

New Reality of Risk ® Transcript

The Changing Face of European Risk Management

Retailers and Consumer Brands

In our New Reality of Risk series Marsh and MMC experts, along with Marsh clients, share insights and experiences relating to topical risk issues of the day. This series of webcasts provides information and expert opinion on issues that could affect your business.

The current downturn in the global economy raises important questions about how organisations conduct their business – and particularly about how they assess and manage risk. This month's webcast looks at the findings of some new European risk management research that Marsh has undertaken with independent research agency Ipsos, focussing on risk priorities, strategy, management and solutions.

Over 700 organisations were interviewed, across 12 European countries and 7 industry sectors. Our findings will be published in a series of reports - one for each of the industry sectors we've looked at - and an eighth report that will capture the overview findings for the whole of the European region.

In this audio briefing, Adrian Donald, the European, Middle East and Africa Practice Leader for Retailers and Consumer Brands (RCB), will summarise some of our key findings in respect of the RCB industry.



Adrian, you talk to companies in the retail and consumer brands sector everyday. Can you provide your perspective on how these firms are managing in the current economic climate?

Certainly, thank you. Well clearly this is a diverse sector. It effectively covers the consumer supply chain, starting with the manufacturers of consumer branded goods at one end of the supply chain, through to the retailers who sell those goods at the other end of the supply chain. This is a sector that has been highly affected by the economic environment that we are now in. Many of these businesses have found it very, very challenging; many are under pressure in terms of profits and margins, and in terms of persuading customers to come and buy their goods.

I think we are seeing a varied response across the sector however. In some areas, for example where we have low cost, value brands or retailers, they are actually doing well, at least relatively in this environment, and they are gaining market share and they're expanding.

I think in other areas of the sector it is tougher. I think today, particularly if you look at the premium branded goods and the discretionary brands, we are seeing that they are having a very tough time; they are finding it very hard work and it's challenging. That's forcing these business to look at how

they manage their business, how they structure their business, and how they can drive costs out of their business. And that is forcing change - and with change comes, potentially, changing risks.

We are also seeing these businesses pressurised by their limited ability to access the credit and debt markets. They are finding pressure on things like payment terms, cash flow and working capital, and their bad debt exposure is increasing. All these things are forcing businesses to try and look at how they are running themselves and how they can drive cost out. That often means that they are looking to drive cost out of their supply chain and in that supply chain they are making changes; as they make changes they are driving potentially greater risks that they need to consider.

We are also seeing perhaps some early signs of more merger and acquisition type activity as various parts of the industry and the sector look to consolidate. All these things, all these changes, changes the risk dynamics for these businesses. And the most important thing, the headline message, is that these businesses need to look at the risk implications of what they are doing, just as they need to look at the cost implications.

With that as a backdrop, we interviewed over 100 senior risk managers, or people with responsibility for strategic decision making in the area of risk, within the retailer and consumer brand sector. Are you able to provide an overview of the main research findings and are they what you would have expected?

I think there are perhaps three main findings. Firstly, that risk management is higher up the corporate agenda; secondly, that risk appetite is decreasing for many companies; and thirdly, that credit risks are high, if not top of everyone's agenda. If we look at each of those three in a little more detail:

As far as risk management is considered, perhaps it is no surprise that it is moving up the corporate agenda – people are becoming more aware of the risks that their business is facing. 67% of organisations that responded to our survey say that the downturn has prompted them to review their approach to risk. We are seeing that in our business (insurance and risk advisory services) in terms of we are getting more questions from our clients around things like risk optimisation and how do they make effective use of both their balance sheet to absorb risk and their insurance programme to transfer risk.

As far as risk appetite is concerned, risk appetite is decreasing for twice as many companies, 36% of those who were surveyed, as for those that it is increasing. Perhaps we are seeing those with stronger balance sheets willing to take more risk where they see opportunities in this environment. Those with weaker balance sheets, less able to take risk (or less willing to take risk), are therefore seeking more certainty and transferring risks where they can – some of these risks can be

transferred to the insurance market.

As far as credit risk is concerned, I think that is something that has been uniformly, ... top of the list for just about every industry sector that has been surveyed; it is no surprise that for retailers and consumer brand companies it is also top of the list. I think some of these credit risks come in different shapes – companies are concerned about their access to lines of credit for working capital; they are concerned about customer credit - either to pay or to fund purchases; and counterparty risk seems to be a recurring theme that everybody is particularly focussed on at the moment.

These pressures make cash flow particularly important to these types of businesses. And again that's a dynamic that needs to be considered when looking at how you retain risk, and from an insurance perspective, how you transfer it. So making sure that your programmes are geared to protecting your profit line is of increasing importance to businesses these days.

Now we researched in twelve countries across Western and Northern Europe. Are you seeing a consistency in the responses or are they less uniform - and if they are why do you think that might be?

Well I think that the response is reasonably consistent across Europe but perhaps we are seeing some differences in one or two countries. There are some interesting dynamics between businesses in France and Germany for example – in France we saw that 83% of companies think that risk is of far greater importance today [at the most senior levels of their organisation] than it was some time ago; in Germany that same number is only 44% - it is still a very, very significant number but it is quite a bit less [than France] and we can speculate as to why that might be, for example Germany has a much bigger manufacturing industry and it may be that they have not yet seen the impact that some countries have, maybe it is a lagging indicator.

Equally we have seen the boardroom view of risk in Germany - 52% of companies at board level view risk as unchanged, whereas in France that is only 21%, suggesting that France's board awareness seems to be greater to the potential changing of risk.

So how would you say the retail and consumer brands sector has changed its behaviour in response to risk in light of this current economic environment?

This is a fairly broad-based sector so it is not surprising if there are some differences in the way businesses across the sector have responded or changed their behaviour - it depends a little bit on the circumstances that these companies find themselves in.

We are seeing a few things that are worth noting. Reputational risk, while it is still important, seems to have taken a slight back seat compared with things like credit and supply chain risks which are obviously front-of-mind right for some of these companies right now.

I think we are also seeing differences between thriving or stronger companies and the companies that are being hit harder by the economic environment. So those stronger companies have probably not changed their approach to risk significantly – they have not been driven to make the same sort of changes as companies who are struggling have been forced to do. Those weaker companies are potentially less tolerant these days to volatility, to the impact of claims, and generally are looking to build as much certainty into their business model as they can. We are seeing, both through this survey and through our conversations with companies in this sector, that businesses in that position are increasingly looking to insure more, in the sense that they want lower deductibles, than companies who perhaps are more strongly placed.

We have seen that two thirds of companies are reviewing their approach to risk and a similar number say that risk management is more important today than it was, so that's a significant portion of the businesses surveyed. Compare that with only a third that have a decreased appetite for risk at board level...

What advice can you give these companies, retailers and consumer brands, that could help them address their current priority risk areas – you talked about credit risk as an issue and supply chain risk was highlighted by the survey – and to do this while staying in budget?

I think it is going to be a challenge for businesses. It clearly is a challenging environment in which they are operating in and this is just one more thing that they need to wrestle with. I think the most important thing for businesses particularly in this sector is being risk aware – be aware of the changes that are going on, be aware of the changes that you are making in your business and think about their implications from a risk perspective.

Businesses are hugely incentivised at the moment to drive cost out and that involves making all sorts of changes – businesses are not always so good at understanding the consequences of doing so and understanding, managing and mitigating the risks that they might be absorbing in making a change, for example in the supply chain.

You need to make sure those changes are understood, that there is strong risk management culture that manages the risks - the impact of those changes on things like business continuity plans and crisis management, for example- that these are being catered for and being kept up-to-date. And as

those change and as the financial position of the business develops, things like understanding the insurance requirements, your appetite for risk retention, these are all factored in to the thinking of the business. In doing so I think you need to understand where insurance is actually adding value. Where cost is important, insurance is a spend outside of the business and you need to make sure that the spend is of value to the business – so, where does it provide value, where is it most important, are you getting the best 'bang for your buck'?

There are number of other things that we can do to help businesses do that. Marsh is in the fortunate position of having a significant portfolio of clients across this sector. That gives us some great insights into what these businesses are doing and how they are positioned. We can develop, and we have got some fantastic benchmarking data, and we can use that to help businesses understand, relative to their peer group, whether they are doing well or whether there are areas where they can potentially do better and thereby reduce costs or have greater certainty for their shareholders.

When we were doing our survey, one of things the surveyed companies told us was that as far as benchmarking was concerned, over 81% of respondents felt that benchmarking was an important measure for them in understanding how they are relative to their peer group. Equally, 79% thought that case study material was of value – well, Marsh is an organisation whose representation in this sector is ideally placed to help companies do exactly that.

Other areas I think companies need to prioritise is to be proactive – make sure that you are understanding the risks in your business, that you are testing your insurance programmes to ensure that they are cost effective, and that you are using tools like benchmarking data to ensure that you are positioning both your risk management and your risk financing and insurance arrangements as effectively as you can. Those who do so I think are best placed to capitalise on, to make themselves more competitive in the current environment. The more you can save in this area, the more you can manage your costs, the better you can manage your claims, the more you can reduce your cost basis – that's just helping the business be more profitable and be more effective.

Adrian Donald, thank you very much.

A pleasure, thank you.

[END]

About Marsh's Power and Utilities Industry Practice

Brokerage excellence, analytical rigor, deep intellectual capital, and seamless access to our global network

The Marsh EMEA Retailers & Consumer Brands (RCB) Practice is led by Adrian Donald, formally Director of Risk Financing at Diageo plc, and is dedicated to providing services and solutions to clients via our global network of Marsh experts and risk specialists.

We foster the sharing of ideas and best practice throughout our Practice, across Marsh and beyond, allowing us to provide seamless and expert advice in support of any client's strategic and operational plans.

Our unique understanding of industry issues and risks, coupled with the Marsh insurance expertise and consultative approach, ensures we provide custom solutions for the full spectrum of risks faced by companies in this fast evolving industry.

Our risk management leadership in the industry is demonstrated by the quality of the clients we serve and our client base includes food and beverage manufacturers and distributors, consumer brand companies, grocery retailers, general retailers, and on-line and catalogue retailers of all sizes.

For further information, please contact your local Marsh office or visit our web site at: www.marsh.co.uk or www.marsh.com.

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