Get a grip on intangibles

The pandemic has focused our attention on intangible risks as business models pivoted. But getting a firm grasp of the data remains a serious challenge.

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90% of the value of S&P 500 companies are now made up of intangible assets

The increasing intangible nature of the risk landscape is nothing new, and yet many of the exposures facing businesses today remain misunderstood and poorly served by traditional insurance products.

On 22 February, *StrategicRISK* hosted a webinar 'Evolution of risk – from the tangible to the intangible' to discuss some of these challenges. Chaired by *StrategicRISK* editor Helen Yates, our expert panel consisted of Riskonnect CEO Jim Wetekamp, group insurance manager at Next Group PLC Martin Smyth and risk consultant Mark Boult.

Latest studies show that intangible assets make up over 90% of S&P 500 companies, up from just 17% in 1975. With the pandemic seeing a further shift in business models, with organisations divesting of business premises, moving systems to the cloud and repurposing supply chains, the trend

has further accelerated over the past two years.

"It is important not to be left behind in a world where an increasing proportion of business value is made up of intangible assets," warned Bout. "If you are behind the curve, you aren't going to be managing your risks as well, and therefore things will go wrong and damage your brand value."

The webinar considered the value of intangible assets and how changing priorities during the COVID crisis have seen a growing appreciation for digital infrastructure, intellectual property and talent, brand and reputation, and corporate culture, among other things. As organisations shift further towards hybrid working patterns and become ever more digitised, our experts considered how risk professionals can better measure, manage and mitigate intangible risks?

A MANAGER FOR EVERY RISK

The discussion began with a look back at how the COVID crisis had elevated attention to intangible exposures and highlighted the need for resilience in an increasingly uncertain and volatile risk environment. "What has changed is an appreciation that risk is distributed across the business," said Smyth. "Everybody in the business is a risk manager of some sort, even if they don't see themselves that way."

Wetekamp noted that different stakeholders were being brought into the risk management process than may have been in the past. This includes HR, legal and marketing teams where risks involving people, intellectual property and brand are concerned, for instance.

"The business continuity and operational resilience point is something that has risen to the top in the discussion [on the importance of risk management] and it is impacting the way we work. Linking to the intangible asset aspect, it has brought new stakeholders into the risk management process that you didn't have before or that you have to engage in a different way."

"You've got to make sure you have a defined risk owner for each one of the intangible assets or areas of risk," he said. "This will create discussion internally around how those things come together from a scenario standpoint."

As organisations become more reliant on digital ecosystems, with the pandemic driving a further shift from server-based systems to cloud-hosted architecture, it is essential for risk teams to have a direct line into the CIO and IT function. Panellists acknowledged there is no turning back and that it was imperative to keep abreast of new and emerging vulnerabilities as threats, including ransomware and supply chain attacks, continue to evolve.

A question was raised about cloud concentration and how this introduced the potential for risk aggregations.

"Aren't we there already?" asked Wetekamp. "If you're worried about how much of our critical business operations, data and processes are being consolidated in the digital experience, I would argue we're over that threshold now. There are four or five systems or platforms that if they had a material interruption (and Twitter is not down) we know it about it within seconds. That has massive impacts on commerce, the flow of data, procurement and supply chains."

"It is less about whether that is going to emerge as a risk and more about, what are some of the strategies we're going to employ a little bit differently. Coming out of COVID, we still have very traditional procurement practices. Should we think about alternative vendors and distributing our relationships a

"WHAT HAS CHANGED IS AN APPRECIATION THAT RISK IS DISTRIBUTED ACROSS THE BUSINESS. EVERYBODY IN THE BUSINESS IS A RISK MANAGER OF SOME SORT."

Group insurance manager, Next Group PLC
Martin Smyth

bit more? Traditional risk mitigation around supply chain and getting our product out the door apply in this context."

MOTIVATIONS FOR ESG

Inevitably, ESG-related risks formed a significant part of the discussion, given how attention to environmental, social and governance factors has elevated the importance of intangible assets, including people, IP and the natural world. Doing the right thing – and being seen to do the right thing in a world where stakeholder capitalism is becoming the norm – is also intrinsically connected to brand value and reputation.

As investors, regulators and other stakeholders ramp up their expectations on the ESG front, including new reporting requirements, organisations are under growing scrutiny. The climate scenario testing requirements under climate frameworks such as TCFD do present a role for the insurance industry, thought Smyth. "Brokers, carriers and other service providers have got a wealth of knowledge in being able to quantify what that risk looks like to the business, which in some cases can be intangible."

"Going through these types of exercises, you begin to see how ESG as a risk of a business is made up of a lot of component risks – some of which are physical, but many of which are not," he continued. "It's great to be able to quantify it, but I don't think at this time much of it is transferable outside of the physical world and that's somewhat concerning."

The broad nature of risks and opportunities that fall under the banner of ESG is a challenge in and of itself. Organisations are having to think about the impacts they have as a business and their responsibilities to the world around them in a completely different way than ever before. And there is no room from greenwashing or clever marketing tricks.

"ESG is making you think about the whole life cycle of a product – the whole beginning to end of your supply chain of an extended enterprise. Although you can control things that you physically manage or do yourself, and that gives you some intangible value, it can be degraded by something happening upstream or downstream in the process," Smyth said.

"That's not necessarily going to be a physical thing – it could be related to diversity, pollution, ethics. All those things may impact your intangible value and then people stop buying from you," he continued. "The risk manager has to look over the much bigger picture and think not just about the financial impact, but also how society and other stakeholders will view what you're doing."

PREPARING FOR THE NEXT SHOCK

The pandemic once again highlighted the interconnected nature of risk in the world we live in, with COVID-19 and country lockdowns exacerbating a broad range of business risks, including supply chain disruptions and cyber vulnerabilities. The sheer complexity of this risk landscape was brought to life in the charts of this year's World Economic Forum's Global Risk Report, published in January 2022 (www.weforum.org/reports/global-risks-report-2022/data-on-global-risks-perceptions#report-nav). Yet, at the time of writing, even that feels out of date.

Speaking as the Ukraine crisis was unfolding, Smyth noted that ahead of the pandemic, Black Swan-type events had, in many instances, been consigned to the history books. Now corporates are carrying out more scenario analysis to consider the impact of other potential shocks, however unlikely they may at first appear.

"It is important to take an open-minded approach to these risks. We've all been in meetings where someone has discarded what could be a valid scenario or approach just because they didn't believe it could happen in that way. And that's quite a dangerous narrative to have within the ERM framework."

Events that lie outside of "living memory" are the ones that can blindside. "Global pandemics seem to happen about once every 100 years, and we should know to expect this," said Boult. "Other scenarios will happen on some sort of regularity. You need to look at the future and think about a range of different types of impact, how you manage similar types of risks and build in resilience."

OUT OF REACH?

The esoteric nature of intangible risks inevitably makes them difficult to measure and quantify. But there are ways of overcoming these challenges. "One of the really good exercises is to look at events that have happened and see where they fit into your risk universe, where the tolerances were and were they material," said Smyth.

Wetekamp pointed to the financial services and healthcare sectors as examples of industries that are pioneering approaches to generating data around intangibles risk. "These two markets are the canary in the coal mine in terms of what other organisations will try to do around more effectively managing risk," he said.

"Is it really true we don't know how to value our intangible assets?" he asked. "There are some quantifications you can do in this area that are really physical and specific, around our operational resilience and even how we source and procure and what third parties we work with. All of those things are really trackable."

"For a long time, organisations have measured and understood consumer sentiment and acted and behaved accordingly to protect their brand and grow their business. Employee sentiment surveys record what makes people happy, excited and mission-driven."

"It's the investor sentiment – how it impacts ESG investing, stock price and future performance – that is now making the gamble on this highly unpredictable," added Wetekamp. "It's a future benefit that we can't quantify that has changed the way we talk about ESG and intangible risks today." **SR**

"IS IT REALLY TRUE WE DON'T KNOW HOW TO VALUE OUR INTANGIBLE ASSETS? THERE ARE SOME QUANTIFICATIONS YOU CAN DO IN THIS AREA THAT ARE REALLY PHYSICAL AND SPECIFIC."

CEO, Riskonnect
Jim Wetekamp

Do you know your value chain?

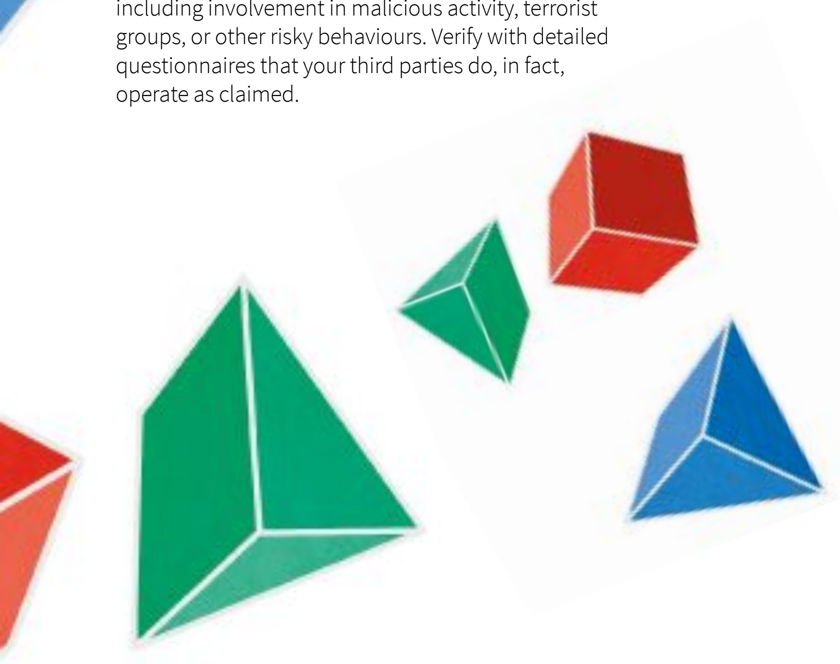
How well you respond to geopolitical risks depends on both your own decisions and those of third parties. So how do you monitor behaviour and standards across your value chain, asks Riskonnect's Jim Wetekamp

Intangible risks, like geopolitical risks, can have a deep impact on business. Immigration and travel restrictions can limit availability of talent and key skill sets. Slow response to social issues or the suspicious activities of third parties overseas could lead to reputational consequences. Trade conflicts, tariffs, and sanctions threaten supply-chain performance. Recessions, inflation, and economic uncertainty can slow revenue growth.

Each of these situations can have a severe impact on an organisation. Together, however, the impact could be devastating for those that haven't properly prepared.

An organisation's resilience to geopolitical risks heavily depends on third parties. One poor decision by a vendor can poke holes in the defences you've worked hard to build. Do your due diligence before the contract is signed to ensure you only engage with trusted vendors that meet your standards and uphold your values.

And make sure you're not associating with any vendors that may cause harm to the company, including involvement in malicious activity, terrorist groups, or other risky behaviours. Verify with detailed questionnaires that your third parties do, in fact, operate as claimed.



"ONLY ENGAGE WITH TRUSTED VENDORS THAT MEET YOUR STANDARDS AND UPHOLD YOUR VALUES"

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Jim Wetekamp

THE NEED FOR INSIGHT-LED DECISIONS

Confident, fast decision-making can minimise geopolitical disruption. And your ability to respond quickly requires facts – not gut feelings or educated guesses. One overlooked threat – minor as it may appear –could trigger a series of events that add up to catastrophe.

Technology is instrumental in creating a complete and contextual view of an organisation's risk environment. The right software centralises risk data from across the organisation, connects the dots between risks, and makes the information actionable. You'll have a clear view of how one risk could ripple through multiple areas – e.g., reputation, competitive position, strategic growth – and what you need to do to prepare.

We've all learned a lesson over these past couple of years about the perils of disregarding even the most unlikely scenarios. No one wants to be caught off guard by an unanticipated geopolitical risk. What can you do now to strengthen your infrastructure to withstand a new wave of threats? Because that next event may be already be on its way. **SR**

Ukraine reawakens business to the importance of political risk

The conflict calls for a strategic re-evaluation of footprints, supply chains, relationships, company cultures, business functions and risk appetite, explains Control Risks' Claudine Fry

The catastrophic events in Ukraine have shattered such assumptions, and left businesses no option but to respond quickly and decisively. While the immense human suffering is front of mind, the impact of the conflict in Ukraine on business has been deep and wide. There have been almost-immediate impacts on the safety of people, the resilience of supply chains, sanctions risk exposure and the operational costs associated with rising commodity prices.

Countless companies have had to cease or suspend operations in Russia, the 11th largest economy in the world. Businesses are also trying to understand the impact of these events beyond the immediate term as it is clear their legacy will be lasting.

No sector will go untouched. No part of the world will escape the effects, be they rocketing prices for food and oil; pressures on services and politics caused by migration; changed inflows and asset seizures influenced by sanctions; or a change in access to resources or influence.

WIDESPREAD RISK IMPLICATIONS

The pace of developments will slow, but watch for things that may suddenly change the pace. Europe will be living with active conflict of some kind on its soil long-term. The status of Ukraine will remain contested and the security situation in and around Ukraine will be hostile. Key relationships between impacted states will remain belligerent, combative and militaristic.

Beyond the immediate neighbourhood of Ukraine, societies and businesses have only just begun to feel the implications of this crisis. These implications will manifest in higher political risk, everywhere.

The succession of events such as Brexit, the election Donald Trump as US President, the pandemic, and now Ukraine, make it clear that political risk events typically seen as low likelihood but high impact demand closer attention by the board, and more engagement beyond the board too.

BUSINESSES ARE BEING HELD TO ACCOUNT FOR THEIR RESPONSE TO POLITICAL RISK EVENTS. THE RUSH OF WESTERN COMPANIES FLEEING RUSSIA IS TESTAMENT TO THIS TREND.

Claudine Fry, principal, Control Risks

For some businesses, there will need to be a strategic re-evaluation of footprints, supply chains, relationships, company cultures, business functions and risk appetite to ensure resilience in a world profoundly changed by the Ukraine conflagration.

Organisations are operating in a world reawakened to the significance of understanding and managing political risk. What is more, businesses are being held to account for positions they are taking in response to political risk events more than ever before. The rush of Western companies fleeing Russia is testament to this trend.

Adopting a position on a geopolitical risk issue can be complex and consequential in ways that may not be immediately well-understood. It requires careful consideration, particularly for global companies doing business in an increasingly polarised and hostile international environment. **SR**

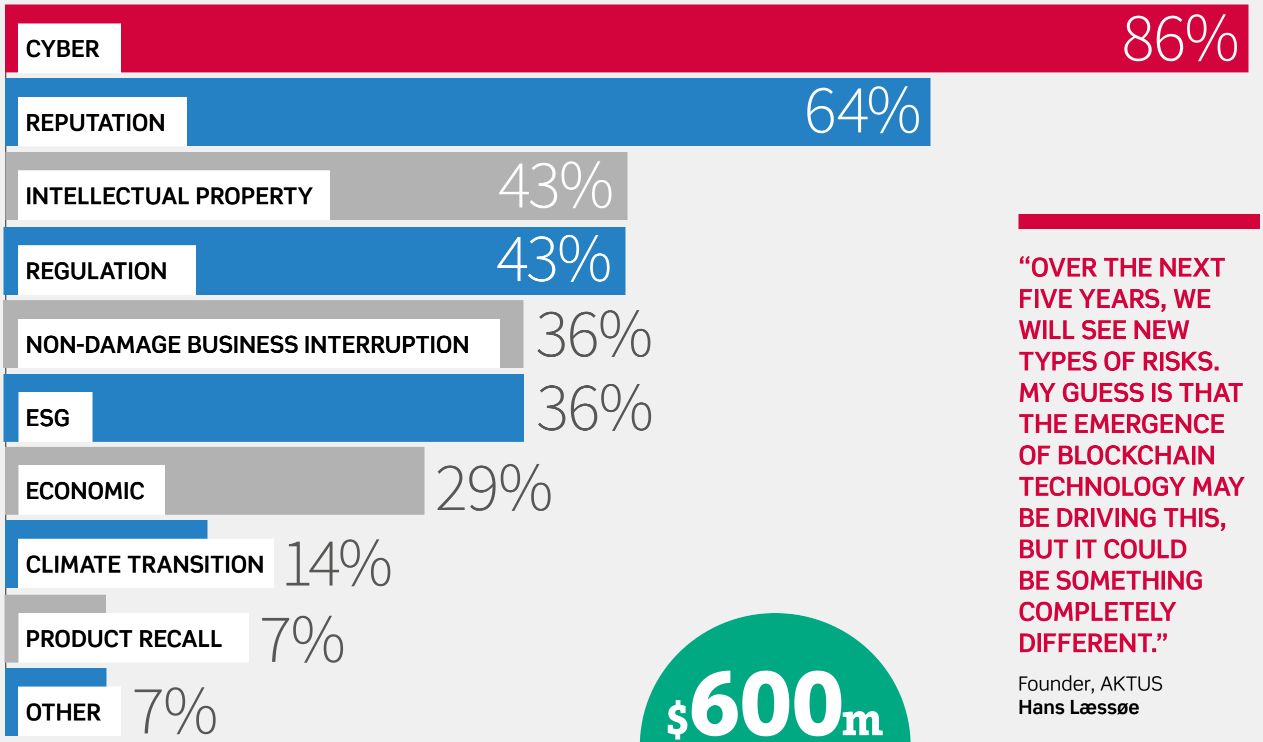
Claudine Fry is principal at Control Risks

In partnership with riskonnect

Cyber and reputation: your top intangible fears

Cancel culture and cyber intrusions can 'kill', and survey respondents know this. Many anticipate more red tape as regulators seek to get a handle on these ever-growing emerging risks.

WHAT INTANGIBLE RISKS/EXPOSURES ARE OF MOST CONCERN TO YOUR ORGANISATION? (CHOOSE UP TO THREE)



"OVER THE NEXT FIVE YEARS, WE WILL SEE NEW TYPES OF RISKS. MY GUESS IS THAT THE EMERGENCE OF BLOCKCHAIN TECHNOLOGY MAY BE DRIVING THIS, BUT IT COULD BE SOMETHING COMPLETELY DIFFERENT."

Founder, AKTUS
Hans Læssøe

$600m
Cost to businesses of the top ten cyber intrusions in 2021

Eighty-six percent of respondents said cyber was the intangible risk of most concern to their organisation in 2022. This is according to a survey of risk professionals carried out by *StrategicRISK* in February.

It was followed by reputation in second place (64%) and intellectual property and regulation in joint third position (43%) and non-damage business interruption (NDBI) and ESG in joint fourth (36%). Fifteen percent of respondents said they had suffered a major loss over the last 12 months relating to an intangible risk.

The impact of cyber attacks on organisations – including costs relating to network disruption – are clearly front of mind when it comes to intangible exposures.

And it is not difficult to see why. The top ten intrusions in 2021 costs companies over $600m, resulted in the loss of tens of millions of sensitive data records and shut down one back for over a week, according to research by Tokio Marine HCC International.

As for reputation, one does not have to look much further than current newspaper headlines to see why risk managers are wary of how suddenly hard won reputations can be lost.

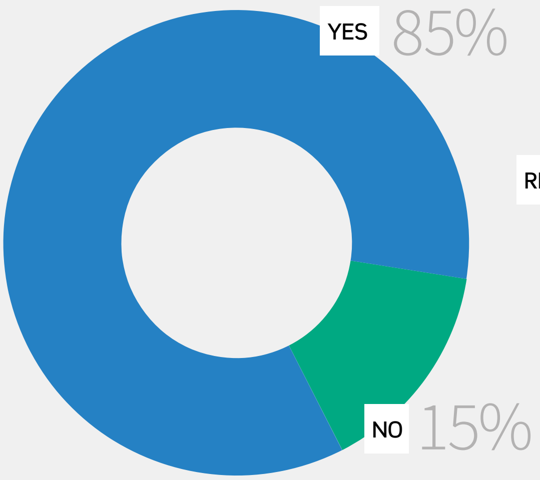
REAL THREAT OF CANCEL CULTURE

AKTUS founder and former LEGO Group chief risk officer Hans Læssøe is not surprised that reputation ranks so highly among the list of concerns.

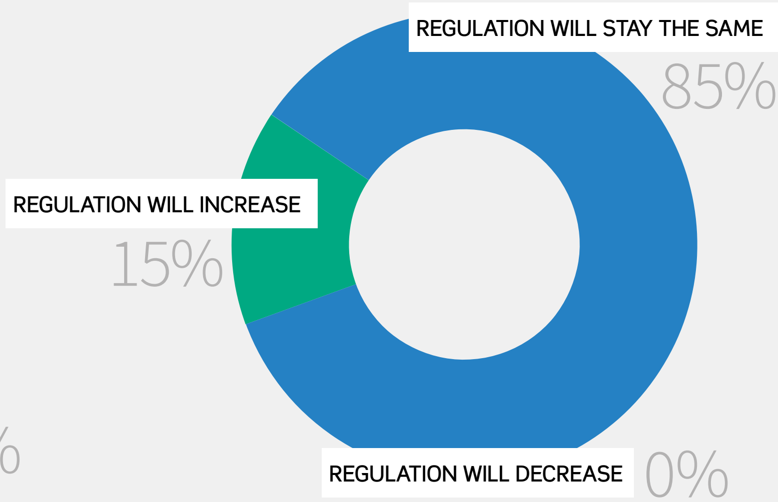
As he explains, a dented reputation may 'kill' the organisation and is complicated for the following reasons:

- A risk may materialise due to change of consumer perceptions (think of the #MeToo movement) rather than due to change of behaviour.
- A risk may materialise based on some untrue accusations made by someone who is 'out to get you'. "I had an example of that while at the LEGO Group, where activists were trying to influence a partner company to change behaviour and (unsuccessfully) leveraged the LEGO Group as a means to the end," says Læssøe.
- A risk may materialise based on the bad behaviour of one 'rogue' person/executive or person you relate to (think Spotify right now).
- A risk may materialise while adhering to legislative controls, which appear to be inefficient or

HAS YOUR ORGANISATION **SUFFERED A MAJOR LOSS** OVER THE LAST 12 MONTHS RELATED TO AN INTANGIBLE RISK?



HOW WILL CONCERNS OVER THE SYSTEMIC NATURE OF INTANGIBLE RISKS IMPACT **REGULATORY REQUIREMENTS** GOING FORWARD?



inadequate (for example, money laundering through a bank).

Respondents acknowledged the global pandemic had exacerbated some of the intangible risks faced by their organisation. This includes exposures relating to new, hybrid ways of working and the direct and indirect business interruption resulting from company lockdowns.

CREATING A SCALE

According to Læssøe, however, pandemic is a tangible risk that materialised, and one that companies should have been prepared for.

Many are taking steps to better measure and manage their intangible exposures going forward, particularly in the absence of traditional insurance solutions.

In order to manage the risk, you first must be able to measure it. But with intangibles, other metrics are often needed. "The key challenge is to rate/scale it," says Læssøe. "Let us take reputation for one, and apply a 1–5 level scale:

- Local press and public attention for less than one week. Very limited social media attention.
- Nationwide press attention for less than one week and/or local attention for two to three weeks. One to two weeks of some social media attention.
- International press attention, locally the issue lingers on for months and international social media attention exceeds two weeks.
- International headline press attention. Significant and 'global' social media attention for weeks.
- International top story. Massive social media 'outrage' for weeks and weeks on end."

"MORE TYPES OF RISKS WILL EMERGE AND THE COMPLEXITY WILL INCREASE AS COMPANIES, SUPPLY CHAINS, BUSINESSES AND PROCESSES GETS INTERTWINED AND AUTOMATED – ALL LEADING TO REDUCED TRANSPARENCY."

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The vast majority of respondents (85%) thought the systemic nature of intangible risks would impact regulatory requirements going forward. As ESG grows in importance and supervisors address the systemic nature of cyber and pandemic-related risks, more rules and requirements appear likely.

Fifteen percent thought the level of regulation would stay roughly the same, but nobody thought oversight would reduce any time soon.

IT'S ONLY GETTING MORE COMPLEX

As for the future, respondents said firms must get better at anticipating emerging intangible risks and integrating these into their strategic risk management frameworks.

"More types of risks will emerge and the complexity will increase as companies, supply chains, businesses and processes gets intertwined and automated – all leading to reduced transparency," says Læssøe.

"Suddenly, the 'butterfly effect' may come very much into play in business. For example, there is currently a shortage of specific materials, which in turn creates a shortage of computer chips being manufactured, which stalls the sale of new cars. If I were a car manufacturer, I may not consider the shortage of chip materials as being a risk to my ability to sell cars – but it is."

"Over the next two to five years, we will probably see new types of risks for the first time ever – some we have never thought about," he adds. "My guess is that the emergence of blockchain technology and metaverses may be driving this, but it could also be something completely different." **SR**

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