



GLOBAL RISKS

BUSINESS LEADERS NEED TO PREPARE FOR THE
BIGGEST RISKS OVER THE NEXT DECADE – NOW

JOHN DRZIK

When executives think about risk, they often focus on sudden shocks, such as financial market crashes, pandemics, and political upheaval. But there are potentially even more important slow-moving threats that develop over time before emerging as full-blown crises – when it is too late to prevent them.

This is why, for the past nine years, our firm, together with the World Economic Forum (WEF) and other partners, has examined which risks pose the biggest threats to global economic development over the next decade in a report issued in conjunction with the annual WEF meeting in Davos, Switzerland. Based on a survey of more than 700 industry leaders and experts, our *Global Risks 2014* report analyzes 31 evolving and interconnected risks that cut across national boundaries, economies, technology, societies, and the environment. (See Exhibit 1.)

This year's research reveals that demographic and societal trends may increasingly shape the risk environment over our report's 10-year time horizon. Economic threats such as severe income disparity and fiscal crises, environmental risks, chronic unemployment, and technological threats rank among the top five risks that are the most likely and most impactful long-term dangers to countries and companies. (See Exhibit 2.)

EXHIBIT 1: TEN GLOBAL RISKS OF HIGHEST CONCERN IN 2014



Fiscal crises in key economies



Structurally high unemployment/underemployment



Water crises



Severe income disparity



Failure of climate change mitigation and adaptation



Greater incidence of extreme weather events



Global governance failure



Food crises



Failure of a major financial mechanism/institution



Profound political and social instability

Source: *Global Risks 2014, Ninth edition*

Note: From a list of 31 risks, survey respondents were asked to identify the five they are most concerned about

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SLOW-MOVING THREATS

In *Global Risks 2014*, we present three “risk cases.” One risk case, titled “Digital Disintegration,” explores how cyberspace could become severely compromised by the growing strength of attacks and dwindling levels of trust, at a huge cost to economies and societies. Another, called “Generation Lost?” offers insight into how high rates of youth unemployment risk stoking social unrest and squandering the human and economic potential of an entire generation. Today, more than half of young people in some developed markets are unemployed or underemployed.

But the key risk case from our perspective this year is titled, “Instabilities in an Increasingly Multipolar World.” It focuses on how today’s fractured geopolitical environment threatens to undermine our ability to deal with global issues. The world needs coordinated governance to counter the many complex risks that stretch across national boundaries. Unfortunately, a new world disorder is developing that could impede progress in industries critical to global economic development, such as financial services, health care, and energy.

Banks are exiting markets and repatriating trillions of dollars to escape new national regulatory regimes that are ring-fencing their capital. International pharmaceutical companies are struggling to take new technologies into different markets as governments apply pressure to lower pricing in their countries. At the same time, the shifting geopolitics surrounding energy supply is creating uncertainties among investors – when nearly \$27 trillion in investment is needed to respond to escalating global demand for electricity alone.

National self-interest is becoming the overriding priority as developed nations focus on finding solutions to their weak fiscal positions and emerging countries make greater efforts to meet the rising expectations of their growing middle class. As a result, multilateral institutions struggle to build consensus across countries, and the international community is unable to take concerted action on critical global challenges like climate change, Internet governance, and illicit trade.

In the near term, domestic pressures are likely to grow – leading to an even more insular focus. Millions of people have taken to the streets in the Ukraine, Argentina, Turkey, Egypt, and Brazil to protest against

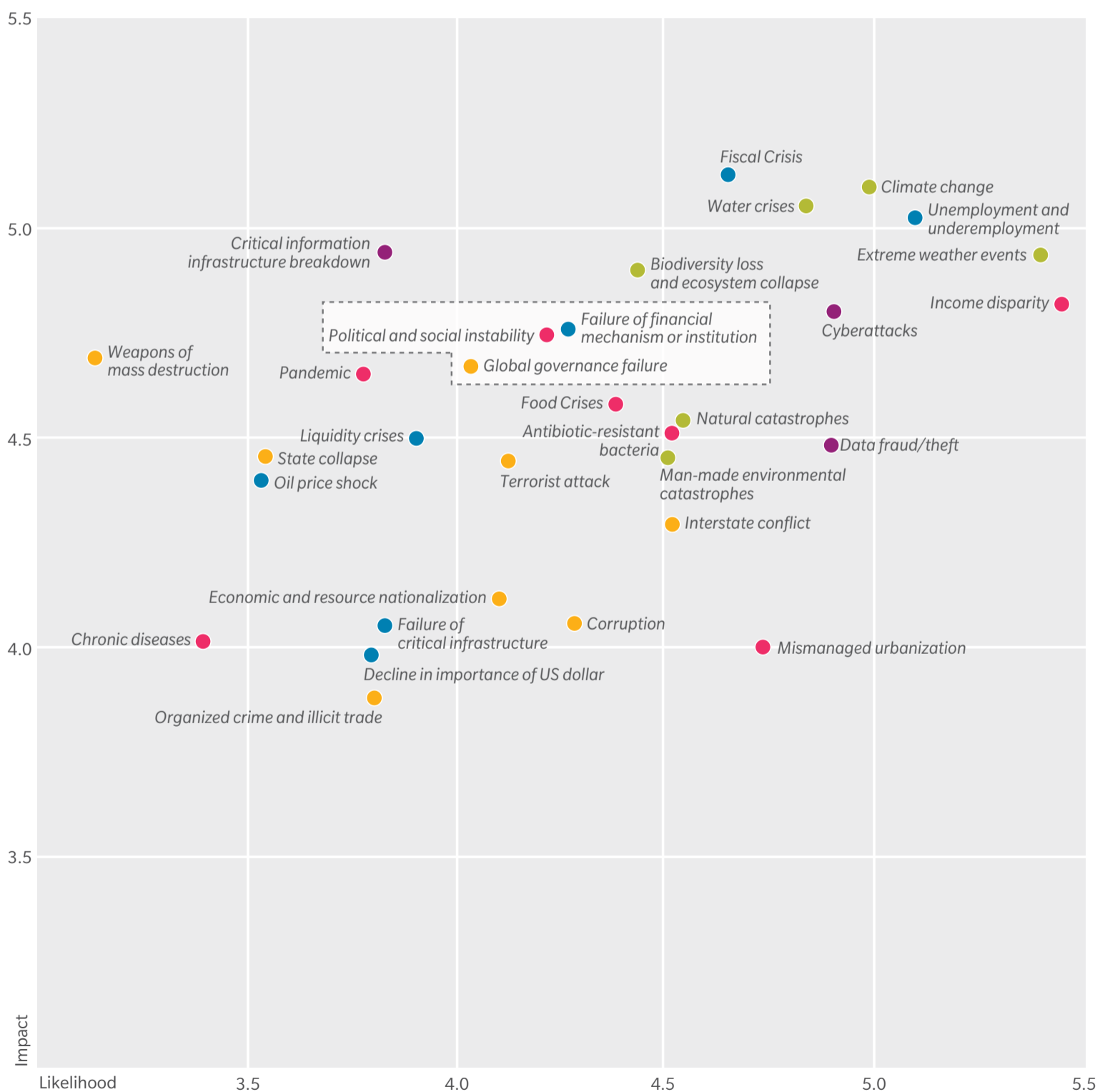
Today’s fractured geopolitical environment threatens to undermine our ability to deal with global issues

EXHIBIT 2: GLOBAL RISKS LANDSCAPE 2014

THE POTENTIAL IMPACT AND LIKELIHOOD OF GLOBAL RISKS OVER THE NEXT 10 YEARS

For the Global Risks 2014 report (published by the World Economic Forum in collaboration with a group of partner organizations, including Marsh & McLennan Companies), more than 700 leaders and decision makers from the World Economic Forum's global community were asked to select, out of a group of 31 global risks, the ones that will be of greatest concern over the next 10 years. These pages summarize the results.

Below lies the full gamut of risks. Note that respondents think that the cluster of risks – political and social instability, failure of financial mechanism or institution, and global governance failure – would have both great impact and are likely to occur.



Source: *Global Risks 2014*: Ninth edition, World Economic Forum and partners, including Marsh & McLennan Companies
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EXHIBIT 3: GLOBAL RISKS LANDSCAPE 2014 GLOBAL RISKS BY CATEGORY



Source: *Global Risks 2014*: Ninth edition, World Economic Forum and partners, including Marsh & McLennan Companies
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everything from their nation's leadership to a five-cent increase in bus fares. In this unstable geopolitical climate, interstate friction is likely to sharpen, and the global business landscape could be significantly altered.

CREATIVE PARTNERSHIPS

So what can companies do in such a fractured environment? We recommend following two parallel tracks. Business leaders should work with political leaders to mitigate emerging risks through multilateral institutions and networks. At the same time, they should adapt their strategies to capitalize on new opportunities created by the changing geopolitical outlook. This could mean forging new cross-border partnerships that span the interests of both the public and private sectors.

GOVERNMENTS

Governments and companies should take a page from the Global Alliance for Vaccines and Immunization (GAVI) coalition, which was formed by the Bill & Melinda Gates Foundation, nonprofit organizations, governments, and the pharmaceutical industry to immunize 250 million children and save 4 million lives globally by 2015. Creative partnerships could also halt rising medical costs if systematically applied toward developing solutions to such challenges as Alzheimer's and championing a global movement to promote low-cost health care models that reward health care providers based on their ability to maintain patient wellness rather than on the number of procedures they perform.

FINANCIAL SECTOR

In the financial sector, global banks should work with regulators across countries to overcome the current balkanization of domestic reforms, which is creating both cost and capital inefficiencies that work against long-term economic growth. New forms of public-private cooperation could also stimulate development. For example, we estimate that a

0.5%
The percentage annual uplift in GDP that Asia could experience by 2020 with a more integrated financial system

more coordinated and integrated Asian financial system could generate an incremental GDP uplift of more than 0.5 percent on an annualized basis by 2020 and transform the sector from a bank-dominated model to a more balanced structure with deeper and wider capital markets.

ENERGY SECTOR

Finally, in the energy sector, companies will need to consider new partnerships as more widely available hydrocarbon resources around the world introduce multiple geopolitical and economic uncertainties. The deep interconnection between geopolitics and business is already taking a new turn due to major shifts in both supply (such as shale gas discoveries in North America) and demand (in rapidly growing markets such as those in Asia). Looking ahead, national oil companies will expand their reach, using the political and financial backing of their home governments, and energy companies will need to consider new partnerships with them, as the involvement of national oil companies in the market escalates.

CONCLUSION

Rapidly evolving changes will lead to growth opportunities for some players, such as companies with sophisticated trading platforms that can acquire and reroute cargoes for commercial advantage. Interstate supply dependencies will also create heightened demand for energy efficiency in all countries – an area where joint ventures and other multi-stakeholder partnerships could be beneficial.

National retrenchment is more likely to increase global risks, rather than mitigate them. Succeeding in a fractured geopolitical environment will require flexibility, foresight, and fresh thinking about risk management. In the face of this emerging context, business and political leaders can improve the resilience of their companies and countries by diversifying their risk exposures and seeking out new partners. The agile and adaptable are most likely to thrive. But companies and countries need to prepare for the biggest risks over the next decade caused by a fractured geopolitical environment now.

John Drzik is the president of Global Risk and Specialties at Marsh. Marsh, like Oliver Wyman, is a subsidiary of Marsh & McLennan Companies, which contributed to the World Economic Forum's *Global Risks 2014* report.

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