CNA / HARDY

Taking the pulse of global business

Global Risk and Confidence Survey

May '19

Contents

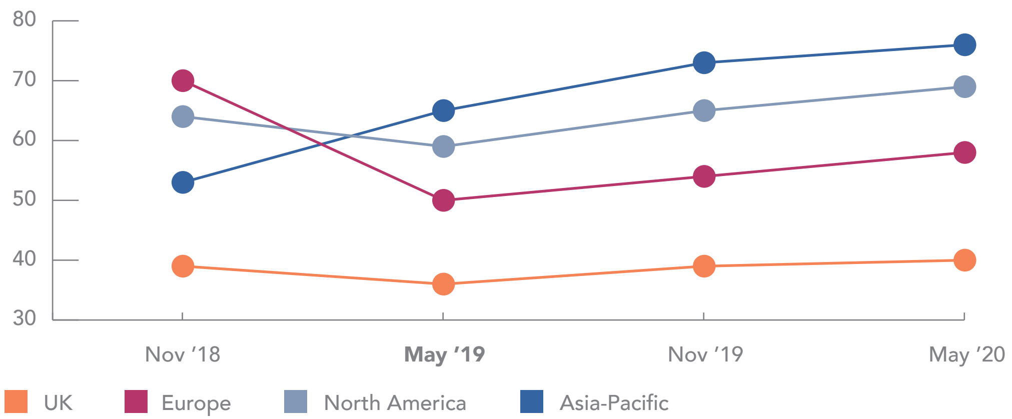
Confidence weakens as reputation risk stalks the new economy

In an increasingly complex, technology-led, interconnected global economy, business leaders are being tested like never before. The result? Confidence has dipped, investment in business fundamentals is down across the board and reputation risk is the new threat that stalks the corridors of power.

Business confidence is a fickle thing. In the past, we have seen confidence remain robust even when the overall risk environment is deteriorating; or weaken even as risk perceptions dissipate. But right now, in May '19, the picture could not be clearer. Confidence is on the slide in three out of the four regions we survey, even while risk perceptions hold broadly steady.

As we look ahead, business leaders in Asia-Pacific become bolder and we see a big uptick in confidence in North America. Europe and the UK meanwhile remain mired in the political and economic uncertainty that is Brexit.

All change in global business confidence

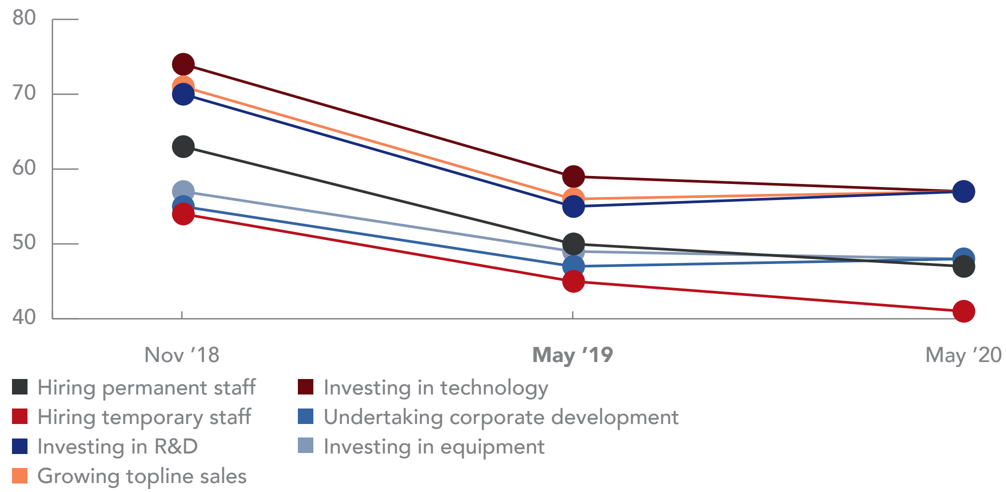


Percentage of companies confident in their ability to grow and prosper

Businesses reining back

For the first time in the history of our research, we are also seeing investment in business fundamentals falling sharply away across every region, including Asia-Pacific. We believe this suggests that confidence has become so febrile, businesses have decided to adopt a 'wait and see' approach before committing capital. The global party, fuelled in part by Chinese growth and expansion has been brought to an end by a combination of rising protectionism, Chinese economic rebalancing and the fallout of Brexit indecision – all of which is causing businesses around the world to put long-term bets on hold.

Investment goes on hold



Percentage of firms globally planning to proceed with investment in business fundamentals

Regional perspectives

North America in May '19 is at a pinch point of rising risk perception and declining confidence. The mood is very much cautious and 'wait and see' as the run up to elections in both Canada and the US introduces risk into any sector subject to the impact of changing public policy. As a trading nation, Canada is particularly exposed to instability in relationships with neighbours near and far. The US is more resilient and its economy performing better, so the risks here are more overtly political than economic.

Executives in Asia-Pacific by contrast have a much less nuanced approach to business in May '19 and have soared to the top of the global confidence pecking order. Asia-Pacific is home to some of the strongest performing economies in the world and is a leader in terms of natural resource wealth, agriculture, mined elements, rare earths and not least, people. Asia-Pacific regionally is also a significant consumer of global output and well placed to leverage its strengths in trading relationships with the rest of the world. As executives double down on growth opportunities within the region, executives in the West will need to position carefully to benefit from China's investment in infrastructure and technology. If Western governments are divided over the appropriate response to Huawei expansion and to Belt & Road opportunities, the challenges will be even more heightened at a company level.

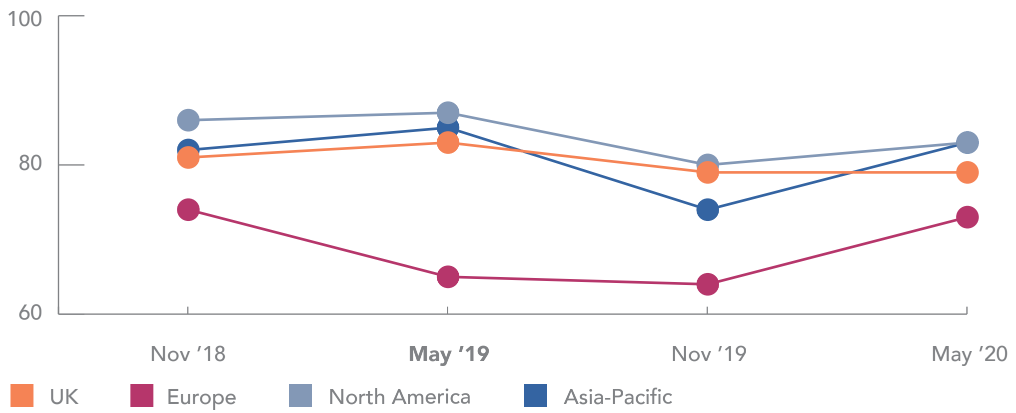
European executives by contrast have sunk back from hero in November '18 almost to zero in May '19, hamstrung by a combination of factors - low growth, poor productivity, high unemployment, civil unrest due to immigration (Germany), tax inequality (France) and Brexit delays. Only the UK remains consistent: while Brexit remains an un-done deal, uncertainty rules, confidence is low and few business leaders are inclined to put capital at risk.

Global risk consensus is striking

Underpinning changes in business confidence is companies' constant reassessment of the shifting risk environment.

In today's interconnected world, no company is really insulated from what's going on in other parts of the world politically, economically or technologically. Even though individual risk rankings vary by country and region, there appears to be a strong consensus among global business leaders on the direction of travel in terms of risk overall. So, while business confidence varies at the local and sector level, the view on risk is global.

The reality of global interconnected risk



Percentage of firms operating in a moderate to high risk environment

Global interconnectivity drives complexity

The alignment of risk perceptions over time across the regions we survey demonstrates very clearly the reality of interconnected risk. From connected devices and international supply chains, to the global financial system, the potential for small problems to trigger unexpected cascading failures, is now all around us.

[5] https://bit.ly/2x616lc [6] https://bit.ly/2yT114p

We are all familiar with the paradigm-shifting Fukushima tsunami that hit Japan's east coast in 2011. It not only caused a desperate humanitarian disaster but halted production of BMWs in Munich, triggered falls in US Treasury bills, and created shortages of iPads in Australia. Risk managers and their insurers were taken by surprise – the marine market had not anticipated a risk aggregation of this order. Risk managers likewise had under-estimated the impact of a single supply chain pinch point and the ripple of interconnected losses it could set in motion.

For anyone who might have hoped that this risk cluster was a distant one-off from which we have learned the lessons, consider the recent US wildfires that are becoming both more frequent and more significant.

When Pacific Gas & Electric filed for bankruptcy protection in January this year, its immediate concerns were around multi-billion-dollar property and business interruption liabilities to its customers. But its decision to use the bankruptcy to reject US$30bn of its high cost, long-term power purchase agreements with renewables companies also set in motion existential risks for West Coast wind and solar businesses. So, at a stroke, a fire threatened to take down a major US utility, disrupted other local businesses and weakened the US renewables industry and its international investors.

Technology-enabled new business models drive new risk exposures

But interconnected risk is not just fuelled by globalisation. New business models made possible by the advent of the 4th industrial revolution have changed the way value is created and in so doing shifted the risk paradigm once again.

Whereas the world's leading exchanges used to be dominated by companies that mined materials or manufactured product, today the highest valued businesses are technology-based – the so-called FANGs (Facebook, Apple, Netflix, Google). While some have valuations based on solid revenue flows and a track record of profitability; others are valued almost entirely on brand and reputation strength and their potential to generate revenue.

The size of these companies and nature of these businesses means the insurance industry has two problems to grapple with:

- The rise of intangible risk in the form of brand and reputation;
- Interconnected technology risk – a problem with a product or service from a global technology company would have widespread implications for other industries that make up the global economy.

According to Airmic CEO John Ludlow: "Intangible assets have grown in value from 20-80% and reputation accounts for circa 50% of value." Intangible risks are, by their very nature, harder to identify, model and mitigate.

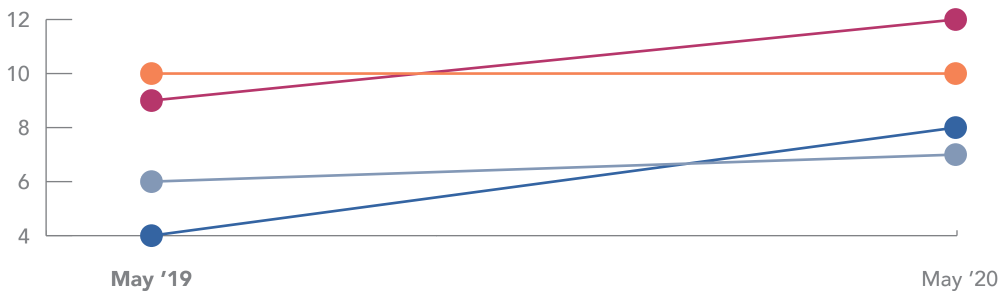
Reputation risk stalks new economy

The inevitable consequence of management struggles to manage intangible, interconnected risks in this new world economy is reputation damage.

In the past we have talked about the concept of 'Boardroom risk' – the trio of corporate, compliance and supply chain risks that fail to hold the attention of the C-suite and thus form a significant blind-spot driving management liability. Our exhortations to 'mind the gap' have resulted in fruitful discussions with brokers and insureds, although the individual risks themselves have remained in the bottom half of the risk radar. What these conversations did suggest, however, was that boards were becoming much more attuned to the concept of reputation risk arising from these and a variety of other drivers.

In this report we took soundings on reputation risk as a new risk category and as business leaders look ahead to May '20, we see that reputation risk is growing faster than any other – up 29% globally, a third (33%) in Europe and doubling in Asia-Pacific between May '19 and May '20.

Reputation is the fastest rising global risk



Percentage of business leaders concerned about reputation risk now and in 12 months' time

Most significant challenges in managing reputation risk

Business leaders' views on the key challenges in managing reputation risk split by region

Reputation risk does not exist in a vacuum, it arises as a consequence of a misstep somewhere in the business – potentially a product failure, service shortfall, technology fault or an error of judgement by management – leading to a governance failure. By its very nature, reputation is a risk that is deeply interconnected with the operation of the business itself.

But reputation risk is also growing in significance because of the increasingly interconnected global trading environment.

All the businesses in our Risk and Confidence survey are multinational – indeed every business with a web presence is a global business, at least in name. So, a slip-up in one territory has the potential to affect business in another. Even if operations can be ring-fenced, news of problems will spread and sometimes the impact of that is worse than the original incident.

Managing logistics and maintaining brand value are core priorities

Businesses we spoke to were divided regarding the most significant challenges they face when dealing with brand or reputation risk. Managing the logistical challenges – securing board buy-in and implementing a timely plan of action – were two of the highest ranked priorities. But maintaining brand value was narrowly the top concern globally, with sentiment particularly marked in Asia-Pacific and North America.

Fake news means good communication is at a premium

Maintaining brand value is a 24x7 responsibility, particularly in a world where much communication is via social media channels. LinkedIn in particular, but also Twitter, are considered mainstream communication platforms by most businesses. They work well for keeping brands 'front of mind', but that same accessibility can have a downside during difficult times. It can be hard for businesses to understand exactly who they are talking to; where commentary is originating from and of course to correct misconceptions once they have been widely shared. The phenomenon of 'fake news' has been widely discussed in terms of politics, but businesses can also be undermined by the same strategies.

[1] https://www.weforum.org/reports/the-global-risks-report-2019

In its Global Risks Report 2019[1], the World Economic Forum notes: "Among the most widespread and disruptive impacts of AI in recent years has been its role in the rise of 'media echo chambers and fake news' a risk that 69% of GRPS (Global Risk Perception Survey) respondents expect to increase in 2019." It cites research into 126,000 tweets and found those containing fake news out-performed those containing true information – reaching on average 1,500 people six times more quickly.

Insurers need to move to a new model: prevention and cure

In the past, insurers were called on to protect tangible assets: homes, buildings, employee liability and belongings. While that's still very much the case, globalisation and the rise of the tech-enabled information economy mean insurance is also being called upon to protect more intangible things like cyber and data risk, trading relationships, supply chains, digital assets, intellectual property and reputation.

As tangible and intangible risks proliferate, insurers, brokers and risk managers will need to work ever-more closely together to build appropriate resilience into business systems, processes and assets if we are to navigate the new tangled web of interconnected risk that increasing reliance on global trade and technology brings.

What do we predict?

Reputation cover will become mainstream as boardroom risk is re-evaluated

When the value of leading businesses is measured by brand strength and investor sentiment rather than dollars in the bank; and when intangible assets outweigh tangibles by a ratio of four to one, it is alarming that only 16% of some intangible assets (like brand and intellectual property) have insurance coverage, whereas traditional tangible assets like property, plant and equipment have 60% insurance coverage. This, despite the fact that intangible assets incurred an average potential loss of US$1.08bn and tangible assets US$795m[2].

Already we are finding significant appetite among our broker network and insureds, for deeper discussion and insight around the drivers of boardroom risk and strategies for risk prevention and mitigation. In the same way the market has found a way to model the cost of non-physical damage business interruption claims as part of terror and political violence cover, we believe there will be appetite to model and mitigate the cost of managing reputation risk and the damage to brand value caused by specific triggers.

Interconnected risk will test management capability and organisational structures

Boards and the departments that serve them are often siloed and fragmented, resulting in risk management plans unaligned to the business' purpose. In this new risk landscape, insurance managers, business continuity managers, security managers, health and safety managers, the risk financing team and the C-Suite need to work as an active community, to create a joined-up view of the business, a cohesive 360 degree risk management strategy and an agile, rapid response to risk mitigation and control.

Global solutions will become increasingly sought after

Business today is becoming increasingly global, whatever the size of the enterprise. This means the insurance community will need to become more attuned to the challenges that raises in terms of politics, economics, supply chain, regulatory compliance and cyber threats that flow seamlessly through and across continents. This will mean much closer evaluation of the quality and efficacy of local partner networks, investment in higher quality partnerships and rapid adoption of technology-enabled solutions, including blockchain and smart contracts, which will provide enhanced visibility, security and service, potentially including automated claims payment.

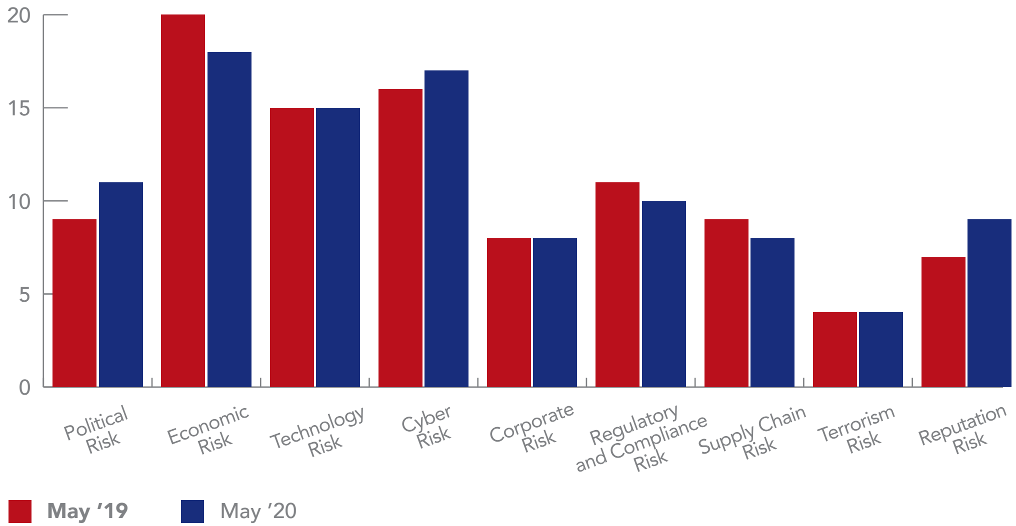
Dave Brosnan
CEO, CNA Hardy

[2] 2019 Intangible Assets Financial Statement Impact Comparison Report; a global study by AON and the Ponemon Institute; https://bit.ly/2VPsiCx

Global Risk and Confidence Highlights

Risk

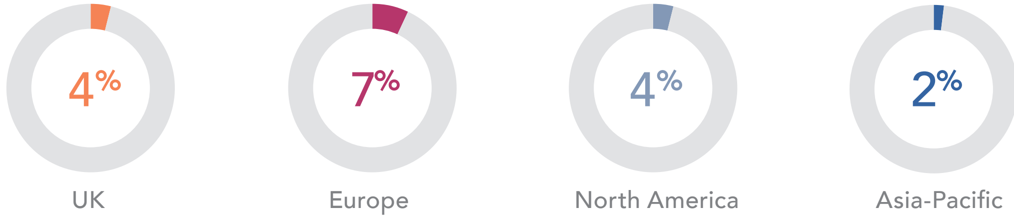
Economic, cyber and tech risk dominate



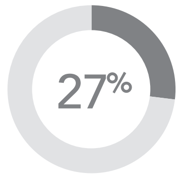
Top risk concerns now and in 12 months' time

Mind the gap

Europe is most concerned by terror risk in May '19



Corporate risk predictions prove accurate

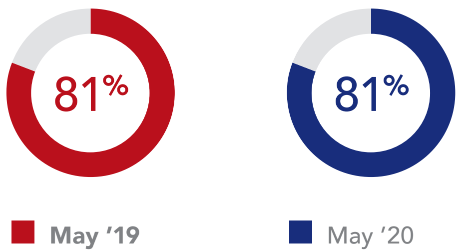


Percentage of firms predicting corporate risk would increase in importance between Nov '18 to May '19

Percentage of firms who think corporate risk is a major risk concern in May '19

Boardroom risk still failing to register in May '19

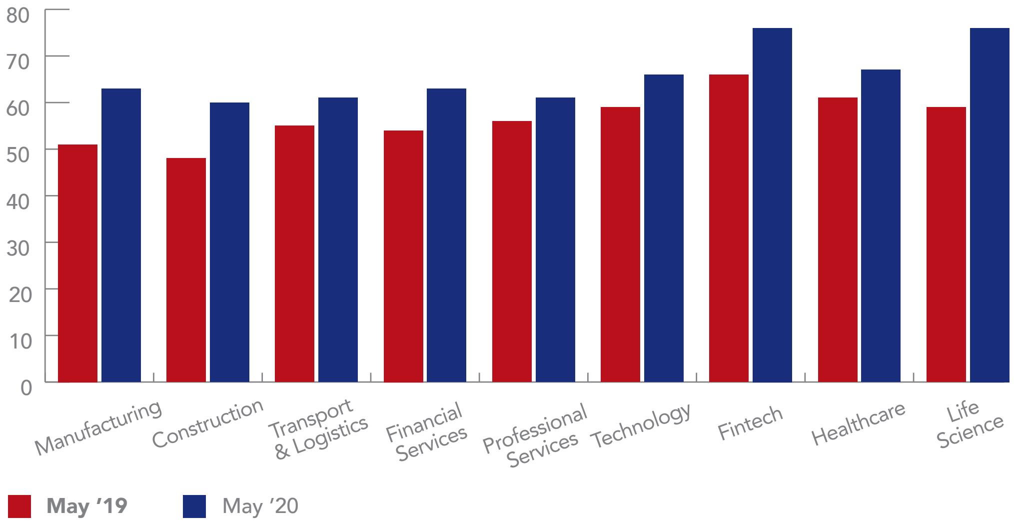
Risk environment remains challenging



Percentage of executives who believe they operate in a moderate to high risk environment

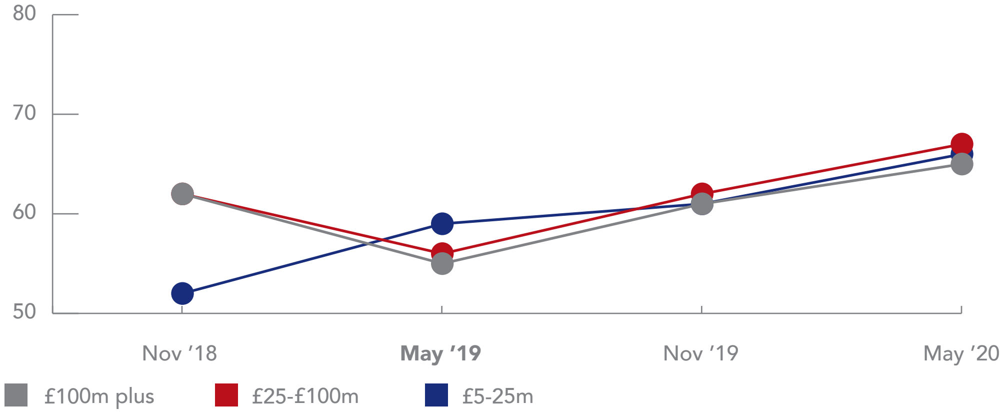
Confidence

Sector confidence is up as leaders look to May '20



Percentage of sector business leaders that believe in their business' ability to grow and prosper

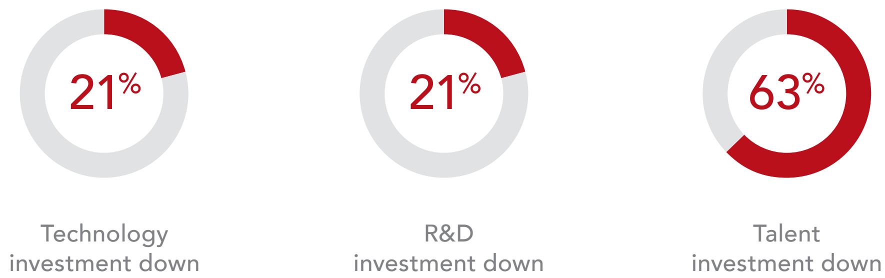
Smaller businesses grow in confidence, but mid-size firms lead in May '20



Percentage of firms feeling confident in their ability to grow and prosper by size of business

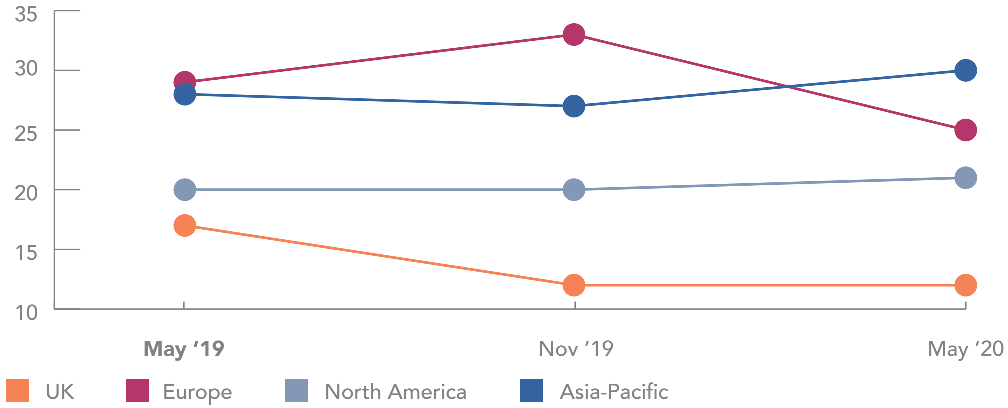
Investment and growth plans

Investment in business fundamentals falls away



Percentage decline in investment in business fundamentals Nov '18 to May '19

Multinationals looking to Asia for growth in May '20



Confidence in Europe as a growth market is in sharp decline, but holding steady in the UK

Brexit batters confidence in UK and Europe

Ongoing discussions regarding how the UK is to exit Europe are having a markedly negative impact on business confidence on both sides of the Channel.

In the UK, confidence has been in free-fall since May '17 when 71% of business leaders were confident in the ability of their business to grow and prosper. In our latest research, only just over a third (36%) are confident and that proportion continues to fall as business leaders look ahead to November '19. This means the UK remains bottom in terms of business confidence across all the regions we survey.

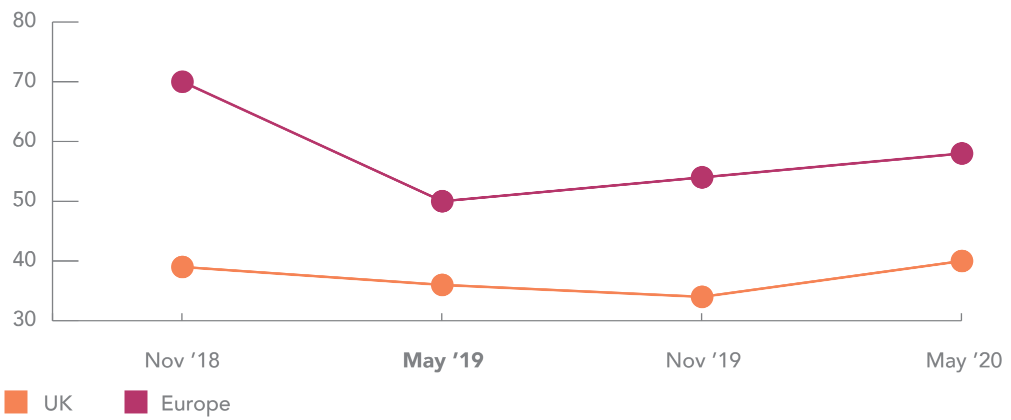
In Europe the picture is only slightly better. Here, half (50%) of businesses are confident in May '19. The mood improves, but only marginally, as leaders look ahead to November '19 and beyond. This means that Europe, which led the world in terms of confidence six months ago, is now the least confident region globally after the UK.

UK risk temperature rises as Europe holds its nerve

High levels of pessimism regarding the UK economy are clearly reflected in rising risk perceptions. Some 83% of UK business leaders see high levels of risk persisting through May '19, though they are hopeful of better times ahead once political uncertainty regarding Brexit has abated.

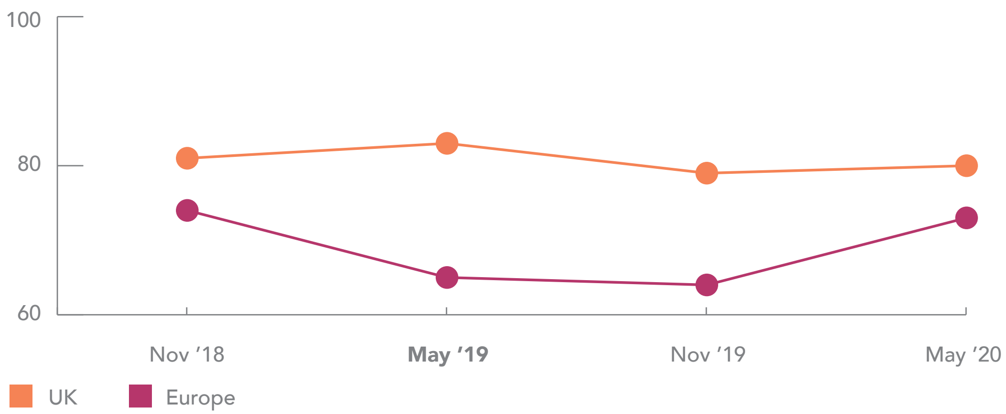
In Europe by contrast, nerves are steadier and risk perceptions have fallen 11 percentage points since November '18 as Brexit remains delayed, with just under two thirds of companies (65%) believing they operate in a moderate to high risk environment. However, the majority (73%) of business leaders anticipate they will be back into more testing times by May '20, when it is likely the impact of actual Brexit may be making its mark.

UK and Europe feeling the blues



Percentage of companies feeling confident in their ability to grow and prosper

Europe more sanguine on risk



Percentage of companies believing they operate in a moderate to high risk environment

Political risk spikes in the UK

Against this backdrop, political risk is given much more weight in the UK than elsewhere in the world. The UK places it second in the risk league table, after economic risk to which it clearly relates. This means the UK is completely out of step with Europe, and indeed every other region, in terms of political risk rankings. With many establishment figures openly questioning whether the UK is on the brink of a constitutional crisis, this result is unsurprising, if somewhat concerning.

The World Economic Forum's Regional Risks for Doing Business report notes: "Although Brexit represents a particularly momentous challenge, the UK is far from alone in experiencing political disruption. Numerous countries across the region now find themselves having to adapt long-standing patterns of government and governance to a new electoral environment characterised by increasing political fragmentation, polarisation and populism."[1]. Indeed, from the anti-tax, socialist, Gilets jaunes in France, to the populist far right Alternative fur Deutschland in Germany (AfD), the evidence of change is all around us.

As we look ahead to May '20, companies in the UK expect that political and economic risks will increase and remain firmly at the top of the risk table. In Europe by contrast, although concerns remain regarding economic and political risk, we also see cyber, regulatory and reputation risk starting to draw focus.

Percentage of UK executives ranking political risk top

Percentage of European executives ranking political risk top

May '19

Regulatory and compliance risk rises as uncertainty reigns

Setting aside the political and economic backdrop, the most significant risks across the Europe region as a whole are cyber, technology and regulatory and compliance risk. We talk elsewhere in this report about the 4th industrial revolution, powered by technology, imperiled by cyber, underpinning new business models and spawning a web of interconnected risk.

But the rise of regulatory and compliance risk in Europe is interesting.

In large part, we believe this can be explained by the changing status of the UK-Europe relationship. While it remains unclear what the nature of the UK's leaving arrangements will be, there has been woefully little progress on reviewing the laws and regulations that will govern trading relationships, export/import requirements or the standards to which multiple industries, products and services must adhere post Brexit. Business leaders are concerned that changes will not be well-signalled and may have to be implemented in haste, creating a significant and complex regulatory compliance burden.

While every industry will be subject to change, it is the distribution and logistics sector which will bear the brunt of Brexit in the early days.

The government has been generous and pragmatic regarding easements in a no-deal situation. But many companies have no expertise in moving goods through Customs. They don't have the people to interpret the information or know how it will impact their business.

Government in turn lacks trained staff at the right level – its no deal plans and training have been too little too late and the wrong people are doing it. So significant regulatory uncertainty remains. The EU is playing hardball. It is a big reputation risk for companies and for the UK.

Mervyn Griffiths, Director, Strategic Shipping

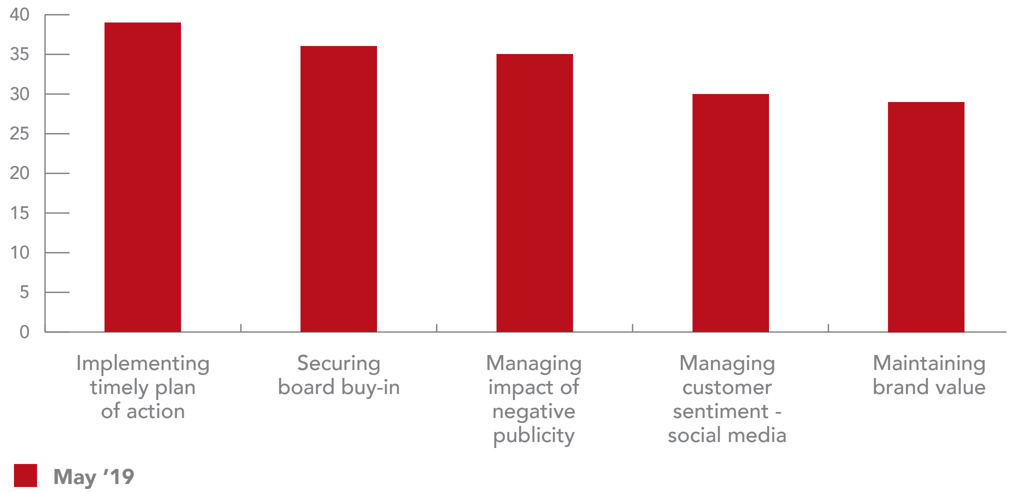
[1] http://www3.weforum.org/docs/WEF_Regional_Risks_Doing_Business_report_2018.pdf

Reputations under threat as interconnected risk proliferates

It is inevitable that the combination of political and economic volatility with regulatory uncertainty will drive reputation risk. Business leaders are at a point where forecasting is problematic, investment in business fundamentals is going on hold and the risk of strategic missteps is rising. Interconnected risk is a feature of modern business life and here we see it played out through the lens of a shifting UK-Europe relationship.

When we talked to UK and European businesses about their concerns regarding brand and reputation risk, it was interesting that they saw internal, logistical issues like securing board buy-in and implementing a timely plan of action – as more challenging than external factors such as managing customer sentiment on social media. The fact that the internal agenda is more challenging than the market agenda is testament to the degree of Brexit distraction among UK and European executives.

UK and European leaders struggle to manage reputation risk



Top challenges facing UK and European boards when managing reputational risk

Despite the many drivers of reputation risk, it is interesting that it ranks only sixth in the UK risk ranking and seventh in Europe. It may be that business leaders are yet to fully examine the linkages between political and economic risk, rising regulatory exposures, and reputation risk.

As a risk engineer now – the job is dramatically changing. Exposures are changing. Contagion is out there and clients have to think through every eventuality of loss. It's like a chess game - we have to work through the subsidiary impact of all the possible moves.
Craig Bennett, Head of Casualty, CNA Hardy,

Risks need to be managed at the strategic, tactical, operational and compliance levels. You have to split it out – it's hard to look at risk from every level simultaneously – you'd have to be a gymnast to do that. But if businesses can knock down the silos and build diverse groups including risk managers, IT, assurance, HR, marketing, lawyers and operators you can learn about risk together. You can combine scenario and crisis planning, invest in the process, make it fun and you get the benefit back in spades. It's timeframes that are the challenge – strategy might look at risk ten years out. Operational people are concerned with today.
John Ludlow, CEO, Airmic

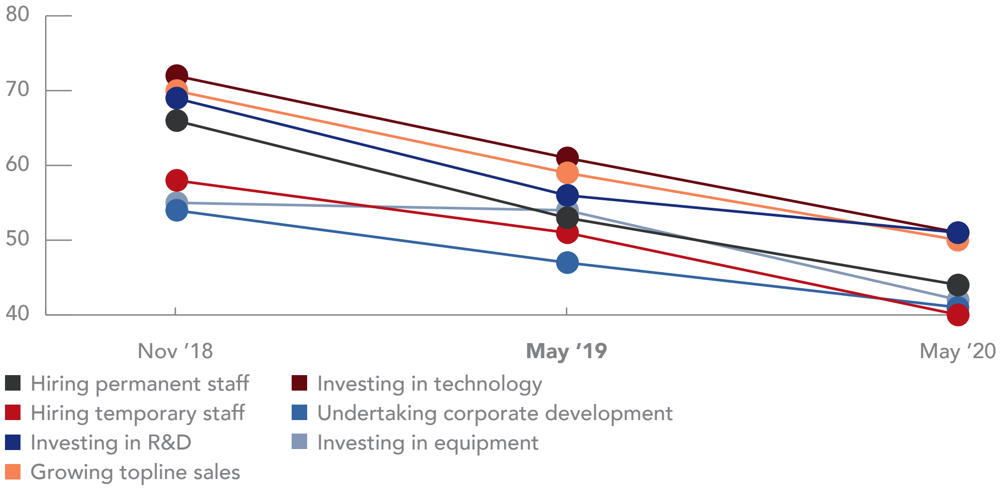
Stagnation building

Uncertainty is a key driver of high levels of caution about investment in business fundamentals. The inevitable, but extremely damaging consequence of plummeting confidence and high levels of risk is that fewer companies maintain investment in business fundamentals – not just on the more significant long-term bets around plant and equipment or corporate development; but also in the technology, R&D and talent which can rapidly drive the business forward and help support the top line.

Whatever lens we choose to examine the numbers – UK, Europe or the two combined – the trend is inexorably negative, with a far smaller proportion of businesses actively proceeding with business fundamentals – for example investment in technology or R&D to drive topline growth. We believe this reflects a significant shift in terms of business planning: companies are simply not prepared to put capital at risk in an environment where unpredictability reigns.

For businesses to be successful they need to have clear achievable strategies that go beyond a short-term timeline; but ongoing Brexit uncertainty means that safety net of visibility about the longer-term direction of an organisation is harder to build. You can reduce risk by scenario planning; but for organisations that run government contracts, the new political spectrum of opinion on how to operate government services is probably more extreme than any time since the 70s/80s and therefore any scenarios need to span a challengingly broad scope.
Jonathan Blackhurst, Head of Risk, Capita

UK and European investment in business fundamentals falls away



Percentage of firms in the UK and Europe proceeding with investment in business fundamentals

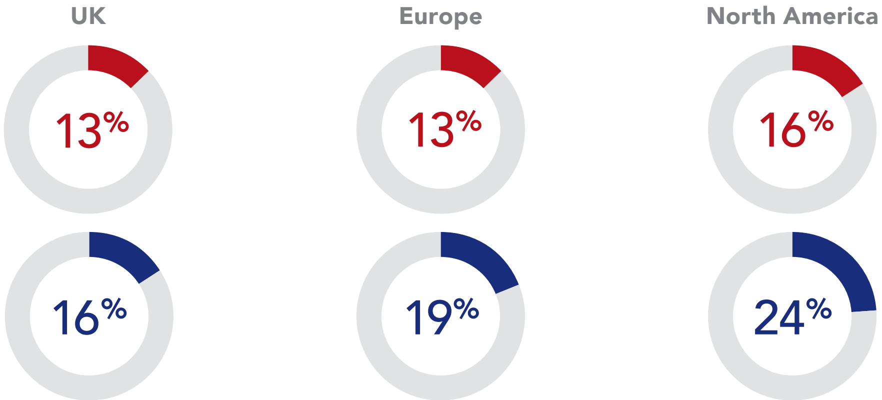
Home markets hold sway but interest in Asia-Pacific is growing

Another way of looking at confidence and risk is to see which markets companies believe have the capacity to perform well.

European business leaders are more confident than their UK peers and this is borne out in their conviction in the ability of Europe to drive growth. Although the trend is for domestic markets to reduce in significance for European companies, in May '19 two thirds (68%) of European business leaders still believed Europe has the greatest capacity to drive growth.

UK executives, perhaps as a direct result of the UK's imminent departure from Europe, have to hold the faith that domestic markets will retain the greatest opportunity to drive growth. In May '19 just under half (48%) of UK business leaders were of this opinion.

Beyond domestic boundaries, business leaders in Europe see Asia-Pacific as their biggest foreign growth market. UK executives by contrast are playing a waiting game and continue to believe that Europe has greatest scope, even though that faith has declined rapidly in recent years.

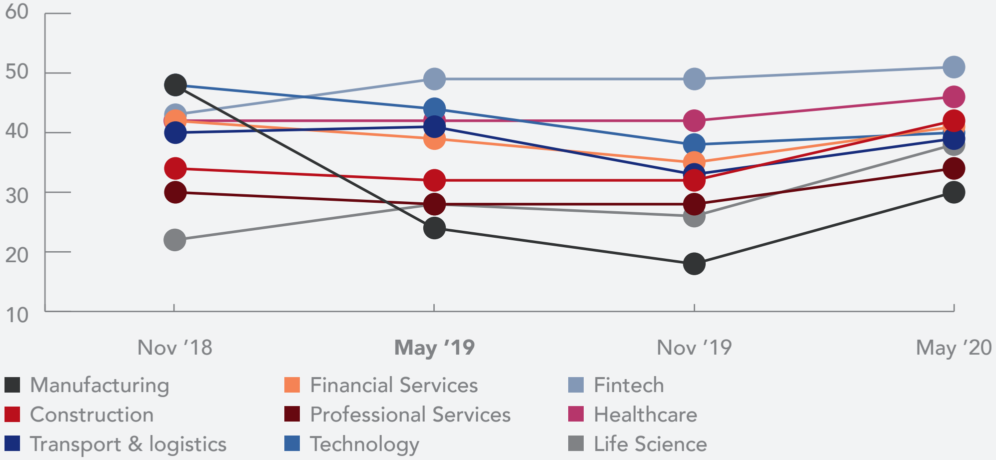


Percentage of business leaders that think Asia-Pacific offers the greatest capacity to drive business growth now and in 12 months' time.

May '19 May '20

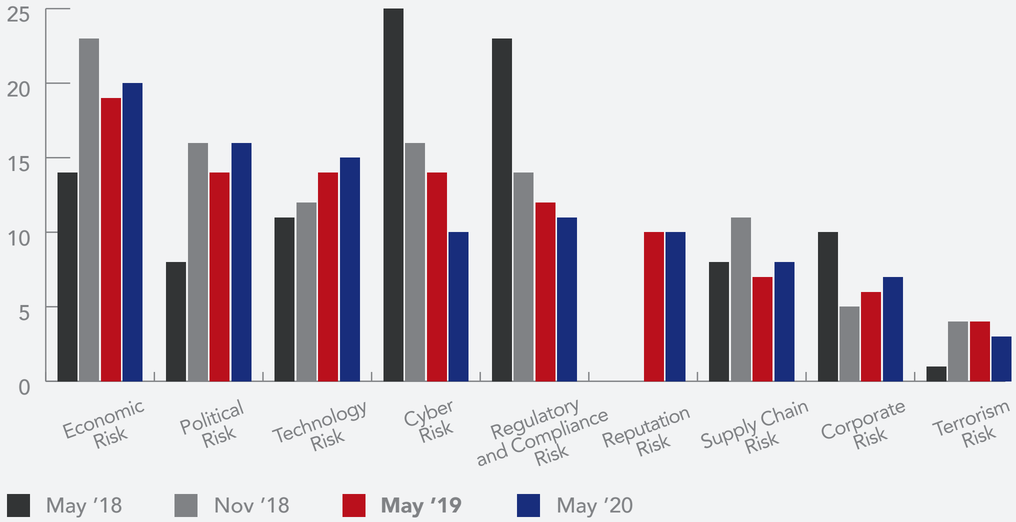
Risk and Confidence in the UK

Confidence strongest among fintech businesses as manufacturing continues deep dive



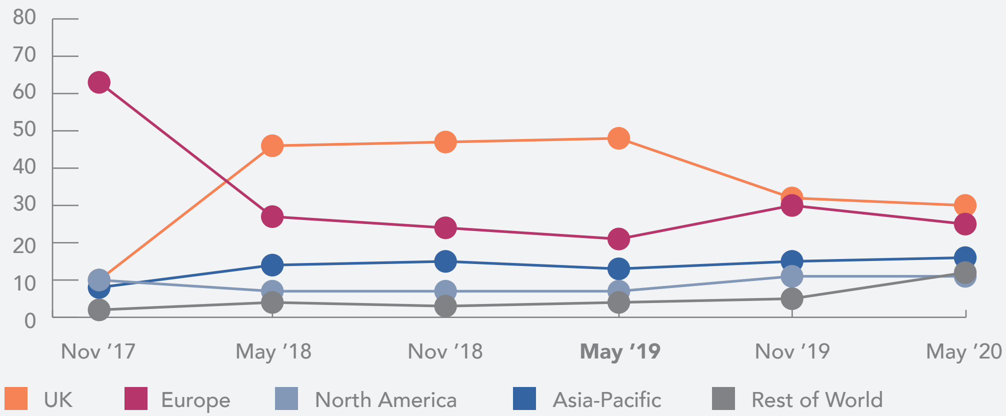
Percentage of companies feeling confident in their ability to grow and prosper split by sector

Economic and political risk dominate; terrorism risk languishes



Top risk concerns for UK business leaders

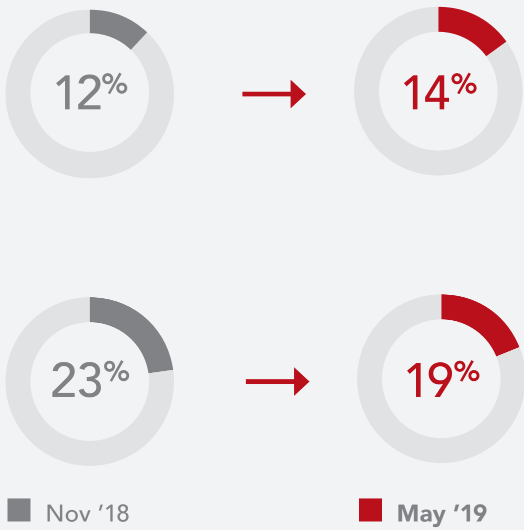
UK volatile on Europe; consistent on Asia-Pacific



Regions where UK companies expect to see growth

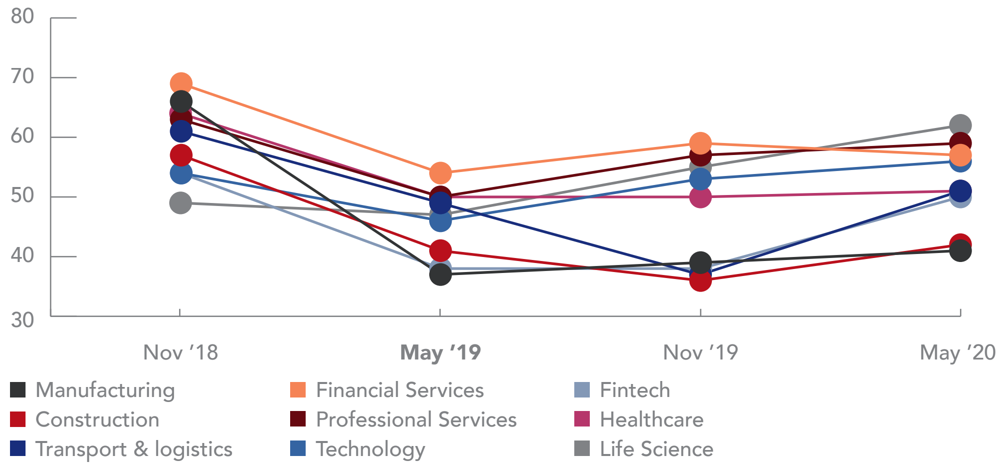
Fastest **growing** risk –
Tech

Fastest **declining** risk –
Economic



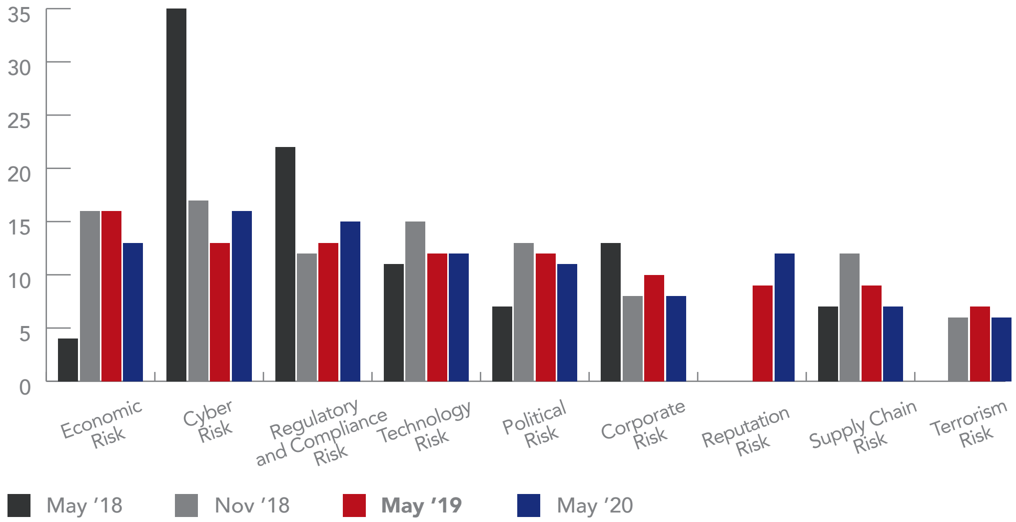
Risk and Confidence in Europe

Confidence strongest among financial services businesses as construction continues deep dive



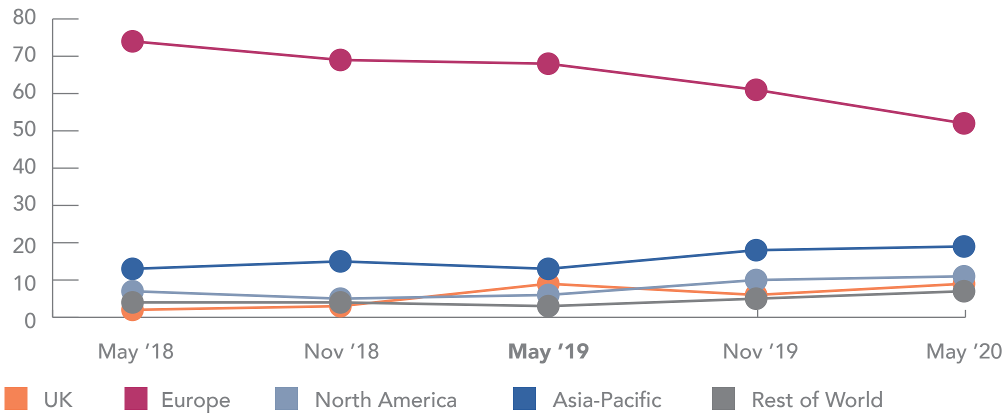
Percentage of companies feeling confident in their ability to grow and prosper by company sector

Economic, cyber and regulatory risk dominate



Top risk concerns for European business leaders

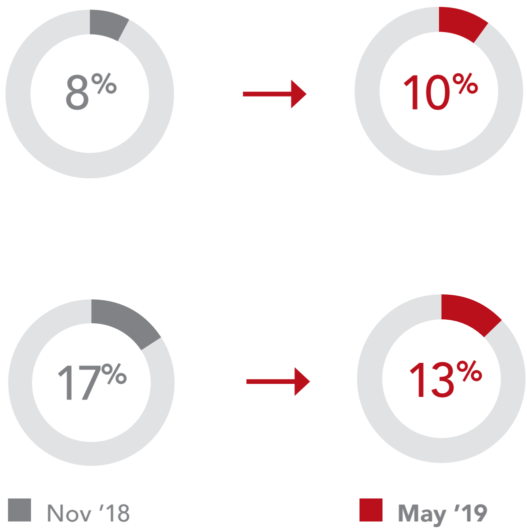
Europe begins to look outward to Asia-Pacific for growth



Regions where European companies expect to see growth

Fastest **growing** risk –
Corporate

Fastest **declining** risk –
Cyber



Cautious North America welcomes Goldilocks

Although confidence levels have dropped five percentage points in North America in the six months to May '19, the region remains the second most confident globally behind Asia-Pacific in what some might describe as a 'Goldilocks' economic scenario – in other words, not too hot and not too cold.

In the US, the economic outlook is healthy, with key economic indicators, including gross domestic product, expected to remain between 2% to 3%. Unemployment is forecast to continue steady and inflation is under control. Business leaders are clearly reassured by the macro indicators, marking economic risk down by eight percentage points between November '18 and May '19.

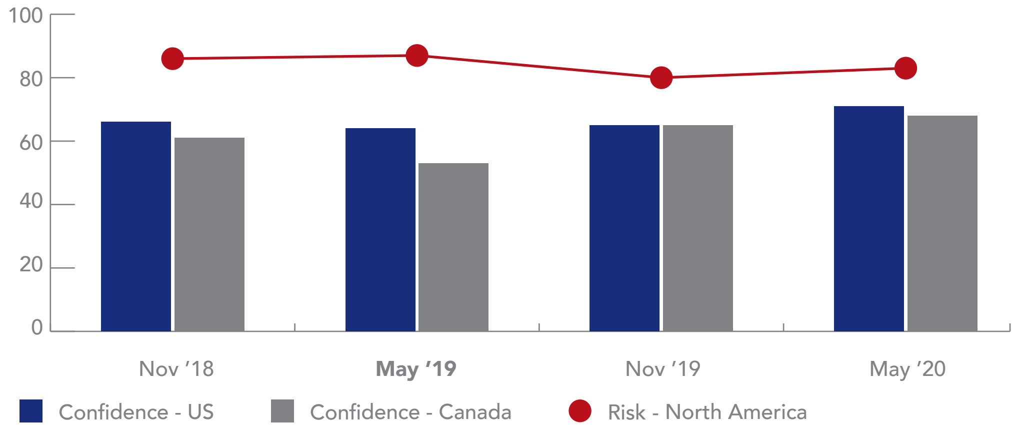
In Canada, the economic omens are weaker. Economic growth under-shot analysts' expectations slightly at the end of 2018, with domestic demand for goods and services in decline. Against this backdrop, Canadian business leaders' expectations for the year ahead are somewhat cooler than their US' peers and there is a sense that businesses will need to look to external markets for growth.

North America risk focus

Cautious confidence among North America's business leaders is supported by risk perceptions, which are holding broadly steady against November '18 levels and then are predicted to fall sharply through to the end of '19 – down seven percentage points in the US and eight percentage points in Canada.

May '19 is a pinch point of low confidence and high risk; but the picture resolves as we look ahead to the end of the year and towards May '20.

May '19 is a pinch point for risk and confidence across North America



Percentage of companies feeling confident in their ability to grow and prosper vs percentage of companies believing they operate in a moderate to high risk environment

Economic and cyber risk still dominate

Economic and cyber risk have both been downgraded in the six months since November '18, but they still manage to dominate risk concerns both now and in 12 months' time, suggesting that although 'Goldilocks' holds sway for now, businesses are not yet convinced that this period of relative quiet prosperity will last. Scope for economic shocks remains – both countries have upcoming federal elections (Canada this year and the US in 2020) putting policy and more particularly leadership in the spotlight with the inevitable knock-on for economic risk.

The cyber threat is also omni-present – businesses' ongoing reliance on ever more complex technology solutions makes that inevitable.

Supply chain risk peaking

It is interesting to see that supply chain risk is at an historic high in May '19.

In our research, supply chain risk has never been a prominent feature in the regional or global risk landscape. However, a push-back on globalisation coupled with a rise in protectionism may be partly to blame here. Trade tariffs and geopolitical disputes between the US and China could escalate in 2019, bringing the risk of further Chinese retaliation and US counter-retaliation. Not only does this cause uncertainty for the US and Chinese economies and their companies' supply chains, it also weakens confidence in export heavy economies in other countries, such as Germany.

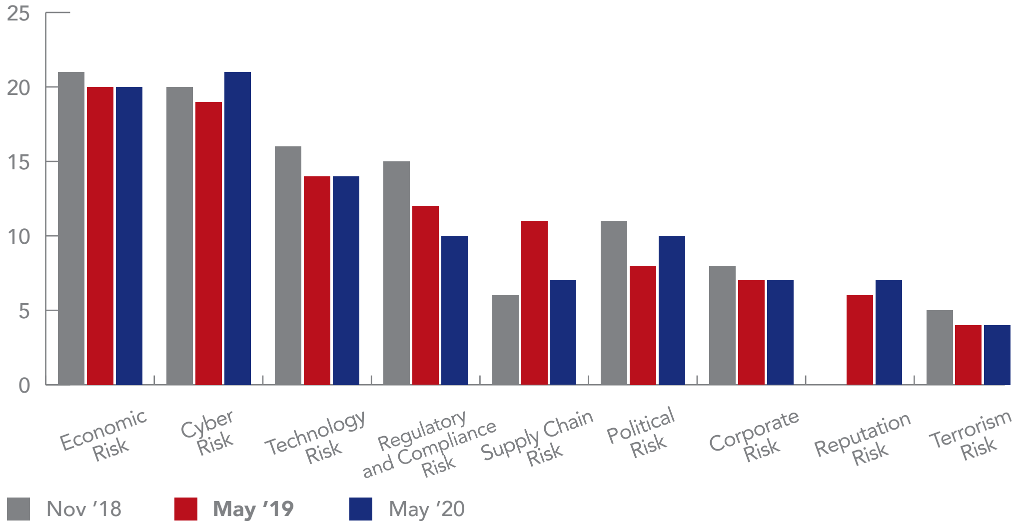
Managing growing supply chain complexity is always an issue, particularly for smaller and mid-size businesses. Although large firms have more at stake, smaller and mid-sized firms still must efficiently manage how and where they produce, assemble and distribute product. Due to their scale they are vulnerable to impact if they move too fast or too aggressively and 'guess' wrong on shifting global politics and policy. This all contributes to this cautionary mood.

Kathleen Ellis, Senior Vice President, CNA International Solutions

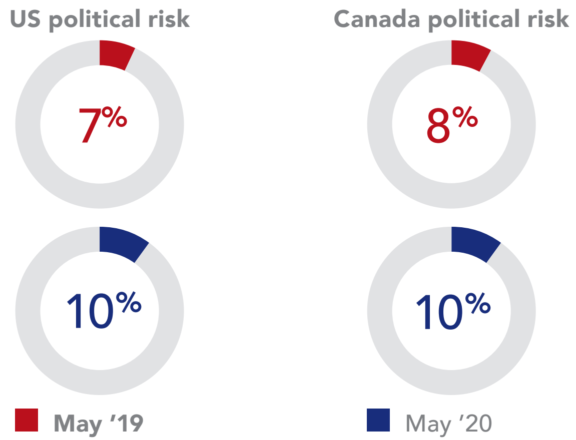
Canada is a trading nation and we are heavily dependent on foreign trade for our economy's health. The continued political and economic uncertainty of the last months coupled with ongoing trade disputes at home and further afield; failure to make any grand leaps forward with climate change mitigation and an increase in extreme weather events only heightens businesses' risk perception and sense of caution around supply chain. This however is the new normal, and businesses operating in a new global landscape no longer have the luxury or security of predictability.

Nick Creatura, President and CEO, CNA Canada

Political and reputation risk waiting in the wings for businesses across North America



Top risk concerns for North American business leaders



Percentage of North American business leaders concerned about political risk now and in 12 months' time.

Political risk recedes as reputation risk rises

Although political risk is on the back burner for now, business leaders predict it will rise in May '20 when the US elections will increasingly take centre stage, making forecasting the future more cloudy, complicated and risky. The process of agreeing the 2020 budget may well crystallise divisions, including the debate over the debt ceiling. For businesses, households and financial markets, the stakes are high.

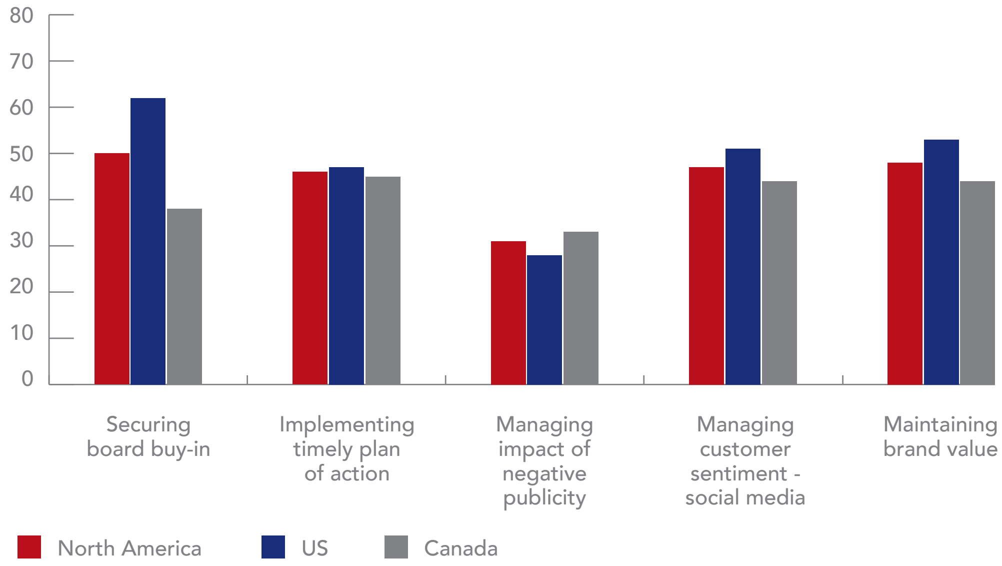
In Canada, the debate over carbon taxes continues to rage and the Court ruling on the Trans Mountain project will further delay the expansion of the pipeline between Alberta and the British Columbia coastal tanker port on which many industries depend.

Businesses thrive on certainty so potential political shocks such as these are a destabilising influence on business strategy and planning. Business leaders are concerned about setting the right course and maintaining growth and are keen not to be caught on the back foot by fast-changing policy.

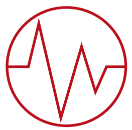
Managing the reputational fall-out from not reading the political runes correctly; or getting caught on the wrong side of an issue is a cause of growing concern for businesses in North America.

Indeed, managing reputation risk is an area that divides US and Canadian executives. Whereas in the US the biggest concern by some margin is securing board buy-in for a particular course of action, in Canada by contrast, concerns focus more strongly on the difficulty of managing the adverse impacts of negative publicity.

Management of reputation risk divides North American executives



Top challenges facing boards when managing reputation risk, May '19



Management liability risk is also rising. This is partly attributable to the increasing pervasiveness of social media. The need to be the 'first to know' drives a heightened sense of urgency to report on events, but that reporting is often overly aggressive and misinformed. The market reacts very quickly – and it never likes surprises. So companies take significant hits in reputation and market value when they experience negative events. The manner in which these situations are handled is extremely important in mitigating the impact of such events.

Nick Creatura, President and CEO, CNA Canada

> In today's social media age, companies of all sizes can be impacted by even minor events that, if not handled with the effective use of thoughtful, responsive media management, can run the risk of appearing detached and unresponsive to current or prospective consumers. There is also a high level of litigiousness driving reputation exposures.
>
> Kathleen Ellis, Senior Vice President, CNA International Solutions

Investment in business fundamentals is on the slide

Reflecting the mood of cautious confidence, our North America research clearly shows that in line with regions elsewhere, fewer businesses are actively proceeding with developing the twin engines of growth: talent and technology in May '19. In fact, investment in developing topline sales fell back in the US between November '18 and May '19. In Canada it grew by only two percentage points over the same period.

Instead, both markets note a slight uptick in corporate development – namely mergers and acquisitions – an activity which has not been prominent in our survey until now. Our view is that as the economy steadies and competition intensifies, companies see greater long-term security and larger growth potential in a significant game-changing deal – rather than in focusing exclusively on slow and steady organic growth.

> As competition has increasingly moved from local to global, businesses need to continue to evolve and build capability in order to compete. It feels like we are on the brink of some very major breakthroughs in terms of robotics, AI and machine learning. The investment dollars required are very significant and the risk of failed projects is always a concern, but leaders can't let that put them off. You've got to be on the bus or the opportunity will be missed.
>
> Nick Creatura, President and CEO, CNA Canada

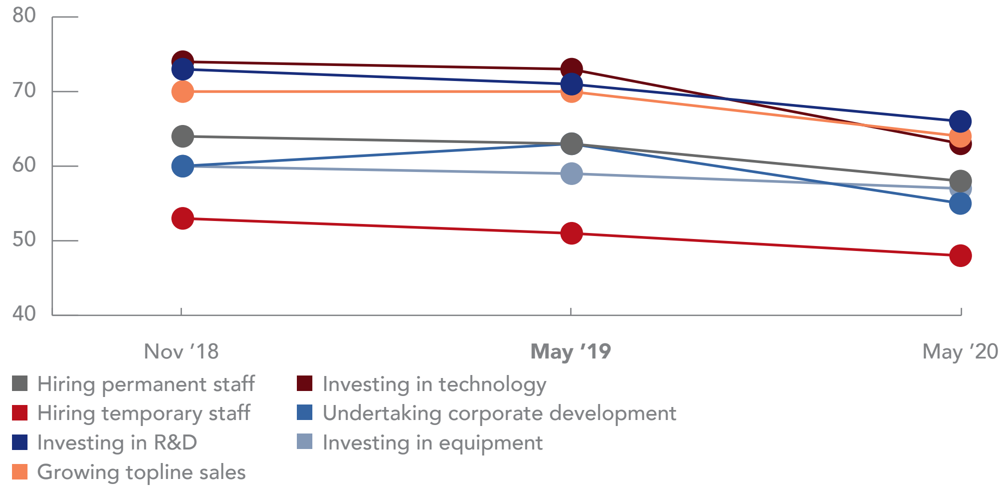
Are business leaders losing their nerve?

As we look ahead to May '20, despite the anticipated confidence recovery in both the US and Canada and the improvement in risk perceptions, the decline in the proportion of businesses actively investing in business fundamentals is predicted to continue.

It would seem that in the current period, North American companies are becoming much less comfortable putting capital at risk in what they perceive to be a relatively high risk operating environment.

Kathleen Ellis comments: "It is a challenge for small and mid-sized firms to make those choices. The percentage of profits and associated risk impacted by those decisions are greater. Therefore, those decisions are made with greater care and thought."

Fewer North American businesses actively investing in business fundamentals into 2020



Percentage of firms in North America proceeding with investment in business fundamentals

Home and away

There are interesting parallels between the US and Canada in terms of the markets that business leaders expect to rely on to drive growth.

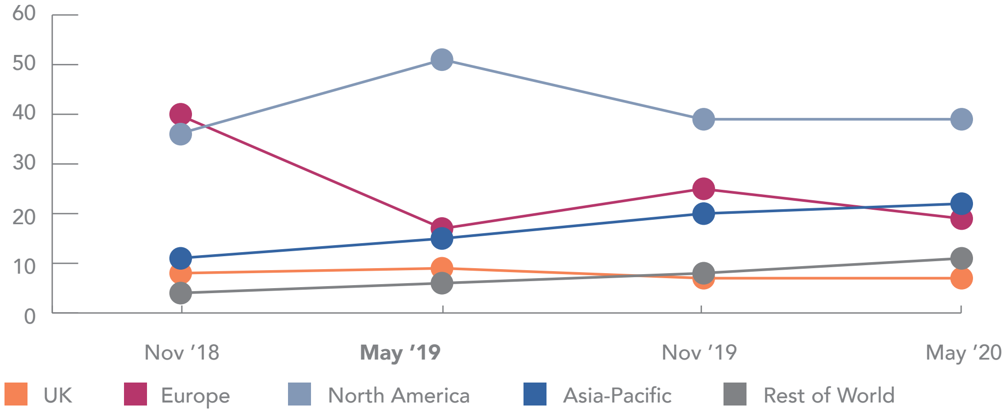
Domestic North American markets feature particularly strongly for US companies in particular, which recorded a rise of 15 percentage points in favour of home-grown opportunities. Canadian business leaders likewise marked-up opportunities in North America by three percentage points. Both countries also showed a notable drop off in interest in Europe between November '18 and May '19. For Canada in particular, this disinterest looks set to intensify.

As we look ahead, the region demonstrating a clear win in terms of growth potential is Asia-Pacific. 60% of the world's youth live in Asia-Pacific, creating a market with both a deep reservoir of talent and significant opportunity for growth. China in particular is a significant consumer of global output, making this a region with significant capacity for growth which no ambitious business can afford to ignore.

Overall foreign direct investment hasn't stopped but it is more cautious. Brexit is casting a bit of a pall on US investment in the UK and Europe. Trade challenges with China and tensions in the region still with North Korea have put a damper on stronger investment. But even with this, there continues to be opportunity in Asia-Pacific. The 'Wild East' still offers pockets of opportunity for growth.

Kathleen Ellis, Senior Vice President, CNA International Solutions

Confidence in domestic markets on the slide



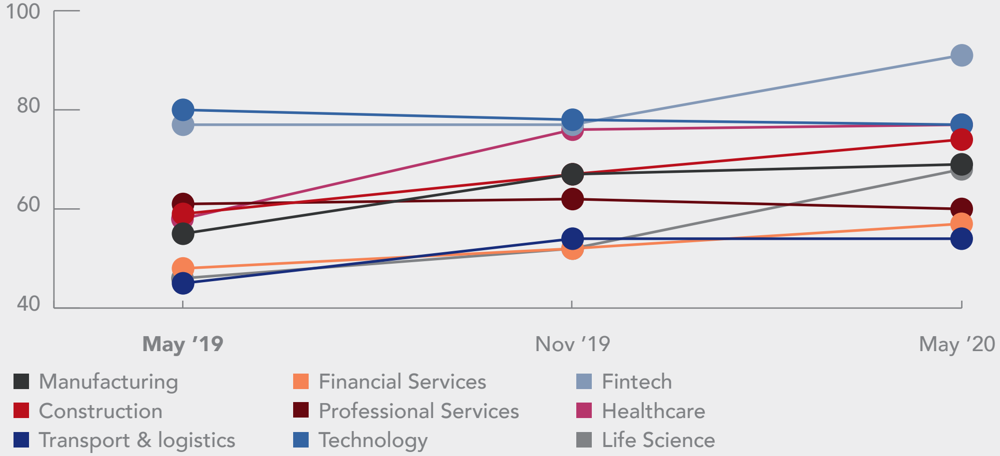
Regions where North American companies expect to see growth

Drops are substantial in US and Canada

Percentage decline in confidence levels in US and Canadian domestic markets by May '20.

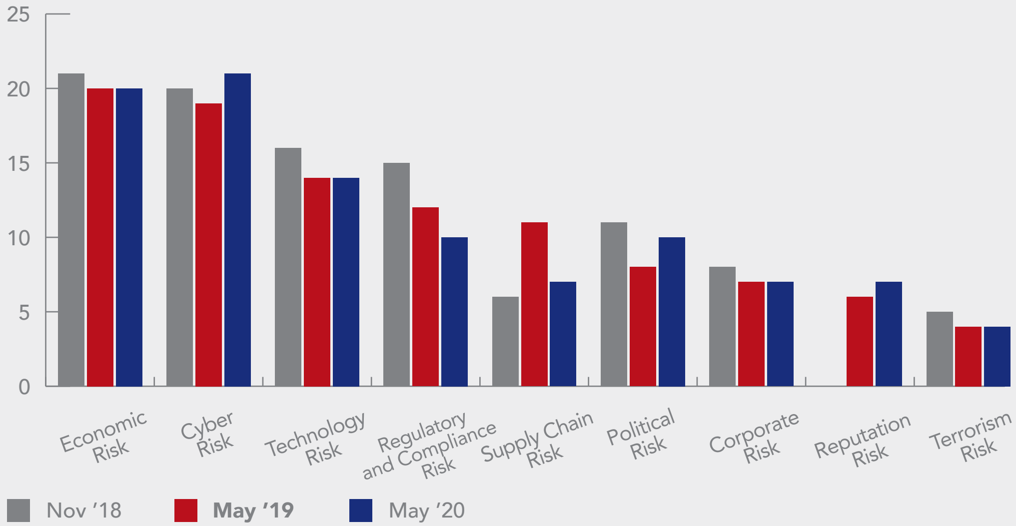
Risk and Confidence in North America

Confidence strongest among technology businesses as fintech surges ahead



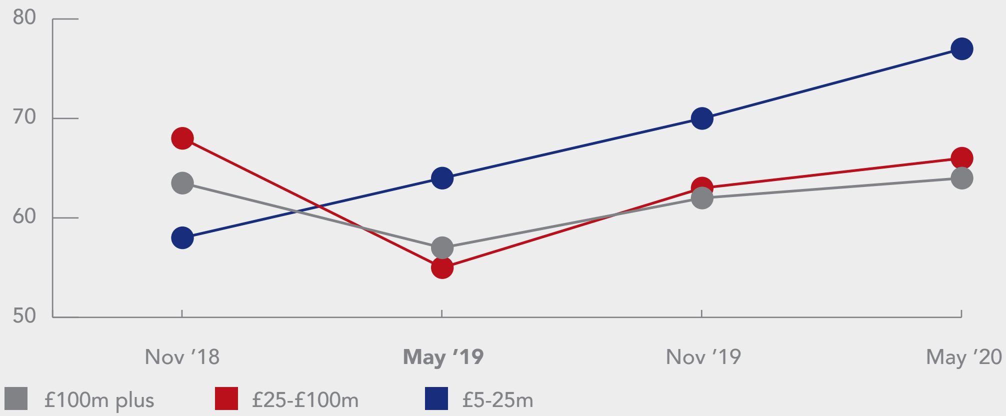
Percentage of companies confident in their ability to grow and prosper by company sector

Economic, cyber and technology risk are top three risks



Top risk concerns for businesses in the US

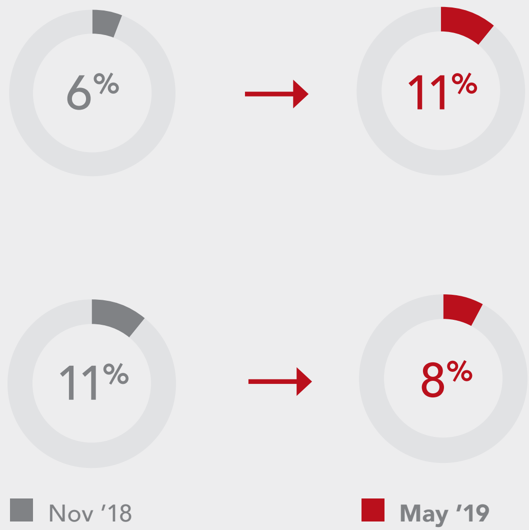
Mid-size companies' confidence is bumpy as small businesses surge



Percentage of companies feeling confident in their ability to grow and prosper by size of business

Fastest **growing** risk –
Supply chain

Fastest **declining** risk –
Political



Asian tiger roars again

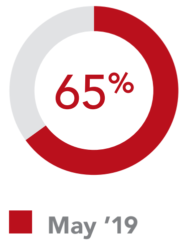
Confidence among business leaders in Asia-Pacific has soared in the past six months with the region now leading the world in terms of its buoyant outlook. This represents a significant shift in sentiment from just six months ago, suggesting the region's leaders believed they may have weathered the worst of the Chinese-US trade war rhetoric and recognising the growing economic dominance of the region as a whole.

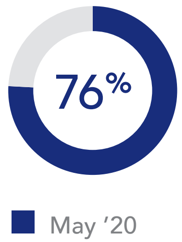
Research for this report was conducted ahead of the May trade negotiations between China and the US, but a report just published by the ECB (European Central Bank) suggests that high levels of regional confidence are well-founded.

In its estimation, the US would be the primary loser in any protracted dispute and in the short term both China and Europe would benefit from 'trade diversion'.

In a complex interconnected world, it seems Asia-Pacific business leaders are comfortable they have both the strength to compete on the world stage and the resilience to withstand consistently high levels of risk whatever the political weather.

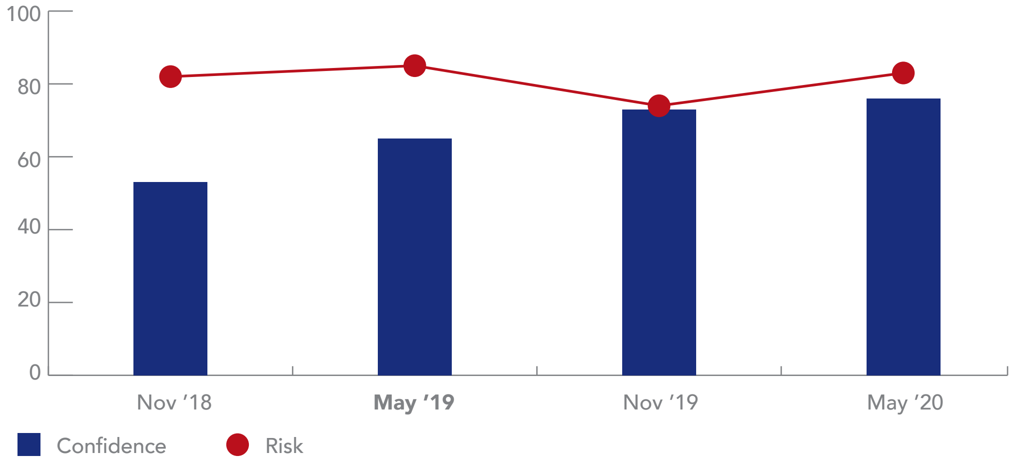
Estimation results suggest that the United States' net export position would deteriorate substantially. In this model, US firms also invest less and hire fewer workers, which amplifies the negative effect[1].





Percentage of companies in Asia-Pacific confident in their business' ability to grow and prosper.

Confidence riding high as risk perception recedes, for now



Percentage of companies feeling confident in their ability to grow and prosper vs percentage of companies believing they operate in a moderate to high risk environment

[1] https://bit.ly/2HrNKVU

Rise of Asia-Pacific

One of the key drivers of optimism across the heart of the Asia-Pacific region is of course its immense resources.

Asia-Pacific is a world leader in terms of natural resource wealth, agriculture, mined elements, rare earth metals (which are a group of metals, such as cerium, critical to most modern technologies) and – not least – people. Notwithstanding the damage caused to economic development by China's historic one child policy, 60% of the world's youth live in Asia-Pacific, creating a market with both a deep reservoir of talent and significant opportunity for growth.

As well as being a major producer, China is also a significant consumer of global output. Indeed, the windfall of rising Chinese demand has been so big the term 'supercycle' was coined because 'bull market' failed to do it justice. Whereas economists used to warn that when America sneezed, the rest of the world caught a cold, now it is China's health that causes other economies concern.

Of course, a changing world order is both an opportunity and a risk for business leaders across all regions.

Decisions taken today in terms of business fundamentals, perhaps particularly around corporate development – joint venturing, mergers and acquisitions – take on a particular resonance for businesses that want to secure their position in the world's fastest growing region. Companies, both domestic and foreign, will want to position not just to supply growing consumer demand in the region, but to ensure their supply chains can tap into the minerals and rare earths which are plentiful here, and are essential building blocks of the computers and technology that power the 4th industrial revolution.

Supply chain strength is crucial

China alone accounted for more than 80% of global production of minerals and rare earths in 2016, placing it front and centre to benefit from the 4th industrial revolution and also providing enormous leverage in terms of its commercial and political relations with other regions. Trade wars over steel would pale into insignificance set against the threat of supply limitation or price rises for materials that simply do not exist elsewhere.

Against this backdrop, it is interesting to see how supply chain risk is rising in importance for businesses in Asia-Pacific. Traditionally, supply chain risk fails to get much airtime with boards in any region surveyed for our Risk and Confidence reports. However, in Asia-Pacific, concerns about supply chain have risen in the past six months and the risk now occupies fourth position in the league table just behind economic, technology and cyber risk. It also remains at a relatively elevated level through to May '20.

As President Xi's signature Belt & Road initiative rebuilds the region's ancient silk routes with nearly a US$ 1 trillion earmarked for infrastructure investments to around 1,000 projects, domestic and foreign enterprises alike will want to ensure that their supply chains are optimised to capitalise on the Asian growth story.

There is opportunity and risk here for international businesses. What the Chinese government describes as an initiative "to enhance regional connectivity and embrace a brighter future", others see as a kind of neo-colonialism in which the Chinese government is pushing for dominance in global affairs via a China-centered trading network.

As the stakes rise, it is not surprising that supply chain risk perception is increasing.

Focus on corporate development by businesses within Asia-Pacific is growing

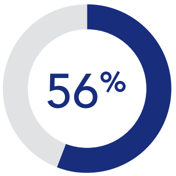
Recognising the shift toward Asia-Pacific, we see a big change in corporate behaviour among domestic and foreign businesses.

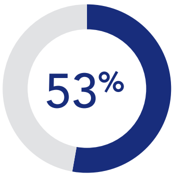
Corporate development has been the least favoured target of investment for businesses in Asia-Pacific – in common with our findings for every other region in the world.

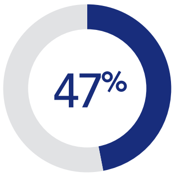
Enthusiasm for corporate development waned in May '19 falling from 51% in November '18 to 32%. This is part of a global picture in which enthusiasm to invest in business fundamentals has fallen back somewhat in the face of global economic uncertainty. However, change is under way. Investment in corporate development is set to go from zero to hero in Asia-Pacific, with just under half (47%) of businesses expecting to be actively proceeding with corporate development plans by May '20.

Although GDP in Asia-Pacific is less impressive than in years gone by, growth is declining less rapidly than anticipated and will still comfortably outstrip that of Western economies for years to come. This intention to invest in corporate development represents a resounding vote of confidence in Asia-Pacific growth by the businesses that operate here. Indeed, local businesses are now moving to secure the scale, the expertise and the market penetration that will position them for future growth.

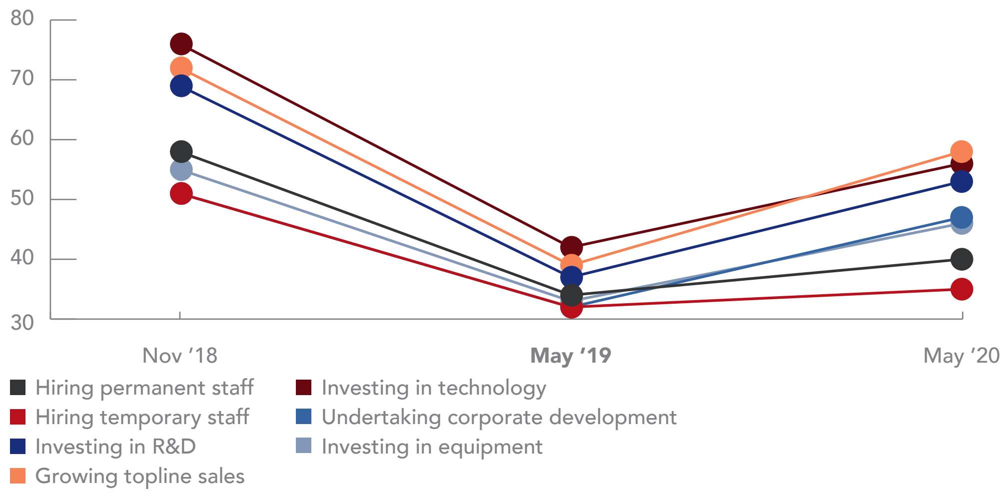
Investment in business fundamentals improves by May '20







Corporate development: zero to hero



Percentage of firms in Asia-Pacific proceeding with investment in business fundamentals

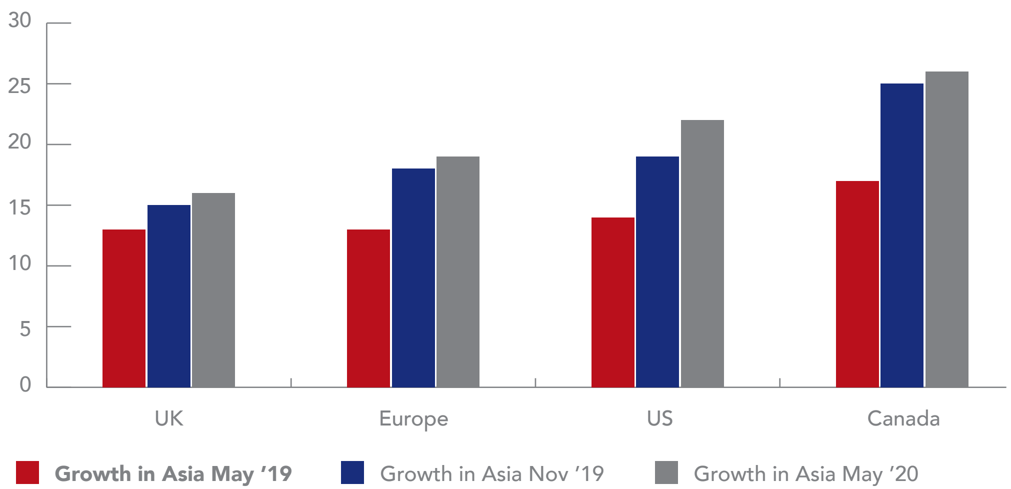
International focus is shifting East

International recognition of the power of Asia-Pacific is also set to rise. In every region around the world, expectation is rising among business leaders regarding Asia-Pacific's capacity to drive growth. The trend is particularly noteworthy among North American businesses.

Kathleen Ellis, Senior Vice President, CNA International Solutions comments: "We are seeing more of an interest in Asia-Pacific from businesses right across the board."

By May '20, over a fifth of global business leaders predict that Asia-Pacific will be the region that has the greatest capacity to drive their growth, putting it well ahead of the global pack.

Every region expects to trade more with Asia-Pacific



Percentage of foreign companies rating Asia-Pacific as a market with strong potential to drive growth

Asia-Pacific risk focus

Economics and politics remain intertwined

Perhaps reflecting confidence in their domestic economy and its resilience against external threats, Asia-Pacific leaders are consistently downgrading economic risk, which is predicted to fall seven percentage points between May '19 and May '20.

Political risk by contrast, although a dramatic faller in the six months from November '18 as concerns around trade wars abated, is set to rise two percentage points looking out to May '20. This rise may reflect the fact business leaders recognise they are not out of the woods yet. The Asian Development Bank commented in a recent report: "The main risk to the outlook is still the ongoing trade conflict, as heightened trade policy uncertainty can negatively affect investment and manufacturing activity."[2]

Tech and cyber risk de-couple

Business leaders in Asia-Pacific believe technology risk will rise this year and next. Our research defines technology risk as IT system failure or disruption from new tech-enabled competition.

We need look no further than the recent grounding of aircraft as an example of the terrible consequences of IT failure – both for customers and for businesses. Thankfully not all failures are so catastrophic, but the example shows the potential scale of the threat and also underlines the huge reputation impact that flows directly from technology failure.

The interconnections here are legion, amplifying the significance of technology risk going forward in every region.

[2] https://bit.ly/2W1zY5s

Cyber risk, by contrast, shows a steady decline from November '18 through to May '19. This does not mean that the threat is diminishing – indeed it remains a top three risk for the region – just that business leaders are becoming slightly less concerned by it. While it is impossible to prevent cyber crime, it is possible to improve protections against risk threats and we believe these results are evidence that business leaders in Asia-Pacific are becoming better attuned to cyber risk and feel more confident about their defence strategies.

Boardroom risks on the rise

There are three risks which pose a particular concern to individuals in the boardroom:

- reputation risk (loss resulting from damage to reputation following an adverse event)
- regulatory and compliance risk (such as new and growing exposures from regulation local and international)
- corporate risk (fraud, corruption and governance failures).

In Asia-Pacific, both reputation and corporate risk are rising through to May '20. Only regulatory and compliance risk is declining in importance.

While it is encouraging to see that business leaders in Asia-Pacific are becoming more comfortable with the ever-growing burden of regulation; concerns remain that the quality of governance in local businesses is not strong and will come under increasing scrutiny as the region becomes more significant on a global level. Poor governance, fraud or corruption lead inexorably to reputation risk and the potential destruction of shareholder value.

Reputation risk is also an inevitable consequence of greater operational complexity in global, technology-dependent businesses which are growing up fast in Asia-Pacific.

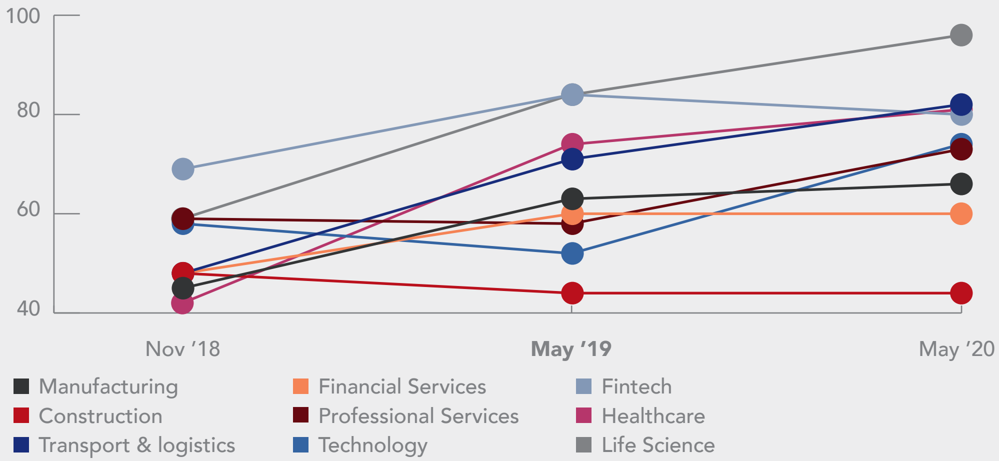
In these new areas of risk, there is a real danger of rushing to address the risk without having the supporting infrastructure. The pressure to act fast is quite a paradigm shift for large scale corporate risk managers. Most traditional risks at the top of the list are attritional. But emerging risks – cyber, tech, data, info – these new principle risks are immediate and can be irrecoverable.

The answer has to be around balance – businesses need to take their time and not be scatter gun or knee jerk. It's about building emerging risk modelling skills faster – maybe a twin or multi track approach to balance the immediate crisis management response issues with longer term business model resilience planning.

Jonathan Blackhurst, Head of Risk, Capita

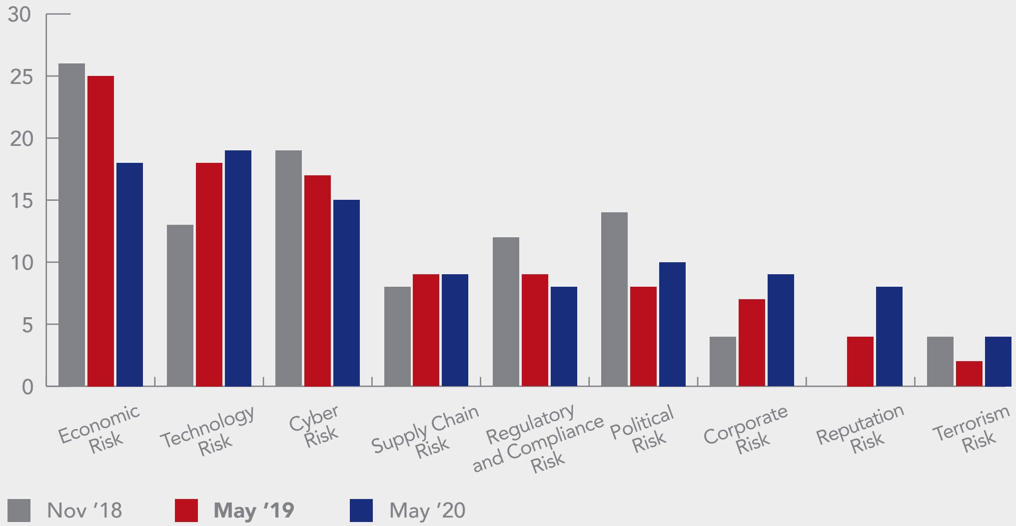
Risk and Confidence in Asia-Pacific

Confidence strongest among life science and fintech businesses



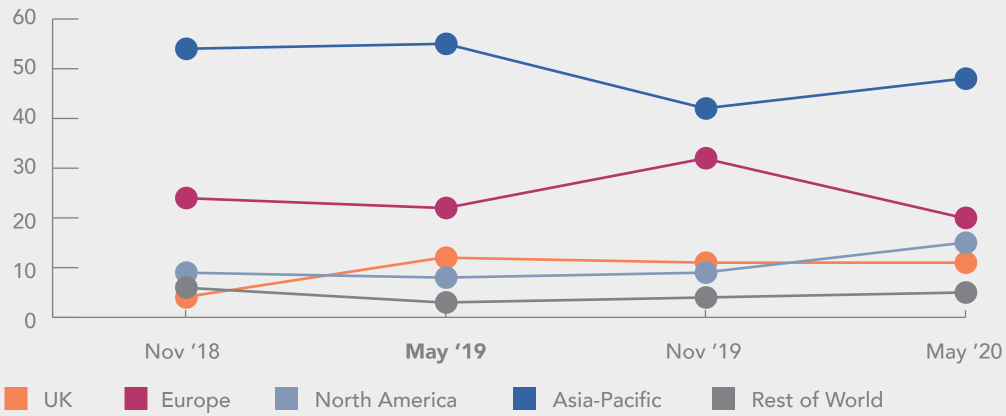
Percentage of companies that are confident in their ability to grow and prosper by company sector

Economic and cyber risk drop as technology and corporate risk rise



Top risk concerns for Asia-Pacific business leaders

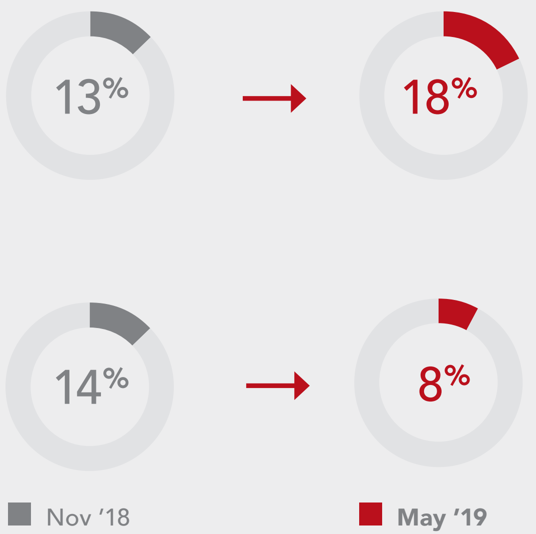
Domestic markets remain key



Regions where Asia-Pacific companies expect to see growth

Fastest **growing** risk –
Technology

Fastest **declining** risk –
Political



Methodology

Opinion Matters, an independent research agency, conducted quantitative research on behalf of CNA Hardy. This research was undertaken between February and March '19, via an online survey of 1,500 business leaders of multinational firms with operations in Europe. Qualitative research was undertaken by independent communications agency Luther Pendragon in May '19.

Company size ranged from businesses with a turnover of US$6.3m up to more than US$126m.

The regional sample split was:

- 450 firms based in the UK
- 250 firms based in France and Germany
- 450 firms based in the US
- 100 firms based in Canada
- 250 firms based in Singapore, South Korea and Australia

The survey respondents were evenly split from across the following industry sectors:

- Manufacturing
- Construction
- Transportation and logistics
- Financial services
- Professional services
- Tech
- Fintech
- Healthcare (private)
- Life science

In addition, Luther Pendragon, a London-based communications agency, undertook telephone interviews with representatives across the target business sectors and CNA Hardy representatives.

Luther Pendragon worked with CNA Hardy to analyse the data, write and prepare the May '19 Global Risk and Confidence survey report.

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