





Our approach to risk management

We maintain a sound and effective system of risk management and internal controls to support us in achieving high standards of corporate governance.

Our approach to risk management

We identify and manage both risks and opportunities, and our internal controls review the effectiveness and efficiency of our operations, the reliability of financial reporting and compliance with applicable laws and regulations – all to build a sustainable business.

Risk Management and Internal Control

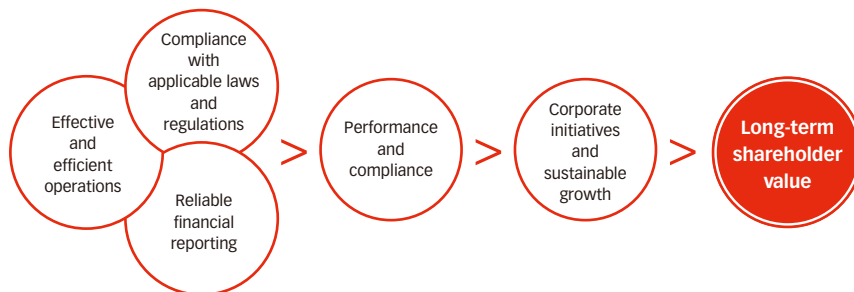
Li & Fung acknowledges that risks are inherent in our business and the markets in which we operate. The challenge is to identify and then manage them so they can be understood, minimized, transferred or avoided. This demands a proactive approach to risk management and an effective group-wide risk management framework.

The Board is responsible for maintaining a sound and effective system of risk management and internal controls at Li & Fung and for reviewing its effectiveness, which forms the development of necessary policies and procedures. We recognize that risk management is the responsibility of all of our people as an integral part of our day-to-day business process. Our system is designed to manage the risk of failure to achieve corporate objectives and aims to provide reasonable, but not absolute, assurance against material misstatement, loss or fraud.

The Board has delegated to management the design, implementation and ongoing assessment of our system of internal controls, while the Board through its Audit Committee oversees and reviews the adequacy and effectiveness of relevant financial, operational and compliance controls and risk management procedures that have been in place. The Audit Committee, in conjunction with the Risk Management and Sustainability Committee, reviews the emerging risks of the Group annually, and the risk management and internal controls in place to address those risks. Qualified professionals within the business maintain and monitor these systems of control on an ongoing basis.

Described below are the main characteristics of our risk management and internal control framework.

Our Internal Control Framework is Designed to Achieve



Control Environment

The scope of internal control relates to three major areas: effectiveness and efficiency of operations; reliability of financial reporting; and compliance with applicable laws and regulations.

The Group operates within an established control environment, which is consistent with the principles outlined in Internal Control and Risk Management – A Basic Framework issued by the Hong Kong Institute of Certified Public Accountants.

Our Governance Structure

Our governance structure enables risk identification and escalation whilst providing assurance to the Board. We assign clear roles and responsibilities for managing risk and implement systems to facilitate the implementation of policies and guidelines. This structure comprises three layers of roles and responsibilities to manage risk and internal control as follows:

Role	Accountability	Responsibilities
Oversight	Audit Committee of the Board, Risk Management and Sustainability Committee of the Board	Oversight of corporate governance, financial reporting, risk management and internal control systems
Risk and control owner	Li & Fung Management and Operations Support Group	<ul style="list-style-type: none"> • Day-to-day execution and monitoring of internal control • Strategic policies and operating guidelines formulation and execution • Balance between business operation efficiency and exercising internal controls
Risk monitoring and communication	Corporate Compliance team	<ul style="list-style-type: none"> • Evaluation of risk management and internal controls to identify areas for improvement • Monitoring of corporate governance disclosure, statutory and listing rules compliance • Undertaking of investigations

Management of Key Risks

Li & Fung's risk management process is embedded in our strategy formulation, business planning, capital allocation, investment decisions, internal controls and day-to-day operations. This includes risk identification, exposure evaluation, control development and execution. There is also a continual process with periodic monitoring, review and reporting to the Risk Management and Sustainability Committee.

The following are considered material risks faced by the Group and are managed as such:

1. OPERATIONS RISK MANAGEMENT

We have adopted a tailored governance structure with defined lines of responsibility and appropriate delegation of authority. This is characterized by the establishment of an Operations Support Group (OSG) to centralize the business support functions and exercise control over global treasury activities, financial and management reporting, human resources, corporate services, legal and information technology systems. This aims to ensure adequate segregation of duties between OSG and front management so that all material transactions, activities, processes, wrongdoings or irregularities can be identified.

All controls of major operations are supplemented with written policies and Key Operating Guidelines (KOGs) tailored to the needs of the respective operating groups in the markets in which we operate. These policies and KOGs cover key risk management and control standards for our operations worldwide, including the businesses of our different operating groups, commitments, credit control and advance payments, capital expenditure, authorizations and approvals for payment processes, and product liability insurance. They also cover administrative activities including information technology use, business travel, HR processes, training sponsorship and procedures for handling grievances.

Contingency and business continuity plans, crisis management including fire drills, preparedness for pandemics and natural disasters and failover tests of key operating systems are also examined periodically to evaluate effectiveness. Corrective actions are taken whenever necessary.

2. FINANCIAL AND CAPITAL RISK MANAGEMENT

The Board approves the Company's Three-Year Plan financial budgets and reviews its operating and financial performance and key performance indicators against the budget on a semiannual basis. Monthly updates are also provided to the Board to give timely and comprehensive assessments of the Company's performance, position and prospects. Management closely monitors actual financial performance at both the Group and operating group levels on a quarterly and monthly basis.

The Group has adopted a principle of minimizing financial and capital risks. Details of our financial and capital risk management covering market risk (including foreign exchange risk, price risk, cash flow and fair value interest rate risk), credit risk and liquidity risk are set out in *Notes 36 and 37* to the financial statements on pages 199 to 202.

3. INVESTMENT RISK MANAGEMENT

The Investment Committee (comprising the Honorary Chairman, Group Chairman, Executive Directors and senior management) reviews strategic investments and acquisitions under a rigorous investment process. Significant investments and acquisitions (with consideration above a threshold pre-set by the Board) also require Board approval. Procedures are in place to monitor the ongoing post-acquisition performance of the investments.

Management also monitors the integration process of newly-acquired businesses through a structured post-acquisition integration program focusing on the alignment of operational and financial controls with the Group's standards and practices. Any significant integration issues must be reported to the Risk Management and Sustainability Committee.

4. REPUTATION RISK MANAGEMENT

The reputation capital of Li & Fung is built on its long-established standards of ethics in conducting business. Our core ethical practices, as endorsed by the Board, are set out in our Code of Conduct and Business Ethics (the Code), available at our internal and external websites, for all Directors and employees. A number of accompanying policies, guidelines and procedures covering anti-bribery, gifts, entertainment and hospitality, declaration of interest and whistleblowing were created to set a framework for our people to make decisions and comply with both the ethical and behavioral standards of Li & Fung. For ease of reference and as a constant reminder, the Code and the accompanying policies and guidelines are available on One Family, our internal communications platform.

All employees are required to abide by the Code and they must apply business principles and ethics which are consistent with those expected by the Board and the Company's Shareholders and other stakeholders. Training sessions are regularly held throughout our global operations to reiterate the Company's zero tolerance approach to bribery and the importance of proper business ethics. Any ethical cases or concerns raised through our guidelines on whistleblowing and reporting of concerns are investigated independently.

The internal audit program integrates the assessment of compliance with the Code and the accompanying policies, guidelines and procedures. The Internal Audit team assesses the significance and risk profiles (e.g. country specific, labor intensity, compliance culture, complexity of regulations, transaction complexity) of the Group's business, operations and processes when determining the audit scope. The scope of internal audits covers the following in respect of the Code:

- Reviewing compliance with the Code and relevant policies and guidelines during the onsite audit of global offices and operations, including business transactions and related documentation
- Reviewing the Code self-assessment program completed by global offices with relevant supporting documentation
- Conducting interactive forums, training and/or individual meetings with management and our people to ensure a culture of good corporate governance, risk identification and compliance is embedded in operations

We are committed to upholding the 10 principles of the United Nations' Global Compact regarding human rights, labor, environment and anti-corruption. As included in our Code of Conduct and Business Ethics, we uphold the International Labour Organization's core conventions for the elimination of forced, compulsory or underage labor, elimination of discrimination in respect of employment and occupation, and respect for freedom of association and collective bargaining. We also acknowledge our responsibility to maintain a respectful workplace that is free of all forms of discrimination or harassment.

In 2015, no incident of non-compliance with the Company's Code of Conduct and Business Ethics that has significant impact to our operations was reported.

5. REGULATORY COMPLIANCE RISK MANAGEMENT

The Corporate Compliance team is comprised of the Corporate Governance and Corporate Secretarial teams. Under the supervision of the Group Chief Compliance and Risk Management Officer and in conjunction with designated internal and external legal advisors, the teams regularly review adherence to relevant laws and regulations, Listing Rules compliance, public disclosure requirements and our standards of compliance practices.

6. INFORMATION TECHNOLOGY RISK MANAGEMENT

Investing in information technology systems is an ongoing priority that supports the growing volume of our business transactions, enables us to improve control and availability of our information, and enhances the security of our systems to manage cyber security risks.

We remained focused on also improving the governance of our IT systems by moving to a managed services model for infrastructure security by leveraging leading vendors' expertise to protect our infrastructure, as well as updating access controls and authentication methods to meet industry standards. In 2015, we established our first Network Operating Center (NOC) in Panyu to monitor our critical data centers on a 24/7 basis. Over 2016 we will bring all data centers under NOC control. We successfully tested our disaster recovery response for all critical systems and applications again in 2015. Security awareness training, which is an important part of our cyber security strategy, is being progressively rolled out to our colleagues around the world.

We continue to develop our core operating systems, including our Export Trading System (XTS), portals for our customers and vendors, Mobile Quality Control (MQC) and OTS, our internal tracking system. We also continue to rollout our financial system E1 to new business units and completed an upgrade of our specialized freight system in China.

In 2015, a program management office was established to bring further consistency, enhanced project delivery and greater visibility of all projects across the Company via an online project portal, Project Central.

Major investments and upgrades continue to be implemented to enhance our financial consolidation tools and forecasting, and our cyber security monitoring with a focus on data privacy policies and governance.

Risk Management Monitoring

In conjunction with the Audit Committee, the Risk Management and Sustainability Committee regularly monitors and updates the Group's risk profile and exposure and reviews the effectiveness of the system of internal control in mitigating risks. Key risk areas covered by the Committees include reputation, business credit, financial and operational risks of our supply chain operations, investment and acquisitions, taxation, inventory and receivable management, group-wide insurance, human resources, contingency and disaster recovery, IT governance, corporate responsibility and sustainability, and specific risks such as operational and adaptation risks arising from climate change.

Internal and External Audit

Internal Audit

The internal audit function is carried out by the Corporate Governance team. Under the supervision of the Group Chief Compliance and Risk Management Officer, it independently reviews compliance with Group policies and guidelines, legal and regulatory requirements, risk management and internal controls and evaluates their adequacy and effectiveness. The Group Chief Compliance and Risk Management Officer reports all major findings and recommendations to the Audit Committee on a regular basis.

The Corporate Governance team's Internal Audit plan is linked to the Group's Three-Year Plan and is reviewed and endorsed by the Audit Committee.

The principal tasks of the Corporate Governance team include:

- Preparation of an Internal Audit plan using a risk-based assessment methodology that covers the Group's significant operations over a three-year cycle
- Review of all operations, controls and compliance with KOGs and corporate policies, rules and regulations. The audit scope covers significant controls including financial, operational and compliance controls, and risk management policies and procedures
- Review of special areas of concerns or risks as raised by the Audit Committee, the Risk Management and Sustainability Committee or senior management

Major audit findings and recommendations from the Corporate Governance team, and management's response to these findings and recommendations, are presented at Audit Committee meetings. The implementation of all recommendations is followed up on a three-month basis and the status is reported to the Audit Committee at its meetings.

As part of the annual review of the effectiveness of the Group's risk management and internal control systems for 2015, management conducted an Internal Control Self-Assessment of business operations and relevant accounting functions. The Corporate Governance team has independently performed a post-assessment review of the findings noted in the self-assessment programs and considered that sound internal control practices were in place for 2015.

External Audit

Our external auditor, PricewaterhouseCoopers (PwC), performs independent statutory audits of the Group's financial statements. To facilitate the audit, the external auditor attended all meetings of both the Audit Committee and the Risk Management and Sustainability Committee. The external auditor also reports to the Audit Committee any significant weaknesses in our internal control procedures which come to its notice during the course of the audit. PwC noted no significant internal control weaknesses in its audit for 2015.

Overall Assessment

Based on the respective assessments made by management and the Corporate Governance team and also taking into account the results of the work conducted by the external auditor for the purpose of its audit, the Audit Committee considered that for 2015:

- The risk management and internal controls and accounting systems of the Group were in place and functioning effectively, and were designed to provide reasonable but not absolute assurance that material assets were protected, business risks attributable to the Group were identified and monitored, material transactions were executed in accordance with management's authorization and the financial statements were reliable for publication
- There was an ongoing process in place for identifying, evaluating and managing the significant risks faced by the Group
- The resources, qualifications, experience, training programs and budget of the employees of the Group's accounting and financial reporting teams were adequate