

Report by the Managing Board

fundamental and applied research and his dedication to innovative science. The award was presented at the IUPAC Macro 2008 Congress in Taipei (Taiwan).

Risk management

Responsibility

The Managing Board is responsible for risk management in the company and has designed and implemented a risk management system. The aim of the system is to ensure that the extent to which the company's strategic and operational objectives are being achieved is understood, that the company's reporting is reliable and that the company complies with relevant laws and regulations.

Reporting structure

In this annual report, reporting on risk management is organized as follows:

- Below, the Managing Board describes the most important risks and responses in relation to the achievements of the *Vision 2010* targets. It is also described how the risk management system is used to arrive at conclusions regarding the functioning of the internal controls over financial reporting (the 'In Control Statement').
- In the risk management section (page 84) of the chapter on corporate governance, risk management, financial policies and related functions, a general description is given of the risk management system, the most important adaptations of the system and the risks that are relevant for the company.
- Information on financial risks is provided in the financial statements on page 131.
- On the day of publication of this report, an updated full description of the DSM Risk Management System as well as a more elaborate description of relevant risks will be published on the DSM Internet site. The descriptions are to be found on the Risk Management pages of the Governance section of DSM's website (www.dsm.com) and should be considered an integral part of DSM's risk management reporting over the year 2008.

Main risks

As part of the annual risk management calendar, the Managing Board updated the Corporate Risk Assessment. For this assessment, last year's list of risks was reviewed and supplemented by information from external and internal risk reports, events and other views and information obtained. These risks were ranked and responses were formulated by the Managing Board. The outcome of the assessment was checked

against internal risk reports. The most important risks and responses are reported here:

- The impact of the global financial crisis and economic downturn is seen as one of the most important risks for the remainder of the *Vision 2010* period. Especially in the end markets for most of the Materials Sciences businesses an unprecedented decline has occurred, whose depth and duration is still very hard to predict. Although the emerging economies have been less affected, their growth rates have also declined below earlier expectations and prospects have larger uncertainties than before. The financial crisis is making access to cash more difficult and more expensive. The pension reserves have been diminished by the stock price developments; this is expected to have a considerable negative non-cash EBIT effect in 2009 compared to 2008. DSM's response to the financial and economic downturn covers all of the above aspects and is coordinated by a newly installed dedicated corporate team that works with the full Managing Board and the DSM Leadership Council. The responses include cost-cutting measures, reduction of capital expenditure programs, as well as an extra focus on cash and credit management. Opportunities are, however, also investigated and promising innovation initiatives are preserved as much as possible in order to safeguard future growth opportunities.

Other main risks are:

- Disposals and acquisitions. DSM has tested methods to conduct these processes successfully. There is, however, always the risk that suitable candidates do not present themselves against affordable conditions. This risk has increased due to the financial crisis.
- Price volatility (and secured supply) of raw materials and energy. Hedging policies have been put in place and are now being reviewed and extra focus has been put on single source situations. Extreme volatility can, however, always lead to unavoidable losses and the stability of suppliers may be affected by the crisis.
- Deteriorating market conditions and/or commoditization for the existing product portfolio. This risk may be aggravated by the global downturn, due to lower global utilization rates. DSM continues to counter this risk by innovation and product differentiation, but also by low-cost country sourcing, cost savings and process improvement measures.
- The ability to turn innovation efforts into profitable business. Close monitoring of the innovation portfolio is in place and best practice solutions for new product development and launch

have been implemented. Nevertheless, uncertainties with respect to the eventual success of new products and applications remain, especially in today's economic environment, where some of DSM's customers might re-prioritize their needs.

- People, organization and culture. The ability to attract and retain the right people and to create an entrepreneurial yet responsible culture is key to the achievement of the *Vision 2010* targets. During the reporting year new recruiting, management development and learning practices were implemented. Organizational changes were set in motion and programs to support the entrepreneurial spirit and cultural change were initiated. Nevertheless, the above remains a critical success factor in the implementation of DSM's strategy.

Functioning of the risk management system

The implementation of the Corporate Requirements, which represent common controls for the most important commonly occurring risks, was continued in those business groups which were allowed by the Managing Board to delay parts of the implementation until after the general due-date of 1 January 2008. In these units, much attention was given to the implementation of temporary controls where necessary.

All business groups and the major operational service units have an Audit Committee, which, under the direction of the director, sets up annual risk management plans, monitors their implementation and reviews risk management issues on a regular basis. Major risk management events, such as the outcome of corporate audits and business risk assessments and the occurrence of material control failures or weaknesses were discussed with the responsible Managing Board member.

Information on the functioning of the system was collected on a continuous basis. Business groups tracked compliance with Corporate Requirements and follow-up of actions from risk assessments; they conducted assessments on the effectiveness of their internal controls and reported and investigated incidents. The business group controllers confirmed that the quarterly financial statements were produced according to the internal accounting rules and reporting procedures by signing an affidavit. Independent audits on the effectiveness of the risk management implementation were executed by Corporate Operational Audit according to a program agreed with the Audit Committee of the Supervisory Board.

The information thus gathered was used for improvements to the risk management system as described on page 84, while any critical findings were addressed immediately.

Together with the annual financial accounts, all business groups, staff and service departments reported on any material operational, reporting and compliance risks or incidents over the past year in their Letter of Representation. The Corporate Risk Management department consolidated the reported risks and incidents and compared them with the outcome of corporate audits.

These data were used to spot weaknesses and formulate recommendations for reinforcement of the risk management system. The reported risks were also compared with the outcome of the Corporate Risk Assessment; on that basis the final overview of main risks and responses was produced. The main risks were discussed with the Audit Committee of the Supervisory Board on 16 February 2009.

Statements of the Managing Board

On the basis of the above and in accordance with best practice II.1.4 of the Dutch corporate governance code of December 2003, taking into account the recommendation of the Corporate Governance Code Monitoring Committee on the application thereof, the Managing Board confirms that internal controls over financial reporting provide a reasonable level of assurance that the financial reporting does not contain any material inaccuracies, and confirms that these controls functioned properly in the year under review and that there are no indications that they will not continue to do so. The financial statements fairly represent the company's financial condition and the results of the company's operations and provide the required disclosures.

It should be noted that the above does not imply that these systems and procedures provide absolute assurance as to the realization of operational and strategic business objectives, or that they can prevent all misstatements, inaccuracies, errors, fraud and non-compliances with legislation, rules and regulations.

In view of all of the above, the Managing Board confirms that, to its knowledge, the financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the annual report includes a fair review of the position at the balance sheet date and the development and performance of the business during the financial year together with a description of the principal risks and uncertainties that the company faces.