 'the Company') is a leading Indian manufacturer of speciality chemicals intermediates with a global footprint. We combine process chemistry competence (recipe focus) with a scale-up engineering competence (asset utilisation) to create a sustainable future.
- This Policy outlines the Company's risk management framework after suitably considering the applicable Regulations, viz., the Companies Act 2013 ('the Act') and the SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015 ("Listing Regulations"), and the organisational context.

## SCOPE AND OBJECTIVES:

AIL recognises that risk is an integral and unavoidable business component and is committed to managing it proactively and effectively. The Company aims to use risk management to make better-informed decisions and improve the probability of achieving its strategic and operational objectives.

Our risk management policy underpins our efforts to remain a competitive and sustainable company. Our strategy enhances our operational effectiveness and creates value for all our stakeholders.

The Company's Risk Management Policy ("the Policy") outlines the program implemented by the Company to ensure appropriate risk management within its systems and culture. This Policy details the Risk Management principles and framework along with the associated procedures for the Company.

This Policy has been established by the management, to periodically identify, assess, mitigate, monitor, and report on the key risk categories. It also prescribes the risk management governance structure and the roles and responsibilities of various stakeholders within the organisation. The Company also has well-defined policies, standard operating procedures, and controls to minimise and mitigate financial and operational risks.

The prime objective of this Risk Management Policy and Procedure is to ensure sustainable business growth with stability and establish a structured and intelligent approach to Risk Management at the Company. This would include the process for development and periodic review of the Risk Registers and Databases in order to guide decisions on the respective risk issues. This would promote a proactive approach in analysis, reporting and mitigation of key risks associated with the business in order to ensure a sustainable business growth.

The specific objectives of the Risk Management Policy are:

- To identify all material internal and external risks of the Company
- To ensure that all the current and future material risk exposures are continuously identified, assessed, quantified, appropriately mitigated and managed, i.e. to ensure adequate systems for risk management and internal controls;
- To establish a framework for the Company's risk management process and to ensure company-wide implementation;
- To address the responsibilities and requirements of the management of the company as they fulfil their risk management duties;

- To enable compliance with reference to risk management, wherever applicable, through the adoption of best practices.
- To assure business growth with financial stability;
- To formulate the Business continuity plan;

## GOVERNANCESTRUCTURE:

### Board of Directors

Board of Directors (BOD) referred to as the "Board," is entrusted with the key role of ensuring effective risk management and aligning the strategic objectives with the organization's key risks to achieve intended outcomes. The Board shall be responsible for reviewing risk assessment activities, providing strategic input and priority areas.

***Key roles and responsibilities:***

- Review and approve risk management policies, guidelines, and associated practices on its own and/or as per the recommendations of the Risk Management Committee.
- Oversee that risk management activities are established, implemented, and maintained in accordance with the defined framework.
- End-to-end governance of ERM.
- Adequate policies and processes have been designed and implemented to manage identified risks.
- Regular Reviews/Audits are conducted to test the adequacy of and compliance with prescribed policies.
- Proper remedial action is undertaken to redress areas of weakness.

By ensuring effective risk management, the Board can help protect the organization's assets, reputation, and stakeholders' interests. It also plays a crucial role in ensuring that the organization remains resilient and adaptable in the face of changing circumstances and emerging risks.

### Risk Management Committee (RMC):

The Risk management Committee shall comprise of a minimum of three members, with a majority being members of the Board of Directors and at least one member must be an independent director.

RMC shall work towards establishing and implementing the risk management process effectively in the company. Further, RMC shall nominate additional members for RMC meetings as and when the requirement for more departments' representation arises.

As per SEBI (Listing Obligations and Disclosure Requirements) the Risk Management Committee shall meet at least twice in a year in such a manner that on a continuous basis not more than 270 days shall elapse between any two consecutive meetings, or such other timelines as may be prescribed under applicable law.

***Key roles and responsibilities:***

As per SEBI LODR, the Risk Management Committee shall have powers to seek information from any employee, obtain outside legal or other professional advice and secure attendance of outsiders with relevant expertise, if it considers necessary.

The role of the committee shall, inter alia, include the following:

- To formulate a detailed risk management policy which shall include:
- A framework for identification of internal and external risks specifically faced by the listed entity, in particular including financial, operational, sectoral, sustainability (particularly, ESG related risks), information, cyber security risks or any other risk as may be determined by the Committee.
- Measures for risk mitigation including systems and processes for internal control of identified risks.
- Business continuity plan.

- To ensure that appropriate methodology, processes and systems are in place to monitor and evaluate risks associated with the business of the Company.
- To monitor and oversee implementation of the risk management policy, including evaluating the adequacy of risk management systems.
- To periodically review the risk management policy, at least once in two years, including by considering the changing industry dynamics and evolving complexity.
- To keep the board of directors informed about the nature and content of its discussions, recommendations and actions to be taken.
- The appointment, removal and terms of remuneration of the Chief Risk Officer (if any) shall be subject to review by the Risk Management Committee.

The Risk Management Committee shall coordinate its activities with other committees, in instances where there is any overlap with activities of such committees, as per the framework laid down by the board of directors.

## Audit Committee

The Audit Committee as constituted under the prevailing regulatory requirements by the Board of Directors of the Company. The following shall serve as the key roles and responsibilities of the Audit Committee authorized to evaluate the effectiveness of the risk management framework.

***Key roles and responsibilities:***

- Examine the organization structure relating to risk management.
- Evaluate the efficacy of risk management systems-recording and reporting.
- Review the strategy for implementing risk management policy.
- Seek regular assurance that the system of internal control is effective in managing risks in accordance with the Board of Director's policies.
- Ensure that senior management monitors the effectiveness of the internal control system

## Chief Risk Officer (CRO)

The Chief Risk Officer will work with the Risk Management Committee and risk owners in establishing and implementing the risk management process effectively in their areas of responsibility. The Chief Risk Officer shall provide inputs and insights in the structuring and establishment of the risk management process and further monitor its compliance in accordance with relevant provisions of the policy.

***Key roles and responsibilities:***

- Ensure updating of risk management policy pursuant to the organization's risk management purpose.
- Validate that the risk management policy is implemented in each department.
- Discuss with risk owners and finalize the ownership of risk registers, thereby entrusting a person with the responsibility of completion of the risk register.
- Coordinate with Risk Owners for periodic update of risk registers.
- Drive collaboration amongst various risk owners & champions to ensure holistic views are adequately captured in the Risk Register
- Ensure mitigation measures are measurable and quantifiable (wherever feasible) through discussion, collaboration and debate with risk owners & risk champions.
- Assess ratings of identified enterprise risks and prioritize them for its presentation to the Board.

- Apprise the Board on a periodic basis with updates in risk policy, new risks identified, major risks, mitigation plans.
- Present the key business risks faced by the organization and their mitigation plans to the Board.
- Create a framework for a holistic enterprise view to the risk management process and ensure inter department dependencies are addressed.
- Sign off risk assessment templates in coordination with the Risk Owner.

## Risk Owner(s)

Risk Owners shall be the Heads of respective functions or personnel nominated by functional heads on a time-to-time basis depending on the organizational structure and business imperatives to ensure that all critical / significant enterprise risks that may impact strategic objective(s) of the organization are captured while identifying, assessing, and managing risks. The Risk Owner will be responsible for identification of risks emerging from these decisions, ensuring discussions on these risks and measures for mitigation of these risks in this meeting. Their responsibilities include:

***Key roles and responsibilities:***

- Ensure that risks for their respective functions / departments are identified.
- Ensuring that the risk assessment is done as per the risk assessment framework.
- Ensure risk mitigating plans are mapped against identified risks.
- Reporting risks along with assessment and mitigation on a quarterly basis to the RMC.
- Participate and contribute to periodic RMC meetings.
- Review the actionable mitigation measures presented by the risk champions.
- Facilitate implementation of risk mitigation plans approved and other inputs provided by the RMC / the Board.
- Present their risks to the RMC with detailed actionable mitigation measures.

## RISK MANAGEMENT PROGRAM:

The Company's Enterprise Risk Management philosophy is centered around achieving strategic objectives. By identifying, analyzing, assessing, mitigating, monitoring, preventing, and managing risks and potential threats, the company aims to enable effective decision-making and improve overall performance.

Risk management is a continuous, organized process that spans the entire lifespan of a company. It involves identifying and measuring business objectives, information assets, and underlying assets such as hardware, software, and networks. Mitigation options are developed, and appropriate risk reduction plans are selected, planned, and implemented. Ongoing monitoring, reassessment, communication, documentation, and coordination ensure successful risk reduction. The selection of countermeasures is guided by a cost benefit analysis, considering the cost of control compared to the benefit of risk reduction, management's risk appetite, and preferred risk-reduction methods.

The Risk Management process is intended to improve management of risks by:

- Introducing specific methods and practices, particularly a regular and systematic risk analysis.
- The use of a common language and criteria.
- Systematically implement action plans where risks are considered high.

The risk management process has been tailored to the business processes of the organization. Broadly categorizing, the process consists of the following stages/steps:

- Establishing the Context
- Risk Assessment (identification, analysis & evaluation)

- Risk Treatment (mitigation plan)
- Monitoring, review and reporting
- Communication and consultation

The Regular communication and review of the risk management process provides the Company with important checks and balances to ensure the efficacy of its risk management program.

## RISK IDENTIFICATION:

Risks are of a diverse nature. For example, risks can be classified as internal and external risks; controllable and uncontrollable risks, etc. These classifications help in risk identification and a better understanding of the interplay between the risks themselves and between objectives, strategies, processes, risks and controls during risk assessment.

Each business faces risks that are unique to that business. Businesses should consider these carefully and briefly describe what steps would be taken if an uncontrollable risk actually happens to the business (contingency plan). For example, if the risk of a recession would severely affect the company,

Identification of risks is the responsibility of each business/corporate function and is performed based on internal ideation, industry and market research, scanning the external environment, inputs from Annual Operating Plans and Long-term strategy and Leadership inputs. The key categories of risks include Financial, Operational, Reputational, Regulatory, Third-party, Sustainability, Social, Environmental, Projects, Commercial, Human Resources, Information Systems and Technological Risks. The process followed includes every function revisiting its key risks at periodic intervals.

## RISK ANALYSIS & EVALUATION: ASSESSMENT AND PRIORITIZATION:

Risks so identified are assessed to classify them as per the criticality for the business. This would enable prioritization of risks and decide the right risk management strategies appropriate for the different classes of risks. Wherever applicable and feasible, the risk appetite is also defined, and adequate internal controls are installed to ensure that the limits are adhered to.

The process of assessment is based on two parameters – risk impact and risk likelihood. To facilitate understanding and usability in decision making of risk, comparison helps. To enable comparison a risk score is used. By measuring the two risk attributes a risk score can be derived for that risk. This risk score is meant for comparison between a cut-off point normally the 'risk appetite' or comparing to other risks thereby filtering for 'significant risks'.

The **likelihood of risk** is generally measured against five levels on a scale of 5, viz.

- Rare (score 1).
- Unlikely (score 2).
- Possible (score 3).
- Probable (score 4).
- Near Certain (score 5).

**Risk impact** can also be against five levels on a scale of 5, viz.

- Insignificant (score 1).
- Minor (score 2).
- Moderate (score 3).
- Major (score 4).
- Critical (score 5).

A risk with the lowest level of likelihood, i.e., rare (score 1), can nevertheless have the highest level of consequences, i.e., critical (score 5). Various indicators include Impact on EBIDTA, market share, business operations, margins, assets, people, ESG, reputation, etc.,, along with the likelihood indicators. A combinations of these are used to arrive at Risk Velocity or Risk Score. The risk velocity score for that risk is a numeric multiple of the likelihood of the risk and the risk consequences. This can be explained by way of an example: The likelihood of an earthquake causing damage to the manufacturing unit can be 'rare' but the consequences of damage can be 'critical'. In such instances, the blended risk velocity score helps to appropriately identify a risk matrix and also ensures a necessary mitigation plan is adopted.

The Board may from time to time categorise the risk score into three buckets i.e. High, Medium and Low.

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|---|---|---|---|---|---|---|
| **Impact** | **Critical- 5** | 5 | 10 | 15 | 20 | 25 |
| | **Major-4** | 4 | 8 | 12 | 16 | 20 |
| | **Moderate-3** | 3 | 6 | 9 | 12 | 15 |
| | **Minor-2** | 2 | 4 | 6 | 8 | 10 |
| | **Insignificant -1** | 1 | 2 | 3 | 4 | 5 |
| **Risk Score Matrix** | | **Rare-1** | **Unlikely-2** | **Possible- 3** | **Probable-4** | **Nearly Certain-5** |
| | | **Likelihood** | | | | |

## RISK RATING & PROPOSED GOVERNANCE STRUCTURE

### Proposed Governance Structure

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|---|---|
| **High 15-25** | Very high level of risk exposure, which requires continuous attention and immediate response from and needs to be reported to RMC on a semi-annual basis. |
| **Medium 7-14** | Accepted Level of risk exposure, which requires regular active monitoring, measures to be put in place to reduce exposure and reported to RMC on an annual basis |
| **Low 1-6** | Accepted level of risk exposure which requires regular passive monitoring measures |

At the end of the risk assessment and evaluation, the top 10 risks at the Company level are prioritised for periodic monitoring and review by the Risk Management Committee

## RISK TREATMENT: Managing the risks

Each functional head (hereinafter also called as "Risk owner") is responsible for implementing the mitigation plan for the identified key risks for their relevant area. For every such risk, result and effort metrics are defined with milestones to ensure that the mitigation plans are acted upon and reviewed. Effort metrics refers to specific actions to be taken by the respective function or the organization. Result metrics are key internal or external indicators which represent the outcome of the efforts on the risk mitigation plan. The respective Risk Owner provides status updates on the mitigation plan to the Risk Coordinator on at least quarterly basis.

## RISK MONITORING AND REPORTING:

Status of mitigation of various risks are monitored by RMC on a half yearly basis. The RMC also conducts a risk review exercise on an annual basis. Risk reviews ensure identifying any new risk, modifying existing risk, scanning external environments for emerging risk and accordingly updating the priority for risks. The Risk Management Committee meets at least twice in a year to review the risk management process and if required revisit the top risks at the company level.

## REVIEW OF RISK MANAGEMENT PROGRAM:

The Company regularly evaluates the effectiveness of its risk management program to ensure that its internal control systems and processes are monitored and updated on an ongoing basis. The division of responsibility between the Board, the Audit Committee and the Risk Management Committee aims to ensure the specific responsibilities for risk management are communicated and understood.

The reporting obligation of the Audit Committee and the Risk Management Committee ensures that the Board is regularly informed of material risk management issues and actions. This is supplemented by the evaluation of the performance of the risk management program, the Committee and employees responsible for its implementation.

## RISK CONCERNS & MANAGEMENT:

To manage the risk, a detailed study of the threat and vulnerability is conducted. After thorough research, the following are some of the key risks identified by the company and relevant primary risk mitigation measures are taken. Below are the illustrative key risks generally faced by the company:

**Market Risk is the** risk of losses caused by adverse changes in market variables such as competitive prices and commodity prices. Sources of market risk include recessions, political turmoil, demand volatility, natural disasters, and terrorist attacks.

**Price Risk:** Probability of margin pressures occurring from adverse movement in the market price.

**Competition Risk:** Risks arising out of competitive forces in the market that can affect profitability.

**Receivables:** Risks relating to credit defaults impact the working capital negatively.

**Supply Chain Risk:** Risks arising out of non-availability/ higher costs of some key inputs and raw materials, supplier concentration, logistics disruption, etc., can affect production plans.

**Geographic Concentration:** Risks relating to excessive dependence on one or two geographies, which can impact revenues in case of a localized downturn.

**Operational Risk:** Risks associated with the operations of an organisation. It is the risk of loss resulting from the failure of people employed in the organisation, internal processes, systems or external factors acting upon it to the organisation's detriment. It includes Legal Risks and excludes strategic and Reputational Risks as they are not quantifiable.

**Environment, Health & Safety:** Risks relating to inadequate /non-adherence to environmental, health and safety measures.

**Project Execution Risks:** Risks relating to the project execution which can have a bearing by way of Cost over run, time over run or selection of inadequate type of materials or service or design gaps, etc which can impact the timely commissioning of the project and generating the expected returns.

**Technology Risk:** The risk of not keeping pace with rapidly changing technologies for business operations. The use of outdated technologies could adversely impact business operations, resulting in loss of reputation, market share, customers, etc.

**R&D:** There are risks related to the immunity developed against the Company's products by insects or pests, and innovative products are not introduced to counter such immunity. There is also a risk of R&D projects becoming infructuous.

**Interest Rate Risk:** Risk is when changes in the market interest rates might adversely affect the Company's financial health and profitability.

**Foreign Exchange Risk:** Risk of loss that the entity may suffer due to adverse fluctuations in the exchange rate movements in currencies.

**Staffing Risk:** Risk of not employing the right person for the right job.

**Business Continuity Risk -** Risk arising from inability to restore operations immediately in the event of an incident/ disaster.

**Strategic Risk:** The current and prospective impact on earnings, capital, reputation or good standing of an organisation arising from its poor business decisions, improper implementation of decisions or lack of response to industry, economic or technological changes. Failure of strategies will adversely impact the business objectives and attainment of the goals.

**Compliance Risk:** It includes material financial loss or loss of reputation which may occur as a result of its failure to comply with the laws, including regulations, rules, related self regulatory organisation, standards and code of conduct applicable to its business activities.

**Legal Risk:** Arises from the uncertainty due to legal actions or uncertainty in the application, interpretation of contracts, laws or regulations. Legal risk arises from failure to comply with statutory or legal requirements.

**Cyber Security & Information (data security) Risk:** Risk of unauthorised access to data. Poor access controls at the network and application levels give rise to this risk.

**Country Risk:** Risks related to country-specific issues, such as policy changes, trade sanctions, currency embargoes, geopolitical challenges, etc.,, can cause trade disruptions.

**Fraud Risk:** Risk of control failures, management override and deliberate acts of omission and commission that lead to financial losses.

**Climate conditions:** Risks relating to the industry's inherent characteristics, such as rainfall and weather conditions, such as droughts and floods, leading to demand fluctuation and industry downturns (acute and chronic physical), and current and emerging regulations related to Climate Change.

**Regulatory Risk:** Regulatory risk arises due to changes made in policies and procedures by the regulators, such as RBI, Central and State Governments, SEBI, etc. Any changes in the rules and regulations that may negatively impact the business activities can be classified under this risk.

**Reputation Risk:** Adverse publicity regarding an entity's practices can lead to revenue loss or litigation. Any event that affects the entity's name or brand image is a Reputational Risk. Any adverse publicity, news coverage, comments, etc,. can dent the trust created by the entity and become detrimental to its business.

**Conflict:** The Risk Management Committee shall coordinate its activities with other committees in instances where there is any overlap with the activities of such committees, as per the framework laid down by the Board of Directors.

**Effective Date:** This updated version of the Risk Management Policy shall be effective from February 1, 2025.

## POLICY REVISION:

Risks are ever-changing in this volatile business environment, and hence, there is a need to revisit the approach towards Risk management periodically. Therefore, this policy shall be reviewed at least once every two years. Any change in the Policy shall be approved by the Board of Directors or at the recommendation of the Risk Management Committee, as the case may be. The Board of Directors or any of its authorised Committees shall have the right to withdraw and/or amend any part of this Policy or the entire Policy at any time, as it deems fit, or from time to time, and the decision of the Board or its Committee in this respect shall be final and binding. Any subsequent amendment/modification in the Listing Regulations and/or any other laws in this regard shall automatically apply to this Policy.

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