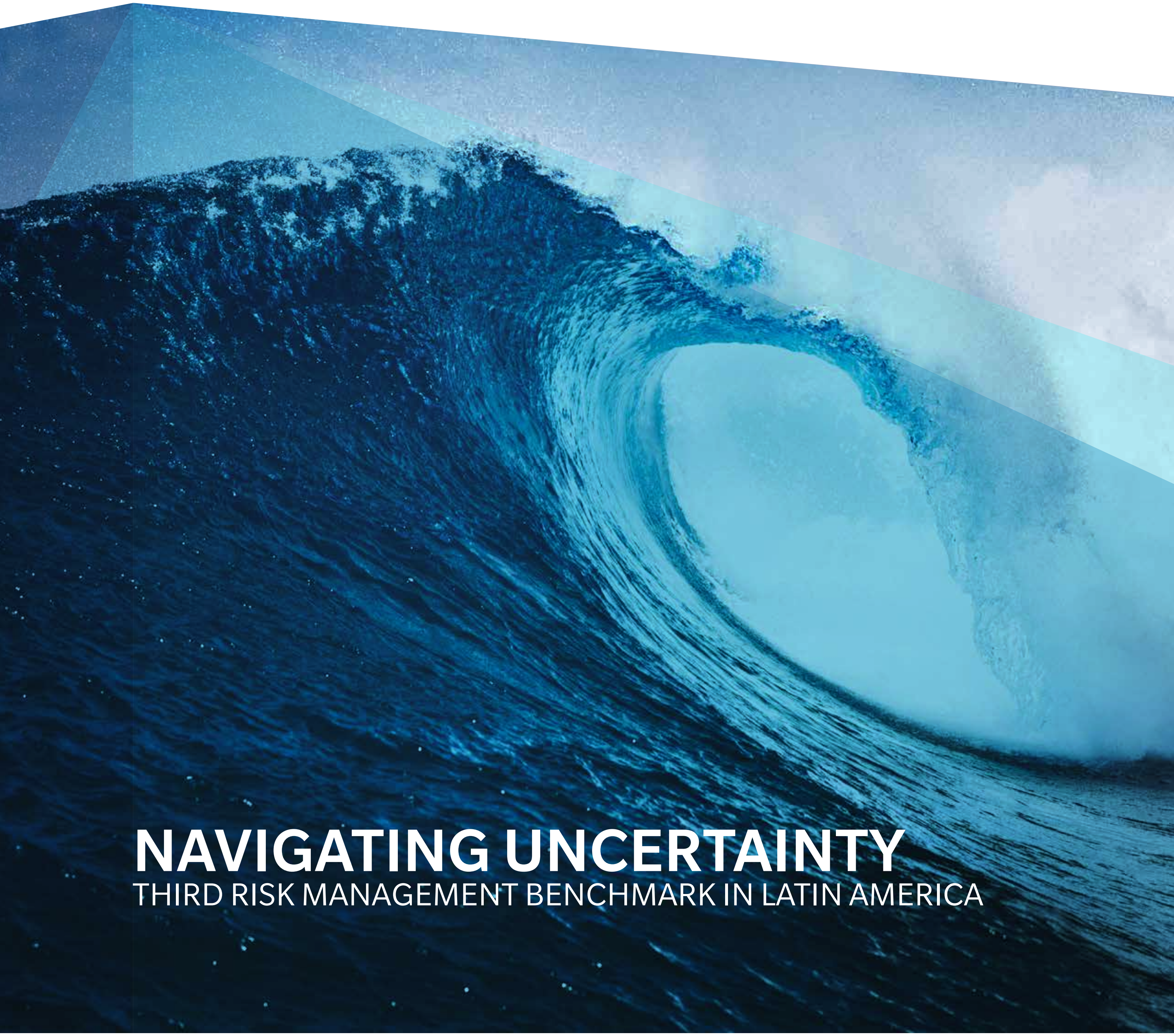
MARSH RISK CONSULTING

RIMS
the risk management society

REIMAGINE RISK

CAPTURING OPPORTUNITIES IN A WORLD OF RISK



NAVIGATING UNCERTAINTY

THIRD RISK MANAGEMENT BENCHMARK IN LATIN AMERICA

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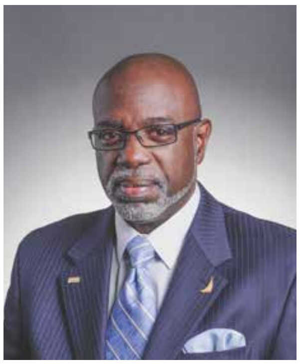
In an increasingly complex, volatile, and interconnected world, one of the keys to capturing opportunities lies in our ability to anticipate, identify, transform, and reimagine risk. Comprehensive and innovative risk management not only creates value for organizations, but transforms risks into real and sustainable competitive advantages.

INTRODUCTION



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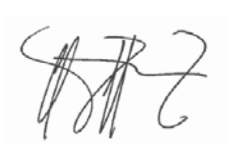

As old as humanity itself, the practice of risk management — with its fundamental objective of identifying and providing the means to act intelligently in the face of dangers and exposures – is constantly evolving and changing to challenge a changing world. That is why, for the third year, Marsh Risk Consulting, part of the Marsh & McLennan Companies group, in partnership with RIMS, The Risk and Insurance Management Society, has conducted this risk management study to delve into topics of interest and share valuable information regarding the reality of risk management in Latin America.

This year, continuing on our path to Reimagine Risk in the region and globally, the study deepens and responds to three topics of great interest:

- How is risk management evolving in the Latin American business world?
- How well positioned is comprehensive risk management in organizational cultures?
- What are the main emerging risks we face?

With an examination of the status quo of risk management, its level of maturity, and its ongoing evolution, the study this year provides relevant information to gain more comprehensive and updated knowledge of where we are, as well as shares the experiences of risk managers in Latin America about their challenges and successes with its implementation.

Likewise, we delve into the problem of risk management culture development and implementation, seeking to understand the common elements that facilitate it, the challenges found with positioning it in the organization, and especially how partners internalize it in their companies.

Finally, looking ahead to the future and at the elements that guide us down the path of organizational resilience, the study delves into the topic of emerging risks. We study the meaning of the concept, the associated information sources, and explore the difficulties that risk professionals are finding in modeling the potential impacts of emerging risks.

In general, our goal this year is to provide knowledge that helps us all to challenge the vision and conventional thought processes in risk management in order to redefine expectations and innovate towards a more comprehensive risk management approach.

We are confident that you will find in this edition of the third risk management study in Latin America a great tool to Reimagine Risk, and open discussions around the evolution of risk, risk culture, and the next steps along the path of organizational resilience.

We invite you to approach our Marsh Risk Consulting's consultants to answer any questions or concerns about the study.

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MATURITY LEVEL OF RISK MANAGEMENT IN THE REGION

Currently, there are many approaches and methodologies to estimate the level of maturity of comprehensive risk management. Ultimately, the purpose of these indicies is to provide insights into the status of the current development of the components of risk management and to encourage striving for continuous improvement as a fundamental element of sustainability, good corporate governance, and strategic planning.

In this study we seek to understand the level of maturity of comprehensive risk management in Latin America, with the aim of delving into the factors that facilitate or hinder its implementation, as well as more thoroughly analyze the Latin American business reality with regards to its adoption. For this study, the following five (5) levels of risk management maturity were defined and are described as follows:

LEVEL OF MATURITY

1 NOT DEVELOPED

There is no structured approach to identify and manage risks. Risk management practices are basic and are not applied consistently. There is a low level of understanding and awareness of them. There are critical improvement opportunities.

2 FORMALIZED

Policies and processes are being established. Risk management practices are in the process of being developed and they are not applied consistently. However, there is a good understanding and awareness of them by a few individuals in the organization. There are significant improvement opportunities.

3 ESTABLISHED

Risk management has been implemented within the routine processes of the organization. Risk management practices are established and are applied in a consistent manner with better levels of understanding and awareness of them by management and employees. There are opportunities for improvement in certain aspects.

4 IMPLANTED AND INTERNALIZED

There is a proactive approach to risk management at all organization levels. Risk management practices are at an advanced level, they are applied consistently, and they are incorporated into processes with high levels of understanding and awareness by management and employees. There are opportunities for improvement in a few specific aspects.

5 OPTIMIZED

Continuous improvement is being carried out and a full range of risk management program activities are being executed. Risk management practices are innovative and cutting-edge in the industry, they are applied consistently, they are integrated transversally in the organization, and they are easily replicable in new areas of the organization. There are very high levels of understanding and awareness of risk management practices by management and employees.

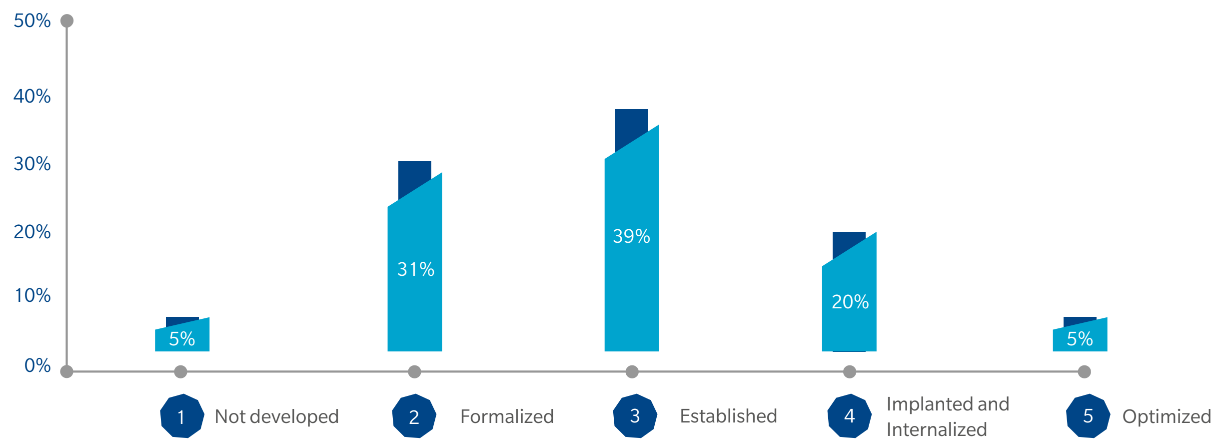
25% of Latin American companies have advanced levels of maturity in risk management.

According to the results of this study, organizations in Latin America are in general terms in the initial stages of maturity but with a clear and determined path towards organizational resilience. According to the results, a small group of organizations falls in the upper segments of maturity (25% in levels 4 and 5) while a larger group of companies is distributed across the initial levels (75% dispersed between levels 1, 2, and 3).

However, two out of every five Latin American organizations are at maturity level 3, where risk management – although it is already implemented within the organization's routine processes, and its practices are established, and are applied in a consistent way throughout the organization – still requires some effort to be truly integrated universally across all areas of the organization, as well as proactively adopted for continuous improvement.

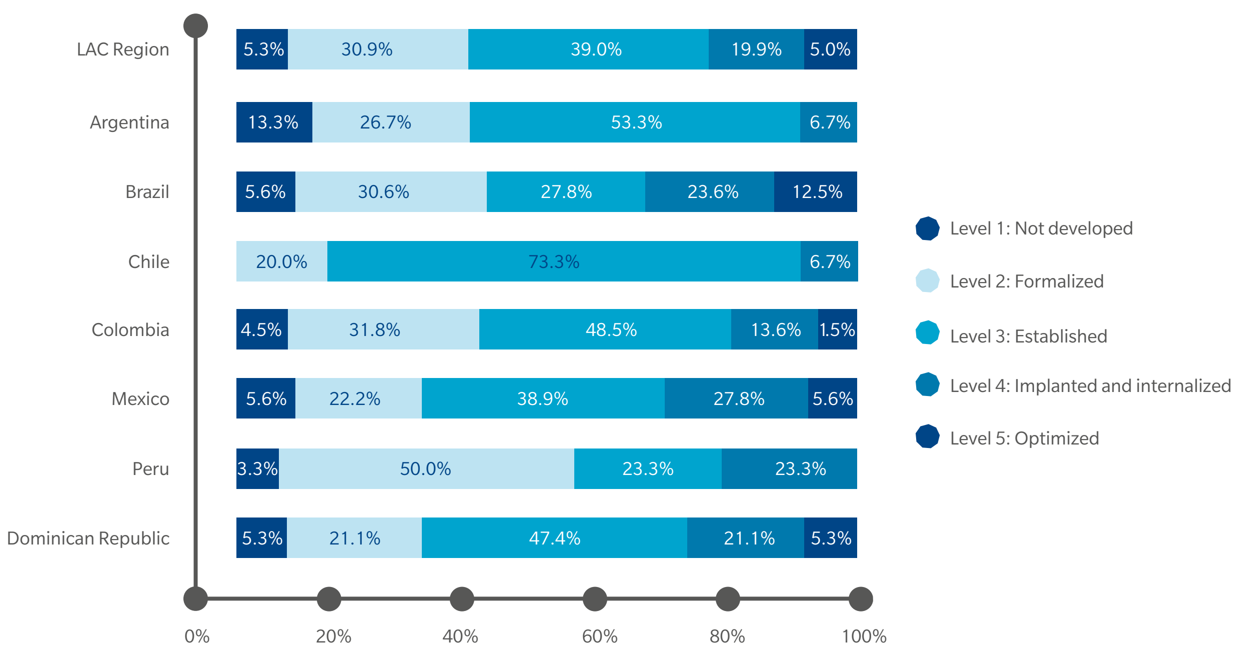
Graphic #1

HOW DEVELOPED IS RISK MANAGEMENT IN YOUR ORGANIZATION?



Graphic #2

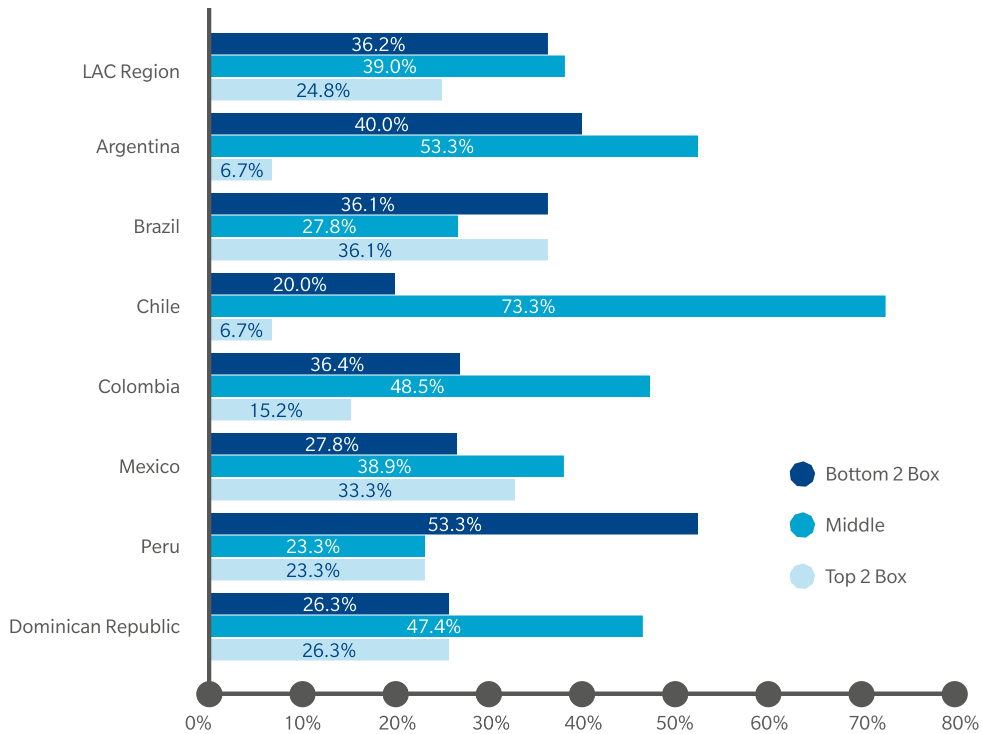
HOW DEVELOPED IS RISK MANAGEMENT IN YOUR ORGANIZATION? BY COUNTRY



Graphic #3

ANALYSIS OF TOP-TWO BOX* AND BOTTOM-TWO BOX** BY COUNTRY

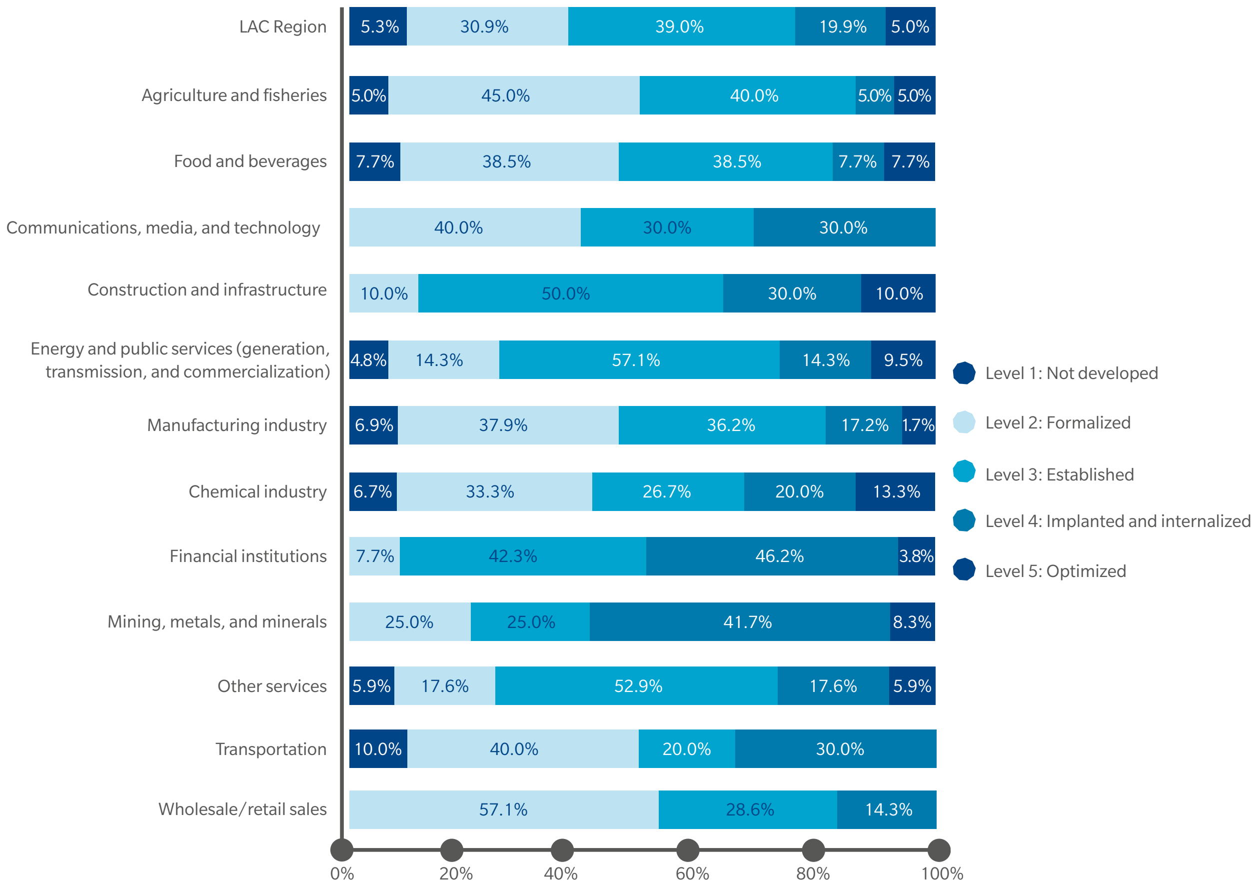
***Sum of scores for the two higher levels of maturity**
****Sum of the scores for the two lower levels of maturity**



When studying the different maturity levels per country, we discover that countries showing the greatest progress are Brazil and Mexico, corresponding to the Top-Two Box level (sum of scores for the two higher levels of maturity (4 and 5)). In contrast, Peru and Argentina fall to Bottom-Two Box levels (sum of scores for the two lower levels of maturity (1 and 2)). Organizations based in Chile, Argentina, Colombia, and the Dominican Republic show a concentration at an average maturity level. There is a strong concentration of Latin American companies at a medium maturity level.

Graphic #4

HOW DEVELOPED IS RISK MANAGEMENT IN YOUR ORGANIZATION? BY SECTOR



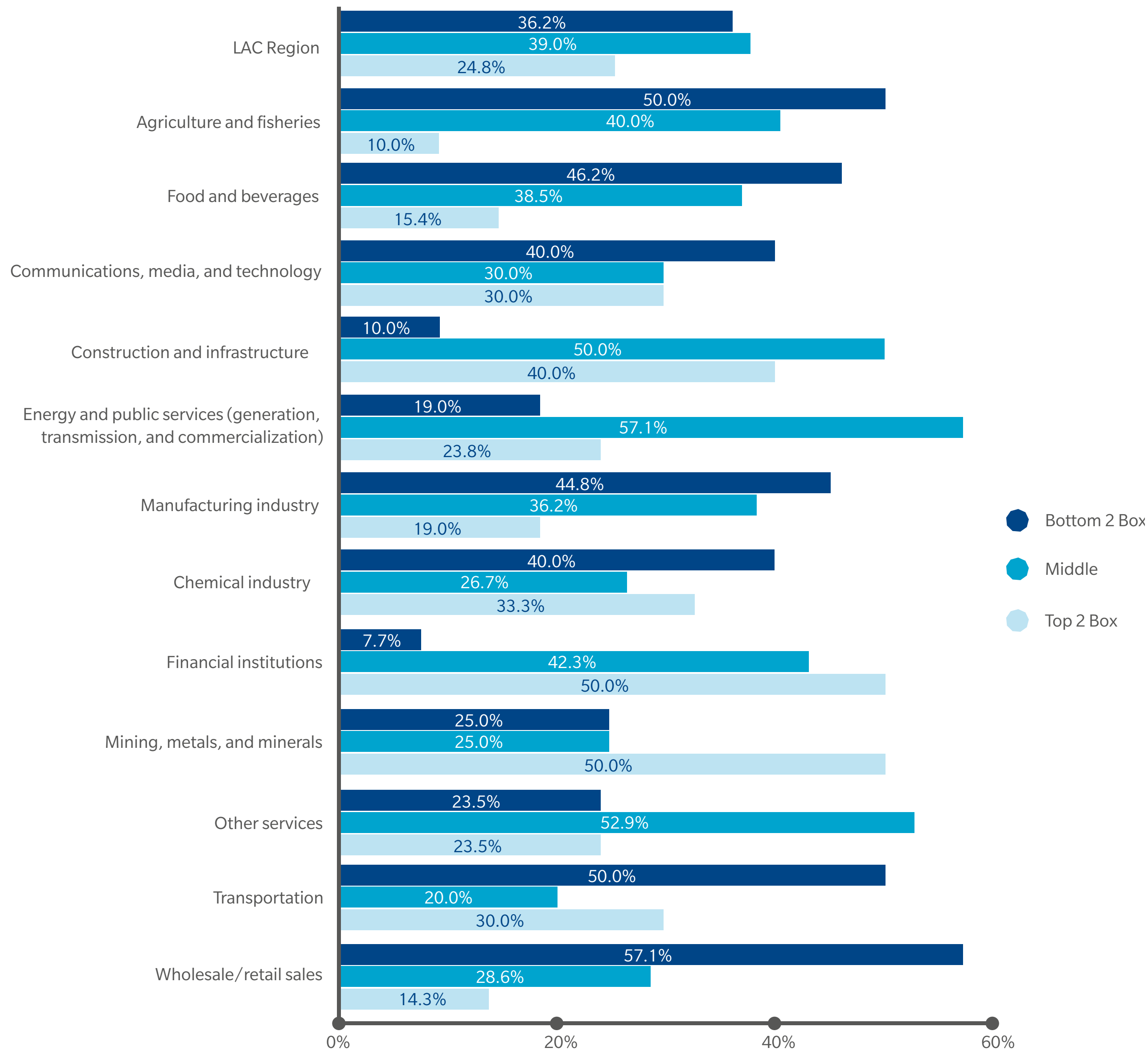
*Sectors with significant data were presented for comparisons

The analysis by sectors shows that financial institutions and mining, metals, and minerals have a higher level of maturity, standing out for having a concentration of 50% in the two upper levels (Top-Two Box). On the other hand, the wholesale/retail, transport, and agriculture and fishing sectors indicate a concentration in the two lower levels (Bottom-Two Box) greater or equal to 50%. Wholesale/retail with a 57% concentation and transport and agriculture and fishing each with a 50% concentration demonstrate the clear influence that regulation and its associated demands, such as compliance timelines, have in certain industries in relation to the application of risk management models. The financial industry is a clear example of what happens in a highly-regulated sector over time, which affects the level of advanced maturity in risk management in the sector.

The more mature risk management is within an organization, the greater its ability to make tangible the benefits of its application and, in turn, it will have greater capacity to demonstrate the value it generates. The above is clearly observed when organizations cross the threshold of only complying with the implementation of the risk management process, which is part of most operational implementations, and instead focus on the development of other risk management structural elements which make it more sustainable. To illustrate with an example, for rail transport to work there must be both wagons and rails (with their attendent command and control systems). If the "*wagons*" represent the activities of the risk management process (identification, analysis, evaluation, treatment, and

Graphic #5

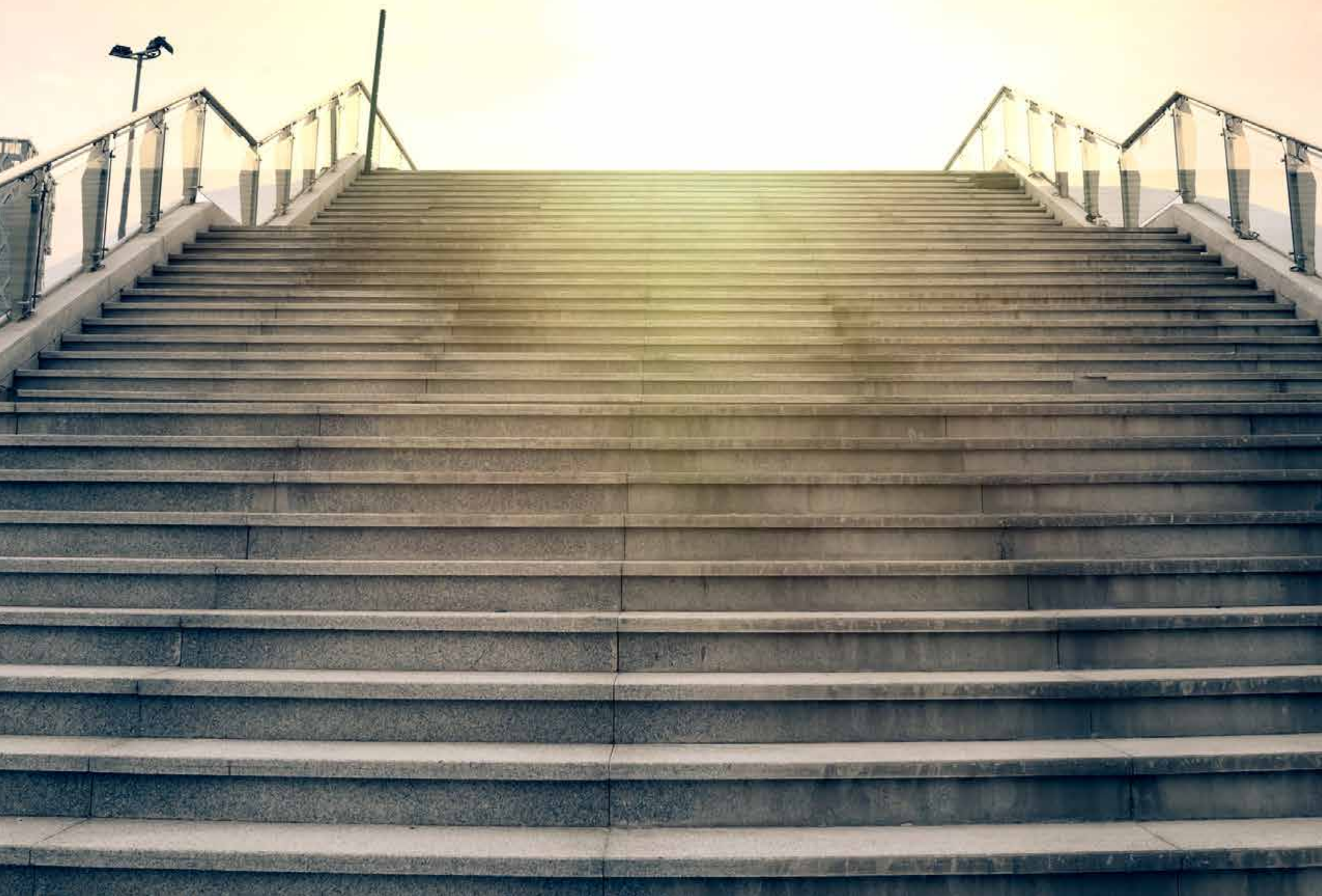
ANALYSIS TOP-TWO BOX AND BOTTOM-TWO BOX BY SECTOR



monitoring) through which the organization of the risk management infrastructure is mobilized annually, the "*rails*" represent the infrastructure of risk management and its elements, such as its organizational structure, the culture of risk management, and risk management's relationship with other areas of the company (including audit, strategic planning, insurance management, and human resources). If these rails are robustly established and maintained, risk management will have facilitating elements and drivers of its evolution, allowing capture of its value as a business management tool. It will be very interesting for Latin American companies to review the foundations of risk management within their organizations, the elements that compose it, and those elements of continuous improvement that should be implemented to continue escalating up the steps of the maturity model and consequently bring more value to the organization.

CHALLENGES IN THE IMPLEMENTATION OF RISK MANAGEMENT

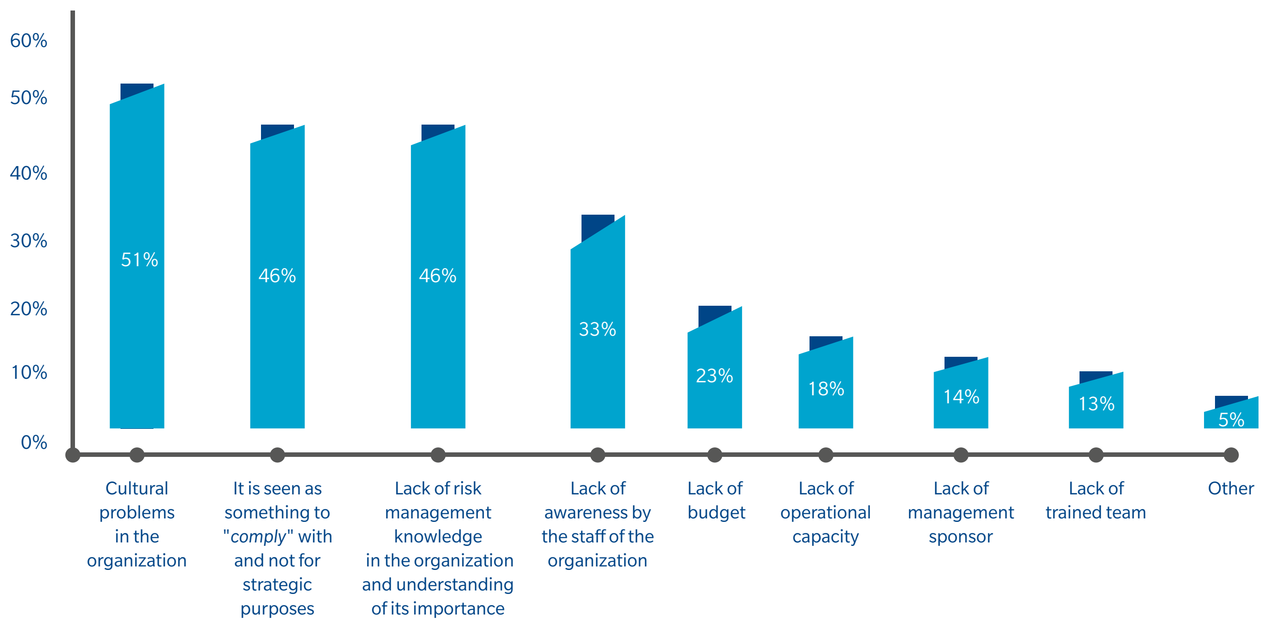
The implementation of comprehensive risk management in Latin America has faced a great number of facilitators and obstacles. Corporate culture and expert knowledge (or the lack thereof) are the main factors that contribute to its success.



Regardless of what factors have been responsible for the emergence of risk management in the organization, implementation of risk management in companies in Latin America has encountered numerous facilitators and obstacles. Exacerbating the implementation challenges that risk management leaders in Latin American organizations have faced, we find that most are related to problems of organizational culture, with the perception that risk management is compliance as opposed to a strategic tool. There is also a lack of information and key knowledge in the consistent application of the model. These three main challenges are highly correlated and one could even argue that they are mutually triggering.

Graphic #6

WHAT CHALLENGES DID YOU FIND IN THE IMPLEMENTATION OF RISK MANAGEMENT IN YOUR ORGANIZATION AND WHAT CHALLENGES DO YOU STILL FACE?



Organizational culture conditions are key to any initiative's growth or stagnation. Risk management, like any other management tool, must find fertile ground by successfully inserting itself into the strategic and operational model of an organization.

If the organization has not internalized the importance of risk management at all levels and across all functions and has not defined the need to generate and report risk managment information (i.e., materializations, aggravations, indicators, alerts, and effectiveness in controls, among others) as a key component of decision making, it is unlikely that employees will adopt and own it as part of their day-to-day life, missing the opportunity to make risk management an essential element in decision making optimization.

The lack of in-depth knowledge of the importance of risk management is emerging as another challenge to establishing it in organizational culture. Without a collective view about its value and its operation, risk management remains another model of compliance.

EXPERIENCES OF RISK MANAGERS IN THE REGION

Some of the most prominent risk managers in the region who participated in the study contributed their experiences and personal reflections on the challenges that many organizations still face and the enablers that help implementation of risk management.

THE CHALLENGES

Some of the risk management leaders participating in the study shared experiences and discussed relevant issues that continue to pose challenges for adoption.

- *"Keep methodology updated."* - Company in paper industry. The constant change within an organization, its processes, and its day-to-day pursuit of operational excellence means that risk management must adapt and remain up to date to respond to the needs of each functional area of the organization, in addition to being best practice and part of daily routines.

- *"Migrate from Excel to stronger tools."* - Multilatina business conglomerate in the concrete sector. Not having a strong technological infrastructure to facilitate users' adoption of risk management – whether for those who enter information or for those who analyze it – makes it difficult to use risk management in practice and for quick response to the needs of the organization.

- *"Falling into the fallacy that buying a 'software package' will solve the issue of structural implenetation of ERM."* - Insurance company. In contrast to the previous perspective, to believe that a technological tool solves the implementation of all the elements of risk management is wrong. It is necessary to focus from the beginning on creating the foundations of risk management – the culture, processes, human interactions, and discussions – and, after that, consider the option of a digital system that automates interactions within risk management.

- *"Achieve integration of risk management with processes, so that the treatment of risk is incorporated into process design."* - Organization in the energy sector. Risk management does not contemplate being an exclusive issue or a process that must be carried out in isolation from the operation itself. If this happens, risk management will be perceived as a duplication of tasks, a management system that parallels day-to-day activities. If risk treatment is considered in structure or redesign processes, it will be assimilated more naturally within the organization as an element of continuous improvement.

- *"Moving from qualitative to quantitative issues, more technical, with scenarios and figures that allow us to anticipate and be more proactive, so that risk management can be used to make senior management decisions with an understanding of potential consequences."* - Multilatina business conglomerate in the concrete sector. The great challenge that risk management faces as a quantitative model is its dependence on data availability, reliability, and quality. Without a reliable and sufficient data universe, a rigorous and strategically useful quantitative analysis is not feasible. For this reason, it is necessary to incorporate into the risk management culture a model of routine collection of materialized events.

- *"Implement the three (3) lines of defense to involve other parts of the organization such as internal audit in a more active role in risk management."* - Organization in the energy sector. There are good practices, such as the model of three (3) lines of defense, that guarantee that three independent groups in the organization work as a team. The model works if fully integrated with all business processes and if those responsible for risk are properly supported and empowered to manage it (1st line), through centralized and analyzed information (2nd line), and finally through a model of assurance or independent guarantee (3rd line).

- *"The appetite or risk tolerance had not been clearly established at all levels, therefore everyone was treated the same."*
  - Energy sector company. The general perception is that the concept of risk appetite is complex and difficult to address. The first approach to risk appetite is often through valuation scales, but it shoud be understood that the concept is not limited exclusively to that. However, appetite is present in any strategic definition, such as desired presence in markets, new products, or acquisitions/mergers and is not limited to a deterministic quantified number.

- *"One of the main challenges is to take that step, to see risk management in a comprehensive manner, through multidisciplinary teams."*
  - Multilatina organization producing construction material. Multiple risk management systems within organizations, each with their own requirements, methodologies, and perspectives, generate division when seeking to incorporate risk management across the operation. That is why it is necessary to standardize risk management under one umbrella, manage it in an integrated way, and incorporate it into the culture under a single agenda.

- *"Impregnate in the DNA of the organization that the risks they identify are then treated. Currently all risks are identified but systematic risk treatment is not yet done."* - Food production company. Definitely one of the great challenges in risk management is to project the value generated and make its benefits tangible. For this reason, organizations that do not manage to cross the threshold of defining the context and assessing the risks associated with continuing to implement all steps in the risk management process will be unable to notice how risk management is evolving or how it is generating value . Through progress with a cross-sectional model, especially in the treatment, monitoring, and communication of risks, it will be possible to perceive the changes in the status of risks and the evolution of the treatment plans as well as verify the effectiveness of the design of controls and key risk indicators (KRIs).

- *"The main challenge is in the management of strategic risks and how to make risk maps a real tool for decision making."* - Multilatina organization producing construction material. It's not easy to transform the results of a risk map into timely action. One of the challenges posed is to provide actionable and proactive information that contains the endorsement to transcend prevention or mitigation actions at once.

- *"It is important to highlight the difficulty in establishing KRIs instead of KPIs. The focus of our work nowadays is on the construction of a strong and integrated system with corporate indicators which permeate the various areas of the company, considering a chain with different risks and their respective aspects and impacts."*
  - Energy sector company. Organizations may have difficulties when trying to establish KRIs and differentiate them from key perforamnce indicators (KPIs). In general, KPIs are typically designed to measure performance. On the contrary, KRIs must be tied to variables related to the causality of the risk to allow projecting or forecasting a certain situation or early warning against the risk being measured.

51% of the organizations recognize that organizational culture problems are a challenge to risk management implementation.

THE FACILITATORS

Along with the challenges, leaders in risk management in Latin America also acknowledged that there are common facilitators that contributed significantly to the implementation task within their organizations.

Just as there are important challenges for the implementation of risk management, risk management leaders in Latin America identified the following common facilitators that significantly contributed to the implementation task within their organizations:

Have a manual that adapts methodologies to the organization and provides the necessary guidelines for their implementation and adaptation to the organizational culture.

Provide training that is sensitive to personnel and that leverages cultural transformation towards a risk management orientation.

Internal control models should encourage implementation of a strong risk management scheme.

Systematic recording of risk management should use advanced applications and move away from Excel databases to other tools more adjusted to the orgnaization's needs.

The endorsement and sponsorship of senior management is essential to widespread adoption of risk management in the organization.

Provide elements of decision making in strategic projects to project management or initiatives for timely decision making.

Adequately assume accountability for risk management so that strategic risks emanate from the business itself and treatment plans are designed and managed by the owners of the processes and the risk as opposed to being authoritatively established by other control areas.

When **risk management is part of corporate governance** and internal control structures, it is easier to interact with senior management so that decision making is more objective.

Integrate risk management into the strategic planning of the organization and use it as a means of planning, management and measurement.

The focus should be on **generating culture** identifying measures, and creating action plans which are then followed up on.

It's key that both risk and action plans are **centralized so that there is visibility into risks.**

HOW TO DEMONSTRATE THE GENERATION OF VALUE

One of the main challenges of risk management is its difficulty in making visible the value it brings to the organization. Key to projecting that value is the ability of risk managers to quantify their effectiveness and the commitment of senior management.

One of the main challenges for risk management is the difficulty in projecting the actual value it generates to the organization, a situation attributable in part to difficulties in quantifying or perceiving its performance effectives in the normal execution of activities in the organization. In different Risk Management Leader Forums, the risk managers who participated in these sessions responded to questions such as how do they manage to demonstrate to senior management value generation through risk management and what are the difficulties encountered? The participants discussed several relevant points including:

Risk management is an intangible that cannot be easily quantified. When risk management is involved with senior management and strategic planning, together with a solid definition of risk appetite, the need for and value created by risk management become more evident. *"When the impact of materialized risk is quantified, it is there where the organization is convinced of the value of risk management. When it is possible to demonstrate how a risk impacts the organization, understanding of the value generated by risk management permeates the organization."* - Food production company.

Materialization of risks makes the organization aware of the need to manage them. Usually the attention of the organization turns to focus on risk management only after events occur that put their reputation, sustainability, people, or assets at risk. *"Unfortunately I have to say that it is because of the materialization of the risks. In our organization, we have connected the topic of risk management with that of crisis management. We found that the unleashing of crisises was due to poor risk management. That was when the organization became convinced that it was better to manage risks before having to manage a crisis."* - Multilatina food production company.

The link between key indicators and risk management is essential to the relationship between measurement, financial result, strategy, and risks, which creates value through proactive decision making. *"The organization imposes a challenge to making the day-to-day impact of risk management more visible. This is achieved by linking the balanced scorecard indicators with risk management. The challenge is to demonstrate how better or worse risk management impacts the results of the balanced scorecard or process indicators. This can be a more tangible or obvious way to*

demonstrate value." - Company in the transport sector.

The key is visibility. Forums in which company risk management issues as well as their frequency are discussed determine how much interest is generated in the organization to implement risk management, make it more dynamic, and keep it updated. *"There are monthly risk operating committees, however there is also proximity and interaction with the risk and audit committees of the board of directors."* - Multilatina business conglomerate in the paint sector.

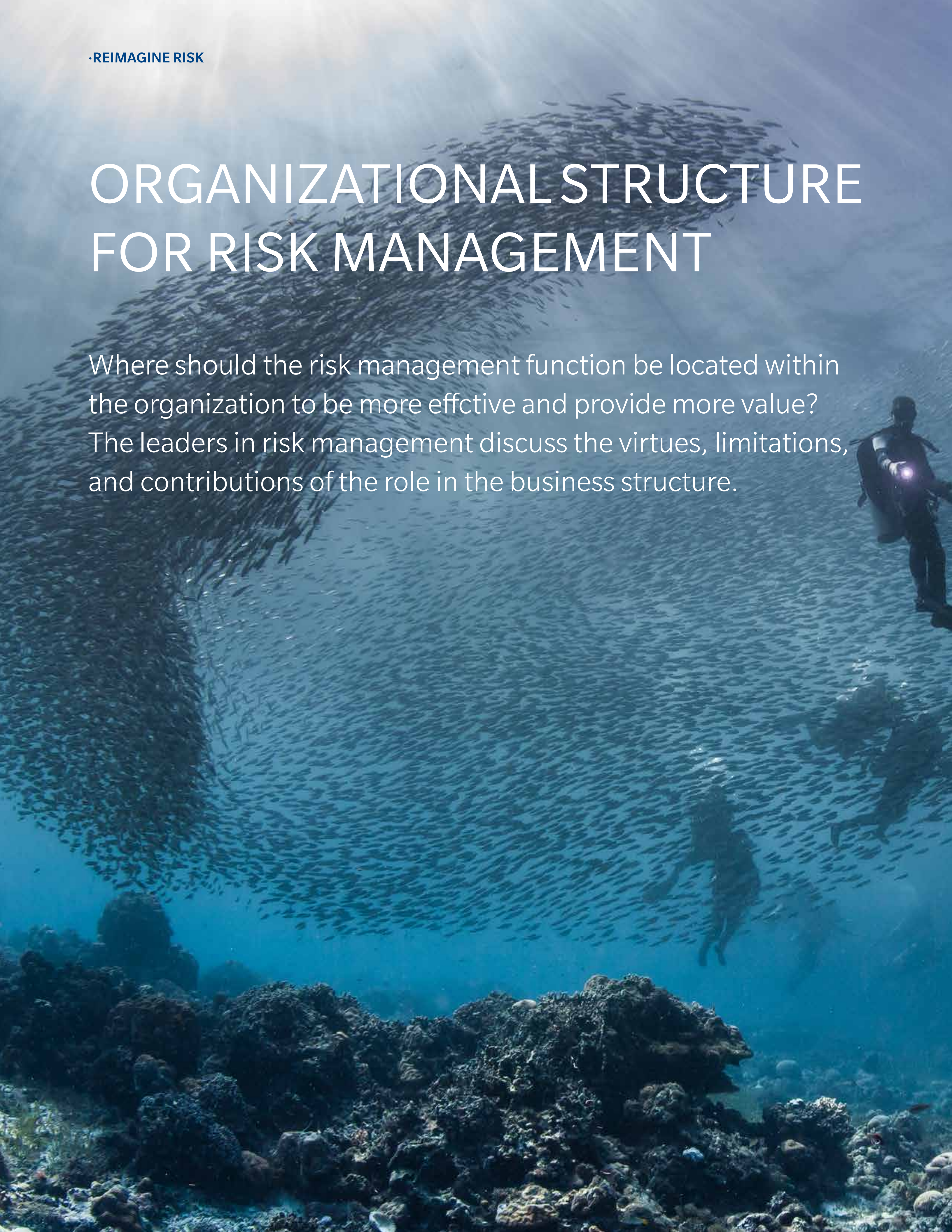
When the initiative to implement risk management in the organization comes from senior management there is no great difficulty in demonstrating the value it generates. Several leaders agreed that the support of top management has been fundamental for its structuring and implementation. The participation of the general management or chairmanship in monthly risk committees where all vice presidents/managers or directors present their risks and their advances makes the issue visible. The results of these periodic interactions are scaled in turn to the respective risk or audit committees of the board of directors/board which makes them even stronger. *"The endorsement and sponsorship of senior management is very important, as is the commitment of the rest of the organization to consolidate a visibility platform in risk management. We begin to take strategic risks to scenarios where they are given importance. For example, nowadays corruption and ethics issues are concatenated with environmental and reputational issues in spaces that have served to study the domino effect between risks and how we should prepare ourselves. This has undoubtedly demonstrated the value of risk management."* - Multilatina retail company.

The example of providing more representative value is the discussion generated with the board of directors. With the risk approach applied to business decisions for the boards of directors or boards, evaluating the initiatives to achieve the objectives of creating value for the benefit of shareholders takes place in an environment of intense discussion and with solid decision criteria since today we must identify which risk considerations exist for each initiative.

For companies that have a risk management system, the search for organic growth through income and earnings is weighted against considerations of what is their integrated portfolio of risks, their absorption capacity, and the required backup capital. As such, they are constantly navigating the definition of capital return of the initiative and the associated risk tolerance.

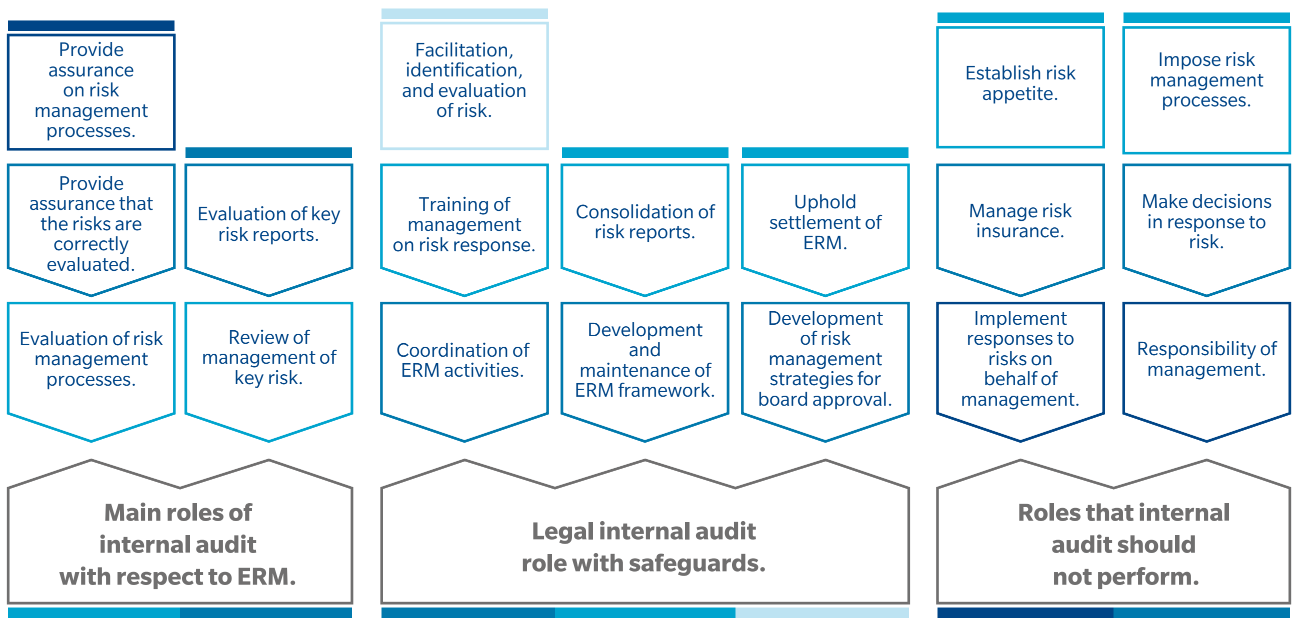
ORGANIZATIONAL STRUCTURE FOR RISK MANAGEMENT

Where should the risk management function be located within the organization to be more effctive and provide more value? The leaders in risk management discuss the virtues, limitations, and contributions of the role in the business structure.



Organizations have concerns about where risk management should be located in the company so that the practice is more effective. That is why in the Risk Management Leaders forums, where risk managers participated in focus groups for this this study, the virtues and limitations of the organizational position of risk management in their organizations were discussed, as well as how much this organizational location contributes to the effective adoption of risk management.

Graphic #7



Source: IIA POSITION PAPER: THE ROLE OF INTERNAL AUDITING IN ENTERPRISE-WIDE RISK MANAGEMENT, January 2009.

RISK MANAGEMENT AND AUDITING

"Previously there was a hybrid between audit and risks; it was a complex issue because it was important to differentiate the roles of these two functions. Currently, the company has a corporate governance structure that has served to differentiate these functions. The board of directors delegates the function to a risk management committee, and does not depend on the chair or the administration, but reports directly through the committee which contributes to the flow of information and the positioning of the function." - Company in the financial sector.

On some occasions risk management has emerged as an initiative within the area of internal audit given that some reference frameworks for audit activities such as RBIA (Risk Based Internal Auditing) of the IIA or the reference *"Internal Control-Integrated Framework"* of COSO is based on risk. However, at a certain point these two functions must split mainly because the audit function must be independent and cannot become *"judge and jury"* in risk management.

The nature of risk management activities and audit are closely related so that sharing information with regards to results obtained in terms of risks from each area of responsibility allows for the improvmeent of the management cycle in both functions. As an example, the chart below shows a guide to the role of Internal Audit within Risk Management.

SUSTAINABILITY AND RISK MANAGEMENT

"Risk management depends on the area of sustainability and is linked to the chairmanship. Having the support of senior management has been fundamental. Before we depended on the financial area and it did not work so well, transferring risk management to the area of sustainability has flow more." - Multilatina organization in the packaging sector.

"The risk management of the company is divided into two Risk Directorates: The Operational Risk Division and the Sustainable Risk Division. Recently, a global CRO was hired to strengthen integration. This structure facilitates the implementation of risk management in the company, mainly by the local integration of the same and the global guidelines." - Multinational company in the food sector.

"Our organization does not have 'chief risk officer' position. The CEO is the chairman of the Executive Risk Committee. Risk management is handled by the CEO using the Executive Risk Committee as the vehicle to the supervising body. He is in charge of the responsibility of ERM." - Insurance company.

Risk management and sustainability are closely linked. If properly executed, sustainability policies promote growth and reduce risk. In fact sustainability covers all aspects of the company's ability to manage risk and grow its business.

This is why the Dow Jones Sustainability Index (DJSI) is based on an analysis of corporate performance in the economic, environmental, and social arenas, assessing specific issues such as corporate governance and risk management.

STRATEGIC PLANNING AND RISK MANAGEMENT

"Functionally risk management is considered as part of strategic and financial planning, which allows for relevance and visibility. In addition, as a process, risk management is cross-cutting in the organization and has direct access to the board of directors." - Natural gas sector company.

In order to understand the dynamics between strategy and risk management, it is important to start from a common definition of what strategy means in an organization. For purposes of this study, we will assume the definition of strategy as a series of decisions about the business that determine the direction and orientation of the same. Strategy defines and articulates the value proposition that an organization brings to the market and must incorporate risk parameters and their limits for their evolution.

An organization should view business risk management as an integral part of its value proposition. Strategic planning is also oriented towards the search for a successful future business model that will thrive despite the perceived risks. Perhaps more than in any other area, it is in strategic planning where risk is "*opportunity*."

A precise statement is that enterprise risk management (ERM) and strategic planning should be seen as complementary issues and not as independent activities. If the strategy is formulated without identifying the risks involved along with their required assessment, treatment, and monitoring, then the strategy will be incomplete and uncertain.

RISK MANAGEMENT AND INSURANCE MANAGEMENT

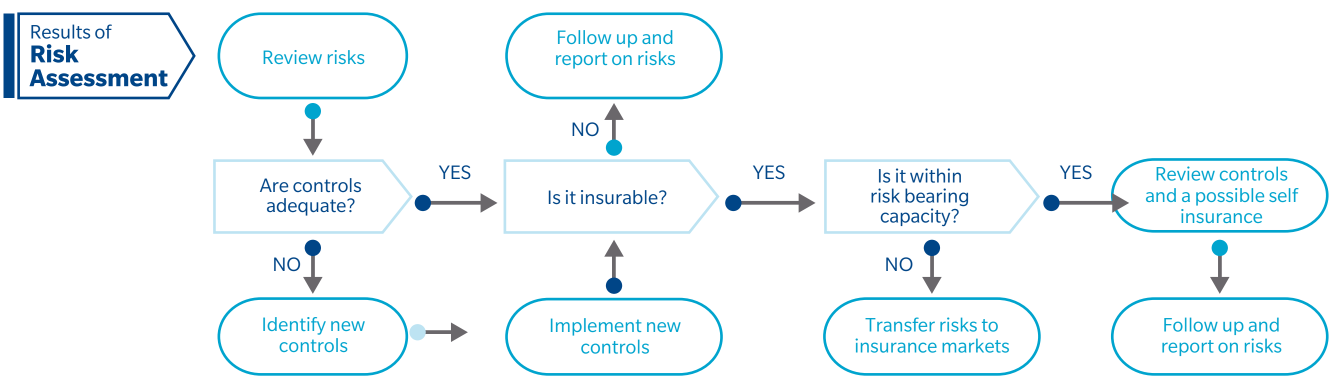
"The two managements responsible for the company's risk management (insurance and corporate risks) are under a single directorate, which facilitates the implementation of risk management processes and tools." - Hydrocarbons sector organization (downstream).

Before the risk management vision existed, insurance management was based on transactions enabling available policies to transfer some traditional risks in the organization.

Integrating the insurance process into risk management expands the transfer model, whereas if in compliance with the risk management process, risks are first identified, evaluated, and analyzed and then the treatment is determined, including the transfer alternative through insurance policies.

All of this involves answering questions such as: Are the controls adequate and sufficient? Is the risk insurable? Is the risk within the bearing capacity?

Graphic #8



MULTIPICITY OF RISK MANAGEMENT SYSTEMS

"There is no position linked to senior management that sponsors or integrates the actions of the three different areas responsible for the company's risk management: Internal Controls (SOX), Insured Risks, and Business Risks. For this reason, there is great difficulty in implementing integrated risk management in the organization." - Aerospace sector conglomerate.

In this study we have already discussed the difficulty of integrating risk management when the company has multiple areas in which there are independent risk management initiatives and where different models are in use, each with specific characteristics. By standardizing risk management under the same umbrella or by managing it in an integrated manner, the systems implemented such as COSO, COBIT, SOX, ETICA, SARLAFT, operational risk, environmental risks, health and safety at work, market, credit, etc. would become more harmonious and more operationally efficient, underpinning the formation of synergies and moving away from siloed work.

RISK MANAGEMENT SCOPE

The effectiveness of risk management is directly related to its involvement in the strategy and operation of the company, as well as its vision of transversal responsibility.

Risk management can have different scopes within the organization, which definitely affects its effectiveness and level of integration. That is why in the Risk Management Leaders forum, the risk managers that participated in focus groups for this study went deeper into the following questions:

What is the scope of risk management in your organization? What are the advantages and disadvantages of applying it at the strategic level? In processes? In projects? In supply chain/purchases? In contracting? In the distribution chain?

Graphic #9

Strategic	Processes by areas/ operations	Projects	Contracts/ supply chain	Investment projects/ acquisitions	New products	Integral	Participants in the focus group sessions
✓	✓						Paper business sector
						✓	Financial institutions sector
✓	✓				✓		Financial information business sector
						✓	Oil and gas sector (upstream)
	✓						TIC sector
✓	✓	✓	✓				Transport sector
✓	✓		✓				Packing multilatina organization
✓	✓			✓			Retail multilatina firm
✓	✓			✓			Natural gas sector
	✓		✓	✓	✓		Financial Institution
✓	✓		✓				Food multinational organization
						✓	Oil and gas sector (downstream)
	✓						Aerospace sector conglomerate
✓	✓						Energy sector
	✓						Construction materials production multilatina

Some advantages and disadvantages:

ON THE POSITIVE SIDE:

Appearance and lessons learned: With scope both at a strategic level and at processes and sub processes levels, you have the advantage that those who handle risk on a day-to-day basis have direct involvement in its mapping and management. Additionally, having a single corporate methodology under the risk area provides a desired standardization, facilitating the management and dissemination of lessons learned and avoiding work by silos, that is disaggregated, or undertaken under different methodologies.

Transversality: The advantages of taking a broad approach to risk management, including at strategic and process levels, are the sharing of risk with the different areas involved as well as the vision of transversal responsibility. Furthermore, risk treatment plans can be articulated in their integral design, encouraging collaborative work and increasing their effectiveness.

ON THE NEGATIVE SIDE:

Lack of integration. The scope of risk management in the organization is still perceived as "*of limited focus*", has been implemented only at some levels of the organization, and does not have general guidelines integrated to the company vision. In these cases the risk area is still seen by other areas of the company, especially by those who are in charge of the "*core*" business tasks, as a bureaucratic area and "*excessive care.*"

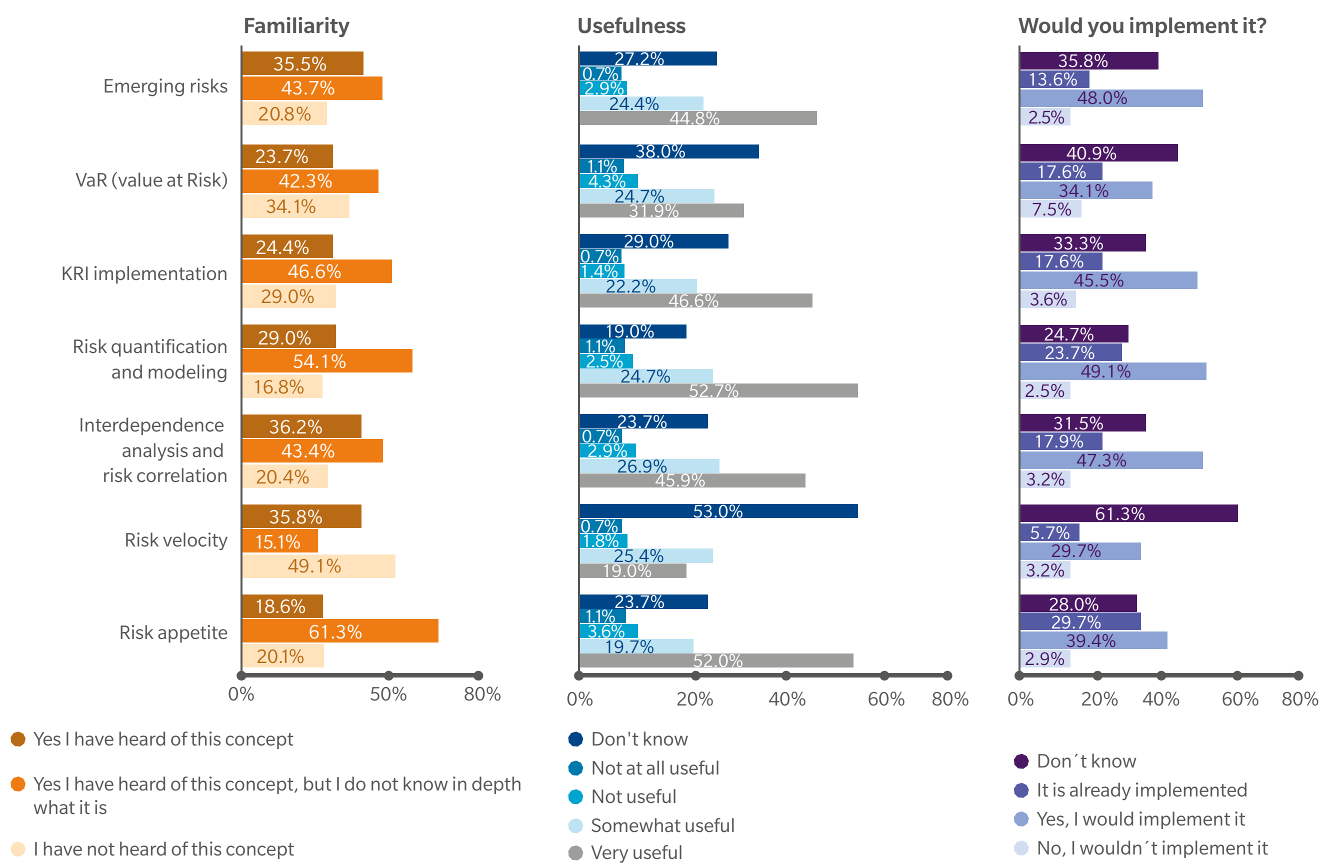
Late participation in the valuation of projects or acquisition initiatives: Sometimes investment projects are confidential and risk management cannot intervene before the purchase or before the start of a certain project, but is done later.

FAMILIARITY AND USEFULNESS OF SOME CONCEPTS IN RISK MANAGEMENT

How well are key concepts of risk managment known and how are they being applied, whether risk appetite, value-at-risk (VaR), key risk indicators (KRI), or risk quantification and modeling?

Graphic #10

HAVE YOU HEARD OF CONCEPTS SUCH AS RISK APPETITE, RISK VELOCITY, ANALYSIS OF INTERDEPENDENCIES AND RISK CORRELATION, QUANTIFICATION AND RISK MODELING, IMPLEMENTATION OF KRI'S, VAR, AND EMERGING RISKS? IF YES, COULD THESE CONCEPTS BE USEFULLY APPLOED IN YOUR ORGANIZATION?



Risk appetite quantification, modeling analysis of interdependencies, and correlation of risks. In terms of familiarity, the study finds that the best known topics are risk appetite and risk quantification/modeling followed by analysis of interdependencies and risk correlation. All these issues are perceived as high-value issues in addition to having a high level of implementation intention from those responsible for risk management in Latin America. This corresponds to the growing need for risk management to adopt a quantitative dynamic, providing limits and guidelines for making objective decisions with figures/data to support it.

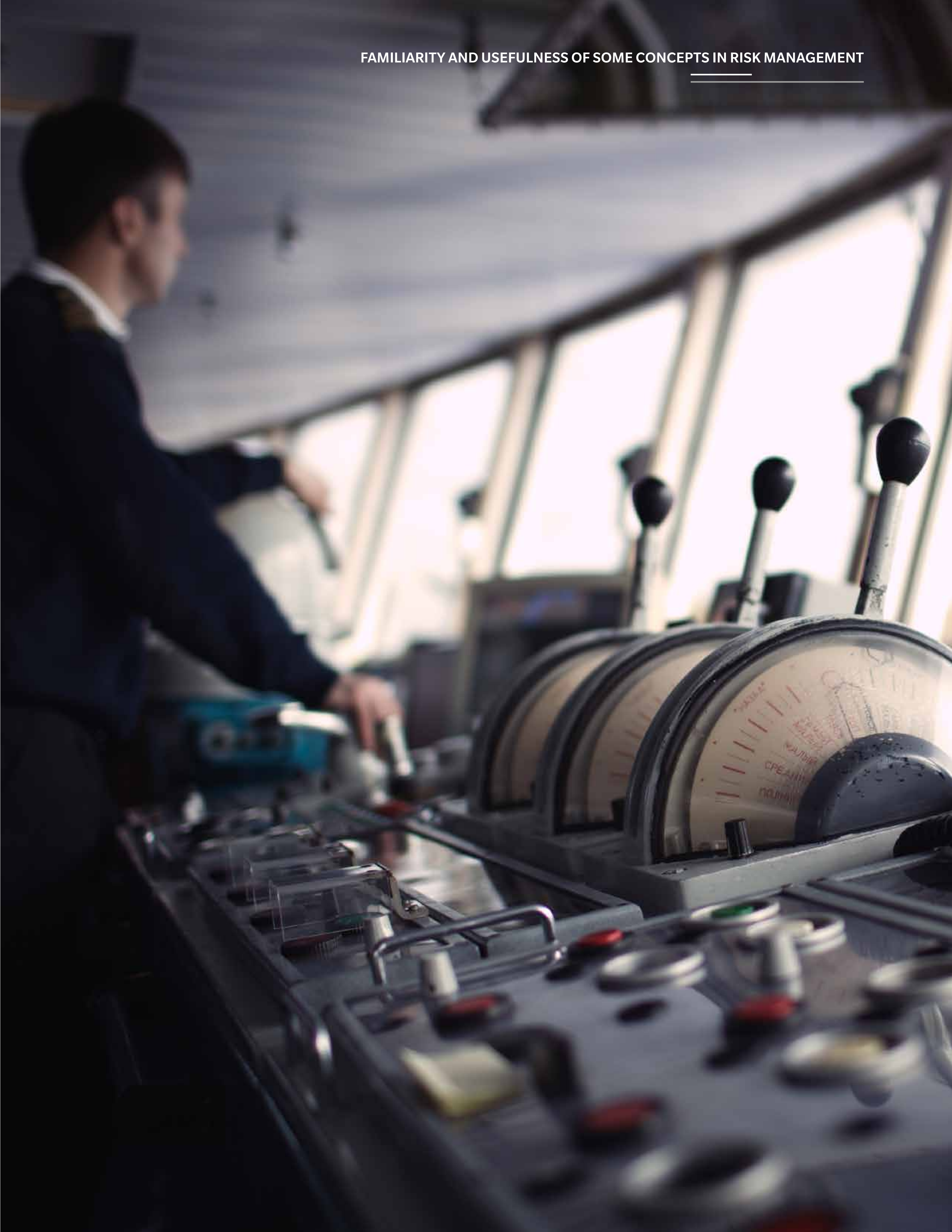
Risk velocity. A less familiar topic is risk velocity with nearly half of the participants saying they have not heard of it and 36% saying they have heard about it but do not know what it is. Although a standard definition of the concept of risk velocity has not yet emerged, this concept began to appear in risk management consulting literature several years ago and is generally defined as the speed in which a risk manifests itself and how quickly its impact is felt. Risk velocity is often the third dimension to be considered after probability and impact.

Key Risk Indicators (KRI). Despite being perceived as a very useful topic by those who know it, key risk indicators (KRI) is a subject not known in depth in the region; surely by advancing the risk management maturity levels of companies in the region qwitih sophisticted risk monitoring schemes, KRIs will become a fundamental element in risk management programs. The intention to implement this concept is high (46%) followed by a limited percentage of companies that have already implemented it (18%).

Emerging risks. Despite being a concept with significant awareness – four (4) out of every five (5) Latin American companies have already heard about emerging risk and it is seen as "*very useful*" (45%) – its degree of implementation is still low in the region (14%). The above, together with a high level of implementation intention (48%), allows us to conclude that emerging risks is an issue in development and of importance to risk leaders and management in the region.

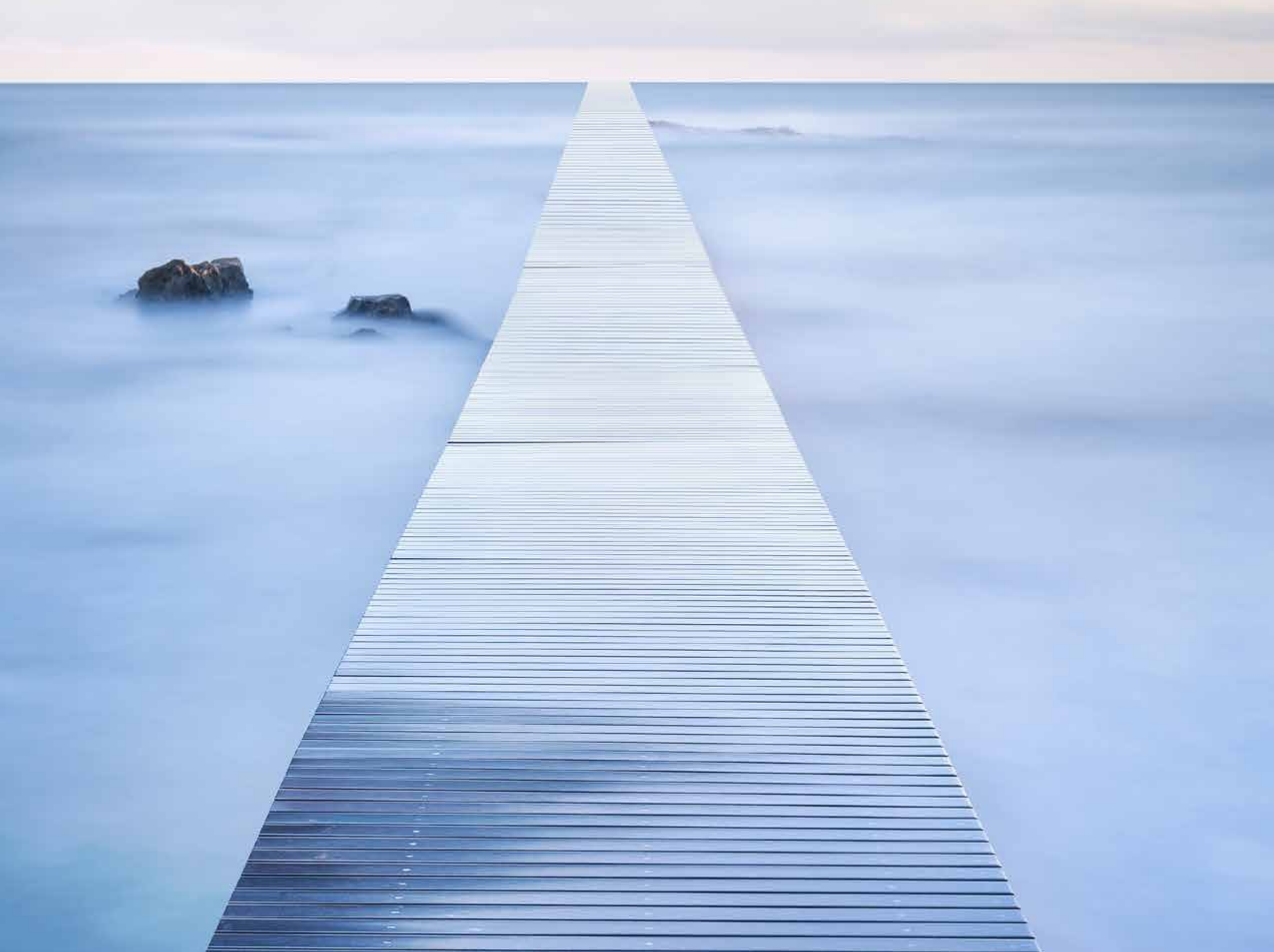
Other interesting topics being considered in risk management in organizations in Latin America are:

- Transition processes from version 2008 ISO 9001 to version 2015. This new quality management model involves implementing risk management in the organization. Additionally, this new model involves contemplating identification and management of opportunities.
- Analysis of trends as an input for the assessment of strategic risks.
- Risk management beyond the limits of the organization in order to improve the quality of risk management of interest groups and third parties linked to the organization such as suppliers, contractors, and supply chain vendors.
- Study of interrelationship of risks with strategic objectives.
- Measurement of risk management and its performance (ERM KPIs).
- Expansion of supervised industries in the application of corruption regulations, money laundering, and terrorism financing (not just exclusively applied to the financial sector or the real estate sector).
- Higher incidence of reputational risk, given the growing use of social networks, which increases the speed of information dissemination and shortens response times.
- Review of organizational resilience.
- Inclusion of Black Swan analysis in risk assessment exercises.
- Use of Big Data to perform predictive analysis.



LOOKING TOWARDS THE FUTURE - WHERE ARE WE GOING?

What do Latin American companies need to implement risk management best practices? Leading managers share a holistic and preventive vision, based on quantitative data.



What should Latin American companies do in anticipation of and to implement these trends?

In the Risk Management Leaders forums, the risk managers that participated in focus groups for this study deepened this question with regards to next steps in the evolution of risk management. The following is a summary of the conclusions reached:

A GREATER SCOPE, GREATER RESILIENCE

Nowadays risk management has broadened its scope to not only address an organization's particular risk, but also the system that surrounds it. *"There is a tendency to account not only for how risk management is in the company, but also in other entities in the chain: suppliers, allies, and even customers."*

BECOME MORE QUANTITATIVE

A path through which risk management will continue to be directed and has been repeatedly mentioned in this study is for risk management to go from being qualitative to quantitative, with more value placed on information focused on figures as well as tangible and quantifiable data.

ADOPTION OF A HOLISTIC AND PREVENTIVE VISION

Risk management is expected to evolve towards a predictive and preventive vision as opposed to being reactive, as it is in most cases today. This holistic vision is only possible through the interaction of various actors in the organization whose contributions broaden the vision and spectrum of action of risk management. This is reinforced through active communication and ensuring that risk managers have an integrated vision.

RISK MANAGEMENT IS NO LONGER OPTIONAL

Another fundamental pillar around which revolve several problems, challenges, and opportunities for those in charge of risk management in Latin American organizations is giving the necessary emphasis to risk management in the organizational culture. It is imperative to incorporate it into operations and overcome the perception that it is a matter of compliance. In the focus groups it was discussed that just as in due dilligence processes many financial, business, and market elements are evaluated, risk management must also be considered as a differentiating element when valuing a company. *"Today a risk management system is a must and not just desirable."*

GREATER REGULATION THAT ADDRESSES IT

Many regulations contemplate the implementation of risk management – some international regulations are being updated and other legislation is emerging in response to market demands. Some examples are the legislation in Latin America for the administration of risks of money laundering and financing of terrorism (LAFT) (see figure), while another one is the update of international standards related to quality.

The recently updated ISO 9001 version 2008 to version 2015 focused on risk management as an important element, which means that any company wishing to be certified in ISO 9001 version 2015 must speak the language of risk management.

Nowadays, applying an ERM is a duty, is a "Must."

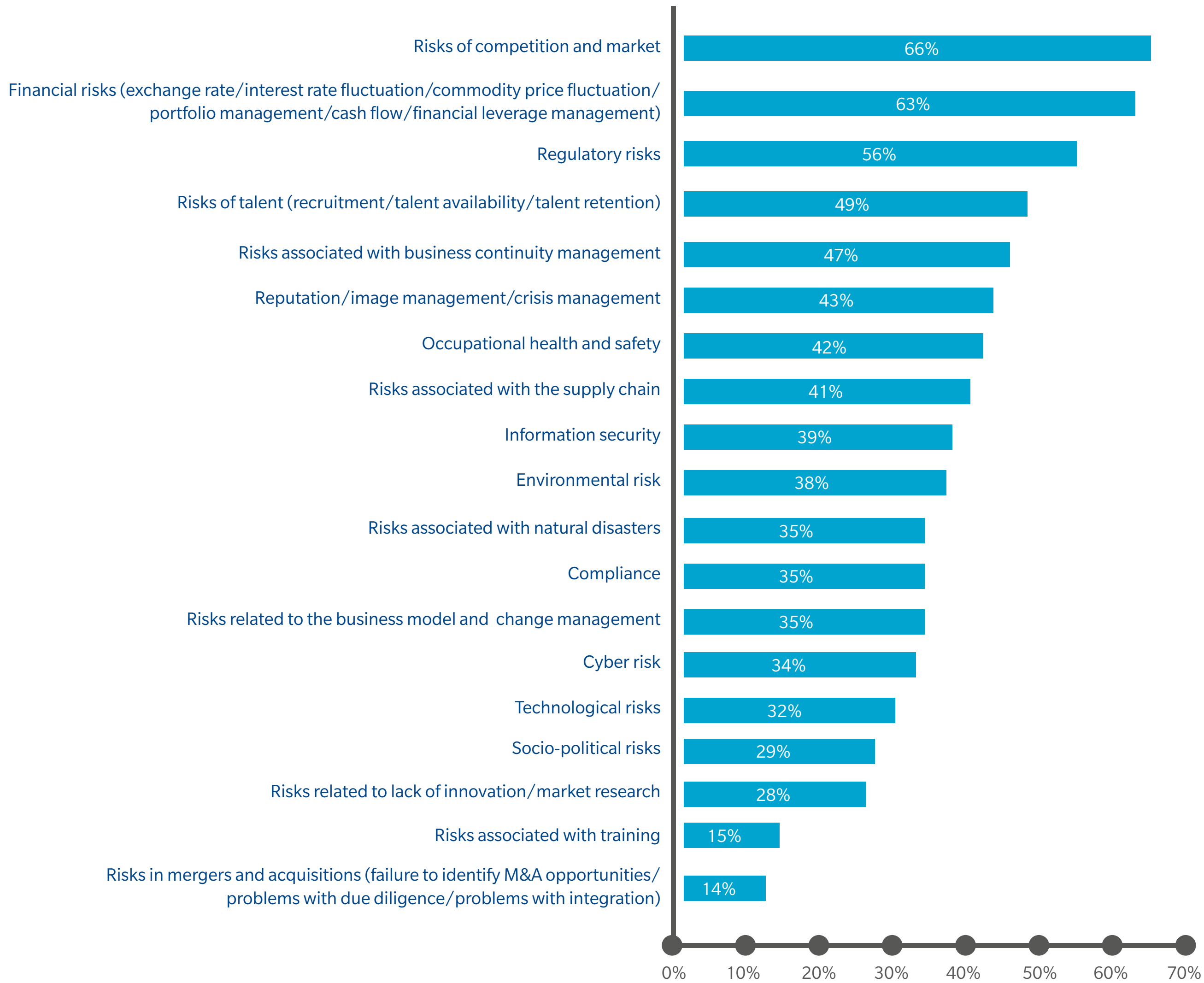
TOP RISKS IN THE REGION

The risks associated with competition and the market, financial risk, and regulation are the issues that most concern Latin American organizations, with a significant increase in risks related to human talent, reputation, and business continuity.

It has always been of special interest to those in charge of risk management to know the prioritized list of business risks for the region, for their country, and for their sector in order to compare themselves and carry out due diligence as to the risks coming over the horizon. Below we present the most important risks for the region.

Graphic #11

WHAT ARE THE TOP 10 RISK AREAS FOR YOUR ORGANIZATION?



In order of importance, this year the region focused on competition and market risks, financial risks, regulatory risk, human talent risks, and those related to business continuity.

When comparing this result with that of three years ago, the concerns that Latin American companies have regarding risks have varied.

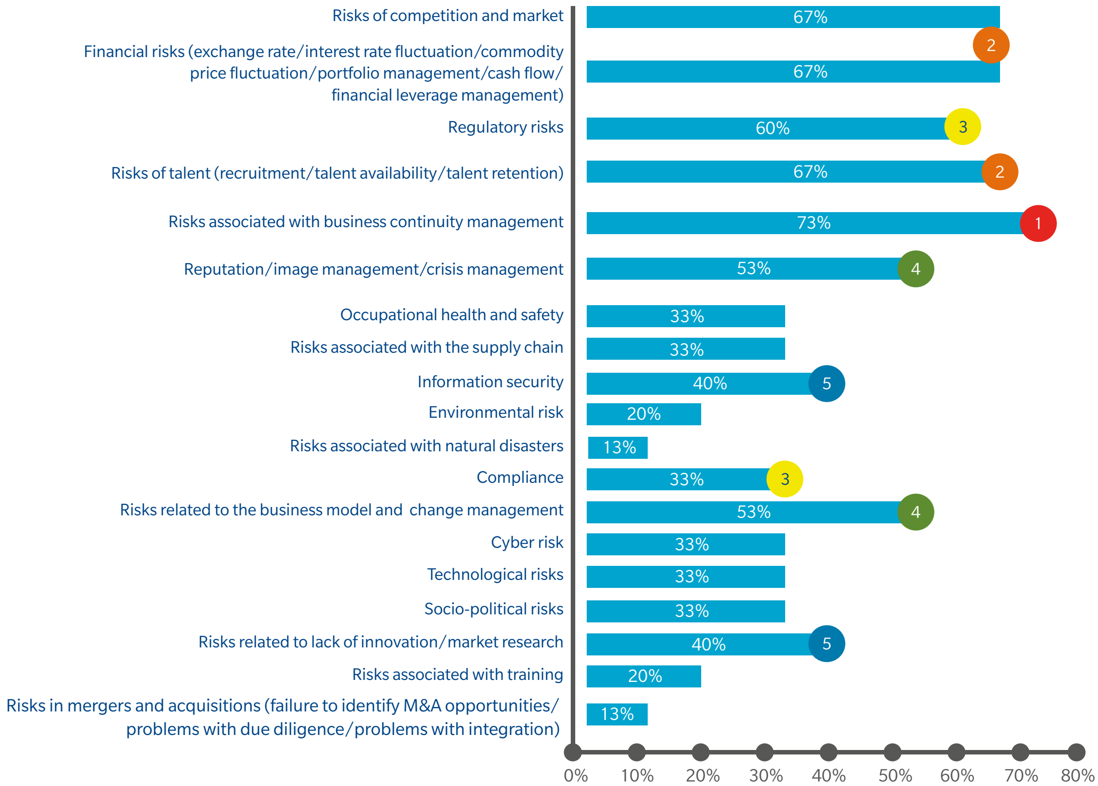
Graphic #12

TOP 10 ANALYSIS

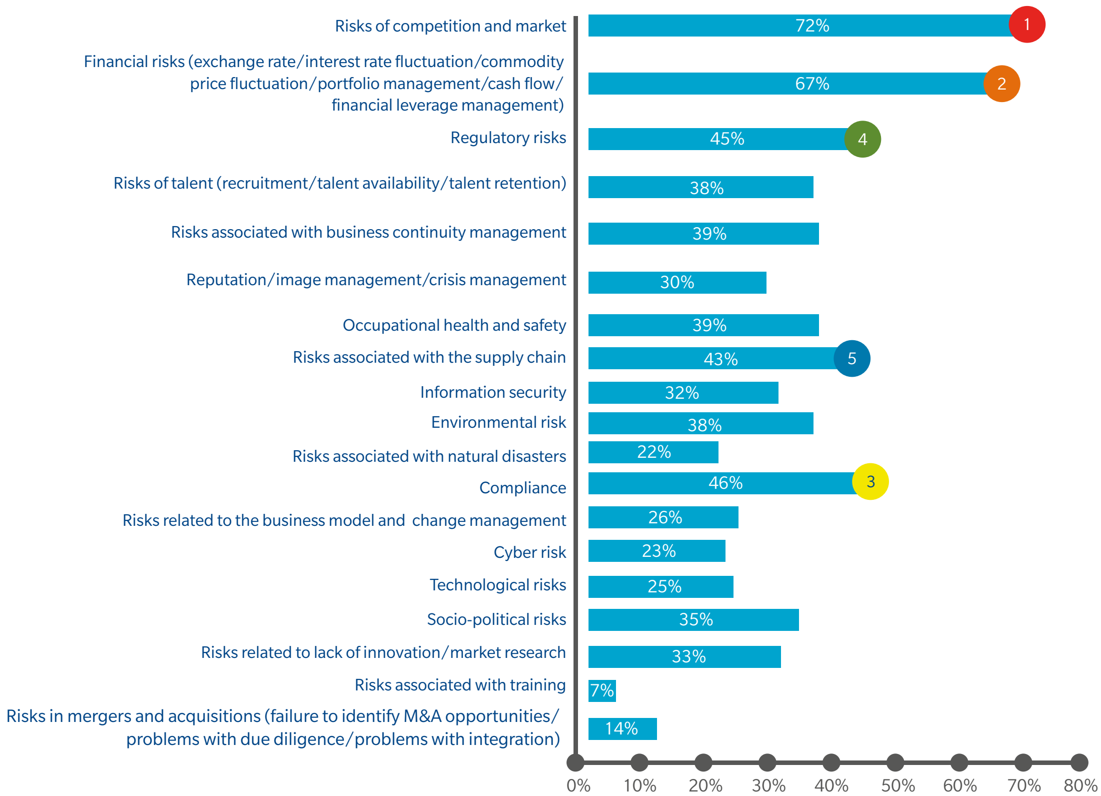
Business Risks in LAC 2017	Trends 2015 -2017	Position	Business Risks in LAC 2015
Competition and market risks	↑	1	Financial
Financial risks (fluctuation of interest/exchange rate/fluctuation of a commodity price/portfolio management/cash flow/leverage management)	↓	2	Talent risk
Regulatory risk	↔	3	Regulation and legal
Talent risk (recruitment/availability of talent/retention of talent)	↓	4	Environmental
Risks associated with business continuity management	↑	5	Operational risks
Reputational risk/image management/crisis communications management	↑	6	Business continuity
Occupational/industrial health and safety	NEW	7	Sociopolitical
Supply chain risks	NEW	8	Reputational risk
Information security	↑	9	Market and customer
Environmental risk	↓	10	Information security

*Source: "LA GESTIÓN DE RIESGOS EN LATINOAMÉRICA, SITUACIÓN, EVOLUCIÓN Y RETOS. EL CAMINO HACIA UNA GERENCIA DE RIESGOS EFICAZ", Marsh Risk Consulting, RIMS, November 2015

Graphic #13
ARGENTINA

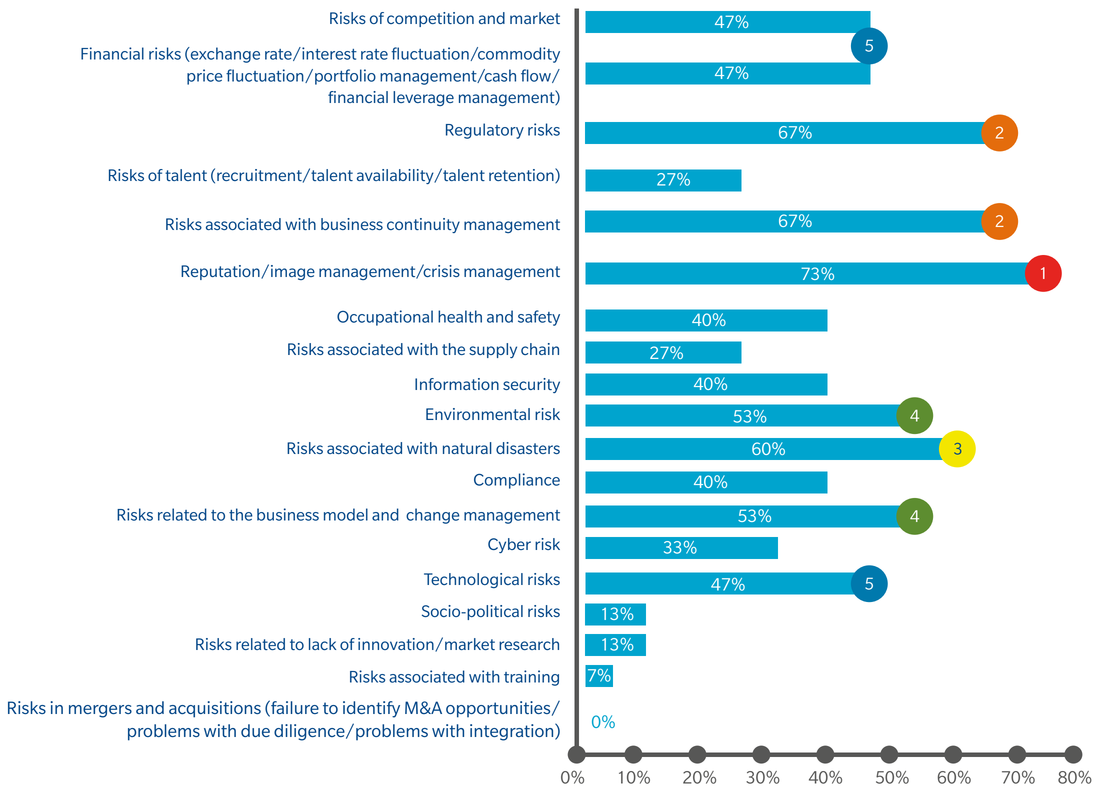


Graphic #14
BRAZIL



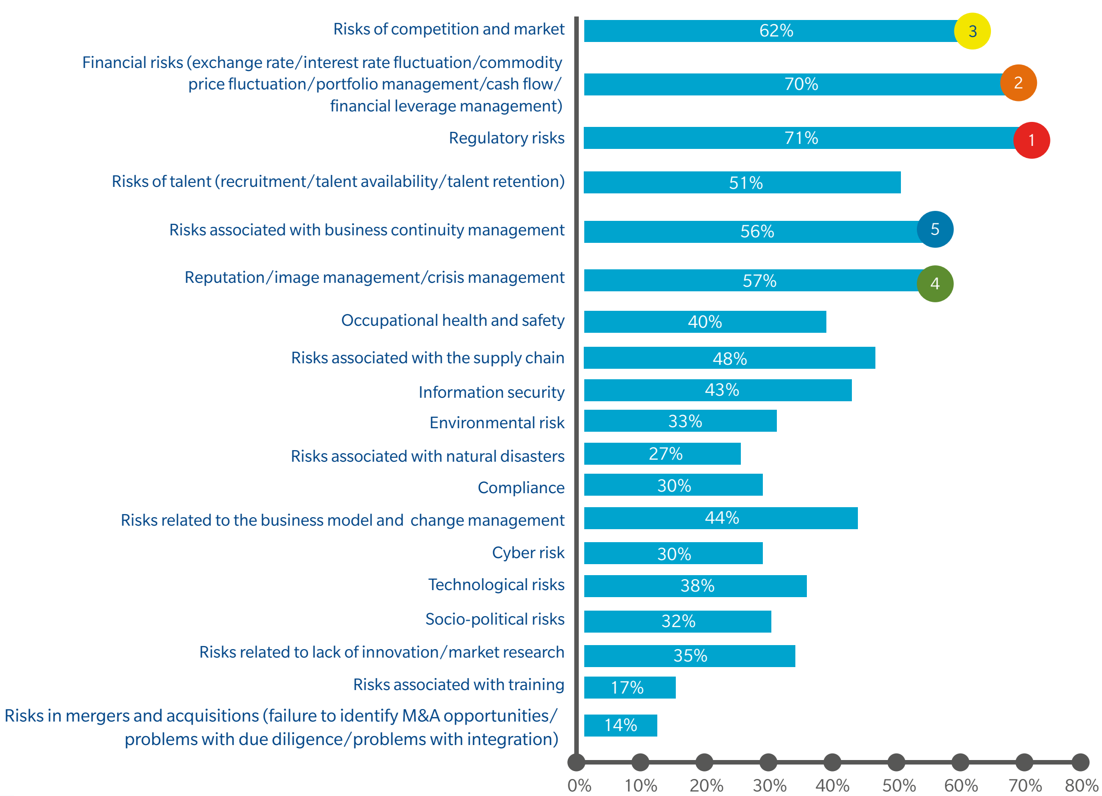
Graphic #15

CHILE



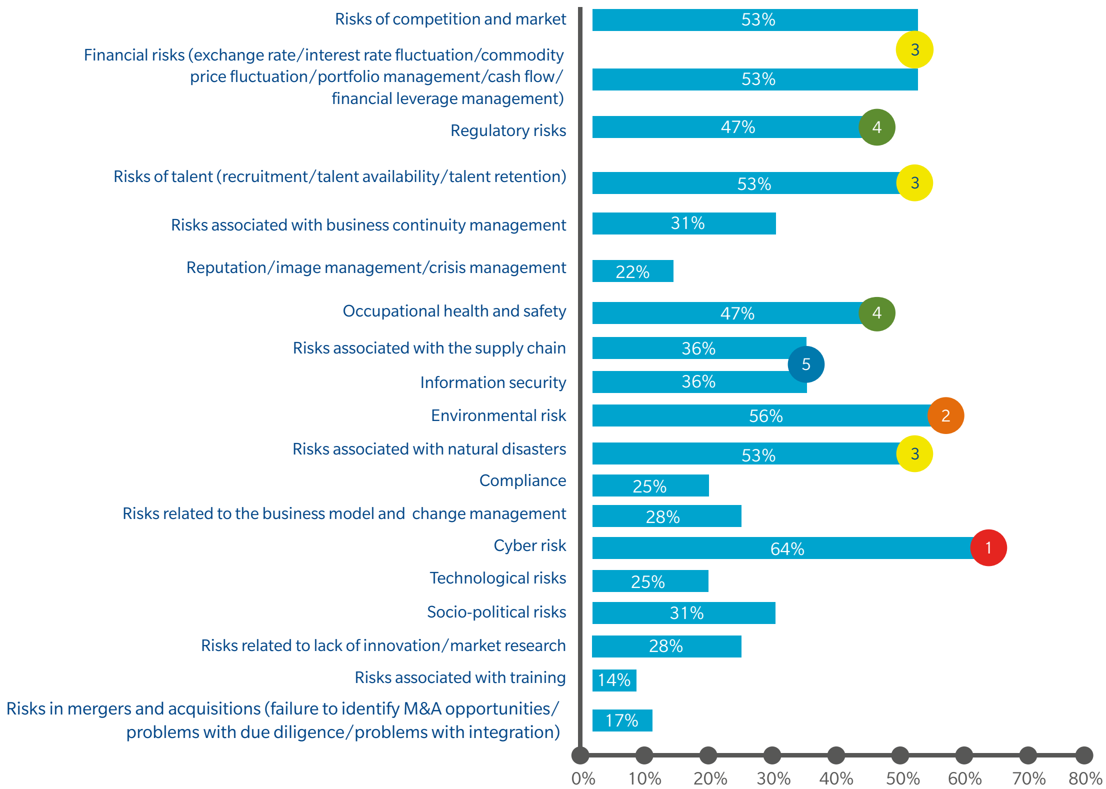
Graphic #16

COLOMBIA



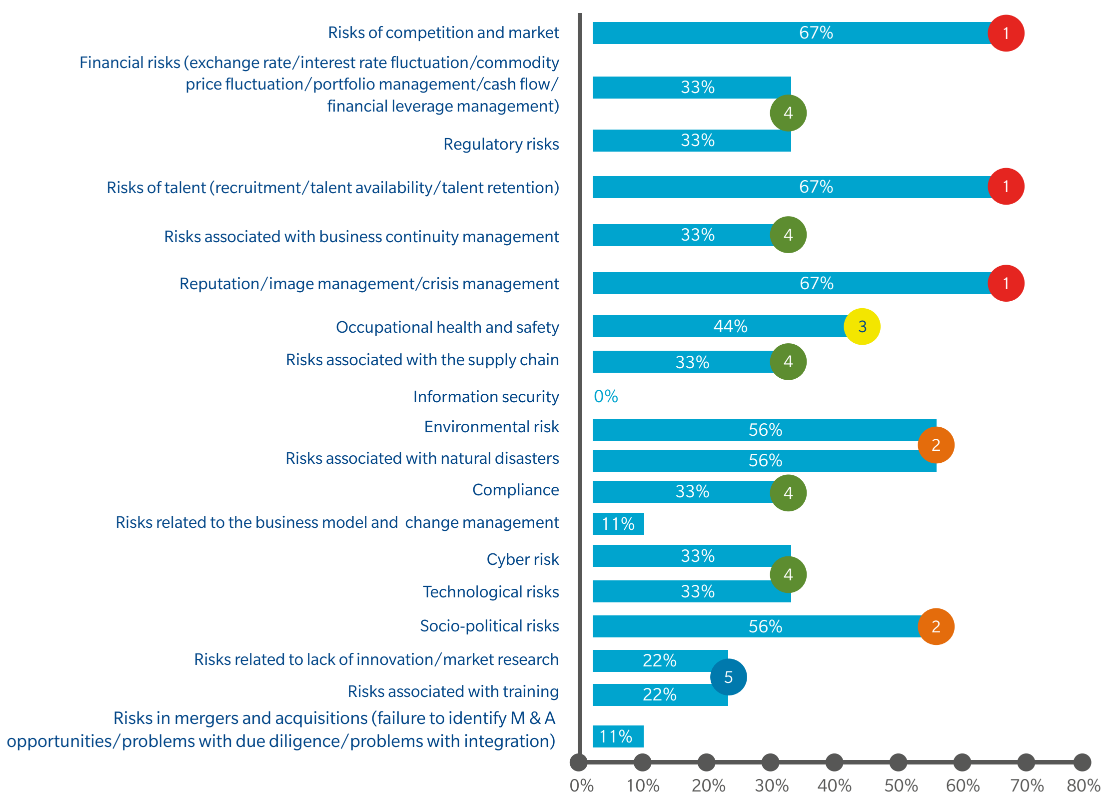
Graphic #17

MEXICO



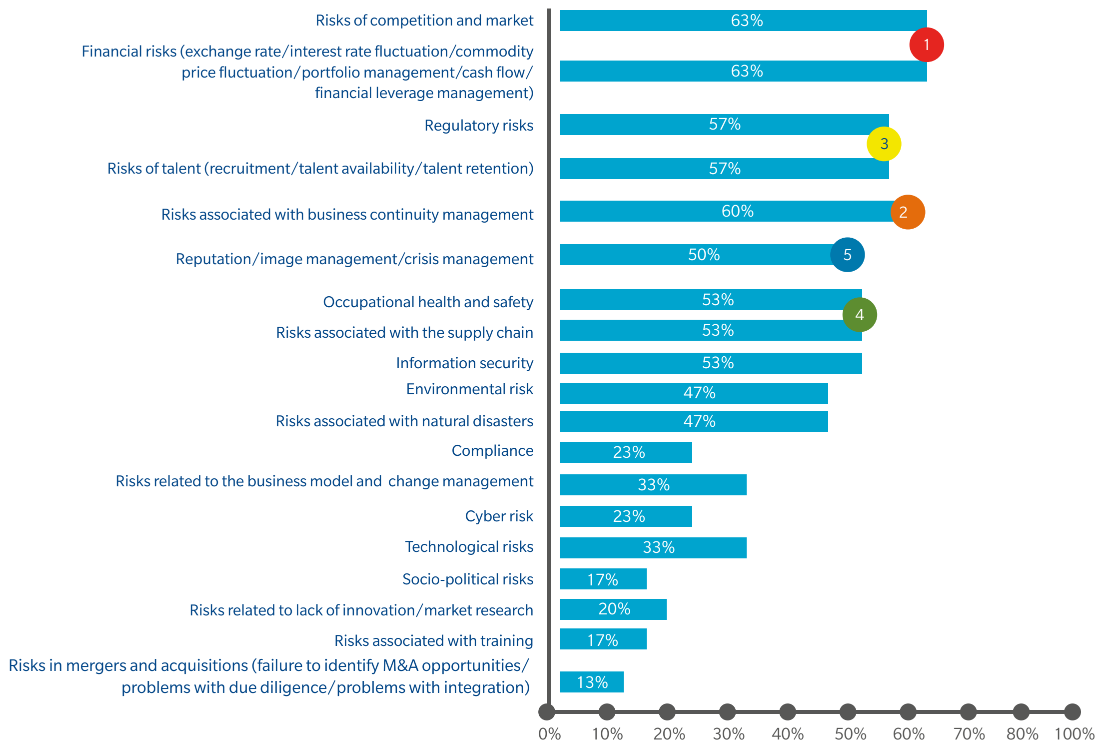
Graphic #18

PANAMA



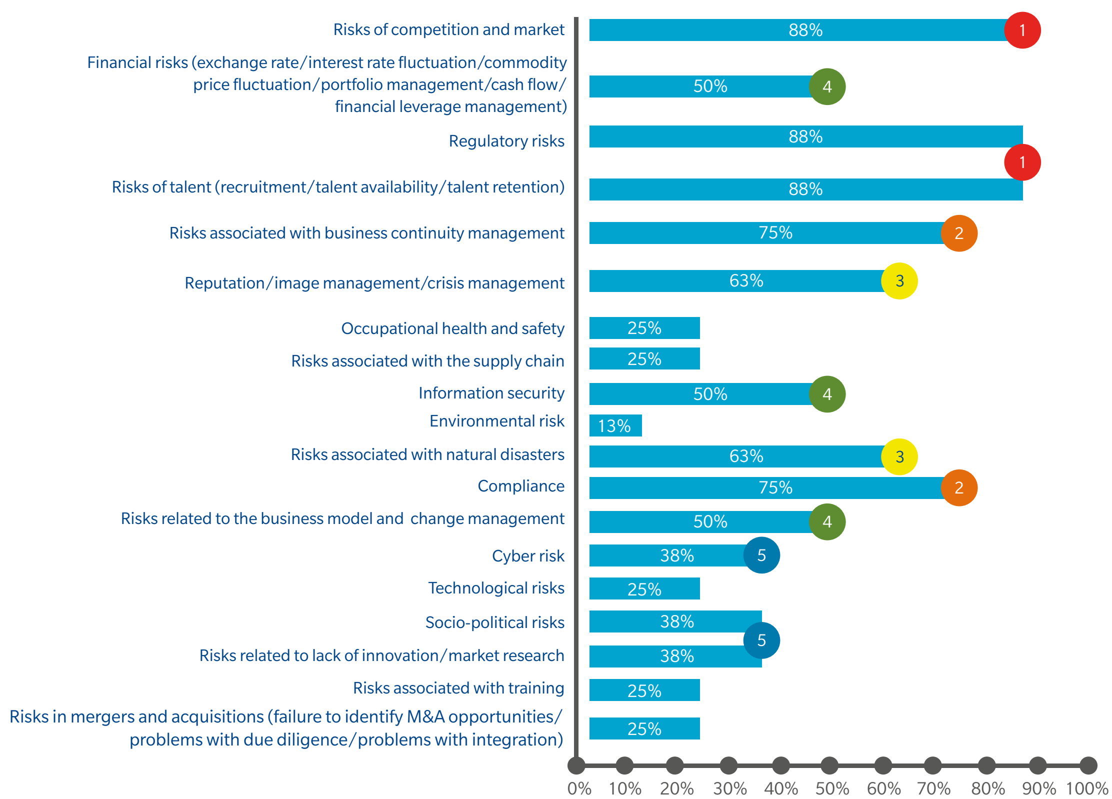
Graphic #19

PERU

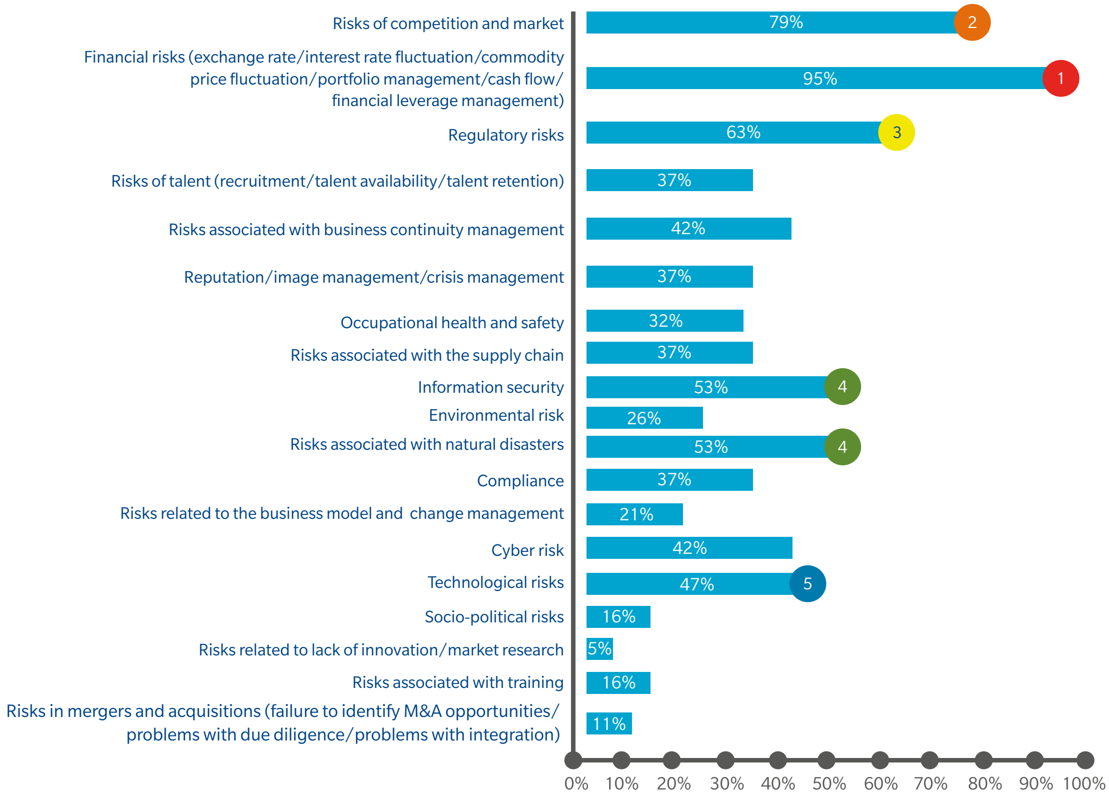


Graphic #20

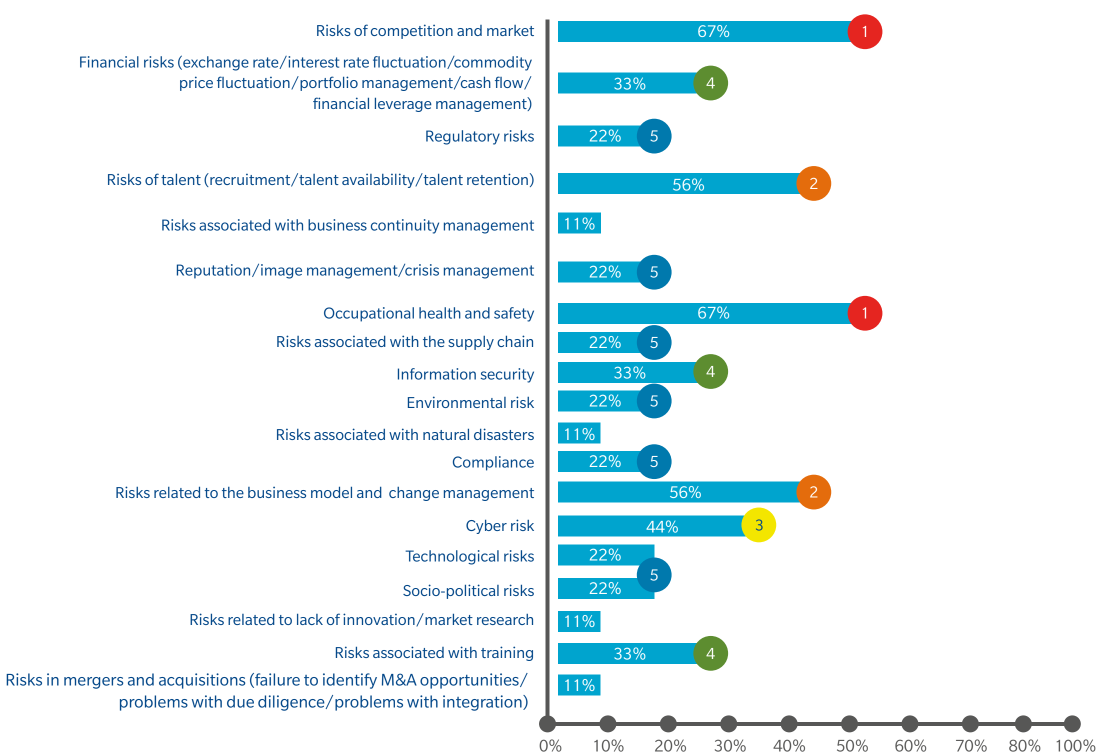
PUERTO RICO



Graphic #21
DOMINICAN REPUBLIC



Graphic #22
URUGUAY



EMERGING RISKS

- Discovering what they are
- Assesment of emerging risks
- Top emerging risks in Latin America
- Experiences of risk managers in the region with emerging risks
- Predictability
- Obstacles to the understanding of emerging risks
- Information sources
- Discussion forums

DISCOVERING WHAT THEY ARE

One of the issues of most interest in risk management is emerging risks, especially how they are defined, how they arise, and the methodologies to manage them. With the aim of a common base of understanding, for the purposes of this study a general description of emerging risks was provided.

Emerging risks are those events or situations that have not manifested broadly enough to be managed with the usual tools already applied to the risks and exposures best known in the organization. In a broad way, these are also risks that an organization has not yet identified or knows exist but are not yet understood.

In other words, these completely new risks have never been previously considered or are known risks that are evolving unexpectedly and having consequences that could not be anticipated. Their characteristics are:

- Their significance is uncertain and is not completely understood.
- They are difficult to quantify or estimate, given a lack of information and/or volatility in their future behavior.
- Their causes, consequences, and implications can be ambiguous.
- Their interactions and interconnection with other risks can be complex.
- They tend to be systemic, outside the control of the organization.
- Only residual impact can be mitigated for these risks.

The following is a definition from the RIMS Strategic Risk Management Implementation Guide:

Emerging risk is a new manifestation of risk that has not been previously experienced.

In order to differentiate between emerging risks and risks that may be evolving over time, RIMS uses the term "*dynamic risks*", which are risks known to exist but that can change over time.

Another definition from the Global Risk Center of Marsh & McLennan Companies is useful when discussing emerging risks:

Global and emerging risks are uncertain and complex threats generally exogenous that can have a significant and unexpected impact on the financial results of companies and their market positioning. As new phenomena or challenges that are sharpened by changing conditions, they are often shaped at the intersection of several fundamental trends and can crystallize in occurrence with abrupt changes in speed.

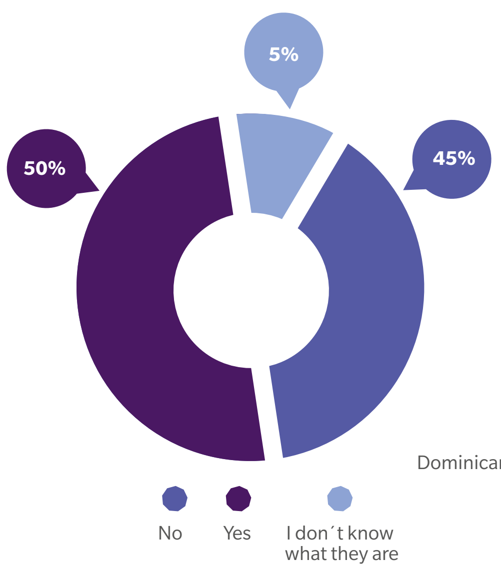
The path of these risks is difficult to predict due to the extensive interdependencies they have with other threats and complex interactions with other systems that absorb the risk. This generates the possibility of rapid dissipation, non-linear surprises, and "*overflow*" effects that transcend geographical sectoral and other boundaries. For some of these risks there is no guarantee of a return to conditions prior to the materialization of the risk and the result is the appearance of a new status quo. In general, companies (individually or collectively) cannot control such risks; they can only mitigate their exposures.

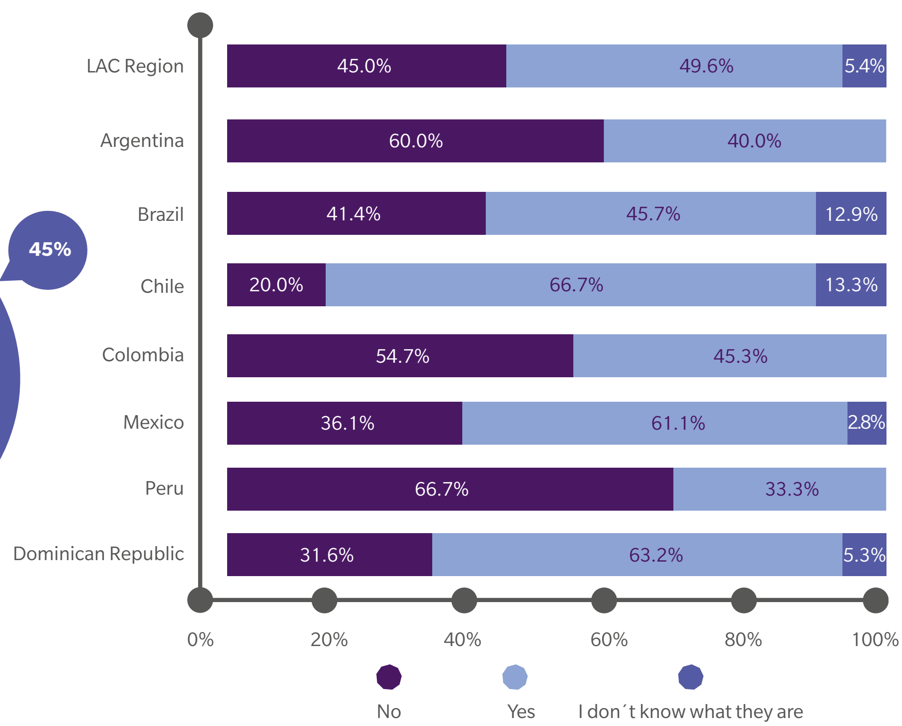
A better understanding of emerging risks and their configuration, valuation, and management could lead to viewing them as a market advantage rather than as a threat. Below are some elements that provide greater understanding of emerging risks, their assessment by Latin American companies, sources of information that make them detectable, and the trends that are the most critical for companies in the region.

ASSESMENT OF EMERGING RISKS

Graphic #23

ARE EMERGING RISKS ASSESSED (IDENTIFIED, ANALYZED, AND EVALUATED) IN YOUR ORGANIZATION?



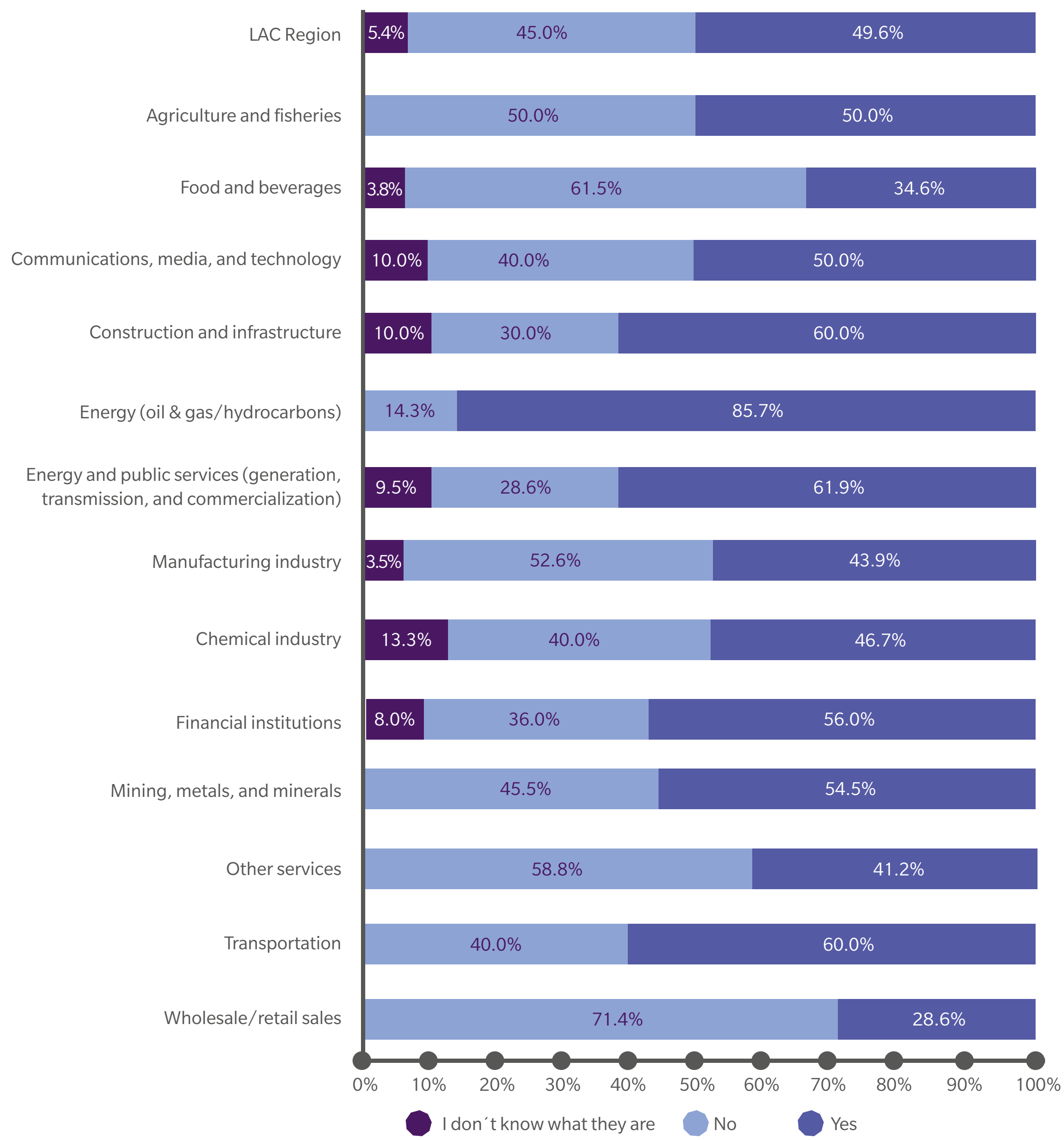


Information shown for countries with enough data to make meaningful comparisons.

One out of every two Latin American companies assesses emerging risks, leaving 45% of companies that say they do not and 5% who say they are not familiar with the concept. There is a large gap to be filled in terms of the dynamics of identification and management of emerging risks in Latin America. When analyzing the issue by country, we find that Peru, Colombia, and Argentina face the greatest gaps, with Chile, Mexico, and the Dominican Republic the most advanced in their emerging risks assessments.

Graphic #24

ARE EMERGING RISKS ASSESSED (IDENTIFIED, ANALYZED, AND EVALUATED) IN YOUR ORGANIZATION?



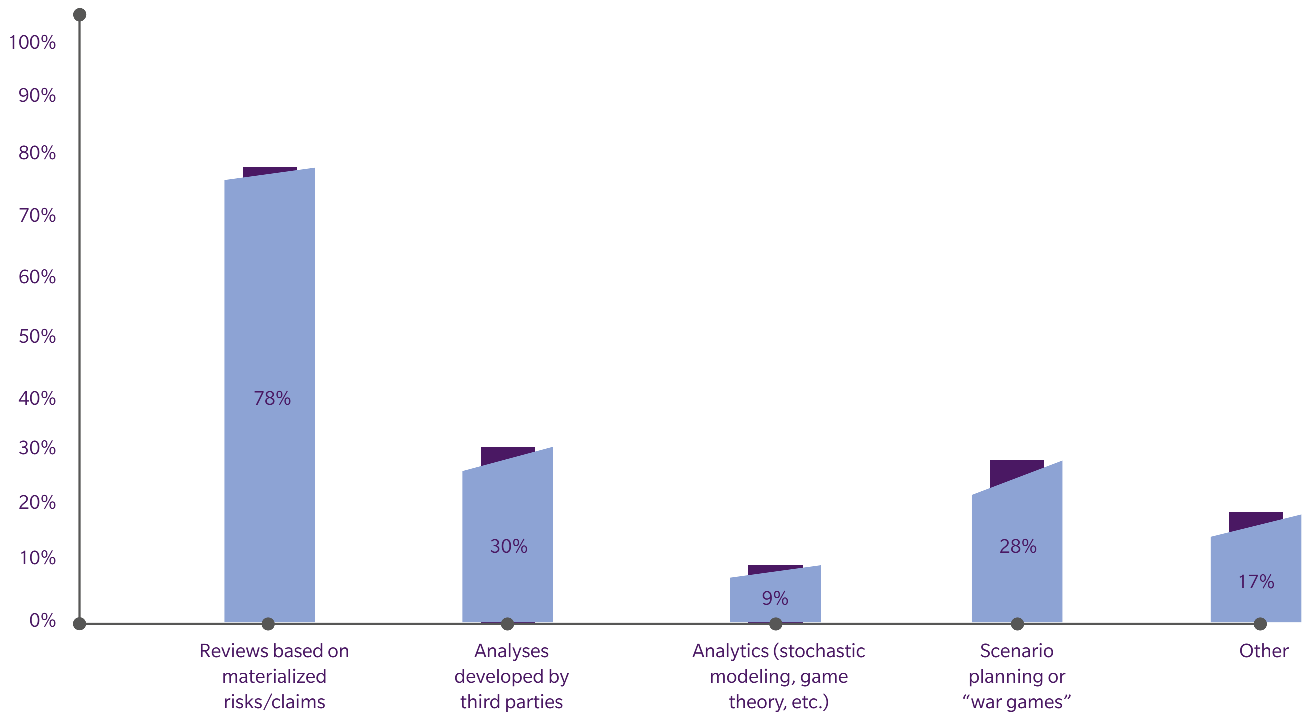
****Information shown for sectors with enough data to make meaningful comparisons.**

From the analysis by sector with regard to the assessment of emerging risks, the oil & gas, energy, and public services industries stand out, well above the average for the region.

50% of companies in the region do not assess emerging risks.

Graphic #25

IF YES, WHAT RISK MANAGEMENT TECHNIQUES DOES YOUR ORGANIZATION USE TO ASSESS AND MODEL EMERGING RISKS.



Another interesting element is that for those organizations assessing emerging risks, the techniques most in use are reviews based on materialized risks (78%), followed by analyses developed by third parties (30%), and scenario planning or "*war games*" (28%).

Other methodologies used for the valuation and modeling of emerging risks, include the following:

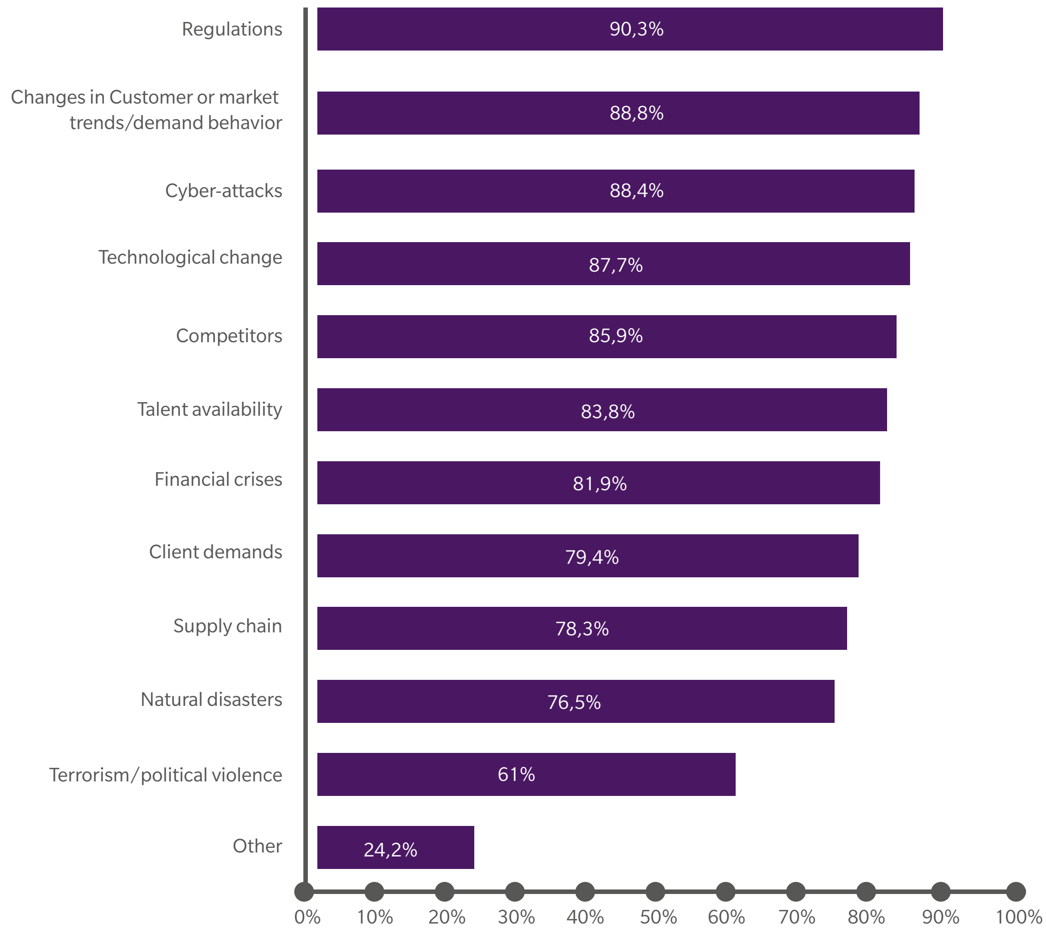
- Predictive techniques.
- Qualitative analysis by panels of experts.
- Multi-area workshops to assess risks, historical information, and internal and external evaluations.
- Quarterly interviews with senior management about external scenarios and the potential impact on the company's strategic planning.
- Managerial brainstorming.
- ROCA Plan in all operating units (ROCA: Risk Management, Operational Controls, Compliance, and Asset Quality).
- Risks identified by third parties based on peer review, other industries, etc.
- Regular holistic analysis.
- Strategic analysis of context by top management.
- Monte Carlo simulations.

TOP EMERGING RISKS IN LATIN AMERICA

The regulatory environment, demand behaviors, and cyber-attacks are the main threats identified by risk managers in the region, with corruption and social impact as new risk factors.

Graphic #26

IN YOUR EXPERIENCE, FROM WHAT AREA ARE THE MAIN EMERGING RISKS COMING FROM?



In terms of emerging risks, the five biggest concerns for Latin America are focused on regulatory issues, demand behaviors, and cyber-attacks.

1 REGULATORY SCOPE

The constant changes in regulation in Latin America and in the world require constant study, interpretation, and action on new legislation and regulations. The regulatory environment impacts both the operations and the strategy of the company and may involve significant investments in compliance as well as large expenses related to litigation. For those who lead the risk management area, the challenge is to develop a model that allows for constant compliance with changing regulations that are subject to multiple interpretations.

2 CHANGES IN CUSTOMER OR MARKET TRENDS/ DEMAND BEHAVIOR

Modernity has posed numerous challenges for risk management as we are in a highly interconnected, constantly changing, and increasingly complex world. Today we are concerned about issues that we had not imagined five years ago such as: replacement of the workforce dedicated to operational tasks by artificial intelligence systems, extreme climate change, or the management of "*millennial*" talent. Likewise, a critical issue is the non-traditional competition emanating from technological innovation in platforms that compete with traditional business models (i.e., Airbnb versus the hotel industry, Uber versus the traditional public transport system, etc.). The growth of interdependencies, globalization, more complex and global supply chains, the dizzying speed of information, social networks, and new challenges arising from global risks such as climate change, water crises, and large scale involuntary migrations are factors that will influence the demand behaviors and consumer trends. The demographic, behavioral, and needs changes in consumers will present new opportunities for agile and adaptable companies in the coming decades, while this same change represents a threat to many traditional marketing and business strategies in operation.

3 CYBER-ATTACKS

A surprising fact is that the risk of cyber-attack, which began to appear as a main emerging risk more than five years ago, is still considered an emerging risk. The reality is that although the concept of cyber-attack has been known for some time, the nature of such attacks continues to evolve in unexpected ways and their impacts are increasingly difficult to assess. Now, when attention to cyber risks emanates directly from the managerial level (board of directors or board), it is not just a topic exclusive to a company's technology group. It requires a holistic vision of its causes and consequences through participation in strategy and planning from across the organization.

The importance being given worldwide to cyber-attacks is significant, as the impacts can be multi-sectorial, simultaneous, and disruptive of operations.

The above is in addition to the multiple forms of cyber-attacks such as the so-called "*destructive attacks*", "*Cyberwarfare*", "*Hacktivism*", or indiscriminate attacks (i.e., the well-known WannaCry Ransomware attack in May 2017).

4 TECHNOLOGICAL CHANGE

The intrinsic risk of change and innovation is especially present in an area where there has been multiple advances and dynamism - the technological field. The risks that arise from innovative technologies and new developments such as synthetic biology, nanotechnology, artificial intelligence, cognitive computing, process automoation with robotics, "*e-commerce*", "*digital mobility*", information in the cloud, and "*big data*" are those that will be transforming organizations and the risk landscape in the future.

In the opinion of many, we are now witnessing the beginning of a future powered by technology.

Globalization and free entry to generate technological developments allows a much wider range of organizations to be active in the economy, which increases the risk of competition. Innovation and technological change come with different benefits and opportunities, but they are not risk free.

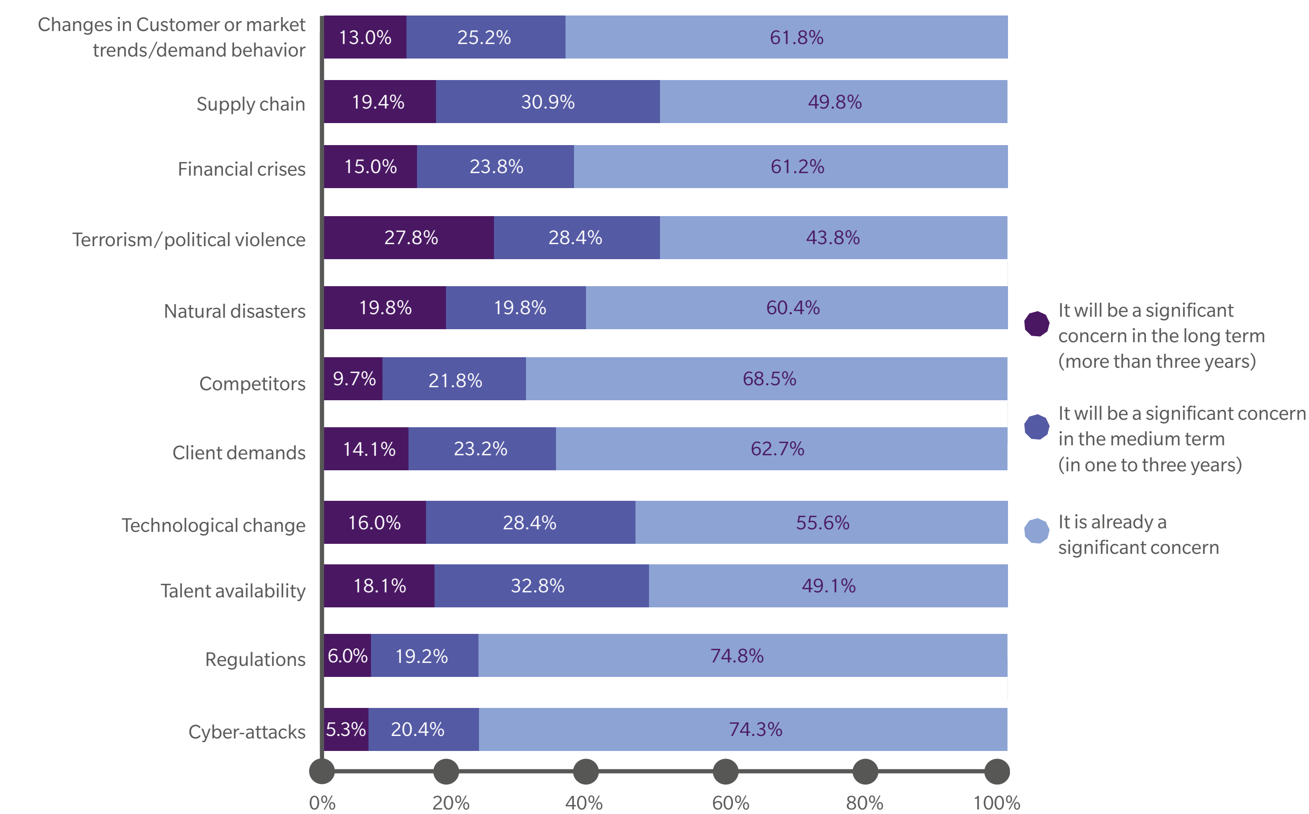
5 COMPETITORS

In a world energized by technological change, changes in consumer and demand trends, the speed with which information flows, the activation of new global players within local markets due to globalization, and the complexity of supply chains, competitiveness becomes one of the biggest concerns of the modern business world. How to stay current and in the vanguard in a changing world? Factors such as price, innovation, location, resources, promotion, distribution, and intellectual property become fundamental when evaluating the competitive environment. The potential of a competitor's actions to negatively impact the business is multifactorial. In recent years, many well-known brands have been victims of competitive threats that have not been managed appropriately. Sometimes the size of the risk presented by existing rivals, new products/technologies, or new companies just entering the market (start-ups) can be underestimated from a position of size and dominance in a sector or market in particular. It is therefore essential to assess the risk of competition, to try to be at the forefront, or opt for offensive strategies as opposed to reactive alternatives, when it may already be too late to protect market position.

75% of organizations consider that cyber-attacks and regulatory changes are the most urgent risks in the short term.

Graphic #27

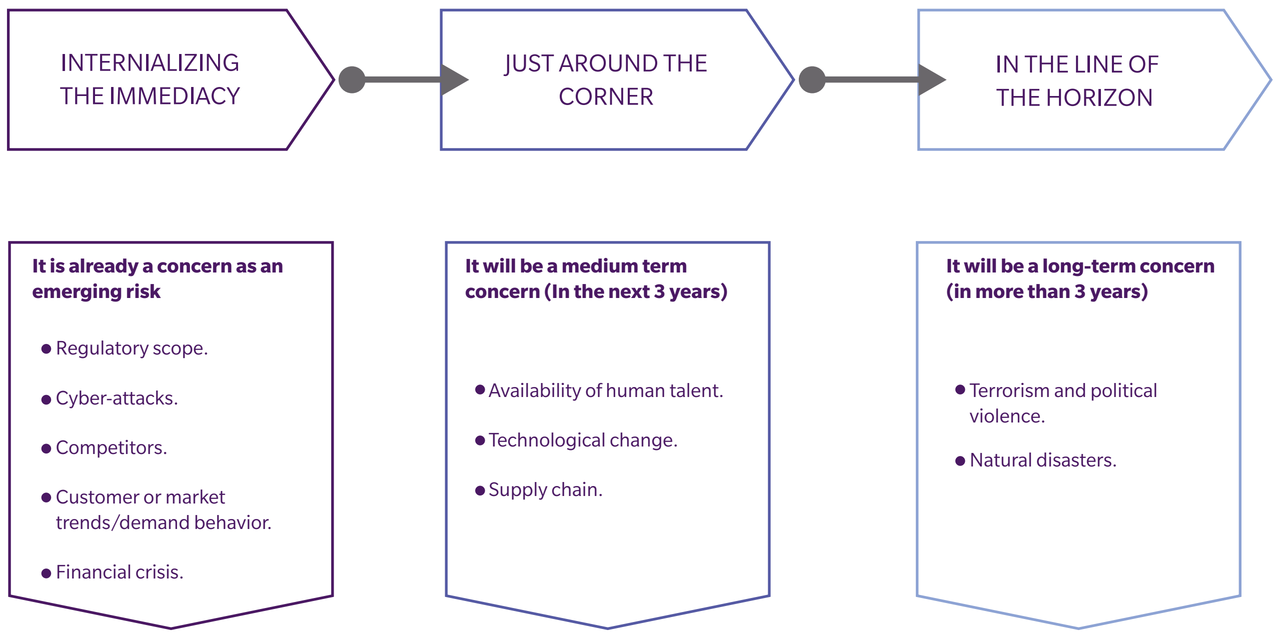
TIME HORIZON FOR EMERGING RISKS



A strategy for deepening organizational thinking about emerging risks is to consider from where these critical risks are likely to arise, specifically the time frame in which the are likely to have an impact or become material. Below is a timeline developed based on reporting by Latin American companies regarding when they expect their main emerging risks to show their impacts and when these risks will begin to be critical for the company.

Graphic #28

OVERVIEW OF TIMELINE FOR EMERGING RISKS IN LATIN AMERICA



OTHER CONCERNS

Within the analysis in the category of "*Other*" emerging risks for companies, three issues arose repeatedly, which are worth mentioning in this study:

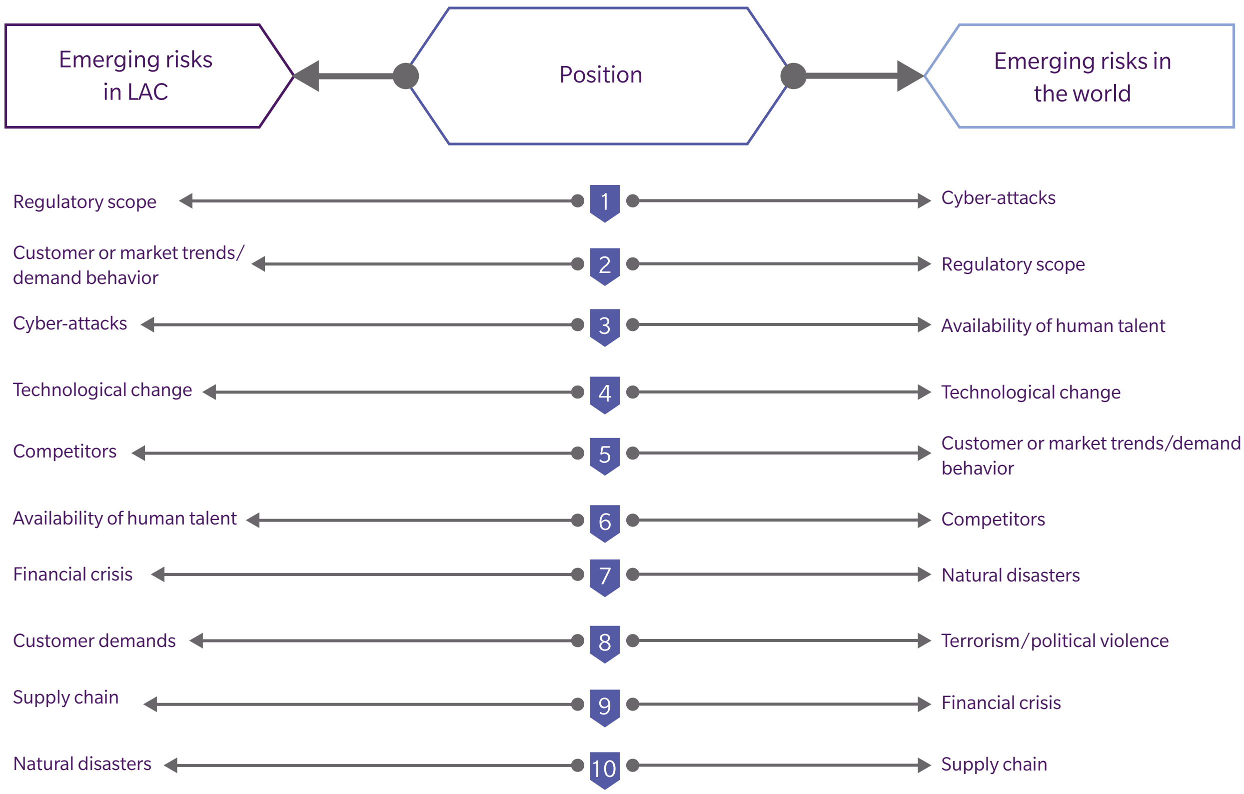
Corruption Risk. Due to recent events in the region and in light of a higher perceived incidence of this issue in the business world, corruption is another issue that requires special scrutiny in the field of business risk.

Social Risk. Nowadays, the impact that an organization has on its environment, its stakeholders, and especially its relationship to the community are very interesting focuses in the area of sustainability and for risk management.

Reputational Risk. It is inevitable that given the increasing use of social networks, the incredible speed of information dispersion, and the variety of public channels through which it is mobilized, reputational risk is a growing concern in the region. With the resounding effect of disinformation or "*fake news*", and how companies protect their image and reputation, reputational risk takes on a different relevance compared to how it was visualized five years ago.

Graphic #29

EMERGING RISKS IN LATIN AMERICA AND THE WORLD



* Source: "Emerging Risks: Anticipating Threats and Opportunities Around the Corner", EXCELLENCE IN RISK MANAGEMENT XIII, Marsh, RIMS, April 2016

When comparing the order of importance in which the emerging risks in the Latin American and Caribbean region are positioned against the ranking of emerging risks in the world, it is obvious, among others, three differences in terms of priority:

- The importance that is being given to the regulatory environment in Latin America [LAC: Position 1, World: Position 2].
- The prevalence that is being given to cyber-attacks in the world [LAC: Position 3, World: Positon 1].
- Customer or market trends/demand behavior [LAC: Position 2, World: Position 5].

The differences in how the risks are perceived and prioritized in the region, compared to how the world sees them, opens the door to understanding in a more related way the business reality of the Latin American region. This can help guide risk managers to more accurately guide their organizations with regards to specific regional or sector risks.

EXPERIENCES OF RISK MANAGERS IN THE REGION WITH EMERGING RISKS

The Risk Management Leaders (risk managers) that participated in the focus sessions of this study shared several impressions about emerging risks and their current approach to them:

- *"By monitoring macroeconomic variables we seek to identify emerging risks."* - Financial institution.

- *"If emerging risks arise they are analyzed when materialized."* - Hydrocarbons sector company.

- *"In each of the subsidiary companies, emerging risks that are not within the strategic risk maps of the subsidiary are identified. These risks are identified, monitored, and even action plans are defined and at any time they can be transferred to the risk matrix. [...] There are still no specific methodologies or specific qualifications for emerging risks, therefore existing methodology is used. The company has not worked on this at the corporate level, but each subsidiary company has its emerging risks."* - Multilatina business conglomerate in the concrete sector.

- *"From internal audit as a third line of defense, very interesting support is provided in the identification of emerging risks, and they also constitute an important source of information."* - Transport sector company.

- *"We started this year with the topic of emerging risks. We are working from the presidency, reporting to the presidency committees and the operations in each country on a monthly basis. We use the same methodology for risk appetite, and additional analysis focuses on what could be the impact of the emerging risk. We are evaluating if the emerging risk changes if it is strategic or operational and how it will be managed."* - Multilatina organization in the packaging sector.

- *"Yes, identification of emerging risks is done with the existing methodology for new projects; however, it is not being done for business risks."* - Multilatina producing construction materials.

- *"The organization monitors communications and news both from regulatory agencies and from industry to determine what applies to the corporation. Based on this, war exercises have been carried out for cyber, events that affect business continuity, hurricane, earthquake, and terrorist attack, among others. These scenarios are discussed in roundtables and are considered within the contingency plans. As a complement, the organization performs another internal exercise including public relations companies with other scenarios from the communications point of view, so that the organization is prepared for what needs to be communicated. The organization also evaluates crisis scenarios in other instances: different committees that are more corporate.* Financial institution.

- *"There is a discussion in the organization of any emerging risk that is mentioned by the members of the Executive Risk Committee (ERC), who together determine whether there is enough relevance to assign a risk owner, a work team that formulates a general assessment and a risk response plan. With the above, the risk will be part of the daily discussion of the ERC and therefore will be assigned to a committee of the board. For information they use all sources: consultants, industry peers, and insurance brokers. They are aware of everything that is happening and evaluate to what extent they concern the organization. Surveys are also done every two or three years to collect organizational views."* - Insurance company.

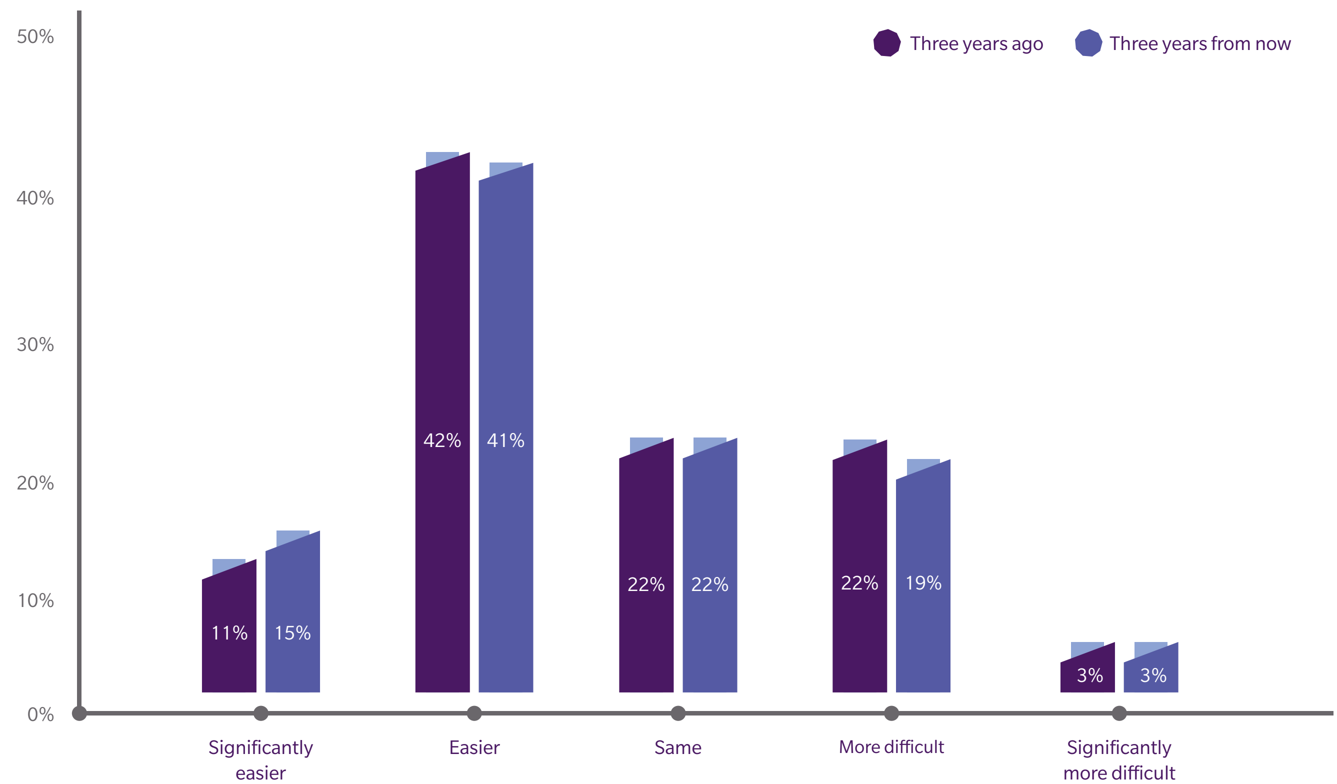
- *"With the annual review of the risk matrix, several issues that arise via committee or in other forums are considered and related to the scope of work in the current year. In this way, emerging risks are measured and those that are priorities are mapped (identified, analyzed, evaluated, and eventually treated, according to the cost benefit of mitigating actions)."* - Energy sector company.

PREDICTABILITY

How easy is it to forecast or foresee emerging risks? Do we have tools for early identification? What are the keys to an effective and integrated response?

Graphic #30

IN YOUR OPINION AND EXPERIENCE, IS IT EASIER OR MORE DIFFICULT TO FORECAST OR FORESEE CRITICAL RISKS FOR YOUR BUSINESS TODAY THAN IT WAS THREE YEARS AGO? DO YOU EXPECT IT TO BE EASIER OR HARDER TO FORECAST CRITICAL RISKS FOR YOUR BUSINESS WITHIN THREE YEARS?



* Source: "Emerging Risks: Anticipating Threats and Opportunities Around the Corner", EXCELLENCE IN RISK MANAGEMENT XIII, Marsh, RIMS, April 2016

The study shows that, compared to their situation three years ago, those in charge of risk management in Latin American companies have seen an improvement in their ability to forecast their critical risks and feel that this trend will continue. This subtle greater confidence is based on the strengthening of the mechanisms that they now have and will have at their disposal to identify critical risks and project their behavior, complemented by a better structuring of information and the use of increasingly advanced quantitative methodologies.

OBSTACLES TO THE UNDERSTANDING OF EMERGING RISKS

The lack of key knowledge or the inability to model the magnitude of emerging risks means that companies do not adequately understand their impact on organizational strategy and in the decision making process.

Among the obstacles that inhibit the ability of Latin American companies to understand the impact of emerging risks on organizational strategy and decision making, are mainly the lack of knowledge of key concepts of risk management, the inability to model the magnitude of the risk, cultural or institutional issues, the lack of transversal collaboration between areas in the organization and, finally, the allocated budget.

Graphic #31

WHAT OBSTACLES INHIBIT YOUR ORGANIZATION'S ABILITY TO UNDERSTAND THE IMPACT OF EMERGING RISKS ON STRATEGY AND ORGANIZATIONAL DECISIONS?

Position	LAC REGION	
1	Lack of knowledge of key risk management concepts	55%
2	Inhabiility to model the magnitude of risk	50%
3	Cultural/institutional themes	48%
4	Lack of collaboration between areas in the organization	46%
5	Budget	25%

Graphic #32

	LAC	Manufacturing industry	Financial institutions	Food and beverages	Utility and energy	Fishing and agriculture
Lack of knowledge of key risk management concepts	1	1	4	3	4	1
Inhabiility to model the magnitude of risk	2	2	1	4	1	2
Cultural/institutional themes	3	3	2	1	3	5
Lack of collaboration between areas in the organization	4	4	3	2	2	3
Budget	5	5	5	5	5	4

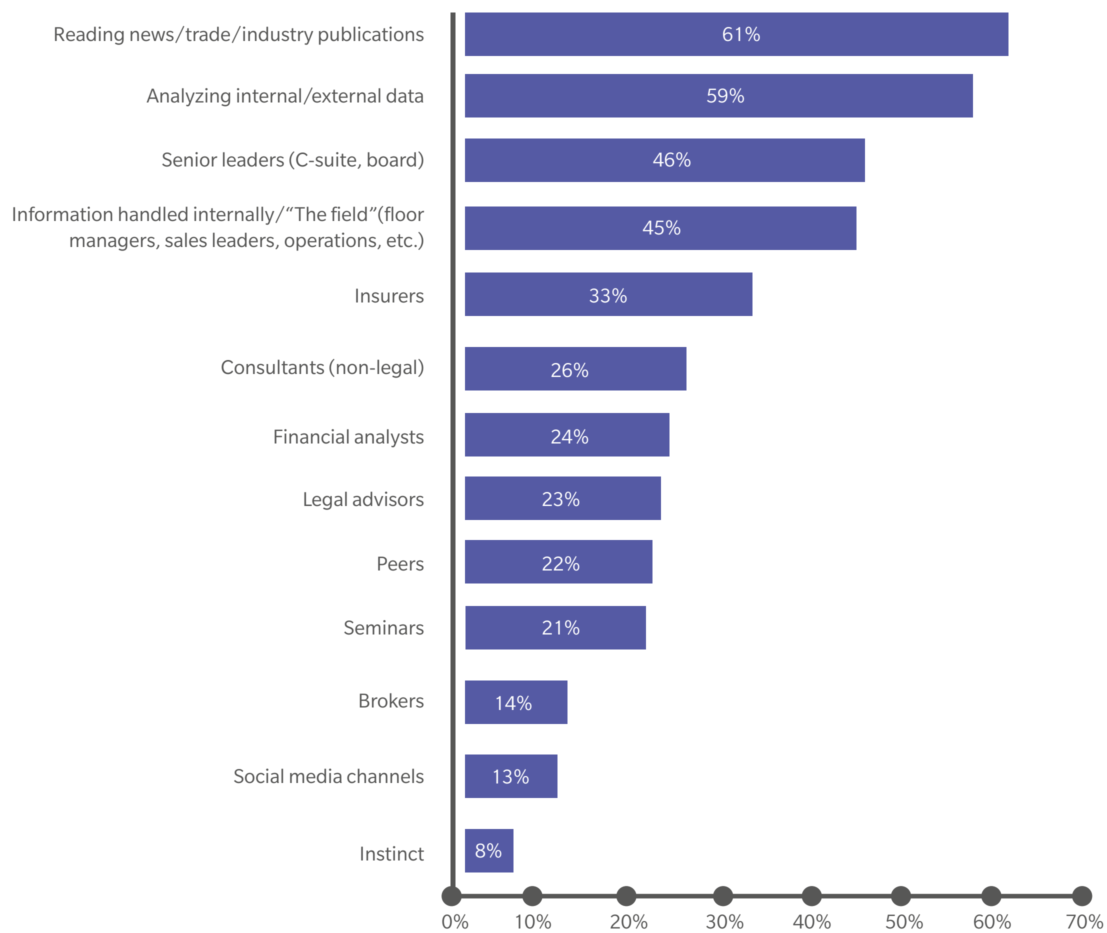
For the region, the initial barrier to understanding emerging risks and their impact on the organization is the **lack of knowledge of key concepts in risk management.** If knowledge is concentrated in a few, the organization will lose its ability to forecast and will lose the "*momentum*" required to become a resilient organization. From the perspective of industry, this first barrier is common to the manufacturing sector, agriculture, and fishing but for the financial industry and the public services sector it is down at level four, as for these two sectors **the inability to model the magnitude of risk** is the main barrier they face. The barrier of **cultural/ institutional issues** manifests itself strongly in the food and beverages sector, as the number one issue in terms of understanding emerging risks, but in the region this same problem occupies the third position. **The lack of collaboration between areas in the organization** occupies the second position for the food, beverages, energy, and public services sectors. **Budget** occupies the last position for all analyzed sectors. From the above it can be inferred that having knowledge in risk management, having the appropriate organizational culture conditions, facilitating cross-collaboration between areas in the organization, and finding mechanisms that assist in modeling the magnitude of risk are fundamental issues to transcend if you want to advance the understanding of the behavior and impact of emerging risks in Latin American organizations.

INFORMATION SOURCES

The sources that risk managers rely on to identify emerging risks can help understand the complexity of anticipating them.

Graphic #33

IN WHAT SOURCES OF INFORMATION DO YOU TRUST TO IDENTIFY AND UNDERSTAND THE POTENTIAL IMPACTS THAT AN EMERGING RISK MAY HAVE ON YOUR ORGANIZATION?



The sources of information in which those in charge of the risk management area rely to identify emerging risks can help us understand the complexity of anticipating them. We asked risk professionals what information sources they consulted to identify emerging risks and estimate their potential impacts. The following are their main responses:

- The main source of information is from reading external publications, with the added attraction that the broader the reading, the more abundant the information will be about the emerging risks that may affect the organization. *"We rely on the annual document of the World Economic Forum about global risks, which gives us a global vision of what is to come,"* commented the risk management leader of a gas company. Other participants noted their use of reports from financial analysts and Futurist blogs, which can reinforce connecting the dots between the organization's strategy and emerging global risks/trends.

- There is also a high concentration of internal and external analysis based on the information that the company produces within its different areas, such as with third parties who contribute different points of view to the analysis.- *"We rely a lot on internal audit, in market monitoring through market analysis reports by external consultants,"* commented the risk leader of a paper sector company.

- The inputs that can be provided by those who know the business properly and the day-to-day, whether senior management, plant managers, sales leaders, or operations, are part of the valuable information sources to be used to identify emerging risks. This approach, in order to not be limiting and not focus exclusively on business risks, must be combined with the perspective of other parties and events, such as trade union debates or specialized sector publications. *"We can say that sector discussion forums, specialized publications, and the constant involvement of the company's internal processes are the main sources of information for us to capture potential impacts of emerging risks,"* noted a risk leader for an energy sector company.

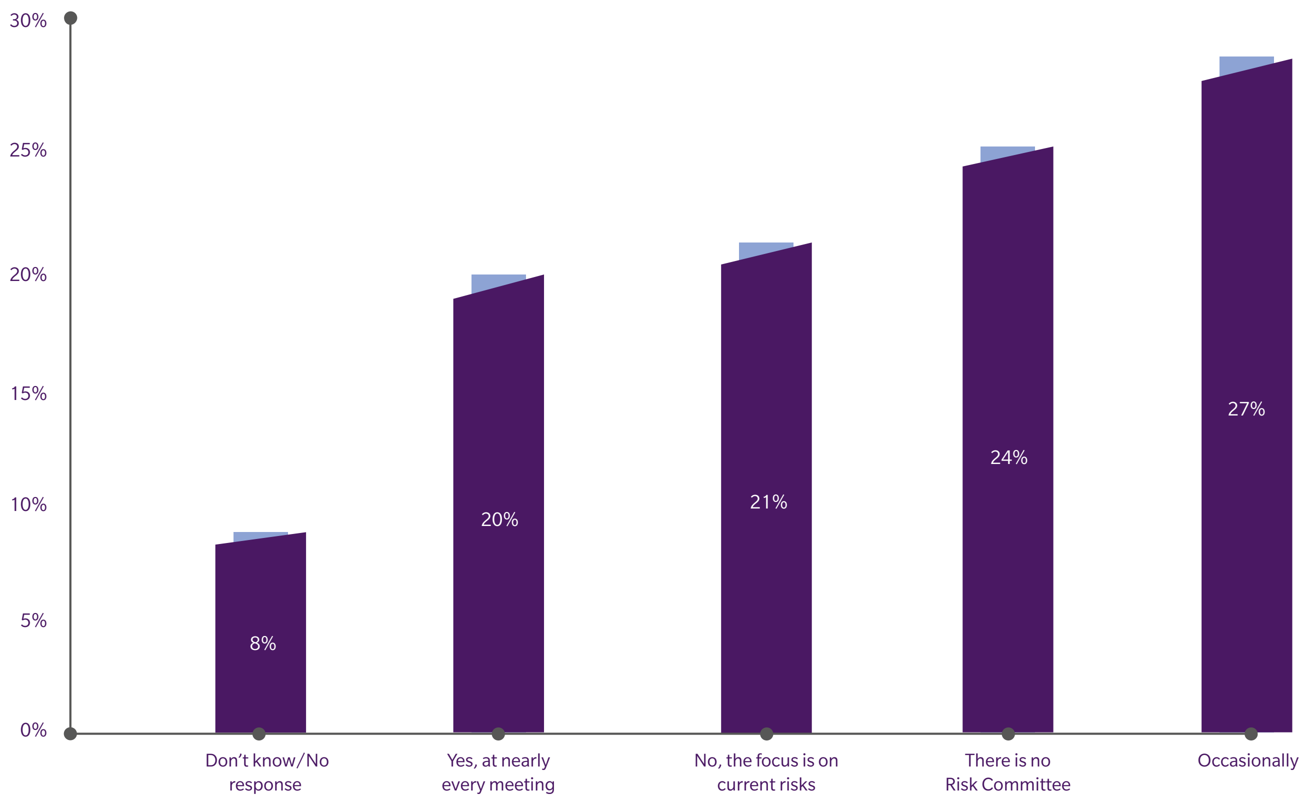
- The specialized knowledge, not exclusively of the sector, but one that crosses the borders of industry, size, markets, etc., is a source that contributes to the conversation of emerging risks, since it brings perspectives not previously explored. *"We use media information and specialized consulting. The consultants have experience with real cases, and the knowledge they have applied to other clients is valuable insofar as the lessons learned,"* said a risk management leader in a hydrocarbons sector (downstream) organization. *"We look for information in the media and in cases that have already happened; real cases or case studies,"* noted a risk and insurance leader of an aerospace sector company.

- It is striking that given that today we live in an environment of immediacy in global information and advanced information flow, social networks are not considered a key source of information. The relevance of social media platforms can increase rapidly and they can become critical tools for gathering information especially with generational renewal. Organizations are beginning to more creatively use social media, where an involved younger and more "*connected*" audience may present opportunities to better understand those trends that may evolve into emerging risks for their organization.

DISCUSSION FORUMS

Graphic #34

IF YOUR ORGANIZATION HAS A RISK COMMITTEE OR CONVENES A SIMILAR FORUM IN WHICH RISK MANAGEMENT IS DISCUSSED AND MONITORED, ARE EMERGING RISK TRENDS DISCUSSED THERE? IF YES, HOW OFTEN DO THEY DO IT?



Almost a quarter of the sample says it does not have a risk committee or similar forum. This suggests, without stating that there is a need for a risk committee, that 25% of Latin American companies do not have any forum specifically structured to review issues of risk responsibilities and related matters, which means that risk issues should be a point of discussion in other areas to give relevance, visibility, and periodicity to their follow-up.

In analyzing the forums where emerging risks are discussed, only one in five Latin American companies discuss the issue with high frequency. 27% confirm that the topic is occasionally discussed and 21% affirm that emerging risks are not the focus of attention, since the topics discussed are mainly existing risks. Most worrying is that in another 21% the issue of emerging risks was never discussed. All of the above shows that there are opportunities for improvement in the governance structure of the risk committees so that the emerging risks topic becomes an important part of the agenda.

RISK MANAGEMENT CULTURE

- Strategies to facilitate its implementation
- Discovering the opportunity in risk
- Demographic information

STATEGIES TO FACILITATE ITS IMPLEMENTATION

The integration of risk management in the strategy, operations, and values of the organization, the commitment of senior management, and adequate training and communication are key factors to maximizing the value of risk management.

Throughout this study we have seen that one of the fundamental points for the successful implementation of risk management is the organizational culture around it. By delving into those strategies that facilitate the internalization of this organizational culture we find several points in common:

- The **integration of risk management with the strategy and values of the organization** is one of the elements that weighs more in the analysis as it is a key factor of the culture of risk management for 64% of the participants. One risk management leader in a financial institution comments: *"Being part of the strategy, it challenges the status quo of the business."*

- Likewise, with 59% in agreement, risk management as **part of the day-to-day business** is also a great facilitator. *"Rooting the practices of risk management, making it part of the people day-to-day is important. The issue of risks is very new within organizations and people have not yet been able to perceive their proper value. The evidence of current news, mainly related to emerging risks, has helped people to think more about risks and their impacts."* - Risk management and insurance leader in the hydrocarbons sector (downstream).

- On many occasions there is a need to use **communication, awareness, and training** as a means of inserting the topic of risk in the organization. A complete communication strategy is required that includes the identification of the different audiences (internal or external), the key messages that we want to impart, the environment, the periodicity and, of course, what measurement instrument will be used at the end of this strategy to measure its effectiveness. It is well known that any process of cultural transformation within an organization must be gradual; persistence is required with a consistent message and it must be adequately reiterated for it to achieve the expected impact on the subconscious and organizational psyche. Therefore, awareness, and effective and measurable communication strategies is one of the main points for risk management leaders in Latin America. *"The most effective strategies to achieve this transformation in the culture of the organization are reflective and practical, experiencing and interpreting internal and external situations in the company. It is a slow and gradual process, so that the public can absorb the idea and put it into practice at all levels of the company."* - Energy sector company. *"Evangelize with campaigns, showing the 'what for' of comprehensive risk management."* - Financial information sector company.

  It is also important that training is designed to adapt to the language that people at different levels of the organization are expecting to receive. In other words, the issue must be made more "*digestible*" and practical in order to get the staff to act out of conviction and with the purpose of really provoking the expected reaction. *"[...] not everyone is used to the terms we use in the management of risks. It is important to develop a common language, for example try not to use technical language; the why should be explained, but in a simple way, because we understand that this is something that can impact the effectiveness of the training."* - Financial institution. *"So, as we must translate sophisticated concepts of risk management into concepts that are totally accessible to the people who are closer to the risk, or to the client that, at the end of the day, is the reason for which there is risk management: to create the fluidity of information, knowledge, and risk perception so that the connection between the problem and resources always happen."* - Insurance company.

- Another important issue is the **sponsorship and interest to promote risk management from top management.** Without the conviction of the leaders of the organization, it will not facilitate the cascade towards other levels of the organization. Many of the participants expressed the importance of having this "*backing*" from top management. *"Sponsorship from senior management helps push the cultural transformation of risk management. Many difficulties are concentrated in reactive attitudes of people."* - Multinational food sector company.

Below we capture some other valuable elements discussed with the Risk Management Leaders in the focus group sessions, which shed light on how to facilitate the process of cultural transformation.

- **Demonstrate its value:** *"Demonstrate the advantages and results of effective risk management, more preventive than reactive."* - Aerospace sector company.

- **Instill taking responsibility for risks:** *"Show the 'because' of risk management, and inculcate the ownership of the risks to whom it corresponds."* - Financial information sector company.

- **Systematic reporting and linking risk management to performance measurement and strategic indicators:** *"Variable remuneration indicators were tied to the way of managing risks. By doing so, we achieve a culture of self management and selfcontrol of risks."* - Multilatina conglomerate *"We have relied heavily on the systematic reporting to management and the tying of risk management to strategic indicators."* - Transport sector company.

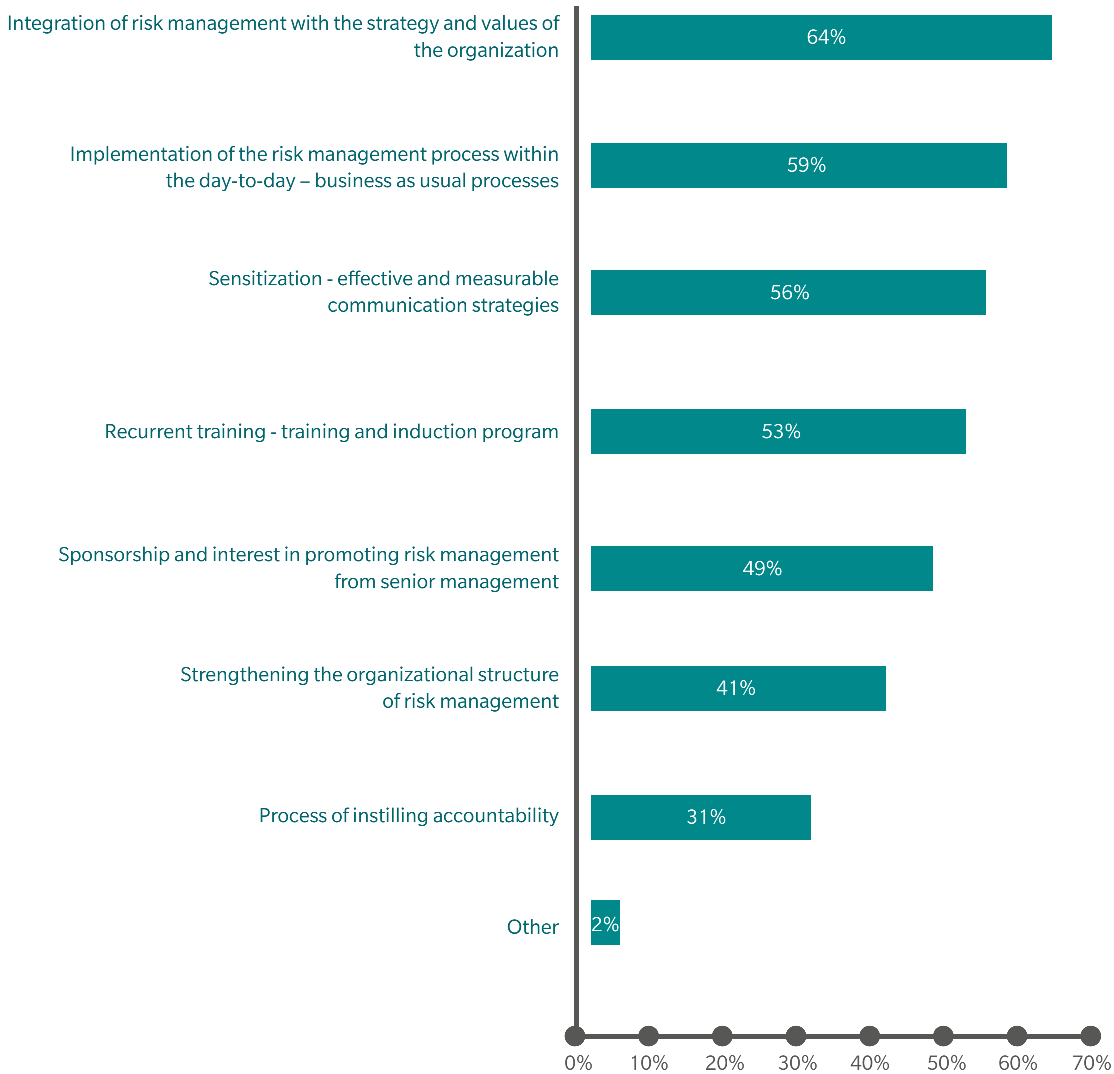
- **Have an empowered work team to multiply the effort and the message:** *"The creation of risk leaders has helped us a lot."* Transport sector company. *"Positioning risk management with the Quality Management coordinators has facilitated the subject. They are an armed wing that has helped us a lot. It has also helped us to empower people with this role supported by the new version of ISO 9001 since it now includes risk."* - Multinational business group.

- **Provide material information to achieve lessons learned:** *"We still have many challenges to instill the culture, but we have found an important ally in having case study information."* - Multilatina organization in the manufacturing and retail sector. *"The analysis of incidents that lead to lessons learned to identify root cause has been of great use. Based on this input, improvement plans are created that leverage preventive management."* - Transport sector company.

On the way to establishing an adequate culture of risk management, more than half of Latin American organizations find the integration of risk management with the strategy and values of the organization, the integration with the day-to-day, awareness, and formal structured and recurring training very useful.

Graphic #35

FACED WITH CULTURE OF RISK MANAGEMENT ISSUES IN YOUR ORGANIZATION, WHAT STRATEGIES DO YOU FIND NECESSARY TO TRANSFORM THE CULTURE OF YOUR ORGANIZATION TO BE RISK MANAGEMENT ORIENTED?

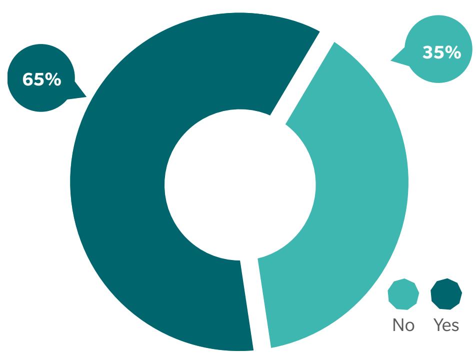


DISCOVERING THE OPPORTUNITY IN RISK

More than a third of Latin American organizations say they do not value opportunities within the scope of risk management.

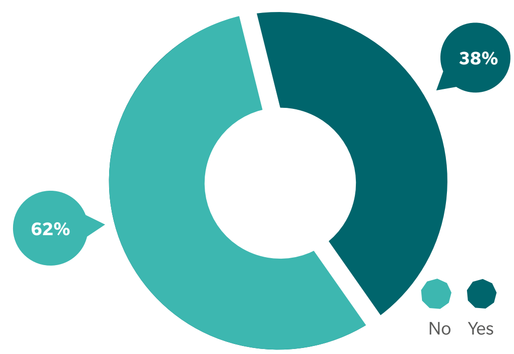
Graphic #36

DOES RISK MANAGEMENT INCLUDE VALUING OPPORTUNITIES?



Graphic #37

IS THERE A METHODOLOGY FOR MANAGING OPPORTUNITIES WITHIN RISK MANAGEMENT?

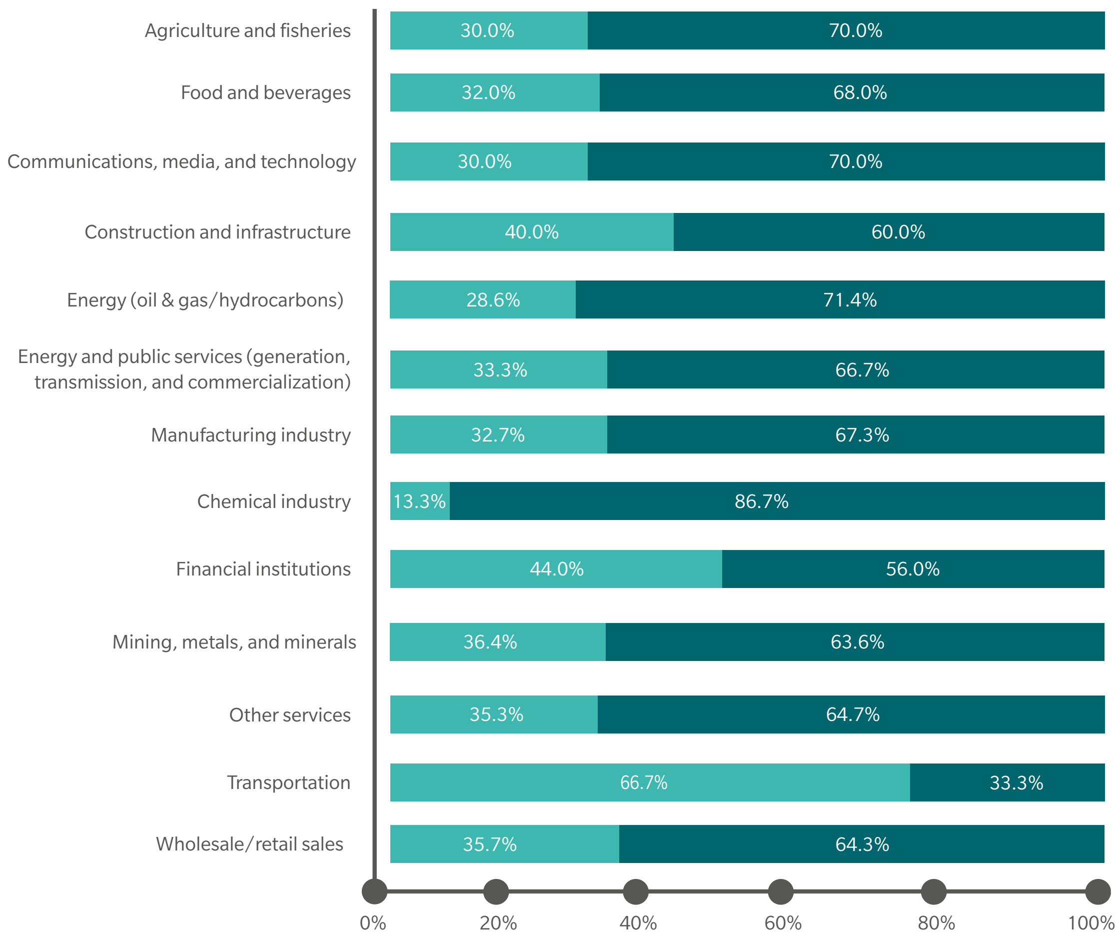


Part of having a risk management culture includes seeing risk as an opportunity. This concept is recognized in multiple regulations and represents one of the reasons for risk management. 65% of Latin American companies agree that there should be assessment of opportunities within risk management, which means that a little more than one in three Latin American companies are not yet integrating the identification and exploitation of opportunities within the scope of risk management. The foregoing demonstrates that the region still has an important way to go and that change could be triggered by changes in ISO 9001, ISO 31000, and COSO (Committe of Sponsoring Organizations of the Treadway Commission), which encourage the integration of risk management with strategy, an area that primarily focuses on the identification of opportunities.

Reviewing the process of identification of opportunities by sector reveals that the ones that do this most in practice are the chemical industry and the hydrocarbons sector, while the transport sector, financial institutions, and the construction and infrastructure sectors adhere less to this practice.

However, although a significant number of Latin American organizations are addressing

Graphic #38



opportunities from the perspective of risk management, most do not have a particular methodology to incorporate them. Only two out of five companies say they have a formal methodology to manage opportunities within risk management, which suggests that the rest of the companies that manage them, but do not have a methodology, do so in a more informal manner. Acknowledging that much can be informal when it comes to seizing risk-realted opportunties, it is natural to suggest that good practice dicatates formalizing a methodology for managing opportunities.

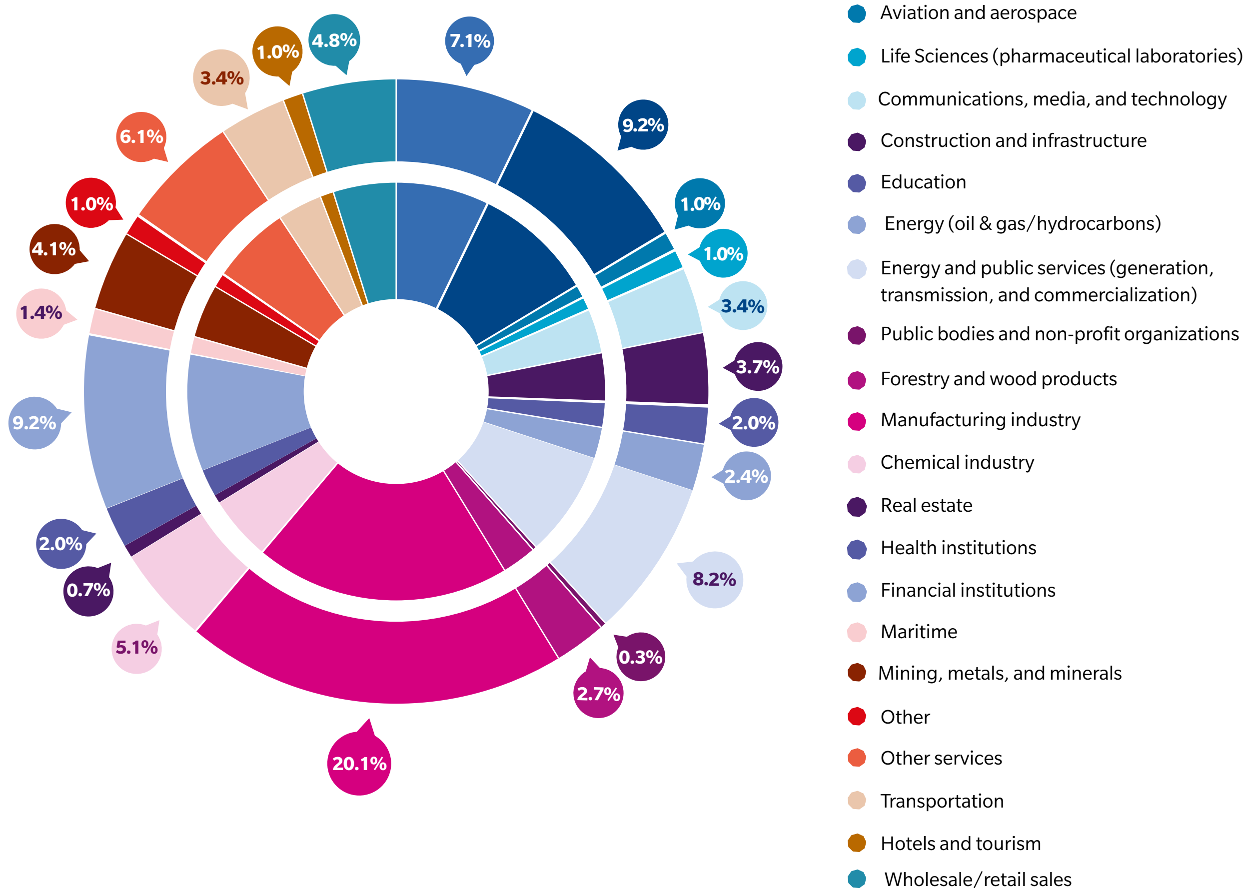
65% of organizations say they value opportunities within the scope of risk management, but 2 out of 3 do not have a formal methodology to take advantage of them.

DEMOGRAPHIC INFORMATION

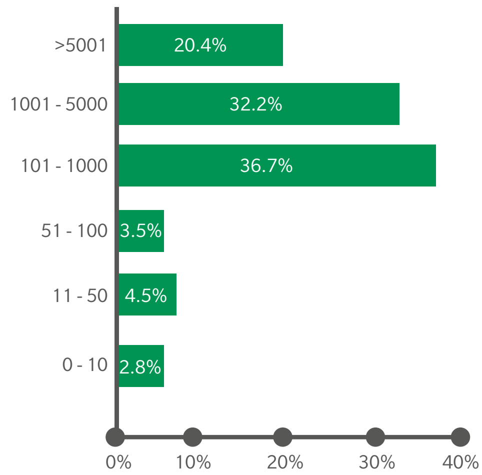
The results of this study are based on the responses of 294 surveys conducted through an online questionnaire between April and August 2017 with participation of more than 10 countries in the region and 20 economic sectors.

Graphic #39

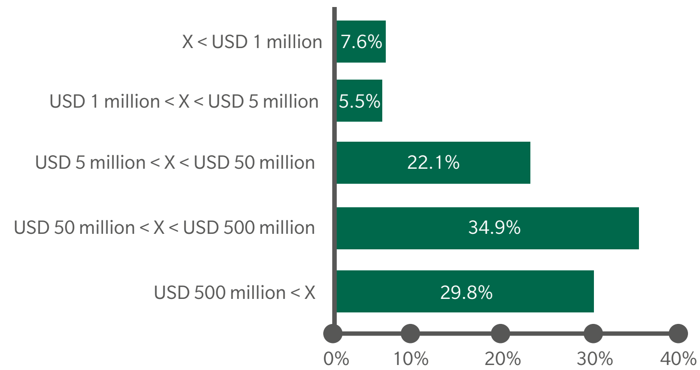
DISTRIBUTION BY INDUSTRY



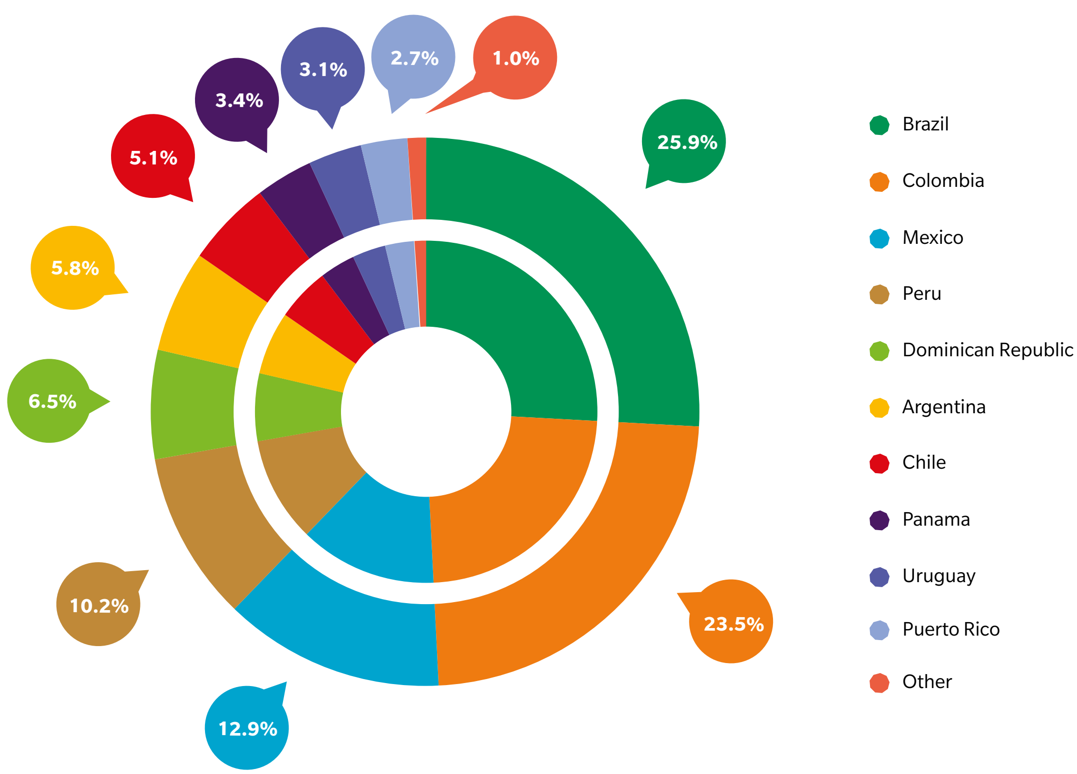
Graphic #40
DISTRIBUTION BY NUMBER OF EMPLOYEE



Graphic #41
DISTRIBUTION BY ANNUAL BILLING



Graphic #42
DISTRIBUTION BY COUNTRY



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Strategic Partner Marsh & McLennan Companies

EXCELLENCE IN RISK MANAGEMENT XIV
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April, 2017.

I BENCHMARK DE GESTIÓN DE RIESGOS EN LATINOAMÉRICA
Marsh Risk Consulting LAC & RIMS,
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II BENCHMARK DE GRESTIÓN DE RIESGOS EN LATINOAMÉRICA
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