StrategicRISK

Risk and corporate governance intelligence

ASIA EDITION

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RISING FORTUNES

Asia on the road to better risk management

Risk Report
The Philippines has one of the fastest-growing economies in the world, but it remains vulnerable

Risk Atlas
Corporates operating in Asia face growing demographic challenges

Class Notes
A new educational series looking at practical ideas for managing a variety of risks


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Better risk management – ample food for thought

THIS IS A SPECIAL ISSUE OF *STRATEGICRISK* ASIA DEDICATED TO OUR region's journey along the road to better risk management. This reflects the theme of *StrategicRISK*'s inaugural annual conference in Asia held in Singapore recently. The Strategic Risk Forum 2014 was a free, invitation-only event for chief risk officers, chief financial officers, corporate insurance managers and corporate treasurers responsible for risk management and insurance procurement for APAC's largest corporations.

The forum featured risk professionals and specialist brokers who explored current and emerging trends in some of the key risks affecting companies today. The emphasis was on discussing practical steps companies can take to identify, assess, manage and mitigate these risks. Topics of discussion included developing a truly practical cyber risk management programme; learning lessons from natural catastrophes; managing the risks of operating across international borders; coping with regulatory change; and identifying and mitigating main people risks.

Although we know that extreme climatic events will affect more and more people in the future, we tend to have short-term memories about past events

We have extensive coverage of the forum throughout this issue, including the 'All eyes on Asia' feature on pp7-13 and a piece on the director of corporate insurance at Thai Airways, Kittiphan Sallakanonta, who spoke at the event. Joining him on the 'Coping with Catastrophe: Lessons learnt from recent Nat Cat Events' panel was Lenny B Conil, risk and business continuity manager at Veolia, whose profile appears on pp15-19. Conil told the forum's audience that although we know that extreme climatic events will affect more and more people in the future, we tend to have short-term memories about past events. His recollections from the 2011 Tohoku earthquake and subsequent tsunami and the Fukushima Daiichi nuclear disaster make for fascinating reading. In typically understated fashion, Conil says it was an event that made it "easier for people like me to convince the board or operational people that we really need to have contingency plans".

We also have special features on two issues that featured prominently at the forum, which are now firmly part and parcel of Asia's risk landscape: construction (pp27-30) and people risk (pp32-37). Add to that a preview of the upcoming *StrategicRISK Asia Risk Report* on the Philippines (pp22-25) and the first instalment of a new educational series (Class notes, p40), which looks at practical ideas on how to approach and manage a variety of risks.

I believe this issue will leave you with a great deal to think about, and I hope you enjoy the read.

Sean Mooney, ASIA EDITOR, STRATEGICRISK

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Risk professionals and specialist brokers participated in *StrategicRISK*'s Risk Forum in Singapore

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Businesses operating in the Philippines may be exposed to risks at the sharper end of the spectrum

The rise of the Asian megacity has multiplied demand for construction – and the complexity of the risk landscape
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The complexity of people risk means risk managers and HR need to work together and apply a holistic approach
page 32


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RISK ATLAS

The next generation

As people around the world live longer, older populations will be dependent on a smaller proportion of working-age citizens. As a result, firms must be aware of the political and socioeconomic risks likely to arise

THE EARTH'S population is on course to reach 9.3 billion by 2050, according to the World Economic Forum, a growth rate that is bound to present governments and businesses with serious challenges.

Currently, about 7.2 billion people live on the planet, but the proportion of non-working-age population is increasing, owing to significantly longer life expectancies in much of the developed world.

This presents a major risk to businesses and governments as a proportionally smaller workforce must support a growing non-working population amid an increasingly sensitive global economy.

Maplecroft's Working Age Population Trends Index (WAPTI) shows the highest risk countries – those with slow-growing or possibly shrinking working-age populations – are found predominantly in the developed world.

European countries, particularly at the eastern edge of the continent, account for 19 of the 20 highest-risk countries in the index. Bulgaria, Moldova, Georgia, Latvia and Ukraine constitute the top five.

Key economies in Asia are also vulnerable to these demographic risks, as *StrategicRISK* discovered after hosting a roundtable in Manila, as the Philippines faces a significant challenge to manage a rapidly increasing working-age population, with many skilled professionals opting to find work overseas.

However, shrinking working-age populations are of particular concern in China and Japan, which are among the nations that are most at risk in Maplecroft's WAPTI.

China's turning point

China's demography has played a significant role in its economic development, with a seemingly inexhaustible labour supply helping to restrain unit-labour costs. This has driven rapid economic growth based on cost-competitive exports and high levels of investment.

However, China is classed as an 'extreme' risk country in Maplecroft's WAPTI because the enforcement of its one-child policy means that the demographic dividend has passed relatively quickly. In fact, recent International Monetary Fund research indicates that the country could reach the Lewis Turning Point – the moment at which it becomes a labour-shortage economy – between 2020 and 2025.

Reaching this point will have important ramifications for the Chinese and global economies, according to Maplecroft, signalling a definitive moment in its transition from production-led growth, with its associated wage repression, to one in which labour holds greater bargaining power and the wage share of the economy can be expected to rise from today's depressed levels, boosting household consumption.

Ageing Japan

Japan is another rare non-European country in the highest risk category. More than 25% of the country's population is forecast to be over 65 by 2030, increasing to 38% by 2055.

This dramatic demographic shift means the total population of Japan is forecast to shrink by almost a quarter, from 128 million to 95 million in the half-century to 2050, leaving its substantial

POPULATION GROWTH PER 1,000 PEOPLE, ACCORDING TO CRUDE BIRTH AND DEATH RATES

1	Philippines	+19
2	Mexico	+14
3	India	+13
4	Indonesia	+13
5	Malaysia	+13
6	Turkey	+11
7	China	+5
8	UK	+4
9	Portugal	-1
10	Japan	-2
11	Germany	-3

Source: World Bank

'Businesses must be aware of the demographic landscape in regions where they operate'

debt burden to be shouldered by a smaller population.

The government faces a significant challenge to support its elderly citizens while continuing to stimulate growth and encourage financial success without the basis of a growing work force.

Crude birth rate figures, the dominant factor in determining population growth together with the age structure of the population, is calculated by the annual number of births per 1,000 people at mid-year. A nation's natural population growth – excluding immigration – can be calculated by subtracting its crude death rate from its crude birth rate.

Using this method with the latest World Bank data reaffirms Maplecroft's analysis. Germany shows the greatest natural population decrease at a rate of -3 per 1,000 people and Japan follows closely at -2. At the other end of the spectrum, the Philippines' population is growing at a rate of +19 people per 1,000 each year, with India, Indonesia and Malaysia on +13.

Age and risk

For businesses and governments alike, the distribution of ages among the population determines the level of risk. For example, in Japan, the working-age population is 62%, according to the World Bank, which is at the lower end of average. However, its non-working-age population is predominantly made up of citizens aged 65 and over, with this section accounting for 25% of the total population. That leaves Japan's 0-14 age group making up a mere 13% of its entire population and raises significant worries regarding the country's future workforce.

The country's government will need to invest heavily in the health and social care sector, and nations with young populations such as India and Indonesia will have to invest greater amounts of capital in education.

Key socioeconomic issues can arise from such imbalances, and history suggests this tends to lead to civil unrest unless significant adjustments are made, such as raising taxes or reducing spending.

Businesses must be aware of the demographic landscape in regions where they operate. An unfavourable ratio of non-working-age citizens could destabilise strong economies as the available workforce shrinks while the Earth's population continues to expand. **Asa Gibson**

EVENT

ALL EYES ON ASIA

StrategicRISK's inaugural conference in Singapore highlighted the key risks faced by businesses operating in the region

The world's fourth-leading financial centre and an important trading hub, Singapore is one of the most attractive countries in the Asia-Pacific (APAC) region for foreign business investment. Risk management has developed alongside corporate expansion, with multinational risk managers headquartered there and many more adopting an enterprise risk management (ERM) framework, so it was fitting that *StrategicRISK* Asia held its inaugural risk management conference there in July.

Themed 'The path to better risk management in Asia', Strategic Risk Forum 2014 provided a meeting place for more than 150 risk professionals and specialist brokers to exchange ideas on current and emerging risks, and also marked one year since *StrategicRISK* first launched in the APAC region.

Since the launch, the team has travelled extensively across the area – to Malaysia, Hong Kong, Thailand, Vietnam, Australia, Indonesia, the Philippines, Japan and, not least, Singapore – holding roundtables with senior risk professionals and brokers to learn about the particular challenges they face and the future risks they are concerned about most.

Not only have these findings culminated in several country reports ranking the biggest risks facing businesses, but these top stay-awake-at-night threats formed the themes for the six panel sessions that took place over the course of the day. These included: emerging cyber threats; coping with natural catastrophes; managing risks across international borders; regulatory change; managing people risk; and risk-management maturity.

One key observation from these meetings was the speed at which risk management is developing across APAC, evidenced by various new risk initiatives and the enthusiasm among the risk community to expand its knowledge.

"These are exciting times for APAC," said Mike Jones, UK-based editor of *StrategicRISK*, who set the tone for the rest of the day with a confident look at the future.

Opening the conference, he said: "Much has changed for the profession and businesses since *StrategicRISK* was first established in 2000 in Europe. After narrowly avoiding a financial apocalypse within the Eurozone, Europe's economies are stagnant and its businesses are looking east for growth potential.

"While Europe threatens to implode through a combination of a lack of innovation and collective inertia, Asia, by comparison, is booming. Businesses and national economies are developing rapidly to maintain their positions on this upward curve.

"Risk managers are at the forefront of this [phenomenon], and the launch of *StrategicRISK* in Asia is indicative of this.

"From academia to science, regulation to reputation, politics to terrorism, we have sought insights from the most pioneering minds to help guide our readers to better understand and deal with the enormous and testing complexities surrounding modern business risk.

"Since *StrategicRISK* Asia was launched a year ago, I have had the good fortune to spend some considerable time meeting with risk managers, brokers and insurers in many countries across the region, and have been impressed not only by their thirst for knowledge, but also by their ceaseless desire to create or refine new and effective strategies.

"The initiatives being developed in the region provide a glimpse of an exciting and innovative future ahead, and I look forward to exploring this with you today and in years to come."

Weathering the coming cyber storm

The first session of the day started with a thought-provoking debate about cyber risk after Jones challenged the panel to consider how the word 'cyber' is often misused and misunderstood.

'Cyber' is such a nebulous term, and the risks – and, indeed, the opportunities – associated with this term depend on what people perceive the meaning of the word to be," he said.

"There is a clear and definite interconnectedness around these risks, which are perhaps better described as intangibles – non-physical risks.

"Cyber is just one of a growing number of threats that sit within the intangible spectrum – together with intellectual property, content, branding and, ultimately, reputation, which is perhaps the most overarching risk of all." »

Photos: Richard Koh

» A spectrum of risks

The panel agreed that because of the interconnected nature of cyber risk, there is no one way to define what this means. Five panellists offered five different, yet interconnected, definitions of cyber risk, and provided examples of incidences that many businesses will recognise.

The panel described a landscape where cyber risk stretches from infringing corporate privacy laws and data breaches to events involving seemingly innocuous yet negligent employees failing to carry out everyday security measures; from physical and non-physical data theft perpetrated by organised criminals to disgruntled staff; and from business competitors to state-sponsored political attacks.

In today's business world, cyber can be best described only as a spectrum of risks. To tackle the risk effectively, Microsoft's chief security officer for Asia Pierre Noel warned delegates against two key phases of an attack.

"There is an ecosystem where 'bad guys' access your systems and install some damaging weapons to steal intellectual information. This phase can be quick and stealthy, and malware can remain in your systems for weeks, months, years – during which time your business will be open and vulnerable to attacks.

"Other bad guys from the ecosystem can – and this is the second phase – rent access to these malware for a period of time and remotely instruct your systems to syphon or destroy valuable information, or blackmail your organisation."

Access to companies' crown jewels

For Matthew Clarke, head of PI and acting head of cyber insurance, Asia-Pacific, at AIG, risks to a company are not only external but also come from within the business. He warned that businesses are increasingly being subjected to social-engineering tactics, where senior management – namely chief executives – are targeted with apparently innocent emails, but in fact these are malicious software in disguise.

"I'm not talking about employees maliciously attacking the company or leaking data – I'm referring to their lack of understanding about the risks in the market, which often lead them to open harmful emails. For example, a week or so after this conference, you may receive an email that appears to be from a contact you made here.

"A PowerPoint presentation is attached. You download it, and before you know it, the hacker is in and has access to the business's crown jewels. These social engineering tactics are taking place more and more, and are increasingly targeting chief executives because they usually have the greatest access to information."

Reputational repercussions

The effect of any event on the cyber risk spectrum, no matter how small the attack, can have far-reaching consequences. The panel summed up the key ramifications of an attack. Although business interruption and financial loss were key features in the debate, the potential for reputational damage raised the most questions from the floor.

Gordon Song, head of ERM and internal audit at Tigerair, started the reputation debate, stating: "It's not only the financial implications that businesses have to worry about, it's also the reputational damage.

"Fundamentally, [preventing cyber threats] is not so much concerned with [stopping] the act of intrusion or the act of being attacked because, if a criminal really wants to attack you, they

THOUGHT LEADERSHIP

Pollution risk awareness

In one form or another, almost every company faces environmental impairment-related risks. Most companies mitigate these risks through procedures and processes such as environmental management plans, waste-management plans, chemical inventory procedures, pollution testing and monitoring.

But despite best efforts to mitigate such risks, pollution incidents do occur, and the subsequent third-party bodily injury and third-party property damage claims, remediation costs and the business interruption losses faced by the company that caused the incident can be significant. Even worse, 'standard' insurance policies, such as public liability and property, are often inadequate to cover all the exposures associated with these incidents.

It is easy to visualise the pollution risks associated with mines, petrochemical plants, pipeline operators, oil tankers, and tank farms. Asia has seen its fair share of pollution incidents in the past few years, including well-documented oil and chemicals leaks in China, mining-related pollution incidents in the Philippines and Indonesia and offshore pipeline leaks in Thailand.

These events tend to result in a greater social awareness of pollution incidents, and consequently, governments in the region are reacting to their voter base by developing more stringent regulations or enforcing existing regulations more strictly. What this means is that the pollution-related risks companies in the region face are heightened owing to the greater probability of receiving a third-party claim or a governmental claim arising from a pollution incident.

Even companies considered to be 'less hazardous' can often be entangled in a pollution incident. For example, hospitals and healthcare facilities are exposed to potential pollution incident-related claims because of the hazardous waste they generate and the tanks they have onsite to fuel emergency generators, as well as more healthcare specific issues, such as healthcare-associated infections, microbial matter and Legionella, among others. Trade contractors are also exposed to the potential of such claims.

Unfortunately, the 'standard' suite of insurance products such as public liability or property does not typically respond to pollution incidents that may occur either through site operations or contractor works. For this reason, environmental impairment liability policies specifically designed to cover these pollution incident-related risks through first-party and third-party coverages have been developed by underwriters, and are being more commonly purchased in the region. In certain instances, these policies are even being used in merger and acquisitions, as contamination-related exposures are typically excluded from standard representations and warranties contracts.

Jota Shohtoku,
vice-president, general casualty, Allied World Asia

ALLIED WORLD

will, and they will succeed. The most important thing is your response and resilience levels.

"The biggest risk for any company is the failure to respond effectively to an incident, rather than the failure to prevent the event. Many recent events have shown that the real 'crisis' for companies was in the badly orchestrated response to incidents – including the failure to address social media and stakeholders, and the poor control over essential information."

Insurance solutions

Panellists then scoped out an effective cyber risk programme. A central issue to the discussion was which steps companies were taking to incorporate internal stakeholders in their cyber risk programme.

Delegates questioned the panel over whether insurance is failing to take account of the interconnectedness of cyber risks, and whether it is reasonable to expect insurers to provide solutions with an approach of 'wholeness'.

Gary Chua, head of FINPRO at Marsh Singapore, suggested that a good cyber strategy involves getting the right balance between insurance and a robust risk management programme.

He added: "Risk transfer solutions do not supersede the risk processes you may have in place; they serve to complement them and act as a safety net if it all goes wrong."

The panel concluded that, above all, risk managers can successfully combat cyber threats only if they have the support of their board. However, for many in the APAC region, there is a worrying disconnection between boards and the risk function.

Coping with catastrophe

The next panel session, 'Lessons learnt from recent nat cat events', brought together four risk professionals with hands-on experience of preparing for and dealing with the consequences of such disasters.

Kittiphan Sallakanonta, director of corporate insurance at Thai Airways, started the session with an insightful account of how the airline responded to the Thai floods crisis of 2011.

Sallakanonta and his team were tasked with challenging objectives, including preventing Thai Airways' aircrafts, components and engines from being damaged by floods.

Many risks – particularly those related to natural catastrophe – carry a reputational threat, and it is crucial that businesses seek to protect their reputation. It was no different for Thai Airways.

Sallakanonta's team devised a plan to ensure the airline repaired any damage to commercial aircrafts and engines on time, and to the highest quality. That plan came in several stages.

The first was the preliminary actions the airline took before the arrival of the floods. This included building water barriers around the airport and renovating the electrical systems, relocating equipment or protecting it by elevating it 50cm–60cm above ground.

Crucial to this stage was a meeting Thai Airways held with its insurer to agree an interim payment based on the airline's loss calculations.

Sallakanonta then explained the action plan for facing the floods. This included activating the continuity plan; moving priority equipment to designated storage areas; activating water barriers, gate valves, pumps, power generators and flood protection equipment and preparing for evacuation.

In the immediate aftermath, the team conducted site and settlement assessments, located damaged areas, assessed the final

THOUGHT LEADERSHIP

Five top cyber tips for risk managers

Sophisticated risk managers are well aware of the increasing level of risk posed by cyber crime. Add to this a dynamic background of legislation and regulation, privacy protection and consumer scepticism and even the most forward-thinking of risk managers may need to pause to catch their breath. These exposures are now too extensive and serious for risk managers to tackle on their own; the require full engagement of senior management and, more critically, the board of directors.

Risk managers can take some simple steps to manage the exposure and mitigate the potential impact of a cyber attack. It is an obvious starting point, but the first step is to understand your company's exposure. What information does the company hold that is critical in the day-to-day operations? Where is it stored and with what security? If you use cloud computing, where is the cloud physically located? Do you keep personal information about customers and staff or credit card details?

The second step is to get buy-in from your employees. They can be the greatest defence or your Achilles' heel. But employees are also still one of the most common sources of a data breach. Educating employees on the responsible and effective management of data and how to recognise cyber threats will be one of the best investments a company can make.

The third step is to do the basics. Make sure your company is not a 'low-hanging fruit' for opportunistic attackers. Deploy anti-virus software and install firewalls. Importantly, keep them up to date. Encrypt all data, particularly mobile data, laptops, smart phones, etc.

The fourth step is to instigate a business continuity plan. How would your business perform if you could not access your data? What processes would need to occur to get the business back onto its feet? Once you have built a business continuity plan, test it. Refine the plan based on the results and test it again.

The last step is to talk to your insurance broker or adviser. The proliferation of cyber liability policies in the market and the broad covers they provide are an excellent safety net in the management of cyber exposures. These will help ensure that the weaknesses in your system are identified, provide you with the immediate support you need should an attack occur and help get your business back up and running at full capacity as quickly as possible.

Matthew Clarke, AIG's Asia Pacific professional indemnity and cyber manager

financial losses and agreed a claims payment with its insurer, while also activating its recovery and restoration plan.

"One of the biggest lessons I have learnt from the Thai floods is that you need to work with all sources to obtain all the information you need," said Sallakanonta.

The panel then opened the discussion to assess whether weather-related disasters have become more frequent or whether increased urbanisation in areas prone to such events are making businesses more vulnerable.

According to the Asian Development Bank, Asia-Pacific is one of the most nat cat prone areas compared to any other region. Natural disasters are now four times more likely to affect people in the region than those in Africa, and 25 times more likely than those in Europe and, in the past two decades, the region has accumulated almost half of the estimated global economic cost of natural catastrophe at about US$53bn each year. Indeed, this has forced many risk managers in the region to improve their risk management processes and risk models, and lessons have been learnt according to Dylan Bryant, Lloyd's general representative in Hong Kong.

"Following a number of catastrophes in the past decade, companies are now much more focused on managing and mitigating this risk," he said. "More time and resources are being directed at business continuity planning and preparedness. Remote working is now much more feasible and companies have made investments in making IT more secure and capable of handling a large workforce. It's also common for companies to consider temporarily shifting critical workers to offices in another country during a prolonged event."

According to Bryant one of the most important lessons learnt is around supply chain management, following the Japanese earthquake and tsunami and Thai floods of 2011. The earthquake and floods halted the production of automotive and other electrical components for a number of multinationals whose main suppliers were based in these countries. "Single point dependencies in supply chains are now getting much more risk management focus and attention," Bryant said. "Companies are also paying close attention to the business interruption element as not only the physical loss of property but also the denial of access issues need to be considered."

THOUGHT LEADERSHIP

China opts to keep weather eye on risk

More and more corporates and individuals are taking up weather solutions in Asia. Nowhere is this more apparent than China, where weather risk management is on the rise.

Swiss Re has promoted weather index solutions in China in the past few years. Although weather exposure is well known in industries such as agriculture and energy, weather solutions are still new to this country.

The emergence of weather solutions makes proactive weather risk management possible. With increasing knowledge on weather risk management, more and more companies and individuals have started to utilise weather solutions to limit their weather exposure to a bearable level.

For example, Swiss Re recently partnered with China Pacific Insurance to launch a temperature index insurance product for farmers of hairy crabs. This product compensates the farmers for the loss of output owing to persistent high temperature, measured by the weather data provided by meteorological stations. This marks the first time the aquaculture industry in China has adopted temperature index insurance.

The public's perception of weather risk in China is beginning to change. Weather risks were previously perceived as *force majeure*, and the managers were therefore not held accountable in the past when the public was unaware of weather solutions.

In the future, however, the public will question whether the managers have made appropriate decisions on risk management and whether there would have been better solutions for weather risks.

If a company manager is aware of their weather risk but takes no action against it, and merely hopes for good fortune to prevail, they are gambling with the earnings of the company against the weather conditions.

A growing number of corporates will choose to transfer part of their weather risks to professional risk bearers to reduce disruption to company operations and to concentrate the corporate resources on more strategically important areas.

Yuanyong Long, Swiss Re's weather expert for China

Although risk processes may have improved, urbanisation may intensify losses, according to the panel. Lenny B Conil, risk and business continuity manager at Veolia, said: "Although we know extreme climatic events will affect more and more people in the future, we have short memories about past events. The concentration of populations in big cities has reached levels never seen in the past, therefore a single big storm has more consequences," he warned. "Run-off is a also major factor in rain-related events; the more impermeable the ground is with roads, car parks and built structures, the bigger the downstream effects are."

Guru Rao, catastrophe management officer at AIG, agreed that urbanisation is increasing the level of loss and damage.

"About 15-16 years ago, I undertook a project in Chicago where I compared catastrophes and their effects in developing countries to those in developed areas, and the big distinction was significant. Developed countries suffered more property and insured losses, while developing countries suffered more from debt and loss of lives.

"Sixteen years later, Asia's economy is growing quickly. In 40-50 years, some of the megacities in nat cat prone areas in Asia are going to experience a four to sevenfold increase in population. The rapid urbanisation of megacities in Asia will contribute to increases in the type of property and economic loss that developed economies have experienced"

Ly Xuan Thu, head of risk and compliance at Vietnamese investment management and real estate development firm VinaCapital, concluded the session by suggesting that whatever the issue – whether natural catastrophes are increasing in frequency or urbanisation is intensifying the loss – natural catastrophes are a real threat in a globalised business world.

Thu suggested all businesses should implement an environmental, social and governance (ESG) plan: "For many countries in Asia, ESG will be mandatory in the future, so it is advisable for all the companies represented here today to start thinking about devising an ESG framework.

"This framework will help measure the effect and likelihood of ESG risk in a sustainable way and is also a good way of minimising the risks from climate change-related issues."

New frontiers

The session on how to manage the risks of operating across international borders produced some interesting debates about the biggest risks for multinationals and how the risk landscape is likely to change in the next five years.

Li Shan, underwriting director at Zurich Insurance Group, Singapore, suggested that corporates with operations abroad must get to grips with three other risks: regulatory changes, extreme weather and political instability.

Shan explained that planning an efficient and cost-effective multinational insurance programme was becoming ever more complex as regulation increased around the world.

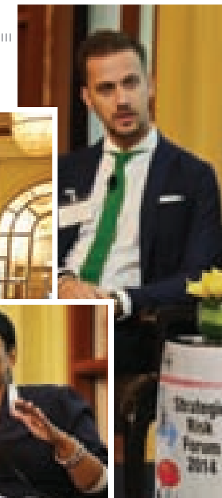
She said: "With the global economy in expansion mode once again, Asian multinationals may be exposed to unfamiliar legal systems and faced with compliance challenges in the jurisdictions in which they operate.

"Complying with local insurance regulations and laws is of increasing importance for multinational businesses, as lawmakers across the globe – especially in emerging markets – increasingly take an interest in previously unregulated or loosely regulated activities. This compliance could prevent unanticipated reputational, tax or financial repercussions."

Singapore-based risk and governance professional Eric Lee Chuin Howe added that human capital is an important problem for multinationals. "We are only as good as the processes and the people who run the show. If your human capital risk is not managed, there will be high turnover, and your processes will fall through the cracks – these risks are important when operating across borders." »





» The discussion then moved on to the challenges of implementing ERM across Asia-Pacific. The main message was that a one-size-fits-all approach was unrealistic. It was agreed that to successfully embed ERM, risk managers must adapt and align their risk or ERM strategy with the mindset and cultural differences of the country in which they want to implement the framework.

Geetha Kanagasingam, Singapore-based vice-president of group risk at Barclays Bank, summed this up well, commenting that risk culture must be cultivated and integrated with the overall organisational culture and values across the region.

She added: "ERM is about connecting the key-risk dots across the departments and territories in which you are operating.

"This provides a holistic view of an organisation's risk profile, so your action plans can be developed to address the key risks effectively, resulting in better-informed strategic resolutions and decisions."

Regional regulatory change

Next, there was a practical session on regulatory change in the APAC region. Panellists touched on data protection and management, employment regulation, directors' liability, trade practices legislation and a perceived lack of consistency in the regulatory environment.

Risk management expert and Pan-Asia Risk and Insurance Management Association board member Steve Tunstall said corporate governance was becoming an important issue for risk managers. "The recent changes of the Singapore Code mean directors now have to talk about risk management in their annual reports, and this is driving more interest in the topic.

"Not only do you have to do that, but you have to watch out for the fact the compliance field is changing dramatically all the time – it's [vital to keep] up with the changing regulations in your area, making sure your company is on top of them and dealing with them in a practical and pragmatic manner."

The panel then considered whether the region is experiencing an increase in regulation or whether the enforcement of existing regulation is increasing.

Amy Sommers, China-based partner at law firm K&L Gates, said it was more of a "tweaking of the margins" than a greater increase in new laws: "I don't see profound change, but rather a

THOUGHT LEADERSHIP

Combating cyber risk needs top-down input

Cyber risk has shot to the top of corporate agendas across Asia in the past 12 months, as senior managerial leaders continue to gain greater understanding of the extent of the cyber threat in today's rapidly changing technological environment.

Although this increased awareness has raised the profile of cyber risk, acquiring a complete understanding of the various forms of cyber threat requires having a comprehensive knowledge of both the external risk as well as the liabilities that are specific to your company.

For this reason, companies cannot afford to treat IT security as a peripheral risk that can be outsourced to third-party security providers or even left to the responsibility of the chief information security officer (CISO). Only with an increasing ownership of cyber risk at board level will we begin to see improved cyber mitigation in the region. Organisations require an approach to cyber risk that detects opportunities resulting from technological innovation, while also identifying and mitigating accompanying cyber exposures, as well as those of legacy systems.

In this respect, responsibility for cyber security needs to sit above the role of CISO; it must sit with the board. This is because the board, although not managing day-to-day cyber risk responses, needs to be satisfied these are robust.

Top-down work must be carried out to map all areas of a company's technological infrastructure, data-related tools and systems and processes. This will make it much easier to establish those points of weakness that are traditionally found at connection points between programs and systems.

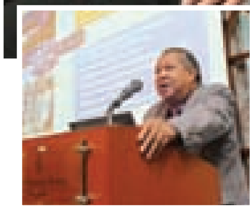
External service providers must be carefully assessed and must be clear on any liabilities and recourse rights. The training of staff is equally important, as human error is also a major cause of data breach.

With these areas identified, businesses can begin to quantify the risk in terms of its potential financial impact and develop an incident response plan in the event of an incident. This should involve undertaking a programme to improve the general understanding of the company's technological structures and how they are integrated throughout the entire organisation.

Finally, insurance can also play an important part in a business's cyber mitigation strategy. Although insurance cover will never eliminate the risk entirely, company data identifying cyber liabilities and any potential impairment to reputation that may lead to loss of business are essential to enable organisations to assess the risk at hand.

As such, this exercise will enable them to determine whether it is value for money to transfer the risk to the insurance market.

Stella Tse, Marsh financial and professional risks (FINPRO) practice leader, Asia



more committed or more intense level of enforcement.

"Some comments were made [at the conference] about economies in other parts of the world being stagnant. APAC is one of the most dynamic places in the world that is also relatively stable. So, as more and more is invested here, it is not surprising that regulators perceive the need to increase the level of scrutiny and enforcement activity."

She added that areas of increased enforcement relate to anti-money-laundering laws and anti-monopoly enforcement, explaining that the Association of Southeast Asian Nations has created a network to tackle money laundering and corruption. These efforts include training on how to track legal financial flows.

Summing up

Strategic Risk Forum 2014 ended with two more sessions: one looking at the regional fight for talent, covering the effect of Asia's ageing population and the shortage of skilled workers; the other reviewing risk management maturity. It provided much food for thought, and – as the theme suggests – perhaps helped many consider paths to better risk management in Asia. **Kin Ly**

THOUGHT LEADERSHIP

Fast growth means increased complexity and greater need for right mix on risk

The fast pace of economic growth in Asia is attracting new investment to the region and encouraging successful local businesses to expand into new markets. However, these growth opportunities are not without complications. Businesses must manage more complex supply and distribution chains and negotiate a patchwork of differing levels of market sophistication, risk and regulatory standards.

At the same time, Asia is going through an increased pace of regulatory development and heightened supervisory scrutiny – which is more than enough to keep most risk managers on their toes.

The issue of consumer protection still dominates regulatory agendas in Asia. Both Singapore and Malaysia have recently introduced data protection legislation that will have a significant effect across industries. Every company must now be periodically checking whether the information it collects is relevant and necessary and undertaking regular risk assessments of its systems and controls.

To ensure best practice, it is worth creating a retention policy that sets the time period for a decision to archive or delete data. Should an individual object to their data being held, it must be immediately deleted, and it is good practice to maintain a list of objectors so they are not contacted again. Regularly training staff is fundamental. It is also crucial robust controls are in place to ensure personal data is held in a secure medium and that access is restricted to those who need it only.

There is also an increased focus on financial crime, with new anti-money laundering (AML) regulations, stricter requirements for customer due diligence and the looming compliance deadline for the US Foreign Account Tax Compliance Act currently comprising the top concerns for most multinational Asian firms. Recent AML sanctions and enforcement actions have shown how vital it is to ensure AML screening and monitoring tools are up to date.

Embedding the right risk culture throughout an international organisation is not an easy task – it requires unambiguous and visible support at the highest level and understanding and advocacy from all. There needs to be an owner for every single risk, but also a sense that it is a team responsibility.

Good risk and compliance people understand not only the regulatory environment, but also your customers, employees and the market in which you operate. They are also good communicators. A combination of the right policies, people and culture will help to pick up an issue in its infancy rather than too late.

Kent Chaplin, Lloyd's head of Asia-Pacific

LLOYD'S

THOUGHT LEADERSHIP

Speaking the right language on multinational cover

Asian organisations are increasingly seeking to implement international insurance programmes to effectively manage a portfolio of cover across countries. A properly crafted programme can save time and reduce uncertainty, but if you get it wrong, it can cost you in terms of fines issued and may leave policies void and useless.

The question companies and their brokers need to ask is: "Where do you want a claim to be paid?" The answer we frequently we hear is: "Where the claim occurs – in which case, it is really important that companies are aware of the local regulations.

To give an example of the complexity of dealing with local regulatory requirements, some countries do not allow non-admitted insurers to provide important insurance-related activities such as claim payment, risk engineering services and loss adjustment activities. In certain countries, policies cannot be backdated, while others require cash before cover; in fact, many countries are now imposing additional minimum premium requirements. Tax is becoming an increasingly important consideration.

International programmes offer the convenience of pulling together insurance under centralised control, with uniform policies for every country where subsidiaries operate or have exposure to risks. This brings greater certainty and transparency, but requires detailed understanding of myriad local regulations.

A carefully planned international programme that runs smoothly provides greater certainty of cover you can rely on. From the start, clear channels of communications need to exist between the insured, the broker and the insurer. Even administrative errors can delay matters, so standardising processes can reduce errors.

Other useful actions include ensuring local contacts are aware a programme is in place; keeping abreast of changes in local conditions, policy restrictions and cover limits; ensuring minimum premium requirements and tax liabilities are adhered to; making sure you understand cash before cover requirements and whether backdating cover is permissible; and ensuring necessary documentation for particular countries is prepared – for example, to meet anti-money-laundering regulations.

Companies looking to effectively protect their business overseas would be wise to choose an insurer with an international network of offices, and local experts who understand local issues and policies. Organisations should choose insurers that offer tools to provide a comprehensive oversight of their risks across the world through tracking of insurance policies and coverage, and knowing the status of claims, documents, tax liabilities, risk assessments and actions. This will give companies the best chance of protecting their business, not falling foul of local regulations, avoiding fines and policies being declared void, and actually getting the claim paid where they need it to be paid.

Reg Peacock, head of customer, distribution and marketing, Zurich Global Corporate APAC

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VIEWPOINTS

Photos: Richard Koh

CAN-DO ATTITUDE

PROFILE: LENNY B CONIL

As Veolia's risk and business continuity manager for all activities (water, waste and energy) in Asia, Lenny B Conil has proved he is more than equal to the multitasking challenge

CV

- Lenny B Conil was born in France and has an MA in science from Cranfield University and another MA in engineering, water sciences and technologies from Polytech Montpellier
- He is co-founder and committee member of the French Association for Solidarity (FAS) Hong Kong
- Conil is a keen photographer – he co-founded Dragon Eye Photography in Hong Kong in 2009

When he first moved to Asia in 2006, Lenny B Conil says it felt as though hardly anyone knew what risk management was and, if they did, "it was seen as something painful you had to do".

These days, the risk and business continuity manager at environmental solutions organisation Veolia believes attitudes have changed significantly in the region. "Now, it is part of everyone's culture and I receive requests from country directors to audit their sites," he says. "They want my input on any number of things, even at the business development and bidding stages.

"There's still a way to go before making risk management a huge part of the business, but it's there, it's recognised and acknowledged as something that needs to be taken care of and taken into account before making major decisions."

'Risk management used to be seen as something painful you had to do – now it is part of everyone's culture, and they want my input on many things, even the business development and bidding stages'

Varied responsibilities

The Hong Kong-based 32-year-old has been employed by Veolia as a risk and management systems co-ordinator, technical centre co-ordinator and hydraulic engineer, working his way up to his current position, in which he is responsible for the management of risk for all activities (water, waste and energy) in China, Hong Kong, India, Japan, Singapore, South Korea and Taiwan. It is an important role, no doubt, but is "actually smaller than [the one] I used to have", Conil admits.

"My role used to include Australia, New Zealand, Thailand, the Philippines and Malaysia, but our operational regions were rearranged about a year ago," he explains.

"Before, I was purely risk and crisis for Veolia Water, one branch out of the three we have, which is water, waste and energy. We merged these different activities, so now all teams are working for the three divisions and I took on the role of purely risk management."

What this means in practice is that French-born Conil is responsible for identifying, quantifying and prioritising the key risks Veolia faces in all the countries for which he has responsibility. "Because we are a listed company, Paris headquarters must be confident that we comply with rules where we have to manage and master our risks," Conil explains. "My role is to go on the different projects that we have in different countries and come up with a list per country of the top 20 risks, followed with an action plan. So I go and meet people and discuss with the experts all the different subjects possible in the company; we're talking legal, financial, image reputation, HR, operations, strategic aspects, purely technical, IT and so on."

As Conil sees it, Veolia "sells know-how" and is, by its very nature, extremely local in its scope. "We treat water or waste for a country with 90%–95% of our staff being local," he says.

"What we bring is not rocket science; it's people who know a lot about chemistry, physics, how to operate an incinerator and so on. We teach our local staff lots of things, but our expertise is not only technical drawings on paper, so we are lucky to be able to operate without really suffering any technological transfer or any criticism over taking resources out of a country."

That is not to say that the company's multitudinous operations do not face many risks. As Conil puts it: "Things are heating up here and there in Asia, so at some point that may endanger some of our economic interests".

Legal instability in China is a major issue he deals with on regular basis. "It's difficult to enforce a contract in mainland China," says Conil.

"A contract is the foundation of everything you do business-wise, therefore this leads to lots of different problems trickling down from the core issue of not having an independent legal system." Extreme climatic events are also affecting more and more people and operations, he adds.

"The concentration of populations in big cities has reached levels never seen in the past – therefore, a single big storm has much more consequences," he points out. "Run-off is a also major factor in rain-related events; the more impermeable the ground is with roads, car parks and built structures, the bigger the downstream effects are."

A memorable event

One natural catastrophe Conil remembers well is the 2011 Tohoku earthquake, with the subsequent tsunami and Fukushima Daiichi nuclear disaster, which he says made it "easier for people like me to convince the board or operational people that we really need to have contingency plans".

"At the time, it was clear no one knew what was going on and it was really difficult," he recalls. "My role was purely as a media person where I was, twice a day, seven days a week for three months, putting together a media brief for my top management in Asia and Japan. Key at the time was knowing what was going on with so much noise and contradictory information, so I was focusing on what I thought were the best pieces of news to help

the team make decisions."

Conil explains that Veolia had approximately 3,000 employees in Japan, and "therefore we needed to put plans in place". "We moved our headquarters from Tokyo to put it further from the heart of things," he explains.

"The management team moved for a month or so to Kyoto, as we were preparing for the possible occurrence of an explosion of the Fukushima Daiichi plant. We're talking iodine pills, and food and water supply in plants within concrete buildings. Fortunately, it didn't happen, but we were preparing for that."

For Conil, the social side of the equation in the areas in which Veolia operates is of utmost importance. "When we are somewhere, we have lots of things done with local schools and the community around the plant to ensure we don't just talk the talk," he explains. "We have anti-discriminatory practices, we involve women and handicapped people and we contribute to local development."

Social cohesion is vital to business success, Conil says, which is why he is somewhat concerned about instability and protests in countries such as Thailand, Vietnam and even China. "China is the big unknown," he says. "Strikes and protests happen every day in China, but people don't talk about it and the media don't really cover it because it's not properly organised, so it hasn't led to anything yet."

But Conil knows well that this kind of talk isn't what many people want to hear. "Asian cultures tend to not be too keen on anticipating bad things happening in the future," he says. "Not that any particular way is better than another, it's just a different way of doing things."

As a risk manager, he feels his role is to force people to consider, in his words, "what might happen in five or 10 years' time and how much it will cost".

"But 'let's not talk about it and hope for the best' is the type of attitude you often get," he laments. **SEAN MOONEY**

LESSONS FROM A PAST MASTER OF DISASTER

Thai Airways not only successfully protected its assets against the devastating floods of 2011, but has also raised the standard for risk managers everywhere in being prepared for natural catastrophes

ADDRESSING 150 RISK AND insurance professionals at *StrategicRISK* Asia's inaugural conference in Singapore in July, Kittiphan Sallakanonta had everyone captivated as he spoke about how his company, Thai Airways, battled against one of the costliest natural disasters in modern history: a 2011 flood that resulted in 1.4trn baht (US$45.7bn) in damages, claimed 500 lives and affected 12 million people.

From prudent mitigation planning, an ultra-tight flood response strategy and a timely clean-up operation, the director of corporate insurance at the airline gave a blow-by-blow account of how he and his team prevented the company from suffering financial losses of up to US$100m.

In his 35 years at Thai Airways, the 2011 catastrophe was biggest threat Sallakanonta has ever dealt with. But as he looked back on an incident still fresh in the minds of many Thai people, Sallakanonta recalled experiencing surprisingly little apprehension, nerves or fear in the lead-up to and during the catastrophe that swept his country.

"We had a job to do," he says, giving an impression of a man with a clear action plan and the confidence to deliver it. Crucially, notes Sallakanonta, this plan had little to do with fighting the floods, but was focused on "protecting our people, our business and the tools and equipment within it".

Indeed, protecting Thai Airways' multimillion-dollar business needed careful planning. The stakes were high – the part- government-funded enterprise owned 89 aircrafts and two airplane maintenance centres, housing tools, spare parts and heavy machinery. One of these centres was based in Don Muang airport in Bangkok, the capital, which was bracing itself for severe flooding at the same time the airline was planning its continuity operation. When the floods finally reached Bangkok, the airport's runways were swamped and all flights were grounded.

With a major potential loss for the company at stake, it was no wonder Sallakanonta stressed the importance of working with government officials to ensure its business continuity and recovery plan was down to a tee. In the lead up to what became Thailand's worst flood in at least five decades, the airline worked closely with Bangkok Metropolitan Administration and public services to track the speed, depth and severity of the floods as they moved from the north. "We gained access to satellite information, which helped us track the movement of the water," he says.

"We followed the satellite month by month and day by day so we could estimate when the floods would arrive in Bangkok."

> *'You can never be 100% prepared for a natural catastrophe – but you can ensure the best possible chance by gathering all the information you can'*
> **Kittiphan Sallakanonta,** Thai Airways

In anticipation of the floods, the team set out to protect its aircrafts, heavy maintenance machinery and spare parts. Its first step was to build water barriers around the airport, renovate electrical systems and relocate as many of its aircrafts and equipment to its second maintenance centre in U-Tapao Airport, on the east coast of Thailand. Any aircrafts or equipment that could not be relocated were covered with protective material and lifted about 2.5m above ground. The team then set up three alerts – green, yellow and red – each to be activated to signal the next stage of its continuity plan as the flood came closer to the capital.

So far, so good. However, the situation took a turn for the worse. A week before the floods reached Bangkok, flood waters were rising drastically. Hundreds of families were mourning family members and the death toll was growing, with many left homeless. Flood waters destroyed local businesses and severely disrupted manufacturing operations. The northern part of Thailand came to a halt. Thus, when the government announced that the floods were about 100km away from the capital, Sallakanonta and his team had to change their plans.

"Officials decided to save the inner part of Bangkok, the country's business centre. Allowing the floods to swamp the


Richard Koh

business hub was not an option because it would drastically paralyse the economy. Bangkok Metropolitan decided to contain the water at Don Muang airport and to turn it into a water-receiving area. This was where our heavy metals were located," he says.

"Giant bags full of stones and sands were placed around the city and the government built flood walls to protect much of the inner city areas and to block the water or encourage a change of direction to the western part of Bangkok and Don Muang airport. We learnt that flood waters had reached 2.5m high in just one week of reaching the capital."

But before the floods started to rise in the city, Sallakanonta says "there was so much to consider: what do we do with parked aircrafts and those in the maintenance centre? Where would we store and protect our spare parts? We had to make decisions and make them quickly.

"For any aircrafts that could not be moved into the hangars and lifted, we had no choice but try and block the flood waters from damaging the inside of the airplanes by placing sandbags at their doors to prevent water from leaking inside. We could not save everything and we had to come to terms with having to lose spare parts we could not relocate. This was when the risk transfer element of risk management became important."

Sallakanonta and his team calculated the potential loss for the company prior to the floods and approached its insurers for interim payment of a total sum of US$45m, which it then began using to purchase new equipment and tools.

"We told our insurers that we needed the claims money to be injected into our pockets as soon as possible," he said. "It was difficult to secure the sums – asking for interim payments of that amount had never happened in the history of Thai Airways. But armed with a thorough loss assessment report based on estimates of the damage, we received the go-ahead."

The eye of the storm

With some of its physical assets protected and interim claims paid, the next phase of the continuity plan was the hardest to deal with. When the floods reached Bangkok in October 2011, they devastated the capital, Sallakanonta recalled. Some of the northern parts of the city were 90% submerged by rising water, according to reports.

Authorities issued a five-day holiday in Bangkok to enable residents to relocate. People living in an evacuation shelter at Don Muang airport were being told to move. The runways were flooded. It was time for Thai Airways to sound its red alert and launch its evacuation plan.

"During the 40 days it took for the flood waters to drain, a group of 30-40 members of staff recovered our undamaged tools, equipment and aircraft and moved them out of the facilities to prevent further damage. They worked around the clock to ensure they were safely relocated.

"Our operation and command centres were based in a property affected by the floods and so we moved these functions elsewhere. Anyone who could not go home stayed in temporary accommodation and the head office sent food and water supplies. These were dedicated members of staff who woke up every morning to work and ensure our operations were still running."

Once the flood waters had finally drained, the team was quick to conduct a series of site and settlement assessments, locate damaged areas, assess the final financial losses and agree a final claims payment with its insurer, while also activating its recovery and restoration plan.

"One of the biggest lessons I have learnt from the Thai floods is that you need to work with all sources to obtain all the information you require," he says."You can never be 100% prepared for a natural catastrophe.

"But what you can do is ensure you have the best possible chance of responding to it by gathering all the information you can.

"Work with the government and other public sector services to track the movements of a potential nat cat. Contact your insurers from the outset – the sooner this is done, the better, because they are they ones who can help you return to service sooner."

"By following these vital steps, you can then prepare an effective business continuity plan."

The other crucial lesson for Sallakanonta was acknowledging that risk management extends beyond the risk and insurance teams. "It was a company wide effort," he says. "Everyone extended their hand to minimise damage. No matter how small the risk, you cannot work in silos – that would be a bigger disaster."

As a result of their efforts, Sallakanonta and his extended team of risk management advocates saved the company millions. The insured losses for the airline amounted to about US$55m–US$60m, which was significantly less than the US$100m the airline initially estimated.

Cool, calm and collected in the face of one of the worst floods to affect his country, it is fair to say, Sallakanonta is indeed the eye of the storm. **Kin Ly**

QUALITY CONTROL

Now that risk management as well as the standard of goods produced are becoming more established in the Asia-Pacific region, the focus is shifting to issues of quality and maturity. Here, panellists at *StrategicRISK* Asia's recent forum share views on the way forward

ASIA-PACIFIC CONTINUES TO attract the attention of many business investors. The emergent market stands strong compared to Europe's economies, which, after inching out of a recession, are stagnant, with many European businesses now looking east for growth potential.

It is easy to see why. Developing countries in Asia-Pacific will experience stable economic growth this year of 7.1% – largely unchanged from 2013 – according to the World Bank. Although this is down from the average rate of 8% between 2009 and 2013, Asia-Pacific remains the fastest-growing region in the world.

However, the 'land of opportunity' for corporates is not without its hazards. As businesses expand into the region, the risks also grow. The question is whether risk management, as a practice and a profession, is developing at a rate that reflects the region's overall market growth.

That question formed the basis of a panel debate on risk-management maturity at *StrategicRISK* Asia's inaugural risk forum, held in Singapore in July. The panel of five risk and insurance experts – Ron Chua, director, head of risk management at Banyan Tree Hotels and Resorts; Shuh Lin Tan, director of risk management, Asia, at InterContinental Hotels; Gordon Song, head of enterprise risk management and internal audit at Tigerair; Douglas Ure, leader of Marsh Risk Consulting in Asia; and Stephen Higginson, sales leader at Swiss Re Corporate Solutions in Asia-Pacific – challenged common perceptions that Asia's risk maturity lags behind its Western counterparts in Europe and the US.

The panel agreed the risk appetite in the Asia-Pacific region is high, even if levels of sophistication vary from country to country. Malaysia and Singapore, for example, have made some headway in developing risk management standards, while Indonesia and the Philippines have a considerable way to go.

The experts said Asia-Pacific's drive to improve the quality of its risk management is gathering pace as businesses become more global and large corporations develop their presence in the region. The fact some of countries are beginning to establish themselves as essential business hubs has meant regulators are getting tough on business compliance, which is increasing the demand for robust risk management even more.

"Asia-Pacific's risk awareness has improved markedly in recent years," Song said, opening the discussion. "Much of that development is down to regulatory pressures and a positive stock exchange driving the need for international best practice. The question we should be asking ourselves now is: 'Are businesses truly embedding a healthy risk culture into their organisations?'"

Ure was quick to provide an answer, suggesting that some firms run the risk of responding to a more stringent regulatory environment by taking a tick-box approach. "Regulation has been a big driver for enterprise risk management (ERM), and that is positive," he said. "But the pressure to remain compliant can take organisations down a road of box-ticking and compliance- driven procedures that may not add value.

"Businesses need to strike a balance between meeting regulatory requirements and establishing the right risk management processes that actually make a real difference."

> *'The question we should be asking now is: "Are businesses embedding a healthy risk culture into their organisations?"'*
> **Gordon Song,** Tigerair

Nat cats

Chua steered the discussion towards natural catastrophes, suggesting that such disasters have heightened an urgency to strengthen risk management across the region. In the past decade, the region has been blighted by several deadly and economically damaging catastrophes: the Indian Ocean tsunami (2004), Cyclone Nargis (2008), the Tohoku earthquake (2011), the Thai floods (2011) and Supertyphoon Haiyan (2013), for example. In 2011, a record 77% of global nat cat losses occurred in Asia-Pacific alone, according to the Asian Development Bank.

"The effect of such disasters on business was huge and has certainly led to greater risk awareness," Chua said. "Lessons have been learnt, businesses are taking risk management seriously in light of these catastrophes. In this respect, risk management is stepping up the maturity index."

Higginson then pointed to a significant business trend: that Asia's industries are moving away from producing high-volume low-value, poor quality goods and services, to focusing on better quality products demanded by the growing middle class and those with new levels of disposable income, a key factor that will continue to encourage corporates to rethink and improve their risk management functions.


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"Look at the white goods, motor vehicles, tyres, entertainment and hospitality industries: quality and reliability are paramount to their success.

"Ten to 20 years ago, China was producing a 'lot of not very good' [products]. Now, it is producing 'less of much better' [products] and this trend is consistent across the region. This is an important move for many industries and has to be underpinned by a more robust risk management function."

Measuring risk management maturity

The panel then considered how risk maturity could be objectified and measured. A topical talking point for the profession in any region, the discussion took the form of five key factors, with each panellist offering their suggestions concerning areas that could be quantified to determine the level of risk maturity. These included reputation, board engagement, level of data analysis, quality of risk leadership and key performance indicators. Underpinning all of these measures is financial performance and all panellists agreed that an advanced ERM function will safeguard and improve profit and revenue streams.

Tan started this debate, suggesting that, contrary to popular belief, brand quality – and the risks that can harm it – can be measured. "It is difficult to quantify reputation, but there are various ways to measure elements that affect how a brand is perceived," she said. "From a risk perspective, creating a tool to measure reputation will help identify the factors that could cause damage and these elements can be measured and quantified to determine what needs to be done to manage those particular risks.

"Another area that will help build a better picture of a brand is conducting employee surveys to establish how employees perceive their company. This can be taken further, by asking customers what they think of a brand, as well as asking for its stakeholders' and owners' views. This information can then be used to make improvements, mitigate any emerging risks and ultimately use that to encourage the signing of deals, further investment, all of which can help generate revenue."

Song offered another perspective, asking delegates to consider the quality of their risk discussions. He said risk managers should ask themselves three questions when assessing risk maturity in their organisation:

1) Who is having conversations about risk and risk management?

2) Where are these discussions taking place? and

3) With whom are these conversations being had?

Taking each of element one by one, he expanded further: "Are you having these conversations with the board and are they only quarterly discussions merely to tick a box to show that you have gone through the exercise or do your risk meetings extend to an operational level and go down to every department? Is everyone in your business encouraged to talk about what is going wrong, what could go wrong and what can be done to mitigate any identified risks?

"Second, where are you having these discussions – is it only in a meeting or do you drill down the risk discussion and focus on areas such as due diligence and internal audit and any other processes that may help to identify risks?

"Last, with whom are you having these discussion? Is it a conversation only with the risk and insurance team or is it company-wide? Are these strictly in-house meetings, without the consideration of how your outsourced partners are managing risk? The majority of us here today will work with third parties, but are we taking the risk discussion to them to ensure they are as good or better at managing their risks? That could, in turn, affect your business."

Song ended his comment with a strong message, saying that a well-risk-managed business with a mature risk outlook will have an ERM function embedded throughout the business. It will be a key feature in every department, in every internal system and process, and this will be extended to outsourced partners.

"We must not," he concluded, "have risk conversations in isolation."

Ure followed by suggesting that risk maturity does not merely involve implementing risk processes and governance structures. He said a financial element can be measured.

"By looking at the cost benefits of your risk mitigation process, you can start to build a picture of how robust your approach is."

Top-down engagement

Ure added that by proactively assessing data, risk managers can demonstrate the real value of their work.

"With tangible numbers, you can tell your board that decisions have been made because they reduce your cost of risk while safeguarding the business from potential financial loss. You could even demonstrate that certain decisions can give the company a competitive advantage."

Higginson concluded the session by urging delegates to engage the board. "The word 'management' in 'risk management' is crucial," he said.

"Firstly, if businesses are to expect their workforce to buy into and practise risk management, employees need to see senior executives proactively thinking about risk. Leadership by example is always the most effective way to get the workforce to believe and to engage and this is definitely true in the management of risk.

"Second, board members have to be fully engaged and involved in the risk management commitment, because without their buy-in you are not going to get the capital expenditure required to continually invest in management of risk in a constantly evolving business environment.

"Third, businesses need to have a conduit to their shareholders too – the people who provide the money. It is essential to have a way of convincing them to see the value to their financial interest from investing in risk management. The board will be responsible for ensuring the message is delivered effectively and it can only do this if it is fully involved and has a complete understanding of the risk management approach.

The last session of *StrategicRISK*'s inaugural risk forum ended on a high note, with all panellists agreeing the future of risk management in Asia is bright. With Asia-Pacific's growth set to continue, the risk management profession will be central to ensuring that businesses maintain their positions on this upward curve. **Kin Ly**

RISK REPORT

A LAND OF EXTREMES

The Philippines has one of the fastest-growing economies in the world, but income inequalities, a growing population and being on a typhoon path mean it remains vulnerable

RISK WILL ALWAYS BE A subjective consideration: a threat to some is an opportunity to others. Risk exists everywhere and manifests itself in everything. Its scale, from non-existent or mild to serious and omnipresent, depends on perception and appetite.

For businesses operating in the Philippines many of the risks faced can be considered to be at the sharper end of the spectrum. Some extraordinary possibilities for growth exist, but there can also be a price to pay in terms of risk exposure in this country of genuine extremes, as *StrategicRISK*'s recent roundtable in Manila showed.

Attended by the country's leading risk managers and brokers, the risk professionals who took part in the discussion represented a broad cross-section of the largest and most important businesses operating in the Philippines and included representatives from the state and private sector.

From the roundtable conversation, it is clear the Philippines is fast-moving and exciting. Freed from the shackles of dictatorship in the mid-1980s, this vibrant young democracy has an almost tangible energy. It is easy to see, therefore, why there is real optimism for the future, particularly when looking at its recent performance. But can this be maintained in the longer term?

The Philippines has one of the fastest-growing economies in the world, with GDP rising by about 7% for the past three years. Unsurprisingly, many economic analysts consider it to be the "most promising" of the emerging Asian nations, particularly since its debt rating was raised to investment grade last year.

Some of this financial boom has been fuelled by the rapid growth of service industries. Although the potential for mining and manufacturing is significant, with mineral reserves valued at an estimated US$300bn as yet untapped, business process outsourcing (BPO) is the engine driving much of this economic juggernaut.

The BPO sector is currently expanding by about 30% year on year, however, the views about its real impact on the country are mixed. Certainly, it has helped grow the economy, but some question whether it is beneficial for the Philippines in the long term because it attracts highly educated people away from jobs for which they are better qualified but that pay less, if they exist at all.

The Business Processing Association of the Philippines estimates this industry has almost one million full-time employees. One roundtable participant suggested the number of call centre jobs had led to a "bubble of people without specialised skills" as they ignored further educational experiences in favour of "having their immediate needs addressed by the economic benefits provided by this sector".

Whether the critics of BPO are correct or wrong, keeping up with the growth curve at its current rate will not be easy.

Sustainable growth

Finding and developing new ways to make money is a common concern among this rapidly shifting business landscape. "Discovering and monetising new revenue streams is the biggest challenge we are tackling now," says Christine Renee Blabagno, head of ERM at telecommunications company Globe Telecom, "as we know that the erosion of traditional revenue streams is accelerating for mobile operators across the globe".

A risk manager from the power sector who wishes to remain anonymous agrees, but says the focus in his sector remains on satisfying an increasingly hungry market. "There is a lot of pressure for energy companies to come up with levels of supply to meet demand," he says.

"The big risk for us is how to get the big opportunities, prioritise them and execute them in the time in which the market requires."

Wider concerns arise that this apparent economic success story might not be all it seems as the country's new wealth is failing to filter through to the majority of its population, who remain desperately poor. Instead, a large amount of the money pours into the accounts of a small group that controls the majority of the country's big business at the exclusion of others, including foreign investors who are keen to develop interests in the Philippines but prevented by law from doing so.

As a consequence, if this situation is not addressed, the expression of fears regarding whether growth is sustainable will become more pronounced, particularly with a population that is expanding almost as quickly as its GDP.

The Philippines is the fourth most populous nation in the Asia-Pacific region but not, perhaps, for long. With Japan's population set to decline while the number of Filipinos increases, it is likely that soon only China and Indonesia will have larger numbers. In July 2014, a child named Chonalyn was born in Manila. Her arrival took the population of the Philippines to 100 million, marking a phenomenal increase of 40 million in under 25 years. The population is expanding so rapidly that it is predicted to rise another 20% within eight years and reach 150 million by 2050.

A survivor of Typhoon Haiyan stands amid destroyed housing in Tacloban, Philippines, in December 2013

Managing these numbers in a meaningful and effective way will not be easy, as Chris Dale, chief executive of Aon in the Philippines points out. "The government has major issues to address around population growth and access to jobs," he says.

"You have significant population growth and significant economic growth. Yet, none of this growth is inclusive. I am not talking about inclusive growth in terms of wealth distribution, but it is about access to education and healthcare."

Brain drain and regulation

A perceived decline in the number of students getting into highly technical professions is also affecting the ability of companies in the Philippines to compete on the international stage.

Of those who resisted the temptation of BPO wages, a number of our roundtable participants suggested the best and brightest of the country's talent often moved overseas in search of "greener pastures".

Many Filipinos leave the country to work abroad, where they can earn more and have better prospects, even if they are overqualified for their roles. People often shun highly technical professions at home to work in the service or hospitality sectors abroad.

One positive consequence of this is that the Forex reserves of the Philippines are strong, with so many expatriates sending money home, but this is hardly a solution to a long-term problem that has started to manifest itself already: in essence, how does the country manage its growth effectively?

Some might consider regulatory issues form an unwanted barrier to this but most risk professionals *StrategicRISK* spoke to agree that although regulations are sometimes cumbersome, they are a necessity. The volume of regulation is not necessarily changing, but enforcement is becoming stricter. Businesses accept this is an essential requirement as the government toughens its stance against the type of corruption that used to be endemic.

"The regulatory environment in which our power industry operates has been stringent and this has caused some delays in the implementation of projects," says a risk manager on condition of anonymity.

"Hopefully, this will end soon. Overregulation is never a solution, but we are going through a phase of transition because the Philippines is still a young country." »

THOUGHT LEADERSHIP

NICK WILDGOOSE
Global supply chain product manager,
Zurich Insurance Group

The Philippines is one of the world's most exposed nations to natural catastrophes, and manufacturers in the country need to reconsider their business interruption strategy. Indeed, many companies are starting to think about the risks they could face and developing a better understanding of the impact of an interruption on their business.

Often, organisations are too focused on internal supply chains, rather than on the external supply chain. Often, owing to cost pressures, companies do not explore proper risk management. However, failure to deliver can have a detrimental effect on a company's profitability. 'Proactive' risk management on more than a selective risk basis can add value and help companies to have a competitive advantage.

Our experience has shown that it is more important to understand the nature of the generic supply chain vulnerabilities and then to formulate cohesive ways of addressing them. This should include implementation of proactive mitigation actions to help reduce the likelihood of an adverse consequence; reactive plans and frameworks to help limit the impact if an event does happen; and agreeing on risk transfer programmes, such as insurance, to help provide monetary remuneration.

Rather than try to predict the next incident or unforeseen event that could disrupt operations, companies can examine whether their suppliers at various levels are at risk from a number of broader perils. Could an incident such as a flood or earthquake damage the supplier's premises? Is the supplier likely to go insolvent? Who or what does a supplier depend on? Who or what are the critical elements to ensure delivery, such as security, packaging or even the availability of labour? Are there any political, geographic or economic issues related to where the supplier is based? Is the quality of the goods and services being received consistent? To what extent is the supply chain dependent on particular transportation routes and what alternatives are required? Are there any other characteristics that make the supply routing vulnerable? Is risk management embedded in the supplier selection and ongoing performance management processes? Are the risk management processes being operated in an optimal manner?

It is clear that only those companies that develop robust risk management strategies with a better understanding of their supply chain will remain resistant the impact of natural catastrophes.

Densely populated housing nestles close to Manila's business district

Geographical vulnerabilities

It may indeed be new in terms of its democratic status, but some of the nation's problems are as old as time itself.

By virtue of its geographical location, the Philippines is one of the most vulnerable places on earth in terms of catastrophe risk. The country straddles the earth's biggest natural danger zone, the Ring of Fire. This connected belt of seismic activity brings an ever-present threat of earthquake and volcanic eruption.

Seismologists expect a major event will hit the Philippines – a one in 350-year earthquake – soon, but predicting where and when it will strike is an inexact science.

What can be forecast with greater certainty is the risk of a major storm. The Philippines lies in the centre of the so-called Typhoon Superhighway – a route that carries about 20 major storms of varying severity across the country each year.

Vulnerability to typhoons is not a recent phenomenon, but their ferocity and impact appear to be changing. In November 2013, Haiyan became the strongest typhoon ever recorded to hit land as it blew across some of the islands comprising the Philippines.

The damage and casualty rate was significant – 6,300 people died – but the toll would have been magnified many times had the strong side of Haiyan struck more densely populated areas.

With about one-third of the population of the country living in or around the capital Manila, there is a concentration of risk that could, if nature conspires against it, cause utter devastation not only to the city and the country's economy, but to millions of its people.

At one stage, Haiyan was tracking towards Manila only to shift course as it bore down on the islands. It was a lucky escape that might not be repeated again.

Manufacturing facilities and infrastructure projects are at risk

from floods, high winds and storm surges. Many facilities have been reinforced and elevated and the government's disaster planning is evolving continually, yet despite these improvements it is likely not enough protection is in place for a major catastrophic event.

"People often talk about climate change as being in the future – in the Philippines, climate change is today," says Jan Mumenthaler, principal insurance officer, International Finance Corporation in the Philippines.

"There is an urgent need for businesses and the government to become more resilient, so that communities and businesses can sustain their future. Some areas might become deserted because the risk of living or doing business there becomes too great."

With such extreme exposure, the likelihood of being affected by a major natural event is particularly high and, as such, catastrophe risk lies at the forefront of considerations not only for companies and government but, more importantly, also for the nation's inhabitants, who grow up surrounded by danger from nature. It is perhaps because of this that Filipinos are not risk averse. Indeed, stoicism and resilience appear part of their DNA, together with a generally positive demeanour that often masks the difficult and impoverished lives many continue to endure.

"Manila is among the four global cities most vulnerable to natural disaster," says Dale. "The first strong typhoon of this year hit Manila in July – it brought wind, but not rain. Still, it shut down the city for 24 hours. When you talk about a city shutting down for 24 hours, what consequences will this type of event have in the future?"

It is a question many in Manila fear will be answered soon.

"The risk management plans exist, but whether they can cope with a catastrophe event of such severity [as Haiyan] I doubt it," says Mumenthaler. **MIKE JONES**

THOUGHT LEADERSHIP

JOHN SCOTT
Chief risk officer of Zurich's Global Corporate business

People-related risks – unemployment, political instability, social unrest and income disparity – rank highly among risks threatening global businesses today. In this environment, it is important for businesses to take a multifaceted approach towards employment and human resource practices.

Focusing on employee wellbeing is one way in which companies can address people-related challenges. This can be in areas such as employee benefits, pensions, accident and health insurance and workers' compensation insurance. For example, Zurich recently finalised an innovative deal with a major corporate to provide employee benefits globally, which is already proving to be an enormously successful retention policy. That kind of approach can be very effective in helping companies to keep a mobile workforce loyal.

Mobility is not just about geography; there is also an integral socioeconomic dimension, as described in *Now for the Long Term*, a report by the Oxford Martin Commission for Future Generations. The report predicts that in the next four decades, billions more people will join the global middle class. The vast majority will come from emerging markets, which are projected to double their share of global consumption from one- to two-thirds by 2050. It states: "This emerging middle class could provide a much-needed impetus for balanced global growth by boosting consumption, investing in health, education and renewable energy, and driving higher productivity, sustainable economic development, and more political stability via increased demand for accountability and good governance. While this constitutes a significant opportunity, there is also the risk of an increasing divide between the growing middle class and those left behind."

As societies in Asia become more middle class, people will become more aspirational. As countries become more affluent, they have more people with more money to spend, leading to growth of their domestic economies. This applies to the Philippines, which has been driven by people working overseas and sending money back to the nation. When these people start returning in large numbers, with higher expectations and more money to spend, this will drive the economy forward and result in an uptake in insurance. This presents the insurance industry with a huge opportunity, albeit accompanied by its own sizeable set of risks.

SPECIAL REPORT:

CONSTRUCTION

Megacities = mega risks

Asia's demand for infrastructure is booming – as is the need to manage related risk complexities

THE DEFINING FEATURE OF 21st century Asia is its vast megacities. Images of neon-lit skylines have become a visual metaphor for global growth as the world's most populated region gets wealthier.

Across the region, construction is booming, from housing to power generation infrastructure. However, although construction work is plentiful, so are the related political, macroeconomic, insurance and labour risks. Companies need to be careful, but not overcautious, as they seek to develop their risk management function.

"Risks drive up the tender and insurance pricing... and firms take [risk] seriously," cautions Richard Warburton, area leader, South-East Asia, at built asset consultancy EC Harris.

He adds: "Multinational companies are taking risks more seriously than the others. This is because they have to protect their reputation and ensure their products meet international standards for export purpose. They have the appetite to know more and to do better, but this is not embedded or institutionalised yet."

Soft market

The long and sustained Asian boom presents a challenging market for insurers but good opportunities for risk managers looking to transfer risk. "There are lots of opportunities for insurers, but the pricing is very aggressive," says Mark Bonnar, AIG's regional head of construction and energy casualty.

Daniel Abramson, AIG's global head of construction, agrees: "The market cycle peaked around the middle of the last decade. Pricing has been under pressure ever since and, more recently, we have seen a deterioration in deductibles and, what is of particular interest to underwriters, scope of coverage. Wordings and policies are becoming noticeably broader.

"Insurers are committing capacity and terms on complex infrastructure projects that may run for the next five or six years, sometimes 10 years or more. Underwriters need to utilise a broad variety of risk assessment tools to select for the highest levels of risk quality in a meaningful way. Of course, strong and deep underwriting expertise, industry knowledge, relationships with key partners and clients and competitive advantages within your operation are essential ingredients for long-term success."

The risk manager's view is, of course, the opposite. "[Risk managers] should be busy," says Abramson. "They should take this opportunity to reassess their insurance solutions and work with their brokers to find the best product in this market. I would in their position. It's a buyer's market, and they can transfer risk at attractive prices."

Although insurance brokers wield more power in a soft market, the environment for brokers is not necessarily rosy. "Many risk managers are tendering all their new projects to multiple brokers with the expectation of obtaining the lowest possible price," says Abramson. "But should a contractor or principal who has been using one regular broker for many years necessarily get the best deal by bidding it out to a half-dozen brokers or more, and letting them fight for the cheapest price? I don't believe that tendering everything always gets you the best price; insurers don't always respond well to multiple brokers. Their ability to offer an insurance proposal carefully tailored to the client's requirements may be compromised."

A curious symptom of a seriously overcapitalised market well into the soft phase of the cycle, according to Abramson, is that "clients and brokers are increasingly designing and creating their own insurance product, pricing it and selling it into the insurance carrier market".

"Asia came out of the 2008-09 financial shake-up and we haven't looked back," says Abramson. "The crisis stimulated public spending on new and upgraded infrastructure projects, and private sector investment also rebounded strongly in, for example, the petrochemical and power generation sectors."

"The Japanese are investing in Vietnam and Australia. Chinese and Korean contractors are exporting their capabilities to Africa and the Middle East and, of course, China and Korea are going ahead with their ambitious and forward-thinking plans to increase nuclear power generating capacity."

Labour worries

In some territories, boom times can bring major problems for construction firms – especially when an accident occurs on site.

This is particularly true in Hong Kong and, to a lesser extent, Macau, where significant numbers of large and complex projects involve sophisticated engineering, such as major bridges, underwater tunnels, bridges through mountainous areas and a third runway at Hong Kong airport. "These are classic infrastructure projects in a highly urbanised area that require a high level of expertise from contractors," says Lincoln Pan, executive director, Willis Hong Kong.

"One particular problem is getting enough qualified contractors

'An industry that requires a lot of imports and works on long timescales to realise project profitability, with across-the-board erratic behaviour by government, will always have problems'

Steve Wilford, Control Risk

and employees to work on the sites. As a result, we are importing a lot of labour. Many [of these employees] have not worked in Hong Kong before and may struggle to meet the international standards required in construction here."

In response, the government has tried to slow projects down by refusing to approve any new projects for six to 12 months. "This is the correct answer for the people of Hong Kong, but it has had the effect of slowing down the construction insurance market," says Pan. "The challenge is that, although Hong Kong has a population of 7.1 million, the number of people who are trained in construction is not that high, and we are therefore importing a lot of labour from China."

Warburton says: "The construction boom in Asia requires more local talent who are well versed in local-market knowledge, legislation and culture to join the construction industry.

"As each market in Asia is unique, we need talent that understands each market to ensure the smooth execution of projects. The workforce is ageing as there aren't enough new graduates entering the industry."

But because of where the Hong Kong dollar is in relation to Chinese currency, this [importing of labour] is becoming expensive. "These labourers expect to be paid the same – or more – than Hong Kong workers," says Pan. "The situation with the currencies is also affecting the price of materials, much of which is imported from China and that is further affecting contractors."

When things go wrong

As a result of these conditions, Hong Kong contractors are facing a more challenging environment for the procurement of insurance than in other Asian territories.

"What has balanced this out is that there is ample capacity in Hong Kong for the classic contractor [looking for] all-risk cover," says Pan. "The market is fabulous and there is a general willingness among carriers to take all-risk cover, third-party liability and professional indemnity cover.

"The exception is employee compensation insurance: the statutory payments required to be made to employees insured on site if they are injured. What is posing a problem is that, because of the labour shortage, workers are coming in from all over the world – from Korea, Thailand, China – and they may be doing their first project in Hong Kong."

Warburton says: "The lack of governance, training and self-awareness are among many reasons why the construction workforce in Asia has a higher workplace accident rate compared to mature markets such as the UK. The health and safety issue needs to be higher up the agenda and embedded in planning, delivery and operation phases."

But unlike all-risk and general liability, the market for employee liability cover is tight. Few insurers are willing to write the risk. In addition, one major insurer in this area, RCA, is having financial trouble, thus further tightening capacity.

"We are seeing more ambulance-chasers than four years ago," says Pan. "Around hospitals, clinics, even building sites, you see more and more pamphlets from lawyers offering to pursue claims."

As a result, contractors are looking to partner with brokers to partner in handling troublesome cases against employees. "[Contractors] not only want us to help place and structure their insurance, but be an active partner helping to provide health and safety guidance on site, and even to go so far as organise onsite medical coverage," says Pan. "They are also looking for assistance in dealing with underwriters and insurers and ensuring that claims are processed in a timely way.

"They expect brokers to have the analytical skills to analyse claims, look for patterns and help bring in appropriate health and safety to deal with these trends."

Construction firms are also employing more and more third-party administrators to check that employees are going to the doctor – a panel doctor, not just any doctor – that they take their medicine and they file the correct documents with the government.

"Clients are constantly asking for us to help them reduce their employee liability costs, and you have to be able to provide that – otherwise, you will lose business," says Pan.

"Unless more capacity comes to the market, there will be inflation as the costs of handling these claims – both from a medical point of view and a legal perspective – keep increasing."

Politics, politics, politics

Elsewhere in Asia, the problems for the construction sector are coming from the politicians, particularly in South-East Asia.

"An industry that requires a lot of imports and works on long timescales to realise project profitability, with across-the-board erratic behaviour by government, will always have problems," says Steve Wilford, Asia-Pacific director for Control Risks. "These are the 'traditional' risks for the region and they have not really changed, which is why construction in this region is not for the faint-hearted.

"There is a higher risk of losing your shirt than in some other markets. There are chronic problems: a facet of the strong nexus between business and politics."

Although the demand for construction in the region is strong and all incoming governments make big promises on infrastructure, real risks related to policy outcomes remain.

"In Indonesia, for example, the demand is really strong in the housing market," says Steve Norris, senior South-East Asia analyst at Control Risks. "The companies we speak to are optimistic and have huge backlogs of work; the problems are all on the policy side.

"For example, the central bank put through several measures to dampen down demand because it is worried about public debt and the condition of the state's current account. In addition, Indonesian construction companies have to import about 50% of the materials they use, so when the central bank tries to reduce this, what it is trying to do is dampen the net imports, because it wants to shrink its deficit, which has been severe for the past year.

"For the construction companies, it's a lose-lose situation, because while that deficit exists, not only are they facing policy problems, but the currency is weak as well – so the imports are costing them more.

"The construction sector is taking the bullet for the deficit, which is not its fault and is a result of mismanagement in other areas."

Warburton adds: "The construction boom in Asia also causes higher and sometime unpredictable construction cost inflation. The shortage of building materials in the supply chain owing to the high demand in the industry can potentially cause a rise in cost and delay of the projects. This has proven to be one of the greatest challenges for many companies in control of their project profit margin. It is particularly difficult to mitigate on programmes spanning several years."

Significant issues also arise across the region in respect of securing land for construction, especially in Thailand, the Philippines, Indonesia and Vietnam. Governments are keen to build highways, railways and other projects, but the process of acquiring land is messy and establishing ownership is not straightforward.

"It's often unclear who owns what – sometimes there are two or three legal owners on paper," says Norris.

In Vietnam, the problem is the banking sector, which is having a knock-on effect on construction. "The banks in Vietnam are out of control and construction firms are saddled with huge amounts of debt. Therefore, they cannot get anything going until the banking sector has been sorted out," says Norris.

"The real estate is on hold and a big debate is taking place at the moment about whether to let foreign investors take more of a stake to see if this can [improve the situation] and the construction sector can pick up slightly. However, this idea is not gaining much traction."

Norris adds: "In Thailand, the problem has been the high level of consumer debt – people are reluctant to borrow for housing – as well as the fact that many projects have gone on hold because of political problems. There are problems ahead for Thailand as the government has a repressive agenda, and there will be a backlash, at some point in the future."

But speaking of the region more broadly, political risk is not seen as a major challenge.

"We don't envisage much of a ripple across the region," says Wilford. "We don't see any dollops of infrastructure spend being redirected into crash defence programmes or anything similar." **SR**

THOUGHT LEADERSHIP

Globalised construction leads to globalised risk

Asia is on the move. No one can doubt the region is undergoing a profound historical change as its local economies boom, driving rapid growth in poorer nations and pushing their more-developed neighbours into the top tier of global leaders.

This growth is built – literally – on new infrastructure as industry and consumers demand a new way of living: more power, better roads, bigger homes and new opportunities for leisure.

But the way this vast expansion is happening has changed dramatically in the past 10 years. Construction firms have gone truly global. They are no longer limiting their operations to domestic markets and the region is seeing more and more companies operating internationally – even beyond the regional.

As Europe has increasingly reached out to the Americas in search of growth, so China and Korea are now operating in all corners of Africa and the Middle East. Finance is changing, and increasingly, both private and state backers are providing capital in return for concessions and commodities such as oil – and even food.

The key to success in this developing theatre is taking an international approach to all aspects of operations. Smart firms realise that from finance to labour, it is vital to look beyond their own borders to gain a competitive advantage.

As San Francisco Mayor Ed Lee said recently: "When we became Sister Cities back in the 1980s, Shanghai asked us for help with their sewer system. We sent our public works director. Fast-forward 20 years later and China is helping us with our bridge."

For risk managers, the challenge is immense. While increasing complexity is an essential driver of growth for their employers, the risk landscape they face as a result has become much more tortuous. Projects are getting bigger – much bigger – and they now take place across many more countries, while their supply chains grow ever longer.

More than ever, it is a case of the devil being in the detail. Risk managers need to understand the intricacies of operations, as success or failure will be weighed on the basis of how well they can make genuinely well-informed decisions about domestic and foreign exposures.

With construction in Asia steaming ahead, risk managers will need to ensure they remain fast and nimble enough to keep up.

Robin Johnson, AIG's head of broker and client management, Asia

SPECIAL REPORT:

PEOPLE RISK

THE REAL LIFE COMPANY

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The human conundrum

People risk encompasses many complex factors, requiring risk managers and human resources departments to work together and apply a holistic approach

WITH BUSINESSES KEEN TO create any competitive advantage they can, it pays to understand that the key differentiators in this process are people. Ultimately, a company's profitability depends on the performance of its staff. Yet, although an organisation's strength lies in its people, they are also a source of risk, presenting a range of issues that can fundamentally affect a firm's success.

It is important that people risk is managed in a holistic way – it is not a risk that should be looked at in isolation, nor is it the sole responsibility of human resources (HR) or the risk manager. Importantly, people risk is not concerned only with retention; it overlaps with many other risks. Particularly in Asia, it encompasses the fierce fight for talent, the effect of large demographic shifts, the shortage of skilled workers, and the effect of employee benefits and insurance.

Although operational and business risks topped most corporates' risk lists until relatively recently, says Daniel Tan Kuan Wei, Singapore-based assistant vice-president in MediaCorp's enterprise-wide risk-management office, people risks are "increasingly gaining prominence and coming to the surface in a company's risk radar".

He adds: "Now, people risks are also given similar – if not more – emphasis, alongside operational and business risks."

Kuan Wei, who is also second vice-president of the Risk and Insurance Management Association of Singapore (RIMAS), says there is no one-size-fits-all type of mitigation measure when it comes to people risk.

> *'If you make a bad hire, you will cause critical loss to the business, and if you make a good hire, the challenge is to retain them'*
> **Dennis Lee,** Singaporean educational institution

"Several complex elements – such as size (big v small company), cultures (Asian v Western), resources (deficit v surplus), and so on – come into play," he explains. "So, companies should first study their internal environment closely and build mitigating measures accordingly."

A dual-lens view

As Kuan Wei sees it, businesses can view people risk through two different lenses. "With the first 'people are the best asset' lens, an array of people risks could materialise such as attrition of good-performing staff and workplace safety and health risks," he explains.

"On the other hand, using the second lens of 'people are a vulnerable asset', a different set of people risks might pop up, such as internal sabotage, misappropriation of assets and fraud.

"As such, risk managers need to be aware of such two-dimensional risk possibilities and work alongside their HR counterparts in identifying such people risks in their own business context, formulating risk likelihood and impact metrics and crafting appropriate mitigation plans."

Kuan Wei points out that insider threat is a key people risk to which firms in Asia should pay close attention. "More often than not, most insider threat cases occur during employment where staff are so familiar with the processes or standard operating procedures that they might know how to exploit it to their advantage and inevitably cause substantial harm to a company – such as asset loss, financial loss or reputation damage," he says.

David Ralph, senior vice-president of risk and facilities management at Hong Kong-based company PCCW, adds that major risks are also associated with people moving to competitors.

These involved departing staff "taking with them all the intellectual property they have gained in your employ, including business practices, new products and designs, customer lists, and so on".

Dennis Lee, a risk officer at a Singaporean educational institution, believes one of the greatest challenges is hiring the right people in the first place. "If you make a bad hire, you will definitely cause critical loss to the business, and if you make a good hire, the challenge is to retain them," he says.

"Retention isn't just about providing the right training and paying the right salary – other areas play just an important role and that relate to a safe environment."

Whose job is it anyway?

Lee says there are two parts of people risks in a tertiary education environment: staff and students. "The risks are mainly around hiring the right people – and that doesn't only relate to our staff, it is also important for us to attract good-quality students," he says, adding that managing human capital risk is the responsibility of the HR department.

For Roland Teo, head of the risk management office at a Singapore healthcare group, and member of the RIMAS and the Pan-Asia Risk and Insurance Management Association (PARIMA) boards, it is the responsibility of business units and department heads to be "risk owners".

Teo says: "HR supports and facilitates as domain experts, while risk management helps to look at the

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context so the solutions meets the enterprise's objective," he says.

Kuan Wei believes risk managers must work alongside their HR functions to identify pressing people risks, as well as help with HR to ensure that the plans that are formed "are aligned towards mitigating those pressing people risks".

"The HR and risk management functions of any business should work hand-in-hand to manage people risk," adds Kuan Wei. "The HR function should 'own' people risk, while the risk managers should work alongside as comrades-in-arms to provide value-adding advice and perspectives to help the HR function."

Some examples of this might include setting up a dedicated risk committee to analyse people risks (with representation by the risk management function) and putting a people risk item on the agenda for a risk management steering committee or board meeting to ensure it gets the attention it deserves.

Human capital issues can strike at the heart of risk management itself. Chairman of PARIMA Franck Baron says the region "deserves to have a strong community of risk managers". He adds: "[However], when it comes to skills, experience, know-how and knowledge, much remains to be done to ensure that our workforce in Asia is up to speed."

Vice-president of group business assurance at Telekom Malaysia Mohamad Bin Mohd Zain agrees there is a critical shortage of people who are able to manage new business risk. "As such, talent pinching will be a key risk," he says.

Employee engagement

Staff retention, especially of risk managers with five to 10 years' experience, will be a problem for many companies as other firms start establishing their own risk management units, adds Bin Mohd Zain, who is also the chairman of the Malaysian Association of Risk and Insurance Management. "Rather than building the expertise in-house, buying over staff from other companies will continue because of the limited supply of qualified ERM practitioners."

Shuh Lin Tan, InterContinental Hotels Group's (IHG) head of risk management for Asia-Australasia, says remuneration issues include challenges such wage gaps and minimum wage pressures that increase the costs of running a business.

"In addition, the lack of the right skillsets and competency of workers and draining of skills/brains to other countries, are additional risks," she says. "At IHG, we have nine very distinct brands that represent our promise to our guests, and it is our people who deliver that promise and bring each brand to life. So it is important for us not only to attract the right talent, but to retain it by promises of better remuneration and recognition."

Although remuneration is obviously a big factor in retaining talented people, another pressing issue is how well managers manage their staff. Are they creating career paths and opportunities? Are they delivering useful feedback? Are they providing staff with a sense of purpose?

Organisations that are good at engaging their employees through performance management and clear discussions about career paths and opportunities are on the right track; those that are not tend to see higher turnover ratios.

Employee retention is becoming an increasingly pressing issue for corporates. Employees no longer expect to remain with a company for their entire career; in fact, people often leave organisations by choice after a few years to join competitors or to take on another profession.

Teo says that, apart from competitive remuneration, career progression, training and staff-welfare programmes, companies are limited in what they can do to retain staff. "This is an economic policy and structural issue that industry leaders, representatives of employees and employers and the government have to work on," he says.

Teo points out that in specialised sectors such as healthcare, the demand for highly trained professionals like doctors, nurses and allied health workers is high, while supply is extremely scarce.

"Even after they are on board, you have to ensure they are not unduly stretched, which may result in the compromise of patient safety and care," he adds. "We need to ensure that the entire ecosystem is there to support and have long-term strategies."

Keeping opportunities equal

Lee says tertiary institutions are also challenged by retention issues of staff and students.

"Just as staff can easily move to another institution, students may also do the same," he explains.

"One way to ensure attrition levels are low is by establishing and maintaining a supportive environment, a place that provides good research facilities for staff and students.

"It is equally as important to ensure that their place of work or study is safe. By doing so, not only do we retain students and staff, but we maintain our reputation."

Lee points out that the staff members who make up senior management are generally more senior, with years of experience under their belt, so the challenges are mainly related to the middle and lower tier, who may be more junior and have fewer years of experience.

"But that is not to say they are less valuable," he clarifies. "What we need to do is understand that the younger generation should be supported to move up the ladder.

"Importantly, across many businesses, job roles need to be redesigned and rearranged to create more opportunities for the less experienced."

Companies face an increasing suite of human capital risks as they expand internationally. Among these are language barriers, opposing concepts of management, workplace policy and government influence on business and the economy. So, how should they approach these challenges to ensure their growth is not affected adversely?

Says Lee: "When policies are being set, [companies] really need to reflect the jurisdiction of that particular country,' he says.

"It is the organisation's responsibility to train all members of staff to ensure they take into consideration different cultures and different working methods or ways to correspond [with] and treat each other.

"So, again, the policy, training and education have to be done by those in charge." SR

Put wellbeing first

An emphasis on employee wellbeing as a main benefit will help employers to retain staff and improve overall productivity

EMPLOYEE BENEFITS ARE often presented as one way for companies to differentiate themselves from other employers, thereby assisting with attracting and retaining employees.

The rising cost of healthcare around the world is becoming a growing burden for the private sector, as governments look to transfer some of the cost responsibility to employers.

Employers in Asia need support to manage this risk, says head of JLT Asia Duncan Howorth.

Furthermore, he adds, an increased emphasis on talent recruitment and retention in the region has focused greater attention on employee benefits at the region's major corporates.

"We see the emergence of more flexible benefit arrangements, with the ability for employees to buy benefits that suit their circumstances and lifestyle," Howorth says.

"We also see government activity across the Asia region to create frameworks in which group retirement plans can be developed to support the ageing populations."

Cost implications

AIA chief executive of group corporate solutions Peter Crewe believes that most employers think highly of employee benefits schemes as an incentive for attracting and retaining talent, but they sometimes overestimate the actual cost implications of this coverage. »

THOUGHT LEADERSHIP

Accurate data is key to mitigating people risk

In discussing people risk, it is necessary to define what is actually being talked about, since most risks can be interpreted as having a people element.

It is accepted wisdom that people risks fall in the category of operational risk. The Basel 11 definition of operational risk has been adapted by many firms. The JP Morgan adaptation of this definition is useful in that it defines operational risk as the risk of "loss resulting from inadequate or failed processes or systems, human factors or external events".

I would like to focus on the type of people risk that can be mitigated by the effective and intelligent use of employee benefit programmes. So which risks come into this category? Those that come immediately to mind are what can broadly be termed 'human resource risks' or the risks associated with poor employee retention caused by inadequate, uninteresting or poorly communicated reward programmes. Low staff turnover is key in preventing high recruitment and retraining costs, building company loyalty and strong, long-lived teams. Conversely, a reasonable staff turnover can be essential for bringing in new talent and ideas and allowing enough through-flow to provide ambitious employees with career advancement opportunities.

So how can employee benefits help in achieving both of these goals? Accurate data is key to understanding employee trends, issues and where they may be occurring. The most efficient way to collate, analyse and present data in an understandable form is by utilising an integrated database management system. By this means, data can be collected on the take-up of benefits offered and the utilisation of benefits can be analysed once they are taken up. Feedback can then be collated from employees regarding their level of satisfaction with the range, extent and understanding of the benefits offered.

Such systems offer other benefits to employers in that they actively engage employees and promote ownership and control, which can further be enhanced with the use of social media and mobile messaging.

Richard Roper, JLT Asia's managing director benefit solutions and sales and marketing director

» "Companies looking to offer critical illness coverage while staying within their budget constraints can consider restructuring their employee benefits schemes to provide a different mix of benefits that will enable them to offer critical illness cover while keeping the cost increase related to this new benefit to a minimum," he advises.

Howorth says that although employee benefits schemes do not achieve better retention rates, they are an important component of any compensation structure.

"Giving employees a better understanding of the value of benefits, through mechanisms such as total reward statements (TRS), enables them to understand that benefits are part of the total compensation package, so they're not just focusing on the salary," he says.

TRS benefits

A TRS provides personalised information about the value of an employment package and includes details about remuneration and the benefits provided by an employer. JLT regional benefits director Asia Pete Whittington explains that a TRS "shows your salary, your bonus, your pension contribution and the costs of all your benefits".

Whittington says companies should make full use of the benefits they already offer. "If they communicate this and employees understand it, they are extracting more value from their current spend without paying another dime," he says.

Ultimately, Whittington advises, an organisation must identify and deal with its people risks. "Is it recruitment, retention, absenteeism or presenteeism?" he asks.

"If retention is an issue, do you introduce TRS? Do you structure the benefit in a way that aids recruitment and retention? If absenteeism is an issue, do you bring in absence management? If presenteeism is an issue, do you bring in health and wellness support services to improve the health of the workforce?

"Do you run campaigns around particular hotspots and issues the company may suffer?"

Richard Roper, JLT Asia's managing director, benefit solutions, and sales and marketing director, says absenteeism and presenteeism can be monitored and analysed using an integrated data management system.

"Then preventive measures can be put in place to lower the frequency of claims and help quickly reintegrate longer term sick employees back into the workplace," he says.

"By using the power of an intelligent data management tool, HR-related people risks can be dramatically reduced, with the added bonus of a happy, stable more productive workforce.

"Deploying such a system in Asia, with its multiple languages, currencies and culture does have its challenges, but solutions exist and they are improving."

Although many companies have employee benefit programmes in place to deal with sickness when it happens, there is an increasing realisation that trying to reduce or prevent sickness in is a responsibility employers need to take seriously.

Wellbeing 'fundamental'

Wellbeing programmes are becoming more widely recognised as effective tools to boost productivity and profitability through reducing sickness and absence, as well as driving up employee engagement.

They can also help identify illness trends within a company and contribute towards a corporate social responsibility policy.

Understanding the relationship between employee wellbeing and productivity is fundamental. Having a healthy, engaged and motivated workforce has a direct correlation to productivity and job satisfaction, which in turn helps reduce sickness absence and ultimately improve profitability.

Investment in an appropriately structured wellbeing programme, therefore, can provide a clear and tangible return. SR

Generational issues: another part of Asia's brain drain dilemma

A risk mapping exercise carried out recently by a Hong Kong-based organisation that was concerned about the poaching of its talent revealed that although the company was spending a lot of money educating its people, staff left for competitors once they had been trained.

This is indicative of a lack of 'bench strength' in many companies, which, coupled with high personal costs, low salaries (in comparison to similar roles in Europe and the US) and low notice periods, makes keeping and growing talent tough.

Head of JLT Asia Duncan Howorth frames it succinctly: "Companies that have invested in training and development should review their retention strategies."

Job hopping

However, even the best strategies may not be enough to retain 'Generation Y' employees, according to Chemical Company Malaysia head of ERM Hafsah Ahmad. "Particularly for highly specialised areas, employee retention programmes and investments to recruit and train are challenged by talents' tendencies to job hop, seeking the ideal job," she says.

"Global warming, deforestation and global headlines ensure no shortage of causes that pull these bright, young individuals – unlike their predecessors, who were inclined to build on company loyalty and lifelong career stability."

Eamonn Cunningham, chief risk officer at Westfield Risk Management, also worries about the generational issues of people risk. "The next generation requires a totally different workplace and development path; they aspire to different things," he says. "Companies need to address their reasonable needs here or they will end up with retention challenges."

Head of the enterprise risk management unit at JTC Corporation in Singapore Sandra Ong agrees: "It feels as though this generation has to move every three years, not because they don't like the job or that they have been offered something more, but simply that they won't work more than three years in any one place."

Ong says when it comes to more technical positions, people often do not stay long enough to acquire the level of detail needed. "There is a shortage of engineers [in Singapore] and concern about this has reached government level. The worry is that there have been no takers for some courses, even if a scholarship is offered."

> *'It feels as though this generation has to move every three years'*
> **Sandra Ong**, JTC Corporation

As Schneider Electric Asia Pacific group insurance risk manager Juliette Gelpi puts it, there is no shortage of highly educated people in Singapore, but "their educational qualifications are not always right for the work available".

Managing director of strategic risk solutions at JLT Singapore Philip Ondaatje calls it a "rotating talent pool that you have to keep rebuilding and reinvesting in".

Head of the employment practice group at Clyde & Co Clasis Singapore Julia Yeo said Singapore's recent regulatory requirements are designed to restrict foreign talent import in favour of homegrown talent.

A new challenge facing firms operating in Singapore is the need to change the hiring process to search locally before extending recruitment searches overseas, Yeo points out. "The increased demand for local talent is likely to exacerbate the trend of employees moving from job to job within a few years," she adds.

"Salary inflation [is another challenge] as employees move often to gain a jump in salary, but sometimes without the relevant depth in experience to match the job, [and] succession planning as employees do not stay long enough to learn the ropes."

JLT Malaysia chief executive Michael Leong says he operates in a country on the road to major growth, but facing serious human capital challenges along the way. "Malaysia aims to escape the second-world chasm and join the league of high-income nations by 2020, but the biggest deterrent to this is the lack of skilled human capital," he says.

"Malaysia is one of the countries that is most affected by brain drain – a major problem in terms of delivering quality and specialised work through the utilisation of the appropriate talent, but also in terms of being unable to retain current local talent or attract foreign talent."

Putri Perdana Sari, risk management manager at Aerofood Indonesia, says significant growth in many industries has given firms little time to develop employees. "Acquisition of [skilled] talent not only saves time and money but also minimises disruption to our customers."

Duma Irene Mitalevanie is a risk consultant at Astra International in Indonesia. She believes that as the general standard of living increases in her country, the more people desire "the better things in life – such as larger income, higher position and greater career opportunities". She adds: "Employees will be more likely to move from one company to another company that has better offers."

Not taken seriously

President and chief executive for JLT in the Philippines Graham Edwards says human capital problems facing businesses in the Philippines are only now beginning to be addressed. "Human capital, managing talent and retention issues are not always seen as a risk – and treated with the same focus, say,as brand and reputational risk or catastrophic event exposures – yet they are key issues," says Edwards.

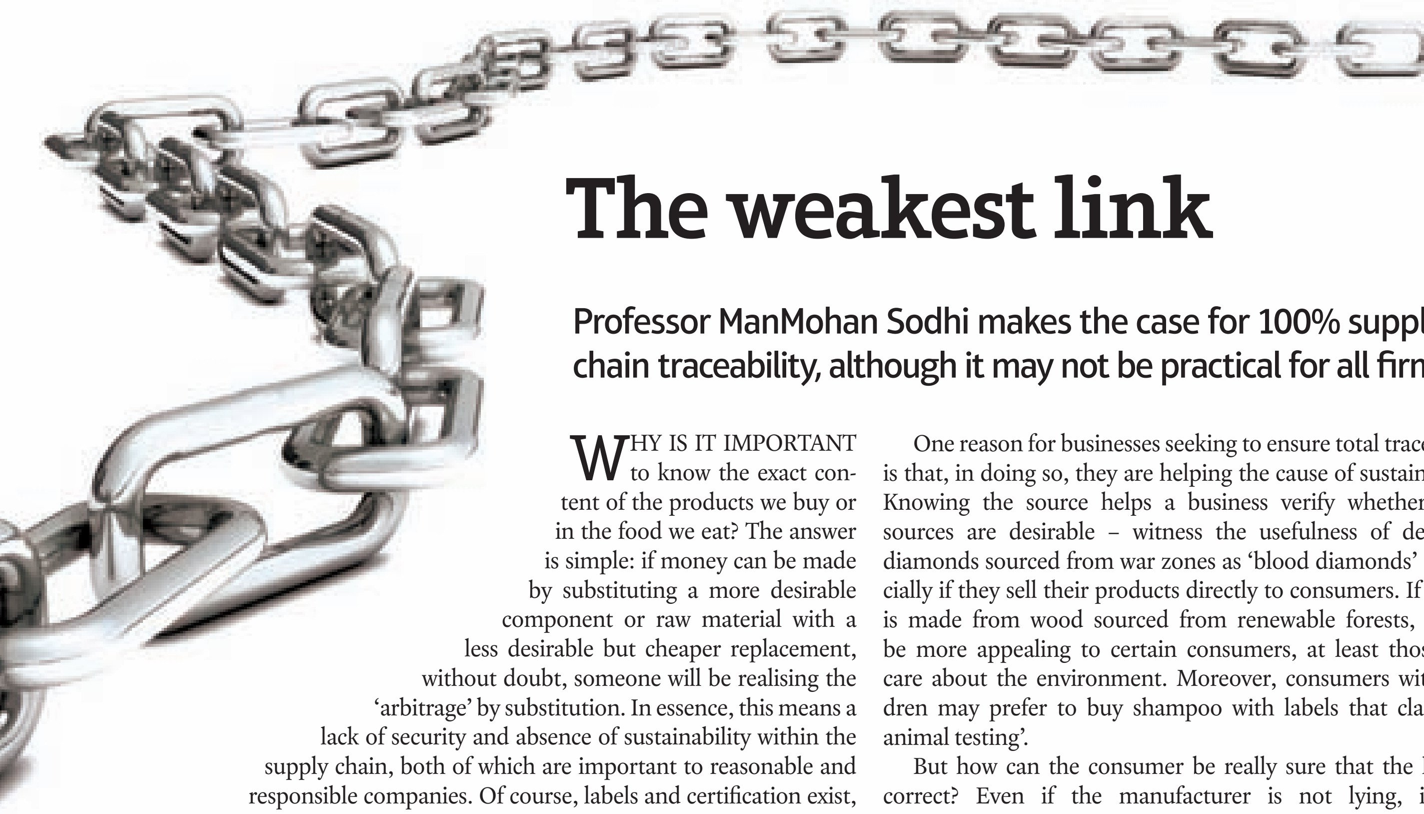
As the Philippines looks to continue growing economically, businesses are increasingly seeking greater expertise for specialist roles, but getting people with appropriate skills is not straightforward.

"A large part of our business is employee benefit consulting, so we often talk to human resources managers, not only risk managers," says Edwards.

"A complaint we hear from most clients in almost every sector is they are struggling to find people with the right qualifications for their businesses.

"We hear this a lot from HR teams, but not so much from risk managers – although when you raise it with them or it is discussed in general, risk managers do recognise that it is becoming an issue for the country." SR

THEORY & PRACTICE



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The weakest link

Professor ManMohan Sodhi makes the case for 100% supply chain traceability, although it may not be practical for all firms

WHY IS IT IMPORTANT to know the exact content of the products we buy or in the food we eat? The answer is simple: if money can be made by substituting a more desirable component or raw material with a less desirable but cheaper replacement, without doubt, someone will be realising the 'arbitrage' by substitution. In essence, this means a lack of security and absence of sustainability within the supply chain, both of which are important to reasonable and responsible companies. Of course, labels and certification exist, as do rules and checking, but while money is to be made from substitution, how can true provenance be guaranteed?

Consider the issue of food supplies in the wake of the horsemeat crisis. Horsemeat cost one-third of the price of beef when the scandal broke and is generally considered a cheaper substitute in markets where it is sold.

After the media revealed the scandal, the real story was not that food labelled as containing beef had horsemeat adulteration. Instead, the real concern is that even today, more than a year later, within the regulation-rich EU, retailers and food manufacturers will not guarantee even from what animal the meat in the food they sell originates. This is the case despite labels – as these are based on the information a company receives from its suppliers, which in turn base the labels on the information provided by their own suppliers. In the end, no one can say with absolute certainty what the end consumer is consuming.

It is likely that someone, somewhere in the supply chain will, at any given point, be tempted to make substitutions. This prospect has increased further because of the tight margins, which supermarkets suppliers consider are ever narrowing. As a result, although genuine traceability for food is desirable it is unlikely to ever happen.

One reason for businesses seeking to ensure total traceability is that, in doing so, they are helping the cause of sustainability. Knowing the source helps a business verify whether those sources are desirable – witness the usefulness of declaring diamonds sourced from war zones as 'blood diamonds' – especially if they sell their products directly to consumers. If a table is made from wood sourced from renewable forests, it may be more appealing to certain consumers, at least those who care about the environment. Moreover, consumers with children may prefer to buy shampoo with labels that claim 'no animal testing'.

But how can the consumer be really sure that the label is correct? Even if the manufacturer is not lying, it may only be basing its statement on what its cheapest supplier says the product is.

Traceability is also important in respect of security. Nobody would want to buy pet food that kills their pet – but that happened to a number of owners in California. Similarly, no one would want to feed their child contaminated baby milk, as occurred in China. Producers cannot have complete security and they cannot guarantee their products for consumers unless the raw materials they buy are completely traceable.

Finally, the question of economic sanctions should be considered. Countries are under pressure not to buy oil from Iran, and even though oil is oil, the sanctions helped bring Iran to the negotiating table. For those taking a side on the issue of Israeli occupation, it is important to know if the Israeli products they are buying are made in occupied Palestinian territories – recall the storm the actress Scarlett Johansson raised by quitting Oxfam in support of one such manufacturer. Those wishing to economically support vulnerable populations such as Afghan women by buying products they produce will need to have assurance about who has actually made the products in question.

Further, anything less than 100% traceability is equivalent to being less than 100% faithful to your spouse: you can easily hide indiscretions. So 100% traceability is highly desirable, if not easily achievable. Therefore, when a large and respected manufacturer announces committing itself to ensuring 100% traceability of a key commodity or raw material, other companies take notice.

Some of those businesses, however, will wonder about the additional cost of traceability and where this will be incurred. Who will pay the price? If traceability requires investment or if it requires the company to pay more for supplies, would the money not be better used to create shareholder value?

Anything less than 100% traceability is equivalent to being less than 100% faithful to your spouse

A little reflection will show three reasons exist as why this may make sense for a manufacturer. Consider this from the viewpoint of, say, a large fast-moving-consumer-goods (FMCG) European manufacturer:

1. For selling in assumedly environmentally conscious Western Europe, a small increase in costs can be easily offset by a large (perceived) increase in revenues. Thus, the benefit may be large continuing revenues, incurring only small one-off costs by way of traceability.

2. Who pays for the cost of traceability: is it the buyer or the supplier? The cost of adoption of radio frequency identification devices by retailers was borne by the suppliers. A large FMCG manufacturer may be able to assert itself with suppliers.

3. Finally, the market may or may not have the capacity to provide traceability or sustainable products. This may affect the supplier's ability to negotiate. If prices are weakening and you are a supplier to this manufacturer that wants traceability, would you not provide it and at your own cost?

As things stand today, it may not be practical for all companies to seek 100% traceability for everything they purchase, but it is certainly desirable. Moreover, it is the absolute minimum if the company wants to commit itself to supply chain security or sustainability. Some companies have already shown that it makes sense to opt for traceability and sustainability where there is economic value – and that benefits not only shareholders and but also society. Perhaps, this will extend even to food and, some day in the distant future, we might even find out what we are eating.

ManMohan S Sodhi, professor in operations and supply chain management, Cass Business School

Obstacles exist around confidentiality and need to be addressed

It is hard for organisations to achieve 100% supply chain traceability. So the question becomes: are there ways to ensure 100% traceability – or traceability close to 100% – in the areas that really matter. This can be vital to ensure appropriate product quality, to comply with regulatory requirements or to ensure required ethical / environmental standards.

The US has implemented regulation around minerals mined from specific conflict-affected and high-risk areas in Africa. The Dodd–Frank Act requires SEC-listed public companies that use particular materials – including gold, tin, tantalum and tungsten – to disclose the use of and source of such materials.

Many of these materials end up as electrical components for electronic devices. Given the lack of transparency in the supply chain, particularly around such minerals, businesses and consumers cannot know whether their purchases might ultimately be financing armed groups.

The Act, which required reporting by 2 June, aims to discourage businesses from engaging in trade supporting regional conflicts. Here, it is vital that companies know where their materials are being sourced from, to comply with the law and to protect their reputation.

Let's take the food industry as another example. It is obvious that food and drink suppliers need to keep tight grip on their supply chain and know where their ingredients come from as contamination or similar faults in the product could have devastating effects on consumer health.

Product quality is equally important for other businesses, particularly those involved with aerospace, nuclear and process industries.

For these industries, managing the supply chain is difficult as the supply chains grow longer and become ever more complex.

However, as the internet develops, with increasing digitisation and connectivity, it becomes increasingly possible for organisations to map more comprehensively their supply chains. Obstacles exist not least concerns around confidentiality and these need to be addressed to realise the benefits of increased traceability.

We're not there yet and few businesses can claim 100% supply chain traceability. However risk managers now have a strong focus on supply chain risk management, with many agreeing the most effective way of managing the supply chain is to be clear about where component or ingredients come from. This will help businesses address product quality and availability which for many companies is at the heart of their business and their reputation.

Chris Mcgloin, chairman of the UK-based Association of Insurance and Risk Managers in Industry and Commerce (Airmic). For more information on Airmic's new global compliance database, go to: http://bit.ly/1tkCDQN

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CLASS NOTES

Rethinking enterprise risk management

In the first of a new educational series looking at practical ideas on how to approach and manage a variety of risks, Andrew Koh outlines why using an ERM approach is crucial for business success

LET'S BE REALISTIC: TODAY'S BUSINESS LANDSCAPE IS constantly evolving and fiercely competitive, driven by game changers, value creators and innovators all trying to match changing consumers' demographics and expectations. Enterprise risk management (ERM) involves preventing potential key risks from happening in such a complex environment.

COSO or ISO 31000 standards relate to managing risks within an organisation in a holistic (breadth) and comprehensive (depth) manner. Yet, many companies find it difficult to quantify all the key risks they are exposed to, leaving them vulnerable to uncertain losses. The real challenges lie within the abilities of firms to effectively quantify losses from potential risks, because they are often intangible, such as lost sales and service disruptions.

Reputational damage is another intangible, as was exemplified by the public relations disaster US retailer Target suffered after the breach of its point-of-sale systems. Another example is when General Motors came under public criticism and intense scrutiny from regulators over its delays in recalling certain car models with safety issues. This raises the issues of questionable internal practices and governance.

Compounding these problems, corporations have to operate within highly competitive business environments. Often, the bigger risks, which are less tangible, quantifiable and frequent, are more challenging compared to the smaller ones, which are more tangible and measurable and occur more frequently.

Where to start with reputation risk

The complexity of managing reputational risk across all corporations and financial institutions can be baffling: direct versus indirect client dissatisfaction, complaints about product or service quality, negative public opinion, cyber attacks, data breaches etc. The stakes are high. So, what is a good starting point and what steps should be taken?

Working with the right stakeholders, using the correct tools to identify and quantify the types of risks involved can harness this complexity and can even prevent reputational risk from reaching its potential. At the same time, companies need to determine how likely a particular risk is to occur and its potential effect on costs, brand, reputation and risk appetite. Companies know exactly what their returns on equity or returns on investments are, but they cannot predict the probability of a major risk occurring tomorrow or its potential consequences.

ERM should prevent a firm's potential reputational risks from being realised. One needs to know whether the quantification and aggregation of risks within a company is likely to make it safer or more vulnerable, hence making some of these unknowns harder to quantify, let alone insure. This is why selecting the right ERM tools is vital to focus a firm on quantifying and aggregating its risks.

One approach to managing reputational risk is to produce triggers to monitor performance metrics by designing key risk indicators (KRIs) with risk owners. These monitor the underlying reputational risk profile changes by linking each risk's potential impact onto the reputation risk that the firm is facing. They can measure the number of customer complaints received, clients' opinions expressed via social media, data losses following cyber attacks from hackers, and even a decline in a company's share prices. In essence, KRIs serve as early predictors of risk transformations.

Once the linkages of specific risks to reputational risk have been established, risk weights can be assigned across each risk's potential effects based on a firm's risk appetite. So, should one or more risks be triggered by their corresponding KRIs and the potential impacts on the firm's risk appetite be sufficiently severe, this will warrant the attention of senior management and the board. Discussion on actionable items to prevent the building up of actual reputational risk from affecting the firm will then be firmly on the agenda.

Andrew Koh is vice-president of enterprise risk management for Network for Electronic Transfers Singapore