

# **Resilience – a first line of defence**



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2020 is likely to be another unpredictable year for businesses, reinforcing the need to build business resilience and develop more dynamic and insightful risk management, according to Cécile Fresneau.

## Overview

The course for 2020 is set to be a year of heightened unpredictability. 2019 will close with the UK general election but Brexit uncertainty is likely to persist with tough trade talks ahead and the risk of a no deal departure hanging in the air. Next year, US President Donald Trump will fight to win another term in office, while US trade wars with China and the EU continue to stymie global trade and economic growth.

According to QBE's Unpredictability Index, we are due another year of heightened uncertainty. Our study showed that periods of unpredictability come in five-year cycles. Driven by the financial crisis and a rise in political volatility, two of the most unpredictable years for business occurred in 2000 and 2005, according to the Index.

Overall, the QBE Unpredictability Index analysis found the world

has become a less predictable and more volatile place. Levels of uncertainty are increasing, in large part a reflection of the pace of change and with growing complexity and ambiguity. The message for business is that they can no longer rely on the defences of the past. They need to become more resilient and more forward-looking; develop new approaches to risk management, prevention and mitigation.



## Unpredictable future

While political and economic factors have driven recent unpredictability, even bigger challenges may lie ahead, with far reaching, yet difficult to predict consequences.

Take climate change. Extreme and unpredictable weather is already becoming more common. The last two years have seen record storms, wildfires and heatwaves around the world, yet our ability to curb emissions and temper climate change is far from certain. The recent annual UN emissions gap report shows that rich countries are not cutting emissions fast enough, yet greenhouse gases reached new highs in 2018, according to The World Meteorological Organization.

The transition to a low or zero carbon economy will also be fraught with uncertainty. Achieving carbon emission reduction targets will require massive investment and significant changes in transport, energy, agriculture and lifestyles.

Technology is another factor radically changing business models and consumer behaviour. Artificial intelligence, for example, will power autonomous vehicles, smart cities and factories,

but it will also have unknown implications for workers and regulation. Adding to the mix are demographic changes. The world's population continues to grow, age and urbanise, with unpredictable societal, political and economic implications.

Individually, these issues would be challenging enough for any business to navigate successfully. However, one of the most interesting findings of the QBE Unpredictability Index is the interconnected nature of drivers and growing complexity – factors that amplify volatility and make for yet more unpredictability.

### The Unpredictability Index

A report detailing the research powering the Unpredictability Series.

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## Changing exposures

The implications of growing unpredictability for business are many and varied. Unpredictability could lead to more volatile earnings, with uncertain demand and potentially higher costs. For example, Brexit has increased costs in the supply chain, reduced consumer demand and affected the supply of labour in certain industries, such as healthcare, food production and agriculture.

Climate change is already exposing assets and supply chains to more intense storms, floods and rising sea levels. The C40 – a network of the world's megacities committed to addressing climate change – estimates that global warming would lead to at least 570 cities and some 800m people affected by rising seas and storm surges by 2050.

Sectors, such as agriculture, energy, air transport and consumer goods,

could face rapid changes in demand as consumers look to minimise their environmental impact and reduce emissions. Changing consumer behaviour could make some goods and services obsolete overnight.

New technologies will also bring new risks, such as cyber security, as well as big changes in regulation – advances in AI are already testing privacy regulations and ethics. Climate change is also likely to

lead to new policies and regulation. For example, climate change reporting requirements or caps on emissions for shipping and airlines, or taxes and incentives to wean people away from fossil fuels and adopt alternatives, such as electric vehicles or public transport.

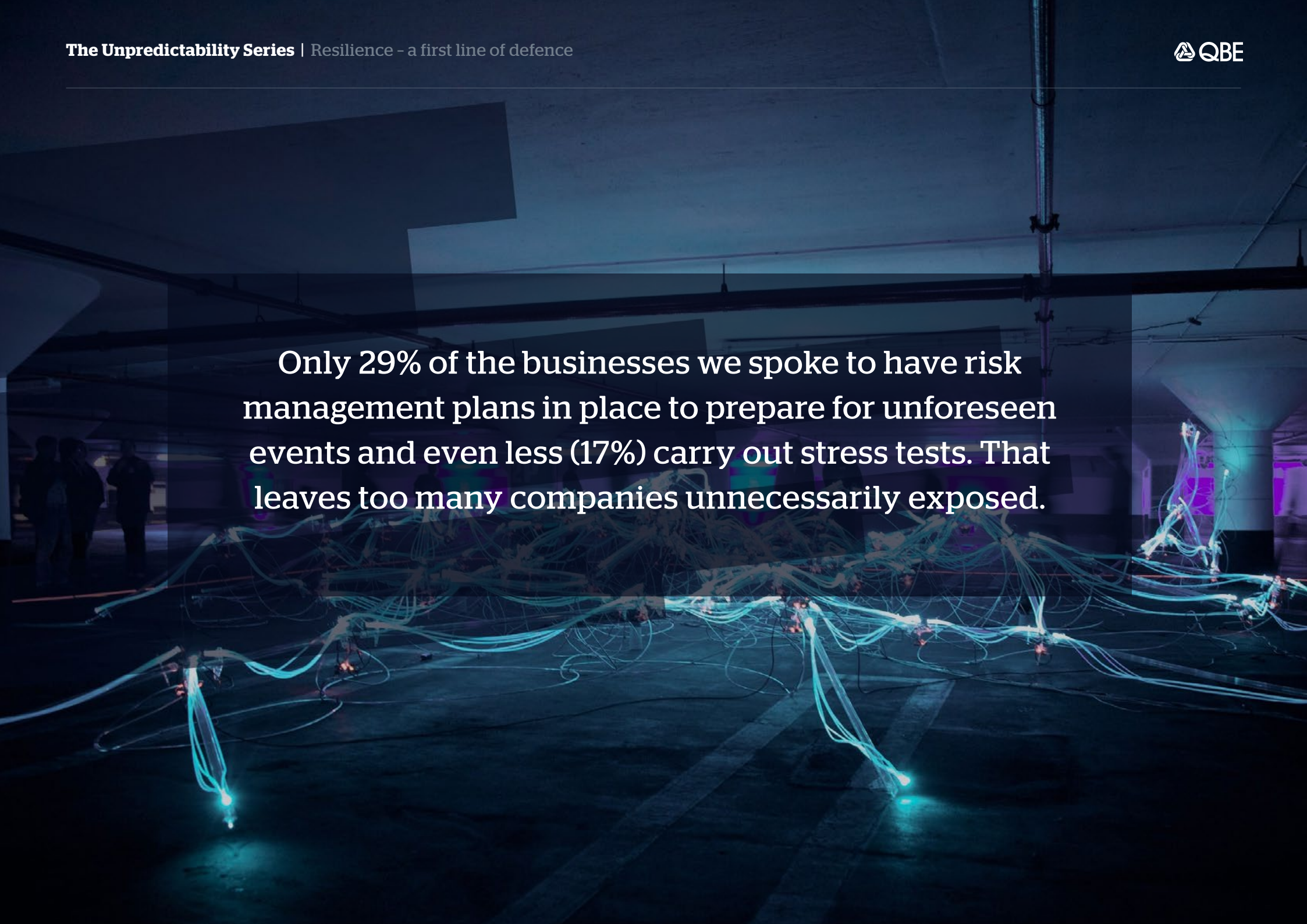
Just as the business operating environment is becoming more complex, regulations, governance and reporting requirements are increasing. Businesses and their senior managers are being held more accountable for their actions, evidenced by increased litigation and regulatory scrutiny for companies and their directors. Stakeholder expectations of corporate behaviour and ethics are also changing – investors and

lenders are shying away from industries linked with fossil fuels while consumers are quick to react to perceived injustices, such as the use of slave labour in the supply chain or environmental issues like single use plastics.

Businesses will need to keep an open mind to new risks. Whether adapting to climate change or adopting new technology or business models, there are likely to be unintended or unpredictable consequences. Even actions to mitigate risk – such as new building codes or construction materials aimed at tackling climate change - could themselves create unexpected exposures.



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## Better prepared

Despite growing unpredictability, businesses of all shapes and sizes are not as well prepared as they could be. Only 29% of the businesses we spoke to have risk management plans in place to prepare for unforeseen events and even less (17%) carry out stress tests. That leaves too many companies unnecessarily exposed.

Even though unpredictable events are typically out of a company's control, that does not mean they can't prepare. A strong corporate risk culture, for example, can guide employees as they face difficult decisions and situations while a resilient business and supply chain will be in a far better position to manage periods of unpredictability.

Companies need to take a critical look at the where risk management fits into the board level agenda. Is it a tick box exercise or a core part of the strategic agenda? Risk is often viewed and reported on through a fixed process, considered by the board as an agenda item for just a few hours each quarter or just once a year. However, risk management



# 17%

**of businesses carry out stress test for unforeseen events**

has a critical role to play in assisting companies with growing unpredictability. Increased volatility and uncertainty will require a more in-depth conversation around risk, supported by modelling, scenario planning and more granular information.

As boards come under more scrutiny, they are likely to want to get closer to the business and more hands on. They will

also increasingly require more information on risk, which will raise expectations on the risk function. In particular, boards will want to better understand risk and business resilience in the context of scenarios. They are also likely to seek a longer term view, obtaining insights into risks and opportunities beyond the traditional quarterly or annual reporting cycles.

In response, business risk management will need to become a more dynamic and embedded process, not just an annual exercise to fulfil corporate governance requirements. There is huge potential for risk professionals that can help boards and their

companies look ahead and anticipate risks and opportunities, and that can shed light on interdependency and complexity.

The role of the CRO and the risk manager can bring real value to a business, especially where they can support a discussion on risk and integrate risk management into the business model and strategy. The risk function should also be strategic, assisting the board when identifying and assessing the business opportunities that inevitably arise from disruption.

## QBE Risk Solutions

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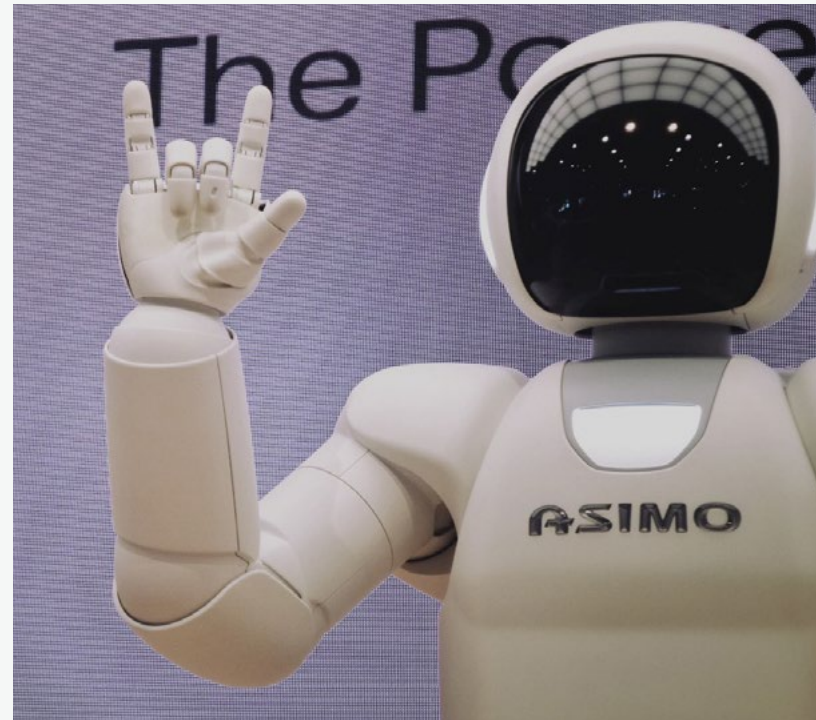
## Conclusion

Unpredictability is here to stay. Looking ahead, it is clear businesses will need to find better ways of operating in an uncertain and volatile environment. New technologies like AI and major challenges like climate change and an ageing population will have profound implications with economic, political and social ramifications that will be difficult to second guess.

In such a world, businesses and their leaders will not be able to rely on the defences of the past. They will need to develop new skills and tools to identify, understand and mitigate risk, and they will need to be open to collaboration. Many of the emerging challenges – such as mitigating the effects of climate change or protecting complex digital supply chains – will

require organisations to work in partnership and build collective resilience. As an insurer, we are already investing in technology to provide customers with insightful information on risk and loss prevention services.

Risk will not go away, but it will change. The best we can do is be informed, prepare and be resilient.



## Keep in touch

If you haven't already signed-up to receive the Unpredictability Series you can do so at

**[www.QBEurope.com/unpredictability](http://www.QBEurope.com/unpredictability)**

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