CNA / HARDY

Taking the pulse of global business

Global Risk and Confidence Survey

November '18

Contents

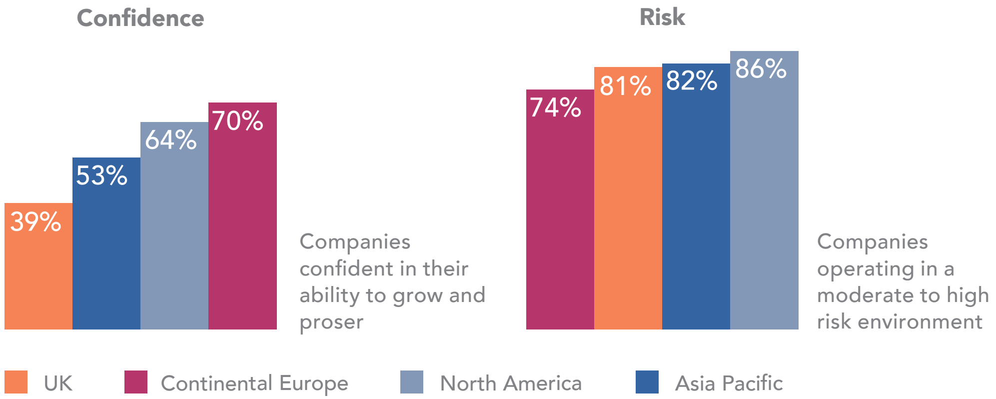
Risk is global, confidence is local

Risk is global, but confidence is local. That is the key finding of our fourth biannual business Risk and Confidence survey, the first to be conducted on a global basis.

Although confidence levels vary significantly between regions around the world, with Asia Pacific and the UK in particular looking extremely cautious compared to Continental Europe and North America, the consensus in terms of the top risks is striking.

Globally, 82% of business leaders believe that they operate in a moderate to high risk environment. Over a fifth (22%) cite economic risk as their top concern followed by cyber risk, cited by 19% of leaders.

Global risk and confidence



It's the economy

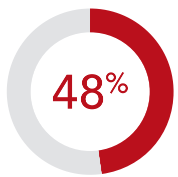
On the face of it, worries over economic risk are surprising. In July this year, the World Economic Forum predicted global growth will hold steady at around 3.9% in 2018 and 2019, reassuringly in line with earlier forecasts[1].

But look a little further ahead, and there are concerns over the sustainability of asset prices, high levels of indebtedness, particularly in China; and continuing strains in the global financial system. In October 2018, mounting tensions between the US and its trading partners saw the International Monetary Fund (IMF) cut global growth forecasts to 3.7%[2].

The IMF has highlighted the potential risks posed by the build-up of debt in the G20. In 2016[3], debt[4] in the non-financial sector hit US$135tr. Meanwhile, corporate debt also soared. According to S&P Global, 162 corporate defaults worldwide occurred in 2016 and debt-to-equity ratios almost doubled on 2010 levels. We need only think of recent significant insolvencies, Carillion in the UK, Toys R Us in the US, to see how the trend is developing.

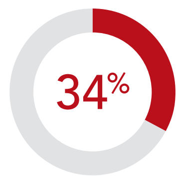
Politics and economics are close bedfellows and business leaders are clearly rattled by the threat to trade growth. Continued expansion depends on robust global economic growth and governments pursuing appropriate monetary, fiscal and especially trade policies. It's clear that escalating trade tensions are affecting business confidence and investment decisions, as are concerns around political events such as Brexit. Just under half of businesses (48%) think that Brexit will have a moderate or heavy impact and just over a third (34%) say trade wars are hitting growth plans and impacting business strategy.

Brexit concerns



North American and Asia Pacific businesses that believe Brexit will have an impact on business

Trade war concerns



Global businesses that believe trade wars are impacting business

[1] https://bit.ly/2NCAG0g [2] https://cnb.cx/2y7umbW [3] the latest year for which data is available [4] government and household debt

Politics is becoming more protectionist

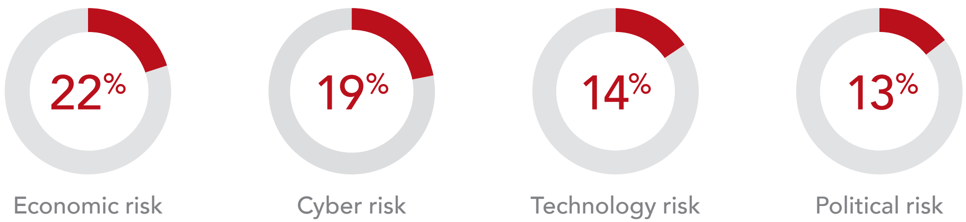
Confidence levels are closely linked to these concerns. In North America, nearly two thirds (64%) of business leaders are confident in the ability of their business to grow and prosper. That proportion falls to 60% across Mainland Europe (where Continental Europe's very high confidence levels are offset by the poor UK showing) and to only just over half (53%) in Asia Pacific where the impact of trade wars would cut deepest. In the UK, where companies are beset by Brexit uncertainty and its political and economic impact, only 39% of business leaders are confident.

In these partisan times, where globalism is falling out of fashion, trade wars dominate headlines and old alliances are increasingly called into question, a large question mark hangs over the ability of political leaders to come together should the need arise once more to restore order to an over-loaded global financial system.

Former UK Prime Minister Gordon Brown warned we are in danger of sleepwalking into a future crisis and that the cooperation seen in 2008 would not be possible in a post-2018 crisis[5]. This kind of sentiment is echoed by commentators all round the world. David Brown, CEO, New View Economics, writing in the South China Post commented recently: "The next time the crisis hits, the supranational agencies will lack the punch to make a difference … The architects of the 2008 bailout are long gone."[6]

No wonder our survey shows economic risk top of the heap globally, with political risk in fourth position. Unsurprisingly, almost half (44%) of leaders globally think economic risk will increase in the next six months and 42% that political risk will increase.

Political, economic and cyber risk continue to dominate



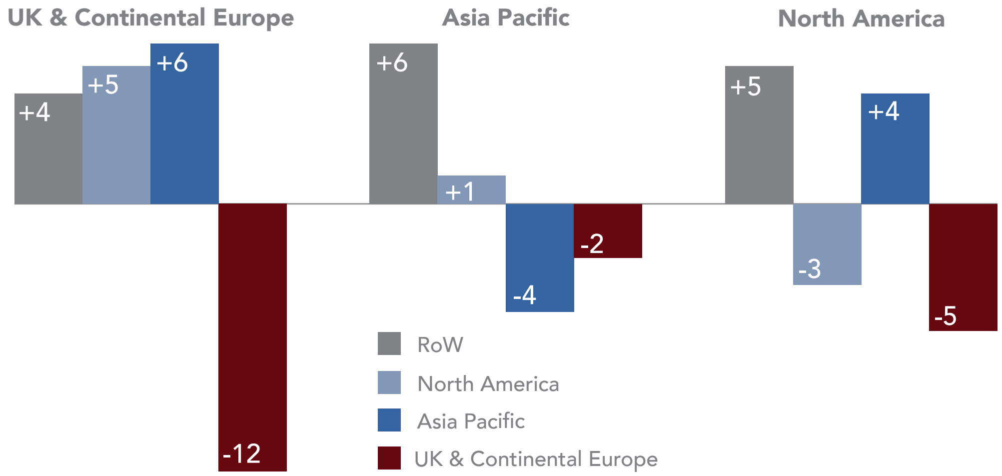
Top risk concerns of global business leaders in Nov '18

Business is more global

As national policy becomes ever more protectionist, so the potential for conflict with the business agenda increases.

Businesses worldwide are focused on growth which means sourcing more broadly, trading more ambitiously and expanding into foreign markets. Our survey shows that although companies invest primarily in their local market, change is underway. Every single region we surveyed showed declining domestic investment and that overall, investment in the rest of the world was set to double. Executing a global strategy is much harder against political headwinds.

Domestic investment declines



Percentage point changes Nov '18 – May '19

Businesses are embracing technology to drive expansion. But the rise of protectionism in politics cuts right across the business agenda and risks de-railing the very organisations it's trying to support.
Rhonda Buege, Head of Specialty, CNA Hardy

[5] https://bit.ly/2x616lc [6] https://bit.ly/2yT114p

Technology: saint or sinner?

Often expansion is facilitated by technology, which offers access to new markets literally at the touch of a button. On the plus side, technology does everything businesses could ask for: enabling more efficient operating, improving customer engagement – even delivering step changes in performance. For example, artificial intelligence (AI) is set to transform the speed and accuracy of everything from medical diagnosis to detecting and managing crime.

But it's a myth that technology inevitably makes companies more nimble and flexible. Robot-enhanced production lines augment very particular human skillsets. Neither the technology nor the people can be shifted easily to accommodate a supply chain that no longer delivers when, for example, Brexit moves the regulatory or fiscal goalposts; or trade wars make imports of essential materials un-economic.

Similarly, if those highly bespoke and complex systems are disabled by ransomware or hacking, then the activity of the company can grind instantly to a halt as we saw with attacks last year on Maersk, Merck and Mondelez.

As this realisation dawns, technology has moved from being the 'nearly risk' that businesses worried about only in six months' time, to a global top three, with 14% of leaders globally ranking this their top risk in November '18 and 37% suggesting the risk will increase in six months' time.

Technology risk perception shifting

Companies globally ranking technology as the top risk today and believing it is set to increase in six months

Our results show that technology is the critical area of spend for companies seeking to drive efficiency, profitability, innovation and closer customer interaction. Three quarters (74%) of business leaders we spoke to globally are prioritising technology spend in November '18. Indeed, in the digital age, it is technology and research and development (R&D) spend where businesses are choosing to concentrate their fire-power, rather than on technology and talent as was the pattern two years ago.

Investment priorities

Businesses' investment priorities Nov '18

Although technology is essential to fuel the global expansion on which business growth depends, in many ways it is also the soft under-belly of the 4th industrial revolution.

Technology companies feel the strain

Anxiety about the role of technology is also reflected within the sector's leadership. Well over half (59%) are confident about the future, but almost a fifth (17%) are cautious about the weight of expectation and the risks that they face.

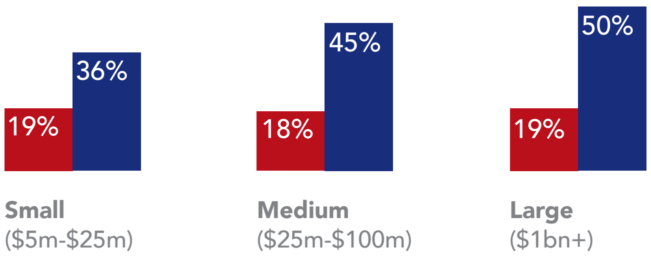
> There is no turning back the tide. The clue is in the name: we are well into the 4th industrial revolution and no enlightened business person would argue that previous revolutions have not delivered huge rewards. But progress is not without cost. Businesses' growing dependence on technology is both a strength and a weakness. It is critical companies build appropriate resilience into business modifications.
>
> Stuart Kenyon, AVP, Risk Control, CNA Hardy

Cyber threat rises as tech dependence increases

In our last survey undertaken in May '18, cyber risk trumped economic and political risk for the first time in the UK and Continental Europe. Now it is the second most concerning risk globally and in six months' time it moves into the top slot.

While received wisdom suggests it is the smaller and mid-size corporates that are least prepared for cyber threats, our data shows that it is the largest companies that are most concerned, despite having more resources and insight to deal with the issue.

Larger businesses most concerned by rising cyber threat



Companies ranking cyber as a top risk Nov '18

Companies predicting cyber risk will increase in six months' time

There is a chronic shortage of cyber security skills and this will continue as new technology like the Internet of Things (IoT) amplifies creating more insecurities. This means the gap between risk and mitigation, exposure and cover will continue to grow. Insurance has a key role to play in helping companies to get that risk management right, both in prevention and incident response.

David Legassick, Head of Technology and Cyber, CNA Hardy

Do changing business models mean new risk focus required?

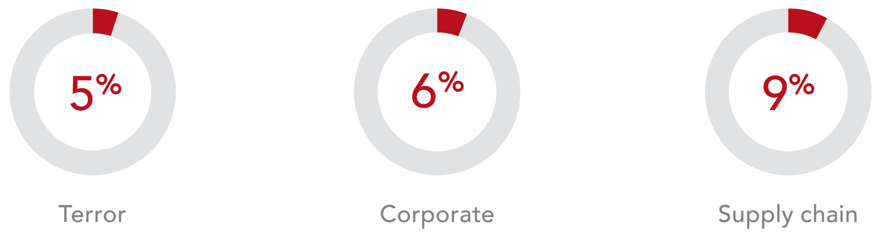
As the business model changes with the adoption of new technology, and global operating models shift to accommodate investment in new growth markets, it is clear that risks are becoming increasingly interconnected.

Globally, only 13% of business leaders rank regulatory and compliance issues as their top risk and fewer than one in ten (9%) cite supply chain as their top concern. Fewer still (6%) are concerned by corporate risk – the exposure to fraud, corruption, poor governance or cultural issues which can do so much reputational damage when management controls are tested in new markets.

Politics shapes economics, which in turn drives supply chain expansion. The more complex the supply chain, the greater the exposure to regulatory, compliance and reputational risks. Broader global footprints require technology investment which creates cyber, terror and even climate change exposures. Risk in the 21st century is increasingly interconnected.

Kathleen Ellis, Senior Vice President, International Solutions, CNA

Low ranking global risks



Lowest ranking global risk concerns Nov '18

Are companies and insurers ready for interconnected risk?

As we look back over the two years of data collected for the Risk & Confidence reports, it is clear that risk is becoming ever more global, more interconnected and more complex. This creates challenges for the insurance industry and for business generally which can only be addressed at the strategic level.

In our view there are three critical priorities.

Leadership
The first is leadership. Not only do companies need the traditional financial and legal leadership skills on the board, they also need a broader, more diverse range of individuals who can help them appreciate reputation/brand risk, supply chain, technology, cyber and human risk. Future risks are intangible, more numerous, more complex and likely to develop faster than in the past.

Culture
The second priority is culture. Organisations need to think harder about culture and specifically about embedding a more proactive attitude to loss and risk prevention. Tellingly, large losses today are caused by the same drivers that created large losses twenty years ago – fire and flood. If businesses are still struggling to embed preventative measures to ensure all employees are effectively and willingly managing traditional, physical risks, they will struggle with getting to grips with more complex, fast moving interconnected risks. It is for this reason the culture of risk is so important and that it is fed through the business from the top.

Strategy
The third priority is strategy. Stronger leadership teams operating within a more proactive risk culture will be better placed to make the investments in people, processes, technology and markets which will enable growth.

The insurance industry is getting much better at understanding and responding to intangible and interconnected risk and about communicating what needs to change. But there is always more to be done. Risk management is increasingly about service and support as much as balance sheet risk transfer. For that to work effectively there will need to be more and better dialogue.

Companies cannot think about risks in silos and neither can the insurance industry. We all have to adapt our thinking to the new realities of global business.

Insurance is not a panacea, it's a partnership.

Dave Brosnan
CEO, CNA Hardy

Regional breakdown

UK and Continental Europe

Brexit divides sentiment. Globally, Continental Europe is the most confident region in the world, while UK business confidence is the lowest.

Technology and R&D investments are set to remain the top priority to support growth, sustaining concerns that cyber and technology risk remain the key threats to businesses' successful navigation of the 4th industrial revolution.

Europe invests, UK stagnates. Continental European businesses are much more likely to be proceeding with spending on business fundamentals than UK businesses and by a significant margin.

Economic risk dominates the UK. While both regions see economic risk in their top three risks, in the UK it is a clear leader, while in Continental Europe the focus is primarily on cyber risk.

Brexit is about to cause **a significant rise in corporate risk,** bringing regulatory uncertainty and supply chain disruption.

It is also having a variable impact across industries; in some sectors Continental European business leaders are more than twice as confident as their UK counterparts.

North America

North American business leaders are bullish, with the economy cited by a sizeable proportion of business leaders as the key to their sentiment.

At the same time they are very aware of the threats that business is facing – **the number of executives who believe they are operating in a moderate to high risk environment is the highest worldwide.**

Investment focus suggests the 4th industrial revolution is taking hold. The hiring of staff is not a priority. Instead, business leaders are looking towards automation and augmentation.

Technology seen as an opportunity and a concern. While North American companies are investing in technology, they are concerned about associated risks, such as IT system failure and disruption from new tech-enabled competitors or start-ups.

Boardroom risks rank low. Corporate, supply chain and regulatory risks are given low priority. Instead, key concerns are economic, cyber and technology risks, more global in nature and harder to mitigate.

The sophisticated sectors with foundations rooted in intellectual property and highly-skilled talent including financial services, life science and professional services **are the most confident** with technology following close behind. Meanwhile, more labour-intensive industries such as construction and transportation & logistics are among the most cautious.

Confidence and risk

64%

Companies confident in their ability to grow and prosper

86%

Companies operating in a moderate to high risk environment

Business fundamentals

Cutting back		Proceeding	
Hiring temp staff	15%	74%	Investing in Tech
		73%	Investing in R&D

Top 3 risks

Economic 21%

Cyber 20%

Tech 16%

Most confident sectors

Financial services 79%

Life science 74%

Professional services 68%

Asia Pacific

In Asia Pacific, short-term risks are currently impacting business sentiment. Despite strong prospects for the economy, executives here display the lowest levels of confidence of any region, save the UK.

Business leaders are coming to terms with operating in a challenging landscape. Unlike in western markets, Asian businesses are struggling to take risks in their stride. A significant majority think that they are operating in a moderate to high risk environment.

Growth remains a priority, despite these risks. Investment – in both technology and R&D – is a key area of focus, along with growing topline sales.

Economic risk is top of mind, reflecting concerns about the impact of trade war disruptions and protectionism on future growth.

Cyber risk is moving up the agenda. It is projected to take top spot in six months' time with executives' awareness heightened by a recent spate of cyber attacks and a shifting regulatory environment.

Fintech business leaders are most confident, with sentiment buoyed by government focus on technology and on the development of Singapore in particular as a key financial services hub.

Confidence and risk

53%

Companies confident in their ability to grow and prosper

82%

Companies operating in a moderate to high risk environment

Business fundamentals

Cutting back		Proceeding	
Hiring temp staff	13%	76%	Investing in Tech
		69%	Investing in R&D

Top 3 risks

Economic 26%

Cyber 19%

Political 14%

Most confident sectors

Fintech 69%

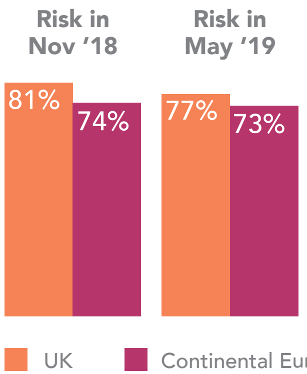
Life science 59%

Professional services 59%

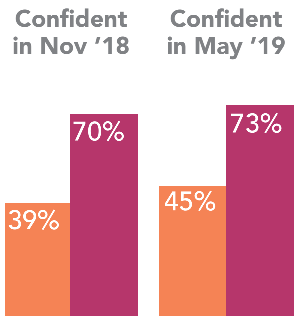
Europe has a swagger on

At the regional level, Europe (including the UK) is second only to North America in terms of confidence, while risk perception – although relatively high at 74% – is lower than in any other territory globally. Remove UK leaders' views from the equation, however, and Continental Europe moves head and shoulders above all other regions globally in terms of high levels of executive confidence and low risk perception. Our research suggests the primary reasons for this are two-fold: Continental Europe has far less to lose than the UK from the impending separation, and it is set to become the export market of choice for North American and Asia Pacific based firms.

Confidence and risk for UK and Continental Europe



Companies operating in a moderate to high risk environment



Companies confident in their ability to grow and proser

Economic expansion, currency strength, wage growth, and investment attractiveness are just some of the factors underpinning Continental European executives' high confidence levels, despite recent stock market volatility. Significantly, our research shows that Continental Europe is the region that North American and Asian businesses are most likely to be targeting for future growth outside their domestic market, and also the region least concerned by trade wars – only just over a quarter (27%) of firms consider these may have even a moderate impact.

But while leaders of businesses in Continental Europe are upbeat about their business prospects – with 70% describing themselves as confident - the polar opposite is true in the UK. Here, confidence has declined significantly since the Brexit referendum, almost halving from 70% in May '17 down to 39% in November '18.

At its very widest point, the Channel between Europe and the UK is only 240km, but the gulf in confidence between the two markets is enormous. Continental European businesses have the luxury of balancing cyber, technology and the economy as their top concerns. In the UK, it's economic risk that is dominating the C-suite risk agenda and sucking up all the oxygen in the boardroom.

Stuart Middleton, CEO, CNA Hardy Europe

As we look ahead six months and uncertainty persists about what Brexit means for business, that gulf in confidence barely changes. Some 73% of leaders in Continental Europe expect to be confident about the ability of their business to grow and prosper by May next year; but only 45% of UK leaders feel equally confident and almost a third (32%) are actively cautious, a trend which became established in May of this year as realisation dawned that Brexit uncertainty would persist for some time.

Uncertainty around Brexit is having a much bigger impact on UK businesses than those in Continental Europe. On average, UK businesses are more than twice as likely to be decreasing their investment on business fundamentals, such as investment in R&D and growing topline sales.

Cold wind of economic reality blows strongest over UK

Economic risk dominates the UK picture – seven percentage points clear of the next two concerns – political and cyber risk, both on 16%. In Continental Europe by contrast, there is only a single percentage point between the top three risks.

Over the past ten years, exports of goods and services to the EU have accounted for between 12-15% of the value in the UK economy[7]. Over the same period, exports from the EU to the UK have accounted for just 3-4% of the Continental European economy. While it is true that some industries in parts of Europe, for example car manufacturing in Germany, are highly dependent on the UK market, the statistics could not be clearer. Given that the EU-UK trading relationship is between three and four times more valuable to UK companies than Continental European businesses, it is not surprising that business leaders in the UK are much more likely than their European counterparts to consider their current situation to be high-risk.

Uncertainty paralysing decision-making

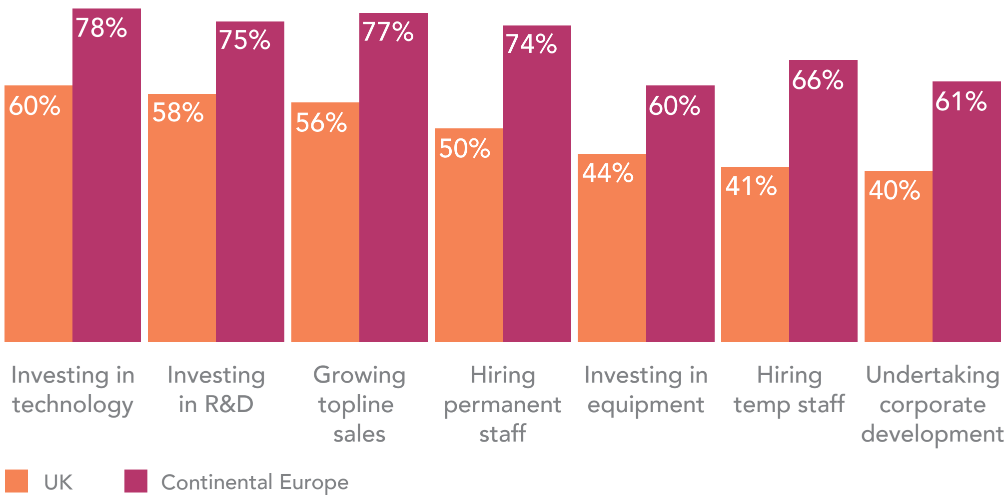
It's not just the economic impact of Brexit which is alarming UK business leaders however. They also expressed concern at the distraction it is causing in terms of managing the UK economy and the uncertainty it is creating in terms of clarity over transition arrangements and future state regulations. Companies are cautious about committing to investments until they know what will be expected of them in the new world order.

Continental Europe invests, UK stagnates

The imbalance in confidence and risk between Continental Europe and the UK is borne out in terms of corporate investment in fundamentals. In general, Continental European businesses are much more likely to be proceeding with spending on business fundamentals than UK businesses in every single area. The scale of difference in some areas is stark – a gap of 21 percentage points in terms of corporate development (joint ventures and M&A), 18 percentage points in terms of technology investments and 24 percentage points in terms of hiring permanent staff.

UK investment falls behind

Nov '18



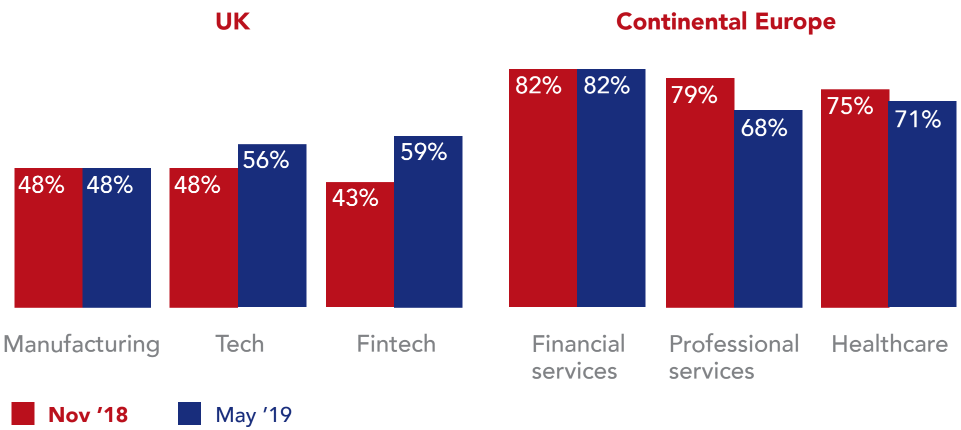
[7]https://bit.ly/299PKO6

Sector confidence levels divided by Brexit

The tale of the divided continent is also evidenced in terms of varying levels of confidence overall and varying sector spending priorities.

In Continental Europe, financial services, professional services and healthcare are topping the confidence league. Healthcare in particular sees significant opportunities post-Brexit and is planning to invest proportionately more in technology, talent and plant and equipment as a consequence. Professional services, fintech, technology and life science are also big post-Brexit investors.

Businesses confident in their ability to grow and prosper



With the exception of technology, these of course are the very sectors in the UK that stand to lose most from Brexit. Life science in particular will be the poorer if it can no longer participate in pan-European R&D programmes and The Francis Crick Institute, the UK's biggest biomedical research lab, warned in October '18 that a hard or 'no deal' Brexit could 'cripple' UK science[8]. It is unsurprising then that life science business leaders are the least optimistic of all with confidence at just 22%. A high proportion of professional services businesses also forecast a sharp drop off in investment, placing the sector as the second least confident at 30%.

The UK's transportation & logistics results are also striking. Although uncertainty hangs over this sector perhaps more than any other, it is in the middle tier of industries in terms of confidence. Our results show, however, that it will be the biggest investor in technology once the deal is done. Although the new customs arrangements are yet to be clarified, there is little doubt that the solution to maintaining frictionless borders will be delivered via technology. The priorities of Continental European transport and logistics businesses by contrast are little changed by Brexit.

With Brexit as the backdrop, Continental European businesses are the most confident in the world, according to our results, in some sectors business leaders are more than twice as confident as their UK counterparts.

> We are planning for Brexit and are optimistic about the outcome, but we cannot move forward and commit to investments until we know how the new system will work. The changes need to be well signalled because we cannot adapt overnight and the processes cannot be built until we know how VAT and duties will be handled for example, or how cargoes might be profiled. Governments appear not to understand the time required to re-engineer the technical solutions for these challenges or the challenges of implementation. The regulatory and compliance risks are significant and there will need to be scope for forgiveness as adjustments are made.
>
> Mervyn Griffiths, Director, Strategic Shipping

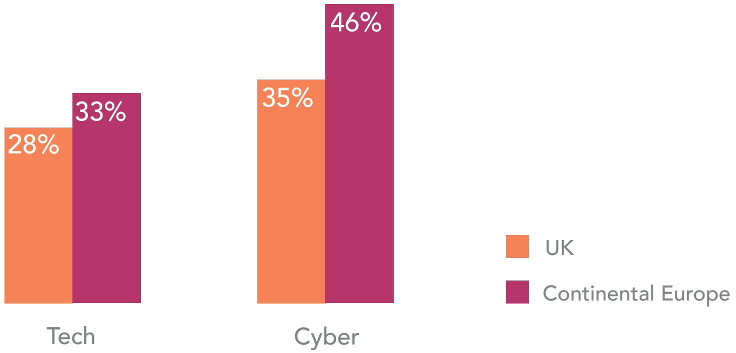
[8]https://bit.ly/2PV0Mx9

Unity over cyber and technology risk

In May this year, compliance and regulation was the second most concerning risk to business leaders in both Continental Europe and the UK. The introduction of the General Data Protection Regulation (GDPR), the febrile environment around #MeToo and gender pay gap reporting were something of a perfect storm. But although businesses predicted this risk would stay high on the agenda, it dips in November '18, rising to the fore once more in six months' time as Brexit threatens regulatory disruption. Instead, the focus in the UK and Continental Europe has remained on cyber, but with a striking pivot in both regions to technology risk.

> Not-Petya moved the conversation on from data security to business interruption. It disrupted the business models of many public companies, causing massive business interruption claims. In many ways it's concerning that companies are not more attuned to protection of intangible assets like reputation and brand that are so vulnerable to this kind of attack.
>
> Ailsa King, Chief Client Officer, Marsh

Looking forward, cyber and technology risk remain a concern



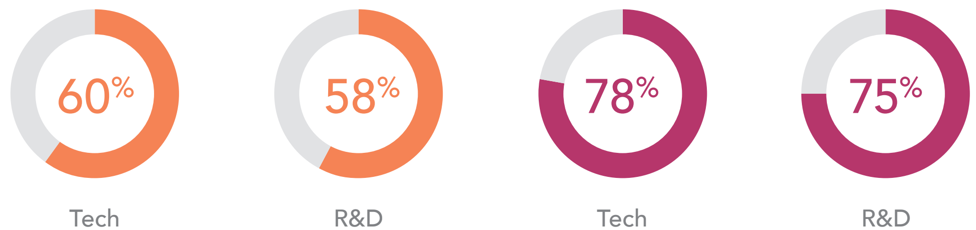
Companies expecting technology and cyber risk to increase by May '19

Ransomware attacks hit Europe particularly hard, with the not-Petya virus causing significant business interruption losses. A trio of big companies: Maersk, Merck and Mondelez reportedly found their operations locked down by the virus and the severity and duration of the impact on a group of big, well run, global businesses shocked the business community and heightened awareness of the scale of the threat we face. This and the focus on privacy risks following the introduction of the GDPR in May '18 have turned cyber into something of a perfect storm.

Businesses and their insurers have worried for some time now about the growing interconnectivity of risk – how a cyber attack can paralyse a manufacturing plant, shut down a global supply chain, put revenues of multiple businesses at risk and undermine the reputation of many leadership teams and the brands they represent. Our data demonstrates how companies are increasingly prioritising investment in technology which can only exacerbate this trend.

Indeed, the emergence of technology into the top tier of risk in November '18 is a global phenomenon across our data set, reflecting a range of concerns including leaders' anxiety around making the right decision, future proofing the business against agile disruptors, augmenting the skillsets within the workforce and protecting high value digital assets against cyber threats and the potential for brand value destruction. Rising awareness of the risk goes hand in hand with businesses' growing preference for technology and R&D investment as we move fair and square into the 4th industrial revolution.

UK and Continental Europe investment priorities



Companies investing in this area in November '18

UK   Continental Europe

Boardroom risk set to explode both sides of the Channel

It is inevitable that Brexit will cause a significant rise in regulatory uncertainty, supply chain disruption and, as a consequence, corporate risk for Continental European and UK-based businesses. When management systems and cultures are placed under stress by such a significant external shock, the risk profile inevitably will rise.

As we look ahead six months to May '19, businesses in Europe and the UK as a whole foresee an explosion in boardroom risk. Almost a quarter believe corporate and supply chain risk will increase and over a third believe regulatory and compliance risks will increase. In fact, looking ahead there is more concern about regulatory and compliance risks than economic.

Which risks are set to increase the most?

Companies' risk forecast for May '19

These figures are encouraging, in that they suggest businesses will turn their attention to boardroom risks in the next six months. However, the fact remains that with the occasional exception of regulatory and compliance risk, businesses rarely focus on these risks in real time. Maybe the UK's exit from the EU in March '19 will be the point at which boardroom risk crystallises on the C-suite risk agenda.

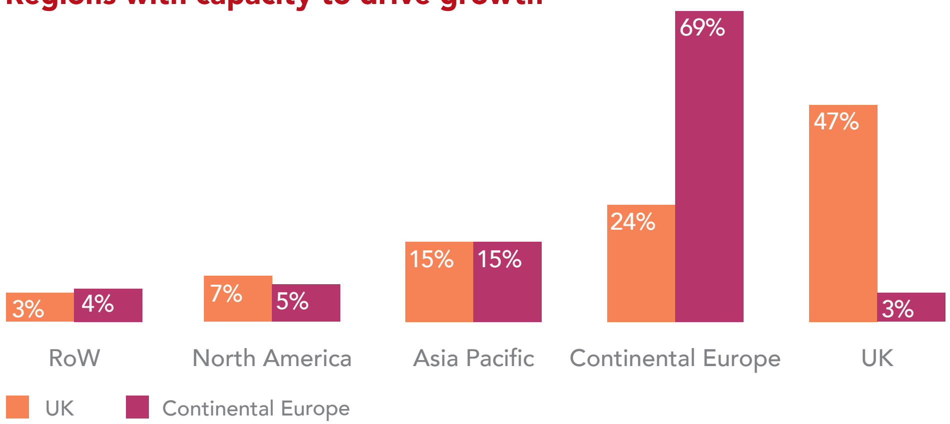
> Increasing risk is never welcome, but we are pleased to see that management teams on both sides of the Channel are alive to the likely threats that Brexit will entail for the Boardroom. Every control system in the business will be impacted by new compliance challenges and significant adjustments to the supply chain will be unavoidable. Brexit will be a real test of corporate confidence and culture.
>
> Dave Brosnan, CEO, CNA Hardy

Growth – but not from each other

No matter how the uncertainty around Brexit resolves, the search for growth must continue. Our report six months ago noted that business leaders in the UK and Continental Europe were set to turn their backs on each other and our findings six months on confirm they have made good on these intentions.

While both have equal expectations of small amounts of growth in Asia, North America and the rest of the world; European corporates are seeing growth in Europe, while UK corporates are looking for growth in the UK.

Regions with capacity to drive growth



UK and Continental Europe regional growth targets November '19

Brexit hits confidence

Post the March Brexit cliff-hanger, the statistics for this region demonstrate the truth of the observation that risk is global but confidence is local. While UK business leaders' confidence remains resolutely 28 percentage points behind Continental Europe; risk perception is broadly comparable.

It is fatiguing for companies not to be able to plan ahead with any real clarity. The need to plan for multiple scenarios is costly and lack of visibility presents a real risk in terms of companies' stability and resilience.

Dave Brosnan, CEO, CNA Hardy

Increasing tech investment increases cyber exposure

Technology and R&D investments remain the top priority to support growth, sustaining concerns that cyber and technology risk remain the key threats to businesses' successful navigation of the 4th industrial revolution. Against this backdrop, better dialogue around loss prevention and risk engineering should continue to be top of the agenda for risk managers, their brokers and insurers.

UK & Continental Europe Predictions May '19

UK

Confidence and risk

45%

81%

Companies confident in their ability to grow and prosper

Business fundamentals

40%

Investing in tech

18%

Hiring temp staff

Proceeding

Cutting back

Top 2 risks

Economic
43%

Political
36%

Most confident sectors

Fintech
59%

Tech
56%

Continental Europe

73%

73%

Companies operating in a moderate to high risk environment

64%

Investing in Topline growth

11%

Hiring temp staff

Cyber
46%

Regulatory
38%

Financial services
82%

Manufacturing
79%

North American confidence pivots on the economy

Business sentiment across North America is upbeat, with over two-thirds of business leaders expressing confidence in the ability of their businesses to grow and prosper. Although C-suite executives in Canada were marginally less positive than their US counterparts, most likely due to the renegotiation of bi-lateral trade agreements that were under-way as our research was conducted, North America is second only to Continental Europe in terms of confidence.

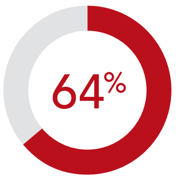
Among the business leaders that we spoke to, economic strength was seen overwhelmingly as the key driver of high levels of business confidence.

Economic fundamentals are sound

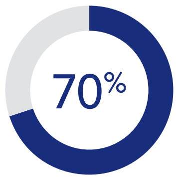
In the US, GDP growth soared to more than 4% in the second quarter of 2018, its highest level since 2014. Respondents here were positive about economic fundamentals, referencing the impact of reduced regulation, tax cuts and fuller employment on rising productivity and their ability to compete. There was a strong sense that the current administration has created a more business-friendly environment and that America First is having a positive impact on business, home and away.

In Canada, the picture was similar, with the economy growing at its fastest pace in a year during the second quarter as exports surged. Respondents cited political and economic stability, high levels of productivity, efficiency and low inflation as particular sources of strength.

North America confidence is high



Nov '18

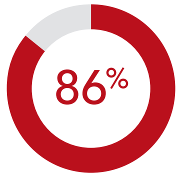


May '19

Companies confident in their ability to grow and prosper

However, despite the positive economic backdrop, economic risk is also perceived as the principal threat to North American businesses, cited by 21% of respondents as the top risk they are facing. Overall, 86% of respondents in North America – more than in any other region – believe that they are operating in a moderate to high risk environment, falling only marginally to 84% in six months' time.

Economic risk rated top concern by 21% of North American executives



Companies operating in a moderate to high risk environment

But can the good times last?

In the US there is concern that economic progress might stall, possibly as a result of higher interest rates, that reductions in regulation and tax cuts might not endure, or that volatility in political decision-making will raise further uncertainty resulting from the imposition of tariffs, leading to supply chain disruption down the line. A surprisingly sizeable minority (39%) were also concerned about higher costs of doing business in Europe and the UK as a result of Brexit.

Canadian respondents likewise emphasised the potential for an economic downturn, triggered by US trade wars, and the related threats this would create in terms of increased tax, regulation, inflation, potential for a market crash, volatility and rising raw material costs – in particular of steel.

The US is currently experiencing the twin phenomena of high growth and high risk. While businesses are bullish on the economy they are contending with an array of threats around geo-politics, trade, cyber security and climate change, to name but a few.

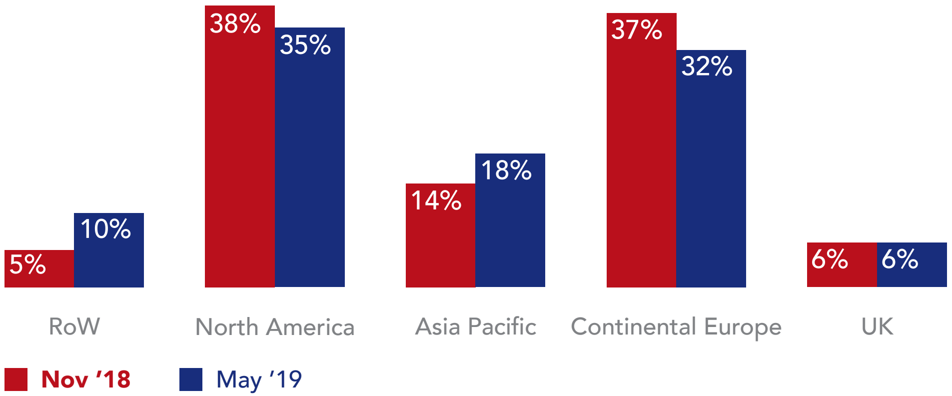
Kathleen Ellis, Senior Vice President, International Solutions, CNA

Overseas opportunities dominate

As North American firms look to exploit the opportunities of business-friendly government policy, buoyant local markets are narrowly still the top priority, viewed by 38% of respondents as having the greatest capacity to drive their business growth now. But look ahead six months and confidence in North America's enhanced ability to compete means expansion in foreign markets is set to take a higher priority than growth at home.

Just under a third of business leaders (32%) say they are looking to Continental Europe for future growth. A smaller, but significant proportion are also targeting Asia, where the balance of those investing grows from 14% to 18% in the next six months. North American's focus on markets in the rest of the world is also set to double in the next six months.

North America's expected global trading partners

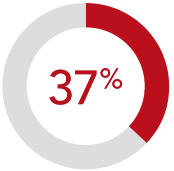


Trade wars and Brexit fears won't slow expansion

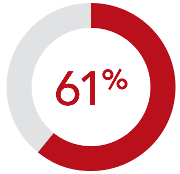
Of course, confidence in the growth opportunities of overseas markets does not come without risk. While the majority were confident they could deal with any fallout from potential trade wars, a sizeable minority, almost four in ten (37%) stated that these risks were hitting their growth plans and were worried by the potential associated risks of customer attrition, rising costs, margin pressure and supply chain disruption.

In the case of Brexit, again, the majority of North American companies – 61% – anticipated little impact.

Brexit and trade wars both issues of minor concern



Businesses that believe trade wars are impacting their business



Businesses that believe Brexit will have little or no impact on their investment and trade with the UK and Europe

The economic fundamentals are good but there are frailties. The unconventional uncertainty in our political environment creates concerns.
Doug Worman, Chief Underwriting Officer, CNA

However, the sizeable minority (37%) that were concerned by trade wars, highlighted the potential for increased complexity as well as some supply chain disruption. Business leaders felt the need to split operations into separate UK and EU entities would be onerous and expensive with negative repercussions for the economy at home.

Once the UK exits the EU it can no longer act as the gateway, forcing companies to deal with two diverging regulatory regimes and multiple languages. This will create a big headache for North American companies doing business with Europe.
Stuart Kenyon, AVP Risk Control, CNA Hardy

Investment focus suggests 4th industrial revolution is taking hold

Alongside new markets, companies are increasingly looking to new technology as a source of growth. Against a backdrop of rising labour costs, more business leaders are looking beyond automation to 'augmentation' for solutions. Advances in robotics and artificial intelligence turbo-charge the insight and capability of highly skilled workers, enabling them to pioneer new solutions and radical business models.

As companies really embrace the 4th industrial revolution, we see 74% of businesses focusing investment on technology and 73% on R&D, a prioritisation of resource and focus which is mirrored in every geographic region. In line with findings globally, many North American businesses are looking to cut back on hiring.

North America's approach to business fundamentals

Businesses' investment priorities now

Is technology creating a people-shaped hole?

However, the opportunities presented by the 4th industrial revolution are not without downside risk. Concerns are growing among our respondents about the risks this creates for the broader economy. Many cited threats to jobs caused by technology and AI.

In the past jobs were about muscles, now they're about brains, but in future they'll be about the heart.
Minouche Shafik, Director at London School of Economics

In response, business leaders may need to consider how they can re-skill the workforce. This may result in tasks that emphasise soft skills such as human empathy and judgement coming more to the fore.

We need to think carefully about the impact on society of taking so many people out of the workforce. Business leaders need to be thinking about the skill sets required for the workforce of the future and putting in place training and development opportunities for staff.
Jennifer Livingstone, Senior Vice President, CNA

Technology gains come with increased cyber threats

While North American companies are investing in technology in a bid to generate efficiencies, seize competitive advantage and access new customers, they are also cognisant of the inherent risks.

With companies increasingly dependent on their digital capabilities and connecting a greater number of devices to the internet, scope for disruption from a cyber attack or data breach is rising. Respondents rank cyber risk as the second biggest they face today, behind economic risk, but they are aware of the full range of cyber threats that they face including ransomware, ID theft, security breaches, data loss, regulatory compliance and cloud security. In contrast to other regions, this awareness has been driven by mandatory breach reporting, which has been in place for some time.

Technology ranks third on the risk radar for North American companies, the highest for any region globally. Technology risk is defined for the purposes of our study as the risk of IT system failure, disruption from new tech-enabled competitors or start-ups.

Technology is often one of the highest cost items on the balance sheet. Executives are acutely conscious of the downside in making the wrong investment decision, the difficulty of keeping pace with technological change and the dangers inherent in reliance on technology to keep the business efficient, competitive and resilient in the face of rising cyber threats. These are becoming increasingly global in nature and adding layers of complexity for businesses with international operations. If a US company holding European customer data is hacked through an Asian office – under which legal jurisdiction will they be prosecuted?

Business leaders hate the red tape

Developments in technology and cyber are also impacting regulatory risk, which sits just outside the top three in fourth place but is still a significant concern for North American executives. In some areas, such as fintech and autonomous vehicles, technology is actually out-pacing regulation, opening up new risks that have yet to be addressed and risking the introduction of new controls down the line.

In our discussions with business leaders, there was a strong sense that regulation had been excessive, cramping enterprise and limiting expansion. While the actions of the current administration have eased the burden substantially, executives can't shake the concern that the regulatory burden could increase.

Cyber and tech risk are key concerns

Companies stating cyber and tech risk are their top concerns today

Perception of regulatory risk increasing

Companies ranking regulatory as the top risk today and expecting it to increase in six months

The high levels of confidence we are seeing in North America are driven by local factors, predominantly the strength of the economy. In contrast, risks are becoming increasingly global – such as trade wars and Brexit – and beyond the immediate control of business leaders.
Nick Creatura, President and CEO, CNA Canada

Supply chain risk set to rise in line with global expansion

Meanwhile, only 6% of North American executives cited supply chain as a top risk today. This is in line with the trend we have seen previously in Europe where so-called boardroom risks, which also include corporate, regulatory and compliance risks, have attracted less attention than they warrant.

However, as North Americans look to develop their businesses internationally in emerging regions of the world, particularly in territories where political instability could impact critical operations, the proportion of business leaders worrying about supply chain rises to 31%.

> Today the world is more interconnected and supply chains are becoming more complex in both emerging and domestic markets. But North American businesses are used to dealing with multiple trading partners and unique, complex regulatory environments. This experience has resulted in an ingrained agility that will enable them to adapt quickly to a changing risk landscape.
>
> Doug Worman, Chief Underwriting Officer, CNA

Supply chain risk becoming a greater concern

Companies ranking supply chain as the top risk today and expecting it to increase in six months

IP-led sectors most confident

The three most confident North American sectors are financial services, life sciences and professional services, with confidence ratings of 79%, 74% and 68% respectively. Confidence is forecast to grow further in the next six months with these sectors retaining their leading positions. Interestingly, sentiment in the technology sector, one of the most cautious now, will surge to put it just behind this group of most confident sectors. It is no coincidence that these are all global industries in which US firms have invested heavily to establish themselves as leaders. They are also sophisticated sectors with foundations rooted in intellectual property and highly-skilled talent.

Meanwhile, more labour-intensive industries such as construction, manufacturing and transportation are among the least confident, both now and in six months' time. Higher interest rates are weighing on sentiment, as is uncertainty around NAFTA and trade with China. The transportation sector has been impacted by the steadily rising oil price over the last 12 months, a trend that is unlikely to reverse in the near future. The outlook for construction, however, is positive with the sector expected to grow almost 5% in 2018, slightly up on 2017. Manufacturing is forecast to increase faster than the general economy, but trade disputes and a strengthening US dollar could have an adverse effect. However, across each of these sectors in the bottom three, confidence is forecast to rise over the next six months: manufacturing and transportation & logistics both by 8%; construction by 6%.

Confidence by sector in North America

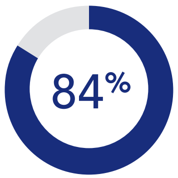
Most confident and most cautious sectors now

Confidence undimmed but caution is the watchword

Looking ahead, sentiment is set to strengthen further with North American leaders' confidence in their businesses' ability to grow and prosper expected to increase by an additional six percentage points to 70% in six months' time, placing North American companies second only to those in Continental Europe with 73%. The proportion believing they operate in a moderate to high risk environment reduces by only two percentage points however.

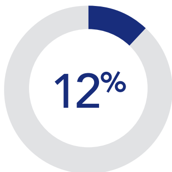
So while North Americans are clearly very comfortable operating amidst high levels of risk, they are not foolhardy. While the overwhelming majority are still investing for the future, those levels of investment are not quite as high in six months' time as they are today, falling on average by twelve percentage points in every area of business, from technology investment to corporate development. It is possible this rising caution may be influenced by the recent mid-term elections in the US, with results likely to increase the scope for political conflict and moderate the pace of change. Political risk rises from fifth place now to second in six months' time.

North America to have the highest risk ranking of any region



Executives who will be operating in a moderate to high risk environment in six months

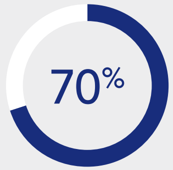
Focus on business fundamentals set to drop



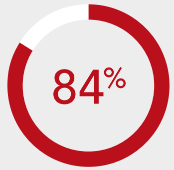
Average drop in investment levels in six months

North America predictions for May '19

Confidence and risk

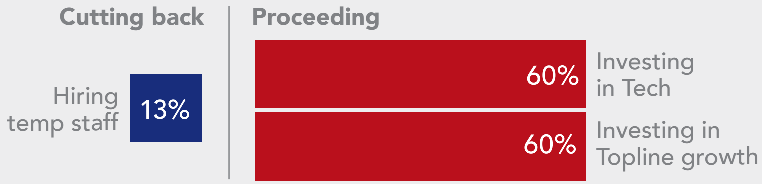


Companies confident in their ability to grow and prosper



Companies operating in a moderate to high risk environment

Business fundamentals



Top 3 risks

Cyber
48%

Political
47%

Economic
44%

Most confident sectors

Financial services
83%

Professional services
76%

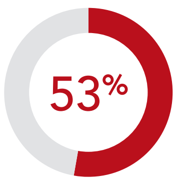
Life science
76%

Asian tiger losing its roar?

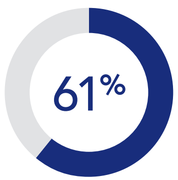
Despite strong growth prospects, businesses in Asia Pacific display the lowest levels of confidence of any region barring the UK. Just over half (53%) feel confident in the ability of their business to grow and prosper and almost a fifth (19%) are actively cautious. As we look ahead the outlook is more positive, rising to 61% expecting to feel confident by May '19.

At first sight this caution is surprising. Historically, the Asia Pacific region has enjoyed buoyant economic conditions and GDP is forecast to rise to 5.6% this year with the region accounting for 60% of global growth, according to the IMF. However, with growth across the region expected to flatline in 2019, some of that local 'feel good' factor is evaporating and short-term risks are starting to weigh heavy on business sentiment.

Executives in Asia Pacific least confident of any region



Nov '18



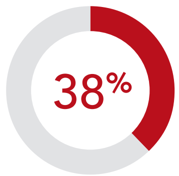
May '19

Companies confident in their ability to grow and prosper

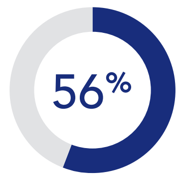
Economics and politics are depressing confidence levels

In November '18, two of business leaders' top three risks are economics and politics. Countries in Asia Pacific are as reliant on China as they have ever been, so it is unsurprising that respondents to our survey frequently cited concerns about the impact of trade war disruptions and protectionism on future growth.

Trade wars and Brexit increasing geo-political tensions



Businesses that believe trade wars are impacting their business



Business that believe Brexit will impact their investment and trade with the UK and Europe

For a threat that was barely present on most risk managers' radars a year ago, political risk tensions are now very much to the fore as the US-China trade war shifts up another gear. Indeed, this is likely to become more of an issue over the coming months.

In early October 2018 the long-awaited announcement by the US government of a further US$200bn of tariffs on imported goods from China instantly quadrupled the amount of tariffs previously implemented. More significant was the pledge that the current 10% tariff level would rise to 25% on 1 January '19 unless China backs down in the escalating trade war.

The effect of the US measures has already started to bite – investment growth in China has slowed to a record low and net exports have been a drag on growth in the first half of the year.

The UK's imminent exit from the EU is also undermining the confidence of the many Asian businesses that trade with the UK and Continental Europe. The UK has traditionally been seen by foreign businesses as the gateway to Europe and companies we spoke to were frustrated by the cost and time needed to navigate the changing situation. Taken together, trade wars and Brexit mean an increase in geo-political tensions that could trigger rising costs and margin pressures, steeper loan exposures and supply chain disruption.

Cyber is moving up the agenda

Cyber risk also looms large on boardroom risk radars, currently in second place between economic and political risks, but projected to take top spot in six months' time, with well over half (56%) expecting it to increase.

Top risks in Asia Pacific

While the cyber insurance market in Asia Pacific is at a relatively early stage of development, with only around 20% of companies insuring against cyber-attacks compared to 66% in the US, leading insurers are seeing policy growth in the region of around 80-95%. This change has come about due to a number of factors and is set to continue.

First, a spate of high-profile cyber incidents across a range of sectors in the region in the last 18 months has served to raise awareness. Most recently, for example, airline Cathay Pacific was hit by a data breach affecting up to 9.4 million passengers. Personal information including passport numbers, identity card numbers, email addresses and credit card details were accessed during the data leak. Not only were customers concerned, but it raised the bar for businesses too. As companies become more global, so they will need to keep a more watchful eye on their international data protection compliance obligations.

Given these developments, it is understandable that cyber risk is moving up the agenda for business executives in the Asia Pacific region.

> Asia Pacific is an ideal environment for cyber criminals to thrive in due to high digital connectivity, combined with a low level of awareness of the importance of cybersecurity, growing cross-border data transfers and the lack of a region-wide regulatory approach which is making compliance increasingly difficult.
>
> David Legassick, Head of Life Science, Technology and Cyber, CNA Hardy

In an attempt to improve the security of personal and business critical data, numerous countries across the region have recently passed new or enhanced data protection regulations.

The list of countries where new regulations now apply includes:

- Hong Kong
- Malaysia
- Singapore
- Taiwan
- Japan
- India
- South Korea
- The Philippines

Others in the region are also in the midst of passing new cyber security laws.

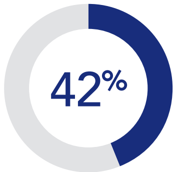
While compliance with this tapestry of new requirements at the regional level is challenging, it is important to note that regulation is also evolving rapidly in other parts of the world. Both Australia and Canada have or are introducing new data protection regulation in 2018 and Middle Eastern countries are also updating privacy laws. In a world where customers are global, the challenge of tracking and managing these multiple and changing commitments should not be under-estimated. Frequently, the task is made all the harder as companies invest more in technology, creating a complex web of integration and related security issues.

Navigating un-charted regulatory waters

Against this backdrop, it is unsurprising that regulatory and compliance risk look set to increase. While only 12% of respondents across all industries ranked it as their top risk now, fully 42% of business leaders think the risk will be higher in six months' time.

Regulatory and compliance risk set to rise

Companies ranking regulatory and compliance risk as their top concern in Nov '18



Companies who believe this risk will increase by May '19

Financial services, which alongside technology is the most important local industry, is particularly strongly impacted by regulatory change. Within financial services, regulatory and compliance risk is the top concern. Since the global financial crisis of 2008, there has been a growing awareness of the need for stronger central regulation in many Asian countries and regulators across the region have spent the last decade trying to replicate the solid regulatory foundations of the EU and the US, especially for more complex financial products.

This has led to the evolution of a patchwork of different frameworks, with a tendency to 'add on' local variances to international standards such as BASEL III and Solvency II, making them more complex. The result has been a slowly building mountain of regulation, which has become very demanding for compliance teams to manage.

There is increasing anxiety in the financial industry in Asia concerning the levels of regulation at not just domestic, but at regional and international levels. These layers of increasing regulation create significant legal, regulatory and reputational risks for organisations. The continuing enthusiasm of the regulators to pursue wrongdoing...in the market and the ingenuity which they are prepared to employ to achieve satisfactory enforcement outcomes, remains a high risk point for institutions.

Alan Ewins, Special Counsel Asia and Matt Bower
China and Hong Kong Partner, Allen & Overy

Boardroom risk running under the radar

Our previous research has found that European business leaders have not been giving sufficient attention to three key boardroom risks – corporate, regulatory and supply chain – and this report indicates a similar finding among executives in Asia Pacific.

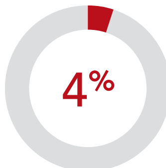
Corporate governance standards in much of Asia remain lower than in more developed economies, according to the Asia Corporate Governance Association, so it comes as little surprise that corporate risk is bottom of the list of concerns for Asian businesses. Corporate risk is defined in our research as the risk of fraud, corruption or poor governance. While regulatory risk does not sit in the bottom three concerns of executives, it is in fourth place with 12%.

Interestingly, supply chain risk is not a major concern either, ranking in the bottom three both now and in six months' time. One could argue that as a sizeable proportion of Asia Pacific companies are focused on growth in domestic and regional markets, so it is possible that supply chains are relatively short and not at risk of major disruption. But this would be to ignore the rapid rise in climate risk and expensive mitigation that many executives also complained of in our discussions.

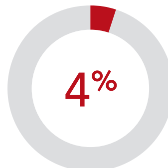
We have noted in previous surveys that boardrooms need to 'mind the risk gap'. Failure to focus on corporate and supply chain risk and the consequent threat to business continuity risks inviting significant brand and value damage down the line.

Bottom risks in Asia Pacific

Supply chain



Corporate risk



Terrorism

Asia Pacific companies' lowest-ranked risks now

Nimble is not the new normal

Against this backdrop of rising risk, it is small wonder that a significant majority of businesses – 82% – think that they are operating in a moderate to high risk environment. The fact that only just over half (53%) remain reasonably confident in the face of economic and political shocks suggests that unlike their European and North American counterparts, Asian business leaders struggle to take such risks in their stride. Here, unlike in western markets, maybe nimble is not the new normal.

Weight of risk is heavy on business leaders

Companies operating in a moderate to high risk environment

If China sneezes, the rest of Asia Pacific catches a cold – business confidence in nearly all the region's markets hinges on developments in the world's second largest economy. The on-going trade war with the US may cause an economic slowdown in China, which may result in increasing caution amongst company executives who will need to adapt their business model accordingly.
Rob Hands, CEO, CNA Hardy Asia

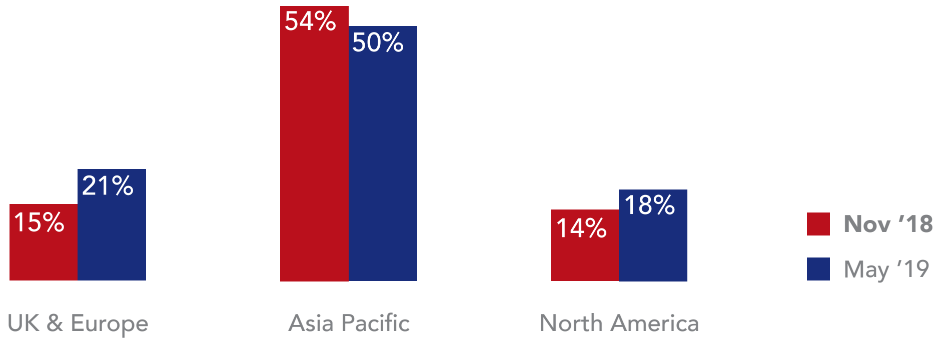
Lack of confidence impacts investment

In line with findings across other regions, Asian Pacific companies favour growth in their domestic markets. In November '18, more than half (54%) cited Asia as the region with the greatest capacity to drive their business. Looking ahead however, despite China's much vaunted 'Belt and Road' programme, the proportion prioritising domestic investment is set to decrease to just 50%.

This luke-warm interest among Asian businesses in their own market is replicated among foreign businesses also. The pivot to Asia which we saw in November '17, with all foreign regions stating they would double investment in Asia has not been borne out by events. In North America, executives think that their focus on Asia Pacific will rise from 14% now to 18% in six months' time, among European businesses interest increases from 15% to 21%, modest but not exciting.

Our statistics demonstrate that though Asia was the market of choice one year ago, today it is Europe that is commanding most interest.

Interest in Asia is muted



Companies focusing on Asia Pacific now and in six months' time

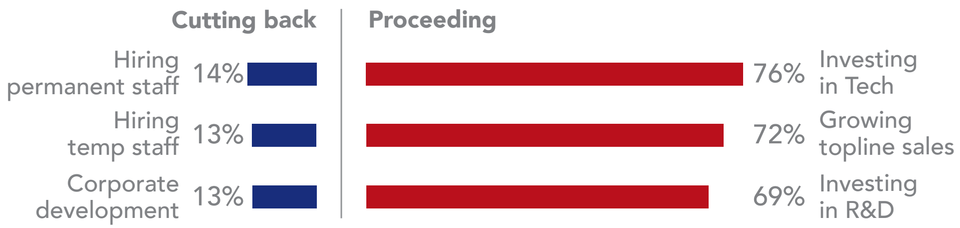
Can technology change the game?

In line with the global trend, investment – in both technology and R&D – is a key area of focus in order to build topline sales. This picture remains stable as we look ahead six months.

Indeed, Asia Pacific's strength in technology, which has long been an investment priority for governments in Singapore and Hong Kong, is bearing fruit both in terms of how local businesses go to market but also in terms of attracting foreign investment. The recent announcement by Dyson that it will site its new electric car factory in Singapore is a vote of confidence in the reservoir of technology businesses and skills that now reside in the region.

Also in line with the trend, companies are reducing headcount. Across businesses of all sizes, 14% are cutting back on hiring of permanent staff and 13% on temporary staff. This reflects the global trend towards automation and AI. It also reflects regional economy reality. Labour costs are rising across the region. While wages have historically been low by global standards, as they increase, companies are shifting their focus to investments in technology in order to maintain competitive advantage. While focus on technology could be the game-changer that Asian businesses need, it is not without risk. Although it can help boost efficiency and flexibility, it also increases companies' exposure to the destructive impact of cyber.

Technology not people primary route to growth



Companies proceeding with or cutting back on business fundamentals now

Fintech and life science lead the charge

Government focus on technology and on the development of Singapore in particular as a key financial services hub means that the Asia Pacific story is not without its high points.

Fintech businesses are the most buoyant right now with 69% expressing confidence. This optimism is only set to increase with that number rising to 85% in six months' time. Life sciences is the next most confident sector with 59%, buoyed by a steady influx of investment into research and development as a result of the ageing population. Professional services is also on 59% with sentiment likely bolstered by the expectation that the increasing focus on cyber risk will lead to new business opportunities.

Which sectors are most optimistic?

Companies confident in their ability to grow and prosper now

Manufacturing and healthcare are two of the least confident sectors both now and looking forward six months. Disruption to export markets caused by Brexit and US-China tariff raising is impacting manufacturers' confidence, while hospitals and health care providers remain under pressure due to rising costs. Confidence is also low in the transportation & logistics sector, weighed down by the threat of supply chain disruption due to trade wars. However, in six months' time confidence in the sector is forecast to recover, suggesting this challenge is perceived as temporary.

Return of the roar not imminent

Looking ahead, the mood recovers somewhat, with 61% of business leaders expecting to be confident. However, global risks will continue to weigh heavy – in particular the threat of cyber breaches and an economic downturn primarily due to international factors including US-China trade wars and Brexit.

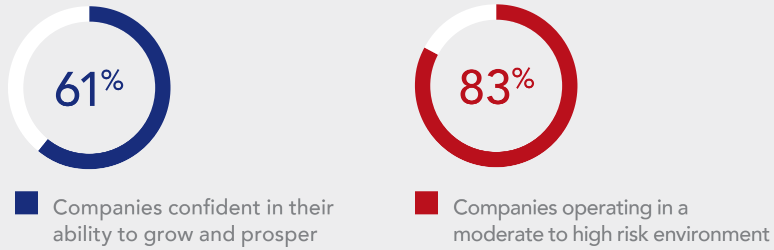
Risks most likely to increase in May '19

Asia Pacific leaders stating key risks will increase

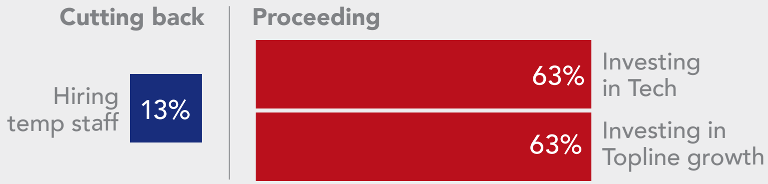
Can technology turn the tide – either in terms of progress from the tech-enabled sectors, or via the investments being made to boost productivity, flexibility and efficiency by businesses across the board? In part this will depend on the evolution of technology risk – a phenomenon which though present in Asia, is less prominent than in other markets.

Asia Pacific predictions for May '19

Confidence and risk



Business fundamentals



Top 3 risks

Cyber
56%

Economic
52%

Political
44%

Most confident sectors

Fintech
85%

Financial services
72%

Transport & logistics
67%

May '19

Methodology

Opinion Matters, an independent research agency, conducted quantitative research on behalf of CNA Hardy. This research was undertaken during July and September '18, via an online survey of 1,500 business leaders of multinational firms with operations in Europe.

Company size ranged from businesses with turnover of US$6.5m up to more than US$1.3bn. The regional sample split was:

- 450 firms based in the UK
- 250 firms based in France and Germany
- 450 firms based in the USA
- 100 firms based in Canada
- 250 firms based in Singapore, South Korea and Australia.

The survey respondents were evenly split from across the following industry sectors:

- Manufacturing
- Construction
- Transportation and logistics
- Financial services
- Professional services
- Tech
- Fintech
- Healthcare (private)
- Life science

In addition, Luther Pendragon, a London based communications agency, undertook telephone interviews with representatives across the target business sectors and CNA Hardy representatives based in the UK, North America, Continental Europe, and Asia.

Luther Pendragon worked with CNA Hardy to analyse the data, write and prepare the November '18 Global Risk and Confidence survey report.

CNA / HARDY 20 Fenchurch Street London EC3M 3BY United Kingdom
Tel +44 (0)20 7743 6800 Fax +44 (0)20 7743 6801

w: cnahardy.com/pulse
e: pulse@cnahardy.com