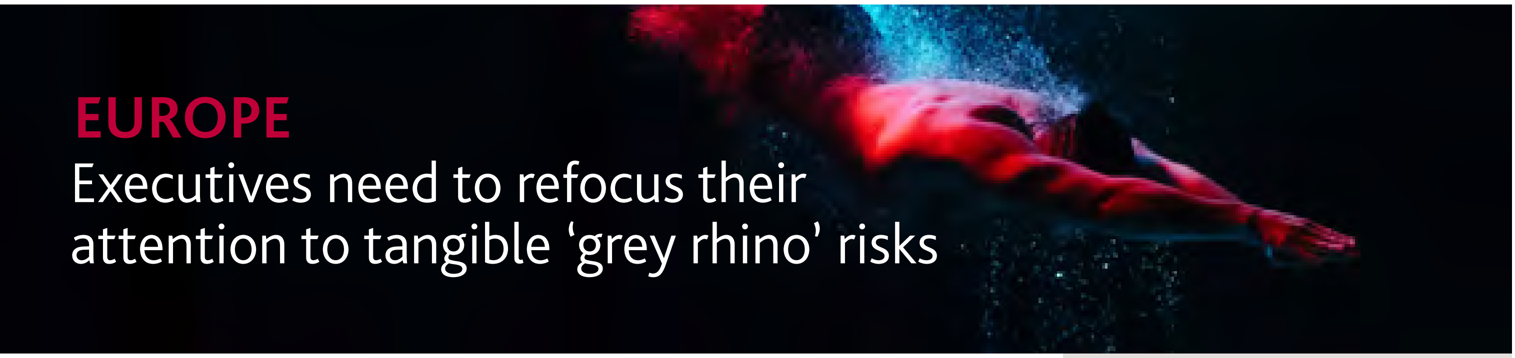

EUROPE
Executives need to refocus their attention to tangible 'grey rhino' risks

BDO's Global Risk Landscape Report 2019 reveals that, in the light of macroeconomic and geopolitical disruption, European Boards need to refocus their risk planning away from 'black swans' and towards 'grey rhino' risk factors.

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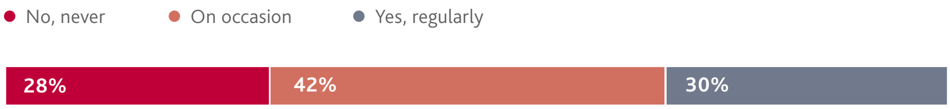
Anticipating and mitigating risk involves carefully weighing up many interconnected factors, from regulatory to economic, environmental to people risk. Understanding the likelihood of any given risk to impact your business over the short and long-term, and the potential negative consequences should such a risk occur, provides a solid foundation for future business resilience.

Have executives across Europe got the balance right in their risk planning? To answer that question BDO surveyed 90 C-suite executives from leading companies across Europe.

Our research suggests a majority of European companies may need to reconsider whether their approach to risk analysis and planning is fit-for-purpose. Nearly three-quarters of those polled say their company's Board has a tendency (either 'regularly' or 'on occasion') to neglect 'grey rhinos' – those risks which are highly obvious but often ignored. Instead they focus their attention on unpredictable risks, so-called 'black swans'. Fewer than three in ten believe their Board pays sufficient attention to 'grey rhino' events.

Figure one: Do you believe that 'grey rhino' events are being neglected by the Board in favour of 'black swan' events?



Today businesses across the European continent face growing uncertainty over the impact of Britain's withdrawal from the EU, particularly on cross-border trade and supply chains. In its Spring Economic Forecast, the European Commission cited Brexit, alongside weakness in the manufacturing sector and a pronounced slowdown in the German economy, as factors that will dampen growth. The Commission expects GDP growth across Europe to decrease to 1.4% in 2019, down from 2.0% the previous year.[1]

There is a pressing need, therefore, to recalibrate risk conversations around the Board. As well as bringing more immediate risk factors into closer focus, executives need to make sure they achieve the right balance of time spent considering preventable risks (the most tangible and measurable), strategic risks (including 'grey rhinos') and external risks (the 'black swans').

What are the risks that concern European executives most? Our research reveals that European business leaders feel most underprepared to address climate and environmental risks. A third of our survey participants (31%) place environmental risk within their top three areas of under-preparedness. This is on an equal footing with damage to brand value or reputation, and closely followed by macroeconomic slowdown and their ability to raise capital.

The two leading risks for 2019 have both rapidly risen up the risk agenda since last year.

In our 2018 risk survey, European executives were most concerned about geopolitical and macroeconomic risk. While both these risks remain important concerns for executives this year, they have been significantly leapfrogged by environmental and brand reputation risks.

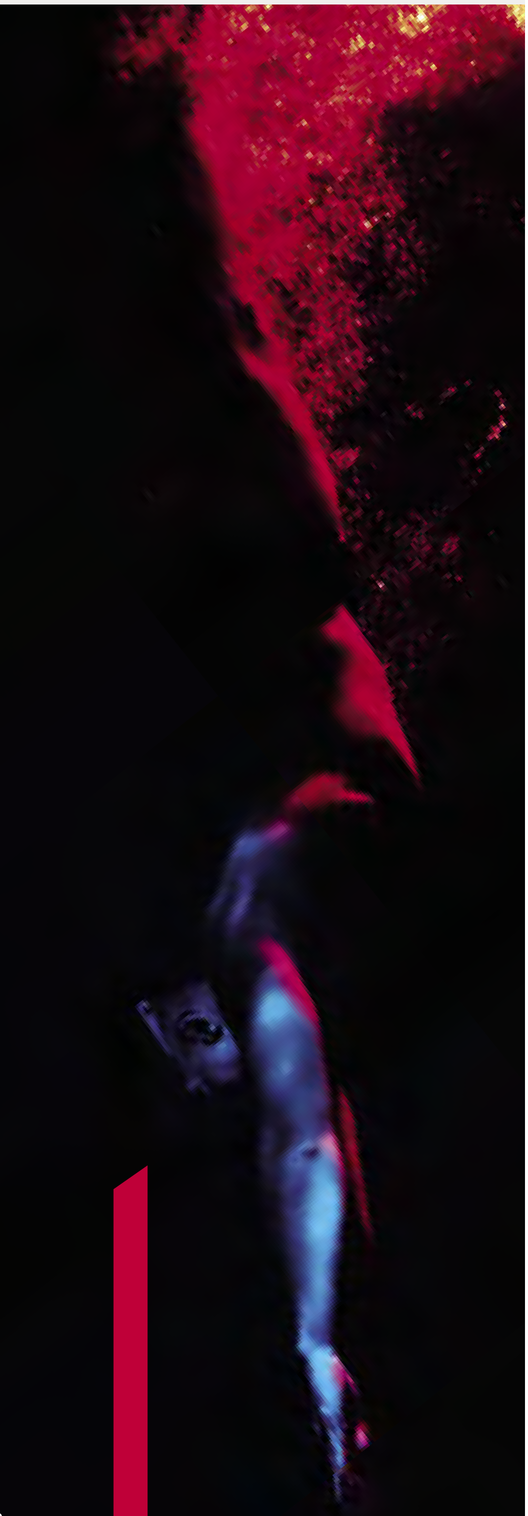
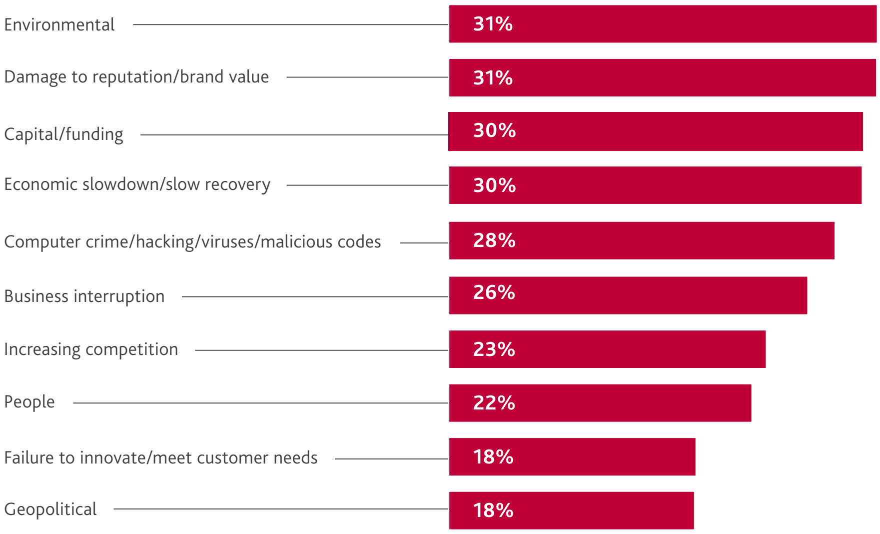


Figure two: Which of the following risk are you most underprepared for?



Environmental risks come in many forms, from disruption to supply chains and transportation, to resource scarcity and extreme weather events that can shut down business operations unexpectedly.

The EU has set itself the target of achieving a 'climate neutral' economy by the year 2050, as well as more immediate greenhouse gas and carbon reduction targets for 2020 and 2030.[2] When asked about environmental risks specifically, a third of our survey respondents say managing the transition to a low carbon business model is their primary concern. This is a risk that has the potential to impact many areas of business operations.

However, the cost of failing to act on climate risks may also be substantial. A recent European Union-funded study, Co-designing the assessment of climate change costs, suggests that extreme weather events have cost European businesses more than €2.5 billion each year since 1998, and that these costs will rise by upwards of 20% over the mid-term.[3]

Our research reveals that, despite the importance of climate, executives have only included environmental risks on their risk register relatively recently. For example, only 19% of survey respondents say that man-made climate disaster first entered their risk register more than three years ago. Only 20% say extreme weather events have been on their risk register for more than three years.

Figure three: Risks businesses are least prepared for, over past three years

	2017	2018	2019
01	Technological changes and development	Regulatory risk	Damage to reputation and brand value
02	Regulatory risk	Macroeconomic developments	Computer crime/hacking/viruses/malicious codes
03	Macroeconomic developments	Environmental	Economic slowdown and slow recovery

Like environmental risks, reputational or brand value risks often come with a heavy financial price to pay.

For example, in 2018 the European Commission levied fines of more than €4 billion on technology giant Google for anti-competitive practices relating to its Android operating system.[4] Consumer research conducted around the time of the fine suggested that only 27% of European consumers believed Google had fair business practices.[5]

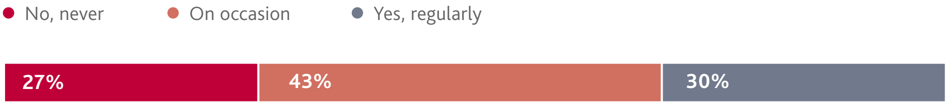
Although these factors may not have adversely impacted the sustainability of Google's business over the long-term, it does suggest that consumers are paying much closer attention to negative stories they read about companies in the press.

Given the rapid rise of new risk factors such as environment and brand reputation up the agenda, executives need to make sure they give these risks the same degree of serious assessment and mitigation that they would to traditional risk areas such as financial risk or operational risk.

Three in ten European respondents to our survey express a concern that their risk register is unduly influenced by 'hype cycles' – issues being heavily covered in the media were given greater attention simply because they were at the forefront of minds. This suggests that executives need to be more conscious of any bias inherent in their risk evaluation approach that may cause them to miss tangible risks likely to impact their organisation.

Rather than approach risk management as a compliance exercise to satisfy governance requirements, it may be time for executives to reframe their conversations about risk. Those leaders who take a more proactive approach to risk management have benefited from better business decisions and improved strategic resilience.

Figure four: Do you believe your organisation's risk register is influenced by 'hype cycles', depending on which risks are being talked about in the industry the most?



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