Strategic RISK

European risk and corporate governance solutions

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[January 2012]
Issue 75 €25

NEWS & ANALYSIS » Another UK bribery scandal » Thailand floods cost billions » The round-up of our SR100

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[SUPPLY CHAIN] How robust are your suppliers, their suppliers … and the suppliers behind them? Our four-page special section explores all the issues

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UNKNOWN UNKNOWNS

Political, economic, security and criminal risks are on the rise like never before. But how do you prepare for the risks you can't see coming?

Ethics
Soft risks are hard to measure but they can still cripple companies

Bribery index
New data on the companies and countries most likely to pay bribes

A cautionary tale
Is there anything that corporate risk managers can learn from the banks?

StrategicRISK

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Nathan Skinner,
EDITOR,
STRATEGIC RISK

WELCOME

Prepare for everything else

I WAS READING BLOGS ONLINE RECENTLY AND CAME ACROSS ONE called 'Software Disasters Blog'. It has a nice strap-line, which I think is equally as relevant for risk managers as it is software engineers: "Prevent what you can, prepare for everything else." Pretty neat, huh?

It sums up the approach that the best organisations take to risk management. You do the best you can to manage down risks to an acceptable level, while at the same time preparing for what might be around the corner.

That's certainly the message I got recently when we arranged for the UK's top risk managers to get together for the Risk Retreat, a one-day event for peer-to-peer networking, learning and socialising. We've had some fantastic feedback, and thanks to everyone who made it along. You can read about it here: goo.gl/NalMW. We're planning to launch similar events elsewhere in Europe soon, so watch this space.

You do the best you can to manage down risks to an acceptable level, while also preparing for what might be around the corner

It's not exactly trendy to learn from the banks at the moment. Not only did their shocking risk management capabilities lead to a crisis that almost destroyed the financial system in 2008, but they are also partly to blame for the sovereign debt problem shuddering through Europe right now.

Yet I suspect there are still some things that companies can learn from financial services firms. This could include making sure the levels of controls put in place to manage a risk are actually proportionate to the threat it poses to the business. We asked Giles Triffitt, formerly head of risk services at The Royal Bank of Scotland (admittedly one of Britain's failed banks, but we can't blame it all on him), to explain how to match control spending with the underlying risk. Hope you enjoy the issue. **SR**

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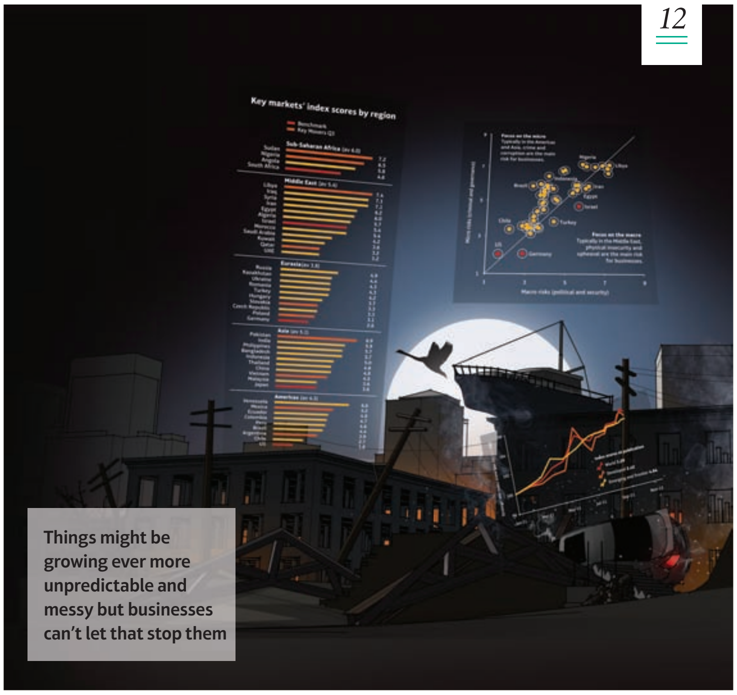

Things might be growing ever more unpredictable and messy but businesses can't let that stop them

Suppliers' poor practices or working conditions can result in damage to your business's reputation

News & Analysis

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Risks

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Supply chain risks

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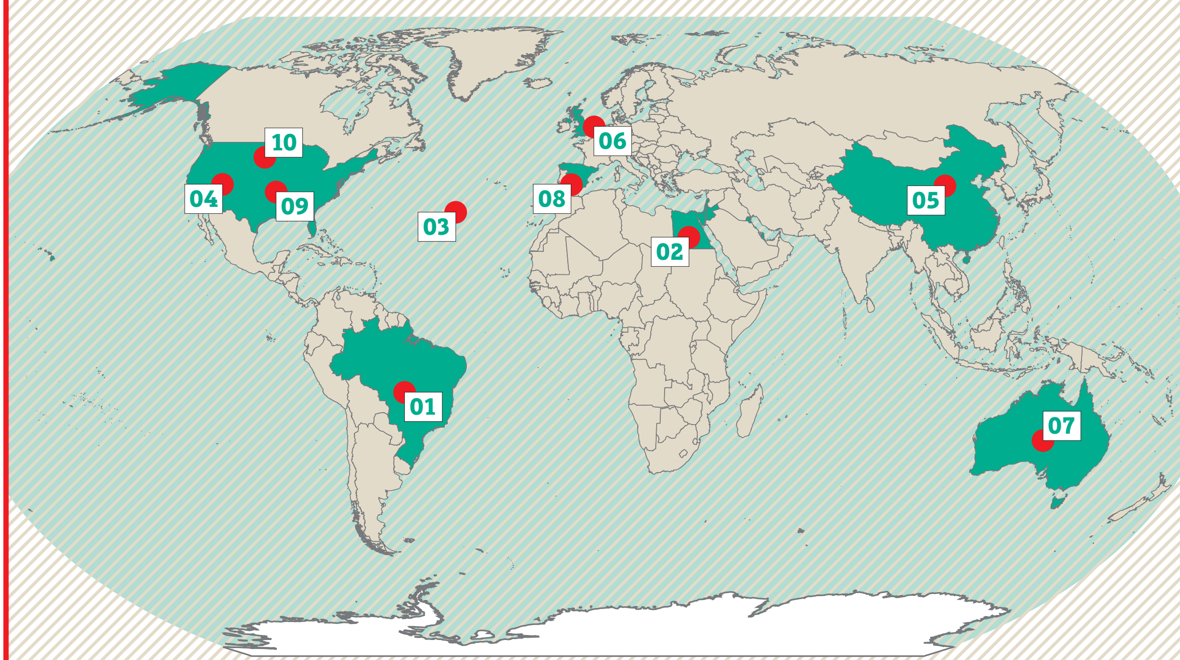
Top 10 essential online stories



01 LATIN AMERICA

Eurozone crisis spreads to Brazil

The eurozone crisis is spreading to Brazil via Spain and Portugal, which have close ties to the Latin American giant, says Exclusive Analysis. If Spain or Portugal default on their debts, companies may sell Brazilian assets to raise capital. Writedowns against European sovereign debt could mean Spanish bank Santander, Brazil's fifth-largest bank, losing market share. Brazil's car and telecom companies are also threatened if Telefónica's Vivo and Fiat lose market share. But there are opportunities: Brazilian banks could invest in Angola as Portuguese banks leave.

web. *goo.gl/ksYC5*

02 PEPS

Focus on political risk intensifies

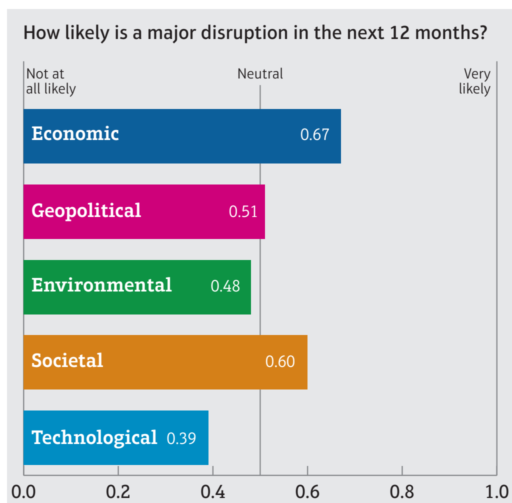
Financial services are significantly increasing their focus on politically exposed persons (PEPs) after the Arab Spring uprisings, say anti-money laundering experts. Organisations became more aware of the PEP threat since the uprisings in several countries forced them to tighten political risk controls. PEPs are individuals linked closely to a prominent public function and therefore with a higher than normal vulnerability to bribery and corruption. The number of institutions with formal processes to identify and monitor PEPs has increased from 71% in 2007 to 88% today, KPMG's anti-money laundering report found. KPMG sees the greater awareness as an encouraging sign.

web. *goo.gl/YmP9C*


Reuters

03 GLOBAL ECONOMY

WEF survey finds a dip in economic confidence



Leading risk experts' confidence about the state of the global economy has dipped, according to the World Economic Forum's Global Confidence Index. Among 1,000 experts questioned for the index, 70% remain pessimistic about the global economic outlook. Concern about a major societal disruption being likely or very likely to occur over the next 12 months has grown from 50% to 60% this quarter. But the index also shows that there is higher optimism for global co-operation to address these risks. One-third of the respondents expressed confidence in the state of global co-operation, compared with one-fifth three months ago.

web. *goo.gl/pe0Ep*

04 DATA SECURITY

Apple's security could be compromised by new bug

Hackers could use a new bug in Apple's operating system to access personal data on its devices. IT security vendor Cryptzone warns that the revelation might compromise the security of iPhones, iPads and Apple Mac computers. The bug allows apps to be turned into malicious software, making the danger hard to detect. "Now that the cyber-criminal community knows that it is possible to compromise iTunes and the iOS platform, you can guess what is going to happen," Cryptzone vice-president Grant Taylor said. The bug was found by software developer Charlie Miller. Apple terminated his developer licence shortly after he revealed details of his research.

web. *goo.gl/XleJg*

05 CYBER CRIME

Cyber attacks reach 'disturbing' levels

Criminals are increasingly using the internet to steal information, says the UK's GCHQ spy centre chief Iain Lobban. Companies, particularly those in defence, are targeted by cyber criminals and even governments. "I can attest to attempts to steal British ideas and designs – in the IT, technology, defence, engineering and energy sectors, as well as other industries – to gain commercial advantage or to profit from secret knowledge of contractual arrangements," Lobban said.

web. *goo.gl/3sxKn*

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06 FTSE 100

Directors' pay leaps 50% in one year

Company bosses are being rewarded with large pay rises, despite it being a time of economic stagnation. Pay for directors at FTSE 100 companies rose by about 50% last year, according to research company Income Data Service. This amounts to a rise of €3.17m per director over the year. Finance directors received an average increase on their bonus of 34.1%, all the other directors an average of 66.5%. Justifying the rise will not be easy for companies. Unite Union's general secretary Len McCluskey even called the pay rises "obscene". "The government should strongly consider giving shareholders greater legal powers to question and curb these excessive remuneration packages," he said. "Institutional shareholders need to exercise much greater scrutiny and control of directors' pay and bonuses."

web. *goo.gl/00HJv*

07 BUSINESS

Mining and metals: top risks listed

Resource nationalism, skills shortages and infrastructure head the top 10 business risks facing mining and metals companies, says an Ernst & Young report. In "a snapshot of the most significant challenges facing the sector", resource nationalism (whereby a nation or state seizes corporate assets) is the top risk, as "governments continue to make demands in order to increase their slice of the profit pie", says the report. Fraud and corruption has also moved up the ranking (to number 10). The report is available online.

web. *goo.gl/VBPzP*

Top five risks facing mining and metals 2011–2012

1. Resource nationalism
2. Skills shortage
3. Infrastructure access
4. Maintaining a social licence to operate
5. Capital project execution


Reuters

US secretary of Treasury Timothy Geithner (left) with France's president Nicolas Sarkozy at the G20 Summit in Cannes

08 BAILOUT FUND

Eurozone deal 'one step' to fix sovereign debt crisis

European banks may cut their lending to meet new capital requirements in the face of the eurozone deal. A heads of state meeting in Brussels last month reached an agreement to increase the size of Europe's bailout fund to €1 trillion. They also decided to order banks holding Greek debt to accept a 50% loss. These decisions will pose a "major challenge" for European banks, said PricewaterhouseCoopers. There is a danger that some banks attempt to meet it by cutting lending instead of raising capital. According to the European Banking Authority, of the €106bn shortfall, €79bn is attributable to the eurozone's 'peripheral' economies, with Greece (€30bn) and Spain (€26.2bn) topping the list, followed by Italy (€14.7bn), France (€8.8bn), Portugal (€7.8bn) and Germany (€5.2bn). The full effect on individual institutions is not yet clear, said PwC partner Patrick Fell. "We will have to wait to see the market's reaction before understanding the implications for other eurozone countries."

web. *goo.gl/cjjxw*

09 CATASTROPHE

Oklahoma rocked by biggest quake ever to hit the state

Central Oklahoma was struck by a magnitude 5.6 earthquake in November, the largest ever to strike the state, according to catastrophe risk modeller RMS. Aftershocks are likely to continue for months, added the US Geological Survey. The earthquake's epicentre was reportedly southeast of Lincoln County, yet it was felt as far away as Cleveland, Ohio and Pennsylvania (more than 900 miles away).

Damage was relatively slight, with minor damage to 12 homes and a buckling of three sections of US Route 62 reported. "Oklahoma appears to have had a phase of heightened seismic activity since 2009 in terms of the frequency of earthquakes recorded in the state," RMS said. "The intensity of these tremors, however, is in line with what is deemed normal seismic activity."

web. *goo.gl/uxBTY*

10 SURVEY

Commercial lines premiums starting to rise, says survey

Eight years of falling commercial insurance rates might be at an end, suggests a survey by RIMS. The survey tracked changes in average programme renewal premiums for directors' and officers' liability, general liability and property and workers' compensation. It reveals that average renewal premiums in three of four lines of business tracked rose in the third quarter. Advisen's Research Division president Dave Bradford said: "Indications have been strong over the past couple of quarters that the market was near bottom, so it's not surprising to see premiums drifting upward a bit now." While directors' and officers' liability fell 1.9%, general liability rose 1.2%, property 1.6% and workers' compensation 2.1%.

web. *goo.gl/yIL2Y*

Online contents

Most read stories

Eurozone crisis: The UK insurers with the most to lose
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SR100 debates global risk implications
web. *goo.gl/9vzGp*
Video: Understanding the risks you can't quantify
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Annual protest in Athens
web. *goo.gl//0o4eB*

Comment

Did a Harvard professor cause the economic crisis? Could ideology taught at Harvard University have contributed to the poor state of the financial system?
web. *goo.gl/9EHGK*

"Risk managers need to be aware of the techniques and tools that criminals can use against them." KPMG's new director of risk consulting Paul Evans
web. *goo.gl/k6qR0*

CRISES

Monsoon blues

The devastating floods in Thailand have left hundreds dead and many corporate supply lines crippled

THIS YEAR'S MONSOON SEASON WAS THAILAND'S WORST IN 50 YEARS, leading to devastating flooding, which by late November had claimed more than 600 lives and cost the country as a whole an estimated $30bn (€22bn).

From a business perspective the flooding has crippled many corporate supply chains, in particular for the automotive and electronics industries.

Research just published by Aon Benfield said the catastrophe has had a "cascading effect" on the automotive, electrical appliance and tourism industries.

It comes as a double blow for those organisations that have or had assets in Japan and were affected by the earthquake triggered nuclear disaster there in March.

Many businesses with interest in the Far East hit by the Japanese catastrophe actually moved their production to Thailand as a way of ensuring continuity of supply. But now that mother nature has dealt another blow to the region, with Thailand's floods, these businesses find themselves in the line of fire once more.

RPC Legal Director in Reinsurance and Corporate Insurance Daniel Saville said that business interruption insurers will face a sharp and potentially devastating increase in claims as a result of these natural catastrophes hitting two large manufacturing centres over such a short period.

The scale and the duration of the Thailand floods will lead to insurance disputes over claims, he believes, adding that insurers could seek to exclude claims where structural or design defects led to buildings collapsing. Local media quoted Allianz's chief executive for global corporate and specialty in the Asia region Lutz Fullgraf as saying that the event would be the largest flood insured loss in many years, possibly ever.

Fullgraf suggested that this event will turn out to be a larger economic loss to Thailand than the 2004 tsunami or the riots in Bangkok last year. Broker JLT Re estimated an insured loss from the Thai floods of up to $13bn, while Thailand's insurance commissioner estimated $30bn in economic losses for the country. **SR**

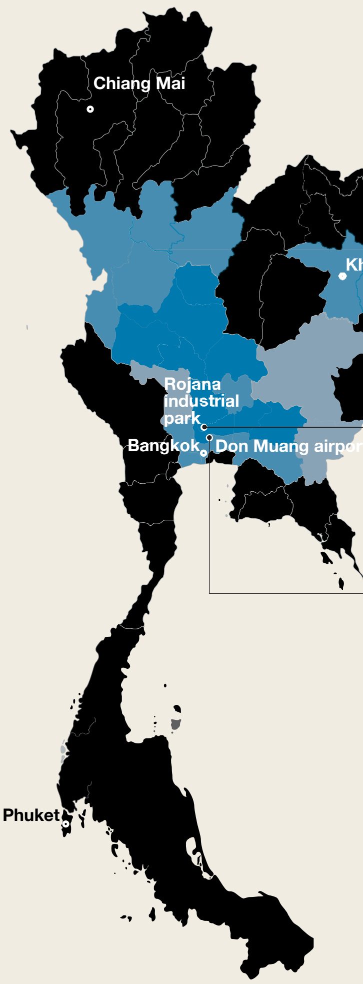
Reuters

Floods in Thailand have been devastating for the country

Thai floods

Thailand's outsized importance in global supply chains was exposed when devastating floods in the country hit several key industrial sites. The worst flooding to hit Thailand in five decades began in July and at the time of going to press one-third of the country's provinces had been declared disaster zones and around one-fifth of the capital Bangkok was under water.

Flood affected regions

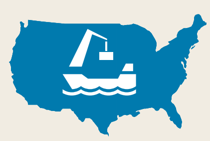


100,000 vehicles may have been lost because of the shutdown of Rojana industrial park in Ayutthaya, one of the most heavily affected areas.

On 25 October, the flood waters breached the barrier protecting Bangkok's second largest airport, Don Muang; commercial flights had to be stalled.

€22bn

Estimated total economic loss



Exports to US hit

It's not just the hi-tech world that will be affected by the floods in Thailand. Intelligence provider Pamjiva studied vessel shipments coming out of Thailand into one of its main markets, the USA. The pie charts on the right give a snapshot of the number of different products affected. The impact of the floods in Thailand will be felt by companies who sell or use these products — because they will have to scramble for supply and likely pay higher prices — and also by consumers.

Affected industries

Transport
Thailand's Department of Highways reported:

535 highways
were flooded

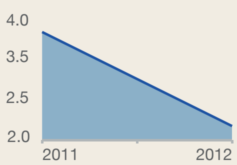
67 roads
listed as destroyed in 16 northern provinces. The economic cost to highways alone was listed at around $163m.

Car manufacturing
The automotive industry is one of the most heavily affected industries. The floods in Thailand have had a major effect on local automotive production and supply chain, causing a large number of disturbances.

Electronics
Flooding affected the production of several key electronic components, most notably car components, cameras, semiconductors and hard disk drives.

The floods are predicted to decrease sales of hard disk drives by 20 million, leading to a 25% hike as demand outstrips supply.

Economic impact
Thailand's Finance Minister expects a negative growth of 1.1% for the fourth quarter GDP. The full-year GDP growth estimate was cut from 3.7% to 2%.



Insured losses
Thailand's Office of Insurance Commission said that insurance claims from the floods are already in excess of $3.3bn. Japan's casualty insurers may face around $2.5bn in payouts to cover damages, according to Deutsche Bank.

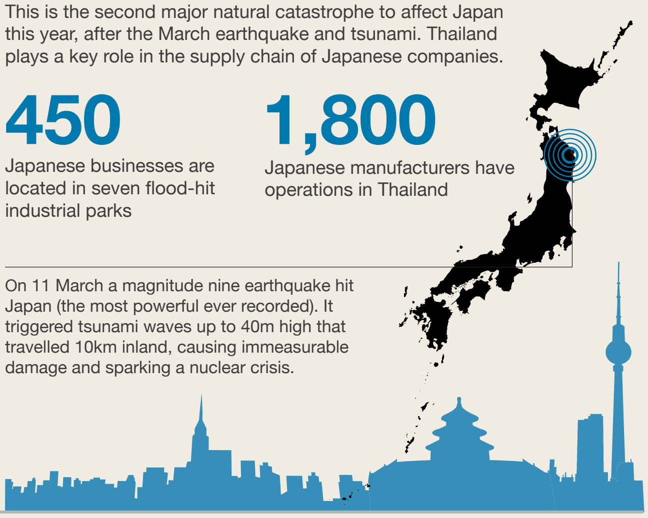
$3.3bn total claims
$2.5bn covered by Japanese insurers

Double blow for Japan
This is the second major natural catastrophe to affect Japan this year, after the March earthquake and tsunami. Thailand plays a key role in the supply chain of Japanese companies.

450
Japanese businesses are located in seven flood-hit industrial parks

1,800
Japanese manufacturers have operations in Thailand

On 11 March a magnitude nine earthquake hit Japan (the most powerful ever recorded). It triggered tsunami waves up to 40m high that travelled 10km inland, causing immeasurable damage and sparking a nuclear crisis.



26% Rice (52,891 shipments)
10% Furniture (24,580 shipments)
27% Shrimp (46,097 shipments)
25% Pineapple (23,209 shipments)
32% Coconut (31,431 shipments)

NB: Figures are a percentage of total shipments going into the USA.

By the numbers

46% North Thailand saw this much more rainfall than average from January to September

2.8m Number of homes that sustained various levels of flood inundation

14,800 Industrial and manufacturing plants damaged

20 Provinces affected

42% of factories damaged in Ayutthaya province, one of the most heavily affected areas, damaged (900 out of 2,150 factories)

602 Fatalities, according to government figures. Around half a million people are living in temporary shelters

Source: Thailand Floods: An Event Update, Aon Benfield

MEGA RISKS

Top five
[EXTREME RISKS]

1. **Depression (low risk, high impact):** A deep and protracted trough in GDP, caused by ineffective growth policies.
2. **Sovereign default (very low risk, medium impact):** A major developed country's default could lead to a return to a gold standard.
3. **Hyperinflation (very low risk, high impact):** Intensely bad for asset returns.
4. **Banking crisis (very low risk, medium impact):** When bank balance sheets cannot absorb another shock. The interconnected modern financial system means that the insolvency could quickly become systemic.
5. **Political crisis (Low risk, medium impact):** The extreme risk for democracies is that public anger gives power to a protectionist political party. For non-democracies, the risk is violence.

Source: Towers Watson

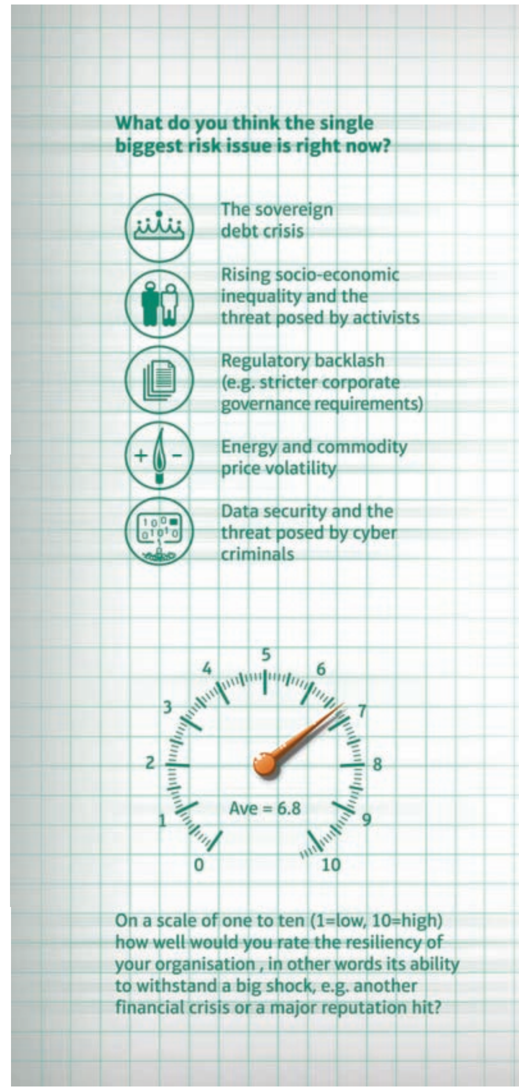
OVERHEARD

"Soundbites"

"The biggest risk I've ever taken was marrying my wife."
Lennart Edstrom, vice-president of group risk management, Electrolux
>> see **Headspace** page 40

"A career in risk management provides the opportunity to explicitly do what everyone intellectually knows must be done."
Hans Læssøe, senior director, strategic risk management, LEGO System A/S
>>see **Viewpoints** page 15

"Even in a first-world country that seems well prepared and organised, a natural catastrophe can be very disruptive."
Jorge Luzzi, president of Ferma and director group risk management, Pirelli
>> see **Special Report** page 28



FORUM

Risk managers must lead in a changing world

The StrategicRISK *100 Risk Retreat tackled failing democracy, the shift in economic power to the East, cyber threats, and the need to give something back*


Corbis

Democracy is failing?: Protests on the two-month anniversary of the start of 'Occupy Wall Street'

RISK MANAGERS SHOULD LEAD the drive for corporations to react to changes in political and economic pressures, as well as tackling emerging and potentially very costly cyber risks. These were among the key messages delivered at the *StrategicRISK* Risk Retreat in November.

Julian Radcliffe, OBE, a founder of Control Risks, opened the panel debate by saying that democracy is clearly failing. "Countries like China are struggling to move to a semi-democratic system, while democracy has failed dramatically in some countries in southern Europe," he said. "As a result, such countries are calling for technocratic leaders with no obvious political bias to save them from ignorant politicians with a stupid voting record."

Coupled with political uncertainties is the huge shift in global economic influence to the Far East. Radcliffe said that India and China could become the world leaders in the same way that the USA and Russia dominated in the past. He did not believe that the result would be open warfare because of the existence of the nuclear deterrent, "but smaller conflicts will escalate and crime will increase", he predicted.

With government spending under pressure, public services in sectors like health, education, transport, policing and defence will be heavily constricted. Radcliffe considered that the corporate sector is in a very strong position to step in.

"Those of us who have a key interest in aspects such as fraud and patent protection and cyber security cannot rely on government doing much for us. Already insurers are funding payment of over 50 policemen to tackle stolen construction equipment and fraud," he explained. "Risk managers should take a significant lead, working together to identify relevant areas for partnerships with the public sector."

Similarly, large corporations should require their employees as individuals to contribute to their communities. "It would be good if every individual's career appraisal included a section on what they had done to support the wider corporate responsibility to society," he suggested.

"I would like to see more public/private partnerships, with risk managers taking the lead, and companies enabling their employees to put more into society so that it moves in the right way with the right calibre of people," he concluded.

'Every individual's career appraisal should include a section on what they had done to support the wider corporate responsibility to society'

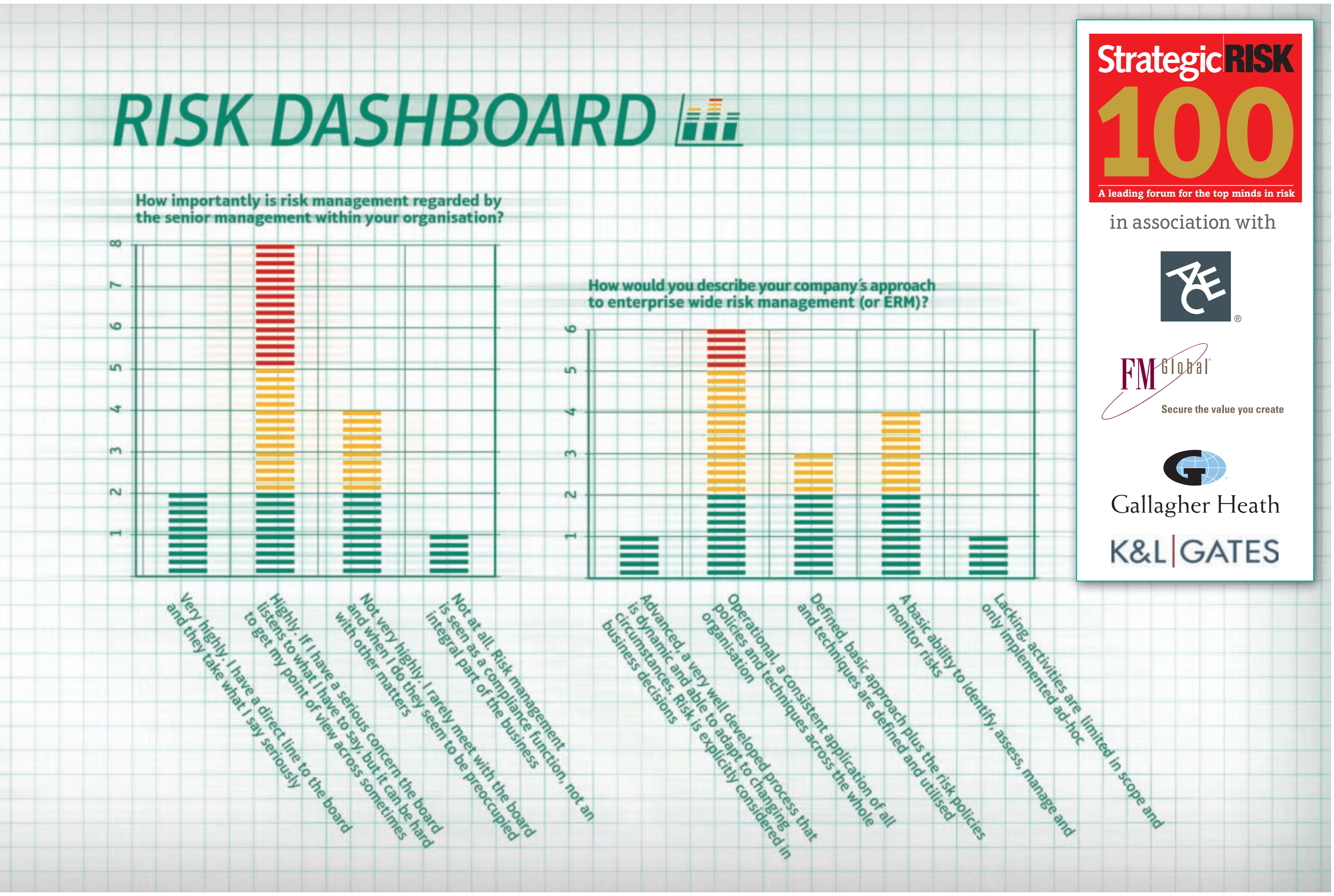
Julian Radcliffe Control Risks

Demographic issues

"The combination of rapid growth of population in emerging economies and rapid expansion in living standards is going to be putting significant pressure on global resources," warned Barclays Capital chief European economist Julian Callow.

Despite western problems, he expected the global economy to continue to grow, although recently most of this growth has occurred in the emerging economies. "In Asia, Africa, the Middle East and South America, rapid growth in population and a very significant improvement in the institutional governance structure in many of these regions is being followed by rapid productivity growth and an increase in standards of living," he said.

The result will be considerably increased pressure on resources. For example, in China current annual oil consumption per capita is about two barrels, compared to around 12 barrels in Europe and 22 in the USA. There are around 45 vehicles per 1,000 people in China,



Above: A sample of views from the StrategicRISK 100, a leading forum for the top minds in risk

compared to 650 in Europe and 850 in the USA. As rising living standards allow the emerging economies' consumption to catch up with that of their western counterparts, Callow predicts huge pressure on resources, particularly food and energy.

In other countries, demographic concerns are very different. "For example, in Europe our population is likely to be quite static but the number of people over 65 is growing substantially, with the working population reducing by a similar figure. This will result in a large transformation in society," Callow warned.

Recent events have also demonstrated the importance of financial market trends on the economy. "Equity market valuation accounts for a large share of GDP and recent price fluctuations have had a considerable impact on investors' confidence," Callow said. "And developments in financial markets and economies are very synchronised now because of the effects of rapid communication through IT."

Debt spreads

He also discussed the problems arising from recent rapid expansion in debt in Europe and the USA, both in private and public sectors. While the private sector in the last two years has taken steps to deleverage and reduce the amount of debt in relation to income, public sector debt is still generally rising and thus increasing the overall growth of debt.

Detica technical director Henry Harrison highlighted USA and UK governments' growing focus on cyber security strategies and related investment, particularly in relation to national security.

He pointed out: "Companies have become more dependent on IT and connected electronic devices for everything they do, which has raised the stakes for all of us. If something goes wrong, it has a bigger effect than before – and our adversaries also recognise that targeting our IT systems has become a more effective way of achieving their objectives."

Cyber risks are enhanced by the fact that the cyber environment differs from others; it is not defined by geographical borders. "Information flows seamlessly between countries and individuals and businesses are right in the front line," Harrison said. **SR**

Forms of cyber crime are many

1. **The known 'traditional' cyber risks of credit card fraud, viruses and other malware**
   This can lead to business disruption and financial loss.
2. **Activists targeting specific sites to cause disruption, financial loss, brand and reputational damage**
   In some cases, this can threaten the viability of the online business concerned.
3. **Cyber warfare and cyber terrorism**
   There have been a few examples, most notable recently being the Stuxnet worm. Cyber terrorism is also a concern, but is as yet hypothetical.
4. **Cyber espionage**
   This involves theft of commercially sensitive information, with some incidents being reported by the chemical, oil and gas industries in particular.

Corbis

Soaring concerns: Allegations of bribery by aerospace company EADS came just months after the implementation of the new UK Bribery Act

BRIBERY

Business as usual …

Claims that a defence company with UK links bribed officials to secure a Saudi contract has left the UK with another potentially embarrassing dilemma

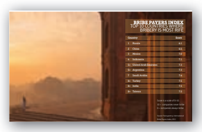
REPORTS THAT A PROBE BY THE UK Serious Fraud Office (SFO) into bribery allegations against a defence company with British links is being delayed – and might even be stopped – while the UK government considers the political implications, have provoked outraged comment.

The investigation centres on allegations that GPT, a subsidiary of European aerospace company EADS, paid bribes to Saudi Arabian officials over a £2bn (€2.32bn) communications contract. Whistleblower Ian Foxley claims GPT sacked him after he told the fraud office the company had given Saudi officials luxury cars, jewellery and briefcases full of cash. According to the *Sunday Telegraph*, a crucial part of his evidence rests on claims that £11.5m was sent to offshore companies in the Cayman Islands and then to a Swiss bank account.

The case is an embarrassing reminder of the SFO's 2006 inquiry into allegations of bribery against BAE Systems involving Saudi Arabia. The UK government halted the investigation after alleged Saudi threats to cease co-operating in counter-terrorism.

Also, it is just months since the UK Bribery Act came into force, widely acknowledged to rank among the most stringent anti-corruption legislation in the world. If applied to the GPT case, the SFO would have greater freedom to decide whether to continue its probe. But the new Act only covers offences occurring after 1 July this year so the less flexible provisions of the earlier Corruption Act apply.

According to McGuireWoods partner Adam Greaves, the real catalyst for the drafting of the Bribery Act, passed in April 2010, was the embarrassment caused to the UK from blocking the BAE investigation.



For the top ten bribe-paying companies and countries, go to our Governance section page 33

Government support needed

Non-governmental anti-corruption organisation Transparency International UK is calling on the government to support a full SFO investigation into the GPT claims. The NGO says the UK's anti-corruption record is under scrutiny by the UN, the Council of Europe and the Organisation for Economic Co-operation and Development (OECD). Under Article 5 of the OECD Anti-Bribery Convention, a state cannot allow political, economic or diplomatic considerations to interfere with the investigation of foreign bribery cases.

Transparency International UK executive director Chandrashekhar Krishnan says: "If the SFO believes it has a strong case, it is vital that it is allowed to investigate and, if necessary, prosecute without political interference. "We would expect EADS, as a leading member of the international defence industry's own anti-corruption initiatives – such as the Common Industry Standards for Anti-Corruption and IFBEC [International Forum on Business Ethical Conduct] – to co-operate with the SFO and undertake a thorough internal investigation.

"The UK government's decision will be closely watched by any corrupt company and government overseas looking for an excuse to continue business as usual. It is imperative that the government sticks by the international rules and ensures this investigation goes ahead."

Greaves says: "A decision to stop the SFO's investigation would clearly be enormously embarrassing to the UK government and damaging to the reputation of the UK as a whole on ethical standards. But, given that the UK economy is in a parlous state and the government's own finances are dire, to investigate and prosecute alleged defences in relation to the EADS/GPT contracts could be enormously damaging to Britain's significant business relationship with Saudi Arabia," he says.

The US angle

While UK attorney-general Dominic Grieve considers his decision, US involvement lurks in the background. The US regulator, the Securities and Exchange Commission, is reportedly looking at evidence that suggests alleged bribes to a Cayman Island company were paid via a bank in New York for what was described as "bought in services". The *Sunday Telegraph* says: "Movement of funds through the US mainland could bring the alleged wrong-doing under US jurisdiction."

Greaves agrees that there could be a US angle to this corruption investigation. Certainly the US authorities continued to pursue BAE Systems even after the UK had dropped its own investigation.

Greaves believes that dropping the GPT probe will send the wrong message to other potential whistleblowers. Foxley's claim for constructive dismissal case against his former employers failed. Since GPT was registered in Saudi Arabia, the case could not be heard under British law.

Blogging on the Bribery Library website, Greaves considers it likely that the intelligence-sharing agreement will be "trotted out again" by the UK attorney-general as a reason not to pursue the investigation. "British jobs and foreign faces will be saved but British justice will take another body blow," he says. **SR**


1
My Advice:
Partnership allows big things to happen.
Allure of the Seas
Jason Liberty, Vice President
Royal Caribbean International®
Corporate and Revenue Planning & Insurance
Know more. Achieve more.
Creating the world's largest cruise ship requires a trusted partner. That's why Royal Caribbean International® trusts in the expertise of Allianz Global Corporate & Specialty – covering the most complex business risks worldwide.
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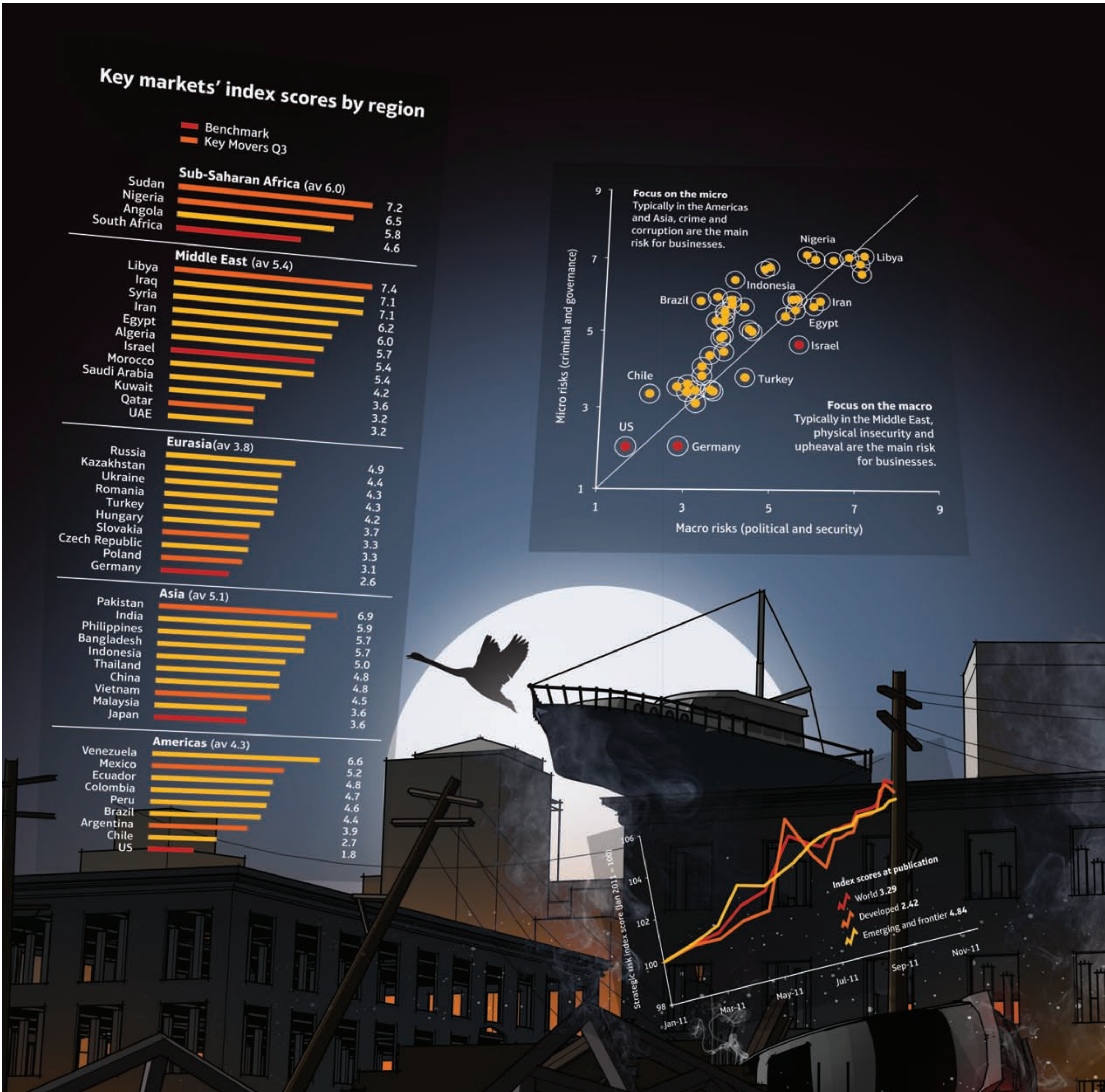


Emerging world risks

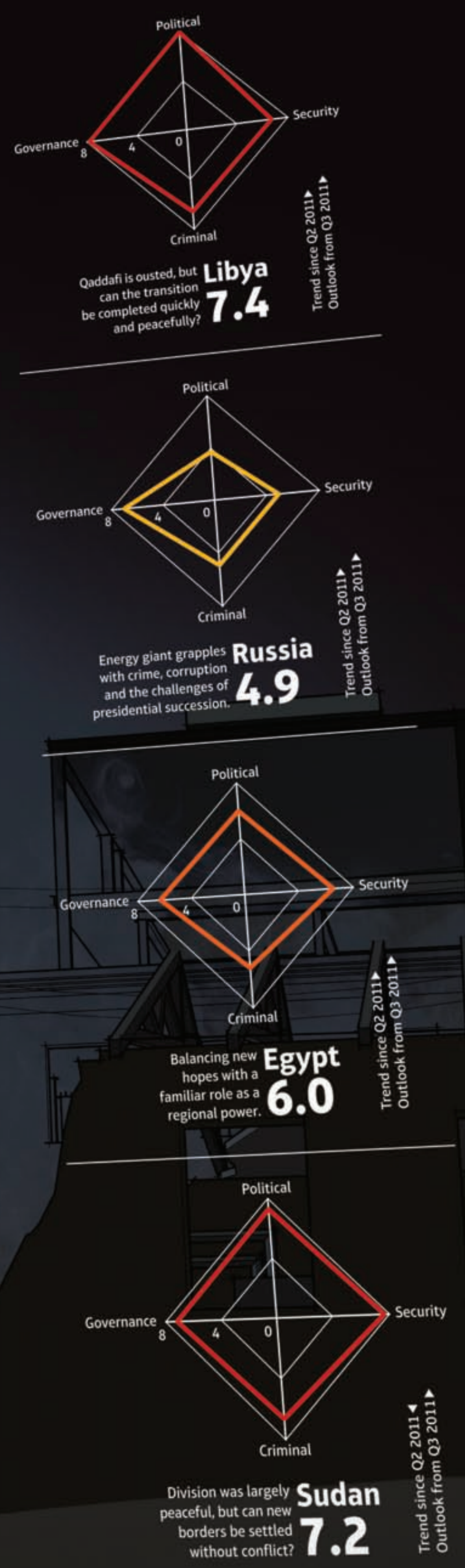
These charts quantify the level of risk faced by businesses operating in the leading emerging markets. Index values are standardised on a scale of one to 10, with one the safest and 10 the most risky

Source: Aegis Advisory and Integro

ECONOMICS

Steady as she goes

In these changing times, one of the few things anyone can be sure about is that uncertainty will continue. But while risk exposure for business is growing, it's not all doom and gloom



Key points

01: Risks are more unpredictable than ever, but companies cannot let this stop them going out and doing business

02: Inflation/deflation, sovereign defaults and food price pressures are all leading to greater volatility

03: Investors should actually buy not sell when an inevitable sovereign default is announced

04: The economic sustainability of China's growth is still under question, due to its reliance on the buying power of Europe and the USA

05: The future will either see governments absolve themselves of responsibility, or businesses will become more creative

POLITICAL AND ECONOMIC INSTABILITY AROUND THE world is increasing risk exposure for businesses. According to research by Aegis Advisory and Integro, 'strategic risks' (political, economic, security and criminal risks) have increased five percentage points this year. "Political and security risks accounted for most of the increase. And the increase in the level of strategic risks in the Middle East has been large. But there is instability across the board," says Aegis Advisory assistant director of risks Mal Bozic.

He says that the current turbulence is challenging but also believes businesses can't just bury their heads in the sand: "It's a bit like going surfing. You can't stay on the beach until the waves get comfortable enough to ride. You have to get out there and ride them, even though they are unpredictable and messy."

It's clear that most companies are paying more attention to risk than they were a couple of years ago. Developments in the eurozone or the Arab Spring are confirmation of how unstable the world has become in recent years. Risks are also becoming increasingly harder to predict and mitigate against.

Principalis Asset Management president and founder Pippa Malmgren specialises in understanding risks that can't be easily quantified. She lists some of the pressures facing the world economy: "We have the risk of inflation versus deflation, and the high probability of sovereign defaults including municipal defaults in the USA, which I think are very likely to occur," she says. "Now you also have food inflation pressures, which lead to political instability and civil unrest issues in emerging markets, all of which starts to deteriorate the productivity of those emerging markets.

"All these things tell me that volatility ought to be higher," adds Malmgren. "And that will affect all sorts of asset classes. We'll see this in particular in commodities. Brands are very powerful in this new environment. You want to own brands that have the capacity to pass on higher costs because I think higher costs are inevitable."

Inevitable defaults

This scale of uncertainty makes life hard for risk managers. But nowhere is uncertainty more monstrous than in the European sovereign debt crisis. Commenting recently on the eurozone crisis, Malmgren said: "I think we're going to have sovereign defaults, I think that's unavoidable. And that's been my view since the beginning of the financial crisis. "What we [governments] did was to »

» take the losses that were on the banks' balance sheets and move them onto the governments' balance sheet. But that doesn't diminish the loss. It still has to be paid for. The round of austerity that we've experienced here in the UK is only round one. Eventually it becomes clear to the political leadership that the cost of defaulting is lower than the cost of paying."

But Malmgren's advice to investors is far from gloomy. "My bottom line is we should buy when the default is announced. Most people will do the opposite, they will see default, get scared and want to sell everything in their portfolio. My view is that once you get default it is like hitting the reset button on your computer. It clears the decks, you start again and now you can grow.

Europe's bailout fund for troubled sovereigns now stands at a staggering €1 trillion. "The European bailout fund was supposedly designed to bail out Greece but what it was really designed for is to bail out the banks if Greece defaults," Malmgren says. "What we now know is that the firewall is working and so maybe companies are a better bet than countries. And that raises some interesting questions for investors. The new risk free rate of return maybe isn't governments. That's something to really think about."

'China is not as safe as it was perceived to be a year ago. There are big questions around dissent and economic sustainability'

Mal Bozic Aegis Advisory

China's own subprime crisis?

China's 'economic miracle', and more importantly the sustainability of it, also raises serious concerns. It is estimated that China needs to sustain economic growth above 8% a year merely to avoid a breakout of widespread civil unrest. There are doubts over its ability to do this in the current climate. "China is not as safe as it was perceived to be a year ago," Bozic says. "There are big questions around dissent and economic sustainability. You always think it had the potential but now we are seeing some symptoms manifest themselves."

China relies heavily on growth in the developed markets to shift the goods that it manufactures, says Bozic. "It's all about linkages. China grows because we in Europe and America buy their products. But we have fewer jobs and less ability to raise debt to buy those products with."

There are signs that China is stockpiling goods and also selling houses to poor families who can't afford them – it could be building up to its own subprime crisis. China's government is even saying that its ability to keep growth high is reaching its limits.

And if China's growth dips it will have catastrophic consequences far and wide. "There is a linear relationship between China, Latin America and Africa," Bozic says. "The great strides of progress in these other emerging markets could not necessarily continue on the current trajectory if China's economy doesn't continue to grow," he says. "If Brazilian growth rates drop, it could lead to considerable unrest in the favelas." Seen in this context, it's easy to see how China lending money to help Europe's ailing economies – as has been mooted – is in its interest, because it gives China the option to grow out of its problems.

The risk is not knowing how the economic situation will play out, warns Bozic. So seeking out a better understanding of the issues could help risk managers prepare for the worst. "Mitigating risk through knowledge can help an entity take the risk it wants to take and transfer the ones that it doesn't," he says.

Overall both Bozic and Malmgren are quietly confident about the risk outlook. "I'm optimistic about the future," Bozic says. "I think we will see similar rates of growth in the future to those of the recent past, but in a rebalanced economy in the North Atlantic [Europe, North America]. If the rebalancing [meaning lower wages, which would tend to attract more manufacturing] is successful we could see a new European renaissance."

Two ways out

As for Malmgren, she says: "The environment we're in has two exit doors. One exit door is what you might call the renegotiation of the social contract – that's where the state is defaulting on its citizens. The state says: 'We're not going to pay for the things you thought we were going to pay for anymore and now you've got to pay for it.' Some countries will manage that process smoothly, others will see some civil unrest. It's going to be complicated but that's one way you fix this whole picture."

"The other exit door is innovation and I'm a big buyer of innovation. These pressures I'm describing are so severe and they will compel businesses to be more creative, more innovative, to use their ingenuity in getting back to the bottom line of positive, unimpaired, genuine cashflows. You want to be in genuine cashflows and out of anything that is strictly driven by speculation. That requires some discernment and skill. It's a trickier, more complex environment than we've had for a while." **SR**

Capitalism will continue to reinvent itself

THE OCCUPY WALL STREET MOVEMENT, a loosely organised political movement in favour of reforming or, in some cases, overthrowing the status quo, is gaining strength around the world from New York to Toronto, Rome and London.

But the collapse of capitalism remains a remote risk. "The genius of North Atlantic capitalism is its ability to renew and reform itself before it is thrown off in a Russian or Soviet style," says Aegis Advisory's Bozic.

"Capitalism's response to communism was to institute workers rights and the weekend. You respond by removing some of the excesses of the system. Right now, in the UK, we have a centre-right government agreeing with some of what the anti-capitalist movement is saying. Our political systems are responsive and able to respond before the masses get the pitchforks out."

Viewpoints

[PEOPLE]
[OPINION]
[COMMUNITY]

PROFILE

Europe's risk leaders

As we enter a new year, 10 leading risk management professionals reveal how they reached their current position and their thoughts on a career in risk management

» **ARNOUT VAN DER VEER** chief risk officer, Reed Elsevier

First steps

My background is of a long experience in risk and auditing on an international basis, through different roles in different industries, developing a deep commercial knowledge.

Current role

My role entails a global responsibility for risk driving a business and a growth-focused approach to risk management through pragmatic and solution-oriented approaches. I report to the board and the chief financial officer.

Philosophy

Risk management is a fantastic career opportunity as it gives people a very broad and deep perspective on the business through strategic and operational involvement, dealing with people at all levels in an organisation.

Next steps

We are looking to incorporate some of the more forward-looking aspects of risk management, focusing on scenario planning and strategy setting to enable risk management to be embedded in decision making. Risk metrics is also an important concern. We have a lot of data that we need to structure.

From a personal point of view, it is perhaps a feature of the unpredictable aspect of the life of a risk manager that there is no clear perspective.

Morgan Crucible's Paul Taylor: The job is what you make it, using all your skills and competencies

JULIA GRAHAM chief risk officer, DLA Piper

First steps

Having relevant qualifications, combined with a varied background in underwriting, sales, marketing and general management, I took every management development opportunity available including volunteering for a number of sector roles in insurance and risk management. The bedrock was, and remains, training at the Chartered Insurance Institute – working among highly qualified communities, this has doubtless earned credibility.

Current role

My role is to provide thought leadership and strategic direction in the firm's approach to managing risk and compliance and I see myself as 'owner' of its framework.

Philosophy

Risk management now is a career option – it wasn't when I first started down this route. Certainly the world today is a riskier place and there is a demand for professional, competent people. You need to be qualified in a relevant discipline (business studies, economics, and so on – financial and economic literacy is key) and consider one of the excellent MBAs now available.

Next steps

It's essential to keep learning, keep networking and stay open-minded. Our world is dynamic and so is risk management – you can never say that "it's done".

PAUL TAYLOR director of risk assurance, Morgan Crucible

First steps

I worked with insurer FM Global for 20 years as a chartered engineer. During this time, I moved to the commercial side of the business and was fortunate enough to work in the USA, Australia, Belgium and France. In 1992, I had the opportunity to move into corporate risk management, progressing from insurable risk to enterprise risk management (ERM) and now internal audit, governance risk and compliance.

Current role

My present work has involved evolving the risk management and control framework within the group. As internal audit reports to me, this evolution has included the internal audit process as well.

Philosophy

My philosophy over the years has been to take new opportunities as they arise. The job is what you make it, using your skills and competencies.

Next steps

Retirement is on the horizon but, initially, I would like to work part time, providing consultancy. I am still very much open to new and exciting challenges.

MICHEL DENNERY vice-president of Ferma and deputy chief risk officer GDF Suez

First steps

I trained as a civil engineer and started in operational roles, for example managing gas and electrical distribution systems. Later, I got experience of a wide variety of management jobs before becoming an enterprise risk manager. Because I am always thinking about the future and the organisation, and planning and analysing developments, the risk management role suits my personality.

Current role

My job is to do what's necessary to ensure that every business everywhere in GDF Suez has the necessary competence in risk management.

Philosophy

To be an enterprise risk manager, you need to get a solid grounding in business and management at different levels. It's not an entry-level job.

Next steps

If I make a change, it could be in the direction of a governance role with oversight of all aspects of corporate governance, such as risk reporting, integrity and ethics and internal audit.

GDF Suez's Michel Dennery: I am always thinking about the future and the organisation, the risk management role suits my personality

HANS LÆSSØE senior director, strategic risk management, LEGO

First steps

My current position emerged after a long path. I had 25 years of broad LEGO Group experience covering IT, planning, strategy and finance before I was asked to create this position.

Current role

My work involves implementing strategic risk management using a combination of tools:

- Preparing and discussing strategic scenarios for developing strategy to ensure its resilience.
- Training and supporting a defined risk management process for business projects.
- Driving and supporting the process of ERM to ensure a validly updated ERM database and reporting on overall exposure.

Philosophy

There are uncertainties in everything we do, and hence a career in risk management provides the opportunity to explicitly do what everyone intellectually knows must be done. Further, the concept of uncertainty provides an intriguing angle from which a company can be addressed.

Next steps

I am focusing on further expanding the deliberate use of risk management wider and deeper into the organisation and its processes. A new and broader management team provides me with an improved platform from which to do this.

JORGE LUZZI president of Ferma and director of risk management for Pirelli Worldwide

First steps

I spent three years in the finance department of a pharmaceutical company, and observed that everything seemed to revolve around risk, but there was little analysis of anything other than pure financial risk. But I also could see the limitations of insurance. I started to think that risk wasn't only about the calculation but also the human aspect. When there is a major loss, for example, it's not just the factory building that is affected but also the workers.

Current role

I have wide responsibilities, including as chief executive of our captive and of Pirelli Group reinsurance. For example, I have oversight of our loss prevention, business continuity and global insurance programmes working with our local risk managers.

Philosophy

You have to care – about jobs, the health of the employees, the health of the factories and the health of the business.

Next steps

For the next two years, I will be fully occupied with my job in Pirelli and with being president of Ferma. Longer term, I want to help develop the profession, pass on my experience to others and make the risk management department as important as possible.

»

SPONSORS' WORD

Peter Robertshaw, senior vice-president global marketing, Active Risk (formerly Strategic Thought)

The many faces of the risk manager

This year at Active Risk we've been thinking hard about what makes a risk leader and the resources they need to support them. To build up a profile of today's risk professionals, we commissioned an independent psychometric survey to gain more insight into what makes a great risk manager.

Since launching the online survey in the summer, we have had close to 600 responses from risk professionals around the world in a wide range of industries. We supplemented this quantitative data with interviews with risk leaders.

Perhaps the more traditional view of risk managers is that they should be numerate, analytical, precise and principled. They must show good judgement and be capable of collecting, recording and processing large amounts of data in a methodical way. Risk professionals have to be able to present risk and opportunity information in the context of corporate governance, risk and compliance needs to increasingly senior levels within the business.

But Active Risk's survey results showed that, though the majority of today's risk managers still have characteristics that conform to the stereotype, there are many more dimensions to risk managers than first thought. Sixty percent of the survey respondents have the traditional profile, a grouping we have named the "technicians". The remaining 40% have more "proactive" psychological characteristics not traditionally associated with risk managers.

The "evangelist" group (30%) are natural communicators, blessed with social skills and capable of using an endless supply of argument and charm until a task is achieved. The "drivers" (10%) represent hard-driving individuals who are determined to see a project brought to a successful conclusion.

The next phase of our research will explore the questions that have emerged so far. What makes a great risk team? How do you retain great risk managers? What career paths and education are needed? What are the best communication strategies?

You can still take part in the survey and receive a confidential, personalised report. A summary report of phase one findings can also be downloaded.

For further information, visit: www.activerisk.com/risksurvey

Active Risk | Embrace risk. Build value.

'You have to care – about jobs, the health of the employees, the health of the factories and the health of the business'

Jorgi Luzzi Pirelli

Key points

01: The world is a riskier place today, boosting the importance of the profession

02: As a risk manager, you have the opportunity to explicitly do what everyone intellectually knows must be done

03: Attending seminars is a vital way to meet other practising risk professionals and share thoughts

ALESSANDRO DE FELICE group risk manager, Prysmian

First steps

I moved into risk management from an insurance and brokerage background. Having been a service provider to Pirelli, I joined that company and then, in 2005 when its subsidiary Prysmian was sold, I took on my current role, which I saw as a huge opportunity.

Current role

Normally my activities are directly linked with the assessment of risks, for example contract analysis, and risk financing. As managing director of our Dublin captive, I am also involved in risk transfer and claims management. Currently I am following the ISO 31000 risk management principles and process.

Philosophy

If you are able to communicate to your colleagues the concept that a risk manager can help the company's business, protecting profit margins and business continuity, and they understand this, risk management is a really enjoyable job.

Next steps

I'm hoping for the opportunity to expand my role and my responsibilities by becoming the chief risk officer, which would involve a wider perspective in terms of not only traditional risk management but also ERM.

FREDRIK FINNMAN group risk and insurance manager, Assa Abloy

First steps

My MSc degree in risk management and safety engineering provides a solid academic ground for insurance and risk management within a multinational industry. My background also includes brokerage (with Aon) and underwriting (with Hannover Re).

Current role

On the risk management side I own the policy and process. But the divisions own the risks. I am there to provide tools to manage the risks and safeguard our business goals.

Philosophy

My motivation is to create value to my organisation by ensuring that we can deliver what we promise to our customers and shareholders through a well-functioning risk management process.

Next steps

We are working hard at creating a cultural shift towards risk awareness and management within the organisation. The local companies must understand their risk exposure and that they own the risks themselves. To achieve that, we work through the group risk committee, which is headed by myself, and also through different tools like premium allocation.


Prysmian's Alessandro de Felice: You must communicate to colleagues that you are there to help the business and protect profits

The ECIIA conference discussed corporate governance plans by the European commission and the importance of a committed chairman of the board on governance issues.

Climate change was the main subject for the annual SIRM conference. The association's members called for risk managers to stop dismissing global warming and address the issue.

Italian risk management association ANRA was held in Milan this month. ANRA's president Paolo Rubini urged members to collect more data to help insurers develop innovative responses to new risks.

PAOLO RUBINI corporate risk manager, Telecom Italia

First steps

My university degree in political economy helped me a lot in broadening my view from my initial expertise in insurance. When Olivetti took control of Telecom Italia, I was asked to reshape the company's insurance programme. I took a broad approach with a true risk management perspective, aligning risk transfer with corporate risk appetite and implementing an enterprise risk management process.

Current role

I control risk transfer of insurable risks, included analysis, measurement, treatment, transfer, reporting, claims management and risk engineering. In addition, I support the risk management committee in the ERM process; definition of the corporate risk profile; evaluation of the maturity index of the top risks; monitoring action plans for risk mitigation and their effect on the risk rating; monitoring key risk indicators.

Philosophy

Risk managers should built professional skills over the following pillars: knowledge of risk measurement techniques; knowledge of the company's processes; skills in spreading the risk culture inside the company; knowledge of the insurance business and risk underwriting: skills in leading internal working groups and designing procedures and control processes.

Next steps

I will bring the ERM process to a high maturity level, so that the board/chief executive can use information on risks and controls to improve the overall performance of the company.

CHRISTINA MARTINEZ member of the board of Ferma and director of corporate risk management, Campfrio Food Group

First steps

My most useful qualifications for risk management have been my professional experience, my degree in actuarial sciences, as well as my PhD research on problems faced by organisations currently when implementing an ERM model.

Current role

My responsibilities include the definition and implementation of the overall enterprise-wide risk management, business continuity, insurance management and employee benefits. I am also leading the creation of an internal network of local risk management leaders.

Philosophy

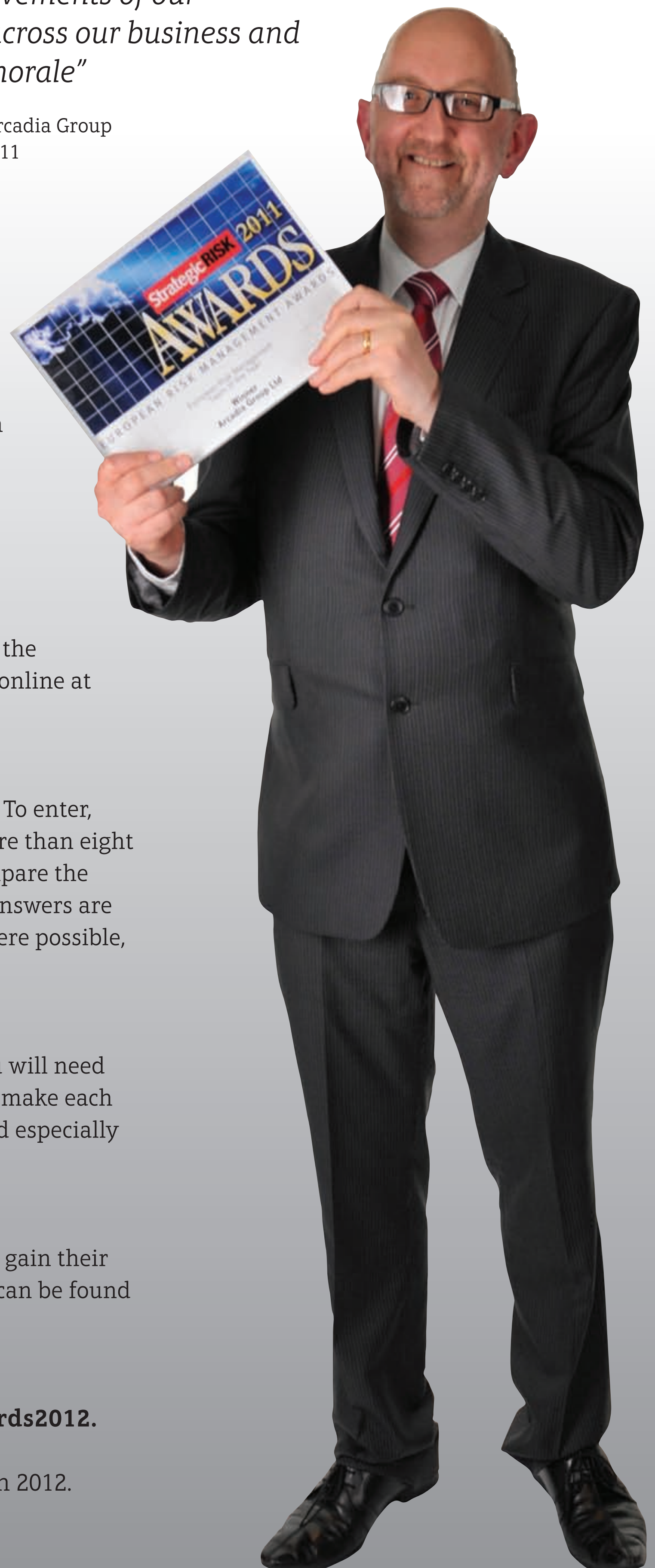
Risk management is about managing risks inherent to the business, so it is critical to understand your business. Moving the company towards a different way of thinking about risk is all about change management and leadership. It's important to share thoughts and experiences with other colleagues in the field. Attending professional and international events, such as the Ferma Forum, specific seminars and courses to meet other practising risk professionals is a good way to do this.

Next steps

I think we have exciting times ahead of us before the business community recognises the current imbalance between the organisation's strategy, risk culture and structure. As a corporate risk management director, I want each member of my organisation to achieve the recognised status of chief risk officer in their domain. **SR**

"It was a great honour to win the StrategicRISK award. It helped demonstrate the achievements of our risk management programme across our business and was also a huge boost to team morale"

Colin Campbell, Head of Risk Management, Arcadia Group
Winner: Risk Management Team of the Year 2011



QUICK GUIDE TO ENTERING THE AWARDS

Now it's time to bring together all the information that you will need to substantiate your entry. At StrategicRISK we recognise how busy you are and that preparing an entry form may not be top of your to-do list. With this in mind, our entry system for you to tell us about your achievements is designed to be quick and easy. To help you submit an entry, here's our five-step guide.

STEP 1 – FIND THE RIGHT CATEGORY

Check each category definition to make sure you are entering the correct award. You can read the full criteria for each category online at www.strategicrisk.co.uk/awards2012

STEP 2 – READ THE QUESTIONS

We've done away with the need to write lengthy submissions. To enter, simply complete our awards questionnaire comprising no more than eight questions, which make up your entry. Our judges want to compare the entrants' answers against each set question. Make sure your answers are succinct, avoid wordy, vague explanations and remember, where possible, to back up your answers with facts and testimonials.

STEP 3 – TIMESCALE AND TEAM

Establish what data, evidence, testimonials and examples you will need to support your entry. Delegate to members of your team and make each responsible for completing a section of the form. Entering, and especially winning, awards is great for team building.

STEP 4 – DO YOUR HOMEWORK

Take a look at previous winners and find out what they did to gain their award. A list of recent winners and a summary of the entries can be found at www.strategicrisk.co.uk/awards2011 under Roll of Honour.

STEP 5 – START TODAY

Enter online at **www.strategicrisk.co.uk/digital/srawards2012.**
All entries must be received by Friday 3rd February 2012.
Shortlisted finalists will be announced on Friday 2nd March 2012.

CALL FOR NOMINATIONS Do you know someone who you think should apply for an award?
If so nominate them now at **www.strategic-risk.eu/srawards**

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Corbis

REPUTATION

Badge of dishonour

A company ignores risk to brand reputation at its peril, and that risk can be much more complex – and have far greater consequences – than anyone anticipates, as BP found out in the Gulf

"IT TAKES 20 YEARS TO BUILD A REPUTATION AND FIVE minutes to ruin it," runs the famous quote by Warren Buffett.

But maintaining brand reputation by ensuring the highest standards possible across operations has become increasingly complex and challenging. While more aspects of many multinational supply chains have been outsourced to third and even fourth-party companies around the world, it is still the brand that picks up the tab when things go wrong.

"You can't outsource reputational risk," says reputation risk consultancy Reputability's chairman Anthony Fitzsimmons. "BP is a classic example of this. They subcontracted out aspects of their operations, but when things went wrong [in the Gulf] outsiders still saw them as responsible.

"The point is that it was BP that was perceived to be responsible, regardless of whether some subcontractor might eventually be found to be technically to blame.

"People are not interested in who in the supply chain messed up. They are likely to regard 'the brand' as being responsible."

Customers today expect firms across the spectrum to be careful that high ethical standards are observed throughout their businesses – a trend that has only increased in recent years – and will frequently deliver a harsh verdict on those who fail to live up to expectations. "Even where allegations of complicity do not result in legal action, companies still face a range of non-legal risks if perceived to be complicit," says Maplecroft principal human rights analyst Chris Kip.

> *'You can't outsource reputational risk'*
> **Anthony Fitzsimmons** Reputability

Risking consumer wrath

Falling down on ethics can be disastrous, and extremely expensive to rectify. Because of increased media coverage and better access to information, there is now a far higher awareness of companies' wrongdoings, while social media and other technology have helped consumers unite with pressure groups to take action against companies seen to be doing the wrong thing, with boycotts and other campaigns rapidly spreading between markets around the world.

And a collapse in sales and a falling share price are not the only consequences. Public exposure to criticism and the resulting brand damage can also mean that companies found to be benefiting from

If poor working conditions are found in the factories of suppliers or outsourced parts of a business, it is still the brand that takes the reputational hit

Key points

01: However much outsourcing or subcontracting is used, it is the core brand that is perceived as responsible when things go wrong

02: Customers expect high ethical standards – and deliver harsh verdicts against wrongdoers

03: In severe cases, only cash-rich companies like BP can survive the fall-out

04: Complex supply chains can also expose a business to reputational damage

bad practice face reduced access to financial capital – or even a shareholder revolt. All of which is expensive to mitigate.

"Companies whose reputation has been tarnished because of association with dubious labour practices in the supply chain will find that they need to spend more – both in terms of finances and time of its employees – for advertising and other CSR [corporate social responsibility] initiatives to reassure investors and consumers that it is acting responsibly," Kip says.

In the worst cases only the strong can survive. "Asset-rich businesses are more capable of riding out a big crisis than those based on debt," Fitzsimmons says. "For example, [after the Gulf blow out] BP lost over 50% of its share value – a huge hit – but it was able to keep going because it was a financially strong business. Had it been financed mainly by debt, it could easily have collapsed or been taken over."

Be thoughtful, be careful

But it's also worth remembering that complex supply chains don't only pose an ethical risk – for example where there could be complicity in environmental damage or human rights abuses – complexity itself can cause problems for business reputations.

"A classic example is the Airbus A380," says Fitzsimmons. "This was manufactured by using factories in different European countries to produce different components, with the whole thing being assembled in Toulouse. When the fuselage segments were brought together to be joined up, the wiring wouldn't mate. The whole thing had to be re-wired.

"That didn't just cost Airbus about €3bn. It also damaged their reputation and caused a €5.5bn drop in their share price. Another example is the financial system in general. It's so complex that no one knows what is really going on, let alone what will happen next week."

In more challenging economic times, increasing competition can increase exposure to risk. "You have to be very thoughtful when driving down costs," says Fitzsimmons. "If you aren't very careful, you will create new risks in the process of saving money. These risks can come back and bite you painfully hard."

Because of this, prevention is far better than cure. But strategy must be tailored to an individual business. "There is no one-size-fits-all solution for all risks that companies could face in their operations," Kip says. "There are steps businesses can all take, such as engaging in human rights due diligence to get a clear understanding of the human rights situation in countries where they are sourcing. Other measures could include the monitoring and auditing of suppliers to identify potential areas of risk – as well as evaluating the human rights impacts of their own operations."

At its heart, Fitzsimmons says, maintaining reputation is a management problem. "The really difficult issues have to do with the soft issues such as culture, leadership, communication and incentives," he says.

"The press often accuse business schools of being good at teaching hard skills, like finance and strategy, which are broadly conceptual or quantifiable, but poor at teaching the soft skills that are harder to quantify. Yet deficiencies in those areas leave 'soft' risks – and these can bring an organisation to its knees." **SR**

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SPOTLIGHT

Forced and slave labour

WHAT DO YOU REALLY KNOW ABOUT CONDITIONS IN THE factories where your products are made? Key manufacturing nations represents a real risk of exposure to forced or slave labour, according to research by Maplecroft, with China, India, Mexico, Indonesia, Malaysia, Vietnam, Bangladesh and the Philippines all presenting an 'extreme risk'.

As a result, due diligence is essential, especially within high-risk industries, particularly those involving temporary or seasonal work, including agriculture, mining, the making of textiles and garments, and construction.

Companies should also be aware that in some countries forced labour is not illegal, and even where laws exist they may not properly enforced. For example, Uzbekistan has used forced child labour in its cotton harvesting for years, while in Mexico and Vietnam law enforcement lacks the resources to effectively police compliance.

One way to minimise this risk is by insisting suppliers provide workers with written contracts outlining terms and conditions. Another is by joining a multi-stakeholder initiative aimed at addressing issues of forced labour, such as the International Cocoa Initiative, Responsible Cotton Network and the Citizen's Charcoal Institute, which brings together trade unions, law enforcement authorities, NGOs, labour inspectorates and others.

SPOTLIGHT

Rotten Apple?

APPLE, ONE OF THE MOST SLICKLY MARKETED and technically brilliant business stories of recent years, has repeatedly suffered attacks on its reputation over ethics.

In 2010, at least 11 15-year-old children were discovered to be working in three factories in China that supplied Apple, prompting widespread media coverage, and the company has been regularly criticised in the press for using factories with poor – even abusive – working practices.

In one instance, also in China, a suicide was linked to a pressurised working environment; in another, 62 workers at a factory were poisoned by n-hexane, a chemical that can cause muscular degeneration and blur eyesight.

The company has admitted that at one time at least 55 of the 102 factories it used were ignoring Apple's own rule that staff cannot work longer than 60 hours per week.

And it is not just human rights groups that are taking a bite out of Apple. As recently as April this year, the Californian company came bottom of a green league table of technology companies compiled by Greenpeace, because of its heavy reliance on "dirty data" centres powered by coal.

RISK ATLAS
POLITICAL RISKS

A different kind of revolution

A year of unrest has seen uprisings in the Arab world and protests on Europe's streets

THE LAST 12 MONTHS HAVE BEEN CHARACTERISED BY political fluctuations in many parts of the globe. Civil unrest in the Arab world has probably resonated loudest. A lynchpin in the world economy because of its oil and gas reserves, peace in the Middle East, sadly rare, is crucial to maintaining stable energy prices.

A recent briefing by Aegis Advisory says rising instability in the Arab nations is affecting the risk exposures of businesses worldwide in two main ways. It is hitting energy prices by creating chronic uncertainty. It is also demonstrating the usefulness of social media, such as Twitter and Facebook, to co-ordinate protests and political activity. Social media has played a part in political unrest from Chile and the USA to Spain, Italy, Greece and the UK.

Mass protest is not confined to the dictatorial regimes of the Middle East

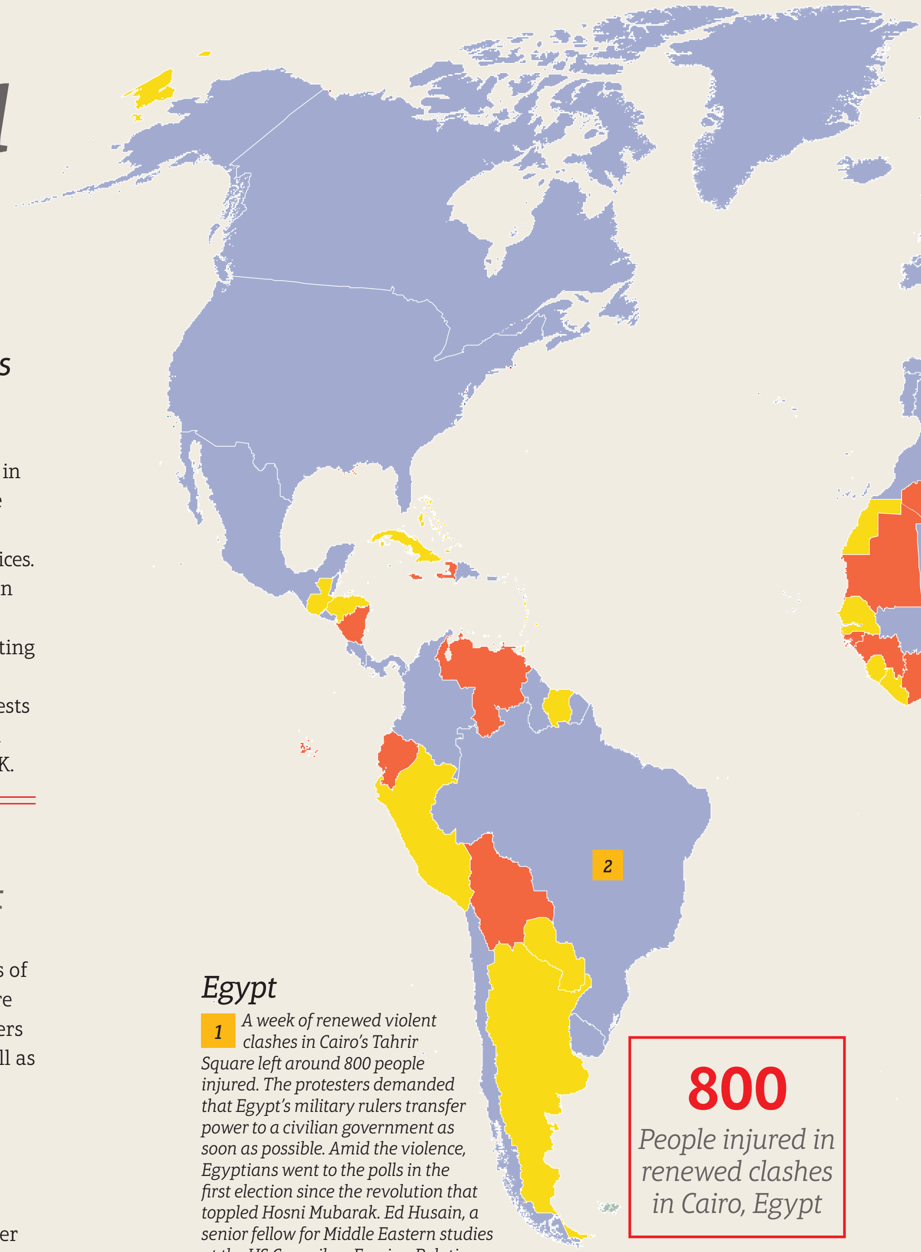
But mass protest is not confined to the dictatorial regimes of the Middle East and North Africa. Across Europe the people are rising up in protest against both the failure of the ruling powers to restrain the excesses of a capitalist system gone mad as well as the austerity measures implemented in response to these failures. In Europe, actions to remedy national financial problems, largely stemming from bank bailouts, are likely to spark further protests and riots.

Greece is expected to make further spending cuts as a condition of its bail-out package from the EU and IMF. Its October strikes and work stoppages in reaction to austerity measures could well be followed by more of the violent protests that began in May.

The same could be true in other European countries as governments fight against a return to recession. The French finance minister announced austerity measures in September. The UK chancellor of the Exchequer has pledged to continue the country's fiscal squeeze, despite unemployment hitting a 15-year high. Spain and, to a lesser extent, Italy have seen protests against cuts.

In contrast to the Middle East, these popular movements are unlikely to lead to wholesale political upheaval or revolution – Western political institutions tend to be fairly responsive and temper the revolutionary spirit. **SR**

➔ [READ MORE ONLINE] Download a PDF of this risk map at www.strategic-risk.eu or goo.gl/joFlH



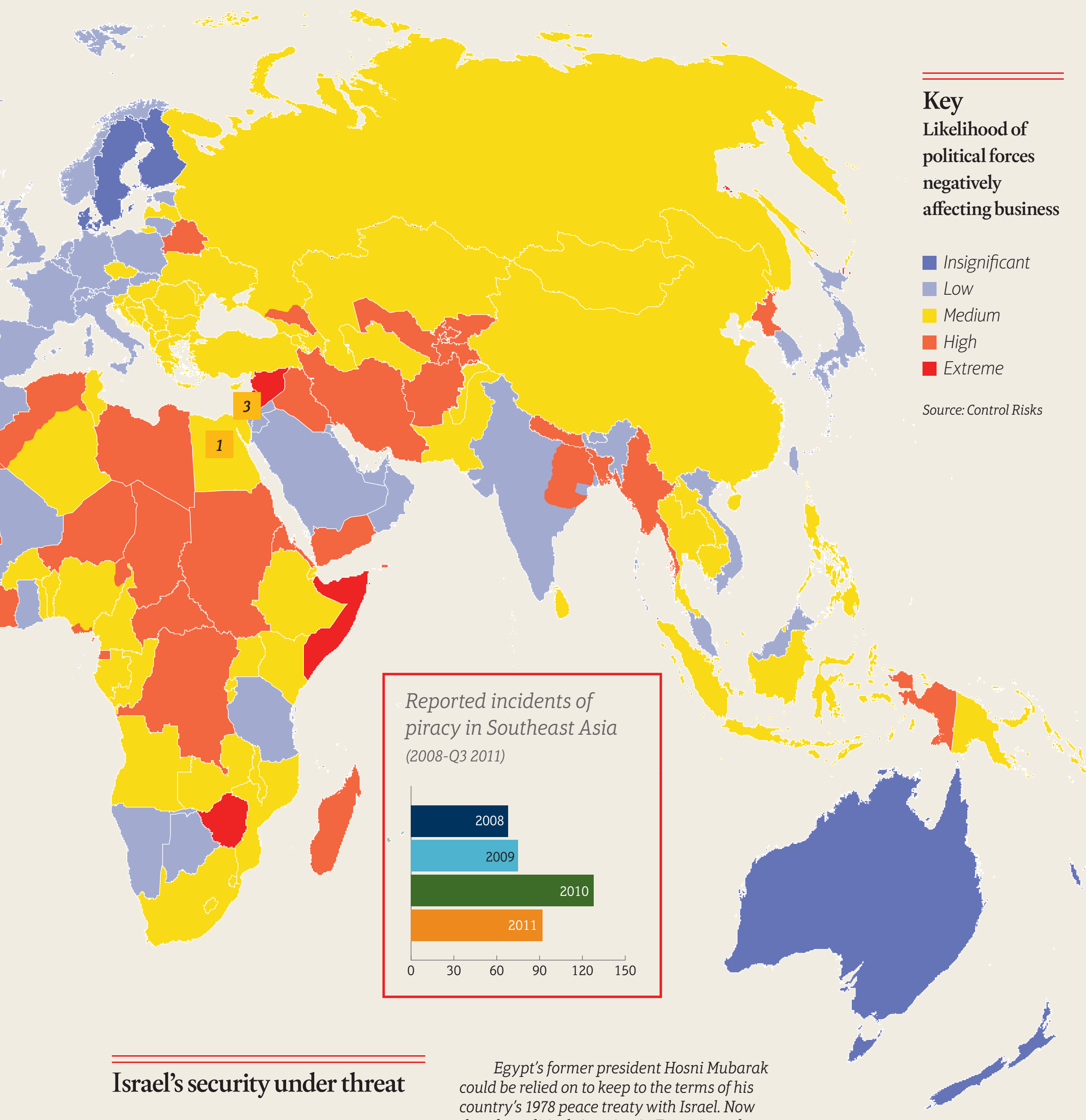
Egypt

1 *A week of renewed violent clashes in Cairo's Tahrir Square left around 800 people injured. The protesters demanded that Egypt's military rulers transfer power to a civilian government as soon as possible. Amid the violence, Egyptians went to the polls in the first election since the revolution that toppled Hosni Mubarak. Ed Husain, a senior fellow for Middle Eastern studies at the US Council on Foreign Relations, said that the Muslim Brotherhood's Freedom and Justice Party looks to be the most organised political force. Commenting on the situation from Cairo, he said: "The liberal, urban, and elite Facebook and Twitter generation of Egyptians may have led the January revolution, but they simply do not possess the real-world resources, unified thought patterns, and socio-political networks of their Islamist rivals."*

800
People injured in renewed clashes in Cairo, Egypt

Brazil

2 *The Federation of European Risk Management Associations (Ferma) urged Brazilian insurance regulator SUSEP to limit the impact of controversial regulations 225 and 232, which require 40% of insurance contracts to be placed locally. Ferma has campaigned to relax the regulations on behalf of its European multinational members. Jorge Luzzi, president of Ferma, made the case in a letter to SUSEP, saying that the possible limits on capacity and threat to insurer security posed by the regulations has raised many concerns from risk managers.*



Key
Likelihood of political forces negatively affecting business

- *Insignificant*
- *Low*
- *Medium*
- *High*
- *Extreme*

Source: Control Risks

Reported incidents of piracy in Southeast Asia
(2008-Q3 2011)

Israel's security under threat

3 The rise of populist movements in the Arab countries surrounding Israel has dramatically changed the security dynamic in this part of the world and revealed the weaknesses of Israel's situation.

According to a blog on JLT's World Risk Review website: "The Arab Spring has reshaped the risk environment for all countries in the Middle East and nowhere is the impact more keenly felt than in Israel."

Israel's security position once relied on deals with ruling military elites and not alignments with the Arab public, who remain broadly hostile to a Jewish state in their midst, according to JLT. Political instability in Egypt and Syria, which both share land borders with Israel, is having a profound impact on the regional security situation. "For more than 30 years Israel has grown accustomed to calling the shots as the regional power broker," continued JLT. But this situation is changing.

Egypt's former president Hosni Mubarak could be relied on to keep to the terms of his country's 1978 peace treaty with Israel. Now that the political situation in Egypt is unclear, this assumption is coming under question.

Additionally, now that Syria's ruling Assad regime, which used to prevent protestors and terrorists infiltrating the Golan Heights, is under threat, stability along this border is far from certain.

60%
of global risk experts believe a major social disruption is likely to occur over the next 12 months, according to a World Economic Forum survey

EXPERT VIEW

Walter Körner, senior officer crisis management/corporate security, Allianz SE

Managing a crisis

MULTINATIONAL COMPANIES WITH operations around the globe and many of their staff travelling on a regular basis are highly prone to geopolitical risks.

This year was particularly turbulent. The conflict in Abidjan, the critical security situation in the north of Mexico, the Arab Spring and catastrophe at Fukushima kept many companies busy co-ordinating evacuations and organising back-up offices for employees on the ground. Precautions to secure their employees and properties in advance should therefore be standard procedure.

A vital precaution is the monitoring of countries where a firm has subsidiaries to which employees often travel. This aids local security and safeguarding of critical business processes. If a serious event occurs, crisis management should immediately be activated.

A big challenge is always if and when a company's foreign staff is to be evacuated. Several factors – such as the security environment, and the individual character and the personal situation of the respective employees – need to be considered, including the possible impact on the foreign employee's reputation.

Global players have various ways to support emergency measures from the outside, for example in situations of disturbed communication or mobility that the local operating entity or the public authorities in the country cannot cope with. In these instances, a central co-ordination of efforts is paramount.

So to minimise the impact of geopolitical risks on employees, two aspects are crucial: first, a central unit is needed to permanently monitor and evaluate changes in conflict areas and incorporate results among international business processes. Secondly, a well-tested crisis management plan is mandatory, acting as fast as possible and in line with the company's specific needs.


a redefined vision of service
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a **reliable** company
available teams
attentive advice

Special Report

Supply chain risks

SUPPLY CHAIN RISKS

HOW ROBUST ARE YOUR SUPPLIERS, THEIR SUPPLIERS … and the suppliers behind them? The trend to source globally has increased as corporations strive to preserve, if not improve, profitability. But cost advantage can come at a price.

Risk managers are increasingly aware of the difficulties in managing supply chain risks. Apart from quality control and intellectual property protection, they are looking harder at the aftermath of disasters like the Japanese earthquake and tsunami.

While natural catastrophes are fairly common in some less developed areas of the world, this year has shown developed countries are also vulnerable. Floods in Australia, the New Zealand earthquake and the Japanese disaster highlighted, there can be risks wherever you or your suppliers are located. Meanwhile, the Intergovernmental Panel on Climate Change warns that the economic cost of future extreme weather could run into billions.

It seems some global companies have chosen a bad time to reduce control over supply networks. How effectively they can manage and monitor the risks is questionable in the light of Japanese companies' experience. For example, major motor manufacturers and electronics businesses suffered considerably from disrupted production when the earthquake and tsunami struck earlier this year. They are now suffering again because of the floods in Thailand affecting production hubs there.

Unfortunately, the factors that drive cost cuts also tend to increase risks. For example, while it is generally cheaper to buy most products and components in bulk from a single supplier, this leads to greater dependence on a few producers – and reduced flexibility to switch sources if disaster strikes.

Further, putting pressure on suppliers to reduce price can start a chain reaction through the network, with small companies tempted – or even forced – to cut corners to save money.

Some risk managers are looking to insurers for solutions. But this is a ball that underwriters may be reluctant to catch. **SR**

Contents

[SUPPLY CHAIN RISKS]

This special report has been produced with input from:
Alain Delcroix, head of marine and transport risk consulting, AXA
Tristan Huon de Kermadec, head of property, AXA
Bernard Laporte, head of R&D, AXA Matrix Risk Consultants

LOGISTICS

As strong as the weakest link

Outsourcing overseas, just-in-time delivery and moving to single suppliers have all been factors in an increased supply chain risk. And, as recent events have shown, when things go wrong it can be devastating

"A MAJOR CONCERN FOR everybody is that supply chain issues are becoming much bigger on the radar than they used to be. From being a medium sized risk, these have grown and it is recognised that they can take catastrophic proportions." So warns AXA Matrix Risk Consultants head of R&D Bernard Laporte.

Supply Chain Resilience 2011, a survey of more than 550 organisations in over 60 countries published in November by the UK Business Continuity Institute, shows that 85% of respondents suffered at least one disruption in the last year.

Forty per cent of analysed disruptions originated below the immediate tier one supplier, while supply chain incidents led to a loss of productivity for almost half of businesses, along with increased cost of working (38%) and loss of revenue (32%). For 17% of respondents, the largest single incident cost at least €1m (£860,000). Of those with weaker supply chains, the number hit by higher costs almost doubled to 32%.

While natural catastrophes, including adverse weather, are frequently blamed for supply chain problems, the real cause lies in the way businesses are run today, says Lockton partner Ian Canham. "Companies in the last 10 years have been stretching the supply chain, moving to just-in-time deliveries, and becoming much more single supplier oriented, focusing particularly on suppliers in the developing world," he says.

'Businesses have made these changes for good economic reasons but they haven't taken into account the full extent of the risk they are taking on'

Ian Canham Lockton

"Businesses have made these changes for good economic reasons, but they haven't taken into account the full extent of the risk they are taking on," he adds. Such risk stems not only from suppliers based in catastrophe-prone regions but may also stem from regulatory issues, as quality standards may not be as high as in developed countries.

PLANNING

Learning the hard way

Natural catastrophes, such as this year's earthquakes in Japan and New Zealand and floods in Australia, have awoken risk managers to the need for business continuity planning should the worst happen

NATURAL CATASTROPHES IN 2011 – and in particular the Japanese earthquake and tsunami – have highlighted many companies' supply chain vulnerabilities. President of Ferma and Pirelli director of group risk management Jorge Luzzi describes recent events that have had the most impact for European companies' supply chains.

"Over the last two years it has been the earthquake and tsunami in Japan in March 2011, the floods in Australia during the winter, the New Zealand earthquakes and, for some Spanish companies, the earthquake in Chile in February 2010. There has been some effect from the more recent floods in Thailand. So far it is not very great – Japanese and Taiwanese companies seem to have taken the brunt – although the full picture is still emerging," he says.

Lockton partner Andrew Cornish does not rule out significant impact from the Thailand floods. "There may be some direct impact on European companies compared to problems caused by the Japanese tsunami, which tended to occur further up the supply chain," he says.

The results of natural catastrophes can be wide ranging. The Business Continuity Institute's November international survey on supply chain resilience in 2011 found that the earthquakes and tsunami experienced in Japan and New Zealand this year affected 20% of responding organisations, headquartered in 18 different countries and across 12 different industry sectors.

What are the lessons of such events? Luzzi says: "We learned that even in a first-world country that seems to be well prepared and well organised, a major natural catastrophe can be very disruptive. We need to consider this in our business continuity planning."

Ian Canham, also a Lockton partner, says that the large amount of manufacturing in Japan and many global corporations' reliance on hi-tech companies and their Japanese manufacturing businesses came as a shock to many people. "You need to understand the manufacturing spread and capabilities of any organisation you deal with now much more

Canham cites the case of Sudan Red, the food colouring banned in Europe, which a few years ago was found in imported products. "That is a classic example of someone not asking the right questions about regulatory approval. The result was a massive recall of affected products," he says.

Laporte says the term 'supply chain' is a misnomer. "It is not a chain but a network – and a very complex and constantly changing network because of the high degree of outsourcing that most large companies do now," he says. "You can have someone in a small town in an Asian country who is providing a key component without perhaps anyone realising the true potential impact of losing this supplier.

"The major risk of supply chain management is loss of control: not knowing where and what are the risks."

It is not just when supplies are being produced in far-flung regions that this loss of control can occur, warns AXA's head of marine and transport risk consulting, Alain Delcroix. "Transport is the weak link of the supply chain, and this link is getting weaker and weaker as the distance between buyers and suppliers increases. When companies

November 2011: Rising floodwaters inside a military airport, Bangkok

relocate suppliers from local businesses to companies far afield, for example in China, at the same time working to tight just-in-time delivery times, they increase their reliance on the transportation industry," he says.

This is particularly relevant in view of changes within the shipping industry. "The trend for carriers to reduce their sailing speeds, so-called 'slow steaming', brings new risks. Extending marine transit time can increase inventory holding costs and expose goods to additional transhipments with many potential risks," says Delcroix.

Many containers are lost overboard due to weather conditions, high vessel speed and, more often, the way that the carrier manages ship planning. The way that cargo is secured on board is also important.

Delcroix says crew shortages and quality are also an issue, with an increased risk of casualties, particularly groundings and collisions in busy seaways such as the Channel, the North Sea and the China Sea.

The transport industry's own supply network has also become more complex. He says: "There may be a large number of subcontractors in the chain, for example road transporters, storage at the port before loading, sea transport, unloading, possibly more storage, then more road transportation. Outsourcing is not only from shipper to freight forwarder."

Laporte concludes: "In terms of impact to a supply chain from a catastrophic event, we tend to think about immediate damage, but this is not the whole corollary of bad consequences. If you lose a key supplier you may have to rely – if you find it – on another producer whose products may be inferior. There may be adverse consequences in terms of faulty products, with direct consequences on the reputation of the brand." **SR**

than in the past. This means looking inside their business and finding out where their own supplies are coming from," he says.

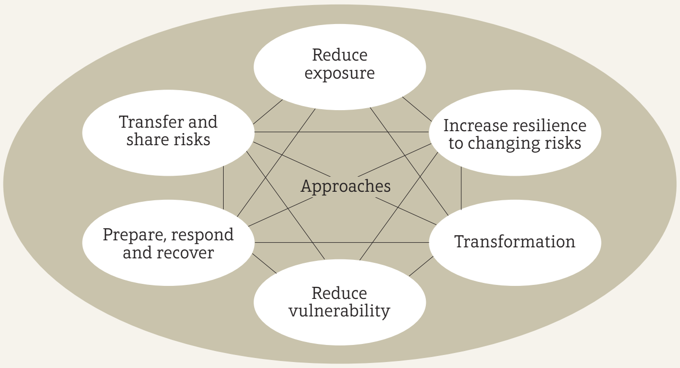
AXA Matrix Risk Consultants head of R&D Bernard Laporte believes that, in supply chain risk terms, the lessons of events such as Japan's tsunami are that whatever the causes – natural and/or technical – they can produce catastrophic results on ever-interwoven human activities and assets. "We should focus less on the causes and more on the results," he says.

Perhaps one of the most significant results of the Japanese catastrophe is growing interest in contingent business interruption (CBI). AXA head of property Tristan Huon de Kermadec says: "The first issue was the property damage and consequential loss arising directly from the Japanese event. Second was the CBI – losses owing to damage and disruption at suppliers. It seemed that this was a big surprise for everyone. It was well understood that a catastrophe can cause major disasters and losses, but less clearly understood that it is possible to have more loss as a result of CBI issues."

CLIMATE CHANGE RISKS AND APPROACHES

THE INTERGOVERNMENTAL Panel on Climate Change (IPCC) approved its special report on *Managing the Risks of Extreme Events and Disasters to Advance Climate Change Adaptation* in November. The IPCC warns that extreme weather could have a major financial as well as human cost.

The report outlines the adaptation and disaster risk management approaches for a changing climate (see diagram).



Retiring Ferma president Peter den Dekker summed up the risk management view at October's Ferma forum. "Our businesses are so complex that we cannot control every aspect of our supply chains when there is a catastrophe," he said. Den Dekker called on the insurers and reinsurers to understand and support clients' new business models by providing CBI insurance.

"To get the sort of financial protection that we need in the face of catastrophes – and to make it a worthwhile business for the insurers and reinsurers – is an issue for us working together," he said. **SR**

PROCUREMENT

Putting risk up front

The complexity of global supply chains may make it impossible to truly assess total risk to a company's business in the event of a catastrophe. But having procurement teams consider risk when awarding contracts would be a start

Entry box head

01: It may be impossible to map all your supply chain risks
02: Procurement departments need to take risk into account – risk managers should raise their awareness
03: Higher limits and wider coverage in CBI insurance will not be available without full clarity on supply chain exposures
04: Some companies may reduce their dependence on extended global supply chains
.

MEASURING AND MONITORING the risks posed by all the components of today's complex global supply chains is a challenge. A truly comprehensive study may be impossible to achieve.

Lockton partner Andrew Cornish says a risk-based approach is important. "There is only so far you can go. If you try to identify every supplier of your suppliers, you will never come up with useful loss reduction techniques to help your business."

AXA head of property Tristan Huon de Kermadec says: "Some risk managers are looking to assess risk beyond their tier-one suppliers, but doing that is quite a lengthy process, and by the time they finish their study the supply chain may have changed." However, Ferma president and Pirelli group risk management director Jorge Luzzi says: "If we only looked at the first tier, we would almost certainly under-estimate the risks. Where, however, we have a strong first-tier supplier or customer, we may be able to let them manage the second- and third-tier exposures," he says.

A key problem is that appointment of suppliers is generally handled by procurement departments – and risk prevention is down the agenda. Huon de Kermadec says: "Procurement departments tend to focus on financial considerations. They need to take in the principles of risk management at the time of procurement."

However, it seems financial pressures are focusing corporations' attention more on survival than risk management. Indeed some have reduced their risk management functions to save money. The drive to push costs down ever further could rebound.

AXA Matrix Risk Consultants head of R&D Bernard Laporte says: "For financial reasons, large companies place huge pressure on their direct suppliers. In turn, these will be placing pressure on their own suppliers – tier two. So you can get a situation where everyone is trying to cut corners and gain extra time on the back of the next organisation they are outsourcing to. What happens if the business at the end of the line becomes insolvent? Loss prevention and risk management are the main losers in this equation."

He adds: "Risk managers cannot do that much because it is not within their province or responsibility – the procurement department is in charge – particularly in those companies that have gone furthest in outsourcing. Risk management is seldom on procurement's agenda, neither is what it will mean if their suppliers do not survive. However, the risk manager can and should still raise awareness in his organisation."

> *'Procurement departments tend to focus on financial considerations. They need to take in the principles of risk management'*
>
> **Tristan Huon de Kermadec** AXA

He adds that contracts can be a key element as far as loss liability is concerned. "If a contract is not well written, you are paving the way for a major loss," he says.

Lockton partner Ian Canham suggests too that, where a company has a sole supplier of a key product or component, it makes sense to pre-validate another production facility elsewhere. "And, if appropriate, you might tell your suppliers they need a more robust supply chain," he says.

But not all procurement managers ignore the risk implications, say Cornish and Canham. The smart ones are starting to look at procurement in a risk-weighted way.

With the fall-out from the Japanese catastrophe, Huon de Kermadec believes risk managers are likely to want more capacity to cover the contingent business interruption (CBI) risk. "As insurers, we need them to be able to give us a clear risk assessment of the CBI risk. For example, a company may have two key suppliers for the same product in the same regional zone. If a catastrophe occurs and it loses both at the same time, it will not have a back-up. It is very difficult for clients to identify these kinds of risk."

"Further, for insurers there may be problems of accumulation of risk because one supplier can be supplying lots of clients. This may not be a tier-one supplier but may be further down the supply chain, say tier two or three. It can be very complex to assess the risk here." But only a precise assessment of exposures would optimise capital for insurance and thus coverage limits and insurance costs for clients, he stresses.

Canham says CBI cover triggered by insurable losses might be relevant to less than half of supply chain problems. "Most supply chain issues start with something that would not have been traditionally insured," he says. And he agrees with Huon de Kermadec that risk managers who cannot map and be clear about their exposures cannot expect insurers to stake their capital.

JLT Specialty partner, and global head of the communication, technology and media practice, Peter Hacker earlier this year summed up what is required for insurers to properly price CBI cover. "You need a very good understanding of the supply chain, the crisis management, the sourcing of the company, and you need models that allow you to be flexible and to consider different cash flow dependencies, or dependencies between suppliers. In a most technical and proper way, one should quantify, structure and cover the CBI exposure within a standalone and bespoke policy."

In online comments for *Foreign Policy* magazine on the downside of globalisation, US Economic Strategy Institute president Clyde Prestowitz says that, in the light of the Japanese tsunami and flooding in Thailand, "while immediate costs may be minimised by the global supply chain, there is also a greater than expected risk of breakdowns that can impose ultimate costs far greater than the immediate gains earned from global component cost arbitrage".

Re-shoring and reduced reliance on extended global supply chains rather than further globalisation may be the way ahead, he suggests. **SR**


*References the 2008 Forbes Tax Misery & Reform Index
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BRIBERY

Bribery revealed

Some companies are no better at tackling corruption than three years ago, despite new anti-bribery laws

»

Perhaps contrary to expectations, India falls around the middle of countries ranked on the perceived likelihood of acts of bribery

Key points

01: There have been few improvements in the index since it was last compiled in 2008

02: None of the 28 countries listed in the index is considered completely free of bribery

03: Russia and China got the worst scores, while Switzerland and the Netherlands were joint first

04: The UK fell three places in the rankings – indicating that perceived bribery had gotten worse

CHINESE AND RUSSIAN COMPANIES ARE SEEN AS MOST likely to commit bribery abroad, according to Transparency International's Bribe Payers Index 2011.

In the fifth edition of its Bribe Payers Index, issued in November, the global anti-corruption coalition ranked the world's 28 largest economies by the likelihood of their firms to bribe abroad. The score system ranks countries from 0 to 10, 0 for 'always' and 10 for 'never' committing bribery (see the rankings on these pages).

The Index captures the supply side of international bribery (the bribe payers) in the private sector. The results are based on the individual evaluations of 3,016 senior business executives in 30 countries around the world, asked about their perceptions of the likelihood of companies to engage in bribery abroad. The index includes all G20 countries and other key regional economic trading powers.

None of the 28 countries assessed is considered completely free of bribery. Russia and China got the lowest scores, with 6.1 and 6.5, respectively, while the Netherlands and Switzerland only scored 8.8 on a joint first rank.

It is significant that there are hardly any improvements in the index since the last was compiled in 2008. Most surprising was the UK. Since the implementation of the UK Bribery Act earlier this year, said to be one of the toughest anti-bribery laws worldwide, one of the first things anti-bribery campaigners will have been looking for is a significant improvement in corruption cases and enforcement. But the UK actually moved three places down the ranking, compared with 2008, and now ranks eighth on the index.

"Over the years, we've always heard governments saying to us that they cannot solve this problem because it's the companies themselves that have to. Our data clearly shows that government regulation matters a great deal, there's no escaping from that any more," says Transparency International chair Huguette Labelle.

Public projects and construction are perceived to be the sectors most at risk of bribery, according to the research. Agriculture and light manufacturing were the least likely to be involved in bribery.

Bribes to secure influence over policy, regulatory and legislative decisions are almost as likely as kickbacks between two private firms, according to the study.

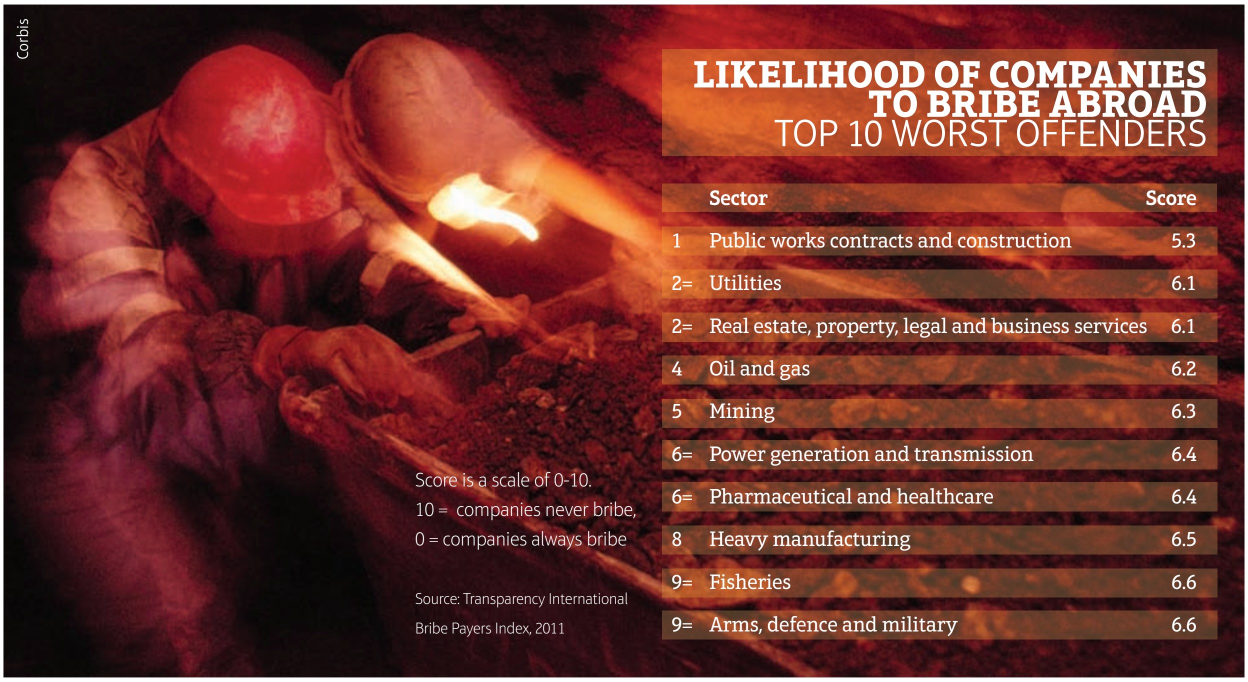
Labelle urges companies themselves to strengthen the enforcements of anti-corruption procedures and improve transparency, especially to tackle 'firm-to-firm' bribery.

While the UK Bribery Act became law in July, a panel discussion between members of Transparency International and its partners Ernst & Young at the index's launch in November suggested that it was yet to have a big impact (note: all panellists wished to remain anonymous). "[The Bribe Payers Index] tells us that so many business executives around the world know about others bribing, but aren't doing much to tell or whistleblow," said one member of the audience at the index's launch. "That's a rather disturbing piece of information."

Differing cultural perceptions over what constitutes bribery is also a concern. The line between a bribe and 'corporate hospitality' or an innocent gift can be a difficult one to draw. In some cultures, rejecting a gift could be seen as extremely offensive. A panel member put it simply: "If you receive a gift and you're confident to put it on your website, you're fine."

Pressure by regulators is pushing companies to address these issues. Ultimately, as panellists agreed, a corrupt company will fail. It's no good "hoping that no one will notice", said one panellist. Referring to the Arab Spring, a panel member commented that the world has "never seen people demand public accountability to the extent that they do now", and that's the pressure that will fundamentally change the dark world of corruption.

Transparency International is confident that attitudes towards corporate bribery will change for the better. In fact, the team was

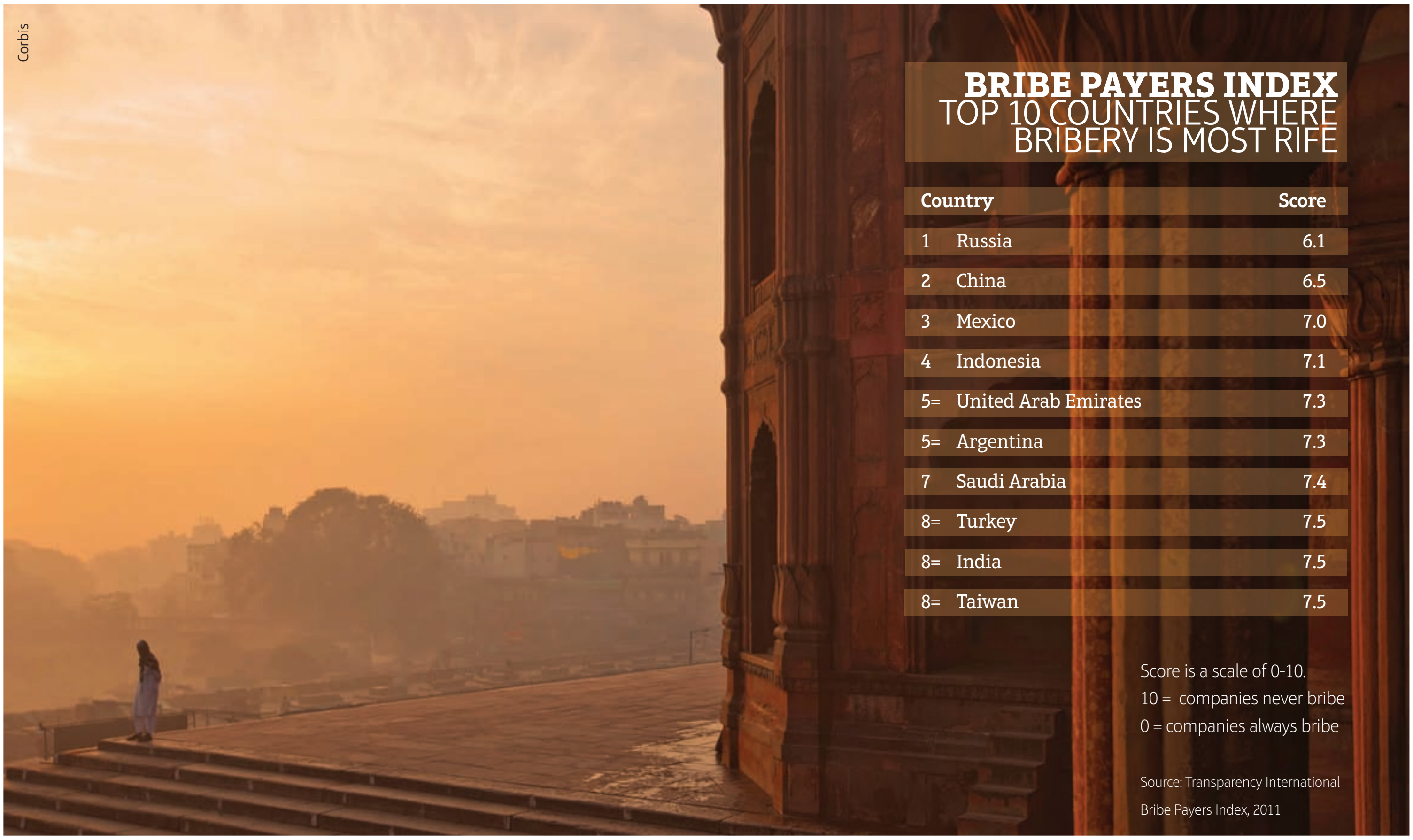

Corbis

LIKELIHOOD OF COMPANIES TO BRIBE ABROAD
TOP 10 WORST OFFENDERS

	Sector	Score
1	Public works contracts and construction	5.3
2=	Utilities	6.1
2=	Real estate, property, legal and business services	6.1
4	Oil and gas	6.2
5	Mining	6.3
6=	Power generation and transmission	6.4
6=	Pharmaceutical and healthcare	6.4
8	Heavy manufacturing	6.5
9=	Fisheries	6.6
9=	Arms, defence and military	6.6

Score is a scale of 0-10.
10 = companies never bribe,
0 = companies always bribe

Source: Transparency International Bribe Payers Index, 2011



BRIBE PAYERS INDEX
TOP 10 COUNTRIES WHERE BRIBERY IS MOST RIFE

	Country	Score
1	Russia	6.1
2	China	6.5
3	Mexico	7.0
4	Indonesia	7.1
5=	United Arab Emirates	7.3
5=	Argentina	7.3
7	Saudi Arabia	7.4
8=	Turkey	7.5
8=	India	7.5
8=	Taiwan	7.5

Score is a scale of 0-10.
10 = companies never bribe
0 = companies always bribe

Source: Transparency International Bribe Payers Index, 2011

convinced that the bringing in of appropriate procedures (such as in the UK) are a sign of a commitment. This proves there are pressures in the right direction, it said.

Recommendations to companies imply that corporate structures should be more transparent, reporting on anti-corruption programmes should meet international standards (such as the UN Global Compact) and political contributions as well as lobbying should be included in corporate reporting.

To advance the fight against bribery, Transparency International suggested bribery and corruption risk should be assessed across companies' entire supply chains, and due diligence should be undertaken in evaluating the anti-bribery programmes of suppliers and contractors.

Governments are also stepping up and taking effective action both at the national level and through international groups such as the G20, EU, UN and Organisation for Economic Cooperation and Development.

If its recommendations are taken up, Transparency International is optimistic that the next Bribe Payers Index could see some big improvements. **SR**

STANDARDS

Business principles in combating bribery

THE FOLLOWING BUSINESS PRINCIPLES HAVE been developed to assist companies to develop approaches to combat bribery in their activities. They are based on a fundamental commitment to the values of integrity, transparency and accountability. The enterprise should:

- prohibit bribery in any form, whether direct or indirect;
- commit to implementing a programme to counter bribery; and
- aim to create and maintain a trust-based and inclusive internal culture in which bribery is not tolerated.

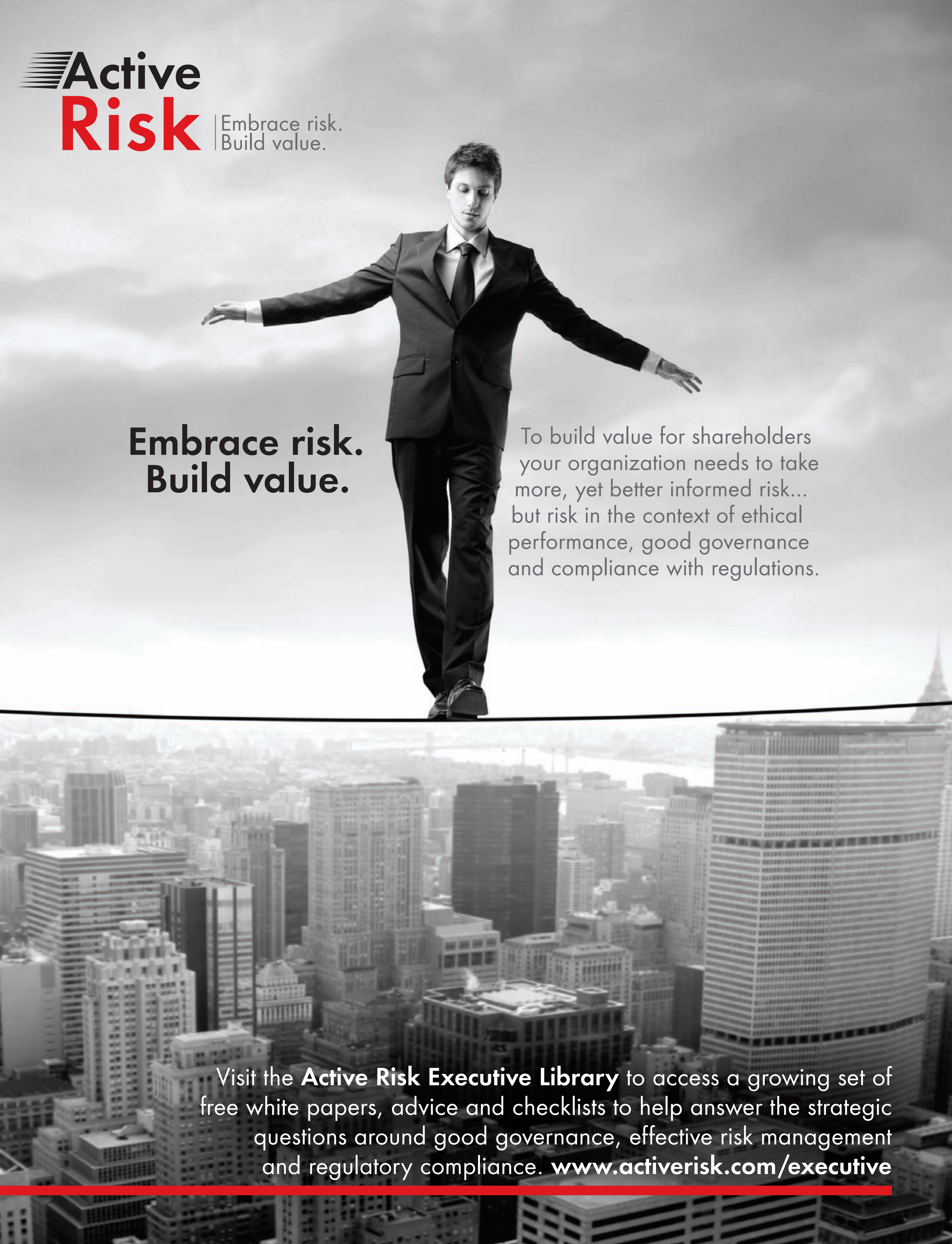
IN THE SPOTLIGHT

International sport hit by bribery scandals

TWO OF THE WORLD'S MOST POPULAR SPORTS, FOOTBALL and cricket, have both recently been tarnished by corruption scandals. In cricket, the scandal involved players accepting bribes to fix betting results. In addition, a number of allegations have been levelled at FIFA, football's governing authority, about corrupt payments surrounding World Cup TV rights and hosting privileges.

FIFA has announced that it will introduce reforms to address these issues and instigate an investigation into its own conduct.

But "there is still a lot of work to do to restore credibility", said Transparency International. "It will be a big challenge to implement the reforms and it will require a change of culture in the whole world of football," it says.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CONTROLS

How to learn from banks on proportionate control

Good risk management can open up opportunities. But too many controls can become costly, cumbersome, and create a false sense of security

RISK MANAGEMENT IS OFTEN dismissed as 'business prevention'. It doesn't have to be that way.

Learning from banks isn't fashionable at the moment. Yet banks have understood that sound risk management can expand choices rather than limit them. The result is a model that creates new value for the business and better processes for customers.

Controls in operational areas tend to become layered, one on top of the other, rather than adjusted in the light of changing conditions. Once a control is in place, people seldom ask whether it remains proportionate to the underlying risk. This can lead to an operation that is too slow and costly to be competitive. And it breeds a dangerously false sense of security.

Banks are alert to this problem of control layering and prefer to look at operational risk in the round – people, environment, technologies and processes. They ask the key question: is spending on controls matched to underlying risk? In some financial service operations, up to half the control bill could be removed, which would also lower delays in customer service.

Here are five steps to eliminating control layering and add value via risk management:

Corbis

The key question is whether spending on controls is matched to the underlying risk

1 ANALYSE REPETITIVE HIGH-VOLUME, MULTI-LOCATIONAL PROCESSES

Be empirical before you get radical. Take a close look at a part of the organisation that informed participants believe is over-controlled. This can blaze a trail for other projects. Robust cost-capture techniques can be used to assess a process, the cost of controls and underlying risks. Don't worry about ad hoc processes, or small ones; look out for the repetitive high-volume activities.

Take time to understand both process and risk levels first; transparency and detailed knowledge are not optional extras.

You need to lay the costs over the process, seeing how spending is matched to areas of serious, rather than residual, risk. Any inverse correlations will then be plain to see

2 RELATE RISK TO CONTROL COSTS

You're likely to discover that some procedures that should be routine are bogged down in checks and counter-checks. As in an old overhead slide presentation, you need to lay the costs over the process, seeing how spending is matched to areas of serious, rather than residual, risk. Any inverse correlations will then be plain to see. This highlighting provides comfort to decision-makers that spending can be aligned with real risks.

3 DEVELOP REALISTIC OPTIONS

A zero-tolerance approach to error breeds over-control. The point is to have controls that are really needed. Some are prescribed by law or regulation. But many others are self-imposed. Correctly engineering a process can reduce costs by removing counter-productive local measures. A word of warning: don't make cost-cutting your primary goal. Aim instead for that rounded view of operational realities. It might be that effort needs to be redirected rather than reduced.

4 INVOLVE AND EDUCATE DECISION-MAKERS FROM THE START

You need their insights to scope the work, and their support to make changes. Make them aware that it's impossible to eliminate risk entirely. The goal is to strike a reasoned balance by analysing investment and risk together. This approach erodes prejudices, notably the natural organisational bias towards fighting the last war rather than foreseeing new problems.

5 LOOK OUT FOR UNINTENDED CONSEQUENCES

Monitor the effectiveness of the changes you make. There must be a preliminary risk assessment to tease out anything that might go wrong with a new or revised process, especially if it involves taking out controls. Draw on everyday data from multiple locations as the new measures play out. You will need to consider the resilience of your control changes in stressed conditions. Now, as always, knowledge will make for real control instead of the illusion of control. **SR**

Giles Triffitt is a risk director in KPMG's financial risk management division. He was previously head of risk services at The Royal Bank of Scotland

HANDLING DATA

Great contraction reveals price of poor money management

The economic turmoil has exposed flaws and inefficiencies in corporate treasury departments that is costing companies much more than they realise, according to a survey

THE GREAT CONTRACTION, AS SOME economists are calling it, has greatly multiplied the problems facing corporate treasurers while exposing flaws in treasury functions.

As McKinsey researchers Tim Hesler, Kevin Laczkowski and Paul Roche point out in a November survey of 170 companies worldwide, "too many corporate treasuries [were] left lagging behind on even core activities in their home markets". In short, they were found out by the crisis and its continuing aftermath.

Deficiencies covered the gamut, the researchers say. Cash management, banking, debt and funding, investments, and risk management for currencies and interest rates – few firms were up to speed.

The price of these shortcomings is probably higher than many treasurers believe. It includes higher interest costs because of over-borrowing, unhedged exposures in currencies and interest rates, needlessly high tax payments (especially when cash moves through tax-heavy regions), and damage caused by fraud.

But arguably the highest price is paid in loss of liquidity. A dearth of funds may mean missed financial covenants, trigger a scramble for high-priced short-term debt, result in credit-rating downgrades or, in the worst but sadly common scenario of the last three years, tip a company into bankruptcy.

The good news is that there are several tried and tested ways of raising your game.

1 MAKE THE MOST OF YOUR WORKING CAPITAL

Stephan Benckendorf of consultancy Hanse Orga says every company has an internal capital market that can be tapped for liquidity. "Corporates can often find potential capital that had not been explored," he says. Just one important element is days sales outstanding (DSO): efficiency gains of 10%-30% are possible through more timely payments from customers. Make this happen

KNOWLEDGE

Accounts can grow like topsy

COMPANIES WITH CROSS-BORDER operations typically end up with a high-risk plethora of bank accounts. Some treasurers don't even know how many they have, but most global organisations own up to about 850 accounts, while even the best have around 200. But the rewards of figuring them all out are considerable, as one heavy-materials company found after analysing cash balances in 300 accounts in 25 countries. The treasurer discovered the company held a daily average (taken over three months) of over $80m. And as none of it was invested, the cash was doing nothing.

DEBT CRISIS

The European debt crisis has spread to Italy and Spain, taking crisis fears to a new high. Could the most eurozone-exposed UK insurers present a threat to the industry as a whole? Download our infographic to find out: goo.gl/5fqZd

Global companies can have up to 850 bank accounts – and even the best have around 200

istockphoto.com

by automating instruments such as processing of bank statements, remittance advice, lock boxes and other cash application measures. Accounts payable can be given the same treatment. The return is counted in reduced bank costs.

2 'CASH POOLING'

This means the surpluses of a subsidiary are routinely identified and tapped to maintain liquidity across the business or even invested in short-term opportunities.

3 REAL-TIME VISIBILITY AVOIDS EXPENSIVE MISTAKES

With transparent cash balances and bank accounts (see box, opposite), treasurers can measure exactly the organisation's liquidity. "Treasuries should pull down these files automatically through a scheduled routine before they start their business day," says financial risk management consultancy Reval's vice-president Jason Torgler.

4 ACCURATE CASHFLOW FORECASTING IS ESSENTIAL

According to McKinsey's researchers, "nearly half of the treasurers surveyed reported their cash forecasting was less than 80% accurate". The chief financial officer of one international airline did not know if he would have the money to pay for aircraft when they were due for delivery.

5 RUN "WHAT-IF" CASH SCENARIOS

This will determine where the company would stand in the event of liquidity-affecting shocks, such as major commitments on essential infrastructure like aircraft. The global treasurer at one US-based conglomerate woke up his far-flung team with a 5am telephone call announcing a simulated disruption. The resulting hasty tests helped hone operational readiness for the real thing.

6 MAINTAIN HIGHER THAN NORMAL CASH BALANCES

"This is particularly true as bank relationships and fee structures change, counterparty risk exposures evolve, and foreign exchange markets continue to be volatile as the result of the eurozone crisis," adds Reval's Torgler.

7 INVEST IN BETTER SYSTEMS THAT CAN AVOID EXPENSIVE MISTAKES

Spreadsheet-based programmes are now considered inadequate because they can mislead management into borrowing instead of investing, or making unnecessary hedging and other wrong decisions. The treasurer of a US-based agrichemical group wired $80m (€59m) to the wrong payee in the wrong country because of a simple data error. By the time the mistake was discovered, currency rates had moved against the company and it cost a lot more than $80m to unwind the payment.

8 THE ULTIMATE SOLUTION FOR TURBULENT TIMES COULD BE A DASHBOARD IN A 'TREASURY COCKPIT'

The best companies are installing F1-style read-outs that flash warnings about liquidity risks specific to the group. The alerts may highlight at-risk payments, breaches of counterparty limits, mistakes in cashflow forecasts, imminent breaches of bank covenants and other potential liquidity threats. **SR**

WHAT'S INSIDE YOUR HEAD?

Headspace

Electrolux's group risk vice-president ***Lennart Edström*** *believes in people and admires those who stand up for what they believe in, regardless of the consequences*

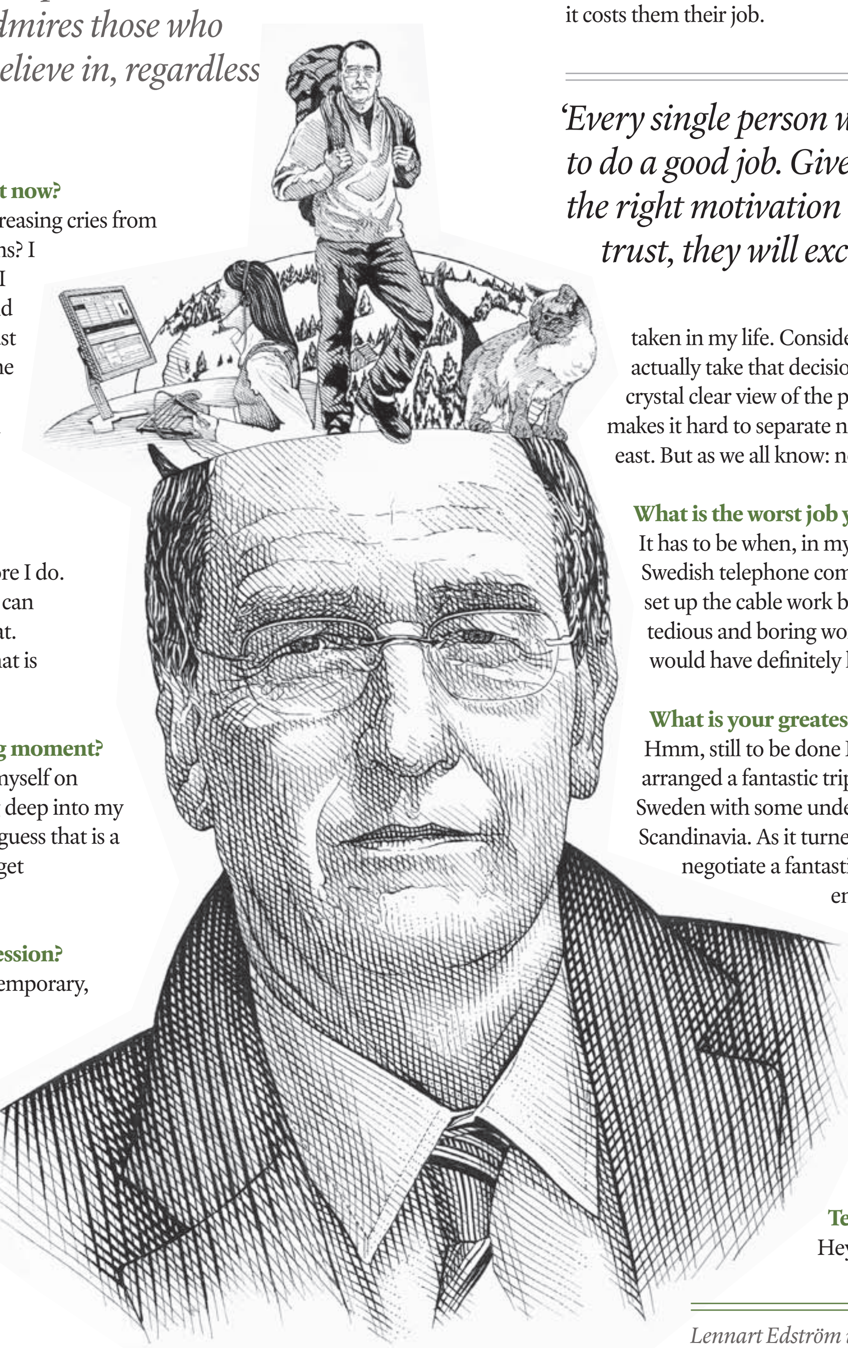

Illustration by Richard Phipps

What are you thinking about right now?
How am I going to meet the ever-increasing cries from insurers for more and more premiums? I may go elsewhere or I may ignore it. I may choose to increase retentions and change the policy wording. I could just pay it, of course, or just jump from the nearest bridge. Another matter occupying my mind concerns critical supplier dependencies within our group.

What is your greatest fear?
That someone in my family dies before I do. That absolutely terrifies me. I think I can cope with most situations but not that. Maybe that is an egotistic view but that is the simple truth.

What was your most embarrassing moment?
I am convinced I have embarrassed myself on more than one occasion. But digging deep into my mind, I can't find anything special. I guess that is a gift in itself, being able to quickly forget my shortcomings.

What is your most treasured possession?
Any "most treasured possession" is temporary, which indicates the low value that possessions really have in my mind. That said, it is probably my iPad (after my kids taught me how to use it).

What makes you happy?
Seeing my kids (who are not really kids anymore) handling themselves in a good way. That makes me really happy. It means that my mission is (almost) completed.

What makes you unhappy?
Calling IT helpdesks is undoubtedly one of the most deeply unhappy things a man can have to do.

Who is your greatest hero?
That changes from month to month. Right now I think it is our cat (it has patiently followed us from place to place. Most recently, we moved from a suburb of Stockholm into the city itself. A difficult thing for a cat to get used to).

Seriously speaking, a hero for me is anyone who dares to stand up for what they believe in, regardless of the consequences, even if it costs them their job.

'Every single person wants to do a good job. Given the right motivation and trust, they will excel'

What's the biggest risk you've ever taken?
Without a doubt, it was marrying my wife. She turned out to be a winner but that must be the most risky decision I have ever taken in my life. Considering the state you are in when you actually take that decision, I don't think you really have a crystal clear view of the pros and cons. The infatuation makes it hard to separate north from south and west from east. But as we all know: no risk, no reward!

What is the worst job you've ever done?
It has to be when, in my late teens, I worked for the Swedish telephone company in their workshop. I had to set up the cable work behind switchboards. It was very tedious and boring work. If I had been my own boss, I would have definitely kicked me out without mercy.

What is your greatest achievement?
Hmm, still to be done I hope. Possibly in the 1990s when I arranged a fantastic trip to the wilderness in northern Sweden with some underwriters from London and Scandinavia. As it turned out I simultaneously managed to negotiate a fantastic premium discount for my former employer. Today, this kind of deal might be classed as bribery – but it was a different era back then.

What is the most important lesson you've learned?
That people matter. Every single person wants to do a good job. Given the right motivation and trust, they will excel.

Tell us a secret?
Hey, if I did, it wouldn't be a secret. SR

Lennart Edström is vice-president of group risk management at Electrolux

"A typhoon in South China wrecked power lines, factory units and the career of a risk manager in London"

A typhoon doesn't just wreck buildings, it destroys production targets, goodwill and reputations. That's why FM Global believes that the best insurance is the kind you never need. So, we don't just insure, we help you to prevent. At our US $123 million research centre, we test just how well your buildings will stand up to a typhoon. We visit critical sites in your supply chain to make sure they're structurally sound. And we work with you on a long-term strategy to lower risk. In short, we don't just help to secure your roof, we help secure your future. Speak to your FM Global representative or contact your broker, and visit www.fmglobal.co.uk/touchpoints to read our latest White Papers.

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