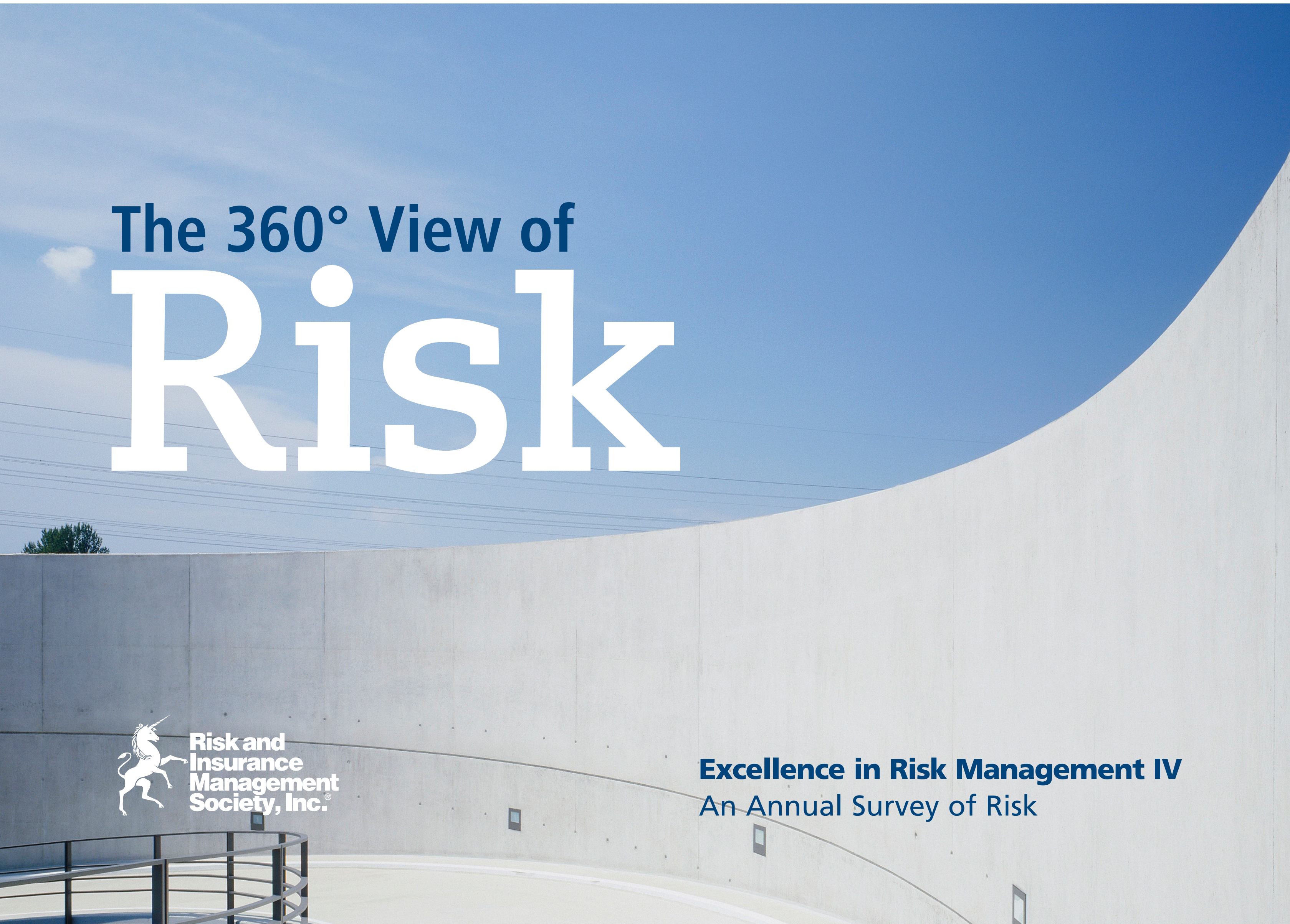
MARSH

MARSH MERCER KROLL
GUY CARPENTER OLIVER WYMAN

The 360° View of Risk



Risk and Insurance Management Society, Inc.®

Excellence in Risk Management IV

An Annual Survey of Risk

Foreword

For nearly a year, the global economy has suffered the fallout from what started as a meltdown in the U.S. subprime lending markets. What might the crisis have looked like if it hadn't caught so many companies off guard? Would the risks have spread so wide if more firms' risk management radars had provided top executives with a 360-degree view of risk? Hindsight says much of the damage could have been avoided or mitigated. When it comes to risk management, however, foresight trumps hindsight.

Most of the information for this edition of the *Excellence in Risk Management Survey* was collected before the credit crunch began. But the subprime crisis provides an exclamation point to our survey findings: It's increasingly important for risk managers and other executives to see the whole picture—to have a 360-degree view of risk.

The good news is that most professionals we surveyed said they want to be more strategic risk managers. There is awareness that from the C-suite to the risk management trenches companies need people who can expand their views of risk. For example, if cyber thieves steal customers' personal data, plans should already be in place that set in motion a chain of events from plugging security gaps to making customers whole. If a product should fail, risk management needs to be ready to execute the recall, work with regulators, and help fix the brand. Companies need forward thinking on risk issues ranging from terrorism to pandemic to climate change and on through risks not yet thought of.

The number of companies moving along the path to strategic risk management continues to grow. But getting to a point where a company's risk management approach is truly strategic will require cooperation and a shared vision among risk managers, C-suite executives, and others. As you'll see in the following pages, some of that shared vision exists now, while in other areas work remains.

This is the fourth year that the Risk and Insurance Management Society, Inc. (RIMS) and Marsh have jointly crafted and sponsored the *Excellence in Risk Management Survey*, a quantitative survey of RIMS members and others. The results were presented as part of the "Excellence in Risk Management IV" session at RIMS 2007 Annual Conference & Exhibition in New Orleans. Significant help was also contributed this year by Financial Executives International (FEI). TNS, a premier strategic-consulting and research firm, conducted the 2007 survey. We offer our sincere thanks to all who took part in the survey.

Janice Ochenkowski
President
RIMS

Tim Mahoney
President, Global Risk Management,
Marsh

The 360° View of Risk

Excellence in Risk Management IV An Annual Survey of Risk

An Annual Survey of Risk Management Issues and Practices

Editor
Tom Walsh
Marsh Inc.

Art Director
Thomas Branco
Marsh Inc.

Designer
Rich Metter

Review Panel
Mark Bates, Marsh Inc.

Brian Elowe, Marsh Inc.

Fiona Gibbs, Marsh Inc.

Lisa Kremer, Marsh Inc.

Felicia Messimer, RIMS

Pamela Rogers, Marsh Inc.

Mary Roth, RIMS

Richard Waterer, Marsh Inc.

Executive Summary

The number of U.S. companies implementing enterprise risk management (ERM) continued to increase in 2007 as firms sought to fulfill their goals of becoming more strategic in their approach to risk. Most companies—75 percent—believe they need to take a more strategic approach to risk management, yet few companies—only 15 percent—consider their current approach strategic. Potential changes by the major credit rating agencies could propel even more companies to adopt ERM/strategic risk management measures.

Key findings in our *2007 Excellence in Risk Management Survey* were:

- 75 percent of U.S. firms said their senior management would not be able to give a satisfactory answer to questions ratings agencies might have about their risk management approach. The more strategic a company's risk management approach was, the more likely it could meet the ratings agency challenge. But even among self-identified "strategic" firms, nearly half could not provide a satisfactory answer to three basic ratings agency questions. For example, nearly two-thirds of firms believe their senior management cannot say how much they are willing to lose from various risks and still meet financial goals.
- The number of U.S. firms saying they have fully implemented enterprise risk management (ERM) tripled to 12 percent in 2007 from 4 percent in 2006.
- There are marked differences in how strategic risk managers view the importance of risk compared to how traditional risk managers view it. Those with a strategic approach ascribe more importance to more risks, particularly in the broad areas of operational, strategic, and financial risks.
- When asked to assign a rank to risk management leadership within their companies, risk managers, CFOs, and CEOs all placed themselves in the No. 1 position. Risk managers and CFOs both ranked the CEO No. 2. Risk managers tended to place more importance on hazard risks than did their C-suite counterparts. C-suite executives and risk managers ranked brand and reputation as their firms' top exposure areas.
- Internationally, risk management is moving toward a strategic viewpoint, although not as quickly as in the United States. There appears to be a feeling in many countries that risk management responsibility should rest at the board level.

Levels of Risk Management

From the beginning of the *Excellence Survey* series, we have been interested in the approach to risk management favored by risk practitioners and others in their organizations. We have categorized the various approaches as traditional, progressive, or strategic. Where an individual or organization falls in these categories depends on such things as their own skill sets, trends in their industry, availability of resources, or a combination of these and other factors. The illustration below provides an explanation of these three levels of risk management and some of their associated functions and best practices.

Traditional Risk Management

- Risk Identification
- Loss Control
- Claims Analysis
- Insurance and Risk-Transfer Methods

Traditional risk management involves many long-established, routine functions. These include identifying risk, using various risk-control measures to eliminate or mitigate loss, analyzing claims and claims trends, and handling the details of insurance and other risk-transfer methods.

Progressive Risk Management

Traditional +

- Alternative Risk Financing
- Business Continuity
- Total Cost of Risk
- Education and Communication

Progressive risk management encompasses all of the concerns of traditional risk management, but adds alternative risk financing (such as self-insurance, captives, and risk-capital products), business-continuity planning, measurement of the total cost of risk (TCOR), and education of and communication with the rest of the organization about risk and its management.

Strategic Risk Management

Traditional +

Progressive +

- Enterprise-wide Risk Management
- Indexing of Risk
- Use of Technology

Strategic risk management goes further still, incorporating all of the areas that fall in both traditional and progressive risk management, but adding the C-suite view of the totality of risk. The practitioner of strategic risk management views risk as something to optimize, not just to mitigate or avoid, taking an enterprise-wide view of risk. Risk is indexed against the organization itself, year-over-year, and against competitors. And risk management information systems (RMIS) and other technologies play a large role in managing risk.

These three approaches to risk management—traditional, progressive, and strategic—will be at the center of the discussion throughout this report.

Note: While strategic risk management does not equal enterprise risk management, we view the two as being largely synonymous: A corporation cannot really be said to be managing risk strategically if it does not embrace the principles and practices of ERM.

U.S. Results

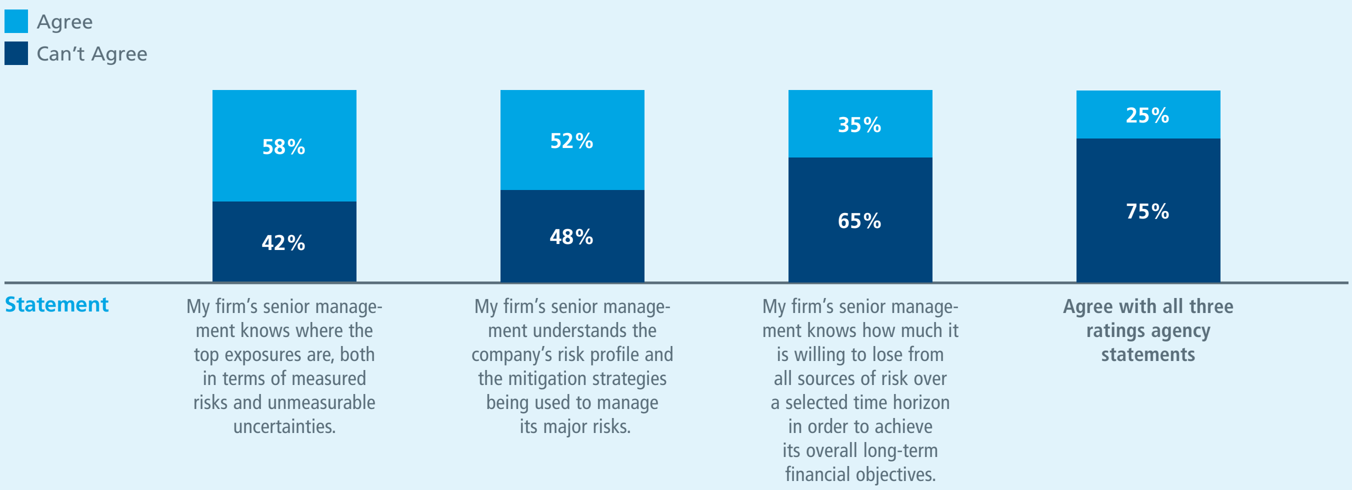
A Challenge from the Ratings Agencies

What if a company's credit rating depended in part on the way it approached risk management? Would the potential financial gain from adopting a more strategic viewpoint—and a penalty for not—motivate companies to practice enterprise risk management (ERM)?

The questions stem from moves underway at the major credit rating agencies to incorporate risk management measures into their analyses. Standard & Poor's, for example, has said it plans to "introduce enterprise risk management analysis into the corporate credit ratings process globally as a forward-looking, structured framework to evaluate management as a principal component in determining the overall business profile. (The business profile, along with the financial profile, are the key factors of a Standard & Poor's credit rating.)"[1] Other ratings agencies have also said they are evaluating the use of ERM analysis in their models.

S&P has said changes in a firm's ERM profile would "potentially drive rating and outlook changes before the consequences are apparent in published financial results."[2] And yet, an eye-popping 75 percent of U.S. firms in our survey said their senior management would fail to answer a set of basic questions from the ratings agencies.

Ratings agencies are starting to push firms to strategic risk management



[1]Criteria: Request For Comment: Enterprise Risk Management Analysis For Credit Ratings Of Nonfinancial Companies, Nov. 15, 2007, www2.standardandpoors.com

[2]Ibid

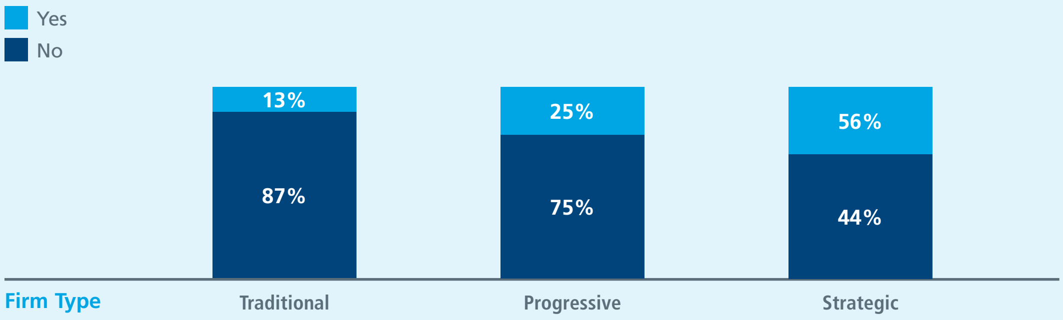
Our survey looked at three key statements that the agencies say companies should be able to answer affirmatively. Only one in four respondents was able to answer "yes" to all three questions.

Although these are not verbatim questions from any one ratings agency, experts at the agencies agreed the following questions were representative of areas they were considering using in their analyses:

1. My firm's senior management knows where the top exposures are, both in terms of measured risks and unmeasurable uncertainties.
2. My firm's senior management understands the company's risk profile and the mitigation strategies being used to manage its major risks.
3. My firm's senior management knows how much it is willing to lose from all sources of risk over a selected time horizon in order to achieve its overall long-term financial objectives.

We then looked at the answers through the lens of whether the respondents had identified their firm as traditional, progressive, or strategic. The farther down the strategic path a company said it is, the more likely it was to answer "yes" to all three statements. Even though the number of strategic risk practitioners answering "yes" was much higher than respondents in the other two categories, it should still cause concern that 44 percent of self-identified strategic firms were unable to affirm all three statements. Even strategic firms, it seems, have ground to cover.

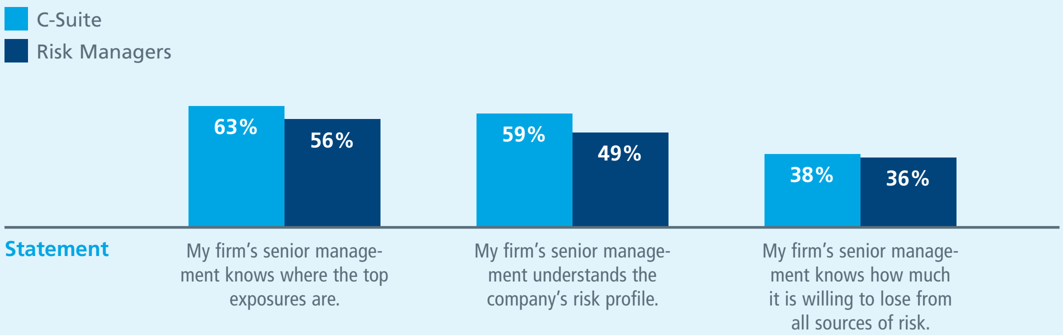
The farther down the strategic path a company said it is, the more likely it was to answer "yes" to all three statements.



It's also interesting to step back and consider the questions apart from their possible use by the credit rating agencies. A large swath of senior managers are viewed as being out of touch with at least part of their firms' risk management agenda. According to the survey, 42 percent of those involved in risk decisions believe their senior managers don't know where the companies' top exposures are. And almost half believe their senior managers don't understand their companies risk profiles and mitigation strategies for major risks. Finally, nearly two-thirds cannot say how much they are willing to lose from various risks in order to meet financial goals.

It is unclear if the results mean that such a high percentage of senior managers are actually out of touch or if risk managers just perceive it to be that way and give the C-suite low marks. Some in the C-suite gave themselves slightly higher marks in answering the ratings agency statements than the risk managers gave them credit for. But even those numbers should give pause, as 62 percent of firms' C-suite executives cannot say how much their company is willing to lose from all sources of risk and 41 percent don't understand their own companies' risk profiles.

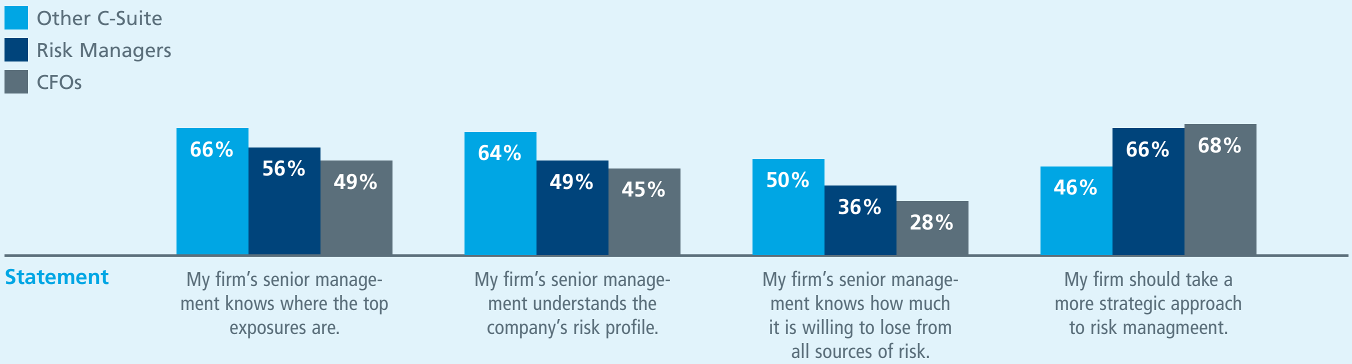
The C-suite gives itself slightly higher marks in answering the ratings agency challenge statements



The harshest assessment of senior management came from within the C-suite, from CFOs, who presumably are well-versed in risk issues. For all three questions, CFOs were the most pessimistic about senior management's risk knowledge.

More CFOs (68 percent) also said that their firms should take a more strategic approach; this is just slightly higher than the number of risk managers (66 percent) who took that position. The closeness of these numbers suggests that CFOs and risk managers in many companies may be natural allies in efforts to pursue strategic risk management and should seek one another out, if they have not done so already.

CFOs were generally less optimistic about senior management's risk knowledge, and felt their firms should take a more strategic approach



The Shift to Strategic Risk Management Continues

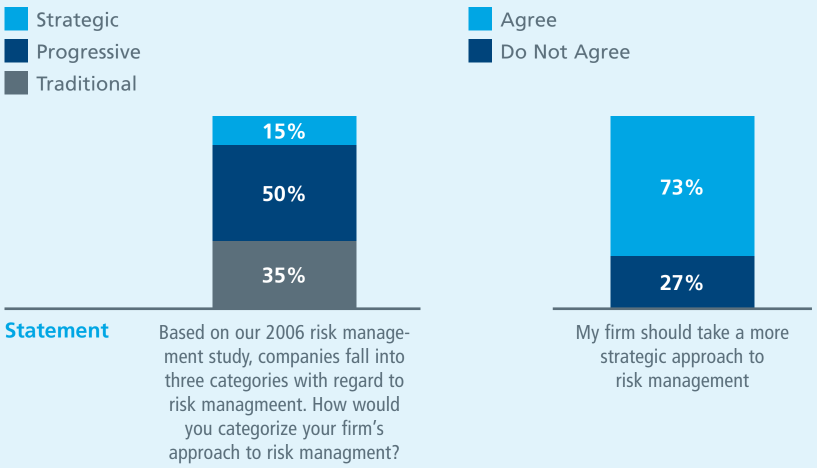
In 2007, we continued to see a shift toward strategic risk management despite the issues raised regarding responses to the ratings agency statements—and perhaps in part because of such issues.

The principle behind strategic risk management is that as risk management becomes more important within an organization, it:

- uses more sophisticated tools;
- becomes more pervasive across the organization;
- becomes more embedded in corporate culture; and
- gains more top management attention and a place in the C-suite.

Fifteen percent of those surveyed considered their companies to have a strategic approach to risk management in 2007. However, most companies—75 percent—said they want to be more strategic in their risk management approach. In theory, if such a shift happens it will show up in the future as a deeper awareness of risk management issues throughout a firm's senior management. That, in turn, should lead more companies to respond affirmatively to the ratings agency challenge statements set out in the previous section.

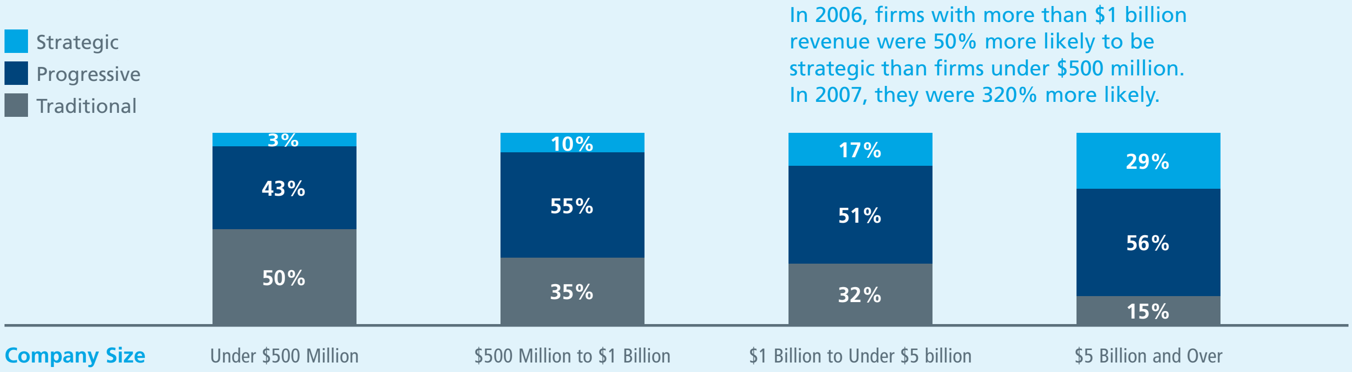
Few companies consider their risk approach strategic; most believe they need to take a more strategic approach to risk management



We also found that larger companies were more likely than smaller firms to have adopted a strategic approach. This may reflect both the complexity of larger firms and also the resources available to them to devote to managing risk. Many of them, for example, have risk management departments with a few dozen employees, compared to smaller firms that may have single risk manager whose main function is to oversee insurance programs. The adoption of risk management by larger companies may also reflect the distance of the board and top management from the activities that they wish to control. That is to say, lack of direct oversight may increase the need for more formal and wider-ranging systems.

Larger firms are more sophisticated in their management of risk

In 2006, firms with more than $1 billion revenue were 50% more likely to be strategic than firms under $500 million. In 2007, they were 320% more likely.



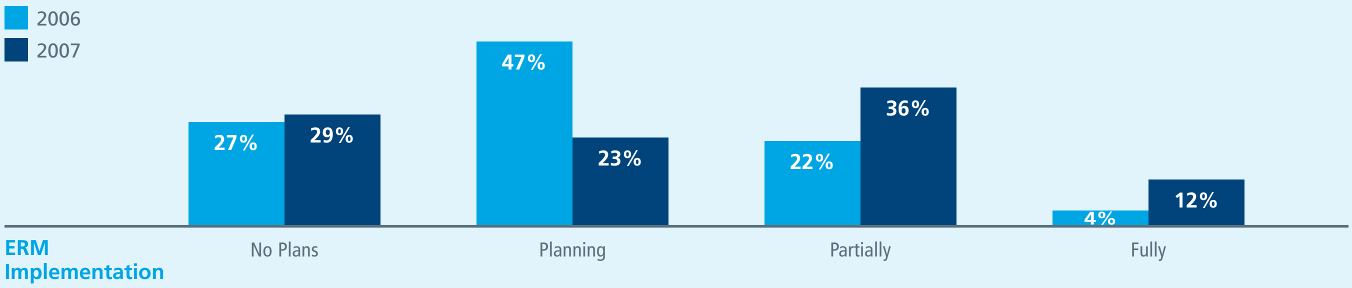
Perhaps the strongest evidence of the trend towards strategic risk management is the continued growth in ERM. Although there is a high level of awareness of the ERM concept, different people and different organizations can have significantly different understandings of it. This is the definition that we took into the study and used in both the qualitative and quantitative components:

Enterprise Risk Management (ERM) is defined as comprehensive risk management that allows corporations to identify, prioritize, and effectively manage their critical risks. An ERM approach integrates risk solutions into all aspects of the business practices and decision-making processes. With an ERM solution, companies have a uniform approach aligned with their strategies and objectives. ERM is a process that is continuously evaluated to ensure that companies effectively identify and manage risks of all types.

As we stated previously, while it is not true that strategic risk management equals enterprise risk management, the two are largely synonymous: A corporation that does not embrace the principles and practices of ERM cannot really be said to be a strategic risk manager.

There was a clear acceleration in the adoption of ERM in 2007. The number of firms saying they have fully implemented ERM tripled in 2007 over 2006's number. It would appear that many companies that had been in the planning stage bumped up to the partially implemented stage. It will be interesting to see if the slowing of the economy since the time the survey was conducted will slow ERM adoption in early 2008.

The use of ERM has nearly doubled in just one year



The percentage of organizations that have no plans to implement ERM remained nearly constant at 29 percent. It is likely that these companies will be found in sectors where the need for strategic risk management is not considered essential. The CEO of a small to midsize construction firm told us: "I have never heard the term ERM, to be honest with you." He also said he was very satisfied that his firm was addressing all of its risks, which he defined largely in terms of insurance-related issues.

We are now in a position to answer the question: "Is there a continued trend towards strategic risk management?" The answer is an emphatic "yes," certainly for organizations that have a need for strategic risk management because of their complexity and the sector within which they operate. It is likely that the trend will continue in the short and medium term, barring major shocks to the economy that could put a damper on available resources.

Are firms coming to adopt strategic risk management on their own? Or are they being pushed there by an increasing awareness of the need to be perceived as a strategic risk manager (as demonstrated by implementing ERM) in order to satisfy ratings agencies or stakeholders? Likely, it is some combination of the two.

In some cases, the move to ERM is being driven internally through the hiring of people within the risk management function who strongly believe in its benefits. "Part of my role since I was hired a few years ago is to develop an ERM platform that comes into the operational and decision-making piece of the company," a risk manager at a Fortune 500 company told us. "I think ERM is the platform by which all business decisions should be made."

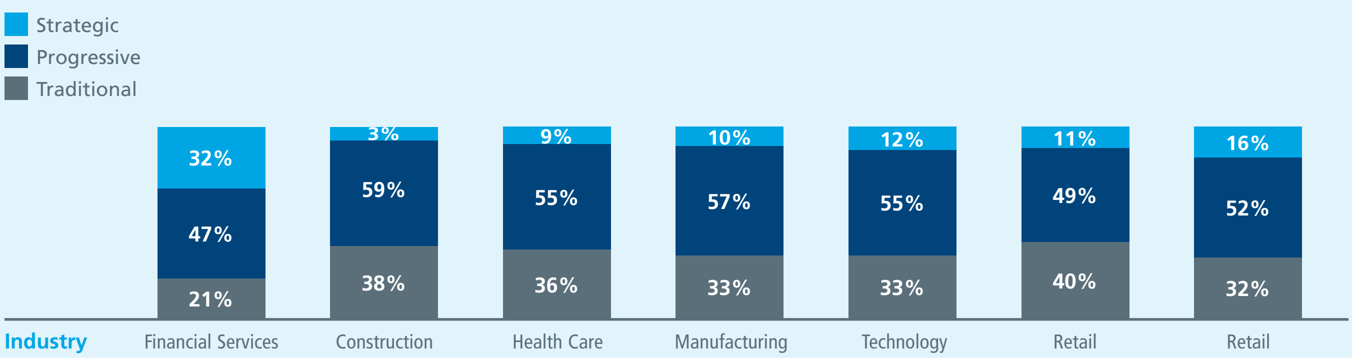
Strategic Risk Management by Industry Sector

Companies' characterizations of their risk management approaches varied by industry sector. The most striking difference from the pack came in the financial services sector; it was a clear standout in terms of the number of corporations that said they have made it through to the level of "strategic" risk management. One possible reason is that financial services companies have had more mandates from ratings agencies, regulators, and others for a robust risk management system.

If there was any surprise in the 32 percent of financial services companies that identified themselves as strategic, it was that the number was so low. This is especially true because the Basel II Capital Accord—the international basis for bank supervision—allows significant cost of capital advantages to banks that have more sophisticated approaches to the management of risk.

It is not as easy to interpret the results for other industries. Sectors with differing risk characteristics may be masked within the overall results. For example, within the construction industry, firms specializing in building to commercial specifications have a different risk profile from those that speculatively acquire land for residential housing.

Financial services firms—certainly driven by regulation—are the most likely to characterize themselves as strategic

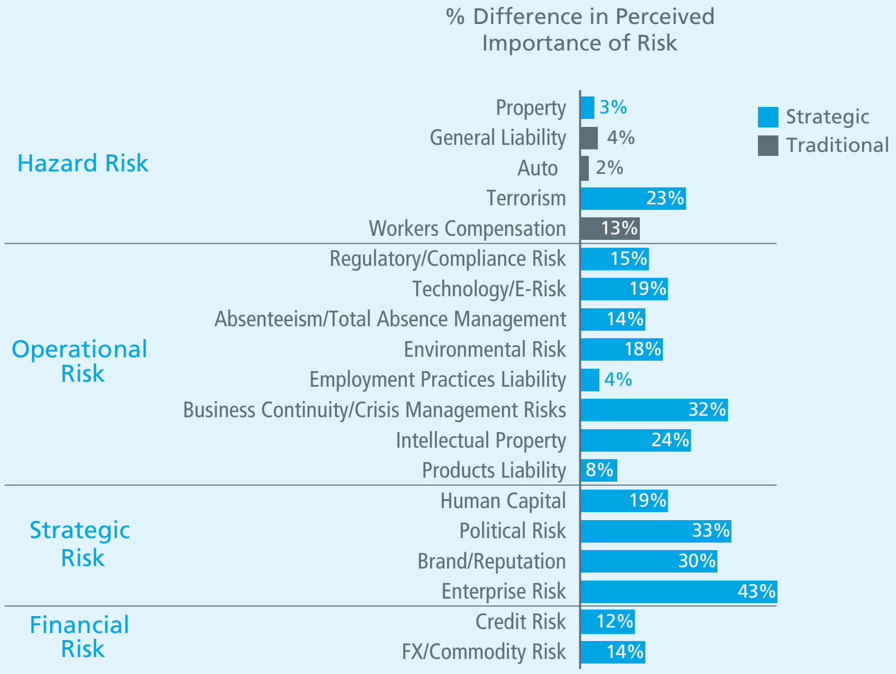


Differing Views of Risk Management

We also found differences in the way risk managers and others perceive the importance of various risks, based on whether they consider their companies to be traditional or strategic. We did so by asking respondents to rank the importance of various risks on a scale. In general, those with a strategic approach were more likely to ascribe a higher level of importance to a grater number of risks, particularly in the broad areas of operational, strategic, and financial risk. Again, this implies that a strategic risk practitioner has a wider lens, or at least focuses the lens differently.

Interestingly, traditional risk managers were more likely to rate hazard risks as having a higher level of importance than were strategic risk managers. Even here, there was an exception: terrorism risk. This can be explained by viewing strategic risk managers as assigning relatively more importance to unlikely events of indeterminable proportions, such as an act of terrorism. That, we believe, is one of the consequences of their radar screens covering a broader territory.

Strategic risk managers are more likely to place greater importance on most risks



Note: The percentages represent the difference in the total number of respondents from each category that ranked each risk as being important or very important. For example, 95 percent in the strategic category ranked brand/reputation risk as important or very important, while only 65 percent in traditional category did so.

As might be expected, risk managers are ahead of the C-Suite in responding affirmatively to the statement: "My firm should take a more strategic approach to risk management." Typically, we might expect that executives within any particular career stream in an organization believe it should have a more strategic role. It's interesting to see how close the C-Suite is to the views of the risk specialists in this area.

Risk managers are slightly ahead of the C-suite in pushing for strategic risk management

Risk Managers and the C-Suite: Who's on First?

Everyone, it seems, wants to be in charge of risk management. When asked to assign a rank to risk management leadership within their companies, risk managers, CFOs, and CEOs all placed themselves in the No. 1 position. Risk managers and CFOs both ranked the CEO No. 2.

Everyone sees himself/herself as the risk management leader

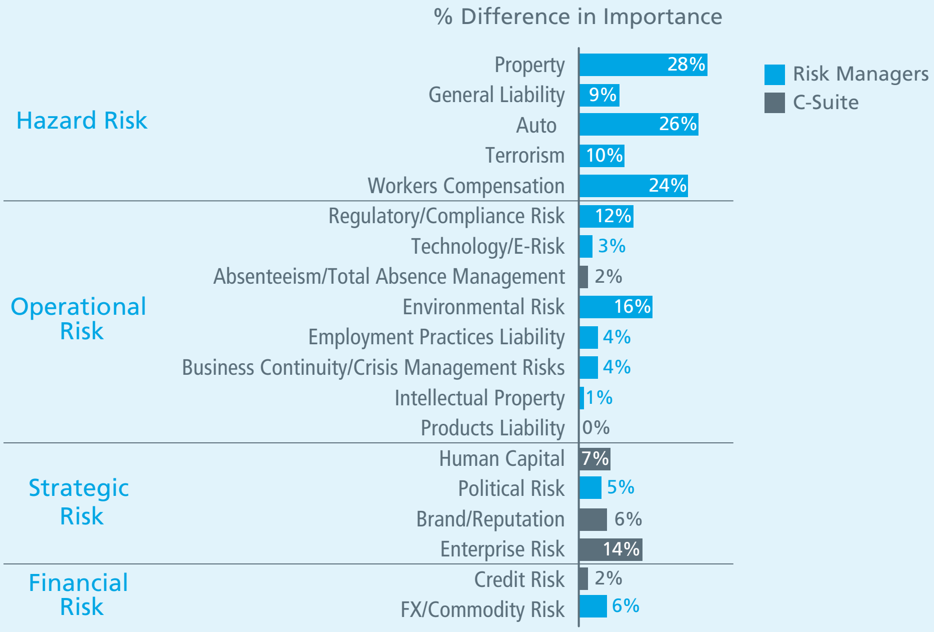
Importance Rank for Risk Leadership by Functional Area

	CEOs	CFOs	Risk Managers
CEO	**1**	2	2
CFO	2	**1**	3
Risk Manager	3	3	**1**

It appears that all parties view risk management as critical to their company's mission. Although problems potentially could arise if no clear leader stepped forward at a moment of crisis, it is perhaps more likely that the leadership issue simply relates to different ideas about what it means to be the risk management leader.

In general, risk managers tended to place more importance on hazard risks than their C-suite counterparts. One explanation may be that no matter if they are traditional, progressive, or strategic, risk managers are likely to be involved with hazard risk issues every day, either directly or through those they manage. In the risk managers' world then, these are important areas. Those in the C-suite, however, do not work regularly with hazard risks. In fact, they ideally trust that their risk management staff has those areas well covered. Their risk radar is more attuned to less quantifiable risks, as seen by their view of such things as human capital risk, brand/reputation, and enterprise risk.

Risk managers are more likely to place greater importance on risks than their C-suite colleagues—especially hazard risks



Note: The percentages represent the difference in the total number of respondents from each area that ranked each risk as being important or very important. For example, 83 percent of risk managers ranked property risk as important or very important, while only 54 percent of C-suite respondents did so.

Another way we looked for differences was in the order in which people ranked certain risk categories. Interestingly, even though the C-suite placed more importance on brand and reputation than did risk managers, risk managers agreed that these are the firm's top exposures. This may reflect a growing awareness of the damage brands can suffer when a crisis erupts—such as a product recall or a high-profile lawsuit. Protecting an organization's reputation shouldn't be limited to protecting only the more "creative" professionals, such as advertising and marketing executives. Traditionally, many risk managers haven't been comfortable enough with brand and reputation issues to really understand if they are being managed effectively. Ultimately, when executives and risk managers include the depth and breadth of the brand issues on their radars, the question is no longer: "Are we protecting our reputation?" It becomes: "Are we doing enough to manage reputational risks?"

Brand and regulatory compliance are rated top exposures by both the C-suite and risk managers; views diverge for human capital and technology risks

Exposure Risks Ranked

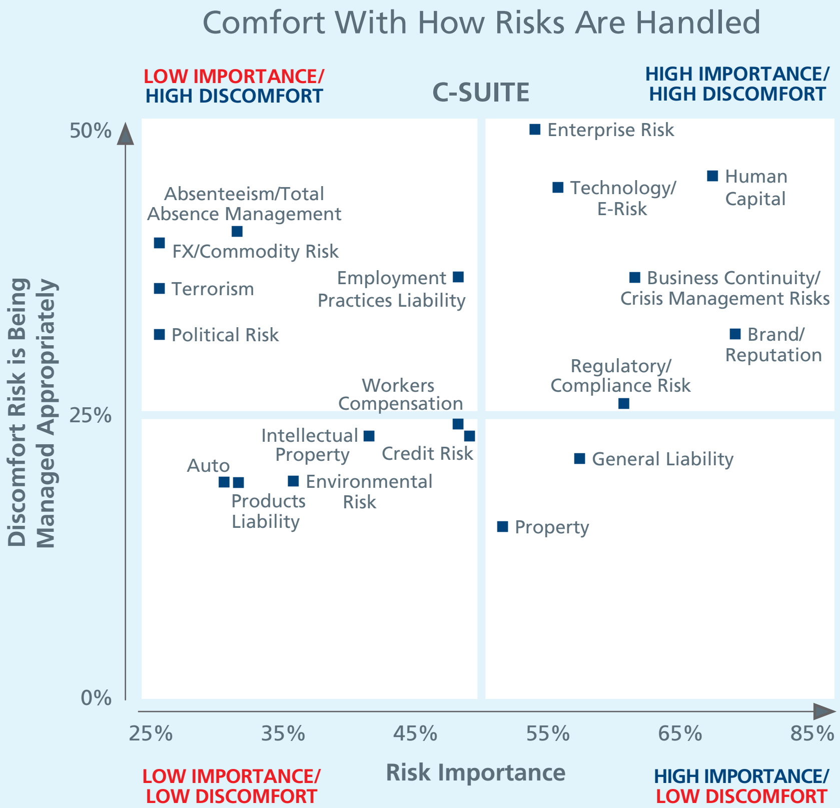
	C-Suite	Risk Managers
Brand Reputation	1	1
Human Capital	2	8
Regulatory Compliance	3	3
Business Continuity	4	2
Technology/E-Risk	5	7
Property	8	4
Workers Compensation	9	5

Ranked Above 5 (Not Top 5)

The C-suite—including CFOs—and risk managers are generally in alignment with regard to the importance and management of risk. However, there are differences:

- Risk managers think worker's compensation is a more important risk than does the C-suite, but are also more comfortable with it.
- Risk managers are considerably more comfortable with FX/commodity and regulatory/compliance risk.
- Enterprise risk is much more important to CFOs and their C-suite colleagues than to risk managers.
- CFOs are especially concerned with absenteeism and business continuity

Risk managers and the C-suite are in reasonable alignment on what's important and what's well-managed



Turning Risk into Opportunity

Risk has long been seen as a necessary counterweight to growth. We believe that a 360-degree view of risk can help companies turn risk into opportunity. Before the 2007 *Excellence Survey* was undertaken, preliminary work led to the identification of 10 state-of-the-art techniques that may help organizations turn risk into opportunity. We wanted to know if these techniques were being used, if they worked, and if their usage would grow. The 10 techniques and the percentage of firms that said they were using each one fully or extensively were:

Emerging use of risk-into-opportunity techniques

Managing people risk is the standout in terms of the number of organizations that pursue it. And it harkens back to an earlier finding, that the C-Suite sees human capital issues as the No. 2 concern, just behind brand/reputation. Interestingly, risk managers had placed human capital as the eighth ranked risk exposure, but saw it as the primary way in which companies are turning risk into opportunity.

Minimizing business disruption is the second most widely used of the approaches listed. This likely shows the recognition of a more integrated business environment, one in which many players increasingly focus on their core competitive advantages. Managing complex supply chains necessarily requires not only addressing the risks of disruption, but making them efficient to wring out economic benefits. Both risk managers and C-suite executives ranked business continuity in the top four exposures.

Managing regulatory compliance is the third most widely used approach. This would seem to turn traditional thinking on its head, as regulatory compliance can be a significant and growing burden on business. What risk practitioners likely are saying here is that regulatory issues are such a significant cost factor that the skill with which they are managed is becoming a source of competitive advantage. It is also the case that firms that do a top-rate job in complying with regulations—particularly those involving health, safety, and the environment—may experience a public relations benefit.

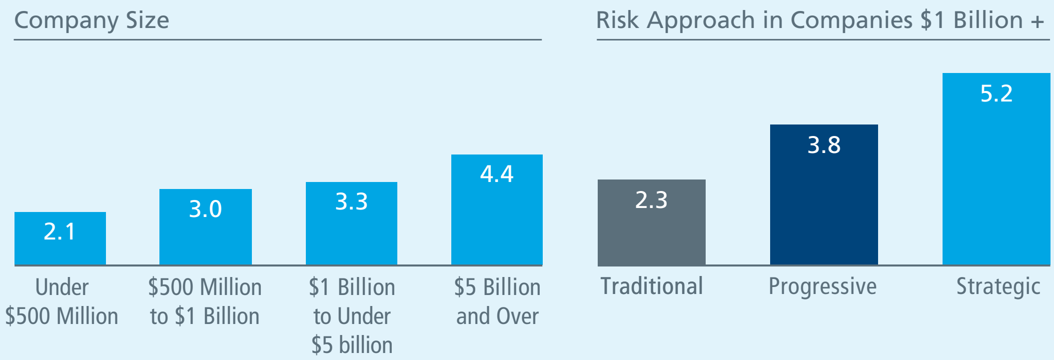
We also asked how many of the risk-into-opportunity techniques individual firms were using. Sixteen percent said they weren't using any; while at the other end of the spectrum, 16 percent said they were using more than five.

- 16%—5 or more
- 37%—3 to 5
- 31%—1 or 2
- 16%—None

Large firms are likely to have both the need and the resources to meet the challenges of risk proactively. Strategic risk managers, as we have seen, assess more risks than do traditional risk managers. They take into account a wider variety of risk and also are more sophisticated at distinguishing between risk and uncertainty.

Large firms and those that consider themselves to be strategic risk managers are most actively trying to turn risks into opportunities

Number of Techniques Fully Implemented or Using Extensively



There appears to be a growing feeling that there is an upside to risk in that it can be turned into opportunity for performance enhancement. There are a number of specific examples of this happening in forward-thinking organizations. However, this aspect of risk management is less fully evolved than others. While a wide variety of techniques are practiced, there is as yet no authoritative framework.

Global Views of Strategic Risk Management

We have seen that strategic risk management is forging ahead in the United States, but what about in the rest of the world? We conducted in-depth interviews with 30 senior executives from a variety of industries in two regions (see map) to see if this trend was evident elsewhere. Eighteen of the companies had annual revenues between US$250 million and US$1 billion; 12 had revenues greater than US$1 billion. Unlike the U.S. survey, the research in Europe and the Asia/Pacific (AP) region should be considered descriptive rather than definitive.

Respondents represented a wide variety of functions—including general management, finance, and risk management—and were all actively involved in risk management practices.

We described our U.S. survey results to each interviewee, then asked them to compare those findings to what they saw in their firms and in other organizations in their countries. We concluded that risk management in these regions is gaining in importance and sophistication—in other words, it is moving toward a strategic viewpoint—although not as quickly as in the United States. Because there are important differences between Europe and AP, we have separated our comments on those two regions.

Strategic Risk Management in Europe

Almost all of the European firms we interviewed expressed a desire to practice risk management more strategically. Few, however, are there yet. None of the respondents outside of the financial services sector classified themselves as currently practicing strategic risk management; even those claiming to be progressive may have been a little too kind to themselves. Equally important, their perception is that peers in their respective countries rarely practice sophisticated risk management.

We considered three possible reasons that Europe lags behind the United States in adopting a strategic approach.

- First, there is a cultural bias in European countries generally toward a more close-knit, laissez-faire management style. That said, the U.K. and German executives we talked to practiced more of a U.S.-style approach than did the French and Italians. For example, a German finance manager said: “I think (German) firms vary between traditional and progressive. Barely any are strategic. Of course they are heading slowly in the strategic direction, but the U.S. is just faster in this case.”
- Second, there are fewer large global companies in Europe than in the United States, and it is this type of firm that is most likely to lead the way in adopting more sophisticated risk management practices. “Italian companies generally are small or medium-size—too small to have an officer specifically dealing with risk management,” said the CFO of an Italian engineering firm.
- Third, the United States is characterized more by the use of scientific management and professional training of executives—evidenced by its proliferation of MBAs. In the United States, “it is more common for someone to take time out from work and do an MBA. They are, therefore, more aware of terms, disciplines, and tools,” said the vice president of compliance at a U.K. financial firm.

With respect to ERM specifically, half of the European executives we interviewed did not recognize the term and some of those that did believed it to be simply new language applied to traditional risk management. The minority of firms that understood ERM and said they had at least partially implemented it were either very large or in the financial services sector.

Russia appears to have a disproportionate share of firms that practice sophisticated risk management. Russia is, of course, experiencing rapid growth and change, meaning there are great opportunities and great risks in doing business there. In this type of environment, the return on investment from sophisticated risk management may be higher and thus may attract more investment, including importing sophisticated managers from the United States and elsewhere.

Emerging Risks in Europe

When looking at the importance executives place on various risks, Europe is generally on the same page as the United States. Brand/reputation and human capital are most often mentioned as representing the most significant exposures. Credit risk and market/investment risk received a lot of attention from European risk practitioners, more so than in the United States. One explanation is that the subprime crisis likely caused these issues to rise in importance during the six-month interval between the U.S. and European surveys.

External Influences

In Europe, the risk management executives we interviewed pointed to a variety of external influences that may be propelling more sophisticated risk management. Many of the executives that we interviewed had compliance responsibilities as part of their duties. Among the drivers of risk management sophistication mentioned were:

- governmental regulations;
- stock exchange listing guidelines;
- ISO standards, especially those dealing with the environment and quality;
- the London Stock Exchange's Combined Code; and
- Basel II requirements that mandate specific risk management protocols for firms in the financial sector.

The European executives pointed out cost as a key factor that may hinder the movement toward strategic risk management, especially at smaller companies. There was particular concern with staffing a chief risk officer (CRO) position rather than having those duties done by existing board-level staff.

Risk Management Leadership

There appears to be a difference between Europe and the United States in terms of risk management responsibility. In the United States, risk managers, CFOs, and C-suite executives all claimed the leadership role. In Europe, however, there was broad agreement that responsibility resides at the board level.

Strategic Risk Management in Asia/Pacific

It appears that, like Europe, the Asia/Pacific region lags behind the United States in terms of adopting the most sophisticated risk management procedures. Our interviews with 13 executives in AP countries found:

- In AP, there is a perception that ERM and strategic risk management are necessary only in the largest firms or in those with global reach.
- Nationality and culture have an effect. Firms with closer ties to the United States and the United Kingdom were likely to be viewed as more sophisticated risk managers.
- Views differed on the Chinese approach. A Hong Kong respondent felt that Chinese firms practiced more traditional risk management than did foreign-owned firms. A respondent from Singapore, however, believed that with the removal of government support from Chinese business those firms were being forced to be more sophisticated risk takers.
- As elsewhere, industry sector has a strong bearing on risk management practices. Firms in the financial services industry are, by culture and regulation, far more likely to be sophisticated risk managers.

There was a sense from the AP respondents that their region is accelerating toward strategic risk management. This may be the result of the fast pace of growth in many AP economies.

Emerging Risks

Asia/Pacific firms agreed with those in Europe and the United States that brand/reputation and human capital represent the greatest exposures. One difference between AP and Europe came in their assessment of credit risk, which European executives ranked much higher. It appeared that the AP firms felt less connected to global credit markets, perhaps being insulated by the strong growth of many AP economies.

On the other hand, it appeared that AP executives felt somewhat greater exposure to terrorism risks than did their European and U.S. counterparts. The attitude about terrorism among AP executives seemed to be that it is not a problem in their home countries, but it can be in areas where they do business. A related concern is the potential for secondary impacts from terrorism. Even if terrorist activity has no direct local impact, some AP executives worry about potentially broader economic, political, regulatory, and insurance implications.

External Influences

Like their European peers, the AP risk management executives appeared to be more concerned with regulatory issues than with any potential changes from ratings agencies. And in terms of what holds back strategic risk management, there was even more mention in AP of the cost of implementing ERM and more sophisticated risk management systems.

Risk Management Leadership

None of the firms we interviewed in Asia/Pacific had an explicitly titled CRO. Most agreed that a board-level position with risk responsibility was appropriate for only the largest firms. And some voiced the same concern expressed by European respondents that the existence of a CRO might cause other board members to make the mistake of thinking that risk management was no longer part of their job. The absence in AP of a strong history of traditional risk management gives this region the opportunity to leapfrog progressive risk management and move directly to strategic risk management.

Conclusion

There is a strong desire among U.S. firms to broaden their approach to risk issues—to attain a 360-degree view of the risks facing them. More companies are moving toward that approach—which we call strategic risk management—whether guided there internally by strategic thinkers or pushed there by external forces.

One such force is the potential scrutiny from ratings agencies, which have looked at ERM measures when evaluating financial services firms for a number of years. The potential that they may soon begin to do so for nonfinancial firms should not be ignored, as credit scores from these agencies have a very real effect on a company's finances. At present, most companies said they would struggle to answer some of the types of questions the ratings agencies would likely ask them regarding their risk management strategies.

But many companies are already shifting toward a more strategic approach to risk management. As they do so, communication between the C-suite and risk managers will play a critical role. The variety of perspectives that individuals in different parts of an organization hold about risk can help a firm reach its goal of having a more strategic approach to risk management. In doing so, companies may find more ways to turn their risks into opportunities.

Strategic risk management and ERM are gaining ground around the world, but at a slower pace than in the United States. While Asia/Pacific countries may now trail their European counterparts, they may be able to quickly accelerate from traditional to strategic risk management. There appears to be a feeling in many countries that risk management responsibility should rest at the board level. Executives outside the United States show little concern with potential moves by ratings agencies regarding ERM, but are concerned by external forces such as regulators and international bodies.

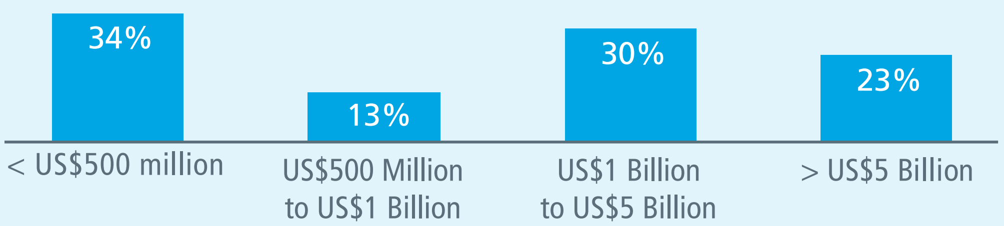
Appendix: The Survey Population

The findings in this report are based on 501 interviews conducted by TNS from February 14, 2007, through March 23, 2007, with:

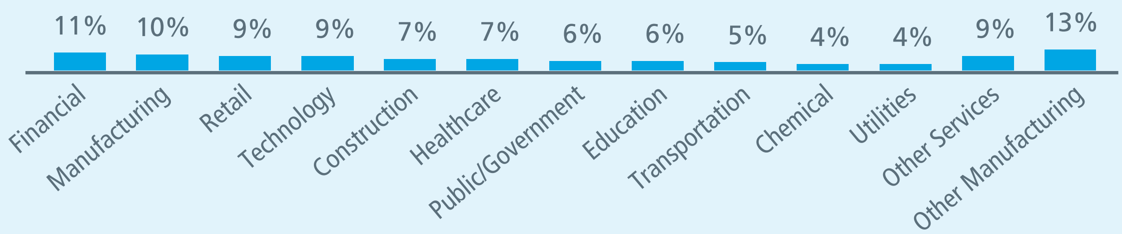
- 297 risk managers;
- 125 C-suite executives (CEOs, CFOs, general counsels, and chief risk officers (CROs); and
- 66 associated titles (controller, accountant, claims manager, and similar titles).

Annual Revenues

The firms represented in this survey were divided into four revenue groupings, nearly equally split between middle-market and large-market companies.



Industry Sector/Affiliation



About RIMS

The Risk and Insurance Management Society, Inc. (RIMS) is a not-for-profit organization dedicated to advancing the practice of risk management, a professional discipline that protects physical, financial, and human resources. Founded in 1950, RIMS represents more than 4,000 industrial, service, nonprofit, charitable, and governmental entities. The Society serves over 9,600 risk management professionals around the world. For more information, visit the RIMS Web site: http://www.RIMS.org

About Marsh

Marsh is part of the family of MMC companies, including Kroll, Guy Carpenter, Putnam Investments, Mercer Human Resource Consulting (including Mercer Health & Benefits, Mercer HR Services, Mercer Investment Consulting, and Mercer Global Investments), and Mercer specialty consulting businesses (including Mercer Management Consulting, Mercer Oliver Wyman, Mercer Delta Organizational Consulting, NERA Economic Consulting, and Lippincott Mercer).

For further information, please contact your local Marsh representative, or visit the Marsh Web site: http://www.marsh.com

MARSH

MARSH MERCER KROLL
GUY CARPENTER OLIVER WYMAN

Marsh
1166 Avenue of the Americas
New York, NY 10036
212 345 6000

www.marsh.com