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As rising global temperatures increase catastrophe risk how can businesses best protect themselves?

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In uncertain times, a self-preservation strategy is key

WE LIVE IN UNCERTAIN TIMES. THE PAST FEW WEEKS HAVE SEEN THE emergence of potentially significant events in terms of human health, political stability and natural disaster. A major outbreak of the deadly Ebola virus is threatening Guinea, moving at alarming speed. Without effective containment procedures, a crisis of great magnitude could endanger the lives of people within and beyond its borders.

Meanwhile, after years of relative stability, relations between Russia and the West have deteriorated following the annexation of Crimea in the wake of the recent uprising in Ukraine. President Vladimir Putin's foreign policy intentions remain as yet unclear, but are no less concerning. News Feature (pp10-12) examines the resurgence of nationalism and protectionism in Europe.

Across the Atlantic, inhabitants of the American west coast could be forgiven for ignoring rising tension with Russia for they are bracing themselves for the much-feared earthquake known as the 'Big One', following several relatively strong tremors and sizeable aftershocks. At the time of writing, it was too early to tell whether an 8.2 magnitude quake recorded off the coast of Chile added to or allayed those fears.

Natural catastrophes are the main theme of this issue of *StrategicRISK*. With businesses having extensive international interests, in terms of customer base, supply chain or both, catastrophe events, wherever they strike, are no longer the sole domain of major multinationals.

Catastrophe events, wherever they strike, are no longer the sole domain of major multinationals

What happens on the other side of the world can have major operational consequences. Although the nature of catastrophes makes them impossible to prevent, businesses can adopt mitigating strategies to minimise damage and disruption. Risk Indicator (pp6-7) examines a year of weather extremes recorded since early 2013, and Risks (pp19-23) considers why major events seem to be more frequent and also reviews some of the latest advances in catastrophe modelling.

Catastrophe events can affect the food and drink sector, but there are many other key risks of greater significance and immediacy. These are explored in Sector View (pp28-31) along with developments in mitigation and risk transfer strategies. Among those risks lies the threat of legal action.

Where once the only route for corporate crime was prosecution, now authorities can, in some instances, pursue US-style deferred prosecution agreements. The Legal section of Governance (pp40-43) reviews what this means for risk managers and their businesses.

In such uncertain times, the need for companies to have an effective self-preservation strategy for most eventualities, remains a constant. **SR**

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TOP ONLINE BUSINESS STORIES

POLITICAL

Ukraine crisis exacerbates political risk for Nordic firms

Nordic firms could feel the effect of potential economic sanctions placed on Russia by the EU, according to Willis's head of Nordic financial solutions specialist unit, Azzizza Larsen.

Larsen said: "Nordic companies will be bracing themselves for what could become an ongoing stand-off between Russia and Europe in relation to Ukraine.

"If… the EU decides to impose wider economic sanctions, it will affect Nordic companies because Russia is one of the two largest emerging market trading partners together with China for the Nordic countries, particularly in Finland and Sweden."

web. *bit.ly/1hG9SGc*

CYBER

Demand for cyber insurance in Europe increases

Demand for cyber insurance in Europe has increased significantly, according to Paul Bantick underwriter for technology, media and business at Beazley.

Bantick said: "In the past six months, we have seen a shift in the demand for cyber insurance and the industry has really become the main service provider in helping clients manage breaches. "Today, the lion share of business growth for Beazley has been in the US. But in the past 12 months, we have seen some rapid growth in Europe. Many large telecoms companies, large financial institutes and retailers are looking at events in the US and then at events in Europe, and are realising that they need to protect themselves."

web. *bit.ly/1nWX5qo*

Middle Eastern energy firms are highly adept at responding to an evolving risk landscape

TRADE CREDIT

Multinationals drive trade credit market growth

Multinationals are showing an increased appetite for trade credit insurance, which is stimulating market growth, according to Marsh head of trade credit UK and Ireland Tim Fisher.

Fisher said: "Various things are driving the growth in the trade credit market. The world is more connected than ever, with increased and faster communication. This is giving companies confidence to trade and invest in new markets, with new customers."

web. *bit.ly/1nWX5qo*

ENERGY

Middle East energy firms lead the way in risk management

Energy firms in the Middle East are able to respond to the ever-evolving risk landscape and have an above average approach to risk management, compared with global peers.

This was the conclusion of Marsh's *Benchmarking the Middle East Onshore Energy Industry*, which found that risk management in Middle Eastern firms is of a higher standard compared to more than 500 global oil, gas and petrochemical facilities.

The report cited hardware as a key strength for energy companies in the region because of land availability, substantial capital investment and the development of modern facilities.

web. *bit.ly/1rtE5Ps*

INSURANCE (EMEA)

AIG EMEA restructure creates new management roles

The Europe, Middle East and Africa (EMEA) region of AIG has announced new appointments after a restructure of its management team.

The team will now manage eight zones instead of 47 countries from consolidated headquarters in London.

In addition, two new strategic leadership roles and eight new managing director positions have been created.

web. *bit.ly/1fVjlLv*

INSURANCE (UK)

XL offers kidnap and ransom cover

XL has expanded its crisis management team's capabilities to provide insurance cover for kidnap and ransom risks for corporate clients and high net worth individuals.

Charlie Matheson was appointed kidnap and ransom senior underwriter in London and Jonathan Beck is his equivalent in Guernsey.

web. *bit.ly/1muBb9i*

SUPPLY CHAIN

Asia named hotspot for shipping losses and piracy

Greater naval capability would enable Indonesia to cope with a wider range of maritime piracy threats between the Malay Peninsula and Sumatra, according to senior marine risk consultant at Allianz Global Corporate and Specialty Captain Jarek Klimczak.

Klimczak said the Strait of Malacca was one of the world's "two most strategic chokepoints" for oil trade along with the Strait of Hormuz in the Persian Gulf.

"Estimates suggest that about one-third of the world's trade still moves through this waterway, so… piracy continues to thrive there."

web. *bit.ly/OVDJ4X*

CYBER (GLOBAL)

Burgeoning black markets facilitate cyber crime

Black markets for cyber criminals (darknets) are facilitating innovation and development of cyber attacks on businesses and governments, according to not-for-profit research organisation RAND

Greater anonymity capabilities in malware and a wider adoption of crypto-currencies will further support the lucrative underworld for hackers. As a result, experts predict the ability to stage a cyber attack will outpace the ability to defend against one.

RAND information systems analyst and lead author of RAND's research report, Markets for Cybercrime Tools and Stolen Data, Lillian Ablon said: "What makes these black markets notable is their resilience and sophistication. Even though consumers and businesses have fortified their activities in reaction to security threats, cyber criminals have adapted.

"In certain respects, cyber crime can be more lucrative and easier to carry out than illegal drug trade."

web. *bit.ly/1fGm2x7*

INSURANCE

FERMA urges caution on EU insurance contract law changes

FERMA urged the European Commission to take a cautious approach to any regulatory changes to EU insurance contract law.

Ferma responded to the final report by an expert group that has been considering whether differences in contract law between EU countries are an obstacle to the cross-border provision of insurance.

The association welcomed the conclusion of the expert group that insurance products for large risks are already widely distributed on a cross-border basis.

web. *bit.ly/1j9lXXc*

REPUTATION (MALAYSIA)

Missing MH370 flight handling threatens reputation

The handling of missing Malaysia airlines flight MH370 may be an example of poor crisis management, according to a Singapore-based aviation risk expert who spoke to *StrategicRISK* anonymously.

"The leaders managing the crisis and facing the media are not properly media trained. Was there a crisis communications plan and did they leaders stick to it?".

web. *bit.ly/OrzHRd*

ONLINE CONTENTS

Most read stories

Opinion: "I challenge risk managers to volunteer to become a member of the board"

web. *bit.ly/1mcmr1z*

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COMMUNITY UPDATE

FERMA is to publish its first European Risk and Insurance Management Report incorporating the results of the 2014 FERMA Benchmarking Survey, which began last month.

FERMA wants to create a reference work for risk and insurance managers in Europe that will also provide a tangible basis for reporting to senior management on risk management. The report will be published at the FERMA Seminar on 20-21 October.

This seventh edition of the survey, which takes place every other year, will be more quantitative and practical and provide more benchmarks for comparison than previous versions.

Cristina Martinez, leader of the survey project group and a FERMA board member, said: "We believe that by strengthening the quantitative nature of the survey we can produce a report that has lasting value both for individual risk and insurance managers and for our member associations to further explore the issues that the survey will highlight. It will also provide a sound basis for analysis of developments with future surveys."

Anton_Ivanov / Shutterstock.com

Indonesia needs better naval capability to deal with pirates in its waters

Hot stuff

Increasingly volatile weather is becoming a global trend and businesses need to be prepared for extreme and unprecedented disruptions

FROM SNOW IN THE MIDDLE EAST TO RECORD high temperatures in Greenland, the past 12 months have produced some extraordinary weather and kept businesses on alert around the world.

The increasingly global nature of commercial operations means catastrophes and extreme weather events have widespread repercussions and affect organisations across many continents. However, it's not just a side-effect of globalisation that is raising the risk profile of natural catastrophes and extreme weather events. The frequency of such events appears to be increasing too.

A sharp rise in the number of billion-dollar events is evident since 2010 in Aon Benfield's *Impact Forecasting 2013* report. Between 2003 and 2013, the average number of billion dollar events per year was 28. However, this figure was not reached until 2010 and subsequently exceeded each year thereafter.

Reasons for the increase in severe weather are widely debated, with global warming at the forefront of discussions, although experts cannot confirm or eliminate these theories owing to the lack of longitudinal evidence.

Typhoon Haiyan, which killed more than 6,000 people in the Philippines in November 2013, was the strongest tropical cyclone on record to make landfall. Professor Nigel Arnell, director at the Walker Institute for Climate System Research, says Haiyan is likely to be followed by equally devastating typhoons in the near future. "We can't definitively say that tropical cyclones have become more or less frequent, but indications show intense cyclones might become more frequent. The analogy we use is the rolling dice; you could get two sixes by chance but when you get too many sixes, you suspect the dice are loaded."

Haiyan was followed by severe winter storms in the Middle East in December. Snowfall caused major disruptions in parts of Egypt, Jordan and Lebanon that had not seen snowfall for decades.

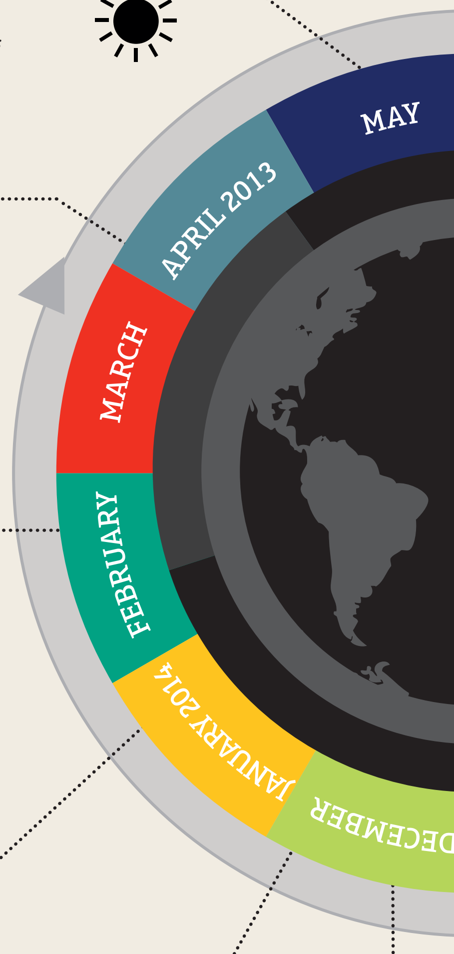
It is not just the weather that has been unprecedented. In February 2013, a 20m-wide meteor smashed into the earth's atmosphere near the Russian town of Chelyabinsk and exploded with the energy of about 500 kilotonnes of TNT. More than 1,000 people were injured and, at its most intense, the rock shone 30 times brighter than the sun, burning the skin of onlookers.

Eleven months later, a shift of the polar vortex covered Canada and most of the US in ice. More than 30 people were killed, with temperatures falling to record lows of less than -30°C in the northern state of Minnesota and snow fell in usually more temperate states such as Florida. Meanwhile, the period between 1 December 2013 and 31 January 2014 was the wettest in England and Wales for 248 years as record rainfall drenched the UK and other parts of Europe. Australia experienced its warmest year on record and was forced to declare a state of emergency in New South Wales as bush fires burnt almost 200 homes.

In its 2013 annual climate statement, the World Meteorological Organization (WMO) said: "Comparing climate model simulations with and without human factors shows that the record hot Australian summer of 2012-13 was about five times as likely as a result of human-induced influence on climate." The report also revealed 2013 was the joint hottest year on record with 2007 and that the coldest average years are now hotter than the hottest average years prior to 1998.

Climate change may or may not be behind the apparent increase in the frequency of extreme weather, but according to the WMO, the world is getting warmer and sea levels are rising. **Asa Gibson**

A YEAR OF EXTREMES



BRAZIL

Brazil endured its worst drought since 1979. North eastern states of Minas Gerias, Pernambuco and Bahia lost at least half their cattle herds and agricultural crops were devastated

ARGENTINA

Flash flooding in Argentina saw an astonishing 300mm of rainfall in three hours in the La Plata region. It was more than the city had ever recorded in an entire month of April

AUSTRALIA

After enduring a record 19 consecutive days of 26°C-plus weather, flash floods soaked Sydney and surrounding areas. More than 64mm of rain fell in the suburb of Bankstown in one day, where the median monthly rainfall is 97mm

JAPAN

Record snowfall in Japan killed at least 37 people in a 10-day stretch and caused disruptions to transportation and significant damage to the agricultural sector

EUROPE

Windstorms Xaver and Dirk caused more than €1.63bn in economic damages in Northern Europe. Meanwhile, extreme snowfall killed at least 10 people in the Middle East

ENGLAND AND WALES

The wettest two months for 248 years in England and Wales concluded at the end of March 2014. Meanwhile, the US was coated in snow and ice at sub-zero temperatures owing to a shift of the polar vortex

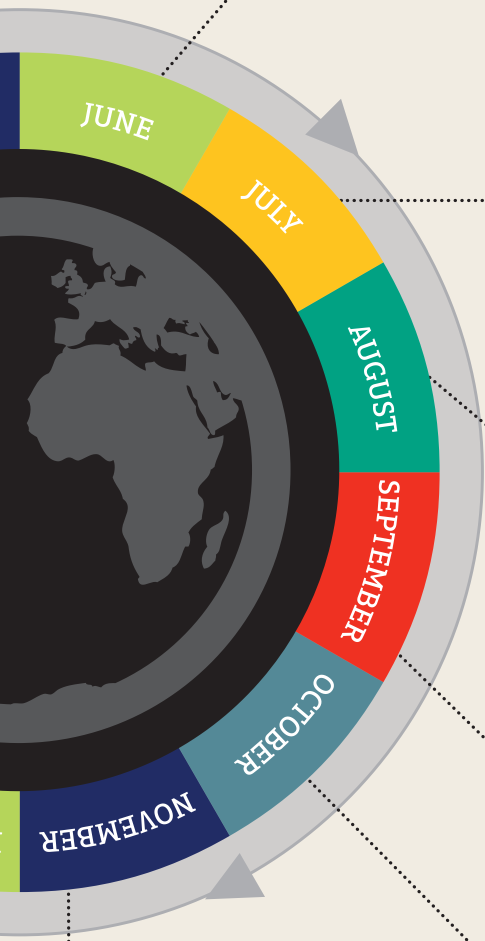
BIG NUMBERS

47.3°C

SOUTH AFRICA

Highest March temperature recorded in Vioolsdriff and 0.5°C short of the highest March temperature ever recorded on earth

Last year was the joint hottest year on record globally, according to the World Meteorological Organization. Rising temperatures caused 12 months of extraordinary weather around the world.



CENTRAL EUROPE

Flooding across Central Europe resulted in estimated economic losses of €16.5bn. The Passau River in South East Germany saw its highest water level since 1501

THE WORLD

Together with 2007, 2013 was the hottest year on average since records began. The World Meteorological Organization's annual report states the global oceans reached record high sea levels

RUSSIA, CHINA & MONGOLIA

The worst rainfall in more than a century submerged large areas of Russia's Far East and neighbouring regions in China and Mongolia. One township in North East China endured half of its average annual rainfall in one day

MEXICO

Hurricanes Manuel and Ingrid hit both sides of Mexico within 24 hours, causing an estimated €4.14bn in economic damages. Super Typhoon Usagi made landfall in China's Guangdong province, killing at least 47 people

PHILLIPINES

Typhoon Haiyan became the strongest typhoon ever recorded to make landfall, killing more than 6,000 people in the Philippines, leaving widespread devastation of the region

AUSTRALIA

Australia's hottest year on record saw wild bush fires destroy almost to 200 homes and a state of emergency declared in the state of New South Wales

25.9°C

GREENLAND

Greenland's highest ever temperature recorded in Maniitsoq, July 2013

€5.79bn

BRAZIL

Estimated damages inflicted by Brazil's worst drought since records began in 1979

5,700

US

The Black Forrest Fire burnt 5,700ha in nine days in Colorado in June 2013

Source: Sydney Morning Herald, WMO, Climate.gov

TOP FIVE

Renewable energy

1. Solar thermal power
The solar thermal power sector grew in terms of average annual capacity and production by 18% globally in 2012, according the REN21 2013 annual report.

2. Solar PV
Conversely, solar photovoltaics, known as solar panels, fell by 18% in 2012 to an average of 42%.

3. Germany
Renewables accounted for 22.9% of Germany's electricity consumption (up from 20.5% in 2011), creating more electricity than its nuclear, gas-fired, or hard coal power plants (but not lignite plants).

4. BRICS
The BRICS accounted for 36% of total global renewable power capacity and almost 27% of non-hydro renewable capacity by the end of 2012.

5. $500bn (€354.5bn)
Predictions show investments in renewable energy of up to $500bn annually by 2020–25.

"SOUNDBITES"

'You have a certain budget. You have limitations. Just make sure you spend it in the right places'

Cath Geyman, Intersys

>> see **Risks, page 20**

'Traditional property and liability exposures associated with the manufacturing, storage and transportation of goods remain the main insurable risks"

John Keating, Sainsbury's

>> see **Sector view, page 28**

'The past few years have seen an increasing political imperative in the UK to hold corporates to account for criminal conduct'

Judith Seddon, Clifford Chance LLP

>> see **Governance, page 41**

Forex rigging scandal set to cause rush of D&O insurance claims

With the Libor scandal still creating havoc in financial circles, banks are bracing themselves for another costly problem

THE FOREIGN EXCHANGE MARKET (forex) manipulation scandal has grown like a mushroom cloud. What started as the suspicions of a few individuals in 2012 is now a global probe involving 15 banks and a dozen regulators.

The affair is, according to an investigation by *StrategicRISK*'s sister publication *GR*, predicted to worsen and to exceed the cost and severity of the London interbank offered rate (Libor) scandal, which it resembles.

So far, investigations have uncovered suspected rate-rigging and shed light onto the shadowy underbelly of forex trading.

How much more serious will the case become and what might the consequences of forex manipulation be on the directors' and officers' (D&O) insurance market?

Alleged offences

The alleged offences centre on the accusation that some traders manipulated the main forex benchmark rate, known as the WM/Reuters rate, which is set at 4pm in London every day and is based on the number of trades placed during a 60-second window.

The forex market is dominated by big banks that place trades for their clients and themselves. Manipulation allegedly occurred when traders conferred strategically to place trades at certain times around the window to manipulate the WM/Reuters rate and maximise their profits. In forex trader slang, this practice is known as 'banging the close'.

The investigations are still at an early stage and, so far, no wrongdoing has been proven. Evidence shows that traders manipulated the WM/Reuters rate; however, proving that this harmed banks' clients is easier said than done.

DAC Beachcroft partner Richard Highley said: "Is the client losing? There is still that second step you've got to take.

"On the basis that banks are being asked to trade for their clients, obviously, they are making a profit off the spread. So yes, you would say there must be, because that spread is based on the daily fix. So yes, there would be a likelihood of detriment.

"You've then got to work out: what is that detriment? Like Libor, that becomes the more difficult process."

Willis financial and executive risks team executive director Julian Martin says that "if the regulators in the UK, US, Switzerland and Hong Kong find evidence of wrongdoing, substantial fines are likely to be levied against the banks and regulatory actions taken against individuals, which could include directors and officers, who condoned the behaviour. The fines would not be covered by D&O insurance but defence costs incurred by individual D&Os brought about by a regulatory investigation should be."

Martin adds that any big bank fine could then cause D&O claims from shareholders alleging damage from allowing the forex fixing to take place.

The forex allegations are similar to the Libor scandal, in which banks rigged the rates at which they lent to each other. This led to a plethora of fines, D&O claims and costly civil litigation.

Perhaps because of the spiralling cost of the Libor scandal, banks are taking the forex allegations seriously.

Banks, including Barclays, Citigroup, Deutsche Bank, HSBC, JPMorgan Chase and UBS have already begun investigations into forex manipulation. The Bank of England has suspended one employee and JPMorgan Chase, Barclays, Citigroup and UBS have also suspended staff.

Highley believes that banks are taking the forex allegations seriously as a reaction to the costly fallout from the Libor scandal. He said: "[Banks] are doing that at a very early stage, and they are doing it in a similar way to which they are approaching Libor, which is to distance themselves or their management from the wrongdoing."

Regulators, including the New York regulator and the UK's Financial Conduct Authority (FCA) are also investigating the issue.

Costly to insurers

So, how serious is the problem likely to become and how worried should insurers be? Early signs show that the forex scandal could cost banks even more than Libor.

Bank of England governor Mark Carney, testifying to the UK government's Treasury Committee in March about forex, said: "This is extremely serious. As [FCA chief executive] Martin Wheatley has rightly said, this is as serious as Libor, if not more so – time will tell – because this goes to the heart of the integrity of markets. We have to re-establish the principles of fair markets so that people in markets know how to behave."

Sedgwick Law partner Jennifer Broda says: "It is likely to be more severe than Libor. That is because, in part, the manipulation that occurred was more direct than occurred in Libor and was actually based on trades."

The potential for D&O claims arising from the forex allegations is obvious and lawyers agree insurers may see many claims.

Pinsent Masons partner Alexis Roberts says that this almost certain. He adds that this is a particular possibility in the

the UK, as the FCA is showing a particular interest in senior management responsibility.

Sedgwick Law managing partner Eric Scheiner thought numerous D&O claims are likely, but added: "I think those will likely, if they happen, be on the back of any anti-trust liability or large regulatory settlements."

To add to the problem for insurers, DAC Beachcroft partner Jonathan Brogden believes the potential pool of D&O claimants is much larger for forex than for Libor.

"With forex, you've got a much more direct link between those people who can claim to be affected by any allegations of wrongdoing on the part of the banks, which were actually making the trades, and therefore also more directly affecting the daily fix," he said. "For forex, I would suggest they have more cause to bring a claim."

But will the culprits be sufficiently senior for claims to result in D&O payments? The banks have suspended traders of all ranks, if that is anything to go by. Of course, the forex investigations are still at an early stage, and it is unclear which individuals, irrespective of their seniority, have done anything wrong.

But for many D&O policies, rank is no longer relevant, because policy wordings cover employees other than directors and officers.

There has also been hot debate in the insurance world as to whether D&O policies should pay out when fraud is involved.

Brogden says: "Where the fraud or illegality is obvious, something that has been talked about in the market previously is whether the policy should respond.

"The commonly held view is that this type of policy is intended to advance defence costs, even where insurers are thinking 'yes, but this individual doesn't deserve insurance, this is a case of fraud, and we can approve it even if the police cannot prove it'."

Insurers can, of course, reclaim these costs after individuals are found guilty in court, but this is little consolation when these individuals are often unable to repay them.

Unlikely to harden rates

So, how will forex rigging affect the future of the D&O insurance market and is there any good news for insurers?

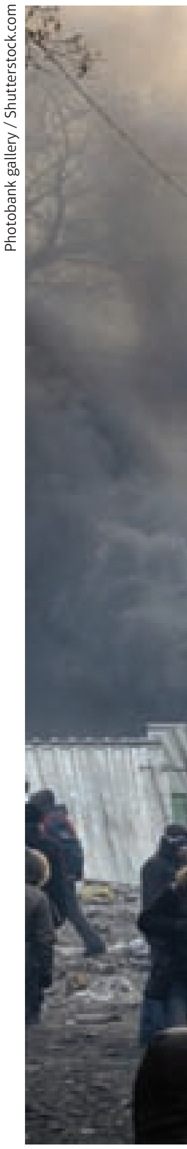
It is unlikely that the forex scandal will lead to rates hardening in the notoriously soft D&O market.

"If losses are great, then for banks we might see a rise, but the market has constant new entrants and has been soft on rates for years," Highley says.

However, the publicity surrounding forex and D&O could at least increase penetration of the insurance, according to Roberts.

"I would have thought that as soon as we start seeing some profile around enforcement action or civil claims on senior management, there will be more of an appetite for people to buy these products," he explained.

For insurers, the full consequences of the forex allegations are unclear because the alleged wrongdoing is still unclear. It is almost certain that insurers will face numerous D&O claims, but the full cost and nature of these claims will be revealed only once the regulatory and bank investigations have run their course. However, insurers and banks will surely be hoping that, following the unearthing of the Libor and forex scandals in the space of only a few years, no more costly cases are waiting to emerge. **Sam Barker, SR**


Photobank gallery / Shutterstock.com

A NEW DAWN IS RISING

Nationalism, in various shapes and forms, is now increasingly dominating the political landscape in Europe

THE RAPIDLY CHANGING events in Ukraine and Crimea have shown how political stability should never be taken for granted.

Unrest is bubbling away not only in the East but also across the wider European continent as the sense of shared direction starts to fade and borders rise up again. Suddenly, the world is looking inward once more, attitudes are hardening and extremism thriving.

Historical anomalies are also being addressed, hence Russia's reintegration of Crimea. To some an opportunistic land grab – to others, not least the overwhelming majority of Russians living there – it is merely correcting a mistake of the past after Nikita Khrushchev 'gifted' the peninsula to the Ukraine in 1954.

National identity forms an intrinsic part of what is currently developing in many parts of Europe.

From the rise of UKIP to the revolution in Ukraine, from Greece's neo-Nazi Golden Dawn to the separatists in Catalonia, the pigments of nationalism in their various shades and textures are increasingly dominating the palate of political debate.

"The key driver at the moment is that more support for nationalism, primarily in the form of support for nationalist parties, but also in terms of more radical movements, is a response to worsening socio-economic conditions coupled with the failure of elites to deal with the current situation or prevent the crisis in the first place," says Dr Florian Otto, head of Europe and Central Asia at Maplecroft. "In Eastern Europe, it is also about the failure to deliver development, coupled with issues of institutional weakness and corruption".

Stuart Poole-Robb, chief executive of KCS Strategic Intelligence and Corporate Security, agrees: "We've come to a point where we are just coming out of a really nasty recession that has affected people's attitudes commercially and politically, and that as a consequence you've got a lot of unrest and a lot of minority groups in a strong position because of this weakness.

"In many ways the rise of nationalism in Europe is an expression of a broader and deeper instability across the world."

The change can also be understood as a reaction to globalisation and the impotence felt by populations who increasingly believe that remote, supranational decision-making is having too great an effect on their daily lives.

"The eurozone crisis has reinforced this," says Otto. "There is a sense that decisions are made in Brussels, Paris or Berlin and imposed on other states."

This perception is being used by politicians on the left and right, safe in the knowledge that the public and the media will pick up these themes.

"Thanks to modern technology, there's a lot of collaboration between nationalist groups across borders and we are seeing a domino effect," says David Lea, senior Europe analyst at Control Risks.

"For example, with the 'angry nationalists', their focus in the late 1990s and early 2000s was often on Islam and immigration, whereas, in recent years, this seems to be resonating less well than it was when terrorist attacks were to the fore, and they have changed focus to the EU, intra-European immigration and its effects on daily life. They are looking around them and seeing what works elsewhere."

Exploiting perceptions

In addition, because nationalism flowers on deep roots, perceptions of history are another accelerant to the rise of populist parties across Europe.

"Where there is a sense of 'past injustice' this can be seized on and exploited," says Otto.

"An example would be Ukraine and Russia. In the west of the country, there is a widespread sense that the country was repressed by first Imperial Russia and then Soviet Russia; while in the east, there is a sense of belonging to Russia and being removed from Russia.

"In the Balkans, with the centenary of the First World War coming up, [history] is a big deal, especially in Serbia. In all the countries of the former Yugoslavia, nationalism is linked strongly to a sense of past injustice. More recently, the civil war has added further friction. You have a combination of legacies being used as a political tool."

Faced with this situation, it becomes ever more important for businesses to understand their operating environment and prepare, not only for social and economic unrest, but the risk posed by populist political agendas and an anti-multinational backlash.

"If an organisation has the commitment, expertise and financial wherewithal to operate overseas, then it should," says Poole-Robb.

"But it should choose its markets with care. The problem is that even companies that we would regard as major players simply don't have these things in place. I call it commercial malaise: a mixture of arrogance, ignorance and naivety. All of these major companies suffer from it to some degree; they all think that they know better."

Avoiding complacency by having the right intelligence is becoming critical.

For example, country profiles are becoming more complex as regional issues become more and more important.

'The key driver at the moment is that more support for nationalism is a response to worsening socio-economic conditions coupled with the failure of elites to deal with the current situation or prevent the crisis in the first place'

Dr Florian Otto, Maplecroft

"It is no longer enough to do your research at a country level, you need to look deeper and understand more fully the detail of what is going on," explains Otto.

Stuart Poole-Robb says: "People don't know enough about the countries with which they are involved. There are plenty of things wrong within our own region before we even start going to North Africa or the Middle East."

Looking out at the broader European context is also important. "There is much greater difference now within the EU," says Otto. "Although I believe companies have always realised that there is a difference between investing in Germany and Romania... what is new, is that you can no longer rely on the fact that newer members will continue along their road to greater convergence.

"If you think about the EU, its appeal is that it offers stability and adherence to a certain set of legal and democratic ideals. If we look closely, there might be a change. Especially when we talk about eastern and southern Europe and businesses need to seek guidance before they go there."

The question should be asked as to whether there is an independent, functioning judiciary that can deal with issues without political interference – and perhaps more importantly – respond independently to political interference.

"Although though there are trends, when it comes to your actual operations you have to look at every investment on a case-by-case basis," says Lea. "It's dangerous to draw too many parallels." »

'Although nationalist movements rise and fall, and at the moment we are in a peak of activity, in the future, the troughs are going to be a lot less shallow'
David Lea, Control Risks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» It is also important for companies to be aware that they, as foreign investors, could be targeted by campaigns or scapegoated in certain situations.

"You need to be thinking about how you can influence public perception," says Otto. "If you can make a strong case for the benefits you bring to a country, you can expose politicians when they start to go for easy answers.

"Make sure you don't confirm prejudices that you are exploiting regulatory loopholes or otherwise taking advantage."

There is the potential for significant change in the months and years ahead – and this is not restricted to countries usually considered the more volatile.

In September, people in Scotland will vote in a referendum to determine whether the country will remain part of the UK. The results will be watched closely across Europe, particularly in Catalonia, which wants to gain independence from Spain.

Meanwhile, British prime minister David Cameron, should he remain in power after the country's general election next year and gain a majority, will oversee a vote that will allow the public to decide if the UK remains in the EU. Although that proposed referendum is another three years away, it has already created uncertainty.

Instability here to stay

The risks presented by these complex operating conditions look set to become the new normal for doing business in Europe.

"Although nationalist movements rise and fall – they always have – and at the moment we are in a peak of activity, I believe, in the future, the troughs are going to be a lot less shallow," says Lea. "We are going to have to get used to their presence on the European stage, even if it fades."

The largest factor in influencing how the risk profile develops will undoubtedly be the economy, which, like everything else, remains unstable and uncertain.

"If we understand support for nationalist parties as a response in part to economic problems and as a way of expressing dissatisfaction with existing political elites, then there is the possibility that if these sentiments retreat, so will support for nationalism," says Otto.

But who now expects a unified European recovery anytime soon? Moreover, until that happens, everyone needs to get used to a world where having the same phone and wearing the same trainers do not mean that we are all friends together. **SR**

HUNGARY

In recent years, Hungary has demonstrated the effect populist national politics can have on investor confidence. When the new government came to power four years ago, it embarked on an important regulatory and legislative overhaul.

"It passed hundreds of laws," says Florian Otto, head of Europe and Central Asia at Maplecroft. "More importantly, it changed the constitution to strengthen the power of the executive over the judiciary.

"It has also made attempts to target sectors where foreign businesses dominate. It has high taxes on businesses, particularly on the financial and utility sector, which is dominated by foreign firms – and this has been hugely popular".

Whether these moves are merely tools to win the next election or a major shift in attitude, remains to be seen.

UKRAINE AND THE EU

"Vladimir Putin doesn't miss opportunities," says Stuart Poole-Robb, chief executive of KCS Strategic Intelligence and Corporate Security.

"He has a lot of power through the oil and gas, and a lot of clout through his political structure; he has also wanted to close the back door to NATO for some time. He wants to close the back door to the EU as well."

The revolution in the Ukraine is beginning to look like another Great Game and the country is feeling the pressure as competing spheres of influence – Russia, NATO, the EU, the US – enact their strategies. But while the West is so-far looking weak, perhaps the crisis may yet galvanise some troubled institutions.

"A resurgent Russia might help NATO explain why the alliance exists 25 years after the fall of the Berlin Wall," says Dr Florian Otto, head of Europe and Central Asia at Maplecroft. "It may also help focus US attention back on Europe, and help the EU develop a single position on foreign policy.

"The situation in Crimea might reinforce the view that Europeans are stronger together."


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A MEETING POINT FOR INSPIRATION

PROFILE: JUAN CARLOS LÓPEZ PORCEL

The president of the Spanish risk management association wants it to become a pioneer in the delivery of knowledge

FINISHING HIS CLOSING SPEECH AT a conference in the harbour city of La Coruña in Northern Spain, Juan Carlos López Porcel is clearly pleased.

This is because his first speech as president of the Spanish risk management association, AGERS, in March, marks an important milestone in the association's history. It has signed an agreement with Fundación INADE (INADE Atlantic Insurance Institute Foundation), establishing the start of a long-term partnership to develop risk management training. This will see AGERS and INADE jointly host educational workshops across the country.

"AGERS aims to become a pioneer in the delivery of knowledge", López told *StrategicRISK* after the conference. "A resource that champions development and growth in risk management," he continues.

This may sound like a tall order for an association run by a small team and that represents a fraction of the European risk management community, but López displays little doubt in achieving this aim. When he talks about his achievements during his 26 years at global steel manufacturing company ArcelorMittal, it becomes clear that he has the right skills to bring AGERS's vision to fruition.

As ArcelorMittal's director of risk and insurance for Southern Europe, López likes to advocate a holistic approach.

A robust enterprise-wide risk management strategy, dedication and hard work ensured risk-free transitions in a series of mergers and acquisitions, which helped form the steel-making brand that the world now knows as ArcelorMittal.

The first M&A he was involved in was when Spanish steel producer Aceralia was established in 1997 as a result of the restructuring of the Spanish steel company Corporación Siderúrgica Integral (formed from earlier mergers of the country's steel producers, Empresa Nacional Siderúrgia Sociedad Anónima and Altos Hornos de Vizcaya).

Five years later, López saw the business through successful takeovers of Luxembourg-based steel producers ARBED and France-based Usinor to become Arcelor. In 2006, he was a member of the team who risk-managed the M&A that brought together Arcelor and Mittal Steel to become ArcelorMittal.

López thrives off managing a project from the beginning to the end and these M&As provided the ideal opportunity to do so. Being involved from start to finish "is important", he says of an approach that may sound simple on paper but has evidently worked throughout his career.

"If you're working in the commercial department, simply put, you are only selling. If you're working in production, you focus solely on the process of manufacturing the products," he says.

"But I wanted to be involved in all areas of the business and, as a risk manager, you have that opportunity.

"It is part of my job to check the entire process: how the company is manufacturing its products, how the products reach our customers, how we can improve customer satisfaction, identifying where the revenue streams are, evaluating the balance sheet and income statements of the company, and finally, determining what we need to do to perfect the process – from beginning to end."

López will adopt this conception-to-completion approach to ensure that AGERS provides the right support to its members.

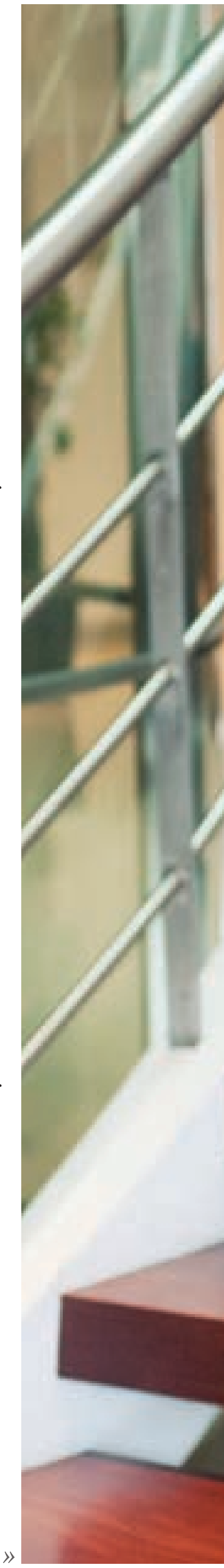
Diving into challenges

Positioning itself to become a resource hub, AGERS aims to develop a community for the exchange of best practice, a network of peer support and a place to learn about new risk management techniques, both face to face in the form of workshops and virtually with the launch of AGERS 2.0, a new web-based forum for members. "I can sum up my vision for AGERS in one sentence" López says: "It is a meeting point to develop inspiration".

AGERS's resources will undoubtedly be valuable to the risk community, particularly as globalisation has expanded the manager's portfolio of risks. As with many European countries, cyber risks, compliance and D&O liability are some of the major threats that Spanish risk professionals are currently juggling.

AGERS's services have already brought about positive change, particularly in helping its members get to grips with the 2007 transposition of the European Liability Directive through its workshops.

The directive 2004/35/EC establishes a framework that defines liability in instances of environmental damage based on the 'polluter pays principle' but "the challenge was much wider than a simple transposition of the rules," López says. »



CV

- President of AGERS since 1 February
- Vice-president of AGERS in 2013 and member of the board since 2009
- Currently manager, risk and insurance management, for Southern Europe & Northern Africa, ArcelorMittal
- Started his career in the steel company ENSIDESA (Asturias - Spain) in 1988
- Holds an Executive MBA, EUDEM, a law degree and a Master in maritime law
- Accredited broker in Spain (DGSFP); accredited expert i n risk management by Mapfre
- Also an associated teacher at Mapfre Foundation and ArcelorMittal University

What are the biggest risks in Spain?

"The risks that top the agenda for Spanish risk managers are regulation and compliance, environmental liability, D&O and professional liability, cyber risks and natural catastrophes.

"The regulatory environment is a major concern. In addition to Solvency II and our efforts to clarify the EU's Environmental Liability Directive, we expect a shake-up of an important local law: the Insurance Contract Act 1980 (Ley 50/1980). This is on the government's table and we await the outcome.

"Employment liability is a big worry as a result of local regulation. In addition, cyber risk is growing and, in a globalised market, the likelihood of suffering a business interruption owing to a natural disaster is on the rise.

"So what are we doing about it?

"We have devised a number of seminars on these risks areas to further support our members. We are co-operating with the regulators and other organisations better to understand how these regulatory changes will affect businesses and then we actively disseminate the information to our members.

"To further ensure that our members have access to the most up-to-date information, whenever and wherever they need it, we have launched a new web forum, AGERS 2.0. By logging in, members have access to a wealth of resources – videos, reports and various literature and a forum to share best practice. Together, these elements form an educational community exclusively for AGERS members."

» "The 2004 directive was transposed in Spain in 2007 with the issue of a local Royal Decree issued by the Spanish government.

"In that year, the government, while respecting the parameters of the directive for transposition, tried to strengthen the preventive aspects of the regulatory framework.

"Now, the Spanish Ministry of Agriculture, Food and Environment is in the process of modifying the Royal Decree of 2007 in order to guarantee an obligation among businesses to prevent and/or repair environmental damage, fomenting environmental risks analysis as an important tool in doing so."

Spanish risk managers now face another regulatory challenge. In 2010, changes to the Spanish Criminal Code (SCC) widened the scope of criminal liability to businesses. The legislation now puts firms in the firing line, which was not the case before 2010. The code now stipulates that, with the exception of government-owned entities, companies can be held liable for corporate crimes committed by its directors or employees, meaning that the business and not merely its directors could face significant aggravated penalties.

Equally as worrying is the code's inclusion of new criminal corporate offences and increased penalties. All these changes have raised concerns over the effect on D&O claims, which have been on the rise since the financial crisis.

"D&O is a big concern right now" López says. "We receive regular questions on our desk from top managers asking for advice on terms and conditions.

"The problem is there is a shortage of insurers that will cover employment-related risks. But risk professionals want to know more, they want to know how best to manage employment liability risks and they want to know how they can build their own defence strategies. As such, we are hosting workshops that focus on regulation and environmental liability. We are also looking at developing tailored services to help our members better understand D&O and professional liability risks – a good example of our dynamic approach and capacity to innovate."

Much to look forward to

As a law graduate, scoping out the regulatory and compliance risks for businesses and drawing up the agenda for these workshops come naturally to López. However, he remains modest about his efforts in devising these seminars and in transforming the association into an essential resource hub. Instead, he puts all the hard work down to his team. "I cannot achieve anything without a team who strongly supports the aims of the association," he says.

"We are a small team but we are putting everything on the table to support our members. The board is also on board with what we are trying to achieve. But a lot of the credit has to go to our new executive general manager, Alicia Soler, who joined in January."

AGERS members have much to look forward to in 2014. In the year that the association celebrates its 30th anniversary, its new president and his team are working to ensure that its goal to "become a pioneer in the delivery of knowledge" is realised through various training initiatives. Undoubtedly, this is a project that López will manage closely – "from beginning to end".

KIN LY

'How do you explain the unexplainable to a global media following a story 24 hours a day?'

OPINION
MIKE JONES
EDITOR, STRATEGICRISK

THE DISAPPEARANCE OF THE CREW OF THE *MARY CELESTE* HAS BEEN THE SUBJECT of bafflement for almost 150 years. In 1872, the ship was discovered abandoned in the Atlantic Ocean with its cargo and valuables still on board, the vessel apparently undamaged. A lifeboat and the seven-man crew were never found, however. This event was popularised by Sir Arthur Conan Doyle in a semi-fictional account in which he put forward his theory regarding the mystery of the 'Marie Celeste'. His story and amended name have over time come to be perceived as the 'truth'.

Over the years, various explanations have tried to rationalise the events – undersea earthquakes, piracy, mutiny and engine problems are among the many suggestions. The most likely theory centres on the ship's cargo of 1,700 barrels of alcohol: when some of these leaked, they released a vapour that exploded. However, because the combustible temperature of alcohol is relatively low, the resulting blast was a shockwave rather than a fireball. This would have been enough to panic the crew to man the lifeboat, yet it would not have caused the type of destruction normally associated with an explosion. The crew then drifted away in the lifeboat and failed to find land before their supplies ran out.

This is a plausible explanation and took more than a century to evolve, but it cannot be taken as fact. Likely does not mean definitely.

One of the *Mary Celeste*'s owners suggested a variation on the combustion theory not long after the discovery of the empty ship, and the advent of recent scientific experimentation has given it genuine credence. However, despite the significant technical advances that have occurred since the *Mary Celeste* event, some incidents still to defy explanation or logic.

On 8 March, Malaysia Airlines flight MH370 left Kuala Lumpur for Beijing. Shortly after taking off, the Boeing 777, carrying 227 passengers and 10 crew, apparently changed course from its scheduled flightplan, headed south across the Indian Ocean and vanished. In the last month, an unprecedented international search involving several countries has taken place, yet, at the time of writing, no trace of the aircraft or those on board has been found.

This extraordinary incident is a mystery that surpasses the story of the *Mary Celeste* because it is so seemingly inexplicable. In an era where governments can read the emails of individuals anywhere in the world, track real-time movements from mobile phone data or view images of people filmed from space by satellite, how can a large, sophisticated and reliable modern passenger aircraft simply disappear?

As with the *Mary Celeste*, myriad suggestions – some similar to those relating to the disappearance of the ship – have been suggested to explain what might have happened. These have ranged from the rational to the bizarre and are too numerous to mention. Some of the finest minds and most advanced technology ever developed have been applied to solve this enigma. So far, none have provided a genuine answer and until one does, the agony of the relatives of those on board will continue.

Handling this crisis has been difficult for the Malaysian government and the country's highly respected flagship airline. In the aftermath, both have suffered a degree of reputational damage. Although some elements of the way in which information has been released could have been dealt with better, how do you explain the unexplainable to a voracious global media following every move of the story 24 hours a day? The benefit of 20:20 hindsight makes an expert out of every pundit and armchair observer and puts those under scrutiny in an unjustly harsh spotlight.

Those heading the search eventually had to admit that they might never find the missing aircraft, meaning they will not be able to discover why it disappeared. Although such an honest admission will only add to the despair of the relatives of the missing, it is a fair, if brutal, concession.

Whatever the outcome, the mystery of flight MH370 should be a lesson to all risk managers and their businesses – that some incidents still cannot easily be explained. Although these are difficult to predict, risk professionals need to ensure their companies have an effective and well-drilled crisis management plan in place that is sufficiently robust to cope with the most extenuating circumstances and pressures. It might not be able to provide all the answers sought, but it could potentially limit catastrophic damage.

Meanwhile, as the search continues, the words of Conan Doyle's greatest literary creation, Sherlock Holmes, come to mind: "When you have eliminated the impossible, whatever remains, however improbable, must be the truth".

As far as risk management goes, he may well have had a point. **SR**

Risk professionals need to ensure their companies have an effective and well-drilled crisis management plan in place

‘As anyone in Asia with half an eye on the horizon will tell you, optimism still reigns in the region’

OPINION
SEAN MOONEY
ASIA EDITOR, STRATEGICRISK

The most recent *World Investment and Political Risk* report from the Multilateral Investment Guarantee Agency (MIGA), makes for largely unsurprising reading. Anything that comes out of the Washington-based political risk insurance and credit enhancement arm of the World Bank Group is odds-on to plug the positive aspects of political risk insurance (PRI) and foreign direct investment (FDI). It doesn't disappoint in this regard, noting that the continuing high level of investor caution is a boon for the political risk insurance industry.

But when I raised this with a respected regional analyst recently, he told me straight there's a problem with MIGA's assumption that FDI is good for development. PRI (with the benefit of World Bank backing) can make it happen that much faster. He said that FDI was good for development, but only if it was the right kind of FDI and the right kind of development. The central question here is about speed – can MIGA serve as a catalyst and make good things (the 'right FDI') happen faster?

Our analyst thinks it can, but only as long as it is supporting a deal that makes commercial sense in a country with plausible prospects for improvement. In short, it can make the tipping point happen faster provided that things are going in the right direction already.

There are some interesting titbits about the Asian region in the MIGA report. First, there's the news that the developing nations of Asia-Pacific receive more FDI than those in any other region – more than $300bn (€216bn) a year. Dig a bit deeper, however, and you discover most of that money – about $250bn – goes to China, which is why a slowdown in its economy is dampening prospects for FDI for 2014. The report goes on to predict that improved economic performances in high-income economies such as Japan are projected to contribute to an estimated rebound to $345bn into East Asia and the Pacific in 2015.

Another section of interest hidden away in the report is an acknowledgement that developing economies with significant domestic imbalances and large current account deficits have been particularly vulnerable to recent currency depreciations and inflationary pressures. As commodity prices have stabilised or eased, commodity-exporting countries such as Indonesia and Malaysia have been negatively affected.

The report goes on to state that additional risks to the growth of developing economies include excessive leveraging in select countries in Indonesia, Malaysia and Thailand that could give rise to domestic banking stress. There's even mention of the spectre of "disorderly unwinding" of the current Chinese investment-lending boom.

But as anyone in Asia with half an eye on the horizon will tell you, optimism still reigns in the region. A survey for the report found that almost half of respondents expected to increase their investments in developing countries in 2014, increasing to 70% when the horizon was extended for three years. Investment opportunities emerging in Laos and Myanmar, for example, bode well for the region.

In fact, Myanmar became MIGA's 180th member late last year, meaning that FDI into the country is eligible for investment guarantees. This is essentially protection of investments against the risks of transfer restriction, expropriation, breach of contract, non-honouring of financial obligations, and war and civil disturbance.

MIGA senior risk management officer Paul Barbour has told me that MIGA currently provides a guarantee to one infrastructure project in Laos and that it is "looking at potential projects in Myanmar".

The World Bank has an important role to play in developing economies such as Myanmar, and MIGA is part of the package. Although it is positive that Myanmar has joined MIGA, we should expect a trickle of guarantees, rather than a flood. In the analyst's words: "MIGA can be a valuable catalyst, but rarely a game changer".

Myanmar is going in the right direction, but it's only just beginning, and specific investments deals need to be judged carefully on their merits. There are still significant political risks. **SR**

A respected analyst told me FDI is good for development, but only if it is the right kind of FDI and the right kind of development

RISKS

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THE EYE OF THE STORM

As debate continues over the reasons for the world's recent weather disasters, risk managers must have a clear position on planning for the unknown

»

BUSINESS PLANNING

THERE'S NO DOUBT ABOUT IT: Earth is getting hotter by the day. The past three decades have been warmer than any others since 1850, while nine of the 10 warmest years on record since 1880 happened between 2000 and 2012, according to the Intergovernmental Panel on Climate Change.

Scientists believe that, in the coming decades, there will be further increases in tropical cyclone maximum wind speed and rain rates, as well as more frequent and severe heatwaves, droughts and precipitation.

While the arguments surrounding climate change rage on, there seems to be relatively little disagreement from the scientific community, business and government that such extreme weather is changing the way in which businesses need to approach decisions on environmental risk. A wait-and-see approach no longer seems an option, according to experts, and companies need to ensure their business continuity plans focus on the most vulnerable parts of their supply chain.

Last year proved to be another catastrophic year. According to Swiss Re's latest stigma study, economic losses topped €101.8bn worldwide and about 26,000 people lost their lives. There were floods in Europe and Canada, severe windstorms in the US, the UK and continental Europe and wildfires and cyclones in Australia.

However, scientists and reinsurers say catastrophic event losses were down on previous years. According to Swiss Re, insured losses from natural catastrophes and man-made disasters in 2013 amounted to €32.7bn – down from €58.9bn in 2012 – while insured losses from natural catastrophes alone were at least €26.9bn.

Change of perceptions

Experts argue that, with the last ice age having taken place only 10,000 years ago, recent extreme weather cannot be labelled either a short-term phenomenon or a permanent shift in weather patterns. Extreme changes in temperature and weather are nothing new; but perceptions are altering.

'You have a certain budget. You have limitations. Just make sure you spend it in the right places'

Cath Geyman, Intersys

Veolia Water risk and business continuity manager Lenny-Baptiste Conil says: "We tend to have short memories. Huge catastrophes happened in the past, but we remember only the last one because it's more vivid. Then you have inflation and other factors that make the financial loss of the past look smaller."

Catlin chief science officer Mike Maran believes fewer catastrophic events happened in the past year, but perceptions of the damage have shifted as a result of the extensive reporting of events.

"There are catastrophes being recorded quite a lot, and there seems to be a lot of them, but what we've heard from scientists is that there were [fewer] than previously," he says. "It depends on where they occur. There don't seem to have been an unusually high number of catastrophes. For example, the hurricane season last year was incredibly low."

Aon Benfield head of Impact Forecasting Adam Podlaha agrees there is a rise in the reporting of catastrophic events, rather than a rise in actual events.

"Now, we record everything – even small earthquakes we cannot hear or feel. The reporting of events is getting better and more frequent," he says, adding: "There are also more places insured."

Lack of certainty

But while climate change is often linked to the increases, perceived or otherwise, in natural catastrophes, Maran says there is no certainty as to the nature of extreme weather events, which makes planning more difficult.

"Most people would agree there's no evidence that the recent weather catastrophes are a sign of climate change as opposed to normal extreme events. That doesn't mean to say they're not. It just means we can't say, 'Yes, of course they are'," he says. "We've always had extreme events. That's what they are: they occur from time to time."

Specialists believe that human activity may be having a greater effect on the overall consequences of catastrophes. FERMA president and DLA Piper chief risk officer Julia Graham says: "Man has a tendency to build in places he shouldn't build, in coastal areas and with an accumulation of potential exposures, which leads to some of the catastrophes we have endured."

Conil says the accumulation of wealth in urban areas has opened up businesses to unprecedented potential risks. "We concentrate more and more people and wealth in cities, so when something happens there, its impact is mechanically greater.

"With all the concrete and asphalt that is being laid in urban areas, any rain-related events are also more severe every year. Where there were water infiltrations, you now have run-off, and that changes dramatically the impact of a simple heavy storm."

Intersys director of risk management Cath Geyman says the locality of the events is also an important factor. "We're seeing more financial pain because the freak events are happening in areas that are much more developed than perhaps they were [previously. It doesn't make the news headlines or hurt the insurers or companies as much if the disasters occur in the middle of the African sub-continent."

Broader remit

Building resilience to withstand natural catastrophes requires much broader and more comprehensive business planning.

Graham believes business continuity and how organisations construct their plans is crucial. Risk managers need to work beyond the immediate horizon of their work and learn to think in different ways. "When you look at natural catastrophe or disease, or other major events such as cyber, we can't avoid networking and working with all of our stakeholders with a view to having proper resilience and response times in place. These are likely to look a bit different than they might have done years ago," says Graham.

Geyman says that in the face of catastrophe, risk managers tend to have business continuity plans that focus on their immediate sites rather than at their extensive supply chain.

"The problem with a large organisation is that in order to maintain really good contingency plans for every single part of their supply chain, in-house and out-of-house, would cost an inordinate amount of money," she says.

As 2014 moves into the second quarter, disasters have already struck in the form of prolonged flooding in the UK and extreme temperatures in Australia and the US. Geyman says it is time for risk managers to prepare for unknown catastrophes ahead, whatever the cost. "Businesses need to find a way of triaging what is going to hurt the most if they fail during a catastrophe, and then focus their continuity plans on the most vulnerable points in their supply chain," she says.

"The amount they spend on preparedness and contingency planning is proportionate to the values at risk from that point in the supply chain," she adds. "You have a certain budget. You have limitations. Just make sure you spend it in the right places in the first place." SR

REX/Ezra Acayan/NurPhoto

MODELLING

CATASTROPHE MODELLING – AT one time a simple, single-event spreadsheet in an insurer's toolbox – is now a multi-tiered, multi-event modelled approach to risk management. New versions of catastrophe models are designed to take into account almost every aspect of potential natural and man-made disasters, alongside a company's own risk portfolio, to provide a much broader picture of what is at stake.

Catastrophe models also have the ability to move and change with an ongoing event, which makes them an indispensable tool for risk managers.

The future for catastrophe modelling looks bright, with the incorporation of new information from scientific models of hazard and engineering perspectives on damage. However, experts are also warning businesses not to rely exclusively on catastrophe modelling as a tool for determining a business's potential catastrophe risk.

Following a number of extreme natural catastrophes in the past year – super typhoon Haiyan, polar vortex winter storms in the US and some of the worst flooding on record in Canada, Australia, India, China, Indonesia, southern Africa and Argentina – experts are concerned about the current scope of models. They believe they do not sufficiently address the unpredictable nature of disasters to provide a single solution for business.

Aon Benfield head of impact forecasting Adam Podlaha says the trend for catastrophe modelling is heading in the right direction by including more scientific analysis, as well as alternative model providers such as academics and proprietary firms.

"These are basically taking into account the things we did not know with the models already available," he says. "An example is [modelling for] earthquakes in New Zealand, which takes into account the same modelling as the Japanese earthquake."

He points to a similar trend with tsunami modelling. "There is a big shift towards a multi-model approach. There are the big companies that are modelling, but there are also lots of new modelling companies coming out as well."

One such firm, Intersys, is looking at ways to combine catastrophe modelling with a company's own risk assessment data to create a more holistic approach to catastrophe modelling.

Intersys director of risk management Cath Geyman says: "We are looking to overlay flood and earthquake zones on the data that our clients work up. Our clients are assessing their own organisations to understand where their critical points are and plot them on a map in order to work out their true exposure.

"What they really then want to do is take the flood and earthquake maps produced by traditional catastrophe modelling firms and combine the two data sets in order to access their risk."

She adds: "At the moment, there is a lot of focus in the modelling world on really understanding each hazard in a lot of detail and being able to model and predict it in a lot of detail. Perhaps what's missing is the company's view on that – each organisation understanding its own complexity, every critical part of it and what the impact would be on it financially should one of these natural catastrophes hit."

Developing economies

Lloyd's head of exposure management and reinsurance Trevor Maynard believes that the future of catastrophe modelling – as well as the likely insurance options – is linked closely to developing economies.

"As economies develop around the world and populations become wealthier, there will be an increasing demand for insurance," he says. "These regions will become more material and therefore there will be an increasing need for more granular modelling in those regions."

But experts in developing nations believe that despite a high rate of natural catastrophes in these regions, the future of catastrophe modelling is still uncertain and there is plenty of groundwork still to cover.

Lockton Wattana Insurance Brokers (Thailand) executive chairman Wattana Wongvisesnopakun says: "The use of catastrophe modelling in Thailand is still very small compared with the international market. It is not as advanced here, so there is not much use for modelling for the industry here just yet."

Recent extreme natural disasters, such as super typhoon Haiyan, which killed more than 7,000, are testing the scope and coping mechanisms of current catastrophe models. Rapidly changing conditions, in combination with the extreme nature of catastrophes, mean risk managers are often faced with using out-of-date information.

"Generally, hazards do not change that rapidly, although our understanding of them can," says Maynard. "The Japanese earthquake in 2011 showed us that mag 9 quakes can occur in

Aftermath of Typhoon Haiyan, Tacloban, the Philippines

that region – when models did not expect that. Inevitably, there will always be new information that surprises us. However, current models have a large spread of events already, which has led to greater financial strength.

"It should be noted, for example, that the Japanese earthquake event in financial terms was much less than some other larger events contained in the model."

Maynard points out that research by Lloyd's and catastrophe modelling firms shows that models incorporate changing conditions implicitly but not explicitly.

"For example, the approximate 20cm of sea level rise at the Battery in New York since the 1950s increased [Cyclone] Sandy's storm surge loss by 30%. Climate change is therefore clearly having an effect on damages," he says.

Lack of flexibility

Podlaha believes it is the unpredictable nature of catastrophes and the innate lack of manoeuvrability of catastrophe models that leave businesses most exposed.

"Most of the current models come as they are," he says. "They are designed to model extreme weather. They are optimised for big events and the models are officially designed to yield information on big events.

"But from time to time, things happen that the modelling company doesn't take into consideration. The result is big, it is bad, and [the company] knew it was always there, but because it did not happen previously, it was not considered properly.

'Generally, hazards do not change that rapidly, although our understanding of them can … There will always be new information that surprises us'

Trevor Maynard, Lloyd's

"In general, the models can cope, but incrementally. You do the basic risk assessment. Following every new event, we learn something new."

A lack of accurate predictability is a driving factor behind the extreme exposure that most businesses face in catastrophic situations. Experts say this unpredictability will continue to underpin catastrophe models for the foreseeable future.

"It is important to realise that catastrophe models are not forecasts. They do not predict what events will occur in the coming year. They show the range of possible events that might occur and their likely costs as insurers deal in probabilities," says Maynard.

"Current models already build in features such as recent higher sea surface temperatures into their projections. The intention, specified by insurance regulation, is to predict current levels of risk and if these are different to the past then adjustments should be (and are) made," Maynard adds.

Oasis framework

The need for more predictable information for risk managers has led to the development of the Oasis Loss Modelling Framework, owned by 21 insurers, reinsurers and brokers, including Lloyd's. The initiative aims to provide a framework for independent catastrophe modelling.

Oasis project director Dickie Whitaker says: "Risk managers from multinational companies will be able to take advantage of catastrophe modelling techniques in a way that has not been practical with large models built for the insurance industry.

"Corporate risk managers seek better information that helps to understand the risks associated with possible catastrophic events. In many cases, this information is not easy to access in a form that is easily usable and some of the avenues available can be very expensive."

The insurance options available to businesses are still costly, say risk managers, but increased uptake of government pools is making this more viable.

"The insurance industry pools risks from around the world to help communities and businesses to offset the randomness of extreme events," says Maynard. "Governments are increasingly seeing the relevance of insurance protection.

"For example, the CCRIF [Caribbean Catastrophe Risk Insurance Facility] is a parametric product that provides fast liquidity to Caribbean governments in the event of earthquakes, excess rainfall or hurricanes."

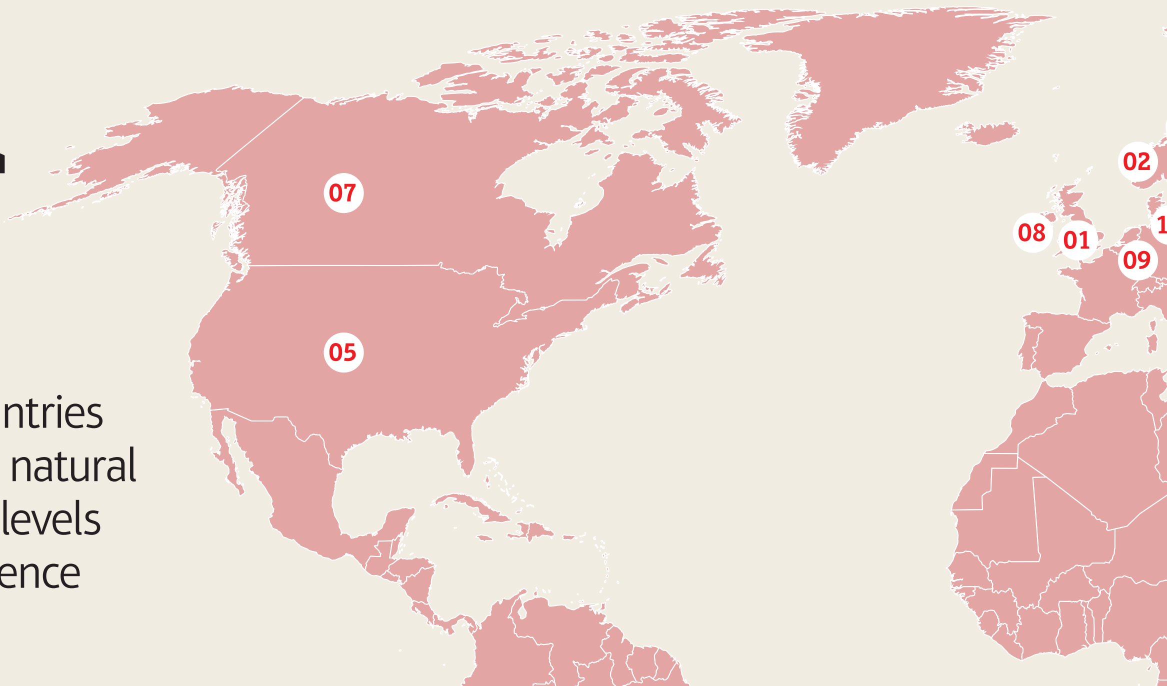
Risk managers need to be more aware of the potential scale of natural hazards facing them and how these might change. FERMA president and DLA Piper chief risk officer Julia Graham believes catastrophe modelling is merely one string to the bow of risk managers and needs to be part of the wider scope of enterprise risk management.

"Risk managers need to work with insurance managers and business continuity managers as a team. That's what enterprise risk management is all about," she says. "It is also about risk managers operating at the most senior level in their organisation. The risk manager needs to be there when businesses are thinking of developing their plans or their businesses in places that perhaps are not totally advisable.

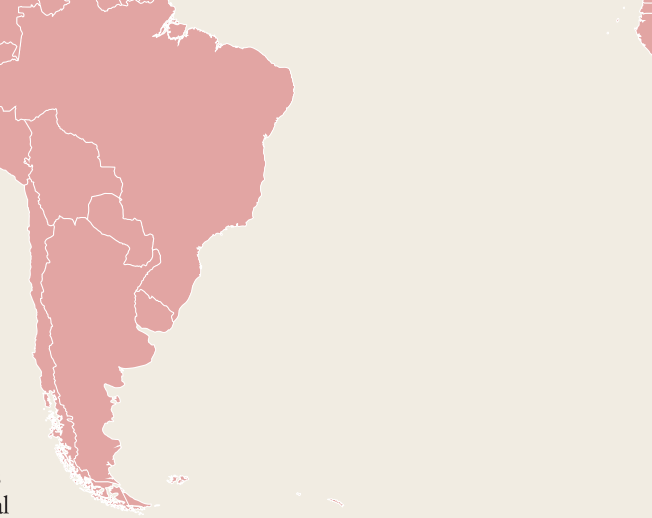
"I think that's getting the risk manager at the right place at the boardroom table to be acting as an adviser in some of these areas, not after the decision has already been made."

Veolia Water risk and business continuity manager Lenny-Baptiste Conil sums up the complex situation in simple terms. "Predicting is impossible," he says, "so planning, training people and keeping up-to-date procedures is the way to go." **SR**

When disaster strikes



Northern European countries are highly vulnerable to natural hazards but have good levels of socio-economic resilience



SEVEN OF THE 10 countries most economically exposed to extra-tropical cyclones are in Europe, according to the fourth annual *Natural Hazards Risk Atlas* by Maplecroft.

The atlas assesses 197 countries on physical and economic exposure to 12 types of natural hazards, including flood, storm surge, earthquakes, tsunamis, cyclones, wildfires and volcanoes.

The atlas shows Germany, the UK and Italy are among the countries for which flooding presents the greatest risk to their economic output.

Northern Europe is most economically exposed to extra-tropical cyclones, which experts suspect is due to a shift in the jet stream that saw the region battered by strong winds between October 2013 and January 2014. Consequently, the UK is ranked most economically exposed to extra-tropical cyclones, followed by Norway, Russia and Sweden.

The atlas also analyses the socio-economic resilience of a country by calculating its capacity to mitigate and manage natural hazard risks.

Sweden is ranked as the most resilient on the socio-economic resilience index. Its high physical and economic exposure to extra-tropical cyclones is therefore diminished by its superior socio-economic resilience. For that reason, the country is a 'low' risk and is ranked 191 on the natural hazard relative economic exposure index.

This trend is consistent in the Nordic region, with Finland (192) ahead of Sweden in terms of relative economic exposure to natural hazards, and Denmark one place behind.

Germany is the most economically exposed European country to flooding and is ranked fifth most exposed globally. The country has suffered together with much of Central Europe in recent years and was the worst affected region by the floods in June 2013.

Similarly to the Nordic countries, Germany's high socio-economic resilience (188) means its relative economic exposure to all types of natural hazard is well placed, at 151.

The UK's high physical exposure to flooding (42), high population density and the proximity of commercial centres, private property and infrastructure to areas susceptible to flooding, means its absolute economic exposure to flooding is seventh highest.

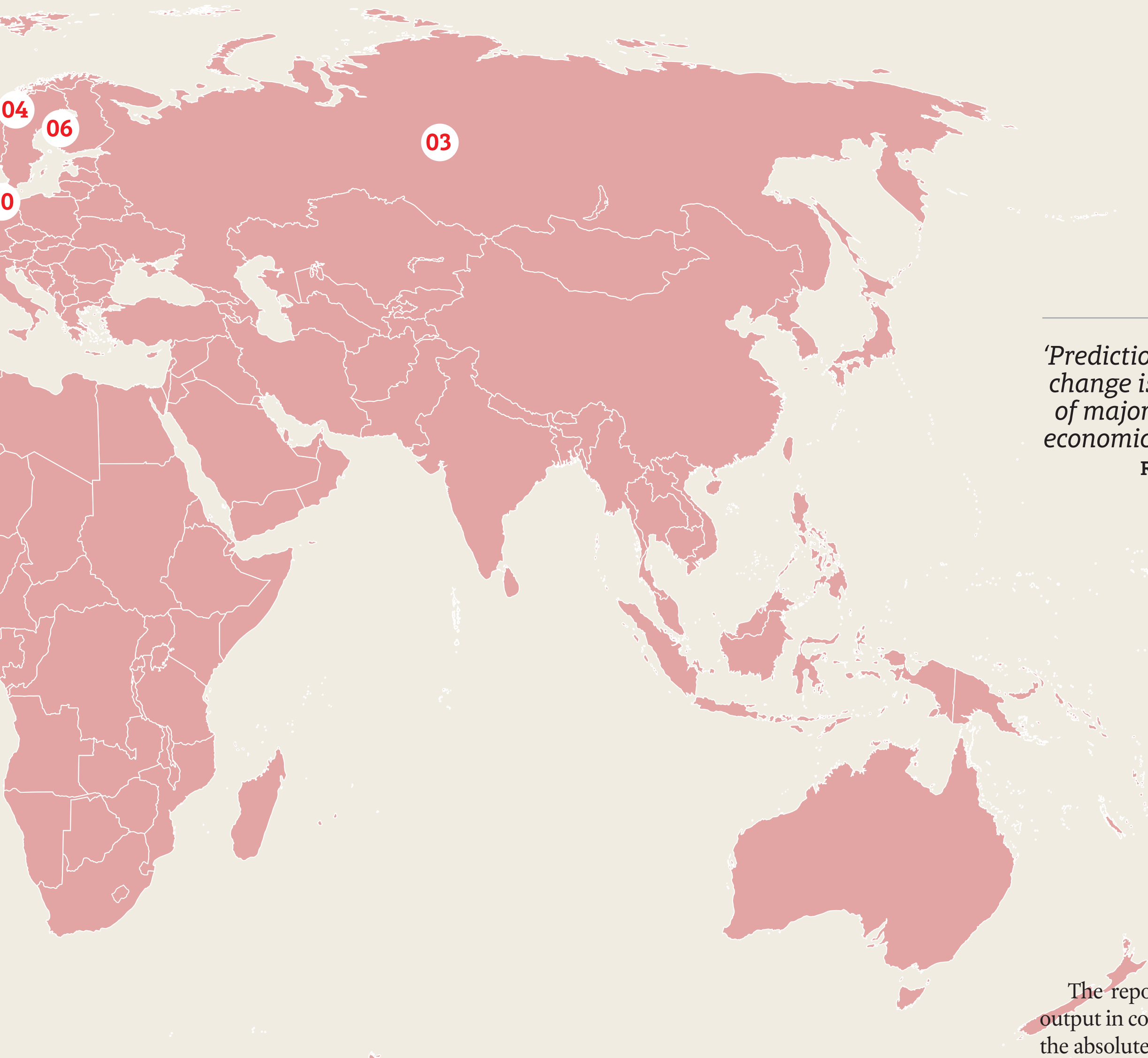
However, the UK's spending power and robust infrastructure and institutions make it resilient to flooding and other natural hazards. The country is ranked 184 on the socio-economic resilience index but languishes considerably lower than Germany (151) in terms of relative economic exposure to natural hazards, at 85.

Although the UK is well placed to rebound from the effects of natural hazards, its physical exposure to extra-tropical cyclones and flooding means resilience in the country will continue to be tested.

"Predictions for the UK suggest climate change is likely to boost the frequency of major storms and increase risks to economic output as a result of flooding," says Maplecroft principal environment analyst Richard Hewston.

"The future scale of the problem will depend on the government continuing to build resilience and apply resources through flood mitigation and risk management schemes."

Moreover, Maplecroft's accompanying report also identifies the need for private sector investment into emerging markets economically vulnerable to natural hazards.



> *'Predictions for the UK suggest climate change is likely to boost the frequency of major storms and increase risks to economic output as a result of flooding'*
> **Richard Hewston,** Maplecroft

EXTRA-TROPICAL CYCLONE ECONOMIC EXPOSURE

1. **UK**
2. **Norway**
3. **Russia**
4. **Sweden**
5. **US**
6. **Finland**
7. **Canada**
8. **Ireland**
9. **Germany**
10. **Netherlands**

Source: Maplecroft

The report says the share of global economic output in countries categorised as 'extreme risk' in the absolute economic exposure index is projected to increase from 44.3% to 49.9% by 2025.

Much of this economic growth will occur in markets susceptible to natural hazards, such as Bangladesh, India, Indonesia and the Philippines. Each of those countries is rated as being 'high risk' in the socio-economic resilience index.

Maplecroft chief executive Professor Alysson Warhurst said: "While significant investment opportunities lie in the growth economies, they are exposed to significant natural hazard risks and have a constricted capacity to bounce back when disaster strikes.

"The private sector has a critical role in building resilience in these countries and companies engaged in disaster risk reduction will see benefits through greater investor confidence, direct cost savings and improved social licence to operate."

Asa Gibson

Taking takaful

There is a growing market for insurance buyers seeking sharia-compliant solutions and options may be closer to home than many may believe

THE RAPID ECONOMIC GROWTH of the Muslim world, increasing acceptance of sharia-compliant insurance and a widening list of specialist reinsurance players have combined to build a takaful market worth $20bn (€14.5bn) in premiums.

The largest markets are Iran and Saudi Arabia, followed by the countries of the Gulf Cooperation Council (GCC) and Malaysia – where Labuan acts as a hub for takaful business from Indonesia and Brunei.

Takaful is essentially mutual insurance – a concept that has a long history in Europe and the US. But to abide with Islamic rules, a takaful insurer cannot earn interest on its investments. The wakalah model is the most popular, whereby operators can charge a management fee to cover expenses plus the cost of capital, in addition to taking a share of investment returns.

Outside Saudi Arabia, which has had its own model of co-operative insurance for many years, takaful insurance is relatively young and has been largely focused on personal lines. The concept was started in Sudan in 1979 and was soon adopted by other countries in the GCC. It is now sold in more than 32 countries, significantly helping to increase penetration in countries where insurance had hitherto not been accepted.

The lack of capacity for retakaful (reinsurance for takaful insurers) has been one of the main factors hindering the growth of the market. Takaful operators have often been forced to place their business with conventional reinsurers, a factor encouraged by the difficulty in applying the mutual concept to commercial risks. This is why so much commercial takaful business goes in through the front door and is reinsured straight back out through the back door.

As Richard Bishop, chief executive of Cobalt Underwriting, explains: "You've got to have a large customer base with a similar risk exposure to create a mutual. So when you bring those markets to bear on a risk that is commercial in nature, the whole concept of mutuality doesn't work.

"All they have done in the past is just transfer the risk through them and out into the corporate reinsurance world, and this makes a bit of a mockery of their claims to be fully sharia-compliant."

A market for commercial takaful is gradually evolving, driven by demand emanating from the GCC. The market in Asia remains largely focused on 'family takaful', such as life, health and pension products. "The Far East takaful market has thus far stayed away from getting involved in the commercial arena, but that is changing and therefore there are opportunities in that part of the world as well," observes Bishop.

Problems over lack of retakaful capacity are starting to be resolved. Many major European reinsurers have set up retakaful operations in the Middle East and North Africa (MENA) region over the past five years, together with local players.

"On the treaty side, there is definitely enough retakaful capacity available either from the regional players like us, ACR Retakaful and Saudi Re and, of course, the retakaful arms of major reinsurer such as Munich, Swiss, Hannover and Scor," says Firas El Azem, general manager of Dubai-based Takaful Re.

"There is surely still a need for facultative reinsurance capacity as far as major or very specialised risks are concerned," he adds. "However, I don't see this as an obstacle for takaful operators and it shouldn't hinder them from growing.

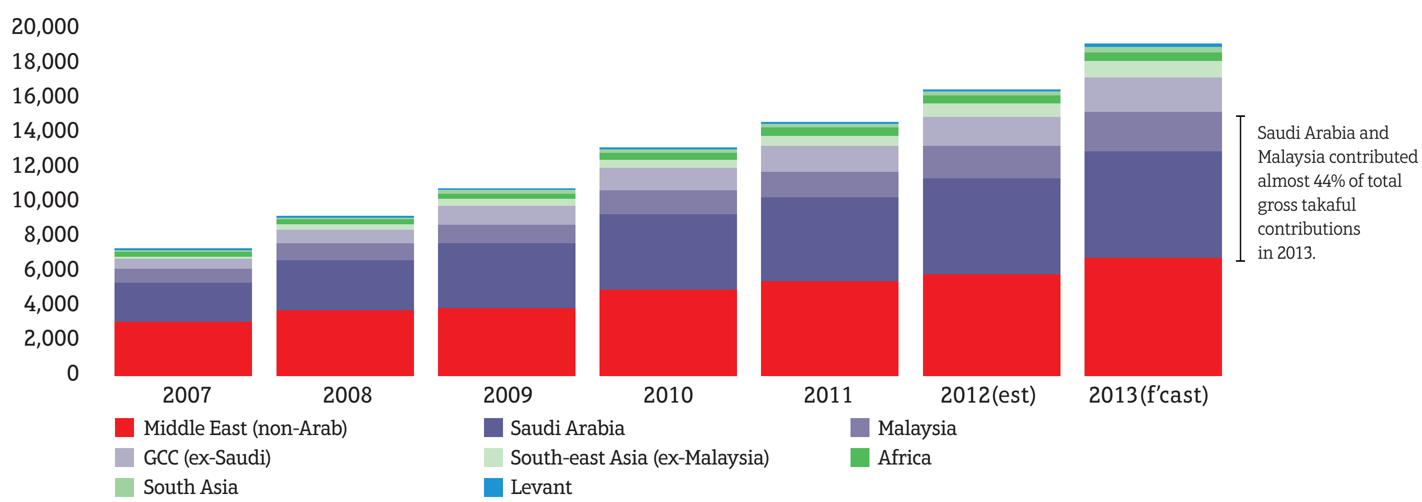
"A lot of big projects planned in the GCC Area need construction all risks and property insurance, and this can be written by the takaful companies too. The more important subject for me is if they – and the conventional insurers – maintain proper underwriting discipline and charge risk-adequate rates. This will be the main trigger for the involvement of retakaful companies as well as reinsurers.

"If everything is done in a professional way, the takaful operator should have a competitive edge. Working to mutual principles, takaful operators have to return part, or in some cases the whole, surplus generated in the mutual insurance funds. This should be a big incentive to insure with a takaful company."

London: a centre for Islamic finance?

Cobalt Underwriting was set up in 2012 with the objective of establishing London as a leading global centre for sharia-compliant insurance capacity. It is financially backed by Capita, assisted by Aon Benfield and has XL Insurance and QBE Europe as

Global gross takaful contributions by region ($m)



Source: World Islamic Insurance Directory, EY, KFH Research

capacity providers. Its underwriting focus is on direct and facultative property and construction, and its first risk, written with XL, covered a deal to acquire a high-profile London property portfolio.

Bishop anticipates significant opportunity for London to attract retakaful business. "Cobalt was formed to act as an underwriting agency on the part of capacity providers who want to get involved in using a standardised blueprinted approach, which we have developed and had signed off by the scholars," he says.

"One has to assume the demand that currently exists for conventional reinsurance that flows through the takaful market should, in theory, be a good starting place.

"Take on top of that the fact that throughout the Muslim world, particularly the Middle East, insurance penetration is very low. Therefore there has to be a greater opportunity to enter the marketplace on the back of the sharia-compliant nature of our products."

There is a keen appetite in London to develop Islamic finance and takaful insurance and reinsurance. "We're only a small organisation based here in London," says Bishop. "We have the capability to be scalable. What we first need to do is to create a flow of enquiry that feeds our market and generates its own momentum.

"We have spent a lot of time educating the brokers who are dealing with that part of the world that may be able to show us the business we'd like to see," he adds. "We try to explain to them what our USP is. Traditionally [MENA clients] are cash-rich, so they are very pro-investment in asset classes, which is exactly what we want to see.

"We don't want to see lots of long-tail risk, so short-tail investment – property or construction projects – is an area where we want to see more activity and where we believe there's more than enough to go around."

Bishop continues: "A lot of it doesn't find its way back to London. It's a highly competitive marketplace. What we bring is high-quality capacity, and not every buyer is motivated to buy on this criteria. But it is something that they are becoming increasingly aware of – particularly if their financiers say you have to have decent quality insurance behind what you do. You can't afford to be so expensive that nobody comes to you in the first place, but at the same time you have to be mindful that certain risks in the Middle East are rated at or below cost, and therefore you can't just write everything that comes in.

"It's about building trust and understanding between two marketplaces and if London is able to provide retakaful capacity that other parts of the world aren't, in theory that should mean the business flows into London."

Lloyd's plans in Dubai

Lloyd's recently announced its decision to open an office in the Dubai International Financial Centre. Retakaful could be one of the areas it looks to develop, assuming it can compete in what is already a highly competitive and soft market.

The decision to establish a MENA base is part of the insurance market's Vision 2025 strategy, which has a focus on emerging markets. "Lloyd's presence here should be an added value to the market," says Takaful Re's El Azem. "It will be additional capacity, but it will be professional capacity, so we trust it will assist."

Insureds looking to take out sharia-compliant insurance do not necessarily need themselves to be based in the Muslim world. Multinationals that find themselves with a growing asset base in Islamic countries are opting for takaful over conventional cover, notes Bishop.

"Sharia-compliant insurance is available to anybody – so long as the asset or risk being insured is sharia-compliant," he says. "We've seen an awful lot of interest from multinationals that are operating in Muslim countries and that want to be seen to be doing what they can to comply with local realities.

"These are countries that will be much more comfortable with people and organisations who are sympathetic to the Muslim beliefs," adds Bishop, "and I believe a number of companies think this might give them a competitive advantage." **SR**

SECTOR VIEW

FOOD AND DRINK

Food for thought

It falls to risk managers to ensure that our key to survival – sources of food and drink – are kept safe and secure

IT IS THE STUFF OF LIFE ITSELF, SO THE FOOD AND DRINK sector finds itself with an almost unique risk profile. On the one hand, everyone needs to eat and drink and that doesn't look like changing any time soon, giving businesses a guaranteed market. But in no way does that make the sector 'easy street'. Competition is brutal, legislation labyrinthine and customers' and regulators' expectations sky high in terms of standards and quality.

Overall, business is booming. Food and drink remains the largest manufacturing sector in the EU in terms of turnover – €1,017bn, according to research by FoodDrinkEurope.

Despite the economic downturn, the sector body's analysis shows that food and drink manufacturers have sustained positive growth in the EU, easily outperforming almost every other manufacturing sector. The sector is also an important employer. The number of people working in food and drink across the EU reached 4.25 million in 2011.

However, for individual firms at least, there are no certainties. You only have to look back to spring 2013 and the horsemeat scandal to see how quickly public confidence can be rocked when firms lose track of their supply chains.

Events began to spiral out of control in January 2013, when horse DNA was found in frozen beefburgers on sale in British and Irish supermarkets. Public outrage prompted retailers and manufacturers to undertake more and more tests, which revealed more and more levels of contamination.

The resulting scandal spread, resulting in empty shelves across the EU as products were withdrawn across 15 countries – and all this although horsemeat poses no risk to human health.

More significantly, the contamination scare revealed a critical breakdown of traceability in the food supply chain, and raised the possibility that other more dangerous elements could have been present – for example, the veterinary drug phenyl-butazone found in meat from illegally slaughtered horses.

However, the scandal also illustrates how tough the sector is and that clients, insurers and their brokers need to be both forward-looking and rigorously analytical in their approach to risk transfer.

"The food industry risk landscape is changing, but most clients still like to start their renewal strategy meeting with a review of the property damage and business interruption/machinery breakdown risks," says JLT major risks practice partner Simon Lusher. "That's probably not going to change soon, although more sophisticated risk management techniques and modernisation of production facilities should align the food industry risk profile more closely with the risk appetite of the wider insurance industry, providing more choice, capacity and coverage."

He believes that many of the major risks discussed are often obvious. Given the massive distances travelled by products via sea, air, road and rail, cargo insurance remains a key risk for exporters (and importers) – whether standalone or a combined stock throughput – and global trade will continue to be supported by credit insurance.

"Traditional property and liability exposures associated with the manufacturing, storage and transportation of goods remain the main insurable risks in this sector as far as I'm concerned," says John Keating, head of insurance and risk management at supermarket group Sainsbury's.

Product recall

But Lusher argues that while product liability remains crucial, product recall – in the form of contaminated products insurance – has emerged as a serious consideration for risk managers.

"The growing importance of contaminated products insurance has been a key trend over the past few years," he says. "Ironically, a lot of positive publicity for this product was generated by the horsemeat scandal, despite the fact that the product recall trigger would not have been activated under the specific circumstances of this event.

"The regulatory environment has also been a driver in promoting interest in contaminated products insurance and we are seeing recall stipulations in supply contracts.

Keating agrees. "Product recall insurance, which provides first-party cover in the event of risks associated with contamination, tampering, mislabelling and so on, has been subject to some comment in the past 12 months, following events in the UK," he says. "This form of insurance has also received a lot of attention internationally in recent years."

'Traditional property and liability exposures associated with the manufacturing, storage and transportation of goods remain the main insurable risks'

John Keating, Sainsbury's

In the US, the Food Safety Modernization Act 2010, which was signed into law by president Barack Obama on 4 January 2011, is intended to ensure that the US food supply is kept safe by shifting the focus of federal regulators from responding to contamination to preventing it.

"The Food Safety Modernization Act has given the Food and Drug Administration a number of new powers, including mandatory recall authority," says Keating. "The Act really led to a convergence of the situation in the US and EU. The US, if anything, was just catching up with the situation already in place in the EU. Having said that, it's important to understand that the way product recalls take place in both continents can be quite different.

"In the EU, the emphasis and expectation tends to be recall on a voluntary basis. The US might be more prescriptive, with more emphasis on mandatory recall."

The voluntary recall more common in the EU works because "if firms don't recall a product, they face real reputational damage", says Keating.

"You only have to look back at some of the big incidences, such as Perrier water – textbook examples of how to get the message out to alert the public, reassure them that all appropriate measures are being taken to resolve a problem and immediately start rebuilding the brand."

Insurers have responded to the changing situation by adapting their offerings. "To give insurers due credit, [contaminated products insurance] is a better product than it was," says Lusher. "The policy wording is now a lot more sophisticated – government recall and adverse publicity endorsements offer value and address key concerns at board level.

"The crisis management support and advice provided under the policy are also hugely beneficial. There must be enough independent evidence across the industry to support this assertion as I'm not seeing the concerns and suspicions about this service that I have in the past."

Food fraud

Another related, if still emerging, aspect of risk is food fraud. Lawmakers across the US and EU are seeing more and more examples of complex international supply chains that provide cover for criminals passing off lower quality products as more expensive items.

In December 2013 and January 2014, a joint operation by Interpol and Europol across 33 countries seized 1,200 tons of counterfeit food and 430,000 litres of counterfeit drink.

The issue involves the potential for reputational damage – for example, if olive oil were found to be adulterated with cheaper oil. But it points to more serious risks too. Illegal vodka and other spirits may contain dangerous levels of methanol and other chemicals, leading to nausea, blindness and even death.

"It will be interesting to see how the food and insurance industries respond to recalls instigated by bona fide companies as a result of defective – and dangerous – branded products that turn out to be counterfeit," says Lusher.

Another area in which recent events have meant a steep learning curve for clients and insurers is supply chain management. From the Icelandic ash cloud to the Japanese

Expert insight: An appetite for teamwork

The food and drink business is an incredibly complex sector. While it shares many industries' long supply chains and global footprint, it presents a unique set of risks because of its vital role in providing for our most basic needs.

Brokers and insurers are responding well to the sector's needs, but there is probably room for improvement. There isn't too much joined up food specialism across the various risks among brokers or insurers. Underwriters will usually specialise in a particular class of business and this makes a lot of sense.

What I'd like to see is more of these class underwriters working together to present a coherent, cross-class approach and philosophy to food business.

Brokers can no longer rely on being merely intermediaries to facilitate the placement of insurance programmes and claims administrators. They should aim to offer industry-focused specialist advice or have a network of third-party consultants who can provide cost-effective expertise.

Food companies know how to run their businesses but brokers should be there to advise, review or challenge on risk management, loss control, supply chain analysis, regulation, emerging risks and business continuity – to name those that spring readily to mind.

Brokers also need a global perspective and access to local overseas expertise for companies with international markets.

The social media revolution has provided companies with additional opportunities to promote their brands, but the flipside of this is that bad news travels faster and further.

Brand protection insurance is generating interest but I'm not sure the insurance industry has yet been able to produce the right product for food producers.

There isn't even a clear consensus on what brand protection is in the insurance market, which must be confusing for potential buyers. Reputation rehabilitation, trademark infringement and loss of profit following lack of consumer confidence as a result of adverse publicity suffered by a competitor's brand have all been sold as separate brand protection insurance policies.

Brokers should therefore be pushing the market to consider new triggers for recall cover, product rehabilitation and adverse publicity, and look to consolidate other brand protection risks into broader wordings.

Some risks will always fall outside of insurers' risk appetite, either because the risk is too volatile or the longer-term implications for insurer balance sheets are too difficult to quantify.

For example, commodity price is always going to be a major concern for any producer, especially when selling prices are being squeezed by the retailer. This is an operating risk that isn't going to be transferred to an insurer any time soon. Coupled with economic downturns and reduced consumer spending power, the main risk facing any company – the failure to make a profit – will remain a risk they face alone.

But in many areas, brokers are proving more essential than ever and we have to ensure we are there to meet that need.

Simon Lusher, partner, JLT

tsunami, from extreme weather events to political disruption in major agricultural areas, food and drink manufacturers have, like many sectors, become more and more aware of their vulnerabilities and exposure to instability.

"Supply chains have grown into supply networks and marine cargo insurance is not necessarily adequate to protect against the risks involved in global transits," says Lusher.

"We're seeing more interest in trade disruption insurance and other non-damage/intangible business interruption solutions, and I think that trend will continue."

Supply chain risks are a major concern, according to Cristina Martínez, director, Corporate Risk Management, at Spain-based Campofrío Food Group Holding. "We need to bring to our supply chain our culture of quality," she says. "As a global corporation, it is mandatory to secure the protection of our reputation and brands globally regardless of the local requirements."

Work still needs to be done to ensure insurers can keep up with the changing needs of the sector in terms of supply chain risk, but the onus remains on businesses to manage the risk. "While the insurance market has the capacity to insure these risks and some have already done so, concerns arise over how the industry would cope with the accumulation of higher values or the duplication of cover in case of overlapping insurance policies held by the manufacturer and its suppliers," she says.

Limiting or reducing cover just provides a financial comfort for insurers but does not offer a solution to the food and beverage industry. "If we want better price for risk because it is well managed, we need to show evidence and get used to exchanging information on a greater scale. I believe the preparation of mitigation actions to minimise the effect of a supply chain disruption depends on the level of endorsement and sponsorship of your top management in risk prevention policies and risk improvement plans more than in purchasing a specific insurance coverage.

"Any additional protection from the insurance market is welcome, but setting internally basic levels of prevention and standards remains essential before exploring a risk transfer solution."

'With terrorism and a general sense of exposure of products and supply chains to tampering, it could be argued that chemical or biological attack on product supply chains is an emerging threat'
Cristina Martínez, Campofrío Food Group Holding

Exposure to terrorism

Food and drink manufacturers can also become targets for those with a political point to make. Contamination by animal rights groups has been a risk for several decades and militant Islam is a developing threat.

Martínez says: "Although terrorism is not an emerging risk, with complex supply chains and the current social economic global environment, an act of food terrorism – deliberate contamination somewhere in the food chain – has become more likely, especially as heightened security has made acts of physical violence harder. With terrorism and a general sense of exposure of products and supply chains to tampering, it could be argued that chemical or biological attack on product supply chains is an emerging threat."

However, acts of chemical or biological attack are excluded from most terrorism covers and expanding cover to include chemical and biological acts is relatively expensive.

Emerging risks

New risks are going to emerge – and from some interesting directions. "Environmental liability has emerged in the past few years on the back of increased regulation and massive public concern," says Lusher. "The insurance industry has responded well to the new regulatory exposures and is becoming less niche than it was.

"Genetic modification is already with us, but will become mainstream in an environment of global population expansion and climate change. Alternative protein sources – following on from the world's first laboratory-grown burger developed by scientists at Maastricht University in 2013 – plus new artificial ingredients and increasing technological innovation in production techniques will all alter the risk landscape for food producers.

"The insurance industry should be able to cope well with these changes, as the risk profile will be similar to the life sciences/pharmaceutical risks that are already written by the major insurers."

Other environmental issues may prove harder to address and mitigate. "Long-term sustainability – balancing the threat of climate change with the demand for cash crops and biofuels – is putting a lot of demand on available land," continues Lusher. "At the same time, consumers are more environmentally aware than ever before.

"This is a balancing act for food companies, which have to deliver affordable food and secure their supply lines while maintaining public acceptability through responsible suppliers and environmentally sound production processes throughout the supply chain."

Elsewhere, food and drink manufacturers face more and

more intangible risks as they increasingly rely on websites, online sales and promotion, networked stock and production systems.

"Cyber liability, cyber extortion, loss of data, intellectual property and so on are all now insurable, and should be insured, as the potential damage to a company's balance sheet through data breach and cyber attack could be enormous," says Lusher.

Health watch

There is one emerging area of risk that is unique to the food and drink sector. In the 21st century, our relationship with these products has become increasingly complex. Although we are generally better fed than before, some health concerns are emerging linked to high-fat and high-sugar products, as well as brands of high-strength alcohol.

The European Commission estimates that 50% of Europeans are now overweight – and 20% obese – and these figures are projected to grow, together with associated health problems.

"I'm not the only one to speculate whether there will be an increase in product liability claims resulting from [conditions] such as obesity, alcoholism and diabetes," says Lusher.

Companies are increasingly seen as liable for any ill effects from the products they manufacture and for educating consumers on responsible use.

"Healthy eating has a high profile, but the debate as to whether the consumer or the manufacturer is responsible for the consumption of too much sugar, salt or fat is ongoing," says Lusher.

"Whether labelling and recommended daily amounts are sufficient to pass that responsibility to the consumer is yet to be settled. How the public liability policies will respond in future will be interesting to see." SR

Expert insight: A world of no surprises

In the modern era of retailing, we all strive to offer the widest range of fresh, high-quality products at the most competitive prices. Our businesses have become increasingly complex as we look to source the best possible fruit, vegetables and meat from around the world at affordable prices.

But over time, as supply chains have become longer and more intricate, it has become harder to know what is happening further down the chain. Without complete transparency, you can lose a certain amount of control, and with that comes risk – probably the biggest risk facing the food and drink industry right now.

As a retailer, customers expect the best – and you are held responsible for everything that has occurred up until the product reaches the supermarket trolley.

While you may have a good idea what is going on with your first and second tier suppliers, what about the third and fourth? How much do you know about their sourcing and transportation? Do you really know where the pinch points are?

In recent years, several major events have shown the impact incidents in far-flung places can have on any business operation: the Icelandic ash cloud, the Japanese tsunami and the horsemeat scandal. Together, they illustrate how critical it is to be prepared for surprises. It also highlights that risk managers must appreciate the global reach of their supply chains.

These events have brought about a major re-analysis of everything we do as risk managers, and it needs to be an ongoing process. We all need to understand what we depend on to maintain our operations, and what we need to protect to ensure we can keep providing those products our customers have come to trust and rely on.

The recent extreme weather was another example of how customers rely on us. When the worst happens, our customers and communities need us to keep going and keep them supplied. In some cases, we are almost an emergency service. Just ask the residents of Muchelney in Somerset, where our local store kept them in supplies for four long weeks when they were cut off by flood water.

The good news is that many of us are getting better at meeting – and exceeding – customers' expectations, whether in terms of product safety or business continuity. Just as we've been working to simplify our supply chains, we've also got better at mapping risks, understanding our pinch points and knowing when to transfer those risks. Our technology is better, our management is better and our people are better too.

In an increasingly unstable world, where the only certainty is uncertainty, we can never assume we have everything covered. All we can ask of risk managers is to be relentless in analysis, to always be on their guard and to expect the unexpected so that when it happens it doesn't come as a surprise.

Helen Pope, head of insurable risk at Tesco and deputy chairman of Airmic

SPECIAL REPORT:

ENVIRONMENT

Varying shades of green

International businesses can no longer afford to ignore environmental issues and need to make sure they keep track of constantly shifting rules and regulations

REGULATORS AROUND THE world are getting tougher on environmental violations. Their powers might be geared towards reducing damage to the planet, but their effect on business could be considerable.

The toll of multinational companies falling foul of increasingly stringent environmental rules is mounting as they struggle to cope with the demands of different jurisdictions. Keeping up with this rapidly changing landscape is an onerous task that catches out unwary businesses.

For every major environmental incident that makes headlines, there are hundreds of smaller ones. The fact they fail to raise a stir in the media makes them no less damaging for the companies involved. As Karl Russek, senior vice-president, environmental, for ACE Overseas General, points out, although many incidents do not make the international news, they still attract the wrath of relevant authorities and have major ramifications.

"These are not just technical issues of environmental management", says Russek. "In an era of 24-hour news and powerful social media, an incident affects companies in terms of their reputation and their brand. That's true [even] if they've not done a lot wrong."

The main challenge for multinationals is the speed at which regulations change. For instance, Chinese authorities startled many foreign businesses in 2014, when they moved environmental issues to the top of the agenda and violations became their priority. Since 1 March, a credit rating scheme measures the efforts of many industries to protect the environment against stiff and specific standards. Under the scheme, a company's environmental scorecard will also go straight to the bottom line – lenders will use the ratings to determine whether a client should get a new loan and, in particular, a government subsidy.

No industry is immune. Coal, transportation, steel, cement, metallurgy, chemicals, building materials, paper, brewing, pharmaceutical, fermentation, textile, leather and mining: all are subject to the new regulations. Inevitably, they will affect many multinational factories in economic zones such as the Yangtze River and Pearl River deltas, both heavily polluted areas earmarked for a rapid restoration.

Further, the Ministry of Environmental Protection, which runs the project, can include almost any business that emits toxic or hazardous materials. Previous offenders attract special and relentless attention. The government's moves, which rate companies on a four-point system between green (trustworthy) and red (offender), are a response to mounting public ire against polluters. With pressure increasing, otherwise exempt businesses are joining the scheme to show themselves as good corporate citizens. As lawyer Ostiane Goh-Livorness of Jones Day explains, "those who do not fall within the scope of the scheme may participate of their own volition".

Mishmash of regulations

Evidenced by the World Bank with its green bonds and other initiatives, the momentum is gathering pace. For instance, the sale of green bonds – whose proceeds are ploughed into anti-pollution projects – increased fivefold last year to $11.26m (€8.26m). As the bonds help pay for major infrastructure projects, companies tendering for these jobs are required to show they prioritise sustainable development. Some of the biggest multinationals are jumping aboard this environmentally friendly wagon – Ford Motor Company and Microsoft bought green bonds for the first time in late 2013.

Penalties are also rising right across the world even for small breaches. The world's oceans and waterways are under particular scrutiny. For instance, Australia, which is influential in maritime law in Asia-Pacific, has increased tenfold – to AU$10m (€6.7m) – the maximum fines for the discharge of oily water under much stiffer, new marine pollution laws. Other countries are following suit under international maritime laws that ban the dumping of all garbage at sea and have been quick to move against offenders.

> *'An incident affects companies in terms of their reputation and their brand'*
> **Karl Russek,** ACE Overseas General

In another development, offences now give rise to criminal prosecutions, once a rare outcome. For example, after a Dutch-owned vessel leaked 200l of oil into Australia's Newcastle Harbour in 2011, the company was fined AU$150,000 despite no evidence of environmental harm, the offender paying for the clean-up. This was the first such incident involving the company – or the captain – in the world. As Australian firm Corrs Chambers Westgarth points out, the court took the view that "the spill was not insignificant, it was reasonably foreseeable, and it was preventable".

In short, Australia's courts are cracking down and targeting individuals. Although only China has introduced the death penalty for those guilty of serious pollution, other countries are taking a tougher line on offenders who acted negligently or recklessly. As many incidents show, owing to public pressure regulators are particularly tough on spills in ecologically sensitive areas.

Trouble can also be found close to home. In early 2014, Dutch food-processing giant Vion Foods' beef-processing plant in Schleswig-Holstein, Germany, was shut down for alleged breaches of hygiene and other regulations – although six independent audits vouched for the factory's compliance. In March, Vion threatened legal action, demanding compensation, but the plant remained closed.

Alarmingly, France is about to put a principle known as "ecological prejudice" onto the statutes. According to insurers, the implications for most industries will be profound in terms of liability to different kinds of sanctions.

As the fall-out from environmental breaches shows, the legal ramifications often endure for years, incurring severe reputational and financial consequences in the process. In March, the Spanish courts fined Ferrovial and six subcontractors €21m seven years after major construction works at Barcelona's container port for the Hutchinson group collapsed into the harbour. (The port authorities had asked for €101m in compensation.)

In this often conflicting mishmash of regulatory risks, it is unsurprising that firms increasingly seek protection across activity and geography. "Clients are looking at covering environmental risks that may be excluded elsewhere, especially within commercial general liability, construction or D&O policies," says Julien Medina, environmental adviser for Marsh France. "They are also adjusting their coverage to follow [the path] of their business activities."

As the price of breaches rises, for example for reputation and repair costs, insurers are boosting capacity to match. ACE group now offers a capacity of $50m for global clients seeking cover for environmental liability, substantially up from the previous $30m.

In this climate, protection considered adequate a year or two ago may be deficient today. SR

Worth the paper it is written on

Many companies may not have an adequate level of cover in respect of environmental risks and should review their exposure to those risks and buy insurance more reflective their needs

AN INSURANCE POLICY IS more than a mere document, much more. Although firms increasingly have to arrange a comprehensive cover against the multiple consequences of an incident – for instance, third-party liability, physical injury, property damage, financial loss, clean-up costs, emergency expenses and business interruption – the onus is on businesses to avoid these repercussions by taking robust, audited preventive measures. As the fast-growing international case law shows, it is vital that an offending company can claim in its defence that, despite slipping up, it had adopted and executed a formal strategy to protect the environment.

As Nicolas Givelet, ACE's environmental risk engineer for continental Europe, explains, the policy should be regarded as merely the opening salvo in a company's green programme. An entire regime of risk reduction, he advises, should be built around the policy against the multiple damage that environmental accidents generally cause.

More regions are waking up to this broader concept of risk reduction.

According to ACE's recent Emerging Risks Barometer, a survey of 650 companies in Europe, the Middle East and Africa, 42% of local businesses rate environmental threats as having the potential to affect their bottom line while three quarters said their shareholders are taking them more seriously than before. Yet ACE's own research also reveals that many firms are woefully underprepared, in countries such as Turkey.

Right level of cover

As Givelet pointed out in a speech at a reinsurance conference in Istanbul in February, many Turkish businesses have significant gaps in their environmental cover, a disturbing finding in a country with 8,000km of coastline vulnerable to breaches. "Our client research suggests a significant level of confusion among companies on the extent of the environmental cover they currently have, if any", Givelet explains. As a first step to redress their exposure, he advises firms to conduct a thorough risk analysis of their exposure to potential environmental risks and then carefully consider whether their existing cover is adequate.

If it's not, the answer is to precisely match the cover with the perceived requirements. It's critical that businesses buy cover that reflects their needs, explains Julien Medina, environmental adviser at Marsh France. "ACE offers well-fitting coverage to clients with a good understanding of their activities," he adds.

Once the cover is in place, the next step is the all-important prevention plan. As China's sudden about-face on the dangers of pollutant industries shows, a risk-prevention regime that was considered fit for purpose a year or two ago may be quickly outmoded. Thus, consultants suggest that businesses work backwards from the regulatory environment applying in each country rather than assume that an all-regions cover will do the job. That's because it almost certainly won't. "A multinational needs a different response according to the demands of each jurisdiction. There's no such thing as a one-size-fits-all action plan," explains one source.

Regular rehearsals of the action plan form an essential element of the preparation – and they become a crucial factor in a court room if a breach occurs. As an extra step, even the most risk-averse businesses should invite outside scrutiny of the plan by auditors and other skilled parties, for instance, practitioners in public affairs.

Some of the initiatives companies should take include: training personnel to operate well within the boundaries of the particular country's regulations; establishing a dialogue with the relevant environmental authorities rather than dealing with them as a necessary evil; developing a much-tested action plan against the occurrence of an event, however unlikely it may seem, that goes far beyond a mere clean-up. It must cover all the company's obligations towards the authorities, the affected community, non-governmental groups that may be involved, local media, public at large and any other stakeholders.

'A multinational needs a different response according to each jurisdiction'

Plans should also be exposed to outside scrutiny by expert third parties.

"This must be a genuine and robust plan for containing the crisis and not something that starts with a panicky 3am phone call to the chief executive," summarises Karl Russek, senior vice-president, environmental, for ACE Overseas General. "It's surprising how few companies think about what to do until after the incident has occurred." **SR**

France takes a controversial ecological step

When solid cakes of fuel oil polluted France's Atlantic coastline recently, it triggered a movement that may result in an upheaval of environmental law in the country with implications for industry. With the support of green activists and government members, a principle known as "ecological prejudice" is to be enshrined in the Civil Code this year, whereby an offending enterprise will face full repair costs for environmental damage in the widest possible sense as well as maximum penalties equivalent to 10% of its pre-tax, global revenues.

The business would also be exposed to multiple, long-running legal actions taken by the state, environmental authorities, local governments and associations, environmental business groups and others with an interest in the "protection of nature and the environment". In effect, anybody with a stake in the particular pollution could sue because of the law's broad definition. "The [ecological] prejudice that we envisage is that which is done to nature, ecosystems, quality of soil etc," according to Professor Yves Jegouzo, who drafted the 10 essential principles.

The business world argue that "ecological prejudice" would add another burden to the already comprehensive legal environmental obligations. All the main private-sector lobby groups for business, insurers and big industry are uniformly hostile, arguing the government would do better to improve existing statutes, such as the law relating to environmental responsibility ("la loi sur la responsabilité environnementale"). The body representing the risk-management industry warns that the size of the proposed penalties "are likely to have a considerable impact on the survival of the business concerned". In short, a contravention of the proposed principles of ecological prejudice could prove ruinous.

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When the worst does happen

Everyone in a company should know what their specific roles are in the event of a crisis

ONE OF THE MOST REVEALING exercises a company's crisis management team can do is to study the environmental incidents suffered by other firms around the world. Often they provide case studies of what not to do. Below is only one example of a flawed response.

When a fire broke out late last year on a landfill for non-hazardous waste in regional France, the firefighters promptly turned up. So far, so good. However, they sprayed water on the 40m² area, a response that is doomed to failure in a deep landfill. After three hours, the fire was raging more strongly than ever and had spread to the bottom of the site. Only at that point was the site operator allowed to dump soil on the fire – the specified technique to extinguish landfill blazes.

In the wake of one incident, painful lessons were learnt. Because of the incorrect initial procedure, it took five days to put out the fire instead of a few hours. The water had penetrated so deeply into the landfill that it required a major exercise to collect and treat the contaminated liquid.

As a result, the total cost of the claim was €200,000, instead of a mere few thousand had the proper methods been employed.

Being prepared

The lesson, say insurers, is to have in hand a thoroughly tried-and-tested response mechanism in which all the parties know their role, including, in this instance, outside agencies such as the fire service.

Karl Russek, senior vice-president, environmental, for ACE Overseas General, has been involved in the fall-out many such incidents. He points out that far too often the response happens on the fly. "Surprisingly few companies think about what actions they should take until after the incident has occurred", he points out. "As a result many events are terribly managed."

According to consultants, the golden rules are straightforward: know what could happen, be ready when it does, and immediately launch communications with all stakeholders. In short, it won't be all right on the night. **SR**

'Surprisingly few companies think about what actions they should take until after the incident has occurred'

Karl Russek, ACE Overseas General

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Growth expectations may have been reined in, but foreign investment will continue to flow into Indonesia despite the risks, agreed participants at *SR Asia*'s final event of 2013

RISK PROFESSIONALS BASED in Jakarta highlighted lasting and looming challenges at the final *StrategicRISK* Indonesia Risk and Insurance Management roundtable for 2013. Indonesia's top risk managers met the *SR* team, local brokers and Zurich's regional representatives to examine the state's risks and opportunities.

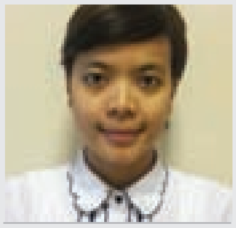
There was wide agreement about the primary risks faced by organisations operating in Indonesia. Education and training, skills shortages and retention of talent were all up for debate, as were regulatory change and challenging economic conditions.

Political risk was another area of concern, with uncertainty over this year's presidential election combined with the global slowdown affecting risk outlooks in Indonesia. It was clear that, despite the huge opportunities on offer, participants felt major investment was likely to remain on hold until after the election.

Economic growth in Indonesia appears to be cooling, reflecting a dip in foreign investment, commodity prices and domestic

Nurture all our resources

Risk consultant at Astra International Duma Irene Mitalevanie says some of Indonesia's biggest future challenges centre on the exploitation of natural and human resources



'With the rapid growth of industry in Indonesia, more workers are needed to run production processes'

Duma Irene Mitalevanie, Astra International

"Indonesia has abundant natural resources. It is an advantage for industry in Indonesia, especially in the mining and plantations sectors. Because of abundance of natural resources, their use is often not accompanied by responsibility to maintain sustainability; in other words, there is exploitation of natural resources. There is a tendency for businesses to exploit natural resources, then leave the used and damaged plants and go looking for new plants to get more results. Many such violations go unpunished because there is no strong legal foundation.

"Indonesia has one of the five largest populations in the world and the number of people of productive age is more than that of non-productive age. With the rapid growth of industry in Indonesia, more workers are needed to run production processes.

"Competition intensifies and global economic conditions tend to be unstable, so it can affect operational cost reduction. Ways of reducing operational costs include the suppression of wages of employees or employing children under the legal age of employment.

"Despite the recent increase of the minimum wage of employees in the manufacturing sector, other sectors have gone unnoticed. This is especially evident in the plantation sector outside Java. Often employees in more remote areas are not officially registered by companies. There is no objection from the employees because economic condition difficulties and their lack of skills mean that they have no bargaining power and will do anything to earn money.

"Indonesia's economic growth is not evenly distributed in all areas, therefore there are things that go unnoticed."

consumption. Its current account deficit continues to widen, with imports increasing faster than exports.

But, as Aon Risk Services technical adviser and head of specialty in Indonesia Cameron Sheild explained, policy shifts such as the reduction in fuel subsidies will help stimulate growth. "The country's growth prospects are undisputed, particularly if long-term development plans and public policies boost investment in the expansion of labour skills and infrastructure," he said. "However, in the current economic environment, corporations' projections a year ago might well fall short of the expectations of today. One might say the honeymoon is over. [But] make no mistake: Indonesia is still an extremely attractive place to invest, in comparison with other countries."

XL Axiata enterprise risk management specialist Johan Candra said inflation was "increasing quite significantly and impacting on purchasing power". "The Indonesian rupiah is depreciating against the US dollar," he said. "Large corporates in Indonesia need to have a sustainable strategy to pass through these harsh economic conditions."

Astra International risk consultant Duma Irene Mitalevanie said the state faced challenges in continuing to develop strongly and sustainably. "Indonesia has a lot of debt, especially to the International Monetary Fund," she said. "The government doesn't clearly define the goals of the country and there is a lack of guidance for creation of healthy and integrated business."

Mitalevanie said economic growth was uneven because of a concentration of economic development on the island of Java, particularly in Jakarta. "Indonesia used to be an agricultural country, focusing on development of the agricultural sector and successfully meet domestic needs," she said. "Now it has to import food raw materials to meet domestic needs."

Howden Indonesia president director Willy Ignatius said major overseas investment had to grow. "The main risks facing foreign

investors remain the same: political uncertainty, legal uncertainty and the ability to repay loans," he said.

Willis Indonesia president director Simon McCrum said that in the run-up to the elections there had been considerable electioneering around nationalism and protectionism, and he expected this to increase. "The mining industry has been particularly affected by changes in regulation, but most sectors are feeling the impact to varying degrees," he added.

'Large corporates in Indonesia need to have a sustainable strategy to pass through these harsh economic conditions'

Johan Candra, XL Axiata

Foreign investment measures

Growing nationalism had all but stopped foreign investment in mining, Sheild said. "In September, the minister of energy and mineral resources issued regulation number 27 of 2013 regarding procedures for share divestment price determination and change of investment particulars [MoEMRR 27/2013].

"MoEMRR 27/2013 makes a number of important changes to the regulatory regime for foreign investment in the local mining industry and has taken most foreign investors in the local mining industry and their advisers by surprise."

Uncertainty over proposals to curb foreign ownership of banks have also been questioned, he added. "On the other hand, the government has pledged to revise a list of industry sectors open to foreign companies as a part of an effort to boost foreign investment amid declining growth figures," he said.

McCrum believes commodity prices and forex pressures "will find Indonesian companies struggling to compete, which in turn brings a different set of concerns and risks to the table".

Ignatius said the weakening of the rupiah had already created additional costs for any company that used US dollars to buy raw materials. "This will, in turn, create higher inflation and push up the cost for any company to continue operating," he said.

The price of commodities was, quite simply, "our benchmark to determine whether our projects are a go or a no-go", said Bumi Resources Minerals enterprise-wide risk management head Rachmadi Gustrian. And Putri Perdana Sari, risk management manager at catering firm Aerofood Indonesia, said commodity price fluctuations "affect food costs and, in the end, our ability to generate or increase profit".

Foreign investors would continue to invest in Indonesia, Mitalevanie said, because it had "a bright future". "It is also supported by the Asean Free Trade Area (AFTA), which will be applied in 2015, so it will be easier for foreign investors and workers doing business in Indonesia," she said. However, Ignatius cautioned that AFTA might cause "disruption between foreign Asian workers and Indonesian workers if Indonesian workers are not able to compete".

He also pointed to the threat posed by last year's street demonstrations demanding higher minimum wages. "This will cause the company on the outset to lose production," he said. "In the longer run, it will create higher overheads. This is frightening for any company – along with the government and associations not being able to balance, it might be forced to go out of business, which would not be good for unemployment figures."

Another people-related risk is the availability of skills and talent, as rising labour costs and low skill levels cause difficulties for companies eager to grow in Indonesia.

McCrum said all industry sectors needed to work together to address the issue. "Education will be the key for the future. I can see a time when industry establishes and supports 'academies' to provide properly trained manpower to their sectors," he said.

JLT Indonesia president director Arman Juffry said there was a need for a more proactive approach in introducing risk management to Indonesian business people. "Perhaps an early introduction to risk management and ERM can be done via associations, chambers and universities," he suggested.

Risk management is often seen as more of a cost centre than a profit centre by boards in Indonesia. Ignatius felt there was a need to educate managers and executives in terms of looking at risks as a whole and not only towards transferring those risks. "People should be developed to review risks strategically and consider management risks from within – that is, the ability for a company to retain some of those risks, and potentially to transfer those risks effectively," he said.

Lockton head of sales (Singapore) Peter Jackson pointed to Indonesia's "fast-growing, young, educated and articulate class of junior and middle managers". "They are eager to learn and can be developed to apply modern thinking in the Indonesian business environment," he said.

Sophisticated risks

Looking ahead, issues such as dealing with sophisticated risks related to nanotechnology and biotechnology were on risk professionals' radars. Natural catastrophe came up time and again, with one participant labelling the country a "supermarket of disaster" because of its exposure to every type of natural hazard.

McCrum saw natural catastrophes as inevitable. "Flooding is and remains a major risk in Jakarta, the financial impact of which local insurers are only starting to take notice of," he said.

Environmental issues would not be the only factors to hit Indonesia's inhabitants and economy, added Mitalevanie. "The big changes will also occur in cultural, media, technological, socio-cultural, political and even biological factors. Business competition is increasing, along with a public mindset that is more self-critical than ever. Companies are required to adjust to the impact of globalisation for the sake of their survival." **SR**

A NEW WEAPON

Deferred prosecution agreements have just been introduced in the UK. How do they work and how will other jurisdictions view them?

A DEFERRED PROSECUTION agreement (DPA) is a new enforcement tool in the UK, available as from 24 February 2014, introduced by the Crime and Courts Act 2013, enabling prosecutors, in certain circumstances and subject to certain conditions, to deal with corporate economic crime without pursuing a full prosecution. This follows the publication of the finalised Code of Practice on 14 February 2014 by the Director of Public Prosecutions (namely the head of the Crown Prosecution Service (CPS) in England and Wales) and the Director of the Serious Fraud Office (SFO).

Rationale and comparison with the US

The past few years have seen an increasing political imperative in the UK to hold corporates to account for criminal conduct, with DPAs being promoted as part of the UK government's commitment to combat economic crime more effectively.

The UK may have realised somewhat late the potential value of DPAs: they have been common practice in the US for many years, with the first corporate DPAs dating back to the early 1990s. Their use has increased markedly: since 2000, the US Department of Justice has entered into 273 publicly disclosed DPAs and non-prosecution agreements (NPAs), which have led to monetary penalties totalling more than $40bn (€29bn)*. The recent news that JPMorgan Chase has agreed to pay $1.7bn underlines the value and significant potential benefits of a DPA.

Sceptics may ponder whether the driving force behind the UK embracing DPAs at a time of financial austerity where a major concern in the Ministry of Justice has been the cost of lengthy and complex fraud trials was financial. Money received by a prosecutor under a DPA is to be paid into the Consolidated Fund (the government's general bank account at the Bank of England). The terms of a DPA may include payment of "any reasonable costs of the prosecutor in relation to the alleged offence or the DPA".

However, the structure of the process, which places the judiciary at the centre of the consideration of the appropriateness of a DPA, is designed to dispel, or at least reduce, such concerns. This distinguishes the UK regime from that in the US: the UK authorities have emphasised the requirement for effective judicial scrutiny – and not a rubber-stamping – of DPAs. Negotiations between a prosecutor and a corporate must be transparent and "ensure that the proposed DPA placed before the court fully and fairly reflects [the corporate's] alleged offending". The court ultimately decides whether a DPA is in the interests of justice and its terms fair, reasonable and proportionate. It makes a declaration to that effect, at which stage a DPA comes into force. The court determines whether a corporate has failed to comply with the DPA's terms; and if so, whether to invite the prosecutor and corporate to agree proposals to remedy the failure or whether to terminate the DPA.

The US have no such detailed rules for judicial oversight of DPAs; rather, the role of the courts has often been restricted to approval of the length of deferral periods and dismissal of charges following successful completion of those periods. However, US courts are starting to take a more active role in considering whether particular DPAs are in the public interest. For example, in approving the DPA entered into with HSBC in December 2012, the court asserted its supervisory authority stating that "a pending federal criminal case is not window dressing. ... By placing a criminal matter on the docket of a federal court, the parties have subjected their DPA to the legitimate exercise of that court's authority".

Another major distinction between the US and the UK is that, unlike in the US, there is a high threshold in the UK to meet the test for corporate criminal liability, requiring a prosecutor to prove that misconduct was authorised at the highest levels of an organisation. The director of the SFO has described this as "the problem inherent in the DPA regime". Thus, it is expected that UK DPAs are likely to be used most frequently in the case of a suspected s7 Bribery Act 2010 offence, which introduced a strict liability offence for commercial organisations for a failure to prevent bribery. The director has called for an extension of the s7 principle, advocating a corporate offence of a company failing to prevent crimes of dishonesty or fraud by its servants or agents, subject to a statutory adequate procedures defence.

How will prosecutors decide

The code gives guidance on the general principles to be applied in determining whether a DPA is likely to be appropriate in a given case. The starting point is the application of a modified version of the traditional two-stage prosecutor's test for bringing prosecutions, which requires a prosecutor to consider first whether the evidential test is met and then whether a prosecution is in the public interest. The evidential stage usually involves the prosecutor being satisfied that there is enough evidence to provide a "realistic prospect of conviction" before considering whether a prosecution is in the public interest. However, the code allows the prosecutor to consider the public interest earlier, enabling a prosecutor to avoid what is often a lengthy and costly investigation, provided there is a reasonable suspicion that the commercial organisation has committed the offence and there are "reasonable grounds" for believing that a continued investigation would provide further evidence capable of establishing a realistic prospect of conviction.

The code is clear that "the SFO and the CPS are first and foremost prosecutors"; that a DPA is a discretionary tool; and the prosecutor is not obliged to invite a commercial organisation to negotiate a DPA, nor is a commercial organisation obliged to accept any invitation made.

The past few years have seen an increasing political imperative in the UK to hold corporates to account for criminal conduct

Further, the director has stated his commitment to prosecute the "topmost tier of serious and complex fraud, bribery and corruption". While the director of the SFO describes DPAs as "a welcome addition to the prosecutor's tool kit for use in appropriate circumstances", he is clear that "there will be cases where a company should be marked with a conviction".

The director emphasised this on the publication of the final code, stating: "The most important features of the DPA regime outlined in the code are judicial oversight, and unequivocal co-operation from the corporate. Prosecution remains the preferred option for corporate criminality". The code reflects both the co-operation expected and the fact that prosecution remains the preferred option. Yet, it is also clear that one public interest factor alone may outweigh other factors tending in the opposite direction, arguably leaving a prosecutor with considerable discretion in deciding how to pursue a particular case.

The code sets out factors for and against prosecution. The (non-exhaustive) list of public interest factors tending against prosecution includes co-operation by the company (the code states that this will include identifying relevant witnesses, disclosing their accounts and the documents shown to them; making witnesses available for interview, where practicable; and disclosing any internal investigation report) as well as the fact that a company's board has changed. In terms of the co-operation expected, and any self-report by the company, the director has recently stated that he expects this to include waiver of legal professional privilege, which "is often claimed, dubiously, over accounts given by witnesses in internal investigations." This is likely to be an area of considerable debate over the coming months. A further factor against prosecution is that a conviction is likely to have disproportionate consequences for a corporate, under domestic law, the law of another jurisdiction, including but not limited to that of the EU. This is directed to the potential for debarment from public procurement contracts under regulations implementing EU directives that render ineligible any bidders convicted of offences, including fraud or bribery. Companies convicted of the s7 offence of failing to prevent bribery are subject to discretionary exclusion rather than the mandatory ban. A DPA would give a contracting authority a discretion to debar a company, which prosecutors may seek to use as a negotiating tool.

The director expects the numbers of self-reports to increase following the introduction of DPAs, and has recently reinforced the SFO's approach in this regard by stating that a self-report opens up the possibility of a DPA or civil recovery, rather than a prosecution.

Content and incentives to enter into a DPA

A DPA must contain a statement of facts, which may (but need not) include admissions by the corporate (although the director has recently stated that he considers that an admission of guilt will be an indicator of cooperation by the company). A statement of fact must "give particulars relating to each alleged offence" and "include details where possible of any financial gain or loss, with reference to key documents that must be attached".

The likely terms of a DPA will comprise a fine, but may include other matters, for example, compensation of victims. Any financial penalty agreed must be "broadly comparable to a fine that the court would have imposed... following a guilty plea". The discretion available when considering a financial penalty is broad, and reference will be had to various factors, including any relevant Sentencing Council (SC) guidelines. Recent SC guidance for the sentencing of corporate offenders suggests that levels of fine will be high and should "substantial enough to have a real economic impact which will bring home to both management and shareholders the need to operate within the law".

Proponents of DPAs in the US regard them as appropriate for resolving even the most challenging criminal allegations in targeted, efficient ways, which they consider exact meaningful punishment, often through hefty financial penalties and rigorous compliance reforms, while avoiding serious collateral consequences of criminal convictions. On the publication of the final code, the director referred to the use of DPAs avoiding "collateral damage to employees and shareholders who may be blameless".

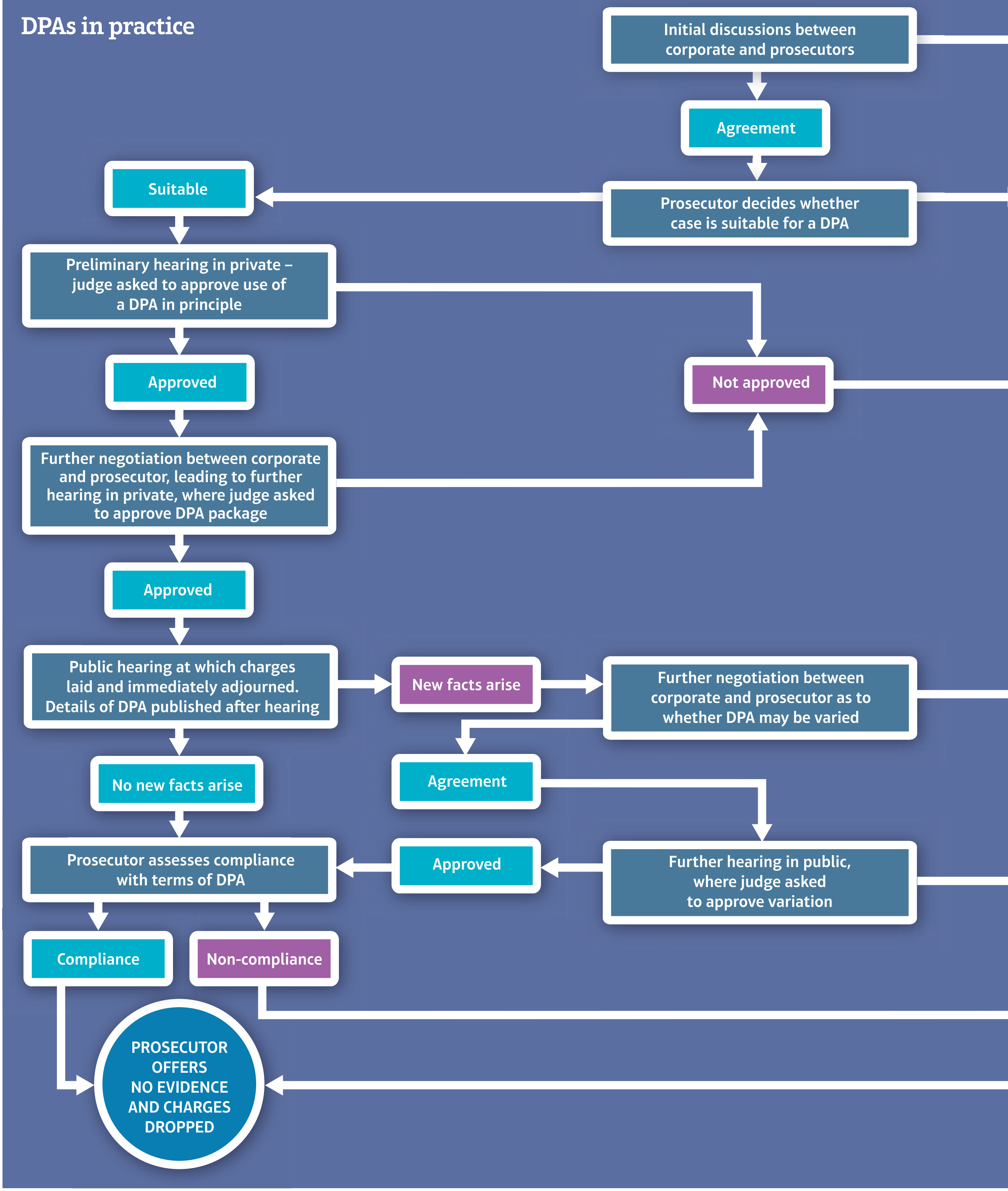
Despite the challenges for the prosecution in meeting the test for corporate criminal liability (other than for s7), corporates being investigated by a more enthusiastic SFO, whose avowed intention is to bring more corporate prosecutions, may take a pragmatic decision to agree to a DPA, particularly if this enables them to negotiate a resolution with other regulators and prosecutors across the globe (since large corporate investigations are likely to involve cross-jurisdictional issues). Nevertheless, the co-operation expected as against the uncertainty of a DPA being approved means that DPAs remain, at this stage, a leap in the dark.

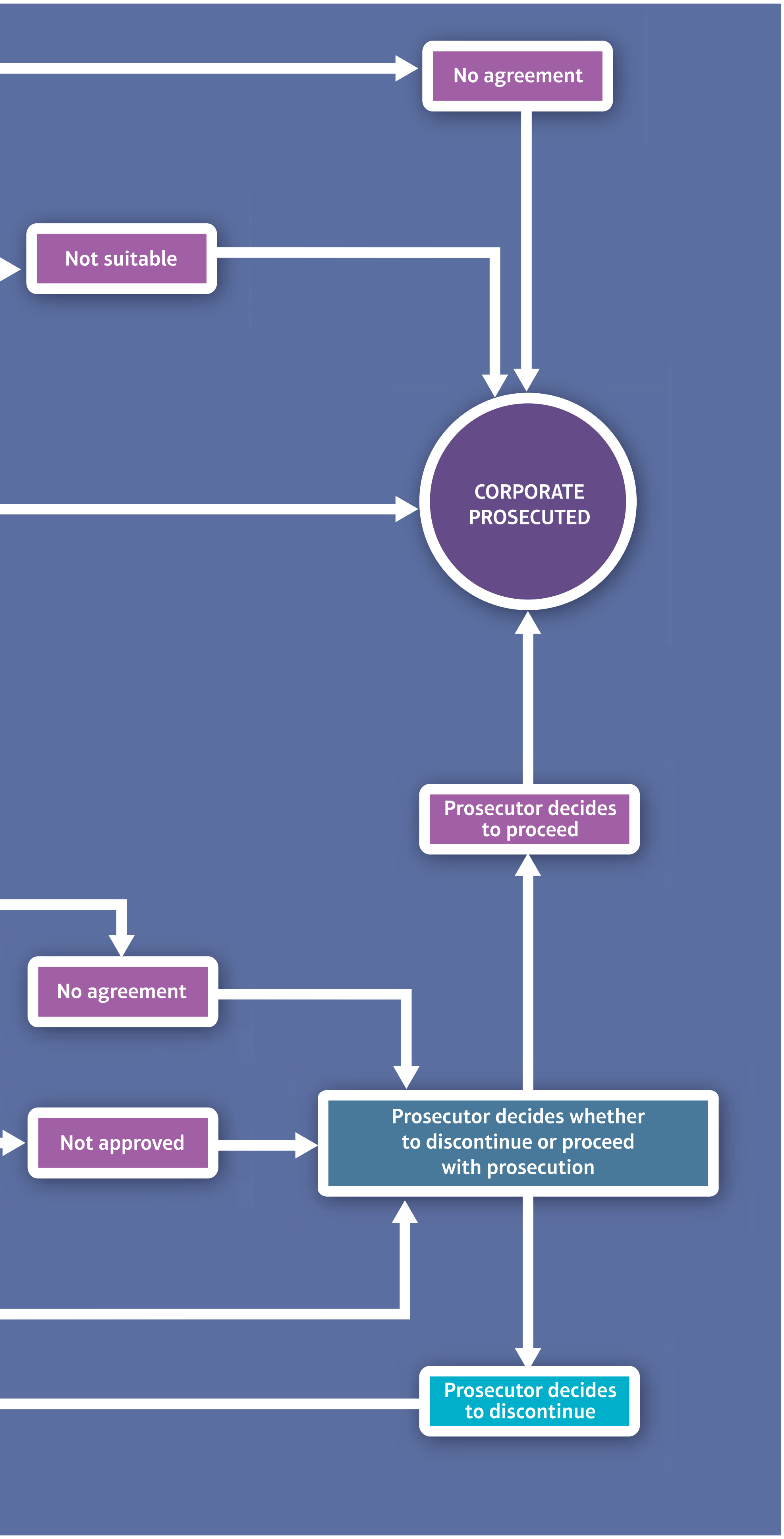
Approach towards prosecuting individuals

A corporate's decision whether to enter into a DPA is likely to include consideration of the position of individuals who may face prosecution, which itself could have reputational knock-on consequences for the corporate, depending in particular on the seniority of the individuals involved. There is no comfort to be taken from either the public pronouncements of the SFO or the code on this point. In setting out the factors tending against prosecution, and in the context of a corporate self-reporting, the code (going further than the draft code did) states that "Co-operation will include identifying relevant witnesses, disclosing their accounts and the documents shown to them". The code states that: "It must be remembered that when [the corporate] self-reports it will have been incriminated by the actions of individuals. It will ordinarily be appropriate that those individuals be investigated and where appropriate prosecuted". This echoes the Guidance on Corporate Prosecutions, to which a prosecutor must have regard, which makes it clear that the prosecution of a company should not be seen as a substitute for the prosecution of criminally culpable individuals, which, it states, provides a strong deterrent against future corporates offending.

The code also states that the prosecutor "must not agree additional matters with [the corporate] which are not recorded in the DPA and not made known to the court" – however, this

DPAs in practice





does not preclude a prosecutor from taking the view that, following a DPA with a corporate, it is not in the public interest to prosecute the individuals, particularly where other, for instance regulatory, action may be taken.

The US experience may also provide some insight into what happens in reality: DPAs are generally entered into without corresponding prosecutions of individuals, a practice recently questioned by US District Judge Jed Rakoff, who referred to DPAs as satisfying prosecutors who "believe that [they] have helped prevent future crimes; the company is happy because it has avoided a devastating indictment; and perhaps the happiest of all are the executives, or former executives, who actually committed the underlying misconduct, for they are left untouched".

Given the stance of the SFO, which has set itself against the culture of "cosy off-record chats", and given the criticism by Lord Justice Thomas in *R v Innospec Ltd* about entering into civil agreements that glossed over corporate criminality, it is likely that the SFO will want to show that DPAs do not represent a way for corporates to buy their way out of trouble or a way of letting culpable individuals off the hook. Whether, in practice, it will succeed in that aim is another question.

Effect of DPAs in other European countries

A key concern of corporates entering into DPAs with prosecutors in the UK is the extent to which any information passed to the prosecutor, or created during the negotiations, may be used in subsequent or parallel criminal or regulatory proceedings. This is dealt with in para 13 of Schedule 17 to the Act, which limits the use of certain information obtained or created during DPA negotiations. This limitation includes material showing that the subject of the DPA entered into negotiations for a DPA, including any draft of the DPA, any draft of a statement of facts intended to be included in the DPA and any statement indicating that the subject of the DPA entered into such negotiations. It also includes "material that was created solely for the purpose of preparing the DPA or statement of facts". However, that material apart, the code expressly states that there is no limitation on the use to which other information obtained by a prosecutor during the DPA negotiation period may subsequently be put during criminal proceedings brought against the subject of the DPA. In light of this, there is a real prospect for information derived from DPA negotiations to flow between UK and other overseas authorities; and there may be circumstances in which European prosecutors may wish to use such information to bring action against the subject of a DPA.

There is also a growing movement in Europe towards criminal liability for corporates, with many European jurisdictions focusing on whether the corporate had proper systems and controls to prevent an offence from occurring. Given the likely focus of DPAs, initially at least, on the s7 offence (and assuming the adequate procedures defence is not met), this may pave the way for other jurisdictions to bring action. It will also mean that corporates need to consider their exposure outside the UK in entering into DPAs.

Judith Seddon is director of business crime & regulatory enforcement at Clifford Chance LLP

* Gibson, Dunn & Crutcher LLP: 2013 Year-End Update on Corporate NPAs and DPAs, published on 7 January 2014

THE AUSTRALIAN EXPERIENCE

As well as the reputational issues created by a corruption investigation, the costs of responding can be significant, writes Herbert Smith Freehills senior associate Guy Narburgh

MANY HEADLINES IN the Australian financial media in 2013 concerned stories about bribery and corruption issues affecting high-profile individuals as well as prominent Australian companies.

The Independent Commission Against Corruption completed six inquiries last year and another four are still ongoing. Australia's ranking in Transparency International's Corruption Perceptions Index dropped two places, from seventh in 2012 to ninth in 2013.

Commentators have called for stricter legislative controls in Australia, mirroring the models adopted in the US and the UK.

Apart from the significant reputational issues created by an anti-bribery or corruption investigation or inquiry, the costs of responding can be significant. While the reputational cost cannot be insured against, these response costs frequently can be. However, given the nature of such investigations, several issues commonly arise that should be considered when purchasing cover and when making a claim on insurance.

Coverage for corporate costs

Insurance for the costs of responding to a bribery and corruption investigation is potentially available to companies (as opposed to individuals such as directors), but it is a relatively undeveloped market.

Insurance products have been developed specifically to respond to investigations conducted pursuant to two of the most prominent international pieces of anti-bribery and corruption legislation: the US Foreign and Corrupt Practices Act and the UK Bribery Act 2010.

These products typically respond prior to any other potentially available insurance coverage, such as coverage for individuals under directors' and officers' (D&O) policies and can provide cover for individuals or the corporate entity in relation to legal fees and expenses incurred in responding to anti-bribery investigations. Importantly, they can also provide cover for costs associated with 'internal' investigations, which can also be significant.

Typically, these products do not respond to investigations related to bribery or failure to prevent bribery that does not involve a public official or liability for any claim (in the form of a judgment or settlement) arising from an anti-bribery or corruption investigation, including the costs of implementing compliance/remedial measures, fines or penalties.

One of the factors affecting the take-up of this type of insurance is its price. Anecdotally, a policy limit of AU$5m can cost as much as AU$1.5m in premium. While it is possible to structure premium payments to reduce up-front costs, this is likely to create a perception that the cover, based on current pricing, does not offer significant value for money. Furthermore, because of the low take-up of these policies to date, information on how they perform in the event of a claim is limited.

Coverage for individual costs

Far more common is insurance for the costs associated with an individual's involvement in an anti-bribery and corruption inquiry or examination. Usually, this cover will be found in a D&O liability insurance policy.

Three main types of coverage under D&O policies are potentially available: investigations cover, extradition cover, and bribery and corruption extensions.

Most D&O policies in the Australian market provide coverage for investigations by 'official bodies'. When purchasing cover for investigations, some of the important things to consider are what triggers the coverage under the policy, whether the definitions of 'investigation' and 'official body' are sufficiently broad to capture the bodies that would typically undertake an anti-bribery or corruption investigation, whether the policy covers investigations, acts or omissions occurring anywhere in the world, and if the cover is subject to a specific monetary sublimit.

Policies commonly provide some cover for the costs of an individual seeking to challenge a judicial order for extradition in respect of proceedings or an investigation. Some policies also contain specific extensions of cover in relation to claims made against individuals for violations of the US Foreign Corrupt Practices Act or any similar legislation in any other jurisdiction.

Exclusions and conditions

If an investigation or claim is potentially covered under one of the insuring clauses or extensions, care needs to be exercised as to whether any exclusion or condition applies that may limit or exclude cover.

D&O policies contain exclusions in relation to certain types of conduct by a director. These 'conduct' exclusions generally have the effect that the D&O insurer must advance investigation or defence costs to a director until such time as a written admission or final judgment establishes that the director acted dishonestly, fraudulently or criminally or gained personal profit or advantage to which they were not legally entitled.

A D&O policy is likely to contain a contractual restriction on cover for fines and penalties. Cover for fines and penalties under D&O policies remains a vexed question, with a lack of clear and consistent guidance on which types of fines and penalties would be treated as insurable, particularly 'strict liability' fines and penalties.

Following a series of Australian cases in recent years, it is common for D&O policies to contain a clear obligation on the insurer to advance 'reasonable' investigation or defence costs to a director while any investigation or claim is ongoing (and provided there is cover for the investigation or claim). Some of these clauses contain specific timeframes for payment of costs; some do not. Even where no timeframe is specified, an insurer's duty of utmost good faith would require it to act reasonably and respond promptly, absent any issue as to cover.

In addition to these issues, given the nature of the allegations underlying a corruption investigation, the D&O insurer may seek information, pursuant to a contractual right under the policy, that will enable the insurer to consider whether there may have been misrepresentations or non-disclosures prior to the commencement of the policy. **SR**

'Most D&O policies in the Australian market provide coverage for investigations by 'official bodies''

Guy Narburgh, Herbert Smith Freehills

THEORY & PRACTICE

More specialists please

Cass Business School makes the case that boardrooms should be filled with experts and not merely people who are just good managers

Do we take risks when we hire leaders with minimal core-business knowledge?

I once appeared on *Start the Week* on BBC Radio 4 to discuss my book *Socrates in the Boardroom*. The book makes an empirical case for putting top scholars into senior leadership positions in research universities, instead of those who have only proved themselves as good managers. I was amazed at the response I received from individuals in banking, the media, engineers, surgeons, social workers, and even a former Formula 1 racing driver. Their stories were very similar. The bankers wrote that the financial crisis had much to do with the role of non-experts in major CEO positions. The surgeons complained that managers were instituting systems that suited other managers but not the doctors or patients. Social workers blamed the sad stories that emerged around the country on systems that were overly bureaucratic. As I write this now, there is a legal battle ensuing in Australia following the tragic death of an adolescent in a psychiatric unit. The coroner in the case has recommended that all mental health teams should have clinical oversight from a consultant psychiatrist, not merely a manager.

If patient safety requires expert leaders, then why not all leadership?

Consulting firms McKinsey and PwC are often responsible for introducing new trends in management practices, so what do they do? The McKinsey website tells us that Dominic Barton, who is the global managing director, has been with the firm since 1986. Barton is no new boy and undoubtedly he has excelled in his consulting profession to stay there that long. Might we also expect Ian Powell, chairman and senior partner at PwC, to be a decent chartered accountant? What about high-tech firms – should they be led by technical experts or managers who are generalists? It is interesting to look at who sits on the Google board. You will find that each person holds at least one computer science or engineering undergraduate degree, Masters or PhD; and there are two university presidents – Stanford's John Hennessy and the former Princeton president Shirley Tilghman, both of whom are eminent scholars. Might former HBOS CEO Andy Hornby have fared less badly if he had spent more years in actual banking rather than in Asda supermarkets?

My research shows that genuine expertise matters. Leaders should be experts in the core business of their organisations. Being a capable general manager alone is not sufficient. This topic is hotly debated. There is recent evidence that major firms have moved away from hiring CEOs with technical expertise, towards hiring leaders who are generalists. Fifty years ago, as society switched from family-owned businesses and employment through entitlement, to a more meritocratic and efficient approach to enterprise, good management was crucial – as it still is today. But the pendulum may have swung too far towards general management functions and away from core business functions. We know, through the work of Nick Bloom and John Van Reenen that good management practices have a positive impact on organisational performance. This has been found in many settings. However, the authors also show that in hospitals, for example, performance improved when clinicians were also the managers. In other words, management should not be separated from clinical functions.

We all admire German cars. It is very likely that these firms perform well because their engineers move from the shop floor into the boardroom, thus taking a deep knowledge of the core business with them into the more strategic areas of the firm. A more common setting for debates of this kind is sport – does it matter that the coach of my beloved football team was a good player? It does, in case you are interested. The managers of the 92 clubs in the English football league have an average of 16 years playing in senior clubs. Alex Ferguson, arguably Britain's best football manager, who played for both club and country, had an average scoring success of one goal every second game in his professional career (and don't MUFC mourn his loss).

Although we admire entrepreneurs, scientists, engineers, artists, and others with ideas, we typically assume that they are no good at running an organisation. I have found these assumptions to be wrong. For example, in professional basketball, we found that teams that win the most are those led by former star-players. Most hospitals in the US and the UK are led by managers with no medical training. Yet I found that the most outstanding hospitals in the US were led by CEOs who are doctors. Similarly, the most successful universities in the world are led by presidents who are also highly respected academics.

A recent study, with co-author Ganna Pogrebna from Warwick University, looks at one of the world's most competitive high-technology sectors – Formula 1 competition. Our study collects and analyses 60 years of F1 data from which each organisation's performance can be measured objectively. We find that the most successful team leaders are more likely to have started their careers as drivers or mechanics compared with professional managers or engineers with degrees. But we find the most notable association between driving and the later success as a leader. Within the sub-sample of former drivers, those with the longest driving careers go on to be the most successful leaders. Prominent examples include former top drivers like Jean Todt of Ferrari and comparative newcomers like Red Bull's leader, ex-driver Christian Horner.

Arguably, hiring the best people is central to the success of any organisation

So why might experts make better leaders?

We believe that hands-on experts have a deep intuition and wisdom that helps inform their decision-making. The understanding expert leaders have of the core business gives them better strategic vision, helping them to identify more business opportunities and challenges – risk-taking is also likely to be better calculated. Having been on the shop-floor, experts know how to create the right work environment and command greater respect having proved they can 'walk the walk'. The long period of training or on-the-job experience required of experts may endow them with a longer view, both to success and to income and profit generation. And as leaders in a specific field, experts model excellence, inspiring the people who work for them to go above and beyond in their own quest for quality. In short, expert leaders may be more likely to bring out the best in their core-workers.

Arguably, hiring the best people is central to the success of any organisation. Experts may hire better people. If it is a leader's job to set the standards in an organisation, one might assume that the standard bearer should first meet the standard. Who gets hired as leader may send a signal to the outside world about both the credibility of the head (someone who has walked-the-walk) and an organisation's strategy. Hiring an expert leader may also signal credibility to a wider audience (media, shareholders, the market, etc).

Let's be clear: to be an expert leader one also has to be an expert manager. But we're accustomed to seeing *Fortune 500* firms choosing charismatic general managers for senior leadership positions over core-business experts. We're also used to seeing CEOs flit back and forth across industries, becoming jacks-of-all-trades, masters of none. Might our organisations be paying the price? If we want to boost our economies and our companies through innovation and entrepreneurship, and if we want to solve major global problems like climate change, I believe we need more specialists and fewer generalists running organisations – real experts, not managers.

Amanda H Goodall is a senior lecturer at Cass Business School

Lack of relevant experience can be to blame for catastrophic failure

Companies that hire leaders with minimal core-business knowledge are taking risks. In fact, Airmic's *Roads to Ruin* report found that one of the main factors of catastrophic failure was board level risk blindness often caused by lack of relevant experience.

A chief executive does not always have to have expertise in the business they run. What is critical is for strategy and operations to be connected. As our research shows, in an event of catastrophic failure there has often been a disconnection between strategy and operations. If the chief executive is not an expert in the field of their business, they must have a governance structure enabling them to be connected to the operations (eg Richard Branson is not a lifetime pilot, but he put together a team who knew how to run an airline).

Similarly, in risk and insurance, more and more chief executives are from a finance background, as opposed to operations. But that doesn't mean the business will be put at risk, so long as the risk function is well connected at a governance level with the board, non-executives are giving good advice and are challenging the chief executives where necessary, and the organisational structure is enabling an information flow essential to maintain the connectivity of the board.

The common denominator in most cases of catastrophic failure is less likely to be the chief executive's background; but how the business fits together, its governance structure and culture.

John Hurrell, chief executive, Airmic

Bénédicte Huot de Luze

'AMRAE's board of directors and its president have implemented a real strategy based on their experiences'

What are you thinking right now?
The future of risk management as AMRAE has recently published the first risk manager framework, which lists the competencies and personal skills necessary to become a risk manager. The association also wants to carry on building relationships with risk managers' associations and risk managers worldwide as we are witnessing the emergence of an international community of risk managers.

What is your most treasured possession?
AMRAE's members. One of the most important aspects of my job is to meet members and hear about their needs and experiences, how they approach problems, what solutions worked and what did not, their successes and failures. It's always interesting to hear risk managers discuss ways to improve their jobs. This fits well with the AMRAE's mindset of research, discussions, publications and sharing.

Who is your greatest hero?
AMRAE's president, Gilbert Canameras, of course!

What's the biggest risk you have taken?
Leaving KPMG for AMRAE 12 years ago, after having developed a risk management and internal audit department there. I wanted to concentrate on risk management. I prefer taking risks than auditing them.

What is your greatest fear?
Missing an important issue, failing the needs of, or misunderstanding the worries of, our members. Even though we collaborate closely with our scientific committee, there is always a risk of missing a subject, pushing the wrong agenda or forgetting something.

Tell us a secret?
AMRAE's board of directors and its president have implemented a real strategy based on their experiences. The board of directors has defined the goals, the ways and the resources required to address the needs of risk managers. Do not repeat this, but AMRAE works, is organised and governed with the same attention to detail as a real business.

What makes you happy?
Schools, businesses, members, the FERMA certification project, all these stakeholders understand that tomorrow's risk management will be a real tool for performance and support in business strategy. Back to reflection! Analysis and decision of acceptable risk are back in business thanks to risk managers. In this context, I am happy and proud to notice the growing success of our training programs. It is a real proof that we meet expectations. We worked so hard in the past years to make the stakeholders aware of the added value of risk management. Now, they will find at AMRAE Formation the Holly Grail: the ARM program!

What is the most important lesson you have learnt?
A professional association should concentrate on the concerns of its members. If it offers a platform for discussions, reflection and interesting and relevant publications, it will be of interest to risks managers. They, in turn, will want to share their problems and solutions. This approach is in the DNA of a professional association such as AMRAE. SR

Bénédicte Huot de Luze, chief executive, AMRAE

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