

Risk Management

Kardan's business strategy inherently comprises risks

Kardan's operating subsidiaries are active predominantly in emerging markets. Hence we are inherently exposed to a relatively high degree of entrepreneurial, geopolitical, financial and legal risks in these markets which, by nature, have a different risk profile than developed markets. The global financial crisis of 2008 and the ensuing sovereign debt crisis negatively impacted the results of Kardan. As a result, the repayment of our two outstanding Debentures – which were issued in 2007 and 2008 by Kardan and are listed on the Tel Aviv Stock Exchange only – became all the more challenging. The current business strategy of Kardan is therefore fully focused on repaying our liabilities as agreed in the Debentures' Amended Deeds of Trust. 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.

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 monthly management reports submitted and presented by the

subsidiaries to enable sound analyses 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, this means – among other things – that Executive Management discusses strategic, operational and budgetary issues with the management and boards of our subsidiaries at least on a quarterly basis. We refer to the Corporate Governance Statement 2016 which can be found on the corporate site, www.kardan.nl.

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 COSO IC 2013. The COSO frameworks were designed to help organizations develop and maintain their internal control systems, to enhance the likelihood of achieving its targets and to be able to adapt effectively to changes in the business and operating environments. In response to the revised Dutch Corporate Governance Code and in anticipation of the proposed update to the COSO ERM Framework we are revising our risk management process for 2017 to secure alignment with best practices.

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 topic 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 in close cooperation with external risk management professionals. 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.

The internal audit, that is carried out by a third-party organization and is done independently of management's own risk assessment, plays an important role in monitoring the risk management framework. Internal audits were mainly undertaken on the operational subsidiaries' level, and no significant shortcomings were detected during 2016. 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 the year under review 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 of December 31, 2016 the control over financial reporting and disclosure is effective (the Control Statement) and the Group's external auditors 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.

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 2016 Statutory Financial Statements. We note that there are other risks that were assessed as having a less significant potential impact on the business. 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

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 and Africa. Our water infrastructure company Tahal recently gained a large 7-years contract in Angola, which doubled its backlog and hence increased the dependence on one project significantly. 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: Highly probable

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 and natural gas. This will mitigate the dependency on the large 7-years contract in Angola. This will also shift the geographical spread of our operational activities gradually, albeit that – given the sector differences – this will not affect the value allocation of our portfolio on our balance sheet. 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 strong governance structure in place to support a communication process 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 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.

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 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.

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.

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.

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

Financial 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 or repayment of shareholder loans, as well as through the sale of assets. 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 execute our objectives, as well as to grow and generate future financial returns.

It is noted that given Kardan's current financial position, the risk of capital availability can also be considered a strategic risk.

Risk Appetite:

Given our debenture debt, cash management is critical to our continuity. We cannot tolerate deficiencies in financing interest and capital repayments; orderly payments must be served.

Impact: Critical Likelihood: Almost Certain

Measures:

In order to bring down debt at the level of Kardan, we aim 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, we sold our remaining 50% stake in Galleria Chengdu in China at the end of 2014, in 2015 we sold our shares in KWIG (transaction completed in 2016), and in 2016 we sold our banking and retail lending subsidiary TBIF. This way, we secured our obligations until February 2018. Our obligations are according to a debt settlement with our Debenture Holders, as reflected in the Amended Deeds of Trust which were signed on July 2, 2015. In general we agreed to defer payment of the majority of the principal by 24 months against certain conditions, restrictions and collateral.

We manage the capital structure and liquidity position of Kardan and each of our subsidiaries intensely. In line with our financial strategy, our operating companies are largely responsible for their own funding. The Amended Deeds of Trust, however, do impact the ability of our subsidiaries to expand their credit facilities. Cash flow forecasts are made on a regular basis and discussed within the subsidiaries and with Kardan's Executive Management and Board, enabling

us to control the cash situation optimally and to be able to make sound decisions.

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

Financial markets

Kardan is a listed company and is strongly dependent on external financing. It has a high exposure to emerging markets in general and China in particular and it currently has a significant debt position. 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, which are largely beyond our control. 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.

Risk Appetite:

We operate in different emerging 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: Almost Certain

Measures:

Kardan monitors the financial positions within its

businesses intensely and hedges these risks if and when deemed necessary and worthwhile. 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. Moreover, we place a lot of emphasis on our investor relations activities by providing transparent and reliable disclosure as well as by maintaining regular contacts particularly with our debt holders all according to the applicable rules and regulations as well as to Kardan's policy on bilateral contacts.

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, such as in our water infrastructure organization Tahal, in 2015, we introduced 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.

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: High Likelihood: Highly Probable

Measures:

With the assistance of its internal and external legal counsels, Kardan continuously monitors the regulatory environments in which it operates, aiming to both anticipate and respond to 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.

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

In-Control Statement of the Board

Based on its review of the risk management and internal control systems, and recognizing the inherent limitations as described earlier, the Board has concluded that there is reasonable assurance that:

- it understands to which extent Kardan's strategic and operational targets are being realized;
- Kardan's internal and external financial reports are reliable and do not include material misstatements;
- internal control over financial reporting is effective;
- the risk management and control systems worked properly in the year under review, within the boundaries of our risk appetite; and, applicable laws and regulations are being complied with.

Kardan's risk management and internal control systems, as described above, have been regularly discussed with the Audit Committee, the Board and the external auditors. During 2016 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. The Board was content with the mitigating measures that were taken in 2016, such as securing debentures repayment, reducing concentration exposure by completing the sale of KWIG, and to CEE by selling TBIF.

It is important to note that effective risk management, with embedded internal control, no matter how well designed and implemented, provides the Executive Management and the Board with only reasonable assurance regarding the achievement of the Group's objectives. The achievement of objectives is affected

by limitations inherent in all management processes. These include the implicit risk that human judgment in decision-making can be erroneous and that breakdowns can occur as a result of human failure, such as a simple error. Additionally, controls can be circumvented by the collusion of two or more people, and management has the ability to override the enterprise risk management process, including risk response decisions and control activities. Another limiting factor is the need to consider the relative costs and benefits of risk responses. Therefore, in this context 'reasonable assurance' refers to the degree of certainty that would be satisfactory for a prudent manager in the management of his business and affairs in the given circumstances. Any assessment of effectiveness in future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with Kardan's standing policies, procedures, and instructions may deteriorate.