StrategicRISK

THE KNOWLEDGE

INTERNATIONAL RISKS

Welcome to the first issue of The Knowledge – *StrategicRISK's* new insight supplement that surveys Asia-Pacific risk managers. Here we look at the key challenges of operating across borders

THE SURVEY

The risk landscape

People risk, supply chain issues and regulatory compliance are the top three risks for doing business across international borders

People risk is the most pressing issue for 50% of risk managers operating in Asia-Pacific.

More risk managers in the region said a people risk event was 'likely' or 'very likely' to occur within the next 12 months, ahead of other key risk events such as cyber breaches, supply chain issues or extreme weather events.

This was one of the key findings of the inaugural StrategicRISK benchmarking study that examined the risk of doing business across international borders.

More than 60 risk managers from around Asia-Pacific took part in the research, which aimed to find out which international risks are most likely to impact businesses and how the companies are managing these.

The results from the survey are outlined on the following pages and aim to provide risk and insurance managers with comparative data and additional material to enable them to benchmark their roles, internal risk function and risk priorities.

According to respondents, the top three risks to impact international business are: people risk, supply chain risk and regulatory compliance.

A risk manager from a major airline told StrategicRISK that this came as "no surprise".

"Today risk managers have to look at managing risks across many geographical areas, involving diverse cultures and regulatory operating environments, and yet continue to be exposed to impacts such as cyber attacks that are not bound by any physical barriers."

For Vincent Ho, safety manager at MTR, the rapid transit railway system in Hong Kong, people risk was deserving of its top spot on the list.

"As businesses go global, many operations start to see their workplace expand into unknown territories and also in area where skillful labour is a scarce resource. We have seen a whole team of staff jump from a company to another overnight," he said.

"People risk can significantly affect the quality standard of a company and cause immediate effect on the bottom line."

But InterContinental Hotel Group, director of corporate risk and reputation, greater China, Rudi Wertheim said he was surprised by the results.

"I'm not discounting the people risk but my view is that the single biggest threat that could potentially have the most catastrophic consequences [on a company] is cyber," he said.

"People can get at data so easily, and clearly if you're in any industry where people have to trust you in order to do business with you and if a cyber event breaks that trust then you've got a huge problem.

"As I see it, people risk is somewhere below cyber in terms of its potential to 'break' a company. But in terms of it being something that we need to be tackling on an ongoing basis, it's absolutely right up there."

RISKY BUSINESS IN ASIA PACIFIC

METHODOLOGY

Respondents were asked to rate 19 different risks by the likelihood of a risk event occurring in the next 12 months and the estimated financial impact this would have on their business. They were asked to rate each risk event by both likelihood and financial impact on a scale of 1-5 (1 being very low, 2 being low, 3 being medium, 4 being high and 5 being very high).

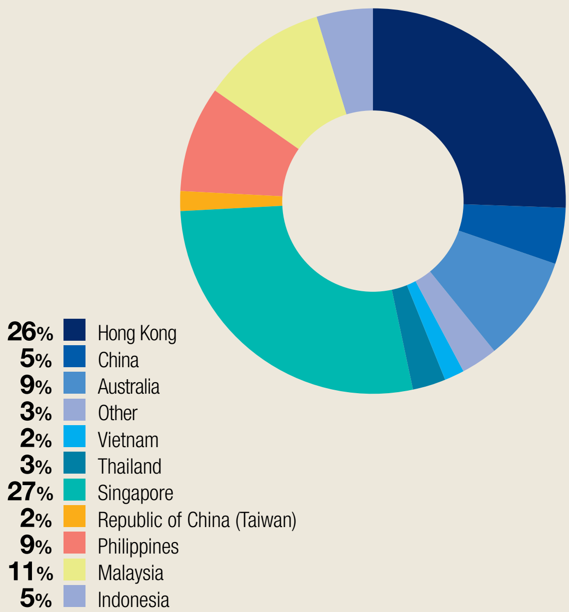
To plot the scatter graph (right), the average likelihood and financial impact score was calculated for each risk and plotted along the x-axis and y-axis, respectively.

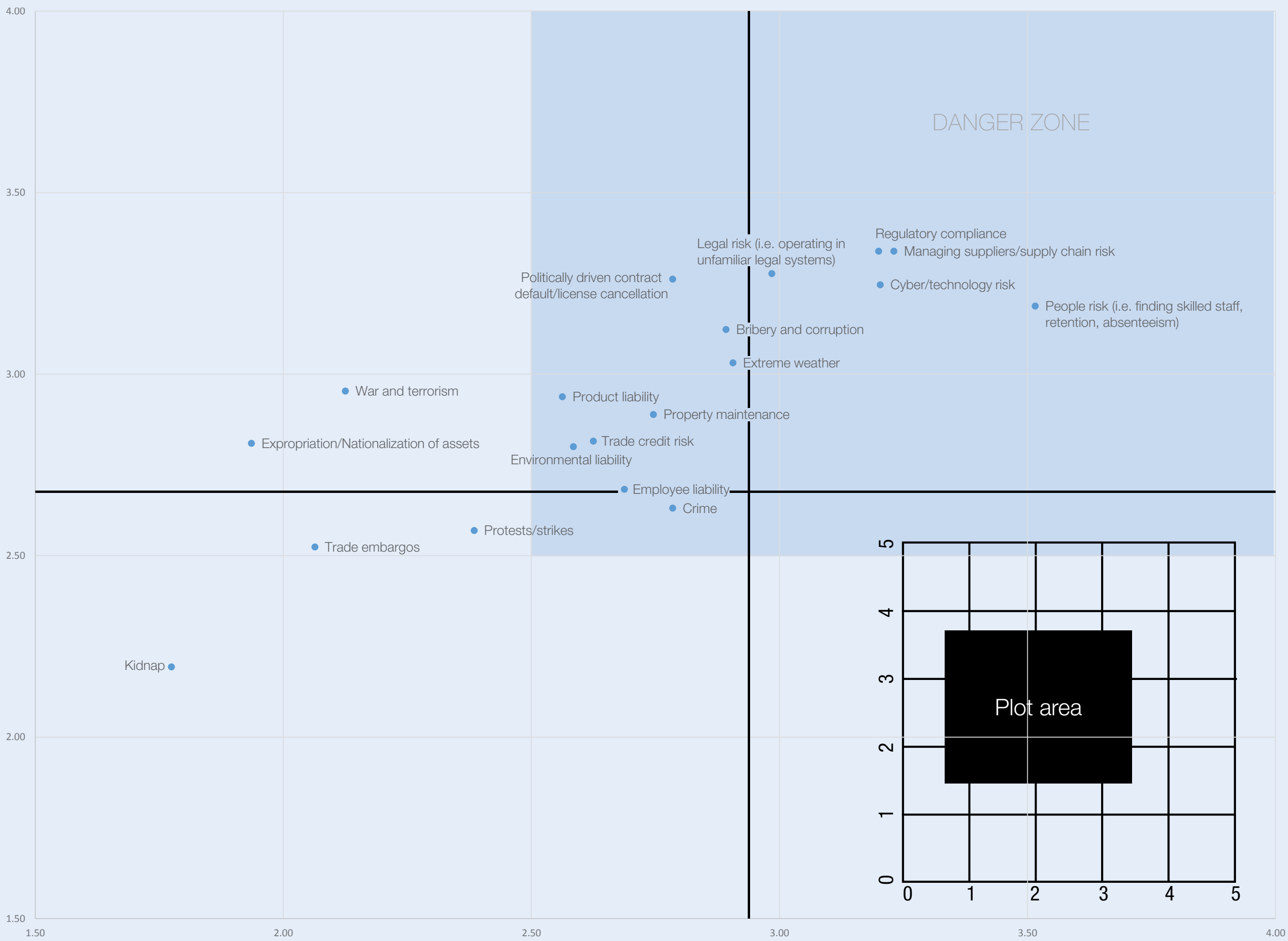
The scatter graph also displays the average likelihood (2.68) and financial impact (2.93) scores across all risks. Those risks in the top right hand corner of the graph were rated by respondents as having above-average likelihood of occurring in the next 12 months and were deemed to have an above-average financial impact if they were to occur.

To identify the risks of highest concern (that is, those most likely to occur with the highest financial impact) a combined average score was calculated for both likelihood and financial impact for each risk and ranked in order of size. The higher the score, the more likely a risk is to occur and have a high financial impact.

WHO TOOK PART?

Risk managers from around Asia-Pacific took part in our survey. Here's where they were from:





TOP RISKS

WHY RISK MANAGERS ARE LOSING SLEEP

TOP 10 RISKS OF HIGHEST CONCERN*	
People risk (i.e. finding skilled staff, retention, absenteeism)	3.35
Managing suppliers/supply chain risk	3.28
Regulatory compliance	3.27
Cyber/technology risk	3.22
Legal risk (i.e. operating in unfamiliar legal systems)	3.13
Politically driven contract default/ license cancellation	3.02
Bribery and corruption	3.01
Extreme weather	2.97
Property maintenance	2.82
Product liability	2.75

(*combination of most likely and highest financial impact)

TOP 10 RISKS MOST LIKELY TO OCCUR	
People risk (i.e. finding skilled staff, retention, absenteeism)	3.52
Managing suppliers/supply chain risk	3.23
Cyber/technology risk	3.20
Regulatory compliance	3.20
Legal risk (i.e. operating in unfamiliar legal systems)	2.98
Extreme weather	2.91
Bribery and corruption	2.89
Politically driven contract default/ license cancellation	2.78
Crime	2.78
Property maintenance	2.75
Employee liability	2.69

TOP 10 RISKS WITH THE HIGHEST FINANCIAL IMPACT	
Managing suppliers/supply chain risk	3.34
Regulatory compliance	3.34
Legal risk (i.e. operating in unfamiliar legal systems)	3.28
Politically driven contract default/ license cancellation	3.26
Cyber/technology risk	3.25
People risk (i.e. finding skilled staff, retention, absenteeism)	3.19
Bribery and corruption	3.12
Extreme weather	3.03
War and terrorism	2.95
Product liability	2.94

THE SURVEY CONTINUED

The top five risks in action

Risk managers, brokers and academics weigh in on the risks that came out on top of the first annual survey about operating across international borders

"You can have the best machines, the best methods (policy and processes) and materials (resources), but when you do not have the best manpower (right people in place) it is the biggest risk."

This is the reality for Roland Teo, risk manager in a Singapore health care group and board member of PARIMA (Pan-Asia Risk and Insurance Management Association) and RIMAS (Risk and Insurance Management Association of Singapore).

Teo has articulated the key reason that Asia-Pacific risk managers chose 'people risk' as their top concern for operating in the region.

"This risk is exacerbated by the current war for talent in almost all sectors and the shortage of qualified healthcare professionals in Singapore and the region," he said.

Myanmar Brewery head of risk management, processes and internal controls Jagath Guru said that the region's people risk was also owing to a generational problem.

"The problem with Generation Y is that they do not stay long in an organisation," he said, adding that many employees are also pursuing opportunities outside of their home countries in search of better living standards.

Similar to people risks, supply chain is the lifeline for many businesses and its no wonder it places second on the list.

"Unless [companies] have a robust, diversified supply management system in place, a ripple from a far side of the world can cause major problems for a company," MTR China and international business safety manager Vincent Ho says.

"The Fukushima accident has woken many companies to the vulnerability of their supply chain, even when most thought they did not deal with Japanese suppliers."

As stated on page 1, people risk, supply chain and regulatory/compliance risk make up the top three risks for Asia-Pacific, according to our study; cyber and legal risks round out the top five.

1 People risk

What is it: The costs and negative implications that an organisation will incur as a consequence of things that happen to its people.

Example: Rates of sick leave, incidents of accidents and levels of productivity are poor compared to the industry average because of a high average age of employees and poor levels of physical fitness.

Impact: There is a drain on the ongoing profitability of the business arising from the characteristics of the workforce. There may be serious consequences in relation to health and safety because some employees are not as alert as they should be. Sick leave of key employees may be disrupting the delivery of sales orders and impacting the company's reputation.

Risk manager view: MTR China and international business safety manager Vincent Ho says: "People risk can significantly affect the quality standard of a company and cause immediate effect on the bottom line."

2 Supply chain risk

What is it: The risks of everyday and exceptional events occurring along the supply chain that threaten business continuity

Example: Japan's Tohoku Earthquake in 2011 caused major supply chain disruption to companies in almost every industry around the world.

Impact: Willis global head of forensic accounting and complex claims Ken Giambagno explains: "What ends up happening is that large corporations can't get a minor component part in the supply chain and therefore cannot manufacture and sell the major products. It could be high-end computers, for instance, but if they can't produce and sell as a result of their ability to get a mechanical device that turns the hard drive (as a result of the damage that second, third or fourth tier supplier) they are unable to get product out to the customers."

Academic view: Nanyang Technological University assistant director Jeffrey Yeo says: "Supply chain management is undoubtedly one of the major concerns of [international] businesses. Factors such as the political climate, local labour conditions and infrastructural conditions compound the risks attributed to the supply chain."

3 Regulatory compliance risk

What is it: The risks and costs associated of failing to adhere to local and industry laws, regulations, guidelines and specifications.
Example: Since 2012 China has tightened its regulatory environment to crackdown on anti-competitive behaviour by introducing measures that aim to promote local business and curb corruption.
Impact: Many multinationals based in China have lowered their growth forecasts to comply with the country's tougher regulatory environment. Control Risks senior managing director, Australia Pacific, Jason Rance said regulators are targeting firms and sectors with "super profit growth" and perceived anti-competitive behaviour, which are both red flags for potential corruption.
Broker view: JLT Strategic Risk Solutions manging director Philip Ondaatje says: "Good corporate governance and compliance are key to business success in the modern world. There are many nuances to building and running a compliant global or regional programme. My best advice – get the professionals to advise you!"

4 Cyber/ technology risk

What is it: Any risk of financial loss, disruption or damage to the reputation of an organisation from some sort of failure of its information technology systems.
Example: Last year in Japan, a rogue systems engineer subcontracted by education services provider Benesse leaked the confidential information of 48.6 million people - approximately one-third of the country's population.
Impact: The breach is expected to result in the largest multi-plaintiff lawsuit ever seen in Japan, with lawyers seeking Y100m. The leak hit every area of the company's operations and resulted in a 25% reduction customers in the year following.
Broker view: JLT broking executive Ronak Shah says: "Do not underestimate the financial and reputational damage a cyber breach can cause to your firm, no matter how isolated it is. Proper risk management, business continuity planning, a robust IT infrastructure, board oversight and other key approaches is required at the very minimum with a view to ringfencing all of this with the appropriate cyber security insurance."

5 Legal risk

What is it: The risk of financial or reputational loss arising from regulatory or legal action for or against a company.
Example: In September 2014, the Chinese courts found GSK China Investment Co, the Chinese subsidiary of the UK drug manufacturer GlaxoSmithKline, guilty of bribery.
Impact: The company was fined nearly $500m, the largest corporate fine in China to date. Additionally, five of the company's managers, including its former top China executive were convicted of bribery-related charges and received suspended prison sentences. GSK's Chinese operations are still the subject of investigations by US and UK authorities.
Risk manager view: MTR China and international business safety manager Vincent Ho says: "This is can be a root cause of many of the top risks listed [in the survey]. Some subtle local unspoken practice can also drive a company to the ground."

THE SURVEY CONTINUED

Global insurance programmes help mitigate regional risks

If the **price is right**, Asia-Pacific firms will look to an international insurance programme as a way to **reduce local compliance and regulatory concerns** that come with operating across borders

1 Reducing the cost of insurance and coverage gaps are the two key benefits for influencing the decision to set up an international insurance programme

Conducting business across multiple countries has never been easier, but doing so leads to a unique set of insurance and risk issues for organisations to manage. Increasingly, insurers are trying to ease this headache through international insurance programmes that coordinate local policies and deliver compliance under the one global policy.

"Fundamentally, the unique selling points for international insurance programmes are the reduction in cost and the reduction of coverage gaps. The so-called double 'R' benefits," says Jeffery Yeo, assistant director, Office of Enterprise Risk Management, Corporate Governance, at the Nanyang Technological University.

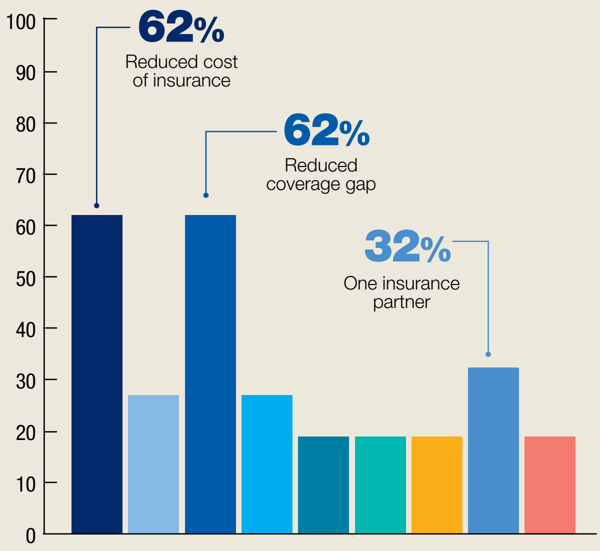
Respondents to the StrategicRISK survey agree.

When asked to choose the top three business benefits for setting up an international insurance programme, reduced cost of insurance and reduced coverage gaps came out in equal first place (62.16% each). The benefits of working with one insurer rounded out the top three, according to one-third of respondents (see table, above).

BENEFITS OF AN INTERNATIONAL INSURANCE PROGRAMME

What business benefits influenced, or are influencing, your decision to set up an international insurance programme?

- 62% Reduce cost of insurance
- 62% Reduce coverage gaps
- 32% Benefits with working with one insurance partner (improved customer service)
- 27% Compliance with local insurance regulation
- 27% Access to a wider range of insurance products
- 19% Reduce administration burden
- 19% Simplification of policy insurance
- 19% Improvement of claims process
- 19% Directive from senior management/board



"Risk transfer has always been a pillar of risk responses, and with the globalisation of risks, international insurance programmes become the default means of protecting businesses from residual risks that persists after prevention and mitigation controls," a risk manager from a major international airline tells StrategicRISK.

"While such programmes are expensive, the ability to diversify the exposures across many sites allows for economies of scale, and structuring/sharing of insurance limits to achieve a reduction in risk transfer costs."

But Lazada Group head of group risk and internal audit Gordon Song offers a word of caution to assuming that an international programme would reduce insurance costs.

"It is is arguable and needs to be studied and evaluated rather than taken for granted," he says. "A company that operates in many jurisdictions which do not recognise global policies and require local policies may find that the cost advantage is not that great."

2 Competitive pricing and a good understanding of the global regulatory landscape are key to selecting an insurance partner

Price is the clear deciding factor in choosing an insurance partner for Asia-Pacific risk managers, with 72.22% of respondents choosing this as their number one option (see results, right). Insurers' understanding of global regulatory regimes came in second, albeit with only 47.22% of responses.

Lazada's Song believes price will remain a primary factor for insurance purchasing decisions for "a long time to come".

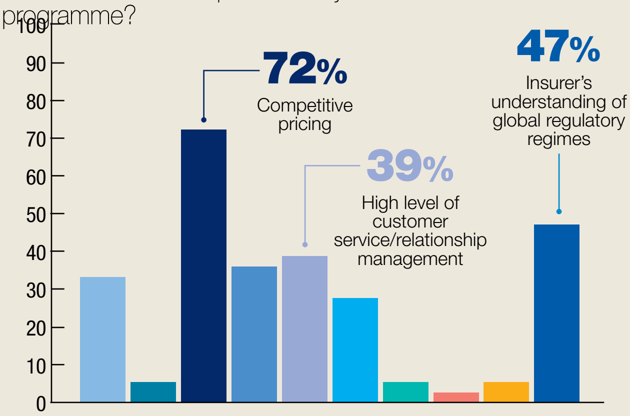
"The reason is intuitive: many people (executives and risk managers included) still hold firmly to the belief that insurance is paying for something that may never happen. All else equal, nobody would want to pay more," he says.

"However, coverage is also important, so there is always a need to balance risk with cost, and that boils down to risk managers having a meaningful, quantified discussion with the senior executives and the board on 'risk appetite'. In many cases this is not a very well developed competency yet, which is where the problem starts."

> "There is a need to balance risk with cost ... that boils down to a discussion on risk appetite

CHOICE OF INSURANCE PARTNER

What factors influenced, or will influence, your decision to select an insurance partner for your international insurance programme?



- 72% Competitive pricing
- 47% Insurer's understanding of global regulatory regimes
- 39% High level of customer service/relationship management
- 36% Breadth of coverage on offer
- 33% Speed and accuracy of claims handling
- 27% Size on insurer's international network
- 6% Ease of access to senior decision makers
- 6% Access insurer's risk engineering expertise
- 6% Other (please specify)
- 3% Access insurers programme management tools

3 Understanding the risk and insurance requirements of regional units remains the biggest challenge when structuring an international programme

In recent years, the legal and regulatory environment in many Asia-Pacific countries has evolved. With this backdrop, it is no wonder that 36% of survey respondents chose 'understanding the risk and insurance requirements of regional business units' as the biggest challenge when structuring an international programme.

"The understanding of the local regulatory requirement is without a doubt the first thing business operators should know and understand before making the plunge. For certain countries, the legal/regulatory requirements could have many shades of grey areas," Nangyang's Yeo says.

JLT managing director Philip Ondaatje agrees: "Good corporate governance and compliance are key to business success in the modern world.

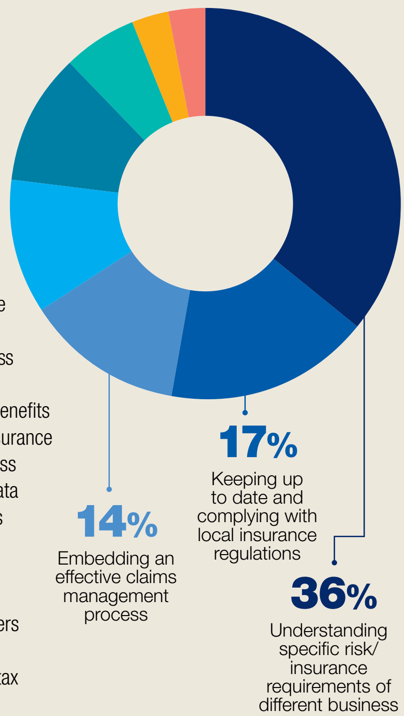
"Given the current macro economic environment and scrutiny placed on expense controls, perceived intangibles such as insurance, are right on top of the list of savings."

But this causes concern, Ondaatje says, owing to the many nuances to building and running a compliant global or regional programme.

CHALLENGES FOR INTERNATIONAL INSURANCE

What is the single biggest challenge you faced, or are facing, in structuring an international insurance programme?

- 36% Understanding the specific risk/insurance requirements of different business units/geographies
- 17% Keeping up to date and complying with local insurance regulations
- 14% Embedding an effective claims management process across business units/geographies
- 11% Communicating the benefits of an international insurance solution to the business
- 11% Obtaining accurate data from different business units/geographies
- 6% Other (please specify)
- 3% Getting expert advice from insurance partners
- 3% Understanding and complying with local tax treatments



THE BIG STORY

Asia yet to fully awaken to cyber exposures

High-profile data breaches in South Korea and Japan and **tightening data protection laws** should drive **cyber liability up** Asia's risk management agenda

Last year a Japanese education services provider hit media headlines for all the wrong reasons. A rogue systems engineer subcontracted by Benesse had leaked confidential information of 48.6 million people – about one-third of the country's population. The breach sparked an investigation and what is expected to be the largest multi-plaintiff lawsuit ever seen in Japan.

In another major cyber breach last year, the data of 20 million South Koreans was stolen. The names, social security numbers and credit card details of 40% of the population was leaked by a computer contractor working for credit scoring firm the Korea Credit Bureau.

But despite these huge data breaches, cyber risk only ranked 24th in the Asia Pacific list of top risks, according to Aon's 2015 Global Risk Management Survey.

This suggests the region's corporates are not as alert to the exposure as the global average, which placed cyber risk in the top 10 for the first time this year.

This could change in the future if greater harmonisation of data protection laws become a reality. ASEAN has stated its commitment to implementing standardised rules across its group of 10 countries.

In response to its major data breach, the South Korean government issued new amendments to existing data protection laws, which came into force on 30 December. These include steep financial penalties for companies that fail to protect data, a move that stands out in Asia where damages are typically not awarded to data breach victims. The rules also place stricter obligations on data handlers, expressly including security requirements for mobile devices.

Singapore and Malaysia have also implemented new 'European-style' privacy laws, while in China, consumer protection laws were amended to include data privacy principles. Hong Kong and the Philippines also have privacy legislation.

In part due to these changing laws and recent high-profile data breaches, cyber liability is on risk managers' radar, says JLT Asia director for risk services Craig Paterson. "If you are in the service industry then the concern is over cyber risks. Have you the right protection in place? Do your staff understand their responsibilities? As technology continues to develop it is becoming increasing more difficult to manage these types of risks."

EVOLVING INSURANCE SOLUTIONS

INSURERS ARE SLOWING RESPONDING TO THE CYBER RISK BUT PRODUCTS ARE OFTEN LIMITED AND LACK STANDARDISATION

While the cyber insurance market is still in its infancy, a range of products and services are starting to emerge.

"Many of our clients have started to put together some quite sophisticated cyber crime blended programmes," says Aon Risk Solutions Singapore regional director Nicholas Clarke. **"Traditionally financial institutions used to buy that cover but now we're seeing a lot of non-financial institutions start to put those types of programmes together."**

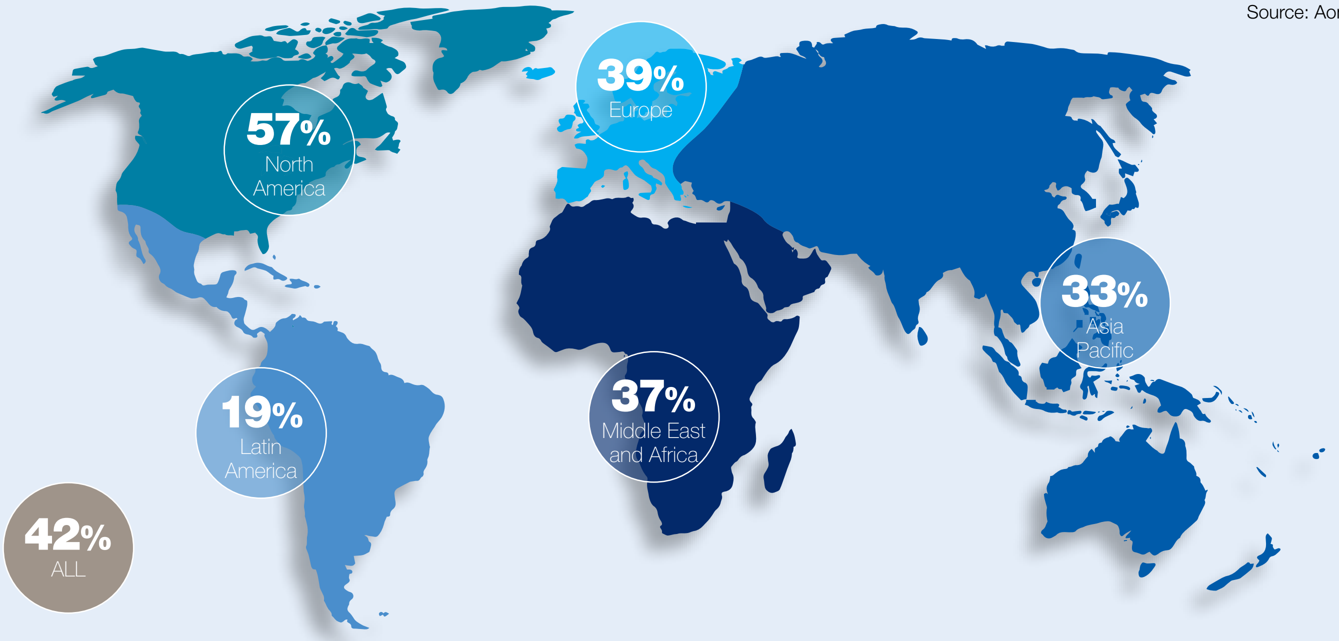
Most cyber insurance policies offer an indemnification along with access to key experts in the event of a breach, such as forensic IT, legal and crisis management. **But while capacity is growing and wordings are becoming broader, there is still a lack of standardisation.**

For the right risk transfer solutions to exist, the exposures themselves need to be properly understood, says Zurich Global Corporate head of international sales and distribution, Asia Pacific, Fernando Denes. "At every event you go to everyone is talking about cyber, but we don't understand it properly. We don't truly understand how connected we are and a lot of people today think that **cyber is only in relation to customer data being stolen,** because those are the indicators we're seeing in the US. **But we're probably going to start seeing variations in claims going forward."**

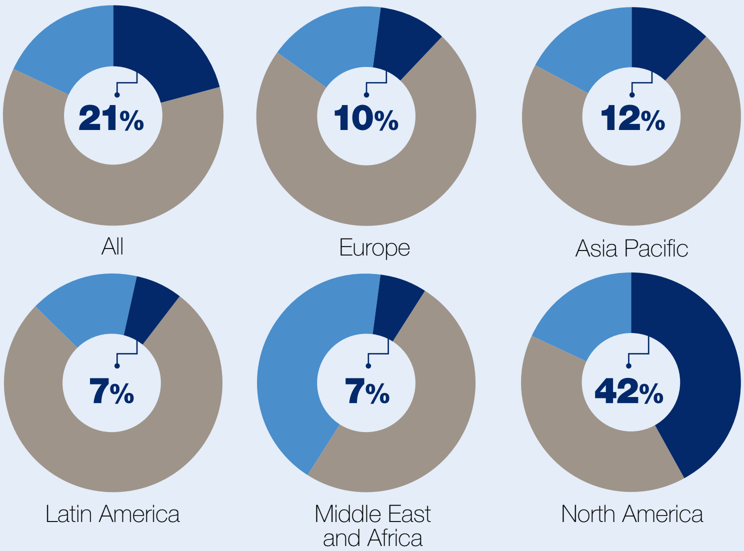
"Cyber insurance is very topical given the number of very high profile events throughout the world," adds Marsh head of placement for Asia Pacific John Donnelly. "The insurance market is only beginning to develop and lots of new capacity is entering the market. The challenge is to get the cover to meet the exposures, which need to be fully understood by the buyer of the insurance and the insurers. **This market for cyber insurance will no doubt develop rapidly in the coming years."**

PERCENTAGE OF FIRMS THAT HAVE CONDUCTED A CYBER RISK ASSESSMENT

Source: Aon



Purchase of cyber insurance coverage by region



■ Insurance currently purchased
■ Not purchased and no plans to purchase
■ Plan to purchase

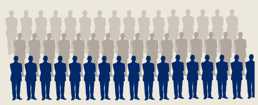
Source: Aon

TOP 10 RISKS

Aon's 2015 Global Risk Management Report picked the following as the top risks in Asia

1. Increasing competition
2. Failure to attract or retain top talent
3. Damage to reputation/brand
4. Business interruption
5. Economic slowdown/slow recovery
6. Political risk/uncertainties
7. Failure to innovate/meet customer needs
8. Regulatory/legislative changes
9. Cash flow/liquidity risk
10. Exchange rate fluctuation

BIG NUMBERS

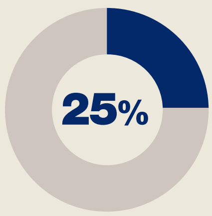


48.6m

Number of Japanese whose data was exposed in the Benesse leak

20m

Number of South Koreans who lost data in the Korea Credit Bureau breach



Reduction in Benesse membership in the year following its data leak scandal

¥100m

Amount in yen lawyers are seeking from education service provider Benesse following its data breach

THE INTERVIEW

Franckly speaking

StrategicRISK spoke to **Franck Baron,** PARIMA chairman and group general manager, risk management and insurance, International SOS, about the risks on his radar in Asia

How has the risk landscape in Asia evolved over the past five years?

Some of the themes that have emerged include super-spreader risks and the greater interconnection of risks. Increased instability can't be washed away but should be taken care of through prevention, proactive risk management and risk financing. Risk is on the c-suite agenda, but are we as risk managers?

We also face a density risk. Growing concentrations of activities take place in a small number of world epicentres: the global financial system is effectively rooted in New York and London, global electrical manufacturing concentrated in certain regions of China and Hong Kong, Thailand produces 40% of the world's hard drive disks etc. When Tropical Storm Nock-ten hit Thailand in 2011 it affected car and computer manufacturers all over the world. Profit-driven outsourcing had led many firms to the same cost-efficient location.

What are some of the risks that you are concerned about?

1. The lack of loss prevention and health and safety focus. We witness a wide range of attitudes and knowledge about health and safety, fire safety, risk engineering and loss prevention, with some owners and managers being highly motivated to make positive changes. Others still see any change as a threat to their status, livelihood or profit line. The motivation ranges from those who feel a moral obligation to make changes (duty of care), to those who are doing it because of external legal, social or financial pressures.

2. The transmission of diseases. Although one generally thinks of globalisation as a process involving a multiplicity of locations, and thus a geographical diversification of risk, in practice it has also resulted in a concentration of risk and instability. By allowing these nexuses to arise, the world is literally putting all of its eggs in one basket and leaving itself vulnerable to highly disruptive hazards.

Globalisation, population growth, and urbanisation have facilitated the transmission of infectious diseases. The complexity of global travel and global integration means that any 'patient zero' is now but a few degrees of separation from formerly isolated communities.

According to medical experts, more than 30 new disease-causing organisms have appeared in just the past two decades. These have included such deadly pathogens as Ebola, Hepatitis C and HIV. In addition, diseases such as cholera, malaria and the plague, once believed eradicated, have returned with even greater virulence.

By 2025, the fraction of the world's population living in cities is expected to rise to 70%. This is important everywhere, but especially in overcrowded or unhygienic conditions, where people live close to animals and where water is easily contaminated. Many 'bio-geographic barriers' have been removed. Continual introduction of pathogens to new regions is inevitable in our globally connected planet. In the 21st Century, no disease can remain a solely local or national problem.

3. Global warming, or, more neutrally, climate change facts include long time series for global average temperature, global carbon dioxide concentrations, and sea level rise. Considerable uncertainty exists in many forward-looking estimates but also highlight the long timescales over which they are expected to emerge.

This impacts both risk management and insurance. The insurance industry serves the broader economy by bearing unwanted volatility. The greater the volatility the greater the value that insurance can add to the global economy. Let's not forget that 183 million Asians are threatened by inundation due to rising of sea levels.

> "The complexity of global travel and global integration means that any 'patient zero' is now but a few degrees of separation from formerly isolated communities."

What are some of the unique risks affecting Asia's megacities now and into the future?

The majority of global urban assets are not adequately protected and insured and yet cities are more at risk than they should be. As economic growth creates more assets which require protection, the insurance industry can move to the next level by successfully demonstrating the value of insurance to businesses, governments and society at large.

2011 was a year of major catastrophe losses from the region. As insured values increase, presumably such events will become more common. What are the challenges from a natural catastrophe perspective?

One area where insurance plays a crucial role is in mitigating the impact of business interruption, which was well demonstrated during 2011. But a recent report by the Asian Development Bank tells us that only 7.6% of Asia's economic losses were insured last year, compared with 67% in the US. With low insurance penetration rates, the burden to cover the cost of catastrophes falls on governments and taxpayers.

Insurance take the risks of natural catastrophes off the balance sheets of businesses and the taxpayer. It is an area where insurers can add very clear value to society. Society must strengthen the resilience of urban areas through both physical and financial precautionary measures.

The nat cat exposure in Asia is, first of all, a great opportunity to raise the need for better risk

"Risk is on the c-suite agenda, but are we as risk managers?"

management, loss prevention and insurance. This being said, a lot still needs to be done, including a more risk management-minded dialogue with local authorities to treat catastrophe exposures as critical ones.

As the economy in Asia continues to grow and develop, how do you see risk challenges and insurance demands altering?

The challenges are twofold: (a) ensuring that the proper risk picture is provided to the final decision makers: as we witness still too much of compliance-driven ERM which does not provide enough emphasis on entrepreneurial risks/opportunities and the operational risk exposures (b) developing a more professional insurance sourcing and structuring to cope with the real risk exposures and provide organisations with a reliable financial protection

Disasters have heightened an urgency to strengthen risk management across the region. In the past decade, the region has been blighted by several deadly and economically damaging catastrophes: the Indian Ocean Tsunami (2004), Cyclone Nargis (2008), the Tohoku Earthquake (2011), the Thai Floods (2011) and Supertyphoon Haiyan (2013).

Asian cities are the most heavily exposed to natural catastrophes, both in terms of the number of people potentially affected and economic impact. The Tokyo-Yokohama region is the top ranked urban area in terms of population exposed (see table, right). Many cities exposed in Asia and particularly southeast Asia are in countries where there is no developed insurance market.

Increasingly, the distinction between natural and man-made disasters is being blurred. Not only the causes, but also the implications, of virtually all disasters are the results of human action, as the differential impacts of hurricanes in Haiti and its neighbour the Dominican Republic (which shares the same island) attest. This should continue to encourage Asian corporates to rethink and improve their risk management functions.

Asia requires more insurance (given its low penetration in a few countries) and more understanding of its related professionalism and expertise. There is also a need for more relevant products such as cyber, business interruption and executive protection. This is a very key ambition and mission of PARIMA.

REGIONAL RISK

MOST VULNERABLE URBAN AREAS

URBAN AREAS WITH THE MOST PEOPLE POTENTIALLY AFFECTED BY ALL 5 PERILS*	
Tokyo-Yokohama (JPN)	**57.1m**
Manila (PHL)	**34.6m**
Pearl River Delta (CHN)	**34.5m**
Osaka-Kobe (JPN)	**32.1m**
Jakarta (IND)	**27.7m**
Nagoya (JPN)	**22.9m**
Kolkata (IND)	**17.9m**
Shanghai (CHN)	**16.7m**
Los Angeles (USA)	**16.4m**
Tehran (IRN)	**15.6m**

URBAN AREAS RANKED BY INDEX OF WORKING DAYS LOST, BY ALL 5 PERILS*	
Tokyo-Yokohama (JPN)	**4.50**
Osaka-Kobe (JPN)	**2.71**
Nagoya (JPN)	**2.69**
Pearl River Delta (CHN)	**1.78**
Amsterdam-Rotterdam (NLD)	**0.96**
Los Angeles (USA)	**0.93**
New York-Newark (USA)	**0.62**
San Francisco (USA)	**0.47**
Paris (FRA)	**0.46**
Taipei (TWN)	**0.39**

URBAN AREAS RANKED BY INDEX OF WORKING DAYS LOST RELATIVE TO NATIONAL IMPACT, BY ALL 5 PERILS*	
Manila (PHL)	**1.95**
Amsterdam-Rotterdam (NLD)	**1.31**
Tokyo-Yokohama (JPN)	**1.29**
San Jose (CRI)	**1.26**
Guayaquil (ECU)	**1.20**
Taipei (TWN)	**1.02**
Ndjamena (TCL)	**1.00**
Nagoya (JPN)	**0.97**
Tainan-Kaohsiung (TWN)	**0.90**
Lima (PER)	**0.90**

* catastrophic floods, storms, storm surges, earthquakes or tsunamis

Source: Swiss Re 2013

THE CLAIM

The shop window

The growing **complexity of supply chains** and conflicts surrounding the interpretation of wordings have **drawn attention to claims** in recent years

There is the common saying that claims are the shop window by which the insurance industry is judged. When a loss occurs, the speed and fairness with which a claim is settled affects the insured's perception of that insurer and the wider industry.

Major events in recent years have put many international insurance policies to the test, and shown the importance of getting the right cover and wordings in place.

For example, there were disputes over policy wordings and claims during the 2010 Bangkok Riots when insurers were deciding whether to classify the event as a 'terrorism' or 'riot' incident.

Multinational claims are often some of the most challenging to process given their inherent complexity and issues surrounding local compliance. These difficulties are often exacerbated in the aftermath of major catastrophes where sites are more difficult to access and claims and loss adjusting resources are stretched.

The complexity of supply chains in today's globalised world is one reason why multinational claims are more of a challenge, according to Ken Giambagno, global head of forensic accounting and complex claims at Willis.

He points to the Thai Floods and Tohoku Earthquake in 2011 as two recent examples of major events that not only caused widespread property damage but also business interruption and supply chain disruption.

"In Japan, there was an issue with the auto industry where they couldn't get certain colours of paint, and that manufacturer couldn't get the pigment from a local manufacturer in Japan that was flooded as a result of the tsunami," he says. "That had a major impact across the supply chain.

"What ends up happening is that large corporations can't get a minor component part in the supply chain and therefore cannot manufacture and sell the major products," he continues.

"It could be high-end computers, for instance, but if they can't produce and sell as a result of their ability to get a mechanical device that turns the hard drive (as a result of the damage to a second, third or fourth tier supplier) they are unable to get product out to the customers."

> "There is an increasing awareness of customers requiring specific language and very clear definitions"
> **Fernando Denes, Zurich**

"What becomes difficult and complex is many contingent business interruption policies typically have sublimits," he adds. "So they may have a sublimit for a tier one supplier. They will have a lesser sublimit for a tier two supplier and it get less and less the further away you get from the manufacturing process. However the impact on operations could be catastrophic. So there is coverage available but you have to be very careful in determining what those sublimits are."

LOCAL COMPLIANCE

The 2011 floods in Thailand were also an eye-opener from a compliance perspective. "Compared to other markets like China and Japan, Thailand is quite flexible from an non-admitted insurance perspective," says Zurich head of international sales and distribution for Asia Pacific Fernando Denes. "For most lines of business, you can cover risks in Thailand without having to place a locally admitted policy. Unfortunately, that was the solution sought by most customers with exposure in Thailand".

"Once the floods hit, brokers and insurers were confronted with the fact that while non-admitted risk cover was allowed, the performance of loss-adjustment activities was not. "

Denes says "this became quite a problem, creating a lot of uncertainty in a time where most customers were in need".

"Such catastrophic events always teach us a few lessons. This was a clear case where more attention to understanding customer needs and service requirements was critical. Customers who made a proper assessment and opted for the issuance of a local policy had an advantage. Compliance in

CHECKLIST OF POLICY GOVERNANCE QUESTIONS - CLAIMS NOTIFICATION/PROCESSING

- Are there any established provisions, statutory or otherwise, governing the notification of claims or circumstances under the local policy?
- In relation to third party covers, are there any prohibitions on the ultimate carrier paying settlement proceeds direct to the claimant, plaintiff or third parties?
- In relation to policies of indemnity, is it standard market practice for insurer consent to be provided prior to settlement?
- Are there requirements of local law that require the local insurance carrier to pay third parties direct and/or permit the insurance carrier to be a party in the litigation proceedings?
- Are there any specificities regarding establishing claim reserves, or the timing of said reserves? Are there prescribed rules relating to the currency in which claims must be paid?
- The extent to which, if at all, the direct payment of claims (direct indemnity provisions/cut through provisions) is permissible?

Source: Airmic

international insurance goes beyond risk coverage."

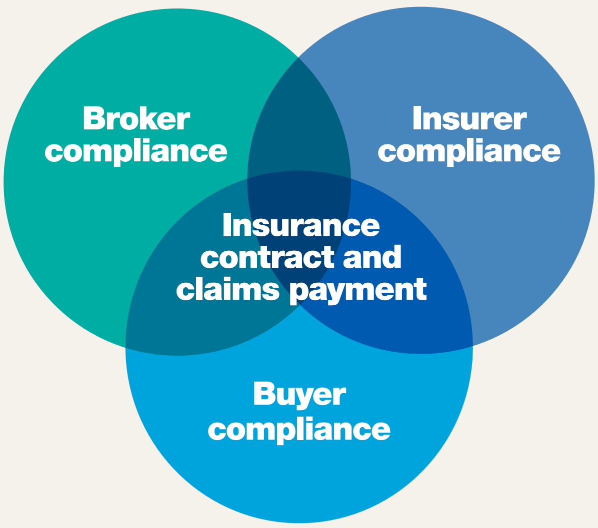
Tools such as Zurich's Multinational Insurance Application can be useful in this regard, helping to keep policyholders updated on changing insurance laws and regulations, tax environments as well as rules surrounding claims payment and loss adjustment among others.

"What becomes difficult and complex is many contingent business interruption policies typically have sublimits"
Ken Giambagno, Willis

Events such as the catastrophes in 2011 have helped to highlight the value of having broad and tailored coverage and thinking carefully about wordings before a loss occurs. "There is an increasing awareness of customers requiring specific language and very clear and precise definitions," says Denes.

"There is increased awareness that you need to care about claims payment when you're structuring an insurance solution," he continues. "A lot of times we tend to go towards whatever is easier and not fully thinking through, where will I have my claims paid? How can I make a $10m payment into Venezuela – is that easy?"

OVERLAPPING COMPLIANCE RESPONSIBILITIES



LESSONS IN CLAIMS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THAI FLOODS 2011

Disputes over claims arose following extensive flooding in Thailand, which reached its peak in December 2011. Seven major industrial estates were inundated, affecting numerous industries including computing and automotive, with a number of critical suppliers out of action for weeks. Disputes arose surrounding 'hours clauses' and whether the floods should be deemed more than one event as well as the inability to mobilise loss adjusters under non-admitted policies.


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BANGKOK RIOTS 2010

Confusion arose after government officials described the riots as a terrorism event, but later retracting that definition. It led to great confusion as insurers were uncertain whether claims should fall under terrorism policies or property policies that contain cover for "strikes, riots and civil commotion".


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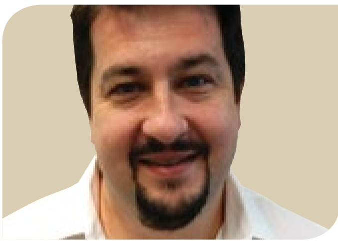
TOHOKU EARTHQUAKE AND TSUNAMI 2011

On 11 March 2011 a magnitude 9 earthquake struck off the coast of Japan, immediately followed by a devastating tsunami. The natural catastrophe triggered a manmade catastrophe when it caused a nuclear meltdown at Fukushima. Organisations that experienced business interruption (BI) as a result of supply chain interruption were not all indemnified for damage to suppliers' premises and the nuclear exclusion zone around Fukushima introduced a non-damage element to contingent BI.

THE PEOPLE

THE VALUE OF INTERNATIONAL PROGRAMMES

Phil Ondaatje, managing director for strategic risk solutions, JLT Specialty Asia



Nicholas Clarke, regional director, Aon Risk Solutions

John Donnelly, head of placements for Asia Pacific, Marsh

Fernando Denes, head of international sales and distribution, Asia Pacific, Zurich Global Corporate

Phil Ondaatje: "As Asian companies increasingly venture overseas and expand into new markets, the need to ensure that insurance programmes are seamless, while complying with increasingly vigilant insurance and tax authorities, is becoming far more relevant.

"For businesses with risks in territories outside their home country, the time comes when they must consider whether their interests are best served by a global insurance programme. The benefits for global insurance programmes typically include: uniform level of cover applied across companies/countries; elimination of gaps or costly overlaps in cover; economies of scale and leverage in negotiating with insurers; and streamlined administration, including coordination of claims.

"In most cases the overriding objective in establishing an international insurance programmes is the cost saving potential. Those unfamiliar with these type of programmes are generally unaware that localised coverages are also required for compliance reasons and thus the economics of setting up, may not necessarily be more efficient.

"Establishing a regional or global insurance programme requires detailed knowledge of local markets and practices."

Nicholas Clarke: "The attitude used to be: Find me the cheapest insurance policy you can get and the specifics don't matter a great deal. The proportion of buyers like that are on the decline and it takes one claim that doesn't work for that mindset to change.

"The priority is now to getting the right wording at the right limits for the best price. Our global clients definitely have that mindset and look at how they integrate their risk management information – so their risk registers, engineering reports and all of their analysis – to really make sure a policy covers all of the knowns as well as many of the unknowns you can think of.

"They are using things like nat cat modelling and scenario modelling to come up with the right limits and sublimits of the programme, and then looking at who is the best partner and how can we design that in the lowest cost way, optimising the total cost of insurable risk.

"Because we are in a soft market it's a great time to really broaden your cover ... and in a hard market you're likely to keep that cover. Normally in a hard market your price goes up, but it's sometimes impossible to get more cover. Soft markets are a great time to broaden what your wording can respond to."

John Donnelly: "The Asian insurance market reflects a buyers' market and premiums have reduced in many countries. The standout exception to this was Indonesia, where a tariff was introduced in February 2014 and, as a result, many clients have increased premiums in that market.

"The major account space has seen a lot of increased capacity over the past 12 months, intensely fuelling competition.

"The lack of catastrophe losses throughout the world is seeing insurers making record profits and shareholders and analysts expect this to continue.

"The reinsurance market, of course, is contributing greatly to pricing: $20bn of new capital has entered the market in the past two years. It's entering the market because of the profitability and lack of other alternative investment opportunities for that capital. The capital, when it comes into the market, must be serviced and reinsurers are providing their capacity to direct insurers at reduced rates. Those insurers are passing on those savings to their customers.

"There are going to be plenty of opportunities in 2015 – lots of new capacity and new entrants coming into the market."

Fernando Denes: "Asian companies operating overseas are increasingly concerned about both the certainty of local claims payments and regulatory compliance. This trend is also seen with smaller companies as the awareness of non-admitted coverage restrictions in key markets like China and Japan increases.

"To address these concerns, customers are looking for international programme solutions so as to obtain access to expertise and, also, convenience and control. Through a single point of contact, customers and brokers can place policies and cover risks in all continents without having to leave their offices. Significant investments in technology allow them to have online access to data such as premium payment, claims and risk engineering.

"This means that while there's greater concern on the ability to have local service and claims payment in the countries where they operate, customers buy an international programme for additional benefits as well.

"For example, subsidiaries often have different risk appetites and look for lower deductibles. But with a centralised solution, customers can ensure that local needs are met while balancing cost and a higher risk appetite at the group level."

EXPERT VIEW

BY ZURICH SINGAPORE CHIEF EXECUTIVE **JONATHAN RAKE** AND ZURICH GLOBAL HEAD OF INTERNATIONAL SALES AND DISTRIBUTION **PETRA RIGA**

BUILDING A HARMONISED ASIAN INSURANCE MARKET

The ASEAN Economic Community's bid to create a more harmonised regulatory environment across Southeast Asia will be a process of evolution and not revolution. But there is much to be gained from such a move.

Growing international investment in emerging markets has created a new generation of multinationals looking for comprehensive insurance programmes to cover all their global risk management and insurance requirements. This puts pressure on the insurance industry to develop international programmes that are capable of covering the full range of risks across different industry sectors in emerging markets.

But this isn't always an easy task. It is estimated that about 140 countries currently do not allow 'non-admitted business': insurance written by issuers that are not licensed in the country. This can create a significant barrier to running an international programme.

An international programme supported by a global insurer with a large geographic footprint should be able to ensure that policies are issued in a timely fashion, claims are paid and services are provided at a local level in all the countries where a multinational customer operates. Such programmes provide multinationals with more consistent coverage. They remove uncertainty about what is covered in insurance contracts and by offering economies of scale, they should prove more cost-effective.

As emerging markets mature, insurance rules inevitably change. Insurers need to stay ahead of local requirements so they can advise customers and react appropriately to developments. Efforts are being made to create globally acceptable cross-border covers that can cater for local difference in conditions (DIC) and difference in limits (DIL) insurance issues. However, this requires changes to international insurance standards, as well as altering multi-lateral trade agreements.

While there is still a long way to go, the ASEAN Economic Community (AEC) has taken the first step towards the creation of a harmonised approach to international insurance. AEC's goal of regional economic integration is centred around the following four main pillars:

- A single market and production base;
- A highly competitive economic region;
- A region of equitable economic development; and
- Integration into the global economy.

Within the first pillar – the creation of a single market and production base – significant progress has been made in the trade of goods. But from an insurance perspective, there is still some way to go and financial services is currently lagging behind other priority sectors.

> 'It is estimated that about 140 countries currently do not allow 'non-admitted business': insurance written by issuers that are not licensed in the country'
>
> **Jonathan Rake and Petra Riga, Zurich**

In October 2014, the ASEAN Insurance Council (AIC) organised its first ASEAN Insurance Summit. The need to better integrate insurance markets is taking on a greater urgency, according to the Singapore MAS deputy chairman and minister for trade and industry Lim Hng Kiang at the inaugural AIC Summit.

"As ASEAN economies develop, cities expand and populations prosper, we have more at stake: more at stake not just in each other's success, but also more at stake should things go wrong," he told delegates at the summit. "As we have witnessed in the past decade, our shared prosperity has become increasingly vulnerable to natural calamities and external shocks. Yet we have not correspondingly taken up better protection for the economic assets at risk."

Through discussions at the AIC Summit it was clear there are many challenges to overcome in the journey towards a more harmonised insurance market. This includes conflicting regulation standards, uneven regulation capability, barriers to cross border investment and differing Foreign Direct Investment requirements among others. But progress on these fronts should help create a more level playing field across the region.

In the future, a more consistent approach to regulation will make it possible to provide the same international insurance solutions across ASEAN, as opposed to disparate local solutions that differ from one country to the next. Insureds will benefit from a greater breadth of services and products and more tailored and sophisticated coverage, as is already the case in market such as Europe where such harmonisation already exists.

While there are many benefits to be gained by insureds and insurers – local, regional and international – the road to harmonisation is not an easy one. There are various stumbling blocks along the way, such as the actions of local regulators, which currently may not be facilitating progress towards AEC targets. Clearly some governments will feel the need to protect their local companies and be reluctant to open up their markets to competition, and this needs to be carefully managed.

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