Risk management and principal risks

Risk management

Risk management

The key risks and the approach we take to their management are set out below. Certain additional risks are explained elsewhere in the Annual Report. Specifically, the impact of the war in Ukraine, the COVID-19 pandemic and resulting economic market risks (which still include Brexit) are discussed in the Chairman's statement and Operational review and the cyber risk to the Group is discussed within the Corporate governance report, alongside our ethical and behavioural risks. Our risk in respect of our key resource, our employees, is explained within this Risk management section but also expanded upon in the Business model and Stakeholder engagement sections of this report. These should be considered alongside this section to give a complete picture of our risks and their management and control.

The Group reviews, analyses and addresses the risks it faces through the Audit Committee, Board, Group Executive and subsidiary management meetings, and subsidiary project and functional reviews.

Depending upon the nature of the risk, review and action may be on an annual basis. In most cases the review is more frequent. Project risks are generally reviewed monthly.

"The Group reviews, analyses and addresses the risks it faces through the Audit Committee, Board, Group Executive and subsidiary management meetings, and subsidiary project and functional reviews."

Risk management and principal risks continued

Unchanged Increased Decreased

Nature of risk	Mitigation and progress	Change
Business risk		
Capacity to grow the Group		
As an AIM-listed group, Cohort's strategy is to grow, both organically and by acquisition. This gives rise to the risk of the Group not having the capacity to grow in line with our strategic objectives. Specific elements of this risk include our ability to win new business and design new and competitive products and solutions, whilst ensuring that we meet our obligations to our customers and identify and execute suitable value-adding acquisitions. It also includes having sufficient people of the right skill sets to deliver our existing commitments and develop our future products and solutions (see below).	The elements of this broad business risk are addressed below, especially the risks in respect of customers, operations, acquisitions and treasury. At a higher level, our federated model of relatively small, independent businesses enables us to respond more quickly to changing market and business conditions. Through this independence, each business is able to retain a good degree of innovation and responsiveness. This model also allows our businesses to keep close to customer requirements and technical changes to enable them to identify the need for new products and solutions and how best to achieve this, whether through our own development or utilising third-party technologies. To ensure that the business growth opportunities are value adding, whether new business, products, services or acquisitions, appropriate controls are in place in our subsidiaries' businesses and at Group level to lessen the risks of such undertakings.	Unchanged
Market risk		
Customers		
The Group's single most important customer remains the UK MOD. £46.3m of revenue came directly from this source in 2022 (2021: £43.9m), 34% (2021: 31%) of Group revenue. In addition, £18.5m (2021: £16.3m) of Group revenue, 13% (2021: 11%), was sourced ultimately from the UK MOD but received via other contractors. Any event which affects the Group's reputation with the UK MOD could also put this revenue at risk.	The increase in the proportion of the Group's revenue to its ultimate primary customer in 2022 compared with 2021 reflects the stronger performance at MCL and SEA as well as the overall decline in revenue at Chess and EID where the UK MOD is a much smaller customer. In the immediate future we expect the revenues, direct and in-direct with the UK MOD to remain at least at this absolute level, but as we see a recovery in revenue at Chess and EID, the latter over the next two years, the proportion of the Group's revenue with the UK MOD is expected to gradually decline. Revenue from the Portuguese MOD, which is also a home market for the Group, was lower at £3.9m (3%) in 2022 (2021: £5.9m; 4%). The fall in revenue from the Portuguese domestic customer was a result of slippage of orders, particularly a naval programme, which we now expect to be secured in late 2022/23. Germany is also a home market for the Group following the acquisition of ELAC Sonar (ELAC). Sales of £4.0m (3%) in 2021/22 (2021: £1.0m; 1%) were higher than last year, in part due to 12 months being reported (2021: five months) by ELAC and higher supplies for German frigate overhauls. Non-defence sales (which include security) increased to £18.0m (13%) from £17.2m (12%). The increase was due to slightly higher transport revenue where the deployment of traffic camera systems increased following the easing of COVID-19 restrictions. Higher education sales at MASS offset slightly weaker security sales following completion of the Metropolitan Police contract and no Subsea sales at SEA in 2021/22 after the business was sold in August 2020. £48.8m of revenue (35%) was delivered to defence and security export customers this year compared with £60.7m (42%) in 2021. This decline was partly expected with high EID deliveries to a Middle East customer in 2021 not being repeated. Chess sales were also down, mostly in export with delayed orders and slippage of some deliveries to European customers. These reductions were partly offset by the full year contribution from ELAC (2021: five months). £33.6m (2021: £40.8m), 24% (2021: 28%) of Group revenue, representing 53% (2021: 68%) of revenue derived from the UK MOD, was in relation to the Astute and other submarine programmes, nuclear deterrent programme and operational support to the Royal Navy, Royal Air Force and Joint Forces, all of which have been confirmed as high-priority areas following the UK Government's latest Strategic Defence and Security Review. This revenue stream is expected to be higher in the coming financial year following some key order wins in the final quarter of 2021/22.	Unchanged

Risk management and principal risks continued

Unchanged Increased Decreased

Nature of risk	Mitigation and progress	Change
Operational risks		
Employees		
The Group's main resource is our employees. We are not a capital intensive business and as such our value and our customers' value derives from the ability of the Group to recruit, retain and train employees with the right skills and flexibility. In some of our key areas, resources are limited, and it is a risk if we cannot maintain sufficient numbers and appropriate skills.	As highlighted in the People section of our Sustainability report, we endeavour to provide an environment in which skilled employees are attracted to our business through the nature and variety of work and the level of responsibility we can provide. We maintain close links with our military and security customers, which provide a primary source of domain experts for our businesses. We, in return, are keen to support people initiatives for and within those organisations, including the UK MOD's Armed Forces Covenant. We maintain close links with academic institutions in our neighbourhoods and further afield where appropriate skills exist. We have apprenticeship and graduate recruitment schemes which ensure that the Group is able to develop its own people and that skills are maintained into the future, especially in the light of shrinking military establishments. In the last year, as our order book has expanded and operating activity has returned to near pre-COVID-19 levels, we have been expanding our work force across the Group, especially at Chess, ELAC and SEA. In some cases, we have experienced a challenging environment to recruit the right skills with challenges in both availability and cost. In some specific areas, especially software and cyber, we have seen even more marked wage inflation. In all cases we have continued to engage closely with our employees, ensuring we develop and compensate them appropriately and continue to offer a working environment that they find both interesting and rewarding. We have already put in place an Employee Value Proposition programme at MASS and are rolling this out across the Group to ensure we attract and retain the key skills the Group requires now and into the future.	Increased
Suppliers		
As is typical in the defence sector, the Group is reliant on certain key suppliers for specific elements of its technical and product offerings. This reliance is long term, with product duration in this sector often being tens of years.	This risk is managed through close liaison with suppliers, good project management and having contingency plans to contract with alternative suppliers or bring the work in house. The long-term life of many defence products requires a regular review of product life and capability, and the Group supports the customer in this respect through funded ongoing product support and re-life tasks. We have continued to see some suppliers struggling to meet delivery schedules because of COVID-19. This has been particularly noticeable where the level of a supplier's output to the defence sector is low, and the supplier is more dependent on the commercial aerospace and automotive markets. We have seen delivery times increase, particularly for semiconductors and certain other components. We have, where appropriate, ordered products and components ahead of schedule to ensure we meet customer expectations. This has resulted in a higher working capital commitment. In the last year, lead times have steadied, but remain longer than we had previously seen pre-COVID-19. We have seen the additional impact of inflation, especially in supplies of products with high energy inputs, e.g., ceramics. As discussed below in operations, we continue to try and manage this inflation by looking for alternatives or passing on costs where we can through higher pricing. Many longer-term contracts include an index-based price adjustment which automatically compensates for some or all supply inflation. In most cases, bought-in parts and equipment are a small proportion of total cost, so the inflationary impact can be managed. Nevertheless, this is certainly a higher risk for the Group in the coming year.	Increased

Risk management and principal risks continued

Unchanged Increased Decreased

Nature of risk	Mitigation and progress	Change
Operational risks continued		
Operations (Chess, EID, ELAC, MASS and SEA)		
The subsidiary trading and business risks are similar in the cases of Chess, EID, ELAC, MASS and SEA. i. Bid risk – the businesses bid on contracts where the scope of work may not be well or fully defined by the customer. ii. Fixed-price contracts – these are often of a long-term nature (greater than 12 months) and typically include delivery of hardware and software, some of which may be developed as part of the contract. iii. Due to the nature of their niche technical skills requirement, Chess, EID, ELAC, MASS and SEA all have a fixed level of core software and hardware engineering and technical expertise.	This is typical in defence and is managed through bid/no bid reviews at the appropriate level using experienced personnel, including the Cohort Executive and Board. These projects are managed by dedicated project management teams, monthly reviews by the subsidiary board and regular interaction with the customer and key suppliers. Revenue and costs are recognised taking account of risk and the estimated cost at completion (including any contingency). This cost base is carefully monitored at budget time and by rolling quarterly forecasts to identify any potential risk of low utilisation and thus under-recovery of cost, or over-utilisation leading to the inability to meet customer commitments. Risks from higher inflation and lengthening delivery times have been seen across the Group. We have increased stock holdings of key components to ensure delivery risk is mitigated as far as possible. In the case of inflation, we have tried to fix prices with our supplier base and where this is not possible have used index-based pricing, particularly in long-term contracts, to protect our margins. We have seen component prices rise, in some cases significantly and have as far as possible reflected these costs in bids and tenders. The risk of staff shortages is mitigated, in the short term, by the use of sub-contractor staff. In the long term, a programme of skills assessment and training is in place to ensure continued flexibility of the Group's engineering and technical resources. Chess was acquired in December 2018. Chess brought with it more production, including machining, than seen elsewhere in the Group. As highlighted previously, we have seen operational, project and commercial weaknesses at Chess. We made progress last year by appointing Operations, Project and Technical Directors to the business. Further work was also completed during the last year to improve Chess's delivery performance and tighten its commercial processes. We did not see the full benefits of these until late in this financial year. The acquisition of ELAC in December 2020 added further manufacturing and testing capability to the Group. ELAC, having been owned by various public listed companies over the last 20 years, has very good control processes in place. However, its recent win of the large Italian submarine sonar contract is a significant development and delivery step for the business and the Group has put in place a Project Advisory Committee (PAC) to act as a review panel for the project and to be able to advise ELAC and the Cohort Board. This PAC comprises individuals with extensive experience in the submarine and sonar domains.	Unchanged
Operations (MCL)		
MCL's revenue visibility is short at typically three to six months. This carries risk to employee utilisation and predictability of revenue and profit.	MCL's employee levels are low, 2022: 39 (2021: 36), and its people are flexible and possess multiple skills, enabling them to take on design, integration and support tasks across the full range of MCL's product offering. MCL has a long-term strategy to improve its visibility by securing longer-term contracts, utilising the Group's size and financial stability. Its order cover for 2022/23 is higher than last year's at 80% (2021/22: 55%) and is a result of increased activity from UK MOD, particularly for hearing protection and drones in the final quarter of our financial year. MCL has significant exposure to the UK MOD (over 90% of its revenue). As we reported last year, the marked increase in the UK MOD budget and agreed four-year spending plan gave MCL some positive momentum and we are seeing this now translate into orders. MCL is very much the Group's weathervane in respect of UK MOD spend.	Decreased

Risk management and principal risks continued

Unchanged Increased Decreased

Nature of risk	Mitigation and progress	Change
Operational risks continued		
Managed service contracts		
The Group (through its subsidiaries, MASS, MCL and SEA) operates a number of off-site managed service contracts. These contracts are long term in nature (typically five years at commencement) and have dedicated project managers. The contracts are fixed price in terms of revenue with opportunities for additional tasks enhancing volume and return. The long-term nature of these contracts does expose the Group to the impact of high inflation.	The Group carefully manages the partnership with its customer and supplier base in all these cases to ensure the customer receives value for money, with skilled Group staff providing a dedicated, flexible and responsive approach. The primary risk to these managed service contracts is termination or loss through competition. We mitigate this risk through the partnering approach adopted by the Group and our close engagement with customers to ensure their needs are met. SEA are in discussions with the UK MOD to secure a long-term service contract to support various SEA products in service with the Royal Navy, including Torpedo Launcher Systems and Sea Gnat countermeasures systems. The Group manages the inflation risk in these contracts through index-based pricing. Elements of these long-term contracts are contracted by the customer as required (e.g., purchases of spares) and are priced at that point in time, taking account of actual costs.	Unchanged
Export contracts		
The Group's subsidiaries seek to win and deliver solutions and services outside its geographical home markets, the UK, Germany and Portugal. The risks that arise for the Group relate to the need to comply with local and domestic legislation, and to ensure we receive payment in circumstances where political and credit risk may be much higher than in our domestic markets. There is also a risk that export licences may not be granted or may be cancelled. The timing of some export contracts can be more difficult to predict.	The Group's long-term strategy is to grow its export business, both in terms of volume and markets. This provides mitigation against reliance on any single customer, in particular the UK MOD. Total export activity in 2022 represented 35% (2021: 42%) of the Group's revenue. Revenue derived directly and indirectly from the UK, German and Portuguese defence ministries represent 47% (2021: 42%), 3% (2021: <1%), 3% (2021: 4%) of the Group total respectively. The completion of deliveries by EID on one export contract in 2020/21 accounts for most of the decline, together with weaker export revenue at Chess. Our commercial employees are highly experienced at dealing with the various regulatory processes associated with the export of defence goods and services, including export licence applications and information security requirements. In particular we have a strong Group-wide Anti-Bribery Policy to ensure compliance with the UK's 2010 Bribery Act. The Group has experienced a very low level of bad debts, including from export contracts. We take a case-by-case approach to payment risk, making use of various treasury and commercial arrangements where necessary to ensure payment. We regularly monitor any potential political risk to any of our export markets, and we do not commit resources to markets where export licences might be difficult to obtain. COVID-19 may impact our export markets with individual customer defence budgets coming under pressure. We may also see more positive demand drivers arising from changes in regional security stances and disputes, notably the recent invasion of Ukraine by Russia. The unpredictability of some export contracts, especially in terms of timing, remains a risk. Any increase in defence spending by NATO members may have both a positive impact on the volume and predictability of the Group's revenue.	Unchanged
Partners		
The Group, especially in the defence sector, often secures business through teaming and partnering with other suppliers and this is often a requirement of securing work with the UK MOD in order to ensure the end customer receives the best solution. This creates a risk that the Group's revenue or profit will be affected by poor performance of partner business.	The Group takes an active part in these arrangements and, through regular (usually monthly) project review meetings and other communication, ensures that the team (including our partners) delivers to the customer and meets the needs of the individual team members. During the year ended 30 April 2022, the Group acquired the remaining 50% shares in JSK (Canada) to ensure that we are able to fully support the Canadian Future Frigate programme.	Unchanged

Risk management and principal risks continued

Unchanged Increased Decreased

Nature of risk	Mitigation and progress	Change
Strategic risk		
Acquisitions		
The buying (and selling) of businesses is a risk in respect of value, distraction, integration and ongoing obligations and undertakings.	The Group's acquisition risk is mitigated as far as practicable by the acquisition process being led at the Cohort Board level, making use of a skilled and experienced internal team augmented by external expertise and resources as and when required. Our approach to acquisitions is set out more fully in our Business model. During the year ended 30 April 2022, the Group continued to review potential businesses with a view to them joining the Cohort Group. One small acquisition completed in the year when SEA's 50% owned joint venture in Canada, JSK, was fully acquired. The work on this acquisition was led by SEA's management team with oversight from the Cohort headquarters. One ongoing acquisition process was aborted during the year following a review of the market prospects.	Unchanged
Financial risks		
Treasury		
A key risk is that the Group deposits monies with banks that are a credit risk, putting our cash resources at risk. A risk for the Group is that its pools of cash and facilities, in the UK, Germany and Portugal, are insufficient for local needs. In addition to our own cash, the Group has facilities with banks to provide debt (structured and overdraft) and other financial products (bonds, foreign exchange instruments etc.) to enable us to carry out our operations efficiently and to execute our strategy of growth by acquisition and organically. Under the facility agreement with its banks, the Group is required to meet certain covenants every quarter. There is a risk that the Group does not meet some or all the covenants and that the facility is amended or cancelled as a consequence.	The Group takes a very prudent approach to the management of its financial instruments, which are described in note 18. The Group's cash (see note 15) is usually held with at least Baa3-rated institutions (including Germany and Portugal) and on deposits usually not exceeding three months. This ensures a very low risk to capital and a reasonable balance of liquidity against interest earned on cash deposits. Over the last 12 months, the credit ratings of most of our banks (see note 15) have remained steady. The Group regularly reviews the ratings and other relevant factors in respect of the banks with which it deposits its cash and on each and every occasion that a short-term deposit is placed. The Group prepares a monthly cash forecast to ensure that cash in the UK, Germany and Portugal is sufficient for local needs over the following three-month period. The shareholder agreement in respect of EID enables dividends to be paid from EID to the UK. In July 2022, the Group completed a new bank facility with Commerzbank, Lloyds and NatWest. NatWest remains the Group's primary bank in the UK, especially for clearing purposes and day-to-day transactions. Commerzbank performs a similar role in Germany. The facility is a revolving credit facility for three years out to July 2025 with options to extend for a further two years to July 2027. The facility is for £35m with an accordion in place to extend it by a further £15m to £50m in total. Of the Group's existing facility at 30 April 2022 (£40.0m), £29.4m was drawn at 30 April 2022. The existing and new facilities provide the Group with a flexible arrangement to draw down for acquisitions and overdrafts. The renewal of the Group's banking facility for three years (with two option years) and our strong net funds position as at 30 April 2022 provide the Group with a robust financial strength for at least the next 12 months. The Group's new facility is available to all the Group's entities (excluding EID) through an offset arrangement. The existing and new facilities are secured against all the Group's UK and German businesses (and assets) including the Group's shares in EID. EID has facilities with local banks in Portugal, none of which have security over its assets. These facilities are for clearing bank purposes, overdraft, foreign exchange contracts, guarantees and letters of credit. The Group regularly monitors its covenant position and considers the impact of proposed transactions upon our banking covenants to ensure that they are not breached. It also has regular (no less than twice yearly) meetings with its banking providers to ensure that any potential issues or risks are identified and communicated early and that any implications for covenants can be addressed. The Group has remained in compliance with its banking covenants in 2022 and expects to continue to do so. The impact of IFRS 16 'Leases' is ignored for the purpose of our banking covenants.	Decreased

Risk management and principal risks continued

Unchanged Increased Decreased

Nature of risk	Mitigation and progress	Change
Financial risks continued		
Currency risk		
The Group has contracts with overseas customers and suppliers requiring payment or receipt in currencies other than sterling (in the UK) and euros (in Germany and Portugal). The Group's exposure to credit risk at 30 April 2022 in respect of financial derivatives (forward foreign exchange contracts) was £10.7m of payable and £23.8m of receivable (2021: £5.9m of payable and £17.5m of receivable). The financial derivatives at 30 April 2022 were held with NatWest and Investec Bank (30 April 2021: NatWest and Investec Bank). These are disclosed in detail in note 18 to the financial statements.	The Group manages its exposure to currency risk by using forward foreign currency exchange contracts. The level of forward cover is determined on an individual contract basis, taking into account the net currency exposure to receipts and purchases. Forward contracts are only put in place when the award of customer contracts has taken place or is considered highly probable. There is a risk of weaker margin or bid loss if exchange rates materially deteriorate from the Group's perspective between bid and contract. There is also an opportunity of margin improvement from favourable exchange rate movements in the same period. The Group does not enter into speculative forward exchange contracts. At 30 April 2022, the Group's primary foreign exchange contracts were to cover exposures to the US dollar at SEA, which has a number of sales in US$ and increased euro buys for supplies, mainly at MCL. The Group does not hedge the exposure to euro/sterling fluctuations that arise from its ownership of either EID or ELAC. The currency risks the Group faces have increased, especially in respect of the US$ requiring the Group to review more regularly its supplies to be paid in foreign currency. The stronger US$ against the pound sterling, if it persists, should improve the Group's competitive position in US$ based markets.	Unchanged
Revenue		
The Group has risk in respect of: i. milestone and acceptance failure on projects; and ii. unrecoverable trade debts. The recognition of revenue is discussed at length in the accounting policies and critical accounting judgements of the notes to the accounts, and as such, may from time to time have a degree of risk. The 2022 net bad debt charge was £0.2m (2021: £nil) on Group revenue of £137.8m (2021: £143.3m). Financial assets exposed to credit risk at 30 April:	The Group takes a prudent approach to revenue and credit risk, and any work done at risk is minimal, authorised at the appropriate level and reviewed on a monthly basis. The Group uses project control processes and regularly reviews project progress to ensure recognition of revenue takes account of external milestones and customer acceptance as well as the internal costs incurred. The calibre of the Group's customers and the control processes in respect of revenue capture and invoicing ensure minimal bad debts. The Group also uses letters of credit and other methods of payment guarantee, including customer advances, especially in respect of overseas customers, to ensure any export debt risk is minimised. Significant debt receivable in foreign currency is hedged using forward exchange contracts. The credit risk of the major debtor of the Group, the UK MOD, is considered very low. The Group's risk to trade receivables is higher in some of our non-defence markets where our customers are not all government bodies. The Group also has a risk, even for government business, where we contract via a prime contractor. This risk has been low historically, especially in the defence sector, but collapses such as Carillion in the past highlight that prime contractor risk needs to be monitored. The cash and bank deposit risk is discussed under Treasury above.	Unchanged

	2022 £m	2021 £m
Trade receivables	**24.4**	30.2
Other receivables including contract assets	**31.8**	36.4
Cash and bank deposits	**40.4**	32.3