

Emerging Risks in an Uncertain World

White Paper Series
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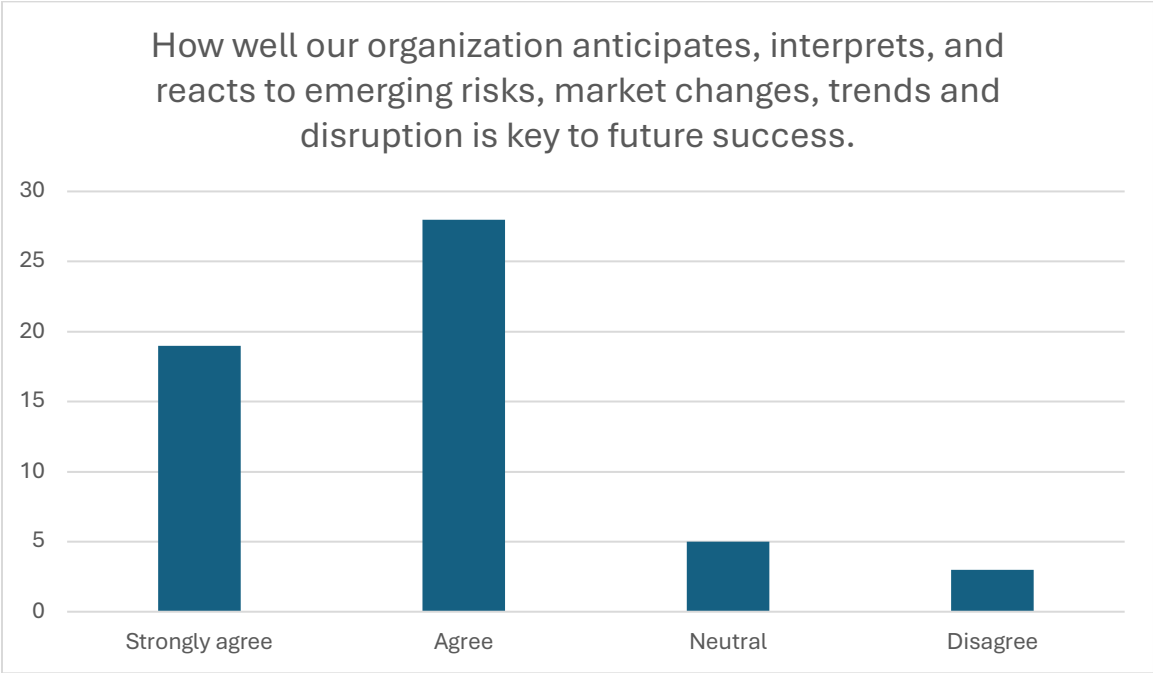
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Emerging Risks

Top risk executives gathered to improve their risk acumen on emerging risks at the Center for Excellence in ERM's 16th ERM Summit. The focus on emerging risks seemed to be driven by the sense that the world is getting riskier and more uncertain. This belief was reinforced by an expert on geopolitical risk that kicked off the Summit. The expert noted that geopolitical risk is growing in importance around the world, partly because the U.S. and China are in strategic competition. The situation is amplified even more by conflicts in the Middle East and Russia/Ukraine, along with global elections around the world in 2024. Some good but still disruptive geopolitical news included the AI boom, the UK's improved relations with the EU, and India's growth. It was noted that geopolitics will likely keep driving change.

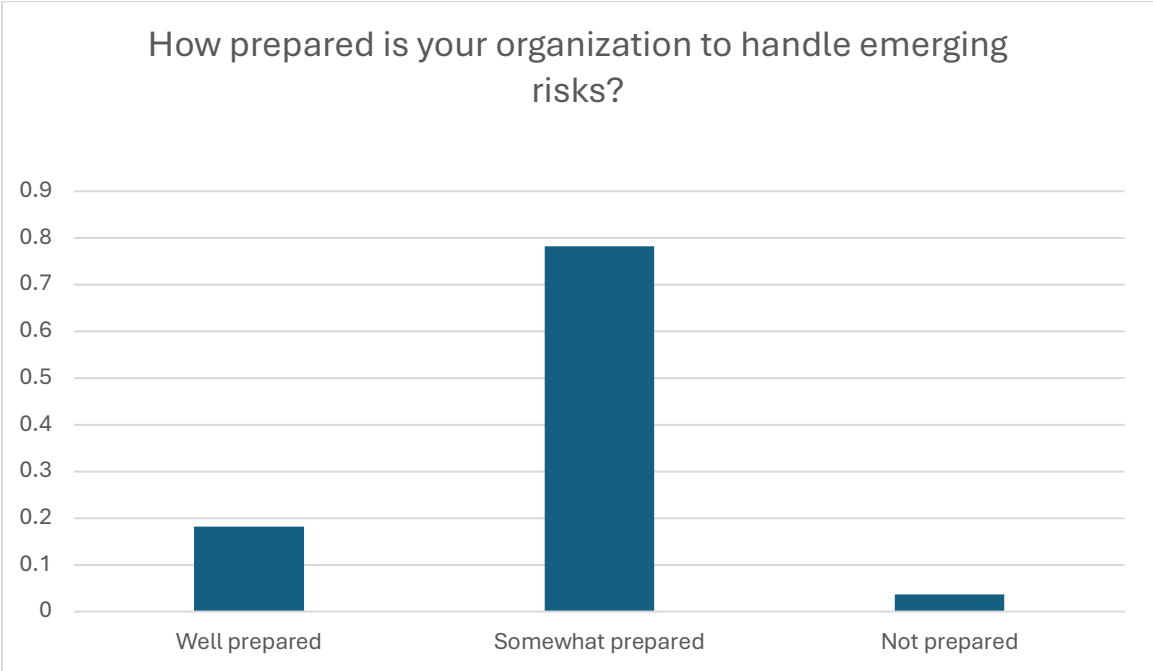
Most risk executives at the ERM Summit agreed that risks such as geopolitical are driving uncertainty. They wanted to understand it better, along with other emerging risks. Hence, the focus of the Summit was on how to build and improve an emerging risk process.

Many risk executives already had an ERM process at their organization but many also felt they lacked the full capacity to comprehend emerging risks and they wanted to get it right. In fact, they needed to get it right since the survey indicated that *almost everyone felt that how well they manage emerging risks is key to future success.*¹



¹ The survey results are based on the risk executives involved in the ERM Summit. The survey was not designed to be a scientific study but rather, was designed to capture the risk acumen of the executives on the subject of emerging risks.

Although many noted that being prepared was key to success, many also added that they were not fully prepared to handle emerging risks. In fact, very few believed they were “well prepared.”



The combination of emerging risks being critical and not everyone being fully prepared implies a lot of room for improvement and exposure to emerging risk. Both ISO 31000 (2018) and COSO Enterprise Risk Management (2017) cover emerging risks. In ISO 31000 it is noted that a range of techniques are used to identify risks and that one (of many) factors to consider is emerging risks. Thus, it seems ISO 31000 implies emerging risks are part of the normal risk identification process. COSO’s Enterprise Risk Management Framework (2017) addresses emerging risks with the approach of including Principle 15 – “addresses substantial change.” The framework notes that organizations need to be aware of changes and new risks and should consider both internal and external sources of change.

A separate emerging risk process?

Fifty percent of the risk executives noted that they have an emerging risk process that is *separate* from the regular enterprise risk process. Many stated that ERM either leads the emerging risk process or is engaged or consulted in the emerging risk process. Many different functions are involved in the emerging risk process. The departments involved vary by organization but can include legal, audit, strategy, the c-suite, product teams, outside counsel, marketing, crisis management, financial planning, etc.

The Process

The actual emerging risk process varies by organization. Approaches include internal and external scans, stand up meetings, surveys, deep dives, strategic planning refreshment workshops, and focused emerging risk workshops. Others utilized design thinking, scenario analysis, or started off by department and aggregated up. Also mentioned were third-party intelligence, country risk data, studying the competition, and peer reviews. Many described their emerging risk process in detail. One risk executive stated:

“The ERM team conducts a targeted risk assessment during odd fiscal years to evaluate exposure to new and/or emerging risks that are not currently included in the Enterprise Risk Profile. Key activities include: 1) Environmental Scan -- Systematically scan internal and external sources of risk; 2) Focus Interviews -- Survey agency senior leaders on potential new/ emerging risks; 3) Focused Interviews -- Validate new/ emerging risks and gathered additional insight and context; 4) Risk Assessment and Prioritization -- Facilitate risk governance deliberation on new/ emerging risks.”

A second risk leader stated,

“Continually scan and monitor the external environment and external publications. Every 2 years we send our Risk Committee an Emerging Issues and Trends survey. We intentionally do not call them "risks," rather issues and trends.”

A final example included,

“We interview all department heads at least annually as part of our normal ERM risk identification. During this process we have a set of questions designed to surface emerging risks. If any are identified, we use a different format to capture and assess those emerging risks. These are then analyzed and included in a separate section on our risk reporting.”

Other risk executives noted that it is important to define emerging risks and distinguish them from other risk categories. One company used the following definitions. *Emerging Risks* - A risk that is underpinned by a high level of uncertainty. Can become a business unit risk or even an enterprise risk over time. *Business Unit Risks* - A risk that could impact a function or region’s ability to achieve its objectives. Can contribute to enterprise risks. *Enterprise Risks* - A subset of business unit risks that has the potential to impact the company’s ability to achieve our enterprise objectives. Another leader used three categories: top 10 risks, a watchlist, and emerging risks. One risk leader emphasized that some emerging risks are best treated as drivers of other risks vs as a separate emerging risk.

The risk leaders used a variety of sources to look for emerging risks. Some top *internal* sources were

- risk interviews,
- surveys,
- talking to the business owners, field staff, senior leaders, and risk champions, and

- ongoing risk assessments.

Some top *external* sources included

- other risk executives,
- third party service providers,
- consulting firms,
- subject matter experts,
- global risk publications (such as World Economic Forum), and
- customers.

Even though there appears to be a plethora of sources, challenges remain. Thirty-five percent noted that insufficient information is still a problem and thirty-two percent identified a lack of resources as a challenge. Other key challenges in emerging risk included integrating the emerging risk data with other data (including data from other parts of the organization), breaking down silos, getting stakeholder buy-in, having the knowledge to identify relevant emerging risks, and “figuring out which emerging risks really merit time and attention.”

Many were trying to link emerging risk to their strategic planning process. The approaches varied from having a conversation with strategy to having a session during strategic planning that focuses on emerging risks. Several noted that ERM “informs” strategic planning. Others had ERM and Strategy working together with senior leadership. Similarly, one company had an annual “strategic risk workshop” that focused on emerging risks. One organizational approach included having the head of strategy be a member of the management risk committee. Another approach or tool explored at a prior Summit was using gen AI to help generate a set of potential emerging risks. This requires some customization of the prompts and a bit of practice but has a lot of potential in coming up with potential emerging risks.

Tools

A variety of tools were being used to identify the emerging risks. Some of the tools mentioned included talking to people, current staff, senior leaders, and conducting emerging risk workshops. Some noted the presence of an emerging risk committee as a tool. One risk leader noted the importance of learning to “ask the right questions to the right people.” Others stated they use external consultants to help them. Reviewing external sources was considered a popular tool, including industry reports, industry conferences, and vendor reporting. Another executive highlighted they don’t use one tool but several tools, including SWOT analysis, horizon scanning, pre-mortems, backcasting, black swans, grey rhinos, and several versions of scenarios analysis. They added, “The trick is to select the right tools and use them at the right time to provide timely, impactful, and actionable advising on emerging risks.”

Differences in Concern

One interesting finding came up in the pre-Summit survey around the question of what's the one emerging risk the risk leader is concerned about vs what is the top emerging risk the board is concerned about. The risk leaders responded that their top concerns were

- geopolitical risks,
- AI risks,
- and technological risks (e.g., missing a key leap in technology or disruption).

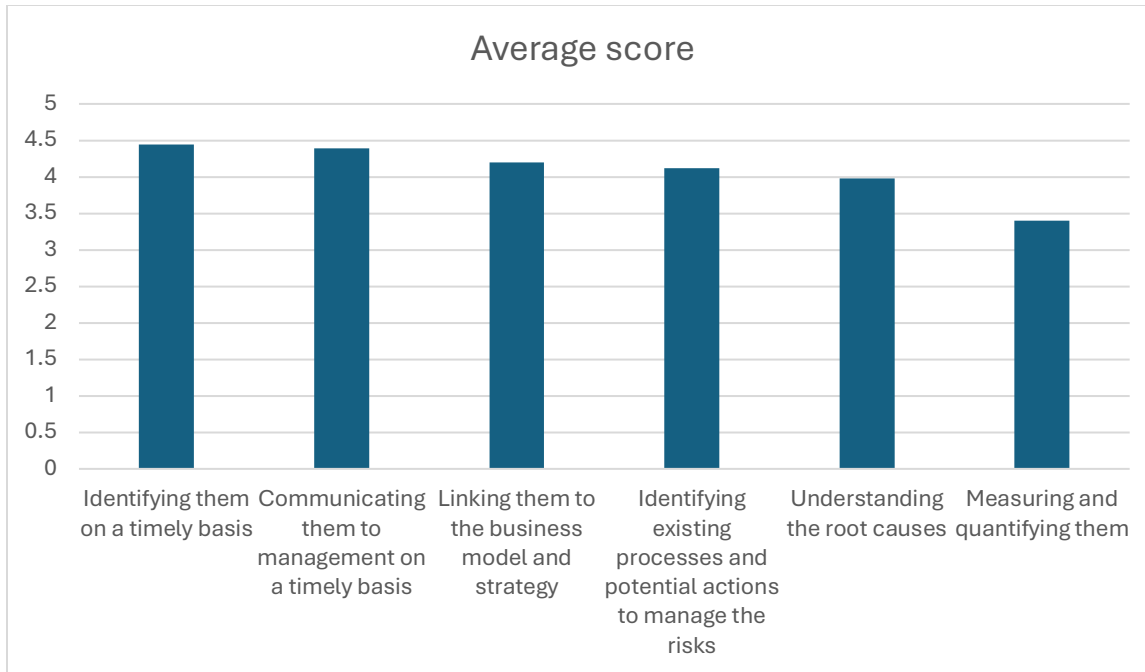
When those same risk leaders were asked the board's top concern the answers were

- the emerging risk process,
- AI,
- technology risk, and
- geopolitical.

In other words, boards appear to be most concerned that the organization has an emerging risk process. Additional comments related to the emerging risk concern question was that the board was concerned that risks were identified timely, that the company knew the velocity of the risk, and that they knew how the risk might impact strategy and the business model. Over half of the organizations noted that emerging risks are included in board reports and another twenty-two percent noted that they have plans to include emerging risks in the board report.

Keys

One important question in the Summit survey asked the risk executives about the keys to emerging risks. The top ranked key was to identify the emerging risks on a timely basis. You have to see the risk. As noted above, this is not always easy. Coming in as the second highest rated key was communication. You have to communicate the emerging risk to the right parties, most likely that's management and the board. But notice the next few keys. It's not enough to identify, you have to link it to the business model and strategy. We all know about certain risks such as gen AI but what the risk executives are pointing out is that it is almost as important to be able to link to the business model. Identifying actions to manage the risk rounds out the top four keys. You've got to act. This one makes sense too, in an obvious way. What is the organization doing about the risk? Recall that Kodak saw digital and Blockbuster saw Netflix – they still had to make some choices about how to react. Many companies today face this same crossroads with geopolitical risks or AI risks.



Thinking about more than emerging risks

Two of the best thought pieces around strategy and disruption over the decades are Drucker’s Theory of the Business and Christenson’s Innovator’s Dilemma. Drucker argues that every 3 years organizations should challenge every assumption they have about their environment, their mission, and the core competencies needed to achieve the mission. Drucker also adds that part of the theory of the business must consider the *ability* to change.

Christensen argues that too many people talking about disruption haven’t read anything serious about what disruption truly means. He notes that if you get sloppy about understanding disruption then you use the wrong tools in the wrong context. Christensen argues that incumbents tend to not fully understand the path of disruption compared to their own efforts to succeed.

Executives and boards must not only see the emerging risks but they must carefully evaluate the level of disruption and how these risks impact the business model and strategy. That is not an easy task but it is a critical task. The importance of this task shows up when the risk executives were asked what the board asks about. The results show that although 71% of boards ask about emerging risks, 81% ask about disruptive risks, 64% ask about legacy business model risks, and 37% ask about unknown risks. Risk executives may want to consider these other types of risks as they build and enhance their emerging risk process.

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