The changing world of strategic risk

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Effective risk management has always been the cornerstone of the most successful companies. But in today's risk-filled business environment, it can be difficult for executives to assess whether their plans and strategies can be executed as anticipated. One of the main reasons is that strategic risks—those risks that either affect or devolve from business strategy decisions—can strike more quickly than ever before. The catalyst behind that reality is frequently new, rapid-fire business trends, as well as technological innovations such as social media, mobile and big data. Companies that fall behind on the innovation curve may quickly fall prey to innovation's evil twin-disruption. That is just one of the several reasons why managing strategic risk has become such a high priority for many executives, worldwide. The fact is that today risks strike at a much greater speed. That is why companies have to be better prepared and ready to respond much faster than they might have been even just three or four years ago.

In a recent study, we uncovered significant and compelling evidence that many businesses around the world are adopting a new view of the risk universe. The study, conducted in spring 2013 by Forbes Insights, on behalf of Deloitte, was a global survey of strategic risk management practices at more than 300 major companies worldwide. In the survey, Deloitte had one major objective: to better understand how businesses can manage strategic risk more effectively—both now and in the future. The survey set out a wide range of issues and questions, such as:

1. **To what extent are companies considering and addressing risks as they develop and evaluate their business strategies?**
2. **What new risks do their strategies create?**
3. **Which strategic risks are critical to avoid or essential to take?**
4. **What is the strategic impact of new technologies, and which investments are essential to managing risks and exploiting new opportunities?**
5. **And, even if a company's strategy is executed flawlessly, what other risks could undermine the business?**

More broadly, the main areas of the survey covered the alignment of strategy and risk, the monitoring of strategic investments, and the emerging views of strategic risk management.

While some findings reinforced what many already believe, there were also some surprises. Here are a few of our key findings:

Most companies are doing more than just making strategic risk management a higher priority

Importance of strategic risk

Strategic risk has become a matter of substantial focus for companies. 81% of the companies surveyed are now explicitly managing strategic risk. In addition, many companies are adopting a broad view of strategic risk that goes beyond a focus on challenges that might cause a particular strategy to fail. They are also weighing any major risks that could affect a company's long-term positioning and performance.

A higher priority

Most companies are doing more than just making strategic risk management a higher priority. They are also changing the very way they manage strategic risk. In fact, nearly all respondents (94%) have changed their approach to strategic risk management over the past three years. The numbers were slightly higher in Asia/Pacific (96%), and slightly lower in Europe/Middle East/Africa (EMEA) (91%).

Progress made

A key improvement noted by the survey is that more and more companies are integrating strategic risk analysis into their overall business strategy and planning processes. And that integration appears to be working. Among the companies surveyed, 61% now believe their risk management programmes are performing at least adequately in support of the development and execution of their business strategy. But that's only part of the story. According to the overall results, only 13% of companies rate their risk management programmes at 5 out of 5 in terms of supporting the development and execution of strategy.

A matter for the CEO and board

Strategic risk management is a CEO and board-level priority. Two thirds (67%) of the companies surveyed say that the CEO, board, or board risk committee has oversight of strategic risk management. In EMEA, CEO direction is much lower than average and board direction is higher. Top-level oversight is particularly common at consumer companies, followed by companies in financial services and technology, media and telecommunications.

An executive of one large European conglomerate explained how risk management policy is set by the managing board. "*Our risk management policy is set by our managing board*", says Siemens AG's Dr. Georg Klein, Chief Risk & Internal Control Officer, Corporate Finance and Controlling. "*On the other side, the organisational and accountability structure is primarily based around Siemens' four sectors: energy, industry, infrastructure & cities and healthcare. Sector managers, together with regional clusters and corporate units, implement risk management programmes that are tailored to their specific industries and responsibilities, yet consistent with the overall policy established by the managing board*."

Reputation

Reputation risk is now the biggest risk concern. That fact is due in large measure to the rise of social media that enable instantaneous global communications. These media make it harder for companies to control how they are perceived in the marketplace. The emergence of new communication vehicles, such as mobile and social networks, has given rise to concerns that new forms of communication may impact corporate reputation in different and faster ways than ever before. Hence the need to monitor these vehicles and the content they carry to accurately anticipate and proactively control the emerging risk.

According to the companies interviewed, social technologies are one of the main factors driving rising concerns about reputation. Given the speed and global reach of social media, companies today are at much greater risk of losing control over how they are perceived in the marketplace. As a result of the rise of social media, reputations built up over decades can be challenged or undermined in an instant. Customers frequently make decisions about an organisation based on social media comment, and sometimes well before any corporate team can intervene to defend the organisation or formulate a response.

Impact of technologies

Technologies are also having a major impact on the business and risk landscape. The majority of the companies surveyed (53%) believe technology enablers and disrupters such as social, mobile and big data could threaten their established business models, and 91% have changed their business strategies since those technologies began to emerge. New technologies have had their biggest impact in three sectors: technology media and telecommunications (97%), consumer and industrial products (96%) and life sciences (94%). Regionally, the largest impact was in Asia/Pacific, where 98% of respondents report having changed their business strategies.

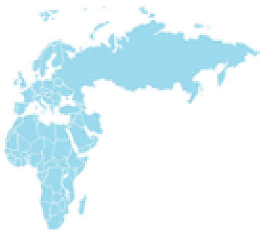
Q: Has your approach to managing strategic risks changed in the last three years?

Total respondents

Americas

94% | Yes
6% | No

Europe/Middle East/Africa



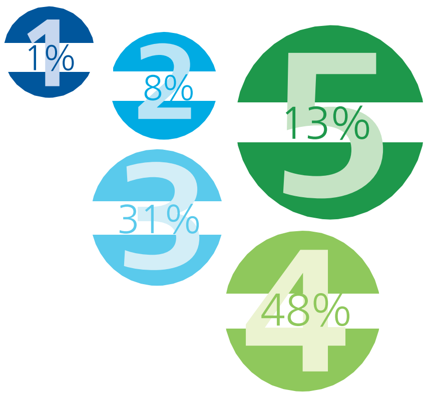
91% | Yes
9% | No

Asia/Pacific

96% | Yes
4% | No

Q: On a scale of 1 to 5, how well do you think your risk management programme supports your ability to develop and execute your business strategy? (5 indicates very well)

Total respondents



Americas

33% | Not as well
67% | Well/Very well

Europe/Middle East/Africa

49% | Not as well
51% | Well/Very well

Asia/Pacific

37% | Not as well
63% | Well/Very well

1-3 | Not as well 4-5 | Well/Very well

Q: Which of the following risk areas have the most impact on your business strategy (three years ago, today and three years from now)? (Respondents could choose more than one answer. The top three are shown below)

2010

41% | Brand
28% | Economic trends
26% | Reputation

Today

40% | Reputation
32% | Business model
27% | Economic tends| Competition

2016

29% | Economic trends
26% | Business model
24% | Reputation| Competition

Human capital and innovation

Three years from now, human capital and the innovation pipeline are anticipated to be the top strategic assets in which businesses will need to invest. Many respondents (47%) view human capital—that includes employees, partners, and contractors—as a strategic asset worthy of investment. The innovation pipeline is another strategic asset closely related to human capital. Again many respondents (23%) consider it a worthy investment. In addition, many respondents (26%) view customer capital as an important area of investment. Three years into the future, we anticipate that the innovation pipeline will emerge as a top risk-related strategic asset in which to invest.

Clearly, in an era in which risk can become reality in the blink of an eye, companies need new capabilities and approaches for managing strategic risk. In particular, they should now weigh and assess a much broader set of risks and strategic assets. That set should include, but should not be limited to, people, intellectual property, customers, marketing efforts and even 'the crowd'. These risks and assets are much more difficult to measure, capitalise on and hedge against. For that reason, they demand a much more systematic and sustained approach to monitoring and managing risk.

In order to address the risk challenges of tomorrow today, companies must also reach outside of their traditional corporate structures to adopt a more 'outside-in' perspective when assessing their strengths, challenges and opportunities. This will require a new commitment to gathering data and appreciating external perspectives from 'outside' sources. That includes customers, bloggers, information trend setters, and marketplace and security analysts. It will also require learning from other companies and industries.

We have witnessed an information explosion in the past decade—what Tom Friedman of 'The New York Times' has called "*the Great Inflection*"—a hyper-connected world grounded in social media, cloud computing, 4G wireless, ultra-high-speed bandwidth, System-On-a-Chip (SOC) circuits, mobile devices, tablets, etc. Managing risk in this new business universe requires much more than listening to customer feedback. The accepted information hierarchy, including established newspapers and media outlets, has rapidly given way to a multidimensional information matrix where no single voice dominates. Information and opinions of all kinds are easier to access, yet more difficult to evaluate and control. In response to these new realities, companies are making a deliberate effort to improve their strategic risk management capabilities and performance.

Traditional approaches to managing risk tend to concentrate on monitoring leading financial indicators in addition to the evolving regulatory environment. Yet, given that they are generally grounded in audited financial statements, the risk strategies and hedges that result are in large measure a reaction to past performance or negative events. They do not, however, necessarily serve to detect future strategic risks or predict future performance. For that reason, they are more focused on protecting value than on creating it. Given the result of this survey, we are confident, however, that the traditional approach is quickly giving way to new and innovative approaches to strategic risk management—approaches that are much more focused on the future.

This piece draws heavily on "Exploring Strategic Risk 300 executives around the world say their view of strategic risk is changing", Deloitte, 2013.
For information, contact Deloitte Touche Tohmatsu Limited or visit www.deloitte.com/strategicrisksurvey.
Exploring Strategic Risk: 300 executives around the world say their view of strategic risk is changing, p. 8